QUARTERLY NEWSLETTER • **4TH QUARTER 2017**

# Praetorian Guard

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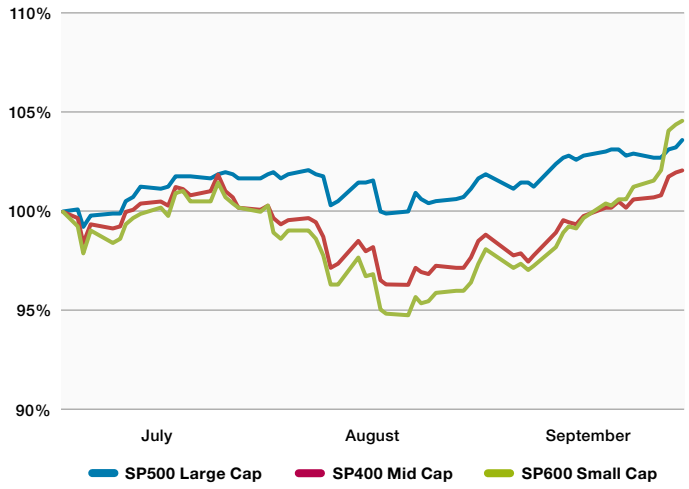
# THIRD QUARTER 2017 MARKET REVIEW

By **JOSEPH P. CLARK**

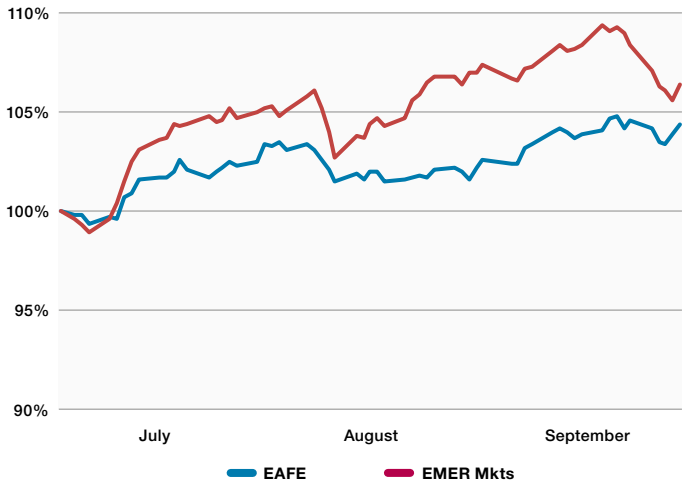
**ALL GLOBAL EQUITY MARKET SEGMENTS POSTED POSITIVE RETURNS FOR THE THIRD QUARTER OF 2017.** The emerging market segment posted the largest gain with a quarterly return of over 6.6%. The international developed markets returned nearly 4.6% as well. In fact, non-U.S. stocks have posted a streak of eleven consecutive months with positive returns. Year to date small, mid, and large-cap U.S. indices are up 7.9%, 8.2%, and 12.5% respectively. However, international markets have dominated with returns of 17.2% and 25.4% in the international developed and emerging markets respectively.

**US Equity Market Performance Q3 2017**




Source: Yahoo! Finance

**International Equity Market Performance Q3 2017**




Source: Yahoo! Finance

2017 has been a year of historically low volatility in U.S equity markets. The S&P 500 has only seen 5% of its trading days post a move of greater than 1% in either direction—this is the lowest level of volatility since 1982 when intra-day data began to be recorded. For the first time in twelve years, there have been no days this year with a 2% move in either direction. Of course there is one quarter of the year left, but this year has indeed been very smooth to date. This may change as economic data is released over the next few months, because it is likely that hurricanes will have significant effects on many economic measures. Therefore (as usual!) we will focus on the longer term.

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# TAXES: LEGISLATIVE HAND TO HAND COMBAT PART 2

By **MARC A. WEHMEYER**

**Efforts to revise the tax code will dominate the domestic agenda during the last three months of 2017.** After failing to repeal and replace the Affordable Care Act, Congressional Republicans will be under pressure to come together and create tax legislation which appeals to all Americans. President Trump's principles for tax reform – simplicity, giving American workers a pay raise, improving the competitiveness of American businesses and workers, and repatriating offshore corporate profits – can be found in a nine-page document jointly released on September 27th by the administration and Congressional Republicans.

Here are some key areas mentioned in the framework that will bear watching:

1. **Increasing the Standard Deduction and Eliminating Personal Exemptions.** The standard deduction is increased to $12,000 for single filers and $24,000 for married taxpayers filing a joint return, compared to the current amounts of $6,350 and $12,700 respectively. The standard deduction is currently indexed for inflation and it is unknown now if this will continue. Personal exemptions, currently valued at $4,050 each, would be eliminated. A hypothetical family of four using the standard deduction under the current system would be able to deduct $28,900 from their adjusted gross income ($12,700 plus $4,050 x 4), but would only be able to deduct $24,000 under the new system. This is an obvious case of an average family being worse off under the new system and will have to be addressed in the details of the plan.

2. **Reducing the Number of Tax Brackets.** The framework says that the number of brackets will be consolidated from seven down to three at 12%, 25%, and 35%. The dollar amounts associated with each bracket are not provided, but the framework specifies the new system should be at least as progressive as the current system and says there may end up being a fourth tax rate above 35%.

3. **Eliminating Most Itemized Deductions.** In the spirit of simplification, itemized deductions will be eliminated except for the mortgage interest deduction and the charitable contribution deduction. We expect that one of the most contentious battles going forward will be over the proposed elimination of the deduction for state and local taxes, including not only income taxes but property taxes as well.

4. **Repealing the Estate Tax, Generation-Skipping Transfer Tax (GST), and Alternative Minimum Tax (AMT).** In addition to repealing the AMT, the framework proposes to repeal the estate tax in its entirety as well as the GST. There is no information about whether or not assets will continue to be stepped-up in basis at death, nor any discussion about changes to the existing gift tax.

5. **No Mention of Capital Gains Taxes.** The framework document is silent on the treatment of capital gains income. Under the current system, short-term capital gains on assets held less than one year are taxed at ordinary income rates. Long-term capital gains are taxed at 0% for taxpayers in the 10% and 15% brackets; 15% for taxpayers in the 25%, 28%, 33%, and 35% brackets; and 20% for those in the top 39.6% bracket. The framework document is also silent on the 3.8% surtax on net investment income above certain income thresholds that went into effect on January 1, 2013 as part of the Affordable Care Act.

6. **Reducing Business Tax Rates.** American businesses would be clear winners according to the framework document. The tax rate for C Corporations would be reduced from 35% to 20% and the maximum tax rate for so-called pass-through businesses (sole proprietorships, partnerships and S corporations where profits and losses flow from the business to the individual's personal tax return) would be set at a 25% maximum. Details still need to be worked out to determine how the tax code would be able to differentiate business income from personal wage income.

# TAXES: LEGISLATIVE HAND TO HAND COMBAT PART 2

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**7. International Taxes for Businesses.** The framework seeks to remove existing incentives for corporations to keep foreign profits "offshore" by calling for a 100% exemption for dividends from foreign subsidiaries in which the American parent owns at least 10% of the subsidiary. Accumulated overseas earnings would be subject to a repatriation process spread over several years with different tax rates for liquid and illiquid assets.

With the Democrats emboldened by the Republicans' failure to pass health care legislation, the stage is set for yet another legislative battle. Both sides will claim they represent the will of American taxpayer. Interest groups and lobbyists are already hard at work attempting to shape public opinion (and influence lawmakers). The administration's goal is to get tax reform passed before the New Year, but Congress first has to agree on a budget resolution. Any plan increasing the deficit would require 60 votes to pass in the Senate which could be an impossible hurdle for Republicans to clear. If you are contemplating any tax-related moves (such as deferring income or accelerating deductions) in anticipation of changes to the tax code, we encourage you to talk to your tax professional prior to taking irrevocable action.

# PRESIDENT'S COMMENTARY

The 12-year drought of hurricanes reaching the United States ended and the best of our country responded in a way to make all of us proud. Affected regions of the country demonstrated that America is comprised of amazing and compassionate people and groups who pitch in where needed and help anyone in need.

As we head into what appears to be an exceedingly challenging domestic and international environment, my wish would be that our politicians are worthy of the citizens of this great country.

# THIRD QUARTER 2017 MARKET REVIEW (continued)

*(continued from pg. 1)*

For quite some time now, the "experts" have been predicting a correction in equity markets. We have recommended that our clients stay the course and focus on the long run, because no one can accurately predict if or when a correction will occur. Together with clients we construct an asset allocation that meets each client's required rate of return while at the same time considering their individual tolerance for risk. Staying invested is the only way to ensure you participate in positive markets returns in those periods where they occur. To quote the famous investor Peter Lynch, "Far more money has been lost by investors preparing for corrections, or trying to anticipate corrections, than has been lost in corrections themselves."

For the past twelve months the return for the S&P 500 has been 16.03%. During this same one year period, our investment models have overweighted the following sectors: consumer discretionary, financials, and information technology. Returns over the same period have been 13.14%, 33.63%, and 26.98% respectively. In the late Fall of 2016 we removed our overweight in the energy sector and added an overweight in the industrial sector. For 2017, the energy sector is down 8.62% while the industrial sector performed on par with the S&P 500 index (12.32% vs. 12.53%).

We expect the fourth quarter to be filled with lots of activity (budget battles, geopolitical concerns, etc.). We will continue to reevaluate our overweighted positions to determine if changes should be made to investment models as we move into the fourth quarter of 2017 and beyond.

# UMBRELLA INSURANCE – WHY YOU NEED IT

By **Edward G. Leszynski**

**Umbrella insurance is a form of liability insurance that will supplement your basic liability policies, such as your auto, home or renters insurance.** An umbrella liability policy covers a much higher limit and goes above and beyond claims directly relating to your home and auto.

The main purpose of your umbrella policy is to protect your assets from an unforeseen event, such as a tragic accident in which you are held responsible for damages or bodily injuries. If another party files a lawsuit against you, your umbrella coverage will pay for the damages you're legally responsible for up to the policy limit.

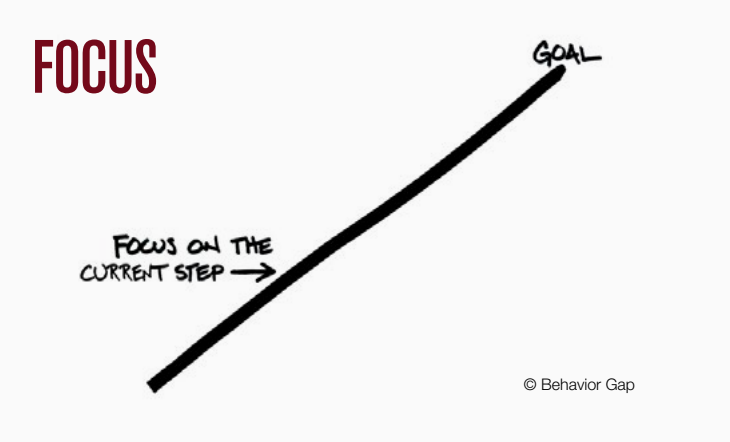
An umbrella policy provides additional coverage or "excess liability" above the limits of your basic policies. It can protect you from bodily injury liability claims and property damage liability claims. Umbrella policies also provide a broader form of coverage and can help cover legal fees, false arrest, libel, and slander.

Your umbrella insurance can come into play if you are found liable and need to pay damages, or if you are sued and need to pay for your legal defense – even if the result is that you are not found to be responsible. An umbrella policy only pays once your basic liability limits have been exhausted or the claim is excluded from the basic liability coverage. Umbrella insurance typically does not cover flood damage. It will only cover property damage and bodily injury that you cause and will only provide payment to a third party. If you want to purchase flood insurance, it's available through the National Flood Insurance Program (NFIP).

An umbrella policy can be a wise investment for landlords too. If you own rental property, you are responsible for making sure your property is safe for your tenants and your guests. An umbrella policy will most likely protect you in several different scenarios, such as:

- A third party sues you for damages your tenants cause
- A visitor is injured in a fall due to a broken step or handrail
- A guest is injured in your workout or pool facilities
- You neglect to change the locks on a unit and a former resident with a key burglarizes the apartment

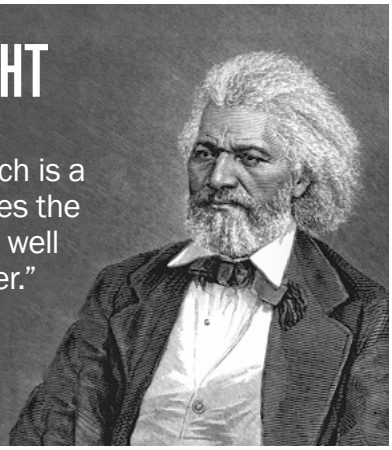
In addition to the coverage, a personal umbrella insurance policy is relatively inexpensive!




## CLOSING THOUGHT

"To suppress free speech is a double wrong. It violates the rights of the hearer as well as those of the speaker."

***—Frederick Douglass***



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