



The Future of Fees

Real Life Pricing Innovations in Wealth Management

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Introduction:

Like it or not, wealth management is in a constant state of change.

This is currently driven largely by *regulation*, which requires advisors (who have not yet done so) to move from 'Suitability' to 'Fiduciary' standards, and *technology*, which is driving them to expand beyond investment management towards holistic planning.

As these trends disrupt the wealth management proposition, the saturation of the asset-rich retiree segment is also leading advisors to target clients beyond the traditional client groups, to encompass Gen X and Gen Y.

Given all this change, new fee structures are only to be expected.

The topic itself is not particularly new. For years, industry commentators have been eloquently setting out pros and cons of the various alternatives. But are people actually doing much about it?

While many firms ostensibly offer a multiplicity of fee models (such as up-front fees, hourly, or project-based), in practice it is likely that the majority of wealth management clients are effectively paying a single AuM-based fee.

There are multiple reasons to expect this to change rapidly in the near future.

First: an AuM-based fee does not effectively reflect the value delivered. Two clients with differing asset levels can pay vastly different fees for effectively the same service.

Second: The model also relies (tacitly) on a minority of high-AuM clients financing the majority of the book, which often includes an unprofitable 'long-tail'. Currently there is no strong commercial rationale for high-AuM clients to continue to do this.

Third: The 'long-tail' referenced above includes individuals who lack assets because they are young, or middle-aged clients who do not have liquid funds. These are the high-AuM clients of tomorrow, but for today the AuM% fee makes it hard to serve these clients profitably (or at all). So they are very often turned from the door.

Fourth: most concerning of all, the standard 100 bps fee seems increasingly under pressure from low-cost alternatives, and advisors are offering higher discounts or so-called 'stealth discounts' (i.e. more work for the same fee) in response. We've done the numbers, and if this trend continues, it ain't pretty.

Add all this up, and you are led to a stark conclusion: there has probably never been a worse time than now to be unclear about your value proposition and how much it is worth.

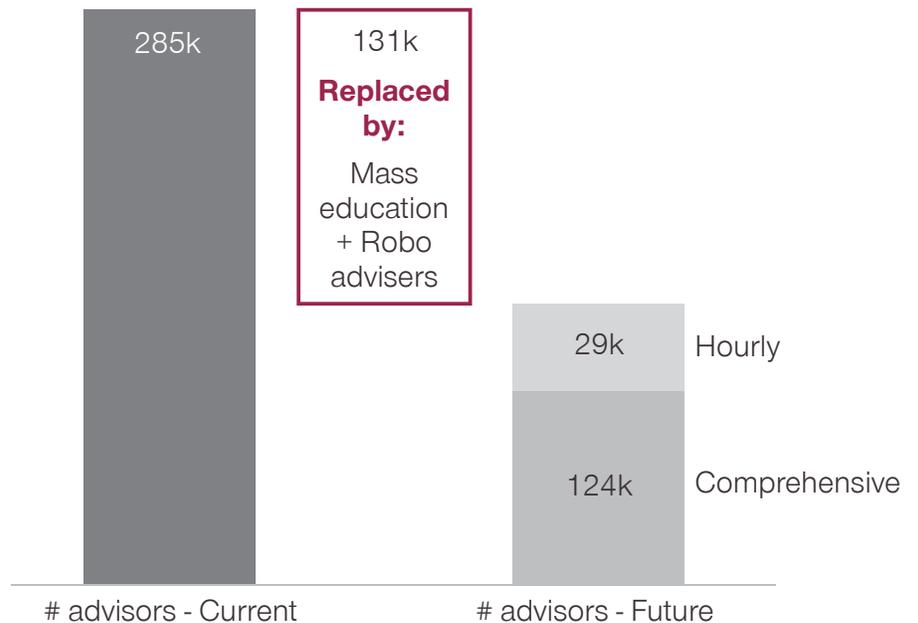
Why not just ‘wait and see’?

At a recent conference, Carolyn McClanahan (whose fee model is featured in this report) half-playfully, half-seriously presented a scenario in which technology and emerging alternatives could eliminate the need for roughly half the current advisor population.

While we agree this scenario is plausible and even likely if the current fee model persists, it is neither inevitable nor desirable.

In the enthusiasm for low-cost, automated methods, the benefits of human advice will perforce be compromised, and what remains will leave many people under-served.

Fig. 1: The future advisor landscape – “no change” is not an option



Source: Cerulli Associates, Carolyn McClanahan

The First Movers have already moved

In reports such as ‘Pricing For Growth’ and ‘Re-wiring Wealth Management’, we have set out a path to developing a new proposition and pricing model that fits your client base.

One of the main obstacles to innovation is the justifiable fear that theory will not translate into practice. So when a real life practitioner implements a new model and - more importantly - makes it work, this is an important milestone.

In the first half of this report, we’re going to look at some of these examples – what new pricing paradigms look like in reality.

In preparing this report, the pricing innovators in question have been good

enough to share their thoughts on the journey and its challenges with us.

In part two, we address common challenges and objections to implementing new price models. Even with a 'proven' approach, there is no guarantee of success. It is always possible to implement a good idea badly.

It may be that the model in question is wrong for your particular client base; the structure may be right, but the level is wrong; or the communication may be mishandled.

But these are simply reasons to do it right – not to avoid doing it altogether.

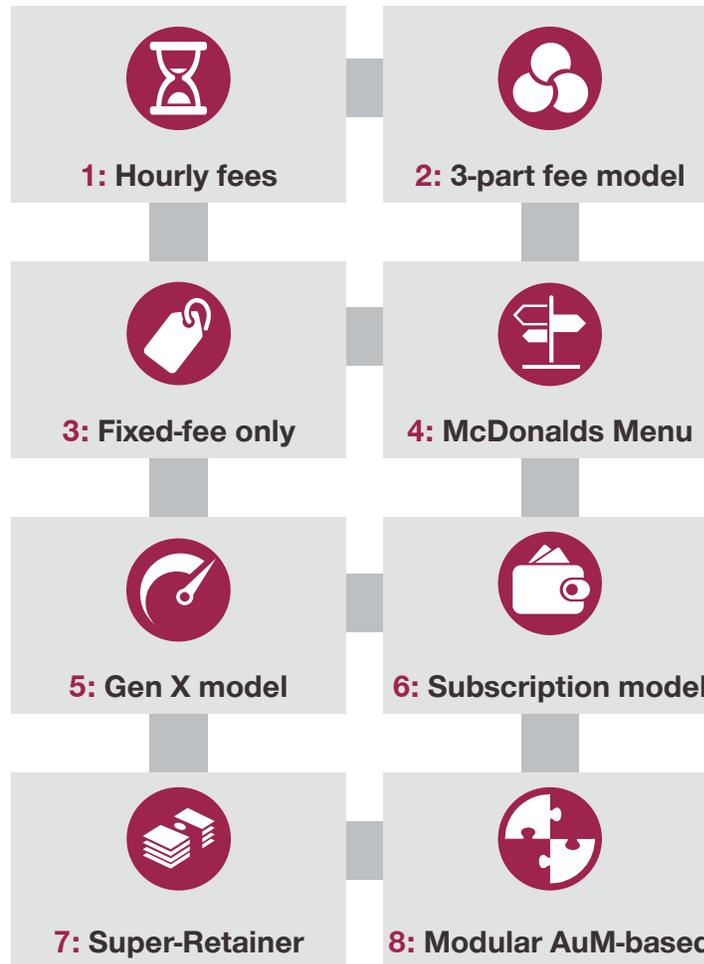
Moving to a new pricing paradigm will not be easy, but it is possible to take note, heart, and insight from entrepreneurs who have walked the walk and are blazing a trail for the future of financial advice.

The future will not wait any longer. The future of fees is now.

Part I

Real Life Fee Innovations – 8 Examples

Fig. 2: Eight Models for Innovation



The diversity of fee models in this report illustrates the fact that there is no ‘new fee model’, but the future is simply likely to be more diverse.

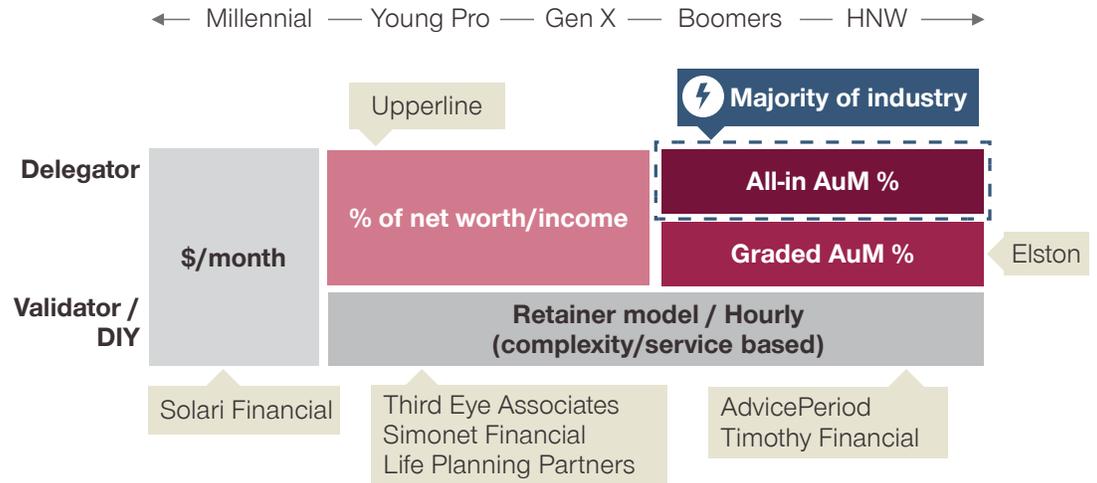
This diversity reflects the need of wealth to adapt to non-traditional segments. Up to now, the fee model of choice – All-In AuM% – has confined wealthy advisors to operating in the top right-hand corner of the diagram below.

Michael Kitces popularized the term¹ ‘high net-worth delegator’ to describe the classic target wealth management client – someone who wants to hand over the keys to their financial life to a third party.

¹Originally coined by Forrester Research in ‘Driving Sales with Segmentation’ (2006)

This is a restrictive approach when considering the full spectrum of potential wealth management clients out there. The innovators in this document are all targeting specific segments of this blue ocean.

Fig. 3: The emerging fee model landscape



The sheer variety of these fee models makes it hard to generalize about their characteristics.

Some themes, however, do emerge that set the models apart from the traditional approach.

- 1. Recognition of complexity** as a driver of variation between clients
- 2. Understanding of the need to ‘fence’ value**, rather than offer everything on an All-You-Can-Eat basis
- 3. A realistic attitude to the ‘sticker shock’ phenomenon** – clients do not run at the sight of a dollar sign, but fees can trigger price sensitivity if not accompanied with coherent story.

The only way to gain a full understanding of these fee models is to peruse them thoroughly.

Good luck, and see you on the other side!

“We’re in the process of getting people to believe – clients as well as the industry itself – that this is who we are, this is what we’re going to be, a profession like any other.”

Part I

Charging by the Hour

Key learnings

- The ‘salience’ of hourly fees is a myth
- Time-based model frees you from the prison of AuM thresholds
- Beware of under-charging!

It’s generally accepted that clients are more sensitive to prices expressed in dollars than in basis points. It’s also one of the sacred rules underpinning the traditional AuM % fee model.

“Clients would have a coronary if they knew what they were really paying!”

This statement is both true and false – it all depends on how the information is conveyed.

Enter Mark Berg, of Timothy Financial. Mark not only charges clients in dollars, but bills them by the hour, as in other professions such as accounting.

Hourly fees, you say? Good luck with that.

When he began with this fee model, he was assured by his friends in the planning community that the approach would fail. “When you grow up, you’ll do AuM” was the prevailing view.

Years later, the model has succeeded, confounding these expectations, and not an AuM fee in sight. How is this possible? It comes down in large part to execution: it’s not as simple as invoicing clients for every phone call.

Mark has taken the approach, set out below, of reflecting on the different clients he serves, and telling a story about these differences (see the third section of our ‘Pricing for Growth’ report for why this is important).

The price is part of this story, but is linked – as it should be – with the corresponding value. Take a look.

Fig. 4: Hourly fees, based on customer situation, Timothy Financial Counsel

Typical split	Complexity level	Typical overall costs	Example issues addressed
23%	Level 5	\$14,000+	High complexity insurance / estate
31%	Level 4	\$6,375 - \$10,200	Pre-retirement decisions
24%	Level 3	\$3,825 - \$6,375	Advanced tax planning
7%	Level 2	\$3,060 - \$4,590	Multiple retirement contribution
7%	Level 1	\$2,550 - \$3,570	Basic retirement decisions
5%	Next Gen	\$1,000 - \$3,000	Guidance for young clients

What's great about this model

It is common among advisors who charge for planning to apply the same fee (e.g. \$5,000) to every planning client – regardless of need, effort, and time required. This creates problems for both parties.

From the advisor's point of view: the price is almost guaranteed to be wrong for a sizeable portion of the client base, because client needs differ. With a one-size-fits-all fee, either some clients will subsidize others, or the advisor will accept a loss.

From the client's point of view: she is presented with a single 'accept or reject' price point, with the comparison point being either zero (refuse the plan) or a cheaper option (go next door to the broker who gives planning away 'for free'). Psychologically, it's best to have the reference point within your offering rather than outside the firm.

Calculating and presenting the different levels of complexity makes the value-price relationship clear, coherent and calibrated. It may lead a client even to question the pricing of a cheaper competitor as potentially lacking in value.

What's the rationale?

Mark explains the story behind his journey from AuM to hourly as follows. Beginning his career in a traditional RIA firm, he found that he was rejecting 80% of inbound leads.

This was because only 20% of leads conformed to the paradigm of the typical wealth management client – the High Net Worth Delegator – who has a substantial pile of cash that needs managing by someone.

For wealth advisors wondering how to maintain growth in revenues, the question “How can I stop turning away 80% of my business?” would seem to be an entirely logical question.

Mark found that the solution is simple: if clients are prepared to pay for services, name the price and ask them to pay it!

Counter to common misconception, clients are not terrified of hourly fees. Some clients call up and express palpable relief at having finally found an advisor who offers this arrangement. “They say they thought that this is what ‘fee-only’ meant!” says Mark.

And since there was no firm offering this logical arrangement, he set up his own.

Who is the target client?

The beauty of the hourly fee is that ‘target AuM’ becomes irrelevant. And, it’s worth reminding ourselves, for most of the commercial world (outside financial services), this is already the case!

There is no ‘minimum AuM threshold’ to buy a Swarovski necklace or Rolls Royce car, besides having the cash to pay for it. Although obviously we are more likely to find these items among the wealthy, the minimum requirement is the price itself.

“It’s a textbook blue ocean strategy,” says Mark, “We’re filling a need that others right now are choosing not to serve.”

This un-served segment obviously includes the problematic High Net Worth ‘Validators’, the nemesis of the classic AuM-based wealth manager. The average net worth of Mark’s personal client base is a cool \$20m - implying there are a lot of wealthy individuals out there who are not only prepared to accept his fee model, but prefer it to the alternatives.

These clients either cannot or will not hand over their wealth to be managed. But they are evidently happy to pay someone to advise them on their own terms, when they require it.

These could be business owners whose wealth is tied up in illiquid assets, or ‘millionaires next door’ who just prefer to retain control of their investments.

But there is a more obvious benefit: a non-typical pricing model also opens up the possibility of serving non-typical client group – a large portion of the rejected 80% – who fall below the typical AuM threshold.

“They spend less than they earn, avoid debt, save for the future – sensible people, basically. They could be just out of college. I’m thrilled to serve them, and help them get on a firm foundation.”

Note that these are not ‘problem clients’ – as they would be (correctly) classified in a typical AuM-based model – *since they use only what they pay for*.

An hour spent with a billionaire is every bit as profitable as one spent with a blue collar client, although the billionaire may ultimately require more hours and bring in more revenue over time.

What are the challenges with this model?

The flip-side of attaching a monetary value to time, is that time suddenly becomes very precious. This has implications for business operations. “A round of golf will cost you \$1500 dollars in lost revenues” says Mark, half-jokingly.”

As with any pricing initiative, it is also important to get the price right. Willingness to pay may be there, but judging that level correctly is a large part of success or failure.

It’s worth noting here that a tendency to undercharge is every bit as calamitous as overcharging. Client price sensitivity aside, there is often a psychological struggle that needs to take place within the advisor.

In Mark’s case, his initial price point was 150 dollars per hour, which turned out to be underpriced, creating a classic excessive-demand problem.

“I realized they’re getting a bargain! Objective advice not money management, no product sales – where else could they get that?” He now charges \$350 dollars per hour, and focuses his time on ‘level 5’ clients with a high degree of complexity, requiring his specific expertise.

But seriously, how do you make this work?

It’s one thing to appreciate the theoretical possibility of hourly fees, and another thing to picture yourself saying the words to a client.

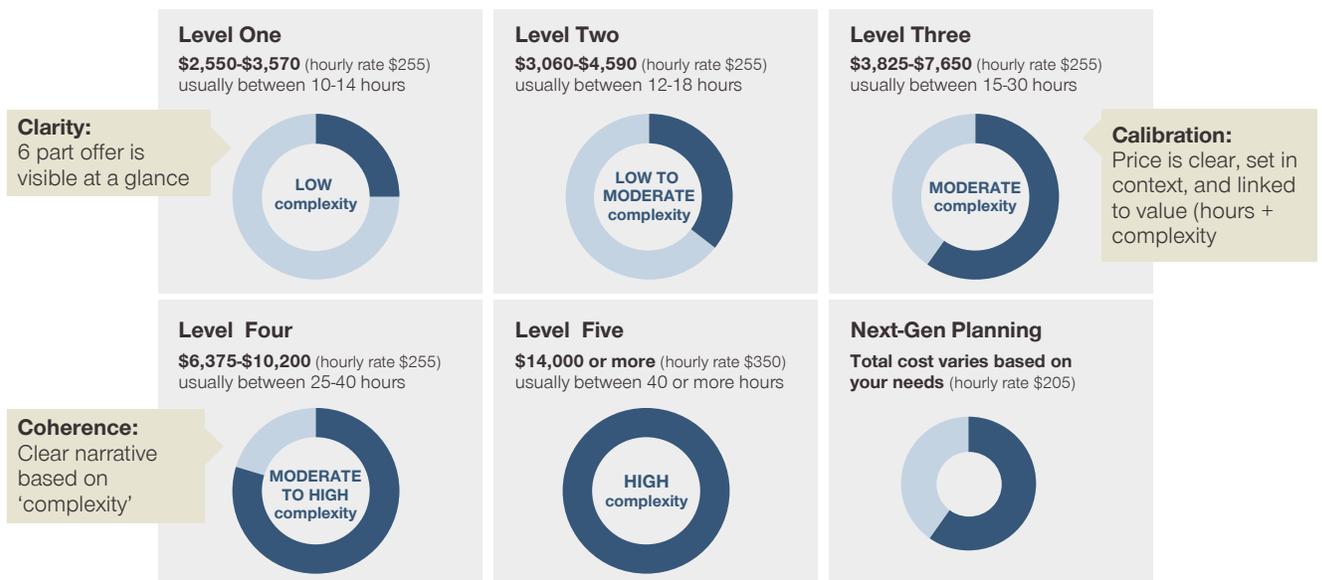
What’s the conversation like? Apparently, very straightforward. “We explain that this [the fee] is your investment in the relationship - we need to get to know you. If you’re not ready for that, fine. Call us when you are ready.”

It seems to go down a storm. “Even during the early years, the closing rate was above 80%.” This is dramatic improvement on the industry standard, which is closer to 20%, and proof that ‘salient’ prices such as dollar fees, if communicated in a value-based way, are no obstacle to growth. Any deterrent power they have may be salutary, as it filters out prospects who were never serious in the first place.

Most egregiously of all, Mark takes the unthinkable step of displaying fees on his website, something normally associated with robo-advisors, who do so in order to emphasize how cheap they are.

The fees of Timothy Financial are displayed with a boldness and clarity that not only contrasts starkly with the coy reticence of 99% of planning firms, but also takes advantage of a hugely important opportunity to link price to value.

Fig. 5: Perfect Pricing Presentment



In terms of pricing psychology this is a work of art. The different levels are essentially value stories – clusters of needs associated with different types of client, and hence easier to accept by the 'System 1' thinking process, classified as follows according to Simon-Kucher & Partners '3 Cs' Value Communication Model.

- **Clarity:** you see instantly that there are six offers and your offer sits somewhere among them.
- **Coherence:** it quickly becomes clear that the difference between the offers is driven by complexity - explaining the difference in price.
- **Calibration:** in all likelihood your plan will sit somewhere south of the maximum fee, meaning that it will naturally appear reasonable compared to higher plans.

So, is this the future?

Mark acknowledges that the industry is undergoing a transformation. He states this forcefully: “We’re in the process of getting people to believe – clients as well as the industry itself – that this is who we are, this is what we’re going to be, a profession like any other.”

This shift from industry to profession is a positive one – not just in terms of an increase in standards and trust, but also in terms of the value clients will perceive. Bob Veres’ testament to this new value proposition in *The New Profession* sets this vision forth in all its grandeur.

We’ve seen time and time again that industries on the brink of price wars can be saved through ‘value warriors’, who understand the worth of their proposition and charge appropriately and transparently.

Mark Berg has busted a myth - the Intractable Saliency of Hourly Fees – and together with other fee innovators, is pointing the way to a new age of professional pricing in wealth advice.

“If they’ve got the money coming in - they’ll pay the whole ride”

Part II

The 3-part Model

Key learnings

- A more flexible proposition calls for a more flexible fee structure
- AuM fees can remain the core revenue driver
- ‘Sticker shock’ is not inevitable, but a question of presentment

As discussed in previous reports, the wealth management proposition consists of essentially three components:

- 1. Managing your money**
- 2. Developing an initial financial plan (year 1)**
- 3. Providing ongoing support (year 2 onwards)**

Beth Jones, founder of the advisory firm Third Eye Associates, Ltd has pioneered a three-part fee model that allows clients to customize the service they receive, and with it the price.

Three-part fee, you say? That sounds complicated...

Although more complex, the mechanics of the fee structure are easy to grasp. And because each fee is linked with a corresponding service, it is easier for clients to see what they are paying for.

- 1. Assets under management** incur an **AuM fee**
- The **initial plan** carries an **initial fixed fee** (differentiated by levels of complexity)
- 3. Ongoing support** can be purchased for an **ongoing annual fixed dollar fee or ad-hoc for an ad-hoc** hourly fee.

The fee structure is easy to grasp *because it is logical.*

Fig. 6: Fixed fees, based on customer situation, Third Eye Associates

	\$2,500	\$3,500	\$4,000	\$5,000
Package				
Coverage	Basic Needs Only	Comprehensive Individual	Suitable for couples	Suitable for businesses
Service hours	13 hours	19 hours	27 hours	41 hours
 Ongoing maintenance	\$1,500 per year Or: \$200 per hour		 Investment management	Charged on a standard sliding AuM % basis

What’s great about this model

One big practical advantage is the flexibility it gives to both the client and the advisor.

Since the revenue model does not hinge entirely upon AuM (investment management can be deselected if the client wants planning only), a client with no liquid assets can still become a client, widening the reach of the firm.

Furthermore, the gradation of up-front planning fees and separation of ongoing support fees acknowledges that not all clients will require the same depth and intensity of attention.

The client will understand the rationale for the fees they pay, and the advisor will have better visibility and control of costs attributable to individual client usage.

Finally, the explicit calling out of the 3 service components emphasizes the multi-layered nature of the value, as opposed to the monolithic obscurity the All-in AuM % fee, which invites unhelpful comparisons with cheaper propositions that may provide less value.

What’s the rationale behind it?

The new model has its roots in the realization that financial planning, if done correctly, is a deep discovery process, rather than a mechanical exercise. In other words, it deserves an explicit price point.

If one calculates the hours involved, it is a natural step to have different price levels for different plans - here separated into Bronze, Silver, Gold and Platinum.

This creates a coherent story for the client, who can see a package in the context of the full range of possibilities, rather than a mysterious, disembodied price point handed across the table by the advisor.

The lowest package 'Bronze' is a modular plan intended only to help clients manage their short-term needs. Its presence in the line-up is important, as it presents an 'emergency exit' for clients who either do not need or do not (yet) want a more comprehensive plan.

The third service component, ongoing service or 'maintenance' as Beth classifies it, is an optional extra which is up to the client to define.

'Maintenance' is particularly relevant for clients undergoing the first two years of a transition or life event, whereas in the ensuing period it may not be required to the same extent or at all.

Being able to switch on and off / dial up and dial down, both highlights the value of the service and reassures the client that she is being charged for what she uses and no more.

Who is the target client?

The flexibility of the proposition means that technically *all client segments* are potential clients, including non-typical clients who fall below the standard AuM thresholds.

As a result, Beth receives referrals from *other* advisory firms - for example those unable to accommodate clients with less than \$2,000,000 in assets.

Beth describes her core 'non-typical' clients as 'affluent middle Americans'. Some of these may not be familiar with planning, and so communicating the value is particularly important.

While suitable for all, the flexible 'ongoing support' service model is particularly well suited to clients dealing with deep emotional crises such as the loss of a spouse.

Accommodating the unpredictable roller-coaster schedule of a client undergoing internal upheaval often means shorter, more frequent meetings.

Beth gives an example: "Four months into a plan, my client's husband was diagnosed with Alzheimer's. I had to keep her calm. She had to run back and forth dealing with her husband, and she couldn't handle a 90 minute meeting. We had 30-minute phone meetings once per month, until she had reached a calm state of mind".

Other non-typical segments include millennial couples, often professionals with a healthy cash flow who can afford to pay the fees out of their monthly paycheck.

Note that insufficient assets does not equate to low willingness to pay or a tendency to select the most 'basic' option. In Beth's experience, "If they've got the money coming in - they'll pay the whole ride".

In case of those who do have cash flow problems – for example those putting aside money for a house – a full-scale plan is not required, but simply some guidance meetings.

Once again, flexibility allows Beth to serve everyone. Not only this, parsing out the value of different services also enables Beth to keep better track of activities she is performing for her clients. A standard all-in fee leaves an advisor with the nagging awareness that the more time they spend per client, the less profitable that client will be (as revenue is not linked to services used).

Aren't there any challenges with this model?

For all the focus on the planning and support fees, Beth is quite clear that 'Nothing makes money like an AuM fee'. It therefore remains a part of her pricing arsenal.

The aim is not to discourage clients from bringing their investments to be managed, but to accommodate those who don't (or can't), such as a forty-something client with only a 401k.

How about sticker shock: surely clients see the dollar fees for up-front planning and 'deselect'? Apparently not, according to Beth.

"I have all new clients since 2005 who have come in, and nobody gives us just assets. I have not found 'sticker shock'. It's about how you present it to the client – I never talk about the money until I've talked about the value and what it includes."

Although a remark made in passing, the importance of communication to successful implementation cannot be over-emphasized (see the topic of 'Presentation' covered in the Simon-Kucher report 'Pricing for Growth').

Allowing clients to pay installments – converting a large dollar figure into a smaller dollar figure – also lessens the potential shock to the system of having to pay in dollars instead of basis points.

So is this the future?

Beth is one of a growing number of planners who employ this model. While Beth's focus is on the \$500k – \$2 million segment, many others work in the ultra-high net worth space. She has also witnessed that the flexible model chimes with the approach of younger planners entering the profession.

This makes sense, as the trend across all services and all industries is towards customization. Viewed from this perspective, the 3-part model is better aligned to shifting client tastes, and opens up new growth avenues for the industry as a whole.

“The only reason we lose clients is if they die or marry somebody mean.”

Part III

Fixed-fee Only

Key learnings

- Fee sensitivity can be neutralized by linking fees directly to value
- Complexity is a better basis for pricing than asset value
- In the future, authenticity will trump salesmanship

When it comes to advisory fees, fixed dollar fees tend to be a somewhat sparsely attended side-show to the main – AuM-based – event.

Carolyn McClanahan of Life Planning Partners is one of a fairly rare group of wealth managers who charge recurring flat fees with no AuM-based component.

No AuM? But....how....why...what did you....why?

Yes, I know. Lots of questions. Why eliminate the one price component that basically everyone agrees works, in favor of one that people find most problematic – and then repeat this error on a yearly basis?

Before getting into the background, let’s look at the model itself in more detail.

Like Mark Berg’s hourly-fees model, the fee varies from client to client, and is ultimately based on complexity and individual needs.

The minimum client fee is \$10,000. Unlike Mark Berg’s model, this is not just a financial planning fee, but a full-service fee. It includes investment management, follow-ups, implementation – the whole nine yards.

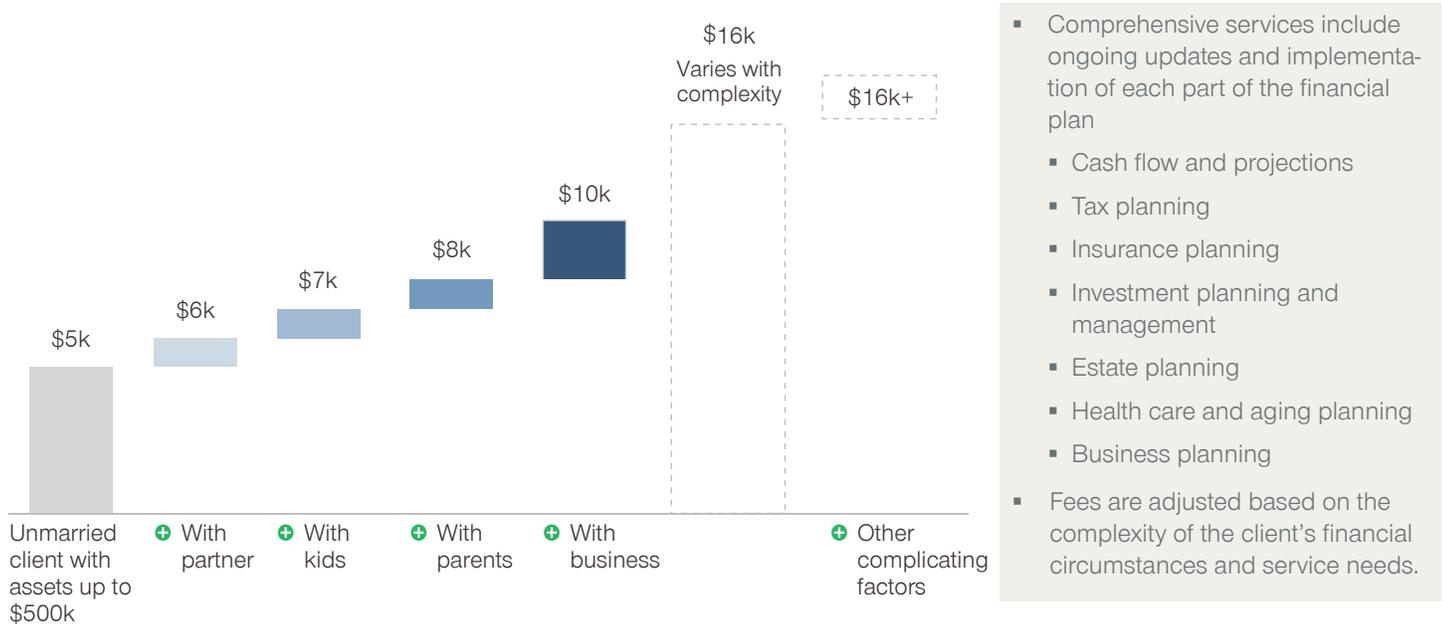
When calculating the fee, Carolyn starts with a base of \$5,000. Each layer of complexity adds more to the fee. Since Carolyn’s typical client is typically more complex, the average fee is closer to \$17k.

If a client doesn’t warrant a \$10,000 minimum, they are referred out. Instead of an ‘asset minimum’ – which doesn’t sound good no matter how you phrase it – there is a ‘complexity minimum’ – which actually makes sense. Why see a surgeon if all you need is a band aid?

Below is a visual impression of how the fee is determined in the initial conversation with the client.

As the client situation becomes more complex– i.e. add a dependent, an ex-spouse, business interests etc. – the fee increases to reflect the additional work for Carolyn’s team. Notice how value is clearly correlated with price – a significant flaw in the pure AuM-based fee model.

Fig. 7: Annual fixed fees, based on customer situation, Life Planning Partners



Assets do matter, but the fee is based on the structure of assets (e.g. the amount that will be dedicated to fixed income ladders, which engender more work), and how much tax planning is required. All is reflected in the flat, dollar fee.

What's great about this model

The first thing to note about this model, is that it has been in place for 10 years. In other words, it clearly works – for clients and for Carolyn.

From a client perspective: complexity-based logic gives a coherent basis for explaining the fee. This coherence speaks directly to a client's 'fast-thinking' decision making faculty, influencing willingness to pay. Alternatively put, if it makes sense, it makes money.

From an advisor perspective: linking value-delivered to fees-charged not only makes the fee easier to explain, but also links revenue to cost and therefore ensures profitability. As we've remarked elsewhere, this contrasts with the AuM model, wherein profitability depends on initial client AuM, client behavior and market movements.

What's the rationale?

Given how unusual this fee model is, it's worth delving into the story behind it. Starting out as a comprehensive planner, Carolyn found the prevailing AuM fee model to be unwieldy and somewhat inequitable.

“I had many doctor clients – some had a lot of money, and some didn’t. The fees were very disparate between them, and it didn’t feel right.”

She came across a fixed fee model (then referred to as the ‘retainer’ model) based on net worth, pioneered by the Alliance of Cambridge Advisors (now the Alliance of Comprehensive Planners), and began to develop her own version.

A central part of the onboarding process is educating clients about what it is they are getting. In marketing terms: value communication.

The Life Planning Partners Client Engagement Standards (publicly available – just Google it) make it clear that investment management is only part of the story. This gives a value-based context to the fees, and differentiates it from a lower-touch, investment-focused offering.

Who is the target client?

Life Planning Partners has a definite target niche, consisting broadly of “millionaire next door” clients with \$2-10m in net worth, who value simplicity, and have more complex needs – such as more expansive estate planning, different investment requests etc.

Being focused obviously helps deliver a proposition that is tailored to a specific needs segment – reinforcing the perception of value and willingness-to-pay.

It sounds too easy. Any bumps in the road?

Of course yes. Transitioning clients from the AuM% model took lengthy communication and time. But once they grasped the concept, clients were soon singing its praises. The waiting list for new clients at one point extended to one year.

Hiring talent continues to be the main challenge, Carolyn admits. “Life Planning Partners is a holocratic ensemble and it takes a very special personality to thrive in that environment.” But this is not a value or a pricing problem. And having demand outstrip supply is certainly not an existential problem.

You mean, price acceptance isn’t the main challenge?

No it isn’t, for acquisition or retention. “The only reason we lose clients is if they die or marry somebody mean,” Carolyn remarks, “We have fired more clients than have actually left us. We lose an average of about one client per year including those who are fired.”

So, clients are not storming out.

But more important than the outcome is the cause. There are various reasons for the success of the model – and all are important.

As mentioned above, the nature of the fee model makes it very easy to understand and explain. As Carolyn puts it: “We tell clients, your fee is based on how much you need from us.”

There is also the fact that for wealthier clients – particularly those over 2m – the fee works out cheaper than being charged on an AuM % basis. A lot of clients who have previously worked with AuM-based fees are well aware of this fact. The firm is now acquiring clients in the \$10-30m range.

Moreover, the fee is revisited every two years, in some cases downwards to reflect a decreased workload (although it’s worth noting that for most clients it remains the same).

For those who are proving more work than anticipated, the conversation is simple.

“We keep an ongoing list of everything we’ve done for clients. If a client keeps coming up with new things and requires new cash flow projections every month, I tell them, ‘You know, you’ve got a lot going on’, and they get it. I have one client who actually laughs when her fee goes up.”

In the long run, the tacit expectation is that the value will come into line with the fee, or the fee will be adjusted down accordingly.

There are many other reasons that account for the loyalty of clients at Life Planning Partners. Crucially, many of these reasons are what one might call ‘human’ benefits rather than financial ones. This is linked in no small part to Carolyn’s background as a medical doctor.

“It’s like being a financial doctor. The deep dive planning brings to the surface personal issues clients face that affect their financial health. We refer complicated cases to traditional and financial therapists.”

This is important to note for the future of fees and the future of financial planning, in an age of ever-encroaching artificial intelligence.

Is this the future?

As we have mentioned before, looking for ‘the right price model’ is a doomed quest. One should instead find the model that is right for the specific client base one is serving.

Millennials, Gen X-ers, classic high-net worth delegators, or ultra-high net worth validators – all of these clients have different models that fit their ability and willingness-to-pay.

Carolyn’s flat fee model would appear to be most suitable – and in fact, only possible – in cases where there is sufficient trust between the advisor and cli-

ent, and if the advisor truly has the best interests of the client at heart.

Regulation and technology are combining to increase transparency of fees charged and value delivered. Furthermore, a new generation of clients is emerging who value authenticity above salesmanship.

But regardless of which fee model they choose to follow, it is likely that the future belongs to planners who can raise prices to the sound of client laughter.

“My younger clients come from their parents, who say ‘Before I give you this money / send you off to college / you graduate, I need you to go and meet with Bill.’”

Part IV

The McDonalds Menu

Key learnings

- Offering choice without target segments in mind is dangerous
- Bundled hours of advice turn loss aversion on its head
- “Gifting” of advice hours is a way to generate inter-generational referrals

As in other industries, the wealth advisory offering will increasingly revolve around client choice.

There are many forces driving this, including access to information, mistrust of the financial industry, and a wider shift in the consumer mindset towards personalization.

Clients already have a choice, of course, but it is mainly centered on whether to go for an ‘expensive’ traditional offer or a ‘cheap’ online alternative.

Bill Simonet of Simonet Financial has developed a sophisticated choice-based model within the traditional high-touch financial advice framework, which he calls the McDonalds approach.

To explain what he means by this, it’s worth contrasting it with the current norm.

Service to clients may be ‘tailored’ in practice, but this tailoring is rarely systematic from an internal delivery perspective, and almost never visible from a client perspective.

Bill’s vision is that a client should be able to view the options and select the one that best suits his or her needs.

That sounds unrealistic. How are clients supposed to know what they need?

How indeed

Client confusion is due in large part to the unstructured nature of most wealth management propositions.

Let’s remind ourselves that financial planning is typically:

1. **Communicated** as a mass of impenetrable bullet points
2. **Delivered** as an afterthought to investment management
3. **Priced** as an undisclosed portion of the investment management fee.

Bill’s model addresses all of the above three points. Let’s look at how it works.

The McDonalds Menu

The Simonet model is planning-led, and consists of four planning packages. The packages vary in terms of 1) the level of interaction (meetings / hours of advice included) and 2) the scope of issues covered (e.g. tax).

Fig. 8: Needs-based packages with bundled advice hours, Simonet Financial

	Premiere	Premium	Standard	Fundamentals	Investment management only
Interaction					
Planning meetings / year	As required	4 meetings	2 meetings	1 meeting	2 Portfolio meetings only
Hours of advice / year (in addition)	20+ hours	15 hours	10 hours	5 hours	-
Planning scope					
Personalized plan	✓	✓	✓	✓	
Monthly updates	✓	✓	✓	✓	
Comprehensive	✓	✓	✓		
Advanced	✓	✓			
Family office	✓				
Pricing					
Advice fee	\$5,500 - 14,500	\$3,600	\$3,000	\$2,400	\$1,500
Investment management fee	90 bps	95 bps	105 bps	105 bps	105 bps
	50 bps	50 bps	95 bps	50 bps	50 bps

The packages are charged for on the basis of an annual fixed dollar fee.

Investment management is also available, on a typical AuM% basis, but only as an ‘add-on’, not a core feature. 90% of clients begin with planning only.

Planning clients who do select investment management receive it at a discounted rate. The more premium the package, the higher the discount received on the investment management.

The most unusual feature of this ground-breaking model is the ‘phone plan’ style packaging of advice hours – with 5, 10, 15, and 20+ hours bundled into each of the packages respectively.

The point of these packages is to encourage interaction.

Bill explains, “I want you to pick up the phone and call me if you have questions. If you’re looking at buying a car, ask me about interest rates. How much do I put down? How much of the car can I afford?”

His team has software that tracks the number of hours used (emails and SMS are not tracked – no ‘nickel-and-diming’). When clients near the limit, they receive a phone call and a heads up.

Clients can move up a package if they need more time, or bulk-purchase additional hours. “I usually recommend they just go up a package,” Bill says, “Because if they’re using a lot of hours they’re probably going to continue at that level for the next year.”

Another part of the ongoing service is the monthly planning update or “Wealth Summary Report”, which gives a running overview of net worth and account balances.

Needless to say, the focus of this document is not investment returns.

What’s great about this model

Bill says that his model simplifies the conversation. “If a client comes into the office, is 35 years old and has kids, their important questions are going to be around paying down the home loan and other debts. So I’ll suggest the Standard package for that client.”

The second great thing about this model is that its central feature is the number of hours of ongoing support, as opposed to investment management or a one-off financial plan.

“Ongoing support” is a powerful and under-articulated component of the value proposition, and crucially, the one that sets premium wealth management apart from the cheap scalable alternatives.

Until General Artificial Intelligence becomes a reality, human-to-human interactions will remain a premium and non-scalable entity, commanding willingness-to-pay, and providing a source of value differentiation.

Ongoing support grants clients access to expertise (“Should I respond to this letter?”), the ability to outsource effort (“Can you shop this rate for me?”), and an emotional stay (“My daughter just married this jerk...”).

Charging appropriately for ongoing support is a goal that has until now evaded the mainstream financial planning community, and with good reason.

In Bill’s case, it’s the pricing *model* that’s the game changer, not the price level.

If advice is charged on a pay-as-you-go basis, loss aversion dictates that clients are less likely to pick up the phone, since every call represents a ‘loss’.

Since Bill’s hours are paid for *in advance*, however, the psychological bias is reversed. When the hours are purchased up-front, they are incentivized to use

the service. *Not* to pick up the phone represents the loss in this scenario.

Clients will be naturally thinking how to use Bill's expertise, and in using it, will gain direct experience of the value he offers. This is really important, as how many clients will be able to understand the value up-front? Not many.

For the advisor, formalizing the ongoing relationship is an efficient way to follow up, identify additional needs, and keep the relationship fresh.

The pricing model also allows the flexibility to increase or decrease the hours required, by moving up or down a package, or by purchasing additional 5-hour batches.

Finally, as with all planning-led models, it allows the advisor to serve a vastly-expanded pool of potential clients. "I don't require them to have any assets," says Bill, "If they choose to bring assets over, great. If they don't want to – no worries".

What's the rationale?

Bill recalls that in the old days, "I didn't know how to price clients, and clients didn't know what they were paying for."

He had an epiphany while at McDonalds with his kids. Seeing how they easily identified an option on the menu by themselves, he began to wonder how to make the process as intuitive for his clients.

The first challenge was figuring out which elements should go into which package.

He took a financial checklist that covers the various areas of planning, and tried to map them on to different client groups. The four packages that he now uses were the result, each with its own target segment:

Fundamentals: Fresh out of college, or in transition (e.g. recovering from divorce)

Standard: 'Typical Americans' saving for college or retirement

Premium: Affluent families (with tax considerations) and business owners

Premiere: High net worth families and business owners

With these packages, it is normally short work to match a client to a package.

Bill gives some examples: "If someone comes in and talks about a business - they're going to start at Premium. If they are talking about retirement or saving for college – they're looking at the Standard. A high-earning doctor is going to be at the Standard or the Premium package."

The top-most package 'Premiere' is priced as a range. Clients in this package are likely to have complex issues that require large amounts of time, but are hard to categorize as predictably.

“Primarily what you’re paying for in that package is the privilege of my time,” Bill says, “I’ll give you my cellphone number, and you’ll have access to me whenever you need to.”

A client paying the maximum price of \$14,500 would in effect be receiving the equivalent of a Family Office service.

So how much choice is really involved? Doesn’t client circumstance dictate the package? While it’s normally fairly clear what package a client needs, the structure of the offer means that it’s possible for a client to reach the conclusion autonomously.

“It’s primarily choice – about 60%”, says Bill, “I do kind of steer my clients to the package that makes the most sense. But if a client says ‘I want to take care of some of these aspects myself,’ I say ‘Great. Let’s pull out executive comp, let’s pull out business planning. Maybe add college planning. The end result is a hybrid of two plans.’”

The flexibility of the proposition means that it is not a ‘once and for all’ decision, but can be adjusted based on experience further down the road. And importantly: if this adjustment takes place, the price will move to reflect this, *because the logic exists for it do to do so.*

Bill can also proactively tailor the offer if he feels that a client does not fit the classic mold.

“You might be a Standard or Fundamentals client in terms of your complexity, but need more time to implement, for some reason. Then I’ll just add more hours.”

The beauty of the model is that it provides a framework for the discussion which is rooted in specific *value* (hours of human advice) rather than an abstract 2nd order pricing construct (bps).

But...seriously how do you get clients to accept this?

It’s possible to object that an annual fee of \$3,000 might appear intimidating compared to the innocuous 1% offered by a competitor. However, it’s important to remember that in many cases the competitor will be asking for \$1,000,000 of assets as well.

Some clients won’t have this kind of money (e.g. ‘Fundamentals’ clients fresh out of college), or will not have the money available (‘Premium’ clients who have invested all capital in their businesses). For such clients there is no way of obtaining the services Bill offers other than through Bill.

“Small business owners may not necessarily want an investment portfolio yet - but they can absolutely write a check. They know they can reach out to you easily, and they know they can fire you easily.” Pretty hard to argue with.

While we’re talking, where do leads come from?

Here is where the pricing model of ‘bulk hours’ really comes into its own. Like most planners, Bill’s number one source of new business is referrals.

Since some clients may have excess hours in a given year, Bill makes it possible to **gift** these hours to a family member, to ‘fund’ a quick meeting or education workshop.

This means that the client is happy (hours paid for have been used, a younger family member is educated), and Bill not only acquires a new (younger) client, but is reimbursed for it. The hours used have already been paid for!

“My younger clients come from their parents, who say ‘Before I give you this money / send you off to college / you graduate, I need you to go and meet with Bill.’”

That’s nice work if you can get it, especially when the industry is anxiously looking for a way to replace an aging client base.

Is this the future?

A choice-based proposition is future-proofed from a number of perspectives. It is easy to explain, easy to understand, and its inherent transparency deals with conflict of interests.

Like all models that do not hinge upon AuM, it also opens up new channels of revenue, while keeping costs under control.

One interesting by-product of moving to a choice-based model, is that the advisor must become a sales person once again.

If the value of the upper packages is not communicated, the initial conversation could result in an overweight percentage of clients gravitating towards the cheapest option. Under-pricing and under-serving is not a happy combination.

But it is almost certain to happen if the packages are constructed without client need profiles in mind, as in that case, willingness to pay will always be lower than the cost-to-serve for the package in question.

Those who take time to address the challenges this model can bring, can look forward to reaping its extraordinary rewards, together with a legion of satisfied clients.

Part V

The 'Gen X' Model

Key learnings

- Build the price around the clients you wish you could serve
- Clients with illiquid assets still have liquid incomes
- Framing the price is as important as choosing the right level

It is a central maxim of professional pricing that the fee metric (how we charge) is often more important than the fee level (what we charge). One of the serious issues with standard AuM% fees is that they do not work well for low (or indeed zero) values of AuM.

This means that most prospects must be turned away from the door, with a stern injunction not to return until they have enough money to be taken seriously. Then we will graciously consider if we will allow them to hand that money to us.

This approach has narrowed the focus of the 'wealth management' profession to 'pre-retirement management', and to a lucrative but limited portion of the population who are under time pressure to make a decision on what to do with their life savings.

The majority of the population either do not have \$1m+ of liquid assets or do not want to hand it over. But they have financial problems and need advice, particularly if they hope one day to become asset-rich pre-retirees.

How can we serve such clients profitably?

Wait, I know this one. Minimum fees, right?

Minimum fees are a good start, but somewhat crude, and also hard to explain. Luckily, Jude Boudreaux of Upperline Financial has a more elegant solution.

He charges what is essentially a fixed fee, but instead of charging based on a % of AuM, he employs two alternative metrics:

- 1) 1% of monthly income
- 2) 0.5% of net worth.

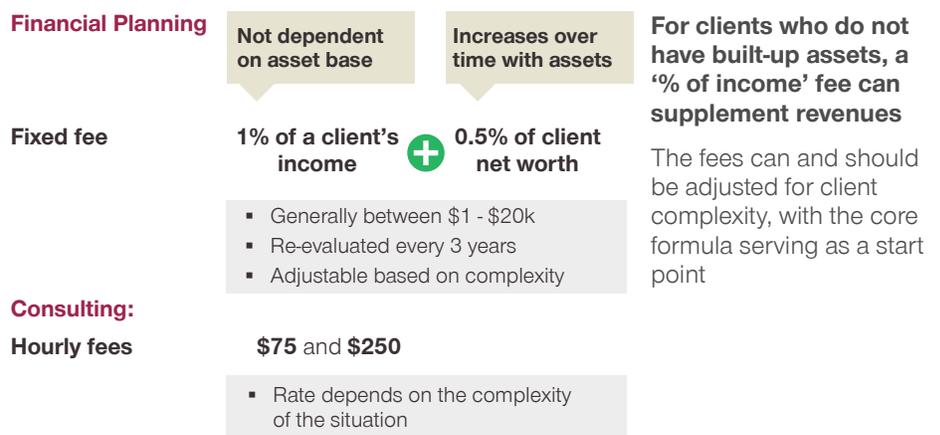
Notice, this is as much a question of framing the fee as it is about calculating it.

The fee is a masterstroke in pricing terms, because it is transparent but not

comparable, making it an ideal response to a price war scenario. The lack of comparability moves the dialogue away from comparing prices to comparing value.

For those who want to use the firm’s services on an ad-hoc basis, Jude also has an hourly fee option, ranging from \$75-250 / hour, with the hourly rate itself depending on complexity of client situation.

Fig. 9: Net worth + Income basis, Upperline Financial Services



What’s great about this model

The model contains three different fee metrics (% income, % net worth, hourly). More metrics is good because it means – generally – more flexibility for the advisor and the client.

But the core innovation is the same as the innovation behind every great price model: it is built around the target client.

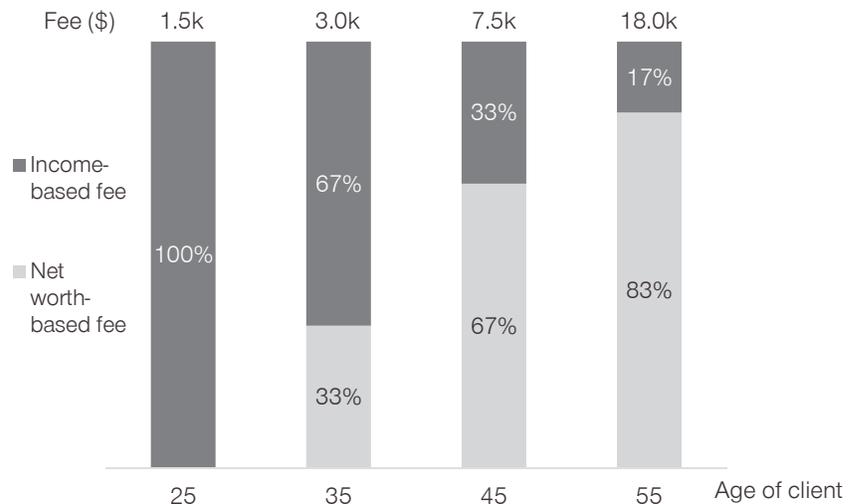
Many middle-aged clients have reached the stage in their careers when they are receiving a decent monthly income. Many are also in the midst of paying off considerable debts.

This fee model allows for this and charges according to ability to pay. It is difficult to argue that 1% of one’s income is unaffordable, particularly when it is being spent not on entertainment but on securing one’s financial future.

The 0.5% of net worth component is essentially “switched off” in the case of clients with significant debts, again matching price with ability to pay. In such cases the, money is better used paying off the debts directly.

The model allows a client with initially low net worth come on board at an eminently affordable rate, and over time graduate to become a high AuM client.

Fig. 10: Contribution of fee components over time



What's the rationale behind it?

The 1% and 0.5% are not rigid. “We want to have flexibility,” Jude says, “There is no magic number.” There are, in other words, other factors that come into play when determining the price for a given client.

He summarizes the additional factors as follows:

- 1. Future potential:** is this a growing client or a static client? What is the saving rate? Are they living on the edge? Getting one’s act together can be incentivized by reflecting positive behavioral changes in the pricing.
- 2. Number of accounts:** a larger number of accounts means a larger fee, as there is more paperwork. Note, this is not the case with account size (another respect in which it trumps the AuM% model).
- 3. ‘Engagement’ factor:** this is a qualitative assessment of how much additional time will be required given the circumstances of the client or client couple.

This final factor – Engagement – is an important one as it is difficult to measure quantitatively, but has a material impact on cost-to-serve, and hence client profitability.

Jude, in fact, takes it seriously enough to break down his assessment into three further sub-factors:

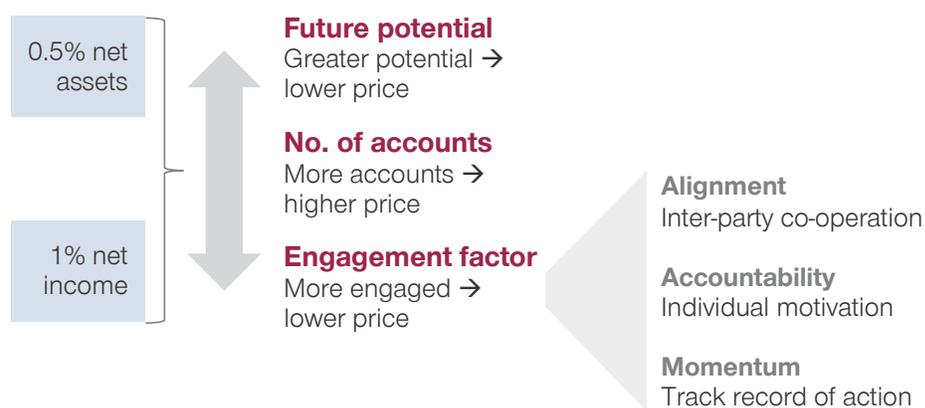
- Alignment:* Are the involved parties heading in the same direction?
- Accountability:* Are the individuals committed to changing their behavior?
- Momentum:* Are the required actions actually being taken?

The fees do have upper and lower limits. For comprehensive planning, the aim is to stick to a \$2,000 minimum, while the maximum fee is capped at \$20,000 (the largest client currently pays \$15,000).

For medical residents and other special cases, Jude has a limited service engagement, covering a ‘vision’, cash flow analysis and debt management plan (e.g. for student loan repayment).

Once flexibility is part of your fee model, delivering what clients need and charging what you require becomes a far simpler exercise.

Fig. 11: Adjustment factors



Who is the target client?

Jude classifies his typical client as a HENRY (High Earning Not Rich Yet).

“A lot [my clients] are young professionals who have accumulated assets, but who have spent a lot of money on education.” In such cases, the debt more than cancels out the assets, but they still have a good income, and can afford to pay a couple of thousand dollars per year.

Another example might be a couple that has 200k of investments and 200k in income (paying a fee of \$3,000 per year).

“This wouldn’t meet the minimum for a typical wealth advisor,” Jude notes, “But the idea is that we help you save smartly now, and you will grow well with us.”

This is clever, as it obvious to clients that it is in the advisor’s interests to help them improve their finances, as the payoff to the advisor improves significantly if this is the case.

As for the hourly model for ad-hoc work, this is targeted at clients who for whatever reason don’t fit into a standard category (roughly 2% of Jude’s book).

“They could be somebody who has worked with us on our standard fee schedule up to this point but need to move on,” he says, “We’ll convert them to an hourly fee, and they’ll pay for a check-up twice a year.”

Aren’t there any challenges with this model?

According to Jude, there are two challenges he has had to overcome.

The first is the sticker shock. “It’s very explicit,” he says, “No matter how you frame it, a fixed dollar amount feels like a lot more than the % of AuM people are used to.”

His method for overcoming this? Tackling the issue head on. The following is an example of a potential framing technique for a client who is unsure about the cost:

“I realize that what we’ve put in front of you is a big number. However, as a % of your overall financial life it’s quite small, and it’s a worthwhile investment in making better use of the assets you have. I’ve made it very clear what you are paying. If it stops being worth that, you can stop at any time.”

Jude is also in a position to point out to clients with large accumulated assets that they would be paying considerably more at another advisory firm (who would likely be charging them 30-40 bps more for the explicit AuM fee alone).

Another challenge he encounters is the question of why the fee levels should be constant year on year, when the amount of work itself may vary.

As is the case with all planning relationships, the workload in the first year is intense owing to the initial meetings, and this level of intensity declines in subsequent years.

Jude has an answer for this, “We frame the first year’s fee by saying that we’re giving a discount. We’re betting on you. If you walk away after 1st year, we would probably lose money.”

As we can see, acceptance of new fee models is much about the narrative as it is the dollars and cents.

The advantage of a fair and transparent model is that the narratives are far easier to construct. And if a pricing model truly makes sense, the narrative writes itself.

So is this the future?

Joe Duran of United Capital is fond of saying, 'If you own Gen X, you own the world'.

Most wealth managers are gambling that the HENRYs they currently turn from their doors will gratefully return decades later, when they have obediently accumulated the assets required to be considered worthy.

This assumption would certainly have been correct in the past, but only because there was no advisor to turn to as an alternative.

Advisors with an eye on the future should compare their offering to Upperline Financial, and ask honestly if it is compelling enough to win back such clients when they have formed a relationship with Jude's team, and or with other firms like his.

If not, it may be time to innovate.

“You have to educate people about how much they may have been paying before, and what they’re getting for what they’re paying now.”

Part VI

The Subscription Model

Key learnings

- Segmenting by client preference makes offer selection easy
- Up-front + Monthly enables a more accurate reflection of effort-to-serve
- Transparent (public) fee communication is the future

Traditional wealth managers will be increasingly aware of a new generation of planners, many of whom march under the banner of Michael Kitces and Alan Moore’s XY Planning Network (XYPN).

This movement has emerged to serve the next generation of wealth management clients, Generations X and Y (aged 25 – 54).

Gen XY have been historically overlooked by wealth management firms. This is chiefly because it is difficult to serve them profitably with the classic AuM-based model, given that Gen XY are not known for being overladen with excess, liquid assets to manage.

As well as offering services better suited to the needs of these clients, therefore, many among the XYPN movement are pioneering better ways of charging XY clients for their services.

Central to this pricing revolution is the monthly subscription model (akin, in more ways than one, to a monthly gym membership), which has been gathering pace since 2014. Kitces and Moore published a concise yet granular guide to implementing this fee model in 2016².

Monthly fees are no longer a curiosity, but a reality. The XYPN website lists approximately 240 planners who offer this model. A scan of 20 representative firms in this category reveals that these monthly fees range from as little as \$35 to \$595 dollars per month.

The existence of many such firms demonstrates that the fee model is a) acceptable to clients and b) profitable for those who offer them.

²*The Monthly Retainer Model in Financial Planning: What It Is, Why It Works, and How to Implement It in Your Firm*, by Alan Moore, Michael Kitces, Aug 16 2016

How is the Solari model different?

Within this new movement of planners, Michael Solari is an innovator among innovators.

As we observed in our prior report *Re-wiring Wealth Management*, it is typical for advisors to make virtually all the decisions on behalf of a client. This is true even in areas where personal preferences should hold sway (such as how often one wishes to communicate, and through which channel).

Not only is the client denied the opportunity to choose, but it is often the case what the client is given or entitled to is not clearly defined.

The Solari model is one of a (tiny) minority that recognizes that clients have different preferences, and reflects these differences by offering clear options, each with appropriate, transparent pricing.

Prospective clients are given three options for engaging with their advisor. Each option has a corresponding pricing model that mirrors the value delivered.

Option 1:

Delegator: This is the classic wealth management client, whom advisors everywhere know and love. He or she has money and problems, and is perfectly happy for an advisor to manage both.

Fee structure: Up-front fee (for the plan) + Ongoing fee (for investment management and advice).

Option 2:

Collaborator: This client wants to have a continuous relationship with an advisor, but wants to make the final decision on trades, and to personally execute on the various aspects of the plan.

Fee structure: Up-front fee (for the plan) and Ongoing fee (for advice, but not investment management).

Option 3:

DIY: This client wants a financial plan and is happy to take things from there. No ongoing interaction with the advisor is assumed (although it remains an option).

Fee structure: Up-front fee (for the plan), and Hourly fees (for on-demand service).

What's great about this model

The most striking feature of this model is that it makes sense. Trite an observation as that might sound, the link between value and price in most fee models is – to put it kindly – somewhat obscure.

For an age in which clients want the ability to personalize what they receive, and furthermore want to have greater transparency on what they are paying for and how they are paying for it, this fee model is hard to fault.

There is no part of the Solari fee model that cannot be cogently explained to the client. And crucially, it also makes sense from the advisor's point of view. Matching price with value is the best way to ensure and protect profitability.

“Most advisors,” Michael observes, “Have some clients that they like and some that they don't like, some that are very profitable and some that aren't. You should segment clients by personality and not just assets.”

What's the rationale behind it?

First of all, the fact that there is a choice at all acknowledges the fact that not all clients want the same thing.

Second, not only the fee structure, but the fee levels as well, are reflective of the value delivered.

For instance:

- *The ongoing fee is higher* for Delegators than for Collaborators, to reflect the fact that Delegators receive investment management as part of the ongoing service, whereas Collaborators do not.
- *The up-front fee* for DIY clients is *higher* than for the other two groups, reflecting the contingency that a plan might require additional refinement or clarification (which would in the case of the other two models be covered by the ongoing fee).

Third, the level of the fee within a given option is determined by the complexity of a client's situation and individual needs. Factors that go into this calculation include the type of retirement account (taxable vs IRA) and what level of income a client enjoys.

“I wouldn't charge a client double because he or she had twice as many assets as another client receiving the same service,” says Michael. “The fees should be based on the amount of work and the value delivered.”

Who is the target client?

Solari Financial started out with a client base typical of most advisors, i.e. consisting mainly of *Delegators*.

These are clients who are overwhelmed with the complexity of navigating the future, and seek an all-inclusive wealth management solution that includes investment management and overall planning advice.

Since investments are involved, Michael has an AuM requirement of approximately \$300-400k for this option. For those who cannot or will not hand over all their money, the other two options are available.

What sort of people tend to be *Collaborators*?

“They have a little bit of the DIY mentality”, Michael observes, “But they want you there along the way.” A physician client, for example, may be quite comfortable placing trades, or re-balancing a 401k. But often such clients also know instinctively that they need someone to “push them along”, so that they don’t drop the ball.

How about *Do-It-Yourselfers*?

The DIY client also tends to have a certain type of personality. “They like to interpret data and take their time before making decisions. A lot of them work in careers like technology.” This very attitude can also lead them into situations that require an advisor to help sort out.

“Sometimes they’re seeking help because they’re in trouble,” Michael states. “Maybe they were trying to run some sort of strategy online that ran into difficulties, and they need a bit of help.”

How do people make the choice between the three options?

This is the advantage of having a model built around client preferences. By definition, it is fairly easy to self-identify.

Michael has a questionnaire to help the process if needed, but can usually tell from the initial conversation what type of client he is speaking to. By doing thinking up-front, the first conversation can be made a lot easier.

Aren’t there any challenges with this model?

“Because most people don’t see the fee they are paying [for wealth management],” Michael relates, “When I say I am going to charge them \$300/month, it can be a hard conversation.”

The newness of the model means that for some clients, the fees require a certain amount of explaining.

Given that regulation, transparency and pricing pressure are quickly threatening the old, obscure forms of charging, this is a rationale for – rather than against – new fee models.

Michael points out, “You have to educate people about how much they may have been paying before, and what they’re getting for what they’re paying now.”

The education process is going to happen one way or another, so it might as well be through you. A fair, transparent model is much easier to explain than a non-transparent one.

One specific, knotty issue arises from the fact that most people aren’t used to paying an explicit fee for financial planning. This is a profession-wide issue, stemming from the fact that advisors typically have not charged for it transparently in the past.

Which brings us to another innovative aspect of the Solari fee model. As is common with many XYPN advisors, the fee model and levels are clearly displayed on the website for all prospects to see.

Along with the fees, freely communicating the fees conveys a confidence that the fees are reasonable, and also means that when clients do get in touch, the ‘sticker shock’ has already occurred and been processed.

Once again, this makes the conversation easier.

So is this the future?

In spite of the challenges, Michael believes that he and the other members of the XYPN are on the right side of history.

“Gen X and Y,” he says, “Are in many cases very wary of the larger firms. In the future, people might be paying using their checkbook, but they will know exactly what they are getting in return.”

Significantly, Michael does not seem to perceive his approach as particularly innovative (although it is – very – when compared to the rest of the profession).

As one of the next generation of planners, this nonchalance foreshadows an age in which the majority of advisors simply expect price models to be based on client needs and preference, and price levels to be completely transparent, as a matter of course.

This is great news for clients, and for advisors willing to dive headfirst into the future.

“The writing is on the wall for the traditional value proposition and pricing structure.”

Part VII

The Super-Retainer

Key learnings

- For ultra-high net worth clients, AuM-based fees are also ‘ultra-high’
- Fee caps enable a fairer and more competitive way to price
- Fees can still be six-figure number

In this report, we can see that pricing innovation in wealth management is not only a possibility, but already a reality. One might even go further, and say that it is a necessity.

There remains a potent objection to moving away from the all-in AuM fee, and it is the most important objection of all, particularly for those managing the assets of ultra-high net worth clients.

Show me the money!

Fixed fees, subscription fees, % of monthly income – can all translate into small potatoes from a revenue perspective.

This inevitably translates into lower profits and, as a consequence, lower growth.

Right?

Possibly ≠ Necessarily

It’s true that some emerging models are less remunerative than the traditional model.

This is due, in part, to the fact that many new players are not as motivated by profitability, or at least do not have 40% margins as their reference point.

XYPN co-founder Alan Moore, at the Disrupt Advice conference in September 2017, asked the room how many would be satisfied with a salary of 100k. Not a single hand went up.

He went on to say that the generation of planners he works with would be more than satisfied with that level of compensation. This has implications for the sustainability of 40% profit margins.

To take another group, retail banks, many of whom are enthusiastically rolling out robo-propositions, are in the unique position of being able to derive multiple revenue streams from a single client. Hence margins are not wholly dependent on one product.

Assuming the cost-to-serve can be managed, \$40 per month from a client who would otherwise have paid them nothing has the makings of an impressive business case.

But the points above all beg the question: does a shift of pricing model necessarily lead to radical decrease in revenues per client?

The short answer to that question is “No”. For the long answer, read on.

AdvicePeriod and the “Super-Retainer” Model

In future years, the history of fee development may hold a special place for the model pioneered by Steve Lockshin of AdvicePeriod.

It’s a simple model to explain.

You go to his office, explain your challenges, and write him a six-figure check.

The service Steve delivers in return is not primarily investment management. In fact, if you place those assets in an automated – or robo – platform, you will receive a discount.

His value-add, as the name of his firm suggests, is advice. Period.

What’s great about this model

When learning about this model for the first time, the reaction of traditional wealth managers – whether large or small – is generally one of disbelief, as it violates so many rules at once.

And yet, Steve’s business has grown its revenues by 100% each year since inception.

As one private banker remarked with grudging admiration, “He’s not hiding behind the AuM fee, but actually standing by the value he delivers”.

The fact that the model does not hinge on AuM is advantageous because it opens up the potential client base to those with insufficient, illiquid, or otherwise employed capital.

No clients are turned away – one, for example, paid a fee of just \$1,000 dollars (and was still profitable).

This is important in the context of the debate around whether new fee models enable revenue growth: since there are more potential clients, this inevitably means more potential revenue.

After the initial disbelief, the next question is, “How does he get away with it?”

Steve’s answer is disconcertingly simple. Most ultra-high net worth clients are

already paying six figure sums to advisors, and in most cases it works out as equivalent or less expensive to work with Steve.

This is a direct consequence of the fact that Steve puts more effort than most advisors into linking the fees to the value delivered.

What's the rationale behind it?

Steve has a calculator that enables him to price his offering appropriately given a knowledge of the client's situation. The calculator was built on a domestic plane journey – in other words, the logic is straight-forward (and hence likely to be comprehensible to clients).

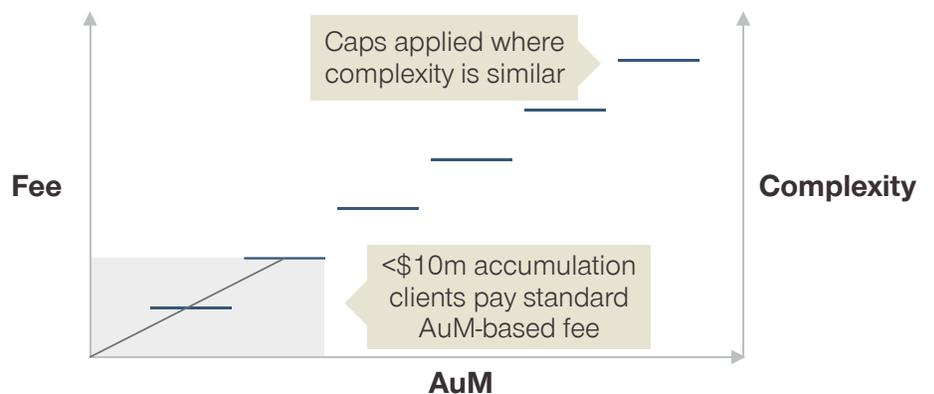
Let's take the example of a client with \$100m net worth, of which \$20m is liquid and \$80 million is tied up in the business.

Rather than rigidly applying a basis point charge to part or all of the \$100m, the eventual fee might be between \$100k and \$350k, depending on the work that needs to be done.

AuM does play a role, but for the majority of the book it is a walk-on role. Caps are applied in each segment, which is why the fees are ultimately competitive.

It is also a more equitable approach to fee management: Client A may have five times the net worth of Client B, but this does not normally entail five times as much work. Smart clients will figure this out for themselves. And in time, financial advice algorithms will figure this out for everyone, smart or not.

Fig. 12: Graded retainers



The calculator does enable Steve to adjust fees downwards where appropriate. This will occur when a client's situation becomes less complex. Again, price reflects value delivered.

In general, fees are actually increased by 3% every year to account for wage inflation (and no, clients do not push back on this).

Who is the target client?

The target client is Ultra-High Net Worth, which Steve defines as having a net worth in the \$50m to multi-billion dollar range.

It's important to note that the definition of 'target' is different from that of most wealth managers. Most advisors seek clients with high amounts of liquid assets because they cannot afford to serve them otherwise.

In Steve's case, it is because very high net worth clients tend to have more complex problems, and thus the potential to add value is higher.

(As already mentioned, Steve is at liberty to entertain clients of any size, shape or form. For those who fall below \$10M and are still in the accumulation phase, he applies a standard AuM scale.)

If AdvicePeriod has a patron saint, it is Angus MacGyver. Generally, you only send MacGyver on missions for which the armed forces or government agencies are inadequate.

Clients with net worth in Steve's target range all likely face hefty tax bills, the avoidance of which requires a creativity beyond that available at most professional services firms.

That is the core of the value proposition, and ultimately why Steve is able to stand by his fees with confidence.

Aren't there any challenges with this model?

Beyond the usual challenges of running a business, such as retaining talent, making technology work for his firm and ultimately for the client, Steve struggles to identify a challenge inherent in his fee model.

The model's value-based roots result naturally in certain clients calling after a few years to question whether the 1st year fees are appropriate to be charged in the 3rd year, given the disparity in workload.

In such cases, the fee calculator provides a basis for re-negotiating the fees, rather than an arbitrary 'give me a discount or I walk' discussion that can be awkward for both parties.

The main challenge with Steve's business, one suspects, lies not in the manner in which fees are charged, but in developing the capabilities to deliver on the value proposition, and the chutzpah to inspire clients who may initially be taken aback.

This is not a small ask. But as human advisors look forward to a stand-off with The Machines, it is a reasonable one.

So is this the future?

The fixed fee model of AdvicePeriod reflects Steve's view that the writing is on the wall for the traditional value proposition and pricing structure.

On the bright side, the emergence of the Super-Retainer is an inspiring story of the triumph of human ingenuity over commoditization and the gloomy specter of the price war.

As a tech savant and tech entrepreneur, he is unperturbed by what he sees as the inevitable automation of much of investment management and planning. If he is right, the rest of the profession cannot afford to be as sanguine.

“I think it should be a menu –
having it transparent up-front
also builds trust.”

Part VIII

Modular AuM-based Pricing

Key learnings

- Price challenges can be responded to with ‘value trade-offs’
- Value of Planning vs Investments can be separated
- Migration issues for existing clients are tricky, but can be overcome

The dilemma facing many wealth managers is the same across the world: clients are getting a clearer view of what they are paying – whether thanks to technology, or regulation, or both – and are starting to question the value of what they are receiving.

It’s possible to react to such questions by enumerating the particular strengths of one’s firm, whether this be superior investment expertise, responsiveness, or a network of professional experts.

An even better way to defend one’s value and prepare for such discussions is to parse out the specific components of one’s proposition, price them out, and offer the client a menu that makes it possible to tailor the service (and the price).

Privately-owned Australian asset manager and wealth advisory firm Elston, which has the tagline ‘Customized Financial Solutions’, possesses the rare distinction of actually delivering on its marketing promise in literal terms.

For this article, Nick Revis (Head of Asset Management) took us through the model developed by the firm.

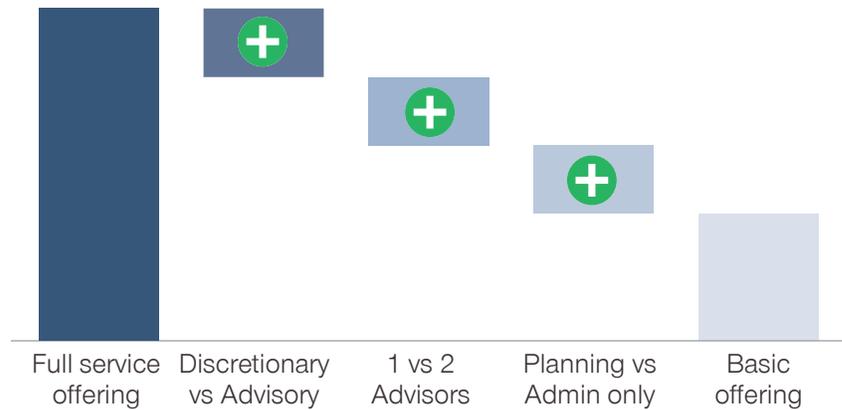
How is the model different?

The Elston approach to pricing is to present the client with a series of price-value trade-offs. In other words, to flip the price negotiation discussion on its head, and turn it into a value discussion.

Since the firm is a premium player, the full offering has the maximum value included.

If the client wishes to pay less, or does not see value in certain aspects of the full offering, he or she can trade-down. As we have explored elsewhere, this is a win for both the advisor and the client, since revenue and cost are linked and profitability is protected.

Fig. 13: Modular pricing, Elston Financial



Even if revenue per client is lower for the 'lighter' option, the fact that there is a lighter option on the table makes it possible to take on board more clients, as the price and offering are acceptable to an additional segment who might otherwise have gone elsewhere.

In terms of fee structure, clients are served a combination of FuM% (Funds under Management) and/or relative performance fee or absolute performance fee. Fixed fees and one-off fees are also offered as appropriate, giving even more flexibility.

What's great about this model

All-You-Can-Eat bundling – one price for as much or as little service as one requires – works well in certain contexts, but can perform poorly during times of fee compression.

This is because, by nature, it is not clear what is being charged for, and hence it is harder to differentiate the value of one offer from another.

Australian regulation is intensifying this trend by requiring the product fees to be split out from the management fees.

“One common issue during times of fee compression,” says Nick, “Is determining what is best for the client and what they are willing to pay for. As an example, do they need a strategy advisor and wealth advisor or are they happy to pay for just the former? In this example, the accountant may already be providing the strategy work. At the end of the day it is about providing a premium service that is appropriate for their needs or they see value in. It is about perceived value versus price.”

Breaking down the value into its components provides a basis for a more robust fee defense. Particularly if the platform or client has the option of taking the lighter option and the lower fee, instead of just beating down the price for the full service.

What's the rationale behind it?

The inspiration for the model sprang partly from the recognition that the needs of the client base were diversifying as the business grew.

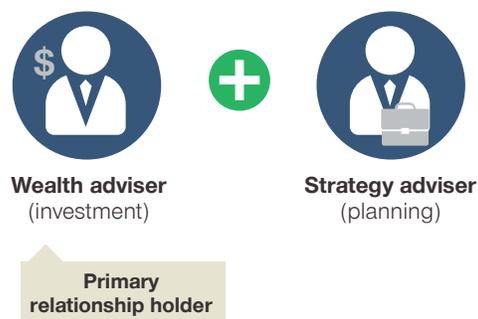
“You might have some high net worth clients and some with lower asset amounts, and they're all getting the same service. The higher AuM guys are paying a whole lot more but in many instances those with lower AuM amounts require higher levels of advice i.e. business owners/professionals. We're at the point now where that model needs to change.”

Elston began life as a brokerage firm, making revenues on a per transaction basis.

After the transition to a fee-for-service operation, the Wealth Advisor was joined by a second expert called a Strategy Advisor, who would handle the financial planning aspect of the client relationship.

The '2 Advisor Model' is a powerful proposition and fairly unique in the market.

Fig. 14: 2 Experts



The problem is that the service and price are not right for everyone. Some people want fully-fledged financial advice, and some just want investment management.

The natural consequence of this situation is variable fee enforcement – i.e. the use of discounts to attempt to tailor the price to the client's needs and price sensitivity. “Our tagline has always been about customizing fees, so advisors always had power to negotiate.”

This approach leads to complexity in keeping track of all the various price points.

It also leads to what Nick calls ‘the barbecue problem’. If all the clients were to get together and compare prices, it would not be clear why some were paying one price over another.

The formal structuring of ‘value-based discounts’ into the price model, by recognizing explicit service trade-offs, is a way of regulating price and standardizing service delivery – even without considering the additional clarity it brings to initial discussions with clients.

The additional benefit is that Elston are now able to clearly articulate the value proposition for each of the services.

Who is the target client?

The target threshold for assets is typically A\$750,000 dollars and above. Those who fall under this threshold are still considered, but likely served using a more basic platform solution.

Above this level, the flexible offering structure enables Elston to serve clients with a wide range of preferences – i.e. the range of ‘targets’ is much broader.

There is even a self-directed proposition in the works, aimed at clients who want full autonomy (i.e. in addition to the discretionary and non-discretionary options).

Are there any challenges with this model?

Nick is quite open about the fact that moving to this new model is not a simple process, and identifies four main challenges.

Process change: The first hurdle to be acknowledged is the initial administrative strain of ensuring that new fees are calculated and charged accurately. “When you implement a new fee structure, it might be simpler in the long term, but you triple your workload in the short term.”

Migration challenges: The second issue is to make sure that there are no unintended consequences arising from the new pricing schedule. For example, it may be that some clients see an increase in price without a corresponding increase in service. Price migration has the potential to be highly sensitive and requires appropriate care.

Consistent communication: The third challenge in rolling out the new price structure is to ensure that advisors know how to explain value. “Advisors normally prefer having discussions where the price goes down, not up.” Ensuring

uniform communication across multiple locations, particularly if these locations are nationwide, is part of this challenge.

Selection guidance: The fourth challenge is ensuring clients are not in a worse off position as a result of change in service, or that advisors are only selling the lowest fee option, because it's easier to sell on low price rather than high value.

So is this the future?

Nick believes this new model is in line with the broader developments in the wealth management profession.

“I think it should be a menu – having it transparent up-front also builds trust. Then it's not a negotiation (i.e. “The price is X but I want to pay Y”). It also provides consistency and allows us to invest in clients by reducing price longer term.”

If anything, the search for growth will inevitably lead wealth advisors to adapt to new segments rather than expect the reverse. If not now, pricing innovation is highly likely to be on the menu for wealth advisors in the near future.

Part II

Where next? The Road to Innovation

Stages of Innovation

There's a steep arc during times of innovation that begins with deep skepticism, and culminates in manic over-enthusiasm, before finally subsiding into the stability of a new normal. Here are some quotations from history that illustrate the stages of innovation.

Stage 1: Denial

“Everything that can be invented has been invented.”

Charles H. Duell, Commissioner,
U.S. Office of Patents, 1899

This confident assertion was made on the eve of the 20th century, which produced, amongst other things, the H-bomb, space travel technology, and the worldwide web. In wealth management, we do not need to wonder about whether this statement applies to the wealth management pricing model. As we have seen this foregoing pages, the fee model for wealth management is far from static or settled.

Stage 2: Ridicule

“Who the hell wants to hear actors talk?”

Harry M. Warner, Warner Bros, 1927

When an innovation (in this case, the ‘talking picture’) presents itself, denial gives way to derision. “Who is going to pay hourly fees?” was the incredulous response to Mark Berg’s then revolutionary hourly fee model amongst colleagues and industry commentators when initially launched. 10 years later, we have an answer: lots of people.

Stage 3: Complacency

“The Americans have need of the telephone, but we do not.
We have plenty of messenger boys.”

Sir William Preece, Chief Engineer, British Post Office, 1878

As an innovation ceases to be a novelty and becomes established, ridicule gives way to complacency. The dismissal of robo-like solutions as a millennial-only solution appears to fall into this category. Now robos are coming after the ultra-high net worth clients.

Stage 4: Over-confidence

“[By 1985], machines will be capable of doing any work Man can do.”

Herb Simon of Carnegie Mellon University, 1965

When the bubble of complacency is finally punctured, there is a tendency to over-extrapolate the pace of change. Herb Simon is remembered for his genuinely pioneering work in various fields, which included laying the ground for behavioral economics. This is pleasantly ironic, as linear projections are an inbuilt flaw in the human brain.

Stage 5: Insanity

“Nuclear-powered vacuum cleaners will probably be a reality in 10 years”

Alex Lewyt, Lewyt Corp., quoted in NY Times, 1955

Announcements of the death of AuM are likely to be highly exaggerated, and it is important to note that even comparatively archaic models such as ‘commission-funded advice’ are likely retain a contingent of clients who understand the deal and are happy with it.

The ideal attitude lies somewhere in between Complacency (resisting change) and Over-confidence (proceeding too quickly). Innovating successfully requires one to ground innovation in common sense and client needs.

Michael Kitces, industry commentator extraordinaire, notes “There have been a lot of advisors over the years who have preached new business models only to cause dozens or hundreds of advisors to follow and fail in their footsteps, as it turned out that what the advisor has pioneered was not actually systematized, scalable, or able to be generalized beyond their own niche practice.”

If there’s one thing that we as a professional pricing firm can state with firmness, it is that professional pricing is a tricky business. Innovating in the wrong way can lead to low growth or negative profitability, or both³.

What the examples of innovation do show, is that it is possible to innovate on price and remain in business. The next question is how you innovate on price and grow profitably.

If the status quo were an option, maybe that would be that. But given that Pandora’s box is now open, if no one answers the question of profitable growth, low-cost models could simply take over the profession. Which would inevitably mean that low-value offerings will take over the profession. Not good.

³Monetizing Innovation: How Smart Companies Design the Product Around the Price (May 2 2016) by Madhavan Ramanujam & Georg Tacke, provides a concrete overview of how to approach pricing innovation in a methodical way.

Particularly with 'fixed fee only' type models, it is very easy for costs to grow faster than revenues as the firm expands, causing a bottle neck.

This is not the fault of the fixed-fee model, but of approach to price level setting. The least sophisticated approach to pricing is 'cost-plus' (i.e. cost-to-serve plus target margin). It contrasts with the ideal pricing approach, which is instead based on willingness-to-pay. If you want to know the difference, check out the cost to produce movie theatre popcorn, which is typically marked-up by about 1,275%.

The missing ingredient in cases of 'expansion-driven overload' is generally a poor understanding of willingness-to-pay ('cost-plus' is no substitute for calculating willingness to pay, and can lead to major pricing problems later on).

We know, however, from other industries that a willingness-to-pay approach is possible. When was the last time you heard someone in a bar bragging about how they own the cheapest clothes, the cheapest car, buy the cheapest jewelry, eat in the most inexpensive restaurants, and live in the cheapest area of town? All of these items have value to people beyond the mere cost involved. Wealth management is – and should be – more important than all of these things, because wealth is what enables spending in the first place!

The fact that people brag about paying 'just 30 bps' stands testament to the failure of wealth managers to articulate, differentiate and monetize their value in the same way that other industries have done.

The Case Against Innovation: A Dialogue

Now, we'll look at some the genuinely relevant objections to tinkering with the status quo, and identify ways to mitigate the potential for error.

The following takes the form of a dialogue with an open-minded skeptic, and is intended to address the questions that arise in the mind of a wealth manager when contemplating fee innovation (particularly if business is looking good currently and there is no obvious reason to change).

Skeptic: First of all, let's get one thing straight. I'm not getting rid of AuM fees. They work for me and they work for the client.

Simon-Kucher: Totally agree. The AuM fee is going to be part of wealth management for as long as wealth is managed.

Skeptic: Then why do you keep talking about 'fixed fees' and subscription fees, and drawing charts showing how AuM fees are 'problematic' and...

Simon-Kucher: There is no fundamental problem with the AuM fee provided it isn't the only fee structure. Improving price sophistication will be a question of adding models rather than replacing the existing model with something else entirely. It's just business sense to have an alternative fixed-fee option for those who don't have assets or don't want to hand them over (i.e. the majority of potential clients). This opens the door for those clients, while ensuring that you remain profitable.

Skeptic: Well, good. And is that your main point?

Simon-Kucher: It's one of them. The other problem that most advisers don't just have a single AuM-based price point, but also a single offering, generally All You Can Eat, rather than choices for how clients want to be served.

Skeptic: I have a fairly clear view on that: we shouldn't be offering clients choice. Period.

Simon-Kucher: Go ahead.

Skeptic: So many reasons. Confusion for the client, difficulty in implementation, issues with delivery....

Simon-Kucher: Let's take one at a time.

Skeptic: Okay, well here's one to start off with. Let's say I've come up with a new, differentiated pricing model that offers choice. Well, what does that mean for my existing book? Under the new pricing, clients are going to be either paying more or less than they are now. That means an instant revenue hit from the ones I adjust downwards, and it also means I've got to tell the other clients that I'll be charging them more for the same service!

Simon-Kucher: The issue of migration (i.e. what you do with your existing book) is always a sensitive one. When introducing a new pricing model, we find it's generally unwise to opt for a 'hard migration' (i.e. move everyone to the new pricing schedule), which is the scenario you're outlining here.

Skeptic: Hard, soft – whatever. The issue is that whenever you change price, you have to literally get them to sign a new agreement that they are happy with it. The physical act of having to read over a new agreement to make sure nothing else was “snuck in” even though we would tell them nothing else had changed, combined with the physical act of signing a new document to increase their price....it is not an appealing event for a client.

Simon-Kucher: Raising fees substantially is particularly problematic if there is no improvement in the underlying offering. Unless you are increasing the value for the clients with the higher price, grandfathering (keeping all clients on their current schedule) is a good default position, with the option of applying judicious price increases for clients who are towards the lower end of the scale and are clearly unprofitable.

Another option is to create an exclusive offering at the upper end (with restricted features such as direct access to the founder of the firm), in which case it is possible to give clients the option of paying a higher fee for this restricted offering or keeping their former fee and former service level. Creating this exclusive 'upper layer' takes serious thinking, work and investment.

One of the advantages of fixed \$ fees versus bps, is that you can regularly raise fees by 3% and people get it because of inflation.

Skeptic: All this is well and good, but let's back up for a second. My retention rates are 98%. My business is more profitable than virtually any other business you can name. I see no reason why I should even take a 1% risk of upsetting the apple cart. So far as I can see, the only result of introducing 'choice' and lower price points would be to make my clients re-assess whether they are overpaying for what they already receive.

Simon-Kucher: You do have a great business, and the industry has hummed along incredibly well on the 100 bps, All You Can Eat consensus up to now. The point is more about future-proofing your business than optimizing your current book – although if you do it right, you will become more profitable in the short-term as well.

A price model change would for the first time make it possible for you to restrict services to lower-paying clients or and justify charging more for clients with greater needs. All your clients will be profitable, your proposition will be easier to defend against cut-price attackers, price negotiations will be easier, consistency in adviser-client conversations will persist as the business grows.

Skeptic: Yeah I get the theory, but it doesn't chime with the reality of my business. I don't need any more 'structure' in my proposition. I'm targeting clients who have complex needs and complex investments. I don't want to have clients who have 'basic' needs - why would I introduce the possibility of a 'lite' version of what I do? Focus is what got me where I am today.

Simon-Kucher: Focus is key, and if you want to exclude certain types of clients, this is a strategic decision. However, in our experience, even within a tightly defined target segment (such as dentists approaching retirement), there will be differences between clients not necessarily connected to complexity or planning needs.

Even when working with 'commodity' businesses, we have never found a client base that was entirely homogeneous. For example, there are sixteen personality types, and that means sixteen different ways of interacting, each of which will place differing demands on your time and business resources. You might have a high-maintenance client that can't focus without a bowl of red M&Ms at every meeting. You or someone in your firm needs to take time out to sort the M&Ms – and that is a preference that you need to price in to the fee.

Skeptic: What if we as a firm believe that high touch service/high interaction/holistic planning is really the right answer for our clients and if you do not want it then do not sign up?

Simon-Kucher: Again, not everyone will want or need the same level of 'high-touch' attention. But furthermore, it's really important to understand the difference between what a client has the right to choose (red M&Ms – dependent on preference) and what you have to decide for them (simple vs complex financial plan – dependent on life situation). You might distinguish between 'neediness' (client choice) and actual 'need' (adviser discretion). Currently these two aspects are not separated, and hence 'choice' is not possible.

Skeptic: Okay, but even if all that were true, if I start offering different versions of my proposition, this will negatively affect my brand. High end customers do not always want to see you also offering the basic stuff.

Simon-Kucher: First of all, versioning does not necessarily need to mean offering stripped-down 'basic' versions of what you do. Coming up with a 'basic' offering will be of great importance to advisers who want to go deeper into 'blue ocean' territory, but having a structured proposition doesn't necessarily lead you in this direction. An alternative to 'Good Better Best' is the Modular concept (core + modules), which simply allows one to tailor a proposition to fit one's needs, like a high-end suit, or a luxury car.

Skeptic: Please, no more analogies to other industries. And also, to come back to a point I made earlier, how is offering menus going to affect my operations? Building an organization to serve all of those wide ranges of different

segment levels is actually pretty complex, and the skills needed to serve each one are different in terms of who you hire and grow.

Simon-Kucher: If you want to target segments with different needs, you'd have to hire new people anyway. But offering choice does not necessarily require this, if you are simply restructuring your offering to better reflect the needs of your existing base, whom you already serve in various ways.

I'd guess your advisers have methods of dealing with this: for example, a spreadsheet with a list of clients whose calls they answer first. It's more a case of systematizing what you already do across the client interactions, and communicating it externally.

Some firms have internal gradings for clients such as bronze, silver or gold. It makes business sense to do so and actually, after the initial effort, makes things easier. For one thing, the difficulty of explaining your offering and value – something which everyone everywhere agrees is a problem – should actually reduce, given that there is now a story to tell.

Skeptic: That sounds too good to be true.

Simon-Kucher: Well, there is a proviso. Messing with an existing pricing model is a deceptively difficult task, and very easy to get wrong. Most advisors know this, and that's why people are leery of innovation. They are right to be.

If you don't get the menu just right, and price levels aren't near perfect, you will experience unexpected consequences, which are seldom positive – generally people tend to over-complicate and under-price. This is why pricing transformation projects in our experience take months, and require rigorous study of actual behaviors, together with price sensitivity and business case modelling, before you even get to the nuts and bolts of how to make the offer look and how to deliver it. Unfortunately there are no short cuts.

Skeptic: That's what I don't like, all of this effort just to take a massive risk changing an idea that already works.

Simon-Kucher: But it's a massive risk to assume that the current system will continue to be subsidized by high AuM clients paying for...

Skeptic: Yes, alright you don't have to ram it home, I get it. My point is: I don't get the need for all the hocus pocus. Solving the problem should be fairly simple: just add a minimum fee to protect the profitability of low-AuM clients, and maybe offer two options for service, one investments-only and one holistic. There, problem solved.

Simon-Kucher: There are many solutions, and this could be one of them. But only if you have basically two types of client, and you're sure that the ones who want 'holistic' services all have very similar needs. Even then, it's not psycho-

logically optimal to force a choice between two options – one cheaper and one more expensive. More people will opt for the cheaper option, a significant portion of whom might have opted for a middle option instead had it been there. At least three choices is generally a good number.

Skeptic: What do you suggest then?

Simon-Kucher: As I said, it's different for every advisor, which is why we answer that question by doing projects.

Skeptic: Sorry, but I'm nowhere near the level I'd need to be convinced in order to invest months with a paid consultant to solve this problem. You're going to have to do a better job of inspiration. Shoot.

Simon-Kucher: Okay, let's discuss some of the ideas that are already out there. If you're looking for alternatives to the 'investment-only vs holistic' model you just outlined, the 3-part model (Model #2 in this report) draws attention to the value of planning and ongoing support, whilst allowing for differences in need within each area, and retaining an AuM-based component. That's a pretty good start.

Skeptic: Okay, but the challenge with combining 'choice' with split pricing models like that one is that consumers tend to 'understand' asset management for AUM fees more than financial planning for planning fees. Which means when the pricing gets segmented, consumers often choose the easy/familiar one (AUM) and reject the less unfamiliar and uncertain value proposition (financial planning). Then the financial planner ends out with a lot of investment-only clients who don't do planning, who turn out to be less valuable clients (weaker relationship in AUM-only) and then perceive less value from the advisor (didn't buy planning, only investments, so sees the advisor as investment-only).

Simon-Kucher: That can happen. But it doesn't need to. Our survey showed that only a minority of clients believe asset management is more important than planning, and that 83% believe planning to be as important or more important. The burden appears to be on the profession to communicate the value of planning. And the bar is set pretty low as of today.

A further point, when a firm doesn't have an explicit fee for planning, internally this means that planning is treated as a cost center, with investment functions treated as the revenue-earners. This can have a knock-on effect on resource allocation as time goes on, and the culture of the firm too. Not a great strategy for a future in which the main value is going to come from what we deliver over and above asset management.

Skeptic: I buy the planning argument. But taking this third thing 'ongoing support', I'm highly skeptical.

Simon-Kucher: Why so?

Skeptic: How many would accurately self-select their 'ongoing service level' needs? If the person has never really worked with an advisor before, how do they really know?

Simon-Kucher: That's an excellent point. At a bare minimum, you need to address this problem head-on by setting out for them the various ways you can support them: providing access to resources / seminars, fielding enquiries from them (financial / emotional) and proactively chasing them to ensure they execute on their goals.

So few advisors do this, and this makes it near impossible for people to assess what their ongoing needs would be. They may well be unaware of the ways they can use you, and this means they are more vulnerable to a tempting low-ball offer from an advisor that does not offer substantial ongoing support.

Skeptic: But I still don't get how are they supposed to know how much support they need if they've never used it before.

Simon-Kucher: The simplest approach is to let them know your hourly rate and track the hours used – then they don't need to know in advance. This plays well with a 'pay as you go' target client, which Mark Berg has shown (Model #1 in this report) is actually a substantial segment.

Skeptic: I don't know about that – in my experience clients hate it when you send them massive bills for what they thought was a casual conversation.

Simon-Kucher: Right. Framing is super-important. What Mark actually does, if you go to his website, is let people know how much they will probably be looking at as a range, based on their life situation. He has a chart where he showed the relationship between your circumstances and the level of advice you will need, on his website. That transparency is what makes the difference.

Skeptic: I'm sure it works great for him – I just don't want to get into hourly fees.

Simon-Kucher: Well, that's not the only option for ongoing support. You can take his approach one step further and calculate fixed fees for the different usage profiles. You'll want to use your hourly rate as a floor price when you're doing your calculations, but you'll also want the price to reflect willingness-to-pay. Then charge quarterly or monthly as appropriate. This lets clients know where they stand. And if it turns out people are straying from their predicted usage profile, that's a conversation for next year when re-assessing the fees (see Model #4 in this report).

The most important thing is to make them aware that the option is there and then make it possible for them to find their appropriate level through experi-

ence. The levels give you some goal posts to measure usage against, if nothing else. You might find that the levels become more clearly defined over time.

Skeptic: How awkward will the conversation be when you call them up and say “you have been exceeding your allowed number of calls to your team”? Or when their parents get sick and they call frantic for help about estate issues with their parents and finding the right long term care and you tell them “Well we could help you but you need to step up to the gold package for us to do that”?

Simon-Kucher: There’s clearly the potential for mistakes and disasters if it’s done without thinking through such situations in advance. Part of the reason this thinking is required is that we are coming from a position where there was no clear link between value and price, so naturally any moves in the direction of charging for value could appear seem unfair if not framed correctly.

People in transition are a special case, and individuals in these scenarios will be incurring various expenses alongside ours. If there is a reference point for, say, what an hour of your time is worth, one could scope out a project fee for the intense support required during a transition period, based on a discounted hourly rate as a sign of goodwill. The problem only comes when the reference price for your time is zero. Beth Jones (Model #2) provides an example of how this can be handled sensitively.

Skeptic: I’m listening to you addressing all these problems, and I can’t shake the thought that none of these problems exist in the current AuM-based fee.

Simon-Kucher: First of all, problems are good. A problem-free business is one that everyone will pile into, (until you have problems again). Second of all, by evolving your pricing model you are trading in a set of insoluble, existential problems for a set of difficult yet solvable ones that will actually make things better for everyone if you solve them.

Skeptic: I’d still feel more comfortable refining the current model than changing it materially. What can’t we just choose that problem to solve?

Simon-Kucher: The problem is that AuM is fundamentally a poor-performing proxy for client needs.

Skeptic: Disagree. Sure, there can be lower maintenance and higher maintenance people at all levels of wealth, but the complexity of their situations is actually decently correlated to their wealth at least in buckets (e.g. under 2 million vs. 3-5 vs 5-10 vs. over 10 etc.).

Simon-Kucher: Okay, so let’s address this point properly. The problem with AuM is not that it isn’t correlated with complexity – it is. The trouble is that it’s not correlated precisely enough, and that matters. A client with 5m is not five

times as complex as a client with 1m. A client with 15m may or may not be three times as complex as a client with 5m.

Another way of looking at it is that complexity is a poor proxy for 'neediness'. It's like only considering the distance covered in a plane journey without considering the cabin, or the check-in and post-flight experience.

Skeptic: I thought I told you – no more analogies from other industries!

Simon-Kucher: This is the last one, I promise.

Skeptic: Alright.

Simon-Kucher: Thanks. Some people want a chauffeur to the airport, even if the flight is from New York to Boston. Similarly, some lower complexity people still want a family-office experience, and we should take their money if they're willing to pay for it.

Building on this line of thought, most of the people you see flying first class are wealthy, and most of the people you see in economy are middle income – income and cabin class are correlated. But it would be incorrect to insist that the price for a first class ticket be calculated as a % of your income, stipulating a 'minimum income threshold' to make the numbers work, and with passengers in the same cabin paying different multiples of the ticket price.

Adviser: As I've said before, I don't want 'economy' clients. Most of my money comes from AuM fees, and I need clients with assets – that's just the way it is.

Simon-Kucher: Alright, let's take your ideal clients, the ones who have assets. Did they have those assets 10-20 years ago?

Adviser: I see where you are going with this, but I don't chase younger clients. When they reach my target AuM zone, they will start to realize that their current firm was not built for them and does not have the level of expertise they need. I don't need to find them. They will come and find me. And if they don't, I probably don't want them anyway.

Simon-Kucher: Are you positive that they will come to you? The minimum threshold model works on the assumption that clients will come back once they pass the magic wealth threshold, and that's certainly an accurate description of the past. For the future, though, it's a hypothesis that is as yet unproven.

It's important to remember that sub-threshold clients have traditionally had very few full-service wealth management options open to them till now. With the emergence of XYPN-style full-service propositions (Models #5 and #6 in this report), that's no longer the case. If the future investor is more intent on understanding what he/she is receiving, matching price to value, tailoring the service level etc., it would be incorrect to assume that they will switch away

from a provider who gives them this to one that doesn't, simply because they have reached a certain level of wealth.

Adviser: Look, I've just realized something else. All this talk about 'structure' doesn't make sense for my business. Our advisers give a fair amount of discounts – that's a reflection of tailored pricing for specific client situations. For example, clients we know are going to be easier to serve or lower maintenance. Why make the client figure it all out when we can retain the control?

Simon-Kucher: That's great if it works. But unless you're very different from the private banks we've worked with, the discount policy is going to vary from adviser to adviser, and come down to a combination of client negotiation skills and adviser communication skills. When we run the numbers, there is rarely a discernible logic governing pricing across the board.

Even if we assume that all advisers are applying the logic consistently, and communicating the value of the proposition accurately, the larger the firm grows, the more dispersion you will see with respect to these two points.

Having a pricing-value logic baked in – whether through external structure of the proposition, or internal discounting rules, is vital. We've seen what happens in organizations where it is a free for all, and it ain't pretty. The advantage of having it external is it makes things easier for the client to understand, which may be increasingly important for the clients of the future, who expect to understand everything.

We leave the dialogue here. If you have any topics to raise that are relevant but not discussed here, please reach out, and we'd be happy to continue it!

Framework for Innovation

To conclude, we'd like to offer up a framework that we have used successfully to help companies create a value-based proposition with the offering and pricing built around the client.

Transparency: What do you want to do?

Primark and Burberry are both great businesses, with completely different pricing strategies. Your pricing approach should have its roots in what you want to achieve.

- **What are your strategic goals with regards to proposition and pricing?**
 - If you don't have a clear 'why?' you cannot have a clear 'how'.
 - Do you want to be a low-cost player with wide-reach and low-touch relationships? Do you want to operate across niches?
- **How do you define your unique value proposition, and where are its competitive advantages?**
 - Understanding your competitive strengths helps give clarity to what premium you can command.
 - What specific strengths do you have or services do you offer that qualify you to succeed in following your strategy?
- **How do you segment clients with regards to needs?**
 - If you're going build your proposition and pricing around your target clients, you need to know what they actually want.
 - Do all of your target clients want the same thing? How do they differ and what does mean in terms of what you should offer?

Intelligence: What are you going to do?

If you know what you want and what your clients want, the next step is to take what you can do and build an offering and pricing system that fits both.

- **How is the product portfolio designed to address the needs of client segments?**
 - Take the segments you have identified and see how the needs cluster.
 - Should you have 2-3 versions of your offer? Does it make sense to have a separate list of 'add-ons' charged in addition?

- **How do you charge for its value and capture willingness-to-pay?**
 - The right price is a question of structure as well as level. Willingness-to-pay, not cost-to serve, should determine both.
 - Do you know what clients really value amongst the various services you offer and how much?
- **What is your discounting policy? How systematic is it?**
 - There should be rules that link price negotiations to i) value delivered and ii) client commitment (give and take).
 - If challenged on price, are you in a position to defend the value of the proposition?

Execution: How are you going to do it?

There's many a slip betwixt strategy and implementation.

- **How do you effectively communicate the value of its products and prices?**
 - Are your communication materials written in priestly jargon, or is it possible to understand what you do and why you are different?
 - Can people clearly link what you charge to what you offer, so as to avoid false comparisons with lower value offerings?
- **What type of negotiation support do you have for initial sales conversations?**
 - Digital presentment systems not only help to guide conversations, but also help capture data about these conversations.
 - Do you have dynamic tools to assist in client conversations, so that value communication can be systematized?
- **What internal capability do you have to manage products and pricing?**
 - Pricing should be reviewed regularly on the basis of experience and data, to identify problems ahead of time.
 - Do you track price enforcement, client-level profitability, and expected / actual client behavior following conditional discounts?

The practice of professional pricing is not without difficulty and requires involvement at every level of the organization. This is partly why pricing is sub-optimal in many companies.

At this point in the development of wealth management, it is more important than ever to take a professional approach to avoid ceding the argument to price warriors, at the expense of value.

We're happy to share our experiences helping companies work through price wars by defining robust value propositions and price structures. Whatever you decide, good luck, and good battle!

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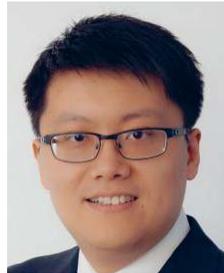
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Simon-Kucher & Partners at a Glance



Simon-Kucher & Partners, Strategy & Marketing Consultants

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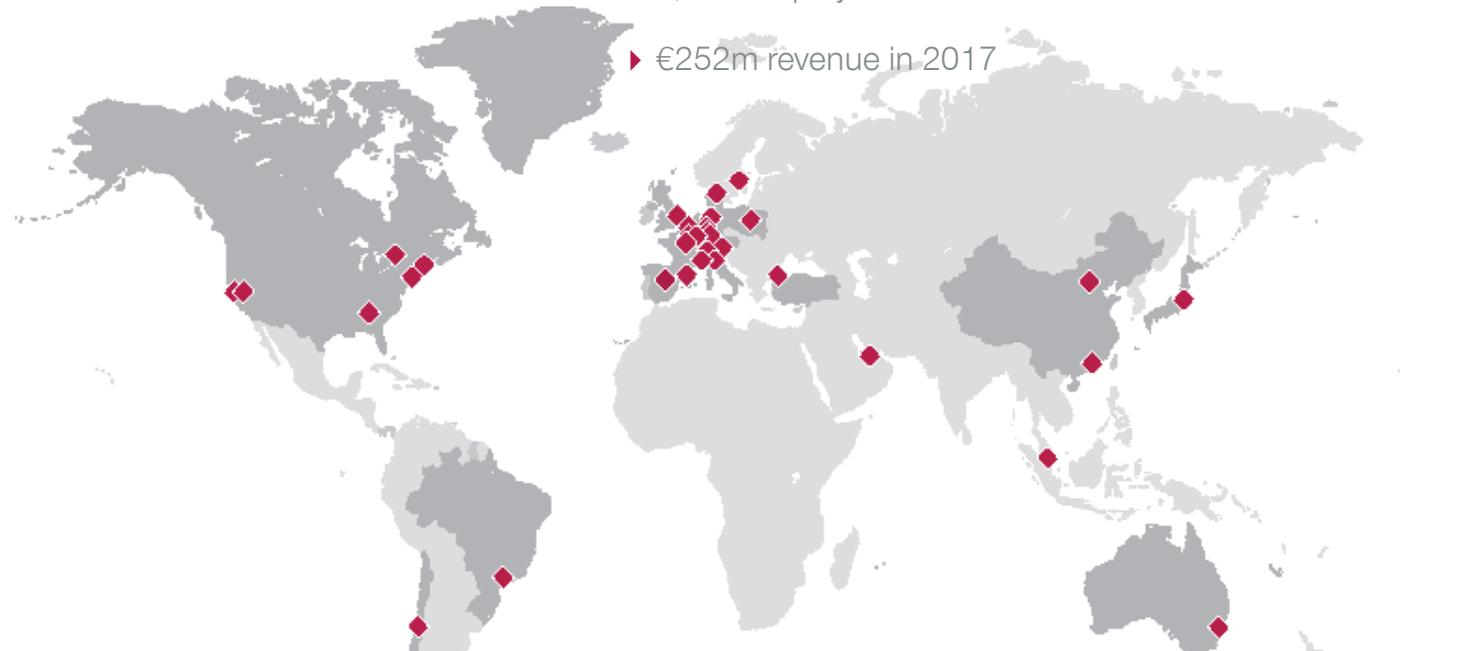


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▶ 34 offices worldwide

▶ 1,100 employees

▶ €252m revenue in 2017



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- USA, **Boston**
- USA, **Mountain View**
- USA, **New York**
- USA, **San Francisco**

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- Belgium, **Brussels**
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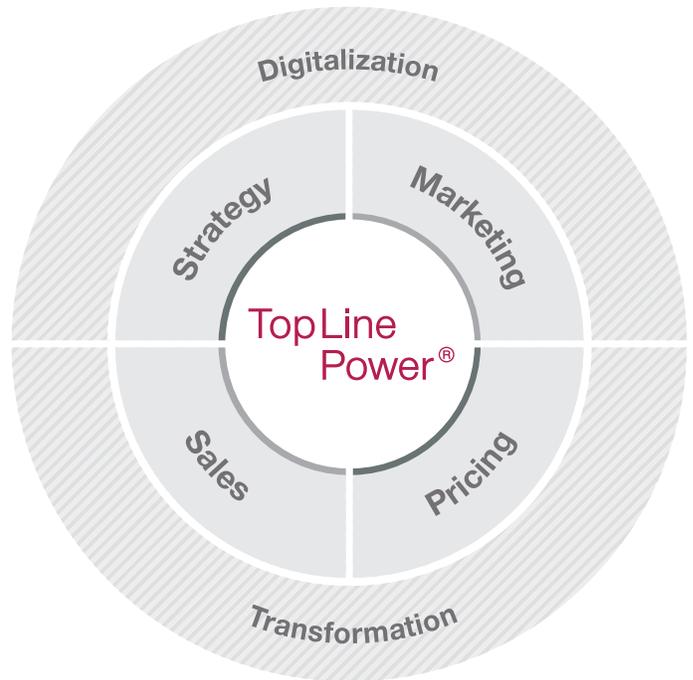
Asia/South Pacific/ Middle East

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- China, **Beijing**
- China, **Hong Kong**
- Japan, **Tokyo**
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"Pricing strategy specialists"

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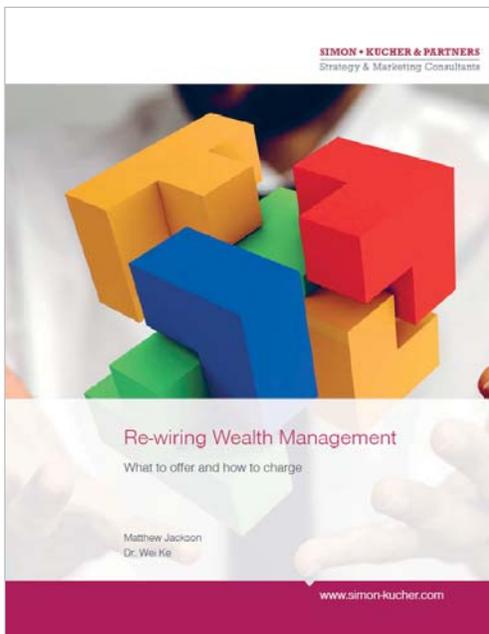
"... in pricing you offer something nobody else does"

Our publications on Wealth Management



Pricing for Growth in Wealth Management

- The wealth management industry is on the cusp of major change. How quickly it happens depends on those prepared to innovate. This has implications for the proposition and how it is structured, how we charge for value, and how we persuade clients that the value is worth the price.
- In this document, we cover all three topics using insights we have gained from other industries facing disruption, increased competition and pricing pressure.
- Given technology, regulation and changing client behavior, the need for innovation is likely to be ongoing. Those who move first are likely to remain ahead of the curve.



Re-wiring Wealth Management

- One of the much needed changes for the wealth management profession is the introduction of choice for the client. Since not all clients want the same things, choice will help improve satisfaction, reach and also profitability.
- In this survey of over 1,000 wealth management clients, including a mix of traditional (55+) and non-traditional (XY) respondents, we asked clients what they would choose if they had the choice.
- As it turns out there is a clear opinion amongst respondents with respect to how they want wealth management delivered and how they would like to pay. This survey provides a solid case for the re-invention of the traditional model.

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