DICKINSON
Investment Advisors

www.dickinsoninvestments.com 712.328.2600

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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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Positive Outlook Continues For The Stock Markets

With the U.S. economy showing signs of self-sustaining growth, the stock market has demonstrated significant strength.

The American economy as measured by gross domestic product (GDP) expanded an impressive 3.2% in the fourth quarter of 2010 and all indications indicate that corporations are making more money.

Inflation has been low, and when combined with low interest rates, businesses are able to thrive. Unemployment is even beginning to ease, although slowly. As more and more consumers enter the workforce, confidence and spending will increase.

With all this good news, investors are finally beginning to trust the stock market and are moving money out of bond funds and into stocks. I agree that bond funds may be in for difficulty when interest rates begin to rise, so this is a wise move if your risk tolerance allows a reallocation.

However, investors should not fall asleep and believe that everything is straight up from here. Remember what I have always said: The stock market predicts what is going to happen in six to twelve months, and occasionally it gets ahead of itself.

So yes, I remain bullish on the near-term outlook, but there will be bumps and uncertainty along the way.

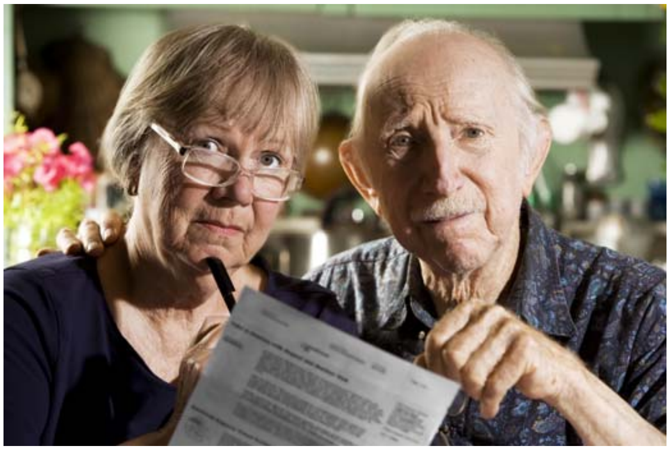
Ron Dickinson

Giving Up Control Over Your Finances

What are your estate planning goals? Chances are, you'd like to maintain control over your assets while you're alive, but you also want to devise a plan that will protect your loved ones if you become disabled. And you intend for your wealth to be distributed when, how, and to whom you want. Finally, you'd like to minimize erosion from federal and state estate and gift taxes.

In other words, you'd like to have your cake and eat it, too. It's possible, but only if you decide to relinquish some control over your financial affairs. And that is often easier said than done. What's difficult is that it's likely to be someone else, not you, who will notice you're beginning to slip a bit. But this is a sensitive issue, and even if your relatives realize that you need help with your finances, they may put off saying anything for years.

To avoid that situation, you may need to establish a system now that won't put any single person on the spot. One solution advocated by Rick Randall, president of the National Network of Estate Planning Attorneys, is to create a "disability panel" with one or more medical professionals along with family members and a financial advisor. The group would observe you and decide when it's time to transfer ownership of assets to a trust or other parties. In some cases, a relative you've given power of attorney might need to initiate legal proceedings to gain control over the assets.



It's crucial to have a doctor involved, Randall says, to provide an expert opinion not only about your current health and cognitive status but also to project that into the future. Family members also play an essential role. They are the ones closest to your situation, and they can help determine when your medical condition and mental health may be deteriorating. And you can choose people you trust to take a compassionate, measured approach. Knowing you've selected these team members may help you accept their judgment even when it goes against your own feelings.

How control will be transferred also needs to be settled well ahead of time, as part of your overall estate planning. And with estate laws currently up in the air, plans and documents may have to be revisited periodically to make sure they conform to the latest laws and strategies. Various kinds of tax-favored trusts are likely to be part of the equation, and you'll probably need to grant a durable power of attorney to someone you trust to act on your behalf.

Though looking ahead to the day when you'll pass the torch is never easy, the benefits can be enormous, and it's important to broach the subject with family members well before your health and competence become issues. We can work with you to establish a plan that meets your needs. ●

Planning For A Child With Special Needs

The daily demands of caring for a child with autism or another developmental disability are daunting enough without worrying about future care. That may be why, in a recent survey, 62% of parents with disabled children said they hadn't established a plan for what would happen when the parents were no longer around. Moreover, about half of the surveyed parents said they planned to leave assets directly to the child, and 58% expected to designate the child as a beneficiary. Those decisions could make the child ineligible to receive public assistance, which could be crucial for the child's long-term welfare.

A better approach may be to create a "special needs trust" that can be funded now or through your will. (The money often comes from life insurance death benefits.) Structured correctly, this irrevocable trust will enable a special needs child to receive public assistance benefits while the trust covers other expenses—including for travel, recreation, and rehabilitation—that aren't fully paid for by government funds.

If the trust assets are used as a primary means of support, the disabled child may be disqualified from public assistance, just as would happen if the child received a direct bequest. To avoid problems, a special needs trust will have an independent trustee who controls distribution of trust assets but uses the money only to supplement government aid. A provision in the trust will typically prevent the trustee from using assets for "support, maintenance, welfare, and education" of the child.

Keep in mind, however, that laws governing trust language and operation may vary from state to state. In some states, for example, assets that remain in the trust after the disabled child's death must be

A System To Always Earn Your Trust

It seems that new revelations about unscrupulous financial planners are practically a daily occurrence. And problems aren't limited to the Bernie Madoffs of the world bilking celebrities and billionaire CEOs. Regular folks, too, have fallen prey to Ponzi schemes and investment scams perpetrated by lower-profile advisors, and it's only natural for you to be apprehensive about your personal investment holdings. Yet while the system for ensuring your safety isn't perfect, it isn't broken either. There are safeguards in place to protect well-informed investors from dire circumstances.

Naturally, you'll have to do some research on your own, but it will be time well spent. Consider these three key areas.

1. Professional background. It's easy enough to do an online background check on a financial advisor. Start with the Financial Industry Regulatory Agency (FINRA) at finra.org. As the largest independent regulator of securities firms in the United States, FINRA oversees almost 5,000 brokerage firms, 173,000 branch offices, and 656,000 registered securities representatives. FINRA's "BrokerCheck" tool will tell you everything you need to know about a particular broker (state registrations, licenses, employment history, etc.) plus any disciplinary actions he or she has faced and the outcome.

For registered investment advisors (RIAs), overseen by the Securities & Exchange Commission (SEC)—generally, these are advisors managing more than $25 million in assets—visit www.adviserinfo.sec.gov to use the "Investment Adviser Search." It profiles the RIA's activities during the past 10 years. Or you can find out more about financial advisors from professional organizations such as the Certified Financial Planner (CFP) Board of Standards at www.cfp.net or the Financial Planning Association (FPA) at www.fpanet.org.

2. Checks and balances. Victims of Bernie Madoff should have been tipped off by a few red flags. Significantly, instead of using a third-party custodian, Madoff's firm held clients' money itself, and investors wrote checks directly to the firm. With a custodian, there's an independent party responsible for accounting for investments, you always know where your assets are, and you can check their status online. A custodian also mails out regular account statements. Of the 11,000 investment advisors registered with the SEC, only 1,000 don't use a custodian.

In addition, Madoff's auditor, on whom investors relied on to verify the authenticity of trades, had only one licensed accountant and was operating out of a storefront. Every state has a database where you can check the credentials of auditors. Also, if you find a firm has switched auditors recently or several times in the past, it could be a signal that something is amiss.

All SEC-registered advisors are required to maintain true, accurate, and current records. Strict supervisory controls also help ensure the integrity of an operation, and an RIA firm should provide you with a service agreement clearly stating how your accounts will be managed.

3. Method of compensation. Financial advisors get paid in a variety of ways. Some receive commissions on securities sales, others charge fees (either a flat rate or based on a percentage of assets they manage), still others have hourly rates, and some use a combination of methods. Make sure you know how you'll compensate an advisor, and be wary if there's any reluctance to provide details. Law requires explicit disclosure of compensation and, if it is based on assets under management, you must be informed of the amount and the calculation prior to it being deducted from your account. RIAs are required by law to disclose all conflicts of interest. However, that rule often doesn't apply to other advisors, and if they work on a commission basis, their firm could reward them for recommending particular products or services. Among advisors charging fees based on a percentage of assets, manipulation may be subtler, but very high rates—more than 2% of assets—should set off alarms.

Our commitment. It is understandable that many investors remain fearful about the security of their investments. Our firm embraces a transparent system of doing business, and we want to do everything we can to reassure you. If you don't understand something on your statement or have any concerns about your investments, please do not hesitate to call.

In our fiduciary capacity, we are legally bound to put clients first, and sharing this information with you is just one of the ways we meet that obligation. You can remain confident that we will represent you to the best of our abilities and with your best interests in mind. ●

used to pay back the government for public assistance benefits. But that provision doesn't limit the trust's ability to help a living child.

A special needs trust, like any other estate planning vehicle, needs to be part of an overall estate plan. One wrinkle here is that money you move into this kind of trust doesn't qualify for the annual gift tax exclusion ($13,000 in 2011) that otherwise limits tax liability on yearly gifts to individuals. Because of restrictions in the trust language of special needs trusts, transfers are classified as gifts of "future interest." That means parents who fund such a trust during their lifetimes will need to use all or part of their $5 million lifetime gift tax exclusion. As a result, asset transfers to other children may be more costly.

Good advice from experienced experts can make sure your special needs trust accomplishes its goals without shortchanging other family members. We can work with your attorney to help you establish a trust that protects everyone's interests. ●

Ups And Downs Of Caregiver Agreements

In 2009, an estimated 66 million Americans provided more than $400 billion worth of unpaid care to elderly parents and other loved ones, according to AARP. As the economy continues to struggle and family budgets tighten, an increasing number of those caregivers are accepting pay for their efforts, most often from an aging parent.

There is a right way and a wrong way to do this, says Linda Fodrini-Johnson, a geriatric care consultant in the San Francisco Bay Area and president-elect of the National Association of Professional Geriatric Care Managers. The right way is to draw up a written caregiver agreement, a formal contract that makes it clear what a caregiver is expected to do, how much he or she will be paid, and other details of the relationship. A well-drafted agreement can help elderly parents remain in their homes while keeping family strife to a minimum, says Fodrini-Johnson. Meanwhile, the caregiver receives extra income and the parent's estate is reduced, minimizing potential estate taxes.

But not every contract will provide such benefits. "Consult an attorney to make sure this is a binding agreement that would hold up in court," suggests Fodrini-Johnson. "If it looks like you're trying to spend down assets or bypass legitimate taxes, you could be breaking the law."

Caregiver agreements cover what the caregiver is expected to do (from cooking and cleaning to helping the person dress and bathe), how much time it will take to do these tasks, the rate of pay, and how often payments will be made. If a family has multiple siblings, each of them should sign the agreement, especially if only one is providing the care. The caregiver is responsible for federal and state taxes due on the income, and the rate of pay must be in line with standard rates for similar work in the area.

But no agreement, however carefully drafted, will succeed if the parties to it aren't comfortable with the caregiving arrangement, says Fodrini-Johnson, who points to several potential problems.

- Someone who provides care out of guilt or an inability to say no will most likely fail to provide adequate care.
- Similarly, a reluctant caregiver doing it only for the money probably won't be successful. "You have to really like people and love elders," she says. "Emotional abuse can happen if you're not happy to be there."
- A caregiver may begin to feel guilty about accepting money from a family member.
- Making this a paid relationship may change the tenor of the connection between parent and child.

We can help your family avoid these pitfalls by setting up a caregiver agreement that takes into account all of the complex financial and emotional aspects of your situation. And if you're in your 50s or 60s, purchasing long-term care insurance now could go a long way in helping to avoid this situation. Please give us a call if you'd like to discuss the possibilities. ●

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. ●