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VOLUME 3

SEPTEMBER 2006

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# NAPFA

## *Planning Perspectives*



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## Visualizing the Big Picture In Your Finances and Your Life

For some people, the absence of numbers, tax strategies, and computations in this issue of *Planning Perspectives* will come as a relief, and for others it might be a disappointment. But the fact is that numbers are only one part of planning our financial futures—and often not the most important part.

Although people usually come to NAPFA members for help with their investments, the advisors often find that their clients have deeper motivations that they need to explore. Life-changing questions arise when advisor and client meet: When do you want to retire? What do you want to do when you retire? What is your hope for your children? Are you satisfied with your life?

Numbers can't answer those questions. They are matters of the head, the heart, and the soul. And yet, our dreams do not have any chance of becoming reality unless they are linked to a plan, a pathway that will lead us to our goals. That's where numbers become critical.

The articles in this issue of *Planning Perspectives* provide a window into how NAPFA members go beyond the numbers to work with clients to define what they want to achieve in their careers, their relationships, and their lives.

## NAPFA Draws Focus on Fiduciary Issues

For the past several months, NAPFA has been working with leading consumer organizations and members of the national and local media to bring to light a crucial flaw of many financial advisors: They are not fiduciaries.

Described simply, a fiduciary is a person who places the interests of his or her client at the forefront of every decision. Fiduciaries avoid conflicts of interest (such as commissions), and if a potential conflict does arise, it is disclosed clearly, completely and prior to any recommendation made to a client. NAPFA takes the fiduciary concept a step further by banning its members from accepting

commissions or other financial considerations from third parties, in exchange for financial recommendations.

We are gratified that our "Focus on Fiduciary" message has been overwhelming received so far. But there is a long way to go before this message will become common knowledge. We know from experience, as we began promoting Fee-Only Financial Planning back in 1980, and it took nearly two decades before the rest of the financial services industry caught up with us.

If you would like to learn more, go to [www.focusonfiduciary.com](http://www.focusonfiduciary.com).



# Investments

## Asset Location Joins Asset Allocation As Investment Necessity

By Warren F. McIntyre, [www.visionquestfinancial.com](http://www.visionquestfinancial.com)

Many investors are familiar with the concept of asset allocation as a way of diversifying a portfolio to protect it in various types of markets and economic conditions. But a new term, asset location, has emerged which should play an important part in the design of a portfolio.

Asset location refers to deciding which investments should be placed in taxable accounts, and which should be in tax-deferred accounts. Under the 2003 tax law, interest income and certain other investment income is taxed at ordinary rates, which can be as high as 35%, while capital gains are taxed at a maximum of 15%, and qualifying dividends are now just 15%. Even people in middle-income tax brackets might benefit from the preferential treatment for dividends and capital gains.

Since taxes reduce the net return that an investor receives, optimal location can make the portfolio more tax efficient and thereby boost after-tax investment return.

Previously, individual stocks and stock funds were most appropriate for tax-deferred accounts, while income-oriented investments went mainly in taxable accounts. There were several reasons for this, including the fact that income at retirement would normally come first from the taxable accounts. This would be the preferred approach if taxes were not a consideration, but the tax rate reductions for capital gains and dividends potentially change the equation today.

The tax law now suggests a shift of income investments, such as bonds, into retirement accounts to the extent practical. The taxable accounts should now have a greater growth emphasis, especially

for people who don't need much investment income. The overall asset allocation for an individual would not change; therefore, any shift of assets between types of accounts would necessitate a compensating adjustment in another account.

Some general rules for placement within accounts are as follows:

- High-return, highly tax-efficient assets should go in taxable accounts. These would include common stocks, stock index funds, and tax-managed stock funds.
- High-return, less tax-efficient assets, such as real estate and high-yield bond funds and many managed stock funds, would go into the IRA or employer retirement account.
- Low-return assets can go in either taxable or tax-deferred accounts. Thus, even though investments such as U. S. Treasury bonds and short-term bond funds are taxed at ordinary rates and are not very tax efficient, they provide a relatively low return so it doesn't matter too much where they are placed.

Despite the potential tax savings from optimal asset location, it's generally not a good idea to overload any one area. The future is uncertain, and tax laws seem to change with the political winds, so it's important to be flexible with your investment plan.

Of course, asset location does not apply to investors who either have all of their investments in tax-deferred accounts or all of their money in taxable accounts. But if you do have a choice, asset location should play a significant role in a tax-efficient portfolio.

### *Asset Location:*

Managing your investments for the optimum mix between taxable and tax-deferred accounts can help improve your long-term financial returns.



# Retirement Planning

## Retirement Projections and Sailing to Ireland

By Kathleen Rehl, [www.rehlmoney.com](http://www.rehlmoney.com)

I've come to understand that pre- and post-retirement planning forecasts—no matter how many bells and whistles the software has—are virtually useless after several years. There are simply too many variables involved: part-time retirement income, pensions, Social Security income, cash flow, tax rates, family dynamics, changes in a standard of living, investment returns for the previous year, inflation, and more. Even if you're off by just a little bit on a few of these factors, future projections can become significantly inaccurate.

Let's use a sailboat analogy that was shared with me by Mark Helm to illustrate the point.

Assume our goal is to travel to Ireland in 3 months from Boston, and we decide to use a sailboat. On the morning of our departure, we rig our boat. The weather on that specific travel day is mild—winds out of the northwest, calm seas, no storms predicted, and an ocean current pushing eastward. Our boat is in tip-top condition, and we have a good crew. With that information, we decide which direction to go, how many sails to use, and where to position the sails to get the kind of speed and direction we need to reach Ireland in 3 months.

Are we going to stay on that exact course and never touch the sails until we reach land? Of course not!

Things change every day—every minute, really, when you are at sea. Wind directions fluctuate, ocean currents vary, storms hit. Maybe we decide we want to reach Ireland in less time than

3 months, or possibly later. Maybe England or Spain looks like a better destination. What do we do if a hurricane is on the horizon one morning? What if our Global Positioning System device starts acting up? With such gorgeous sunsets, we might even fantasize about writing a book about our travels at sea. You get the idea—the possibilities are numerous, and course corrections are inevitable.

The same is true with retirement planning. We should expect to reevaluate a number of things every year. Retirement planning is a process, not just a one-time event.

Each year, I meet with my clients and look at cash flow needs so I can judge if the past year's living expenses are still appropriate for the future. Maybe an adjustment is needed, either up or down. I will look at how your investments have been doing, because if your investment portfolio has grown over the last year, perhaps you can save less even though your income needs are greater. Many other variables may alter your situation as well—tax law changes, a part-time job, moving to a more or less expensive location, receiving a bequest, a child who needs help, the purchase of a new car, etc.

Neither I nor any other financial advisor can give you an accurate long-term retirement plan that can be used without updates for the next decade or more.

Retirement sailing can be exciting. We just may need to trim the sails now and then, which is all part of the adventure.



**In retirement, change is unavoidable. The possibilities are numerous, and corrections are inevitable for smooth sailing.**



# Financial Planning

## Managing Your Most Valuable Asset: You

By Michael P. Haubrich, CFP®, [www.toyourwealth.com](http://www.toyourwealth.com)

What would you consider to be your most valuable asset? Typical things that come to mind may include your home, savings, and pension. Given the number of working years left before traditional retirement, your career should be listed among your most valuable assets.

Look at it this way, if you're in your mid-30s you've still got many years of working life remaining before traditional retirement. Even if you are in your early 50s, your career could represent more value than the total of all your current financial assets. Your career is the engine that drives your financial machine. It produces the income and provides you with the resources to invest, save, and build toward your retirement.

If you consider your "career asset" as the sum total of your time, plus talent, plus potential, it should be managed to maximize its long-term return, just as you would manage other assets. Your career asset return is made up of not only the current salary you are paid, but the satisfaction you receive by doing what really energizes you. That is much harder to quantify but no less of an important consideration in managing your career asset. By not balancing your work and life objectives you run the risk of suffering job burnout—reduced productivity, stress-related health issues, and a lessening number of work years prior to retirement.

So how do you manage your work-life balance to protect your career asset? In her book, *Work+Life*, author Cali Williams Yost, outlines a three-step process that continuously moves you

toward optimum balance. The process begins with introspection, then moves to planning, and finally generates action.

Step One challenges the way we think about work and life and dispels some of the common misconceptions we hold as fact, such as believing that only our workplace managers or human resources experts can resolve work-life conflicts. In fact, individuals willing to work through the process are the best-positioned to create ensure their long-term work-life satisfaction.

In Step Two, Yost identifies real or perceived roadblocks that can derail a person from achieving productive balance. Fear, resistance to change, and stuck-in-the-box thinking are factors that have the potential to prevent an individual from effectively managing his or her career asset.

After doing a lot of the self-work in the earlier steps, Step Three centers on creating the actual roadmap. It becomes a business project or case—with the goal of reaching the balance you need to be the most productive.

The outcome of achieving work-life balance doesn't mean that you have to leave your current job. Effectively managing it may ultimately mean changing jobs, but there are many options and alternatives to such a drastic step. Ultimately, if you take this path you can achieve the balance you need and allow you to work—and earn—with higher levels of satisfaction for a longer period of time.



**Your career should be listed among your most valuable assets.**

*This article first appeared in the Racine (Wisconsin) Journal Times in June 2005.*



# Financial Planning

## Preuptial Agreements Can Bring Out the Best

By Morris Armstrong, CFP®, ChFC, CDEA, [www.armstrong-financial.com](http://www.armstrong-financial.com)

As a financial planner and divorce planner, as well as someone who has been through a divorce, I understand how couples may feel when contemplating the use of prenuptial agreements. To many people, a partner's inquiry about a prenuptial agreement signals that one party thinks that the marriage is going to fail, a lack of commitment.

I don't view prenuptial agreements in this way. I see them as planning in advance for some of the money issues that typically arise in a marriage and especially in a divorce. It's much better to have a legal document, signed before the marriage, which addresses issues such as maintenance, child support, and division of assets than to start discussing those matters when the divorce is occurring.

Couples should communicate how they feel about spending, saving, and giving things away. Discussing a prenuptial agreement may give insight into how both parties feel about money issues and foster greater understanding that will strengthen a marriage. Note that I used the term "money issues," which is different and greater than "money."

Among the obvious candidates for prenuptial agreements are couples in which one spouse is substantially wealthier than the other. Wealth can be family money, a business, property, or securities. The couple may agree prior to marriage that the less wealthy spouse cannot make a claim on these assets in the event of a divorce, or that the claim will be for a limited percentage.

One bride who sought my advice was bringing approximately \$15,000 more into the marriage than the groom. The money was going toward

the purchase of a home. The bride was a bit concerned that she would lose the money if the marriage ended. The reality is that even if the couple's property were split 50/50, she would lose just \$7,500. The couple did not require a prenuptial agreement, but it was beneficial for them to discuss how they felt about money.

In another situation, a business owner asked me whether he should suggest a prenuptial agreement that would exclude any claim on his business or create a threshold value. I suggested that he consult an attorney since that seemed to be a valid concern.

A prenuptial agreement is legal and enforceable, but that does not guarantee that a judge will accept and enforce all of it. The key words in the preceding sentence were "legal" and "enforceable," so do yourself a favor and consult with an attorney who practices family law. Don't draft something yourself and assume it will be valid. Remember, you aren't drafting the prenuptial agreement to protect a few dollars, but in all likelihood, to protect things which are very important to you. Wouldn't you feel like an idiot if you learned that all your efforts were for naught because you missed some technicality or used the wrong language?

Common errors which may invalidate the entire agreement include: not disclosing all assets with correct values; signing the document too near the wedding date, which may provide the excuse that it was signed under duress; or a lack of independent counsel for both parties.

Again, this is not a do-it-yourself project. What you read here, or anywhere online, may not be applicable to your state; please consult a qualified attorney.

Sources for more information about prenuptial agreements include:

DivorceNet online:  
[www.divorcenet.com](http://www.divorcenet.com)

Bankrate.com online:  
[www.bankrate.com/brm/prenup.asp](http://www.bankrate.com/brm/prenup.asp)



# Financial Planning

## Money Grounded-ness

By Paul Lemon, [www.tenweeks.com](http://www.tenweeks.com)

You don't have to be an electrical contractor to know how important a ground wire is in establishing an electrical circuit. You can have all the power in the world, but without a ground wire to complete the circuit that energy will be confined to the power source, unable to energize countless applications.

Most of us have experienced this when we are completely present in the moment. We feel a powerful flow of energy in our bodies. It's like we have momentarily "plugged in" to some source of power that transforms our existence. Could it be that being "grounded" to what is happening right here and now is key to finding happiness and contentment?

I like the way that Robert Johnson describes contentment in his book, *Contentment - A Way to True Happiness*:

"Contentment gives you a different experience of time; your mind stops wandering into the past or the future...it grows out of a willingness to surrender preconceived ideas and affirm reality as it is."

In our culture, money is perceived as the key to unlocking the "good life" and proving that we are "important." Over the 30 years I have spent as a tax and financial advisor, my own experience (and that of my clients) around money has been that there is very little contentment and happiness with money. Discontent, or "money suffering," seems to prevail—regardless of financial net worth. We live with an underlying message that "more" will fix our money suffering—and it's just over the "top of the next hill."

Having my eyes opened to the powerful impact of money in our culture to shape our lives, I've tried to explore the lessons that are available to those who would be present or "grounded" with their money. I've seen the power of such grounded-ness as clients have courageously looked at what money and their relationship to it was revealing about the reality of their lives. In almost every other area I can deceive myself, but a close look at my finances helps uncover my deepest fears and actual priorities.

What do I mean?

I may say how concerned I am about the environment, but does my budget commit to a reduction in gasoline purchases? If I expound the benefits of reduced work in creating opportunities for awareness and meaningful living but make no allowance for reduced expenses to allow for that reduction in income, then my actual money management reveals what my true values are at this moment in my life. Such a realization ushers in a new consciousness which is much more helpful than all my "good" or "bad" self-judgments.

I believe that in our culture, accepting our propensity to ask money to make us safe, happy, and secure is a key to staying grounded. Rather than asking money to do these things—which it can not, I can begin to see it as a tool that helps me pay attention to the journey of living day-to-day more in alignment with my true values and accessing my greatest asset—my soulful adaptability.

Consider these questions that illustrate "money grounded-ness":

- **Income** – What payback do I get from working so hard and always being stressed? What is it about my identification with my career that keeps me from cutting back?
- **Budgeting** – Could a simpler life be more fulfilling than mindless consumption? What fears do I feel when I say "no" to a craving?
- **Investing** – Does it matter what the companies that I invest in do to make a profit? Does the end justify the means?
- **Philanthropy** – Do I share a meaningful portion of my abundance, knowing that I have determined what amount of money is "enough"?

May we each unlock the power of this money mirror to see when we "short-circuit" and return to asking money to do what it cannot. With grounding, we can restore this flow of energy and awareness and experience the rich and meaningful lives we all desire.

**Money is a tool that helps me pay attention to the journey of living day-to-day more in alignment with my true values.**