



# Building Trust in the Age of Madoff

By Bill Bachrach, CSP, CPAE



On January 27th this magazine co-hosted a webinar entitled Building Trust in the Age of Madoff; 10 ways to answer the question, "How do I know you or your money managers aren't stealing my money?" The 1,000 seat capacity to participate in that webinar quickly filled up so we knew we hit a nerve and the response from the participants was very positive.

This article is a summary of a few of the key points from that webinar. If you missed the webinar and like what you read here, you're in luck because it was recorded. You can go online at [www.baivbfp.com](http://www.baivbfp.com) to view the recorded version.

So, how *do* you answer the question, "How do I know you or your money managers aren't stealing my money?" Of all the events in 2008 that can affect the relationship between a client and their advisor, the Madoff scandal was a biggie. At the end of the day, your clients don't really believe that you could have or should have known when the markets were going down, when to get them out, time the bottom, and get them back in. Even if they were looking for a scapegoat to vent their frustration for their losses and fired their advisor, deep down most people know that nobody can predict the markets. Stealing from them, on the other hand, is another matter entirely. This is something you DO have control over and placing their money with a money manager who won't steal it is your fiduciary responsibility.

This was well summed up by James Hedges IV of LJH Global Investments who said, "Letting Madoff manage your money wouldn't pass an institutional-quality due diligence because when you get to page two of your 30-page due diligence questionnaire, you've already tripped eight alarms and said I'm out of here."

Christine Williamson wrote in the Pensions & Investments newspaper, "Most major U.S. institutionally oriented hedge funds didn't have anything to say – they had passed on Mr. Madoff's funds because he wouldn't provide enough transparency on the investment process."

One thing you can tell your clients to assuage their fears about you and the money managers you place your clients' assets with is to explain the thorough and effective due diligence process you use to determine where you place their money. If you didn't have

this level of a due diligence process a few months ago, you better have one now. It sounds like this, "One reason you can be secure in the knowledge that your money is not currently, and will never be, in the hands of someone who can steal it is because we have a 15-step process for screening money managers. Madoff would not have gotten past step four. Would you like me to show you every step in the process and how it works?"

Perhaps the advisors at most risk right now are those who still put together their own portfolios and do the securities selection. You know you're honest, but would you pass an institutional level due diligence process? Food for thought.

Where does one find a due diligence process like this? I googled "institutional money manager due diligence" and found many sources of valuable information that can help you get this done. Many fund-of-funds companies boast about their "rigorous due diligence process." Ask to see it. If I were still an advisor I would ask the most respected money managers I worked with to tell me exactly what they would do to screen a money manager if they were on the other side of the table as an investor.

Another way to handle the question is the approach of our financial advisor, Mark Little. He has a peer review process that makes it almost impossible for something like Madoff to happen to him and his clients. Here's how he would explain it to a client, "As you know, we have a team of independent, subject matter experts who provide a multiple layer, peer review in the creation and implementation of your financial plan and every element of that plan, including the investments. We identified these professionals as the best-in-class CFPs, CPAs, lawyers, money managers, and insurance experts to create and implement your plan so you have the highest probability to achieve your goals. They don't just work with us. They have their own separate businesses, clientele, relationships with other financial advisors, transparent processes, and are accountable to each of their own industry's regulations. The probability of all of these individually vetted and independently credentialed professionals being willing to risk their professional careers and personal freedom to conspire in a scheme like this is almost impossible. Ponzi schemes are predictably master-minded and executed by one person who has eliminated all the usual checks and balances, as was the case with Bernie Madoff. What other questions do you have so I can help you be confident that we're looking out for you

so you don't have to worry that someone is stealing your money?"

The power for Mark in having a Deliverables Team of Subject Matter Experts is the fact that it truly is very unlikely that multiple independent professionals from reputable companies governed by separate regulatory agencies are going to successfully conspire to steal people's money. Somebody is going to blow the whistle.

Another great response is the age-old investment rule of diversification. It might sound like this, "You have a globally diversified portfolio of investments across all asset classes with many different money managers. Each is an expert in their particular category. All of them have met our stringent due diligence process. In the unlikely event one of them is a crook it can't affect more than \_\_\_% of your portfolio. Frankly, the people who got burned by Bernie Madoff violated many basic rules of investing, diversification being the most obvious. How else can I help you be confident that we have this under control so you don't have to worry about someone stealing your money?"

In today's economic environment I'm not a fan of leaning on responses like, "Even if I screw up and your money does get stolen the SIPC will make you whole." First of all, that doesn't really answer the question, "How do I know you or your money managers are not stealing my money?" Secondly, many people these days aren't especially confident that these government guarantees are adequate. Can you blame them? What's that old saying? "An ounce of prevention is worth a pound of cure."

A pattern that you will notice in each of these responses is that they follow some of our basic rules for trust-building communication. They are succinct, direct, and delivered with confidence. They also end with a question inviting the client or prospective client to ask whatever they need or want to ask to feel confident they can trust you and your processes. This is not just a question of you knowing what to say and how to say it. It is also a function of you being a very good financial advisor who has your ducks in a row. That means you have systems and processes for taking care of your clients and you are a stickler for making sure your systems and processes are followed. If this does not yet describe you, I encourage you to continue to move in that direction.

Chances are that you won't need more than one of these responses to answer the question, "How do I know you or your money managers aren't stealing my money?" Or you may find that by combining 2 or 3 of these responses will provide you and your clients with all the confidence necessary to continue to place your money and their money in the hands of the thousands of capable and trustworthy money managers.

Remember, this is a great time to be a financial advisor!

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