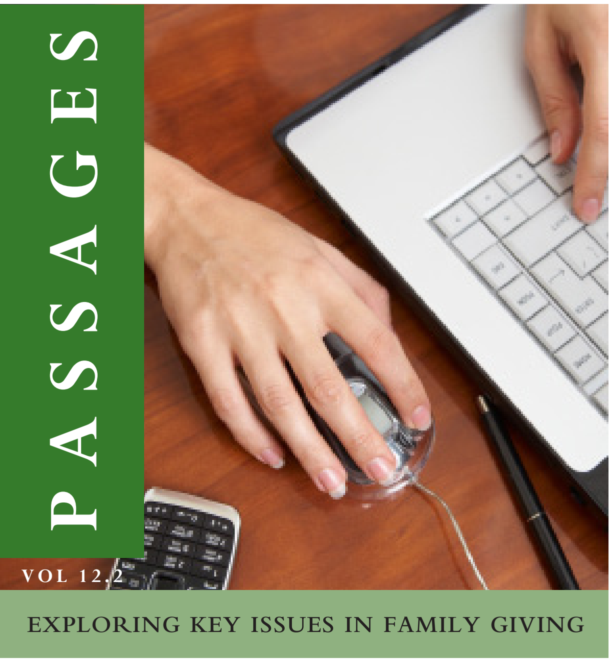
SPECIAL REPORT!
NATIONAL CENTER FOR FAMILY PHILANTHROPY

Working Together for Common Purpose: The First National Study of Family Philanthropy Through the Family Office



As the field of family philanthropy evolves, the options available to families for managing and making the most of their giving continue to keep pace. One option that a growing number of philanthropic families are considering is the creation of a single family office, a private entity that manages the investments and trusts for a single wealthy family—or multiple branches of a family—while also providing a variety of other personal services, among them philanthropic advising or the housing of a family foundation.

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NATIONAL CENTER
FAMILY PHILANTHROPY

This special *Passages* report is based on results of the first national study to explore the relationship between family offices and family philanthropy, identifying common themes for both success and failure. As a benchmark report for the field, the study draws on personal interviews and results from a survey of family offices to highlight emerging best practices by which family foundations and family offices can effectively work together to maximize the positive returns for the community and the family.

ORIGINS OF THE PROJECT

Over the past decade, the National Center for Family Philanthropy has closely followed the growing trend among very high net worth families of embedding their philanthropic giving within a family office. Both anecdotal evidence and an increasing number of reports and guides on the use of family offices led the National Center to join with the Threshold Group and the Family Office Exchange to create a collaborative research initiative designed to delve more deeply into the working relationship between family offices and family foundations. This report explores how family philanthropy is typically supported within a family office, as well as the potential pitfalls and opportunities of this approach.

Probing that relationship was done through a widely distributed survey document and personal interviews that asked questions about governance, management, planning, structure, and the real or perceived differences in family office and family foundation cultures.

It is clear from both the survey results and personal interviews that each family office is different from the next. However, through this study we were able to identify common themes for both success and failure. Examples of key takeaways from the study include:

- Philanthropy is taken seriously by the families and family offices. Family offices report a high degree of involvement in the family's philanthropy and foundation management by helping the foundation find a strategic focus, leverage the impact of its giving and the effectiveness of its grants.
- Managing a family's philanthropy through a family office works well for many families, and can be a particularly good choice when the family has multiple philanthropic entities or branches of the family. The decision for structuring the philanthropy through the family office should be aligned with the family's governance and long term plans to minimize challenges to this structure.
- Families and professionals should consider all family assets when structuring and governing.
- Families should think carefully about both who they hire to manage their family office and philanthropy, as well as how these individuals should interact with one another.
- Having a committee structure and term limits, as well as multiple family meetings per year, can create a platform for good governance to evolve.
- It is unlikely that families who don't get along in the usual course of things will suddenly get along when forced into a family office/foundation structure.

What also became apparent in interviews is the need to create a language that helps practitioners in family offices and family foundations each explain behavior that might seem foreign to the other. Additionally, there is the need for these practitioners to distinguish in their minds the very different roles of the private, public, and nonprofit sectors.

PROJECT PARTNERS, ADVISORY GROUP AND SCOPE OF WORK

The research effort was guided by an Advisory Group (see page 25) of individuals with experience in family offices and philanthropy to inform the process, review data and analysis, and provide critical context and perspective. National Center staff created the survey document, compiled survey results, and managed the

PROJECT PARTNERS

About the National Center for Family Philanthropy: www.ncfp.org

The National Center for Family Philanthropy is the only nonprofit resource center dedicated exclusively to families who give and those who work with them. The Center works to strengthen the field of family philanthropy and to support giving families through research, education, convenings and a national network.

About the Family Office Exchange: www.familyoffice.com

FOX is a global community of wealthy families and their advisors, pursuing best practices for optimal family legacy and wealth management. FOX is an objective, independent resource to help high net worth families, family office executives, and their advisors more effectively understand their responsibilities and enhance their opportunities as managers of family wealth and well being.

About Threshold Group: www.thresholdgroup.com

Threshold Group leads a select yet diverse group of families and family foundations through the opportunities and challenges of family wealth. Our services—financial planning, investment advisory and family office—provide the solid foundation necessary for a family to grow, thrive, and give back, not just for a lifetime, but for generations. Founded as a family office in 1999, Threshold today guides private family investments of $2.7 billion and serves more than 50 families and family foundations across the United States.

writing of this report. The Family Office Exchange (FOX) helped facilitate distribution of the survey to all of its single family office members and assisted in editing the report. Underwriting was provided by the Threshold Group. Each organization sees this new research as a valuable new source of information for its stakeholders.

The research broadly explored topics such as the advantages and disadvantages of embedding a family foundation in a family office, becoming part of a multi-family office, and questions of a "class divide" between staff members of family offices and family foundations.

Specific questions in the survey document included:

- How is the family foundation supported through the family office?
- How many generations does the family office serve?
- What is the number of family and/or non-family member employees working for the family foundation and the family office?
- What are the primary staff roles within the foundation?
- Who oversees the family's philanthropic initiatives?
- Approximately what percentage of the family office staff's time is spent supporting the family's philanthropic work?
- What are some of the common areas of conflict or concern?

According to FOX, the universe of single family offices in the United States is estimated to range from 3000 to 5000. FOX estimates that 95% of all family offices in its network support family foundations and/or other philanthropic activities of the family. The National Center and FOX sent surveys to approximately 400 family foundations connected to family offices. These offices, like the families they serve, come in all shapes and sizes, but the majority are single family offices serving just one family's interests. The survey response rate was approximately 10%.

The National Center then followed up with fifteen personal interviews with representatives of both the foundations and the business-side of selected family offices. In some cases, those who were good enough to give of their time were remarkably candid in their comments and requested one thing in return: anonymity. We have respected that request.

RECOMMENDATIONS FOR THE FIELD

The study results and interviews with practitioners and family office experts suggest a variety of key recommendations for the family office and family philanthropy fields, including:

1. **There should be a greater investment in professional development for family office staff on philanthropy issues.** Family office staff are often involved in a significant way in supporting the family's philanthropy, and providing them with more tools and training in this area can help to make philanthropy more effective both for the family and for the foundation's grantees.
2. **Families should set clear expectations and boundaries for both family office and family foundation staff.** There must be alignment among family members about the respective roles of these entities in order for the organization as a whole to function smoothly and effectively and to create an appropriate culture.
3. **There needs to be a common language of understanding between family foundation and family office staffs.** Families should be sure to recruit, train, and promote individuals who are able to learn and speak this language.
4. **Families and family offices need to invest more in educating and training the next generation for leadership.** "Next gen" education is high on most family's list of goals for the family office, but few families are able to carve out the amount of time needed to do this well. Because family offices are designed to work with multiple generations over many years, dedicating additional resources to this work is vital.

5. **Organizations that support family offices and philanthropy have a role in developing best practices for strong governance and effective communications across entities.** While there are well-established networks for family offices and family philanthropy, to date little research or training has been done to support families engaged in both types of entities.
6. **Families that manage their philanthropic foundations through a family office should pay special attention to the self-dealing laws and regulations, as well as to new SEC regulations governing this arrangement.** For a more thorough introduction to these issues, please see the special appendix to this report, "Legal Issues to Consider When a Family Office Provides Services to a Family Foundation."
7. **There are significant opportunities for family offices to support mission-related investing and capacity building approaches through the foundation, leveraging the expertise of their financial staff and expanding the impact of the philanthropic arm.** Based on the study results and other interviews with experts, it appears that mission-based investing is of increasing interest to newer family offices and philanthropic families.

Chart 1: Asset Size of Foundations in Sample

30% have assets over $50 million

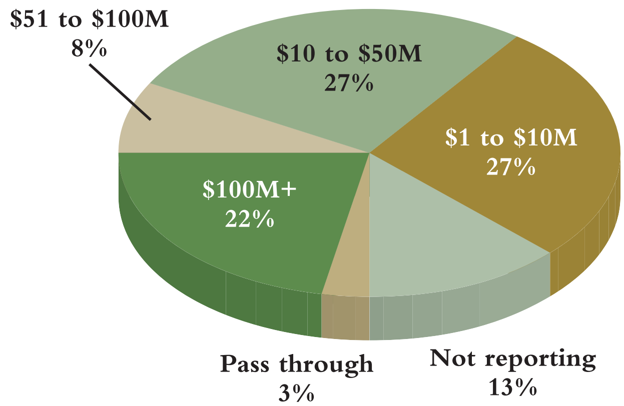
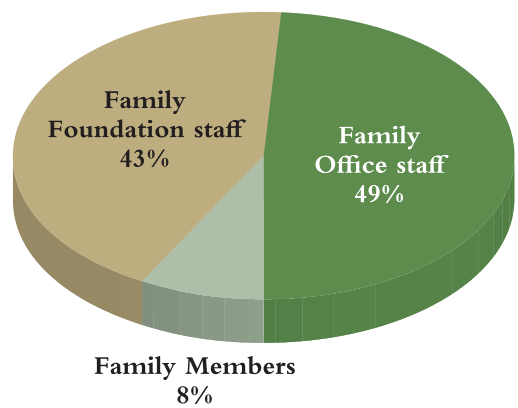


Chart 2: Role of Respondents



SNAPSHOT PROFILE OF SURVEY RESPONDENTS

This survey represents single family offices that house at least one foundation or other philanthropic entity: a full 98% of respondents work in single family offices; only 2% serve multiple family clients. In addition, 92% of respondents had at least one foundation as part of their office.

The collective assets of the foundations supported by the family offices tend to be under $50 million, with 27% of respondents reporting asset sizes between $1-10 million, and 27% ranging from $10-50 million. Only 22% of respondents noted assets of at least $100 million in the foundation. This is noteworthy given the multiple foundations served by these offices (see Chart 5 on page 8).

They are relatively young organizations, with the majority of family offices (78%) and family foundations (60%) formed since 1980. From 1900 to 1979, there were almost twice as many family foundations started as family offices within our sample; since 1980 family offices in the sample are outpacing family foundations in their growth rate.

The results provide insight into a variety of perspectives: 49% of respondents are in senior positions within the family office; 43% work for the foundation and 8% are family members.

The family offices in this sample are all based in the United States. While the field is rapidly expanding overseas, this survey targeted US-based offices.

AN INTRODUCTION TO THE FAMILY OFFICE

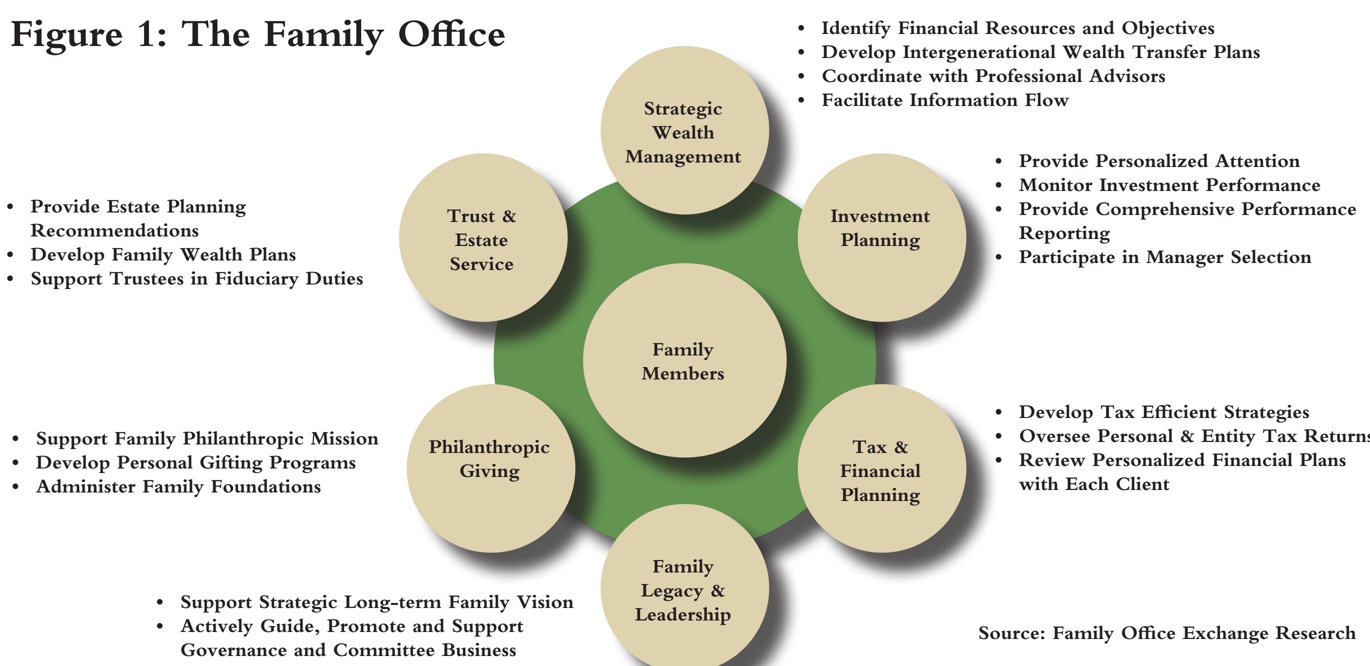
According to the Family Office Exchange, "The family office is a unique family business that is created to provide tailored wealth management solutions… in an integrated fashion while promoting and preserving the identity and values of the family. Some families start an office to provide economies of scale for the family by leveraging the investment buying power of the group; others want control over the process, and a dedicated staff; most are seeking a way to keep family members connected through the generations. All look to the family office to provide professional, private, and conflict-free management of their affairs to increase their chances of sustaining their human and financial capital for the long term."

As Figure 1 demonstrates, the family office can offer a wide range of integrated services, determined by the family's priorities. Families seeking increased scale sometimes make the decision to transition to a multi-family office (MFO), which seeks to provide comprehensive services developed for the founding family to additional families. *For more on the MFO option, please see the box on page 17. There is no one model for a family office, and one size does not fit all.*

THE HISTORY OF FAMILY OFFICES

To the general public, the family office is a relatively unknown institution, but the fact is that its roots are hundreds—if not thousands—of years old. For example, Vargas Partners can trace its history back 300 years. It works solely with billionaires, and some client relationships are more than a century old. The Medmenham Abbey can be traced to the 1700's and the Friars of St. Francis of Wycombe. Many Medmenham clients have genealogical links to European royalty. The Soloton Society claims a connection to the Poor Knights of Christ and the Temple of Solomon, predecessor of the Knights Templar. (*The Family Office: Advising the Financial Elite* by Russ Alan Prince, Hannah Shaw Grove, Keith Bloomfield, and Richard Flynn. Charter Financial Publishing 2010, page 19). The Rockefeller Family Office was created in 1882 and, in the intervening years, has moved from a single family office (SFO) to a multi-family office (MFO), to a full service asset management firm.

Figure 1: The Family Office



Source: Family Office Exchange Research

Similar to a family's philanthropic interests, the ideal family office structure and services reflect the mission and goals of the family. Following are the most common reasons families cite for starting a family office:

1. **Coordination:** The family office coordinates the multiple dimensions and relationships of a family including philanthropy, investing, estate planning, tax planning, custodial services, and banking, etc. Beyond these professional services, the family office can coordinate family governance, communication, education, and other support required to meet the family's mission and goals.
2. **Control:** Given the complexity inherent in managing the financial, philanthropic, and personal interests of a wealthy family, a family office can provide owners with control of the entire process and a single point of contact. It can offer the family and their advisors a centralized structure to make management decisions and ensure alignment of interests across all entities.
3. **Conflicts of Interest:** Family members may not always be aware of the embedded conflicts of interests that exist in relationships with product and service providers. The role of the family office is to ensure objective advice and alignment of interest with the family's goals and objectives. The family office professionals are relied upon to provide due diligence and should be required to provide full disclosure of any conflicts of interests.
4. **Confidentiality:** In a high tech world where privacy is a challenge, particularly to higher profile families, the family office can play a critical role in providing a secure environment for maintaining family records and personal information. The family office may also oversee personal security for family members.
5. **Customization:** The family office structure can provide a great level of flexibility and customization of services. As a family's interests evolve and generations expand, the family office's focus on the family's situation can enable it to evolve and grow with the family.

The family office structure can provide a great level of flexibility and customization of services. As a family's interests evolve and generations expand, the family office's focus on the family's situation can enable it to evolve and grow with the family.

According to FOX, a single family office should have at least a hundred million dollars in assets to be economical. In order for the office to remain viable, those assets must be nurtured and grown to keep pace with the growth of the family.

When Russ Alan Price conducted research for his 2010 book, he interviewed 903 family offices. Only forty percent of those offered philanthropic services to their clients. For others, philanthropy ranked beneath other lifestyle services such as family security, concierge services, and concierge healthcare.

Family Office Exchange believes one potential reason for this low percentage is that more than half of families with family offices elect to keep the philanthropic affairs in the hands of family members. They do not ask the family office for guidance or involvement, since the family enjoys being in charge of its philanthropy. FOX estimates that more than 90% of its 400 members have family foundations housed in their family offices, with many hosting two or more family foundations. Across the country and around the world, there are a growing number of family foundations supported by family offices, from both a strategic and an administrative standpoint.

STUDY FINDINGS: STRUCTURE AND SATISFACTION

This study provides a baseline for understanding family foundations within family offices. Key findings include:

Philanthropy is taken seriously by the families and the family offices. 84% of study participants have paid staff for the foundation and 60% have active boards of directors that oversee the foundation's giving, with 34% reporting that a foundation CEO serves as the primary decision-maker on giving. Only 5.7% reported that the family office CEO played this oversight role. Staffing at the foundations was also healthy: with 73% having a formal CEO, followed by grants/program officer (54%), administrator (46%) and finance/accounting staff (27%). The foundation staff also is engaged with philanthropic networks and associations, including the Council on Foundations (60%), the National Center for Family Philanthropy (57%), regional associations of grantmakers (43%), and the Association for Small Foundations (33%). Only 3% report currently being part of the Giving Pledge, spearheaded by Bill and Melinda Gates and Warren Buffett.

The majority of family offices are working with three or more generations, and families are often two or more generations removed from the founder(s). 100% of respondents are working with more than one generation, with 87% of family offices serving three or more generations. The largest population served by family offices in the study is the third generation, followed by the fourth and then second generations. Not surprisingly, for families serving the fourth (and beyond) generations of family

> *The majority of family offices are working with three or more generations, and families are often two or more generations removed from the founder(s).*

Chart 3: Primary Staff Roles at Foundations in Sample

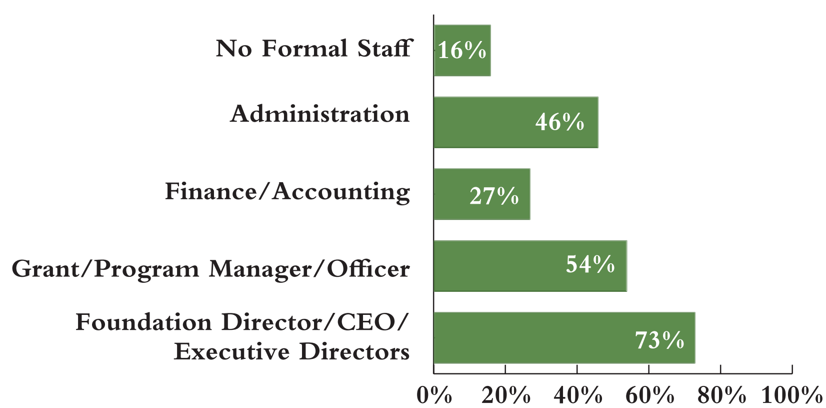
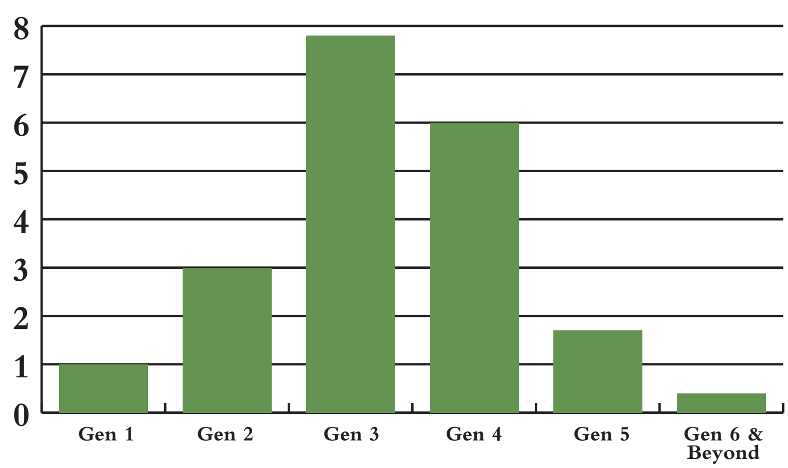


Chart 4: Average Number of Living Family Members Served by the Family Office Generation



members, the average number of family members served increases by nearly 300%, from an average of 10 to 28.

A growing number of family offices support multiple foundations, with more than one in five supporting three or more foundations. Nearly 40% of the family offices surveyed support more than one foundation, with 16% working with two different foundations, and 22% working with three or more foundations. For family offices that are 15 years or older, the percentage supporting more than one foundation increases to 44%. The diversity of individuals, interests and giving vehicles housed within family offices brings both challenges and opportunities for which family office professionals need to be prepared.

There is a range of satisfaction with the relationship between the entities. The majority of survey respondents reported a high degree of integration and cooperation. A full 81% said the family office and family foundation staff always have a cohesive working relationship, with another 13% saying it frequently meets this goal. Almost 77% of respondents said the foundation and family office are always aligned in servicing the family, with another 16% reporting that they frequently are. In addition, 55% of respondents said the two entities never have competing priorities with another 42% reporting that they only occasionally face this situation. Only 3% said competing priorities were frequently an issue and none reported it as always an issue. At the same time, our interviews revealed candid insights on the challenges associated with housing a family foundation within a family office, particularly from the foundation staff perspective.

Chart 5: Number of Family Foundations Served by the Family Office

More than two-fifths of family offices support more than one family foundation.

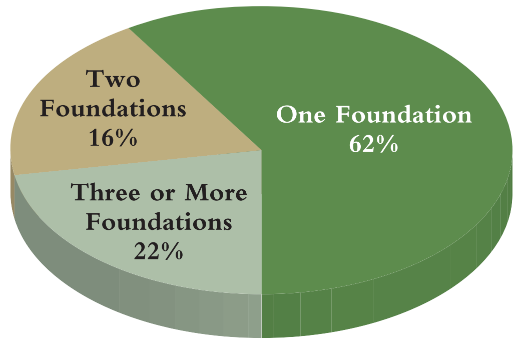
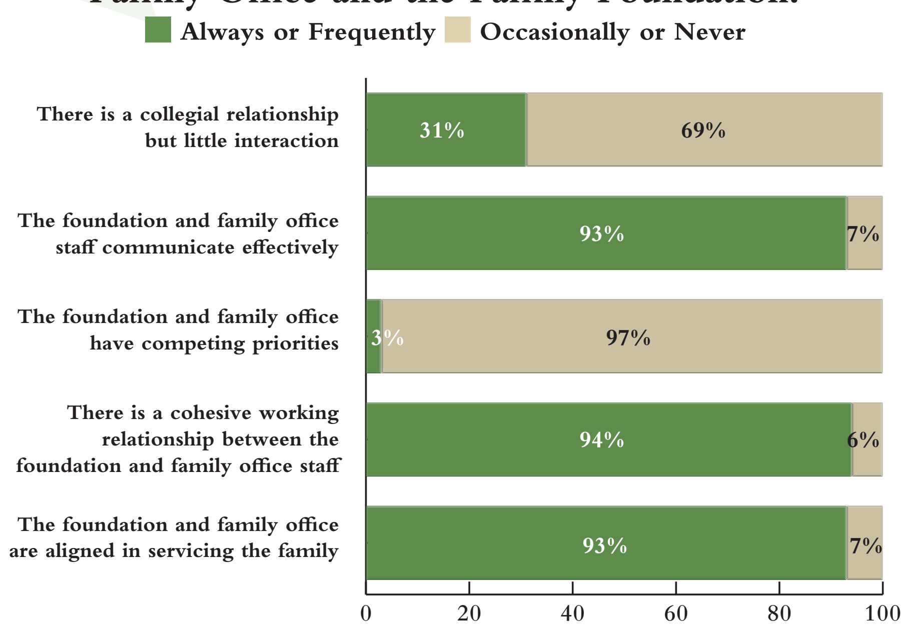


Chart 6: What is the Relationship Between the Family Office and the Family Foundation?



STUDY FINDINGS: ROLES AND BENEFITS

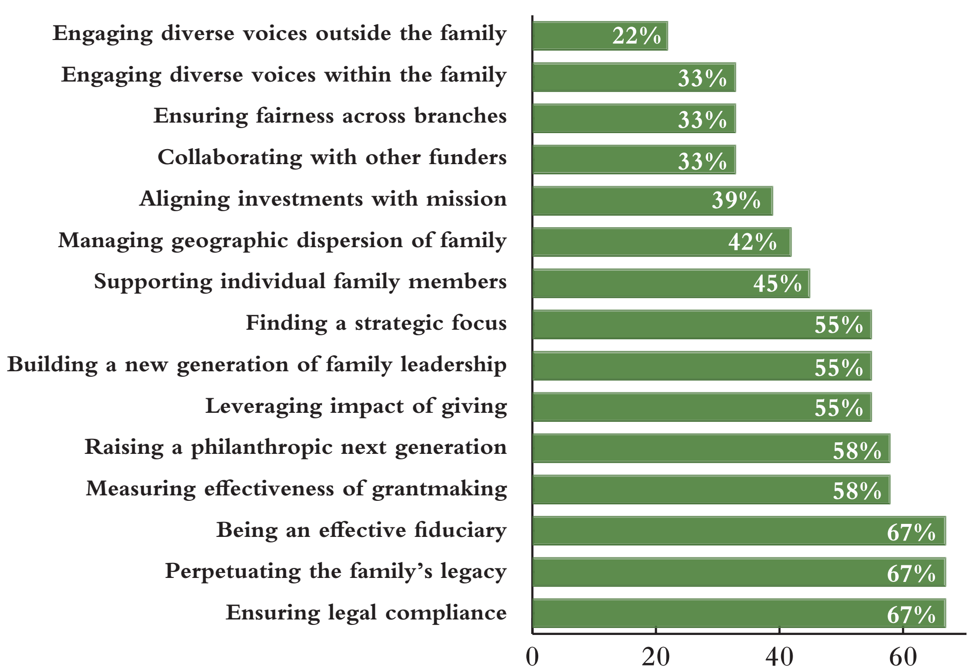
In addition to looking at the demographics of family foundations housed within family offices, this study also took a close look at the roles and benefits offered by this structure. Key findings include:

Family offices report a high degree of involvement in the family's philanthropy and foundation management. The majority of respondents noted that the family office is involved in helping the foundation find a strategic focus, leverage the impact of its giving, and measure the effectiveness of its grants. Looking at time spent by family office staff, after the financial and administrative duties, a large percentage of time was focused on grantmaking and philanthropic strategy, followed by governance support, and board and program meeting organization.

At the same time, the family office provides the type of financial and administrative services one would expect and these services are highly valued. Respondents noted that the largest amount of time that family office staff spend supporting the foundation was in the areas of investment management, foundation administration, and reporting and compliance. Specifically, they note that the family office supports the family's philanthropy by helping them serve as effective fiduciaries (67%) and ensuring legal compliance (67%).

> *Respondents noted that the largest amount of time that family office staff spend supporting the foundation was in the areas of investment management, foundation administration, and reporting and compliance.*

Chart 7: Common Services Provided by the Family Office

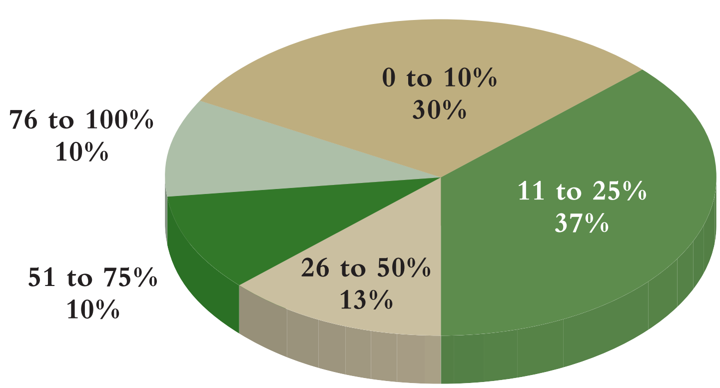


> *All parties place high priority on engaging and developing the next generation of family leaders, but neither side is spending much time in this area.*

Involvement does not always mean significant amounts of time. There are large variations in the amount of time that family offices spend supporting philanthropic activity and the foundation. At the high end, approximately 20% of family office staff spend at least 50% of their time supporting the foundation, with another 13% spending between 26-50% of their time. At the low end, 30% of the family offices are spending less than 10% of their time supporting the foundation and another 37% spend between 11-25% of their time. According to one respondent, "The family's philanthropy is not in any way managed through or by the family office. We handle the investments, compliance, and tax preparation for the foundations. What we do for the foundations could easily be outsourced. What the foundation staff does could never be outsourced."

All parties place high priority on engaging and developing the next generation of family leaders, but neither side is spending much time in this area. Surprisingly, family office staff report that they spend more time than the foundation staff on leadership development, mentoring, and family communication. A full 65% note that an important family goal is to develop philanthropic leadership among their children, grandchildren and great-grandchildren, and they are evenly divided on whose responsibility it is (39% says family office; 39% say family foundation). But looking at the time spent educating family members, including next generation leaders, family offices spent almost triple the amount of time (8.8%), than the staff of the foundation does (2.9%). Neither spends a significant amount of time on this activity. Mentoring is another area of philanthropic support where the family office is noted for playing the primary role (39%) vs. the foundation (26%).

Chart 8: Time Spent by Family Office Staff on Activities Related to Philanthropy



FAMILY OFFICE SPOTLIGHT:

The Frey Foundation: Working in Harmony with the Family Office

Year family office established: 1997

Year first foundation established: 1985

Number of foundations managed: 1

Approximate total philanthropic assets: $55 million

Number of staff in family office: 2

Number of staff dedicated to philanthropy: 2

Grantmaking focus area: Twin Cities (Minnesota) metro area and Naples, Florida

Grantmaking issue areas: Education, supportive affordable housing, and health and human services

In the late 1990s Jim Frey's father asked him to help set up a family office after he had sold his company.

Things started out relatively small, with Jim as president and his father as president and CEO. Additionally, there was a finance person and a general office person. A small family foundation was folded into the family office.

For a number of years, Jim ran both the family office and the family foundation, but found that family office operations were taking up most of his time. As a result, the foundation became somewhat moribund.

To address this, the family office CFO was promoted to president and CEO, and assumed primary responsibility for the office while Frey became president and CEO of the family foundation. His father remains chairman of the board. Staff has been added in finance, investment management, philanthropy, and administration. Even with these additions, the office is not a large one. There are four people working in the family office and 2.5 in the foundation.

"Locating a family foundation within a family office depends on the circumstances," Jim says. "Given our size, everyone does everything. Our family office CEO is exceptionally familiar with what's going on with the foundation. He knows the goals and the mission, and he works very closely with us to make sure the planning for the next few years is commensurate with the investment goals. So we're not dealing with two silos with very different interests. We have interim goals we've established and we check in regularly.

"I sit right next to the family office CEO, so we can't help but see each other every day. Formally, we have three foundation board meetings a year. The investment committee meets four times a year. So those are the more formal times when we can say these are the goals and this is where we want to be. We're a cohesive family and find we work together quite well across the generations. We don't have serious issues of diversity of opinion about where things ought to go. We regularly check in and say, 'These are the goals we have for the next several years.' We re-visit those with enough regularity and input that most board members feel it works well.

"If you have a family where that's not the case, it might be wise to segregate the two (FO and FF), but then you can lose economies of scale. That said, you can't manufacture family harmony if it's not there."

BENEFITS OF MANAGING PHILANTHROPY THROUGH THE FAMILY OFFICE

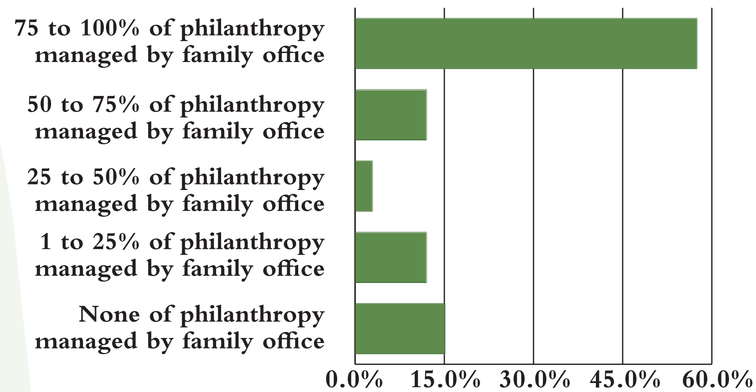
The decision to place a family foundation inside a family office often comes about for practical reasons. Families choosing this option typically seek to leverage the family office environment to better manage the family's philanthropy and to achieve the overall goals of the family. A key benefit for families is the centralization and efficiency that the family office provides: **58% report that 75% of the family's philanthropy is managed through the office, with another 12% noting that at between 50 and 75% of the philanthropy is centralized**. This coordinated approach is evident even when multiple vehicles are used, as is the case with the majority of family offices participating in the survey.

Many families have also discovered that there are economies of scale to be realized by cohabitation. In our survey sample, family foundations housed in family offices often took advantage of the resources a full service family office provides, including support they might not have access to in a different structure. These included such things as investment management and oversight, bookkeeping, tax preparation, legal compliance, technology support, board meeting facilitation, human resources expertise, office space, and access to retirement plans and health benefits.

"The family office working in concert with the family can be a very smart and strategic relationship particularly if it partners with other advisors when needed, to serve the family's best interests," says Betsy Brill, founder and president of Strategic Philanthropy, Ltd. "The family office team has only the family in mind which can be invaluable for some families who need or want that focus."

A broad set of distinct advantages for enhancing the family's philanthropy through a family office structure were cited by respondents to the survey:

Chart 9: Percentage of Family's Philanthropy Managed Through the Family Office



- *Integration:* Integrates a variety of key functions, including investment management, administration, tax strategy, tax compliance, governance, and charitable giving; provides a more complete picture of the family's wealth and "investments."

- *Alignment:* Allows the foundation staff to have a clear understanding of the family as a whole, beyond their giving, enabling the foundation to be aligned with the values of the family regarding family governance, financial management, long-term investment strategies, and family leadership development.

- *Enhancement:* The investment advisory services offered by the family office can be leveraged to support mission-related investment activity by the foundation.

- *Economies of Scale:* The foundation and the family receive more services at a lower cost than if each operated independently. Similarly, the family office can support multiple giving vehicles for the family's philanthropy as well as multiple foundations.

- *Efficiency:* Provides greater efficiency for family members and external vendors.

- *Communication:* Provides one point of contact for family members and simplifies communication channels.

- *Culture and Synergy:* The family office creates a sense of fun and energy by mixing different professional skills in a small office. This helps to build pride and active involvement in the community and beyond.
- *Next Gen Education:* Family offices can provide enhanced learning opportunities for younger generations in financial literacy, socially responsive investing, family communication, and mentoring/leadership development experiences.

CREATING SYNERGY BETWEEN THE FAMILY FOUNDATION AND THE FAMILY OFFICE

By Sara Hamilton

Effective family office executives can develop a strategic partnership with wealth owners or foundation directors that, in its best form, can greatly enhance the value of the foundation. Working together to identify and align goals to ensure both wealth distribution and wealth preservation is a goal worth striving for. The talents and efficiencies of family office staff members can make family foundations more effective in their vision, their grantmaking, and their impact assessment. It is the synergies between the teams of managers that can really energize a family foundation that is properly supported by a family office.

Family offices that effectively support family foundations are known for having the following characteristics:

- *Understanding Donor Intent:* Family office staff often make great historians, and they are able to review historical records that interject original donor wishes, especially if they knew the original donor. They are able to help clarify concepts when there is a lack of agreement among different family factions.
- *Supporting the Foundation's Visions:* Helping the family bring the foundation vision to life is one of the contributions that family office staff can make. Staff members are typically good process people, and they are able to map out the steps needed to go from A to Z on a project or a process. They can help define/clarify a common vision, and help build consensus among various family constituent groups.
- *Mentoring Foundation Board Members:* Family office staff are natural mentors of younger family members who are learning to become foundation leaders. They have the training and the skills needed to identify future talent potential, and if given encouragement in this area, can support family members responsible for identifying and growing future leaders.
- *Ensuring Philanthropic Impact:* One of the natural skills of family office professionals is to hold groups accountable for their performance on behalf of the family, and they can provide the follow-up needed to document performance and help measure the impact of the grants made.
- *Providing Time Saving Administrative Services:* Because family members often have busy and evolving schedules, knowing when to delegate to the office staff is key to ensuring that projects move forward in a timely fashion.

All of these support services are best provided in conjunction with family members who serve as leaders of the foundation. Building strong teams of owners and managers makes the most sense and has the greatest impact on the foundation's effectiveness.

Sara Hamilton is the founder and CEO of Family Office Exchange, based in Chicago.

CHALLENGES OF MANAGING PHILANTHROPY THROUGH THE FAMILY OFFICE

In many of the interviews conducted for this report, it was noted that a natural tension exists between the family office and the family foundation. This should not come as a surprise: typically, these two family entities have two very different goals. One exists to preserve capital and make money. The other gives money away. This tension can become more pronounced when the office is managing one or more family businesses, and the funds for philanthropy come from those businesses.

There are also very different matrices for measuring success. To say to an investment manager, who measures success based on concrete performance, that the philanthropy aims to do good in society can be perceived as a little soft. This is where the development of a common language, as well as mutual respect and understanding, can be critical to the integrated functioning of the two entities.

Bruce Maza, executive director of the C.E. & S. Foundation, describes these as "conversations of the heart and soul." He observes:

> *"Philanthropic professionals play a values-centered role in the family office. Members of a donor family rarely have conversations with accountants or investment managers about the moral passions that drive their family's philanthropy. Nuts and bolts about numbers are objective. But, donors talk with their philanthropic professionals about the subjective issues in the grantmaking process, their emotional engagements both with the leaders of those nonprofits whom they fund and with fellow trustees when they are striving to reach consensus on the moral use of philanthropic resources. These matters carry emotional complexity. Therefore, inside a family office there is an 'otherness' that distinguishes philanthropic professionals from financial managers."*

We also heard stories in our interviews about the sad consequences of haphazard decision making, blurred boundaries, unfortunate family dynamics being played out among staff, and the practical results of the natural tension between family office and family foundation goals. Interviewees who expressed the view that the foundation should be separate from the family office had opinions that ranged from dispassionately business-like to highly charged, probably as a result of personal experiences.

REFLECTIONS: OVERCOMING THE WE/THEY MENTALITY

"The original family office executive had read all the literature and believed that everything had to be absolutely separate. He carried that to an extreme—even down to reams of paper. So there was a real we/they mentality when I arrived. I had to work really hard to build my credibility with the family office side."

—*Family Foundation Director*

At the same time, some long-time observers of the family office field pointed towards the real opportunities that arise when advice is available from a variety of perspectives. Patricia Angus, founder and CEO of Angus Advisory Group, notes:

> *"It's important to recognize that parallel conversations can occur in larger family offices. While doing estate and financial planning for family members, family office professionals often touch on the most intimate aspects of their client's lives. Other professionals in the same office may be working on philanthropy and grantmaking that also touch on issues of meaning and purpose, but the connection may not be made between the two. There is a real opportunity to link these two conversations for greater impact on both sides of the equation."*

Regardless, based on the interviews conducted for this study, it appears that there is a natural tendency for one organization to want the upper hand over the other, particularly if family leadership is ineffective or unclear. It is impossible to manufacture family harmony if it doesn't exist, and those dynamics can easily cast a shadow over the family office environment.

When a family decides to combine the family office and the family foundation without careful planning, they are setting a course fraught with challenges. There must be alignment at the top in order for the organizations to function smoothly and efficiently and to create the appropriate culture.

In addition to this overarching issue, specific comments on challenges cited by respondents to our survey included:

- Competing interests and priorities
- Lack of respect for philanthropic goals and endeavors
- Competition for the attention of family members
- Cost and inefficiency
- The complicated and counter-intuitive restrictions the IRS imposes on interactions because of the affiliation
- Issues created by separate management structures
- Impact on family office staff time
- A "them/us" mentality
- Emotional ties that can conflict with best practices

When a family decides to combine the family office and the family foundation without careful planning, they are setting a course fraught with challenges. There must be alignment at the top in order for the organizations to function smoothly and efficiently and to create the appropriate culture.

Unless boundaries are very clear and respected by the family, the foundation staff can find themselves pulled between the two.

"I wear both hats in a full service family office. It can be somewhat schizophrenic. One minute we're reviewing grant proposals and the next we're asked to make sure the plane is gassed and ready to go. This is not to imply that one task is more important than the other, but it does point to the need to have very clearly defined roles that everyone understands and respects," said one family foundation/office director.

On the other hand, if approached with a clear sense of roles and boundaries, the relationship can be synergistic. Richard Woo, chief executive officer of The Russell Family Foundation, reports that upon the sale in 1999 of the Frank Russell Company, a global investment services firm, the Russell family set out to create "two separate but equal enterprises that are driven by similar values." Woo and his counterpart at the family office both report to separate, independent boards, although there is some overlap in family membership on the boards. "There are benefits to this approach as well as challenges," says Woo, "but we are absolutely viewed as peers within the constellation of family enterprises."

OPTIONS FOR MANAGING FAMILY PHILANTHROPY THROUGH THE FAMILY OFFICE

Attitudes toward wealth differ widely, and style preferences, management, and governance are shaped by those attitudes. For some there is little desire to create a legacy or dynasty. For others, wealth is viewed as a way to bring the family together utilizing governance, asset management, the foundation, wealth building, and continuation of the family business in whatever form. In some cases, philanthropy may be the "glue" for the family.

There are a number of giving vehicles through which family philanthropy in the family office is practiced. In increasing order of use, our survey respondents listed giving circles (3%), corporate foundations/giving (8%), operating foundations (11.4%), supporting organizations (16%), community foundations (24%), donor advised funds (32%), direct gifts to charities (62%), and private foundations (92%) among the many options their families chose. The vast majority of (86%) of respondents indicated that they used the family office to manage more than one of these options for their philanthropy.

The survey results also revealed limited interest in mission-related investing, although its popularity is growing among newer foundations. Only 19% of respondents ranked mission investing as "very important," with 33% saying it was "not important" at all, and the remainder evenly divided. But looking at those foundations started since 1980, the interest grows significantly, with almost 47% of these respondents ranking mission-related investing as important or very important, and only 24% of the newer foundations ranking it as not important.

Chart 10: Giving Vehicles Used by Respondents

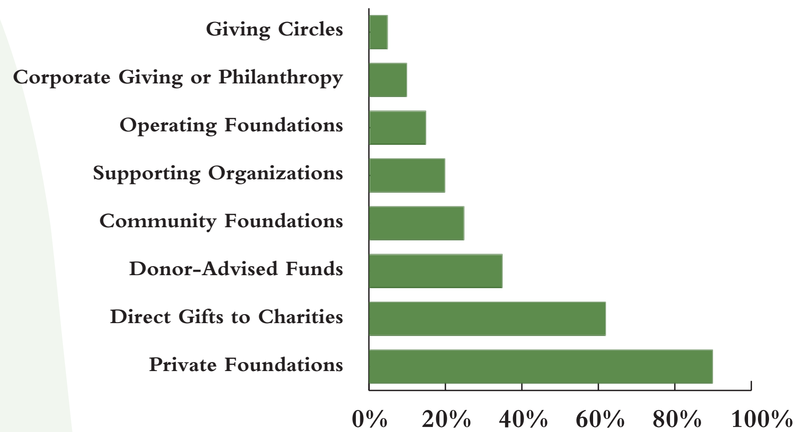
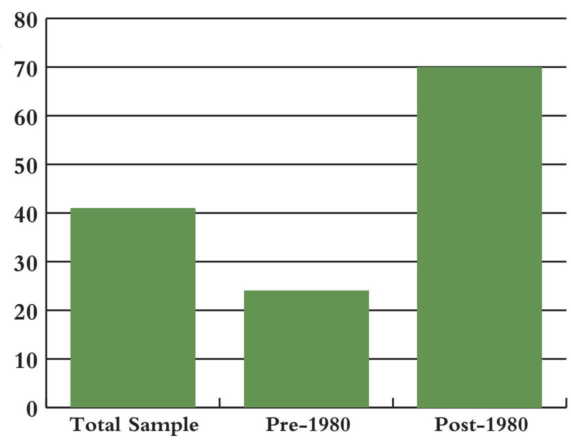


Chart 11: Percentage of Respondents Ranking Mission Investing as "Important" or "Very Important" by Year Family Office Established



ADVANTAGES OF THE FAMILY OFFICE SURVEY RESPONSES:

- The family office "provides a deep and diverse set of readily available resources that we would otherwise be unable to afford. It can be a very efficient and cost effective way to run a foundation."
- "We work together for the complete fulfillment of trustees. The investment services divisions maximize the family portfolio while philanthropy allows individual families to pursue personal passions and interests. We maximize the expertise of investment, accounting and tax preparation, so the foundation staff is fully focused on supporting the family in giving."

A NOTE ON MULTI-FAMILY OFFICES

Families and individual private investors may decide not to set up their own family office because they do not want to be responsible for managing a financial services business. Or, they may prefer the continuity offered by an established institution where they can evaluate the quality of financial services before they choose to become a client.

Individuals and families with assets greater than $20 million may be best served by a multi-family office (MFO) or a financial institution with a dedicated wealth management specialization. Multi-family offices have historically provided high net worth families with comprehensive financial services and confidentiality not available from larger, product-driven financial institutions. Participating families have access to a wide array of integrated services that are not collectively offered anywhere else.

While multi-family offices are increasingly popular, the majority of the single family offices participating in this study did not indicate an interest in this option. A full 77% reported that they have never considered becoming a multi-family office, either through expansion or merger, with another 14% saying they considered it but decided against it. However, there are some alternatives in the marketplace that offer similar services, along with varying levels of access to philanthropic support staff. The key is finding the right fit.

Family Office Exchange suggests a number of value-added supports that multi-family offices can provide, including:

- Financial "quarterback" supported by specialists in each field
- Teams of qualified professionals who can collaborate
- Continuity of service if current MFO contact leaves
- Experience in managing generational transitions
- Strong risk management policies and procedures
- Comprehensive information systems
- Relationship pricing for inter-disciplinary services
- A tactical, values-based approach to investing, transaction planning and philanthropy

Advisors familiar with both the single family office and the MFO approach say that the two options can be equally diverse or insular depending on the structure and generational wealth issues. One advisor noted that "the term 'MFO' is used inconsistently and families should first understand the services they seek and use that to assess an institution." "The advantages or disadvantages relate to a multiple sets of values, styles, and shares of wealth and culture," says Diane Neimann of Family Philanthropy Advisors. "Philanthropy can be well managed in either setting if there is a convergence of higher standards, time devoted, and good governance and management. It all depends on the commitment and quality of the people involved."

For families interested in additional information on the multi-family office option, a special addendum to this report will be available in December 2012.

FAMILY OFFICE SPOTLIGHT:

The Weaver Foundation: Active Communications, Practical Advantages

Year family office established: Services have been provided for many years

Year first foundation established: 1967

Number of foundations managed: 1

Approximate total philanthropic assets: $22.5 million

Number of staff in family office: None formally. 2 in foundation; 6 in business entity; shared reception with an affiliate company

Number of staff dedicated to philanthropy: 2

Grantmaking focus area: Limited to greater Greensboro, NC area

Grantmaking issue areas: Broad areas of interest

Herman and Edith Weaver started W. H. Weaver Construction Company in 1939. During the early years, the company specialized in residential construction. Weaver Realty Company, a real estate management and mortgage banking firm, was started in 1946, and, in the early 1950's, the Weaver Construction Company diversified into commercial and industrial construction. By the 1960's the companies had grown and expanded with operations in six southeastern states.

The Weaver's son, H. Michael Weaver, joined the family businesses in the fall of 1961 and later expanded the companies into real estate development, investment, brokerage, and syndication. The primary company now is the Weaver Investment Company, which owns and manages commercial office and apartment buildings, and other business concerns and ventures.

The Weaver organization is a three-part entity that includes the Weaver Investment Company and its affiliated companies, the Weaver Foundation, and a family office that manages the equity and fixed income portfolios for Weaver family members and provides a variety of support services. All three components are housed together.

Herman and Mike Weaver founded The Weaver Foundation in 1967 as a way to support activities and causes that benefit the greater Greensboro area. Richard (Skip) Moore is the president and CEO of the Foundation, and one of three vice presidents at Weaver Investment.

The company, family office services, and the family foundation are well integrated. While the foundation's investment portfolio is managed by an Investment Committee appointed by the foundation board, company staff provide the typical back office functions like bill paying, accounting, and HR administration. The company president is a member of the Investment Committee and the CFO of the business is the treasurer of the foundation.

"Our offices are hosted within the company facilities and the staff handles our accounting, reception, and telephone," says Skip Moore, president of the foundation. "But it would never occur to me to say that the family office pays for us."

"We have two top non-family executives," says Moore. "The president and CEO of Weaver Investments and me. As far as family office functions, we're both involved. We both deal with family relations. For example, I plan the annual family retreats. Lee handles investments and real estate and family business services. But I report to the foundation board and they approve the giving budget."

continued on page 19

THE ROLE OF THE FAMILY OFFICE VS. THE FAMILY FOUNDATION

As noted earlier, the survey identified a number of roles for each entity that were anticipated: the family offices reported spending significant time on investment management, foundation administration, and reporting and compliance. In turn, foundation staff are primarily focused on grantmaking (71%), followed by philanthropic strategy (35%), foundation administration (32%), and governance (9%).

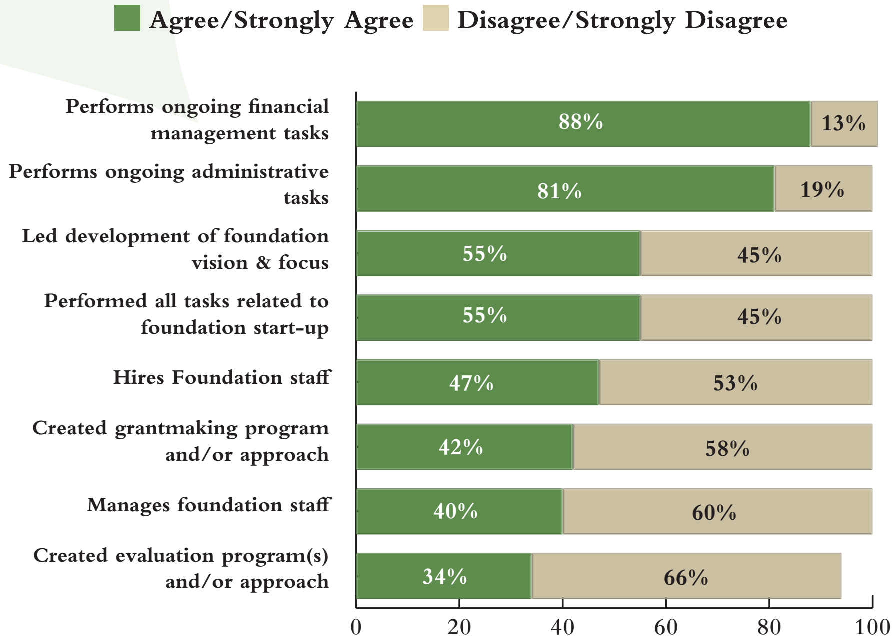
But a significant percentage of family offices reported a high degree of involvement with the family's philanthropy, from the early days of finding a strategic focus to all phases of foundation start-up and ongoing management and evaluation. A full 55% of survey respondents said the family office performed all the tasks related to foundation start-up, with an equal percentage saying the family office led the development of the foundation's vision and focus. In addition, 42% said the family office created the grantmaking program or approach, 47% noted they hired the foundation staff, and 34% said they created the evaluation program or approach.

The high level of involvement by the family office in shaping the direction and implementation of the family's philanthropy has multiple ramifications—from staffing and professional development to community engagement and representation.

"Those with whom we partner in the mission of the family foundation need to feel that they are going to interact with the representatives of a philanthropic institution, not merely with some kind of financial function within a mysterious and wealthy family office," said one foundation director.

"My experience is that having the family foundation located inside the family office can have unexpected consequences," said one west coast

Chart 12: Role of the Family Office in the Development and Management of the Foundation



The Weaver Foundation, continued from page 18

There are also practical advantages to having the small staff of the family foundation folded into the larger family business/office structure. "I'm employed jointly by the foundation and the company which involves me with the other staff more fully and also supports benefits such as health care and retirement."

Active communication is one of the keys to maintaining a smooth relationship between the family foundation and the business entities. "I send out a monthly newsletter to the Board and to all family members and the Investment Committee, which is composed of external individuals. It also goes to staff and top management at affiliate companies," says Moore, "so they all know what's going on with the foundation. It is important for everyone to feel a part of the philanthropic activity as what we do extends the Weaver name throughout the community."

family office director. "Most people who don't work in the family office universe have no idea what they are or what they do. If a non-profit executive comes in to the family office, it's immediately apparent through something as simple as the office décor or the art on the walls that there are significant resources. In very subtle ways, a playing field and a power structure that is already inherently uneven becomes more so. Under those circumstances, it's very difficult for the foundation representative to maintain the idea that the foundation and the nonprofit are equal partners."

THE FAMILY COUNCIL: OVERSEER AND CATALYST

By Patricia M. Angus

Many families with a single family office may also elect to set up a Family Council. While the particular roles and responsibilities of Family Councils vary across families, they typically function as an oversight committee that consists of a small group of family members elected or selected out of the larger family. For example, in a family with five branches totaling more than 100 members, the Family Council might include a representative of each branch, along with one or more members chosen by the group at large. In a small family, the Family Council might consist of all adult family members (with "adult" defined by the family itself).

Family Councils can serve an important role for a family when their philanthropy is supported by a Family Office. The Family Council may be assigned responsibility for leading the process of discovering and articulating the family's goals and the principles that guide the family's work together. As an oversight body, the Family Council may work to ensure that the Family Office supports activities that enhance the positive development of individual family members, and can help ensure that family members do not become adversely dependent on family resources. On the philanthropy front, the Family Council can serve as a catalyst for an exploration of the family's values and vision, which can then be implemented through the family's philanthropy.

While the Family Office is tasked with the day-to-day responsibility of supporting the family's needs, the Family Council has the privilege (and burden) of focusing on long-term objectives and the unique challenges of implementing the family's mission and vision. In some families, members of the Family Council may also serve on the Board of Directors of the Family Office, which requires those individuals to carefully distinguish between the two roles. The Board of Directors serve in a legal capacity, with all that entails, while the Family Council is generally more akin to an advisory board. Ideally, the Family Council's lack of legal authority should not diminish the Council's potential for influence and impact in the family. For example, if the Family Council sees that there is a disconnect between the family's philanthropy and the values of individual family members, or the family as a whole, it can initiate an exploration of whether and how greater alignment might be achieved.

In all cases, despite the unique characteristics of a particular family's Family Council, it must function as a "live" entity comprised of family members who are actively engaged in guiding family activities in a way that is informed by—and responsive to—the larger family's principles and goals.

Patricia Angus is the founder and CEO of Angus Advisory Group (www.angusadvisorygroup.com).

GETTING IT RIGHT: BEST PRACTICES FOR THE FAMILY OFFICE AND FAMILY FOUNDATION RELATIONSHIP

Perhaps the most significant contribution this study can make to the field is to identify practices that can help family offices and family foundations build successful relationships. Through the survey and personal interviews, it is clear that the keys to success are a strong and healthy family structure, family knowledge and understanding of shared goals, and the recognition of very clear boundaries and reporting relationships among staff.

Clarity of Goals

The family offices and family foundations participating in this survey were most successful when they both shared a commitment to the common purpose they served: the goals of the family. The majority cited the importance that families place on leveraging the impact of their giving as the most significant goal, followed by being effective fiduciaries, finding a strategic focus, and ensuring legal compliance. Moderately ranked family goals included raising a philanthropic next generation, perpetuating the family's legacy, and building a new generation of family leadership. Lower on the list but still important? Engaging diverse voices outside of the family, ensuring fairness across the family branches, and managing the geographic dispersion of the family.

> **Best Practices: Clarity of Goals**
>
> "If the family values philanthropy, then the foundation and the office are a whole. A smart executive in the office will bring both sides of the office together so there is mutual respect, understanding and involvement. He or she will make sure there is cross participation to some degree in board meetings of both. Also it helps if the foundation people have a thorough understanding of the business goals and vice versa. Family members can give a strong message about this as well, and the best of them do."
>
> —*Diane Neimann, Founder, Family Philanthropy Advisors*

Effective Leveraging of Strengths

Foundations that utilize the investment management and financial expertise of a family office can expand their impact beyond grantmaking, through mission-related investing and combining complementary skillsets between the non-profit foundation and the commercial family enterprise. The Russell Family Foundation has developed a reputation for mission-related investing since it first began exploring that field nearly a decade ago. "The Russell Family was very interested in this hybrid approach. In turn, The Russell Family Foundation staff had to work hard to coax and cultivate these types of services from the family office," notes Richard Woo, CEO of the foundation. "It required us to develop a very close working relationship and agree on values and measurements of progress against non-traditional goals. Early on, the Foundation made a mission-related investment that failed. We hired an external consultant to do a post-mortem and the end result is that we now have a joint committee with representatives from both the foundation and the family office that reviews every mission-related investment opportunity. It's a model that has benefited the work and serves as an example to other clients of the family office."

Regular, Structured Communication

Communication is at the center of a wheel with many spokes. In interviews, it was made clear that the family needs to communicate with each other and with staff, the family office and foundation staff needs to communicate with the family and with each other and, ultimately, the foundation staff has to communicate with the community.

"We're a very cohesive family and work quite well together across generations. When we have issues of diversity of opinion we usually find a way to accommodate those differences. We regularly check in and re-visit our goals with enough regularity and input that most board members feel it works well," said Jim Frey of the Frey Foundation of Minnesota.

The family offices participating in the survey that reported strong satisfaction almost always noted communication as a key factor. More than 93%

reported that staff always or frequently communicates effectively; only 3% noted occasional problems and another 3% cited ongoing issues.

"I was brought in to build the family office, using the FOX Family Office Blueprint™. I was told to set up a family office, and that I was to oversee everything," one family office director remembered. "It's not entirely clear to me that the family ever told the family foundation director what was going on. There was internal conflict from the beginning. My ultimate takeaway was that the family didn't communicate clearly. They didn't bring everybody together, and they weren't willing to deal with the resulting conflict."

Best Practices: Communications

"We created what we call the Dashboard. It's an electronic newsletter sent out every two and a half months or so. It's an update on activities, identifies trends, mentions a milestone we've hit along the way that the family should know about and celebrate—that kind of thing."

—*Marcie Skelton, Walker Foundation*

"I send a monthly newsletter to the Board and family members that includes information about Foundation staff activities as well as grantee updates and community activities. It is also sent to the top management and staff of the affiliate companies. As a family-related activity, it is important that everyone feel a part of the Foundation's work."

—*Richard Moore, Weaver Foundation*

Integration

Another key to success is the careful integration of every family asset when setting up the family office. In this scenario, an already existing family foundation is recognized as an asset that expresses the family's values and interests. A smart family office CEO will understand that the family foundation can enhance operations by providing a vehicle for bringing generations of the family together around a common purpose that has little or nothing to do with the preservation or inheritance of money.

Diane Neimann, who has worked with dozens of family offices and family foundations during the course of her career says, "The well-integrated office is the ideal, and one which considers all the assets of the family when structuring and governing. The foundation is then viewed as an asset that expresses the family's values and can often help to transmit history, educational interests, and perspective on investment and governance. For some, it is a training ground. For others, it is a life's work. And for many, it is a focal point for family meetings, long-range planning and generational transition. In a family office which has achieved full integration, both staff and family are well informed about the business and philanthropic work of the office."

Clear Reporting Relationships and Governance

Ultimately, the family is in charge, and there must be agreement between family leadership about the plan they develop for either creating the family office, or bringing their foundation into that environment. Alignment at the top is the first crucial step in the process. If the family is in disagreement, those conflicts and misunderstandings can seep into staff relationships.

Almost every interviewee talked about the importance of clear reporting relationships. Most family office directors believe that family foundation directors should report to them rather than directly to the family.

"If the asset base is not sufficient to be separate, then both entities should be under one roof. But there must be a clear chain of command. My bias would be to have the family foundation director report to the family office director who reports to the family," said one family office director.

Added another: "If the family office is formed and then hires the family foundation director, there should be only one silo—one chain of command. It works well. There's no doubt that the family foundation director reports to the family office director.

FAMILY OFFICE SPOTLIGHT:
The Meyerhoff Funds: Bridging Geographic Boundaries for Shared Impact

Year family office established: 1980

Year first foundation established: 1964

Number of foundations managed: 6

Approximate total philanthropic assets: N/A

Number of staff in family office: 4 full-time, 1 part-time

Number of staff dedicated to philanthropy: 2 full-time, 2 part-time

Grantmaking focus area: Baltimore and Israel

Grantmaking issue areas: Middle class issues, Jewish issues

The Joseph and Harvey Meyerhoff Family Charitable Funds are a group of Baltimore-based family foundations whose philanthropic contributions have had significant impact not only on the city of Baltimore, but nationally and internationally as well.

Joseph Meyerhoff, a premier Baltimore businessman, philanthropist, and fundraiser, began the tradition of giving in his family that continues to be a legacy today through his children, grandchildren, and great grandchildren. Among other activities, Meyerhoff is most well known for his leadership of the Baltimore Symphony Orchestra and his work in the creation of the state of Israel.

Joseph's son, Harvey M. "Bud" Meyerhoff, was instrumental in the building of the United States Holocaust Memorial Museum in Washington, D.C. and the Funds' gift still remains among the largest gifts to the Museum. Bud Meyerhoff is also a long standing supporter of the Johns Hopkins University, Johns Hopkins Hospital, and the Johns Hopkins Health System, where he was chairman of the board and currently serves as a trustee emeritus.

Bud Meyerhoff's children and grandchildren serve as trustees on several family foundation boards and are active in their communities. His sister, Eleanor Meyerhoff Katz, and her children are all actively involved in family foundations, as well as in their own communities. For 14 years, Terry Meyerhoff Rubenstein served as the executive vice president of the Family Funds. She orchestrated the transition to the current operating structure.

The Funds currently operate under a management committee that oversees grantmaking decisions. The management team is made up of three professionals who work directly with the committee chair.

In advance of meetings, committee members are sent emails advising them that board dockets are available on an internal, password protected website. From there, they can download materials to their electronic devices.

"We strive to make our grantmaking process as user friendly as possible for both trustees and grantees" says Elizabeth Minkin, a fourth generation family member and director of Baltimore and domestic initiatives. "This is a business. This is our long-term legacy—to steward this money which has been entrusted to good decisions made by the family. Our goal is to involve all generations in carrying on the family tradition of philanthropy."

Ms. Minkin is part of the three-member management team that includes a director of Jewish and Israel initiatives and a director of grants administration. This team of professionals reports to the chair of the grants management committee. The director of grants administration works with the family office. In total, there are four individuals who work for the family office and two full-time and two part-time employees who work for the charitable funds.

The family office director reports to the family. Then there's no question. That works fine."

Another added, "It's a challenge if you've got two chains of command, two separate payrolls, two separate legal entities, but the family says it's integrated," one family office director said. "Somebody's got to be in charge."

But perspectives shared by foundation leaders offered quite a different view. "I've been doing this work for nearly three decades and I firmly believe that if the family foundation is housed in the family office, then the family foundation executive should report directly to the family, or to the chair of the foundation board," says one west coast family foundation executive. "This sort of direct reporting relationship emphasizes the importance of philanthropy to the family. It also sends a subtle but important message to the family office staff and the outside community. Having the family foundation director report to the family office director dilutes the importance of the foundation, and makes it appear that the family's philanthropy is secondary to driving the capital."

Best Practices: Governance

Multiple family meetings per year, committee structures, and term limits force good governance. Well-integrated offices have a regular and consistent plan for financial education and make training in this area part of every board/family meeting and a "must" for the coming of age experience. *See additional resources list on page 26 for additional resources on the topic of governance.*

When the family office already exists, it helps if staff recruited for the foundation have come from a family office, family foundation or client services perspective, as well as having some kind of nonprofit experience. Woo believes his background in corporate philanthropy at a global family owned company has served The Russell Family Foundation well. "Because I understand the demands of achieving responsible returns and corporate goals in the context of a family enterprise, I was able to walk into this partnership as a peer," he notes.

When the family office does not yet exist, it behooves the family to plan carefully and perhaps call upon the expertise of outside professionals to assist in that planning.

Reflections: The class divide

"One of the things we've had to be mindful of when making hiring decisions is to get people who don't have issues with the differences between family office and family foundation staffs, and the economic difference between the family and the staff. We have had a much better experience with more mature individuals. Over the years we've had a few younger employees where an attitude came out sideways. They didn't last all that long. The present staff is set to be here a good long time, and they understand that the chances of promotion are small because we're small. We make it a pleasant environment. We pay quite well. We know we need to do that because there might be other opportunities elsewhere if they're looking for advancement."

Managing the Shared Environment

In order to create the appropriate culture that allows for the cohesiveness of the family foundation and the family office, consideration should be given to the shared environment. For instance, if the family wishes the family foundation and the family office to be perceived as having equal importance, they should recognize that office placement and assignment send unspoken messages to staff.

Jill Seltzer, formerly of The Prince Charitable Trusts, commented, "We were treated with great respect. Our offices were right next to Mr. Wood Prince's. We weren't down the hall. We were right next-door; this sent a very important message to the staff. He clearly cared about us."

"The family foundation has always been housed with the family enterprise," said Sally Lew, a consultant/foundation administrator to the Y&S Nazarian Family Foundation. "From my point of view, it's absolutely advantageous. Everything is here. All the family members can find foundation files, grant files, etc. It's readily available if they need any information. The foundation and its staff are not that large that it would require a separate office. It's a perfect fit to be housed in the family office. I can't imagine it any other way."

CONCLUSION: SETTING THE STAGE FOR SHARED CONVERSATION

What are the key things to keep in mind for family foundation and family office professionals seeking to work together toward a common purpose? Results from this first-ever study and follow-up interviews suggested a number of important starting points:

- ***A focus on values:*** The values of the family will influence both the philanthropic arm as well as the family office. If all parties commit to understanding and supporting these values, there is greater opportunity for integration and success.

- ***Different measures of success:*** Recognition on both sides that the indicators of performance for financial management and philanthropy are very different but equally important. Clear, definitive answers are less easy to come by in philanthropy, but family foundation staff must find ways to demonstrate the real value of their work.

- ***Recognize the role of emotions:*** Issues that get discussed around the family's philanthropy carry emotional complexity. While financial discussions can also be emotional, it's a different kind of emotion.

- ***Good governance does not just happen:*** Having a committee structure and term limits as well as multiple family meetings per year can help to "force" good governance within the family. Family councils can also be an excellent tool for achieving this goal (see page 20 for details).

- ***Family offices are not a cure-all for challenging situations:*** It is unlikely that families who don't get along in the usual course of things will suddenly get along when they find themselves in a family office/foundation structure. Families and professionals should consider all family assets when structuring and governing their philanthropy, and should find ways to ensure that the family office and foundation staff are aligned in their understanding of the family's goals and challenges.

Finally, our surveys and interviews told us that across the country there are people committed to working together in family offices and family foundations. Whatever their structure might be, there is a common goal: to have all of the family assets brought into play for the benefit of the family and the communities they serve. Every family is at a different place on that pathway. Some are dealing with difficult challenges. Others have successfully overcome those challenges. But each and every one of them is working towards that common purpose.

LIST OF ADVISORY GROUP MEMBERS

The National Center is grateful to the following individuals for helping to guide the development of this report.

- Patricia Angus, Founder and CEO, Angus Advisory Group

- Ruth Easterling, Managing Director, Member Services, Family Office Exchange

- Virginia Esposito, President, National Center for Family Philanthropy

- Bruce Maza, Executive Director, CE & S Foundation

- Craig Muska, Director of Investments, Foundation Services, Threshold Group

- Caren Yanis, President and Executive Director, Crown Family Philanthropies

- Danielle York, Director, 21/64

ADDITIONAL RESOURCES ON FAMILY OFFICES AND FAMILY PHILANTHROPY

Periodicals

- FOX Connects
- Private Wealth
- Family Office Review

Membership Organizations:

- Family Office Exchange
- Family Office Association
- Family Offices Group

Books:

- *Family Governance: A Primer for Philanthropic Families* by Patricia Angus (National Center for Family Philanthropy, 2004)
- *Family Governance Meets Family Dynamics: A Survey and Strategies for Successful Joint Philanthropy* by Patricia Angus and Fredda Herz Brown (National Center for Family Philanthropy, 2007)
- *The Family Office: Advising the Financial Elite* by Russ Alan Prince, Hannah Shaw Grove, Keith Bloomfield, and Richard Flynn. (Charter Financial Publishing, 2010)
- *Family Legacy and Leadership: Preserving True Family Wealth in Challenging Times* by Mark Haynes Daniell and Sara S. Hamilton (John Wiley & Sons, 2010)
- *Family Wealth—Keeping It in the Family: How Family Members and Their Advisers Preserve Human, Intellectual, and Financial Assets for Generations* by James Hughes Jr. (Bloomberg Press, 2004)
- *Generations of Giving: Leadership and Continuity in Family Foundations* by Kelin E. Gersick, Deanne Stone, Katherine Grady and Michèle Desjardins (Lexington Books, 2004)
- *Guide to Impact Investing for Family Offices and High Net Worth Individuals: Managing Wealth for Impact and Profit* by Julia Balandina Jaquier (Guidetoimpactinvesting.net, 2012)
- *The Power to Produce Wonders: The Value of Family in Philanthropy* by Virginia M. Esposito (National Center for Family Philanthropy, 2010)
- *Splendid Legacy: The Guide to Creating Your Family Foundation* by Virginia M. Esposito (National Center for Family Philanthropy, 2002)
- *Strategy for the Wealthy Family* by Mark Haynes Daniell (John Wiley & Sons, 2008)

SPECIAL APPENDIX: KEY LEGAL ISSUES TO CONSIDER WHEN A FAMILY OFFICE PROVIDES SERVICES TO A FAMILY FOUNDATION

By Ellen Kaye Fleishhacker and Andras Kosaras

When a family uses a family office to manage its wealth and a family foundation to carry out philanthropic activities, the question arises whether the family office can provide professional services to the family foundation, such as investment management, banking, and grantmaking services. Here are some key legal issues to consider when a family office provides services to a family foundation.

Self-Dealing. The private foundation self-dealing rule prohibits a family foundation from engaging in financial transactions with a "disqualified person." Disqualified persons, a term defined by the tax code, generally include substantial contributors to the foundation and its managers (e.g., directors and officers), as well as certain family members of these individuals and businesses controlled by these individuals. A family office is likely to be classified as a disqualified person.

There are some exceptions to the self-dealing rule. In general, a family office may provide services to a family foundation without charge without violating the self-dealing rule. If compensation is desired, a private foundation may pay reasonable compensation to a disqualified person for "personal services" that are reasonable and necessary to carry out the foundation's exempt purposes.

Reasonable compensation may include market rate compensation. The compensation may be structured in various ways, for example, hourly rate, fixed fee or a percentage of assets (especially in the case of investment management). The family foundation must be able to document through the use of comparables that the compensation paid is fair and reasonable in relation to the services provided.

Common examples of transactions that implicate the self-dealing rules include the following:

(a) *Banking, investment management and legal services.* A family office may provide banking, investment management and legal services to a family foundation because the tax regulations define these services to be "personal services" that fall within the exception to the self-dealing rule. These services may also include tax planning and compliance, financial reporting, accounting, and related services. The family foundation may pay reasonable compensation for these services.

(b) *Administrative and grantmaking services.* The IRS has published guidance in the form of private letter rulings that indicate that administrative and grantmaking services (e.g., grantee due diligence, strategic planning, and similar services) should qualify as "personal services" under the self-dealing rule (private letter rulings may not be relied on by taxpayers other than the taxpayer who requested the ruling, but they are helpful in providing insights into the IRS's position on a certain issue). As a result, a family foundation may pay reasonable compensation to a family office for providing these services.

(c) *Sharing employees.* A family foundation may reimburse a family office for the employees who provide "personal services" to the foundation. The foundation may reimburse the family office for the allocable share of such employees' salaries and benefits. The family office and the foundation should keep precise records of time spent on foundation activities.

(d) *Sharing office space.* A family office may provide office space to a family foundation, but it must do so without charge to comply with the self-dealing rule. The family office may not charge any rent to the foundation, even if the proposed rent is below market rate. However, the foundation may pay its allocable share of utilities or maintenance costs incurred for the use of the property, as long as the foundation makes those payments directly to the third-party and not to the family office.

(e) *Side-by-side investments.* A private foundation that has an opportunity to invest in a fund managed by a family office or in which disqualified persons are significant investors should consider any restrictions on such investments under the self-dealing rule. A side-by-side investment may be beneficial to the foundation because it may reduce administrative costs of investing, diversify assets, and gain access to additional investment opportunities. However, if the foundation's investments provide a benefit to disqualified persons, such as, for example, increasing the ability of disqualified persons to participate in a fund, then the foundation's investment may be prohibited under the self-dealing rule.

Investments. Under the private foundation rules, a private foundation is prohibited from making investments that jeopardize the carrying out of the foundation's exempt purposes (with certain exceptions, a private foundation, together with its disqualified persons, is also prohibited from owning more than 20% interest in a business enterprise). No type of investment is strictly prohibited, but careful scrutiny is applied to trading in securities on margin, trading in commodities futures, buying or selling puts, calls or straddles, buying warrants, and selling short.

A private foundation must also comply with any state law requirements regarding its investments. For example, the Uniform Prudent Management of Institutional Funds Act ("UPMIFA"), enacted in almost every state, provides requirements and investment standards that fiduciaries must follow when making investment decisions (these standards are generally consistent with modern portfolio theory). UPMIFA requires foundation managers to make decisions regarding investment management "in good faith and with the care an ordinarily prudent person in a like position would exercise under similar circumstance." UPMIFA also requires foundation managers to incur only "costs that are appropriate and reasonable" in connection with investment management.

Investment Adviser Registration. A family office that provides investment management services to a family foundation should be aware of any registration requirements pursuant to applicable state laws and recent federal laws enacted and new rules adopted by the Securities and Exchange Commission ("SEC"). Before the Dodd-Frank Wall Street Reform and Consumer Protection Act ("Dodd-Frank") was enacted in 2010 in the wake of financial regulatory reforms, most family offices fell within the definition of an "investment adviser" under the Investment Advisers Act of 1940 (the "Advisers Act") because they provided advice about securities for compensation. However, many were nonetheless exempt from investment adviser registration with the SEC in reliance on the Advisers Act's "private adviser exemption."

Under Dodd-Frank, Congress repealed the private adviser exemption. Nonetheless, following Dodd-Frank, the SEC adopted the "family office rule," which excludes certain single family offices from the definition of "investment adviser" and therefore provides some relief to certain family offices from the investment adviser registration requirements. The family office rule provides that a "family office" that is excluded from the definition of "investment adviser" must (i) provide advice about securities only to "family clients"; (ii) be wholly owned by "family clients"; (iii) be controlled by "family members"; and (iv) not hold itself out to the public as an investment adviser. "Family clients" include, among others, current and former family members, private foundations and other charities funded exclusively by family clients, estates of family members, and companies that are wholly and exclusively owned by and operated for family clients. "Family members" include all lineal descendants (including by adoption, stepchildren and foster children) of a common ancestor no more than ten generations removed from the youngest generation.

A private foundation is only a "family client" if all of the funding it *currently* holds came *exclusively* from one or more family clients. This reliance on funding from "family clients" instead of the more restrictive "family members" is seen by many as the SEC's attempt to strike a middle ground for family foundations under the family office rule. (In addition, the SEC provided a special transition rule that gives a family office the ability, under certain limited circumstances, to continue advising family foundations that do not meet that criteria without the obligation to be registered until December 31, 2013.) As a result of these definitions, family offices need to apply the criteria above to determine whether any family foundations or related entities they advise are "family clients."

To the extent that a family office advises a family foundation that does not meet the criteria above, if it wishes to rely on the family office rule to avoid the need to register as an investment adviser (and otherwise complies with that rule), its primary options are to (i) stop advising the family foundation or (ii) have the family foundation dispose of the non-family funding. In addition, a family office needs to consider potential state registration requirements that may apply under state law.

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About the Author

Anne Etheridge is the founding director of the Norton Family Office, which was created in 1990. She also served as Executive Director and Secretary/Treasurer of the Board of the Peter Norton Family Foundation until the Foundation was dissolved last year. Deeply committed to family philanthropy and, in particular, to exploring what personal wealth means to women, Anne was the driving force behind WomenGive. Last year, she helped to create the Women, Wealth and Philanthropy Initiative, based in Orange County, California. Anne has written for public and commercial television, and her articles have appeared in newspapers and magazines across the country.

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