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Four Things to Know About Family Office Compensation and Talent

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In an increasingly competitive market for sophisticated and experienced professional and investment talent, family offices are seeking and applying new approaches to attract and retain top level executives. Transactional Tax Planning partner and chair Saul Rudo, Mergers and Acquisitions partner Tom Lamprecht, and Employee Benefits and Executive Compensation partner Mitch Pahl of Katten recently hosted Family Office Compensation and Talent panels in New York and Chicago with Linda Mack, CEO of Mack International, and Trish Botoff, Founder and Managing Principal of Botoff Consulting. In each meeting, we sought to assess and address common issues that family offices face in attracting and retaining executives and staff, as well as best practices that family offices are employing to meet the challenges of ever-competitive markets for good talent.

1. Competition for talent and impact on compensation

Family offices have not been immune to increased competition for executive, accounting and investment team talent. Heightened competition for key roles and competencies has spurred family offices to increase compensation for incumbents and candidates to remain market competitive. In a 2023 Botoff Consulting survey, 33 percent of family offices reported higher performance bonuses and 46 percent of family offices reported higher salary increases than prior year compensation actions. Notably, the family offices surveyed reported that these increases were not due to inflationary concerns but instead due to the strong talent market.

Key takeaway: Family offices have increased salaries and bonuses at a rate higher than the broader US market due to the competitive market.

2. Recruitment and retention: market demands

More than half of the family offices surveyed reported recruiting challenges in the past 12 months. The strong market for family office professionals is driving family offices to proactively define their compensation strategy to improve recruiting outcomes and to recognize and reward the value of employee retention.

Eighty percent of family offices report the use of annual bonuses, and nearly two-thirds have incorporated formalized annual incentive plans for executives. This has been in response to the increasing professionalism in family offices and provides more clarity of compensation opportunities in a competitive market.

Key takeaway: Family offices are increasing the use of formalized metrics and objectives in their annual incentive plans.

3. Long-term incentive (LTI) plan trends

The increased focus on professionalism, business sophistication and investment has increased the breadth and depth of demand for family office professionals. As a result, family offices have continued the trend of implementing LTI plans, with 59 percent of participants in Botoff's 2023 survey reporting the use of such a plan or plans. Family offices have the ability to tailor their plan designs to meet the long-term goals of the family with attractive long-term compensation arrangements for key employees. Of the family offices surveyed, the most common types of incentive compensation arrangements provided were deferred incentive compensation, carried interest and co-investment opportunities with fewer family offices offering profit sharing plans, phantom equity, phantom carried interest or operating company equity.

Family offices are incorporating well-defined performance measures to structure long-term incentives with scaled performance thresholds, as well as with a variety of vesting and award payout options.

Increasingly, family offices are implementing a variety of forms of equity for tax purposes, like a profits interest, which allows a family office to offer specific tax-advantaged options that would not be available to a corporation issuing equity.

Key takeaway: Family offices have adopted a variety of LTI plans, which are aimed to align goals and performance while promoting employee retention.

4. Most commonly used LTI arrangements

Deferred Incentive Compensation

- Incentive compensation that is based on longer-term performance and typically vests over time and pays out in the future
- Commonly used by family offices focused on oversight/management of family's affairs and/or investments; used for teams without investment/allocation responsibility and/or non-investment team members
- Can be implemented as a nonqualified deferred compensation plan, which will allow participants to defer payouts to assist with tax planning

Co-Investment Plans

- Allows participants to invest with the family, allowing access into deals with participants' financial contribution;
- Most commonly used by family offices with in-house public and private investment teams; plans often incorporate use of leverage
  - Leverage may be provided via loans, which typically have an attractive interest rate and are repaid from transaction proceeds

Carried Interest

- Provides participants with a share of investment profits typically in excess of a specified return, and frequently in direct and alternative investments such as private equity, venture, hedge funds and real estate; no "one-size-fits-all" model—pools range from 10 percent or less to a traditional private equity level of 20 percent
- Most commonly used by family offices with a private equity function; firms employ both real and synthetic plans

Key takeaway: Family offices vary long-term incentive arrangements with the strategy and goals of the family office.

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