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Challenging Conventional Wisdom

How to spot a crooked financial advisor

Every year the media reports on numerous investment scams that have blown up and cost investors millions. Many of the big ones are first exposed by Moneyweb and I am surprised by how angry the victims are with the journalist who is essentially helping them. Usually they are angry because they feel the scam-artists are being unfairly victimised. This dynamic clearly changes when reality bites and the investors have no more money. Sadly it seems that the scam artists continue to lure people into their traps with sickening regularity. Here are some pointers to help you identify when someone might be trying to scam you.

1. **Your advisor is selling an investment where the returns are high and very consistent in all market conditions**

I use the word "advisor" in this column very loosely, scam artists are obviously crooks but you might not be aware of this when you start working with a new advisor. If you are being offered an investment that consistently grows at the same rate every year irrespective of how the stock, bond or property markets are performing, you are probably invested in a Ponzi scheme. The only time that you should expect such consistent returns is when you are invested in a money market-type investment where your growth should be very similar to current interest rates. In the current interest rate environment, if someone tells you they can give you 10% when most money markets are offering 6.5% to 7.5%, you should be very cautious.

2. **You cannot get a proper statement from the product provider.**

It is a great service if your advisor provides you a consolidated statement of all your investments and financial products but you should still be able to get a statement directly from the product provider. This should be on the product provider's "letterhead" and should state your name and your specific account number. It is also a good sign if you can get online access to your statements via the product provider but sometimes the international product providers are a bit backwards in this regard.

3. **Your advisor has a secret formula or "black box" that ensures he/she knows how to beat the market consistently**

No one has a formula for beating the markets all the time. Hedge funds are proving fallible when compared to the index and unit trusts have the same issue. Any time you are trying to beat inflation with an investment, you are taking risks and these are going to cause you losses from time to time. The best investors are only right 60% of the time and no formula or investment magic will do any better. It is particularly important to bear this in mind with people who trade based on algorithms that "predict" the market.

4. **Your advisor is vague on his commission or he earns double digit commissions**

With the property syndication scams we saw a few years ago, some brokers were earning 11% upfront commission. There is no way that this is sustainable and eventually this money comes from investors' capital.

5. **Guaranteed "interest rates" that are more than double the current market rates**
Remember that scheme that advertised guaranteed interest rates of 19% per year? These were guaranteed and were nearly 4 times higher than money market rates at the time. Sadly it blew up and the only losers were the investors…again.

HOW CAN YOU FIND A REPUTABLE ADVISOR?

- Look for a CFP® professional, you know they have studied financial planning at post graduate level and comply with a global ethical standard.
- Go to www.fpi.co.za to find a CFP® professional in your area
- Try to interview at least three different advisors before selecting one.
- Is your advisor open and transparent about his or her remuneration?
- Does your advisor deal with well-known product providers?
- Is your advisor registered with the Financial Services Board? This is a legal requirement and you can check to see if the person and the advisor's employer are registered via the FSB's website https://www.fsb.co.za/fais/search_fsp.htm