

THE BUTTONWOOD



Third Quarter 2006



On May 17, 1792, twenty-four merchants gathered under a buttonwood tree at 68 Wall Street.

There they signed the *Buttonwood Agreement*, creating the first investment community, which later evolved into the New York Stock Exchange.

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OUTLOOK

By Gail Gardner, CFP, ChFC

As we approach the end of the year in the financial sector, thoughts naturally turn to such questions as “how will the year end” and “what can we expect going forward?” There are a lot of mixed signals on the horizon, and as a result, predictions are conservative and cautious. The major players in the near term are the housing market, interest rates and oil. Since the housing market appears to have peaked, with inventories up around 50% and prices declining for the first time since the early 1990’s, there are plenty of pundits throwing around the “R” word. Since World War II, they claim, housing bubbles have typically ended in recession. On the other hand, it is likely that the Fed is done hiking interest rates and may actually have to lower them at some point in 2007, to give our asset-driven economy a little steam.

The threat that higher gas prices would result from imposing economic sanctions on Iran has been delayed. That, coupled with a mild 2006 hurricane season, has helped provide some relief in gas prices. The retail sector should benefit during the upcoming holiday season, as lower gas prices mean more disposable income for the consumer. I recently returned from a trip to the

Detroit area, where I noticed gas prices were around \$2.10/gallon for regular unleaded. That sounded like a bargain to me when a gallon of gas here was \$2.60-2.70. However, the land that I remember from the 90’s as recession proof has been anything but that. Since 9/11, I am told, the Detroit economy has never fully recovered. As in other places, housing prices are down and there is a swelling glut on the market. If there aren’t enough takers in Ford’s buyout plan then many jobs are likely to go on the chopping block. According to a *Realty Times Market Condition Report* (September 25, 2006), Detroit already has the highest unemployment rate of any metropolitan area in the country.

Aside from the problems in Detroit, however, business overall appears to be doing well. Earnings are strong and growth has been positive. Conventional wisdom tells us to expect a strong fourth quarter in a mid-term election year. However, fears about the uncertainty of our oil supply appear to be consistently priced into the market, and that leaves us vulnerable to future volatility as the ongoing saga in the Middle East evolves. Put all these factors together and about the best you can predict is that we should finish the year on a moderately strong note, and expect growth to be slower in 2007 than in the past two years. I intend to set my sights low and hope for a pleasant surprise.

2006 Income Tax Planning

By Gail Gardner, CFP, ChFC

In addition to making plans for the upcoming holiday season, another thing to think about this time of year is income tax planning. Charitably inclined? How about donating appreciated stock to your favorite charity this year in lieu of cash? If you still want to hold the stock, you can buy it back at the current price with a higher basis. Are you over 70.5, but don't need the income from your required minimum distribution, either now or in the future? For 2006 and 2007 only, the IRS will allow you to contribute up to \$100,000.00 of your IRA plan dollars to a qualified charity without any income tax consequences. Of course, you don't get a deduction, and the donation has to go directly from the trustee of your plan to the charity.

Thinking about selling a mutual fund that you've held at least 12 months? Do it before the dividend date and avoid the ordinary income taxation. The stock will have a higher selling price, to reflect the upcoming dividend, but it will all be treated as capital gain. Even better, if you have any losers in your portfolio that you don't think will come back, sell them to offset the capital gain from the fund sale. In the unlikely event that you sell a security that you plan to repurchase, be sure to wait at least 30 days to avoid the wash sale rules. If you pay quarterly income taxes and you

expect your marginal tax bracket to be lower next year, consider paying your fourth quarter state tax bill before December 31st. That makes the payment deductible in the current tax year. Of course, this strategy will only work if you itemize and are not in danger of becoming subject to the Alternative Minimum Tax (AMT).

If you plan to include some weeding and cleaning in your pre-holiday preparations, there are some new rules with respect to donations of clothing and household items. Those items donated after August 17th, 2006 that are not in "good or better" condition, will no longer be deductible. In addition, both the value and condition of donated items should be documented.

Still have money left in a flexible spending account? Make sure you use it before year-end or you'll lose it! You can clear out your unused balances by purchasing a new pair of glasses or contacts, by filling prescriptions early, or by taking care of any medical or dental procedures you've been putting off. And make sure you've been reimbursed for the medical expenses you've already incurred this year. Before implementing any tax planning ideas, it's important to consult your tax advisor, since any number of the recommended adjustments could affect your status for Alternative Minimum Tax (AMT) calculation, the tax status of your social security income, or the status of other deductions and contribution limits.

Have you been in recently to review your portfolio? If not, please contact us to schedule a meeting.