

# MICHIGAN PROBATE & ESTATE PLANNING JOURNAL

## TABLE OF CONTENTS

Vol. 26 • Winter 2006 • No. 1

### Feature Articles:

2006 Desktop Reference on the Economics of Probate and Estate Planning Practice in Michigan ..... 3

Attorney and Estate Planning Client Relationships and Practices Involving Charitable Planned Giving in Michigan ..... 35

Preparing Heirs for the Challenges of Wealth  
Ron Yolles ..... 52

Swatting Gnats, Ignoring Elephants  
Hon. Kenneth L. Tacoma ..... 56

Drafting a Flexible Irrevocable Life Insurance Trust, Part 2  
Julius H. Giarmarco ..... 59

New Law Clarifies Funeral Rights  
Douglas G. Chalgian ..... 66

### Plus:

Uniformity of Practice—Are We There Yet?  
Joan C. Von Handorf ..... 68



## Preparing Heirs for the Challenges of Wealth

By Ron Yolles

"Some parents spend more time preparing estate documents than preparing their children for the wealth and pressures that result from those documents."

### Part I: Background Information

#### Data Re: Estate Transitions

Research evidence outlined below suggests that inherited wealth is often more of a curse than a blessing. In this context, "preparing heirs" involves teaching them skills that will help them lead an independent and fulfilled life, immune from the dependence, resulting ills, and loss of initiative that inherited wealth often creates.

Based on conservative estimates, \$40.4 trillion will pass to heirs by the year 2052, or about \$800 billion per year plus an additional \$11.6 trillion that will be donated to charities.<sup>1</sup> So preparation to help heirs and families improve their effectiveness is essential.

Research data indicates that approximately 70 percent of estate transitions fail—where failure is defined as the second generation involuntarily losing control of the family business or a significant part of the family's wealth.<sup>2</sup> More importantly, several of these research studies illustrate that the primary cause of failure in wealth transitions is a high degree of splintering, divisiveness, and lack of communication within the family.

One of the most comprehensive studies on wealth transitions and preparing heirs was completed in 1994 by Family Coach and author Roy Williams and Professor Michael Morris, PhD, of Syracuse University's Whitman School of Business, which was summarized in William's book *For Love & Money: A Comprehensive Guide to the Generational Transfer of Wealth* (San Francisco, CA: Reed Publishers, Inc., 1997). They studied 3,250 affluent families between 1973 and 1994 and confirmed the 65 to 75 percent estate-transition failure rate, isolating the following causes:<sup>3</sup>

- 60 percent of the failures were due to breakdowns in trust and communication within the family unit
- 25 percent of the failures were caused by inadequately prepared heirs
- Less than 3 percent of the estate-transition failures were caused by incompetent advisors, lawyers, and accountants
- Approximately 12 percent of the failures were due to lack of a family mission or purpose that clearly defines the use of the family's wealth

#### Heirs Are Ill-Prepared

Not surprisingly, affluent families are concerned with the effectiveness of both their estate plans and the steps that they've taken to prepare their heirs for the challenges of wealth. A recent nationwide survey by U.S. Trust Company (New York, N.Y., June 6, 2006) indicated that the greatest concern to 83 percent of affluent Americans is that their children will have a tougher time financially. Additionally, 55 percent of those surveyed felt that their children were naïve about the value of money and placed too much emphasis on material things. In addition, 34 percent were concerned that their children would find a spouse who was only interested in their affluence.

Affluent parents' concern about the preparation of their children is justified, because the evidence is strong that wealth is often built by an entrepreneurial first generation and then dissipated by the second and third generations. Based on studies of affluent families between 1973 and 1996, while both were serving as professors at the University at Albany, State University of New York, Thomas Stanley, PhD, and William Danko, PhD, in their best-selling classic *The Millionaire*

*Next Door* (New York, N.Y.: Simon & Schuster, 1996), offer the following insights on building and preserving affluence:

- 67 percent of U.S. millionaires were self-employed entrepreneurs who saved over 20 percent of their annual income
- 80 percent of millionaires were first generation (i.e., not inheritors)
- While millionaires lived well below their means, inheritors exhibited the exact opposite behavior by not saving any money and spending more than they earned
- 80 percent of millionaires have college degrees and 40 percent have graduate degrees

Stanley and Danko found that there was an inverse relationship between cash gifts to children and both the net worth and wealth that those children were able to accumulate. They termed these cash gifts "Economic Outpatient Care (EOC)" because the gifts created a dependency on handouts from Mom and Dad. For example, CPA's and attorneys who received cash gifts from their affluent parents had 57 percent and 62 percent of the net worth and 78 percent and 77 percent of the income respectively of their peers who did not receive cash gifts. This inverse relationship between cash gifts and financial success applies over all occupational groups except professors and teachers who save and invest the cash gifts given to them.

Predictably, the ultra-successful children of the affluent who become corporate executives and physicians became even more financially successful because they were not given cash gifts; whereas, their less successful siblings became increasingly dependent on their parents and never developed sound financial habits.

### **How Some Families Succeed**

Outlined below is a process for families to follow in order to prepare children and grandchildren for the challenge of managing significant

wealth and/or a family business. Part of the discussion focuses on how children, and ultimately grandchildren, can learn to work effectively with professional financial, tax and legal advisors and/or the professional executive team managing a family business when those heirs themselves are not directly involved in the family business. We draw on research, which shows how families can cooperate and collaborate to make wise planning decisions for all family members and develop self-sufficiency as opposed to dependency among the younger generation.

In the 30 percent of affluent wealth transitions that were successful, Williams and Morris found three broad common elements:<sup>4</sup>

1. **Candid Communication.** There was a tremendous degree of trust, openness, cooperation, and mutual respect among family members. This was in sharp contrast to the pattern in the families where estate transitions failed, and where parents communicated more with professional advisors than with their children.
2. **Independent Achievement/Meritocracy.** Only after achieving independent, academic, and career success were heirs allowed to choose to become involved in either managing the family's business or assets. At the time of transition, these heirs indicated to researchers that they felt "well-prepared" to take over.
3. **A Written Plan.** Families whose transitions were successful prepared a formal succession plan and family mission statement, which included concrete steps to train (and test) heirs. These families also laid the groundwork for their children to have successful working relationships with competent professional advisors.

## Part II: Steps to Prepare Heirs

### Five Basic Steps

In addition to the three steps above, there are several steps that parents should take to help their children avoid the pitfalls of inherited wealth:

1. Conduct **regular family meetings** where open dialogue is encouraged and professional advisors are often present to help facilitate discussion and ensure that every adult family member's point of view is heard and a consensus achieved.
2. **Encourage teamwork** and a sense of objectivity and fairness within the family so that even when a decision does not go a family member's way, he or she realizes that the decision making process was fair and is able to wholeheartedly embrace the direction that the family decided to take.
3. **Do not make cash gifts** to children before they are ready (often age 35+), but rather invest in their and their children's college education. As mentioned, in *The Millionaire Next Door*, Stanley and Danko found that there was an inverse relationship between cash gifts to children and both the net worth and income that those children were able to earn. They suggested teaching children to save 20 percent of their income each month and to live within their means.
4. **Allow children to learn from failure** and encourage an environment where all family members, including parents, can candidly assess their own strengths and weaknesses. Don't act as a safety net unless health and well-being is involved.
5. **Encourage** your children to pursue their passion, not yours.

### Real Communication Examples

On this last point, many experienced professionals are aware of cases where children achieved independent success and then "came back" to run a family business. Just this month we heard directly of two such cases: 1) After experiencing success in a "fast-paced" career environment, a daughter and her husband came to appreciate the value in returning home to run a family business that was founded in the 1960's; 2) two successful attorneys returned home to take over a 50-year old business from their ailing father and took the business to a new level as they embraced the information age.

Families should strive to create a culture of openness in which all family members over the age of 14 are welcomed and encouraged to understand at least some aspects of the family's wealth and to participate in the decision-making process. Additionally, some steps should be taken from a young age to make sure that children learn to appreciate the value of a dollar and develop sound educational, work, saving, and money management skills. These skills need to be honed and developed from the time that kids are toddlers through middle age.

This open communication process can be picked up at any point during a child's life cycle. It is perfectly appropriate for elderly parents to work on collaborative decision-making, money management, and business skills with both their middle-aged adult children and young adult grandchildren. Additionally, all children from a young age should be made to feel that their opinion is valued and respected in important family matters.

### Part III: Summary

The evidence is strong that even a sound estate plan will fail if steps are not taken to prepare heirs. Even if communication within a family is less than ideal, the family's investment manager, attorney, and CPA working as a team can help lead a family meeting that encourages mutually

productive dialogue. If necessary, experienced family coaches with training in psychology can be brought in to break down barriers and facilitate discussion.

### Notes

1. The Boston College Center on Wealth and Philanthropy has done groundbreaking research on estate transitions including John J. Havens, PhD, and Paul G. Schervish, PhD; "Why the \$41 Trillion Wealth Transfer Estimate is Still Valid," (Boston, MA; January 6, 2003); *Wealth Transfer Report*; Boston College Center on Wealth and Philanthropy.

2. A summary of some of the studies illustrating this 70 percent failure rate are as follows:

(A) J.H. Astrachan, PhD and M.C. Shanker, PhD; *Family Businesses' Contribution to the U.S. Economy*, Family Firm Institute (Brooklyn, MA; August 28, 2005) Web site home page summarizing findings from the *Family Business Review Journal* ([www.ffi.org](http://www.ffi.org)). (Only 30 percent of family businesses survive to the 2<sup>nd</sup> generation; 12 percent to the 3<sup>rd</sup> generation and 3 percent to the 4<sup>th</sup> generation).

(B) Victor Preisser, MBA, "Preparing Heirs: Successful Estate Plans for Wealthy Families Require Open Communication, Participation Across Generations", *Stanford Business Review*, 72:3 (May 2004) Pages 18 -20. (Quotes 65-75 percent failure rate of estate transitions).

(C) John A. Davis, PhD, Chairman, Harvard Business School's Families in Business Program; quoted in *The Wall Street Journal* (Saturday, July 1, 2006, page A8). (Re: 70 percent failure rate of estate transitions).

(D) Richard Beckard, PhD and W. G. Dyer, Jr., PhD, "Managing Change in the Family Firm: Issues and Strategies", *MIT's Sloan Management Review*, 24:3 (Spring 1983). (Many of the 70 percent of family firms that fail would survive if the owners better understood how to manage change within their family and did explicit transition planning in conjunction with their family.)

3. Williams synthesized this same survey data in the following: Roy Williams and Victor Preisser, *Preparing Heirs: Five Steps to the Successful Transition of Family Wealth and Values*, (San Francisco, CA: Reed Publishers, Inc. 2003).

4. *Id.*



Ron Yolles, JD, CFA, is a Principal at Yolles-Samrah Wealth Management, LLC, Bloomfield Hills. The firm was twice recognized by Bloomberg Media, LP as one of the country's 60 leading multi-family office firms. He is a former member of the Charles Schwab & Co.

Institutional Advisory Board. Mr. Yolles received a BA with honors from the University of Michigan in 1982 and a JD from the University of Michigan Law School in 1985. He earned his Chartered Financial Analyst (CFA) designation in 1991 from the Institute of Chartered Financial Analysts. He is a past Director of the Investment Analysts Society of Detroit and a founding member and Director of the Council of Independent Financial Advisors (CIFA). Ron has served on Charitable Endowment Boards with stewardship over \$400 million in assets. In 1998, he published the best-selling retirement book, *You're Retired, Now What? Money Skills for a Comfortable Retirement* (John Wiley & Sons, Inc., New York, 1998). He was twice recognized by *Worth* magazine as one of the top financial advisors in the country. His second book on retirement, *Getting Started in Retirement Planning*, was published by Wiley in 2001.