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CLIENT BULLETIN

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➢ *Time to Choose*

The central issues of the presidential election next week are the scale and scope of government involvement in the U.S. economy, and how to prevent America from going down the path of a sovereign debt crisis. The questions stem not just from the rapid rise in federal government spending in recent years but also from worries about projected increases in future spending on government programs such as Social Security, Medicare and Medicaid. Rarely have candidate choices been this stark. In the last 50 years, only two other elections with a similar plot come to mind. In 1964, LBJ's vision of a Great Society encompassing vast new federal spending programs won the day. In 1980, a vision of smaller and less intrusive government championed by Ronald Reagan swept the election.

➢ *Running On Empty*

The average car and light truck on the road today is 11 years old, tying an all-time record. (Source: Experian Automotive)

➢ *Thanks Dad*

Bill Gates is ranked #1 as the richest American today with a net worth of $61 billion, but the six living heirs of Sam Walton, who died in 1992, are worth a combined $103 billion.

➢ *Taxmageddon is Coming*

Taxmageddon is a humorous term for a serious matter: the convergence of the expiration of the Bush-era tax legislation, coupled with the implementation of new investment taxes under the Patient Protection and Affordable Care Act (AKA Obamacare). The twin impact of these events can wreak havoc on an investment portfolio. Taxes on ordinary income next year go up by 24%; capital gains taxes rise by 59% and dividend income paid by corporations can be taxed as high as 43.4% next year – a 189% increase over the current 15% tax rate! The first line of defense in combating these taxes is the proper allocation of investments between tax advantaged and taxable accounts. In general, more tax efficient investments should be held in taxable accounts.

➢ *For the Record: Who Pays Federal Taxes?*

Warren Buffett's comment about paying a lower tax rate than his secretary makes good political fodder but it is misleading when looking at which income groups pay what percentage of the total tax liability overall. The federal income tax is designed as a progressive tax – the higher your income, the higher the tax rate. Whether it is currently too progressive or not progressive enough is of course a big topic of political discourse, but the chart below shows the facts about who pays what percentage of the total tax liability so you can form your own opinion.

Taxpayers	Income breakpoint	% of total federal taxes paid	Average tax rate
Top 1%	**$343,927**	**36.7%**	**24.0%**
Top 5%	**$154,643**	**58.7%**	**20.5%**
Top 10%	**$112,124**	**70.5%**	**18.0%**
Top 25%	**$66,193**	**87.3%**	**14.7%**
Top 50%	**>$32,396**	**97.7%**	**12.5%**
Bottom 50%	**<$32,396**	**2.3%**	**1.9%**

Source: The Tax Foundation, *Summary of Latest Federal Individual Income Tax Data*, October 24, 2011

➢ *If You Were King*

Keeping this chart in mind, let's role play for a moment – you have just been elected president of the United States. Your budget director brings you the numbers and they aren't pretty – three consecutive years of $1.3 trillion deficits with more red ink on the way for the foreseeable future and roughly $16 trillion of accumulated debt. You're going to focus on the revenue side first - you can take a whack at spending cuts next month – but for now you need more money! Taking a look at the table above you try to decide which group to raise taxes on. Take a moment to make your choice. The easy pickings' are of course – tax the rich - who could be against that. Two problems however – the top 5% of taxpayers already pays nearly 60% of the total taxes. You can't get blood from a stone. More importantly, you make a startling discovery - there aren't enough rich people in this country! Even if you raised their tax rate to 100% it wouldn't make a dent in your problem.

➢ *How about the bottom?*

Since the top of the income pyramid doesn't yield much you turn to the lower half of the pyramid – the 50% of people who pay little or no income taxes now. Surely this has to be fruitful since their tax-paying starting point is basically zero and half the country is in this earning category. Wrong again – even though there are a lot of people in this category, there isn't enough aggregate income to move the needle by taxing them more.

➢ *Be Like Jesse*

Finally you start to think like Jesse James who robbed banks because that's where the money was. Ah, the "middle class". Now you've hit the sweet spot – there are a lot of folks in this country earning between $32,396 and $154,643 and they make enough money that applying higher taxes to that income will really make a difference. This is the dirty little secret in politics – both parties know that they need to tax the middle class more but neither of them wants to say it because those taxpayers are also voters.