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What does it take to handle your legacy asset issues?

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Imagine that you have invested millions of dollars in a company overseas. Years go by and you have lost sight of precisely how the company is doing or what it is worth today. You receive a notification that the investment has been redeemed, or that the local government has taken over the company, and you cannot get a straight answer regarding what your investment is worth. How rare do you think these kinds of situations are?

It turns out that, in the family office world, these issues are very common. Stories abound of family offices wrestling with natural resource investments in China, property portfolios in Germany or fund managers in India. It is the experience of Emissary Partners that family offices are holding a silent asset class, typically in excess of five percent of assets under management (AUM), known as *legacy assets*.

In our experience across five continents, legacy assets around the world bear the same set of characteristics. A family office will hold long-term, alternative investments for which reporting has been inadequate and, more often than not, there will be a related party, possibly a counterparty or stakeholder, impairing the family office's exit.

The occurrence of legacy assets is a secular trend for family offices in the long run, linked to increased allocations to illiquid and international investments. And yet, some family offices are better equipped than others to resolve them. So, we ask the question: "What does it take to handle your legacy asset issues?"

What It Takes

We started our firm five years ago to help family offices better manage their global special situations and legacy assets. From dozens of mandates across five continents, we find three factors that make a family office well equipped – or not – to handle these challenges:

1

Family Office Environments Rewarding Candour

Legacy assets often pose complex choices. Does the family office decide to negotiate a redemption, litigate against a counterparty, sell a secondary interest or reposition the asset? Optimizing these choices requires an evaluation of facts that is objective and unemotional, and which may give rise to uncomfortable discussions.

Warren Buffett once wrote that "honesty is an expensive gift." In a family office context, honesty is only possible if (i) the principal rewards it, and (ii) there are decision-making processes that reward it. The courage required to voice honesty, and the potential positive impact it may have, both rise in cases of investment complexity such as legacy assets. If a member of the investment team, or an outside advisor, cannot speak directly about why a legacy asset situation has arisen, or what the choices and trade-offs entail, then there is a lesser probability of success in resolution.

2

Principals Who Take Deliberate, Calculated Risks

The archetype of most first-generation family office principals is one who takes a series of calculated risks, often over the course of decades, and who builds wealth by winning in the majority of those calculated risks. Comfort with calculated risk, and acceptance that you may not always win, is inherent in building great businesses.

Many next-generation principals feel a very real imperative to show that they are responsible stewards of the family office, which can lead to a mindset of perfectionism. A mindset of perfectionism is akin to taking an academic exam, aiming for a 100% success rate, and looking to minimize the number of answers that are wrong. Wanting not to make mistakes, however sincere, can run in tension with the imperative to take deliberate, calculated risks, in managing the portfolio which resolution of legacy assets requires.

3

Investment Team Integration of Non-Financial Capabilities

Untangling legacy asset situations requires skills including and beyond financial analysis, which together we call "Emissary's Five Lenses". To make sense of an ambiguous situation around a cross-border investment, and to know how to make responsible decisions, a board or fiduciary will also want to understand the investigative, legal, geopolitical and reputational considerations. However, most family offices, certainly those below $10 billion in assets under management, tend not to have internal capacity to deal with the latter four elements.

As investment footprints grow globally, the Five Lenses will become even more important for members of family office teams. Family offices can either hire in these skillsets or work with external firms, such as Emissary, as a trusted partner. Skills development can also come in the form of executive education, with business schools such as Oxford's Saïd Business School offering courses on global and non-market strategy.

Our readers may wonder why we do not cite as decisive factors governance best practices or sophistication in managing global investment risks. The truth is that family offices of all shapes, sizes and structures can be successful in handling global challenges in the portfolio; what is ultimately decisive is the underlying mindset and whether a family office team can make room for candour, calculated risk, and the Five Lenses.

Isolated Experiences, Shared by All

From conversations with over 200 family offices in the last five years, we find that over 80% of family offices acknowledge experiences with legacy asset challenges. Family offices wrestling with these issues should know that, even when these situations may feel isolating, the experiences are shared across the family office sector.

Our work at Emissary Partners helps family offices to problem-solve these esoteric cases, working through complexity to achieve exits and realise value. Most rewarding in this work are the deep relationships of trust that we build and seeing our clients empowered to achieve their goals. Please be in touch if you ever wish to discuss your potential or actual legacy asset issues.

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For more information, please visit www.emissarypartners.com.