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**Kim Inglis, BCom, CIM, PFP, FCSI, AIFP**

Navigating the different account fee structures

Determining the right structure for you

Investors pay fees for portfolio management, as they do for any professional service, but many are unaware of the variety of options regarding fee structure. One of the most popular is the fee-based pricing model.

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 7 million investors with a combined \$3.5 trillion in investment assets and found that from 2011 to 2014, the percentage of fee-based assets in the average advisor's book of business increased by 35%. There are many reasons for the increase.

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.

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 GICs and some bonds 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

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Continued from Page 1

maintenance portfolio. It's more likely this person is better served by a traditional structure paying a fee per transaction.

Of course there are some people who opt for a blend. According to PriceMetrix, 52% of clients that have fee-based accounts also maintain transactional accounts with their advisors.

In the end, investors must take a sober look at their portfolios and determine what's suitable for

their unique objectives. 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.

Kim Inglis, CIM, PFP, FCSI, AIFP is an Investment Advisor & Portfolio Manager. The views in this column are solely those of the author.
www.kiminglis.ca