DJ Van Keuren: Welcome to the U.S. Family Office Real Estate podcast. This is DJ Van Keuren, with the Arsenault Family office, for U.S. Family Office Real Estate.

And today we have with us Ben Smith, who is a partner for Plante Moran Real Estate Investment Advisors. They're a family office and institutional asset manager and real estate advisor. Ben, thanks so much for being on the show today.

Ben Smith: Thanks for having me, I appreciate it.

DJ Van Keuren: So, why don't you tell me a little bit about Plante Moran.

Ben Smith: So Plante Moran is actually I think now the 11th largest accounting, tax, and consulting firm in the U.S. Obviously we focus on our core business of accounting and tax services, but one way that the firm's differentiated itself, really over the last 25 or 30 years, is to provide boutique consulting services to our clients. And so that would entail a variety of things including wealth management, trust banking services, IT consulting, and obviously real estate, which is where we sit.

DJ Van Keuren: So, how ... is my understanding from some conversations that we've had in the past, that this division was, seemed to be borne out of necessity, more than anything. Can you tell me a little bit about that?

Ben Smith: Yeah. So when I joined the firm just about 10 years ago, the real estate advisor services we had were limited to really, what we call corporate real estate services. So our clients were organizations or businesses that [inaudible 00:02:07] occupied real estate, as a necessity to support their core operations, which were not real estate.

Really about five years ago, or maybe a little more, we noticed an opportunity to provide services for real estate investors; meaning folks who own real estate for the purposes of achieving a return on investment or diversifying an investment portfolio, but who may not have that expertise in house.

And so, right about the time the idea came to fruition, we merged with a firm in Chicago called Blackman Kallick; and that firm had a fairly substantial family office advisory practice. And so that kind of aligned and we formed the new [inaudible 00:02:51] real estate advisors to focus on providing services in the investment real estate space to those family office clients and again, some institutional clients as well.

DJ Van Keuren: So then what type of ... what would you say the percentage of allocation that you see that families have toward real estate; and have you seen that increase with you guys coming into the fold and working with these families when you introduced your division?

Ben Smith: So it really runs kind of a wide spectrum, DJ. We've seen some portfolios [inaudible 00:03:29] no real estate and that's a different story. But for those that do, it could really run from anywhere from 10% all the way up to, we've got some clients that are north of 40%. Typically, you know, the kind of average might be 15 to 18% in real estate. And part of our role is to work with other groups within our firm, or other outside advisors to help a client develop the appropriate diversification strategy.

So if we look at a portfolio that's too heavily weighted towards real estate, we may advise the client that they need to diversify some of those holdings actually, and reduce their exposure to real estate. Our objective is to help our clients [inaudible 00:04:11] investment portfolio and then oversee the [inaudible 00:04:14] component.

I will say that over the last couple years especially as the market has performed well and frankly outperformed stocks and bonds, there is a much greater interest in increasing real estate allocations. So we have seen that and we help clients do that. Another kind of tranche of our client base would be again clients who have no real estate exposure but would like some. And so we'll help identify what the right strategy is for that and help build that portfolio.

DJ Van Keuren: So then what type of investments are you doing with these families in real estate? Is it funds, is it managed accounts, is it joint ventures, is it direct? Where are you recommending and what are you seeing when you're meeting with these families that may have existing real estate?

Ben Smith: So, the majority of our clients ... well first of all, we really employ more of a separate account strategy; meaning we don't typically co-mingle multiple families into one investment pool. We do do joint ventures, but primarily our family office is that we assist our direct investors in direct real estate investments; with more often than not, their allocation, they will have investments in different funds, their syndicated vehicles for real estate, and we'll provide insight and advice on those, but those don't really require the active management and asset management that a direct investment would require.

So I guess to get back to your question, again the majority of our clients are directly invested in real estate assets that would comprise their real estate portfolio. And again with that said, we have another, I would say 20% of our clients who are providing equity to a sponsor, where it's [inaudible 00:06:15] ten deal, or a 95/5, where the sponsor goes and actually serves as kind of the operator; but our client provides the equity and we underwrite those investments, and then oversee our client's interests in those investments.

DJ Van Keuren: So then that would be in the capacity like an asset manager for overseeing those? Those assets?

Ben Smith: Absolutely. So our job is to again, as you pointed out, oversee our client's equity investment in that real estate transaction; and then to report on it, and serve in that role as sort of the fiduciary for the client's investment.

DJ Van Keuren: You know, being from a real estate family office myself, and being intricately involved in real estate for about 15 years now, I really don't think people understand the complexity, you know, that's involved in real estate, when you're dealing on a direct basis; that I think a lot of times, people feel, "Well even if I buy a good asset and I lease it up, that's it." You know? I don't have to worry about it, it doesn't have to be there. That's not necessarily the case, is it?

Ben Smith: No, it's not. Everyone looks at real estate as an opportunity to maybe enjoy greater returns than you might see with stocks or bonds or similar other investments. But what they don't often realize is it's a very active asset class and it requires active strategy, it requires really day to day oversight, and family offices like yours have those capabilities internally.

A lot of our clients and other families don't, and so that's where we can come in and help them; that's our day job, so to speak. That's kind of what our expertise is in, and providing that service is, we think, pretty valuable for those clients.

DJ Van Keuren: So then, I have to ask you, you know - what are some of the mistakes that you've seen family offices make with their real estate allocation? Or their portfolio?

Ben Smith: Yeah, I think you touched on it with your last question a little bit. The number one mistake we see in our clients is going into, or sort of entering the real estate space without a strategy. You know, we look at every building, every investment as a small business, or in some cases even a medium size business. And you wouldn't buy a business without a very thorough underwriting, and a very well thought out business plan that you actively monitor and modify. You shouldn't do that with real estate either.

And so again, the number one mistake we see is just kind of think you can buy a building, lease, you're done. The example I love to give is we took over asset management of about $100 million portfolio that was actually cashflow negative, so our first order of business was to kind of get in and figure out why that was. And it was really a turnaround process from there that took about two years.

But some of the questions we asked when we went in, they owned a 60,000 square foot office building that was 20% occupied by one very credit tenant. That tenant happened to have a lease that was expiring in two years, but they had a termination option that was currently active.

And one of the questions we asked was, "So what's the plan if they terminate or if they don't renew?" And there was no answer. We said, "Okay, well what's going on in the market right now that would help us understand, if they do leave, how long is it going to take to lease up the vacant space? What's our tenant improvement cost going to be? What rental rates can we get? And what's the business plan surrounding that?"

And there wasn't one and that's not to lay blame on the client; that's not their core business, that's not their expertise. And so we went in and that's kind of the microcosm of how you build that strategy and proactively kind of think through the issues ahead of time.

I think the other misstep we've seen is sort of in the management side of things. You know, real estate is a dynamic and a fluid industry. Things change; things change based on local market dynamics, they change based on macroeconomic factors, and managing to those factors and constantly modifying your strategy is absolutely key to success.

And I get that ... I would add to that, maybe especially in a family office situation, transparency, reporting, things like that are very, very important, just to keep different stakeholders in alignment and make sure that everyone feels as though they're going in the same direction.

DJ Van Keuren: So then how much participation do you require the family offices to take part in this allocation in the real estate when they work with you? Do you have an option where they can say, "Well we want to be pretty involved. You know, we want to be just updated, you know, 'Hey Ben, you guys are specialists, you go do your thing and just tell me how it's going and just report, et cetera,'" how do you work with family offices in that capacity?

Ben Smith: Sure. So for our particular [inaudible 00:11:48] organization is a non-discretionary asset manager model. Where we don't make decisions, we don't take custody of assets because frankly that's not our role, how we structured it.

Our role is to provide the expertise and make recommendations that allow our clients to make the most informed decisions that they can. And hopefully they follow our advice, but ultimately, at a minimum, we'll ask the client to be involved enough to understand what's going on and be able to choose to take our advice or not to take it, and understand the implications of the decision.

We also have [inaudible 00:12:29] frankly that are very sophisticated real estate investors that are looking for maybe not a full asset management package of services, but maybe they're looking for help underwriting an acquisition, or sourcing data or equity, or working through some kind of complex loan workout or partnership issue; and in those cases we'll bill to take our services off the shelf and help them with a specific task, and they're handling things more internally from an asset management standpoint.

DJ Van Keuren: So then would that be, you know, more like as a, you said, it'd be more off the shelf. Would that be based on an hourly basis, would that be based upon the project itself? I mean, obviously Plante Moran being an accounting firm, I would imagine that they charge on an hourly basis, et cetera. So how do you go about those off the shelf services?

Ben Smith: So for the most part, if we're providing an off the shelf service, it would be either on a fixed fee or on an hourly basis. Wherever we can, we really prefer to value bill; and by value bill I mean we want to create value and then capture a portion of the arbitrage that we created as our fee. And that way everybody feels good about. And that sometimes makes sense and that sometimes [inaudible 00:13:52]. So we kind of take it on a case by case basis and really think about what's best for the client and their situation.

But I add to that actually to that almost all of our relationships with our clients start with some sort of consulting or hourly assignment where there's some problem that needs to be solved, whether it's with an existing portfolio that isn't performing, a specific asset that has a problem, a loan that needs attention, or something along those lines.

And so those types of engagements will typically be, again either fixed fee or hourly. And then if it leads into something bigger, we look at [inaudible 00:14:31] percentage of assets under [inaudible 00:14:33] fee structure. And you know, occasionally it makes sense to go back and look at some of the previous work done, and roll that into the fee structure as well.

DJ Van Keuren: So basically what I hear you're saying is that the families are having an opportunity, to after they tell you where they're at, and you guys are basically gathering this information; you're able to come back and say, "This is what we see. This is what we recommend." So that they're actually able to see where your thinking is, the direction that you're going, how you feel you can help. And then from there, they're able to make an educated decision on if they feel that you guys can help them move forward. Is that safe to say?

Ben Smith: That's exactly right. And those types of projects can range from, you know a $400 million partnership dissolution and loan workout, all the way down to, we recently helped a client who was a minority partner in a single office building and there was a capital call that was made and they just weren't sure whether it was appropriate for them to make the capital call or not; they didn't know if they were being treated fairly. And so we did a quick assignment to help them make an informed decision on that capital call. So really we're kind of a, no job's too big, no job's [inaudible 00:15:54], for lack of a better term; we're really more interested in developing relationships and thinking about things from a long-term perspective.

DJ Van Keuren: Fantastic. Ben, we're going to take a little break here, and then we're going to come right back and I've got a number of questions that I want to go into and go over that I think would be extremely helpful for any of the family offices or people that are listening to this podcast. So we're going to be back in one minute with Ben Smith from Plante Moran.

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DJ Van Keuren: Welcome back to usfamilyofficerealestate.com podcast. Today our guest is Ben Smith, partner with Plante Moran Real Estate Investment Advisors. We're talking about real estate and family offices, and the services that they provide, and how they help families with their allocation toward real estate. Ben, once again, we're happy that you're here with us today.

So I want to continue with some of the questions that we were going over before. So you know, what would you say ... you talked about how you guys will come in and you'll help assess the situation with their current holdings, and what they're trying to accomplish.

One of the things that when you take over their assets or you manage their assets for them, there comes up questions that have ... of how do you handle governance issues and reporting for your family office clients?

Ben Smith: Sure. I think that's a really important question, and it's something that we spend a lot of time focusing on. Again, when you're dealing with a family office environment, there's often multiple generations, there's multiple levels of involvement with the portfolio; and having an unbiased reporting and governance mechanism really helps avoid some pitfalls and some conflicts, both at that time and potentially in the future.

So we have a pretty defined reporting [inaudible 00:18:41] where we provide quarterly reports; and those reports roll up into an annual report. And at the annual report delivery, we revisit the strategy from the previous year and we review the results, and see how that matches up against the strategy. And then we realign the strategy for the following year, memorialize it, and revise our asset and portfolio level business plans to reflect that strategy.

Mechanically how that works, we happen to use two systems; one is Yardi and one is ARGUS, ARGUS enterprise. And those are fairly standard real estate industry tools. The Yardi system is sort of the, I'll call it the collection point for property level data, all the way down to what bills were paid, what rent was due, what rent came in, where are there variances, and that really feeds kind of the returns and the numbers from an investment perspective; and that's when ARGUS comes into play.

So the property manager on the ground will input data into Yardi, telling us what's actually happening. We'll take that Yardi information, roll it into ARGUS, and look at it from an investment perspective. And then between the Yardi and the ARGUS reports, those actually inform our quarterly reports to say, "Hey, here's how the property's performing, here's what our business plan was. Here's where variances are happening and here's why they're happening."

And then probably the most important piece is, "And by the way, here's what's happening in the market. Employment's going up, these are the industries that are growing, here's where we see risks, here's what's happening with the property; you've got these leases maturing, or you've got a loan coming into maturity in six months and here's the strategy for it."

Again, those quarterly reports are delivered in person, and we meet with the client and walk through those, and then they roll up into the annual report at an aggregate, and help us understand how our strategy did and think about what we need to do for the next year.

DJ Van Keuren: So then how many, with family offices that you take on as new clients, I would imagine that you probably don't see a lot of these reporting and the various supporting documents already in place.

Ben Smith: That's a correct assumption. I would say that they all have some form of reporting, but what we don't often see is a consistent format and consistent timeframe for delivery. And often it's very accounting focused. They'll have maybe an internal controller or CFO for the family office who is handling things through Quickbooks or Excel; and it works functionally, but it doesn't give a window into how we can take that data and use it to build and modify and refine a strategy.

So far more often than not when we meet with a new client, we will bring sample reports and deliver those and they're often very pleased by what they see and it's something that they find a lot of value in when we help them put that together for their own family office.

DJ Van Keuren: So then if you get a family that comes in, and let's say they have existing assets, do you offer to say, "Hey, we can evaluate these; we can take over the asset management upon this, as well as work on future opportunities and acquisitions." Do you allow those existing assets to come under you guys, or is it strictly on the new opportunities that you're presenting to them?

Ben Smith: Both. I mean, we more than welcome the opportunity to serve as an asset manager for assets that are already existing in the client's portfolio. One value that we hold pretty strongly to is that we want to help where it makes sense to help, we want to stay out of the way where it makes sense to us to stay out of the way.

So if things are running smoothly and the client is either managing things [inaudible 00:22:50] or they have a third party asset manager that they're happy with for those assets, and they want us to help build maybe a new tranche of the portfolio, we're happy to leave the existing assets alone.

If there is some reason that the client wants us to help oversee existing assets, then we're more than happy to onboard those; more often than not that is the case where we get brought in because something isn't working well with the existing assets, if they do indeed have real estate in their portfolio, and we have pretty defined process internally to understand and dig into the details of what's happening with existing assets, onboard those assets into our [inaudible 00:23:33], and either combine that with new acquisitions, or not.

DJ Van Keuren: So of the families that you guys currently manage, what would you say is the percentage of the families that buy a property for income, compared to someone that might buy a property for that value-add or appreciation that real estate can provide?

Ben Smith: So I would say probably 80% of our clients are in the real estate business, or have a real estate allocation, as more of a diversification tool, an inflation [inaudible 00:24:14], maybe for tax purposes. And so they have already built their wealth in either a previous generation or a different industry, and our job is to help preserve that wealth. So with those clients with that profile, you know again, we're going to trend more towards the core and core plus assets that are still going to outpace the stock market, but aren't going to necessarily going to shoot for a 25% IRR.

There is a component of our client base, again probably about 20%, who are more aggressive. And when we sit down and develop their strategy, part of our [inaudible 00:24:53] is to help understand the risks and [inaudible 00:24:56] associated with the more aggressive value-add investment strategy. And as long as everyone is understanding what that means, and accepting of the risks, then our job is to help them through whatever that investment strategy is.

DJ Van Keuren: Now when you say majority, about 80% are either core or core plus, can you give me an example of an asset type for that?

Ben Smith: Sure. So we ... I'll give you an example of a core asset and then what I would consider maybe a core plus asset. So we recently acquired a, probably about an 85% occupied, 7 building industrial complex for a client and they had credit leases, meaning the tenants had strong balance sheets, they had reasonably long lease terms left, and we purchased the asset with fairly low and conservative leverage. And so we're looking at a deal like that, and we're saying you're going to an eight, nine, ten percent return. I would call that a core asset. There's obviously risk there but it's mitigated and there's not a lot of turnaround or opportunistic characteristics of the asset.

Maybe a core plus example would be [inaudible 00:26:16] industrial asset that we acquired for a client where there was ... it was previously owned by a family business who had occupied the facility as their headquarters, and they sold the business to a private equity firm. The private equity firm didn't want the real estate, so the family retained ownership of the real estate and really weren't real estate experts; so there was some deferred maintenance, there were some site issues, and there was some vacancy in the building, and there was not a lot of term left on the leases.

So we went in, we underwrote that deal, and we said, "Okay, we really believe that these tenants are going to be here for a long time, even though they only have a few years left on their lease, [inaudible 00:27:00] facility or they've made substantial capital investment, and we think there's a low likelihood that they're going to leave.

So we acquired that asset, handled the deferred maintenance and the capex that was required. Cleaned up the site, negotiated with the tenants to extend their leases, cleaned up the vacant space, and leased that out, and because we were purchasing that asset with a little bit of hair on it, we were able to purchase it at a discount. And as we've added the value through lease up and addressing the other issues, both the returns and the value of the asset have increased. And so I would call that more of a core plus or even slightly opportunistic investment.

DJ Van Keuren: Got it. So you know, would somebody that comes to you, and if they were to ask you a question, to say, "Is it better to invest in the funds, or directly into an asset?" How would you answer that?

Ben Smith: I would say that it depends on what your objectives are. With a fund, you are going to have a much lower management responsibility, but your liquidity may be low, and that you may not be able to pull your money out exactly when you want. And you're going to have little or no control over what happens. So you're effectively [inaudible 00:28:20] a commodity [inaudible 00:28:22] you hope to earn a return on. So if your goal is more passive investment and you don't want to have the cost or the time associated with active management, then that fund approach or that syndicated investment approach might make more sense for you. With that said, there are still fees and costs associated with those investments, they just may be buried within the returns.

If you desire something that you have more control over, that you can have more flexibility in extracting equity and so forth, then perhaps more direct investments [inaudible 00:29:01] make sense for you; but you need to understand, again as we talked [inaudible 00:29:05] beginning of the podcast, that the management time and the strategiC approach that you needed to take to make that successful.

And again, to go back to my point about liquidity, I want to kind of reiterate that real estate is not known as a liquid asset; so I don't want to set the expectation that if you have a direct real estate strategy, you can take your money out at any time, because that's certainly not the case, no matter what type of real estate you're in.

DJ Van Keuren: Right. So what would you say to a family office that has no real estate allocation in their portfolio? How would you go about that if they told you that and they said, "Yes we have no allocation whatsoever to real estate?"

Ben Smith: Yeah, I think the first thing I would ask them is "What are your investment objectives?" And depending on how they answer, I might say, "You know what, you're absolutely right. You shouldn't have a real estate allocation." If they are looking to, I use the term coupon clip, and their return objectives are not high, and their risk tolerance is very, very low, and their desire for management time and expense is non-existent, I might actually say that real estate isn't the spot for you.

I would advise them [inaudible 00:30:24] missing out on some of the benefits [inaudible 00:30:27] real estate and the tax benefits, maybe the succession planning component of real estate, the inflationary edge and so forth. But as long as they're educated on those factors, I might say that it's okay not to have any real estate.

If they told me a different story and said that they wanted to maybe have the opportunity for some increased returns, and their risk tolerance was not at the lowest level, I might suggest that we explore a real estate allocation and what that might look like. And again, if we were to go down that path, that real estate strategy might vary from very moderate return type of strategy to something different.

You might've picked up by now, I like to speak in examples. But we had a client who sold a business, had no real estate allocation, but had a pretty substantial tax gain based upon the real estate that was sold with the business, and wanted to defer that gain into a 1031 exchange. We asked him what his objectives were; he said, "I want to retire and I want to relax with my family. And I want to go collect a check every month."

So we actually employed a net lease strategy for that client and purchased a small portfolio of net lease retail assets that he could [inaudible 00:31:47] very limited management responsibility, that would provide a tax shelter and succession planning benefits, and a little bit higher return, but not all the intensity of a more active real estate portfolio.

DJ Van Keuren: So you said, I mean to me as you're walking through that process and your thought process, along with that example, that you guys really do take that advisory approach where with that initial conversation or analysis that you're doing with the families, then you're able to really take a step back and make the best recommendation possible from, after you know everything, rather than just coming out of the gate, which unfortunately a lot of real estate people do, is just buy real estate, buy real estate, this is what you need to do. And where you guys truly take that advisory and long-term approach with a client.

Ben Smith: Absolutely. I mean, our perspective on that, DJ, is that we strive for very long-term relationships with our clients. And the way we achieve that goal is to provide advice that we believe is in the client's best interest and while it might not provide us with the greatest fee or scope of work in the short-term, if our clients feel that we're working for them, then that benefit over the [inaudible 00:33:08] much greater. And so that's just the approach we take, and it's kind of how we're structured.

DJ Van Keuren: Well with family offices being really relationship-based, I could understand why you guys have been so successful in such a short period of time since you guys rolled out your real estate investment advisory area for Plante Moran.

So Ben, if people want to get in touch with you or learn more about the services you guys provide, and how you can help them, what's the best way to get in touch with you?

Ben Smith: So they can always visit our website, which is pmria.com, pmria.com. Or they can email me at ben.smith@plantemoran.com. Which is p-l-a-n-t-e m-o-r-a-n. Or they can call me direct at (248) 223-3275.

DJ Van Keuren: Great. Ben, thank you so much for being on today. Today we had Ben Smith, who is a partner for family office and institution asset management and realty advisory services. Ben thank you so much for being on today's podcast. We really appreciated your time.

Ben Smith: Thank you for having me. I enjoyed it.

DJ Van Keuren: Great. So this is DJ Van Keuren with usfamilyofficerealestate.com. Be sure to check our website for other educational information for family offices and real estate. From great podcasts like this, we had our guest Ben Smith with Plante Moran, and you can also get other information on the website from videos to articles, to information on a variety of ways in order to have real estate in your portfolio as a family office.

Thanks so much again Ben, and we hope you come in to our next podcast next time.

Ben Smith: Thanks. Take care.