

Whose decision is remuneration?

Remunerating the financial adviser has been a much publicised debate both locally and globally – how financial planners earn their money has been dissected in the media and divided opinions in the industry. Money earned is most often a private matter for each individual but not so for financial advisers.

Gavin Came, director and Board member of the FIA (Financial Intermediaries Association) says that each FIA member and financial adviser in fact arranges how they earn their income according to their practice and client profile and needs. "Each member decides and arranges how their income is earned."

Came says the FIA has held the view that following the introduction of FAIS and mandatory cost disclosures, commission should not be regulated. There are many

different ways to earn income which relate to various client profiles calling for different ways to remunerate the adviser.

To illustrate he uses two examples – a practice in a small town with lower income clients and a practice focusing on high net worth clients.

In the first case, where an adviser operates in a small town with lower income clients, the average client could be in a position to set aside say R250 – R1000 a month, they perhaps require life assurance as well as saving towards retirement. These clients would most likely not be in a position to pay the kind of fee for advice as is justified by the skill and expertise of a qualified and compliant financial planner. In this case a front end commission calculated on premiums and the term of the contracted savings on life assurance products introduced would cover the remuneration, cost

of advice, compliance with legislation and FAIS. Provided the client committed to the contracted investment term and was aware of the penalties for early surrender then commission would be earned over the term. In effect, the client is sacrificing some time and money to fund the correct reward for the advice received. If on the other hand a unit trust was offered for this amount, would the as-and-when commission earned be worth the adviser's time and effort? In many cases it would not cover the cost the adviser had incurred in analysing needs, recommending investments and facilitating that investment. The result would be and often is that this client base receives very little in the way of advice supporting their investment and financial security decisions.

In the case of an adviser focusing on high net worth clients, where assets have already been built up and

the decisions are related to optimising how these assets are invested, together with the fact that in many cases these clients are shedding life cover rather than securing more cover, a fee based on say a percentage of assets under management would be a more correct remuneration model.

So the debate around fee or commission based model is often a moot one because, Came says, the truth is that most advisers are in the middle – some work for fees and some receive remuneration by way of commissions and many earn a combination of the two.

Perhaps the most salient point of the commission remuneration debate is an evaluation of the work a financial adviser does, with who they do it, and their role in the community and country. Advisers offer much needed financial advice, analyse needs, research products

and record and adhere to regulation and in the process look after the current and future wealth of their clients. In any country, but especially in South Africa this role is needed. As an adviser operating in SA we also need to look at the country's citizens and what they can and cannot afford.

SA has no typical average earner or citizen – and perhaps analysing it logically involves splitting the country into income zones as the Insurance Gap study did. So for high earners certain products, advice and payment models will be relevant and for middle and low earners a different set of products, advice and payment models will be more suited. Some advisers' clients' profile may just not make a fee only based model viable. "There is no one perfect model."

Came says his big fear is that if commission is outlawed or too heavily regu-

lated the people that need advice the most will be excluded from receiving it – and would by default purchase an off the shelf product that may not be suited to their needs.

In a recent article Almo Lubowski at the FPI noted the British experience after commissions were banned as follows:

"the ban (of commissions) will not prevent banks from selling investment products without advice. Barclays launched an online "execution-only" website in November and believes it will be a big driver of new business.

Other banks are expected to follow. The Ernst & Young report forecasts that by 2015, the majority of retail investment funds could sit on bank platforms.

Providers of investment products sold on execution-only sites will still be able to pay banks a commission for hosting their products. But independent financial advisers have warned that a growth in execution-only sales could mean that many consumers do not buy the right products."