

KNOW HOW BULLETIN

AGREEING THE PURPOSE OF FAMILY WEALTH

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The growing trend for wealthy families to discuss and agree the ‘purpose’ of their wealth has been confirmed in numerous surveys in many countries, including the findings of Stonehage Fleming’s own report on family succession, entitled ‘The Four Pillars of Capital’.

This paper explores the practical benefits such an exercise may bring to a family, in particular to those who are beginning to plan the transition to the next generation.

All wealthy individuals are eventually faced with the decision as to how to leave their wealth, to whom and in what form. They also have to consider whether to leave it unconditionally or to leave guidance on how it should be used and managed. It is difficult to leave guidance without addressing the question ‘what is it for?’

Families have widely differing “purposes” for their wealth. At one extreme, there are some entrepreneurs who have left 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 FOUNDER’S PERSPECTIVE

Most of those who create large fortunes do so by building substantial businesses. As the business grows, the assets and revenues often exceed their needs, but the motivation to continue growing rarely abates.

Entrepreneurs are driven and ambitious and frequently seem to operate in a bubble of “eternal youth”. Only when they begin to consider succession do they think about the impact of wealth on their heirs.

The issues they need to address include the following:

- How to find a simple basis of “fairness” for dividing assets among their heirs and other potential beneficiaries, identifying particular circumstances or needs which should be considered
- The importance or otherwise of keeping the family business or other assets in family ownership
- Any wish to give guidance on the use and management of the wealth, including interests of other stakeholders, such as employees and the wider community
- Whether to arrange their affairs to encourage family unity and a broader legacy of family values and culture

The answers to these and many other questions are strongly interrelated and difficult to resolve in isolation. Conflicting objectives may need to be prioritised and reconciled around a central philosophy and purpose.

It can be immensely helpful to the next generation if that purpose and philosophy are developed and communicated well before the founder passes on. If not, the decisions made might come as a shock, causing resentment and perhaps dispute in the future with many negative consequences, including wealth destruction.

THE FAMILY PERSPECTIVE

A family will probably include a number of individuals with differing abilities, personalities, interests and aspirations which are not always easily reconciled.

However, they may also have much in common and most people grow up with values, hopes and expectations which have been influenced by their family and their surroundings. Nearly all have a need to be treated fairly, if not equally, and to understand the difference.

Yet gross inequality and unfairness can be accepted, if they are ingrained in the family culture. For example, the English tradition of primogeniture involves large estates passing from eldest son to eldest son, whilst other children may receive relatively modest inheritances.

Underlying this culture is the tacit understanding that the central purpose of the wealth is to preserve the estate in family hands. In such cases, this fundamental objective takes priority over most other considerations, including the needs of individuals.

Some business-owning families may take a similar view in that they have a strong preference to keep the business in family ownership, which may have to be reconciled with the income needs of individual family members. It is well known that a family business can be the glue which holds a large family together, but it can equally be a divisive force which corrodes family unity, sometimes driving the business to insolvency in the process.

In any family dispute, the alleged intentions of the founder will be used by both sides, so clearly stated guidance can help prevent potentially disastrous consequences. Such guidance is no easy matter, as it must allow future decision makers the flexibility to adapt to changing circumstances.

Many families also have to cope with inheriting specialist investments which rely heavily on the skill and experience of the founder or other family members. Some families want to continue the heritage of investing in new ideas and young companies, in which case a carefully crafted statement of purpose will be of enormous assistance, especially if things go wrong.

Cash, quoted investments and some properties may be easily divisible between family members, but an art collection, for example, may benefit

from continuing in collective family ownership, thus requiring an agreed strategy, decision-making framework and governance.

The desire to promote family unity is sometimes a factor in agreeing the purpose of wealth. Unity is usually not driven by fairness through equality, but fairness through common understanding. Understanding is driven by communication and leadership. Leadership without a purpose is almost impossible.

HOW TO DEFINE A PURPOSE

If the aim of a “purpose” is to help a family set clear objectives and make better decisions, with a recognisable strategy for their wealth, then it must be clearly articulated. There are numerous conflicting issues to be addressed and reconciled, so a few bland headlines are unlikely to be sufficient. Purpose is much more detailed than a ‘mission statement’.

Families sometimes assume that by bringing up their children properly they will understand the family’s vision through osmosis. This is possible, but not easy, as families are rarely as good at consistent communication as they think. It is not what one generation says that it is important, it is what the other one hears that matters!

Other families therefore opt for a more formal process. It is likely to involve a number of family meetings, possibly assisted by an external facilitator, who will drive the process and make sure all voices are properly heard. The objective will be to arrive at a consensus which is accepted by everyone involved, despite the fact that they may start out with widely differing perspectives.

The need for agreement is greatest when assets such as a family estate, family business or art collection continue to benefit from a degree of common ownership which implies shared decision making. This particularly applies to families who are asset rich, but have insufficient cash flow to support all the needs of a growing number of family members.

Issues to be covered should include the following:

HERITAGE AND BUSINESS ASSETS

For those with landed estates in the family for centuries, the practice of primogeniture will be clearly understood, but may need to be discussed

rather than assumed, in the light of changing values in society.

The issue for business-owning families is even more complex. If there is an agreed preference for the business to remain in family ownership, the reasons for this must be clearly stated, with well-designed caveats to provide for changing circumstances.

Similar considerations may apply to other assets where there is a desire to maintain them intact, and which require active management.

MANAGEMENT OF INVESTMENTS

Whilst the main object of investment is usually to preserve and grow the wealth in real terms, changing attitudes and values increasingly emphasise the importance of 'Socially Responsible Investment' and 'Impact Investing'.

Families with a business background may also wish to encourage a continuing culture of entrepreneurialism and participate directly in backing new ideas and talented individuals.

There are numerous issues which need to be discussed in defining the family's approach, in particular the willingness to adapt investment criteria to meet social and other 'non-financial' objectives.

FINANCING THE FAMILY LIFESTYLE

The ongoing income required to support family members will usually be a key factor and the need for income should be debated in some detail, especially where it conflicts with other objectives.

Wealth is only beneficial if it helps family members to lead more fulfilling lives and to explore their potential as human beings. This may lead to certain controls designed to encourage the young to make good use of their own talents, and not rely too heavily on inheritance to make their way in the world.

CONTRIBUTION TO THE COMMUNITY

A strong theme underlying many of the decisions above will be the extent that the family wishes to use its wealth to benefit the wider community. In some cases, the motivation is a balance between genuine altruism and enlightened self-interest.

In many countries, increasingly hostile public attitudes to wealth represent a significant threat, which may be mitigated by demonstrating how that wealth benefits the wider population.

This contribution can be made through the way the family conducts its business and investment activities, creates employment and supports the local community, but many families also dedicate part of their wealth to philanthropy.

There are various ways in which the family can organise charitable giving, often including active involvement by a number of family members, so that it helps to reinforce the unity of the family, working together for the good of the community.

All of the above will benefit from clearly thought out structures and decision-making processes, which can only stem from a detailed and well-articulated statement of purpose. This will often include a set of agreed values which guide individual behaviour and which can be more strongly applied to collective decision making. For some the family 'brand' is important.

DEFINING AND MANAGING 'RISK'

Purpose cannot be discussed without risk, and risk cannot be addressed in the absence of purpose and objectives.

Management of risk is one of the most complex subjects to be considered as risk takes many forms, from the performance of the family business and the volatility of the share portfolio to the more intangible risks such as family reputation or transferring leadership and control to the next generation.

The discussion needs to take place within a structured process, if meaningful results are to be achieved.

FINAL THOUGHTS

Wealthy families and entrepreneurs have relatively few options when considering succession. They may of course prefer to leave it to the next generation to manage the responsibilities and privileges of wealth without guidance, but they are still faced with practical decisions which cannot be ignored.

Most people want to avoid giving excessively prescriptive guidance which ties the hands of their successors, but may still wish to create some form of legacy which is more than just financial.

Those families and entrepreneurs who want to establish parameters for their legacy have three main alternatives:

- They can trust in osmosis and take the “what if I just bring my children up properly” route
- The family leaders can set the rules themselves, without family consultation, in the hope that their decisions will be accepted and respected by the next generation; or
- The family can opt for a more structured, facilitated process which can encompass all generations

Whilst a defined purpose of wealth does not guarantee success, the process of agreeing that purpose can provide families with a clarity and understanding that ensures the plan for the transfer of wealth is understood and not imposed.

There may, however be circumstances in which the differences are unlikely to be bridged by such a process, in which case the terms of the legacy and the parameters for decision making will probably need to be defined in enough detail to avoid ambiguity.

FOR MORE INFORMATION



Matthew Fleming
Partner - Succession and Next Generation

Matthew is a Partner of Stonehage Fleming responsible for Succession and the Next Generation across the Group.

Matthew joined the Group in 2002, having retired from his professional cricket career where he played for Kent CCC for 13 years. Since retiring from cricket, he has held various positions within the family business, including Managing Partner at Fleming Media and a Director of Ian Fleming Publications and James Bond Enterprises. Matthew was educated at Eton College and was commissioned into the Royal Green Jackets in 1985. He is a Director of the England and Wales Cricket Board, the Norfolk and Norwich University Hospitals and holds several external non-executive positions. Matthew was President of the Marylebone Cricket Club (MCC) during 2017.



Ari Tatos
Managing Partner

Ari is joint Managing Partner of Stonehage Fleming, he joined the Group in 1986 after qualifying as a Chartered Accountant with Arthur Andersen. He has been a key member of the leadership team for over 20 years, directly overseeing a major expansion of the Group. Ari also acts as a Key Adviser to several wealthy families and chairs family councils.

Ari holds a BCom (Hons) and a Certificate in the Theory of Accountancy from the University of Cape Town. He is a member of the Society of Trust & Estate Practitioners and the South African Institute of Chartered Accountants (SAICA).

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