



4 Advisor Compensation Plans Our Clients Use to Incentivize Reps and Drive Revenue

How you compensate your advisors is a defining characteristic of your firm. A well-designed compensation plan attracts high-performing advisors, sets you apart from the competition, and contributes to the overall financial success of your firm.

Without a clear and effective compensation plan in place, you run the risk of not complying with regulatory requirements, as well as seeing valuable talent walk out the door. That's why it's crucial that firms regularly review their compensation plans to ensure they align with their larger business goals.

If you're wondering whether your firm's compensation plan is in need of a change, here are four advisor compensation plans our clients use to incentivize their reps and drive revenue:

1. Commission-Based Compensation

Commission-based compensation is one of the most common models firms use to pay their advisors. It's a pretty straightforward way to incentive reps. It directly encourages them to increase the volume and value of their transactions, which results in higher revenue for the broker-dealer. It's also a cost-effective model, as the firm only pays reps for revenue-generating activity. And this model can also impact recruiting by attracting ambitious, confident candidates who are motivated to hit their goals and be rewarded for their efforts.

However, despite being a popular model, there are definite drawbacks to a commission-based compensation structure. One major concern is an advisor's interests not aligning with their client's interests. Commissions can potentially incentivize advisors to recommend unnecessary trades or promote products with higher fees. This potential conflict of interest is a big reason why Registered Investment Advisors, who act as fiduciaries to their clients, have exploded in popularity over the last decade.

2. Fee-Based Compensation

Fee-based compensation involves advisors charging clients a fixed fee, or sometimes a percentage of the client's assets under management (AUM). This compensation structure avoids one of the major pitfalls of commission-based compensation by aligning the interests of the advisor with those of their client. When an advisor's earnings come from a percentage of their client's AUM, that means their income increases as their client's wealth grows.

This does two things. First, it encourages the advisor to make smart, long-term investments that will lead to asset appreciation. Second, it pushes advisors to offer

great service so that their clients will trust them to manage a larger portion of their assets, thus leading to more income for the advisor.

Fee-based compensation also provides a more predictable income for brokers. This can be particularly beneficial during market downturns when transaction volumes may decrease.

However, fee-based compensation isn't immune to regulatory risks. Regulators still want to ensure clients in fee-based accounts are actually benefiting from those accounts. For example, in cases where a broker performs very few trades for a client, it can be argued that the client would be better off in a commission-based account that only charges them for the few transactions that occur. Like with the other models we'll discuss, it's still vital to ensure that your client's needs and interests are the top priority.

3. Hybrid Compensation

Hybrid compensation models combine elements of commission- and fee-based compensation. A hybrid structure allows advisors to earn fees for providing advisory services and also receive commissions for selling certain investment products. This can help broker-dealers attract a wider range of advisors and clients. Plus, the diversification of revenue streams can help firms achieve stable financial growth.

But contrary to what its name might imply, adopting a hybrid model doesn't necessarily mean you're getting the best of both worlds. In fact, hybrid models carry one potentially costly drawback: managing a complex blend of fee-based and commission-based compensation can lead to compliance issues. This may require additional disclosures and fiduciary responsibilities that would not be necessary if only one model was used.

In a recent disciplinary case brought by FINRA, a financial advisor working for a hybrid firm advised clients who had both advisory and brokerage accounts to purchase variable annuities in their brokerage accounts, despite the availability of identical advisory shares at a lower cost. This recommendation resulted in the

advisor earning a 7% commission on the sales. Subsequently, the advisor suggested that customers transfer the variable annuities from their brokerage accounts to the advisory account, leading the customers to incur additional annual advisory fees on top of the commissions they had already paid. As a consequence of these actions, customers ended up paying approximately \$594,590 in unnecessary fees.

This situation clearly illustrates a case where an unethical individual exploited their client and took advantage of the compensation system in place at their company. It is the responsibility of the firm to implement protocols that effectively manage this risk and ensure that clients receive comprehensive disclosures regarding their advisors' compensation.

4. Salary-Based Compensation With Performance Bonuses

Salary-based compensation models work exactly how you might imagine: advisors are paid a fixed amount every month and provided a bonus based on performance during a given time period. This model has declined in popularity as of late and is mostly employed within bank and credit union brokerages.

Benefits of a salary-based model include income stability for advisors, as well as the ability for firms to manage conflicts of interest by controlling which metrics contribute to advisor bonuses. Firms can incentivize business from new clients, gross dealer concession, AUM, and more.

Before committing to a salary-based compensation model, firms should consider how well this structure fits with their organizational goals. A salary-based model may not motivate advisors to grow AUM or win new clients as powerfully as commission- and fee-based models. This can be offset somewhat with non-monetary incentives like health insurance, paid time off, and development opportunities. However, these benefits can end up making salary-based models more expensive to maintain.

How EAI Can Help You Build a Winning Compensation Plan

Whichever compensation plan you determine is best for your business, your success will depend on your firm's ability to manage that plan well. With one of the most flexible and automated advisor compensation systems on the market, EAI can give you full control over every aspect of your compensation plan.

Our system is designed to allow firms to build compensation plans based on their unique business practices. This includes generating reports on the productivity and performance of advisors and branches, as well as creating customized compensation structures that align with the specific goals of broker-dealers.

If you're ready to motivate your reps and grow your business with better compensation software, schedule a demo today! We'd love to talk with you.

Learn more at:

www.eaiinfosys.com