



ILLINOIS STATE  
BAR ASSOCIATION

# The Counselor

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## Editor's notes

We are about to rectify an area of neglect. The Section Council is known as Business Advice and Financial Planning. It is the "Financial Planning" aspect that has long been neglected and members of the Section Council have asked more than once when we will have some articles on the topic of "Financial Planning."

Most of the Section Council members lack the expertise to author articles on financial planning, so we practically scoured the State of Illinois writing to financial planners to determine if they would prepare articles for publication in this newsletter. Those who volunteered all responded via e-mail, which is unique in itself, because all of them received old-fashioned letters.

The articles written by the financial planners (1) lack the "legalese" often found in this newsletter, and (2) cover a multitude of topics. For the most part, the financial planners as authors were given free reign to write on any financial planning topic they desired, although several of the Section Council members have been critical of annuities, and the financial planners were requested to devote a portion of their article to annuities. Some did and some didn't, which was acceptable to the editor.

Depending upon the success and reception of this edition of the newsletter, we may ask different financial planners to write a "guest column" or "guest editorial" for insertion in the upcoming newsletter editions.

We encourage our readers to advise us if they desire more articles pertaining to annuities, which have become one of the hottest investment products. Sales of variable annuities have more than doubled in the last several years to more than \$100 billion. We also encourage our readers to inform us if there is any type of specialized topic they would like more information and knowledge of and we will attempt to find authors for that subject matter. Please address all comments to:

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## The financial planner

By Cindy Menker

"To the Rescue," an article published in the February 2003 edition of *Smart Money Magazine*, notes that there are approximately 650,000 in the financial planning field workforce. Many think that all financial planners are certified; this is not true. Anyone can call himself a financial planner. However, only those who have fulfilled the certification and renewal requirements of the Certified Financial Planner ("CFP") Board can use the CFP certification marks. Presently, over 41,000 worldwide have earned the right to use the CFP marks.

### Certification requirements

There are four requirements to receiving the CFP certification:

- **Education:** Extensive financial planning knowledge is gained by completing a comprehensive course of study at a college offering financial planning curriculum approved by the CFP Board. Areas of study include insurance, estate, retirement and benefit plans, income tax and investments. Others can opt out of taking the coursework by demonstrating previous financial planning-related coursework or showing the attainment of certain professional designations, such as a CPA or JD.
- **Examination:** CFP professionals must pass a comprehensive two-day, 10-hour CFP certification examination given three times a year. The multiple-choice examination covers the areas mentioned in the previous paragraph. Approximately half of the test takers pass the exam.
- **Experience:** CFP practitioners must have a minimum of three years experience in the financial planning field prior to completing the work requirement.
- **Ethics:** CFP professionals must agree to abide by a strict code of professional conduct. The CFP Board performs a background check on each applicant. Any investiga-

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tions or legal proceedings related to his or her professional conduct must be disclosed.

Once certified, the CFP practitioner is required to complete a minimum of 30 hours of continuing education every two years to stay current with recent developments in the financial planning practice. Certain organizations will require more hours. For example, as a member of the National Association of Personal Financial Advisors (NAPFA), I am required to complete a minimum of 60 hours of continuing education every two years.

## The financial planning process

Financial planners are often considered strictly investment advisors. While investment review is important, this is only one part of the financial planning process. A family with two young children comes to a financial planner seeking investment advice. It is our role to ask additional questions. Is life insurance adequate? Are wills up-to-date if both parents die suddenly? Are any unusual expenses, such as a new car or a house addition anticipated that would require a greater cash reserve? A financial planner should spend the time getting to know his client. To simply invest the family's money without delving deeper does a disservice to the client.

## Methods of compensation

Not all financial planners are compensated the same for their services. Many are remunerated through commissions. For example, a client comes to a financial planner for investment advice. After interviewing the client, determining his or her goals, time horizon, and risk tolerance, it is determined that the client should purchase \$20,000 of XYZ mutual fund and \$20,000 of ABC mutual fund to properly diversify his portfolio. The back-end and front-end loads on these mutual funds generate commission revenue for financial advisors. In this example, if a mutual fund has a five percent front-end load, the commission is \$2,000 and the remaining \$38,000 is invested in the two mutual funds. A financial planner might also earn commissions through the sale of insurance or annuities depending on the securities licenses he carries.

The other end of the spectrum is the fee-only financial planner. Normally the planner will have a Series 65 securities license. Fee-only planners do not receive commissions. Rather, the client with the \$40,000 to invest would pay the planner in one of several ways. The planner could choose to charge a percentage of assets under management. While one percent of assets under management is common, a planner may have a sliding scale with the percentage declining as the assets increase. The percentage may range from .5 percent to two percent.

Others prefer to charge an hourly rate. Hourly rates can be advantageous to those starting out since some planners will not work with a client below a certain minimum.

Looking at the Web sites of financial planners in the Chicagoland area, it is not unusual to see a range of \$100 to \$200 hourly. With current market conditions, some planners have switched to charging a flat fee or a percentage based on total net worth. To further complicate matters, others charge a combination of commissions and fee-only!

Our firm has chosen the route of fee-only. Currently a straight one percent of assets under management is charged. Our hourly rate for financial planning advice is \$100. It is our philosophy that fee-only is in the best interest of the client and eliminates potential conflicts of interest with the client. No additional compensation is received whether a \$100,000 or \$1 million life insurance policy is recommended. The coverage is determined strictly based on the client's needs and potential income streams. Members of NAPFA, of which we are one, are not permitted to receive any commissions to avoid the appearance of a conflict of interest.

## Types of investments

Besides different methods of compensation, fee-only planners frequently have a different philosophy regarding certain investments. Consider the suitability of annuities for an individual. A commission-based financial planner might emphasize the advantages of annuities. It grows tax-free. There is no limit as to the amount of money placed into this tax shelter. This investment vehicle can provide protection of the original investment for the beneficiary through a death benefit guarantee.

A fee-only planner rarely recommends a variable annuity. First, there is the cost. The administrative and mortality risk fee can total one percent to two percent of assets. This does not include the cost of managing the sub-account fees that can range from .15 percent to 1.5 percent of assets. Coupled with the charges if the policy is surrendered early, a variable annuity can be a very expensive product. Another disadvantage is that all capital gains earned in the variable annuity are eventually taxed as ordinary income. For a high tax bracket individual with capital gains, this can result in a significant tax bill.

Are annuities ever appropriate? The answer is yes. Many high-income individuals have contributed fully to their retirement plans. Annuities offer a way to defer taxes for many years. The cost of an annuity is very high, however. For most people, holding a basket of individual stocks or tax-efficient funds is a better option. The yields on fixed annuities also are attractive to many investors as the stock market continues to struggle. The downside of a fixed annuity is when interest rates rise; the yield is diminished by the inflation.

How does a consumer locate a financial planner? Obviously, a referral from a family member or friend is the best source. In addition, the Financial Planning Association has a planner search on its Web site, <[www.fpanet.org](http://www.fpanet.org)>. For individuals interested strictly in fee-only services, <[www.napfa.org](http://www.napfa.org)> will show all planners accepting new clients within the specified state.

Once you select two or three planners to interview, develop a list of questions. Will the financial planner provide a complimentary initial consultation? Are you comfortable with their investment philosophy? Will they bill you every time you phone to ask a question? Request references from the planner. At the first meeting, the finan-



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cial planner should provide the potential client with an ADV, a document that is filed with regulators. This form offers information regarding the planner, his background and compensation. It is also recommended to visit <[www.CFP-board.org](http://www.CFP-board.org)> to check whether the planner has violated the board's strict ethic requirements. Once the planning process is completed, plan on meeting once or twice a year to update the planner on any changes that can affect your financial future.

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Cindy Menker is President of Contour Financial, a fee-only firm located in Orland Park. She is a CFP<sup>TM</sup> certificant, CPA and MBA. She works with another financial planner and financial analyst. She is a member of the Financial Planning Association, American Institute of Certified Public Accountants and the National Association of Personal Financial Advisors. For more information, visit their Web site at <[www.ContourFinancial.com](http://www.ContourFinancial.com)>.