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Family Values, Family Wealth

Inspire, involve and inform your children to help preserve your financial legacy and traditions.

As global economic woes hit home, even families of the greatest means were forced to reassess how they can preserve their financial legacies for generations to come. But the greatest risk of losing family wealth may have less to do with market forces, and more to do with how families manage their legacy planning in both good times and bad. A recent study by the Williams Group, a family wealth consulting company, underscores the problem: As many as 70% of wealthy families actually lose control of their wealth by the end of the second generation, and 90% by the end of the third. It's an alarming statistic that unfortunately bears out the adage, "From shirtsleeves to shirtsleeves in three generations."

The risks may be greatest among families that fail to communicate across generational lines—and, as a result, fail to prepare younger generations for what's ahead. During the next fifty years, the post-World War II generation will pass along its wealth to heirs and philanthropic causes. These benefactors are looking for an enduring legacy that goes beyond dollars and cents. "People may lose sleep over the economy," says Stacy Allred, Director of the Wealth Structuring Group at Merrill Lynch, based in Bellevue, Wash. "But their greater worry for the long term may be whether their children will handle the responsibilities of wealth."

What they can learn during a downturn may ultimately strengthen a family, says Allred. "For younger family members, seeing the bottom of the markets gives some perspective as they face the future." But creating a solid family legacy requires much more than knowing how transitory wealth can be. It takes a concerted approach to educate the next generation on financial matters and set a course for philanthropy and other good works.

EDUCATION FOR ONE AND ALL

Making younger members feel they have a stake in that family legacy depends, paradoxically, on making sure they feel free to follow their own paths, says Charles W. Collier, senior philanthropic advisor at Harvard University and author of *Wealth in Families*. Collier frames the challenge this way: “How can you, the parent or wealth holder, encourage your children to lead their own lives while staying connected to the family?”

Collier argues that the most successful multigenerational families are characterized not only by an emphasis on hard work as a prerequisite for a fulfilling life, but also by a willingness to “invest in the dreams of the second or third generation.” Rather than being a significant advantage in accomplishing these goals, wealth can actually create problems if the younger generation feels obligated to follow closely in the footsteps of the wealth creators. Yet the notion of pursuing their own ambitions can be daunting for children whose parents, the wealth creators, have accomplished so much, according to James E. Hughes Jr., a family wealth consultant and author of *Family: The Compact among Generations*. Having to match their parents’ or grandparents’ often unattainable example can cause some children to distance themselves from the family. Though privileged in terms of wealth and comfort, they may feel overwhelmed by the pressure to excel and reject family unity. “The problem of the second and third generations is much more complex than most people understand,” Hughes says.

A HABIT OF SUCCESS

Most family fortunes are created through a combination of hard work, visionary ideas and disciplined execution. Lee Hausner, a Los Angeles psychologist and business consultant, thinks families can overcome the shirt-sleeves-to-shirtsleeves phenomenon by applying the same standards to maintaining family traditions and financial stability that made the family successful in the first place. It’s a matter of fostering a family habit of success, which includes a sense of the responsibilities and foresight needed to maintain family wealth and use it wisely.

Keeping the family in good financial shape is vital, of course, but that’s hardly the only concern. “Total wealth is a broader concept,” says Hausner. She and other experts often refer to four distinct types of capital—human, intellectual, social and financial—each of which must be put to work if the family is to establish and sustain its legacy over multiple generations (see “The Four ‘Capitals’ of Family Wealth”).

Before a family can define its legacy, it must articulate a vision. That’s normally the responsibility of the senior generation (the wealth generators or those who currently have the greatest control over family assets). To help them in this process, Allred conducts a six-hour “values retreat” with only these few family members, whom she likens to “co-CEOs” of a business.

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“It’s a time for them to be very reflective,” says Allred. “We talk about what they want their legacy to be, and about the opportunities and challenges their family faces.” By day’s end, the conversation has produced a written, bulleted value statement outlining the family’s core beliefs and objectives.

MEETING UP

Once the leaders of the family outline their goals and values, a family meeting can be an invaluable next step for educating younger family members and for creating a sense of shared purpose. Consider a yearly meeting at which the family can cover several distinct segments in the agenda. Allred recommends periods of discussion and learning with experts on hand, alternating with family-only recreation time, which helps foster unity.

Structured time for education gives everyone a chance to learn about the family wealth and its management. “That doesn’t necessarily mean opening the balance sheets for everyone,” Allred says. “This is about sharing the right amount of information at the right time.” A Private Wealth Advisor can explain the complexities of the family’s situation, describe various investment options or discuss the state of the economy. Though what is discussed will vary according to each family’s needs, topics might include estate and tax planning issues affecting the whole family; family history, with each family member sharing personal dreams and goals;

or even discussions of the meaning of wealth or other subjects. That could lead into a final session during which family members talk about underlying priorities, including philanthropy. “This gives the entire family the opportunity to see the bigger picture,” Allred says.

FAMILY STYLE

To preserve traditions, a family needs strong governance that defines a clear decision-making process and the roles various family members play in making those choices. There needs to be sufficient structure to set out rules members can follow, yet enough flexibility to accommodate individuals’ evolving needs.

“Begin by making joint decisions on simple subjects,” suggests Hughes, who notes that governance and communication are inextricably linked, and that it’s important to settle on ways of keeping in touch that work for a particular family. Some families communicate most effectively through e-mails; others like to set time aside during the holidays or vacations for face-to-face meetings. It also helps to think about who in the family naturally falls into certain roles, such as making arrangements for meetings or setting an agenda.

Next, consider how to formalize a process for making larger family decisions. A wealth consultant, after observing family dynamics, can suggest a customized approach that fits a family’s style, Hughes says. And whatever governance system is established, it needs to remain flexible enough to accommodate new members. Otherwise—if, for example, a family trust enforces rigid rules without seeking input from grandchildren—the younger generation may come to resent what it sees as a lack of respect and support. “A trust should not harm the ability of each person to live out his or her dream,” says Hughes.

A LEGACY OF PHILANTHROPY

Philanthropy, which is often a cornerstone of a lasting family legacy in good times, can still serve that purpose, even in times of economic difficulty. To be sure, donations may decline and some tax advantages (like reducing capital gains taxes by putting appreciated assets in a charitable trust) can lose their appeal. “But that doesn’t override a family’s desire to create its own philanthropic legacy,” says David Ratcliffe, Director of the Center for Philanthropy and Nonprofit Management at Merrill Lynch. Most philanthropic families continue to give during recessions, and contribution levels tend to rebound with the economy.

Although the senior generation may guide the process,

The Four “Capitals” of Family Wealth

Wealth is not confined to dollar signs. In fact, family wealth experts insist that a multigenerational legacy rests on these four cornerstones:

Human capital. The strengths and skills of each member can contribute to the family’s shared vision and values. To develop a family’s human capital, it is important to establish standards for supportive parenting and grandparenting, for communication among family members and for conflict resolution and team-building.

Intellectual capital. To promote intellectual development and help members meet career and life goals, the older generation can advise and mediate as younger members develop the processes to keep the family going. And supporting individual career choices enables family members to reach for their dreams rather than feel forced down paths someone else has chosen.

Social capital. “Together, a family can establish its overarching values and initiatives,” says David Ratcliffe, Director of the Center for Philanthropy and Nonprofit Management at Merrill Lynch. Whether expressed through a philanthropic foundation or individual gifts, a family’s strong social and philanthropic vision can help define a multigenerational legacy.

Financial capital. Family members need to understand not only how to grow and maintain wealth but also that money comes with significant responsibilities as well as opportunities.

every family member needs to feel vested in the family’s philanthropy, Ratcliffe says. Consider a couple in their sixties who are eager to support worthy causes and also want to instill in their children and grandchildren a strong sense of the family’s values. “They should communicate to younger generations that wealth brings responsibility,” Ratcliffe says. “The more they can get the generations working together, the better.”

If the couple simply tells the rest of the family about the gifts they are making, there may be little engagement. “If the younger generations feel it is Mom and Dad’s money and that they are going to do what they want with it, they may divorce themselves from the whole process,” says Ratcliffe. To avoid that unwelcome result, the family might enroll children and young adults in a program such as Merrill Lynch’s Financial Boot Camp, an intensive but fun course in the basics of investment and wealth management. Philanthropy and the use of wealth in family foundations is a core session in the Boot Camp program that always gets participants talking and can help energize younger family members and prepare them to assume a greater role in the family’s philanthropy.

A family foundation can also serve to bring multiple generations into the philanthropic process. With important, well-defined roles for each member, a

FAMILY VALUES, FAMILY WEALTH

foundation gives the family broad control over the size and types of grants it makes to charities, as well as the investments that keep the foundation going.

Because of the administrative costs and oversight required, foundations are best suited to families with substantial assets. Foundations average \$1.5 million in assets and are most efficient when they have at least \$3 million to \$5 million, says Ratcliffe. And family members must be prepared to make a significant commitment. “You’ve got to strategize for the long term,” he says, “because most foundations are created for perpetuity. You need to carry out succession planning and to engage the next generation’s interest in managing and maintaining the foundation.”

Younger family members might get involved through a junior board charged with developing its own philanthropic strategy. Junior board members would be authorized to identify appropriate charities and make recommendations to the foundation’s regular board. Or the junior foundation might be given authority over a specified amount—say, 10% of the foundation’s annual gifts.

Once grants are made, the junior board would be responsible for overseeing how the money is spent. If the family is geographically dispersed, the foundation

might choose to create a series of donor-advised funds through local grant-making organizations, known as community foundations, in the cities where younger family members live. Community foundations could provide valuable advice about the greatest needs and most reputable charities in their areas. The younger family members could then become donor advisors, with a key role in directing money into their community. Engaging the younger generation in this way also helps older family members identify likely future leaders who can perpetuate the family legacy.

Instilling passion in younger generations requires more than merely retelling the patriarch’s and matriarch’s stories; rather, the young must feel empowered to write their own stories. After all, says Hughes, “you can be a good steward of someone else’s dream only when you’ve been a good steward of your own.”

The Private Banking and Investment Group understands the responsibilities that come with substantial wealth. Your Private Wealth Advisor is singularly positioned to discuss these issues with you and your family and to help implement solutions on your behalf.

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