

# INVESTMENTS & WEALTH MONITOR

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## It's Not Just Assets Under Management Anymore: How and Why Advisor Fee Models Are Changing

*By Christine Gaze, CFP®, CIMA®*



**INVESTMENTS & WEALTH INSTITUTE®**

# It's Not Just Assets Under Management Anymore

## HOW AND WHY ADVISOR FEE MODELS ARE CHANGING

By Christine Gaze, CFP®, CIMA®

**N**ow that our industry's long march from commissions to fees based on assets under management (AUM) is nearly complete, a new fee movement has begun. Research indicates an increasing number of advisors are experimenting with fees and rethinking their fee models. The days of AUM alone may be numbered as advisors migrate toward a hybrid model that incorporates multiple pricing strategies. As shown in figure 1, more than 35 percent of advisors are planning to migrate from AUM to an alternative pricing model in the next two to five years.<sup>1</sup>

### WHAT'S BEHIND THE SHIFT IN FEE MODELS?

Several trends are driving fee innovation.

### MORE CLIENTS WANT COMPREHENSIVE FINANCIAL PLANS

Savvy clients increasingly are demonstrating a preference for goals-based

planning and comprehensive plans. This demand comes at a time of highly visible advertising about the benefits of having a financial plan. Numerous financial services firms have used advertising depicting a competent advisor who uses a slick, digital display to show a client's financial health. Additionally, in 2018, the CFP Board launched its multimedia "Let's Make a Plan" campaign to drive consumer awareness about the value of planning and partnering with a Certified Financial Planner® (CFP®) professional.

Recent research from Envestnet MoneyGuidePro may provide evidence that these strategies are working. Advisors indicate that 55 percent of their clients have financial plans, an increase of more than 14 percent during the past five years.<sup>2</sup> Cerulli Associates' research presents an even larger uptake: The advisors in their survey report that 71 percent of their clients receive modular or comprehensive planning advice.<sup>3</sup>

### TECHNOLOGY MAKES PLANNING EASIER

Financial planning software that produces an engaging visual display and client-facing output has become much easier to use and more affordable for the average independent advisor. Cerulli Associates recently reported that 73 percent of advisors currently use financial planning software and another 6 percent plan to use it in 2022.<sup>4</sup>

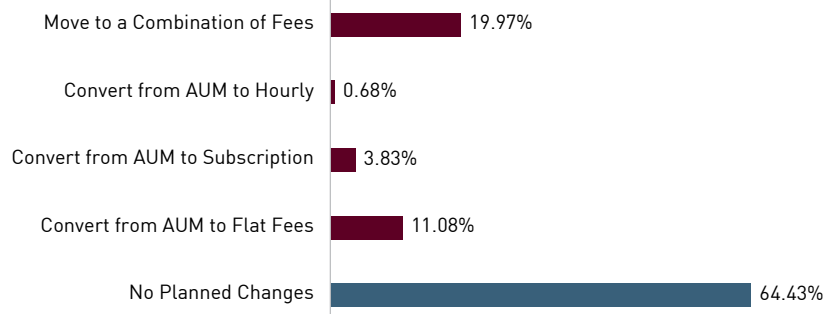
The coronavirus pandemic also helped boost advisors' tech savvy. As offices shut down, virtual meetings became commonplace. As clients sought reassurance regarding their financial well-being, many advisors mastered the art of delivering collaborative financial plans virtually.

Finally, the advent of AdvicePay, a payment processing system co-founded by Michael Kitces and Alan Moore, has removed friction for advisors and clients who choose direct payments versus AUM. The idea for AdvicePay was born from the need for a convenient and compliant fee-for-service solution that could be used by advisors in the XY Planning Network, also co-founded by Kitces and Moore. More than 6,000 advisors now use AdvicePay, according to Kitces.<sup>5</sup>

### PROFESSIONALIZATION IS GROWING

The influence of mega teams that manage more than \$1 billion has enjoyed significant growth in recent years. These teams often are formed to serve the needs of high-net-worth

**Figure 1** ADVISORS' PLANS TO CHANGE FROM AUM IN THE NEXT 2-5 YEARS



Source: Bob Veres, Insider Information Fee Survey, 2020

(HNW) clients, and they tend to offer holistic wealth planning.

Mega teams account for just 11 percent of advisory practices but manage nearly two-thirds of all client assets in the United States.<sup>6</sup> The leaders of mega teams frequently are profiled in the industry press for their organic growth prowess. The average advisor looks on and sees wealth planning as the model to effectively compete for HNW clients.

At the same time, more than 200 colleges in the United States offer the CFP curriculum embedded in a degree program. These programs are turning out thousands of graduates a year who require only three years of client experience to achieve CFP certification. Those who become advisors begin their careers with a solid understanding of the basics of financial planning, so they enter the business with greater professionalism.

### CERTIFICATION IS GROWING

Overall, the number of CFP professionals in the United States has grown by 31 percent in the past eight years. In addition, the Investments & Wealth Institute reports the number of Certified Private Wealth Advisor® (CPWA®) certificants who provide planning advice to HNW individuals has increased by 257 percent in that same timeframe.<sup>7</sup> Both seasoned professionals and new entrants are driving the “professionalization” of financial planning advice, spurring innovation with regard to planning fees and structures.

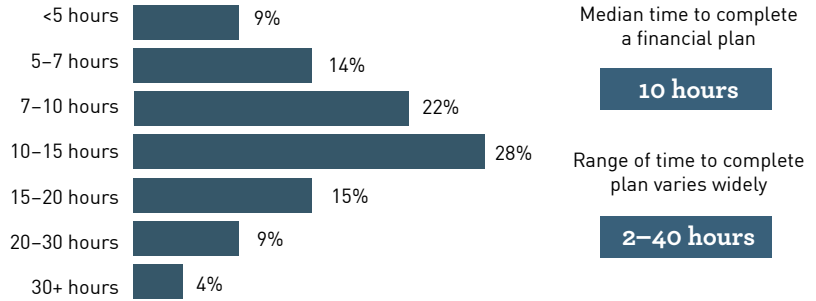
### CONSUMER DEMAND FOR TRANSPARENCY

The Department of Labor fiduciary rule, though not enacted in its initial form, still played a key role in both forcing the industry to improve transparency around fees and other business practices and boosting clients’ awareness about protecting themselves when seeking financial advice.

Gone are the days when fee structures were hidden within the Form ADV. In

Figure 2

## HOW MUCH TIME DOES IT TAKE TO COMPLETE A FINANCIAL PLAN?



Source: Bob Veres, Insider Information Fee Survey, 2020

fact, the U.S. Securities and Exchange Commission requires investment advisors with retail clients to disclose their fees, in plain English, on Form CRS. And more clients want to know exactly what they’re getting and what they will pay for it before they commit to an advisor.

Data from the 2022 World Wealth Report from Capgemini supports the need for advisors to improve both their services and their transparency. The report found that 27 percent of HNW investors weren’t comfortable with fees charged by their advisors in 2021—chiefly because of high rates and low transparency, and the perception that they were not getting value commensurate with the price.<sup>8</sup> EY research takes a more alarming tone. EY reports that nearly half of discretionary wealth management clients are dissatisfied with the fees they paid and do not trust they are being charged fairly.<sup>9</sup>

Often the most profitable clients are the least demanding, but they also could be the ones at greatest risk of defecting. As a whole, they are often the cohort with the largest imbalance of fees paid versus services given or demanded. Thus, advisors would benefit from examining their offerings and taking steps to create alignment between value-added services and fees.

### AUM MODEL LIMITATIONS

As more advisors seek to deliver quality financial planning to clients, they are

finding limitations in the traditional AUM model’s ability to compensate them fairly and adequately. In addition, during times of significant market decline, an AUM model alone can mean greater stress—and a sizable pay cut—for advisors.

AUM fees have been flat during the past decade, but financial planning fees are up. According to *The Kitces Report*, the median hourly fee for financial planning is up 25 percent in just the past few years.<sup>10</sup> As more advisors offer financial planning, they are realizing that it’s a time-consuming proposition. Research shared by *The Kitces Report* and a 2020 report by financial planning columnist Bob Veres<sup>11</sup> found that the median time to create an initial financial plan was approximately 10 hours, with a range from as few as two to as many as 40 hours (see figure 2).

As more advisors engage in “real planning” by expanding the scope of their services beyond retirement consultations and asset allocation to include developing net-worth statements, cash-flow planning, advising on tax efficiency, etc., they face a challenge: Who’s going to pay for all this work?

Operating under an AUM model, the fee stays the same, but the added services are time-consuming, creating a profitability challenge. Therefore, advisors facing this predicament require a suitable alternative fee model that aligns services provided with fees charged.

### FEE TRENDS FOR ADVISORS

Survey results from Veres show that AUM still reigns supreme as a fee model for advisors. Nearly 90 percent of advisors were using AUM for some clients, and 73 percent used AUM as their primary revenue model (see figure 3).

Notably, however, 14 percent of advisors declared flat fees are their primary revenue model.

Then Veres asked, “Do you have a different revenue model for some than for others?” The answer he got, detailed in figure 4, is that only 41.2 percent of advisors are using the same fee model for all clients. The majority, 58.8 percent of advisors, reasonably can be called hybrids. They are using a variety of models to meet client needs. This data

implies that the shift in fee models may be a more mature trend than most in the industry would suspect.

It’s worth noting that younger advisors are most likely to consider alternative pricing structures, such as flat and subscription fees, in part because many of their clients don’t have the assets to make the AUM model feasible. Research from Cerulli Associates finds that 43 percent of millennial advisors charge for an initial financial plan, as opposed to 29 percent and 28 percent, respectively, for Gen X and baby boomer advisors.<sup>12</sup>

### PRICES FOR FINANCIAL PLANS

The median flat fee for a financial plan is \$2,500. Kitces found the range to be quite broad, from as little as \$250 to as

much as \$12,000. That said, 80 percent of all fees fell between \$1,000 and \$4,800.<sup>13</sup>

The range makes sense given the variety of ways that advisors define and deliver planning for clients of varied needs and complexity. For some advisors, a flat fee defrays the startup costs and the AUM fee compensates for the ongoing relationship. Others charge flat fees for time-consuming special situations that go beyond basic planning. Increasingly, as shown in figure 4, advisors are using flat fees as their primary revenue source, which requires considerable thought to establish an approach that is both profitable and sustainable.

### PREVAILING HOURLY RATES

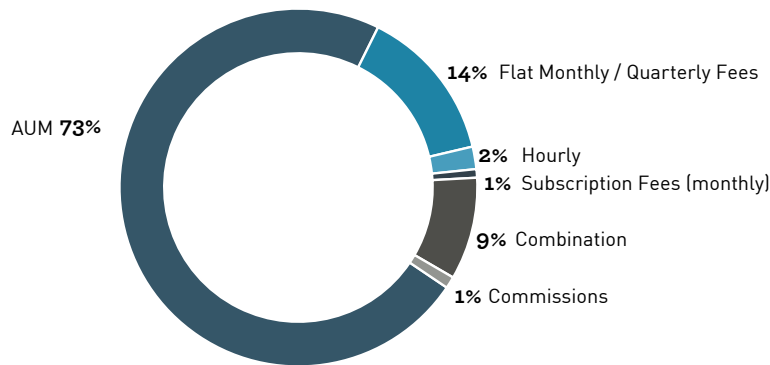
Only 2 percent of advisors charge an hourly fee for financial planning as their primary revenue model, but a growing number are using an hourly construct as a supplement. There is wide dispersion in hourly rates. Kitces noted a strong convergence of around \$250 per hour; Veres, whose data is cited in figure 5, found the median value of a senior advisor’s time was \$300 per hour.

### EXAMPLES OF FEE-MODEL ADJUSTMENT

The case studies below illustrate how two advisors have created their hybrid fee models to address some of the industry’s longest-running challenges.<sup>14</sup>

Figure 3

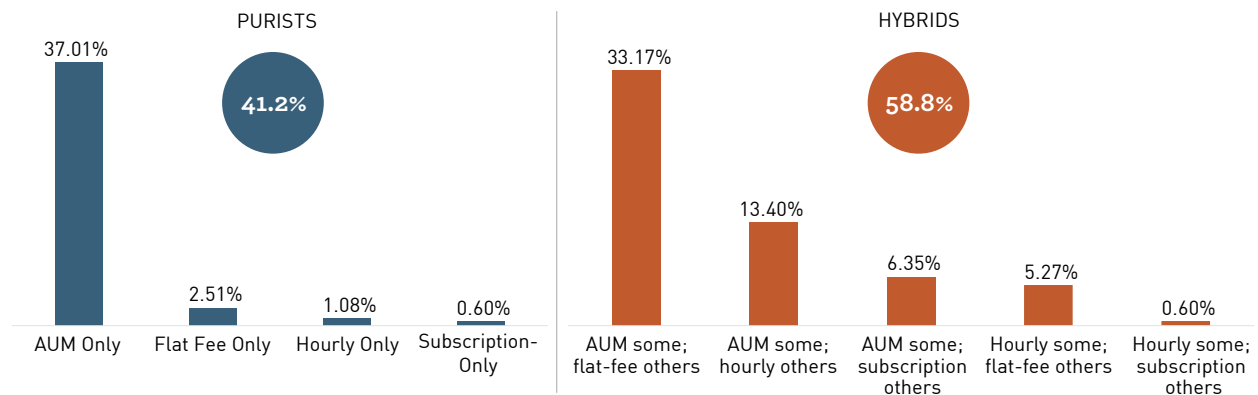
#### WHAT FEE MODELS ARE ADVISORS USING?



Source: Bob Veres, Insider Information Fee Survey, 2020

Figure 4

#### DO YOU USE THE SAME FEE MODEL FOR ALL CLIENTS?



Source: Bob Veres, Insider Information Fee Survey, 2020

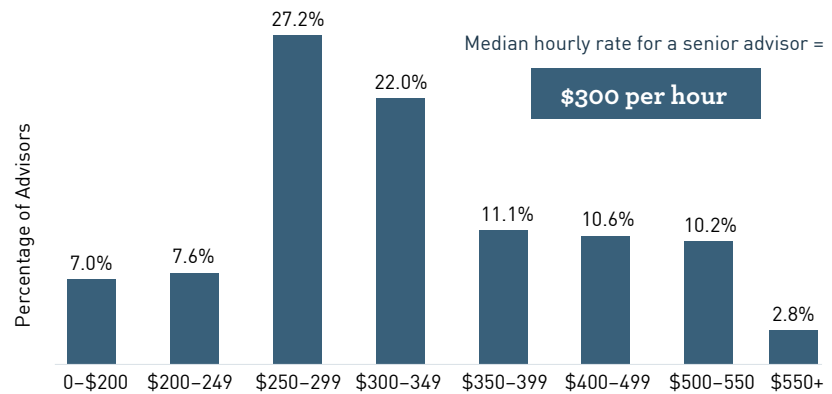
**STEVEN JONES**

Many advisors base fees on AUM, implying that their value lies in managing and growing investment assets. But Steven Jones, founder of a successful, multi-generational team, became uncomfortable with this model. "I felt like I was creating a hostage situation," Jones said. "Give us the assets we require to get paid and then we'll give you the advice that you need."

His team was originally built to deliver unbiased investment advice to wealthy clients. Jones gravitated toward business owners because he appreciated the decisiveness they displayed. During the past decade, the team has expanded to provide in-depth financial planning for HNW clients.

**The fee approach.** Five years ago, the Jones team began experimenting with a flat fee model for the referrals they get thanks to relationships with CPAs, attorneys, and business valuation experts whose clients need help with specific wealth planning problems. Some potential clients bristled at the idea of consolidating their assets with the team to get the planning advice they needed; in other words, they wanted out of the hostage situation. After many leadership discussions and some experimentation with hourly fees, the team created a new fee-for-service option. It began with a flat fee for referrals, many of which are complex. Getting the pricing right has taken time. Team members have grown more adept at assessing a prospect's needs, developing a scope of work and fee range that is on target. The pricing is based on rates of \$350/hour for a senior advisor and \$200/hour for junior support. The flat fee range is based on the hourly rates, but clients prefer the fee approach over a straight hourly charge.

**The result.** The team's revenue has grown by more than 60 percent in the past five years. The fee-for-service model accounts for more than half of

Figure  
5**HOURLY VALUE OF A SENIOR ADVISOR'S TIME**

Source: Bob Veres, Insider Information Fee Survey, 2020

that growth. And most clients that begin working with them through the fee-for-service model migrate to the AUM model. "When you clearly outline your services, your fees, and then deliver, the level of trust clients have is incredibly high," Jones said. "By the time we have addressed their initial issue, they know us, understand that we deliver, and cannot imagine managing their finances without us."

**OLIVER FLYNN**

Advisors are acutely aware of the research showing that heirs are likely to fire their parents' advisors after inheriting family wealth.<sup>15</sup> Industry veteran Oliver Flynn found ways to maintain intergenerational relationships, but doing so profitably has presented its own challenges.

Flynn hired a junior advisor, then created a distinct offering for the next gens, focusing on cash flow, debt management, building net worth, and teaching investing basics. But he didn't change his pricing model. Then he realized that the gross revenue from his numerous next-gen clients totaled less than \$9,000. He also realized that each year, an average of 10 high-end clients had significant life events that required complex planning. Using an hourly rate of \$350, he calculated he was giving away roughly \$52,500 a year.

**The fee approach.** Flynn created a menu that articulates fees across three different packages that vary in terms of the level of engagement and the depth and breadth of services needed (see table 1). Clients are charged an agreed-upon, fixed-dollar fee based on the scope of work on a quarterly basis. Investment management is charged quarterly as well based on a percentage of AUM.

**The result.** It took two years to migrate existing clients to the new pricing model. The flexibility it provides allows the team to align the fees clients are paying with the value they receive. A growing number of wealthy parents are gifting the bronze package to their children and grandchildren. Flynn's strategy also has created a consistent source of wealthy client referrals from parents hoping to ensure their grown children's financial well-being.

**HOW TO FIND THE RIGHT FEE MODEL**

When considering new pricing models, advisors need to begin by taking stock of what financial planning means to them (see table 2).

It may involve simply creating a "rapid plan" that provides a quick gut-check on a client's probability of retirement success given current investments and savings. Or it can refer to a complex and comprehensive plan, such as the one prescribed

Table 1  
**FEE PACKAGES**

Engagement	Platinum	Premium	Bronze
Target Segment	Wealthy families with complex tax or estate issues and/or special situations and/or business owners	Typical couple saving for college and/or retirement	Child of platinum or premium client; often a recent college grad or young couple
# of Planning Meetings	As required	2 meetings	1 meeting
Hours of Advice	20+ hours	15 hours	5 hours
Level of Service	<b>Advanced</b> Includes complex issues such as: complicated estate planning, business transition planning, elder care planning, divorce planning, executive compensation analyses, etc.	<b>Comprehensive</b> Includes a holistic wealth plan: cash flow, savings, and retirement projections, insurance and risk management, estate planning review, and investment plan	<b>Topical</b> Includes a basic plan and consultation designed to address specific client questions such as: Should I rent or buy? How do I pay down debt? Can we afford this house, car, or life?
Advice Fee	\$5,000–\$10,000	\$4,500	\$1,500
Investment Management Fee	75 bps	75 bps	100 bps

Table 2  
**WHAT DOES FINANCIAL PLANNING MEAN TO YOU?**

Basic Needs				→ More Comprehensive			→ Highly Specialized		
Cash Flow & Debt Management	Retirement Planning	Investment Planning	Education Planning	Tax Planning	Insurance Planning	Estate Planning	Family Needs Planning	Philanthropic Planning	Business Owners & Key Execs
Develop net worth statement	Review retirement savings strategy	Assess risk tolerance	Establishing tax-efficient savings plans	Ensure tax efficiency in asset location	Review insurance policies	Establish or update will	Divorce planning	Develop family mission & values	Assess cash management strategy
Examine current savings & expenses	Develop retirement vision and goals	Analyze current portfolio	Assessing affordability and funding options	Harvest tax losses	Assess coverage adequacy for life, long-term care, disability	Establish or update trusts	Elder care planning	Create impact goals & priorities	Advise on employee benefit plans
Identify short- & long-term savings goals	Review corporate benefits	Translate savings goals to investment objectives	Maximizing tax-free gifts	Advise on tax-aware strategies	Develop strategies to mitigate risks	Ensure appropriate control parties: financial & health	Planning for special needs children	Fund charitable strategies	Analyze business disruption risks
Establish emergency fund	Claiming strategy for Social Security	Create asset allocation strategy	Helping children save and budget	Keep up to date on tax law changes		Organize estate documents	Planning for a solo journey	Optimize tax benefits	Assist with business transition
Create optimal savings strategy	Retirement distribution strategy	Construct tax-efficient portfolios	Educating on FAFSA & loan options			Ensure proper asset titling		Philanthropic planning	Assess compensation plans
Analyze liabilities for savings opportunities	Retirement-income planning	Regularly review investment performance				Create and manage gifting strategies			Develop strategy for stock options
	Planning for healthcare & caregiving expenses					Assist with charitable giving			

by the CFP Board, that addresses savings, debt management, and planning for education and retirement, establishing or maintaining an estate plan, ensuring adequate insurance coverage, and creating a tax-efficient investment strategy to fund the client's future goals.

One hallmark of many mega teams is the depth of financial planning services and expertise they provide wealthy

clients. Mega teams increasingly are adding talent with specialized knowledge such as family needs, philanthropic planning, and transition strategies for business owners.

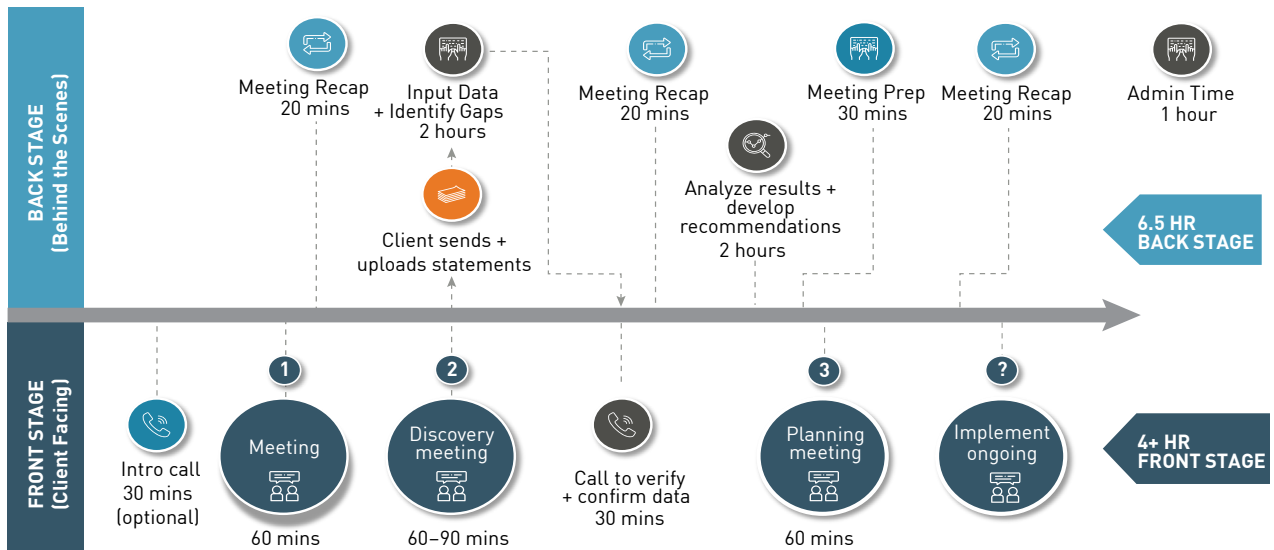
When crafting options for a new fee model or models, advisors need to get clear on the “what” of their planning offering(s) and then calculate the time involved for typical clients.

Figure 6 provides a visual display of the breakdown of tasks and the time it takes to create an initial financial plan based on the industry median of 10.5 hours.

Some steps, such as inputting data, identifying data gaps, and analyzing results, can be delegated to an associate advisor or paraplanner; others, including client meetings and potential meeting recaps, require the lead advisor's time.

Figure 6

ANATOMY OF AN INITIAL FINANCIAL PLAN



Advisors should consider industry benchmarks and where they fit in, and ask themselves:

- Can they quantify the time spent on planning and advice-giving for various client segments?
- Is their current pricing model working?
- Do they perceive alignment among the time spent, value delivered, and fees paid?
- Can they command a premium due to the depth of planning they offer or the unique nature of the expertise they bring?
- Are they clearly communicating their offering and their fee model to clients?

LOOKING AHEAD

Fee models must be transparent and create a fair alignment between the price paid and the value of services offered and delivered. Advisors and firms that recognize this will continue to fuel the hybrid approach to “right-sizing” client fees.

The AUM model as a solo approach has many limitations for advisors that offer “real financial planning” and can be unfairly punitive during bear market cycles. It also is the least preferred

method of compensation for rising generations of clients. Therefore, we anticipate this model to continue to lose favor.

The advisors of the future are those who can define their planning offerings, understand the value of their services, and effectively articulate this to clients and prospects along with their fees. ●

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