



Financial Planning

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Fee-Based Planning

To Fee or Not to Fee

This month's article by Andrew Rickard, CFP, is an excerpt from CCH's [The Financial Planner](#) issue No. 141 dated June 2009.

When Marc Lamontagne left banking to become an independent financial planner in the 1990s, he said he felt there was something wrong with the way he and most other advisors were paid.

He struggled for two years at a mutual fund dealer, and came to the conclusion that the commission model didn't adequately compensate financial planners for giving clients the services they actually wanted. A client might need tax advice, help understanding his or her company's pension plan, or estate planning advice, but unless there was an opportunity for the advisor to sell a financial product, he or she wouldn't make any money.

"There's nothing wrong with selling products, but the compensation model was backward", commented Lamontagne. "I didn't like spending ten hours producing a 'free' financial plan for small assets that wouldn't compensate me for the work I did. I wanted a business instead of a job."

More than a decade later, Lamontagne has built a successful fee-based financial planning business in Ottawa. He's written a book on the subject, *To Fee or Not to Fee*, and is now helping other advisors make the switch. At a three-day seminar in Toronto in late May, Lamontagne shared his expertise with a number of planners who are considering incorporating fees into their business.

Pros and Cons

For advisors, one of the key advantages to relying on fees, rather than commissions, is that existing clients become more profitable, and there is less of a need to be constantly searching for new business. Lamontagne points out that there is another good reason for advisors who are nearing the end of their careers to make the switch to fee-based planning—when it's time to sell, fee-based books of business often command nearly twice the price of commission-based practices. This is because of the reliable stream of income they generate.

That's not to say that fee-based planning is without difficulties. Financial planners obviously need to keep demonstrating their value to clients in order to justify their ongoing fees, and there is a higher level of fiduciary responsibility as well as a higher amount of administrative work. Because they are paying out of pocket, rather than through a third party, clients may also be more demanding. And if a financial planner is charging a fee based on assets under management, it's possible that smaller clients will no longer be profitable.

Tiered and Bundled Services

Financial planners ultimately have to take a look at their clientele and their target markets. Clients must determine what services they want, and then decide if they are able and willing to pay for advice directly. Lamontagne recommends advisors create a bundled service that includes the three most common services their clients use. This might be, for example, a combination of financial planning, tax preparation, and investment management.

Once advisors have settled on their bundle of services, they can then customize the offering into tiered levels of service. Lamontagne points to the service matrix designed by Brett Davidson, founder of *FP Advance*, a British business consultancy firm, as an example.

A client paying for the "platinum" level of service each year would receive quarterly reviews, access to an investment counsellor, and tax returns for the entire household, while the "gold" service level would include yearly semi-annual reviews, a fee-based investment account, and tax return preparation for the individual client. At the "silver" level, the client would be entitled to an annual review, a wrap account, and tax returns would be billed at an additional cost.

How Much To Charge and How To Charge It

Financial planning fees can be calculated hourly, set as a flat rate, or based on a percentage of assets under management. Lamontagne says it doesn't have to be an all or nothing decision. Many advisors use a mix of fees, depending on the needs of their clients, charging a flat rate for financial planning services and a percentage of assets for investment management.

In his practice Lamontagne has always offered hourly fees, but they represent less than 5% of his annual earnings. He notes that in his own 2008 survey of Canadian fee advisors, only 2.9% billed less than \$100 per hour, while 20.6% charged \$201 to \$250 an hour, and 26.5% charged more than \$250.

"Hourly fees work well with lower to middle income clients, do-it-yourselfers, and one-off clients", said Lamontagne. But he adds that hourly billing often has both the advisor and the client looking at their watches. "Financial planning is a process, and that process takes time. That is why I use it only when flat fee and fee-based don't make sense."

Flat fees, on the other hand, work well with ongoing and bundled planning services. The advisor can work backwards, estimating the number of hours a task will require, and then add together the times in order to come up with an appropriate fixed price.

Lamontagne says that flat fees can reduce clients' stress levels, since they don't feel rushed or pressured to buy something from the advisor. He says that \$1,000 to \$1,500 is a reasonable fee for the preparation of a financial plan, although high net worth clients with more complicated situations may be prepared to pay up to \$2,500. Generally speaking, he recommends that advisors who are not sure of their pricing points err on the high side when setting their fees. "It's always easier to decrease your fees than to increase them", he said.

For investment planning, charging a fee that's based on assets under management is ideal because it separates compensation from transactions. While commission-based advisors will make less money if they recommend a G.I.C. instead of an equity mutual fund, a fee-based advisor will be paid the same amount no matter what he or she recommends.

"It removes any conflict of interest regarding one product over another and it is very transparent to the client", said Lamontagne, who noted that it also provides advisors with a steady source of income. "This is the revenue that is going to give you an average raise of 6% to 8% almost every year based solely on the increase of your clients' portfolios."

The most common fee investment advice is 1% of assets under management, although advisors will usually charge on a sliding scale, since it may take more effort to manage \$5 million than \$1 million, although it doesn't take four times as much work.

Getting Paid

Lamontagne says one of the easiest and most favoured methods of collecting payment is to use a fee-based investment account. The securities dealer that holds the account will collect the fee directly from assets under management, or take it directly from the client's bank account.

In situations where there are no investments under management, the financial planner can obtain a credit and debit machine, send invoices, use PayPal, or establish a pre-authorized debit where the client signs an agreement to pay a monthly fee. Lamontagne says that the latter results in relatively few administrative headaches. "You set up the client on negative billing, and you keep charging the fee until the client cancels your service", he said.

Much depends, however, on the regulatory regime to which the advisor belongs. Some securities dealers may not allow the use of certain fee collection methods. Because of the MFDA's dual occupation rule, mutual fund dealers, in particular, may insist that all billing be done through them—and they may take a share of the proceeds for themselves.

Making the Transition

Once advisors have decided to make the switch from commissions to fees, they need to develop a transition plan. "The same as you produce financial plans for your clients, you should produce a business plan for the transition to the fee model", said Lamontagne. He recommends that advisors set specific goals and a timeline for meeting them. For example, if an advisor is currently serving 150 households, he or she may plan to

convert two households each week over the next 75 weeks.

Where to begin? Some financial planners may want to start with their top clients, since they have the deepest relationship with them, and because they may actually generate more revenue under a fee model. Others may want to begin with the smallest accounts, since fees can turn previously unprofitable clients into profitable ones. Still others may want to begin in the middle, since that's the range the planner has designed and priced services around.

When meeting with clients for the first time to discuss the switch to fees, Lamontagne suggests advisors have a letter on hand that explains why they are making the transition, as well as a fee schedule and a new letter of engagement. Clients won't remember everything they've been told, he says, so this documentation will help to reduce misunderstandings at a later date.

"The single best influence on your transition would be to have a fee advisor in your office, someone from whom you can draw experience and guidance", concluded Lamontagne. "If you don't have access to someone like that, then consider moving offices."

Advisors interested in learning more about making the switch to fee-based planning can purchase a copy of Lamontagne's book or sign up for one of his seminars at www.tofeornottofee.com.