Transcription details:

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| Host: | Bill Coppel, First Clearing Chief Client Growth Officer |
| Guest: | Carolyn Armitage, ECHELON Managing Director |

Transcription results:

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| Intro | Welcome to the Next Frontier where we examine what the role of the financial advisor will be in a world that's being disrupted by artificial intelligence and algorithms. Our mission is to spark new conversations that create stronger connections and build greater client confidence. Join us as we look at our industry and others through a new lens and explore the opportunities emerging at the intersection of high tech and high touch. It's time for a new conversation. Are you ready? |
| BILL COPPEL | Hi, this is Bill Coppel and welcome to the Next Frontier. I'm always looking for opportunities to learn what I can from the advisors and business owners I meet along the way. About a month ago, I was speaking to a group of about 35 successful advisors. And whenever I'm in front of a group I like to ask three questions. The first one is, "How many of you have a financial advisor?" Well, as you can imagine, not a hand went up in the audience. The second question I ask is, "How many of you lead with planning?" Well, there was an overwhelming positive response because perhaps planning is really at the heart of what we do. And finally, third, I ask, "If I were to come to your house tomorrow or your office, how many of you could actually pull out and show me your plan?" It rings a bit of the old cliche the cobbler's children have no shoes. And then I read an article recently that suggested our industry is facing a succession crisis. Translation, we as advisors don't think seriously about tomorrow. And that's odd as this is at the heart of planning. So it got me thinking who advises advisors? We spend so much time focused on preparing clients for life transitions. But clearly, we still do so little to help ourselves prepare. I invited our guest today to help us explore this succession crisis. |
| BILL COPPEL | Carolyn Armitage is a managing director of ECHELON Partners. She is an industry veteran with more than 30 years of experience providing valuations, management consulting, and investment banking services to CEOs and firms and extends a strategic and holistic approach to each engagement. Carolyn is a frequent keynote speaker for corporate clients and industry events and is quoted extensively as a leading authority in the private wealth management by industry publications. Financial Planning recently named her number 8 on a list of 19 people who will change wealth management in 2019. She holds numerous FINRA licenses and is CFP and CIMA certified. In addition to growing numerous financial organization, Carolyn founded and runs the public nonprofit True Circle Organization helping feed, clothe, and improve the lives of homeless people throughout Southern California. She holds a Bachelors of Science in Business Administration from the University of Minnesota and a Masters in Management from American College of Pennsylvania. Carolyn, welcome to the Next Frontier. |
| CAROLYN ARMITAGE | Thank you, Bill. Glad to be here. |
| BILL COPPEL | We've talked about a few types of disruption to our industry over the course of this podcast. And I think we're all aware of the importance of succession from a business owner's perspective. But we haven't really spent any time looking at what we call this succession crisis. Could you tell us some of what you're seeing from where you sit as it relates to this topic? |

CAROLYN ARMITAGE Thank you, Bill. I would love to share a few things here. We seem to be at a perfect simultaneous event going on in society with clients maturing and needing financial planning more than ever before, especially the baby boomers as they're in their peak earning years. And they're being sandwiched between their parents needing elder care and their children needing assistance as they become young adults and through those college years. And at that same time as consumer demand has increased, the advisors in our industry, the number of them are decreasing. And they are too, of course, aging. And so you've got this interesting scenario where the consumer demand is increasing and the number of advisors are decreasing. Fortunately, technology has come in to help advisors be more efficient with their business. At the same time, we've got a terrific market cycle that we're in right now, the business cycle. So there's a lot of advisors who have built up a business over the last 30 to 40 years. They were the original founder, entrepreneur of their own financial planning firm. And they're wanting to take advantage of this terrific market cycle and the fact that their businesses are more profitable than they ever have been. And so it's creating a terrific succession planning opportunity. We've got increased liquidity in the marketplace. We've got outside investors looking to invest into our industry. And it's really a tremendous opportunity if you are a senior financial advisor looking at what comes next. There really couldn't be a better time for you to consider what your transaction and transition's going to look like.

BILL COPPEL So my question to you then is - obviously, it's an opportune time based on all the information you just provided, market conditions, the maturity of these practices, to consider this - are they lining up at your door for help?

CAROLYN ARMITAGE No. They're not. And it's for a variety of reasons. The one that we hear most often-- it's often unspoken. It's more that procrastination that you hear in advisors' voices as you talk about it. It's that "Uh, yeah, I've been meaning to do that." When you've built up your business and it's so personal because you've put in not only financial equity but the sweat equity over the years and you serve your clients, it's hard to imagine that anybody else in our industry could serve your clients with the same care that advisors do today. All of the clients that I work with, their number one objective is to find that perfect fit of someone who could take care of their clients as well as they do if not better. And that feels almost like an impossibility because our own sense of self-worth.

BILL COPPEL Yeah. But I think you've hit on something very interesting, Carolyn. I was just recently chatting with Dr. Michelle Pannor Silver who is a professor at University of Toronto and has written a wonderful book. The title of it is Retirement Discontent. And one of the takeaways from that research that she did was around this notion of in professions like the one we're talking about today - being a financial advisor or being a physician or being a lawyer - so much of your identity is wrapped up in what you've done for so long. In the conversations that you're having with advisors, are you beginning to detect that it's not so much-- it's certainly they're concerned about making sure their clients are cared for, but what's next for them?

CAROLYN ARMITAGE Absolutely. That's the other aspect of a psychological transition that advisors need to make with their businesses. It's not just caring for their clients and their employees and what that legacy is, but, "What do I do next?" And so one of the misperceptions that advisors think of is that "If I do my succession plan, if I document and actually create one, I'm putting myself out of work. Yes, I may sell my business. I may get a terrific lump sum of money or payments over a few years. I may be able to transition internally to a great team that I have. But what will I do next?" And there's a lot of times where the advisor may sell either a portion or all of their firm. And they continue to work with the firm for as long as they're comfortable with. What they get

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| | to do instead of running everything is they get to select the areas where they really enjoy the work and offload the rest. So for example, if they are terrific at business development or client servicing, they can sell a portion or all of their firm or transition that to somebody internally and continue to work and build up new clients as they are playing golf, as they're yachting, as they're doing wine tasting. And so they can really do the things that they love to do and continue to build their business and stay involved, stay active in the community, give back to the financial planning industry. And so it's really the best of both worlds. |
| BILL COPPEL | So it's really not an all or nothing proposition if I hear you correctly. What I hear you saying-- |
| CAROLYN ARMITAGE | Exactly. It's a continuum of options. |
| BILL COPPEL | So to start, this process begins with sort of that emotional reflection, if you will. It doesn't mean it's the end. It really could be simply the beginning of the next chapter as an example. And at the top of our conversation, I mentioned the fact that when I was out speaking recently to a group of advisors and asked them if they had an advisor and the answer was well, they didn't, which I found rather interesting as I mentioned. Here's a wonderful opportunity, perhaps, to begin thinking about this by reflecting with an advisor of sorts who can help the individual business owner begin that process of identifying what's next, which could be built right into the plan if I hear you correctly. |
| CAROLYN ARMITAGE | Yes, exactly. Just as in when a prospect comes to a wealth management firm, ideally that client would come in five years before they're ready to retire so that there may be certain aspects of how they're saving or where they're saving that can be tweaked and refined that will help enhance their retirement plan. We love to start working with advisors five years out before they're ready to retire. Sometimes there are certain aspects of their business that we can help improve upon. We can help them with their financial preparedness and what key performance indicators, or KPIs, that they're tracking or how to refine some of their business offering to help improve their transition down the road. Another element along those lines is oftentimes when people think about this transitioning, they think about, "I need to transfer my equity to somebody." And they kind of forget the other elements. Certainly, you want somebody to take good care of your clients and that's a relationship. But also the governance of the firm is an important element that often gets overlooked if the advisor's trying to go it alone. Does that make sense? |
| BILL COPPEL | Yeah. It makes complete sense. And what's interesting to me is when you start to break it down into these sort of bite-size pieces, it again goes back to as important as it is for all of us to have a plan, a life plan if you will, obviously it takes into account what we do professionally and how we have secured our future relative to how we've invested and managed our resources around that. But also what you're pointing to is that this advisor can help the individual begin to shape their identity, which we spoke about a few moments ago. In your work in the advice-- the counseling you've been providing practices like this, how much time do you spend on that identity piece? |
| CAROLYN ARMITAGE | Oh, that's a great question, Bill. And that's where, oftentimes, people think of M&A as really the economics of a deal. And quite frankly, the economics are much simpler than the emotional aspects of selling your firm. And so while we certainly have terrific financial models and do all the analysis - we are highly networked where we can find the right buyer for your firm or the right strategic partner, the right merger partner - it's helping advisors go through that transition process of acceptance and embracing their next phase in life. And so we provide that turnkey approach of the economic package as well as the emotional aspect. |

BILL COPPEL

All right. So let's do a little role play here for a moment. I'm a financial advisor. I've been in business now for 35 years. I'm in my late 50s and I'm going as hard as I did when I was 35. But I realize and recognize that I probably need to figure out what I'm going to do next. Maybe I had a crisis in my family or some other shock that has made me step back and think. Maybe the advisor in the next office down suffered a heart attack and died. Maybe the firm leadership is in the process of changing. Or my partners are chasing different dreams than they did when we started out together. I want to sit down with someone and have this conversation. I want you to help me think through this. Give me a sense of how you would begin to talk to me about re-identifying or reshuffling my own deck to find what that next chapter is going to be.

CAROLYN ARMITAGE

And just as in financial advisors are working with a new client that comes to their firm, we do the same type of discovery process with advisors. So we need to fully understand how they got to where they are today. How did they come to build their business? What are some of their values that have made them successful? Have they considered what their transition would look like? What have they experienced with their other partners going through the health situations and crises that you mentioned? All of these have impacted an advisor's perception of what their retirement could look like. And so we'll probe to find out what their financial readiness is as well as their mental readiness because as you know, advisors do go through a variety of events. And sometimes advisors are very financially ready to retire. But they're not emotionally ready to retire.

CAROLYN ARMITAGE

So these are those folks that are really well off but they continue to choose to work because they love what they do. And that's a really terrific position to be in unless you're also make that transition to be mentally ready to exit as well. And that's where we will usually call these folks the rich and ready. They've had a very successful career. They're financially set. And they're ready to transition on and go through other lifestyle activities and move on from the financial planning world. Sometimes advisors are not quite financially ready. And so they chose to either stay and grow the business if they're not emotionally ready or if they really want to get out, but they haven't saved as much as perhaps they could have, then that's where the financial price that they get out at can be more important than perhaps to other folks. So you really have a spectrum or a quadrant, if you will, of advisors between their emotional readiness and their financial readiness.

BILL COPPEL

That's very interesting because they're mutually exclusive or tied at the hip depending on the individual, right?

CAROLYN ARMITAGE

Mm-hmm.

BILL COPPEL

Let me direct a question to you around the rich and the ready. I love that. These are people that have been successful. My sense is they're relatively high energy. They've worked very hard. They're disciplined. They're structured. Things that are very-- they have priorities. They have purpose. You mentioned values. Those constructs are very difficult to transition away from when you've been doing it for so long. Talk to us a little bit about what you've seen here in terms of as they transition away and remain active, what are some of the roles they've played in the currency that they are now using to measure their value as opposed to simply money.

CAROLYN ARMITAGE

Many advisors are looking to find where they will add value, where that sense of identity comes from. And, of course, it's a multifaceted response based on the personalities of the advisors. Because so many of our successful advisors in the industry are these type A drivers - very successful, highly skilled, very purpose driven - I actually will see many advisors choose to create, start, or work with a nonprofit organization so that they can give back to whatever fulfills their heart's purpose. So sometimes those are a domestic organization, sometimes they're international. And that can be a driving force as to how they want their deals structured because of the economics that they're looking for in that potential part of the deal. Sometimes folks love the industry so much and it is so much a part of their identity, they want to focus on those areas that perhaps was underserved while they're a financial advisor such as financial literacy. How do we educate the youth in this country to help them understand how to budget better, how to invest as they get that first job out of college and start to save for retirement early and not expect social security to be there for them? How do we help them make smart decisions early on as opposed to overspending and running up their credit cards? Another option would be to continue on with the organization and help the next generation by mentoring them and providing guidance as to how to work with clients in a more advanced fashion.

BILL COPPEL

You know what's interesting is that as you've pointed out-- and I kind of want to emphasize this point with our listeners, is that there's two broad aspects to this succession. There's clearly the valuation or the monetary, the economic, aspect of this succession. But I think equally important, and maybe in some cases even more important, is the destination of where they're going to go. And what you're pointing out here is that that is almost as important if not more important, to have a place to go or a path to follow which begins to give you a framework in many respects, I would think, to judge the economic deal that's on the table. So many times I've seen the succession opportunities essentially stop cold or blow up over valuation. How do you talk to your clients today? Or what's the advice you'd be giving to advisors who are approaching this period of time? How should they approach this notion of valuation? What is the right frame of mind to really understand or comprehend what your life's work is worth?

CAROLYN ARMITAGE

The valuation, the math part of it, is fairly straight forward. We essentially work with the financials that the firm has and normalize those so that you can compare one firm to another. Sometimes we do have to level set or educate-- or reeducate an advisor as to what their firm is worth based on some other rules of thumb or multiples of revenue that they've heard of for a book of business. For larger businesses, of course, it's all designed around cash flow and what does that mean to another firm. And there's other times where advisors are delighted and surprised by how much their business is worth because they have been using some numbers that really undervalued what their business is worth to another entity and what that synergy value or multiple arbitrage that's created by finding the right partner.

CAROLYN ARMITAGE

But all in all, an advisor won't put together their succession plan. They may get a valuation because they're interested in the number. But they won't necessarily put together the succession plan until they have a solid vision of what their next phase looks like. And so they need to find their heart's purpose again. So as they retire, they need to renew themselves and relaunch themselves into this next phase of life as to how they want to give back. Do they want to mentor somebody in their organization? Do they want to give back to the industry and help educate, perhaps be a volunteer and work with the FPA organization or the CFP board or something like that, to help organize educational events and free financial planning or pro bono work for their communities helping to educate children make smarter financial decisions? Or do they want to have some other purpose in their life, whether it's through a church group or some other organization, that they really are passionate about participating in? Once somebody can visualize that, then they will take action.

BILL COPPEL

That's interesting because it's a bit counterintuitive if you think about it. So often I hear in conversations around this topic is, "I need to figure out what my business is worth before I put my plan together." And what you're sharing with our listeners is well, maybe not so fast. While that's an important factor and there's plenty of ways to get there, you need to figure out where you're going to go first and understand what's next, again. And I think that's a very important point. If you don't know where to go, any road will lead you there, A, as the old saying goes. But I imagine in the absence of having some direction or some destination, there must be a lot of emotional energy that goes into looking at these valuations. So if I don't know where I'm going and you hand me a number to tell me what I'm worth, I have no real gauge to determine whether that makes any sense. Am I right when I say that?

CAROLYN ARMITAGE — Yes. So let me share with you a couple of ideas. One's the notion about advisors starting with a valuation. It actually is a normal part of the process to have a valuation. But as far as discussing the succession aspects whether it's at an industry event or with peers, folks are only going to talk about the numbers or a little bit of the strategy. They often won't really open up some of the psychological aspects that they're going through as they think about transitioning. So part of that is just posturing. And, of course, it would be great to measure the value of your firm compared to somebody else's and try to see how you fit in compared to some of your peers. The valuation process is really a process that's not static. Your business can have many values. It's not just one number. As we do formal valuations for firms whether it's to support a expert witness case or for a new business joining the firm or to sell the firm, we do go through a series of questions to fully understand the firm, what the history has been for the last five years. What are some of the ups and downs? What have been your expenditures or investment into the business? Are they frivolous? Are they one time or are they ongoing?

CAROLYN ARMITAGE — All of that combined along with our proprietary database of understanding the financials wealth management and asset management firms in the industry will help us come up with a nominal valuation number for a firm. And then we'll give you a range as to plus or minus 20%. And we'll talk about the factors that can impact making that valuation higher and those that'll make it lower. But if you were to sell your firm, your firm is worth, just like any other open market, what somebody else is willing to pay for it. So if we can find you the right fit, the right firm to be your next partner, and your firm helps to get them into a new geographic market, a new niche that they haven't been in before, or perhaps it's the exact same business that they're in and so they can really have tremendous scale and efficiency with your business, that's where your business will be worth even more than that nominal value because of the synergy that they can realize by combing the two firms. And if that firm happens to be larger than your firm, the advisor who's selling will actually benefit from a multiple arbitrage because that firm would be selling at a higher multiple than they would.

BILL COPPEL — Well, that's excellent information for our listeners to absorb. This is not simply whatever we think our practice might be worth. Leveraging your skills and the database that you've built over time creates a context in which to contrast and compare, perhaps, valuations. And again, as you point out, how you proceed in terms of whether it's an acquisition or you're being acquired or being absorbed into another firm or, in fact, you are bringing a partner on as part of that process can certainly impact what that number is. If I were to be starting out right now and I called you, what are the kind of steps you would guide me through to get started on this process of succession? Or put another way, what should an advisor listening to this podcast--what are two, three, four, five things they should start to think about in the process of beginning dealing with the idea of what's next for me?

CAROLYN ARMITAGE — So I think one of the things advisors need to consider is part of what you opened with, Bill. And that is advisors need a financial advisor. I don't need to manage your money per se. But I need to be able to help you make better decisions, just as advisors do for their clients. To help take some of the emotions out of that decision-making process or help you understand what those emotions are so that advisors can make better-informed decisions. Super important takeaway for advisors to understand that M&A, or investment banking, is an exchange of unequal information. And so the more advice, the more information, the more data points that you have will help you make a more sound decision on your business. And so as financial advisors think about a succession plan, they'll think about a few different aspects. One of them is that, oftentimes, their wealth management is their largest financial asset that they own, even more than their house here in California. It's their largest financial asset. So you really don't want to screw it up. And you only get one shot to do it. And so while you can try to see if your wealth management prowess can carry over into the investment banking side of the business, oftentimes it doesn't. And while a financial advisor may be a wonderful wealth manager and help guide their clients through a financial plan, those skill sets often don't translate into being their own advisor. Otherwise, they would have already put together their financial plan, right? So having somebody to help guide them through the emotional aspects of the decision-making process will lead to better outcomes.

BILL COPPEL

And my sense is that if I were a client of an advisor and I'm aging and I'm watching my advisor age, I would be concerned as a client. And I'd probably want to ask my advisor, "So what's your plan?" And I've done that with my accountant recently. We're about the same age. And I said, "Hey, Rich, how long? When do I have to find a new accountant?" So my question around that is in your experience, this lack of preparedness on the part of the practice is really, in a sense, underserving their clients, have you seen that play out in certain circumstances?

CAROLYN ARMITAGE

Absolutely. Sometimes clients will feel comfortable enough with their advisor to ask them. More often, they sit in silence because they're just too polite to ask and they don't want to offend them. Sometimes they don't even want to know the answer if the advisor's unprepared. So they do question that and wonder and feel so much better when the advisor is proactive and says, "Just as in I'm doing your financial or retirement plan, your estate plan, as a professional organization, we have a fiduciary obligation to you as our client to make sure that you're well taken care of. If something happens to myself or one of my business partners, here's our plan for succession and continuity." The advisors need to keep something in mind. There's two different ways that you will retire. It's either going to be planned or not planned. And so if you don't plan for something, that proverbial bus still may come along. Sadly, in the decade that I've been working with advisors I've seen this happen [so?] too many times. And sometimes that can be a motivating factor for one of their colleagues to take a stance and actually put together their succession plan. But the fiduciary obligation of a financial advisor is probably one of the driving forces to help advisors get off the dime and actually put together their plan.

BILL COPPEL

It seems to me-- and I want to go back to the comment I made at the top and ask you one last question. We have a large part of our advisor population which is clearly at a point in their careers where this should be a high priority in their life. It'd being characterized in the press as a succession crisis, if you will. I think you pointed out the fact that it's obvious, yet few are moving against this challenge. To wrap it up, I want to ask you this one last question, Carolyn. If you were to leave one idea for our listeners today around this really important issue - let's focus on just getting them off the dime - what's the one thing you would share with the audience that would help them, perhaps, move forward?

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| CAROLYN ARMITAGE | So I think the one thing advisors need to really comprehend is that the sooner they get started working on their plan and documenting their plan, the more options that they will have. Just as when your clients come to a financial advisor five years out before retirement, you can do much more with them because you've got that runway to help them plan. We do the same thing with firms. If they have a partner that's looking to retire in five years, we can start working on the plan and making some adjustments to their organization in that first year we start working with them. Thinking about who advisors can turn to for confidentiality and advice, if you're a owner or founder of a wealth management firm it can be pretty lonely. If you're a single partner in a firm or 100% equity owner in your firm, you don't necessarily have someone that you can turn to to help guide you and give you that professional business advice or second opinion. And that's where firms like ours can really help be that structured guidance that a financial advisor needs to successfully put together their own retirement plan and determine what's next. |
| BILL COPPEL | Well, that sounds like sounds advice to me. And so I guess the message to all of our listeners is today is as good a day as any to begin this process. And getting help, reaching out to find an organization or a firm, much like ECHELON, that can play that role of being the advisor is a really important first step. Carolyn, I want to thank you so much today for your insight and your ideas. I think this is a true crisis our industry is facing among many. And certainly, the clients we serve will be better served if, in fact, we move forward in trying to find ways for advisors to, in fact, prepare for their next chapter. So let me ask this question. If our listeners want to learn more about you and what you do, how can they go about doing that? |
| CAROLYN ARMITAGE | Thank you. I would love to have folks that are interested in continuing the conversation. Feel free to reach out to me directly at carmitage or C as in Carolyn, Armitage, A-R-M-I-T-A-G-E at echelon-parters.com. Certainly, you can go to our website echelonpartners.com and see more of what we offer. We'll gladly provide you with a complimentary consultation and discuss what your vision for the future is. |
| BILL COPPEL | And I'll just tell our listeners that all of the information that Carolyn has provided will be in the show notes when you listen to the podcast. You can also-- if you haven't captioned them just now, you can certainly get them off of the notes. Thanks, Carolyn, for sharing your insights with our listeners today. I'm sure we can take a lot away from what you've talked about and help us better prepare for what's ahead in the next frontier for all us. |
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