Kensington Times

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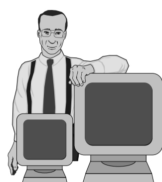

From The President's Desk

Ralph H. Phillips

From our family to yours, I would like to wish you a very happy, safe and blessed Holiday Season!

- **Area Code Change: Beginning March 1, 1998, our Area Code will change to "724" please make a note of it!**
- **Look For It: Our clearing firm is the sole sponsor of football reports on NBC. Look for the SunAmerica Sports Desk, throughout the season!**
- **Internet Change: We are in the process of updating and drastically changing our internet homepage. Please be patient with all of the "under construction" signs you see at www.kensingtonfinancial.com.**

Shop Around the Choices of Annuitizing

Variable annuities have exploded in popularity in recent years as baby boomers start accumulating retirement money. These products are typically designed to be converted into an income stream and paid over the course of years. The Industry is trying to give investors more choices in what are known as "Payout Electives." It is a way for companies to separate themselves from the pack of competitors offering similar options. Unfortunately, however, the alternatives themselves can be confusing. Here are the most-common options currently available:

- **Lump-sum distribution**. Investors can get their entire account balance in a single

payment. This avoids the annuitization issue but has several downsides. First, investors will have the hassle of figuring out what to do with the money. More significantly, however, are the tax consequences; if you are over 59 1/2, the earnings will be taxed at regular income tax rates upon withdrawal. If a withdrawal is made before age 59 1/2, an

Should you set up a custodian account for your child?

The Uniform Gifts and Uniform Transfers to Minors Acts (UGMA/UTMA) enable you to make a gift of securities to a minor. Under UGMA/UTMA, you may designate yourself or another adult to act as "custodian" for the minor's account. The minor is still the beneficial owner of the shares, and the account earnings and transactions are reported to the IRS under the minor's Social Security number. The custodian's job is to direct transactions on behalf of the minor. When the child reaches the age specified in the state's act, the custodian is legally required to transfer the shares into the name of the minor.

Here are the advantages of UGMA and UTMA accounts. In some cases, the tax liability of money invested in a minor's name may be lower than the taxes due on the same money if it were invested in an adult's name, because of possible differences in tax brackets (see table on page 3). However, parents should be aware that money in a UGMA or UTMA account becomes the property of the child when he or she reaches the age specified in the state's act. Your daughter (or son), therefore, has the right to use the money

New State Law Simplifies Transfer of Securities To Survivor

Pennsylvanians who own stocks, bonds, mutual funds or similar securities should be aware of a new state law (Act 168 of 1996) which can simplify the transfer of securities to survivors. The new law endorsed by AARP, the American Bar Association, and the Security Industry Association adds specific provisions in Chapter 64 of Title 20 (Decedents, Estates and Fiduciaries) pertaining to the "Transfer on Death Security Registration."

The new law allows the owner of a security to designate a beneficiary when the security is issued or purchased. If the owner dies, the security passes directly to the beneficiary rather than becoming an asset of the owner's estate.

Securities transferred under the new law would avoid probate, but would still be subject to estate and inheritance taxes. Since the law just went into effect in February, it may take some time for issuers, banks and brokers to develop procedures for registering securities. For more information., contact us at (724) 334-1950.

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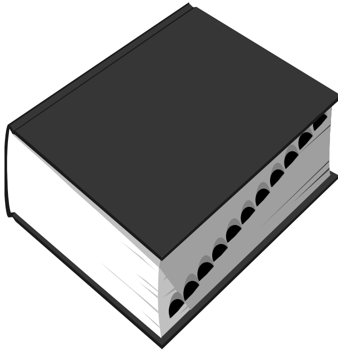
Year's Top Investment Books



1. Cyber Investing: Cracking Wall Street With Your Personal Computer, David L. Brown & Kanssandra Bentley, John Willey & Sons, $24.95. Shows beginning investors how to unleash the awesome potential of their PCs to spot investment opportunities, for maximum earnings with a minimum of time spent.

2. What Works on Wall Street, James P. O'Shaughnessy, McGraw-Hill, $29.95. The author has taken all notable market strategies and tested them over the past 34 years of data to discover what really works on Wall Street.

***3. The 100 Best Stocks To Own In America*, Fourth Edition**, Gene Walden, Dearborn Financial, $22.95. Ranks the best 100 stocks, using a variety of formulas and criteria.

4. Traders' Tales: A Chronicle of Wall Street Myths, Legends, Outright Lies, Ron Insana, John Wiley & Son, $24.95. A collection of stories that captures the true flavor of Wall Street from some of the best-known names in the business as well as some people you've probably never heard of.

5. Soros On Soros, George Soros, with Bryon Wien and Krisztina Koenen, John Willey & Sons, $39.95. Unquestionably the most powerful and profitable investor in the world today. Soros ends the speculation and candidly reveals his views of investing and global finance, politics and the emerging world order and the responsibility of power.

Taxable vs. Tax-Free Funds

An 8% taxable bond fund yield might not be as attractive as a 5.5% yield on a tax-free bond fund. (Investors sometimes pay less attention to the differing returns between taxable and tax-free funds, and then put the money on the higher risk investment.) You can determine for yourselves whether you should own a tax-free fund or a comparable-quality taxable fund, in two ways. First, both require you to know your marginal tax bracket, which is the percentage tax rate shown in the tax table applied to your last dollar of adjusted gross income. The tax rates vary for each income level depending on whether you file singly, jointly or head of household. The 1997 tax rates are generally unchanged from those in 1996, so you can now use the 1996 tax tables.

(*Continued On Page 3)*

"The inherent vice of capitalism is the unequal sharing of blessings; the inherent virtue of socialism is the equal sharing of miseries."

- Winston Churchill

Wall Street Wisdom

***Q.** In a market like this, what is a good strategy for the individual investor?*

A. The individual investor who is taking a very long-term approach to their money should just let the money sit there.

***Q.** What is the best strategy for individual investors to employ in this market environment?*

A. The best strategy for an individual is not to panic. If you have loaded up on speculative (very risky) stocks or bought on margin (borrowed money to buy), you really have to reassess things. But if you are in good companies that are growing well and they are not too expensive, you just stay put if you are a long-term investor.

You might be right about where the market is going — but you have no idea where it will go after that.

Patience is more important than market timing.

"Any man who is a bear on the future of this country will go broke." **— J.P. Morgan**

From "...Annuitizing" Continued From Page 1

- **Systematic withdrawals**. Annuity owners can receive periodic payments while the balance of their investment continues to grow, without annuitizing. Depending on which company you are with, investors can select payments in a certain dollar amount, a percentage amount, mostly equal payments or a five-year payment. This option is attractive because owners have a lot more control.

As boomers approach retirement, annuitization will become an increasingly attractive option. Especially as Social Security and private pensions are not as reliable as they used to be. Here are the most-common options for annuitization.

- **Life-only.** This option provides a series of guaranteed payments —either monthly, quarterly or yearly— for as long as the annuitant lives. Payments stop upon death. Any money left over is forfeited to the insurance company, a standard practice that allows the companies to subsidize the payments of the long-lived with the proceeds of the short-lived.
- **Life with period certain**. A combination of life-only plus guaranteed payments for a certain number of years, usually 5, 10, 15, or 20. Under a 10 year plan, an annuity owner would get guaranteed payments for that period. If he or she dies before the 10 years ends, payments go to a beneficiary for whatever period remains. If the annuitant lives past 10 years, payments continue for life.
- **Joint-life and survivor.** This provides income for two people, the annuity owner and a beneficiary. Payments stop after the death of the survivor.
- **Term-certain.** Guaranteed payments for a specified number of years. The annuity owner gets the regular payments for whatever period of time was selected, and if he or she is not alive, a beneficiary receives the money.
- **Commutable contracts.** In some cases, annuity owners who have period-certain or term-certain annuities can cash

From "Taxable vs. Tax-Free Funds" (Continued From Page 2)

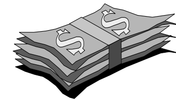
In future years, both your income and tax rates may change, so it pays to reexamine your situation periodically.

The easiest way to make the taxable/ tax-free comparison is to compute the after-tax yield of a taxable fund whose portfolio quality and average maturity is equivalent to the tax-free fund you are considering. This means reducing the taxable fund yield by the amount of taxes you would pay. For example, if your marginal tax rate is 31%, simply subtracting that from 100 indicates you will keep 69 cents of your last dollar of earnings after taxes. Now, if you are looking at a taxable bond fund yielding 8%, multiply that yield by 0.69. The answer, 5.5% is what you will need after taxes. A tax-free fund yielding above 5.5% is obviously more attractive, while a tax-free fund yielding below 5.5% is unattractive.

The second, and more popular method of comparison, is to convert the yield of the tax-free fund you are considering to a "taxable-equivalent yield." Subtract your tax rate from 100 to determine how much income you will have left after taxes from of-income; each dollar of income; then divide that into the tax-free yield. Using this example, if you are looking at a tax-free fund that yields 5.5% and you are in the 31% marginal bracket, divide 5.5% by 0.69. The result, 8%, is the taxable-equivalent yield. Comparable-quality and maturity taxable bond funds yielding more than 8% are superior to this tax-free fund; taxable funds yielding less than 8% are inferior.

The current marginal tax rate for individuals under the Budget Reconciliation Act of 1993

Single	*Married Couple*	*Marginal Tax Rate*
up to 22,000	up to $36,900	15%
22,101-53,500	36,901-89,150	28%
53,501-115,000	89,151-140,000	31%
115,001-250,000	140,001-250,000	36%
over 250,000	over 250,000	39.6%



From "Should You Set Up..." Continued From Page 1

as she, or he, pleases. Money registered under your child's name may be a disadvantage when applying for college financial aid. Before granting financial aid, many colleges often first determine a family's "need." Need is based on a standard formula that typically requires 35% of the student's assets be used each year for the cost of higher education, versus a maximum of only 5.65% of a parent's assets. That means considerably more money might be expected to go for college before financial aid could be granted than would be required if the same money were in a parent or custodian's name.

For lower-income families or those with only small amounts to invest, UGMA's and UTMA's still hold the prospect of modest tax savings. For other families, for whom an 18- or 20-year olds control of large sums of money may be a consideration. The question is, Does the potential tax savings outweigh the possibility of losing financial aid

Find the words from "The Educated Investor" in the right hand column. (Solution on page 4).

C	**H**	**D**	**I**	**V**	**I**	**D**	**E**	**N**	**D**	**W**	**I**	**B**
P	**J**	**B**	**R**	**I**	**A**	**N**	**O**	**Y**	**O**	**S**	**X**	**R**
F	**O**	**S**	**F**	**K**	**O**	**I**	**R**	**O**	**Y**	**P**	**N**	**E**
R	**U**	**P**	**R**	**O**	**S**	**P**	**E**	**C**	**T**	**U**	**S**	**A**
A	**B**	**Z**	**I**	**N**	**S**	**A**	**L**	**M**	**M**	**R**	**Q**	**K**
L	**W**	**A**	**E**	**T**	**A**	**R**	**D**	**V**	**C**	**N**	**K**	**P**
P	**Z**	**T**	**L**	**O**	**K**	**V**	**Q**	**G**	**H**	**K**	**F**	**O**
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Z	**A**	**E**	**T**	**I**	**E**	**U**	**R**	**E**	**N**	**E**	**F**	**T**
C	**U**	**J**	**H**	**N**	**T**	**E**	**U**	**A**	**B**	**O**	**Y**	**W**

The Educated Investor

1. Beta: A statistical measurement correlating a stock's price change with the movement of the stock market

2. Breakpoint: A purchase amount that qualifies for a reduced sales charge.

3. Call option: An option contract that gives the holder the choice to buy the stock and the writer the obligation to sell the stock at a specified price.

4. Dividend: A payment of corporate earnings to shareholders. Dividends are normally paid in cash, but may also be in stock.

5. Extension: An extension allowing an additional three business days to make payment for a customer who fails to pay for a purchase of securities by the third business day after trade date.

6. NAV (Net Asset Value): The assets of the fund less its liabilities, divided by the number of shares outstanding. This is the price a mutual fund shareholder receives when selling shares of the fund.

7. Par Value: The face value appearing on the certificate. Preferred stocks normally have a par value of $100, bonds, a par value of $1,000.

8. POP (Public Offering Price): The price of shares in a mutual fund including the maximum applicable sales charge.

9. YTM (Yield To Maturity) The yield of a bond, taking into account the gain or loss at maturity.

Will the Capital-Gains Tax Cut Hurt Variable-Annuities?

As Congress and the president finished haggling over how much to lower the capital-gains tax, questions arise over whether the tax-cut could hurt annuity sales by making other investments more attractive. This is because variable annuities grow tax-deferred. Annuity companies have found the tax-deferral feature to be their strongest marketing component and a growing number of investors are choosing annuities to pay for their retirement or to supplement existing retirement savings. When it comes time to withdraw money from variable annuities, the gains are taxed at regular income-tax rates, which range from 15% at the lowest end to 39.6% for the highest level.

In contrast, the top capital-gains tax on profits from the sale of mutual fund shares and other investments currently is 28%. Under the recently passed tax bills, that rate will drop to 20%. Although this tax-cut could affect variable-annuity sales, some experts argue that variable annuities are popular for reasons that they believe would outweigh any change in tax treatment due to the death benefit. It guarantees that if an investor dies while accumulating retirement money, heirs receive at least as much as what was invested. Many investors view the death benefit as protection from the stock market's unpredictable ups and downs.

Another reason is the ability of variable-annuity investors to trade from one investment portfolio to another without incurring taxes. Switching in and out of mutual funds, on the other hand, can generate a capital-gains tax bill with each transaction. Whatever the outcome, some significant long-term changes are clearly on the way. Variable-annuity companies will have to review how they market their products, and may have to emphasize other features instead. If you have questions about how the '97 Tax Law Changes will affect you, we urge you to contact your Certified Public Accountant. If you have questions about variable annuities

KENSINGTON FINANCIAL IS . . .

Ralph H. Phillips, President
Renee M. LeVeque, Vice President & Executive Editor
Chuphong Taveesup, Intern Editor
Carlo Ciappetta, Intern

TELL US WHAT YOU THINK!!

Phone us at: (724) 334-1950 or 800-547-6998

Fax us at: (724) 334-1954

See us on the internet at:
www.kensingtonfinancial.com

Send us e-mail at:
k-admin@kensingtonfinancial.com

Here is the solution...

C	H	D	I	V	I	D	E	N	D	W	I	B
P	J	B	R	I	A	N	O	Y	O	S	X	R
F	O	S	F	K	O	I	R	O	Y	P	N	E
R	U	P	R	O	S	P	E	C	T	U	S	A
A	B	Z	I	N	S	A	L	M	M	R	Q	K
L	W	A	E	T	A	R	D	V	C	N	K	P
P	Z	T	L	O	K	V	Q	G	H	K	F	O
H	X	P	L	S	U	A	Y	V	U	R	S	I
E	Q	R	C	A	L	L	O	P	T	I	O	N
Z	A	E	T	I	E	U	R	E	N	E	F	T
C	U	G	H	N	T	E	U	A	B	O	Y	W

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