Recruiters to Advisors: Cut Your Best Deal Now

BY **KRIS FRIESWICK**
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It shouldn't surprise anyone that if you put nine top recruiters in a room to discuss the state of the wealth advisor industry, they would come down on the side of now would be an excellent time for many of those advisors to make a move. But over the course of the day-long discussions that comprised On Wall Street*'s 2014 Recruiter's Roundtable, it became clear that their reasons were far from self-serving.*

These talent scouts recognize that 2013 was a stellar year to be an advisor, with a rising market lifting all boats. But—cue ominous music—the group also sees trouble brewing in paradise, beginning with the FINRA transition package disclosure rule that will most likely be enforced. Meanwhile, other changes are afoot that make the timing right for advisors to take stock and consider a move. In the wide-ranging conversation that follows, our panel of experts explains their thinking.

KRIS FRIESWICK/ON WALL STREET: What does today's landscape look like for advisors?

DANNY SARCH: Ten years from now, I believe that we're going to look back on the last couple years and maybe the next few years as the "glory days." These are really the best of times. If you're a substantive advisor you've never had more choices. You've never had more options. You've never had more freedom. You've never had more client loyalty. This has been a wonderful market. The advisor who doesn't consider moving during this time will look back in the future and say, "why didn't I get in on the ground floor of something exciting or take a check before disclosure or before things changed?'"

RICK PETERSON: The universe has expanded a lot in the past years. We have a lot more firms recruiting than we used to. There aren't as many major firms anymore, but there are a bunch of smaller firms that have emerged and are in great shape to get at some of the brokers who they used to always wish they could have and now they're seeing them. The dynamic has kind of changed over the past year. The bad publicity that sunk many firms a few years ago, either through acquisitions or legal problems, has largely disappeared. So what we're noticing is brokers are not fleeing the big firms anymore.

RICH SCHWARZKOPF: I think we're in a shrinking industry. There are 12% fewer brokers than there were four years ago. The average age is older. And half of the assets in this industry are run by guys who are in their early 60's. We have more money in this country than ever before and yet fewer brokers dealing with it. The money is flowing away from the big houses; their control over client assets is diminishing every year. I think this wirehouse model of only going after high net worth clients only is a broken model.

ELIZABETH MCCOURT: I think that the aging advisor population and the stopping of the trainee programs are real issues. How do you get new advisors to come into the business? I don't think the older advisors are adapting enough for the new money that could potentially be coming and that wants things more automated.

MICKEY WASSERMAN: I think we're seeing a larger divisiveness and a class system among brokers. There are the higher producers and the lower producers and trainees coming in. And I do see that lower producers are starting to get squeezed out regularly from the wirehouses and there's going to be room for them at the smaller houses. The wirehouses are going to continuously look for ways to keep and retain larger producers, the million-dollar plus producers. And if that means new retention plans, so be it. They're going to take the money away from the smaller producers and give it to the larger producers.

BILL WILLIS: There's complacency out there, there are retention deals, but you know when this year's better than last year and this month's better than last month, it's hard to think about disrupting that momentum. I think that's what we're seeing right now. But it is probably the single best time to make an exit and make one of the selections that's right for you. Because clients are very happy right now; their returns should be very good on all types of basis. Disclosure's coming. We don't know when; we don't know what it's going to be. But we know what we have now and we don't know what we're going to.

OWS: Let's talk about the new types of advisory models that are emerging. Which ones are capturing your attention?

JONATHAN MANELA: Technology has advanced enough so that the Fidelitys, the Pershings, the Schwabs, these firms can take you as an individual financial advisor, and, if your entrepreneurship is strong enough, you can build your own boutique operation and bring in other advisors around you to build your own private shop. You've been able to do that for the last five to 10 years, but what's changed in some of these boutiques, I think, is the leadership. So when you combine technology and this independent model with leadership, you can create businesses that appeal to more of the higher net worth type advisor; that's been the significant change. I think a lot of the smaller producers have been doing this for years. Now you're seeing larger producers do it.

MCCOURT: One thing I see is that the most entrepreneurial high-end advisors are still afraid to make that jump toward independence. A lot of the ones I'm talking to would rather be legitimized by a big name firm. I'm still seeing a fear factor. I don't think that there is this massive flow to go independent. I think it's a great opportunity, and it's one of the most entrepreneurial businesses that you can have. Yet there's still not a major flow to independence.

WASSERMAN: Many of the higher net worth advisors would like the structure of a major firm around them when we have a uniform fiduciary standard coming up. We're looking at a regulatory environment that's going to be very strict. Being independent means you have to be in control of those things and pay for your own attorneys, and I don't know if a lot of advisors really want to go that route. So I don't see the exodus from the wirehouses being as great as some of my peers do.

PETERSON: Yes, some advisors are a little afraid to go into independent. They're afraid of paying their own bills. They're afraid of the payroll, the health insurance issues that people have. But there are only a couple of ways to accumulate wealth. One is with stock or stock options; the other is to own your own business. They're starting to buy that. We've been selling that for several years, but as they talk to people who have gone independent, they see that it's a lot easier than they thought. I think the word is getting out that it's become a very logical and a very positive step forward in their career, as opposed to just a sideways move.

MINDY DIAMOND: RIA-land always existed, but the big advisor who wanted cachet would never have considered it. Today, the custodians and technology allow them to duplicate the desktop, and the experience and the service of a wirehouse in a boutique, so advisors are really working in a turnkey environment. The cherry on top is getting not only cash but equity, which again is a way to create wealth, or to build wealth, that wasn't necessarily available to them as an employee advisor.

OWS: What do you think about the wirehouse strategy of focusing on high and ultrahigh net worth clients and pruning smaller producers in favor of the big producers?

SCHWARZKOPF: It just seems ridiculous. I was a broker and some of our biggest accounts started as $50,000 accounts; they didn't start out as a half a million-dollar account. They're just focusing on the now and not the future. They're not training; they're not going after the young money; I think it's a disaster.

SARCH: The problem is, if you're focusing on the smaller client, you have to generate so much from so many different households that you can't possibly provide the same level of service.

DIAMOND: Advisors wouldn't argue that servicing a large number of lower net worth clients may not be as profitable and, with the regulatory environment changing and the fiduciary standard, they want to have a small number of high net worth clients. But the broader issue for advisors is the issue of control. They want to be the ones to make the decision whether Joe $50,000 client today could be my next millionaire tomorrow. It's the mandate, I think, that is really troublesome. And that puts, almost without exception, something about independence in every conversation with a quality advisor, because everybody's looking for more control.

SCHWARZKOPF: I don't really care too much about the wirehouses, but they're making their own bed and they're missing a big part of this country's growth.

SARCH: When we talk about the different models, you have to remember that, as much as the grab for the client assets is there, the client has more choices than ever before. I've got a neighbor who's retired, wealthy and in his 70's, and when I asked him about his advisor, he said he trades on his own. He chooses to do the research on his own; he just loves it and has immersed himself in it. He does have somebody review his portfolio who's an RIA. He pays this woman by the hour to review his portfolio; something I had not heard of before. His view was that he didn't want the agendas of the advisors.

WILLIS: Danny's opened up an interesting topic: fee-for-advice. In the not-too-distant future, rather than pay a fee based on assets, clients will be charged on an hourly basis, with some type of retained arrangement for hours per year. What we're doing right now—fee on AUM—is probably better than paying on a commission basis. But does it make sense to charge someone with $800,000 more than someone with $700,000? It doesn't make any sense at all. It's not fair. You're a victim of the system if you're a client. You should be charged for the time that advisor spends advising you. And how do you calculate that? What are the standards? That's to be determined, but I believe we'll be seeing that, and superior advisors will be able to charge more—just like a well-known attorney with a good track record. I think that's the right way to charge people.

PETERSON: The next logical step is that we actually charge customers for the quality of the advice. Brokers would get compensated by how much they've grown their client's assets or net worth, as opposed to the number of transactions or a 1% fee or whatever.

SARCH: Doesn't a 1% fee essentially incent them to provide better performance?

WASSERMAN: It's a major change that we're talking about in the United States—going from a commission-based situation over to a salary-based or hourly-based situation, and I don't see it coming anytime soon.

MANELA: The firms won't even pay a multiple on your transition packages for consulting advice. If you're an independent and you drive $1.3 million in revenue and $150,000 in consulting advice, the firms are going to discount that from your deal. It's just not worth that much to the business, which ultimately is why we won't see larger firms move in that direction.

DIAMOND: The mere mention of "salary/bonus" as a compensation model has made most advisors say, "I'm out of here." It also speaks to the notion of Merrill pushing advisors to up their fees. We've talked to a lot of advisors who are offended by the notion. Not that they don't concede that they'd like to be charging more, but it's about control; advisors want to be able to determine when they do it. There's been a lot of talk about the industry moving to salary/bonus. Some firms may, and there will be a number of very smart firms that won't, and they'll be the ones where people fly to.

MANELA: It'll be the best day for all of us.

COMPENSATION FOR 2014

OWS: Where do we see that trend line going in terms of the amount of money advisors are going to be able to take home in 2014?

SARCH: I think that the firms are all terrified; they all would love to cut pay. Morgan Stanley raised its grid level by 10%. That's the first salvo; they are watching to see what happens in terms of that. They all would love to do that. But they're all scared to do something dramatic to the bigger producers. So instead, each year they tweak their payout plans to either drive behavior or charge a fee to the advisor. It's not enough to make a single advisor say, "I'm out of here," but it's another little paper cut that's annoying.

MANELA: Certain firms are rewarding advisors for growth. For the last two years, Wells Fargo has been giving advisors on the bank side who have 15% revenue growth a retention bonus, which is tied to some very long-term deferred comp program. That might be something that other firms start to do, or Wells Fargo does for some of the financial advisors within their organization as a way to keep people in their seats.

WASSERMAN: I predict average advisor income of about $400,000 through 2014. I don't see any major changes. Where there may be changes—and some very creative changes—are in their deferred compensation in order to give them golden handcuffs or to try to tie them up for future years to come.

WILLIS: Just a comment on retention packages. I think we'll see some additional retention packages as attrition picks up at these firms and as existing packages wind down.

OWS: Even though they've stated that they're not going to?

WILLIS: Right; they're saying that. They're kind of opening the door. But if people run out that door, you might see some packages. The payouts look flat out there for 2014, but there are incentives to encourage advisors to sell a lot of products that create revenue for the firm and pay them either once, or not at all. Lending seems to be everyone's favorite, and it grossly underpays the financial advisor relative to the revenue it brings to the firm. Many firms are aggressively promoting all forms of lending. So in a sense, it's a bit of a pay cut when you don't get paid on a piece of business.

SCHWARZKOPF: The grids at the large firms are so incredibly difficult to understand. If you have to put your grid on a 25-page document, very few people will understand it. Advisors don't really know how much they're getting paid. The actual pay is going down because the products are being peeled off and paid differently. Comp is down. It's going to go down forever.

SARCH: I agree that these advisors generally don't know what they make. I tell them to do an exercise, which is pretty basic. Take your W-2. Get a year-end production run. Do the division and that's your payout. Now, compare that to what the firm says you're making at that level. It's always less because of all these other charges. That's the thing that's so eye-opening to these advisors.

DISCLOSURE DISCONNECT

OWS: Let's talk about the inevitable disclosure rule. How bad do you think it will be?

DIAMOND: We all sort of expect it to pass in some form at some point; we're waiting now to see if the SEC approves it. We think that they will. By and large, we think that high quality advisors—those generating more than a million in production who service a relatively affluent client base—are not bothered by the notion of having to tell the client what they were paid or how they were paid it. But I wouldn't want somebody else telling me I had to have that conversation, and there are plenty of clients that in a vacuum wouldn't understand how I'm comped or what it means.

PETERSON: I have said that brokers should be proactive on this for years, and years and years. Anyway, the first thing I think a broker should say to his client is, "Yeah, I did get a check. I got a big check. But why did the firm want to give me such a big check? Because every firm that offered me big checks to come over recognized that I do a pretty good job for my clients. The reason they valued me so highly was because of the quality of my advice. Why did I take it from Firm B? I actually was offered more money to go to a different firm, and I did not accept it. I was even offered some financial incentives to stay right where I was. I didn't do that either. I left, Mr. Client, because there are so many other good things that Firm B can do for you and me that Firm A couldn't. That's why I left." If they take that proactive approach, I can't imagine a client being upset about it.

MANELA: When I communicate with my family or friends and explain to them what it is that I do, they don't get it. The percentage of clients, wealthy or not, sophisticated or not, that truly understand the economic relationship that a financial advisor has with the parent company is so small that this is only going to bring about questions.

MICHAEL KING: I think it's going to have some impact. The spinning of it, as we're discussing now, is the only way to go. But someone has pointed out to me that if the broker has done well for the client, and the client is making money, it's going to really be a non-issue. But if the client has lost money, it's going to be harder to deal with.

SCHWARZKOPF: I don't think it will have any effect at all; I think it's a non-event. I don't think one broker will not decide to move because of it. I think it's a discriminatory, illegal law if it passes, but you know they can pass what they want. If a lawyer was paid to move to another firm, no one would say anything. I think it's discriminatory toward one industry in the United States. Any other sales position—whether you're in tech sales, computer, legal—you can move and get a bonus check for moving. Why choose our industry?

OWS: I bounce that question back to you. Why? If you had to put on your regulator hat, what would you say the explanation is if someone asked you that question?

SCHWARZKOPF: The industry now is run by Washington. It moved out of New York years ago. They're all trying to look like they're doing something, while not doing anything. I mean Dodd-Frank, how many years has this been trying to go into effect? So this is something like, "we're being tough." So pick on the salesmen.

MANELA: I do disagree with that. The financial advisor isn't like a tech salesman. To be a financial advisor, you need to get a license, a license in a regulated business, and if the regulators want to regulate their industry they have the right to do it. I wouldn't compare it to someone who's in tech sales or selling vacuum cleaners.

WILLIS: I think the whole thing's an outrage. It's symptomatic of our over-regulation, which almost always misses the mark in this country. I don't think the people involved in this know what they're doing, and the devil's going to be in the details. What's the disclosure going to say to the client? How do you explain that? I sit down with advisors that get deals proposed by managers, and frankly they don't understand the deal. I have to sit down and go through the deal piece by piece with them. How is a client who is totally unfamiliar with the topic going to read a paragraph and understand it? So we want to have sunshine and transparency, but we're just going to cloud the water more.

Furthermore, I think this is a total villainization of the industry. It says that these were bad people—look at the big check they took. They used to do this under the table, now we're exposing it because they're bad people. It's awful. And it casts a negative pall on the industry. But when request for comments went out, everyone said something positive. If you're a firm, how can you vote against transparency? They said 'Yeah, we all love this.' No they don't. No one wants to do this. There's not a single firm or broker that has any interest in this happening because it's going to be fumbled. It's going to be a mess because the government's involved. Now we've got the DMV running your transition packages.

OWS: This rule puts a band-aid on a much bigger problem, which is that most clients have no idea how their advisors are actually making money. Why doesn't the government mandate a broader conversation to explain how advisors are compensated overall, instead of this sort of mandatory revelation that advisors will be forced to make only when a big deal happens?

DIAMOND: I think that maybe that'll happen someday. But one of the reasons they're choosing advisor comp and transition payments, if they make a move, is because the numbers are sexy and big. The regulators are looking for a victory, where they can say, "look at this guy. He must be bad because he was paid five million dollars to make a move. He can't be acting in your best interests because a check that big would mean he's a bad guy, and he's only moving for his own benefit."

SARCH: I'm not here defending the regulators, but how can we not understand how there's a distrust of an industry that, for years, has hidden how much they actually make and how they do business? We had the Swiss banking scandal, and we had, recently, the mortgage scandal that's still being played out. Bank of America is in the paper today paying yet another fine for what they've done, and we haven't even touched upon J.P. Morgan's stuff. This industry has done really well by playing in the gray areas. I think the regulators go overboard, but they have a right to be suspicious.

WITHER THE WOMEN

OWS: Why are the firms having such a hard time getting their percent of women and minority advisors up?

PETERSON: I have wondered for years why women don't come into the brokerage industry. I've always felt that women kind of shied away from a direct sales environment and maybe they were afraid of the financial advisor role. It's too bad, because we really do need female advisors.

DIAMOND: I actually think that as the industry has evolved and advisors have become more relationship-based consultative money managers, as opposed to sellers of stocks and bonds, this is an incredibly wonderful position that is so well suited for a woman. And speaking as a woman—women are natural relationship geniuses. Also, this is a career that can offer a lot of flexibility. I mean as long as you're growing, clean, compliant and doing right by your clients, and there isn't a mandate on check in at 9:00 and leave by 5:00, and you know most advisors—most quality advisors—spend a lot of time out of the office. The job of branch manager is different because you are required to move around, and that would hardly be well suited for a women who's young and raising a family, or something of the sort. I think the problem comes down to the fact that in order to get to be a senior leader in a firm, you have to work your way up from advisor to branch manager to regional to senior leadership. There aren't enough women in senior leadership positions at the firms, and it's a problem for all firms. Every firm, high quality or not, large or small, has a mandate and would love to recruit more women. It's an industry problem; it's not an individual firm problem, for sure.

MCCOURT: Maybe it goes back to these training programs that don't really work and a lot of people fall out. But we have to figure out something different, because otherwise women and minorities, or whomever, go into these programs and there's a 90% chance they're going to fail out.

MANELA: I want to just stand up for these organizations a little bit here. It is my perception that these firms are doing everything in their power to create an environment to attract women and minorities, to the point where I think it's starting to become extreme. I can't imagine that there's any stone that they haven't overturned to try to deliver on that.

DIAMOND: I think that they've done a ton to change their culture to be hospitable to women, to create networking groups or best practice groups. I work with a lot of women advisors, and these women are spectacular. They're incredibly happy. They're doing incredibly well. They outperform, in a lot of cases, their male counterparts, and the things that make them unhappy about their firms are not because they don't feel welcome as a woman. They are the same things that make their male counterparts unhappy—it's too bureaucratic or whatever.

WILLIS: But let's not forget what we talked about earlier; we're not training anybody. There are no new people coming into the business. How can you move the numbers unless you have a hoard of new people joining?

RECRUITERS' CONVENTIONAL WISDOM ON MORGAN STANLEY

DIAMOND: New technology, the hiring that they've done and the infrastructure they've built out will really make them a very, very strong competitor this year.

SARCH: I think they're still suffering. People are still voting with their feet.

MANELA: Culturally speaking, they offer a unique value proposition to advisors who are entrepreneurial. It's a great place to go and they've got pretty good people in leadership right now.

SCHWARZKOPF: There's a lot of Morgan Stanley brokers out there looking right now.

PETERSON: The biggest threat that they face right now is their aging population of brokers. The Smith Barney brokers were pretty advanced in age before that merger.

WILLIS: They have a lot of unhappy managers who've had their compensation taken apart.

RECRUITERS' CONVENTIONAL WISDOM ON WELLS FARGO

KING: They're concentrating more on the mass affluent people; they have that group to themselves. They haven't set up any kind of a platform for the really high net worth brokers, which is odd.

WILLIS: We like all the channels. We like the choices they offer. The RIA channel is developing, so any way you want to go, they have it there—and I think it's smart.

SCHWARZKOPF: Danny Ludeman will be missed. It's another one of those firms where the bank definitely has taken over control, like Merrill.

DIAMOND: Danny Ludeman has always been seen as an advisors' leader. There are some questions about Mary Mack coming in.

PETERSON: If advisors start to see any cross-product shifting from the bank to the brokerage channel, it'll hurt Mary Mack a lot. She's got a lot to prove.

RECRUITERS' CONVENTIONAL WISDOM ON MERRILL LYNCH

KING: Merrill was always the most innovative of all the firms. I don't have the sense that's going to happen anymore.

PETERSON: The only thing that's keeping a lot of Merrill brokers in place is that retention package, and it comes off this year.

SARCH: I think they're very vulnerable. When a Merrill advisor calls me back on the phone, the caller I.D. says Bank of America now, it doesn't say Merrill Lynch.

MANELA: I think we'll see a consistent bleed over there.

WASSERMAN: They're doing a better job at training new advisors than any of their competitors.

DIAMOND: Bank of America owns Merrill, and it's Bank of America that makes the decisions. A lot of those decisions don't feel broker-centric.

RECRUITERS' CONVENTIONAL WISDOM ON UBS

MCCOURT: Their high net worth client strategy has really worked, and they've really hired some tremendous brokers this year.

KING: They're one of the best turnaround stories I've seen in years.

PETERSON: Their deals are strong. I think the firm is terrific.

DIAMOND: UBS probably wins the award for the greatest turnaround story in terms of advisor sentiment.

MANELA: They played the cards that they were dealt very well. They played this boutique, high-end story, and the advisors who were there bought into it. The wind has stopped blowing against them.

WILLIS: No one can dispute the turnaround's been great. The question is where do they go from here? Can they go from good to great?