COMMITTEE REPORT:
ULTRA-HIGH-NET-WORTH FAMILIES & FAMILY OFFICES

By Hannah Shaw Grove & Russ Alan Prince

Generational Differences Can Lead to Succession Issues

Considerations for private client attorneys when advising family enterprises

Succession within family enterprises is complicated by numerous factors—history, interpersonal relationships, power dynamics, emotions—that influence the beliefs and the objectives of interested parties. Our recent research of family enterprises (and their private counsel) clarifies that the founding and inheriting generations possess distinct views that further cloud the issues related to succession and can make it difficult to construct and execute plans to ensure the continuation of the family business, wealth and values.

Our research was part of a global survey we conducted with representatives of two types of family enterprises: single-family offices (SFOs) and family businesses. The respondents were senior executives and/or family members in the organizations that met specific criteria. In both types of enterprises, the respondents were further segmented into two categories:

- **Founders** who built the family fortune and established the enterprise; and
- **Inheritors** who currently own and control the enterprise, having assumed responsibility from the founding generation

To augment the data from the family enterprises, we also surveyed their private client lawyers as they're essential to the success of both types of enterprises, including the transfer of entities and assets between generations. See "About the Research," p. 53, for more information about our study respondents.

Here are our key findings and considerations for private client attorneys as they help family enterprises navigate succession.

Succession Plans

The use of financial and operational succession plans varies widely by type of enterprise.

SFOs are typically created to preserve and enhance family wealth across generations while retaining control. As such, it's not surprising that they're twice as likely to have financial succession plans in place than a family business. See "Who Has a Financial Plan in Place?" this page. On average, 80% of SFOs have a financial succession plan as compared to just 41% of family businesses. It's worth noting that SFOs under founder control are proportionately more likely than those under inheritor control to have such a plan. The absence of financial succession plans can result in conflicts that can hinder the effective functioning of family enterprises. The same can be true if financial plans are outdated and no longer reflect the family composition or objectives.

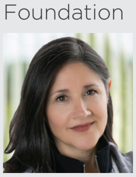
Who Has a Financial Plan in Place?

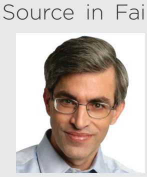
Single-family offices vs. family businesses

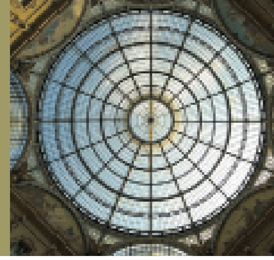
Generation	Single-family office	Family business	Weighted average
Founders	88.4%	37.5%	74.3%
Inheritors	66.7%	42.6%	53.7%
Weighted average	79.9%	40.9%	64.0%

403 respondents

Hannah Shaw Grove is the chief marketing officer of Foundation Source in Fairfield, Conn., and Russ Alan Prince is the president of R.A. Prince & Associates in Redding, Conn.







Who Has an Operational Succession Plan in Place?

Single-family offices vs. family businesses

Generation	Single-family office	Family business	Weighted average
Founders	41.8%	73.2%	50.5%
Inheritors	8.6%	61.1%	36.8%
Weighted average	28.9%	65.2%	43.7%

403 respondents

The opposite is true for operational succession plans, which are much more common among family businesses, of which 65% have such a plan versus SFOs, of which just 29% have one. See "Who Has an Operational Succession Plan in Place?" above. This is likely due to extensive experience among wealthy business owners and their advisors around the transfer of business assets to subsequent generations. These plans form the groundwork that enables inheritors to take over a business with minimum disruption and are critical to continued stable operations.

Multigenerational Planning Rationale

Importantly, some founders and inheritors have financial succession plans that span multiple generations—which is different from a plan that ensures succession from the current generation to the subsequent generation. This is frequently intertwined with estate planning and is especially true within SFOs, of which an average of 58% have multigenerational plans, as compared to just 12% of family businesses that make little effort to address the matter beyond immediate heirs. See "Multigenerational Planning," p. 54. Two generational differences are important to note regarding the use of multigenerational plans. Inheritors are more likely to use them within SFOs, which may stem from the growing interest in ensuring the long-term future

About the Research

Information about who responded

The data in this article, and more findings about single-family offices (SFOs) and family-owned businesses, are from the forthcoming book, *Family Fortunes: How Family Enterprises Thrive Across Generations* (2022). Note that "N" stands for the number of respondents; all monetary values are in U.S. dollars.

SFO Demographics, N = 239

Generations
61.1% = Founders
38.9% = Inheritors

Estimated family net worth of SFOs (weighted average)
17.2% = Less than $500 million
45.6% = $500 million to $1 billion
37.2% = More than $1 billion

Primary jurisdiction

17.2% = North America
14.2% = South America
22.6% = Asia
20.1% = Europe
2.9% = Middle East and Africa
23.0% = International (families that operate across more than one jurisdiction)

Family Business Demographics, N = 164

Respondents had a personal net worth of at least $30 million, a significant equity position in the family business and a minimum of 5 years as a C-level executive within the business with responsibility for governance.

Generations

34.1% = Founders
65.9% = Inheritors

Jurisdiction

60.4% = North America
37.2% = Europe
2.4% = Other

Primary industry

26.8% = Manufacturing
24.4% = Real estate and construction
14.0% = Distribution
12.8% = Retail/wholesale
11.6% = Services
10.4% = Undefined

Private Client Attorney Demographics, N = 148

Jurisdiction

25.5% = North America
17.1% = South America
20.2% = Asia
23.4% = Europe
13.8% = Tax-advantaged (for example, the Cayman Islands)

100% use time-based compensation, while 57% also use project fees and 14% use success fees.

Average annual compensation ranged from $1 million to $3.6 million in the most recent year (2020, 2021), with an average of $1.5 million.

— Hannah Shaw Grove & Russ Alan Prince

of the family, while founders are more likely than inheritors to use them within family businesses, albeit at much lower overall rates than what's seen in SFOs.

Multigenerational Planning

Single-family offices vs. family businesses

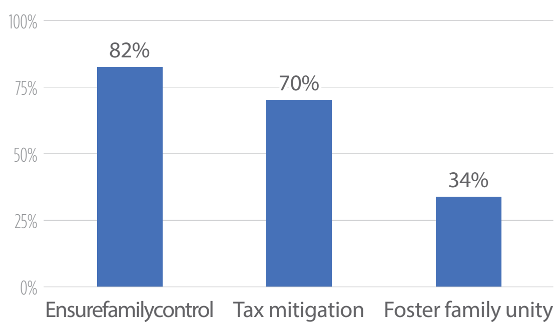
Generation	Single-family office	Family business	Weighted average
Founders	51.9%	15.4%	43.5%
Inheritors	71.0%	8.7%	44.4%
Weighted average	58.1%	11.8%	43.8%

276 respondents

The private client attorneys who consult with their clientele on such matters cite several reasons why founders and inheritors will choose to pursue a multigenerational approach to financial succession. See "Planning Rationale," this page. The most common is to help the family retain control, which dovetails with the purpose of many SFOs and family-run businesses in helping bolster and secure the family's stature and legacy. Another important factor is to help support the tax-efficient intergenerational transfer of a family enterprise. To a lesser extent, some attorneys point to these plans as a way of encouraging the family to work together. While forcing family members to collaborate can be detrimental in certain circumstances, some productive and proven methods promote family togetherness and unity.

Planning Rationale

Three primary reasons



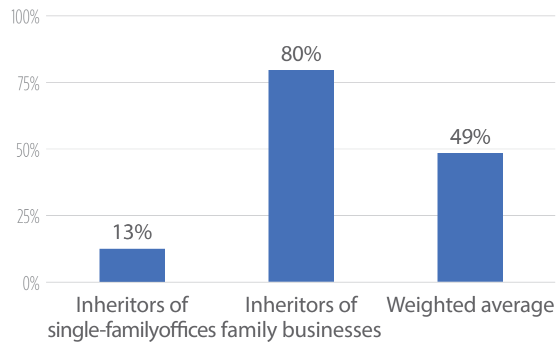
148 respondents

Preparation and Conflicts

Despite the high degree and use of planning within SFOs and family businesses to ensure perpetuation, on average just half of inheritors say they're prepared to assume control of the family enterprise. When viewed by type of enterprise, we see a sharp difference between SFOs, where just 13% of inheritors are prepared, and family businesses, where 80% are prepared. See "Well-Prepared Inheritors," above. The latter figure is likely due to individuals growing up in and around the business and having worked in multiple capacities over the years helping to boost their understanding of the industry, operations, clients, vendors and market cycles.

Well-Prepared Inheritors

Percentages differ based on type of enterprise

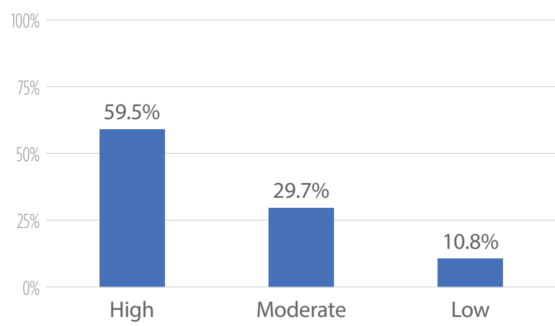


201 respondents

Private client attorneys observe that family conflicts can escalate when heirs aren't prepared

Likelihood of Conflict

When heirs aren't prepared to take control



148 respondents

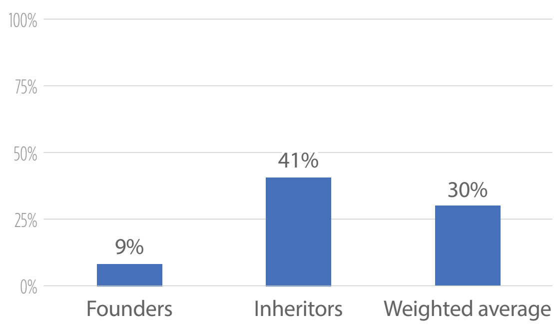
to take operational control of the family wealth, including the family business or the SFO. See "Likelihood of Conflict," p. 54. Aside from bad feelings, which can be abundant and cause lasting damage to relationships, such conflict often results in the wasting of family assets and potential erosion or disintegration of family enterprises. These conflicts may be avoided or diminished when founders put legal structures in place that compensate for the inheritors' present lack of knowledge and abilities.

Exiting the Family Enterprise

Even when the intent is to transfer the family business among generations, that outcome may not be possible due to a lack of capable and engaged heirs or unforeseen circumstances that threaten the value or existence of the enterprise. In this case, the ownership of the business will probably need to change.

Sale of Family Business

Inheritors most likely to consider this step



164 respondents

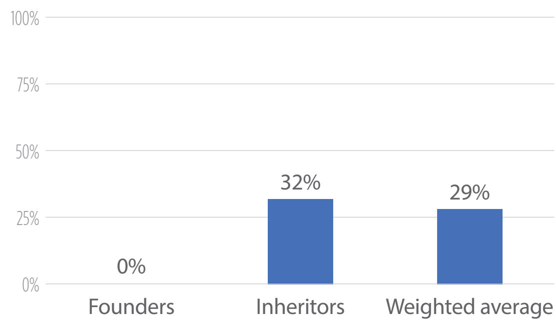
A wide array of considerations should be taken into account when it comes to exiting a family business, including the fact that select family executives may need to remain involved through a transition, and performance projections will need to be met if earn-out provisions are in the agreement. These scenarios can mean that the prior owners are, in essence, employees of the new owner for a period of time, which may be unexpected and uncomfortable for some individuals.

Even though our study participants were focused on the intergenerational succession of their family enterprises, on average about one-third of family business owners have or are considering the sale of their organizations See "Sale of Family Business," this page. It's interesting to note, however, that the idea of selling the family business is nearly five times more common among inheritors than founders.

Among the group of family business owners who are considering a sale, a similar percentage have or are presently taking steps to prepare for such a transaction. See "Preparing for Sale," this page. As before, these actions are occurring entirely among the cohort of inheritors, with none of the founders reporting any preparation. It's important to note that selling a business without any pre-sale planning can result in sellers getting lower prices for their companies and potentially having to pay more taxes on the transaction.

Preparing for Sale

Founders vs. inheritors



49 respondents

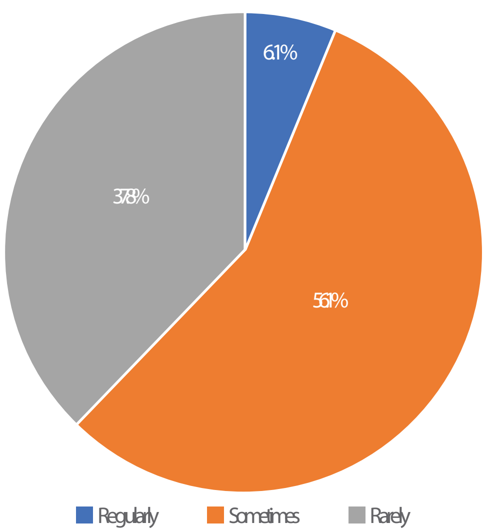
About four in 10 private client lawyers say successful business owners rarely take meaningful pre-sale action to mitigate the taxes on the sale of their companies, which represents millions of dollars in lost proceeds. See "Pre-Sale Action," p. 56. At the same time, slightly more than half report that business owners sometimes take meaningful action, and just 6% say it regularly occurs. It's quite common for business owners to look for ways to mitigate taxes as the transaction date nears or even after the sale is completed, but without sufficient lead time for thoughtful planning, it's often too late to achieve the desired results.

While exiting a family business is a well-established process, the same can't be said for

SFOs. Exiting an SFO may be accomplished in multiple ways. Some family members choose to leave and take their assets with them, providing there are no restrictions. This scenario doesn't change the inherent nature and mission of the office. Increasingly, exiting an SFO means transforming the business model so it's no longer an SFO but provides expertise to non-family members. This can take many structural forms; some organizations have explored ownership for all participating families.

Pre-Sale Action

Meaningful steps often aren't taken



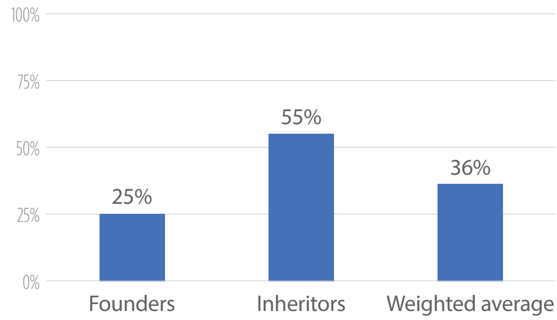
148 respondents

Among the SFOs surveyed, 36% have a strong interest in expanding their operations to work with non-family members. See "Interest in Expanding Operations," this page. Of note, this interest is significantly higher among inheritors than founders.

Ultra-wealthy families consider opening their family offices to other families for two dominant reasons. See "Motivations," this page. Founders and inheritors are at odds in how they view these two motivations. Founders cite interest from other families, and inheritors cite the ability to leverage their in-house expertise and capabilities in a way that results in potential profit and creates a larger pool of assets that can result in lower fees and better access to managers. That is, founders are likely more motivated by the idea of using their knowledge and infrastructure to support people they know, understand and trust, while inheritors are likely more driven by conventional business principles of profitability and expansion.

Interest in Expanding Operations

Founders and inheritors who want to work with non-family members



239 respondents

Considerations for Attorneys

Our research reveals that SFOs and family-owned businesses struggle with many of the same issues, but the founding and inheriting generations see things differently and are gauging future opportunities against their own unique set of criteria. This disconnect can create some critical exposures that, if left unattended, could snowball into bigger issues that detract from family harmony, profitability and success.

Family businesses are the cornerstone of economic growth and the engines of personal wealth creation. To help them survive across generations and eventually prosper and thrive, private client and family office attorneys should:

Motivations

Why families provide investment expertise

Motivations	Founders	Inheritors	Weighted average
Leverage investment expertise and capabilities	22.2%	82.4%	64.4%
Strong interest from other wealthy families	88.9%	9.8%	42.5%

87 respondents

- Evaluate the use of financial succession plans within family-owned businesses, where usage is low.
- Ensure that financial succession plans are up to date and reflect family composition and objectives.
- Evaluate the use of operational succession plans within SFOs, where usage is low.
- Help the family identify skills that are weak or lacking in the inheriting generation, and build professional development objectives into operational plans to ensure stable and continued operations.
- Work with the family to identify the motivations for multigenerational succession and estate planning, and ensure plans are drafted to meet those goals.
- Stay abreast of leadership plans to sell a family business to identify places in which you can assist with pre-sale planning.
- Help the family conduct comprehensive exit planning when selling the family business, which, to get the best results, may require the same elements of corporate exit planning paired with strategies and solutions for personal and family tax planning and wealth protection.
- Identify the extent to which families want to pass on more than business assets or wealth, and incorporate family meetings, mission development and philanthropy into your toolkit to provide them more holistic support.

— The data in this article, and more findings about single-family offices and family-owned businesses, are from the forthcoming book, Family Fortunes: How Family Enterprises Thrive Across Generations *(2022).*