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### Courting The Little Guy

Mar 1, 2009 12:00 PM, By Brooke Southall

**TD Ameritrade Institutional is shifting its focus back to its core client group of RIAs with \$50 million or less in assets. But it has some tough competition from Schwab and Fidelity.**

A war is on for the little guy in the RIA custody business. Suddenly, everyone wants his calling card. Things were a little different a couple of years ago. In the two years following the TD Waterhouse-Ameritrade merger, which closed in 2006, TD Ameritrade managed to alienate its core client base — RIAs custodying \$50 million or less with the firm — due to integration headaches and service interruptions. It also dropped the ball for these clients as it began to court larger RIAs who offered to custody \$1 billion or more in assets with the firm.

In the interval, rivals Schwab Institutional and Fidelity Institutional Wealth Services — the Nos. 1 and 2 in the RIA custody business in terms of assets — moved in on its turf, throwing open their doors to small RIAs, say executives at both firms. These days, they claim, they're as good as or better than TD Ameritrade on serving and recruiting this group. And they say TD can expect tougher competition in the future.

Naturally, Tom Bradley, president of TD Ameritrade Institutional, is having none of it. TD Ameritrade has refocused and won back the favor of its small clients, says Bradley. His firm "owns" the under \$50 million shop, he claims. Though the firm won't provide data on the breakdown of its client base, Nexus Strategy, an RIA consultant in Larkspur, Calif., estimates that TD Ameritrade caters to some 3,600 RIAs with under \$50 million in assets custodied at the firm, by far its biggest client group. (That's 3,600 out of TD Ameritrade's total of 4,040 RIA clients, or 90 percent of its RIA firms.) That said, Schwab is not far behind, serving 3,300 RIAs that custody under \$50 million in assets, while Fidelity serves 2,450, according to the Nexus data. (See table on page 46.)

#### SMALL IS BEAUTIFUL

Why so much fuss over the smallest-of-the-small RIA shops? After all, firms with fewer than \$50 million custodied with TD Ameritrade generate less than 10 percent of TD Ameritrade's annual revenues, says Bradley. (Obviously, the other 10 percent of its client base — those RIAs with over \$50 million in assets at TD Ameritrade — generates the other 90 percent of revenues for the division.) Still the small-RIA business is solidly profitable, he says. In fact, Nexus estimates that custody firms generally earn about 12 basis points on assets from an RIA with under \$50 million, versus 15 basis points for RIAs with \$500 million or more in assets — a difference of three basis points. That's because the bigger guys often negotiate discounts, explains Nexus Strategy's Timothy Welsh.

And anyway, some of these "small" RIAs are large firms in disguise, with \$1 billion or more in assets spread across multiple custodian firms. In these cases, the point is simply to get a foot in the door and eventually convince them to bring over additional assets, says Welsh. Perhaps most importantly, "small" RIAs represent a tremendous opportunity these days: Many of the breakaway brokers who are leaving Wall Street firms to set up independent RIA shops fall into this under \$50 million category. In 2008, Schwab recruited 123 breakaway teams with \$13 billion in assets, Fidelity brought on 102 breakaway teams with \$6.1 billion of assets, and TD Ameritrade

netted 59 teams. (The firm declined to disclose assets.)

**TD ADVANTAGE**

Some of the biggest problems TD RIAs faced after the merger in 2007 included faulty mutual fund order processing, difficulties executing wire transfers and problems with quarterly statements, says TD Ameritrade CEO Fred Tomczyk. To top it off, high call volume to service centers meant there were long wait times, RIAs complain. That year, TD's RIA clients registered their dissatisfaction on the firm's Client Satisfaction Index. According to a survey of the firm's RIA clients, just 30 percent of TD's RIA clients were "satisfied" with its service in 2007, down from 80 percent before the merger. The good news for TD Ameritrade is, that metric has since bounced back and is again at around 80 percent today, according to the company.

TD's advantage with the small RIA group is that it can focus on them without being distracted by the distinctly different challenge of serving big, sophisticated RIAs, says Philip Palaveev of Fusion Advisor Network in Elmford, N.Y., and a former senior analyst for Moss Adams LLP. (TD caters to just 50 RIAs with over \$1 billion in assets, according to Nexus.)

Greg Phelps, principal of Red Rock Private Wealth Consulting, of Las Vegas, with \$30 million in AUM, says he gets better service at TD Ameritrade. "I had under \$25 million with Schwab [in 2005] and they treated me like peanuts. It was like I was a bother," he says. But his experience with TD was different. "I got spectacular service from TD even though I only had \$10 million or \$15 million with them" initially, he adds. For instance, he says, TD takes him seriously when he calls to make a \$25,000 bond purchase. The broker will take extra time doing research and getting him a good price. Plus, it was salt in the wound to have to pay quarterly custody fees to Schwab when his assets fell below \$10 million. Phelps decided to park all of his assets at TD Ameritrade, despite the hassles of transferring clients.

Indeed, unlike TD Ameritrade, both Schwab and Fidelity charge firms with under \$10 million in assets a \$1,200 fee every three months. (Fidelity waives the charge for small RIAs that agree to put their assets in designated turnkey asset management programs, tamps, however.)

TD depends on these smaller RIAs, because, while they have fewer assets, they are not as demanding on service or fees. Big fish want high-end service even on their small custody accounts. Of course, TD will provide that kind of service if the RIA offers a big enough chunk of assets, says Bradley. The firm designates four to six employees each to the biggest accounts.

**THE COMPETITION**

Jon Beatty, national sales manager of relationship management for Schwab Institutional, says that Schwab became less attentive to the small RIA in the early 2000s. But when company founder retook the helm as CEO in 2004, Schwab returned its attention to the group. In the past two years alone, Schwab has about doubled the assets it manages for RIAs with fewer than \$50 million. The firm also attracted 500 new small RIAs in 2008. "It's all about scale and we have the benefit of being the biggest provider" to RIAs, Beatty says.

To attract more of these small RIA clients, Schwab has hired 50 percent more service agents and relationship managers who are dedicated to the group, says Beatty. The relationship managers help familiarize existing small RIAs with Schwab's products and services and recruit new RIAs, he explains. "We believe we are now the best service provider to the small advisor," he says.

Fidelity has also made serving small RIAs a strategic priority during the past two years, says Pat Jancsy, a senior vice president of Fidelity Institutional Wealth Services. Fidelity shifted its emphasis to this group in order to attract breakaway brokers, most of whom manage \$40 million to \$50 million in assets when they arrive.

"We view this as a critical component to our business plan," says Jancsy. "The breakaway broker opportunity brought it to light."

Still, Schwab and Fidelity's love of smaller RIAs may be temporary, a function of the current market, says Palaveev. (Fusion's network of 120 RIAs are virtually all firms with under \$50 million in AUM, and they custody assets with whichever firms they want.) "It's the ebb and flow of business development" to move up market and down market based on the prevailing economic conditions, he says. The lower end is attractive now, because crashing portfolios have made yesterday's bigger RIAs into today's smaller ones and all assets are welcome in a drought, he says.

"They're trying to have their cake and eat it too," he says, by reaping profits from big advisors and proclaiming their love of small advisors, too.

**RIA MARKETSHARE**

**TD AMERITRADE LEADS IN THE UNDER \$50 MILLION SEGMENT, BUT NOT BY MUCH.**

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	Total RIA Marketplace	SCHWAB	FIDELITY	TDA
\$1 B +	1,260	300	125	50

<b>\$500mm - \$1 B</b>	1,080	260	100	40
<b>\$100 - \$500mm</b>	3,960	950	125	160
<b>\$50mm - \$100mm</b>	4,680	1,100	470	190
<b>\$0 - \$50mm</b>	7,020	3,300	2,450	3,600
<b>Total</b>	18,000	5,910	3,270	4,040

Note: These numbers are estimates. Totals do not add up due to RIAs using multiple custodians.

Source: **Nexus Strategy, LLC**

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