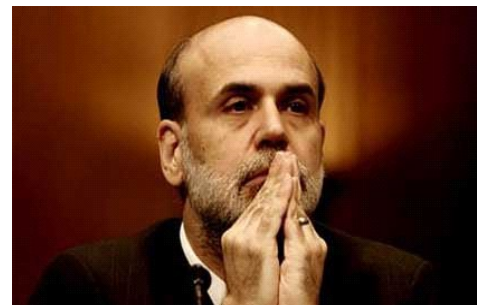




MARKET UPDATE

DOW -634 +429 -519 +423: All in One Week!

August was a historic month for investors as they witnessed the first ever downgrade of the U.S. credit rating by a major credit rating agency. The downgrade came as a surprise to many, but S&P was clear that political brinkmanship displayed throughout the debt ceiling debate played a pivotal role in the downgrade. This downgrade, coupled with a continued Euro Zone debt crisis and fears of a global economic slowdown led to a dive in global stock markets. While volatility in the markets reached levels not seen since the "flash crash" in May of 2010, they did not reach the levels seen during the Fall of 2008, and for that we are thankful! Stock markets did stage a late month rally, but could not make up for the amount lost early on, with the S&P 500 ending the month down (5.68%) and (3.08%) for the year.



The irony of the U.S. credit downgrade was that U.S. bond prices went up as yields fell dramatically. This is contrary to common logic in the event of a credit downgrade. With an increase in perceived risk of an investment, the typical response would be a rise in yield and a lowering of price. In this case, the assumption is that the U.S. will have to tighten its financial belt, which may slow down the economy. This slowdown could have a negative impact on company earnings, and as investors fled stocks, they invested in money markets and cash. All of this money has to go somewhere, and much of it went to buy short term U.S. bonds, thus the rise in U.S. bond prices.

Economic data was mixed as GDP for the 2nd quarter was revised down to 1.0%, which made many concerned over a new recession. The employment situation was also dealt a blow as it was widely reported that no jobs were added in the month of August. Another concern was a drop in consumer confidence, which was blamed on the recent fall in stock prices, the east coast earthquake, hurricane Irene, and the debt downgrade. Given the number of events, we can understand why consumers are less confident.

Investment Outlook Summary

Asset Class	Outlook	Commentary
Cash / Stable Value	<ul style="list-style-type: none"> – In general, higher than normal levels of cash 	Even though money market rates are basically zero, having investments with high safety and liquidity provides access when opportunities arise, and stability when markets turn volatile.
Bonds / Fixed Income	<ul style="list-style-type: none"> – In general, slight underweight level of bond exposure – Cautious of Treasuries for the long-run – Positive on Treasury Inflation-Protected Securities (TIPS) – Positive on emerging market bonds 	<p>Many bond mutual funds have enjoyed great gains, along with record inflows from investors during this latest "flight to safety." It may be time to look for fixed income investments outside of the traditional mutual fund.</p> <p>Primarily used for safety, but with yields at historic lows and the risks of future inflation present, treasury owners may not be paid adequately for the potential risk.</p> <p>Essentially, these are treasury notes with an interest rate tied to inflation. Used for safety, but the future interest paid will increase with inflation. TIPS continue to perform well.</p> <p>As this asset class develops and matures, there will be great potential for investors over the coming years.</p>
Stocks / Equities	<ul style="list-style-type: none"> – In general, underweight to normal levels of stock exposure – Positive on dividend paying stocks – Utilizing covered call strategies to hedge – Selective of international stocks – Positive on Korea, Brazil, Canada and Australia. Cautious of China – Avoid much of Europe, the U.K., and Japan 	<p>Pullbacks should be seen as an opportunity to increase stock exposure to neutral levels, that is neither underweight nor overweight.</p> <p>Many of the traditional dividend paying companies are more attractively valued than the general stock market. <i>A number of large companies are now paying a dividend that is higher than the yield on the 10 year US Government bond, some are even higher than the 30 year.</i></p> <p>Covered call options strategies can provide extra income to your portfolio while you own stocks.</p> <p>International diversification is still very important to your portfolio, however individual country selection will likely play an increasing role in international stock performance.</p> <p>While the long term opportunities remain with emerging market economies, resource rich countries like Canada and Australia provide the building blocks the world needs in order to grow.</p> <p>Current solutions appear to be a band-aid to a much larger problem inherent in a shared currency. <i>Issues continue in Europe, recent news has increasingly affected the markets.</i></p>
Alternate Assets	<ul style="list-style-type: none"> – Positive on Gold and Silver – Negative on the Euro currency – Positive on energy trusts 	<p>Primarily used as an inflation and currency hedge. The risks of global currency dilution are present.</p> <p>Fiscal problems in Europe continue to be on center stage.</p> <p>Many energy trusts provide a good dividend source with the potential for capital gains.</p>

Italics denote a change from last month

The Income Tax Planning Landscape: 2011

At this time last year, income tax planning was particularly challenging. Several tax deductions had already expired, and significant changes, including new, higher income tax rates, were scheduled to take effect at the end of the year. Legislation passed in mid-December, however, hit the "reset" button, reinstating already-expired deductions, and extending major tax provisions--including lower rates--for an additional one to two years.

As a result of the December legislation, 2011 tax planning takes place in an environment characterized by something that was missing last year--a relative degree of certainty. That being said, here are some things to keep in mind as you consider your current tax situation.



Tax rates/calculation

Federal income tax rates--

The same six federal income tax rates that applied in 2010 will continue to apply in 2011 and 2012. So, depending on your taxable income, you'll fall into either the 10%, 15%, 25%, 28%, 33%, or 35% rate bracket. Remember, though, that all of your taxable income is not necessarily taxed at that rate--instead, the rate at which

you pay tax generally increases as your income increases. For example, if you're a single individual with 2011 taxable income of \$100,000, you fall into the 28% tax bracket. However, your first \$8,500 of taxable income is taxed at 10%, your next \$26,000 of taxable income is taxed at 15%, and your next \$49,100 in taxable income is taxed at 25%. Only \$16,400 of your taxable income is actually taxed at 28%.

Rates for long-term capital gains and qualifying dividends--As in 2010, long-term capital gains and qualifying dividends continue to be taxed at a maximum rate of 15% through 2012; if your income (including any long-term capital gains and qualifying dividends) puts you in the 10% or 15% income tax brackets in 2011 and 2012, a special 0% rate will generally continue to apply.

Alternative minimum tax (AMT)--While regular income tax rates and the maximum rates that apply to long-term capital gains and qualifying dividends were extended through 2012, the latest AMT "fix" (in the form of increased AMT exemption amounts) is effective only through 2011. So, if you think you may be subject to the AMT this year, the good news is that you know ahead of time what the relevant exemption amounts are (\$74,450 for married individuals filing jointly, \$48,450 for unmarried individuals, \$37,225 for married individuals filing separately); the bad news is that the AMT situation for 2012 remains up in the air. You can probably expect another AMT fix later this year, but as it stands now, AMT exemption amounts will drop significantly in 2012, dramatically increasing the number of taxpayers ensnared by this parallel tax system.

Temporary payroll tax reduction

Available for 2009 and 2010, the Making Work Pay tax credit was a refundable tax credit equal to the lesser of 6.2% of earned income or \$400 (\$800 for married couples filing joint returns); the credit was phased out for those with higher incomes. The tax credit was not extended to 2011, but the December legislation created a new one-year 2% reduction in employee Social Security payroll taxes (the 2% reduction also applies to the self-employment tax paid by self-employed individuals).

So, if you're an employee, 4.2% of your 2011 wages (up to the 2011

taxable wage base of \$106,800) is being withheld for your portion of the Social Security retirement component of FICA employment tax instead of the 6.2% that would normally be withheld. If you're self-employed, the 12.4% you would normally pay for the Social Security portion of your 2011 self-employment tax is reduced to 10.4%. So, if you earn \$100,000 in wages, you'll have an extra \$2,000 in take-home pay for 2011. Consider opportunities to take advantage of this extra income by, for example, increasing your retirement savings; applying the extra money toward a long-term goal could extend the benefit of this temporary tax reduction beyond 2011.

Other considerations

IRA qualified charitable distributions--Unless Congress passes additional legislation, 2011 will be the last opportunity for individuals age 70½ or older to make qualified charitable distributions (QCDs) of up to \$100,000 from an IRA directly to a qualified charity. These charitable distributions can be excluded from your income, and count toward satisfying any required minimum distributions (RMDs) that you would otherwise have to take from your IRA for 2011.

Depreciation and IRC Section 179 expensing--If you're a business owner or self-employed individual, you're allowed a first-year depreciation deduction of 100% of the cost of qualifying property acquired and placed in service during 2011. The "bonus" first-year depreciation deduction drops to 50% for property acquired and placed in service during 2012.

Small business stock--Generally, you can exclude 50% of any capital gain from the sale or exchange of qualified small business stock provided that you meet certain requirements, including a five-year holding period. For qualified small business stock issued and acquired in 2011, however, you'll be able to exclude 100% of any capital gain from income if the qualified stock is held for at least five years and all other requirements are met.

Energy efficient improvements--Though not as generous as it has been the last two years, a credit is still available to individuals who make energy-efficient improvements to their homes. You may be entitled to a 10% credit for the purchase of qualified energy-efficient improvements, including a qualifying roof, windows, skylights, exterior doors, and insulation materials. Specific credit amounts may also be available for the purchase of specified energy-efficient property: \$50 for an advanced main air circulating fan; \$150 for a qualified furnace or hot water boiler; and \$300 for other items, including qualified electric heat pump water heaters and central air conditioning units. There's a lifetime credit cap of \$500 (\$200 for windows), however. So, if you've claimed the credit in the past--in one or more tax years after 2005--you're only entitled to the difference between the current cap and the total amount that you've claimed in the past. That includes any credit that you claimed in 2009 and 2010, when the aggregate limit on the credit was \$1,500.

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SDW's TAKE

While Roth IRA *contributions* are still limited by Adjusted Gross Income, Roth IRA *conversions* became available for everyone regardless of income in 2010, this continues in 2011.

Depending on an individual's situation, a "synthetic" Roth IRA contribution can be made for those who make more than the AGI limit and currently do not have an IRA balance. This can be a complex endeavor with extra tax forms, please consult your tax advisor before acting upon this.

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