

Udders and Herds

By Stuart Lucas

Cows have played a central role in our family's lore for over a century. My great grandfather founded the Carnation Company in 1899, and it remained a family-led business for three generations. A cartoon drawn over 40 years ago, now hanging in our summer home, depicts my grandfather, when he was CEO, milking a cow. Instead of milk, dollars are flowing into his pail. Underneath, the caption reads "All I have I owe to udders".

The cartoonist was only half right. Carnation's slogan was "Home of Contented Cows". Our family relied on and served those "suppliers", as well as the firm's customers and employees. Collectively these key constituents of the business's success are the "udders" to whom the cartoonist refers. But, the family was definitely not milking the cow, at least metaphorically. Through representation on the Board of Directors, senior management, and deep into the organization, we were feeding and caring for cows, strengthening the herd and helping it grow stronger and larger. That's what made Carnation so successful and what built our family's fortune until the company was sold to Nestlé 86 years later.

Successful family controlled businesses like Carnation have clarity of purpose that is respected in the marketplace and is the basis of their stakeholder relationships. The family embodies the corporate culture and benefits from its visibility and acceptance in the marketplace. Family members involved day-to-day in the business develop experience and deep expertise in the work of the family company. This can reinforce competitive advantage. Wealth creation over years and decades is the result, but it isn't an end unto itself.

The cartoonist unknowingly identified a problem faced by many wealthy families. So often when family businesses are sold the family cultures shift from feeding the cow to milking it.

Selling the business and establishing a family office - or hiring a multi-family office to manage the family's wealth - risks a fundamental and potentially damaging change in the family's culture. No longer activist shareholders or active managers, they may become inward looking. The family's clarity of purpose can get fuzzy. There is no longer a public face or the threat of competition to hold the family accountable. And there aren't customers. The family becomes focused on outcomes instead of process, on being the customer rather than serving the customer, and on a time horizon for wealth creation measured in quarters rather than decades. How well is my financial advisor or family office taking care of me? How's my investment return so far this year? What's happening to my distributions? Am I getting my fair share of the family pie?

In my view, a multigenerational family culture should be all about empowerment to serve others, not about entitlement or ease. The simple fact is that it is as hard to maintain and grow wealth once you have it as it was to generate it in the first place. It is an uphill battle to generate returns robust enough to overcome the tug of spending, fees, taxes, inflation and numerical growth of most families. The math clearly shows that each generation must create a strong economic engine (or more than one!) and the means to manage it, or the wealth will erode.

But empowerment is compelled by more than math and money, it's about the satisfaction that comes from being useful. Who knows whether the next generation will have within it talented wealth creators who are invested in the family? Maybe there are wealth creators, but family dynamics or personalities will push them to work outside the family structure. Maybe there are great violinists, environmentalists, teachers or politicians, instead. Maybe there are simply quality people of average talent. But they can all address the question, "Am I useful?". If the answer is affirmative they are likely to lead fulfilling lives.

Building a successful family business, nurturing its growth, and selling it at just the right time make you an outlier. Producing multiple generations of wealth creators is even more out there. But a family culture

focused on human capital – talent development, risk taking, and an appetite for hard work – should be at the forefront of every decision the family makes, including the mission for the family office.

It's easy to lose focus. In study after study, the primary criterion wealth owners use to evaluate single and multi-family offices is customer service. Many family offices respond by delivering their investment and estate planning solutions in a highly personalized, though not necessarily efficient, way. Many also offer an array of concierge services. These can be as straightforward as teaching the next generation to balance a check book or getting tee times at prestigious golf clubs, but they often include personal bookkeeping for family members, private plane management, nanny services and oh so much more. These services threaten a healthy multigenerational culture.

Family offices counter that their clients demand this kind of personalized service, and clients are more loyal because of it. They may be right, but is that really what you want? At least Warren Buffett calls his private plane "The Indefensible".

"Wait a minute, Lucas!" I hear a wealth creator say. "I've worked long and hard to make enough money so that I could acquire these luxury services. Don't go telling me I can't have them." Fair enough. But don't saddle the family office with these responsibilities and don't build in the expectation that ensuing generations are entitled to them. Organize them separately, pay for them separately, and explain to your children that the family office doesn't do this stuff. If they want these luxuries, they had better darn well create their own economic engine, strong enough to pay for them.

If you are not careful, a family office, especially a multi-family office, will change your family culture in another way. A family office holds out the promise that it can maintain your wealth indefinitely so you can focus on other things. You no longer need the intellectual capital, the business resources, and mostly the hard work to keep a good thing going because they're doing it for you, in perpetuity. They may be right for years or even a few decades, but when it comes to multigenerational wealth management they are flat out wrong. Each generation of all but the very wealthiest families is going to need to create new economic engines, or perpetuate and grow existing ones, if they expect to match or exceed the wealth of their parents. It won't happen any other way. Don't let your family office focus you on the udder. Instead, use your financial security as an opportunity to strengthen the herd.

Some families try to maintain a culture of service by establishing a family foundation and promoting a philanthropic example. I think that is wonderful. But don't underestimate the power of a checkbook to turn you into a customer instead of a provider of service, even when your goal is socially responsibility. I encourage wealthy families to go a step further – engage in public service, too. As a public servant you have customers, as a philanthropist you are the customer.

My family has a several members in my generation who have demonstrated that they are wealth creators. Together, we make up our family's investment office. We have trained for our current positions over decades, we work hard, we have learned to work well as a team – and we offer no concierge services. Other family members work outside the office as a doctor, a teacher, a speech pathologist, a consultant. All of us are engaged in public service.

Ten years ago my generation, with my advocacy and full support, set an explicit goal for our investments of "maintaining real per capita wealth across generations". But now our children are starting into their teenage years and we worry that this message emphasizes outcomes more than process, being the customer instead of serving the customer. Our forebears built a strong herd. Our parents set a fine example. We've adapted it along the way to serve our strengths. It will be the next generation's challenge to strengthen the herd in its own way.

We are herders, not milkmen.

©2009, Stuart E. Lucas.