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Getting the Best from a Family Office
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MEMORANDUM

**Getting the Best
from a Family Office
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Sometimes I wish I was back in my crash pad days,
Before I knew what “cash flow” meant.
Jimmy Buffett 1

INTRODUCTION

The family office has existed for over a century, but almost exclusively as a tool of the very wealthy. In recent decades, its use by families with less dramatic levels of wealth has increased, largely due to the advent of the multi-family office (discussed below). Today, there are an estimated 3,500+ family offices within the United States.² This article examines the nature of the family office, how it is constituted, why it can be very useful for certain clients, and when an estate planning attorney should advise a client about creating a family office.

Most estate planning attorneys have only a slight familiarity with the concept of a family office, usually through offices maintained by one or two clients as part of their ongoing businesses. Estate planning attorneys rarely understand the full scope of the services that are provided by a fully functioning family office, and they are even less aware of how these services can enhance the quality of the attorney's own work, and facilitate a higher level of estate planning services.

A BIT OF BACKGROUND

It is usually agreed that the first two family offices in America were created by Judge Thomas Mellon, of Pittsburgh, and John D. Rockefeller, of New York, both in the 1860's.³ One also should trace the roots of the family office to the practice among wealthy 17th-, 18th- and 19th-century landowners of employing an estates manager and staff to handle rental and farming activities on the landowner's property. When wealth

was largely one's real property, this arrangement served many of the same purposes as a modern family office.

Industrialists who found that their wealth vastly complicated their investments, charitable activities, and personal lives created the first generation of American family offices. One can neither invest nor give away vast sums of money without an established infrastructure to do the requisite due diligence and oversight. It also is difficult to maintain several residences, a yacht, and other significant tangible assets without a substantial staff.

These first generation family offices were created in order to provide an intermediate level of management to handle the day-to-day affairs of the wealthy. The family office freed the wealthy individual to make only the most necessary and strategic decisions, without the need to oversee their implementation. In this sense, the family office creates a comprehensive level of management for the client's non-business life comparable to that which usually exists in the client's business; the client, however, remains the chief executive officer and chief operating officer of the client's non-business life.

The second generation of family offices arose after the creators of large fortunes had distributed their wealth among their children and more remote descendants, usually (though not always) at their deaths. This division of wealth created new problems that made a family office particularly appropriate.⁴

Great wealth may make investing more difficult, but it also provides investment opportunities that do not exist for people of lesser means. These opportunities often are not available to the second- and later-generation family members who have only a small share of the wealth of their common ancestor. A family office allows these later-generation family members to reassemble the family wealth, to broaden the spectrum of available investment opportunities, and to obtain the best possible investment advice. It then fully integrates these investment decisions into the family's legal, tax, philanthropic, and personal lives.

MAJOR FUNCTIONS OF A FAMILY OFFICE

In addition to the status currently associated with having a family office (which is itself a prominent, if foolish, reason to have one), there are several good reasons why a wealthy individual or family should have a family office. These relate to the major functions of a family office, a list of which typically begins with the ten functions that the Chicago-based Family Wealth Alliance, which has studied family offices in great depth, uses as a guideline for evaluating family offices.

The Family Wealth Alliance cites the following ten functions as among those most often provided by a family office:

1. Comprehensive financial planning;

2. Portfolio management;
3. Back office/consolidated reporting;
4. Estate and wealth transfer;
5. Tax planning, preparation, and compliance;
6. Risk management;
7. Trustee services;
8. Life management;
9. Family consulting, governance, meetings, and education; and
10. Strategic philanthropy and administration.

Obviously, not all families require all of these services, and some families require services that are not on this list. Nonetheless, this list has become a common basis for reviewing and evaluating family offices. Thus, each of these functions should be examined, along with two common functions that are not on the list.

Comprehensive Financial Planning

Financial planning and portfolio management are two of the core services for most family offices. One of the most advantageous aspects of the financial planning performed by a family office is the consolidation in one financial plan of the wide variety of assets often held by the wealthiest investors.

The very wealthy have complicated financial needs and investment strategies, a fact which usually causes them to deal with a number of different investment advisors and managers. It is common for very wealthy individuals to present the family office with a portfolio that reflects the work of seven or more investment advisors, each acting independently. In many cases, some of these advisors believed that they were entrusted with all or a very substantial portion of the client's portfolio, when they had only a relatively modest portion. Such multiplicity of independent investment advisors often results in a portfolio the asset allocation of which bears little resemblance to the asset allocation that any single advisor would recommend had he or she been entrusted with the entire portfolio.

The family office analyzes all of these investments as a single unit, and determines the best asset allocation for the individual family members and for the entire family unit. The family office may rely on its own financial planners, though outside advisors are often consulted, particularly with respect to highly specialized investments.

The family office evaluates each of the investments already held by the client family, determining where they fit in the financial plan, identifying multiple investments that overweight particular asset classes, and individual assets that are not successfully filling their roles in the family portfolio. The family office then provides the investors with a consolidated evaluation of the total portfolio, recommending specific retentions, dispositions, and additions.

One of the major distinctions between the financial plan created by a family office and that created by other investment advisors is that the family office deals with a broader range of assets, including traditional investment assets, and such “non-investment” assets as artwork, airplanes, yachts, and multiple residences. The family office's investment advisors are keenly aware of the important role that such non-traditional assets play in the wealth of a family, particularly where those assets are likely to be retained for several generations.

Wealthy families spend a substantial amount on non-investment assets, such as residences, yachts, and artwork. The liquid assets of the oldest generation of family members will suffer depletion by both taxes and charitable dispositions on their way to the succeeding generations. The residences, yachts, and artwork, however, are likely to remain in the family for many generations. These assets thus gain in relative importance as part of the total family wealth with each generation. A family office will deal with these assets in structuring the investment portfolio for the client family. One commentator explains this issue well as follows:

Family wealth usually involves a broader range of asset classes than stocks, bonds, and cash. Multiple homes, boats, planes, commodity investments, art collections, various venture capital and private equity investments — all must be considered in designing the asset allocation for each portfolio. The ownership structure of all the assets may also influence allocation, as well as the purpose of the portfolio, its time horizon, and many other factors.

Ultra-wealthy families tend to have a greater understanding of correlation because of the diversity of their assets.... The family may have valuable art collections, significant real estate holdings, or other non-traditional investments. These assets must be taken into consideration when planning an overall asset allocation. Correlation of assets is key to protecting financial assets. This is a critical missing link in asset allocation programs at large firms, which primarily focus on diversification among traditional asset classes and sub-classes.⁵

The family office coordinates the financial plans of various family members and entities, and the family office's financial plan is prepared for the entire family, including members of different generations and trusts for their benefit. This coordinated comprehensive planning assures that the financial plan for children and grandchildren properly takes into account their parents' and grandparents' assets that are likely to pass to the younger generations. The family office also may consider the increasing wealth of one generation of family members in determining how the assets of the other generations should best be invested.

Financial performance of family offices is sometimes superior to that of individual investors or individual investment advisors, because the inter-generational focus of family offices leads them to invest for longer-term than is common with most individual investors. This may be particularly important when investing the assets of inter-generational trusts. The financial plan prepared by a family office may consider how the

family will benefit from certain investments over a century, rather than just over the next five years.

The stock of one or more closely-held corporations sometimes occupies a prominent place in the portfolio of a wealthy family. The family office, in such cases, evaluates the closely held stock to determine whether a low dividend rate and lack of marketability are adequately balanced by the potential for extraordinary growth and employment of family members. The family office also must take into account the effect of the lack of dividend yield of the closely held stock on different generations of family members who may have different approaches as savers or spenders.

Financial planning by a family office includes allocation of both investments and investors. The growth segments of the total family portfolio normally should be held by trusts that will not be subject to wealth transfer taxes or at least by the youngest generation of family members, whose exposure to wealth transfer taxation is deferred for the longest term of any family group.⁶

Investment Management

Investment management also is an important function of the family office, whether performed in-house or through an open architecture that employs the best sub-advisors available for each class of appropriate investment. The family office can evaluate the merit of various outside investment managers for each class of assets against the appropriate indices and benchmarks, and can assure that the management of each family member's portfolio serves a specific purpose in the overall family investment allocation. The pooling of family funds by a family office also allows the family to invest in a wider selection of investments, many of which have entry requirements that would exceed the capacity of individual family members or that would overweight the investment as part of an individual family member's portfolio.

The family office typically constructs a broadly diversified portfolio for the client family, including appropriate allocations of publicly traded equity interests, debt instruments, foreign investments, hedge funds, private equity investments, venture capital, commodities, and tangible assets. The family office often deals with a significant number of expert investment analysts, both in-house and independent outside analysts, because of the complicated nature of the portfolios involved. The family office acts as the clearinghouse for these recommendations. Thus, the family office may deal with many different investment advisors and managers for a particular client family, but the family member needs only to deal with the family office.

Backoffice/Consolidated Reporting

The breadth of investments available to a family office tends to create portfolios that are both highly balanced and widely diversified. Yet, the family office can combine the data

received from many advisors and investment managers and present it in a consolidated, consistent basis in one report, using consistent assumptions and reporting techniques. This may increase the transparency of the investment process, which is particularly important when third party investment advisors or managers are used.⁷

Consolidated reporting is a relatively expensive function for a family office, and some client families are comfortable receiving separate reports from the individual investment managers. The family office can, in such situations, still prepare an overall portfolio analysis that takes into account all of the divergent investments and the manner in which their returns are reported.

Estate and Wealth Transfer

A family office does not plan a family member's estate; that is the responsibility of each family member's personal estate planning attorney. The family office, however, may help assure that the estate plans of various family members are consistent, and that each family member's attorney has detailed and accurate data about both his or her own client and about other family members whose estate plans may affect the estate planning attorney's client.

One leading expert on family businesses commented that “[t]oo much business and estate and business planning takes place in secret.”⁸ A family member will plan to dispose of his or her own estate without knowing what his or her children desire and ought to desire, what they need and ought to need, and what the children's own estate plans (and those of any other relevant family members) may be.

The family office serves as a central repository on information on each family member, and can confirm the accuracy of the data provided by the family members. The family office also is often the repository of documents that support the asset ownership of each family member. In this capacity, the family office can assure that the counsel for each family member has both complete and accurate information, including relevant information regarding family members other than the client himself or herself, where relevant. It also can provide the attorney representing a family member information on the estate plans of other living family members, and on the trusts created by and for other family members, to the extent that they relate to the plans being proposed for the attorney's own client. Neither the attorney nor his or her client may be comfortable asking other family members for data regarding their own estate plans, but compiling and distributing such data is a key task of the family office.

The family office also can propose to the individual family member's attorney one or more ways in which the individual family member's estate plan can be altered to make it more consistent with the plan of the other family members. For example, a child's will that leaves property to the child's own children may be changed when the attorney learns that the child's parents are skipping the child's generation of beneficiaries and leaving property to their own grandchildren. The child will decide to whom he or she wishes to

leave his or her estate, but the family office can make the child and the child's attorney aware of how the child and his or her children will benefit from the parents' estate plan.

The greatest failing of most estate plans is in poor client implementation. It is not unusual for clients to fail to: (1) fund their revocable trusts fully, (2) follow the terms of their buy-sell agreements, (3) follow the terms of their family partnership or LLC agreements, and (4) enforce the relevant provisions of intrafamily loans and sales. Family offices provide oversight for the administration of the estate plans, and can help assure that the attorney-designed estate plan is implemented fully and effectively.

The family office is also often a source of support for the attorney when the client's demands are unreasonable, in light of tax consequences, control, and speed of document preparation. A family member who demands that his or her lawyer prepare estate planning documents before the family member leaves on vacation later that week, is more likely to accept that those demands are unreasonable when told by an advisor in the family office, than when heard from the attorney.

The family office also can give the attorney a chance to explain the proposed techniques to both the grantors and the beneficiaries of a trust, or the donors and donees of a gift, assuring that all parties understand what they will and, perhaps, will not receive from the particular transaction. This opportunity often is provided as part of family meetings and educational sessions, discussed below.

Tax Planning, Preparation, and Compliance

The family office can offer full tax planning, preparation, and compliance services; it also can work with the professionals who are advising the various family members to assure that these services are provided consistently and that the needs and circumstances of all family members are considered. As with estate and financial planning, tax planning can be far more effective when the entire family is viewed as a unit. Income can sometimes be shifted to family members with lower income tax rates, for example, or taxable gains shifted to family members who have expiring loss carryovers.

The family office also organizes the investment data gathered from the family members in order better to implement tax compliance. This is particularly important when the family members own investments in complex partnerships, from which the K-1 forms often do not arrive in a timely manner. The family office can analyze and compile the data received throughout the year, to provide more complete data in advance of the receipt of the actual K-1 forms and thereby reduce compliance problems.

Risk Management

Risk management is an area of increasing concern for wealthy families. Risk management covers such issues as assuring that all family members and ventures have correct liability, excess liability, property and casualty, and health insurance, and that

steps are taken to insulate family assets from the claims of creditors. It also includes such more personal issues as assuring that family members who marry have appropriate premarital agreements, and that all family members have adequate personal safety.

The family office can be a particularly useful way of communicating to family members the importance and need for these services, and arranging for their implementation. Some security services may be personally distasteful to some family members; one may not want a bodyguard because of the lack of privacy, and another may not want a premarital agreement because of the lack of romance. It often is easier to accept that such security steps are necessary when they are advised by the director of the family office or an expert that the director has selected, than when they are advised by a parent.

Trustee Services

An abundance of trusts is a common attribute of great family wealth, because trusts can minimize wealth transfer taxes, assure a consistent and continued capable management of family investments, and shield family fortunes from the importunities of ill-chosen spouses, business associates, creditors, and other predators. Many multi-family offices are organized as trust companies and some private family offices are associated with a private trust company, so that they may serve as trustees of various family trusts.

All family offices, including those that are not organized as or affiliated with trust companies, should be involved in the operation of trusts created by or for their families. The family office can help select and evaluate proposed trustees, establish and enhance communication between the trustee and the beneficiaries, and oversee the trustee's actions.

These services can be of particular importance when family members insist that individuals who are not professional fiduciaries serve as trustees. The family office can oversee their activities, and assure that all tax and legal obligations are being met. They also can provide early warning to family members of any possible deficiencies in the administration of a trust by an amateur fiduciary.

The family office also is important when large corporate fiduciaries serve as trustees of family trusts, because such institutions can sometimes be perfunctory in their communications with the grantor and beneficiaries. They often may not communicate to the beneficiaries all of the actions that the trustee has taken or decisions that the trustee has made; indeed, they often are not legally required to do so.⁹

The family office can provide intermediary services, communicating to the beneficiaries and grantors the decisions the trustee has made and the actions that the trustee has taken, analyzing those actions, and discussing and estimating their long-range effects on the trust and the family. The type of communications that the family office provides can reduce significantly the number of fights, both in and out of court, between or among beneficiaries and trustees, and current and remainder beneficiaries.

Family Consulting, Communications, Governance, Meetings, and Education

The oft-quoted proverb “shirtsleeves to shirtsleeves in three generations” reflects the disparate education, experience, needs, and desires of family members as they move from one generation to another.¹⁰ One of the great accelerators of the descent of a family fortune into relative insignificance is family disharmony. Family disharmony, whether or not it actually erupts into litigation, is an impediment to sound financial and estate planning. The use of a family office to foster harmonic investment and general interaction among family members may be viewed as its highest and best function.

One source of family disharmony is the failure of the second and third generations, whose wealth is inherited, to understand the immense difficulty and sacrifice that was required to create that wealth. This lack of understanding often is made more poignant by the fact that the experience of the members of these later generations with the first-generation wealth-creators is frequently quite unsatisfactory. It is a rare person who can create vast wealth while providing substantial time and attention to children and other family members. It is a rare child or grandchild who will consider great inherited wealth to compensate fully for a childhood of parental or grandparental coldness and absence.

Family disharmony also results from the fact that money amplifies and highlights: it makes one more of whatever he or she already was. The children of the wealthy are no more emotionally insecure and unbalanced than those of the less wealthy. Some children of the wealthy want to work hard and contribute to society, while others want to spend and test the limits of indolence. Substantial sums of money merely make both character traits more obvious and increase their impact. It also makes it easier for the public to notice the less desirable of these traits in some family members, often to the embarrassment of other family members.

This magnified distinction between the contributions and costs of various family members can create serious rifts within a family. One family member may feel that he or she works hard to support non-working relatives, who may themselves feel that they are not being supported in a manner to which they believe themselves entitled. These rifts can destroy a family and a family fortune with speed and efficiency.¹¹

The family office can help foster family harmony by balancing the ever-increasing number of divergent opinions within the family, with a continued emphasis on the core values and goals upon which the family's financial and personal future are based.¹² The family office offers a structure by which family members with differing interests and views can interact without hostility. This structure may be as simple as semi-annual family meetings at which every family member has a chance to air his or her views and grievances, to a more complicated representative structure. The family governance of each family office is individual and depends upon the size, dynamics, investment complexity, and needs of the client family.¹³

Family governance usually begins with a family mission statement, drafted by the family office in concert with the family members.¹⁴ The mission statement can set forth the family's financial and personal goals, the roles and responsibilities of each family member in achieving those goals, and the services that the family office is expected to provide towards reaching those goals. It also may establish a significant role for philanthropy, and any preference for a family foundation or other specific charity as the recipient of charitable gifts.

The mission statement often also documents the family's agreement regarding how, in broad terms, their wealth will pass from generation to generation. The mission statement may provide, for example, that the family wealth should be invested in a manner designed to maintain the family fortune, keeping up with inflation but taking no additional risks that might be required to increase the family fortune. It might state that the more speculative portion of the family portfolio will be invested in start-up businesses, rather than smaller existing businesses, or that certain industries or locations in the world will be stressed or avoided. It could express a preference for investing in family-owned businesses or businesses that adopt "green" policies. The mission statement does not typically address specific asset allocation, however, as this is likely to change as economic and world conditions change.

Mission statements also explain the core family values and beliefs, regarding the role of each generation in structuring the future of the family and in maintaining its financial and personal standing. It may establish rules for maintaining family privacy, discouraging conversations with the media on certain subjects, or enhancing public recognition of the family's activities, encouraging conversations with the media.

Mission statements also may address the question of the family office as the employer of last resort. Some families view the family office as a training ground for the brightest and most promising family members, and as an employer for those who find few other offers. The mission statement may state whether family members will be employed by the family office, and the minimum standards of education and experience that will be required for employment.

Family governance problems tend to increase in the third and later generations, as the number of family members holding substantial portions of the initial fortune grows sometimes to triple-digits. The children of the first generation are likely to make most of the important family decisions after the death of the members of the first generation, and those second-generation family members who are not economically productive may clash with those who are more interested in preserving or expanding the family fortune. As grandchildren age, they also may wish to participate in family investment and other decisions.

The mission statement for larger families often creates a family council to provide a form of representative government for the family unit.¹⁵ A family council provides a means by which a great number of family members can interact in a reasonable and orderly manner, and creates an orderly and reasonable method of making family decisions. The

mission statement will describe how membership in the family council is determined, and whether certain groups of family members participate directly or through representatives. Family councils can be a great means of permitting family members to air unpopular views without acrimony. It is usually better for family members to air unpopular views in front of a professional, who can provide a fair and impartial analysis, rather than to suppress those views and to have them erupt later with greater violence (and, often, in court).¹⁶

Family councils also often provide for training of family members who wish to become active in the family governance. The family council also may have an auxiliary council in which interested family members can receive specialized training in finances and other areas of importance to the family office, and may observe, without a vote, the actions of the family council. This assures a continued source of capable family members to constitute the family council.

The family office also minimizes disputes and disharmony by assuring that all family members obtain consistent advice from the same group of experts, and that their financial and estate planning decisions, as well as many of their personal decisions, are made with the same high level of informed intelligence. The family office assures that the needs and desires of the entire family, and not just those of the most vocal members, are considered in all decisions. The likelihood that a family member will feel ignored is much lower when all family members share and have the same access to the same advisors.

A family office also is a very useful means of educating the family members regarding the reasons for various estate planning and financial techniques and strategies, and regarding the details of such non-financial topics as personal development. Such education often includes periodic family seminars on investments, estate planning, trustee-beneficiary relationships, and other issues of concern to the family. It also may include finding or establishing internships and mentoring arrangements for younger family members.

The individual attorneys and other advisors for family members, even if not employed by the family office, often are invited to attend and participate in such educational opportunities, enabling them to understand more fully the overall family needs. This also minimizes unrealistic expectations and disappointed hopes, and tends to promote general satisfaction with estate planning recommendations.

The family office may enhance family harmony by organizing periodic family meetings. These meetings emphasize the family's sense of shared heritage and cohesion and its desire to achieve consistent goals. After two or three generations, family members may be quite widely dispersed, and organizing such meetings may be a significant undertaking.¹⁷

Strategic Philanthropy and Administration

Family offices often are particularly useful in integrating charitable giving by various family members.¹⁸ The office can assist the family foundation in its operations, and

assure that various family members coordinate their gifts to the best tax and non-tax effect. It also can assist in either minimizing the publicity that sometimes accompanies great philanthropy, or in maximizing the benefits of such publicity.¹⁹

The IRS stated in PLR 200238053, that it is not self-dealing for a family office to require the family private foundation to reimburse it for expenses incurred for the benefit of the foundation. The donor of the private foundation in that ruling also had created a family office that provided personal services to meet the business needs of the donor, his family, and various for-profit business enterprises. The family office services included accounting, bookkeeping, asset management, business travel, tax, investment, secretarial, and administrative and support services. The family office provided similar services to the foundation, as well as support services related to the foundation's particular operations and other services related to the preservation and handling of the foundation assets for charitable use. It also served as liaison with outside advisors, such as legal counsel, tax and accounting advisors, banks, and various consultants, including consultants hired by the family office to assist the foundation in accomplishing its charitable programs.

The grantor had been paying all of the expenses related to the services provided all of his various interests. The family office now proposed to provide personal services to the foundation and the grantor's other family interests, under a cost sharing service agreement.

The agreement stated that each party would pay the family office directly for his or her allocable share of its operating expenses, based on time incurred by the employees of the family office and the actual direct and indirect costs of the services provided by the family office's employees. The proposed agreement stated that the family office would provide the following services: accounting, bookkeeping, coordination of tax matters, investment management, business travel, administrative support, coordination with outside advisors (including legal counsel, tax advisors, and various consultants) and administrative assistance for the foundation's charitable programs. Secretarial services, previously performed by the family office, would not be included in these agreements.

The agreement also stated that the foundation would not be charged for any services performed on its behalf other than those directly in furtherance of its exempt purpose. The foundation would not pay rent or make lease payments of any type to the family office.

The foundation represented that the services to be provided by the family office were necessary for the carrying out of its exempt purposes, including the management of its assets and the administration of its charitable activities. In addition, the foundation represented that the fees charged for these services would be reasonable, and to ensure their reasonableness, the family office would continue to contract with an independent consultant who specialized in employee benefits and human resources issues to review both the service agreements and the salary of each employee.

The IRS stated that the foundation's payments to the family office for its services provided through the agreements would not be an act of self-dealing under §4941(d)(1).²⁰ The IRS explained that, generally, the furnishing of goods, services, or facilities between a private foundation and a disqualified person is an act of self-dealing,²¹ but that the payment of compensation (and the payment or reimbursement of expenses, including reasonable advances for expenses anticipated in the immediate future) to a disqualified person for the performance of personal services that are both reasonable and necessary to carry out the exempt purposes of the private foundation is not self-dealing, unless the compensation (or payment or reimbursement) is excessive.²²

The IRS explained further that both the grantor and the family office were disqualified persons, with respect to the foundation, but charging the foundation for the services of the family office under the proposed service agreement was not an act of self-dealing. The IRS stated:

It has been represented that, O will provide these services to you on an allocable basis. O will use an independent consultant with experience in employee benefits and human resources to ensure that the fees charged would be reasonable. It has been represented that these services are directly and indirectly related to accomplishing the purposes for which you have been recognized as exempt. Therefore, we have concluded that this arrangement is analogous to the situations described in examples one, two and three of §53.4941(d)-3(c)(2) of the regulations.²³

Life Management

The category of “life management” services covers a wide variety of functions, some of which involve very substantial sums of money, and some of which involve less tangible considerations. Life management services are one of the things that distinguish a true family office from a traditional trusteeship or investment advisory relationship, in part because life management services demand an enormous amount of flexibility and personal interaction from the family office administrators.

Some of the life management services that involve substantial sums include evaluating whether it is better to lease or buy a private jet (or, perish the thought, fly commercial), and assuring that the acquired jet is properly staffed, housed, and insured. The family office also can help a client evaluate and find accessions to the client's collections of art, antiques, or artifacts, and assure that these items, too, are properly housed and insured. Such items sometimes bridge the areas of life management and investment, to the extent that acquired assets may represent a non-traditional investment portion of the total family portfolio. The family office also can assist a family member in locating and arranging for personal or business credit, where necessary.

Some of the life management services that may not involve as substantial a sum include helping family members select attorneys, accountants, and other professionals, select the best private school or university for a child, evaluate and arrange for medical care or a

nursing home for an ill or elderly family member or special rehabilitative services for a family member with drug or other substance abuse problems, and obtain worldwide medical help by private subscription.

Another very important life management issue is helping each generation address the fact that each child and his or her family is very likely, despite extensive planning, to have less wealth than the family in which he or she was raised. This is an almost invariable result of the division of the wealth among multiple children and more remote descendants, the imposition of estate and generation-skipping transfer taxes, and the making of charitable dispositions.

Addressing this issue requires that each family member understand why this result is likely, if not inevitable. Each family member needs also to learn how family investment strategies and spending patterns affect this process. They also must learn how to deal with requests from friends for loans that are unlikely to be repaid, or investments that are unlikely to be successful.

Concierge Services

The Family Wealth Alliance list of family office services does not specifically include concierge services, but most single-family offices and a few multi-family offices provide some level of such services. Concierge or “personal” services include such functions as making travel arrangements, obtaining hard-to-find tickets to events, hiring a personal chef or personal trainer (or, more logically, both), and even arranging for the retrieval of objects left behind on vacation.²⁴

These services tend to be the most-often written-about facet of the family office, even though they represent a tiny portion of the operations of a family office. These services do make the life of the wealthy family office member easier, but the family office must be careful not to create a generation of family members who take no personal responsibility for their actions.²⁵

It is easy to criticize these personal services as obscene indulgences for the rich, but one also should consider that some of these services, such as hiring household staff, may be more difficult for the very wealthy than they are for more ordinary people. Household staff (including the aforementioned chefs and personal trainers), must be carefully scrutinized, and their backgrounds must be thoroughly checked, to assure that they are not likely to kidnap a child, steal valuable artwork or jewelry, or expose the details of the family's personal life.²⁶

Gatekeeping

One way in which the very wealthy are very different from the rest of us is that they have far more people vying for their time, interest, and money. Though also missing from the

Family Wealth Alliance list, the family office often is a tool for insulating the wealthy individual from these nuisances, while not rejecting out-of-hand appropriate contacts. The wealthy do not necessarily begin life as a reclusive group, but their wealth attracts so many people asking for favors and attention, that they tend to become very private people — Donald Trump, Paris Hilton, and Nicole Ritchie to the contrary notwithstanding. The family office can free the wealthy from a substantial portion of unwanted attention- and favor-seekers, so that the clients can interact with society in a more open manner.²⁷

SINGLE-FAMILY VS. MULTI-FAMILY OFFICES

Family offices are usually divided into single-family offices and multi-family offices. These terms are misnomers, but they are used so widely in any discussion of family offices, that they will be relied upon in this article (with appropriate explanations of their inaccuracies).

Single-Family Offices

A single-family office is one that serves the needs of one family, and that uses its own employees (as well as outside advisors in appropriate circumstances) to provide the various professional services required.²⁸ Single-family offices also may serve the needs of a small number of separate families whose wealth arises from a common source, such as the families of the founders of a single successful corporation.²⁹ Multiple families whose wealth arises from a common source often have extensive social and financial ties that make it practical to treat them as a single family for this purpose. Single-family offices that serve such families of common interest, however, have very special governance problems. Special effort must be made to maintain the same relative control each family has in the affairs of the office, regardless of how many descendants may share in that control in each generation.

The single-family office offers several advantages over a multi-family office, discussed below, but also suffers from several disadvantages. The single-family office's primary advantage is its ability to focus all of its efforts and attentions on the needs of one family. This can enable the personnel of a single-family office to develop a deeper understanding of the needs and desires of the family members they serve, and possibly better to address them.

Grove and Prince, in their 2003 survey, report that the primary reason given by wealthy families for creating a single-family office, however, is control. The wealthy want to have absolute control over the people who will be advising them.³⁰ This control is one of the key benefits of the single-family office format.

The primary disadvantage of the single-family office is its high cost. The physical office, technological equipment, and staff requirements make it very expensive to operate a single-family office, limiting its utility to only the wealthiest families, though the

threshold for such offices depends upon the services required and the efficiency of the operation created. A single-family office that provides only common bookkeeping and accounting services may be created for as little as \$250,000 a year, and may be practical for a family with a combined net worth of \$50 million.

A single-family office that provides a full range of family office services, including comprehensive investment, tax, estate planning, bookkeeping, accounting, and family governance services, often will cost at least \$2 million a year to operate, and is practical only for those with at least \$200 million in investable assets. The greater the complexity of the family dynamics and investments, the greater will be the cost of maintaining a single-family office. The \$200 million figure assumes a relatively harmonious family with relatively conventional investment objectives.

One of the biggest problems faced by a single-family office is finding and keeping key personnel. The executive director of a single-family office must be someone who understands fully how a family office operates, and who can help develop the special relationships that must exist among the experts and teams that work within the office, and between those experts and teams and the members of the family. A wealthy individual often decides to start a family office by hiring the individual's personal attorney or investment advisor to create and direct the office. Such professionals may be excellent at their jobs and may fully understand the needs and desires of the family, but they typically lack an understanding about how a family office operates and how the members of the family office must be selected and must interact.

It also is very difficult for a single-family office to retain its best people. The single-family office has, by definition, limited opportunities for advancement within the office itself.

A single-family office cannot usually maintain a staff with the same breadth of skills and expertise as can be maintained in a multi-family office. Many of these skills can be hired from outside advisors, but such advisors will not understand the important family dynamics, or the existing estate and financial planning, and they will not necessarily be skillful in working with the other members of the family office. The use of a large group of outside advisors also can increase the risk of a breach in the confidentiality of family information.

A single-family office also often will not have enough assets under management to make available the widest possible selection of investments. This may lead to the creation of a portfolio that is not diversified with the same degree of sophistication as will exist with a larger single-family office or a multi-family office.

These disadvantages have resulted in the creation of the “supported” single-family office, in which the single-family office becomes a member of a multi-family office, or a group of single-family offices merge to create a multi-family office. These approaches give the single-family office access to a broader selection of advisors and investments, without greatly expanding the circle among which family information is disseminated.

Multi-Family Office

A multi-family office is an independent entity that provides family office services to a large number of wealthy families, recognizing that these families have overlapping needs.³¹ Multi-family offices give their member families the advantages of a family office, without the administrative oversight responsibilities or the need to create an appropriate infrastructure. They are far less expensive to operate, and they extend the family office concept to individuals with as little as \$10 million of investable assets.

Multi-family offices often are organized as corporations or limited liability companies. Many multi-family offices now are organized as trust companies, enabling them to provide full trust management services, which are often important to a family office, without restricting their ability to provide the other services that the individual family may require.

Grove and Prince distinguish between those multi-family offices that have an anchor family and those that do not. This distinction is sound and meaningful. Many multi-family offices began as single-family offices, but later decided to allow other families to participate. One or more members of the anchor family often manage such multi-family offices, and the anchor family may have a substantial amount of assets held by the office. An anchor family tends to produce an office with a history of dealing with family issues from a first-hand perspective. It also creates a history of family dynamics and harmony (or disharmony) that families wishing to participate in the multi-family office may examine in order to ascertain whether they wish to replicate the anchor family's own experiences. Among the better known and larger of the multi-family offices with an extant anchor family are Pitcairn Trust (the author's employer), Rockefeller & Co., and Whittier Trust Company.³²

Some investment and accounting firms have created multi-family offices, in an effort to capture a share of the business generated by multi-family offices. Such multi-family offices often merely repackage investment and tax services, and do not offer the fullest range of family office functions. Families seeking a true family office should carefully scrutinize the range of services offered by these multi-family offices, to be sure that they are acquiring all of the services that they need.

Several major banks, investment houses, and trust companies have created family office divisions or affiliates. Such organizations as JP Morgan and US Trust are good examples. It is not yet clear how well these large retail organizations will handle the personal and family dynamics that are common in family offices, and whether they merely will use their family office operations to sell other investment, loan, and business services that they offer to the public.

A few multi-family offices offer their services strictly by electronic communication, creating so-called virtual family offices.³³ These obviously are less expensive than

physical family offices, but they also lack the permanence and presence required to coordinate family issues over a long term. It is unclear how well virtual family offices will serve to implement recommended estate and charitable planning arrangements. These entities may be able to consolidate bookkeeping, reporting, and information for an entire family, which is certainly an important purpose of a family office, but it seems unlikely that they competently will be able to provide a full range of family office services.³⁴

The multi-family office offers several advantages, and suffers from several disadvantages, in comparison to the single-family office. One of the major advantages of a multi-family office is that it can provide a full array of family office services at a substantially lower cost than can a single-family office. This makes the multi-family office ideally suited for the individual or family with net worth of \$10 to \$50 million. Such individuals and families often have financial and tax needs that are as complicated as much wealthier families, and their family dynamics can be at least as complex and troublesome as those of wealthier families.

Second, a multi-family office can assemble a wider expertise and create more complex structures to address the problems of the family than can a single-family office. This is possible because the multi-family office necessarily deals with a greater selection of family needs and desires, and of family relationships than does a single-family office. These experts also can be fully integrated into the operation of the office, unlike the outside expert brought in by a single-family office to handle a single matter. They already will work together better, and know each other's strengths and weaknesses, and share a commitment to a high level of personal service.

Some single-family offices have addressed this structural disadvantage by becoming themselves clients of multi-family offices. The single-family office contracts with the multi-family office to provide a range of services that may be beyond the capacity of the single-family office. This also preserves to the family the sense that their family office is wholly theirs, and permits the integration of trusted family advisors into the family office, without forcing those advisors to give a full scope of services. This appears to be a growing trend, as a means of affording the wealthy family the benefits of both structures, though often with the disadvantages of both, as well.³⁵

The principal disadvantage of a multi-family office, vis-a'-vis a single-family office, is that the personnel within a multi-family office are not as focused on the needs of one family as are those of a single-family office. The personnel in a multi-family office must focus on the needs of several different families. To a certain extent, this diversity of experience enhances expertise and makes the personnel of a multi-family office more effective in dealing with the needs of each individual family.

The focus on the personal needs of the family is a learned skill. This may make it more likely that a multi-family office that originated as a single family office will be better able to establish a close focus on the individual family situation than would one that arose from an investment advisory firm, bank or brokerage house.

PRINCIPAL EMPLOYEES OF A FAMILY OFFICE

The family office counsels the wealthy individual and implements his or her decisions. To accomplish this, the office typically assembles a group of advisors in whom the wealthy individual has confidence, and who are always available and familiar with the individual's particular situation and needs. The selection of advisors is highly individualized; some family members integrate into their family offices a substantial number of existing advisors, while others rely largely on the personnel selected by the administrator of the family office.

It is facile (though rather true) to say that each family office is unique. Like most trusts, most family offices share many fundamental features; also like each trust, each family office has its own idiosyncratic needs and issues. Both a single-family office and a multi-family office are likely to undertake several important functions on a continual basis. These functions each require specific expertise, which may be provided either within the office itself, or by outside advisors. Even when outside advisors are used, however, the office must have someone who can evaluate and select advisors, review recommendations and decide which should be recommended to the family for implementation. The complexity of the staffing requirements of any family office is determined by the complexity of the family situation, the nature of their assets and investments, their family dynamics, and the special needs of various family members.

Many family offices will have internal staff to perform some of these functions (typically accounting and bookkeeping, trust administration, philanthropy, and communication with family members), but they will hire outside experts to provide one or more of the more specialized services, such as hedge fund investments, venture capital, specialized asset investments, and legal services. Of course, even those family offices that outsource many services still must employ persons to coordinate, review, and analyze the recommendations of these outside advisors, and make the ultimate recommendations to the family members.

Investment Managers and Financial Analysts

A family office may have one or more high-quality investment managers and financial analysts. The precise list of advisors required depends upon the nature of the family's investment strategy and the amount of wealth under management. Obviously, one wants expertise on sophisticated portfolio allocation and selection of publicly traded equity and debt instruments, but it is common for a family office also to need the skills of specialists in various forms of private equity, hedge funds, venture capital, commodities, and alternative investments, including artwork and antiques. If one or more family members have a special collection, investment specialists in that field may be particularly important.

One of the key advantages of any form of family office is that the investment advice given to each family member is part of an integrated whole; the advice given to the parents can take into account the investment focus of the children, and vice versa. Thus, the investment managers and financial analysts must deal with various family members, and consolidate the advice given to these family members, in order to create a superior overall family investment strategy.

Trust Administrators

Virtually all family offices need a professional trust administrator, because families with wealth sufficient to justify a family office almost always will create a substantial number of trusts, to save taxes, provide professional management, divide benefits among multiple beneficiaries, and limit the availability of assets to claims of creditors, spouses, and ex-spouses of beneficiaries. A family office that is not structured as or affiliated with a trust company and cannot serve as a trustee can still oversee and evaluate the administration of the trusts and explain to the family the work of the individual and corporate trustees.

Lawyers

Family offices almost always employ lawyers, because only lawyers can fully understand and appreciate the work of other lawyers. The family office needs its own attorneys to review and coordinate the work of the attorneys who represent individual family members, to explain to family members the recommendations that they have received from their own attorneys, and to assure that the legal work that is done is fully and properly implemented. The attorneys for the family office also can assure that the data provided the attorneys representing family members is complete and sufficiently detailed. Most adult members of any wealthy family have their own attorneys by the time a family office is created, and the lawyers in the family office attempt to augment and enhance the work of those professionals, rather than duplicating it. The family office and its lawyers must know when to refer a family member to his or her own lawyer, and when to advise the family member that the matter is not worth litigating or, in some cases, even negotiating. The independence of the family office often gives the advice of its own lawyers special weight to the family member.

Accountants

A family office needs accountants for many of the same reasons it needs attorneys: to review and coordinate the work of the accountants who advise individual family members. The accountants for individual family members often handle their tax compliance and related issues, such as preparing individual and fiduciary income tax returns and gift tax returns. The family office typically has its own accountants to do this work for those family members who do not have their own accountants, and to assure that the work of the accountants representing individual family members is consistent and, to

the extent required, coordinated with that of other family members. The family office accountant can help assure that all family members who participate in an intrafamily transaction report it consistently, reducing the likelihood of an IRS audit and tax penalties. The accountants for a family office also often will evaluate financial reports provided by various investment managers and create a uniform basis for reporting the performance of diverse investments to the family.

Common bookkeeping for family members is one of the traditional family office services. This may include paying the salaries of and handling withholding for personal employees of family members, paying the personal bills of family members who do not wish to do so themselves, and creating cash flow and budget analyses. This is important even if the services of the family office do not include hiring or firing domestic employees.

Family Governance Experts

The extent to which family governance is important in a family office varies widely from office to office, generation to generation, and family to family. Most family offices that continue for more than one generation need some form of family governance to minimize dissention and disputes, and to maximize the value of the contributions of various family members to the economic and personal success of the entire family.

Family governance experts are usually psychologists who have devoted time to the study of family relationships. They can help a family create a family governance structure that assures that every family member is informed as to the investment and other decisions that are made by and for the family, why those decisions are made, and that those decisions are consistent with the family's values. They also can help assure that all family members believe that their views are being heard and considered, that good ideas are not ignored merely because they come from family members who have historically had few of them, and that bad ideas are not implemented merely because they come from family members who have a good track record of creative planning.

Family governance experts also can help assure an orderly transition in the de facto control of the family from one generation to the next. The phrase “control of the family” has a somewhat sinister connotation in a post-Sopranos world, but it is common for one or more members of any family to wield a disproportionate amount of power over the decisions of the family. This control may stem from the fact that the particular individual is the wealthiest, the oldest, the most intellectually gifted, or simply the most aggressive family member. The death or incapacity of such a family member can have an effect on the economic growth of a family unit similar to the effect of the death of a key employee of a corporation on the business's success.³⁶ A family governance expert can arrange for orderly succession in the control and operation of the family, in much the same way as a business consultant arranges a business succession plan for a family-run business.

Insurance Experts

Someone in a family office usually advises the family on the purchase of life, health, casualty and liability insurance policies, and assists in administering such policies. This is especially important if one or more family members own unusual assets, such as an historic residence or a substantial collection of art, antiques, or artifacts. Adequately insuring such items often requires skills and expertise not possessed by the typical insurance agent.

Some family offices have their own subsidiaries or affiliates chartered to write life insurance. Other family offices have insurance experts who obtain and evaluate proposals from various well-chosen insurance professionals, and assist the family in selecting the best insurance arrangements for their special situations.

Health Care Advisors

As the wealthy population ages, the family office often has personnel who can assist in evaluating and obtaining health insurance and quality health care. A good family office develops expertise on medical conditions from which family members suffer, evaluate the sources of the best and most appropriate care and arrange such care for family members. The family office may need to become adept at arranging for medical care in many locations, because the family is far-flung or because one or more family members travel widely.³⁷

Personal Security Experts

Some family offices retain experts on personal security. This is especially important for offices whose families have a high profile or travel to parts of the world in which kidnapping is a recognized form of business enterprise. The 2003 Grove and Prince survey of family offices revealed that approximately 30% of family offices currently provide security services. The authors of that survey estimated that this number is likely to double by 2009.³⁸

The family office also can help ensure family confidentiality, by retaining family records and documents, and by controlling the distribution of family information among outside advisors. This, in turn, can enhance family security, as each distribution of family information makes it easier for others to take illegal or improper advantage of family members.

Contact Person

Multi-family offices typically create a team of three or more professionals for each member family. These teams will include whatever professionals are most likely to be

important to the particular family, working together with a contact person. The contact person is the individual whom the family members call whenever they have a problem or question, and who keeps the family members informed about the actions of the family office.

The contact person and other team members are assisted by professionals in the other areas of concern or interest to a particular family member, such as specialized investment, insurance and security experts. The team may, of course, be far larger than three members, if the needs of the particular family so dictate.

The contact person is not like the primary care physician at an HMO. A family member who has a narrow problem need not always go first to the contact person; he or she may consult directly the appropriate specialist within the family office.

Concierges

Some family offices do employ individuals who are skilled in such things as buying tickets to popular events, hiring nannies and domestic servants, and acquiring hard-to-find luxury goods.³⁹ Family offices that do provide such services may employ one or more full-time concierges and even a travel agent.

WHEN A FAMILY OFFICE IS ESPECIALLY APPROPRIATE

There are an almost infinite number of situations in which a family office can be a useful tool in organizing and managing a family's wealth. The following are some of the more common and interesting situations in which creating a family office can be useful. Some are virtually classic situations that call for a family office; others are somewhat more unusual and a family office may not be the most obvious solution. In each instance, the amount of wealth to be administered and other personal factors will determine whether a single-family office or a multi-family office better serves the client.

The Newly-Liquid Business Owner

A closely held business may be immensely valuable, but its owners may not feel very wealthy, because they are using the bulk of the business profits to develop and expand the business. A business owner who sells or plans to sell the business for cash or publicly-traded stock, or whose business finally starts to generate substantial cash in excess of the amount needed for its future needs, presents a classic situation in which a family office can be an important tool for personal and financial growth.

Many business owners are very familiar with the family office concept; they often create a type of informal family office within their businesses. Their assistants in the business (often including the Chief Financial Officer or Chief Operating Officer) will use office

staff to handle the principal's personal investment decisions, and arrange for various personal services. The sale of the business, however, renders unavailable this informal family office, necessitating its replacement with a true formal family office.

The sale of the family member's business can have as dramatic an effect on other family members as it does on the business owner. The business owner's spouse and children find themselves suddenly wealthy and may just want to spend money, or they may want to understand exactly what their new wealth signifies, both in terms of their own lives and the lives of future generations of their family.

It is difficult to keep secret the sale of a significant privately-owned business. The local press will report or at least speculate on the amount that the individual received for his or her business, causing the former business-owner to become subject to substantial requests for time, attention, and money. Again, a family office can act as a gatekeeper, protecting the business owner from such unwanted attentions.

With increased wealth and exposure comes an increased risk of being subject to crime, both violent and non-violent. The likelihood of kidnapping, burglary, confidence tricks, and identity theft increases as one's wealth and public attention increase. This raises a serious need for all types of security, which can be provided through a family office. Suddenly rich, a former business-owner now may move to a larger residence, buy one or more vacation residences, or both. All of these require a staff to maintain them and provide for the comfort of the owners. The business-owner has not been personally responsible for staffing decisions in a very long time, and the other family members have never been responsible for staffing decisions. This adds an entirely new level of complexity to their lives.

Often, former business-owners adopt one or more new hobbies. Golf and tennis are not major life-complicating factors, but breeding horses, racing cars or boats, collecting art, or collecting antique cars can create a new array of insurance, storage, security, and staffing issues.⁴⁰ Again, the family office can assist in managing these interests.

More money, more things. More things, more complexity. More complexity, less peace. Less peace, less happiness. See Jimmy Buffett quote at beginning of article.

The Family Office as Tool of Family Financial Succession

The family office that is created by the business-owner or former business-owner often raises special family governance issues. Many business owners succeeded by adopting a fairly dictatorial decision-making style. This style often is reflected in a dictatorial family governance structure.

The family office must, at least initially, reflect the demands of the wealth-creator, even if those demands are not in the long-term best interests of the family. The family office structure then can be used to increase both the competency of the next generation of

family members to handle the family affairs and fortune, and the wealth-creator's recognition of that capability. A wealth-creator who recognizes that the next generation is capable of managing the wealth that will pass to it, ultimately will be likely to pass this control to the next generation at an opportune time, when the wealth-creator remains available to counsel and advise, even if not to dictate.

The family office always attempts to create this type of planned, orderly succession of control over the family functions and the family fisc. Sometimes, however, the iron grip of the wealth-creator continues unabated until death. Whether the succession is well-planned or precipitous, it raises the second principal situation in which the family office may be a useful tool for managing family wealth — the family office as tool of family financial succession.

Many controlling elderly clients eventually become concerned that their death, disability, or retirement will precipitate a rapid decline in the family fortunes, because the family lacks a clear successor. Such a family chief financial officer recognizes that a vacuum in family leadership can, without adequate preparation, be disastrous.

The outgoing family chief financial officer often discusses this problem first with his or her estate planning attorney. In a less fortunate situation, the attorney for a deceased family member's estate may be asked to advise on the succession of control over the family finances, where the deceased has refused to surrender the control until death.

Too often, the attorney advises leaving or placing the family funds in trust with a competent professional fiduciary. This advice is standard, competent estate planning, but it is deficient in several ways.

First, non-investment assets, such as residences, planes, yachts, artwork, and collections, represent a significant portion of the wealth of most very wealthy families. Most professional fiduciaries are ill-equipped to manage these assets, particularly when their use will be shared among multiple family members. As a result, these assets often are left directly to various family members, who then must arrange for their shared use. The family financial plan is too often constructed without regard to these assets.

Second, combining a very large trust fund with a professional fiduciary and a wide group of beneficiaries who are unfamiliar with how financial decisions are made, how financial assets are managed, and the proper relationship between fiduciaries and beneficiaries, is a fine formula for fiduciary litigation. A good estate planner creates a trust or series of trusts that protect the fiduciaries from the costs of excessive litigation, and that make it difficult for disgruntled beneficiaries to upset the fiduciaries' sound professional judgment. A great estate planner creates a structure that substantially reduces the risk of that litigation, by educating the beneficiaries as to how the trusts will function and how their wealth must be administered and managed, and allowing the beneficiaries to participate in the decision-making process for the management and administration of their family's wealth. The former approach requires one or more trusts. The latter approach requires a family office, and one or more trusts.

A family office is the best means of assuring proper succession in family financial management, whether instituted by the wealth-creator or by the next generation. First, the family office establishes a means of both educating the family and permitting them to participate in the decision-making process. If one or more family members have the interest, intellect, and skill to become the new chief financial officer, they can do so. If they lack this skill, intellect, or interest, the family office creates a structure through which the entire family can participate in selecting a proper family chief financial officer. This also can be done while the present family chief financial officer is available to assist and advise.

Second, the family office creates an important line of communication between the new chief financial officer and the other family members. The chief financial officer meets with the family, either directly or through their representative family council, and communicates to the family how the financial plan is being implemented and how it meets the family's goals and objectives. The family office also permits family members, either directly or through their family council representatives, to communicate regularly with the chief financial officer, to raise any questions regarding the financial operations, and to clear up any misunderstandings before they erupt into open hostilities.

Reunifying the Family's Economic Power

Another classic situation in which a family office is useful is where the family fortune has been recently dispersed among a new generation of family members (and, in most cases, the federal government, through estate taxes). The deceased parents had a net worth of \$300 million, but state and federal estate taxes took one-half of the estate, and the remaining \$150 million was then divided among three children. These children now must re-evaluate their lives on the basis of their wealth, which is much reduced from that of their deceased parents.

The range of investment options available to someone who has \$50 million is smaller than that available to someone who has \$300 million, or even \$150 million. A family office can assist the children by pooling the children's investable assets, maintaining to a far greater extent the array of investment options that had been available to the deceased parents.

Keeping the Liberated Family Members in Line

An individual who has had substantial liquid assets may decide to make substantial lifetime wealth transfers to family members, rather than relying solely on testamentary transfers. This often is sound estate tax planning, as well as a way to observe the donees' enjoyment of the transfers and receive the donees' lavish expressions of gratitude. Unfortunately, children who are no longer financially dependent upon their parents also are free to express contrary views on various social, political, financial, and family issues,

and to ignore requests from their parents to pursue courses of action that the parents view as appropriate or desirable, but that the children view as boring or ill-conceived.

A parent-donor may therefore find that decisions that once were made by fiat now cannot be made at all, or can be made only after long negotiations. A family office can provide the structure and governance to help keep financially liberated family members in line (and, perhaps, educate the older generation as to the actual needs of the younger generation, where appropriate).

Caring for the Infirm Elderly Family Member

A noted attorney who specializes in elder law recently proposed an interesting use of the family office for certain elderly clients. The attorney stated:

The Older Client must consider reallocating his or her investments to pay for needed services and care. Frequently, the Older Client must cease to live independently and seek long-term care assistance in his or her home or in an assisted living facility, continuing care retirement community, or nursing home. In-home care agencies and long-term facilities have contractual agreements that the client must review and execute. The elder law attorney should assist the client in establishing a mechanism to provide or obtain the delivery of necessary services and assistance. We call this mechanism a 'Family Office.' The Family Office will ease the financial burden experienced by our Older Clients and their families.⁴¹

The aging of the population thus has created a substantial new function for the family office—arranging for the care of aged and infirm family members, supervising the institutions and personnel who provide that care, and in appropriate situations, assuring that financial arrangements made for such care are implemented fully and correctly.

CONCLUSION

The family office was once a tool only of the very rich, and relatively few attorneys and other professionals had contact with even one family office. Now, particularly through the use of the multi-family office, family offices are available to virtually all families for which they may be useful.

A family office can enhance and simplify the personal lives of families of moderate or great wealth, increase their economic prosperity, and reduce family discord. It also can substantially enhance the effectiveness of the estate plans devised for family members by their own attorneys, enable the attorneys to provide better representation for their clients, and reduce the chances that the attorney's good ideas will be frustrated by poor implementation, inconsistent planning by other family members, or family in-fighting. Estate planning practitioners should consider the family office a significant tool to help clients obtain both long-term financial and personal success.

Footnotes

1 J. Buffett, “We Are The People Our Parents Warned Us About,” from the album, *One Particular Harbor* (MCA 1983). The author's fondness for the music of Mr. Buffett prevented insertion of a “sic” notation after the word “was” in the first line of the quote, to indicate that the correct word is “were,” in the subjunctive mood. One allows a certain degree of artistic license for classic Gulf and Western music.

2 See Greycourt & Co., “White Paper No. 10 — Establishing a Family Office: A Few Basics,” available at www.greycourt.com [hereafter Greycourt No. 10].

3 Greycourt No. 10.

4 One recent study notes that the wealthy are, as a group, happier than the middle class, but that they do not believe that more money has made them any happier. Their middle-class counterparts might not agree with that assessment. The Worth-Harrison Taylor Study on the Status of Wealth in America at 17 (2005) [hereafter The Worth-Harrison Taylor Study].

5 Gray, *The New Family Office: Innovative Strategies for Consulting to the Affluent* at 60 (Euromoney Inst. Investor Plc 2004) [hereafter Gray].

6 See Hughes, *Family Wealth — Keeping It in the Family* at 63-68 (Bloomberg Press, 2d ed. 2004 [hereafter Hughes].

7 This can be an expensive process where there are a great many different classes of investments managed by a great many different investment managers, and some families may choose to consolidate reporting of less than all of their investments. Also, consolidated reporting delays reporting of some investment results until all results have been received, which can cause undue delays, particularly when some of the investment managers are outside of the United States.

8 LeVan, “Representing Estate and Trust Beneficiaries and Fiduciaries: Creative Settlements,” SH002 ALI-ABA 95, 101 (July 18-19, 2002) [hereafter LeVan].

9 On the Uniform Trust Code and common law requirements that a trustee provide certain information to the beneficiaries, see O'Brien, “The Trustee's Duty to Provide Information to Beneficiaries: When Can the Settlor Say ‘Don't Ask; Won't Tell?’” 40th U. Miami (Heckerling) Inst. on Estate Plan. Ch. 4 (2006); Millard, “The Trustee's Duty to Inform and Report under the Uniform Trust Code,” 40 Real Prop. Prob. & Tr. J. 373 (2005).

10 As a study of wealthy families explains:

The phenomenon of the fleeting family fortune is so well-recognized that it inspired a proverb: “Shirtsleeves to shirtsleeves in three generations.” Vanishing wealth is not unique to the United States, and variations of this proverb are found around the world, from Asia to Ireland. The Irish variant — “Clogs to clogs in three generations” — depicts things in the following way. The first generation starts out wearing work clogs while digging in a potato field, receives no formal education, and through very hard work, creates a fortune while maintaining a frugal lifestyle. The second generation attends university, wears fashionable clothes, has a mansion in town and an estate in the country, and eventually enters high society. The third generation's numerous members grow up in luxury, do little or no work, spend the money, and fate the fourth generation

to find itself back in the potato field, doing manual labor. It is a classic three-stage process: first, a period of creativity, second, a period of stasis or maintenance of the status quo; and third, a period of dissipation.

Hughes at 3. This same authority also notes that the Chinese have their own proverb, “rice paddy to rice paddy in three generations.” Id. at 7.

11 See also Cohn, “Integrating Family Governance and Legal Architecture for Family Business Clients,” 40 U. Miami Est. Plan. Inst. Ch. 13 (2006); Boyce-Abel, “When to Use Facilitation or Mediation in Estate and Wealth Transfer Planning,” Family Office Exchange, Vol. 9, No. 35 (1998).

12 See generally Report of the Family Office Exchange, “Recasting the Central Role of the Family Office as Risk Manager” (2006).

13 See Gray, ch. 8.

14 See a very good discussion of mission statements in Bourland, “Implementation and Documentation of the Succession Plan,” SM003 ALI-ABA 689 (July 2006).

15 One of the leading writers about very wealthy families describes the process of family governance as follows:

Wealth preservation is a dynamic process of group activity, or governance, that must be successfully re-energized in each succeeding generation to overcome the threat of entropy.

* * *

To successfully preserve [sic] its wealth, a family must form a social compact among its members reflecting its shared values, and each successive generation must reaffirm and readopt that social compact.

Hughes at 14, 19.

16 See LeVan at 106. LeVan notes that one of the more difficult and important issues in establishing a family council is membership:

Shall the family council include spouses? Children above a certain age? Fiance'es? Significant others? Shall in-laws and children have voting privileges? What are the responsibilities of the family council? What matters are appropriate agenda items, and which issues are out of bounds? For example, what input should the family council give on family employment issues? What is the purpose of the family council? For most families, the purpose is tied to the family business or to shared family wealth.

Id. at 116.

17 Even family offices that generally do not offer travel arrangement services often handle the travel arrangements for family meetings, to reduce the risk that one or more family members will find it unnecessarily difficult to attend, or will miss portions of the meeting due to poor travel arrangements.

18 One study notes that the longer a family has had wealth, the greater their charitable motivations. This reflects a strong desire to give back, and a comfort level with their possession of more assets than they will need. See Worth-Harrison Taylor Study at 22-23.

19 The latter approach often is highly desirable when the manner in which the family wealth was created is accompanied by labor or antitrust problems. The “taint” of ruthless

business practices often can be cleansed by several decades of substantial philanthropic efforts.

20 Unless otherwise noted, all section references are to the Internal Revenue Code of 1986, as amended, and the regulations promulgated hereunder.

21 [26 USC 4943(d)(2)(E)] §4943(d)(2)(E); Regs. §53.4941(d)-2(d)(i).

22 Regs. §53.4941(d)-3(c)(i).

23 See also 879 T.M., Private Foundations — Self-Dealing (Section 4941); Crozier, “Maddening Uncertainty on the Scope of the Personal Service Exception to Foundation Self-Dealing,” 14 Tax'n of Exempts 251 (May/June 2003).

24 Not all multi-family offices offer these services. Rockefeller & Co., for example, does not offer most such services. See Rottenberg, “Inside Room 5600,” Bloomberg Wealth Manager 89, 90 (Sept. 2004).

25 One may note, of course, that it always has been common for the wealthy to delegate a substantial portion of the more mundane aspects of their lives to trusted staff. A reasonable amount of such delegation is both common and appropriate. A family office may want to avoid taking over responsibility for an excessive portion of the family members' lives, however.

26 See a good discussion of this point in Shapiro, “Family Matters,” Worth Magazine (Dec. 2002).

27 One study notes of the very wealthy that “[t]hese people know they are wealthy and that their money is a magnet for chicanery and merchandising.” Worth-Harrison Taylor Study at 30.

28 Most articles refer to a single-family office as an SFO. This one eschews such abbreviations.

29 I prefer to refer to such single-family offices as “limited-family offices,” but as there appears to be no recorded use of this term by anyone other than me, it will not be used outside of this footnote. Pity.

30 See Grove and Prince, *Inside the Family Office: Managing the Fortunes of the Exceptionally Wealthy* (Wealth Management Press 2004) [hereafter Grove & Prince].

31 Most articles refer to a multi-family office as an MFO. What went for the use of the term SFO goes equally well for the term MFO.

32 See, e.g., Edwards, “Family Office Issues,” SH002 ALI-ABA 95 (July 2006) (referring to commercial offices). These offices also are referred to as “multiple client family offices,” in at least one study of family offices. Gray at 43.

Grove & Prince refer to anchor-family offices as multi-family offices, and to family offices that have no anchor family as commercial offices. This distinction is meaningful and it has been used elsewhere, but it is not yet widely accepted and will not be used in this article.

33 See, e.g., Gray at 85-86.

34 It is unclear whether there even exists a wholly virtual office offering a full spectrum of services linked together electronically. First, the technology for linking such services is not thoroughly seamless. Second, such electronic linking does not create the full synergy that occurs when different advisors are physically present to work on a single matter. Virtual participation by some specific advisors, however, may work well in individual situations. See Gray at 48.

35 See Beer, "Special Report: Multifamily Offices: Varsity Crew," *Bloomberg Wealth Manager* 43 (Sept. 2005).

36 The effect of the death of a dominant family member usually is negative, like the effect of the death of a key executive of a corporation. Of course, occasionally the effect is surprisingly positive. Most estate planners can recall at least one situation in which the children of a deceased business owner were surprisingly successful in running the family business after their parent's death. One can never really be sure what to anticipate, but planning usually should assume the more likely negative result.

37 Providing these services has become more difficult as medical offices have become more strict in their dissemination of confidential medical data and in their refusal to discuss a patient or prospective patient with persons other than immediate family members.

38 Grove & Prince, "Competing As a Family Office," *Financial Advisor* (June 2006).

39 See LeVan.

40 Some readers who are avid golfers or tennis players may question my characterization of these activities as "not major life-complicating factors." They may become a major focus of one's life and they may become very expensive hobbies, but they do not often involve serious depletion of family capital or employment of extensive personnel. One may make an exception for the golfer who builds and maintains his or her own course, or the tennis player who builds several indoor tennis courts and hires a full time tennis pro, but these are distinctly the exception.

41 Hook & Begley, Jr., "Lawyering For Older Clients: A New Paradigm — Part 2," 32 *Est. Plan.* 46 (May 2005).