From fighting fires to fire insurance: Transforming to a subscription based business model

Ron Baker, Founder
VeraSage Institute
Chief Value Officer, Armanino LLP
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Today’s speaker

Ron Baker
Founder, VeraSage Institute
CVO, Armanino LLP
@ronaldbaker
Value Pricing 2.0

Hourly Billing: Prices the inputs

Fixed Fee: Prices the outputs, the scope of work

Value Pricing 1.0: Prices the customer outcomes (transformation)

Subscription model: Prices the relationship and the portfolio
“In five years, you won’t buy anything, but subscribe to everything.”

Tien Tzu, CEO of Zuora
“In five years, you’ll have the option of subscribing to everything—and every business will have to accommodate that fact.”

Anne Janzer, Subscription Marketing
Exercise

Why would you subscribe to:
Roofs
Refrigerators
Drills
Guitars
Cars
Birthday Parties
Shoes

What are the advantages and disadvantages to the customer?
What are the advantages and disadvantages to the provider?
Tease out the value proposition.
Why subscription?

Why now?
PUNCH UP 10 SELECTIONS FOR ONE CENT!

AND GET THE GOLD BOX BONUS SHOWN ON TV

SELECT 10 ALBUMS

Hotel
California

Columbia House
Four trends ushering in the subscription model

- Reduction of transaction costs
- Light-switch reliability
- Delicious Data
- The Long Tail
McKinsey says

Subscription ecommerce market has grown by more than 100% a year for past 5 years

Subscription-based companies growing 8x faster than S&P 500 (17.6% vs. 2.2%, and 5x than US retail sales (17.6% vs. 3.6%)
If a member retains membership and engagement for a year = 90% chance member for life
AICPA: Cost 11x more to acquire a new customer than retain one
Advantages of the subscription model – 1

- Predictable revenue
- Customer lock-in and switching costs
- Not selling services, but creating annuities with a lifetime value that far exceeds whatever you paid to acquire them
- Collective knowledge of your customers is a competitive advantage that can’t be duplicated
- 1:1 Marketing: Changes the 4 Ps of marketing. We’re not pricing a service, we’re pricing a transformation, insurance (peace of mind), and the portfolio
Advantages of the subscription model – 2

- Shift to a long-term relationship focus rather than delivering tasks—the very definition of a professional
- Attract new customers (rather than just selling more to current customers)
- You can plan cash flow and capacity more effectively
- Moving beyond efficiencies and into possibilities
- Breaks down silos, and molds the firm around the needs of customer
- Truly a “one-firm” model: Portfolio approach to analyzing profit, rather than silo P&Ls, and realization rates
Advantages of the subscription model – 3

- Dynamic cycle customer interaction: renew, suspend, upgrade, downgrade, etc.
- They increase the value of your largest asset (Amazon Prime carved out of Amazon would be worth billions; the New York Times would be a Unicorn)
- Get paid automatically, less financing, collections costs
- Increases customer loyalty
- Recession-proofs your business
Amazon Prime: “It was never about the $79. It was really about changing people’s mentality so they wouldn’t shop anywhere else.” Vijay Ravindran
Nine Subscription Models

The Automatic Customer
Creating a Subscription Business in Any Industry

John Warrillow
Founder of Soylent and author of Built to Sell: Creating a Business That Can Thrive Without You
Web-site membership

THE WALL STREET JOURNAL

The Economist
All-you-can-consume content
Private club
Front-of-the-line

PEACH PASS

CLEAR
Consumables
Stud Club

12 month Subscription Service

Earring of the Month Club

Surprise box
“The name perfectly describes how it feels to be a member: a citizen of Porsche enthusiasts given the opportunity to drive many miles in many models. The Porsche Passport service really sets this apart from any other brand I’ve been loyal to.” —Porsche Passport Member
Peace-of-mind
What are the Benefits of Concierge Healthcare?

Concierge medical services take a much more personalized approach to your health and overall well-being. You benefit from a bespoke level of customized healthcare, with an amount of time and attention to detail from your doctor that scales to your circumstances as they change over time.

- Develop a long-term relationship with your doctor
- Access your physician and medical team when and where you need to
- Benefit from a proactive approach to your health including preventive and integrative medicine
- Receive customized care specific to your individual needs and preferences
- Referrals to the best specialist care when you need it
- Customized research and case management if required

MDMG Suite of Concierge Medical Services

- Executive health program
- Premier service levels for direct physician access
- Extreme privacy services for high-profile individuals
- House calls and office visits in San Francisco
- Hospital inpatient care
- Discreet mental health and substance use treatment for patients or their family members
- Second-opinion and customized research services
### Level of Service Offerings in Subscription-Based Practice Models

<table>
<thead>
<tr>
<th>Service Level</th>
<th>Patient Panel</th>
<th>Features</th>
</tr>
</thead>
</table>
| **Preferred Access** | 800–1,200 | - Prioritized same- or next-day appointments
- Email consultations and texting
- Personalized health assessment, preventive services, and counseling
- Online platform to track progress and share data with healthcare team
- Extended appointments |
| **Concierge** | 400–800 | - Guaranteed same-day appointments
- Access to physician’s mobile number
- Expedited imaging and labs
- Specialist appointment facilitation
- Inpatient rounding
- Predictive/diagnostic tools and testing
- Ancillary and wellness services, including nutritionist and fitness consultations
- Mobile/video consultations |
| **Premium Concierge** | 200–400 | - At-home visits
- Premium transportation services
- Physician availability 24/7/365
- On-site imaging and lab services
- Preferential referrals to specialists
- Inpatient care management
- Genetic screening and testing
- Prescription drug pickup/drop-off services
- International care coordination |
Adoption Models

The subscription trial—low risk, low reward, lack of commitment may doom transition

The segmented approach—offer only selected services, or only to selected customers

The all-in pivot—Adobe Systems most visible example, in 2011, “won’t this lower our margins? How will sales sell this stuff?” By 2016 revenue $5.85B, 78% from subscriptions
Three factors of production

Land
- Rents

Labor
- Wages

Capital
- Interest

Where do profits come from?
RISK
Three actuarial axioms

If what you sell entails risk, you are not a commodity.

There is no such thing as a bad risk, just a bad premium.

There is no model for pricing risk by the hour.
Subscription Metrics

- **MRR** – Monthly Recurring Revenue
- **ACV** – Annual Contract Value
- **CAC** – Customer Acquisition Costs

Churn rate = MRR beginning of month divided by amount of lost MRR in the month

**Recency** (last visit), **Frequency** (how often do they visit), and **Volume** (how many articles read)

LTV > 3 x CAC (3:1 ratio of lifetime value must be 3 times greater than cost to acquire. Most successful sub business have 8:1 ratios)
## Traditional vs Subscription P&L

### Traditional

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount</th>
</tr>
</thead>
<tbody>
<tr>
<td>Net sales</td>
<td>$100</td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>(40)</td>
</tr>
<tr>
<td>Gross income</td>
<td>60</td>
</tr>
<tr>
<td>Sale and marketing</td>
<td>(20)</td>
</tr>
<tr>
<td>Research and development</td>
<td>(20)</td>
</tr>
<tr>
<td>General and administrative</td>
<td>(10)</td>
</tr>
<tr>
<td>Net income</td>
<td>$10</td>
</tr>
</tbody>
</table>

### Subscription economy

<table>
<thead>
<tr>
<th>Item</th>
<th>Amount</th>
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</thead>
<tbody>
<tr>
<td>Annual recurring revenue</td>
<td>$100</td>
</tr>
<tr>
<td>Churn</td>
<td>(10)</td>
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<tr>
<td>Net annual recurring revenue</td>
<td>90</td>
</tr>
<tr>
<td>Recurring costs</td>
<td></td>
</tr>
<tr>
<td>Cost of goods sold</td>
<td>(20)</td>
</tr>
<tr>
<td>General and administrative</td>
<td>(10)</td>
</tr>
<tr>
<td>Research and development</td>
<td>(20)</td>
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<tr>
<td>Total recurring costs</td>
<td>(50)</td>
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<tr>
<td>Recurring profit</td>
<td>40</td>
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<tr>
<td>Sales and marketing</td>
<td>(30)</td>
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<tr>
<td>Net operating income</td>
<td>10</td>
</tr>
<tr>
<td>New annual recurring revenue</td>
<td>30</td>
</tr>
<tr>
<td>Ending annual recurring revenue</td>
<td>$120</td>
</tr>
</tbody>
</table>
Resources

- Subscribed, Tien Tzuo, founder of Zuora
- Subscription Marketing, Anne Janzer, 2017
- Retention Point: The Single Biggest Secret to Membership and Subscription Growth, Robert Skrob, 2018
- Subscription Economy Index: www.zuora.com
- Tomorrow 3.0, Michael C. Munger
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