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Are You Genuinely Independent and is Your Advice Entirely Objective? Jessica Cutrera of Leo Wealth Opines

Jessica Cutrera is a regular at Hubbis events and on our pages. That is not surprising, as she offers a wealth of expertise and a robust historical perspective on the evolution of independent wealth management in Asia. She is the President of Leo Wealth, a global wealth management firm created in its current guise in 2021 to bring together The Capital Company (which she had co-founded in 2017), Leo Group, and BFT Financial Group in the US, thereby linking Asia and North America in terms of client connectivity, expertise and flows. She spoke to Hubbis again recently to articulate some very forthright and detailed observations on the independent wealth model and what differentiates firms from their peers and, implicitly, from the private bank competitors and other major market incumbents, such as the wealth arms of major brokering firms in the region. She believes that to be truly independent of thought and action, the wealth firm and its team must approach clients with a fiduciary mindset at all times. This is not easy, and there are plenty of challenges to overcome. But it is, she argues, more than possible if the right mindsets, business cultures, strategic approaches, wealth industry collaboration and regulation can all merge towards delivering a more truly client-centric offering.

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JESSICA CUTRERA
Leo Wealth

Jessica was a Founding Partner, Responsible Officer and Compliance Officer of The Capital Company Hong Kong Limited, which is an independent asset management firm formed in early 2017. Prior to her time at The Capital Company, Jessica co-founded EXS Capital Asia Limited in 2008 and served as a Responsible Officer and head of Operations and Compliance for the firm until the end of 2016. She and her team built a substantial asset management and financial planning practice during their time at EXS, which in 2017 became part of The Capital Company.

Jessica's expertise spans many areas of individual financial, regulatory and tax issues, particularly in relation to US citizens living in Asia. She and her team specialise in providing comprehensive wealth management and estate and tax planning services to US citizens expatriated to Asia and to individuals and families with US-related planning needs.

Are you truly independent?

She drills down beneath the surface of what makes a differentiated and independent wealth management proposition stand out. "I believe there are two fundamental aspects to genuinely embodying and demonstrating independence to clients," she states.

Firstly, she says the cornerstone of claiming independence revolves around the concept of being a fiduciary. "This is a crucial distinction, as the term 'fiduciary' implies a standard far elevated from what is commonly referred to as 'suitability', implying a far greater degree of responsibility for the client's financial well-being. It is far more than determining if a particular product suits at a moment in time, and making sure the advice given is truly in the best interest of the client. In my view, the label of independence cannot genuinely be applied unless one is acting as a fiduciary. This principle underscores a deeper commitment to the client's welfare above all else, differentiating mere suitability from a more profound, client-centric approach."

Are there conflicts of interest?

She reports that, in her view, the second critical element in achieving genuine independence involves addressing how to hire, retain, motivate, and properly incentivise individuals who make recommendations to act as genuine fiduciaries in all their engagement with clients.

"This brings us to the issue of conflicts of interest, a significant barrier to independence," she elaborates. "If your compensation models or business structures embed conflicts of interest, particularly in how recommendations are made to clients, and the linkages to income, then claiming independence is not feasible. Such conflicts directly undermine the capacity to function as a fiduciary, as they skew incentives away from prioritising the client's best interest."

She adds that conflicts of interest are pervasive in the market, deeply

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embedded within many firms' business and compensation models. While there has been some progress, with certain firms genuinely acting as fiduciaries and embodying the essence of independence, many others struggle to overcome these inherent conflicts. At the heart of this issue is product distribution. "When employees are incentivised to favour one product over another based on the compensation received- earning more for selling Fund A over Fund B, or not being compensated at all for recommending Option C - a clear conflict of interest arises," she clarifies.

Steering a careful path for the clients

This conflict of interest not only compromises the advisor's independence but also leads to a higher cost structure for the client. These additional fees are not inconsequential; they are the direct result of a compensation system that incentivises advisors based on specific product recommendations. "Given the vast array of investment products, solutions, and financial planning services available, any model that fosters such conflicts cannot claim to be truly independent," she states unequivocally.

Addressing the institutionalisation of the principle of independence, Jessica observes that transitioning towards genuine independence within financial advisories is undoubtedly challenging but entirely achievable.

Adapting mentalities and approaches

"Our global team includes advisors who have transitioned from traditional 'wire-house' or product distribution models to a fee-based approach," she reports. "This shift has empowered them to offer a superior level of service without conflicts of interest. Unlike the conventional model, where compensation is tied to product sales, these advisors earn their keep by providing solutions that best serve the client's interests, embodying the fiduciary standards I outlined earlier."

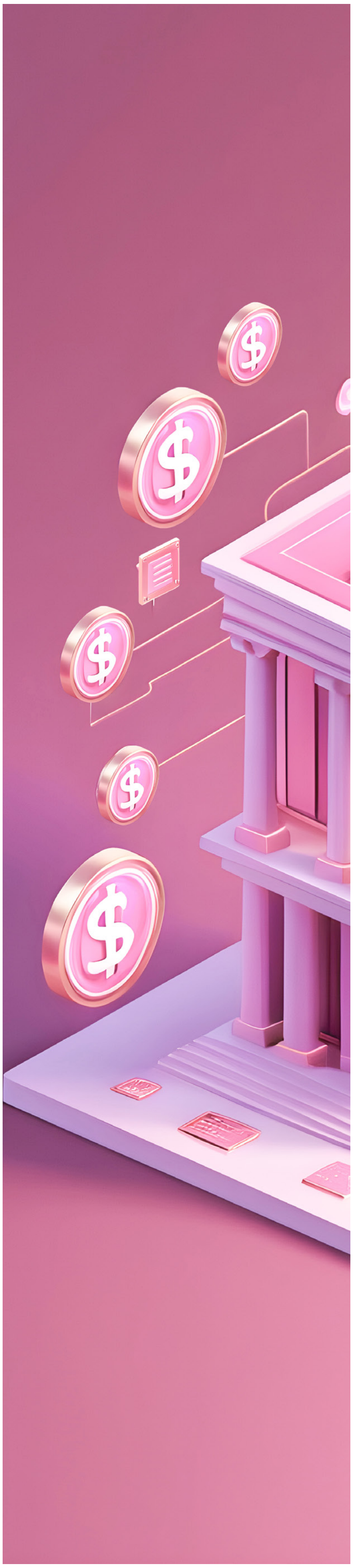
She adds that this change often offers clients a more cost-effective solution. It paves the way for a broader, more diverse range of services and investment products that are neither excessively leveraged nor carry undue risk and that are carefully handpicked as best-in-class.

Elevating understanding

"The traditional model frequently necessitates higher risk to offset steep fees and retrocessions," she elucidates. "Thus, without significant changes in the institutional framework to eliminate these embedded conflicts and move towards a model that prioritises fiduciary responsibilities, the growth of truly independent advice and services will likely remain difficult to achieve."

Addressing key questions around how new clients should approach and assess their wealth managers so that they can avail themselves of the 'fiduciary' model, if they so wish, Jessica focuses first and foremost on the future, the next and younger generations. She observes that an often overlooked yet crucial aspect of wealth management, particularly as it pertains to multi-generational planning for families, centres on the importance of educating the younger members about financial responsibility.

This includes lessons on investing, recognising and understanding conflicts of interest amongst advi-



sors, and key strategies for wealth accumulation. "We have observed that when second and third generations are well-informed about what it means to have a fiduciary duty, then when they are given unbiased investment advice, and when they are introduced to a wide array of products and services, they tend to make choices that lead to better financial outcomes," she explains. "This actually helps the whole family make better decisions and become more discerning."

The pivotal role of education

She says that educating young individuals about these topics is fundamental not just for the affluent but for families at every economic level to enhance their wealth and financial security over the long term. "Admittedly, instilling this knowledge is a long-term endeavour, and patience is required, but the benefits of such an investment in education are immense," she states. "I am a strong advocate for this approach, underscoring the need to educate not only young people but adults as well, ensuring they are aware of the various options available to them, along with an understanding of potential conflicts of interest. Good decisions make for a better future."

She notes that there are many so-called independent firms today that openly say they operate more of a product distribution business model, attributing this approach to client preferences. Indeed, she says there are still plenty of wealthy families in Asia and beyond who prefer the fee-for-play model rather than mandating their advisors for discretionary and advisory solutions or explicit fee structures.

Working with the cards you are dealt

"The reality is that fees tied to embedded product compensation, such as trailer fees or profit splits, can still result in favourable outcomes for them, but it is better by far if the advisors are not biased towards recommending one product over another due to personal gain," she states. "This comes back to adopting a fiduciary mindset - a firm can sift through and exclude non-suitable products, rate solutions based on risk, and ensure that employee compensation is not contingent on the sale of one fund over another or deriving more commission from certain products."

She concedes that this approach may not fully align with the pure fiduciary standard, but it does at least allow for serving clients who are adverse to fee-based or discretionary services with a higher-grade offerings. "Understanding and catering to this segment of the market, resistant to change, presents its own challenges, but it is a reality, and we need to work within these parameters. Even working within the constraints of the client's preferred fee-for-play model, it is possible to prioritise clients' best interests and adequately meet their needs, moving towards more transparent and equitable advisory practices."

Challenges on the road to independence

Jessica draws the discussion towards a close by commenting on the challenges and rewards of elevating the model. She says that in regions or markets where the product distribution model prevails, such as Hong Kong and Singapore, there is a tangible apprehension regarding the potential upheaval of jobs, revenue, and profitability. This concern extends to regulators, who are acutely aware of the market dynamics and the possible impacts of sweeping reforms. "Transitioning away from entrenched business practices is undoubtedly challenging, necessitating a comprehensive and considerate approach to change," she says.

She remarks that there is progress. For example, Hong Kong has exemplified progress in this area, particularly with reforms in the rules governing the sale of investment-linked insurance products, marking a significant improvement in consumer protection. "Such developments are encouraging, indicating that shifts toward more consumer-centric practices are achievable, albeit complex," she comments.

Aligning the stars

She concludes that the shift toward a fiduciary model, while daunting due to fears of client loss, diminished revenue, job cuts, and reduced profitability, is not insurmountable. "Achieving this transformation requires a balanced and fair approach that considers all market participants," Jessica observes.

"It demands a strategy that not only allows for a gradual transition but also prioritises the education and empowerment of financial professionals. This involves equipping them with the necessary skills and knowledge to adapt to and embrace these changes and fostering conversations around these shifts. Yes, there is no simple solution for navigating this transition. The path forward involves a blend of regulatory support, market adaptation, and professional development to facilitate a smooth transition towards a more completely client-centric model." ■