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## Regulators Target Compensation Structures

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The current compensation model for financial industry participants\*, who promote the use of investment funds and other managed investment products for retail clients, has been mostly unchanged for over 30 years.

Regulators, led primarily by the Canadian Securities Administrators, (CSA – a national committee representing most Provincial Securities Regulators) have been studying and reviewing current compensation approaches for a few years. While few people like change, 2017 is likely the year in which the current industry compensation practice of collecting fees and commissions indirectly from consumers via fund companies may change.

The banning of "embedded commissions" is likely to become public policy, in some form or another, later this year. The final implementation and administrative rules will likely take another year or two to be finalized, but like it or not change is coming in one form or another.

While there has been a lot of debate about these compensation changes, the focus for this article will be on the **potential impact on consumers** who choose to work with an Advisor for advice and guidance in their asset building and investment management efforts.

We have been following the debate on both sides for several years. The regulators are intent on bringing down investment management costs overall for consumers while the industry has argued, based on evidence from other jurisdictions that have gone this route, that access to advice will be reduced for most Canadians under the new proposed compensation model. (This is a very simplified summary of the whole issue.)

We all intuitively understand that the wealthy and those with large [investment accounts](#) [1] of \$1 million dollars or more, can already access advice and negotiate lower fees for pure investment management. However, an estimated 5% or less of Canadians currently qualify for the services of investment counsellors or discretionary portfolio managers.

The one point that has not arisen in any of the official dialogue concerning compensation structures is the range of services currently covered by investment fees and commissions and how many Advisors and financial planners subsidize other services with the income earned on investments.

As one accountant explained many years ago, he builds in a small fee into his services pricing model to cover the cost of providing free assistance for the small percentage of his clients who annually are challenged by the CRA on some aspect of their tax returns. In effect, all his clients contribute a portion of their accounting fees for the general benefit of the few who may be in a dispute with the tax department.

Many Advisors do something similar when they provide "free" financial plans, tax advice, Estate Planning and so on at no extra charge on a consultative basis. But, with the move to change the compensation model, the financial industry will be pushed to a more cafeteria style menu approach where each service is priced individually – much like how lawyers charge for their time.

Even more concerning for the average Canadian is the increased complexity in assessing how each Advisor works, their specific [value proposition](#) [2] and how it compares, at what pricing levels, to other Advisors. Currently there are four options, no-load or fee-based, front load, low-load and full deferred sales charge or some variation on these. Under the new rules, the comparisons between Advisors will become more complex as more pricing variables come into play. These may include minimum administrative account fees, regulatory account fees, minimum revenue fees, minimum investment account sizes and price competition to win market share, etc.

The experience in other countries is that the cost of investment advice has surprisingly, gone up, and not down, as Canadian regulators presume. These pricing increases are already occurring in Canada based on anecdotal

evidence. It is also ironic that Britain is currently offering subsidies for certain people to help them pay for planning advice.

It may take 10-20 years to determine if the coming changes are "good" for consumers. There is almost no discussion amongst Regulators about helping investors get better investment returns or create more wealth for themselves and their families. The only focus is on investment costs.

Call us today to [discuss our value proposition](#) [3] in the new regulatory environment.

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