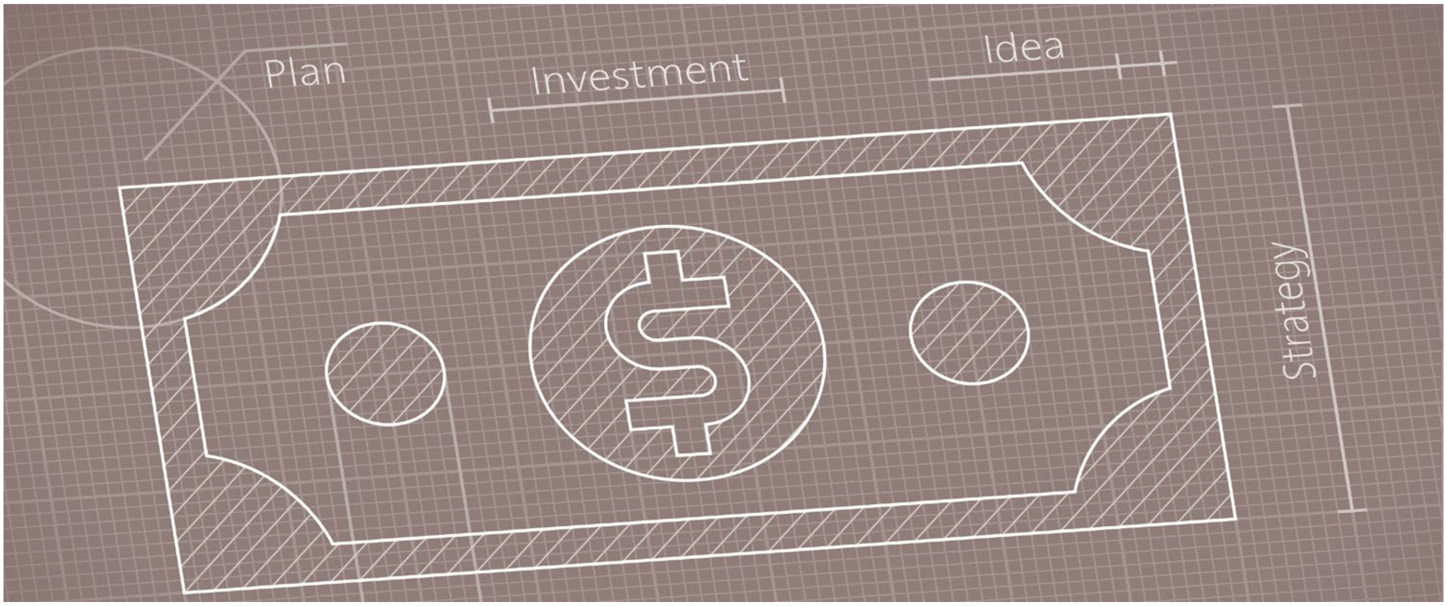
TRANSITION TO RIA



11 Ways The Economics Of The RIA Model Are Superior To Other Advisor Affiliation Options

The economic advantages of the Registered Investment Advisor ("RIA") model versus other affiliation options are a key component to why financial advisors transition to the model. This whitepaper explores 11 ways the RIA model provides superior economics to you as a financial advisor.

By Bradford N. Wales

Bradford N. Wales is the founder and principal of TRANSITION TO RIA. He has nearly 20 years industry experience, including direct RIA roles in compliance, finance, and business development. He has a B.S. and MBA, and has held multiple industry licenses (4,7,24,63,65).

11 Ways The Economics Of The RIA Model Are Superior To Other Advisor Affiliation Options

1. Higher Payout

As your own Registered Investment Advisor ("RIA"), you receive 100% of the advisory fees you charge your clients. It is not really a "payout" in the true sense of the word. For most advisors, "payout" is what is remitted to them after 100% (i.e., "gross") of the advisory fee first goes to the firm they're affiliated with, their firm deducts a portion, and then what is remaining is remitted on to the advisor ("net").

With your own RIA, though, the custodian is simply processing the fees on your behalf. You instruct the custodian how much to deduct from each client's account (for your fee), the custodian deducts each amount, and then remits the aggregate balance back to you in full. These fees are never considered "revenue" for the custodian, and likewise never appear on a custodian's Profit & Loss statement ("P/L"). For lack of a better term, the process of the custodian deducting the fees and remitting them to you is essentially a *courtesy* to make the process easier for both you and the client.

As an example, assume you charge your clients a 1% advisory fee, billed quarterly. You, in theory, could each quarter send your clients an invoice for their quarterly fee, and have them in return mail you a check for the fee amount. Under this scenario, those funds would (correctly) never flow through the custodian. The transaction is solely between you and your client.

Now realistically speaking, for both the ease of the RIA and client, such an approach is generally never utilized. Instead, fees are usually deducted directly from a client's investment account and remitted to the RIA. Under this latter scenario, though, it is no different for the custodian (from a P/L perspective) than had you sent invoices, and collected checks on your own. The advisory fees never flow to the custodian, and thus they are never remitted to you through any "payout" arrangement. The custodian is merely processing fee deductions on your behalf.

You keep 100% of your advisory fee. "100% payout" is still a common phrase used to describe this arrangement, even if that is not what is technically occurring.

Now from this 100%, you then need to deduct the expenses of running your RIA, to determine your final bottom-line take-home pay. In the pages to follow, I describe several ways your ability to control your expenses will significantly increase your bottom line take-home.

You keep 100% of your advisory fee. "100% payout" is still a common phrase used to describe this arrangement, even if that is not what is technically occurring.

At a macro level, though, a reasonably sized, reasonably run RIA can generally expect to net (before owners' compensation) in the range of 60-70% after expenses. For the example to follow, we'll assume a take-home amount of 65% (the mid-range.)

I invite you to then compare this 65% post-expense "payout" to what you are receiving from your current firm. Which as I frequently remind advisors I talk to, this exercise is not as easy as it at first might seem.

For simplicity's sake, let's assume you are at a wirehouse firm, and per the "grid," your payout is 45%. Now to be fair, we should add in a few extra % points for things like retirement plan contributions your firm might make on your behalf. So, for example, let's increase that to a hypothetical 47%.

The spread between our target 65% (as your own RIA) is favorable to the 47% you are receiving from your wirehouse firm. That alone drives home a significant increase in take-home you could receive as your own RIA.

However, this 47% wirehouse "payout" comparison is almost guaranteed to be overstated. While the "grid" might say you receive 45% (plus an extra few % points for other items), you are almost guaranteed to be receiving less than that.

Depending on the firm you are at, most large firm comp plans have additional deductions that cannot be overlooked from the calculation. Examples: some firms have a lower (or even 0%) payout on accounts under $X in size; some firms have a 0% payout on any family related accounts; some firms pay nothing on the first X% in production each month; some firms have a lower payout ("penalty") if you haven't implemented a financial plan with the client or sold them a banking product; some firms charge some sort of initial bps "platform" fee and only after that is deducted then the remaining amount is sent through the grid; some firms reduce your payout if/when you discount a client's advisory fee; some firms involuntary defer part of your income years into the future as deferred comp, etc.

Depending on the composition of your book, and the way you run your practice, after you factor in all of the potential variables designed to reduce your comp, your 47% initial grid "payout" might be something like 42%.

Point being.... the "spread" between what you are actually receiving currently and what you generally could expect to receive as your own RIA (~60-70%), is usually larger than at first would even seem.

Takeaway: Calculate the dollar amount difference of what your current (actual) bottom-line take-home is compared to what you could typically expect to receive as your own RIA?

2. No Comp Plan Changes

If you are working at one of the large traditional ("captive") brokerage firms, the flexibility you have to run your practice as you see fit is significantly narrowed vs if you were running your own firm. But it is wise for such advisors to still strategically approach their practice as if it was its own standalone business as best they can. Set annual goals for themselves. Craft strategies on how to achieve those goals. Etc.

While every business must adapt to the changing landscape in which they operate, captive advisors are challenged by an extra burden: frequent changes to their comp plan, sometimes as often as annually.

It is nearly impossible to maximize a growth strategy for your practice (and thus increase your income) when perhaps every year, a key variable (how you are compensated) continues to fluctuate. This frequent "moving of the goalposts" creates an environment not at all conducive to having a foundation upon which you can strategize for growth.

Examples:

- One year you are compensated on accounts of at least $X in size; the next year, that hurdle has perhaps risen and you are now no longer paid on those accounts (and/or now at a lower grid rate.)
- One year you are paid for working with your clients as you have been for many years now; the next year, unless you implement a financial plan for them (or perhaps cross-sell some sort of banking product), you are now paid less on that exact same client.
- One year you are paid a grid rate of X%, for having production of $Y; the next year, even if you produce the same $Y in production, you are perhaps now relegated down to a lower grid rate than the X% you received previously.
- One year, the structure of your team qualifies you for a grid rate of X%; the next year, that exact same team composition/arrangement no longer qualifies for the same rate.
- This all also overlooks that these comp changes often force you to utilize products and/or services with your clients you might not otherwise choose or desire to on your own based on what you feel is best for the client themselves.

Perhaps some sort of banking product is best for a client. Or perhaps creating/implementing a formal written financial plan is a good service offering for certain clients. However, it would seem more prudent to allow the advisor/client relationship to dictate when, and if, such tools/offerings should be introduced into the relationship. Instead, many comp plans mandate such implementations. And if not rendered, the advisor is, in return, compensated less.

Combine the frequently moving goalposts, coupled with often required implementation criteria, and it simply does not provide for an environment in which an advisor can maximize their growth (income) potential.

Takeaway: Could you grow your practice faster if you were no longer constrained by the terms of (an ever-changing) comp plan mandated upon you?

3. More Flexibility On How To Charge For Services

As your own RIA, you have significant more flexibility on what services you wish to offer to your clients, and likewise how you want to charge for those services.

As an RIA, you have the ability to (among others) charge:

- **A fee based on a % of the client's assets** (e.g., 1% of AUM). Further, you have full flexibility to determine exactly how you want to assess the fee (quarterly, monthly, in advance, in arrears, etc.) as well as exactly what the pricing tiers of the fee schedule will be.
- **Flat fees** (e.g., $2,500 for a financial plan)
- **Hourly fees** (e.g., $300 per hour)
- **Retainer fees** (e.g., $500 per month)
- **Fees on assets held elsewhere** (e.g., $350 to review/advise on 401k account)
- **"Floor" pricing** (e.g., 1% of AUM, with a minimum of $1,000 per quarter)
- **Performance-based fees** (e.g., 1% of AUM + 20% of profits above benchmark). Note: While it is generally uncommon to see RIA's utilizing performance-based fees, done properly, it is a viable option of the RIA structure.
- **Plan level fees** (e.g., 0.20% of plan assets for advising a business on their 401k at the plan level.)

As your own RIA, you have significant more flexibility on what services you wish to offer to your clients, and likewise how you want to charge for those services.

Having the ability to introduce various fee options provides advisors the opportunity to work with, and generate revenue from, additional clients they might not otherwise currently be able to. Examples:

- So-called "HENRYs" (High Earning, Not Rich Yet). An example might be a new doctor. Revenue from an AUM fee alone might not make the relationship profitable, but "HENRYs" are often able and willing to pay via some sort of flat/retainer/hourly type arrangement instead for your advice and services.
- Clients that won't (or cannot – think: some trust scenarios) move assets to the advisor's firm/custodian.

Takeaway: What sort of fee arrangements would you consider adding (or modifying) to your practice if you had the flexibility to do so?

4. Ability To Control Expenses Yourself

The more you can control your costs and tailor the cost structure to the specific practice you desire to have, the more income you can drive to your bottom line.

As your own RIA, you cover a spectrum of expenses that your current captive firm most likely now covers for you. Examples of these include:

- Office rent
- Benefits
- Staff salaries
- Office overhead
- Retirement plans

At first glance, many advisors are concerned about what each of these might cost, let alone what the aggregate total might be. However, there is a better way to contemplate this expense obligation.

Assume you are at a firm producing $1,000,000 per year, receiving a 40% grid payout. Which as noted prior, the payout % figure is most likely something lower. However, for this example, we will assume you are receiving the full 40%.

For your services producing $1,000,000 in gross, the firm pays you out $400,000. Or put a different way, they retain $600,000 to cover the overhead expenses. The question therefore is…. if you were instead in charge of covering your own expenses (such as those listed above), could you do so for less than $600,000? And consider that for every $ under $600,000 you spend, that $ flows directly into your pocket as additional income.

I often find this is simply a mental adjustment, as the math speaks for itself. Make no mistake, you are already paying for each of the above items as part of what your firm is retaining via the payout grid. In this example, you are simply paying a flat 60% of your gross for the luxury of not having to pay an itemized bill you would otherwise have individualized control over.

With this individual control, you have complete influence over exactly what expenses you do, or do not want to pay for. The more you can control your costs and tailor the cost structure to the specific practice you desire to have, the more income you can drive to your bottom line.

Takeaway: How much are you paying to your current firm for overhead, and do you feel you could manage that cost better yourself?

5. Ability To Deduct Business Expenses

With the prior focus on controlling your own expense levels, it is also important to recognize the economic benefits of expensing such items under the structure of your own business.

Provided the costs are recognized expenses by the IRS, the ability to deduct such expenses can meaningfully reduce your bottom-line taxable income.

Provided the costs are recognized expenses by the IRS, the ability to deduct such expenses can meaningfully reduce your bottom-line taxable income.

A telling example relates to a two-person advisor team previously at a traditional wirehouse firm. Both advisors were members of a local social club. (ex: golf club, country club, etc.) They established their club memberships initially/primarily for their own personal benefit, and thus were paying the club dues/expense from their after-tax income.

However, over time they increasingly invited existing and prospective clients to join them at the club (perhaps for a meal, round of golf, meeting, etc.) Upon starting their own RIA, they can now expense most of these same dues/expenses they were previously having to pay for with after-tax funds, but can now record as a business expense, thus reducing their taxable income.

Further, their clients have become so fond of meeting the advisors within the club's meeting facilities (which the advisors have access to as club members), that the advisors are considering reducing, if not eventually outright eliminating their current (rented) office footprint. Instead, the advisors would use a virtual approach coupled with the club facilities for physical meetings when needed.

So not only are the advisors potentially reducing the expense of their RIA in general (their existing office footprint), they can also deduct certain expenses as business expenses, thus further increasing their after-tax income.

Takeaway: What expenses do you currently incur yourself that you could instead deduct as a business expense (thus saving on taxes) if you transitioned to your own RIA?

6. Flexibility To Save On Taxes Via More Optionality With Retirement Plans

Some options could result in a significant increase in the amount you can contribute to such tax-deferred accounts.

As your own RIA, you have optionality with which sort of retirement plan you want to implement as a small business owner. Some options could result in a significant increase in the amount you can contribute to such tax-deferred accounts.

Of note is your ability to maximize both the amount you contribute as a plan participant yourself (employee), and what the level of matching firm contribution is. While all plans still have IRS-mandated deferral limits, with some plans the maximum firm contribution level is higher than simply the employee contribution alone.

As your own RIA, you can potentially defer significantly more income on a tax-deferred basis, than you could solely as an employee of another firm's plan.

And to be sure, this "deferred compensation" is different from the "deferred compensation" that is potentially forced upon you under your current firm's comp plan. Under the latter, that is usually simply withholding already earned income from you and not paying it to you until a later date, all usually without any sort of additional long-term tax benefit.

Whereas instead with the above RIA scenario, is your ability to decide on your own to defer compensation to lower your current-day tax obligation and potentially grow your wealth for decades on a tax-deferred basis.

Takeaway: If you had the optional ability to contribute more of your income into a tax-deferred vehicle, would you do so?

7. Operating Leverage

The cost structure of a typical RIA provides a meaningful opportunity to take advantage of "operating leverage". Now to be sure, operating leverage exists in your current affiliation model as well. The question is, who is the one able to take advantage of it today? You or the firm you work for?

Most costs associated with running your own RIA are "fixed" costs. Examples include office rent, staff salaries, compliance, etc. The "variable" cost of adding one additional client is usually almost zero. Now granted, at some point, if you add 50 new clients, 100 new clients, etc., at some point, you might need to add another member to your staff (as an example).

However, going from 150 clients to 151 clients, or when an existing client's account simply increases in value, usually results in little additional variable cost to the firm. Once your revenue exceeds your fixed costs, the incremental additional revenue you generate flows almost entirely to the bottom line as income.

Now note, if you are an employee advisor at a large traditional firm, this phenomenon is already occurring. Here, your firm is the one benefiting. They pay for your fixed costs, and in return, are retaining 60% (for example) of your production for that responsibility. However, once that 60% contribution to the firm exceeds what it takes for them to cover the fixed costs of having you as an advisor on their platform, every additional $ of that 60% flows almost entirely to their bottom line.

Let's consider a few examples:

- If you grow your production by 20%, does your firm give you a 20% larger office?
- If you grow your production by 20%, does your firm give you 20% better healthcare insurance?
- If you grow your production by 20%, is your firm giving your sales assistant a 20% raise?

The answer to the above is, no. Instead, once your main fixed costs are covered, all of the incremental additional production you bring in (and which they retain X% of through your payout) is almost entirely bottom-line profit to them. Which is why they are so interested in seeing you continue to grow your production.

Your own income potential maxes out at the top grid payout level. Which, for example, let's say is 48%. Once you reach that payout level, whether you add 1 additional client, 10 additional clients, or 100 additional clients, you will still only be paid out at the same 48%. You receive no benefit from the operating leverage of your growth.

Whereas instead, if you started your own RIA, you would be the one able to benefit from operating leverage, not your current firm. As noted previously, as your own RIA, you have much more control and flexibility over the expenses you incur for your practice. The majority of which will be fixed costs. Once you exceed those fixed costs via your revenue flows, operating leverage starts to grow your bottom-line income exponentially.

Takeaway: Do you plan to grow your practice to be larger than its current size? If so, who would you rather benefit from the operating leverage that will result from that? You, or the current firm you work for?

8. More Flexibility = Faster Growth

I like to frame the "more flexibility" explanation by referring to "two sandboxes". This harks to the saying that we must play within the sandbox. Here, there is a larger sandbox, and then a smaller one within it.

The large sandbox is the "regulatory" sandbox. All advisors must play within the regulatory sandbox. Now some advisors are beholden to FINRA rules, others SEC rules, and still others that must adhere to both. Regardless, the regulatory sandbox is fairly black and white. If a rule says you can't do X, then you can't do X. It doesn't matter what kind of firm you are at, or what size firm, etc. If the rule says no, the answer is no. So, all advisors play equally within that sandbox.

However, within the regulatory sandbox is a smaller (sometimes much smaller) "firm policies & procedures" sandbox. This sandbox represents the individual policies and procedures set by the firm you work for. Case in point, if you work for one of the large traditional brokerage firms, you work for a firm that must establish policies & procedures for you and the thousands of other advisors at the firm. This is where the sandbox shrinks in size and closes in on you.

I like to frame the "more flexibility" explanation by referring to "two sandboxes". This harks to the saying that we must play within the sandbox. Here, there is a larger sandbox, and then a smaller one within it.

Just because a regulation says you can do X, does not necessarily mean that your firm feels they can properly supervise thousands of their advisors actually doing X. After all, with thousands of advisors, there are surely some very experienced advisors within the group, right alongside some extremely not-so-experienced advisors. Firms generally are forced to establish "lowest common denominator" policies and procedures to fully encompass the entire spectrum of experience levels of their advisors as a whole. While this is not much of adherence to the actual lowest common denominator advisor at the firm, it is essentially a handcuff on all of the remaining advisors, and certainly those on the more experienced end of the spectrum.

As an example, consider an advisor who I consulted for previously who worked at one of the large traditional brokerage firms. For business development reasons, he wanted to create YouTube videos of himself explaining financial planning topics to demonstrate his expertise to attract prospective clients.

There is no regulatory rule that says he could not do this (i.e., the "regulatory" sandbox.) However, his firm did not feel they could adequately supervise their thousands of advisors making such videos. Now to be sure, the advisor I was working with clearly had the experience and good judgement about what should or should not be included in such videos. However, there were arguably many of advisors amongst the thousands of others at his firm that did not have such clear capabilities. As a result, his firm told him he could not proceed with the videos (i.e., the smaller "firm policies & procedures" sandbox.)

This should not come as a surprise, though. Imagine if you were the Chief Compliance Officer of one of the large traditional brokerage firms, and hence you are responsible for establishing policies and procedures to adequately oversee thousands of advisors at that firm. When faced with such a dilemma, and knowing your job security is based on your ability to minimize the firm's risks, saying no to making videos is probably an easy decision. That, however, is small consolation to the advisors that would indeed have used them responsibly.

Now compare this to the "sandbox" if you started your own RIA. Yes, you would still have to play within the "regulatory" sandbox, but your "policies & procedures" sandbox can potentially be a lot more flexible than that of the large traditional firms. After all, the large firms must establish their policies and procedures based on the experience, knowledge and trustworthiness of thousands of advisors (which inevitably includes some bad apples). With your own RIA, though, you only must consider yourself and any other advisors at your particular RIA when establishing such terms.

Likewise, the advisor wanting to utilize YouTube videos left his large traditional firm to establish his own RIA. He was then able to make such videos as his own smaller RIA firm could completely use such a business development strategy responsibly.

Point being with all this, consider what sort of additional strategies you would implement within your practice if you were not held to the lowest common denominator standard of your large existing firm. What strategies would you use to increase your client prospecting activities, your client retention activities, your referral generation activities, etc.? More flexibility inevitably increases your ability to grow at a faster pace. More growth equals more income and a higher value for your firm.

Takeaway: Next time you are told you cannot do something at your firm, ask yourself if it is because the "regulatory" sandbox does not allow it, or because the lowest common denominator "policies & procedures" sandbox is unfairly grouping you in with much less experienced advisors and thus limiting your options unnecessarily.

9. Eventual Exit Strategy Part 1: Valuation

While you may not currently be planning your exit from the business, such a step will arrive for all advisors eventually. And when it does, you will want to maximize the value of your life's work. For most advisors, that involves decades of building their practice into what it is today. Decades of hard work. Decades of working through market cycles. Decades of having to make sacrifices (including time with family) to build their practices. You deserve to be the one who gets to maximize the value you have worked so hard to build. You will generally receive a (meaningfully) higher enterprise value for your practice as your own RIA.

Over time, valuation methodologies have changed and been refined. What once was a simple multiple of T12 production calculation, is now generally a more robust process involving a deep dive into the client base, expenses of the practice, growth trajectory, etc.

While many of these variables are consistent across different affiliation models, owning your own client "book" as your own RIA undeniably increases the value of your practice. After all, consider if you are a buyer looking to acquire a practice. Would you rather attempt to buy an advisor's practice who is currently captive to a traditional employee firm where the firm feels they, and not the advisor, "owns" the clients? Or would you rather buy a practice already 100% independent and where there is no question on who owns the practice, and the portability of the clients?

As the latter provides for a lower risk for all parties involved, a higher probability of success, and a better experience during a sale process for the clients, advisors and office staff, a premium on price can naturally be attached to such a scenario.

While no longer as common of a valuation method, a multiple of T12 provides for an easy case example. Most of the large traditional brokerage firms provide some sort of "sunset" or "retirement" type programs to their advisors. Under these structures, a "sunsetting" advisor partners up with an (often younger) advisor to hand their client book off to. In return for this, the sunsetting advisor is provided a level of compensation. This compensation is often derived based on a % of existing T12 production, and perhaps also some sort of Length Of Service (LOS) component.

(As an aside, also note that firm sunset programs generally have a very rigid structure. They must be entered into in a certain way, they have a firm derived timeline, the payout must follow a prescribed payment structure, etc. Even discarding the financial benefits alone, transitioning your practice as your own RIA also significantly increases the flexibility in exactly how you want to structure your eventual planned exit.)

Based on a prescribed calculation method, a traditional firm might offer one of their sunsetting advisors, perhaps 150% of their T12, usually paid out over a number of years. Or put another way, a multiple of 1.5 as their practice valuation. Whereas that same sized practice as an independent RIA might generate a sale value closer to perhaps a 2.2 multiple (or higher). Again, the added benefits, flexibility, and

You deserve to be the one who gets to maximize the value you have worked so hard to build.

lower risks of an independent practice transaction allow a seller to command a higher sales premium.

Likewise, it is highly likely that exiting the business as your own RIA will result in significantly more flexibility regarding when/how you do so, and will result in a significantly higher financial reward for your decades of hard work.

Takeaway: For potentially a higher enterprise sales value, would you consider moving to the RIA model to fully benefit from your life's hard work?

10. Eventual Exit Strategy Part 2: Taxes

To add further to the prior point regarding the higher enterprise values placed upon the sale of a practice under an RIA umbrella, it is also important to consider the tax benefits of doing so as well.

This point is all too often overlooked by advisors, in part because their existing (captive) firms certainly do not proactively make them aware of it.

In a typical "sunset" arrangement (discussed in the previous section), the departing advisor is to receive a sum of money, usually paid out over a number of years. The key with this, though, is that each payment will be paid out to the advisor through the normal W2 payroll process. Or put another way, such payments will be personal income, and be taxed to the advisor at personal income tax rates. Depending on your overall aggregate income, and potential additional state/city taxes, for some advisors, this can run to perhaps a 50% tax rate.

To the contrary, if/when you sell your practice as an RIA, you can typically structure the deal so that ~85% of the sale price will be taxed at a capital gains tax rate, while only the remaining ~15% is taxed at personal income tax rates. Now, there are a multitude of reasons this 85/15 split might be an 80/20 split, or a 90/10 split, etc. However, usually the final negotiated sales agreement prescribes a roughly 85/15 split on tax treatments.

In other words, 85% might be taxed at the much lower capital gains tax rates (perhaps ~20%), and only the remaining 15% at the higher personal income tax rates (perhaps as high as 50%).

The key is you need to consider the "after-tax" benefit of selling your practice, not just the practice valuation itself.

Example:

Let's assume you have a practice generating $1,000,000 in T12 production. You are in the (to use simple numbers) 40% personal income tax bracket; 20% capital gains tax bracket.

The valuation of your practice is almost certain to be higher as your own RIA. But to further drive home the importance of considering taxes on your exit strategy, we'll use an example where the price your existing captive firm will pay you via a sunset program, actually matches what you could get as your own RIA. (Which again, the RIA valuation likely would be higher than the captive sunset valuation. But for discussion's sake, we'll assume they are the same.)

In this example, we will assume you can get a 1.5 multiple on your T12 (from both the sunset, as well as RIA valuation). You will be paid $1.5mm for your practice. Under both scenarios, the proceeds are usually received over time, but that rarely impacts the math on this example.

In a typical "sunset" arrangement, the departing advisor is to receive a sum of money, usually paid out over a number of years.
The key with this, though, is that each payment will be paid out to the advisor through the normal W2 payroll process.

Under the captive sunset plan, you would be taxed on the $1.5mm at the 40% personal income tax rate, which after-tax would net you $900,000 ($1.5mm X 60%).

Under the RIA sales plan, 85% of the sale price ($1,275,000) would be taxed at 20% capital gains rate, while the remaining 15% ($225,000) would be taxed at 40% personal income tax rate. Running this math would net you after-tax take-home proceeds of $1,155,000 (($1,500,000 X 85% X 80%) + ($1,500,000 X 15% X 60%)).

This is a difference of $255,000, for the exact same practice, under the exact same valuation multiple! Now consider that under the RIA model, the valuation by itself would probably be higher. Add in the tax treatment, and the overall variance between the two only increases further.

And this is for a practice of $1mm in T12. Larger practices drive the variance even further apart between the two potential exit strategy scenarios.

Takeaway: Run the above math on your current sized practice (which, mind you, doesn't even factor in any additional growth you might achieve before now and your eventual exit timeline) and determine how much more you could potentially take home "after tax" with a sale under the RIA model, vs a captive employee model.

11. An Upfront Transition Check Is Not As Lucrative As You Think

Each year many advisors depart from large traditional brokerage firms, only to join other large traditional brokerage firms (and/or sometimes independent contractor platforms). While there are various reasons advisors might make such a move, an underlying element often involved is the "upfront check" that often comes with it. Also known as a forgivable loan or note.

The merits of making such a firm-to-firm move are not the intent of this segment of the paper. Instead, it is worth considering the true financial impact of receiving an "upfront check".

Consider the often-cited "marshmallow" example of a child offered two choices:

1. Receive three marshmallows today, right at this very moment.

2. Receive one marshmallow a week for each of the next five weeks.

The point is simply to drive home that an upfront check is not a windfall for the recipient. Often, it is simply the equivalent of taking a meaningful haircut on your future earnings for the ability to receive some of those funds today.

Option 1 provides instant gratification, and most children would like receiving three marshmallows they could eat right now.

Option 2, though provides a better longer-term result for the child if they have the patience and wherewithal to wait for the aggregate rewards.

This is essentially what is occurring if/when you receive an upfront check. Such cash is not magically created out of thin air by the firm giving it out. Instead, the firm is essentially advancing you part of your future earnings you could otherwise generate/receive over time (such as with your own RIA). And for this luxury, they give you a discounted amount. Case in point, only 3 marshmallows today for the child not patient enough to wait for all 5.

The intent with this is not to imply advisors taking such checks compare to children. The point is simply to drive home that an upfront check is not a windfall for the recipient. Often, it is simply the equivalent of taking a meaningful haircut on your future earnings for the ability to receive some of those funds today. (And to be certain, the haircut is generally meaningfully more than a discounted net present value type calculation.)

Further, it is possible to effectively create your own "upfront check" within the RIA model anyway. If you were intent on needing/wanting some sort of front-end liquidity, there is a way to essentially create your own synthetic upfront check. All while still benefiting from the advantages of the RIA model.

Once fully versed on the economics of receiving an upfront check from a traditional firm, and how it impacts their long-term aggregate earning potential, many advisors opt-out of going down such a path.

Upon understanding the math of upfront checks, they often realize they are meaningfully better off not receiving one.

As it is challenging to explain the math behind this solely in written form, please refer to video #32 on the following page of the TRANSITION TO RIA website for a full explanation of how it works and how you, too, can create an upfront check for yourself if so desired:

www.TransitionToRIA.com/videos

Takeaway: Before assuming that receiving an upfront check would provide for the most advantageous economic outcome, make sure to calculate the aggregate math over the life of the arrangement to ensure you are comparing options accurately.

Now do something about it

You have worked hard to become a successful financial advisor by helping your clients achieve their maximum potential. Have you stopped to reflect on if you are maximizing your own potential as well?

For all the sacrifices, both professionally and personally, you have had to make to achieve the success you have, you deserve to fully benefit from the rewards your hard work has earned you. Depending on your current affiliation circumstances, you are potentially falling well short of the economic upside your experience has positioned yourself for, and which many of your peers have already taken steps to benefit from themselves.

I hope this whitepaper provides a useful starting point as you explore how the advantages of the RIA model can be of benefit to you.

TRANSITION TO RIA

TRANSITION TO RIA empowers financial advisors by providing them with the knowledge necessary to fully understand how the RIA model works, how it would look for their own unique circumstances, and how to make a transition to it.

Similar to the role you play with your clients helping them to navigate the countless products, services, and solutions available with managing their financial lives, I help advisors navigate the numerous options and decisions that go into transitioning to the RIA model.

Why And How To Go RIA?

Should you start your own RIA? Should you utilize the services of a middle office provider? Should you join an already established RIA? How do these options work, how do they compare, and what are the steps involved in them?

What Are The Vendors Involved?

No matter what model you decide on, there are a number of vendors that you'll need to be aware of and familiar with. Custodians, technology providers, compliance consultants just to name a few.

Who Should You Contact?

I utilize my deep industry contact list to provide you with introductions to the specific key person contacts for each of the vendors in the process. You will be confident you are connecting with the right people that can provide you the expertise you need.

FOR MORE INFORMATION

visit
www.TransitionToRIA.com

Bradford N. Wales
brad@TransitionToRIA.com
(727) 504-6627