

How Will American Households Respond to the New Tax Reform?



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Introduction

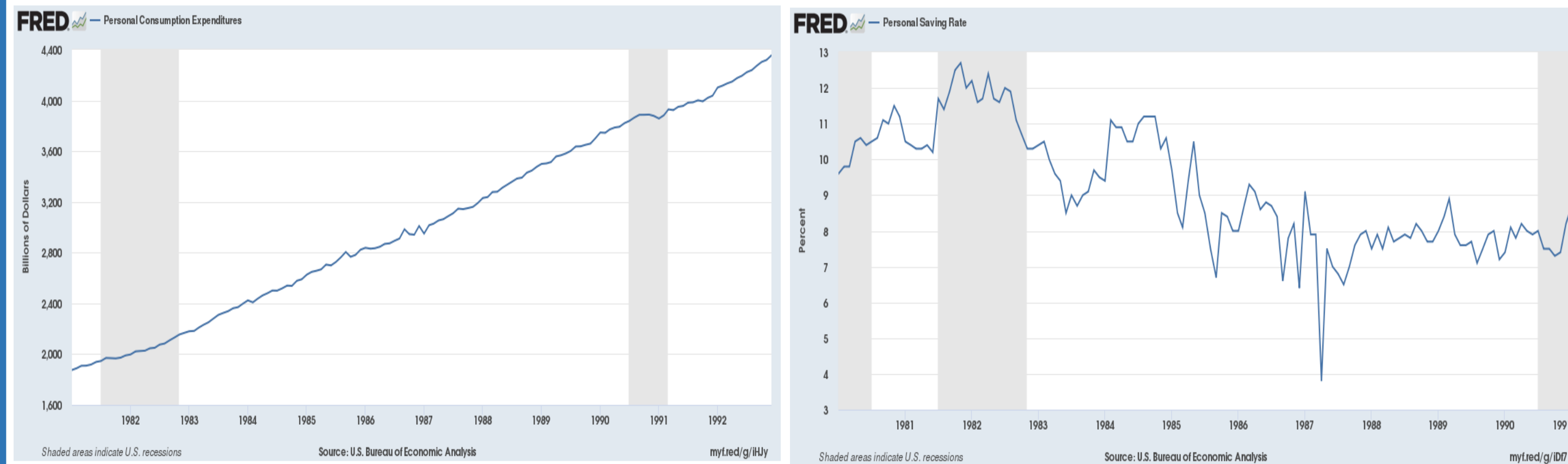
A historical tax cut was one of the promises President Donald Trump made during his presidential campaign. On December 22nd, 2017 that proposal was enacted into a law that aims to revitalize the United States' economy. To achieve this goal, there is one action that the government expects American households will respond to: savings. According to the House Speaker Paul Ryan, the H.R. 1, Tax Cuts and Jobs Act "provides particular relief to low income and middle class families to make sure they keep more of their hard-earned money" (n.d). From this Government's perspective, saving should prevail over consumption for an economic growth in the short term. The dilemma comes when how the target audience, in this case American households will respond to this stimulus. Thus, this research addresses two questions:

Research Questions

1. How American households have responded regarding consumption and saving due to past tax cuts?
2. What would be the households' response to consumption and saving with the new H.R. 1, Tax Cuts and Jobs Act enacted by President Donald Trump's administration?

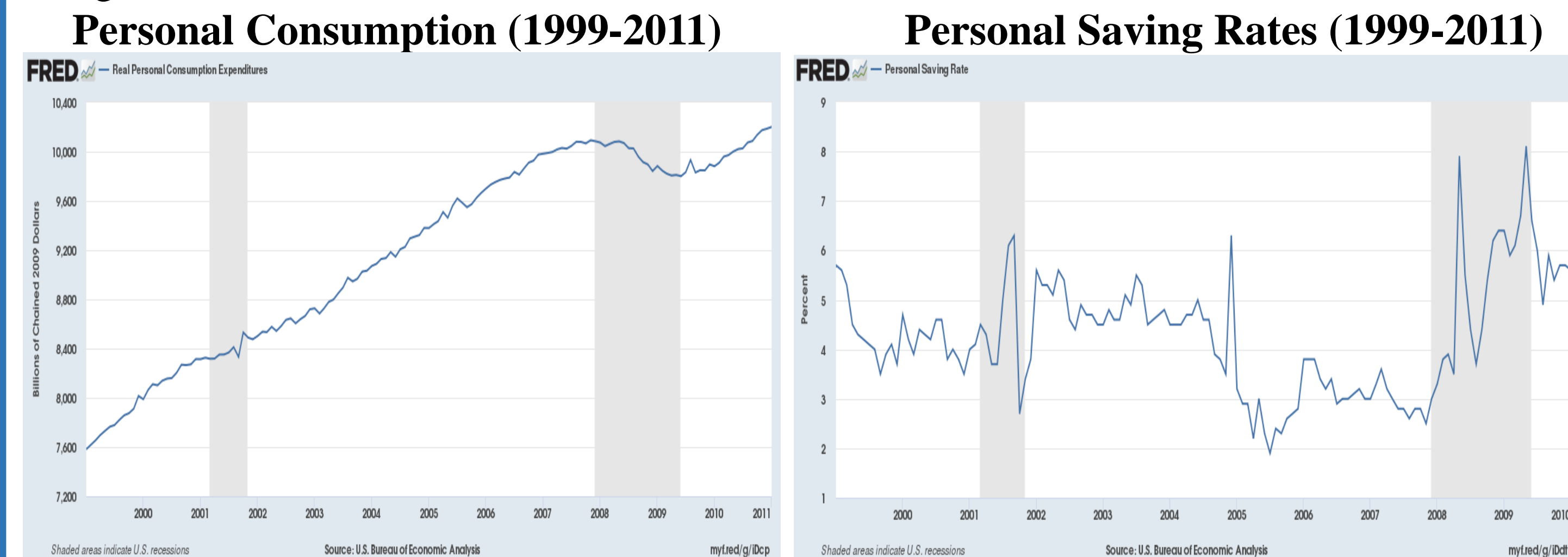
How did personal consumption and saving behave before and after past tax cuts?

Ronald Reagan - The Economic Recovery Tax Act of 1981 and Tax Reform Act of 1986



Source: U.S. Bureau of Economic Analysis, Real Personal Consumption Expenditures [PCEC96], retrieved from FRED, Federal Reserve Bank of St. Louis; <https://fred.stlouisfed.org/series/PCEC96>, February 23, 2018.

George W. Bush - Economic Growth and Tax Relief Reconciliation Act of 2001

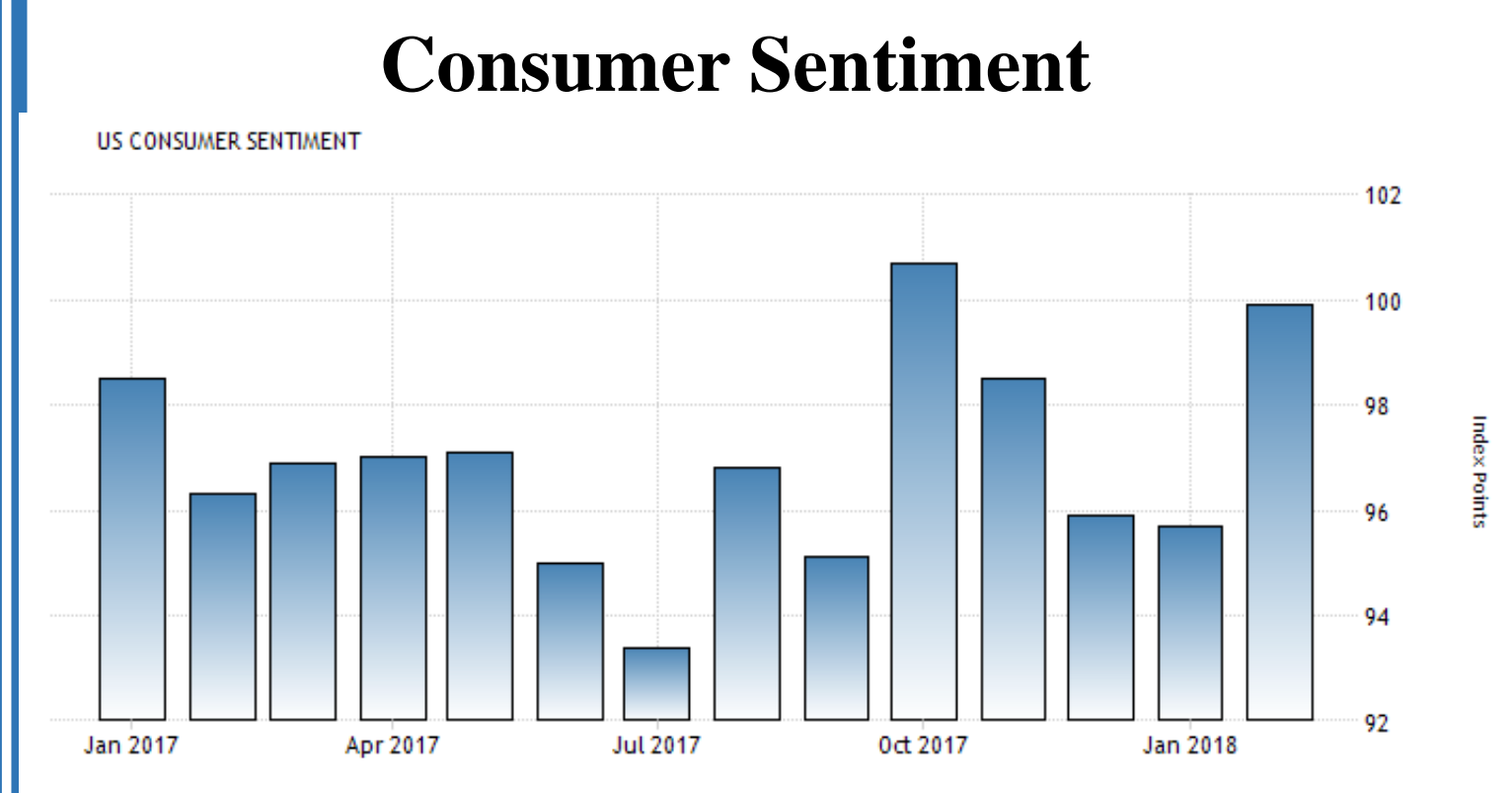


Source: U.S. Bureau of Economic Analysis, Personal Saving Rate [PSAVERT], retrieved from FRED, Federal Reserve Bank of St. Louis; <https://fred.stlouisfed.org/series/PSAVERT>, February 23, 2018.

During the Reagan and Bush Eras' tax cuts may or may not have been the main cause of the changes presented in the Personal Consumption and Saving Rate. Historical data shows that American families started spending more and saving less in a 10-year period right after the tax cuts were enacted.

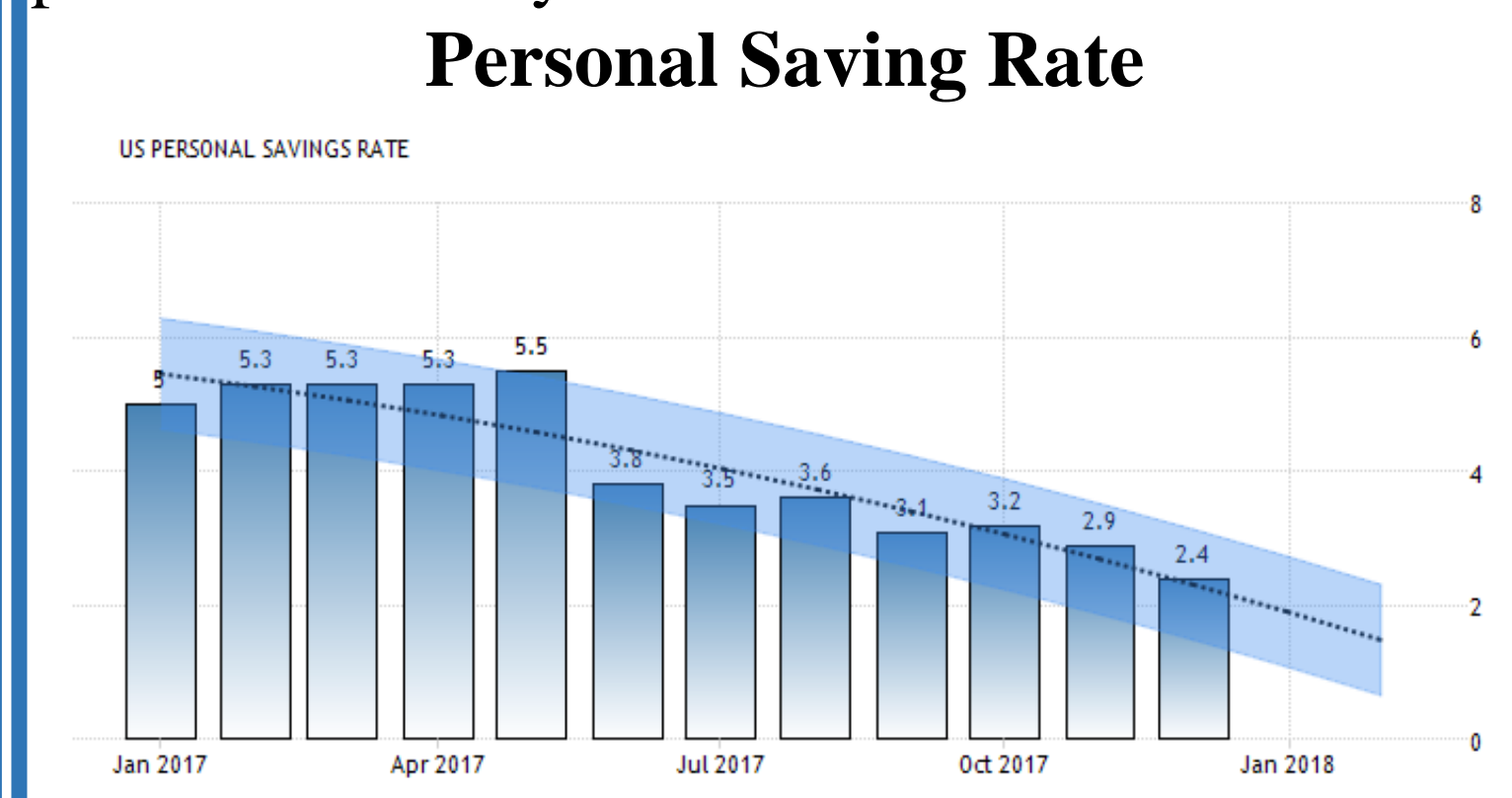
Previous research includes: Consumption is excessively sensitive to tax cuts (Souleles, 2002).

What is the situation of current consumption and saving (2018)?



Source: Trading Economics.com – University of Michigan "United States Consumer Sentiment". Retrieved on 02-22-2018, from: <https://tradingeconomics.com/united-states/consumer-confidence>

According to the University of Michigan's survey, in February 2018, the U.S. consumer sentiment has increased to 99.9 from 95.7 in January, (Taborda, 2018). This means that Americans are gaining more confidence about public and personal economy.



Source: Trading Economics, "United States Personal Savings Rate – Forecast". Retrieved on 02-22-2018, from: <https://tradingeconomics.com/united-states/personal-savings/forecast>

Based on current trends on consumer sentiment and saving rates presented above, Americans are addressing their feelings about the economy toward an increase in spending.

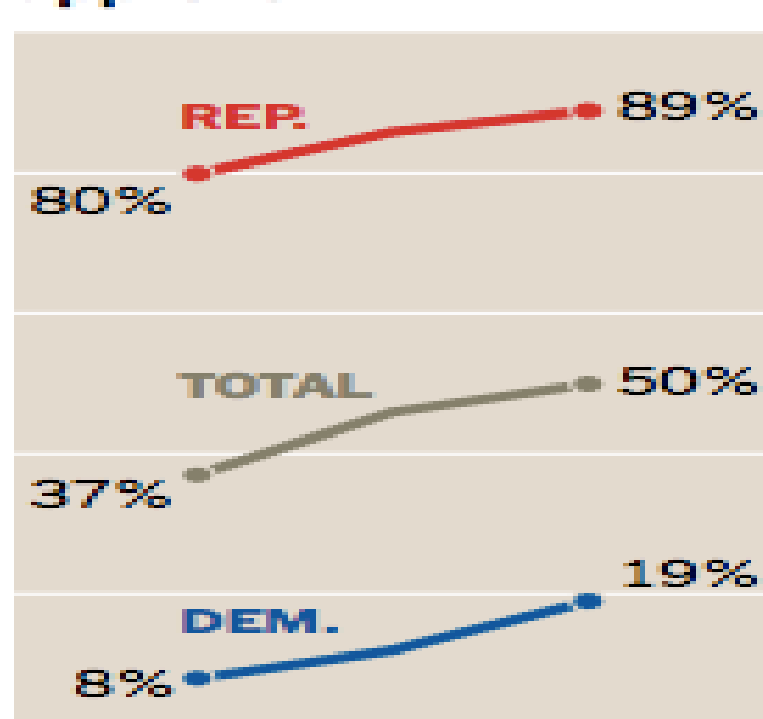
What is Americans' opinion about the new H.R. 1, Tax Cuts and Jobs Act?

The New York Times-poll (February 5th – 11th, 2018 survey)

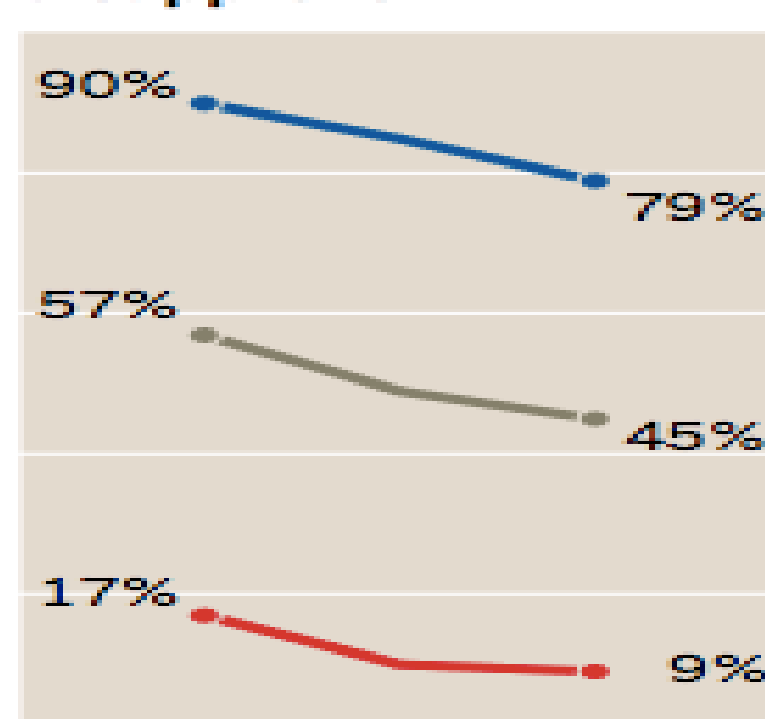
Americans approval or disapproval on the new tax plan

Do you approve or disapprove of the tax plan?

Strongly/somewhat approve



Strongly/somewhat disapprove



Source: SurveyMonkey | By The New York Times. Retrieved on 02-26-2018, from <https://www.nytimes.com/2018/02/19/business/economy/tax-overhaul-survey.html>

According to The New York Times' poll, the H.R. 1, Tax Cuts and Jobs Act "Overall, 51 percent of Americans approve of the tax law, while 46 percent disapprove".

H.R. 1, Tax Cuts and Jobs Act

Previous and new tax rates

INCOME	TAX RATES	
	Previous From	Current (2018-2016) To
1 Up to \$9,325	10%	10%
2 Over \$9,525 to \$38,700	15%	12%
3 Over \$38,700 to \$82,500	25%	22%
4 Over \$82,500 to \$157,500	25% to 28%	24%
5 Over \$157,500 to \$200,000	28% to 33%	32%
6 Over \$200,000 to \$500,000	33% to 35%	35%
7 Over \$500,000		37%
Standard deduction		
Individuals	\$6,350.00	\$12,000.00
Couples	\$12,700.00	\$24,000.00
Personal exemption	\$4,050.00	Eliminated

Why this research proposal?

The new tax reform may or may not have a significant impact in the personal economy of American households. Therefore, this research proposal aims to present what would be a possible households' response to consumption and saving, having studied what happened in the past.