Texas State Securities Board

Regulating the securities industry and protecting investors since 1957

INVESTOR ALERT: ROBO-ADVISERS

Investors who don't think they need a lot of face time with a traditional investment adviser have an emerging type of adviser to help them manage their portfolios: Robo-advisers.

Robo-advisers provide automated but still personalized investment guidance. Dozens of firms offer robo-advisory services, with smartphone apps and online portals making it easy to sign up. You'll be asked to fill out an online questionnaire with details about your financial goals, income, assets, risk tolerance, short- and long-term goals, and investing time horizon.

Using a variety of high-tech tools – including advanced software and algorithms – your robo-adviser then crunches the data you've provided and churns out what it determines to be the most appropriate mix of assets for your portfolio.

Robo-advisers can handle single accounts, such as an Individual Retirement Account, as well as multiple portfolios of taxable accounts, college savings accounts, or other categories of investment accounts.

Fees for robo-advisers typically are less than those charged by traditional advisers because the service is largely automated. In addition, robo-advisers often use low-cost index mutual funds and Exchange Traded Funds (ETFs) to build portfolios.

To learn more about mutual funds and ETFs, read the State Securities Board's Making Investments, which explains the basic types of investments, how to manage risk, building a portfolio, and investing costs.

Researching Robos

Firms that offer robo-advisory services must be registered.

Investors can use the SEC's Investment Adviser Public Disclosure site to research the background, including registration or license status and disciplinary history. Robo-advisers are typically registered as investment advisers with either the SEC or one or more state regulators.

Investors can also contact the Texas State Securities Board.

For More Information

The TSSB's Choosing a Financial Professional covers:

- Identifying the type of financial professional you need
- The differences between investment advisers and brokers
- Understanding fees and other charges
- Researching the background of prospective advisers

Adding the Human Touch

Since not everyone is comfortable getting all their advice online, some robo-adviser services have expanded to offer a dose of human interaction.

The cost of the expanded service varies, depending on whether you want to talk to someone online or on the phone, and how often.

For example, you may be comfortable with a robo-adviser most of the time but want to speak with a human expert to discuss strategy during times of market turmoil.

You should consider that robo-advisory services are much more of a one-way street than working with an actual person. While conversations with an investment adviser are likely to result in a valuable exchange of ideas and information, the effectiveness of a robo-adviser can be limited by the information that only you provide.

Compare Robo-Advisers

Robo-advisory firms differ in their approaches.

One thing you should make sure you're clear on is how often your robo-adviser rebalances assets in your account to ensure that the overall mix of investments doesn't significantly differ from your target allocation.

Rebalancing, which involves selling some assets and buying others to keep your portfolio aligned with your investment strategy, can also affect your taxes. For example, if the robo-adviser updates your portfolio frequently, you could have large short-term gains that are taxed at the same rate as your regular income rather than at the lower rate that applies to long-term gains. To qualify for a long-term gain, you must hold an asset for more than year before selling it.

Finally, be sure to consider a robo-adviser's approach to investing before signing up. Just like their human counterparts, robo-advisers have varying investing styles and offer different investment products.

Regardless of whether you use a fully automated service, or a hybrid with some human interaction, the final decision on how to allocate your assets is up to you.

At Your Discretion

Robo-advisers may be discretionary or non-discretionary, meaning a customer may allow the platform to execute trades automatically on his or her behalf or may withhold trading authority and use the platform's advice as a basis for the customer's own investment decisions.

Bottom line: There's little chance the HAL 9000 from "2001: A Space Odyssey" will tell you, "I'm sorry, Dave, I cannot execute this trade."