A Road Map: Choosing Advisors To Help Your Family With Governance and Family Dynamics

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General Tips for Your Selection Process

1. Consider this a learning experience – having a number of firms and/or individuals to choose from will help your family continue to focus your requirements.
2. Clearly define the family's criteria for advisor selection and the process. Make sure to incorporate key family members in your process.
3. Use one questionnaire or "request for information" for all candidates. It will help to compare firms and/or individuals on a consistent basis and will help to eliminate candidates who do not suit your family's purposes.
4. Interview your finalists based on your questionnaire. Interview your finalists using the same representatives of your family if possible and using a rating system in order to most efficiently evaluate each candidate relative to the others.
5. Ask for and check references of your finalist. Use a standard set of questions for each reference and use the same person to do each reference check if possible (to minimize interviewer bias). Do not notify other finalists of your selection until you complete your reference checks and are satisfied. (You may need to opt for your "runner-up" choice, and it is not necessary that they know their ranking.)

Determine Your Family's Criteria for Selection of an Advisor

- What is our purpose in hiring an advisor? Can one person do all that we need?
- What is the task our family is looking to accomplish? Set objectives.
- Are we looking to accomplish a specific project? Define that project.
- Are we looking to establish a long-term relationship?
- What kind of professional is likely to be able to help us? What kinds of competencies should they have?

- What personal qualities will serve our family well? Think about "fit."
- Who have we used in the past? What worked and did not work in that advisor relationship?
- Write down your criteria and get your key participants to agree to it.
- Prioritize your criteria. What compromises are we willing to make?

Questions

- Nature of Business
- History, Background, Firm Culture
- Personnel
- Fees
- References

Five Issues on Employment Policies in the Family Office

Raised at a Member Roundtable during the 2007 Winter Forum

1. Principal/family office executive relationships: just business or part of the family?
2. How should family office executives be compensated? Performance-based bonus? Or a base salary plus bonus determined from qualitative standards?
3. Where do you find good talent for the family office?
4. Co-investing with the family: built-in incentive to perform well, or incentive only to perform well where co-invested?
5. Reporting: how do you communicate with each family or generation of each family in an effective way?

How To Handle Lack of Disclosure

Inside the Electronic Community

Excerpts of a dialogue from the private investor listserv

Question

I am wondering how others have handled family members' preferences for not disclosing their wealth to their children. We are facing a situation where one sibling wants to change investment managers for a trust (for which I am co-trustee). He has "of age" children who are contingent beneficiaries, whose signatures are therefore required. He does not want them to know about the trust. I do not want to shirk my fiduciary responsibility. Does anyone have suggestions for how to handle this?

Respondent #1

For our family this kind of issue not only never has come up, it never would come up as our typical question is how early should children be told about their wealth and in what level of detail, with the preference of sooner and more information if they can be induced into becoming involved.

Nonetheless, once a person accepts a trusteeship they have taken on a fiduciary duty to ALL the beneficiaries. Some trust instruments have a non-disclosure provision specifically allowing the trustee to keep information from the beneficiaries, and I have even seen some that allow the trustee to keep the existence of the trust secret from the beneficiaries.

If you get the signatures but don't tell the signers what they are signing, [this] would edge toward deceit, if not fraud (how else could you obtain their signatures unless you misled them about what they were signing). It would seem that the choices are:

1. Don't change the investment managers so you don't need the signatures.
2. Go against your sibling's wishes and inform the beneficiaries as you get the signatures.
3. Resign as co-trustee before you have to make a choice.
4. Do what your sibling asks of you.

#1 is the path of least resistance, and it buys time for your sibling to have a change of heart. #2 will probably, but not necessarily, result in some personal ill will. #3 doesn't completely get you off the moral hook, as you are now aware of what is

likely to happen, but it probably gets you off the legal hook. #4 likely is the beginning of a slippery slope for which you will be the slider, and this will probably not be the last time this is asked of you.

Respondent #2

I think that if you consult your lawyer and then explain to your sibling that he has not only fiduciary responsibility but is personally liable if the investment goes bad, he may have a change of heart. You could try to get examples of good parent-child relationships gone bad with this sort of thing. Getting advice from the forum is a great first step, but checking with your lawyer and then getting advice from the Jay Hughes of the world is a great second and third.

Respondent #3

Unless the trust instrument specifically requires notification of the contingent beneficiaries' signatures (and that would be quite unusual in my experience), I'm not sure there is a duty to disclose. Do you have to advise every contingent beneficiary whenever any assets are sold or purchased? Why should this be different? If the selection of the manager is done with due care and diligence, and the style/advice of the investment manager is consistent with the Prudent Investor Act (if adopted in your jurisdiction) and the general fiduciary of fairness as between the income and remainder beneficiaries is observed, I doubt that there would be any requirement of disclosure unless the trust agreement specifically requires it.

Respondent #4

I am not sure why contingent beneficiaries need to sign off on a change in investment managers. Typically a change in investment managers is something the trustee would do without requiring the consent of the primary or contingent beneficiaries. If the investment manager is also a co-trustee, then that is another matter. In that situation I understand why the beneficiaries would need to consent to a change in trustee.

I agree with comments regarding disclosure to primary beneficiaries. However, I don't believe there is the same level of disclosure required to contingent beneficiaries as to primary beneficiaries. You should check with your legal counsel to understand how your trust instrument and state law affects the duty to disclose to primary and contingent beneficiaries. My philosophy is similar: disclose early and disclose often. The challenge lies in how best to frame the disclosure and how well the parents, trustees, and/or family office have laid the groundwork for disclosure.

Having seen the non-disclosure route pursued I can't think of any instance where that resulted in a positive outcome. Quite the contrary: it always seems to have negative results, often lawsuits.

P.S. Are you indemnified for your service as a trustee and/or do you have any type of professional liability insurance? We have acquired what is essentially a D&O liability policy to cover not only director and officer liability but also fiduciary exposures. We have extended the coverage to all of our family members that serve in director, officer or trustee roles and to all of our entities. It is not inexpensive until you consider the liability exposures. We view the primary benefit of the coverage as having legal defense costs covered by our insurance carrier.

Respondent #5
You have received some great suggestions as to how to handle this. I would add that seeking legal counsel has several benefits of both a legal and interpersonal nature.

First of all, you could ask legal counsel to review the trust to see if there is any way to comply with your sibling's request legally. Some trusts have flexible covenants or interpretations that may lead you to a solution that does not require you to get the kids' signatures. When I deal with lawyers I always say, "This is what I want to accomplish, now tell me how to do it." Most lawyers like a challenge and will seek to get you an answer if it is possible. If you ask them, "What can I do or should I do?" you may get a very different answer.

Secondly, if the lawyer says, "I have looked at every possible angle on this, and you have to get the kids' signatures etc., then you can go back to your sibling and say, "I tried my best, but I have a legal responsibility!" Depending on your feelings you can also offer your resignation as trustee as an alternative. It won't change the legal reality, but maybe your sibling can find someone who is willing to break the law and set themselves up for litigation. In any case, it is not you telling your sibling that the kids need to be informed, it is a lawyer who is telling your sibling.

Respondent #6
Disclosure is the easiest path for the trustee and, according to Charles Collier's work on family wealth, it's supposed to be "best practice" as well.

But one could argue that, depending on the maturity or age of the beneficiary, non-disclosure, reduced disclosure or a staggered disclosure is more beneficial. We were facing this issue a while back and found the following: In Delaware, according to section 3303(a) of Title 12, the trustor can clearly limit or eliminate disclosure.

> § 3303. Effect of provisions of instrument
> (a) Notwithstanding any other provision of this Code or other law, the terms of a governing instrument may expand, restrict, eliminate or otherwise vary the rights and interests of beneficiaries, including the right to be informed of the beneficiary's interest for a period of time, the grounds for removal of a fiduciary, and a fiduciary's powers, duties, standard of care, rights of indemnification and liability to persons whose interests arise from that instrument.

From your email, the fact that the sibling doesn't want disclosure isn't much help unless that desire mirrors the grantor's wishes as expressed in the trust.

But a parent's wishes to shield children from lavish gifts from elders in the late teen/early 20's period is legitimate. It's hard for emerging adults to appreciate their first paycheck when burdened with (too much) trust fund information.

It's a delicate balance. As trustee, I would look at the following:

1. Perhaps you can get comfortable that a change of manager does not require contingent beneficiary's approval based on the trust language.
2. Perhaps the sibling would agree that a limited disclosure is appropriate at this time, focused on concepts, but without numbers.
3. If not, and the sibling feels that the non-disclosure issue trumps all others at this time, perhaps delay the change of manager for a few years.
4. And of course, resigning as a trustee (which may not help if it is more likely to trigger a notice to the contingent beneficiaries than a change of manager).

Good luck, and perhaps you can post the outcome on the listserv!