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Family Business and the Role of the Family Office

The family business consulting industry has done a remarkable job educating families on how to run successful businesses and help lay the groundwork for the generational transitions and ownership transfers. We now regularly encounter outside advisory boards, fiduciary boards, family councils and family assemblies that assist families in better managing and operating this complex social system called a “family business.” As families grow and generations pass, these vehicles are essential to the maintenance of control and the successful operation of the family business enterprise. They promote the collective good and centralized decision making which are essential for success in business.

The family office serves a very different function. It is the place where the personal financial affairs of the owners and related family members are overseen and managed. A family office can provide a wide range of services to family members—from ministerial bill paying services to oversight of the financial affairs of each family member, including income tax and estate tax planning, preparation of tax returns, investment management, asset protection strategies, entity administration, etc. It often plays an integral role in keeping the ownership of the family business within the family. From a control perspective, it is essential to have these functions performed properly.

A less appreciated but no less important function of the family office is as a confidential communication vehicle for family members to discuss and gain a more comprehensive understanding of their individual financial position vis-à-vis the family business and other family members.

Many families operate a family office type structure from within their company and utilize either existing or former trusted employees, typically a CFO, attorney or other trusted employee, to handle the family’s personal financial affairs. This has the advantage of convenience and cost since the work involved is not generally perceived as a full-time job. In the early years, this is logical since the financial affairs of the family are likely quite intertwined with those of the business and the financial interests of the family members tend to be aligned.

However, as the family business grows and becomes more complex—especially as the business passes from generation to generation—this internal approach becomes problematic. The work burden increases, the required skill sets grow and, as family members multiply—with some in the business and others not—conflicts of interest and resource allocation issues inevitably arise. The biggest challenges occur when the so-called “spoils of ownership”—dividends, salary and capital ownership—are divided unevenly among members of the extended family. There comes a time when the separation of the family office from the family business is necessary.

For many families, the option of creating their own single-family office is not financially feasible. The out of pocket cost of a properly staffed single family office runs \$500,000 or more per annum and it is a significant burden to staff and supervise. The burden will be on the family to identify and recruit the requisite talent to staff the office and oversee the management of the office over time. Moreover, even if a family has a member with the qualifications to accomplish this, that member may not wish to spend his or her time performing these functions and being responsible to other

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family members.

The cost of operating a family office also should be evaluated in the context of the “other” costs that families of significant wealth will necessarily incur. These include professional fees for investment management, income tax return preparation and planning, wealth transfer planning, entity management and accounting, etc. Will the family office provide these services itself, or will it serve only as an intermediary for their procurement? What will the all-in cost of such arrangements be for the family? How economical is this?

The Benefits of the Independent Multi-Family Office

The independent multi-family office has become the vehicle of choice for many families as the family outgrows the internal office structure or determines that a single-family office is not viable. The benefits of using a multi-family office include the following:

Cost | By having multiple families using the same service provider, the costs of staffing and maintaining a high-quality service team are divided among all the users. Many of these offices are staffed with partner equivalent talent from major law, accounting and investment firms, a benefit that most single-family offices cannot afford. A multi-family office can be retained for a fraction of the cost of running a single-family office and the level of service team expertise is often much higher. An effective family office team can have the scale and resources required to achieve significant cost savings for each family they serve in areas such as investment management and tax preparation. Often, these savings will exceed the cost of retaining the multi-family office on an annual basis.

Need for a “Quarterback” | Wealth management is complicated. Families with significant wealth typically work with a number of advisors with no central point of contact. A multi-family office can serve as a “quarterback” for a family’s wealth management team, ensuring that all planning is coordinated and optimized. A multi-family office takes responsibility for implementation and ongoing administration of a family’s estate and tax plan and has the tools and information necessary to provide consolidated reporting for the family.

Access to Diverse Opinions from Experienced Professionals | A major advantage of a multi-family office is access to professionals that have experience with issues typically confronted by owners of family owned businesses. These firms, by design, have exposure to other clients and their advisors who regularly confront similar issues. The sharing of best practices and experiences across a variety of clients and their professional advisors is a valuable attribute of a multi-family office.

Separation of Business and Personal Issues | Family members—including spouses and other relatives of the owners of the family business—often want and need the opportunity to discuss and assess their particular financial issues and concerns apart from the business. Often issues are specific to each individual family unit, and those families may not feel comfortable talking about them with their parents, other family members or employees of the company. Many questions that otherwise would go unasked and unanswered can be dealt with seamlessly by the multi-family office staff.

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Personal Responsibility and Shareholder Sustainability | The managers and operators of a family business have a great deal of responsibility to bear. They have to look out for the entire family and make business decisions that are best for all the business owners as a group. To be successful, a majority (or more) of the owners need to be on the “same page” as to how the business is run. Questions relating to important issues such as growth strategies, dividend policies and employment practices need to be right for the company and all its owners.

It is challenging to look out for both the company and the interests of individual family members simultaneously—each have different wants, needs and issues that are often in conflict. Family members need to take responsibility as to how their own family unit’s affairs will be managed in relation to these important decisions—Can we live within our means?, How reliant are we on the financial success of the business?, How will we pass ownership of the business to our heirs?, Will our children be able to work in the business?, How much financial independence from the business do we want or need?, What expectations are reasonable? For family members without financial literacy or knowledge, the office can help them understand how the business is performing. Discussing these issues with a knowledgeable and independent advisor away from the company is a very healthy exercise for each family unit and enhances shareholder sustainability.

Planning for the Unexpected and Continuity | Many spouses and offspring of talented founders and leaders of family businesses are not equipped to deal with a sudden loss of the family business leader. They often have not been exposed to the critical financial issues and ownership issues of the family business and are totally unprepared to take over where their spouse or parent left off. Even if the loss of the family business leader is not sudden, there are challenges associated with transition. The family office can provide the support and continuity needed in these situations. In these circumstances, the longer that the office is involved with the family, the better, especially in terms of building strong relationships with the other professional advisors to the family and the business.

Help Implement and Monitor Best Wealth Management Practices | There is a litany of so-called best practices which families of means are well advised to follow. These include maintenance of adequate insurance, regular updating of estate planning documents, implementation of annual wealth transfer strategies, estate administration or entity management, investment management and diversification, etc. The family office will make sure that best practices are implemented in a timely matter.

Wealth Education for Family Members | A key role for the family office is to provide on-going financial education of family members, especially the next generation. Topics include such things as proper budgeting and cash flow management, investment management, how trusts work and their responsibilities as trustees or as beneficiary, philanthropy and much more.

Confidential and Expert Resource | One of the major benefits of utilizing an independent multi-family office is that candid conversations can take place in a completely confidential setting. This can include conversations about the family business and how decisions there impact the particular family member or affect unrelated family issues. The office can also be a resource for the family business

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itself and provide a way to communicate complex business issues and decisions to individual family members when that is appropriate.

Multi-family offices can offer tremendous advantages to family business owners. The selection process to find such a provider should include a matching of the skill sets of the particular firm with the needs of the family and an assessment of the compatibility or “chemistry” of the professionals there with the family members (particularly spouses).

The interests of the office should be properly aligned with those of the family. A key attribute of such a firm is independence—is the firm able to provide the expert advice needed free from conflicts of interest? How are the firm and service team compensated? Are their financial incentives aligned with those of a client family? Is the firm incented to sell products or particular solutions, such as insurance?

It is also important that the firm regularly and expertly serves other families with similar characteristics and needs. The best way to verify the “fit” and credentials of a particular multi-family office is through reference checks with their existing clients and the professionals who represent those clients.

Finally, the cost of the provider needs to be evaluated. How are its fees assessed? What impact will the provider have on the other significant costs which the family incurs, such as investment management and required fiduciary services? How skilled is the provider in reducing income and estate taxes? Costs need to be compared to benefits, recognizing that the most important benefits of hiring a family office—such as family harmony and peace of mind—are priceless.

St. Louis Trust & Family Office is an independent, multi-family office and trust company that advises clients on more than \$10 billion of investment assets and more than \$12 billion of total wealth. Founded in 2002, St. Louis Trust & Family Office provides holistic, high-touch client service including customized, independent investment management and a full range of family office and fiduciary services. The firm serves a limited number of clients with substantial wealth in order to maintain very low client-to-employee ratios. Visit stlouistrust.com to explore how the firm manages complexity with unmatched expertise and focuses on Family, Always.