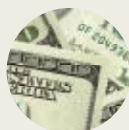




# NAPFA

*Planning Perspectives*



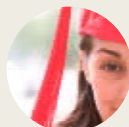
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In this issue...

## During Time of Volatile Markets, Long-Term Outlook Remains Crucial

In the last two months, we have been reminded forcefully that stock markets around the world can be very volatile. It's a lesson that is periodically learned...and then forgotten...and then relearned.

In this issue of "NAPFA Planning Perspectives," we provide basic investing advice that is both timely and has withstood the test of time. There are several recurrent themes in the investment articles, including the importance of maintaining a long-term outlook and avoiding the temptation to jump in or out of the stock market. Remaining calm is necessary, whether

you are investing in individual stocks or bonds, mutual funds or bond funds, or highly popular ETFs. Your advisor's role is to help ensure the implementation of an objective, long-term oriented approach.

"Planning Perspectives" concludes with two articles on other subjects. The first is an analytical piece that puts into perspective the amount of money that a parent might wish to save for a child's college education. The second is a reflection about losing a beloved family member, and how each of us can ease those burdens on the people we leave behind.



## NAPFA Expands Fiduciary Information Online

In an ongoing effort to bring important information to the public about the importance of working with a Fiduciary financial advisor, NAPFA has added more

information and links to its Website, [www.focusonfiduciary.com](http://www.focusonfiduciary.com). The Website includes a link to NAPFA's Fiduciary Podcasts.





# Investing

## Keep It Simple

Chad Carlson, CFP®, [www.bdfllc.com](http://www.bdfllc.com)

Investing can be overwhelming. You have to do research, read articles, listen for tips, review your existing investments, maintain diversification, and so on. In reality, investing is only as difficult as you make it. The basics of investing are easy:

- Step 1: Pick a stock/bond mix.
- Step 2: Select diversified investments to achieve that mix.
- Step 3: Monitor the portfolio.

Of those steps, the one that captivates many investors is step 2. Though it is far more important to focus energy on proper asset allocation, stock picking is, unfortunately, the part that delivers the most excitement. People enjoy stories, and the stories lie in the investment selection.

The draw of stock picking creates a problem because investors are often overconfident in their ability to achieve success. Sure, someone can get lucky and pick out a hot stock before a price jump, but what isn't acknowledged is that he or she is just as likely to pick a stock that is a dog. Often, investors arrogantly believe they can identify investments that will outperform, either through quick research on the Internet, an overheard stock tip, or some new product release that is identified as a "sure thing."

If our expectations for stock picking are so high for ourselves, then our expectations of mutual fund managers must be even higher. They are professionals who spend their days doing research. Surely a manager with a research staff and high-powered analytical tools can identify winners.

The scary part is that even these well-informed professionals have the odds stacked up against them. These smart people are competing with other smart people like themselves that collectively form the market—the very thing they are trying to outperform.

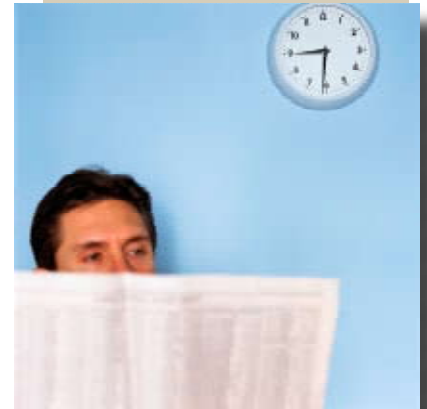
Simply look to 2006 for an argument against using stock pickers. The S&P 500 outpaced 80% of active mutual funds. Had you simply invested in an S&P 500 index fund, you could have outperformed, avoided the higher management fee, and most likely paid less in taxes due to the efficiency of index funds.

### Simple = Boring = Effective

That strategy may seem too simple...but what's wrong with simple? The problem for most of us is that it's a boring strategy.

My response is this: Sure, active management may deliver a better story, but getting good stories to tell should not be your goal in investing.

By investing in index funds that capture large, small, and foreign companies, you work to own the market. You don't have the ability to beat it. Your aim is to have a different kind of story to tell, one that involves a happy ending and attainment of your financial goals. With index investing, not only do you give yourself a better chance of reaching your investment goals over the long run, but you will spend less time worrying about your investments and more time with your family enjoying the wealth you have worked to create.



## Keep it Simple

- ➔ *Pick a stock/bond mix*
- ➔ *Select diversified investments to achieve that mix*
- ➔ *Monitor the portfolio*



# Investing

## The Study Your Broker Doesn't Want You to Read

J. Patrick Collins, Jr., CFP®, EA, [www.greenspringwealth.com](http://www.greenspringwealth.com)

A groundbreaking study published earlier this year confirmed many of the thoughts we had about the financial services industry, but were unable to prove. The conclusion: Years of research have found that as a whole, do-it-yourself investors outperform brokers.

“Costs and Benefits of Brokers in the Mutual Funds Industry,” written by three academics from Harvard Business School and the University of Oregon, may have long-reaching implications for broker-sold investment products and investment advice altogether. Quoting the study, “We begin with a positive hypothesis: the prominence of funds sold through brokers implies that brokers provide consumers with valued services. Our study has identified few, if any, of these benefits.”

The study tries to answer five questions.

**1. Do brokers help their customers find hard-to-pick funds?** Yes—but those funds have underperformed their do-it-yourself counterparts.

**2. Do brokers help their customers find lower-cost funds?** No. Even before sales loads, the costs associated with a broker-sold fund easily exceed a no-load fund. The excess costs of broker-sold funds over no-load, directly purchased funds are: equity, 0.77%; fixed-income, 1.38%; money market, 0.21%. And remember, that’s a cost differential that occurs year after year after year.

**3. Do brokers offer and sell higher-performing funds?** No. The study reviewed fund performance from 1996 to 2002 and found that directly sold, no-load funds outperformed broker-sold funds (before sales loads) by a small margin.

We would add this point, which is not mentioned in the study. The broad stock market outperformed both do-it-yourselfers and brokers, handily (see table of annual returns on right).

The implication is that passive managers consistently outperform active investors. That’s why so many Fee-Only financial advisors build

their clients’ portfolios using low-cost, passive investment vehicles.

**4. Do brokers exhibit better asset allocation and timing abilities?** The study found no evidence that brokers provide superior asset allocation or market timing.

**5. Do brokers help their customer’s correct destructive behavior?** Investors often allow their emotions to play a large part in their decisions. This is one of the largest reasons for underperformance. Unfortunately, both do-it-yourselfers and investors who rely on brokers seem to act emotionally and chase returns.

In fact, emotion can be a broker’s ally because he or she is typically paid on commission. Investors tend to get excited and want to buy an investment that has performed well. Conversely, when an investment does poorly, a typical investor wants to sell it. Brokers take advantage of an investor’s emotional state for the easy sale.

### Conclusions

What conclusions can we draw from this study? First, investors should take a hard look at the advice and service they receive from their broker. We believe that how an advisor is compensated (product sales vs. advice) does affect the long-term performance of an investor’s portfolio, even though it is not specifically measured in this study. Because brokers get paid to sell products, closing the sale will often be the primary goal, not reliable investment advice.

Second, costs matter. One of the reasons do-it-yourself investors have outperformed brokers as a whole is that the products they use have lower costs.

Finally, it is imperative that investors (whether using an advisor or not) have a written process with regard to how their portfolio is managed. Without a disciplined process, investors and advisors have shown they allow their emotions rule their decision making.



Average Annual Return (1996-2002)
Broker-sold equity funds: 1.13%
Do-it-yourself equity funds: 1.65%
Russell 3000 Index: 6.45%



# Investing

## Ten Most Commonly Asked Questions about ETFs

By Russell Wild, MBA

Exchange-Traded Funds are one of the fastest-growing investment categories for individual investors. ETFs are bought and sold just like individual stocks or mutual funds. But ETFs are designed to provide an ultra low-cost way to track the performance of a broad stock market index or a specific sector of the economy. For an investor seeking to build a balanced portfolio, ETFs can be an attractive solution.

Here are common questions that investors ask about ETFs.

1. Are ETFs appropriate for individual investors?

You bet they are. ETFs are essentially friendly index mutual funds with a few spicy perks. They are more than appropriate for individual investors. In fact, given their low expense ratios, high tax efficiency, and the ease with which you can use them to construct a diversified portfolio, ETFs form the perfect building blocks for just about any individual investor's portfolio.

2. Are ETFs risky?

That depends. Most ETFs track stock indexes, and some of those stock indexes—such as technology stocks or the stock markets of emerging-market nations—can be extremely volatile. Others track broader segments of the U.S. stock market, such as the S&P 500. Those are less volatile. Other ETFs track bond indexes, which are even less volatile (but less potentially rewarding).

3. Do I need a financial professional to set up and monitor an ETF portfolio?

Do you need an auto mechanic to service your car? I don't know. It depends on both your particular skills and your inclination to spend a Sunday afternoon getting greasy under the hood.

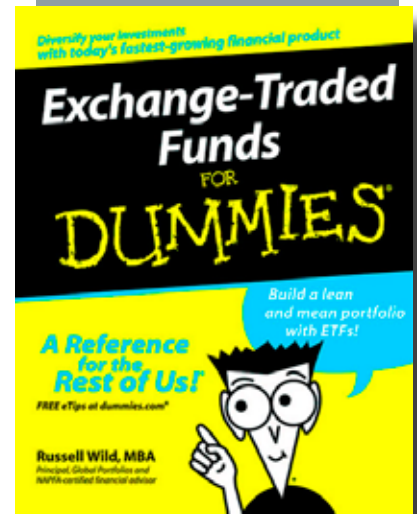
Setting up a decent ETF portfolio is very doable. You can certainly monitor such a portfolio, as well. A professional has special tools and (I hope) objectivity to help you understand investment risk and construct a portfolio that fits you like a glove, or at least a sock. A financial planner also can help you to properly estimate your retirement needs and plan your savings accordingly.

Do be aware that many investment “advisors” out there are nothing more than salespeople in disguise. Don't be at all surprised if you bump into a few who express their disgust of ETFs! ETFs make no money for those salespeople, who make a living hawking expensive (often inferior) investment products. Your best bet for good advice is to find a Fee-Only financial planner. If you are more or less a do-it-yourselfer but simply wish for a little guidance, try to find a Fee-Only advisor who will work with you on an hourly basis.

4. How much money do I need to invest in ETFs?

You can buy one share of any number of ETFs for as low as the price of a share. But since you pay a commission to trade (average is about \$15), buying one \$20 share (and thus paying a 75 percent commission) would hardly make good sense. Starting at about \$3,000, it may

*Continued on next page.*





# Investing

ETFs...Continued from previous page.

be worth investing in ETFs, but only if you plan to keep that money invested for at least several years.

5. With hundreds of ETFs to choose from, where do I start?

The answer depends on your objective. If you are looking to round out an existing portfolio of stocks or mutual funds, your ETF should complement what already exists. Your goal is always to have a well-diversified collection of investments.

If you are starting to build a portfolio, you want to make sure to diversify within stock and bond asset classes.

6. Where is the best place for me to buy ETFs?

I suggest setting up an account with a financial supermarket, such as Fidelity, Vanguard, T. Rowe Price, Charles Schwab, or T.D. Waterhouse. Each of these allows you to hold ETFs, along with your other investments.

7. Is there an especially good or bad time to buy ETFs?

Not really. Studies show rather conclusively that the stock and bond markets (or any segment of the stock or bond markets) is just about as likely to go up after a good day as it is after a bad day (week, month, year, or any other piece of the calendar). Trying to time the market tends to be a fool's game.

8. Do ETFs have any disadvantages?

Following an index, as most ETFs do, it is unlikely that you will see your ETF wind up

No. 1 on any magazine's list of Top Funds for the Year. (But you are unlikely to find any of your ETFs on the bottom of such a list, either.)

The bigger disadvantage of ETFs is the cost of trading them, although that cost should be minimal if you do not shift investments constantly.

9. Does it matter which exchange my ETF is traded on?

No. The vast majority of ETFs are traded either on the American Stock Exchange or the NASDAQ. It doesn't matter in the slightest to you, the individual investor.

10. Which ETFs are best in my IRA?

Generally, those investments that generate income and either interest or dividends are best kept in a tax-advantaged retirement account, such as your IRA or 401(k) plan. That would include any bond, REIT, or high-dividend paying ETF.

Try to put your ETFs that have the greatest potential for growth into your Roth IRA.

*Note: This article is based on a chapter in Russell Wild's book, "Exchange Traded Funds for Dummies," published by Wiley in 2007.*



## Five highly traded ETFs

### SPDRs

(Available on American Stock Exchange, symbol: SPY)

**PowerShares QQQ**  
(NASDAQ symbol: QQQQ)

**iShares Russell 2000 Index Fund**  
(AMEX symbol: IWM)

**iShares MSCI Emerging Markets Index Fund**  
(AMEX symbol: EEM)

**iShares S&P 500 Index Fund**  
(New York Stock Exchange symbol: IVV)



# College Planning

## The 22-Year Car Payment, Or How to Finance a Newborn’s College Education

By: Ronald W. Rogé, MS, CFP® and Christine Parisi, CFP®, [www.rwroge.com](http://www.rwroge.com)

My staff and I were eating lunch together in the office, as we often do. Jeff Roberto, our Director of Portfolio Operations and Administration, who is the father of three children, thanked me for giving him an article on how much it costs to raise a child these days: about \$1 million, according to the calculations used in this analysis.

The conversation quickly turned to the cost of a college education. I said to one of our planners, Christine Parisi—who recently became a mom—that you could probably think of a college-saving program as a 22-year car payment, since saving for a newborn’s college education from birth is the equivalent of making 22 years of car payments, assuming the child enters college at age 18.

With this thought in mind, Christine crunched some numbers for her daughter Emily, who was born in December. She used cost of attending a private college today, approximately \$40,000 a year, as her baseline assumption. Christine also factored in a 6% rate of inflation (the historical average for college tuition inflation) and an 8% return on investments. She then repeated the calculation but with a \$20,000-a-year public college education as the alternate factor.

The table shows the results.

To meet the expense of a typical private college, one can make an initial investment of \$113,248, or one can make a monthly payment of \$872 for 22 years.

For a public college, the numbers are less daunting but still a challenge: a lump sum investment of \$56,624 at birth or monthly payments of \$436 per month for 22 years.

Then Christine decided to have some “fun” with our colleague Jeff. She ran the numbers for his three children—ages twelve, nine, and seven—for

both private and public schools. His monthly savings number for the next 14 years is \$1,894 for public college or \$3,789 for a private college. The poor fellow was understandably in a state of shock. “What’s a family with three children to do?” asked Jeff. “Hope? Hope for scholarships, I guess.”

Christine pointed out that, as car payments go, these numbers are in Porsche and Maserati territory. For many American families who have more than one child, these figures are perhaps out of reach.

Let’s not even consider graduate school payments.

### Helpful Strategy

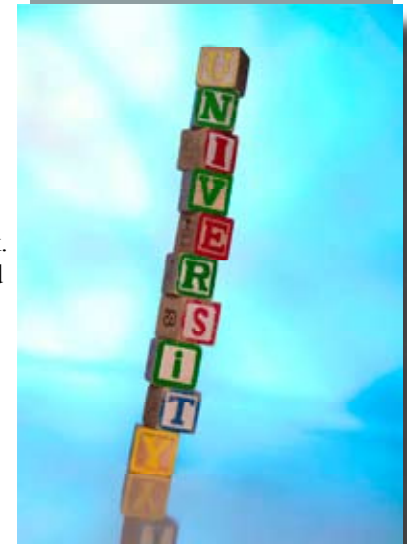
Coping with responsibilities of this magnitude requires serious long-term planning. The bottom line is that the sooner you start a focused savings program, the better off you’ll be—not only financially, but also in terms of your peace of mind.

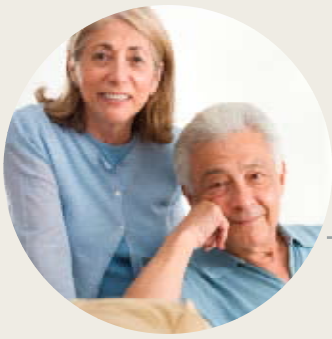
In addition to savings, we counsel our younger clients who are buying a home to take a 15-year mortgage rather than a conventional 30-year note. The idea is to have the mortgage paid off by the time the first child enters college. It also means equity in your home can be tapped for college funding.

If you implement a timely and realistically

College	Number Yrs.	Annual Tuition	Total Cost	Lump Sum Payment	Monthly Payments
Private	4	\$40,000	\$471,194	\$113,248	\$872
Public	4	\$20,000	\$235,597	\$56,624	\$436

structured tuition savings program, you might be pleasantly surprised when the time comes to send your future Nobel Prize winners to college. You’ll have assets accumulated, equity in your home, and maybe your little wizard will conjure up a scholarship or two.





# Planning and You

## We're All Going to Die Someday

By Kathleen Rehl, PhD, CFP®, Member, Alliance of Cambridge Advisors, [www.rehlmoney.com](http://www.rehlmoney.com)

**M**y soul mate and husband, Tom, died in February. Then my dear 84-year old mother passed one month later in March.

Although I miss their physical presence tremendously, their spirits and love will always be with me. I'm grateful for my faith in God, along with friends, family and clients who have offered their caring support.

Yes, managing grief at the death of a loved one is difficult. You may have experienced an intense heartache similar to mine.

I'm now in the process of settling two estates. That's pretty straightforward work, although it is time consuming. Tom and my mother did almost everything right in terms of their end-of-life planning...thanks in part to their astute financial advisor.

Think of it this way. Having all in order is the last gift you can give those you leave behind. It could also be called "tying up the loose ends of our lives." If left undone, incomplete estate plans may cause a lot of pain, guilt, sorrow, and regret for family members.

My husband's and my mother's IRAs and other retirement plan beneficiaries were identified correctly. Tom's and Mom's wills were current. Annuity and life insurance beneficiaries were up to date. Their non-retirement accounts were designated as "payable on death" or "transferable on death" status to avoid probate. Prior to their deaths, they both had updated their living wills so there was no question about their wishes when they were near to death.

Still, there are dozens of smaller and important decisions that I'm making now, especially with Mom's estate. She wanted everything

split equally among her three children, but what does that really mean in terms of the family mementos? My brothers and I amicably divided the sentimental items. We donated much of her household furnishings to help needy families through Lutheran Services of Florida. I ended up taking some things none of us really wanted, but that I couldn't bear to let leave the family (including a small well-worn green stool made by my great great grandfather for Mom when she was a little girl).

Here are loose ends you can tie up for the benefit of your relatives and friends:

- Check your beneficiary statements and make sure they are current and accurate.
- Revisit your will (often, this means finding it first!).
- Have your advanced health care directives in place, including a living will, along with a do-not-resuscitate order if you wish.
- Identify who gets which special keepsakes; be clear and specific.
- Decide what you want for your funeral or memorial service, and let your family.

One more thing. Tell people you love them — TODAY. Remember that you will die someday. We're all guaranteed to have that experience. Waiting until then will be too late to say I'm sorry and make up. Let the healing begin while you are still alive.

