RAISING YOUR FEES

To Reflect the True Value of Your Services

Part of Securities America's Business Mastery Series

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Introduction

Financial advisors are usually hesitant to formally examine their fee structure because by doing so, they are forced to confront and address the disparity between their current pricing and their true value to clients and must then act to correct this discrepancy. The old adage, “Ignorance is bliss” often applies, as almost every advisor we have worked with has been less than eager to approach loyal, long-term clients to discuss increasing their fees.

The work a financial advisor does for his or her clients is valuable and important. As with any business relationship, advisors should be compensated fairly for their services. However, advisors in general, and particularly independent advisors (who have the flexibility to set their own rates), typically struggle with pricing their services objectively.

Businesses of all types and sizes must increase their fees over time, and independent financial advisors are no exception. More than likely, you are undercharging for the services you provide. In light of the Department of Labor’s new fiduciary rule, most advisors will need to raise fees due to compensation restructuring of advisory products and platforms. The information provided in this guide will help you take the steps necessary to enhance your profitability and ensure the long-term stability of your practice.

Why Pricing Transparency and Consistency Is Important

Advisors must embrace transparency, equality and consistency in their pricing strategies. Pricing each client on an individual basis creates problems for an advisor. For one thing, discounting one client versus another, charging one client a higher fee for nearly identical services and varying your asset management fees for the same asset level are unjustifiable from a compliance standpoint.

Further, you will be asked at some point for the rationale behind your pricing decisions, and without a consistent fee and service schedule to rely on, you will be forced to provide individual explanations as to why certain clients are paying significantly more than others.

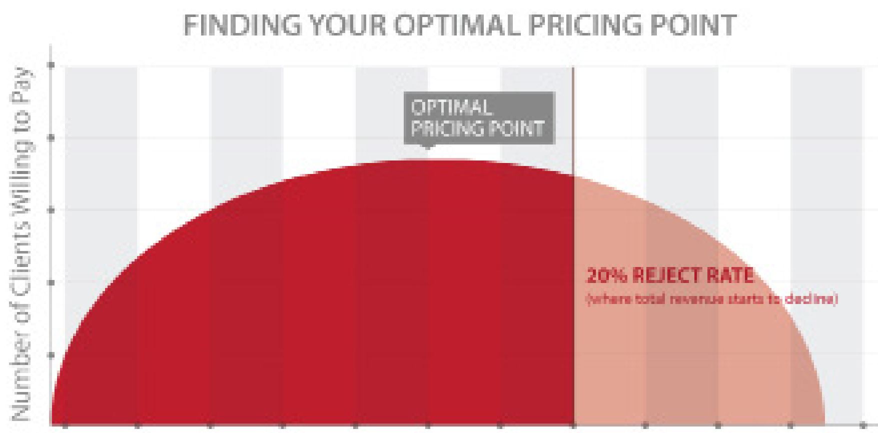
Inconsistent pricing is also problematic for your staff from a service efficiency standpoint. If staff members do not know what a client is going to be charged, workflow inefficiencies result, including incorrect paperwork and billing as well as missed service deliverables. With inconsistent pricing, your staff will most likely treat each client differently, counteracting a “WOW!” service standard that you want your clients to experience. And, what if two of your top clients are discussing your fees at your next client appreciation event and discover they are being charged significantly different amounts? How do you think the one being charged more will feel about you?

Finding the Optimal Pricing Point

Pricing needs to be purposeful and integrated into your overall business strategy. Price and value are linked together and cannot be decoupled. There must be a fair charge for the value delivered. When price and value become unbalanced, you have an unprofitable and unsustainable business. The chart below shows that optimal pricing occurs when your pricing attracts the greatest number of buyers at the highest price. **The optimal pricing point is the peak of the curve.** This point can also be viewed as a "tipping point," beyond which pricing becomes a point of rejection for your services and you would begin to lose a significant number of clients. That is, beyond this point, you are likely overcharging relative to the value you provide and your competition.

Many advisors ask themselves: *"Am I underpriced? How much should I be charging for my services? What's fair? How much is my competition charging?"* The optimal pricing approach will help you to answer these questions.

Getting to optimal pricing can involve a process of trial and error, but the mistake advisors often make is to pull back or lower pricing when just one customer rejects their service. The standard we



apply is as follows: **You are at optimal pricing when 20% of customers reject your pricing.** If more than this percentage of your prospects are rejecting your service due to pricing considerations, then you are likely overcharging for your services. However, you shouldn't hold back on pricing changes simply because one or two clients or prospects balk at a warranted price increase.

Embracing optimal pricing will have a great impact on your profitability. There is far greater price elasticity in your market than you assume. Financial services are just that — they are services. In many service professions, there is a wide spectrum of pricing. The services of doctors, lawyers and CPAs are priced on a continuum of value or perceived value.

Even within specific professions, there are pricing differentials. For example, an attorney specializing in a specific legal service may charge a significantly higher fee than an attorney who is a legal generalist. And a surgeon in one practice specialty may charge a substantially higher fee than a surgeon in another specialty.

Making optimal pricing even more elusive in the financial services profession, many advisors are not clear on the tangible deliverables a client will receive and the corresponding cost of delivering those services. To overcome this lack of clarity, the fees-and-services schedule is your “tangible deliverable” that can be used to show clients the value you provide for the fee they will pay. That’s important because clients don’t know what services you offer unless you tell them. For example, clients who joined you many years ago may not know that you offer insurance, estate planning or long-term care insurance.

Consumers are confronted with pricing decisions all the time, and they often make their buying decision based on emotion. If they value your relationship, feel that the services you provide are valuable and their needs and concerns are being addressed, pricing will be secondary.

Developing the Confidence to Raise Your Fees

The fear of a client strongly objecting to a price increase is often used as a justification for not making a change. From our experience, we believe this concern is largely unwarranted. We have worked with hundreds of advisors over the past 20 years and have found client objections to price changes are likely to be substantially less than anticipated. Advisors have reported they have received little pushback on pricing and what pushback they received was from clients who they didn’t really enjoy working with.

The few clients that advisors reported losing because of a pricing change actually reduced the advisor’s workload and the stress level of their staff, and in hindsight, freed up time for new, more profitable client relationships. So, be realistic and prepare to lose a small number of clients when raising your fees, but be sure to view client losses from a business owner’s perspective. That is, the loss of a certain number of clients may be necessary in order to improve your overall growth and profitability in the long run.

Many advisors lack confidence in presenting their fees, and as such, either avoid or fumble through these conversations with clients. Keep in mind clients expect to pay a fee and can understand why a fee increase is necessary as long as a logical explanation is provided in an up-front, educational manner.

The relationships you have built and the value you provide weigh much more heavily with clients than the price they pay. That’s not to say an unjustified or excessive price increase will be tolerated by your clients. Understanding your services, the value you provide and why you charge the fees you do will give you the conviction to sell your services at the fees that you determined are appropriate and reasonable for your practice. Having this confidence will allow you to engage clients in a conversation about raising fees that goes smoothly and generates very little pushback.

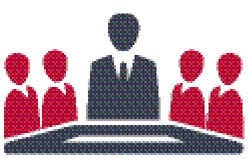
Developing Your Optimal Fee Structure

To develop the confidence to raise your fees, you will need to develop the rationale for doing so. First, you should determine your optimal fee point and structure. Calculate your practice's inflection point, the point at which the additional dollars from raising your fees minus the potential lost revenue from client attrition are equal. If your analysis indicates you will achieve a sizable revenue increase by raising fees to competitive market rates, it is likely your practice could withstand a significant exodus of clients without a corresponding drop in revenues. Indeed, the more quickly you replace underpriced or over-serviced clients with new, properly priced and properly serviced clients, the greater your chances are of maintaining and substantially increasing your revenue.

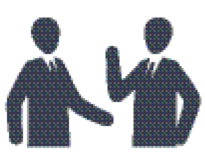
When raising your fees, you should also be proactively working to replace any clients that you lose. If you keep your marketing and referral campaigns firing on all cylinders and targeted toward your ideal prospective clients, the revenue impact of your price increase should be minimal to your practice.

Best Practices for Building Confidence to Raise Fees

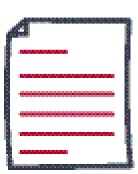
We recommend the following best practices to help you increase your confidence when approaching clients to discuss fee changes.



Best Practice No. 1: Use an advisory board or an individual-meetings approach with the clients you value most to get feedback on your pricing and fee-raising strategies. Many advisors have reported this is a valuable exercise, as the client feedback has been overwhelmingly positive. Clients understand the need for a fee increase, especially when the services provided are revisited. Focus the justification for your fees on the services you provide, not the amount of assets a client has, and your confidence level will soar.



Best Practice No. 2: When making substantial pricing changes in your practice, work with your lower-tier clients first. This will give you the opportunity to hone your message as you get initial reaction to your changes, and you can build talking points for specific situations for yourself and your staff.



Best Practice No. 3: Formally notify clients by letter offering your rationale for making pricing changes in your practice and preparing them for the need to sign new fee agreements to "bring their account(s) into compliance" with your new pricing structure. Be straightforward that a pricing change needs to take place. (See Sample Client Letter at the end of this paper.)

Creating Goodwill When Raising Fees

Making strategic decisions about pricing is often a necessary part of being a business owner. Fees, especially financial planning fees, cannot remain stagnant over time. Because your services and expertise have evolved over the years, you are most likely providing additional value you may not have delivered when you first started working with your clients. If you have not adjusted your fees as your value-added has grown, your relative fee structure has naturally eroded to the point that you are now likely underpriced in your marketplace. Overcoming your fear of losing clients is vital to positioning your practice on a course of sustainable profitability.

Raising fees should be done using an approach that leaves the client with the feeling that the increase is reasonable and in their best interest. “In their best interest” means they are receiving a set of services in line with their needs that they find valuable at a fair price. This may include a formal plan addressing their most important financial concerns and working toward their most important goals as a tangible benefit. Remember, even if you think they do, clients don’t really know all the services you provide. You must constantly remind them about everything you can do for them.

One best practice is to create and publish your fees-and-services schedule, a tangible reinforcement of the value you provide. Psychologically, this schedule cements in writing what your services cost and what they are worth – no negotiation allowed. And it also reinforces to your staff what your services are worth. If you charge $5,000 for a financial plan, your staff will treat the process as a $5,000 process. Distribute your fees-and-services schedule at every opportunity with your clients.

At this point, it should be mentioned a reduction in fees will be the appropriate action in some cases. We have discussed matching pricing with the value provided, and the SEC has made it clear certain advisory accounts should have fees reduced or turned off all together if the management of the account and trading activity are minimal. Accounts with high cash balances and low trading activity will generate a red flag, causing the account to be reviewed by SEC Supervision for excessive fees. Be sure to discuss any specific client accounts that may fall under this scrutiny with your Sales Supervision principal before including them in any fee-raising strategies you may choose to implement.

Raising Fees Requires Analysis and Takes Time to Implement

Raising your fees should be the result of an intensive analysis of your current services, revenues, costs and fee structure as well as the competitive environment. Because of this, it takes time to implement. Some advisors take a year to 18 months to successfully complete the process. Take time during each step of the analysis to correctly gather and assess the data, obtain feedback from your best clients and determine possible fee-increasing strategies; then include your staff in the decision process and ultimately in the execution process.

Raising fees starts with a systematic analysis of your revenues and expenses. Your revenues include your retainer, as well as AUM and planning fees. Even if you do not charge planning fees, we suggest that you take the time to conduct a full revenue analysis of your firm. One mistake advisors often make is to avoid conducting the analysis because, they believe, *"My business model is different."* Not true; every business owner will benefit from this exercise as revenue disparities are exposed.

Your expenses include your fixed costs and the costs associated with providing services to individual clients. To conduct your expense analysis, build a detailed spreadsheet with all of the components. This work should be done by your staff under your direction. Be sure to communicate to your staff the value of this exercise in beneficial outcomes for them such as: increased profitability, which leads to greater stability of the firm, increased efficiency in workflows by having standard service levels and clear expectations as to which clients should receive best-in-class or VIP service. The data gathering may take several months to complete and up to a year to validate the time costs discussed in the next section.

Conducting the Analysis

STEP 1: Analyze Your Revenue

The first step in analyzing a practice's profitability is knowing how much revenue is coming in and where it's coming from. Start by creating a spreadsheet of client households and the revenue each has generated over the past 12 months. Include any ongoing fixed insurance revenue and revenue from sponsor companies that don't download to your system.

Next, gather the recurring planning fees and AUM fees you charge on an individual client basis and enter those onto the spreadsheet. Be sure to include separate columns for advisor, platform and manager fees and list this information again on an account-by-account-level basis. You will need this information later in the process.

Next, combine revenue for each client account in the household into one amount for the entire household.

Sort the households by revenue, from greatest to least. Segment the list into 10 parts and calculate the revenue per decile. By dividing your client base into 10 segments, it will be easier to see which client groups generate the bulk of your revenue.

STEP 2: Analyze Fixed Office Expenses:

Step two is the straightforward process of analyzing your fixed expenses. Fixed expenses, including office space, equipment and utilities, fund the existence of your business. Add up your fixed expenses and divide the total by the number of households in your client base. This will give you a base amount of revenue that each and every client household must generate just so you can open your doors each day.

Create a Fixed Cost column and enter the allocated fixed cost of running your business into the spreadsheet for each client household.

STEP 3: Analyze the Cost of the Services You Provide

What does it cost you to do business, and what are the costs associated with serving specific clients? Time costs – the value of your time and your staff's time – can be the most difficult to measure. There is time spent running the business itself and time spent serving clients collectively and individually.

Compiling a spreadsheet to calculate the cost of services provided requires a little more effort than the revenue analysis. You may need to review the past several quarters with your staff to arrive at an hours-spent figure for each client or household.

If you are unable to get a good estimate of time spent from your staff, another approach is to implement a client time-tracking sheet and ask your staff to log time spent with clients on each activity, including account maintenance, annual or semi-annual reviews, performance reporting and trouble-shooting. You may want to track your time separately from staff time, as your "hourly rate" should be significantly higher. Assign hourly values for staff time and advisor time and calculate the total time cost per client or household. To get an accurate picture of the cost of services you provide, you may need to continue the time-tracking for up to a year.

Create a Time Cost column and enter the time cost of the services you provide for each client household.

Create a P&L column and use the calculation "revenue generated by household" minus "cost of services provided by household" minus "fixed expenses" to arrive at a simple profit/loss for each client.

Sort your list again by the P&L column and compare that figure to your initial revenue analysis. Typically, the most revealing figure to advisors at this point is the amount of services provided to some customers where no revenue is being generated – which means they are doing work for free. Take a look at your data: Did some households drop from the top 20 percent and others rise up when you compared the P&L to the revenue analysis? What percentage of households landed in the "red zone" – those who are actually costing you money to serve?

STEP 4: Analyze for Consistency Within Your Firm and in the Marketplace

Four Outcomes of Your Analysis

- Determine if your fees are competitively priced in your local market
- Determine if each client segmentation group is profitable
- Determine if clients in the same client segmentation group are being charged the same fee
- Determine if clients are matched to the proper service level

Now comes the most difficult, but incredibly valuable, part – deciding what to do with your analysis. With the information gathered and your revenues and expenses determined, conduct a four-part review based on marketplace, revenue, pricing and services consistency.

- **Marketplace Consistency –** Analyze your firm's fees versus fees charged by your competition.
  - Determine if your retainer, AUM and planning fees are competitive with what advisors in your local area are charging for similar services to determine if you are underpriced, and develop your strategy for increasing your fees on a "global" basis (i.e., for the firm as a whole).
- **Revenue Consistency –** Analyze your revenue by client segment. Each client household in the segment should be generating the same or nearly the same amount of revenue on an annual basis.
  - Determine which clients are underpriced (or providing no revenue at all) and determine your strategy for increasing the amount of revenue earned through retainer, AUM, converting to AUM or planning fees.
- **Pricing Consistency –** Analyze the amount charged to each client in the segment. Each client household in the segment should be priced the same on an AUM, planning fees and retainer fees basis.
  - Determine the appropriate set of fees for each client segment and determine your strategy for increasing the fees of those clients who are underpriced and decreasing fees for those clients who are overpriced. Often, advisors will find a small number of clients who are actually overpriced. This can happen when a client's fees are not adjusted upon reaching a breakpoint where they have added assets.
- **Services Consistency –** Analyze services provided by client segment. Each client household in the segment should receive the same set of services.
  - Determine the appropriate set of services for each client segment and determine your strategy for communicating the right-sizing of services or the addition of services to clients who are being over served or those who could be served at a higher level.

Your first priority should be ensuring clients in the top 20 percent of profitable households never have a reason to go elsewhere. Meet with your staff so they understand who these clients are and determine how they will be treated differently from other clients. That's not to say your other clients should receive poor service; it's a matter of prioritization. For example, if your service standard for all clients is to return calls and emails within 24 hours, your top 20 percent of clients may get calls and emails returned within two hours.

Strategies for Raising Fees

Of course, further segmenting your client base, establishing service levels for each segment and adjusting client expectations may require additional considerations that you and your staff should discuss as a team and then determine which are right for your practice. There are nine strategies for raising fees:

1. New pricing for new clients
2. A practice-wide price increase
3. Converting non-fee-based accounts to fee-based
4. Increase pricing for top-tier clients who are being undercharged
5. Enhance services for top-tier clients
6. Charge premium pricing for premium services
7. Reduce services for low-tier clients
8. Implement retainer fees for low-tier clients who want top-tier service
9. Reset expectations as to what services clients are going to receive for their segment level (e.g., one meeting per year versus four meetings per year)

Determine which strategies are appropriate for your practice and then determine the order of priority that makes sense for you. We recommend you start with the "new pricing for new clients" strategy, as it is the easiest to implement — where new clients can have expectations for service and pricing firmly established at the outset of the relationship. Next, determine the strategies that can have the highest effect on your overall profitability and prioritize them with your staff's input.

Summary

Raising your fees should not be an across-the-board price increase just for the sake of generating more revenue. Rather, it should be a systematic process of analyzing your client segments and the services you provide in those segments and pricing their value accordingly. Generating more revenue will be the ultimate outcome, of course, but the process of analysis helps you to systematize your practice and charge fees that are consistent with the services and value delivered. Systematization of the services you provide and the fees you charge lays the foundation for you to bring on additional clients in a more efficient manner. Your staff will be better able to prepare paperwork, and they will know the amount of client touches the new client should receive and what services the client should be scheduled for without having to wait for instructions from you.

Set a goal to conduct your fee-raising analysis over the next year. As you evaluate your prices and consider increasing your fees, keep in mind the Department of Labor fiduciary rule requires any investment advisor representative or registered representative who gives investment advice regarding retirement accounts such as IRAs and 401(k) plans to act in their clients' best interest. Under that standard, you must be able to show the compensation you receive is reasonable for the services you provide.

When you carefully analyze your fees, you will undoubtedly uncover lost opportunities and service-level discrepancies that, when corrected, can help you to generate additional revenue and make your practice more efficient and ultimately more profitable.

Sample Client Letter

Dear

We at <firm name> work hard every day to deliver the highest quality of asset management and related services to valued clients like you. We believe we are a leader in delivering outstanding service at a fair price.

I'm writing to you today about our program to systematize our fee structure to provide clients with the best service priced consistently relative to value delivered and to competitive industry standards.

Over the past year, we have been analyzing our client accounts, along with the fees we charge, and comparing them to the industry at large. We are now publishing our Assets Under Management (AUM) fee schedule (see below). Over the course of the next several weeks, we will be sending you paperwork, or we will schedule a meeting with you so you can sign new agreements to bring your accounts into compliance with this schedule. We are happy to speak with you by phone or meet with you to discuss these agreements in further detail. In some cases, we have included your paperwork in this mailing. If the paperwork is included, please review, sign and return the new fee schedule applicable to your account relationship.

Asset Management Fee Schedule*

Minimum AUM	Charge On Assets	Minimum AUM	Charge On Assets
$10,000,000+	0.60%	$ 1,000,000	1.15%
$ 5,000,000	0.80%	$ 500,000	1.25%
$ 2,500,000	1.00%	$ <500,000	1.45%

*Percentages shown in this schedule represent fees paid to <advisory firm> as an average based on total assets under management. Fees charged to the client may be greater than those shown if the fees charged by the Model/Investment Manager and the Account Custodian are included.

We believe this fee schedule is both competitive and fair for the services we provide. To remind you of the services we offer, we have enclosed our Services Overview.

We look forward to either receiving your signed paperwork or meeting with you for the same purpose.

If you have any questions, please do not hesitate to contact me at:

Sincerely,

<name>
<advisory name>

Securities America
Your business growth expert.

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