

The Client is Always Right, or is He?

By Christopher Tan

For the longest time, we have been advocating that the best way to give financial advice is to charge only a fee for advice and not take commissions at all. Since 2003, detractors to this approach gave their reasons (or rather excuses) for not adopting this advisory model. Some said that Singaporeans are not ready to pay a fee. Others said that commissions will not affect the objectivity of advice and some said that it is ultimately the integrity of the adviser that counts. The latest of all these excuses was in a recent interview by The Edge (28 May 2007). The director of one of the commission-based wealth management firms said: "One may think that the fee model is the best but clients can always disagree and the client is always right." He added that he won't force his clients to pay a fee if they don't want to. "There are many investors with different needs and mindsets. To do well in a small market like Singapore, I think a win-win model is to listen to what clients want." Another CEO of a commission taking wealth management firm concurs by saying: "whether fee or commissions, the choice is really up to our clients." But are the clients always right? Is the choice really up to the clients? Or are we using our clients' name in vain, to satisfy our own need for profitability?

About 2 years ago, someone asked a 60 years old retiree to come and take advice from me. He is a pensioner and has just received half a million dollars for his retirement. Sadly, the half a million dollars is about all that he has got. Due to poor advice, he invested a large part of his savings in technology funds in 1999. He lost 80% of his money in that investment. He now needs to make sure that

this amount of money will last him throughout his retirement. Fortunately for this gentleman, he is quite thrifty and do not require much for his monthly spending. As such he need not take too much risk in his investment to generate a high return on his capital to make his retirement fund last till his life expectancy. He also does not have the ability to take high risk as he needs an immediate draw down on his capital to fund his livelihood. But when I asked him to complete a set of risk questions to assess his risk appetite, he was very willing to take risk. In fact, he WANTS to take risk. Here is case of someone who need not take risk, cannot take risk but wants to take risk. So, if the client is always right, I should have just given in to his wants and recommends some high risks instruments for him. If the market turns volatile and his retirement lifestyle is affected, I would simply tell him that this was his own wish and he as a client is always right. I would have also covered myself legally as he has completed the risk questions as required by the central bank. But would that be the correct thing to do? Would I be a good adviser to him?

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Some years back, a couple came to see me for financial advice. In the area of risk management, the husband would need an additional insurance coverage of \$600,000 so as to ensure that his family lifestyle would not be affected should he pass away prematurely. Although we recommended him to take up a term insurance plan of less than \$2,000 per year in premiums to cover him till his planned retirement. He insisted on buying a whole life plan as he has been told that he will at least get some money back from his whole life plan unlike a term insurance plan, where he will not have anything back on expiry. When I told him that a whole life plan would cost him about \$15,000 or more a year in premiums, I thought he would see the light and go for the term insurance cover. Instead, he still asked for a whole life plan but with a much lower coverage to fit his budget. We have always suggested that the best way to cover against loss of income due to death, disability and illness is through the use of term insurances and not whole life plans. This is because:

- a. Most of us don't need insurance cover beyond our retirement years, except for medical expense insurance such as Hospitalization & Surgical plans as in our retirement, income is not the problem and we would likely have no dependents to depend on us for income.
- b. The premiums for whole life plans can be 10 times more expensive than term plans and as such one can never afford to cover their risks fully.
- c. It is a misconception that whole life plans give you returns and a term plan does not. It is only because you have paid a lot more extra in premiums above the mortality (insurance) charge that the insurer can use this "extra" premium to

invest for you. The mortality charge, just like the term insurance premiums is always expended and not invested for returns.

So if the client is always right, I should have again given in to their wants and let them go for a lower cover. If death happens to the husband, and his family has less than enough to live day to day and his children suffers, I would simply tell his wife that this was what they wanted and they as clients are always right. Again, I would have covered myself legally as all this discussion will be well documented and signed by them. But once again, would that be the right thing to do? Would I be a good adviser to his family? These are rhetorical questions, isn't it?

By now, you should get what I am trying to drive at. How can the client be always right? If they are always right, they wouldn't need to see an adviser in the first place. They can decide what they want and simply buy products on their own. If the client is always right, what is the value of financial advisers? No wonder many out there, especially the more financially educated ones often think that getting financial advice is a complete waste of time. Can you imagine a patient seeing a doctor and when the doctor prescribes a certain treatment, the patient refuses it and suggests an alternative? Will the doctor give in to the patient's wants and say: "Oh, because the patient is always right." Is unthinkable isn't it?

Maybe customers are always right. But clients, they aren't. They come to us for professional advice and they expect us to tell them the right thing to do. Customers are always right because product salespeople want to give in to all their wants so that their customers will make a quick decision to buy from them. However, the financial advisory profession is not a sales business! It is an advisory business. We don't have customers.

We have clients that depend on us for best advice. But even customers may not always be right. Recently, I went to a Chinese restaurant with a friend. We were over enthusiastic and ordered one dish after another. Halfway through, the waitress stopped us and said we probably over ordered. Despite us telling her that we really wanted to try a certain specialty from the restaurant, she gently advised us to cut down. Fortunately, we took her advice. We were really full three quarter through the meal. Imagine if she has given in to our wants. We would either have over eaten or wasted plenty of expensive food. Both ways, we would have been upset.

If the food and beverage people know how not to always give in to their customers and they do it for their customers' interest, we professional advisers have a lot to learn.

Interestingly, since 2003, many wealth management firms that were interviewed somehow agree that charging only a fee encourages the growth of independent advice, which is best for the clients. But many cited market readiness as well as survivability of the firm as reasons for not moving into this model, even though it is a better model. Healthcare giant, Johnson & Johnson states in the first few paragraphs of its credo that their first responsibility is to their customers which are the patients, the doctors, the nurses and so on. Their last responsibility is to their shareholders. They believe that if they take care of their customers, shareholders will be rewarded ultimately. Maybe as wealth management firms, we should not focus too much on our bottom line but focus on taking care of our clients' interest. Once we do that, the bottom line will take care of itself.

This article is not about whether the fee-only model or the commission-based model is right or better and I have nothing personal

against commission-based advisers. My point is that as professionals, we must truly believe in what is right for our clients. Whether it is the fee or commission model, whether we decide on using term or whole life products, whatever investment products we want to recommend to our clients, we must do so because we have searched our hearts and know it is truly the best for them. Let us not use the clients as an excuse to achieve our own financial end. We must have the courage to do what is right for them. To the clients out there, if your advisers do not always give in to your wants, thank them, for they really have your interest at heart.

Why did we take time to convince our clients on what they should do instead of giving in to their wants? Because we are not salespeople but adviser to our clients and we have a fiduciary responsibility to tell them what is best for them and their family. We have an obligation to them to tell them, albeit nicely, that they are not always right.

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