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## **The Attorney As “Complete Advisor” - Fiduciary Ancillary Business Models**

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According to an often quoted study by DALBAR, over the last 19 years the average equity investor earned a paltry 2.57% annually, compared to inflation of 3.14% annually and average annual returns of 12.22% for the S&P 500 Index. Over the same period, the average fixed income investor in bond mutual funds earned 4.24% annually, compared to the long-term government bond index of 11.70%.<sup>2</sup> This underperformance by individual investors in mutual funds can be attributed to various behavioral factors, including attempts to chase the “hot fund,” overconfidence leading to attempts at market timing, and the “flight” emotional response which often causes individual investors to bail from the stock market during market downturns.

Even if the individual investor can conquer the psychological barriers to successful investing, he or she is confronted with an investment marketplace consisting of a plethora of often complicated products and investment strategies, including many types of mutual funds, exchange-traded funds, hedge funds, unit investment trusts, individual stock trading strategies, and variable insurance products. Given the advent of IRAs, 401(k)s, and similar defined contribution plans, and the demise of private sector pension plans promising a lifetime of income, individual investors possess far greater more responsibility for their own financial security than that of prior generations. If proposed Social Security legislation is enacted with “private accounts,” investors will possess even greater control over their financial destinies.

Most individual investors require professional assistance to navigate the investment world, made even more complicated by tax planning opportunities such as differing income tax rates for capital gains, dividends and ordinary income, the ability to defer realization of capital gains through tax efficient investing techniques, deferment of taxation on income through retirement plan or IRA contributions, undertaking Roth IRA contributions and conversions, planning to effect distributions from traditional IRAs and qualified plans at lower marginal rates, and planning to avoid the alternative minimum tax. Individual investors are not generally tax savvy, as evidenced by a study by a major accounting firm which found that investors in actively managed mutual funds (held in taxable

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<sup>1</sup> Please note that the opinions expressed in this article are those of the author alone and should not be viewed as the opinion of The Florida Bar as to the issues addressed.

<sup>2</sup> DALBAR's 2003 update to the *Quantitative Analysis of Investor Behavior*. See Press Release dated July 15, 2003, at <http://www.dalbarinc.com>.

accounts) lose an estimated 2.6% a year over average in annual returns to taxes.<sup>3</sup> Considering that actively managed stock mutual fund costs (both "disclosed" and "hidden") can average 2.8% or more per year,<sup>4</sup> taxes and costs can combine to eliminate 50% or more of an investor's expected annual return in stock mutual funds. On a compounded basis, that 50% annual loss can equate to an erosion of the vast majority of the returns the capital markets have to offer to individual investors.

Estate planning can also affect investment decisions, including what planning for property to gift or devise to either charities or family members and planning for stepped-up basis. Traditional financial planning decisions such as funding of college education expenses still arise, made more complicated by the vast array of new college savings plans available, many with their own set of federal and/or state tax rules.

Within the realm of the legal practice, issues arise as to how the attorney advising a guardian, personal representative, trustee or other fiduciary adequately guide the client in the choice of a financial counselor, including necessary compliance with the prudent investor rule.<sup>5</sup>

How can the attorney help his or her client navigate this maze, especially in a manner which seeks to minimize investment risks while achieving the needed long-term rates of after-tax returns to meet the clients' financial goals, all while keeping total fees, costs and taxes relating to investments low and reasonable? The answer, as suggested by a recent contributor to the *Florida Bar Journal*, is for the attorney to become the "complete advisor."<sup>6</sup> Since that article was submitted for publication, however, the Florida Bar's Professional Ethics Committee ("PEC") issued a final and substantially revised version of Ethics Opinion 02-8 ("EO 02-8").<sup>7</sup> This opinion sets forth important standards of conduct on the attorney who seeks to act as a financial advisor in an ancillary business and refer law firm clients to that business. Accordingly, this article explores the three business models for attorneys who desire to provide financial planning and/or investment services or products in light of the PEC's recent interpretation of the Florida Rules of Professional Conduct.

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<sup>3</sup> KPMG Peat Marwick LLC, *An Educational Analysis of Tax-Managed Mutual Funds and the Taxable Investor* (1999), 14, as quoted in SEC Final Rule: Disclosure of Mutual Fund After-Tax Returns [17 CFR Parts 230, 239, 270 and 274]. The KPMG study analyzed the performance of 496 domestic stock funds for the ten years ended December 31, 1997. The average annual total return for the median fund in this group was 16.1% before taxes and 13.5% after taxes.

<sup>4</sup> Estimates of the total annual average costs of actively managed mutual funds vary, when all fees and costs are taken into account (including sales charges, bid-asked spreads, market impact, and opportunity costs). John Bogle, former Chairman of the Vanguard Group, estimated total mutual fund costs at 3.3% at year. *What Can Active Managers Learn from Index Funds?* Remarks to the Bullseye 2000 Conference, Toronto, Canada, December 4, 2000. For an overview of the costs of mutual funds, see Rhoades, Tringali and Ceparano, *Conversations With An Investor: The Seven Secrets of Investing*, Chapter 8, available as an online publication at [www.josephcapital.com](http://www.josephcapital.com).

<sup>5</sup> The Florida version of the prudent investor rule, embodied in F.S. §518.11 (2004), proscribes additional rules which certain fiduciaries must follow. For more on the application of the prudent investor rule to Florida fiduciaries, see Rhoades, *The Florida Prudent Investor Rule: What Every Judge Should Know and Ask*, a 2004 white paper available online in the Publications section of [www.josephcapital.com](http://www.josephcapital.com).

<sup>6</sup> Stephen A. Taylor, *The Complete Advisor-One Attorney's Case for Ancillary Practices*, *The Florida Bar Journal* (Feb. 2004, p. 46).

<sup>7</sup> Florida Bar Ethics Committee Opinion 02-8 (January 16, 2004) (hereinafter EO 2-8).

## EO 02-8 and the Prohibition On Referral Fees

On January 16, 2004, the third version of EO 02-8 was adopted and subsequently finalized by the Florida Bar's Professional Ethics Committee. EO 02-8 has been interpreted by Florida Bar staff to flatly prohibit an attorney from accepting a referral fee for the referral of a client to a stockbroker, as it now states in the preface to the opinion, "A lawyer may not enter into a referral arrangement with a nonlawyer who is a securities dealer to refer the lawyer's clients to the securities dealer, who would then pay the lawyer a portion of the advisory fee for the clients referred."<sup>8</sup>

While the body of the opinion did not expressly provide this prohibition, EO 02-8 did require all benefits obtained by the lawyer from referrals to financial services to be passed on to the client pursuant to EO 70-13, which states "the client shall receive the benefit of the finder's or referral fee paid by the attorney by the institution seeking the investment."<sup>9</sup> This effects a practical result which, under a combination of EO 02-8 and securities laws, would prohibit payment of referral fees. This is because commission-splitting by broker-dealer firms with entities which are not registered as broker-dealers is generally prohibited.<sup>10</sup> Moreover, while fees may be paid to a "solicitor" by a registered investment adviser firm if certain requirements are met (such as having a contract with the solicitor), the client would not normally meet the requirements for payment as a "solicitor" and hence the passing on of the benefit to the client could not normally occur.

The author notes that several other jurisdictions have found it *per se* unethical for a lawyer to refer a client to an investment advisor and take a referral fee from the commission paid to that advisor under Rule 1.7 and or Rule 1.8.<sup>11</sup> In essence, these state bars appear to conclude that the substantial compensation which could result from the referral fees would create an impermissible conflict of interest between the lawyer's desire to collect the referral fee and the lawyer's duty to the client to make an impartial judgment as to the best investment adviser available, which might or might not be the firm offering the referral fee. The overpowering economic interest of the attorney in such a circumstance would create such an impermissible conflict of interest is not of the type that can be satisfied by consent and disclosure.

Additionally, such pure marketing arrangements, whether they are called referral fees, finder's fees, or kickbacks, could serve to substantially undermine the public confidence which the legal profession must have if its integrity is to be maintained. Regardless of disclosure, without the substantial involvement of the lawyer in the delivery of the financial services there is an appearance of impropriety created when fees are paid to the attorney. Disclosure of the existence of the referral fee does not cure this problem, as clients "view recommendations of other professionals as part of their representation by their lawyers, and expect that lawyers will act as trusted fiduciaries in such matters."<sup>12</sup> Moreover, the payment of a referral fee in the absence of substantial involvement in the provision of the financial services also brings into play rules prohibiting attorney fees which are clearly excessive.<sup>13</sup>

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<sup>8</sup> EO 2-08.

<sup>9</sup> Florida Bar Ethics Committee Opinion EO 70-13.

<sup>10</sup> The SEC has stated that an entity receiving transaction-related income generally is required to register as a broker-dealer. *See, e.g.*, Letter re: Birchtree Financial Services, Inc. (Sept. 22, 1998); Letter re: 1st Global, Inc. (May 7, 2001).

<sup>11</sup> *See, e.g.*, New York State Opinion 682, North Carolina Formal Opinion 99-1, Ohio Opinion 2000-1, and Texas Opinion 536.

<sup>12</sup> N.Y. Op. 682. *See also* Virginia Advisory Ethics Opinion 1998-08.

<sup>13</sup> F.R.P.C. Rule 4-1.5(a).

## EO 02-8: The Fiduciary Standard To Act In The “Best Interests Of The Client”

The second major aspect of EO 02-8 is its imposition upon the attorney, who seeks to refer law clients to an ancillary financial services business in which the attorney has a financial interest, of a broad duty to “act in the best interests of the client”<sup>14</sup> in connection with making the referral. The attorney must also “not allow his or her own personal interest to affect the advice which is given to the client”<sup>15</sup> in connection with the referral. This language evolves from the Florida Rules of Professional Conduct and implies the application of the fiduciary duty of loyalty to the client for the attorney, a duty which has historically been imposed upon attorneys.<sup>16</sup>

Moreover, EO 02-8 requires, as to standards of conduct which arise in connection with the services or products actually provided by the ancillary business, that: (1) the nature of the business relationship with the client is fair and reasonable to the client; (2) the terms of the business relationship are fully disclosed and transmitted in writing to the client in a manner that can be reasonably understood by the client; (3) the client is given a reasonable opportunity to seek the advice of independent counsel in the transaction; (4) the client consents in writing to the relationship; and (5) the lawyer advises the client, preferably in writing, that the services provided under the ancillary business are non-legal and that the protections of a lawyer-client relationship (including but not limited to attorney-client privilege) are not available.<sup>17</sup>

EO 02-8 therefore requires the attorney to ensure, through a due diligence process, that the financial services and/or products to be delivered through the ancillary business, and the fees and costs incurred by a referred client in connection therewith, are fair, reasonable, fully disclosed, and in the client's best interests. The author submits that this imposes upon the attorney substantial requirements. For example, the attorney to ensure that the client receives from the ancillary business a comprehensive, easily understood listing of all fees and costs the client is likely to bear in association with the recommended action. The attorney should also ensure that the ancillary business provide full disclosure of any and all material conflicts of interests to the client. Moreover, the attorney should analyze any material conflicts of interest to ensure the referred client's interests are not impaired thereby.

While all of the dictates set forth by EO-8 are important, the requirement that the referral be in the “best interests of the client” implies fiduciary duties of due care and loyalty upon the attorney in undertaking the referral. It should be noted that the very strong and broad duties imposed upon fiduciaries are far more stringent than that required of ordinary persons engaged in commerce. As Justice Cardozo observed, “Many forms of conduct permissible in a workaday world for those acting at arm's length are forbidden to those bound by fiduciary ties. A trustee is held to something stricter than the morals of the market place. Not honesty alone, but the punctilio of an honor the most sensitive is then the standard of behavior.”<sup>18</sup> Moreover, to paraphrase Supreme Court Justice Brandeis, acting as a

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<sup>14</sup> EO 2-08.

<sup>15</sup> *Id.*

<sup>16</sup> *See Florida Bar v. Burton*, 218 So. 2d 748, 749 (Fla. 1969) (“The judgment of disbarment is certainly justified when an attorney misappropriates funds which he receives by virtue of his fiduciary relationship with his client.”); *See also* comments to F.R.P.C. Rule 4-1.6, “Confidentiality of Information,” where, in discussing fee disputes, it states: “This aspect of the rule expresses the principle that the beneficiary of a fiduciary relationship may not exploit it to the detriment of the fiduciary.” *See also* comments to Rule 5-1.1. dealing with trust accounts, which states, “A lawyer must hold property of others with the care required of a professional fiduciary.”

<sup>17</sup> EO 02-8.

<sup>18</sup> *Meinhard v. Salmon* (N.Y. 1928) 164 N.E. 545, 546.

fiduciary “is an occupation which is pursued largely for others and not merely for oneself. It is an occupation in which the amount of financial return is not the accepted measure of success.”<sup>19</sup>

### **The Three Main Types of “Financial Consultants.”**

There are three regulated professions today which provide investment advice and/or financial products to their clients - insurance agents and brokers (hereinafter “insurance agents”), registered representatives of broker-dealer firms (hereinafter “registered representatives”), and representatives of registered investment adviser firms (hereinafter “investment advisors”). At times a financial consultant may be acting in two or three of such roles. Each of these professions is regulated under different rules and each individual practicing in these professions is held to different standards of conduct. The attorney seeking to provide financial services through an ancillary business should carefully consider his or her choice of business model in light of EO 02-8.

### **The Insurance Agent Business Model.**

F.S. §626.112(1) (2004) requires the registration of insurance agents. Generally, separate licenses are issued through state licensing procedures for property/casualty insurance agents, health insurance agents, and life insurance agents. Requirements to become an insurance agent involve taking a course (of varying length, usually up to 40 hours) followed by passage of an exam.

An insurance agent is traditionally defined as a licensed individual or organization authorized to sell insurance by or on behalf of an insurer. An agent has binding authority from insurance companies and generally does not charge a fee to the client. Insurance brokers, however, might charge a fee to the client (which might be paid directly by the client or through commission from the insurer), and may represent the customer in negotiation with various companies. However, the distinctions between insurance agents and insurance brokers have substantially blurred,<sup>20</sup> and most insurance brokers serving individual investors are paid through commissions only, by the insurer, from the sale of an insurance product.

Florida insurance regulations prohibit certain deceptive or fraudulent conduct, including twisting, defamation and misrepresentations, and impose upon insurance agents certain duties which may be deemed “fiduciary” in nature.<sup>21</sup> Under principles of agency law, however, insurance agents also owe a fiduciary duty to the company they represent.<sup>22</sup>

The dual allegiances which exist for the ancillary business, as well as the wide variance of commissions payable upon different types of life insurance products (such as between term and universal life insurance), gives rise to difficulties in compliance with EO 02-8. For example, an attorney who advises a law client how much insurance and what type

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<sup>19</sup> Supreme Court Justice Louis M. Brandeis in his 1914 book, *Business - A Profession*. In Brandeis's view, a profession has three characteristics. First, it is an occupation for which the necessary training is intellectual, involving knowledge and learning as distinguished from skill. Second, it is an occupation pursued largely for others. Third, it is an occupation in which the amount of financial return is not the accepted measure of success.

<sup>20</sup> Insurance brokers can possess obligations to both the insurers and insurance consumers. Unless there is an agreement otherwise, an insurance broker does not represent or speak with authority on behalf of either the insurance consumer or the insurer. Even though an insurance agent is the appointed representative of an insurer in the insurance marketplace, and as such speaks and acts with a level of some authority on behalf of that insurer (or insurers), the law also expects the agent to know and execute their obligations to the insurance consumer.

<sup>21</sup> See F.A.C. § 69B-215.210 to 215.230, as to standards of conduct imposed upon life agents.

<sup>22</sup> Florida Bar Ethics Committee Opinion 90-7.

of insurance is needed, and then sells that client the insurance, possesses an inherent conflict of interest of a type “that cannot be cured by asking for the client’s consent.”<sup>23</sup> While the Florida Rules of Professional Conduct do not, *per se*, prohibit attorneys from selling insurance through an ancillary business to their law firm clients, differences of opinion may occur as to the appropriateness of the type and specific policy chosen. Given the wide variance in the amount of commissions paid under different insurance policies, this poses serious concerns for the attorney who must later demonstrate that he or she has not allowed his or her own personal interest to affect advice given to a client. This is particularly so with the advent of “low-load” life insurance policies in recent years as well as term life insurance policies with longer periods for conversion to permanent forms of insurance without further need of medical examination of the insured.

### **The Registered Representative Business Model.**

F.S. §517.12(1) (2004) requires the registration of the sellers of securities. These are often referred to as “securities brokers” or “stockbrokers,” but more accurately they are “registered representatives” of a “securities broker-dealer” firm. At the state level, registered representatives generally must possess either a Series 6 license (for mutual funds sales, generally) or Series 7 license (for mutual fund, individual stock and other security sales, generally). Regulation is also provided by the U.S. Securities and Exchange Commission (“SEC”) pursuant to the Securities and Exchange Act of 1934 (“SEA”), as amended and the NASD (a self-regulatory organization). Under Section 3(a)(4) of the SEA a “broker” is defined broadly as any person engaged in the business of effecting transactions in securities for the account of others. Attorneys who seek to provide financial services through an ancillary business and act as a registered representative would typically associate with an existing broker-dealer firm.

Brokers have statutorily or regulatory imposed duties, including the duty of “suitability.” Under the suitability doctrine, the registered representative must believe that his or her recommendation to a customer invest in the security is suitable for that particular investor. To reach this determination, a registered representative must, in accordance with NASD Rule 2310, examine the investor’s financial status, tax status and investment objectives, as well as any other pertinent information. In addition, NYSE’s “Know Your Customer Rule” requires NYSE members (and their firm’s registered representatives) to use due diligence to learn the essential facts relative to every customer, every order, every cash or margin account accepted or carried by the member, and every person holding a power of attorney over any account. Violations of suitability obligations have been among the most frequently asserted arbitration claims by investors who have experienced trading losses.

While the suitability doctrine imposes a limited form of fiduciary duty, the registered representative in Florida does not generally possess a broad fiduciary duty to his or her customer. As stated in recent comments by the Financial Planning Association to the SEC, “some attorneys in the securities bar will argue that the suitability duty is very similar to a fiduciary obligation, or that all brokers are fiduciaries, but this is not correct.”<sup>24</sup> Rather, under principles of agency law, and similar to the relationship held by insurance agents, the fiduciary duty of a broker lies to his or her principal - the securities brokerage firm, and not generally to the client. However, certain factors can transform the relationship with the customer into one in which fiduciary status is conferred and broad fiduciary duties to the customer are imposed, such as when discretion is obtained over a customer’s fee-based account and other

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<sup>23</sup> *Id.*

<sup>24</sup> Comments of Duane R. Thompson, Group Director, Advocacy, Financial Planning Association, Sept. 22, 2004, regarding Release Nos. 34-42099; IA-1845; File No. S7-25-99 (“Certain Broker-Dealers Deemed Not To Be Investment Advisers”).

circumstances exist in which investment advisory services rendered are no longer “solely incidental” to a securities brokerage transaction.<sup>25</sup>

### **The Investment Adviser Business Model.**

F.S. §517.12(3) (2004) requires the registration of investment advisers. These are more accurately referred to as “investment adviser representatives” of a “registered investment adviser” (RIA) firm. A Series 65 or 66 license is required for an individual to become an investment adviser. The State of Florida regulates smaller RIA firms, with larger RIA firms (i.e, generally those with over \$30 million of continuously managed assets) regulated by the Securities and Exchange Commission pursuant to the Investment Advisers Act of 1940 (“Advisers Act”), as amended.

Providing financial advice to clients, even in the most basic circumstances, could require the individual or firm to register with the SEC or the Florida Department of Financial Services (Office of Financial Regulation) as a Registered Investment Adviser. The term “investment adviser” is defined by Florida Statutes to include “any person who for compensation engages for all or part of her or his time, directly or indirectly, or through publications or writings, in the business of advising others as to the value of securities or as to the advisability of investments in, purchasing of, or selling of securities ....”<sup>26</sup> Exceptions are provided to any “licensed practicing attorney whose performance of such services is solely incidental to the practice of her or his profession” and to “any person who does not hold herself or himself out to the general public as an investment adviser and has no more than 15 clients within 12 consecutive months in this state.”<sup>27</sup> Given the limited scope of these exemptions, however, most attorneys who desire to provide investment advisory services will be required to register, especially if there is any “holding out” as an investment adviser.<sup>28</sup>

The regulatory scheme imposed upon investment advisory firms is generally regarded to be stricter than that imposed upon registered representatives. For example, under the “brochure rule” an RIA firm must provide to the client the information set forth in Form ADV, Part II, which contains a multitude of disclosures about the RIA firm, its fees, and its representatives. Additionally, RIA firms are prohibited from utilizing client endorsements in advertising. Additionally, investment advisers are prohibited from “[f]ailing to disclose to customers in writing before any advice is rendered any material conflict of interest relating to the adviser or any of its employees which could reasonably be expected to impair the rendering of unbiased and objective advice ....”<sup>29</sup>

Investment advisers may charge clients in a variety of ways. The most common form of compensation is payment of a quarterly or other periodic fee based upon a percentage of the “assets under management.” Other investment advisers charge hourly fees, flat fees, or some combination of the foregoing.

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<sup>25</sup> The SEC is currently considering ways to further define the “solely incidental” brokerage exception to the Investment Advisers Act of 1940, as it relates to fee-based brokerage accounts, and has promised action by April 15, 2005. See Proposed Rule, *Certain Broker-Dealers Deemed Not To Be Investment Advisers*, [Release Nos. 34-50980; IA-2340; File No. S7-25-99], January 7, 2005, available at [www.sec.gov](http://www.sec.gov).

<sup>26</sup> F.S. §517.021(13)(a).

<sup>27</sup> F.S. §517.021(13)(b).

<sup>28</sup> See Myers, Krause & Stevens (no-action letter publicly available August 31, 1988) (a law firm engaged primarily in estate planning and administration also engaged in and held itself out as providing financial planning to its clients. A client requested a lawyer in the firm to serve as trustee. The SEC staff responded: “The exception is not available to a lawyer who holds himself out to the public as providing financial planning services.”).

<sup>29</sup> See F.A.C. Rule 68W-600.0131(1)(k), and generally F.A.C. 68W-600.

It should be noted that while the term “financial planner” is often used, the financial planning profession remains largely unregulated as a separate profession. Rather, “financial planners” may be either insurance agents, registered representatives, or investment advisers. However, the most common registration required of the financial planner is that of an investment adviser.<sup>30</sup>

Attorneys who desire to engage in the investment advisory profession as an ancillary business would first study for, take and pass the Series 65 exam (unless excepted by reason of holding certain designations, such as Certified Financial Planner<sup>®</sup>). The attorney might then associate as an investment adviser representative with an established RIA firm, and this might offer a quick and relatively easy method to enter the profession. However, the attorney must take great care in the selection of the RIA firm. A due diligence process is required, as the attorney should ascertain whether low cost and tax efficient investment products can be obtained on the platform presented. The attorney should be aware that many low-cost, institutional-style products are not available through some RIA firms (as is the case with some broker-dealer firms). Moreover, the attorney should ascertain whether the RIA firm’s investment philosophies coincide with those of the attorney and are in the best interests of the client. Additionally the attorney should determine whether the investment skill and philosophies utilized, the level of initial and ongoing planning and other services provided, and the fee structure employed by the RIA firm, are appropriate to ensure that substantial benefits to the clients will result.

An alternative method for entry into the investment advisory profession is the formation of an independent RIA firm and its registration with the state or the SEC. In connection with the formation of such a firm a great number of ongoing “compliance” requirements are imposed, including net capital requirements, advertising restrictions, and disclosure requirements. The attorney should also research options as to custodian selection, professional liability insurance, portfolio management software, client relationship management software, and investment policy statement formation. In addition, efforts should be made to secure access for the newly formed firm to low-cost, institutional-style mutual funds and other investment products. Marketing materials, client fee agreements, client disclosure forms, and various required compliance procedures and manuals should be developed. These elements add up to make the formation of an independent investment advisory firm somewhat costly and/or time intensive, although certain “turnkey” providers can offer assistance. Nevertheless, for the law firm consisting of one or more principals willing to champion the ancillary business, and for the firm which can devote sufficient resources to the ancillary business until it is self-sustaining, the formation of an independent RIA has potential long-range benefits, both in terms of independence of product selection and in terms of long-term profitability and building of equity.

At all times, the attorney practicing in an ancillary business as an investment adviser should be competent to provide the services required. Should the attorney desire to utilize the talents of others within the RIA firm to supplement the attorney’s knowledge and experience, the attorney should be knowledgeable enough so as to judge the competency of the other service providers. While the scope of knowledge required to provide comprehensive financial planning and investment advisory services is both broad and ever-changing, the author suggests that a minimum level of knowledge would include (but would not be limited to) knowledge of the following: (1) Modern Portfolio Theory; (2) the Efficient Markets Hypothesis; (3) global strategic asset allocation, including the historical relative rates of return and volatility of various asset classes and the effects of combining different asset classes in an investment portfolio; (4) the costs and potential benefits of passive and active investment management; (5) the

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<sup>30</sup> SEC Release No. IA-1092 (October 8, 1987). It should be noted that this release may be subject to modification during 2005 as the SEC considers its Temporary Rule on the broker-dealer exception to the Advisers Act (*see* Proposed Rule, *infra* at note 25).

fees and costs of various investment products; and (6) the tax characteristics of various investments and the various methods by which the "tax drag" on investment returns can be minimized in the construction of investment portfolios. Given the broad base of knowledge required, a team approach - involving investment advisor representatives who originally hail from different disciplines, such as accounting, law, and financial services - may prove most effective in serving the diverse planning needs of an RIA firm's clients.

### **Conclusion.**

Since investment advisers are required to disclose any facts that might cause the adviser to render advice that is not objective and must affirmatively disclose their disciplinary histories,<sup>31</sup> and since investment advisers possess clear status as fiduciaries, attorneys seeking to adhere most closely to the dictates of EO 02-8 might find this business model for an ancillary services firm to be more attractive. However, with an appropriate amount of initial and ongoing due diligence, and with the adoption of certain additional policies and procedures, under EO 02-8 an attorney may also provide financial services as either an insurance agent or a registered representative.

Justice Harlan Fiske Stone once observed: "Most of the mistakes and major faults of the financial era that has just drawn to a close will be ascribed to the failure to observe the fiduciary principle, the precept as old as holy writ, that 'a man cannot serve two masters.'" <sup>32</sup> Given the necessity for an attorney to act in the best interests of his or her client in undertaking a referral to a financial services provider in which the attorney possesses an interest, as required by EO 02-8, the attorney should seek to secure an ancillary business model, with adequate policies and procedures adopted within ancillary business, to ensure the client's best interest remain paramount.

Clients are increasingly seeking out objective, trusted advisors. With their analytical training, often detailed knowledge of estate planning and taxation, and existing ethical framework of advancing client interests ahead of their own, many attorneys may be uniquely positioned to become "trusted advisors" to their clients in matters involving financial advice and investment advice. With strict adherence to an ancillary business structure which keeps the clients' best interests first, and a commitment to lifelong education in the many areas which might impact a client's lifetime financial goals, an attorney can provide truly holistic services and become a "complete advisor," either alone or in conjunction with a team of professional advisors.

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<sup>31</sup> 17 C.F.R. 275.204-3; F.A.C. 69W - 600.0131(1)(k).

<sup>32</sup> Stone, *The Public Influence of the Bar* (1934) 48 Harv. L.Rev. 1, 8-9.