CHANGING THE PLAYBOOK:
How to Prepare Heirs for What's Coming

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Imagine you're at a football game. You are excited to see your team play because you've heard great things about the quarterback. On the first snap of the game, you watch as this quarterback takes the ball and scans the field for an open receiver. Instantly, you can tell what all the hype was about: The quarterback obviously knows what he's doing. He exudes the confidence of a well-practiced athlete. The quarterback finds his target and throws the perfect spiral downfield.

It is only then that you realize the problem. The receivers not only aren't paying attention to the play, it looks as though they don't even know the rules of the game. Although they appear to be strong, capable athletes, they clearly have never practiced. The quarterback never had a shot – his receivers didn't even know the ball was coming, and from the looks of it, they wouldn't have known what to do with the ball if they caught it.

This may seem like an unlikely event, but in the world of estate planning, it happens all the time. James Grubman, founder of FamilyWealth Counseling, uses this football analogy to make a compelling point. Even the most knowledgeable, successful clients (quarterbacks) often attempt to pass their hard-earned fortune (football) to heirs (receivers), who are completely unprepared to complete a pass. When it comes down to it, a strong, well thought-out estate plan is only half of the equation. Having an excellent game plan is worthless if the team never practices. Or, as Matthew Wesley, founder of The Wesley Group, has stated, "'Generation One' of a family must be willing to transition from quarterback to coach of the team. At some point, the leaders of the family must begin actively 'coaching' the younger generations, so that they know how to successfully play the game."[1]

Importance of Human Capital

In estate attorney Avi Z. Kestenbaum's article, *Rethinking the Fabric of Estate Planning: Have We Gotten It Wrong?*, Kestenbaum discusses the risks of using an estate planning philosophy that places too little emphasis on the importance of building up human capital.[2] The potential damaging effects of such a philosophy are well documented in *Preparing Heirs* by Roy Williams and Vic Preisser. The authors found that out of 3,000 families who failed to successfully preserve or grow family wealth, 25% of the families attributed the failure to unprepared heirs and 60% attributed the failure to lack of communication and trust among heirs. Only 3% pointed to investment or planning mistakes as the reason a family inheritance failed to transcend multiple generations.[3] It seems we, as estate planners, must do a better job of reminding clients that as they prepare their money for family, it is also crucially important for clients to prepare their family for money.[4]

Education Strategy

So how can an estate planner equip a client's family to successfully receive and manage an inheritance? The best way is to help the client establish an education strategy for his or her family. An education strategy shouldn't mean the simple creation of a curriculum or development of a test that heirs must pass prior to taking control of their inheritance. It should go beyond conducting programs that teach family members about the basics of investing or how to manage finances because programs and curriculum, alone, are only part of the picture. Rather, the strategy should be a dynamic, multi-faceted plan that aims to instill knowledge and wisdom in the next generation. Essentially, the education strategy is about laying a firm foundation upon which future generations of the family can continue to build.

Picture a stately mansion resting on a tiny foundation. It may be hard to visualize because it's unrealistic. Everyone knows a tiny foundation will never be successful in supporting the weight of a mansion.[5] Similarly, if a large inheritance passes to a family with a weak or small foundation, it is very unlikely the family will be able to support the weight of a substantial inheritance. This is why it's all too common for a wealthy family to disintegrate or squander the family wealth so quickly after the leaders of the family pass away. It's why there's the saying, "shirtsleeves to shirtsleeves in three generations." As the size of an estate increases, the need to prepare heirs for the inheritance they'll receive increases along with it. Creating an education strategy for a family will widen and strengthen the foundation of a family. This provides the family with the opportunity to flourish as a result of an estate plan, rather than be burdened by it.

When creating an education strategy, the estate planner should help the client focus on planning for two main time periods: (1) what can be done to prepare heirs now, while Generation One ("G1") is around to help teach the younger generations and (2) what can be done in the future to prepare heirs after G1 is gone and no longer available to provide advice and guidance. For the estate planner, the "now planning" is less about specific estate planning techniques and more about guiding and facilitating the creation of a new family paradigm under which the family will become intentional about equipping younger generations. Planning for the second time period, when the client has passed away, will require more technical solutions to be built into the estate plan itself.

The fundamental goal of "now planning" is the creation of a system through which family members may grow to understand the responsibilities of ownership. Whether heirs will own part of a family business or a share of the family wealth, being a responsible owner includes everything from financial management to community involvement and family participation. In a recent presentation by the Family Office Exchange ("FOX"), Amy Hart Clyne and Teresa Bellock identified a four-step process for creating a family education system: (1) assess family needs and establish education objectives; (2) develop and deliver education programs; (3) evaluate progress and get feedback; and (4) modify the method and materials to continue to achieve family goals.[6]

Assess Family Needs & Establish Education Objectives. Assessing family needs should start with a review of whether the governance structure of the family is conducive to implementing an education system. Is there open communication between family members? Are family meetings scheduled on at least an annual basis? Is there a functioning and effective family leadership structure in place? Is there an independent advisor accessible to all family members? These questions should help the estate planner gage whether the family environment is "healthy" enough to support an education system.

It is also important to identify from the start who will be responsible for the ultimate implementation of the education system. This could be the family office, an independent advisor, or a learning committee formed within the family. Whomever is selected to lead the education charge, that person (or persons) must hold the respect and trust of the family.

When it comes to choosing education objectives, the ultimate goals of each family will be as unique as the family itself. Planners should take into account the ages, occupations, and sophistication level of the family members, as well as the characteristics of the estate, to determine what types of programs will be beneficial for preparing the family members to manage their inheritance. In most instances, a solid starting point would be a program or series of programs that aim to provide heirs with (1) an understanding of family virtues, values, and history, (2) a basic financial education, (3) the ability to read and understand legal duties, (4) the skills to make competent decisions in coordination with financial advisors, and (5) the desire to participate in family meetings.[7]

Develop and Deliver Education Programs. Once the family has established the objectives, it should develop and deliver individual education programs. An education program doesn't have to be tied to any special format. It can be a handout of reading material, a teleconference, a discussion led at a family meeting, an outside speaker or any combination of the above. There are even fun, interactive computer games for elementary school children that teach responsible money choices.

One increasingly popular type of education program is the establishment of a "family bank." Essentially, it's a way for families to lend money to younger generations in a way that's empowering and educational. Instead of simply handing money over to a child so that he or she may start a business, pay for school, or buy a home, creating a family bank allows the child to gain more of a real-world borrowing experience. The family bank can be as formal or as informal as the family prefers. Generally, most family banks are structured as a trust or a limited liability company and can be led by a family member or a board of members. The bank's protocols outline the process for borrowing money. Maybe a child must submit a lending request summarizing the purpose of the loan, the proposed loan terms, and how the child plans to repay the money. Regardless of the specific requirements, undergoing a simulated loan process will provide the child with practical experience that will be useful throughout the child's lifetime.[8]

As different needs of the family arise, programs can be developed to achieve the overall strategy of ensuring the heirs are attaining the family's education objectives. Take, for example, a family who is transitioning into their fifth generation as a cohesive unit. Over 25 years ago, the family began holding quarterly meetings and hired an independent advisor to form a solid governance structure. The family created an education committee and encouraged younger family members to participate by selecting topics and ideas they would like to discuss during family meetings.[9]

This particular family opted not to adopt any formal curriculum. Instead, they utilize different formats like in-person meetings, teleconferences, and self-studies to stimulate education. Furthermore, the family chooses themes for each family meeting such as "how to read financial statements" and "what does 'trust fund baby' mean to you." Their current focus is on how to find the right balance between finance and fun. Though the family admits scheduling meetings for the entire family has become increasingly challenging, the firm foundation established decades ago has positively impacted this family for generations.

Evaluate progress and get feedback. As a family implements different education programs, it's important to seek feedback so that the family may evaluate its progress. As demonstrated, education programs can take a wide variety of forms, but overall, an education program should be carefully crafted so as to have a profound influence on the family. The FOX presentation summarized five main principles that can help to maximize the effectiveness of an education program:[10]

1. **Get key stakeholder buy-in.** *The most interesting education program in the world won't be effective if the family isn't interested in participating.*
2. **Customize the program for the family's needs.** *Remember your audience. If necessary, plan separate programs for different sophistication levels within the family.*
3. **Ensure the program is engaging.** *Use formats that facilitate open communication rather than just lectures.*
4. **Remember education is an evolving process.** *As family members grow and learn, the education programs should change along with them.*
5. **Seek to empower educated family members.** *Utilize programs that will instill heirs with confidence and not just facts.*

Modify the method and materials to continue to achieve family goals. In a survey of 38 families who have succeeded in preserving significant wealth for at least three generations, professor and organizational consultant Dr. Dennis T. Jaffe isolated several characteristics common among the families.[11] One of these commonalities was the ability of the family to "continually adapt, innovate, and change as they face new realities inside the family and in the business environment." A family must constantly reevaluate plans and procedures—especially education programs—in order to keep up with the changing world.

The best way to complement and enhance a strong education system is to provide heirs with opportunities to internalize what they've learned by connecting the knowledge they've attained to real life experiences. Two kinds of experiences can help heirs gain a deeper understanding of important lessons: The first comes from hands-on practice, and the second comes from a familiarity with the family's heritage.

Ted Beck, president of the National Endowment for Financial Education, has stated that "[m]erely talking about teamwork and money isn't enough . . . Tying the educational moments to an actual event is when it really sinks in . . . Otherwise, it is too theoretical."[12] For example, when teaching their children how to work together when handling money, Beck and his wife placed their children in charge of several garage sales. Tom Rogerson, of Wilmington Trust, also advocates hands-on teaching techniques. Rogerson and his wife give their four children $5,000 each year to invest. If the children's investments provide a healthy return, the money is used to take a fun family vacation. For the years when the children's investments lose money or bring in weak returns, the family vacation is a camping trip or a road trip to visit family.[13]

In addition to personal experience, younger generations can also learn invaluable lessons from the experiences of those that came before them. Studies have shown that children who are familiar with both the good and bad aspects of their heritage are more likely to succeed when faced with conflict.[14] A well-rounded education strategy, therefore, should incorporate the experiences of older generations not only to preserve the family legacy, but also to impart wisdom through the life lessons of their ancestors.

Estate planners must not underestimate the significance of helping clients establish an education strategy for their families. Investing in younger generations can alter the entire history of a family. Take, for example, the Vanderbilts and the Rothschilds.[15]

Cornelius Vanderbilt died in 1877 with an estate valued at over $160 billion in today's dollars. Although Cornelius had numerous legal and financial advisors working on his estate plan, his focus was on financial planning (growing his wealth) and estate planning (preparing his money for his heirs). He failed, however, to realize the importance of preparing his heirs for the great fortune he'd amassed. The effects of Cornelius not having created a solid family foundation are reflected in the fact that at a 1973 family reunion, not a single family member could claim the title of "millionaire."[16]

The Rothschilds provide a direct contrast. This renowned European family rose to preeminence in the banking and finance industry during the 19th and 20th centuries. In addition to financial and estate planning, the Rothschilds placed an intentional emphasis on preparing heirs for their inheritance. Not only do the Rothschilds seek to educate younger generations, but they also utilize real life experiences to guide their children to become responsible owners.

Using family banks, the Rothschilds lend out money to those in the younger generations who wish to pursue business or investment ventures. Stressing the importance of philanthropy and participation in the family, the Rothschilds provide a well-rounded education to those who will one day be responsible for a share of the family fortune. A continued strong family bond and the financial stability of the family demonstrate that the time and effort invested into the family's education has paid off. As Nathan Rothschild once remarked, "It requires a great deal of boldness and a great deal of caution to make a great fortune; and when you have got it, it requires 10 times more wit to keep it."[17]

As demonstrated by the Rothschilds, a well-executed education strategy can continue on for generations. Once the founder of the family business or the primary amasser of family wealth passes away, the dynamics of the family can shift drastically. Accordingly, estate planners should encourage clients to use two specific planning techniques that will facilitate the continued education of heirs even after they gain access to and control over their inheritance. The first technique involves establishing the trustee as a mentor figure for the beneficiary, and the second technique constructs a peer review system to supervise an heir's management of his or her trust after he or she assumes the role of trustee.

Mentor Figure. In his article *The Trustee as a Mentor*, James E. Hughes, Jr. dissects the traditional trustee-beneficiary relationship and discusses his finding that a fundamental misunderstanding has occurred regarding each party's role in the relationship. Far too often, accusations and mistrust flourish because neither party has a true, clear vision for how the trustee and beneficiary should function together. Hughes argues that even the most intelligent and capable of trustees can't be successful unless they recognize the main objective of acting as a trustee: empowering the beneficiary. A trustee should act as a mentor to the beneficiary, rather than as just a simple gatekeeper to wealth. Hughes puts it this way:

> In all relationships which are successful learning experiences for both participants, the party with more knowledge at the beginning must offer that knowledge to the party with less knowledge in such a way that the party with less knowledge willingly places herself/himself in the role of pupil.[18]

One of the most effective ways a trustee can empower a beneficiary is by helping him or her to become a "good beneficiary." As Hughes points out, many beneficiaries have never read nor attempted to understand the actual terms of their trust. The trustee should educate the beneficiary on the rights and obligations bestowed on him or her by the trust agreement and should make resources available to the beneficiary that will complement his or her unique learning needs. Some beneficiaries may need advice on what it means to be a better investor, while others may need help reading a balance sheet. Regardless of the sophistication level of the beneficiary, the trustee should be there to offer knowledge and guidance. Estate planners must do a better job of helping clients select trustees who will view their role as an opportunity to advance the client's education strategy.

Peer Review System. Within the contest of trusts, peer review is a scheme used solely as a positive review process of a trust's governance. Essentially, peer review is a way for an objective person or committee to perform a "check-up" on how well the trust is continuing to meet the grantor's original objectives. The system can also provide an avenue for the reviewers to inject new, refreshing ideas into the governance of the trust. Because many clients provide in their trust documents for beneficiaries to become trustees of their own trusts at some point in the beneficiaries' lifetimes, the peer review process is a healthy way to assure the grantor that the long-term stability and effectiveness of the trust will continue to be monitored.

A peer review system, while not particularly complex, does require careful thought and drafting. To start, the trust agreement should include a requirement that the review occur periodically. (Hughes recommends every five years). Estate planners should also ensure a system is in place to select objective, unbiased reviewers who will receive reasonable compensation for their efforts and expenses. Ideally, the trust document should limit the permissible duration of the review and grant the reviewers access to all trust reports, financial documents, and accounts. It is also advisable to prepare guidelines for how the reviewer should approach the review process. Although peer reviewers have no enforcement authority, their reports act as checks on the authority of the trustee and can provide clients with the reassurance of knowing that as beneficiaries take control of their inheritance, they won't be without continued guidance.

Explain the Rules of the Game

It may take a lot of planning, but preparing heirs for their inheritance should no longer be an afterthought. Speaking with clients about the importance of establishing an education strategy is invaluable to the creation of a successful estate plan. We can't expect heirs to seamlessly play out a client's estate plan if we never told them the rules of the game or when to show up for practice. Clients and estate planners can invest all their time into crafting an estate plan that will effectively and efficiently pass on the client's wealth to the next generation, but if the client's family doesn't know of the importance of family relationships, has never learned to appreciate the value of a dollar, or has never experienced the reward that comes from giving back to the community, then the expertly crafted estate plan will likely be very short-lived. Because, at the end of the day, there is no such thing as a perfect pass if there is no one there to catch the ball.

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ENDNOTES

1) Matthew Wesley, founder of The Wesley Group, and Sara Hamilton, "Family Culture and Embracing Change" presentation at 2015 FOX Fall Forum (Oct. 22, 2015). After the presentation, the author and Matthew continued the discussion, and Matthew talked about the idea of Generation One having to move from being quarterback to the coach. He often uses this analogy when talking about educating heirs.

2) Avi Z. Kestenbaum, "Have We Got It All Wrong?," *Trusts & Estates* (February 2016).

3) Roy Williams and Vic Preisser, *Preparing Heirs: Five Steps to a Successful Transition of Family Wealth and Values* (Robert D. Reed Publishers 2010).

4) Tom Rogerson and Nancy Pellegrino, "Family Wealth Preservation: Integrating Family Virtues with Wealth Planning for a Lasting Legacy," BNY Mellon Wealth Management (January 2009).

5) "Elements of Family Harmony Across Generations" presentation by Clint Haggard, President of Burgher Haggard (Feb. 27, 2013).

6) Amy Hart Clyne and Teresa Bellock, "Family Education in Action" presentation at 2015 FOX Fall Forum (Oct. 22, 2015).

7) "Preparing the Next Generation for the Responsibilities of Ownership," FOX (2007). Copyright© Family Office Exchange.

8) "The Family Bank," *Trust & Estates Insights*, UBS Private Wealth Management Newsletter (December 2013).

9) *Supra* Note 7.

10) *Id.*

11) Dennis T. Jaffe, "Good Fortune: Building A Hundred Year Family Enterprise," Wise Counsel Research (August 2013), *available at* http://wisecounselresearch.org/sites/default/files/ Good_Fortune_Complete_Report.pdf.

12) Geraldine Fabrikant, "Teaching Teamwork, but With Real Money," *The New York Times* (Dec. 9, 2007).

13) *Id.*

14) Bruce Feiler, "The Stories That Bind Us," *The New York Times* (March 15, 2013).

15) "A Tale of Two Families," The Heritage Institute, LLC, *available at* https://purposefulplanninginstitute.com/ pdf/Tale%20of%20Two%20Families-9-14.pdf.

16) *Id.*

17) *Id.*

18) James E. Hughes, Jr., "The Trustee as Mentor." *The Chase Journal* (Volume II, Issue 2, Spring 1998).