SUSTAINING WEALTH

Whittier Trust

From Myth to Reality

FORBES BRAND VOICE 2021

Lessons Learned From History

At his death in 1877, Cornelius Vanderbilt was considered the richest man in the world. Less than a century later, 120 of Cornelius' descendants gathered for a family reunion at Vanderbilt University. None of the family members in attendance were still millionaires.

In a research paper provocatively titled "The Myth of Dynastic Wealth: The Rich Get Poorer", Robert Arnott, William Bernstein, and Lillian Wu explore how wealth erodes over time. Their findings? The rise and fall of the Vanderbilt fortune is more common than you think. Relative to the wealth of the average American, inherited wealth declines by 50% every 20 years. That represents an 88% reduction in relative wealth every 6 decades. As the saying goes: "from shirtsleeves to shirtsleeves in three generations."

A Holistic Approach

While the researchers focused solely on the wealthiest American families, their findings have broader implications. Family business owners and executives, focused on the difficult task of building wealth, may overlook obstacles in sustaining what they have built. Fortunately, these obstacles are not insurmountable.

At Whittier Trust, we have helped hundreds of families sustain and grow wealth over multiple generations. Our success is built on a holistic approach to wealth management, where we focus on both your finances and your family.

Balance Sheet

The first step of our approach is to determine where things stand today. To accomplish this, we help our clients create holistic balance sheets. A holistic balance sheet lists all of your assets and liabilities, including unique assets like art or stock options. It is a comprehensive snapshot of your total net worth.

Trying to execute a wealth management plan without first creating a holistic balance sheet is like trying to use a map without knowing where you started. The balance sheet is a "you are here" icon for your financial life.

Cash Flow Analysis

After creating your holistic balance sheet, the next step is to examine your personal cash flow needs. We use simulations and scenario analysis to determine the size of the asset base needed to support your lifestyle.

Without an effective cash flow plan, unexpected liquidity needs could force you to sell equities during a market drawdown. Selling stocks at depressed valuations makes it difficult for your portfolio to recover when markets rebound. Investors caught in this trap can turn temporary losses into permanent ones.

According to Charlie Munger, "the first rule of compounding is to never interrupt it unnecessarily." By conservatively providing for future liquidity needs, we build portfolios to withstand market volatility and allow equities to do what they do best: compound.

Tax-Conscious Investing

Much of the investment management industry is focused on pre-tax returns. Ignoring taxes is fine for retirement accounts, pension funds, and endowments. But it is a costly approach for families looking to sustain wealth. For top earners, 40% or more of your investment return can be consumed by taxes. These investors should focus on limiting taxes and increasing after-tax returns.

The US tax code favors specific investment behaviors, structures, and strategies. It is important to ensure your investing is aligned with the tax code, not fighting against it.

For example, taxes are particularly punitive for short-term traders, incentivizing taxable investors to maintain long time horizons. Certain investment structures, such as equity mutual funds, can be incredibly tax inefficient, and often should be avoided in taxable accounts. Other investments, such as direct real estate, can provide tax-advantaged returns that make them more attractive to taxable investors.

In addition to deciding what assets to buy, taxable investors need to pay particular attention to where those assets are held. Identifying the optimal asset location can have a big impact on your after-tax returns.

Family Dynamics

Our holistic approach to wealth management begins with your money and ends with your family. A thoughtful and thorough consideration of financial issues is critically important, but the success of an estate plan often hinges on family dynamics. Families are complicated, and the potential for conflict can grow with each new branch on the family tree.

In many situations, proactive communication can help limit conflict. After creating an estate plan, discuss it with your family. Proactive communication can limit feelings of surprise or inequity. Family conversations, however, can be difficult. Trusted family advisors can provide an objective point of view and help guide these challenging dialogues.

Family conflicts often arise because different individuals and generations have different values and needs. Philanthropy can help your family bridge these divides, creating a shared culture and mission. While a family foundation's primary focus is on societal benefit, it can also have tangible benefits for your family. A foundation can deepen bonds among family members and even change their perspective on wealth. Foundations can also help build financial literacy in younger generations.

Estate Planning

If done correctly, estate planning can be a powerful tool for sustaining family wealth. Effective planning can help you reduce tax liabilities, protect assets, avoid probate, and much more. However, nothing in life is free, and these benefits can come with their own unique costs. Certain strategies will require you to give up control of your assets. Others will limit your flexibility or increase the complexity of your financial plan. An experienced team of advisors can help you navigate these trade-offs.

Estate planning is not a "set it and forget it" task. An effective plan should be a living document. As your family evolves, your plan needs to evolve.

Moving Forward

At Whittier Trust, we believe real wealth management balances your finances with your family. Each topic listed above is helpful in isolation, but the integrated whole is much more powerful than the sum of its parts. A high-touch multi-family office can coordinate with your existing advisors to create a holistic plan for sustaining your family wealth.

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