



# Trends in Wholesaler Compensation



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## Executive Summary

Beginning in the mid- to late-1990s, the asset management industry entered an historic period of unprecedented growth. New money flowed into investment products faster than ever before. For asset managers, acquiring new assets was like shooting fish in a barrel. Since that time, however, attracting new assets has grown increasingly difficult. As a result, asset retention has become more and more important.

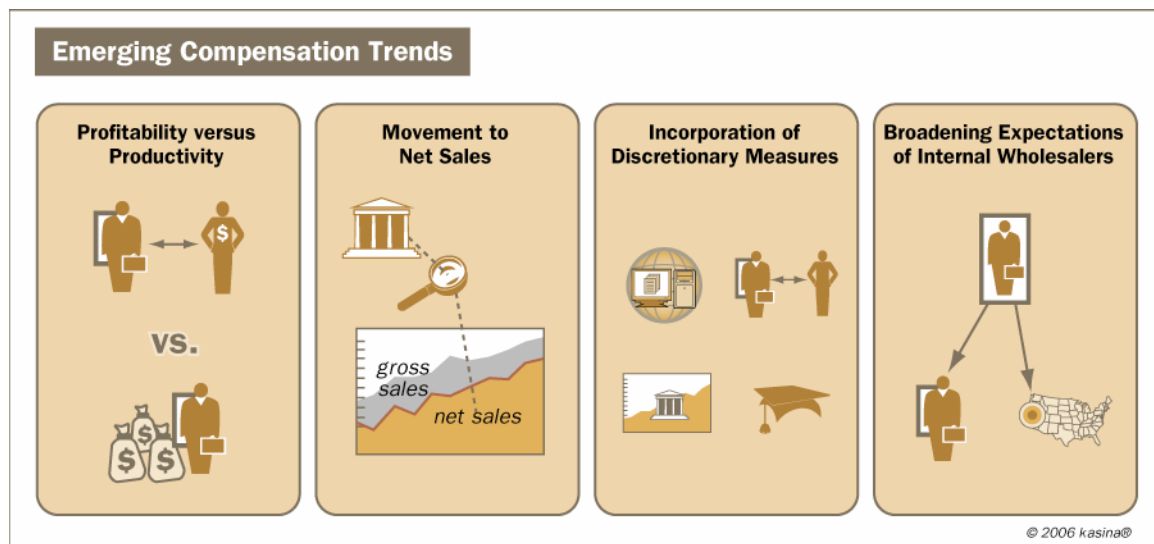
Despite this change, compensation models across the industry have remained more or less the same. Overall production and new asset acquisition are the predominant drivers of wholesaler pay among most industry firms, and compensation levels vary significantly across firms and according to specific roles.

As competition for assets intensifies, senior Sales executives are beginning to sense a widening gap between firm objectives and wholesaler goals. Firms are recognizing that the manner in which wholesalers are compensated must change to reflect the industry's new competitive dynamics.

Among the primary drivers of change in compensation models are:

- **Profitability** – firms are moving closer to Intelligent Distribution, a strategy characterized by a shift in emphasis from sheer assets to profitable relationships
- **Asset retention** – realizing that new inflows to asset management products are down, firms are focusing on retaining assets already under management

In light of firms' emphasis on these considerations, a set of trends is emerging that stands to impact wholesaler compensation in the near future. Foremost among these trends are:



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## Sample Snapshot

### Role-Specific Compensation Practices

This study describes the current compensation practices for four primary wholesaling roles, briefly defined as:

	<b>Externals</b>	Wholesalers operating in the field with responsibility for sales to specific territories, firms, or advisor types
	<b>Hybrids</b>	A cross between internals and externals, hybrid wholesalers generate sales from within the home office with limited travel or administrative support
	<b>Internals</b>	Wholesalers responsible for administratively supporting the efforts of externals while, in some cases, balancing territory sales responsibilities
	<b>Regional Sales Managers</b>	Sales managers responsible for overseeing regional teams of wholesalers

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Most firms have external wholesalers, internal wholesalers, and regional sales managers, although firms vary according to the layers of sales management present in their wholesaling organizations. Firms also vary in the extent to which they have introduced a hybrid wholesaling role. Only a few firms have established a well-defined hybrid wholesaling role that is truly independent from internal and external wholesaling roles.

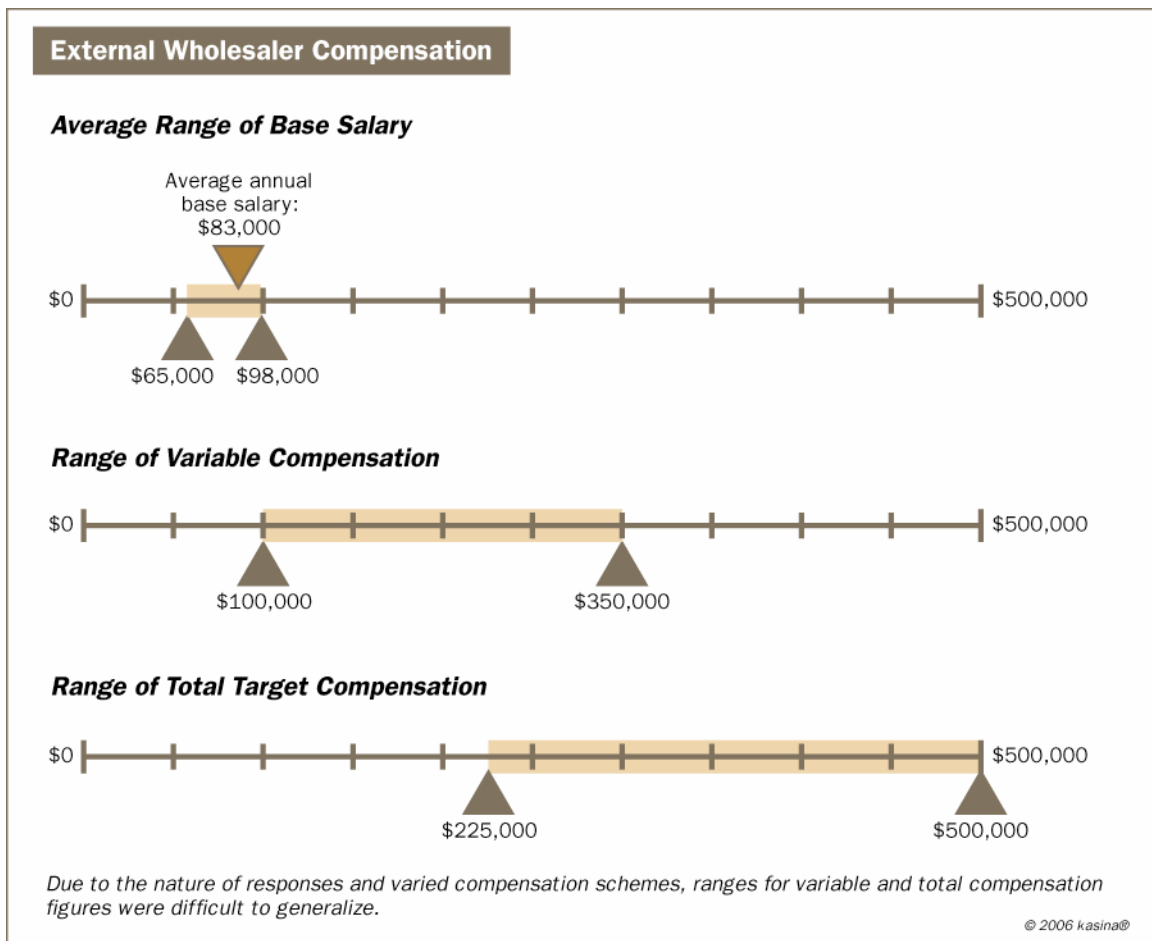
In some firms, however, internals who are responsible for territory sales are not given the title “hybrid wholesaler,” despite maintaining a hybrid set of responsibilities. For purposes of this study, hybrids are defined as wholesalers who are office-based and responsible solely for territory sales, with no element of compensation based on administrative or sales support of external wholesalers.

#### External Wholesalers

Externals typically receive an average annual base salary that ranges from \$65,000 to \$98,000, with an average of \$83,000. Relative to hybrid and internal wholesalers, externals receive the highest base salary, though it generally represents a smaller portion of their total target compensation. Total target compensation can range broadly from \$225,000 for an average-performing wholesaler to over \$500,000 annually for top performers.

### *Variable Component Comprises Majority of Total Compensation*

Most of externals' total pay is derived from variable compensation, which can range from \$100,000 to over \$350,000 annually, depending on a given wholesaler's performance relative to established sales goals. Variable compensation is driven primarily by individual sales commissions. In awarding commissions, most firms pay basis points on gross sales. Another approach, placing greater emphasis on asset retention, involves paying basis points on net sales. Only one firm interviewed for this study uses this approach.



### *Variety of Factors Govern Basis Point Payouts*

The factors governing basis point payouts on individual sales vary from firm to firm. However, the two most predominant factors are:

- **Product profitability:** Many firms seek to drive sales of profitable products by varying basis point payouts according to product profitability. For example, a firm specializing in annuities products pays wholesalers up to three times more basis points for its variable products than for its fixed annuities. While this

approach is common among firms interviewed for this study, one of its opponents stated that suitability issues have prevented his firm from adopting it. As he put it, "What if the best product for a given advisor client is one of our lower margin offerings? Will wholesalers feel inclined to recommend it, knowing the impact it would have on his or her variable compensation?" Despite this concern, most firms view assigning higher basis point payouts for more profitable products as one way to align wholesaler goals with firm objectives.

- **Advisor type:** Firms also use basis point payouts to focus wholesaler efforts on specific advisor types. Firms generally segment advisors according to one of two criteria, channel (e.g., national wirehouse, regional, independent) or relationship with the firm (e.g., emerging prospect, existing client). In an example of varying basis point payouts by advisor channel, one firm pays up to six basis points more for sales of equity mutual funds to the wirehouse channel than to the bank channel. Another firm pays an additional two basis points on sales to advisors with important emerging focus firms.

On top of individual sales, some firms award commissions on territory and, in rarer cases, company-wide sales. These broader incentives generally represent a smaller but additional source of variable compensation for wholesalers.

- **Territory sales:** In addition to paying wholesalers 14 basis points on the net cash flow of clients they control, one firm also pays wholesalers four basis points on the region's overall net cash flow. In this model, wholesalers' median variable compensation ranges from \$175,000 to \$200,000 annually, with top performers earning up to \$350,000.
- **Company-wide sales:** To reward top performers, firms will sometimes set aside a separate bonus pool for wholesalers who exceed their individual sales goals for a given period. In one such example, a firm sets aside one basis point of its total gross sales for the year, paying it out to wholesalers based on the margin by which they exceeded their individual annual sales goals.

Other variations in awarding basis points include the frequency with which they are paid and the extent to which payouts are capped, or reduced, upon achieving a certain individual sales threshold.

- **Payout frequency:** While most firms pay commissions quarterly, semiannually, or annually, a few firms pay them monthly. In the most interesting example of this approach, a firm distributes annualized basis point payouts on a monthly basis. Wholesalers receive monthly commission checks based on their projected annualized performance against annual sales targets. The major downside of this approach, as a senior Sales executive with the firm conceded, is the volatility of wholesalers' monthly commission checks. However, the firm has found that

rewarding its wholesalers in this fashion keeps them motivated from month to month.

- **Capping payouts:** Seeking to limit compensation expense, a few firms interviewed place a cap on wholesalers' total potential sales commissions for the year. In one firm, for example, wholesalers who reach their annual sales target receive the maximum basis point payout, but are then ineligible for additional payouts for exceeding their goal. Of question with this approach is the behavioral impact on wholesalers who achieve their sales goals early in the year. Under this structure, wholesalers are left with little in the way of compensation incentives to continue generating sales for the remainder of the year. In another model, one firm cuts basis point payouts in half after wholesalers achieve their sales goals for the period. In this situation, too, the firm seeks to limit its compensation expenses at the risk of de-motivating wholesalers. This practice was only observed in firms that pay basis points on gross sales. In net sales arrangements, firms typically do not limit wholesalers' upside sales commission potential because net sales are more closely correlated to profit growth than gross sales.

### *More Firms Introducing Discretionary Elements*

While sales commissions comprise the vast majority of externals' variable compensation, more firms are starting to consider and, in a few cases, introduce discretionary elements to their variable compensation models. By incorporating a discretionary component, firms hope to reward wholesalers who take all of the right steps to generate sales but are, for a variety of reasons, not yet seeing the results of their efforts.

To demonstrate the rationale behind incorporating a discretionary element, one executive cited a wholesaler tasked with selling a newly launched product. It requires more of a wholesaler's time and effort to build awareness and understanding of the product among advisors, and the firm wants to make sure that wholesalers are rewarded for doing all of the right things to ultimately sell the product. Another example, used by the same executive, involved a wholesaler who had been assigned a new territory. Obviously, as the executive put it, the firm wanted to assign important new territories to its best wholesalers, but they needed to make sure that the wholesalers were provided incentives in spite of the initial difficulty of generating sales.

Discretionary bonuses often represent a small portion of externals' total variable compensation, paying, on average, between \$20,000 and \$50,000 annually. In most cases, discretionary bonuses are easily attained by average performers. One executive used the term "economic welfare" to describe his firm's discretionary bonus because almost every wholesaler received it. In other words, it was not awarded on a truly *discretionary* basis. Current implementations of discretionary bonuses fall short of achieving their intended objective: rewarding the best wholesalers for planting the seeds of future sales within a new territory or distribution partner, or in support of a newly-launched product. This issue is discussed again later in this study.

### *Externals' Compensation Primarily Driven by Sales Commissions*

In summary, external wholesalers receive an annual average base salary of just over \$83,000, but most of their total annual compensation is derived from sales commissions. On average, externals can earn between \$100,000 and \$350,000 annually, depending on how they perform with respect to their sales targets for the year.

In terms of how commissions are calculated, most firms use basis points on gross sales, while a few using basis points on net sales. A variety of factors, including product profitability and advisor type, govern how basis points are ultimately awarded. Currently, only a few firms have incorporated a discretionary bonus to reward wholesalers for taking the right steps to develop profitable relationships. Ironically, current implementations of discretionary bonuses fail to reward *only* those wholesalers who embrace best practice behaviors.