PRIVATE BANKING &
INVESTMENT GROUP

CAN YOU MAKE THE MONEY LAST? THE ROAD TO SUSTAINABLE WEALTH

Maintaining family wealth over generations can be challenging.
Now is the time to create and share a plan designed to benefit your children and their children.

SUSTAINABILITY IS TOP OF MIND—from sustainable environmental practices to businesses to investments. Yet as ubiquitous as these ideas are in most realms, few people articulate what sustainability means in their own personal lives. Determining how long you want your wealth to last, to whom you want to dedicate your money and what strategy you plan to use to get there can lay the foundation for finding broader purpose, meaning and empowerment for all involved. Consider the business owner who started with nothing and built a company that is now a leader in its industry. To her, sustainability means children and grandchildren who not only benefit from the wealth she has created, but, for those interested in expanding the business, keeping it thriving for generations to come.

Have you identified what sustainability means to you with respect to your own wealth?

For another couple, sustainability means perpetuating a philanthropic legacy through their private foundation; they will pay for their children's education but then expect them to find their own way in the world.

What about your life? Have you identified what sustainability means to you with respect to your own wealth? Is it about leaving a legacy for children, grandchildren and the generations beyond? Is it about charitable intent? Or is it focused on ensuring that you and a spouse or partner have sufficient resources for the rest of your lives?

Findings from a recent survey conducted on behalf of Merrill Lynch's Private Banking and Investment Group underscore that sustainability is a universal goal. All of the 171 participants in our proprietary survey, "The Meaning of Sustaining Wealth,"[1] indicate a strong desire to make their money last for the long term. Yet their plans and goals for making that happen vary widely. They all face essential questions of how to get from here to there.

[1] "The Meaning of Sustaining Wealth" survey was conducted in December 2013 by Phoenix Marketing International, an independent market research firm, on behalf of Merrill Lynch Private Banking and Investment Group.

Consider that among the wealthiest participants (with at least $10 million in assets), 63% take a dynastic, multigenerational view of sustainability. For this group, the optimal outcome is to maintain family wealth through many future generations. Among respondents 55 and younger the goal takes on a shorter time horizon: 58% say their goal is to support themselves and their children through their lifetime. Still others equate sustainability with a goals-based approach that will allow family members with financial resources dedicated to particular purposes—helping children make a down payment on a home, for example, or providing seed capital for a new business.

Why Definitions of Sustainability Matter

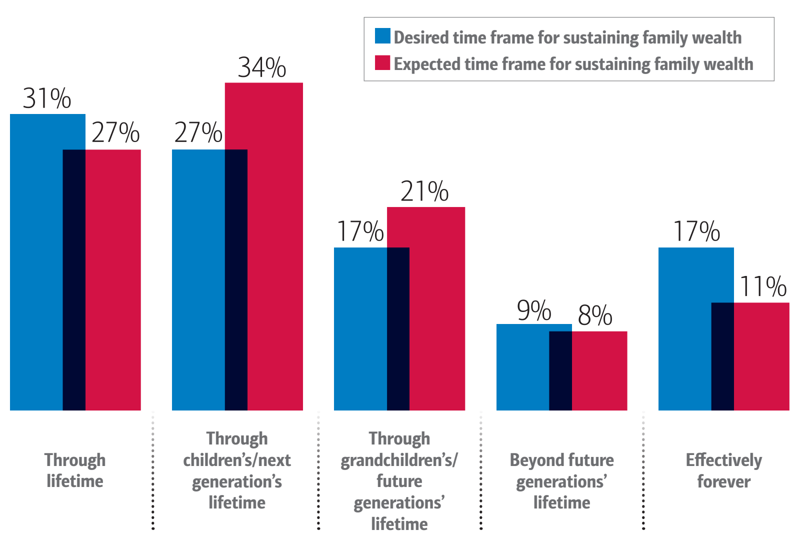
Determining what you mean by sustainability is crucial, because there's a big difference between providing partial support to two adult children trying to launch their careers and funding the education of eight hypothetical great-grandchildren in 2040. Your definition of sustainability will also influence how much you can spend each year without depleting family assets. But that, too, raises complications. Many people have unrealistic notions about what a sustainable spending strategy might be. For example, nearly two in five people surveyed believe a portfolio could last forever with a distribution rate of 6% or more, while another fifth say they simply don't know what might be appropriate (see "Perception vs. Reality" on page 4). In fact, data suggest that even for the wealthiest families, to be truly sustainable a wealth distribution rate may need to be as low as 2% to 3%. Only about a sixth of those surveyed identified this as the correct answer.

Even as they desire to sustain their wealth, many people are

Knowing your goal has a direct impact on what you can spend each year without depleting family assets.

DESIRE VS. EXPECTATION

What people want to happen and what they expect.



Source: Merrill Lynch "The Meaning of Sustaining Wealth" survey, December 2013.

More than two times out of three, family wealth fails to outlive the generation following the one that created it.

concerned about their ability to do so. A third of survey respondents say uncertainty about wealth sustainability is their primary financial worry, and research indicates those concerns are well founded. More than two times out of three, family wealth fails to outlive the generation following the one that created it, and 90% of the time assets are exhausted before the end of the third generation. “Shirtsleeves to shirtsleeves”—the notion that in financial terms, a family will soon find itself back where it started—is a looming and very real possibility. (For more on this subject, see *For Love & Money: A Comprehensive Guide to the Successful Generational Transfer of Wealth* by Roy O. Williams.)

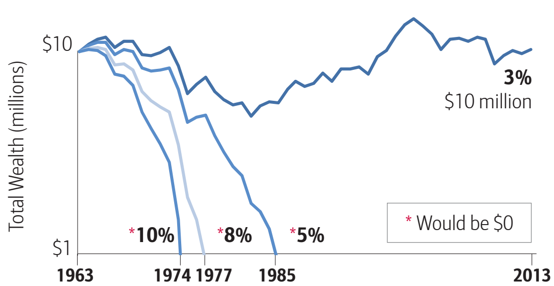
PERCEPTION VS. REALITY

These are the distribution rates that survey respondents believe can sustain wealth indefinitely.

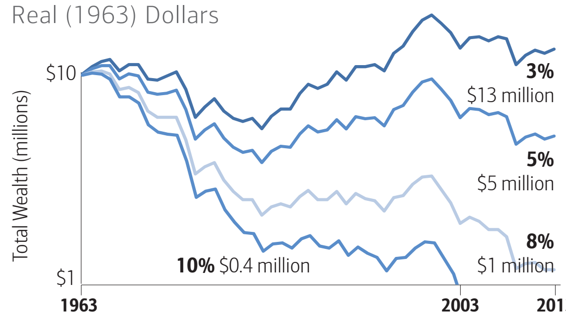
1–3%	4–5%	6–8%	10%	Over 10% per year	Don’t Know
16%	25%	16%	13%	10%	20%

But here’s what actually happens with two approaches to wealth distribution. (For more information, see page 11.)

A FIXED DOLLAR AMOUNT THAT GROWS WITH INFLATION‡ Real (1963) Dollars



A FIXED PERCENTAGE OF ASSETS‡ Real (1963) Dollars



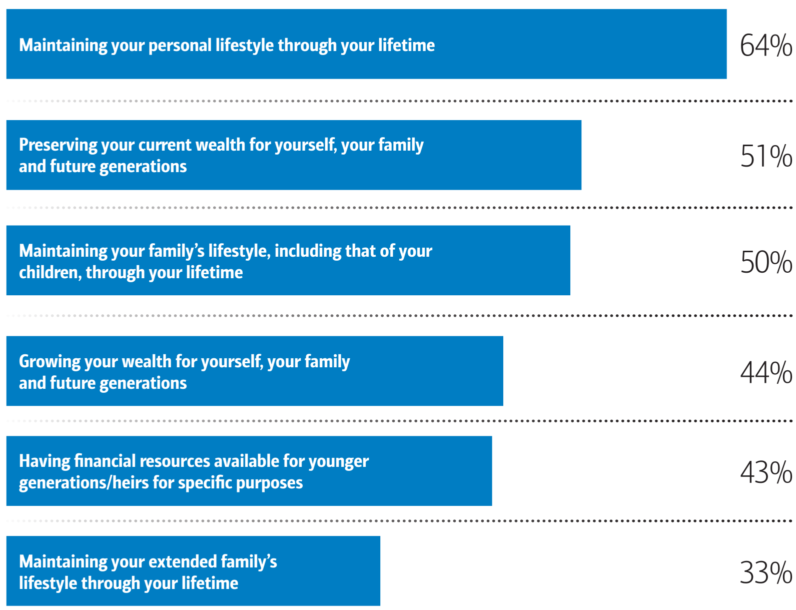
Sources: Merrill Lynch “The Meaning of Sustaining Wealth” survey, December 2013, and analysis by Merrill Lynch Global Wealth Management Investment Management & Guidance Investment Analytics.

These hypothetical results are for illustrative purposes only and are not meant to represent the past or future performance of any specific investment vehicle. Investment return and principal value will fluctuate and, when redeemed, the investments may be worth more or less than their original cost.

Taken together, these findings illustrate a striking discrepancy. While most people surveyed strongly desire to sustain their wealth through the next generation or beyond, more than a third are uncertain that they can achieve that goal and nearly half don't know what distribution rate could realistically be expected to succeed.

WHAT DOES "SUSTAINING WEALTH" MEAN TO YOU?

Survey participants chose these definitions.



Source: Merrill Lynch "The Meaning of Sustaining Wealth" survey, December 2013.

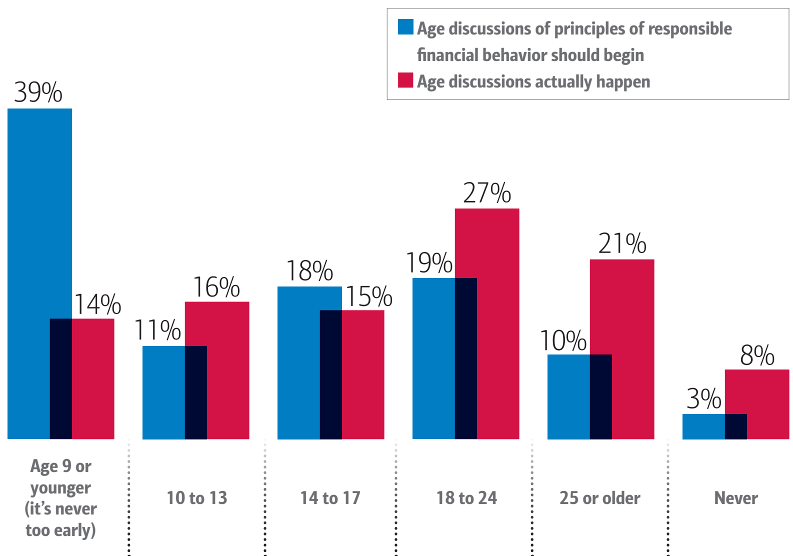
Fortunately, data isn't destiny. Identifying the challenges to wealth sustainability is the first step toward clarity and finding a new direction. But without clearly articulating a purpose, picking one distribution rate over another and rallying a family to stick with a plan can be very difficult. Success may require comprehensive, cross-generational family conversations about spending, saving and giving priorities. Wealth creators must drive this process by crystallizing and explicitly communicating their expectations. In some cases, families may have to temper expectations about their lifestyle choices. In other cases, they will need to sort through complex and sometimes negative emotions in order to clear the way for candid, productive discussions.

As with clean air and water, sustainable wealth is not a finite goal with a "begin" and "end" date, but rather a process that demands ongoing attention and continual mapping of current desires and needs against the longer-term goal of making money last. With that in mind, the themes we explore here may suggest a road map for you and your family as you navigate a path to sustainability that aligns with your vision, values and expectations.

Ask people to name the biggest threats to their wealth and they're likely to cite things that are almost totally outside their control.

TALKING ABOUT MONEY

Although almost four out of 10 survey participants say it's never too early to begin talking with children or other heirs about the principles of responsible financial behavior, few actually initiate such discussions with young children.



Source: Merrill Lynch "The Meaning of Sustaining Wealth" survey, December 2013.

Risks to Sustainability and Communicating About Wealth

Ask people to name the biggest threats to their wealth and they're likely to cite things that are almost totally beyond their control. In our survey, 55% of participants consider "performance of the markets" a risk to wealth sustainability, while 52% point to investment returns and 44% worry about government actions. "Lack of communication among family members," in contrast, is far down the list, cited by fewer than one in 10. Yet in fact those perceptions are upside down. A Williams Group study† showed that whereas risks from market events and taxes are relatively minor, most failures—about 60%—to transfer wealth from one generation to the next can be blamed on breakdowns in family communication and trust. In the context of this research, "trust" refers to reliability, sincerity and competence within the family.

The lack of communication between children and parents may create a deafening silence.

Though ideally that communication and trust-building start at an early age, many families view money as a difficult if not taboo subject. Whereas 39% of the participants in our survey believe it is never too early to discuss the principles of responsible financial behavior, most end up putting off those conversations until their heirs are 18 or older.

Parents may avoid such discussions for fear of dulling their kids' ambitions or creating a sense of entitlement when they discover the extent of the family wealth. Our own research has shown that those fears may not reflect reality: Young investors appear more burdened by wealth than entitled. Unfortunately, the lack of communication between children and parents may create a deafening silence that does not enable this financial discovery. And naturally curious children will likely fill the void with their own assumptions, perceptions and information—however right or wrong those may be. (Also see "Millennials and Money," here: pbig.ml.com/millennials.)

Parents may also fear losing control if they disclose too much and the kids unintentionally divulge too much information to others. The next generation may view that resistance as a sign of distrust or lack of faith in their judgment—which could actually set them back in later years when it's their turn to act as stewards of family wealth. And they may end up modeling their parents' spending behaviors without understanding the values that underlie them.

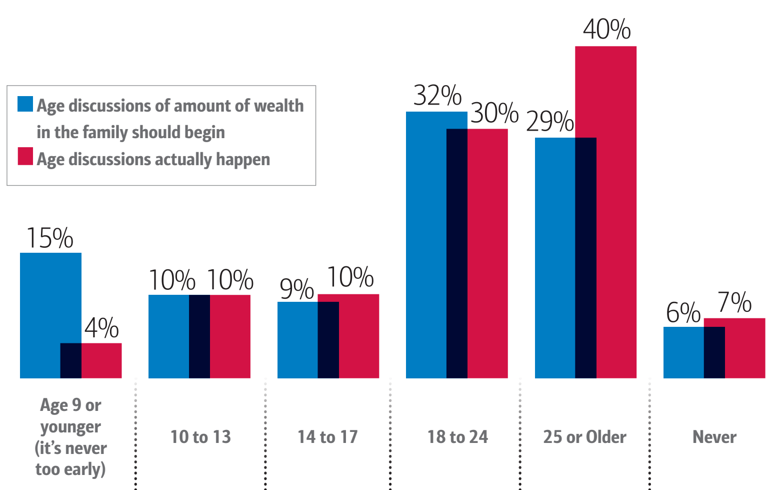
The next generation may view resistance to discussion as a lack of faith in their judgment.

Consider a client who was at odds with his daughter over what the father saw as the daughter's financial irresponsibility. Meeting with his wealth advisor, the father complained that his daughter expected to be given a luxury car. As it happened, the father himself recently purchased a car worth far more than the model the daughter requested. The advisor pointed out that under the circumstances, the daughter may have thought she was asking for a modest car, by comparison.

The advisor suggested that the father explain to his daughter how his car was a personal reward. In fact, the car purchase was a goal he

REVEALING YOUR WEALTH

Most survey participants believe discussions with children or other heirs about the amount of a family's wealth should—and do—begin at or after the age of 18.



Source: Merrill Lynch "The Meaning of Sustaining Wealth" survey, December 2013.

had set for himself decades earlier that came only after many years of extraordinarily hard work. By seeing the bigger picture, the daughter gained valuable lessons in accountability and earned rewards—and, by extension, became a more thoughtful manager of her own and the family's money.

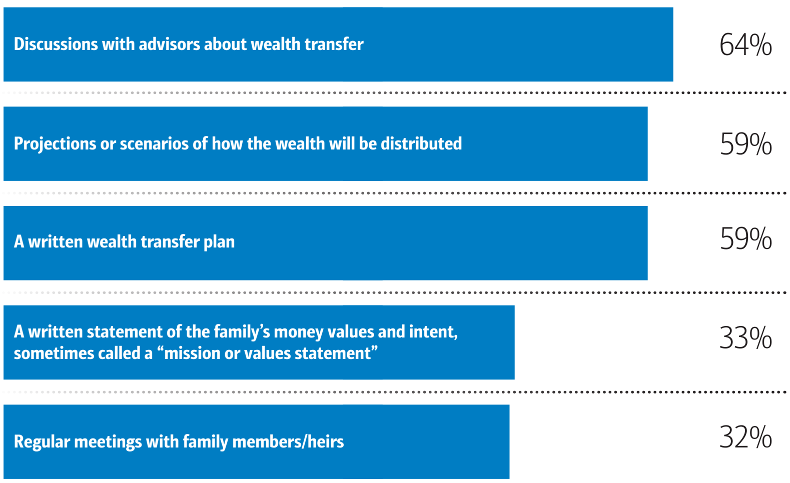
Making Wealth Sustainable

Mitigating the shirtsleeves-to-shirtsleeves scenario can begin with identifying the purpose of wealth and deciding how to define sustainability. Each family member will bring something unique to this conversation, and it's crucial to understand each perspective. For one thing, gender often plays a role in how people talk about wealth. Our research shows that women tend to have a higher level of uncertainty about the distribution rates that can sustain wealth indefinitely—yet at the same time, they're more likely than men to admit when they are uncertain. That willingness can lead to important questions and open up lines of communication among all family members.

The younger generation, in particular, may be anxious about what discussions of family wealth and sustainability could mean for their own future. Will they enjoy the lifestyle they've grown up with, or be expected to earn their own way in the world? Will they be expected to preserve and maintain family wealth for their own children?

YOUR ADVISOR'S ROLE IN SUSTAINING WEALTH

Survey participants believe that they work with their advisors in several important ways.



WORKING WITH ADVISORS APPEARS TO BOOST CONFIDENCE

Participants who haven't discussed sustaining wealth with advisors were less confident.

Source: Merrill Lynch "The Meaning of Sustaining Wealth" survey, December 2013.

GENDER AND SUSTAINABILITY‡

Understanding how male and female tendencies may differ can open the door to improved communication and better outcomes.

Although men and women are first and foremost individuals, not types, proprietary Merrill Lynch research suggests the genders do tend to diverge in crucial ways when it comes to how they view investing, wealth and sustainability. These differences don't have to be dividers; on the contrary, a better understanding of them can actually help open the lines of communication and put families that much closer to achieving their long-term financial goals.

Some gender differences apply specifically to sustaining wealth. For example, compared with just 9% of men, 30% of women in our survey said "I don't know" when asked to define an appropriate distribution rate that would sustain wealth indefinitely. Meanwhile, 82% of women, compared with 65% of men, feel more comfortable earmarking money for specific milestones, such as funding a graduate degree or buying a first home, rather than not. In terms of wealth distribution, women were twice as likely as men to prefer drawing down a fixed percentage of assets, with the dollar amount increasing to keep pace with inflation. That approach gives them the security of a steady income.

These findings speak to some underlying tendencies about how men and women approach their financial lives. Men are often more confident in their investment knowledge—sometimes to the point of overconfidence that ignores the inherent uncertainty of investing. But more than half of women self-identify as "less knowledgeable than the average investor," and they're more likely to admit when they don't know something. These preferences also speak to women's paramount concerns about wealth management. Research shows that a larger proportion of women than men fear outliving their assets, and that women place greater importance on investing for an overarching purpose.

Rather than seeing these difference as drawbacks, it's important to shine a light on the opportunities they create. Women's willingness to admit uncertainty and ask questions not only facilitates discussion, but it can also highlight gaps in knowledge for both novice and experienced investors. And a woman's emphasis on pinpointing a specific purpose for wealth helps to distill family priorities and hone investment goals. Putting these differences on the table can open lines of communication and create a productive dynamic—keys to sustaining wealth.

What's more, when both men and women are confident about expressing their investment personalities, the entire family may benefit. Behavioral finance research on group decision-making shows that groups that spend more time in discussion and generating solutions tend to outperform those that arrive at a solution immediately. Your advisor can help you better understand your partner's perspective by facilitating dialogue and asking questions targeted to your needs. One tool to ask your advisor about is the Investment Personality Assessment, Merrill Lynch's proprietary approach to help you and your family share your thoughts and feelings about investing. It can help you highlight key opportunities for sharing information by identifying your unique investment personality. The assessment includes many questions, but this sample offers some thoughts on where to start:

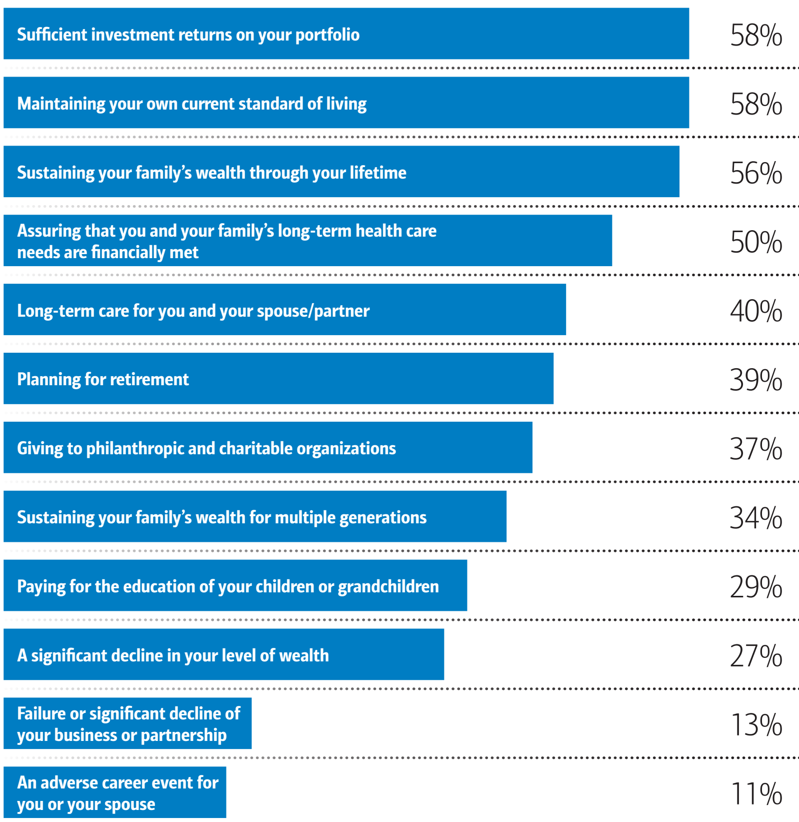
	STRONGLY AGREE	AGREE	DISAGREE	STRONGLY DISAGREE
My primary reason for investing is to provide for my lifestyle.				
I believe that I am investing enough for my future.				
I would like to leave behind a substantial sum of money to family members.				
I enjoy giving money to charities or other nonprofit organizations.				

Finally, keep in mind that it's crucial for matriarchs to help initiate family conversations about wealth and help lead the discussions—regardless of their self-perceptions about their financial knowledge. Everyone brings something unique to the table, so make sure that all voices are heard.

Source: "Women and Investing: A Behavioral Finance Perspective," Merrill Lynch's Wealth Management Institute, November 2013.

TOP FINANCIAL CONCERNS

Concerns about the future vary from whether portfolio returns will cover living expenses to whether there will be money available for philanthropy, paying for heirs' education, and meeting long-term health care needs.



Source: Merrill Lynch "The Meaning of Sustaining Wealth" survey, December 2013.

One way to empower heirs is asking them to videotape an interview with the family matriarch or patriarch about his or her values on wealth. Having the younger generation guide this process can help overcome rigid family hierarchies that too often hamper meaningful dialogue. A professional advisor may also help facilitate better conversations by drawing quiet voices into the conversation. Of the participants in our survey who met with their advisors to discuss wealth sustainability, more than half reported feeling a greater sense of confidence about reaching their goals.

An advisor's experience can also come into play during the next, all-important step in this process—considering how, exactly, to achieve the kind of sustainability of wealth that a particular family envisions. What rate of spending will permit the family to reach whatever goals they have agreed upon? Families often discover that their current lifestyle and spending patterns could exhaust family wealth much sooner than supposed.

Choosing among five potential distribution strategies described in our survey, most participants favored either of two approaches: establishing an initial percentage of assets as a family budget and then adjusting that amount for inflation in subsequent years; or spending the same percentage of assets each year. “The strategy you choose has a lot to do with your personal goals, but one major factor to consider is how flexible one or the other allows your spending to be,” says David Laster, director of Investment Analytics for Merrill Lynch.

According to Laster and Nevenka Vrdoljak, also a director of Investment Analytics for Merrill Lynch, these are some pros and cons to consider:

Strategy 1: Choose a percentage of assets as an initial spending budget, then increase that amount annually with inflation.
Suppose a family begins with assets of $10 million and chooses to spend 5% of that wealth—$500,000—in the first year. They would have the same amount to work with, adjusted for inflation, every year thereafter.

- **Advantage:** This approach provides consistent spending power that is unaffected by returns on investments. The family knows how much money will be available each year. “It’s a clear, smooth path,” says Laster.

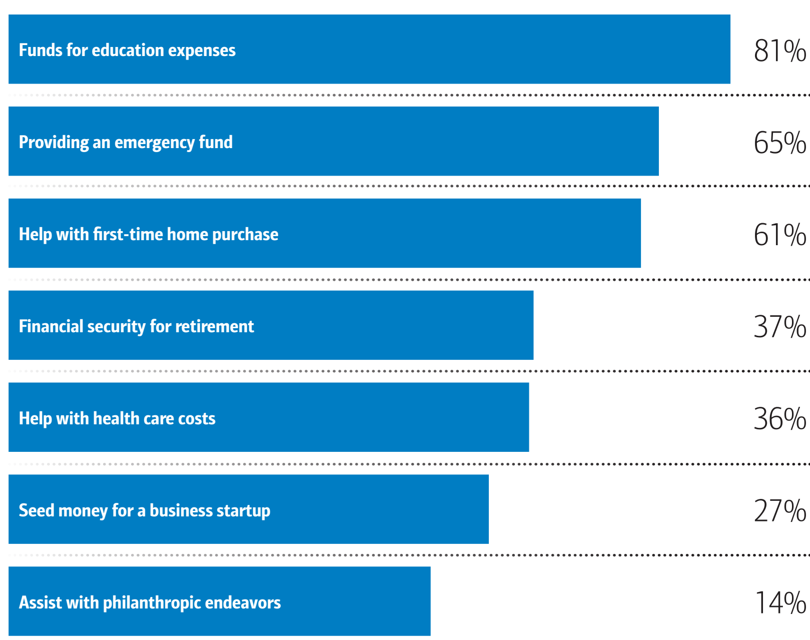
- **Disadvantage:** Because spending is disconnected from the amount of assets that remain, running out of money is a possibility. That puts a premium on choosing a sustainable distribution rate.

Strategy 2: Spending as a fixed percentage of assets.
With this approach, a family could choose that same 5% rate of spending, with the same initial distribution of $500,000,

BASE:
The 43% who say the meaning of sustaining wealth includes “having financial resources available for younger generations/heirs for specific purposes” (Refer to chart on page 5 for more information.)

HELPING YOUR HEIRS

Survey participants who hope to provide financial support to younger generations have wide-ranging priorities.



Source: Merrill Lynch “The Meaning of Sustaining Wealth” survey, December 2013.

> The spending rate a family chooses could have much to say about the sustainability of its wealth.

but future amounts would depend on portfolio performance. If investments have lost 15%, spending would fall by that amount, to $425,000.

- **Advantage:** Because spending is adjusted and the family spends the same proportion of its assets each year, assets could last much longer.

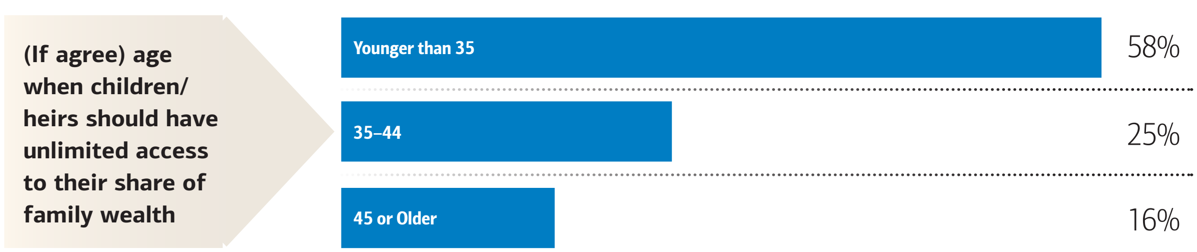
- **Disadvantage:** For the same reason—that the amount the family can spend will vary yearly—spending behavior may need to be modified.

In either case, however, the spending rate a family chooses could have much to say about the sustainability of its wealth. Beginning with a hypothetical $10 million portfolio in 1963, a family that opted to have spending grow with inflation and selected a 10% distribution rate would

ATTITUDES ABOUT ACCESS

Survey participants have varying ideas about when and under what circumstances their heirs should have access to their share of family wealth.

STRONGLY/SOMEWHAT AGREE	TOTAL	AGE		INVESTABLE ASSETS	
		55 or Younger	56 or Older	$5M to $10M	$10M+
Your heirs' share should be distributed as they achieve specific goals (complete their education, start their career, get married, etc.)	74%	83%	64%	74%	74%
Your heirs' share should be earmarked to help with specific goals (education, first home, etc.)	73%	84%	62%	72%	75%
Your heirs' share should be distributed on a controlled basis for their lifetime through a trust	66%	75%	57%	63%	71%
Your heirs should be given unlimited access to their share when they reach a certain age as determined by you	54%	56%	51%	57%	49%



Source: Merrill Lynch "The Meaning of Sustaining Wealth" survey, December 2013.

have exhausted its wealth within little more than a decade. With a 5% rate, the wealth would have lasted about twice as long, while a 3% rate would have resulted in the portfolio still being worth about $10 million in 2013 in real, inflation-adjusted dollars (refer to page 4 for more information). Keep in mind, too, that while these calculations account for fees, they don't factor in the impact of taxes, which could amount to a significant drain on wealth over the long term. For distributions to family members, it's important to set expectations for any distribution-related taxes.

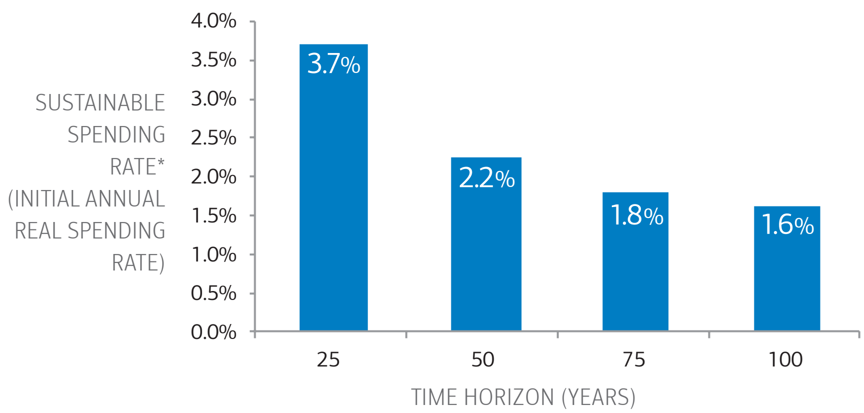
It's important to get specific from the outset, by articulating dollar amounts, time horizons and priorities for spending, sharing, saving and investing. The next step is to "test-drive" the plan, considering how it may fare in best- and worst-case scenarios. The better a family understands those scenarios in advance, the more prepared members will be to make needed adjustments along the way.

The biggest challenge—one that brings us back to the value of communication—may be unifying the entire family behind the same definition of what sustaining wealth really means. Consider how one

A CHECKLIST FOR SUSTAINING WEALTH

These steps provide the fundamentals of an ongoing process that can help a family get and keep on track.

1. **Identify** the purpose of wealth: Get specific about goals related to saving, investing, spending and sharing.
2. **Create** a strategy to pursue this purpose—and do the math: Articulate the dollar amounts, time horizons, risks and priorities with respect to saving, investing, spending and sharing in the best and worst of times.
3. **Readjust**, reprioritize and redo the math: Continuously course-correct on the journey toward sustainability.
4. **Build** in flexibility: Consider safeguards—for example, methodologies that decrease the likelihood that distributions will exceed a specified percentage.
5. **Prepare** the family: Continuously improve communication and planning via best practices and a holistic view of family wealth. For example, focus not just on the financial capital (and financial education), but on the human, intellectual and social capital. How can you best utilize the financial capital to help family members find their purpose and work together to solve problems and achieve shared goals?
6. **Monitor** the plan: Ensure a rigorous evaluation process of the strategy's success—or failure—during structured annual or quarterly family meetings.



*Based on Merrill Lynch capital market and fee assumptions. The assumed asset allocation is: 60% allocation to equity, 35% allocation to fixed income and 5% allocation to cash.

Source: Analysis by Merrill Lynch Global Wealth Management Investment Management & Guidance Investment Analytics and Quantitative Wealth Management Analytics Group (QWeMA).

It's important to get specific from the outset.

couple approached the question of what they hoped to provide for their grandchildren. They wanted to give each grandchild an edge in life, but they also realized that there needed to be limits, both in terms of their capacity to give and in what would be most helpful to their grandchildren. So, to guide their choices, they developed a family philosophy: Utilize money to support freedom of choice, allowing family members the ability to follow their passion, including a lower-paid career. They were able to define a sustainable distribution rate and to create a framework for gifts that would cover specific expenses for their grandchildren. They resolved to provide the fundamentals of an education, a home and a car for each grandchild—a legacy that would give all of them the ability to pursue their passions.

As lives, careers and goals evolve, paths will shift, and so may spending strategies.

The initial plan, of course, is just the start. As lives, careers and goals evolve, paths will shift, and so may spending strategies. Whereas most wealthy individuals and families have engaged a professional for investment management, tax planning and estate planning, most don't have anyone advising them on complex, emotional, intergenerational issues that they will encounter on their journey. Working together, families and their advisors have the opportunity to collaborate to develop a well-thought-out strategy that helps ensure wealth has the impact the family wants for themselves and their larger communities.

Guided by a statement of values that lays out an explicit family philosophy, family members are much less likely to see distributions as paychecks and more as tools. Being intentional about this process leaves families poised to make better decisions. And while you and your family members will no doubt feel vulnerable as you begin to work together to define your goals and create a plan, you're likely also to experience excitement and relief. As you collaborate to forge a clearer vision of how to bridge expectations and reality, the gap will start to narrow, and your personally meaningful vision of sustainability will come within reach. ■

QUESTIONS TO CONSIDER: Here are some questions you may consider on your own and with your advisor as you plan for sustainable wealth.

How do I define sustainable wealth?

What are some of the things I'd like to see my wealth accomplish over time?

How can I speak with my children and grandchildren about wealth and sustainability?

What are the biggest risks to my ability to sustain wealth?

What lifestyle changes would I be willing to make in the interest of sustainability?

DEMOGRAPHICS

"The Meaning of Sustaining Wealth" survey was conducted in December 2013 by Phoenix Marketing International, an independent market research firm, on behalf of Merrill Lynch Private Banking and Investment Group. The survey polled consumers in the U.S. about wealth sustainability; and a total of 171 people completed the survey, which took approximately eight minutes to complete. All respondents were 21 years of age or older and possessed $5 million or more in investable assets. The primary purpose of this survey was to gain insight into the meaning of sustainability, the desire to sustain wealth over generations, the role of advisors and the perceived risks to wealth sustainability among wealthy individuals and families.

Age

55 OR YOUNGER	56 OR OLDER
65	106

Investable assets

$5M TO $10M	$10M+
106	65

*The age and investable asset groupings were developed to determine whether differences exist between these groups of respondents.

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STACY ALLRED, managing director and wealth strategist in Merrill Lynch's Ultra High Net Worth Client Solutions Group, provides wealth management services to multigenerational families and executives. Her experience includes planning for income and estate taxes, retirement, philanthropic goals, investment strategy, insurance and employee benefits. She earned her B.S. in accounting and business, as well as a masters in taxation, with distinction, from DePaul University.

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‡Assumes a $25,000,000 investment that at year-end 1962 was allocated half to U.S. stocks (proxied by the S&P 500 Index) and half to U.S. bonds (1963–1975: Ibbotson U.S. Intermediate Government Bond Index; 1976–2012: Merrill Lynch Broad Market Index) and rebalanced annually. It is not possible to invest directly in these unmanaged indexes. Returns are net of annual fees of 1.3%. Annual spending as a percentage of the portfolio for the first year is as indicated in the figure and rises in subsequent years with inflation (CPIU). Withdrawals are taken at the end of each year.

† *For Love & Money: A Comprehensive Guide to the Successful Generational Transfer of Wealth*, Roy O. Williams, 2010.

‡ *Women and Investing: A Behavioral Finance Perspective*, Merrill Lynch's Wealth Management Institute, November 2013.
