



FAIS promotes true alignment of interests

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The Financial Advisory and Intermediary Services Act, 2002 (FAIS) is very clear when it refers to its objective. The interests of the consumer must be served and one thing is for sure: If the interests and actions of financial advisors are not aligned with the interests of their clients, it will be impossible for investors, especially for people planning for their retirement, to achieve their long-term investment objectives.

The investor, advisor, administrator, multi-manager and asset manager make it possible for investors to achieve their investment goals.

These parties are interdependent. If any of them follow a selfish agenda, success will be impossible. The whole process of true alignment starts with the financial advisor. If he/she aims astray as a result of ignorance or serving own interests, the efforts of all the other parties become meaningless. But before we go into the issue of serving own interests, it is important to understand the current status of the relevant parties, with specific reference to individuals planning for retirement.

Current status of role players

Investor

Investors generally do not take enough responsibility for their own decisions. In many cases they expect financial advisors to be magicians. Many investors expect advisors to grow their capital at unprecedented levels, without investment risks. Because of their unrealistic expectations, such investors make life difficult for advisors. Ignorance is the main reason for these perceptions and that is why the focus on appropriate advice in terms of FAIS is so important. Desperation, greed

and ignorance are human elements that can be managed through simple consumer education techniques.

FAIS emphasises consumer education. The fact that advisors are faced with the legal obligation to lead their clients into making well-informed decisions will help advisors to take more care in their planning process. However, investors will have to accept that the ultimate decision is still theirs and with it they will have to accept some responsibilities.

Advisor

Our industry has many competent advisors, which I am proud to name my colleagues, and some even my friends. The assurance I can give consumers is that there are many advisors with a true desire to serve their clients, regardless of the industry perception.

One thing that professionals in this environment have learnt over the last years is that we desperately need better and sustainable investment solutions for individuals with a need for wealth preservation.

Once again FAIS will help to distinguish between investors' wants and needs. One of the most important obligations of an advisor is to do a client needs analysis. If investors do not truly understand clients' needs they will never be able to make appropriate recommendations.

Advisors must also ensure that all other role players are aligned with the proposed investment strategy. They should become the clients of the other role players. But there is one serious prerequisite – advisors must know what they are doing!

Historically, I had to use investment models that were based on theories, written by academics that did not have the privilege of serving the needs of people

who just could not afford to lose their capital or just could not afford negative returns. Hopefully FAIS will help more professional advisors and their clients to distinguish between investment objectives that are measured subjectively and objectives that can be measured according to objective benchmarks. The main reason for this statement is that the way you feel about your investments leads to herd behaviour, which would not pass the appropriate test. Furthermore, it exacerbates the issue of trying to hit a moving target continuously. On the other hand, investment objectives that are measured according to objective benchmarks, like inflation, tend to lead to rational investor behaviour, which is aligned with the new legislation's objectives.

Investors will also have to come to grips with the fact that although advisors are obliged to serve clients' interests, it does not mean that they have to work for free. Alignment of interests will be the key to successful investing – especially for those planning their retirement.

Administrator

Currently the administrator, like a Linked Investment Services Provider, is responsible for administration only. Investors tend to underestimate the importance of sound administration of investment schemes and that it costs money. It is important that advisors try to keep a sound balance between cheap administration fees and making sure that the administrator can continue with a sustainable business. This is also of importance for consumers as I have witnessed a number of administrators that cut their fees to such a point where they could no longer sustain their business. This resulted in admin-intensive take-overs, causing clients a lot of heartache and in some

cases, additional costs.

In many cases administrators were forced to request “kick-backs” from fund managers to maintain their businesses, which obviously cannot be tolerated under a FAIS environment. In other cases advisors were putting pressure on administrators to pay them additional commission above their advisory and management fees, which developed into a vicious circle. I am confident that this practise will be exposed under the new law as the “kick-back” system does not serve the interests of the consumer and as it is not disclosed to consumers in general, it also means that this practice will be non-compliant.

MSCI World Index, S&P 500, the JSE etc.

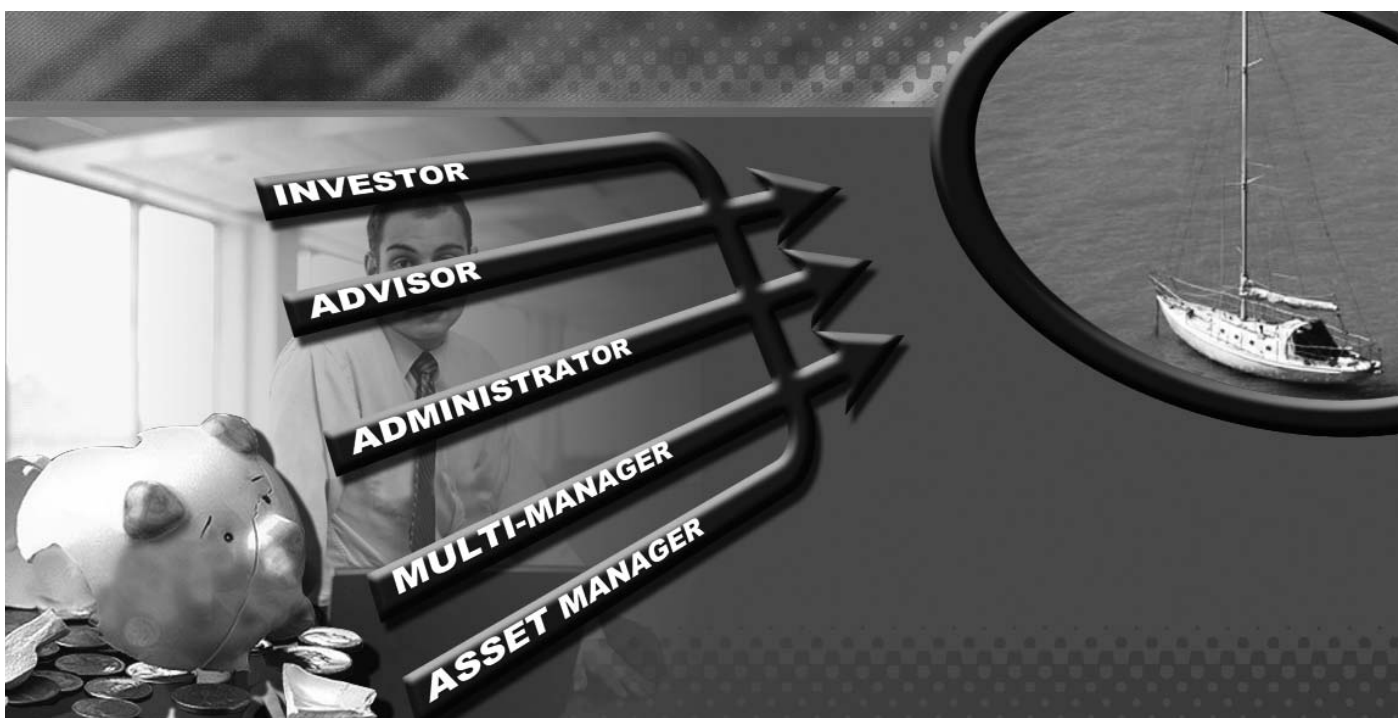
Financial advisors have been tasked to construct portfolios to meet investors’ objectives, which are based on absolute return expectations.

Asset managers made ongoing suggestions to advisors pertaining to ideal asset classes and portfolios and then it was up to the financial advisor to make the changes. This allowed investment advisors to become quasi-asset managers – a job that the majority of advisors are not “fit and proper” to do.

Asset managers are in a much better position to manage investment portfolios according to absolute return benchmarks.

advisors.

● Salespeople are forced to become professional financial advisors.
● Investors have lost a lot of money over the years. Many “advisors” were blaming the markets, but perhaps one should also question some of the advice given and some of the investment tools. One of my favourite quotes is by Warren Buffet, who said: “It is only when the tide goes out that you can see who has been swimming naked.” I think that this principle also applies to financial advisors - when the good tide of the markets turned, one could clearly see investment philosophies showing their true colours. Although painful, these lessons will stand us in good stead in



Multi-manager

The multi-manager can be friend or foe, depending on how they apply their services. In my view, they are friends if they do the following:

- Listen carefully to the needs of professional financial advisors who are trying to serve their clients – especially those who expressed the need for wealth (preservation).
- Make pro-active suggestions to improve current models, instead of persisting with their own asset allocation models as it defeats effectively the object of true multi-management.
- Charge fair, market-related fees.

Asset manager

Historically, asset managers have been measured based on investment portfolios with relative benchmarks, like the Nasdaq,

Hopefully asset managers will be measured differently in future. The time is long overdue for asset managers to manage assets and financial planners to do financial planning. I am also confident that FAIS will help us all to focus on our respective strengths and to stay out of each other’s areas of expertise.

Hopefully fit and proper requirements of FAIS will take care of the confusion that existed and allow true professional advisors to take their rightful place in the circle of professions.

Need to revisit current position

An industry turned into a profession

● Historically, investment advisors were insurance salespeople that sold investment plans. It became clear that investment planning requires a lot of technical skills and as a result more highly trained people joined the industry as financial

future.

● The only way to protect the consumer was to turn the industry into a profession and there is one major difference between the selling game and a profession. A salesman sells on the upside, whereas a true professional knows what can go wrong and protects his/her clients against it.

Ethics, legislation and codes of conduct

- Many countries have implemented legislation to protect consumers against poor advice.
- As the industry turned into a profession, more attention was given to advisors’ ethical behaviour. We will see the same happening in South Africa.
- The profession needed a code of conduct to guide advisors in their day-to-day practice.

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Offering professional financial and investment advice requires different skills

- Financial and investment advisors are experts who have to focus on general issues affecting investors. Subjects like individual tax and estate planning, general financial planning, and investment planning are specialist subjects. To keep up with all the changes require full time attention.
- What we have seemed to miss is that the fundamental difference between plan-



ning and asset management is that planning deals with timeless fundamentals, which can be controlled. On the other hand, asset managers, economists and actuaries tend to be experts in understanding the variable elements.

- Asset management requires specialist skills that are totally separated from that of giving holistic financial and investment advice. If financial advisors confuse the subjects it will lead to one of the areas, or both, being neglected.

I am confident that we will see a generation of financial advisors that will take up the challenge of enhancing their levels of advice and alignment of interests, thereby also enhancing the level of the industry's integrity.