WEALTH MANAGEMENT

Investing 101: Asset Managers vs. Wealth Managers

by Jon McGraw

Knowing the difference between the two types of investment firms can help you define the correct long-term strategies.

In an investment world full of industry jargon, fancy titles and new-fangled investment products, it can be a daunting task just to find the answer to the simple question, “Which financial firm is the right firm for me?” As president of a wealth management firm, one of the most common questions I hear revolves around what to look for when trying to differentiate the various companies an investor can turn to for financial advice.

In the broad view, there are two main types of firms: Those that focus first on management of investment assets (asset management), and those that focus first on the strategy surrounding the total wealth of a family (wealth management).

Asset management firms are often registered with, or as, broker dealers and typically have the Financial Industry Regulatory Agency as their regulatory agency. FINRA firms are held to a “suitability” legal standard of care. Wealth management firms are often registered with the Securities and Exchange Commission and are held to the higher “fiduciary” legal standard of care. There is also the ability for “dual registration,” firms with both FINRA and SEC registrations.

Compensation for asset management firms is traditionally based on commissions, but a growing number of firms are now moving to a “fee based” or fee for assets under management model. Compensation for wealth management firms has traditionally revolved around the use of retainer fees and/or a fee for assets under management, rather than commissions for product sales.

The logic for retainer fees in the wealth management industry is fairly simple: As you enter into a wealth-management-focused relationship you are partnering with a team to serve as an outsource “Family CFO.” Just as you expect the CFO for your business to continually review and proactively implement financial strategy, your “Family CFO” should be doing the same, day in and day out.

Wealth management is often defined as a professional service combining the oversight of financial and investment advice, accounting and tax strategy, and legal and estate planning. While this is accurate, the definition tends to lead to confusion as almost every mainstream company in the financial industry says they can help with at least some of these items.

Both consumer and industry studies have shown the most successful wealth management relationships, as measured in terms of client net worth and longevity, are focused upon a comprehensive and detailed plan of action. The development of a plan and lifelong strategy as well as written investment policy has been shown to make significant headway on the road required to achieve a successful and holistic approach for high net worth individuals and multi-generational families.

During the first year or two of a wealth management relationship, the expectation of several scheduled and agenda-driven meetings is common. Often, the first meetings provide the foundation for development of a unique client-centric plan. The plan is then implemented, a formal review of progress is conducted annually and modifications to the plan are proactively enacted as family dynamics, tax code, economic cycles and estate laws change over time.

Again, in contrast to asset management, wealth management centered firms typically delve much more deeply and assist with non-investment-oriented prioritization of family goals and objectives. They often define real risk-adjusted rate of return requirements to meet those goals; determine the appropriate role of debt; show how to maximize the productivity of income; minimize the impact of taxes on family assets; explain strategy to protect income, cash flows and assets with insurance; and coordinate multi-generation family and estate issues.

Each of these topics could become an article unto itself, but suffice it to say wealth management firms typically differentiate themselves with core strategies emanating from solutions to real-life issues, rather than core strategy being accomplished through the use of investment products.

In the complex world we live in today, families who incorporate a trusted financial adviser into their lives fare better than those who do not. The decision of who to partner with is not simple, but having the knowledge to differentiate between asset management and wealth management-focused firms is the first step in determining which type of firm to select as your financial resource.

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