An exit strategy to help ensure wealth legacy

In Asia, as more families join the ranks of the wealthy, concerns over wealth succession while keeping a sense of family cohesion are also rising in tandem, writes **Wing-Gar Cheng**.

Internal family conflict is prevalent among the ultra-rich families in Asia, as seen in media reports of wealthy dynasties fighting over their fortunes. The battle for control of the family business empire between the Ambani brothers in India, the dispute of the Kwok family in Hong Kong that ousted the eldest sibling as chairman and chief executive at Sun Hung Kai Properties and the legal fight over the late Taiwanese tycoon Wang Yung-ching's estate are cases that have dominated the headlines.

For such families, the business side is often very well set up, but the family side isn't. These conflicts have been the major factors contributing to the disintegration of businesses controlled by the Asian families.

One reason for the conflicts is that too much attention and emphasis is placed on the "business system" of the family business and too little on the "ownership system" and the "family system", according to Christian Stewart, Managing Director at Family Legacy Asia, a consultancy that specialises on family governance. "Family businesses would fail because of family conflicts and family businesses have family conflicts because of role confusion between family rules and culture, and what should be done in terms of best commercial practices."

"So the more that you can separate family matters from business matters, the better the boundary between family and business, the more robust your business will become and the less likely you will have family conflicts."

Exit strategy

Typically, the patriarch of the family tends to believe the family relationships are going to be constant, and that the working relationships between the family members will be consistent, Stewart says. But there are differences of opinions and often the views of one generation are vastly different from the next.

And when there is a change, for example, when the patriarch is no longer around, the family must start to think about how the members can work together. A change in the family relationship can lead to a family conflict, Stewart says. Should such incidents occur, a good rule of thumb, he says, is to think about how family members can exit from the relationship if things change and if things don't work out. "If you want to successfully preserve family wealth, then an important part of family governance is having an exit plan. Having the process in place so that you can consolidate the ownership, so if somebody doesn't like working jointly with the family, there must be a process that would enable them to leave."

Christian Stewart

Such solutions are best worked out when the patriarch is still around and increasingly, discussions about unexpected events and even the distribution of wealth after a patriarch's death are becoming less of a cultural taboo among Asia's wealthy families.

Some are increasingly seeking external advisers for help in overseeing their personal fortunes, according to Lee Woon Shiu, Managing Director and Head of Wealth Planning, Trust and Insurance at the Bank of Singapore.

"Through hearing all these stories and the friends around them that got into strife with their families, they have become more aware of the issues and as they get closer to the banks that they work with, they are more open to listening to what the banks would suggest to them, more feasible ways to deal with these disputes, which could happen if no better steps are taken."

Typically, advisers would share the experiences of other wealthy families and educate them on the tools of wealth planning, making the family understand the issues involved and inculcate the concept that "something must be done", Lee says. "That's the importance of looking at wealth not just in terms of financial capital, but also human and intellectual capital, to take a wider view of wealth."

When it comes to overseeing their personal fortunes, the typical options for the families may include seeking the advice of private bankers, establishing trusts or setting up family offices to manage the administration and accounting for various family assets.

Preservation versus creation

In Asia, the emphasis is not as much on continuity of wealth but more on growing wealth. In the family office context, there's a very big difference between a wealth preservation mindset versus a wealth generation mindset, Stewart says. But before a family can advance to this stage, establishing a family governance structure is the critically important first step. "It should all start with family governance."

Fan Choi

"The term governance talks about the way in which families make decisions together. Every family has a way of making decisions together but usually it's informal, so when people talk about governance, they usually talk about it as some kind of formalised process of making decisions.

Typically in Asia, when the patriarch is still in control, he isn't that interested in joint decision-making or formalised decision making, Stewart adds. "He's not that interested in bringing in the family into the decision-making process, but the Asian patriarch, if they have enough liquidity, will still set up family offices, which supports the investment decisions of the patriarch."

Some patriarchs who have created the wealth may not necessarily be as successful in conserving that wealth, or in maintaining that wealth. Still, the patriarch will be motivated to keep some core values that they hold dear to their hearts and may utilise western wealth planning tools to preserve and enshrine their values in the wealth succession plans.

Lee adds: "It's important that no matter how many children you have, each generation share the same vision and philosophy as the founding father. That's key. You get at least the second generation to buy into what the family wants to agree on family governance principals."

Wealth planning tools

It's also important that families, when deciding what is the best way forward for them, that they take into consideration factors such as the family's total wealth, their capital and income requirements over the short and longer-term, their risk appetite or whether the family consider themselves stewards of wealth, according to Mark Evans, Head of Coutts Institute.

Lee suggests starting a family trust first. "Because you can see in action when you're still alive, how that pans out. It doesn't have to be something that you can only envisage but you can't see it in action."

There are a pluses and minuses to family trusts, Stewart says. The good side of a family trust is the presence of a very clear control mechanism. The bad side is the inability of a family to exit from the trust if that member can't work with the rest of the family.

Some other issues may also arise, says Fan Choi, Head of Wealth Planning for North Asia at Coutts. "A trust could create potential issues if the beneficiaries or the trust assets are situated in a civil law jurisdiction such as mainland China because a trust is a common law concept and China is a civil law jurisdiction."

A family foundation, Choi adds, would work well for confidentiality and succession planning purposes as a substitute for a Will in Hong Kong and Singapore and would avoid the public probate procedures after the death of the founder. However, it might not be effective for tax planning purposes.

Lee Woon Shiu

A private trust company run by a family office which acts as the trustee of the family trust would enable the founder and the family to have more direct control and make speedy decisions on the administration of the family's trust structure, Choi says. But the private trust company must be administered professionally which can be costly.

Care must also be taken to ensure the tax status of the directors of the private trust company would not jeopardise the tax status of the private trust company and the trust structure. Legal and tax advice is important in the decision, Choi adds. "There is no best or one size fits all solution. It really depends on each family's circumstances and situation and the purpose for the planning."

Best solutions

Similarly for patriarchs contemplating family offices, there aren't any cookie cutter solutions for the process, according to Munish Dhall, Head of Ultra High Net Worth Offering and Client Development at UBS Wealth Management. "We don't provide standard solutions to a billionaire family. It's all very tailored. We work with the clients to provide the right setup for them."

Mark Evans

Families should really work on the family governance and a family constitution, a key document that institutionalises the management of the family office, he says. "The basic parameters that define whether the family wants maintain and preserve the wealth or grow the wealth, what is permissible and what is not permissible, what is the rule of play."

"You have agreed within the family, who is going to take what decisions, what is the process by which the decisions will be taken, who will be at the table, people who take the decision, be responsible for the consequences of the decision etc."

Agreeing on the family governance would take the most time, as well as defining the family constitution, he adds. Setting up a family office requires less time once the family constitution has been defined.

Stewart adds that having a family office which runs the liquidity of the family kept separate from the business would be the ideal solution. Family offices have been adapting their business models to more effectively help family business dynasties attain the objective of sustaining their legacies for as many generations as possible.

"The business has its own goals, it's entrepreneurial trying to make more money, taking risks and generating return, whereas the family office should be about wealth preservation. Often family offices provide shared services to the family, it should have a different set of goals from the business."

Asia-Pacific family offices (both single and multi-family offices) have a large proportion of their assets tied up in core family business holdings and illiquid assets, according to a study by UBS and Campden. Liquid assets only make up 40% of their total wealth, the study, Growing Towards Maturity: Family Offices in Asia-Pacific Come of Age, found. Families also worry about how to bring in the next generation to continue with the business operations.

Ultimately, the family wants to see the longevity of the wealth and prosperity of the family. Dhall says: "Asia will have its own solutions, it may not copy Europe or the US."

The big difference, Dhall adds, is that Asia is still in the wealth creation phase and Europe and the US aren't. "In Asia, the family continues to be involved very actively in the business so wealth management of the family is not only about the liquid wealth, it's going to be about how to grow the business and how to realise the values that are tied up to the business, which will require not the standard wealth management solutions but unique solutions." ■