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

John Cline
Projected Budget Deficit 2010-2019

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

<table>
<thead>
<tr>
<th>Year</th>
<th>Current Law</th>
<th>Alternative Baseline A</th>
<th>Alternative Baseline B</th>
</tr>
</thead>
<tbody>
<tr>
<td>2010</td>
<td></td>
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<tr>
<td>2011</td>
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<td>2012</td>
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<td>2014</td>
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<td>2015</td>
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<td>2016</td>
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<td>2017</td>
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<td></td>
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<tr>
<td>2018</td>
<td></td>
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<td></td>
</tr>
<tr>
<td>2019</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

2015–2019 Averages
- Current Law: 2.7%
- Alternative Baseline A: 5.3%
- Alternative Baseline B: 6.6%
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.
Percentage of Revenues by Major Source

- **Social Security/Tax**: 30%
- **Corporate Income Tax**: 7%
- **Medicare**: 9%
- **Corporate Income Tax**: 9%
- **Individual Income Tax**: 45%

Source: Congressional Budget Office.
States Starving for Cash

- **California**
  - Gap: $6.6 B
  - % 2010 Budget: 7.2%

- **Washington**
  - Gap: $2.8 B
  - % 2010 Budget: 2.0%

- **Kansas**
  - Gap: $0.5 B
  - % 2010 Budget: 7.5%

- **Kentucky**
  - Gap: $1.2 B
  - % 2010 Budget: 12.2%

- **Illinois**
  - Gap: $5.0 B
  - % 2010 Budget: 14.3%

- **New York**
  - Gap: $3.2 B
  - % 2010 Budget: 5.7%

- **New Jersey**
  - Gap: $2.2 B
  - % 2010 Budget: 7.4%

- **Virginia**
  - Gap: $1.8 B
  - % 2010 Budget: 11.1%

- **Georgia**
  - Gap: $1.4 B
  - % 2010 Budget: 0.3%

- **Arizona**
  - Gap: $1.0 B
  - % 2010 Budget: 12.7%

- **Colorado**
  - Gap: $0.6 B
  - % 2010 Budget: 13.0%

- **Oklahoma**
  - Gap: $0.9 B
  - % 2010 Budget: 15.1%

- **Mississippi**
  - Gap: $0.4 B
  - % 2010 Budget: 8.8%
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 2011 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 significant 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 proposed 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 targets, application procedures of advance pricing arrangements.

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.

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 significantly increase compliance activities.
Scope of Reform

Revenue

- 45% Individual Income Tax
- 7% Corporate Income Tax
- 5% Other
- 1% Estate Tax
- 3% Excise Taxes
- 9% Medicare
- 30% Social Security

Total Revenue: $2.1 Trillion

Spending

- 36% Other Entitlement
- 15% Non-Defense Discret.
- 17% Social Security
- 11% Medicare
- 4% Net Interest
- 17% Defense

Total Spending: $3.5 Trillion


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”

- Tax Carried Interest as Ordinary Income: 23.1
- Reform Business Entity Classification Rules for Foreign Entities: 31.0
- Reform Foreign Tax Credit (Pooling): 45.5
- Defer, Deduction of Expenses, Except R&E, Related to Deferred Income: 51.5
- Repeal LIFO Accounting: 79.5
- Extend Look Through of Payments Between Related Controlled Foreign Corporations: (0.6)
- Extend the Deduction for State and Local Sales Tax: (2.8)
- Extend Subpart F Active Financing Provisions: (3.9)
- Make Research and Experimentation Tax Credit Permanent: (67.9)
CBO’s Options

- End of the Expensing of Exploration/Development Costs for Oil and Gas Companies: 44.9
- Eliminate the Source-Rules Exception for Exports: 53.7
- Tax the Worldwide Income of US Corporations as it is earned: 65.2
- Exempt Active Foreign Dividends from U.S. Taxation: 76.2
- Repeal Sec. 199 for all Companies for Domestic Production Activities: 136.2
- Extend Period for Recovering Cost of Equipment Purchases: 267.5
- (67.9)
- (417.3)
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

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

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

Source: Joint Committee on Taxation.
# Headquarters Location of Global 500 in 2000 and 2009

<table>
<thead>
<tr>
<th></th>
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</thead>
<tbody>
<tr>
<td></td>
<td>Total Revenue ($billions)</td>
<td>Number of companies</td>
<td>Statutory Corporate Tax Rate 1/</td>
<td>Total Revenue ($billions)</td>
<td>Number of companies</td>
</tr>
<tr>
<td>United States</td>
<td>4,681</td>
<td>179</td>
<td>39.2%</td>
<td>7,544</td>
<td>140</td>
</tr>
<tr>
<td>Japan</td>
<td>2,931</td>
<td>107</td>
<td>43.3%</td>
<td>2,980</td>
<td>68</td>
</tr>
<tr>
<td>Germany</td>
<td>1,217</td>
<td>37</td>
<td>52.0%</td>
<td>2,259</td>
<td>39</td>
</tr>
<tr>
<td>France</td>
<td>922</td>
<td>37</td>
<td>37.8%</td>
<td>2,166</td>
<td>40</td>
</tr>
<tr>
<td>China</td>
<td>200</td>
<td>10</td>
<td>33.0%</td>
<td>1,661</td>
<td>37</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>765</td>
<td>38</td>
<td>30.0%</td>
<td>1,585</td>
<td>27</td>
</tr>
<tr>
<td>Netherlands</td>
<td>391</td>
<td>10</td>
<td>35.0%</td>
<td>1,044</td>
<td>12</td>
</tr>
<tr>
<td>Italy</td>
<td>264</td>
<td>10</td>
<td>39.5%</td>
<td>699</td>
<td>10</td>
</tr>
<tr>
<td>Korea</td>
<td>242</td>
<td>12</td>
<td>30.8%</td>
<td>603</td>
<td>14</td>
</tr>
<tr>
<td>Switzerland</td>
<td>293</td>
<td>11</td>
<td>24.9%</td>
<td>566</td>
<td>15</td>
</tr>
<tr>
<td><strong>Total Top 10 1/</strong></td>
<td><strong>11,904</strong></td>
<td><strong>451</strong></td>
<td><strong>39.8%</strong></td>
<td><strong>21,106</strong></td>
<td><strong>402</strong></td>
</tr>
<tr>
<td>Other</td>
<td>792</td>
<td>49</td>
<td>35.7%</td>
<td>4,069</td>
<td>98</td>
</tr>
<tr>
<td><strong>Total Global 5001/</strong></td>
<td><strong>12,696</strong></td>
<td><strong>500</strong></td>
<td><strong>39.2%</strong></td>
<td><strong>25,175</strong></td>
<td><strong>500</strong></td>
</tr>
</tbody>
</table>

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.
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)

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

Source: Congressional Budget Office.
## Components of the Highway Trust Fund, 2011

(Billions of dollars)

<table>
<thead>
<tr>
<th></th>
<th>Estimated Revenues and Interest</th>
<th>Budget Authority and Obligation Limitations</th>
<th>Estimated Outlays</th>
</tr>
</thead>
<tbody>
<tr>
<td>Highway Trust Fund</td>
<td>36.9</td>
<td>52.7</td>
<td>44.3</td>
</tr>
<tr>
<td>Highway account</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Federal-aid highway program</td>
<td>n.a.</td>
<td>43.0</td>
<td>35.4</td>
</tr>
<tr>
<td>Motor carrier safety program</td>
<td>n.a.</td>
<td>0.6</td>
<td>0.5</td>
</tr>
<tr>
<td>Highway traffic safety program</td>
<td>n.a.</td>
<td>0.7</td>
<td>0.7</td>
</tr>
<tr>
<td>Mass transit account</td>
<td>5.1</td>
<td>8.4</td>
<td>7.6</td>
</tr>
</tbody>
</table>

Source: Congressional Budget Office.
Status of the Highway Account of the Highway Trust Fund

(Billions of dollars)

Revenue, Interest, and General Fund Transfers

Actual vs. Projected Outlays

End of Year Balance or Shortfall

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


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
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.

<table>
<thead>
<tr>
<th>Assumed Levels of Obligation Limitations</th>
<th>2012</th>
<th>2013</th>
<th>2012 Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>FHWA Federal-aid Highways</td>
<td>41,564</td>
<td>42,227</td>
<td>83,791</td>
</tr>
<tr>
<td>FMCSA Operations and Programs</td>
<td>245</td>
<td>251</td>
<td>496</td>
</tr>
<tr>
<td>FMCSA Motor Carrier Safety Grants</td>
<td>313</td>
<td>318</td>
<td>631</td>
</tr>
<tr>
<td>NHTSA Operations and Research</td>
<td>112</td>
<td>114</td>
<td>226</td>
</tr>
<tr>
<td>NHTSA Highway Traffic Safety Grants</td>
<td>626</td>
<td>636</td>
<td>1,262</td>
</tr>
<tr>
<td>FTA Formula and Bus Grants</td>
<td>8,435</td>
<td>8,568</td>
<td>17,003</td>
</tr>
<tr>
<td><strong>Total, HTF Obligation Limitations</strong></td>
<td><strong>51,295</strong></td>
<td><strong>52,114</strong></td>
<td><strong>103,409</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Contract Authority Exempt From Obligation Limitations</th>
<th>2012</th>
<th>2013</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>FWHA Exempt Obligations</td>
<td>739</td>
<td>739</td>
<td>1,478</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>General Fund Appropriations for Mass Transit</th>
<th>2012</th>
<th>2013</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>FTA Administrative Expenses</td>
<td>101</td>
<td>104</td>
<td>205</td>
</tr>
<tr>
<td>FTA Research and URCs</td>
<td>67</td>
<td>68</td>
<td>135</td>
</tr>
<tr>
<td>FTA Capital Investment Grants</td>
<td>2,020</td>
<td>2,052</td>
<td>4,072</td>
</tr>
<tr>
<td><strong>Total, GF Transit Authorizations</strong></td>
<td><strong>2,188</strong></td>
<td><strong>2,224</strong></td>
<td><strong>4,412</strong></td>
</tr>
</tbody>
</table>

| Total New Federal Obligation Authority               | 54,222| 55,077| 109,299|