The Right Stuff

All advisers are sure to be in the competitive line of fire, but many have exactly what it takes to keep from falling

Mary Rowland

FIVE OR SIX YEARS AGO, A financial adviser told me that he'd seen the results of one of those surveys in which consumers rank the trustworthiness of various professions: doctors, lawyers, gardeners, accountants. Planners didn't make the list, but insurance agents and stockbrokers were near the bottom, where you'd find used-car salesmen. Like other advisers at that time, this one wanted to make sure he wasn't lumped in with that crowd.

He had good reason to be concerned. In those days, planners were seen as cut from the same cloth as agents and brokers. The elite planners I talked with at that time, as I was working on *Best Practices for Financial Advisors* (Bloomberg Press), were marking their territory, feeling their way along, creating a new profession.

That was then; this is now. Over the past five years, financial advisers have garnered such cachet that everybody wants to be one. It doesn't hurt that the job has been so lucrative, either. Instead of defending their professionalism, advisers today are defending their turf. Look at the agendas for the big planning conferences: survival strategies get a lot of play.

One of the more controversial spokespeople on the subject of how best to ward marauders off your territory is Mark Hurley, chief executive officer of Undiscovered Managers in Dallas, who appeared on the *Wealth Manager* panel at the Impact 2001 Schwab Institutional Conference in Seattle in October. Lots of advisers love to hate Hurley for his dire predictions. He believes planners have three choices: they can get big, find a niche, or get eaten. I've been critical of Hurley's forecast. But when I checked in with him recently, I discovered that we actually agree on some major points regarding how to survive. We simply aren't talking about the same financial advisers.

Hurley did advisers a big favor by giving them a wake-up call. That was his intention, of course. He acquired plenty of marketing savvy from his stints at Goldman Sachs and Merrill Lynch. When he set up the Undiscovered Managers funds, he counted on independent financial advisers to be his distribution arm. The funds are too sophisticated and the minimums too high to sell directly to consumers. If independent advisers go the way of the dinosaur, he'll have to roll up his rug.

I first met Hurley in 1999 in Dallas at a great little workshop on the future of the financial-advisory business, which was sponsored by advisers Dave Diesslin, principal of Diesslin & Associates in Fort Worth, and Richie Lee, president of Lee Financial Corp. in Dallas. The idea behind the workshop was to do scenario planning on the industry's future. After coming up with some broad possibilities, we split up into small groups. My group of four, which included Hurley, was assigned to look at competition. Hurley told us his tsunami story, which I've rehashed a couple of times since: It was a clear and sunny day in Galveston in the summer of 1900 when a hurricane warning was issued. Most Texans ignored it. The tidal wave that resulted wiped out 6,000 people, and the survivors were forced to burn the bodies on the beach. That, Hurley explained, was what was in store for financial advisers. "Everything looks quiet

Illustrations by Jeffrey Fisher

now," he said. "But it's going to hit out of nowhere and planners are going to be swamped."

Hurley stands by his prediction of vicious competition from the big wirehouses, insurance companies, and accounting firms with lower fees that come from economies of scale and more services—and then poof! When the winds settle, 40 to 50 big advisory firms will emerge with assets of at least $20 billion apiece. These firms, Hurley says, will operate as multiclient family offices that provide at least seven services for clients: financial planning, tax planning, tax preparation, investment management, insurance, estate work, and charitable giving—all for less than 1 percent in fees. And the rest of the planners? Washed away.

When I checked in with Hurley this fall, he pointed out that I'd mangled his story because I'd put his official 1999 report—*The Future of the Financial Advisory Business and the Delivery of Advice to the Semi-Affluent Investor*—together with his unofficial tsunami anecdote at the Dallas workshop. "For the record, we never said that 6,000 planners would be wiped out," Hurley says. "They just won't make any money, as the changes we have predicted will slash their margins. Many who currently earn $100,000 to $125,000 per year may find themselves earning $50,000 and working a lot harder for it. As entertaining as the business may be at $125,000 per year, if compensation is cut to $50,000, a lot of these planners may feel as if they have been wiped out."

That may be true—for some. But I don't see insurance agents or wirehouse brokers, no matter how much training they've been given, as real competition for the advisers I know. Advisers are fiduciaries, who put the client's needs first. That's not the wirehouse approach. Such businesses have a different mind-set.

Still, I don't see financial planning in the future as the Power Rangers kind of business that we have now, with stockbrokers morphing into planners morphing into fee-only advisers who then build a business they can sell. Instead, I believe different financial-planning models will emerge from the floodwaters. We're already seeing that.

But I'm getting ahead of myself. Let's hear what Hurley has to say. He stands behind the 1999 report, reminding me that he projected changes across the industry occurring over seven to 10 years and that the paper has been out for only two. "The changes are on the way. Many of them are already in evidence," he says, citing the $100,000 in stock Merrill Lynch is paying its trainees to get CFP certification and new ad campaigns by wirehouses and insurance companies claiming that their people can do the job as well as financial advisers. Of course, anyone can make that claim. It seems to me that the stock market's fall may have cemented planners' relationships, that clients with diversified portfolios would be more loyal to their advisers after watching their footloose friends lose half their money in tech stocks.

Hurley says the opposite is true. The correction in the equity markets will serve as a catalyst for many more changes, he says, because the advisory business grew up in a time of inflated equity returns. When clients earned higher investment returns, advisers could charge them more. "Advisers—unlike any similar professionals—have been able to charge a percentage of assets instead of a flat fee and earn more money for larger clients although the adviser [brings] no incremental value added to the larger client," he says.

Hurley's right about that. Changes in the fee structure are coming. With investment returns moving into line with the historical average of 6 percent to 7 percent per year, "much of what we have written about will likely happen even sooner," he says. One of the first things that will go will be this percentage fee structure; advisers will shift to retainer fees or flat fees, he says. I agree with this point, too. Many advisers, such as Keats, Connelly and Associates in Phoenix, have already shifted to retainers. Four years after the switch, cofounder Bob Keats says it has improved their business, taking the guesswork out of budgeting. I would certainly rather pay a professional a set fee than a percent of assets, and I'll bet a lot of other people would, too.

And planners, Hurley says, will have to add more value

I don’t see insurance agents or wirehouse brokers, no matter how much training they’ve been given, as real competition for the advisers I know. Advisers put the client’s needs first

than simply a financial plan and mutual fund selection. Morningstar’s plan to offer money-management services for as little as 15 basis points “makes it official,” Hurley says. “Asset management—defined as selecting a portfolio of mutual funds—is a commodity.” Again, I agree. I’ve been talking about that for years now: asset management is the least important thing advisers do and the one thing that clients can do on their own if they’re motivated. A client could just buy the Vanguard Star Fund, a diversified portfolio of other Vanguard stock and bond funds. I’ll bet it performs as well as most customized mutual fund portfolios that are well diversified. The fee is a lot lower than 1 percent, too. You won’t find me wagering on any contest between a planner and a wirehouse broker if we were awarding points only for investment returns. Insurance agents are another matter.

So if Hurley’s report was focused on the future of those financial advisers who charge a 1 percent fee to put together a portfolio of mutual funds, he wins. They’re beached. But that doesn’t describe the advisers I know, planners like Katharine McGee, a financial adviser in Davenport, Iowa, who persuaded a freshly divorced 50-year-old client to forget about money and move to Santa Fe, N.M., to see if she could make it as an artist; or Cynthia Meyers, an adviser in Sacramento with her own firm, who accompanied her 65-year-old client to an audition to help her conquer stage fright and get a singing career off the ground; or Charlie Haines, president of Charles D. Haines LLC, in Birmingham, Ala., who hired a security firm to teach clients how to defend themselves against kidnapping; or Bob Willard, principal of Willard & Co. in Colorado Springs, who is willing to take over the management of the limited partnership in which a client had invested; or Tim Kochis, president of Kochis Fitz Tracy Fitzhugh & Gott in San Francisco, who probably knows more about stock options than the companies that offer them to his clients; or Jim Budros, principal of Budros & Ruhlin in Columbus, Ohio, a highbrow foodie who has done restaurant reviews on public radio and might cook a meal for a newly widowed client while he listens to her talk about grief; or Myra Salzer, founder of the Wealth Conservancy in Boulder, Colo., who holds four-day workshops to show clients how to sort through the emotional baggage that comes from inheriting great wealth. We’re not talking about stockbrokers here, folks.

I fear I’m beginning to sound like Bob Veres. He publishes a newsletter for advisers called *Inside Information* and believes in the altruism of financial planners in a way I haven’t been able to believe in people since the 1960s. I think it’s wonderful that Veres has been able to hang on to his idealism, but I’m a skeptical and cynical journalist who once saw advisers as salespeople—as threats to the consumers I typically write for. But in my own small way, I’ve become a convert to financial planning as I know it. The advisers I know are not salespeople. They aren’t stockbrokers or insurance agents, and they don’t push their own company’s products or work for the Paris insurance giant, Axa. They’re businesspeople, of course. Planning isn’t a hobby for them. But they are each creating a practice that’s a tapestry, weaving together their own strengths with their clients’ needs. Certain models are emerging, like Charlie Haines’s family office or Keats, Connelly and Associates’ dual-citizen niche. But each of their practices is unique.

Hurley concludes that things look bleak for planners. “We are already hearing of a rising level of fear from many advisers as their margins are being compressed,” he says. “This will only accelerate.” There are advisers on the margin—yes, those who’ve been eating the frosting instead of baking the cake. But they’re not the planners I know. Planning will look different a decade from now, it’s true. But I suspect that when the consumer rankings for 2012 come in, where advisers land on the list will depend a lot on the size of the company they keep.

Mary Rowland is the author of Best Practices for Financial Advisors *(Bloomberg Press). She speaks regularly to financial advisers on issues of practice management.*