



The AFC[®] Learning System

MODULE 3: Assist the Client with Future Planning





A background image showing a person's hand writing on a notepad, with a laptop and other papers visible on a desk. The image is dark blue and serves as a backdrop for the text.

COMPETENCY: Educate Client on How to Manage Financial Risks

Educate Client about Financial Risk

Provide clients with rationale to manage financial risk, educate client on the financial risk management process, and assist the client to periodically review insurance needs

Rationale to Manage Financial Risk

Risk = uncertainty

- Pure risk
 - Loss or no loss
 - Examples: Illness, accident, natural disaster, scams, identity theft
 - Often insurable
- Speculative risk
 - Gain or loss
 - Examples: New business, investing
 - Not insurable



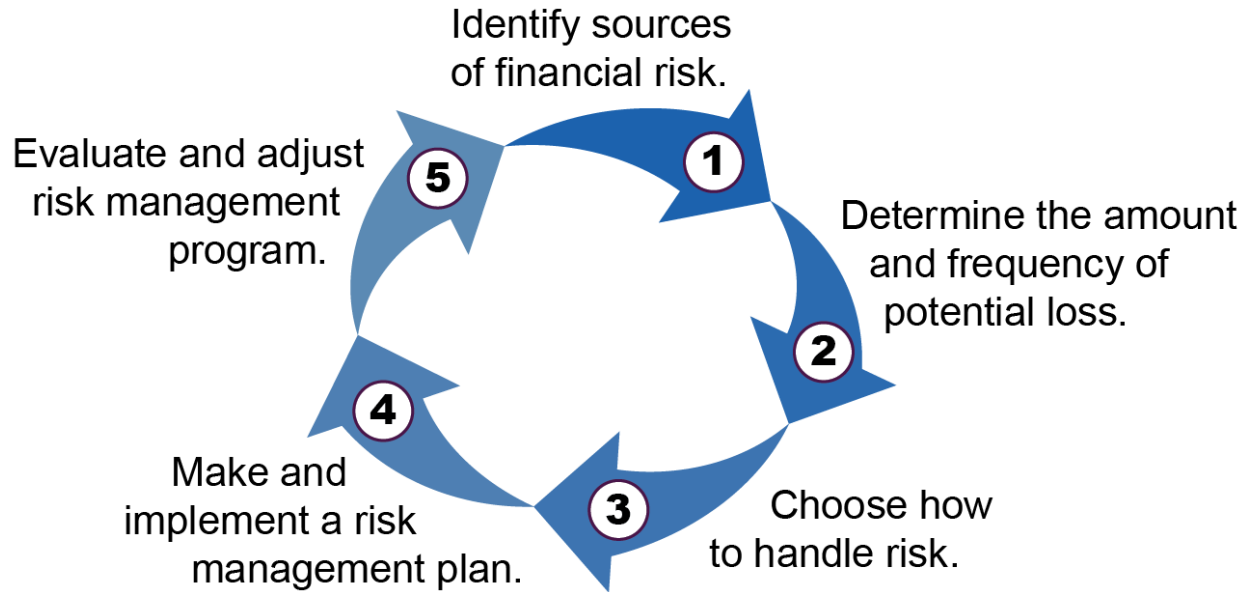
Types of Financial Losses



Property, liability, and medical are three categories of losses. What are their characteristics and what are some examples?

- Property: Damaged/destroyed property with high repair or replacement costs. Home damage from tornado.
- Liability: Being held liable for other people's losses. Crashing one's car into someone's house.
- Medical: Large medical expenses and lost earnings due to injury or illness of self, dependent. Caretaker to someone with expensive medical needs.

Risk Management Process





Identify Sources of Financial Risk

- If client has exposure (e.g., owns a home)
- Peril could occur (house burns down)
- Hazards impact frequency (region prone to wildfires)

Identify Sources of Financial Risk



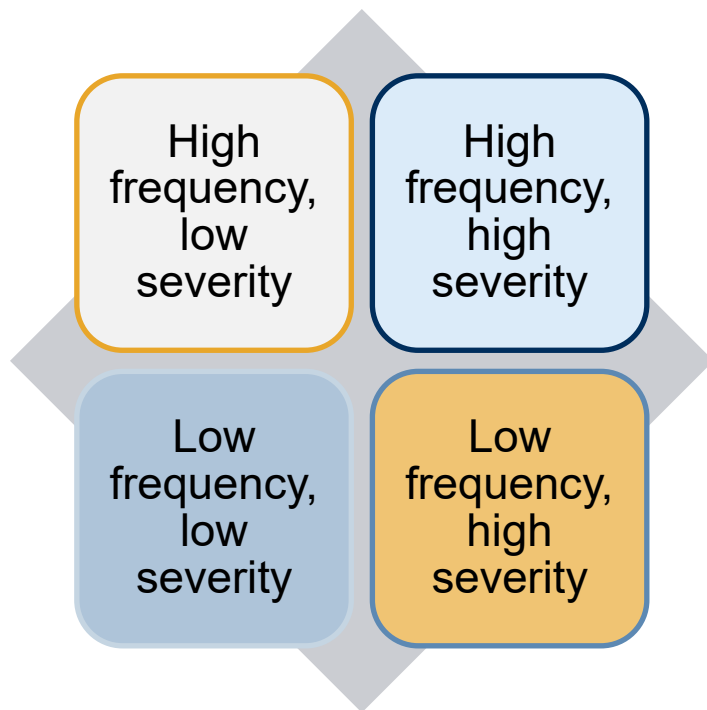
Insurance companies are concerned with hazards. What is the difference between a morale hazard and a moral hazard?

- a) Morale: physical characteristics of a person or property that increase chances of a loss. Moral: indifference or carelessness.
- b) Morale: indifference or carelessness. Moral: conscious negligence.
- c) Morale: conscious negligence. Moral: indifference or carelessness.

Answer: b.

Characteristics of the person or property that increase chances of a loss are called physical hazards.

Determine Severity and Frequency of Potential Loss



- Insurance most effective for low frequency, high severity
- Explore insurance for high/high, but may not be available or affordable
- Low severity: retain rather than insure

Choose How to Handle Risk

- Avoidance
 - Do not do the activity or own the asset
- Retention
 - Retain some (deductible) or all risk
- Reduction
 - Reduce frequency or severity of risk
- Transfer
 - Move some or all risk to third party: insurance or co-signer

Choose How to Handle Risk



Which is an example of risk retention?

- a) Getting renter's insurance
- b) Taking public transit rather than own a car
- c) Choosing not to get a protection plan for a coffee maker
- d) Ensuring fire alarms batteries are changed regularly

Answer: c.

a. is transfer, b. is avoidance, c. is retention, d. is reduction

Make and Implement a Risk Management Plan

- Risk management plan: Implement risk choices and periodically review
 - Emergency savings and insurance form much of the plan
- Large-loss principle
 - Get insurance for risks of financially devastating losses
 - Cover expenses that can be reasonably managed out of pocket

Educate Client about Financial Risk



Periodically Evaluate and Adjust Plan as Needed

Risk management not one-time activity:
periodically reevaluate

- Income: e.g., a raise
- Lifestyle: e.g., start a family
- Health: e.g., health status changes

Assist Client to Periodically Review Insurance Needs

Insurance needs common to clients in their 20s:

- Life: Perhaps less of a priority, but could be important if have dependents
- Medical: Important, but client could resist paying for much coverage
 - Test for needs and means
- Car: Get at least liability (state minimums), consider higher levels for major accidents
- Renter's insurance (or homeowners)



Insurance Needs of Clients in their 30s to their 50s



What levels of life, medical, vehicle, homeowners, and umbrella insurance do clients in their 30s to 50s often want as they progress in their careers, perhaps start or grow families, and/or acquire more assets?

- Life: Vital for families. Cover both parents (especially if a primary earner)?
- Reassess medical insurance needs often. E.g., in-network providers?
- Car: Several vehicles plus more assets to protect?
- Homeowners: Enough insurance for current home value?
- Umbrella: If more assets, extend liability coverage beyond policy limits?



Assist Client to Periodically Review Insurance Needs

Insurance needs for clients in 60s+

- Life
 - Less vital if dependents now independent
 - Is death benefit to survivors a priority?
- Medical
 - Age specific coverage? Insurance options?
 - Prepare to enroll in Medicare
- Car: Evaluate transportation choices
- Home: Still important if own home

Reducing Insurance Cost

- Discounts
 - Improvements
 - Bundling
 - Annual payment
 - Others specific to type
- Adjust deductible amount
- Shop around for better rates
- Might cancel some insurance policies that are no longer needed

Insurance Cost and Needs Relative to Risk

	High Deductible	Low Deductible
Pros	<ul style="list-style-type: none">• Lower premiums• Greater potential for long-term savings on insurance costs	<ul style="list-style-type: none">• Lower out-of-pocket costs in event of major loss• Cost/expense is more predictable (can budget for cost of premiums, deductible)
Cons	<ul style="list-style-type: none">• Higher out-of-pocket costs in event of major loss• May need to access emergency funds to pay deductible	<ul style="list-style-type: none">• Higher premiums• Less potential for long-term savings on insurance costs

Educate Client about Insurance Products

Educate client about insurance types, clauses, property and liability insurance, the health insurance market, and insurance for health, life, disability, and long-term care

General Insurance Types



Which is true of general types of insurance?

- a) Named-peril insurance covers comprehensive losses and specifically named losses
- b) All-perils insurance cannot have exclusions to coverage
- c) Covering risk of a wedding cancellation would use all-perils insurance.
- d) Fire insurance is an example of named-peril insurance

**Answer: d. All insurance has exclusions (specific perils not covered).
Named-peril insurance only covers specifically named perils (not comprehensive losses).**

All-perils insurance can have specifically excluded risks in policy.

General Insurance Clauses: Principle of Indemnity



What is the principle of indemnity?

- Policyholder will be compensated for actual cash value of financial loss
- One cannot profit from an insurance claim
- If have two types of insurance that cover a claim, the two policies will not pay out more than the total cost of a claim

General Insurance Clauses: Cash Value versus Replacement Value

Actual Cash Value

- Price less depreciation
- Default coverage, lower premiums
- Example
 - \$500 laptop depreciated to \$250
 - If stolen, get \$250 (minus deductible)
 - Might not be able to afford replacement

Replacement Value

- Cost of new item of similar kind, quality
- Higher premiums
- Example
 - Same \$500 laptop, comparable model costs \$600
 - If stolen, get \$600 (minus deductible)
 - More likely able to replace



General Insurance Clauses

- Can request policy customizations to fit needs
- Riders
 - Optional add-ons to modify/expand coverage
- Homeowners insurance examples
 - Inflation protection rider (automatic adjustment based on inflation)
 - Add coverage for jewelry or computers
- Vehicle insurance example
 - Accident forgiveness

Flood and Earthquake Insurance



Floods and earthquakes can cause significant property damage. How does insurance for these types of perils differ from other named-peril insurance?

- Flood protection administered and subsidized by federal government
 - National Flood Insurance Program: Up to \$250,000 for home, \$100,000 for contents
- Earthquake coverage will vary by state (e.g., in California, insurers must offer as add-on)
 - No government insurance program

Burden of Proof



What does the burden of proof mean in relation to making an insurance claim?

- Insured party responsible for proving risk occurred
- After proof provided, burden shifts to insurer who will assess if covered or excluded

Types of Homeowners Insurance Policies

- Basic coverage offering named-perils insurance
- Broader coverage for homeowners, offering named-perils insurance
- Open perils insurance
- Renter's insurance
- Coverage for condominium owners
- Coverage for older homes

Homeowners Insurance Includes Property and Liability Sections

Property

- Dwelling
- Other structures (e.g., garage)
 - Limited to 10% of home's coverage
- Personal property (has exclusions)
 - Limited to 50% of home's coverage
- Loss of use (becomes uninhabitable)
 - Limited to 20% of home's coverage

Liability

- Personal liability
 - If someone injured on property
 - Excludes business and car-related
- Medical payments to others (non-family)
 - Up to \$1,000 for medical expenses

Homeowners Insurance

- Not required by law, but is mortgage lender requirement
- Always recommended, even if no mortgage
- Standardized property and liability sections and coverage levels per section help pick right insurance for client's situation
- Offset catastrophic loss, not all loss
- Umbrella insurance: after regular coverage exhausted

Renter's Insurance Benefits

- Broad protection for property damage or loss (in home, in moving truck)
- Liability (e.g., injured in home)
- Loss of use
- Tenant belongings not covered by landlord's property insurance
- Inexpensive insurance



Addressing Gaps in Renter's Insurance

- Get replacement cost coverage?
- Need endorsements for items worth more than policy limits?
 - E.g., jewelry, money, firearms, electronics
- Identity theft coverage
- Pet damage
- Military equipment/uniforms coverage: for items kept in home
- Must be named on policy (e.g., roommates not covered unless on policy)



Automobile and Other Major Property Insurance

- Liability insurance required by law
- Proof of insurance
- Minimums by state laws
- Lender requirements

Factors that Impact the Cost of Vehicle Insurance



What are some of the factors that affect the size of premiums (in addition to the deductible amount)?

- Age and gender
- Driving history, amount of driving
- Car type
- Location
- Credit score

Standardized Personal Automobile Policy (PAP)

- Part A: Liability coverage
 - Common split: 25/50/25 (\$25,000 medical coverage per person, \$50,000 medical coverage per accident, \$25,000 for property damage)
 - Other parts below also use similar terminology and format for limits
- Part B: Medical expenses
- Part C: Uninsured/underinsured motorist
- Part D: Physical damage (non-collision-related, such as theft, weather damage)

Educate Client on U.S. Health Insurance Market



Match the term to its identifier.

- | | | |
|---------------------------------|---|-----------------------------------|
| a) Co-payment | → | 1. E.g., 80/20 after deductible |
| b) Coinsurance | → | 2. May need to provide referrals |
| c) Out-of-pocket maximum | → | 3. Small required upfront payment |
| d) Primary care physician (PCP) | → | 4. Maximum insured payout in year |

Answer: a. 3, b. 1, c. 4, d. 2.

PCP is medical professional who serves as first point of contact, offering general treatment, preventive care, and referrals.

U.S. Health Insurance Market: Affordable Care Act (ACA)

- Reduced uninsured
- Can't deny due to pre-existing condition
- Open enrollment period
 - Time frame to enroll or modify, usually once per year
 - Exceptions for certain life events (e.g., marriage, baby, lost health coverage)
 - Prevent adverse selection: most likely to file are most eager to get (e.g., already sick)
- Special enrollment period
 - Termination, divorce, death of covered employee, and more

HealthCare.gov versus COBRA

HealthCare.gov

- Marketplace for health insurance plans
 - Check eligibility, compare, and enroll
- Premium tax credit
 - Income-based federal tax credit
 - For Marketplace plans only

COBRA

- Federal law allowing continued coverage after job loss or work hours reduction
- Entire premium (employer portion too)
- Employers can charge up to 102% of their cost
- Expensive, may prefer HealthCare.gov's special enrollment period

Risk of No/Inadequate Health Insurance

Why Some Clients Have No/Inadequate Health Insurance

- Young and healthy persons may feel it is not needed
- Want more take-home pay
- Client is self-employed and full cost is more obvious

What to Highlight to Clients without Health Insurance

- Make link between good health and ability to earn income
- Medical costs high and growing
- Financial goals at risk
- Required in several states

Commercial Health Insurance and Spending Accounts

- Preferred Provider Organization (PPO)
 - In- or out-of-network, referrals not required
- Point of Service (POS)
 - Primary care physician required for referrals, but can be in- or out-of-network
- Health Maintenance Organization (HMO)
 - Primary care physician required for referrals, but in-network only
- Exclusive Provider Organization (EPO)
 - Must use in-network, but referrals not required

High-Deductible Health Plan (HDHP)

- Lower premiums and higher deductibles than traditional fee-for-service insurance
- Maximum limits to out-of-pocket expenses
- Small employers may offer if unable to get deals larger employers get
- Often feature Health Savings Account (HSA)
 - Savings for qualifying medical expenses
 - Tax-free contributions and withdrawals



Health Savings Accounts versus Flexible Spending Accounts



Some clients may have both a flexible spending account (FSA) and a health savings account (HSA). What are some key similarities? Key differences?

- Both set aside pre-tax money
- HSA only for qualifying health expenses as defined by IRS
 - Is client's asset (not use it or lose it)
- FSA for qualified out-of-pocket healthcare costs, some medications/medical equipment, deductibles, coinsurance, co-pays, dependent care
 - Generally, use it or lose it

Government Health Insurance: Medicare

- Medicare.gov: 65+ (or younger if disabilities/conditions)
- Parts
 - Part A: Hospital Insurance
 - Part B: Medical Insurance
 - Part C: Medicare Advantage (covers Parts A and B, but private providers, may cover Part D, other differences)
 - Part D: Prescription Drug Coverage
- No long-term care or personal care (in-home) services coverage

Medicare-Specific Support



What are some ways for clients to get more information on Medicare including access to a free counselor who specializes in Medicare?

- Educate clients about Medicare.gov and its Care Compare tool
- Counselors who do not feel comfortable with Medicare intricacies can refer clients to a free State Health Insurance Assistance Program (SHIP) counselor (see also www.shiphelp.org)

Government Health Insurance: Medicaid

- Free or low-cost government insurance for persons with limited income and resources
- Joint federal and state
- See state site for criteria, but all states cover
 - Children, parents, pregnant
 - Elderly low income
 - People with disabilities
 - LTC and personal care
- See state Medicaid agencies for databases of providers who accept

Other Government Health Insurance

- Children's Health Insurance Program (CHIP)
 - Children in families with income too high for Medicaid, too low for private insurance
- Military only
 - TRICARE: All branches, retirees, and eligible family members of active/retired
 - CHAMPVA: Administered by VA
- Workers' Compensation
 - State-mandated for job-related injuries or illnesses



Healthcare Billing and Insurance Calculations

- Balance billing
 - Difference between fee and what is covered
 - Could be considerable, unexpected charge
- Coordination of benefits (COB)
 - If multiple insurance, primary pays first
 - Avoid overpayment or duplicate payment
- Explanation of benefits (EOB)
 - Summarizes what is covered, not a bill

Insurance Calculations: Coinsurance with Deductible



A client has an 80/20 coinsurance plan with a \$1,500 deductible and needs a minor surgery that will cost \$10,000. What is the total cost to the client?

Example: Minor surgery with 80/20 plan and \$1,500 deductible

Cost	\$10,000
Deductible	<u>\$1,500</u>
Cost after deductible	\$8,500
Coinsurance	$\$8,500 \times 0.2 = \$1,700$
Total cost	$\$1,500 + \$1,700 = \$3,200$

Medical Debt

- Lower priority debt
- Low or no interest rates
- If < 1 year old, no credit report impact
- Don't pay on credit card
- Might be eliminated if eligible
- Can still get emergency care



Educate Client about Life Insurance

- Cash payment to limit financial impact of one's death on others
- Are dependents, spouse, parents, siblings getting support?
- How much of family income does the client provide?
- How will family pay funeral expenses?
- Does the client have debt that is co-signed?
 - Co-signer responsible for that debt
- Will the client need evidence of insurability to get coverage?
 - Assessment of client income, assets, and age, possibly a medical exam

Life Insurance Terms



Define policyholder, beneficiary, and death benefits.

- Policyholder: The individual or entity who owns policy and has right to make decisions (e.g., beneficiary).
- Beneficiary: Recipient of assets, benefits, or insurance payouts. Can be changed.
- Death benefits: Amount paid out to beneficiaries when insured person passes away. This is the total (untaxed) payout amount.

Differentiate among Types of Life Insurance

Term Life Insurance

- Specified term
- Straightforward, affordable
- Renewable term
- Group term: e.g., employees as group
- Credit or mortgage group life insurance
 - Designed to pay off mortgages and other debts before distribution

Permanent Life Insurance

- Lifelong coverage + cash value component (savings feature)
- More complex, expensive
- Refer to insurance agent?

Term versus Permanent Life Insurance



If premiums are paid for either type, how do these insurance types differ?

- a) Term life only pays out if the client dies during a specified term, but permanent life has a lifetime term.
- b) Term life can't be renewed for more terms, but permanent life can be.
- c) Term life is more expensive than permanent life.
- d) Term life premiums do not go up if renewed while permanent life has regular premium increases.

Answer: a. Term life insurance covers a specified term. If the term expires and is not renewed, there is no death benefit.

Permanent life has a death benefit that the policy must pay on the death of the policyholder.



Educate Client on Life Insurance Details

- Questions
 - Priorities?
 - Amount of insurance?
- Priorities
 - Children's college education
 - Pay off debts
 - Income replacement
 - Final expenses

Approaches for Assessing How Much Life Insurance to Have

Income Multiplier

- 5-15 times buyer's annual gross income

DIME Approach

- Simpler than complex needs approach
- Focuses on Debts, Income, Mortgage balance, and Education costs

Complex Needs Approach

- Involved version for unique circumstances
- Uses time value of money concepts (addressed later)

Human Life Value

- Person's potential future earnings based on inflation and future raises

Educate Client about Disability Insurance

Income replacement from inability to work

- Check employer options first
- May also be state-provided options or Social Security coverage options



Own-Occupation versus Any-Occupation Disability Insurance



What are the differences between own-occupation and any-occupation disability insurance?

- Any-occupation pays only if individual is unable to do any work reasonably qualified to do. It is more restrictive and will have lower premiums.
- Own-occupation pays if individual is unable to do specific occupation held at onset of the disability. This is a more lenient policy type.

How Much Disability Insurance?

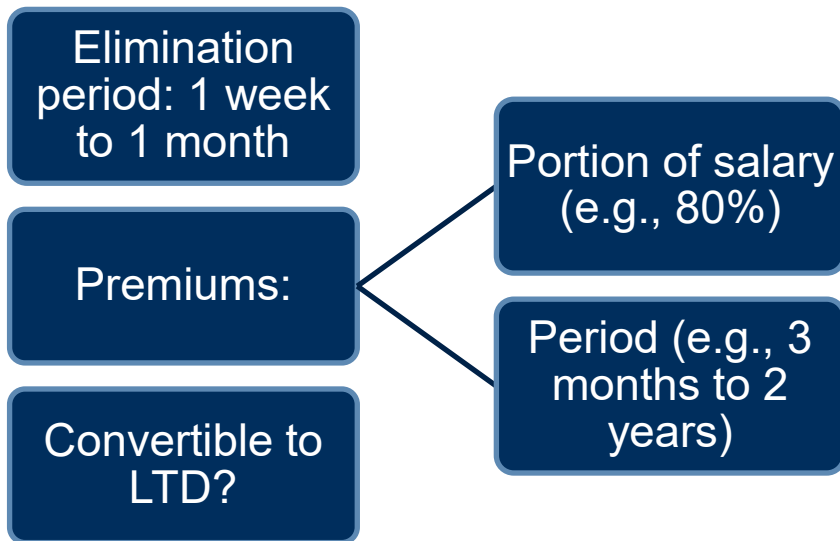
- Income benefit formula
 - % of pre-disability income, often between 50% and 75%
 - May factor in workers' compensation or Social Security benefits
- Flat amount
 - Predetermined set amount when policy purchased
 - Paid out regardless of other benefits received

Educate Client about Disability Insurance

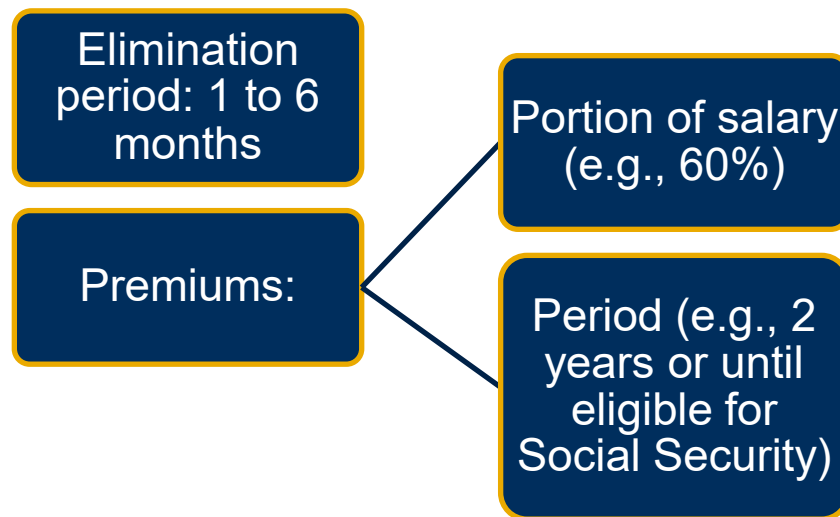
- What if there is an income gap after getting benefit?
 - Emergency funds
 - Government assistance programs
 - Consider a COLA (cost-of-living adjustment) rider
- What if there is a long elimination period?
 - Elimination period: From start of disability to start of benefits
 - Shorter elimination periods increase premiums

Educate Client about Disability Insurance

Short-term disability



Long-term disability



Educate Client on Long-Term Care (LTC) Insurance

- Expensive: high severity, high frequency
- Alternatives
 - Family care
 - Retirement savings
 - Medicaid if have no assets
- Covers skilled nursing facilities, assisted living facilities, or at-home care
- Maximum daily/monthly, likely won't cover all
- What if client can no longer afford the premium?

Activities of Daily Living (ADLs)



The elimination period for long-term care begins after insured is unable to do 2 activities of daily living (ADLs). What are some of these ADLs?

- Walking
- Eating
- Dressing
- Sometimes cognitive impairment

COMPETENCY: **Discuss Investment** **Fundamentals with the Client**

Educate Client on Investment Fundamentals

Assist client in goals, priorities, and risk tolerance



Assist Client in Goals and Priorities

- AFC not investment professional: educate, don't advise
- Goals and timeline
 - Short-term investments
 - Long-term investments
- Inflation risk: loss in purchasing power due to rising prices

Assist Client in Goals and Priorities



Which is true of various investment terms?

- a) Returns are only the positive gains over a specified period.
- b) Assets include cash, property, and investments.
- c) A portfolio is always diversified among all asset classes.
- d) Assets include cash and physical property but not investments.

Answer: b.

Returns can be positive or negative (gain or loss).

Assets include cash, property, and investments.

Portfolios can be diversified or hold a more limited set of assets.

Systematic (Market) Risks: Risks That Can't Easily Be Diversified Away

- Interest rate risk: Negative impact from changes in rates
- Reinvestment risk: May earn less when reinvested
- Volatility risk: High volatility means wider changes in value
- Exchange rate risk: Unfavorable currency exchange rate (international investments)

Diversification Helps Reduce Unsystematic Risks



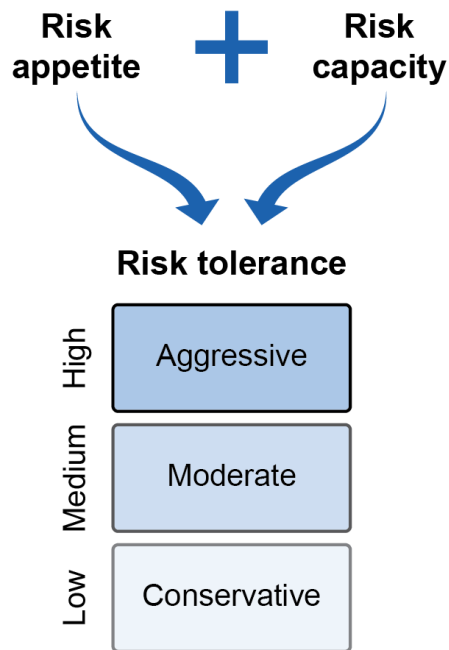
What are some type of unsystematic risks that a diversified portfolio can reduce?

- Business risk: Lower profits or failure of individual business
- Financial risk: Related to how a company manages its debt and capital
- Regulatory risk: Negative impact of changes in laws or regulations
- Liquidity risk: Risk of being unable to sell quickly enough

Importance of Diversification

- Asset allocation (diversify categories)
 - Classes react in different ways to economic change
 - Rebalancing: Realign to intended strategy
- Diversify assets within categories
 - Concentration risk: Too much weight in one asset or type
 - Some high risk/return, some low risk/return

Client Priorities and Risk Tolerance



- Aggressive (risk seeker): Ok with volatility
 - E.g., Mostly stocks, but some fixed-income securities, cash equivalents
- Moderate (some risk ok): Balance
 - E.g., About half fixed-income securities
- Conservative (risk averse): Preservation
 - E.g., Mostly fixed-income securities, but some blue-chip stocks, cash equivalents

Educate Client on Time Value of Money

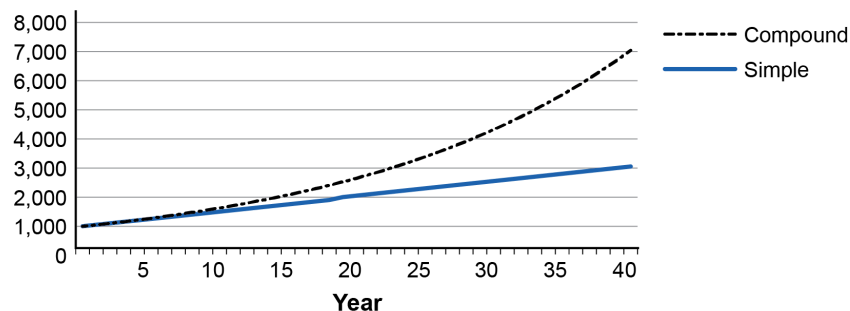
Explain the time value of money to the client

Explain Time Value of Money to Client

Time Value of Money

- Dollar today worth more than dollar in future
- Today's dollar: more purchasing power
- Does investment gain outpace inflation?

Simple versus compound interest



Calculating Compound Interest



Go to: www.investor.gov then Financial Tools and Calculators, Compound Interest Calculator. Inputs: Initial investment: \$1,000, monthly contribution: \$100, length of time in years: 25, estimated interest rate 5%, interest rate variance range: 2%, compounding: monthly. Best/expected/worst returns?

- Best (7%): \$86,733
- Expected (5%): \$63,032
- Worst (3%): \$46,716

Educate Client on Time Value of Money



Explain Time Value of Money to Client

- Future value (FV): Are current savings at given return enough to meet goal?
- Present value (PV): Work backwards from goal
- Rule of 72: Years for investment to double
 - Divide 72 by APR (rough estimate)

Educate Client on Active and Passive Investments

Determine client's interest in investing education and educate on active and passive investing strategies and types of investments

Avoid Giving Advice (Unless Additional Licenses) in These Areas



Give examples of subjects that would be considered investment advice.

- Asset classes to select
- Market trends
- Pros and cons of asset classes compared to others
- Allocation choice
- Distribution options
- Specific investment recommendations

Interest in Investing Education: Level of Desired Involvement

Active Investing

- Frequent buying/selling: Individual stocks, bonds, etc.
- Individual or analyst market analysis
- Greater time commitment
- Hands on: Knowledge needed

Passive Investing

- Minimize buying/selling: Pick funds
- Diversified portfolio
- Smaller time commitment
- Hands off

Long-Term Investment Methods



What are differences between buy-and-hold and dollar-cost averaging?

- Buy-and-hold: predetermined period regardless
 - Growth and minimized fees
 - Reinvest dividends, eventual gains taxed as long-term capital gains
- Dollar-cost averaging: Regular equal purchases (e.g., per paycheck)
 - Naturally get more when prices low, fewer when prices high



Active Investments: Cash Equivalents

- CDs: Interest/term fixed, early withdrawal penalty
- MMAs: Higher interest FDIC/SPIC checking
- MMMFs: Low risk, highly liquid, not FDIC
- U.S. Treasuries: Risk free, easy to liquidate

Bonds



What are some different categories of bonds and what differentiates them?

- Treasuries (T-Bills, T-Notes, T-Bonds): U.S. government issued, risk free
- Municipal bonds: Municipalities issue; federal tax exempt, not risk free
- Corporate bonds: Corporations issue, no tax benefit, higher interest
- Junk bonds: New or struggling company issued, high risk, high interest

Bond Terminology

- Bond yield: Return as % of face value
 - Coupon interest rate: APR
 - Coupon payment: Periodic interest payment
- Face value (par value): Amount repaid at maturity
 - Maturity date: When it will be repaid
- Zero-coupon bond: No coupon payments, but matures at face value

Bonds



What are two different possible sources of bondholder income?

- Hold to maturity: Get regular interest payments and principal at maturity
- Sell before maturity: Trade in over-the-counter markets, get fair market value (not face value)



Common and Preferred Stocks

- Blue-chip stock: Established, stable companies
- Growth: Growing faster than peers
- Income: Regular, predictable dividends
- Value: Undervalued bargain purchase

Real Estate



What are two ways that individuals can invest in real estate?

- Direct ownership as residence or investment property
- Real estate investment trusts (REITs): Portfolio of properties

Alternatives

- Commodities: bulk, interchangeable goods (e.g., gold, oil)
- Derivatives: Contracts that derive their value based on another asset
- Collectibles: Art, coins, memorabilia
- Cryptocurrency: Digital currency valued based on supply and demand



Passive: Mutual Funds and ETFs

- Fund manager sets fund objectives and manages allocation, diversification
 - Alternately, can be structured as active investment for individuals
-
- Mutual fund: Not traded on exchange
 - Exchange-traded fund (ETF): Traded on exchange

Passive: Types of Mutual Funds and ETFs

- Balanced: Stock, bond mix; growth, income, and risk reduction
- Target date: Adjust to more conservative as date nears
- Stock (equity): Capital growth and/or dividends
- Fixed-income: Bonds or other fixed income, lower risk
- Index: Replicate market index by buying tracked assets

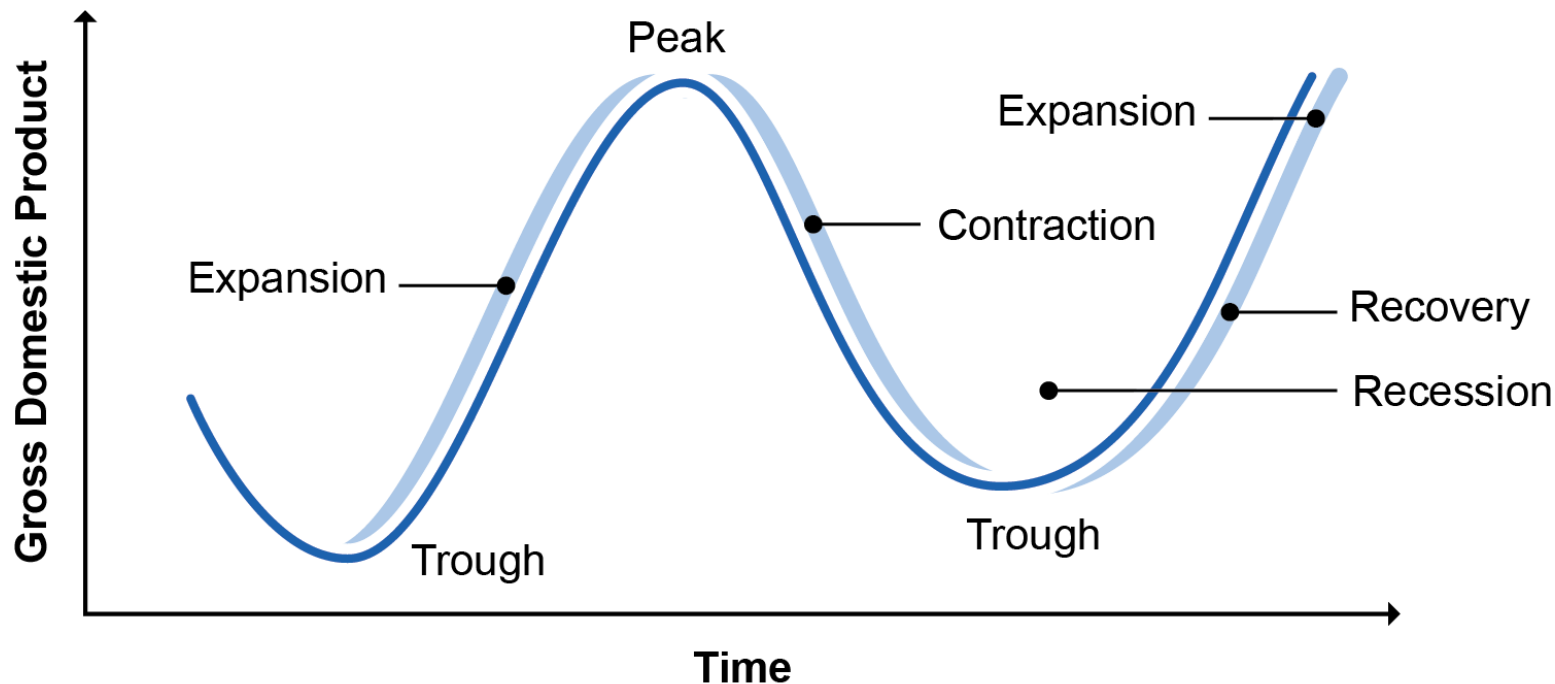
Common Investment Fees and Impact on Returns

- Fee size/frequency varies: impact on return
- Net asset value (NAV)
- Expense ratio
- Load or no-load funds (mutual funds)
- 12b-1/distribution fees
- Management fees or commissions
 - ETFs: Brokerage commission, bid-ask spread, expense ratio

Educate Client on Markets and Portfolio Management

Educate client about stock market, bond market, and financial professionals

Business Cycle



GDP and Recessions



Gross domestic product (GDP) is the market value of all goods and services produced by a country. How is a recession defined in terms of GDP?

- a) GDP starts falling instead of rising
- b) GDP falls for one quarter
- c) GDP falls for two consecutive quarters
- d) GDP falls for three consecutive quarters

Answer: c.

Consumer Price Index (CPI) and Inflation (Change in Purchasing Power)

- CPI: Basket of specific products, used to measure inflation
 - Fed funds rate: Basis for other rates, influences inflation
-
- High inflation
 - Often results in high interest rates
 - Big purchases prohibitively expensive
 - Lower corporate profits: stock price, dividends
 - Deflation
 - Economic weakness



Market Fluctuations

- Bull market: Prices 20% over prior peak
- Bear market: Prices 20% lower
- Market correction: 10% drop
- Market volatility: Degree of price variation

EMH and Irrational Investor Behavior

Efficient Market Hypothesis (EMH)

- Prices fully reflect all available information
- Difficult to outperform market
- But irrational investor behavior occurs

Irrational Investor Behavior

- Herd behavior: Buy into hype/pessimism
- Stock bubbles: Fail to follow fundamentals
- Overconfidence: Excessive risk/trading
- Loss aversion: Value loss drives to safety
- Fear of missing out (FOMO): Pick overvalued

Capital Gains/Losses and Paper Gains/Losses

Paper gains and losses

- Unrealized value of asset relative to purchase price
- No impact on income or taxes until sold

Capital gains and losses

- Capital gain
 - Unearned income has different tax treatment
- Capital loss
 - Offset gains for taxes

Short-Term versus Long-Term Gains



What is the tax implication difference for holding long-term (held for over one year) versus short-term (hold for one year or less) capital assets?

- Long-term: Usually have lower tax rates
- Short-term: Typically taxed as regular income

Educate Client about Robo-Advisors



Which is true of robo-advisors that use algorithms to manage a portfolio?

- a) They require higher account minimums than financial professionals
- b) They have limited access to certain investment types
- c) They do not need information on investor goals or risk tolerance
- d) They have higher fees than financial professionals

Answer: b.

They have lower account minimums and lower fees than investment professionals.

They need information on investor goals and risk tolerance.

Educate Client about Financial Professionals



Which follows a suitability standard (must be suitable for client's goals and risk tolerance but can promote profitable trades) rather than a fiduciary standard (must act in clients' best interests when offering advice or managing assets)?

- a) Certified public accountant (CPA)
- b) Registered investment advisors (RIA)
- c) Broker-dealers/brokers
- d) Chartered financial consultant (ChFC)

Answer: c. The other types are held to a fiduciary standard.

Educate Client about Financial Professionals

- Certified financial planner (CFP): Wealth building, retirement planning
- Chartered financial consultant (ChFC): Financial planning, insurance, estate planning
- Chartered financial analyst (CFA): Investment analysis, portfolios, ethical planning
- Certified public accountant (CPA): Auditing, tax preparation, financial consulting
- Investment advisor: Manages assets under \$100 million
- Registered investment advisor (RIA): Manages assets over \$100 million



When to Refer

- Client needs investment advice
- Client needs tax planning advice
- Client needs investment products or insurance products

Selection Criteria for Financial Professionals: Questions Clients Can Ask

- What experience and qualifications do they have?
- How can they help the client?
- What fees do they charge?
- Do they adhere to fiduciary standards?
- How and how often do they assess client portfolio?
- Do they provide a written agreement/contract specifying services?

Educate Client on Investor Protection

Educate client on investor protection and investment fraud

Market Regulators: Securities and Exchange Commission (SEC)

- Enforces trading laws
- Issues new security exchange regulations
- Coordinates enforcement and interpretation
- EDGAR database for research



Market Regulators: FINRA

- Independent self-regulatory organization
- Oversees brokerage firms, exchange markets
- BrokerCheck tool to see broker's:
 - Registration and licensing information
 - Employment history and regulatory actions
 - Complaints history
- Fund Analyzer
 - Research fund fees information

Market Regulators: State Regulators



When considering state regulators, what do they regulate and how do their regulations coordinate with federal regulations?

- They regulate licensing for firms and financial professionals in state
- They regulate registration of securities offered within the state
- Federal regulators supersede state regulators
- “Blue sky” laws are state-level equivalents of federal investing laws

Securities Investor Protection Corporation (SIPC)

- Nonprofit, nongovernment
 - Covers losses if SIPC member brokerage firm fails
- Account holders' assets
 - Up to \$500,000 of securities per brokerage account (not per depositor)
 - Up to \$250,000 protection for cash in account yet to be used to buy securities

Red Flags for Investment Fraud

- Cold calls or text, instant message, or social media contact
- Unlicensed or overseas investment professionals
- Aggressive, exuberant, or time-sensitive sellers
- Too good to be true or claim risk-free
- Anonymous/insider information
- They ask for personal information

SEC's Advice for Avoiding Fraud

- Ask questions if contacted about opportunity
- Ask for a prospectus or annual review
- Do independent research
- Do background check of professional
 - SEC's investor.gov has background checker



Types of Investment Fraud

- **Affinity:** Pretend to be part of group (e.g., religious community) to gain trust
- **Ponzi:** New customer deposits used to pay “returns” to existing ones
- **Pyramid:** Grow by recruiting to sell product/service that is not genuine
- **Internet/social media:** Widen scam reach and manipulate investment networks
- **Relationship investment scams:** Develop trusting or romantic relationship as long con

Types of Investment Fraud



Other types of investment fraud include spam/phishing, pump-and-dump schemes, and churning. Describe each.

- Spam/phishing: Email to get personal information or solicit advance fees
- Pump-and-dump: Scam to inflate a stock and sell when price rises
- Churning: Excessive trading to generate more fees and commissions



A background image showing a person's hand writing on a notepad, with a laptop and other papers visible on a desk. The image is overlaid with a dark blue gradient.

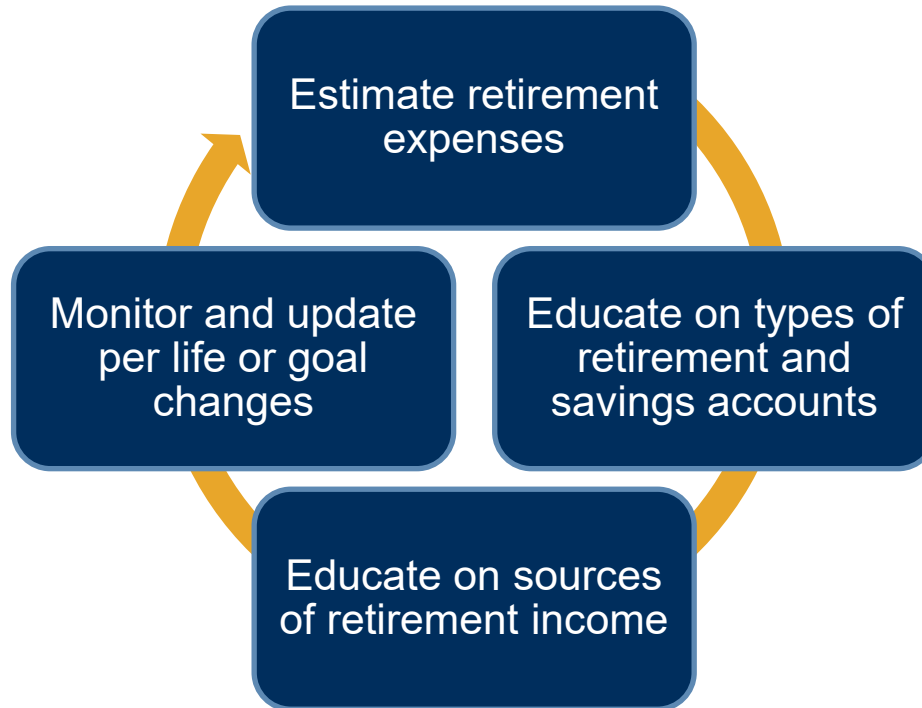
COMPETENCY: Educate Client on Retirement and Estate Planning

Educate Client on Retirement Planning

Educate client on income needed for preferred retirement lifestyle, tax-advantaged retirement accounts, other sources of retirement income, and assist a retired or near-retired client to get ready for retirement

Educate Client on Retirement Planning

Income Needed for Preferred Retirement Lifestyle





Retirement Lifestyle Changes

- Housing: Pay off home?
- Healthcare: Medicare/Medicaid
- Food: Inflation, home meals
- Clothing: No work attire
- Transportation: No commute
- Entertainment: Hobbies
- Travel: More or less?
- Family support
- Taxes

Retirement Budget versus WRR

Retirement budget

- Like standard budget, but during retirement years
- Helpful if client near retirement

Wage replacement ratio (WRR)

- $$\text{WRR} = \frac{\text{Post-Retirement Income}}{\text{Pre-Retirement Income}}$$
 - Post: Current income – FICA taxes – budgeted retirement savings
 - Live on X% of pre-retirement income?
- Helpful if retirement farther off

Educate Client about Retirement Calculation Tools

Common inputs

- Current age
- Preferred/expected retirement age
- Social Security income
- Other income
- Current savings rate, savings
- WRR

Inputs AFCs cannot advise on

- Expected tax rate during retirement
- Inflation assumption
- Rate-of-return assumption

Tax-Advantaged Retirement Accounts: Defined Benefit Plans

- Pension
 - Fewer being offered
- Guaranteed, defined, monthly payment based on
 - Years of employment
 - Average salary
- Employer has investment risk (both gains and losses)
- May or may not have cost-of-living adjustments (COLA)



Tax-Advantaged Retirement Accounts: Defined Contribution Plans and IRAs

Defined contribution plans or IRAs:

- Value based on contributions, timing, and returns
- Individual chooses asset allocation and has investment risk (gains and losses)

Defined contribution plans

- Employee and/or employer contributes

Individual retirement accounts (IRAs)

- Need earned income
- Spousal IRA
 - For low- or no-income spouse
 - Higher earning spouse can contribute

Traditional versus Roth IRAs

Traditional IRA

Contributions can be
tax deductible

Distributions taxed

RMDs: age 73 (75 if
born 1960 or later)

Roth IRA

After-tax contributions

Distributions tax-free

No RMDs

Early Withdrawal Penalties and Exceptions



Traditional and Roth IRAs have a 10% penalty for early withdrawals pre-59-1/2. Roth also requires account to be open at least 5 years. What are some exceptions to these penalties for each type?

- Traditional: Already retired, disability, disaster recovery, medical expenses, terminal illness, education expenses, and first-time homebuyer expenses
- Roth: Disability, disaster recovery, medical expenses, terminal illness, education expenses, first-time homebuyer expenses, and death (survivor can access account).

Types of Retirement Plans

401(k)

Private-sector defined contribution plans

- Traditional or Roth each with variety of investment options
- Annual contribution limit

Small company plans

SEP, SIMPLE IRAs, SIMPLE 401(k)s

- Each plan has own contribution limits

403(b)

Public-education and not-for-profit

- Employer and employee make pre-tax contributions

Thrift savings plan

Federal government employees

Educate Client on Sources of Retirement Income

- Cash and cash equivalents: Emergency fund and safe investments
- Investments: If habit is not to touch, withdrawals hard
- Full- or part-time job
 - Taxed
 - Social Security benefits temporarily reduced before full retirement age (FRA)
- Social Security (see next slide)
- Annuities: Guaranteed payments for life reduce longevity risk
- Reverse mortgage (see later slide)

Social Security (SS)

- Eligible if worker paid FICA/self-employment taxes long enough (40 SS credits), is disabled, or is survivor of deceased eligible worker
- Age impact
 - 62: Earliest, lowest benefit that is permanently lower
 - Full retirement age (FRA): Unreduced retirement benefit at 66 to 67
 - FRA to age 70: Higher basic benefit per year up to age 70
- SSI eligibility: Aged and limited income or younger but blind/disabled

Reverse Mortgages

- Loan repayment is due when move or pass away
- Eligible if 62+ and have significant equity in primary residence
- Cannot be delinquent on any federal debt (including student loans)
- Must meet HUD-approved reverse mortgage counselor
- Risks
 - High interest rates and closing costs
 - Foreclosure risk: Miss payments on property taxes or insurance or fail to maintain

Educate Client on Retirement Planning



Readying for Retirement: When and How to Enroll in Medicare and More

- Expected to enroll at 65
- If on employer health insurance may postpone
- 7-month window starts 3-months before 65
- SHIP counselor: free counseling (shiphelp.org)

Assist Client to Adjust Spending Plan for Retirement

- Develop workable retirement budget
- Plan for changes in travel, hobbies, and entertainment
- Risk of outliving retirement savings
- If there is a preferred retirement lifestyle and savings mismatch:
 - Delay retirement
 - Downsize
 - Relocate
 - Delay or reduce retirement fund withdrawals during times of low market value

Educate Client on Estate Planning

Educate client on estate and end-of-life planning, the estate planning process and tools, the end-of-life planning process and tools, and estate planning legal assistance

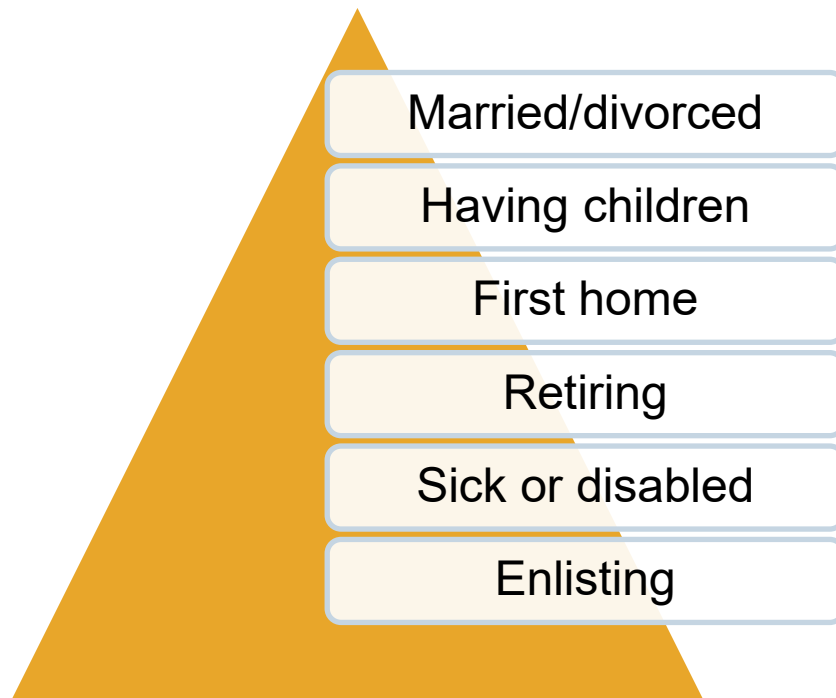
What if Clients Put off Estate Planning?



Many people put off estate planning. It is a sensitive topic. How can counselors promote estate planning even for younger adults?

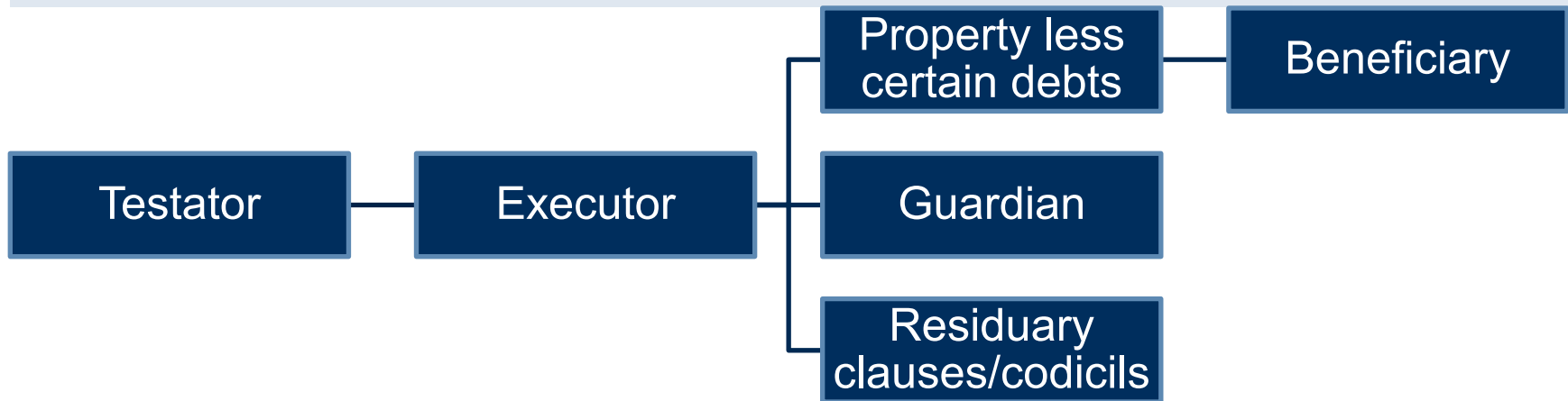
- Positive framing: It can help others during difficult time, avoid misunderstandings, and provide peace of mind
- Patience: Avoid remonstrating clients
- Affirmation: Affirm any steps that move toward estate planning
- Young adults: A health care proxy (for medical decisions if incapacitated)

When to Revisit/Update Estate and End-of-Life Planning



Wills

- Attorney help valuable: comprehensive, clear
- Formal with witnesses versus holographic will



Probate: Typical Process for Will or Intestate

Who is legally the debtor?

- Co-signed loans: Surviving co-signer
- Co-owned credit cards: Surviving cardholder
- Community property: In states with community property laws, the surviving spouse
- Independently-held debt: Creditors can try to claim from estate
 - Private student loans
 - Medical debt

Non-Probate Assets



Non-probate assets are assets that pass directly to a beneficiary upon the owner's death without going through the probate process. Examples?

- Life insurance
- Investment accounts
- Payable on death (POD): A bank account beneficiary designation
- Joint Tenancy with Right of Survivorship (JTROS): Shared property ownership or insurance, decedent's share goes to surviving members

Life Insurance Death Benefit: Tax-Free, No Probate

Term life insurance

- Death benefit only if die during term covered

Permanent life insurance

- Know want a death benefit
 - Guaranteed if premiums paid
- Can borrow against cash value
 - Repay or is taken from death benefit

Trusts

- Grantor transfers assets to form trust
- Trustee appointed to manage trust for beneficiaries
- Why create a trust?
 - Bypass probate
 - Manage assets for children
 - Fund education
 - Manage property for disabled
- If client is interested in trusts, refer to an attorney

Gifts

- A way to transfer assets before death
- For large gifts, consult tax professional for tax and tax reporting advice
- Gift tax reporting exemptions
 - No limit between spouses
 - Pay educational institution directly
 - Pay medical expenses directly



Advance Healthcare Directives

- Living will: Outline medical wishes and life sustaining treatments
 - Can do so on Physician Orders for Life Sustaining Treatment (POLST) form
- Do Not Resuscitate (DNR) Order: Do not administer CPR
- Do Not Intubate (DNI) Order: Do not provide mechanical ventilation
- Healthcare proxy: Appoint person to make medical choices if incapacitated

Medical Power of Attorney (MPOA)



What is a medical power of attorney?

- Legal document granting someone authority to act on behalf of another person for defined tasks or a set period of time.

Power of Attorney (POA)

Grantor



Attorney-in-fact (agent)

Durable: Continues even if incapacitated

Financial: Manage grantor's finances

Medical: Healthcare decisions

Limited: Clearly defined tasks or set period

Springing: Only if certain conditions occur (e.g., incapacitated)

Educate Client on Legal Assistance Selection

Criteria

- Can they help with specific needs?
- Qualifications?
- Qualifications current?
- Written agreement (retainer)?

Questions to ask

- Free consult?
- What services do they provide?
- Cost and how charged?
- How will they communicate?
- Pros and cons of suggested solutions and strategies?

Final Taxes

**Estate tax
return**

**Final tax
return**

- Decedent's surviving spouse or executor
- April tax deadline (or extension)
- Report person has died on final tax return
- Tax owed paid by estate