Financial Planning

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Delia Fernandez, MBA, CFP®
Delia Fernandez, MBA, CFP®
Fernandez Financial Advisory, LLC
5212 Katella Avenue, Suite 205
Los Alamitos, CA 90720
562-594-4454
delia@fernandezllc.com
Today’s topics

- Risk management/insurance
- Tax planning
- Investment planning
- Retirement planning
- Estate planning
- 529 plans for education
Risk management

Obtain objective advice to be sure you have proper types and coverage

- Health insurance
- Homeowner’s, auto, and personal liability insurance
- Long-term care insurance
- Life insurance
Risk management - the Umbrella concept

Additional liability coverage

- $1 million increments

- Auto
  - 250k/500k

- Uninsured motorist
  - 250k/500k

- Homeowners
  - Residence: $300,000
  - Liability: $500,000

$1 million increments
Risk management – life insurance

- Who needs it?
- How much is enough?
- Review old policies periodically
Risk management – life insurance

- Still working? Need to replace wages
- Dependents? May need even more
- Term vs. cash value insurance
- Life insurance as an estate planning tool
Tax planning

Financial strategies are based on your tax profile

- Deductions
  - Standard deduction or itemize?
- What’s your tax bracket?
- Taxable income
Retirement planning

- How much will you have?
- How much will you need?
- Calculate impact of additional savings
- What is the impact of taxes and inflation?
- How much can you spend?
- How should you invest to meet your goal?
- Social Security and Medicare
Retirement planning – retirement income resources

- Social Security
- Employer retirement plans
- Other savings
  - Spouse/partner retirement plans
  - Plans from former employers
  - IRAs
  - Regular investment accounts
  - Inheritance?
Nest egg needed to sustain various spending levels

<table>
<thead>
<tr>
<th>Annual pre-tax expenses</th>
<th>ROR 2%</th>
<th>ROR 5%</th>
<th>ROR 8%</th>
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<tbody>
<tr>
<td>$100,000</td>
<td>$3.5 million</td>
<td>$2.3 million</td>
<td>$1.6 million</td>
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<tr>
<td>$150,000</td>
<td>$5.2 million</td>
<td>$3.5 million</td>
<td>$2.5 million</td>
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<tr>
<td>$200,000</td>
<td>$6.9 million</td>
<td>$4.6 million</td>
<td>$3.3 million</td>
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</table>

3% inflation 30 year retirement
Retirement planning – 401(k) contributions

- 2021 contribution maximum $19,500
- 2021 over-50 catch up $6,500
- The best way to save for retirement – you get an immediate return because of the tax break!
Retirement planning – Social Security

- Based on “quarters” of coverage
- Amount is based on how much you earned while working
- Annual benefits increase with inflation
- Reduced amount for benefits prior to “normal retirement age”
- Increased amount for delaying benefits past normal retirement age
## Retirement planning – Social Security

- Social Security – Normal Retirement Age (NRA)

<table>
<thead>
<tr>
<th>Birth Year</th>
<th>NRA</th>
<th>Birth Year</th>
<th>NRA</th>
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</thead>
<tbody>
<tr>
<td>Before 1938</td>
<td>65</td>
<td>1955</td>
<td>66 2 mos</td>
</tr>
<tr>
<td>1938</td>
<td>65 2 mos</td>
<td>1956</td>
<td>66 4 mos</td>
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<tr>
<td>1939</td>
<td>65 4 mos</td>
<td>1957</td>
<td>66 6 mos</td>
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<tr>
<td>1940</td>
<td>65 6 mos</td>
<td>1958</td>
<td>66 8 mos</td>
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<tr>
<td>1941</td>
<td>65 8 mos</td>
<td>1959</td>
<td>66 10 mos</td>
</tr>
<tr>
<td>1942</td>
<td>65 10 mos</td>
<td>After 1959</td>
<td>67</td>
</tr>
<tr>
<td>1943-1954</td>
<td>66</td>
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</table>
Retirement planning – Social Security

Maximum monthly benefit
For someone retiring in 2021, based on a typical retiree who has paid into the Social Security system over his or her entire career.

Age 62  $2,324
At FRA   $3,113
Age 70  $3,895
Retirement planning – taxation of retirement benefits

- Pre-tax retirement contributions decrease taxable income now
- Earnings grow tax-deferred
- You pay taxes when you receive the benefit
- CA does not tax Social Security
- In taxable accounts, CA muni bonds (usually) tax-free both Federal and CA income tax
Investment planning – identify issues and problems

- What is your investment philosophy?
- Investment portfolio not diversified?
- Investment losses, but still a tax liability?
- How to benchmark performance?
- Trouble keeping track?
Investment planning – basic asset classes

- Cash & Equivalents
- Bonds
- Stocks
- Alternatives
Investment planning – Cash and Equivalents

- What are they?
  - Deposits with a bank or financial institution
  - Contracts with an insurance company
  - U.S. Treasury securities
  - Also referred to as stable value investments

- What risks do they have?
  - Inflation risk – are they outpacing inflation?
Investment planning – Bonds

- What are they?
  - Loans made to a company or the government that may have a fixed rate of return
  - Can be short, intermediate or long-term bonds

- What risks do they have?
  - Inflation risk
  - Interest-rate risk
  - Market risk
  - Company performance risk
Investment planning – Stocks

- What are they?
  - Units of equity ownership in a company

- What risks do they have?
  - Purchasing power or inflation risk
  - Principal risk
  - Market risk
  - Company performance risk
Investment planning – “Alternatives”

- Non-correlated Assets (reduce volatility of overall portfolio)
  - Commodities
  - Hard assets
  - Hedge funds
  - Real estate
  - Venture capital
  - Private equity
Investment planning – stocks, ETFs & mutual funds

- Individual stocks – Disney, Apple, etc.
- Exchange-traded funds – a security that trades like a stock on an exchange, and tracks a stock index, a commodity, bonds or a basket of investments
- Mutual funds – a managed portfolio of investments that pools investors’ money to purchase a collection of stocks, bonds or other investments
“Active” and “Passive” Investing

- Active – ongoing buying and selling of investments
  - May involve higher costs (trading costs, management fees, capital gains)
  - May not perform better than an index of the same category of investments

- Passive – buy and hold, typically using index funds
  - “If you can’t beat the market, buy the market”
  - Usually lower-cost alternative, more tax-efficient
Investment planning – diversifying stocks

- Domestic vs. International funds
- Growth vs. Value Funds
  - Growth: high price/earnings ratio
  - Value: low price/earnings ratio
- Small Cap vs. Large Cap Funds
  - Market capitalization – number of shares outstanding multiplied by share price
    - Small Cap: generally less than $5 billion
    - Mid Cap: generally between $5 - $10 billion
    - Large Cap: generally more than $10 billion
Investment planning – asset allocation process

- 1st step: determine asset classes to be used
- 2nd step: make a pie!
- 3rd step: implement, rebalance periodically, and evaluate performance
Past performance is no guarantee of future results. Risk and return are measured by standard deviation and arithmetic mean, respectively. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. © Morningstar. All Rights Reserved.
Asset allocation

Moderate Growth Portfolio

- US large cap stocks: 30%
- US core bonds: 33%
- US mid cap stocks: 9%
- Emerging market corporate bonds: 7%
- Emerging market stocks: 8%
- International developed stocks: 7%
- US small cap stocks: 6%
Past performance is no guarantee of future results. Risk and return are measured by standard deviation and compound annual return, respectively. They are based on annual data over the period 1970–2018. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. © Morningstar. All Rights Reserved.
Ibbotson® SBBI®

Stocks, bonds, bills, and inflation 1926–2018

Past performance is no guarantee of future results. Hypothetical value of $1 invested at the beginning of 1926. Assumes reinvestment of income and no transaction costs or taxes. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. © Morningstar. All Rights Reserved.
Investment planning – annuities

- What are they?
- Do they make sense?
- If you have one
  - Should you get out? How?
  - Should you annuitize?
Investment planning – income tax consequences

- Always look at *total return*
- Not everyone should own muni bonds
- Beware of mutual fund distributions
- Investment location
- Beware of annuities: they may be the most tax *inefficient* investment
Taxes Significantly Reduce Returns
1926–2018

Past performance is no guarantee of future results. This is for illustrative purposes only and not indicative of any investment. An investment cannot be made directly in an index. © Morningstar. All Rights Reserved.
Capital gains and qualified dividends

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<tr>
<th></th>
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<th>15%</th>
<th>20%</th>
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<tr>
<td><strong>Married Filed Jointly</strong></td>
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<tr>
<td>Cap Gains S-T&lt;12mos.</td>
<td>$0-$78,750</td>
<td>$78,751-$488,850</td>
<td>&gt;$488,850</td>
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<tr>
<td>Cap Gains L-T&gt;12mos &amp; Qualified Dividends:</td>
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<tr>
<td>Single</td>
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<td>Cap Gains S-T&lt;12mos.</td>
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<td>$39,376-$434,550</td>
<td>&gt;$434,550</td>
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<tr>
<td>Estate &amp; Trusts</td>
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<tr>
<td>Cap Gains S-T&lt;12mos.</td>
<td>$0-$2,650</td>
<td>$2,651-$12,950</td>
<td>&gt;$12,950</td>
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<tr>
<td>Cap Gains L-T&gt;12mos &amp; Qualified Dividends:</td>
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<td>20%</td>
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Estate planning

- Durable power of attorney for finance
- Advanced health care directive
- Will(s) for both of you
- Living trusts
- Letter of instruction
Estate planning – identify issues and problems

- Beneficiary designations on accounts
  - Be sure they’re up-to-date
  - Naming a trust vs. naming a person
  - Remember that named beneficiaries take priority over those named in a will!
- Joint accounts – gift issues
Education planning

- 529 Savings Plans (now also for private K-12)
  - Individual funds
  - Age-based and risk-based funds
  - Tax-free withdrawals for qualified expenses
  - Contribution limit $475,000 for CA
  - Small initial investment – as low as $25

www.savingforcollege.com
529 ABLE accounts

- Tax-advantaged savings accounts for individuals with disabilities, beneficiary not taxed on earnings in account
- Onset of disability before age 26
- Total annual contributions for a single tax year is $15,000
- SSI exempts the first $100,000 from the SSI $2,000 individual resource limit
- Can transfer up to $15,000/yr from a regular 529 plan to a 529 ABLE account


http://www.ablenrc.org/about/what-are-able-accounts
Financial planners

- Overview
  - Independent vs. associated with a brokerage firm
  - Compensation method
    - Commission
    - Fee plus commission
    - Fee-offset
    - Fee-based
    - Fee-only
Financial planners

- Credentials
  - Registered investment advisors
  - Certified financial planner (CFP)
  - Chartered Financial Consultant (ChFC)
  - Chartered Financial Analyst (CFA)

- Experience

- Rapport/trust
For more information

- Financial Planning Association (FPA)
  - www.fpaocc.org

- National Association of Personal Financial Advisors (NAPFA). Fee-only planners
  - www.napfa.org
  - 888-Fee-Only or 1-888-333-6659