BEYOND THE HORIZON

1st Quarter, 2007 Issue

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Just a reminder that you can find this and other newsletters on our website at www.horizonfinancialadvisors.com.

IN THE NEWS

Our first quarter issue reports the tax rules and limits for the new year. The following are those for the 2007 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 2007 will be $10,700 for married individuals filing jointly (plus $1,050 for each spouse age 65 or older); $7,850 for heads of household (plus $1,300 if age 65); and $5,350 for single filers (plus $1,300 if age 65).

- A reminder that a taxpayer can claim Head of Household status only if a "qualifying child" lives with them. A "qualifying child" is defined as being under age 19, under age 24 if a full-time student, or any age if disabled.

- **Personal exemption** increases to $3,400 per person.

- Maximum **contribution limit for Traditional and Roth IRAs remains at** $4,000 for 2007. **The additional "catch-up" contribution** for those age 50 or older **holds at $1,000** for a total maximum contribution limit of $5,000.

- For those who participate in an employer retirement plan, **taking the deduction for IRA contributions may be limited.** The income phaseout is $83,000—$103,000 for couples and $52,000—$62,000 for singles. Where only one spouse is active in a plan, the income phaseout is $156,000—$166,000.

- There are income limits for making **Roth IRA contributions.** The income phaseout for couples is $156,000-$166,000 and for singles is $99,000-$114,000.

- Contribution limits for company-sponsored retirement plans increase. The **401(k) contribution limit** will be $15,500 (plus a $5,000 "catch-up" for those age 50 or older). The limit for **contributions to a Simple IRA** increases to $10,500 (with the "catch-up" holding at $2,500).

- The income phaseout for the **Hope and Lifetime education tax credits for 2007** begins at $94,000 for marrieds and $47,000 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 holds at** $12,000 per recipient.

- The **estate tax exemption also holds at** $2.0 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 $97,500 in 2007.

- Those **collecting Social Security who are between the age of 62 and 66 can earn wages** up to $12,960 without losing benefits in 2007. 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 for 2007 will be 3.30%, slightly less than the 4.10% increase last year.

- The **standard mileage** rate for 2007 increases to 48-1/2 cents per mile for business miles driven and 20 cents for medical or moving purposes. The allowance for charitable miles driven remains steady at 14 cents.

Sources: Internal Revenue Service website; Social Security Administration website; The Kiplinger Tax Letter Vol., 81, No. 26.

2007 OUTLOOK

As we look in the rearview mirror at 2006, it certainly was a good year for the stock markets. The Dow Jones Industrial Average led the pack gaining 16% for the year, as investors flocked to the big caps as a result of the economic slowdown. The S&P 500 followed close by at 14% with the Nasdaq coming in at 10%.

As for 2007, we expect healthy returns once again for stocks, but not as healthy as 2006. Large caps are expected to continue to lead with the small caps taking a backseat after outperforming for the past five years. Tech stocks are due for a comeback but perhaps more so in 2008 than this year. Businesses are planning to update their hardware and networks, which they haven't done in great stride since the Y2K scare. Healthcare is also due to regain leadership. Though politics have held these stocks back in the short-term, demographics certainly point to high demand over the long-term. Lastly, defense contractors should be at an advantage moving into the new year. Defense spending for 2007 is expected to exceed $500 million, which is about 16% of the total Federal budget. This far exceeds defense spending of past Administrations.

As for the bond market, quality is favored over the high-yield issues at this point. An economic slowdown does not have a favorable impact on high-yield issues. As for foreign issues, the central banks overseas are not done raising rates. Therefore, U.S. bonds are more predictable at this point.

In terms of the economy, the economic slowdown will continue, perhaps leveling off sometime this summer, keeping a recession at bay. The U.S. automakers will continue to struggle. Toyota is expected to take the lead from GM this year, becoming the world's largest automaker. The sharp correction in housing should also level off. Fortunately, consumer spending is expected to remain steady. Oil prices will again rise above the current level of $55+ per barrel, probably spiking around $80 in the summer. However, they should end the year closer to $60, which puts the national average of gasoline around $2.30 per gallon. As for interest rates, the Federal Reserve is expected to hold rates steady, contrary to earlier suspicions of rate cuts.

As we have communicated with clients during 2006, overall the picture is not a bleak one for investors - and certainly not as bleak as the media tends to portray. Here's a thought — If the markets are doing well despite rising interest rates, spikes in oil prices, and a slowing economy, just imagine how well equity investors could fare if interest rates and oil prices remained steady and the economy continued to chug along at a modest growth rate?

Sources: The Kiplinger Letter Vol. 83, Nos. 50 & 51; Financial Planning, January 2007 issue.

FOR YOUR INFORMATION . . .

- Savings bonds issued in 1977 or earlier should be redeemed this year since they are no longer earning interest.

- TD Ameritrade account numbers will be changing sometime around Presidents' Day (February 2007). Notices will be sent to clients in advance of the change.

- For the 2006 tax return you are about to prepare, remember to take the tax credit on the Federal return for the telephone excise tax refund. You will do so on Line 71 of the 1040, Line 42 of the 1040 A or on Line 9 of 1040 EZ.

- Another reminder while you're preparing your 2006 tax returns —– contributions made to a 529 College Savings Plan are deductible from taxable income on your Pennsylvania state return.

- For the 2006 and 2007 tax years only, those over 70-1/2 can donate their required IRA distribution to a charity without having to claim the distribution as income on their tax return.

- A WORD OF CAUTION to our Annuity clients— There is a company soliciting individuals with a postcard informing them that they have an annuity coming due. The return address on the card is "Annuity Service Center located in Medina, OH." Please be advised this is a solicitation and has nothing to do with annuity policies you may own.

- For those who own employer stock held in a 401(k) plan, you now have the option of divesting out of employer stock and into other choices offered in the 401(k) plan. Additionally, employers can no longer mandate that company matching of employee contributions be directed into employer stock.

INVESTMENT CORNER

In light of recent tax law changes surrounding the 529 College Savings Plan, we choose to again highlight this investment strategy. Why choose the 529 over other investment plans to save for college?

- Earnings in a 529 plan can grow tax-free.
- Withdrawals used to pay qualified higher education expenses are also free from Federal tax.
- Pennsylvania now allows a deduction from income of contributions made to your 529 (not to exceed $12,000 per year).
- Anyone can contribute to a 529 regardless of their income.
- You, not the child, maintain control of the assets.
- You can contribute up to $12,000 ($24,000 for married couples) each year without gift tax consequences or as much as $60,000 ($120,000 for married couples) at one time under a special election.
- Since many institutions and mutual fund companies offer 529 plans, you have a wide selection of investment vehicles to use for the plan.

Though 529 plans have been available for many years, two recent tax law changes make them even more attractive. Under the Pension Protection Act passed last August, the tax-free nature of the earnings for Federal income tax purposes became permanent. Originally, the law allowing the tax-free earnings was due to expire in 2010. Additionally, Pennsylvania passed a law last summer allowing taxpayers to deduct the contributions from their taxable income, retroactive back to January 1, 2006.

There are downsides to the 529s. Withdrawals that are NOT used for qualified education expenses are subject to ordinary income taxes and a 10% Federal tax penalty on the earnings. Additionally, you cannot take the Hope or Lifetime Education Tax Credit on the same dollars used as a tax-free distribution from a 529. For financial aid purposes, assets set aside in college savings plans will be considered as assets to be used for educational expenses. However, it is our understanding that grandparent-owned 529s do not have to be reported for financial aid purposes.

Another type of plan designed to save for college is the Coverdell Education Savings Plan. It is similar to the 529 in that it also offers tax-free advantages. The differences are in terms of control, contribution limits, and cost, among other things.

If you have questions or would like more information on the 529 plan or other types of college savings plans, please call our office.

Highlighting this topic in no way implies that it is suitable for everyone. There may be fees and/or risk associated with investing in a 529 plan. FOR MORE INFORMATION ON THIS OR OTHER PRODUCTS, PLEASE CALL OUR OFFICE.

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