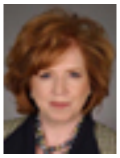

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Why It Pays to Consider A Congruency Audit

Many families lack congruency among their various legal, financial, business, and estate planning documents. Here's how you can help bring all the pieces into alignmnent.
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By Patricia M. Annino, J.D.

It's hard to overstate the importance of creating congruency among a client's various legal, financial, business, and estate planning documents. Does their estate plan—which is hopefully aligned with the family's goals, desires, and objectives—match their legal and financial plan documents? If the client is connected to a family business, real estate or philanthropic endeavor, is the estate plan congruent with their goals, objectives, and financial plan?

For most families, the answer is no. Although families may have possibly attempted to keep their plans congruent, the reality is that various independent professionals have been responsible for building each plan. Each of those professionals, such as estate planning attorneys, accountants, financial planners, bankers, life insurance professionals, and philanthropic advisers, is focused on a different part of the system.

While independently their work may be excellent, these professionals are often responding to a particular need expressed at a particular time, such as minimizing estate taxes, establishing who should control the vote of the company stock, deciding how to equalize assets, and protecting assets from a child's or sibling's divorce. Even if the "team" communicates well at these independent junctures, it is unlikely that this communication is deep or continuous.

Every adviser tends to focus on his or her specific area of specialty. Although some families might be fortunate enough to have a family office or trusted adviser who can help coordinate the communication among various professionals, neither tends to offer the 30,000-foot perspective that is usually necessary to provide true congruency among the many plans.

And that type of perspective can be critical. When viewed at that level, it is common to see black holes in coverage—areas that no family member or adviser thought of because they were focused on their own specialty or on a specific need at a specific time.

It is wise to perform a congruency audit for your most important clients. This can reveal technical, communication, fiduciary, tax, or liquidity issues, as well as a lack of coordination of the puzzle pieces. A core issue that surfaces in almost every congruency audit is the lack of enough education about what the plan is, what the plan means, and what the consequences of the plan are.

It is typical for a plan to be a "snapshot," but a family and its advisers must really view the plan as a "movie." The system must be coherent, workable, and flexible enough to accommodate the changes that are inevitably around the corner. When congruency does not occur, the black holes eventually become visible and disrupt the system's foundation.

In my 25 years of practice, I am still amazed at the black holes a congruency audit can show.

Recently, a family whose net worth exceeds $500 million asked us to review 26 irrevocable trusts that were drafted by one top law firm. Our analysis revealed that none of the trusts contained a “spendthrift provision,” which makes all of the trust assets vulnerable to creditors and division in case of a divorce.

In another case, individual discussions with multiple generations of a family revealed that the advisers and the family were still primarily focused on estate and financial planning at the parental/entrepreneurial level, even though $50 million of wealth had been transferred to each child at the next generation level—and no significant planning had been done there.

A planning objective should be to attain congruency—when the family’s goals, desires, and objectives match the system that is established to support those goals, desires, and objectives.

The ideal client candidate for a ‘congruency audit’ can be:

- A family that understands the importance of congruency and would like to embark on an in-depth discussion of goals, objectives, and desires in tandem with an in-depth diagnostic review of all legal and financial documents and structures. A family in such a situation is comfortable working with its current advisers, and, as a precautionary measure, would want an additional review. It’s like a family that is comfortable with its current physicians, but would go to the Mayo Clinic for a thorough battery of tests and a comprehensive diagnosis. While the current team of advisers may feel threatened by an independent review, they really do understand that this type of review is both prudent and valuable.

- A family in transition in which a key patriarch, matriarch, or influential family member has died, whose family office has disbanded, whose trusted adviser has retired, where there has been a generational switch in voting control of a family business, or a family member who must switch advisers because of a divorce or life-changing event. When a significant change occurs, it is important to view the system with fresh eyes. This process will ground the family, educate them about how they are currently positioned, and highlight recommendations that will be useful as they move forward.

- A family in need of education whose dynamic and financial wealth is entwined with legal documents such as irrevocable trusts, dynasty trusts, charitable trusts, limited liability companies, family limited partnerships, and/or charitable foundations. The parties to each of those legal documents must understand their respective roles and responsibilities, e.g., the role of settlor, trustee, beneficiary, manager, limited partner, and unit owner. Within the complexities of family dynamics, there are those who wear both a legal hat and a family member hat. There is often, however, a general lack of understanding regarding how and when those hats compete and collaborate.

- Often, the family members who currently operate the documents are not the same family members who established the documents. The current family members may be the settlor’s children, grandchildren, or great-grandchildren. As part of the educational process, the family and its advisers should prepare collateral documents and mission statements that allow the members who are currently operating the documents to understand and work through their roles and responsibilities.

What a diagnostic assessment process could entail

Should you wish to embark on this type of analysis for a key client, the process should consist of three phases:

- **Phase One:** Assess what each family member understands, i.e., what are his or her individual goals, objectives, and desires, and those of the overall family plan.
- **Phase Two:** An in-depth review of what the plan actually is against the backdrop of what different family members have envisioned. This encompasses a thorough review of all pertinent legal documents (estate planning documents, corporate documents, shareholder agreements, voting trusts, and foundation-related

documents) and discussions, if applicable, with the family advisers.

- **Phase Three**: Preparation and delivery of a report that summarizes phases one and two, and provides specific recommendations to achieve congruency.

A congruency audit is a critical element in a financial plan and CPAs are the most qualified advisers to perform it, being well-accustomed to applying objective audit methodology to financial situations. The CPA financial planner combines this approach with a thorough understanding of the components of financial planning, including tax, estate, retirement, investment and risk management planning, and is supported by the AICPA's PFP Section. The CPA/PFS credential demonstrates this combination of knowledge and experience and adds credibility to the audit report.

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