

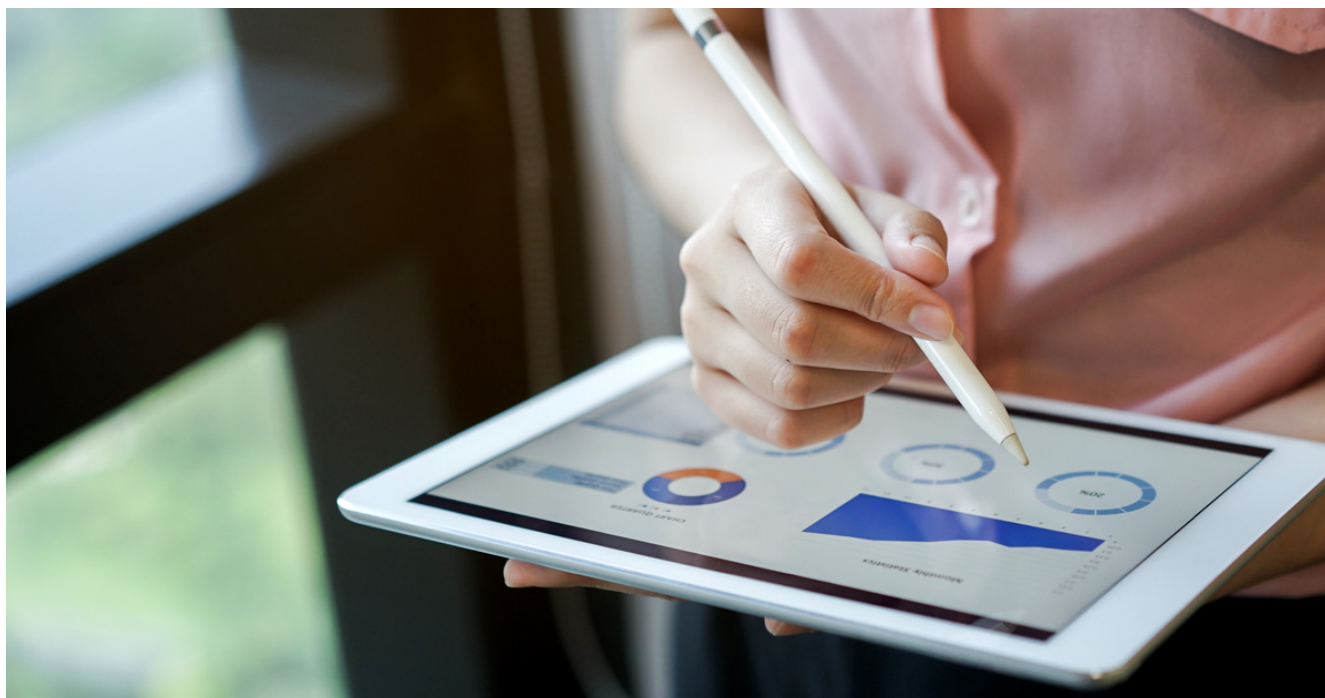


July 30, 2021

# Three key financial metrics for retirement plan TPAs

If you're a third-party administrator (TPA) who services retirement plans, you know there's a lot of disruption in the industry.

Understanding the causes of this disruption and where your firm currently stands can help you set goals and position your firm for continued success. We've highlighted three key financial metrics that can help you focus your efforts.



# The drivers of change

Before we dive into the numbers, let's set the stage by looking at the multiple external and internal factors affecting the retirement plan industry—and, in turn, TPA firms. These changes are likely to continue for the foreseeable future.

- **Aging demographics:** The retirement plan industry is a graying industry. Do you have a succession plan for your business or key employees? What about your referral network? Thirty-five percent of financial advisors plan to retire in the next 10 years. And there aren't enough new ones to replace them.<sup>1</sup> As a result, your firm may need to rethink how it pursues new business.
- **Constant regulatory changes:** We've had two pieces of major legislation in the past two years: the SECURE Act and CARES Act, and more bills are winding their way through Congress. New laws create cost pressures for your firm, as you have to adapt or build systems to comply.
- **Competition for high-performing talent:** How people view their careers continues to evolve. Many now want a role that's not only professionally fulfilling but also offers the flexibility to enjoy their passions outside the office and to work remotely.
- **Industry consolidation:** Mergers and acquisitions have become commonplace as TPAs, recordkeepers, and financial advisory firms seek economies of scale. Many are asking themselves, "Is it best for our company's long-term corporate health to sell, acquire other companies, or remain independent?"
- **Evolving technology:** The answer to the above question may depend, in part, on a firm's ability to take advantage of technological advances to streamline operations, increase efficiency, and remain competitive.

With this as the backdrop, let's talk about where you can take some control, set some goals, and measure your success.

## Metric #1: the cost to run your business

How much are you spending annually on compensation, benefits, marketing, and overhead? How much is this amount increasing year over year? These figures are the

foundation for evaluating your corporate health. Your annual spending not only determines your overall profitability, it may also help you determine whether your services are priced appropriately and uncover opportunities to become more cost-efficient.

Benchmarking can help you assess the reasonableness of your business expenses. See below for a snapshot of the TPA marketplace and the most profitable firms.

<b>Firm metric</b>	<b>TPA marketplace</b>	<b>Most profitable</b>
Annual revenue	\$3,104,383	\$6,440,764
Notional expenses	\$2,396,336	\$4,758,566
Notional salaries as a percentage of		
Revenue	54.8%	43.6%
Expenses	69.9%	75.8%
Rent as a percentage of		
Revenue	4.1%	3.4%
Expenses	5.4%	5.0%
Marketing as a percentage of		
Revenue	1.1%	0.9%
Expenses	1.5%	1.2%
Number of plans	977	2,139
Total number of full-time staff	2.1	2.6

Owners	3.9	8.3
Professional/consulting	10.9	21.2
Administrators	7.8	18.6
Support staff		
Revenue per plan	\$3,666	\$3,756
Revenue per full-time staff member	\$135,579	\$144,605
Plans per full-time staff member	41.6	57.6
Notional profitability	21.8%	30.6%
Notional profit per plan	\$792	\$1,131

Source: Business Health Pty Ltd, April 2021.

The results above have been calculated using the averages at an individual firm level and then averaging these across the data group. This approach produces a far more meaningful result and explains the apparent “discrepancy,” if some of the key practice attributes are simply multiplied or subtracted from each other. All of the “notional” profit and salary calculations assume a notional \$120,000 draw/salary for each principal working in the practice. The most profitable firms are the top 10% of the most profitable firms based on “notional” profitability. All of the staffing ratios have been calculated using a full-time equivalent basis.

## Metric #2: return on investment per employee

Is staffing an investment or a cost? That’s the next question you’ll want to answer, and it’s a bit philosophical. But the answer can help steer you toward the right metric, as costs and investments are viewed quite differently.

Staffing costs account for 70% of all TPA expenses and equate for just over \$1 in \$2 of revenue.<sup>2</sup> Hopefully, you see this figure as an investment. After all, it’s the people who

make a business. So, you'll want to make sure you're both maximizing productivity and helping your staff realize their full potential. And as with other business investments, you'll want to measure the return you're getting.

Here are some things to consider to help you assess your return on investment (ROI) per employee:

- Do you have the right people in the right jobs?
- Do you have formal job descriptions and conduct annual reviews?
- Do employees know and understand your company's 12-month plan?
- Do you have an employee value proposition?
- Are you tracking the hours and salaries of staff assigned to each client?

Based on your answers to the questions above, you may need to take action to improve your ROI. See below for the number of TPA firms using specific profit drivers and the potential impact.

<b>Profit driver</b>	<b>Percentage of TPA firms</b>	<b>Potential profit impact</b>
75%+ of staff with up-to-date position descriptions	69%	170%
75%+ of staff with individual performance objectives	72%	103%
Business planning	26%	+72%
Strategic planning	24%	+31%

Seek staff feedback	64%	+6%
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Source: Business Health Pty Ltd, April 2021. The profitability calculations include a notional \$120,000 salary for each working principal.

## Metric #3: economies of scale

The third key financial metric is economies of scale, and it can have a direct effect on the other two. Using productivity-boosting software and automating common administrative tasks can help reduce your operational costs and increase your return on investment per employee—improving your overall corporate health. For example, a client relationship management system can make sharing and tracking leads and client relationships more efficient. Project management software can help employees manage their time better and keep projects flowing.

Forty-three percent of workers who use automation software say it helps them complete projects faster, and 40% say it enables them to be more organized.<sup>3</sup>

Wondering what you can automate? Start by auditing daily tasks and processes performed by your staff and how your clients interact with the firm. Are you using bots and digital forms to streamline the client experience? Do your systems interface with third-party recordkeepers efficiently and provide an accurate flow of information among all the parties servicing the plans?

Nimble TPA firms that have the foresight to embrace new technologies to become more efficient are better positioned for continued success in an ever-changing marketplace.

## The importance of corporate health and key financial metrics

Strong corporate health and an equally strong balance sheet are essential ingredients for successfully navigating the great disruption occurring in the retirement plan industry. Invest the time to know where your TPA firm stands today, so you can create

the best plan to get you where you want to be in the future. You owe it to yourself and the firm you've worked so hard to build.

#### **Important disclosures** ▼

**1** "U.S. Advisor Metrics 2020: Dimensions of Diversity and Inclusion," The Cerulli Report, Cerulli Associates, 2020. **2** Business Health Pty Ltd, April 2021. **3** "Zapier's quarterly Automation Confidence Survey," Zapier Inc., September 2020. The survey is conducted by The Harris Poll and measures the growth, interest, and usage of automation. The research involved surveying 1,198 employed U.S. people, including 912 knowledge workers, or those who work in a professional setting and use a computer as part of their job.

In April 2021, John Hancock commissioned a White Paper, "Insights into the "health" of TPA firms" with Business Health Pty Ltd. John Hancock and Business Health Pty Ltd. are not affiliated, and neither is responsible for the liabilities of the other.

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