Introducing the Virtual RIA

By Kerry Pechter *Tue, Sep 27, 2011*

Internet start-up Personal Capital is out to prove that mutual funds and face-to-face financial advice are obsolete. (At center, CEO Bill Harris, with Jim Del Favero, VP, product management (seated) and Ehsan Lavassani, engineering director.

With just $27 million in venture capital, less than $500,000 in assets under management and only a handful of Series 65 advisors in its San Francisco call center, Personal Capital Corp. hardly seems like a serious threat to Vanguard, Fidelity and other giants of the financial industry.

But the entrepreneurs behind this Silicon Valley startup believe that by offering the convenience of financial account aggregation (think Mint.com or Pageonce.com) and the expertise of Series 65 phone reps on one web platform, they can make sophisticated wealth management scalable and affordable for tens of millions of currently under-advised "mass-affluent" Americans.

Personal Capital's management team isn't made up of newbies. It includes CEO Bill Harris, the former CEO of Intuit (which bought Mint.com last year) and CEO of PayPal; strategist Rob Foregger, co-founder of EverBank and former president of Personal Trust Services at Fidelity Investments, Jay Shah, former CIO of E-Loan, and Jim Del Favero, former group products manager for Quicken.

"We're a scalable Registered Investment Advisor. That's our framework. We're trying to empower the investor and give a level personalization that hasn't existed in financial services. You have personalized radio stations, you have LinkedIn, you have social networks, and you can even have shirts tailored online. Why not do true personalization for financial services?" Foregger told RIJ this week.

After talking to Personal Capital managers, I was a little skeptical. Will people hand over the usernames and passwords of their mutual fund and bank accounts to a start-up? (Apparently they will: Mint.com has six million users.) And don't companies like Vanguard and Fidelity already offer opportunities for account aggregation and advice? Yes, but only to their shareholders.

After looking at Personal Capital's website and exploring their services a bit, I was a little surprised not to any functionalities directly related to retirement drawdown strategies. If near-retirees have the most savings, and if they're worried about retirement income, shouldn't a new service give a nod to decumulation planning? Personal Capital doesn't have that—at least, not yet.

No one doubts, however, that financial clutter plagues millions of people and that the financial advice industry fails to reach millions of middle-income people with $100,000 or more in household savings. That's the niche that Personal Capital wants to fill.

How it works

At Personal Capital's website, members have access to a two-tier service. There's an free tier that includes account aggregation and other services and an asset management services that costs from up to 115 basis points a year.

On the first tier, customers upload the usernames and passwords of their financial accounts into an aggregation engine powered by Yodlee to create a dashboard for tracking all of their money at banks and brokerages.

"Transaction modeling, daily e-mail alerts and military-grade security" also comes free, as does a financial check-up and access to "financial analysis and objective advice" from a salaried call-center employee with perhaps a Series 65 securities license.

"The dashboard is free, the vast majority of functions are free, and the vast majority of clients wont be paying us anything, they'll just be using the dashboard to track their finances and make decisions on their own," Foregger said.

But "Aggregation is only one component," he added. "We aggregate, we append third-party data, we provide valuable insights and advice, and we present in a easy to use, but sophisticated UI [user interface]. It's very challenging, and not done well by many."

A more sophisticated second tier of service is available for a maximum all-in cost of 115 basis points (a 95 bps wrap fee plus an ETF-sized investment expense ratio) for accounts from $100,000 to $250,000. It costs 90 bps to manage the next $250,000, 85 bps for the next $500,000, 80 bps on the next $4 million, and 75 bps on amounts above $5 million.

The fee covers the services of a "professional advisor," the creation of a diversified separately managed account (SMA) from existing assets, "continuous rebalancing and tax optimization" and a cash management account.

Personal Capital calls the SMA a "Personal Fund." According to Craig Birk, the firm's portfolio manager, each fund will include up to 60 stocks and will be designed to offer broad global diversification across companies of all sizes and sectors. The funds will be somewhat customized according to Personal Strategy—the "way wealthy families and endowments manage their money." Birk spent 11 years at Fisher Investments. Personal Capital clears its trades through Penson Financial Services.

The folks behind Personal Choice believe that the mass-customized SMA will replace the mutual fund for many mass-affluent investors. "We're in the first or second inning of the post-mutual fund era," Foregger told RIJ. "Mutual funds were great for their day. Mainframe technology helped spur that. But we're at the next level, where technological can create truly personalized solutions, as opposed to mutual funds."

Foregger added: "In the traditional model, you meet with an advisor and you push a shoebox full of confirmations across the table and say, 'Figure this out for me.' In our high-tech and high-touch model, you add a new account, you put in your user name and password, hit continue, and full data on any particular account appears."

Competitive landscape

One competitor to Personal Choice is Manhattan-based Betterment.com, but the two have significant differences. Launched to the public by Jonathan Stein and Eli Broverman in 2009, Betterment allows people to connect their checking accounts to an investment account consisting of index funds.

The clients themselves determine the balance between equity and fixed income investments by the manipulating a simple slider bar. Betterment doesn't aggregate or provide personalized advice, but it does offer automatic account rebalancing—so that investors pick up bargains rather than lock-in losses.

"Personal Capital's philosophy is, 'We'll give you tools but you need one our human advisors. We believe that if people want a human advisor, they'll go to someone they know personally," said Stein, who noted that when he was a graduate student at Columbia Business School a visiting speaker named John Bogle encouraged him to pursue Betterment.

Fidelity Investments has an account aggregation service called Full View where Fidelity investors can aggregate their investment, retirement, banking, loan, mortgage and credit card accounts. People with at least $50,000 at Fidelity can get advice over the phone for free, and Fidelity also offers managed accounts and mutual fund advisory services, according to a spokesman.

Vanguard offers something similar with its over-$50,000 a Vanguard Vantage Account, which according to the company website "lets you consolidate and manage your investment and cash management needs in one convenient place" along with the ability to trade stocks, bonds, CDs, non-Vanguard mutual funds. Cash management services are included.

Two assumptions

For Personal Capital to succeed, people have to be willing to entrust it with the passwords and usernames of their most valuable financial accounts. But will they? The people at Yodlee told RIJ that that problem is why Yodlee, a now widely used aggregation engine, didn't become a retail business.

"[That's] "the primary reason Yodlee decided not to pursue a B2C [business-to-consumer] strategy when we started in 1999 but rather to leverage the trust of the bank brands to offer these services to consumers with the context of secure online banking," said Melanie Flanagan, a press contact at Yodlee.

"But we currently have more than 30 million consumers using services powered-by-Yodlee at both banks and non-banks, so if the value proposition is high enough and the trust/security/privacy is clearly communicated and made a top priority, I think the majority of consumers are now past that fear," she added.

The successes of Mint.com and PageOnce.com, which have an estimated five million users between them, shows that the public accepts the security of account aggregation, said Foregger. To reinforce that acceptance, Personal Capital touts its "military-grade" security.

The aggregation companies are also assuming that the IT people at large companies keep doing their jobs. The startups are piggy-backing, in a real sense, on more than a decade of frenetic work and investment by the larger financial services firms to create high-capacity, high-speed, high-security, high-reliability, real time account maintenance and administration systems. Those systems are the shoulders that the likes of Personal Capital and Mint.com stand on.