Concentus Wealth Advisors

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VALUABLES

Ideas, Systems and Strategies for Managing Family Wealth to Fulfill Your Greatest Values.

About V A L U A B L E S

Many financial advisors focus on communicating with clients to provide complex analysis of the investment markets and economies. However, we have learned that most clients are not particularly interested in this complex analysis. Most clients hire an advisor for their knowledge of the markets, not for their ability to explain that knowledge. Most want to know what time it is, not how to build a watch.

Experience has taught us is that wealthy families care most about using their wealth as a means to a desirable end, which is to achieve a more satisfying, fulfilled and impactful life, and to fulfill their most important Life Values.

V A L U A B L E S is a periodic article series focused on the concepts, systems, and habits which we have observed among families who have been successful in this quest to use their wealth as a tool to live a life of significance. The most successful families share a set of habits, systems, and insights which enable them to use their wealth as a tool to fulfill their Values and what is most important to them.

We are naming this article series **V A L U A B L E S**, because it will provide an exploration of those habits, systems, and insights. We hope it will help you to consider your assets and possessions which are most valuable to you, and how you can use your financial wealth to enhance and cultivate your true "Valuables".

The Family Bank – A "Sound" Idea

By Erik Strid

"Along with being a phenomenally successful banker, Rothschild was shrewd about protecting his heirs from the temptations and pitfalls of great wealth. He developed a family bank system to regulate his heirs' access to the family fortune, and to discourage spending family wealth for frivolous reasons."

Establishing Family Governance

In our work advising families, we have discovered that one critical element of raising a significant and successful family is the need to provide sound financial education to future generations, and establish strong financial skills and habits among children from a young age. By establishing a strong program of financial education, as well as family wealth governances, we believe you increase the chances that you will raise a family which will be successful over multiple generations, and enable your children and grandchildren to avoid many of the pitfalls of inherited wealth.

The Family Bank Concept

One specific area of family governance has helped many successful families manage their wealth over multiple generations: the "family bank". The Family Bank controlled access to the money and prevented reckless use of it. The Rothschild family invented this brilliant concept in the early 1800s, and it may be a great strategy for your family today.

Born in 1744 in a Jewish ghetto in Frankfurt, Germany, Mayer Amschel Rothschild went on to launch a banking dynasty that survives to this day. Forbes Magazine has called Rothschild "the founding father of international finance" and also named him one of history's most influential business leaders.

Along with being a phenomenally successful banker, Rothschild was shrewd about protecting his heirs from the temptations and pitfalls of great wealth. He developed a family bank system to regulate his heirs' access to the family fortune, and to discourage spending family wealth for frivolous reasons. Instead, the Rothschild fortune was earmarked for education, investment, or starting a new business venture. Family members understood that the fortune was there for their betterment, but not an open treasure box. They were encouraged to think of themselves as stewards of that family wealth…to respect it, to work hard to grow it and preserve it. The "family bank" concept that Rothschild used in his own dynasty became a widely copied model for successful family governance and wealth management.

Borrowing from the Rothschilds

Essentially, the family bank is a conceptual repository, which can be established to provide ground rules for family members who are seeking access to the family's resources. Instead of providing future generations with open access to the family money for any reason they desire, the bank might permit access only for productive purposes, such as buying a home, securing education or starting a business. In addition, family members are not "given" money from the family treasury, but instead are required to "borrow" money from the family, and these loans are expected to be paid back.

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This concept allowed the Rothschilds to instill the understanding among future generations that the family's wealth is not their ticket to a life of ease and freedom from responsibility. Future generations were expected to make their own way in life through their own hard work, even though the family wealth was available to help them become educated or start a business. But it was a loan, not a handout. Instead of acting as a crutch that heirs could lean on to enable a life of excess and leisure, the family bank was intended to act as a resource to enable future generations to strive and flourish, by supporting their productive enterprise.

Your own family bank may take many forms, depending upon your family's wealth and complexity. Very large and wealthy families might create actual accounts or trusts, governed by written rules that specify the criteria for loans and the repayment terms. In smaller or less wealthy families the banking system may simply involve a set of ground rules and principles for children and grandchildren who seek access to money.

The Family Bank in Practice

The Rothschild family was fabulously wealthy and set up their bank using a complicated and sophisticated set of structures and rules. However, families with much smaller fortunes can think like a Rothschild. Here's an example that illustrates the family bank concept, from the excellent book *The Cycle of the Gift* by James E. Hughes Jr., Susan E. Massenzio, and Keith Whitaker.

> *The father of this family was a practicing attorney who served as trusted counsel to many of the largest global companies of his time. But he was as comfortable with the work of Marcus Aurelius, the Roman emperor and philosopher, as he was with legal briefs. His highest praise was that person's choice or action was "sound."*
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> *He had four children. A few weeks after the youngest of these had graduated from college, he called his eldest child, a son (and also an attorney), into his office. He announced that with the completion of the siblings' collegiate careers, he had decided that they, as a family, were to create a bank. His son naturally asked what in the world this meant. His father replied, "it's really quite simple."*
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> *He went on to explain to his son, and eventually to his other children as well, that he and their mother had decided that they had more than enough money to live comfortably. "Nothing too much" was a precept he knew well. With due allowance for their personal needs, the mother and father had decided to dedicate their remaining assets to a family bank. This bank would take the form of various family trusts, educational accounts and other savings vehicles.*
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> *The purpose of the family bank, he explained, would be to support the children and eventual grandchildren and great-grandchildren in their own personal pursuit of happiness. To do so, he asked the children to serve as the board of the bank. They would have discretion over disbursements. He and their mother would be happy to provide asked-for consultation, but they would hold no veto. Eventually the children could nominate their successors to the board.*
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> *Disbursements could take the form of loans, secured against property or unsecured. Or they could take the form of grants, requiring no repayment. As the family practiced with the bank, they decided that any disbursements for the acquisition of property – such as the down payment on a house – should be made as loans and repaid. But disbursements made to help a family member through hard times should likely be a grant.*

The family's experience with the bank was not always smooth. The father and mother found it hard at times to resist the urge to suggest certain disbursements or to question others. Two of the siblings went through difficult divorces requiring significant grants from the family bank. One sibling died in an accident, requiring the remaining siblings and the bank to take more responsibility for the surviving spouse and children. The siblings also pursued their own careers, which earned some of them much more income than others. As a result, loans and grants from the bank to the various siblings and their children were not equal. But their shared spirit of helping each other grow allowed the bank and the family to grow even in the face of such inequality.

An enormous spirit infused this gift of the family bank. It has inspired the lives of these family members and many others who have come to know them. It was, in the patriarch's words, sound.

We can take a number of lessons from this patriarch and his family. First, their process of discernment began with a vision of family wealth as separate and distinct from individual family members' resources. As a result, they took concrete steps to distinguish the family's resources – the family bank – from the individuals.

Second, this family made full use of their options for giving, through trusts, loans, and outright grants. But they maintained a loose structure amid those options. The function of the family bank was clear: to foster the pursuit of happiness of the individual family members, present and future. The form was more free-flowing. Form follows function, not the other way around.

Third, unlike many givers who proudly create complex (and expensive) estate plans, this patriarch deliberately understated his plan's complexity. He kept the family focused on the simple purpose of the bank, because that is what is most important, rather than any complexity, which turns out to be only a nuisance. His quiet pride rested in the lives of the enhanced, not in the plans he could have paid for.

Modern Day "Family Banking"

As you consider these uses of a family bank, it is easy to understand how it may help your own family manage its wealth and make responsible decisions in many typical situations. Here's one that will resonate for most families.

Imagine that your teenage son comes to you in the spring of his junior year in high school and asks for a new car for his birthday. This request takes you back slightly, because he is not asking for just any car – he wants you to buy him a convertible BMW. The hair on the back of your neck begins to stand on end, as unwelcome emotions begin to flood your senses. You are overcome with worry that your son is becoming spoiled, and frustration that you feel powerless to do anything about it. You articulate that frustration and worry with anger, as you begin to berate him with stories about how "in my day, I walked 10 miles to school every day," and "you kids just don't appreciate all your mother and I have done for you."

Your son is familiar with this dance, since he has heard this angry response many times before. This time, he is well prepared with some talking points. First, he appeals to your deep desire for him to be a successful and popular child. He explains that "all of his friends at school" own fancy sports cars, and asks if you want him to end up as an unpopular nerd. He reminds you that he has been earning good grades in school, scored well on his SAT test, and appears to be positioned for acceptance into your Alma Mater, fulfilling your long-held dream. Finally he hits you with the ultimate guilt trip when he observes that you live in a 6,000-square-foot house and drive the latest Mercedes sedan. You obviously have the money, and are willing to spend it on yourself, so why not on a reward for him? He has hit his target, and has made you feel guilty for withholding a reward for his hard work and studies.

You are defeated. You put up a token argument for several more minutes, but he has won the battle. Pressured by guilt, you agree to buy the car, but you don't feel very good about it. You feel as if you have taken yet another step to spoil your child, powerless before the peer pressure and guilt that drove you to do it. You also know that owning a BMW convertible in the spring of his junior year will likely distract him from his studies.

Now let's look at how the situation might be handled if you had a family bank…

Your teenage son is about to turn 17, and at this age he naturally develops a burning desire to own his own car. He also understands that he lives in a family in which access to money requires accountability and responsibility, and that money is not granted for purchases like this without strings attached. He knows that, in order to obtain the money he needs to buy a car, he needs to apply for a loan from the family bank.

Highly motivated to get his own set of wheels, he resolves to do what it takes to get one. He requests a meeting with his parents, aunts and uncles who sit on the board of his family bank to make his pitch. He carefully crafts his application request, keeping in mind the guiding principles of the family bank:

1. **Loans are only made for productive purposes that support the flourishing and growth of family members, such as education, starting a business, professional advancement, or buying a family home.** He creatively constructs an argument that access to a car will get him to school more quickly and conveniently than the school bus. The time he now spends waiting for the bus and on the long ride to school with multiple stops can now be used to focus more intently on his studies.

2. **Loans are expected to be repaid.** As part of his proposal, he outlines his plan to spend his summer caddying at a local golf course and earn the money to pay back the loan. He includes a repayment schedule with his application, and also points out that the car will help him meet the responsibilities of his new job schedule without inconveniencing his parents.

3. **Loans require the security of collateral.** Your son offers his laptop and video game console as security for the loan, to be returned to him upon the successful repayment of the loan.

4. **Loan requests must be practical and not excessive.** Finally, because he knows that he is going to be required to repay his loan, he doesn't ask for the money to buy a BMW convertible, but instead opts for a much more modest purchase of a used Ford Explorer, which will be an easier expense to repay.

Because of his thoughtful request and presentation, the bank board grants his request, and your son is able to buy his car. He feels a great sense of pride from having earned something of his own, and learns a valuable lesson about the value of hard work and accountability. He also keeps the car in mint condition, because he values the sacrifice he had to make to earn it. You feel thrilled that your son has had yet another experience to teach him these valuable lessons.

The success story ends with your son earning a spot as a regular caddy at the local country club through hard work and persistence. He loves the experience of working as a caddy, and particularly loves the great money he earns. He quickly earns enough to pay off the loan, but decides to keep working because he likes the extra income. He caddies during summers all the way through college, and ends up making some wonderful connections with golfers at the club, who help him start his business career after he graduates.

Although this example may sound a bit like a "fairy tale," this story effectively describes the true essence of the family bank concept. It can be used to transfer more than just money to the next generation, by ensuring that they learn about the accountability that comes with access to money. Regardless of the structure and complexity of your family bank, it will help foster respect for money, the discipline and satisfaction of hard work, and the confidence of experience.

Whether we're talking about the Rothschilds or the Smiths down the street, it all comes down to the same issue: The transfer of wealth without accountability leads to trouble. We deprive our children of the opportunity to make their own choices, learn their own lessons, find out who they are and how best to create abundance for themselves and contribute to society.

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