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6 Wirehouse Comp Trends to Watch in 2023

Industry experts predict grid changes and a continued focus on team compensation for next year.

By Jeff Berman | December 12, 2022

There were few significant changes made to compensation at the wirehouses this year, and there likely won't be many major changes in 2023 either, outside of tweaks already signaled by Merrill Lynch in recent weeks, according to advisor compensation experts interviewed by ThinkAdvisor over the past few weeks.

Two of the three experts we spoke to predicted we would see a continued focus on both advisor team-based compensation and encouragement of fee-based revenue versus transactional revenue.

But they were split on whether we should expect wirehouses to change their comp grids. Before the pandemic, such changes were typically a yearly occurrence.

Below are the experts' top expected changes for 2023 compensation.

1. There could be a return to grid changes in 2023.

"Since we haven't seen too many grid changes the last few years, I would expect the firms to consider increasing grid level thresholds (i.e., moving up the requirement to get a certain payout)," according to Louis Diamond (https://www.diamond-consultants.com/team/louis-diamond/), president of Diamond Consultants.

"The rationalization would be inflation and increased costs to operate the business since the costs of professionals across the board have risen," he told ThinkAdvisor.

Merrill Lynch "altering its growth grid … has been wildly unpopular since advisors feel as if they are being pushed to bring in a certain number of households even if this is contra to their business model (i.e., advisors who focus on the UHNW and don't focus on volume of households or those who grow based on acquiring additional assets from existing households)," he pointed out.

Merrill Lynch said in late 2021 (https://www.thinkadvisor.com/2021/10/27/merrill-moves-to-trailing-12-month-advisor-comp-structure/#:~:text=Merrill%20Lynch%20has%20made%20no,Transfer%20Account%20Policy%20starting%20Ja it was making no major changes to its pay grid for 2022 but decided to move to a trailing 12-month grid structure and away from its retroactive comp structure in which payout was determined based on the prior calendar year's production.

The incentive grid "remains core to the comp program," Merrill said at the time. But "compensation will now be calculated based on an advisor's previous 12 months of production," starting Jan. 1, 2022, the company noted. "After each month, the most recent 12 months of production will determine that month's grid payout."

Diamond's prediction is Merrill "will make it so advisors just need to grow their business by a certain compound annual growth rate (CAGR) or grow it by an amount of AUM rather than by a number of households."

However, executive search consultant Mark Elzweig (https://www.elzweig.com/about-us/), president of Mark Elzweig Co., predicted: "Going forward, firms will leave grid breakpoints untouched."

"The bottom has been reached in advisor grid breakpoints," he said. The decisions by Morgan Stanley, UBS and Wells Fargo "to leave their grids untouched says it all," according to Elzweig.

"The hypercompetitive recruiting environment now includes other wirehouses, regionals and turnkey independent platforms who offer attractive deals and monetization opportunities," Elzweig said.

"There's simply too much competition for wirehouses to continue to monkey with grid breakpoints every year," he added, predicting: "Going forward the emphasis will be on incentivizing advisors to grow their AUM but not on chopping payouts."

Compensation consultant Andy Tasnady (http://www.tasnadyassociates.com/our-team.html), managing partner of Tasnady Associates, pointed to the fact that "grid creep" happens because, "as advisors got more productive, there's a compensation cost effect to companies."

Firms' compensation as a percentage of revenue rises year to year as an advisor's average revenues go up, and the effect adds up over several years, Tasnady noted.

"So that's why firms sometimes put in grid adjustments, called grid stretches, as a partial way to slow down this cost increase effect, where to get the same percent payout rate, an advisor has to do a little bit more in sales that next year."

"That's a long-term trend that'll continue," he predicted. "But that's a slow-moving boat. In the short run, there's probably less pressure on that now because, with the stock market down, many advisors and firms are likely seeing a slight reduction in their comp expense percentage because advisors' revenues are going down that are largely fee-based."

Tasnady considers it "very reasonable for firms to use grid stretches over time, especially if the market has been growing … in large amounts," he said. But it's going to "likely be a tougher environment for firms to use grid stretches" in 2023 so "the timing's not great right now for a grid stretch because the market's been down."

2. Firms will continue to focus on growth in fee-based business.

Both Elzweig and Tasnady predicted the large firms will continue to encourage and incentivize growth in fee-based business versus transaction-based business.

"That's part of the change for Merrill 2023," Tasnady noted. "A couple of the other wirehouses didn't make any changes or just minor tweaks. And that's typically what happens in any given one year. These compensation plans are typically evolutionary, not revolutionary in their type of direction.

"One trend that I see might be forming is to increase the differential between what advisors earn on fee-based revenue and relationships versus transaction-based," Tasnady said.

"For 15-20 years, many top firms have encouraged their advisors to move clients into advisory, fee-based relationships and move away from transaction-based relationships," Tasnady pointed out. "They started that by increasing payouts for fee-based business and trying different targeted bonus schemes."

For a while, “UBS used to pay +3% higher grid payout rates for fee-based revenues, for example,” he noted. “Over the years we saw many examples of firms also supporting the push to fee-based through education, products, design, a lot of management encouragement push, in addition to comp design.”

As a result, he explained, the “revenue mix at a lot of firms shifted to be much more balanced and many are near 50/50, in a mode where maybe half their business is fee-based and half the business is transactional.”

Top firms, however, are “already predominantly fee-based, especially when considering weighted revenue mix, as fee-based revenue rates are holding steadier, while transactional business revenue rates (revenue as a percent of AUM) continue to fall,” he said.

Each firm is now at its “own unique point of success in terms of transitioning to ongoing fee-based (advisory) business as a preferred service model,” he said.

But that is “definitely where the market targets are going and it is accelerating by the transaction commission rates falling precipitously due to low- and no-commission trading pricing by discount and online brokerages,” he said. “There’s just less revenues available with transactional commissions.”

There is one additional factor he said is “supporting the shift toward fee-based,” and that is the stricter “compliance requirements with transactional business.”

3. There will be a potential twist.

“The new comp twist that might be happening is rather than paying extra for fee-based business, firms might be reducing payout rates on transactional business instead,” Tasnady told ThinkAdvisor.

“That’s what Merrill Lynch seems to have just done, where they’re reducing the commission credits for transactional business,” he said. “So instead of paying extra for a fee, they’re paying less for a transaction.”

Although Merrill communicated its 2023 comp plan changes to advisors in November, the firm has yet to announce them publicly.

But sources familiar with Merrill’s 2023 compensation plan said the company plans to reduce commission credits on certain brokerage products because the cost structure and regulatory landscape for delivering brokerage capabilities has changed.

There are said to be no changes to products that can only be delivered via brokerage, such as alternative investments, 529 plans, annuities and institutional retirement, and, where brokerage is being used to support a broader fiduciary relationship with a client, there will be a more modest impact.

In the past, brokerage made up a larger part of a wirehouse’s business. But today it is under 10%.

4. True team-based compensation designs may finally happen.

Major wirehouses want as much of their sales forces as possible to consist of “high-end teams doing fee-based business,” Elzweig explained. “Fee-based business is viewed as more reliable and steady Eddy. It generates fewer compliance issues.”

Wirehouse executives also “feel that teams deliver a superior client experience,” Elzweig said. “Clients of teams often have a stickier relationship with the firm. There’s a real shortage of good producers, so firms want to use longevity bonuses and beefed-up succession programs to encourage them to stay and retire with the home team.”

Tasnady says he has been“advocating to some firms about coming up with true team-based compensation designs.”

But right now, “the whole industry is really using an individual-based commission and compensation administration design,” he noted. “Almost every credit and payout rate is individual-based.

“The only team big compensation benefit that most firms have come up with is, and this depends on a few additional caveats for several firms, if you meet certain criteria, then the lower paid people on an official team can get paid at the highest team member’s payout rate of compensation,” he said. “This is a meaningful benefit for especially the more junior team members.”

But it doesn’t help the top-earning team member, he noted.

There’s an opportunity for firms to improve their approach to team comp, as they shift their entire preferred service design to be team-based, he said.

Some firms are already far along on this trend, including Merrill Lynch, which says it’s 80% team-based. Andy Sieg, president of Merrill Lynch Wealth Management, recently said he wants to go to 100% in the coming years (https://www.thinkadvisor.com/2022/04/08/nearly-all-merrill-brokers-expected-to-shift-to-teams-by-2030/).

5. More compensation will be tied to loan business.

“Another future trend is on aligning more of the compensation toward the liability side of the business: loans and lending,” Tasnady says.

“As firms are getting increasing amounts of products and services from lending, not just asset management, the way people get paid on that is typically very different than on asset management,” he noted.

“So there might be some more evolution in that it’s not as well balanced,” he explained. “Most firms and advisors still get much higher proportional payout on their asset management business, which forms closer to 90% of their compensation even in firms with full lending products and emphasis.”

6. Advisor payouts for cash balances may increase.

The wirehouses “make a nice amount of spread on cash balances but typically haven’t paid the advisors much if at all for them, particularly over the last few years because interest rates were essentially zero,” Tasnady said.

“So they weren’t making as much money on cash balances. But now, with interest rates up, the question is might some of them reinstate or increase advisor payouts for cash balances?”

“For example, I think Merrill just bumped up their payout as part of their 2023 on cash balances from what I understand,” Tasnady said. “I’ve seen this trend in another firm or two in a return to this new higher interest rate environment.”

(Pictured: Compensation consultant Andy Tasnady, managing partner of Tasnady Associates)

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