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LLBH Private Wealth Management LLC

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"What potential red flags should I look for in my wirehouse portfolio?"

By Kevin Burns

As an independent advisor, I am often asked to review portfolios of prospective clients with assets held at wirehouse firms. Having spent 26 years in the big banks, it is unfortunate how little has changed since my partners and I left to start our own firm in October 2008.

Among the reasons we sought independence was our desire to avoid the inherent conflicts we found in these institutions and to extract ourselves from any perceived influence on our investment decisions beyond serving our clients' best interests. We value our ability to invest free of any inappropriate forces and are struck by the many examples we see of these conflicts manifesting themselves in portfolio construction.

It's not unusual for the internal products of wirehouses to find their way into client portfolios, often with higher fees and payouts to brokers who sell them. Remember, an independent registered investment advisor has a fiduciary responsibility for putting clients' interests ahead of his or her own. A wirehouse broker has only a suitability standard, meaning that the requirement to make investment decisions is based on what is suitable, not necessarily what's best for the client.

For their own benefit, investors should understand the logic behind the investment decisions their advisors make. A portfolio should be constructed using clearly defined investment criteria and a well-defined process to determine an overall asset allocation strategy. Yet, in our experience, clients of these brokerage firms have a difficult time getting straight, succinct answers to the most fundamental of questions: What investments do they own, and why?

Some of the more urgent red flags to look out for include:

Proprietary Bank Mutual Funds: Obviously, it's unlikely that the in-house mutual funds marketed by banks will be best in class across the asset spectrum, with superior performance and lower cost than their outside alternatives. During our tenure at large banks, we rarely selected in-house "solutions," as they simply weren't the best.

Proprietary Hedge Fund of Funds: It's important to know what these funds were designed to accomplish, their fee structure and liquidity provisions. More importantly, would the answers to these queries be the same had they been negotiated at arm's length?

Preferred Stocks and Closed End Fund Offerings: The fees paid to wirehouse brokers for these products are often exorbitant. At the same time, we've seen many instances where the products have little-to-no relevance in an overall allocation strategy, which exposes the investor to unnecessary risk. A recent portfolio we examined had 22 newly issued preferreds and 18 of them were below the offering price!

Structured Notes: Many are sold as risk-adverse strategies; however, our experience is that they are often expensive and have other issues such as counter-party risk and potential liquidity limitations during difficult markets that are not fully understood. For instance, if you have a note linked to the S&P 500 with downside protection, you may believe you own equities. In reality, you own a big bank derivative and are an unsecured creditor of that institution.

Long-Term Annuities: Investors are often unclear as to the initial fees and penalties for early withdrawal.

Many portfolios we see from clients of big banks have higher costs, greater risk and less liquidity than these investors realize. All clients should feel comfortable about what investment decisions are being made on their behalf, and why. Ultimately, we believe this is the best way to minimize risk and increase long-term returns.

"All clients should feel comfortable about what investment decisions are being made on their behalf, and why."

—Kevin Burns

How to reach Kevin Burns

I look forward to discussing how LLBH can help you reach your financial goals and can be reached at 800.700.5524.

Left to right: Jim Pratt-Heaney, Bill Lomas, Kevin Burns, Bill Loftus

ILLUSTRATION BY NANCY JANUZZI

About LLBH Private Wealth Management LLC

LLBH Private Wealth Management LLC is an independent registered investment advisor offering a full range of wealth management and family office services, including financial planning, asset management, concentrated stock hedging, lending, cash management and alternative investment due diligence. Often referred to as a virtual family office, LLBH delivers these myriad solutions to its clientele to help bring clarity and control to their financial lives. From its base in Westport, Conn., LLBH provides these services to wealthy families across the country and has a significant West Coast presence focused on the entertainment industry. LLBH works with approximately 140 families approaching $1.6 billion in assets under advisory.

Assets Under Care $1.6 billion (approximately, as of 12/31/2014)

Minimum Fee for Initial Meeting None required

Minimum Net Worth Requirement $10 million (investment services)

Financial Services Experience 200 years (combined)

Compensation Method Asset-based

Primary Custodian for Investor Assets Pershing, A BNY Mellon Company

Professional Services Provided Financial planning, asset management, concentrated stock hedging, lending, cash management, alternative investment due diligence and family office services

Association Membership Financial Planning Association, Investment Management Consultants Association

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