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Death by Benchmarking (Compensation)
DALBAR Introduces Profit-Based Pricing Model Calculator to Avoid Fee Compression

(Boston, MA. April 20, 2016) As part of the Best Interest Contract Exemption (BICE), advisors are prohibited from making recommendations that will cause compensation for their services that is in excess of reasonable compensation. Unintended executioners of the advice industry have proposed to determine reasonable compensation by calculating an average or median compensation benchmark. This will inevitably lead to unlimited compression of compensation – death by benchmarking.

Fortunately, there are alternatives and the DALBAR Profit-Based Pricing Model Calculator answers the BICE requirement that “no more than reasonable compensation is paid for the services.” The Calculator was developed to extend the boundaries of traditional AUM pricing in which clients are charged an arbitrary basis point fee that is independent of the cost of servicing that client. It permits the advisor to determine and set a price that makes each client profitable based on the advisors skills, costs, time, expense, overhead and risks.

“There is no reason for advisors’ compensation to decline just to remain compliant. Section II(c)(2) requires ‘reasonable compensation’ not benchmarked compensation,” said Cory Clark, Head of Research and Due Diligence at DALBAR. He added “With the Calculator, advisors can account for the time and resources needed to deliver the specific services that clients elect to use and the basis for the pricing can be explained and understood by clients.”

Implementing the Calculator makes every client profitable, replacing the current practice of having winners pay the way for unprofitable clients. Results from three clients¹ with the same assets (\$1.5 MM) and portfolio composition illustrates this:

Low maintenance (10 hours per year)	\$6,660 or 44 BPS
High maintenance (40 hours per year)	\$31,279 or 209 BPS
High service –ERISA plan (20 hours per year)	\$23,459 or 170 BPS

The calculator for computing reasonable compensation is included in DALBAR’s training course on BICE and can be found at <http://training.dalbar.com>. A stand-alone version is planned for release later this year.

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¹ Details of these examples are available on request.