SUCCESSION PLANNING: STRATEGIES THAT WORK

***Mark McMullen,* partner - CEO – family office at Stonehage Fleming (Switzerland), explains the practicalities of successful succession planning. He also explains succession planning's growing importance as a tool for long-term risk management**

It is often repeated that families go from 'clogs to clogs in three generations'; wealth earned in one generation seldom lasts through to the third.

Given the hard work involved in building such fortunes, it can be difficult to understand how such seemingly successful families so often fail in their attempts to transfer wealth.

Some immediate explanations spring to mind: a lack of diversification of assets, insufficient interest from the inheriting generation, or rigid control by the previous generation.

A more insidious – and less well-known – cause of wealth destruction is a breakdown of communication within the family. Such breakdowns in communication can come at any time, but there are certain key moments when they are more likely to occur: the death of the head of the family, divorce, when a family business is sold, or when a member of the next generation assumes a leadership role within the family or within the business.

These inflection points are all part and parcel of life, but they can become very damaging in instances when a family lacks both a clear framework for making decisions and an agreed set of objectives, which have been originated by the founder and renewed by successive generations.

Succession planning is the most important tool of long-term risk management. It does not guarantee the preservation of wealth through the generations, but it can – and does – improve the chances that the wealth will survive.

Each individual family has a unique culture that can be thought of as an amalgam of beliefs, values, practices, norms and ideas. These are what help drive a family's strategy.

Despite all family cultures being different, there is a common theme that rests on the belief that culture brings the family together to identify common values. Succession best practice, therefore, begins by identifying and understanding these values and addressing three key elements of next-generational planning and family governance.

THE PURPOSE OF WEALTH

Agreeing the purpose of wealth is key when faced with the decision as to how to leave wealth, to whom and in what form. Asking the question 'what is it all for?' is an exercise that provides many benefits, especially to those who are beginning to plan the transition to the next generation.


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Consideration must also be given to whether to leave it unconditionally, or to leave guidance on how wealth should be used and managed. At one extreme there are some entrepreneurs who leave nearly all their money to charity, and at the other extreme there is a family trying to create a 200-year trust with guidelines for distributions across eight generations.

The next question is how the wealth is to be divided between different family members. Fairness and equality are easy words to use, but it is not so easy to define what they mean in practice.

It could be argued that the wealth should be divided equally between members of the next generation, or alternatively, that a greater share is allocated to those with responsibility for carrying forward the family business or other assets. The responsibilities of family leaders must be specified and mechanisms put in place to protect the interests of others. Without a guiding philosophy, every decision has the potential to cause a rift.

Finally, the processes by which decisions are made are critical to the future wellbeing of a family.

Constitutions define the overall objectives and decision-making processes for the entire family and most see a benefit in this tool. It is also true that some families prefer a less businesslike management approach, finding such documents to be too structured and restrictive.

Communications will usually include family meetings – the whole family and consultative only – and the family council – a representative body with some decision-making powers.

Where there is as a family business making up a substantial part of the assets, the relationship between the family and the business will be critical, as will the rules that govern the highly sensitive area of family members working in the business.

Succession best practice, therefore, is not just one set prescribed procedure. The biggest challenge is to agree the format and get the process started.

Regardless, it goes beyond reasonable doubt that in the majority of cases an effective succession planning exercise brings considerable benefit to a wealthy family.

In our experience, families that navigate wealth transfer positively are those willing to communicate freely, take outside advice when necessary and keep an open mind about their long-term goals, and what they would consider a successful outcome. ■