The rapid expansion of the financial services industry over the past two decades has given rise to a unique hybrid enterprise: the independent trust company. With roots in the departments of commercial banks, independent trust companies occupy an interesting space in the investment management community, positioned somewhere between a family office and an institutional asset manager. As a result, there really is no one-size-fits-all definition of an independent trust company, and recognition of the particular attributes of independent trust companies is significant to understanding their value.

As high net worth clients migrated from the traditional sales mentality investment approach of brokerage firms, the idea of independent investment advisors began to gain steam. The financial advisory business model transformed from cold calling staffs paid by transaction-based commissions to unbiased and credentialed professionals paid on the basis of assets under management by client bases built primarily on referrals. The popularity of Registered Investment Advisors, or RIAs, centered on the fiduciary responsibility associated with such practices, as well as the greater degree of accessibility and high touch nature of the business operations, which often originated in smaller family office operations. Additionally, the smaller size of independent advisors allowed for greater innovation and more specialized services.

The number of total investment advisors registered with the SEC expanded from 6,360 in 1999 to 8,614 in 2005 (excluding all investment advisors only required to register with their respective states). This number expanded by an additional 1,676 in 2006; however, much of this growth was largely attributable to SEC rule modifications requiring hedge fund managers to register as investment advisors. More than 90% of all RIAs reported less than 50 employees.1

Assets managed by independent RIAs more than doubled from 2000 to 2006, while their share of investable assets expanded from 9.0% in 2003 to 14% in March of 2007. A comparison of the market share allocations of U.S. investable assets at year end 2003 and March 31, 2007 is shown in Figure One and Figure Two.2,3

Total assets under management (AUM) reported by SEC-registered investment advisors reached an all-time high of $31.4 trillion as of April 2006. Assets held in discretionary accounts grew 18% from $24.3 trillion in 2005 to $28.6 trillion in 2006. Figure Three illustrates the growth in discretionary assets reported by investment advisors in all AUM categories and total assets under management.  

<table>
<thead>
<tr>
<th>Category of IA by Assets Under Management (AUM)</th>
<th>2006 AUM</th>
<th>2005 AUM</th>
<th>% Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>&gt;$100 Billion</td>
<td>$12.927</td>
<td>$11.197</td>
<td>15.5%</td>
</tr>
<tr>
<td>$50-100 Billion</td>
<td>$4.092</td>
<td>$3.338</td>
<td>22.6%</td>
</tr>
<tr>
<td>$10-50 Billion</td>
<td>$6.535</td>
<td>$5.599</td>
<td>16.7%</td>
</tr>
<tr>
<td>$5-10 Billion</td>
<td>$1.503</td>
<td>$1.354</td>
<td>11.0%</td>
</tr>
<tr>
<td>$1-5 Billion</td>
<td>$2.309</td>
<td>$1.779</td>
<td>29.8%</td>
</tr>
<tr>
<td>$100 Million to 1 Billion</td>
<td>$1.110</td>
<td>$0.871</td>
<td>27.4%</td>
</tr>
<tr>
<td>$25-100 Million</td>
<td>$0.166</td>
<td>$0.138</td>
<td>20.3%</td>
</tr>
<tr>
<td>&lt;$25 Million</td>
<td>$0.007</td>
<td>$0.007</td>
<td>0.0%</td>
</tr>
<tr>
<td>Total</td>
<td>$28.649</td>
<td>$24.283</td>
<td>18.0%</td>
</tr>
</tbody>
</table>

In spite of all the changes taking place in recent years, there remains some debate regarding whether the independent trust industry is mature or evolving. On the one hand, the concept of providing comprehensive wealth management within the context of highly personalized customer service is not new, but on the other, the level of sophistication expected across the spectrum of trust services has never been higher and, indeed, seems to be growing at a rapid pace.

**RULES OF THUMB**

There are both formal and informal approaches to value, and while we at Mercer Capital are obviously more attuned to the former we do not ignore the latter. Industry participants often consider the value of investment managers in general, and independent trust companies in particular, using broad-brush metrics referred to as “rules-of-thumb.” Such measures admittedly exist for a reason, but cannot begin to address the facts and circumstances specific to a given enterprise.

---

4 Ibid
As an example of this, industry participants might consider asset managers as being worth some percentage of assets under management. At one time, investment manager valuations were thought to gravitate toward about 2% of assets under management.

Understanding why such "rules of thumb" exist is a good way to avoid putting too much faith in them. During periods of consolidation, buyers often believe that the customer base of an acquisition candidate can be integrated with the acquiring firm's existing managed assets to generate additional profits in line with industry expectations. So if the investment management industry is priced at, say, 15x earnings and profit margins are 20%, the resulting valuation multiple of revenue is 3.0x. If revenue is generated by fees priced at about 67 basis points of assets under management, then the implied valuation is about 2% of asset under management. Note, however, all the "ifs" required to make the 2% of AUM rule of thumb work …

Kristin C. Beckman  
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