The Purposeful Advisory Firm

Maximize your firm by design, not by default

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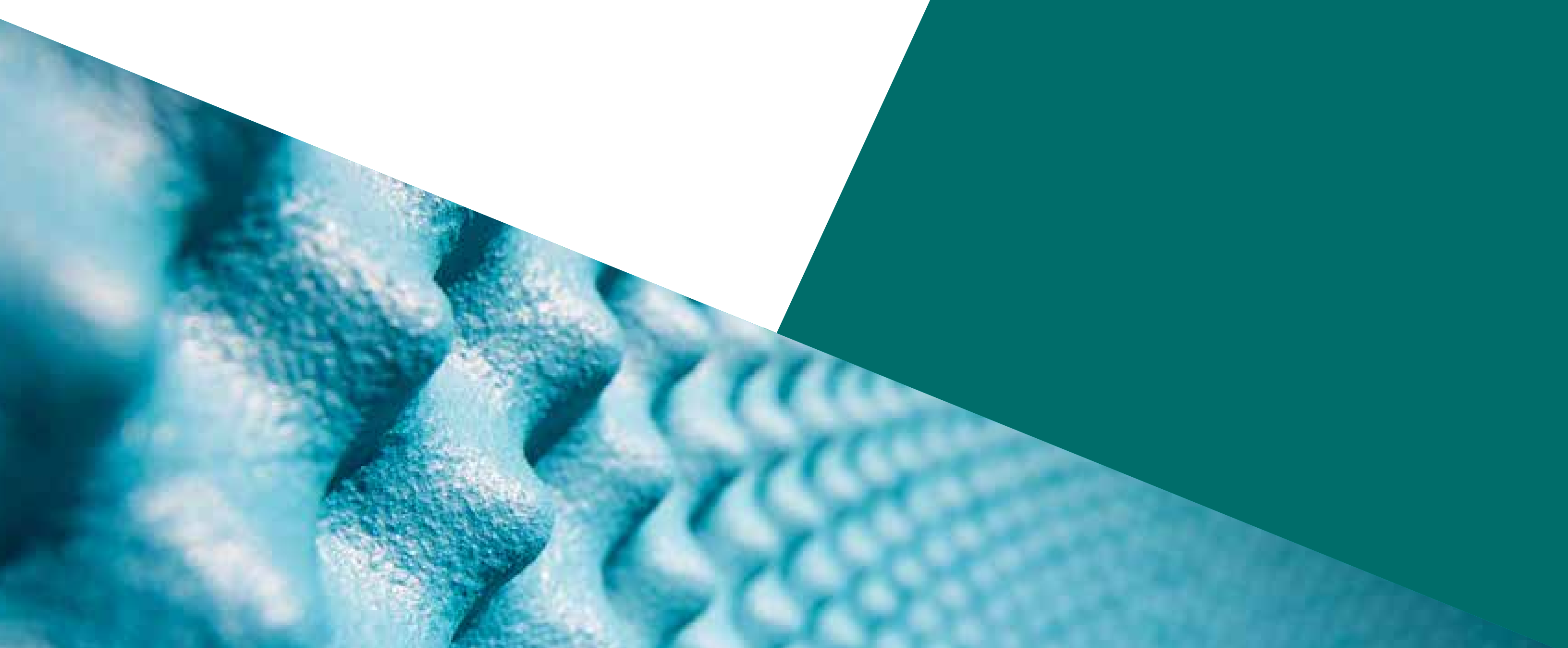


Introduction

It's 2:00 a.m. You're wide awake.

Every firm struggles with its unique business challenges.

If you are focused on building enterprise value, you are focused on building your firm. Maybe you worry about retaining your best clients and finding more just like them. You might look at your designated successors and wonder if they'll succeed. You may also agonize over the pace of technological innovation and how to keep up with complex markets and regulatory changes that seem to consume more of your time than ever before.

Or maybe you own a thriving firm that still affords you an ideal work/life balance, but you worry that the income stream you've built may not be sustainable in the future. Outside pressures, like regulations, competitors and compression, seem to be working against you. What happens when you decide to call it a day (either intentionally or not)?

Your firm's next phase: Trade-offs and opportunities

The advisory business landscape supports many different business models. So why is the industry forcing the enterprise model as the 'correct' approach? **Defined, an "enterprise firm" will live beyond the original owners, and has professional management and processes**.

Our research reveals that no single model is better or worse than another; as long as your model serves your goals and your clients' needs, there is no right or wrong choice. Eventually though, you must decide to either maintain the status quo or lead your business to the next level—a classic dilemma fraught with trade-offs and opportunity costs. If you're not interested in scaling your business or increasing your valuation, investing may not be necessary. **This would mean you might be more interested in creating a "lifestyle firm."** But if you're looking to expand or optimize your firm's future value, reinvestment is essential. The choice is up to you.

Time to make a decision

Many advisors habitually focus on the urgent rather than the important. Or they engage in tasks that come easily at the expense of longer-term strategic decision-making. **Default occurs when you don't decide**—either because the decision is too difficult so you deliberate until time runs out, or because you simply decide not to decide. You've thought about hiring more people, investing in better technology, or even merging with another firm. But you might be thinking, "Why fix something that isn't broken?" Or when you look at the costs you wonder, "Why would I make those changes now?" There is no right or wrong path, but not choosing has consequences, too. The risk is that many key business decisions are neither acknowledged nor evaluated with full intention and awareness of those consequences.

You decide. Do you want to build an enterprise or a preserve a lifestyle business? You're in the driver's seat to run your business—by design or default.

Economics teaches us about making choices about the best possible use of scarce resources. When you choose among various alternatives, you have to forgo other options. We wanted to understand how the trade-offs—what you give up to get what you want—compare to the opportunity costs for evolving advisory businesses. If you want your firm to keep growing, what choices should you make today to build a sustainable enterprise? Conversely, if you're satisfied with what you have, what choices can you make to optimize your firm's future value? Our goal for this paper is to help ensure that you make an intentional decision about the path you choose.

A GUIDE TO THIS PAPER

In this paper, we consider the evolution of an advisory business—from Startup to Mature—and examine some of the trade-offs you should evaluate as you decide what kind of firm you are now, and what sort of firm you want to be.

What do other financial advisors say?

Results from our March 2017 online survey offer a timely snapshot of the broad universe of advisor businesses, including fee-only and dually registered RIAs and broker-dealer affiliated advisors. Survey participants fell neatly into three basic categories: Startup, Emerging and Mature, with substantial differences in structure, size and profitability. Size of firm—as measured by employees, assets and number of clients—also proved to be a driving factor in the evolutionary process.

Insights from the 400 respondents who identified themselves as owners/managing partners shed light on the state of the industry and distinct business models to help them better understand and assess their own agenda.

Key finding: Advisors vs. business owners

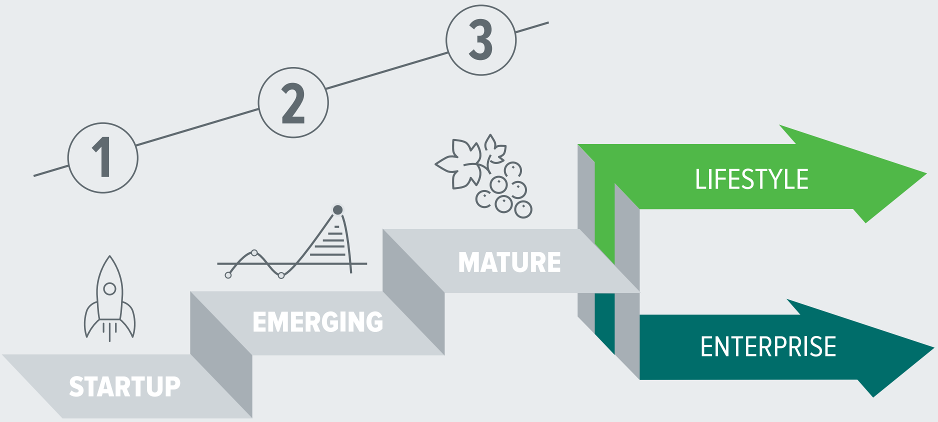
Our research revealed a striking insight: **Most respondents (64%) view themselves as advisors who also happen to be business owners—not business owners who are advisors**. While it may seem nuanced, the advisor-first view manifests itself in ways that may limit future opportunity. More than a quarter of these advisors (26%) report they have no intention of building the next generation. Many may be unrealistic about translating their firm's hypothetical value into a retirement plan or a legacy for their heirs. Absent a plan, many of these firms will perish with their owners.

- Fielded through SEI email and in conjunction with Bob Veres and his advisor community
- Questions focused on:
  - How advisor firms run their business
  - Maturity stages of an advisor firm
  - Firm demographics

?

What is a purposeful advisory firm?

We define a purposeful advisory firm as one that is led and guided by an owner who intentionally develops and executes a strategic plan—either to **build an enterprise** focused on maximizing the firm's value, or to **remain the single owner** through retirement with no intention of transforming the firm's ownership structure.



The business phases shown on the following page offer realistic representations of today's firms at each stage of their evolution, based on our survey. The results reflect only those responses from owners/managing partners and can be used as a reference to situate where on the spectrum your firm sits today.

DEFINITION OF TERMS

PHASE 1 Startup
Startup firms tend to be younger (42% of firms are under five years old) and so are their owners, with most aged 30 to 60. They have the smallest number of employees (74% have one or two total firm employees), and total assets under management are more likely to be less than $25 million.

PHASE 2 Emerging
While still relatively small, Emerging firms are well established (most have been in business between six and 20 years) and manage $25 to $75 million in assets. They occupy a sweet spot in the sense that many future options may be available; 40% are under age 50. Intentional decision-making at this stage in their evolution could prove highly rewarding. Firms at this stage often partner with others to share resources and expenses, but still run separate practices. Most are in a growth mode, adding clients, technology and even new advisors to lower expenses and reduce overhead, but on average have five or fewer employees.

PHASE 3 Mature
Mature firms have more assets under management, and most have been in business longer than 20 years (58%). They are further characterized as what we call "Mature Lifestyle" or "Mature Enterprise" firms.

While the term "lifestyle advisor" historically has had negative undertones, we have come to appreciate the model that has evolved intentionally and is associated with strong cash flows, high quality standards and loyal clients.

We use the term **"Lifestyle"** to describe firms that are typically owned and managed by the founder and often bear that individual's name. Lifestyle firm owners tend to enjoy the sales and client relationship aspect of the business and are less interested in managing teams and/or unwilling to hire a full-time COO. On average, they employ fewer than 10 individuals with 57% operating for more than 20 years. Fifty-five percent of assets under management range between $150 million to $500 million, with 8% exceeding $500 million.

"Enterprise" firms are slightly larger; one-fifth of these firms have more than $500 million in assets under management and 28% have more than 11 employees. About half serve 250 to 500 clients, but 30% have greater than 500 clients. Most (59%) have been operating for more than 20 years.

How can you firm up your firm?

In this section of the paper, we pose key questions to help you determine what phase your business is in and what model suits you best.

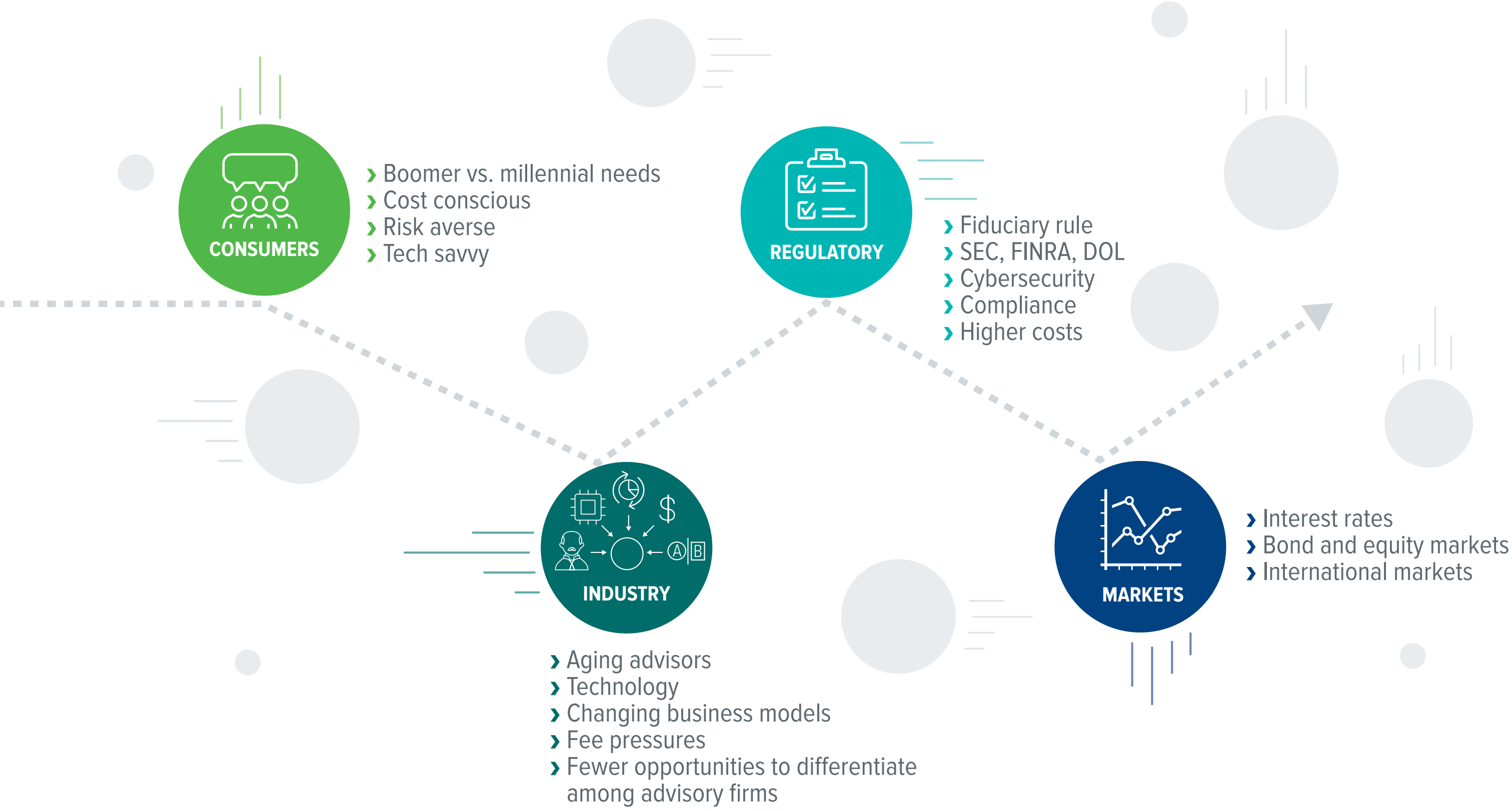
Firming up your mature firm
We're convinced—and our research confirms—that owners have to choose a path or their firms will become lifestyle defaults. This represents the worst of both worlds: they won't have much to sell, and the owners won't make as much money as they hope.

Too many firms are neither having the conversation nor making a conscious decision about their path forward. In this final section, we summarize the kinds of decisions you might face in your firm's evolution, and we highlight the opportunity costs of default or of becoming a purposeful advisory firm. Regardless of where your firm sits today, these best practices will help you strengthen your organization and optimize the value of your firm.

CHANGE IS EVERYWHERE

The forces of change—consumer, industry, regulatory and the markets—are everywhere. Their impact on the advisory profession is staggering and the pace of change is unlikely to abate. With this added pressure, some advisors are leaving the profession which is contributing to an increasing number of transactions. You can neither ignore these factors of change nor use them as an excuse to avoid critical decision-making.

We observe that the most successful advisors are investing conscientiously to varying degrees in their talent, technology and value proposition to drive growth, sustainability and the potential to sell. For your business to thrive in the future, you'll want to establish a serious and deliberate vision of the kind of firm you are and want to be.



Priority highlights: 2017 Wealth Management Outlook[1]

Focus on improving profitability

- Over two-thirds of executives indicate that client profitability will be even more of a concern for their company over the next 12-18 months.
- Nearly half of wealth management firms' most significant area of focus is client strategy and engagement, followed by sales and advisory strategy.
- Increasing advisor capacity for sales, planning, and advice is the most important priority for executives in 2017.

Firms concerned about next gen clients, data and digitization

- Less than half of executives express confidence in their ability to engage younger clients.
- Data and the digital experience present the biggest challenges for executives in 2017; the largest gaps between importance and confidence arise in applying data for actionable business analytics and enhancing digital channels to complement the advisor.

Emphasis on efficiency in technology/new regulation

- Technology initiatives that contribute to advisor efficiency represent the most important IT issues in 2017.
- IT executives anticipate new regulations and increased cost pressures having a significant impact on their technology strategies.
- Respondents identify CRM technology as their firms' most critical employee adoption priority.

An industry in flux

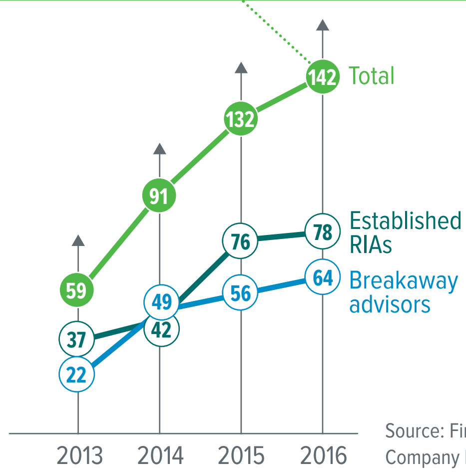
The vast majority of SEC-registered RIAs are small businesses. Small businesses are the core of the investment adviser industry. In 2016, 56.8% (6,725) of advisory firms reported that they employ 10 or fewer non-clerical employees, and 87.8% (10,404) reported employing 50 or fewer individuals. Industry-wide, the median number of employees is nine.[2]

Consolidation continues

One cannot ignore the growing and aging elephant in the room: The demographics of owners. The continued procrastination of the RIA community to execute succession planning will likely force a surge of unanticipated sales in the future. More and more owners will eventually find that the growth of their company has conspired against them: When they finally seek to put their successors in place, they will often realize that their companies are now too expensive for their next generation to afford.[3]

However, there is a rule of thumb. According to FP Transitions® 2017 data, an advisor can sell their firm for roughly 1 x its commission-based annual revenue plus 2.4 x its fee-based annual revenue.

Merger and acquisition activity hit an all-time high of **142 transactions in 2016**. The fourth quarter was the ninth successive quarter of 30 or more transactions, demonstrating a sustained and robust M&A market.



Source: First Quarter 2016 | DeVoe & Company RIA Deal Book

BOB VERES
weighs in

The biggest challenge that founding advisors are facing is their own inertia. The dynamic baby boom generation that created the financial planning profession out of nothing more than an idea has become the obstacle to change in this mature phase of careers. How can you create a new vision for the company when you're perhaps a bit too comfortable with the status quo?

Of course, the status quo is a dangerous fiction. The profession is going to have to adapt its value proposition and revenue model to a new generation of clients, who have very different needs and preferences. At the same time, a rapidly growing outsource ecosystem and what I call "smart software" (think robos) are creating enormous new opportunities for business leverage.

My proposed solution? Identify two younger advisors in your firm who would like to be majority owners 5 or 10 years down the road, and give them a project: reinvent this firm into the type of firm you would want to own, first on paper, and then through a series of business decisions on service models, marketing and outreach, technology, etc. (This white paper could serve as a guide to that process.)

VALUE ENGINEERING FOR TODAY'S ADVISORY FIRMS

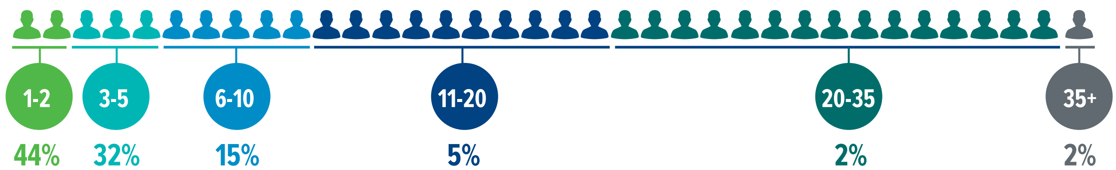
Popular in the manufacturing industry, value engineering determines what changes in design or process can be made to reduce costs without reducing utility. It's more complicated for service businesses; not only do many factors influence the customer's purchase decision, but the motivation of the business owner factors more meaningfully into the equation.

Every advisory firm consists of four essential components—**people, value proposition/brand, investment philosophy** and **technology**. These are the levers you control and about which decisions are made. Analyzing these component parts helps advisors assess what's essential, what can be eliminated and what changes could be made to greatly enhance the overall service. **Purposeful planning and decision-making depend largely on the owner's goal to either maximize cash flow or enhance the value of the firm**.

The value of people

As a professional service business based on relationships, your staff—administrative and professional—is your firm's most valuable asset. Three-fourths (76%) of our survey participants employ five or fewer individuals, including the owner.

How many employees, including you, work for the firm?



- Client service (74%), administration (63%), investments (43%) and compliance (48%) rank among the top roles for which advisors have dedicated employees.
- Many advisors delegate non-critical roles—such as bookkeeping, marketing communications and investment research—to third parties while focusing on core competencies in-house.
- Regardless of your size or shape, intentional decisions about what you do in-house and what you delegate to a third party will dictate what services you offer, whom you hire, and how you develop staff to contribute to the firm's overall success.
- An overwhelming majority of wealth managers surveyed by Cerulli agree that developing the next generation of talent is very important. Discussion also focuses on the millennial workforce, of which the youngest are just graduating college and the oldest are in their prime working years.[4]

A B

Purposeful decision-making prompts

Ask yourself these questions to help drive your people process.

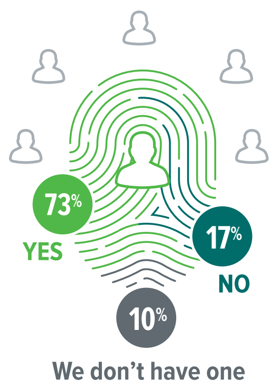
1. Do you have the right staff in the right jobs to maintain your current business?
2. What aspirations do you have for taking your firm to the next level?
3. Do you have the appetite for adding (and managing) more employees?
   a. What roles will they play?
   b. What training and development resources are you committed to providing?
4. Do you have the right processes in place to keep your staff's morale high?
5. What strategies do you have in place to develop next-generation talent and acquire next-generation clients?
6. Can you define your firm's culture, and does everyone fit well within that culture?
7. Do you have a compensation model in place to keep the people you want to keep?
8. Does your staff have the right process and workflows in place for your lifestyle or enterprise model?

Your value proposition/brand

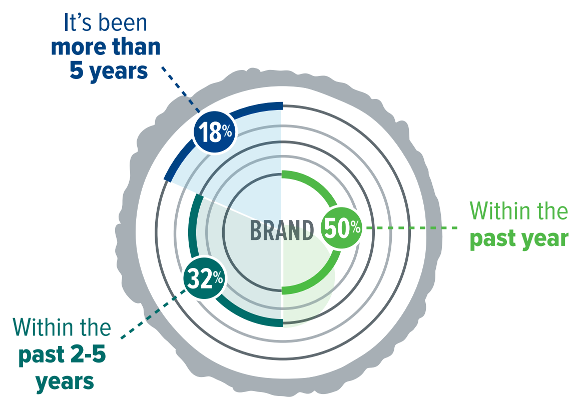
Your value proposition answers the question “What do I offer to whom, and why?” Intentionally framing the unique attributes of your business—the *who* (the type of client you serve), the *what* (the solutions you offer), and the *why* (the obstacles your clients face)—helps articulate what your firm stands for.

- Nearly three-quarters of our survey participants (73%) believe their brand differentiates their firm from others—yet only half (50%) have revisited their brand within the past year. Nearly one in five firms (18%) haven’t done so in more than five years.

Q Do you feel your brand differentiates you from other advisors?



Q When was the last time you revisited your brand?



- Business owners can choose to deliberately define their value proposition or let it evolve organically. Realize that if you choose the latter, your brand will occupy a market position—it just may not be the one you intended. It’s a serious mistake not to take control and manage it.

Purposeful decision-making prompts

Ask yourself these questions to help drive your value proposition/brand.

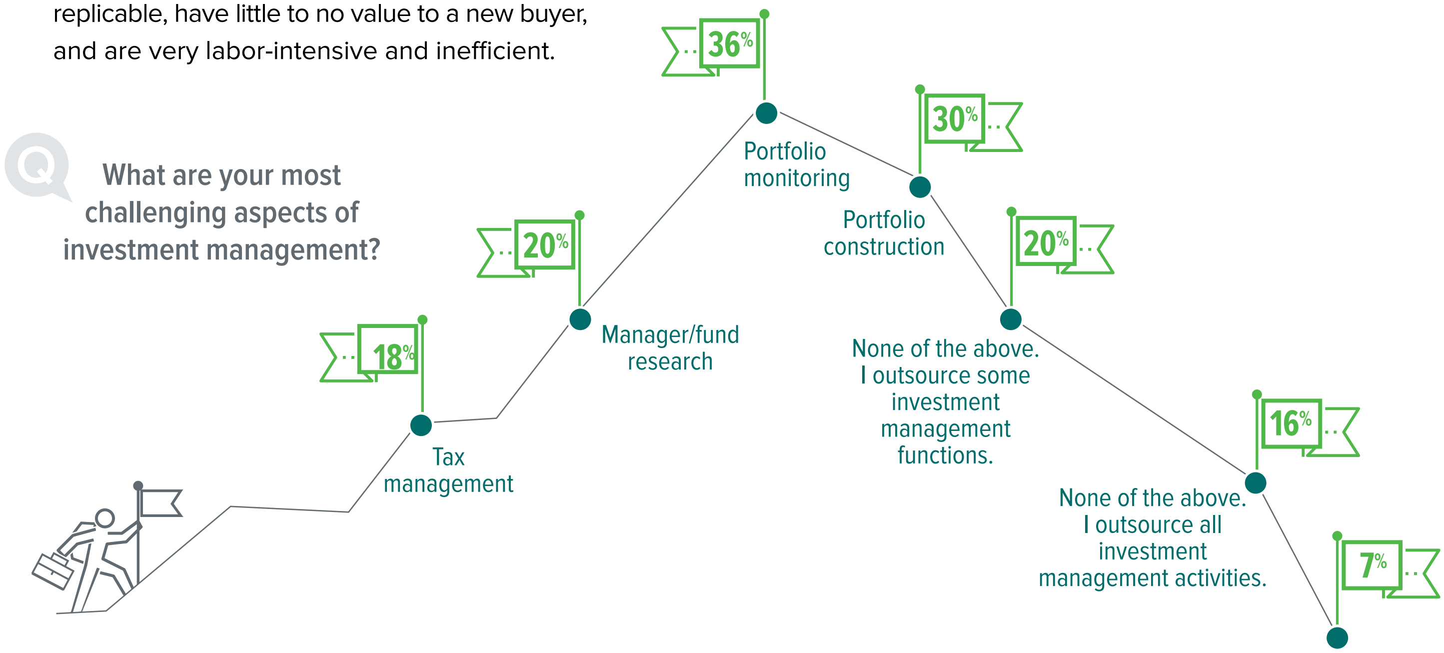
1. Does your value proposition truly differentiate your business from your competitors? How?
2. If you decide to expand your reach, how will your value proposition change?
3. What new services are you considering adding to retain existing clients and attract new ones?
4. Have you ever asked your existing clients how your value proposition matches up with their view of your firm?
5. Many owners choose simply to brand their personal identity; that decision could dramatically restrict their ability to sustain a valuable enterprise in the future. If you are the brand, how will your firm endure without you?
6. Is your brand clear? Does it match your value proposition? Are your current clients’ needs and characteristics consistent with the who, what and why stated in your value proposition?
7. Have you segmented your clients by what is important to them—and not you? Do you offer different services to the different segments?

The value of your investment philosophy

Articulating your wealth management approach—including the types of services you offer—as well as describing your investment methods and philosophy will not only benefit your current clients, it will help you attract new ones and hire like-minded professionals in the future. The value hub of most wealth management firms is advice—an extension of the wealth management value proposition referenced above. How that advice is rendered and valued by clients is an essential ingredient for long-term success.

Thirty-six percent of our survey respondents delegate some or all investment-related activities to a third party, while the vast majority (64%) have built, we believe, commoditized businesses that are key-person dependent, performance-dependent and/or market and economy dependent.

If your firm is performing all investment-related tasks internally, we believe you may be severely limiting your firm's future value as your models may not be replicable, have little to no value to a new buyer, and are very labor-intensive and inefficient.



Percentages may not equal 100.

Nearly half (46%) of "mature" advisory firms have a dedicated employee who oversees the investment role. Unless your CIO or investment team has created a process that is truly differentiated and demonstrable, the ability to deliver broad investment expertise may be challenged in the future by price compression, automation, lower expected returns and client demands. Given the intensifying complexity of capital markets and the regulatory climate, demonstrating value will be increasingly more difficult to achieve in the future.

Respondents indicate that portfolio monitoring (37%), portfolio construction (30%) and manager/fund research (20%) are the most challenging aspects of investment management.

Purposeful decision-making prompts

Ask yourself these questions to help drive your investment philosophy.

1. What investment-related tasks do you do well and enjoy most? Conversely, what do you least enjoy and do poorly?
2. Is your firm differentiated by factors outside of your control, e.g., the markets and the economy?
3. Can you fire yourself?
4. What investment services do your clients value? How do you know?
5. If you are an enterprise firm and bring in a CIO, are you changing your focus from wealth management to investment management, and at what cost?
6. Are you being compensated for your advice—are you charging enough for your investment-related services to cover your costs? How do you know?
7. How do you want your clients to see you—as a money manager or a provider of advice?
8. What is the risk of diminishing your value to clients when delegating certain investment management tasks? How do you know?
9. Are there ways to streamline your process?
10. What do your clients value most from your wealth management services? How do you know?
11. At what AUM level is your firm capacity constrained?

BOB VERES
weighs in

Regardless of whether you intend to create a sustainable firm or a lifestyle practice that lives through the next and future generations, your goal is to get rid of the tasks on your desk (and the desks of your staff members) that are non-critical to your core service model to clients. The fastest way to achieve this is to delegate those activities to a third party. Doing so shifts the burden of training, staff management and quality control from your desk to somebody else's—and typically you have an expert handling tasks that were being done part-time by people you (poorly) trained yourself.

But, many advisors resist delegating or outsourcing tasks to a third party because they feel that it's somehow akin to "cheating." If somebody else does the work, how can you take credit for it?

Here's the key insight that some of the most successful advisors have learned over time: Clients really don't care who does the work. They only care that you're ensuring the work is done to a high level.

The value of technology

Technology has enabled smaller, independent RIAs to compete head-on with the largest wirehouses. Though historically relegated to the realm of operations, innovation and processing power have dramatically elevated its importance for all advisory firms. Technology solutions are as important to business development and client retention today as they are to the administration and account management process. The arduous task of gathering current values for multiple types of assets and accounts (a responsibility that historically has fallen mostly to clients), for example, has improved dramatically thanks to automation and account aggregation.

- Your firm's technology platform has a significant impact on the kind of firm you have today and expect to grow into tomorrow.
- Technology has grown so fast, advisors haven't maximized what they currently have. From financial planning software to automated workflow processing, new innovations can save you time, money and grief. But all your firm's technology decisions require an intentional weighting of short-term cost vs. long-term benefits. That's not easy in today's climate, where Moore's rule (the golden rule that states that computing dramatically increases in power, and decreases in relative cost, at an exponential pace) is driving innovation faster than advisors can adapt.
- Our survey participants rank "Using and integrating the right technology" among the top five most important success factors for their business.
- Technology outsourcing is an increasingly popular choice for advisory firms. Research finds that the top motivations to outsource today, compared to five years ago, include: improving efficiency; adapting to fast changing technology without spending on dedicated IT teams; enriching the customer experience; and regulatory compliance and transparency.[5]
- About 20% of our survey respondents handle this in-house, while a slightly larger percentage (22%) delegate the majority of the function to a third party.
- Cost/benefit analysis and system integration remain the most challenging aspects of advisors' technology decisions.
- In today's environment, it makes no sense for firms to build or buy every new technology that comes along. Working with an outsourcing, consulting, or technology vendor can allow wealth managers to experiment with new technology before committing to creating their own solution.[6]

Purposeful decision-making prompts

Ask yourself these questions to help drive your technology strategy.

1. Is your firm getting the most utility from your current technology platform?
2. Have you assessed your firm's technology needs within the past 12 months?
3. What are you biggest obstacles with your current technology platform?
4. Are your systems integrated? Do you use workflows?
5. How will new technology purchases/outsourcing improve your client experience?
6. How will new technology purchases/outsourcing improve your firm's overall efficiency?
7. Will the new technology solutions you're considering disrupt your business? How?

FIRM CHARACTERISTICS: A closer look at the phases of evolution

The following personas offer a realistic picture of today's firms at each stage of their evolution, based on our survey results. The results reflect only those responses from owners/managing partners.

Which persona most closely matches your firm?

MEET
JAKE

PHASE 1 – STARTUP
Business profile: The struggle

- Sales, sales, sales
- Only 18% have AUM-only income
- Adaptable to any sales opportunity

Clients	Fee Structure	AUM	Net Profit	Age	Years in the Business	Firm Employees
51-250	AUM + COMMISSION	< $25M	< 30%	30s-60s	< 10	2

People	Value proposition/brand	Investment philosophy	Technology
› One advisor	› Historically broad › Overstated › Fine-tuning required	› Putting together custom solutions for every client	› High initial expense—spending ranges between 5% and 10% of revenue
› Reactive hiring › Staff added gradually to support founder	› Paperwork and redundant tasks	› Leveraging wholesaler support	› Affordable and easy to use › Not well-integrated
› Long hours, doing everything themselves	› Brand is nonexistent	› Lure of commissions	› Broker-dealer clearing through institutional custodian
› Growth constrained by individual limitations	› Exploring client niches	› Lack of clarity around investment process	› Website is an online brochure

Source: SEI Advisor Survey – Business Models, n=400 Managing Partners/Owners, March 2017

MEET SARAH

PHASE 2 – EMERGING

Business profile: Breaking out

- View as advisor, not business owner
- Business growth happens quickly; multiple technologies; unclear roles of staff; no niche
- High level of profitability due to small staffs and investment variety
- 54% have fee structure combining commission + AUM/planning
- 57% believe fiduciary is important to clients
- 73% expect practice to survive their career

Clients	Fee Structure	AUM	Net Profit	Age	Years in the Business	Firm Employees
100-250	AUM + COMMISSION	$25M-$75M	30% to 50%	40s-60s	6-20	1-5

People	Value proposition/brand	Investment philosophy	Technology
Founder leveraged with support staff and possibly junior advisor	A service model with many exceptions	No defined, repeatable investment process	Multiple technologies collected over time, not well-integrated
Staff is brought on as pain is felt	Personality-driven marketing	Most portfolios are custom, without the scale of models	Basic CRM tracks client data but not workflows
Advisor in a steady state of execution rather than a management role	Brand is not clear. The lead advisor is the brand	Many small accounts/clients who didn't grow. Some clients were sold investments and expect advice for life	Sending out performance statements rather than facilitating client access to account data via client portal
Need to solve continuity and succession issues		Evolving investment process leaves orphan accounts and old investments in client portfolios adding risk of oversight or monitoring	Half (50%) spend 6%-10% of revenue on technology

Source: SEI Advisor Survey – Business Models, n=400 Managing Partners/Owners, March 2017

MEET
MARK

PHASE 3 – MATURE: THE LIFESTYLE PRACTICE

Business profile: The personality

- Lead advisor is the image of the firm
- 57% are SEC/state-registered RIAs
- Lead advisor focuses on clients

Clients	Fee Structure	AUM	Net Profit	Age	Years in the Business	Firm Employees
100-150	AUM + COMMISSION	$75M-$500M	>30%	50s-70s	>20	Founder + 2-5

People	Value proposition/brand	Investment philosophy	Technology
Founding advisor with junior advisors who have defined client-facing responsibilities	Founder is the brand Reputation is well established in niche area. Sixty-nine percent believe being a fiduciary is important to clients	Evolution toward model portfolios for greater efficiency	Spend on average 6%-10% of revenue on technology Internal IT support—only 17% of advisors outsource the function
Back-office specialists comprised of legacy staff members who evolved into key roles	Haven't visited brand in 2 years or more Increasingly rely on fee revenue and de-emphasize commissions	Do we hire a CIO and a team of investment analysts or delegate to a third party?	CRM used to help founding advisor keep track of who's doing what
No clear successor, but hopes that one or more junior advisors will "step up" to the challenge	Personality based—junior advisors are trained in the founding advisor's client service methodology	Customized performance statements posted quarterly in client vaults	Website emphasizes client fears, planning process and credentials of the founder
Change is difficult; Less likely to adapt to new market challenges	Founding advisor works with the clients who pay the most Junior advisors work with less complicated legacy clients	Many "one-off" demands from larger investment-focused clients No defined investment process	Support staff manually re-enters data into a suite of legacy tools

Source: SEI Advisor Survey – Business Models, n=400 Managing Partners/Owners, March 2017

MEET THE
EXPONENTIAL FIRM

PHASE 3 - MATURE: THE ENTERPRISE BUSINESS

Business profile: Team

- Management team running the firm
- Transformation—takes a multi-year plan
- 86% confidence that firm will survive founders
- Focus on efficiency (expense cutting)
- Expansion by acquisition now an option (or to be acquired)

Clients	Fee Structure	AUM	Net Profit	Age	Years in the Business	Firm Employees
200-500+	AUM + PLANNING	$150M-$500M	>30%	40s-60s	>20	Up to 35 +

People	Value proposition/brand	Investment philosophy	Technology
› Multiple advisors with shared client responsibilities › Shared ownership or shared equity in the firm	› Clearly defined and repeatable service models › Brand is differentiated › Comprehensive wealth management › Used to determine pricing	› High cost structure to support investment-related services › Risk that planning-focused value prop may change to investment management	› Technology is customized/optimized for the firm › 28% outsource the technology function
› Lead advisor/founder moves into senior management role	› Client segmentation (both niche and small accounts)	› Monthly reviews of investment climate and individual investments	› CRM used to design workflows › Consistent operational processes
› Stakeholders help shape a shared vision › Collaboration and scale	› Clear branding has evolved around the firm's target market(s)	› Investment returns available after market close on client portals	› Software is tightly integrated through single sign-on
› COO function handled as a full-time position (or managing partner)	› Firm plays a role in the niche market, generating business through visibility	› More complex use of strategies for higher-net-worth clients	› Technology suite is evaluated against new opportunities
› Clear career path for advisors and teams	› Average age of clients stays constant as new, younger clients are onboarded		› Integration of systems is high priority

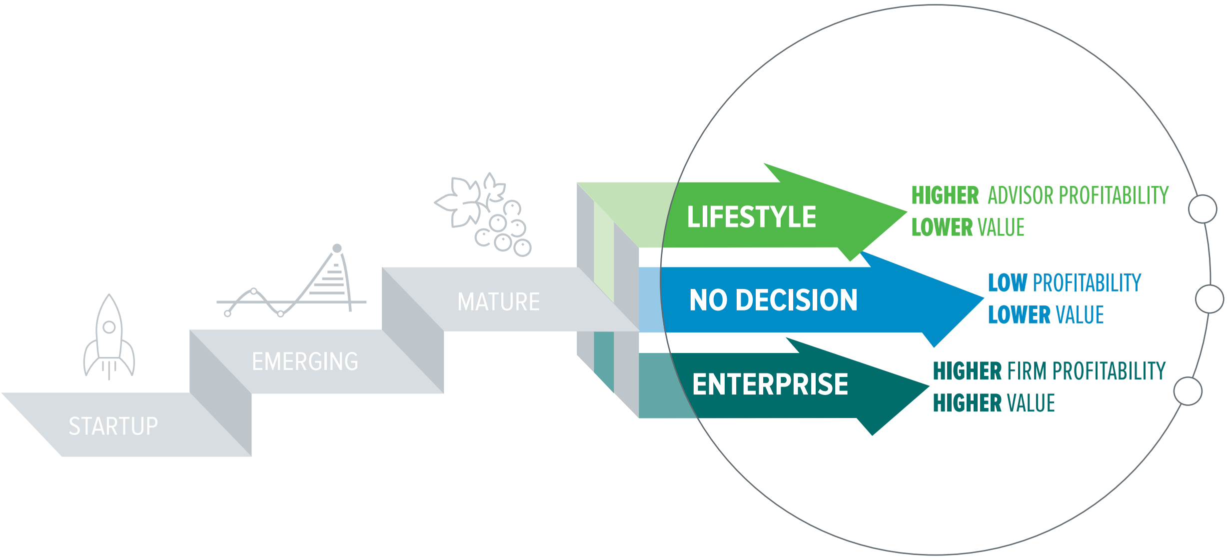
Source: SEI Advisor Survey – Business Models, n=400 Managing Partners/Owners, March 2017

Summary: Key research findings

- The most profitable firms are the emerging businesses, with an average of one to five employees; enterprise firms vary in their profitability—depending upon their infrastructure and costs.
- Most lifestyle practice owners think of themselves as advisors first, not business owners. These same respondents identified themselves as mature, lifestyle businesses with no intention of looking for the second generation of advisors.
- The lifestyle business goal is to maximize current cash flow—not future value or equity.
- We specifically asked advisors who had self-identified as lifestyle businesses whether they thought that their practice would live past them. 74% said yes. **Of special note:** in actual practice this may be very difficult.

Determine your firm's financial future

Remember, purposeful planning and decision-making depend largely on your goal to either maximize current cash flow or long-term value. When you make your decision, regardless of choosing the lifestyle or enterprise model, you should be able to direct your firm's financial future to match your goals and your clients' needs.



BOB VERES
weighs in

The survey noted that the smaller firms are the most profitable, but this might be misleading. The smaller firms will generate the highest cash flow for the owner, but that additional cash flow is probably exactly equal to profits that the less profitable firms are reinvesting back into their staff and operations. In other words, the money either goes into the pocket of the founder today, or builds the value of the business, which the founder can monetize in the future.

FIRMING UP YOUR FIRM

Decide what kind of firm you are.

Now that you've identified with one of the personas, you should focus on firming up your firm. Start by asking what kind of firm do you foresee in your future? Because personal goals typically drive business goals, you'll need to start with a clear vision of your future. If you haven't already, you may soon reach a crossroads and will need to decide whether to become a **lifestyle** or an **enterprise** business. While either path is acceptable, **you must decide**. As we've suggested throughout, if you don't purposefully make the decision, then your firm will, by default, become a limited lifestyle firm with limited value beyond your retirement. Therefore, it is important to **make the decision and then proactively create the optimized lifestyle or enterprise firm you imagine**.

When should you make the decision?

It's rare that any firm can be an enterprise firm from the onset. Why? Because when you're in the startup phase, your focus is on sales and gathering assets. You expect to be successful, but you won't succeed if you start building an enterprise structure too early. So although this decision can be made at any time, in our experience, it most likely happens when the firm:

- Reaches $100 million or more in assets under management. The sweet spot to actively decide to change your firm is between $100 million and $200 million. In our experience, most don't make the decision until they reach $250 million in assets under management.
- Has more than one top advisor.
- Has built an infrastructure with seven or more employees.

Purposeful questions to ask yourself as you make your decision.

1. Do you want to maintain your role as a great advisor, or do you want to try a new, more managerial role?
2. Do you have the appetite for the significant work to transform the firm away from the individual into a team business?
3. Do you have a clear idea of who the next generation of leadership for your firm is?
4. Do you have family members in your firm who have a passion for the business?
5. Do you want your clients to be advised by you or by a new or different team advice model?

If there is more than one lead advisor:

6. Have you ever discussed the future of your firm?
7. Do you have a common vision?

Note that we didn't pose the question directly: "Do you want to be a lifestyle or enterprise firm?" Most advisors will say they are building or want to own an enterprise firm, as they may believe it's the "right" thing to say. Our survey results clearly demonstrate this tendency:

- Almost three quarters **(74%)** of our survey respondents indicate that they expect their practice will survive beyond their careers
- Nearly the same amount **(73%)** believe their brand differentiates their firm from others
- Actively acquiring new clients and operating efficiently rank among all respondents as the two most important business success factors

In our view, these are strong indicators that imply a desire to grow and reflect the owners' belief that they are building enterprise firms. The responses, though, are instinctive and do not necessarily consider the true commitment or capability of the key players or the amount of effort required.

Further considerations

This is not a moral or ethical decision. The advisory ecosystem will probably achieve the same steady-state equilibrium that you currently see in the law and accounting professions: a very small number of national firms, a somewhat larger number of regional firms, a still larger number of firms with a significant presence in individual cities—and a majority of the total number of firms functioning as solo practices or smaller firms. If this is true for the advisory profession, then most of the founders and successors reading this will opt for the lifestyle model, and the lifestyle model may continue to be the center of gravity in the profession for the foreseeable future.

However, in the future, the lifestyle practices will almost certainly become stronger, more intentional, and managed more professionally than they are today. We designed this white paper to help you make an intentional decision as to what you want your firm to look like in the future, and then, once you've made that decision, to achieve greater success in your chosen pathway.

- **You should choose the lifestyle model if:** You are uncomfortable managing teams and/or unwilling to devote the revenue to hiring C-level people such as a COO. This model applies if you believe that taking on the challenge would affect your personal time and personal revenues in unacceptable ways—and, importantly, you've saved at a rate where you don't need to monetize your practice to afford retirement.
- **You should choose the enterprise model if:** Your goal is for the firm to continue to serve clients after your departure from the profession, and you would like to confine your personal contribution to a particular area of interest or expertise.

BOB VERES
weighs in

I suspect some advisors have given up on following the enterprise model path, thinking that it's too late to embark on what seems to be a complicated and ultimately expensive endeavor. But if you look at the appendix to this report, you'll notice something interesting: 34% of the mature enterprise firms have been in existence between six and 20 years, and 7% have been around fewer than six years.

And lest you think that you have to dramatically staff up, notice (further down in the appendix) that 72% of the mature enterprises have 10 or fewer staff members. This may be evidence that these firms are taking great advantage of their outsourcing opportunities.

The point is that once you've mastered the startup phase, and created a workable lifestyle firm, you probably have the foundation in place to create that sustainable business that you might have been thinking about all along—and it might take a lot less time and staffing than you anticipated.

And if you worry about losing profitability, yes, there will have to be reinvestment in order to create the systems and procedures that are associated with a sustainable enterprise. But the appendix shows that 25% of the mature enterprises experience profitability levels in the 31% to 50% range, and even more, 37%, experience profit margins above 50%—almost certainly out of a much bigger pie. It's possible to run a large enterprise firm ***and*** *be significantly profitable.*

However, I agree with the conclusion here: there is nothing wrong with optimizing your lifestyle practice, and these firms will continue to be the backbone of the profession. If you choose to follow the road more traveled, then the best advice is to make the journey the best—which means most intentional—it could be, given your own unique goals and skillset.

FIRMING UP THE MATURE FIRM

The advisory business prides itself on helping clients prepare for the future. Yet, paradoxically, most advisors don't heed their own advice. Most advisors don't purposefully plot a path for their business. As you tell your clients, without a plan, you can't get to your destination. The same is true for your firm.

We've talked about the need to make a decision and to be purposeful. Once you've identified your business model, it is imperative to take action. And the ways you firm up your firm are very different. Use the following guide to make the most of your purposeful firm.

Phase - Mature: Lifestyle

People	Value proposition/brand	Investment philosophy	Technology
› Provide your people with profit sharing and bonuses. You want to provide instant recognition rather than long-term gratification. › Ensure there is a robust business continuity plan in place, with a clear destination for clients.	› Double down on the personality of the brand. › Focus on referrals and client/prospect events. › Segment your client base and pass the less profitable clients to a junior advisor.	› Unless you are a pure investment advisor, outsource to create efficiencies and systems that enable you to focus on solving client needs. › Spend as much time with prospects and clients as possible, with a focus on goals-based planning/investing. › Pursue a disciplined model portfolio process for scale. › Focus on the best income distribution strategies as the client base ages.	› Focus on client-facing technology such as client portals, financial planning tools and performance reporting. › Hone the client review reports/documents that are provided to the clients; you want to keep your clients as sticky as possible. › Update website with focus on the trustworthiness and qualities of the founder.

Phase - Mature: Enterprise

People	Value proposition/brand	Investment philosophy	Technology
› Define roles and job descriptions, and provide career path for team members. Create employee manual and performance reviews; you'll be bringing on new employees and you will want a good process. › Create a team client model, where more than one person interacts with the client. › Create succession plan with clear ways for the new generation of advisors to be partners. › Start to create the C-level—staff members with a management, not an advisor role. The COO is typically first. › Create partnerships or processes to find and bring on new employees.	› Create a new value proposition from scratch. It will be different. Find help to do so. › Create new branding that supports the new value proposition. › Look to broaden the client segments and services; you'll want a fuller range of services. › Create a multi-generational client program. › Create new lead generation models (such as COI partnerships, digital marketing, radio).	› Determine if investments are a key part of your value proposition, and if so, engage a CIO for non-core assets. › Expand your investment solutions (e.g., alternatives and tax management) to fit with your broader value proposition. › Ensure that your client reporting is especially good so that the client sees the value of your investment processes.	› Review and upgrade your technology and workflows to enhance efficiency with your new team structures. › Deepen the integration between the core technologies (especially CRM, financial planning and portfolio management). › Outsource your IT (including IT strategy, computer support and cyber-security).

WHAT HAPPENS WHEN YOU DON'T MAKE A DECISION?

If you don't make a decision, your firm will make it for you. Fall down the middle path, and there could be consequences.

No Decision

People	Value proposition/brand	Investment philosophy	Technology
› Low morale › Key employee retention issues › No continuity or next gen ownership in place › Inefficient business operations can reduce revenue	› No brand identity can limit growth › No value proposition can limit scope of services › Hard-to-justify fees	› Inefficient investment process can diminish client experience › One-off investment approach (no models) could add inefficiency, risk and expense › Overcomplicate by hiring investment specialists for non-differentiated assets	› No clarity on how to spend technology budget can lead to expensive mistakes › Technology budget is not given priority, limiting future profitability and efficiencies › In-house technology detracts from core business functions › Little appetite for technology efficiency

The move to an enterprise firm requires significant change management and should be done in a road map way, identifying the various initiatives and implementing them over time in a way that your budget will support.

The move to a purposeful lifestyle business, although not as traumatic as the move to an enterprise firm, is more work than most people envision. You should also approach it with a road map and complete it over time.

Our assumption is that the enterprise firm will create more value for the owners upon transfer or sale, while the lifestyle firm can generate more current income for the owners. Each has its own benefits and trade-offs, and both can be done on purpose—by design, not default.

CONCLUSION

In our combined decades of working with advisors, our research and thought leadership efforts have uncovered and analyzed best practices to shed light on the experiences of the nation's leading advisory firms. Time and again, we find that firms that have experienced the greatest success are those that are willing to move beyond their comfort zone, constantly evolving their businesses to adapt to new market realities. We believe that future success will be short-lived and increasingly difficult for firms that rely solely on old thinking or gut instincts. Becoming a purposeful advisory firm requires intention, prioritization and planning.

Appendix

Item	Startup	Emerging	Mature (All)	Mature (Lifestyle)	Mature (Enterprise)
Will you firm survive beyond your career? Yes	70%	73%	81%	80%	86%
Firm Maturity					
0 to 5 years	42%	15%	3%	1%	7%
6 to 20 years	41%	51%	38%	42%	34%
>20 years	17%	34%	58%	57%	59%
Revenue					
$150,000 to $250,999	85%	23%	1%	2%	
$251,000 to $500,999	9%	58%	9%	8%	11%
$501,000 to $1M	3%	16%	33%	33%	30%
>$1M	4%	4%	56%	55%	59%
Net Profit					
0% to 30%	47%	33%	43%	46%	39%
31% to 50%	18%	25%	25%	24%	25%
>50%	34%	41%	32%	29%	37%
AUM					
$0 to $25M	100%				
$26M to $75M		100%			
$76M to $150M			43%	37%	51%
$151M to $500M			43%	55%	28%
>$500M			14%	8%	21%
Charging for Service					
All commission	5%	3%	1%	1%	2%
AUM Only	18%	19%	28%	29%	28%
AUM + Commission	35%	31%	18%	20%	13%
AUM + Planning	16%	23%	26%	21%	34%
Is Fiduciary Important?					
Important	53%	57%	70%	69%	72%
Is Brand Important?					
Important	69%	68%	79%	77%	82%

Percentages may not equal 100

Item	Startup	Emerging	Mature (All)	Mature (Lifestyle)	Mature (Enterprise)
Revisit Brand					
Past year	57%	48%	45%	44%	46%
Past 2-5 years	26%	36%	35%	31%	41%
>5 years	17%	16%	20%	25%	14%
Technology					
I buy systems to address a solution	38%	28%	25%	29%	20%
I buy systems to support the overall integration	15%	23%	32%	29%	35%
I insource my technology	21%	21%	18%	21%	13%
I outsource my technology	21%	25%	22%	17%	28%
Technology Spend (% revenue)					
1% to 5%	35%	35%	35%	37%	33%
6% to 10%	40%	50%	55%	55%	54%
11% to 20%	19%	14%	8%	6%	11%
Employees					
1-2	74%	50%	12%	13%	10%
3-5	21%	39%	37%	36%	37%
6-10	2%	9%	32%	37%	25%
>10	3%	2%	20%	14%	28%
Firm's Primary Service Offering					
Financial Planning Only	9%	4%	3%	2%	3%
Investment/Asset Management	14%	8%	3%	3%	3%
Wealth Management	74%	85%	90%	91%	89%
How many clients?					
<50	29%	11%	3%	2%	5%
51 to 100	25%	30%	12%	13%	11%
101 to 250	29%	32%	34%	42%	23%
251 to 500	13%	21%	26%	23%	32%
>500	5%	8%	23%	19%	30%
Type of Firm					
B-D affiliated	53%	50%	36%	31%	42%
Hybrid	8%	6%	10%	8%	10%
RIA	33%	41%	52%	57%	46%
Other	6%	3%	3%	3%	2%
Age					
21 to 30	2%	2%			
31 to 40	19%	7%	6%	3%	10%
41 to 50	25%	31%	22%	20%	25%
51 to 60	30%	30%	40%	41%	38%
61 to 70	21%	27%	28%	29%	28%
>70	3%	4%	4%	7%	
How would you describe yourself?					
Advisor	69%	64%	59%	100% (61)	
Business Owner	31%	36%	41%		100% (86)

Percentages may not equal 100

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[1]CEB Wealth Management Leadership Council Agenda Poll; conducted in July and August 2016; n = 116.
[2]Investment Adviser Association and National Regulatory Services, "2016 Evolution Revolution: A Profile of the Investment Adviser Profession," April 8, 2016.
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Primary research included survey on Advisory Business Models; March 2017, n=400 Owners/Managing Partners.

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