Will Middle Class Canadians Become “Financial Advice Orphans?”

By Greg Pollock, President & CEO of Advocis

The Canadian Securities Administrators (CSA), the association of provincial and territorial securities regulators in Canada, is considering the removal of embedded commissions in mutual funds. This would mean for consumers, they would have to pay a separate and more costly fee for the advice they receive from their financial advisors.

While a fee-based compensation model may work well for wealthier investors, this is not the case for “Main Street” Canadians, most of whom are unwilling or unable to pay higher fees.

Moving to a fee-only arrangement would put financial advice out of the reach of hundreds of thousands of middle-class individuals and families.

In Canada, over nine million people receive advice from financial advisors, with the vast majority paying for this service through trailer fees (service commission). One of the biggest benefits of this arrangement is it offers consumers affordable access to financial advice.

StatsCan reports that on average Canadians put approximately $2,600 into their RRSPs (through the purchase of mutual funds.)

Let’s look at the cost of advice on a $2,600 investment, where the trailer fee is around 1%. For $26, the investor typically receives a number of services such as:

- The development and monitoring of an investment strategy
- Portfolio rebalancing
- Proper account structure and appropriate placement in each account

- Continued understanding of the client’s objectives and risk tolerance
- Advice, reporting, meetings and ongoing management

That’s a pretty good deal. Paying a fee for the same services would cost anywhere from $150 to $350 an hour.

In my mind, banning commissions outright would solve nothing, and in fact, would harm Canadian consumers, who in the wake of a possible exodus of advisors out of the industry, would find themselves with less access to financial advice.

Those who believe Canada should ban embedded fees have not given the matter enough thought, especially if they are holding up the U.K. and Australia – two countries where similar bans have had negative effects – as two examples to follow. Recent reports tell us that the U.K. has lost 25% of its advisor distribution network, and that as much as 80% of U.K. consumers are no longer able to access financial advice.

The cost of banning embedded commissions would far outweigh any perceived benefit of consumer protection. Simply put, while those who would advocate the ban may have their hearts in the right place, they’re not seeing the full picture, which is that fewer advisors in practice means less access to financial advice. This is unacceptable, especially at a time when Canadians are struggling to manage debt while saving for retirement.

Studies tell us that consumers actually prefer to pay for their financial advice through fees that are part of their mutual funds. This is especially true among young investors with less money to invest. Giving consumers choice ensures a competitive marketplace and is the right thing to do from the perspective of the consumer.

If protecting consumers is at the heart of the matter for regulators, then why not require all advisors to adhere to a higher professional standard? This is what Advocis has been advocating for by way of our proposed Professions Model, which would require all financial advisers to be registered with an accredited body, meet and maintain proficiency standards, and be subject to disciplinary action including loss of registration for misconduct.

Studies have shown that those who receive professional financial advice are better off financially. A 2012 study from the Center for Interuniversity Research and Analysis of Organizations (CIRANO) demonstrates that people who use an advisor have two to three times more wealth, save twice as much and are better prepared for retirement.

So let’s not respond to the challenges by narrowing choice and reducing access to financial advice. That’s where banning commissions will take us, as both the U.K. and Australia are discovering.

Let’s put in place a system of oversight that will raise the professional bar while ensuring that this advice remains affordable.

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