July 13-17, 2015

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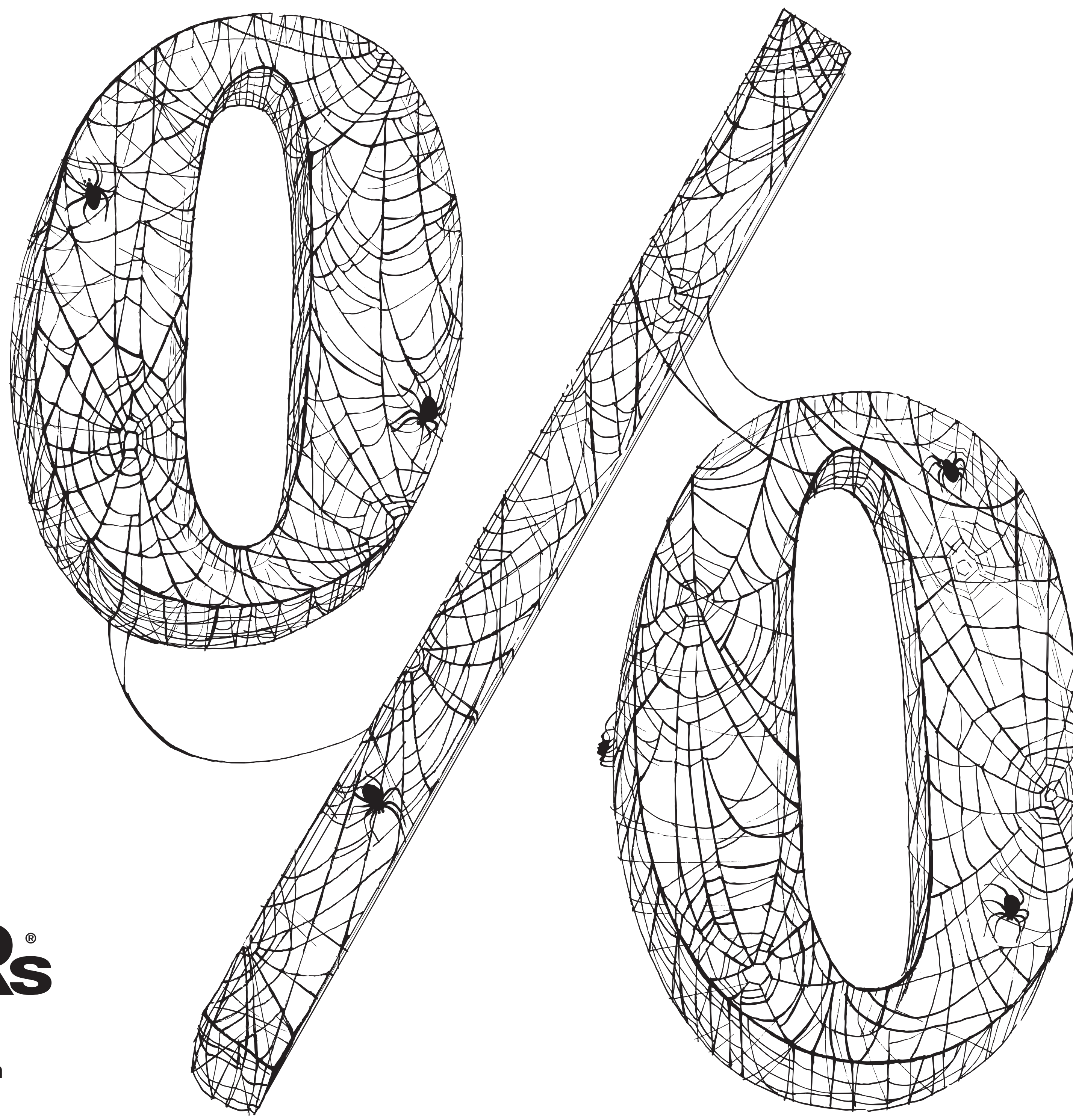
GAME CHANGERS

The Great Wealth Transfer

66%

of children fire their parents' financial adviser after they receive an inheritance. Are you prepared? Page 32



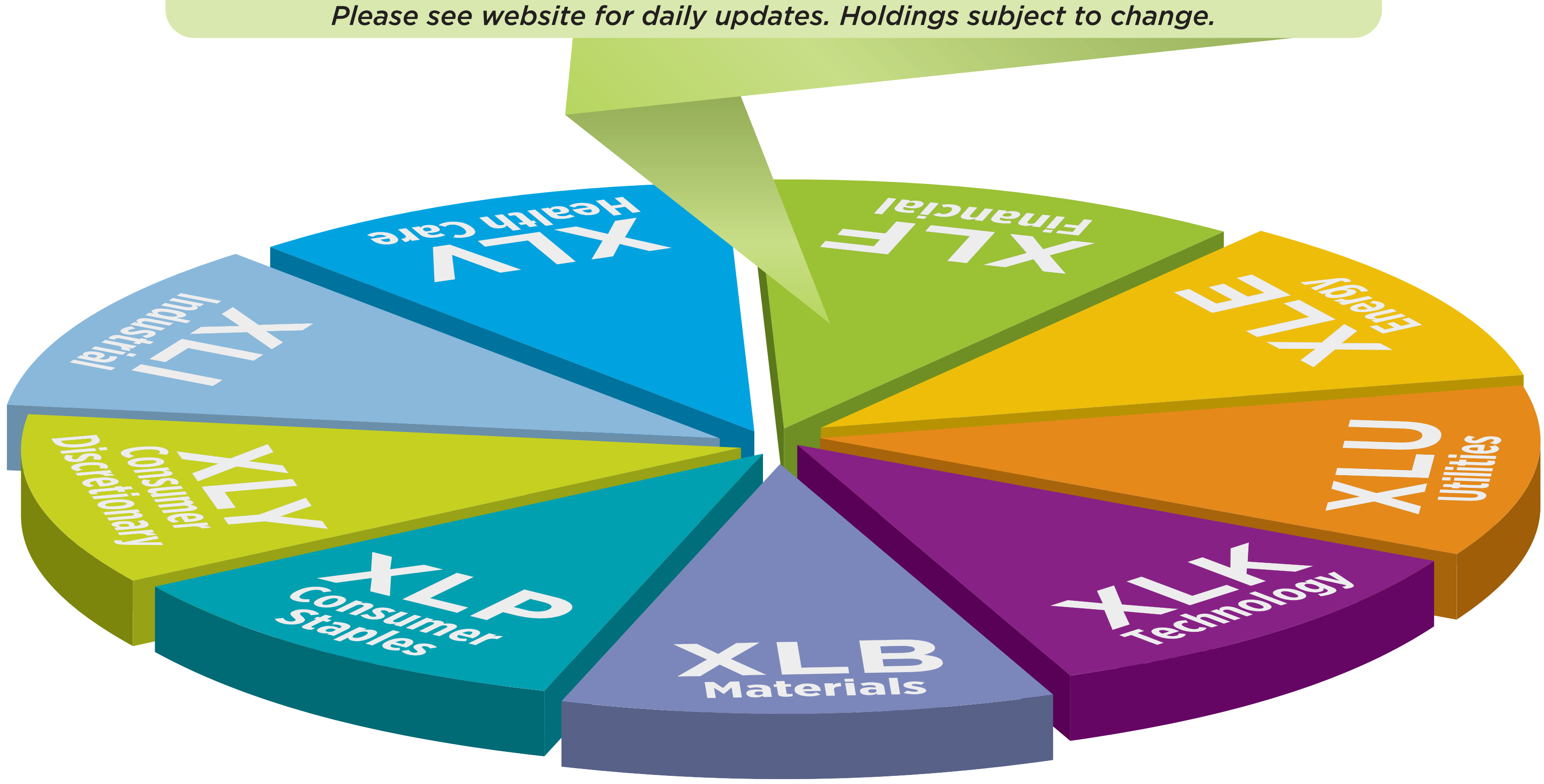
Financial Sector SPDR ETF

Top Ten Holdings*

XLF - FINANCIAL

	Company Name	Symbol	Weight
1	Wells Fargo	WFC	8.66%
2	Berkshire Hathaway B	BRK.b	8.61%
3	JP Morgan Chase	JPM	8.09%
4	Bank of America	BAC	5.73%
5	Citigroup	C	5.41%
6	Goldman Sachs	GS	2.76%
7	American Intl Group	AIG	2.65%
8	US Bancorp	USB	2.53%
9	American Express	AXP	2.31%
10	Morgan Stanley	MS	1.94%

** Components and weightings as of 5/31/15.*
Please see website for daily updates. Holdings subject to change.



domestic common stocks. Investors cannot invest directly in an index. The S&P 500 Index figures do not reflect any fees, expenses or taxes. Ordinary brokerage commissions apply. ETFs are considered transparent because their portfolio holdings are disclosed daily. Liquidity is characterized by a high level of trading activity.

Select Sector SPDRs are subject to risks similar to those of stocks, including those regarding short-selling and margin account maintenance. All ETFs are subject to risk, including possible loss of principal. Funds focusing on a single sector generally experience greater volatility. Diversification does not eliminate the risk of experiencing investment losses.

ALPS Portfolio Solutions Distributor, Inc., a registered broker-dealer, is distributor for the Select Sector SPDR Trust. STATE STREET GLOBAL ADVISORS.

Three B-Ds to repay $30M in overcharges

By Mark Schoeff Jr.

Three major broker-dealers must repay investors more than $30 million after improperly charging them for mutual funds that were purchased for retirement accounts and charities, Finra announced last Monday.

The Financial Industry Regulatory Authority Inc. ordered the restitution from Wells Fargo ($15 million), Raymond James ($8.7 million) and LPL Financial ($6.3 million) after the firms failed to waive sales loads for Class A mutual fund shares sold between July 2009 and the end of 2014.

The firms either passed along the charges improperly or put investors into Class B or C shares, which come with high back-end and ongoing fees. Often, mutual funds waive their Class A sales loads for retirement accounts and charities.

Finra said the firms failed to supervise mutual funds sales and

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Issues raised in CFP suit not settled yet

By Mark Schoeff Jr.

A judge's decision last week to dismiss a controversial lawsuit filed against the Certified Financial Planner Board of Standards Inc. involving how CFPs can describe their compensation model to the investing public may not be the last word on the matter.

The couple who brought the suit said they are considering an appeal, while others in the industry said the decision fails to settle all of the issues that the case has raised.

The suit was filed in 2013 by Jeffrey and Kim Camarda, married financial planners who accused the CFP Board of breach of contract, unfair competition and false advertising. This stemmed from a disciplinary case that the CFP Board brought against the couple in December 2011. The organization held that the Camardas misrepresented themselves as "fee-only" advisers because an arm of their firm sells insurance for commissions. The correct description should have been "fee-based," according to the CFP Board.

Many planners prefer to call themselves fee-only because they believe it carries more credibility in the eyes of investors.

After the decision, the Camardas said they might continue their legal battle against the CFP Board.

> "WE ARE CONSIDERING an appeal, but need to review the court's actual opinion before making that call."
>
> **Jeffrey and Kim Camarda,** in a statement

"At this time, we are considering an appeal, but need to review the court's actual opinion before making that call," the couple said in a statement last Wednesday.

"We are clearly disappointed in the decision and do not think it is correct if it rules that the CFP Board — being a private organization — has the prerogative to treat its licensees any way it wishes without any meaningful legal recourse to the judicial system available to certificants," the Camardas said.

In granting the CFP Board's request for summary judgment, U.S.

Continued on Page 31

Timing matters in divorce filings

Ben Affleck and Jennifer Garner: The couple announced their breakup the day after their 10th wedding anniversary.

GETTY IMAGES

Affleck-Garner split may point to role of 10-year mark

By Liz Skinner

Advisers with clients headed for divorce may want to keep in mind that sometimes it makes sense to wait a bit, just as Jennifer Garner and Ben Affleck have done.

The Hollywood couple announced June 30, the day after their 10th wedding anniversary, that they are splitting up. The famous pair said in a joint announcement that they'll continue to co-parent their three young children.

"Ten years is a magical number for a number of reasons," said Jeff Landers, president of Bedrock Divorce Advisors in New York.

In California, where the couple lives, marriages that last at least 10 years are considered "long duration."

Judges in California and a few other states can award alimony for an extended period of time to the receiving spouse if the marriage lasted at least a decade, Mr. Landers said. For marriages shorter than 10 years, California judges who order spousal support usually do so for about half the length of the marriage.

SIGNIFICANT MILESTONE

Many other states, including New York, do not tag marriages as long-duration until the couple has been wed for more like 20 years, he said.

In Texas, no spousal support can be ordered until the couple has been married at least a decade.

It's unclear whether any spousal support

Continued on Page 29

Crippled by false claims flap, F-Squared files for bankruptcy

By Trevor Hunnicutt

F-Squared Investments Inc. filed for bankruptcy protection last Wednesday and arranged for its investment strategies to be managed by a new firm, capping the rise-and-fall story of the exchange-traded fund manager once popular with financial advisers.

The company filed documents seeking Chapter 11 bankruptcy protection and asked the court to allow it to sell its investment strategies, contracts to manage money and other intellectual property to a competing money manager.

The move likely will allow the firm's flagship AlphaSector strategy to live on, managed by the buyer, Broadmeadow Capital, which is affiliated with F-Squared rival Good Harbor Financial.

"The opportunity presented itself," said Paul R. Ingersoll, chief executive at Cedar Capital and Good Harbor. "For all the things that F-Squared has gone through, and however unfortunately some of their materials have been represented, a significant amount of their clients like their approach to investing and like their strategy."

He said his primary goal, if the deal closes as expected within 45 days, is to "maintain the client relationships."

$35 MILLION SETTLEMENT

F-Squared was unable to do that. In December, the firm agreed to pay $35 million to settle charges it made false claims about the performance of its AlphaSector index.

The settlement didn't end F-Squared's problems, as it began bleeding assets. Lawyers and investors went after the company, its mutual fund distribution partner and financial advice firms that sold the products. At least one broker-dealer, Wells Fargo Advisors, currently is facing claims challenging those sales in arbitration. One of the firm's former executives also filed a lawsuit against F-Squared.

Continued on Page 30

Plucky candidates seek Finra board seats

Three contenders had to work way onto ballot, want reform in exams and arbitration

By Mark Schoeff Jr.

Three candidates for open seats on the Finra board who had to work their way onto the ballot say they will stand up to the regulator to defend their segments of the industry.

They were not selected by the Financial Industry Regulatory Authority Inc. nominating committee, and had to gather enough petition signatures to launch races.

Two — Stephen A. Kohn, president and chief executive of Stephen A. Kohn & Associates, and Joseph R.V. Romano, president of Romano Wealth Management — are running for the open small-firm seat. Beefs with Finra exams are a common rallying point.

"It is evident that examination tactics have no bounds; every aspect of our business and personal affairs is fair game," Mr. Kohn wrote in a letter to the 3,600 small-firm Finra members, calling for a code of conduct for examiners. "It is not acceptable that examiners can invade our offices with impunity, having no fear of being called to task for improper, disrespectful or coercive behavior."

"IT IS EVIDENT that examination tactics have no bounds; every aspect of our business and personal affairs is fair game."

Stephen A. Kohn
Chief executive
Stephen A. Kohn & Associates

Although he agrees that Finra rules can have unintended and costly consequences for small firms, Mr. Romano argues that his experience working within the Finra governance system better positions him to change it. He is serving this year as chairman of the Small Firm Advisory Board and has served on Finra committees over the past seven years.

"I'm running on proven results, rather than just promises," Mr. Romano said. "We need more than just griping. We need someone who can advocate solutions."

Frustration with the Finra examination process inspired Mr. Kohn to conduct his fourth campaign for the organization's board. His previous attempts were unsuccessful.

He said reviews last too long — his most recent one began in December 2013 and closed in September 2014 —

Continued on Page 31

EDITOR'S NOTE

Don't let trillions walk out the door

For all their talk about the importance of long-term planning, financial advisers are terrible when it comes to planning for anything beyond a few years down the road. We already know that most advisers do not have a formal succession plan for their practices and, as this week's latest in our popular Game Changers' franchise points out, even fewer are thinking about how they are going to manage assets for their client's children after their clients die.

Frederick P. Gabriel Jr.

In fact, the vast majority of advisers are likely going to see those assets walk out the door as soon as their clients' death certificate is signed.

To put an even finer point on the matter, an estimated $30 trillion in assets will be passed down from baby boomers to Generation X to millennials over the course of the next 30 years. Financial advisers who give short shrift to developing relationships with their clients' children — while their clients are still alive — are sure to lose more assets than they can ever hope to bring in. That, in turn, will negatively affect the value of their firms — thereby putting a crimp on their own ability to pass on wealth.

Hopefully, our story "Courting the kids," which begins on Page 32 and was written over a period of months by reporter Liz Skinner, will serve as a call to action to financial advisers who are serious about building a sustainable business.

As with all our Game Changers, this one is really meant to be experienced online. There you will also find compelling videos featuring financial advisers who have developed a plan for working with their clients' children. We also put together a series of interactive illustrations that make it easier to understand how quickly a large portfolio can dwindle once it is divided up into several inheritances. Finally, we also offer links to additional resources that will be useful if you decide to answer our call to action.

All that can be found at InvestmentNews.com/transfer.

fgabriel@investmentnews.com, Twitter: @fredpgabriel

We'll be back.

InvestmentNews won't publish a print edition July 20. Print publication resumes July 27.

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INTV VIDEO Watch this week's clips at InvestmentNews.com/INTV

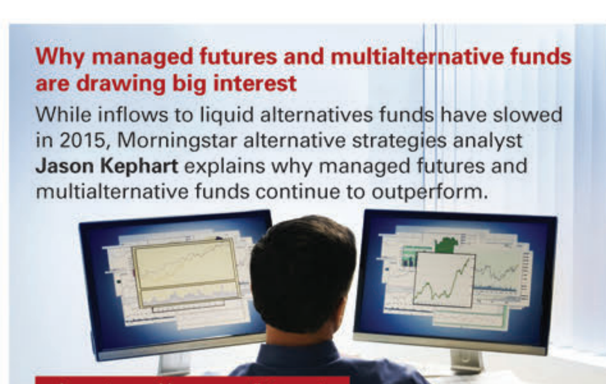
Where opportunities lie in today's bond market

Michael Fredericks, lead portfolio manager of the Multi-Asset Income Fund (BIICX) at BlackRock Inc., says that bond investors looking for income will need to reposition their portfolios, and highlights the areas of the market with big potential.

InvestmentNews.com/bond

Why managed futures and multialternative funds are drawing big interest

While inflows to liquid alternatives funds have slowed in 2015, Morningstar alternative strategies analyst **Jason Kephart** explains why managed futures and multialternative funds continue to outperform.



InvestmentNews.com/interest

Female advisers have an opportunity to lead

Erinn Ford, president of Cetera Advisors, says the advice industry is depending on women to step up and assume more leadership positions.

InvestmentNews.com/lead

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Billy Joel paid Uncle Sam, and his expected kid could collect

Singer is 66, so he could trigger benefits for baby by filing and suspending

Mary Beth Franklin
On Retirement

I was surprised to hear the strains of "Just the Way You Are" on my local all-news radio station this week. It was the song that my husband and I danced to at our wedding nearly four decades ago.

The music served as the lead-in for a news item about its composer, singer/songwriter Billy Joel. The Piano Man tied the knot for the fourth time over the Fourth of July weekend in a ceremony at his sprawling estate on Long Island. He married Alexis Roderick, 33, a former Morgan Stanley executive. They are expecting their first child this summer.

I have no idea whether Mr. Joel is collecting Social Security benefits. I doubt he needs the money, as his upcoming appearances in Boston and New York City are sold out. But he has reached the magic age of 66, when the earnings cap no longer applies, meaning he can collect Social Security benefits without reduction even as he continues to work.

What Mr. Joel may not know is his soon-to-be born child may be entitled to Social Security benefits, too.

Because Mr. Joel is now 66, he can file and suspend his Social Security benefits, triggering a monthly payment for his minor dependent child worth 50% of his full retirement age benefit amount. In the meantime, Mr. Joel's own retirement benefit will continue to grow, earning delayed retirement credits of 8% per year up to age 70.

'VIAGRA COLLEGE FUND'

I have jokingly referred to this phenomenon of Social Security benefits for minor dependent children of retirement-age fathers as "the Viagra college fund." Put that money in a 529 college savings plan, and you'll have paid for Harvard. Minor children are entitled to collect Social Security dependent benefits until they turn 18 (or 19 if they are still in high school).

You would be amazed at how many questions I receive about this subject, both in person during Social Security presentations to consumers and financial advisers, and via email from *InvestmentNews* readers. A child may be eligible for benefits if he or she is your biological child, adopted child or dependent stepchild. (In some cases, a child also could be eligible for benefits on his or her grandparents' earnings.)

The high rate of remarriage in America apparently has led to an increase in the number of older parents with minor children. In fact, more than 4 million children receive approximately $2.5 billion in Social

Continued on Page 29

Big brokerage turned its back to sham: Galvin

By Mason Braswell

Massachusetts' top securities cop has charged Securities America Inc. with failure to supervise a broker who allegedly used deceptive advertising on his radio show that targeted senior citizens.

The regulator accused the firm, a subsidiary of Ladenburg Thalmann Financial Services Inc. with more than 2,000 brokers, of approving ads from a broker who "exploited the dangers of Alzheimer's disease in order to gain access to senior clients," according to a statement from the office of William Galvin, secretary of the commonwealth.

Mr. Galvin has filed a separate complaint against the broker, Barry Armstrong, the statement said. Mr. Armstrong and his firm, Armstrong Advisory Group, manage $400 million in client assets, according to the firm's website.

The complaint against Securities America requests a censure, an undisclosed fine and a requirement that the firm retain a compliance consultant.

Mr. Armstrong, who hosts a regular radio show that runs on several AM stations, ran ads that instructed listeners to call him for "medical and support" information about Alzheimer's disease in order to get their contact information and then attempt to sell financial advice, according to the complaint.

'BAIT AND SWITCH'

Mr. Armstrong "pulled a 'bait and switch,' falsely advertising one service to obtain contact information, and then switching it out for another — financial services," the complaint said.

"Securities America's failure to raise a single question about the content of the Alzheimer's ads and the attendant mailing materials represents an utter failure that goes to the very purpose of a compliance function," the secretary's office said in the news release. "Securities America failed to prevent or even flag glaringly unethical conduct."

Securities America disagrees, according to spokeswoman Natalie Haley, who wrote in an emailed

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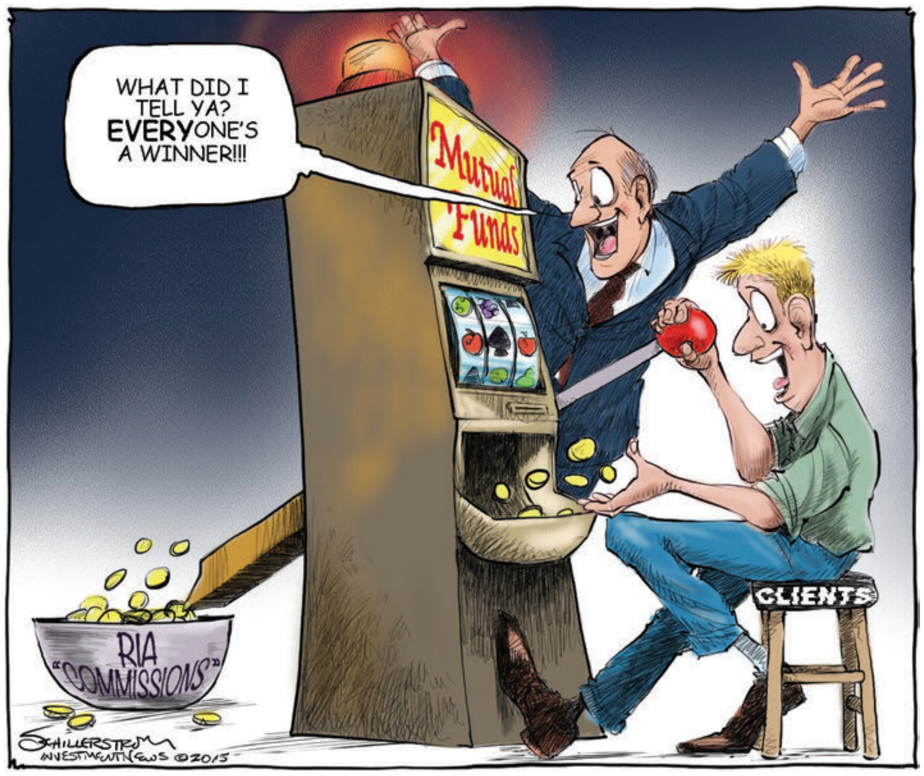
VIEWPOINT

EDITORIALS

Fees from custodians fail smell test

THE PRACTICE of registered investment advisers' collecting fees from custodians for recommending certain mutual funds to clients throws the raging fiduciary debate into a whole new light.



As reported in *InvestmentNews,* more RIAs are quietly accepting such payments of up to 0.2% of assets held in certain no-transaction-fee mutual funds. Charles Schwab & Co. Inc. and Fidelity Investments, the nation's No. 1 and No. 3 custodians for advisers, respectively, are among the biggest payers. TD Ameritrade Institutional, the No. 2 custodian for advisers, does not pay such fees.

RIAs who hold themselves out as fee-only, conflict-free advisers and yet accept such fees ought to be called out for the practice so clients can determine on their own whether the advice from these agents is indeed fee-only and conflict-free. Can these advisers really be fiduciaries? At the very least, the practice fails the fiduciary smell test.

'AN ELEMENT OF BIAS'

An adviser could, certainly, in good faith determine for himself that even though he accepts these "small" fees, they do not sway him to recommend a fund from a custodian that pays them over one that doesn't. After all, these are no-transaction-fee funds, so their cost is low. Aren't they in the best interests of clients? In some cases, depending on the entire fund lineup, perhaps. But why raise a conflict of interest in the first place? We would question the veracity of that adviser's point of view and whether it can really hold true.

"We think this is one of the most egregious [conflicts of interest] we've seen in recent years, and it seems to be more widely practiced," Tom Nally, head of TD Ameritrade Institutional, told *InvestmentNews* recently. "It's a problem. It adds an element of bias that most clients probably don't understand."

To be sure, firms disclose the practice fully, and some, like HighTower Advisors and Mariner Wealth Advisors, acknowledge that the payments create conflicts of interest. Kudos to HighTower, Mariner and other firms that 'fess up, but the reality is that if such an admission is buried in a Securities and Exchange Commission filing or a 30-page investment brochure, chances are slim that clients will see it.

And that's probably how the firms would like it.

Sure, RIAs taking these fees must report them. But where? Part 2 of their Form ADV. The next question would be: How many clients a) know where to look for the disclosure and b) know how to make sense of it in order to make an informed decision?

YOU CAN CALL it whatever you want, but it's equivalent to a payment for sales.

Mr. Nally said the trend may be driven at least in part by the increase in wirehouse breakaways who are used to receiving service fees on mutual funds. He added that the fees sounded to him like a commission, which is something that raises certain expectations in the minds of clients. Namely, if their adviser charges commissions, clients know there will be some level of bias in the recommended investments. No commission, no bias.

Ah, the c-word. We can hear the hackles rise already. "It's not a commission!" "Do you even know what a commission is?!" "Commission? That's insane!"

But if something smells like and looks like a commission, you can call it whatever you want, but it's equivalent to a payment for sales of a product. And clients understand the word commission a whole lot better than "shareholder services fee," which is how these payments are classified.

If anyone wonders why the financial advice industry has not risen to the level of a noble cause (as it surely could, considering the number of people who are unlikely to meet their financial goals but might if they had some solid guidance), blame practices like this.

SUBPAR PLANNING

A survey from Northwestern Mutual earlier this year found that while 58% of Americans think their financial planning is subpar, 34% haven't done anything about it. In addition, 43% haven't spoken to anyone about retirement planning, while 21% don't even think they'll be able to reach their financial goals.

That spells a lot of opportunity for advisers. Unfortunately, too many of them are too worried about their own compensation to truly put clients first.

Freeing VAs from information overload

Investment product-marketing materials inevitably come with the warning: Read the prospectus carefully before investing. But do investors really read them? Not many. Do those who read them understand them? Hardly.

This reality has gotten regulator attention — at least when it comes to mutual funds. In 2009, the Securities and Exchange Commission adopted a final rule requiring funds to include key information in plain English in a standard fashion at the beginning of prospectuses. It also allowed mutual funds to use the key information as a standalone summary prospectus, with the traditional version still available for those hardy investors who just can't get enough details about what they're buying.

Now the call has gone out to adopt similar rules for variable annuities, most recently from the SEC's own investor advocate, Rick Fleming.

JUST DO IT
New call for VA summary prospectuses.
Page 27

Summarizing key information that is standardized across investment options is useful when comparing important factors such as objectives, performance, cost and risks.

UNWIELDY PROSPECTUSES

Current rules prohibit VAs from offering a pared-down version of their unwieldy prospectuses — often filling 150-200 pages. Clearly this prohibition does not align with the SEC's mandate to protect investors. Confusing or blinding investors with information overload hardly helps them.

Better yet, all relevant players seem to be on board with such a change. According to an *InvestmentNews* article by Mark Schoeff Jr., the Insured Retirement Institute, an interest group representing the annuity market, has been pushing for VA summary allowances for about nine years. And the IRI said all five SEC commissioners expressed their support for such summaries in meetings last fall.

We appreciate that the SEC's agenda is heavy with Dodd-Frank mandates, but for goodness sake, take the easy win when it's so clearly ahead of you and so obviously will benefit investors.

Last year, the SEC reported that about 80% of mutual funds had developed summary prospectuses since the rule came out six years ago. Time to allow the same logical disclosures for VAs.

ADD YOUR VOICE to the mix. Readers: Keep letters brief. Include your name, title, company, address and a telephone number for verification purposes. Email Frederick P. Gabriel Jr. at fgabriel@investmentnews.com. All mail may be edited.

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Audit Bureau of Circulations

Vanguard wants to help advisers woo clients

Services include custom brochures using firms' logos

By Trevor Hunnicutt

The Vanguard Group Inc., which became the world's largest mutual fund company after an ongoing marketing campaign to attract financial advisers, will launch a service this month to help those professionals communicate their own value to clients and prospects.

The money manager's new online service, dubbed the "Client Relationship Center," will, among other features,

ADVISERS ARE "grappling with their value propositions."

Dave Swanson
Managing partner
SwanDog Strategic Marketing

allow advisers to generate customized brochures for their clients. The documents will include value statements outlining an adviser's approach to managing wealth, client meeting agendas and a list of services they provide to clients. The materials will display each adviser's logo and information, not Vanguard's.

Vanguard's new program reflects a belief that its growth will be driven in part by financial advisers, and it comes as advisers are "grappling with their value proposition," according to Dave Swanson, managing partner at SwanDog Strategic Marketing, and an industry specialist who is not affiliated with the new Vanguard effort.

"It's symbolic, if nothing else," Mr. Swanson said. "Everyone responds so quickly in this space that if what Vanguard is doing gets any demand, you'll see other firms come out with something that looks and smells like it pretty quickly."

Vanguard, which manages approximately $3 trillion in assets, may not exactly be in the business of supporting financial advisers' practice management efforts. But they've built one of the best-known brands in retail investing. After building a sales effort to reach out to advisers and large broker-dealers that started in full force in 2002, the firm built an enterprise that helped it become the top mutual fund and exchange-traded fund brand by combined assets, according to Morningstar Inc. It's fought for that distinction against formidable firms, such as Fidelity Investments, BlackRock Inc. and American Funds.

In May, Vanguard officially launched its own automated investment platform, Personal Advisor Services, stoking fears that it might compete with financial advisers.

In recent years, the firm has tried to combat those fears. That effort includes the firm's "advisor's alpha" concept, which argued that financial planners can add "about 3%" to their clients' returns through investment selection, rebalancing, behavioral coaching and other services. Vanguard's adviser-sold unit now accounts for a third of the firm's assets and about half of its sales.

BETTER RELATIONSHIPS

Michael Lucci, a top sales executive at Vanguard, said the idea for the Client Relationship Center came from conversations that the firm's fund-sellers had with advisers. He said he hopes the service will allow advisers to build better relationships with their own clients and with Vanguard.

"This is a tool to help them be more consistent," Mr. Lucci said. "Continuing to build on that is going to be critical for us as we build relationships with advisers."

"This only helps an adviser without the wherewithal to do it themselves," Daniel P. Wiener, editor of the newsletter Independent Adviser for Vanguard Investors, wrote in an email. "Suppose I'm a prospective client and I go see a couple of advisers to interview, and they both show me the same document with a different name on it? Impressive? Not."

Vanguard said it built the platform in consultation with advisers and a series of focus groups. The company plans to add features in the coming months.

"The Client Relationship Center will enable advisers to more easily create customizable communications that can be made to look and feel unique," said David Hoffman, a Vanguard spokesman. "Importantly, this frees up advisers to spend more time on the practice of wealth management."

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Spotlight

Focus on REITs

INSIDE

12 Top publicly traded REITs, ranked by one-year total return.

14 Niche REITs take specialization to new levels.

Online For more REIT rankings, including data on nontraded REITs, go to InvestmentNews.com/REITS2015.

Selective market: REIT sectors that have the ability to increase rents, including apartments and hotels, should perform well once interest rates start to go up.

GETTY IMAGES

A SILVER LINING

Rising rates might hurt REITs initially, but they could benefit from a strengthening economy

By Jeff Benjamin

JUST BECAUSE real estate investment trusts have been riding high as an alternative source of income during an extended — and unprecedented — period of low interest rates, there is no reason to assume REITs can't thrive when rates start rising.

"There's a prevailing thinking that REITs don't do well in a rising-rate environment, but that's not a given," said Kevin DiSano, chief portfolio strategist at IndexIQ.

Under historically normal conditions, a rising-rate environment would logically equate to a higher cost of financing for leverage-heavy REITs.

"The cost of financing is the key, because that obviously puts pressure on the free cash flow that is paid out in the form of dividend yields," Mr. DiSano said.

That's the logic that might trigger an initial spike in REIT price volatility. But it is also assumed that the logic, when carried a step further, recognizes that a decision by the Federal Reserve to move short-term interest rates off a floor of near zero will be seen as a sign of a stronger economy.

"Initially, with any discussion of rising rates, REITs should come down with the rest of the market because they get lumped into the fixed-income category, but that's when you have to start thinking of the business structure of a REIT," said Michael Black, owner of Michael Phillips Black Wealth Management.

A strengthening economy allows many REITs to raise rents, making properties more valuable, he said. "So, I see it as a buying opportunity."

3.8%
Percentage decline in the FTSE Nareit Index between Jan. 1 and June 26.

LACKLUSTER YEAR

By various measures, it has not been a great year for REITs, but they've had a good run over the past few years.

This year, through June 26, the FTSE NAREIT Index declined by 3.8%, which compares with a gain of 3.1% for the S&P 500, a 0.3% gain for the 10-year Treasury, a 10% decline for the S&P utilities sector, and a 7.3% gain for the Nasdaq Composite Index.

In the same period, open-end U.S. real estate mutual funds declined by 4%, while global real estate mutual funds were up 0.5%.

Last year, the NAREIT index gained 27.2%, outpacing all the previously mentioned investment categories with the exception of the utilities sector, which gained 29%.

"You always need to be selective when investing in REITs, but when you're looking at rising rates, you want to invest in areas that have the ability to increase rents and therefore their income," said Gilbert Armour, a financial adviser with SagePoint Financial.

"As rates rise, competition with other sources of income could make REITs less attractive," he added. "But I think it still makes sense if you're selective, because rising rates probably favor REITs with the ability to raise rents more frequently, such as apartments and hotels."

A key element to investing in REITs in a rising-rate cycle is to recognize the unprecedented context of the

Continued on Page 16

Focus on REITs

Publicly traded real estate investment trusts

Ranked by one-year total return

	Company/Ticker symbol	Phone/Website/CEO	Property focus/ # of properties	One-year total return*	Dividend yield*	Implied market capitalization ($M)*	2014 funds from operations per share/growth	Debt-to-total capitalization 2014/2013	Fixed-charge coverage ratio (multiple) 2014/2013
1	**Associated Estates Realty Corp. (AEC)** 1 AEC Parkway Richmond Heights, OH 44143	(216) 261-5000 associatedestates.com Jeffrey I. Friedman	Multifamily 51	**70.6%**	2.9%	$1,656.8	$1.26 -0.8%	35.9% 46.8%	3.9 3.2
2	**CoreSite Realty Corp. (COR)** 1001 17th St. Denver, CO 80202	(866) 777-2673 CoreSite.com Thomas M. Ray	Data center 17	**49.5%**	3.5%	$2,238.5	$2.22 22.0%	14.0% 12.6%	9.3 9.1
3	**QTS Realty Trust Inc. (QTS)** 12851 Foster St. Overland Park, KS 66213	(913) 814-9988 qtsdatacenters.com Chad L. Williams	Data center 12	**39.4%**	3.4%	$1,823.0	$1.91 N/A	33.8% 27.6%	6.2 8.5
4	**Sun Communities Inc. (SUI)** 27777 Franklin Road Southfield, MI 48034	(248) 208-2500 suncommunities.com Gary A. Shiffman	Manufactured home 243	**35.0%**	4.0%	$3,678.0	$3.06 -1.6%	36.2% 45.9%	2.7 2.5
5	**Extra Space Storage Inc. (EXR)** 2795 E. Cottonwood Parkway Salt Lake City, UT 84121	(801) 365-4600 extraspace.com Spencer F. Kirk	Self-storage 835	**34.8%**	3.4%	$8,788.3	$2.52 28.6%	24.9% 27.5%	4.9 4.5
6	**CyrusOne Inc. (CONE)** 1649 W. Frankford Road Carrollton, TX 75007	(713) 821-1260 cyrusone.com Gary J. Wojtaszek	Data center 27	**34.8%**	4.1%	$2,003.3	$1.73 41.8%	28.8% 29.3%	4.0 3.0
7	**CubeSmart (CUBE)** 5 Old Lancaster Road Malvern, PA 19355	(610) 535-5700 cubesmart.com Christopher P. Marr	Self-storage 463	**33.9%**	2.7%	$4,071.7	$1.03 18.4%	23.9% 32.8%	3.7 3.4
8	**Pennsylvania REIT (PEI)** 200 S. Broad St. Philadelphia, PA 19102	(215) 875-0700 preit.com Joseph F. Coradino	Regional mall 39	**33.3%**	3.7%	$1,770.6	$1.82 0.6%	45.3% 51.6%	2.2 2.0
9	**Equinix Inc. (REIT)** One Lagoon Drive Redwood City, CA 94065	(650) 598-6000 equinix.com Stephen M. Smith	Data center 104	**31.9%**	2.6%	$14,876.9	$2.76 -67.5%	26.8% 31.8%	3.7 3.6
10	**Summit Hotel Properties Inc. (INN)** 12600 Hill Country Blvd. Austin, TX 78738	(512) 538-2300 shpreit.com Daniel P. Hansen	Hotel 90	**30.4%**	3.6%	$1,148.7	$0.90 36.4%	32.8% 30.6%	2.8 2.5
11	**Chatham Lodging Trust (CLDT)** 50 Cocoanut Row Palm Beach, FL 33480	(561) 802-4477 chathamlodgingtrust.com Jeffrey H. Fisher	Hotel 131	**28.7%**	4.3%	$1,076.2	$1.91 28.2%	35.7% 33.6%	2.7 2.9
12	**Macerich Company (MAC)** 401 Wilshire Blvd. Santa Monica, CA 90401	(310) 394-6000 macerich.com Arthur M. Coppola	Regional mall 68	**28.6%**	3.2%	$13,921.0	$3.54 0.3%	30.3% 33.2%	3.5 3.2
13	**Equity LifeStyle Properties Inc. (ELS)** Two N. Riverside Plaza Chicago, IL 60606	(312) 279-1400 equitylifestyle.com Marguerite Nader	Manufactured home 386	**27.6%**	2.7%	$5,018.5	$2.69 28.7%	31.4% 39.0%	3.0 2.7
14	**DuPont Fabros Technology Inc. (DFT)** 1212 New York Ave. Washington, DC 20005	(202) 728-0044 dft.com Christopher P. Eldredge	Data center 11	**27.3%**	5.3%	$2,582.4	$2.37 62.3%	25.2% 27.1%	4.1 3.1
15	**Iron Mountain Inc. (IRM)** One Federal St. Boston, MA 02110	(617) 535-4766 ironmountain.com William L. Meaney	Data center 264	**27.0%**	5.8%	$6,891.0	$2.55 N/A	36.5% N/A	3.4 N/A
16	**Essex Property Trust Inc. (ESS)** 925 E. Meadow Drive Palo Alto, CA 94303	(650) 494-3700 essex.com Michael J. Schall	Multifamily 244	**25.7%**	2.6%	$15,063.8	$7.89 4.0%	27.1% 34.4%	3.9 3.4
17	**UDR Inc. (UDR)** 1745 Shea Center Drive Highlands Ranch, CO 80129	(720) 283-6120 udr.com Thomas W. Toomey	Multifamily 166	**25.6%**	3.3%	$8,961.7	$1.56 8.3%	29.8% 35.9%	3.6 3.4
18	**Digital Realty Trust Inc. (DLR)** Four Embarcadero Center San Francisco, CA 94111	(415) 738-6500 digitalrealty.com A. William Stein	Data center 130	**25.4%**	4.9%	$9,542.8	$5.04 6.3%	31.3% 40.9%	3.7 3.7
19	**Alexandria Real Estate Equities Inc. (ARE)** 385 E. Colorado Blvd. Pasadena, CA 91101	(626) 578-0777 are.com Joel S. Marcus	Office 183	**24.9%**	3.3%	$6,721.3	$4.42 2.1%	35.2% 38.2%	4.3 4.2
20	**Apartment Investment and Mgmt Co. (AIV)** 4582 S. Ulster St. Denver, CO 80237	(303) 757-8101 aimco.com Terry Considine	Multifamily 198	**24.8%**	3.1%	$6,305.6	$2.07 1.5%	40.1% 50.1%	2.5 2.4
21	**Equity Residential (EQR)** Two N. Riverside Plaza Chicago, IL 60606	(312) 474-1300 equityapartments.com David J. Neithercut	Multifamily 387	**24.6%**	3.0%	$28,298.0	$3.15 34.0%	28.5% 35.4%	3.5 3.0
22	**Gaming and Leisure Properties Inc. (GLPI)** 825 Berkshire Blvd. Wyomissing, PA 19610	(610) 401-2900 glpropinc.com Peter M. Carlino	Casino N/A	**24.5%**	5.8%	$4,331.5	$2.37 690.0%	44.0% 34.3%	3.5 5.1
23	**Ryman Hospitality Properties Inc. (RHP)** One Gaylord Drive Nashville, TN 37214	(615) 316-6000 rymanhp.com Colin V. Reed	Hotel 12	**24.0%**	4.7%	$2,863.1	$4.27 14.2%	33.3% 35.4%	4.6 3.9
24	**Preferred Apt Communities Inc. (APTS)** 3284 Northside Parkway N.W. Atlanta, GA, 30327	(770) 818-4100 pacapts.com John A. Williams	Multifamily 22	**23.7%**	7.0%	$234.3	$0.63 N/A	51.1% 45.3%	1.6 1.0
25	**Winthrop Realty Trust (FUR)** 7 Bulfinch Place Boston, MA 02114	(617) 570-4614 winthropreit.com Michael L. Ashner	Diversified 47	**23.3%**	0.0%	$553.7	N/A N/A	39.3% 50.7%	1.8 2.0

Ranking based on unrounded figures. Includes only those publicly traded U.S. equity REITs with an implied market cap greater than $200M. As of Dec. 31 unless otherwise noted. NA = not available. *As of June 18.

Source: SNL Financial, Charlottesville, VA (434) 977-1600, www.snl.com/real_estate

Calling all investors: Some REITs limit their portfolios exclusively to cellphone towers.

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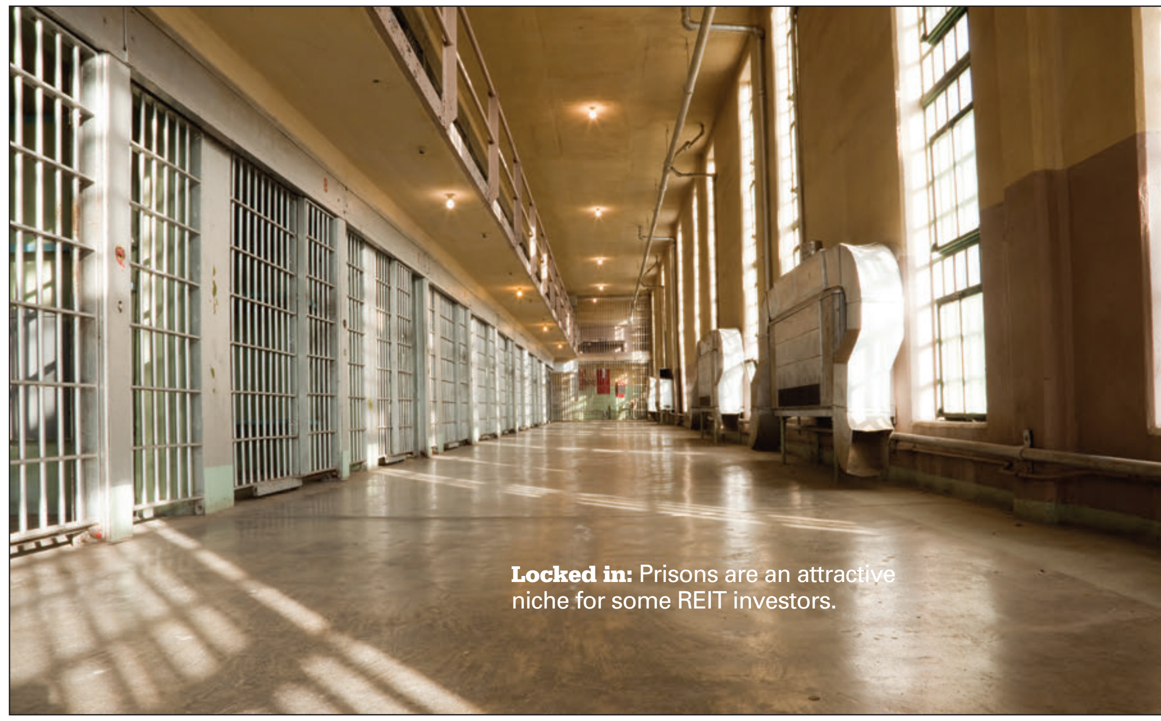

Locked in: Prisons are an attractive niche for some REIT investors.

ISTOCK

Specialty REITs offer something for everyone

Niche firms focus on a single type of property

By Mason Braswell

MOST INVESTORS who are looking to diversify their portfolios with real estate know they can turn to real estate investment trusts for access to fairly standard holdings such as office buildings, multifamily homes or hotels. But beyond that is a second layer of publicly traded REITs focused exclusively on some rather unusual properties — from cell phone towers to FBI field offices.

These lesser known REITS, often referred to as specialty REITS, have started to outgrow their name in recent years, becoming more mainstream as some sectors, such as self-storage REITS, have performed well. Of the 166 REITs tracked by the National Association of Real Estate Investment Trusts Inc., a membership group for REITs, roughly 45, or close to 30%, could be considered specialized. Advisers, however, are still weighing the risks.

"They are an interesting play from a cash-flow perspective, but clearly have some real risks, said Duncan Rolph, a managing director at Miracle Mile Advisors. Those risks include low trading volume and an over-reliance on specific industries.

Because they are hard to categorize, limited data exists on the growth of specialty REITs. The category itself is fairly open-ended — a company can be considered a REIT as long as at least 75% of its revenue comes from real estate, which is defined as land and the improvements on it, according to Ron Kuykendall, vice president of communications at Nareit.

Specialty REITS were introduced in the late 1960s as a way for investors to buy into microwave towers. Billboard REITS came along in the 1990s, and then came self-storage REITs, which benefited from the 2008 mortgage crisis when homes were foreclosed. They have multiplied in the past decade and now include data storage centers, multiplex theaters, prisons and others.

ACCESSING CAPITAL MARKETS

"What you're seeing as of a couple of years ago is a focus on creativity in the market, and in how real estate can access the capital markets," said Daniel Crate, chairman of Easterly Government Properties Inc., a REIT focusing on FBI offices and other government properties. The REIT went public in February under the ticker symbol DEA. "It's becoming less about the manager and more about the assets."

Nareit no longer uses the term "specialty" in describing these REITs, and considers self-storage REITs its own sector. Self-storage units provided a total return of 31.44% in 2014, according to data

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Silver lining in rising rates

Continued from Page 10

Fed's monetary policy over the past six years.

"One of the things we need to consider is that we have been through an abnormal period for REITs, because for the past several years, they've been treated as income vehicles, just like utility stocks," said David Spika, global investment strategist at GuideStone Funds.

"REITs haven't really been trading based on the underlying cash flow," he added. "A lot of the valuations did get somewhat excessive because of investor demand for income, but as rates rise, those yield-producing asset classes should underperform. And for REITs to perform well going forward, they need to trade more than they have historically, based on the underlying investment properties."

Todd Rosenbluth, director of mutual fund and ETF research at S&P Capital IQ, acknowledged the abnormalities that have encompassed the REIT space as a result of Fed monetary policy. But he said the smart play is to expect REITs and REIT investors to normalize as rates start to adjust higher.

"Higher rates don't directly benefit the REIT space, but if the Fed is raising rates because the economy is improving, a better economy is a tail wind for REITs," Mr. Rosenbluth said. "We don't think people who are already invested in REITs have to steer away from them when rates go higher."

While Mr. Rosenbluth doesn't expect the appetite for REITs to be as strong as it has been over the past few years, when the category became a predictable proxy for bond income, he does subscribe to the case for investors getting back to the basics of REIT value.

"We think the economy is going to strengthen, and we think that's good for shopping centers and malls because rents will go higher," he added. "Investors have gravitated toward REITs because of the low yields out there, but we think REITs will continue to stay in focus even as rates move higher."

INTEREST RATES IMPORTANT

Calvin Schnure, an economist with the National Association of Real Estate Investment Trusts Inc., said the benefits to REITs of rising interest rates are well-documented, even if sometimes overlooked by investors.

"We've seen concern and lots of confusion, but interest rates are important for the REIT market," he said. "Right now, the market is paying more attention to the interest rate issue than to the solid fundamentals underpinning REITs. It's true that some investors have become attracted to REITs for the income, but going forward with rising occupancy rates, rents and property values, REITs will continue to provide income."

ISTOCK

"A better economy is a tail wind for REITs."

Todd Rosenbluth
Director of mutual fund and ETF research
S&P Capital IQ

He cited 16 periods since 1995 during which interest rates rose significantly, noting that REITs were positive for 12 of those periods.

Mr. DiSano also studied the performance of REITs during recent periods of rising rates and found that REITs have held up quite well.

"If rates are rising because the economy is improving, that's different than if you're Greece and rates are rising because nobody wants to lend you money," he said.

RISING YIELDS

Like Mr. Schnure, Mr. DiSano pointed out that the market might have an initial reaction to a Fed hike of short-term rates, but it is the rising yields of longer-term bonds that tend to affect REITs.

With that in mind, Mr. DiSano measured large-cap and small-cap REIT category returns against the six most recent periods that saw the yield on the 10-year Treasury bond gain 100 basis points or more.

The most recent period, from June 11, 2012 through Sept. 6, 2013, during which the 10-year Treasury yield gained 135 basis points, large-cap REITs, as measured by the Vanguard REIT ETF (VNQ) gained 4.9%.

Over that same period, small-cap REITs, represented by IQ US Small Cap Real Estate ETF (ROOF), gained 23.9%.

During the period of Dec. 18, 2008 through June 10, 2009 when the 10-year yield jumped 187 basis points, the large-cap REITs fell by 17.2%, while the small-cap counterpart gained 33.6%.

But during the period of June 7, 2005 through June 28, 2006 when the 10-year yield gained 135 basis points large-cap REITs gained 12.4%, and small-cap REITs lost 2.6%.

"I think the message here is that you want to stay diversified when it comes to REITs," said Mr. DiSano. "There will be some volatility associated with a rate hike, but the point is, there seems to be some prevailing misperception that REITs don't do well in a rising-rate environment."

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Specialty REITs doing well

Continued from Page 14
from Nareit.

The Dow Jones U.S. Specialty REITs Index also performed well last year, growing 19.58%. The index is up about 60% in the past five years.

"The industry has evolved to provide specialized structures to house specific elements of the U.S. economy," Mr. Kuykendall said. "Consistently, over long periods of time, it has outperformed the S&P 500."

Some advisers, however, worry that the good times can't last. For Mr. Rolph, some of the companies are still too specialized. Many of the REITs have low trading volume, which means that if a big investor is spooked or exits its position, it could cause a sudden drop in value for that REIT. That's a risk conservative investors who are looking for bond alternatives might not be able to stomach, Mr. Rolph said.

"If ... you get a liquidity crunch, you're going to have big gaps [on the way] down in the pricing."

Duncan Rolph
Managing director
Miracle Mile Advisors

"It's a very, very thin asset class," he warned. "There's not a whole lot of depth to this market, so if things go bad and you get a liquidity crunch, you're going to have big gaps [on the way] down in the pricing."

The other concern is that because they are so specialized, niche REITS have a high level of risk inherent in the specific industry they represent, Mr. Rolph said. New and unpredictable regulations on cellphone companies, for example, could quickly alter the value of a cellphone tower REIT, he said.

"You have to be careful when you look at the ways in which you can introduce meaningful risk," Mr. Rolph said. "When you're an investment adviser talking about replacing bond income or at least a portion of it with this, then you don't want this to be as volatile."

Mr. Crate, whose government properties REIT has a daily trading volume of about 4,300 shares, said volume is low mainly because the REIT is not well-known, having just recently gone public. On the flip side, the low volumes mean investors have more to gain if interest grows in the stock, he said.

"Bigger is not always better," Mr. Crate said. "As people recognize value and the businesses grow, there's greater opportunity out there for appreciation."

Investors must understand the fundamental business they are buying into, and they need to research the manager, Mr. Crate said.

"It's hard to have transparency as to the fundamentals that will change the price of the real estate," he said. "You have to have a lot of trust in the manager."

Meanwhile, specialty REITS remain in limbo as investors wait to see what will happen to the real estate market when the Federal Reserve raises interest rates. As of the end of June, many specialty REITS that had seen dramatic growth in the past five years were down about 8% to 12% from their 52-week highs.

"In a moderately rising rate environment, they're going to do OK," Mr. Rolph predicted. "Probably not great, probably not bad."

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Now playing: Multiplex theaters are among the properties raising investor money through the REIT structure.

ISTOCK

Index funds vulnerable to 'front-running'

By Jeff Benjamin

As asset management firms scratch for every possible edge in the dirt-cheap world of indexed investing, some passive strategies are becoming more active than others.

Consider the slightly varied year-to-date performance of three popular ETFs tracking the S&P 500, which is up 1.54%. The $170.1 billion SPDR S&P 500 ETF (SPY) is up 1.51%, the $32.7 billion Vanguard S&P 500 ETF (VOO) is up 1.61% and the $68.3 billion iShares Core S&P 500 ETF (IVV) is up 1.62%.

"The differences could just be a matter of how they're managing the stocks coming in and out of the index, or how they're managing the cash that leaves the fund, but if they're doing anything else they're affecting the tracking error and that's not what they're being paid to do," said Paul Schatz, president of Heritage Capital.

$4.3B
Front-running's projected annual impact on index funds.

While the performance variation is subtle and something Mr. Schatz acknowledges most investors probably don't notice or care much about, it does reflect a subjective influence on what is supposed to be a strict passively managed strategy.

GAMING THE MARKET

What some analysts are noticing is renewed interest in an old strategy of gaming the market by investing in stocks just before they are added to popular indexes such as the S&P 500.

The tactic in some ways resembles illegal front-running, but it's perfectly legal. As a short-term trading strategy, it could be employed by anybody with a basic brokerage account, but Theodore Feight, owner of Creative Financial Design, warns it doesn't always work.

"The price of the stock could get a big up and then fall back down before the date the index is scheduled to add it," he said. "If you're not one of the first ones to buy, you could lose money doing it."

As the popularity of index investing soars, the emergence of index front-running raises fundamental questions about so-called passive investment strategies. By one estimate, buying into stocks as they're being added to an index — rather than ahead of time — gouges owners of funds tracking the S&P 500 to the tune of $4.3 billion a year, a sum that can double or even triple the cost of such investments.

Over the course of a year, front-running of stocks going into and coming out of indexes costs investors in S&P 500 tracker funds at least 20 basis points, according to research published last year by Winton Capital Management Ltd.

A 2008 study by Antti Petjusto, now a money manager at BlackRock Inc., estimated the impact could boost the expense of owning an index fund by as much as 28 basis points.

While that might not sound like a lot, the added cost can look huge when compared to the handful of basis points most of the index funds charge.

"The moment you say index, you're telling the world you're going to be trading on this particular day," said Eduardo Repetto, co-chief executive officer at Dimensional Fund Advisors. "If you have zero flexibility when you trade, it's going to cost you money."

TELEGRAPHING CHANGES

It might be tempting to blame savvy Wall Street types for taking advantage of mom-and-pop investors, but one of the big reasons front-running exists is because providers of popular benchmarks such as the S&P 500 usually telegraph changes ahead of time.

Another is the pressure that passive fund managers face to track benchmarks as closely as possible, even if it means sacrificing potential returns.

Some fund companies are working to combat the problem. Managers at The Vanguard Group Inc., which oversees $3 trillion, "mitigate a good portion" of the risk by gradually building positions over time in stocks that are scheduled to be added, said Doug Yones, Vanguard's head of domestic equity indexing and ETF product management.

"It just comes down to being smart with your trades," he said. "It's a big enough deal that index managers are aware and spend time and energy making sure there isn't an impact."

For its part, Standard & Poor's said it doesn't dictate when index funds buy, and its rebalancing process ensures everyone gets the same information at the same time.

"We don't require them to trade in a certain way," said David Blitzer, chairman of the index committee at S&P Dow Jones Indices. "That's their business, not ours."

Mr. Repetto said Dimensional avoids buying stocks immediately before they go into an index. Instead, fund managers purchase them earlier or after the fact.

While the strategy increases an index fund's divergence from a benchmark's performance, it can help fund managers boost performance, which was the issue raised by Mr. Schatz.

Michael Rawson, an analyst at Morningstar Inc., said the impact of front-running is minimized in index funds that buy the entire market, such as the Vanguard Total Stock Market Index (VTSAX).

This story was supplemented with reporting from Bloomberg News.

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Barclays advisers sniff at Stifel, move to Merrill

By Mason Braswell

Fifteen advisers, including most recently a team in Texas managing $750 million in assets, fled Barclays PLC's U.S. wealth management group in the last month to join Bank of America Merrill Lynch following the announcement that the Barclays unit was being acquired by the lesser known Stifel Financial Corp.

Recruiters said the flight to Merrill is a testament to the challenges Stifel faces as it tries to hold onto the rest of Barclays' brokers and make inroads into the highly competitive market for ultrawealthy clients.

With the addition of the team in Texas, Merrill Lynch has picked up close to 10% of the 180 advisers who were at Barclays at the time the deal with Stifel was announced June 8. The Texas group, which includes three advisers, managed approximately $250 million per adviser, well above the average of $189 million per adviser for the Barclays unit.

"Those are the cherries that they want to have," said Howard Diamond, a managing director at Diamond Consultants, a placement firm for financial advisers. "When the Stifel deal was announced, advisers weighed the retention package that they'd get from Stifel against a huge upfront package they'd get from Merrill Lynch. So if they're going to go to a different firm, they might as well go where they want and be paid a lot more money."

300% OF REVENUE

Mr. Diamond estimated that Merrill Lynch could have offered over 300% of the advisers' annual revenue in the form of upfront and back-end bonuses tied to performance goals. Stifel's retention deal generally has been around 150% for advisers, Mr. Diamond and other recruiters said. Other firms are also competing for Barclays advisers, including Morgan Stanley Wealth Management, Wells Fargo Advisors and Raymond James & Associates, Mr. Diamond said.

A spokeswoman for Merrill Lynch, Susan Atran, said the firm did not discuss specific numbers. Brian Spellecy, a spokesman for Stifel, declined to comment.

For Stifel, the Barclays acquisition represents an important moment as it could help the once-regional firm secure a foothold in the ultrahigh-net-worth channel, analysts said.

Stifel advisers manage approximately $89 million on average, compared with the $189 million per adviser at Barclays and $159 million at Merrill Lynch, according to a report from Credit Suisse analyst Christian Bolu.

COMPLICATED BUSINESS

But the Barclays addition could be complicated by a number of factors, including Stifel's more regional brand and whether or not the firm can service some of the Barclays advisers' more complicated businesses. That would include alternative investments, syndicate business and equity underwriting products, Mr. Bolu wrote in the report.

"This could mean significant revenue attrition post-merger as we do not believe Stifel has the depth of underwriting and alternatives capabilities of Barclays," Mr. Bolu said.

It is not clear whether these were concerns of the team in Texas. The advisers were not available for comment, according to Ms. Atran.

The three, Barry Schneider, Cris Bera and Chris Dewhurst, joined Merrill's Private Banking and Investment Group, a division of about 150 teams focused almost exclusively on clients with $10 million or more in assets.

Ron Edde, who places financial advisers through his firm Millennium Career Advisors, said another factor for a large team he is working with on the West Coast is how clients will respond to the Stifel name.

'PANACHE' OF THE NAME

"I think a lot of people who are with Barclays were there because of the panache that the name carried," Mr. Edde said. "While Stifel is a good firm, it's not exactly a household name if you walk down the street and ask 100 people."

Still, the number of defections will not hurt Stifel financially. The deal was valued at around $150 million to $250 million, but Stifel will only pay for the assets that they retain, recruiters said.

Mr. Diamond said that despite the most recent move to Merrill, a lot of advisers were happy with Stifel. Most of those who are moving now were those who were already planning on going somewhere else before the deal, he said.

"Stifel is a good firm, and many Barclays advisers are going to be very happy there," Mr. Diamond said. "They like the regional name. They like being paid 150% and being able to stay put."

He estimated that if Stifel can manage to hang onto around 70% of the advisers from Barclays, then they would have gotten a good deal.

"That would be a great win for Stifel," he said.

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2nd QUARTER RECAP

Wirehouses open their doors to those who left

Taboo against hiring advisers who jumped to competitors erodes

By Mason Braswell

It's homecoming season for some wirehouse advisers.

As head count continues to decline and competition for the assets of veteran advisers grows, firms like Bank of America Merrill Lynch are now more comfortable extending employment offers and bonuses to what once was considered an off-limits group: advisers who had left the firm to join a competitor.

ON THE WEB
Track the latest adviser moves and recruiting activity at InvestmentNews.com/aotm

"The competition for top advisers has gotten more fierce," said Mindy Diamond, a recruiter with Diamond Consultants Inc. "Where people are going if they choose to leave is becoming more fractured, so the firms need to be more open-minded and flexible about who they are willing to consider."

'A PR BENEFIT'

Ms. Diamond and other recruiters and former wirehouse managers said that while it's still not a common practice, they are seeing it happen more often and noticing firms are changing their tone toward ex-advisers. Hiring returning advisers has now become a selling point for some firms, according to Danny Sarch, a recruiter with Leitner Sarch Ltd.

> "IT ALL DEPENDS on the individual case, if they left on relatively good terms."
>
> **Danny Sarch**
> Recruiter, Leitner Sarch

"It's desperation for firms … as well as the fact that [the advisers] can say they thought the grass was greener, then they came back," Mr. Sarch said. "There's a PR benefit."

Merrill Lynch, for example, made two announcements this past quarter spotlighting a manager and adviser who had left to join competitor firms and then returned.

"Merrill Lynch is my home," Michael Casey, who is a director of the firm's Nevada complex, said in a statement announcing his move. "I like the people and like their spirit of doing what is best for their client."

Mr. Casey left in 2009 to work at Wells Fargo Advisors and then Morgan Stanley Wealth Management before returning in April.

Last month, Merrill Lynch brought back a team in Baton Rouge, La., with $350 million in assets that had left in 2008 to join UBS Wealth Management Americas.

"Merrill Lynch is pleased to have The David/Robertson Team rejoin our company," Jeremy Silvas, a manager for the Louisiana and Mississippi market, said in a statement.

"We're very glad to be back at Merrill Lynch and believe the breadth and depth of their services will help us serve our clients well," the lead adviser, Chad David, said in the statement.

A spokeswoman for Merrill Lynch, Susan Atran, declined to comment beyond writing in an email that the firm's platform was "resonating with advisers."

Other firms preferred to stay quiet on the issue. A spokesman for UBS Wealth Management, Gregg Rosenberg, declined to comment, as did a Morgan Stanley spokeswoman, Christy Jockle, and a spokeswoman for Wells Fargo Advisors, Rachelle Rowe.

"No other firms are willing to blatantly admit that they are doing it, but they are," a former UBS branch manager who left the firm last year said on the condition of anonymity because he did not have permission from his current firm to speak publicly.

"Hiring somebody back after they jumped to another firm used to be a no-go," he added. "As recruiting pressure increased and the number of firms dwindled, senior management abandoned the principle and went with the practical."

EIGHT TO 10 YEARS

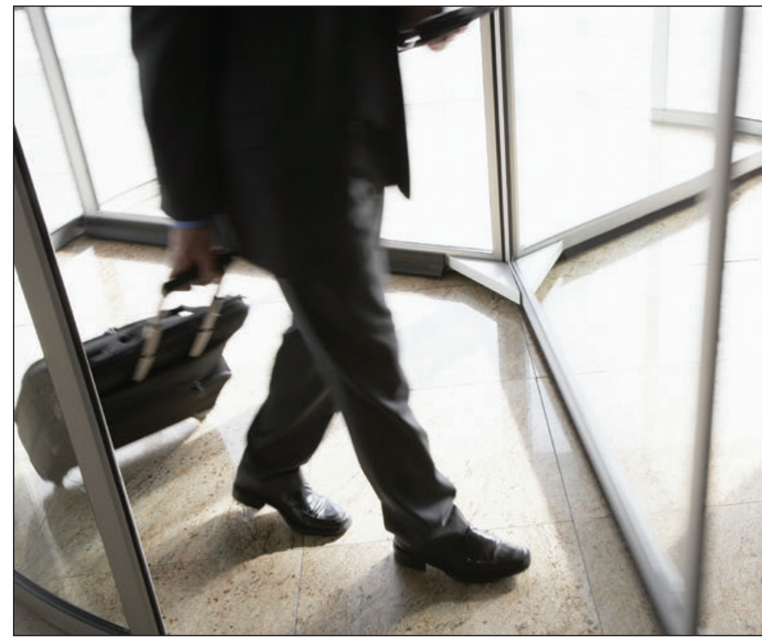
Most managers avoided hiring former employees, and firms had unofficial policies that advisers had to be gone for eight to 10 years, the average length of a recruiting contract, before they could come back, recruiters and former managers said. Even after 10 years, most managers shied away from the practice for fear of inciting blowback from advisers in the branch.

"We couldn't even look at the guy," said Tony Sirianni, a former wirehouse manager with Morgan Stanley Smith Barney who now runs an eponymous marketing firm. "What does it say to the guy sitting there who has been loyal?"

It's also hard to justify to clients, Ms. Diamond said.

"For an adviser to say to his client, 'I left there for a good reason several years ago and now I'm coming back,' it sort of looks like you have your tail between your legs," she said.

Mr. Sirianni said that it also is not a good growth strategy for firms



ISTOCK

because it doesn't result in a net increase in head count.

"It's a prisoner exchange," he said. "They have to keep paying more and more money to get these guys to come over, and it's a shrinking pool."

Ron Edde, founder of the recruiting firm Millennium Career Advisors, said he found that among Merrill Lynch's 14,000 advisers, he could identify 140 current Merrill advisers who had left and worked at one other firm before coming back, according to a proprietary database he maintains using publicly available registration data. UBS, which has about 7,000 advisers, had around 20 such examples, he said.

MOVING BACK HOME

Mr. Edde admitted the calculations are not exhaustive, but said it resonated with what he was seeing in practice.

"There's some increased activity in that area," he said. "It's kind of like someone who lives in a community for a long time then moves away because they want to see the world, and then they move back home."

Mr. Sarch noted, however, that it makes sense for some advisers to come back now, particularly since many may have jumped ship in 2008 and 2009, when the industry was going through rapid consolidation. Since then, senior leadership and platforms have changed at all the firms.

"It's not hard to be cynical about it, that they left for the money and came back for the money," Mr. Sarch said. "But I think the truth is somewhere in the middle. It all depends on the individual case if they left on relatively good terms and they can justify the reason at the time."

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2nd Quarter

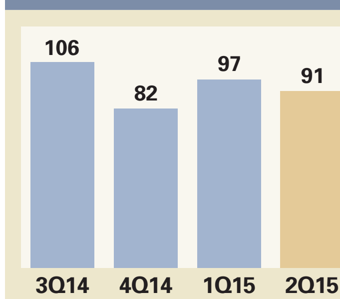
Top-ranked firms by net change in AUM

	AUM ($M)			# of teams	
	Gained	Lost	Net change	Gained	Lost
Raymond James	$4,740	$199	**$4,541**	6	2
RBC Wealth Management	$2,274	N/A	**$2,274**	6	1
Bank of America Merrill Lynch	$3,625	$2,782	**$843**	16	7
Frontier Wealth Management	$750	$0	**$750**	1	0
Wells Fargo Advisors	$2,193	$1,478	**$715**	6	11

Lowest-ranked firms by net change in AUM

	AUM ($M)			# of teams	
	Gained	Lost	Net change	Gained	Lost
The Fiduciary Group	$0	$600	**-$600**	0	1
JPMorgan Chase & Co.	$0	$926	**-$926**	0	4
Barclays	$0	$2,300	**-$2,300**	0	7
Morgan Stanley Wealth Mgmt	$1,785	$5,607	**-$3,822**	6	19
UBS Financial Services	$160	$3,989	**-$3,829**	6	13

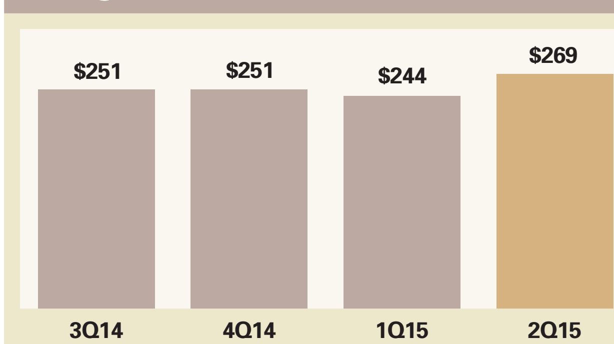
Total teams moving



Top moves in the second quarter

	Name of advisers	Adviser AUM ($M)	Firm adviser is leaving	Firm adviser is joining	Location of adviser
1	Don d'Adesky, W. Kristopher Lemke, Matthew Cicero, Jose Cabrera Sr., Kevin Gourrier, Ryan Weber	$2,400	Morgan Stanley Wealth Management	Raymond James	Boca Raton, FL
2	Greg Fullmer, Daniel Hawkins, Douglas Dyakon	$1,300	UBS Financial Services	Morgan Stanley Wealth Management	Los Angeles
3	Dodd Newton Koeckert, Nicholas H. Anger	$1,200	Bank of America Merrill Lynch	RBC Wealth Management	Stamford, CT
4	Barry Schneider, Cris Bera, Chris Dewhurst	$750	Barclays	Bank of America Merrill Lynch	Houston
5	David K. Neal, John Jenkins, Chace Dillon, Michele Horton, Tracy Ruddle, Deborah Farnham	$750	UBS Financial Services	Frontier Wealth Management	Wichita, KS

Average AUM size of moves ($M)



CHARTS: GERARDO TABONES

Source: *InvestmentNews* Data

To submit an adviser move, complete the form at data.InvestmentNews.com/aotm

FIDUCIARY CORNER

Blaine F. Aikin

It's not about robo-rocket science

Investors want a combination of digital help and personal advice, but you have to lead the way

"Investors tend to see financial advisers and digital investment tools as complementary."

That innocuous statement from a May 2015 Wells Fargo/Gallup survey packs quite a bit of power when it comes to how advisers should be thinking about bringing digital and personal advice together in their practices. Investors don't want to choose between digital or personal advice. They want both.

In fact, the survey found that only 9% of investors want to get their advice entirely online or digitally, while 23% prefer to rely exclusively on a personal financial adviser. More than two-thirds of investors want both. While there are differences between younger and older investors, both groups strongly favor using both personal and digital advice. Moreover, the desire for a strong client-adviser relationship dominates the allure of digital advice across age groups.

Advisers who can successfully incorporate digital investment tools into a client-friendly customer experience will surely stand out in the crowded market of advisory services. To construct a successful hybrid model, advisers should be thinking about the human and computer interfaces they have with clients in at least four key aspects: access, consistency, literacy and trust.

KEY ASPECTS

Access involves what tools and people the advisory firm will make available to clients. The Wells Fargo/Gallup survey found that the top three digital investing tools of interest to investors are platforms that:

1. Help the client review and make changes to existing investment accounts.
2. Provide long-term planning assistance.
3. Perform retirement calculations.

All three of these types of tools were found to be of interest to at least 50% of all respondents. A tool described as providing "an automated investment advisory service that uses computer-based portfolio management" (the main feature of most robo-platforms) was of interest to one-third of the respondents. It is noteworthy that "household budgeting tools" had a higher interest rating. These results suggest that advisers should step back from the industry fixation on digital portfolio management capabilities to think about what digital service offerings investors may find most useful.

The survey found that having a strong relationship with an adviser is much more important for most people than having access to state-of-the-art tools. Sophisticated analysis doesn't necessarily resonate with clients unless it is delivered by trustworthy and competent professionals who are also skilled communicators capable of bridging the gap between humans and technology.

There is a whole field of research dealing with human-computer interaction that is based on the premise that, unlike human interactions with mechanical tools, human interactions with computers are so varied that they are much like human-to-human dialogues. That notion helps bring into focus the need for consistency between digital and personal services.

Literacy becomes a consideration because the extent to which a tool will be of interest and helpful to an investor depends in large part on that person's financial literacy.

CLIENTS WANT TOOLS

This may help explain why in the Gallup survey relatively straightforward tools that provide account access, retirement calculators and household budgeting capabilities were of interest to more investors than complex applications like portfolio management.

For archived columns, go to InvestmentNews.com/fiduciarycorner

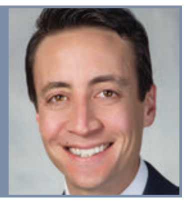
A particularly interesting survey finding is that online financial planning education models were fourth on the highest interest list. That indicates people recognize that they are limited by their level of financial literacy and want to improve it. If an adviser can provide fundamental financial education that is digestible and explains how the tools and advice offered by the adviser work for the investor's benefit, it is likely that the client-adviser relationship will be strengthened even though the adviser may spend less time with the client.

Finally, trust is at the heart of all client relationships. Trust involves confidence that, regardless of how the advice is delivered, it will be objective, serve the client's best interests and be based on sound professional practices. Trust is also grounded in the client's expectation that their personal information is secure. Services delivered digitally must be built with these core fiduciary principles embedded in the technical specifications, just as advisers must hardwire fiduciary principles in their interactions with clients.

Blaine F. Aikin is president and chief executive of fi360 Inc.

INVESTMENT STRATEGIES

Josh Yafa



The ladder beats the barbell and the bullet

In rising-rate environments, laddered bond portfolios benefit from reinvestment opportunities

As the Federal Reserve prepares to normalize interest rates, fixed-income investors are finally facing the cycle they have feared for the better part of a decade. Here we examine the impact of rising-rate environments on various fixed-income investment strategies as measured by periods in which both of the following occurred: the Fed was hiking the federal funds rate and the bond market reacted strongly, which we define as an increase in 10-year U.S. Treasury yields of greater than 100 basis points over the course of 12 months.

Predicting the path of the fed funds rate is difficult, given an unwieldy combination of variables. After each meeting, the Fed governors publish their so-called "Dot Plot," a forward-looking projection of policy rates assuming normal economic conditions. Over the past several years, these predictions have proven to be inaccurate. Even the Fed, arguably in possession of the best real-time macroeconomic data available, is frequently incorrect with its forecasts. Keep in mind that these are the very people who set the fed funds rate.

INVESTOR SCRUTINY

One could expect that "the market" usually gets it right. This seems logical given the intense investor scrutiny and sheer amount of global capital riding on the back of policy rates. But fed funds futures also miss the mark, expecting more-rapid rate hikes than actually occurred.

Investors must decide whether to trust in manager skill to overcome the problem of increasing interest rates by outsmarting the set of circumstances laid out above. Or, perhaps an alternative solution to the problem of rising rates could come from a directional rather than period-specific investment, and one that balances the synchronized and ever-present risks of duration, reinvestment and liquidity.

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Laddering involves building a portfolio of bonds with staggered maturities so that a portion of the portfolio will mature each year. To maintain the ladder, money that comes in from currently maturing bonds is reinvested in bonds with longer maturities.

RISING-RATE SCENARIOS

Though laddered bond portfolios can be beneficial in many interest rate environments, we will specifically focus on rising-rate scenarios. Generally speaking, over long periods, laddered strategies tend to perform well against barbell or bullet bond strategies. This is principally because they can capture price appreciation as bonds roll down the curve and their remaining life shortens. In a normal (upward-sloping) yield curve environment, laddered portfolios benefit from constantly reinvesting principal from maturing bonds into new higher-yielding bonds.

Since 1990, there have been four discrete periods during which the Fed raised its federal funds rate and the bond market reacted strongly:

- February 1994-January 1995
- February 1999-January 2000
- June 2003-May 2004
- July 2005-June 2006

We measured returns for three hypothetical bond strategies — ladder, barbell, and bullet — across these time periods using a three-year holding period. A reasonable time horizon is essential for judging the performance of a bond strategy, given the offsetting effects of income and duration. The start/end points for the three-year return streams begin one year prior to the start of the 10-year U.S. Treasury yield increase, and end one year after the conclusion of the 12-month U.S. Treasury measurement period.

BEST STRATEGY

Taxable laddered portfolios, as measured by the Barclays Intermediate U.S. Aggregate Index, outperformed the barbell and bullet strategies across all time periods. Municipal laddered portfolios, represented by the Bank of America Merrill Lynch 1-12 Year Municipal Index, outperformed the bullet strategy in all time periods, and outperformed the barbell strategy in all but one time period, with July 2004-June 2007 being the lone exception.

It appears that across almost all time periods examined, the laddered portfolios' ability to benefit from reinvestment opportunities in an increasing-interest-rate environment, mitigating interest-rate risk, led to outperformance. The strategy was able to generate robust annualized positive returns during each time period. Thus, bonds can produce absolute positive returns even during periods of increasing interest rates. Investors can still hold bonds for their traditional asset allocation role as ballast for an overall portfolio and a counterbalance to riskier assets, and yet not suffer the feared drawdown in a typical rising-rate scenario.

Josh Yafa is a client portfolio manager at Thornburg Investment Management.

RETIREMENT WATCH

Jamie Hopkins

Getting Gen Yers to take some risk

Young investors' conservative investing mindset will work against them in saving for retirement

Generation Y (age 18-34) is very concerned about the future of Social Security and has a strong desire for other sources of guaranteed income, such as annuities, to provide secure monthly income in retirement.

That's according to a new study released by TIAA-CREF that included seven questions on retirement. The survey polled roughly 1,000 respondents, age 18 and older.

The survey showed that Gen Y has taken on a pragmatic view of retirement, realistic assumptions about their longevity and a desire for less risky investments.

"Gen Y tends to be more guarded and cautious with their retirement savings but it is surprising how many want to put money into lifetime income sources," said Amy Podzius, director of TIAA-CREF's field consulting group.

While Gen Y takes a conservative view of their retirement security, some areas raised great concern. More than 30% of Gen Y respondents reported that they were not saving anything for retirement. The percentage of nonsavers was much higher for Gen Y than for other age groups. The lack of saving is a real problem, especially because Gen Y does not expect to rely upon Social Security at the same level as past generations. For instance, only 56% of Gen Y respondents stated they are counting on Social Security to provide income in their retirement, compared with 76% of 35- to 44-year-olds and 73% of 45- to 54-year-olds.

FEAR OF RISK

Perhaps most important is what Gen Y wants for retirement. Nearly 34% of Gen Y respondents stated their primary goal for retirement would be to ensure the safety of their savings regardless of what happens in the market. Gen Y appears to be more concerned about market risk than previous generations, with a strong desire for guaranteed monthly income in retirement. Nearly 42% of Gen Y respondents stated their primary retirement goal is to have sufficient guaranteed monthly income to cover their living expenses in retirement.

This desire to avoid market risk with guaranteed income should be welcome news for any annuity provider. Of any age group in the survey, Gen Y demonstrated the largest desire to purchase an annuity, with nearly 14% stating they had already purchased an annuity and 16% stating they plan to purchase an annuity before retirement. While only 26% of Gen Y respondents stated being familiar with annuities, an astonishing 61% of Gen Y respondents stated they would be willing to commit a portion of their retirement savings that would allow them to receive a monthly income for life.

While negative sentiments toward annuities exist, expanded company product offerings, more research demonstrating the strategic uses of annuities and increased government support have solidified a place for annuities in retirement planning. A deferred-income annuity, which pays lifetime income starting later in life, can be a great retirement income planning tool for Gen Y. New government regulations have furthered the applicability of annuities in retirement planning by allowing for 401(k) and IRA participants to buy a longevity annuity, often referred to as a QLAC, using funds from their retirement plan.

For archived columns, go to InvestmentNews.com/retirementwatch

According to David Littell, a professor of retirement at The American College, "Diverting a portion of savings to retirement income through the purchase of a deferred-income annuity could meet Gen Y's desire for both guaranteed income and avoidance of risk. But this leads to the difficult questions of what is the right age to start buying income and how much of savings should be devoted to an annuity."

The lack of savings is troubling for Gen Y, but when combined with a conservative investment approach, it could spell disaster for meeting their future financial goals. Gen Y needs specialized help to utilize the guaranteed income solutions they want to incorporate into their retirement income plans.

FINANCIAL EDUCATION

"When dealing with Gen Y clients, it is not about leading with retirement planning," Ms. Podzius said. "Instead, it is about leading with holistic planning and education. I can't think of a Gen Y client who didn't change their thought process when they learned more about risk, mutual funds and other financial topics." Financial education is the key to helping clients create a secure retirement, and Gen Y is no exception.

Jamie Hopkins is a professor of tax in The American College's Retirement Income Certified Professional program. Follow him on Twitter @jamiehopkins521.

SEC official warns against diluting fiduciary duty

Investor advocate says harmonization could water down rules

By Mark Schoeff Jr.

A Securities and Exchange Commission official whose job is to represent retail investors has warned the agency not to water down current investment advice standards as it considers a rule to raise the bar for brokers.

SEC Investor Advocate Rick A. Fleming said June 30 that as the SEC considers a uniform fiduciary-duty rule, parameters mandated by the Dodd-Frank financial reform law could result in a weaker standard than the one that now applies to investment advisers.

"An ill-advised rule could be worse than no rule at all," Mr. Fleming wrote in a report to Congress. "We will fight to avoid these outcomes and to encourage rule makings that are as strong as possible for investors."

Advisers must act in the best interests of their clients, or as fiduciaries. Brokers must recommend investment products that are suitable, giving brokers leeway to put clients in high-fee products when lower costs ones would work.

Under Dodd-Frank, the SEC has the authority to propose a best-interests standard for all retail investment advice. But the law also stipulates that the standard must allow for sales-based compensation, the sale of proprietary products and sales from a limited menu of products, as well as relieve brokers from a continuing duty of care for clients.

If the SEC follows that prescription, it won't benefit investors, Mr. Fleming asserted in his report.

He argued that harmonizing adviser and broker rules could "dilute the existing standard for investment advisers" and that a "poorly designed" rule could mislead investors into thinking they're receiving a fiduciary-level of protection.

Promoting the fiduciary-duty rule is one of eight items on Mr. Fleming's policy agenda for fiscal 2016, which begins Oct. 1. The June 30 report to Congress on his office's objectives is the second he's filed since he was appointed in February 2014. It represents the first time he has made fiduciary duty a priority.

ANOTHER HURDLE FOR WHITE

Mr. Fleming's stance gives SEC Chairwoman Mary Jo White one more person to try to assuage, as she begins work on a rule. In March, she said she supports a fiduciary standard but acknowledged in congressional testimony that she may not be able to persuade at least two of the four other SEC members to join her.

Rick Fleming: If SEC follows Dodd-Frank, it could weaken fiduciary standard for advisers.

While the SEC struggles with a fiduciary rule, the Labor Department has proposed a best-interests standard for brokers working with retirement accounts.

Mr. Fleming suggested that if the SEC follows Dodd-Frank in its own rule making, the prohibition against continuing care would produce a rule that is weaker than current rules pertaining to retirement accounts.

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Regulator appeals own judge in fund fee case

By Trevor Hunnicutt

The Securities and Exchange Commission is fighting a decision by an in-house agency judge to dismiss charges accusing two financial advisers of not informing clients they were paid by Fidelity Investments to sell certain mutual funds.

In a filing posted on the SEC website June 29, the agency argued that an SEC administrative law judge's June 4 decision in favor of the Houston-based financial-advice firm Robare Group set a troubling precedent.

"It shifts the burden of fully disclosing a conflict of interest from an investment adviser, who has a fiduciary duty to and a relationship with its clients, to a compliance consultant," the SEC said in the appeal. "As a practical matter, such a rule would improperly mean that an investment adviser may be excused from securities violations so long as he retains a compliance consultant who does not affirmatively object to a particular disclosure."

> "IT SHIFTS THE BURDEN of fully disclosing a conflict of interest from an investment adviser, who has a fiduciary duty to ... its clients, to a compliance consultant."
>
> SEC appeal

FEW ALJ LOSSES

The judge's decision dealt the SEC one of very few losses it's seen in often-criticized, court-like proceedings it administers itself.

The 29-page appeal seeks a review of the judge's decision by the full five-member commission.

The case underscores a controversial practice by custodians that pay affiliated, independent advice firms to sell certain third-party funds.

Since 2004, the Robare Group has been enrolled in a program in which Fidelity pays a share of the revenue it earns on some third-party mutual fund sales to the advisers who sell the funds. The funds also are made available to the advisers without transaction fees.

Transaction-free platforms are popular with advisers and lucrative for custodians, who receive payments from fund companies to participate. Custodians sometimes pay financial advisers who participate.

'ADMINISTRATIVE SERVICES'

But Fidelity does not describe the payments as a commission; instead it calls them compensation for "shareholder administrative services." That's despite the fact that advisers provide the exact same services to other funds not enrolled in the program.

Robare did not always disclose those payments in its Form ADV. Separately, it provided to new clients a Fidelity document that more explicitly acknowledged the payments. But Fidelity determined the firm's disclosures were inadequate and told Robare to update its filings in 2011.

While the advisers argued that the disclosures of the Fidelity payments were not "material," administrative law judge James E. Grimes disagreed.

But he said the evidence didn't suggest the advisers were acting fraudulently. He noted that a high percentage of their clients' assets were in funds not offering revenue-sharing. Robare manages $160 million for clients.

In a 44-page decision, Mr. Grimes wrote that the owners, advisers Mark L. Robare and his son-in-law Jack L. Jones Jr., "came across as honest and committed to meeting their disclosure requirements," including relying on their broker-dealer and compliance advisers.

The judge said testimony during the proceedings in February showed that advisers "operate in a difficult environment" for compliance with securities law. The ruling suggested that advisers in many cases are right to rely on advice from compliance specialists, including that from broker-dealers.

ISTOCK BLOOMBERG COMPOSITE

"Judge Grimes made so many credibility determinations in favor of my clients they might be difficult to reverse," said Alan M. Wolper, a lawyer at Ulmer & Berne who represents the advisers. "It is my hope that the commission will recognize that."

NO SETTLEMENT

The advisers decided not to settle the case because they "couldn't stomach" admitting that they committed fraud, their lawyer has said.

A Fidelity spokeswoman, Nicole Abbott, did not respond to a request for comment.

An appeal in this matter will now be reviewed by the five SEC commissioners, who can decide to reverse the judge's decision. If the commissioners' decision is appealed, the case would move to a more traditional venue, a federal appeals court.

The agency has faced criticism over its administrative law court hearings from politicians and securities lawyers, as well as former SEC commissioners and staff members. Those critics have argued the increasing practice of relying on its own judges comes at a cost to defendants, who lose cases more often during in-house proceedings than in cases taken to trial.

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Finra raked in revenue in '14, doubling fines

$129M in net income, up from $1.7M in '13

By Mark Schoeff Jr.

Increased revenue, including a doubling of money raised through fines, helped Finra significantly increase net income in 2014, according to the regulator's annual report.

The Financial Industry Regulatory Authority Inc., an industry-funded organization, obtained $129 million in net income in 2014, a sharp increase from the $1.7 million it reported in 2013. Revenue increased to $996.6 million, from $900.7 million, while expenses dropped to $964.8 million from $998.9 million, in part due to a voluntary retirement plan.

> **7**
> Number of Finra execs who earned more than $1M last year

"Financially, 2014 was a strong year for Finra due primarily to an increase in revenue and our continued efforts to control costs," Finra chairman and chief executive Richard G. Ketchum wrote in a letter accompanying the annual report, released June 29.

Thanks to its financial results, Finra distributed a $20 million "discretionary rebate" to member firms for the second year in a row. In addition, each Finra member also received a $1,200 rebate to offset its annual gross-income assessment fee and a rebate based on its prorated share of regulatory fees.

RETIREMENT PLAN

The organization was able to reduce its expenses thanks to a voluntary retirement plan. Finra said that 176 employees retired in 2014 out of a staff of 3,500.

Seven Finra executives earned more than $1 million in compensation in 2014, up from four in 2013. They included Mr. Ketchum ($2.89 million, up from $2.62 million in 2013), Todd Diganci, executive vice president and chief financial officer ($1.29 million, up from $1.24 million), Steven Randich, executive vice president and chief information officer ($1.20 million, up from $514,825 in 2013 when he worked only part of the year); Robert Colby, executive vice president and chief legal officer ($1.17 million, up from $948,420), Susan Axelrod, executive vice president for regulatory operations ($1.10 million, up from $1.01 million), J. Bradley Bennett, executive vice president for enforcement ($1.057 million, down from $1.064) and Thomas Gira, executive vice president for market regulation ($1.02 million, up from $961,898).

Regulatory revenue, which includes trading activity fees, gross income, personnel and branch office assessments, increased to $428.1 million in 2014 from $414.6 million in 2013. Finra attributed the rise to increased trading volumes.

FINES GOT STIFFER

Although the number of monetary sanctions decreased in 2014 to 645 from 754 in 2013, the average fine increased to $205,600 from $80,100 in 2013. Last year, Finra brought 1,397 disciplinary actions against member firms and registered representatives and assessed $132.6 million in fines. In 2013, it levied $60.4 million in fines.

In 2014, the organization barred 481 brokers and 18 firms from the industry while suspending five firms and 705 brokers. It ordered $32.3 million in restitution to harmed investors.

Finra's investments also did well in 2014, rising to $2.08 billion from $1.95 billion in 2013. Finra's portfolio return was 5.8%. Its net investment gain "was primarily driven by the performance of our fixed-income portfolio," Finra wrote in the annual report.

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Nationwide®

How to Identify Opportunities in International Investing

Peter Hill
Chairman and Chief Executive, Bailard Inc.

Bryan Jordan
Deputy Chief Economist with Nationwide Economics

On May 12, Peter Hill, chairman and chief executive of Bailard Inc., and Bryan Jordan, deputy chief economist at Nationwide Insurance, sat down with Matt Ackermann, director of digital content at InvestmentNews, in a recent Portfolio Manager Viewpoints webcast to discuss opportunities in markets outside the United States.

Matt Ackermann | Could we start with your macro market view?

Bryan Jordan | We're nearly six years into the recovery, but a lot of developed and some developing markets have come into this recovery more recently. Since the recovery began, U.S. GDP is up nearly 9%. But Japan has contracted by nearly 1% since the peak in the last cycle, in 2007, and the Italian economy has shrunk by close to 10%. The German economy is up by less than 4%; the French economy up by just over 1%.

A number of these countries experienced double-dip recessions that were largely driven by tighter monetary policy, specifically when the European Central Bank was raising interest rates in 2011. Central banks that were tightening a few years ago are easing, and those economies are in recovery mode.

American influence on the rest of the world has increased because of its GDP growth and the strength of the dollar, which is up nearly 20% year over year. In China, 4.8% of GDP is attributable to exports to the United States. Nearly 10% of the Canadian economy and over 20% of the Mexican economy is accounted for by exports to the U.S. Those economies should benefit.

We have many reasons to be optimistic about near- and intermediate-term performance given what have been the accommodative monetary policies in most big economies. But a number of economies, including Mexico and India, also look attractive long term, with structural drivers like low debt and dependency ratios, high savings rates and relatively young populations.

Ackermann | Can you explain the benefits of your country-first strategy and how it affects the way you build your portfolios?

Peter Hill | It was a temptation a few years ago to think, 'The currency has been taken out of all those European countries. We can just follow stocks around the world and create global portfolios.' And that's not necessarily bad. But the country can have a big influence on markets, on the companies domiciled there, and on their stocks.

For instance, Spain and Germany share a currency but have huge differences in culture and business practice. We like to look for adding two-thirds of our extra value from being in the right place.

We usually invest in 25 or more countries, and which move to the top of the list can be a surprise.

For example, Russia is at the top at the moment because it has stabilized along with oil prices. Pakistan is another surprise. Particularly on the risk side, changes in the country have been toward improvement.

Ackermann | How do you approach country selection?

Hill | We assess countries according to three broad groups of characteristics: value, growth and momentum, and risk. But to properly weight those categories, you must have a picture of the global environment.

One of the best measures is market volatility. When it's low, investors tend to pursue markets that have been doing well. When it rises, people tend to move toward value. If the world is anxious, we want to dial up value countries; when it's calm, we put more emphasis on momentum. We're moving from a calm period to more volatility.

Ackermann | What are some of the best short- and long-term growth areas?

Jordan | We start with core European economies outside of Germany and some that are beginning to show signs of life, like France and Italy. Both were in recession in the first half of last year and both seen increases in leading indicators that would suggest growth is about to pick.

It's important that these countries have engaged in some serious reform measures. France has done a major tax cut and deregulation. Italy enacted labor market reform that will make it easier to hire and fire employees.

Corruption has dogged India for decades, but given recent election results, there's some hope that will diminish.

Ackermann | Talk about some of the areas that are struggling.

Hill | I would be surprised to see ongoing performance from resource-based economies. I prefer the demographic-driven economies of India, China, Indonesia. Some of them should do very well based on increased purchasing power.

Jordan | The Australian economy depends heavily on the Chinese economy, which is slowing, transitioning from an investment- to a consumer-led economy. Australia's leading indicator turned negative recently. And there's the possibility of a housing price bubble in Australia that may leave it vulnerable.

In Brazil, which is resource-dependent and whose economy has been mismanaged for some time, interest rates have pushed higher because of inflation. Though the last election brought some encouraging signs, the country will probably be challenged for some time.

Ackermann | How do you and your team choose your portfolio companies in a particular country?

Hill | It's important to get a portfolio that's representative of the country; we're careful to make sure that we're in all sectors. At the same time, we look at metrics like valuations, earnings quality, growth and momentum, analyst revisions. We then try to pick the best-scoring stocks from our analysis and approach.

We tend not to make sector bets within a country. But by its very nature, if you're a country top-down picker from an investment point of view, you'll end up with a slight bias in the sectors you're in.

Ackermann | What goes into your process when you decide to trim or sell a country within the portfolio?

Jordan | Our primary consideration is a change in the underlying drivers. Has the macro story gone from great to good, or good to fair, or fair to worse?

It's a question of what's happening at the margin. You begin to see early signs of a slowdown or some other problem in an economy that had been doing extremely well. That would lead us to become more negative on something we've liked. The same would be a drive on the upside, when a story with bad news built in becomes a bit better.

We look at markets and economies as very much driven by the flow of money through them. Over the past few years, central banks primarily have been acting to one side — pushing rates lower, conducting QE. These stories have marginally moved further in that same direction.

Over the next couple of years, central banks will begin to tighten and growth rates will start slowing. That's when we'll become more cautious.

Ackermann | Why should we be investing internationally?

Hill | Diversification is a key element — some places overseas are growing more rapidly — and the stronger dollar means those assets are cheaper. Investing internationally spreads risk and allows different opportunities.

Jordan | The non-U.S. economy accounts for nearly 70% of the global economy and over 50% of global market cap. Investors without exposure are missing out on a lot. There are compelling stories. It's a challenge to find them, but they're always out there. ❖

'Greedy' adviser's Ponzi costs him 25 years

By Mason Braswell

A former financial adviser who admitted in December to stealing more than $10 million from about 55 clients in a Ponzi scheme is set to serve 25 years in prison for his fraud.

From around 2007 to 2014, Sean M. Meadows, 42, collected some $13 million through his registered investment adviser Meadows Financial Group. He said he would invest funds in bonds, real estate or other investments and promised 10% returns, according to the original complaint filed in August.

Instead, the money went to pay Mr. Meadows' salary, make payments to his spouse, pay credit cards bills, travel to Las Vegas for gambling and make "numerous payments totaling over $100,000 to adult entertainment establishments in Minnesota and Las Vegas," prosecutors said. He also used funds to pay back earlier investors, to whom he provided false account statements.

"The defendant preyed on these everyday hardworking individuals," prosecutors said in asking for a 30-year sentence. "The defendant alternately charmed and intimidated his victims. The defendant convinced them that he cared about their lives, that he was their friend. He sat in their living rooms, hugged them, and called them by affectionate nicknames. He shared the details of his own family life, and ultimately convinced his victims that they could trust him. And it worked."

A U.S. District Court judge in St Paul, Minn., Susan Nelson, handed down a 25-year sentence June 26.

Mr. Meadows was also ordered to forfeit properties tied to the scheme, including a boat, expensive watches and real estate.

> "IN ALL HONESTY, Mr. Meadows, your conduct in this case was shocking."
>
> **U.S. District Judge Susan Nelson** in sentencing Sean M. Meadows

"The defendant destroyed the lives of more than 100 people, and he did it merely to satisfy his own greed," prosecutors said in the sentencing guidance. "He paid himself a significant salary, bought his wife jewelry costing tens of thousands of dollars, traveled and dined, spent opulently at strip clubs, gambled extensively and generally got to act like a big shot."

Mr. Meadows began his career in the brokerage industry in 1997 and worked at three independent broker-dealers before giving up his securities license in 2006 to found his own firm.

Federal agents raided Mr. Meadows' home in May last year with guns drawn, according to court filings.

So far, roughly $3 million of the $13 million has been returned to investors, according to an attorney appointed to represent Mr. Meadows, Mark Larsen of Lindquist & Vennum.

Mr. Larsen expected Mr. Meadows to appeal the 25-year sentence, hoping for lesser time.

"He pleaded guilty to all but one of the counts and has offered up his apology to victims and the court," Mr. Larsen said.

"I am so sorry for my conduct," Mr. Meadows said before sentencing, according to court filings. "I know I have an addiction to gambling and to alcohol, but that is no excuse for what I did."

The judge did not buy the apology, according to the StarTribune, which first reported the sentencing.

"Your apologies don't ring true," Ms. Nelson said, according to the report. "In all honesty, Mr. Meadows, your conduct in this case was shocking."

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Momentum behind streamlined prospectus for VAs

By Mark Schoeff Jr.

Securities and Exchange Commission Investor Advocate Rick Fleming has added his voice to what advocates say is growing support for improving disclosures for variable annuities.

In a report to Congress on June 30, Mr. Fleming said he backs a variable annuity summary prospectus, which would provide information about the risks, costs and benefits of the complicated products in a streamlined manner.

Usually, prospectuses run 150 to 200 pages for a variable annuity, which is an insurance product that combines an underlying mutual fund investment with income-guarantee features. A summary prospectus would be five to 15 pages. Current rules prohibit firms from issuing a pared-down prospectus.

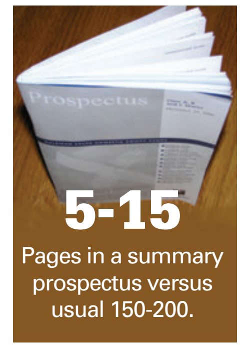
"We strongly support [SEC] staff's efforts to address the problem of lengthy and complex disclosure for each variable annuity," Mr. Fleming wrote.

A former SEC commissioner said June 29 that strengthening disclosure is an issue on which the increasingly fractious five-member SEC should be able to agree.

'WIDE CONSENSUS'

"This is an area that it would seem to me ... you could find pretty wide consensus," Troy Paredes, who served as an SEC member from 2008-13, said at an Insured Retirement Institute conference.

He added: "It's so straight down the fairway. It's all about disclosure. It's all about empowering investors by rethinking the format and presentation of information to make it more understandable and digestible."



5-15 Pages in a summary prospectus versus usual 150-200.

The IRI has been pushing for a variable annuity summary prospectus for about nine years. The SEC approved a mutual fund summary prospectus in 2009.

The problem is "not that it's not a priority," Mr. Paredes said. Rather, the SEC agenda is crowded with other proposals mandated by the Dodd-Frank financial reform law.

But Lee Covington, IRI senior vice president and general counsel, said that all five commissioners told IRI in meetings last fall that they back the summary prospectus and believe the agency could propose a rule.

"It's unclear what the holdup is, particularly in light of the strong support by all commissioners," Mr. Covington said.

The effort to get the agency to move on a proposal could be boosted by the naming of Andrew J. "Buddy" Donohue as SEC Chairwoman Mary Jo White's chief of staff.

Mr. Donohue supported a VA summary prospectus when he was the director of the agency's Division of Investment Management, according to Richard Choi, a partner at Carlton Fields Jorden Burt.

'UNIQUE OPPORTUNITY'

"We have a unique opportunity," Mr. Choi said at the IRI conference. "Perhaps we should be reaching out to Buddy."

Mr. Covington said the SEC should act quickly.

"They need to release a rule proposal in the next two to three months or we'll miss the 2016 window, and investors won't have a summary prospectus until 2017," he said.

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Advisers simulate SEC exams to find gaps before real thing

By Liz Skinner

Additional regulatory scrutiny of investment advisers has led more advisory firms to conduct mock exams to root out any compliance problems before examiners show up.

About 52% of advisers have had internal staff or a third party run their firms through a simulated examination of the kind that the Securities and Exchange Commission conducts periodically of advisers, according to a survey by the Investment Adviser Association in April and May.

That's up from 41% of respondents to the IAA survey just two years ago.

Financial adviser Wade Chessman, with an eponymous firm in Dallas, had compliance firm National Regulatory Services conduct a mock exam after learning that the SEC is focusing efforts on inspecting advisory firms that it hasn't visited previously. Chessman Wealth Strategies, founded in 2004, has never been examined by the commission's staff.

"The test was helpful to get an idea of what the SEC is looking for," he said. "We made a number of positive changes as a result, like locking files and desks at night, and reviewing our website and other marketing materials."

$5,000 WELL SPENT

Mr. Chessman said he'll have another mock exam conducted in two to three years if his firm isn't inspected by the SEC before then. He said the exam and a detailed report of the findings cost $5,000.

"It's a lot of money, but it's an important part of our business," he said. "You want to make sure you're doing everything right, especially in this climate."

ISTOCK

Currently, the SEC examines about 10% of the approximately 11,500 registered investment advisers nationwide annually.

The commission said earlier this month that it will specifically examine the retirement-planning guidance provided by financial advisers, and in February it said it would scrutinize cybersecurity preparedness in the industry.

"The compliance atmosphere has gotten much more challenging and complex for advisers," said Karen L. Barr, president and chief executive of the IAA. "The focus by the SEC on compliance program rules and chief compliance officers has certainly raised the level of anxiety for compliance personnel out there."

Mock exams are a useful tool for advisory firms to make sure their policies and procedures are working as intended, she said.

About 34% of advisers use a third-party compliance consultant or legal counsel to conduct the mock exam, 15% had internal compliance staff run the test and 3% used their parent company to handle the exam, found the IAA survey of 474 firms.

Todd Cipperman, principal at Cipperman Compliance Services, said that the simulated exams often expose conflicts of interest and documenting processes that fall short of best practices.

He added that advisers don't need to complete full mock exams every year — probably every other year is enough.

HIGH-RISK AREAS

Ms. Barr said some firms pick high-risk areas for their business and conduct mock exams only in those areas.

In the recent IAA survey, firms reported increasing the amount of compliance testing in cybersecurity, advertising, personal trading, disaster-recovery planning and best execution.

Karen Bordonaro, an adviser and Demming Financial Services Corp.'s CCO, said that her firm hasn't conducted mock exams in the past, but probably will in the future.

The SEC examined the Aurora, Ohio-based firm for the first time in September, and it took two people five days, working up to 10 hours a day, to gather all the information that the inspectors asked for, she said.

The firm was not found to be deficient in any area, but it will look to make changes in some areas the SEC probed, such as disaster planning, she said.

The SEC examiners were incredibly comprehensive, Ms. Bordonaro said.

"They gave us a list of 18 to 20 areas that we had to supply information, and ours was a limited-scope audit," she said.

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Investors not reaping all bond gains

Advisers need to give more guidance on when to get into nontraditional funds

By Trevor Hunnicutt

Investors in bond funds used to dampen the risk of rising interest rates underperformed both the "unconstrained" managers of those investments and traditional fixed-income funds during the past decade, according to a new analysis. That's because many investors got into and out of those investments at the wrong times — buying high, selling low or both.

MORE LATITUDE

Over the 10-year period that ended May 31, investors captured just 44% of the nearly 4% return generated by managers in the nontraditional bond fund category tracked by Morningstar Inc., which includes a popular group of unconstrained and "strategic income" funds that give managers more latitude to explore fixed-income securities across global bond markets.

44% Percentage of nontraditional bond fund gains captured by investors

That means the average investor captured a gain of just 1.75% annually over that 10-year period, which compares unfavorably not just to the return of unconstrained managers, but to the returns of investors in the popular intermediate-term bond fund category.

Investors in the latter took home nearly 2.94%, pulling in nearly 70% of the returns that category's managers generated, which were also higher than the unconstrained managers' gains.

The intermediate-term fixed-income category includes funds such as the Vanguard Total Bond Market Index (VBMFX) and Pimco Total Return Fund (PTTAX) that are widely used as the core bond exposure in portfolios that financial advisers build.

"That's pretty shocking," Michael Herbst, the director of fixed-income manager research for North America at Morningstar, said last month during a panel at the research firm's conference for financial advisers and fund managers in Chicago. "What that says to us is the more that we, the managers and the folks in this room, can shape reasonable expectations for how these funds will behave in various market environments, the more it can help keep clients in these markets or keep them out."

TIMING IS EVERYTHING

Mr. Herbst said Morningstar data showed that the greatest flows into the funds came after years of strong performance, and the greatest outflows came after years of poor performance. Research has shown that sort of ineffective timing can erode returns.

Morningstar calculates "investor return" by estimating the return achieved by the average investor based on when investors bought and sold the fund.

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Timing of divorce likely to pay off

Continued from Page 4
will be needed in the divorce of Ms. Garner, 43, and Mr. Affleck, 42, who reportedly are worth about $40 million and $75 million, respectively. The custody of the children also would play into a future agreement.

The fact that they seem to have waited until the 10-year threshold "shows they are at least planning and acting for the mutual benefit of each other at this point, as opposed to some cases where both go for the jugular," Mr. Landers said.

Ten years is a significant milestone for other important financial reasons, even if those reasons probably don't apply to these actors.

If a marriage lasts at least a decade, an ex-spouse is entitled to Social Security benefits related to the former husband or wife.

Most people married 10 years can take a benefit equal to half of the ex-spouse's full retirement benefit if they meet certain parameters, such as being older than 62, not married and as long as their own Social Security benefit would not be greater than what is received through the ex-spouse's benefit.

John LeMieux, an adviser and principal at Anton LeMieux Financial Group, said these benefits can be a reason to stay married until that 10th anniversary, especially if one spouse did most of the earning. Such a move doesn't hurt the spouse who earned more because the benefits come from Uncle Sam, not the spouse.

Whether it's worth staying together for such a benefit is a case-by-case decision.

'THE BEST WAY'

"It's one piece of the puzzle, but it's difficult to give financial advice in an emotional world," Mr. LeMieux said. "If people are at a place where their marriage is coming apart, they ought to do their due diligence and figure out the best way to end the marriage for both parties and any children."

A marriage of 10 years also is significant when one spouse is in the military.

A non-military former spouse is entitled to the military benefits of the spouse if the marriage has lasted 10 years, said David Horowitz, an attorney with Hottell Family Law Group.

Non-serving spouses would do best to hold off on asking for a divorce until after the 10-year threshold, while the military spouse would want to seek a divorce before this important milestone because any award to the ex-spouse would reduce the military pension the serving spouse would receive, he said.

Health care benefits available through the military also are at stake when a couple divorces before that 10-year mark, said Lili Vasileff, founder of Divorce and Money Matters.

Finally, 10 years can be an important marker if a couple has a prenuptial agreement that incorporated this milestone.

It could be that the lower-earning spouse might be eligible for a greater split of assets under that agreement if they hold out for the 10-year mark, said Mr. Landers, who recently published a second volume of "Divorce: Think Financially, Not Emotionally" (Sourced Media Books, 2015).

Ms. Garner and Mr. Affleck reportedly did not have a pre-nup.

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Joel's baby is Social Security-eligible

Continued from Page 6
Security benefits each month because one or both of their parents are disabled, retired or deceased, according to the Social Security Administration.

"The guidelines for managing the beneficiary's [child's] funds are pretty clear," Social Security spokesman William Jarrett said in an email. "The investment should not be invested in a vehicle that involves the payee (usually the parent) in any conflict of interest, the funds should not be kept at home or mingled with the payee's money, and the payee must keep accurate records."

SAVING FOR EDUCATION

Mr. Jarrett confirmed that funds may be set aside for foreseeable needs, such as the child's education. "While U.S. Savings Bonds are most common, deposits in other interest- or dividend-bearing accounts is acceptable, provided the institution is insured under federal or state law


ISTOCK

Billy Joel: Will his child collect from the "Viagra College Fund?"

and the account is titled properly," Mr. Jarrett wrote.

The Social Security Handbook says invested funds must be titled in a way that shows a representative payee holds the property in trust for the beneficiary. The titling must show that the payee has a fiduciary interest for the beneficiary, permits the payee ready access to the funds when needed for the beneficiary's current maintenance and does not permit the beneficiary to have direct access to the funds.

But there are limits to the government's largesse. The family maximum amount limits the total amount of Social Security benefits that can be collected on a worker's earnings record. The limit varies but is generally equal to about 150% to 180% of the worker's basic benefit. If the sum of the benefits payable to family members is greater than this limit, the benefits will be reduced proportionately for the minors.

In the event of a parent's death, the minor dependent child would be entitled to a survivor benefit worth 75% of the deceased parent's benefit until the child turned 18 (or 19 if still in high school), subject to family maximum limits.

(Questions about Social Security? Find the answers in my ebook at InvestmentNews.com/mbfebook.)

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Securities America on hot seat

Continued from Page 6
statement that the firm "will vigorously defend against the allegations."

An attorney for Mr. Armstrong, Timothy O. Egan with Peabody & Arnold, also disagreed. He said there was no false advertising. Mr. Armstrong was sincere and his personal experience with Alzheimer's motivated him to provide information as well as financial advice, according to Mr. Armstrong.

"Motivated by his personal experiences, Mr. Armstrong has endeavored to provide the public with valuable information about the disease and sound financial strategies that families can consider to protect themselves in the event they become a direct or collateral victim of the disease," he said. "This is precisely what the ad offers and what Mr. Armstrong provided."

NO CUSTOMER COMPLAINTS

Mr. Egan added that the ad generated no customer complaints and it was "unclear what has prompted the secretary of state's office to pursue this matter.

"Mr. Armstrong intends to vigorously defend his good name," he said.

Regulators have been focused on advertising and marketing to seniors as part of several recent investor protection initiatives. The Financial Industry Regulatory Authority Inc., for example, recently launched a toll-free securities help line for seniors, and has said it is focusing on marketing, including senior designations, as part of its regulatory efforts.

Mr. Armstrong has five disclosure events on his Finra BrokerCheck record, including a termination from a previous broker-dealer and three customer disputes. Two of the disputes were settled for a smaller portion of what was requested and one was withdrawn. Mr. Armstrong disputed the allegations behind the termination and customer disputes, according to BrokerCheck.

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TECH CONNECT

Flames no match for cloud protection

By Alessandra Malito

Jon Ten Haagen, a financial adviser with Ten Haagen Financial Group in Huntington, N.Y., has used cloud-based programs for years, but it was the day after Memorial Day when the web-based applications ended up saving his business.

A fire broke out in the office building in which he was renting space, due to a spark from an unspecified cause. Everything from the back wall to his office was obliterated, he said. Metal filing cabinets were melted and twisted. Personal items like a calculator his parents gave him as a child and old photos and trophies of his boat-racing days were gone. His clients' information, however, was safe — it was in the cloud.

"If I didn't have it [in the cloud], I would be out of business," Mr. Ten Haagen said.

48 HOURS

Mr. Ten Haagen is displaced, working out of an office in neighboring Northport. It only took about 48 hours to get everything back up and running, he said, noting that's the time it took for his new computer to ship.

Certainly, cloud-based technology is becoming the norm across the industry. Not only does it prove useful in recovering from natural disasters, but it also provides an increased level of efficiency and scalability, said John Rourke, chief executive of Gotham Tech Labs' Wealthbox customer relationship management system.

BETTER THAN A LAPTOP

"It's getting cloudier — in a good way," Mr. Rourke said. "We kind of take it for granted now, but it wasn't too long ago that everyone thought having all your data stored on your laptop was more secure than on the cloud."

He said that perception has changed, since data stored in the cloud is safer than a hard drive that could be lost in a fire, flood or theft.

The cloud-computing trend will only solidify. According to the State of the Cloud 2015 report by Bessemer Venture Partners' Byron Deeter, 62% of CRM programs will be cloud-based by 2018. The study also projected that the cloud computing market will reach $127.5 billion by 2018, growing at a 22.8% compound annual growth rate.

Clouds of smoke: Firefighters battle blaze that destroyed Jon Ten Haagen's office in Huntington, N.Y., on May 26.

Joe Lukacs, a coach for financial advisers with International Performance Group Inc., said he recommends his clients work — and back up their work and client data — in the cloud. He calls it the Starbucks test: If there's an emergency and that adviser can work remotely from anywhere, even a Starbucks, then his or her business will be OK.

"You always want to have that disaster-recovery process, but you don't want to wait [to move to a cloud-based system] until you need it, whether it's a fire, flood or whatever else goes wrong," Mr. Lukacs said.

In fact, he suggests advisers purchase their own source of portable Wi-Fi, both for convenience and security reasons.

"I don't know how you're going to be in this business today or in five years from now if you're not cloud-centric," Mr. Lukacs said. "As an adviser, you don't want to be in the data business."

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F-Squared files for bankruptcy

Continued from Page 5

Those burdens have made it increasingly hard for F-Squared to change the subject: One wholesaler for the firm recently described his company as being in "the penalty box" with investors.

F-Squared's filings on Wednesday with the U.S. Bankruptcy Court for the District of Delaware offered new insight into its challenges in recent months.

The Wellesley, Mass.-based company lists as its largest creditor its co-founder and former chief executive, Howard B. Present, who it says is owed nearly $2 million.

The former Putnam Investments executive was the force behind F-Squared's attempt to capitalize on adviser interest in ETFs, as well as exposures to the stock market that manage risk.

Mr. Present left the firm in November and has been fighting the Securities and Exchange Commission in federal court to keep from being barred from the industry and having some of his earnings clawed back.

EMPLOYEE CONTRACTS

F-Squared also lists claims by two law firms totaling $827,328, a credit-card bill for $115,537 and hundreds of thousands of dollars in employee contracts.

As part of the deal, Broadmeadow Capital will enter into agreements with F-Squared employees necessary to manage the investment strategy and client relationships. Operations responsibilities will be handled mostly by existing Broadmeadow staff. Mr. Ingersoll said he could not yet estimate how many F-Squared employees would be brought over; Laura P. Dagan, the chief executive, will not be among them.

In March, F-Squared cut 25% of its workforce, leaving it with about 121 employees. It has also trimmed and reorganized its executive ranks.

"THIS IS PROBABLY a little bit of a fresh start for the algorithm."

Greg M. Vigrass
President and CEO
FOLIOfn Institutional

F-Squared routinely promoted seven years of pre-2008 results for its AlphaSector strategy, despite launching the product that year. The results were hypothetical and miscalculated in a way that made them look more favorable, according to a statement of facts the company signed as part of the settlement process.

F-Squared's claim that its rules-based strategy could sidestep violent market swings — by trading in and out of nine industrial-sector ETFs — appealed to advisers stung by the 2008 free fall of stock markets. The company built itself from a virtual nonentity in 2008 to the force behind a $28.5 billion strategy as of June 2014.

Those assets have fallen significantly: The company saw nearly $8 billion in asset declines in its ETF strategies in the 12-month period ended March 31, Morningstar Inc. said. The mutual fund distributor Virtus Investment Partners Inc. also cut F-Squared as a manager on five of its products, with some $5.7 billion in assets.

F-Squared said it will "continue operating in ordinary course throughout the sale process," paying its employees on "a timely basis." Company officials declined to comment further.

"This is probably a little bit of a fresh start for the algorithm," said Greg M. Vigrass, president and chief executive of FOLIOfn Institutional, whose investing platform includes F-Squared strategies and is used by financial advice firms. "It's potentially good news for investors and those that were fans of the F-Squared business model and investing approach."

Broadmeadow, which reports $15 million in assets under management, said it expected to be in a position to close the deal within 45 days. Broadmeadow owner Cedar Capital also owns Good Harbor, another ETF strategist that's struggled to retain assets after performance challenges.

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Issues in CFP suit not settled yet

Continued from Page 4

District Court Judge Richard J. Leon placed his opinion under seal for 14 days. The basis of his decision will be revealed at that point, unless the parties convince the judge to keep parts of it confidential.

The Camardas said they can't comment in detail until they read the full opinion, but they are concerned that Mr. Leon supports the argument that the CFP Board made in its motion to end the case, essentially that the court can't second-guess the organization's interpretation of its own rules.

A former CFP Board chairman whose disciplinary case has been at the heart of the board's struggles over compensation definitions said that the court ruling gives the organization too much power.

'SOME RECOURSE'

"There ought to be some recourse for certificants if they have an argument with the CFP Board," said Alan Goldfarb, managing director of Financial Strategies Group. "This [decision] seems to take away all that."

Mr. Goldfarb stepped down as CFP Board chairman in November 2012 as the board began an investigation into allegations that he mischaracterized his compensation on the Financial Planning Association website.

Another action that drew much attention revolved around the use of the fee-only description by Rick Kahler, the president of Kahler Financial Group. Mr. Kahler and the board reached a resolution in November that involved his giving his interest in a family real estate firm to his wife.

The court ruling "strengthens the CFP Board's position on fee-only; there's no question about that," Mr. Kahler said. "Overall, it's a good thing for the profession. Fee-only needs to mean something."

But the meaning of the CFP Board's compensation description is still up in the air, according to Mr. Kahler. Confusion still exists about terms such as "non-trivial economic benefit" and "related party" in the organization's rules.

"They remain undefined today," Mr. Kahler said.

Kim and Jeffrey Camarda: Their dispute with the CFP Board involves an arm of their firm that sells insurance for commissions.

The CFP Board agrees that the ruling bolsters its authority when it comes to its own standards.

"CFP Board is very pleased that Judge Leon dismissed the case on the basis of deficient legal claims without the need for a trial," Marilyn Mohrman-Gillis, the CFP Board's managing director of public policy and communications, said in a statement last Tuesday. "This ruling affirms CFP Board's authority to set and enforce its Standards of Professional Conduct, which serve as critical consumer protections."

As part of an effort to underscore its current compensation terms, the CFP Board temporarily removed the fee-only description from its website in September 2013 and told the 8,000 CFPs using the label to reevaluate whether they complied with the CFP rules before resetting it on their profiles.

Now that the CFP Board is not embroiled in a court case, it should reconsider its punishment of mark holders who tripped up on the fee-only definition, said Mr. Goldfarb, who at one time headed the board's disciplinary body.

"It would be nice if they would go back and give retroactive amnesty to anyone that was affected by the unclear or misunderstood meaning of fee-only," Mr. Goldfarb said. "To be sanctioned for a misunderstanding to me was over the top."

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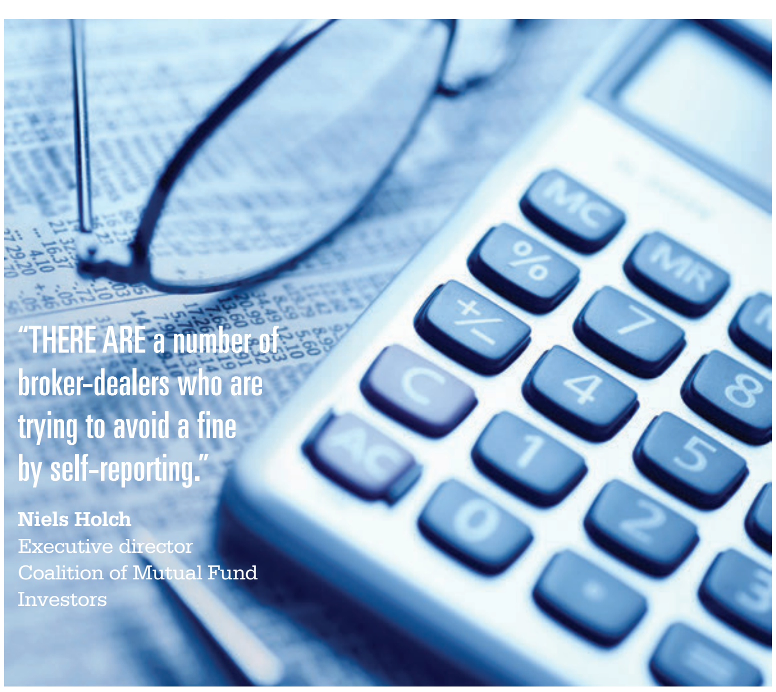
B-Ds to repay $30M

Continued from Page 4

train their brokers on the discounts. The brokerages neither admitted nor denied the charges in settling with Finra.

The regulator credited the firms with "extraordinary cooperation" for self-reported these errors, and will provide full restitution to customers," Brad Bennett, Finra executive vice president and chief of enforcement, said in a statement.

Last year, Finra fined Merrill Lynch $8 million in addition to



identifying the infractions and improving their systems to provide mutual fund discounts. Finra did not impose any fines on top of the reimbursement to investors.

"While Wells Fargo, Raymond James and LPL failed to ensure that their customers received these discounts, Finra's sanctions acknowledge that the firms detected and ordering restitution for similar overcharges on mutual fund sales.

The fact that Wells Fargo, LPL and Raymond James came forward on their own is no coincidence, according to Niels Holch, executive director of the Coalition of Mutual Fund Investors.

"There are a number of broker-dealers who are trying to avoid a fine by self-reporting," Mr. Holch said. "They're trying to get ahead of this."

The firms touted the fact that they blew the whistle on themselves.

"As noted by Finra, Raymond James discovered the issue internally, proactively initiated client refunds and self-reported the findings to Finra," Steve Hollister, director of public communications at Raymond James, said in a statement. "Given the firm's extraordinary cooperation, Finra waived any fines which would have otherwise been assessed. We are pleased to have the issue resolved."

STRUCTURAL PROBLEMS

LPL echoed those points.

"LPL self-reported this issue, and we are addressing it to help uphold our commitment to serving the best interest of investors," the firm said in a statement. "Importantly, there are no fines associated with this agreement as a result of our ongoing efforts to ensure a proper resolution of this issue for investors."

Wells Fargo declined to comment.

Failure to pass along mutual fund fee discounts is structural, according to Mr. Holch. It occurs when brokerages consolidate thousands of mutual fund sales into a single omnibus order to a fund.

"Until we address the problems with omnibus accounts, we're going to see more of these enforcement actions," Mr. Holch said. "The broker-dealers are not providing what's promised in the prospectus regarding sales load discounts. The fix is transparency [for the fund] down to the account level."

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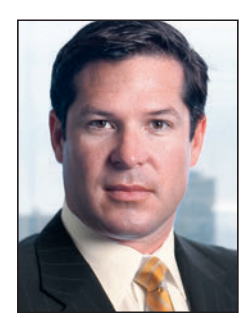
Finra board seats in play

Continued from Page 5

and require firms to provide too much documentation. He also complained that examiners can ask "leading questions" and firms have no way to defend themselves.

"We have no rights," Mr. Kohn said in an interview. "Check the Constitution at the door when you take your Series 7. You can't plead the Fifth Amendment."



Brian Kovack

Mr. Romano said that he, too, wants to improve the exam process.

"I've got my own [exam] scars," he said. "I've been fighting that fight for four years."

Brian Kovack, president and co-founder of Kovack Securities Inc., is running for the midsize-firm seat against John Muschalek, vice chairman of First Southwest Co., who was nominated by Finra.

ARBITRATION

If elected, one of Mr. Kovack's targets would be Finra's arbitration system.

"It needs a better structure of accountability for lawyers who file frivolous claims," he said.

Mr. Kovack also wants to refine the disclosures registered representatives must make on documents that form the foundation for the BrokerCheck database. He said reporting requirements on liens and other legal settlements go too far.

"There needs to be de minimus exemption," Mr. Kovack said.

Mr. Muschalek did not respond to a request for comment.

John Thiel, head of Bank of America Merrill Lynch, is running uncontested for the third seat up for a vote — the one representing large firms.

A small firm employs between one and 150 registered representatives, a midsize firm between 151 and 499 and a large firm more than 500. Finra oversees about 4,100 firms.

Small firms need to be heard because they get short shrift from Finra, Mr. Kohn said.

"We're almost treated like we're invisible," he said.

Mr. Romano underscored the need for the board's financial services representatives (of which there are 10) to explain industry issues to their 13 public-representative colleagues on the board.

"We've got to sway those public governors," he said. "I believe I'm that best voice."

Each seat has a three-year term. The Finra board consists of 24 members, including the board chairman, Finra chief executive Richard G. Ketchum.

This year's election will be held at the Finra annual meeting July 30 in Washington. Members can vote this month online, by telephone or by U.S. mail.

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GAME CHANGERS/The Great Wealth Transfer

COURTING THE KIDS

Advisers will see their assets disappear if they can't connect with their clients' children

By Liz Skinner

"We had built a trusted relationship and all of a sudden it had come undone."

Karen DeRose
Founder
DeRose Financial Planning Group

TODD WINTERS

FINANCIAL ADVISER KAREN DeROSE never saw it coming.

A week after the husband of a couple she'd worked with for 10 years dropped dead of a heart attack, Ms. DeRose received an order to transfer the couple's $6 million portfolio into a self-directed account at Charles Schwab & Co. Inc.

That's when Ms. DeRose realized she had overlooked the obvious: the couple's son.

"I felt bad," she said. "I felt like all of the planning we had done really didn't matter."

Some of that planning even took the form of "family meetings," which included the couple and their two daughters, Ms. DeRose said.

"All of a sudden, the son shows up with lots of questions," she said. "We had built a trusted relationship and all of a sudden it had come undone."

Unfortunately, Ms. DeRose's experience with the transfer of assets from one generation to the next is all too common.

Over the next 30 years, an epic $30 trillion will be passed down from baby boomers to Generation X to millennials. In that enormous transfer of wealth, many investment advisers will see their hard-earned asset base evaporate — and the value of their firms plummet — because they don't know how to connect with their clients' children. The problem is especially difficult for the many advisers ill-equipped to connect with clients who are technologically savvy and expect a very different service experience than their parents did.

"The largest wealth transfer ever is coming and financial advisers are looking down the barrel of not being used by the heirs of the vast majority of their current clients," said Vic Preisser, founding director of the Institute for Preparing Heirs, a consultancy that works with advisers on wealth transfer issues.

FIRING THEIR PARENTS' ADVISER

The simple, undeniable truth is this: Sixty-six percent of children fire their parents' financial adviser after they inherit their parents' wealth, according to an *InvestmentNews* survey of 544 advisers in April.

Advisers unable to prove they are effective at establishing relationships with clients' children and serving the next generation also will discover their businesses are worth less to potential buyers, experts said.

"Advisers are woefully behind in getting to know their clients' adult children," said Bernie Clark, the head of Schwab Advisor Services. "The tricky part is that boomers still have to be served, so I think advisers will have to go through a period with multiple models to make sure they are serving all clients."

At the same time, the giant wealth transfer on the horizon could be an opportunity for advisers who have a plan to draw in the children of their best clients and become the trusted family adviser.

TRAINING THE NEXT GENERATION

With proper guidance, advisers might even train heirs to be better stewards of their family's wealth than past generations — a bar that wouldn't be that tough to raise, given 70% of family money disappears by the end of the second generation, and 90% is gone by the end of the third, according to oft-cited research of 3,250 families conducted in 2003 by Mr. Preisser and Roy Williams, an independent wealth transfer consultant who helps advisers and their families.

"Bringing up wealth transfer with clients shows them you care about the future success of their children; it can be a huge differentiator," said Diane Doolin, an adviser with Morgan Stanley Wealth Management.

"It's not just about advisers losing assets when the clients die, it's about taking the current relationships to a deeper level."

In most cases, however, advisers aren't even trying to make inroads with clients' children.

Only 20% of advisers are targeting younger family members of their clients, according to a February survey of 500 advisers and 1,200 investors by Corporate Insight.

Many advisers said they don't know how to appeal to clients' kids, or they believe that connection is not worth the effort.

For some, it's too much work to invest time developing relationships with a client's family, given how diluted assets can become as they are passed from one generation to the next, said Silviya Simeonova, an analyst at Corporate Insight. Advisers who have their own retirement in sight and aren't planning a second evolution of their firm are especially reluctant to invest the time.

"I'm not trying to collect new clients," said Walter Altorfer, 71, principal of WRA & Associates. He rarely works with clients' children and isn't worried about his firm's valuation.

Mr. Altorfer doesn't foresee selling his advisory firm, having found it too difficult to find a successor.

But advisers who are dedicated to creating sustainable businesses will need to start imagining what their balance sheets would look like if 66% of their best clients departed.

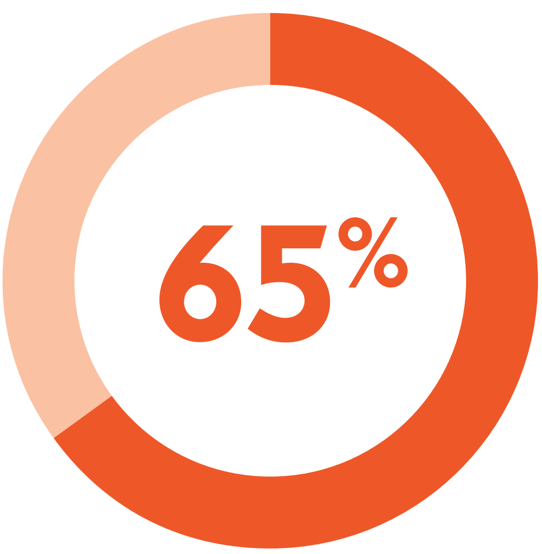
Often, heirs bring the assets to an adviser they already work with or choose to manage the money themselves. Sometimes the inheritance is split among so many parties that

Continued on Page 34

Bridge the Generation Gaps.

GEN Xers

65% are saving for retirement, but not using a financial advisor.

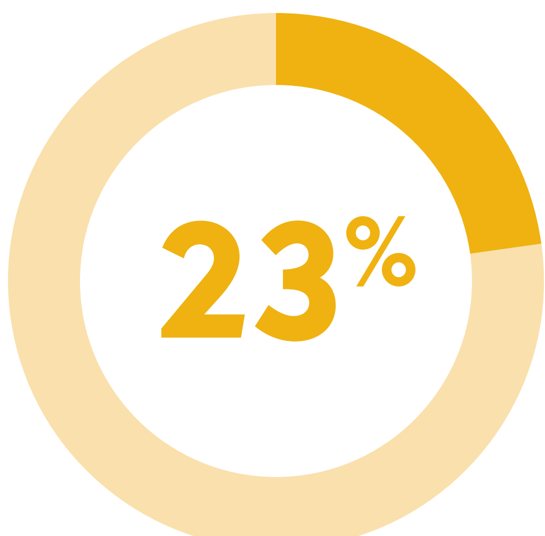


HOW WILL YOU INTRODUCE YOURSELF?

Collinson, C. (2014, August). Generation X Workers: Retirement Reality Bites Unless Answers Are Implemented.

MILLENNIALS

represent 23% of America's millionaires.

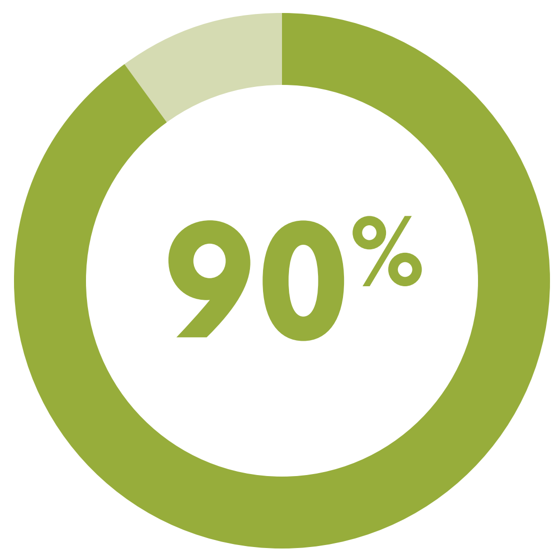


HOW CAN YOU CONNECT WITH THEM?

Shullman Research Center (2014, March)

HEIRS

90% will change financial firms after they inherit.



CAN YOU BUCK THE TREND?

Pershing Advocates Focus on Attracting Gen X and Gen Y Investors to Support Future Success. (2012, June 6).

Financial advisors understand the importance of multigenerational planning. Putting strategy into action, however, can be daunting. GenLink offers advisors a combination of academic research, demography, trend spotting and actionable takeaways that can be applied immediately.

To learn about Ivy Funds GenLink program, contact your Ivy Funds wholesaler, call the sales desk 1-800-532-2751, or visit ivyfunds.com/genlink.

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GAME CHANGERS/The Great Wealth Transfer

Courting the kids

Continued from Page 32

there's not much left to manage. In other cases, heirs just spend the assets too quickly.

IMMUNE TO ADVICE

Mike Johnson, a principal with Moneta Group, got a call from a client's son the same week the client died to ask how soon he could have his mother's money.

"He said he was building a pool and the contractor wanted to be paid," Mr. Johnson said.

Some children aren't used to paying for financial advice and don't see the wisdom in doing so, even after they are suddenly awash in wealth.

"I see 60-year-old children, who have created little of their own wealth, leave and take the assets because they don't want to pay us to manage the money," said Sybil Praski, an adviser with Prosperion Financial Advisors. "I have worked with clients for 25 years sometimes and all of a sudden, their wealth was gone."

From the child's perspective, if they have no relationship with their parents' adviser or one of their own, they will likely seek a financial professional who is closer to their own age or one who appeals to their own interests or needs. Why would they remain with an adviser who's destined to retire before they do?

For Anne, who asked that her last name not be included, the responsibility of overseeing the multimillion-dollar estate that her father left her when he died in 2012 was overwhelming.

She transferred her inheritance away from the two brokers who had handled the money for her father at a large firm because she didn't feel she was getting enough direction.

Anne brought the assets to Family Wealth Planning Group because Tom La Macchio and his partners seemed to better understand what she needed, which was everything from handholding to creating a trust for her son.

"I had big decisions in front of me and I didn't know how to deal with it," said Anne, 58. "With their guidance, I could start seeing pathways and a vision of how to do this."

The lack of a relationship, as in the case of Anne and her father's financial professionals, is the No. 1 reason advisers lose assets when clients leave their wealth to their children, according to the *InvestmentNews* survey.

The absence of a relationship between advisers and clients' children also affects how much buyers are willing to offer for an advisory firm, even before the money changes hands between generations.

When calculating an advisory firm's value, experts factor in the age of its clients and discount businesses whose clients are predominantly in their 70s and above, said John Furey, owner of consulting firm Advisor Growth Strategies.

Firm valuations will be higher if the adviser can show the business has a relationship with the children of their older clients, such as the younger generation's having accounts with the adviser, he said. Experts also look at the adviser's track record of retaining assets after clients die.

"There can be a precipitous drop in revenue if suddenly clients are 72 and advisers aren't doing a good job retaining the assets or bringing in new clients," said Tom Nally, president of TD Ameritrade Institutional. "Advisers have to start preparing for these huge shifts of wealth if they want to be able to capitalize on the opportunity."

TD Ameritrade and many of the nation's largest custodians and brokerages recognize the impact the coming transfer of wealth could have on their own firms. They offer programs to help advisers develop skills to embrace multigenerational clients and create teams that can better serve diverse investors.

Fidelity Investments is one of several large firms that have employed the Institute for Preparing Heirs to train advisers on how to establish relationships with a client's family members. And timing is everything.

> *"If you wait till an event-driven crisis to engage with surviving children, it's likely too late."*
>
> **David Canter**
> EVP
> Fidelity Investments

"If you wait until an event-driven crisis to engage with surviving children, it's likely too late," said David Canter, executive vice president of practice management and consulting at Fidelity's clearing and custody business.

DO INITIATIVES WORK?

Not everyone agrees that formal initiatives targeting the next generation are effective.

Richard Hough, chief executive of Silvercrest Asset Management Group, said the education and other programs offered by some wirehouses and banks are more "marketing and window dressing than something real."

"Clients are going to set the tone for how and in what way you're going to be allowed to work with their children," he said.

Silvercrest, which manages $18 billion in assets, retains clients with its intense focus on client service, Mr. Hough said. The firm's advisers assist clients with major events in the children's lives, such as buying a first house or advising on a trust for a child.

"You end up working with the next generation and hopefully you're remembered for playing a big role in those important events in their lives," he said.

Paul Reilly, chief executive of Raymond James Financial, puts it this way: Advisers should be thinking in terms of serving families from the beginning, not just couples or individuals.

"Advisers have to make kids, the inheritors, part of the trusted relationship," he said. "The best advisers are family advisers."

Thinking about the family as the "client" isn't new for the firm. When Robert James started Raymond James, he would not accept a client whose spouse and children didn't attend meetings once a year, Mr. Reilly said.

"He might have been ahead of his time 50 years ago, but the advice should be that if advisers aren't going to follow the funds or bring people into their teams who work with their clients' kids, they're going to have a generational business and the assets are going to go somewhere else," Mr. Reilly said.

If advisers do decide it's worth reaching out to the next generation, they should do so early because it takes years to establish a relationship.

For example, advisers should help grandparents set up 529 college savings plans, make sure there is enough life insurance to protect the children, create lifetime gifting plans "and find any other way to get an introduction to the children," said William Morgan, president of Herbein Wealth Management.

His firm's fee structure supports its multigenerational goal. Everyone within a family pays the same rate at Herbein. If grandparents have an investment account, their children and grandchildren can open accounts with the firm and be charged the same rate — likely much lower than they'd get elsewhere.

"We're not batting a thousand, but last year we had three deaths of significant clients for our firm and we retained every one of those," Mr. Morgan said.

Today Ms. DeRose is among the advisers who actively work to stem the flow of assets as wealth is ceded to children. First and foremost, she reaches out to clients' children before they seek out their own adviser.

Even more important, Ms. DeRose brought her son, who is 32, into DeRose Financial Planning Group. Now clients' children have an associate at the firm who is their peer and relates well with them.

"It also shows we're doing our own intergenerational planning," she said.

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"Advisers have to make kids, the inheritors, part of the trusted relationship."

Paul Reilly
CEO
Raymond James Financial

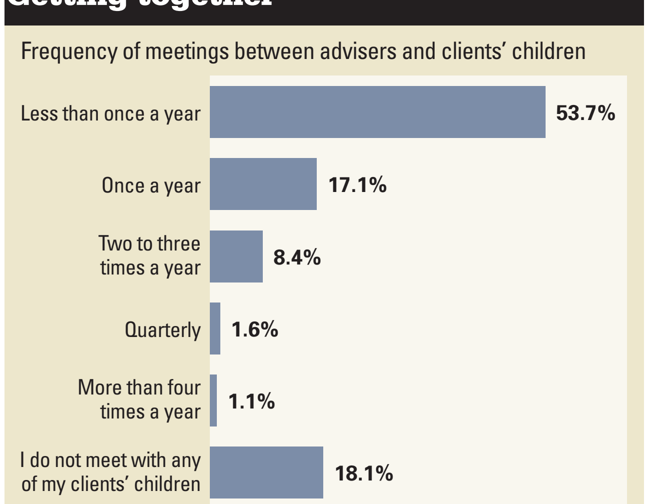
TIMOTHY HEALY

7 strategies for holding on to families

- Help children of clients with early financial planning decisions around events such as home buying, new births, college savings, etc.
- Encourage clients to hold family meetings to discuss philanthropic missions, impact investing and estate planning.
- Sponsor events that encourage clients to bring family members and offer programs that appeal to different age groups.
- Develop a team that includes younger advisers who can relate to clients' kids.
- Embrace a fee structure that allows advisers to provide affordable planning services to clients' family members (some advisers provide pro bono services until the person has enough assets).
- Communicate early and often with clients' children to gain their trust before they go looking for an adviser of their own.
- Develop digital-based services that appeal to next-gen investors, such as virtual communications capabilities and mobile apps.

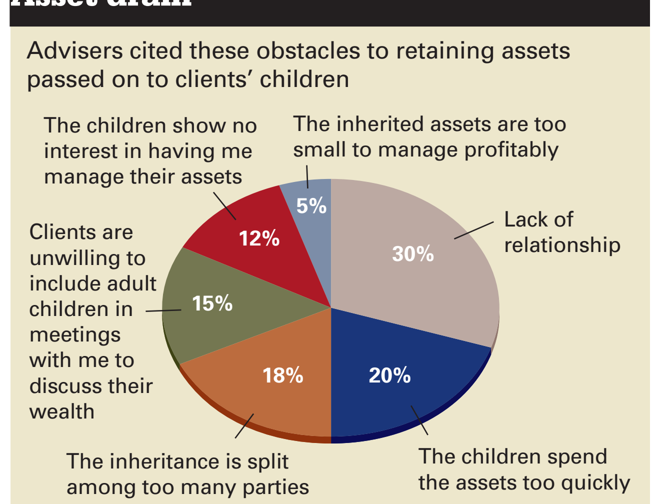
— Liz Skinner

Getting together



Source: *InvestmentNews* Data

Asset drain



Survey of 544 advisers in April **Source:** *InvestmentNews* Data

GERARDO TABONES