
Washington Update

FTA Revenue Estimating and Tax
Research Conference
Minneapolis, Minnesota
September 24, 2001

Purpose

- Review legislation affecting state tax authority
- Review major elements of recent federal tax bill and issues for states
- Overview fiscal conditions and implications for states

ITFA/E-commerce Legislation

- Cox bills - Straight extension/permanent moratorium; repeal grandfather
- Dorgan et al. - S. 512 - Extend ITFA, set simplification standards, procedure for fast track approval of collection authority
- Wyden/Leahy - S. 288 - Extend IFTA, require BAT nexus standards, simplification standards, no fast-track

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Legislation [Cont.]

- BAT Nexus Bills - Gregg/Kohl (S. 664) and Goodlatte/Boucher (HR 2526)
 - Establish “substantial physical presence” standard (G/K also sales tax)
 - Establish carve-outs that are not “substantial physical presence”
- Conyers (HR 1697) 4-R protection for broadband providers

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State of Play

- House - Leadership committed to ITFA extension; interested in BAT nexus; uncertainty regarding strength of conviction among membership
- Senate - Good support for Dorgan bill with ultimate congressional review before authorization; mixed bag on BAT

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Outlook

- Congress working on seriously shortened and focused agenda
- ITFA is not on agenda
- Concern that 'rapacious' states will attack Internet with new taxes
- Issues may indeed 'go quietly into that good night' for this year
- BAT and sales tax likely to arise again; sales tax timing is ours
- Alternative scenario is straight, short-term (18-24 months) extension

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States need to ...

- Sharpen understanding of BAT issue among delegation
- Develop understanding/projection of the impact on state
- Strengthen positive approach on dialogue, etc. to resolve issues

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Major Pieces

- Marginal rate reductions
 - New 10 percent bracket
 - Drop others over time
 - Repeal “Pease” and “PEP”
- Marriage penalty relief
 - Standard deduction increase
 - Increase width of 15 percent
 - Begin in 2005

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Major Pieces [Cont.]

- Tax benefits relating to children
 - Increase child credit
 - Adoption assistance
 - Dependent care credit
- Education incentives
 - Expand Education IRAs
 - Above the line deduction for four years
 - Other stuff

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Major Pieces [Cont.]

- Retirement and pension provisions
 - Increase elective deferrals
 - IRA tax credit
 - Increase IRA contributions
- Phase-out of the estate tax
 - Increase unified exemption
 - Phase down rates
 - Step up basis limited
 - Repeal estate (not gift) tax in 2010
 - Phase-out state death tax credit

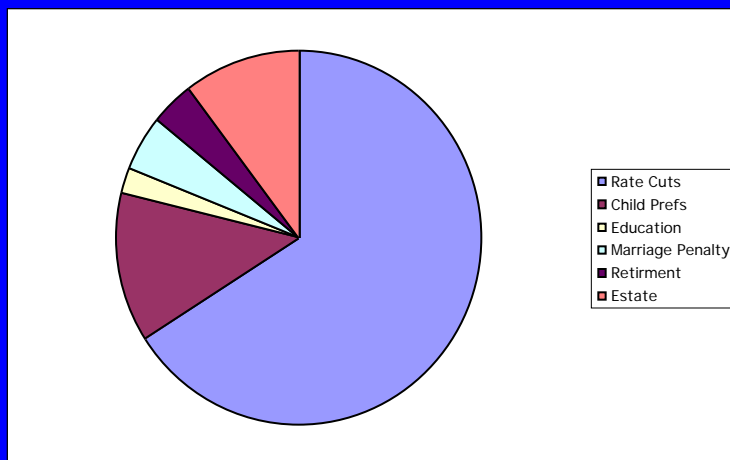
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State Death Tax Credit

- Credit calculation remains the same
- Amount allowed is reduced by 25% in 2002; 50% in 2003, 75% in 2004 and 100% in 2005
- Effect is to reduce state revenues in pick-up tax states; shift revenue to federal government
- Some movement to not conform to change -- leave at amount computed

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Distribution of Cuts



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Issues for States

- Quite Modest
- Estate tax
 - \$50 to \$75 billion over 10 years
- Base reductions
 - Higher education deduction
 - IRA expansions
 - Elective deferral expansions
 - Education IRAs

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Federal Issues - Pre-downturn

- Total sunset in 2010
- Intermittent sunsets
 - Education deduction
 - IRA credit
- AMT Relief
 - Number triples; \$300 billion
- Other relief 'requirements'
- Current surplus minus tax cut minus additional spending minus interest cost equals non-trust fund deficit

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Post-Downturn/Pre-attack

- Softening economy reduces receipts by \$40 billion in 2002
- Absolutely NO non-Social Security money for
 - More spending
 - Education and defense
 - Tax cuts
- Political spotlight on Social Security surplus and the proverbial “lockbox”
- Terrible predicament for both sides

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Post-Attack Outlook

- Near-term economic deterioration
- International threat to nation
- Lockbox pressure is off
 - Respond to terrorist threat
 - Meet critical national needs
 - Economic stimulus seems important
- Huge constraints removed
 - Will choices be made
 - What choices will be made

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Congressional Agenda

- Want to be home within one month
- Seriously curbed/focused agenda
 - Response to attacks -- Fiscal and legislative
 - Finish FY 2002 appropriations bills
 - Airline industry assistance
 - Education bill
 - Economic stimulus

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Stimulus Package

- Spending component
- Tax component
 - Capital gains
 - Rates/rebates
 - Accelerated depreciation
 - Energy provisions
 - Corporate reductions
- Not a lock-cinch
 - Disagreement on need
 - Disagreement on tools

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Issues for States

- Some potential “good news”
 - Bad things may not happen
 - ITFA-related bills could be left untouched
- Stimulus package has some risk
 - Efforts aimed at promoting investment could affect state tax bases
 - Unintended “bad things” could happen if state issues sacrificed to “national need”

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Conclusion

- Tax bill was a HUGE deal
- Impact on states is relatively modest, but terribly ill-timed
- Real issues are at federal level
 - Removed fiscal flexibility
 - Exacerbated by economic downturn and attack
 - Long-term economic outlook and unmet needs could occasion debate on wisdom of out-years
 - Debate on role and size of government
- Contentious period forthcoming

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