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Tax Tax Tax

When asked if we subscribe to the New York Times, a favorite reply is "No, we prefer our fiction in hardcover."

Oh that it could be so simple. Truth be told, once in a while we need to know what the old gray lady is saying, haggard and fading and partisan to a fault though she may be.

A recent Times article is a case in point. The piece, partially presented below, explores the possibility of the US instituting a wealth tax. This would be a new form of taxation presumably devised to soak the rich, pad government coffers, redistribute wealth, and punish the successful, all at once. But before we editorialize, here are excerpts from the article:

> *Income tax rates have recently been raised slightly for some affluent people, and there is pressure for additional increases. But some economists say raising marginal income tax rates on high earners may miss the mark.*
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> *One reason is that the truly wealthy employ all kinds of legal means to minimize their tax liability, including shifting income around the world, deferring gains on their assets and many other sophisticated strategies. Another, though, is that taxes on ordinary income simply don't apply to inheritance or investment, principal sources of wealth.*
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> *Taxing wealth in addition to income is one way to make sure that the rich contribute more to government coffers. That would essentially be a tax on household assets like property, stocks, bonds, unincorporated businesses, trusts, art and yachts.*
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> *The idea is to aim at the wealthiest part of the population, perhaps the top 1 percent, a group that has seen the most significant and consistent accumulation of wealth over the last few decades.*
>
> *Countries like Canada have a tax on asset appreciation, based on the value of the assets at the time of the owner's death. The United States does not, and the tax code contains a huge loophole through which to pass wealth to one's heirs.*
>
> *Here is how that can work in practice:*
>
> *A billionaire can borrow against his stocks, art and real estate, and spend that borrowed money without paying tax. All he has to do is pay interest on the loan. When he dies, his*

heirs can sell the assets to pay off the debt. Under an existing rule known as the "step-up in basis," no matter how much the assets have appreciated in value, no one will owe income tax on that gain. And the rest of his fortune goes to his heirs without anyone ever paying income taxes on the appreciation in the assets.

Partly to close loopholes like this, Ronald I. McKinnon, an economist at Stanford, advocates a wealth tax in addition to income tax. He outlined his proposal in a recent op-ed article in The Wall Street Journal titled "The Conservative Case for a Wealth Tax."

Professor McKinnon's plan would require households to list all domestic and foreign assets annually. There would be a $3 million wealth exemption, which, in his estimation, would exclude more than 95 percent of the population. The remainder would be subject to a flat tax of about 3 percent of household wealth.

In Europe, in addition to a wealth tax, many countries have a value-added, or consumption tax. Because the idea of a consumption tax is politically unpopular in the United States, he said in an interview, "I think the case is even stronger in the U.S."

"Plus," he added, "the income tax is a poor vehicle for hitting the wealthy."

Other economists say that a wealth tax would also address other problems.

"Wealth inequality and lack of access to opportunity is destroying the meritocratic aspects of our economy," said Daniel Altman, an economist at New York University and a former member of the editorial board of The New York Times. "That will cost us growth in the long run."

Mr. Altman proposes replacing the income tax with a wealth tax. He estimates that a flat wealth tax of 1.5 percent would be more than enough to replace the revenue from current income, estate and gift taxes. But he proposes establishing tax brackets according to wealth levels. For instance, no tax might be imposed for a household's first $500,000 in wealth, 1 percent for the next $500,000 and 2 percent for wealth above $1 million.

Proponents of a wealth tax also say it would encourage innovation and risk-taking because it wouldn't tax wealth in its early phases, but only after it has been amassed.

It is unclear whether the idea of a wealth tax will ever gain traction in the United States. But longtime deficit problems remain, and tax increases of some type may well be part of the solution. According to the Organization for Economic Cooperation and Development, the United States raised less tax revenue in 2010 as a proportion of gross domestic product than any other industrialized nation, aside from Chile and Mexico.

"Should we reform the income tax, the estate tax or bring in a third tax like the wealth tax?" asked Professor Shackleford at the University of North Carolina. "We have to do something. There's a tremendous amount of tax escaping because we don't tax the deceased and we don't tax the heirs."

Uncle! Enough already. If this does not make your blood boil, check for a pulse. This may be the most blatant re-distributionist propaganda the Times has ever published.

First, note the rhetorical barrage:
".. make sure the rich contribute more to government coffers "
".. aim at the wealthiest part of the population "
".. the tax code contains a huge loophole "
".. the income tax is a poor vehicle for hitting the wealthy "
".. destroying the meritocratic aspects of our economy "
".. tax escaping because we don't tax the deceased "

By the sound of it, America's successful are nothing more than modern day robber-barons, tax dodgers, and escape artists, and all the weapons of society should be aimed at the large target on their backs. Rubbish, pure rubbish.

Some of the 'experts' cited in the article should freshen up on the tax code. The US does in fact impose taxes on the wealthy deceased.. it is called an estate tax. This is a tax on money that has already been taxed when earned, then taxed again on any current income or capital gains. So the estate tax is taxation to the third power. And before we pile on the 'tax the rich' bandwagon, remember that the US tax code is already progressive, so much so that nearly half of all wage-earners pay no income tax.

A wealth tax 'only on the wealthy' and 'only a little bit' would quickly morph into a wealth confiscation and redistribution scheme. The income tax of 1913 was 'only a little bit'. The top rate was seven percent. Within five years the top rate was 77 percent. When it comes to taxation, there is no such thing as 'only a little bit', only a moving target.

It is a long way from a goofy idea to the passage of a wealth tax, but stranger things have happened. The 16th amendment permits taxation of incomes, not assets. But then again, before 1913 there was no income tax. The next idea floated might be a Value-Added Tax, or a National Sales Tax. Any of them would codify an expanded role of government in our economy, to the benefit of a bloated government, and to the detriment of our economy.

The danger here is a mindset that believes all assets, wealth, income in the nation may be claimed by the Federal government; that people serve the government and not vice versa. That is not Capitalism, not America, and not a safe idea.

Busting Gold

Be it viewed as a currency, a store of wealth, or an inflation hedge, Gold has one quality that is beyond dispute: for all practical purposes, Gold is indestructible. In a literal sense, you can smash it with a hammer, freeze it, melt it, then restore it to its original size and shape. Figuratively, you can replace it with fiat currency and pretend it is inconsequential. Yet as history has shown, Gold will outlast any paper currency the world may contrive.

So how do you bust Gold? Through the market's pricing mechanism. That's just what happened in April, when the yellow metal suffered its worst two-day drop in 30 years, a 14 percent collapse that sent it back to early-2011 levels.

Gold Spot Price January 2000-April 2013

Where does Gold go from here? Probably nowhere.
Oh sure, it continues to trade in an active global market, and has already recovered nearly half of its precipitous two-day decline. But this is most likely a trading bounce, nothing more. The metal peaked 20 months ago and is 22 percent off its high of $1900 per ounce. That is a bear market. The real Gold trade, the one that lasted over a decade, is probably over.

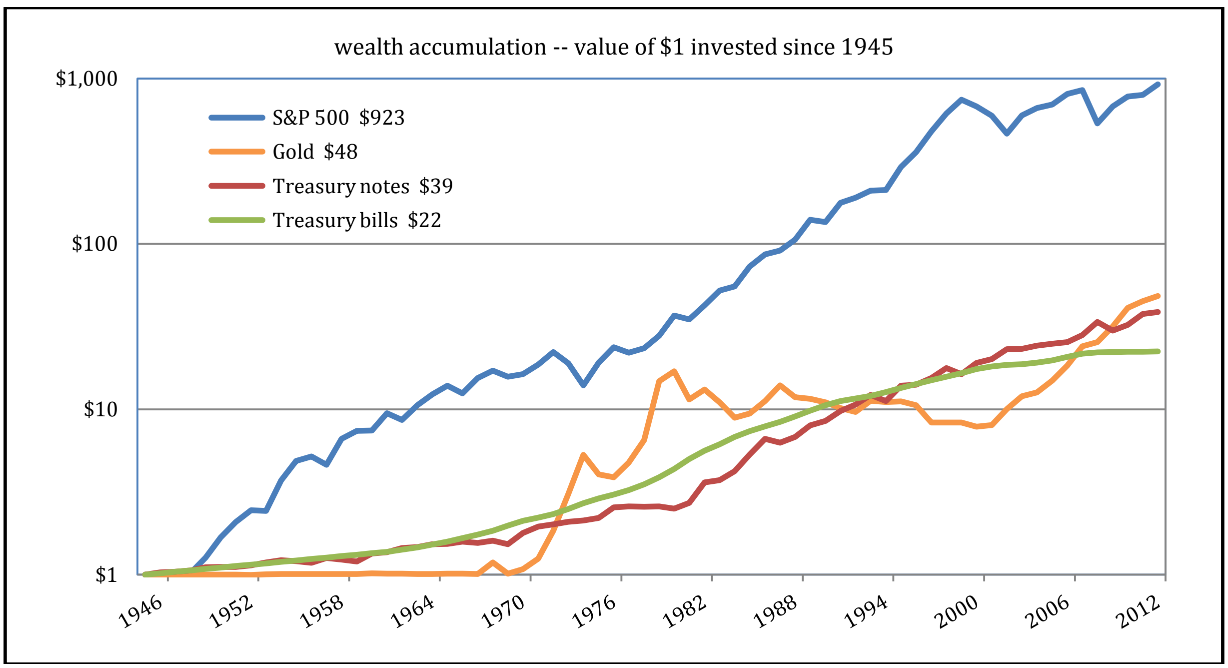
Here's why:
No matter the asset, all market moves are subject to price and time. Both are working against Gold. Gold prices rose for 12 consecutive years, a seven-fold increase in value for an asset that, as always, carries a zero yield and an infinite PE. At some point the trade -- buying a metal in hopes of someone paying more for it -- gets old.

In the US, the weak Dollar/free money policy is in the middle-innings, closer to its end than its beginning. For the past 12 years, money supply has grown at an average rate of eight percent; in each of the past two years growth was nine percent. Year-to-date, that rate has slowed to three percent. For now, money is cheap, but it is not easy. Japan and Europe will take the lead in flooding the market with money; this should provide support to the Dollar. Global commodities priced in Dollars once enjoyed a currency tailwind; that wind is either shifting or subsiding. Gold is not immune to this development.

Finally, Gold became the world's most crowded trade, and market action is telling us the game is over. While not absolute proof, that is still a powerful combination. To take the other side -- to be bullish on Gold -- would force an investor to both follow the crowd and fight the tape. There may be easier ways to lose money, but we cannot think of one.

From a longer-term perspective, Gold has outperformed Treasurys since 1945, despite having its price fixed for the first 25 of those years. Does that prove Gold to be the better investment? Hardly. There is no inherent reason for Gold to outperform Treasurys, or any other asset. It just happens now and again.

In contrast, there is a reason for stocks to outperform most assets. It does not happen every year or every decade, but it is the default setting. At today's prices, stocks offer investors modest value and potential gains; Treasurys offer little value; and Gold offers little of value plus zero yield. The Gold rush is ending.



Sources:
Barclays
Bloomberg
New York Times
Tax Foundation
Wall Street Journal
Zillow

Tidbits..

Minor budget cuts enforced as Sequester hits federal spending.
World does not end, US economy survives.

Short selling -- bearish bets on stocks -- hits six year low.
'VIX', market volatility index, drops to six year low.
In stock market, fear is replaced by complacency.

Time Warner to spin off iconic Time, Inc. publishing business, as print media continues to fade.

Federal Reserve stress test shows major US banks are well-capitalized.
US banking industry profits approach all-time record levels.
Profitable, well-capitalized, and unloved.

Household debt-service costs reach new lows, aided by defaults, foreclosures, low interest rates.
Credit card delinquencies drop to 18-year trough.
A newly liquid consumer, perhaps for all the wrong reasons, but still.

Cyprus becomes focal point of Euro failures, uninsured bank deposits to be severely taxed.
With no good option available, choosing the least-worst alternative.

Euro-area unemployment rate hits record level of 12.1 percent.

Hewlett-Packard Board Chairman Ray Lane to step down from leadership role, two other directors to leave the Board after barely winning re-election.
At HP, shareholder victories are mostly symbolic.

Bank of Japan ramps up its version of Quantitative Easing, Yen value plunges, equities rally.

J.C. Penney ousts CEO Ron Johnson after failed make-over of department store.
After a four-billion dollar sales decline, mounting losses, sinking stock.. someone had to go.

Job openings in US approach five-year high.
A rebounding job market, or a mismatch of worker skills versus employer needs?

Residential land values jump 13 percent in 2012, first increase since 2005.
Case-Shiller home price index rises nine percent in past year.
Zillow study warns homes prices may be rising too fast for household incomes.

Personal computer shipments fall by double digit percentages in first quarter.
A staggering drop, nobody gets excited about a new PC anymore.

US oil production reaches 21-year high.

Apple, Inc. completes largest bond issuance in market history, raises 17 billion dollars to help fund share repurchases.

US Income Tax hits 100-year anniversary. *Ughh.*