Center for Family Legacy

Private wealth vs. family wealth: A holistic approach to sustaining generational wealth

Successful wealth management can be positive and transformative for those who benefit from the wealth. However, in order to embrace these benefits, wealth management must extend beyond the private wealth. This sort of management requires intentional effort and preparation, which involves a focus on preparing the human capital for a life with wealth and setting up a framework to govern the family enterprise.

For the most part, private wealth management centers on financial capital issues, while family wealth management focuses on all three forms of capital: financial (the money); human (the individuals); and intellectual (the knowledge). Together, these three components form the family wealth.

Successful wealth management incorporates both private wealth and family wealth. We at the Center for Family Legacy believe that in order for a family's private wealth to have that transformative, generational impact, successful wealth management must extend beyond the money, and the fate of that money cannot be left to chance.

Build the foundation around financial capital

Let's start by defining private wealth. Private wealth represents the financial capital, whether that is actual dollars and cents or ownership in a family enterprise. This wealth represents all the hard work, time and effort a family leader employed to create the family fortune.

Growing and sustaining the family's financial capital—the private wealth—requires a focus on investments, tax and estate planning and risk management.

Take a multi-generational perspective

While it is essential to employ the best investment managers, accountants, attorneys and experts to guard the private wealth, from a multi-generational perspective, it is crucial to think beyond the private wealth, and incorporate the family wealth.

As stated earlier, family wealth is comprised of three components: the money; the individuals; and the knowledge. Families who wish to have the wealth transferred to future generations while also having a positive impact on those generations, must widen their focus from solely on private wealth—the financial capital—to include family wealth.

TRUIST

Wealth

Only 10% of families succeed in maintaining wealth beyond the third generation.[1]

This shift requires building a professional infrastructure to include the necessary advisors, technology, etc. to prepare the human capital for the roles and responsibilities necessary to successfully lead a life with wealth. This will also provide the necessary framework, guidelines and structures to govern the family enterprise.

The result will be well-prepared heirs who are better positioned to govern the enterprise by working cohesively for the common good of the family.

In summary, in order for a family's private wealth to succeed multiple generations, it is necessary to:

- Prepare the human capital
- Enhance the intellectual capital
- Build the appropriate governance framework

So why is all this important? It is widely known that wealth transfer beyond the third generation is unlikely. Only 10% of families succeed in maintaining wealth beyond the third generation.[1] Research uncovers a variety of reasons:

- Poor or no communication between generations
- Lack of trust
- Poorly prepared heirs
- Absence of a defined, agreed upon mission
- Multi-generational mathematics (i.e. exponential growth of the family vs. mathematical growth of the wealth)

This is where family wealth plays a significant role. Families who see beyond their financial capital to the importance of nurturing their human capital and intellectual capital will:

- Foster clearer communication among family members
- Build stronger family cohesiveness
- Create better prepared heirs

The result? An increased success rate of transferring wealth to future generations.

Build a professional infrastructure

The first step is to build a family governance structure, which is especially important for those families with shared assets and common goals. Family governance, at its core, is joint family decision-making. Unless there is an agreed-on principle around how the family will come to consensus about their combined assets/goals, there is the potential for a breakdown in the family. Consider:

- Are you investing together across the family with entities like trusts, limited liability companies or limited partnerships?
- Do you own a family business or manage commercial real estate owned by family members?
- Are you overseeing a family foundation or does your family own a shared vacation home?
- Do you want to keep the family connected and organized around common family traditions or a family retreat?

These are all situations that would greatly benefit from some governance on how to proceed and make decisions. Having an agreed upon process for working together often results in just what we are hoping to achieve: enhanced communication, which, in turn, reduces potential family conflict.

Clear communication provides the heirs with a better understanding of the purpose of the wealth, and gives them a voice in how the wealth is utilized toward the accomplishment of the family legacy. Ultimately, the process will prepare and educate future family leaders.

Over the years, by studying families who have been successful at wealth transfer, we have identified 25 best practices, which focus on the non-financial aspects of living a life with wealth. These best practices center on six areas:

- Family cohesiveness
- Governance
- Strategic planning
- Mentoring
- Philanthropy
- Trusts & estates

The family members are asked to rate activities that fall under these categories in three areas: the activity's importance; whether the family is practicing the activity; and the activity's impact on the family (i.e., from benefit to detriment). The family members and a facilitator discuss the responses and work as a group to create a prioritized action plan for adopting these practices.

One of the key best practices is centered on teamwork and communication. Communication is the platform from which every other facet of successful wealth sustainability is built. Creating a forum for open, honest communication allows each adult member to have a voice. Having regularly scheduled family meetings can provide that forum.

These meetings have formal agendas, take place in a neutral location and, often include a skilled non-family-member facilitator. This allows for all family members to gain an understanding of what they own and how their ownership will impact their lives.

In addition, this process helps clarify the part each member will play in developing and preserving the family legacy. In turn, this prepares the current and next generation for the important decision-making the family must engage in to sustain their wealth.

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Shared values and family mission

Another crucial component of family wealth is gaining an understanding of the values family members share and how the family will come together around these shared values. A values and mission exercise provides an opportunity to create a shared vision of the future to clarify what is essential to the family while bringing meaning to the wealth.

Values are the motivation behind everything we do in life; they tie you to your relationships and they influence how you deal with and interact with others and your environment.

They are at play at all times.

Values are the fundamental principles you will stand by and fight for. Understanding the values your family shares is key to helping the family come to consensus on its purpose, vision, goals and objectives. Focusing on the family's shared values will allow family members to concentrate on their common ground with the goal being a values-based family mission statement, which can be used as a touchstone for current and future generations.

Going through the process of gaining clarity and understanding shared family values will also lead to improved teamwork and communication, a best practice we discussed earlier. In short, a family mission statement:

- Brings meaning to the wealth
- Creates alignment
- Establishes guidelines
- Plans for the future

It is paramount to remember that the mission statement is just words on a piece of paper and requires guidance and a framework to be brought to life. We have found it can be helpful to read the document at the beginning of a family meeting and ask the participants to describe how they are living the vision.

Also, a shared values and mission discussion can be an excellent way to introduce the younger generations to family governance. Having them listen to their grandparents, parents, aunts, uncles and cousins share stories about how they are following their values and living the mission can be a powerful and enriching exercise.

Policy & procedure

After completion of the family mission statement, to reach its multi-generational goals, the focus should shift to the establishment of family structures and policies and procedures that will be employed to oversee the family legacy.

These structures and policies will guide the family on the cadence of family meetings, identify roles and responsibilities each family member will be held to, and how family members will treat each other.

Family policies can provide guidelines to help avoid operating from assumptions and ad-hoc decision making. It is important to remember these policies are morally, not legally, binding.

What might some of these policies cover?

- A decision-making policy would detail how a family would come to consensus around the many choices they will make about joint wealth
- A code conduct policy would deal with how family members will conduct themselves with each other and their communities
- A conflict resolution policy would put in place steps and procedures for dealing with conflict
- A risk management policy would help deflect and/or better handle the many risks one can encounter along life's path (e.g., having the proper estate planning documents in place, possibility of prenuptial agreements, having the proper insurance in place)

Of course, there are many other policies families can create. Each would be specific and prioritized by the goals and objectives of the family.

Every family member needs to endeavor to build a skill set and find their true purpose within the family structure.

Family governance

As family members begin to identify their roles and responsibilities, it allows them to find purpose in the process. It provides an outlet for them to use their intellectual capital and developmental capacity to perpetuate the family mission. Generally, family governance:

- Organizes the family around decisions that must be resolved
- Assists in the organization of the family's activities
- Defines the family's future
- Creates ongoing entities to accomplish the family's goals

For example, one of the most common family governance structures is the family council, which is usually responsible for taking on the tasks of organizing, growing and developing the family.

The family council typically explores the family values and is responsible for preserving the family history as well as the family legacy. This group would design the agenda for future family meetings and also might be engaged in shared philanthropy and the advancement of shared learning. Succession planning is another key duty of this group of family members.

The family assembly is another structure that should be considered when establishing family governance.

The assembly is the most inclusive family group where all family members will have the opportunity to come together and gain a sense of belonging. It is usually a forum for family education, gaining an understanding of the family mission and the family value system.

While these two governing bodies are not legally empowered like a family board would be, they are equally as important in the development of the family wealth as well as the continued growth of the family largess.

Prepare the human capital

Every family member needs to endeavor to build a skill set and find their true purpose within the family structure. This allows them to be wealth creators striving to be net contributors and not net detractors from the family's largess.

It is also important to develop an education strategy for identifying talent and understanding the competencies that might need to be developed.

- Does everyone have the level of financial literacy required to utilize the wealth to their advantage while not depleting it so that future generations can also benefit from it?
- Is there a support for entrepreneurship, which will enable the possible increase in the family wealth?
- What is being done to cultivate and mentor future family leaders?

- What type of college and career planning might family members have access to?
- Does the family have a foundation that could serve as a learning platform for younger family members?
- What do we need to do to prepare the next generation of leaders?

These are all questions that can lead to the identification of what is required for family members to be responsible, contributing family members. Putting this sort of plan in place prepares family members to live the family mission, and accomplish their multi-generational goals and objectives.

Strategic succession planning that is aligned with the family mission can only take place if the human capital attains the level of knowledge necessary to meet overarching family goals and objectives. By looking to the future and planning together, prospective family leaders can be properly trained and mentored to take the reins once the current generation is no longer able or willing to carry on.

Considering who might take on a leadership role and how to prepare them to attain those responsibilities is a process that takes deliberation and time. When families take the time to envision the future, everyone has a chance to express their thoughts and hopes as to where they see themselves and what might be necessary to reach the vision. If this planning does not take place, it will be difficult to come to consensus on how to get to the destination.

In addition to financial literacy, it is equally important to educate the next generation on the emotional impact of wealth. Great wealth tends to magnify the day-to-day complexities of life. Therefore, it is vital to mentor family members on how the wealth might impact their lives so that they can be prepared for any challenge. Having open and honest conversations about money and how each family member views their wealth and tying these conversations back to the family mission statement, will again add to family cohesiveness and strength.

In summary: Govern the enterprise

As stated earlier, family wealth encompasses more than just the financial capital of the family. Family wealth incorporates the family members themselves, who they are, what they know and the competencies that might be missing.

It is our belief that families of significant wealth could prevent many of the risks to their multi-generational goals of sustaining wealth by centering their efforts on family wealth. Doing so will create a forum for communication to help prevent operating from assumptions, which are generally incorrect and lead to a level of distrust.

Better communication that is open and transparent reduces family stress and conflict and increases the involvement of family members and the feeling of inclusivity.

Focusing on family wealth helps the family to clarify what is important and gain an understanding of what energizes them, drives their behavior and motivates them to action by bringing meaning to their wealth.

Finally, focusing on family wealth will help the family reach consensus, come together around what matters most to them and create a framework and a path for the family to enjoy their capital for well into the future.

Author: Truist Wealth's Center for Family Legacy

Case study: A simple miscommunication

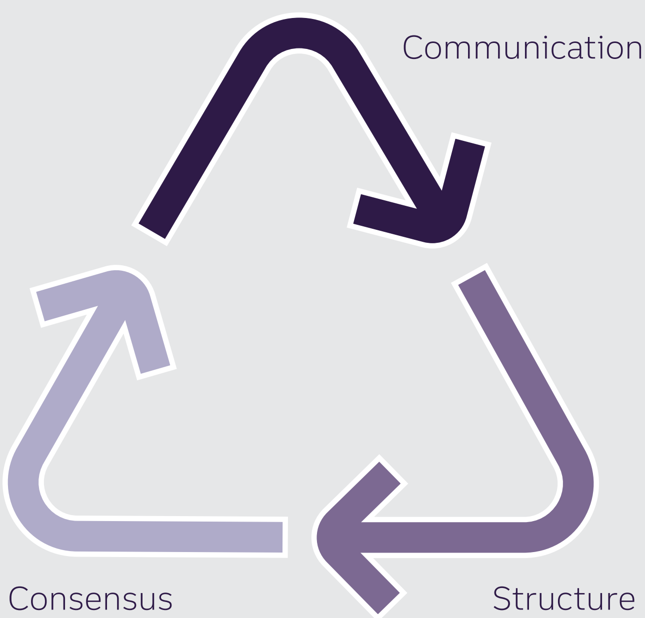
We began working with a family several years ago. When the family came to us, the patriarch complained of his fractured relationship with his son. Previously, the two families spent a great deal of time together; at holidays, traveling on vacation and dinner every Sunday. Now, they barely spoke and the only time he saw his grandchildren were at school events like plays, concerts and sports.

At the first meeting, the patriarch talked about how he retired from his position leading the family business and placed his son as president. He gushed about how proud he was of his son. How he had started at the company in college as an intern, and worked his way to become the head of their sales team and the leading salesperson for the company.

The son said very little at the first meeting.

At the second meeting, the patriarch began to discuss the family business when the son interrupted and told his father he did not want to be president. When the patriarch asked why, the son told him he never wanted to run the company. He wanted to focus on sales. That was what he was good at and liked to do. When the father asked why this is the first time he was hearing this, the son responded that he did not want to disappoint him. The reason the relationship deteriorated was because the son was ashamed and hoped he would grow into the role.

The next day, they began a search for a new CEO, the son went back to sales, the company continues to flourish and the family relationship has never been better.



- Communication without structure and consensus is ineffective
- Consensus without communication and structure is temporary
- Structure without consensus and communication is fragile and authoritarian

References

1. Chris Taylor, "A little honesty might preserve the family fortune," Reuters, June 28, 2016, https://www.reuters.com/article/us-money-generations-strategies/a-little-honesty-might-preserve-the-family-fortune-idUSKBN0OX1RH20150617

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