Family Office

Special Report

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For wealthy individuals and families, setting up a family office usually offers the benefits of professional advice, confidentiality and the ability to preserve wealth across generations.

This supplement explores these themes and others, from new EU laws that may curtail privacy and affect the choice of jurisdiction to investing in alternatives and the London property market.

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ALTERNATIVES

GUEST COMMENTARY BY MARTIN GRAHAM, ORACLE CAPITAL GROUP

Luxury Demand From Asia Boosting Alternatives Markets, Says Oracle's Graham

Martin Graham, chairman of Oracle Capital Group, says alternative investments have grown increasingly attractive since the global downturn, with wine and art in particular maintaining their appeal.

Since the financial crisis was first felt in 2007-08, we have seen a notable trend among our clients — and wealthy individuals more broadly — emerge: As traditional investment returns suffered, many have looked to alternative assets as a viable component of their investment portfolios.

Much has been written speculating on the virtues and pitfalls of investing in the "alternatives" market, a loose term which can include assets as diverse as cars, jewelry, watches, furniture, ceramics and rare spirits as well as art and wine.

While we always advise clients to keep a fully diversified portfolio, the majority of which will be in the more traditional instruments (equities, fixed income and so on), there are excellent investment opportunities far wider than these traditional asset classes that advisers may have pointed to historically.

The potential for more attractive returns is evident. There are any number of benchmarks which endeavour to track the 'alternatives' sector as a whole including The Coutts Index: Objects of Desire which in January this year reported a rise of 77 percent since 2005. And the wealthy are chasing these returns: a recent WealthInsight survey forecast that investment into 'luxury' asset classes is set to increase 10 percent between 2013 and 2017.

Broadly speaking, the outlook for both wine and art is strong. Unlike a luxury fashion house which can increase production of a popular iconic bag or scarf, there is a limited supply of masterpieces by a certain painter or bottle from a certain vineyard and vintage. The rapid emergence of great wealth in China and other Asian economies has also resulted in an exponential increase in demand for luxury products, boosting prices across a range of markets. Furthermore, the attraction of alternative assets is not limited to performance returns but can also extend to tax breaks if investors access the underlying asset through an Enterprise Investment Scheme (EIS) or similar structure.

It is therefore not surprising that, particularly in a low rate environment such as the one we have experienced for the past six to seven years, investors have looked beyond the boundaries of a traditional investment portfolio. There is also something to be said for the tangibility of assets such as art and cars; just as investors flock to gold in times of market turbulence, physical assets which you can view on your wall or in your garage can offer some psychological reassurance.

While alternatives can play an important part in a balanced portfolio; the secret is to invest in a sensible way. We strongly advise investors to never place more than 5 percent of their portfolio into alternative investments. By their very nature, they represent a higher risk investment where success is never guaranteed, and investors and their advisers must be extremely vigilant when assessing this risk.

It is also essential to seek the advice of a credible adviser who has a depth of knowledge and experience in their specialist sector. After all, these are unregulated and off-exchange markets, and forgeries across both the wine and art sectors are rife, sometimes hoodwinking successive generations who have believed themselves in possession of an invaluable family heirloom. James Butterwick, a world expert on Russian art and adviser to Oracle Capital Group, comments, "Always seek advice from auction houses and dealers — a little knowledge is a dangerous thing. A dealer acts as a filtering mechanism; experienced at buying and selling, they understand where the potential pitfalls are."

Investors must also accept that art and wine should be viewed as long-term investments. David Nathan-Maister, manager of the Oracle Paradis Wine Fund, warns that investors must expect to wait at least five years before they are likely to see a significant return in real terms. Butterwick adds that you must never rush into the sale of a painting, and timing your sale to the exact moment when the art is in high value can save you time and substantial costs.

A good way to spread risk is to invest through a fund. As when assessing an equity or fixed income fund, investors should also look carefully at historical performance and the managers' credentials.

Other factors to consider are transaction costs, which are usually higher than trading stocks and shares. It can also be difficult to track performance; after all, a painting is only worth what someone is willing to pay for it, and in the absence of an exchange, and a general lack of liquidity, this can be difficult to track. As such, many indices tracking an alternative asset class will be based on prices generated at auction and in private sales.

Art and wine, along with the other alternatives mentioned above, are often referred to as 'passion' investments because investors take a particular interest in, or feel a particular affinity with, the underlying asset. When it comes to assessing the investment case, however, passion should be sidelined in favour of a mindset that is detached, rational and in control; involving your wealth manager or adviser when considering investments of this type should help retain a position of neutrality. Finally, we always advise clients never to invest anything that they cannot afford to lose — but for the new generation of ultra wealthy, this can still be a significant amount.

Oracle Capital Group is a global independent multi-family office and wealth consultancy, providing comprehensive services for high net worth individuals, including investment advisory (through their offices in Switzerland and the Bahamas). Oracle Capital Group's in-house services include both an in-house wine fund, the Oracle Paradis Wine Fund, and an art advisory service.

SETTING UP

Considerations, Challenges of Starting a Family Office

Five advisers give their perspectives on how best to establish a family office.

RON GONG, MANAGING DIRECTOR AT CTC CONSULTING | HARRIS MYCFO, A PART OF **BMO FINANCIAL GROUP**:

1) Have the size and scale of wealth necessary to establish and sustain a single family office. Establishing a family office can be an expensive proposition, particularly if a family seeks to hire top professional and experienced talent. Be mindful of liquidity and wealth levels that can truly support a long term single family office. Understand and document your needs. The key is to compare the goals, objectives and related services the office will perform on behalf of the family to their associated costs, on both an in-house and outsource basis.

2) Do assess your family goals for the office. What services/role do you foresee the office performing? Investments? Tax planning? Some family offices offer everything from investment management, to family education as well as concierge services. Others may be strictly investment focused. The scope of services and role you intend on the family office providing will drive answers to how you structure and staff your office.

3) Do treat managing your family office just like a business. Managing wealth successfully, like managing a business, requires thoughtful planning, diligent research and the construction of a fully-integrated plan to coordinate all of the components of the process. Hiring and retaining core talent is essential for longevity.

4) Do your homework and take your time. Understand and make decisions based upon all the options available to you, from 100 percent in-house, to hybrid structures, to core-satellite or virtual family office structures. Consider seeking the advice of reputable family office associations.

5) Don't underestimate the amount of resources it takes to build a core family office capability. Consider the costs and capabilities of those tasks to be performed in-house versus outsourced. Many families underestimate the true scale and investment required to build-out core capabilities in-house to manage their portfolios, technology and reporting needs, conduct thorough investment research, stay abreast of capital markets and valuation levels, etc.

6) Don't try to do it all at once. As you build the family office, keep to your goals and take your time to hire experience professionals. Consider utilizing the depth of a multi-family office to complement your needs.

7) Don't ignore the ever-changing regulations. Understand the complex rules surrounding family offices, their structures, including the Dodd Frank family office registration rules and regulated investment rules.

> *Trying to build something that is all singing and dancing can quickly become an expensive undertaking.*
>
> *— Catherine Grum*

IAN SLACK AND **RICHARD JOYNT**, DIRECTORS OF **BEDELL FAMILY OFFICE**:

Firstly, it is critical that the client or head of the family defines precisely what the family office's roles and responsibilities are.

Secondly, the family need to find suitable professional staff to meet those roles and responsibilities — they may be existing trusted advisers or they may be suitably qualified family members. It will be important that the family tax and legal advice on how the family office should be set up as there may be regulatory issues in certain jurisdictions, and there will almost certainly be tax issues especially if the family office is managing and controlling some of the family companies.

CATHERINE GRUM, GROUP HEAD OF FAMILY OFFICE SERVICES AT **SALAMANCA GROUP**:

A good starting point is to take a step back and start to draw up some plans.

You can build a house brick by brick without advanced planning or the benefit of an architect for example but you risk making some costly mistakes and ending up with something that doesn't quite meet your needs.

Don't think that a family office has to cover every possible area of your life either — my advice would be to identify the core areas where you particularly need support or specialist expertise and consider outsourcing other areas. Trying to build something that is all singing and dancing can quickly become an expensive undertaking, especially as you may only need certain services infrequently or as a one-off.

Multi-family offices often provide a good compromise for families that need some help and assistance but cannot justify the expense of a dedicated full-service offering themselves. The key is to choose one that has a focus on building strong client relationships and seeks to get an understanding of your personal situation so that they can work with you effectively

The benefit of this approach is that you can leverage their wider knowledge, expertise and contacts to fill any gaps while making the most of the skills in your team.

Even a multi-family office will struggle to offer every possible service in house, at least without compromising somewhere or becoming internally conflicted.

CHARLES GOWLLAND, INVESTMENT MANAGEMENT PARTNER, AND **FRANK AKERS-DOUGLAS**, PRIVATE CLIENT TAX SERVICES PARTNER, AT **SMITH & WILLIAMSON HOLDINGS LIMITED**:

Be flexible. No two families are alike, and even within a family each generation and each individual will have different requirements. There is no one-size-fits-all solution. Secondly, encourage longevity in client relationships, preferably by retaining key advisers. Third, manage expectations within the family, so that each member understands their position in relation to the family's assets.

Don't try to fit a family to an off-the-shelf product or service. Don't let tax structures lead the family's investment decisions; rather, these should be driven by the overall strategic financial objectives agreed by the family. Last, don't be overly complex; the family should be able to understand their financial affairs.