Portfolio Management Association of Canada

Selecting Investment Counsel

Introduction

Choosing an investment advisor need not be a difficult undertaking. While it may seem challenging due to the vast array of firms and individuals offering various services and financial products, we believe we can simplify the process. This section is intended to give you a clear understanding of all the options available so that you can make an informed choice.

The Portfolio Management Association of Canada (PMAC) represents firms, registered as "portfolio manager" whose primary focus is discretionary investment management for clients. Few organizations are permitted to provide discretionary management where the portfolio managers make their own decisions in making and changing investments for clients. To be able to do so, portfolio managers meet the highest conditions of registration with the securities commissions.

Financial Services Providers and Their Products

Below you will find information that highlights the differences between the products and services offered by others and compare them with those of investment counsel. On the Understanding Your Investment Options webpage located under the Investor Centre on our website (http://www.portfoliomanagement.org/nav-investor-info/useful-links/), you will find a Due Diligence Checklist that we encourage you to use, not only for selecting an investment counsel or portfolio manager, but, if appropriate, for understanding the important details of others offering investment services. We think it will give you greater insight into the style, qualifications and compensation of advisers.

Portfolio Managers

These firms are registered with securities commissions as portfolio manager and are regulated by them. Most portfolio managers in these firms hold the coveted Chartered Financial Analyst designation and abide by a strict code of ethics. Their only business is the discretionary management of investment portfolios for individuals, estates and trusts, charitable foundations, corporations, pension funds and endowment funds. Investment counsel fees are limited, in most cases, to a percentage of the assets under management. For individuals, the tax-deductible fees generally range from 1% to 2% plus a fee for the safe custody of client assets by a separate financial institution. Investment counsel and portfolio managers also offer pooled funds to clients with smaller amounts to invest than the minimum for segregated accounts. These firms provide:

Segregated Accounts

Not to be confused with segregated funds, (see below) these are separate, custom portfolios only available from investment counsel and portfolio management firms. Care is taken by the investment counsellor to understand the investment objectives, personal circumstances and risk tolerance of each client and, with this information, a suitable portfolio of investments is constructed. Portfolio managers seek a minimum account size for segregated accounts that typically ranges from $500,000 upwards and is, most commonly, in the $500,000 to several million range.

Pooled Funds

These are similar to mutual funds in structure but require a minimum investment of $150,000 and disclosure is in the form of an information circular as opposed to a prospectus. There is no sales fee involved in buying a pooled fund and the management fee is generally in the range of 1% and is 1% to 2% less than in mutual funds. Pooled funds are generally available from investment counsel firms, portfolio managers and insurance companies.

Brokers, Investment Dealers and Securities Dealers

These are firms registered with securities commissions to trade in securities as agent or principal - they can buy or sell securities for you through other brokers or by selling from their own inventory or buying directly from you for their own account. Brokers and investment dealers are members of a stock exchange and are regulated by the Investment Industry Regulatory Organization of Canada (IIROC) (www.iiroc.ca). Securities dealers are regulated by securities commissions. All these firms are compensated by transaction commissions that are shared with salespeople.

Salespeople employed by brokers and investment dealers are registered and regulated through the Investment Industry Regulatory Organization of Canada (IIROC) and are known by various titles. Some of these are investment advisers, account executives and registered representatives but there may be others in use. Whatever they are called, it is important to know that they generally are compensated by transaction commissions. But, in some cases, certain salespeople are able to charge an annual fee for the advice and recommendations that they provide. Products available from brokers and investment dealers include:

Securities advice and execution: Brokers and investment dealers buy and sell securities and mutual funds for clients ***only on direction of the client***. Only brokers who have been conferred the CIM designation are able to provide discretionary investment management. Investment dealers also assist corporations in raising capital through new bonds or shares that they sell to clients and the public.

Wrap Accounts: In wrap accounts, typically, the broker or dealer selects an investment counsel or portfolio management firm to manage pooled funds in which clients of the broker invest and the individual salesperson provides the client with advice. These are products where the cost of advice and the management are "wrapped" into one fee. You can expect "wrap" fees to average between 2.5% and 3.7% and, if mutual funds are used in the wrap account, make certain that trailer fees are excluded from the "wrap" fee.

Financial Planners

The term "financial planner" is broadly used in Canada by a variety of financial services professionals. As a consumer, it is often difficult to wade through the myriad of information and determine what services are being provided and at what cost when seeking financial planning services. Currently anyone in the financial services sector can use the term "financial planner" to market or describe his / her skills. However, there is only one registered and governed financial planning title in Canada and that is the Certified Financial Planner Designation or the "CFP" as it is often referred to. The CFP designation is conferred and monitored by a not-for-profit organization called the Financial Planners Standards Council (FPSC) of Canada.

Certified Financial Planners have taken extensive courses and examinations to earn this professional designation and they must participate in annual continuing education programs to maintain their CFP status. Furthermore, they must ensure they operate their planning practices in accordance with the FPSC's stated ethics and guidelines. Detailed information regarding the designation, the FPSC and helpful consumer information can be found on their website: www.fpsccanada.org.The FPSC website also lists registered planners in your area and you can use this resource to confirm that a planning professional you are interested in working with is indeed a CFP designation holder in good standing.

Certified Financial Planners are compensated in a variety of ways but in essence compensation breaks down into three possible models:

Fee for Service

The planner will charge a fee for any services rendered. This fee can be calculated based upon an hourly rate or a flat fee negotiated at the time of engagement.

Fee for Service and Commission

The planner will charge a fee for the development of a financial plan and will also receive a commission (either from the consumer or from the product provider, for example, a life insurance company should life insurance be purchased) for any product purchased to assist in meeting the stated objectives of the financial plan.

Commission Only

The planner will be compensated solely by commission generated from products that are purchased to fulfill the objectives of the plan. Commission may be paid by the consumer or by the product provider.

Each of these models has its pros and cons and it is important that consumers ask when interviewing a prospective planner to ensure they fully understand how the planner will be compensated. It should also be noted that some planners provide strictly planning services. Other planners may provide planning and can also assist consumers with their investing or insurance needs.

Mutual Fund Dealers

These are firms registered as mutual fund dealers with securities commissions that employ salespeople to distribute mutual funds. Some Dealers have their own mutual fund products or products of a related firm while others are independent and sell only products of unrelated mutual fund companies. Mutual fund dealers are compensated by commissions, earned on sales to clients that they share with their salespeople. Some mutual fund dealers also charge a management fee for their advice on a portfolio of mutual funds. Mutual fund dealers are to be regulated by the Mutual Fund Dealers Association.

Salespeople employed by mutual fund dealers are also to be regulated by the Mutual Fund Dealers Association. They are largely in the business of selling mutual funds in return for commissions. These commissions include a portion of the sales charge and an ongoing "trail commission" or service fee. For a fund sold on a deferred sales charge basis, a salesperson typically earns 4% to 6% on the sale, an ongoing commission of .5% to .75% plus a portion of the sales charge (if any) levied when the client sells. Many refer to themselves as "financial planners" and you certainly should know the qualifications they really have. (See Financial Planners above) Products offered by mutual fund dealers and their salespeople include:

Mutual Funds

These are investment products where many investors pool their money with others and share in a professionally managed portfolio of securities. Mutual funds are sold under a prospectus, which is a disclosure document reviewed by a securities commission to ensure its completeness. Mutual funds charge fees and expenses to the fund and disclose this as the management expense ratio - the percentage that the total fees and expenses are of the total value of the fund. Management expense ratios of funds range between 2% and 3.5%. Mutual fund companies are members of the Investment Funds Institute of Canada.

Segregated Funds

These are similar to mutual funds except that they provide a long-term guarantee of the return of the capital invested and they are sold by insurance agents, as well as mutual fund dealers. Disclosure is in the form of an information circular as opposed to a prospectus. The fee for the guarantee is about 1% in addition to the management expense ratio which averages 3% to 4.5%.

Financial Institutions

A special note about financial institutions. Typically, financial institutions are in all of the businesses discussed above, in addition to banking services. It is important to note that each subsidiary offering specific services, and the people working in the subsidiary, must be registered and regulated to provide such services. The separate subsidiaries all must operate in the manner described above for investment counsel and portfolio managers, brokers and investment dealers and mutual fund dealers. Some wealth management divisions of financial institutions also provide financial planning services.