



To Fee or Not to Fee

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Is Timing Anything? When To Move To A Fee Model

So you've done all the research and your due diligence. You've decided it makes good sense to change your business to a fee model.

The only decision left is "Should I do it now, or is there a better time?"

The most common assumption is that you should wait until your book is large enough to make it financially worthwhile. However, this may not be the case. In our rapidly-evolving industry with stiff competition from the banks and ever-increasing demands from clients, "today" is often the best choice.

The following questions might help you with your decision about timing.

- What is your philosophy about fees?

If you've decided that a fee practice is the right thing for you to do, whether for business reasons or for a better fit with your philosophy on the delivery of financial services, then obviously you are going to be a lot happier the sooner you make the change.

In fact, a survey in 2000 by *Investment Executive* www.investmentexecutive.com found that the overriding reason advisors changed to a fee business was due to philosophical, not financial, reasons.

- Are you an "early adopter" of progressive business practices?

You may already have a successful practice, so why rock the boat by moving to fees? Because you know from a business point of view it is the right thing for you to do. So why delay the inevitable?

Even if you are just starting out, it still doesn't make any sense to wait, because waiting may be a detriment. I moved quite easily in 1996, but I had been an independent financial planner working on a commission basis for only two years and had a very small book when I made the leap. In fact, in a report on the transition to fees by Cerulli Associates www.cerulli.com, they advise that "shying away from fees will put young rookie advisors at a long-term competitive disadvantage and ultimately hamper their attempts to solicit more affluent clients".

- Do you have at least five years before retirement?

There is typically an initial drop in income during the transition period to fees because of the loss of commissions. The benefit, though, is that your ongoing fee revenues usually grow at a faster pace than projected commission revenues.

There is good data to suggest the transition may take up to three years, but it could take even longer to get the full value of your practice up to where it was before. So, if you have less than five years before you plan to sell your practice, it just doesn't make sense to change.

On the flip side, if I were buying a practice, I would be very leery if the clients had just been moved to fees. You never know if they were getting full value for their money or were just waiting for an excuse (i.e. the introduction of a new advisor) to bolt.

- Are you financially stable?

You have to be in a financial position to sustain a temporary decrease in income. To sustain your practice during the transition period, you can decrease business and personal expenses, use savings to sustain you (i.e. plan ahead), draw on a line of credit, or take out a loan.

John Page, CFP, R.F.P. of the Wealth Enhancement Academy, in his "5 Keys to Introducing Fees" webinar www.wealthenhancement.ca, suggests looking to your broker/dealer. Some broker/dealers have a budget to help transition reps moving from another broker/dealer. If you have a solid business plan to show how you are going to make more money in the long run based on the move to fees and, hence, they will make more on their override, why would they not consider helping you? It may be a long-shot, but what is the worst they can say?

- Do you want to segment your book?

The 80/20 rule says you are receiving 80% of your revenue from 20% of your clients. Companies that want you to buy into their 80/20 practice management system might tell you to fire the 80% and focus on servicing and replicating the 20%. Makes sense if you have a large client base to work with, except some advisors may lack the number of large clients needed to support this strategy.

As an alternative, Doug Nelson, CFP, CLU a practicing fee-based advisor and presenter for the Knowledge Bureau www.knowledgebureau.com, suggests focusing on client profitability instead of just revenue: "by focusing on profitability by client you can ensure that each client pays you the right amount of income for the services they receive. Today, many of your largest clients are over paying you while your smallest clients are significantly underpaying you. One option is to

switch to F-class mutual funds and then charge the client a fee based on your actual service.

What you will find is that your total profitability will increase 20% to 40% because the vast majority of your clients are underpaying for your service and your value”.

- Do you want to focus more on servicing existing clients and less on acquiring new ones?

You may have moved beyond the growth stage of your practice and want to focus on maintaining your existing clients. Since you will no longer have the large initial commissions from the acquisition of new clients, you need to develop profitable relationships with your current clients by providing more valuable, more comprehensive, or more in-depth services for those who want them.

- Are you prospecting for the HNW client?

Slowly but surely the net worth of your prospects are steadily increasing. You would like to solicit more HNW clients, but you may also have reached a plateau.

The Emerging Affluent and HNW client is attracted to lower-cost products such as F-class mutual fund shares and Exchange Traded Funds. Naturally, they are also attracted to fee-for-service arrangements with their advisors, who can also offer a high degree of service.

No matter what stage your practice is at, you always need to look ahead to where you want to be. The fee decision-making process is the same as when you decided to get your insurance licence to complement your investment licence or move from an MFDA to an IDA or ICPM platform.

If you know where you want your business to go, the only question left in your mind should be “Am I committed to making the transition to fees today?”

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