Bukaty Companies Financial Services reigns as the 2019 PLANSPONSOR Retirement Plan Adviser Mega Team of the Year, and President Vince Morris has some thoughts on how adviser firms can maintain profitability in these fee-pressured times.

"Don't rush to be the lowest common denominator, on your fees," suggests Morris, who founded the Overland Park, Kansas, advisory practice. "We're seeing a lot of pricing pressure in the [industry] now, but it's better for the health of your practice in the long term to run as a profitable entity. Every company deserves to be profitable, including yours."

This is a complicated time for plan advisers to assess their profitability, as more plan sponsors focus intensely on fees. Sponsors ranked plan fees first—above other much discussed concerns such as financial wellness and retirement readiness—as their "most likely primary area of focus over the next 12 months," according to Callan's "2019 Defined Contribution [DC] Trends" report.

"Yes, our clients are demanding more and more value from us as advisers," Morris says. "But you are only going to do great things for your clients in the future if you have that profitability." By charging reasonable fees, Bukaty has profited enough to reinvest significantly in its business—for example, in its financial wellness program and technology—to help plan administration run more smoothly. "You can't do that if you're always the lowest common denominator on fees," he notes.

Gauging Profitability

Fee and profitability pressures also seem to be partly self-imposed by some plan advisers riveted on growing their practice's client list. "I see advisers who are relatively new to the institutional-market business, coming in with low-ball fees to win a plan's business," says Michael Maresh, senior vice president at CAPTRUST in Austin, Texas. "At some point, that strategy is going to come back to haunt them. At some point, they'll have to increase the fee so the client can be profitable."

According to Richard Applegate, some plan advisers pay too little attention to having a sustainable business. "What we're seeing now in the marketplace is the same mentality as a broker's, but on a fee basis: 'I can do it for less,'" says Applegate, senior financial adviser and managing director of DBR Fiduciary Plan Solutions in Pittsburgh. "There are many people rushing into this business just looking to get the plan assets, and if that's all they're doing, they will end up being disappointed. It's their own issue—not the client's—because to get the business, they promised the client the moon and the stars."

Plan advisers who want to build a sustainable business need to determine how much time—and staff—it actually takes to do their client work, sources say. "We do a time analysis at least annually, and we have a fairly sophisticated calculator that we've developed internally," Morris says. "The calculator is based on time studies we do to track how long each specific task takes. So, for example, we'll ask our six relationship managers, 'For the next two weeks, track all the client work you do, in 15-minute intervals, and record it in our [Salesforce] CRM [customer relationship management] system.'"

That shows Bukaty how much time it takes, for instance, to prepare for a particular client's quarterly committee meeting. "You track the time as you do the work, so at the end of the year you can see how long you spent doing each task for each client," Morris says. "Then you can see things like, 'We dedicated X extra hours to servicing that plan during the year.'"

Strategic Retirement Group Inc. (SRG) has put effort into clarifying how its team members spend their time, says David Hinderstein, president of the advisory firm

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in White Plains, New York. But he has chosen not to track individual employees' exact hours. "We could count hours, but that would change the collegial, collaborative way we work together," he says. Instead, SRG estimates time and costs—i.e., payroll and other expenses—for each client. "As soon as you get to the point of counting hours," he says, "then you have to compare individuals, which changes the team chemistry."

Renegotiation Approaches

Sometimes, the amount of work the adviser is doing relative to the fee the client pays becomes unbalanced, leading to fee renegotiations. "I think you have to have a basis for that conversation, and the best basis is independent benchmarking data on the advisory fee," says Stace Hilbrant, managing director of 401k Advisors LLC in Wilmette, Illinois. His firm does benchmarking of its fees with third-party services every year, relying primarily on data from Fiduciary Benchmarks (FBi). "If the benchmarking finds that our fees are too low, we go to the sponsor and say we need to adjust our fee," he says.

"We can say to the sponsor, 'Based on benchmarking of plans with your demographics and asset size, the mid-point fee is $10,000, and we're only charging you half that," Hilbrant says, speaking hypothetically. "That's a pretty clear basis for renegotiating.'"

SRG also benchmarks its fees annually and shares the results with its clients. "If the benchmarking shows we're low, we can tell the client that it's time for us to adjust it," Hinderstein says. "I think it's important to have the backup data, rather than just shooting from the hip."

It is also important for an advisory practice renegotiating its fee to document what specific work it has done for that plan, including any recent increase in services requested, Hinderstein says. "If you need to have a fee conversation, it's often really a services conversation," he says. "It's an issue of, 'Hey, it's been a great relationship for five years, and now we're doing all these additional things for your plan. We need to adjust the fee."

Applegate recently had smooth renegotiations with a sponsor of a $2 billion plan with rapidly growing participation. "You've got to be methodical about it:

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Renegotiating can't be a 'land grab' by the adviser," he says. "I showed the sponsor, 'Here's the benchmarking for what is considered to be a reasonable fee for an adviser's work with a plan like yours. It shows that our fees are not only in the first quartile—the lowest quartile—but are half of what the benchmarking shows is the reasonable fee.' I also showed the sponsor that by adjusting our fees, we would still be at the same fee, on a per-participant basis, that we've had for the past several years." The client agreed to the new flat fee.

If there is a mismatch of services and fee, an adviser can try to renegotiate the amount of time-consuming services a client receives, such as on-site participant education and sponsor meetings. "The easiest answer, there, is, 'Our time is valuable,'" Hilbrant says. "I can say to a client, 'If I'm in your plant 12 days a year doing education, that's what needs to go.' We can leverage resources from a plan's recordkeeper to sit down with employees at the client's plant and do education."

Some sponsors have no problem with decreasing the number of committee meetings, Morris says, which reduces an advisory firm's expenses, as an adviser has to travel less often. "If we're doing quarterly meetings, we can talk to the sponsor about going to semi-annual meetings and keeping the fee the same," he says. "Or if the sponsor wants to keep the quarterly meetings, then our fee needs to go up. That way, the client can make a choice."

Preventing Unprofitability

According to sources, advisers have several means to keep a plan from turning red on their spreadsheet.

Choose carefully how you spend your time. Hilbrant's firm spends considerable time doing on-site group and one-on-one participant meetings across the country, and having follow-up conversations with participants by phone. "Some advisers don't want to do these types of time-consuming services," he says. "It's been a real advantage and differentiator for our work efforts." On the other hand, he says, his firm does not aggressively promote conducting formal vendor reviews, doing them only every three-plus years; there are other ways to judge fee and service competitiveness, he notes.

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As Philip Chao sees it, too many plan advisers spread themselves too thin. “We don’t do 90% of the stuff other advisers do,” says Chao, principal and founder of advisory firm Chao & Co. Ltd. in Vienna, Virginia. “Many advisers don’t know where their value is. They are just going in and commoditizing themselves: Today it’s, ‘Let’s do HSA [health savings account] education,’ and tomorrow it’s, ‘Let’s work on student loan debt.’”

Chao & Co. concentrates on a couple of core, in-depth services for plans. “I have a very defined model, and my model is that I do two things,” Chao says. “Number one, I’m a fiduciary adviser, and I offer plan sponsors a prudent investment process. And, number two, I am very good at being a quarterback, so I help sponsors prudently select and monitor their other service providers.”

Clearly define service deliverables. Strategies Capital Management (SCM), headquartered in Denver, specifies in its flat-fee contracts exactly what it will do for a client, and notes an additional hourly fee will come into play only if services exceed the work SCM and the client agreed to, says President Tom Gonnella. “The service agreement details, in line items, all the different services that the client will get from us, and we price it accordingly,” he says.

Managing a client’s expectations about the services it will receive is crucial, says Maresh. “I always explain to clients at the start of every year, ‘Here is “a year in the life,” working with us.’ We show what we’re going to do for them. Then they know what to expect, and it gives us accountability.”

Be transparent about when fees will rise. Some advisers charge an additional, specified fee for any extra work beyond the service agreement, and some incorporate an annual cost-of-living fee adjustment into the contract. With more advisers moving from an asset-based fee to a flat fee, Maresh says, that means they no longer automatically get a fee increase as plan assets grow. “In our practice, we now put an annual fee increase in our service agreements, and that’s usually between 3% and 5%,” he says. “Our clients understand there’s an increase in our costs every year. And 3% to 5% is not a big increase to them. Our clients get it.”

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Offer a multi-tiered service model. SCM did an in-depth study of its profitability five years ago. The study found that the firm sometimes gave small, lower-revenue plan clients the same full level of service as its large, higher-revenue clients. “So we bifurcated our services and developed a second service model that’s more scalable and economical,” Gonnella says. Clients choosing that newer model—mostly plans with less than $10 million in assets and just starting to work with a specialist plan adviser—are paired with a less-senior adviser, get less in-depth reporting, and have an investment menu limited to target-date funds (TDFs) or target risk funds.

“This has really helped us to educate our clients,” Gonnella says. “We can tell them at the outset, ‘Here are a couple of service options. Here’s our typical full-service model, and here is what it costs. If you don’t need all those bells and whistles, and you want something simpler and more economical, here’s our second model, and here is what it costs.’”

Quitting Time

When should a plan adviser consider ending the relationship with a plan sponsor client? Possibly under these circumstances:

• **The sponsor is uninvolved.** “It hasn’t happened often, but the termination of a relationship for us is usually because of the lack of involvement on the client’s side to fulfill its own fiduciary responsibilities,” says Richard Applegate of DBR Fiduciary Plan Solutions. “What I’m most concerned about is, are they doing their part to mitigate the fiduciary liability? If a participant ever sues the sponsor, you are always going to be enjoined in that suit as the plan’s adviser.”

• **Big logistical obstacles exist.** David Hinderstein of Strategic Retirement Group has ended only one client relationship—with a West Coast company that was difficult logistically for his East Coast firm to service. But he recalls an adviser who wanted to drop an unprofitable client asking him what to say. “You can say, ‘You know, I don’t think this relationship is working for either of us. I

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know how important the plan is to you, and doing a good job for our clients is very important to us. I'd like to figure out a transition strategy to end our work with your plan."

• **Your firm is changing markets.** Over the evolution of his former firm, InTrust Fiduciary Group, before he joined CAPTRUST, Michael Maresh and his colleagues switched from targeting small plans to midsize and large plans. "In some cases, we had to say, 'We're shifting markets and now have a different service model and revenue requirement, and we'll need to help you transition to another adviser,'" he says. "If we continued serving these plans with our new [higher] fees, that could have put those sponsors at risk of now paying unreasonable fees."

• **The plan doesn't grow.** In his days as a registered investment adviser (RIA) building a stand-alone firm, Maresh says, the practice occasionally took on unprofitable clients, expecting these small plans would grow profitable in time. "But a plan doesn't always grow as expected," he says. "If that happened, I explained to the sponsor that, at this time, we couldn't make the relationship work. I recommended they look for another plan adviser, and I gave them recommendations."

• **Major interpersonal issues appear.** 401k Advisors' Stace Hilbrant has ended only a few client relationships in his career, usually with over-demanding, under-appreciative sponsors. "It's funny: There are a lot of negatives to having your own business, but there are a lot of positives, too. And one is that you don't have to work with nasty people," he says. "The idea of sitting down with someone every quarter and being treated poorly? I think, 'Life's too short.'"

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