

► **Greycourt White Paper**

White Paper No. 10 – *Establishing a Family Office: A Few Basics*

Background

Many families who have experienced a significant liquidity event will consider setting up a family office. The purpose of this white paper is to discuss the reasons families consider establishing an office, to describe the typical duties of such offices and to suggest a basic framework for designing and setting up a successful family office.

Discussion

Why a family office?

The Family Office Exchange estimates that at least 3,500 family offices exist in the United States, powerful testimony to the attractiveness of the concept. While the specific reasons families establish offices are as numerous as the families, the most fundamental reason has to do with the challenge of stewardship: no one will take your issues as seriously as you will take them yourself. For most of American history all but the wealthiest families¹ entrusted their assets to banks and trust companies, and the results tended to be dismal at best. Moreover, outside institutions were either indifferent to or completely ignorant of families' needs for advice on issues beyond asset management: philanthropy and intergenerational issues, for example. As a result, many families who began with substantial fortunes found that, three generations later, they were merely affluent at best. The point of a family office is to focus attention on the needs of the family, whatever those needs may be and however they may evolve over the generations.

What is the minimum size for a family office?

The answer depends on the mission of the office. If the goal is simply to provide family-wide accounting and bookkeeping, a family with as little as \$50 million will find it economic to establish an office. On the other hand, a fully integrated² family office is probably accessible only to very large families, typically over \$1 billion.

What responsibilities are carried out by a family office?

¹ We believe that the first true family office in America was established by Judge Thomas Mellon in Pittsburgh in 1868. John D. Rockefeller set up an office for the Rockefeller family shortly thereafter.

² that is, one handling, in-house, the full array of investment, accounting, legal, intergenerational, educational and concierge services required by a complex family

A full-scale family office will typically be responsible for the following activities, either by handling them directly or by outsourcing them:

- ◆ *Investment management.* For all wealthy families, Job #1 is to manage the wealth effectively, yet managing wealth on a large scale and over the course of many decades is probably the most challenging issue most families will face.
- ◆ *Direct investing.* Many families made their money through operating a business, real estate development, or venture investing. These skills can be applied to increase the family's wealth through direct investments in similar enterprises.
- ◆ *Accounting and reporting.* If family members are to have any confidence in the management of the family's wealth, the family office will have to provide timely and accurate accounting, tax reporting and performance reporting.
- ◆ *Coordinated estate, tax, trust and insurance planning.* Given the complex nature of the U.S. tax code, the confiscatory level of estate and gift taxation, the fiduciary responsibilities associated with complex trust planning, and the litigious nature of American society, families who neglect to coordinate their activities in these areas will find their wealth rapidly hemorrhaging.
- ◆ *Philanthropy.* Philanthropy plays an important role in the lives of most members of wealthy families. But if charitable giving is to prove fulfilling and a method of binding the family together across generations, it will have to be pursued professionally, proactively and with a focus on issues that resonate with family members.
- ◆ *Management of a closely-held business.* Many families not only possess great liquid wealth, but also control an operating business. A family office can provide an ideal forum for discussing how such a business will be managed and governed, for dealing with issues posed by the fact that some family members work in the business and some don't, for thinking about capitalizing and recapitalizing the business, and so on.
- ◆ *Intergenerational conflict.* It is a rare family, wealthy or otherwise, that doesn't experience intergenerational conflict at some point. For wealthy families, such conflicts can lead at best to unwanted publicity and at worst to deep emotional trauma and dissipation of the asset base.
- ◆ *Education of younger generations.* A great challenge for wealthy families is raising children to be productive adults, fully capable of stewarding the family's wealth in their turn. A family office can play a highly positive role in helping educate younger generations about their future responsibilities and in offering opportunities to gain hands-on experience in dealing with those responsibilities.
- ◆ *"Concierge" services.* This phrase refers to a variety of services typically needed by wealthy families, and may include bill-paying, making travel arrangements, property management, oversight of aircraft operations, and so on.

Where do we begin?

The business of setting up a family office will differ from family to family, but the following steps will typically prove useful:

1. *Where do you want to go?* The first step is to think not about the family office, but about the family itself. What do you want to do with your wealth, with your talents, with your philanthropy, with your family business (if one still exists), with your children?
2. *The mission statement.* Once you know where you want to go as a family, the next step is to draft a mission statement for the family office. That mission statement will articulate the role of the family office in furthering the successful accomplishment of the family's goals.
3. *The business plan.* Now that you understand the mission of the family office, it's time to prepare a business plan detailing how that mission will be accomplished. The plan will discuss such issues as:
 - ✓ the legal structure of the office (corporation, partnership, limited liability company, etc.);
 - ✓ the specific activities the office will need to engage in;
 - ✓ whether those activities will be carried out in-house or will be outsourced;³
 - ✓ space needs;
 - ✓ the anticipated capital and operating costs of the office;
 - ✓ how those costs will be allocated among family members and entities;⁴
 - ✓ how the office will be governed and monitored;⁵
 - ✓ the role of spouses;⁶
 - ✓ how the office will report to the family.
4. *Hiring family office personnel.* By far the most important consideration in hiring family office personnel is trust. For this reason, many families will launch their offices by hiring someone they have known and worked with for many years: the CFO of a family business, a trusted attorney or accountant, a seasoned family office

³ Activities that are typically carried on in-house include direct investing, bookkeeping, accounting and reporting, philanthropy, education of younger generations, concierge services and oversight of a family business. Activities typically outsourced include investment management (the chief investment officer function), asset custody, tax accounting, estate and trust planning, and such "soft" issues as intergenerational conflict, where an objective viewpoint is useful.

⁴ Note that if costs are to be allocated to a private foundation, a private letter ruling from the IRS should be obtained approving the allocation methods.

⁵ For example, most family offices will report to a board of directors consisting of family members and perhaps one or two non-family members.

⁶ The issue here, of course, is not the "spouse problem" but the "ex-spouse problem."

manager, a long-time financial advisor. Beyond this, personnel decisions will shake out from the business plan.⁷

Are there alternatives to the stand-alone family office?

In recent years a great variety of alternatives to the stand-alone family office have been developed. Following are just a few of the options available:

- ◆ *Multi-family offices.* A few families have gone into the business of offering family office services to families other than their own.
- ◆ *Law firms.* Some larger law firms have organized special groups designed to provide an array of family office services to their wealthiest clients.
- ◆ *Accounting firms.* The largest accounting firms offer services that enable families to outsource many family office activities.

Information about alternatives to stand-alone family offices can be obtained from the major affinity groups serving wealthy families, including the CCC Alliance,⁸ the Family Office Exchange⁹ and the Institute for Private Investors.¹⁰

SUMMARY

Establishing a family office is one of the most important and, if properly done, ultimately one of the most satisfying activities a family can undertake. Greycourt will be happy to discuss this issue with you in greater detail.

GREYCOURT & CO., INC.
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(This paper was written by Gregory Curtis, Greycourt's Chairman.)

⁷ Many families will seek out the services of executive recruiters to fill senior positions. The Family Office Exchange manages a placement service specifically for family offices.

⁸ CCC Alliance LLC, 121 High Street, Suite 400, Boston, MA 02110, 617-457-8368.

⁹ Family Office Exchange, Inc., 137 North Oak Park Avenue, Suite 310, Oak Park, IL 60301, 708-848-2030.

¹⁰ Institute for Private Investors, 74 Trinity Place, New York, NY 10006, 212-693-1300.