

The Registered Investment Adviser Advantage

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Introduction

In the current financial services business environment, an increasing number of independent agents are evaluating whether or not they should set up a registered investment adviser (RIA) firm or become an investment adviser representative (IAR) of an existing RIA firm. The RIA question will directly impact the success of many independent agents during the next ten years.

Retirement Planning and Investment Advice

The ability to offer written retirement and financial plans to prospective clients stands out as one of the main benefits of becoming an RIA or IAR. Being an RIA does not mean giving up on being an insurance agent. To the contrary, the two services are entirely compatible, and actually, are very complementary. By preparing a written plan for a prospective client, an agent is able to present himself as an adviser. Consumers have become very good at identifying agents who are just looking to sell them a product. Consumers want objective, financial advice that is personalized and customized for their situation. By preparing such a plan, the agent-adviser goes a long way in establishing trust, credibility, and in delivering a valuable service. Although preparing a retirement plan for a consumer does take time and expertise, the agent benefits are strong; they include the ability to:

- Demonstrate the Agent-Adviser's Objectivity
- Eliminate the Perception of Being "Just an Annuity Salesman"
- Analyze the Prospect's Current Investments and Identify Needed Changes
- Position Annuity Recommendations Within the Proper Context of an Overall Plan
- Get Hired to Manage Prospect's Investment Funds for an Ongoing Fee
- Provide Excellent Advice and Solve Problems
- Create Client Relationships that Produce Referrals

As an RIA, an agent is free to build a customized financial plan for each client's unique situation. Plans can include recommendations for the clients to purchase a variety of investment and savings vehicles. For example, part of a plan could be the recommendation of the best fixed index annuity for the client's situation (for which the agent will receive the standard commission from the insurance company), while another part of the same plan could be the implementation of a balanced portfolio using no-load growth mutual funds and income securities (for which the RIA will be paid a fee to manage on behalf of the client).

When hired to manage a client's investment funds, the adviser provides recommendations about whether or not to buy, sell, or keep specific investments. These recommendations can and should be highly customized to fit each individual client's situation.

It is important to note that agents who choose to become IARs (or RIAs) are *insulated* from accusations of providing "unregistered investment advice." However, that does not mean that agents can make reckless, totally self-serving recommendations and then escape the

consequences of their actions by hiding behind the shield of being an RIA. RIA or not, unethical, irresponsible behavior can and should be punished.

How to Become an RIA

To provide financial planning and investment advice, agents must be affiliated with an RIA firm as an IAR. There are three IAR choices for most agents:

1. Do-It-Yourself RIA
2. Broker-Dealer's RIA
3. Independent RIA

Do-It-Yourself RIA

Although not a viable option for most agents, any agent can set up a separate corporation and then register that corporation with their state's division of securities or with the Securities and Exchange Commission (SEC). Prior to registering, the agent must complete the series 65, 66, and/or possibly another exam, depending on the requirements in the agent's state. To register, the agent must then submit the appropriate application and disclosures to his or her state and prepare the RIA firm's ADV disclosure brochure. This is a lengthy document that describes what services the RIA firm provides, information about its staff, how it charges fees, and how it manages clients' assets. Most financial professionals who decide to establish their own RIA corporation are wise to retain an RIA consultant to help them with the regulatory application process. There are also ongoing state and SEC requirements such as filing annual reports, updating documents maintained by the regulatory body, and of course, paying fees. A separate errors and omissions (E&O) policy is usually necessary to cover RIA services, since the typical insurance agent E&O policy excludes coverage for these financial planning and investment advisory services.

Separate, and in addition to setting up and maintaining the RIA firm with the regulatory bodies, the RIA firm must also develop expertise and capacity in two very important areas:

1. **Managing Client Assets:** To manage client assets, an RIA must perform a variety of important functions that include:
 - Selection of a custodian to hold client funds
 - Development of investment portfolio strategies
 - Selection of investment funds
 - Monitoring of client accounts
 - Reporting investment performance to clients
 - Trade execution as necessary
 - Deduction of quarterly fees from client accounts
 - Organization and retention of client documents and correspondence
 - Development and testing disaster recovery plans

2. **Building Financial Plans:** To build customized financial and retirement plans, an RIA must have the *know-how* to:

- ***Build an integrated retirement plan*** with the proper mix of investment and savings vehicles. This requires financial planning expertise and experience with retirement income planning. For the safe part of the plan, the RIA must be well-versed in principal-protected strategies and, ironically, must be licensed to recommend and sell such products. For the rest of the plan, the RIA must know which investments to recommend in what quantities or percentages. Then the RIA must know how to guide the client on drawing income from these various components of their retirement plan to achieve the desired result.
- ***Clearly articulate customized recommendations*** to his or her client in way that is both accurate and easily understood. It also requires skill in computer software like PowerPoint[®], Excel[®], and Morningstar[®].

Agents should not be discouraged from embarking on the *Do-It-Yourself* route if they are prepared financially and mentally for the substantial work required for this approach.

Broker-Dealer's RIA

For agents who are already registered representatives of a broker-dealer, another approach to access RIA capabilities may be to become an investment adviser representative of their broker-dealer's RIA firm. This may be the same firm or a "sister" firm owned by the same company. Either way, an agent can get up to speed rather quickly offering RIA services to their clients. The RIA and/or broker-dealer should have already done the work to set up the RIA and have the capabilities to manage client assets.

Agents should understand two fundamental points when considering this RIA option:

- Broker-dealers are responsible for the recommendations that their representatives make, regardless of whether that recommendation is an immediate annuity, fixed index annuity, mutual fund, stock, bond, REIT, or variable annuity. Used incorrectly, or in the wrong situation, the sale of an immediate annuity, a fixed interest annuity, or a fixed index annuity, can do as much damage to a client's finances as a variable annuity or stock. Therefore, broker-dealers are completely justified in their supervision to ensure that all sales, variable and non-variable, are appropriate for each client situation. Accordingly, many broker-dealer registered representatives will be subject to supervision and *haircuts* on their fixed index annuities, not because the fixed index annuity product is a security, but because broker-dealers have the supervisory responsibility for whatever financial products their registered representatives may recommend. It is the association with a broker-dealer that drives supervision, not the product itself.
- Financial advisers who do not want their broker-dealers supervising their non-security activities, nor taking a piece of the commissions for that supervision, should be looking at other ways of doing business. Becoming an independent RIA allows agents to leave their

broker-dealers, eliminate broker-dealer supervision, eliminate broker-dealer commission *haircuts* on fixed product sales, and provide ongoing investment advice to their clients.

Many registered representatives have already left their broker-dealers or are considering such a move to escape broker-dealer supervision of their fixed index annuity business. Unless there are other reasons to maintain their broker-dealer relationships, many independent agents would be wise to consider affiliation with an independent RIA firm

Independent RIA

Agents who have never been associated with a broker-dealer or who have terminated their broker-dealer relationships may be well-served by becoming IARs of an independent RIA. Becoming an IAR of an independent RIA firm means just that. The agent becomes a representative of the RIA for the purposes of providing investment advice for a fee and preparing retirement and financial plans. With this approach, the agent is taking advantage of what the independent RIA has already developed and refined:

- Selection of the investment custodian
- Know-how on building investment portfolios
- All the administrative details
- Know-how to build customized retirement plans
- Know-how to present plans

The independent RIA firm can also guide the agent on their registration, facilitate E&O coverage for RIA services, and handle billing of clients and payment to the IAR-agent. The trade-off, naturally, is that the RIA will keep part of the fees generated by the IAR-agent. The RIA firm may also make financial planning support available for a fee so the IAR-agent can choose to use this service when a formal, written retirement plan is needed.

Other Considerations

As is obvious (from the table on the next page), establishing an RIA firm is no small task. The upfront and ongoing time required is substantial. However, agents should not be discouraged from establishing their own RIA if they can afford to spend time away from their day-to-day activities.

An obvious key advantage to establishing an RIA firm is that the agent does not have to share investment advisory revenues with anyone else. If an agent chooses to be an IAR of someone else's RIA firm, he or she will receive a portion instead of all the fees. Each agent must carefully weigh the opportunity of keeping more fees against the work required to do it all on his or her own.

The RIA versus IAR Choice

The following table provides a list of some of the tasks and requirements to set up an RIA firm or to become an IAR. It is not a comprehensive list. Agents choosing to set up their own RIA firm would be required to complete all items checked in the “RIA” column, while an agent choosing to become an IAR of an independent RIA firm would be required to complete those items checked in the column labeled “IAR.”

Task/Requirement	RIA	IAR
Establish Separate Corporation	✓	
Take Required Exam (e.g., Series 65)	✓	✓
Set up IARD Access with NASD Regulation	✓	
Prepare Form ADV Part 1A and/or Part 1B along with applicable Schedules	✓	
Prepare RIA Disclosure Brochure	✓	
Register Corporation as Investment Adviser Firm with State or SEC	✓	
Complete U-4 and Submit to IARD	✓	
Complete U-4 and Submit to RIA Firm for Processing		✓
Establish Written Policies and Procedures Manual	✓	
Prepare Investment Advisory Agreement with State Specific Language	✓	
Prepare Financial Planning Agreement with State Specific Language	✓	
Prepare Code of Ethics, Privacy Notice, and Policies for Particular Firm	✓	
Prepare and Test Disaster Recovery Plan	✓	
Find, Select, Evaluate, and Apply for E&O Coverage	✓	
Pay for E&O Coverage	✓	✓
File Annual Financial Report to State	✓	
Pay Annual Fees to State and Other Regulators	✓	✓
Maintain Minimum Working Capital Requirement for State	✓	
Prepare for Unannounced Audits by State or SEC	✓	
Determine and Maintain All Regulatory and Compliance Files	✓	
Maintain Client Files	✓	✓
Submit Monthly Reports and Requested Documents to RIA Firm		✓
Interview and Select Investment Custodian	✓	
Prepare Investment Risk Tolerance Questionnaire	✓	
Develop Investment Models to Match Levels of Investor Risk Tolerance	✓	
Select Investment Funds and Build Investment Models	✓	
Monitor Investment Models and Investment Funds; Replace as Appropriate	✓	
Develop Competitive Investment Advisory Fee Schedule	✓	
Calculate and Deduct Advisory Fees from Client Accounts	✓	
Identify Investment Custodian’s Applications for Each New Client	✓	
Prepare Investment Performance Reports or Pay Outside Firm to Do Same	✓	
Monitor and Recommend Changes to Client Accounts When Appropriate	✓	
Meet with Clients to Maintain Relationship and to Make Recommendations	✓	✓
Recruit, Hire, Develop, and Retain Investment Adviser Personnel	✓	
Stay Abreast of Evolving Regulatory Environment that Affects RIA Operation	✓	

Better, Stronger, Faster

Simply stated, the decision “to be” or “not to be” an RIA can be reduced down to whether or not being an RIA improves an agent’s ability to serve the needs of his or her clients. Today’s retirees, and of course, the upcoming wave of Baby Boomers, are going to expect their financial advisers to guide them on their complete financial picture. Besides offering fixed index and other non-variable annuities, agents would be wise to position themselves now to provide investment advice and integrated retirement plans to help meet their clients’ *overall* retirement planning needs.

About the Author:

David D. Holland is an independent financial planner, investment adviser, and annuity agent in Ormond Beach, Florida. He has sixteen years experience in the financial services field, including ten years operating his own financial planning firm.

David holds the following professional licenses and credentials:

Certified Financial Planner®
Certified Public Accountant
Personal Financial Specialist
Certified Retirement Planner®
Retirement Income Specialist
Chartered Life Underwriter
Chartered Financial Consultant
Certified Annuity Specialist
Certified Fund Specialist

David received his Bachelor of Arts in Business Administration from University of North Florida and his Masters of Science in Financial Services through the Institute for Business and Finance.

David is the CEO of three companies: Holland Financial, Inc. (a retail retirement planning firm), Retiree Investment Advisers, Inc. (an SEC registered investment adviser firm that helps independent annuity agents manage client assets on a fee basis), and Retiree Adviser Marketing, Inc. (an independent annuity marketing organization that provides annuity selection and planning support to agents).

David spends most of his time advising retirees on how to get the right mix of growth, income, principal protection, and liquidity for their individual situations. Most of David's new clients come from his monthly seminars and client referrals. In 2006, David personally wrote \$18 million in fixed annuities and another \$12 million in RIA accounts. He achieved this uncommon level of success by developing a comprehensive marketing and planning system to meet the retirement planning and investing needs of today's retirees. This system is available exclusively to annuity agents affiliated with Retiree Adviser Marketing, Inc.

Personal info:

David is 39. He is married to his high school sweetheart, Toni, and has three children. He is a Florida native and his interests include weightlifting, running, science fiction, and bow-hunting for whitetail deer. David has also established a private charitable foundation to directly fund restorative surgical procedures for disadvantaged children with craniofacial deformities caused by accidents, abuse, or genetic abnormalities.