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MAY 2007
VOLUME 16, NO. 2

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How Will You Handle the Next Market Correction?

Now that the Dow has hit a record 13,000, it's party time. Investors are making money in many sectors, corporate earnings are strong, the economy is doing well, and interest rates are relatively low. Although the fundamentals look good at this time, we will have a market correction, but don't ask us when or for how long. No one knows. So this is a good time to rationally think about your reactions when this party ends—especially if the markets don't quickly rebound like they did after the February correction. With the speed of today's global markets, it's too late when emotions and the media frenzy cloud your thinking.

Here are some points to consider.

1. **Market timing does not work.** If anything, the February market drop and its rapid recovery show that. Nobody anticipated how quickly the market would rebound. For several months leading up to the February sell off, a lot of "I-told-you-so's" predicted a correction, but none of them knew when, how much, and how long it would last. Numerous studies have shown that market timers need to be right at least 70% of the time, both going out of and back into the stock market to come out ahead. No one is consistently that good.
2. **When will you need your money and why have you invested it?** This is still the most important question to ask before making major investment moves. If you need some of it within the next year or two, put it somewhere more stable. If you need it for retirement, you may want to keep a large portion of your retirement assets in the equity markets.
3. **Where will you put it?** Your money has to be employed somewhere. It was an easy decision in 1987, 1990, and 1994 when interest rates were much higher than today. If you can't find anything better, don't move.
4. **How will you get out of the market and what will be your triggers?** The Internet traders and individual investors discovered that they couldn't get out and back in as easily as the huge institutional investors, and even they weren't all that nimble. By the time you are ready to take action, it may be too late.
5. **How will you get back in?** This is one of the most difficult decisions to make. We have observed over the years that those who get out of the market are often more reluctant to move back in when stock prices are at a bargain. By the time they see things finally looking better, they may have missed a significant amount of appreciation. They would have been better off never investing in the first place.
6. **Are you confusing volatility with value?** There are other kinds of risk to consider, which we have written about before. Losing purchasing power is a real one. A temporary market loss on a portfolio may not be a permanent loss until you sell. But purchasing power loss is forever. One of the benefits of financial assets such as stocks and bonds is that they are relatively liquid. The price you pay for this convenience is volatility. Unlike real estate, they are constantly priced by willing buyers and sellers every minute of the trading day.
7. **Does a market correction matter in the long run?** Although past performance is no guarantee of future results, the stock market has on average, doubled every eight years since 1926. A 1,000 point correction on the Dow will have meant nothing to long-term investors. In fact, it's not even an 8% correction. It would put you back to where you were in early December, 2006.
8. **Use today's nice gains to put things into perspective.** Remember how you felt in 2001 and 2002? And how low your account values were? It didn't feel all that good. But you got through it and are enjoying these higher values now. You'll survive the next correction too, if you keep your cool.

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Understanding The World Of Financial Advice

Since we took the less-traveled path and converted to a fee-only practice last July, many people have asked us questions about what it really means, and how is it different from other financial consulting options. Fee-only means fee-only. Our revenue comes directly from our clients—not from product or brokerage commissions, finder fees, trail commissions, or revenue from related entities. We are fiduciaries.

In recent years the distinctions about fiduciaries have become more blurred as brokerage firms entered the advisory arena. An important federal appeals court decision on March 30 sheds some new light on the distinctions, particularly as to what it means to be an investment advisor acting as a fiduciary.

First, a couple of definitions:

- **Registered investment advisor (RIA)**—a person or firm that is registered with the Federal Securities and Exchange Commission (SEC) or the states to provide investment advice for a fee. As explained below, they must act as fiduciaries.
- **Broker-Dealer—**a firm (typically called a brokerage firm) registered with the National Association of Securities Dealers (NASD) or a major stock exchange to buy and sell investments for commissions and mark-ups. Many banks and insurance companies are also affiliated with broker-dealers.
- **Fiduciary—** *(adj) Involving confidence or trust; (n) held or holding in trust for another.* In the financial world it means putting the clients' interests first. The duty is to the client, not the company.
- **Suitability Standard—**whether or not an investment recommendation is appropriate (but not necessarily the best) for an individual. This is the more lenient standard to which broker-dealers are held accountable.

The court ruling did two big things. First, it upheld the **1940 Investment Advisors Act** in a strongly-worded 3-0 decision. Under it, those who charge fees and are registered with the (SEC) or the state as registered investment advisors are held to a fiduciary standard. They must provide unbiased advice and full disclosure of potential conflicts of interest.

Second, it overturned a January 2006 SEC rule under which many in the brokerage environment were charging fees but avoided the fiduciary requirements of investment advisors. The Court reaffirmed that those who sell securities must not hide their sales activities and imply a fiduciary standard where none exists. They also may not hold themselves out as being a financial planner or as providing comprehensive financial planning.

An increasing numbers of individuals are fee-based advisors. They wear two hats, sometimes more if they sell insurance, broker mortgages, prepare taxes, practice law, or sell real estate. Many of them are registered with the SEC as investment advisors and they are required to operate as fiduciaries only in the fee-based areas of their practices.

What's next?

Some brokerage firms already have registered themselves and some of their representatives as investment advisors for the fee portion of their business. It will take time for other brokerage firms to adapt and convert their fee-based business over to an investment advisory/fiduciary relationship. And it may cost some of them money because they won't be able to collect both fees and commissions from the same accounts. Other firms may decide to go back to their brokerage roots. Some commentators have suggested that the brokerage industry may apply its financial and political muscle and try to change the 1940 law.

Which model is right for you?

There is no one right way, it depends upon your needs, your comfort level with your advisor or broker, and how you want to pay for services. If you need assistance trading stocks, bonds, mutual funds or a huge variety of initial public offerings or esoteric investments, and/or you are pretty-much a buy

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COMPENSATION MODELS

Type	Description	Standards	Regulator
Commission-only	Security commissions, spreads, product sales, trail commissions, production bonuses	Suitability	Mostly NASD, some SEC
Fee-only	Revenue only from clients, not from products, other firms, related entities, or referral fees	Fiduciary	SEC or the states
Fee-and Commission	A combination of the above	A combination. All conflicts must now be disclosed. The advisor and employing firm must act as a fiduciary on fee business. Until the court ruling, brokerage firms could offer fee-based accounts without being investment advisors or held to fiduciary standards.	Both
Fee-based	Mostly from fees		Both
Salary	Salary from employing bank, mutual fund, brokerage firm, or investment advisory firm	Suitability, unless the employer is a registered investment advisor (RIA)	Mostly NASD, but SEC if employer is an RIA

KEY DIFFERENCES—ADVISORS AND BROKERS

Official Title Of The Individual	Common Names	Firm	Main Regulator	Compensation	Standard
Advisory Associate	Advisor, Investment Advisor, Financial Advisor, Financial Planner	Registered Investment Advisor (RIA)	Securities and Exchange Commission (SEC) or the states	Fees, paid directly by the client	Fiduciary; Full disclosure of conflicts of interest
Registered Representative, Registered Principal	Broker, Financial Consultant, Investment Advisor, Financial Advisor, Financial Planner	Broker-Dealer (brokerage firm)	The National Association of Securities Dealers (NASD), a self-regulatory organization	Commissions, product trail fees, asset management fees	Suitability

Designing Your Own Long Term Care Policy

Last issue we discussed the criteria for deciding whether to self-insure your potential long-term care (LTC) costs or to transfer some or all of that risk to an insurance company. In this article, we'll examine some of the criteria to consider when selecting a policy.

Compared to life insurance (where either you are dead or your aren't), long-term care insurance is complex. There are many options from which to choose, but this also gives you the opportunity to control the cost and tailor a policy to your own situation. **The most important question is strength and solvency of the insurance carrier.** You really don't have any options here—pick an exceptionally strong company that has claims experience with LTC.

Beyond that, your decision will ultimately boil down to cost. There are basically five design criteria that drive the cost:

1. How much? **2.** How long? **3.** How soon? **4.** How broad? **5.** How current?

How Much and How Long?

We discussed this at length last issue. Over 78% of claims paid are for less than four years. **So consider a plan design of a higher daily benefit amount combined with a shorter benefit duration of three to five-years.**

Today most long-term care insurance policies base the available benefit on a **"pool of money"** concept, which is calculated by taking the number of days in the benefit duration times the daily benefit amount. The "pool of money" can be used to cover the cost of any combination of long-term care, be it home care, assisted living or a nursing facility, regardless of the time it takes to use up the pool.

One of latest trends is the **"Shared Benefit" rider**. This is a way for couples to have access to more years of coverage without purchasing a longer benefit duration. This provides a couple with greater flexibility and can make particular sense for women, who tend to live longer than men.

How soon?

Normally a large deductible or waiting period is a way to save money on insurance. But not so with LTC insurance. As inflation increases, the daily cost of care—and thus the cost of the deductible—increases dramatically, way beyond what would be saved with a 90-day waiting period. Make sure it's not "consecutive days of service" or "calendar days." With care early on, especially home care, it may not be required every day. **We generally recommend a 20 to 30-day elimination period as the most cost effective.**

How Broad?

This is where it gets complicated and expensive—kind of like buying a new car with lots of different packages and expensive options. Today most long-term care insurance policies are considered to be "comprehensive" covering in-home care, assisted living, foster care, adult day care and nursing care facilities. This comprehensive approach combined with the

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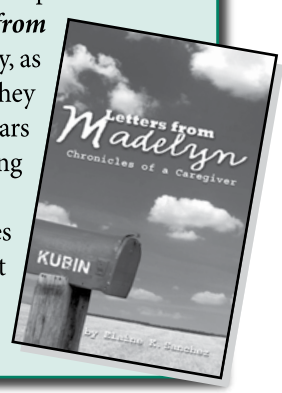
Congratulations, Elaine!

We have never published a client's name before, but with her permission we are so proud to announce the publication of Elaine K. Sanchez' delightful new book ***Letters from Madelyn, Chronicles of a Caregiver.*** It's a true story, as told through letters written by Elaine's mother after they both experience life-altering events. You will laugh through your tears as Madelyn describes the physical and spiritual struggles of caring for her husband following his debilitating stroke.



Elaine's book is available through bookstores, although most stores will have to order it. It is also available online at Amazon.com and at www.LaineyPublishing.com. It's a good read, and very appropriate with this issue's LTC article. Congratulations, Elaine!

The Team Advantage

Ron Kelemen and Mary Way are independent Certified Financial Planner™ certificants. Together with Alex Sheppard they jointly serve their clients as a team with over 37 years of combined experience. Their fee-only practice focuses on wealth planning and management for professionals, business owners, and retirees. Together, they have developed ***The Planning Vision Process***® and several other unique processes. They are advisory associates of The H Group, Inc., one of the largest independent fee-only registered investment advisory firms in the Northwest with 18 professionals and over $1 billion under active management.

About Ron Kelemen, CFP®

In practice since 1981, **Ron Kelemen, CFP®** is a contributing author of three financial planning reference books. *Medical Economics* listed him as one of the 150 best financial advisors for doctors. He is active in Salem Rotary, mentoring and in several local charities, and is frequently quoted in the national press and professional journals.

About Mary Way, CPA, CFP®

Mary Way, CPA, CFP®, recently celebrated her 13th anniversary as a member of the practice. She is also a non-practicing CPA with 16 years experience in banking, business, and finance. She sits on the Investment Policy Committee of The H Group, Inc. and is on the board of the Willamette Valley Estate Planning Council. She is active in Salem Rotary and the Financial Planning Section of the Oregon Society of CPAs.

About Alex Sheppard, MBA

Alex Sheppard, MBA joined the practice in March 2005, and has passed his CFP® comprehensive exam. He has a variety of experience in financial services, including four years as an analyst with a major mutual fund company. He is a active in the Salem Area Chamber of Commerce and serves on the board of South Salem Rotary.

TEAM UPDATE

Tax season this year was relatively calm and orderly until about the last week of March. But we survived it, and so did our clients and their tax professionals. Now that we no longer have a broker-dealer relationship and every client is on our portfolio reporting system, it should be much easier next year.

Lani and husband Jim are now empty nesters for the first time in 30 years after their 19-year old son moved in with his older brother. She traveled to Salt Lake City at the end of March to visit family, attend meetings and a reunion. She and Jim recently created a large semi-circular garden to accommodate espaliered fruit trees and several flats of seedlings they've been growing.

Debbie remained really busy processing retirement plan and IRA contributions, plus a large amount of tax-related withdrawal requests. Off duty on weekends, she helps husband Bob with his wedding business and gets to go to some pretty nice weddings at fancy places.

Alex and his new bride Virginia have settled into a comfortable routine now that the big wedding and honeymoon are over. He flew to Detroit for his brother-in-law's PhD graduation and spent a few days showing off Oregon and Seattle to his in-laws from Venezuela. They couldn't have picked a more beautiful time of year.

Mary is learning more about the virtue of patience, while her beautiful south Salem home is on the market. She and husband Steve can hardly wait to move into their new Silverton home. Mary was a featured panelist at the annual Leave A Legacy symposium and a co-speaker with Ron for the Silverton Rotary on the topic of financial planning. She is actively involved in Salem Rotary's annual raffle. See her for tickets!

Ron and wife Kathy are also learning about patience. Their new condo finally broke ground over one year past the originally projected occupancy date. Completion is scheduled for late fall of 2008. Ron gave a two-hour presentation to the Eugene Financial Planning Association on practice management. As President of the Medical Foundation of Marion and Polk Counties he was highly involved in its annual fundraiser. He traded in his snowboard and has clocked over 500 miles on his road bike since March 1.

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and hold investor, then perhaps the **brokerage model** is best for you. Just be sure to ask your broker about all costs and the conflicts of interest of the employing firm.

If you seek on-going portfolio management and/or financial planning advice, and you want a fiduciary standard, perhaps the **fee model** is better for you. For us, we are glad we chose the fiduciary fee-only model because:

- Full and simple disclosure is easier for our clients to understand
- The concept of absolutely no commissions, product sales, or finder fees is easy to understand and it simplifies our lives
- We can recommend courses of action without bias
- It puts us on retainer to work only for our clients.

THE H GROUP, INC. *The Independent Wealth Management Firm*

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The Kelemen, Way & Sheppard Financial Perspective
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Designing Your Own Long Term Care Policy. . . continued from page 3.

"pool of money" concept and the "Shared Benefit" rider provide the consumer with choice and flexibility. Due to space limitations we can't discuss other available options in detail, but here are some of the main ones:

- A Survivorship rider
- A Return of Premium rider
- Non-Forfeiture Coverage rider
- Accelerated Premium options

How Current? - – The Role of Inflation Protection

Since long term care costs are rising faster than inflation, this is one area where you don't want to skimp. With an inflation protection provision your daily benefit increases a certain percentage each year to help keep pace with the rising cost of long-term care. Often there are at least three options; 5% compound interest, 5% simple interest and the future purchase option.

We don't recommend the future purchase options. These could end up costing you much more when you exercise your options to purchase more benefit because the cost of the additional benefit is based on your "attained" or new age, not your "original" age when the policy was issued. More than anything, this rider is a way to guarantee you medical insurability. In the long run, it is less expensive to buy sound base coverage with the 5% compound increase.

There are other criteria, and certainly more whistles and bells than mentioned above. And as discussed in the last issue, you need to analyze whether or not to self insure. We can help you assess whether or not you need the insurance and elaborate on these various options in much more detail. And if you do need LTC, we can refer you to a trustworthy independent specialist who represents a variety of companies.

Long-term care planning is not a pleasant topic. But you owe it to your future and your loved ones to address this important personal and financial issue.