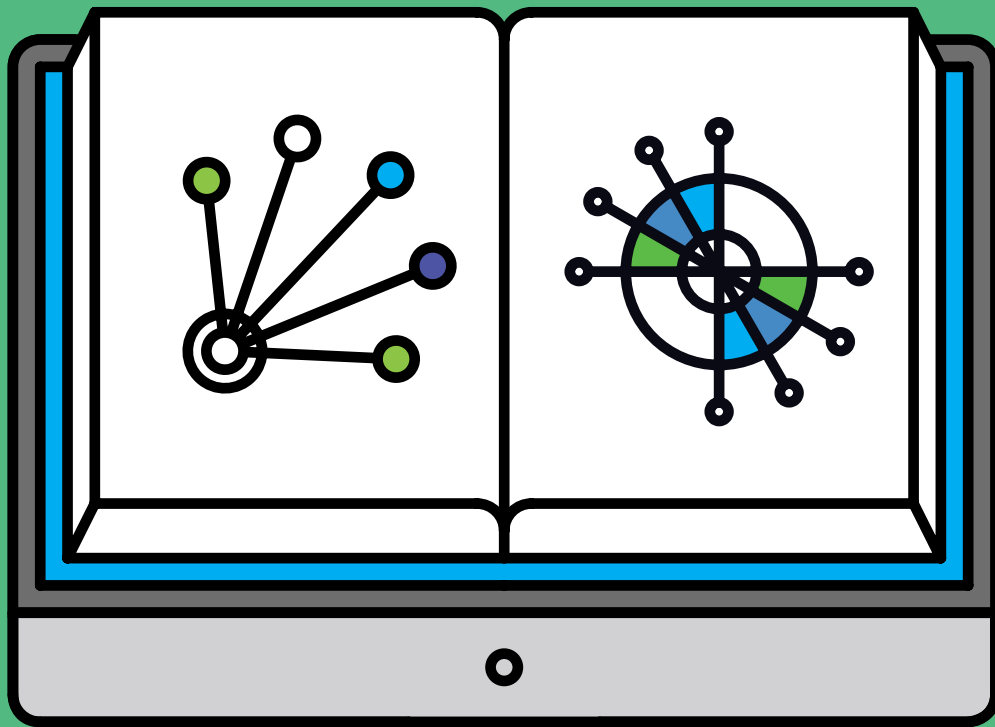


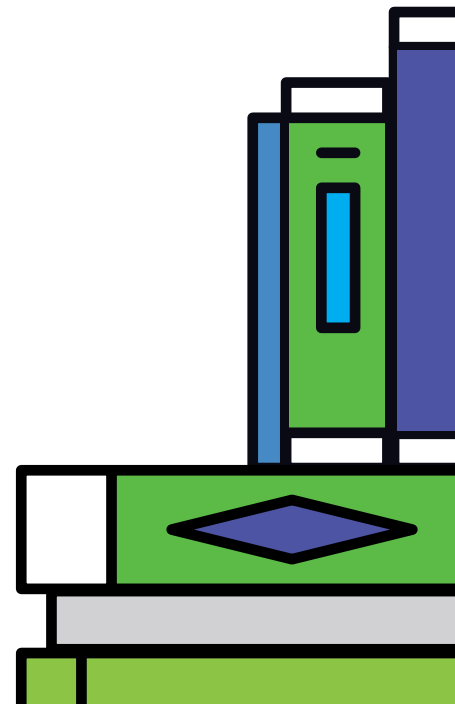
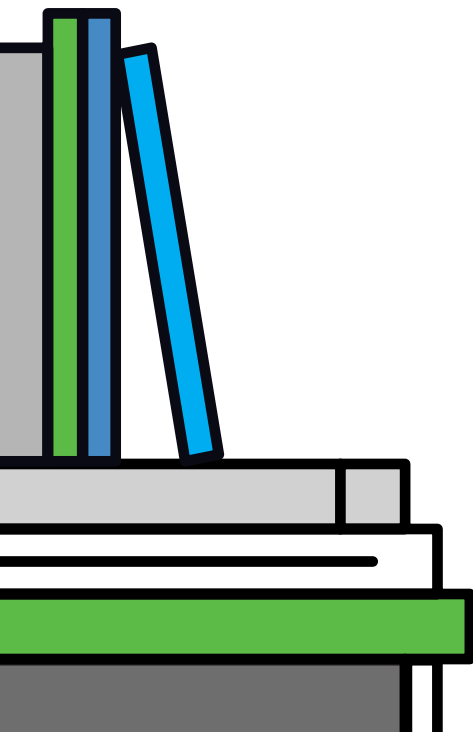
INTEGRATED INDEPENDENCE:  
**FIDUCIARY  
TECHNOLOGY**  
FOR THE DOL RULE AND BEYOND



 **ORION**

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# INTRODUCTION

Orion Advisor Services, LLC is pleased to provide this industry report developed exclusively for the wealth management industry based on the latest research and expert opinions to help advisors succeed.

Massive change is happening in wealth management – ranging from regulatory updates, to new technologies bringing new competition and fee pressures to advisors, along with shifting consumer expectations that is raising the bar for all players.

As a result, advisors and independent broker-dealers need to re-think their approach to building a sustainable business to survive and thrive in this new environment. Industry experts all agree that a key to success will be to harness the latest technologies to develop a flexible infrastructure so that firms can adapt to the many macro changes impacting the industry.

Chief among those big changes are new regulatory requirements driven by the Department of Labor’s fiduciary rule. The DOL rule represents a generational regulatory change that ultimately is a vast, sweeping piece of regulation, poised to become the biggest change to the business of delivering financial advice since the de-regulation of commissions in the 1970’s.

While there may be some modifications to the rule’s timing and substance due to the new political regime recently voted into office, firms can’t afford to ignore the best-interest standard movement in the industry.

Leading firms are taking the initiative to introduce new approaches to comply not only with the base requirements under DOL, but also to build a fiduciary competitive advantage in the industry as being a forward looking firm that puts their clients’ interests first – a compelling message no matter what your business model that will solidify relationships for the long-term.

To help firms think through their response to embracing this change, this white paper will provide a detailed review of the new requirements under the DOL rule, put forth an independent technology “vision” for building a sustainable and flexible fiduciary infrastructure that will not only comply with best interest requirements, but also position firms for success in a much more competitive, complex and uncertain future.

We invite you to learn more about our business and practice management resources by logging on to [www.OrionAdvisor.com](http://www.OrionAdvisor.com).

# THE DOL RULE - NEW PILLARS FOR COMPLIANCE

In April 2016, the Department of Labor released its revised proposal to update the definition of “fiduciary investment advice” under the Employee Retirement Income Security Act of 1974 (ERISA). The key premise of this new rule is to determine what types of activities subject a financial advisor to fiduciary requirements. This change is important for retirement investors as it dictates that those providing fiduciary investment advice must act in their client’s interest ahead of their own and significantly expands the types of communications that constitute fiduciary investment advice.

Based on the DOL’s research and position, their mandate is to create a new rule to protect retirement investors from being over-charged in their retirement accounts by commissions that ultimately benefit the industry more so than investors. The DOL estimates that retirement investors will save \$40 billion over the next 10 years<sup>1</sup>. A hotly debated rule, the DOL has been a lightning rod in the industry that will create massive change in how firms will comply.

Under the new rule, the DOL is expanding the definition of fiduciary investment advice to now include situations where advisors receive compensation for providing recommendations that are related to an employee retirement plan, a plan participant, as well as IRA and IRA Rollover account owners, as well as other types of clients not previously covered. A key provision to the rule is that it includes a functional approach to who is considered a fiduciary based on the types of services rendered, not based on the title of the person. Thus, broker-dealers, RIAs, insurance agents and other advisors will be held to the same standard when they perform the same advisory function.

The best interest fiduciary standard requires that any advice given should be based on the premise that the advisor is being prudent with his/her recommendations, avoids misleading statements, and is charging a reasonable fee for services rendered.

Due to the inherent conflicts that come with receiving variable compensation (commissions) that vary based on a client’s investment in certain products, an advisor’s recommendation of such products would typically violate the best interest fiduciary standard. However, rather than an outright ban of variable compensation, the DOL has sought to create a flexible regulatory structure that can theoretically apply to all business models so long as they can satisfy the requirements of one of a number of exemptions. Qualifying for one of these exemptions will be critical for the continued utilization of variable compensation business models by broker-dealers and insurance companies.

<sup>1</sup> <http://www.usatoday.com/story/money/personalfinance/2016/04/05/fiduciary-ruling-investor-adviser-advisor/82655312/>

## AT A GLANCE DOL SUMMARY<sup>3</sup>

“The organizing principals for following the DOL rule for all participants – both BDs and RIAs – can be summed up into three words: notify, satisfy, document,”

“All firms when working with retirement accounts need to notify their clients that they are acting as a fiduciary in specific communications, satisfy that commissions and prohibited transactions are managed via the best interest contract (BIC) or level-fee exemptions, and document all aspects of their client interactions for future audit from examiners and plaintiff attorneys.” ~ Brian Hamburger, CEO at MarketCounsel, an industry leading compliance consulting firm.

Of particular note is the DOL’s new exemption called the Best Interest Contract Exemption (BICE), which according to attorney Marcia Wagner, principal of the Wagner Law Group<sup>2</sup>, generally permits firms to, “use current compensation models as long as they acknowledge their fiduciary status, give prudent and impartial advice, disclose potential conflicts of interest and information about their revenue model, avoid misleading statements and receive no more than reasonable compensation.” The BICE will be a key way firms will be able to continue with their commission-based practices under the new rule.

For independent RIAs who are already held to a fiduciary standard, the DOL has also created a “level-fee” exemption, which streamlines many of the BICE requirements for qualifying “level-fee” business models for RIAs working with retirement accounts. However, there still will be new documentation steps RIAs will need to incorporate to show compliance upon audit or litigation.

As a result of these new requirements, all firms will need to adopt new workflow processes and procedures to ensure that they are compliant. Documentation will be key to this approach as all firms now need to be able to prove that they are following the requirements of the rule when it comes to working with retirement accounts to ensure that disclosures are provided appropriately, any BICE-related agreements are provided, signed, and fees are justified as reasonable. This information must be archived and be able to be retrieved on demand for audits and/or legal actions.

As you can imagine, these new steps will require an upgrade to current systems and technologies. Many in the industry are investing aggressively to create a new technology infrastructure that spans the entire client relationship, from proposal to account opening to ongoing monitoring and review. First movers are being rewarded with industry leadership positioning and the ability to have a flexible infrastructure that will serve them well in a post-DOL world.

In the meantime, however, industry experts are actively cautioning advisors and broker-dealers to be skeptical about technology companies promising total DOL compliance through a single platform. As noted above, DOL requirements will touch virtually all systems, applications and components of the client lifecycle. Effective DOL compliance must be customized based on the advisor’s unique services in view of a specific client’s needs. Thus, it is critical to have a strategy and vision for your entire technology stack, and not simply rely upon one system for compliance.

<sup>2</sup> <http://www.fa-mag.com/news/understanding-the-best-interest-contract-exemption-26741.html>

<sup>3</sup> <http://www.thinkadvisor.com/2016/11/08/forget-robos-regulations-now-top-driver-of-advisor?slreturn=1479492096>

# A TECHNOLOGY VISION FOR FIDUCIARY AND BEYOND

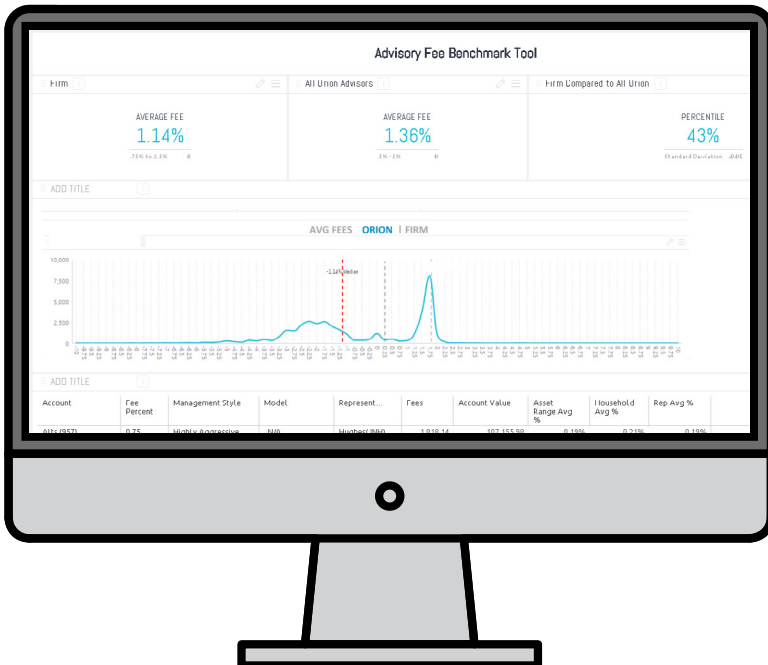
Our research and consultation with legal, compliance and technology experts confirms that the key to success will be the ability to develop an integrated, independent, fiduciary workflow process that brings in various components into a composite application to automate a complex process, end-to-end.

According to Mike Forker, Chief Compliance Officer for CLS Investments, LLC, a leading ETF Strategist that works with more than 2,500 advisors and 1,300 qualified plan sponsors to manage more than 35,000 investor portfolios, there are key aspects to managing fiduciary duties beyond just what the DOL is requiring. “Even further than the DOL rule implications, the industry is moving towards a fee-based model and the only way to effectively grow and scale that business is through technology.”

Forker describes a technology vision that begins with a comprehensive wealth management platform that has the key components necessary to provide internal efficiencies, while also meeting client and compliance needs through a superior technology experience.

For other components such as proposal generation, risk analysis, financial planning and CRM, it is critical to be able to tightly integrate those pieces through open architecture and advanced API functionality.

As an example, consider the client relationship, end-to-end workflow process that can be automated beginning with Orion’s comprehensive wealth management platform and integrating other key systems to create a unified advisor/client experience:



Orion’s Advisory Fee Benchmarking Tool

**Proposal Generation** - In order to initiate a new relationship or expand an existing one, a good place to start is with the proposal process. Through integrations with leading proposal systems, key data is uploaded from Orion and relevant financial planning and risk analysis systems to develop a comprehensive proposal with any language, disclosures, and sign-offs needed. These proposals are archived and are available on demand for any future documentation requirements from audits and/or lawsuits.

“At CLS, our first interaction with a client is in the proposal process,” Forker notes. “Thus, any recommendations contained in that proposal need to have compliance oversight so that recommendations are prudent and consistent with the

## THE IMPORTANCE OF FEE BENCHMARKS

In addition to what will be required under the new DOL fiduciary rule to show that fees are “reasonable,” there are also many practice and client management benefits advisors will be able to realize with the new fee-benchmarking tool in the Orion wealth platform.

A common client management issue that routinely comes up for advisors is to explain how their fees stack up in the industry. When clients ask, advisors are often left to more qualitative explanations to describe how their fees relate to their services. Now, with the new fee-benchmarking tool in Orion, advisors will be able to query millions of accounts to determine fee-benchmarks based on specific portfolio sizes, asset allocations and services offered.

This quantitative information will be a powerful communication tool to showcase how a firm’s fee schedule stacks up, providing more transparency to the advisor-client relationship, ultimately enabling advisors to better communicate the value they are providing.

client’s risk tolerance and financial situation such as goals and net worth. In order to bring that information in, we are integrating Orion with a proposal platform that can automate this process and archive for any future requests.”

**Disclosures/Contracts** - In order to minimize paper processes, leveraging advanced client portal and document vault features of Orion enables clients to take delivery of any contracts, agreements necessary to be signed via integrations with popular file sharing platforms such as Box and Dropbox. Further, by integrating with e-signature platforms, clients are able to electronically sign documents, speeding up the process.

“In situations where we need to enter into a BICE agreement, regulators have confirmed that we are able to put a copy of that contract behind a login, and then integrate with file sharing systems through Orion plug-ins,” says Forker. “This approach will streamline the process and ensure we have the right disclosures and agreements in place.”

**Fee Analyzer** - One of the most important aspects of DOL compliance will be the ability for advisors and their firms to prove that their fees are “reasonable.” By creating custom fee-benchmarks for accounts based on size, asset allocations and services provided, advisors will have a documented process to show that fees are in the realm of reason. Orion’s massive account database contains millions of accounts that can be the source for benchmarking what is a reasonable fee, as well as identifying when fees may be outliers.

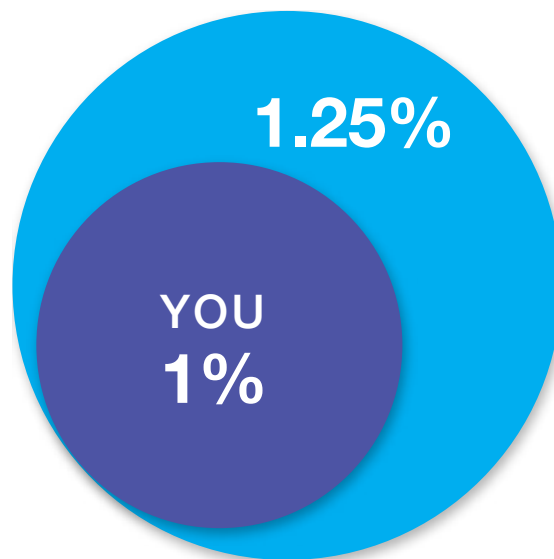
“Proving fee reasonableness will be a key aspect of complying with a fiduciary standard,” Forker says. “The ability to leverage Orion’s fee analyzer will be a real service to the industry. While you could look at other firms’ form ADVs, those don’t provide the specifics you can get by looking across millions of accounts.”

**Ongoing Monitoring** - Another key aspect of DOL compliance will be the ability to show that advisors and their firms are actively monitoring the clients’ situation and are continuing to operate in a best interest standard. Through integrations with risk analysis tools, batch reviews of all clients can be conducting on an ongoing basis to document that advisors are keeping an eye on client portfolios as well as updating through ongoing questionnaires to again document when client circumstances change over time.

“There are two levels to ongoing monitoring compliance,” Forker notes. “Firms need to look at what they are doing as well as what is happening with the client’s situation. On our side, we are looking to bring in external checks through a risk batch review in order to monitor existing accounts and thus need technology to do that efficiently over 35,000 accounts to comply. On the client side, we need to monitor suitability through clients’ providing us with updated information and letting us know if their circumstances have changed – a very important part of being a fiduciary.”

**Education** – In order to meet prudence standards, advisors and their firms will need to conduct frequent interactions to keep clients informed. Thus, ongoing communications will be a critical component to prove compliance through a rich client portal, mobile applications, all the way to even text message updates and video statements.

“Ongoing education with clients is very important to help set expectations, particularly if they indicate that they are a conservative investor, yet also expect high returns from their portfolio,” Forker says. “In order to do this efficiently, we need to communicate regularly with clients in the manner that works best for them. That is why we will be leveraging the Orion client portal with updates there, through text messages, as well as video, so that we meet all personality types.”



- = Your Advisory Fee %
- = Compared to Benchmark



# INTEGRATED INDEPENDENCE - THE FUTURE OF WEALTH MANAGEMENT TECHNOLOGY

The above framework provides a compelling approach to building the right technology strategy for not only the DOL's requirements, but also for future changes that are sure to come in this rapidly evolving industry.

The one thing that will always be a constant is change in the wealth management space, according to top advisors.

"We're on the eve of the greatest disruption this industry has faced since the Great Recession," according to Ron Carson, one of the industry's most successful and well-respected advisors.

He recently noted<sup>4</sup>, "If you're an advisor, you need to decide whether you are going to be a disruptor or one of the disrupted. Clients are becoming 'smarter by the day' about the differences in how advisors work," Carson says. "Many still don't understand about embedded conflicts of interest, but they are getting the difference between a planner and a broker. They want transparency and an advisor who's a fiduciary. If they are not getting those things, they're going to move to another advisor who offers them."

This articulation of where the industry is headed goes beyond the DOL rule and points to the fact that there is a clear fiduciary movement gaining momentum in the industry. Even the largest broker-dealers are driving this movement, including such industry luminaries as Merrill Lynch and JP Morgan who are both dramatically altering their business models and marketing to promote a fiduciary standard.

Thus, the message is clear - now is the time to prepare and the best way to do so is through an independent technology strategy. As fiduciaries, advisors will need to provide customized advice through best-in-breed applications, implying that your technology also needs to be independent from conflicts of interest.

Relying on "all in one" bundles from custodians and asset managers often imply subsidies to firms, creating additional conflicts of interest that limit advisors and their firms from choice and flexibility to best serve their clients.

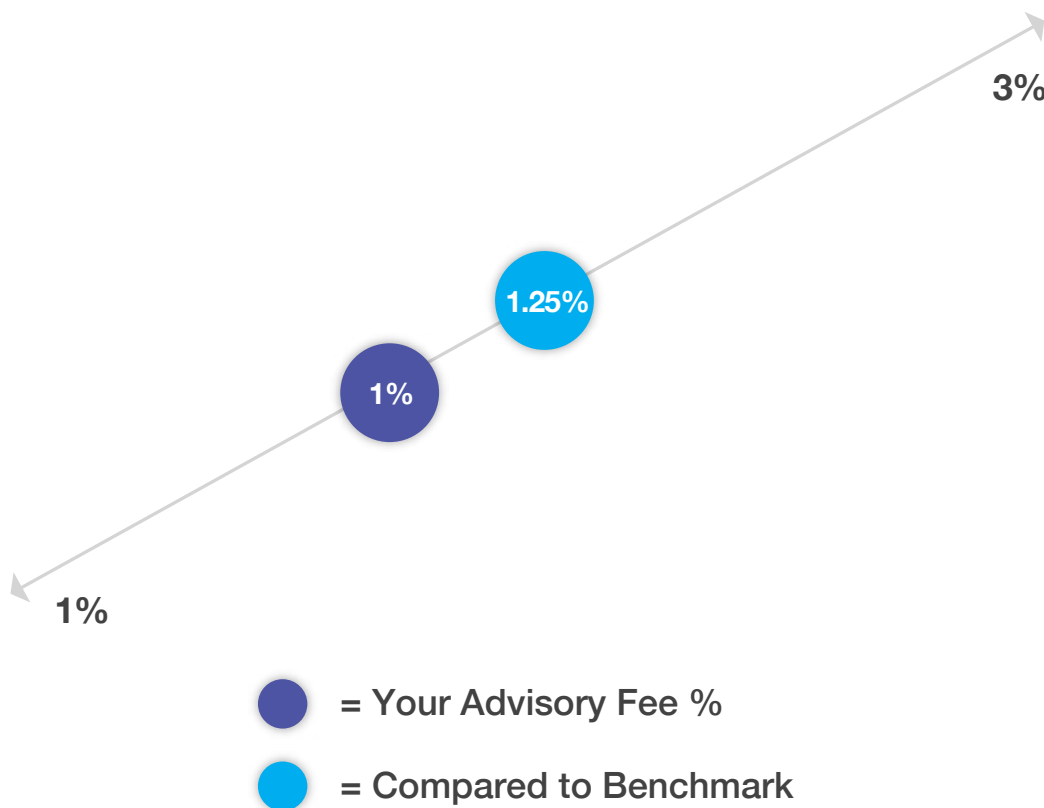
A better way forward is to pursue an integrated, independent technology strategy that can be the foundation upon which to create a nimble infrastructure. Firms are able to take advantage of advanced integration capabilities to bring multiple systems together to simplify processes, drive efficiencies and automate workflows.

<sup>4</sup> <http://riabiz.com/a/2016/11/18/commonwealth-financial-will-reverse-course-on-commissions-if-dol-gets-reversed>

The DOL is just one manifestation of a longer-term trend, which is the fiduciary movement to better serve clients by putting their interests first. The SEC also has a mandate from the Dodd Frank bill to put forth a fiduciary requirement for all brokerage accounts. Despite the short-term uncertainty created with the new Trump administration, winning firms are going all in on fiduciary.

The good news is that with advancements in advisory technology and API integrations, there are now more independent solutions available to keep advisors on the forefront with a scalable infrastructure that provides a superior client experience, along with the tools that are flexible to manage whatever the future brings.

But make no mistake, there will be big winners and losers as the industry continues to change and evolve. Those firms that have a fiduciary strategy driving their decisions will be best positioned in a much more competitive, complex and challenging environment.



# ABOUT ORION ADVISOR SERVICES

Orion Advisor Services, LLC (Orion) is the premier portfolio accounting service provider for advisors. Our firm has unique insights into the advisory profession because it was founded for investment advisors by an investment advisor in 1999. Orion frees advisors from back-office tedium so they can enjoy their business again by devoting their time and energy to better serving clients. Orion provides the integrated and fully customizable technology solutions that advisors need to help grow their businesses over the long term. The firm's technology solutions empower more than 900 advisory firms with total assets under administration in excess of \$375 billion, from more than one million individual accounts.

For more information about Orion, visit [www.orionadvisor.com](http://www.orionadvisor.com) and follow Orion on Twitter: [@orionadvisor](https://twitter.com/orionadvisor)



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