**Straddling the Peak**

Balancing Excellence and Profitability with Ultra-High-Net-Worth Clients

By Mark Tibergien

To a growth-minded firm owner, ultra-high-net-worth (UHNW) clients beckon to advisors as sirens to the sailors. They offer the promise of interesting and challenging work, highly personal relationships, substantial revenue, and the opportunity to grow referral business within an elite sphere of influence. However, as many advisors have discovered, the rewards of serving such clients come at a cost. UHNW individuals expect the highest level of excellence from every product and service. They demand constant availability and rapid response. Advisors need a deft hand with complex family dynamics, as well as a keen eye for intricate financial, legal, and regulatory issues. Meeting these challenges requires serious investments in infrastructure, technology, and talent. Also, if one UHNW client leaves, the sudden loss of revenue can imperil the stability of a firm that is not designed to withstand such disruption.

The question is, are UHNW clients worth it? Can a firm really strike a balance between the exacting needs of its clients and its own imperatives as a business? The answer is yes, so long as a firm structures its business model carefully. The key is to find the right clients, charge them the right fees, and take the right steps in advance to protect the firm from a potential client loss.

**How to Find the Right Clients**

Whether your firm is trying to break into the UHNW circle or simply refine its existing business model, the first step is to define the optimal client based on a clear vision of where you want your business to be. Often, advisors who are new to this space mistakenly think UHNW individuals are a homogenous segment. However, net worth alone does not define this market; wealthy people are astonishingly different from each other and have distinct needs. For example, families with inherited wealth—whether in liquid assets or in the form of a business—often struggle with complex family dynamics. They may need help with family governance, ideas for protecting the interests of members who will not be involved in a business, or mentoring to prepare the next generation for wealth. By contrast, a tech entrepreneur may be the only wealthy individual in his or her family. Instead of financial counseling for extended family, he or she may be looking for professional advice about financing or investing in new ventures. A senior corporate executive faces issues that include concentrated stock exposure, restricted stock positions, and regulations involving control persons and requires an advisor with specialized expertise in those matters. Personalities vary as well. Many wealthy individuals pride themselves on being very down-to-earth and like to work with unassuming advisors. Others prefer more formality. Some want an advisor they can contact with every need and question, while others are looking for a set-and-forget type of relationship.

The point is, no single advisor can serve every type of wealthy client—at least not profitably. Each type requires a different service offering, contact frequency, staff expertise, and office infrastructure. The key to profitable relationships is targeting the ideal client: the one who makes a uniquely good match for a firm’s skill set, personality, and interests. This targeted strategy can pay off in multiple ways. It typically results in clients who are more satisfied and more engaged with their advisors. It also can lead to sources of qualified referrals from engaged clients who see the advisor as part of an inner circle.

To target an ideal client, start by looking at your current clients and assess which ones you would want to replicate. Which existing clients seem most engaged and provide the most referrals? Who demands an extraordinary amount of contact and service to remain satisfied? What personality types mesh best with the firm’s staff? Who is profitable and who is not? By evaluating every data point imaginable—not simply assets under...
management, but also profession, age, family structure, cultural affinity, and so forth—you soon can flesh out a portrait of an ideal client. This picture tells the firm whom to pursue and whom to avoid. It also develops a compelling value proposition because now you understand the specific needs you should try to meet as well as the story you should tell.

Setting the Right Fees
Once a firm identifies which clients it will serve, then it must decide how and what to charge them. The link between pricing and profitability seems blindingly obvious, but it is one that deserves closer attention from advisors. Many firms simply hew to traditional industry norms for asset-based fees. Others look at their competitors’ pricing first—a potentially perilous strategy. Surprisingly, only a fraction of firms consider the actual costs of delivering services as part of the pricing strategy. Yet in a highly service-intensive segment such as the UHNW market, it is absolutely critical for advisors to understand their cost structures. Otherwise, they have no way to calculate whether they are breaking even with pull-out-all-the-stops service, and they have no clear path to higher profitability.

Determining a break-even point for every client and service may seem daunting, but it is really just simple arithmetic. The basic rule of thumb for estimating the cost of any complex effort—whether it is a large software development project or an advisory service—is to work from the bottom up. Start by estimating the smaller building blocks of a project, roll them into larger components, then finally calculate an overall cost. First, an advisory firm should set hourly rates for every professional and nonprofessional. Simply divide each individual’s total annual compensation by the number of client-related hours worked per year. With these rates in hand, a firm can calculate its labor costs to perform each activity—say, 20 minutes for a client service manager to set up an appointment, or an hour for a principal advisor to conduct modeling. Then, these costs can be combined to find the total cost for a larger task, such as signing up a new client, conducting a family meeting, or formulating a complex estate plan. By adding up all the tasks performed for each client, it is now possible to see the total labor cost of service. All that remains is to allocate to each client a share of the firm’s overhead. Now the firm can see its break-even point for each client. To arrive at an actual fee, the advisor can add its target profit margin (typically 20–25 percent in normal times, a bit less in uncertain times such as the past few years).

This exercise can be a bit time-consuming, but most of these calculations need to be performed only once every year or two. More importantly, the exercise can be revealing for advisors who serve ultra-wealthy clients because it answers the question about which clients are profitable—and which are not. It also helps advisors understand what to charge and which services to offer to maximize profit potential.

In addition to setting price levels, you need to think about pricing structure. Some pricing structures make more sense than others—for both the firm and the client—depending on a firm’s particular offerings. Options include:

Asset-based pricing models. The traditional favorite, this pricing structure is easy to administer. However, it provides no explicit payment for services other than investment management, such as tax or estate planning. In addition, the fees generated by larger portfolios can seem hard to justify because there is no clear link to the value actually delivered. Wealthy clients might suspect they are subsidizing smaller, less-profitable relationships.

Flat or tiered dollar fees. To generate revenue on services other than investment management, some firms charge either a flat dollar fee or a fee that varies according to the complexity of a client’s needs for advice. With this fee structure, a firm can be certain all of its costs are covered. The challenge here is building a strong value story that is credible to wealthy clients, and then clearly delivering the services as promised.

Hourly fees. As with flat fees, hourly fees effectively capture all of a firm’s costs in delivering advice. However, keeping track of billable hours requires a serious investment in infrastructure, and each staff member has to commit to tracking their own hours.

Value-based pricing. In this approach, clients pay for the outcomes they receive. For instance, a fee may depend on the amount of tax savings due to asset restructuring, or making a significant donation to a particular philanthropy. This approach can help a firm support a premium pricing strategy because it explicitly connects fees charged to value delivered. A big challenge, of course, is to actually deliver the outcomes for which the clients have agreed to pay.

Combination approaches. Because each type of UHNW client is unique, each may require a somewhat different pricing structure to remain profitable. For example, asset-based fees may cover costs for investment management, while flat or hourly fees may be more appropriate for tax and estate planning. If clients and advisors can agree on measurable and achievable outcomes, a value-based approach can work exceedingly well for both.

Making the Right Plans to Protect against Loss
One attraction of UHNW clients is that they can provide a lion’s share of a firm’s revenue. But if this is the case, then losing even one very large client may threaten a firm’s profitability or viability. To manage this risk, advisors must first
Finding the Way Up

For many advisors, UHNW households represent the peak of the industry, offering work that is both challenging and rewarding. To keep ascending, however, firms need to carefully balance client characteristics, pricing practices, and risk management plans. With the right business model in place, advisors can be ready to earn sustainable profits for their firms while delivering truly superior value to their clients.

Mark Tibergien is chief executive officer of Pershing Advisor Solutions, a BNY Mellon company. He is also a managing director and a member of Pershing’s executive committee. Contact him at mtibergien@pershing.com.

Endnotes

1 Control persons include senior managers, members of the board of directors, and officers such as the chief executive officer and chief financial officer. Control persons are able to use both their authority and their influence to make decisions on the corporation’s activities. A control person is also called an affiliated person.

2 Pershing Advisor Solutions and research firm FA Insight developed “Profitable Pricing Practices: An Independent Advisor’s Guide,” which examines the leading pricing practices among top advisory firms and provides best practice guidelines to drive profitability. To obtain a copy of this guide, contact pasinformation@pershing.com.

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