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How Insurance Brokers Get Paid

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Why don’t employers ask?

An employer with 100 employees may easily be paying $5 million in salaries and $750,000 (15%) in employee benefits costs. Why wouldn’t every employer want to know how much their advisor is being paid to manage this expense, and what services they are providing?

- For medical insurance, which typically takes up 80% of the benefits budget, brokers/consultants/advisors typically get paid around 3% to 4% of premium, or up to $25 per enrolled employee. This equals $30,000/year.

- Other benefits pay out more but carry lower premium amounts. This includes dental, vision, disability, life insurance, and flex plans.

- For qualified retirement plans (e.g. 401(k), 403(b), etc.), a Fidelity Investments report from July 2015 shows that, depending on services, advisors get paid as a percentage of plan assets ranging from 0.50% for small plans to 0.10% for large plans. To translate this, see the below grid:

Plan Size	**Advisor Fee (% of Plan Assets)***	**Advisor Payment ($/yr)**
Under $1 million	0.46% (+year 1 addtl. comp.)	$4,600
$5 million	0.33%	$16,500
$15 million	0.24%	$36,000
$30 million	0.16%	$48,000
$50 million	0.14%	$70,000

(These amounts reflect average levels. Most fees are negotiable. Plans over $100 million in size will often still pay advisors 0.10% of assets, depending on services provided.)

Over the years we’ve found that executives, who are already very busy with their primary job responsibilities, would rather not focus on another line item on the budget. Instead, they just accept how the industry works and know that “the carriers or vendors pay the broker”. This is true, and perfectly fine, but also causes executives to forget to evaluate the value they get for the amounts that they are paying, albeit indirectly.

IRS guidelines state that employers should review all their service providers (including carriers, record-keepers, and advisors) at least every 3 to 5 years. Amazingly, employers generally don't do this with their advisors. This is especially surprising given that most employers "stumbled" into advisory relationships. Contrast this with the selection process for any carrier or service provider of benefit plans. An RFP/Market Analysis is standardly performed.

Is it worth it?

For over a decade, our team evaluated various company's benefit plans every month during our M&A Due Diligence work for private equity firms. In almost every review, we found mistakes or significant liabilities. Below are some examples:

- **Cost & Liabilities**: This company liked the potential savings of self-funded but were never advised to retain a claim reserve for Incurred but Not Reported (IBNR) claims. I violation and significant liability.
- **Cost**: A growing mid-sized firm had a partially self-funded plan with a major carrier. At each renewal, the carrier buried the client with underwriting assumptions and contract provisions in an attempt to hide that the client had a surplus amounting to over $500,000. They were unaware that they were free to cancel the contract at any time and move to a better program - and realize the surplus savings.
- **Liabilities**: This firm, like many, had high turnover in the HR/Benefits department. Executive contracts had been made which promised high life insurance benefits. Unfortunately, no underlying policies had been secured which left the company completely exposed.
- **Cost & Compliance**: A small tax benefit ended up costing the company money and IRS audit concern. A vendor sold this company the ability to arrange pre-tax commuter benefits and its only cost was the payroll tax savings from the deductions. This cost should have been company savings. Further, and of most concern, the company arranged the pre-tax deduction for every employee and just reimbursed all employees. This created a significant IRS audit liability.
- **Tax & Compliance**: Life insurance and disability insurance benefits are straight-forward. However, this firm neglected to calculate imputed income for life insurance amounts over $50,000 (a requirement). Also, the LTD policy had been written on an employee pay-all basis, but the company never implemented this process. This contract violation put the policy and any benefits paid at risk.
- **Cost & Compliance:** A broker helped start a new benefits program for a mid-sized program but put inaccurate old rates on all employee communication. Discovered months later, the employer had to revisit all employee deductions and pledges made to employees.
- **Fiduciary Liability**: Ten years ago, the 401(k) plan had been started with a good vendor. Unfortunately, the client never went back and reviewed the investment options. Many of the funds were "dogs".

- **Compliance**: a company was never advised about 5500 reporting (by 1 of the top 10 consulting firms) and after our review, was required to submit multiple years under the delinquent filing program (and pay late fines).
- **Cost & Liabilities**: This mid-sized company had been sold a "differential program" with high fees and even higher liabilities. The promised savings never occurred, and the company soon had to dismantle the program.
- **Cost**: A private equity firm bought a division of a larger company (a 50-employee division spinning out from a 3,000-employee parent company). The parent company just averaged costs across all their divisions. The true cost of the smaller division was unknown until a customized analysis was done. We found that the smaller division had a healthier population and would have been less expensive on a stand-alone basis (despite the advantages of being part of a larger group).

In addition to the value a good advisor brings in the areas of Cost and Compliance, services related to employee enrollment, education, and overall program administration are extremely valuable. Not all advisors are the same. Whether they work at a big consulting/brokerage firm, or at a small boutique firm, their expertise, services provided, and even their trust-worthiness can be extremely varied. It literally pays to be sure to evaluate who's providing the advice.

See related articles "10 questions to ask your broker", "Six Strategies every Employer should Explore", "Six Services every Advisor should Provide"