Preparing for the Windfall

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KLINGENSTEIN FIELDS
WEALTH ADVISORS

Introduction

We are in the midst of one of the largest wealth transfer eras in modern history. As the "Greatest Generation" transitions its assets to baby boomers, and baby boomers in turn pass on their wealth, more than $20 trillion is anticipated to transfer over the next fifty years, according to Boston College's Center on Wealth and Philanthropy.

But are current and future generations equipped to handle both the benefits and responsibilities that come with inheritance? The answer to this question is critical, as research has consistently proven that inherited wealth does not usually last once it is passed through as few as two generations.

According to Shomari Gilyard, Wealth Strategies Advisor at Klingenstein Fields Wealth Advisors, "The key to sustaining wealth is preparation, education and planning." Stakeholders must engage in "dialogue, communication and education targeted to the current holders of wealth, as well as the inheritors." While wealthy individuals and families may focus on estate and other technical aspects of wealth transfer, often individuals and families about to inherit are unprepared to meet many of the challenges of managing, growing, and sustaining significant assets.

Shomari continues, "At Klingenstein Fields Wealth Advisors, we believe wealth planning that aligns a client's multiple goals with resources helps set boundaries for each family's "financial behavior" as well as manage the risk and the opportunities that accompany wealth."

Money in Motion

The U.S. is at a crossroads. The older generation has amassed significant assets and is now in the process of transitioning it to future generations. While the numbers vary, all studies point to a similar conclusion; money is moving now, and will be for the next several decades.

According to a report published in early 2015 by Wealth-X and NFP Family Wealth, high-net-worth through ultra-high-net-worth families hold a significant amount of wealth "waiting" to be transferred.

Family Assets	**2014 Adult Population**	**2014 Wealth** (US$ Trillion)
Above $30MM	211,275	$29.7
US$10MM – US$29MM	682,775	$14.9
US$5MM – US$9.9MM	835,950	$6.2
US$1MM – US$4.9MM	14,930,000	$26.2

Source: Wealth-X, NFP

The Challenge of Maintaining Wealth

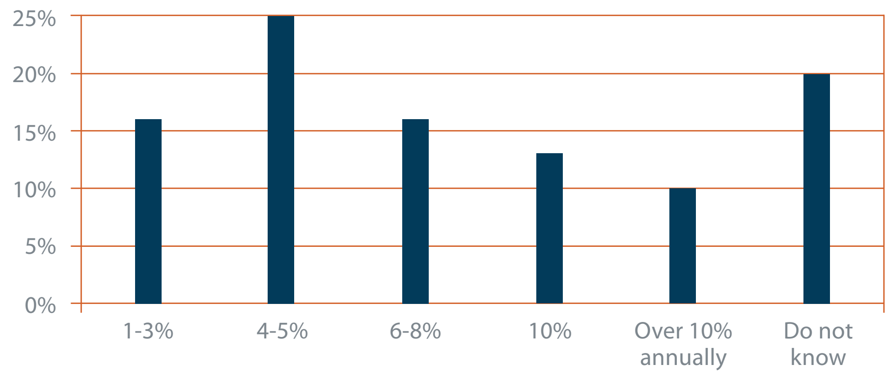
Although there are exceptions, most families do not set out to use up all of their assets or intend for future generations to spend it all. According to a 2014 study by Merrill Lynch, 69% of high-net-worth Americans would like their wealth to last at least through their children's lifetimes and 43% would like to see it make it through their grandchildren's lives. This is in sharp contrast to the harsh reality that money typically does not make it through to the third generation.

	Desire to have it last	**How much is really left**
Next generation	69%	<33%
Grandchildren's generation	43%	10%

Source: Merrill Lynch

This may be partially due to a lack of understanding of what it takes to sustain assets. For example, 39% of individuals surveyed feel that the principal of a portfolio with an annual distribution rate of 6% can be sustained. However, data on returns, taxes, and other obligations points to a maximum distribution rate that may be closer to 2% in order to maintain principal.

What distribution rates individuals believe can sustain wealth indefinitely



Source: Merrill Lynch

Many experts do not believe the U.S. stock market returns that have been experienced recently can be sustained and forecast single digit returns for 2015 and beyond, which could significantly affect sustainable distribution rates.

It's All About Communication

For families considering wealth transfer strategies, failure is not inevitable. A well-designed strategy can build a strong foundation for setting family expectations and managing behaviors that can deplete wealth.

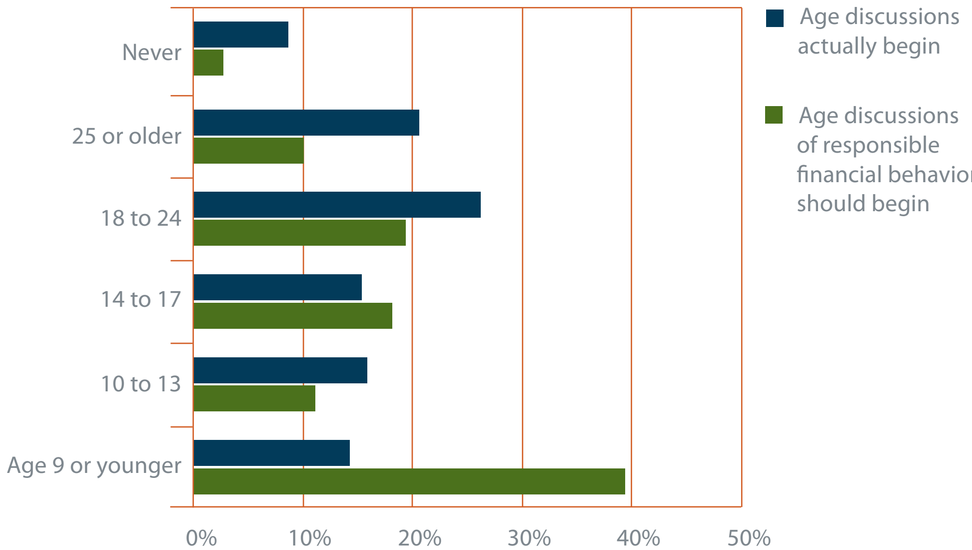
A study by the Williams Group, found that about 60% of the problems in generational wealth transfer are attributed to gaps in family communication and trust and 25% due to heirs who are unprepared to make decisions about wealth management. Only 3% of the time is the cause of wealth depletion taxes or investment performance. In other words, the main threats to sustaining wealth across generations are clearly elements that families can control.

Overfocused on Transfer "Mechanics"

Many individuals focus solely on ensuring that the technical aspects of wealth transfer, such as setting up trusts and designating appropriate trustees and administrators, are in place when building their strategies.

Building a successful family wealth strategy is similar to building a successful business. Establishing clear values about education, roles for family members, and personal responsibility are critical. There should be an understanding or appreciation of the values and effort that go into building wealth. Most wealthy individuals, in theory, believe that discussion of responsible financial behavior should begin early but do not follow through on their intentions.

When wealth discussions with your children should begin



Source: Merrill Lynch

According to Tim Voorhees, an attorney and wealth counselor specializing in family wealth, without this communication, heirs will not invest the time or effort necessary to understand family values. Further, those inheriting wealth will have little incentive to develop the structural and emotional control mechanisms, such as planning, budgeting, patience and thrift.

Financial Education Makes a Difference

Recent research indicates that education and discipline can have a significant effect on sustaining wealth (survey and analysis conducted by Jodi Letkiewicz at York University and Jonathan Fox at Iowa State University). The survey measured the impact of both financial literacy and conscientiousness on illiquid and liquid holdings among a population of individuals between the ages of 23 and 27.

Research indicates a connection between financial literacy and asset accumulation.

- Financial literacy was measured through questions regarding compound interest, inflation and stock risk, with the overall score weighted toward the questions that are most difficult to answer
- Conscientiousness was measured based on respondents' agreement or disagreement with how well the characteristics "dependable/self-disciplined" and "disorganized/careless applied"

Results indicate that both conscientiousness and financial literacy are consistent predictors of asset accumulation among younger Americans. A measurable increase in financial literacy is correlated with a significant increase in illiquid and liquid asset holdings.

Beginning early to educate the next generation can have a measurable effect on financial preparedness. An understanding of the effort that went into building wealth can help to instill a sense of appreciation and responsibility.

Bucking the Trend

It's never too early to begin the process of working with the next generation to ensure that there is a common foundation that will encourage building and sustaining wealth. Some important steps include:

- Develop a family mission/value statement that ensures all family members have an understanding and appreciation for the values the family holds and the efforts involved in accumulating substantial wealth
- Make sure succession and estate planning are in place and is customized to the circumstances
- Educate future generations and help them to understand the opportunities, issues and challenges that wealth brings
- Encourage financial literacy and instill knowledge of how personal objectives and financial resources must work in concert with each other
- Allow heirs to have direct access to advisors and other experts to instill independence and give them the privacy to express their concerns and ideas in an objective forum, increasing their confidence and ability to understand how their lives are connected to their family's wealth

Klingenstein Fields Wealth Advisors: Deep Expertise in Multi-Generational Wealth

The professionals at Klingenstein Fields Wealth Advisors have been helping our clients successfully address multi-generational wealth transfer for over twenty-five years. We are adept at understanding the intellectual and emotional issues that accompany family dynamics and wealth transfer.

"A highly customized approach works best" says Shomari Gilyard. The Klingenstein Fields Wealth Advisors' team works side-by-side with you to help inform and educate all family members. Our assistance with family dynamics complements our deep expertise in key financial transition strategies, including executor services, trust administration, estate management, insurance and tax considerations.

We can help to develop integrated strategies for families, including the facilitation of:

- Early intervention for family members and heirs
- Wealth and financial education programs
- Informational meetings with next generation members of clients
- Peer discussions among wealthy families
- Financial literacy information

We invite you to learn more about how Klingenstein Fields Wealth Advisors can help grow and sustain your wealth for generations to come. Please contact us at 212.492.7000 or visit us online at www.klingenstein.com. We look forward to hearing from you.

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