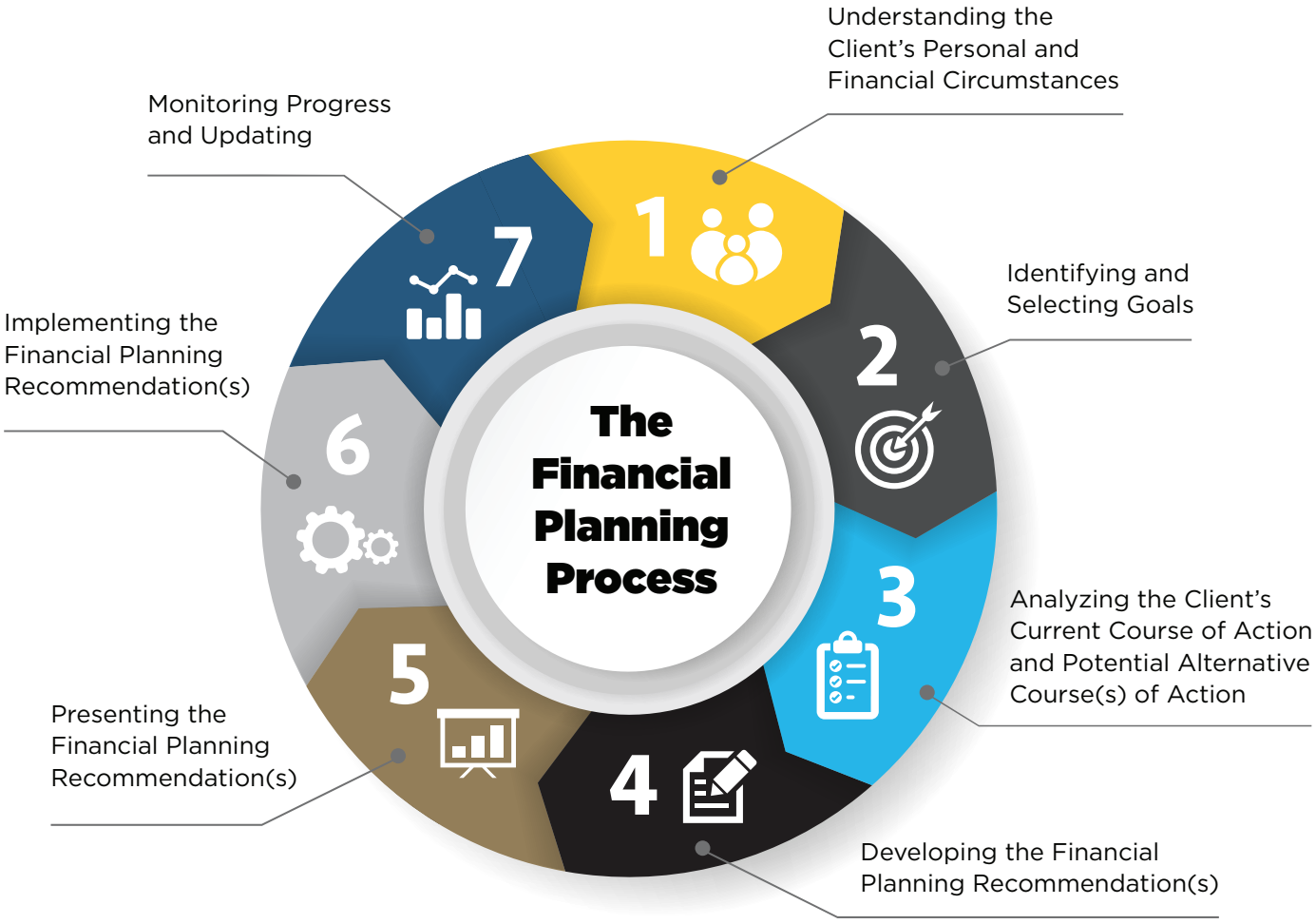
CFP BOARD

GUIDE TO THE 7-STEP FINANCIAL PLANNING PROCESS

A CASE STUDY ILLUSTRATION FOR SOLO PRACTITIONERS

CFP Board developed this Guide to the *Practice Standards for the Financial Planning Process* to illustrate how a CFP® professional might provide financial planning to a Client in accordance with the *Code of Ethics and Standards of Conduct*. This guide presents a hypothetical circumstance and then applies the *Practice Standards* to that circumstance. The guide does not set forth the only way to apply the *Practice Standards* to the hypothetical circumstance. There is more than one way that a CFP® professional might exercise professional judgment to satisfy the *Practice Standards*.

7 Steps: The Financial Planning Process



Joe, a CFP® professional, is a solo practitioner at an independent Registered Investment Adviser. He meets with Martha and Dan Miller. One of their friends recommended that they engage Joe's firm for financial planning. They agree to a Scope of Engagement for financial planning that includes all seven steps of the financial planning process.

The Millers provide Joe information about their personal and financial circumstances. Joe tells the Millers more about his practice and his firm. Joe prepares and provides to the Millers an Engagement Letter and Advisory Agreement that describe:

Engagement Letter and Advisory Agreement	The services and products to be provided;
	How the Millers will pay for services and products, and the additional types of costs that they may incur;
	How Joe and his firm are compensated for providing the services and products; and
	The terms of the Engagement, including a Scope of Engagement and any limitations, the period(s) during which the services will be provided, and the Millers' responsibilities.

The Millers agree to the terms of the Engagement and sign the Advisory Agreement. Joe also provides his firm's written Privacy Policy and the firm's Form ADV Part 2A, 2B, and 3 (Form CRS), which describe material conflicts of interest, referral compensation agreements, and other material information. At an appropriate time during the Engagement, Joe will have the Millers sign several documents, including an account opening form for a custodial account and an investment policy statement.

Joe then schedules a follow-up meeting with the Millers to provide financial planning.

STEP 1

UNDERSTANDING THE CLIENT'S PERSONAL AND FINANCIAL CIRCUMSTANCES

The CFP® professional must:

- Obtain Quantitative and Qualitative Information
- Analyze Information
- Address Incomplete Information

Joe wants to learn more about Martha and Dan's personal and financial circumstances, so he begins by asking questions and listening intently. Joe explains that he will provide a form that asks for more information about them. Through the information requested on that form and a series of questions that Joe asks the Millers during both in-person and telephonic meetings, Joe seeks to obtain several categories of qualitative and quantitative information to fulfill the Scope of Engagement:

Examples of Qualitative or Subjective Information

- Health
- Life expectancy
- Family circumstances
- Values
- Attitudes
- Expectations
- Earnings potential
- Risk tolerance
- Goals
- Needs
- Priorities
- Current course of action

Examples of Quantitative or Objective Information

- Age
- Dependents
- Other professional advisors
- Income
- Expenses
- Cash flow
- Savings
- Assets
- Liabilities
- Available resources
- Liquidity
- Taxes
- Employee benefits
- Government benefits
- Insurance coverage
- Estate plans
- Capacity for risk
- Education and retirement accounts and benefits

Joe provides a list of documents he needs from the Millers to fulfill the Scope of Engagement, including tax returns, details of their employer benefit programs, insurance policies, loan and mortgage statements, and estate planning documents. In addition, Joe and the Millers agree that any potential future inheritance is uncertain and thus will not be addressed in the financial planning recommendations.

After the Millers provide Joe the completed form and the requested documents, Joe asks follow-up questions to confirm that he has complete and accurate information.

Age, Income, Dependents

Martha and Dan Miller are both 32 years old. They both have secure jobs, with annual salaries of $120,000 and $110,000, respectively. The Millers recently had a daughter named Emily. They have no other dependents, and they have no plans for additional children.

Savings, Assets, Liabilities, Education and Retirement Accounts

Many years ago, the Millers opened a savings account to save money for a rainy day. They were late, however, in making contributions to their 401(k) plan accounts. In their late 20s they realized that they could "earn" additional money by taking advantage of their companies' matching contributions, so they started making contributions to their 401(k) plan accounts. Now they make enough money to pay their expenses and contribute to savings, with enough money left over for vacations.

The Millers have a low-yield savings account with a balance of $70,000 that they currently use for college savings and emergencies. They want to keep a $30,000 emergency fund and are interested in investing $30,000 to earn funds that they may use to purchase a lake cabin. The remaining $10,000 is earmarked for Emily's college savings.

The Millers' current market home value is $300,000 and they have $60,000 of equity in their home, a small portion of which is protected by state law from the claims of creditors. The interest rate on their existing mortgage is high compared to current market rates. They own two cars without loans, both of which are relatively new and reliable. They carry their state's minimum levels of liability protection on their cars. Aside from their $240,000 of mortgage debt, on which they are making regular payments, they have no other material outstanding liabilities.

Martha has accumulated $80,000 in her 401(k) plan account and Dan has accumulated $70,000 in his 401(k) plan account. They also have a taxable investment account valued at $10,000 that they established with the $8,000 they received from their wedding. The mutual fund investments in the taxable investment account have higher-than-average expense ratios and have not been tax efficient. The allocation in their retirement and taxable investment accounts is 50% equities and 50% fixed income.

Expenses, Cash Flow, Liquidity

Dan and Martha recently paid off their student loans. While paying off student loans, Dan and Martha limited contributions to their 401(k) plan accounts to $13,800 to obtain the employer match, which is 6%. With the student loans paid off, they recently have increased their contributions to 10% of their salaries, or approximately $23,000, to their respective 401(k) plan accounts.

They are contributing $12,600 annually to the low-yield savings account.

Taking into account additional fixed expenses (mortgage, property taxes, utilities, food, clothing and cleaning, income taxes, transportation, health and other insurances, household supplies and maintenance) and variable expenses (vacations, travel, recreation and entertainment, gifts and charitable donations, and household furnishings), the Millers now have $34,500 in unallocated cash flow each year.

The Millers use their credit cards to pay for most of their expenditures because they want to take advantage of the credit card reward program, but they pay off their credit card bills each month in full and have an excellent credit rating.

The Millers have sufficient cash to cover at least six months' worth of living expenses.

Taxes, Government Benefits

The Millers file their own taxes as "Married Filing Jointly" and are in the 24% marginal tax bracket based on their combined incomes. Because Dan and Martha have employer-sponsored health insurance plans, they do not need to utilize government health insurance options. The Millers provide Joe their most recent Social Security benefit statements.

Insurance, Employee Benefits

Their employers match 6% of their salaries for a $13,800 employer contribution. The Millers each have employer-provided life insurance coverage that is equal to two times their salaries (Martha has $240,000 in coverage and Dan has $220,000). They each also have employer-provided health insurance that provides reasonable coverage. Martha has both short-term and long-term disability insurance coverage through her employer, but Dan only has short-term coverage in place through his employer.

Estate Plans

The Millers have yet to create any estate planning documents. They believe, but are not sure, that they have designated each other as beneficiary on their life insurance policies and listed their daughter as the contingent beneficiary. They established their 401(k) plan accounts before getting married and believe they still have other relatives designated as beneficiaries on their retirement plans.

Millers' Current Annual Personal Balance Sheet and Cash Flow Report

Assets		Liabilities	
Taxable Investment Account	$10,000	Mortgage Debt	$240,000
Current Market Home Value	$300,000		
Low-Yield Savings Account	$70,000		
401(k) - Martha	$80,000		
401(k) - Dan	$70,000		
Net Worth			
Total Assets	$530,000	Total Liabilities	$240,000
Net Worth	$290,000		

Income		Expenses	
Martha's Income	$120,000	Fixed Expenses	
Dan's Income	$110,000	Income Taxes	$48,000
		Mortgage	$15,000
		Health and Other Insurances	$15,000
		Utilities and Household Maintenance	$11,900
		Food and Clothing	$10,000
		Transportation	$10,000
		Variable Expenses	
		Vacations and Travel	$15,000
		Recreation and Entertainment	$20,000
		Gifts and Charitable Donations	$15,000
		Low-Yield Savings Account Contributions	$12,600
		401(k) Contributions	$23,000
Cash Flow			
Total Income	$230,000	Total Expenses	$195,500
Unallocated Cash Flow	$34,500		

Health, Life Expectancy, Family Circumstances, Available Resources

Dan and Martha and their family members—including their parents and siblings—are healthy. With some exceptions, most of Martha's family lives into their 90s. Her grandparents are alive and in their 80s and have the assets needed to pay to live in an assisted living facility. Dan's grandparents passed away in their early 80s, which is common in his family. His parents are in their late 50s and still are working. The Millers have no other available resources.

Earnings Potential, Risk Tolerance, Capacity for Risk

Both Dan and Martha have successful careers and they work at large companies with opportunity for advancement. Martha hopes to receive a promotion in the next couple of years and, if so, she would receive a commensurate increase in her salary. Dan recently was promoted and does not expect to receive another material promotion for at least five years, or perhaps longer. Martha is concerned that if either one was to lose their jobs that this would negatively affect their earnings potential.

PRACTITIONER'S NOTE

Joe assesses the Millers' risk tolerance, capacity for risk, and how they perceive risk. Joe's initial analysis shows that if the Millers do not take on additional risk, they likely will not be able to meet their goals.

Joe takes the Millers through a risk tolerance process and asks several questions to properly assess their risk profile. This includes their (a) risk tolerance (the willingness to pursue an uncertain positive outcome, with the potential that a negative outcome could result instead); (b) capacity for risk (the financial ability to endure a potential financial loss; and still be able to achieve their goals); and (c) perceived risk (the perception of risk of the market and their own investments). Joe's questions also are designed to assess the Millers' time horizon, available assets, and need for income, along with Dan and Martha's willingness to sustain market volatility and maintain a comfort level with staying invested through a market decline.

Dan and Martha have near-term and mid-term goals that they would like to achieve on the way to their retirement in 35 years. The Millers do not have a current need for investment income; instead, they use their investment income to fund their future goals. While both Dan and Martha are cautious, both are willing to take on more risk to increase their potential return. Dan and Martha tell Joe that they are long-term investors and that, during previous market downturns, they did not make any investment changes, even though the value of their portfolio fell in the short term.

Values, Attitudes, Expectations

The Millers are savers. Their parents taught them that it is important to prepare for tomorrow. They expect to do well in their careers and are very positive about the future. They believe in protecting themselves in the event of an emergency, but they also want to take advantage of life's opportunities.

Reported Goals, Needs, Priorities

The Millers explain their current goals, needs, and priorities for the near term, the mid term, and the long term:

Near Term	Mid Term	Long Term
Save to purchase a $150,000 lake cabin, with no mortgage, within the next decade.	**Send Emily to an elite private university (current estimated annual cost of $71,000) without student loans.**	**Retire at age 67.**

The lake cabin seems particularly important to the Millers because Dan and Martha met at a lake community during their summer vacations when they were younger.

Other Professional Advisors

The Millers do not work with a financial advisor. Dan and Martha have a property and casualty insurance agent, but they do not have a pre-existing relationship with a CPA, attorney, or life insurance agent.

Address Incomplete Information

The Millers are not sure who they listed as beneficiaries on their 401(k) plan accounts and life insurance policies. Joe asks the Millers to review the beneficiary election forms or go online and obtain that information.

Joe also requests that the Millers provide information about the additional costs they expect to incur when they purchase the lake cabin, including annual costs for property taxes, insurance, utilities, and ongoing maintenance. The Millers have a good understanding of the initial cost of the lake cabin, but they had not considered these ongoing costs.

Joe documents the Millers' information in his firm's Client record-keeping system (his firm uses customer relationship management and financial planning software).

Now that Joe has obtained sufficient information to assess the Millers' personal and financial circumstances, Joe will use the information gathered to identify and select goals, analyze the Millers' current course of action and potential alternatives, and develop, present, and implement the financial planning recommendations.

PRACTITIONER'S NOTE

The Millers call Joe a week after their meeting to provide additional information. Joe adds this information to his Client record-keeping system.

STEP 2

IDENTIFYING AND SELECTING GOALS

The CFP® professional must:

- Identify potential goals
- Help the Clients select and prioritize goals

The Millers raised three goals during their initial meeting with Joe:

(1) Saving to purchase a lake cabin, with no mortgage, within the next decade;

(2) Sending Emily to an elite private university without student loans; and

(3) Retiring at age 67.

Following the initial meeting, Joe analyzes the information that he obtained from the Millers and applies reasonable assumptions and estimates, including life expectancy, inflation rates, tax rates, and investment returns. Joe initially determines that 67 is an appropriate retirement age, assuming that their longevity is consistent with their family longevity and personal health.

Joe's analysis also reflects that the Millers do not have adequate insurance coverage and do not have an estate plan. He schedules another meeting with the Millers to help them identify additional goals, including:

(1) Ensuring adequate insurance coverage for Dan and Martha; and

(2) Creating an estate plan that appropriately documents their wishes for the distribution of their assets and their wishes for Emily's care.

Joe and the Millers review and discuss this expanded list of goals. The Millers agree that the list is accurate, but they tell Joe that after some discussion, they now have decided that they would like to acquire the lake cabin in six years so that they will have more time to enjoy it.

PRACTITIONER'S NOTE

Joe notes the impact that selecting the goal of acquiring the cabin in six years might have on their other goals, including accumulating retirement assets and saving for Emily's college education. He emphasizes that without some adjustments, the goal of purchasing the lake cabin for cash in six years may be unrealistic. Joe also notes that choosing a higher-priced college for Emily will have a negative effect on their other goals. The Millers, however, are adamant that Emily attend an elite private university at a higher cost.

Based upon the discussion above, Joe identifies an expanded list of goals:

	Accumulate adequate retirement assets to retire at age 67 and live a comfortable life during retirement.
	Acquire a cabin at the lake within approximately six years to create lasting memories and friendships.
	Ensure that the Millers have adequate insurance coverage.
	Create an estate plan that appropriately documents their wishes related to the distribution of their assets and care for Emily and updates their beneficiary designations.
	Accumulate assets to cover four years of elite private university costs for Emily.

The Millers agree with Joe's expanded list of goals, and they work with Joe to develop the following prioritization:

1. **Ensure that the Millers have adequate insurance coverage.**
2. **Create an estate plan that appropriately documents their wishes related to the distribution of their assets, care for Emily, and updates to their beneficiary designations.**
3. **Acquire a cabin at the lake within approximately six years to create lasting memories and friendships.**
4. **Accumulate assets to cover four years of elite private university costs for Emily.**
5. **Accumulate adequate retirement assets to retire at age 67 and live a comfortable life during retirement.**

STEP 3

ANALYZING THE CLIENT'S CURRENT COURSE OF ACTION AND POTENTIAL ALTERNATIVE COURSE(S) OF ACTION

The CFP® professional must:

- Analyze the Clients' current course of action
- Analyze potential alternative courses of action

Joe analyzes whether the Millers' current course of action maximizes the potential for them to meet their goals.

Joe identifies advantages of their current course of action. The Millers:

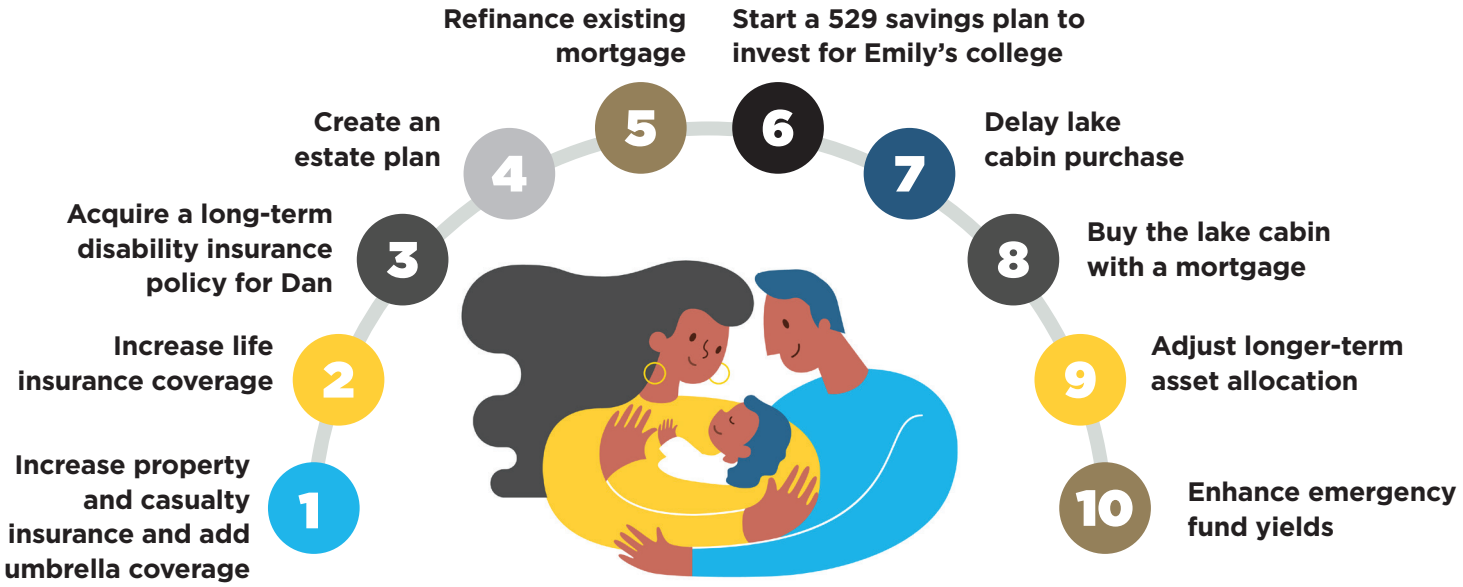
☐ Have a cash reserve in the event of an emergency.	☐ Do not have significant liabilities and have no credit card debt.
☐ Are contributing approximately 15.5% of their gross income annually to a savings account and to their 401(k) plan accounts (does not include employer match).	☐ Have some insurance coverage (Martha's short- and long-term disability policies though her employer, Dan's short-term disability through his employer, and Martha and Dan's life insurance policies through their employers.
☐ Are building equity in their home.	☐ Have established an excellent credit rating.

Joe identifies disadvantages of their current course of action and potential opportunities. The Millers:

☐ Should be allocating their assets in alignment with their risk tolerance.	☐ Have an interest rate on their existing mortgage that is high compared to current market rates.
☐ Have mutual fund investments that have high costs and are not tax-efficient.	☐ Are using a low-interest savings account with taxable interest for college savings.
☐ Do not have adequate insurance coverage (Dan and Martha lack appropriate liability and life insurance coverage and Dan lacks long-term disability coverage).	☐ Have no estate planning documents and have outdated beneficiary designations on their retirement accounts and life insurance policies.
☐ Are not planning for the additional costs of owning a second home, such as property taxes, insurance, and maintenance costs.	

Joe's analysis of the Millers' current course shows a low probability of meeting all their targeted goals.

Joe analyzes potential alternative courses of action, each of which helps maximize the potential for the Millers to meet their goals and integrates the relevant elements of the Millers' personal and financial circumstances. Joe also identifies some of the advantages and disadvantages, which he will analyze further when developing the recommendations.



1

Increase property and casualty insurance and add umbrella coverage.

Advantages:

- Reduces the risk of large outlays to pay for a casualty event.

Disadvantages:

- Increases their costs and reduces money that could be used for other purposes.

2

Increase life insurance coverage.

Advantages:

- Provides additional resources, such as income replacement for lost wages, for the surviving spouse to help in meeting financial goals.
- Reduces the risk of not being able to obtain, or paying substantially higher costs for, life insurance coverage in the future.
- Provides adequate resources for Emily's future needs if both Dan and Martha pass away.

Disadvantages:

- Increases their costs and reduces money that could be used for other purposes.

3

Acquire a long-term disability insurance policy for Dan.

Advantages:

• Provides income replacement for Dan's lost income if he suffered a disability.

Disadvantages:

• Increases their costs and reduces money that could be used for other purposes.

4

Create an estate plan.

Advantages:

• Increases the likelihood that their wishes for the distribution of their assets and care for Emily will occur should they pass away or become incapacitated.

• Reduces the uncertainty that will result in the management of their affairs upon their death or incapacity.

Disadvantages:

• Increases their costs and reduces money that could be used for other purposes.

5

Refinance existing mortgage.

Advantages:

• A lower interest rate will decrease costs and increase cash flow.

Disadvantages:

• The lender may charge closing costs to refinance the mortgage that increases their costs and reduces money that could be used for other purposes.

6

Start a 529 savings plan to invest for Emily's college.

Advantages:

• Contributions grow tax deferred.

• Distributions for eligible education expenses are not taxed.

• State may offer tax benefits for contributions.

Disadvantages:

• Distributions of earnings that Emily or other family members do not use for qualified education purposes will be subject to income taxes and a 10% penalty.

7

Delay the lake cabin purchase by a year or two (or longer) to decrease the annual savings required to accumulate sufficient assets to purchase the lake cabin.

Advantages:

• Increases discretionary cash flow for current spending.

Disadvantages:

• Lake cabin savings will likely be invested conservatively due to the short-term time horizon to purchase the cabin.

• One less year (or more) to enjoy the property.

• Lake cabin prices may increase during this period.

8 **Buy the lake cabin with a mortgage.**

Advantages:

- The mortgage interest deduction may reduce their tax obligation.
- They may purchase the lake cabin sooner and enjoy the cabin for more time.
- The Millers could utilize the equity in their home for college or retirement planning.

Disadvantages:

- The increased costs may require them to delay other goals.

9 **Adjust their longer-term investment allocation in their retirement plans and college savings to provide for more growth potential. Joe would base all asset allocations upon the Millers' Investment Policy Statement that reflects their tolerance for risk.**

Advantages:

- Increased probability of reaching their goals due to having higher expected average returns.

Disadvantages:

- Increased growth exposure adds the potential for increased volatility and lower or negative returns.

10 **Enhance their emergency fund yields by moving the funds in their savings account to a higher-yielding FDIC or NCUA-insured savings or money market account.**

Advantages:

- Increased probability of reaching their goals due to earning higher interest yield.
- Protects emergency funds in the event their financial institution fails.

Disadvantages:

- The Millers may need to switch banks to find the appropriate account for their needs.

STEP 4

DEVELOPING THE FINANCIAL PLANNING RECOMMENDATION(S)

For each recommendation, the CFP® professional must consider:

- Assumptions and estimates used to develop the recommendations
- Basis for making the recommendation
- Timing and priority of the recommendation
- Whether the recommendation is independent or must be implemented with another recommendation

Joe speaks with the Millers over video conference to clarify some facts about their insurance coverages, confirm that he has full and complete financial information, and confirm that the goals and priorities established in Step 2 accurately represent the Millers' values and wishes. Joe also engages in a quantitative review, which includes financial modeling and time value of money calculations, and applies reasonable assumptions for life expectancy, inflation rates, tax rates, and investment returns. Joe explains to the Millers these assumptions and calculations.

Joe develops recommendations designed to help maximize the potential that the Millers will meet their goals. Joe concludes that the recommendations are independent and do not need to be implemented with other recommendations. Joe's recommendations, and the timing and priority of the recommendations, are as follows:

1. **Manage risk by increasing the liability protection on their property and casualty insurance policies—within one month.**

   a. The Millers may obtain insurance to protect against risks of events that do not occur frequently but may result in high costs that negatively affect the potential to meet long-term goals. The Millers' home and cars present such risks.

   b. Joe recommends that they incur a known expense—the insurance premium—to protect against the risk of harm to their home or cars that may result in unknown but potentially large expenditures.

   c. Joe does not recommend an umbrella policy at this time due to their current net worth and risk profile, but an umbrella policy may be appropriate in the future.

2. **Increase Dan and Martha's life insurance coverages by purchasing cost-effective individual life insurance policies in an amount determined by Joe's life insurance needs analysis—within one month.**

   a. Joe recommends that the Millers obtain life insurance that matches the term for which the insurance is needed to protect against the negative financial consequences of death, including a loss of income and additional expenses.

3

b. Life insurance provides the surviving spouse a pool of funds that may be used to provide for the deceased spouse's final expenses, the surviving spouse's ongoing living expenses, and savings that may be used to achieve financial goals. Without these resources, the surviving spouse may not be able to meet his or her goals within the desired time frames.

c. The Millers will have greater confidence knowing that if a death occurs the family will have resources available to meet their needs.

d. A disadvantage is the reduced cash flow resulting from the cost of ongoing insurance premiums.

4

Obtain long-term disability insurance for Dan—one to three months.

a. The Millers are at risk of Dan becoming disabled and unable to work.

b. Joe recommends that Dan obtain long-term disability insurance through his employer or a third party to secure income replacement for Dan's lost income if he suffers a disability.

c. The insurance proceeds would enable the Millers to pay for everyday expenses and invest for the future even if Dan becomes disabled.

d. A disadvantage is the reduced cash flow resulting from the cost of ongoing insurance premiums.

5

Refinance existing mortgage to take advantage of current low interest rates and increase cash flow—within one month.

a. The Millers may refinance their existing mortgage to obtain a lower interest rate, which would result in lower monthly mortgage payments.

b. By reducing the annual fixed cost of the mortgage on their home, the Millers would have additional monthly cash flow to save toward their goals and accommodate increased risk management costs.

c. The lender may charge closing costs for the refinance. However, with the savings that the Millers would achieve over time, the Millers would "break even" not long after refinancing.

d. Joe recommends that the Millers speak with a mortgage professional as soon as possible to "lock in" a low rate and offers to review the mortgage quote and mortgage application forms.

6

Work with an estate planning attorney to create estate planning documents and update outdated beneficiary designations on retirement and life insurance accounts —one to three months.

a. The lack of an estate plan may hinder the Millers' ability to meet their long-term goals in the event of the death or incapacity of either spouse.

b. An estate plan should help to make assets available to a surviving spouse and then pass as intended, in an appropriate way, to provide for Emily's needs should Dan and Martha both die prematurely.

c. An estate plan should help avoid unnecessary costs, delays, and ambiguity in the administration of their affairs upon their deaths or incapacities.

7

d. Joe recommends that the Millers work with an estate planning attorney to create estate planning documents, and he provides a list of issues that they should address, such as a potential trust, guardianship of Emily, and plans for how their estate will be divided. He also offers to help provide financial information their attorney may require.

e. The Millers will need to update their beneficiary designations, as they are outdated and may not reflect their intended beneficiaries.

f. A disadvantage of developing an estate plan is the large up-front cost to hire an estate planning attorney. Joe recommends that the Millers budget for these costs. To save on legal costs, Joe also recommends that the Millers discuss their estate planning issues prior to engaging the estate planning attorney and involve other family members or friends in their pre-meeting planning, as appropriate.

8

Adjust the asset allocation of their investment selections across accounts to better match their risk tolerances and targeted retirement dates by increasing equity exposure and reducing fixed income exposure—three months.

a. The Millers' taxable account investments have higher than average expense ratios and have not been tax-efficient. Therefore, Joe recommends reallocating to funds that have lower costs and are more tax-efficient.

b. Joe recommends that the Millers invest a greater percentage of their assets in equities to better match their risk tolerances and targeted retirement dates and provide increased opportunities for growth in asset values.

c. Joe makes investment return assumptions given the targeted asset allocation and the Millers' investment time horizon.

d. Joe anticipates selecting equity funds with lower expense ratios that should result in the Millers' investments being more tax-efficient and earning higher expected average returns, which should increase the probability of the Millers' meeting their financial goals.

e. A negative effect of increasing equity exposure and decreasing fixed income exposure is an increase in current market volatility and risk of lower or negative returns. Joe concludes that the Millers have both the risk tolerance and the risk capacity to accept this risk.

9

Increase their current savings rate and invest the savings in a taxable investment account to allow for the additional savings needed to meet the lake cabin funding goal —three months.

a. Joe recommends that the Millers increase their annual lake cabin fund contribution from $12,600 to $20,000 and invest the funds in a conservative blend of fixed income and equity investments that is appropriate for the six-year time horizon.

b. Joe anticipates that by increasing their savings for the lake cabin, the Millers will maximize the potential to reach their goal within the six-year desired time frame.

c. A negative effect of this additional savings is less cash flow. However, without these additional resources, the Millers significantly decrease the potential to purchase the lake cabin within the desired time frame.

10

Increase their current savings rate and invest the savings in a 529 savings plan to allow for the additional savings needed to meet the college funding goal—three months.

a. Joe recommends that the Millers open a 529 savings plan account for Emily's college education, fund the plan with the current $10,000 college savings in the low-yield savings account in the first year and $15,000 every year thereafter, and adopt an initial aggressive allocation for the underlying investments due to the 17-year time horizon until college. Thereafter, based upon the Investment Policy Statement that reflects Dan and Martha's risk tolerance, Joe recommends that the Millers gradually adopt a more conservative investment allocation as Emily gets closer to college age.

b. The 529 savings plan contributions will grow tax deferred, and qualified distributions can be free from federal and state taxes in the Millers' current state of residence.

c. Joe will determine if the Millers' state of residence offers residents tax benefits on contributions to 529 savings plans.

d. Unlike the current savings account, the 529 savings plan will allow the Millers to earn compound interest on their investment and longer-term market growth, increasing the likelihood of having adequate value accumulated in the 529 savings plan to fund Emily's elite private college without student loans.

e. A negative effect of the 529 savings plan contributions is that the distributions of earnings that are not used on qualified education purposes are subject to income taxes and a 10% penalty. However, Joe and the Millers determine that the benefits of the 529 savings plan outweigh this risk.

11

Accumulate adequate retirement assets to retire at age 67—in parallel with other goals.

a. After they have accumulated the required savings for Emily's college expenses, Joe recommends that the Millers maximize their contributions to their respective 401(k) plan accounts and continue making those maximum contributions through the end of their work careers. Joe notes that if they receive salary increases or promotions before they maximize their retirement contributions, they should increase their retirement contributions by the same percentage to increase the amount that will be contributed to their 401(k) plan accounts.

b. Joe anticipates that by increasing their 401(k) plan account contributions, the Millers will maximize the potential to reach their goal of accumulating adequate retirement assets to retire at age 67, assuming that their longevity is consistent with their family longevity and they continue to have good health.

c. A negative effect of increasing retirement savings is that the Millers will have less cash flow. However, without these additional retirement resources, the Millers significantly decrease the potential to reach their goal of retiring at age 67.

12 **Enhance their emergency fund yields by moving the funds in their savings account to a higher-yielding FDIC or NCUA-insured savings or money market account—three months.**

a. Joe recommends that the Millers place their savings in a higher-yielding account that is insured. This will provide the Millers with greater wealth accumulation while maintaining a conservative savings approach.

b. This change will increase the likelihood that the Millers will have adequate savings accumulated to meet their goals. Moreover, the savings will be insured against loss if the financial institution fails.

Joe uses his financial planning software to develop his recommendations, including on the Millers' current financial circumstances and the potential outcomes that might result from different actions. For each recommendation, Joe considers the assumptions and estimates used to develop the recommendations. Joe also conducts stress testing and probability analysis of the financial planning recommendations. This includes analyzing factors that cannot be controlled, such as inflation, tax law changes, solvency of Social Security, premature death or disability, a prolonged bear market, and other factors that could negatively impact the likelihood of success of the recommendations.

Joe documents the recommendations and basis for the recommendations in his firm's Client record-keeping system. In so doing, Joe also captures the assumptions and estimates that he used in developing the recommendations.

STEP 5

PRESENTING THE FINANCIAL PLANNING RECOMMENDATION(S)

For each recommendation, the CFP® professional must:

- Present to the Clients the selected recommendation(s) and information that was required to consider when developing the recommendation(s)

Joe provides the Millers a written document containing the financial planning recommendations and online access to the recommendations through his firm's secure online portal. Joe also presents the information to the Millers at an in-person meeting. Joe tailors the presentation to the Millers' level of sophistication and comfort with financial planning concepts and makes sure they understand the assumptions and calculations.

Joe informs the Millers that the financial planning recommendations are tailored to their personal and financial circumstances, which Joe summarizes for them. Among other information, Joe reviews their current annual balance sheet and cash flow statement, risk profile, employee benefits, insurance coverages, and savings and investment accounts. Based upon his prior interactions with them, Joe knows that the Millers are very analytical, so he provides a granular view of the Millers' financial situation using technical reports and graphs.

PRACTITIONER'S NOTE

While financial planning recommendations may be presented orally, in writing, in person, over the phone, or in another format, Joe finds an interactive presentation is the best way to present the financial planning recommendations to the Millers.

Joe also reviews the Millers' goals and provides observations and findings concerning the Millers' current circumstances. Joe summarizes the Millers' goals and confirms with the Millers that they are complete and accurate.

Joe presents the financial planning recommendations developed in Step 4 of the financial planning process. Joe uses the financial planning recommendations as a roadmap to the Millers' financial future. He displays a summary of the Millers' assets and shows how they might change over time. He also discusses with the Millers the probability that the financial planning recommendations will allow the Millers to meet their established goals. For each recommendation, Joe discusses the assumptions and estimates used to develop the recommendation, the basis for making the recommendation, and the timing and priority of the recommendation. He also explains that the recommendations, although interrelated, are independent and do not need to be implemented with each other.

Among other things:

Joe knows that the lake cabin is particularly important to Dan and Martha, so Joe spends additional time discussing how the financial planning recommendations maximize the Millers' potential to purchase the lake cabin within six years. Joe discusses the expenses associated with owning two homes and shows the Millers how his recommendations account for both the purchase of the lake cabin and the annual costs of that property, including insurance, utilities, and ongoing maintenance. Joe also makes sure the Millers understand how incurring these added costs impacts their college and retirement savings goals.

Joe discusses with the Millers the advantages and disadvantages of increasing their group life insurance and Dan's disability income insurance through their employers' policies compared to purchasing policies outside of work and offers to help the Millers shop for the coverage that is best for them. Joe also reminds the Millers that their life insurance and disability income insurance needs may change as circumstances in their lives change; therefore, Joe should monitor the Millers' insurance needs so that the recommendations may be updated when appropriate.

Joe explains how he analyzed their risk profiles and existing taxable and tax-deferred retirement accounts and developed a revised asset allocation that would produce a more risk-appropriate, cost-efficient, and tax-optimized investment portfolio.

Joe ensures the Millers understand each recommendation and allows time between each recommendation. At the end of the presentation, Joe invites the Millers to ask questions. Joe takes time to address the Millers' questions and provide additional explanation on issues raised during the meeting.

Q: The Millers ask Joe whether they should invest in asset classes and stocks that they have heard about, including digital assets such as bitcoin or meme stocks.

A: While Joe provides information concerning these asset classes and stocks (discusses risk, returns, etc.), he does not change his recommendation. Instead, he confirms the current asset allocation is appropriate to maximize the potential for meeting the Millers' long-term goals.

Q: The Millers ask Joe about transferring their savings account to a higher-yielding FDIC or NCUA-insured savings or money market account based upon the current interest rates.

A: Joe explains that the current rates likely will increase over time and that moving the funds maximizes the potential of meeting the Millers' long-term goals.

Q: The Millers also ask Joe about their 401(k) plan accounts and saving for retirement. They have a strong interest in having Emily attend an elite private university and want to make that a priority.

A: Joe explains that there often are tradeoffs in establishing goals. He explains that if they were interested in having Emily attend a much less expensive school or if Emily receives scholarships that would reduce the cost of her education, they might be able to retire earlier or have additional funds available for discretionary spending. Given their age, Joe discusses how they might prioritize Emily's education by making 529 savings plan contributions that enable her to be able to afford the elite private university and wait for a few years before maximizing their retirement savings. This likely means that they would need to work until age 67. The Millers tell Joe that they understand the tradeoff and believe that he has found an appropriate balance given their goals.

Joe lets the Millers know that he will contact them throughout the process to discuss any material updates. Joe urges the Millers to contact him with any questions that may arise. Joe advises the Millers that if they implement the recommendations, they will need to coordinate with other professionals to update beneficiaries on retirement accounts and adjust life insurance policies. Joe also advises the Millers of the compensation that he and his firm will receive if they implement his investment recommendations.

STEP 6

IMPLEMENTING THE FINANCIAL PLANNING RECOMMENDATION(S)

(Unless Specifically Excluded from Scope of Engagement)

The CFP® professional must:

- Address implementation responsibilities
- Identify, analyze, and select actions, products, and services
- Recommend one or more actions, products, and services for implementation
- Select and implement actions, products, or services

After reviewing the financial planning recommendations with the Millers, Joe describes their shared responsibilities for implementation, as set forth in a written implementation plan that lays out the following schedule:

Within One Month

- ☐ The Millers are responsible for working with their pre-existing property and casualty insurance agent to obtain the appropriate level of liability coverage. Joe advises the Millers to share his recommendation with the agent and encourage the agent to reach out to Joe with any questions.
- ☐ Joe introduces the Millers to a life insurance agent to obtain the appropriate amount and type of life insurance coverage to meet their needs. Joe has a reasonable basis for the recommendation based on the agent's reputation, experience, and qualifications.
- ☐ Joe introduces the Millers to an estate planning attorney who is available to create their estate planning documents. Joe has a reasonable basis for the recommendation based on the attorney's reputation, experience, and qualifications.
- ☐ If the Millers do not want to work with Joe's initial referrals, Joe advises the Millers that he is able to recommend other estate planning attorneys and life insurance agents.
- ☐ The Millers are responsible for meeting with a mortgage professional to complete the refinance of their existing mortgage.

PRACTITIONER'S NOTE

Joe knows that even though the implementation plan has been set, the timing of the implementation could change based upon updates from Dan and Martha.

- ☐ The Millers are responsible for going online to their retirement plan website and reallocating their 401(k) plan account investments to the targeted asset allocation in accordance with Joe's recommendations, as well as updating their beneficiaries in accordance with their new estate plan.
- ☐ Joe will meet with the Millers to discuss investments for their taxable investment accounts.

Within Three Months

- ☐ Joe works with Dan to obtain an appropriate long-term disability policy that is in Dan's best interests.
- ☐ The Millers will increase their total savings to $1,666.67 each month, which equates to $20,000 annually, to meet the lake cabin goal.
- ☐ The Millers will transfer their regular savings account to a high-yield savings account Joe identified that is FDIC or NCUA insured.
- ☐ The Millers will select a 529 savings plan that Joe recommends and begin funding Emily's college education.
- ☐ Joe will confirm with the Millers that they have changed investments to reflect the recommendations.
- ☐ Joe and the Millers will confirm what recommendations have been implemented.
- ☐ Joe will confirm that the Millers have met with the estate planning attorney and determine whether estate planning documents have been created.
- ☐ Joe will confirm that the Millers have met with the life insurance agent and determine whether the appropriate amount and type of life insurance coverage to meet their needs has been obtained.
- ☐ Joe will confirm that the Millers have met with the property and casualty insurance agent and determine whether the appropriate amount and type of property and casualty insurance coverage to meet their needs has been obtained.

Within Six Months

- ☐ Joe and the Millers will meet to update assumptions, adjust recommendations, if necessary, and measure progress toward goals. They also will address any recommendations that were not implemented.

Within Nine Months (and at appropriate intervals thereafter)

- ☐ Joe and the Millers will meet again to update assumptions, adjust recommendations, if necessary, and measure progress toward goals. They also will address any recommendations that were not implemented.

STEP 7

MONITORING PROGRESS AND UPDATING

The CFP® professional must:

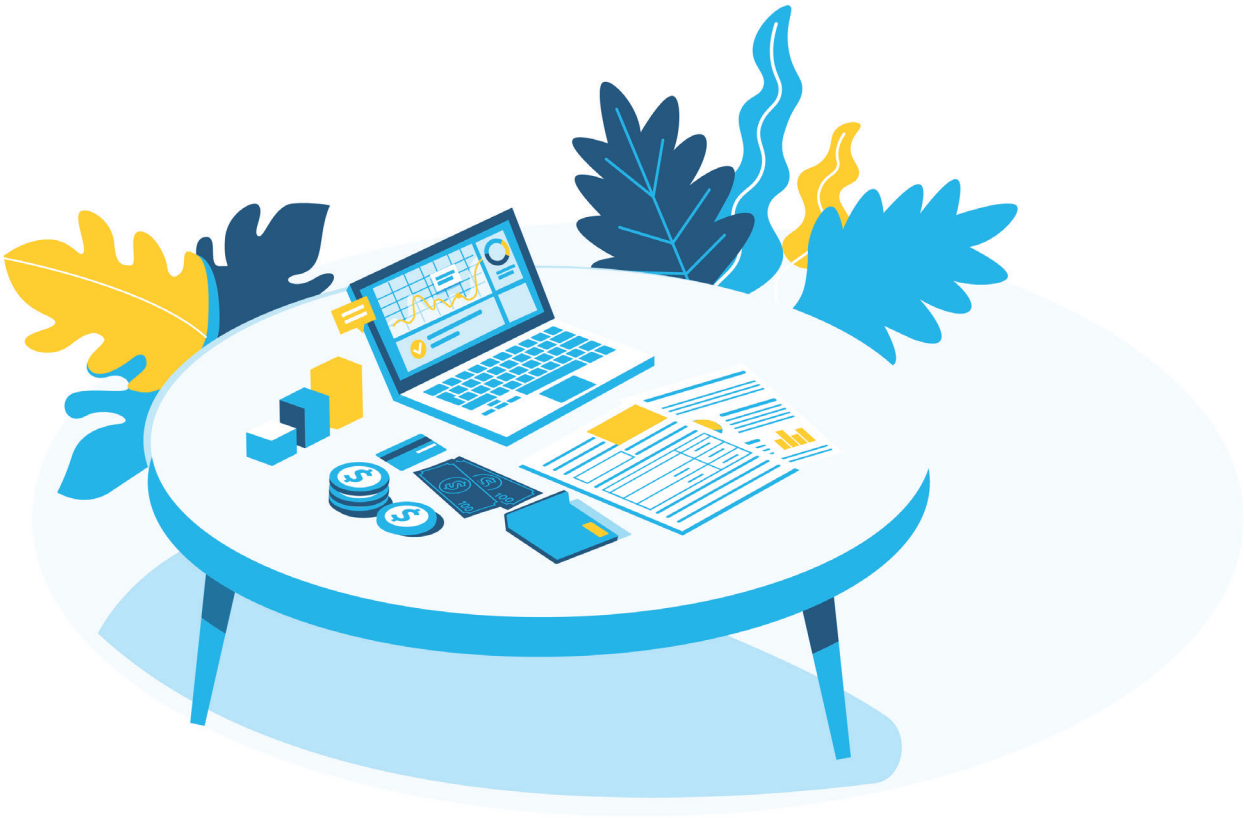
- Establish monitoring and updating responsibilities
- Monitor the Clients' progress
- Obtain current qualitative and quantitative information
- Update goals, recommendations, or implementation decisions

The Engagement Letter provides that Joe has monitoring and updating obligations. Joe and the Millers agree that Joe will conduct a periodic review of their asset allocation and investment performance within their 401(k) plan accounts and taxable investments. This includes monitoring the Millers' life insurance needs so that the recommendations may be updated when appropriate.

Joe checks in at appropriate intervals to review the Millers' progress toward their goals and reviews their current personal and financial circumstances for any changes that would necessitate an adjustment to their plan of action. Joe reminds the Millers it is their responsibility to provide current quantitative and qualitative information concerning their personal and financial circumstances. He also encourages them to ask him questions and raise concerns that they have as they arise. During their meetings, Joe requests that the Millers provide any relevant changes to their information (such as life events, employment changes, and goal changes) that may affect the financial planning recommendations. As their ongoing monitoring meetings occur, Joe updates his recommendations and works to help the Millers get closer to making their dream lake cabin a reality.

Documentation

Joe's firm's Client record-keeping system includes customer relationship management and financial planning software. Joe complies with his legal and regulatory obligations for record-keeping. In complying with the *Practice Standards*, Joe must act prudently in documenting information, as the facts and circumstances require, and taking into account the significance of the information, the need to preserve the information in writing, the obligation to act in the Millers' best interests, and Joe's firm's policies and procedures. Throughout the financial planning process, Joe goes beyond the requirement set forth in the *Practice Standards* by capturing in the record-keeping system (a) the documents that the Millers provided, including both paper documents and documents uploaded to the firm's online Client portal; (b) evidence of delivery of regulatory documents to the Millers; (c) Client correspondence; (d) meeting notes; (e) written agreements, including the Advisory Agreement and the Engagement Letter; (f) investment policy statements that the Millers completed; (g) Joe's final recommendations; and (h) the Implementation Plan, including the Millers' acknowledgment that they wish to move forward with the financial planning recommendations. The financial planning recommendations that Joe provided to the Millers in writing also serve as documentation for the advice given at a specific time and the rationale behind the advice.



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