THE NORTHERN TRUST INSTITUTE

SECRETS OF ENTERPRISING FAMILIES

HOW WILL YOUR SUCCESS IMPACT LOVED ONES?

Fear that your children will squander the wealth you built throughout a lifetime of hard work can be the very thing that undermines a successful transfer of your wealth and values.

Learn five secrets that lead to successful wealth transfer from families that have succeeded, generation after generation.

For wealthy families, a top concern is often the impact their success will have on loved ones.

The well-known business adage “shirtsleeves to shirtsleeves in three generations” portrays a cautionary tale of how successful wealth creators risk having their life’s work squandered by heirs, leaving grandchildren and other relatives left to start the process of building wealth all over again.

New data has called into question the accuracy of this premise, finding that such fear-based planning can hinder the ability of future generations to build on past wealth and even lead to family tension. Using money to control outcomes ignores the fact that family members often grow up under very different circumstances and, thus, their definition of wealth may not look the same. Behavioral research finds that building confidence and trust is more effective in equipping rising generations for their own responsibilities and the decision-making required to manage wealth successfully.

The Northern Trust Institute has studied the behavioral patterns of thousands of families and found five clear patterns that have led to lasting wealth, generation after generation. In this sense, wealth is defined not just in monetary terms, but also in the well-being and happiness of your whole family. These shared characteristics of familial success have one common theme: intentionally and deliberatively taking a collaborative, multigenerational approach to managing wealth.

SECRET 1: SILENCE DOESN’T MAKE IT GO AWAY

When a family does not have enough, they are often forced to discuss money matters to negotiate scarce resources. Who is going to use the family car?

Can we find a more affordable college? But when a family does have enough, there is less need to talk about it. Families may even shy away from having these discussions. But being silent robs you of the opportunity to teach valuable lessons.

Don’t Make Money a Taboo Topic

Talking about money often does not come naturally. It can be an incredibly emotional subject, even for wealth creators. Growing up, you may even have been taught it is impolite to talk about personal finances or ask questions about money. While people who grow up without money may learn skills of negotiation and compromise out of necessity, such discussions may well come less naturally after achieving financial wealth, and therefore require deliberate attention. Rather than apologizing for how success might negatively impact your family, you can choose to talk about how money gives you options, like being able to live the life you want, retire when you want, take care of your family, enjoy your hobbies or contribute to causes you are passionate about.

As children become aware of wealth, they may ask questions you are not prepared to answer, such as “How much money do we have?” Talking about your wealth does not mean sharing your entire balance sheet before children are ready. You can wait until they have enough life experience to handle the answer. But do not dismiss their questions with a question, such as “Why do you ask?” This opens the door to having an open conversation about the responsibilities, challenges and obligations that accompany wealth. Normalizing conversations about money creates an environment where children feel comfortable asking questions and gain valuable perspective.

ACTION ITEMS

- Before talking to children about wealth, it is important for both parents to be on the same page. Together, seek opportunities to talk about money and demonstrate gratitude.
- Empower loved ones to pursue their own financial success — and take an active role in finances — by voicing the reasoning behind your choices.
- Ask them questions to encourage their own answers, bringing them into the conversation. As your children age, you may want to introduce them to your trusted advisors and invite them to engage in age-appropriate goals-based financial planning.

SECRET 2: RESIST THE CARROT AND THE STICK

Many wealthy families earned their success through hard work, resilience, and determination, leading them to attribute the happiness of their success to having earned it. As a result, they pass down this work ethic to help loved ones obtain the same degree of satisfaction. However, overusing money as a carrot to incentivize work, academic excellence or other accomplishments can backfire.

Research shows when there is excessive use of monetary rewards, desired behaviors can start to feel like work or obligations. Recipients are coerced into behaving a certain way not because they want to, but because they want something in return (money) or want to avoid something in return (no money). The benefits of this carrot-and-stick approach are often short-lived and fail to develop authentic self-motivation.

Some wealth creators even continue this type of control beyond their lifetime. They create restrictive and overly prescriptive trusts with detailed language to incentivize desired behaviors. Carrots and sticks include things like matching provisions to subsidize income and withholding distributions for less desired behaviors, such as substance abuse. Such provisions often lead to resentment and even beneficiary manipulation.

If passing on grit and resilience is a goal, allowing family members to achieve financial independence can be a strong reward. To that end, rather than using money as a carrot, we suggest setting expectations about the need to work. While you may be tempted to provide enriching experiences and travel to fill young ones' time, leaving space to allow them to start earning a paycheck in the real world teaches valuable lessons. It is not enough to model this behavior; they need to experience it.

Know Your Money Story

If your goal is to foster self-driven, intrinsic motivation, communicate how the desired behavior contributes to your end objective. The best way to do this is to reflect on your "why." Understanding your money story is necessary to understanding why you make certain financial decisions. Even if money was not openly discussed in your family, your relationship with money is still likely to reflect how it was handled when you were growing up.

Start by answering these questions: What are your earliest memories of money? Was it a source of tension? Did your family experience a significant financial event when you were a child (a divorce, windfall, death)? Based on this history, what does your family try to emulate? What lessons did you learn? What mistakes did you make along the way? How did the values you hold contribute to your success? Your money story should demonstrate a unique intention that is tied to your personal history, values and perspective. What do you intentionally do differently? By articulating your "why," you can be more intentional about the values you want to pass on.

Once you know your own money story, you can rewrite the ending, What lessons did you learn along the way? If your money story led to a transformation, communicate that as well. It helps if your story is relatable, not aspirational. There may be good and bad chapters in this transformation, but resist telling only the hero story. Wealth creators may set a standard that could be hard to live up to, and sometimes unearned wealth can foster unintended guilt and shame. The mistakes you made along the way may well offer more effective education than your successes. These moments of insight and transformation give loved ones permission to make mistakes as well, and to develop resiliency in the face of stumbling blocks. Your goal is to instill confidence.

ACTION ITEMS

- Start by answering these questions: What is your money story? What lessons did you learn? What mistakes did you make along the way? How did the values you hold contribute to true wealth? Your story should demonstrate a unique intention that is tied to your personal history, values and perspective.
- Start with the end in mind. What does wealth look like — not just for you, but for each of your family members? Identify the values that you want to transfer to your family members and reflect on why these values lead to success. Ensure that these values, and the reasons behind them, are communicated to the next generation and reflected in your estate plan.

SECRET 3: COMMUNICATE, COMMUNICATE, COMMUNICATE

Estate plans are often divulged only after the wealth creator has passed away, leaving family members to guess the goal of the plan and their own financial future. Family members must interpret the wealth creator's intentions by reading legal documents, with some restrictive trusts coming across as "they didn't trust me."

Provide context to your estate plan by writing a letter of wishes that reflects your "why." Providing this detail to an estate plan allows loved ones to gain a better understanding of, and become invested in, the "bigger picture" end goal. In addition to a letter of wishes, consider formulating the purpose of your wealth in a statement of wealth transfer intent.

Estate plans that are meant to last for generations require you to forecast what the world will be like years, or even decades, into the future — an impossible task. That is why clearly defining the purpose of your family's wealth gives better guidance to the trustees as to the values you are trying to inspire than does prescribing every distribution. This kind of purpose-based trust document can be drafted to give your trustee the maximum flexibility to navigate changing circumstances while still being guided by your statement of wealth transfer intent, aided by the context of a letter of wishes.

Bring the Next Generation into the Discussion

In many families, conversations about wealth are informal and infrequent. Instead, set aside time to facilitate family discussions, diffuse conflict and allow family members to collectively contribute to a shared vision for long-term success. Family meetings may begin casually around the dinner table or on car rides, and may transform into something more formal as the family grows in complexity. Eventually, details of the family's estate plan may be shared with beneficiaries to allow them to understand the family's objectives and to do their own planning.

Actively listening to family members gives them a voice and builds their self esteem by showing others that their ideas are considered and that they are a valued member of the group. Be sure to structure your family meetings and conversations so no family member is a passive participant. To gain buy-in and allow everyone to feel heard, each member should be given the opportunity to contribute to the agenda, moving from monologue to dialogue. Make the meetings fun, potentially combining them with a nice meal, a family vacation or a celebration. If some meetings prove difficult, consider engaging an outside facilitator so everyone feels heard and valued. Through open discussions about money, families can learn to work together as thought partners, forming solutions alongside each other rather than rushing to solve problems in isolation.

ACTION ITEMS

- Write down your money story in a letter of wishes and formalize your values in a statement of intent.
- Provide regular time and space to discuss family matters. Allow everyone an opportunity to participate and be heard. This will help you make informed decisions about who will best support your family in stewarding your wealth while fulfilling the family's joint vision for future success.

SECRET 4: DEVELOP THE FINANCIAL SKILLS TO MEET EACH FAMILY MEMBER WHERE THEY ARE

Many people agree that teaching younger family members financial skills is a priority. Yet, wealth creators often say that younger people lack the time or interest to learn, or they are too young to be privy to information about the family's finances.

In deciding what information is age-appropriate, it helps to separate financial education from financial disclosure. To achieve trust and self-motivation, be transparent by sharing information and enabling children to have the flexibility they need to identify what really interests them as individuals.

Each child is unique, with their own individual learning style. Some may need a more formal setting, while others benefit from bouncing ideas around with a community of peers or through self-study. Work with advisors who can tailor education to the learning style of each family member.

Cultivate an Entrepreneurial Spirit

Younger family members are not just placeholders in the family's wealth. Rather, they may have their own entrepreneurial goals, whether in the family company or by launching their own venture. Controlling every decision may have been key to the creator's success, but the mindset of control may draw the resistance of the creator and inhibit the upcoming generation from demonstrating their skills as they embark on their own path toward innovation.

Cultivating an awareness that each generation has their own vision for the future is important. Determine what inspires them, even if it differs from the wealth creator's inspiration, and help them set attainable goals. Meeting them where they are also means helping them discover what they are good at; what may be inspiring to one may not work for another. Introduce them to advisors who share this philosophy of finding motivation and can explain things in a relatable manner without a lot of jargon.

Start small. Provide opportunities for younger family members to practice making financial decisions that have real, but limited, consequences before they are forced to make bigger financial decisions with lasting consequences. They can plan the family vacation or purchase a car. Some families require "skin in the game" by asking them to put some of their own money into a project. Encourage them to try something new, and to embrace well thought out risk. Practicing will instill confidence, both in themselves and in the wealth creator's view of them.

ACTION ITEMS

- Resist the urge to save children from failure in their low-risk endeavors, as these missteps provide an opportunity to grow, adapt and learn strategies before they are forced to make more significant financial decisions. Encourage spending time with other entrepreneurs and peers to learn from their successes and failures. The wealth creator's vulnerability to share their own failures goes a long way in being relatable and demonstrating resilience.
- In your estate plan, consider creating a "family bank" that can provide loans to family members and seed potential ventures that have sound business plans. Family banks can codify a process for younger family members to bring business ideas to the family and provide the necessary checks-and-balances, including access to outside advisors such as professional trustees.

SECRET 5: ANTICIPATE CONFLICT AND FIND COMMON GROUND

In later generations, a family can be paralyzed by conflicting views across generations and between siblings or extended family members. Conflict can arise when family dynamics and diverging views are left to develop into problems. These problems can be exacerbated when the family has shared assets (such as a business, vacation home, charitable foundation or family office) that require joint decision-making.

For example, in the case of business owners, estate plans often simply divide ownership of a business equally. But conflict may arise when some beneficiaries rely on distributions to fund their lifestyle while others earn enough income to pay their expenses and want income reinvested for growth. Or one family member may want to work in the business, but in the absence of transparent hiring decisions, other family members or employees question their qualifications.

Families can benefit from anticipating this conflict and develop a framework for decision-making early on. An effective governance structure may include forming employment or operating agreements, independent boards of directors, family councils and other governing bodies or policies that "professionalize" the entity. Roles in the family enterprise should be clearly defined, including the qualifications and methods of selection, roles of spouses, and whether or not family members are required to work outside the enterprise prior to working at the enterprise. Be intentional about the development and education necessary to succeed in each role. Having ground rules in place before decisions have to be made helps create an understanding of fairness and promotes peace.

Guided by Shared Values

You will not be able to put a rule in place for every decision. However, when your family adopts an agreed-upon set of values and understands which behaviors support those values, you no longer need to rely on procedures setting out what people should or should not do in specific situations. All the rules reduce to one: Live the values. People can work out for themselves what they need to do, and in so doing become responsible and accountable for their behaviors.

Naturally, family members may lack complete agreement on their beliefs. Even within families, individual members are shaped by different environments. But if you uncover what drives those beliefs you are likely to find a common set of values. While beliefs may be disparate, values unite families. Building a values-based consensus around a shared vision for the future provides an enduring tool for decision making to build a legacy.

ACTION ITEMS

- Codify values in a shared document such as a "Cornerstone Statement" to serve as a guide for all financial and investment decisions. A written statement can be revised as family dynamics and goals change over time, but it serves to set an intentional course of behavior for shared decision-making.
- Values may be somewhat aspirational, but they should be true to how your family lives their lives. If a shared asset is part of the plan, establish clear policies for the entity. For larger families, consider forming a family council to facilitate information sharing.

MAINTAINING WEALTH ACROSS GENERATIONS

Many families that are Wealthy generation after generation share the characteristics of being intentional in defining and aligning with their core values, anticipating conflict, encouraging life-long learning and engaging in regular communication. Experienced advisors who work with multigenerational families can help guide you while acting as a sounding board to ensure your family is set up for success.

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