VOLUNTARY
BENEFIT SYSTEMS
CORPORATION
OF AMERICA

P.O. BOX 151
343 MILLBURN AVENUE
MILLBURN
NEW JERSEY 07041
973-379-7666
973-379-7277 FAX

INVESTMENT OUTLOOK **March, 2003**

In October 1998, I attended a cocktail party preceding a Columbia football game on the West Coast and met Leonard Koppett, the Hall of Fame baseball writer and Columbia graduate. I told him that with Bernie Williams about to become a free agent, the broadcasters on WFAN in New York were telling us that there would be no deal with the Yankees. “Bernie was gone!” they said.

“What do they know?” Koppett replied. “They know nothing. All they know is how to get people to make phone calls.” And of course he was right. Bernie signed a contract with the Yankees, which, at the time, made him one of the highest paid players in baseball.

And so it is also true that financial writers and broadcasters know how to sell papers or attract listeners. They don’t necessarily know anything about the financial products on which they report. The Dolans on WOR in New York are a perfect example of broadcasters with a loyal audience who religiously knock permanent life insurance and annuities... all kinds of annuities.

Let’s look at the facts. Annuities were created to be retirement plan vehicles that provided tax deferral. If a person in the 25% bracket invests money at 4% interest into a bank account, he compounds at a net 3%, which will then take 24 years for the funds to double. If he earns the same rate in an annuity, which is tax deferred, he compounds at the full 4% and now it will take only 18 years for the funds to double. Assume this person invests $100,000. 24 years later they will end up with $200,000 in the bank account or $250,000 in the annuity.... each still paying 4%. If this person starts taking out interest only at 4%, it is taxable either way. The bank will pay $8,000 per year while the annuity will pay $10,000 per year. Which investment do you like better? And who cares if the additional profit in the annuity becomes taxable at death?

Then came Variable Annuities. People liked them because of the presumption of higher returns from equity investments, which, in fact, was the case for many years. Insurance companies charged a fee for putting their annuity wrapper over the funds, which created the same tax deferral... except that now we were talking about a greater advantage because of the assumed greater rate of return. Insurance companies charge anywhere from about 0.4% to 1.6% for the tax-deferral wrapper. The low cost products come from TIAA-CREF, Vanguard, Fidelity, etc. who include only their own funds. The higher priced annuities offer multiple managers. I sell a multiple manager annuity that charges 0.95% as its base fee which includes the guaranteed death benefit.

Annuities offer a great many wrinkles for additional fees. You can invest $100,000 and immediately be worth $103,000 by paying an additional fee of 0.45% for seven years. You can be guaranteed that there can be no loss after ten years by paying an additional 0.50%. Every option has its own price. The customer picks the options they want. The annuity sells because it offers options not available in mutual funds or stocks. Funds and stocks offer taxation at long-term gain rates and annuities offer options. If held inside IRA accounts, they are taxed the same. If the total cost of annuities is 2.25% or 2.5%, they come in very close to B Share mutual funds. The total cost of my annuities including both mutual fund and annuity fees is under 2%.

What happened when the market went down? Suddenly... everything looked bad. My God! Cisco went from 85 to 13. G.E. lost half its value. IBM, Amex, Citibank and a lot of other Blue Chips hit the skids. Janus Worldwide and Janus Twenty funds went from 85 to 28. PBHG Growth Fund went from 80 to 13. And variable annuities went down also. So the financial writers and broadcasters now have to decide who they can beat up in their next column or broadcast.

In fact, these low prices give anyone with cash an incredible buying opportunity. Just read the history of the Depression. In the darkest economic time in this country's history, those that had the guts to buy ended up being our biggest winners. We are not as bad off now as we were then but lets face it... three straight down years hasn't happened since 1939-1941. Therefore, if World War II took us out of the depression and the Gulf War took us out of recession... then maybe the President feels that a war can fix our economy.

So tell me, do you know which stocks will go up? My bet is that fund managers have a better handle on this situation than individuals. Annuities allow those funds to be owned tax-deferred and, oh yes, Variable Life Insurance allows us to own those funds on a totally non-taxable basis.

As they used to say... "That's the story!"

Now, here's something new I want you to know about. It's not new, but then we've not written about it in the past.

How would you like an insured investment that gives you an absolute guarantee that it cannot go down in value, but where the growth in value is linked to a stock market index such as the S&P 500? This opportunity is created for you by **Equity Indexed Annuities** (EIA's). Basic to an EIA is the underlying guarantee that you cannot lose your money over the term of the annuity, which normally runs between seven to fourteen years. On the other hand, you participate in the stock market's growth (with no downside risk). You give something up for eliminating the risk. Some EIA's will place a cap on the maximum growth they will allow... such as 7% or 9%. Other EIA's will have no cap but will pay you 70% of the growth in up years, keeping the other 30% to protect themselves in down years. The bottom line is that you are guaranteed a gain... you just don't know how much until the investment period is over. In some cases, in order to keep your gain, you must take periodic withdrawals over a four or five-year period rather than a lump sum distribution.

One of these EIA's has a wonderful option that can help you convert a regular IRA into a Roth IRA, save about 35% in tax liability and defer the payment of those taxes for five years. Now, with a Roth IRA, 100% of your future withdrawals would be free of income tax.

Remember that with EIA's as with any annuity, there are surrender charges or pre-mature withdrawal penalties if you cash out during the holding period and you pay a 10% penalty tax on any withdrawals made prior to Age 59½. For more information, just give me a call.

Paul A. Gomperz, CLU, ChFC
1 – 888 - *PLAN AHEAD*
pgomperz@vbscorp.com
Visit our website at www.vbscorp.com

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