

# Fiduciary Lessons Learned from Scoundrels and Thieves

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# Fi360



Mission: To promote a culture of fiduciary responsibility and improve the decision-making processes of investment fiduciaries.

## Topics to be covered

- Why are there so many scandals?
- Fiduciary findings – What did fiduciaries miss or where did their processes fail?
- The highest cost of scandals – the collapse of investor trust and confidence
- How to help avoid future scandals and restore trust

# Why so many scandals?

- Incredible rewards for short term success
- No perceived penalties for long term failures (moral hazard)
- Crony (false) capitalism
  - Regulatory capture
  - Lack of transparency and meaningful regulation
- Ignorance of, or inattention to, fiduciary responsibilities

# Fiduciary Finding 1: The best defense is a great IPS

- The IPS is the management plan
  - Roles and responsibilities
  - Due diligence procedures
  - Risk management policies

## Fiduciary Finding 2: Rely on RFPs, not references

- People still using a service provider will never say they are stupid to do so
- Scoundrels seek to penetrate particular networks such as
  - Foundations and endowments
  - Religious communities
  - Charitable and cultural circles
- Select service providers through a request for proposal process; conduct background checks; read disclosures

# Fiduciary Finding 3: Self-custody is a big red flag

- Advisors should never take custody of assets
- Statements can be readily manufactured
- Checks and balances are essential
  - Administration: Custodians, TPAs, Recordkeepers
  - Managers
  - Advisors
  - Trading firms (broker-dealers)

## Fiduciary Finding 4: Value isn't a matter of opinion

- Securities should be “marked to the market”
- Independent valuation of securities is essential
- Intensely question the value of any asset if there is not an active (preferably auction) market

## Fiduciary Finding 5: Trade records are telling

- A great deal of money can be made from trading commissions (churning)
- Heavy trading bets with growing frequency suggest desperation
- A preponderance of principal trades suggests self-dealing
- Money never deposited never gets traded – this is where Ponzi schemes can often be detected
- Examine all custodial statements

# Fiduciary Finding 6: Alternatives aren't for everyone

- Alternatives are generally not:
  - Regulated
  - Transparent
  - Easily valued
  - Liquid
- Alternatives are generally:
  - Extremely profitable for the providers
  - Difficult to understand
- Extraordinary due diligence is required

# Fiduciary Finding 7: Key systems should be audited

- Financials – (AICPA recognized auditor)
- Performance (GIPS)
- Control Procedures (CEFEX\*/ASPPA Recordkeeper Certification; SAS 70)
- Investment Fiduciary Practices (CEFEX\* Certifications of Stewards, Advisors, and Managers)
- Fiduciary Adviser (DOL requirements)

\* Disclosure: fi360 is a founding member of, and has an ownership interest in, CEFEX

## Fiduciary Finding 8: Heuristics can help

- “Too good to be true” often is
- Where there is smoke, there often is fire
- Don’t put all your eggs in one basket
- Act like you are from Missouri, say “Show me!” [A black box is what gets opened after a disaster to determine what caused the catastrophe.]
- Money is a better servant than a master

# Trusted professionals?

- Financial scandals, on top of market meltdowns, have destroyed trust
- Financial service representatives are not held in high regard
- Investment fiduciaries – Stewards, Advisors, and Managers – are in the best position to restore trust by exposing scoundrels and thieves and preventing future scandals

# Legislative & Regulatory Trends

- More transparency and exemption-oriented rules
  - PPA statutory fiduciary advisor exemption
  - Class exemption for conflicted advisers
  - 408(b)(2)
- Rules-based regulations can be effective but are inefficient (*Fiduciary Lite*)
- Principles-based (Fiduciary) approach is both more effective and efficient (NASAA initiative)

**Bottom line:** The rules-based approach is, at best, a transitory phenomenon.

## Call to action

1. Raise your fiduciary IQ and polish your professional reputation
2. Counter market and economic uncertainty with trustworthy fiduciary processes.
3. Seek simplicity: business models, fees, affiliations, disclosures, communications, etc.
4. Play great defense: market, litigation, regulatory and business risks are at all-time highs.
5. Hold legislators, regulators, professional associations, and service providers accountable
6. Go to [fi360.com](http://fi360.com) for more information and to the fi360 Blog ([blog.fi360.com](http://blog.fi360.com)) to continue this discussion.

# Questions or Comments?

# Announcements

- Fi360 will be hosting three exciting events in Scottsdale, AZ May 5 - 8, 2009:
  - 2009 fi360 Conference
    - **Agenda Just Released!**
  - Capstone Accredited Investment Fiduciary® (AIF)® Program
  - Fi360 Toolkit Workshop

Visit the fi360 Conference page for more info:  
[fi360.com/conference09](http://fi360.com/conference09)

- Mark your calendar! New Resources Webinars will be available quarterly. The next event is tentatively scheduled for Thursday June 4th from 4:00 – 5:00 p.m. Check back for content details and registration links as they become available.

# Webinar Special Offers

**Conference:** mention “Fiduciary Lessons Webinar” on your registration form and receive \$100 off the current conference registration prices. Sign-up for all three events and save even more. Go to [fi360.com/conference09](http://fi360.com/conference09) to register.

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Blaine Aikin is the Chief Executive Officer of fi360. Fi360 is a national and international leader in the field of investment fiduciary responsibility, providing training, Web-based analytical tools, and resources for those who manage money on behalf of others. He is the author of numerous articles on the subjects of fiduciary responsibility and investment management, and the author of the monthly Fiduciary Corner column in InvestmentNews magazine.

Blaine received his Master of Public Management and Policy degree from the Heinz School of Carnegie-Mellon University. Upon graduation from CMU, he was selected for the prestigious Presidential Management Intern Program which involved management assignments in the U.S. Department of Treasury and the U.S. Senate. He subsequently served as Budget Officer for Prince William County, Virginia. Blaine then entered the private sector in professional financial management. He earned the Certified Financial Planner (CFP) and Chartered Financial Analyst (CFA) designations and served as a principal and Chief Investment Officer of Allegiance Financial Advisors. After providing contract training and consulting services for PNC Financial Services Group, Blaine became a Senior Vice President and Director of Product Development and Management for PNC Advisors. For several years, he also served as an adjunct faculty member of the College for Financial Planning; providing instruction in investment planning and other subjects leading to the Certified Financial Planner designation.



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Rich Lynch is the COO of Fiduciary360, which delivers training, tools and resources for investment fiduciaries. As one of the main instructors for fi360 Training, he is instrumental in providing investment education and training programs that award the Accredited Investment Fiduciary® (AIF®) and Accredited Investment Fiduciary Analyst™ (AIFA®) professional designations. He also provides oversight to fi360 Tools, which has developed sophisticated Web-based tools and reporting, including the innovative Fiduciary Score™ and the Fund Family Fiduciary Rankings™ for trustees and investment professionals.

Rich assisted with the development of the industry's fiduciary handbook series, **Prudent Investment Practices**.

Rich graduated from the United States Coast Guard Academy with high honors in Economics-Management, where he received the Superintendent's Award for leadership at graduation. During his twenty-year Coast Guard career, he served aboard three ships as Operations Officer, Executive Officer and Commanding Officer respectively. In addition, he held various senior-level financial management positions, including an assignment to the National Pollution Funds Center, a newly established Coast Guard unit responsible for managing the \$1 billion Oil Spill Liability Trust Fund. Rich received his Master's of Business Administration degree (Magna Cum Laude) with an emphasis in Operations Research from George Washington University.