charles SCHWAB
ADVISOR SERVICES

EXPLORING INDEPENDENCE

AS A REGISTERED INVESTMENT ADVISOR

“The most rewarding aspect of being independent is knowing that we own our business. We are our brand.”

—Stephen Korving
Korving & Company

EXECUTIVE SUMMARY

The financial industry environment is changing. Over the last few years, advisors have watched their peers migrate away from wirehouses and independent broker-dealers as those firms struggled to reposition themselves in the wake of the 2008 financial crisis. More and more advisors have responded to the market by taking advantage of the freedom and control that comes from operating as a registered investment advisor (RIA).

Clearly, the business is evolving, and advisors have noticed these trends. They want to understand which channel is best for them, and whether going independent will help them meet their personal and business goals.

But despite the benefits of independence—including the potential to keep 100% of the revenue and the freedom to determine the shape of the business—many advisors don't know whether independence is really right for them. Some aren't sure they want all the responsibilities of running their own RIA firm. Others imagine that the transition will be slow and complicated. And many aren't aware that independence can take many forms.

Fortunately, as the RIA channel has evolved and matured, more choices are available. Advisors have a spectrum of options to start or join the RIA model, along with the support to make a smooth transition.

It just requires cutting through the noise and finding the right fit.

In the following pages, we'll take a closer look at the options for becoming an RIA, including:

- Pure independence
- Independence with support
- Affiliation with a financial partner
- Setting up a business as part of an established firm or group
- Joining an existing RIA firm

We'll also discuss the benefits of becoming an RIA, analyze the economics of independence, and explore the role of the custodian in the RIA relationship.

THE MOVEMENT TOWARD INDEPENDENCE AS AN RIA

Why more advisors are choosing to become RIAs

The RIA channel has been growing steadily for the past several years. As advisors feel more confident in their options and support services continue to expand, analysts are bullish on the channel's future.

It's been a turbulent few years for wirehouses and independent broker-dealers (IBDs). Industry research indicates that the number of financial advisors overall has steadily declined since the 2008 financial crisis. The wirehouse and IBD channels have been hit particularly hard, shrinking by 2.5% and 4.3%, respectively, since 2008.[1]

The outlook is far more positive for the RIA channel. In fact, research indicates that the RIA channel is one of the only channels showing sustained growth, adding more than 6,000 advisors from 2008 to 2011.[1] The growth in assets within the RIA channel was even more pronounced, increasing by 7.5% in the same period.[2]

And many advisors are upbeat about the channel's future. In a 2012 Schwab survey of advisors at major financial firms, 76% said they expect to see a continued increase in the number of advisors becoming RIAs.[3]

So why are advisors continuing to flock to the RIA model?

They are entrepreneurs. Many advisors have an enterprising mindset. They're self-starters, organizers, and motivators, who are invigorated rather than intimidated by challenges. To many entrepreneurs, starting their own firm is a lifestyle choice as much as a business decision.

They are dissatisfied with the culture of wirehouse firms. Although most advisors say they put clients first, some wirehouse advisors are ultimately working for their firms as much as for their clients. Many advisors bristle at this lack of autonomy, in addition to the fees and "haircuts" that wirehouses impose on advisor earnings.

They want to build their own brands. In the aftermath of the financial crisis, many investors soured on the big Wall Street firms. RIAs can build their own brands from scratch, matching them to client priorities and advisor goals.

They want access to best-of-breed technology and support. Some wirehouse advisors and IBDs may be limited by their options for technology, compliance, and management support—and sometimes report paying for services they don't want or need. These advisors are increasingly turning to the RIA channel, which gives them the freedom to choose the platform and services that best fit their firms' unique needs.

In addition, advisors are growing more confident that they have what it takes to be their own boss. They see their colleagues enjoying success with the RIA model and are inspired to go into business for themselves.

"I became an RIA because **this is the future.**"

—Amit Stavinsky
Tamar Securities

7.5%

RIA CHANNEL ASSETS FROM 2008 TO 2011

6.3%

MORE ADVISORS IN THE RIA CHANNEL SINCE 2008

Source: Cerulli Quantitative Update 2012.

WIREHOUSE AND IBD CHANNELS HAVE SHRUNK BY

2.5% & 4.3%

RESPECTIVELY SINCE 2008

Source: Cerulli Quantitative Update 2012, historical change in total advisors by channel.

In 2011, wirehouses held 41.1% of assets. By 2014, market share is projected to drop to 34.2%.

Source: Cerulli Quantitative Update 2012.

THE FIDUCIARY STANDARD

Advisors serve as fiduciaries for their clients. Their job is to provide personalized financial advice and services to their clients, charging a fee based on a percentage of the clients' assets.*

Many RIAs work with complex portfolios and address unique needs that require a highly customized level of investment management strategy and consultation. Under the fiduciary standard, firms are required by law to act in the best interests of their clients.

RIA firms are registered with the Securities and Exchange Commission (SEC) or state securities regulators and are held to the fiduciary standard by the Investment Advisers Act of 1940 as well as similar state laws. As explained by the SEC: "As a fiduciary, an advisor must avoid conflicts of interest with clients and is prohibited from overreaching or taking unfair advantage of a client's trust."[4] Advisors are required to file annual Form ADVs describing their firms' business practices and client communications. Registration does not mean a government agency approves an advisor or reviews his or her qualifications.

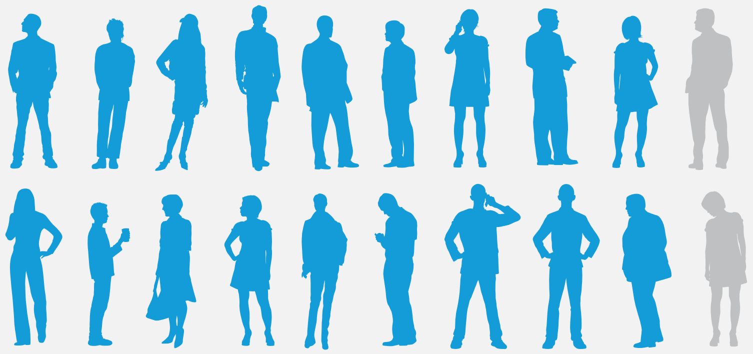
As one advisor remarks when discussing the fiduciary standard, "My organization is lined up to do exactly what our clients want. Whatever their issues are, wherever their life and wealth intersect, I can help make a difference."

* Independent RIAs and other financial services professionals receive compensation for services in a variety of ways. It is the responsibility of each investor to determine which method of compensation offers the lowest total costs and best aligns the interests and needs of the investor with those of the investment professional chosen.

COMMITTED TO CLIENTS

89%

of non-RIA advisors surveyed say they are more committed to serving their clients than to serving their firms.



Source: Charles Schwab Advisors Turning Independent Survey, 2012.

THE BENEFITS OF BECOMING AN RIA

Choosing Independence as an RIA Is Good for Business

Advisors cite numerous benefits to becoming an RIA, including greater autonomy and the potential for a larger income. However, much of it boils down to a single concept: control.

In a 2012 study, Schwab asked advisors at large firms why they found the RIA model appealing. Although the responses varied, they all shared a common theme: Advisors wanted a bigger say in how the business was run.[3]

Here are some of the benefits they identified.

Autonomy: RIAs have the final word on all decisions related to the business. They decide everything from the compensation structure to the technology platform to the sign on the office door.

Income potential: RIAs determine how much of their revenue they keep—up to 100%, depending on the model of independence they choose (see page 13). They can assert complete control over fees and expenses, choosing only the products and services they need. Firm owners can also build equity as they grow, leading to a higher long-term payout should they choose to monetize or sell the business down the road.

Client flexibility: While most advisors say they put a high priority on client relationships, the RIA model helps them deliver on that promise. RIAs can decide how to engage and communicate with clients—from building a marketing plan to creating a customized product portfolio for each client.

By contrast, some advisors are confined to their firm's business model, which often includes a limited number of products or services or prepackaged communications strategies. In addition, the net compensation of some advisors is tied to the products they sell. RIAs are under no such restrictions. However, RIAs are subject to the many risks and responsibilities of being a business owner. These may include oversight of the business strategy, business management, personnel management, compliance, and financial performance.

There are several additional reasons independence as an RIA may be attractive.

Access to the right tools: RIAs can choose the technology and platform that best suits their specific needs. The latest portfolio management systems and customer relationship management (CRM) systems make it easier to streamline workflows, access crucial information, and serve clients—all while adapting to an advisor's key priorities.

Opportunity to keep commission-based business: RIAs with successful brokerage businesses don't have to choose one model over another. With the hybrid model, advisors can offer advisory services as an RIA while keeping their commission-based business by affiliating with a third-party IBD.

Compliance options: RIAs have more options when it comes to managing compliance. They can conduct compliance in-house or turn to a third party for help, freeing up more time for clients.

BENEFITS OF INDEPENDENCE

Top three benefits cited by those who find the idea of becoming an RIA appealing.

1. Potential for a larger **income**
2. **Freedom** that comes with running your own business
3. Ability to **prioritize** client needs and **customize** client service and communications

Source: Schwab ATI Survey, 2012.

"It's really about the freedom to make decisions—not only for the business, but for your clients."

—Colin Higgins
The Golub Group

PUTTING CLIENTS FIRST

For advisors, acting in their clients' best interests is a key principle. But pressure to sell particular products or deliver returns to shareholders can take priority in some firms. Independent RIA firms face no such pressures. They have the freedom to put clients and their goals above all else.

Karen McCloskey, principal and founder of CMH Wealth Management in North Hampton, New Hampshire, appreciates the difference. Formerly a bank employee, she now runs her own RIA firm. "Our independence benefits clients every day because I can act on their needs, their instructions, and what's going on in the world around us," she says. "I can make that adjustment without having to go and get layers of approval."

A 2012 Schwab advisor survey revealed that 89% of respondents say they feel more committed to their clients than to a firm.[3] In fact, on average, 79% of clients make the jump with advisors when they turn independent.[5]

The numbers agree. Clients have been steadily moving assets to the RIA channel for the past few years. The median firm in Schwab's 2012 RIA Benchmarking Study ended the year with 4.7% more net new clients than the prior year and revenues up 12%.[6] The RIA model tends to create a special kind of advisor-client relationship because:

- It offers transparency: Clients know how much they're paying and the value they're getting.
- Advisors can offer unfiltered advice: They're under no obligation to sell proprietary products and can choose the solutions they think are best for their clients.
- Investments are chosen for only one reason: to help fulfill clients' goals.

"Advice is the most important thing you offer to your clients," says Leo Arms, who owns Thomas Leo Advisory, an RIA firm in Minneapolis. "They can get the transaction at many different places." The role of an independent RIA, he says, is to listen to what clients need, help them, offer advice, and "ultimately be compensated for the advice you offer."

> **"Advice is the most important thing** you offer to your clients."
>
> —Leo Arms
> Thomas Leo Advisory

FINDING THE RIGHT FIT

Understanding the Differences Between RIA Models

The advisor landscape is rapidly changing, and advisors have more options for levels of independence than ever before. But before making a decision, advisors should decide exactly who they want to be.

1 PURE INDEPENDENCE
The advisor opens a firm and maintains full control of the business.

2 INDEPENDENCE WITH SUPPORT
The advisor opens a firm but uses the services of a platform provider for help.

3 AFFILIATION WITH A FINANCIAL PARTNER
The advisor opens a firm with the help of a financial partner, who invests in the business.

4 SETTING UP A BUSINESS AS PART OF AN ESTABLISHED FIRM OR GROUP
The advisor opens a new office for an established firm and becomes the firm's employee.

5 JOINING AN EXISTING RIA FIRM
An advisor joins an existing RIA firm as an employee or potential partner.

MOST INDEPENDENCE ⟷ **LEAST INDEPENDENCE**

There's no right or wrong way to go independent as an RIA. Different models appeal to different personalities and aspirations.

Some advisors envision themselves in the driver's seat and relish the idea of building a firm from the ground up. Others want to control their own revenue and set their own hours but aren't crazy about negotiating contracts with multiple vendors for office and technology support. And some just want more flexibility in their client relationships but don't want to run a business.

Fortunately, the RIA channel has matured dramatically in recent years, as thousands of advisors have successfully chosen the well-worn path to independence. The transition no longer requires a leap of faith. Regardless of the option chosen, an advisor can leverage available resources and support to help with the transition.

Advisors considering independence have five models to choose from.

There's no cookie-cutter approach to going independent. What kind of model fits you?

PURE INDEPENDENCE

1 "I want the freedom to run the business my way."

What is it? The advisor opens a firm and maintains full control of the business.

Priorities:
- Full control
- Maximizing potential income
- Freedom and flexibility

Structure: The RIA is the true business owner. He or she decides which vendors and products best fit the business and makes all the necessary arrangements. This includes everything from hiring the cleaning service to establishing a brand identity and company culture. The advisor is responsible for all expenses.

Custodians like Schwab often offer consulting support, introducing advisors to third-party vendors to help with office setup, compliance, technology, and more.

Main benefits: Full control. Owners keep 100% of the revenue and can run the business however they want. The RIA also earns 100% of the equity that the firm builds through the years—which may pay off upon retirement.

Other considerations: This model can also work well for multiple advisors entering into a formal partnership, provided the advisors have complementary strengths.

INDEPENDENCE WITH SUPPORT

2 "I want to be the boss, but I don't want to deal with all the details."

What is it? The advisor opens a firm but uses the services of a platform provider for help.

Priorities:
- Full ownership
- High potential revenue
- Hassle-free operations

Structure: The RIA still makes most of the decisions but hires a platform provider to provide à la carte services. These services may relate to compliance, technology, reporting, financing, or office setup, depending on the arrangement. The platform provider contracts with all the vendors but provides some flexibility in vendor choice. The advisor pays a platform fee for the services.

Main benefits: The advisor has full control over the business but with fewer decision-making hassles. Notably, the platform provider doesn't take any ownership stake, so the RIA still receives 100% of equity as the firm grows.

Other considerations: It's relatively simple for advisors to transition from this model to full independence should they want more control.

AFFILIATION WITH A FINANCIAL PARTNER

3 "I'm willing to trade some control for financial support."

What is it? The advisor opens a firm with the help of a financial partner, who invests in the business.

Priorities:

- Up-front payout
- Easy transition
- Freedom to focus on clients

Structure: An advisor sells a portion of the revenue stream at a multiple to a holding company, which buys a majority or minority stake in the firm. This in effect monetizes part of the advisor's book. The advisor can take the payout in cash, in partial equity, or in some combination of the two. The financial deal is similar to a wirehouse relationship but typically offers a better upside for the advisor.

Main benefits: The advisor receives cash upfront, along with the potential for additional payouts as the business grows—typically in years three and six. The transition is also relatively easy, as the holding company handles most of the setup work. This gives advisors more time to help clients achieve their goals.

Other considerations: This is a popular model among advisors nearing the end of their careers who want to cash out and enjoy their retirement, and for advisors who want a lump sum to help pay off a loan. It's also a good option for succession planning, as it allows a firm to cash out an experienced partner while ceding the business to younger partners.

SETTING UP A BUSINESS AS PART OF AN ESTABLISHED FIRM OR GROUP

4 "I want to be independent, but not necessarily self-employed."

What is it? The advisor opens a new office for an established firm and becomes an employee of the firm or group.

Priorities:

- Freedom to focus on clients and business development
- Infrastructure support
- Work-life balance

Structure: As with the financial partner model, advisors enter into a financial deal and structure similar to a wirehouse. They join an established brand and gain access to the firm's built-in infrastructure, which may include technology, compliance, and more. One crucial difference, however, is the ownership structure, as advisors in this model typically acquire an equity stake in the parent company.

Main benefits: Advisors have more flexibility in client communications and product choice than do wirehouse advisors. They also have the potential to earn more, depending on the terms of the deal. And because someone else handles the operational details, advisors can devote most of their attention to their clients.

Other considerations: The firm's existing infrastructure and support make the transition relatively easy for wirehouse advisors. Succession planning is also simple compared with some other models, as the parameters are already defined.

JOINING AN EXISTING RIA FIRM

5 "I want to take smaller steps to independence."

What is it? An advisor joins an existing RIA firm as an employee or potential partner.

Priorities:

- Low-risk transition
- Flexibility
- Cultural fit

Structure: The structure can vary widely, depending on the existing firm. Some firms are content to split some expenses, take a percentage of the advisor's revenue, and let the advisor work independently. Others are looking for a complementary fit, perhaps targeting advisors who run different investment models or who blend in with the firm's culture. Financial terms are negotiated upfront.

Main benefits: Advisors can negotiate the best possible terms for their situation. That could mean an up-front payout, a partnership with long-term equity, or some combination of the two. Advisors don't have to deal with the challenges of building their own infrastructure, and they are free to interact with clients like a fully independent RIA, provided their strategy matches the firm's.

Other considerations: In many ways, this model provides the softest landing for advisors, as they're piggybacking on an existing firm's success. Most advisors report a smooth transition, with minimal disruption to their practice. Culture is key, however. Advisors should do their research and find a firm with similar values and aspirations.

CAN I KEEP MY COMMISSION-BASED BUSINESS?

Many advisors who receive revenue from commission-based business don't want to give it up when becoming an RIA. To keep a foot in both worlds, they may choose one of two hybrid models.

- Dually registered: The advisor starts or joins a fee-based RIA while affiliating with an independent broker-dealer (IBD) for transaction business. The advisor may have more flexibility in choosing advisory services and investment options, and may leverage IBD turnkey infrastructure or assemble a customized platform.
- Semi-captive: The advisor affiliates with a broker-dealer that has a corporate RIA and restrictions on RIA custodian access. The IBD chooses the custodian, manages and sometimes restricts investment options, and provides turnkey infrastructure and support.

The hybrid model is increasingly popular. In fact, no other channel in the industry is growing faster—the combined number of dually registered and semi-captive hybrid advisors grew by 6.9% in 2011.[1]

Choosing a hybrid model has implications for all aspects of an advisor's business. Key considerations include:

- The degree to which offering diverse brokerage and advisory products is important to the advisor's approach
- Long-term and short-term revenue goals
- The freedom to choose business partners and vendors
- Strategies for growing the business
- Equity ownership and whether it's a long-term financial and business objective

For more information about the hybrid model, see Schwab's MKT Report: Understanding the Hybrid Practice: Considerations for Advisors in Transition.

THE ECONOMICS OF INDEPENDENCE AS AN RIA

RIA Firms Enjoy Increased Earning Potential

The benefits of independence are an easy sell to many advisors, but a crucial question remains: How do the economics work? Schwab uses its experience with advisors to run the numbers and shows how an independent advisor's potential revenue compares with the wirehouse and independent broker-dealer models.

In analyzing the revenue potential of the RIA model, most analysts return to the same rough numbers time and again: 40, 85, and 100. They refer to the average percentage of client fees that advisors typically earn in each channel: 40% for the wirehouse advisor, 85% for the IBD advisor, and 100% for the RIA.[7]

It's important to note, however, that these percentages do not account for expenses but instead refer to the percentage of revenue that's under an advisor's control.

Wirehouse advisors earn a flat rate, with the remainder of the revenue belonging to the firm. The firm then divides its share between expenses and shareholder profit. From the advisor's perspective, expenses are fixed. On the plus side, this means wirehouse advisors don't need to worry about paying monthly invoices or negotiating with vendors. On the downside, wirehouse advisors often end up paying for products and services they don't use.

Advisors working in the IBD channel generally control up to 85% of their revenue. (Roughly 15% goes to broker-dealer fees.) In practice, however, they pay roughly 30% of that revenue in expenses, leaving them with 55% of the revenue—still an improved share over wirehouses.

Fully independent RIAs are in the best position to maximize their revenue. With no wirehouse or broker fees, they control 100% of their revenue. Assuming they dedicate 30% of that revenue toward expenses, that leaves them with a net compensation of 70%.

Hybrid advisors using an RIA as a custodian also tend to earn a higher payout percentage than IBDs, as they may pay broker-dealer fees only on their commission-based business. In contrast, IBDs traditionally pay broker-dealer fees on all their assets. Hybrid advisors using an RIA as a custodian typically fall between the IBD and RIA on the chart at right.

If an RIA firm is well managed, advisors can often increase their payout by a few percentage points. In Schwab's 2012 RIA Benchmarking Study, firms with the tightest expense controls reported earnings from 71% to 73%.

Schwab Advisor Services™ offers a number of practice management solutions to help advisors become more efficient and profitable. Schwab's annual RIA Benchmarking Study, for example, captures trends and best practices in the RIA industry, based on data from participating firms. Advisors can use the study to assess where they are, where they want to go, and how soon they can get there.

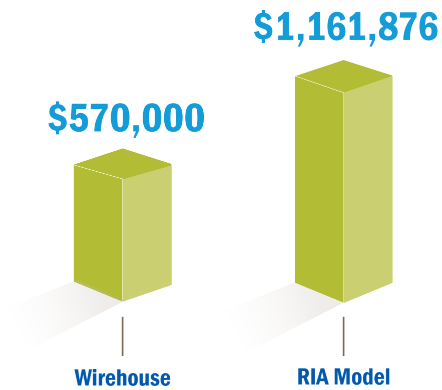
Advisors can also enroll in Schwab's Insight to Action practice management consulting program, which offers RIAs hands-on support and guidance on how to successfully grow and manage their firms.

ADVISOR EARNING POTENTIAL

Using $1 million in revenue as an example

	Wirehouse	IBD	RIA
Revenue	**$1,000,000**	**$1,000,000**	**$1,000,000**
Fees/Expenses			
House	($600,000)	--	--
Broker-dealer fee	--	($150,000)	--
Expenses	--	($300,000)	($300,000)
Payout or Profit	$400,000	$550,000	**$700,000**

Source: Schwab estimates. Hypothetical example.



PUTTING THE NUMBERS INTO CONTEXT

What do the percentages mean in practice?

Using its RIA Economic Discovery Tool, Schwab evaluated the potential increase in profits for a hypothetical wirehouse advisor transitioning to full independence as an RIA.

The example at left assumes the advisor is transferring $150 million in assets under management and is earning an income of roughly $570,000 at the wirehouse.

After accounting for expenses and transition costs, the analysis concluded that an RIA could potentially earn more than $1,160,000 in the first year on the same assets under management.

POTENTIAL FIRST-YEAR PROFIT AND INCOME

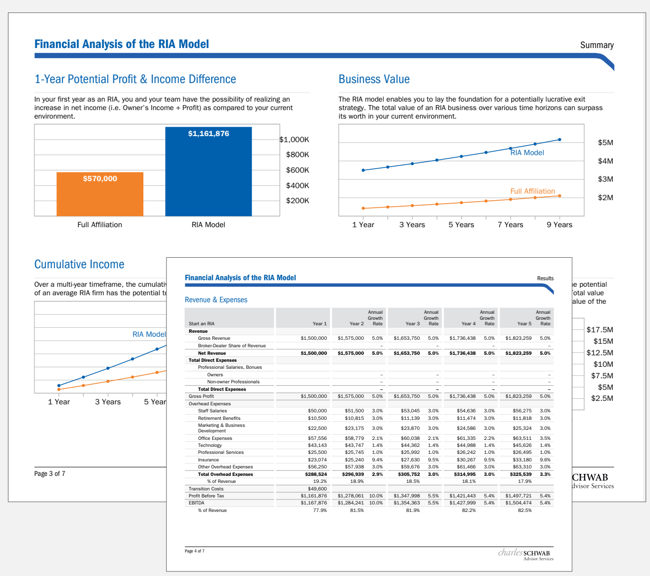
Advisors who switch to the RIA channel can potentially earn substantially higher net incomes compared with their current environment.

Source: Schwab Economic Discovery Tool. Assumptions: $150 million AUM, 1 owner/1 employee, 100% fee-based. Hypothetical example.

SCHWAB RIA ECONOMIC DISCOVERY TOOL

Advisors can use the RIA Economic Discovery Tool to evaluate how they would fare as an independent RIA. Advisors simply enter their specific data points into the tool. Using insights from Schwab's RIA benchmarking studies and the experiences of more than 7,000 advisors, the tool charts their potential income, profit, and business equity.

Contact a business development officer to create your customized report. To learn more about the tool, see advisorservices.schwab.com/econtool.



BUSINESS EQUITY AND SUCCESSION PLANNING

In addition to potentially earning higher incomes, owners of RIA firms also maintain another financial advantage over wirehouse advisors: equity. The RIA model allows advisors to lay the foundation for a potentially lucrative exit strategy.

RIAs have plenty of options for succession planning. They can sell the business, merge with another firm, or recruit an external or internal successor. In each case, owners can choose the outcome and financial terms that best match their goals.

There are several methods for valuing firms, but in general, multiples are higher in the RIA model than in the wirehouse and IBD channels. Recent transactions show that buyers are valuing RIA firms at four to six times cash flow for firms generating between $750,000 and $1.5 million in earnings.[8] When using revenue multiples, values range between 1.5 and 3.3 times the firm's gross revenue.[9]

Wirehouse advisors, by contrast, tend to receive a negotiated percentage of their gross revenue paid out over a 3- to 5-year period. The payout generally ranges from 100% to 180% of gross revenue, with 125% to 150% being the most common. IBD firms are commonly valued between the wirehouse and RIA models because of their mix of fee-based and commission-based assets.

Combine the potential income an advisor earns in each channel with the business equity, and the financial disparity between models is even greater.

It's also important to note that in the wirehouse model, advisors don't get to choose who receives their book of business upon retirement. While the IBD model offers some control, the RIA model gives advisors full autonomy to decide the legacy of their firm.

"Part of the reason you go independent is to grow. Before, as much as you grew, the house took 60% of that growth. Now, once you have your expenses covered, it's nice to see how every new dollar of revenue can **impact your cash flow and also the value of your firm.**"

—Brian Power
Gateway Advisory LLC

LEARNING TO MANAGE EXPENSES

RIA firms are in full control of expenses—they decide how much to spend on things like technology, compliance, insurance, marketing, and office setup. Unlike wirehouses and, to some degree, IBDs, RIA firms never have to pay for services they don't use.

But keeping a tight leash on expenses isn't always easy. Fortunately, Schwab offers ongoing practice management solutions, including programs and consultants to help RIA firms learn how to efficiently manage costs, create capacity, and become more productive and profitable.

UNDERSTANDING STARTUP COSTS

Once an advisor decides to go independent, more practical matters loom: How much will it cost, and how will I manage this?

Schwab can help advisors answer this and other cost questions, with tools to help estimate and track startup costs for an RIA firm and forecast expenses for the first few years. Schwab can also connect advisors to third-party vendors for additional support and offers a Business Startup Solutions program to help advisors get started.

Here are a few questions that will influence startup costs.

- Is the advisor starting a firm or joining an existing RIA?
- What's the current and future staffing mix? What will employees be paid?
- How much space does the firm need?
- What other infrastructure is required to open the doors?
- Is the advisor keeping his or her commission business? If so, who will the broker-dealer be?
- How will technology and trading be handled?

To provide a sense of likely startup costs, the hypotheticals below reflect conversations with advisors who recently made the switch.

Keep in mind that costs can vary widely based on the size of the team, the complexity of the offer, and which services the advisor chooses to outsource. Many of these decisions involve trade-offs. For example, choosing to keep most services in-house saves in up-front costs but takes up valuable staff time.

PROJECTED STARTUP COSTS FOR TRANSITIONING WIREHOUSE ADVISORS

$15,000–$35,000	$35,000–$75,000	$75,000+
Typical of firms with less than $100 million in assets under management, with a single owner and no staff	Typical of firms with less than $250 million in assets under management, with one owner and one or two staff members	Typical of larger, more complex firms with multiple staff members and owners
Major considerations: Technology sophistication, level of up-front legal support, initial branding impact, and choice of office space (home office, corporate office suite, standalone office lease)	**Major considerations:** Technology and benefits outsourcing, initial branding impact, and choice of office space (corporate office suite versus standalone office lease)	**Major considerations:** Technology and benefits outsourcing, initial branding impact and website sophistication, office location, and buy-versus-lease decisions on equipment
Note: Advisors transitioning from the IBD channel have most of their infrastructure in place already. Their expenses are typically limited to technology, rebranding, and legal assistance. Assuming average legal support, transition costs range from $15,000 to $30,000, based on the level of technology and branding sophistication the advisor elects.		

Source: Schwab RIA Economic Discovery Tool.

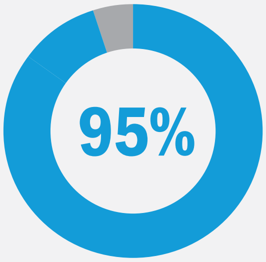
IMPLICATIONS OF ACCEPTING A BONUS

In the wake of the market turmoil in 2008, some advisors were offered retention packages and signing bonuses structured as forgivable loans. Secured by promissory notes and paid out over a defined period, these seemingly lucrative offers can be hard to pass up. Many advisors who signed the deals may not have fully understood the legal, tax, and financial implications of these agreements.

In general, such signing bonuses and retention packages come with extended repayment terms. These typically average from five to nine years, depending on the firm. Programs vary, but most share a few key features:

- The forgiveness of the retention amount typically depends on achieving some benchmark level of production over time.
- Not all of the bonus or retention money is paid upfront, but rather is predicated on future production targets.
- The financial advisor is required to stay with the firm until the end of the contract to be relieved of all repayment obligations.

To understand the fine print details of the contract and the tax implications, advisors should consult legal counsel before signing an agreement.



95% of respondents cited the opportunity for long-term financial success as an important reason for turning independent.

Source: Schwab Advisor Services, Advisors Turning Independent, Interviews with "Sophomore Year Advisors," 2013.

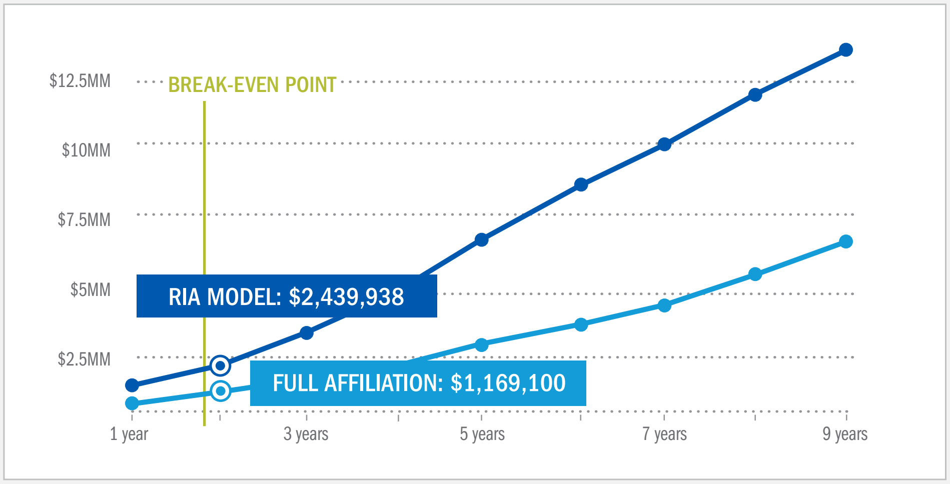
SUNSET PROGRAMS

Another technique, sometimes called sunsetting, is designed to encourage successful advisors to join a firm late in their careers or to stay with a firm until retirement. The advisor agrees to pass along his or her book of business to a teammate in the same firm in exchange for a share of that business at retirement. While seemingly attractive, sunset programs may restrict advisors' choices when transferring their book of business.

By contrast, advisors with equity in their firms often have more exit options and may earn more from selling their business than from a potentially more secure—but more restrictive—sunset program.[10]

CONSIDER LONG-TERM VALUE WHEN EVALUATING YOUR OPTIONS

Assume that a hypothetical advisor pays off an outstanding forgivable loan with a balance of $1.2 million. Based on the incremental income the advisor can generate in a move to the RIA model, the advisor can break even in a little less than two years. The chart here also illustrates the advisor's potential cumulative income in the RIA scenario, showing significant growth year over year. Not shown is the increase in the advisor's enterprise value as he or she continues to build equity in the growing firm.



Source: Schwab RIA Economic Discovery Tool. Assumptions: $150 million AUM, 1 owner/1 employee, 100% fee-based. Hypothetical example. The results generated by the RIA Economic Discovery Tool are limited as set forth in the Terms, Conditions, and Assumptions. The scenarios and alternatives covered are not exhaustive and may not be representative of those you actually encounter. Moreover, the simulated pro forma results are materially dependent on various assumptions and inputs, some of which are made and specified by you and some of which are static.

ROLE OF THE CUSTODIAN

The Custodian Acts as an Extension of the RIA

RIA custodians do much more than simply hold client assets. They also provide a range of investment and banking products, business management, technology, and service support to RIA firms.

It's easy for new advisors to think of custodians in purely functional terms. But a good custodian can be an RIA's best friend and biggest advocate. Custodians can provide access to a wide range of financial products, technology options, educational resources, and business consultants. Consultants work closely with advisors to help them develop a successful business strategy. Custodians also provide thought leadership and industry insights.

Moreover, custodians play an integral role in helping RIA firms serve their clients. A good custodian isn't merely a consultant; it's an ally in the advisor's success.

Given the importance of the relationship, advisors should thoroughly evaluate their options before choosing a custodian—keeping in mind that they can freely move from one custodian to another and can choose only the services they want.

Schwab Advisor Services™

With over 25 years of experience working with independent investment advisors and more than $800 billion in client assets, Schwab Advisor Services is the market leader in RIA custodianship.[11] Schwab offers a full menu of services for RIA firms.

While launching a new RIA firm can be exciting, it can also be intimidating, especially for advisors who have no experience running their own businesses. Schwab's business consulting team can ease an advisor's concerns by providing critical expertise on key business issues.

Management consulting: Managing a successful transition is just one of many factors that contribute to the success of an RIA firm. Schwab consultants help advisors see the big picture and create a holistic business strategy—including developing and implementing solutions to help scale the business, accelerate firm growth, and create a potentially profitable, sustainable model for the firm's future.

Technology and operations consulting: Schwab consultants can help advisors streamline operations by analyzing the effectiveness of the firm's back office, identifying opportunities for improvement, and developing solutions to improve the systems, processes, and workflows that are fundamental to a firm's success.

Compliance resources: Schwab connects advisors to third-party resources for compliance support, including consulting, insurance, recordkeeping, and software.

RIA Benchmarking Study: This powerful business-planning tool gives RIA firms access to insights and best practices from their colleagues in the RIA industry, helping them make informed decisions about how to build the business. Participating firms receive a comprehensive analysis of their firm's performance and how it compares with their peers, including insights into strategy, business development, financial performance, and more.

Insight to Action consulting programs: Our business consultants help advisors identify and address key issues that can affect a firm's success. Insight to Action programs include workshops, an immersive curriculum, and 1-on-1 consulting on business strategy, marketing and business development, client segmentation, and technology strategy.

"The difference between being the client of a custodian and being an employee at a large national firm is like night and day. If you work for a firm with 10,000 advisors, you can feel like the company doesn't pay attention to you and what you need. **But when you're a client, they're in business to serve you."**

—M.J. Nodilo
Pathlight Investors

"There are people out there who will listen and understand your needs. You don't have to go it alone and search for the best options without guidance."

—David Bromelkamp
Allodium Investment Consultants

Choosing the Right Technology

Wirehouses and independent broker-dealers typically offer 1-size-fits-all technology, with little or no customization available. Advisors working for these firms often end up paying for technology they don't want or use. Even more frustrating, they're stuck with the technology package even if it doesn't perform to their expectations.

RIAs, on the other hand, have the freedom to choose the technology they want, from portfolio management systems to CRMs. And they're not restricted to one company's technology.

Schwab offers a variety of technology solutions for RIAs through its affiliate company Schwab Performance Technologies®. Leveraging its deep understanding of advisor needs, Schwab Performance Technologies offers advisors the autonomy to build the platform they want.

RIAs can choose a complete turnkey package, such as Schwab OpenView Integrated Office®, or they can opt to build a technology system piece by piece from leading providers, then leverage Schwab OpenView Gateway™ integration to help connect them easily.

Schwab Advisor Center® is the centerpiece of Schwab's technology offerings. A comprehensive and secure custody and trading platform, Schwab Advisor Center makes it easy to open and service accounts, make trades, and manage portfolios with mobile solutions for both advisors and their clients.

When choosing technology, advisors should also consider the degree of support available. Schwab's technology and operations consultants can help RIAs get the most out of their technology—both today and as advisors' needs evolve.

"One of the great things about the RIA model is that you get to pick and choose the different technology packages that you want to use for your clients, **that best fit your clients' needs."**

—Fran Hoey
Hoey Investments

FOUR TIME-TESTED STEPS TO SUCCESS

1 **BUILD** A BUSINESS AND TRANSITION PLAN

2 **LAUNCH** YOUR NEW FIRM

3 **TRANSFER** CLIENT ASSETS

4 **PROVIDE** ONGOING SUPPORT

Making the Transition

Transitioning to independence can be intimidating. Advisors on the verge of starting, affiliating with, or joining an RIA firm often wonder about timing, costs, and legal risks, among other factors. Many are particularly concerned about how the transition will affect their clients.

Fortunately, resources are available to help advisors make the transition. Most custodians offer at least some transition support—from basic office setup to assitance through every phase of the move.

With an average tenure of more than 12 years at the company, the consultants at Schwab Transition Services have helped more than 1,460 advisors transition to the RIA model, and moved more than $122 billion in assets under management.[12]

Schwab tailors its transition support to an advisor's business goals. The degree of support is up to the advisor, but it typically starts with business planning, then moves into other phases.

Schwab's support services generally include the following:

Building a transition plan: Schwab appoints a business development officer to listen to an advisor's goals, evaluate his or her needs, and build a transition plan.

Setting up the business and back office: Schwab offers in-house and third-party referrals to help advisors get started, including resources for technology, legal and compliance, locating office space, marketing, and more.

Transferring client accounts: The Schwab Transition Services team prepares the paperwork for a hassle-free asset transfer.

Building a successful business: Schwab's service team and in-house consultants can help advisors operate more efficiently, take full advantage of the Schwab technology platform, and craft a long-term growth strategy.

The important thing for advisors to remember is that they're not alone. Custodians like Schwab have helped thousands of advisors successfully make the transition to independence. It's just a matter of deciding whether independence is the right choice.

GETTING STARTED

Interested in learning more about your options for independence? Contact Schwab Advisor Services™ today.

877-687-4085

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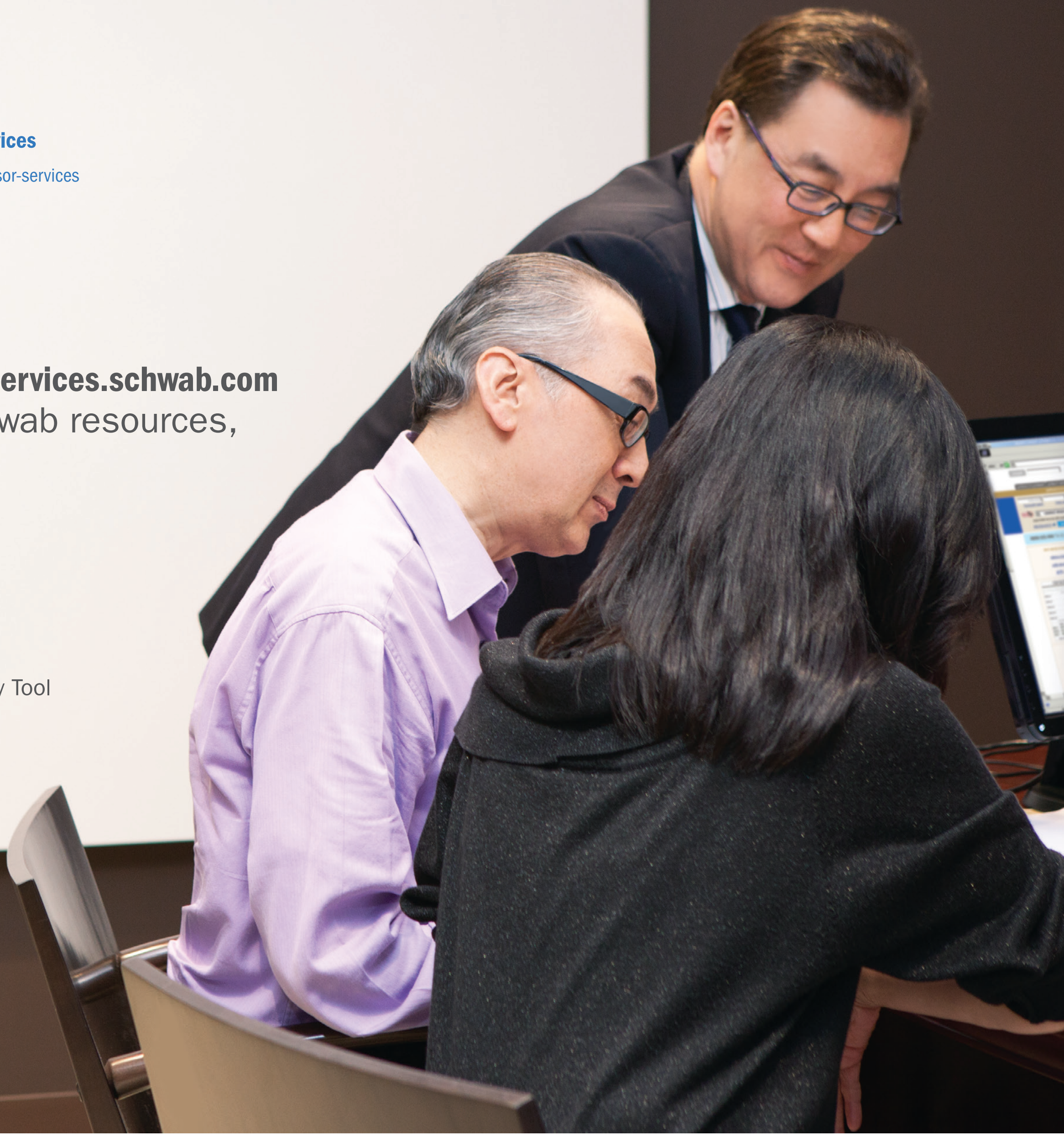
- White papers
- Webinars
- Case studies
- RIA Economic Discovery Tool



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“When we go out and canvass our advisors that have made the move to independence, the most common response we get is, ‘I wish I had done this sooner.’”

—Brian Hamburger
MarketCounsel

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Experiences reflected are not a guarantee of future performance or success and may not be representative of your experience.

The RIA Benchmarking Study from Charles Schwab comprises self-reported data from advisory firms that custody their assets with Charles Schwab. Participant firms represent various sizes and business models. They are categorized into 12 peer groups—6 wealth manager groups and 6 money manager groups, by AUM size.

Best-Managed Firms

This group, also known as High-Performing Firms, represents advisors in the annual RIA Benchmarking Study who are in the top 20% of qualifying firms, ranked by productivity (revenue per professional), profitability (standardized operating margin), and revenue growth (4-year compound annual growth rate in revenue). The top 20% of firms was calculated after removing those with less than $1 million in revenue or fewer than two professional staff. Best-Managed Firms were selected without regard to peer group, and most groups are represented in the Best-Managed Firms.

The **Economic Discovery Tool** (Tool) is intended solely for use by investment professionals. The Tool simulates the pro forma financial results of various hypothetical scenarios for establishing, operating, joining, and/or selling an investment advisory practice or firm and compares those simulated outcomes to various alternatives. The scenarios and alternatives covered are not exhaustive and may not be representative of those you actually encounter. Moreover, the simulated pro forma results are materially dependent on various assumptions and inputs, some of which are made and specified by you and some of which are static. These assumptions and inputs may not reflect actual circumstances, and thus the Tool is inherently limited and intended for general informational purposes only. The simulated pro forma results do not reflect, and are not guarantees of, actual or future results. Your actual results may be materially different from those simulated. Schwab makes no warranty of the accuracy or completeness of the Tool or the simulated pro forma results and shall have no liability for your use of the Tool. The Tool is not intended to provide financial, investment, legal, tax, or regulatory compliance advice. You are urged to consult your own professional advisors.

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