SESSION 5: FAMILY FIRM GOVERNANCE

FAMILY OFFICES AS A NEW FORM OF FAMILY BUSINESS GOVERNANCE

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Abstract

Family firms form the majority of companies in almost every country in the world. The organization of the founding families, however, does not play a big role in corporate governance theory and practice. German family firms have created a relatively new form of family firm governance and organization: the family office. This specific form of organization deals with family organization, financial assets, and general family consulting.

1. HISTORY

The beginnings of family offices can be traced back to the sixth century. The so-called "mayor" acted as an interface between noble families and external service providers (Dimler & Theil, 2018, p. 135). In addition, the mayor was also responsible for the management and development of the family assets. Asset management was carried out in the interests of the noble families (Brückner, 2016, p. 212).

With the founding of the House of Morgan in 1838, the first classic single-family office was created by the Morgan business dynasty in the USA (Dimler & Theil, 2018, p. 135). The family office later also managed the fortunes of the Vanderbilts, Guggenheims, and Du Ponts. Thus, over time, the House of Morgan transformed itself into a multi-family office (Gaul, 2017, p. 104). In 1882, oil billionaire John Davison Rockefeller also developed a central unit of experts to manage the family's assets. Today, this would also be called a single-family office. At that time, however, these terms did not exist (Brodtmann, 2018, p. 83).

Industrialization and the resulting prosperity led to the establishment of a large number of family offices in the 19th century, in addition to the examples mentioned above. Due to the economic depression, family offices receded into the background again in the 20th century and lost importance. It was not until the 1980s, when prosperity returned to the USA, that family offices again became the focus of interest. Family offices then leaped Germany in the 1990s, when prosperity was generated by decisive developments in the technology sector. The development of family offices can thus be observed in parallel with economic cycles (Schaubach, 2019, p. 322).

Influenced by the 2008 financial crisis and a persistent low-interest-rate policy, wealthy families have increasingly turned away from traditional banks in recent years (Holler, 2017, p. 39). As a result, interest in family offices has risen sharply and the family office market has experienced strong growth in recent years (Brodtmann, 2018, p. 83).

2. TYPES

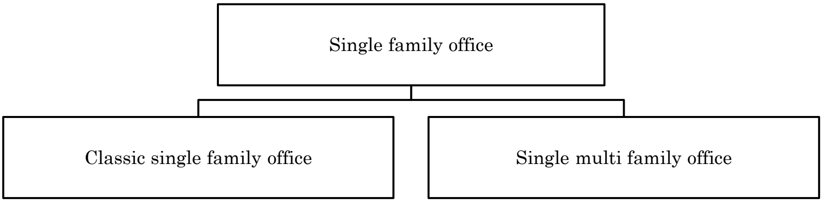
Family offices can be divided into two main groups:

Single-family offices are dedicated exclusively to the concerns of a single asset owner or family and often operate discreetly in the background. As a rule, single-family offices are founded by the asset owner himself (Bornmüller & Grossmann, 2011, p. 27). As a result, there is a high degree of dependence on the owner's family, and the orientation of the single-family office is tailored to their wishes. However, all costs must be borne by the owner's family. Therefore, a single-family office is only suitable for substantial assets (Freiherr von Oppenheim, 2008, p. 176).

Multi-family offices, on the other hand, manage the assets of multiple asset owners. Services are provided to all potential clients, although the client group may change from time to time (Bornmüller & Grossmann, 2011, p. 27). By pooling resources, greater efficiencies can be achieved and costs to asset owners are significantly lower compared to a single-family office. In addition, the range of services is generally broader than in single-family offices, as experts can be deployed for a wide range of topics and a broad network exists (Freiherr von Oppenheim, 2008, p. 177).

Within the typology of single and multi-family offices, there are further subcategories. These are shown and explained below:

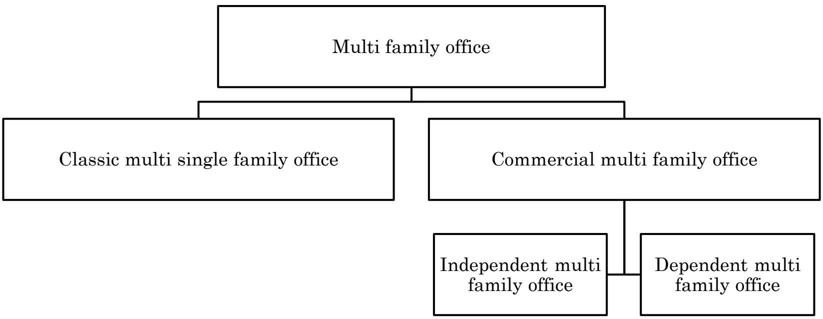
Figure 1. Subcategories of single-family offices



Source: Canessa, Escher, Koeberle-Schmid, Preller, and Weber (2016b, p. 42).

The classic single-family office is founded by a family and exclusively manages their assets. The owner is the family. The single multi-family office manages the assets of several families. However, unlike multi-family offices, it does not accept non-family mandates. Both subcategories can exist without the family business, alongside the family business, or integrated as part of the family business (Canessa et al., 2016b, p. 42).

Figure 2. Subcategories of multi-family offices



Source: Canessa et al. (2016b, p. 42).

The classic multi single-family office is owned by multiple families and manages the assets of the owning families jointly. Additional families may be subsequently integrated as shareholders. The management can be carried out either by the owner families themselves or by an externally contracted manager.

Commercial multi-family offices are suitable for families who wish to join a family office as a client without becoming (part) owners of the office. An independent multi-family office is owner-managed by the founding families or a non-family founder and is independent of banks. A dependent multi-family office is usually a subsidiary or a division of a financial services provider, which is also the owner of the dependent family office. However, it is questionable whether a dependent family office acts independently and exclusively in the interest of the asset owner in the sense of the definition of family offices or whether its profit maximization is in the foreground (Canessa et al., 2016b, p. 44).

Occasionally, commercial multi-family offices are also referred to as corporate family offices (Freiherr von Oppenheim, 2008, p. 177).

3. SCOPE OF SERVICES

There is no generally accepted definition of family offices, and the term is not protected by law (Rosplock, 2014; Bornmüller & Grossmann, 2011, p. 25; Dimler & Theil, 2018, p. 136). The scope of services provided by family offices, therefore, varies widely. The public perception that family offices are exclusively a family secretariat is generally not true. Although they also perform administrative tasks for families, family offices are usually viewed as professional asset managers. While some family offices actively manage securities portfolios, others limit themselves to selecting professional external asset managers or negotiating good terms with them (Canessa, Escher, Koeberle-Schmid, Preller, & Weber, 2016a, p. 6). An empirical study by UBS confirms this. It shows that 90% of strategic asset allocation and 83% of risk management, respectively, are performed by the family office itself, while 74% of investment activities and securities portfolio management are outsourced (UBS, 2021, p. 38).

According to an empirical study by Schaubach (2011), in addition to the aforementioned liquidity and securities management, insurance management, investment property management, tax advice, and corporate governance are also relevant. In some cases, the management of art and consumer goods can also be found. In addition to the financial asset services described above, some family offices are also active in the area of human and social assets. For the development of human assets, in some cases schooling, studies or internships are arranged and health services are recommended. In the area of social wealth, preparation for assuming family responsibilities and mediation of family disputes are recommended (Schaubach, 2011, p. 266).

Despite the very different services provided by family offices, what they all have in common is that they act as a central point of contact for all issues relating to family assets in a continuous cycle of analysis, consulting, and controlling (Bornmüller & Grossmann, 2011, p. 31). A family office always acts in the family's best interests and exclusively represents their interests. The aim is to increase the family's value chain and not that of the provider. Compared to large asset managers, the focus there is often on maximizing the family's success in the placement of its products, which can lead to a conflict of interest with the family's goals. Indeed, large asset managers and banks occasionally consider establishing their own family offices. However, this is conflict-prone for the reasons mentioned above (Schaubach, 2019, p. 329; Brückner, 2016, p. 213).

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