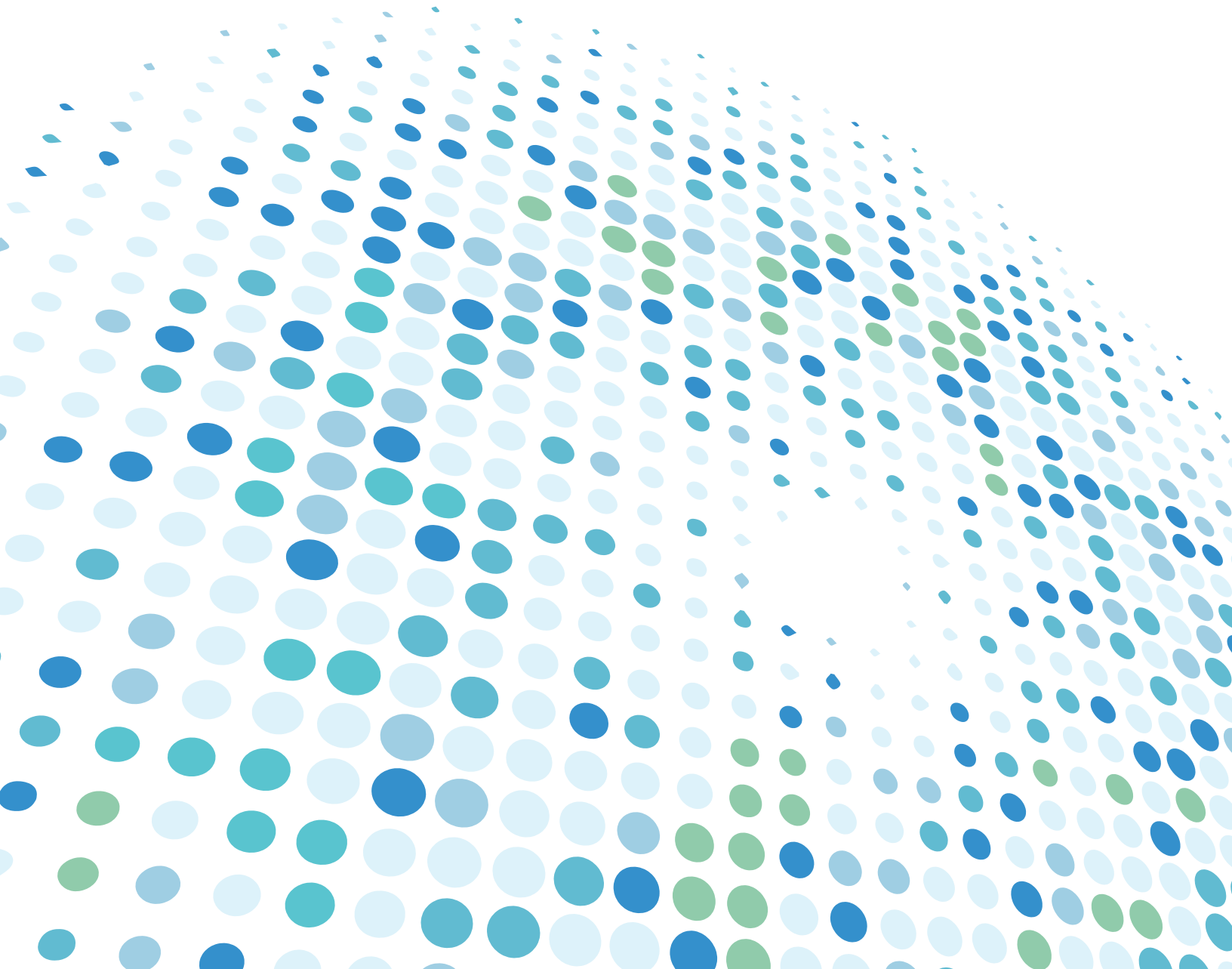


2017

# Evolution Revolution

A Profile of the Investment Adviser Profession





The Investment Adviser Association (IAA), based in Washington, DC, is the leading organization solely dedicated to representing the interests of SEC-registered investment advisory firms. The IAA's members collectively manage assets of approximately \$20 trillion for a wide variety of individual and institutional clients, including trusts, endowments, pension plans, private funds, mutual funds, and corporations. In addition to serving as the voice of the advisory profession on Capitol Hill and before the SEC, DOL, CFTC, and other U.S. and international regulators, the IAA provides extensive compliance and educational services and resources to its membership. For more information, visit [www.investmentadviser.org](http://www.investmentadviser.org).

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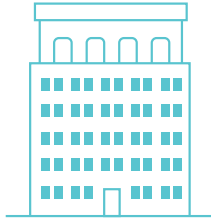
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# The 2017 "Typical"\* SEC-Registered Investment Adviser



Most of its clients are individuals



Highly likely to have at least one pension/profit sharing plan as a client



**\$333 million**  
in regulatory assets under management

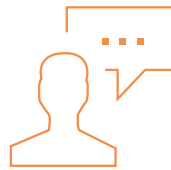
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employees



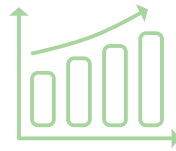
26-100

clients

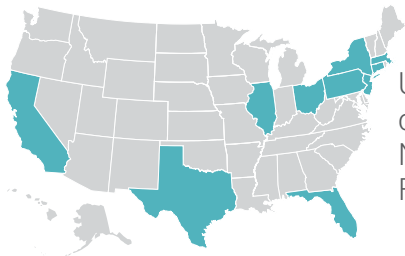


108

accounts



Exercises discretionary authority over most accounts



U.S.-based limited liability company headquartered in NY, CA, TX, MA, IL, FL, PA, CT, NJ, or OH



Does not have actual physical custody of client assets or securities

\*(median)

# Table of Contents

Executive Summary . . . . .	6
Number of Investment Advisers . . . . .	8
Regulatory Assets Under Management . . . . .	10
Industry Concentration. . . . .	12
Clients of Investment Advisers . . . . .	14
Investment Adviser Compensation . . . . .	23
Custody of Client Assets . . . . .	25
Employees of Investment Advisory Firms. . . . .	27
Other Characteristics of Investment Advisory Firms . . . . .	30
Location of Investment Advisers . . . . .	33
Disciplinary Information . . . . .	34

# The Investment Adviser Profession: Still Thriving Amidst Disruption

The Investment Adviser Association and National Regulatory Services are pleased to present our 17<sup>th</sup> annual *Evolution Revolution* report, the most comprehensive profile of SEC-registered investment advisers available. This year's report contains data on 12,172 firms that manage \$70.7 trillion for more than 35.6 million clients. This dynamic profession continues to be critically important to investors, our economy, and the capital markets.

The investment adviser industry remains a powerful provider of high-quality jobs to the economy. Investment advisers now employ a total of 778,002 non-clerical workers, a 10.0 percent increase over the past four years. Over 400,000 of these workers perform investment advisory functions. Many of these positions benefit small businesses. The investment adviser profession has always been dominated by small businesses and this year was no exception, as over 10,000 firms reported employing 50 or fewer individuals. And, as the investment adviser profession evolves to meet the demands of a growing, more tech-savvy client demographic, the industry may add positions supporting the development of automated advice platforms, trading algorithms and robust client portals and access systems.

Over the same four-year period, the number of clients served by the profession grew by 39.6 percent. During this time, product and service innovation has made discretionary investment advice more accessible to the retail investor. Automated investment advice, particularly for retirement plan participants, is a significant driver of client growth over the past several years. The trend toward automation in advice – both as a standalone model and incorporated into “human touch” businesses – is likely to continue, driven by investor demographics, fee pressure, and increasing costs.

The investment advisory industry is not monolithic, but is rather comprised of a wide range of business models and client bases, many with distinct focuses and strategies. In fact, the vast majority of advisers – more than 87 percent – report that the majority of their clients are of a single client category. Nearly 51 percent say more than half of their clients are individuals, for instance, while 29 percent report that most of their clients are pooled vehicles such as mutual funds, hedge funds, or private equity funds. While it remains true that the industry serves a wide range of client types, this specialization has important implications for client service, operations, and regulatory approaches.

*2017 Evolution Revolution* provides a full portrait of the SEC-registered investment adviser profession, presenting data on these major themes as well as on industry concentration, compensation, non-core business activities, financial industry affiliations, geographic concentrations, disciplinary information, and more.

It is our hope that our 2017 report provides information and analysis of value not just to investment advisers but to the public, policymakers, and the millions of clients SEC-registered advisers serve.

**Karen L. Barr**  
*President & CEO*  
IAA

**John Gebauer**  
*President*  
NRS

# Executive Summary

**The number of SEC-registered investment advisers continues to grow.** The universe of SEC-registered investment advisers continues to grow, albeit more slowly than last year. This report contains data on 12,172 federally registered advisers, reflecting a net increase of 2.7 percent since the 2016 report.

**The industry continues to experience strong job growth in investment advisory positions.** In 2017, SEC-registered advisers reported a total of 778,002 non-clerical employees – relatively flat since 2016. Of these employees, however, 400,163 provide investment advisory services (including research) – a healthy increase of 13,631 since 2016.

**The vast majority of SEC-registered investment advisers are small businesses.** Small businesses are the core of the investment adviser industry. In 2017, 56.8 percent (6,911) of advisory firms reported that they employ 10 or fewer non-clerical employees and 87.4 percent (10,641) reported employing 50 or fewer individuals. Industry-wide, the median number of employees is nine.

**The aggregate RAUM managed by SEC-registered advisers remains substantial – \$70.7 trillion – up from last year and a record high.** RAUM managed by advisers grew a healthy 5.8 percent from \$66.8 trillion in 2016 to \$70.7 trillion this year. This RAUM growth is likely primarily a function of strong stock market performance in the past year.

**SEC-registered investment advisers serve more than 35.6 million clients – relatively flat since last year.** The number of clients served by investment advisers appeared to have dropped 2.1 percent since 2016. However, after taking into account changes in definitional methodology and a reporting error, the number did not in fact decline. The number of advisers reporting that they provide advice exclusively through an interactive website rose by 20 firms – nearly 16 percent – to 146.

**Individuals comprise the largest categories of advisory clients, with pension plan clients coming in second.** Almost 61 percent of advisers serve either high net worth individuals, non-high net worth individuals, or both, while 45.6 percent reported at least one client is a pension or profit-sharing plan (not including plan participants or state or local pension plans). We estimate that these clients represent \$8.9 trillion and \$6.2 trillion, respectively, of the total \$70.7 trillion RAUM.

**Most investment advisers focus their services on one category of client.** More than 87 percent of advisers report that the majority of their clients are attributable to a single category of client. For example, 51 percent of advisers report that more than half of their clients are individuals. Another 29 percent of all advisers report that most of their clients are pooled vehicles (registered or unregistered). Many of these advisers serve pools exclusively: 2,195 report that 100 percent of their clients are private funds, while 298 advisers report that 100 percent of their clients are registered funds. Finally, more than seven percent of advisers specialize in non-pooled institutional clients.

**The average RAUM per client is just under \$2 million.** The average varies significantly, though, across the different segments of advisers based on their overall RAUM and number of clients. Those advisers with fewer clients tended to have a larger RAUM/client average. Additionally, those that have a higher aggregate RAUM, tended to have a larger RAUM/client average. At the extremes, there are three advisers with fewer than 10 clients each and an average RAUM/client of \$29.7 billion RAUM, and 343 advisers with more than 100 clients each and an average RAUM/client of only \$12,250.

**The number of private funds and registered private fund advisers is growing.** In 2017, 4,574 advisers reported advising 34,409 private funds with total gross asset value of \$11.5 trillion (up from 4,448, 32,445, and \$10.5 trillion respectively in 2016). While the percentage of hedge funds and private equity funds was exactly equal last year, there is now a divergence, with private equity funds making gains while hedge fund growth is stagnant. That is not surprising, given recent reports within the past year of hedge fund performance issues and closures. Hedge funds now make up 33.8 percent and private equity funds represent 37.2 percent in this space.

## What's in a Name? A Note on Terminology

The terms “investment adviser,” “financial advisor,” and “adviser” are used imprecisely in the press and by market participants and are often employed when referring to a wide range of financial services professionals, including agents representing life insurance companies and registered representatives of a broker-dealer. This is unfortunate and adds to the general public’s confusion regarding the different types of providers in the financial services industry. Throughout this report, the term “investment adviser” refers to an entity that is registered as such with the SEC, based on the definition set forth in the Investment Advisers Act of 1940.<sup>1</sup>

That said, the term “investment adviser” describes a broad range of companies and people in the business of giving advice about investing in securities. In addition to investment adviser, they may use other titles such as investment manager, wealth adviser, financial planner, investment counsel, asset manager, wealth manager, or portfolio manager. Investment advisers typically provide ongoing management of investments based on the client’s objectives, often with the client giving the adviser authority to make investment decisions without having to get prior approval from the client for each transaction (called discretionary authority).

The terms “broker” and “broker-dealer” refer to companies in the business of buying and selling securities (called trading) on behalf of customers. Individual salespeople employed by brokerage firms are registered representatives of the brokerage firm. But these individuals also use many other titles, including financial consultant, financial professional, financial advisor, advisor, wealth manager, and investment consultant.

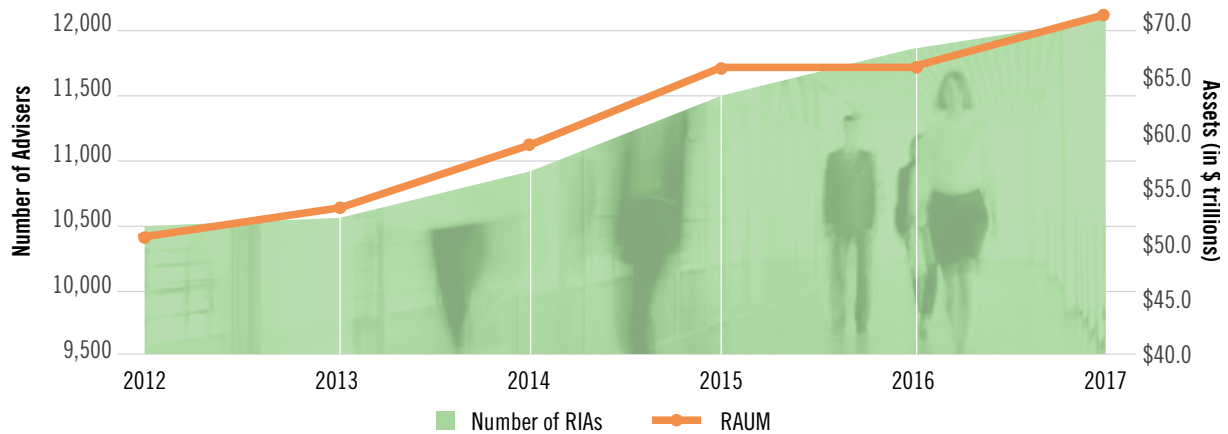
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<sup>1</sup> Section 202 of the Investment Advisers Act defines an investment adviser as “any person who, for compensation, engages in the business of advising others, either directly or through publications or writings, as to the value of securities or as to the advisability of investing in, purchasing, or selling securities, or who, for compensation and as part of a regular business, issues or promulgates analyses or reports concerning securities...” Section 202 also excludes certain entities under certain circumstances, including banks, bank holding companies, broker-dealers, and publishers of bona fide news publications.

# Number of Investment Advisers

This report contains data on 12,172 SEC-registered investment advisers, which represents a net increase of 325 advisers or 2.7 percent since the 2016 report. This increase continues the trend from the previous year, when there was a 3.3 percent increase in advisers. The aggregate RAUM managed by SEC-registered advisers is \$70.7 trillion, a healthy 5.8 percent increase from \$66.8 trillion in 2016.

**Chart 1: Industry Grows and Innovates Despite Challenges**



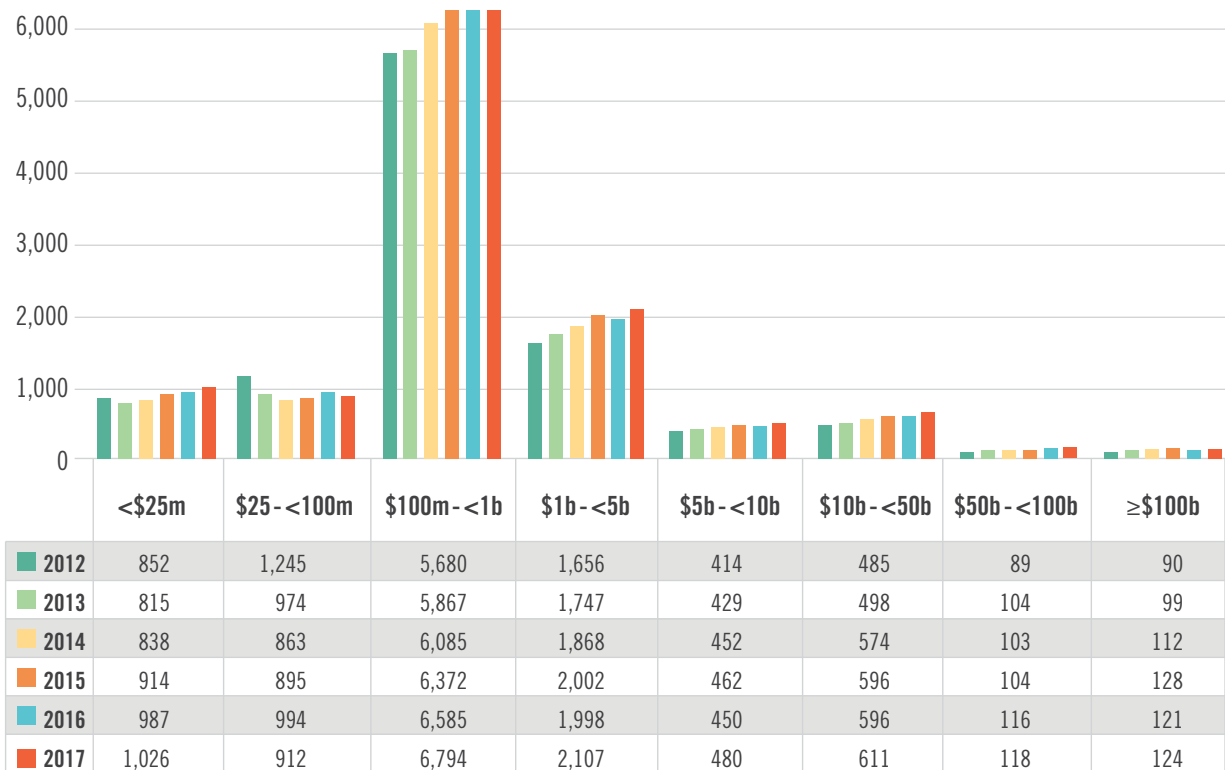
	2012	% Change	2013	% Change	2014	% Change	2015	% Change	2016	% Change	2017	% Change
# of Advisers	10,511	(8.9)%	10,533	0.2%	10,895	3.4%	11,473	5.3%	11,847	3.3%	12,172	2.7%
RAUM	49.4	12.8%	54.8	10.9%	61.7	12.6%	66.7	8.1%	66.8	0.2%	70.7	5.8%

As in past years, more than half of all SEC-registered advisers have RAUM between \$100 million and \$1 billion. The RAUM category from \$1 to \$25 million showed the biggest percentage increase during the period, increasing 8.4 percent and adding 30 advisers since 2016.<sup>2</sup> The category comprising advisers with RAUM between \$100 million and \$1 billion saw the largest total increase by number of advisers, increasing by 201 or 3.0 percent. It remains to be seen whether the robo-adviser trend will increase discretionary RAUM over time, particularly as older and wealthier clients become increasingly comfortable with their use.

<sup>2</sup> Effective July 1, 2017, an adviser having less than \$100 million in RAUM whose place of business is in Wyoming will be required to register with the State of Wyoming instead of the SEC. As of April 10, 2017, 33 advisers that have their principal office and place of business in Wyoming were registered with the SEC.



Chart 2: Number of SEC-Registered Investment Advisers by RAUM Category  
2012-2017



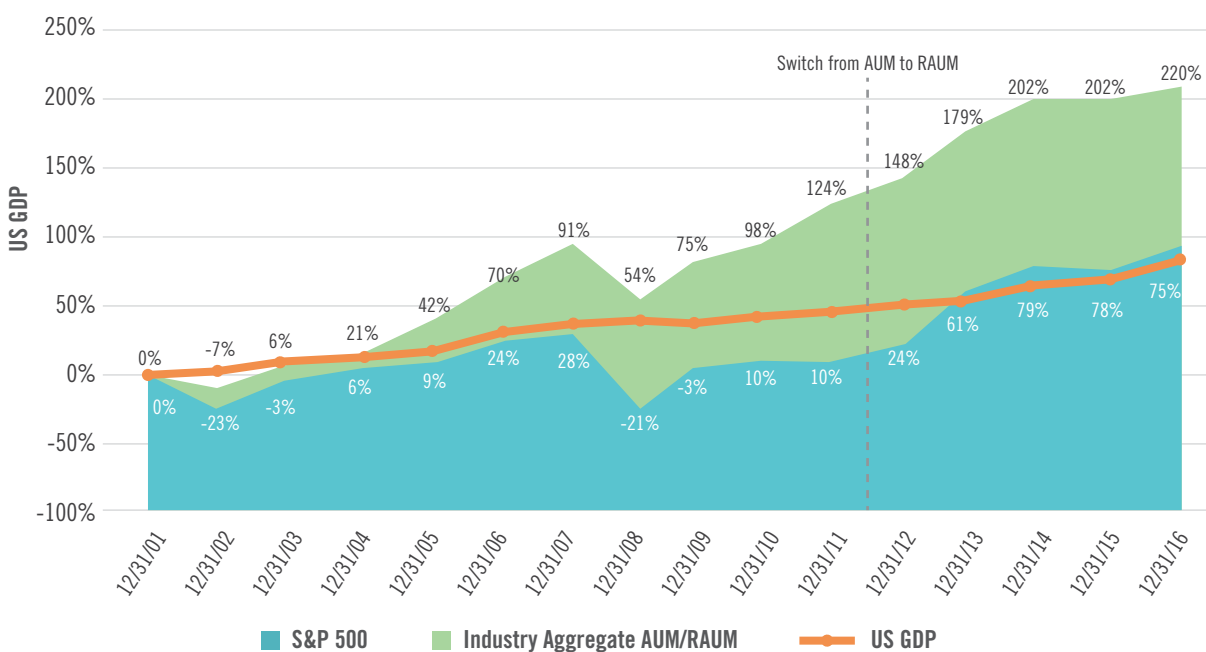
The number of Internet advisers increased by 20 since last year's report, to 146, resulting in a 15.9 percent increase. While the growth of Internet advisers continued at a brisk pace, ostensibly due to the ongoing interest in robo-advisers and robo-technology, it did not eclipse the previous year's growth rate of 59.5 percent. Certain Internet advisers have a website but do not appear to be actually doing business – they are essentially shelf registrations. As the robo-tech industry has evolved, many advisers have evolved into hybrid, or "bionic" advisers, and have incorporated human advice alongside robo-advisory solutions. Selection of the bionic option precludes registration as an Internet adviser, which limits non-electronic advice to a maximum of 15 clients in a 12-month period.

# Regulatory Assets Under Management

Regulatory assets under management (RAUM) reported in 2017 increased from \$66.8 trillion in 2016 to \$70.7 trillion, a one-year growth of approximately \$388 billion or 5.8 percent.

The historical growth of the industry's aggregate assets under management (AUM) or RAUM (depending on the prevailing regulations) has been quite impressive at least since our first report in 2001. The \$70.7 trillion RAUM that registered investment advisers now manage is more than three times 2001 AUM levels.<sup>3</sup> The total industry aggregate AUM/RAUM has grown 220 percent since 2001 – a compound annual growth rate (CAGR) of 8.1 percent. By way of comparison, during the same period, the S&P 500 Index and the US Gross Domestic Product produced cumulative growth of 95 percent (4.6 percent CAGR) and 75 percent (3.8 percent CAGR), respectively.

**Chart 3: Total RAUM has Grown at a Faster Pace than the Overall Economy**



Since the first edition of *Evolution Revolution*, we have reported that the vast majority of assets are managed on a discretionary rather than a non-discretionary basis. This year, 91.7 percent of the total reported RAUM are discretionary assets, a 0.3 percent increase over last year and consistent with the historical values that have stayed in a range from 87.9 percent to 92.1 percent.

<sup>3</sup> In 2012, the methodology for calculating RAUM changed significantly from the methodology used to calculate AUM in previous years.

RAUM is the best metric available to measure the relative size of the investment adviser market on a year-to-year basis. RAUM is rigorously calculated by each adviser according to the same rules. As an absolute measure, however, RAUM has several flaws. First, as we've reported in past years, the aggregate RAUM reported across the industry overstates actual RAUM because more than one adviser can "claim" the same assets. For example, an adviser that allocates assets among mutual funds on a discretionary basis and the adviser to those funds will both correctly include those assets in their RAUM calculation. Similarly, a sub-adviser to a fund will count the assets it sub-advises as RAUM, as will the primary manager of the fund. In addition, we note that the RAUM figure includes assets in addition to those actually currently invested for clients. For example, RAUM includes uncalled capital commitments and proprietary assets.<sup>4</sup>

## Enhanced Data Reporting: Form ADV Part 1 is Changing

Beginning with amendments filed after October 1, 2017, Form ADV Part 1 will require investment advisers to report additional data about separately managed accounts ("SMAs"). The enhanced data collected will include information on the types of assets owned by SMA clients. In addition, certain advisers will be required to provide information on borrowings and the use of derivatives, including gross notional exposure of derivatives in the aggregate held in client SMAs.

The amendments to Form ADV also will require advisers to disclose more information about their advisory business, including data on clients, social media, branch offices, custodians, outsourced CCOs, and more. Further, the rules will permit a single registration for certain groups of private fund advisers operating as a single advisory business.

Look for next year's *2018 Evolution Revolution* report for information and analysis on this important new data.

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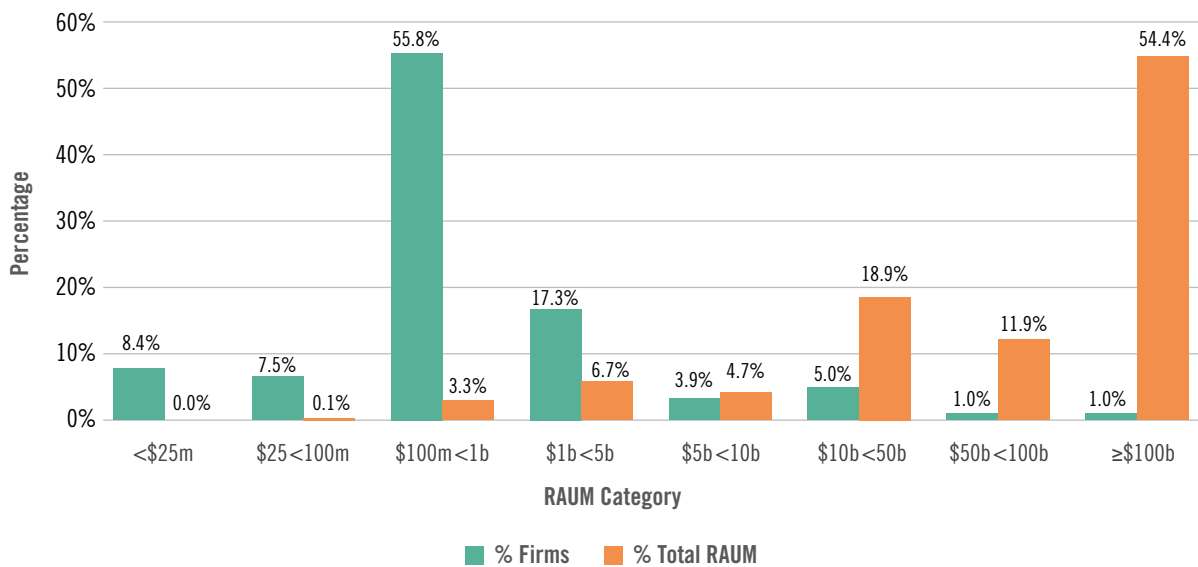
<sup>4</sup> Additionally, the timing of Form ADV filings can impact the accuracy of the aggregate RAUM. Form ADV requires advisers to calculate and report their RAUM within 90 days of the filing. Most advisers calculate their RAUM as of December 31, but 780 (6.4 percent) choose another day. Depending on the timing of the RAUM calculations made by each adviser, the aggregate RAUM may include some temporal variations in market value.

# Industry Concentration

As reported in previous years, a relatively small number of very large advisers manage a high percentage of total RAUM. This year, 124 advisers reported managing \$100 billion in RAUM or more—a 2.5 percent increase following the net 5.5 percent decrease in the number of these advisers from last year. Despite accounting for only one percent of SEC-registered advisers, these 124 firms collectively managed more than half (54.4 percent) of all reported RAUM.

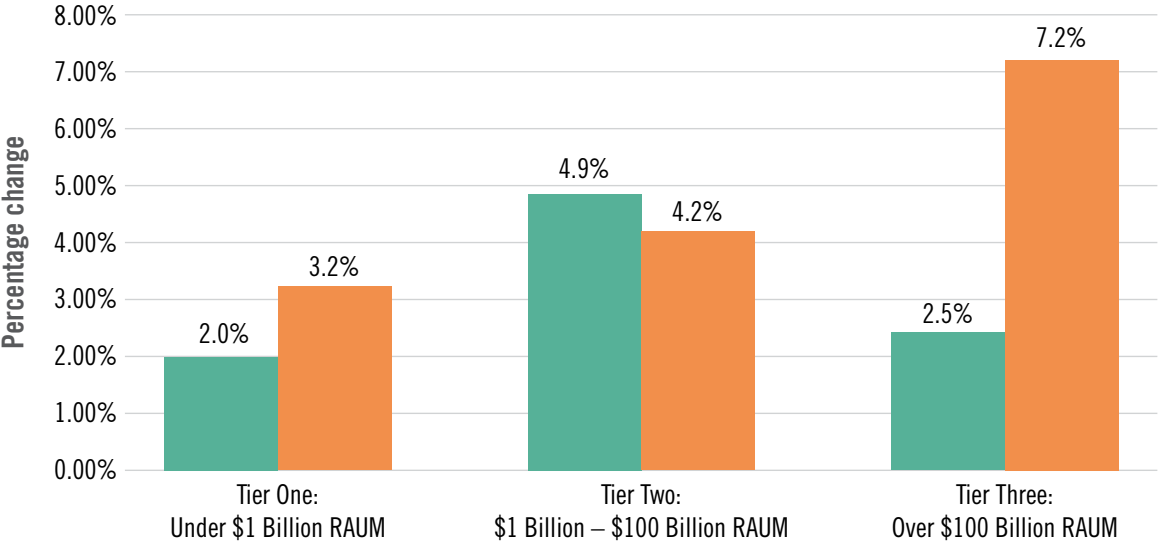
At the other end of the spectrum, 71.7 percent of all advisers managed less than \$1 billion RAUM, and they collectively managed only 3.4 percent of all reported RAUM.

**Chart 4: The Industry Barbell – The Largest Firms Manage More than Half the Assets**



When viewed in tier groups of under \$1 billion, \$1 billion to \$100 billion, and over \$100 billion, all three tier groups showed growth in both RAUM and number of advisers. This is a departure from last year’s report, in which there was variation among and within the tier groups. Another point of differentiation from last year is the resurgence of the largest advisers, which grew faster in terms of RAUM than any other group, in contrast to last year, in which the smallest advisers grew at the fastest rate.

**Chart 5: Growth Rates by Tier Groups—Largest Advisers are Growing Faster**



	Number of Advisers	RAUM
<b>Tier One: Under \$1 Billion RAUM</b>	2.0%	3.2%
<b>Tier Two: \$1 Billion - \$100 Billion RAUM</b>	4.9%	4.2%
<b>Tier Three: Over \$100 Billion RAUM</b>	2.5%	7.2%

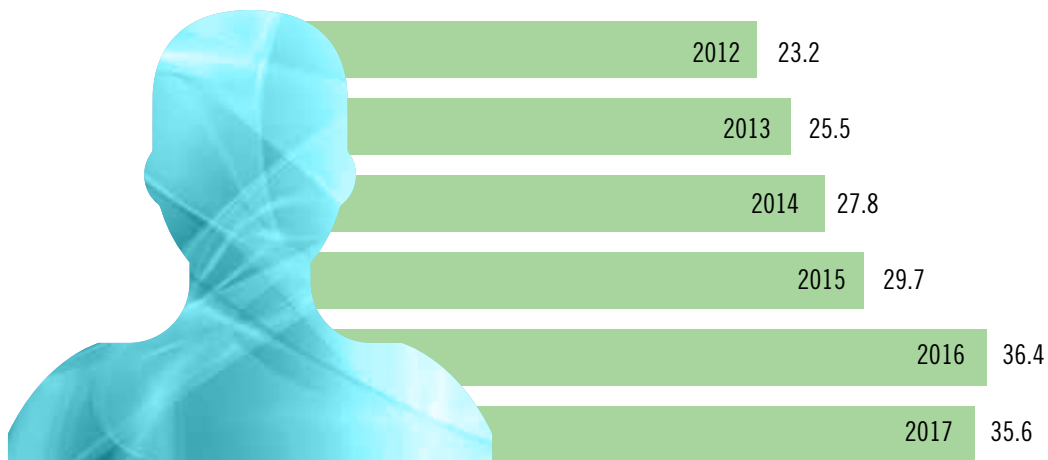
# Clients of Investment Advisers

Form ADV requires advisers to report their approximate number of clients and the types of those clients by number and RAUM. This data provides several insights into the industry.

## Advisers by Number of Clients

SEC-registered advisers in 2017 reported a total of more than 35.6 million clients, down slightly from the 36.4 million clients reported in 2016.<sup>5</sup> This slight decrease is not meaningful, however. A number of “robo”/retirement advisers reported large decreases, which we understand are primarily attributable to changes in definitional methodology,<sup>6</sup> shifts in firms’ business models, and a reporting error that has since been corrected. Overall, 932 firms reported a decrease in clients, 2,147 reported an increase in clients (or were newly registered), and most firms remained within their previously reported client range. The fact remains that, in aggregate, SEC-registered advisers have reported significant client growth over the past five years – over 12 million clients.

**Chart 6: Number of Clients**  
(in millions)



A substantial part of this five-year increase can be attributed to two trends, both related to the rise of automated investment advice models – the provision of automated advice to retirement plan participants and the growth among advisers using websites and/or mobile device apps to reach a greater number of clients with lower investment balances.

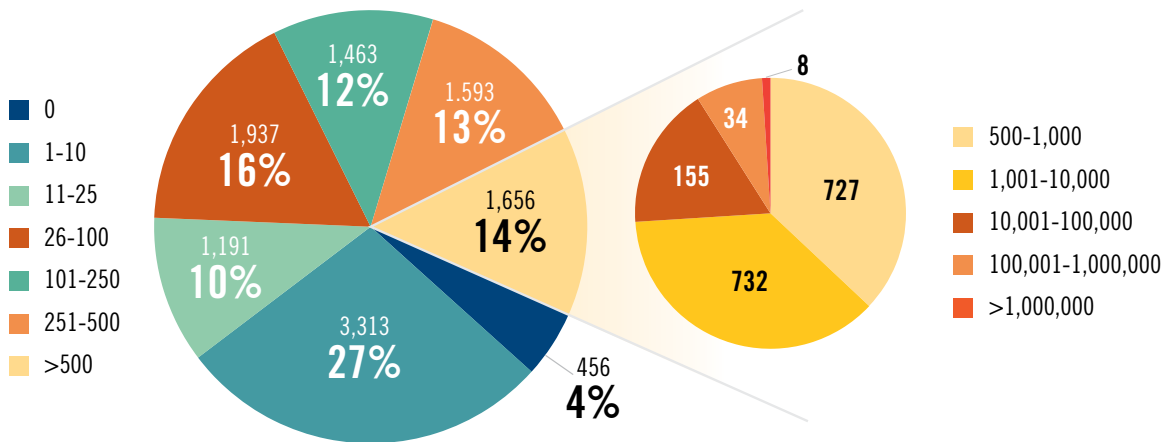
<sup>5</sup> The Form ADV data shows that advisers had 35,636,603 clients, down from 36,401,005 clients in 2016. This data has limitations. For example, for purposes of this section, we only use Form ADV responses that provided a specific number of clients. Advisers are required to provide a specific number only if they have more than 100 clients, and advisers are permitted to round to the nearest 100. As a result, 563 advisers wrote in 100. We have included those responses in the category of 26-100 clients in Chart 7. We note that while the vast majority of firms round to the nearest 100, others appear to provide an exact number. In addition, the number of reported clients for certain advisers may include individuals eligible to receive investment advisory services on the basis of retirement plan participation.

<sup>6</sup> As a result, if one accounts for the methodology adjustment, the large aggregate increase in clients reported last year may have been somewhat overstated, but there has been no actual decrease in aggregate clients year-over-year.

- **Retirement plan participants.** Three advisers, each of which specialize in providing services and advice to retirement plan participants, account for over 32 percent of all reported clients – nearly 11.2 million among them. Defined contribution participant advice is clearly a substantial and important part of the market for investment advice.
- **Web- and app-based advisers.** Although the overall number of clients declined slightly, the gaining popularity of advisers that attract clients with web-based and app-based savings and investment models is evident. Seven of these types of advisers alone collectively reported nearly 1.2 million additional clients in 2017. And, more generally, the number of advisers reporting that they provide advice exclusively through an interactive website rose by nearly 16 percent to 146. On the other hand, a number of “robo” advisers appear to have changed their business model or shifted away from providing investment advice to individual clients (instead providing education or going to a B2B model, for example). This dynamic, evolving landscape of innovating firms may have an impact on the year-over-year comparability of the data.

Although some firms have hundreds of thousands – or even a million – clients, it is still true that most advisers have 100 or fewer clients. As in past years, the median number of clients reported by registered advisers in 2017 is between 26 and 100.

**Chart 7: Advisers by Number of Clients—Most Advisers Have 100 or Fewer Clients**





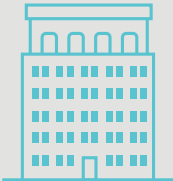
The substantial number of advisers with fewer than 10 clients can be explained, at least in part, by the fact that pooled investment vehicles like mutual funds and private funds count as a single client for reporting purposes. 3,313 advisers, representing 27.2 percent of all advisers, reported having between one and 10 clients. Of these, 2,388 (72.1 percent) also report that more than 75 percent of their RAUM comes from registered investment companies, business development companies, or private funds.

Taking a closer look at the 1,656 advisers that have over 500 clients, the categories of 501-1,000 and 1,001-10,000 are evenly distributed at six percent each. Only eight advisers have over one million clients.

## Advisers by Category and Type of Client

Form ADV requires advisers to report client types by indicating the approximate percentage that each type of client comprises of an adviser's total number of clients. For example, an adviser might indicate that 11 to 25 percent of its clients are high net worth individuals, 26 to 50 percent are charitable organizations, and 26 to 50 percent are pension and profit sharing plans. Form ADV includes 12 identified client types and a catch-all "other" category, and asks for separate responses based on the number of clients and based on the adviser's RAUM.

The 12 specific client types fall into three distinct categories: individuals, pools, and institutions. These categories, along with the estimated portion of the \$70.7 trillion industry-wide RAUM that each type of client represents,<sup>7</sup> are:

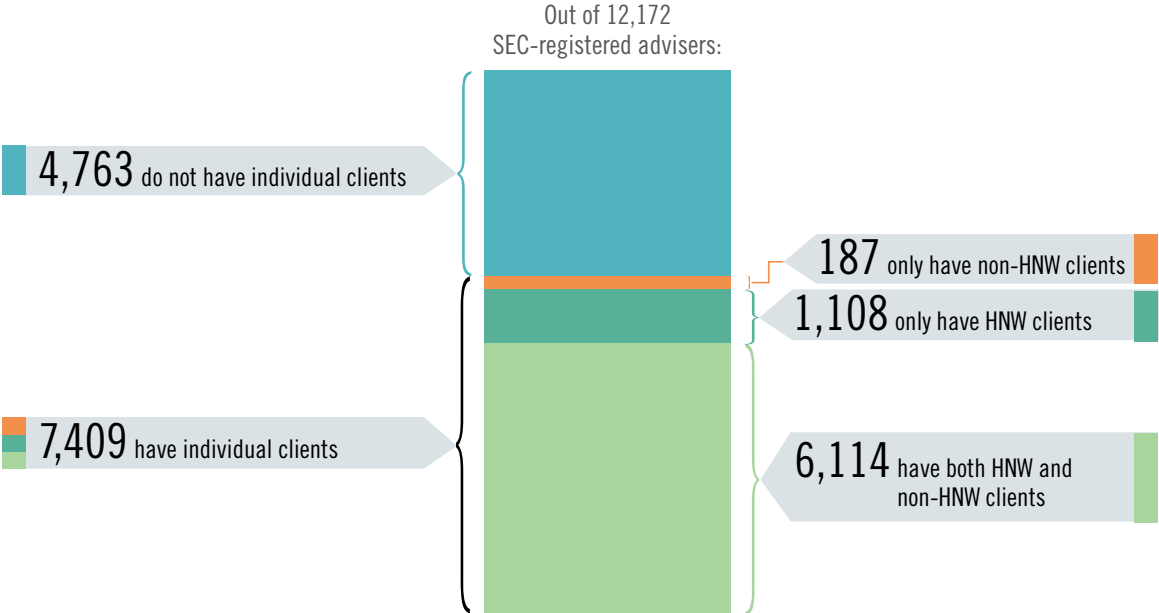
	<p><b>Individuals</b></p> <ul style="list-style-type: none"> <li>• High net worth individuals</li> <li>• Other individuals</li> </ul>	<p>\$5.0 trillion – 7.1%</p> <p>\$3.9 trillion – 5.5%</p>
	<p><b>Pool</b></p> <ul style="list-style-type: none"> <li>• Investment companies</li> <li>• Business development companies</li> <li>• Pooled investment vehicles other than investment companies (private funds)</li> </ul>	<p>\$17.2 trillion – 24.3%</p> <p>\$344.1 billion – 0.5%</p> <p>\$12.8 trillion – 18.1%</p>
	<p><b>Institutions</b></p> <ul style="list-style-type: none"> <li>• Banking or thrift institutions</li> <li>• Pension and profit sharing plans</li> <li>• Charitable organizations</li> <li>• Corporations or other businesses</li> <li>• State or municipal government entities</li> <li>• Other investment advisers</li> <li>• Insurance companies</li> </ul>	<p>\$2.7 trillion – 3.8%</p> <p>\$6.2 trillion – 8.8%</p> <p>\$3.5 trillion – 5.0%</p> <p>\$4.6 trillion – 11.3%</p> <p>\$3.8 trillion – 5.4%</p> <p>\$2.4 trillion – 3.4%</p> <p>\$4.7 trillion – 6.6%</p>

<sup>7</sup> These categories do not include \$3.5 trillion reported as an "other" type of client. It appears that some of the responses included as "other" could have been included in one of the specified category choices.



Individuals remain important to a great many investment advisers and continue to comprise the largest type of advisory clients. 7,409 advisers (60.9 percent) report that they have high net worth clients, non-high net worth clients, or both. Consistent with prior years, the 2017 data indicate that 7,222 (59.3 percent) of SEC-registered advisers have at least some high net worth clients and that 6,301 (51.8 percent) have at least some non-high net worth clients.<sup>8</sup> These two types of client categories listed on Form ADV are the only ones that exceed the 50 percent mark for all advisers. This dominance of individual clients continues despite the Dodd-Frank Act changes that shifted a significant number of smaller advisers to state registration and required SEC registration of certain private fund advisers.

**Chart 8: Most Advisers Serve Individuals**

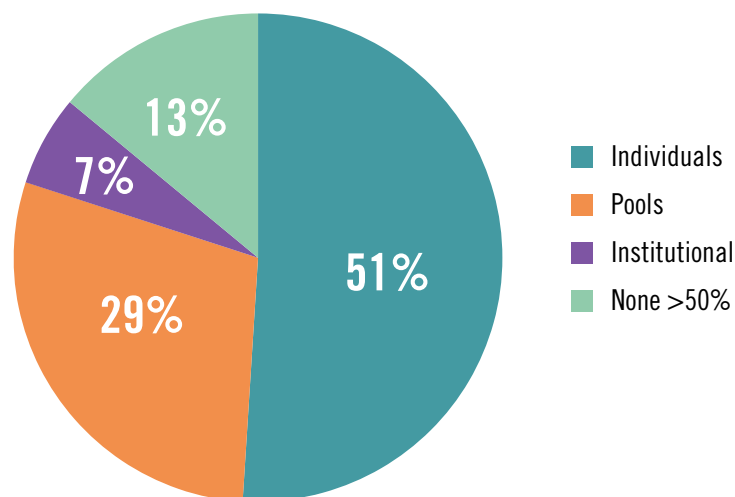


Many advisers have pension clients as well. In 2017, nearly half of all investment advisers (45.5 percent) reported that at least one client is a pension or profit sharing plan. This data relates to advisers to the plans only; it does not include advisers to plan beneficiaries or participants in 401(k) plans or individual retirement accounts.

<sup>8</sup> For purposes of this reporting item, high net worth clients have at least \$1 million managed by the adviser or have a total net worth (including assets held jointly with his or her spouse) exceeding \$2 million (excluding the value of a person’s primary residence for purposes of the net worth test).

Another way to look at this data is by focusing on advisers that report that the majority of their clients are attributable to a single category of client. More than 87 percent of advisers fit this description, gathering the majority of their clients from a single category.

**Chart 9: Almost Nine out of 10 Advisers Have the Majority of their Clients from a Single Category**



The following pages take a closer look at these statistics, focusing on individuals, pools, and institutions.

## A Note on Methodology

This part of *Evolution Revolution* focuses on advisers that report that more than half of their clients are individuals, pools, or institutions. The statistics in this section are a combination of direct and other responses to Form ADV because advisers report ranges of client types: whether none, up to 10 percent, 11 to 25 percent, 26 to 50 percent, 51 to 75 percent, 76 to 99 percent, or 100 percent of the adviser's clients are attributable to any particular client type.

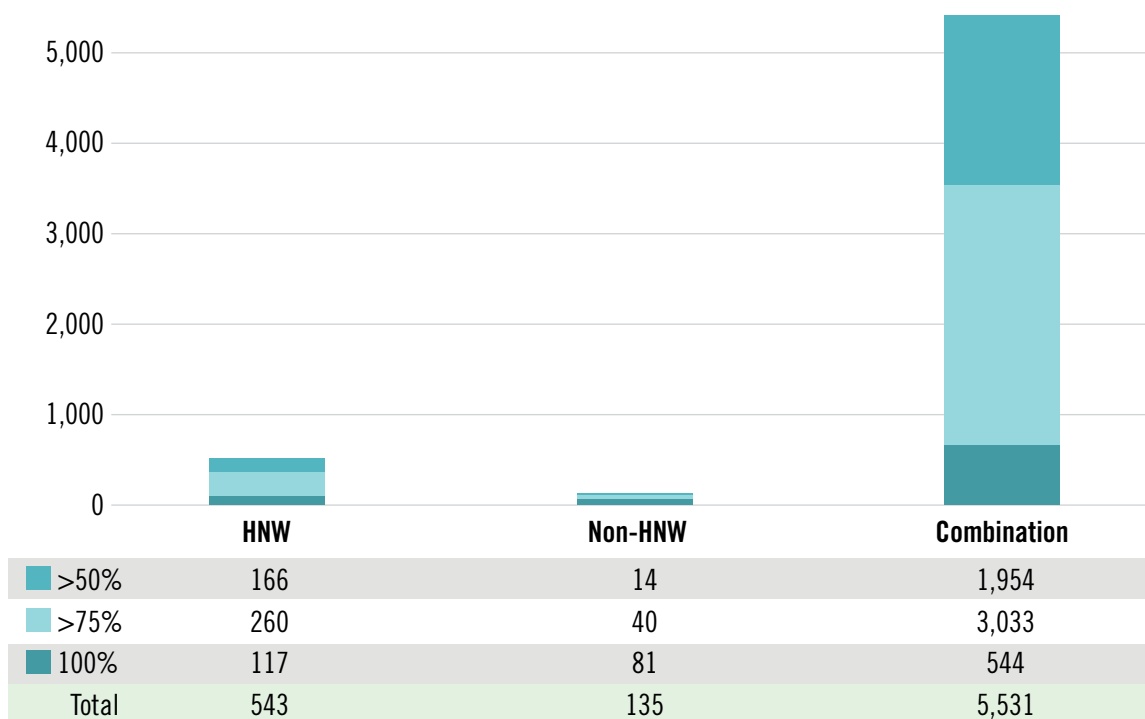
Some of the data is clearly evident from the reported ranges. For example, an adviser might report that 100 percent of its clients are high net worth individuals. Other data is more difficult to discern, such as where an adviser reports a combination of ranges. In order to categorize advisers for purposes of this section, we assumed that each adviser had the lowest possible percentage of clients in each of its reported ranges. For example, an adviser that indicated that 26 to 50 percent of its clients were high net worth individuals was assigned 26 percent to that client type. Advisers were included in the statistics in this section only where it was clear from this process that they had a majority of clients from a particular category.

## A Closer Look at Advisers to Individual Clients

A total of 6,209 advisers report more than half of their clients are individuals. This represents 51 percent of all advisers.

The vast majority of these advisers primarily serve a combination of high net worth (HNW) and non-HNW individuals.<sup>9</sup> Only 678 advisers primarily serve HNW individuals or other individuals, but not both.

Chart 10: Advisers with a Majority of Individual Clients



Note that relatively few of these advisers, however, exclusively serve individual clients. Only 124 advisers reported that 100 percent of their clients were HNW individuals, and only 89 reported that 100 percent were non-HNW individuals.<sup>9</sup> 544 advisers exclusively serve a combination of HNW and non-HNW individual clients.

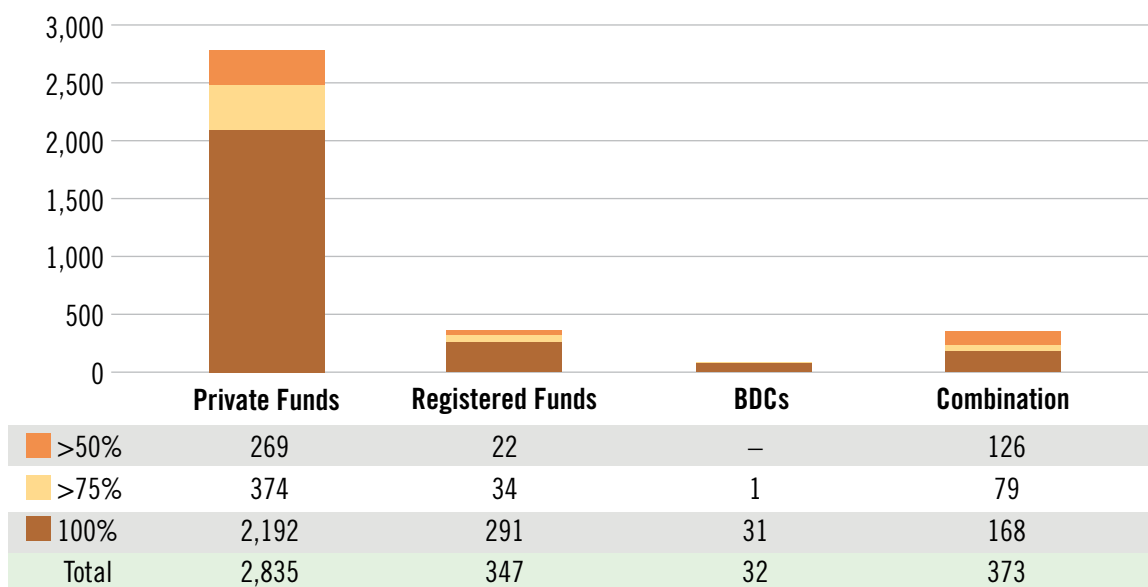
<sup>9</sup> Note that a few advisers report having 100 percent of their clients in two or more categories that are mutually exclusive/add up to over 100 percent. For example, an adviser might report that 100 percent of its clients are HNW individuals and that 100 percent of its clients are private funds. We have excluded those firms where the data is clearly incorrect. As a result, Chart 10 shows that 117 advisers have 100 percent of their clients as HNW individuals although 123 advisers reported such data. Chart 10 also shows that 81 advisers have 100 percent of their clients as non-HNW individuals although 89 reported such data.

## A Closer Look at Advisers to Pools

A total of 3,587 advisers report more than half of their clients are some type of pool, which represents 29.5 percent of all advisers.

2,835 of these primarily serve private funds, 347 primarily serve registered funds, and 40 primarily serve business development companies. An additional 373 advisers reported that some combination of pools accounted for more than 50 percent of their clients.

Chart 11: Advisers with a Majority of Pool Clients



In contrast to the advisers that have a majority of individual clients, many of these advisers exclusively serve pools. In fact, 298 advisers report that 100 percent of their clients are registered funds, 35 report that 100 percent of their clients are business development companies, and 2,195 report that 100 percent of their clients are private funds.<sup>10</sup> 165 more advisers exclusively serve some combination of pools.

Form ADV provides additional detailed data on advisers to private funds. In 2017, 4,574 advisers (37.6 percent) reported advising 34,409 private funds, 25.1 percent of which are funds of funds. The raw numbers of private funds increased slightly from 2016, and as a percentage of the now-larger industry, the percentage also increased slightly (in 2016 there were 4,448 advisers or 37.5 percent, advising 30,342 private funds, 26.1 percent of which were funds of funds).<sup>11</sup>

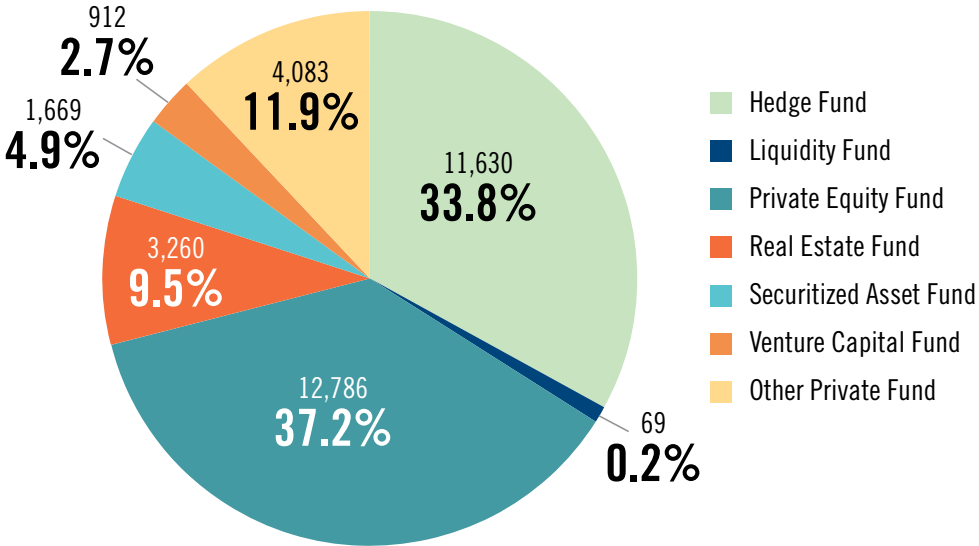
<sup>10</sup> As explained in note 9 above, we have excluded those firms where the data is clearly incorrect. As a result, Chart 11 shows that 291 advisers have 100 percent of their clients as registered funds although 298 advisers reported such data. Chart 11 also shows that 2,195 advisers have 100 percent of their clients as private funds although 2,192 advisers reported such data.

<sup>11</sup> Section 7.B(1) of Schedule D of Form ADV, Part 1 asks private fund advisers questions relating to each fund's type, gross asset value, number of owners, service providers, and a number of other areas. 4,574 advisers reported being "an adviser to any private fund" and 4,354 advisers reported advising at least one private fund. 716 advisers reported advising at least one private fund that is reported by another adviser.

Hedge funds and private equity funds continue to represent the largest portions of the private funds group, comprising 71.0 percent of all reported private funds, with hedge funds making up 33.8% and private equity funds representing 37.2%. While the percentage of hedge funds and private equity funds was exactly equal last year, there is now a divergence, with private equity funds making gains (advisers reported more than 1,000 additional private equity funds) while hedge fund growth is stagnant (the number of reported hedge funds is virtually unchanged). That is not surprising, given recent reports of hedge fund performance issues and closures. This trend may be short-lived, however, as recent data hints of a hedge fund “revival” in Europe.<sup>12</sup>

The total gross asset value of reported private funds is approximately \$11.5 trillion (a 9.0 percent increase above \$10.5 trillion in 2016), more than 16.3 percent of all reported RAUM with an average gross asset value of \$333.9 million. The median gross asset value, on the other hand, is \$50.8 million. The difference between the median and average is attributable to a relatively small number of very large private funds. The number of beneficial owners of private funds also continues to vary widely, with most funds reporting few owners and a small number of funds reporting a very large number of beneficial owners. The median number of beneficial owners is 14, while the average number is 53.

**Chart 12: Private Equity Funds Make Gains While Hedge Fund Growth is Stagnant**



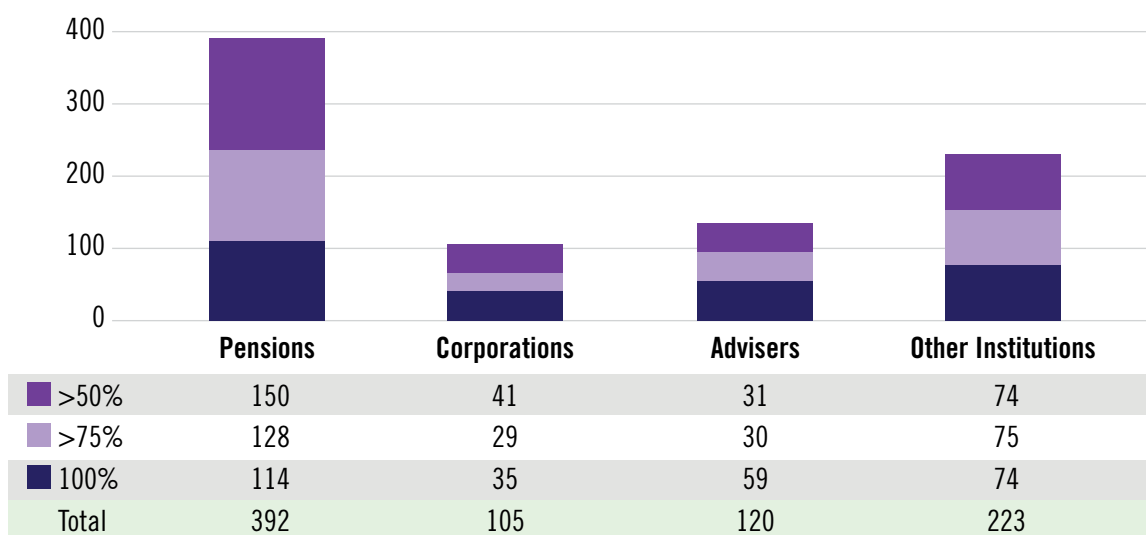
<sup>12</sup> See Nishant Kumar, *Hedge-Fund Revival Quickens as Event-Driven Trades Prosper*, Bloomberg Markets (June 18, 2017), available at [https://www.bloomberg.com/news/articles/2017-06-18/hedge-fund-revival-gathers-pace-as-event-driven-trading-prospers?utm\\_medium=email&utm\\_source=newsletter&utm\\_term=170619&utm\\_campaign=moneystuff](https://www.bloomberg.com/news/articles/2017-06-18/hedge-fund-revival-gathers-pace-as-event-driven-trading-prospers?utm_medium=email&utm_source=newsletter&utm_term=170619&utm_campaign=moneystuff).

## A Closer Look at Advisers to Institutional Clients

A total of 840 advisers report more than half of their clients are institutions. This represents over seven percent of all advisers.

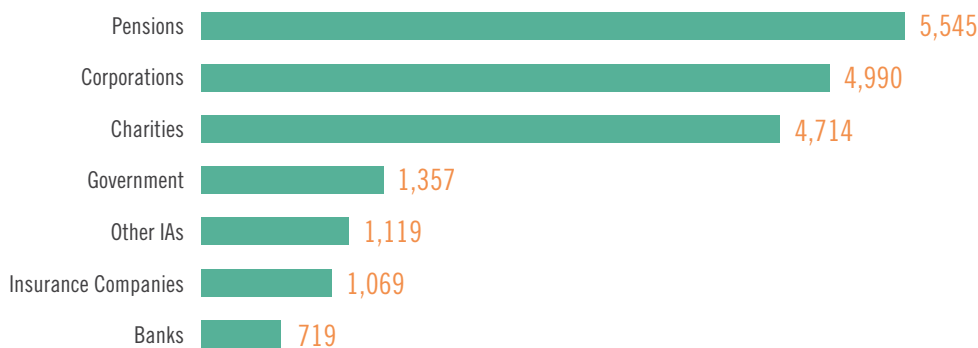
As noted above, nearly half of all advisers serve at least one pension client. The importance of pension clients is evident here as well, as 392 advisers primarily serve pension clients – far more than any other single type of institutional client. 120 advisers primarily serve other investment advisers, and 105 primarily serve corporations. Other institutional clients include banks, insurance companies, charities, and governmental entities.

### Chart 13: Advisers with a Majority of Institutional Clients



An adviser often may have relatively fewer institutional clients with relatively larger investment mandates. Focusing on the number of advisers that report *more than half* of their clients are from a single client category is instructive – but the overall importance of institutional clients becomes clearer by looking at the number of advisers that report *at least one* institutional client of a particular type.

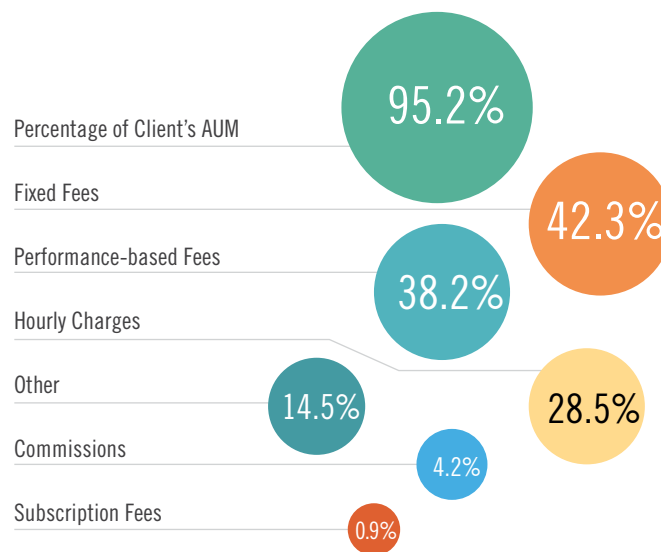
### Chart 14: Advisers with at Least One Institutional Client



# Investment Adviser Compensation

Although advisers may be compensated in a number of ways, asset-based fees continue to dominate in the investment advisory profession. Consistent with our prior reports, 95 percent of advisers indicate that they are compensated based on a percentage of their assets under management. The other types of compensation arrangements largely mirror the percentages seen in recent years. The slight decrease in the number of firms charging commissions likely reflects the decrease in the number of dual registrants discussed below. It is possible that this decrease may become more pronounced next year in response to the Department of Labor's fiduciary rule.

**Chart 15: Asset-Based Fees Continue to Dominate Adviser Compensation Arrangements**



Of the 1,769 (14.6 percent) advisers that report receiving "other" types of compensation arrangements, some of the more common types cited are a percentage of assets under advisement, various fees associated with private funds, 12b-1 fees, referral fees, percentage of client net worth, percentage of plan assets, retainers, selection of other advisers fees, seminar fees, and wrap fees. It appears that some fees included as "other" could have been included in one of the specified answer choices (such as performance-based fees and fixed fees).

Chart 16: Investment Adviser Compensation (Past Three Years)

Category of IA Compensation	2015		2016		2017	
	# of Advisers	% of Advisers	# of Advisers	% of Advisers	# of Advisers	% of Advisers
Percentage of Client's AUM	10,902	95.0%	11,274	95.2%	11,592	95.2%
Hourly Charges	3,224	28.1%	3,345	28.2%	3,475	28.5%
Subscription Fees	116	1.0%	122	1.0%	115	0.9%
Fixed Fees	4,765	41.5%	4,992	42.1%	5,144	42.3%
Commissions	531	4.6%	530	4.5%	506	4.1%
Performance-based Fees	4,415	38.5%	4,540	38.3%	4,651	38.2%
Other	1,667	14.5%	1,731	14.6%	1,769	14.5%

In addition, 4,651 advisers charge performance-based fees. This is not surprising, given that there are 4,574 private fund advisers. Performance-based fees are nearly universal in the private fund context.



# Custody of Client Assets

Form ADV includes a number of questions about the custody of client assets. These questions – and the investment adviser custody rule<sup>13</sup> – appear to continue to be a source of widespread confusion and inconsistent interpretations in the asset management industry. Indeed, a 2013 *Risk Alert* published by the SEC’s Office of Compliance Inspections and Examinations (OCIE) emphasized that non-compliance with the custody rule, as amended in 2009, was one of the most common issues found in routine investment adviser examinations and that, in fact, many advisers failed to realize they even had custody as defined in the rule. These issues persist today.

The confusion stems from the fact that while advisers in general are prohibited from having physical custody of client assets, advisers are also deemed to have custody under certain other circumstances. Many of the questions in Form ADV relate to advisers that are deemed to have custody, although to complicate matters further, advisers that are deemed to have custody for certain types of reasons (such as the ability to deduct fees) are not required to answer certain custody questions<sup>14</sup> on Form ADV and are therefore not reflected in the data we discuss below, unless otherwise indicated. Moreover, the questions in Item 9 of Form ADV, Part 1 are confusing in their use of the terms “you” and “your related persons,” leading us to conclude that some advisers are double counting, and other questions embed double negatives. There also continues to be confusion about the difference between having “custody” and being a “custodian,” resulting in frequent misinterpretations.

Given this backdrop, Chart 17 shows that the number of advisers reporting that they or a related person had or were deemed to have custody increased by 133 (2.6 percent) to 5,289 in 2017 compared to 5,156 in 2016. This number may significantly increase in next year’s edition of *Evolution Revolution* following SEC staff guidance that beginning with the next annual updating amendment after October 1, 2017, an investment adviser should include client assets that are subject to a standing letter of authorization (SLOA) that result in custody in its response to Item 9 of Form ADV.<sup>15</sup> This number may also increase next year in response to the SEC staff’s guidance on inadvertent custody.<sup>16</sup>

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<sup>13</sup> Rule 206(4)-2 under the Advisers Act requires an adviser with custody of client assets (with some exceptions) to: (1) maintain the assets with a “qualified custodian” (generally a bank or broker-dealer); (2) if the adviser opens the custodial account on behalf of the client, provide certain information to the client; (3) have a reasonable belief, after due inquiry, that the qualified custodian sends account statements directly to clients; and (4) undergo an annual surprise exam by an independent public accountant to verify client assets.

<sup>14</sup> According to a March 5, 2014 Form ADV, Item 9 Completion Reminder, advisers that have custody solely because they deduct fees from client accounts would respond “no” in Item 9.A, would likely respond “no” in Items 9.B., and 9.D., and likely would not need to provide information in Items 9.C. or 9.E. However, in Item 9.F., these advisers likely would need to indicate that there is at least one person acting as qualified custodian for their clients in connection with advisory services they provide to clients.

<sup>15</sup> See Investment Adviser Association, SEC No-Action Letter (Feb. 21, 2017), available at <https://www.sec.gov/divisions/investment/noaction/2017/investment-adviser-association-022117-206-4.htm>.

<sup>16</sup> See SEC Division of Investment Management Guidance Update, *Inadvertent Custody: Advisory Contract Versus Custodial Contract Authority* (No. 2017-01), available at <https://www.sec.gov/investment/im-guidance-2017-01.pdf>.

### Chart 17: Custody of Client Assets Remains Consistent

Category	2015		2016		2017	
	# of Advisers	% of Advisers	# of Advisers	% of Advisers	# of Advisers	% of Advisers
Adviser has custody of client cash/bank accounts	3,666	32.0%	3,796	32.0%	3,919	32.2%
Adviser has custody of client securities	3,610	31.5%	3,746	31.6%	3,881	31.9%
Related person(s) has custody of client cash/bank accounts	3,321	28.9%	3,526	29.8%	3,638	29.9%
Related person(s) has custody of client securities	3,290	28.7%	3,477	29.3%	3,584	29.4%
Adviser and/or related person(s) has custody of advisory client assets (answered yes to any of the above)	4,954	43.2%	5,156	43.5%	5,289	43.5%

About a third of investment advisers (4,063 or 33.4 percent) reported having custody of client cash, bank accounts, and/or securities.<sup>17</sup> However, only 71 advisers – about 0.6 percent of all advisers – reported acting as a “qualified custodian” in connection with their advisory services, meaning that they had actual physical custody of client assets. In fact, given the prohibition on having physical custody, each of these advisers is also either a broker-dealer or bank and acts as a custodian in one of those other capacities. The longer-term data shows that this already uncommon practice is becoming increasingly rare. The universe of 71 firms reflects a 4.1 percent decrease in 2017 and a 40.8 percent decrease since 2011, when 120 firms reported acting in such a capacity.<sup>18</sup>

Similarly, the number of advisers reporting that a related person acts as a qualified custodian also continued to trend downward (by 3.1 percent), to 372 advisers in 2017. Of these, 174 firms reported being able to demonstrate that the related person is operationally independent. These firms are not required to obtain a surprise examination for client funds or securities maintained at the related qualified custodian.

It is worth noting that private fund advisers report a high incidence of custody of client assets because the SEC interprets “custody” as acting in a capacity that gives the adviser legal ownership of or access to client funds or securities (e.g., a firm that acts as both adviser and general partner (or has a related person that serves as general partner) to a limited partnership is deemed to have custody). In fact, of advisers that identified themselves as advisers to private funds, 87.2 percent also reported that they or a related person have custody of client assets.

<sup>17</sup> As shown in the first two rows of Chart 17, advisers separately report whether they have custody of (1) client cash or bank accounts and (2) client securities. There is substantial overlap in this data, as nearly all advisers that report having custody of client cash or bank accounts also report having custody of securities.

<sup>18</sup> The SEC’s 2009 amendments to the custody rule required advisers to provide responses to additional questions on custody in their first annual updating amendment to Form ADV after January 1, 2011.

# Employees of Investment Advisory Firms

In 2017, SEC-registered advisers reported a total of 778,002 non-clerical employees, a 0.4 percent decrease in employment from 2016. However, of these employees, 400,163 provide investment advisory services (including research) – a healthy increase of 13,631 over 2016. Three advisers account for 41.8 percent of the decline in employees in 2017, which we understand is a combination of a large insurance company that de-registered as an adviser, having previously reported 13,000 employees who were unrelated to its small advisory business, asset management mergers and acquisitions, and workforce reductions by the two other firms.<sup>19</sup> Interestingly, only the largest firms – those with more than 1,000 employees – experienced a decline in the aggregate number of employees year-over-year.

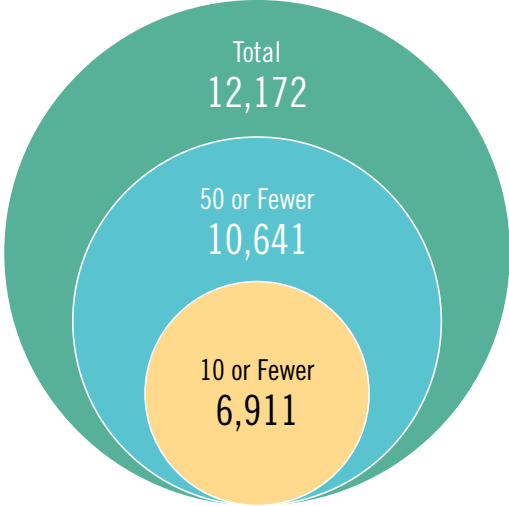
**Chart 18: Investment Adviser Non-Clerical Employees**

Number of Employees	2016		2017		% Change in Aggregate # of Employees
	# of Advisers	Aggregate # of Employees	# of Advisers	Aggregate # of Employees	
1 to 5	3,965	12,321	4,058	12,599	2.26%
6 to 10	2,760	21,155	2,853	22,025	4.11%
11 to 50	3,679	81,701	3,730	81,882	0.22%
51 to 250	1,070	114,465	1,137	119,450	4.36%
251 to 500	170	58,704	181	61,500	4.76%
501 to 1,000	104	74,684	113	81,444	9.05%
More than 1,000	99	418,305	100	399,102	(4.59)%
Total	11,847	781,335	12,172	778,002	(0.43)%
Average	–	66	–	64	–
Median	–	9	–	9	–

<sup>19</sup> The data has some limitations, particularly in the smallest cohort, which includes 104 advisers that reported zero employees. In addition, some job growth may be attributable to firms that were previously state-registered.

The data confirm that the vast majority of SEC-registered investment advisers are small businesses. In fact, 56.8 percent (6,911) reported that they employ 10 or fewer non-clerical employees, and 87.4 percent (10,641) reported that they employ 50 or fewer non-clerical employees. These segments increased by 266 and 237 advisers, respectively, but due to growth across all segments, both of these percentages are the same or very similar to those reported in 2016 (56.8 percent and 87.8 percent). The number of advisers reporting that they have no non-clerical employees stayed essentially flat, going from 105 to 104.

**Chart 19: The Vast Majority of Advisers are Small Businesses with 50 or Fewer Non-Clerical Employees**



SEC-registered investment advisers collectively reported employing 400,163 individuals who perform investment advisory functions and 386,413 employees who are also registered representatives of a broker-dealer. The number of employees in these categories increased by 3.5 percent and 1.5 percent, respectively, and in addition, the percentage of advisers that reported no registered representative (8,655) increased by 3.7 percent from 70.4 percent to 71.1 percent in 2017.

Chart 20: Activities by Investment Adviser Employees

Number of Employees	# of advisers with employees who:				
	Perform investment advisory functions	Are registered representatives of a broker-dealer	Are registered with more than 1 state as investment adviser representatives	Are registered with more than 1 state as investment adviser representatives for another adviser	Are licensed agents of an insurance company
0	212	8,655	5,694	10,959	9,295
1 to 5	6,144	1,845	4,161	919	1,974
6 to 10	2,508	534	1,110	135	320
11 to 50	2,540	718	870	113	330
51 to 250	597	252	213	37	142
251 to 500	78	58	49	4	37
501 to 1,000	44	46	28	2	28
More than 1,000	49	64	47	3	46
Total	400,163	386,413	282,027	19,818	247,420
Average	33	32	23	2	20
Median	5	0	1	0	0

Although 212 advisers report that they have no employees who perform investment advisory functions, it is likely that those persons are shared with, and technically employed by, an affiliate of the firm.

# Other Characteristics of Investment Advisory Firms

## Other Business Activities

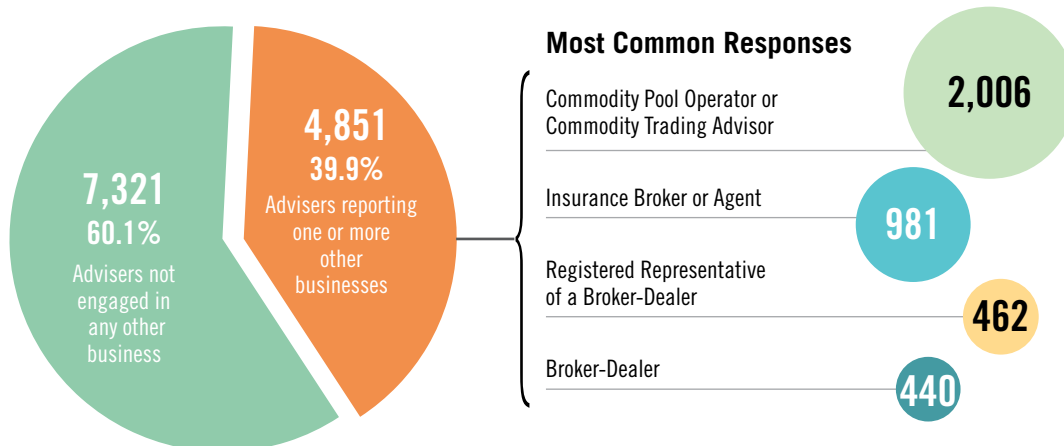
As in years past, most advisers are primarily focused on providing investment advice to clients. In 2017, 7,321 advisers (60.1 percent) reported that they are not actively engaged in any other business other than rendering investment advice about securities, a proportion that is relatively unchanged compared to 2016.

Of those advisers that are actively engaged in another business activity, the most common is to be engaged in business as a commodity pool operator (CPO) or commodity trading advisor (CTA). Over the last six years, this category has grown by 99.8 percent, from 1,004 in 2012 to 2,006 this year, which remains more than twice the number in the next closest category.<sup>20</sup> In 2017, 16.5 percent (2,006) of advisers reported being engaged in business as a CPO or CTA, an increase of 35. However, the growth in the number of advisers is leveling off with only a 2.7 percent increase year-over-year.

The number of dual registrants (entities that are both SEC-registered investment advisers and SEC-registered broker-dealers) fell by one percent to 440 (from 444 in 2016), but the number of advisers actively engaged in business as a registered representative of a broker-dealer fell at a much faster rate of 4.7 percent to 462 (from 485 in 2016), reversing the longer term growth trend evident in past periods. For more on dual registrants, see “Financial Industry Affiliations” below.

The number of advisers that are also an insurance broker or agent slightly increased (up only 0.4 percent from 977 to 981) but remains the second most common other business activity (8 percent). Based on 2017 filings, certain business activities are distinctly more popular than others. In fact, four of the 14 categories – CPO/CTA, broker-dealer, registered representative of a broker-dealer, and insurance broker or agent – collectively represent more than 83 percent of all reported Other Business Activities of investment advisers in 2017.

**Chart 21: Most Advisers Focus on Providing Investment Advice About Securities**



<sup>20</sup> This trend is likely the result of (1) the Dodd-Frank Act’s inclusion of “swaps” in the definition of commodity pool; and (2) the 2011 clarification in Form ADV that this question applies to both registered and exempt CPOs/CTAs.

## Financial Industry Affiliations

Form ADV requires investment advisers to disclose information relating to their affiliations and activities with other persons within the financial industry. The net percentage change relating to affiliations and activities with other persons within the financial industry from 2016 to 2017 is negligible – a decline of 1.4 percent. All of these percentages are similar to those reported last year.

**Chart 22: Financial Industry Affiliations**

Related person is:	Number of Advisers	Percentage of Advisers
Sponsor, general partner, managing member (or equivalent) of pooled investment vehicles	4,548	37.4%
Other investment adviser (including financial planners)	4,508	37.0%
Broker-dealer, municipal securities dealer, or government securities broker or dealer	2,446	20.1%
Commodity pool operator/trading advisor (whether registered or exempt)	2,209	18.1%
Insurance company or agency	2,009	16.5%
Accountant or accounting firm	819	6.7%
Banking or thrift institution	800	6.6%
Trust company	791	6.5%
Sponsor of syndicator or limited partnerships (or equivalent), excluding pooled investment vehicles	657	5.4%
Pension Consultant	634	5.2%
Real estate broker or dealer	559	4.6%
Lawyer or Law firm	465	3.8%
Registered municipal advisor	318	2.6%
Futures commission merchant	211	1.7%
Registered security-based swap dealer	79	0.6%
Major security-based swap participant	9	0.1%

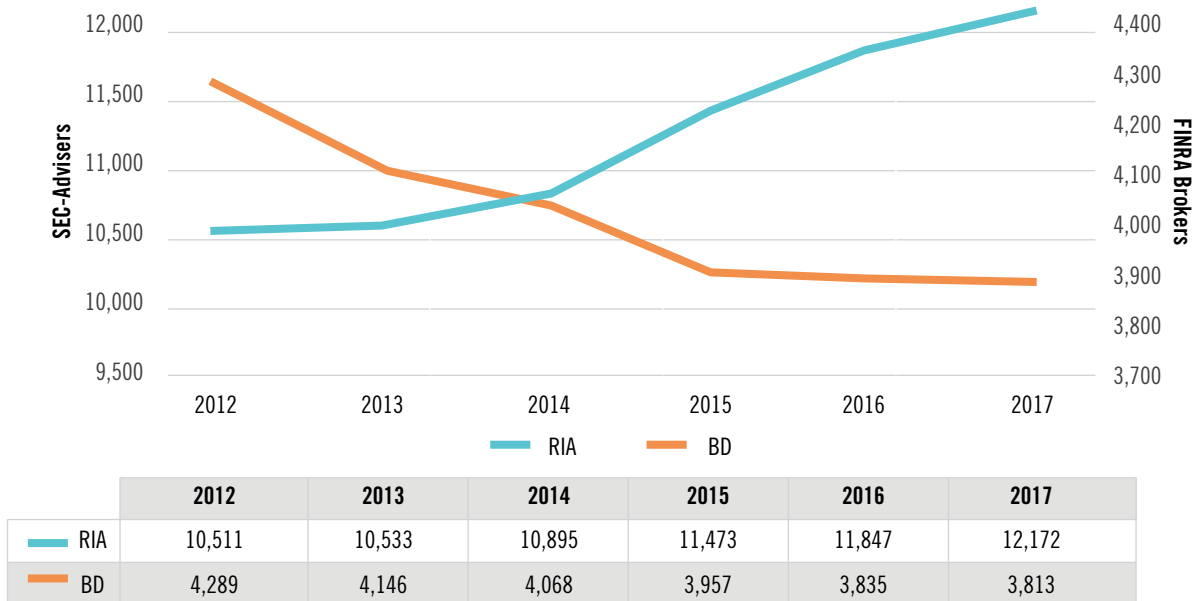
The most common affiliation reported in 2017 among investment advisers is with sponsors, general partners, or managing members (or equivalent) of pooled investment vehicles, with 4,548 (37.4 percent) reporting such an affiliation, and gaining 3.5 percent (154) since 2016. Since 2015, this category of affiliation has increased by 9.5 percent, edging out the percentage of advisers affiliated with other investment advisers in 2017. With 4,574 (37 percent) advisers reporting such an affiliation, this represents a 2.8 percent gain since 2016 and a 5.2 percent increase since 2015.

Included in the numbers cited under “Other Business Activities” and “Financial Industry Affiliations” are broker-dealer relationships, where investment advisers are either dually registered as broker-dealers or are affiliated (through common ownership and/or control) with broker-dealers.

A small percentage of advisers, only 440 in total (3.6 percent) are dually registered (those entities registered both as SEC-registered investment advisers and SEC/FINRA broker-dealers). This year, the number of dual registrants only dropped one percent, continuing the downward trend from past years. However, the decline is negligible compared to last year’s drop of three percent and suggests a leveling off.

Those advisers affiliated with broker-dealers increased again slightly this year to 2,446, continuing the trend from previous years (2,381 in 2015 and 2,438 in 2016). At the same time, we continue to see the number of FINRA member broker-dealers on a steady decline. Over the last five years, membership in the SRO has fallen eight percent from 4,146 to 3,813, though the decline in the number and rate of year-over-year change has slowed significantly in recent years. This is a stark contrast to the growth in the number of SEC-registered investment advisers, which has increased by 15.8 percent over the same 5-year period.

**Chart 23: Number of Advisers Rises While Number of Broker-Dealers Falls**



Interestingly, as of March 2017, the number of securities registered representatives has reversed its five-year growth trend, dropping slightly from 635,902 in 2016 to 633,822.<sup>21</sup> More than half of these securities registered representatives (approximately 60 percent) are employed by SEC-registered investment advisers (SEC-registered advisers reported employing 386,413 registered representatives in 2017). This signifies a 1.5 percent increase in the number of registered representatives employed by registered investment advisers (380,853 in 2016).<sup>22</sup>

<sup>21</sup> Source: <https://www.finra.org/newsroom/statistics>.

<sup>22</sup> Robert Cook, Chief Executive Officer of FINRA, recently said “There has been a decline in the number of [broker-dealer] firms, less of a decline in the number of registered reps ... [FINRA is attempting to understand] what’s going on in the industry — are firms just dropping away or are smaller firms wanting to associate with a larger firm?” Cook was also quoted as saying that the shift of broker-dealer assets to the advisory side is “a trend we’re seeing.” Melanie Waddell, *FINRA Watching Falling Number of BDs*, *CEO Cook Says*, ThinkAdvisor (May 17, 2017), available at <http://www.thinkadvisor.com/2017/05/17/finra-watching-falling-number-of-bds-ceo-cook-says>.

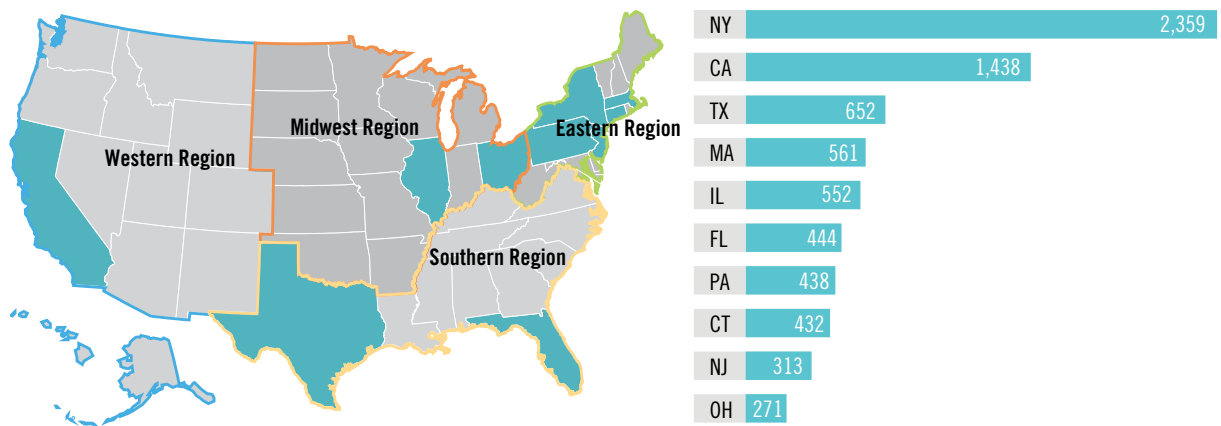


# Location of Investment Advisers

Investment advisers continue to find states such as New York, California, Texas, Massachusetts, and Illinois to be desirable locations for their main offices, ostensibly resulting from proximity to financial markets, growing financial hubs, and large population centers. Bordering states such as Pennsylvania, Connecticut, and New Jersey and have also found favor with investment advisers, likely because of the combination of proximity to New York financial markets, affluent suburbs, and local specialization.

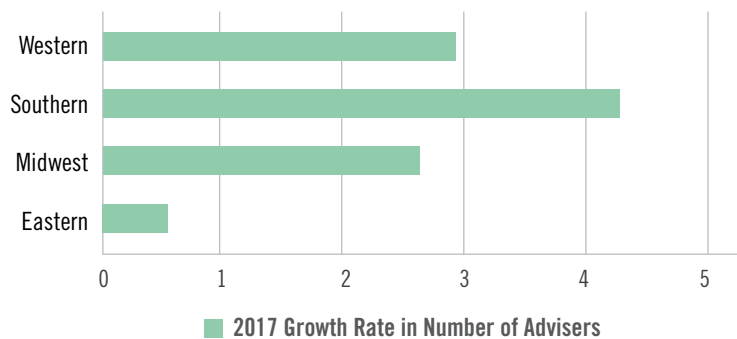
The top ten states for SEC-registered advisers remain unchanged from 2016 and 2015. Indeed, the top three states remained unchanged, while Massachusetts and Florida increased their ranks.

**Chart 24: Top Ten States for Advisers**



On a regional basis, the Southern region showed the strongest growth, an increase of 4.3 percent from 2016, and was the only region with no single state losing advisers. In addition to the perennially strong growth demonstrated by Texas and Florida, the Carolinas were a highlight, with North Carolina growing at 5.2 percent and South Carolina growing at 12.5 percent. The Western and Midwest regions experienced respectable growth, at 2.9 percent and 2.7 percent, respectively. While still reporting growth of 0.6 percent, the Eastern region was a distant fourth.

**Chart 25: Southern Region Outpaces the Nation in Growth**



As in recent years, investment advisers located outside of the United States continue to seek SEC registration. The number of such foreign advisers increased 7.7 percent since 2016, following an 8.5 percent increase the previous year.

Investment advisers are still predominately located in or near the major cities and financial centers of the United States, although the data reveals the trend is toward increasing geographic diversity. It is, perhaps, too soon to draw conclusions, but future patterns may reveal that such trends resulted from technological advances that have made it feasible to locate in any area, from current or former broker-dealers joining the ranks of investment advisers in the wake of the DOL Fiduciary Rule, or from demographic or migration patterns generally.

Whether the advent of the robo-tech era brings unintended consequences commensurate with these advantages is an open question. The emergence of bionic advisers somewhat lessens the dilemma of clients who are gaining the benefits of convenience at the expense of reduced personal attention, but does not completely eliminate them. Either the industry will innovate in order to allow clients to experience the best of both worlds, or clients will have to adjust to the so-called new normal. Client demand will largely determine the path forward.

## Disciplinary Information

It is difficult to draw meaningful conclusions from the disciplinary disclosure information provided in Form ADV, Part 1. For example, Form ADV, Part 1, Item 11 contains many “true or false” questions relating to a fairly broad set of questions relating to disclosable disciplinary events by the adviser, its employees, officers, directors and advisory affiliates. Determining the details contained in the disciplinary disclosure reporting pages for Form ADV, Part 1, Item 11 requires delving deep into the specifics of each disclosure event to have a clear understanding of what was involved. Also, the information required to be disclosed is provided for the advisory firm and its employees, officers, directors, and advisory affiliates for the past 10 years, whether or not these persons or entities were affiliated with the reporting firm during that time. However, firms can specify whether any of the events reported involve the firm or its supervised persons. In addition, the same disciplinary event at one firm may be reported by multiple separate affiliates, and the same disciplinary event may generate affirmative answers to several different questions.

Subject to these limitations, we make the following observations:

- 10,517 of registered investment advisers (86.4 percent) reported no disciplinary history at all, which is comparable to last year, when 10,273 advisers (86.7 percent) reported no disciplinary history.
- Only one percent of all advisers reported that they or their affiliates had been charged with a felony. Of the 125 firms that did so, only 60 (0.49 percent of all advisers) reported having been convicted or having pled guilty or nolo contendere (“no contest”) to the charges in court.
- Repeating last year’s reporting in the category, once again 164 firms or advisory affiliates (1.3 percent) reported that the SEC or the Commodity Futures Trading Commission (CFTC) found them to have made a false statement or omission; 542 firms (4.5 percent) reported that they have been involved in a violation of SEC or CFTC regulations or statutes, representing a 4.8 percent increase from 2016. Only 15 firms reported that they or an advisory affiliate have been found by the SEC or CFTC to have been the cause of an investment-related business having its authorization to conduct business denied, suspended, revoked, or restricted, which is a 6.3 percent decrease from the previous year.

- 537 firms or advisory affiliates (4.4 percent) reported that the SEC or the CFTC imposed a civil money penalty on the adviser or its affiliate or were ordered to cease and desist from an activity; although this is a 3.7 percent increase from 2017, when considering percentage of all advisers, it remained a flat 4.4 percent year-over-year.

Of the 1,655 advisers reporting at least one disciplinary event, 811 advisers (49.0 percent) attributed the disclosure events to an affiliate and not directly to the adviser or its supervised persons.

## Explanation of Report Data

*Evolution Revolution* and its findings are based on Form ADV, Part 1 data filed by all SEC-registered investment advisers as of April 10, 2017. Advisers are required to file specific information electronically using the Investment Adviser Registration Depository (IARD) system.

Approximately 17,500 investment advisers are registered with the states.<sup>23</sup> This report focuses solely on SEC-registered investment advisers.

Form ADV, Part 1 has significant limitations and anomalies. Please consult the text of Form ADV (available on the SEC's website at <http://www.sec.gov/about/forms/formadv.pdf>) for a more thorough understanding of the underlying data included in this report.

The IAA and NRS have independently tabulated all data in this report. Whenever a number is rounded, it is rounded from the original data source. This method of rounding creates more accurate percentages, but may create complementary percentages that do not sum to 100 percent. Unless otherwise stated in this report, a null response to a "Yes or No" question is considered a "No," and a null response to any other question is not included in the data set.

When obvious errors have been found in the reported data, we have made certain corrections or omissions to avoid skewed results.

Several items in Form ADV, Part 1 are commonly misunderstood and answers are misreported. For example, Item 1.0 asks "Did you have \$1 billion or more in assets on the last day of your most recent fiscal year?" meaning the adviser's balance sheet assets, but many registrants respond based on their RAUM. Other areas that are commonly misinterpreted include how to calculate RAUM, custody, and disciplinary history questions.

The Form ADV, Part 1 data underlying the findings in *2017 Evolution Revolution* and additional information is contained in the report's Appendix, which is available online at <https://www.investmentadviser.org> (<https://goo.gl/CWg3qy>) or <http://www.nrs-inc.com/About-Us/White-Papers/>.



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