

From FAMILY WEALTH REPORT

Families first: New wealth-management principles

Charles Lowenhaupt - 29 January 2009

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It's been a tough period, and more chaos and uncertainty is likely to follow. In the past year, vast amounts of private wealth have been lost or stolen in the most spectacular financial meltdown of our lifetimes.

Volumes will be written on the "whys" and "wherefores" of **Lehman, AIG, Wachovia, Bernard Madoff**, auction rate securities, and other names and concepts associated with the downturn. Meanwhile, people around the world who once had substantial wealth have seen their holdings cut in half or worse; some of the once-affluent are now destitute.

But looking back is only so helpful. This is a time for action. Private wealth is in urgent need of protection to prevent more pain and suffering. We should never again suffer another Madoff. Never again should we allow supposedly trusted financial institutions to squander our money and faith. Never again should we let conflict-riddled business practices serve as handmaidens to bad judgment. Never again should we allow failure to follow best practices to destroy the lives of so many people.

Up from the ashes

Convinced that the time has come to design protection for private-wealth holders, a team (of which I am a member) has drafted a new set of principles to guide the management of private wealth. These experts are trusted advisors -- lawyers, accountants, family-office executives, investment professionals -- to families around the world. They have the vision and see the risks a global financial contagion poses to family wealth and the loss of freedom and independence that comes from the mishandling of wealth.



They have joined with **Don Trone**, one of the primary forces behind the institution of ethical standards in institutional investment management and the investment-management industry generally, and an expert on the relationship between best practices and objective evaluations of fiduciary competence.

Together we have created the "**Principles of Wealth Management for Private Wealth Holders**" to articulate a sound philosophy for managing private wealth that will prevent the destruction of any more private wealth due to failure of investment process. The Principles give private wealth holders a roadmap or set of guidelines for

imposing responsible management on the service providers entrusted with their money.

More specifically, these far-ranging Principles call for:

- Separation of custody of assets and investment management,
- Transparency of advisors' fees,
- Disclosure requirements to prevent conflicts of interest,
- Standards for compensation of family office executives,
- Discouraging investment vehicles without transparency or liquidity,
- Insistence on customized investment portfolios meeting the needs of the owner,
- Requirements that any trustee or foundation director perform as a fiduciary subject to fiduciary standards.

To realize the benefit of the Principles, private wealth holders around the world must take two steps. First, they should adopt the Principles with respect to *all* of their operations worldwide. In other words, private wealth holders should say to themselves and their families, "This is the way we will have our wealth managed." Second, private wealth holders must ask their banks, family offices and other trusted advisors to ensure that wealth holders comply with the Principles by complying with the Principles themselves.

Managing in accordance with the Principles is likely to be a challenge for many advisors and providers, but without a groundswell initiated by private wealth holders, many will not be motivated to change.

Standards and certification

These Principles are necessary in a world where private wealth holders are now a global community. Families live, work and invest around the world. Family members are linked with one another and with their trusted advisors by technologies that span oceans and continents. As a result, contagions like Madoff or Lehman can spread around the world touching families everywhere. Indeed, family wealth worldwide has been battered by a "perfect storm" of economic volatility, credit tightening, fraud and bank failure. Borders and jurisdictional boundaries have protected no one. Nor is it likely that laws in a single jurisdiction will be effective to protect global wealth holders in the future.

Contagion can be contained only when each wealth holder puts in place protection for his wealth. That framework of protection is enshrined in the Principles and includes recognition that trust is only the beginning: processes to govern human nature and to ensure a design that can insulate in crisis must follow. The framework cannot be rooted in distrust if we are to live in a world, but can be grounded in objective and sound process.

Lowenhaupt Global Advisors and members of its Global Council intend to help our clients adopt and comply with the principles. *We encourage other trusted advisors and service providers to join us for the good of their clients.*

The Principles will likely lead to standards developed by Trone, who has experience designing standards for fiduciaries. Those standards (after a period of public comment) will likely be adopted by national and international certifying agencies and serve as the basis for education, auditing and, ultimately certification, of private wealth holders and their advisors.

Consider the family with a family office run by a competent staff of professionals. This family recognizes the solidity of the Principles and the benefits to themselves and others in adopting them. The family office can then be trained and audited in the Standards and even certified as compliant, thereby giving all family members the peace of mind that best practices are observed. The client of a lawyer, an accountant, a bank, a multifamily office or another trusted advisor can determine to follow the Principles and direct those advisors to adopt the Standards and adhere to them, subject to independent audit under clear guidance.

Here and now

Individual by individual, the rebuilding of 2009 must start with the design of process around Principles that will protect wealth holders in the next crisis. The Principles must be articulated so that they are available to every family member, every trusted advisor, and every provider of services and they must become the foundation for all decisions relating to the management of the family wealth. They are the best practices for the individual wealth holder, the "fiduciary practices" and more for the trustee or the foundation director, and the rules of stewardship for the family office or anyone responsible for the family's wealth.

The Principles benefit the community of those who own and provide advice on private wealth. Their adoption by wealth holders throughout the world can protect against wealth-wasting disease the way vaccination protects against small pox; if uniformly adopted worldwide, the Principles may even eradicate contagions like those that have brought us to the present crisis. Wealth holders can then place their trust in systems and processes that can be monitored and audited and certified -- and *then* they can then lead their lives as they want without the need for constant vigilance and the fear of collapse or fraud in a wealth-management program.

Now is the time for thought and action. Only when wealth holders shoulder the responsibility of protecting themselves by adopting the Principles can we put an end to reckless and self-serving behavior of those entrusted with serving private wealth and, in so changing the face of private wealth management, ensure peace of mind. - FWR

The illustration for this column is a detail from a Japanese woodblock print in the Charles A. Lowenhaupt Collection.

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