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Shifting Your Compensation Model

Making the Most of Your Planning Expertise

For most of its history, the financial services industry has been focused on sales and dominated by individual transactions. However, in recent years the industry started shifting toward financial planning and fiduciary investment management.

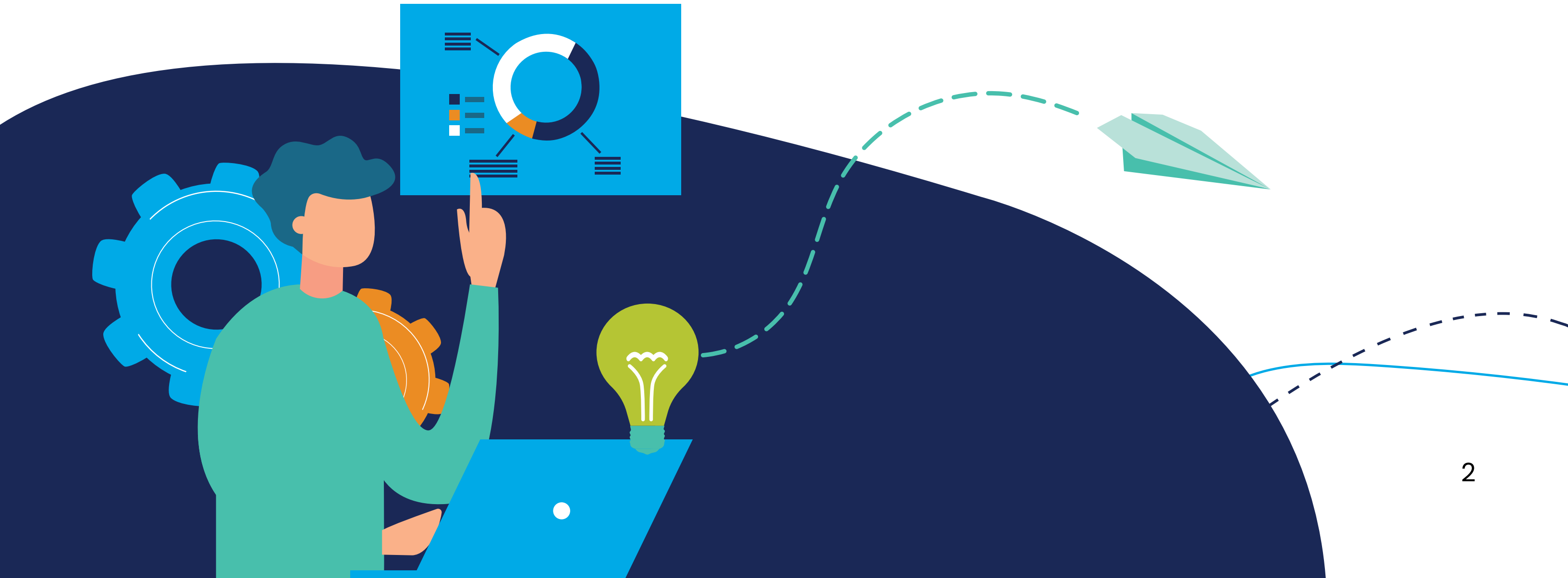
Even though many financial professionals are charging for planning services, it's common for them to find the bulk of their profits come from just a few clients, while all the rest are unprofitable. This is particularly true for those using the popular AUM fee model. Similarly, those charging AUM fees are often finding that reaching middle-income households with planning is exceedingly difficult—many simply don't have the assets to justify a one perfect fee.

At the same time, the industry is experiencing fee compression due to a race to the bottom in which investment companies are attempting to undercut the competition's prices by lowering—or even eliminating—fees for some services.

Throw in the desire for transparency in pricing preferred by younger investors and you have fertile ground for needed change.

What can be done to remedy this misalignment between the value being delivered, what's being charged, and those being served? This question has led many financial professionals to wonder what a different compensation model would look like for their business.

This eBook explores what firms should consider when looking at alternative compensation strategies.



A Change for the Better

As Baby Boomers begin retiring, the next generations of financial planning clients are looking for a different type of advice from financial professionals—the type of advice they may not be accustomed to giving.

According to our research[1], young investors want a financial plan that balances the transactional and emotional dimensions of their lives to build a roadmap that not only leads them in the right direction monetarily but addresses their needs holistically:

- **Life-stage planning:** Effectively preparing the client for major life events such as funding a college education, buying a house, or growing their family.
- **Values-based planning:** Allowing the client's belief system to shape and contextualize their financial milestones.
- **Total well-being:** Threading the needle to produce a wealth management strategy that fosters long-term health and well-being.

A focus on these "softer" sides of planning can help financial professionals grow their client base while differentiating their practice.

Eric Dahm, Lead Advisor and Partner at Range Financial Group, believes that taking a holistic approach to advice sets their business up for success now and in the future. **"You're going to need a holistic set of services to stand out in the future," Eric said. "At Range, we're not going to be commoditized. We're not going to be one of a hundred places where you can find money management. Our relationships set us apart."**

Real-world Application: Delivering and Scaling High-touch, Holistic Financial Planning with eMoney

Clients stand to see better outcomes than ever before with a holistic approach to advice. However, this approach requires special attention to ensuring financial professionals are being appropriately compensated for the expanded planning services they are providing.

The Importance of Planning

As investment firms compete to gain new clients, differentiation through financial planning increases in importance. And as that differentiation becomes a larger component of the planning services you provide, building your compensation strategy around portfolio performance becomes a less effective way to charge for the value you deliver.

For investors, transparency is the most important trait when looking for guidance with financial planning.[2] Forty-eight percent of financial professionals say they are being asked for more transparency around the services they are providing for their fees.[3]

Additionally, investors are looking to their financial planners for help in achieving not only their financial goals, but their overall life goals, ambitions, and dreams. Even though this is the case, many financial professionals continue to assign the value of the work they do to portfolio management rather than financial planning.[2]

Being able to offer broad financial planning services fosters client confidence, long-term relationships, and loyalty. But advice is challenging to accurately value and price. There are aspects of financial planning that are conceptually abstract and it's important to show clients your ideas in black and white.

Davin Carey of Carey & Hanna Tax & Wealth, and Regional Vice President, Avantax Planning Partners, believes that even if clients can't put a name to this type of service, it's what they're expecting from advisors today. **"I think when clients come to someone for advice about their future retirement investments, they kind of expect you're building a full picture behind the scenes."**

Real-world Application: How Expanding from Tax Planning to Holistic Planning Led to 3,000% Growth

So, when a firm's compensation strategy is based on investment management, this shift in services warrants a look at adjusting that strategy. Further complicating this is the rise of robo-advisors and intense digital competition which are causing fee compression in the industry. So much so that a recent report from BCG shows that margins on investment management may be cut in half.[4]

In the face of fee compression, Abbey Henderson of Abaris Financial Group combines the emotional and psychological elements of life planning with the data-driven aspects of wealth management to deliver value to clients in new ways.

> **"I realized I wanted more tools in the toolkit. Adding coaching and life planning makes client relationships more sticky. And I personally think it just makes you a better planner."**
>
> **— Abbey Henderson, Abaris Financial Group**

Real-world Application: Where Life Planning, Behavioral Finance, and Data-based Wealth Management Meet

When your firm leads with planning and you begin serving your clients holistically, new revenue streams open up that could lead to a move to a retainer or fee-based pricing model. Why base your compensation strategy on a model that's not central to the services you are providing?

Engaging with Millennials

Millennials are projected to comprise 75 percent of the global workforce by 2025[5]. The oldest part of this generation is nearing their peak earning years and they are drastically underserved in the financial services industry.

To engage Millennials and the opportunity they represent, firms still using the AUM pricing model must come up with alternative methods of pricing financial planning as the AUM model doesn't work well for those who don't have $100,000 or more to invest.

Additionally, connecting with Millennials requires a whole new playbook for engagement. Financial professionals successfully working with this generation are using the latest financial wellness technology, aligning themselves with trusted sources of advice, and committing to an educational experience for prospects and clients. And because this generation values transparency throughout the entire financial planning process, as financial professionals they are also redesigning the way they price and deliver planning services with 62 percent of millennial advisors using a fee-for-service planning model in their own practices[6].

When it comes to the services younger generations are looking for—and willing to pay for—from financial professionals, the list expands well beyond the expectations of Gen X and Baby Boomers. These generations are highly likely to pay for services targeting those just starting out in their financial journey and for services adjacent to the traditional role of the advisor including[1]:

Millennials Will Pay for Non-traditional Services

A straightforward pricing model that supports personal budgeting and allows for assigning fees to the above services is particularly appealing to this demographic.

In fact, simplicity is one of the best policies when it comes to pricing for financial planning, and it's quickly taking hold in the industry for those attempting to connect with younger clients who are accustomed to simple and predictable pricing in everything—wealth management included.

A Break from Tradition

The AUM model is far and away the most popular method of charging for wealth management services and has replaced product commissions as the way firms generate revenue. Both pricing methods essentially include financial planning as an add-on with no additional fees attached.

The rise in holistic financial planning is changing this and financial professionals are looking for ways to charge for the true value they deliver, thereby covering the technology investments and increased staffing and service needs incurred as clients demand more. The rising equity market has resulted in greater revenue in recent years, but this will not cover these costs indefinitely, especially if there is a prolonged market downturn.

As these changes continue, the AUM fee becomes less applicable to planning-led relationships. **Firms that can offer more straightforward, transparent fees for planning have a much stronger value proposition in the eyes of clients.**

Bill Simonet, Managing Principal of Simonet Financial Group, has seen these trends play out at his firm. **"The planning fee lets you lead with financial planning, which is a far better value proposition than investment management alone. It's easier to differentiate yourself as a planner," said Simonet. "The fee also more directly ties the value you deliver to the price being paid. It draws a clear and important connection between the two for prospective clients, whereas the AUM fee can cause confusion or fail to convey the true value of planning. Since finding the right fee for my planning services, my closing rates have skyrocketed, I've spent far less time prospecting, and I'm bringing on three to four new planning clients every month as a one advisor shop."**

Real-world Application: Growing My Firm with Fee-based Financial Planning

In addition to these market forces, only about seven percent of U.S. households have enough liquid assets to invest in an account to be transferred to an advisor.[7] As noted, this results in the exclusion of younger generations who don't yet have the assets to warrant this type of pricing.

But younger generations notwithstanding, fee transparency would benefit all groups of investors—not just those who are starting their financial planning journey. As of the second quarter of 2020, 22 percent of investors indicated they were unsure how they pay for advice, and 23 percent believed that the financial advice they received was free.[8]

Research shows that these numbers are improving. Investors are becoming more aware of their financial professional's compensation models and 56 percent are willing to pay for advice[8]—no matter their generation. Evidence also suggests that when clients are dissatisfied with the fees they are paying, it's often because the value of the work was not effectively communicated.

Pricing models based on assets continue to dominate in the wealth management industry. However, planning-oriented advisors should be cognizant of the disconnect this creates between how they position their value and how they charge clients.

Alternative fee structures can help with this, and at the same time, allow financial professionals to profitably expand their reach into historically underserved client segments. Introducing service and pricing models that align the complexity of the client's needs with the fees they are charged improves transparency, makes planning accessible for the masses, and prepares firms for the next generation of clients.

Keep Learning: The Business Opportunities with Alternative Financial Planning Fees

Top Compensation Strategies

No matter where you are in the process of investigating alternative pricing models, it's worth looking at those that rise to the top of current usage[8].

COMPENSATION STRATEGY	DESCRIPTION	ADOPTION	FAVORABILITY
Assets Under Management	Fee derived by charging a percentage of the assets under management	2020—70% 2022E—74%	Accepted practice
Commission Based	Fee charged on the instrument purchased/sold	2020—24.6% 2022E—17.7%	Tradition
Plan Flat Fee	Fixed fee per service (or set of services) provided	2020—2.6% 2022E—3.5%	Very transparent
Annual or Retainer Fee	Fixed annual fee is charged to provide a predetermined list of services throughout the year	2020—1.4% 2022E—2.1%	Consistency of revenue
Hourly Fees	Charging an hourly rate based on the amount of time spent dispensing services	2020—0.5% 2022E—0.7%	Client familiarity (consultants)
Other (such as Subscription)	Recurring fee for continued access to services, information, and support	2020—1.4% 2022E—1.9%	Client familiarity (streaming services)

Sample Fee Models

Flat Fee Model Based on Complexity

	LEVEL OF COMPLEXITY				
	VERY HIGH	HIGH	MEDIUM	MEDIUM-LOW	LOW
FEE RANGES	$15,000–$25,000	$7,000–$11,000	$4,500–$6,000	$2,000– $3,500	$500–$1,200
SAMPLE PLAN SERVICES					
Business Planning	●				
Executive Compensation	●				
Estate Planning	●	●			
Stock Options	●	●			
Tax Planning	●	●			
Retirement Distribution	●	●	●		
Long-Term Care	●	●	●		
Asset Location	●	●	●		
Social Security	●	●	●	●	
Disability	●	●	●	●	
Retirement Accumulation	●	●	●	●	●
Investments (including employer 401k)	●	●	●	●	●
Education Funding	●	●	●	●	●
Employer Benefits	●	●	●	●	●
Life Insurance	●	●	●	●	●
Debt Management	●	●	●	●	●
Cash Flow	●	●	●	●	●

Subscription-based Model

	SERVICE LEVEL		
	GOLD	SILVER	BRONZE
Client Meetings Per Year (at least 1 in-person, others may be a call or virtual)	4	2	0.5
Client Education and Appreciation Events	2	1	0
Educational Newsletter	12	6	4
Services	Comprehensive Financial Plan, Reviewed Annually	Retirement Plan, Reviewed Annually	Needs Analysis Module
Access	Access to financial planning portal, financial aggregation, and storage	Access to financial planning portal, financial aggregation, and storage	Access to financial planning portal, financial aggregation, and storage
Fee	$99/month	$49/month	$29/month

Keep Learning: Pros and Cons of Popular Financial Planning Fees

The Mechanics of Shifting Strategies

One of the first things to consider if you are thinking of changing your compensation strategy is to determine how and what to charge.

Take the time to figure out the cost of the services you are providing to your clients. It can be done simply by assigning costs to your client-facing staff, adding the costs of your administrative, operations, and investment management staff plus the costs of running your office (rent, utilities, etc.). Divide this by the number of clients you have.

Here's a simple example:

If you want to gross $150,000 of planning revenue, you could allocate 1,000 billable hours (about 20 hours per week) to planning activity (in addition to marketing, servicing, etc.)

$150,000 / 1,000 hours = $150 per hour. Your planning time is worth $150 per hour.

If the financial plan is going to take you 10 hours, then you should charge at least $1,500. If it's going to be more like 30 hours, $4,500 would be your minimum fee.

You may discover by doing this exercise that the proverbial 80/20 rule applies—your firm's profits are being generated by 20 percent of your clients. Which means 80 percent of your clients may fall in the unprofitable category. In fact, some of the heaviest lifting you do—for less wealthy clients who demand more of your time—may be for clients who are not profitable.

So, what do you do if you make this discovery? It certainly doesn't feel right to work with so many clients at a loss or to have some clients pay more and receive the same services as those who are paying less. It may be time to test out some alternative pricing strategies.

Keep Learning: How to Price Your Financial Planning Services

A Client-centric Approach to Fee Structure

With so many fee models available from which to choose, one way to determine what's best for your practice is to take a client-first approach. If you specialize in a particular type of client or niche market, there may be an ideal model for that client base.

If differentiation by client base has been a way to set your business apart from the pack, use the work you have already done to assist with this important pricing decision. Understanding the financial nuances of your niche clientele will guide your fee strategy.

Are they high earners with a great deal of student loan debt and few investible assets, like doctors? If they are coming to you for advice that doesn't cause a conflict between paying down debt and saving for retirement, they might best be served by paying a fee based on net worth or by a flat fee structure.

Do they work in the military or government where their pay is tied to grade levels? You could also adopt a tiered monthly fee schedule that is tied to pay grades and thus increases as they rise through the ranks.

Allowing your client niche to flow into how you structure your fees is yet another way to demonstrate to those clients that you understand them and their financial planning needs.

Tips on Implementation and Transition

Even if you aren't ready to make the change, thinking through how you would do so will go a long way toward helping you make the decision. No matter what model you choose, telling your clients about the change is an essential rollout step. The good news is clients tend to stay with someone they have developed a relationship with. If you've been providing them with value, the chances are they will continue to trust that you are working in their best interests.

One of the first things you should do is prepare a list of the services you'll be providing the client on an ongoing basis. Actually sit down and write them out. Perhaps set the list up against a client service calendar so they can see all the times throughout the year you will be working with them on their plan and investments. This exercise can also help you set up scalable, repeatable processes and allows you to articulate your value proposition and explain your fees—no matter what pricing strategy you use.

When it comes time to notify clients, an in-person conversation is recommended. Use your clients' annual review meeting to provide notice of the change. You'll be able to gauge their reaction, as well as answer immediate questions.

Use a direct approach to explain that the way you've been charging them is less valuable than the way you want to do it going forward. Keep in mind that the conversation will differ depending on the fee model you intend to adopt. If you are moving from commission fees to AUM, the conversation starter sounds something like this:

"We're in the process of making some changes to our business model. You have been a great client and we want to work with others just like you. We're going to be charging an ongoing X fee so let's review the list of services we'll be providing on an ongoing basis."

Another approach is to use stories to illustrate the change to the client. Say something like, "As we've been working together, we have been focusing on the method of transportation—or the product—and not the destination you are striving to reach. There could be some things you're missing out on, and I want to be sure I'm clear on where you want to go."

If you have been working closely with them for some time, you should know what will resonate with them. Of course, grandfathering fees for existing clients is an option, but remember that your goal is to ensure you are being fairly compensated for the planning services you are providing. Clients who truly see value in your advice will understand the change. And if they don't, remember it's okay if they decide to move on.

> **"I added a retainer-based pricing model about four years ago that I operate alongside my traditional AUM-based fee business. It gave me a way to work with non-traditional clients who have high net worth but whose money is tied up in their 401(k) or their business—so they wouldn't necessarily qualify for an AUM-based fee structure. Using this model, I have brought in more clients with more money to advise than I had been before."**
>
> **— Frederick Hubler, Creative Capital Wealth Management Group**

Real World Applications: How eMoney Flexibility Supports Non-traditional Clients

Research Compliance Considerations

Beyond the practical calculations needed to find the right strategy are other things that must be considered, one of the most critical of these is compliance. Depending on the change you are making, the types of services you offer, and the location of your practice, compliance requirements play a big role in how you are allowed to operate and under whose jurisdiction, including the SEC, FINRA, the states in which you operate, and the CFP® Board.

For example, some states do not allow a blended fee structure where a subscription fee and an AUM charge are utilized, and others don't allow financial professionals to charge income, net worth, or complexity-based fees. A thorough investigation into the regulatory requirements will be a necessary part of the process.

Keep Learning: 9 Compliance Considerations When Switching to Fee-based or Fee-only Financial Planning

Fee Administration Needs

Another aspect of the fee model transition that must be considered is how to calculate and charge those fees. The AUM model is very straightforward to calculate, and the methodology already exists to deduct the fees directly from investment accounts. It's also easy on clients because it happens automatically without any interaction on their part.

Other models are trickier and collecting these fees can be much more time-consuming and labor-intensive on the part of the financial firm. There are invoices to generate and manage, the collection and handling of checks, and the process needed to stay on top of clients to avoid late or missed payments. It also means clients are much more aware of the monetary outlay.

Additionally, there are regulatory considerations advisory firms must comply with that vary by location and agency. Careful research must be conducted to ensure risks are mitigated once you decide on the type of pay-per-service billing your firm will utilize.

Test a New Fee Structure

Take your new fee structure investigation a step further by testing it with unprofitable clients. Use the profitability calculations you completed to determine the fees that will bring unprofitable clients to a breakeven point. By testing this strategy with those unprofitable clients, you avoid the risk of jeopardizing your relationship with your profitable clients.

Not all the clients under the new fee structure will elect to stay and pay the higher fees, but research[9] has shown that clients are less likely to leave than advisors think they are. The most difficult part of the change will most likely be overcoming your own objections to making it.

Depending on the results of your test, you may ultimately decide to adopt a hybrid compensation model as the most profitable option. Just as all clients are not the same—with differing levels of service or wealth—the way you charge those clients for your advice may not have to be the same. It all comes down to what makes the most sense for your clients and your business.

Leveraging Technology

Providing more high-touch services to clients may seem like an insurmountable task when your time is already at a premium. Look to financial planning technology to help scale your new service offerings by supporting the workflows you incorporate into your client process.

Your clients will benefit when the software can aggregate their account information across institutions and incorporate client portals for the contextual presentation of financial data, plans, and goals, as well as from having a plan that is always up to date. While clients are reaping these benefits, you'll have the ability to generate financial plans for clients with different types of goals, help clients work on their plans by alerting them to next steps or check-in meetings, and use one customizable interface that tracks your whole book of business. Not to mention the advantages of scalability allowing you to deliver more plans to more clients more efficiently.

> **"Technology has allowed us to streamline our planning process so the time we spend with clients is focused on the actual plan and how it is going to help them achieve the future they picture rather than sitting with them looking at point in time statements and updating balances. It's one way we've been able to gain efficiencies in our model of service in an industry experiencing rising operational costs."**
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> **— Alex Mayrand, MRK Financial Solutions**

Real-world Application: Simplifying Planning and Streamlining the Process with eMoney

Conclusion

As you embark on this journey to explore your fee model options, something to remember is that there is no "right" answer. Just as service models differ from practice to practice—and even from client to client—there may not be a one size fits all solution. Figure out what feels right for your firm and your clients—what aligns with the value you provide. What types of clients do you want to continue to work with and how do you want to do it?

It's also important to understand that not all the clients are going to come with you on this transition and that's okay. Providing a high-touch, intimate relationship model is hard work, and you can only do that with so many clients. Find a model that lets you have this type of practice and ensures you are compensated fairly for the work you do.

> **"eMoney is the tool that allows us to provide planning and charge an appropriate fee for the service. At the close of the financial planning experience, the question commonly asked by clients is, 'How can we continue to work together?'"**
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> **— Daniel J. Galli Principal, Daniel J. Galli & Associates**

To see how eMoney is used to scale planning services that enable profitable fee-based relationships, read this case study Adding Value and Driving Growth Through Fee-only Planning.

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