UBS

WHAT'S IT ALL FOR?

Wealth and the next generation

Foreword

What's it all for?
That was the surprisingly deep question suddenly posed by a UBS client at one of our regular dinners. Until that moment, it had been a relatively routine conversation about wealth planning and succession. With this unexpected intervention, however, it became a passionate discussion and debate that lasted for more than two hours.

The question of what wealth is fundamentally for has no single answer, and will be a deeply personal matter for most individuals. Is wealth simply to be enjoyed by the people who have made it? Those with children and grandchildren will usually feel a sense of responsibility to their descendants. Setting them up in life, though, without taking away their drive and incentives for success, is a complicated task.

In this report, we are bringing together eight different case studies, which highlight some of the real challenges and dilemmas faced by different families when it comes to making plans for transferring wealth to the next generation. No two situations are the same, but you may recognise elements of each in your own story.

Among the questions we consider are what happens when a husband and wife don't agree, how to cope with ever-more complicated family structures, how to involve future generations themselves in the planning process and the eternal quandary of how to be fair to siblings with very different interests and skills.

There can be no right or wrong answers to such difficult questions, even though the financial solutions themselves may be relatively straightforward. UBS, in these cases, has been the facilitator of conversations about what are often very emotional and even life-defining themes.

Our advice and counsel is shaped by our experience of working over many years with individuals and families who have faced similar challenges. By sharing these stories, others may find useful insights and perhaps even some inspiration.

What's it all for? That is indeed a tough question. I hope we can help to guide you carefully towards the right answer for you and your family.

Nick Tucker
Head of UK Domestic, UBS

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HUSBANDS AND WIVES

"My wife has a clear view that our children should make their own way in the world, but I feel that they face very different pressures now compared to when we were in our 20s".

Sometimes they disagree on the right thing to do
Very often, husbands and wives share the same values and attitudes in discussions about family wealth. Occasionally, though, they can have different perspectives and instincts on the big questions around succession. The case study below is an example of how difficult that can be.

Some entrepreneurs think that if they hadn't had to fight every step of the way, they would never have achieved the success they had. Their partner, on the other hand, might have a different opinion and want to use the family wealth to give the children the best possible head start.

Sometimes differences are less fundamental. One partner may want to travel more and do big things, while the other might prioritise a better day-to-day standard of living. Our client advisers won't take sides, but they do sometimes find themselves in the middle of these interesting conversations. The important thing is not to offer a pre-conceived solution, but to work hard to understand the feelings and motivations on both sides.

It's surprising how often the big questions aren't considered in real depth before the discussion with the adviser is taking place. Occasionally, one partner may have even misread the views of the other. Until the conversations are happening in a more structured context, small misunderstandings and misconceptions can linger. Once clarity has been established on the family's goals, though, agreement on how to reach them is generally easier.

Case study – a couple at odds
This client is in his early 60s and made his money in senior corporate roles. His wealth is jointly owned with his wife. The couple have three children – two daughters and a son – who are all in their 20s. It was very difficult for this couple to make progress with their plans, because husband and wife had different approaches to how money should be passed to the children.

Even though both came from similar backgrounds, she had a clear view that the children should build their own lives with very little support, as they did. He, though, thought the world had fundamentally changed, and that young people face very different challenges than they did in the past.

The couple say their wealth needs to sustain them for another twenty years at least. Their children have some immediate needs, however, particularly around housing. One daughter was paying a large amount to rent an average property in an undesirable area. The mother was quite shocked when she visited. This was the catalyst for her to change her approach, and agree to provide money for a deposit on a flat.

The couple say they will make one-off gifts to their children for now. In the future, they are considering setting up a trust as a solid foundation for longer-term wealth transfer.

SONS AND DAUGHTERS

"I have involved my wife and daughter in all of the decisions. It has been a very open process all the way through".

Siblings can be very different and knowing when to involve them is hard

Transferring wealth to the next generation is bound up with difficult questions about fairness. When wealthy individuals have one child, as in the case study below, things can be relatively simple. With multiple siblings, the situation gets more complicated.

One child may be experienced in business and financially astute. Another may be creative, but with no interest in the commercial world. Parents may take the view that it's better to help a child who is likely to struggle the most. Or, instead, trust the more financially competent sibling with a bigger share.

If families misjudge the situation and get these decisions wrong, it can sow the seeds of lasting resentment. Some clients will take the view that each child should get the same healthy lump sum and that's it. Do with it what they will. Others will try to identify where the need is greatest and respond accordingly. There is never a perfect formula that works for every family's situation.

Even if the parents are completely "fair" in respect to the amounts, that doesn't answer the question of how much wealth should be passed on to the next generation and when. Each client, with their adviser, must decide when the time is right. If the children are old enough to be responsible, but financially inexperienced, then appropriate training and education might be a useful part of the plan.

Case study – a smooth transition

This client went from being in a well-paid role to having much more wealth than he expected, after a sudden windfall from a stock market flotation. The family are EU nationals, but resident in the UK for tax purposes. From having little interest in tax and wealth planning, he suddenly found himself in a wealth bracket where he needed guidance.

He quickly started to involve his wife and daughter in all the critical decisions in what was a very open process. Some assets from share sales were transferred to his daughter immediately. A discretionary fund was set up, as well as pension arrangements for her, all within the context of managing inheritance tax liabilities.

The daughter has had separate meetings with the UBS client adviser and has also taken part in courses introducing some of the principles of investment and financial planning. This autonomy and independence are important as both generations feel they have sight of the bigger picture as well as the ability to make their own decisions on spending, investing and giving.

The client has set up a charitable foundation. The transfer of some shares up to the value of his gross salary has been used to take advantage of tax relief. The daughter is also able to support the causes she cares about through charity donations.

PARENTS AND GRANDPARENTS

"Communication in the family has all but broken down, and we have really reached a stalemate".

Often decisions involve multiple generations and complex family structures

With so much wealth now in the hands of baby boomers, situations can now be more complex and involve multiple generations. We often think of wealth being transferred to people when they reach the age of 18 or 21. Because people are living longer, and earning for longer, much wealth now transitions to people who are already in their 30s, 40s or even 50s.

Sometimes, wealthy couples only start taking these conversations seriously in their 60s. By then, their children will be adults and have firm views of their own. It's possible that there will also be grandchildren to consider and the temptation to skip a generation becomes much more real.

New demands for income and capital tend to arise with time, as families extend and widen. Plans that seemed sensible ten years ago may have to be looked at again. Complex multi-generational arrangements may be considered with wealth being parcelled up in different ways. It's more normal now that a settlement could make those in different generations equal beneficiaries.

With complex family structures, the devil is often in the detail. It is critical to have sound governance in place and to ensure there are independent representatives that can be called upon to resolve family disputes. Long-standing plans for succession should be reviewed regularly with the appropriate paperwork updated when there are changes in the family situation.

Case study – a troubled succession

In this family, the grandfather was the original source of the family money. The wealth has been held in a company structure, which he initially planned to divide in a 50/50 split between his two children. As time went on, the grandfather felt that one of his children wasn't financially responsible enough to be given half of the family fortune.

So, he changed his plan to a five-way split of the company shares between his two children and three grandchildren, who were already grown-up. Unfortunately, the grandfather died before his will was formally redrawn. Relationships in the family have suffered badly, with lawyers now involved on all sides.

The company is now being run along the same lines as it was prior to the grandfather's death. The grandchildren had been appointed to the board, so they have to approve dividend payments to the individual whose inheritance was reduced, but he has stopped paying an allowance to them in turn.

Resolving this complex and difficult situation will require the involvement of a trusted professional to mediate. A solution won't be reached quickly or easily. Repairing relationships in the family will be difficult. For the future, clarity will only be restored with the establishment of a formal governance structure that is respected by all sides, something that will take time to draw up and agree on.

CHARITIES AND CAUSES

"We are passionate about our charity, but it is time consuming and we don't want it to be a burden for our children".

Families may want to give away some wealth or invest for impact

Wealthy individuals and couples will want to provide for their children in the most sensible and effective way. They may, however, also want to use their wealth to achieve something else, for society or for those less fortunate. This is where discussions of succession are inseparable from the broader values that are held important by those currently responsible for the wealth.

Traditional philanthropy was about giving money away to good causes. But now the conversations are a lot more strategic. Clients often want to invest with impact, generating social and financial returns at the same time. Questions about sustainable and ethical investment can get us into difficult territory. One family member's view may be completely different from another's.

Values can also shift substantially between generations. A wealthy individual might want to set up a foundation to support a charity long after he or she has gone. The next generation, however, may not want to be locked into supporting the same cause forever.

Couples who have been able to build up substantial savings and investments may also want to use that wealth to enable their children to follow careers that are not wholly focused on financial gain. After a sensible consultation process with their advisers, families may devise plans to allow their children to follow their hearts in their working lives, whilst being guaranteed a minimum annual salary that allows them to live in a degree of comfort.

Case study – a charitable couple

This family benefitted from the sale of a business, the proceeds of which more than met the needs of the husband and wife, who continue to live modestly. They have three children all approaching or in their 20s and no desire to live anywhere other than their current property.

The couple have used a cash-flow model with their advisers to estimate the level of capital they will require, well beyond the standard length of a retirement. With this prudent approach, they calculate that they will be able to live at a similar level for decades to come if necessary. This has allowed them to think carefully about what to do with the rest of their accumulated wealth.

The children have an income stream to supplement their salaries, allowing them a free choice of which careers to pursue. Each will also come into lump sums at the ages of 25 and 30.

Charitable giving is a key part of the plan. The family has set up a charity that helps children in Africa get access to private education and university places. The couple don't, though, want their philanthropy to be an endless burden on the next generation. So, in their wills, they have made provision for any young people supported by the charity to complete their programme of study, so that the children don't have to make up any future shortfall in the charity's accounts.

MARRIAGE AND DIVORCE

"My main aim really is to provide for the education of future generations – and to protect the family money from divorce settlements".

When the next generation marry, things can get even more complicated
When it comes to wealth, family structures have always been complicated. With people living longer, having multiple careers and sometimes multiple marriages, the issues can now be more tangled. There is no set formula for "blended families", with children from more than one relationship. Each situation will be unique and will require a unique solution.

Lives may not be as linear as they were, but one fact remains. Nothing dissipates wealth as quickly as divorce and remarriage. In discussions with advisers, these issues can be treated as current or future risks and looked at in a pragmatic and professional way, removing some of the emotion and impulse that sometimes characterises debate in families.

All future possibilities and relationships will never be anticipated with perfect accuracy. But some general principles can be established. This is, perhaps, particularly relevant for prenuptial agreements. If this question is first discussed when marriage seems likely, it may well be a fraught discussion. If, however, prenups are established as normal practice from an early stage then this could well be an easier conversation.

A wealthy parent remarrying can also cause great concern for children from the first marriage. In this situation, it may be hard to find a perfect solution that pleases everyone equally. Discussing the issue openly, though, in the context of a much broader conversation around financial planning, is sometimes the best way to make progress.

Case study – a pragmatic entrepreneur
The couple in the previous case study insisted on pre-nuptial agreements for their children. They were quite clear that only direct descendants should benefit from their wealth. Other clients also worry about what happens if and when the next generation choose to marry.

One semi-retired entrepreneur amassed a fortune from the sale of family businesses, and now focuses his business interests on a variety of areas, ranging from horses to property. As these activities are at the risky end of the scale, his portfolios are generally medium to low risk.

Around half his capital is held in trust for his two sons, both in their 30s and independently wealthy. Neither is, yet, married. Both sons are astute financially, but he hasn't discussed the terms of the trust directly with them. Elsewhere provisions are also being made for charity, with about 10% of his wealth currently dedicated to charitable giving.

The priorities for this client are to keep enough control of his wealth to be able to provide schooling for future generations and insure against messy divorces. To ensure this, he is looking for a suitable trustee to replace him after he dies.

This person will probably be a third party rather than one of his sons, and will be charged with protecting and preserving the family wealth.

HOUSING AND SCHOOLING

"Some people seem to think that setting their children up with a house and a car is all they need. It's as though they wash their hands of them after that. But life's not like that".

Often property and education are the two biggest issues in succession planning

In almost every conversation about intergenerational transfer, two themes recur: housing and schooling. The discussion often starts with the question: what's the minimum I need to do to set the next generation up in life? This then creates a subset of unexpected further conversations.

With house prices surging for decade after decade, it's accepted now in the UK that it's almost impossible to get onto the property ladder without substantial help. Some wealthy couples will want to buy a house outright for each of their children. Many will want them to earn it in some way, pay a mortgage and feel a sense of ownership.

Private school fees have also accelerated well ahead of inflation, taking them out of reach of parents without savings in most lines of work. This is another area where wealthy individuals and couples may want to make special provision for children and grandchildren. Families often want to support the next generation at the critical milestones: the birth of a child, starting school, starting university, graduating, setting up a business and getting married.

Whenever and however parents try to help, they will usually want to do so in ways that don't take away their children's desire and ability to find their own path to success. Here the adviser can provide an external sounding board, helping clients map out their goals with clarity and precision before suggesting the right financial solutions for each situation.

Case study – a prudent grandmother

This wealthy individual is semi-retired but still actively involved in corporate life with non-executive directorships and investments. She has three children, two of whom are married, and seven grandchildren. All her money is self-made relatively recently, so her children didn't grow up with wealth at the family's current level.

Advisers started talking about estate planning when she was 45, but that seemed too early for her to focus fully on the big questions. Until her children started to make their way in the adult world, it was very hard to anticipate the type of support they might need.

Help with housing for her children has been a priority. Money is also being put in trusts to cover school fees for the grandchildren. She believes that support needs to go well beyond housing and schooling, though, for instance with the funding she provided for one of her children to attend business school.

Her youngest son has a large family with four children being born within five years, during which time he also started his own business. There was, in her view, no way he could have financed all of that himself. But, after initial support in the shape of an interest-free loan, his firm did well.

This client is also conscious that her generation are living longer. One of her friends gave all his money away, but was then ruined by care costs for his wife who became seriously ill.

DISCLOSURE AND DISCRETION

"We've set up a trust that allows us to exercise more control. I've worked hard to earn that money and I want to make sure it stays in the family".

When and how to reveal the extent of wealth to the next generation

Some wealthy families may decide that complete transparency involving all the generations is the only sensible way forward. Talking about the extent of personal wealth is, though, often difficult. Friends and colleagues may treat you differently if they think that you are "rich", and there's the worry of potential stigma for children at school.

Many clients have sons and daughters who are completely oblivious to the family's wealth. Some 40-year-olds are still not aware of trusts. Increasingly, however, younger generations are being included in discussions at an earlier stage. With so much information publicly available now, it may be better for parents to disclose the situation sooner rather than their children find out from other sources.

In some cases, wealthy parents will want to make a partial disclosure, perhaps transferring a limited amount of wealth to see whether it is put to responsible use. Such a test-and-learn approach can in certain situations help to build a different, more mature, relationship between generations. Gifts that are seen to have no-strings-attached, however, can just as easily have the opposite effect.

Providing financial training and involving the next generation with the wealth adviser can help parents feel more confident with increasing transparency over time. Educating younger generations about the value of money and the responsibilities that come with wealth are important steps towards making them trusted partners in managing family capital.

Case study – a cautious custodian

This individual is in her early 60s, married, with three adult children all in their 20s. Significant capital was released recently with the sale of part of her trading business. The remaining shares will be sold for a similar large sum in a few years at which point she is planning to retire.

In the meantime, she continues to take an annual salary, lives in a nice house without a mortgage and has good pension provision, so anticipates no further personal requirement to draw on the remaining wealth for the time being. She can't anticipate spending anywhere close to her total wealth on her lifetime needs.

She wants to transfer to the next generation, but is concerned that having too much too young would be bad for her children. They aren't fully aware of the extent of the family's fortune, and she feels they need guidance and clear boundaries.

When each child was given a £50K lump sum to see them through university, there were negative consequences. One child quickly got through the money, and still ended up in debt. The client has now realised that she needs to prepare her children more carefully and exercise more control.

She has now drawn up detailed plans for wealth transfer and established a trust. Conversations have started with the children about the extent of the family's wealth and the responsibilities that brings. Now the client says she is better able to enjoy her wealth without constant fear that it will cause damage and division.

DEATH AND TAXES

"As the main earner for a relatively young family, I want to ensure that they are provided for in the event of my death and that our family's standard of living will be protected".

Inheritance taxation hangs over it all. But this is a much bigger conversation

The words death and tax never seem too far apart. One recent client was only too happy to pay a large amount of tax, as he felt that was an excellent way of transferring money back to society. Most, though, will want to reduce the tax bills associated with moving wealth to the next generation.

Historically, trusts were viewed as the best way of reducing tax liabilities and having some control after you die. They still have a role to play. But structured arrangements can also be too rigid, given the constantly shifting environment and increasingly frequent revisions to tax law in different countries.

Tax is complicated. Our advisers will always be on hand to work with a client and their tax adviser to guide them through the various considerations. In fact, the number of different types of solution for dealing with potential inheritance tax liabilities is relatively limited and well known. The bigger, more important questions are: what do I want to achieve while I am alive, and what if anything do I want to try to control after I am dead?

Often, wealthy individuals, in thinking about death, underestimate how much living they'll still need and want to do. Someone who 'retired' at 55 might have another 40 years of life. By the age of 60, they might be feeling refreshed and ready to launch back into business or take things in a completely new direction.

Case study – a young family

The final client case study is a wealthy individual from a private equity background who is married with two young children. She is the main earner for a relatively young family and wants to ensure that the children are protected should the worst happen and that that the family will be able to carry on living at the same standard.

Her concerns grew about the impact changes to her tax status would have on the family's inheritance tax liability. The potential bill might have been huge. An offshore trust was set up to manage a significant portion of the wealth but this arrangement was found to be expensive and inflexible. Almost three-quarters of her capital was tied up in the trust, which also attracted high management and oversight charges.

After revising her succession plans, she dissolved the trust and returned the money to her and her husband, allowing them to set up investment portfolios with lower fees that are more closely tailored to the family's needs. This has given the family greater flexibility for the future, as they respond to changing priorities as the children grow up.

Any future inheritance tax liabilities are covered for now by a life insurance policy. The proceeds from the scheme will offset the tax bill should the worst happen. These arrangements have given the family peace of mind, without their future room for manoeuvre being unnecessarily restricted.

CONCLUSION – A plan for wealth

Transferring wealth from one generation to the next is never entirely without its difficulties.

It may be best not to think about this as "succession planning" at all. There is unlikely to be one single moment when the entire family gathers to agree the shape of any settlement. Every situation will be different, reflecting that family's values, level of wealth and approach to parenting.

The role of UBS is not to be rigid or prescriptive about the solutions on offer. Before we can even think about products and recommendations, we need to find ways to help families work out what the purpose of money really is. Managing wealth is about far more than seeking the most secure investments and highest financial returns.

At its best, this is part of a much broader conversation about long-term financial planning, which continues over many years, and even decades. Wealthy individuals will ask themselves any number of challenging questions: What are my goals? What do I want to achieve in the rest of my life? What are my children's goals? How can I best help them reach those objectives?

Any plan for wealth, and the transfer of wealth, must be flexible enough to deal with changing priorities but solid enough to withstand future shocks.

In the past, a wealth manager might have focused on the investment side, without being part of these more subtle and complicated interactions. At UBS, though, we have helped families like the ones featured in this report over many years, facilitating essential conversations about the most complex and sensitive issues.

The financial products and solutions may, in the end, be relatively simple to find. The more difficult part is always helping our clients find an answer to the big and critical question: **what's it all for?**

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