Contemplating a Change: Should You Go? How Do You Choose?

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Deciding to go independent, by joining a registered broker-dealer or starting your own firm, is a weighty decision. The factors that have helped someone be successful in a large organization oftentimes do not translate into the skills needed to run an independent business.

To help you understand the issues faced by advisors looking to go independent—what works, and more importantly, what does not—take a look at Aaron, who decided to go independent in February 2008.

Aaron knew from the start he would leave his employer one day, so he was very careful not to sign any non-compete or non-solicitation agreement when he joined. This is the first big hurdle for many people who go on their own—understanding the legal "handcuffs" that prevent them from actively soliciting their existing clients. In Aaron's case he had not signed any agreement, but to be "safe," he did not take any client files or any property that could be considered the company's when he left. Instead, Aaron asked his clients to send their personal contact information to his home email address and his personal cell phone. In all likelihood, his existing employer quickly "seized" all information on company property—including his laptop and cell phone. In addition, he provided his clients with a copy of their accounts, including all holdings, so that they would be in possession of the information he needed when he left.

Aaron considered both joining an independent broker-dealer and setting up his own registered investment advisory (RIA) firm and decided to go the independent broker-dealer route. In making his decision, Aaron had to weigh a number of factors.

Going completely independent into a new RIA firm meant doing virtually everything on his own. Aligning with a large broker-dealer offered a number of "built-in" support mechanisms and the people internal to that firm who could guide decisions and provide support. He knew that many independent broker-dealers have a great system in place to provide the operational support on the back end he would need.

Next Aaron had to consider what kind of investing style or approach is being used? In Aaron's case he really wanted access to a platform of investment options and analysis. A person moving to their own RIA could be more focused on practicing their own investing style and doing their own research, but Aaron wanted to align with a firm where he could access built-in options and research. Making sure the approach was consistent with what he had been doing for his clients was key, though, and he did a lot of research to determine which broker-dealer offered him the best fit.

Compensation was clearly a driver for Aaron. In the independent RIA model, he would have counted in client assets and the commensurate fees for his sole income. Setting up an independent RIA requires a "cash cushion" while things get up and running. Of course, all fees that eventually come in belong to the owner of the RIA, but not knowing which clients would come and which would stay made planning a bit difficult. In this regard a key concern for Aaron was the fee-only structure of becoming an RIA. Aaron was more comfortable with the accelerated payouts offered from his broker-dealer in anticipation of the assets he would eventually be able to move and the ability to maintain a number of commissions from existing clients.

Lastly, in Aaron's case he felt he really needed the background and support of a firm with knowledge about compliance and legal issues. Going on his own would have required getting a lawyer and becoming quickly acclimated to all of the compliance issues he would face, but the broker-dealer was willing to provide information, access, and support. The opportunity to work with a firm that had done all of this with so many investment professionals before was very important to him.

By aligning with a broker-dealer, Aaron gained the freedom and independence he always wanted, even though he sacrificed a portion of his overall fee to gain access to a transition team, operations and compliance support, and investment products. Which business model works best depends on the advisor, the need for infrastructure, and the ability to sustain the business. Ultimately the decision is a tradeoff between a need for support and a desire for total freedom, and depends on where the advisor sits in that equation.