

## A New Approach to Fee Negotiations

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It's a rare advisor who has not been confronted with resistance to fees. Indeed, in an article in *The Wall Street Journal*, Jonathan Clements says that the time has come to end the 1% of AUM fee rate. Recent research reveals a tactic that advisors can use to lower their fees – without sacrificing revenue in the long run.



It's particularly difficult for advisors recommending actively managed funds to justify their fees since the majority of these funds underperform their benchmark index in any one year. The odds of outperformance decline markedly over the long term.

The prevalence and growing popularity of robo-advisor platforms have added to the fee pressure on traditional advisors. A recent [blog](#) posted on Seeking Alpha noted: “Robo-advisors can do an advisor’s work for a lot less in fees, placing heavy new competitive pressure on FAs.”

In this competitive market, prospects are negotiating fees. Faced with the possibility of losing potential income, many advisors find themselves challenged to justify the fees they have historically charged.

### **A different approach to fee discussions**

A study co-authored by Simon Blanchard and Kurt Carlson of Georgetown University’s McDonough School of Business with Jamie Hyodo of the Smeal College of Business at Pennsylvania State University provides some much-needed insight into how to handle fee negotiations.

Through a series of five experiments, the authors of the study found that pairing a discount with a request for a favor increases the probability of a successful outcome. For example, in one experiment, participants were told to engage in discussions over the price of a coffee table-record player. One group was given an “absolute lowest price” by the seller with no further information. Another group was told the lower price was tied to a promise to post a positive review on a trade website. A third group was told the lower price was conditioned upon recommending the store to a friend.

Participants who were asked for a reciprocal favor (either posting the favorable review or recommending the store) had a significantly higher rate of acceptance than the group that received the lowest price without any such request.

### **Why it is effective**

The authors of the study refer to the pairing of a discount with a request for a favor as “the favor-request effect.” They note the increased rate of acceptance is consistent with prior research showing the power of our psychological need to reciprocate.

We have all experienced this phenomenon. If someone does something kind or generous for us, we feel compelled to respond in kind. The authors believe that pairing the discount with a request for a favor facilitates “consumer perceptions of their interaction with the seller as being more reciprocal.”

To be successful, the discount has to be perceived as unique to the buyer. An across-the-board discount available to everyone, coupled with a request for a favor, did not produce the same favorable results.

### **Implications for advisors**

How can you use the favor-request effect to your advantage in fee negotiations? If you simply reduce your fees without requesting a favor, you lower the possibility that your proposition will be accepted. What’s more, you are missing out on an opportunity. Even if your prospect accepts your offer of a lower fee, you could have gained something of value in the negotiation.

Consider coupling your agreement to a lower fee with a request for a favor. It could be phrased as follows: “I want the opportunity to show our value to you and am willing to lower our fee to get your business. However, I’d like to make this request for a favor: If you are satisfied with our services, would you be willing to recommend us to at least two friends who might also benefit from our advice?”

This request serves two goals. It should help you convert a higher number of prospects into clients. It may also help overcome your reluctance to ask for referrals.

If your prospect becomes a client and reciprocates by making the promised referrals, the additional fee income may more than compensate for the fee discount.

It could be a win-win.

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