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Barriers to Financial Advice For Non-Affluent Consumers

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SECTION 1: EXECUTIVE SUMMARY

1.1 Introduction and Research Objective

Millions of Americans are at risk of entering retirement without the resources necessary to maintain their standard of living and provide the financial security they need for their retirement years.[1,2] Data from both the Health and Retirement Study and the Retirement Confidence Survey demonstrate that many workers approach retirement with very low amounts of wealth.[3] For the middle class, recent economic trends of rising debt,[4] personal bankruptcies[5] and foreclosures[6] tell a clear story of families struggling just to make ends meet.

A number of factors have contributed to what many have called a "retirement savings crisis," including the shift from defined-benefit to defined-contribution employer retirement plans,[7-11] the sustained rises in health care costs,[12-14] increased life expectancy[15] and the possibility of future reductions in government-provided retirement benefits. These factors, along with the growth and increasing complexity of offerings in the marketplace of financial products and services,[9] call for a more financially sophisticated American consumer.[16,17]

All of this contributes to a greater need for financial advising that goes well beyond 'investment advice.'[18] The transition from defined-benefit to defined-contribution pensions, in particular, has shifted the burden of retirement planning onto the shoulders of American consumers. Rather than providing a lifelong benefit as defined-benefit pensions do, defined-contribution pensions require that employees manage privately held accounts, which may be vulnerable to poor investment choices by employees who do not have adequate knowledge to manage their funds.[19] The 2001 Survey of Consumer Finances found that not only do defined-contribution pensions dominate the retirement income profile of the middle class, but defined-contribution assets constitute over half of middle class families' financial assets.[18]

Although Americans' individual responsibility for their own retirement has increased over the past few decades, their financial knowledge and planning has simply not kept pace. Specifically, there appears to be a widespread lack of both financial knowledge and formal, long-term financial planning among the middle class.[20-23] For example, Annamaria Lusardi et al. argue that lack of planning is supported by the data that demonstrates how little workers know about their pensions or the rules governing Social Security Benefits.[3] Further, the 2009 FINRA Financial Capability Study found that "the majority of Americans do not plan for predictable life events, such as their children's college education or their own retirement," with only 42 percent reporting that they have ever tried to even figure out how much they need to save for retirement.[24]

The need for professional, customized financial advice is compelling: the complexity and uniqueness of each person's financial situation and retirement savings challenge require customized solutions, which in many cases are best delivered by properly credentialed, trained and motivated professionals.[25]

This need is acknowledged in both academic and practitioner circles. For example, writing from a research perspective in *The Journal of Consumer Affairs*, John Kozup and Jeanne Hogarth explain why the role of third-party advice is crucial:

> In today's complex financial marketplace, it can take a great deal of motivation, ability, and opportunity to sort through both relevant and irrelevant data necessary to make optimal decisions. This asks a great deal of consumers, many of whom face the pressures of time poverty as well as limited financial resources. Others simply cannot or do not want to perform all the tasks needed to optimize their financial situation (i.e., set decision criteria, diligently search for information, weigh attributes, and evaluate alternatives). Furthermore, these financial decisions are highly person or household specific: one family's decision may not work for another. And even if consumers go through a rigorous decision-making process, there can be problems with implementation.[25]

Writing from a practitioner standpoint in *Accounting Today*, CPA Kent Irwin forms a similar argument:

> People and society are at risk. Those in the middle market are not taking full advantage of their 401(k) plans, buying adequate insurance protection, or saving for future needs such as emergencies and college education. This puts the financial security of Americans at risk, possibly leading to greater dependence on entitlement programs, which would not be good for the US economy…Part of the blame falls on economic conditions: high gasoline and health care costs, the demise of high paying domestic manufacturing jobs, and the sub-prime mortgage market. Some may lack self-discipline, or perhaps they may not have been taught personal financial management in school or at home. *Regardless of the causes, people need help* [italics added].[26]

However, despite the need, the data consistently demonstrate that non-affluent consumers are not accessing financial advice from licensed and informed professionals. Fewer than half (47 percent) of all consumers have ever used the services of a financial

professional for retirement planning, a trend that has persisted since at least the 1980s.[27,28]

The use of licensed and informed professionals for financial advice is primarily concentrated among affluent consumers.[29,30] For example, a 2006 survey by the Financial Planning Association (FPA) found that only 11 percent of its members serve clients with a net worth below $250,000. FPA members are providing financial planning services to about one to two percent of the potential 108 million households in the middle market.[31] A more recent FPA survey confirmed these trends, finding that non-affluent consumers are less likely to *seek or receive* financial advice.[30]

The low utilization of financial advice by non-affluent consumers is particularly troubling in the current economic environment. For example, Karin Maloney Stifler of True Wealth Advisors argues that the recent market downturn “makes it even more important that middle-market clients have access to affordable quality financial planning advice…[but] we all need to work together to change the idea that planning is only for the wealthy.”[32] Such research establishes that to understand the barriers to financial advice for non-affluent Americans, one must examine both the *seeking of advice* by consumers and the *delivery of advice* by professional financial advisers.

The objective of this study is to identify and explain the barriers to professional, customized financial advice among non-affluent households in the U.S. As such, this study centers its attention on the threshold question of why financial advice is not delivered to or sought by this group.

This paper represents Phase 1 of a two-phase effort by the Society of Actuaries' (SOA), Product Development Section and Actuary of the Future Section. While Phase 1 focuses on identifying and explaining barriers to professional, customized financial advice, Phase 2 will focus on strategies for overcoming these barriers.

1.2 Methods

LITERATURE REVIEW

This study reviews the research on providing individualized financial advice to non-affluent households, as well as the larger body of research on providing general financial education to non-affluent households. The review and analysis of the larger field of financial education generate insights on critical issues relevant to the financial advice field.

To address the research question, the Financial Literacy Group (FLG) conducted a systematic literature review that evaluates and synthesizes primary empirical research, analysis of national data sets,[i] practitioner advice, and select news and opinion pieces. The literature review drew from the following types of sources:

- Peer-reviewed academic journals (e.g., *Financial Counseling and Planning, Financial Services Review, Journal of Personal Finance, Journal of Consumer Affairs, Journal of Family and Consumer Sciences, Journal of Family and Economic Issues*)
- Reports and working papers from established national research and policy institutions (e.g., National Bureau of Economic Research)
- Publications written toward a practitioner audience (e.g., *Financial Planning, Journal of Financial Planning, Advisor Today*)
- Select articles in the popular financial press (e.g., *Money Magazine*).

INTERVIEWS WITH NATIONAL EXPERTS

The literature review was complemented and refined by a series of in-depth, semi-structured interviews with a range of researchers, policymakers and practitioners in the financial literacy and financial advice fields. These interviews allowed for extensive exploration and explanation of the barriers to participation in financial advice.

The interviews provide a more focused and nuanced understanding of the barriers: how they are formed, reinforced and reproduced; how they function; and how they may be overcome. The interviews also allowed for midstream adjustments to conceptualization of the barriers identified in this study, determining if and how they should be modified.

[i] These data sets include: the Federal Reserve Board’s Survey of Consumer Finances, the Financial Industry Regulatory Authority Foundation’s National Financial Capability Study, Rand’s American Life Panel and the University of Michigan’s Health and Retirement Study.

RESEARCH PHASES

The research process consisted of five phases for identifying and refining the barriers.

- Phase 1: Initial scan of the literature.
- Phase 2: Development of preliminary findings.
- Phase 3: Semi-structured interviews with national experts to refine the initial findings.
- Phase 4: Systematic literature review.
- Phase 5: Synthesizing and consolidating the findings into barriers, based upon an integrated analysis of the total body of data—the interviews, existing research and national data sets.

1.3 Key Findings

THREE TIERS OF BARRIERS

The results of this study are organized according to a three-tiered framework for conceptualizing barriers to financial advice. The three tiers are: individual, social and institutional. All three shape the development and reproduction of the barriers that prevent non-affluent consumers from accessing and participating in financial advice.

Barriers operating at the individual level have to do with a consumer's internal attitudes, knowledge and decisions around seeking and utilizing financial advice. Barriers operating at the social level involve the processes by which interpersonal interactions and group dynamics reduce participation in financial advice. These include consumer social interactions within his or her immediate social sphere (friends, family, spouses and partners, colleagues, etc.), as well as interactions among consumers and financial advisers. Barriers operating at the institutional level are the result of structural policies and macroeconomic factors that shape the opportunities, constraints and incentives for providing financial advice.

The barriers described in this paper are conceptualized as patterns of communication and behavior between: a) non-affluent consumers and b) professional financial advisers and their firms. The value of the three-tiered framework is that it demonstrates how both parties to this transaction are affected by individual, social and institutional forces. Although the barriers ultimately cross the individual, social and institutional dimensions, this study's three-tiered framework provides a robust approach for a better understanding of how these barriers function—and how they can be overcome. The barriers are summarized below:

INDIVIDUAL-LEVEL BARRIERS

- Many non-affluent consumers lack the basic financial knowledge that is necessary to seek and utilize financial advice.
- There is a widespread misunderstanding of the process and value of financial advice.
- Non-affluent consumers often do not trust – and therefore avoid – financial advisers who also sell products due to the perceived conflict of interest.[ii]

SOCIAL-LEVEL BARRIERS

- Many non-affluent consumers only seek financial advice from informal sources, such as family and friends, because they view these sources as inherently trustworthy.
- Professional financial advisers often do not have the necessary social relationships and community connections to access the non-affluent market.
- There is often a cultural disconnect between financial advisers and non-affluent recent immigrants.
- Strong and pervasive gender roles often reduce financial advice utilization by couples.

INSTITUTIONAL-LEVEL BARRIERS

- Most financial advising firms have not traditionally focused on non-affluent consumers because they are less profitable. Further, most firms and advisors either cannot afford or do not want to make the long-term, high-involvement investment that is necessary to cultivate business with such consumers.
- The structure of the provision of financial advice incentivizes selling products, which often sets up an inherent conflict of interest in which advisers sell more products and services to a particular client than is prudent in order to maximize profits.
- The recent turmoil in the financial markets has significantly lowered American consumers' confidence and trust in the financial services profession.

[ii] Note that *conflict of interest* represents the general meaning of the term as is used in popular press and common usage. This report is not using the technical meaning of the term to connote that professional standards and codes of ethics are systematically being breached.

1.4 Limitations and Conclusion

This paper focuses on two main categories of non-affluent consumers: low wealth and moderate wealth. Although a range of metrics are used across academic, financial and government sectors to define these two categories, for the purposes of clarity, this paper defines low wealth consumers as having a net worth below $100,000, and moderate wealth consumers (popularly referred to as the “middle market”) as having a net worth in the range of $100,000-$500,000. Generally, the data reviewed did not allow for quantifying the differential effects that the barriers have on low versus moderate wealth consumers. Very few empirical studies provide data that would allow such comparisons to be made. However, where possible, the paper specifies whether a barrier is more prevalent for a particular category.

Similarly, although this paper confirms that non-affluent consumers seek and utilize financial advice significantly less than affluent consumers, it does not attempt to identify the prevalence of the barriers or the degree to which they operate for affluent consumers. Nonetheless, this paper points to wealth-specific trends in the seeking and delivery of financial advice when the data is available.

The analysis and interpretation of the research reviewed and interviews conducted for this study suggest that the barriers group into larger themes that cut across individual, social and institutional levels. These themes are: trust and personal relationships; cost, price and value; and access and facilitation.

The findings from this study have significant implications for practitioners who are increasingly expanding beyond their narrow focus on affluent clients. Several firms have begun attempting to serve the middle market. Many of these firms are struggling to accomplish this goal, and have reversed their efforts after a short time because the endeavor appeared to be financially unsustainable. This paper identifies barriers that such firms have encountered, as well as barriers that many may not have identified, all of which may prove valuable as the financial advising profession continues to evolve.

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SECTION 2: FINDINGS

2.1 Individual-Level Barriers

This section focuses on the barriers that operate at the individual level of the non-affluent consumer. The research presented in this section indicates that individual-level experiences, knowledge and cognitive phenomena affect consumers' decision-making processes and behaviors regarding seeking and utilizing financial advice. This section is grouped into three core barriers:

BARRIER 1: MANY NON-AFFLUENT CONSUMERS LACK THE BASIC FINANCIAL KNOWLEDGE THAT IS NECESSARY TO SEEK AND UTILIZE FINANCIAL ADVICE.

This section utilizes the literature on Americans' general financial literacy to argue that many lack the "on-ramp" knowledge that often functions as a prerequisite for pursuing and utilizing financial advice. That is, the evidence indicates that a baseline level of financial literacy is necessary in order to seek and utilize financial advice. This is important because it directly challenges the concept that financial advice can function as a substitute for basic financial literacy. If a consumer's lack of knowledge causes him or her to avoid professional advice in the first place, then the adviser cannot play a role in guiding that consumer through more complicated financial issues.

The research shows that many non-affluent Americans lack a basic working knowledge of the mainstream financial products and government programs associated with retirement planning.[33] For example, an analysis of data from the 2007 Health and Retirement Study (HRS)[iii] found that

> Half of older workers do not know which type of pension they have and fewer know about their pension wealth. Many workers could not even venture a guess about their Social Security wealth. Despite many years of annual mailings of individual benefit statements from the Social Security Administration, less than twenty percent of workers in the population knew the correct age at which they were entitled to full Social Security benefits.[3]

[iii] The HRS is sponsored by the National Institute on Aging under a cooperative agreement with the University of Michigan. It follows more than 20,000 men and women over 50, offering insight into the changing lives of the older U.S. population. Launched in 1992, this multidisciplinary, longitudinal study has become known as the nation's leading resource for data on the combined health and economic conditions of older Americans.[34]

To test the relationship between financial literacy and planning, Lusardi and Mitchell devised and fielded a module of questions for the 2004 HRS. Summarizing the results in a National Bureau of Economic Research (NBER) working paper, Lusardi finds widespread lack of critical financial knowledge regarding retirement and investments:

> Most individuals cannot perform simple economic calculations and lack knowledge of basic financial concepts, such as the working of interest compounding, the difference between nominal and real values, and the basics of risk diversification. Knowledge of more complex concepts, such as the difference between bonds and stocks, the working of mutual funds, and basic asset pricing is even scarcer.[35]

Lusardi and Mitchell interpret these data to conclude, "financial illiteracy is widespread among older Americans."[22] Critically, they also found that low financial literacy is correlated with lack of financial planning: holding constant for race, gender and other demographic variables, both the knowledge of interest compounding and the ability to perform simple calculations are the strongest predictors of financial planning.[35]

On a closely related note, the lack of even a very basic level of financial knowledge can keep people from engagement with important financial products. This relationship between financial literacy and the willingness to invest was confirmed by Yoong, who analyzed data from the RAND American Life Panel to find that individuals with lower financial knowledge are less likely to participate in the stock market. This finding is consistent with the behavioral economics principle of ambiguity aversion: people avoid what they do not understand.[36]

Ultimately, without basic financial literacy, consumers get intimidated out of pursuing advice. When they do have prospective conversations with professional financial advisers, many become alienated or overwhelmed by the jargon. Indeed, lack of basic financial knowledge and experience has a strong emotional and cognitive component. Pam Krueger, co-host of the PBS television program *MoneyTrack*,[iv] points out the shame and embarrassment many feel about their lack of knowledge. Therefore, Krueger contends that going to a financial adviser makes some consumers feel potentially "stupid or ignorant." As she put it:

> This is the intimidation factor: people feel ashamed by what they don't know. It feels like dirty laundry. They don't know what kind of jargon that person (the financial adviser) is going to throw at them. So first they need to know that jargon, like what is an annuity, and then they can go talk to someone who is going to advise them on annuities.[37]

[iv] Krueger is an investment expert who created *MoneyTrack* in 2005. *MoneyTrack* is a weekly half-hour public television series about personal finance and investing. The show features stories about average investors and advice from investing experts like John Bogle, Warren Buffett and Ben Stein, and has recently partnered with MSN Money, a heavily-trafficked personal finance website.

Similarly, in his discussion of why the middle market is not being served, Irwin notes, "many people are 'financially shy' of having to reveal their financial mistakes, mishaps, or insufficient funds."[26] To this point, financial planner Bert Whitehead explains the potential of the financial adviser:

> People have so many choices with their 401(k) plans, insurance and college investing needs, they're confused and don't understand the jargon. If, in a six-month period, I can get an individual a will, help them set up a Roth IRA, get them investing regularly in and outside of a qualified plan and make sure their insurance needs are met, I have changed that person's life forever.[38]

Finally, consumers who lack basic working financial knowledge, but nonetheless seek financial advice, are more likely to suffer from the dynamics of asymmetry of information[v] by paying higher fees at best and falling victim to predatory schemes at worst.[39] This perpetuates a cycle of avoiding financial advice because those consumers will generate negative word of mouth. Moreover, many potential consumers of advice have been scared off by the prominence of news stories that reestablish the familiar story line of naïve consumers who are taken advantage of by the sophisticated, unscrupulous financial professional.

Even if, on average, most consumers will not be victimized, the possibility that they could be taken advantage of without even knowing it undercuts the prerequisite confidence those consumers need to put themselves and their finances in the hands of an adviser.

[v] Information asymmetry models assume that at least one party to a transaction has relevant information whereas the other(s) do not. Some asymmetric information models can also be used in situations where at least one party can enforce, or effectively retaliate for breaches of, certain parts of an agreement whereas the other(s) cannot.

BARRIER 2: THERE IS A WIDESPREAD MISUNDERSTANDING AMONG NON-AFFLUENT CONSUMERS OF THE PROCESS AND VALUE OF FINANCIAL ADVICE.

The previous section presented the evidence on how the lack of basic financial knowledge creates a barrier to financial advice. This section now profiles the evidence on consumer knowledge and consumer experience with professional, individualized financial advice more deeply.

Both academic research and the literature for financial advisers consistently demonstrate that, among non-affluent consumers, there is a considerable lack of knowledge about the process and value of professional financial advice. Indeed, many of the articles written for financial planners and advisers stress the critical need to educate clients on the nature and value of financial advice.[40]

One fundamental component of this barrier is the “alphabet soup” of certifications in the financial advising industry. These certifications include Certified Financial Planner (CFP®), Certified Public Accountant (CPA), Accredited Investment Fiduciary (AIF®) and Accredited Financial Counselor (AFC).

The second fundamental component of this barrier is a misunderstanding of the potential value of financial advice. Non-affluent consumers are willing to spend money on services that are perceived to provide value. However, many of them do not know what financial advice actually consists of, what it costs, and what its benefits are. As Beth Hirschhorn, Senior Vice President & Chief Marketing Office of MetLife, Inc., put it:

> Financial advice is often perceived by middle market consumers as high cost because you cannot find the price. It’s not transparent. If you search for the price on the Internet, you cannot find it. So consumers know that, for financial products, the cost is not clear. There is also no rule of thumb for consumers to follow: What should it cost for specific advice and products, and what will I get out of that?[41]

These two components, discussed in greater detail below, cause many non-affluent consumers to think that the cost of financial advice outweighs its value, and is therefore too expensive.

Non-affluent consumers generally do not know what working with a financial adviser actually entails. Although financial advice can involve a broad range of topics—from managing cash flow, to planning for college, to long-term care insurance—non-affluent consumers generally do not receive this message.[42-48] The research shows that public perception equates financial advice with high-risk investing.[49] As will be discussed in the

section on institutional-level barriers, this misperception has been given credence in the last few years with a series of high-profile news stories about financial advisers who sold their clients—sometimes inappropriately—overly-risky investments. Indeed, since 2008, the public view has turned to an even more risk-laden perception of financial advice, one that equates any kind of financial investing with high-risk investing.[50] Compounding this risk-laden perception of financial advice are two additional factors: most people are not equipped to consider long-term issues of risk, and American consumers tend to be extremely risk-averse.[51] The result is that non-affluent consumers commonly equate financial advice with financial risk, which they avoid because they do not understand it.

Further, many non-affluent consumers think that they cannot afford financial advice. Traditionally, this belief closely reflected the reality that wealth management advisers required high minimum balance—typically half a million to one million dollars—and primarily targeted only high-net-worth clients. While affluent consumers remain the most desired client base for many in the financial advising industry, a growing number of firms are targeting the middle market with a range of affordable financial advising services.[26,52]

Many consumers continue to believe that working with a professional adviser is out of their price range because of the complicated, and sometimes opaque, pricing structure. For this reason, publications for the professional financial adviser commonly stress the importance of open and consistent communication about fees with both current and prospective clients. The research shows that many consumers are willing to pay for financial advice if they understand the fee structure and feel that they can participate in determining it.[53] George H. Walper Jr. and Catherine S. McBreen of Spectrem Group emphasize that talking about fees and fee structures is a critical component in the advisor-client relationship. They explain:

> Fee structures can be complex, multi-tiered aspects of financial management. Younger investors especially need to understand the fees and fee structure they are working with as they typically have fewer assets and relatively more to lose if they aren't aware of an advisor's fee structure and feel they have been misled. And some fees—like 12b-1[vi] and transaction fees for purchasing securities—are not as obvious to some investors as those fees paid directly to one's primary advisor for services rendered.… Opening a dialogue about fees can be difficult depending on your client's comfort level with the fee structure and interest in discussing it, but it's essential to do so. A fee structure that is perceived as unfair or out of the norm can cost an advisor important clients and referrals.[53]

[vi] 12B-1 fees are a type of marketing or distribution fee on mutual funds, and are considered an operational expense.

Even for consumers who understand that financial advice involves more than investing, and that financial advisers can be affordable, it is difficult for them to place a value on such services. Many non-affluent consumers think that the cost of financial advice outweighs its value, and is therefore too expensive.

In this sense, the value of working with a professional financial adviser is often misunderstood because financial advice is generally abstract and long-term. That is, purchasing financial advice does not necessarily translate into concrete and immediate benefits for the consumer. For example, financial advice is not like hiring a plumber, in which the immediate and concrete benefit of the service is a fixed sink. Instead, the benefits of financial advice are delayed and more abstract. This challenge is nicely summarized by Gary Selnow in *Motivating Retirement Planning: Problems and Solutions*:

> People often find it difficult to make the right decision about retirement savings. The payoffs are in the distant future, and the promise of pleasure tomorrow can mean pain today. The wrong decision yields an instant gain, the outcome is uncertain, the decision can be postponed without immediate penalty. In the end, the pressures of immediate gratification, delayed benefit, the unknown, the uncertain, the uncomfortable, ally against wise decisions.[54]

Finally, the difficulty of calculating the value of financial advice is compounded by the fact that financial planning for retirement involves a long-term time frame. It is notoriously difficult for consumers to make intertemporal choices in the face of uncertainty and risk. This phenomenon is commonly (and perhaps unfairly) framed as "lacking the future orientation" to appreciate the value of financial advice. A more fruitful understanding can be found in the behavioral economics literature as the principle of hyperbolic discounting, in which consumers overweight present benefits and devalue (discount) future benefits.[55-58]

Interviews with Teresa Russ Winer, FSA, MAAA, and Paul Richmond, ASA, EA, MAAA, confirmed that, in terms of working with personal actuaries, consumers have misunderstandings and misperceptions on the value and process of financial advice.

Ms. Winer is a consulting actuary with experience in traditional and nontraditional areas, including personal actuarial work. She has conducted market research for the SOA on the viability of actuarial counseling and the perception of financial professionals.[59] This research pulled together one focus group of retirees, and a second focus group of financial planners, lawyers and bankers to discuss this issue. Her main finding was that "most do not know what a personal actuary could do, and there is a high perceived cost of financial advice." Winer pointed out that wealthy people are more accustomed to paying lawyers, including on retainer, so they are used to paying for such professional advice. She explained, "this is a mental anchoring issue," referring to

the phenomenon in psychology and behavioral economics in which individuals display behavioral biases based upon their limited reference points. In other words, non-affluent consumers do not have a reference point for paying a significant price for advice.

Richmond is a personal actuary who ran his own financial planning firm. He found that both his clients and their adult children often did not appreciate the value of professional financial advice:

> There was a lack of recognition of the value added by a personal actuary. I experienced this in the form of resistance from family members to pay appropriate fees for my services…I was looked upon with suspicion, especially by adult children of clients, who became suspicious that I was taking their inheritance. This was compounded because the financial services industry did in fact take advantage of people, often these very same clients. So this was a trust issue that I tried to address by attempting to make it a requirement that I meet with children and parents, which sometimes worked and sometimes didn't. That was an ongoing challenge.[60]

Sally C. Hass is a nationally recognized expert in workplace financial education issues. She earned that reputation over 20 years for her work implementing innovative life and retirement planning programs for the employees of the Weyerhaeuser Company, which is considered a national pioneer and leader in the field.[61] Hass explained that, for her employees, intimidation is a barrier to seeking more financial advice:

> In regards to sitting down with a financial planner for a one-on-one session, my employees don't know what they're getting into, or what will they get out of it. So having a trusted speaker at the seminar describe a first financial planning meeting takes away the intimidation factor. They describe what it will be like and what are the fees.[62]

Hass further explained that Ameriprise (one of Weyerhaeuser's vendors) found that 30 to 40 percent of the audience would sign up for a complimentary meeting within six months, with no other marketing, because "the intimidation factor was reduced."

Consumers are blocked from financial advice, in part, because of their own misperceptions. As the research indicates, consumers overestimate the cost and underestimate the value of advice because of unfamiliarity with the process. The future-oriented nature of financial advice creates an additional challenge, as even a consumer who intellectually understands the financial value of advice will refrain from seeking it because of the psychological inclination to devalue the benefit of something in the

distant future. The result is that the misunderstanding of the value of financial advice is a significant barrier to those who might seek it.

BARRIER 3: NON-AFFLUENT CONSUMERS OFTEN DO NOT TRUST—AND THEREFORE AVOID—FINANCIAL ADVISERS WHO ALSO SELL PRODUCTS DUE TO THE PERCEIVED CONFLICT OF INTEREST.

Relationships and trust are cornerstones of the financial advice industry. However, non-affluent consumers often perceive financial advisers (and the institutions for which they work) to be attempting to sell financial products at the expense of providing unbiased financial advice. As a result, such consumers avoid financial advisers because of lack of trust.

In 2008, HM Treasury undertook a comprehensive review to design a national approach to delivering generic financial advice to citizens of the United Kingdom. The term ”generic” in this context means advice provided by an independent third party, not affiliated with any financial services company. This study found that “while people want to be told exactly what to do, they do not want to be sold that solution.” Further, the principles people valued most in a proposed generic advice service was that it would be “on my side” and “sales-free.” Most people surveyed wanted to make their own decisions and did not want the service to be linked directly to selling.[63] While the survey used U.K. consumers, which is not the focus of this paper, it is reasonable to infer that Americans facing a very similar financial services marketplace would have nearly the same response.

Bert Whitehead and Sheryl Garrett—financial planners who founded fee-only services for the middle market—have consistently found that one of the top reasons why many middle class consumers do not seek financial advice is because they “are not sure whose interest an adviser is really serving.”[29]

The lack of trust in the financial services industry has become rampant over the past few years, due to the intersection of the economic downturn with a number of high-profile news stories about financial advisers betraying the trust of their clients. This phenomenon is addressed in more depth in the section below, which discusses institutional-level barriers. However, regardless of the events of the past few years, non-affluent consumers often perceive a conflict of interest when a financial adviser is selling the very financial products that he or she is recommending. Further, articles in the popular media have highlighted this issue. Consider the passage below from CNN’s *Money Magazine*, titled “Inside the Mind of Your Adviser”:

> While your planner may vehemently deny it, the financial and psychological incentives built into the advice business sway the nature of the advice that's dispensed. Some of those influences—a hope that you'll be satisfied enough to refer

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> friends, for instance—can work in your favor. But most incentives don't, even if your planner is a genuinely nice guy. "I think the majority of advisers have clients' best interests at heart," says Bing Waldert, associate director of the financial services research firm Cerulli Associates. Maybe so, but that's a paradox you face as a financial client. Your biggest challenge isn't to avoid crooks and incompetents (though both exist). It's to make sure you're getting the most from an adviser with good intentions—but with interests that may run counter to yours…
>
> When you're sitting across the desk from a financial professional, you should realize that there's a fundamental misalignment of interests. You're looking for sage advice. Chances are your adviser is looking to hit sales targets. However much your adviser's office strives to impress clients as a place of refinement and learning, behind the wood paneling it's a sales culture. Every influence, from crass coercion to gung-ho competition, is designed to increase revenue.[64]

Hass' experience sheds further light on this issue. During her 20 years running Weyerhaeuser's workplace financial education program, she was always experimenting with content, format and types of guest speakers. Hass explains that she thought of her seminars as "an incubator to test different strategies to figure out which ones are the most effective." Hass often used financial planners as guest speakers. One of her earliest lessons that she learned from her employees was that they do not trust guest speakers who are supposed to be providing education and instead are perceived to be selling something. This was such an issue that she began to thoroughly screen all guest speakers. This included hearing them speak in front of another audience before she would invite them to speak to her employees.

"I also had rules," she explains. "If they needed to collect names, they could not use them for marketing purposes or they would not be invited back. If they wanted to leave cards, that was OK, but no self-promotion, and no trashing other firms."

The fact that lack of trust partially derives from mixing selling with advice-giving helps explain why government and nonprofit sources of financial information generally have higher levels of trust with consumers: they are not trying to sell something. This was emphasized in an interview with Edwin Bodensiek, former Director of Outreach for the U.S. Treasury's Office of Financial Education, about the focus groups he conducted in the development of the Treasury's *Bad Credit Hotel* resource, a web-based, interactive video experience that helps citizens understand basic principles of credit and debt management.[65] When focus group participants were shown the Treasury seal, everyone

expressed confidence that the information would be accurate. Further, when participants were shown possible web addresses for the *Bad Credit Hotel* website, they were most distrustful of web addresses with a .com suffix because, as they explained, such sites are seen as “people trying to sell something, not trying to help you,” whereas participants were more trustful of .org websites, and most trustful of .gov websites.

Andrew Biggs, Resident Scholar at The American Enterprise Institute and a leading researcher on the use of the Social Security statement to provide workers with guidance on saving and planning for retirement, confirmed this point regarding public trust of the government to provide financial advice. He explained:

> For all the public debate around funding Social Security, people are reasonably trustful of the information they get. People trust the information on the [Social Security] statement – that it is accurate and helpful – even if they do not think they will get the benefits they are promised.[66]

An interview with Patricia Humphlett, Coordinator of Department of Labor’s Employee Benefits Security Administration’s (EBSA) Retirement Savings Education Campaign, told a similar story.[67] EBSA has designed and launched several tools to help workers plan and save for retirement. For example, *Taking the Mystery Out of Retirement Planning* is a free resource designed to assist individuals who are within 10 years of retirement to calculate future income and expenses, and to get a better idea of whether they are on track with their savings[vii]; *New Employee Savings Tips – Time is on Your Side* is for workers on their first job highlighting the importance of starting to save early; and *Savings Fitness: A Guide to Your Money and Your Financial Future* is for those who want to take charge of their finances during their working years with information on how to include saving for retirement among life’s many expenses. Ms. Humphlett explained that in order to establish these tools as trusted resources, EBSA provides unbiased information, and has no connection to the selling of any financial products or services.

This point was echoed by Michael Herndon, Manager of Financial Security Institutional Outreach at AARP.[68] Herndon explained that AARP conducts extensive research on its members’ attitudes and has generally found that members trust both the organization and the services that it recommends—whether health insurance or financial—because “members trust that these services have been vetted by AARP, and the information we provide is credible.” Herndon continued, “This trust derives in part from the fact that AARP has been around for 50 years, and that we do much, much more than simply sell products.”

[vii] This publication was developed with the Actuarial Foundation, the North American Securities Administrators Association and AARP.

The research shows that, in the view of many consumers who have not utilized advice, a financial adviser can either sell product or give unbiased advice, not both. National studies and interviews with consumer experts reveal that even unsophisticated consumers are sophisticated enough to spot a potential conflict and be distrustful of it. The independent sources that addressed this topic were strikingly similar in reaching this same conclusion. The widespread practice of mixing financial advice with financial product sales inherently engenders strong distrust on the part of some consumers, and gives rise to a formidable barriers for those who might otherwise seek advice.

2.2 Social-Level Barriers

Barriers operating at the social level involve the processes by which interpersonal interactions and group dynamics reduce participation in financial advice. These include consumer social interactions within the immediate social sphere (friends, family, spouse or partner, colleagues, etc.), as well as the consumer-financial adviser interaction.

The skillful process of learning to function effectively in consumer roles is called consumer economic socialization.[69] There are several economic socialization processes that normalize the avoidance of formal, professional financial advice. The economic socialization process can be viewed as assimilation of the internalized and collective forms of values and norms, which occurs through parental influences and the influences of others, including individuals, groups of individuals, organizations, media and the greater society.[70]

Values formation is crucial to understanding financial behavior, because behavior results from deep-seated, emotion-laden and often unconscious values.[71] Therefore, understanding the consumer economic socialization process sheds light on how values about financial advice are formed and transmitted, and the role that those values play in a consumer's decision to pursue financial advice.

BARRIER 1: MANY NON-AFFLUENT CONSUMERS ONLY SEEK FINANCIAL ADVICE FROM INFORMAL SOURCES, SUCH AS FAMILY AND FRIENDS, BECAUSE THEY VIEW THESE SOURCES AS INHERENTLY TRUSTWORTHY.

While most Americans seek informal advice, non-affluent consumers are more likely to only receive financial advice from informal, trusted sources, such as family and friends.[72] While informal advice may be customized to an individual household's financial details, friends and family may be uninformed and therefore may provide inappropriate advice.

First, the correct advice for previous generations may not apply for middle-class families today. For example, a family saving for college education 20 years ago did not have the option of tax-advantaged 529 plans. Baby boomers may not know about these investment vehicles and therefore neglect to advise their children to take advantage of them. This issue of uninformed, cross-generational advice is present in retirement planning as well, given the transition from defined-benefit to defined-contribution pensions.

Second, informal sources may have ulterior motives. For example, several poor and immigrant communities have suffered by being sold inappropriate products by trusted

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members of their own social networks.[73,74] This betrayal among friends and colleagues is certainly not limited to poor and immigrant communities, however, as this phenomenon was also part of the investment scandal surrounding Bernie Madoff. This point was elaborated on by Steve Vernon, Fellow of the Society of Actuaries and now President of Rest-of-Life Communications, who regularly provides employer-sponsored retirement workshops to non-affluent employees. He explains:

> Trust is a problem for low-income and moderate-income people. They are taking advice from friends and family. I see too much of it, and they're not experts. This is the affinity stuff, this is how the Madoff thing happened, which I talk about because people recognize that name. This is tied into the trust issue in the sense that if they don't trust an institution, friends and family may be the only source of financial information they get. What happens is there is an advisor that the friend or family recommends, but that person may not be properly trained or have your best interests at heart. The adviser may be charismatic, for example the way Bernie Madoff was for high-end clients.[75]

David Grace, Vice President of Association Services at World Council of Credit Unions, explains that many recent immigrants, as they assimilate and acculturate into U.S. society, rely especially upon their social networks and communities:

> They are finding their footing, and they get informal support because they are looking for guidance, and not just on financial matters. So word of mouth is important for a whole range of issues.[76]

Similarly, Louis Barajas, CFP® has observed that members of the Latino community in East Los Angeles have taken advantage of what he calls the "compadre system," whereby people will look to friends and family for financial advice.[77] He explains, "In this community, a lot of financial planners are part-timers and they are out to sell a product. What I'm trying to do is allow people to see we are really trying to help them out.… I'm here to offer the community an alternative."[77]

The difference between the inherent trust in friends and family on the one hand, and the lack of trust most non-affluent consumers feel toward financial service professionals on the other, often creates a substantial barrier to seeking financial advice.

BARRIER 2: PROFESSIONAL FINANCIAL ADVISERS OFTEN DO NOT HAVE THE NECESSARY SOCIAL RELATIONSHIPS AND COMMUNITY CONNECTIONS TO ACCESS AND SERVE THE NON-AFFLUENT MARKET.

A consumer must have trust in a professional financial adviser to discuss and handle his or her finances. This is why financial advisers emphasize the importance of establishing and maintaining good communication and relationships with their clients. In an article in the *Journal of Financial Planning* titled "A Matter of Trust," George Kinder states:

> It has become clear from surveys over the past several years that the primary quality that consumers look for in a financial advisor is trustworthiness. In fact, the issue of trust rates higher than the issue of professional skills, and far higher than our [financial advisers] ability to deliver the highest possible rates of return.[78]

Financial advisers very clearly understand the importance of developing and maintaining close relationships with their affluent clients. Such relationships retain current clients. As the saying goes, "you fire an adviser, but you never fire a friend."

Such relationships also provide valuable connections that can translate into referrals to other wealthy clients. Indeed, the 2010 Financial Planning Marketing Methods Study, conducted by the Financial Planning Association Research Center, found that "requested referrals from current clients" was the most common marketing strategy, used by 77 percent of planners, which was more than 20 percentage points higher than the next most popular method.[79]

The emphasis on cultivating referrals from wealthy clients is ever-present in the practitioner literature. Articles with titles like "From Friends to Clients" teach financial advisers "how to convert your wealthy friends and acquaintances into profitable clients," while articles with titles like "Keeping the Kids" and "A Way to Investors' Heirs" emphasize strategies for maintaining business with heirs once their parents pass away.

However, financial advisers generally have not invested the same type of energy in developing relationships with potential clients who are not affluent. In fact, there is widespread recognition that financial advisers have traditionally under-served or ignored non-affluent consumers because they are not profitable - or significantly less profitable than affluent clients.[26,80-83] CPA Kent Irwin summarizes this point:

> Most firms that provide financial planning pursue the people in the top five percent income and net worth bracket. The market competing for their attention is crowded; nearly every investment, insurance, planning, and estate planning firm is focused entirely on the wealthiest people.[26]

Carolina Reid, Ph.D., Manager of the Community Development Research Group at the Federal Reserve Bank of San Francisco, connects this issue back to trust. She explains that, for many non-affluent consumers, the line of thinking is, "I don't trust them to understand my financial situation. They don't want to understand my situation and tailor their advice to my situation."[84]

As the evidence shows, the lack of investment of time and energy by financial advisers to cultivate relationships with non-affluent clients has often led to a situation where advisers do not have the requisite relationships. Not only does this present a barrier to non-affluents accessing advice, but its persistence across generations has helped the barrier grow strong and deep roots. Because advisers have not targeted the non-affluent market in the past, they have little knowledge of that market's needs or how to approach it. Over time, the lack of a relationship between financial advisers and non-affluents affected has helped to perpetuate a cultural norm among non-affluents that financial advice is only for wealthy people.[26,32] These factors combine to make a barrier to access that is buttressed by history and challenging to overcome.

BARRIER 3: THERE IS OFTEN A CULTURAL DISCONNECT BETWEEN FINANCIAL ADVISERS AND NON-AFFLUENT RECENT IMMIGRANTS

As has been discussed above, the financial advising industry has traditionally focused on building relationships and understanding the financial needs of the affluent. While this affluent clientele tends to be demographically homogeneous, non-affluent consumers in the United States are significantly more diverse, and often have different values and attitudes toward money and the financial services industry. This is particularly true of several recent immigrant groups, who are an important and growing part of the American population. This dynamic creates a cultural disconnect whereby recent immigrants think that financial advisers do not understand their needs and priorities.

This point is clearly made in "Lessons Learned in (Not Yet) Serving the Masses," an article written for the practitioner audience in the January 2010 edition of *Journal of Financial Planning*:

> When devising a process for underserved markets, we must listen and understand how ethnicity and other factors create visions of retirement and financial well-being that differ from our own experience. Lisa Markus of The Sentinel Group shared this insight at FPA Anaheim 2009: "Looking at the standard retirement brochure put out by the big firms, you'd think that everyone's picture of retirement was the same: a stroll with your spouse on a beach. Maybe even a dog. The

> problem is that, for multicultural audiences, it's the wrong picture. Latinos would look at the couple and say “poor them, they were so stingy in saving for retirement that no one wants to hang out with them. Good thing they have a dog.” For them, retirement is the time to spend with family and have fun with the grandkids.[32]

For recent immigrants from countries with different financial systems and credentialing regimes for financial professionals, this cultural disconnect can be even larger. For example, Sant La, a Haitian Neighborhood Center in Miami, conducted a financial literacy needs assessment of its constituency, and found that one major theme that prevents Haitian immigrants from accessing the financial mainstream is “cultural baggage.”[74] The research participants, who included both Haitian consumers and Haitian financial service professionals, agreed that many Haitian immigrants had brought with them decision-making processes informed by the culture of scarcity and the absence of financial institutions responsive to the needs of the average citizens.[74] They cited as an example the fact that in order to secure a loan in Haiti, one must have social connections—access is guaranteed not by creditworthiness by whom one knows.[74]

For other immigrant groups, certain beliefs or influences sometimes directly conflict with seeking financial advice for long-term planning. A few examples from the research on Latinos illustrate this point.

Lisa Peñaloza conducted an ethnographic study of the consumer acculturation of Mexican immigrants.[85] Not surprisingly, she found that her informants both assimilate consumption patterns associated with U.S. consumer culture, and maintain aspects of the consumption patterns they had acquired in Mexico. This study also found a general distrust for financial institutions by Mexican-American immigrants as a result of negative experiences in their country of origin. Further, Penaloza found that informants “expressed concerns about getting caught up in U.S. consumer culture, and they actively resisted its pull.”[85]

Similarly, in 1991, Barajas left a lucrative accounting and consulting firm and returned to the East Los Angeles neighborhood where he grew up to found his own firm dedicated to working with the underserved Latino market. Part of his mission was “transforming the community’s attitudes about money and finances.” Barajas explains that many Latinos “put their destiny in God’s hands—'Si Dios quiere' or 'If God wills it'—rather than taking financial matters into their own hands.”[77]

There is some limited evidence to substantiate Barajas’ assertions. Medina et al. conducted a controlled experiment comparing Mexican-American and Anglo-American consumers using a psychometrically valid Money Attitude Scale.[86] The authors found that Mexican-American consumers, as a group, display greater present-oriented

attitudes and lower propensity to postpone gratification, and are relatively reluctant to engage in long-term money-management behaviors. The authors interpret these findings to suggest that "Mexican-Americans are not likely to respond to offers by firms whose products/services require a long-term consumption view and where some degree of individual planning is required." Because the two groups had comparable education and socioeconomic status, "observed differences in money attitudes may indicate genuine cultural variations." If such results can be replicated for the broader population of Latino immigrants, the implications for these consumers and those who wish to advise them would be significant.

Many non-affluents are recent immigrants to the United States, bringing with them diverse cultures that influence both their understanding and handling of financial matters. Some of these cultures may have elements that reduce the seeking of professional financial advice or create cultural disconnects with financial advisers, thereby creating a barrier.

BARRIER 4: STRONG AND PERVASIVE GENDER ROLES OFTEN REDUCE FINANCIAL ADVICE UTILIZATION BY COUPLES.

While each person is shaped by his or her own individual experiences, there is some compelling research on gender and money that raises potential barriers to advice-seeking by couples. Specifically, research on gender differences in money attitudes and practices finds that women are more likely to seek and actually use financial advisers, while men are more likely to get information on their own.[87,88] In traditional mixed-gender relationships, women are typically more involved in routine money management tasks (e.g., household shopping and bill paying), while men traditionally manage the investment-related activities. Indeed, the research shows that men typically find investing exciting and satisfying, while women generally find it more stressful, difficult and time-consuming.[89] These factors create a situation in relationships in which women leave the long-term planning to men, who are less likely to pursue financial advice because of their overconfidence in their own abilities and preference for self-directed learning.[87,88] This situation is compounded by the fact that couples often avoid conversations about long-term financial issues so that the need for advice may not be addressed and a plan to seek advice may never be developed. This gender dynamic can operate as a barrier for couples who might otherwise seek advice.

More broadly, couples' general inability and reluctance to discuss money or make joint decisions could figure into why couples avoid financial issues with or without a financial adviser. Family counselors and financial planners often report that financial behaviors are a leading cause of relationship distress.[90] Most previous studies that have addressed the finance-relationship connection have found that personal and couple financial behaviors are one of the primary reasons for relationship dissatisfaction.[90] The extra sensitivity about money issues within a couple may be a reason the couple is not eager to bring a third party into such an intimate and emotionally charged discussion.

With respect to traditional gender roles, the dynamics of money management are changing. While men traditionally have managed the family's finances, women have begun to have greater control, as decision-making is becoming more balanced between breadwinning spouses.[91-94] This new dynamic may itself be a barrier in the sense that financial advisers are not equipped to service couples who are negotiating new patterns of family money management.

It is also important to note that experts still know very little about the financial decision-making process of couples.[95] As Viviana Zelizer puts it, "In terms of evidence, to study money in the family is to enter a largely uncharted territory … we know less about money matters than about family violence or even marital sex."[96]

As gender roles and relationship dynamics may prevent couples from seeking advice in a number of different ways, this barrier appears to add an extra level of complexity for

financial advisers who hope to serve the millions of American adults in mixed-gender relationships.

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2.3 Institutional-Level Barriers

This section presents the evidence on how both the pursuit and delivery of financial advice are shaped by institutional forces—such as pricing policies and macroeconomic factors—that influence the opportunities, constraints and incentives for providing financial advice.

BARRIER 1: MOST FINANCIAL ADVISING FIRMS HAVE NOT TRADITIONALLY FOCUSED ON NON-AFFLUENT CONSUMERS BECAUSE THEY ARE LESS PROFITABLE. FURTHER, MOST FIRMS AND ADVISERS EITHER CANNOT AFFORD OR DO NOT WANT TO MAKE THE LONG-TERM, HIGH-INVOLVEMENT INVESTMENT THAT IS NECESSARY TO CULTIVATE BUSINESS WITH SUCH CONSUMERS.

There is widespread acknowledgement in the financial advice industry that the middle market has largely been under-served or ignored.[26,80-83] The traditional logic among financial advisers has been that one cannot make a profit by serving non-affluent clients.

However, this logic is under revision as competition has increased over the shrinking affluent market. Several firms, both large and small, are experimenting and innovating new strategies for profitably serving the middle market. This study has analyzed the literature on this recent development, which demonstrates that advisers and firms that try to serve non-affluent markets are fighting an uphill battle. The middle market can be profitable, but presently it is not as profitable as serving affluent clients. Serving this market often requires developing new systems and spending more time per client. In other words, firms must operate on leaner margins and with greater efficiency.

While part of this barrier is the economics of the firm, the brutal truth is that financial advisers, in order to serve the non-affluent, would have to accept a substantial pay decrease. Michael E. Kitces, CFP®, Director of Research for the Pinnacle Advisory Group, lays out this argument:

> According to the census bureau, the median U.S. household annual income in 2007 was just over $50,000. Maybe serving the middle market successfully really might be—dare I say it—a job that only earns $60,000–$80,000 per year.… This would place the job right on par with what many other professionals (for example, attorneys, accountants) typically earn in the early years of their careers—when they, too, often serve more middle-market clients, before a select few move on to the most wealthy and affluent of clients. Yes, this

> isn't the $150,000+/year income that many financial planners set their eyes on.

Generating profits from serving non-affluents takes time, which many firms cannot afford. As Bonnie A. Hughes, CFP®, puts it

> Building it and hoping they come won't work. One reason planners who try to serve the underserved fail is that if the volume doesn't come in a relatively short period (a year, for example), the model doesn't work well.[32]

The fact that some smaller firms have been driven out of business by attempting to serve non-affluent markets may intimidate other firms who were planning to do the same. In fact, the common wisdom is that only big firms have the economies of scale to generate profits from serving non-affluents.[83]

Hughes and Garrett, however, dismiss the notion that the only advisers available to serve a middle market are large firms that can scale the deliverables. Hughes and Garrett believe that planners themselves may be the stumbling block to serving the masses. As Hughes puts it:

> While attorneys and accountants have both found business models that serve more than just the wealthy, but getting planners to believe it is an uphill battle. No one is suggesting that the middle market is for everyone already practicing…What we're talking about here is faster paced, with potentially less pay, and frankly, more work for the money.[32]

In this context, it is helpful to understand how one firm, Charles Schwab, has developed a business strategy that profitably serves the middle market. Steve Anderson, Schwab SVP and Head of Retirement Plan Services, explains that Schwab focuses first on meeting its existing clients' needs as a way to drive brand loyalty over the long term. Mr. Anderson characterizes the contrast of Schwab's model against conventional models as being marketing- and service-driven, as opposed to sales- or business-development driven.

> Marketing and service driven is what Schwab does: they focus on serving existing clients as a way to build loyalty to their brand. Sales-driven means that brokers have to generate most of their own leads, so they can spend 80% of their time figuring out who to talk to, and then once they get them, they will sell to them aggressively.[97]

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Mr. Anderson stressed that Schwab's philosophical approach is to help everyone be financially fit. This view, along with the firm's size and commitment from the top to serve the middle market, allows Schwab to have a "culture where it is safe to have those longer conversations [with middle market consumers] that will not yield immediate high profits." Schwab's internal research indicates that meeting such clients' needs drives their loyalty to the firm. Mr. Anderson emphasized that, because of this, Schwab has "a client-centric business model that requires a very efficient firm, in terms of operating costs, in order to make that work."[97]

Mr. Anderson explained, "We provide financial advice to non-affluent customers because loyalty will be built over time and customers will stay with us as they make more money. People stay with their provider if they have trust, loyalty to brand."[97] Schwab considers moderate-income customers as the "nursery for the firm" 10-15 years down the road:

> They are going to develop the nest eggs and we want to be there for them. Also, if you treat people right, you get referrals. They are going to take care of you by referring family and friends.[97]

Schwab supports this strategy by using a fee-based and service-based incentive structure for advisors, as opposed to exclusively commission-based pay. For most of the industry, however, the perceived low profitability of non-affluent consumers is a barrier to providing those potential clients access to financial advice.

BARRIER 2: THE STRUCTURE OF THE PROVISION OF FINANCIAL ADVICE INCENTIVIZES SELLING PRODUCTS, WHICH OFTEN SETS UP AN INHERENT CONFLICT OF INTEREST IN WHICH ADVISERS SELL MORE PRODUCTS AND SERVICES TO A PARTICULAR CLIENT THAN IS PRUDENT IN ORDER TO MAXIMIZE PROFITS.

As discussed in the individual-level section, non-affluent consumers often perceive financial advisers (and the institutions for which they work) to be attempting to sell financial products at the expense of providing financial advice, resulting in consumers avoiding financial advisers because of a lack of trust. This section first provides the institutional and economic context for this conflict of interest, and then establishes how it disproportionately affects non-affluent consumers, resulting in a bad experience that discourages them—and their friends and family with whom they talk—from seeking further advice.

The inherent conflict of interest between advising and selling products is universally acknowledged within the industry. Although this issue has been discussed and debated extensively, it has not yet been resolved.[80,83] In fact, as competition has increased, advisers are increasingly pressured to generate profits. As recently as May 2010, Dean Zayed of Brookstone Capital Management wrote, "A problem our industry has created through fierce infighting has been forcing sales quotas on advisors, turning them into product pushers."[98]

In a classic 1990 column in the *Journal of Financial Planning* titled "To Think... Like a CFP," Richard Wagner argued that "financial planners do not have a professional identity," and instead of being viewed as service delivery system that plays a unique and powerful role in today's society, financial planning has been defined as a "product delivery system." In honor of the *Journal*'s 25th anniversary in 2004, the editors reprinted what they considered to be its best content. Wagner's column was only the second article reprinted.

More formal analyses have confirmed that there is a fundamental conflict-of-interest problem with the current advising model, in which the majority of financial advisers are paid on a commission basis. For example, in their article "Financial Advising in the Presence of Conflicts of Interest," Miriam Krausz and Jacob Paroush show that actions by profit-maximizing advisers will not necessarily coincide with their clients' objectives.[99] Further, because the cost of switching advisers is not negligible, advisers are able to exploit information asymmetries "up to a threshold that causes client intervention."[99] Therefore, established personal and institutional relationships often afford advisers greater opportunity to continue to pursue their own interests rather than those of clients.

The amount that consumers pay in financial product commissions is large. Ralph Bluethgen et al. find that 12b-1 fees amounted to $10.9 billion in 2005, 40 percent of which were paid as sales commissions to financial advisers. In addition, another $1 billion of sales commissions were paid through front-end loads.[100] After a careful

analysis of the economics of the financial advice industry, Bluethgen et al. posit that "it remains to be explained why most payment for advice is indirect by means of commissions."[100] They suggest that financial advice is a public good, which, once produced, can be cheaply copied and distributed, and so in order to make a profit, firms utilize a tie-in sale model in which advice is bundled with an exclusive good, such as a name-brand financial product. Thus, while information may still be copied cheaply, only a few can distribute it profitably.[100]

Further, Bluethgen et al. find that the attributes and pricing of financial products are opaque. Even highly educated consumers find it difficult to fully comprehend how to unbundle and price the products that they are sold. Thus, "structuring [bundling additional costs into products] may be interpreted as 'obfuscating' or 'shrouding' product attributes."[100]

Daniel Winslow, CPA and Fellow of the Society of Actuaries, is a fee-based financial planner who continues to see many practitioners that sell products at the expense of providing sound financial advice, but also emphasizes the inherent tension involved in the financial advice business model:

> Frankly, there are a lot of sales people pretending to be financial advisors, who sell to earn commissions. There are hundreds of thousands of people like that. Part of the difficulty is establishing a reputation that you care about your clients. That takes years. On the other hand, to succeed in this business you have to have sales skills. Clients do not just walk in the door![101]

Mr. Anderson from Schwab adds an important explanatory point: non-affluent consumers are typically paired with junior advisers who generally lack advising experience and product knowledge, and must put more emphasis on selling than advising. This can result in a bad experience for consumers, which will discourage them from seeking advice later in life.

> For people who have made it in financial services business providing advice, they tend to work with upper echelon clients: they have built credibility and reputation, so they can work with high net worth individuals. On the opposite side, new advisers have to slant their solutions with non-affluent customers to make money. That's a challenging model to gain credibility. If your only solution is an annuity, that's the only advice you will give, and how valid is that advice? This situation is widespread in the insurance, brokerage, and bank environments.[97]

Krueger expanded upon this point, explaining how the treatment of non-affluent consumers—and the perception of their treatment—creates this barrier.

> There is a common perception that financial advice comes at the cost of buying something, that you will be pushed into something. And it's a very real perception, it's very accurate, especially at the lower end. For example, teachers who have pensions and are earning forty thousand a year, they are very skeptical. They know that there's no one out there who's going to profit by giving advice to this market. They think to themselves, "We don't have enough money for financial advisers to make money [from serving us], so we're gonna get a sales pitch. We're gonna get the cheap and pre-packaged version, and it's gonna be poor quality, not genuine advice. The advisor will be looking at his watch." It's perceived as a sales pitch, to the benefit of the seller. [37]

This conflict is also present in the credit-counseling industry. Michael Staten et al. find that credit counselors are increasingly incentivized to set up a debt management plan (DMP) for their clients, even when one is not necessarily the appropriate course of action for clients.[102] This overselling of DMPs is driven by the fact that they generate nearly 90 percent of agency revenues, even though only one-third of agency clients use them.[viii] In this way, consumers who are in debt are often steered into the wrong product at the expense of proper credit counseling.

While non-affluent consumers may not have perfect knowledge of the conflict inherent in the advice industry, they often know enough to sense it and be concerned. Further, non-affluent consumers who do seek advice are likely to be referred to younger advisers who are especially motivated and incentivized to sell products. The result is that these consumers are given evidence to confirm the belief that advice is being compromised in order to make a profit.

[viii] DMPs consist of creditor concessions in the form of reduced interest rates, fees and minimum payments. Unlike markets for most services, the consumer-client pays only a small portion of the cost of providing counseling services. Approximately 72 percent of agency revenues come from the fees that creditors pay to agencies ("fair share") to support their operations. These fair-share payments to agencies are linked to the volume of DMPs established for agency clients, and are typically calculated as a percentage of debt recovered. DMP clients often are asked to make additional payments as part of their monthly payment plan. Agencies derive about 18 percent of their total revenues from such client contributions. Consequently, nearly 90 percent of agency revenues derive from the debt management plan product that is delivered to just one third of all clients.

BARRIER 3: THE RECENT TURMOIL IN THE FINANCIAL MARKETS HAS SIGNIFICANTLY LOWERED NON-AFFLUENT CONSUMERS' CONFIDENCE AND TRUST IN THE FINANCIAL SERVICES PROFESSION.

The prevalence of stories about financial professionals who have made millions of dollars from reckless investing has generated substantial public outrage at those who represent Wall Street. This has made it even more challenging for financial advisers to overcome the non-affluent consumer's skepticism about the advice, skills and integrity of the financial services industry.

The research shows that consumer trust of financial services professionals is at historically low levels.[98] For example, Forrester Research's Annual Customer Advocacy Rankings, which are based on a survey of more than 4,500 consumers, found that consumer levels of trust were at an all-time low in 2009.[103] In this context, articles in publications for financial advisers have titles such as: "Shattered Confidence"; "Before Marketers Ask For Trust, Perhaps They Should Apologize"; and "Excuse After Excuse."[104-106]

In "Repairing Relationships and Restoring Trust: Behavioral Finance and the Economic Crisis," an article published in the *Journal of Financial Service Professionals* in July 2009, Kathleen M. Gounaris, Psy.D., M.B.A., and Maurice F. Prout Ph.D., provide a particularly compelling and informative narrative of how recent events have damaged consumer trust, and are therefore worth quoting at length.

> In the fall of 2008, the nation witnessed the crashing of our financial system with disbelief and dismay. Reactions were immediate, intense and emotional, as is typical when people are confronted with a traumatic experience. For both financial advisors and their clients, the economic turmoil has been a jumbled, overwhelming experience of adrenaline and fatigue, optimism and hopelessness, panic and fear.
>
> In its wake, the relationship between investors and the financial services industry is badly damaged. Like the feelings of betrayal following the discovery of a partner's affair, clients are experiencing a range of feelings: shock, anger, resentment, despair, and shame. At the most fundamental level, basic trust in the relationship—with investment advisors or financial institutions—has been broken.
>
> The initial cracks in the ice were seen in the overnight disintegration of a single institution such as Lehman

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> Brothers, which released the flood waters into the U.S. economy and around the globe. Since then, the corporate roster of faltering institutions and massive downsizing grows longer and more impressive. The flood waters also sprang open a Pandora's box of Wall Street deceit, revealing systemic greed, hubris, incompetence, and sheer ignorance.[55]

The authors go on to describe continuing public outrage—particularly in regards to Bernie Madoff, Allen Stanford and CEO compensation packages—and conclude that the public has “lost confidence and faith in the ability of formerly trustworthy institutions, leaders or government to protect them.”[55]

The damage to consumer trust is not permanent, but will likely reverberate for many years, especially as new revelations of fraud and deceit emerge and are reported in the popular media. However, these events have created an economy in which non-affluent consumers need financial advice more than ever. Ironically, the vivid and painful history of the crash has itself become a barrier to those very consumers.

SECTION 3: CONCLUSION

3.1 Core Themes Across All Barriers

The objective of this study was to identify and explain the barriers to professional, customized financial advice among non-affluent households in the United States. The research conducted for this study confirms that this population group has low utilization rates of financial advice. Through a systematic literature review and in-depth interviews with a range of national experts, this paper identified the barriers to financial advice that operate within or on individual, social and institutional levels.

This study concludes that the barriers identified group into larger themes that cut across individual, social and institutional levels. These core themes are presented below.

TRUST AND PERSONAL RELATIONSHIPS: "CAN I TRUST YOU WITH MY MONEY?"

Non-affluent consumers commonly cite lack of trust as one of the top reasons why they do not hire financial advisers. Consumers must have trust in a professional financial adviser to discuss and handle their finances. As Kozup and Hogarth put it, "Personal finance is, after all, personal."[107] This is why financial advisers emphasize the importance of establishing and maintaining good relationships with their affluent clients, and why advisers seek much of their business through referrals. Non-affluents need to feel that same trust, although it may need to be earned through different ways than with their affluent counterparts. The trust gap between financial advisers and non-affluent Americans is real and persistent. Central to that gap is the prevailing sales-driven adviser compensation system along with the inherent conflicts it causes for advisers and suspicions it raises for clients. Although this trust gap has existed for decades, the evidence demonstrates that the recent economic downturn has significantly worsened it.

COST, PRICE AND VALUE: "WHAT WILL FINANCIAL ADVICE DO FOR ME AND IS IT WORTH IT?"

Non-affluent consumers often perceive financial advice as being too expensive or they are unclear of what the cost will be. The perception of the high cost of financial advice is driven by both its actual price and the public perception of financial advice as being a service reserved only for the wealthy. Many are also unclear what the cost will actually be, as it is not immediately apparent due to the complicated pricing models—such as embedding pricing into the product—used by many financial advisers.

The perception of financial advice as being too expensive is also driven by lack of clarity over what financial advisers actually do, what their certifications mean and the value of

the advice they provide. The public perception is that financial advice primarily consists of guidance on high-risk investing. There is a lack of simple and clear information to consumers about financial advisers and the services they offer.

ACCESS AND FACILITATION: "HOW MUCH OF A HASSLE IS IT TO SIGN UP AND USE?"

Access and facilitation refer to institutional policies that make participation in financial advice more or less difficult to utilize. The financial advising industry has traditionally ignored non-affluent consumers, often erecting barriers to eligibility. For example, financial advising firms have traditionally required high minimum account balances as a prerequisite to work with a financial adviser. Through its eligibility policies, the industry effectively taught middle-market consumers that advice was not for them, and the middle market simply learned that lesson. Access and facilitation also involve making the utilization of advice easier and more automatic, such as being required to attend a seminar at work, or removing practical obstacles, such as driving distance and time commitment to get to a financial planner's office, through the use of technology.

3.2 Limitations, Implications and Future Research

This study reviewed a broad range of literature and solicited expert opinion to identify and explain the barriers to financial advice for non-affluent consumers. However, this paper does not empirically test the barriers through a controlled experiment. Rather, this paper cites the results of such experiments when available in the extant body of peer-reviewed, scientific research.

Generally, the data reviewed did not allow for quantifying the differential effects that the barriers have on low versus moderate wealth consumers. Very few empirical studies provide data that would allow such comparisons to be made. However, where possible, the paper specifies whether a barrier is more prevalent for a particular category.

Similarly, although this paper confirms that non-affluent consumers seek and utilize financial advice significantly less than affluent consumers, it does not attempt to identify the prevalence of the barriers or the degree to which they operate for affluent consumers. Nonetheless, this paper points to wealth-specific trends in the seeking and delivery of financial advice when the data is available.

Finally, this paper focuses on the narrow threshold question of seeking and accessing financial advice. It does not attempt to address the implementation questions regarding whether an individual or family acts on advice provided.

There are several areas for future research to explore. All of the barriers identified in this paper warrant empirical testing. For instance, a more robust understanding is

needed regarding the processes by which non-affluent consumers' trust is developed in the financial advising context. Also, the changing dynamics of couples' joint financial decisions remains poorly understood and would benefit from additional exploration. Perhaps most important, future research should have an applied orientation, developing and testing policies and programs to overcome the barriers identified in this study.

In conclusion, the findings from this study have significant implications for financial advisers and firms who are increasingly exploring expansion beyond the traditional narrow focus on affluent clients. However, while several advisers and firms have begun attempting to serve the middle market, many have struggled to accomplish this goal, and therefore reversed their efforts after a short time because the endeavor appeared to be financially unsustainable. This paper identifies barriers that such firms have confronted, as well as barriers that many may have not yet identified, all of which may prove valuable as the financial advising profession continues to evolve.

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