



# The Fragasso Group, Inc.

*The Retirement Planning and Wealth Preservation Specialists*

*A Registered Investment Advisor*

*...For the Serious Investor*

E-mail: [fgi@fragassogroup.com](mailto:fgi@fragassogroup.com) • Website: [www.fragassogroup.com](http://www.fragassogroup.com)

## Saving Taxes Through Your Investments

**C**onsider that any dollar that you do not pay out in taxes is available to grow on your behalf over the years. The purpose of this newsletter is to make you aware of some of the methods by which you can save tax dollars for your own use.

***The most effective way to save taxes and invest money for your future is through retirement plans.***

As an **individual**, you can use:

- *Your employer-provided 401K or 403B plan.* If you take a dollar of wages or other income and use it for consumer goods or services, you must first run it through the tax collector. So, for example, you might pay out 25% of that dollar in federal income tax and then have 75 cents left for consumer purchases. If instead you contributed that same dollar to your contributory retirement plan, 100 cents would be available for that contribution. The government has given you, in effect, an interest-free loan equal to your highest tax bracket to invest for yourself.

- *Individual Retirement Accounts (IRAs).* These may include tax deductible or non-tax deductible

contributory plans. But, all such retirement planning vehicles grow tax deferred until withdrawn during your retirement years. They are meant for retirement, so a 10% early withdrawal penalty is assessed if money is withdrawn prior to age 59½.

Exceptions are made in the case of disability or if a beneficiary withdraws after the death of the owner. The most intriguing of such plans is the Roth IRA where the withdrawals are made *totally tax-free\** during retirement.



As a **business owner**, you can use various retirement planning vehicles. The big news this year is that all defined contribution retirement plans now allow for maximum contributions up to *25% of net income!* This is a wonderful opportunity to build substantial wealth and security. Someone said recently to us, "My business and my home are my retirement plans." Very true, but the problem there is that both are illiquid investments. That means they must be sold in order to raise cash. Retirement plans are liquid investments and readily can throw off income and make principal distributions for retirement living.

*continued on page 2*

*\*Roth owner must have held the IRA for 5 years before tax-free withdrawals are permitted.*

*Announcing:*

### The Private Trust Company, NA

**I**magine that you have worked your entire life building assets for your family and that you have had a terrific relationship with your trusted financial advisory firm. Then, upon your death, a bank takes over your financial affairs.

At first thought, that may seem comforting as the bank has perpetuity. But, the people at this big bank, well intentioned as they may be, are not the people with whom you've worked for so many years. Also, the personnel within that bank's trust department change with regularity. They have large caseloads and can't take the time to get to know your family or the needs of its member's.

That's exactly what happens in many estate plans. Your estate attorney knows this, and he or she sympathizes with your plight. But, until now, there wasn't any way around the problem when a trust company is called for in an estate plan.

Now that's changed!

Announcing The Private Trust Company, NA. This is a 50-state licensed, private trust company

*continued on page 2*

Koppers Building, Suite 300 • 436 Seventh Avenue • Pittsburgh, PA 15219 • 412-227-3200 • 1(800) 900-4492 • Fax (412) 227-3210

South Hills Office: Suite 420 • 2000 Oxford Drive • Bethel Park, PA 15102 • 412-835-3100 • Fax (412) 835-3108

North Hills Office: 10925 Perry Highway • Wexford, PA 15090 • 724-940-4088 • Fax (724) 940-4098

Securities offered through Linsco/Private Ledger

Member NASD/SIPC

## Saving Taxes Through Your Investments *continued from page one*



The correct type of retirement plan for your business will be decided based on several factors. Those include:

- Cash flow
- Employee retention and motivation issues
- Your age and compensation level as well as the age and compensation profile of your work force

We can help evaluate the right type of plan for your situation and work with your accountant, tax attorney and plan administrator to implement it.

### **After retirement plans, education savings ranks high for tax saving opportunities.**

The basic economic principles of *time and tax burden shifting* allow for a much cheaper cost of funding than the pay-as-you-go method or borrowing. Time and tax burden shifting are hallmarks of:

- Education IRAs
- 529 Plans
- Uniform Transfer to Minors Accounts (UTMA)
- Trust accounts

All of these allow for an asset allocated portfolio to go to work on behalf of your child's or grandchild's education funding. The tremendous growth compounding effects afforded by the use of time allows for the creation of education dollars that would otherwise need to be found from future income. Simply stated, it's much better to pay 25 cents now and let it grow to \$1.00 than it is to find that dollar later on during the child's college years. Next, as is the case with retirement plans, money not sent away in taxes remains available to grow and pay tuition bills. That tax savings compounds along the way also.

### **The last tax savings vehicle to be discussed here is saving taxes through charitable gifting.**

That concept is well recognized. But, what is not so well understood or practiced is the concept of *tax burden shifting*

*or elimination as a part of the charitable gift itself.* For example, many of us make regular cash contributions to our church, synagogue or mosque. Yet, some-time during each year, we may also sell a security at a gain. (Yes, there are still securities at a gain!) What if, instead of paying cash to the religious institution, we contribute an appreciated security equal to the entire year's expected contributions? The contribution is the same. The tax deduction is the same. But, what is different is that we would not have to pay capital gains tax on the appreciation inherent in the gifted security! For many people, that's a savings of 15 cents on the dollar! Fifteen cents you didn't pay in taxes is 15 cents you get to keep.

Charitable gifting strategies can be as simple as gifting appreciated securities as described, or it can become as sophisticated as charitable remainder trusts. What is right for you can readily be determined by an understanding of what you are trying to accomplish in your financial planning along with an analysis of your current situation.

Retirement plans and planning, education funding vehicles and charitable gifting strategies are all part of what we bring to our work with our clients. Talk to your financial consultant at the Fragasso Group now to determine what's right for you. And, enjoy the tax savings that the Internal Revenue Code has been programmed to provide to you!

*Note: All analysis should be done and decisions made in conjunction with your accountant or tax attorney. Also, the above information is not meant as specific tax advice. Rather, it is geared to begin a dialogue and probing that may lead to tax savings for individuals who thoroughly analyze their investment and tax situation with the assistance of their investment and tax professionals.*

## **Announcing: The Private Trust Company, NA** *continued from page 1*

that is wholly owned by Linsco/Private Ledger, our clearing broker/dealer. With the addition of this tremendous planning resource, you and your family can have the comfort of appointing a financially solid trust organization with perpetuity. And, you can also continue to have your investments and financial instruments managed by the very people who have worked with you all these years to build those assets – The Fragasso Group, Inc.

The cost is reasonable, your flexibility is preserved and, most importantly, there is no break in the communication and understanding of your family's needs. The Private Trust company can work efficiently with both living and testamentary trusts in all 50 states.

To learn more about The Private Trust Company, NA, contact your financial consultant at The Fragasso Group, Inc. If you are not currently a client of our Group, call Robert

Fragasso at 412-227-3200 or 1-800-900-4492 or email him at [robert\\_fragasso@fragassogroup.com](mailto:robert_fragasso@fragassogroup.com). Estate attorney inquiries are welcomed.

You will be remembered by the manner in which you leave your financial and estate affairs as much as by the way in which you accumulated those assets. Make sure that the arrangements are truly what you want and not fashioned in the haste that often accompanies estate planning.

## RETIREMENT PLAN SPONSORS :

# ERISA Keeps You On Track, But Evaluation Is Your Job

**W**e all have bad habits. Procrastination is an example of one that plagues many of us. Most of the time, it's harmless enough. After all, who can't say that they've put a high-priority item on hold while a "crisis" issue arose and quickly took its place.



**Nicole Cavoti**  
Financial Consultant -  
Corporate

For retirement plan sponsors, the task of evaluating of the plan is one example of an item

that can end up getting bumped for seemingly higher priority issues, despite good intentions.

The problem is, this postponement *isn't* always harmless. Your employees need you, and as their "fiduciary," you have a big hand in their financial success or failure in retirement. The recent years' poor stock market performance is casting more light on that fact, as employees seek someone to blame.

"Because of the losses participants have suffered over the last three years, the likelihood of litigation has increased. Prudence hinges on process, not performance." noted Richard M. Todd, a *CPA Journal* contributor in the April 2003 issue. "The process of ongoing evaluation is a fiduciary requirement," Todd continues in his article.

And, as if that's not enough pressure, ERISA chimes in, too.

ERISA (The Employee Retirement Income Security Act) does its job to keep fiduciaries and retirement plan sponsors on their toes by creating certain minimum standards to assure that employee benefit plans are established and

maintained in a fair and financially sound manner.

The Department of Labor has principal jurisdiction over Title I of the Act, which requires persons and entities who manage and control plan funds to:

- manage plans for the exclusive benefit of participants and beneficiaries;
- carry out their duties in a prudent manner and refrain from conflict-of-interest transactions expressly prohibited by law;
- comply with limitations on certain plans' investments in employer securities and properties;
- fund benefits in accordance with the law and plan rules;
- report and disclose information on the operations and financial condition of plans to the government and participants;
- provide documents required in the conduct of investigations to assure compliance with the law.\*

And after all, evaluation gives you the opportunity to change what could be wrong. The past is the past, but if you think your plan has suffered unduly from what may be limited investment choices, high fees or insufficient service and employee financial education, now is the time to determine that and change it.

*For information on conducting a free retirement plan analysis or sponsoring a complimentary employee financial education program, contact Nicole Cavoti at 412-227-3205 or by email at [nicole\\_cavoti@fragassogroup.com](mailto:nicole_cavoti@fragassogroup.com).*

*\*Source: HR Next, The ERISA Facts Guide*

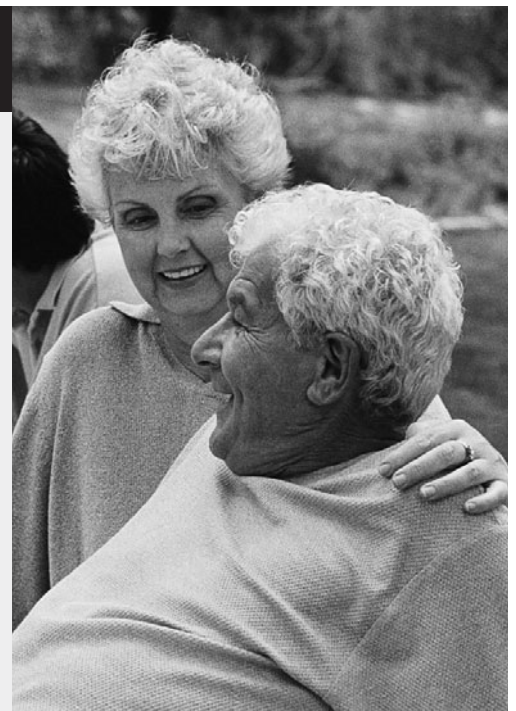
## Your Company's Retirement Plan

**T**he retirement plan that your company offers is one of the best ways to save for your future financial security. First, the employer's contribution and the employee's contribution are made before taxation. So, 100% of the money goes to work for the employee. Second, the growth of that capital in the plan compounds without current taxation. Finally, the funds can be withdrawn during retirement in a fashion that best meets the employee's needs and only the withdrawals are taxed. The remainder continues to grow tax-deferred.

A very comforting picture – provided that the plan and its assets are managed properly. That word "properly" refers to a three-pronged approach that is meant to provide retirement security for all participants.

The first consideration is proper plan utilization. Is the plan you have the best choice for your company's needs, employee makeup and time frame? Is it up-to-date in light of current law? For example, money purchase pension plans are out dated for most sponsors given a change in contribution formulas for other types of defined contribution plans.

*continued on page 4*



## Our Revamped Web Site Is Even More Valuable For You

The Fragasso Group is proud to announce the re-launch of its web site. As a result of comments and suggestions from our clients, we have redesigned our site to not only be more esthetically appealing, but also to



**Lauren LaManna**  
Manager, Seminar &  
Marketing Department

add greater functionality. We have worked to overhaul our web presence so that you can more easily access vital information and take full advantage of our convenient online services. The Fragasso Group site continues to be located at its original web address: [www.fragassogroup.com](http://www.fragassogroup.com).

### *So what's new at [www.fragassogroup.com](http://www.fragassogroup.com)?*

■ **Better Organization:** Our site has been redesigned so that it is easier to navigate and locate the information that you need faster. Our homepage

offers you quick access to our Personal Financial Services for individuals and Corporate Financial Services for businesses.

■ **More Information:** We have improved our ability to inform and educate clients with on-line content. Learn more about college savings vehicles, estate planning tools, trusts, and much more.

■ **Added Features:** We have added features to offer you the most up-to-date and meaningful information.

➤ **Market Watch:** Allows you to monitor the market climate using the top three indices: the S&P 500, the Dow Jones Industrial Average, and the NASDAQ.

➤ **Market Highlights:** A weekly market commentary is available every Friday to provide you with information on U.S. financial markets, European markets, international and U.S. fixed income markets.



➤ **Account View:** We have update our account view to give you easy and effective on-line access to your account information. You can easily set up your account to view account balance, positions, and transactions.

➤ **News:** Search our archives of quarterly newsletters as well as monthly E-news and articles published in business and industry publications.

➤ **Seminars:** This section allows you to view descriptions of upcoming financial planning courses given by The Fragasso Group. You can also register online as well as download maps to any of the seminar locations.

➤ **Life Goals Data Form:** You now have two ways to submit your data form to create a personal financial plan: download the Life Goals Data Form PDF file or you can submit it online through the secure site.

The enhanced look and features of our web site will play a key role in making the most current information available for the benefit of our clients. Implementing our new web site is just another step in using the Internet to foster client communication and build relationships.

## Your Company's Retirement Plan

*continued from page 3*

The second consideration deals with the management of the plan's investment assets. Is this being handled in the most professional method possible? Is the portfolio asset allocated in a way to reflect the reward/risk trade off that is appropriate for a plan such as yours? Does it consider the current economic climate? Is performance measured and is it compared to appropriate benchmark indices to gauge if the plan is on track to provide the desired results? Is there a written criteria for the selection of investments and managers? Have an Investment Policy Statement and Guidelines been established?

And, the third consideration reflects the education provided to plan trustees and to plan participants. Trustees must know and address the rules governing plan management. Participants must be educated so they are able to make the proper investment selections in keeping with their family's needs, risk tolerance and time frame. This last effort is mandated by federal retirement plan law. (ERISA, Section 404(c)).

We specialize in providing plan sponsors with guidance in all three phases of plan evaluation, management and education. *Contact Nicole Cavoti at (412) 227-3205 or 1(800) 900-4492 to schedule an initial consultation.*

## Stock Options:

### *Why You Might Want To Exercise, Even If They're Barely Above Water*

Given the recent downturn in the market, we hear many disparaging words from our clients regarding the stock options on which they used to depend for enhanced wealth. In many



**Deborah Sales**

*Managing Director,  
Operations*

cases, the options that were granted years ago have only a small profit compared to the market value of the stock today. Thus, there seems to be little motivation on behalf of the employee to exercise their stock options.

But wait, maybe there is a very GOOD reason to exercise those options now.

First, you must consider that there are two different types of stock options issued by companies. Non-Qualified stocks options (NQ) and Incentive Stock Options (ISO's). When a NQ is exercised, the spread between the exercise price and the current market value is immediately taxable to the employee at ordinary income tax rates. Conversely, when an ISO is exercised it is not immediately taxable to the employee. Better yet, provided that the employee holds the shares of stock for one year after exercise and two years after the grant date,

they will benefit from a lower long-term capital gains tax due on the difference between exercise and ultimate sale price. That long-term capital gains treatment could mean a tax savings as much as 57% (15% vs. 35%) over the short-term capital gains tax that would otherwise be due.

For the purpose of this article, we are going to focus on the benefits of exercising Incentive Stock Options in today's market environment. Although for diversification purposes we typically recommend the exercise and immediate sale of company stock options, there may be some cases where exercise and hold may make more sense.

Let's assume that in 2000 you were granted 1000 stock options of XYZ stock with an exercise price of \$10 per share. You are now fully vested in those stock options, but the market price for XYZ is only \$15 per share. So, with an intrinsic value of \$5 per share you feel that it is not appropriate to exercise the options. You think the stock will return to its 52-week high of \$25 per share, and when it does, then you'll exercise those options.

If you're willing to bet that the stock will reach \$25 per share at least one year from now, then this strategy may work well for you.

Consider exercising your ISO's at \$10

per share. It will cost you \$10 x 1000 shares = \$10,000 to exercise the options, but no taxes will be due upon exercise. The shares are already worth \$15,000 at today's market price but you think they're worth more, so you hold on for a year. After one year of ownership, you find that your intuition was right and that the stock is now selling at \$25 per share, as you suspected it would. After a 12-month holding period you can sell the 1000 shares of XYZ stock and realize a gain of \$15,000 (\$25,000 market price - \$10,000 exercise price = \$15,000 gain) that is subject to a 15% long-term capital gains tax. Had those shares been sold prior to the 12-month holding requirement, short-term capital gains would be due at your ordinary income tax rate, which can be as high as 35%. So, by exercising "early" and holding on, you saved yourself approximately \$3,000 in taxes.

You should consult with a tax professional prior to utilizing this strategy as the tax benefits may be minimized if you are subject to Alternative Minimum Tax, or other conditions exist. We recommend that you coordinate with your financial advisor and your tax preparer to determine the proper time and amount of stock options to exercise in any given year.

## The First-Ever Pennsylvania Animal Rights Seminar

A "must-attend" seminar for those who want to:

- Get tips on how to strategize civil and criminal matters involving animals
- Hear successful approaches to protecting your clients and their pets
  - Learn how to advocate for your clients in these issues
  - Gain insight into this developing area of law
  - Come away with fresh perspectives for your cases
  - Explore a variety of increasing important legal issues your clients encounter today!



**Tuesday, July 15, 2003**

City-County Building  
ACBA Auditorium  
Grant Street, Pittsburgh, PA

**9:00 a.m. to 1:15 p.m.**

Registration beginning at 8:30 a.m.

Attorney's can earn up to 4 Substantive Continuing Legal Education Credits

For tuition and registration information, contact the Pennsylvania Bar Institute at **1-800-932-4637** or visit their website at **www.pbi.org**



## A Caution In Switching Variable Annuities

Some investors have come to us owning variable annuity contracts issued by insurance companies that have experienced a downgrading of their credit rating. They wish to switch those annuities from the company that caused their concern to one that is more credit-worthy. Certainly, the first step is to determine the investment merit of such a switch, and that is left to a case-by-case analysis. However, once the decision is made to switch from one insurance company's annuity to one issued by another company, the most tax-wise method of doing this must be determined.

While all such decisions should be made with the guidance of your accountant or tax attorney, the following will assist you in making the most tax advantageous choice.

If your annuity is at a gain, the usual course of action recommended is to accomplish a "1035" exchange. That title comes from the IRS code Sec. 1035 that allows for a tax free exchange of one insurance contract for another. This happens without current taxation of the gain provided the contract particulars are the same. That means same owner and same insured or annuitant.

However, if your contract is at a loss vs. your cost basis in

the contract, you may want to cash it out and then reinvest the proceeds in a new and better contract. By doing this, you can deduct the market loss on the current year's tax return as an ordinary income loss. This is much more beneficial than a capital loss, which limits the deductibility against ordinary income to \$3,000 per year. An ordinary income loss allows for the full loss to be deducted against your earned income in the year the loss is realized.

Also, if your annuity contract is at a loss, and you are cashing it out prior to age 59½, there will be no early surrender penalty assessed by the IRS as such penalties apply only against gain in the contract. The old contract may have a surrender penalty accessible by the issuing company if it is still in the first few years of its existence. However, those penalties usually diminish and disappear over time. And, sometimes a modest penalty can be preferable to the worry over potential credit problems with the insurance company.

If you wish to have a current contract evaluated as to the credit worthiness of the issuing company or relative to any other feature of the contract, please contact us for a no-cost, no-obligation analysis.



**The  
Fragasso  
Group, Inc.**

Securities offered through Linsco/Private Ledger  
Koppers Building, Suite 300  
436 Seventh Avenue  
Pittsburgh, PA 15219-1818

PRESORTED  
STANDARD  
U.S. POSTAGE PAID  
Pittsburgh, PA  
Permit No. 1890