4th Quarter 2001

Investors Face Uncertainty and Added Risk as Markets Move Forward

Uncharted waters. While we can look back to prior tragedies for a clue to the future, the financial markets have never encountered a situation similar to September 11, 2001. The loss of life and the financial devastation to New York City and the Pentagon were unprecedented in terms of a single event. The real damage to our $9 trillion dollar diversified economy, however, goes far beyond the financial impact of the actual destruction. The timing of the terrorists' acts compounds the damage of the attack and makes the repercussions of the event hard to predict.

With business spending slowing in the face of overcapacity and excess inventories, economists have been looking to the U.S. consumer to pull the country out of a pending recession. In turn, economies throughout the world have been counting on the U.S. economy regaining strength to prevent a deepening global recession.

Shell-shocked and faced with uncertainty, massive layoffs in the airline industries, and the potential of rising transportation prices, consumers initially seem more inclined to hunker down and wait it out. When you factor in the fact that the U.S. consumer currently has the highest debt load in history, spending caution would not be unexpected. The pending holiday sales will tell the tale and will have worldwide attention.

Nor would one anticipate increased government spending to avert a recession. Unlike the bombing of Pearl Harbor, there is no identifiable enemy to mobilize against. Winning the fight against terrorism is more likely to require small, specialized strike forces rather than massed armies. The $40 billion initially approved for retaliation is again insignificant when one considers the size of the U.S. economy.

So is it all doom and gloom for investors? Not really. We already knew that the market had excesses that needed to be worked out of its system. While the returns of the 1990s were nice while they lasted, history clearly showed that they were an aberration.

continued on page 2

Market Shocks from the Past

The following table shows the percent loss or gain in the Dow Jones Industrials following major tragedies. In all cases, the market recovers and starts focusing again on the same issues as before the tragedy.

Date	Event	1 Day Later	1 Week Later	1 Month Later	1 Year Later
2/15/1898	Sinking the Maine	-2.138%	-5.855%	-11.251%	24.9%
5/7/1915	Lusitania torpedoed	-4.714	-7.293	6.264	35.897
12/7/1941	Pearl Harbor attacked	-2.916	-4.59	-1.45	-.076
11/22/1963	Kennedy assassinated	4.498	5.481	6.578	24.989
12/21/1988	Lockerbie bombing	-0.194	-0.088	3.442	24.531
8/2/1990	Iraq invades Kuwait	-1.918	-3.69	-8.736	4.945
2/26/1993	World Trade Center bombing	-0.457	1.002	2.052	13.883
4/19/1995	Oklahoma City bombing	0.551	2.195	3.181	31.563
	Average	-0.91	-1.60	0.01	19.99

Guidelines for Financial Stress

While it may be reassuring to reflect that over the long run the market's trend has been up, dealing with the here and now can be a different matter during market declines and the slow climb back up. The following are some guidelines for investors:

1) *It may be too late to panic and sell.* Selling equities should only be done if you have a clear plan for re-entering the market. Selling now without a re-entry plan will just lock in losses and could result in you missing an opportunity to profit from the market's inevitable upturn.

2) *Look for ways to cut back on your spending*, particularly if you depend on your investments for current income. The return on your investments in the near future may not be able to keep pace with your old rate of spending. Rather than eat into your principal at the market's bottom, look for ways to conserve capital.

3) *Keep saving.* You may not want to start investing yet, but you want to have money available so that when your financial advisor says it's time, you can take advantage of the market's recovery.

4) *Refinance.* Following the World Trade Center disaster, the Federal Reserve lowered the Fed Fund's rate again and may not be finished lowering rates. Lower Fed fund rates can mean new opportunities for borrowers to refinance mortgages and other loan arrange-

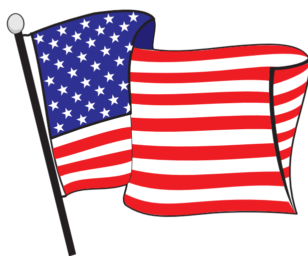
continued on page 2

Investors Face Uncertainty…

contined from page 1

Some market analysts even blame soaring stock valuations and the subsequent severity of the market's drop since mid-2000 on that old bugaboo, Y2K. In advance of the year 2000, companies and governments worldwide made massive investments in new technologies and the technologies worked. They worked so well that we saw tremendous productivity increases and the growth of excess capacity. The telecommunications infrastructure that was built during the years of soaring stock valuations alone offers excess capacity for considerable time to come.

The long-term prospects for economic growth remain favorable. It's also encouraging to realize that the stock market tends to lead the economy, beginning its recovery when all seems darkest. However, it is not unlikely that the market's upward trend will be a fragile one, prone to starts, stops and



sudden drops. We're in uncharted waters, but that doesn't mean the lessons of the past don't count.

We believe that the best opportunity to reduce risk and profit from upward moves in the coming market will come through active management — the type of investment management that recognizes that losing money means losing opportunity and time. We welcome your calls and look forward to the market's inevitable recovery and our nation's victory over destructive terrorism that creates in a free people the will to overcome.

Retirement Record-Keeping

Job hopping and even career hopping during your working years make it more important and more difficult to keep good records of employer-related retirement earnings. That includes defined benefit plans, such as employer-paid pensions, as well as 401(k) accounts you may have at past employers.

By the time you're ready to retire, you've likely worked for several different employers and you may have been self-employed. If you haven't rolled over pension plan benefits into your own IRA or other account form, past employers may owe you retirement benefits. Don't count on them to come looking for you.

Go back through old paperwork and contact past employers to confirm what you're owed at retirement. Some of those companies may have merged, changed names, or gone out of business. If you have a pension plan and the company no longer exists, the plan should still be funded. Contact the Pension Benefit Guaranty Corporation in Washington DC at 800-400-7242 or visit the government agency on the web at www.pbgc.gov to find out about it. The web site has a pension search feature that allows you to look up information about a particular pension, and it has a listing of publications about pensions you might find of interest.

Also keep in mind that your life may have changed considerably since you filled out beneficiary forms for both pension and 401(k) accounts at past employers, so make sure they're current and accurately reflect your desires and contact information.

If you haven't already done so, you should consider consolidating your 401(k) investments into your current employer's plan or rolling them over into an IRA where you can control the investment choice. It's a good idea to do this with every change of employer. This will help simplify record keeping and reduce paperwork, making life easier for you and your heirs, and perhaps increasing your investment power and lowering fees in the process.

And when the time comes for retirement, consider moving your existing 401(k) accounts into a rollover IRA. The benefits of this include severing ties with your employer and having investment options beyond the offerings in that plan.

Keep or Toss?

Spring cleaning isn't always a good idea. Sure, it's nice to throw away broken lawn furniture that's gathering dust in the basement, but there's one thing that you should hold on to for a long time – financial records. Those records include tax forms and their supporting documents as well as investment records and statements.

Tax law requires you to keep tax records for as long as you could be audited for a particular year's return, which is usually three years. But some tax professionals recommend a minimum of six years, because the IRS can still audit a return if a taxpayer underestimates income by more than 25 percent. And the IRS can always audit a return when people intentionally fail to report income.

Investment statements are also important to keep, at a minimum three to six years after you have reported the sale of the investment. Paperwork for IRAs should be kept for several years after all funds are withdrawn.

Because these records cannot be duplicated, it's wise to keep them. The adage 'better safe than sorry' certainly applies when dealing with the IRS.

Guidelines for Financial Stress

contined from page 1

ments. Every penny you don't pay in interest represents real savings.

5) *Borrow before tapping into retirement funds prematurely*. When you pull money out of a government-recognized retirement account, you incur taxes, both state and federal income taxes, and often a penalty. Combined, the cost can far exceed that of borrowing the funds you need and paying interest. It is also difficult to rebuild retirement assets once tapped.

6) *Talk to your financial advisor*. Seemingly insurmountable problems often have solutions once they are approached from a different viewpoint. Take advantage of the experienced professional resources available to you.

Taxpayers Get a Break

If you like the tax law changes in the new Economic Growth and Tax Relief Reconciliation Act of 2001 (commonly known as the Bush tax plan) make certain to let your legislators know now and continue to let them know for the next ten years. The bill will be voided come 2011 if Congress fails to re-enact the bill's provisions. And because much of the bill involves slow phase-ins and phase-outs of exemptions, deductions and credits, Congress could eliminate full phase-in of various tax benefits in the bill.

The bill starts with modest savings and a flash-in-the-pan rebate. This summer, Americans began receiving checks reflecting a rebate from a reduced tax level on the first $12,000 (married couples), $10,000 (single parents) and $6,000 (single) earned.

But the tax relief goes far beyond a one-time check, and should be discussed with your financial advisor to determine exactly how it will impact your tax, retirement and estate planning situations.

Here's a summary of the plan's highlights:

Tax Brackets Reduced:
Through 2006, tax brackets gradually go down:

New bottom bracket – 10%
28% falls to 25%
31% falls to 28%
36% falls to 33%
39.6% falls to 35%

As a result, tax deductions taken this year will have more value than they will in coming years. You'll probably benefit from taking as many deductions this year as possible and deferring the receipt of income until a later year. If you're planning to make a donation, evaluate the benefits of doing it all this year as opposed to over several years.

Dependent Tax Credit Increased:
Beginning this year, tax credits for dependents under age 17 are increased to $600 from $500 per child. The credit gradually increases to $1,000 in 2010. Eligible childcare expenses that can be deducted will also increase, beginning in 2003.

Easier to Save for Higher Education and Retirement:
Allowed contributions to education IRAs rise from $500 to $2,000 per year starting in 2002. State-directed tuition savings plans now also cover private schools, and qualified withdrawals are no longer taxed.

Retirement plan contribution limits are increasing: The $2,000 IRA limit increases to $3,000 in 2002, growing to $5,000 by 2010. Workers over 50 can contribute $3,500 in 2002 and $6,000 by 2008.

401(k) contribution limits increase to $11,000 next year, and $15,000 by 2006.

A new retirement vehicle – called a Roth 401(k) – allows taxpayers to put money away for retirement after taxes. Any future gains can be withdrawn without paying taxes. This new plan can be helpful to individuals whose income was too high to participate in Roth IRAs in the past.

Estate Tax Reduced:
And there's good news concerning taxes paid on the transfer of wealth between generations. The new tax plan gradually phases out the estate tax by 2010, and reduces the top rate from 55 percent this year to 50 percent next year, and eventually moves it down to 45 percent.

The amount of an estate that can be passed on to heirs without paying taxes on it is also increasing. It currently stands at $675,000 this year, but moves up to $1 million next year. The amount continues to increase until it reaches to $3.5 million through 2009 before it is eliminated in 2010. The break is short term. Estate taxes will be back in 2011 without further action by Congress to repeal them permanently. That's why you might want to continue to communicate with your representatives about permanent repeal.

Saving for College – Know The Options

Never before have there been more ways to save for college – and that's good news given the lofty and ever-rising cost of higher education. According to the College Board, the average cost of tuition, room and board at a four-year public school is $3,510, while the average private college or university cost was $16,332. And those expenses continue to rise, increasing an average of 4-5% last year alone.

The task of saving for a child's college education can seem daunting. But as with any investing scenario – time is your ally.

The first step in any savings strategy is to determine your goal. Is it to pay full expenses for all children to go to college, help pay part of the expenses for a grandchild, save for in-state tuition, or finance an Ivy League education? Once you've determined your objective, consider the following options to get you there.

Savings Options With Income Restrictions:
Roth IRAs – If your family income is less than $160,000 a year if you're married, or $110,000 if you're single, you can participate in a Roth IRA. Roth IRAs can be used to fund college expenses in addition to retirement. If you meet the income restrictions, each parent can save up to $2,000 per year in a Roth IRA. Those savings caps go up to $3,000 in 2002 and $4,000 in 2005. After a five-year period, funds may be withdrawn for qualified tuition costs. If the Roth IRA holder is under 59 ½, earnings will be subject to income taxes the year the money is withdrawn, but there isn't a penalty. In addition, contributions can be withdrawn first, further deferring the need to pay income taxes. If the accountholder is over 59 ½ and the funds have been in the account for at least five years, no income taxes apply.

Roth IRAs may be part of a college savings scenario, but you'll need to

continued on page 4

Saving for College – Know The Options

continued from page 3

take into consideration the savings limit that comes with this vehicle and factor that into meeting your savings goal.

Education IRAs – Education IRAs carry the same income limits as Roth IRAs. The Bush tax plan raised the annual contribution limit to $2,000 from $500, and tax-free withdrawals also may be used for primary and secondary school. If the proceeds are used to pay for college tuition, earnings on the funds are tax-exempt. Again, an education IRA can be part of the college-savings puzzle, but consider how much of a role it will play given the contribution limits. Education IRAs can provide a good way for relatives to help pay for a child's college education, while not funding the entire amount.

Savings Options Without Income Restrictions:

Section 529 (qualified state savings plans) – Named after the section in which they appear in the Internal Revenue Code, state savings plans are one college savings option getting a lot of attention, as available plans increase in number and flexibility. These plans carry no income restrictions, and earnings grow tax-free until funds are distributed. Plans in some states are also exempt from state sales taxes. This type of plan qualifies for the $10,000 annual gift exclusion, and you can elect to treat a one-time contribution as if it were made over a five-year period, allowing up to $50,000 in one lump-sum gift. Any withdrawal not used for education is assessed a 10% penalty. Check out www.savingforcollege.com to compare state plans.

Uniform Gift to Minors Account or Uniform Transfer to Minors Account – While this type of savings option also comes without an income limit, it does carry some risk. A parent or guardian serves as custodian of the funds and makes investment decisions, although the child's social security number is on the account. The child pays any income taxes due. Depending upon state law, when the child turns 18-25, she gets control of the account to pay for college, a trip to Bermuda or the hottest sports car. Before choosing this option, you'll need to determine how you feel about this risk.

Crummey Trust or 2503© Trust – While this investment option offers more investment control, it also has a greater cost involved to set up a trust and handle the paperwork and obligations required of the trustee.

I would like more information about:

- ❒ Retirement planning
- ❒ Investing lump sum distributions from retirement plans
- ❒ Risk management of mutual funds
- ❒ Investment options offered by your firm
- ❒ Past performance for your investment programs
- ❒ Tactics used by your firm to avoid market declines
- ❒ Information on your firm's history
- ❒ The following topics discussed in the newsletter ________________________

NAME ____

ADDRESS____

CITY ________________________ STATE ______________ ZIP ____________________

PHONE ________________________ BEST TIME TO CALL ________________________