How to manage the challenges of an embedded family office

BY CHARLIE CARR

Many successful family businesses have a form of family office embedded in the company. It may start with the CFO helping family members with their taxes, or someone in accounting setting up the books for a family member's outside business, or perhaps someone advising a family member through the purchase of a house or car.

Over time, this often becomes two or three employees supporting the owners' outside needs, plus one-off support from staff in IT, legal and other departments. Many families don't think of this as a family office. As one founder told me, "The business is my family office."

The pitfalls

This is not necessarily a bad thing. A family office embedded in the business can be the most cost-effective way to manage risks to the family while supporting their wealth and endeavors outside the family firm. However, there are several challenges to an embedded office, which require careful management or may even result in the family deciding to separate the office from the business.

• *Distraction*. Business staff should be focused on growing the business and serving its clients. Supporting family members' personal acquisitions or handling their separate needs may distract company staff from their primary roles. It is difficult for even a senior staff person to explain to one of the owners that an upcoming tax deadline or new technology release won't leave them time to support the family member's personal request.

• *Privacy*. When business staff also support the family, they may not be as diligent about protecting the family's privacy as dedicated family office staff would be. They might not be discreet when the president of the company asks about her brother's personal financial matters, and they might be tempted to tell co-workers about the new sports car a family member is buying.

• *Fairness*. Is it fair when family members who work in the business are able to make greater use of business staff for personal needs than family members who do not work in the business? In some situations, large shareholders don't have the opportunity to take advantage of business staff, while minority shareholders who work in the business leverage staff extensively.

• *Risk*. A family office should reduce or mitigate risk to the family, perhaps by providing advice and support as family members make large acquisitions, ensuring they have adequate property and casualty insurance or providing technology and cybersecurity support. If family members outside the business are not comfortable using the business staff, then the family isn't mitigating this risk as intended.

> Handling family members' separate needs may distract company staff from their primary roles.

• *Part-time focus.* When the family office consists of business staff who support the family on the side, those staffers might not perceive the family office as their full-time job. It is unlikely that anyone is providing strategic planning, being proactive about risk management or even looking at how to most effectively support the family's needs. For example, someone in accounting may provide paychecks for household staff, but is anyone in the organization performing background checks on those staffers?

• *Control*. An embedded office can fall into a "no man's land," where everyone assumes somebody else is providing proper oversight and control. In one case we know of, nobody was reviewing business credit card expens-

Charlie Carr, CFP®, leads PwC's Family Enterprise Advisory Services practice, which advises family businesses and family offices (pwc.com/us/familyenterprises).

es for the embedded office — accounting considered the task to be the responsibility of "the chairman's office," and the family had never thought about doing so.

• *Cost and value.* When the family office is embedded and split between parts of the business, nobody knows how much the office really costs. When we identify the various pieces and assign costs to them, owners are often shocked at how much they are spending on a family office. Family members also may not truly appreciate or value the services they receive when they don't know how much they really cost, how much time various staff put into those services or the level of expertise they are accessing.

An embedded office can fall into a 'no man's land,' where everyone assumes somebody else is providing proper oversight and control.

Mitigating the challenges

Embedded family offices can take many forms, and most of the above challenges stem from staff splitting their time between the business and the family. Some offices are embedded within the business legal entity but are actually a separate department or group that is fully dedicated to the family. Such an office can operate as though it were completely separate.

A hybrid version we see involves a small number of staff fully dedicated to the family (perhaps in the CFO's office), who oversee family requests. These staff in turn may leverage business employees and relevant expertise. This version minimizes the size of the office, provides dedicated staff and still leverages the skills and capabilities of the larger family business. This dedicated team also allows the family to create specific controls, measure costs and focus on key risks involving the family.

In one family office we recently designed, business staff were clear that they enjoyed providing support for family members — it was different from their day-to-day job, and they didn't want to lose that. Some hybrid solutions, such as the one described above, can accommodate that desire.

Why some businesses choose to separate the family office

Some people perceive embedded family offices as temporary, filling a need until the family or business is large enough to support a separate entity. That may be true, but not necessarily. Many families maintain an embedded family office for generations, and don't see any reason to change.

However, there are several reasons that a family may choose to separate the family office from the business. Here are a few such reasons:

• *The family is planning to take the business public.* Such families will want to carve out any personal support as quickly as possible, so advisers and analysts are not confused by the functions. It is extremely rare for a public company to house a family office (although we are aware of a few), and it is not something we recommend.

• *The family is planning to sell the business.* While we often see provisions within such transactions providing the family six months or even more to carve out the family office, there may be value to separating the family office before the transaction is in progress. One such reason is to ensure that staff whom the family wants as part of the family office will not be included in non-solicit arrangements with the new owners. We have seen scenarios where a family wanted the business CFO to run their new family office, but since they didn't plan it before the sale, they were not able to hire the person.

• *The family is looking to receive outside funding for the business, perhaps for future growth or liquidity.* Depending on the source and amount of such funding, they may be able to maintain an embedded family office, but it is likely that, even if the family maintains control, the new owners will prefer to have personal services separated.

• *The family decides that its privacy needs are not being met or business staff are being distracted.* While there are ways to mitigate these challenges, as described above, the simplest way remains separating the family office from the business. Many families have concluded that these challenges are insurmountable, leading them to a separation.

While there is no definitive research itemizing the number of family offices, embedded or otherwise, we believe there are more embedded offices than separate ones. Carefully considering and balancing the goals and needs of the family and the business enables you to decide if an embedded office can continue to support the needs of both. FB