Why the PE that helped take LPL public now controls Edelman Financial and plans to invest more heavily

by Lisa Shidler

Brooke's Note: In the game of soccer, players pass endlessly in hopes of getting off a clean shot. And one failed shot does not mean the next one won't get put past the goalie. Ric Edelman can take heart. He has taken his company public once only to take it private and bring on a super-partner in David Bach. Now he's angling for an IPO again presumably by courting LPL's IPO maestro. The half empty view of all this financial engineering is that Ric is creating a blur of activity to distract from the killer issue at hand of trying to find a successor for a company where he does so extraordinarily much, as radio host, seminar host, advisor, CEO and dog owner. Or you can look at it that Ric is just that irrepressible soccer player angling for a shot, safe in the knowledge that he only needs to get lucky once. In the meantime, as one of the biggest RIAs, he has the defense back on its heels.

The prime mover behind LPL Financial's initial public offering is now the majority private-equity owner of Edelman Financial Services LLC.

Hellman & Friedman LLC, which has invested a staggering $35 billion in its 29 years of existence, purchased a block of equity formerly held by Lee Equity Partners, which until now had been the majority private-equity owner of Edelman. Hellman & Friedman now owns the firm in partnership with Edelman's senior management team and with Lee Equity. CEO Ric Edelman is the still the firm's largest individual shareholder.

New York-based Lee Equity Partners had begun to act as a drag on Edelman's efforts to grow — a consequence of its lame duck status in the classical PE term, according to Edelman.

"Lee was more interested in focusing on its exit rather than having the company make long-term investments," he says. "It's not a criticism of them, just the nature of the life cycle of a private-equity firm." See: Ric Edelman strikes a private-equity deal that subtracts $2 million in expenses — now let the after-bidding begin.

Lee Equity took Edelman Financial private in 2012 for $8.85 per share in cash or $265 million. But Lee Equity, which only managed about $1 billion when it bought Edelman, wasn't exactly deep into that lifecycle, says Steve Levitt, principal of Park Sutton Advisors.

No Lee retreat

"The Edelman acquisition, because of the growth of Ric's business, has been a home-run for Lee Equity Partners. Ric's business has been phenomenally successful and a sale or IPO was expected, in my view. Lee only invested 3.5 years ago. I imagine this represented an attractive opportunity for Lee to take some chips off the table."

Still, back in 2012, press reports listed Edelman Financial's AUM at $17 billion. It is now listed at $15 billion.

Benjamin Hochberg, a partner at Lee Equities, is adamant about his firm's confidence in Edelman Financial.

"We aren't getting out. We were looking for a partner to help Ric grow in the next phase and we thought Hellman & Friedman would be a great partner," he says. "We were comfortable making long-term investments but we thought having another partner in the company for these investments made a lot of sense for everyone."

Supersize me

Ric Edelman: We need to over time institutionalize me. It can be done and has been done.

The move comes amid an all-out, but thus far unsuccessful, institutional effort to replace Edelman as CEO and as key man of the Fairfax, Va.-based firm. In August, David Bach, author of 11 best-selling books and CEO of FinishRich Media, resigned as vice-chairperson of the firm after efforts to install him as heir-apparent came a cropper. The company has also switched search firms. See: Ric Edelman and David Bach go their own ways after super-partnership dissolves.

Edelman acknowledges that his company needs to bring on additional media-savvy executives.

“We need to over time institutionalize me,” he says. “It can be done and has been done. The best example is Charles Schwab. There are companies who have done it well and some who have done it well and others who haven’t. We need to learn from their mistakes.” See: What a close reading of Barron’s cover story on Walt Bettinger reveals .

High rollers

If its track record for backing major players in the RIA industry is any indication, Hellman & Friedman may well be the PE firm to get the job done.

Charles “Chip” Roame, managing partner of Tiburon Strategic Advisors, is particularly impressed by its managing director, Allen Thorpe.

“Allen is super-smart and also knows the financial advisor business well. He invested a substantial sum in LPL Financial and was on their board for their fastest growth years. I think Allen will bring an institutional mindset and rigorous financial focus.” See: LPL to Wall Street types: We’re in phase three .

Thorpe’s stops along the way to Hellman & Friedman include Stanford University, Harvard Business School (where he was a Baker Scholar) and Bain & Co.

The San Francisco-based private-equity firm, founded in 1984, has made numerous financial investments over the years, particularly focusing on financial services and professional services firms. It invested in Franklin Resources, a division of Franklin Templeton, in 1992, selling it in 1997.

In 2005, Hellman & Friedman, along with Texas Pacific Group, took a 60% stake of San Diego, Boston and Charlotte, N.C.-based LPL Financial, which became a publicly traded company on 2010. See: What to make of LPL nearing a successful — but scaled back — IPO.

In 2013, Hellman & Friedman sold the remainder of its overall LPL holdings, 12.6 million shares of common stock, to the institutions that funded the original PE investments. See: As LPL Financial braces for a share sell-off and loss of two directors, a Citi analyst says it’ll be good.

Terms of the deal were not disclosed.

Low-capital intensive

H&F is part of a blue-chip strata of private-equity investing firms that invest about $300 million to $500 million in a firm, says Levitt, founder of Park Sutton Advisors, an RIA M&A firm in New York.

“This is a very big deal. They are very successful with their investments.” See: Why exactly private equity firms are dumping money into IBDs at a time when many are going bust.

This has been a busy year with numerous private-equity deals involving giant RIAs.

“It has been a very active year for M&A in general and wealth management is a very attractive, low capital-intensive business — with client demographics on its side given an aging U.S. population,” Levitt writes in an email. “Ric’s business is one of the most successful RIAs in the United States using media and direct marketing [as does] groups like Wealth Enhancement Group, Mutual Fund Store, and Fisher Investments. See: Almost lost in the robo shuffle, Personal Capital, in its 'special category,' is winning as told by an overlooked metric: revenues.

IPO again?

Chip Roame: Edelman is well on its way to institutionalizing its business ... I am an optimist here.

Edelman Financial manages approximately $15 billion for more than 28,000 clients in 41 offices across the country and online. It has been ranked the No. 1 Independent Financial Advisor in the nation by Barron’s. See: How Ric Edelman’s bounty of radio and TV leads pushed his $12-billion RIA from Microsoft to GoldMine to Salentica.

Although this is the latest push for Edelman, 57, to find a successful long-term partner, he says there’s been a method to the firm’s toggling between public and private status.

“Our original transaction in 2005 was success and Lee Equity was very successful and we expect this to be our most successful one of all. This reason we did each one in sequence was very simple. When we did the deal with Sanders Morris Harris they were public and we became the subsidiary and in 2009, I took over the firm and didn’t want them to be public anymore. It didn’t make sense for it to be public and that’s why we did the deal with Lee. Lee’s original time-line is three years and this was on the shorter-end of the time-line. They’re investment has done well and they wanted to monetize it.” See: Encouraged by early success in New York, Edelman ramps up office openings.

Is an IPO is in Edelman’s near future? It’s still too soon to say, he says.

“That’s many years out and that’s one possible outcome and there are many other strategic outcomes. We’re not terribly worried about five years from now. We’re continuing to serve clients and we’ll be growing aggressively and adding hundreds of advisors in the next several years.” See: How Ric Edelman manages to bring on 4,500 new clients each year by force of personality while diminishing key-man risk at the same time.

Fulfilled potential

Edelman sees his firm ramping up growth under the new owners. “We’ve not been able to achieve all we’re capable of and now we'll be able to do so."

He is particularly excited about H&F's history in the financial services field.

"I love that fact because it proves they are intimately familiar with registered investment advisors and the kind of organization we are and the kind of services we provide. This will be a tremendous help to us. Their experience, knowledge and resources are going to be put to good use with our firm," he says in a statement.

"Edelman is well on its way to institutionalizing its business," Roame says. "I believe it has something like 115 financial planners. I am an optimist here."