

10 FAQ: FAMILY CONTINUITY

In this honest and detailed interview, Keystone Private's CEO Managing Director, David Jackson discusses ten most commonly asked questions about family continuity.

1 Firstly, what is it?

Family continuity covers a variety of areas. It's the 'soft stuff', it's not the finance and accounting, it's not the investment, it's not the property. It's the education programs developed for each generation, whether you're first, second or third and so on. It's managing the philanthropic side of things, establishing and assisting with foundations and the ongoing management of such. It's the family councils, family boards and committees; establishing them, sitting on them, facilitating them, and creating communication strategies between the generations. It's managing divorces and estate planning processes, wealth transition and the intergenerational process. It's that trusted advisor role; being your power of attorney, your alternate director, executor of your estate or trustee. It's being the person you can ring at 10 o'clock at night saying, "My husbands' just left me, what do I do?" or "You're the only person I can talk to because you're the only one who understands my situation." We are often the "Chief Emotional Officer" of a family office on top of all the other roles.

2 When should we start a Family Continuity plan?

You should start as early as possible if you can... People often wonder "When should I start educating my children about growing up in an environment of wealth?" Should it be when they're 5 years old with pocket money, should it be as a teenager or should it start when they read that Mum and Dad are on the Rich 200 list? I'm a big believer of 'the earlier you start the better'. There's no reason it can't start with pocket money; earning it, being responsible for it, saving it, spending it and choosing how to spend it. At the other end of the spectrum, patriarchs and matriarchs who've created wealth should never assume that the education journey is finished either. And to that end, we have a curriculum from the Family Office Exchange (one of the resources we use) that actually goes from age 5 to 70, covering topics across the education process. When should you start? As soon as you can.

3 Should we involve spouses?

People often wonder, "Should we involve spouses?" i.e. in-laws, or 'outlaws' as they are often referred to as. There is no right or wrong answer to that. Lots of families insist on 'bloodline only', whereas other families are of the opinion that spouses end up being 50% of the bloodline of the next generation and should therefore be included. It all depends on the family dynamic. I'm a big believer that if you choose bloodline only, then make that for decision making scenarios but have spouses included in education programs, make sure they know what's going on. I feel it's important that spouses aren't brutally excluded from the goings on as this can drive a wedge in the family unit which often passes onto the next generation. Having spouses excluded from decision making but included in the other important awareness areas is a reasonable middle ground. This, however, begs the question; if Warren Buffet was your son-in-law, would you exclude him from the process?

4 How do we deal with wealth distribution and when?

One issue that keeps coming up a lot now is distribution policies. When to start them, how much is enough? How much is too much? Does it happen in the will, or should it happen beforehand? I believe that if you are asking the next generation to manage your wealth when you're gone, you should engage them in the process while you're still alive. For example, how can you ask a family to manage \$100 million, if you won't give them \$500k per year to manage? It's important to create an environment where they can get used to managing wealth, used to dealing with the advisors, used to dealing with professionally managed, asset allocated, diversified portfolios. Often patriarchs and matriarchs have a different opinion than the next generation and this needs to be dealt with through communication and setting of guidelines, whereas if you're in a third, fourth and fifth generation family, those things have often already been covered, so they grow up with 'what it is', rather than 'what it might be'.

5 What are some of the processes and why is a Family Office advisor necessary?

Family continuity can be addressed in a number of ways. The first step is usually the assignment of a trusted advisor filling a role in some shape or form. Some families require a regular forum. For example; we have a family whom we meet with every fortnight. We discuss certain formal agenda items and then there is an informal part of the conversation where issues can be tabled and resolved. There are cases where the parents are still alive and an executor of the estate is brought on in a trustee role during their final years to allow for an easier transition rather than there being a sudden change when Dad or Mum is gone. It's an opportunity for the next generation to get to know the advisors and understand the process while Dad or Mum are still around. If you go down a formal path of family boards and councils, then questions will be raised on who should be on the family board from the family's point of view, and also from an external or independent point of view. It's often lawyers, accountants or investment specialists. While there's nothing wrong with that, sometimes the process needs an advisor with broader experience. An experienced advisor can assist both parents and children as an independent voice and can raise queries, concerns and issues without fear or favour. Essentially an advisor can raise an issue that is effectively brought to the table anonymously. It can be a formalised process, it can be a casual one, there is no right or wrong way to do it, but it's good to know you have options.

I'm a big believer that you can't just stick a shingle out and suddenly say "I'm a family office executive". Part of my mantra is you need to have knowledge, experience and understanding. You need to know what you're doing, have done it before and apply that knowledge with understanding. It needs to be somebody whom the family can relate to, it often falls to the long term lawyer or accountant, and there's nothing wrong with that, but it's not always the right person. Sometimes you need new blood. The other issue is that the trusted advisor is usually as old, if not older than the patriarch and matriarch so you have an intergenerational issue within that role. The second generation may feel no connections to that advisor, or if they do have a connection, that advisor often retires quite quickly, so the matter of 'who' is actually quite important and needs to be addressed. Should the advisor be completely new to you? Should it be an old family friend, noting that friendships can wax and wane? Should it be a professional? I have seen enough family dynamics and situations to confidently say it should be a professional in the family office field. But I'm aware of a number of lawyers and accountants who have grown into these roles and have acquired the knowledge and experience so, I don't think it's a matter of a specific qualification or profession, I think it's the amount of knowledge, experience and understanding that's brought to the table.

6 What are some of the issues that come up in family continuity, particularly inside the family? What if the wealth is not generated yet, or is in the process of being generated? How do we start family continuity now?

If the liquidity event or the development of the wealth hasn't happened yet, or is in early stages, often the patriarch and the matriarch might consider that it's too early to start thinking about it, so they put that project on the back burner. I believe that it's better to start early because you can begin to deal with it and the children can be a part of the process. The bottom line is; you're trying to teach the next generation to have a sense of stewardship for future generations, rather than have a sense of entitlement to the money. So the earlier you do this and with less money at the table, often the easier and better it is. One of the challenges we face when presenting the value proposition of 'soft services' such as Family Continuity is that the family is investing in knowledge that needs to be imparted; the processes and responsibilities. You're not investing in a share or a property. It's a cost, it's an overhead, but families need to see that there's value in that. It's an investment in the transition of wealth through the generations. I try to engage my own son in the processes that I use and the systems that we apply to our family so he learns how to be a responsible adult growing up.

7 And what about family continuity in terms of wealth education when the children are grown up? How do we educate our kids when habits have already been formed?

This circumstance is actually the norm in Queensland for wealthy families. Most families are first generation, the liquidity event has occurred relatively recently, Mum and Dad are baby boomers and still very much alive and kicking. Hopefully there have been good habits formed already because the kids have usually grown up without wealth. In most cases they've grown up watching Mum and Dad reinvest most of their money back into the business, so they haven't grown up with flash cars and in flash houses and most of them haven't even been to private schools or university. They've grown up very much like normal kids, in a normal environment, so in most cases their understanding of wealth and responsibilities will be easier because they don't have any level of expectation. What you do have to manage however, is their knowledge. Because they have not grown up in a financially sophisticated environment with advisors and managers, they will need to understand the processes. So whilst they may have developed good values from growing up in quite a nice, normal environment, you need to transition them to being people who know how to manage significant wealth... which means you've got to start educating 20-40 year olds anew when they thought they'd finished the education process.

Adult children usually respond very positively. They're some who think that they know it all, or who think that because they've been involved in some part of the family business, they have a certain skillset. But generally, everyone I've worked with to date has been really positive about learning. They react extremely well and get engaged to learn more about structures and understand more about cash, shares, fixed income, property and other investments. They also respond well to meeting other high net wealth families to learn more about how other families deal with wealth. This can be important as most of these kids/adults grew up in a relatively normal environment.

What about educating the grandkids?

Yes! I have found that grandkids embrace the process a lot. It can be as simple as the pocket money exercise I do with my son, he gets \$10 a week, \$5 goes into savings which he can't touch, ever, \$2.50 goes into a charity bin which he has to decide every six months who he gives that money to, and \$2.50 goes into pocket money which he can do what he wants with. So he learns about putting money away, learns about helping the community and helping others and also learns that only a bit of his money is ever available to spend. I often find that the second and third generation education processes start at the same time.

8 What is a Values Exercise and why do we need to do it?

Many clients ask why we do a 'Values Exercise'. We do a Values Exercise to find out from Mum and Dad what their values are and find out the kid's values are, and if the third generation are old enough, we find out what theirs are. Sometimes people see this as a typical business planning exercise; something unnecessary that you put in a folder in the corner, but I disagree. You need to work out what everyone's inherent personal values are. This will determine whether you can keep the wealth together or whether you may need to separate it. An example I'll give you is, if everyone's values are pretty similar, you're far more likely to be able to keep the wealth together, manage it and then distribute the income in a successful pool of funds. If one person's values are more consumption based and believe that the money is there to be spent on lifestyle, entertainment and enjoyment and their sibling believes that the money is there to be saved for the grandkids then there may be challenges. Mum and Dad need to understand that these two children have different values and that the best solution may be to separate the wealth at some stage in the future. So that is why you do the values exercise. I have experienced that if you try to keep the wealth together for two children that don't have similar values, it'll blow up. And the lawyers will be the ones who end up making money out of it.

9 What if you've got a 'black sheep' in the family? How do you deal with that?

This is a common issue that comes up with Sydney and Melbourne families. With first, second and third generation families, the patriarch and matriarch are still a direct influence to the family. But by the time you get to that fourth and fifth generation then that influence just isn't there so you've got the higher likelihood of a 'black sheep' scenario. When there are more and more people involved, the founders of the money are less of an influence, or maybe not even around so the propensity to have a 'black sheep' is higher. Sometimes the black sheep can be really good for the environment because they can be that left field thinker, which can be quite beneficial, but it depends on what kind of 'black sheep' they are. I've seen cases where one family member chose a spiritual path which meant that they chose to have nothing to do with the wealth. That brought up questions of; are we excluding them from this, or are we just holding it for them if they decide to come back in the future? What if they want to give it all away? The free thinking, left field sort of person is a great example of a good black sheep because they often reinvent ways to deal with things. You may have a family member who doesn't want to be part of the wealth story and that's a choice too.

Another example is a family member who says "Actually, I don't play how you guys play; I don't think how you guys think, so there is no point in me being a part of this story". This is why a family needs to have a system in place which is developed to provide for people to exit the environment. There is no point trying to control people, it doesn't work. You can have controls in place on how the family money is dealt with, and if you're receiving the benefit of it, what's expected of you. The counter proposition being that if you don't live up to that, then you don't receive the benefit of the funds. This brings up questions of, is that a permanent thing, or is it a temporary thing? Can you exit a family and then choose to come back? And if so, has your share changed? Again, no right or wrong answer, but it's something the family needs to address and have procedures and systems in place to deal with these situations.

Sometimes there'll be cases where one person believes that they should receive more benefit because they are running the family business which is generating the family wealth, going to work every day, working really hard, etc... whereas another sibling might have run off to travel the world. The first sibling feels they deserve more of the benefits of the family wealth than the other sibling. Well, the simple answer is that the first sibling needs to be paid a market based salary for their job. But you need to have the systems in place to deal with that, otherwise it builds resentment which creates disagreement. Disagreement in a family breaks up family wealth and again, if it's done poorly, lawyers get a big chunk of it and the family doesn't. It creates transaction costs; stamp duty, taxation consequences, advisor costs etc... This all comes back to having the right advisor and a decent family continuity program so you can minimise the consequences.

10 You just mentioned arguments and tension within the family; most people don't want to talk about it. What is the best way to deal with this?

Having a trusted advisor is the first step. They can be the independent, non-judging sounding board as well as the facilitator to raise issues, open conversations and offer reasoned opinions. It is hard, for siblings particularly. With the first generation, you have Mum and Dad at the dinner table then, the second generation gets involved. Now you have brothers and sisters and it's still all around the dinner table. Sometimes it can be very hard for them to get past squabbles and resentments. It can be hard to overcome typical sibling rivalry. Third generation councils usually involve cousins or other family members and this can often be easier because they haven't dealt with each other on a day to day basis. But again, I'm a big believer in having an environment in which issues can be raised. If no one is willing (or afraid) to raise an issue, query or even just start a conversation, they can fester and they do blow up eventually. If you have an environment where the trusted advisor can almost act as the anonymous drop box for issues and queries then these can get tabled and be discussed appropriately. One child might be offended that another child gets frequent flyer points when they don't, when it's because the other child works in the business. Frequent flyer policies have been known to bring down families of substantial wealth, when it could have been dealt with very, very simply.