Growing Up

AS FIRMS EXPAND, HOW SHOULD THEIR ORGANIZATIONAL STRUCTURES EVOLVE?

By Ed McCarthy

The private wealth management business continues to grow rapidly. According to *Financial Advisor* magazine's 2014 RIA (registered investment advisor) survey of 529 firms, total asset growth was up 20% in 2013, following 19% growth the previous year. The number of firms managing more than $1 billion swelled from 143 in 2012 to 170 by year-end 2013, making that group the largest in the survey.

KEY POINTS

Independent RIA firms continue to add assets, and the number of firms managing over $1 billion continues to increase.

Most RIAs' managers simultaneously advise clients and manage the business, but the ranks of dedicated managers are growing.

Some firms require that dedicated managers have wealth management industry experience; other firms are hiring from outside the industry.

Successful firms are using a range of organizational structures and career paths to maintain their growth.

Growth brings new challenges, especially for founders who handle multiple roles. This cohort often works directly with clients, brings in new business, and oversees day-to-day management. As assets under management (AUM) and the number of employees grow, the juggling act becomes more difficult and founders frequently consider reorganizing the firm. "What we find is that advisory firms' transformations are often based on the number of people in their business," says Mark Tibergien, CEO and managing director with Pershing LLC in Jersey City, New Jersey. "When you are under 15 people, I would say that typically the adviser or the founder is still very much involved in client activity," he says. "They hit a wall at 5 people, they hit a wall again at 15 people, they hit a wall again at 30 and then again at 50. What I mean by that is their span of control and the nature of the responsibilities seem to change at different levels of growth."

Refocusing a growing wealth management firm involves more than simply shifting around the organizational chart. Founders are often skeptical and detail oriented; they started their firms to retain control and hesitate to loosen up on the reins. "Delegating responsibility and holding other people accountable is more challenging than actually just doing it themselves," observes Rob Francais, CEO of Aspiriant in Los Angeles. "That piece of the evolution is hard from an organizational perspective."

SEPARATE ROLES?

At some point a founder must decide whether to work primarily as a client adviser or a business manager, or attempt to serve in both capacities. Peggy Ruhlin, CEO of Budros, Ruhlin & Roe, Inc. in Columbus, Ohio, faced this decision 13 years ago when she and her two partners realized they needed a full-time business manager. Her partners were unwilling to hire an outsider who lacked wealth management experience and appealed to Ruhlin to take the job. She declined at first and then reluctantly agreed to try it for two years, with the written agreement that she could return to client service if the new arrangement didn't work out.

The roles can be separated in reverse as well. Advisers can transition out of management and back to working with clients full-time. The four co-founders of Westport, Connecticut–based LLBH Private Wealth Management LLC left Merrill Lynch and launched their firm in October 2008 with roughly $450 million of AUM. They initially shared the business management roles but decided to scale back on those duties by hiring a professional manager as AUM approached $1 billion. In 2013, they hired Jeff Fuhrman as chief operating officer and chief financial officer. His arrival has allowed the original partners to spend less time on management and more time with clients, according to founding partner Jim Pratt-Heaney.

Other advisers argue in favor of combining the business management and client service roles. Peter Mallouk purchased Leawood, Kansas–based Creative Planning, Inc. in 2004. At the time, the company managed $30 million; the firm and its affiliates have grown to include a staff of about 180 and $11 billion of AUM. Mallouk believes that a core reason for the company's success is that its managers, including him, genuinely understand the business as a result of working directly with clients. Those ongoing client-advisory relationships are vital, he maintains, because they give him and his management team direct insight into clients' concerns. Removing himself completely from client service would cut off a key source of business intelligence. "Otherwise," he says, "I'm going to get it all secondhand or reading it in magazines or talking to people, and to me, I'm going to spend just as much time doing that and it's not going to be as valid."

Most advisers seem to share Mallouk's opinion. According to a December 2013 Financial Planning Association survey, "The Future of Practice Management," non-advisory management roles are rare. Only 13% of respondents said their firm's chief operating officer was a dedicated (i.e., non-adviser) manager; the response for chief financial officers was 12%. The results were not broken out by firm size.

EXPERIENCE REQUIRED?

Mallouk believes that wealth management firms' leaders must have industry experience to be successful. Others disagree. Tibergien notes that advisory firms have become large, complex entities. The discipline of managing a business is very different from the discipline of managing a client relationship or giving personal and financial advice. Managing is a special and unique capability, and having intimate knowledge of what it takes to advise a client is not a critical skill set for a business manager. In his experience as a consultant to RIAs, Tibergien has found that most financial advisers have limited business management experience, are not naturally equipped to perform that job, and do not enjoy the role. "Having the ability to understand how a service business works, how a closely held business works, and how a growth business works are far more important," he says.

Fuhrman is an example of a full-time manager who lacked prior wealth management industry experience. He believes that being a newcomer to the industry gives him a fresh perspective that benefits the firm. He sees himself as unencumbered by legacy relationships and legacy thinking and believes he can approach the business as a client might. His lack of experience wasn't a negative factor in the hiring decision, according to Pratt-Heaney. The founding partners wanted someone who could take over management duties so they could concentrate on clients' needs; they didn't want another wealth manager. "We don't need anybody in the space to tell us how to manage money or how to get clients or how to service clients. We do that extremely well," says Pratt-Heaney. "What we wanted to do was just have it more professionally managed."

Steve Janowski worked as a consultant in other industries before becoming chief operating officer of Wetherby Asset Management in San Francisco in 2005. At that time, the firm had slightly under US$1 billion in AUM. Today, it has $3.65 billion in AUM and another $4 billion under advisement. The organization has an office on each US coast, with about 500 clients and 57 employees. He agrees that full-time managers must remain focused on clients' needs as well as the business, but he believes that the right organizational structure can facilitate both objectives.

Wetherby has three client-service teams, each headed by a senior wealth manager who carries a full client load and is also a shareholder in the firm. When Janowski meets with the firm's senior wealth managers, he doesn't tell them how to take care of the clients because he is a step removed. He sees his role instead as asking the right questions to ensure that clients are being taken care of. "Yes, it's important to have your finger on the pulse of the client, and yes, it's important to listen to the people and work with the people that do have their fingers on the pulse of the client," he says. "But does it need to be me? You know, I would say no, and I think the last nine years have probably proven that this model works pretty well."

KEEP GOING

"Expanding Horizons," *CFA Institute Magazine* (May/June 2014) [www.cfapubs.org]

"The Big Lie of Strategic Planning," summarized in *CFA Digest* (April 2014) [www.cfapubs.org]

"The Future of Wealth Management," *CFA Institute Conference Proceedings Quarterly* (January 2014) [www.cfapubs.org]

STRUCTURES AND PATHS

The different approaches indicate that independent private wealth management firms can succeed with a range of organizational models. Wetherby has five functional areas: client service (which includes the wealth management teams), research, operations, administration, and business development. Other firms have similar structures, according to several sources contacted for this article.

A different model can be found at Budros, Ruhlin & Roe, where the major shareholders do not have any direct client responsibility. They serve instead as in-house experts for the firm's six client-service teams. One shareholder has extensive tax- and estate-planning experience. Another serves as chief investment officer, and a third helps clients set and prioritize goals. Each shareholder is expected to be a subject-matter expert in his field. "We're counting on them to make sure that they are always up to date in what's happening in their particular area that they have responsibility for," says Ruhlin.

Organizational structure also has implications for employee career paths, although the options are naturally limited by size. At LLBH, the clearest path is on the client side of the business, according to Fuhrman. Entry-level hires progress from client-service associate to support adviser and then to associate adviser and ultimately to lead adviser.

Wetherby provides career paths in all its areas. New employees often start in an entry-level client-service role because that area has the largest department. After two years or so learning the business's basics, some employees will continue in client services and others may decide to focus on more analytic investment work in the research area. "Most of them will go on into the client-service track," he explains. "They'll spend a couple of years as an associate, a couple of years as a senior associate, and ultimately move toward being a wealth manager. On the research side, we do have people that maybe started as a client-ops person; ultimately, they become a research analyst, then a senior research analyst, and given an opportunity or a need in the business, possibly a director of research. [It's the] same thing on the administrative side."

EVOLVING BEST PRACTICES

Given the lack of a widely accepted best-practices structure, Janowski advises that the choice of an organizational model should be driven by how the firm wishes to service clients, not vice versa. Even then, he cautions, don't underestimate the time needed to manage the firm and be willing to adapt over time as needed.

Ed McCarthy is a freelance financial writer in Pascoag, Rhode Island.