

Wealthy Clients Love To Collect Hard-to-Value Assets

(AKA)

Those Ever-Special “Unique Assets”

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Anyone Know The Value Of This Collection?



How About This Collection?



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What The Experts Say

Collection 1:

Grouping of mid to late 19th century Yixing clay bowls is a nice example of worthy opium bowls from the late Qing Dynasty. The bowls are to be offered as lot 348 with an estimate of \$700 to \$900.

Collection 2:

<https://youtu.be/Ed8vJdlWbWs?t=238>

In Concept This Is Easy

- * Identify your responsibility
- * Identify the risks associated with the asset
- * Identify mitigating factors you can employ
- * Evaluate acceptance based on your corporate level risk tolerance
- * Determine asset management approach
- * Execute
- * Go home feeling comfortable

Understanding Your Responsibility

- * Read the documents
- * Understand the objective of the planning / Grantor intent
- * Nuances in language around responsibilities
- * Nature of our role: management, monitoring, custody
- * Who is responsible (someone needs to be)
- * Conflicts between documents (such as LLC operating agreement vs. Trust Document)
- * Impact on investment policy statement
- * Concentrations
- * Use of releases/indemnification and identifying the parties

Pre-Acceptance Reviews

- * Understand responsibilities in the documents
- * Identify any potential risk with the asset
 - * Inspect asset as appropriate
 - * Have environmental reviews completed as appropriate
- * Evaluate your internal or external vendors capabilities to manage the asset
- * Analyze ways to mitigate identified risks
- * Analyze cost of managing this asset and set pricing expectations
- * Accept or reject asset based on pre-acceptance review

Bringing In The Asset

- * Determine appropriate valuation
- * Insure proper titling and re-registration
- * Status of tax and other payments required
- * Proper insurance coverage obtained, including title insurance for real estate
- * Engage outside vendors / managers as appropriate
- * Collect physical assets and ensure they are properly stored and secured
- * Execute on any pre-acceptance review action plans

Annual Reviews

- * The post-acceptance review should be included as part of the first annual review (90-day review) for all assets in the account. Purpose: to evaluate if assets meet the account's investment or planning objective
- * Determine if the asset remains an appropriate holding for the account both individually and collectively with the other assets in the account
- * Analyze the financial performance of the asset
- * Ensure valuations are appropriate
- * Perform any necessary inspection that is required
- * Ensure Taxes and insurance are current
- * Documentation of the review, the decisions made, and the actions plans developed

Common Risks Among All Unique Assets

- * Valuation (statements, IRA's, buy/sell, gifting, how often)
- * Specialized accounting and tracking systems required
- * Family ties/desire vs. fiduciary duty
- * Generation 1 and Generations 2 and 3: ongoing desire to hold?
- * Litigation among family members
- * Non-productive assets (family home housing Generation 1)
- * Concentrations
- * Evaluating buy/sell agreements
- * Split interests and restrictions on sales
- * Evidence of ownership and reregistration
- * Highly leveraged assets
- * The desire to hold these assets in IRA's

Mitigation Of Common Risks

* Specialists

- * In asset management
- * In valuations
- * In legal specialties such as state law, family, fiduciary, small business, mergers and acquisitions, real estate, farm, ranch, mineral, timber, environmental, endangered species, art etc.
- * In alternative investments
- * In leverage
- * Specialized asset and attribute accounting and tracking systems

Real Estate – Which Property Would You Prefer To Manage? Why?



Real Estate – Possible Risks

- * Many property types present particular risks (grantor-occupied, residential, retail, office, agricultural, industrial, vacant land, etc.)
- * Environmental issues
- * Fiduciary impartiality (on all and among beneficiaries)
- * Disrepair
- * Personal injury and property damage liability
- * Impact on the rest of portfolio (asymmetrical risk)
- * Family vacation home vs. rental property
- * Statement carrying value
- * Rent collection
- * Out-of-footprint real property ownership

Real Estate – Possible Mitigating Factors

- * Environmental inspections (pre-acceptance)
- * Annual property inspections
- * Liability insurance
- * Taking beneficiary use into consideration
- * LLC to shield other assets in portfolio
- * Maintaining the property (repairs, taxes, mortgage)
- * Professional property manager
- * Appraisals
- * Specialized policy and procedures to insure compliance with regulations

Closely Held Business - Which Small Business Is More Risky To Hold? Why?



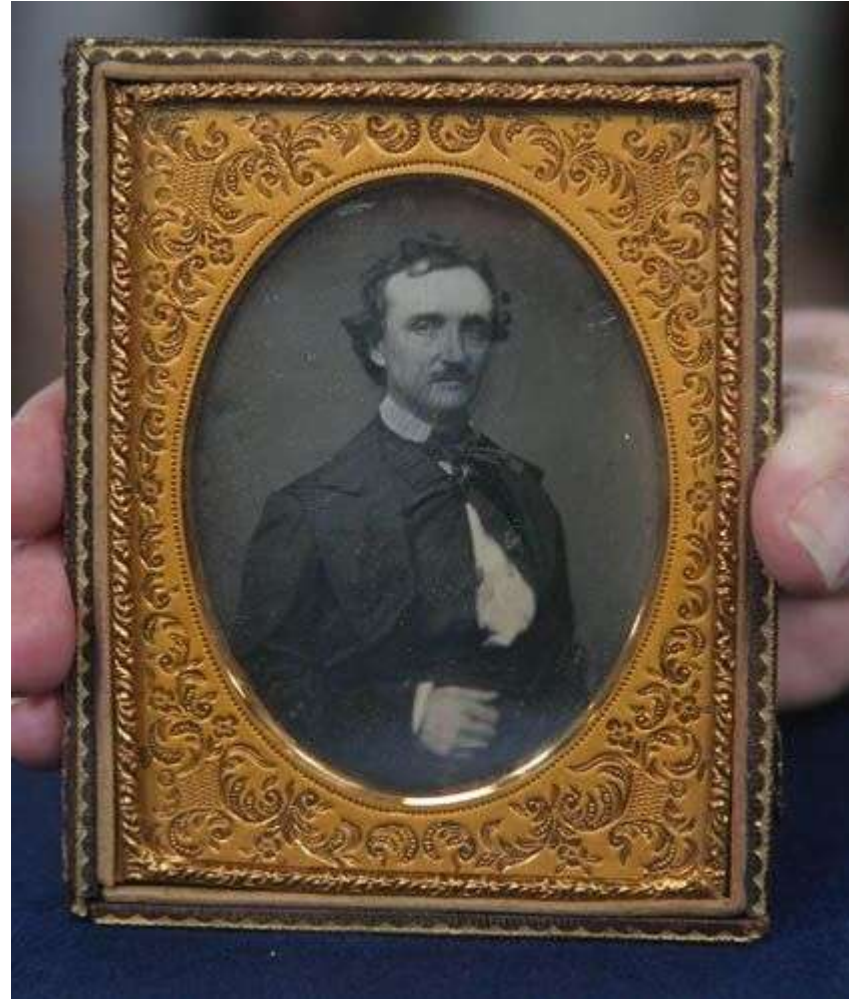
Closely Held Business – Possible Risks

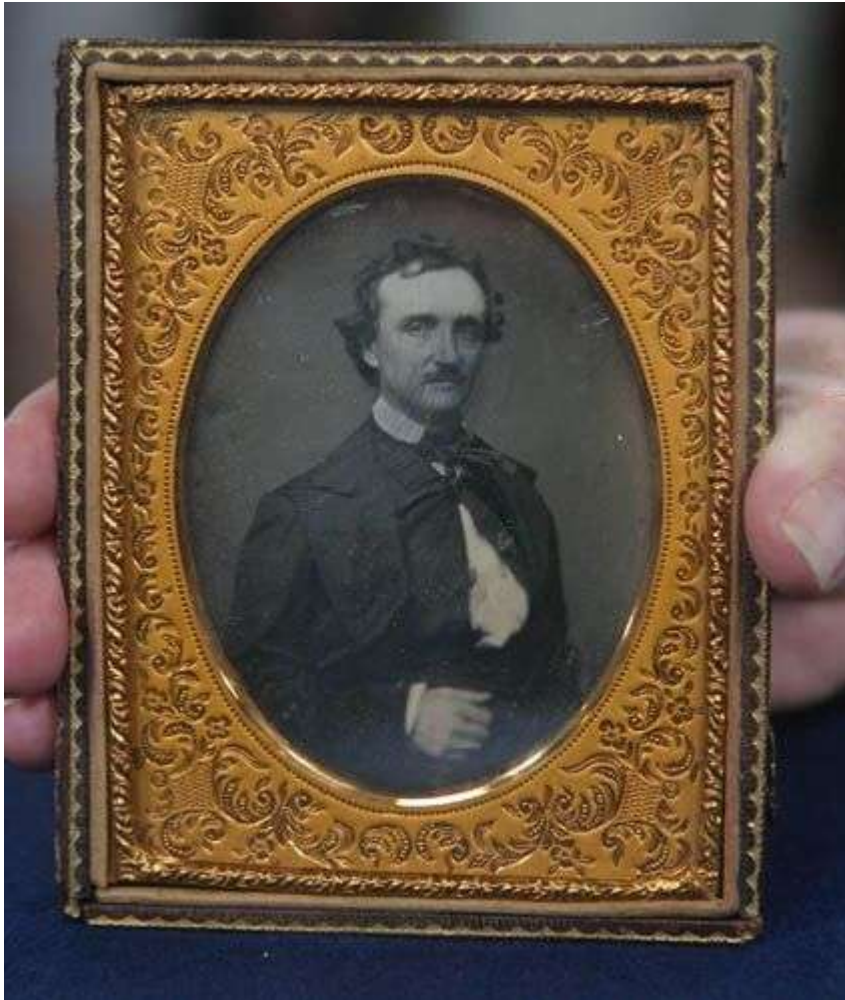
- * Conflicts in governing documents
- * Beneficiaries inside and outside the company
- * Majority/controlling interests and heightened oversight
- * Reputational impact of business
- * Multiple business forms with varying rights, liabilities and registration requirements (sole proprietorship, partnership, LLC, LLP, FLP, C-Corp, S-Corp, joint venture)
- * Minority/non-controlling interests and lack of influence
- * Buy/sell restrictions/agreements
- * Unique business risks (customer concentration, single driver)
- * Refusal by business to provide financial statements
- * Impact of BSA/AML, OFAC and Volcker Rules

Closely Held Business – Possible Mitigating Factors

- * Robust acceptance review of documents, the business, the family and the relationship among the three.
- * A process to insure appropriate information-sharing among beneficiaries.
- * With control, you may have heightened responsibility, which may include Board participation and weekly, monthly or quarterly reviews with management.
- * Annual asset reviews to keep current on the business performance
- * Buy/sell process: scrutinize it with assistance of knowledgeable professionals
- * In-house or contracted valuation expertise
- * Specialized policy and procedures to ensure compliance with regulations

Is This Valuable or a Picture of My Grandfather?





Rare Edgar Allen Poe Daguerreotype

As if a very old [photo](#) of author Edgar Allen Poe wasn't unusual enough, it turns out that this particular daguerreotype had been stolen from the Players theatrical club in New York City. What would have been the discovery of a new and important historical find (only a few original Poe photos are known to exist, according to appraiser Wes Cowan) ended up being the most famous theft-recovery story in *Roadshow* history. The photo from 1847, appraised for \$30,000 to \$50,000, has thankfully since been returned to its rightful home, in case you were wondering.

Notes And Mortgages – Possible Risks

- * Amortization accounting
- * Variable vs. fixed-rate accounting
- * Underwriting (LTV, ability to repay, interest rates, etc.)
- * Collateral, valuation, perfection, monitoring, insurance
- * Discretionary action vs. investment
- * Loan and delinquent-loan collections
- * Proper lending disclosures and parties with specialized rights (military)
- * UCC filings as needed
- * Impartial treatment of beneficiaries
- * Conflicts of interest

Notes And Mortgages - Possible Mitigating Factors

- * Specialized operations and accounting systems
- * Partnering with lenders in your bank
- * Loan/note documentation
- * Standardized note and process
- * Collateral appraisal, collateral custody or binding agreements, ongoing collateral monitoring and insurance
- * Investment policy statement or discretionary committees
- * Standardized collection process with specialists
- * Third-party lender documentation or policy against own bank lending

Ranch – Do You Know the Proper Care & Feeding Differences Between Baby Cattle & Pigs?



Farm – Do You Know Which Crop Fits the Soil & Environmental Conditions To Produce the Best Yield?



Farm and Ranch – Possible Risk Factors

- * Responsibility for the land and structures as well as crops and livestock production
- * Tenant Risk
- * Revenue collection
- * Cash lease vs. crop share lease
- * Environmental contamination
- * Illegal/controversial crops or livestock, creating potential legal/reputational risk
- * Highly specialized daily manager requirements
- * Insurance (liability, crop/livestock, physical structures)
- * Verification of revenue streams
- * Evaluation of government farm programs
- * Unique laws and regulations that impact operations

Farm and Ranch – Possible Mitigating Factors

- * Environmental inspections
- * Property and crop/livestock monitoring
- * Onsite managers that work for you (employees or contract)
- * Purchase of specialized insurance
- * Financial reasonableness analysis
- * Commodity hedging programs
- * Specialized policy and procedures to ensure compliance with regulations

Oil & Gas - Which Well Has More Revenue Potential? Can You Read Reserve Reports?



Oil, Gas & Coal – Possible Risks

- * Environmental damage
- * Specialty contacts with variable rights (land, royalty, working interests, etc.)
- * Specialized accounting and tax requirements
- * Verification of proper revenue streams
- * Liability for reclamation
- * Forced pooled land owner
- * Incorrect titling, resulting in suspension or escheating of funds
- * Unique laws and regulations that impact operations

Oil, Gas & Coal – Possible Mitigating Factors

- * Controlling the types of interests accepted
- * Upfront reclamation plans
- * Maintain staff or hire a consultant with industry-specific knowledge and specialized skills such as:
 - * Reviewing royalty checks (know terms of the lease)
 - * Interpreting reserve reports
 - * Land contract negotiations (drilling commitments, limited post production charges)
 - * Pro-active leasing and ensuring proper follow through)
 - * Searching for suspended or escheated funds
 - * Notifying purchasers to update records
 - * Monitoring dormant mineral laws
- * Revenue analysis and verification process
- * Ongoing monitoring programs
- * Overall written management plan
- * Programs to control the payment of taxes and insurance
- * Specialized policy and procedures to insure compliance with regulations

Timber – Where Do You Even Start?



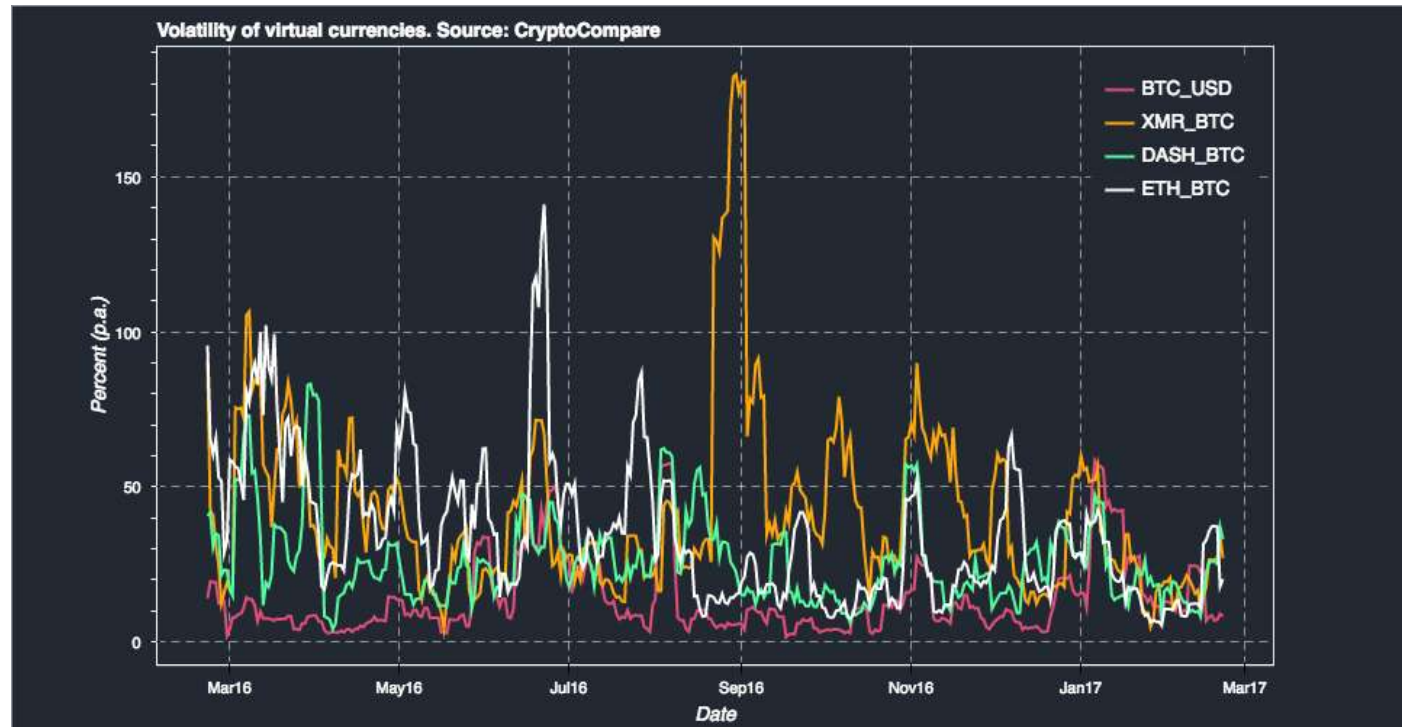
Why Timber



Timber

- * Combines farming and commodity risks
- * Highly specialized manager required
- * My opinion: no bank has critical mass needed to properly execute on the entire process, so we all need to hire professionals.

Soft Assets - Whoa – How Many of Your Clients' Investment Policy Statements Call For EXTREME Risk?



Soft Assets – Possible Risks

- * Soft assets include such things as: leases, virtual currency, patents, life insurance
- * Multiple variations of each asset type with unique characteristics
- * Thin, uncontrolled markets
- * Missed or underfunding premium payments
- * Missed Crummey notices
- * Lapsed insurance policies (insurability issues, higher premium)
- * Leveraged purchases
- * Cash-flow continuance
- * Potentially high price volatility

Soft Assets – Possible Mitigating Factors

- * Use only experienced, specialized brokers
- * Ensure systems in place to monitor premium due dates
- * Monitoring insurance company ratings
- * Review sufficiency of premium payments
- * Process to track and send Crummey notices
- * Monitor market developments germane to the asset
- * Review suitability of various assets types
- * Policies to exclude out-of-risk-tolerance asset classes
- * Plan for and monitor potential margin calls on highly leveraged assets

Hard Assets – Do You Immediately Recognize Value?





Patek Philippe Pocket Watch

A modern pocket watch from Swiss watchmaker Patek Philippe can already fetch quite a pretty penny. But a [pristine timepiece](#) from the brand dating back to 1914? That's *Antiques Roadshow* gold. The owner brought the treasure, which was handed down from his great-grandfather, to the show's stop in St. Paul, Minn. in 2004. Appraiser Paul Hartquist estimated the auction value at \$250,000, a total that was increased in 2016 to \$1.5 million.

Hard Assets – Possible Risks

- * Hard assets include: jewelry, art work, furnishings, frozen storage, boats, cars, guns etc.
- * Fakes
- * Proper storage
- * Lack of custody
- * Transportation
- * Specialized appraisal skills needed
- * Lending assets to others (artwork in museums)
- * Very small market

Hard Assets – Possible Mitigating Factors

- * Hire expert appraisers for each specific asset
- * Obtain a professional opinion on how to store sensitive items
- * Create a process to maintain control of titles and oversee any artwork loan programs
- * Specialized insurance
- * Bonded and insured delivery services -- if appropriate, armored-car service
- * Vault control over held assets
- * Required licenses or a licensed service (guns, marine, etc.)

Do You Know The Artist?



70s High School Art Project Mistakenly Valued At \$50K On “Antiques Roadshow”

An expert antiques appraiser who likened a high schooler’s art project to the work of Pablo Picasso and valued it at up to US\$50,000 (£35,000) has chalked up the mistake to a learning experience.



**When Your Appraiser is Wrong - Guess Who
The Fiduciary Is !**

Points To Ponder

- * Comptroller's Handbook on Unique and Hard to Value Assets is a good source to help identify risks.
- * Industry groups are a good source to identify best practices.
- * Coordination with the Reg 9 process and the account's investment policy statement.
- * Expertise required – “critical mass” dictates Internal vs. External.
- * Vendor management can be tricky.
- * The Bank's Board and Senior Management need to appropriately understand the risk in managing these assets and be prepared to invest in properly managing them.



Questions?