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The Cost of a Name: Nominee accounts lower fees

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ADVISOR'S EDGE REPORT (November 2007)The joke among some MFDA dealer executives is that advisors almost need to hold signing ceremonies, akin to those needed for a real estate purchase, when opening new client accounts.

The analogy is a bit of an exaggeration, but the sentiment seems to be shared and appreciated by most of those grappling with ways to streamline orders, trades and client reporting. Some even suggest that the constant need to gather signatures for each and every step of the financial planning process perpetuates the image of MFDA dealers as second-tier service providers, relative to those operating in the IDA space.

Debates about paper and efficiency inevitably emerge when a group of dealer executives are put together in one room. At the recent Advisor Group annual dealer conference in Collingwood, this discussion turned into one examining the pros and cons of the nominee platform, typically used by IDA dealers, compared to client name accounts used by most MFDA dealers.

Admittedly, a lot of this debate is fueled by those who have a vested interest in seeing the nominee platform take off in the MFDA world. That said, more and more client name dealers are beginning to ask questions about the platform and are beginning to offer the nominee name option to advisors who are interested in providing more specialized service.

"I honestly think it's going to be a generation thing," says Worldsource Wealth Management's chief compliance officer, Bill Donegan. "Looking forward, lets say 10 years from now, I think the nominee platform will be quite pervasive."

In a client name environment, advisors help clients to open mutual fund accounts, directly with fund companies and manufacturers. If a client decides to invest in products with more than one company, the advisor, in turn, must facilitate the process - filling out forms, collecting client signatures for each and sending the paperwork on to all the right places. With nominee accounts, on the other hand, a client opens his or her account with the dealer alone. Nominee dealers can then trade, rebalance and manage assets for the client and issue one statement that reflects changes across all holdings, no matter which manufacturer's product is being used.

Richard Binnendyk, executive vice-president and vice president of client service at Univeris Corporation, says the two different platforms were likely born of necessity as mutual fund dealerships evolved. In the securities world, nominee platforms have been the de facto standard since the beginning. Fund companies had this technology and the ability to process orders, execute trades and issue all the required paperwork. The client name way of doing things allowed advisors to have relationships between investors and the fund companies.

With technological advancements, however, more dealers are able to manage contributions, cash, tax receipts and processing just as well as the larger manufacturers. What's more, the technology allows dealers to rebalance holdings and provide consolidated reporting, introduce additional products, specialty products, sophisticated services and do it all in a way that is dealer-branded, eliminating multiple fund company statements and reporting.

With this ability though, comes increased responsibility for dealers — instead of one annual statement, dealers are required to send paperwork to clients at least quarterly. Monthly statements are also required when there is activity in the client's account.

"This was imposed on us. That kind of regulation was established in a day when the internet and 800 numbers didn't exist," Scott Sinclair, president and chief executive officer of MRS Inc. and MRS Securities Services told the group gathered in Collingwood. "Even though clients can now see the state of their account as of the last business day we still need to send this out," he says, adding that it is perhaps an issue that needs to be addressed by advocacy groups.

The biggest issue though, outside of the fact that most MFDA advisors are comfortable and used to the client name way of doing business, seems to be that nominee accounts usually include account fees ranging anywhere between $80 and $130 annually.

For a lot of advisors, this fee, in addition to the usual fees charged by mutual fund companies, is sufficient cause to stay the course using client name accounts.

"Many clients just don't want to pay the fee that's associated with nominee," says dealer conference panelist, Scott Plaskett, senior financial planner and CEO at Ironshield Financial Planning. "I personally like the nominee environment because you can have a cash account, you have the ability to shuffle money much quicker. You don't need to use a transfer from to get from there to there, taking a few days to get it done. But it's the fee that's the real(problem)for some clients."

Proponents though say these concerns can be addressed and the benefits usually outweigh this cost. To further sweeten the argument, they also point out that nominee account assets can be more "sticky" than those invested in client name accounts.

"If I want to redeem money out of a fund or group of funds I can put it in cash, then meet with the client. In a client name world, those assets need to be paid directly to the client. The client needs to deposit the check to his bank account and cut another check back to the advisor," says Binnendyk. "Frankly, there's the opportunity for the advisor to lose that money because the client may decide to cash out and buy a big screen TV instead."

For dealers, meanwhile, in addition to branding and service opportunities, the nominee platform eliminates issues related to direct trading where advisors trade directly with fund companies. Although the trades should get reported back to the dealer for compliance purposes, such trades can be harder for the dealer to control. Those executed through the dealer system, though, can be stopped on the spot if compliance notices any issues. In cases of direct trading, if compliance departments need to step in, such action usually occurs after the fact.

At the same time, many fund companies have moved to offer fixed MERs, which could make them more cost sensitive and inclined to promote systems or encourage habits that result in less paper being shuttled between companies.

Although Sinclair is usually the first person in the room to admit that he's not objective about the situation — the MRS platform processes 100% of its business using nominee accounts, he says nominee business is subsidizing client name business in the form of MERs. If a dealer is processing the trades and taking care of the paperwork, the fund company expenses for nominee name business rings in around 10-15 basis points, whereas the cost on a group RSP in client name is around 60 basis points.

"You end up with a weighted average. Those weighted averages are coming in around 25-30 basis points," he says. "The fund companies were happy to take your paper because it had no impact on the bottom line. But with the move to fixed MERs, the fund companies are going to care about the paper coming in and client name costing three times as much as nominee name to service."

That said, it is unlikely firms will be telling anyone that they can't transact business using the platform of their choosing. Even Sinclair agrees that it doesn't make sense for fund companies to "shoot themselves in the foot" over the few basis points it costs to process client name accounts.

"People are people and we have to respect that," says Donegan. "If the advisor wants their business model to be around a client name platform because that's what they're comfortable with, that's how their operations work, that's fine. We'll respect that."

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