FOCUSPOINT CASE STUDY #2:

ADVISOR: Fee-only sole practitioner

GOAL: *Grow 100%+ without adding staff (outsourcing only)*

BEFORE

FPS: **Why did you ultimately decide to transition to the independent RIA model?**

ADVISOR: There were two things that drove me, actually.

The first and most important thing was that I wanted to be able to provide the high level of service I've always wanted to provide to clients—and be compensated for it with regular cash flow. I've always been focused on a service—not sales—model. I've spent a great deal of time studying what I know makes sense for my client base, not just now but in the future. I've often asked myself this question: Is it possible to start out as a producer as a fee-based advisor? I always wanted –at least conceptually—a fee-based relationship with my clients.

If I have clients who are appropriate candidates for a fee-based service model in the future, the level of service they're going to require and look for isn't covered by trail revenue. So you're servicing those clients for a lot less money. No other business exists where you would tell yourself, "I'm going to service these accounts at a very high level for the next 2-3 years until I get to $50 million." The commission-based sales model was never designed to support quarterly reviews. This is fundamental to my thought line.

The other thing—and this really kicked in the last year or so I was on the IBD side—was the whole FINRA regulatory environment.

I remember vividly realizing I needed to make a change when I had a new client who had transferred over from a friend of mine. The prior advisor hadn't had his eye on the business in the last year or so he was a broker. My new client owned some extremely poorly rated bond funds by that point—no matter which rating system you use—and I wanted to switch those out for a couple Pimco funds. When everything was said and done, I would have ended up with a 1% commission on the trades. I received an email from my IBD's compliance department wondering how on earth I could have justified transferring from one bond fund to another. Rather than sending something back with some basic reasoning, I put together a 5-page email. In it I explained thoroughly my planning and review process, that if you took any time to look at things you would see the justification.

At the same time, in my case, the only reason whatsoever I saw to keep an IBD was to accommodate some small accounts and the odd situation…maybe some 529 assets.

For me personally, I wanted to get myself away from asset management and into asset gathering. Not because I wasn't good at asset management—I think I actually did pretty well, objectively evaluating things—but when it comes right down to it, there are only so many hours in the day, and I did not enjoy it most. I had to look at running the business I was going to be in from a business owner's standpoint.

To me it just made no sense. If I kept the IBD relationship, even once I had the RIA, I'd still be operating under a FINRA-, transaction-oriented compliance department.

I tell other advisors, I can't tell you for your practice whether it makes sense for you to keep the IBD relationship. For me personally, I saw no reason to overcomplicate things.

FPS: **What were your main goals for after your transition was complete? Have you achieved them?**

ADVISOR: I had two main goals. And yes, I have achieved both of them.

The first part was to get all the elements of my business in terms of client communications in order, and to get everything on the operations management side of things very streamlined. I wanted to make sure my business would be capable of running on a systems basis. If I bring someone new in, I can say, "Here's our compliance manual, here's our CRM, here's how everything fits together, etc." At this point, another person—staff or partner—could very easily come in and understand how things work and run the business.

Today I have systems in place for everything from when and how to send birthday cards to quarterly letter setups to client review months. Before I transitioned to my own RIA, I didn't have any of this in place—but I definitely had a sense of exactly what I wanted to do. Post-transition, there's been a little learning curve in the process of moving everything over; for example going from one CRM to another. I also think one of the biggest inhibitors of running and growing a practice is portfolio management. And with my current situation, that really isn't something I have to deal with anymore.

What a new client experiences—thank you notes, any letters, timetables, reviews, holiday gifts, etc.—really getting all of that down, has taken more time than I intended to but it's now in place. I expect my business will always be a work in progress, but I know at this point there are systems in place to run things smoothly.

The second part was making sure I had everything completely transitioned before I started growing again. I recently made the decision to move geographically towards where my ideal clients are located. Right now my emphasis has really shifted to asset-building. I feel like with the systems I now have in place and an operational platform which really runs itself, I no longer have to worry about managing money—I am putting all of my efforts into building business, and I know my systems will be able to accommodate this growth.

DURING

FPS: **What was your biggest challenge as you made the transition?**

ADVISOR: Cash flow. In my case part of the problem was that I had slowed down commission business so much in anticipation of making the transition that by that point I had essentially, for the first 6-7 months of 2005, made no commission transactions. I was doing fee-in-lieu business for most clients at that point because I knew I wanted to make the leap. So it was not at a regular pace by any means. This of course dictated a very quick transition for me.

FPS: **We read all these discussions with industry experts who tell advisors they should have $50 million before moving to the RIA business model. While we support firms with a wide range of client assets, some much higher than that number, we also know that it can work for firms smaller than that. What are your thoughts on that number?**

ADVISOR: Too high. That said, based on my experience, I definitely feel like nobody should be making a transition with less than $10 million.

Right now my clients pay an average of 1.5% revenue on the assets I manage for them. This includes everything I pay for outsourcing. I experienced a couple months of revenue shortage, tops.

What I want to add to that is for advisors who keep telling themselves, "I'll make the move once I'm at $50 million or some other number" is that I think if this is a business model that you know you want, it makes sense to make the transition as quickly as possible in your career. At some point in time, if you know, deep down, that forming your own RIA is what you really want to do, then make it easier on yourself and do it as soon as possible. You'll avoid having to deal with a more complicated transition and many more client meetings.

FPS: **We spend dozens of hours talking and consulting with individual advisors considering making the transition. Many times advisors feel like they need to have 100% of their questions or issues or potential client scenarios addressed prior to making the move. But in reality, what we've found is that if you have about 70-80% of your questions answered and you know it's the right business model for you, you're ready. What do you think?**

ADVISOR: I totally agree with that.

You're always jumping into any business venture before you feel you're completely ready. It reminds me of when I was a training manager with my previous IBD. The reps I trained who always felt like they had to study this or that or have absolutely everything covered before they got on the phone never made it.

In my case, I started out straight out of college and just went for it. I had a 14k month my first time out (never mind I was only keeping 12% of that at that point). It was interesting because the reason it worked for me was because I went out and met people and tried to do as convincing a job as possible because I knew if they had questions I might not know every single answer. It was just like my transition to doing fee-only work and explaining that to clients.

You've got to just jump in there and start the transition. While I didn't know everything and definitely had questions as I went along, my new team did a phenomenal job of filling in as much as possible.

FPS: **How long did your transition take vs. how long you planned for it to take?**

ADVISOR: I planned for essentially a 90-day transition.

Obviously I prioritized my clients in such a way that my I sat down with my best clients first, and they *were* done in the first 90 days. So, 50% complete. In six months I had about 85% of client assets transitioned. The rest were trickier cases of one sort or another. To get every single client asset moved in, materially everything moved over, took nine months total. But the remaining 15% wasn't important from a revenue standpoint.

A lot of the holdup resulted from paperwork and a couple specialty products here and there—annuities, missing beneficiary information from the previous application they filled out ten years earlier. Things like that.

FPS: **Looking back, what advice would you give advisors that might help them to have the smoothest and most successful transition possible?**

ADVISOR: I would tell them that the job of reviewing assets up front (specific products and compatibility with platforms, etc.) is not easy, but you can enlist help with most or all of that. I think that doing it alone can be a very complicated thing to do.

While I'm glad I went out and had confidence to meet with clients very quickly, if I had it to do over, I'd spend a little more time up front gathering missing information from clients so that I could hand everything off on the front end. For example, my transition team did everything they could with the data that was transferred over from my previous CRM—names, SSNs, etc. When you're dealing with repapering every single acct, had I gotten copies of statements to them in advance, my transition would have been expedited quite a bit.

And as far as how to really be successful during a major transition like this, I think you need to really announce it to clients! Make a big deal out of it!

When people see you're doing something new and different they tell other people about it! They sense your excitement and confidence and they want to be a part of it. I believe these conversations can actually become a referral campaign if you do it right.

FPS: **What would you tell advisors who are concerned about losing clients because they're now going to be charged a (higher) fee for advisory services?**

ADVISOR: For the most part, any concern on the part of the client is a concern that you plant.

Fee discussion is so prevalent in the financial services industry, but the truth is that it *doesn't exist* in our clients' minds. I would never charge this but I could have said my fee was 2.5% and most of my clients wouldn't have blinked.

Most concerns clients have are those that you are *even subconsciously* bringing to the table.

FPS: It's amazing—we hear that from advisors all the time. Most issues really do exist in our minds and not clients'. What are your thoughts on establishing fee relationships or raising fees in a declining market?

ADVISOR: I started my transition during 2005, a good market. I don't know how much price resistance you might have over, say, the next six months in a declining market. Being in the business since 1995, what I've found is that if clients, within the first six months, have a good experience, this makes a very big difference in how cautious they are. Because of this, I like to dollar cost average in to reduce the likelihood of clients seeing significant losses in the first few months of working with me.

When things are good and clients are impressed about the returns they've experienced, I make sure to tell them it won't always be like this; we got a little lucky. That way they're not as concerned when it goes down.

FPS: When advisors are converting to fees, we encourage them to create a new client experience—not just intangibly with their new service offering, but visually. This way, clients can actually *see* the difference. Do you think it helps to give clients a whole new experience?

ADVISOR: Absolutely.

Visually, my clients are seeing a big difference. From day one, for each account we now have a dedicated investment policy statement—which we didn't have before—as well as our investment philosophy and so forth. I use things like the standards of engagements letter, spend a little bit on professional binding materials or tabs and put everything together in a nice little bound folder.

Every annual review includes a report I run myself which we've customized for my business and which has been a huge hit with my clients. They used to ask for something just like this year after year when I was in the commission-based world: "What was my rate of return last year? How much have I contributed to my account since I've held it with you? How much have I redeemed? Am I on target to reach the financial goals you've set for me?"

It seems simple but it wasn't before. Now everything clients want to see each year is on one easy-to-read report. And their reaction to the editable quarterly letters I now have access to has been fantastic.

During my client transition meetings I showed people a couple sample tax reports. I was able to talk about how previously in our commission-based relationship, I wasn't able to provide this for you, but here is what you're now going to receive. You can *immediately* go to clients and show them the enhancements they're going to now see on a regular basis.

TODAY

FPS: How has your profitability and revenue been affected?

ADVISOR: Upward. Definitely upward.

My revenue is considerably more regular. In a nutshell, the heart of my problem was that I was operating in a commission-based world. At the same time, I've always believed in delivering a very high level of service and promised it to clients because I *wanted* to. This level of service was higher than one supported by a commission-based revenue stream.

Essentially I'm even in assets—and growing—but now I'm able to set up systems for everything I need and want to provide to clients.

FPS: Would you consider going back to your previous business model?

ADVISOR: Never, ever.

I can honestly say I would find a different way to make a living before I went back to the previous business model. It's not that I wouldn't go into commission sales of something; it's that I believe there is no such thing as financial services *sales*.

It's the only business in the world where you're expected to service it *forever* for a very small charge—and be liable for it.

FPS: What is the best thing about your having made the transition to this model?

ADVISOR: There are really a few things.

For me, after working for ten years on a commission basis, the standardization of cash flow is the best thing.

However, if I look deeper, the real answer is what that allows me to do—things with my practice that I couldn't do otherwise. I truly have peace of mind. I just work better with clients who are looking for more and I like providing more. Any conflict I may have felt before is just gone.

Also, my perception, my gut feeling, is that I am much more proud of the business I have today than I had two years ago, before I went fee-only. I feel like it's a dramatically more professional practice than it was before.

LOOKING BACK

FPS: **What were your biggest fears about going independent and how did you overcome them?**

ADVISOR: Honestly, I just didn't have them; I'd been studying the business model for so long. I guess there was some fear about the unknown. But as soon as I researched some options and chose an experienced team to put together some of the pieces for me, everything came together.

In terms of the unknown, during a transition like this, I assumed that there would be questions from my clients that came up that I might not be able to answer right off the bat. But if I could just say, confidently, "I don't know, but I'll find out. That's what you're paying me for and that's why you need someone" I was in good shape.

Consider that many clients you bring in for the last two years before your transition may have to wait to be transitioned. If you're still doing commission business today, fundamental best practices dictate that the clients you've sold to in the past will have to wait 12 months since you just charged them a 4% commission.

I think if that's the case, you've got a very compelling argument to move forward as quickly as possible. And you don't necessarily need to move your biggest clients first. You will learn things on your very best mid-sized clients which you can then share with larger clients.

Many advisors I talk to who are coming from a commission-based background said they can give it some thought, but that they would have a hard time charging more than 1%. Again, to this I say, figure out the level of service you want to provide.

Some of my clients would easily pay more—and I'm earning it.