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PROTECTING AND GROWING YOUR WEALTH

"Solve your problems. Don't let them lick you."

—E.A. Stuart

What can an individual like you and families like yours do to protect and grow your wealth, share it with others, enjoy financial security, and build lasting personal and family legacies based on it?

Over the last 25 years, I have learned that effective wealth management has little to do with how much money you have or how you accumulated it. Effective wealth management is much more about how well you manage than it is about how *much* you manage. The hard lessons that I've learned as a financial industry insider and from managing substantial wealth for my family are the focus of this book and are applicable to anyone willing to meet the challenge of managing wealth. By sharing those lessons, using illustrations from my family's actual experience, I'm certain that you can avoid many of the pitfalls inherent in managing your personal wealth.

Wealth management is about more than investing, though that is an important part. Money, family, and community are invariably bound together. People pay taxes, save, spend, support philanthropic causes, and transfer wealth to their heirs. Successful wealth management involves the integrated and effective management of all these components.

Transitions

Some people build their wealth by saving money a little bit each month and managing it with the goal of having financial security in retirement. Even after years of accumulating financial assets, working with advisors, and experiencing the volatility of financial markets, they are still uncomfortable with how their assets are managed and are looking for better ways to achieve their goals.

Others achieve financial independence in sudden and sometimes difficult and tumultuous ways. Their transitions to wealth are abrupt and often stressful. Some sell a business into which they had poured their entire savings. Some retire with a pension that they are now responsible for managing. Some receive assets as a result of divorce or loss of a spouse. One of the biggest sudden and high-stress circumstances for coming into wealth is the death of a parent. Over the next 50 years, the United States will see the greatest transfer of wealth in its history. Boston College researchers John J. Havens and Paul G. Schervish estimate that, over this period, total bequests to heirs will range from $25 trillion to $65 trillion, or an average of between $500 billion and $1.3 trillion per year.[1] In many of these circumstances, people will not be prepared to take on the responsibility of their new wealth, and the event itself will often come as a surprise.

Building wealth and conserving it takes time, and it demands considered action. The key is to not do something *prematurely* that results in a significant loss of capital. For that reason, resist the impulse to act quickly or to retain outside wealth advisors before you are ready to act. Do your homework first and plan ahead.

How the Wealth Management Industry Works

Why is it important to plan before engaging wealth management advisors to manage your assets? You need knowledge to protect your interests. Unless you are a proactive, thoughtful, and informed client, the structure of the wealth management industry today actually works against your interests in three ways:

1. The wealth management goals of clients and their financial advisors can easily diverge. When conflicts of interest arise, advisors may put their own interests ahead of their clients.
2. Advisors are unlikely to fully understand or appreciate your personal and family dynamics. These dynamics are key drivers of wealth management priorities, goals, and strategies in families, and they influence many business and investment decisions—frequently behind the scenes.

3. Very few wealth management professionals have enough breadth of skill and experience to operate across multiple disciplines or to anticipate how advice offered by one expert can potentially affect that offered by another. The advice of one advisor should, ideally, complement and reinforce the value of another advisor's input. But the siloed nature of professional fields such as estate and tax law, financial planning, investment management, and banking usually works against this desired outcome.

Wealth management firms that are waiting to make money (from *your* money) include brokers, mutual fund companies, life insurers, money managers and hedge funds, law firms, banks, independent financial planners, accounting firms, and multi-family offices. The organizational culture in most firms focuses on finding a balance between getting acceptable results for the client and achieving the firms' profit goals. As with any market-driven business, the financial rewards and recognition that wealth management practitioners enjoy are based on the amount of business they bring in the door. There's a premium placed on generating revenue. It's easy to measure and is tied directly to firm profitability. But larger revenues and bigger profits don't always mean better service.

By contrast, it's *not* easy to measure the value added that a wealth management firm or advisor actually generates for a client. Thus, clients are often left in the position of having to trust their advisors without an accurate yardstick to measure their effectiveness. This is a big reason why studies of the wealth management industry show a high level of customer dissatisfaction.

This state of affairs hasn't been in the long-term interests of either party. Fortunately, the problems are not insurmountable. That's why America's wealth management industry is in a state of dynamic transition, where old business models are competing with new ones in a struggle between service and profit. No one knows which will be the winner. There is no better system than a competitive marketplace to resolve industry problems, but the process is messy and clients can get hurt. For that reason, I say: "Buyer beware!" and "Keep reading this book!"

Classic Approach to Wealth Management

Many people rush to retain wealth management advisors in whom they desire to place their trust. Clients are busy, and most are anxious to have professional oversight in place. They either look to an existing trusted advisor who helped them before (maybe with issues unrelated to current wealth management challenges) or they respond to inquiries from enterprising advisors who identify them as new business prospects. In either case, people often choose one firm immediately or decide to have multiple firms compete for their business before they really know what they want or how to assess accurately the characteristics and quality of each firm's offering. During the course of the selection process, prospective advisors are asked to explain the strengths of their firm and their own background and to describe how they would manage the assets if the prospective client chose them. The prospective client tries to absorb this information with limited relevant experience and typically chooses the most attractive-sounding sales pitch without a thorough understanding of what they want to achieve or the likelihood of doing so.

Sidebar 1.1: Learning the Language of Wealth Management

Many people's experience with wealth management advisors is minimal at best. Making matters worse, the language of the wealth management industry is often mysterious and intimidating.

I am regularly reminded (usually by one of my children) of just how much a "language barrier" can incite feelings of misgiving and uncertainty. The latest reminder of this barrier comes in the form of Pokémon, the hugely successful Japanese trading card game based on mythical creatures pitted against one another in combat. Pokémon is a game at which my eight-year-old son excels, but at which I am at best an outmatched opponent. Pokémon consists of a complex world filled with hundreds of creatures—some that evolve into others—with myriad powers and weaknesses and all with unpronounceable names. Besides trading cards, there are also stuffed animals, television shows, "how to" books, and Pokémon T-shirts. My son is both an expert at Pokémon and a supremely

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confident Pokémon salesman. Here's a typical exchange that we might have in the course of playing a round of Pokémon:

Son: Daddy, why don't you battle this Cyndaquil against my Feraligatr? Cyndaquil is really cool; he has singe attack and an HP of 50!

Dad: What attacks does Alligator have?

Son: Not alligator, Daddy, *Fer*aligatr! He has slash attack.

Dad: Oh, okay. Well, can I use slash attack instead of singe attack with my Cindyquill?

Son: No, Dad. You have to play by the rules. You should know that…

As you can see, this conversation is already a slippery slope. After five minutes of talking with my son about the arcane details of Pokémon, my head is spinning. I don't remember what HP is, let alone whether 50 is good or bad. Singe attack doesn't mean anything more to me than slash attack. As I play the game, I never quite know when the rules change, and even if I did, my facility with the vocabulary of Pokémon is too rudimentary to argue my case. (My son knows this, of course.) In addition, I haven't read the small print at the bottom of the Cyndaquil trading card, which states that its weakness is slash attack. After my inevitable loss, I don't have to ponder very long whether my son has systematically memorized all the small print this game has to offer, with the intention of clobbering me every time we engage in battle. I know he has!

When faced with managing their wealth, many individuals find themselves in situations similar to those I face when I play Pokémon with my son. They must operate in alien territory, trying to understand the parameters of an unfamiliar game while being outmaneuvered by complex rules and a vocabulary they don't understand.

To further assist you in learning the language of wealth management, please see Appendix, "Learning the Language of Wealth Management." This is serious stuff, but it's also important to have a little fun with it.

After the new client chooses an advisor, both client and advisor are limited to solutions that the advisor can provide, whether or not they are advantageous to the client. Because most private wealth advisors don't generate revenue from a client until they have sold one or more products, and because many clients want the security of knowing their assets have been invested, there's often an unspoken urgency on both parties' parts to consummate investment arrangements and to lock the client into specific solutions, often with long-term consequences.

When they rush to action, most clients have not thought deeply about their financial, personal, or family goals, how to realistically achieve them, or their comfort with financial risk before hiring their advisors. So their advisors end up driving the agenda. Most advisors inquire about the client's financial situation and learn something about his/her goals, family situation, and personality. This classic approach leaves little incentive for advisors to explain the pros and cons of all the financial options available, especially low-cost, high-value ones. After interviewing a client, the advisor typically selects the firm's investment policy that most closely matches the expressed need. He then chooses an asset allocation from among the available options. Assets are divided by major category or asset class—stocks, bonds, cash, private equity, hedge funds, real estate—and a target allocation is assigned to each category so that the total equals 100%. Then the advisor reviews his firm's stable of available investment managers and recommends a subset that represents each asset class. The client then reviews the list, approves the recommendations, and invests the target amounts.

Within a month or two, and sometimes faster, the client's strategy is set, the assets are fully invested, and the revenues are flowing to the advisor's firm. From here on out, the advisor meets periodically with the client to review the performance of the portfolio, to offer suggestions for improvement, and to make any agreed-upon changes. This classic approach to wealth management (which, as you may already have guessed, I want you to avoid) can be broken down into five steps, as shown in Figure 1.1. This classic approach is standard across the industry, and it happens time after time.

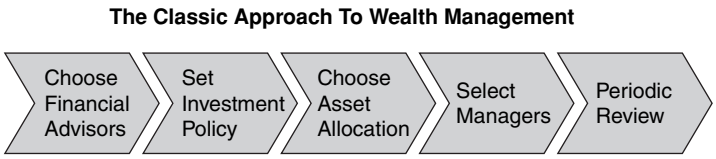

Figure 1.1 This is the standard process used by most wealth management advisors.

Strategic Wealth Management

Instead of the classically flawed approach I just described, this book focuses on a new way to structure your wealth management affairs. I call it "strategic wealth management." It's not that the classic approach is wrong. It's just incomplete. Like having a gun without a good aiming system, you're unlikely to hit your target. In contrast to the classic approach, strategic wealth management is a holistic approach to wealth management that *focuses on your interests*. It explores all of your strategic options and puts you back in the driver's seat while showing you how to employ your advisors to greatest effect. Your values, your skills and resources, and how you relate to your family are at the core of the strategic wealth management approach and are key elements of what I call the Strategic Wealth Management Framework©.

For example:

Do you want to use your wealth to reflect your deeply held values and beliefs? The Strategic Wealth Management Framework can help you design a wealth management strategy that does this.

Do you or members of your family have competitive advantages that you can leverage in the marketplace to drive increased returns on your assets? The Framework can help you do that, too.

Are there family members or others to whom you wish to pass wealth, as well as the skills to manage it well? The Framework provides guidelines for doing that.

How much risk are you comfortable taking? The Strategic Wealth Management Framework can help you determine the level of investment risk that is most in keeping with your investment skills, interests, and temperament.

Are there simple, low-cost, highly effective wealth management techniques that you can use to great effect and with little hassle? Yes. I show them to you.

In Figure 1.2, you will see yourself at the center of the Strategic Wealth Management Framework. *You* are the heart of the Framework. Early on, using this framework requires more time and effort to implement than the classic approach to wealth management. But it is a more thoughtful, systematic approach designed to help you manage your wealth according to your personal and family goals, whether for your lifetime or, in some cases, for multiple generations of your family. If you follow this framework, you will also get better performance out of your advisors, and in many ways you will be a more attractive client to them.

In Figure 1.2, projecting left and right out from the core are two arrows labeled Context and Infrastructure. In order to set a coherent strategy and then execute it, you will need to evaluate the context within which you wish to operate and build an effective infrastructure to achieve your goals, based on the reality of that context.

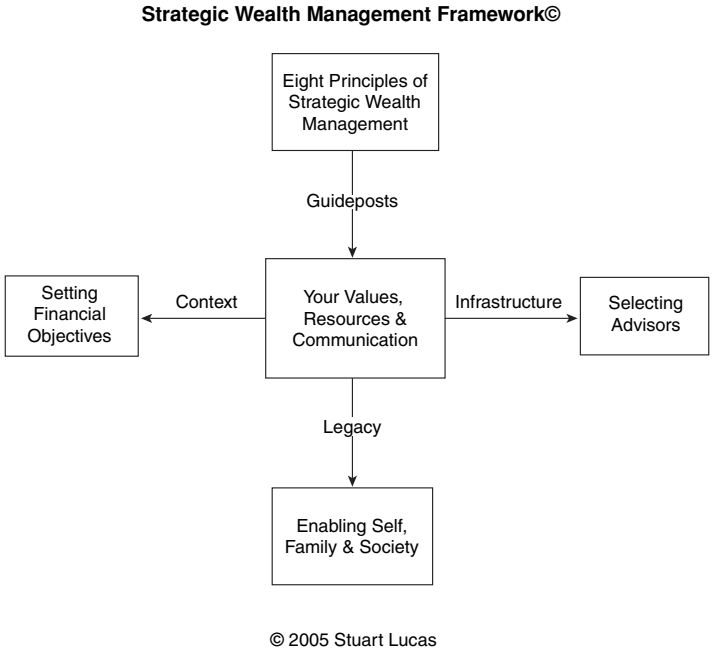

Figure 1.2 Use the Strategic Wealth Management Framework© to create a fully integrated plan that meets *your* objectives.

The external context in wealth management includes the financial markets and the many institutions that operate within its confines, the tax code, and for those who have a multigenerational timeframe, estate planning law. For those with philanthropic interests, the external context also includes the non-profit sector. It is critical to the success of this model that you examine the external context early in the wealth management planning process. Only by understanding the context within which you must make decisions and the specifications for an effective infrastructure can you set appropriate financial objectives and organize the right advisors to execute *your* wealth management strategy.

The dynamism of today's wealth management industry coupled with the complexity of family dynamics can make wealth management a difficult challenge. To help my family and my readers manage the process, I have devised the Eight Principles of Strategic Wealth Management to bring clarity and precision to our actions and activities within the Strategic Wealth Management Framework (see Chapter 2, "Eight Principles of Strategic Wealth Management"). I use these eight principles all the time. They are guideposts that keep me focused on the things that are most important. When decisions get complicated, the Eight Principles help me narrow my choices while maximizing the impact of those I make. They can do the same for you.

I know that the Strategic Wealth Management Framework and the Eight Principles of Strategic Wealth Management work because they have worked very well for my family and me. By using them

- You'll make sound wealth management decisions based on purposeful reflection, planning, and action.
- You'll select advisors whose skills and experience best match your financial objectives and wealth management strategy.
- You'll make sound investment decisions that are closely aligned with your investment skills, interests, and risk tolerance.

Finally, by embracing the Strategic Wealth Management Framework and the Eight Principles of Strategic Wealth Management, you'll be able to project your values and ambitions (and those of your family) outward into the external environment to achieve specific and concrete wealth management goals—*your* wealth management goals. When your

strategy is a success, you create a legacy that improves your satisfaction and significance and that benefits your family and society.

The Family as a Cultural System

No two families are alike. All families, wealthy or not, are complex, dynamic organisms that are forever changing cultural systems. The culture of a family, like any other cultural system, consists of the beliefs, values, attitudes, norms, and behaviors of its members. Each family's history affects its current culture. Individual family members influence one another in countless, complex ways. Numerous external forces influence the life, identity, and culture of a family as well. Marriages bring "outsiders" into a family, while death and divorce can shatter families and shift lines of power and influence. The extended families of spouses who marry into a family exert their influence too, bringing with them new issues of culture, heritage, business success, family dysfunction, and social prominence.

Still another factor that can color the dynamics in any family is the very presence of wealth itself. Money can be tremendously empowering and can afford its owners extraordinary opportunities. At the same time, money can complicate family relationships, foster resentment, and create dependency. At the extreme, poorly managed wealth can lead to degeneracy and even corruption.

I believe that wealthy parents—like all parents—need to be intentional about instilling values of accountability and responsibility in their children when it comes to the use of money. Indeed, doing so can be critical to the family's long-term survival! Many wealthy parents indulge their children financially. In so doing, they often foster economic dependency and create a generation of children that feels entitled to the benefits of wealth, but which is ill prepared to manage the responsibilities that wealth entails. Such children often become reliant on their parents for their lifestyles and often lack the discipline to use money wisely. It's no wonder that some people believe that passing wealth from one generation to the next is doing their heirs and society a disservice.

Not surprisingly, financial dependency can affect a family in significant ways. Just how do you go about raising a generation to be empowered

by its wealth, not filled with a sense of over-entitlement because of it? I don't know of a single wealthy parent who doesn't worry about this issue a great deal.

That's one more reason why wealth management is about so much more than money. It's also about fostering strong intergenerational values related to productivity, work, accountability, and personal responsibility. Doing this can ensure the health of families for multiple generations. The failure to do it can lead to family dysfunction and the rapid loss of wealth.

Taking Control of the Wealth Management Process

Using the Strategic Wealth Management Framework requires leadership—*your* leadership. Leadership is necessary to protect your financial interests and to reinforce a positive family culture. You must accept personal accountability for managing your wealth, regardless of whether you want to manage simply and conservatively or with focus and risk. It doesn't matter whether your goal is to build the next Rockefeller dynasty, launch a new start-up business, or hand over day-to-day responsibilities for wealth management to an advisor who has earned the moniker "trusted." In all cases, you, as the wealth owner, must take personal charge of your wealth management by assuming a role I refer to throughout the book as the "Wealth Strategist."

Sometimes the Wealth Strategist is an individual. Sometimes several family members work as a team to play the role. Typically, a first-generation wealth creator takes on the role him- or herself. In a multigenerational context, either model can operate successfully. However, in the multigenerational context, it is important that the Wealth Strategist serve at the pleasure of the family. Dictatorship as an American family governance structure tends to be fundamentally unstable, even when the position is earned through merit and sanctioned by the previous generation!

For those with substantial wealth and a multigenerational timeframe, a managed transition of the Wealth Strategist role from one generation to the next is a critical task. In turn, my great-grandfather, my grandfather, and then my father played the role of Wealth Strategist. Today, I share the

Wealth Strategist role with my brother William and my sister-in-law Melissa, though my father still plays an important oversight role. As a rule, our family believes in gradual generational transitions, not as a delaying tactic by the older generation to retain power, but to diligently work through the inevitable issues that arise. Time has been our ally in working out complex family and financial dynamics. It can be yours, too.

You and your family stand to benefit greatly from having a designated Wealth Strategist in place to work closely with advisors. Having been a wealth industry advisor myself, I know that the relationships I've built with designated Wealth Strategists from other families over the years make wealth management activities a lot easier and more efficient for everybody. If I'm able to work with a designated Wealth Strategist, we can optimize our working relationship in numerous ways. We use our time more efficiently, make better investment decisions during times of stress, and our decisions are based on a clearly understood set of operating principles and investment goals. As an educated client, you'll also delegate responsibility more effectively and you will confidently and accurately distinguish between good and mediocre performance.

The Nature of the Wealth Strategist's Role

The Wealth Strategist plays the critical role in developing and executing a family's wealth management strategy. He or she works closely with their family to define management plans and goals and then oversees implementation, coordinating the involvement of both family members and professional financial advisors as needs require. The key function is to integrate the advice and activities of various professional advisors and to make sure the advice is consistent with the overall wealth management strategy and goals and with the dynamics and priorities of the family.

Becoming a Wealth Strategist doesn't require detailed knowledge of investment theory, estate law, or the tax code. But, it does require the following:

- Patience and a long-term perspective
- The ability to foster good communication among family members
- Accurate assessment of your own wealth management skills and those of prospective advisors

- An informed layperson's understanding of how the wealth industry works
- Reasonable financial and managerial discipline

I'll have much more to say later in this book about the critical role of the Wealth Strategist. Suffice to say for now that the Wealth Strategist is in fact the CEO within your family, and it is the job of this individual or team to ensure effective wealth management over time.

Conclusion

This chapter introduced the Strategic Wealth Management Framework and the Eight Principles of Strategic Wealth Management and explained why it's so important for you, the wealth owner, to grasp the reins of control when it comes to implementation. Exercising strong leadership as a Wealth Strategist while following the Framework significantly enhances the productivity of your advisors, and will put you and your family on track to fully realize *your* wealth management goals.

Let's go on now to Chapter 2, where I talk in depth about the eight principles that are central to the effective management of wealth.

Chapter 1: Issues to Discuss with Your Family

1. Do you find the subject of wealth management intimidating? If so, why?
2. Are you convinced that "doing your homework" and planning ahead before hiring your wealth management advisors is a reasonable approach to take? If not, what forces compel you to act now? What are the long-term costs of acting prematurely?
3. Do you have a personal interest in closely managing your finances? If so, how much time are you willing to devote to this activity? If you do not have interest in closely managing your finances, can you structure your wealth management strategy accordingly?
4. Who is the logical Wealth Strategist for your family? Why? What if there isn't a logical choice or a consensus pick?
5. Does your family communicate well about money? How might communication be improved?
6. How would you describe the "culture" of your family? In what ways do your family's beliefs, values, attitudes, and norms shape behavior when it comes to spending and saving?
7. Has your family taken time to articulate its "culture" and how that culture should drive future wealth management planning efforts?
8. Have you ever hired someone to manage your finances? Was it a positive or negative experience? If it was negative, how can you improve things in the future?
9. Do you know how to assess the relative merits of prospective advisors? How do you know you've assembled the best alternatives to choose among instead of a middling pool of talent? (Hint: Brand alone is not the answer.) After you've hired an advisor, how and when will you know they're doing a good job?
10. What advantages do you see in using the Strategic Wealth Management Framework as a tool in wealth management planning instead of the classic approach?

Endnotes

[1] William H. Gates, Sr., and Chuck Collins, *Wealth and Our Commonwealth* (Beacon Press, 2002), pp. 9-10.