Responding to HNW fears of scandals

Alison MacAlpine / September 15, 2009

Earl Jones and Bernie Madoff defrauded investors of millions and billions of dollars, respectively. They both ran schemes that went undetected for decades. Then they ended up in the media spotlight alongside reports of unprecedented market turbulence and a global recession.

Accordingly, high-net-worth (HNW) investors are feeling anxious. The question is, what are you doing to maintain their trust in you and your practice?

Dan Richards, president of Strategic Imperatives, thinks advisors need to deal with their clients' concerns proactively. With both existing and prospective clients, he recommends saying something like this: "In light of what's happened with Bernie Madoff and Earl Jones, some investors are a little bit concerned about whether their money is safe â€¦ Would you like to spend a couple of minutes going through the safeguards in place to protect you from fraudulent activity?"

Doug Lamb, a CFP with Dundee Private Investors Inc./Spera Financial in Toronto, has had these kinds of conversations with clients. He methodically outlines the layers of protection that are built into his practice. First, he is a certified financial planner and clients can easily check to make sure his certification is up to date. Second, his dealer is registered with the Ontario Securities Commission. Third, investment recommendations are accompanied by a formal proposal and relevant prospectuses. Sometimes, Lamb goes so far as to include independent reports on mutual funds from Globefund or Morningstar. Fourth, before investing, clients fill out application forms from companies they know and trust. Fifth, cheques are made out to the dealer in trust, never to Lamb personally. And finally, there's the paper trail.

"Too often, advisors say, 'You don't want all that paperwork so I'll tell the investment companies not to send you stuff,' " he says. "That's just not good practice. They should have independent verification of their holdings periodically from the investment companies or the fund companies, as well as from the advisor or the dealer."

Éric Mercier, conseiller principal with Mercier Services Financiers inc. in Quebec City, operates in the home province of Earl Jones. In Quebec, the Norbourg Asset Management and Triglobal Capital Management scandals are still fresh in investors' minds. He's been fielding indirect questions from HNW clients along these lines: "We know you're not a crook, but if somebody was [a crook], how would he do that and what do I need to do to protect myself?"

Mercier says he hasn't lost any clients, but he acknowledges that the current environment may see some investors leave independent advisors for the perceived safety of the banks. Where independent advisors have the edge, he says, is in the HNW market. That's because HNW investors demand more services, advice and time — and the banks can't necessarily deliver this. Since many of Mercier's clients are business owners, he also has the advantage of being an entrepreneur working with entrepreneurs.

"That's not what you get at a bank," he says. "You get an employee dealing with an entrepreneur."

At the same time, Craig Hayman, principal, products and services, at Edward Jones' headquarters in Mississauga, Ontario, believes it's important to have a large institution standing behind you, reinforcing your personal credibility.

"The sad thing is that, in any basket of apples, there are usually one or two bad ones," he says. "A very difficult market environment and economy â€¦ heightens the sensitivity of the regulators, it heightens the sensitivity of the clients and it certainly heightens the sensitivity of the media. All of that together means the questions that we're hearing â€¦ they're simply saying, 'Is this a safe place for me to do my investing?' "

Advisors should have materials on hand that emphasize their professionalism and principles, Hayman suggests. But he adds, "I don't think you can tell somebody you're trustworthy to build trust. I don't think you can ask for somebody's trust â€¦ I think the only thing you can do to create trust is to act trustworthy."

Like Lamb, David Burnie, a CFP with Ryan Lamontagne Inc. in Ottawa, thinks advisors can "defuse the bomb before it goes off" by demonstrating to HNW clients that they have appropriate credentials, that they're licensed by a provincial securities commission and that they have a reliable custodian. A comprehensive letter of engagement completes the package, letting clients know what they can and cannot expect from you.

"My clients always know where they stand," he says. "Keep it simple. Keep them informed â€¦ Trust is something you earn. It's not something you hang on the wall."

Richards says advisors need to recognize that they may not be able to keep every client when investment fraud cases are splashed across the headlines. So, beyond focusing efforts on retention, they need a plan for business growth. That way, new clients will be on the way in, if existing clients leave.

It may feel like the worst possible time to ask for referrals, especially since both Madoff and Jones fuelled their fraudulent activities with recommendations from family and friends. Furthermore, Richards says that, especially in an environment of poor market performance, investors are reluctant to jeopardize relationships by making referrals that may not work out.

Still, he thinks advisors should persevere. Before meeting with a client, send out an agenda, he suggests. Tell your client that you have the capacity to take on a certain number of clients this year, so you've added one item at the very end of the agenda. Explain that, after you've covered everything your client needs to discuss with you, you'd like to take a few minutes to talk about the types of clients you work with most effectively.

"At the end of that, you could get a little more aggressive and you could say, 'Tell me, just out of curiosity, does this profile fit any of your brothers or any of the people you work with?' " he offers. "Now you're becoming a little more assertive, which may or may not be right depending on the client and the advisor."

If you do win a meeting with a new prospect, chances are some trust will transfer with the recommendation. But don't assume that's the case.

"I always try to treat people as if they're just off the street and I have to earn their trust," emphasizes Lamb. "You do your homework. You're prepared. You give them the information they need to make informed and considered decisions. And you provide service to them — you don't just sell them product."

Richards says the advisors who have the best opportunity to attract HNW clients in the current environment have identified the value they deliver to their clients and have clear processes in place to deliver that value.

Even more simply, he says, successful advisors listen to their prospects and clients.

"Over the years, I've talked to a ton of investors. I have yet to run into an investor who says, 'You know, my advisor is a great talker,' " he says. "I run into lots who say my advisor is a great listener."

So listen carefully. Communicate and deliver on your value proposition. Most importantly, explain how your clients are protected from fraud. You'll be well positioned as long as Madoff and Jones linger in investors' memories — and when the next investment scandal inevitably rolls around.

Alison MacAlpine is a Toronto-based editor and writer.

(09/15/09)