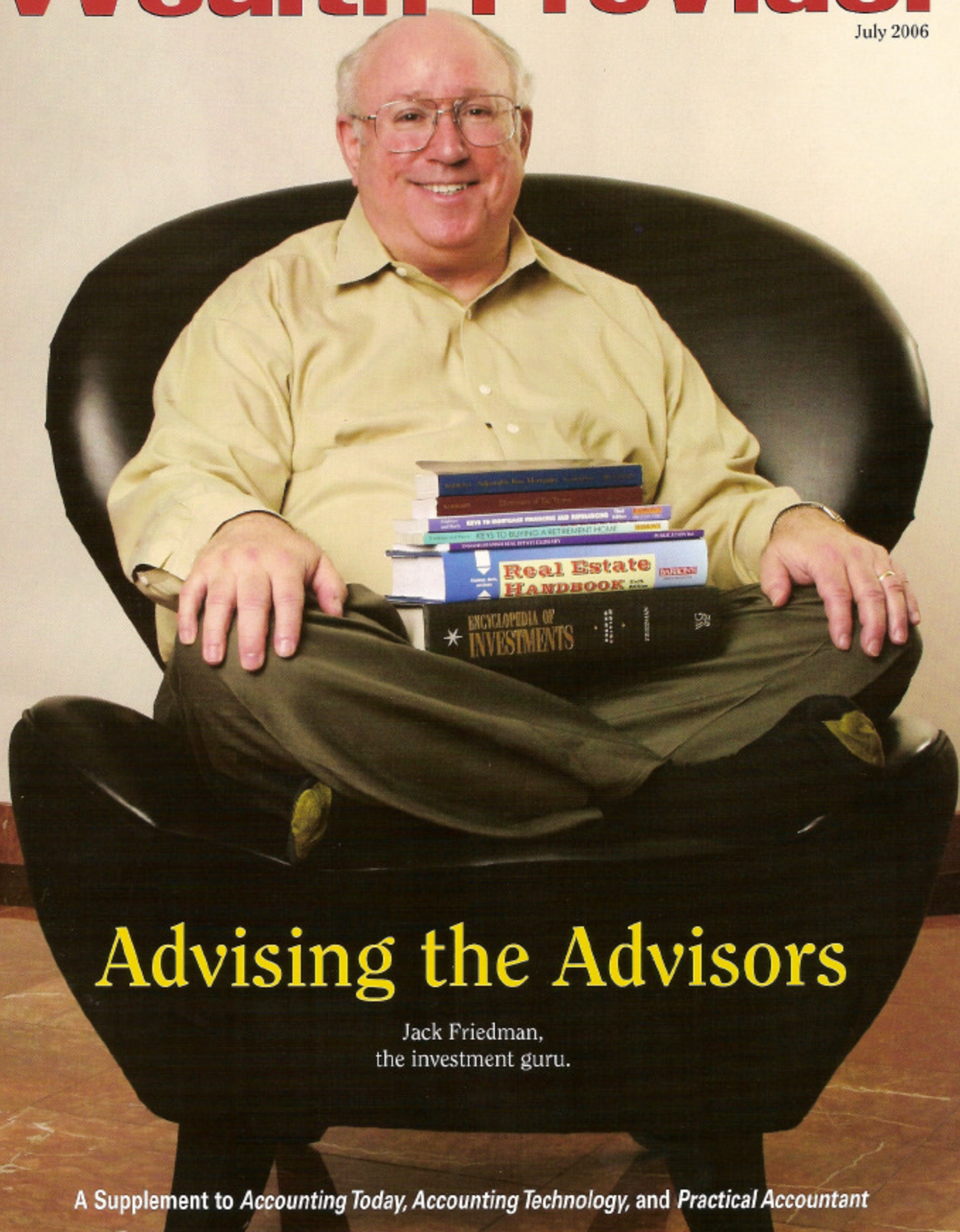


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FOR A SUCCESSFUL FINANCIAL PLANNING PRACTICE<sup>®</sup>

July 2006



## Advising the Advisors

Jack Friedman,  
the investment guru.

A Supplement to *Accounting Today*, *Accounting Technology*, and *Practical Accountant*



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July 2006



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**Jack Friedman**  
Photography  
by Kris Hundt



# THE ADVISING THE ADVISORS GURU

By Stuart Kahan

**J**ack P. Friedman is a real estate economist in Dallas, Texas. He has enough degrees to qualify for a charter membership in an alphabet soup association. They include CPA, ABV, MBA, Ph.D., MAI, CRE, and ASA. And to top matters, he is an Eminent Member of the Royal Institute of Chartered Surveyors (FRICS).

Most of Friedman's work involves litigation support in real estate matters, including contract disputes, environmental damages, condemnations, and construction defects. But, he is also an avid individual investor and has become to many of those in financial planning circles as a guru, perhaps because he was the creative talent behind the



*Encyclopedia of Investments* (Warren, Gorham & Lamont), which was also published in paperback form as *The Complete Guide to Investment Opportunities* (Free Press). Actually, he created an outline of essential information that an investor should have about any investment medium—stocks, bonds, real estate, and precious metals—and even secured an expert on each medium to write a chapter. Marshall Blume, a Wharton finance professor, extended the list of investment types and, with his Wharton School recognition, was named Editor in Chief of the first edition.

He is also the author of two-dozen books including four best sellers published by Barron's: *Real Estate Handbook*, *Real Estate Dictionary*, *Dictionary of Business Terms*, and *Dictionary of Tax Terms*.

### The Road Well-Traveled

Friedman says he first learned about stocks and bonds as a youth from his father, a prominent New York City attorney who later became a stockbroker. He subsequently learned about real estate from extensive audit work for two shopping center developers while he was a young auditor and CPA with a Big Eight firm in New York. Later, he learned about other investments such as precious metals, gemstones, antiques, insurance, and annuities. Friedman excelled in classes at the New York Institute of Finance as a teenager and had considerable opportunities on Wall Street early in his career. Even though the net ups of the market have been greater than the net downs, Friedman preferred life in the slower lane with reliable income to the roller coaster ride.

He left New York for good after earning his CPA and MBA. His first stop in the South was Atlanta. His MBA work had been done in the evenings at Pace University when its graduate school was in an office building in lower Manhattan. Similarly, his Ph.D. (in business with a real estate major) from Georgia State University was earned mostly through night classes. In both situations he held full-time day jobs. "The hardest part was staying awake in class. Some professors would let me nap for a while, but others would rouse me by throwing chalk or an eraser. Weekends were for homework at a quiet place away from home. When I became a professor myself, I had more compassion than my colleagues did for students who dozed off in class." Friedman is the former La Guardia chair professor, Department of Finance, at Texas A&M University.

Despite his acknowledged expertise in real estate investment, Friedman believes that most people are better off investing in securities. "Prices are transparent, there is no property management, and you can't beat the liquidity."

Friedman doesn't manage others' money, though he says if an ultra-wealthy individual or an institution offered a great package, he'd be tempted. "Some days on Wall Street are really tough, and it's hard to deal with people who have just suffered huge losses. I happened to be visiting my Dad's office in 1961 when Kennedy made U.S. Steel rescind its \$6-per-ton steel price increase. Kennedy said it was inflationary. What a depressing day! My Dad loved his work, said he would do it for free. But he would come home after days like that and be bombarded by unhappy clients. Some customers would give him an earful. Others wanted an explanation and direction. Others wanted their money back. Still others ordered him to sell everything; the last thing he would advise was to sell anything, especially when the market was low."

Friedman points out that helping others invest money can be a tough responsibility, especially when the market abruptly turns south without warning. "Dad wasn't the cause of the problem that day. That credit goes to Roger Blough of U.S. Steel or even President Kennedy. But investors needed someone close to talk to or blame for their losses."

He says that bad years are worse than bad days. "The pain of a down market must be at least three times as great as the pleasure of an up market change of the same proportion. The period 1973-74 was awful. In fact, the entire decade of the 1970s was awful on Wall Street."

He notes that one finance professor at Pace explained that tangibles were the appropriate investment choice in an inflationary environment. "That professor had participated in the post-World War II Bretton Woods conference and had much to offer." Friedman woke up to alternative investments.

### Spreading the Word

Although Friedman is not presently engaged in investing others' money, he offers some sound advice to investors and financial planners:

- *Don't invest in the company or industry in which you make a living.* "Anyone who does will not be diversified. Just when you lose your job and need to tap investments, they will be at the low. Too many Enron



employees learned that the hard way. The same is true for any corporate employee, real estate broker, stockbroker, or independent businessperson.”

- *Allocate portions to different investment media.*

“Stocks might represent 30-70 percent, depending on your age, risk tolerance, and portfolio composition. Bonds might make up 30-50 percent. The line between stocks and bonds is fuzzy. Dividend-paying stocks with long dividend histories may have some bond qualities. If you own junk bonds, treat them as part of the stock percentage. Alternative investments might be 5-20 percent of the total portfolio. Keep at least 25-30 total stocks in 10-15 different industries. This will minimize

of quality and condition. Buy art or collectibles for their beauty and the pleasure they give you, not as a retirement account.”

- *Some real estate investments may be excellent, but most have serious drawbacks.* “First, good market information may be difficult to find. Second, real estate is illiquid. It may take months or years to sell, and selling costs are high. Real estate is like a mousetrap, easy to get into, hard to get out of. Third, it is immobile. Real estate is a prisoner of its environment. Fourth, if you pay someone to care for it, you’ll pay through the nose and possibly get poor results. Taking care of it yourself has pitfalls.”



losses for any isolated problem while increasing the chances of getting one that grows exponentially.”

- *Be an owner.* “Sometimes I have to explain that you can put your money in the mattress and earn nothing. Or you can deposit it in a bank that pays 3-5 percent on a CD. The bank in turn lends it to a corporation and charges 5-8 percent interest. The corporation borrows the money expecting to get a 10-15 percent return on its leverage. Wouldn’t you rather own a piece of the corporation that likely earns 10-15 percent than be in the other situations?”

- *Tangible investments are for love, not money.*

“Precious metals, gemstones, arts, and antiques need special and costly care. They are inert. They don’t manufacture valuable products. They don’t add intellectual value. They tend to be inflation hedges, but they are not a place to invest most of your money. Resale prices are negotiated, with prices varying by subjective judgments

Friedman also talks about a colleague who spends his lunch hours doing small repairs (such as fixing leaky faucets) on a number of houses he bought. He spends weekends on bigger repairs, such as changing water heaters. Summer vacations are spent painting and leasing for fall occupancy. “His work ethic and accomplishments are commendable, but as they say in the real estate trade, with more than five toilets, you’ve bought a job, not an investment.”

He explains that some syndications are good, but many syndicators look for ways to maximize *their* income, not the investors’.

- *Be wary of hedge funds.* “Many hedge fund managers are gifted and talented. However, some of the best and brightest have not yet figured out their worst nightmare. If someone is going to have fun gambling with my money, I want it to be me.”
- *Many mutual fund charges are high.* “Index funds typi-

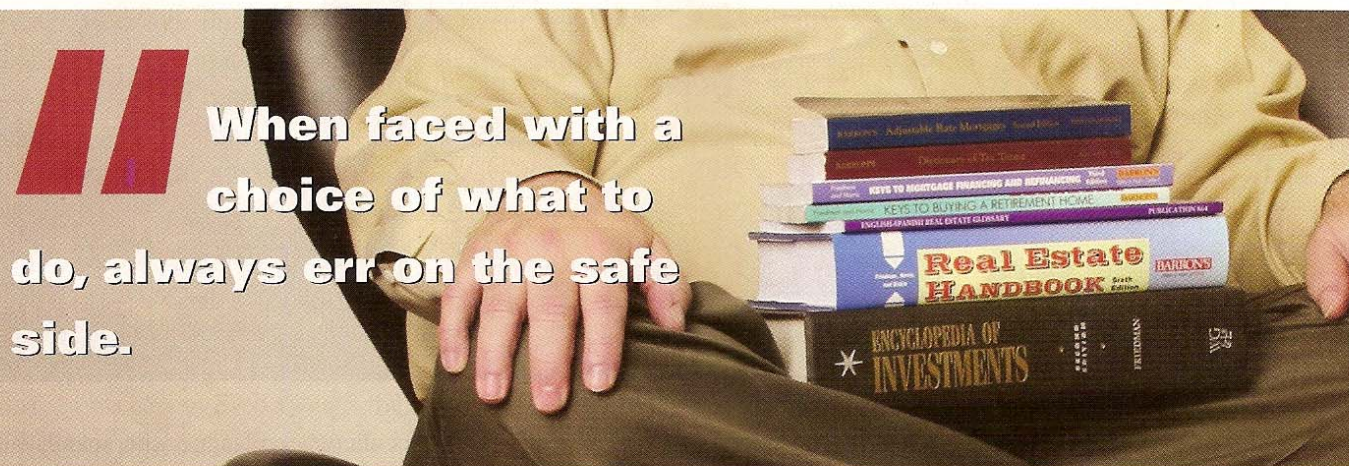


cally outperform managed funds, at a much lower cost. Always consider no-load index funds to give your clients the lowest cost with broad diversification.” Friedman says that academic studies show that no-load funds essentially perform just as well as load funds which, he notes, may bring up an ethical dilemma for financial planners, depending on how they are compensated. “When faced with a choice of what to do, always err on the safe side. Not only is that the right thing to do; it may keep you free from litigation, worry, and trouble.”

- *Develop a niche.* “This applies both to finding and serving clients and finding suitable investments. Most financial planners work on such a broad level that they do not consider individual securities. They can, however, become expert in families of mutual funds.”

quate grasp of the market and portfolio composition, including many who have recently entered the financial planning industry.”

- *Focus clients’ attention on the big stuff.* “It is tempting to spend 90 percent of your conversation on the latest hot topic or niche, leaving little or no time for the more conservative investments that comprise the bulk of a portfolio. When 90 percent of the talk is about risky hot stocks, people get the misleading impression that 90 percent of the portfolio is invested that way, and they feel uncomfortable.”
- *Monitor portfolios regularly.* “Set goals. For example, the amount of assets necessary to achieve a certain steady rate of distributions in retirement. Don’t let short-term events misguide long-term strategies.”



Friedman's investment niche is what he calls “fallen angels.” He looks for both out-of-favor industries and individual companies with problems. His favorites are still utilities where he points out that most have guaranteed customers and monopolies with public service commissions that set rates to allow profits. “However, they have squeamish investors who sell at the first sign of trouble.”

Friedman doesn't like to sell short. “At this writing, income from homebuilder and oil refinery stocks appears to be at unsustainable levels. Selling short, however, exposes the investor to unlimited losses.”

- *Investment knowledge is less common than many people think.* “I know people who think they know everything about real estate from buying and selling their own house. They don't! Likewise, some people think they know all about investments because they own a few shares of stock. Relatively few people have an ade-

Friedman notes that estimates of annual amounts available on retirement can be provided from the above list, calculated on both full amortization over a period of time and creating an income into perpetuity. Moreover, a longitudinal record can be used to chart progress in reaching or exceeding a goal.

### Lots Out There

Most of the above advice, he says, can be found in assorted books on investments. Friedman is particularly fond of Benjamin Graham's *The Intelligent Investor*. He says that he is impressed by the ability of many investment advisors to serve clients long after they pass retirement age.

Despite his expertise in real estate, the only property Friedman owns is his own modest house and some small acreage as an inflation hedge. “It is too illiquid, immobile, and time-consuming for me to manage,” he concludes. ■