

## In-Class Exercise: Robo-Advisor Business Models

### Exercise 1: Structured Debate — “Is Betterment an Asset Manager or a Software Company?”

*Format:* Split into two teams. Each team prepares arguments for its assigned position, then presents. After both sides speak, the class votes — but first, read the debrief questions. Use Betterment as the reference case because its product footprint now spans direct-to-consumer wealth, employer-plan administration, and advisor-technology licensing.

#### Team A — “Betterment Is an Asset Manager”

*Anchoring evidence:* Betterment holds registered investment advisor status, earns its primary revenue as a fee on assets under management, owes fiduciary duty to retail clients, and is supervised by the Securities and Exchange Commission. Its economic value rises and falls with the size and performance of the assets it manages — the central metric of an asset management business.

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#### Team A: Betterment Is an Asset Manager

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Argument I

Argument II

Argument III

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Concession    *Strongest argument AGAINST your position:*

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Closing    *How you address the concession:*

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#### Team B — “Betterment Is a Software Company”

*Anchoring evidence:* Betterment’s core revenue engine is a platform that allocates, rebalances, and tax-optimises portfolios through software. Its cost structure is dominated by engineering, compliance automation, and cloud infrastructure, not by research analysts or portfolio managers. Its growth model has progressed from a direct-to-consumer app to an advisor-technology licence, a trajectory more typical of a software firm than an asset manager.

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#### Team B: Betterment Is a Software Company

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Argument I

Argument II

Argument III

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Concession    *Strongest argument AGAINST your position:*

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Closing    *How you address the concession:*

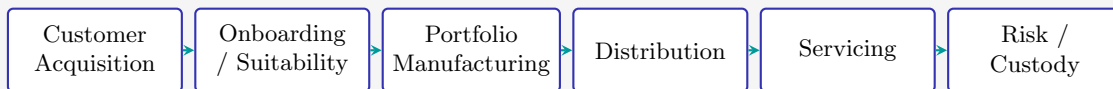
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### Debrief Questions

- Q1:** Does the answer — asset manager or software company — matter for how securities regulators should supervise Betterment? Why or why not?
- Q2:** Could the answer genuinely be “both”? If so, what does that imply about the usefulness of traditional industry categories when applied to a firm whose product is a software-delivered financial service?
- Q3:** Name another financial-services company that blurs this same category boundary. What tensions does the blurring create for its investors and its regulators?

**Exercise 2: Value Chain Mapping**

*Scenario:* Wealth management can be broken into six links. For each link, identify which of the five robo-advisors on the reference slate (Betterment, Wealthfront, Nutmeg, Scalable Capital, Schwab Intelligent Portfolios) most clearly owns the link, and describe what the robo is substituting for the incumbent’s approach at that link. Be explicit when the robo rents the link via a partner custodian, fund manager, or parent broker.



Value Chain Link	Robo Owning It	What It Substitutes For the Incumbent	Sub-Owned or Rented?	Is the Link a Moat or a Margin Cap?
Customer Acquisition				
Onboarding / Suitability				
Portfolio Manufacturing				
Distribution				
Servicing				
Risk / Custody				

**Synthesis Questions**

- Q1:** Which value-chain link creates the strongest moat for a robo-advisor, and which link most clearly caps its margin? Defend both answers with reference to ownership, data, and regulatory barriers.
- Q2:** For at least two of the five robos on the reference slate, identify a link where the robo “rents” via a partner. What would it take for the robo to convert that rented link into an owned one — and should it?

## Facilitator Solutions

Sample answers for instructor reference. These are illustrative; student reasoning may diverge and still be valid.

### Exercise 1: Debate Sample Answers

#### Team A (Betterment Is an Asset Manager) — sample arguments

*Argument I.* Betterment operates as a registered investment advisor and owes statutory fiduciary duty to its retail clients. That duty is the legal backbone of the asset management industry, and it shapes every material decision Betterment makes about suitability, disclosure, and conflict management. A software company carries none of these duties; Betterment does, placing it squarely inside the asset-management regulatory perimeter.

*Argument II.* Betterment's primary revenue line is a management fee expressed as a fraction of assets under management. That revenue model is the definitional pricing structure of asset management. When assets grow, revenue grows; when assets shrink, revenue shrinks. The Business Model Canvas applied to Betterment maps Revenue Streams onto an asset-fee structure, which is the asset-management archetype.

*Argument III.* Betterment's Key Activities include discretionary portfolio construction, tax-aware rebalancing across client accounts, and ongoing supervision of allocations relative to stated client goals. These are the operating activities of an asset manager. A software firm's Key Activities are typically limited to product engineering and customer support; Betterment's activities span both of those plus portfolio decisions that carry fiduciary weight.

*Concession.* The strongest argument against Team A is that Betterment's cost structure, release cadence, and advisor-technology expansion all resemble a software company rather than a traditional asset manager.

*Closing.* Regulatory form follows economic substance: because Betterment manages assets on a discretionary basis under fiduciary duty and charges an asset-based fee, it is an asset manager regardless of how efficiently its workflow is automated.

#### Team B (Betterment Is a Software Company) — sample arguments

*Argument I.* Betterment's cost structure is dominated by engineering, product management, and cloud infrastructure. A traditional asset manager's cost base is dominated by research analysts, portfolio managers, and institutional-sales staffing. The two cost profiles barely overlap. On the Business Model Canvas, Betterment's Cost Structure and Key Resources blocks read like a software company's, even though the Revenue Streams block uses an asset-management pricing convention.

*Argument II.* Betterment's growth channels are the app store, content marketing, employer-plan integrations, and an advisor-technology licence. None of these channels resemble the institutional distribution network through which traditional asset managers reach clients. The release cadence of the product — frequent software updates, in-app experiments, gradual feature rollouts — is a software-firm cadence, not an asset-manager cadence.

*Argument III.* The advisor-technology licence, in particular, is the most revealing product line. When Betterment licenses its platform to a registered investment advisor, it is selling software to another professional firm, not managing that firm's money. The economics of that line are software economics — a recurring licence fee against a scalable code base. The presence of this line demonstrates that the dominant logic of the firm is platform software, with the direct-to-consumer asset management being one deployment of the platform rather than the platform itself.

*Concession.* The strongest argument against Team B is that Betterment's fiduciary duty, asset-based fee, and discretionary-portfolio decisions are genuine asset-management responsibilities that a pure software firm never carries.

*Closing.* Regulatory classification is a lagging indicator. The economic substance driving most of Betterment's valuation, product road map, and competitive advantage is platform software; the fiduciary-advisor licence is infrastructure, not identity.

### Debrief Q1 — Regulatory supervision

Whether securities regulators should supervise Betterment as an asset manager depends on the economic risks the entity creates, not on the label it prefers. A firm that exercises discretionary investment authority over retail client funds can create suitability failures, conflict-of-interest problems, and misallocation at scale if its software is misdesigned or its disclosures incomplete. These risks are the exact risks fiduciary supervision exists to address. Classifying Betterment as a software company and supervising only its consumer-protection footprint would leave the fiduciary risks unguarded. The answer matters because the supervisory toolkit — fiduciary enforcement, suitability review, disclosure adequacy, books-and-records inspection — is calibrated to the risk, not to the interface through which the risk is accessed.

### Debrief Q2 — “Both” as an answer

The answer can genuinely be “both at the same time.” Betterment operates a regulated fiduciary advisor inside a software-company organisational structure, with engineering-led product development and an advisor-technology licensing line that is unambiguously a software-as-a-service business. This duality exposes the limits of categorical industry labels inherited from a world in which portfolio manufacturing, distribution, and client relationship management were bundled inside one institution. If “both” is the right answer, the implication is that functional regulation — regulating by what a firm *does* with client assets — is more robust than institutional classification. That shift in focus is already visible in how securities regulators approach robo-advisors relative to traditional advisor firms.

### Debrief Q3 — Cross-sector blurring example

Addepar provides a close parallel inside wealth technology. Addepar is a software platform used by registered investment advisors and family offices for performance reporting, portfolio analytics, and client reporting. It never manages money directly, yet it sits deep inside the advisor workflow and earns software-style revenue against an addressable market sized in assets under administration. Investors and analysts have struggled to classify it: is it a wealth-technology software firm valued on recurring-revenue multiples, or a financial-services infrastructure provider whose revenue should be valued against the underlying assets it supports? The tension is directly analogous to Betterment's. For investors, the blurring affects which peer set should anchor valuation; for regulators, it affects whether technology-risk supervision or financial-services supervision should lead.

## Exercise 2: Value-Chain Mapping Sample Answers

Value Chain Link	Robo Owning It	What It Substitutes for the Incumbent	Owned or Rented?	Moat or Margin Cap?
Customer Acquisition	Betterment (direct-to-consumer app plus employer-plan channel)	Adviser-led introduction and branch-channel acquisition; replaces human-adviser acquisition with app-store and content-led flows	Owned	Moat (content and partner referrals compound over time)
Onboarding / Suitability	Wealthfront (in-app risk profiling and documentary checks)	Paper-based suitability questionnaire administered by a human adviser; replaces it with a guided digital flow	Owned	Moat (suitability evidence feeds on-going supervision)
Portfolio Manufacturing	Nutmeg (in-house discretionary-portfolio construction using third-party funds)	Adviser-led portfolio selection from an open-architecture menu; replaces it with algorithmic allocation over a curated fund universe	Rented (underlying funds are third-party)	Margin Cap (fund charges set a floor the robo cannot push below)
Distribution	Scalable Capital (pan-European app distribution under a unified execution model)	Country-by-country adviser distribution with separate legal entities; replaces it with a single-licence cross-border app footprint	Owned	Moat (regulatory footprint, once built, is hard to replicate)
Servicing	Schwab Intelligent Portfolios (in-app service supported by the parent broker's phone desk)	Pure adviser-led servicing; replaces it with a software-plus-phone hybrid subsidised by the parent broker's infrastructure	Owned (inside parent)	Moat (marginal servicing cost is very low at ecosystem scale)
Risk / Custody	Partner custodians and clearing brokers	Self-cleared custody at an incumbent broker; replaces it with a rented custody relationship (except where the parent broker provides it directly)	Rented (owned for Schwab's in-house case)	Margin Cap (custody fees cap the share of total fee the robo can keep)

### Synthesis Question 1 Sample Answer

The link that creates the strongest moat for a robo-advisor is Portfolio Manufacturing, specifically the allocation engine plus the tax-aware rebalancing logic. That engine is where the robo's proprietary intellectual work is concentrated: the optimisation across accounts, the tax-lot awareness, the glide-path automation, and the drift-control logic cannot be described adequately in a specification sheet. A competitor that licenses an incumbent engine obtains feature parity on paper but loses the compounding advantage that a robo earns by training its own engine on its own book. Regulatory barriers are moderate (fiduciary oversight of the engine's outputs), but the intellectual moat is the dominant barrier.

The link most likely to cap margin is Risk / Custody, particularly where the robo rents the link through a partner custodian. The custodian captures a share of the economics and controls the operational schedule for settlements, corporate actions, and tax reporting. Converting the link to an owned one requires obtaining clearing capability — a capital-intensive and regulation-intensive undertaking that most robos defer. The exception is Schwab Intelligent Portfolios, where

the parent broker already owns custody; for that case the margin cap is much weaker precisely because the rented link is instead an in-house adjacency.

### Synthesis Question 2 Sample Answer

Nutmeg rents its fund-manufacturing link through third-party fund partners and its custody link through a partner custodian. Converting fund manufacturing to an owned link would require Nutmeg to launch its own funds and bear the manager-selection and portfolio-risk workload that currently sits with its partners; converting custody would require a clearing or banking relationship of a kind Nutmeg has historically chosen not to build. The case for converting is margin expansion; the case against is management capacity, capital intensity, and the regulatory overhead of carrying the risks in-house. For Nutmeg, renting both links is the rational steady state given its size, and the strategic focus has instead been on owning the customer-facing links where its wedge advantage is clearest.

Scalable Capital rents its custody link but has invested heavily in its regulatory licensing across euro-area jurisdictions to avoid renting the distribution link country-by-country. Converting custody would require the broker-dealer infrastructure that Scalable Capital has consciously not built; instead, the firm has converted its early regulatory arbitrage into a cross-border execution licence that now functions as a moat. The case study is a reminder that renting is not a waystation to ownership — it can be a deliberate steady-state choice, provided the firm owns the adjacent link that actually produces the wedge.