THE HYBRID RIA ADVANTAGE

INSIDE: The appeal of the RIA model | Hybrid RIAs: A customizable solution | Making the move to a Hybrid RIA

Growing numbers of breakaway advisors are choosing the Hybrid RIA model. What's the appeal—and what do advisors need to know before making the switch?

An increasing number of advisors in recent years have left large firms and adopted the registered investment advisor (RIA) model. They have found that operating as an RIA offers greater flexibility in managing and growing their practice, as well as greater latitude in the ways they work with clients.

Many of those converts have chosen to pursue the Hybrid RIA model, which helps streamline the process by which advisors can offer both advisory and commission-based services and products to their clients. With the right platform, advisors can broaden the scope of their investment and planning services, while minimizing complexity. The rapid growth of the Hybrid RIA model represents an important evolution in how advisors can manage their practices—and provide better service to their clients. "The Hybrid RIA has become the model of choice for advisors looking to make a move," said Matt Enyedi, executive vice president, RIA solutions at LPL Financial.

A recent survey by LPL and WealthManagement.com found that nearly one in four advisors considering a move from their current firm would choose to transition to the Hybrid RIA model. Advisors can pursue this by joining an existing RIA or starting their own. Mindy Diamond, president and CEO of Diamond Consultants, a New Jersey-based search and consulting firm specializing in advisor placement, said advisors have embraced the flexibility of the Hybrid RIA model. "It's been a perfect storm," she said. "Advisors want more control and freedom, and the industry has expanded with models that allow advisors to be more independent while also monetizing their businesses."

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LPL Financial

THE APPEAL OF THE RIA MODEL

Advisors traditionally have operated under the following models:

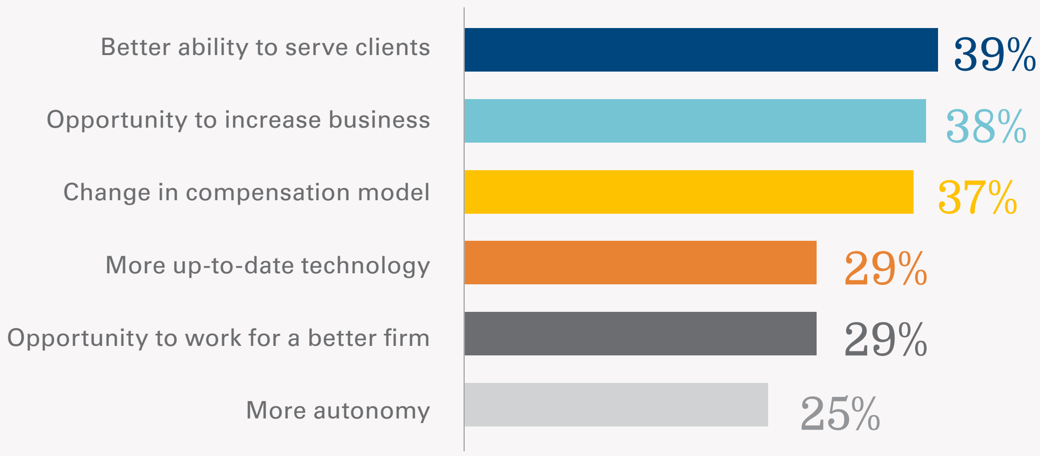
- **Traditional broker-dealer representative:** Advisors can work directly for a wirehouse or maintain an independent advisory practice that is affiliated with an independent broker-dealer. Transactional business is handled through the broker-dealer, while advisory business is done through the corporate RIA.
- **Fee-only RIA:** Advisors can launch their own RIA firm by registering with their state or the SEC. Client assets are typically held by a custodian, which can also provide a range of practice management services, like processing and back-office assistance. Advisors working under this model aren't registered representatives of a broker-dealer and can't offer commission-based products.
- **Hybrid RIA:** Similar to the fee-only RIA model, where advisors must register their RIA Firm with their state or the SEC, the Hybrid RIA means advisors are also registered representatives of a broker-dealer. As a result, advisors can handle commission-based products through their broker-dealer and fee business through their RIA.

In the case of an advisor coming from a wirehouse environment, the move to an RIA model—whether a fee-only RIA or a Hybrid RIA—may offer more control over investment policy, investment decisions, staffing, marketing, and other business functions.

For instance, wirehouse advisors are often required to keep clients' portfolios within the bounds of their firm's investment policy. That may pose challenges for advisors who want more latitude to use particular wealth management strategies or products, such as hedge funds and other alternative investments.

> "It was very attractive to us to transition to a firm that we owned. We were very aware at our old employer that our clients weren't our clients; they were the firm's clients. They're our clients now, and they generate a recurring revenue stream that has real market value."
>
> *Bennett Marks, president and chief investment officer of Marks Group Wealth Management*

The Benefits of Changing Firms



Source: WealthManagement.com. Survey of 336 advisors, February 2014

Advisors at wirehouse and insurance firms may have little control over the ways revenues are reinvested in the practice. For example, a portion of an advisory practice's revenue may be earmarked by the wirehouse or insurance firm for branding and corporate marketing. An RIA can offer advisors greater control to allocate revenue as they see fit. "They have earned the revenue, they want to determine where it goes," Enyedi said. "That's a big reason why advisors like the RIA model."

The RIA model also gives advisors the flexibility to grow their practice. An advisor may choose to add advisors or acquire another firm's book of business. In contrast, Enyedi noted that in his experience, wirehouse advisors typically don't grow through acquisition. They may also face hurdles when trying to add staff: Choice candidates may simply not want to work in a wirehouse environment, while others might have difficulty transitioning to a transaction-based practice.

Finally, the RIA model can offer the benefit of ownership, both during an advisor's time at the firm and during any transition or exit strategy. That's what helped drive Bennett Marks, president and chief investment officer of Marks Group Wealth Management, a Hybrid RIA in Minnetonka, Minn., to move away from the wirehouse environment. The RIA model allowed Marks and his partner John Feste to benefit directly from the practice's growth.

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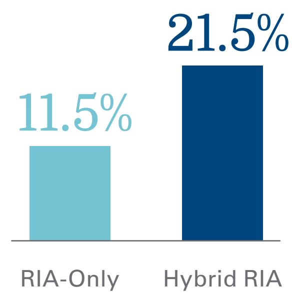
The Growing RIA Market

Growth trend data from January–December 2012



(Year-over-year AUM growth)

Source: Cerulli Associates, *RIA Marketplace 2013: The Changing Landscape of a Maturing Industry*, December 2013

HYBRID RIAS: A CUSTOMIZABLE SOLUTION

As advisors are becoming attracted to the flexibility of the RIA model, many are finding that the Hybrid RIA model can be easily tailored to fit the specific needs of their practice. What's more, the Hybrid model opens avenues for growth and client service beyond those offered by a fee-only RIA. Here are some ways Hybrid RIAs stand apart from fee-only RIAs:

- **A broader array of investment products:** Advisors moving to a Hybrid RIA have access to a wider range of investment products traditionally offered through transaction-based relationships, such as annuities. At a fee-only RIA, an advisor may need to refer clients to third-party brokers or other professionals to purchase such products, causing the advisor to forego a potential revenue stream.
- **An adaptable model:** A Hybrid RIA allows advisors to choose a structure that best suits their practice and clients. Enyedi noted that on average, LPL Hybrid advisors maintain a 70%/30% split between fee-based activities and commissions. However, advisors can adjust those ratios to best suit their practice, whether that means moving the bulk of their revenues to the fee-based side or the commission-based side.
- **Flexible revenues:** According to the LPL and WealthManagement.com survey, a major concern of advisors considering a switch is the cost of moving the practice and the potential for lost revenues, with 56% of respondents listing this as their primary worry. A Hybrid RIA can help smooth that transition by allowing advisors to retain trailing revenue on commission products.

MAKING THE HYBRID LEAP

Transitioning to a Hybrid RIA offers advisors the potential for flexibility and freedom. Yet before making this move, advisors need to consider where they want to take their practice. Is the goal to sit on the same side of the table as clients, or is the advisor more concerned about owning a personal book of business?

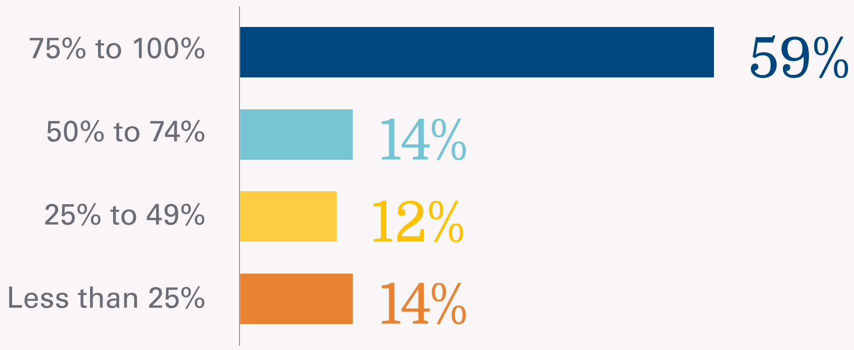
Diamond, who works closely with advisors during the transition process, said advisors must educate themselves about their options. "Going independent requires a tectonic shift in thinking," she said. "The biggest mistakes I've seen have happened when advisors chose to make a move without really doing their homework and without knowing their own goals and aspirations. The truly catastrophic part is that if you haven't taken that time to understand whether it's the right move, the impact is mostly on your clients."

Furthermore, Diamond said advisors need to ask themselves whether they are ready to run their own business. Advisors must handle their own profit and loss statements, hire staff, consider marketing strategies, and even handle finding office space and outfitting it with furniture. "Mentally, you have to have entrepreneurial DNA," she said. "Some people are just better suited to working in a turnkey environment."

In many cases, partnering with an independent broker/dealer can let advisors delegate key activities such as compliance, automated fee calculation and billing, and portfolio management and reporting. Marks and Feste chose to partner with a firm that could deliver custodial and broker/dealer solutions in part to streamline the client experience. They wanted clients to have assets with just one custodian, and one website where they could access all of their account information. "It's critical to find the right support," Bennett said. "Your business partner is your backbone. It's important to sit down, learn what they have to offer, and decide whether they're a good fit for your business."

Retention Rates

What percentage of clients stay during a transition?



Source: WealthManagement.com. Survey of 336 advisors, February 2014

Diamond said advisors planning a move must start the process well in advance. Doing so will help keep disruptions to the practice and the client base to a minimum. “It takes at least three months for a quality transition, and that’s a best case scenario,” she said.

Advisors can start by soliciting advice and guidance from colleagues who have gone through this process. They may also seek referrals to professionals such as custodians, compliance consultants, HR services, and transition consultants to help build a foundation for the move.

The transition to a Hybrid RIA can be challenging, but advisors who have done the legwork to plan and prepare for the move are well-positioned to earn the dividends of running their own firm. “We launched in the fall of 2008, and we’ve never looked back,” Marks said. “There’s a lot of appeal of being independent. Now, when clients walk in, it’s our name on the door.” ■

ARE YOU READY TO MAKE THE RIA MOVE?

Once you’ve made the decision to transition to an RIA, it’s time to start preparing for the move. Don’t rush the process: The transition period is a critical one for advisors, said Matt Enyedi, executive vice president, RIA solutions at LPL. “It’s very important to be thoughtful on the front end of this process,” he said. “If you’re hasty, you could make decisions that could have a long-term negative impact.” Here are several issues you should consider before making the move.

- **Rules and regulations:** Moving to an RIA often means taking on new compliance and regulatory responsibilities, from filing your own ADV form with the SEC to developing systems and policies to manage your books and records. Should you outsource that work or hire a dedicated staffer to manage these tasks? There’s no right choice—different approaches are appropriate for different types of practices. Here’s some advice: Solicit feedback from advisors who have made the switch to the RIA model about what worked for them, and what mistakes they made that you can hopefully avoid.

- **Technology:** Traditionally, independent advisors are responsible for handling their practice’s technology needs—from customer relationship management software to systems for trading and rebalancing. “You need to figure out how to navigate all those systems,” Enyedi said. “The right partner can help you seamlessly integrate solutions that will work for your business.” Again, depending on the size and style of your business, you may choose to outsource your technology needs or hire a chief technology officer who can implement—and manage—the appropriate systems for your practice.

- **Your book of business:** Transitioning to a new firm offers advisors an opportunity to be strategic about their book of business. Bennett Marks says that when he and his partner John Feste left a wirehouse firm in 2008 to launch Marks Group Wealth Management, a Hybrid RIA in Minnetonka, Minn., they transitioned most—but not all—of their clients. “This move offers a great opportunity to upgrade your book,” Marks said. “For some relationships that are difficult or aren’t generating much revenue, this is a good time to move them out of your practice.”

YOUR PRACTICE, YOUR WAY

However you envision the future of your practice or program, our comprehensive support and broad range of innovative business models can help you build and grow your business, your way. We understand that independence doesn't have one single meaning. Whatever lens you view your independence through, we are here to support and provide clarity to that vision. Here are just a few ways how:

- Become an RIA or Hybrid RIA and access our fully integrated platform and custodian services to address the varied needs of your clients
- Join an existing practice, bank, or credit union for established infrastructure, inferred credibility, structured support, and access to new referral sources
- Offer a suite of insurance solutions through our full-service, in-house insurance agency
- Specialize in retirement plans and leverage tools and resources built *by* retirement plan advisors, *for* retirement plan advisors
- Bring your team or build one—we offer customized clearing, advisory platforms, and technology solutions to help create efficiencies and scalability within your practice

We are 100% committed to your success. Give us a call today and put our capabilities to the test.

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