

# The Importance of Independent Advice\*



Investors are better off when they receive independent advice. But the concepts of independent advice and independent advisors are very confusing to them. For example, most investors don't know the importance of independence or how to measure the objectivity of the advice or sales recommendations they receive from their advisors. Independence is further obscured by companies and advisors who have something to hide. They don't want investors to know their advice is tainted by self interests that increase company profits and advisor incomes. It's safe to say they are very skilled at hiding information they don't want investors to have.

## What is Independent Advice?

Independence is a critical characteristic that impacts the quality of advice investors receive from financial professionals. Independent advice has four primary characteristics:

- Advice is always in the investors' best interests
- Advice is free of any potential conflicts of interest that damage investors
- Advisors who provide independent advice also practice full disclosure
- Advisors are compensated with fees for their knowledge and services

### Investors' Best Interests

Companies, executives, and advisors want to control investor assets so they can achieve their goals for revenues, profits, and incomes. Investors are dependent on the same assets to achieve their goals for a comfortable retirement and financial security late in life. The critical question is: Whose financial interests come first? The answer to this question will vary by company and advisor, and it will be based on their ethics and willingness to tell investors the truth.

### The willingness to put investor interests first eliminates most potential conflicts of interest.

### Conflicts of Interest

Let's assume that a fictitious company we'll call Acme Financial produces products that make the company a lot of money — for example, mutual funds, annuities, and life insurance. The products deliver below-average returns for above-average

expenses. Acme sales representatives are required to market the products, even though investors would be better off with unrestricted choices. This major conflict of interest impacts hundreds of brand-name financial services companies that produce their own products and services.

Other conflicts of interest are more subtle, but all of them damage the financial interests of investors. For example, advisors who are new to the industry describe themselves as investment experts because it helps them sell products. They fail to disclose they are new because investors might not buy what they are selling. They put their need to sell products ahead of the investors' need to buy from professionals who have knowledge that will help them achieve their financial goals.

### Investors should select only advisors who are willing to document that they have no potential conflicts of interest.

### Full Disclosure - Objective

Advisors who provide independent advice are willing to practice full disclosure because they have nothing to hide. They realize consumers need objective information when they select advisors. They also know written information is more reliable than information that is communicated verbally in advisor sales pitches. Investors benefit because they can use the information to screen out weak, conflicted advisors and select competent, ethical, independent professionals. These advisors provide documentation that includes:

- A professional profile that documents their credentials, ethics, business practices, and services

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- A disclosure statement that describes potential conflicts of interest
- A code of ethics that describes their principled treatment of investors

**The high-quality, independent advisors can afford to practice full disclosure. Lower-quality advisors don't want to disclose their weaknesses and conflicts of interest.**

### Advisor Compensation

Commission compensation creates additional conflicts of interests that may damage the independence of the advice investors receive from their advisors. Some of the conflicts that surround this method of compensation include:

- The sources of commission payments and their interests
  - Third parties pay commissions to advisors who sell their investment and insurance products (mutual fund, annuity, and life insurance companies)
  - Brokers/dealers charge commissions when investors buy or sell securities

- Advisors being paid commissions to sell products
- Advisors not being compensated to provide ongoing advice or services
- Advisors' licensing permitting them to sell products and receive commissions, but not give advice
- Advisors' compensation not being impacted by the achievement of investor goals

Even though third parties pay commissions to advisors for selling their products, this form of compensation is ultimately paid by investors. That's because companies raise the fees they charge investors, or they create additional fees to cover their commission costs. For example, mutual funds charge 12b-1 fees to investors to offset their marketing expenses.

**Independent professionals are paid directly by investors because they charge fees for their knowledge and services. Investors know what they are paying and what they are receiving for those payments. There are no third-party interests when investors pay directly.**

## The Independent Advisor

There are several characteristics that describe high-quality professionals who provide independent advice:

1. They are Registered Investment Advisors (RIAs) or Investment Advisor Representatives (IARs).
2. They are acknowledged fiduciaries, which means they are held to the highest ethical standards in the financial services industry.
3. They practice full written disclosure for information that impacts the achievement of investor goals.
4. They are compensated with fees, like other professionals (CPAs, attorneys).
5. They provide sophisticated wealth accumulation and preservation services that deliver results in complex financial markets.

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### Contact Us

When you understand and look for independent advice, you greatly increase the likelihood that you will receive professional advice which is suited to your needs. At Wipfli, we believe providing such independent advice is the only way to serve clients. If you would like to learn more or discuss the ideas presented in this article in more detail, please contact Ed Drake at 608.270.2917 or [edrake@wipfli.com](mailto:edrake@wipfli.com).



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