ENVESTNET, INC.
Form 10-K
March 01, 2019

UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

ýANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
For the year ended December 31, 2018
¨TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934
Commission file number 001-34835

Envestnet, Inc.
(Exact name of registrant as specified in its charter)

Delaware	20-1409613
(State or other jurisdiction of incorporation or organization)	(I.R.S Employer Identification No.)
35 East Wacker Drive, Suite 2400, Chicago, IL	60601
(Address of principal executive offices)	(Zip Code)

Registrant's telephone number, including area code:
(312) 827-2800

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class:	Name of Each Exchange on Which Registered:
Common stock, par value $0.005 per share	NYSE

Securities registered pursuant to Section 12(g) of the Act:
None

Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes ý No ¨

Indicate by check mark whether the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act. Yes ¨ No ý

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes ý No ¨

Indicate by check mark whether the registrant has submitted electronically every Interactive Data File required to be submitted pursuant to Rule 405 of Regulation S-T (232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit such files). Yes ý No ¨

Indicate by check mark if disclosure of delinquent filers pursuant to item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrants knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ¨

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer," "smaller reporting company," and "emerging growth company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer	ý	Accelerated filer	¨
Non-accelerated filer	¨	Smaller reporting company	¨
Emerging growth company	¨		

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act. Yes ¨ No ý

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Act). Yes ¨ No ý

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Aggregate market value of registrant's common stock held by non-affiliates of the registrant, based upon the closing price of a share of the registrant's common stock on June 30, 2018 as reported on The New York Stock Exchange on that date: $1,507,416,864. For purposes of this calculation, shares of common stock held by (i) persons holding more than 5% of the outstanding shares of stock, and (ii) officers and directors of the registrant, as of June 30, 2018, are excluded in that such persons may be deemed to be affiliates. This determination is not necessarily conclusive of affiliate status.

As of February 22, 2019, 48,149,473 shares of the common stock with a par value of $0.005 per share were outstanding.

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Forward Looking Statements

Unless the context requires otherwise, the words "Envestnet," "the Company," "we," "us" and "our" are references to Envestnet, Inc. and its subsidiaries as a whole.

This annual report on Form 10 K contains forward looking statements regarding future events and our future results within the meaning of the Private Securities Litigation Reform Act of 1995, Section 27A of the Securities Act of 1933, as amended (the "Securities Act") and Section 21E of the Securities Exchange Act of 1934, as amended (the "Exchange Act"). These forward looking statements include, in particular, statements about our plans, strategies and prospects under the heading "Management's Discussion and Analysis of Financial Condition and Results of Operations". These statements are based on our current expectations and projections about future events and are identified by terminology such as "anticipate," "believe," "continue," "could," "estimate," "expect," "expected," "intend," "will," "may," or negative of those terms or variations of such words, and similar expressions are intended to identify such forward looking statements. In addition, any statements that refer to projections of our future financial performance, our anticipated growth and trends in our business and other characteristics of future events or circumstances are forward looking statements. These forward looking statements involve risks and uncertainties. Important factors that could cause actual results to differ materially from the forward looking statements we make in this annual report are set forth in Part I under "Risk Factors"; accordingly, investors should not place undue reliance upon our forward looking statements. Factors that may cause our actual results to differ materially from our forward looking statements may include, among others, statements relating to:

- difficulty in sustaining rapid revenue growth, which may place significant demands on our administrative, operational and financial resources;
- our ability to successfully identify potential acquisition candidates, complete acquisitions and successfully integrate acquired companies;
- our ability to successfully execute the conversion of clients' assets from their technology platform to our technology platforms in a timely and accurate manner;
- the amount of our debt and our ability to service our debt;
- the variability of our revenue from period to period;
- the targeting of some of our sales efforts at large financial institutions and large Internet services companies which prolongs sales cycles, requires substantial upfront sales costs and results in less predictability in completing some of our sales;
- the deployment of our solutions by customers and potential delays and risks inherent in the process;
- the competitiveness of our solutions and services as compared to those of others;
- the concentration of our revenues from the delivery of our solutions and services to clients in the financial services industry;
- our reliance on a limited number of clients for a material portion of our revenue;
- the impact of fluctuations in market conditions and interest rates on the demand for our products and services and the value of assets under management or administration;
- changes in investing patterns on the assets on which we derive revenue;
- the renegotiation of fees by our clients;
- our ability to introduce new solutions and services;
- our ability to maintain the security and integrity of our systems and facilities and to maintain the privacy of personal information and potential liabilities for data security breaches;
- the effect of privacy regulations on how we operate our business;
- liabilities associated with potential, perceived or actual breaches of fiduciary duties and/or conflicts of interest;
- failure of our solutions, services or systems, or those of third parties on which we rely, to work properly;
- the failure of our insurance to adequately protect us;
- our dependence on our senior management team;
- our ability to recruit and retain qualified employees;
- regulatory compliance failures;

- changes in laws and regulations, including tax laws and regulations;
- adverse judicial or regulatory proceedings against us;
- the failure to protect our intellectual property rights;
- potential claims by third parties for infringement or their intellectual property rights;
- risks associated with our international operations;
- the impact of fluctuations in interest rates and turmoil in market conditions on our cost of borrowing and access to additional capital;
- the impact of fluctuations in foreign currency exchange rates;

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- the uncertainty of the application and interpretation of certain tax laws;
- changes in accounting principles and standards;
- issuances of additional shares of common stock or issuances of shares of preferred stock or convertible securities on our existing stockholders;
- general economic conditions, political and regulatory conditions; and
- management’s response to these factors.

More information on these important factors that could cause actual results to differ materially from the forward looking statements we make in this annual report are set forth in Part I under “Risk Factors.” In addition, there may be other factors of which we are presently unaware or that we currently deem immaterial that could cause our actual results to be materially different from the results referenced in the forward looking statements. All forward looking statements contained in this annual report and documents incorporated herein by reference are qualified in their entirety by this cautionary statement. Forward looking statements speak only as of the date they are made, and we do not intend to update or otherwise revise the forward looking statements to reflect events or circumstances after the date of this annual report or to reflect the occurrence of unanticipated events, except as required by applicable law. If we do update one or more forward looking statements, no inference should be made that we will make additional updates with respect to those or other forward looking statements.

Although we believe that our plans, intentions and expectations are reasonable, we may not achieve our plans, intentions or expectations.

You should read this annual report on Form 10 K completely and with the understanding that our actual future results, levels of activity, performance and achievements may be different from what we expect and that these differences may be material. We qualify all of our forward looking statements by these cautionary statements.

The following discussion and analysis should also be read along with our consolidated financial statements and the related notes included elsewhere in this annual report. Except for the historical information contained herein, this discussion contains forward looking statements that involve risks and uncertainties. Actual results could differ materially from those discussed below.

Except where we have otherwise indicated or the context otherwise requires, dollar amounts presented in this Form 10 K are in thousands, except for the Report of Independent Registered Public Accounting Firm, Exhibits and per share amounts.

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Item 1. Business

General

Envestnet is a leading provider of intelligent systems for wealth management and financial wellness. Envestnet's unified technology enhances advisor productivity and strengthens the wealth management process. Envestnet empowers enterprises and advisors to more fully understand their clients and deliver better outcomes.

More than 3,500 companies, including 15 of the 20 largest U.S. banks, 43 of the 50 largest wealth management and brokerage firms, over 500 of the largest registered investment advisers ("RIA"), and hundreds of Internet services companies, leverage Envestnet technology and services. Envestnet solutions enhance knowledge of the client, accelerate client on-boarding, improve client digital experiences, and help drive better outcomes for enterprises, advisors and their clients.

Founded in 1999, Envestnet has been a leader in helping transform wealth management, working towards its goal of building a holistic financial wellness network that supports enterprises, advisors and their clients.

Through a combination of platform enhancements, partnerships and acquisitions, Envestnet uniquely provides a financial network connecting software, services and data, delivering better intelligence and enabling its customers to drive better outcomes.

Envestnet serves clients from its headquarters based in Chicago, Illinois, as well as other locations throughout the United States, India and other international locations.

Segments

Envestnet is organized around two primary, complementary business segments. Financial information about each business segment is contained in "Note 21 – Segment Information" to the notes to consolidated financial statements in Part II, Item 8. Our business segments are as follows:

- Envestnet – a leading provider of unified wealth management software and services to empower financial advisors and institutions.

- Envestnet | Yodlee – a leading data aggregation and data intelligence platform powering dynamic, cloud-based innovation for digital financial services.

Envestnet Segment

Envestnet empowers financial advisors at broker-dealers, banks and RIAs with all the tools they require to deliver holistic wealth management to their end clients. In addition, the firm provides advisors with practice management support so that they can grow their practices and operate more efficiently. At the end of 2018, Envestnet's platform assets grew to approximately $2 trillion in nearly 11 million accounts overseen by more than 96 thousand advisors. Services provided to advisors include: financial planning, risk assessment tools, investment strategies and solutions, asset allocation models, research, portfolio construction, proposal generation and paperwork preparation, model management and account rebalancing, account monitoring, customized fee billing, overlay services covering asset allocation, tax management and socially responsible investing, aggregated multi custodian performance reporting and communication tools, plus data analytics. Envestnet has access to a wide range of leading third party asset custodians.

We offer these solutions principally through the following product/services suites:

- Envestnet | Enterprise – provides an end-to-end open architecture wealth management platform, through which advisors can construct portfolios for clients. It begins with aggregated household data which then leads to a financial plan, asset allocation, investment strategy, portfolio management, rebalancing and performance reporting. Advisors have access to over 19,100 investment products. Envestnet | Enterprise also sells data aggregation and reporting, data analytics and digital advice capabilities to customers.

- Envestnet | Tamarac™ provides leading trading, rebalancing, portfolio accounting, performance reporting and client relationship management software, principally to high end RIAs.

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- Envestnet | Retirement Solutions (“ERS”) offers a comprehensive suite of services for advisor-sold retirement plans. Leveraging integrated technology, ERS addresses the regulatory, data, and investment needs of retirement plans and delivers the information holistically.

- Envestnet | PMC®, or Portfolio Management Consultants (“PMC”) – provides research and consulting services to assist advisors in creating investment solutions for their clients. These solutions include nearly 4,000 vetted third party managed account products, multi-manager portfolios, fund strategist portfolios, as well as over 1,200 proprietary products, such as quantitative portfolios and fund strategist portfolios. PMC also offers an overlay service, which includes patented portfolio overlay and tax optimization services.

As the tables below indicate, Envestnet’s wealth management solutions have experienced steady and significant growth over the last several years. We believe this growth is attributable to secular trends in the wealth management industry, the uniqueness and comprehensiveness of our products, as well as acquisitions.

The following charts show growth in the number of advisors, accounts and assets supported by Envestnet, distinguishing those metrics between assets under management or administration (“AUM/A”) and subscription. Beginning March 31, 2018 and for periods thereafter, subscription metrics include assets, accounts and advisors associated with Envestnet | Tamarac performance reporting, where applicable. Previously, Envestnet | Tamarac’s metrics were limited to those associated with its rebalancer solution. Prior period metrics have been conformed to the new definition in the tables shown below:

AUM/A & Subscription Advisors

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AUM/A & Subscription Accounts
(in thousands)
AUM/A & Subscription
($ in billions)

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Envestnet | Yodlee Segment

Envestnet | Yodlee is a leading data aggregation and data intelligence platform. As an artificial intelligence ("AI") and data specialist, Envestnet | Yodlee gathers, refines and aggregates a massive set of end-user permissioned transaction level data, combines them with financial applications, reports, market research analysis, and application programming interfaces ("APIs") for its customers.

More than 1,100 financial institutions, financial technology innovators and financial advisory firms, including 15 of the 20 largest U.S. banks, subscribe to the Envestnet | Yodlee platform to underpin personalized financial apps and services for over 23 million paid subscribers.

Envestnet | Yodlee serves two main customer groups: financial institutions ("FI") and financial technology innovators, which we refer to as Yodlee Interactive ("YI") customers.

- The Financial Institutions group provides customers with secure access to open APIs, end-user facing applications powered by our platform and APIs ("FinApps"), and reports. Customers receive end user-permissioned transaction data elements that we aggregate and cleanse. Envestnet | Yodlee also enables customers to develop their own applications through its open APIs, which deliver secure data, money movement solutions, and other functionality. FinApps can be subscribed to individually or in combinations that include personal financial management, wealth management, card, payments and small-medium business solutions. They are targeted at the retail financial, wealth management, small business, card, lenders, and other financial services sectors. These FinApps help consumers and small businesses simplify and manage their finances, review their financial accounts, track their spending, calculate their net worth, and perform a variety of other activities. For example, Yodlee's Expense FinApp helps consumers track their spending, and a Payroll FinApp from a third party helps small businesses process their payroll. The suite of reports is designed to supplement traditional credit reports by utilizing consumer permissioned aggregated data from over 20,000 sources, including banking, investment, loan, and credit card information.

- The Yodlee Interactive group enables customers to develop new applications and enhance existing solutions. These customers operate in a number of sub-vertical markets, including wealth management, personal financial management, small business accounting, small business lending and authentication. They use the Envestnet | Yodlee platform to build solutions that leverage our open APIs and access to a large end user base. In addition to aggregated transaction-level account data elements, we provide YI customers with secure access to account verification, money movement and risk assessment tools via our APIs. We play a critical role in transferring innovation from financial technology innovators to financial institutions. For example, YI customers use Yodlee applications to provide working capital to small businesses online; personalized financial management, planning and advisory services; e-commerce payment solutions; and online accounting systems for small businesses. We provide access to our solutions across multiple channels, including web, tablet and mobile.

Both FI and YI channels benefit customers by improving end-user satisfaction and retention, accelerating speed to market, creating technology savings and enhancing their data analytics solutions and market research capabilities. End users receive better access to their financial information and more control over their finances, leading to more informed and personalized decision making. For customers who are members of the developer community, Yodlee solutions provide access to critical data and payments solutions, faster speed to market and enhanced distribution.

We believe that our brand leadership, innovative technology and intellectual property, large customer base, and unique data gathering and enrichment provide us with competitive advantages that have enabled us to generate strong growth.

- Envestnet Analytics provides data analytics, mobile sales solutions, and online education tools to financial advisors, asset managers and enterprises. These tools empower financial services firms to extract key business insights to run their business better and provide timely and focused support to advisors. Our dashboards deliver segmentation analytics, multi-dimensional benchmarking, and practice pattern analyses that provide mission-critical insights to clients.

Market Opportunity

The wealth management industry has experienced significant growth in terms of assets invested by retail investors in the past several years. According to the Federal Reserve, U.S. household financial assets totaled approximately $90 trillion as

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of September 30, 2018, representing a sizeable wealth management opportunity. According to Capgemini's 2018 World Wealth report, global high-net-worth financial wealth is on course to exceed $100 trillion by 2025, up $30 trillion from 2017.

In the next 5-10 years, fewer firms will manage far more assets at a significantly lower cost. Industry margins will be squeezed making scale and operational efficiency far more important. Firms will need to integrate technology in all areas of the business and develop a clear strategy for the future. As low-cost products gain share and larger firms benefit from scale economies, there will likely be further consolidation and new forms of collaboration.

A number of significant trends are impacting the wealth management industry. Market forces are converging to bring about changes in wealth management, including those described below:

- More consumers are recognizing the need for advice and are willing to pay for it. Consumers are also becoming more cost conscious and tech savvy. They want advice to be objective and non-conflicted.
- Investment advice will be rooted in financial planning and centered on achieving investor goals.
- There are significant gaps between the services investors actually receive and the wealth management services they would like to receive. The key change that wealth managers must deliver today is personalization.
- Federal and state regulations and investor demand are changing, and a fiduciary standard is expected to become more broadly applicable in the investor-advisor relationship. According to Cerulli Associates Managed Accounts Qualitative Update 2018, fiduciary assets represented approximately 45% of industry assets as of 2017.
- Based on data from Cerulli Associates, fee-based financial advisory services topped $10 trillion in 2017 and advisors had discretion over 57% of managed account assets in 2017 which is expected to climb to 59% by 2021.
- Advisors are personally managing $2.8 trillion in assets but as Envestnet's September 2018 Envestat showed, those advisors who attempt to "do it all" are experiencing mixed results, at best. Only a small percentage of advisors succeed at outperforming the market, and those advisors who do so have relatively fewer accounts and assets in their care. This opens the door to potentially more outsourcing of investment management by advisors to professional money managers and strategists.
- According to various media sources, a massive wealth transfer estimated at $30 trillion is expected to take place over the next 30 to 40 years as baby boomers transition assets to their offspring (Gen X and Gen Y), who tend to favor greater use of technology in their engagement with advisors and prefer access to advice and their assets anywhere, anytime, and on any device.
- Technology is transforming the financial advice industry. Control is shifting from manufacturers and distributors of products to consumers. As consumers become better informed in an increasingly complex market, they not only seek guided advice, but they seek unbiased advisors who put their best interest first. They demand greater transparency in product pricing.
- Digital technology is revolutionizing the way financial advisors can do business as they increasingly employ technology to service clients.
- Financial services firms will need to be able to interact with customers on a digital basis via investor portals and other technology.
- Regulations and digital advice start-ups are putting pressure on advisor and firm fees and profit margins. To survive and thrive, advisors will need to increasingly rely on technology to achieve efficiency and scale to serve a growing client base.
- We are entering a new era of the unified advisory platform ("UAP"), a single, all-encompassing platform, which creates one advisory superstructure. The UAP will drive profound changes throughout the financial services industry and will remove structural silos. The most important feature of a UAP is the aggregation of all programs on a unified technology architecture. The UAP gives advisors a comprehensive view of a client's entire household portfolio. It simplifies portfolio management by allowing the advisor to organize all the client's advisory accounts from a single desktop portal. Nearly half of managed account sponsors are moving towards a single account architecture, but three-quarters of firms say this could take more than a year or two to achieve.

These trends are impacting Envestnet's business and creating a significant market opportunity for technology enabled investment solutions and services like ours.

A technological shift is also underway in the broader financial services industry. Outdated enterprise hardware and software are being replaced by cloud-driven solutions that are easier and less expensive to implement, update and manage. Banks continue to spend heavily on IT in order to compete effectively in an increasingly competitive environment. The addressable market opportunity is large.

- As financial institutions continue to spend on technology, we believe a growing proportion of that spending will shift to cloud-based solutions.

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- In addition to the opportunity that exists with traditional financial institutions, we believe that we also have a significant opportunity with Internet services companies providing innovative financial solutions.
- Open platforms and application-level developer ecosystems are driving innovation forward. New technology platforms are leveraging big data.
- As mentioned in PwC's Asset and Wealth Management report, investors want solutions for specific needs, not products that fit style boxes. Technology is enabling outcome-based planning. It can quickly identify important life goals and solutions to match. Technology and data analytics are expected to be used to construct multi-asset outcome-based solutions using low-cost building blocks such as ETFs or index trackers. For just a small fee, computer algorithms will be able to create customized solutions.
- It is widely believed that technology is set to disrupt all areas of wealth management. Studies have shown that: 58% of an advisor's occupation can be digitized using AI; 73% of 18 to 34 year olds would try a tech firm's credit card, deposit account, investment or mortgage; and 69% of advisory firms' websites are optimized for mobile use.
- A report from Roubini Thought Lab indicated that by 2022, the "SMAC" stack (social, mobile, analytics, and cloud) will become a necessity for investment providers, and over half of those surveyed plan to use a cloud platform to replace their legacy systems. Digitally advanced firms now spend approximately 17% of their revenue on technology and plan to increase that investment to 24% by 2022.
- Given that clients expect to be able to access their account information from any device at any time, advisors (and financial services firms in general) must be prepared to interact with clients through a wider range of communication channels. New technologies are being adopted by wealth management firms to better communicate with clients and give them the same type of experience they receive in other aspects of their lives, such as using devices like Amazon's Alexa and video performance reports.

As we continue to expand our presence in the markets outlined above, the number of potential end users who use our solutions increases dramatically. Our potential end user base includes any consumer of financial services on the Internet—and this end user could be a paid user of Envestnet | Yodlee many times over across multiple customers and products.

Business Model

Envestnet's business model lends itself to a high degree of recurring and predictable revenues. Envestnet provides asset-based, subscription-based and professional services on a business-to-business-to-consumer ("B2B2C") basis to financial services clients, whereby customers offer solutions based on our platform to their end users. On a business-to-business ("B2B") basis, we deliver an open platform to customers and third-party developers through an open API framework. We believe that a number of characteristics contribute to the success of our business model, including:

- Favorable trends with respect to growth in fee-based assets and need for advanced technology;
- Recurring and resilient revenue base; and
- Strong customer retention.

Revenue is generated in the following three categories:

Asset-based recurring revenues

Asset-based recurring revenues primarily consist of fees for providing customers continuous access to platform services through the Company's uniquely customized platforms. These platform services include investment manager research, portfolio diagnostics, proposal generation, investment model management, rebalancing and trading, portfolio performance reporting and monitoring solutions, billing and back office and middle-office operations and administration and are made available to customers throughout the contractual term from the date the customized platform is launched.

The asset-based fees the Company earns are generally based upon variable percentages of assets managed or administered on our platforms. The fee percentage varies based on the level and type of services the Company provides to its customers, as well as the values of existing customer accounts. The values of the customer accounts are affected by inflows or outflows of customer funds and market fluctuations.

In approximately 90% of asset based fee arrangements, customers are billed at the beginning of each quarter based on the market value of customer assets on our wealth management platforms as of the end of the prior quarter, providing for a high degree of revenue visibility in the current quarter. Revenue may fluctuate from quarter to quarter based on changes in asset values, fee rates on those asset values and asset flows.

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Subscription-based recurring revenues

Subscription-based recurring revenues primarily consist of fees for providing customers continuous access to the Company’s platform for wealth management and financial wellness. The subscription-based fees generally include fixed fees and or usage-based fees.

Envestnet’s subscription fees are also highly predictable because they are generally established in multi year contracts providing longer term visibility regarding that portion of total revenues.

Subscription fees vary based on the scope of technology solutions and services being used, and are priced in a variety of constructs based on the size of the business, number of users or number of accounts, and in many cases can increase over time based on the growth of these factors.