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# How the financial industry profits from bafflegab (at their clients' expense)

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*Financial literacy month is a good time to flag banking and investment practices that exploit people's ignorance*

November is financial hypocrisy month.

Officially, it's financial literacy month. But banks and the investment industry are avidly participating in this initiative, and that's a problem. On one hand, these companies are supporting programs that undoubtedly promote more rational spending and saving habits. On the other, they're profiting by selling products that exploit people's ignorance. Let's look at some examples:

**Mortgages:** The financially literate mortgage customer compares rates and the fine print on matters such as getting out of the loan before maturity. Banks devour people who don't pay attention to mortgage breakage fees by charging much larger penalties than many alternative lenders. These bank penalties have been a top source of complaints to this column in 2014.

**Credit-card balance transfer offers:** Here's the deal – you transfer the unpaid balance on your credit card over to another bank and you get a fabulous but temporary rate of something like 0.99 per cent.

You certainly benefit from the lower rate because standard credit-card interest rates are close to 20 per cent. But the balance transfer does more harm than good by fostering the idea that with some clever finagling, you can carry a card balance just fine. Banks don't offer those low rates as a helping hand. They know people will still have a balance once the low introductory rate ends.

**Credit-card convenience cheques:** Write a cheque to someone and the money comes from your credit card as a cash advance. There could not be a stupider way to pay for anything because up to 23 per cent interest is charged starting the day your cheque is processed. As long as you pay your balance in full in any given month, credit cards offer an interest-free grace period of at least 21 days on regular purchases. The federal government banned banks from sending unsolicited credit-card convenience cheques to clients, but you'll still find sales pitches for this product in bank mailings.

**Mortgage life insurance:** Banks are hyperaggressive in selling this junk product, and some mortgage brokers are getting into the act. Buying insurance to pay off your mortgage if you die is a great thing to do for your family. Just buy it from an insurance company with competitive rates on term life policies. The coverage will most likely be cheaper than a bank-sold policy, and you pick the beneficiary. If you buy coverage from a bank, it gets the money should you die unexpectedly and your family has no say in how it's used.

**Mutual fund trailing commissions:** Buried in the fee that investors pay to own most mutual funds is a trailing commission that is distributed by fund companies to the advisers and firms that sell their products. Trailing commissions are one of the biggest contributors to financial illiteracy because they lead people to believe that financial advice is free. Advice is not free, nor should it be. In hiding the cost, the fund industry and its adviser sales force prevent us from having a financially literate conversation about how much advice should cost, and what advisory fees should buy you in terms of service and financial planning.

**Hidden advice fees:** Advisers who aren't paid by trailers offer fee-based accounts, where investors pay roughly 1 to 2 per cent of the assets in their account per year. But just try and find out what a firm's actual fees are. Almost no one in the advisory world posts fees online, which means there's no easy way to compare costs from adviser to adviser or firm to firm. Financial literacy suffers when access to key information like price is restricted.

**Index-linked GICs:** A basic rule of investing is that low risk means low returns. Banks know people don't want to hear that, so they sell index-linked guaranteed investment certificates by highlighting the potential for stock market returns with GIC safety. The typical return with these GICs is well below what a basic diversified portfolio of stocks and bonds can achieve over the long term. That's how financially literate people invest.

**Prospectuses:** Before stocks, exchange-traded funds and closed-end funds are issued, a prospectus must be filed with regulators. Prospectuses cover all pertinent details about an investment, but in an in-your-face legalese that refuses to clearly and prominently answer basic investor questions. The mutual fund industry's disclosure documents are, by comparison, very good. In the interests of financial literacy, the rest of the investment industry should be held to the same standard.