OSC warns of pooled RESP risks

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Fees, sales incentives and 'aggressive marketing' draw fire

The Ontario Securities Commission warned investors yesterday about pooled scholarship Registered Education Savings Plans, issuing a brochure saying their risks are too easily misunderstood.

Group scholarship plans, some created in the early 1960s, account for 55% of the $7-billion Canadians have invested in RESPs. The plans, which are often advertised at doctors' and dentists' offices, took off in 1998 after the federal government offered parents the enticement of a Canada Education Savings Grant, or CESG, equivalent to 20% of an annual contribution.

Terri Williams, the OSC's manager of investor education, says the commission targeted the group scholarship plans because it received 120 complaints about them in the past two years.

The OSC is worried about the costs and cancellation policies of group RESPs and the industry's sales practices. A section in the brochure on "RESP tips" says, "Don't fall victim to aggressive marketing techniques." Another tip warns investors not to invest in RESPs if they don't understand the product.

Scholarship plan RESPS have come under fire for such tactics as offering sales incentives -- such as free trips -- to sales people who sell certain minimum quantities of product. Such practices are no longer permitted in the mutual fund industry, but scholarship plan dealers are not subject to mutual fund sales rules.

In its brochure, the commission also criticizes the myriad of costs and fees of the group scholarship RESPs. These include enrollment fees, administration and management fees, sales incentive fees, trustee fees, adviser fees, custodian fees and "transaction costs such as commissions on the purchase of securities .... Fees are paid up front from your contributions -- you don't earn any interest on your investment until the scholarship trust company gets paid."

Ms. Williams said the upfront fees charged on group RESPs "can be exorbitant."

Paul Renaud, co chair of the RESP Dealers Association of Canada, argued that the OSC overstates the number of fees because it gathered different names for the same fees from different firms and listed them all. He says the brochure contains other "factual inaccuracies" and that the RESP industry was not consulted in its creation. It wants the commission to withdraw the brochure until it is corrected.

Rival pooled RESP executive Peter Lewis, vice-president of Canadian Scholarship Trust, said the brochure is "largely accurate" but "fails to describe features of group plans which counterbalance what they view as pitfalls."

The OSC reminded investors they must be given a prospectus after purchasing group RESPs and that if they change their minds after reading it, they have 60 days to cancel. This cooling off period is much longer than for mutual funds or self-directed RESPs.

But Mr. Renaud insisted the OSC should not be making a distinction between pooled individual (or family) scholarship plans and the pooled group plans. "They are actually the same plans -- just different options with the same plans."

The brochure also attacks the limited flexibility of pooled RESPs: "Pooled group plans are riskier than pooled individual plans because you have less flexibility in the way you make your payments and there is a greater danger of losing your earnings if something goes wrong. This is the only type of RESP where such a danger exists."

Mr. Renaud said the section on forfeited earnings when plans are terminated or a child does not go on to secondary education are inaccurate.

Consumers also need to realize what happens if they miss payments, terminate plans or try to transfer RESPs between beneficiaries.

The OSC warns that if payments to pooled group plans are missed, "your account goes into default and you may lose your plan membership or "you will have to pay interest on the missed payment."