Episode 2 - Good Advice | At the kitchen table with Alan Heath

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Episode 2, in the series 'At the Kitchen Table' from Momentum Advisory Group

This podcast is a way to share stories from families we support and family advisers we partner with. These stories share a common theme - a critique of the idea that to be wealthy is not just about how much money you have but how you put your family's resources to use for future generations.

In this episode I was fortunate to have Alan Heath join me at the kitchen table. Alan has 30 plus years working with families, family offices and is faculty at the Harvard Business School Executive Education Program for families in business. I really enjoyed Alan's global perspective and his insights on family governance.

Episode Transcript

Tiffany: Alan Heath, CEO and director of the Strategy Group, based on Boulder, Colorado. My knowledge of your experience having 30 plus years working with families, family offices and in the last 10 years with the Harvard Business School Executive Education Program about families in business are absolutely well placed. To just share a little bit insight from your travels with families about some of the real issues that we should be expecting to face families as we look ahead into the next 5 years particularly thinking about Australia given how much of a change we're going to see in terms of leadership handing down wealth, handing down a significant generational shift happening but really would love your global lens on this if you wouldn't mind sharing a few ideas with us.

Alan: Okay. Well, I think that what I can say first is that what we see in one country, we typically tend to see in other countries probably about 85% of the issues in families that own businesses and families in general the same worldwide.

If you're in Japan or you're in the US or you're in Latin America or you're in Europe, you're going to see many of the same issues. I think a lot of it is dependent upon where the world is moving at that particular time. We have very basic issues that repeat themselves over and over again but now, we're starting to see trends that are different.

We're also seeing a huge creation of wealth and I think that that creation of wealth in itself is creating a lot of problems. What I'm experiencing is that there's a fair amount of stress in families about how they're going to pass that wealth on, what they're going to do with it, how much are going to talk about in the families, what they're going to do about it, what structures are important.

I think we're finding more and more that sometimes the typical trust that are put in place for families are doing more damage than they're doing good because they tend to be drafted in a way that focuses on tax efficiency, minimizing taxes.

Just recently here in Australia, the conversation was someone who was very concerned whether or not the business was actually paying taxes. We're finding in the US in particular now that the millennial generation wants to be certain that their family businesses are actually paying taxes because they think it's an obligation and they think it's a best practice.

I think that this rapid growth of wealth is created. It maybe is one of the biggest changes because it's affecting more and more families and it's creating a need to think really carefully about giving. We tend to look at these gifts that we give as from the eyes of the giver and not from the eyes of the receiver.

We really don't think through carefully enough what it might be like to be a recipient of wealth. You and I have just been talking about how much trouble it can cause when you receive wealth because you tend to get this as a surprise sometimes. You know you're going to get something but you generally don't have any idea about how much it is and it creates, in many cases, a stress on the recipient.

Because of this and because advisers are talking more and more about it, we're seeing much more transparency between the parents and the children about what's discussed in advance. I think that's very, very healthy. I think that this transparency and this preparation for receipt of wealth has long been under addressed.

Tiffany: One question a lot of families ask is when should I start doing this work? Hence, I find it kind of interesting that that question comes up some assume it might have to happen right around the time of their passing or when they're creating a will. I'd like to think it could happen well before.

What's your take on that question?

Alan: Well, I think that paying attention to this, you know, starts very, very early. I think the earlier you start, the easier it is. There are steps that you can take when children are very young. We've seen the use of philanthropy has been very effective here. Teaching children about money in very, very soft ways.

I've dealt with families who don't yet have children or have children at very young ages and what we do is we start to work on a plan. How are we going to do this? What is it that we desire? I think that having discussions early on about what you want to accomplish, what you want your children to experience is really important, when they get the money, how much money they get. I would recommend doing this at a very early stage and I think that one of the things we don't tend to do is to tell our advisers, our lawyers and our CPA and tax advisers and so on what it is we're really trying to accomplish, what we want.

The other thing we fail to do is to articulate in some way, in some kind of document or at least some conversation going forward to the children or the recipients of this wealthy why we're doing what we're doing and what our expectations are.

They have a tendency to get very, very focused on the tax implications and the correct legal structure. We don't really talk about what our expectations are. Do we want our children to feel somewhat kind of obligation? Do we have some soft desire that we want them to follow?

We're seeing more and more, in US in particular now, we're seeing the use of what I've call purposeful trust which have actually language in them from the grantors. It's beyond what the lawyers typically put it. Some of it's not mandatory but it's just getting an impression of why the parents are doing what they're doing. I really think it's very wise to do this.

Tiffany: You know, I have to pick up on the lawyers because when I started in Australia as to who was helping families start to define what the purpose of the wealth look like and bring that family together. Often it seemed to fall to the lawyers and accountants. Now, you're a lawyer by trade. Do you think you need to have a legal point of view or even an accounting tax point of view in order to do this work?

Alan: Well, I think you have to understand that what I do feel that there has to be a balance. I'd be probably a bit critical of my own profession because I think that we have a tendency to get too technical about things.

I think having an understanding of basic psychology, having an understanding of family systems theory is very, very helpful. You know, I think that what's happened over the years is families haven't understood this so it's just not become a part of the estate planning process.

I think it's really, really critical because again, we're driven by certain things but we're not driven enough by what the impact is going to be on those who receive the wealth. I mean there's a whole profession that's been built up in certain areas around the psychology of wealth. That tells you that there's some issues.

We say in family businesses in particular, that more family businesses are destroyed by bad owners than by bad managers. I think what we failed to do in the family business environment is to really train people to be good owners. I think in the other side of the equation we also failed to train people how to be good beneficiaries.

This has been an area that's been under addressed I think for quite some time. I think that what works best in my mind is if you have a team of lawyers and CPAs or tax advisers and family business professionals or family psychologist who can work together and build the right kind of scenario.

Tiffany: Yeah. Speaking of what triggers those sort of events, life events, liquidity events, that tend to bring families together, do you find families are moving more toward doing this kind of work based on fear of what the wealth might do or based on the opportunity of what the wealth might create?

Alan: I would say that right now it's the former because probably one of the most frequent requests we get is what can I do to be certain that the wealth doesn't harm my children.

I think once you get beyond that, you have discussions about that, you try to work that out, then you can address what the benefits are because wealth gives you opportunity. I think it's just the way you handle it that becomes important. There's a huge concern I think about those who particularly have created new wealth as to what the impact is going to be on children.

I think that there are two key things - good parenting and education. It's not an easy task because there's no right and wrong way, there's no kind of standard approach to this because every family is different. Each child takes this in in a different way. It's a very hands-on process.

Tiffany: I guess that our last question to you particularly given your experience in the space is governance, which is such an important part of a business entity but when you think of a family entity as an enterprise, what's the role of governance in your view and how should families be thinking about this?

Alan: Well, I think the governance process for every family maybe is different but I think that what I find that runs through all families is that as families, we don't plan very well.

In businesses, we tend to have policies and procedures and rules and structures and things of that nature. In families, we don't typically do this in a normal sense. I think that having some guidance on developing a little bit of process, some rules, some structure, it gives us a place to go when things turn bad.

It also gives us a place to do this education that I was talking about. I'm a great believer in governance because I also think it teaches the next generation a process and a way to move forward in a logical sense.

The other thing it does is if you have some rules, if you some structure, when times get bad, it gives you a place to go to make decisions. When I hear a family say to me, "You know, we had a problem, we were trying to figure out how to solve the problem and somebody in the family said, well, we have a constitution or we have a protocol or we have a procedure. Let's turn to that procedure and utilize it."

Then I know that things are working and that the families got a rational way to come to some kind of decision.

Tiffany: Which is a really nice place to land. One of the phrases used by a family I've been working with was having a guidebook that the family can look back generation upon generation.

Can I ask one last question? What would be a must read guidebook for families in your opinion who are starting to think about doing this work?

Alan: Well, you probably know what I'm going to say and I really think the best book, first read book out there is the book by James Hughes which is "Family Wealth: Keeping It in the Family."

I think it's philosophical. It comes at things from a different direction than most books do. There's more and more stuff being published but I like this as a first shock because it talks about governance. It talks about the important of governance in institutions, family institutions and other institutions. It's sensitive to the emotional piece of this whole process. That would be my number one recommendation.

Tiffany: Thanks Alan. Nice to have you in Sydney. Thank you for the time.

Alan: It's great to be here