

BEYOND THE HORIZON

1st Quarter , 2006 Issue

IN THE NEWS

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Look for our new website coming in February 2006 — you'll find us at www.horizonfinancialadvisors.com.

As we have in past years, the first quarter issue reports the tax rules and limits for the new year. The following are those for the **2006 TAX YEAR** (not the return you are about to file):

- **Federal income tax rates** will not change but the brackets widen a bit, adjusted for inflation.
- The **standard deduction** for 2006 will be \$10,300 for married individuals filing jointly (plus \$1,000 for each spouse age 65 or older); \$7,550 for heads of household (plus \$1,250 if age 65); and \$5,150 for single filers (plus \$1,250 if age 65).
- Already effective for 2005, a taxpayer can no longer claim Head of Household status for merely providing 50% support for a child who lived with them. A child must be a “qualifying child”, who is defined as being under age 19, under age 24 if a full-time student, or any age if disabled.
- **Personal exemption** increases to \$3,300 per person.
- Maximum **contribution limit for Traditional and Roth IRAs** remains at \$4,000 for 2006. However, the additional “catch-up” contribution for those age 50 or older **increases to \$1,000** for a total maximum contribution limit of \$5,000.
- For those covered in a plan at work, the income limits to **deduct Traditional IRA contributions** are not yet available. Per the IRS, they expect the deductibility to phase out at \$75,000–\$85,000 for marrieds and \$55,000–\$65,000 for singles, an increase from last year.
- Contribution limits for company-sponsored retirement plans change. The **401(k) contribution limit** increases to \$15,000 (plus a \$5,000 “catch-up” for those age 50 or older). The limit for **contributions to a Simple IRA** remains at \$10,000 (but the “catch-up” increases to \$2,500).

- The income caps for the **Hope and Lifetime education tax credits for 2006** are also not yet available from the IRS. They will most likely to be similar to or greater than the income caps for 2005, which had phase-outs beginning at \$87,000 for marrieds and \$43,000 for singles.
- Annual limit for **contributions to a Coverdell Education Savings Account** holds at \$2,000 per child. Remember, the contribution deadline is April 15th of the following year.
- The **annual gift tax exclusion increases to \$12,000** per recipient (up from \$11,000).
- The **estate tax exemption increases to \$2.0 million** (up from \$1.5 million).
- **Self-employed** individuals can continue to **deduct 100% of medical premiums** for coverage, including those paid for the family.
- The **Social Security wage base** for this payroll tax rises to \$94,200 in 2006.
- Those **collecting Social Security who are between the age of 62 and 66 can earn wages** up to \$12,480 without losing benefits. Those over 66 can earn an unlimited amount without losing benefits.
- The normal retirement age for Social Security holds at age 66 and will remain at age 66 for those born in the years 1943 to 1954.
- Annual cost-of-living increase for Social Security recipients will jump to 4.10%, a significant rise compared to the 2.70% increase for 2005.
- The **standard mileage** rate for 2006 will be 44-1/2 cents per mile for business miles driven; 18 cents for medical or moving purposes; and 14 cents for charitable miles driven.

2006 OUTLOOK

Let's first recap 2005. For the most part, last year was very much like what we expected, though stock market returns pulled back going into the last few weeks of the year. In 2005, economic growth came in at a respectable rate of 4.20%. The Federal Reserve increased short-term rates SEVEN times during the year for an additional increase of 1.75% in 2005 alone. Despite rising interest rates, continued turmoil in Iraq, an unexpected natural disaster named Hurricane Katrina, and resulting oil prices hitting record highs, the S&P 500 and NASDAQ managed to produce modest gains of 3.00% and 1.37%, respectively. The Dow Jones Industrials fell short, however, coming in at a 0.61% loss for the year. [WE EARNED AN AVERAGE RETURN OF 6.89% LAST YEAR (net of advisory fees) for our "growth" clients for whom we manage brokerage accounts held by TD Waterhouse.]

As we head into 2006, we begin to discern what we anticipate for the coming year in terms of the economy and the markets. In our preliminary assessment of what is being forecasted for 2006, modest changes are expected. According to Kiplinger, we should see continued

economic growth (though at a slower pace) in GDP, employment, retail sales, and corporate earnings. However, increases in energy prices, inflation, though at a slowing pace, and the rising trade deficit, will act as opposing factors. Falling auto sales and easing housing sales will also help to impede growth.

Concerns over energy prices, interest rates, and a slowdown in the housing market have been getting quite a lot of press. So we'd like to briefly address each of these concerns. It is likely we will see additional spikes in oil prices by mid-year due to tightening supplies. Any unexpected turn of events in the Middle East could push oil to \$100 a barrel, and \$3.00 a gallon at the pumps would not be out of the question. Consider, though, that we have already survived a 500% increase in oil prices over the past five years with a 50% increase occurring in the last six months alone. Rising energy prices have not crippled us economically. We've proven we can survive another spike if it occurs.

As for housing, data shows that much of the equity pulled from the sale of large homes due to downsizing was not used for spending or fueling economic growth. Much of it has been sitting in cash, so a slowdown in housing alone should not have an impact on economic growth.

Lastly, we address rising interest rates. We should remind ourselves that rising interest rates are a result of a growing economy. That's a good thing! The increases are to prevent the economy from growing too fast. The new Fed chairman, Ben Bernanke, does have a reputation of focusing on fighting inflation, even more so than his predecessor, Alan Greenspan. Nonetheless, we anticipate rate hikes to come to an end, possibly by Spring. (Ironically, as soon as rates stop rising, the doomsayers will cry that a slowdown is coming.) The forces above act to stifle economic growth, though one factor alone will not cause a significant impact over the long-term.

Despite the muted growth anticipated, there are ALWAYS OPPORTUNITIES TO MAKE MONEY, though some come with added risk. We feel that opportunities lie in the global and technology sectors. Half of global investing is now outside the United States. Contrary to overall muted growth expected for the U.S. and Europe, other countries around the world are experiencing growth, like Latin America who is benefiting by energy. Other countries are making progress due to long-term efforts that have been in place. Diversification globally is important because many industries are no longer well represented in the U.S. or are no longer represented by the best of an industry. In 2005, many mutual funds that were diversified globally outperformed their domestic equity counterparts.

Technology, on the other hand, has been an out-of-favor and, understandably, feared sector. However, indications are this sector is poised for a recovery. Technology companies have built up cash. Tech spending budgets are increasing. Global competitive pressures are driving prices down. The NASDAQ 100 index has already begun to break out of its trading range and has been showing improvements since November. Market technicians feel that for the bull market to continue, we need a change in the "hot" sectors - away from energy, gold, and real estate.

In every market, there are always winners and losers. Though we may not be predicting robust gains, we're confident we won't see big setbacks. Remember, the markets price based on what's next. It's important to appreciate what is NOT happening as well as what IS happening. For 2006, we're anticipating another year of positive returns for stocks. Despite not having a

crystal ball, we anticipate that gains will again be modest and likely to be single digit returns. But it won't be positive across the board. Proper allocation, as well as good stock and fund selection, will be key. It may be time for rebalancing or allocation changes. As an investor, take this opportunity to re-assess your goals and objectives. As always, patience is key! Leave the worrying to the professionals.

INVESTMENT CORNER

There are many variable annuity products on the market. What is a variable annuity? It is a long-term investment product designed for retirement purposes. Variable annuities are known for their ability to provide tax-deferred earnings, guaranteed death benefit options, guaranteed life payout options, and investment options that allow you to participate in the bond and equity markets. Transamerica, a leader in the variable annuity industry, now offers two unique riders that can be added to their variable annuities — "5 for Life" and "5 for Life with Growth".

Both riders, which can be added for an additional cost to the policy, offer investors the ability to receive a **guaranteed stream of income for life OR a guaranteed rate of growth** to produce a guaranteed stream of income later. In addition to providing a guaranteed lifetime income, the rider lets the investor lock in potential market gains and protects the guaranteed income from down-market performance.

The "5 for Life" riders on the Transamerica variable annuities were designed to help investors meet the retirement income challenge. Today, retirees need to plan for possible longer life expectancies. In our opinion, this type of investment could be suitable for those seeking a guaranteed stream of income at retirement, along with the ability to earn additional growth or gains typically not available with traditional pensions. Because of the death benefits available, these riders can also provide the opportunity to leave any remaining contract value to beneficiaries upon death.

There are fees associated with this investment as well as risks associated with the investment options. Highlighting this topic in no way implies that it is suitable for everyone. Please refer to the prospectus for complete details. FOR MORE INFORMATION ON THIS OR OTHER INVESTMENT PRODUCTS OR TO RECEIVE A COPY OF OUR FORM ADV, PLEASE CALL OUR OFFICE.

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