REALITY CHECK$

With the suddenly wealthy client, planners must emphasize patience and a clear, step-by-step plan.

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Stephen King apparently went a little crazy when, after years of just getting by, he found himself wealthy from the paperback sale of his first horror novel, Carrie. Like other newly rich people, King went on a shopping spree. Fortunately for his bank balance, he was living in a small town and the most expensive present he could find for his wife was a hair dryer.

Other people with unexpected windfalls have been more fiscally inventive than King, making enormous ill-advised purchases and ghastly investment errors. Even those who work with a planner from the outset can prove to be unusually difficult and irrational. Planners who choose to work with the suddenly rich have to use special people skills and sometimes even wear a psychologist's hat.

An unexpected inheritance, large divorce settlement, sale of family business, sudden access to retirement savings or even a lottery jackpot can all put millions into the hands of people who never had large sums to manage and never felt the need for advice. For those of modest means, even half a million dollars can radically and permanently change their lives.

"Unfortunately, this is a time when there are more emotion-based decisions than rational ones," says Susan Bradley, CFP, of the Sudden Money Institute in Palm Beach Gardens, Fla. "Helpful" friends and relatives come out of the woodwork with advice on investing the money -- and spending it -- leading to continued confusion. The planner's job is to deal with the emotions while piloting a rational course. Planners seem to agree that although the management of the money may be the same whether it came gradually or all at once, the management of the client differs.

For example, the clients can have certain distinct attitudes based on how they got their money. Heidi Flammang can understand this. She found herself a widow at 27 with a considerable insurance settlement. Her own experiences managing her new wealth, and her frustration dealing with planners she felt were incompetent, led her to create the Maginot Group in Parker, Colo., which specializes in helping clients with sudden wealth issues.

"When a client inherits money, particularly in a tragic situation, they may want to become totally involved in all investing decisions," she says. "They see the money as a special responsibility, a trust." Those who won a lottery,

or a professional athlete who just hit the big time, for example, may be more willing to leave the details to the professionals. However, in their giddiness they may lack discipline; Flammang says this sub-group is likely to change planners a lot.

In general, says Ron Selik, CFP, of Selik Financial Services in Troy, Mich., what separates the suddenly rich from those who became rich gradually is the emotional event that led them there. To work through these problems, planners must have a combination of patience and discipline. Experienced advisers even stand ready to refer particularly difficult clients to psychologists.

An initial period of reflection may be the best advice a planner can offer the newly wealthy. Before clients buy a mansion or book a suite on the QE2, Bradley and other planners in her network recommend a decision-free zone for six months to a year. During this period the money, whether it comes from an insurance settlement, relative's estate or IPO windfall, goes into conservative, liquid investments, such as CDs or money market accounts. Based on the amount of money, planners may authorize small expenses, such as a new car to replace the old clunker (but not a Rolls Royce), but no new houses or commitments to long-term investment strategies.

Planners also have to stand firm. Steve Wightman, a planner at Lexington Financial Management in Lexington, Mass., practices financial tough love, saying, "Clients commit with us from the start or we don't work with them." And Selik says, "I act as the scapegoat," particularly during the decision-free zone. When friends and relatives descend on the client with requests for money or dubious investment opportunities, the client can just say, "I'm sorry, but my planner has it all tied up now and won't let me make any commitments at the moment."

The decision-free zone is a deceptively quiet period, because even though no strategies are being implemented, both planner and client are using the time to create a foundation for long-term money management. Bradley sees planning and preparation as the first part of a structured plan, in which implementation (such as buying a house and making investments) and stewardship (i.e., cash flow and estate planning) constitute the second and third, respectively. "If clients know there is an order, they will hold off on major spending and buy into the plan," she says.

Meanwhile, they should compile a "bliss list," a list of what the client wants to do or accomplish with the money. If a couple receives sudden wealth, each one will create his or her own list, which they will eventually merge. Bliss lists are subject to revisions over time, as the planner helps the client assign values and "perform reality checks." What is affordable? Do you want to buy a new house? Retire at 45? Sail around the world? "You can probably do some things on your list, but not everything," Bradley says.

Once there is a game plan that is in line with reality, the planner can move into implementation. Of course, these clients may never have even considered a financial plan before, and never thought actual management of money was going to be an issue in their lives, and so the planner has to keep this in mind. "The plan can be a hard sell," says Kent (Chip) Addis, Jr., of Addis & Hill in King of Prussia, Pa. "About a third of sudden-wealth clients will say a new house is the top priority. Another third will say education is." But, as he grimly relates, only about 2% want to primarily use their money to pay down current debt, and only 1% consider investments as most important.

Problems can crop up no matter where the money comes from. Selik says some of his sudden-wealth clients came into money not from something startling like a lottery but from the very prosaic source of a well-funded 401(k) plan. "For years, they couldn't really touch this; it was Monopoly money. Now they could have $1.5 million in the account." He has to point out that this money has to last for years; it's not something they can quick go out and spend. Maybe the new retirees can afford to set up a college fund for a grandchild? Great, says Wightman, as long as no one is too squeamish to discuss money. "You need intergenerational planning," he says. "Preparation is better than surprise." For example, he knew of one family in which parents and grandparents each started a college fund for a child without the other's knowledge, over-endowing the future scholar.

Shelley Fernstrom, of Raymond James in Naples, Fla., works with lots of divorced women. "It doesn't matter whether they're getting $100,000 or $10 million. They have to develop a budget," something they may not have done before if their husbands handled all the money issues. "Did they get the marital residence or is it being sold? Is there child support?" In addition to a settlement, some women get "rehabilitative alimony" for a few years until they can get back onto a career path. "I have to explain that this money isn't going to last forever."

This was a concept Wightman had to hammer home in a case involving a $12 million estate. "The divorced woman's new boyfriend was already talking about a yacht and mansion, without giving any consideration to taxes she still had to pay." Also working with many divorced women is Michelle Maton, CFP, of Aequus Wealth Management Resources in Chicago. "Some of these women now have $4 million and up. They have to ask themselves what they want to accomplish." Maton teaches them about managing their own money and cash flow with the aid of Quicken, the simple off-the-shelf budgeting software.

Fernstrom also has to explain that unlike salaries, income from investments can vary from year to year. George Strickland, CFP, of Financial Synergies Advisory in Houston, finds even a good investment year causes problems for clients just getting used to the idea of living partly or entirely from

investment income. "If we're assuming a steady 10% a year from certain investments and one year we get 20%, I tell clients to give the extra back." That is, he tells them to reinvest it and not assume there will be another 20% next year.

Many clients also want to use their new wealth for charitable purposes. Again, this is a sudden ability, not a gradual development as with clients who slowly increased their money, and charitable giving, accordingly. Philanthropy should be subject to the same rational plan as other uses of the money. And clients don't have to have tens or hundreds of millions of dollars to engage in charitable giving in a meaningful way. Harvey Rowen, of Starmont Asset Management in San Francisco, says even clients with a few million can set up a charitable foundation. "The planner needs to assemble a team, with a lawyer, CPA and a charitable-giving consultant, if necessary."

As with all your clients, the investment specifics will vary with the amount of income, age of clients and their goals. Nevertheless, Fernstrom has found that many of her clients can do well with a mix of mutual funds and bonds for income. In a more general way, Strickland says he ascribes to the "three-bucket theory." For many of his clients, he puts two years of what the client will need to live on into CDs. The client then lives off that. Three additional years of income is in bonds. The rest is in long-term investments. He finds this a suitable balance between the desire for high interest and the need for some liquidity.

Of course, investment plans and matching goals with money is nothing new for planners. But with a suddenly wealthy client, it isn't the "wealthy," it's the "suddenly" that's the problem. Instead of getting to prepare for wealth over many years as a business grows over the decades, or as a client rises from junior manager to CEO, these challenges hit recipients all at once. Sober analyses of fund performance sometimes come up hard against irrational human emotion. Bradley sums it up: "The client will follow your lead, but the adviser has to be strong. Clients with new money may suddenly feel too empowered and thus not acquiesce. They think of themselves as too rich, too beautiful, too popular, to follow your advice."