Is your financial adviser any good?

I find that many people use advisers who are earning more from the client's portfolio than the client. Sometimes it's from financial agents or firms not using their fiduciary responsibility which requires them to put the client's interest above their own. Or sometimes it's because they are getting advice from a friend, insurance sales agent, tax accountant, or overhear a braggart at a barber shop or beauty parlor.

I know people who have worked with an adviser for a number of years, developed a personal relation, and feel they would be embarrassed to change advisers. I kid these people by saying, "I'll bet that they send you birthday cards too." The response is almost always, "Of course." People who continue to get bad help are sacrificing their retirement future and are unwilling to take the little effort required to compare their actual investment performance with the general market performance. For example, if you didn't churn your investments and if your total portfolio growth last year was 4% and similar securities reported 7% returns, you have lost 3% to fees and costs. In my view, 1.5% difference is too much. I keep my own investment costs below 0.2% of my portfolio and only rebalance, never churn.

Churning is another reason for poor performance. Perhaps fund Y did better than your fund X last year, so your switch to Y. Then you read or hear or a recommendation that fund Z is supposed to do very well, so you switch from Y to Z. Morningstar has reported that actual investors do much worse than reported returns because they chase the market, selling when stocks are low and buying when they are high. The average loss from churning and fees is 3%, but can be much higher.

Or perhaps your adviser wants to enhance his take from commissions. I've seen cases where school teachers were advised to buy variable annuities within their 403(b)s. The variable annuities provide another source of revenue for the administrators at the often large expense of the teachers. The 403(b) is already a tax deferred investment. There's no need to put a tax deferred investment within another tax deferred investment. Or perhaps your advisor recommends changing from one annuity to another. This can be very costly.

I've seen a home owner's association turn their portfolio over to an adviser who invested the money in funds with high front-end loads, back-end loads, redemption penalties, 12(b)1 kickbacks every year, etc. Not only that, but the funds themselves all had high internal costs. I know that same adviser has many private clients who are likely subject to the same treatment.

It's possible that the new laws requiring funds to disclose their costs may help expose part of your costs, but don't put it past the financial industry to hide their costs. For example, it's virtually impossible to find the difference between the fund manager's buy and sell costs when they trade securities within the fund—and trading costs can be a big source of income for a financial firm. Financial firms take in hundreds of billions each year from their clients. That's why their executives get such large compensation.

So, how do I know how much I am losing to fees and costs?

It's really simple. There is a free return calculator on www.analyzenow.com. Put in your beginning and ending balances for the year as well as any deposits or withdrawals you made during the year. Bingo! Out pops your actual before-tax return. This is a before-tax return, not an after-tax return, even if your

withdrawals were to pay taxes. One Wall Street Journalist who recommended the program got that wrong when she said you would get an after-tax return if you entered withdrawals made to pay taxes.

It's also the total return, not the return that just comes from growth as you would get comparing a stock price at the end of the year compared to the beginning of the year. The growth of stock prices does not include the additions that dividends provide. Total return includes dividends and interest. So, if you didn't reinvest dividends or interest, you would enter them as withdrawals in the calculator.

I like to simply enter the total of my investments, not look at each fund individually, but you can do that too it you want using the calculator. The problem is that your financial firm may not include the fees that it charges in the report of the individual security. For example, an advisor may charge 1% to manage your portfolio. He can show the individual performance and then subtract the 1% from the total at some point during the year. By capturing the entire portfolio performance from beginning to end of the year, you can find the total costs.

This same calculator offers something else. You can compare your before-tax total return to the market results for various securities in financial publications or the Web. I personally keep this very simple, and you may want to do the same. For example, if your portfolio had 50% stocks, 40% bonds and 10% money markets, you might look up how comparable indexes did last year. I compare my results using the S&P 500 index for stocks, an AAA corporate bond index for taxable bonds, a broad index for municipal bonds and short term treasuries for money markets. Or you can use the performance of comparable funds from known low-cost providers such as Vanguard and Fidelity.

Then enter market results along with the percentage allocation in your portfolio in this part of the return calculator. Bingo! Now you have the before-tax total return of a comparable market portfolio. If this is much higher than your own return from the first part of the calculator, you should find out why. It may be from high costs of your adviser. It could be from investment churning.

If there is more than 1.5% difference between your actual return (from the first part of the calculator) and the market return for a similar allocation of market indexes (from the second part of the calculator), it may be time to fire your adviser, or if you are your own adviser, it may be time to seek advice from a certified financial planner.

How do I find a good adviser?

I suggest that you go to www.napfa.org or www.fpanet.org to find certified financial planners (CFPs) in your area. Interview two or three. Learn about their investment and planning philosophies, what they offer, and the amount of their fees. You can find some good questions to ask in the book *Getting Started in a Financially Secure Retirement* (Wiley,2007). Then select the one that seems the best fit for you.

A good financial adviser may be the best investment decision you every made—especially if your current adviser is making more from your investments than you are.

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www.analyzenow.com