Designing an optimal compensation program

Investment News

The cost and complexity of developing effective compensation programs for advisory firm employees represents an ongoing challenge for firm principals. A successful approach to the issue is to focus on a top-down, strategic approach to compensation rather than bottom-up approach designed at the individual level.

That was the suggestion of IMPACT speaker John Furey of Advisor Growth Strategies, who focused on compensation and equity plans that he believes can drive excellence, not entitlement.

Furey noted that since many advisory firms develop from one- or two-person businesses that gradually add staff, owners of growing advisory firms may wake up one day to find their compensation and equity plans are not reinforcing desired behaviors, but instead are rewarding people for tenure or for work that is only tangentially related to firm performance.

"Firm leaders should articulate the firm goals, and then define how employees will help the firm reach those goals," Furey said. "Leaders also should be clear about desired behaviors, and be willing to link roles to the firm's growth plan."

Essentially, establishing roles and responsibilities, as well as clear career paths, helps remove a lot of the compensation confusion. Also important, Furey said, is not over-relying on either a base salary plus bonus plan or a revenue-sharing plan. With the former, he said, firms can wind up with some employees whose compensation is too generous by market or performance standards; over-reliance on the latter allows some employees under favorable conditions to capture too much of a firm's upside.

"The answer is to create targets and activities that give employees the ability to materially increase earnings over time, but also shares risk," Furey said.