Investment ADVISOR THE VOICE OF INDEPENDENTS

Globalization Now

It's not a question of if, but when, every advisor will embrace the reality that the world is shrinking. Are you ready?

Melanie Waddell

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Globalization. We hear the term over and over nowadays yet it's often hard to define succinctly because it encompasses myriad issues. At its core, globalization means to make worldwide, and as we know, virtually every industry--particularly financial services--is conducting business around the globe. As part of that financial services community, advisors--whether they're attuned to it or not--are being touched more and more by globalization. Advisors' failure to embrace and prepare for the ever-increasing changes that globalization will present to their businesses will ultimately determine their future success.

To get a better handle on exactly how globalization is affecting advisors, consider these variables. While the world has, in essence, become flat, in the phrase popularized by *New York Times* columnist Tom Friedman, with technology making it easier for advisors to communicate and carry out their global affairs, clients, too--for personal or professional reasons--are increasingly on the go. As Leigh Basha, an attorney who is a partner at Holland & Knight's Private Wealth Services Group in Tysons Corner, Virginia, points out, advisors control only one piece of a client's "overall financial puzzle," since many clients have "multiple financial relationships in different countries"--from banking or investment accounts to real estate.

Everybody these days "is mobile," either for business reasons or a personal "desire to spend part of their time in one country versus another," says Basha, who also specializes in international tax and estate planning.

Indeed, adds Barry Glassman, a senior VP at the wealth management firm Cassaday & Company in McLean, Virginia, it's increasingly the case that "our clients don't always come from within our borders." Advisors are noticing, too, that as the dollar's value has plummeted, U.S.-based clients are looking to diversify their assets among better-performing currencies. The flipside is also true as well in that international investors are seeking to take advantage of the favorable exchange rate in the U.S. "There are so many deals to be had for European investors given the exchange rate that they are snapping up real estate properties" in the U.S., Basha says. "They're thinking that if the markets in the U.S. have bottomed out, now is the time to buy." (*Our friends from north of the border are finding opportunities, and facing planning issues, in the U.S.; see "Canadian Invasion" sidebar.*)

Overseas Alpha
Advisors and money managers are also noticing that institutional and even retail investors "are understanding that to get any kind of exposure to the new world, if you will, you need to be allocating a significant portion of your portfolio to non-U.S. companies and investments," says Uri Landesman, head of global growth at ING Investment Management. Non-U.S. markets, he says, "have outperformed U.S. markets the last five years, and so the evidence is fairly compelling." This implies "that there's been a funds flow from the U.S. markets into non-U.S. markets, with the emerging markets, from a proportionate basis, seeing the most in flows. Emerging markets have outperformed mature markets probably for the last three or four years running."

It's important for investors to have exposure to emerging markets like Brazil, Russia, India, and China (known as the BRIC countries), Landesman adds, because "the growth prospects for the intermediate and long term will be much greater" in these countries than they are in the U.S.

Five years ago, Brett Ellen, president of American Financial Network in Calabasas, California, was investing 15% of clients' portfolios in overseas markets, but today that's been bumped to 25% depending on a client's risk tolerance, age, and goals. "At a younger age with a more aggressive platform, we want to see [clients] in 25% offshore investments," he says.

Tim Kochis, CEO of the giant wealth management firm Aspiriant (formerly Kochis Fitz/Quintile) in San Francisco, says that his firm is "very strenuous in our encouragement to clients to adopt portfolio strategies that have substantial overseas exposure--in the neighborhood of 30% to 50%." While he doesn't try to make regional bets, Kochis says "if we had to, we'd bet more on East Asia than other parts" of the world. "But we look to the world as a whole--Europe, Latin America, Asia, the Mideast." Landesman of ING believes that the "places to go" are Asia and Latin America. ING "will be increasing our investments in those fast growing regions."

Models and Standards

Another trend that's pushing globalization of financial planning is the fact that countries across the globe are interested in adopting the financial planning model that's used in the United States as well as the Certified Financial Planner (CFP) mark, says Noel Maye, CEO of the Financial Planning Standards Board (FPSB) in Denver, which promotes the CFP mark globally. "The trend in the States 10, 20, 30 years ago where people were looking for a shift from working with someone who's selling a product to really working with somebody who could advise them--and not in only one area but advise them across all areas of their financial life--those trends are emerging around the world," Maye says.

As it stands now, 20 countries around the world offer the CFP mark with another three countries "preparing to offer it," he says. Maye was in Bangkok promoting the CFP mark during an interview in early June, and said that Thailand plans to offer the CFP mark by the end of the year. "We have about 112,000 CFP professionals in those [23] countries and around the world."

Kochis adds that the CFP mark's "common regulatory scheme is the unsung development in the industry, and it's gone a long way to make financial planning perhaps the first universal profession--a profession that looks to a common set of international standards that I'm not sure is true of any other profession."

The host of issues that are driving the need for advice in the United States are also contributing to the need for financial planning around the globe, Maye says. "More complex products, people living longer, people having to take care of their own financial futures, uncertainty of the marketplaces, and a need for people to have advisors who are looking out for their interests--those are the major drivers for financial planning globally."

The traditional family-based cultures in the emerging market countries where families have typically relied on multiple generations "as a way of investing in the future or protecting their retirement" are dissipating as "those markets emerge and you see a lot more mobility among young people," Maye says. More and more people in those countries, as in the U.S., are "faced with having to take care of their own financial futures more thoughtfully."

Unlike in the U.S., however, some emerging market countries' citizens are actually saving too much, as is the case in India, Maye says. In India, "it would be very common to save your money and buy gold and then have that as part of the family wealth, but it's not something that will accumulate and grow the way the stock market would over time," he says. So the government of India is looking to "turn the population from a nation of savers to a nation of investors. With that comes increasing financial literacy of the population and ensuring there are advisors on hand to work with them and put their interests first when giving them advice on strategies and products." (*For more on planning overseas, see "Shrinking Planet" sidebar.*)

World-Class CFPs

Yet another trend that's "growing significantly" around the world is cross-border CFP certification, Maye says. A planner working for a major global bank in Zurich recently asked Maye how he could become CFP certified in the U.S. and Switzerland. "Clients aren't being stopped by borders," Maye says. "People are looking across borders, families are living across borders, and people are investing and holding assets across borders. So as they start looking for financial planners they can work with in various jurisdictions; the CFP certification is one of the ways they are identifying who's competent and who's ethical."

Kochis of Aspiriant says there will be some cross-border practice activity--like with the U.S. and Canada and in "the three Chinas," Taiwan, Hong Kong, and the People's Republic. He doesn't see cross-border activity taking hold as much in Europe because of language and cultural barriers (though some companies, like Allianz in the Netherlands, seem to be ahead of the curve: see Dutch Life Planning sidebar on page 48). Advisors who don't believe that globalization will really affect their bottom lines need a wake-up call because more investors are accepting the CFP mark as a "global standard now for competence and ethical practice," Kochis says. "If one realizes that your competition is not necessarily the person on the next street corner but that it's a worldwide profession that's setting a standard that you need to comply with--your potential clients are going to become aware of the global standard."

That's not to say, of course, that only CFPs will prosper in the global financial planning world. Whether an advisor will need to hold the CFP credential is a "function of the regulatory environment in a particular country," Kochis admits. However, "increasingly what will be demanded or expected by the marketplace [in various countries] will be the CFP credential."

Unlike the United States--where the Securities and Exchange Commission (SEC), state regulators, and FINRA--all oversee the advisory industry--internationally when there's just one regulator the FPSB is "seeing some interesting efforts between the regulators and the CFP education bodies to ensure the public is protected--all the way down to regulators looking at some type of registration function for advisors--asking professional bodies to step up oversight of the CFPs for the benefit of consumers," Maye says. For instance, "in Malaysia, the term financial planner is limited in use and the individual must be a member of our affiliate organization there and hold the CFP certification."

International Regulatory Cooperation

The SEC, too, has stepped up its interaction with foreign regulators as the global capital markets converge. One of the Commission's most recent global initiatives is mutual recognition, which the SEC says would "provide foreign exchanges and foreign broker/dealers an exemption from certain U.S. registration and regulatory requirements, as long as those exchanges and broker/dealers were regulated in a foreign jurisdiction with a comparable securities regulatory regime." The SEC is currently piloting mutual recognition programs in Australia and Canada.

But to be a player in the global arena, advisors must be global themselves, says attorney Basha. That means advisors "have to be able to understand what's affecting their clients, they can't skirt away from it, be fearful of it, and say, 'We'll I'm not going to deal with an international client' or when they do, bury their heads and say their accountant or lawyer will be looking out for this or that" issue. Basha also warns that advisors can't simply dabble in helping international clients because "it's fraught with pitfalls." (See Avoid These 15 Tax Traps! sidebar below.)

Advisors must ask the right questions, she says. For instance, while a client might be a U.S. citizen, the advisor should also ask if they have other citizenships. Another question is whether the client's spouse is a U.S. citizen, "If not, then they should think twice about opening a joint account because you have gift tax issues that you otherwise wouldn't have if they're a U.S.-citizen spouse," Basha says.

Planner Glassman, who says 10% of his 74 clients are international, has a client who is a U.S. citizen but his wife is a Canadian citizen. "Unlike my wife and I, he can't just leave his assets to her. He also can't give her money and move it to her name," Glassman says. "If he were to pass and leave it to her, there are going to be millions of dollars in estate taxes leaving it to his Canadian citizen wife versus doing some estate planning and avoiding that."

For non-U.S. citizens, "assets must be left in a special trust for a surviving spouse called a qualified domestic trust (QDOT), which requires a U.S. person as trustee," adds Martin Shenkman, a planner in Paramus, New Jersey. A QDOT is a trust used to postpone estate tax when more than the amount of the personal federal estate tax exemption is left to a non-U.S. citizen spouse by the other spouse.

Getting Help

The most crucial part of dealing with international clients is knowing when to call in additional experts, Glassman says. Dealing with international planning issues "goes beyond knowing your client; it goes to applying the broad-based rules of investment, tax, and estate planning, and knowing when to call in additional experts."

Another tricky area is titling and gifting, Basha says. "When you have a foreign client, you have gift tax and estate tax implications that affect them that don't affect a U.S. citizen to the same extent." For instance, if a foreign individual is investing in U.S. stocks, a U.S. estate tax of 45% is applied, she says, but if the foreign client invests in American Depositary Receipts (ADRs), there's no U.S. estate tax.

If the advisor puts the foreign client into a money market fund, there's U.S. estate tax, but if the advisor puts the same amount in a CD, no U.S. estate tax, Basha explains. "So you have to know how you invest the assets for a foreign individual both from an income tax perspective and an estate tax perspective."

Once investors cross borders into another jurisdiction, "you have a multitude of issues, the primary one being taxes because now you've got two countries trying to often tax the same dollars," Basha says. "How they are taxed depends on how [the property is] titled; so you have vastly different tax results based on how a client invests or takes title to property in the U.S." An advisor could have a situation where if a client dies, "they will have pretty much the whole estate subject to a 45% estate tax, or if [a foreign client] invests in U.S. real estate through a foreign corporation, they have zero estate tax." If an investor hails from a country that has a treaty with the U.S. and is eligible for treaty benefits, it's often beneficial from a tax standpoint because "the two countries have created more preferential treatment than the domestic law would otherwise give," Basha explains.

For example, she says, from an estate perspective, the U.S. has 16 treaties with other countries for estate and gift tax, versus for income taxes, for which there are hundreds of income tax treaties.

Forced Heirship

Countries that are civil law jurisdictions--which includes nearly all the world except North America, the United Kingdom, and Australia--enforce what's called forced heirship, Basha explains. This means that these countries require "a certain percentage of assets to pass to children" so children cannot be disinherited, even "if they're louses or have abandoned the parents," she says. "A U.S. citizen having assets in those countries has to plan for that. And what if their children are minors and that country doesn't permit trusts, now what?"

When dealing with a "multinational family that has their foot in more than one country and is exposed to very different rules, it's not always like a glove on the hand--sometimes it's putting a square peg in a round hole," Basha explains. "You have to plan differently based on the various jurisdictions involved."

What's also quite shocking, Basha says, is that advisors in the U.K. are obligated--whether it's an attorney, accountant, or banker--to file a suspicious activity report with the government if they suspect that a client is not complying with tax laws. "There's a snitchers rule. They can't claim attorney-client privilege. So basically advisors are acting on behalf of the government to turn in clients. In addition, they can't tell the client they are turning them in when they file the report," she says. The rule is part of a European Union directive, and "in England the rule is very strong. The trend is to have all countries following that directive to a certain degree. Even the U.S. is looking at possibly implementing something along these lines."

Advisors should take note, too, that the IRS now has enforced what's called preparer penalties, so anybody who helps prepare a tax return--not only the accountant who signs the return, but also the attorney who may have given the accountant and tax filer some advice, is considered a preparer "and subject to a higher standard of disclosure on the return," Basha says. "Attorneys and accountants now have to scrutinize any position they take on a tax return."

One only has to look at the impact the U.S. subprime loan crisis has had on the rest of the world, as well as oil and energy prices, to know that we are globally connected. Advisors could choose to refuse to be a player in the global arena, as Bank of America did five years ago when it "fired" all of its clients with international accounts, notes Basha. But as planner Kochis points out, to do so is extremely shortsighted and flies in the face of how the world is progressing. Younger generation planners and the children and grandchildren of advisors' clients are going to increasingly perceive themselves "as citizens of the world as opposed to having an isolated focus on one's home country," he says. "The more sophisticated people are moving away from those parochial orientations, and seeing themselves as a participant in not only the global economy but global culture."

Melanie Waddell *is IA's Washington Bureau Chief. She can be reached via e-mail at* mwaddell@investmentadvisor.com.

1

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