# Does it matter how financial planners and investment advisors are paid?

**Category : Payment of Investment Advisors, Financial Planners, and Investment Counselors**

**Published by** The Skilled Investor on Aug/1/2005

Does it matter how financial planners and investment advisors are paid?Yes, it can matter significantly how a financial advisor is paid. The heart of the compensation issue is an advisor’s potential "conflict of interest" with respect to payments from third parties. Does third party compensation change the quality of the recommendations that the advisers make? If an advisor works on sales commissions or accepts other third party payments, will he still provide the best recommendations based solely on the client’s best interests? *The Skilled Investor* believes that the great majority of advisors are ethical. They work to manage properly the conflicts of interest associated with third party compensation that most advisors receive. Many objective, competent, and ethical practitioners are doing excellent jobs for their clients – no matter what their source of compensation. Fee-only advisors, receive compensation directly and solely from their clients. Other advisors receive compensation from third parties. Some may receive both. When choosing an advisor, individuals should first decide the type of advisor compensation that makes them most comfortable. (For information on the different types of advisor compensation, see: Financial planner and investment advisor compensation paid by clients and Financial planner and investment advisor compensation paid by third parties) However, the problem for individual investors is not the ethical majority of practitioners. The problem is the ethically challenged minority. The heart of the conflict of interest issue is whether a client can tell the difference between an ethical practitioner who “just happens to be paid by third parties” versus an unethical advisor to whom the client’s interests are secondary. As you might expect, substantial controversy exists within the advisory industry about which forms of advisor payment are better for the client. Fee-only advisors argue that they have absolutely no conflict of interest in their obligation toward their clients. Assuming that a fee-only advisor is competent and diligent, a client can reasonably expect that the advisor’s recommendations will be objective and in the client’s best interests. Fee-only advisors say that commissioned advisors are just disguised salespersons. Advisors who accept various forms of third party compensation insist that they can be objective. They also contend that they still can and do offer the best products to their clients. Some commissioned advisors suggest that they are more motivated to meet clients’ needs. They say that their advice costs nothing, unless the client acts on a recommendation. Commissioned advisors may say that fee-only advisors are too disinterested, because they are paid whether or not a client acts upon their advice. They also argue that a client will still have to pay a transaction charge, if he were to go elsewhere to make the recommended purchase. Note that the size of the transaction charge is the crux of the issue, as well as the ongoing charges. See: Excessive investment costs are a huge problem for individual investors Note also that conflict of interest relates only to suboptimal advisor recommendations and to associated actions that confuse fiduciary priorities. Clients will still receive legitimate financial products for their money. These products just might not be the best or the most cost effective product available. More severe ethical shortcomings involve outright fraud. Such actions are not the subject of this article. For more information on protecting oneself from advisor fraud, see: ->Avoiding financial planning and investment advisor frauds and scams – Overview ->Avoiding advisor frauds and scams – The “Never-do” list, Part 1 ->Avoiding advisor frauds and scams – The “Never-do” list, Part 2 ->Avoiding advisor frauds and scams – The

“Never-do” list, Part 3

Also, see these related articles on advisor compensation: ->Fee-only compensation aligns the interests of clients and their financial advisors ->Fee-only financial planner and investment advisory groups ->The securities industry calls marketing and selling “advising” ->Many investors are not fooled by an ethically challenged securities industry