Citi Personal Wealth Management

Financial Insights from Your Advisors at:
Citi Personal Wealth Management

Fall 2011

Citi Personal Wealth Management

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Looking for Lifetime Retirement Income?

You're retired. You are worried about outliving your nest egg. Your bonds aren't generating enough income. You don't have a traditional pension plan that pays you a monthly check. Social Security covers only part of your regular expenses.

What you might need is an annuity. And that's when the confusion begins.

The problem: The term *annuity* covers a variety of products—and it's crucial that you make the right choice. With that in mind, here are three types of annuity to discuss with your Financial Advisor.

1. Immediate fixed annuity. Want income you can't outlive? One option is an immediate fixed annuity that pays lifetime income. You hand over a chunk of cash to the issuing insurance company and, in return, get a check every month for as long as you live.

You might view an immediate fixed annuity as an alternative to buying bonds. Both will give you a stream of regular income. But the annuity might pay you more—though the extra income comes at a price. If you die soon after purchasing the annuity, you will receive precious little income in return for your big annuity investment. Your heirs could still get a payout—but that depends on the annuity options you choose.

For instance, you could buy an annuity that pays income for a minimum of 10 years or that guarantees to return at least your original investment. But keep in mind that these bells and whistles will usually mean reduced monthly income. As with other annuities, the income you receive hinges on the insurer's claims-paying ability.

2. Variable annuity with living benefits. Immediate annuities typically provide a fixed stream of income. By contrast, a variable annuity has the potential to grow. Its value will change based on the performance of the underlying investments you have chosen.

You can use a variable annuity to supplement other sources of income by adding a living benefit for an additional fee. These benefits can guarantee payments for as long as you live, and the payments could rise if your investments perform well. Keep in mind, however, that these benefits come with conditions. For example, you could lose the guarantee by taking excess withdrawals. Remember also that the income is guaranteed by the insurance company and is based on its claims-paying ability.

3. Tax-deferred fixed annuity. These annuities pay interest until the end of the annuity's term, at which point your original investment plus the accumulated income is returned to you. All the income taxes due are deferred until then.

A tax-deferred fixed annuity might make sense for a conservative investor who wants to set aside some money for later in retirement and would benefit from the tax deferral. Keep in mind that you typically can't get your money back before the end of the annuity's term without incurring a penalty.

It's important to understand that a variable annuity is a long-term, tax-deferred investment that is designed for retirement. Its value and rate of return will fluctuate with the performance of the investment options you choose within the annuity. An annuity allows you to create an income stream that can be fixed or variable. The performance of investment options within the annuity are subject to investment risk, including the potential loss of the money you've invested. A variable annuity has contract fees and charges.

Taxable distributions (and certain deemed distributions) are subject to ordinary income tax and, if taken prior to age 59½, may be subject to a 10% federal income tax penalty.

Benefits are subject to state availability. See the prospectus for complete information

All annuity and life insurance guarantees are based on the claims-paying ability of the issuing insurance company.

Bonds are affected by a number of risks, including fluctuations in interest rates, credit risk and prepayment risk. In general, as prevailing interest rates rise, fixed income securities prices will fall. Bonds face credit risk if a decline in an issuer's credit rating, or creditworthiness, causes a bond's price to decline. High-yield bonds are subject to additional risks such as increased risk of default and greater volatility because of the lower credit quality of the issues. Finally, bonds can be subject to prepayment risk. When interest rates fall, an issuer may choose to borrow money at a lower interest rate, while paying off its previously issued bonds. As a consequence, underlying bonds will lose the interest payments from the investment and will be forced to reinvest in a market where prevailing interest rates are lower than when the initial investment was made.

Bolster Returns—With Better Cash Management

Stocks are struggling. Bond and savings yields are modest. How can you boost your returns? You might add another weapon to your arsenal: careful cash management.

The idea is to become more sophisticated in how you cover your living costs so you earn extra interest, collect credit card rewards, save on borrowing costs and avoid unnecessary tax bills. To that end, here are a few pointers:

1. Credit cards. Your credit cards may offer rewards programs that can help you earn frequent-flier miles, tickets to concerts and even cash rebates. If you use one or two cards for all your everyday spending, you can build up rewards points fairly quickly.

Using credit cards also allows you to postpone paying for purchases for perhaps a month or more without incurring interest costs, though you should pay close attention to each card's terms. In the meantime, the money you have earmarked to pay for these purchases could be sitting in an interest-earning account. This strategy works best if you pay off your card balances in full every month. If you don't pay the balance in full, the charges you incur will likely be greater than the financial advantages you enjoy by using the cards.

2. Bank accounts. Do you keep a lot of money in a low-yield bank account in case of a financial emergency? Consider allocating some of this money to bonds, which likely pay somewhat more interest.

To be sure, if you need cash for an emergency, you may find you no longer have enough in your bank account or money market fund. But you could always sell some of your bonds—though there's a risk they may be worth less than the price you paid for them.

3. Taxable accounts. Let's say you are reluctant to sell your bonds, preferring to wait and see whether they rebound in price. You also don't want to unload other investments because selling would trigger a big capital gains tax bill.

Another possibility: You might borrow against the value of your portfolio or home. More aggressive investors sometimes hold investments in a margin account so they can borrow against their value to purchase more investments. But when you borrow against your portfolio, you don't necessarily have to buy more investments.

Instead, you could use the money to, say, buy a new car or pay an unexpected tax bill. These "nonpurpose" loans can be attractive because the interest rate charged is often relatively low and approving the loan may take only a few days.

Be warned: Nonpurpose loans come with risk. If your portfolio drops in value, your losses could quickly grow and you might receive a margin call. At that point, you would need to add more securities or cash to the account or sell some investments to pay back part of the loan.

You also might explore borrowing against your home's value through a home equity loan or line of credit. Let's say you want to borrow $25,000 to upgrade your kitchen. You might arrange a home equity loan. The interest rate charged should be lower than the rate on a credit card or an unsecured personal loan. Keep in mind that repaying such loans will increase your monthly expenses, so carefully consider whether you can handle the debt payments involved.

4. Retirement accounts. If you are under age 59½, you usually can't tap retirement accounts, such as your IRA or 401(k), without incurring early withdrawal penalties. True, you might be able to borrow as much as $50,000 from your 401(k). But if you leave your employer, you must repay these loans immediately or you could incur taxes and penalties.

Similarly, you may be able to withdraw your Roth IRA contributions (but not the subsequent investment gains) without tax consequences. But withdrawing your contributions means losing the potential tax-free growth on this money.

What to do? You may want to funnel some of your monthly savings into a regular taxable account. That way, if you suddenly need cash, you'll have money you can access without worrying about tax penalties.

Although a money market fund seeks to preserve the value of your investment at $1.00 per share, it is possible to lose money by investing in the fund. An investment in the fund is not insured or guaranteed by the Federal Deposit Insurance Corporation or any other government agency.

Remember, when investing in mutual funds and variable annuities, please consider the investment objectives, risks, charges and expenses associated with the funds and separate accounts of the annuity carefully before investing. You may obtain the appropriate prospectus by contacting a Financial Advisor. The prospectus contains this and other information, which should be carefully read before investing.

A Home Equity Line of Credit is a form of revolving credit in which your home serves as collateral. Home equity plans typically involve variable interest rates rather than fixed rates.

Costs to obtain a home equity line.
Many of the costs in setting up a home equity line are similar to those you pay when buying a home. For example: a fee for a property appraisal, which estimates the value of your home; an application fee, which may not be refundable if you are turned down for credit; up-front charges, such as one or more points (one point equals 1% of the credit limit); other closing costs, which include fees for attorneys, title search, mortgage preparation and filing, property and title insurance as well as taxes; certain fees during the plan; for example, some plans impose yearly membership or maintenance fees; you also may be charged a transaction fee every time you draw on the credit line.

Borrowing against securities may not be suitable for everyone. If the value of the securities should decline below a minimum level, you may be subject to a collateral call without specific advance notice, requiring you to deposit additional cash or securities. If you cannot do so, all or a portion of your collateral could be liquidated, and a potentially taxable event could result. You are not entitled to choose which securities are sold or any extension of time to meet a collateral call. A concentrated portfolio holding a single or a few securities may be subject to greater risk of a collateral call than a diversified portfolio; a diversified portfolio will tend to be less subject to a sharp decline resulting from the negative performance of a single security. Availability, qualifications and other restrictions may vary by state. Ask your advisor for details.

Surprise: 5 Financial Planning Insights

Do you really need a financial plan? It might seem like a laborious exercise, with lots of questions to answer and financial information that needs to be gathered.

But as a reward for your efforts, you could uncover some startling insights into your financial situation. Here are five possible surprises.

1. You own lots of investments, but you're poorly diversified. Over the years, you might have collected a dizzying array of investments. Your financial plan may reveal that, quite apart from making your portfolio unwieldy, these investments, taken together, don't form an intelligent portfolio.

To get back on track, consider overhauling your investment mix to create one that includes a well-rounded array of asset classes, including large and small U.S. stocks, developed foreign markets, emerging markets, high-quality bonds, and possibly alternative investments. By combining a diverse collection of investments, you won't avoid short-term losses, but you could reduce your portfolio's overall volatility. But keep in mind that investments include risks and possible loss of principal. Alternative investments (e.g., hedge funds, private equity) are speculative, not suitable for all clients, and intended for experienced and sophisticated investors who are willing to bear the high economic risks of the investment. Small-cap stocks carry greater risks than investments in larger, more established companies.

If the overhaul is done in a tax-deferred account, such as an Individual Retirement Account, you can make the necessary trades without worrying about tax consequences, as long as you don't make a withdrawal. If you're dealing with a taxable account, you might talk to your Financial Advisor about ways to help minimize taxes as you remake your portfolio.

2. Your kids' college fund is wrecking your retirement. You are determined to have enough for your children's college costs, so you're socking away every dollar you can into a 529 college savings plan. Meanwhile, however, your financial plan may indicate you aren't setting aside nearly enough for your own retirement.

But failing to save enough won't just imperil your retirement. It could also mean missing out on valuable tax benefits and possibly a matching employer contribution in your 401(k) plan. An added bonus: Money in retirement accounts typically doesn't dent eligibility for financial aid.

Indeed, thanks to financial aid, you may discover you don't have to pay the full cost of college. Even if your children don't qualify for grants and scholarships, they could always take out student loans. By contrast, to pay for retirement, you typically need cold, hard cash.

3. You might be saving too much. While many Americans are struggling to amass enough for retirement, your financial plan might suggest you have the opposite problem: You're saving too much.

This may not seem like a problem. But if you're putting aside too much money for retirement and other longer-term goals, you could be missing out on experiences that might enrich your life today, such as travel, charitable contributions and evenings out with friends.

4. Your insurance coverage has holes. Maybe, when you last looked at your life insurance, you had enough coverage to take care of your spouse and pay off the mortgage if you died.

Since then, however, you've had kids, bought a larger house and perhaps started your own business. By drawing up a financial plan, you will have a better sense for whether your life insurance coverage matches your situation.

Your plan may also reveal that you need disability insurance in case you can't work for an extended period and a long-term care policy for nursing-home expenses. The latter may not be needed for many years, but the annual premiums should be lower if you first buy the policy when you are younger.

5. You're headed for an estate tax problem. This year and next, the federal estate tax exemption is $5 million for individuals and $10 million for couples. Don't have nearly that much wealth? Estate taxes could still be an issue for three reasons.

First, your financial plan may indicate that your wealth could grow substantially between now and the time of your death, so estate taxes could indeed be a problem. Second, unless Congress acts, the federal estate tax exemption will revert to $1 million in 2013. Finally, even if your estate isn't taxable at the federal level, it could be subject to estate taxes at the state level, so you should probably seek advice from a qualified tax professional.

Diversification does not guarantee a profit or protect against a loss.

A change to your current policy may incur charges, fees and costs. A new policy will require a medical exam.

Since life insurance and long-term care insurance are medically underwritten, you should not cancel your current policy until your new policy is in force. Your actual premiums may vary from any initial quotation you receive. A change to your current policy may incur charges, fees and costs. A new policy will require a medical exam. Surrender charges may be imposed, and the period of time for which the surrender charges apply may increase with a new policy. You should consult with your own tax advisors regarding your potential tax liability on surrenders.

Before entering into a plan, consider how you will pay back any money you might borrow. Some plans set minimum payments that cover a portion of the principal (the amount you borrow) plus accrued interest. But, unlike the typical installment loan, the portion that goes toward principal may not be enough to repay the debt by the end of the term.

Preparing Your Portfolio for Higher Taxes

The bad news: Higher federal income taxes may lie ahead. The good news: You have more than a year to get ready—and you might want to start making adjustments in 2011.

Yes, Congress extended the Bush-era tax cuts at the end of 2010. But it didn't extend those cuts past 2012, which means higher federal tax rates in 2013 can't be ruled out.

Even if the Bush-era tax cuts are extended again, upper-income Americans are already looking at higher taxes in 2013, thanks to a special Medicare tax increase included in the 2010 health care law. The 3.8% Medicare tax, which can also hit investment gains, will affect couples with modified adjusted gross income of more than $250,000 and individuals above $200,000.

To prepare yourself for the possibility of higher taxes, consider a twofold strategy.

1. Shift income into 2011 and 2012. Without a new law, the long-term capital gains rate will rise from 15% in 2011 and 2012 to 20% in 2013. Even if the 15% rate is extended, high-income families may be hit by the Medicare tax. One implication: If you have appreciated stock in your taxable account that you're contemplating selling, you may want to sell in 2011 or 2012, or possibly split the income between the two years.

Similarly, if you have a traditional Individual Retirement Account, you might consider converting it to a Roth IRA so you can pay the conversion tax at today's lower income tax rates. Converting may make sense if you expect to be taxed at the same or a higher rate in retirement—and you have funds outside your IRA to pay the tax bill on the taxable sum converted. If you pay any taxes triggered by the Roth conversion with money from your IRA, you may end up incurring both income taxes and a tax penalty.

A Roth conversion could also be appealing if you plan to bequeath your IRA. If you have a Roth, you don't have to take required minimum distributions, as you do with a traditional IRA, so you could leave the account intact for your children or other beneficiaries. Your children will need to take annual distributions. But as designated beneficiaries, your children could tease decades of tax-free growth out of their inherited Roth if they're careful.

2. Make the most of tax-favored investments. If tax rates do go up, municipal bonds may become more attractive. For example, a 3% municipal bond has a tax-equivalent yield of some 4.6% at today's top federal rate of 35%. But if the top rate rises to, say, 40%, the tax-equivalent yield would climb to 5%.

While you're at it, look into increasing your retirement account contributions so you can shelter ongoing gains from both the Medicare tax and any future general tax increases. In 2011, you can contribute as much as $16,500 to a 401(k) plan, or $22,000 if you are age 50 or older. Meanwhile, this year's maximum IRA contribution is $5,000, or $6,000 for those age 50 and above. Going forward, all these contribution limits will increase based on an inflation index.

Also, think carefully about which investments you buy within your retirement accounts. It typically makes sense to use IRAs and 401(k) plans for tax-inefficient strategies, such as buying taxable bonds and real estate investment trusts, which tend to generate a lot of immediately taxable income.

To that list, you might want to add dividend-paying stocks. High-income earners may have to pay the Medicare tax on dividends starting in 2013. Also, Congress might not extend the special tax treatment for qualifying dividends beyond 2012. Currently, dividends are taxed at a 15% maximum federal rate. But without a new tax law, they could once again be taxed as ordinary income, which could push the top rate to over 40%.

Looking for more year-end tax tips? Ask your Financial Advisor for our 2011 tax-planning checklist.

Q&A With Peter Orszag

The federal government's budget deficit has emerged as perhaps this year's most hotly debated political issue, thanks in part to the wrangling over the debt ceiling and Standard & Poor's decision to lower its credit rating for U.S. Treasury bonds.

For a fresh perspective on the issue, we turned to Peter Orszag, Citi's vice chairman of global banking. Peter previously served as President Obama's director of the Office of Management and Budget. He has also worked as director of the Congressional Budget Office.

Q: In your writings, you've mentioned that growth tends to be sluggish in economic recoveries that follow a severe financial crisis. Can the U.S. avoid that fate—or is it pretty much a sure thing, given the depressed state of the U.S. housing market and the amount of consumer debt?

Peter Orszag: History suggests it'll be a hard slog. That means we need to adjust expectations. It also means we should put more emphasis on fixing the housing sector. From a macro perspective, I'm most concerned about clearing the excess inventory of housing, because that's depressing home prices. For instance, you might create a government program to transform some properties into rentals, so the properties aren't weighing on the market, or you might accelerate depreciation on residential housing held by investors.

With regard to fiscal policy, we need to emphasize both fiscal stimulus in the short term and deficit reduction in the long term. Creating a path to a sustainable long-term fiscal situation will help confidence. The lack of a credible long-term fiscal path would make short-term stimulus less effective than it could be.

Q: We hear a lot about the need to raise the eligibility age for Social Security, cut back benefits or both. But isn't Medicare the real problem?

PO: Medicare and Medicaid spending is currently equal to around 5½% of GDP, while Social Security is a little under 5%. By 2050, Social Security goes from 5% to 6% of GDP, while Medicare and Medicaid go from 5½% to 12%. It's important to deal with Social Security. But the major problem is health care, particularly the high costs incurred by a relatively small number of patients. A quarter of Medicare participants account for 85% of the program's expenses.

Q: Do you think it's inevitable that Americans will pay more in taxes in the years ahead?

PO: Over the next 10 to 15 years, it's difficult to see how we get to a sustainable fiscal situation without more revenue, in part because any changes to entitlement programs are likely to be phased in slowly. But to reach a sustainable fiscal situation between now and 2050, we will need to address spending, especially spending on health care.

Q: What do you think the aging population will mean for economic growth and the typical retirement age?

PO: An aging population means slower growth because the work force will grow more slowly, unless we have a change in immigration policy. Meanwhile, for the bulk of the population, there's no question in my mind that we should be encouraging people to work longer. It's good for the country, but it's also good for individuals. When I look around, the people who remain most active are the ones who seem to be enjoying their later years the most.

Q: If you were advising folks who were preparing for retirement, what steps would you suggest they take?

PO: You clearly want to save enough. But there are also three other issues that people approaching retirement should think about: how they might tap into the equity in their home, how they can protect themselves against outliving their assets and how they might pay for long-term care costs. There are already products available that can help you address these issues, such as reverse mortgages, lifetime-income annuities and long-term care insurance, although each of them has shortcomings. As demand for these products picks up, I hope the choices will improve in the years ahead.

Forecasts may not be attained. The views of the interviewee may differ from the views of Citi Personal Wealth Management.

Reverse Mortgages are complex; be sure to understand all the terms and conditions (including the Total Annual Loan Cost) and consequences of reverse mortgages.

7 Mental Mistakes to Avoid

When markets drop, we might lose money. Perhaps a bigger problem: We often also lose sleep, lose perspective—and end up straying from the strategy we settled on in calmer times.

Has this year's market turmoil jangled your nerves? It is, alas, all too easy to get emotionally caught up in the markets' day-to-day price swings. Still, by understanding some of the mental mistakes identified by behavioral finance experts, you might find you're better able to cope with market turmoil. Here are seven common mistakes.

1. Suffering losses. Research suggests we get far more pain from losses than pleasure from gains, which is why bear markets can be so painful. Our aversion to realizing losses can stop us from selling rotten investments that we ought to get rid of.

Sometimes, however, our fear of losses can be a helpful trait. Many investors hate to sell when their investments are underwater, instead hanging on to losing positions, hoping to get even, then get out.

This loss aversion can keep us invested in stocks during a bear market, so we potentially benefit from any market recovery. We might become anchored on the price we paid for our investments or the highest price they got to, and we're reluctant to sell until our investments return to those levels.

2. Sitting tight. Our reluctance to sell is also fueled by status quo bias, our preference for staying put rather than changing.

But failing to change can sometimes be risky. Imagine you have a big position in a single stock. It might be shares that you inherited or that you received from your employer through stock options. While sitting tight may feel like the right thing to do, it could be wise to sell your big stock position and spread the proceeds among a broader collection of stocks and possibly other investments.

3. Extending trends. We often read too much into recent market action. For example, when stock prices rise, we may extrapolate the trend and assume shares will continue climbing. This can prompt us to load up on stocks even though prices are significantly higher than they were just a few months earlier.

4. Feeling cocky. We tend to think we're smarter than we really are and that we know more than we really do. Our overconfidence can climb along with the markets, as we attribute our portfolio's gains to our own brilliance. This may lead some folks to trade excessively and to take on too much risk.

5. Predicting the past. In retrospect, it might seem obvious that stocks would weaken this year after the big gains since early 2009. Indeed, it's easy to forget about all the bullishness among investors earlier in 2011 and convince ourselves that we foresaw the summer market slump. This so-called hindsight bias can further bolster our confidence, possibly prompting us to make bold market forecasts and then act upon them, even though past performance is often a rotten guide to future results.

6. Seeking confirmation. We tend to latch on to evidence that supports our beliefs, while discounting contradictory evidence. For instance, bullish investors will ignore bad economic news, while bearish investors will dismiss positive developments.

7. Raising risk. During bull markets, our appetite for risk can balloon because of the "house money" effect. Like casino gamblers who get lucky early in the evening, we may feel like we're ahead of the game and we can afford to take more risk.

Trouble is, the house-money effect—coupled with our overconfidence and tendency to extrapolate market trends—may lead us to take excessive risk late in a bull market, potentially setting us up for nasty losses if the market turns lower.

Investment results may vary. The investment strategies presented are not appropriate for every investor. You should review each individual client's situation, including the terms, conditions, fees, charges, expenses and risks involved with specific products or services.

Investments are subject to market risk, fluctuation in value and possible loss of principal. Before investing, investors should consider whether tax or other benefits are only available for investments in the investor's and designated beneficiary's home-state 529 College Savings Plan.

Sources: To read more about behavioral finance, see Behavioral Finance and Wealth Management *(Wiley, 2006) by Michael Pompian and* Why Smart People Make Big Money Mistakes *(Fireside, 2000) by Gary Belsky and Thomas Gilovich.*

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Past performance is no guarantee of future results.

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There may be additional risk associated with international investing, including foreign, economic, political, monetary and/or legal factors, changing currency exchange rates, foreign taxes, and differences in financial and accounting standards. These risks may be magnified in emerging markets. International investing may not be for everyone.

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