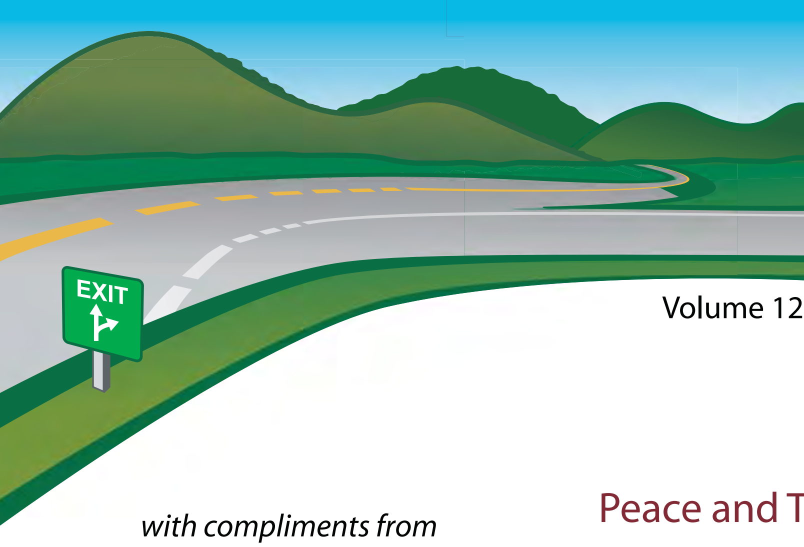

Changing Lanes

Transition planning for entrepreneurs and family businesses

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with compliments from

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Guiding Family Business, from Now to Next

Peace and Tranquility at the Cottage – Or Not?

Folks all across North America have fond childhood memories of their family's cottage, particularly the fun activities such as campfires and fishing with siblings and cousins. As adults, that family cottage became an oasis — a place where they could escape the rat race to relax and enjoy some peace and tranquility on weekends and vacations.

It's not surprising that over eighty percent of families feel strongly that the cottage should be passed down to future generations. Parents and grandparents want to keep the family connectedness of yesteryear alive and well, and their now-adult children anticipate recreating that happy environment for their offspring. In situations where the cottage was literally built by the parent or grandparent, the emotional pull of the property is even greater. However, gifting or selling the cottage to multiple next generation family members is not without drawbacks.

An estimated 97% of today's cottages are owned by more than one family member with 11% reporting that they have already experienced some conflict among co-owners. Another 22% anticipate feuding going forward. While shared ownership of the family cottage can be manageable when the senior generation is alive and providing leadership and guidance, preventing disputes in subsequent generations will require advanced planning to discuss and agree on how both financial and non-financial decisions will be made and responsibilities shared. Often dubbed "the cottage rules", issues around the sharing of costs, completing repairs or renovations, paying bills, allocating cottage time to each member, bringing guests, and/or renting to non-family members are just some of the policies to be determined. Successful families not only collaborate to find common ground, but then document their decisions as policies for what is essentially a "cottage agreement".

Adopting this same mindset is a critical component of a successful inter-generational transition and ongoing management of the family wealth. In this edition of Changing Lanes we explore the need to proactively create **POLICIES** or guidelines for managing and deploying wealth going forward — policies that will act as a reference point for future decisions and actions.

Inside....

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Build on the Philosophy

Having invested the time to explore your personal convictions and clarify your own philosophy around wealth, you are now ready to initiate the **PLACES TO TALK** (introduced in the previous issue of Changing Lanes) and begin engaging the next generation in a meaningful dialog. The objective is to compare your **PHILOSOPHY** around wealth with theirs, understand each other's perspectives, and ultimately agree on what will drive your inter-generational wealth transition plan.

Remember that this active participation is essential to creating alignment around what will eventually become the family legacy, **and** raising your confidence that the next generation will be good stewards of the wealth.

The outcome will be the development of guidelines for managing, protecting and sharing the family wealth — **POLICIES** or imperatives that will ultimately be documented and communicated through a number of integrated plans.

Key steps to achieve this desired outcome:

- We suggest you first share the article entitled **DEFINE YOUR WEALTH PHILOSOPHY** (included with the third of the Ten P's) with all stakeholders and ask that they independently consider the conversation starter questions provided in that article.
- Each stakeholder should then record their personal philosophy for all the conversation starter questions. This will ensure that, together, you capture what each member believes is fundamental to protecting and transitioning the physical, social, and intellectual assets that collectively make up the family wealth. To recap, the conversation starter questions posed in the wealth philosophy article cover a number of topics including the following:
  - Assignment for lifestyle needs versus legacy building.
  - Reinvesting versus distributing the wealth.
  - How the wealth might be shared (for example: merit or need versus entitlement; individual versus household).
  - Supporting others through philanthropic pursuits or charitable giving.
- The next step is to compare and contrast the input from all stakeholders to see where philosophies are aligned. If there is significant disparity, we recommend engaging a facilitator to help examine the pros and cons of the individual viewpoints and guide the group towards consensus.
- Once there is an alignment of convictions, it is time to develop the policies that will:
  - Communicate common philosophies and stipulate how they will be upheld.
  - Form the basis of the plans that will direct and support the desired outcome.
  - Act as a touchstone for all discussions and decisions going forward.

For examples of the types of policies that are fundamental to a well-prepared inter-generational wealth transition plan, see page 3.

The Ten P's – Number Six

In the first five of the Ten P's, our focus was on identifying common ground as the basis of an inter-generational wealth transition plan that has a clearly-defined purpose for the wealth. Our objective was to:

- Help you clarify your desired purpose or outcome for the wealth transition — i.e. "where you want to go".
- Provide you with tips and techniques to use in exploring "what" is most important to you and yours, and "why".

With this greater clarity around the "where, what and why", it is now time to define the "how you will get there".

This edition of Changing Lanes explores number six of the Ten P's. Specifically, the focus is to highlight the importance of developing **POLICIES** that will support and enhance effective management and deployment of the family wealth going forward.

These policies will form the basis of the plans that will be implemented to manage and protect both the tangible and intangible capital — those assets that span the three overlapping types of wealth — physical, intellectual and social capital.

For an overview of all items that comprise the Ten P's of a Successful Wealth Transition, review the first issue in the series.

Formulate the Policies

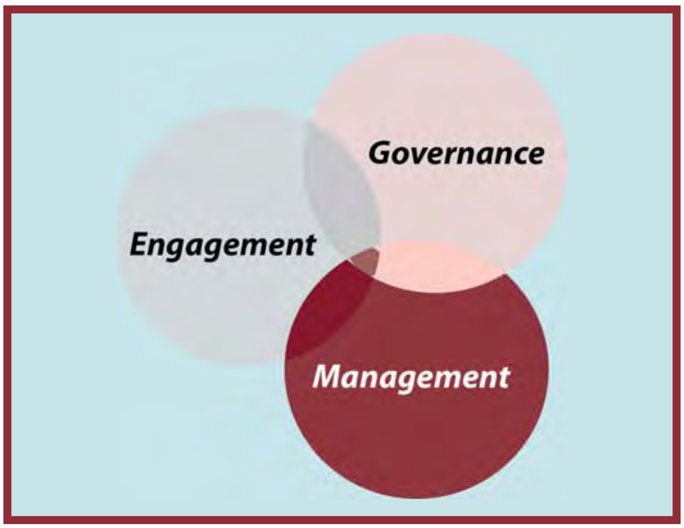
Similar to the purpose for having "cottage rules", setting policies around the overall strategy for transitioning, managing and preserving the wealth will ensure there is a high level of clarity around:

- What is to be done and why;
- How it is to be done; and
- Who is to do it.

Such policies might range from a set of more liberal standards and guidelines designed to be educational, to very prescriptive or directive rules and regulations that are to be enforced. To help families focus their discussions and delve deeper into formulating policies, we have separated the imperatives into three distinct but overlapping groups:

Engagement

This imperative is focused on creating a culture of engagement and getting commitment among stakeholders around "what is to be done and why". It requires communication and **PARTICIPATION** by all to develop policies that will ensure actions always align with the "why" (the common **PURPOSE**, **PRINCIPLES** and **PHILOSOPHY**).



In general, families of wealth appreciate the importance of developing policies that lay out stakeholder responsibilities and aim to create a sense of ownership. Achieving the required level of stakeholder commitment can be supported by an education policy that provides appropriate financial literacy for family members, supported by real life experience in money management, as well as clarity around the rights and responsibilities that accompany the inheritance. An education policy also serves to build additional, more intangible wealth within the successor generation, specifically from the skills, commitment, and sense of stewardship that the learning experience generates.

One of the first steps taken by the Patel* family was to calculate how much money would be required to meet the lifestyle needs of each stakeholder versus how much could be invested in the longer-term family legacy. They also considered whether or not their policy would be sustainable if the number of family members multiplied significantly in subsequent generations.

Across the country, the Spencer* family debated whether the inheritance, along with the authority and responsibility for managing that inheritance, should be shared equally among the three second generation family members (who would in turn determine how to divide their one-third among their respective offspring), or if all eight members of the third generation would have an equal share of the wealth and an equal say around how that wealth might be deployed.

Each family of wealth needs to find their own balance between family first and wealth first principles and set policies accordingly. Once set, these policies can be documented in a rule book that is commonly referred to as a Family Constitution.

Governance

Some form of a decision-making structure is required to oversee the implementation of the family's wealth strategy. Every family of wealth needs a governing body that will be responsible for determining and implementing the "how it is to be done" policies while also ensuring accountability among those assigned to the "who is to do it" imperative.

This role is commonly undertaken by a Board of Directors that has the authority to make decisions on behalf of the stakeholder group. While it is conceivable that all stakeholders are seated at the boardroom table in the beginning, most families grow to the point where it is necessary to instead appoint one or two individuals to represent each branch of the family.

The governance imperative typically covers decisions and policies around capital preservation and risk management. This would involve a myriad of financial, legal, compliance, tax, compensation, contingency and reporting matters. Specifically, the Board of Directors would be responsible for ensuring there were documented policies, appropriate records, and formal agreements around "how" the wealth will be invested, divested, protected and preserved, both at the family and individual level.

Continued on Page 4

** Names have been changed to ensure confidentiality*

Formulate the Policies continued

With a significant real estate empire to protect, the Huang* family set up a formal Board to deal with all the legal and financial reporting complexities. For them it was imperative that the capital remain in the family at all times, so the Board also developed a risk management policy that included life insurance to provide liquidity upon the death of each stakeholder, pre-nuptial agreements to protect against an involuntary sale of property as the result of a divorce, and estate plans for all adult family members. In addition, they set policies for paying dividends to provide stakeholders with financial independence.

Good governance has two major components — sound decision-making and accountability around subsequent implementation of those decisions. The key to both is inclusiveness and transparency. In ensuring effective governance of their inter-generational wealth transition, the Coffey* Board of Directors was tasked with developing guidelines for "how" the family's culture, principles and risk tolerance could be supported and upheld through appropriate investments and philanthropic initiatives that were directly aligned with the philosophy and strategy set by the stakeholders. They were transparent in their approach, even including policies for selecting their financial advisors.

A forward-thinking board will also develop policies for the more unexpected and unlikely events, such as "how" the family will deal with issues caused by adoption, mental incapacity, substance abuse, bankruptcy, fraud, or perhaps even kidnapping.

Management

The "who is to do it" is the final piece of the puzzle. With clear policies in place around the engagement strategy and a governing body focused on ensuring there are no ambiguous standards around how the wealth will be transitioned and preserved, it is now time to establish guidelines for appointing, selecting or hiring the people who will administer the initiatives required to effectively manage the wealth transition and preserve and grow assets over the long-term.

The policies developed in the other two imperatives will have provided some indication of the depth of the wealth management / administration roles. From this information, we recommend developing an ARA for each role required. An ARA is a policy that outlines the **A**uthority, **R**esponsibility and **A**ccountability that will accompany the title of Wealth Manager or Wealth Administrator. Be sure to check that all important responsibilities have been covered and that there is no duplication between roles.

From the clarity provided by the ARAs, it will be easier to identify the instincts, skills and competencies that are most likely to predict success in each role. Add to this list any preferred prerequisites with regard to education and prior experience.

This ARA and competency list were invaluable in helping the Dobrinski* family formalize their wealth management process. Instead of merely accepting his nephew's request for the job, Hermann took the time to inventory what the role required and then compared the nephew's financial and investment skills and experience. He identified areas where further personal and professional development would be required and set the expectations up front. Taking this proactive approach was a key step in avoiding potential disagreements some time later.

Integrating the policies for each imperative not only provides clarity, awareness and education around the family wealth philosophy, but also acts as a touchstone for addressing current or impending issues. More importantly, having defined policies encourages stakeholders to be proactive in the consideration and discussion of hypothetical or longer-term matters.

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