

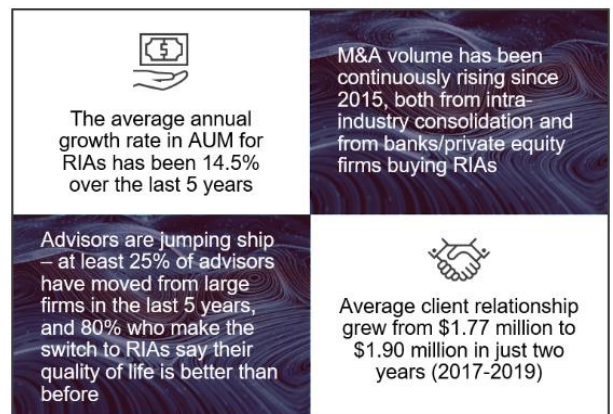
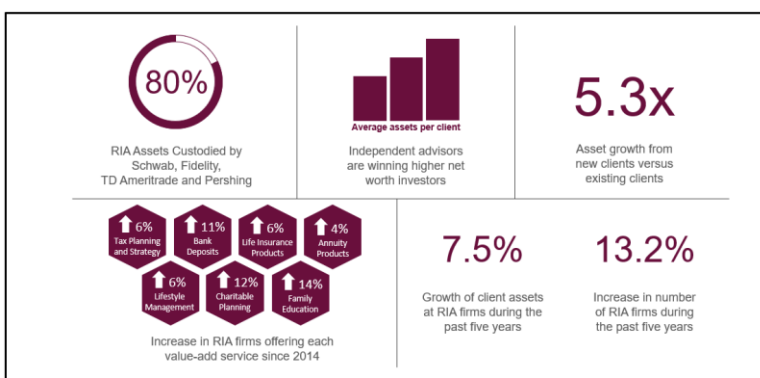


Should Traditional Broker-Dealers Consider an RIA Platform?

Introduction

A Registered Investment Advisor (RIA) is a person or firm who advises high-net-worth individuals on investments and manages their portfolios. RIAs have a fiduciary duty to their clients, which means they have a fundamental obligation to provide investment advice that always acts in their clients' best interests and report any conflicts of interest. RIA's are regulated and mandated to register either with the US Securities and Exchange Commission (SEC) or with state securities administrators, based on the size and AUM of the firm. RIA's are typically compensated through a fee-only model determined by an annual percentage of client assets held under management, as opposed to a commission-based model leveraged by traditional broker-dealers.

RIA's continue to grow in popularity as portrayed in the data tables below. Interestingly, the number of RIA firms and the number of FINRA registered broker/dealers has continued to trend in opposite directions. RIA registration increased by 3% in 2019, while FINRA membership decreased by 3%. Client assets at RIA firms grew at ~7.5% per year over a five-year horizon, , while the number of independent RIA firms increased by 13.2% over the past five years¹.

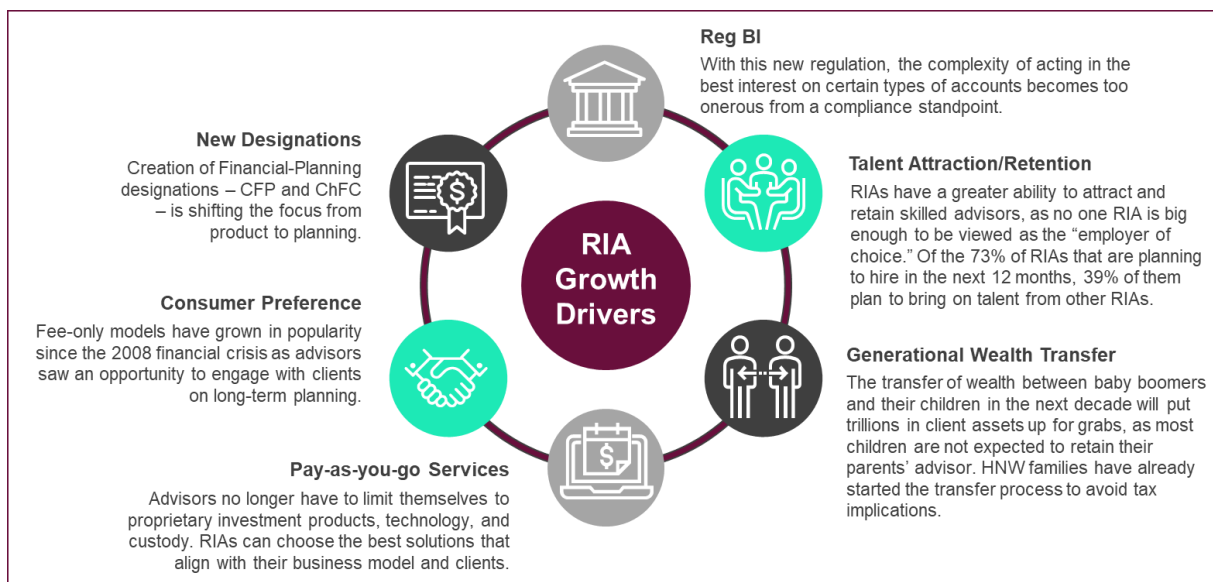


Key Drivers of Growth

The increasing interest in RIA channels can be attributed to several growth factors. For instance, in the aftermath of the 2008 financial crisis there was a notable shift in client preferences to RIA's, who touted their fiduciary duty to act in a client's best interest². Moreover, the ability of RIA platforms to offer auxiliary services and manage the entire client relationship have been well received. Further industry enablers have been highlighted below.

¹ 2019 Benchmarking Study from Charles Schwab

² Financial Advisor Magazine, 'The Global Financial Crisis Catalyzed Growth, Changes in RIAs, Says Schwab'



Source: 2019 Benchmarking Study from Charles Schwab

Challenges Faced by Traditional Broker Dealers / Wirehouses

The growth of the RIA industry has also been supported by the challenges prevalent with the traditional wirehouse business model. Consumer preferences, new sources of competition, regulatory pressures, and even movement of advisors themselves are all putting pressure on the wirehouses’ bottom line.



Shifting Consumer Preferences

Over the last 5 years, RIAs have been growing at a much faster rate than the advising industry overall, reflecting consumers’ desire for fee-based advising models. The fiduciary standard, which all RIA-based advisors are held to, and the knowledge that their advisor is truly independent, has led investors to flock to RIAs. 62% of investor households prefer fee-based payment arrangements over commissions, and consumers in fee-based arrangements also report significantly higher levels of trust in their advisor.



Falling Prices & Competition

Prices in the wealth management industry are being driven down by a number of factors. Advisory fees are falling across the board, and many brokerages are beginning to offer no-cost trading on stocks and ETFs. Additionally, the entry of robo-advisors, who charge fees well under the industry standard of 1% AUM, into the wealth management space has increased competition significantly. Robo-advice is spreading from its initial customer base of young people with relatively few assets to older and higher-net-worth investors.



Breakaway Brokers

In addition to customers, advisors themselves are jumping ship from brokerages to RIAs in increasingly large numbers. 25% of brokers have moved from large firms in the last 5 years, and 80% who moved to RIAs say their quality of life is better than before. Brokerages limit advisors in a number of ways – they can only sell certain products to their clients, and the compensation structures tend to focus on high-producing advisors to the detriment of newer or lower-producing ones.



Regulations & Compliance

Increased regulation of broker-dealers, from privacy & disclosure to Reg BI, has squeezed brokers’ resources. The number one issue that broker-dealer executives report is worrying them is the need to do and spend more on regulatory matters. Brokers considering a move to RIAs listed the regulatory environment as the number one challenge facing their current employer, and many hybrid broker-dealer/RIA firms are considering moving into the RIA space exclusively, to avoid double-regulation by the SEC and FINRA.

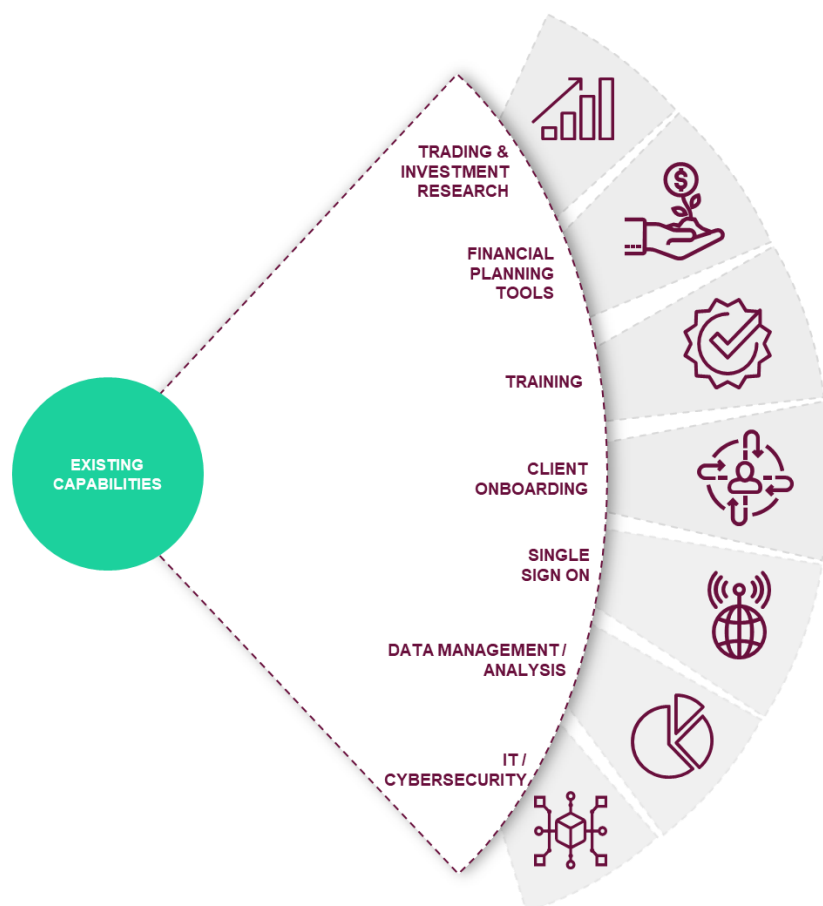
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RIA Custodian Operating Models

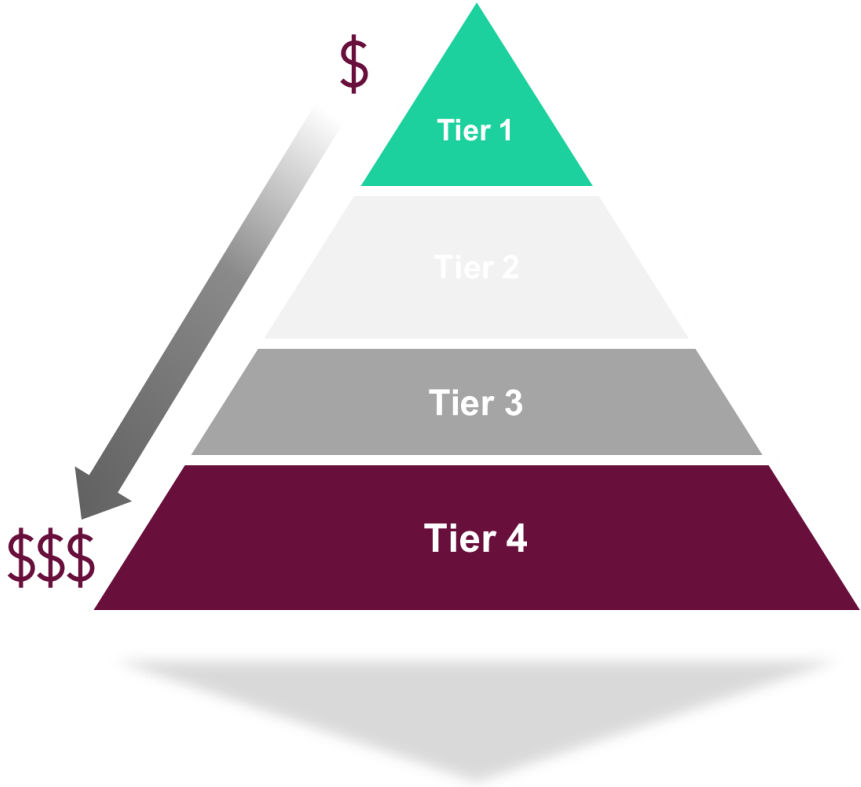
While RIA's and Broker-Dealers offer many of the same services, RIA's are afforded a level of flexibility that many Broker-Dealers are not when it comes to product offerings and the types of clients they can accept. Conversely, Broker-Dealers enjoy robust middle and back office support structures, as well as brand name recognition, that RIA's must build on their own.

The four leading RIA custodians, Charles Schwab, TD Ameritrade, Pershing Advisor Solutions, and Fidelity, which collectively custody approximately 80% of RIA assets, use their existing client facing tools and back office infrastructure to offer additional services to their RIA clients on an a la carte basis, or in some instances offer tiered packages that increase in price with the level of service². For example, Charles Schwab, the largest custodian of RIA assets, provides a variety of support services such as client servicing operations, practice management, account management, and trading functions. Clients also have access to the custodian's experienced support personnel. If their proprietary tools are not enough to meet a client's needs, they offer an a la carte menu of third-party service providers in areas such as practice management, research and analytics, cybersecurity, financial planning, and CRM. Each of these third-party service providers integrates seamlessly with the Schwab platform which allows advisors to build the service package that best suits their business.



² <https://www.investmentnews.com/when-it-comes-to-ria-custody-how-big-is-too-big-190013>

The figure below exhibits a tiered service delivery model offering a menu of support services bundled together and offered at different price levels based on the requirements of the client. The Tier 1 package is offered at the least cost and comprises basic custody, trading, and client reporting services. The quantity of bundled services increases along with the price point, with the Tier 4 package offering a full suite of cutting-edge services required to allow RIA firms to achieve operations and technology excellence.













Stacking proprietary tools with integrated third-party service offerings is a method to ensure that RIA's don't feel the need to search for a new custodian when their current custodian's proprietary tools alone are not a good fit for their practice. This allows RIA's to seamlessly change their client servicing and technology platforms as their practice grows or changes over time. An engagement would benefit RIA to leverage a broader set of services, and a robust ability to scale.

Key Considerations for Broker-Dealers Entering the RIA Custodian Market

The figure below lists some of the key questions and considerations in making the strategic decision of pursuing an RIA service channel. Potential options include Integrate and Invest or Integrate and Maintain, which involves the acquisition of an existing platform, or building a new RIA service platform in-house.

A recent entry into the RIA channel, Wells Fargo, built their platform from the ground up, giving RIA's access to their bank products, trust services, and proprietary planning software, while directing them to a single third-party partner for broker-dealer and support services. To assist new RIA's moving to their platform, their broker-dealer partner established a service team entirely dedicated to helping new RIA clients with their transition.


	What are the various drivers of growth / movement of advisors from wirehouses to RIAs?		What technology and operational complexity exists and what are the initial and ongoing costs to support the RIA platform?
	How will retaining or growing the RIA platform help, hinder the existing broker-dealer business?		What are the sizing / scaling requirements to increase the overall profit margin?
	What are the additional services we can charge for and what do customers value?		What are the channel conflicts that would exist?
	What is the up-front investment for the different models / scenarios?		What are the strategic advantages and opportunities of having RIA assets custodied?
	Which client segments are impacted by integrating the RIA business?		What are the risk factors & potential mitigation plans?

Implications – Outlook & Preparing for the Future

There is a fundamental need for broker dealers to recognize the paradigm shift in the way that the wealth management business is currently modeled. This argument is supported by the robust growth statistics of the RIA industry and the positive drivers that continue to fuel this channel. In order to stay competitive in the wealth management space, it is imperative that such firms recognize the actions of their peers and carefully deliberate the value of creating an additional revenue model by lending their expertise and industry-leading tools and services to independent advisors.

Sia Partners is well positioned to serve as a trusted advisor and help firms navigate the spectrum of challenges and critical analysis required to successfully branch into this space.

How Sia Partners can Help?




Discovery & Market Analysis

Perform a market / industry analysis of the RIA landscape including key drivers, pricing, services and product offering.

Perform an internal assessment with key stakeholders to better understand the key drivers for migrating to an RIA business model

Perform a current state analysis to identify the key services, products and platform capabilities that could be offered to an RIA channel




SWOT & Risk Analysis

Perform a SWOT analysis to assess the firm's position relative to the industry

Document the potential risks including potential cannibalization of existing advisors and revenue

Perform an economic and NPV analysis to understand upfront investments / costs and revenue projections

Evaluate the competitive implications from a branding and reputational perspective including value proposition



Design Target Operating Model

Work with key stakeholders to determine day 1 product offering and services (MVP)

Propose a pricing model for basic / base services and incremental pricing for add-on's

Project management of transformation initiative to develop and execute service offering to RIA clients

Gap analysis of your current program and requirements definition to service the RIA channel

Determining and implementing a strategic path to achieve future state requirements



Revenue Model Development

Perform a qualitative assessment of the broker dealer's technology and operational service offerings.

Determine optimal service product mix and pricing strategy to cater to RIA clients & assist with identification of prospects



Program Implementation & Assessment

Forecast revenue potential from newly bundled service offering, and track progress against actual sales.

Ensure successful implementation of TOM and define optimal integration strategies to enable successful functioning of BAU activities.

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TD Ameritrade Institutional. TD Ameritrade Institutional 2020 Break Away To Independence Survey

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