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Private Wealth

ADVISING THE EXCEPTIONALLY AFFLUENT

FAMILY MATTERS

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CRAIG SMITH AND MICHAEL TIEDEMANN
OF TIEDEMANN WEALTH

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FAMILIES FEUD OVER BAUBLES
A PATH TO FAMILY HARMONY

Family Matters

Tiedemann Wealth Management was forged by people who wanted to sit on the same side of the investing table as their clients.

BY CAREN CHESLER

PHOTOGRAPHS BY BILL BERNSTEIN

When Carl Tiedemann's grandfather, an executive for American Tobacco, died in 1932, he left his family $100,000 in a trust. By the time Carl inherited the estate in 1972, the assets had been maturing in a bank for 40 years, enough time to have grown and matured into a small fortune. The trust's worth instead? Still $100,000.

Tiedemann was working on Wall Street at that point, and for about 20 years he had been trying to force the corporate trustee to invest the money in common equities and to be less restrictive with it in general. Until then, most of it had been invested in deferred equities or preferred stock.

"He had a very personal and very frustrating experience with how the traditional trust structure managed assets," says Carl's son, Michael Tiedemann.

Carl's own father, who had a horse blanket business in Cleveland during the Great Depression, died in a tragic accident when Carl was just 3. His mother moved the family from Ohio to New Jersey and married a war hero. The family lived far more modestly than it had when Carl's father had been alive, but his stepfather, who had driven an ambulance during World War I and had been involved in several rescue missions, would regale Carl with stories of war and heroism, and Carl was determined to work hard and become successful, says Michael Tiedemann. He saw Wall Street as his path to doing that.

He started a small broker-dealer called Stone Webster. In 1962, he joined the brokerage Donaldson, Lufkin & Jenrette and became its sixth partner. He rose through the ranks and eventually became its president in 1975. When he left the firm in 1980, he founded one of the first hedge funds, TIG LLC, when Julian Robertson was starting his first fund.

"He was always a visionary," says Michael Tiedemann, 44. "He will look at what is needed in an industry and see there's a real need for it and talk to people to confirm that [thesis], and then he'll take the entrepreneurial risk to make it happen."

Which is how Carl came to start Tiedemann Wealth Management in 1999. Well into his 70s, he still saw the need for a trust company free of conflicts of interest—one that did not have any proprietary mutual funds or in-house inventories of stocks or bonds, a firm that did not make commissions on the products it sold to clients. He started a firm that would instead hire outside money managers, the best for every asset class, and essentially sit on the same side of the table as the clients—in some of the very same investments.

"Back then, the term 'open architecture' was not an embraced term or business model," Michael says. "Today it is. And it's the model most wealthy families are seeking, and most businesses that start up use that as their investment platform."

Carl, who is now 89, also wanted to ensure that any client who took on his firm could fire it just as easily. In the past, beneficiaries had no power to remove a trustee—something he knew only too well because his family's trust had gone from one bank to another as the institutions were bought and sold. The family was unable to take its money elsewhere.

"He felt as if the assets had just been orphaned, and they had no incentive to perform," Michael says.

When he started the firm, Carl brought in Michael, now 44, who had been working in emerging markets through much of the 1990s at Banco Garantia, a Brazilian bank. Michael says that while his friends were enjoying the tech bubble in the U.S., he was getting an education in rolling devaluations, first in Mexico, then in Asia and Russia and eventually in Brazil.

"I grew up learning how to invest in wildly volatile markets," he says.

The firm eventually brought in Craig Smith, a trust and estate lawyer-turned-wealth advisor who ran J.P. Morgan's trust, estate and transfer tax planning services for the New England region. Carl has since retired, and Smith, 52, is now president.

Tiedemann Wealth Management has since its founding grown to 55 employees, 14 of them partners. It has about 140 clients, each with some $60 million to $70 million in investable assets. In total, the firm has $9.5 billion in assets under advisement.

The firm boasts a sterling investment committee roster with executives from such firms as Goldman Sachs, Warburg Pincus, J.P. Morgan Chase and State Street Bank and Trust. But Michael Tiedemann also boasts about his firm's deep bench of fiduciary tax experts and estate planning lawyers. After witnessing all of the consolidation in wealth management in the late 1990s, where service, even at well-respected firms like J.P. Morgan, suffered as banks merged and sought to improve margins, Tiedemann's founders wanted to offer something different.

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That means each family's global financial picture is thoroughly evaluated when they come on board. Not just their assets and estate plans, but all of the insurance structures they have (or don't have), their commercial banking relationships—essentially all of their intertwined financial relationships.

The firm's professionals work with a limited number of families to give them more responsive, proactive service. Michael Tiedemann likens it to a family office model.

"In many of those cases, the [client's] company and its key staff, such as the CFO, had been essentially acting as a family office for the family, providing needed liquidity, managing invested assets and overseeing tax compliance and estate planning. Once the company is sold, the family is faced with a void," Smith says.

At that point, Tiedemann steps in and helps the family transition from company wealth to managed wealth—educating the family about what spending and lifestyles their portfolios can now support; helping the family create and manage those portfolios; and helping them manage trusts and other structures whose once illiquid private company holdings have changed into liquid assets.

Michael Tiedemann

Most of its clients are at some point of transition. They might have experienced death or a divorce or transferred wealth to a new generation. But most typically sign up when they are selling a private family company. Such clients want their wealth advisors to assess their situation and come up with a new plan for the management of their assets and estate, addressing all the tax and accounting issues that may arise, says Smith.

Given its specialty of clients in transition, Tiedemann Wealth Management opened a five-man office in late 2013 in San Francisco, where there are not only a lot of suddenly liquid

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—CRAIG SMITH

technology executives, but also a lot of private equity investment opportunities in which that cash influx can be invested.

The dollar amounts Tiedemann allocates to money managers in Northern California with access to venture capital deals and other opportunities at this point are “very meaningful,” says Spencer Edge, 35, a partner and senior member of the firm’s investment team. Edge says Tiedemann sees the Bay Area as a hub of innovation and entrepreneurialism, and that can make for highly profitable investments.

“Having a perspective that’s outside of New York is beneficial to our clients,” he says. “Clearly, out here we’re on the doorstep of Silicon Valley, where much of the venture and growth capital investors are based, so many of the firms we work with are based out here.”

San Francisco is also a gateway to Asia, where the firm sees a lot of growth evolving, Edge adds.

“This is very much an investment presence. That’s what we’ve always prided ourselves on, as a firm,” says Michael Yelverton, 39, a partner who runs the West Coast operation.

The firm finds most of its clients by word of mouth, getting referrals from other financial services professionals, from trust and estate lawyers, M&A bankers and lawyers and insurance professionals who deal with ultra-high-net-worth individuals.

“If they see us doing a good job for those families, they’re more prone to recommend us if they come across a family looking for a firm like ours,” Yelverton says. “What you will not see from us is a marketing effort. We’re not transactional. We’re building long-term relationships with our families.”

Adds Michael Tiedemann, “We’ve been around long enough and are of a certain scale and reputation that we tend to be introduced to people.”

What also differentiates the firm is its approach to clients, where each one is advised by a whole team of wealth professionals rather than one advisor.

“One of the phrases I hear over and over again when clients come to us from other institutions—and it’s something that frustrated clients in my J.P. Morgan days—is that their investment specialist or portfolio manager wasn’t having regular conversations with their trust advisor or estate planner or banker,” Smith says.

The firm’s analysis for clients, conducted by an investment review committee and an account review committee, also involves reviewing their other advisors, such as accountants, commercial bankers and lawyers, to make sure the clients' investment, tax, accounting and trust objectives are being met.

"We are not in the business of displacing trusted advisors," Michael Tiedemann says. "We partner with them. But we are another set of eyes overseeing the work that has been done. Families get a huge amount of value from a refreshed look at their estate structures and their flow of assets upon death because they've set these things up over time, sometimes with different lawyers, and invariably the underlying assets move, families change; there are a lot of moving pieces."

"We become the consummate collaborator," Smith says. "We can do whatever the client's other advisors don't do well." That also means taking stock of different accounts and tax strategies. "There's a lot of value in making sure the right investments are in the right pools."

While the firm acts somewhat like a family office, Tiedemann doesn't offer concierge-type services—booking restaurants or finding private chefs, for instance.

"It's just a bad business model," Michael Tiedemann says. "You recommend a dog walker, and the dog walker steals their stuff, you're liable."

The firm has whittled down the number of money managers it uses to 40 or 50. Tiedemann won't invest with a management firm if it doesn't understand how the firm is making money, or if the manager has its own broker-dealer or an inadequate auditor. Sometimes Tiedemann has a difficult time explaining to clients why it wants to pull out of a manager still doing well. But if Tiedemann's research and strategy teams say it's time to get out, the clients abide by that, Smith says.

"That discipline helped us avoid investments in funds like Madoff," Smith says.

The firm and its clients also largely avoided the financial crisis of 2007 and 2008—in part because of Michael Tiedemann's experience with the volatility of emerging markets.

Sensing a banking liquidity crisis was on the horizon, the firm starting raising cash (up to 20% to 40% of portfolios) and placing clients into short-term Treasurys and into money market funds with no counterparty risk. In 2007, the firm also created a pooled entity for its clients that invested in protective put options on the equity markets so that clients could have an asset in their portfolios that would profit if markets fell.

"We made some extremely binary investment decisions," Michael Tiedemann says. "And what I mean by that is, if there had not been a crisis, we would have been massively underinvested—and likely fired for sitting on piles of cash."

But their clients followed their advice, and the firm was right about the crisis. In fact, clients became so fearful about a market collapse that the firm had a hard time convincing them to go back into the market in the wake of that crisis. For instance, in the fourth quarter of 2008, the firm saw oil prices falling dramatically, largely because Lehman Brothers was the largest swap counterparty in the energy master limited partnership space, and its bankruptcy wrought havoc on many of the firms with exposure in that market. Tiedemann wanted its clients to take advantage of the market, but many were reluctant to reinvest at that time.

"What can't be underestimated is how difficult it was to convince our clients to invest in anything at that time," says Michael Tiedemann. "It was a very uncertain time. You didn't know where the bodies were going to rise to the surface. There was just carnage everywhere. And we had no visibility as to what was going on in any money organization aside from our own."

So the firm created its own partnerships to invest directly into MLPs. It hired a consultant, the foremost senior analyst at one of the very large money management firms, who essentially began to acquire positions in master limited partnerships so that the firm could gain exposure to the sector but also pick and choose which credits it wanted to hold.

Michael Tiedemann says, "We created our own partnerships because we had no visibility into closed-end funds and hedge funds operating in that space, because of the massive redemptions occurring across the money management industry."

Tiedemann has also created an exchange-traded index fund that identifies companies trading at a deep discount but poised to undergo some kind of change that's likely to improve the share price. Perhaps activist shareholders begin buying up the stock, or the company undergoes a change in its CEO or board, or maybe there's a share buyback effort or the sale of a non-core business. With the tax advantages implicit in an ETF, Tiedemann's clients receive the benefit of the rise in the share price without suffering the capital gains tax consequences.

"These are businesses that are out of favor, but they are generating a lot of cash flow. In 2013, Apple was on the list. HP (Hewlett Packard) has been on the list. They are names that have fallen to the level where the valuation is such that they become part of the portfolio, but there's an improvement in earnings, or a strategic shift in direction," says Michael Tiedemann. "But because it's considered a tax-free exchange due to the fact that it is an index rebalancing, you're not paying capital gains. That's huge. It reduces the largest cost of the investing over time."

Asked how this fits in with the firm's stated goal of steering clear of proprietary products, he responds, "The ETF was created exclusively because it solved for the biggest issue of managing a portfolio of names, and that is the tax rebalancing and gains that would occur over time. … The active management portion of the strategy [that] would generate tax bills over time was removed, which is of huge value over time."

Carl Tiedemann's goal was to create a firm that offered clients the customization of a small firm or family office while still having the depth and breadth in the investment process and the legal expertise associated with a large Wall Street firm.

"We've tried to combine the best of both worlds. And I think we have," says Michael Tiedemann.

Please note that certain facts and figures may have changed since the time of this May 2014 interview.