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# Celebrate Financial Independence

By Louis E. Conrad II, CFA

- Some individuals are resistant to hiring a professional to manage their portfolio and oversee their financial planning needs, including retirement planning and education funding.
- However, a competent financial advisor can assist you in meeting your financial goals by establishing a prudent path and ensuring you don't stray from it.

With Independence Day upon us, you may want to celebrate your own independence from overseeing your investment portfolio and financial planning needs by hiring a professional. Too often I meet with prospective clients who have worked hard to save money, but who have not worked with a competent financial advisor to the detriment of their investment portfolio and financial planning needs. You may have the best of intentions, but a lack of knowledge, discipline, and time can work against you and place your financial goals at risk. Just as you visit a dentist for dental work, you may want to consider hiring a financial advisor to assist you in meeting life's critical financial goals.

This article answers questions often posed by those who are considering the services of a financial advisor, financial planner, or wealth manager. Here we use the generic term financial advisor to refer to any of the above who offer investment and financial planning-related services.

1. What are the benefits to working with a financial advisor?

The benefits can vary depending on you and the financial advisor, but generally speaking, a financial advisor offers in-depth knowledge of the subject matter involved and keeps abreast of the best practices in the investment and financial planning realms. This knowledge base, combined with a keen sense of judgment, is a critical factor in providing you with competent advice. In addition, advisors subscribe to numerous, complex software products that can enhance the level of advice and service you receive as a client. An advisor's disciplined approach is also important to avoid the emotional decisions too often made by individuals who lack objectivity.

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## More about COMPASS Wealth Management, LLC

COMPASS Wealth Management, LLC is a client-focused wealth management firm dedicated to providing superior advice to individuals, families, and corporate retirement plans.

Our wealth management services include investment management, retirement and gift planning, education funding, and other advisory services.

We take pride in offering you expert financial advice along with personalized service. Assisting you in reaching your financial goals is our business and we take that responsibility very seriously.

For details on the selection criteria used to determine the recipients of the FIVE STAR Wealth Manager award, please visit our web site.

# Celebrate Financial Independence, continued

A good financial advisor should be able to evaluate your situation and offer you various options to meet your financial objectives. Ultimately, you benefit from the creation of a plan that is designed to meet your financial goals and which acts as a benchmark to evaluate the progress toward your goals.

Perhaps more importantly, hiring a financial advisor can remove one burden from your life and allow you to spend your time pursuing your career, spending time with your family, or enjoying other activities to enhance your life.

2. What services are typically offered?

Though most financial advisors focus their efforts on managing investment portfolios, many advisors also offer a range of financial planning services. Professional management of your investment portfolio usually involves establishing a structure, or an asset allocation and diversification plan, that is based on the risk that you are willing to undertake for your portfolio. This structure is designed to provide discipline to the investment process and avoid the emotional decisions as mentioned above that lead to subpar investment returns.

Advisors may also offer financial planning services, such as retirement planning, education funding, gifting strategies, and stock option planning. Depending on the focus and size of the firm, it may also offer estate planning, tax planning, and insurance, or offer to refer you to competent professionals in these fields.

Two of the most often pursued financial planning services are retirement planning and education funding. Retirement planning attempts to answer two general questions: before retirement, how much money do you need to save to ensure sufficient assets for the balance of your life, and during retirement, how much money can you afford to spend without depleting your assets? Education funding involves determining the most appropriate type of investment account, as well as how much in savings is likely to be needed for the projected educational costs.

3. How much does it cost?

The cost for financial advisory services depends on the financial advisor's business model and compensation scheme. Generally, there are two different business models and two different compensation schemes. A financial advisor comes in two flavors: (1) one who has a legal, fiduciary responsibility to act in their clients' best interests or (2) a broker, whose standard of care is one of suitability, or offering products that are deemed to be suitable for the given client's situation. The first type of advisor tends to "fee-only" and may be more advice oriented. Fee-only compensation is based on either an hourly rate, a fixed fee, or a percentage of investment assets overseen. The typical percentage charged is 1% annually, though greater investment balances are charged a lower rate. A broker, the second type of advisor, receives commissions based on sales of financial products.

Most financial advisors have minimum investment asset requirements, which usually begin at $250,000, but may be as high as $2 million or more, depending on the firm.

You should be aware that an advisor's fee may be a deductible expense on your federal income tax return. Further, if your financial advisor invests your assets in mutual funds, they may also have access to institutional versions of many common mutual funds that can save you 0.25% - 0.40% in annual mutual fund costs.

So consider celebrating financial independence by hiring a professional to oversee your investments and financial planning needs. It may also free up your time to enjoy summer days like these.

# Required Minimum Distribution (RMD) Tips and Traps

- RMDs are a necessary evil for holders of tax-deferred retirement accounts.
- RMDs require a certain portion of your retirement balance to be withdrawn each year, depending on your age.

The tax-deferred compounding you get via an IRA or a company retirement plan enables you to grow your savings without having to fork over taxes on your investment earnings year in and year out. However, at some point, required minimum distributions, or RMDs, will take effect. All retirees must begin taking RMDs from their tax-deferred retirement plans by April 1st of the year following the year in which they turn age 70 1/2. They must then continue to take distributions by December 31st of each year thereafter. Roth IRAs aren't subject to RMDs. However, you exert more control than you might think over the timing of your RMDs, as well as over which accounts you tap. Here are some tips for getting the most out of your RMDs, as well as some traps to avoid.

Do

1. Even though you must calculate your RMD amounts for each of your traditional IRAs, you can draw your RMD from the investment that's most advantageous for you. If you've assessed your asset allocation and determined it's time to rebalance, take your RMD from the IRAs that hold assets where you need to lighten up.

2. Rather than taking your whole distribution at year-end, consider spacing your distributions throughout the calendar year to obtain a range of sale prices for your longer-term assets.

3. Consider "bucketing" your IRA and retirement-plan assets. That means dividing assets into cash or cash-like accounts to help address RMD and other income needs, intermediate-term assets (such as bonds) that are next in line for distributions, and long-term assets.

4. Put your distributions on autopilot to avoid the last-minute rush to execute trades (or worse, to avoid missing the deadline altogether). If you go the autopilot route, be sure to maintain cash assets in your accounts to avoid having your fund company or brokerage firm sell a long-term asset that you would have preferred to hold.

5. Coach elderly parents on taking their RMDs.

Don't

1. Miss the deadline. You'll owe a tax penalty equal to 50% of the distribution amount you should have taken but didn't, as well as the taxes that are due on any retirement-plan distribution.

2. Pay a tax penalty without stating your case first. The IRS' website indicates that the penalty will be waived if "the shortfall in distributions was due to reasonable error and that reasonable steps are being taken to remedy the shortfall." If you've missed a distribution or didn't take as much of an RMD as you should have, you'll need to fill out an IRS form. You'll also have to submit a letter detailing why you had a shortfall in your distribution and what you're doing to remedy it.

3. Spend your RMDs right away unless you've analyzed your retirement plan's viability and determined that you can afford to splurge.

4. Plow the proceeds into a Roth IRA without doing your homework first. You need to have enough earned income (generally, that means income from a job) to cover the amount of your IRA contribution. For example, if you want to contribute $6,000 to a Roth, you'd need to have at least $6,000 in earned income to do so. Unfortunately, income drawn from your retirement accounts doesn't count. Note that you can't make additional traditional IRA contributions after age 70 1/2.

Funds in a traditional IRA grow tax-deferred and are taxed at ordinary income tax rates when withdrawn. Contributions to a Roth IRA are not tax-deductible, but funds grow tax free, and can be withdrawn tax free if assets are held for five years. A 10% federal tax penalty may apply for withdrawals prior to age 59 1/2. Please consult with a financial or tax professional for advice specific to your situation.

# Know Your Risks

- Risk can be defined in many ways. This short article reviews some of the risks investors face.
- Life is full of risks--investments are no different. However, some investment risks can be mitigated with proper investment management.

Risk is the chance that you won't be able to meet your financial goals or that you'll have to recalibrate your goals because your investment comes up short. Investors face many forms of risk depending on the kinds of investments they choose.

Market, industry, and company risk: General market fluctuations can affect securities trading in that market. Stocks tend to fluctuate more than other asset classes, and may pose more risk over short periods of time. Investors looking to time the market run the risk of jumping into the market during the worst times, and out of the market during the best times. Security values can also decline from negative developments within an industry or company.

Credit and interest-rate risk: Credit risk is the possibility of a bond issuer not being able to make timely payments of principal and interest. The value of a bond may also decrease due to financial difficulties or the declining creditworthiness of the issuer. Interest -rate risk relates to how bonds tend to rise in value when interest rates fall, and to fall in value when interest rates rise. Typically, bonds with longer maturity exhibit greater price volatility.

Inflation risk: Inflation is a rise in the general level of prices for goods and services. If investments do not keep up with inflation, an investor's money will purchase less in the future than it did in the past.

Liquidity risk: Some investments may not be widely held by the public and may be difficult to sell if prices drop dramatically.

Currency risk: Returns achieved by local investors are often different from returns achieved by U.S. investors because of foreign exchange rates, even though both are investing in the same security.



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