



Approaching the Underserved Middle-Market: Insights from Planners

A summary of focus groups with financial planners at the Financial Planning Association 2012 Retreat in Scottsdale, Arizona on May 6-7, 2012

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Many surveys of America's middle-market have found that this market is vastly underserved when it comes to financial planning, services and products. Such individuals have little savings and little or no access to, or use of, financial services and products that help foster financial security. As a result, many of these households are ill-prepared for retirement as well as for the many financial demands they face before retirement. How to turn this situation around is becoming a top financial industry priority.

In early spring of 2012, the Society of Actuaries, the Financial Planning Association (FPA) and the International Foundation for Retirement Education (InFRE) decided to co-host some focus groups to study the problem. The group participants were FPA members who have experience with serving the mid-market. The goal of the sessions was to learn how advisors are reaching out to this market and to uncover the roadblocks that they think are deterring greater mid-market use of financial services. The planners were also asked to suggest strategies that could help increase mid-market access to financial advice and products.

The planners' responses provide telling insight into the problems and opportunities that lie ahead for financial professionals, actuaries, educators and others who want to see this market expand. Some of the key points follow.

I. Planner Profiles

The planners in the focus group each provided an overview of their firms. Several included their own definition of the mid-market when outlining their firm's financial activities. It is striking to see that there was not a common understanding of the mid-market among these individuals. Here are examples:

Planner 1: This planner defines mid-market as \$100,000 or less in assets. She does corporate benefits and meets with lots of people.

Planner 2: The firm where this planner works bases its definition of mid-market on career level. It serves commissioned and noncommissioned officers in the military, with \$60,000+ in income, not including benefits.

Planner 3: This planner defines mid-market as having investable assets in the range of \$250,000 to \$1 million.

Planner 4: This planner defines mid-market individuals as having as \$250,000 to \$500,000 in investable assets. This is a new firm, so the planner could not offer a percentage of how much of current business is currently mid-market.

Planner 5: This planner said the firm sets fee scales based on age demographics. The profile does not include a mid-market definition.

Planner 6: This planner has spent 34 years in financial planning. One-third of clients are now retired, the planner said, adding that a wave of retirees from first generation is expected.

Planner 7: One-third to one-half of this planner's clients is wealthy. He said the firm sets no minimum requirement on wealth.

Planner 8: This planner described the mid-market as the children and grandchildren of current clients. The firm has also picked up parents of clients. In this practice, advisors view the mid-market as a loss leader.

Planner 9: At this firm, the planner has a CFA for a business partner, and they manage account sizes ranging from \$500,000 to \$5 million. A younger planner they have hired for their firm's succession plan is the one who is working with mid-market clients.

Planner 10: This planner said mid-market clients are those with less than \$5,000 in annual investment income. Ninety-five percent of the firm's clients are in this category, he said. They are located in 22 states, and three clients have more than \$1 million.

Planner 11: This planner said the mid-market centers around people with \$100,000 to \$250,000 in investable assets. The firm provides services to them for a fee.

Planner 12: At this firm, the average account size is \$120,000 to \$130,000. It has 900 clients, and provides retirement plans for employees.

Planner 13: This firm targets seniors, particularly older women, and military. The planner said it provides bill paying and advice to these individuals, whose investable assets average around \$200,000.

Planner 14: Here, 90 percent of all clients have \$100,000 to \$1 million in investable assets, and the wealthiest has \$4 million. The planner said that all clients "worked" for their living and are very much middle class. The firm provides income tax, estate planning, and financial planning services. The client base includes a lot of 20-30 year olds, the planner added, and some clients don't manage their assets at all.

Planner 15: This firm also has 90 percent of clients with \$100,000 to \$1 million in assets. The planner commented that the clients have an overall lack of appreciation for how “things financial” work, so the planner believes that education of the client is crucial.

Planner 16: This planner partners with a wealth management firm. One-half of the clients have \$10+ million in net worth, while the other half is mass affluent, with a net worth of about \$300,000. This planner has a lot of passion around the mid-market and the importance of helping the planning profession serve this market.

II. Definition of middle market

Definitions varied on whether the market account values are asset or income based, but they include individuals who have regular income and no accumulated assets as well as those with several hundred thousand in investable assets. This is a brief summary of the definitions they provided:

- \$100,000 or less in assets
- Based on career level. The market includes people with \$60,000+ in regular income and no accumulated assets
- \$250,000 to \$1 million in investable assets
- \$250,000 to \$500,000 in investable assets
- \$100,000 to \$250,000 in investable assets
- \$200,000 in investable assets
- \$100,000 to \$1 million in assets
- Those with less than \$5,000 in annual investment income
- Children of high net worth clients—a feeder program for future assets under management
- People that don't meet current minimums but have future potential—also a feeder program
- People with limited assets; this includes people at all career stages, but needs vary by career stage.
- Employees of benefit plan clients. This includes specialized groups such as military. For people who are not yet retired, the bulk of financial assets are likely to be in the 401(k) plan.

Needs of the mid-market:

- Spending more than people can afford is a common issue. Help with managing spending is critical to getting mid-market clients on a track toward saving and lifetime financial security.
- Credit card debt is an issue.

Views of planners who actively target the mid-market:

- Thirty-six percent of one focus group said they actively target the mid-market.
- The planners said the mid-market is typically thought of as unprofitable.
- For many years, planners have received calls from people with no investable assets, but with good incomes. Some said they basically refer those calls out.

III. Business models for serving the mid-market

Overall:

- Focus group members included both fee-only and fee-plus-commission clients.
- Many agreed that they provide the first meeting free, but do not give advice.
- Planner use of electronic data submission depends on age of the client. Younger clients tend to like electronic.
- Planners said they need volume to make this business profitable. One said that, when first starting in this space, the planner took on 10 new clients a month, or 100 a year.

Business models:

1. *Hourly.* Planners use the hourly approach on an as needed basis. There is no retainer and therefore no client expectation of monitoring. It's important not to have open-ended hourly fees, the planners said. Clients want to know what something will cost in advance. Hourly rates that are too high are a problem. One planner requires a deposit of 50 percent, up to \$500, up front, and refers out to others who can implement with product.

2. *Flat fee.* One example of this approach is to offer a \$600 financial checkup for three hours, face to face, plus 45 minutes of outside work. In these cases, the client provides documentation ahead of time. The client can ask three major questions, all submitted ahead of time. Clients like the fixed/known cost, the planners said. In this model, the planners provide choices on how they can be hired—on retainer, based on assets under management; per financial checkup; or hourly.

3. *Commission.* Planners said they use this model for clients with \$60,000+ in income and no assets. The work focuses on rearranging cash flow by decreasing tax withholding and helping reduce debt payments so funds can be re-channeled into savings.

4. *Hybrid.* Planners who use a hybrid model charge a fee based on assets under management for anything above \$250,000 in assets, but use commissioned products for those with under \$100,000. They do a financial plan for every client, even if it's a short report that spells out when they can afford to retire and how to boost duration of retirement assets.

5. *Good, better, best service level.* One planner who uses this model segments clients into three, first-year planning brackets; for work in subsequent years, the cost is 60 percent of the first-year fee. Another provides five planning service choices A-E (like Medigap policies) where additional services build on a base: Plan A covers the foundation; Plan B adds more services; Plan C adds investment management; etc. Some clients “graduate” and can do basic things on their own.

6. *Monthly recurring fee.* This model runs like a gym membership (\$125/month). Once 40 people are enrolled in this system, the firm can hire a younger planner to take over those clients. There is no minimum requirement.

IV. Planning approaches

Some planners said they seek to help clients’ overall situation whereas others said they address single issues. There is substantial variety in how they accomplish this, but most indicated that efficiency and technology are important factors. Here are some of the models:

1. Focus on efficiency approach

Efficiency is critical in the mid-market, the planners said. Some said the employer market is a great vehicle for reaching the mid-market efficiently. Here are some suggestions they had for achieving efficiency.

Don’t provide a big book financial plan. In the first year, hold eight to 10 meetings with new clients and fewer thereafter. Work in three distinct “seasons” (prepare tax returns, help set goals, and every third year, update the investment policy statement and estate plan). Make the meetings action-oriented. For example, in meeting on a 401(k), do the asset reallocation during the meeting rather than discussing how it will be done later. Hold meetings in person, online or by phone. To decrease the cost of data gathering, use Money Guide Pro, Junxure or other software products that do screen scraping to aggregate online data.

Have support staff prep and process data and information before and after meetings. A staff of 12 can create full plans and do 650 reviews a year. Setup repeatable processes so things don’t get dropped; those processes allow lower level employees to help provide service (think: “wash, rinse, repeat”).

Use almost no paper. For instance, have clients fill in a PDF of their annual tax planner. Teach the client how to enter data, such as current year tax data. Provide tax returns to the client on a CD. Keep all data on a platform that can be viewed by the individual and the advisor.

“Most middle market issues can be handled without research.”

In sum, the mid-market needs streamlined, disciplined processes where clients input data and/or there are account aggregation tools that really work. If data gathering is automated, then the system can spit out the plan and the planner can focus on providing the advice. The value that the advisor plays is not in creating the plan, but in helping the client take action and steps needed.

2. Cash flow management approach

The mid-market is all about cash flow management, not wealth management, the planners said. So, rearranging cash flow appropriately builds wealth. Some suggestions include the following.

Take on mid-market people when they don't have wealth. That will help grow future business in this market, since clients will typically stay with planners who helped them when they had only modest sums to manage.

The more comprehensive the approach, the better the assets grow and wealth accumulates. Some mid-market clients arrive to the planner's office with a government paycheck and benefits but no cash. The planners said they review risk management, life insurance, long-term care, property and casualty--all the risks that can derail a plan.

"Debt management is a huge issue for some people in this market. It is about cash flow management rather than asset management."

Put mid-market people on a path that includes savings. This is very important, the planners said. Suggestions for doing this include changing the tax withholding and helping clients reduce debt, so clients have more money available for savings.

Focus on key aspects of mid-market. These include housing, cash flow and risk management, guardianship for kids, how to pick 401(k) investments, and quarterly rebalancing. Start with an upfront plan that they buy separately and then provide them six to eight hours a year thereafter. For clients with under \$100,000 in investable assets, put the money in an asset allocation fund. The clients may break even or lose a little the first year but they will be on their way to growth long term.

3. Modular planning approach

Most of the problems faced by mid-market have been seen many times before. Mid-market clients generally don't need 10 hours of prep or a full financial plan. In fact, mid-market clients won't show up to get a full financial plan. They say they want an answer to a problem. Planners can respond by offering a modular planning approach. Such plans are not messy. It's a matter of diagnose, prescribe, and implement. Suggestions include:

Set up processes for common types of clients ahead of time. Slot clients into an appropriate process. Focus on driving to actionable steps by the end of a meeting.

Use software that has a built-in structure that can help with this. For instance, a software program might divide expenses into "past money, current money, future money." That helps clients focus on the issue and helps the planner move to action.

Create a replicable system that can be individualized. Registered investment advisors (RIAs) are not restricted and are able to do what is needed when needed. However, in the broker-dealer world, compliance issues can overshadow or override the process at times, as when the full process isn't needed.

Provide a menu of services that are “one-off projects.” Alternatively, offer different service packages with a fixed price list. While some individuals will come back for more service, this approach means there is no continuing service until there is a new engagement.

Reminder: It is more important to manage client behavior than to focus on investment results. But eventually, many of these clients will have acquired assets that need to be managed, and they will need other services, too, as their assets grow.

Other versions:

- *Pain point or as needed approach.* This is another version of a modular approach. For instance, everyone needs to do tax returns, and some clients will want the planner to handle this. Firms differ as to whether they offer this service.
- *One topic approach.* Here, the planner uses a single-page retirement plan spreadsheet. This presents all key facts about the client’s retirement situation and resources. For some clients, this is very helpful.

4. Flat recurring fee plus client data entry approach

Under the flat fee model, one planner puts clients on a \$600 flat fee minimum retainer for a three-hour meeting to address up to three issues. This is a special engagement, in which the planner expects to spend an additional hour or two preparing for the meeting.

Another version of this is a first-year fee level. Here the planner charges \$4,500 to \$10,000, depending on the complexity of the situation and an annual fee thereafter that equals about one-third of the original fee.

This approach does not entail a “big” comprehensive plan. The planner meets with the client six to eight times in the first year and three times a year thereafter. These meetings can be in person, online, or by phone and they are linked to specific issues. Tax preparation is included.

First-year topics include: data entry how-to’s, tax preparation, review of insurance, review of spending, 401(k) check-up and reallocation of assets during meeting.

Variations:

- *Separate, streamlined organized process.* Here, the planner develops a plan in year one and then, for a monthly fee of \$125 after year one, offers highly automated services, with the client entering the data. Some advisors in the firm focus on handling this book of business. This can be good for newer advisors.
- *Organized process that is tailored to segment needs (e.g. military).* In this model, clients enter their own data. The planner’s service package includes focus on spending and managing spending, insurance, learning to save and debt management. Highly automated tools and special services including bank and debt management service. The planner earns commissions on insurance products sold.

“Without organized processes, firms can’t effectively serve middle market clients”

5. Use home equity to cover basic expenses

Reducing the cost of housing may be important as people near retirement as well as at other times in life. When this is the case, the planner-client discussions are around how the size of the house fits current and future needs. Does the client need to downsize, perhaps to less expensive housing? Is the client concerned about retirement security? If so, managing home equity is central to achieving that security.

Mortgages generally should be paid off before retirement, the planners said. Some felt housing is not a spendable asset; most said they prefer to keep home equity as asset of last resort.

However, some planners said they are using reverse mortgages to help those with limited other assets in retirement. For instance, one planner reviews whether a reverse mortgage is suitable for a client who needs to pay for insurance, taxes, and other necessities.

V. Risk management and the mid-market?

Insurance is a time-honored tool for risk management. Here, clients transfer the risk insured against to an insurance company in exchange for payment of a premium. Most mid-market people need insurance, the planners said. In fact, insurance is the traditional entry point for planners who enter the mid-market market.

Example: For clients who want to retire, the biggest hurdle may be lack of availability of health insurance, which protects against the expense of suffering serious health problems. Since availability of health insurance is critical to deciding when to retire, the planners recommended discussing the health insurance early in the retirement planning process.

“Middle market clients need insurance.”

Other challenges include possible disability and need for long-term care, and the cost of insurance to help pay for this care.

Insurance. Insurance issues like these are so important that one planner said the longest review meetings often entail changing the insurance limits and deductibles—an activity undertaken to uncover dollars that can be used to achieve client goals. For some mid-market clients, debt management is also big risk management issue. This is key to client security longer term, according to one planner.

Long term care. Regarding managing the risk of a long term care event, the planners agreed that this is a big risk. However, they said they would not automatically recommend long term care insurance, because the cost now and in the future can be prohibitive in the mid-market. They said their approach here is to discuss the issue and see where it goes.

Longevity. Where longevity risk is concerned, the planners pointed out that software is available that can help with projecting retirement income. However, they added that much of the software primarily

addresses how to accumulate assets for retirement, not how to take distribution of those assets during retirement. In addition, they said the software tends to lack effective modeling of risk in the areas listed above—areas that are critically important for the mid-market. The advisor needs to be selective.

Defined contribution planning. What to do with money in defined contribution plans, such as 401(k) plans, is extremely important for many people in the mid-market, the planners said. That’s because, while most mid-market people that planners see do not have defined benefit pensions, the clients do have defined contribution plans. To help such clients, the planners said they often use a one-page organized statement of the client’s retirement situation.

“401(k) distributions at time of retirement are more money than people have ever had, and they need help deciding how to manage that money.”

Older client challenges. Risk management also entails deciding how to serve older clients in the mid-market. These clients may be uneducated but may have lump sums that they do not know how to protect or manage. They may want help but may not feel comfortable working with planners who are younger than they are. That can create problems because the younger planners are often the more cost-effective solution for serving this market, the planners said. Firms need to work on this.

Considerations:

- Keep in mind that wealth management versus wealth accumulation are two separate businesses, the planners said. Eighty percent of people who call for a free initial consultation are wealth accumulators. When accumulator clients come into the office, the planners said they focus on making sure that the client’s risk management plan is in place.
- Use educational tools like the Society of Actuaries Decision Briefs, the planners suggested. The Briefs are topical articles about various decisions that people need to make as they approach and enter retirement. Planners can give the Decision Briefs to clients as a risk management resource and/or as a value-added tool that reinforces points made during the planning meetings.

VI. What do planners need from technology to make serving the mid-market more profitable?

Technology tools do not automatically translate into more profits, the planners said. But the tools allow planners to drive down to the asset levels that they can service.

Clients differ greatly in what is comfortable for them, the planners noted. For instance, social media heavily influences the technology that Generations X and Y consider to be comfortable. Planners said they can often provide their NextGen clients with a lockbox program or uniform application programming interface (API) that allows clients to add their own data and also provides the advisor with access.

On the other hand, many older clients simply avoid technology, the planners said. This is due to security or other reasons. One method planners are using to address this concern is to use meeting time to work in system together with the client and to teach clients how they can do that on their own.

However, most people will not go into a system to handle transactions, said one planner.

Integrated automated platforms are extremely important, the planners said. One suggestion for improving the user experience in this area is to try registering a data-collection process with a website like Mint.com and then passing the baton to the client to populate, they said.

“Technology allows the client to input information, and both client and planner can look at it.”

Here are some technology-related features that the planners predicted will be important in the future:

- Automated tools to provide much of the information needed
- Aggregator systems that automatically update account balances
- Systems that require clients to do their own data input to keep costs down
- Technologies that allow client and advisor access to data maintained in a secure environment such as Mint.com, AllAccounts.com, CashEdge.com, and Juncture
- Structure information so that it is easy to use and understand by both parties, and is usable directly in meetings
- Systems that enable documents to be readily available on a system for the planner and/or client to review
- Electronic communications that can supplement meetings
- Technologies that enable online meetings
- Software technology that is able to speak with other programs and transfer data readily from one package to the next

Organized systems feature many of these characteristics today and they will grow in importance, the planners predicted. Some newer firms—such as Veritat—have already redefined their processes to make them much more efficient.

Placement of webcams in all offices has introduced new efficiencies. The planners said they have noticed that meetings don't take as long. Many couples' meetings that used to get cancelled are no longer cancelled.

Also, the ability to make changes to 401(k) asset allocations or deferral levels right in the office, while meeting with the client, has been an important help in executing plans, the planners said.

VII. What will help make working with the mid-market more profitable?

1. One issue that needs to be addressed is the regulations coming out of Washington, the planners said. The ERISA regulatory environment is the biggest impediment to getting employer sponsorship so that

planners can help employees with their retirement plans. However, employers are ultimately afraid of liability if they offer planner services as a benefit to employees.

2. The new fee disclosure rules might shut advisors out of the 401(k) market, where participants are largely mid-market customers, the planners pointed out. The fee cost will show up on the employees' statements, but not on statements directly from mutual fund companies. The problem is, employees may stop using the 401(k) plan if they think they won't pay any commissions by buying a mutual fund outside the plan. To avoid misunderstandings, there will need to be a huge education effort, the planners said.

3. Some planners are walking away from the employer market because of the new regulations, and there is no groundswell of planners who are trying to get in, they pointed out

4. In a couple of years, research will be needed on how well the new regulations have helped participants and whether the regulations have added to, or cut back on, advice and help offered to employees. Perhaps the Financial Planning Association can provide this research, the planners said.

5. Planning firms need better ways to identify which level of planner should meet with clients, the planners suggested. One suggestion is a system that matches client needs to planning skills and sets appropriate costs for providing advice. It might recommend using a planning team, for instance, so that expertise can be shifted from the lowest cost denominator only when needed.

“New entrants into the market are doing some processes at a fraction of the traditional cost.”

6. Addressing the planner's role in the 403(b) market also needs attention, the planners said. But with all the additional regulations now coming out, this could not be a near term. Put it on the longer-term agenda.

Putting it together

Clearly, the financial planners in the focus groups hold varying views on the financial profile of mid-market individuals and how best to serve them. Some see this market as referring to people who have accumulated \$100,000 or less in investable assets, while others use a higher the maximum—of \$500,000 or even \$1 million.

Most planners in the focus groups indicated they think it best to find efficient systems and technologies that enable them to serve this market economically, but some also recommend developing comprehensive plans, at least at first. Some take a cash flow management approach to mid-market services, while others take a modular approach. Some use fees while others work on insurance commissions or a combination of fees and commissions. Some don't use home equity as a financial funding vehicle except as a last resort while others will entertain using reverse mortgages in certain types of situations. Some position insurance as part of the risk management program, and some view insurance as the door-opener to mid-market client relationships.

What seems universal is the fact that financial planners see the mid-market as a distinct financial demographic. Because mid-market clients often have modest or moderate asset profiles, planners are developing distinct business models that will enable them to serve these clients efficiently. They want their services to be affordable for the clients and profitable for the planning firm. Challenges remain, such as federal regulations and fee disclosure rules. But the planners indicate they are continuing to look for ways to serve this market effectively.

Sources: These summary notes were prepared by Anna Rappaport, principal of Anna Rappaport Consulting, on behalf of the Society of Actuaries; Jaleen Edwards, on behalf of the Financial Planning Association; and Betty Meredith, director of education and research for the International Foundation for Retirement Education (InFRE), on behalf of InFRE. All were observers of the focus groups. The focus group facilitator was FPA Board Member Julie Littlechild.