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# Is Your Broker-Dealer a Screaming Eagle or a Box Wine?

By Jonathan Henschen, CFS

In the wine industry, few captivate a cult following quite like Screaming Eagle Cabernet. If you're not familiar with Screaming Eagle Cabernet, it's a legendary cult wine produced by Screaming Eagle Winery in the Oakville region of Napa Valley in California.

Screaming Eagle Wines are sold by subscription only, with no tasting rooms or ability to visit the winery. The label's extreme popularity has caused a waiting list just to get on the subscription list, and each vintage is pre-sold. A bottle of Screaming Eagle will set you back \$750, with subscribers often times flipping their purchase for \$1,500 or higher. (The winery has been known to drop subscribers if they get wind that you're immediately reselling their wine.) In 2001, a six liter bottle of '92 Screaming Eagle set a world record for the highest price ever paid for a single bottle of wine through the Napa Valley Wine Auction, selling for \$650,000.

For this kind of money you have to wonder what kind of experience a wine can offer to justify such a demand. Here was one explanation from a wine aficionado:



*"It was as though we'd been sucking on the world's most perfect blackberry... one single, perfect blackberry... and, at that moment, exactly 70 minutes after we had opened and decanted the bottle, the fruit had burst open, with dramatic, intense, ripe tastes of earth, minerals, acidity and sunshine. In the world of wine-lovers, this is what you always hope for but never expect: a brief, ephemeral moment of perfection."*

While most don't expect an ephemeral moment from a broker-dealer, it is your experiences—of relationship, service, technology, belonging and feeling appreciated—that determine if your broker-dealer has a cult following that separates them from the competition. For the few firms that have achieved this cult status, we have found that, like cult-status wines, "Culture, Purity and Technology" are the traits that set them apart because they do them all and they do them well.

## Culture: Learning the Business From the Ground Up

Screaming Eagle and other California cult wines share three common threads. First, they are all located in Napa Valley because the single most important factor in producing a great wine is soil, soil, soil. Second, these wineries are managed by wine school graduates, with the University of California at Davis (UCD) being the most common. Heidi Barrett, Screaming Eagle's renowned winemaker, graduated from UCD in 1980 with a B.S. Degree in Fermentation Science. She cut her teeth working at numerous wineries, improving her craft along the way until she started making wine at Screaming Eagle in 1992. The third common thread is output. Cult wineries such as Screaming Eagle produce only 600–700 cases per year, while their commercial counterparts produce in the tens of thousands.

Cult-status broker-dealers also share several common trends. Broker-dealers with the best cultures are nearly always headed by a founder or president who was themselves a registered rep, learning and applying their craft over the years before starting their own broker-dealer. When a broker-dealer president has walked in the shoes of the representatives, it brings a connection that you rarely see when top management has backgrounds such as accounting or compliance.

In 2012, a top rep leaving a large broker-dealer was quoted as saying, "My broker-dealer doesn't understand broker-dealer culture. They understand business but not culture." The president of that particular firm didn't have a registered representative background, so it came as no surprise to hear of the cultural disconnect.

As firms grow, maintaining a highly functional culture becomes increasingly difficult. One cult-following, mid-sized firm we place advisors with is keenly aware of this so they set a growth cap of 500 representatives in order to preserve the high touch qualities that attracted advisors to the firm

in the first place. They also tell prospective representatives that their compliance department doesn't cater to the lowest common denominator because they don't have a lower denominator—they simply don't bring on reps unless they have \$200,000 or more in production.

A firm's success and growth can be their greatest downfall if management starts to operate out of an Ivory Tower, granting access sparingly or only to the highest producers. Mark Cuban, entrepreneur and owner of the Dallas Mavericks, recalled his first job out of college with Mellon Bank, where he tried a bottom up approach to communicating with management. He started a "Rookie Club" where he'd invite senior executives to a happy hour to talk to younger employees. He also started a newsletter that discussed current projects. His boss called him into the office, ripping into him for going over his head, threatening to crush him unless he backed away. Cuban left Mellon shortly thereafter, realizing they were more concerned with their power structure and egos than making improvements. I've also witnessed a broker-dealer president who belittled and practically interrogated reps during recruiting visits, which is a time when he should be trying to woo them to join the firm. Recruiting is difficult enough without a bridge burning leadership mentality that turns off potential prospects. The intoxicating effects of power and success can turn a broker-dealer's culture upside down as representatives' contributions take a back seat.

To be certain, growth makes maintaining a highly functional culture increasingly difficult. If you want to have the ear of management, quality relationships with back office staff and a sense of belonging, a broker-dealer's growth has the potential of being your worst enemy.

## **Purity: Maintaining the Integrity of the Original**

Cult winemakers, like broker-dealers, are diligent about keeping external forces from ruining what they've painstakingly built. The greatest threat to wine is a yeast called *Brettanomyces* or "Brett." Brett is a mischievous foe that can be difficult to recognize before it's too late. Left unchecked, Brett can become overpowering, manifesting itself as a sweaty horse saddle character, or barnyard stall (the Wine Aroma Wheel has other similarly fragrant descriptions, such as cat pee and diaper), dramatically altering the palate and the wine's bouquet. The best way to combat Brett is through sanitation and a pristine cellar. Without this due diligence, entire wineries may need to rebuild in order to eradicate the troublesome Brett.

Purity for cult-status broker-dealers starts with the recruiting process as prospects are filtered through compliance for problematic compliance patterns, questionable outside business activities or credit issues caused by personal negligence. With FINRA passing out fines for anything and everything, while at the same time drilling down on every aspect of our business, broker-dealers have no choice but to scrutinize more details than they have in the past. Like Brett, misguided representatives can bring a firm down, so filtering out such candidates at the onset preserves the integrity of the firm as it was built.

The wild cards for compliance departments are reps that are concealing outside business activities and ponzi schemes. Even the best of firms can be blindsided by such deceit. For cult-following broker-dealers, besides vigilant compliance and audit procedures a focus on representatives with quality backgrounds on every level, a financial planning approach to investing and larger asset base representatives helps to deter the likelihood of such occurrences. The smaller culture and close relationships at cult-status broker-dealers also makes it much more likely to uncover illicit activities before they mushroom into something more serious.

## **Technology: Advances Improve Quality and Productivity**

The last 10 years has been a technological renaissance for wine with the use of stainless steel tanks that allow temperature-controlled fermentations, new presses, advanced filtration techniques as well as a deeper understanding of the chemistry behind quality wine making. Winemakers are not just craftsmen but enologists, with university degrees in wine science. The result has been an increase in quality for nearly all wines, with many 91–92 point rated wines now available for as little as \$15–\$20. This was rare 10 years ago.

Technology has brought the same renaissance to the broker-dealer community, as all broker-dealers have benefited from technology improvements. Ten years ago consolidated client statements were available at only a few broker-dealers. Now, they are commonplace. Having a centralized, web-based paperless technology platform was equally rare, while today it's quickly becoming the norm. Cult-status broker-dealers may choose to set themselves apart by developing their own technologies rather than outsourcing to bring greater accuracy and customization that outsourced technologies typically don't offer.

Cult-following broker-dealers realize that in today's broker-dealer environment, technology is critical to regulatory and competitive success with proper execution on all three levels—rep, operational and compliance. The greatest pressures come from regulators requiring broker-dealers to have technology in place to increase their rigor in monitoring their representatives, with the greatest scrutiny directed at the suitability and sales practices with products such as alternative investments and variable annuities. Broker-dealers also need to disseminate "Know Your Customer" data, which has greater inclusive data requirements.

To compete, cult-status broker-dealers are bringing together technology to cater to the hybrid model, offering multiple platforms—be it Pershing, NFS, TD Ameritrade or Schwab—with broker-dealer generated administration at value pricing. A growing trend is the ability to offer outside advisory platforms under the broker-dealers corporate RIA while traditionally reps could only work with outside advisory platforms if they had their own RIA.

This frees the rep from the burden and liability of setting up and maintaining their own RIA. Broker-dealer generated administration, as opposed to reliance on their clearing firm for billing, statements and performance reporting is also a growing trend. In-house performance reporting utilizing companies such as Orion brings greater performance reporting accuracy along with very broad customization abilities.

Bringing in cutting-edge technology is always at the forefront for cult-status broker-dealers—by necessity. Often times they complement technology with elements of practice management, which helps representatives to better understand how to utilize the technology to make their practice more efficient and save time. After all, the best technology is the technology you need to spend the least amount of time managing.

When we interview representatives, we frequently hear, “I want a firm that leaves me alone,” which for some of these reps is quite literal. For them, a box-wine broker-dealer that simply processes business and supervises them works out just fine. They are not looking for culture or relationship and are content with being an island. As production increases, you generally find the opposite to be true as a representative’s broker-dealer is looked at as a partner in their success. That explains why cult-status broker-dealers tend to

have unusually high average production per rep. Once representatives experience a cult-status broker-dealer, we’ve found that if they do need to make a change of broker-dealers, they want to find another firm with similar cult status. Author T.C. Boyle summed it up best when he said, “Wine is like sushi to the degree that once you’ve had the best, you really have no tolerance for that which is not so good.”



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