Unlocking hidden AUM: Prospecting from within your client base

How savvy advisors can effectively prospect within their own books of business. • Jim Farmer and Susan Danzig

In today's competitive wealth management market, it is critical for financial advisors to focus their efforts on acquiring new clients to grow their assets under management, but an equally effective strategy lies within their existing client base.

Many advisors who have about $100 million in AUM have clients holding two to three times that amount in discount brokerages and banks, with much of it potentially classified as "dead money." By strategically addressing these opportunities, advisors can prospect effectively in their own books of business and enhance their service offerings.

The asset allocation challenge

It is common for clients to allocate their investments across various platforms. These clients often keep one-third of their investments with their primary financial advisor, one-third with low-fee discount brokerages and the remaining third with banks, often in low-yield certificates of deposit or money market accounts earning between 4% and 5%. This division not only limits potential growth but also reduces the advisor's fee income, since the financial advisor does not earn fees from these assets. This presents a clear opportunity for advisors to migrate assets held elsewhere into more effective investment vehicles.

Institutional life insurance contracts

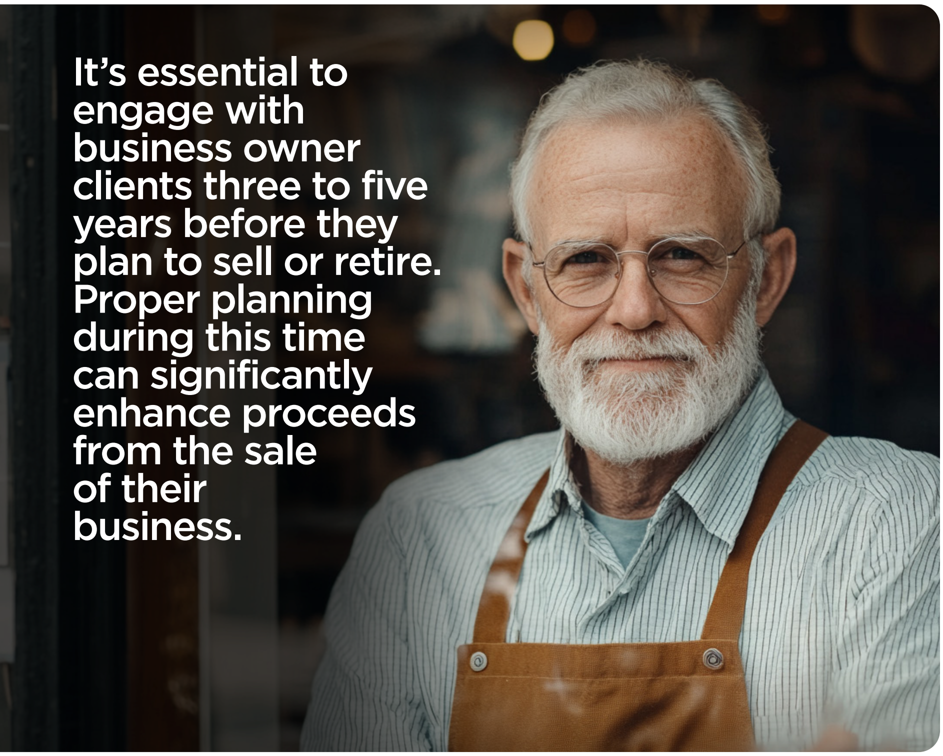
One promising solution for moving assets from banks and discount brokerages is the institutional life insurance contract. These contracts offer high cash values, low fees and the potential for tax-free income distributions.

Another attractive feature of institutional life insurance is the ability to grow invested capital tax-free, which is critical for high-income earners who expect to remain in the top tax brackets during retirement. Unlike traditional investments, which are subject to capital gains taxes upon withdrawal, distributions from these life insurance policies do not count as income. This feature allows policyholders greater flexibility in their retirement planning.

Moreover, with institutional policies, advisors can provide clients with a tax-efficient method to grow their wealth. If clients die before the age of 80, the historical average fees may even net out to 0%, making this product extremely appealing compared to traditional options.

Some investment options underlying an institutional policy can be compared to investment choices commonly purchased from banks. For example, a negative 20% buffered option in an institutional policy has returns on par with CDs and other fixed investments but with tax-free returns and without a management fee. This makes an institutional life insurance policy a compelling alternative for clients hesitant to pay management fees for traditional investments with a lower return.

Many clients at discount brokerages are attracted to the S&P 500 and may resist paying a financial advisor for managing their index accounts, especially when they can pay as little as 5 basis points at a discount brokerage. However, the taxable nature of these investments can lead to significant tax liabilities upon withdrawal. In contrast, the institutional life insurance contract allows clients to maintain exposure to the S&P, including dividends, as just one of nearly 100 investment choices, all while growing their money tax-free.



Upon the client's death, their heirs benefit from an income-tax-free death benefit and a step-up in basis by realizing all of the underlying investments as a part of the death benefit. This means that the heirs not only inherit the money but also avoid capital gains taxes, making this an attractive option for wealth-transfer planning.

Leveraging low-performance assets

Many clients may hold appreciating stocks without diversifying their investments. Advisors can introduce charitable strategies such as a charitable remainder trust to diversify these holdings. A CRT can provide clients with a higher income than dividends, as well as an up-front partial tax deduction and a means for leaving a legacy through charity. Upon the client's death, the remaining assets in the trust can be directed to a donor-advised fund, creating an opportunity for ongoing engagement with the financial advisor.

Similarly, for clients with appreciated real estate, a CRT allows them to transfer properties without incurring immediate tax liabilities. This process not only helps in diversifying their portfolios but also creates new AUM for the advisor.

When the CRT purchases an institutional life insurance contract, the death benefit can be used to replace the value of the donated assets, making the heir whole.

Engaging business-owner clients

Business owners present a unique opportunity for financial advisors looking to increase AUM. It's essential to engage with these clients three to five years before they plan to sell or retire. Proper planning during this time can significantly enhance proceeds from the sale of their business, often significantly more than a passive approach would yield.

Integrating a CRT can mitigate capital gains taxes when it comes time to sell a business. By facilitating this process, financial advisors can position themselves as invaluable partners in their clients' long-term planning, ensuring that they are included in the sale proceeds and subsequent investments.

Capitalizing on charitable intent

For clients with a charitable mindset, financial advisors can offer various charitable planning strategies. Techniques such as charitable lead annuity trusts, life estates and CRTs can provide significant tax advantages while allowing clients to fulfill their philanthropic goals. The tax deductions from these strategies can offset taxes due on Roth conversions, making them even more attractive.

Moreover, such initiatives not only aid clients in their charitable intentions but also create opportunities for financial advisors to gain referrals. Clients often share their positive experiences with their network, leading to new business opportunities.

A strategic shift

Financial advisors possess a unique advantage when they recognize the potential within their existing client base. By strategically repositioning assets held in discount brokerages and banks into an institutional life insurance contract and using charitable strategies, advisors can unlock significant AUM growth without the need for cold prospecting.

Advisors should encourage their clients to rethink their asset allocation strategies, focusing on how institutional life insurance can offer competitive returns, tax-free growth and distributions, and a smooth transfer of wealth. By doing so, financial advisors can enhance their service offerings and solidify their relationships with clients, leading to long-term growth. AN

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