

Family offices in Europe and the United States – A different evolution with common objectives

“It requires a great deal of boldness and a great deal of caution to make a great fortune, and when you have got it, it takes ten times as much wit to keep it.” – Nathan Mayer Rothschild (1777–1836)



By Dr. Steen Ehler
 Managing Director
 Ferguson Partners Family Office
 Zurich and London

Opposed to common belief, although the term “family office” originates from the U.S., the concept of generic “offices” or “gatekeepers”, “protectors of family wealth” etc. goes considerably further back, i.e. to the Crusades and the concept of the “trust”, but also to banking families in Europe (Medicis, Rothschilds). In fact, even during the Shang dynasty in China (1600 B.C.) and merchants in ancient Japan, there were individuals and groups of people dedicated to serving, protecting and preserving families and their members across several generations.

Comparing different strands of evolution and schools of thought relies heavily on different cultures, laws and regulations, even if in recent times,

there has been a certain cross-fertilization of models as well as an assimilation. Despite of this, specialization and differences have remained to this day.

Depending on the various branches of families, jurisdictions, education, business activities etc., there are usually *several offices* in various locations, taking advantage of different regulations and opportunities. This differentiation probably becomes more apparent between more *local* and *global* families, especially also in terms of the location of the HQ and subsidiaries (mostly centers of service excellence).

A considerable number of structures and organizations act as family offices, even if they don't bear the denomination “family office” or even regard themselves as acting as such, but merely as “*hommes d'affaires familiales*” or “*chefs d'orchestre*”. Hence it is time to pose the question “why do families really need, want or have family offices, i.e. who really needs one?”

When the extent of the overall family wealth exceeds a certain size and the number of family members, activities, businesses, wealth classes etc. reaches a certain complexity and opaqueness, there is the call for a *central coordinating resource* which has the global (consolidated) *overview* and control over these activities – on the business and *wealth side* as much as on the *human side*. To name a few of the common denominators and needs served by family offices, there are the following:

- Tailored/individual approach catering to family needs (financial/non-financial)

- Reduction and management of complexity
- Access to a wide range of (best-of-breed) experts, services and opportunities
- Consolidated view, non-emotional controlling and reporting of overall global wealth
- Professionally run service organization
- Reduction of cost – increase in efficiency, decrease in redundancy
- “Advocatus diaboli” for families
- Business learning for next generation
- Training, education and succession planning
- Family cohesion – “glue” by means of family constitution, family charter, family governance
- Family values, stewardship and philanthropy

In order to understand, how different the offered service propositions (in-house or outsourced) developed, it is essential to understand the differences which led to the existing models in Europe and the U.S.

Europe – from endogenous banking to open architecture

European banking goes back to antiquity and the Crusades. Due to various religious conflicts, it was often the “solver of needs” rather than the creator of demands. Banking activities evolved from lenders to *preservers* of family fortunes and played a key role for entrepreneurs, merchants and trade. It was the Medicis, the Bardis, the Jewish bankers, Swiss Protestant bankers, but also Scottish bankers, who played a

key role in trade and politics throughout Europe.

In a generic sense, families like the Rothschilds and other families and dynasties had their “family offices”. The “old” banking houses/families acted as entrepreneurs, i.e. they were the forebearers of today’s multi-client family offices (MFOs), as they offered their services to others, beyond their own families – for a fee. They also played a key role in the industrial revolution and the financing of infrastructure in Europe. Some banks retained their specialization catering to wealthy private clients, whilst others took on the financing and commercial banking role.

Hitherto, (private) banking in Europe had been considerably more *heterogeneous* than in the U.S. It has always been about tradition, protection and *preservation* (wars, political unrest etc.) and especially about *confidentiality*, not necessarily about transparency and performance. However, it was not until the creation of the modern portfolio theory, that many private banks began to focus more on pure asset management and less on the overall global wealth needs. The “industrialization” of private banking led to more inhouse funds being created and actively solicited instead of finding solutions for clients.

Like with hedge funds, it was the cognoscenti UHNWIs and families, who had their own networks of providers and access to non-mainstream opportunities. Many wealthy families and entrepreneurs had independent structures (inhouse banks, trading, forex), which, besides the banks, catered for their own needs – acting per se as *single family offices*.

Simultaneously, the family banks and family-owned private banks acted increasingly as “families/banks for other families”, a pre-form of MFOs, had that term been known in those days. For the landed gentry, on the other hand, stewards, estate offices, consiglieri etc. had a long tradition, running especially the non-financial side of families.

Throughout this recent decade, European banks have started offering more comprehensive services (back to their roots), besides the focus on mod-

ern portfolio management, which had taken the upper hand since Markowitz. As a consequence, despite a certain organizational separation, trust services are often an excellent entry point to more comprehensive services. On the other hand, banks with commercial banking, lending facilities and corporate finance offer “one-stop-shopping”.

The jury is still out when it comes to answering the question of *independence* and conflicts of interest, when family-office services are offered within banks, as they are unfortunately often merely regarded as new “distribution channels”. Simultaneously, private offices have become aware of the need to be run more professionally and *profitably*, not just as cost centers, i.e. family offices have become *businesses* in themselves, no longer mere centers of administration.

Due to the above-described evolution and emphasis on client confidentiality, a large number of family and private offices are not accounted for in statistics and research. Foundations, trusts and charities in civil-law countries often operate on a very low-key basis, opposed to the more outgoing approach of Anglo-Saxon and Anglo-American entities.

U.S. – from networks of professional advisors to professional networks of advisors and banks

In the late 19th century, some industrial families and family dynasties, due to the lack of private banks, started out their own “private (investment) offices”, which gradually “opened up their doors” to other families. In the U.S., there has always been a strong tradition of large “family trusts”.

Financial planning, homogeneity, optimization and growth as well as a more extroverted view (also in terms of charities and philanthropy) are the main characteristics to describe wealth management in the U.S. Due to the Glass-Steagall Act (banking separation act of 1933), banks could not offer comprehensive services, i.e. brokerage, investment banking and asset management were separated from commercial banking and lending. (This separation, however, was not applicable outside the U.S., which ex-

plains the swift integration once the separation was reversed by the end of the 1990s – since U.S. institutions had been offering all services akin to their peers, on a global scale, ex U.S.).

Because of the banking separation in the U.S., families and UHNWIs often had *teams* of independent advisors, financial planners, lawyers etc. Hence, law firms, financial planners – i.e. groups of specialist advisors were utilized. Often accountants were running the FO. As there were no banks offering comprehensive services, open architecture and outsourcing were quite common.

The sophistication of “investment offices”, “family services” and the institutionalization of clients led to the denomination – *instividuals*, as these families and UHNWIs often have the size and sophistication of institutions but often still have the qualities and behavior of individuals.

Philanthropy and charities have long been part of family offices and family-office services in the U.S. In Europe, many centuries-old families and family businesses are only just entering the transition from *family business* to *financial family*, i.e. family office, and learning to come to terms with the professionally run family offices. Besides the main forms as elaborated above and virtual family offices, there are several *family networks*, offering peers access to exclusive investment opportunities, “club deals”. The heterogeneity of family office models derives from that fact that no two families and their needs are the same, and despite having a mutual set of common needs, as a result, there is always the need for one or the other form, as families, like businesses, pass through different stages of the life-cycle.

Finally, a clear trend is also going in the direction of certain family offices “going private” again.

Dr. Steen Ehlerl is the author of “Global Private Wealth Management: An International Study on Private Wealth Management and Family Office Services for Ultra-High Net Worth Individuals”.

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