NEW SFO REGULATIONS

CREATE OPPORTUNITIES WITH THE AFFLUENT

BY TIM VOORHEES

Technological and regulatory changes are creating unparalleled opportunities for advisors who provide high-tech and high-touch solutions for America's millionaires.

Clients with substantial assets need advisors who simplify the wealth management process by offering integrated and personalized investment, risk management, accounting, tax planning, philanthropic and family governance services. Insurance professionals who embrace the trend toward integrated services find that clients value advisors who can illustrate how risk management strategies complement other wealth planning solutions used by affluent families.

Integrated one-stop planning has been offered traditionally by multifamily offices ("MFOs"), which target the 10 percent of America's eight million millionaires who have more than $10 million of assets. Even more specialized family offices are known as single-family offices ("SFOs"). SFOs serve centi-millionaire families that are willing to pay the high costs related to maintaining a qualified staff of internal wealth management experts.

Before the passage of the new Dodd-Frank regulations in July 2010, MFOs and SFOs were not required to register with the Securities and Exchange Commission if they had fewer than 15 clients. This exemption from the Investment Advisors Act of 1940 helped groups of wealthy families minimize administrative expenses and make investment decisions with minimal regulatory scrutiny. The new law, which goes into effect July 2011, replaces the broad exemption from the 1940 Act with restrictive new rules. The new "family office" will likely be an entity that has no clients other than family members, is owned and controlled entirely by family members, and does not hold itself out publically as an investment advisor.

Because large numbers of America's estimated 3,000 SFOs may not meet this new definition of a family office, many families with SFOs may have to seek services elsewhere. Single-family offices are closing down their boutique operations and forming relationships with RIA wealth management groups or wealth advisory teams that have left banks and brokerage houses. These former SFOs tend to form firms that focus on investment management issues, but often do not have the full array of family office services requested by wealthy families.

Industry changes create opportunities for professional advisors who maintain cost-effective and technologically efficient MFOs. New regulatory burdens have set in motion "creative destruction" that will likely force SFOs to seek the lower-cost services of the MFOs that harness new technology. Entrepreneurial MFOs will harness the power of the microchip to monitor investments, manage risks, generate accounting reports, develop advanced tax planning illustrations, fund charitable foundations and unite family members with Web-based project management and reporting systems. High-tech MFOs can develop customized deliverables and serve wealthy families at costs much lower than those charged by traditional SFOs.

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Astute MFO managers realize that many wealthy clients go to their firms primarily for tax-efficient asset management, estate planning and risk management services. Helping wealthy families with these services requires integrated solutions. Only by combining multiple disciplines with investment planning can a family office consistently maximize after-tax cash flow and wealth transfers while minimizing risks.

More families are asking for fully integrated solutions that evaluate all relevant issues when calculating lifetime cash flows and expected inheritance amounts for each beneficiary. Comprehensive planning systems have traditionally required large commitments of capital to train staff, standardize processes and maintain state-of-the-art technology.

As overburdened SFOs are being forced out of business by the new regulations and technological demands, the largest regional and national accounting and law firms have invested resources to create MFOs with full-orbed capabilities.

Now, CPA and law firms of all sizes are seeing the potential opportunities of MFOs that provide the services requested most often by millionaires. Such professional firms have a strong competitive advantage because they can cost-effectively train current staff members to provide a broad array of family office services to wealthy families who are already clients of the firm. Accounting and legal professionals often have the diverse education, experience, intelligence and professionalism that wealthy families trust when seeking help with complex multidisciplinary planning issues.

Costs of adding MFO capabilities to an existing professional firm will typically be much lower than expenses associated with maintaining a traditional SFO. Professional publications and conference speakers showcase a growing array of ready-made investment, risk management, accounting, tax planning, philanthropic and project management resources designed for firms adding family office services. Thanks to the wonders of Web technology, planning and reporting resources previously available only to the wealthiest families are now cost-effective for most of America's millionaires.

Savvy investment and insurance professionals are licensing the family office technology and forming relationships with CPA and law firms. Accounting and legal firms express growing willingness to open a "Family Office" and refer existing wealthy clients to an investment or insurance professional "down the hall." Traditional insurance and investment advisors are flocking to training in order to gain the relationship and technical skills needed to unite family members and advisors around an integrated plan for managing investments and wealth transfers. Former stockbrokers, insurance agents and other financial industry professionals are reinventing themselves as competent and credible family office managers within CPA and law firms.

When an accounting or legal firm opens its own family office, the professional firm will typically take an ownership interest in the family office. This business model aligns the economic interest of the family office and professional firm while minimizing regulatory challenges. Such family offices within professional firms have flourished as traditional SFOs have languished over the past few years.

Financial advisors may hear enough negative news about traditional single-family offices to think that nothing but storm clouds define the horizon. But the wise advisors know that the darkest clouds can have a silver lining. As is so often true in the 21st century, each time the regulators shut down a business, high-tech entrepreneurs see exciting and profitable new vistas. The family office entrepreneur who focuses on the needs of wealthy families and the power of new technology will develop the most hopeful vision of the future. In the midst of regulatory uncertainty, insurance and investment professionals have unparalleled opportunities to provide high-tech and high-touch solutions to millions of American millionaires. INN

Tim Voorhees, *J.D., MBA, is the managing partner of the Copenbarger & Voorhees LLP law firm and the president of Voorhees Family Office Services, Inc. Tim can be reached at Tim.Voorhees@innfeedback.com.*