BUILDING A BALANCE:

Scaling your business to serve plan sponsors and wealthy clients

VOYA FINANCIAL ADVISORS

IN RESEARCH

Positioning advisory firms for today's competitive environment

The financial advice business has never been more competitive, nor has it ever faced more relentless pressure on pricing. Fortunately, a decade-long equity bull market has increased the value of assets managed by advisors, thereby boosting revenue from fees based on assets under management (AUM). This has camouflaged the underlying trend in margin compression, but has not reversed it.

The current environment, therefore, provides an opportune moment for advisors to prepare for a time when markets are less favorable and pricing pressure more keenly felt. Advisory businesses can do this by concentrating on business development and organic growth fundamentals that could help them better weather a market downturn as well as prosper in the face of greater competition.

This paper will focus on the ways that two types of advisory firms can do this. First, for firms that consider themselves primarily retirement plan advisors (RPAs), a case will be made for widening their business model to include personal wealth management services. For advisory firms that consider themselves largely personal wealth and investment managers, a corresponding case will be made for adding a retirement plan advisory component to their current business mix.

Findings from *InvestmentNews* Research will be used to support these suggestions, and specific strategies will be offered for implementing them.[1]

The case for widening the RPA business model — and how to do it

In their specialized niche of serving plan sponsors with retirement plans, retirement plan advisors (RPAs) are experiencing cost pressures and competition coming from the consolidation of providers in their market segment. As solo practitioners and small RPA firms find advantages in joining forces with larger competitors, those who remain independent are finding it more difficult to acquire new business from plan sponsors as well as attract additional advisors to their firm.

Adding an individual wealth management arm or expanding a current small advice business that serves individuals can make considerable financial sense for RPA firms. *InvestmentNews* Research has found that revenue per client at advisory firms with a significant proportion of assets under management dedicated to retirement plan accounts tends to be only slightly less than that of firms with a very small share of plan clients.[1] However, it is on the profitability front where an expansion into personal wealth management can make the most sense. This is because RPAs have opportunity for increased profitability by expanding into wealth management business. According to a recent *InvestmentNews* Research benchmarking analysis, advisory firms where retirement plans account for less than 5% of total AUM tend to average an operating profit margin of 29.3%, as compared to the average profit margin of 17.2% at firms that consider themselves RPAs.[1]

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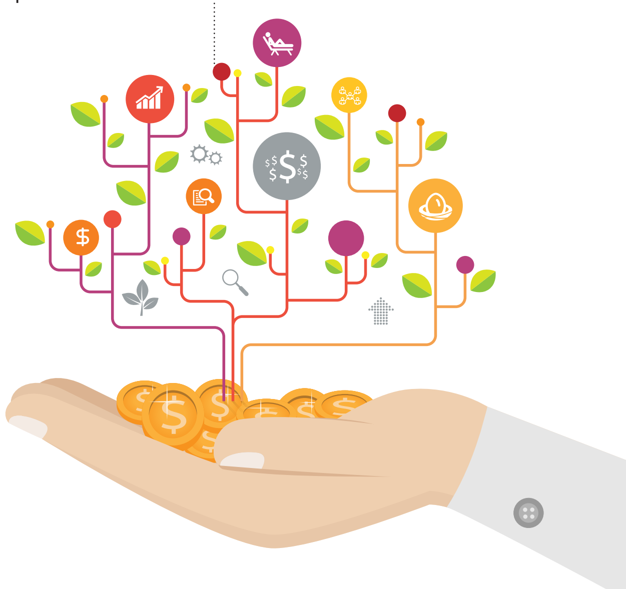

[1] *InvestmentNews* Study of Pricing & Profitability 2018, September 2018;

In addition to adding a revenue stream that is potentially more profitable, providing an individual-oriented wealth management offering, or bolstering an existing offering, diversifies an RPA firm's revenue base, making it less vulnerable to client loss and less dependent on adding new plans in the face of growing competition. Based on research that identified the services offered by different types of firms, the areas RPAs might consider bolstering include income tax planning (offered by 85% of retail-oriented advisors, but only 58% of RPAs); life, health, disability and long-term care insurance planning (84% vs. 61%); property and casualty insurance planning (51% vs. 32%), and major purchase consulting (87% vs. 55%). And while 81% of RPAs offer concierge services, an overwhelming 96% of personal wealth management firms provide such services. These service offering figures show the areas RPAs need to bolster in order to be competitive in the personal wealth management market.[1]

For RPA firms serving plans of smaller businesses, meeting the personal wealth management needs of company principals is a way to cement business relationships by providing additional, valued services. A similar, if slightly less extensive, personal wealth management offering can be attractive to long-term plan participants when they retire and, in many cases, have accumulated sizeable plan balances.

Finally, diversifying a largely RPA business model increases a firm's enterprise value, making it a more attractive candidate for acquisition and more valuable to principals should they wish to sell.

Adding or bolstering a personal wealth management business can be done organically, through hiring or through the acquisition of an existing retail business. Each approach has its advantages and disadvantages.

One organic growth path taken by RPA firms seeking to expand into the personal wealth management business is to seek the rollover business of current plan participants. That, of course, continues to be an effective course of action.

Building on that approach, firms can start by creating an appropriate compensation program so one or more current advisors can focus on attracting (as direct clients) plan participants with sizeable plan balances and perhaps significant financial assets outside the plan. These advisors can also work on attracting personal wealth clients who are not participants in plans the firm manages or advises. Since this wholly organic approach to building the business can be lengthy, RPA firms may choose to recruit an advisor, or an advisory team, that already has a book of advisory business.

Many advisors are likely to find RPA firms that seek to diversify an attractive choice. Hybrid advisors who are considering moving to the registered investment advisory model, but who don't want to go out on their own, may be receptive to an appeal from an RPA firm to join its team and build their retail business. For such advisors, moving to an established business eases the transitition to the advisory world and eliminates the need to handle the administrative and operational aspects of running an RIA business.

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The outright acquisition of an independent advisory firm geared to individual investors is perhaps the fastest, if immediately most expensive, way to build a presence in the personal financial advice business. Fortunately the demographic profile of the advisory business is likely to be supportive of such an RPA expansion into personal wealth management. Many older advisors/advisory firm principals are seeking an exit or succession strategy as they approach retirement. Selling their business to an RPA-focused firm can be an effective way for them to capture the value of their firm, as well as be able to continue to work and serve clients on a less demanding basis, an arrangement many advisors nearing retirement are seeking.

Other changes in the personal advice business can work in an RPA firm's favor. As their baby boomer clients age, many personal advice firms are grappling with how to serve milliennial investors — considerable numbers of whom have high incomes but not enough assets to merit targeting as clients on an AUM-fee basis.

Younger advisors, however, have found that subscription and retainer models can be very effective and profitable ways to attract and retain millennials. Many younger investors have expressed a desire for financial advice and a willingness to pay for it, but on terms that make sense for them. That is not necessarily an AUM-based model. RPA advisors, who likely would be less beholden to an AUM-fee model for a new venture, could find it easier to experiment and branch out using these new revenue models. However it is done, reaching out to millennials — who tend to be underserved — provides a strong basis for future firm growth.

In expanding their services, RPAs will find help in the form of new technology-based tools. Automated financial planning, as well as algorithm-based advice and investment management services, commonly referred to as robo-advice, are now offered on a white-label basis by many providers. More than half of financial advisors, according to research conducted by Voya Financial, believe that a digital advice tool would enable them to expand their practice by up to 10%. This would complement their services by providing clients with easier access to information and enabling advisors to reach younger and less affluent clients, many of whom may be under the erroneous impression that they can't afford professional financial advice or that their questions or financial situation do not warrant advisor interest. A digital offering, as well as fee-based financial planning performed by human planners, can be bolted on to the chassis of an advice business to provide a lower-cost solution for clients who may not need or want the high level of service provided by experienced human advisors, and prefer a level of service that combines human and automated solutions.

For RPA advisors unsure of how to expand into personal wealth management, many firms can provide support and resources. Voya Financial Advisors, for example, offers a range of services and investment solutions as individual components or as part of a comprehensive package, which are designed to meet the needs of high-net-worth investors with $500,000 or more to invest. These services include centralized financial planning services, portfolio construction, portfolio and goal monitoring, trust services and asset lending.

To recap, strategies for RPA firms to expand into the personal wealth management include:

- Providing full-service wealth management advice for top-level plan participants including senior managers and owners of closely-held companies.
- Offering a wide range of advice for plan participants who are nearing retirement and who have retired from full-time work.
- Adding a third-party robo-service to appeal to younger and/or less affluent investors.
- Hiring established personal wealth management advisors who can bring business with them.
- Acquiring a personal wealth management firm or practice.

Widening personal wealth management to include retirement plan advice

Just as firms concentrated on serving retirement plans can benefit from offering personal wealth management services, so too can retail-oriented firms profit by offering retirement plan services. By expanding into the retirement plan advice market, personal wealth management firms can not only increase their total assets under management, but also lock in a steady source of revenue that usually grows predictably because it is based on an asset pool benefitting from the regular contributions of plan participants.

The asset-growth potential of providing retirement plan advice cannot be overstated. Data from *InvestmentNews* Research show that recent one-year asset growth at RPA firms was 29%, versus 18% growth at personal wealth management firms. New assets from business development efforts was just 3% at those firms, but 17% at RPA firms; new assets from new clients showed a similar gap — 10% vs. 22%.[1]

For many advisors, these and other revenue and asset growth opportunities that come with the retirement plan business often outweigh the sector's typically lower profit margins. What's more, expansion into the RPA market often is accompanied by the adoption of systematized and automated processes to handle the administrative demands of the plan advice business. Greater automation and process improvement in turn increases overall firm efficiency and permits firms to benefit from the advantages of scale.

The business-to-business nature of RPA firms also helps shape an organized approach to marketing, which can have benefits for personal wealth management firms. Almost 65% of RPA firms, for example, use email marketing campaigns as opposed to just 36% of personal wealth managers. Similar differences are found in the use of social media (71% vs. 54%) and digital content (26% vs. 10%).[1]

Other advantages come in the form of synergies created by offering plan advice. Just as having a retail arm can be advantageous to RPAs by enabling them to offer advice to the principals of closely-held plan sponsors, conventional wealth management firms that operate a robust plan business are able to widen the services they can offer to business-owning clients, which can help retain those clients and perhaps help attract other business owners.

Another positive is that the large number of plan participants served creates a reservoir of potential individual clients. As those participants near retirement age, many will seek advice about rollovers, retirement income and other wealth-related issues that may not have been top of mind as they built wealth through their working years. In fact, a study by Voya Financial found that the #1 trigger for participants to seek an advisor was to get help preparing for retirement.[2] After having worked with a trusted firm that has served as their plan advisor for years, plan participants are likely to feel more comfortable turning to that same firm when seeking advice for their post-working lives. For many advisors, having access to a large base of plan participants who could become individual clients is reason enough to expand into the RPA space.

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[2] Based on findings from an online consumer survey completed in June and July of 2018 by Voya Financial with Greenwald & Associates, Inc. involving 1,000 workers over the age of 21.

Over the years, of course, many personal wealth managers have served one or two plans — typically as a result of seeing an opportunity to help a client whose business wanted to start a retirement plan or needed help in managing one. To enter or expand into the RPA space in a more determined and dedicated way, however, advisors should talk to a plan record keeper, whose job is chiefly to process employee enrollment, manage and track employee investments, log the nature of the contributions (pre-tax, Roth, employer pre-tax match, etc.), and generate the documents sent by plan sponsors to participants, including statements.

In addition to explaining the nuts and bolts of getting started as an RPA and what is required by participants and plans on an ongoing basis, a record keeper can provide information about RPA firms that may be interested in being acquired, as well as advisors who may be looking for a new home. Record keepers also can help inform decisions about the technology and software required for the RPA role, as well as share expertise on how to drive better participant outcomes.

Input from legal counsel specializing in ERISA and retirement plan regulation should also be sought to ensure that advisors understand the requirements, restrictions and fiduciary responsibilities of their role, as well as any new liabilities they may face.

To recap, for personal wealth management advisory firms considering a move into the retirement plan business, strategies to consider include:

- Acquiring or merging with an advisory firm or practice that currently serves retirement plans.
- Discussing growth opportunities with a retirement plan record keeper.
- Pursuing the retirement plan needs of current clients who may be principals of companies that offer a retirement plan or who serve in a senior executive capacity at such companies.
- Asking current clients if they participate in a workplace retirement account to help discover possible business development opportunities at companies that might create a retirement plan or that may consider a change in plan advisor.

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Takeaways for RPAs and wealth management firms

Venturing into new territory can be challenging for advisors — but so too can be sticking with a business model that is coming under increasing pressure. For RPA firms and personal wealth management firms exploring each other's area of expertise for possible expansion, it's important to remember that the similarities outweigh the differences. Successful firms in each camp place emphasis on the fiduciary nature of their relationships, the importance of treating clients and plan participants ethically, and the value of raising the level of financial wellness and understanding among plan participants and clients through education and comprehensive financial planning. Affiliating with a broker-dealer offering a strong 401(k) program and expansive record-keeper experience and resources provides a deeper level of support that can make a difference for RPA and personal wealth firms alike.

By building on these commonalities and taking careful and prudent steps to widen their businesses and by adopting a core part of each other's model, RPA-oriented advisors and wealth managers alike can increase revenue, profitability and enterprise value.