PROFILES

21st Century Single Family Offices: What Service Providers Need To Know-Special

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Directory of Family Office and Wealth Advisory Technology Service Providers
Executive Summary

Current Trends
• The 21st Century SFO is run like a business. SFOs value quality of service, control, flexibility and cost efficiency more than longstanding relationships
• Generational and technological shifts are the main accelerators of structural change in SFOs. Recent market turmoil has added momentum
• Increased number of providers and solutions creates more flexibility and cost leverage for SFOs

Key Take-away
• SFO service providers who adapt their business model to these current trends will win
The establishment of an SFO has long been regarded as the best way for a family of significant wealth to exert control over its destiny, to fulfill its legacy and provide stewardship for successive generations. Recently, the continued viability of the SFO business model has been called into question. Far from becoming extinct, we believe that the SFO is alive and well and is evolving to take advantage of market opportunities.

SFOs oversee a broad range of services, including financial, tax and estate planning, investment management, financial accounting, reporting and bill pay, trusteeship, lifestyle management and education for their family member clients. While some SFOs fulfill nearly all of these services internally, many SFOs are able to effectively oversee the balance between internal and externally provided services. Almost all SFOs oversee the investment process. A recent Family Office Metrics SFO survey revealed that 9 out of 10 multi-generational SFOs were formed specifically to manage the family's investment assets. Nevertheless, new technology and service models have made it possible for SFOs to delegate vital functions to external providers while maintaining strong oversight, control and a focus on increasing returns and minimizing costs.

The 21st Century SFO Is A business
The 21st century family office is managed like a business. With a corporate structure and hierarchical governance framework the modern SFO values speed, quickness, flexibility and efficiency. Generational and technological influences have been the biggest drivers of this shift because younger family members and executives appreciate the benefits of technology and know how to use them to best advantage. Recent market pressures have accelerated the move to employ more technology and automation as SFOs seek to become more efficient and reduce expenses, including labor costs. According to Family Office Metrics client experience, SFOs spend up to 70% of their operating budget on labor costs excluding investment management fees. SFOs understand that there are more choices and flexibility than ever before and, as a result, they are making more demands upon their service providers. SFOs are also open to new channels and are increasingly receptive to Software as a Service (SaaS), for example. SaaS can be extremely cost efficient because software is paid for each year to the vendor who is responsible for all uptime and support, thereby reducing the need for onsite IT support. Many software and service providers offer SaaS alongside the traditional in-house ownership and outsource service models.

Surprisingly, one of the biggest problems for SFOs is 'too many choices.' SFOs are faced with a growing number of service providers and software solutions. Adding to the sheer volume of choices available is the fact that the lines between providers are blurring.

In the past few years there has been an explosion of firms that offer services to SFOs. Firms that previously only served the hedge fund or private equity markets are gaining traction with SFOs because they provide accounting and reporting solutions for alternative asset classes in which many family offices are heavily invested. Firms like Archway Technology Partners, SunGard Investran, Relevant Equity Systems, eFront, Vitech, Jobstream and TheNextRound can accommodate a complex portfolio of alternatives combined with complex multi-tiered ownership structures. Jason Brown, CEO of Archway, noted that "Previously, nothing in the family office space could do the type of reporting families needed" (for all asset classes).

Technology firms like Advent and SS&C that previously provided portfolio accounting only for traditional assets to SFOs have begun to offer accounting and reporting solutions for alternative assets.

Alongside the improvements in portfolio accounting and reporting there has been forward progress in other important technology applications for SFOs, including client relationship management, document management and database management. Relatively new technology software manufacturers like Salentica and Aristata provide client relationship and document management solutions, respectively, that are specifically targeted to SFOs. Tim Davey of Salentica noticed that "there was a glaring lack in the (family office) marketplace for a product that could track every aspect of the family, even art, real estate, and collections where the linkages can be immensely complicated." While many integrated service providers and analytics engines, like PerTrac and FinCad, offer data management tools as components of their platform, firms like DataAgent now provide the capability to 'bolt-on' data management and analytics capabilities to portfolio and general accounting software.

Some firms are broadening their offering to provide higher value add and greater efficiency to SFOs. Fidelity Family Office Services joins the power and reach of its market leading broker dealer together with the personal service and access that SFOs need for trading desk, clearing and custody at a competitive price.

Some CPA firms, like Rothstein Kass and WTAS, that traditionally focused primarily on tax and audit services to SFOs have created and successfully grown practices providing planning, analysis, back office support, transactions and advice on investment services to SFOs.

The top tier custodial banks have taken notice and responded. Building on their dual strengths of data aggregation and custody processing, market leaders like BNY Mellon and Northern Trust offer enhanced performance reporting and investment analytics inside their technology platforms to SFOs with traditional and alternative investments.

21st Century SFOs are constantly looking for ways to reduce or re-engineer internal labor as they identify and integrate best in breed service providers. Smart SFOs know that 'no one size fits all' and plan accordingly to buy, build and integrate the very best solutions based upon their business strategy and budget.

21st Century SFO Business Strategy

With so many existing players and new entrants offering services and solutions, SFOs have difficulty finding the most suitable providers. Additionally, SFOs have to determine the right mix of services and solutions delivered both internally and externally. Family Office Metrics is a leader in advising family offices on business strategy before selecting or deploying a technology or service solution. What do successful SFOs do?

The successful family office will have a clear vision of the future and well defined scope of services, as well as a strategy for achieving its objectives. Often, the mission of the SFO will include multiple objectives; the education and integration of younger family members, the preservation of the family legacy, cost controls, risk management or simply the provision of superior investment results. It is these objectives that will dictate the principal services provided by the family office which will in turn determine how the office is organized, and appropriate staffing, operations and technology.

Business Models Impact Technology Selection

SFOs must consider the impact of their business strategy when selecting a technology platform. There are several important factors that have an impact on the choice of business model and the selection of technology and other services.

Figure 1 describes the SFO service needs and shows the hierarchy of family office service models. At the bottom of the hierarchy, an SFO can be described as following a Compliance and Control business model, essentially providing a back office for the family. In this case the SFO provides record keeping, reporting, trust and tax accounting. The SFO may also provide bill paying and other personal services.

Further up the ladder is the typical investment based SFO, which provides investment management services in addition to the basic services of compliance and control. SFOs focused on investments will typically oversee investment policy, due diligence, manager search and selection, monitoring and reporting.

Finally, some SFOs provide a fully integrated and interdisciplinary approach incorporating financial, tax and investment planning as well as coordination of strategy. In this approach, planning is the key to successful wealth transfer and the forward look by the SFO is the important service delivered to family clients.

Depending on the business model, its primary focus and outputs, SFOs will have different technology requirements. Successful SFOs view technology selection as part of a larger business strategy that follows an interdisciplinary planning approach.

A Case Study

The following is an example from a recent Family Office Metrics client engagement. This SFO serves a multi-generational, multi-billion dollar family and employs the integrated planning approach described in Figure 1. The SFO was facing the problems arising from the intersection of a complex entity structure and an even more complex asset allocation. Although the primary pain point was reporting across asset classes and ownership structures, the SFO needed more than investment reporting software, it needed a way to communicate and collaborate across the various constituencies, including management, external advisors and family members. The SFO decided to plan and execute a complete re-engineering of business process and workflow in conjunction with needed systems and technology improvements.

The SFO vision statement identified achieving and maintaining a ‘world class office’ as a prime objective. The project envisioned by the SFO set the following as goals:

- Accurate and timely accounting
- Comprehensive and consolidated reporting
- Easy and available, firm-wide communication and collaboration

The first step was to conduct a business process assessment that involved all levels of the organization, from the CEO and family members to the administrative staff, and that also crossed over all disciplines. Following the assessment, a strategic plan was constructed with the input and agreement of all stakeholders. A formal governance structure – a project management office – was created and used to manage project work, mitigate risk and provide regular reporting. The project team, composed of SFO employees and Family Office Metrics consultants worked with multiple vendors and service providers, to implement the strategic plan. Using multiple best in class solutions, core accounting and reporting operations were modernized and automated. With the help of different vendors, data management and document management were enhanced and made available in controlled environments to all stakeholders based upon need. Building on the Microsoft server array, a web portal served as a personalized window on the portfolio, accounting and financial reporting, and document repositories. The relationship management and the work flow optimization tools created a framework for the SFO to modernize and control its activities much more effectively and efficiently. The goals of the project were met and the SFO achieved a level of control and quality by pursuing a combination of best in class and open architecture solutions.

What does this mean for providers selling to SFOs? The case sends a clear message to providers who want to succeed in this market. The SFO is a sophisticated buyer looking for a best in class solution. Market conditions and technological developments have shifted the power to the buyer. SFOs can leverage client relationships to get the services they want and need, and SFOs favor open architecture and collaboration across all channels. Now, more than ever, providers need to be open to working with other providers to provide the best total solution for SFOs.

A Prediction

In the 19th century, SFOs had an in-house army of clerks preparing and approving the accounting records and reports using quills and inkwells. In the late 20th century, SFOs applied systems and technology to perform routine accounting and reporting and opened up to the opportunity presented by readily available market data. In the 21st century, SFOs favor the independence and objectivity of the open architecture approach. The implication of open architecture for providers is that of teamwork and collaboration. Technology is changing the game for SFOs. Service providers who embrace open architecture will prosper.

Jon Carroll is CEO and co-founding partner and Elvira Orza Hnatov is managing director and partner of Family Office Metrics in New York. Family Office Metrics is the leading provider of technology, operations and strategic consulting to the family office marketplace. We focus exclusively on the family office to provide business and technology solutions that help family offices better serve their clients. We also work with ultra high net worth clients who are considering starting or joining a family office. Our professional consultants leverage our combined business, operational, and technical expertise to develop solutions that address the unique challenges family offices face today—solutions that can carry your family office successfully into the future.