

# THE EMERGENCE OF THE 'HYBRID' RIA MODEL

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The wealth management industry is evolving – clients are becoming more sophisticated, have complex demands, desire transparency, as well as holistic wealth and investment advice. This has led to the rise of the 'independent' advisor industry and in turn the RIA (registered investment advisor) channel, where entrepreneurial advisors are looking to make this shift to a fee-based independent model in order to gain more autonomy, access to a broader spectrum of investment products and wealth services, and provide a transparent compensation structure.

Along with every benefit comes associated challenges. While advisors appreciate greater control and flexibility, this also entails taking on additional responsibility, including increased regulatory scrutiny, compliance oversight, additional resource costs as well as administrative tasks associated with managing your own business. Additionally, clients are demanding more 'solutions' (to meet their unique situation) over 'products' (to beat a market benchmark), and this is forcing advisors to go above and beyond in meeting client needs and requirements. All these factors are causing advisors to gravitate towards a 'hybrid' model, which helps them meet the complex needs of their clients, who are demanding more comprehensive solutions along with more transparency and trust by running a fee-based business for their overall portfolio.

## WHAT IS THE 'HYBRID' MODEL?

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Hybrid RIAs are dual-registered RIAs that offer a unique opportunity for advisors to operate both a fee and commission-based business concurrently. Advisors typically conduct the advisory portion of their business through the independent RIA and the brokerage portion of their business through an affiliated broker-dealer. The latter provides advisors with a technology platform, product shelf, operations, and back-office support in an a la carte selection process, to conduct the brokerage part of their business. The hybrid approach is truly a win-win for advisors that want to operate both a fee as well as commission-based business, but wish to maintain their overall independence without being tied to a single provider/platform. Additionally, the new segment of wealth clients requires a high degree of personalization and customization. The hybrid

model helps the advisor be better suited to provide such unique advice on all aspects of the clients' financial situation and provides the ability to offer solutions beyond just investments.

Hybrid firms typically tend to attract more affluent clients (requiring holistic solutions) and generally generate more revenue than fee-only advisors (since they also earn a share of the brokerage revenue from the affiliated broker-dealer, along with advisory revenue through the independent RIA). These factors have helped make the hybrid RIA segment the fastest-growing advisor segment of the independent market.

# WHAT IS THE 'HYBRID' MODEL? CONTINUED

Share of advisor headcount in the market has **MORE THAN DOUBLED** in the **LAST FIVE YEARS**<sup>1</sup>

**HYBRID RIAs** are the **FASTEST-GROWING ADVISOR SEGMENT** of the independent market.<sup>2</sup>

Almost **30 PERCENT** are break-away from wirehouses and nearly **25 PERCENT** from IBDs.<sup>3</sup>

More than **ONE-THIRD** of all RIAs are 'hybrid.'<sup>4</sup>

“The RIA and dually registered advisor channels are the only ones that had a positive annual growth rate in advisor numbers over the last five years. The growth is mostly from attracting advisors out of other channels.”

CERULLI ASSOCIATES<sup>5</sup>

One key consideration with this model is that the advisor is subject to a dual compliance structure; the investment and compliance restrictions associated with being an employee/independent contractor of the affiliate broker-dealer as well as the additional burden of being a 'business owner' and having to complete all the administrative tasks as well as due diligence for products, platforms and outsourced vendors for the RIA that they own. Moreover, the advisor now comes under the scrutiny of FINRA (Financial Industry Regulatory Authority) as well as the SEC (Securities and Exchange Commission), given that they are offering both advisory and brokerage services to their clients.



## BRAND & MARKETING

- The RIA will have a distinctive brand
- Advisors will have complete autonomy and flexibility to brand and market the RIA as they want



## RISK & SUPERVISION

- The advisor will be responsible and accountable for all the risk, compliance and supervision aspects of the RIA
- The advisor will be subject to the standards and best practices of the affiliate broker-dealer for the brokerage part of their business



## PLATFORM AND TECH

- The advisor will be responsible and accountable for providing all tools, platforms and technologies from both client and trading perspective for the RIA. They will also need to conduct the required due diligence for all platforms as well as any outsourced vendors in their network
- For the brokerage part of their business, the advisor will be restricted to the platforms and systems provided by the affiliate broker-dealer



## PRODUCTS AND SERVICES

- The advisor can provide a wide variety of investment products and wealth services as per client needs, through various providers and custodians from their network. They will also need to conduct the required due diligence for all products and vendors they work with
- For the brokerage part of their business, the advisor will be restricted to the products and services offered by the affiliate broker-dealer



## PRICING AND COMPENSATION

- The advisor will earn a share of the brokerage revenue from the affiliated broker-dealer along with (potentially 100 percent of) the advisory revenue earned through the RIA business



## OPERATIONS AND HR

- The advisor will be responsible and accountable for all administrative, operational and resource costs and planning for the RIA business
- For the brokerage part of the business, the advisor will be expected to follow the policies & procedures of the affiliate broker-dealer they deal with



# IS THIS THE ONLY APPROACH?

Another popular hybrid approach that advisors can take if they want to lower their administrative and overhead burdens is the corporate RIA. While breaking away has numerous benefits and is certainly enticing and rewarding, advisors should not overlook the risk and cost associated with being wholly independent. It is vital for advisors to carefully weigh the benefits and considerations involved in making this shift to make the most informed decision for their business. Some of

the critical considerations for making this decision include: the degree of independence desired, the risk appetite they are willing to take as a business owner, access to products, services, and platforms within their network and business as well as succession planning requirements. The advisors that fall at the lower end of this consideration scale may opt for the corporate RIA model, which may be better suited for their profile, personality and risk appetite in the long term.

## WHAT IS A CORPORATE RIA?

A corporate RIA is a legal entity (typically of a large wirehouse or traditional broker-dealer) that allows investment advisor representatives (IARs) to also operate a fee-based business through the firm's corporate umbrella, under one single brand. The corporate RIA functions like a subsidiary of the existing corporation; this differs from an independent RIA which is a standalone business under its own unique branding. Advisors tend to give up some level of autonomy if they are a part of a corporate RIA since they are recruited like employees of the firm and have to follow the firm's best practices, while also being restricted to

the products and services they offer, including choosing the custodian that the corporate firm deals with. This is a win-win for corporations that would prefer for advisors to continue holding assets with them, and also for advisors that are looking to break-away but want to avoid the administrative tasks and overhead associated with being business owners. The additional benefit for advisors to consider this option is to avoid the hassle of completing the initial filing requirements with the SEC and state since the parent company would usually take care of all the licensing and legal and regulatory requirements.



### BRAND & MARKETING

- IARs will operate both a fee and commission-based business through the parent firm's corporate umbrella, under one common brand
- The parent firm will be responsible for all branding and marketing related costs and planning



### RISK & SUPERVISION

- The burden of risk, supervision and compliance is taken over by the parent company, and advisors are subject to the best practices and standards of the parent firm
- All the licensing and regulatory requirements will be taken care of by the parent firm



### PLATFORM AND TECH

- IARs would be employees of the Corporate RIA within the parent firm and thus have access to the parent company's technologies and platforms
- They will also receive complete and comprehensive support with compliance, technology, research and reporting



### PRODUCTS AND SERVICES

- IAR's will have access to the parent company's product shelf, operations and back office support. They can provide their clients with a variety of investment products, managed accounts as well as sophisticated packaged products on either commission or fee basis; and will also receive complete and comprehensive support with compliance, technology, research and reporting



### PRICING AND COMPENSATION

- The advisor will earn a percentage of both their brokerage and fee-based business, as per the parent firm's pricing and compensation guidelines



### OPERATIONS AND HR

- The advisor will follow the policies and procedures of the parent firm, and will receive all administrative support including administrative tasks, operational support and comprehensive back office support



# DRIVERS & BENEFITS OF THE CORPORATE RIA MODEL

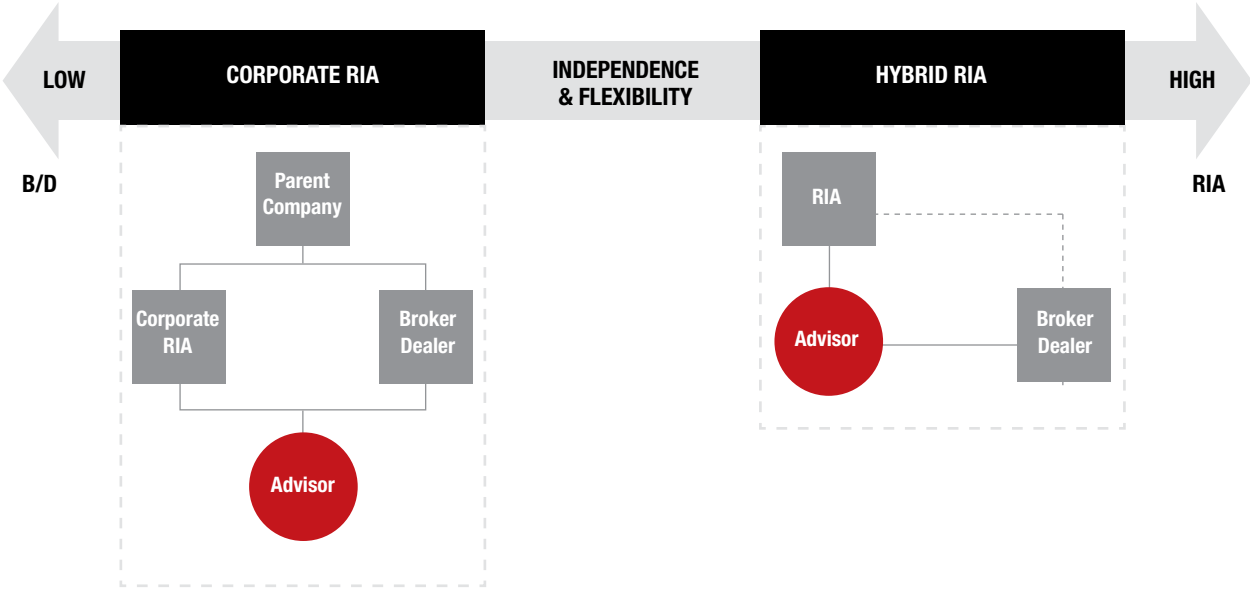
One of the biggest drivers behind advisors moving to this model is the ease of compliance oversight. The burden of risk, supervision, and compliance is taken over by the parent company, which frees up a lot of time for advisors to focus on prospecting, sales, and actual advisory activities. Additionally, if the parent company already has an existing

brand value in the market, it may be beneficial for advisors to operate under the same name which provides a certain level of legitimacy and merit, versus going the independent route and start building their business and branding from scratch.

# PRODUCT AND PLATFORM OFFERINGS

IARs would be employees of the corporate RIA within the firm and thus have access to the parent company's technology platform, product shelf, operations and back-office support. They can provide their clients with a variety of investment products, managed accounts as well as sophisticated packaged products on either commission or fee basis, and they will also receive complete and comprehensive support with compliance, technology, research and reporting.

## OPERATING MODEL <sup>6</sup>



# IS ONE MODEL BETTER THAN THE OTHER?

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The hybrid RIA model certainly provides more independence and freedom and helps advisors earn a higher revenue (potentially 100 percent of their advisory fee). However, as a business owner, advisors also tend to spend a lot of time on administrative tasks and overhead, including operational support, resource planning, compliance with regulatory requirements, as well as following a dual compliance structure managed by the broker-dealer and the RIA. The corporate RIA model, on the other hand, allows advisors to focus their time on prospecting and purely advisory related activities since all the policies, procedures, back-office support and licensing and regulatory requirements are taken care of by the parent firm. However, this comes at the cost of being restricted to the parent firm's product shelf as well as earning lower revenue; since advisors only make a percentage of the fee they charge, depending on the compensation structure of the parent company.

In order to decide between the hybrid or the corporate approach, advisors need to keep in mind the drivers for choosing one over the other. Both models have had proven success, and one model is not inherently better than the other. This decision is primarily based on the advisor profile and preference; of one who is confident of running a fee-based business, but has to decide whether he/she is ready to be a business owner or would rather continue with the overall support and guidance of an already established corporate. It is a decision of several factors, most of which include the advisor's skill set, personality, type of clientele and size of external network.

## AUTHORS:

**Phillip Kerkel**, Managing Principal

**Anushka Nadkarni**, Senior Consultant

## CONTRIBUTORS:

**Nicholas Bamberger**, Consultant

**Kyle Shoop**, Consultant

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