ADVISORS

BECOMING A PROFESSIONAL BUYER

How to Harness RIA M&A Strategies for Growth

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INTRODUCTION

Welcome to the second white paper in PFI Advisors' ongoing series of industry content designed to help advisors build successful businesses.

Currently, there is a growing movement of independent RIAs looking to inorganic growth strategies through Mergers and Acquisitions (M&A) to capitalize on industry opportunities and trends that point to consolidation in the independent wealth management space.

There are significant mega trends impacting wealth management today. Advisor demographics; shifting client service expectations; encroachment by new, low-cost, online competitors; availability of advanced technologies; and changing regulatory requirements that will forever alter the delivery of financial advice.

As a result, a growing number of opportunistic RIAs are gearing up to become buyers of practices that either don't have the scale to survive in the new environment or will be looking to exit after a long, successful career as pioneers in the independent space.

However, becoming a successful acquirer is not a simple matter - M&A activities in wealth management can be extremely complex and potentially value-destructive if not done with due care and diligence. Furthermore, many aspiring buyers are not sophisticated in their approach, nor do they have a scalable infrastructure to easily support a successful M&A process.

Accordingly, PFI Advisors is pleased to present our recent research into the best practices and approaches for establishing an inorganic growth strategy. We've researched and interviewed top firms who have become adept at M&A to fuel their growth strategies and are looking forward to sharing their best ideas, along with profiles of their firms and approaches. This research can go a long way to helping aspiring firms looking for inorganic growth to gain a leg up on the competition.

We'd like to thank Angeles Wealth Management, Osborne Capital Partners, Savant Capital Management, and Summit Trail Advisors for sharing their stories so that the industry can benefit from their experience and wisdom.

To learn more about PFI Advisors' business and practice management content, visit www.pfiadvisors.com.

WEALTH MANAGEMENT MEGA TRENDS DRIVING CONSOLIDATION

The independent RIA industry has experienced an unprecedented surge in growth the last several decades that has made RIAs leaders in the wealth management space. As legacy wirehouse firms continue to decline, both investors and advisors are leaving to experience a better model for financial advice in an open architecture environment.

Cracks are beginning to form in the industry, however, that are creating both challenges and opportunities for future leaders. These "mega trends" currently impacting the industry will forever alter the makeup of wealth management, creating an unprecedented opportunity for consolidation as the historically fragmented independent space begins to mature.

Most notably, the aging of the advisor population is driving the increase in the need for ownership transitions as founding principals reach retirement age. Accelerating this demographic driver is the lack of succession planning throughout the industry, leaving the future for many of these firms in doubt.

According to recent research conducted by IMCA[1], one-quarter of the industry is planning to retire in the next 5 years, yet less than one-third actually have a succession plan in place, creating a growing urgency for these principals to find a transition solution – an excellent opportunity for growing firms to tuck-in these advisors and their clients through M&A activity.

Building upon the demographic aging of the profession are other industry shocks and mega trends that also point to consolidation and opportunities for M&A.

Chief among them are advancements in technology in the wealth management space. New capabilities now being wielded by the big online financial service brands and asset managers will force legacy advisors to have to invest significantly in the latest client experience and mobile technologies just to keep up. Additionally, these low-cost, online competitors are creating a dynamic that will drive fee compression, putting further pressure on firms' long-term profitability and sustainability.

Other significant regulatory changes, such as the DOL Fiduciary Rule, will increase the compliance costs for operating a wealth management firm. This has created additional reasons for not only aging principals but also for smaller firms that don't have the scale or operating leverage to seek out a larger firm to plug into in order to survive. Combine these factors with a war for advisor talent, the industry is creating a perfect storm for consolidation. Continued on pg 3

[1] http://www.imca.org/sites/default/files/2016-Q2%20IMCA%20Research%20Quarterly.pdf

Beyond a simple "asset grab," another compelling reason for existing RIAs to pursue M&A is to acquire talent. Top firms have invested in the operational infrastructure to gain scale; however, due to the aforementioned war for talent, there is a lack of next generation advisors entering the industry, thus slowing down growth plans. Acquiring emerging, growing firms that are struggling to reach scale and profitability - as well as onboarding disenfranchised wirehouse advisors - can be a powerful way to capture new talent to continue to fuel growth goals.

Despite these industry issues and trends that suggest the independent RIA industry is ripe for consolidation, M&A activity remains relatively sluggish. According to recent industry data, there are only roughly a hundred deals or so reported each year[2] for an industry that should be turning over a thousand firms yearly.

Why is that? Industry experts concur that there currently are very few options for selling advisors, and the buying pool is fairly shallow. Additionally, selling advisors often have psychological attachments to their firms and clients after years of nurturing them, along with strong emotions to continue their legacy. Thus, potential acquirers need to have a very compelling value proposition that brings confidence to the selling firm that their clients will be well cared for in order to make a deal happen.

When asked, many potential selling advisors have been put off by their choices, as the aggregators and roll-up firms do not appeal to their sense of legacy or outcome for their clients, nor do they provide compelling long-term economic value. Furthermore, many potential RIA buyers that sellers run into are not sophisticated in their M&A approach and are not able to articulate a compelling value proposition. Thus, these sellers remain on the sidelines.

That means that RIAs considering pursuing inorganic growth through M&A need to be prepared to respond to these seller issues by having a scalable platform, operational excellence, a strong service culture, and the ability to communicate these strengths so that sellers will be able to meet their ultimate definition of success by joining forces.

These capabilities are not just acquired overnight. Rather, it takes focused business and practice management effort to build and often requires bringing in outside consultants in order to properly prepare, prior to embarking on an M&A growth strategy.

"TODAY WE WOULD HAVE A LOT MORE SELLERS ENGAGED IN TRANSITIONING THEIR FIRMS, HOWEVER, THEY OFTEN GET TURNED OFF BY THE UNIMPRESSIVE BUYERS THEY RUN INTO. THERE NEEDS TO BE A LOT OF IMPROVEMENT IN THE BUYER COMMUNITY."[3]

- DAN SEIVERT
CEO OF ECHELON PARTNERS

[2] http://www.investmentnews.com/article/20160712/FREE/160719989/ma-deals-for-billion-dollar-advisory-firms-double-this-year

[3] http://www.riabiz.com/a/5052367338733568/spinning-200-years-of-legacy-culture-as-a-virtue-bny-mellon-uses-pershing-insite-to-show-its-software-side-softer-side----as-it-gets-beyond-netx360-and-men-a-hard-wired-approach

M&A GROWTH STRATEGY REQUIREMENTS

Based on extensive interviews with top firms who have been successful with their approach to M&A, we've identified the following areas that aspiring buyers need to have in place, prior to engaging with prospective sellers.

To become a professional buyer, it is critical to have:

- **A Clear Value Proposition** – Having an easily communicable message about your firm and strategic direction is critical to explaining why a potential seller would want to work with you and transition their clients. Whether that is a scalable platform, an investment management specialty, better technology, nurturing culture or other reason, being able to articulate what you stand for is critical for successfully closing an M&A transaction.
- **Technology and Operational Expertise** – Having an up-to-date technology suite and operational excellence that you can showcase to the selling firm goes a long way to building confidence that their clients will be getting an upgrade in service and operating leverage for their advisors to be able to grow faster than on their own.
- **A Multi-Disciplined Leadership Team** – Having multiple owners with specific management responsibilities provides leverage and expertise so that selling firms know their clients will be better served. Not only do these "departments" allow a less-sophisticated advisor to offer more complex solutions to his/her clients, but by handing over "servicing" responsibilities to these respective teams, it allows the advisor to get back to growing their clients and not have to worry about the day-to-day servicing of accounts.
- **Management Capacity for Deals** – Successfully completing a transaction and realizing the promised synergies takes a full-time, focused effort by one or two management principals. Thus, it is critical that the acquiring firm has management capacity available to follow through on the many logistical details, legal issues, financial implications, negotiations, due diligence and client transition requirements. For even the largest firms, they typically do not do more than 2-3 deals per year.
- **A Transparent Compensation Structure** - In order for deals to go through, acquiring firms need to have a clear equity, compensation, buy-out/exit schedule that is transparent and easily communicable for the firm being acquired so that they know what they will receive over time, as well as expectations for their role and responsibilities as they transition their business.
- **A Strong, Defined Culture** – For many deals it often comes down to personality. Having a strong, defined culture is critical to ensure there is a good fit for both seller and buyer. Deals can quickly go astray and result in damage if personality compatibility is not a priority. Many firms often define their M&A success in terms of the "deals they didn't do vs. the deals they did do." Firms tend to spend all of their pre-close efforts focused on the economics of the deal, but it always seems to be the ever-elusive "cultural fit" that will ultimately determine whether the deal is a success or not.
- **Transition Support** – In order to harvest the promised synergies from an M&A transaction, it is critical that a majority of the clients transition to the new firm and have a good experience in order to ensure retention. Having a powerful post-M&A transition strategy, team, and onboarding resources ensures that client transitions go smoothly and is paramount for success. For many leading firms, bringing in outside consultants on demand to provide additional resources and expertise post-transaction can be a flexible, efficient and cost-effective approach.

SAVANT
BUILDING IDEAL FUTURES

Savant Capital Management at a Glance

Savant Capital Management is a comprehensive investment and wealth management firm with multiple locations across the country, focused primarily in the Chicago, IL, Wisconsin, and Washington DC areas. After successfully growing the firm organically, Savant has recently concentrated on strategic acquisitions to spur growth and acquire talent.

Led by CEO Brent Brodeski, Savant's recent growth has been due to a series of acquisitions that has propelled the firm to national standing. "Our first deal was with a large firm in Washington, DC that had $500 million in assets back in 2012," Brodeski says. "Through that process we learned a great deal about what to do, what not to do, how to create value for acquired firms, and the potholes to be missed."

- **Founded:** 1986
- **Headquartered:** Rockford, IL, with multiple offices in Wisconsin, the Chicago and Washington DC areas
- **AUM:** $4.7 Billion
- **Staff Size:** 140

From there, Savant started to hit its stride and has since done a number of strategic transactions driven by both geography and capabilities. "Our clients really valued the tax work we were doing for them, however, it wasn't a core function that we wanted to build out, so we sought out an accounting firm to acquire and now do nearly 2,000 client tax returns a year. These new accounting capabilities also set us up to be able to expand into family office services."

The types of firms Savant is targeting are ones where the principal of the firm wants to, "Diversify and take some chips off of the table, but still stay involved," Brodeski notes. "We don't want to acquire them outright and have the advisors all immediately exit, rather, we want to take the operational back-office support and infrastructure concerns they have away and leave them to focus on growing their client base as part of our team. Often times this inspires the new partners to commit to another 5-10 (or more) years since they no longer have to deal with the headaches and the less fun aspects of running an advisory firm."

By plugging into Savant's resources, these newly-acquired advisors can leverage specialists that allow them to better serve their existing clients, attract more clients, and offer more sophisticated solutions. Taking advantage of Savant's in-house estate attorneys, staff accountants, investment team, financial planning experts, and experienced marketing team, advisors will be better suited to service larger, more complex client relationships. **"If you are a small firm doing it all on your own, you are a 'jack of all trades, and master of none;' Savant has a whole lot of 'masters' that are there to support client-facing advisors."** The new partners get to focus on the part of the business they love most (client relationships) and delegate compliance, technology, accounting, trading, reporting, HR functions and many other tedious aspects of day-to-day operations.

Brodeski advises that to do M&A on the scale that Savant is approaching, it is important to consider the management oversight that is needed and to stay disciplined on having one brand that standardizes investment philosophies, financial planning processes, technology tools, and service operations to create a highly leveraged structure that creates lots of value for the advisor and their clients. "We want them to become part of Team Savant, not just assemble an aggregation of individual firms."

Angeles WEALTH MANAGEMENT

Angeles Wealth Management at a Glance

Angeles Wealth Management ("Angeles Wealth") is an independent RIA founded by Jonathan Foster and Angeles Investment Advisors to provide personalized, discretionary portfolio and wealth management services for wealthy individuals and families.

According to Foster, "AIA serves as an investment advisor to endowments and foundations, and many of these organizations are blessed with support from wealthy, charitable families. We created Angeles Wealth to serve the wealth management needs of these families as well. Our investment research process is powered by the AIA institutional team, and our Angeles Wealth team does all the rest."

Foster came to Angeles Wealth as the past President of Carson Wealth Management in Omaha, NE, a top-ten Independent Advisor as ranked by Barron's Magazine. Foster has focused on growing the firm via three initiatives; harvesting leads generated by AIA, community outreach marketing, and recruiting a small number of elite, growth-oriented advisors to join the firm. "Angeles Wealth is not looking for retiring advisors in order to harvest their books. We are a creator of high-quality leads via our AIA referral pipeline. We are looking for experienced advisors who can join us, manage these referred opportunities, and bring their current clients to a better environment."

Angeles Wealth's key value proposition for advisors, Foster says, is the "Tiffany" reputation and institutional investment process of AIA provided to its private clients. "We are a great home for advisors looking for new business opportunities, a more robust investment offering, and the opportunity to help build an elite organization," Foster says.

Foster has extensive experience in M&A throughout his career, having bought and sold multiple companies in several roles in wealth management. His advice for doing deals centers on being disciplined and focusing on overall personality, culture and fit. **"I have always measured my success more in terms of the deals I didn't do vs. the ones I did do,"** Foster says. "If you stretch to do a deal that doesn't fit perfectly it can derail both you and your potential new partner, everyone will be miserable and lose years of their professional life."

Beyond a complimentary cultural fit, targeted advisors should be showing organic growth. "I appreciate the effort all the aggregators are doing, but some seem to be focused on quantity, not quality. If you acquire a business that's not growing when you buy it, it's not magically going to start growing after you buy it." A proper M&A strategy should be focused on a few accretive acquisitions or tuck-ins, rather than driven purely by attention-grabbing volume. "The true value is achieved through cultural synergy, great organic growth, and better operating margins," says Foster.

- **Subsidiary of Angeles Investment Advisors ("AIA")**
  Founded: 2001

  Headquartered:
  Santa Monica, CA

  AIA Total Assets under Advisement:
  Over $27.5 billion*

  AIA Assets under Discretionary Management:
  Over $2.5 billion*

* Assets as of May 31st, 2016

OSBORNE PARTNERS
Capital Management, LLC

Osborne Partners Capital Management at a Glance

Osborne Partners Capital Management, LLC (OPCM) is one of the oldest independent RIAs on the west coast, with nearly 80 years of experience providing multi-asset class portfolio management for high net worth individuals through discretionary management of individual securities.

- **Founded:** 1937
- **Headquartered:** San Francisco, CA
- **AUM:** $1.5 billion
- **Full Time Staff:** 22

"We like to say it spanned 65 years to reach $300 million and then only another 15 years to pierce $1.4 billion," says Justin McNichols, CIO and Principal of OPCM commenting on the firm's history. "Key to that growth expansion 15 years ago was a focus on expanding our investment discipline to include multi-asset classes, as well as a change in management philosophy to elevate the next generation of firm leaders."

As part of that growth strategy, OPCM has been active in acquiring other independent advisors and firms. "We identified acquisitions as a strategic way to augment our high growth," says McNichols. "It really started out as more of an opportunistic approach, but now is a key focus going forward."

The first deal OPCM did was a 2-person team from a bank that had $100 million in assets. "The bear market at the time really stopped the bank's asset management build-out, and it was a win-win for both parties," McNichols said. Following that deal, OPCM targeted another 2-person advisor team, with approximately $100 million in assets that was looking for scale and support so that they could continue to grow and have a succession plan.

McNichols credits their success in attracting these tuck-in acquisitions to their comprehensive back office systems and support along with their unique investment approach and transparent management style. **"At our size, we can offer advisors the same type of office life they would experience at the large institutions, but with more freedom and without the fear of a constantly changing compensation package."** OPCM offers an in-house investment team of CFA Charterholders, and a client service team of CFP's or "portfolio counselors" that service client relationships and complete financial plans. Newly-acquired advisors can service their clients or shift their attention back to business development (what they may truly enjoy).

McNichols' advice to aspiring buyers is that personality fit is the most important aspect to making a successful deal. "The process should be thorough where you interact with your future partners in different settings, environments and activities in order to get to know the real person before committing to a career merger."

SUMMIT TRAIL ADVISORS

Summit Trail Advisors at a Glance

Summit Trail Advisors is a recently-launched RIA, yet has decades of experience in its advisor and leadership teams. Formed by three groups breaking away from Barclays, Summit Trail's vision is to provide the investment prowess and resources of a private bank through the independence of a boutique.

"Most experts will tell you that when you are just getting started with your RIA, you shouldn't also be engaged in M&A activities," said Managing Partner, Jack Petersen. "But we did and believe that strategy will be key to our long term growth."

- **Founded:** 2015
- **Headquartered:** New York, with offices in San Francisco, Chicago, and Boston
- **AUM:** $3 Billion
- **Staff size:** 38

Summit Trail quickly brought on two additional teams via a lift-out strategy to begin the establishment of a national footprint and has focused on building expertise in the critical areas of a powerful investment platform, cutting edge technology and operational excellence.

"Our key value proposition for teams looking to grow their business is our multi-disciplined management team," Petersen said. "We have industry veterans and experts at all of the key roles necessary to provide a complete solution for advisors looking to focus on growing their business with us, while not having to worry about the constraints of their current employer."

Summit Trail has aggressive growth plans and is targeting advisor lift-outs from both traditional wirehouse firms as well as independent RIAs looking to jump start their growth. "Many advisors are very good on the planning side, but don't have access to a differentiating investment process," Petersen said. "We have a very robust investment platform that includes an in-house six-person research team from industry leading firms and relationships with 3rd party managers that date back over 10 years."

In an effort to attract more RIA sellers, Summit Trail has recently established a relationship with a third major custodian, in hopes of providing a robust back office solution for all potential candidates. **"Wirehouse advisors are stuck with outdated technology – we are big believers in using technology to drive productivity and to enhance the client experience.** The advisor experience in the independent space compared to the broker-dealer community is night and day, and only going to get better."

Petersen believes that recent industry changes are creating a unique opportunity for sophisticated, elite brokerage advisors to seek out alternatives, such as the boutique, independent RIA model. "As an employee advisor, it is such a challenging environment to work with large, sophisticated clients and be able to offer them all of the products, services and access they need to meet their goals. We believe that Summit Trail can be a great fit and are excited to be able to offer a complete solution."

ABOUT PFI ADVISORS

PFI Advisors, LLC ("Pure Financial Independence") was founded in 2015 with the following mission in mind:

To further evolve the RIA industry from a collection of "practices" to "businesses," and to be a continued voice in validating the industry as a legitimate landing spot for billion-dollar teams and their clients.

PFI Advisors is pioneering an operational consulting service that supports the unique back-office, technology, and operational needs of RIAs in growth mode. PFI Advisors conducts Technology Assessments, manages Technology Conversions, and provides M&A Preparation and Integration Services.

For breakaway advisors, PFI Advisors manages full RIA set up and transition to Independence, including office build-out, RIA infrastructure, client transition, and billing services, all for a simple consulting fee. There is no complicated long-term AUM fee structure or equity stake required to build the firm's future and provide advisors **Pure Financial Independence.**