

Overview of Budget & Debt Implications on the Reauthorization of Surface Transportation Programs

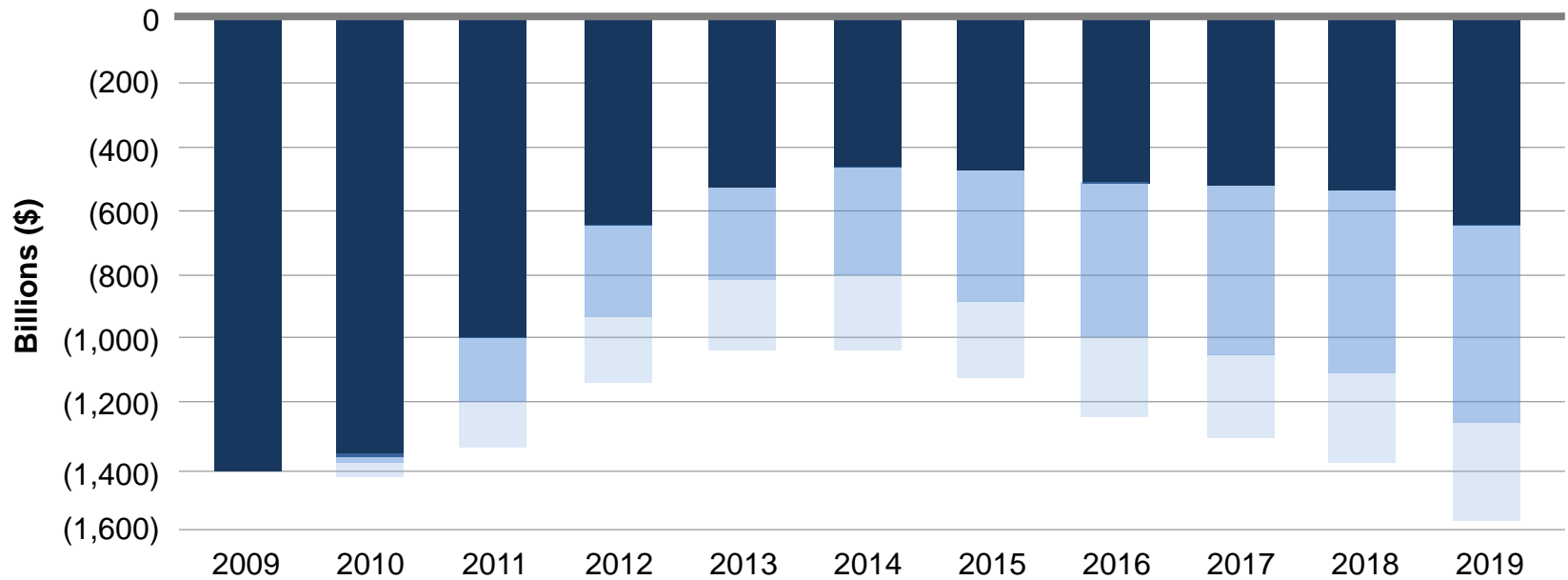
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C 2 G R O U P

Projected Budget Deficit 2010-2019

CBO Alternative Baselines A and B



Cumulative 10-year deficit = \$14.0 trillion

Assumptions

Current law assumes

- 2001 and 2003 tax cuts sunset as scheduled in 2012
- Congress stops “patching” the alternative minimum tax

Alternative Baseline A assumes

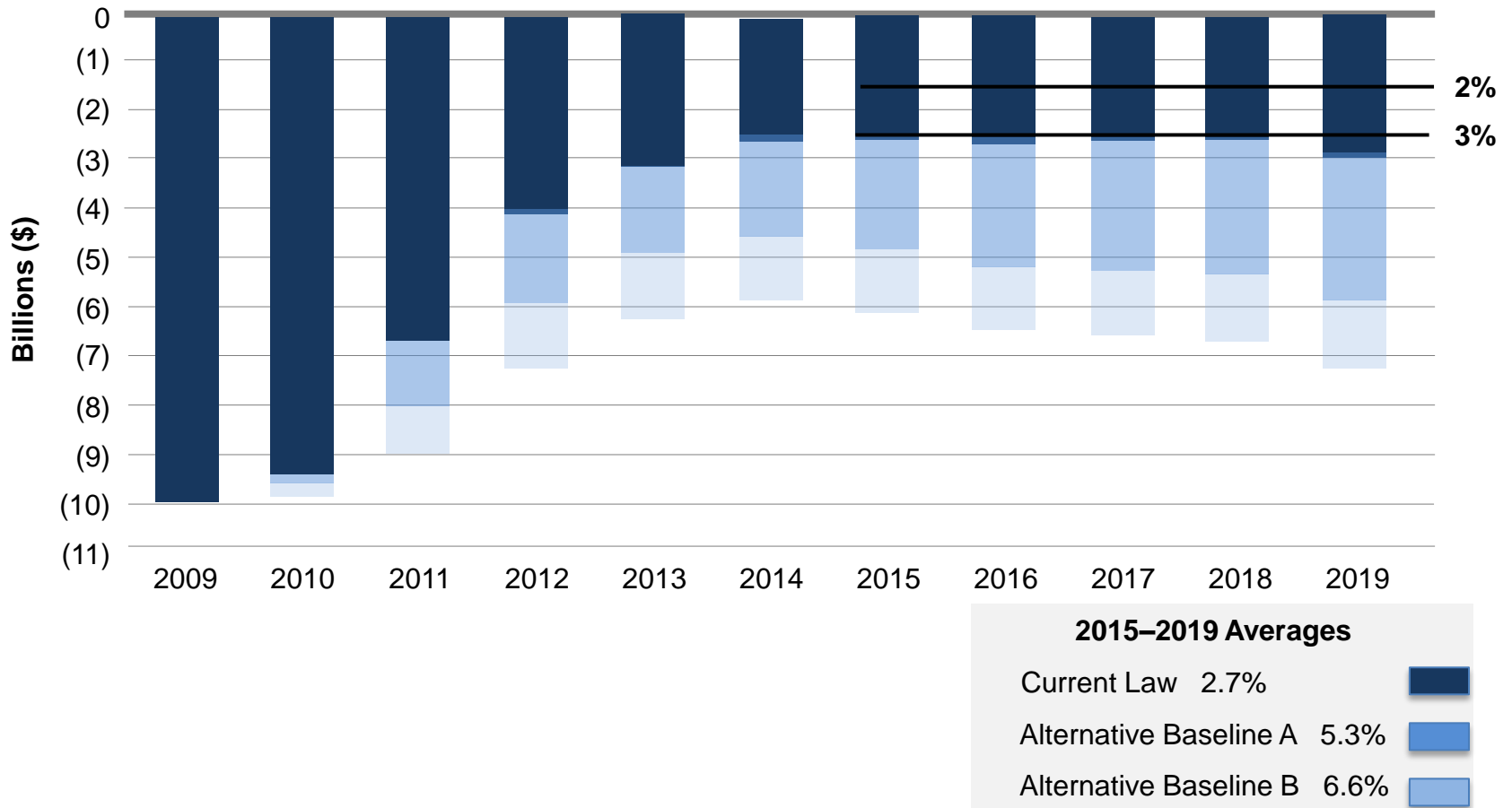
- 2001 and 2003 tax cuts are extended
- Estate tax compromise is maintained at 2010 parameters
- 2009 AMT patch is extended
- AMT exemption, rate bracket threshold and phase-out exemption thresholds are indexed for inflation
- Includes the budgetary effects of the 2010 Healthcare Reform Act

Assumptions Continued

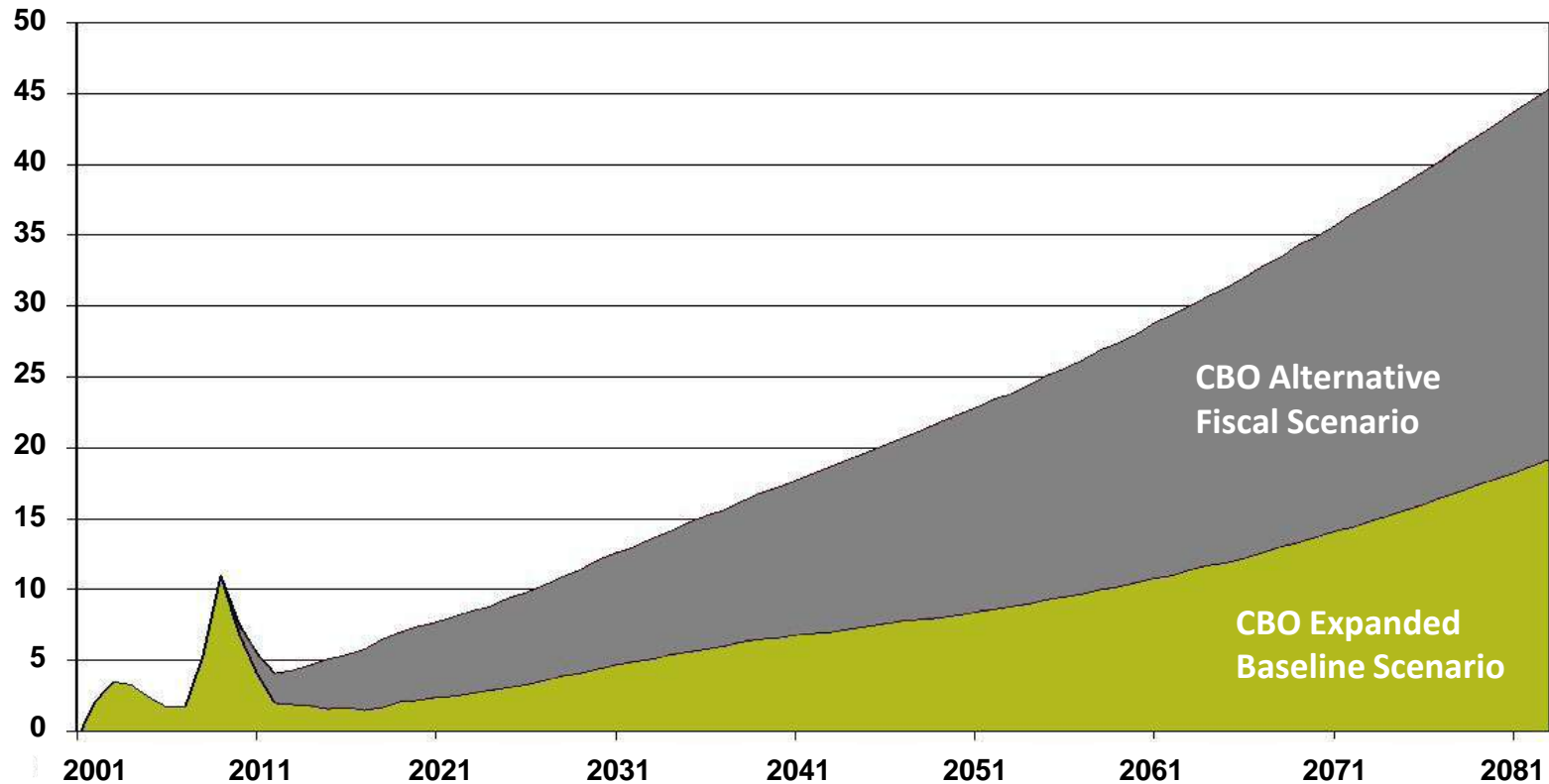
Alternative Baseline B is

- Alternative Baseline A plus
- Extension of several expiring provisions of ARRA including Making Work Pay credit, American Opportunity Tax Credit, exclusion of certain amounts of unemployment benefits
- Extension of expiring provisions, i.e.:
 - Research and Development tax credit
 - Energy extenders
 - Active Finance
 - Bonus depreciation

Projected Budget 2010-2019 Deficit as a Percent of GDP



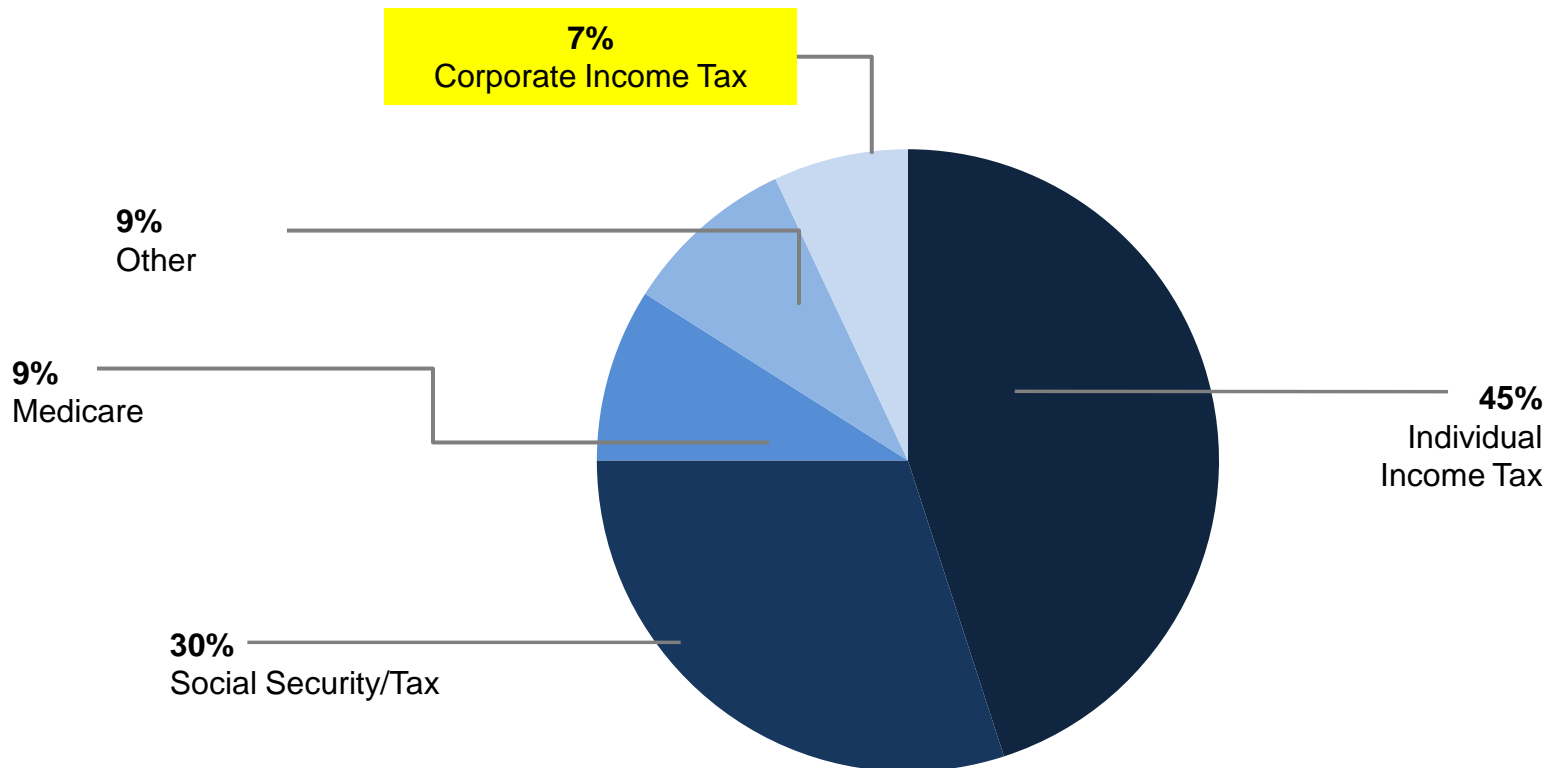
Long-Term Deficits as a Percent of GDP



Notes: Unlike the CBO “extended baseline,” the “alternative fiscal scenario” extends 2001 and 2003 tax relief, indexes the AMT for inflation, and reverses scheduled reductions in Medicare physician reimbursements.

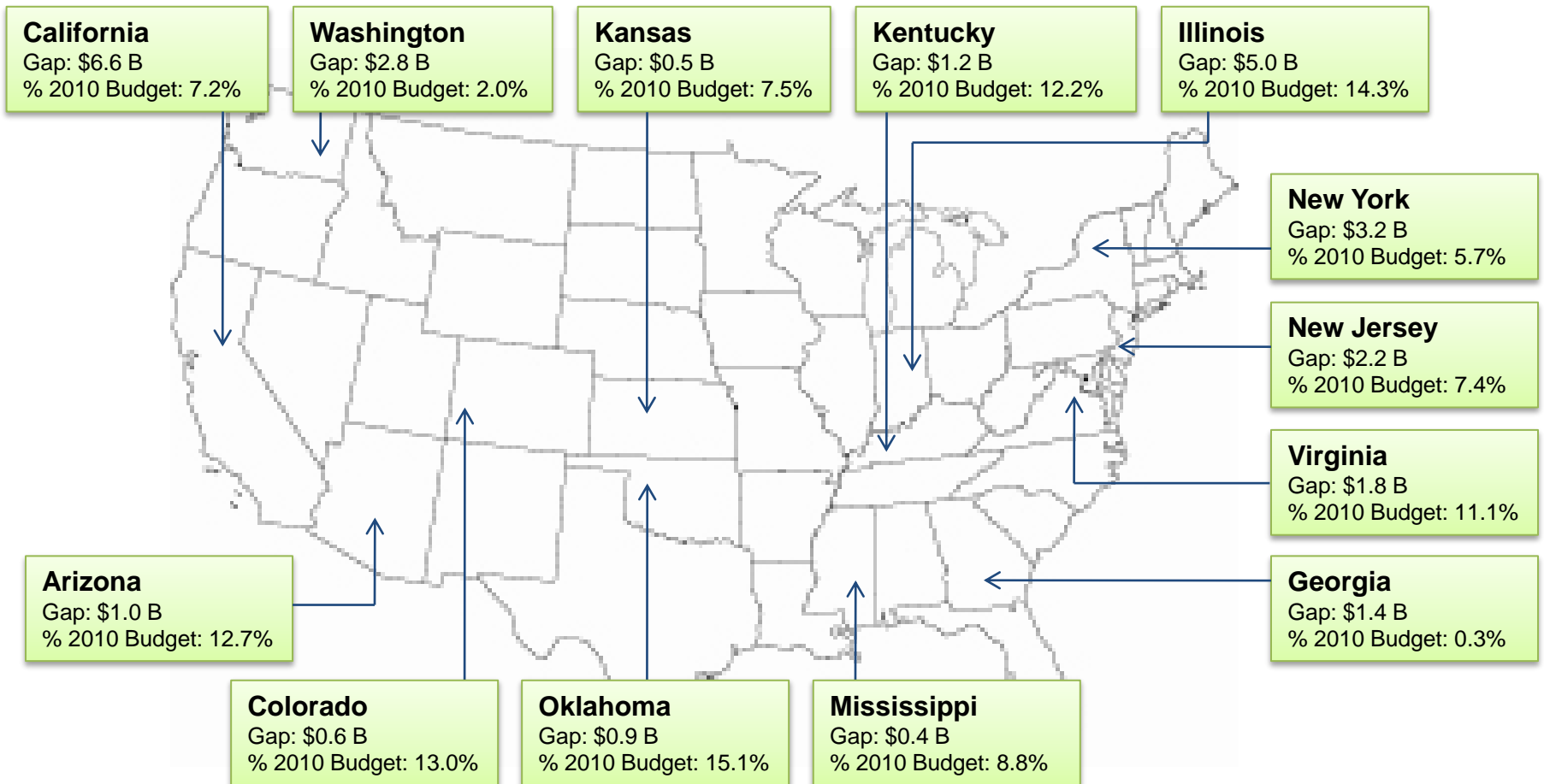
Footing the Bill

Percentage of Revenues by Major Source



Source: Congressional Budget Office.

States Starving for Cash



Revenue Pressure is Global

2010 Regulatory Landscape

Select Jurisdictions

1 Canada

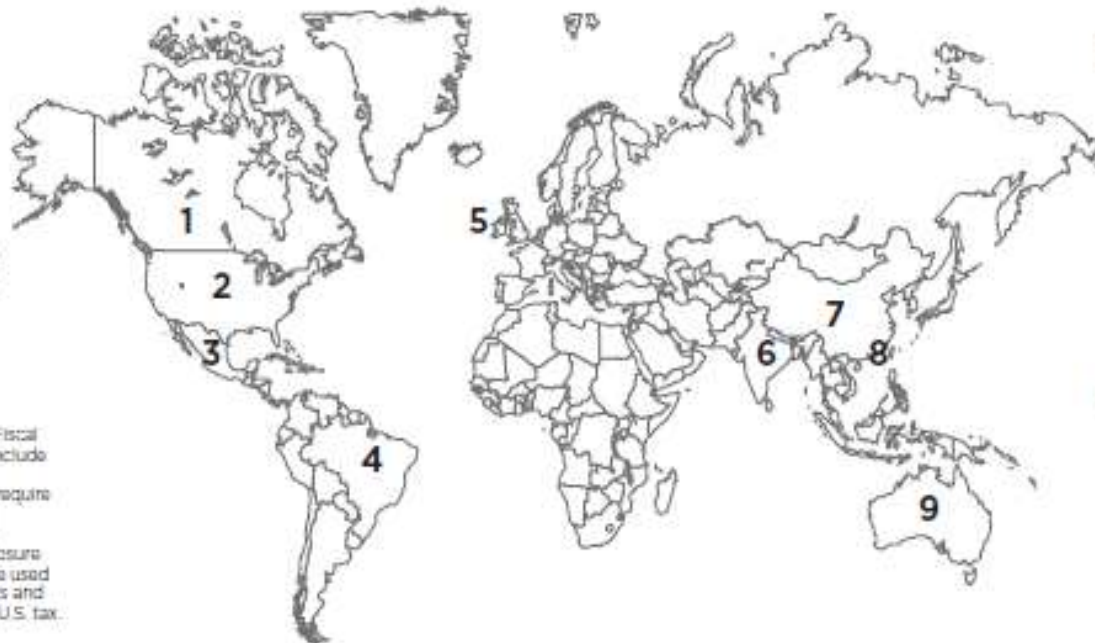
- Harmonized Sales Tax (HST) to come into effect on 1 July 2010 subject to legislative approval.
- Changes to the Canada-United States treaty deem United States and Canadian corporations to have a permanent establishment in that other country.
- Introduced a new "look-through" regime for determining the eligibility of certain flow-through entities, such as U.S. LLCs and Canadian ULCs, for treaty benefits.
- CRA is looking to improve the SR&ED program, July 2010.

2 United States

- Obama Administration released the Fiscal year 2010 Revenue Proposals which include international tax provisions.
- IRS announced proposal that would require companies to disclose uncertain tax positions on their annual tax returns.
- Announced Offshore Voluntary Disclosure Program to bring taxpayers who have used undisclosed foreign financial accounts and undisclosed foreign entities to avoid U.S. tax.

3 Mexico

- Approved transfer pricing reporting requirements that will pose a sig. compliance burden not just for taxpayers but for their registered public accountants.
- Approved 2010 tax changes which include temporarily increasing corporate tax rates, limiting deferral of taxes, disallowing application of flat tax loss credit against income tax, and increasing the VAT rate.



4 Brazil

- Effective 1 January 2010, Brazil established a new transfer pricing method for justifying the import prices on cross-border transactions with related companies.
- Established new procedures for audits by the tax authorities.

5 United Kingdom

- Senior Accounting Officer Legislation requires such officers to certify annually and take reasonable steps to establish and monitor accounting systems.
- Published proposals for Multinational taxation for a more targeted CFC regime to catch profits being artificially diverted to low-tax jurisdictions.

6 India

- Finance Ministry unveiled the draft of a new direct tax code and proposes structural changes to direct taxation in the country.
- Provisions of the transfer pricing law amended to apply the permissible safe harbor of 5% on the price charged by the taxpayer rather than on the average of prices of comparables.

7 China

- Supplementary rules following the recent reform of China's tax system include:
 - General anti-avoidance rules empower the tax authorities to initiate tax investigations.
 - More detailed guidelines on selection of TP method, application of each method, selection criteria for TP investigation target, application procedures of advance pricing arrangement.

9 Australia

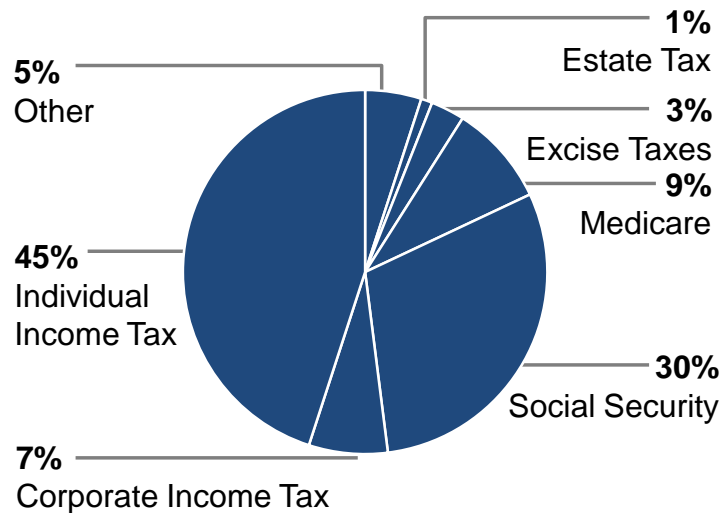
- Announced complete rewrite of foreign source income rules, expected to take effect 1 July 2010.
- Released a paper on the revision of CFC rules.
- ATO has expanded budget to build additional transfer pricing capability and sig. increase compliance activities.

8 Hong Kong

- introduced transfer pricing guidelines focusing on the timing of imposing a transfer pricing adjustment, arm's length principle in the OECD guidelines, treatment of losses, source of profits, and documentation.

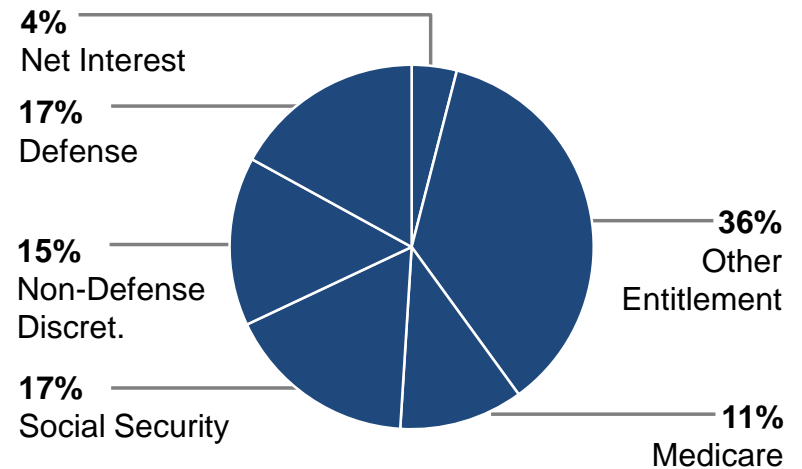
Scope of Reform

Revenue



Revenue
Total: \$2.1 Trillion

Spending



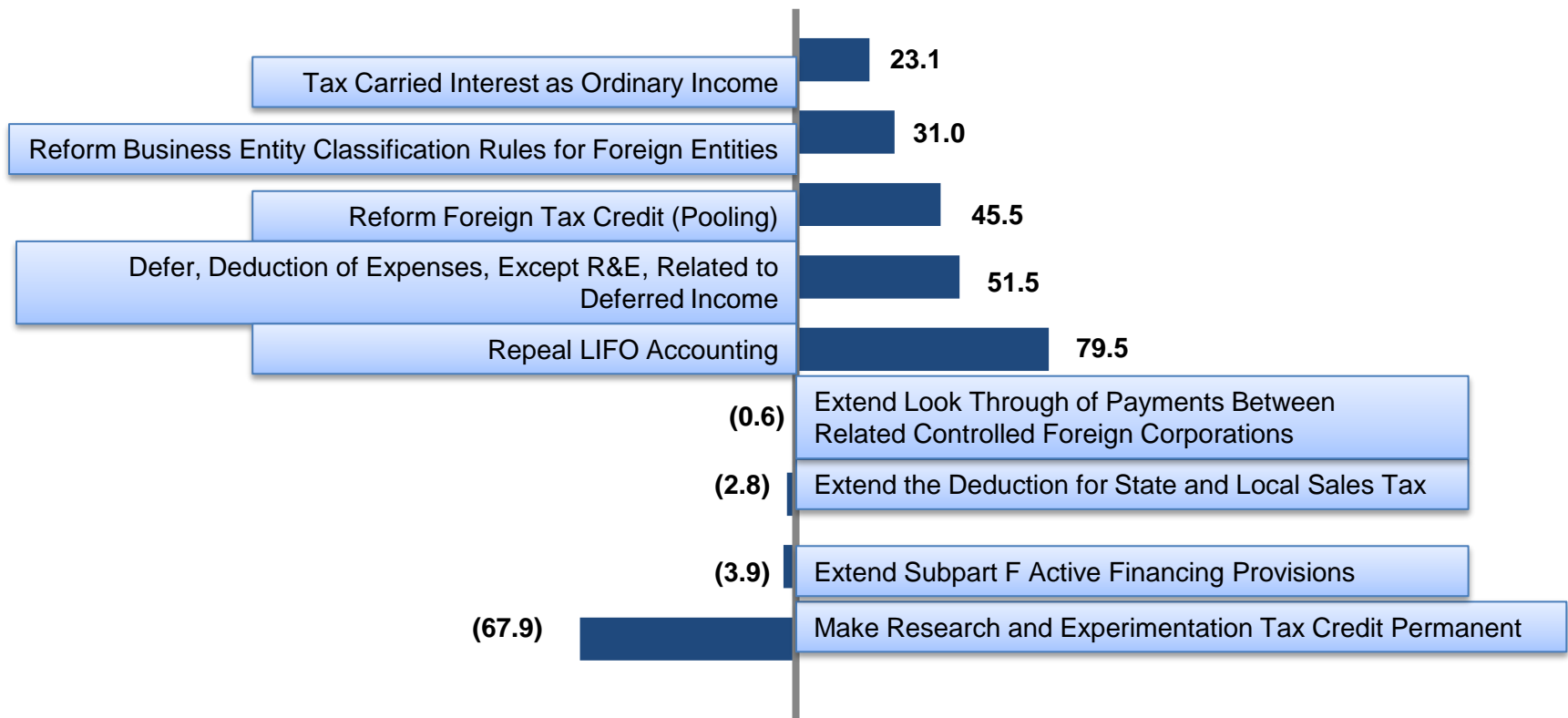
Spending
Total: \$3.5 Trillion

Source: FY2011 Budget of the United States Government.

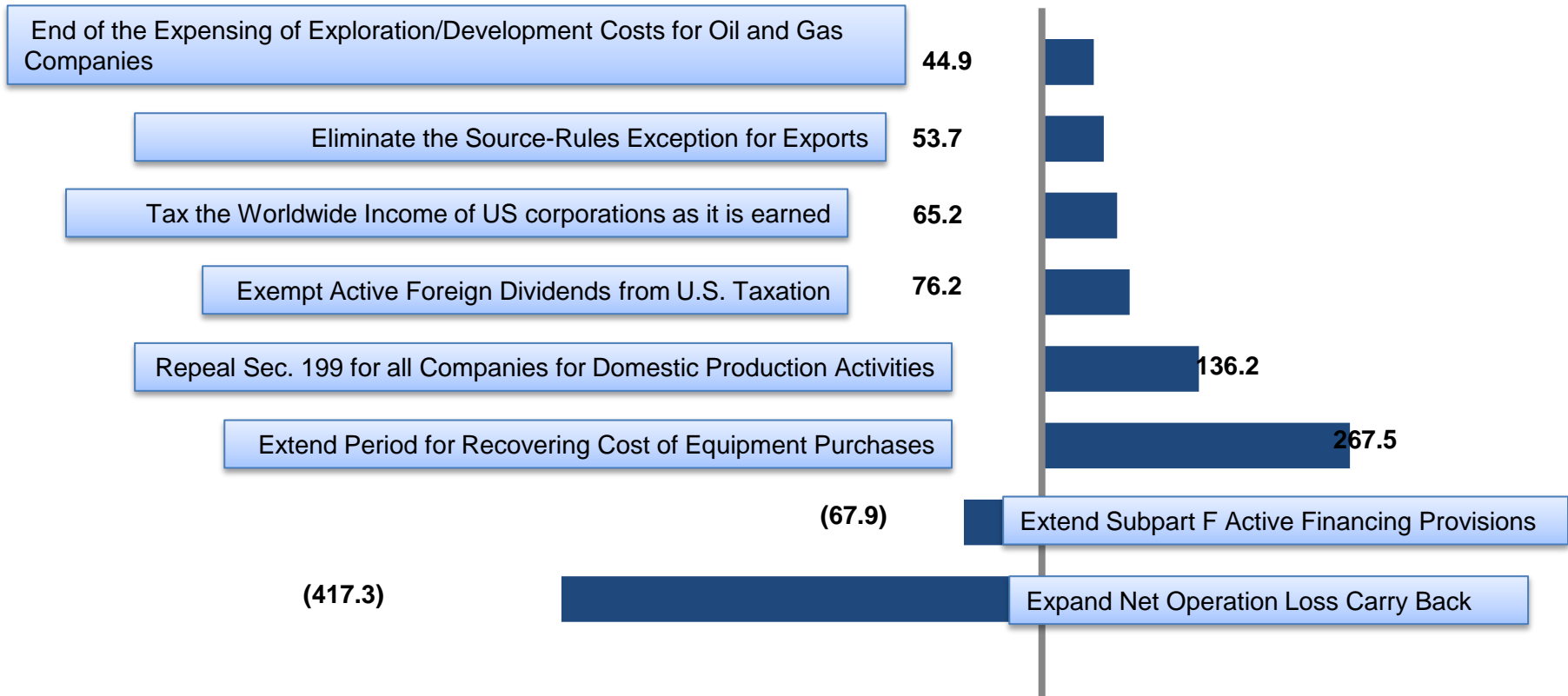
Notes: "Other entitlement" includes Medicaid, SSI, SCHIP, TANF, Food Stamps, and various refundable credits.

"Non-defense discretionary" includes international affairs, transportation, commerce, energy, agriculture, education, science and technology, natural resources, veterans' benefits, and community and regional development.

Obama's Proposed Tax "Reforms"



CBO's Options



National Commission on Fiscal Responsibility and Reform

- Zero-Base Budget Approach
- Lower Corporate Rate (Between 23 and 29 Percent)
- Eliminate all Business Tax Expenditures
- Create/Maintain Five “Buckets” of Tax Preferences
 - Low-Income Assistance (e.g., EITC)
 - Mortgage Deduction
 - Employer-Provided Health Care
 - Charitable Giving
 - Retirement Security

Top Corporate Tax Expenditures

Top 10 Corporate Tax Expenditures	FY09–13 (\$billions)
Deferral of active income of controlled foreign corporations	\$60
Credits for alcohol fuels	\$42
Exclusion of interest on public purpose state and local government bonds	\$42
Five-year delay of inclusion of income arising from business indebtedness discharged in 2009 or 2010 by the reacquisition of a debt instrument	\$40
Deduction for income attributable to domestic production activities	\$38

Top 10 Corporate Expenditures (Cont.)	FY09–13 (\$billions)
Classification of certain farm property placed in service after 12/31/09 z 5-year Property	\$35
Low-income housing credit	\$29
Expensing of R&E expenditures	\$24
Inventory methods and valuation, including LIFO and LCM	\$20
Reduced rates on first \$10 million of corporate taxable income	\$20

Source: Joint Committee on Taxation.

Headquarters Location of Global 500 in 2000 and 2009

Country	2000			2009			Taxation of Foreign Source Income, 2009
	Total Revenue (\$billions)	Number of companies	Statutory Corporate Tax Rate 1/	Total Revenue (\$billions)	Number of companies	Statutory Corporate Tax Rate 1/	
United States	4,681	179	39.2%	7,544	140	39.1%	Worldwide with deferral and FTC
Japan	2,931	107	43.3%	2,980	68	41.3%	95% dividend exemption enacted in 2009
Germany	1,217	37	52.0%	2,259	39	33.0%	95% dividend exemption
France	922	37	37.8%	2,166	40	34.4%	95% dividend exemption
China	200	10	33.0%	1,661	37	25.0%	Worldwide with deferral and FTC
United Kingdom	765	38	30.0%	1,585	27	28.0%	100% dividend exemption enacted in 2009
Netherlands	391	10	35.0%	1,044	12	25.5%	100% dividend exemption
Italy	264	10	39.5%	699	10	30.3%	95% dividend exemption
Korea	242	12	30.8%	603	14	24.2%	Worldwide with deferral and FTC
Switzerland	293	11	24.9%	566	15	21.2%	100% dividend and branch exemption
Total Top 10 1/	11,904	451	39.8%	21,106	402	32.1%	
Other	792	49	35.7%	4,069	98	28.4%	
Total Global 5001/	12,696	500	39.2%	25,175	500	31.1%	

Source: Fortune Global 500, Ernst & Young LLP

1/ Average statutory tax rates, including state and local taxes, weighted by number of Global 500 companies in the country excluding the U.S.

Business Tax

The U.S. statutory corporate income tax rate is high by international standards—what is the effect on the U.S. economy?

- Is the statutory or the effective rate more important?
- Dividends bear a second level of tax (at rate post-2010 yet to be determined)

Lowering the corporate tax rate without revenue loss requires broadening the corporate tax *base*. What are the options?

- Debt versus equity
- Choice of entity: pass-through entities (partnerships, S corporations) and sole proprietorships versus double-taxed C corporations
- Retaining earnings versus paying dividends

Ten Key Topics in Tax Reform

1. Scope of Reform
2. Who Should Pay?
3. Revenue Neutrality
4. Economic Growth
5. Individual Income Tax
6. Business Tax
7. Use of Code for Non-Tax Purposes
8. Global Issues
9. Alternative Tax Systems
10. Transition

Estimated Revenues And Interest Credited to the Highway Trust Fund, by Source, 2011

(Billions of dollars)

	Highway Account	Mass Transit Account	Total	Share of Total Trust Fund Revenues and Interest (Percent)
Gasoline Tax	20.2	3.9	24.0	65
Diesel Tax	7.6	1.0	8.7	24
Tax on Trucks and Trailers	2.2	0	2.2	6
Use Tax on Certain Vehicles	1.0	0	1.0	3
Truck Tire Tax	0.4	0	0.4	1
Interest Credited	0.4	0.2	0.6	2
Total	31.8	5.1	36.9	100

Source: Congressional Budget Office.

Components of the Highway Trust Fund, 2011

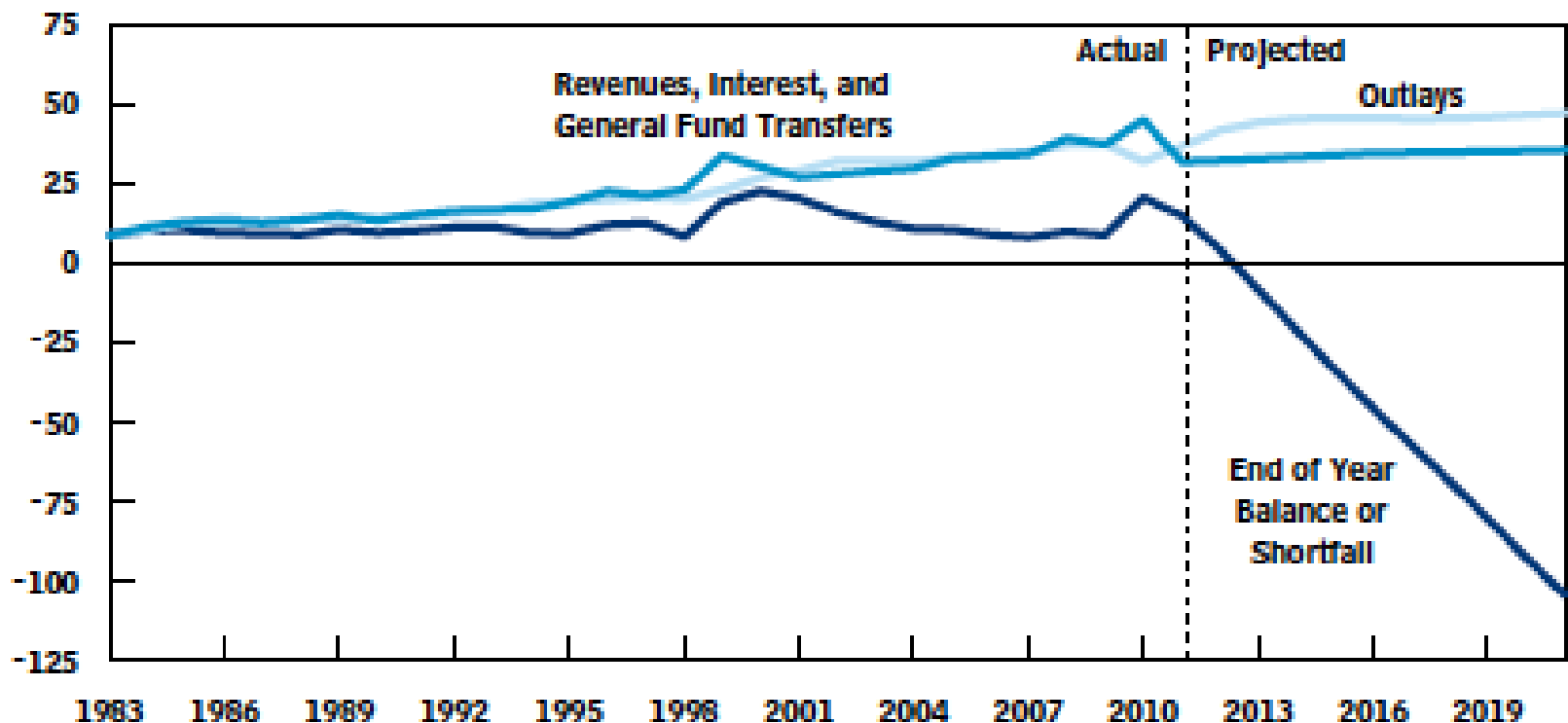
(Billions of dollars)

	Estimated Revenues and Interest	Budget Authority and Obligation Limitations	Estimated Outlays
Highway Trust Fund	36.9	52.7	44.3
Highway account	31.8	44.3	36.7
Federal-aid highway program	n.a.	43.0	35.4
Motor carrier safety program	n.a.	0.6	0.5
Highway traffic safety program	n.a.	0.7	0.7
Mass transit account	5.1	8.4	7.6

Source: Congressional Budget Office.

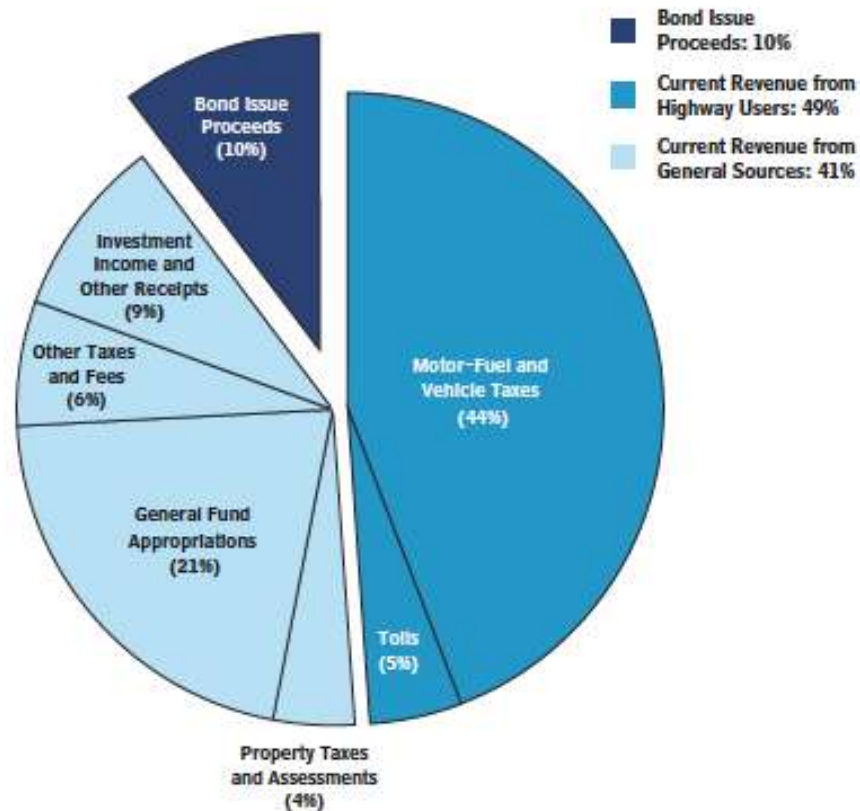
Status of the Highway Account of the Highway Trust Fund

(Billions of dollars)



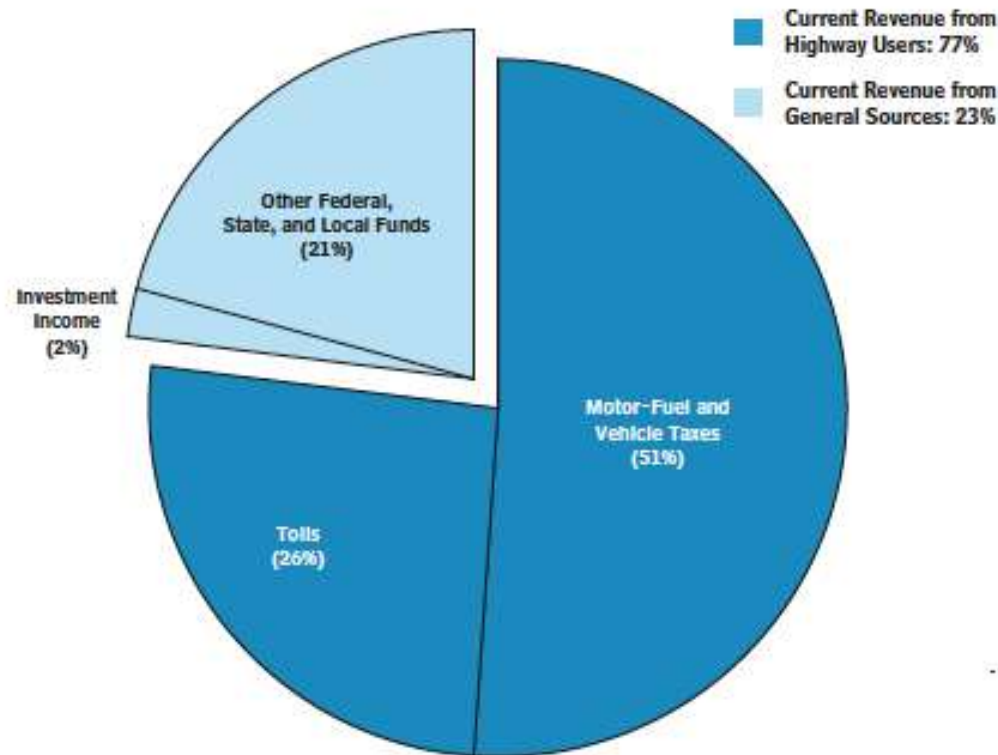
Source: Congressional Budget Office.

Sources of Funding for Highways, All Levels of Government, 2008



Source: Congressional Budget Office based on Department of Transportation, Federal Highway Administration, *Highway Statistics 2008* (December 2009), Table HF-10.

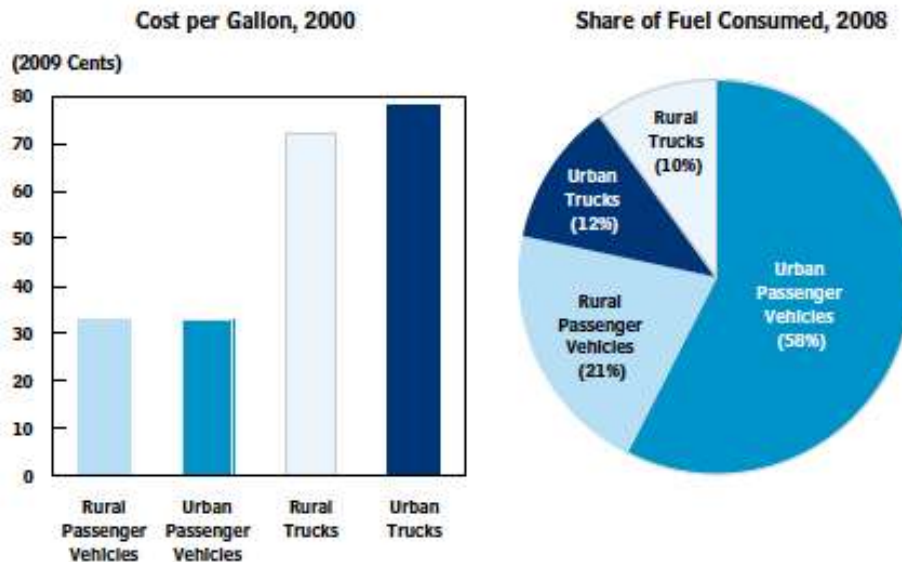
Sources of Funding for Paying Debt Service on Bond Issues, All Levels of Government, 2008



Source: Congressional Budget Office based on Department of Transportation, Federal Highway Administration, *Highway Statistics 2008* (December 2009), Table SB-3.

Note: Excludes proceeds from sales of other bonds.

Estimated Fuel-Related Costs and Fuel Consumed in Various Years



Sources: Congressional Budget Office based on Ian W.H. Parry, "How Should Heavy-Duty Trucks Be Taxed?" *Journal of Urban Economics*, vol. 63, no. 2 (March 2008), p. 660; and Department of Transportation, Federal Highway Administration, *Highway Statistics 2008* (December 2009), Table VM-1.

Notes: Passenger vehicles have two axles and four tires and include automobiles and light trucks (pickup trucks, minivans, and sport-utility vehicles).

Fuel use shares exclude motorcycles and buses.

Local air pollution costs are classified as mileage related for passenger vehicles and fuel related for trucks.

Summary of Mica Proposal: Highway and Transit Programs

- Transportation Reauthorization Bill Funding – 230 Billion over 6 years
- Better Leverage Existing Resources – TIFIA & 1 Billion
- Surface Transportation Program Reform – 70 programs consolidated or eliminated
- Streamlining the Project Delivery Process
- Federal Highway Program – distributed by Formula
- Federal Transit Program – promotes greater private sector financing

Senate EPW Proposal For Surface Transportation Funding

Chairman Boxer appears to be working from Congressional Budget Office's March 2011 baseline, under which new obligation levels for Highway Trust Fund spending and the three general fund mass transit accounts add up the \$109.3 billion, as shown below.

	<u>2012</u>	<u>2013</u>	<u>Total</u>
Assumed Levels of Obligation Limitations			
FHWA Federal-aid Highways	41,564	42,227	83,791
FMCSA Operations and Programs	245	251	496
FMCSA Motor Carrier Safety Grants	313	318	631
NHTSA Operations and Research	112	114	226
NHTSA Highway Traffic Safety Grants	626	636	1,262
FTA Formula and Bus Grants	8,435	8,568	17,003
Total, HTF Obligation Limitations	51,295	52,114	103,409
Contract Authority Exempt From Obligation Limitations			
FWHA Exempt Obligations	739	739	1,478
<u>General Fund Appropriations for Mass Transit</u>			
FTA Administrative Expenses	101	104	205
FTA Research and URCS	67	68	135
FTA Capital Investment Grants	2,020	2,052	4,072
Total, GF Transit Authorizations	2,188	2,224	4,412
Total New Federal Obligation Authority	54,222	55,077	109,299