FINANCIAL ADVISOR

What's New At The Custodian

By Eric Rasmussen

Custodians are continuing to offer new services for fee-only planners In their efforts to woo RIAs.

Freud never asked, "What does an RIA want?" But if he had, he might have found something like the financial planner's version of the Maslow's Hierarchy: not shelter, food and sleep, but simply the back-office comforts planners used to have when they were reps for a brokerage firm or worked in another large organization, before they hung out a shingle and went it alone.

According to people who serve them, these breakaway independents, for the price of their freedom, have found themselves drowning in paper.

"What we're hearing is that they are very good at raising money and managing money, but not nearly as well-versed in running a small business," says John Iachello, managing director at Pershing Advisor Solutions LLC. "So while they have been given a fairly wide range of products in the marketplace by custodians like ourselves, their first and foremost concern is running a more successful business. It's not terribly different than any other small business, like lawyers, doctors or accountants."

With this challenge in front of them (and competitors trying to woo advisors away, sometimes literally out from under their noses), broker-dealers and custodians have been called upon to constantly step up with new fee-based offerings targeting breakaway RIAs—services such as beefed up technology, more bulk trading, trust services and outsourced portfolio management, as well as practice management help.

Keith Newcomb, a financial planner with Full Life Financial LLC in Nashville, Tenn., dropped his broker-dealer affiliation last year, which freed him to seek new vendors. Though the process of finding new partners may not have been as exciting as the reality show elimiDATE, Newcomb says he did see a lot of interesting suitors pitching innovative services. Among them were Foliofn, which attracted him for its innovative and cheap trading platform that tried to match bid and ask prices, and Fiserv Investment Support Services, which did omnibus level trades for ETFs. "A big deal," he says. Eventually, though, he went with TD Ameritrade because "they blew the doors off on service," and gave him the one stop he needed for most of his services.

Expanding Platforms

This idea that advisors are not being allowed to spend enough time with their clients is a recurring theme that has brokers and custodians working to give RIAs more outsourcing options. TD Ameritrade acknowledged that issue when it announced in February that it was expanding its managed accounts platform in partnership with Capital Market Consultants LLC.

"They are going to help us in broadening that selection of investment management available to RIAs—those who want to either do their own investment management research and selection or those who want CMC to do that work for them, if they want to outsource it completely," says Brian Stimpfl, managing director of business solutions.

One piece of the puzzle will be a new unified managed accounts offering that will roll out from TD Ameritrade some time in 2007. These types of accounts, which primarily have been the domain of the broker-dealers, have been a big noise recently, since they can wrap together a bouquet of multiple products—individual securities, mutual funds separately managed accounts, ETFs, multiple-style portfolios and alternatives—all within one account, without multiple brokerage fees.

"UMAs are just starting to gain attention," says Stimpfl. "In the traditional world, if you had three separately managed accounts, that would mean three brokerage accounts. If you wanted a mutual fund, that would be another brokerage account. If you wanted an ETF, that would be a fifth. The UMA would combine it into one, and then you would have an overlay manager that would sit on all the brokerage in that account and allow you to just manage those investments in a tax-optimized way."

Pershing and Schwab Institutional are working on UMAs as well. Meanwhile, Pershing has developed a wrap-fee retirement product with a third-party asset management provider to address some of the thorny issues facing retirees, namely, a longer retirement where their nest egg has got to last longer. It's an account with multiple "sleeves," divided between cash-bearing vehicles, blue-chip stocks and smaller-cap stocks that have a longer time horizon, says Iachello.

These are all managed in one brokerage account with a third-party provider that buys three different models from three different managers, and this third party can monitor the account to make sure there is no overlap. Pershing has created the technology that allows them to do it all within one single account with a single performance report and a single package. The firm is testing other similar products with other providers.

"We don't look at it as an annuity per se," Iachello says. "It's the type of solution that has to be developed in our industry for all the baby boomer retirement groups. It will not be feasible, in my opinion, for advisors to separately manage each small relationship that will be coming their way."

Broker-dealer Commonwealth Financial Network has also expanded its fee-based platform with two new initiatives. One is its PPS Retirement Solutions retirement plan, which allows RIAs on its platform to offer 401(k) plans to corporate clients with full transparency and disclosure. Managing principal Wayne Bloom says the new product was not meant as a response to changes in last year's Pension Protection Act of 2006, though the timing was perfect with the new law.

"What the PPA is all about is that they do not want variable compensation at the point of sale," Bloom says. "Typically, reps in this segment of the marketplace earn 12b-1 or finder's fees. Depending on what a traditional no-load company, say a Vanguard, will pay them versus a traditional 'A' share, the company's compensation will be different. Now we've removed that so that the advisor gets a flat fee based on the assets in the plan. There is no variable compensation based on the assets selected."

The firm has also come out with a new turnkey mutual fund and exchange-traded wrap program called PPS Select, which offers 15 different sets of portfolios as part of the firm's partnership with research and consulting firm Ibbotson Associates.

Trusts Become Trendy

In the meantime, execs at Schwab Institutional have been looking more closely at trust products, which it sees as a big area of growth as advisors deal with more wealth-transfer issues amid mass Baby Boomer retirement. "At Schwab Institutional, when we look at the assets that our advisors have with us, 40% of the non-retirement assets are held in trusts," says Cathy Clauson, vice president of product development. "As we go out and talk to advisors, that number gets greater for the percentage of assets under management."

And as that happens, she says, advisors will have a great opportunity to clinch (or lose) those assets, depending on whether they have relationships with the successor trustees and the beneficiaries. Evolving trust laws have begun to liberate these assets from their past stranglehold by banks. Until fairly recently, most of the money was held in such a way that trusts holding the money also did the management, and advisors often got cut out—often at a time, Clauson says, when the trustee has died and the family needs the advisor the most.

Schwab has taken a couple of steps in this area, she says. The firm is building a corporate trustee offer in which the advisor can name Schwab as a successor trustee, and that allows the firm to manage the trust. Schwab has also partnered with Innovest Systems LLC, a technology developer whose trust accounting software will be integrated into Schwab Institutional's custody and trading platform so that advisors can provide trust accounting. The new system is in a pilot program now.

"Traditionally you'd separate the principal of the investment and income and you'll pay the income beneficiary," she says. "However they want that paid out, we'll be able to do that now, where before we had that [software] we couldn't. Broker systems in general haven't been able to do that. Banks were the ones that were set up to do that. So this weds the full functionality of the broker-dealer system with the full functionality of the trust accounting system."

The trust strategy differs from Schwab's arrangement when it owned U.S. Trust, Clauson says. Because the previous offering required custody at U.S. Trust, she says it was less efficient for advisors and limited the number of investment products. The new approach allows the advisors to keep custody at Schwab Institutional and avail themselves of the firm's mutual funds and managed accounts platform.

Outsource A-Go-Go

Pershing has been focusing a great deal of its energy on practice management issues as it aggressively pursues RIAs. In conjunction with a study the firm commissioned with Moss Adams LLP on buying and selling firms (called Real Deals: Definitive Information on Mergers and Acquisitions for Advisors), Pershing has begun a series of workshops around the country for small groups of 15 to 20 advisors to bring the lessons from the study down to a personal level, says Iachello. Pershing has also released a report focusing on hiring and retaining the best staff (called A View From the Top: Best Practices in Leveraging Human Capital).

“Another thing we keep hearing from RIAs is that they are frequently at risk of loss of control if they lose senior operational people,” Iachello says. “The advisor is not frequently in a geographic region that has a lot of knowledge of the brokerage industry, so it’s hard for them to reach out and get new staff that is trained.”

Raymond James has also focused on succession planning, says Mike Di Girolamo, managing director of the Investment Advisors Division. The firm formed a practice management and succession planning department and will roll it out this year. The new department will help advisors value their practices, and help buyers and sellers find each other. The firm will offer financing for advisors who buy other firms and bring the assets into the Raymond James platform. In addition, Raymond James has been integrating new kinds of software into its platform, having paired up with Microsoft to integrate its customer relationship management software—Microsoft Dynamics CRM—after last year adding the CheckFree APL institutional portfolio management system into its platform and routing portfolios there from its in-house system. “We’ve made a concerted effort in the last two years to really integrate the various modules right into our platform,” says Di Girolamo.

A recurring theme in practice management is that advisors want more time to spend with their clients, and that’s the overarching theme motivating many of these big initiatives. Outsourcing is the buzzword at TD Ameritrade, says Stimpfl, and the firm is sending out consultants to help tie together all of the firm’s business development programs, including the new managed accounts platform. TD Ameritrade is also trying to step up its technology initiatives, and in 2006 it bought iRebal, Gobind Daryanani’s popular rebalancing software, which it will continue to sell separately but also integrate into its platform.

“You could really outsource everything,” Stimpfl says. “You’ve got to have processes and procedures with your vendors, but you could do nothing but manage your client relationships in this day and age and outsource everything else in your business. I don’t think many advisors are doing this. Many don’t want to. But they could outsource any of those disciplines: trading, back office, portfolio management, investment management compliance. We’re helping them make those choices.”