

# The Super Rich Stress Test Their Financial Plans—and So Should You!



## KEY TAKEAWAYS:

- Testing the assumptions of a financial plan, product or service can help confirm it's right for you—or identify any ways it could jeopardize your goals and put you at risk.
- High-level stress testing involves a systematic process that examines goals, changing scenarios and costs to determine the right course of action.
- Individuals and families don't have to be outrageously wealthy to benefit from a financial stress test.

The Super Rich (those with a net worth of \$500 million or more) who have a family office typically engage a sizable lineup of professional advisors to help them create and implement financial plans. To ensure those plans are both state-of-the-art and in line with their needs and wants, many of the Super Rich regularly “stress test” these plans.

Here's why you should join them in that effort—even if you're not nearly as wealthy.

## Asking “What if...?”

Stress testing your financial plan can be a very smart way to help make certain that the plan will deliver as promised. The fact is, financial plans that might look great on paper all too often prove to be much less impactful once they are implemented. It is not uncommon for there to be unintended consequences that can even derail your agenda.

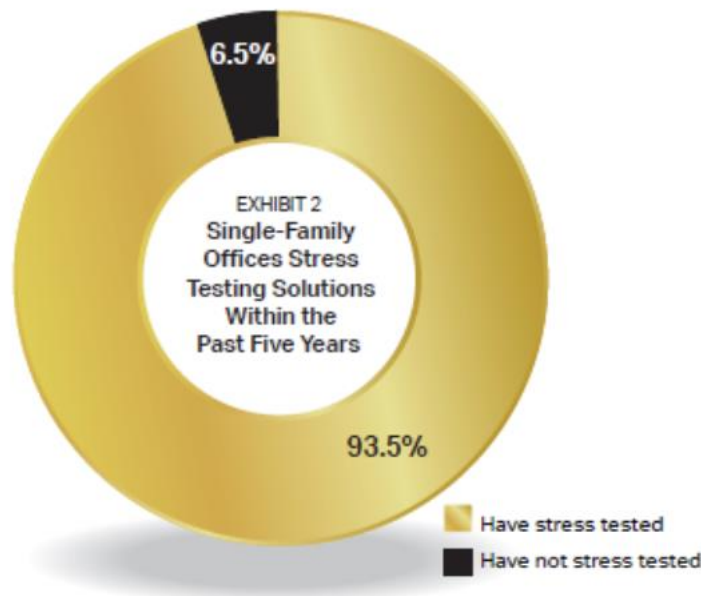
At heart, stress testing is when you ask, “What if...?” about a variety of areas of a financial plan you have or are considering. You probably conduct the same type of exercise in your business when considering options for your next product launch, expansion and so on.

When it comes to estate planning, for instance, a wealthy individual might ask questions like:

- What will actually happen to my assets when I pass on?
- How, precisely, will my family be affected?

- Who will be tracking the hard assets such as artwork and jewelry to make sure they go to the designated heirs as opposed to vanishing?
- Who is going to make sure my estate plan is being executed as it's supposed to be?

Stress testing is a very powerful form of a second opinion—and getting second opinions is very characteristic of successful family offices. More than nine out of ten single-family office senior executives we surveyed had stress tested financial services and products they were considering for their affluent family clients over the past five years (see Exhibit 2).



N = 199 single-family office senior executives.  
 Source: Russ Alan Prince and John J. Bowen Jr., *Becoming Seriously Wealthy*, 2017.

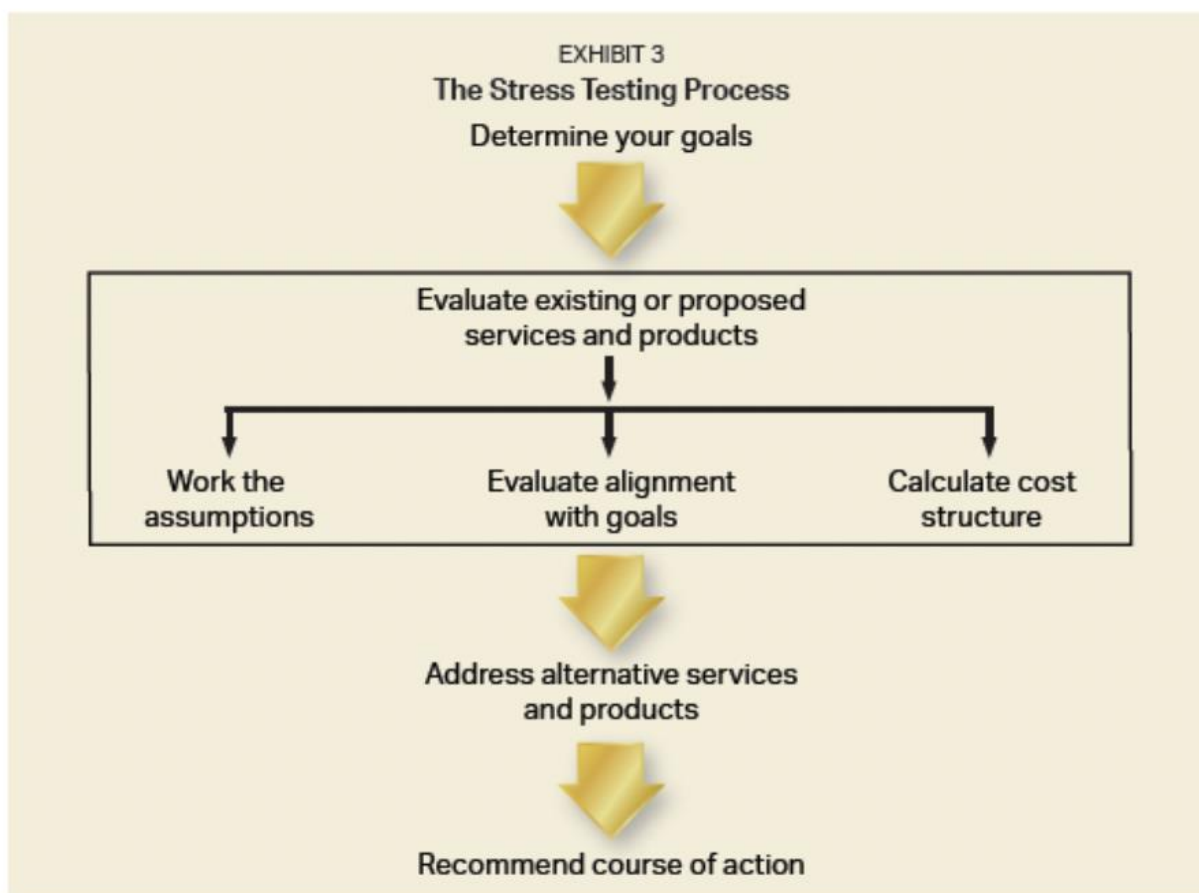
The impact of these stress tests on the financial lives of the Super Rich has been powerful:

- **Reaffirmed service or product.** For 90 percent of the single-family office senior executives, the stress testing confirmed that certain financial services or products they were considering were indeed applicable to them and appropriate for their situation.
- **Went in a different direction.** For four out of five single-family office senior executives, stress testing resulted in their choosing to go in a different direction—opting *not* to use the financial services or products that had been recommended to them.
- **Chose a different provider.** For nearly three out of five single-family office senior executives, getting a different perspective prompted them to implement the solution—but with a different provider.

- **Modified approach with original provider.** About half of the single-family office senior executives, after stress testing, modified the service or product but chose to implement it with the initial professionals making the recommendations.

## Running a reliable stress test

To be effective and informative, stress testing should be done in a systematic manner. While there are some variations, the basic process starts by determining the individual's or family's goals and objectives (see Exhibit 3). The goals being sought, the problems to be solved and the opportunities to benefit from should be the driving forces behind the choice of financial and legal solutions.



Once the goals and objectives are clearly understood, the specific existing or proposed financial services or products can be evaluated. There are numerous ways to dissect and critically assess financial services and products:

- **Work the assumptions.** A plethora of assumptions underlie all services and products—and it's common for professionals to use somewhat Pollyanna-based

assumptions when trying to sell their solutions. In stress testing, these assumptions are modified to determine how the solutions will work when a given scenario changes.

- **Evaluate alignment with goals and objectives.** A solution might prove to work extremely well, but still not achieve the desired results. It's essential to ensure that the services and products will accomplish the individual's (or family's) goals and objectives.
- **Calculate cost structure.** The intent here is to identify the best *and most cost-effective* solution possible. When calculating cost structures, all the expenses should be specified—including long-term costs.

Based on the stress test's evaluation of the existing or proposed solutions, alternative products or services might be considered. It can be very useful to do side-by-side comparisons between such alternatives and the solutions being considered or currently used, asking questions like:

- How do the assumptions compare?
- How do the alternatives rate when it comes to achieving the individual's or family's goals and objectives?
- Which solutions are more cost-effective?

The end result of the process: recommendations. Based on those recommendations, there are five courses of action to consider taking (see Exhibit 4).

EXHIBIT 4  
Courses of Action

Course of action	Critical factors
Stay the course	The solutions are appropriate
Choose different solutions	A "system fail"
Choose a different professional	The solutions are appropriate except that the providers are not truly capable and/or are cost-inefficient
Use a modified approach with the original professional	A little tweaking is required
Continue stress testing	A different professional should conduct the stress test

1. If the stress testing finds the solutions being used or proposed to be on target and of high quality, the recommended action is to "stay the course."

2. If the stress testing finds what may be described as a system failure—for instance, the financial products being used are not going to achieve the desired results and might even blow up—the right move is to take a different course of action.
3. If the solutions are appropriate but the professionals involved are really not up to the task of implementing them (or they charge too much money), it will usually make sense to switch to more capable and/or cost-effective experts.
4. If the solutions can be made more powerful with only slight modifications, the best route is often to stick with the original professionals and have them make the minor changes needed.
5. There are occasions when the individual or family chooses a professional to conduct a stress test and that professional is not up to the task. This often comes out clearly in the process or the results of the stress testing. The only viable course of action is to select a different professional to conduct the stress testing.

## Stress testing for everyone

Although stress tests are commonly used among the Super Rich, they should be a part of most people's due diligence process when vetting financial plans, products and services. Frequently, stress tests uncover flaws in financial plans as well as better ways to achieve desired outcomes. For those reasons, stress tests will likely benefit a great number of people—especially business owners and their families, who generally have so much of their future financial security riding on one asset: their business.

Certainly there is a cost to stress testing estate, asset protection and income tax plans. That cost will depend greatly on the complexity of the testing involved and the family's situation. However, in our experience, a stress test fee can be a whole lot cheaper than the costs—financially but also emotionally and psychologically—of a plan or solution that is fundamentally flawed or in conflict with your goals.

If you are curious about whether a financial product or service you have—or are considering—will work the way it is supposed to under various conditions, you might benefit from a stress test.

**Our recommendation:** If you think this strategy may help you achieve your goals, contact your financial or legal professional.

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VFO Inner Circle Special Report

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