LONG-TERM INCENTIVE PLANS (LTIPs)

#FP*INSIGHTS*

Successful wealth management businesses have one common attribute: they know how to attract and retain talented advisors and support staff and consistently execute on that mission. Part of their success is in knowing what rewards work. Competitive compensation is often not enough to keep the best people for the long term. Sustained retention of top employees often requires equity to be deployed strategically. Where an equity solution is not yet the answer, synthetic equity may be. Synthetic equity can provide ownership-level economic returns without the need to buy or sell actual stock. Long-Term Incentive Plans (LTIPs) are one of the most common forms of synthetic equity used to align key employees with a business's vision and growth plan.

WHAT ARE LONG-TERM INCENTIVE PLANS?

A Long-Term Incentive Plan, or LTIP, can be designed to meet a variety of objectives, with various time horizons, all within one plan. LTIPs can reward both short term behaviors and encourage and incentivize employee retention for the long-term. They typically pay the employee a cash bonus after 3-5 years and are reissued on a rolling basis to continue to ensure ongoing engagement and alignment with business objectives.

HOW DOES IT WORK?

Long-Term Incentive Plans are customized to fit each advisor's fact pattern and goals. Most LTIPs start by determining participation, desired performance parameters, and funding amounts. Many LTIPS are structured with a one-year goal but a deferred payment for an additional year or two. These goals can be objective or subjective, tailored to individual employees, or aligned with business-wide objectives. For example:

- Personal Goal: An advisor passing the CFP exam within the year.
- Group Goal: Increasing top-line revenue by 10%.

If the goal is met, a predetermined amount of money is "awarded" but the payment is deferred an additional 24 months, creating a continuous cycle of incentive and retention.

WHO CAN USE THIS TOOL?

Any independent advisor or business owner (RR, RIA or IAR, or those with insurance licensure) can implement an LTIP, regardless of revenue structure. FP Transitions designs LTIPs that integrate seamlessly into any business model, including S-Corporations, C-Corporations, Limited Liability Companies (LLC), or even businesses without a formal entity structure.

WHICH EMPLOYEES SHOULD BE CONSIDERED FOR LTIPs?

LTIPs are an excellent solution for employees who are highly valued but may not be positioned for ownership. Licensing is not a prerequisite, and plans can be structured for individual employees with personal goals or for all staff working toward a collective business goal.

WHAT PROBLEMS CAN LTIPs SOLVE?

LTIPs are a strategic compensation tool that can help businesses:

- Motivate key employees to increase business development activities.
- Align key employees with ownership-like thinking without requiring an equity sale.
- Provide enhanced compensation opportunities – paid as a share of the bottom line – that encourage long-term retention.

WHAT TYPE OF PLAN IS THIS?

There are three main types of synthetic equity plans. **1) Appreciation only plans, such as stock appreciation rights**, are designed to pay out the increase in the underlying stock value over a certain period of time from the date of the grant. **2) Full value plans, such as phantom stock**, pay both the value of the underlying equity as well as any appreciation that is earned over a set period of time and can result in a much higher payout to an employee than an appreciation only plan. **3) LTIPs** often exchange the use of equity as the measure of value for another metric such as growth in revenue, profitability or assets to achieve similar objectives, but over a shorter time horizon.

IS A VESTING SCHEDULE USED?

Yes and no. The recipient of an LTIP has to wait—for a predetermined period of time—to receive any award. LTIPs are designed to provide an incentive to non-owners to be successful and to stay with the business. The recipient must be employed on the day the payment is made to receive the award, otherwise it is forfeited.

HOW DO KEY EMPLOYEES RECEIVE VALUE FROM AN LTIP?

Typically, participating employees will receive LTIP payments as a cash bonus, taxed as ordinary income and is deductible to the employer when paid. FP Transitions designs Long-Term Incentive Plans to ensure compliance with tax regulations (Sections 409A and 83(a) of the tax code) while maximizing benefits for both employees and business owners. LTIPs can be designed to pay out in shares of company stock but that is not common.

WHAT IS THE COST TO SET UP AN LTIP?

The cost depends on several factors, including the number of participants, complexity of performance metrics, customization required, the payout structure and other factors. FP Transitions provides tailored proposals outlining flat fee costs before engagement.

HOW DOES FP TRANSITIONS SUPPORT THIS PROCESS?

FP Transitions' Legal, Consulting, and Analytics teams collaborate to develop and implement LTIPs that align with business objectives and growth strategies. Our professionals provide expertise in:

- Eligibility determination
- Plan structuring and documentation
- Performance metric selection
- Tax and compliance considerations

For more information, including benefits, detriments, and caveats associated with an LTIP, be sure to download our white paper, Synthetic Equity: An Innovative Approach to Compensation at fptransitions.com/syntheticequity.

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