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For a number of wealthy families that maintain single-family offices (SFOs), the 2008 financial crisis caused an intensive examination of the structure and even the viability of these offices. Declining asset bases, poor investment results, hedge fund blowups, and over-allocation to alternative (illiquid) investments have all combined to rattle many families. In addition, there are increasing service, compliance, and tax and estate planning requirements that are making many offices and families consider alternatives to their current approach. According to a study of single-family offices by Hannah Shaw Grove and Russ Alan Prince, “about four in ten family offices are considering a full-scale merger with another entity” (Grove and Prince [2009]).

There are several alternatives for these families to consider: merge with another single-family office; merge with a multifamily office (MFO); co-op with other offices; close; or build their own MFO. All of these strategies clearly have plusses and minuses for the founding family. Making the right decision requires extremely careful analysis of the family’s goals for the management of their wealth and the successful continuation of their legacy. The following are among the goals for most families:

- Receive top-notch wealth management services;
- Receive a high level of personal service;

- Maintain organizational and staff stability for their wealth management firm;
- Pay reasonable fees for the services required;
- Maintain confidentiality; and
- Maintain control (if possible).

As pointed out well by Charlotte Beyer and Timothy Brown in *Families in Business*, “Unless the MFO has the commitment and resources of its owners to stay current with the latest information management technology, to retain key employees by compensating them like owners and to maintain the absolute integrity of the MFO in all aspects of its business, the MFO will not be the long-term solution sought by family business owners and their families to the complex challenges they face” (Beyer and Brown [2008]).

If a family chooses to go the route of an MFO to gain scale, the choices it has are to either merge with an existing MFO or build its own. Merging with another family office might be a viable option to immediately increase the scale of the office. However, the merging offices must be compatible, families with similar philosophies and culture. Each SFO typically has a unique personality molded by or for its founding family, and a “marriage” may not be easy.

Obviously, building its own MFO is a very significant undertaking for a family, requiring long-term commitment, experience, significant capital, and a strong belief that this

approach will best foster family success and unity. Very few organizations have been able to successfully navigate from an SFO to an MFO given these stringent requirements. Glenmede, Rockefeller, and Bessemer are the notable exceptions. Bessemer's transition to an MFO and the depth of reasoning behind the decision may be useful to other wealthy families as they consider their future.

Henry Phipps established Bessemer Trust in 1907 after selling his interest in Carnegie Steel to J.P. Morgan. It served as the bedrock of his vision for preserving and enhancing his family's wealth for generations.

In the early 1970s, the Phipps family (Davis [2007]) began to consider the future of the office in light of the increasing cost of operating a first-rate company that provided comprehensive investment, trust, and other wealth management services. After the 1973–1974 stock market decline, the family's assets were approximately \$1 billion, a substantial amount. However, Bessemer Trust was a fully staffed organization with more than 200 employees. It had even developed its own IT system. In addition, Bessemer served increasingly more family members; there were 100 by the time I arrived at the trust in 1975. Adult members of the founding family all very appropriately expected to receive individual attention for their investment, tax, and estate planning needs. With inflation rising during this period, expenses were increasing in all areas, but particularly in maintaining Bessemer's professional staff and the recordkeeping system. Further, there was increasing need for specialists in the investment area to implement new strategies in international investments, precious metals, oil and gas, and other commodities. In fact, the current environment for SFOs is reminiscent of Bessemer's experience in the 1970s; today SFOs are faced with increased costs related to heightened compliance needs, service needs for family education, family governance, and investment due diligence for alternative investments, among other expenses.

With help from A.T. Kearny and McKinsey & Company, Bessemer explored its options, which were essentially the same available to families today: sell (or merge), reduce services, or expand to become an MFO. It rejected the option to sell, an unacceptable alternative that could have resulted in loss of control, reduction in the level of service, or the loss of the family's unity and legacy.

Reducing services to core capabilities, such as investment and fiduciary services, and eliminating tax, concierge, and other services was another ultimately rejected option. Bessemer Trust's history since its founding in 1907

had been as a *comprehensive* wealth manager, the family reasoned, and this was viewed as key to the family's total financial success, even if it was expensive. In fact, it was excellent estate planning in the 1930s and the use of generation-skipping trusts that enabled a significant portion of the family's wealth to avoid estate tax for multiple generations.

While expenses were high as a percentage of assets under management, the Phipps family had been quite pleased with investment performance and service. As a result, the family believed that Bessemer's services would be attractive to other families. Therefore, in 1974 it decided to build out an MFO and take on other families. The process began with the charter of a national bank and trust company in 1974. Bessemer's family office had always been organized as a trust company, unlike other SFOs that operated only as service companies. The trust structure offered several benefits for the family, including: 1) greater financial stability and soundness through financial regulation; 2) facilitation of a long-term estate plan; and 3) maintenance of control of family assets over multiple generations.

Our experience suggests there are several key strategies required for success as an MFO:

- *Treat shareholder and non-shareholder clients the same.* It is imperative that non-shareholder clients receive equal access to investments and planning advice, along with a level of service equal to that offered shareholder clients.
- *Focus solely on serving very substantial families.* While some MFOs focus in part on institutional or smaller retail clients, the best MFOs remain focused on ultra-high net worth families.
- *Add directors outside the owner family to gain added insight and experience.* By including some directors outside the owner family, an MFO gains important input from people with varied business or legal experience. Non-shareholder clients will also feel more comfortable that the owner family's interests do not dominate decisions.
- *Maintain client service at the level of an SFO.* The hallmark of an SFO is an extremely high level of service, and a successful MFO will remain committed to keeping client/staff ratios low. Delivering a high-quality client experience is something families desperately want that is severely lacking at most wealth management firms.
- *Attract, provide incentives for, and retain professional management and staff to achieve client goals.* The success

and sustainability of any MFO depend highly on building a team of committed professionals. Two factors have aided Bessemer's success: 1) an ownership interest by management; and 2) compensation tied to client-centric goals, not merely to profitability. For many SFOs, the greatest challenge has been to create a professional staff that maintains the service mentality required by wealthy families, yet delivers investment and financial expertise that competes with that of the best Wall Street firms. An MFO with a growing client base allows for the financial success necessary to provide competitive compensation and to offer career opportunities for younger professionals.

We believe an SFO that evolves to an MFO should measure its success in three principal ways: 1) the performance and service the family has received as clients; 2) the continued stability and ability of this entity to insure the proper management and control of its wealth and family legacy; and 3) financial success. As measured by financial stability, Bessemer Trust stands out from many competitors that have been acquired, are in financial distress, or no longer exist. Furthermore, Bessemer serves as a vehicle for maintaining the founder's legacy and is a focal point for family reunions and family communication.

The MFO's financial success can be measured in two ways: by the expenses owners incur in receiving service from it, and by its market value. With regard to the first, the owner's expenses should diminish significantly, perhaps by as much as 50% over time, as economies of scale are realized. As to market value, because the typical wealth management firm is valued at perhaps 3% to 4% of assets under supervision, the "value" of the MFO can be considerable. Even if an owner family has no interest in selling the office, as is the case with Bessemer Trust, the creation of that new business is gratifying. Turning the "expense" of having one's wealth managed into a significant asset (and income stream) is an attractive outcome. A final, intangible benefit to the owner's family is its ability to attract significant non-shareholder families to its MFO, which gives the owner family comfort that it (as a "captive" client) is receiving highly competitive services and paying competitive fees.

Families that are considering a transition from an SFO to an MFO must weigh all the tradeoffs associated with creating a larger, more profit-oriented business. As described by Patricia Soldano and Kathryn McCarthy, "The most significant reason that it's so difficult for SFOs

to convert into MFOs is that, usually, their cultures are just too different" (Soldano and McCarthy [2005]).

In addition to culture, they cite a number of areas of change that may prove disconcerting for the owner family, including:

- *A more formalized decision-making and reporting process.* A single family can be served on a more informal basis, but external clients require well-documented decision-making and reporting to the SEC, OCC, and other regulatory bodies, which can result in less flexibility and responsiveness for clients.
- *Personnel who may value compensation over service.* While its larger scale permits the MFO to hire better talent, this talent may have a greater interest in compensation than the previous SFO's staff.
- *Building an infrastructure that can be more costly than anticipated.* The scale of a larger client base can spread costs over a greater number of users, but IT, compliance, and other expenses can eat up that benefit quickly if not managed properly.

In summary, a number of families will be considering how to most effectively manage their wealth over the next few years and whether their current family office structure is optimum. For some, a change may be necessary and a merger or sale may be a viable option. A small number of families may consider turning their SFOs into MFOs. However, only with a unique combination of commitment, capital, culture, and personnel can this be a successful option.

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