

# Financial Planning Quarterly

J.P. Collins & Associates, Inc.

Volume 2, Issue 1

## Special points of interest:

- Newsletter published quarterly by J.P. Collins & Associates, Inc.
- Educational newsletter designed to help its readers make better financial decisions
- Articles will cover a broad range of financial topics

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## Broker vs. Advisor

It seems as if every professional in our industry is calling himself/herself a financial advisor (or something similar). For those of you thinking about hiring a financial professional, we thought it would be helpful to look at the two primary types of advisors in the financial services industry: Brokers and Registered Investment Advisors. Here is a brief explanation of their differences:

### Brokers

1. **Compensation:** brokers are typically paid by a commission for the investment products they sell. Some will also charge a percentage of assets that they manage for a client.
2. **Fiduciary Duty:** brokers are required to recommend products to clients that are suitable for their time horizon, risk and goals. Brokers are NOT required to act in a client's best interest and may recommend products that benefit their firm



(high commissions) as long as they are suitable for a client.

3. **Expertise:** brokers are typically required to obtain a securities license (i.e. Series 7, etc) in order to sell investment products for a commission. This exam requires some preparatory time and brokerage firms have their new advisors take the exam after about 2 months studying.

### Registered Investment Advisor (RIA)

1. **Compensation:** RIAs cannot accept commissions for the sale of investment products. Their fees

(i.e. must come directly from their clients. RIAs often charge a percentage of assets they manage, a retainer fee, or hourly consulting fees

2. **Fiduciary Duty:** RIAs must always have the client's best interest in mind when making recommendations. There is a higher level of liability on the part of the RIA when it comes to Fiduciary Duty.
3. **Expertise:** like brokers most RIAs must obtain a license (Series 65) in order to advise clients on financial planning and investments.

We believe that the legal structure of a RIA is more conducive to trust and objectivity, which is the primary reason our firm is structured as such.

Warm Regards,  
-J.P. Collins & Associates

## Simple Truths

Written by J. Patrick Collins Jr., CFP®, EA

Clients often come to us looking for the magic formula for wealth creation. We typically respond with the same answer, "It's not our job to make you rich. Our number one responsibility is to

protect what you currently have and help you grow your wealth to achieve your goals." We believe there are some simple truths when it comes to wealth creation, several of which we have outlined

below:

1. **Save at least 12 percent of your income per year:** spending less than you earn is the cornerstone of wealth creation. Unfortu-

## Simple Truths (cont.)

nately, the savings rate in the United States is currently hovering around zero. The “buy now and pay later” mentality makes it difficult to fulfill this simple truth. For example, a 30 year old who earns \$50,000 per year (with an annual 4% COLA) and saves 12% of his/her income for 35 years will be able to replace approximately 65% of their pre-retirement income at 65 (assumes a 9% return, 4% withdrawal rate, and Social Security Benefits collected at age 65).

2. **Relish Risk:** as you save 12 percent of your income per year, it is important to invest in vehicles that adequately compensate you for the risk you take. The statistics below, taken from a study done by Dimensional Fund Advisors, measures rolling 30 year periods from 1926 to 2004:

Number of Periods	Percentage of Periods Of Outperformance	Results
589	100%	Stocks outperformed bonds
589	86%	Small stocks outperformed large stocks
583	93%	Value stocks outperformed growth stocks

As indicated above, the risk that you take often has a direct correlation with the returns you achieve. Designing an optimal portfolio to manage both risk and return is extremely important in the wealth building phase of your life.

3. **Pay off Debt:** this truth is frequently overlooked since it is not often preached by financial institutions. We find it ironic that credit card companies advertise the freedom you achieve when you can buy what you want, when you want. Unfortunately, the opposite is almost always true. When we meet an individual with high credit card debt, they don't feel free, they feel trapped. Minimizing debt payments is crucial to building long term wealth. A high debt load can create a hindrance on savings for the future. If 40 percent of your income is being used to pay off debt, and 30 percent goes to taxes, it is very unlikely that a family will be able to save 12 percent and have enough left over for regular spending. Families should strive to keep their debt to income ratio (total debt payments divided by gross income) below 25 percent. By doing so, you will not only have additional income to save, but you will limit the interest you are paying to lenders.

While this is not meant to be the magic formula I spoke about in the first paragraph, these simple truths will help you and your family continue to build and create wealth for the long term.

*The author, J. Patrick Collins Jr., CFP, EA, is the President of J.P. Collins & Associates, Inc., a fee-only financial planning and investment management firm, located in Towson, Maryland. The firm specializes in working with business owners, retirees and pre-retirees, and families of children with special needs. Mr. Collins is also a contributing author to The Journal of Special Needs Planning.*



*“Then you will know  
the truth, and the  
truth will set you free”  
-John 8:32 (The Bible)*



## “Stretching” Your IRA

Written by Joshua P. Itzoe

Did you know that your IRA is an excellent estate planning tool that can be used as a wealth transfer vehicle for your loved ones? In planning for the distribution of IRAs after death, a primary goal should be to maximize income tax deferral through the proper use of beneficiary designation forms. While planning for estate tax minimization and deferral at the same time is a constant balancing act, there are strategies available that can dovetail nicely with your overall estate plan. One such strategy that you should consider is a “Stretch IRA.”

The Stretch IRA is not a new type of product that you can buy, but rather a strategy that allows your beneficiaries to take mandatory retirement distributions over their own life lifetime. This can result in a minimization of income taxes due and the ability to keep the money growing tax-deferred for many years and across multiple generations. This strategy works best by named beneficiaries who are younger than the original IRA owner. The younger the beneficiary, the longer the IRA can grow tax-deferred and the greater the potential impact.

### How the Stretch IRA Works

Consider the example of John Smith who will turn 70 ½ this year and has an IRA valued at \$1,000,000 and earning a 7% annual return each year. He names his wife Jane, 67, as primary beneficiary on the account and his daughter Jenny, 37, is named as contingent beneficiary. Due to the pension John receives, he decides to only take the required minimum distributions (RMD) out of his IRA each year to supplement his income. If John dies at age 75 he will have taken a total of \$209,783 in annual distributions from the IRA before income tax. At this point the account is worth \$1,158,436 and Jane rolls this money into her own IRA and names Jenny the primary beneficiary. Jane also only takes annual RMDs until her death at age 82 and receives a total of \$616,102 in RMD income. Upon Jane’s death the account is valued at \$1,457,227 and Jenny, now age 53, inherits the IRA (leaving it in her mother’s name) and begins taking only the minimum distributions based on her own life expectancy of 31.4 years (according to IRS tables). If she continues to do this and the account earns 7% each year, Jenny will be able to withdraw roughly \$5,475,97 over her lifetime from this account!

### A Word of Caution

While it may sound easy to “stretch” your IRA, implementing this strategy is often very difficult because of the complexities that exist within the tax code regarding retirement plan distribution rules. There are a labyrinth of rules and regulations that must be properly understood and followed or the IRA owner could be subject to substantial and often irreversible penalties. Because of the complexities involved it is critical to have competent and knowledgeable advisors set up and monitor these strategies for you.

One last note- it is important to evaluate this strategy and how it affects your overall estate and financial plan before making any changes. Feel free to contact J.P. Collins & Associates to learn more about this and other advanced retirement planning strategies.

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*“A mind once stretched by a new idea, never regains its original dimension..”*

*-Oliver Wendell Holmes Jr.*



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and click on "information  
request."



## What's New

The fourth quarter saw additional expansion at JP Collins & Associates, Inc. On November 1st the firm officially changed its office location to LaSalle Road in Towson, MD enabling the firm to continue its growth. This was evidenced by our new hire, **Irene Catlin** on December 1, 2005. Irene will be serving as the firm's Client Service Manager, and has extensive experience in both the investment management and mortgage banking industry.

The firm's President, **Patrick Collins**, CFP®, EA was quoted on the website [www.bankrate.com](http://www.bankrate.com) with regards to retirement and life planning during the past quarter. Also, Mr. Collins earned the designation of Enrolled Agent from the IRS. An Enrolled Agent (EA) is a federally-authorized tax practitioner who has technical expertise in the field of taxation and who is empowered by the U.S. Department of the Treasury to represent taxpayers before all administrative levels of the Internal Revenue Service for audits, collections, and appeals.

**J.P. Collins & Associates, Inc is a fee-only financial planning and investment management firm located in Towson, Maryland. The firm specializes in working with business owners, retirees and pre-retirees, and families of children with special needs.**

**The firm has extensive knowledge of the issues surrounding financial planning and its advisors are frequent guest lecturers on the topic. The firm's team members hold designations such as the Certified Financial Planner™, NAPFA Registered Financial Advisor, Enrolled Agent and are active within several financial planning organizations like the National Association of Financial Advisors and the Financial Planning Association.**

**Is there an issue or topic you would like to see addressed in  
Financial Planning Quarterly?**

**Email us your ideas and opinions at [info@jpc-associates.com](mailto:info@jpc-associates.com)**

**ALWAYS CONSULT YOUR FINANCIAL PLANNER, ACCOUNT-  
ANT, AND/OR ATTORNEY BEFORE MAKING ANY CHANGES  
THAT MAY EFFECT YOUR FINANCIAL SITUATION**

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