

engage a corporate custodian and/or a broker-dealer to hold client assets, provide trading platforms, issue monthly account statements, and assist with compliance and numerous other back office services. The largest custodians providing services to the RIA community include Schwab Institutional, TD Ameritrade and Fidelity Investments. Using an independent custodian provides a system of checks and balances, as a client's funds are not held by the same entity that is providing investment advice. Since the RIA is not an employee of their chosen custodian(s), they are free from any pressures to promote proprietary investments and are compensated via an asset-based fee rather than by sales commission.

Unlike the service structure of a broker, most advisors manage client assets under a discretionary contractual arrangement. Thus, it's important for investors to understand the RIA's investment philosophy and process. This information is detailed in a registration document, known as the *Uniform Application for Investment Advisor Registration* (or Form ADV), which is required to be filed with the SEC and is distributed to clients annually. Form ADV also provides information on an advisor's ownership structure, fee schedules, compliance history, information about key staff members, and other information deemed relevant to a client's decision to hire the advisor. (Visit adviserinfo.sec.gov/IAPD/Content/Search/iapd_Search.aspx to access this information about any RIA.)

Registered Investment Advisors with assets under management in excess of \$110 million are required to register with the SEC and are governed by the Investment Advisors Act of 1940. Advisors with assets under \$110 million follow their state's statutes, rules and regulations. RIAs are required to pass the FINRA Series 65 exam, or the Series 7 exam in conjunction with the Series 66, unless they have successfully earned and maintained the Chartered Financial Analyst (CFA) or Certified Financial Planner (CFP) designations, in which case they are exempt from this requirement. The Advisors Act defines an investment advisor as any individual or entity that provides advice by making recommendations regarding securities or securities markets for compensation and who regularly engages in the business of providing advice regarding securities.

Highest Duty of Care

The most significant difference between a broker and an RIA is the requirement set forth by the Investment Advisors Act that defines an RIA as a *fiduciary*. (Recall that a broker is only required to make "suitable" investment recommendations based upon their client's financial circumstances). As a fiduciary, RIAs are legally obligated to act in the best interest of their clients, even if that runs counter to the RIA's own self-interests. A fiduciary duty is the highest duty of care recognized by the U.S. legal system, requiring an individual to act with both honesty and full disclosure. Therefore, RIAs operate under a higher standard of responsibility to their clients than any other financial service provider.

All indications appear to reflect that investors appreciate the fee transparency, flexibility and accountability associated with the service model of an RIA. According to a report by Cerulli Associates, client assets managed by independent RIAs grew by 45 percent from 2005 through 2011, compared to just five percent within the broker-dealer community.

Before hiring any investment professional, it's important to look beyond an individual title to gain a true understanding of the caliber, soundness and thoroughness of their financial advice. One should research their credentials, obtain a comfortable understanding of their investment philosophy and process, and review their firm's audited historical rates of return. Lastly, make absolutely certain that you understand their economic motivation and that they are fully transparent with their fee disclosures. **iBi**

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