A Guide to Working with Registered Investment Advisor (RIA) Firms

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Introduction

This guide is designed to provide you with an overview and insights into one of the fastest-growing areas in financial services: the independent Registered Investment Advisor (RIA) industry. The guide is meant to facilitate an understanding of how RIA firms tend to structure their businesses, the types of services they provide and why they are attracting high-net-worth investors to their practices. The more you understand the independent RIAs world—with its unique challenges and opportunities—the better positioned you'll be to effectively work with RIAs. This guide was developed as part of GrowthPoint,® Schwab Institutional's integrated practice management program. It is intended to facilitate successful relationships between RIAs and third-party resources like you, and is part of our ongoing commitment to helping investment advisor clients grow and sustain their competitive advantage.

What is a Registered Investment Advisor (RIA)?

An RIA is defined as an individual or firm that is compensated to give advice about investing in securities including purchasing or selling securities, or issuing analyses or reports about securities. In many cases, RIAs are small professional businesses that are entrepreneurial in nature and often consist of professionals who may have worked at larger financial institutions but decided to go independent. An advisor's background may represent many different professions, including:

- Certified Financial Planner (CFP)
- Chartered Financial Analyst (CFA)
- Certified Public Accountant (CPA)

Why Do Advisors Become Independent?
The reasons RIAs choose to become independent are usually linked to:

- A desire to provide a broader range of products and services
- The ability to keep more of the revenue they generate and have more control over expenses
- The opportunity to build equity in—and realize the value of—the firm they're creating
- The desire for greater control of their business and the client experience they provide

Legal Considerations

RIA firms are registered with and regulated by the Securities and Exchange Commission (SEC) or their state securities regulator. (Generally, firms that manage more than $25 million in assets register with the SEC and must comply with the Investment Advisers Act of 1940; those that manage less than $25 million typically register with their state securities administrator unless certain conditions apply.) The registration process requires that the RIA candidate submit a registration statement called Form ADV. Currently, Form ADV is divided into two parts:

- Part I of Form ADV provides information about the advisor's education, business, and disciplinary history within the last 10 years.
- Part II provides information on an advisor's services, fees and investment strategies.

Note: Individual states may have additional requirements.

How do they structure their businesses?

RIA firm structures vary based on size, development stage and client service model. In terms of size, RIA firms can range greatly (e.g., from $1MM to $1B or more in assets under management [AUM]). As firms grow, they typically gain staff, increase departmental specialization, and define and develop their operations and administrative support structure. Larger firms often have multiple stakeholders, each empowered with decision-making authority. This is particularly important to understand as you nurture business relationships with these firms.

When it comes to their service delivery model, advisory firms typically fall into one or a combination of the categories listed in the table below. It is important to gain an understanding of the various models so that you can accurately depict their range of services and the process to deliver those services to their target clients.

Wealth Managers	Deliver advanced financial planning to HNW individuals, including asset/investment management, estate planning, tax management and trust services
Money Managers	Perform active trading and asset management for high-net-worth and institutional end clients
Family Offices	Offer comprehensive investment, wealth, and lifestyle management services for UHNV, multigenerational families with $10MM+ assets
Financial Planners	Provide comprehensive planning that includes income planning, estate planning, college planning and so forth, but do not necessarily oversee investments or otherwise implement the plans they create.

Source: Business Model Segmentation Analysis (2/20/08).

Who are their target clients?

Some RIAs manage assets for institutions such as mutual funds, pension plans, endowments or private investment funds, but many RIA firms concentrate on high-net-worth individuals. High-net-worth individuals are defined in many different ways, but a common definition is individuals with more than $1 million in net investable assets. Some small firms further focus on specific niche markets or practice specialties, such as those who work with corporate executives with concentrated stock positions, business owners or ultra-high-net-worth families.

What are their primary opportunities and challenges?

The opportunities for RIAs are clear and numerous. According to Schwab Institutional's 2007 RIA Benchmarking: Growth Trends Study, RIAs have achieved a median growth rate of 20 percent in AUM and 16 percent in revenues from 2003 to 2006. In that same time period, their median client asset level grew to $1.04 million—up 42 percent.

While RIAs are experiencing tremendous growth, managing this growth successfully is a challenge for many firms. Eighty-two percent of RIAs plan to grow aggressively or moderately over the next five years.[2] Top barriers to achieving these growth objectives include:

RIAs Gaining Share of Market
Today, there are approximately 16,000 RIAs in the U.S. with a total of $2.1 trillion AUM.[1] Once known as a cottage industry, RIAs are now a real force in the financial industry.

- **Time to focus on new business development:** Forty-five percent of advisors rate insufficient time for business development as their number one barrier to growth.[2]
- **Hiring talent:** Thirty-five percent of RIA firms are challenged with finding new employees to support their firms' growth.[2]
- **Marketing success:** Approximately 30 percent of RIA firms believe investment in marketing and executing a successful marketing plan is another hurdle in their growth plans.[2]

Understanding these challenges up front may help shape your relationship with these firms—providing insight into which solutions will be appropriate and actionable for them at this time.

[1] Schwab Institutional estimates, Cerulli Associates, 2007.

[2] Schwab Institutional 2007 RIA Benchmarking: Growth Trends Study.

Challenge	Description
Time	Having enough time—and dividing it appropriately among business development, planning, operational functions and client service—was reported to be the number one challenge for RIAs.[2]
Staffing	Attracting and hiring the right employees at the right time, and knowing when and how to outsource activities, was cited as the second-greatest challenge for advisors.[2]
Prospecting Success	Finding effective ways to consistently attract new clients and close new business was reported as the third-largest barrier to growth.[2]
Marketing Expertise	Not many RIAs have dedicated marketing staff, and very few would claim to be marketing experts. As such, many are looking for assistance determining which strategies are most effective and how they should prioritize and implement the tactics they pursue.
Budgets	As firm owners, they struggle with budgetary concerns—and want to ensure that they're getting the greatest value for their dollar and that there is clear return on investment (ROI).
Generate Awareness	Lack of top-of-mind awareness and familiarity with a firm's brand sometimes makes it difficult for clients to evaluate their experience, trustworthiness and qualifications.
Credibility	As consumers grow more informed, they also grow more demanding. A firm's overall messaging must immediately communicate credibility, trustworthiness and high-touch service.
Process	RIA firms reach critical thresholds throughout their life cycles, frequently when they realize annual revenues of around \$2 million and again around \$5 million.[3] As they reach those size thresholds, operations and processes become the center of many discussions. Developing disciplined processes can help set a path for growth, articulate measurable goals and assign accountability to key personnel.

[2] Schwab Institutional 2007 RIA Benchmarking: Growth Trends Study.

[3] McCarthy, Ed, "It's not a matter of being bigger; it's about being better," *Wealth Manager,* October 2007.

Who are their competitors, and how do RIAs differentiate themselves?

The RIA industry—and the overall financial services industry—has become intensely competitive. Among the various players vying for client assets are full-commission brokers, also known as wirehouses, seeking to reinvent themselves as fee-based advisors. Similarly to RIA firms, these wirehouses typically offer investment advisory services, but may also provide investment banking services and use a commission-based model. More indirect competitors include professional groups such as CPAs and Bank Trust Departments.

This level of competition makes it essential for RIAs to have a clear understanding of their ideal client—and how their firm sets itself apart to stand out in the marketplace.

The Unique Attributes of RIA Firms
There are some noteworthy and common attributes of RIA firms that differentiate them from competitors mentioned above, which are important to understand when working with them.

Independent
Many RIA firms are independent, which means they own the business and are not employees or agents of a large financial institution. RIA firms generally charge a fee for their services, rather than commissions on the sale of investment products. RIAs are not required to promote proprietary products and have greater control of the products and services they offer their clients. In addition, because RIA firms bear fiduciary responsibility, they are legally bound to act in the best interest of their clients.

Flexible, Fee-Based Compensation

Fee structures vary among independent RIA firms. Most charge asset-based fees that are designed to align their interests with those of their clients. As the account size grows, so does the advisor's compensation. However, some independent RIAs are offering alternative fee structures to accommodate client needs; these may include fees for financial plans, annual or retainer fees and hourly fees. Regardless of how they charge, RIAs are obligated to disclose all fee arrangements prior to entering into the client relationship.

Tailored, Personalized Approach

RIAs take the time to conduct a detailed analysis and evaluation of their clients' financial goals and investment timelines and create customized strategies and solutions to meet them. Those solutions can range from determining a client's risk profile and asset allocation to developing more sophisticated solutions—like trusts, concentrated stock strategies and charitable gifting programs. Often, at the beginning of a relationship, RIAs will define service-level agreement parameters, setting expectations for the frequency and type of communications that will be provided to clients.

Fiduciary Responsibility: In a Client's Best Interest

As a fiduciary, an investment advisor has an affirmative duty of utmost good faith to act solely in the best interests of his or her client and to make full and fair disclosure of all material facts, particularly potential conflicts of interest.

—**Thomas P. Lemke and Gerald T. Lins, *Regulation of Investment Advisors*, Thomson West, 2007.**

Discretionary Management

RIA clients may sign a Limited Power of Attorney (LPOA), authorizing an advisor to buy and sell securities on behalf of a client without the client's trade-by-trade notification or advance approval.

Credibility

Many RIAs have come from larger financial institutions and offer years of experience and specialized expertise. Some may have credentials such as CFP, CFA or CPA. This means they have met the rigorous experience, education, examination and ethics requirements of the educational institution from which they obtained their qualification.

What are the best practices to consider as you engage with RIA firms?

Present a Clear and Comprehensive Request for Proposal

You are most likely familiar with receiving a Request for Proposal (RFP) and Statement of Work (SOW) from potential or existing clients to help them narrow the field and choose the best service provider to meet their firm's needs.

As you seek to present your firm to an RIA, there are some points you should consider. RIAs are not necessarily self-described business managers or marketers. This doesn't mean that they don't fully grasp or appreciate the drivers of their businesses—quite the opposite. What it does mean, however, is that you may want to take extra steps to help them see the value of the proposed solution—linking it back to firm goals and illustrating how it will help fuel profitability and growth. RIAs are savvy business owners and entrepreneurs; they're looking to maximize revenue while minimizing cost and won't risk a large investment without a measurable payoff.

Request for Proposal Writing Tips

- **Be concise**—RIAs are often time-starved, so the more direct your language, the better.
- **Avoid jargon**—Such language may come off as "fluffy" or lacking substance or meaning.
- **Use facts**—Where possible, link return on investment and success measures back to firm goals.

In addition, many advisors will appreciate it if you bring knowledge of best practices to the table and work with them to understand and refine their needs. For example, an advisory firm may engage a marketing agency based on an immediate need (e.g., "I need a high-quality capabilities brochure"), but upon further analysis, the problem isn't the quality of their collateral. The real issue is the clarity and differentiation of their story as well as how their marketing materials are supporting their sales process. Providing such strategic guidance will be valued and can help foster a long-lasting, rich relationship.

The People

When describing members of the project team, be sure to provide full definitions of roles and responsibilities and what percentage of their time will be devoted to the project. An RIA firm may not be familiar with various roles, and providing this information, in addition to biographical information and an organizational chart, will offer transparency into the process and help set expectations.

The Process

Some RIAs are likely to have little or no knowledge of the project process. When you respond to an RFP or SOW, be sure to communicate your firm's distinctive approach to providing solutions and answer in a way that shows the RIA that you understand his or her business. For instance, let's use the above marketing example of developing a capabilities brochure. Instead of simply saying you will produce a beautiful brochure, explain how the piece will enable the RIA to present their unique value proposition to prospects.

Also, when describing how the working teams will interact, try to be as specific as possible—outlining how often the teams will meet, where they will meet (via phone or in person), how feedback will be gathered, and how to account for compliance or other issues during the review process.

Questions an RIA Typically Considers When Evaluating Your Proposal

- Do they know my business?
- Do they understand my issues and goals?
- Do I understand their solution?
- Do I like what they have done for others?
- Do I trust their team to deliver on the solution they're recommending?
- Can they capture my firm's unique point of view?
- Can they effectively manage the review and revision process?
- Do they have the manpower to provide the service I need in the time frame I'm looking for?
- Is their estimate reasonable?
- How will I measure my return on investment?
- Does this support my business goals?

The Service or Product

Be very clear about the service or product you are providing and what the exact deliverables will be throughout the process. This means being specific about the number of drafts, at what point copy and design will come together (if applicable), and how the review process will be managed. When describing the deliverable, ensure that you are clear on exactly what the RIA is getting and when. For example, the end deliverable could be a marketing plan, analysis report, recommendations or creative art files. If there are multiple steps in the process, provide a project plan that details when each task is due and specify the file type of each deliverable (e.g., Word, PowerPoint, PDF).

The Price

However you choose to price your services, it is important that your fees be clearly communicated. If you prefer to work on a monthly retainer, explain what the monthly amount covers—and also what it does not. If you prefer a flat project fee, specify the number of revisions or the processes that are included. If you're working on time and materials, outline a general estimate for how long you expect the work to take and provide regular updates as you proceed.

It is also important to be up front about any additional costs that might be incurred throughout the development process and provide a general estimate of how much you think these will be. For example, marketing projects might include things like professional printing, travel costs, photo purchase, and so forth. The closer your end costs come to the original estimates, the more credibility you build with the firm.

Once You've Won the Business

Once you've won the business, it's time for the kickoff. This is where you explain your strategic and creative process and present a comprehensive project plan that outlines key milestones, sets expectations for weekly check-ins and allows key stakeholders within the firm to become familiar with your working team. Bear in mind that principals are busy individuals for whom servicing clients will always come first, so RIAs will appreciate assertive project management to ensure that projects continue to move along and are completed within the set time frame. Also, RIA firms often have multiple stakeholders, so your timeline and review process should include all appropriate parties. This will ensure that everyone in the firm buys into the final product and will make the process more streamlined.

The kickoff is also a good time to make sure that everyone agrees on the key assumptions that will form the foundation for the direction of the project. It also provides a forum for team members to ask questions and get clarification on the ongoing development and approvals process.

A Few Resources

Before engaging with an RIA firm, you'll want to do your homework. We suggest familiarizing yourself with the firm's capabilities, their service delivery model and the overall competitive landscape—identifying both primary and secondary competitors. The following resources can help you gain a deeper understanding of the RIA industry and the opportunities it offers. The more you learn about the independent advisor business, the more effectively you will be able to communicate your value and expertise.

Publications

Investment News	A weekly publication for financial advisors that provides news and information about the financial services and investment industries.	**investmentnews.com**
Journal of Financial Planning	The official publication of the Financial Planning Association, published 12 times a year to members. Its goal is to foster informed dialogue and enhance the knowledge and understanding of the technical and practice management challenges facing the growing community of financial planning practitioners.	**fpajournal.org**
Financial Advisor Magazine	A monthly publication for independent broker-dealer-affiliated financial planners and registered investment advisors.	**financialadvisormagazine.com**
Investment Advisor Magazine	A monthly publication that offers news, information, and demographic and social trends on a range of topics including wealth management, alternative investments, retirement planning and practice management.	**investmentadvisor.com**

Institutions

National Association of Personal Financial Advisors (NAPFA)	An organization of fee-only comprehensive financial planning professionals. Individuals join NAPFA to enhance skills, market services, and be a part of a collective, influential voice on matters that affect them and their clients.	**napfa.org**
Investment Adviser Association	A nonprofit organization that exclusively represents the interests of SEC-registered investment advisor firms.	**investmentadviser.org**
National Endowment for Financial Education	A private, nonprofit, national foundation wholly dedicated to improving the financial well-being of all Americans.	**nefe.org**
Financial Planning Association (FPA)	A Web site that helps practitioners succeed as financial planners by cultivating the body of knowledge for financial planning, sharing best practices and encouraging professional development.	**fpanet.org**
Schwab Institutional	Our public site provides more information about our history, focus and commitment to the RIA industry. Through a secure login, Schwab Institutional offers RIA clients a variety of tools, resources and intelligence to help them run their firms more efficiently.	**schwabinstitutional.com/public**

Conclusion

The RIA industry is currently experiencing unprecedented levels of growth, which we believe represents many opportunities for RIA firms but also presents challenges as they try to manage their rapid growth. RIA firms will be looking to engage with you for your expertise, with the expectation that you will have an understanding of their business. We hope this guide is a good first step and wish you every success as you begin to engage with RIAs.

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