

# Clientel



*The central message of Clientel is that I value my clients.  
I'm as close as your telephone, and available  
and anxious to serve you.*

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Welcome to another edition of *Clientel*. In this issue, I shall discuss:

- A brief stock market commentary
- Some comments on “fee-based” financial advisory services
- What is a financial plan?

## **A Stock Market Commentary**

On July 24, I sent a letter to all clients that contained extensive comments with respect to stock markets and investment strategies.

(If you would like another copy of this letter, please let me know. You can also view the letter on the Rogers Group Financial website at [www.rogersgroup.com](http://www.rogersgroup.com)) — click on “Our Financial Advisors,” then on “David Chalmers,” and then scroll down to see the letters and newsletters I have sent to clients.)

As I went into considerable detail in my letter in the summer, I shall only make very abbreviated comments in this newsletter. Suffice it to say, we do indeed “live in interesting times.”

Stock markets continued to decline in 2002 and hit a low point in October. There has been a

general upward movement in prices over the last several weeks punctuated by days in which substantial losses have occurred.

While the general upward trend of recent weeks is encouraging, it is difficult to judge whether or not the horrific “bear market” that we have gone through has ended and we are now in the recovery phase, or whether we are simply experiencing “the calm before the storm.”

Interest rates are at their lowest level since World War II. Some economists are predicting a major recession or depression coupled with deflation and even lower interest rates. Other economists are predicting renewed government deficits in Canada and the United States. (Any such deficit in the United States would be exacerbated by any military action in the Middle East). This could cause a renewal of inflation and higher interest rates.

With the uncertainty that we are facing with respect to interest rates and stock markets, it is very important that each and every client has their investments allocated amongst investment classes in the most appropriate way to hedge their position against the various outcomes that can occur. There is a risk in being in the stock market, and there is a risk in not being in the stock market. There is a risk in committing money to interest-bearing investments at this

time, and there is a risk to not committing to interest-bearing investments. There is a reasonable and prudent balance for each and every client, which should be driven by each person's specific financial resources and objectives. As I meet and speak with clients, we are always seeking to refine our strategies to provide the best possible likelihood of financial success.

## Fee-Based Financial Planning

In my July 24th letter, I noted that I was considering a "new model" for managing client accounts. I have, in fact, decided not to introduce a new option at this time. I shall, however, make a few comments on the strategy that I have been considering, as I may introduce it as an option at some point in the future.

I earn my income from the commissions that are embedded in the financial products that I place on behalf of clients. For example, I earn a service commission for placing mutual funds for clients. The cost of this service commission is built into the management fee of the respective mutual funds. I earn a commission for placing guaranteed investment certificates or insurance products. The issuer of the GIC or insurance product builds a commission into the product pricing.

This approach has both advantages and disadvantages. The primary advantage to my clients is that there is no "extra billing." My compensation is built into the products that I recommend for clients. I also have made a concerted effort to make sure that the products I recommend are priced fairly (that is, they are not deliberately inflated in their price in order to provide for a higher commission).

There are three main disadvantages with the approach that I currently use: (1) conflict of interest; (2) client subsidization; and (3) a misunderstanding of competitive advantage. Let me

address each of these:

**Conflict of Interest.** Different products have differing levels of commission built into their pricing. Thus, when I arrive at an asset allocation for a client, I am also determining the amount of compensation that I will earn. The potential for conflict of interest here is obvious. While I try to set the potential conflict aside and focus on the most appropriate allocation of investments for that client's specific circumstances, the fact that there is a potential conflict is troublesome to me.

**Client Subsidization.** As I make different investment recommendations to different clients (everybody's circumstances are different), the level of revenue that I derive from one client's portfolio may differ quite substantially from the revenue I would earn from another client's portfolio (even with the same quantum of assets). This means that not only is my revenue from some client accounts greater than from others, but also I am sometimes put in the position where I will earn a profit on the management of accounts for some clients and lose money on the management of accounts for other clients. Thus, in essence, some of my clients end up subsidizing others. This is a scenario that troubles me.

**Competitive Advantage.** I am quite aware of the overall costs for financial products and services that I provide versus the costs generally in the marketplace. I believe that, in most instances, I (and, therefore, my clients) enjoy a competitive advantage. I am quite happy to calculate an overall management expense ratio for any of my clients (feel free to ask me at our next meeting). This "competitive advantage" is, however, often not readily apparent, as I generally do not state costs in the same way that many of my competitors (who run fee-based accounts) state their costs.

**The Essence of a Fee-Based Approach.** The most common approach for a fee-based account

is to place only products that have no commission built into them on behalf of clients and to charge a fee (usually based on the size of the account).

A variation of this is to place the best products possible, regardless of whether or not a commission is involved. A fee is charged and any commissions are “netted against the fee.” If the commissions exceed the fee, the excess is refunded to the client.

These approaches have some appeal to me and, similarly, some potential pitfalls (for example, a client who is not hither to paying a fee might find it difficult to pay that fee, even though his or her overall expense for the account may not have changed or may have diminished).

After studying the pros and cons of introducing a fee-based option, I have decided to stay with my current approach for now. The primary reason for this is that, in my opinion, the expense and complexity of making the change outweighs the potential advantages at this point.

My most likely approach is to do nothing for the foreseeable future. If at some point in time I feel that I can efficiently introduce the fee-based model for clients, it would be my intention to give all existing clients the choice of moving to the fee-based model or staying with the existing model.

## What is a Financial Plan?

There is a certain amount of discussion in our industry as to what does or does not constitute a “financial plan.”

As a financial advisor (a.k.a. a financial planner), I prepare financial plans for clients. However, I note that the “plans” I prepare follow a template that is quite often different from the approach taken by other advisors in the industry.

My typical approach is to meet with a prospective client and gather information. Following

this, I usually build a computer model that simulates the client’s long-term financial future based on reasonable expectations of investment return, inflation, and taxation. I usually accompany this with a letter that outlines a series of investment recommendations and an action plan.

I meet with clients regularly. Where strategy is discussed in a meeting, I usually provide a letter (or email) summarizing the meeting in order to update the strategy that we have on record. (If the meeting is administrative in nature or deals with a specific transaction, I may only summarize that specific transaction).

While I have done a great deal of “financial planning” for clients (in many cases, over a time span of many years), I generally have not produced a single document that can be referred to as “the financial plan.”

I note that there are a number of software packages available to financial planners, whereby client data can be inputted and a “plan” is produced by a computer. In many cases, the plans run into dozens (sometimes hundreds) of pages with lots of pie charts and graphs.

I have shied away from using this approach, as I have generally found the output to be overwhelming (and, in many cases, not particularly meaningful). Thus, I have often felt that my three-page financial projections, accompanied by a two- to three-page letter, are a more effective approach for summarizing a financial strategy.

As the financial planning world becomes more complex, however, I have decided to expand the template that I use for communicating recommendations to clients and to adopt the strategy of having a single “plan” for each client who would like me to prepare such a document on their behalf.

**Components of a Financial Plan.** My intention is to prepare (for each client who requests

that I do so) a document which will contain the following information:

- An introduction
- A checklist of items being covered in the plan (and, similarly, a checklist of items that are not covered or are to be covered at a later date)
- A long-term financial projection (this is no different than my current approach, although I have rewritten the software that I use for preparing projections to make it more comprehensive)
- A recommended investment strategy that includes a target asset allocation and an “investment policy statement” (an investment policy statement or “IPS” is a document that formalizes the parameters under which investment decisions should be made)
- A recommended cash-flow strategy
- A series of commentaries (the equivalent of the letters that I have written in the past), which deal with such items as taxation, cash-flow strategies, etc.
- An executive summary of the points covered in “the plan”

**Additional “Modules”.** Part of my reason for adopting this new strategy, and part of the reason for starting each plan with a checklist, is to make sure that I am covering all the areas that my clients want me to cover. I also note that many clients may be unaware of the scope of the work that I and my associates are able to do. Thus, additional modules may be added to a basic plan. These additional modules would include items such as:

- *Estate planning:* An analysis of tax liabilities, arising on death, strategies for minimizing probate fees, some will planning strategies

and commentaries on the use of trusts ... (copies of wills or trust documents may be kept with the plan)

- *Advocacy:* Comments on power of attorney or representation agreements (copies of these agreements may also be kept with the plan)
- *Risk Management:* An analysis of the need for life insurance, disability insurance, or creditor protection of assets (a very big issue that is now becoming topical in our society is an analysis of the need, of lack of need, for critical illness insurance or long-term care insurance)
- *Cash Management:* A commentary on maximizing the interest earned on savings or minimizing the interest paid on debt
- *Detailed Tax Planning:* Some tax-planning issues, such as income splitting, minimizing the claw-back of old-age security, and the effective positioning of investments will tend to appear as part of my investment commentary in the “basic plan” (some clients, such as owners of corporations, will have more detailed tax planning issues to address)
- *Charitable Gifting Plans and Programs:* Strategies for meeting charitable objectives and tax strategies for maximizing the contribution of federal and provincial governments toward the charities of your choice.
- *Intergenerational Financial Planning:* Dealing with issues such as helping children or grandchildren with the establishment of educational savings plans or “in-trust” accounts
- *Other Issues:* Any other items that may be important to you

**Implementation.** I am happy to address any or all of the items noted above for each client and to formalize a comprehensive planning

document for that client. Please contact me if you would like me to start this process for you, and let me know which specific areas you would like me to address.

I should note one slight caveat at this point. I do have a fairly large number of clients and cannot prepare a comprehensive planning document for every client on a moment's notice. I shall, however, respond as promptly as I can to requests from clients (either for the preparation of the comprehensive document or to address some of the areas that I have outlined in this newsletter).

My support team is slightly understaffed due to the departure of one of my assistants (Michael Zsigmond). I am, therefore, seeking a qualified associate to assist me in the preparation of financial planning reports and the delivery of financial advice and client service.

## Summary

Here is a brief summary of the points in this edition of *Clientel*:

- The future direction of stock markets and interest rates continues to be uncertain. We must work hard at making sure that each client has the most appropriate allocation of investment assets to hedge their position for varying contingencies.
- I am contemplating the introduction of a fee-based model for managing client accounts at some point in the future, but I am making no changes at this time. Should I

introduce a fee-based model in the future, my plan would be to make it optional for any existing clients.

- I intend to make a comprehensive planning document available for all clients in which I summarize a number of strategies in a single report.

## Clientel

Thank you, again for reading this edition of *Clientel*. Please do not hesitate to contact me if I can provide you with any additional information on the subjects outlined in this issue.

Thank you, again, for our ongoing relationship.

Sincerely,

ROGERS GROUP FINANCIAL



David N. Chalmers  
Financial Advisor

P.S. For many years, I have sent "pop-up" calendars to clients early in the new year. The company that provided these is no longer doing so. Thus, 2003 will be a "non-pop-up" year. I am looking for another supplier and I hope to provide these again in 2004.

*"David N. Chalmers is a Financial Advisor with The Rogers Group Financial Advisors Ltd. The views expressed are those of the author and not necessarily those of The Rogers Group, which makes no representations as to their completeness or accuracy."*

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