

JOHN E. SESTINA

PLANNING A SUCCESSFUL FUTURE

Managing to Be Wealthy for Individuals
and Their Advisors



WILEY

PLANNING **A**
SUCCESSFUL
FUTURE

Managing to Be Wealthy for
Individuals and Their Advisors

JOHN E. SESTINA

WILEY

Copyright © 2016 by John Sestina. All rights reserved.

Published by John Wiley & Sons, Inc., Hoboken, New Jersey.

Published simultaneously in Canada.

No part of this publication may be reproduced, stored in a retrieval system, or transmitted in any form or by any means, electronic, mechanical, photocopying, recording, scanning, or otherwise, except as permitted under Section 107 or 108 of the 1976 United States Copyright Act, without either the prior written permission of the Publisher, or authorization through payment of the appropriate per-copy fee to the Copyright Clearance Center, Inc., 222 Rosewood Drive, Danvers, MA 01923, (978) 750-8400, fax (978) 646-8600, or on the Web at www.copyright.com. Requests to the Publisher for permission should be addressed to the Permissions Department, John Wiley & Sons, Inc., 111 River Street, Hoboken, NJ 07030, (201) 748-6011, fax (201) 748-6008, or online at <http://www.wiley.com/go/permissions>.

Limit of Liability/Disclaimer of Warranty: While the publisher and author have used their best efforts in preparing this book, they make no representations or warranties with respect to the accuracy or completeness of the contents of this book and specifically disclaim any implied warranties of merchantability or fitness for a particular purpose. No warranty may be created or extended by sales representatives or written sales materials. The advice and strategies contained herein may not be suitable for your situation. You should consult with a professional where appropriate. Neither the publisher nor author shall be liable for any loss of profit or any other commercial damages, including but not limited to special, incidental, consequential, or other damages.

For general information on our other products and services or for technical support, please contact our Customer Care Department within the United States at (800) 762-2974, outside the United States at (317) 572-3993 or fax (317) 572-4002.

Wiley publishes in a variety of print and electronic formats and by print-on-demand. Some material included with standard print versions of this book may not be included in e-books or in print-on-demand. If this book refers to media such as a CD or DVD that is not included in the version you purchased, you may download this material at <http://booksupport.wiley.com>. For more information about Wiley products, visit www.wiley.com.

Library of Congress Cataloging-in-Publication Data:

ISBN 978-1-119-06912-6 (Hardcover)

ISBN 978-1-119-18798-1 (ePDF)

ISBN 978-1-119-18797-4 (ePub)

Cover Design: Wiley

Cover Image: New shoot © zimmytws / iStockphoto

Printed in the United States of America.

10 9 8 7 6 5 4 3 2 1

Acknowledgments

Thanks to the many clients I have had through the years. They have given me opportunities to see every combination of financial circumstances and improve their financial lives and lifestyles.

I also deeply appreciate the sharing among fellow financial planners, particularly other NAPFA members. We have educated each other as this profession has grown. Special thanks to Margery Wasserman, Bob Underwood, and Jim Schwartz.

Thank you to my contributing authors: Tyler V. Cook, Lawrence Funderburke, Stephen A. Lukan, Bhagwan Satiani, and Kimberly E. Wirtz.

A special thanks to Tula Batanchiev, my editor at John Wiley & Sons, as well as to the other professionals there, including Stacey Rivera. My thanks also to marketing consultant Sandra S. Nichols, who worked with me in the beginning to find creative ways to show consumers that they do indeed have choices in financial planning.

John E. Sestina
Dublin, Ohio

Preface

If you're a consumer, maybe you wonder why your paycheck never seems to last until the end of the month. Perhaps you've lain awake at night, considering how to pay for your children's college, or tried to make prudent investments, only to see the stock market go down along with your savings.

You're not alone. Most of us struggle to make ends meet, whether we earn an annual \$50,000 or \$150,000. And when we seek advice, who can understand what the professionals are saying? Finances can be so intimidating! This book will help you chart your way to financial freedom without putting you to sleep or confusing you.

Before you can chart your specific financial plan, however, you need to know the basic concepts behind successful financial planning. Why do you want to invest? What are the obstacles to your financial freedom? Why is it important to start saving now? This book will teach you a proven, tested way to become financially independent. Isn't that what you need? Let your Uncle Harry brag about his latest hot stock tip. You will be able to sit back and smile, knowing that you will achieve your financial goals without any help from Uncle Harry. After all, it's not how much you make along the way, but whether you reach your destination.

If you're a financial planner, this book offers you a look inside the thinking of one of the country's preeminent financial planners. I began building and refining my wealth management system in 1965. In this book, I cover everything from the philosophical advantages of fee-only planning to tips on what clients should expect from you and how you can best serve their needs.

When I taught the first university-level course in personal financial planning in 1969, few had even heard the term. No one could have

predicted that fee-only financial planning would be so popular nearly 50 years later.

- Consistent processes, designations, and organizations have helped make financial planning a profession.
- The National Association of Personal Financial Advisors (NAPFA), made up exclusively of fee-only financial planners, has grown from 60 members at its beginning to a global organization with more than 2,400 members
- Financial planners can earn 21 different professional designations in more than 20 job titles dealing with different aspects of the field. Colleges and universities in nearly every state prepare students for the profession.
- Financial planning has grown to the extent that it warrants government regulation from both federal and state oversight bodies.
- Countless websites market the services of industry participants seeking to capitalize on the growing popularity of personal financial planning.

Establishing a brand-new profession has been a long, challenging, and rewarding road.

When I started looking for my first client in 1965, financial compensation was a concern. By the early 1970s, I had run the compensation gamut. I had taken commissions only, charged fees and taken commissions, and charged fees and offset them with commissions. I felt compelled to make a decision. Charging fees and accepting commissions from product sales had too much potential for clouding my recommendations. Offering the optimum in nonbiased advice required that I charge fees only.

About that time, I learned that another planner had become successful by charging fees rather than selling products. I met with him and soon discovered a few others who had the same philosophical concerns that I did. Out of that core group grew the fee-only financial planning movement and the first national fee-only organization, the National

Association of Personal Financial Advisors (NAPFA), which I founded with Bob Underwood and Jim Schwartz.

Fee-only financial planning is a client-centered, profitable profession. My experience has proved that an educated, motivated entrepreneur can become wealthy in his or her own right. The system is simple: give your clients the objectivity, comprehensiveness, and peace of mind they want. Financial planning must be client-centered in order to be profitable.

In the early years, a common misconception held that only the very wealthy could afford the best in objective and comprehensive advice. In truth, fee-only financial planning can be accessible to everyone.

Fee-only planners have the opportunity to serve an enormous and largely untapped market. Today's consumers are both more affluent and more educated than in the past. Thanks also to the technology revolution, they can become much more personally engaged in the planning process. Working with educated and involved clients is always more productive and profitable for both parties.

Making fee-only financial planning accessible on a systematic basis to every American was the foundation for creating the Sestina Network of Fee-Only Financial Planners in 1994. Others have also seen the potential and are following suit.

This book systematizes a wealth of resources to support your success in fee-only financial planning.

Contents

	Acknowledgments	ix
	Preface	xi
	Introduction	1
	Creating Your Financial Plan	2
	How Does This Relate to Investing?	3
	Are You Meeting Your Goals?	3
	Obstacles to Reaching Financial Goals	4
	Fuel Your Goals with Income	6
	Developing Your Plan	7
	Attaining Peace of Mind	8
Chapter #1	What Do You Want?	9
	Put It in Writing	9
	Six Steps to Financial Freedom	10
	Start Planning	13
	Other Goals	18
	Review Your Plans with Your Family Members and Advisors	18
	You Know What You Want	19
Chapter #2	What Do You Have Now?	21
	Materials	22
	Information You'll Need	22
	Filing the Information	22
	Looking for Missing Financial Information	24
	Understand What You Have	25

	Cash Flow Planning: When, Where, and How Much?	26
	Plan Your Future Cash Flow	34
	Plan Your Cash Reserve	34
	Balance Sheet: What Is Your Financial Worth?	43
Chapter #3	Retirement	51
	Review Your Retirement Goals	52
	Your Cash Flow Worksheet Is Crucial	52
	Assumptions for Retirement Planning	53
	But What About . . . ?	62
Chapter #4	Planning to Send Your Children to College	67
	How Much Will a College Degree Cost?	67
	Where Will You Find the Money?	68
	Review Your Goals	70
	Who Controls the Money?	71
	Effects of Tax Laws on Your Education Goal	72
	Income Shifting to Save Taxes	75
Chapter #5	A House Is Not Always a Good Investment	81
	The True Cost of Home Ownership	82
	A House as an Investment	85
	Shopping for a Mortgage	90
	Saving Money on Your Mortgage	94
	Buying and Selling	98
Chapter #6	Insurance	101
	Types of Life Insurance	101
	My Recommendation	105
	Types of Insurance Companies	106
	Tax Considerations	106
	Disability Insurance	109

Chapter #7	Liabilities	115
	Good Reasons to Borrow Money	115
	Bad Reasons to Borrow	116
	Types of Credit	117
Chapter #8	Taxes	125
	Four Methods for Reducing Taxes	125
	Tax Tools	131
Chapter #9	Investments	137
	Financial Basics	138
	How the Financial Cycle Works	141
	Your Investment Goal	143
	Evaluating Risk	143
	Investment Triangle	146
	Investment Strategy	148
	Investment Choices	152
	Common Investment Mistakes	160
	Other Investments	165
Chapter #10	How to Find and Work with a Financial Planner	171
	<i>Tyler V. Cook</i>	
	What Is a Financial Planner?	171
	Exposing the Myths	174
	How to Find a Financial Planner	175
Chapter #11	Financial Planning for Women	179
	<i>Kimberly E. Wirtz</i>	
	Learn About Family Finances While You Can	180
	Understand Your Assets, Where They Are, and Who Legally Owns Them	182
	Consolidate Accounts	182

Name Primary and Backup Beneficiaries	183
Understand Pension and Social Security Arrangements	184
You Need a Will, a Living Will, and Two Powers of Attorney	185
Both Spouses Need Life and Disability Insurance	186
Balancing It All	188
Chapter #12 Financial Planning for Business Owners	189
<i>Stephen Lukan</i>	
Business Structure	190
Turning a Hobby into a Business	191
Tax and Retirement Planning	192
Building a Team	193
Business Partners	194
Succession Planning	195
Chapter #13 Financial Planning for Physicians	197
<i>Bhagwan Satiani</i>	
Reasons for Bad Financial Decisions	198
Results of Financial Mistakes	198
Chapter #14 Learning from Professional Athletes' Mistakes	207
<i>Lawrence Funderburke</i>	
Holes in Their Pockets	208
Inexperience Hurts	209
Learn from Their Mistakes	209
About the Contributors	215
About the Author	217
Index	219

Introduction

No matter how dire your situation, there is hope. You can take control of your financial life and build a prosperous future.

I'm saying this from personal experience. I was raised in a coal camp near Clarksburg, West Virginia, the son of an uneducated miner. The tarpaper shack I called home had no running water. I lost the first joint of a finger when I played catch with a sharp piece of anthracite, a common pastime in a setting with few childhood diversions. My parents had no way to help me get an education or any start toward a prosperous adult life. I have faced poverty, disconnected utilities, empty refrigerators, and thieving business partners.

I am also the well-educated, prosperous owner of a financial planning firm, a loving husband, and a devoted father. I've earned the ability to enjoy my friends, my hobbies, my family, and the financial security I've created. I did it myself, and I am absolutely passionate about helping you do it, too.

This book is the culmination of my career as a financial planner. In it, I endeavor to share decades of knowledge and experience in both the nuts and bolts of planning and investing, which you can find in other places, and my thinking about money and life, which you will only find here.

At its best, I believe that good financial planning is synergistic. When you learn to set and achieve financial goals, you also learn a great deal about yourself: your priorities, your values, your beliefs about marriage and family, your professional ideals. When we align money with our deepest beliefs, we become much more able to lead lives that are in keeping with our values.

In that sense, this book is only partially about money. At a deeper level, it is about teaching you to find and bring out the best in yourself. Whether you're 26 and have tons of student debt, 40 and realizing that you will have two kids in college at the same time, or 60 and worried about retiring, there is help and hope for you.

Reacting to financial circumstances is what most people do. Retirement is five years away, and they wonder how they'll have enough money to live on, never mind enough money to travel to places they've always dreamed of going. Their child is due to begin college in just three years. How will they get the money they need to pay tuition and other college expenses? Or perhaps they hear about what someone else calls a great investment opportunity. How do they know whether it's a wonderful opportunity for *them*?

So many of us wait until the need for money or decisions is nearly upon us before we take action. It can be different for you. In this book, I will show you—as I've shown clients for 50 years—how you can achieve financial independence by making financial decisions proactively, not reactively. You have the ability to take care of yourself and your family, without waiting for any kind of miracle. I'll show you how.

Creating Your Financial Plan

The key is in creating a financial plan. An individual financial plan is a map, helping you navigate the complex, constantly changing world of finance. This book will guide you as you prepare your plan and put it into action. That will take time and effort, but it will also help you sleep better at night, undisturbed by worries and questions about money.

This book will help you create your own financial plan and will also tell you what a financial planner can do for you, how to find a good planner, and how to best work with that person when your search is successful. If you're a planner, it's my hope that this book will serve as a kind of mentor, showing you my thinking on a variety of issues, including what good financial planning entails.

If you already have insurance, an estate plan, investments, tax planning, a college fund, or a pension, you might think that your financial plan is already set. Think again. What you have isn't a financial plan. A good financial plan incorporates everything you already have and adds an objective evaluation of your current financial picture, your goals, and what it will take for you to achieve those goals. Pull all these things together in an organized way, and you have a financial plan.

A financial plan helps you understand what you have now, where you want to be, and how you will get there. It's personal, designed to map an individual path between your current position and your unique end goal. It's not your neighbor's retirement plan or one created by a computer algorithm.

Follow the lessons in this book, and you will learn to manage your money and your life so that eventually you can attain financial independence. Working will be an option for you—not a requirement.

How Does This Relate to Investing?

Financial planning is more than investing. Many people believe that choosing the right investments will put them on the proverbial Easy Street. But this isn't usually the way things work out. Most people react to each financial event, instead of planning ahead for their whole financial future. When they hear a hot stock tip, they buy stocks. When they hear gold is going up, they buy gold. But they never consider which investments will help them achieve financial freedom and when and how to buy. You will learn a step-by-step process for setting up an investing plan, as well as how to avoid common investment mistakes.

Are You Meeting Your Goals?

Throughout this book, I explode some myths about money, taxes, insurance, and investments, reminding you that taxes, rates of return, and other details are just that: details. It's easy to let them become short-term distractions from your long-term goal. You don't win this game by paying the least in taxes or getting the best return on your investments. You win by reaching your goal.

Let's say your goal is to save \$1 million in the next 10 years. The first year, you put \$100,000 in your savings account. The second year, you put \$100,000 under the mattress. The third year, you hide \$100,000 in the closet. Every year for 10 years, you put aside \$100,000. At the end of 10 years, you've met your goal—and where you stashed the money, how much return you earned on it, or what taxes you paid on it don't matter very much.

Working through the financial planning process helps you find the money you need to meet your goals. When you have both goals and a financial plan, you will know when:

- You don't have enough money, and you must revise your goal or reach it later than you'd hoped.
- Or you have enough or more than enough money and can reach your goal on time or sooner than you'd planned.

You may not like what you discover. Your goals may have to change. But you'll know where you stand—and where you stand may be within reach of surprisingly high achievements.

Obstacles to Reaching Financial Goals

Along the way, you'll learn more about the obstacles that prevent many people from reaching their financial goals: taxes, inflation, death and disability, lack of a plan, ego, and leakage.

Federal and state taxes are said to be one of life's two certainties, and they're nearly always on the rise. Fortunately, there are ways to minimize the taxes you pay.

Inflation eats away at income. Those who don't plan for it can end up with less than they need. Inflation is one of the villains that can get people into financial trouble before they realize it. Even a tiny amount of inflation over time can affect your lifestyle if you don't plan properly. Consistent planning and saving can help you stay ahead of inflation.

Although no one likes to talk about them, death and disability can be devastating to a family that has not planned for these events. You may

have estate plans, and you should have a will. Alone, however, these are not enough. What would your financial situation be if a disability forced you to stop work for months, years, or perhaps the rest of your life?

How would you cope as you watch your car being repossessed? How would you feel if your spouse had to work two jobs? Many find it uncomfortable or even painful to talk or think about these things, but you must. You will learn how to plan for death and disability, giving you a greater sense of security than you have now.

I've already mentioned that many people react to financial events as they happen, instead of creating a unified plan for reaching their goals. Without a plan, you'll have a much lower chance of success.

Ego is the hardest obstacle to overcome. Some people cannot reach their financial goals because their egos get in the way. They buy cars and join clubs to impress people. They live in houses they can't afford. Instead of planning for the future, they keep up with the Joneses today, a decision that keeps them from reaching financial independence. I'll show you what happens if you increase your lifestyle one year too soon. You'll be shocked by the difference one year can make in whether you reach your goals.

Leakage can be a hidden obstacle between you and your financial goals. Leakage happens when you don't reinvest your investment earnings to help you meet your goal. Did you spend your last stock dividend, instead of investing it? That's leakage, and it can really add up over time. If you save \$5,000 a year and earn 10 percent annually, you would earn \$500 the first year. It's so easy to spend that 500 on immediate needs and wants. If you do that, after 20 years you will have the money you put in: \$100,000. But if you reinvest the interest every year, you'll have \$286,375 instead. Are those new clothes or golf clubs worth a difference of more than \$186,000?

Leakage also occurs when you pick an arbitrary dollar amount as a goal, but sabotage your goal by spending part of that money. For example, you think things would be great if you had \$30,000. When you've saved \$30,000, you celebrate with a vacation that costs

\$5,000, leaving you with just \$25,000. You can build back to \$30,000, but a lack of discipline has cost you time and compound interest. To avoid leakage, you must treat the money you are saving and investing as untouchable for any purpose other than your goal. Otherwise, you erode your nest egg. Don't spend the college savings on a new car.

Fuel Your Goals with Income

You know that a financial plan is your road map to financial freedom, and you've seen some of the obstacles in the road ahead. What fuel will get you to your goal? You'll need financial gasoline in the form of your earnings.

The next sentence is one of the most important you'll read in any book about personal finance: **whatever your earnings are, they are.** They aren't any bigger and they aren't any smaller. You must find a way to live within your current financial means.

You can't live now on what you think the future will bring. Maybe you'll get a raise or a bonus next year, or perhaps your business has good prospects. That's great—for the future. It means nothing right now.

It's surprising how many people don't know what they earn, especially if their pay is hourly, seasonal, or includes sporadic bonuses. Nor do they know what they spend, because they don't keep track of their purchases. To make a financial plan, you need to know how much money you need to fund your current lifestyle. If you're married, your spouse must also know how much money comes in and how much goes out in any given month, so you can act as a team.

Communication is key. In many couples, one spouse—often the husband—handles the family finances. When he dies, his wife doesn't know the lawyer or the accountant, isn't aware of the trust fund, and struggles to understand her finances while grieving at the same time. You might think it's difficult to talk about financial matters now.