THE DANA VIEWPOINT

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Tax (Un)certainty

In tackling the topic of taxes and tax reform, we can certainly guarantee that this will not be one of the most entertaining or humorous Dana newsletters you will ever read. It has also taken most of the year to get to tax reform because having the light of day shined on the political machinations of tax policy is not comfortable for the 535 members of Congress. The way our democratic system works, members of Congress are incented to delay taking a stance, or a vote, on any issue for as long as possible. There is no value to a political contribution given after the issue in question has had a vote. We know this seems to be a pessimistic view. Lawmakers love to talk about what they might or might not do, but actually voting is often one of the most uncomfortable parts of their job. Once they have voted, the rationalization of the vote begins.

So here we are discussing tax reform as a country. Certainly the word "reform" can have positive or negative connotations, depending on whether you think the changes help or hurt. We almost hesitate to use the word "reform" when discussing Congress, because it seems to give them entirely too much credit. Reform often doesn't mean improve, and it almost never means simplify. The largest tax reductions in the plan come from reducing the corporate tax rate, reducing individual tax rates, and increasing the standard deduction. The largest tax increases, yes increases, in the plan come from eliminating personal exemptions (offset by a higher standard deduction), reducing deductions for mortgage interest and state taxes, and an excise tax on corporate funds held offshore. Dozing off yet? None of this seems to be making things simpler and the rewrites are in process now, so expect things to only get more complex. The problem with phase- ins, phase-outs, credits, and deductions is that they complicate economic decision making and add uncertainty. We all know uncertainty is a cost.

The other problem they have is that the tax code continues to get more progressive. In order to get tax cuts passed over the last few decades, those in the top income quintile cannot get tax cuts that are larger than the cuts for those with lower incomes. This has generally been true whether the party in power is republican or democrat. As of 2014, the top 1% of earners made

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20% of the taxable income and paid almost 40% of the income taxes. The next 49% of earners paid almost 58% of the taxes collected, while those in the bottom half of the income scale paid 2.7% of the income tax collected. In this environment, how do you provide a tax cut if it is not for the "haves"? We are sure the wrangling in Washington will not be pretty, and hopefully there will be progress to report before our next letter.

Turning to the Fed, the Federal Open Market Committee sets monetary policy. President Trump has the opportunity to have a lasting effect on this policymaking entity through his appointments. Trump recently appointed one member, and he will have the chance to appoint four more if Yellen doesn't stay on as a Governor. This policymaking body will look completely different than it did five years ago. Jerome Powell, the new Fed Chairman appointee, will have the longest tenure at five years on the Board. We hope they follow the physician's Hippocratic oath: First do no harm. But what policy path keeps the economy healthy? They have to be somewhat puzzled that inflation has stayed low even as the unemployment rate has moved down towards 4%. We hope they move cautiously and raise rates no more than the market expects.

Unemployment has moved lower, wages are increasing, we have had two quarters of real growth at 3%, and stocks continue to move higher. All of this while the dreaded Fed unwind has started and interest rates remain low. All things to be thankful for, along with fall, family, and football.

Happy Thanksgiving from our family at Dana

Random Thought for November 2017: "The hardest thing in the world to understand is the income tax."

- Albert Einstein

20700 SWENSON DRIVE • SUITE 400 • 53186 • P.O. BOX 1067 • BROOKFIELD, WI • 53008-1067 • 262.782.3631 • FAX 262-782-0581
365 ERICKSEN AVENUE.N.E. • SUITE 312 • SEATTLE, WA • 98110-1888 • 206.855.8781 • FAX 800.560.6227

E-Mail: dia@danainvestment.com
Web Site: www.danainvestment.com