Wealth Management

KANE COMPANY

A FEE-ONLY REGISTERED INVESTMENT ADVISOR

Certified Public Accountants and Financial Advisors

Kane Company, P.C. 515-270-2727 Spring 2011

Why A Fiduciary Standard Is Important To Investors

Why didn't anyone discover what Bernard Madoff was up to? Why didn't the Securities and Exchange Commission or another regulatory group stop the former wealth manager, now imprisoned for life, from defrauding investors of an estimated $50 billion? The federal government will spend years looking for answers, while many investors wonder whether their advisor, too, may be taking advantage of their trust. But recently strengthened regulatory standards for financial advisors who hold the Certified Financial Planner (CFP®) designation could ease those concerns for investors working with CFP® licensees.

The Certified Financial Planning Board of Standards requires all CFP licensees to place clients' interests above their own. But the revised standards, enforceable as of Jan. 1, 2009, call for an even higher standard of care. And advisors who don't practice by the rules will lose the right to use the CFP® designation.

In a recent CFP Board web seminar, officials outlined two required standards of care. The baseline standard governs a CFP® whose dealings with a client are limited to a single aspect of financial planning, such as college planning, estate planning, or taxation. In those cases, a CFP® must place the client's interest first in every way. A CFP® who sells insurance products, for example, must disclose how he is compensated and must research and recommend the best product for the client. Because most insurance salespeople are paid by commission—a form of compensation that can lead to conflicts of interest between salesperson and client—requiring this standard for the sale of insurance represents an extraordinary step toward protecting consumers.

But a second, even higher standard of care applies when a CFP® has an ongoing relationship with a client and makes recommendations across a range of planning issues. CFP® licensees in those cases must adhere to a fiduciary standard, which involves acting as a trustee, always in utmost good faith. It applies to a CFP® who writes a comprehensive financial plan, requiring the advisor to analyze the client's situation objectively and to recommend products with the best price and execution for the client. But the fiduciary standard also requires a CFP® to look at the client's individual situation and offer a customized plan. It rejects boilerplate language as not being "in the client's best interest," because it tells every client to do the same thing, regardless of financial circumstances. Nor is it acceptable to offer the same investment portfolio to every client.

The most important impact of the CFP Board's fiduciary standard may involve the financial advice some employers make available to participants in 401(k) plans. The Pension Protection Act of 2006 encouraged plan sponsors to hire financial consultants to work with plan

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DFA Funds Market Leaders In 2010

During the financial crisis between October 2007 and March 2009, the S&P 500 Index declined 57%. This was definitely a tough time, but as I stated in my 2008 4Q newsletter article, "do not panic, but rather continue to buy". For those of you that did persevere in the market, you should have seen very positive returns. Between March 9, 2009 and Dec. 31, 2010, the S&P 500 Index had a powerful rally of 93%. The rally is striking; however, Dimensional Funds such as certain small cap funds performed even more impressively. DFA U.S. Small Cap was up 160%, DFA Emerging Markets Small Cap up 210% and DFA Asia Pacific Small Cap up 225%.

2010 market leaders: DFA U.S. Microcap Fund up 31.29%; DFA U.S. Small Cap Value Fund up 30.9%; DFA Emerging Markets Small Cap Portfolio up 30.18%; and DFA Asia Pacific Small Company Fund up 29.41%. Portfolios that included an allocation of U.S. Small Cap and Asia-Pacific and Emerging Market funds proved beneficial to boost overall returns the last couple of years.

Dimensional Fund Advisors continues to monitor closely the book-to-market values and price-to-earnings ratios of their underlying stock holdings and continually adjust their funds to stay fundamentally sound.

If you would like to learn more about DFA Funds, please visit our website or contact me for further information.

Steven L. Kane, CPA/PFS, CFP®

Retiree Relocation: Tax-Friendly States

Are you thinking about pulling up stakes when you retire? You may want to move to a state with warm temperatures and lots of sunshine, but there's also another kind of climate to consider—the tax climate. State taxes as well as federal levies can take a big bite out of retirement income, and some states devour decidedly more than others do. Here are several factors to take into account.

State income taxes. Seven states—Alaska, Florida, Nevada, South Dakota, Texas, Washington, and Wyoming—have no state income tax, and New Hampshire and Tennessee tax only investment dividend income that exceeds specified limits. However, many other states and the District of Columbia provide tax breaks for retirees, so you shouldn't automatically assume a no-tax state will be the best choice.

Retirement income. Most states that normally tax income provide partial exemptions for pensions. Even better, 10 states fully exempt income received from federal, state, or military pensions. And in Pennsylvania and Mississippi, all retirement income, including distributions from 401(k)s and IRAs, is state tax-free. Some other states impose high income tax rates on retirement income, however, with California leading the way at 9.55% on income of less than $1 million.

Social Security benefits. Up to 85% of the Social Security benefits you receive may be subject to federal income tax. However, the seven no-tax states, 27 others, and Washington, D.C. don't tax Social Security, though other special rules may apply. For instance, in Colorado, New Mexico, and Utah, you must add back a portion of Social Security benefits not taxed on a federal level when determining your eligibility for certain state income tax breaks.

Sales tax. These levies are often overlooked when retirees contemplate a move. On the plus side, five states—Alaska, Delaware, Montana, New Hampshire, and Oregon—currently have no sales tax, and other states may exempt food, medicine, and other necessities. But California has an 8.25% rate, and many cities and counties pile on additional sales tax charges. In Chicago and Los Angeles, you'll pay a combined rate of 9.75%—the nation's highest. And things could get worse. In 2009, 649 U.S. cities imposed new sales taxes or increased existing rates, while only 192 reduced sales tax rates (Source: Vertex Inc.).

Property taxes. The property tax burden varies widely throughout the country and even within states. The five states with the lowest median property taxes are Louisiana, Alabama, West Virginia, Mississippi, and Arkansas, while New Jersey, New Hampshire, Connecticut, New York, and Rhode Island have the highest.

Of course, tax rates aren't likely to be your only reason for choosing a particular retirement location. But it can't hurt to factor in these very real costs when planning your move. ●

401(k) Alternatives For Business Owners

If you have fewer than 25 employees in your small business, a 401(k) plan may not be right for you. But if your business offers no retirement plan at all, you could lose out in attracting the most qualified job candidates. One or more of these alternatives might be a better fit for your situation.

Simplified Employee Pension (SEP IRA). A SEP IRA is low cost and low maintenance.

- The employer makes all of the contributions; employees can't add to their accounts.
- The plan must cover all eligible employees.
- There is no "plan document."
- You don't have to file annual reports with the IRS.
- Contributions are tax deductible.
- Contributions can vary from year to year. So if you hit a lean spell, you aren't locked in.

Savings Incentive Match Plan for Employees (SIMPLE IRA). For a business with fewer than 10 employees, the SIMPLE IRA is a great starter plan.

- Your contribution is required; employees have the option of contributing.
- But you can't sock away as much for yourself as you can with a SEP IRA, which for 2010 allows a maximum contribution of $49,000. SIMPLE IRA contributions are normally capped at $11,500 ($14,000 for those 50 or older at year's end) plus an employer matching contribution that can't exceed 3% of salary.
- Don't confuse the SIMPLE IRA with the SIMPLE 401(k), which is like a traditional 401(k) plan but with higher fees and less flexibility.

Profit-Sharing Plan. This gives each employee a slice of the company's earnings.

- An overall annual contribution, based on the company's performance, is apportioned to individual accounts according to each employee's salary.
- Contributions are discretionary and

Recession Reshapes College Choices

At a time when getting into college has become more competitive than ever, the nation's economic crisis is making it harder for students and their parents to pay tuition and obtain financial aid. Those trends are affecting students' choices of where to apply and how many applications to send, and there are more hard choices to be made when admission letters arrive.

Families at all income levels, beset by job layoffs and mortgage woes, are trying to make college plans despite persistent economic uncertainties. At the same time, investment losses have forced many universities to cut back on scholarships and other aid. Rising numbers of private lenders, including such giants as Bank of America and Wachovia Bank, are pulling out of the student loan market, and lenders that remain have tightened requirements and raised interest rates and fees. And though government-backed loans carry lower interest rates, that pool of funds is limited.

Meanwhile, many households are cutting back on savings for college, and the value of education accounts has taken a hit. According to Morningstar Inc., all 79 of the tax-advantaged 529 college savings plans it tracks lost value in 2008, with most falling 10% or more. Another potential source of funds to pay for college—home equity loans or lines of credit—is also becoming more difficult to tap, according to Dennis Nostrand, vice president of enrollment management at the University of New Haven in Connecticut. "The value of homes has dropped, and banks are being extremely cautious in making home equity loans," says Nostrand.

David Hawkins, director of public policy for the National Association for College Admission Counseling, agrees that the economic slowdown is making it more difficult for families to plan for college. "They just don't know what to expect," Hawkins says. "We see students and parents attempting to hedge their bets by filling out more applications, a trend that has further fueled the increasing competition."

The average student today applies to five to seven schools, and some apply to 10 or more, Hawkins says. A generation ago, students typically applied to just two or three. "State colleges, which tend to cost much less than private institutions, are reporting higher-than-expected application numbers," says Hawkins. "Students and families are including state colleges in their application lists in larger numbers than in the past."

For example, Clemson University, a state school in South Carolina, has seen a 10% increase in in-state applications, and applications are up 18% this year at both the University of Idaho and the University of Central Florida. Binghamton University in New York, however, may take the prize, posting a 50% surge in applications for classes in fall 2009.

Another factor boosting the level of competition is steady growth during the past 15 years in annual numbers of high school graduates. That trend is expected to peak in 2009, when some 2.9 million teens will finish high school.

Students today have about a 70% chance of acceptance into a four-year college, according to Hawkins. Ivy League schools are among the most competitive, with some accepting fewer than one in 10 applicants, while a wide range of top-tier universities admits fewer than half of those who apply. Many very selective private colleges, despite their much higher costs, are also seeing application numbers rise. Private institutions often have more scholarship opportunities, some of which are not available through public schools.

In this intensely competitive environment, more parents are hiring educational consultants, sometimes when their children are only high school freshmen or sophomores, to help guide them through the application process. Yet while applications are surging at many colleges, pushing down the chance of being accepted, the economic crisis means universities often don't have the institutional dollars they once could use to convince admitted students to matriculate. "In the spring, when admission and financial aid letters go out, students and families are really going to have to take a close look at each school's combination of scholarships, grants, and loans," Hawkins says. "There is going to be some serious comparison shopping."

As you and your children formulate their college admissions strategies, we can help you explore ways to pay tuition and costs that won't undercut your own retirement planning. Please give us a call. ●

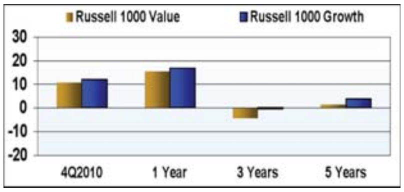
tend to vary from year to year.

- A business of any size may use a profit sharing plan and can combine it with other retirement plans.
- Businesses with profit-sharing plans must file IRS Form 5500 each year.
- Administrative costs may be higher than under more basic plans, because this plan must perform a non-discrimination test to ensure it doesn't favor highly compensated employees.

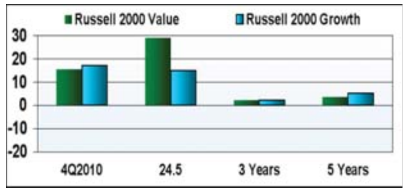
Defined-Benefit Plan. This is the most costly, complex plan for small businesses, but it has one big potential advantage—it lets you make very large contributions that can quickly build your nest egg. You're now allowed to fund a maximum annual retirement benefit of $195,000.

- Your contributions are mandatory.
- You can't decrease benefits retroactively.
- Defined-benefit plans are available to businesses of any size and can be combined with other retirement plans.
- Requires filing an IRS Form 5500 with a Schedule B each year.
- The Schedule B must be signed by an enrolled actuary, who will calculate contribution amounts based on your employees' ages and the target benefit. ●

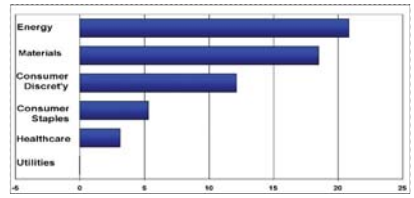
Market Data Bank: 4th Quarter 2010



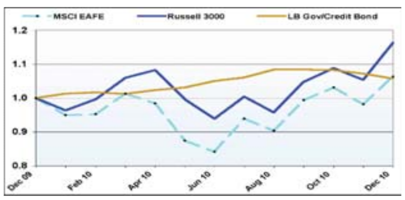
LARGE VALUE VS. LARGE GROWTH
As the prospect of a 4Q10 economic downturn dimmed, U.S. stocks extended their advance. Growth kept the lead, up 11.83% in the quarter compared to large-cap value stocks' 10.54% advance.



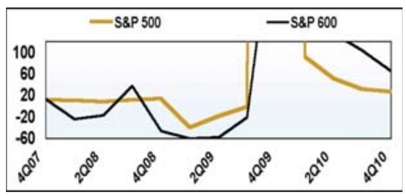
SMALL VALUE VS. SMALL GROWTH
Economic optimism fed demand for smaller U.S. companies that might benefit from a turnaround in domestic spending. Small growth surged 17.11% in 4Q10 while small value gained 15.36%.



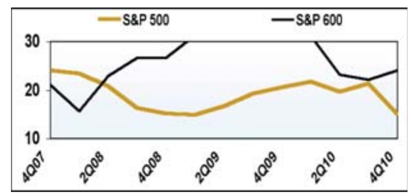
THREE BEST AND WORST SECTORS
Nine of the ten Standard & Poor's industrial groups ended the quarter in positive territory. Only the utilities sector, often viewed as a haven in economic downturns, lost ground.



FOREIGN, US STOCKS & US BONDS
While foreign stocks seemed to recover their balance as 4Q10 wore on, on an annualized basis their performance barely matched that of U.S. government bonds. U.S. stocks fared substantially better.



LARGE VS. SMALL STOCK EARNINGS
Even as the 2008-9 disruptions recede into the past, U.S. companies are still posting impressive earnings growth. Large-cap companies boosted their profits 27% in 4Q10; small caps grew 65%.



PRICE-TO-EARNINGS RATIO
The rotation into smaller stocks made blue-chip companies cheaper on an earnings basis than at any time since late 2008. For small-cap stocks, the ratio of price to earnings climbed slightly, to 24.

Small-cap stocks represented by Russell 2000 index, large-cap stocks represented by Russell 1000 index. Foreign stocks represented by the Morgan Stanley Capital/ International's Europe, Australia, Far East Index, and US bonds by the Lehman Bros. Government/Corporate Bond Index. P/E ratios exclude negative earnings. Small-cap stocks tend to be more volatile than large-caps. Bonds offer a fixed rate of return while stocks will fluctuate. Indices are unmanaged and do nott represent any specific investment. Foreign investing involves special risks, including political unrest, economic instability, and currency fluctuation. Past performance does not indicate future results.

Source: Russell/Mellon

Standard Is Important

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participants, but it didn't define what kind of advice would be suitable. In January 2009, the U.S. Department of Labor issued guidelines saying the advice could come from brokers as well as from Investment Advisor Representatives affiliated with Registered Investment Advisors.

Investment Advisor Representatives face regulation by the SEC or the states and receive fees for their advice, while brokers are regulated by the Financial Industry Regulatory Authority and can get commissions for sales of financial products. Because commissions may lead to at least a perceived conflict of interest, some members of Congress vehemently disagreed with allowing brokers to advise individuals on 401(k)s and argued that advice should come only from advisors who adhered to a strict fiduciary standard, such as the one the CFP Board enforces. Rep. Rob Andrews, a New Jersey Democrat, pointed to heavy losses in 401(k) accounts in 2008 and 2009 as underlining the need for objective advice from advisors adhering to a fiduciary standard.

Andrews criticized brokers for offering "conflicted advice," because their compensation could depend on which products they recommended. The DOL ruling would "expose millions of Americans to the Madoffs of the world," Andrews said, and he introduced legislation permitting only Investment Advisor Representatives, or others whose compensation isn't based on which investments they recommend, to work with 401(k) plan participants.

At the end of 2009, the DOL withdrew the ruling that would have allowed a broad range of advisors, including brokers, to offer 401(k) advice. And while that hasn't settled the issue, the dispute over who should advise plan participants has made more investors and regulators aware of the fiduciary standard and why it's important. ●

Steven L. Kane, CPA/PFS, CFP® Kane Company, P.C. 5526 N.W. 86th Street, Suite A, Johnston, Iowa 50131
phone: (515) 270-2727 fax: (515) 270-1509 email: KaneCompany@kanecompanypc.com www.kanecompanypc.com