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Planning for Family Offices: Understanding the Big Picture

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Overheard at Crowe Soberman is a series of blog posts and videos where we talk about the things we talk about around the office and with our clients except with the cameras or recorders on. It's sort of like going out for coffee with one of our Crowe Soberman experts, but without the caffeine jitters. Feel like you need more? Connect with our author.

According to a 2019 WealthX report, close to 68 per cent of the world's richest people are 'self-made,' thanks in part to new opportunities in technology and in emerging economies of the past decade. While self-made individuals have experienced great success operating and growing their businesses, there is a stark difference between managing a business and managing a portfolio of various assets, be it cash, real estate, alternative investments, etc.

With newfound wealth (and inherited generational wealth) also comes the responsibility to make smart and long-lasting decisions that will benefit you and your family for years to come. Mayeer Pearl, Audit & Advisory Partner and SuRE (Succession, Retirement and Estate Planning) Group member, shares some of his experiences working with high net worth ("**HNW**") family offices and the important steps he urges clients to take to preserve, optimize, and grow their wealth.

There is no "one size fits all" model for HNW family wealth planning.

As accounting and tax advisors, we find that HNW families can be divided into two categories:

1. Families who have accumulated multi-generational wealth and who understand the responsibilities that come along with that.

From monitoring, organizing, tracking, and looking for new investment opportunities when appropriate, these individuals tend to be on top of everything from a wealth planning perspective and are already treating their family office like a proper business.

2. Typically, first generation ("**G1**") or multi-generational families who have run a successful operating business but are not taking advantage of the opportunities available to them. Whether they are still focused on the day-to-day operations of the business, or if they simply don't understand the complexities and it's easier for them to keep "running the money," they are missing out on opportunities for growth and in turn, are putting themselves and their business at risk. They do not treat investing like a business and do not devote the proper resources to investing and monitoring their net worth.

What is a Family Office?

According to Forbes, "Perhaps the simplest definition of a family office is an organization that assumes the day-to-day administration and management of a family's affairs. To that end, to honestly call itself a family office, an organization needs to provide more that just the standard wealth management functions. Most people in the industry would agree that a family office should be able to provide for tax compliance work, access to private banking and private trust services, document management and recordkeeping services, expense management, bill paying, bookkeeping services, family member financial education, family support services, and family governance."

Determine your goals and assemble a team of advisors to support them.

The first and most important step is figuring out what you want to do with your money. Based on those goals, develop an investment policy statement for your family and then work with the proper team of advisors to invest inline with your values.

Many HNW families miss out on two fundamental pieces in their policies: measurement and reporting. Measurement and reporting the results are essential because as advisors, we often find that families have no idea what the return on their investment actually is. Nor do they measure whether their investments are appropriate within the framework of their investment policy or whether the investments are performing as expected. Family offices need to understand that they are running a business and with that, they need a proper investment officer. Often, many HNW families think that they are "not high net worth enough" to have a family office as they are too expensive. This may be the case, as there are varying opinions as to how much net worth a family needs to have a dedicated office. That being said, there are family office solutions for all levels of HNW. There are external firms called Multi-Family Offices ("**MFO**"), which are established to meet the investment, estate planning and, in some cases, the lifestyle and tax service needs of multiple HNW families.

As successful business owners, you are already on top of your game and have utilized outside resources to build the business that created your wealth. A manufacturer knows they need a foreman, a designer, a marketing person, etc. to make their business a success – and running a family office is no different.

Often HNW families don't realize how much work it takes to manage their investable assets. However assembling the right team of professional advisors is the key to looking at the big picture and unlocking any missing wealth planning opportunities. Make sure that your team is stacked with the proper legal, accounting, tax, and investment advisors. An often-overlooked piece of HNW family management is ensuring you get the proper social work advice on how you and your family deals with the wealth, especially when it comes quickly. There is a lot of responsibility that comes with wealth. Education is a key component of understanding how to deal with wealth.

Investment income may be passive, but you must actively take care of it.

Lower HNW families (valued between $15M-$50M) often face difficulties as they are too big to only be using traditional investment advisors but too small to get a lot of opportunity coming their way. They require professional assistance to figure out how to leverage the monies properly and to not be stuck in investments tailored for a different platform. MFO's are ideally suited to these families.

With increased investment income also comes more complicated and multi-faceted accounting, advisory and tax needs, especially when we look at brick and mortar-type investments that are not liquid. Family offices need to consider more estate planning, intergenerational wealth education, insurance needs, and even security needs. For example, during the early days of the COVID-19 pandemic, local rent strike campaigns protested outside of their landlord's homes, and as a result, landlords who were publicly named and required professional security teams to monitor and secure their personal residences.

While your life is changing (often in a very positive way), it's crucial to adapt.

Newly HNW families understand that something must change – they just don't know what or who to go to. As trusted advisors, it's our job to help point them in the right direction and lead them to the proper resources.

When family with newfound wealth do not get the advice disasters can happen. We have heard stories such as one individual who sold their business for close to $100M and after extravagant and reckless spending, they were left with $10M within four years of the sale. They were handing out personal (non-collectable) loans whenever a friend or family member asked. They even stopped travelling commercial and only flew on private jets. The biggest mistake they made was not waiting for the capital from the sale to be fully invested to return enough income to be able to live the lifestyle they wanted. (*Frankly, even the amount of capital that they had after tax was probably never enough to sustain the lifestyle they were living after the sale of the business.*) By the time the individual sought a professional advisor, it was too late as they never received the right advice to slow down and understand the responsibility that came with their wealth.

On the flip side, we have also encountered many success stories and examples of advantageous, long-term wealth planning. An already financially successful client won the lottery. Their intentions with the winnings was to give each child a sum of money to pay of their mortgages (and nothing more), with the rest put together in an investment plan where the wealth could grow and ultimately sustain them. The children understood while they would be able to maintain their lifestyle, their lives would not be changed so much that they could stop working and had to continue earning their own income. The parents in this case made a very responsible decision and part of the reason they had the wisdom to do so, was that there was already inherited wealth in the family.

The first step: Don't touch your money for a year.

One piece of advice that I would suggest to newly HNW individuals and their families: Don't touch your money for a year. Invest it and don't make any large purchases. If you come into $100M quickly (through the sale of a business or lottery win), go buy yourself a nice car; don't purchase a $5M house. Take a year to research your options, understand, invest, and determine what you really want and need, and what your long-term goals are. When you jump into new wealth, you are often trying to 'keep up with the Joneses,' but don't necessarily have the wealth to do that.
Until the money is invested and generating income, you are spending capital – and the whole point of strategic wealth planning is to preserve capital.

Understand the moral obligations that come with wealth.

Especially in new HNW families, it's important to understand community responsibility. It can be argued that with wealth, comes a moral obligation to understand that there are people who need help. You have an opportunity to make a significant difference in people's lives at a very minimal cost to you and the difference you can make is enormous.

Talking openly about intergenerational money from an early age is also fundamental to the stewardship and longevity of your wealth. We're not saying that you should tell your kids exactly how much your family is worth, but there is no doubt that they already understand the lifestyle they lead compared to someone they go to school with might be noticeably different. Educate your kids to understand the privileges they have and to appreciate them, but to also understand that it's not an entitlement and it could disappear. Allowing your children to believe they can live a life of luxury is a huge disservice.

Connect with the Author

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