

Considerations for Your Evolving Family Office

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The "Smith" family has been in business together for almost 80 years, today through a holding company that includes some operating businesses, real estate and a family office that manages substantial wealth. At a recent shareholder meeting several cousins expressed frustration that so much of their wealth was tied up in illiquid investments, and that they had no seat at the table in selecting those investments. Others were protective of the professionals whom they felt were better qualified to vet investments, and judgmental that their cousins were looking to tap into more distributions. The family recently sold a significant operating company and planned to put more resources into the family office, to best serve the needs of their growing family.

This incident made clear to them that they needed to embark on some intentional planning for this aspired growth of their family office...

1. Alignment

Why do we have a family office? What are we looking to accomplish together?

In well-run family enterprises, shareholders feel an emotional connection to the business that may make them more willing to work together and collaborate on shared goals; they see the family as part of the business' success and want to continue that tradition. They feel a part of something bigger than themselves, which is rewarding. Compared to how family members may internalize the story of grandpa and grandma's sacrifice and ingenuity in getting their first widget to market, changing their industry, and maybe creating thousands of good paying jobs in their community, it can be harder to feel that sense of connection and purpose around passive or active investment strategies.

Many families expect that a major liquidity event will lead

to more family harmony because family stakeholders may now be able to access significant cash resources for the first time (distribution policies are a frequent source of tension between family business stakeholders). While that may be true, to the extent that the family is seeking to continue to invest together (or will be tied together due to how the estate planning or liquidity event was structured) stakeholders now must align on some core pillars of family office purpose and design. Some questions to consider:

- What is the purpose of our wealth?
- Are we aligned on the right balance of growing the wealth and using the wealth? How will we navigate different needs or desires on this question without falling into judgments of one another?
- Beyond the benefits of economies of scale, why are we choosing to invest together and what do we hope to accomplish as a family through this effort?
- How do we balance the desire for the family office to serve and support family members, with our goal of developing competent adults?
- Are we willing to commit to learning this new business? What resources do we put towards helping family understand the risks and strategies involved in investing money, so that we might be effective stewards of this wealth?
- How much time do we want to devote to being an extended family and building shared memories? Does the family continue to have appetite for these kinds of efforts, and is the family office organized to advance these goals?

As is the case with any family enterprise, these alignment questions must be considered at least once a generation, or at any inflection point that could impact the nature of the family office.

Families sometimes fail to truly get aligned because much of this work touches deeply held values that individuals often want to avoid discussing. Are we looking to continue to grow this wealth for future generations yet unborn – or might current generations be able to use the wealth for some individual goals or desires? What is an acceptable "use" of the money? Who gets to decide? If some wealth has transitioned to the next generation, at what age do they get what autonomy over these assets? What ambivalence do family members have about their wealth, or about the acceptable uses of wealth by themselves or other family members. How do we build competence in our family around these new responsibilities, and what do we do about family members who are unwilling or unable to develop or nurture these skills?

These questions highlight the inevitable complexities and disparate goals that must be wrestled with when building or evolving a family office. It requires collaborative discussion as well as compromise to build a plan that best reflects collective objectives.

2. Scope

What is the strategy and what services will be provided?

Once the family has addressed some of these important philosophical questions, it is time to pivot to the practical. What is the scope of services that should be provided by the family office, and how will this get paid for? How are these tasks currently getting accomplished? What changes are being contemplated, and what does that mean in terms of new outside advisors or services that need to be contracted, talent the family office needs to hire, as well as the knowledge and skills that family members may need to develop?

Family offices have many possible forms. Early on they are often embedded into the operating business, which provides certain economies and efficiencies. You ask people within the business with whom you already have a trusting relationship, to provide some basic tax filing and assorted other services for the shareholders. This structure can work for a time, however as the family and the business grows, a distinct and separate family office structure makes more sense for several reasons:

- The scope and complexity of the services expands considerably.
- The family may be investing as minority or majority partners with others, necessitating a more

sophisticated oversight role. Even when family offices outsource investment management, there typically remains a need for management/oversight of active investments.

- Privacy is important to family members, and as more services are provided, there is often concern about employees knowing too much about the inner workings (and possibly conflicts) within the family.

While in no way comprehensive, some of the services a family office might deliver or coordinate for the family include:

- Tax & estate planning
- Wealth management
- Private investments
- Trustee services
- Bill paying and other administrative
- Family education
- Family philanthropy
- Lifestyle services (e.g., coordinating travel, childcare, art collections...)

Once the family is clear on the services they want from their family office, it is important to determine which of these will be delivered 'in house', and which will be services that the family office coordinates and oversees, without having all those experts directly on the payroll.

This, in turn, establishes who you need to have as part of your family office staff. In our experience, headcount varies wildly across family offices, and is a function of many variables, including number of family being served and range and types of services provided. Most Single Family Offices have a CEO (or Director of Family Office, President), as well as a CFO. The CFO will likely have some staff reporting to him/her, just given the administrative needs around tax/accounting/trust-related services, as well as risk management responsibilities. In addition, if there are diverse investments being managed by the family office, a Chief Investment Officer (CIO) might be required. In some cases, the CEO can do that job if he/she brings the requisite skills for that responsibility.

3. Oversight

Family Office Governance

The governance of family offices also varies. In some cases, the family office will report to the family council,

if the family has a family council. This is quite common in first- and second-generation family enterprises. As the family transitions into the third generation and beyond, often the family office CEO reports to a family office board (which may be made up of just family members, but in some cases can include independent directors). As in any business entity, the board is responsible for overseeing strategic development/execution, and for ensuring that leadership is held accountable to established expectations.

If the family office is pursuing extensive investments, there may also be an investment committee that reports to the board. This committee will most often be composed of family and non-family experts, and carries significant responsibility for executing the investment strategy.

In closing

Successful enterprising families that have a family office (whether as an SFO, part of an MFO, or embedded inside an operating business) will have:

- A shared vision that is motivating to family stakeholders (why are we collaborating in this way, what are we seeking to accomplish)
- Aligned goals and priorities of the family office (what we do, for whom & how)
- A well-developed strategy around these core goals, and an understanding of how that translates to operational objectives and specific job roles
- Strategies to grow the family's human capital as well as the financial capital

- Effective oversight of management
- Clear qualifications for management and governance roles
- Excellent development of beneficiaries
- Strong communication between beneficiaries and trustees

Additional helpful guidance we would offer includes:

- Start small – and pilot various initiatives first – it's amazing how quickly family offices can grow – and exponential growth can be dangerous for many reasons beyond the economic impact;
- As you build or evolve your family office, hire the best people you can find – someone with FO experience, who understands strategically and structurally what will be needed, has good technology experience – and has the interpersonal skills to deal with a very diverse group of people across a variety of stakeholder groups.

We have posed many questions in this article that we hope you will keep in mind when you engage in family office planning. The questions are easier to ask than answer, and the answers are different for each family. In addition, your answers to these questions may change over time, which highlights one additional source of success: a willingness to design your family office with flexibility, so that it can respond to the ever-evolving needs of the family.

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To learn more about our firm and how we serve families like yours, call us at (773) 604-5005, email info@thefbcg.com or visit www.thefbcg.com. There is absolutely no obligation.

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