

YOUR MONEY

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Fee-based investing can save money

Getting tangible value in exchange for the fees you pay

Investors have a variety of options regarding fee structure. One of the most popular is the fee-based pricing model.

Investors in fee-based accounts pay a set percentage generally based on the size of the account. Fees can also be set by asset type, where portfolios comprised mostly of low turnover, fixed income investments are charged less than equity-based portfolios.

According to PriceMetrix, fee-based structures are the preferred method of investing for higher net worth clients and they are growing in popularity. PriceMetrix conducted analysis on 2.3 million investors with a combined \$850 billion in investment assets and found that from 2007 to 2010, fee-based account business increased by 24% while transactional assets declined by 1%. There are many reasons for the increase.

Fee-based accounts offer transparency. Everything is included in one inclusive fee, so there is no inherent conflict of interest, and investors don't worry that their advisor is recommending a specific product or action just to generate commission. Instead, the advisor is focused on achieving the client's long-range financial vision. It is an important distinction. The fee will grow with an increase in assets under management and therefore the advisor has a vested interest in increasing the client's wealth through positive portfolio performance.

Just converting to a fee-based account can generate a cost savings. Consider an investor with a \$500,000 portfolio making 25 trades per year. If the average size of the trades was \$15,000 with a 2% commission per trade, the fees would be \$7,500 per year. If that investor was instead in a fee-based account charging 1%, the fee reduction would be \$2,500 per year.

Pricing flexibility is another advantage. In most cases, advisors are given much more discretion over the pricing they set for fee-based accounts than for commission-based scenarios. For instance, advisors can make concessions for clients who have consolidated all their assets with them.

There are potential tax benefits in fee-based accounts. While brokerage fees or commissions associated with the purchase or sale of a security have tax benefits only in the year of sale, fees linked with fee-based accounts are generally deductible every year.

For some people, fee-based accounts aren't suitable. An elderly retiree whose \$500,000 portfolio is comprised mostly of cash and fixed income is not likely suited to a fee-based account, and any advisor would be hard-pressed to justify charging \$5,000 per year for managing such a low maintenance portfolio. It's more likely this person is better served by a traditional structure paying a fee per transaction.

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Fee-based accounts are most suitable for an investor with complex financial needs. Beyond investment counsel and the execution of trades, this client needs the correlation of all aspects of a complicated financial picture. This might include research and guidance on other factors such as tax efficiencies, estate planning, education and retirement planning, insurance needs and implementation strategies.

However, no matter which fee structure is best for you, there must be tangible value in exchange for the fee and your advisor should be able to articulate that value clearly.

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