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Broker? Adviser? And What's the Difference?

By [PAUL SULLIVAN](#)

THE Great Recession has intensified a long-running debate: who is better able to look out for your money, a broker or an independent adviser?

Now that the shock of last year's losses has worn off, many investors are reconsidering what their financial professionals did — or failed to do — for them. At the same time, many brokers are trying to refocus themselves as advisers. Fed by the discontented, the debate has taken on a new urgency.

At the center of the discussion are business practices and regulatory guidelines that are rarely understood by the client and often blurred in practice. Brokers are governed by the "suitability rule," which requires them to have "reasonable grounds for believing that the recommendation is suitable," according to the Financial Industry Regulatory Authority. Registered financial advisers are supposed to adhere to a higher standard — "fiduciary responsibility," an ethical and legal requirement that the investor's best interest comes first, not the adviser's own financial gain.

The conventional view of the two camps goes like this: the brokers at the big firms have access to every product imaginable, but may be pressured to sell you one of them and earn more if they do. They are not obligated to get you the best price for what they advise you to buy or sell — or even to be free of conflicts.

The independent investment advisers proudly promote their independence and lack of conflicts. If their clients feel that the fiduciary responsibility was not met, they have legal recourse through the state courts. Brokers counter that the advisers lack the infrastructure and support of a big firm that would protect clients in the event of irregularities in their accounts or with their advisers.

In practice, though, the two standards seem to confuse investors. Congress is now considering a provision that could alleviate some of this confusion by requiring brokers to act in their clients' best interest. "I don't know if more than 10 to 20 percent of my clients understand the difference," said Susan Fulton, president of FBB Capital Partners, a fee-only adviser outside Washington. "The investment advisory and brokerage businesses don't make it clear."

Adding to the confusion is that the difference between a broker and an adviser is not always black and white. Consider Shawn Rubin and Kelly Campbell, money managers at two very different firms.

Mr. Rubin, a managing director in the wealth management group at [Morgan Stanley Smith Barney](#) in New York, has thick binders lining one wall of his office. Each contains information on a client — [mortgages](#), [life insurance](#), property and casualty policies, wills, tax returns, charitable giving. The last section contains investment breakdowns, the only part of the binder he is paid to oversee, as a broker.

“Ninety percent of my time is spent on things I’m not compensated on,” he said, sitting in a modest office that gives little indication that he manages more than \$800 million for 50 wealthy clients. “I want to be a trusted adviser, the chief financial officer for my clients. You end up doing a lot more than just financial stuff.”

Mr. Campbell, in contrast, is an independent adviser in Fairfax, Va. His business model is mixed: 60 to 70 percent of it is fee-based, he estimated, and the rest comes from commissions for selling products. This would seem to violate the standard of fiduciary responsibility, but the way Mr. Campbell sees it, he has one foot in each camp, and there is no conflict.

“Having the ability to do both is extremely important,” he said. “I’ve been very clear about this. I say this is the piece on which we’ll be charging you a fee, and this is the part where we’ll charge you a commission.”

So Mr. Rubin, the broker, acts like the head of the family office; Mr. Campbell, the fee-based adviser, occasionally sells commission-based products. They render the traditional definitions obsolete.

Most registered investment advisers started at brokerage firms, and many left, they say, because they grew tired of the conflicts of interest. This trend is accelerating, says Schwab Adviser Services, which acts as a custodian for \$590 billion in assets managed by 6,000 advisers. It said 2009 was its best year for signing up new advisers, with 172 new teams and \$13 billion in assets.

The big brokerage firms, meanwhile, scoff. “I’ve read that advisers are leaving here at record levels, but in the fourth quarter we had historically low attrition levels among our financial advisers,” said [Sallie L. Krawcheck](#), president of [Bank of America](#) Global Wealth and Investment Management. She reeled off the advantages to being with a big firm, like continuing education for brokers and products and [loans](#) offered by other parts of the firm.

“The business has gone through brokerage to investment management to wealth

management,” she said. “Now clients want us to take it more broadly than that.”

What may matter more than the array of services is **the mind-set of the adviser**. When a broker tells a client to buy or sell something, the suitability rule does not mean the broker has to be free of conflicts of interest. After all, **the broker’s salary is ultimately paid by the brokerage firm, which has various products to sell**. But brokerage firms say they are trying to eradicate that appearance of conflict.

“A real important piece is that compensation never be slanted to selling our own product,” said Patrick O’Connell, vice president at [Ameriprise Financial](#), a brokerage firm. “We’re in the process of completing an acquisition of Columbia Management. If an adviser was paid more to use a Columbia fund and not a Fidelity fund, which is also on our platform, that would be problematic.”

But others still hold to the traditional distinctions. “There are people who are very successful brokers who do a great job every day,” said Kemp Stickney, chief fiduciary officer at [Wilmington Trust](#), a century-old fee-based trust company. “**But if you think about it from an investment point of view, the way a lot of brokerages work is they sell you a bond out of their inventory**. Because we’re not an investment banking firm, we have to ask for bids from four, five, six different firms before we buy a bond for our clients.” (Ms. Krawcheck says the array of products that Bank of America keeps in inventory is a benefit to clients.)

Advisers like Mark Matson, chief executive of Matson Money, said brokerage firms should get out of the advisory business altogether. “The problem is they hold themselves out as offering advice and value-added services,” he said. “They should just tell clients, ‘**I work for a brokerage and I’m going to suggest some things, and you have to make the decision if they’re right for you.**’”

This is where the fiduciary standard gets invoked. Rooted in trust law, that standard means that an adviser has to act impartially and solely for the benefit of the client, avoiding conflicts of interest and self-dealing.

“It’s never about us; it’s about our clients and their interests,” said R. Hugh Magill, chief fiduciary officer at [Northern Trust](#). “They entrust their assets to us for management. But the more subtle distinction is they entrust their family to our care.”

Asked how an adviser who leaves a brokerage can become a fiduciary, Mr. Magill said: “It takes time to learn these things. Are they going to pick up ‘Fiduciary Responsibilities for Dummies?’ You learn it by example.”

During the depths of the financial crisis last year, Mr. Matson, a former broker who speaks of fiduciary responsibility with the zeal of the converted, took that responsibility

to an extreme. He resigned from about 250 accounts because he felt the clients were doing things not in their best interests — namely trying to time the market.

“This is what the average adviser can’t do,” said Mr. Matson, who manages \$2.4 billion. “A client has a \$1 million account that has gone down 30 percent, and he says, ‘I feel uncertain and want to be in cash.’ The adviser knows you can’t time the market, but he says if I don’t do what he says, I’m going to lose this account and the \$10,000 fee. That adviser has a wife, family and expenses. He can’t say no.”

But many investors still select their advisers — whether at a brokerage firm or on their own — based on the advisers’ skill and personality, according to a new study by the Oechsli Institute, a research group.

“The most important factors in selecting the adviser is the reputation of the individual and the impression that person makes in terms of professionalism and competence,” said Matt Oechsli, the chief executive. “The trust you have for the firm goes up if you trust the adviser; if you don’t trust your adviser you don’t trust the firm. This is the first time this has been inverted.”

The Oechsli report, “The New World Adviser,” found that clients with \$250,000 to \$10 million in investments were more worried about clear, timely communication and quick problem resolution than about investment performance. A majority of respondents on the lower end of the investment range said they did not believe their adviser was doing a great job, it found, and were looking for a better option.

That may be heartening to the registered investment adviser who has left a big firm to go solo. But what it really means is that the onus is on the individual adviser. Someone like Mr. Rubin, whose platform was switched from [Citigroup](#) to Morgan Stanley when Smith Barney became a joint venture last year, understands the importance of service over brand.

“Our goal is staying ahead of what the client needs,” Mr. Rubin said. “When they write check 180 and we know they have 200 checks, we send them another book. That service makes them more inclined to put large amounts of money here on which we generate our compensation.”

Of course, some investors do not have enough money to attract the interest of a top adviser. It should not come as a surprise that the level of personalized service gets ratcheted up with wealth level. Mr. Rubin’s clients have a minimum of \$5 million with him, while Mr. Campbell’s clients have \$1.5 million to \$2 million. Most registered investment advisers require a minimum investment of \$1 million, though some will accept clients with \$500,000.