SPARTA SPECIAL REPORT: WHY FIDUCIARY DUTY MATTERS

One of the best ways to start managing investment risk is by asking the right questions. An important question that you need to know the answer to is whether your financial advisor owes you a fiduciary duty or not. This is why:

If your investment advisor owes you a fiduciary duty, this means that they are obligated to put your interests ahead of theirs. If they do not owe you a fiduciary duty then that is one more reason why you should be supervising your financial advisor and keeping a close eye on your portfolio.

In the current regulatory environment, there is a difference between a "registered investment advisor" and a "financial advisor." These are not interchangeable terms despite their apparent similarity. **Investment Advisors** owe you a fiduciary duty. **Financial Advisors and stockbrokers** (typically employees of the large brokers and investment banks) do NOT owe you a fiduciary duty! They do have to make sure that the products they sell you are "suitable". For example, there may be three different funds to choose from, and it may also be that given your investment objectives and your current portfolio, one of the three funds would be much better for you, but all three funds are technically suitable. The stockbroker then picks the fund that pays the most commissions. Because he does not owe you a fiduciary duty, this behavior is ok under the law – and not uncommon.

TD Ameritrade did a study of investors back in 2006 that showed that:

- 54% believe that both stockbrokers and investment advisors have a fiduciary responsibility to act in investors' best interests in all aspects of the financial relationship (as explained above, this is incorrect; only 26% of investors knew that only investment advisors owe this duty).
- If investors knew that stockbrokers were not required to disclose all conflicts of interest and were not required to act in the client's best interest in all areas of the financial relationship, 70% of clients would not seek advice from them (how many investors understand this?)

In 2005, the SEC required that brokerage firms offering fee-based advice must make the following disclosure: "Your account is a brokerage account and not an advisory account. Our interests may not always be the same as yours. *Please ask us questions to make sure you understand your rights and our obligations to you, including the extent of our obligations to disclose conflicts of interest and to act in your best interest.* We are paid both by you and, sometimes, by people who compensate us based on what you buy. Therefore, our profits and our salespersons' compensation may vary by product and over time." After reading the previous disclosure, 79% said that they would be less likely to go to a brokerage firm for financial advice. **Do you use an investment advisor *or a financial advisor*? Does your advisor owe you a fiduciary duty to put your interests first or not?**

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