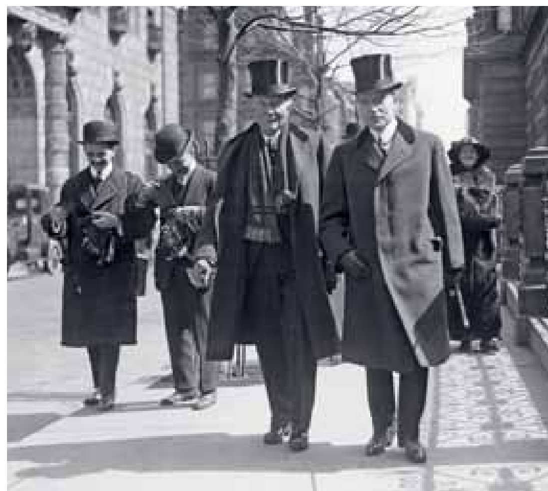
THE NEW RULES OF WEALTH MANAGEMENT

Lauren Razavi examines how families are protecting themselves and growing their assets in these turbulent times



Above: *The Standard Oil Company made John D Rockefeller, seen here with his son in New York, the world's first US dollar billionaire in 1916*
Right: *Rockefeller Center*

Rags to riches tales never truly end with the closing credits. While earning a fortune can make a great story, maintaining it isn't quite so glamorous: according to the Williams Group wealth consultancy, some 90 per cent of wealthy families have lost their wealth by the third generation. What's more, it's an issue that will affect growing numbers of people. In North America alone, the next three decades will see roughly $30 trillion in assets transferred from baby boomers to their heirs. So as money passes from one generation to the next, families should plan carefully to ensure their financial legacies live on.

The concept of professional financial planning has been around a long time. Kings, queens, tsars and maharajahs have for centuries employed specialists to manage the finances of their countries, and in England the Tudor monarchs, who ruled from 1485 to 1603, created the position of Lord Steward to handle the royal household's financial affairs.

But as economies developed and wealth spread beyond royal families and their aristocratic cousins, new models of wealth management arose. For example, in recent history few clans have commanded as much global wealth and influence as the Rockefellers. The Standard Oil Company made patriarch John D Rockefeller the world's first US dollar billionaire in 1916. By this time, the famed industrialist was already two decades into retirement, and part of his fabled success was down to his decision in 1882 to set up his own office of finance professionals to organise his business operations together with his family's growing investments. In doing so, he created what is often known today as a "single family office": a private wealth management firm dedicated to overseeing the fortune of one family.

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Since the heyday of the Rockefeller dynasty, the financial world has become immeasurably more complex. Globalisation has opened up new markets and investment possibilities, innovative companies and individuals have created whole classes of new financial instruments, governments and financial authorities have put in place tier upon tier of new regulations, and information about market conditions and investment opportunities has never been more widely available.

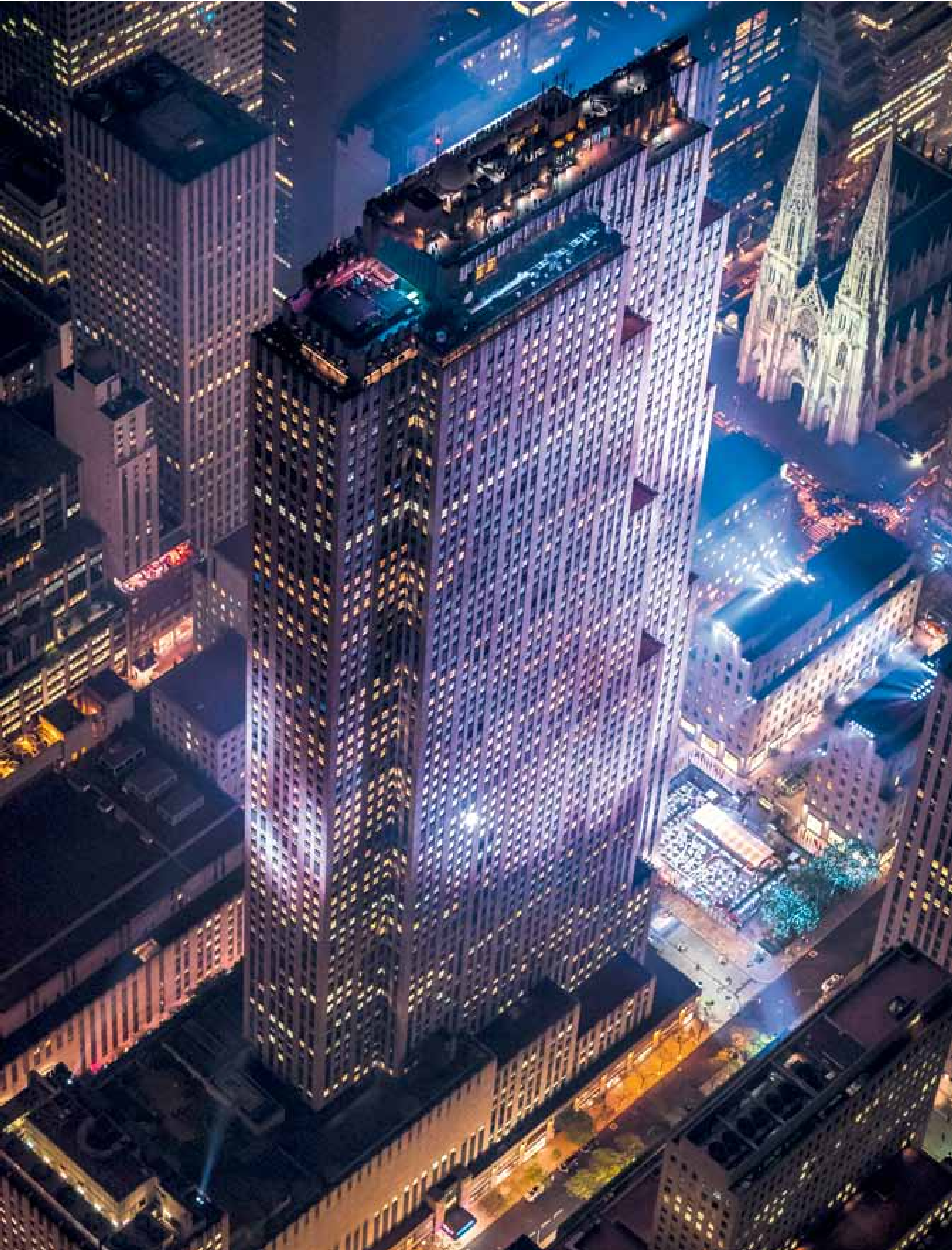
For some wealthy individuals, these developments have led to a dangerous temptation: the idea that the best person to manage their fortune is themselves. If they happen to be a highly successful and well-informed investor, that might possibly be true, but for the vast majority the evidence points to this simple conclusion: that professional financial advice and management get the best results.

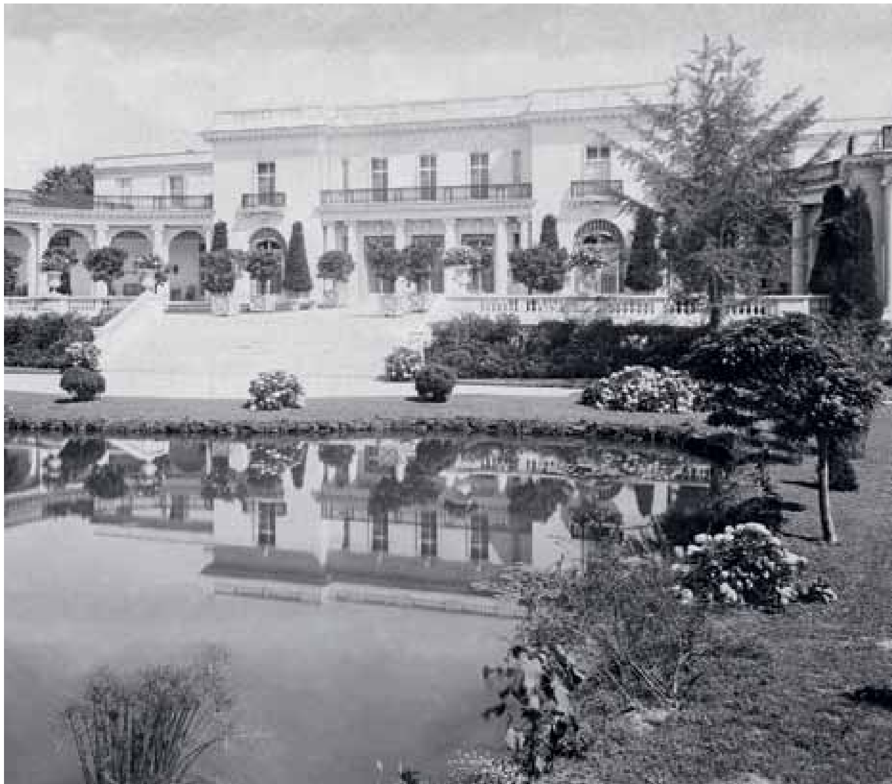
"You'd be surprised how many people invest money into unregulated investments," says Richard Curtis, a financial adviser at AMAS Investments, based in the east of England. "Most advisers worth their salt will be able to tell you whether an investment opportunity is a scam."

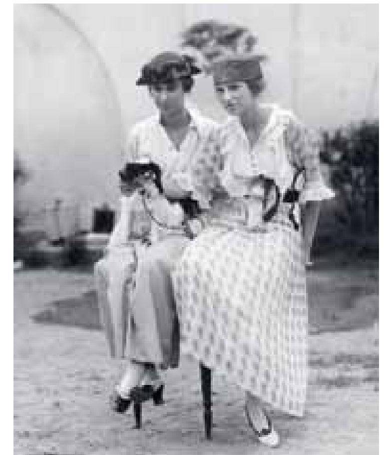
A survey by management consultancy Aon Hewitt and investment advice firm Financial Engines found that participants who received investment advice earned, net of fees, 2.92 per cent per annum more than those who didn't get help. Qualified advisers and wealth managers have the expertise that matters.

It's also worth noting that family wealth won't always be maintained if funds are simply tucked away in trusts that are spent or neglected by beneficiaries. Active investment is important. But it's critical, too, that wealthy families seek advice and investment services that will result in good returns over the longer term, rather than potentially spectacular but risky returns in the short term.

"Most of the families we deal with have a long-term view. Whether it's for them personally or for the next generation, they're looking after their money in the long term," says Robert Paul, executive director of the US Family Office at London



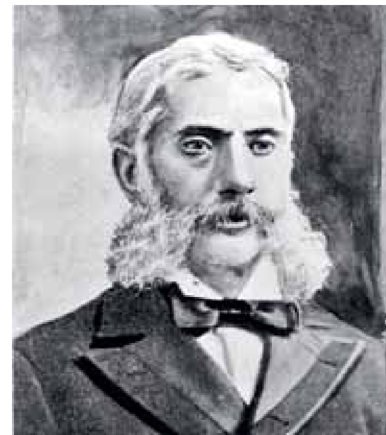




Clockwise from top: *Karol Vail, granddaughter of Peggy Guggenheim and curator of the Solomon R Guggenheim Museum; Benita and Peggy Guggenheim; the Guggenheim family estate in New York, 1910. In the late 1800s the Guggenheim family possessed one of the largest fortunes in the world. They later became known for philanthropic activities*

& Capital, a global wealth and asset management company. "The families that have money these days are less interested in sexy products. It's about clear, transparent investments."

The amount of estate or inheritance tax levied on a fortune varies by country. In Japan, estates worth more than 600 million yen are subject to a 55 per cent tax rate, the highest in the world. In the UK and the US, inheritance above a designated threshold is taxed at 40 per cent. Setting up trusts and succession guidance can help to safeguard against inheritance tax. But the relatively low thresholds for inheritance tax mean that business magnates are not the only ones who need measures in place to keep their wealth within the family. Once an individual is wealthy enough to be vulnerable to taxation, it's probably time to seek professional advice. "Distribution of wealth is something you need to consider as you start to reach the threshold for the amount of money you can pass on to your family tax-free," says Curtis. "When you're young, perhaps your priority is buying a house. You start saving once you've got more disposable income. Then you speak to a financial adviser to help steer you in the right direction."



Meyer Guggenheim, the patriarch of the Guggenheim family

Another potential problem, according to Alexandra Altinger, CEO of London's Sandaire, an international investment office that caters to wealthy families, is the natural expansion of families over time. "With every generation the number of children generally grows," she says, "so when the wealth is passed down it becomes fragmented. The greater the fragmentation, the smaller the individual pots become, and the harder it is to invest in a diversified way, or in illiquid opportunities."

Further, the rate that money vanishes will depend on the spending habits of the heirs. A study by Ohio State University's Center For Human Resource Research found that the average adult who receives an inheritance only saves about half of it. The rest is spent, donated or otherwise lost.

Uncontrolled spending even gets a mention in the Bible. In the parable of the prodigal son, the younger of two brothers asks his father for his inheritance, only to run away and squander it. It would be easy to attribute this kind of behaviour to a person's being spoiled, but the underlying cause is often not self-indulgence alone, but the struggle faced by the children of the rich to find a sense of purpose in the shadow of a successful relative. "One of the greatest challenges for second and third generation wealth-holders is shaping their own identity in light of the legacy they've received," says Diana Chambers, president and CEO of the Chambers Group, a wealth-mentoring firm. "First generation wealth creators are often powerful figures. When the legacy is very significant, second and third generation family members may struggle to identify and follow their own unique paths."

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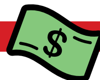

So whether the problems faced by a particular family relate to tax, family conflict, excessive spending, or fragmentation, action is necessary. That action could include putting legal agreements and structures in place, or it might mean establishing trusts and other investment vehicles. The key to getting the formula right is to consult a specialist.

For the newly wealthy, a financial adviser might be a practical first port of call. These professionals offer advice on many elements of their clients' financial lives, including investments, mortgages, taxes and estate planning. Financial advisers often specialise in different products and planning services, and prospective clients should seek out advisers with the expertise they're looking for.

High and ultra high net worth individuals can also turn to wealth managers to build them an investment portfolio and coordinate future planning. Various types of finance specialists – from investment brokers to private bankers – can brand themselves "wealth managers", but the key point that sets wealth managers apart from financial advisers is that they manage a client's portfolio directly. In some cases, this can mean playing the role of coordinator across a client's existing network of tax and legal specialists.

"When we have new high net worth clients on board, one of the first things we do is make sure that they have an estate planner, a lawyer and an accountant who understands all the jurisdictions that this family have to report to," says Paul. "We might say, 'This is how we should manage the money,' but we have to make sure it's managed in the right structure."

Beyond wealth managers, there's one further possibility for ultra high net worth families who want truly personalised attention: family offices providing services not typically available at traditional investment houses. There are two types of family office: single and multi-family. A single-family office will serve one ultra high net worth family, while a multi-family office will deliver expertise to a number of wealthy clients. Some multi-family offices are simply expanded single-family ventures, while others are divisions of existing wealth management firms.

Clockwise from left: *Miwako Date, president of Mori Trust Hotels & Resorts, a unit of Mori Trust Co; a view of Tokyo; a boy and his mother look at visitors waiting outside Toranomon Hills, developed by Mori Building Co, in Tokyo*

The difference between a wealth management firm and a multi-family office isn't always easy to pinpoint, especially if the former specialises in providing planning services to families. However, the distinction can usually be found in the degree to which a company's offering is tailored. For instance, family offices will often help their clients set up philanthropic outlets for their wealth, and will provide guidance on lifestyle management.

"Wealth management firms mainly manage money, and that's only part of what a really wealthy family needs in the long run," explains Patricia Woo, a trust fund and tax lawyer at international law firm Squire Patton Boggs. "Some people do want to manage their money, but sometimes they want to invest in things that banks or wealth managers don't want to touch. The advantage with single-family offices is that families are able to hire the people that they need to create something that's otherwise not available."

Akira Mori (left), president and CEO of Mori Trust Co, and Minoru Mori, his brother, who passed away in 2012. The Mori family is one of the wealthiest in Japan, where estates are subject to a 55 per cent tax rate, the highest in the world

Last year, multinational professional services firm Ernst & Young's Family Office Report stated that there are more than 10,000 single-family offices in operation globally, at least half of which have been established in the past 15 years. The document cites the increasing concentration of wealth held by ultra high net worth families, paired with rising globalisation, as the reason for the growth in single family offices. But Woo has also observed increasing dissatisfaction with the wealth management products offered by major banks, especially in emerging markets.

"If you go to a big private bank, or to a global custodial bank," she says, "they'll tell you that they have some products for emerging markets, but they'll be embedded in a fund that is run by the bank. If a family wants something very specific, they can only achieve it within their own family office."

One factor that will determine which wealth management structures are accessible to a family is net worth. Evidence cited in Ernst & Young's Family Office Report suggests that a full-service family office would cost a minimum of $1 million per year to run, which means that a family should be worth somewhere between $100 million and $500 million for a family office to be financially viable. For international consulting firm Capgemini the net worth threshold is lower: in 2012 it published a report which said multi-family offices are affordable for ultra high net worth families with wealth of around $50 million.

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While choosing the right professionals is key to creating a prudent portfolio of investments that will deliver long-term returns, so is preparing heirs to inherit wealth. Communication between advisers and family members is key, for example, no matter who a family decides to employ to manage their wealth. Ultra high net worth families using family offices will often use a family governance structure to manage their relationship to their wealth and businesses.

"Family offices have to be fully aware of what the family wants to achieve in the long run," explains Woo. "This can only be done through education and communication, by building understanding in the family. Family governance is an internal system that is documented so that families have that understanding."

Any family making use of wealth management services has a twofold responsibility: to understand where their money is going and to understand their relationship to it. Even if establishing formal family governance isn't part of a family's chosen solution, family members and their advisers must be committed to transparency. Without transparency, the task of managing conflicting personalities and expectations will be all but impossible.

"Families that are successful are skilled in multiple dimensions," says Chambers. "They communicate effectively about their wealth and the topics of concern to their family, they genuinely trust and support one another, and they prepare their next generations for the responsibilities that will be theirs."

Outsourcing wealth management responsibilities to trusted professionals is a time-honoured tradition for wealthy families. In today's world, the picture is more complex, more concerned with technology and more likely to involve objectives – such as sustainability – rather than simply maximising returns. But whether you're using the services of a small wealth management firm or a multi-family office, the goal is the same: to preserve your financial legacy across generations.

While few can hope to replicate the success of the Rockefellers, finding the right professional advice and investment guidance will certainly help high net worth families maintain, and even grow, the wealth they pass on.