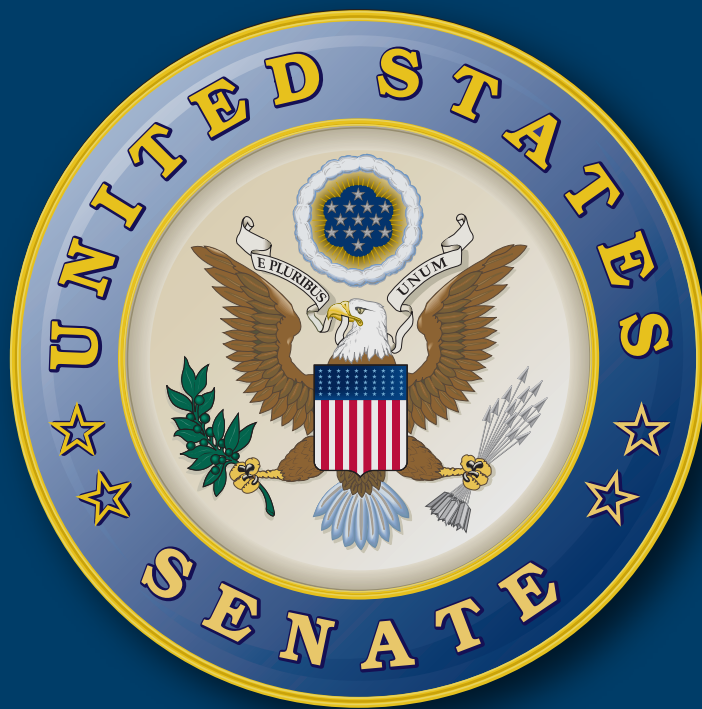


United States Senate Committee on Finance

The Community Development & Infrastructure Bipartisan Tax Working Group Report



July 2015

**REPORT OF THE COMMUNITY
DEVELOPMENT AND INFRASTRUCTURE
WORKING GROUP**

Submitted by the Working Group Co-Chairs

To: Chairman Hatch and Ranking Member Wyden

From: Community Development and Infrastructure Working Group Co-Chairs

As co-chairs of the Community Development and Infrastructure Working Group, we present to you this report. We want to begin by thanking the members of the Working Group: Senator Maria Cantwell (D-WA), Senator Dan Coats (R-IN), Senator Bill Nelson (D-FL) and Senator Tim Scott (R-SC).

We also want to thank the Chairman and Ranking Member for setting up these five working groups to continue the discussion on comprehensive tax reform. We also want to thank Tom Barthold and his team at the Joint Committee on Taxation (JCT) for their endless help on this report and throughout this process. Finally, the working group would like to thank the over 200 individuals and organizations that submitted recommendations.

In developing this report, our group met with a wide array of experts in both the public and private sectors, including holding numerous roundtables with key stakeholders, academics and other policy experts, as well as relevant policy staff at the Treasury Department and the Department of Transportation. We also regularly held information sessions with the JCT team and Congressional Budget Office (CBO) on select issues.

Our working group was tasked with not only exploring the current state of the Highway Trust Fund, but also examining the tax expenditures related to economic and community development. Some tax expenditures help state, local and tribal governments build infrastructure such as roads, bridges and airports, while other tax expenditures are for affordable rental housing for low-income families or for businesses to invest in impoverished and difficult-to-develop areas. Another area the working group analyzed was the current state of the tax code as it relates to the energy industry.

This report is in two parts. The first part describes the options that the co-chairs believe provide a funding alternative for the Highway Trust Fund. The second part, the appendix, describes background and present law of four specific areas [Highway Trust Fund (both funding and financing), energy, community tax incentives, and tribal tax incentives] the co-chairs believed were significant in future tax reform efforts. The appendix was prepared with substantial assistance from the staff of the JCT.

Additionally, both the co-chairs' staff and the working group members worked diligently to find common ground on various areas within our working group in an effort to move fundamental tax reform forward. We hope to continue working with the Committee on some of these ideas. Furthermore, this experience only reinforces that tax reform cannot be operated or negotiated in a vacuum. If lawmakers want tax reform, we all will need to work together in a collaborative manner.

That being said, our working group believes fundamental tax reform provides an opportunity to simplify the tax code, provide certainty to taxpayers and expand economic growth. Further, the Highway Trust Fund, which for all purposes is broke, provides an option to handle two of our country's most pressing problems: providing sufficient resources to fund highways and providing a competitive, permanent tax code for taxpayers.

As the Committee moves forward with fundamental tax reform, we are prepared to help in any way to advance the work of the working group. Moreover, we may be prepared on an individual member level to follow up with bipartisan legislation in the near term. Finally, the engagement of the other working group members were essential to the process, but their participation does not indicate that they agree with any or all of the details of the report outlined below.

Introduction:

According to the American Society of Civil Engineers, if we do not address our system of infrastructure funding, there will be an over \$1 trillion gap between our investment needs and the funding available by 2020.¹ Approximately 65% of major roads are rated in less than good condition, one in nine bridges are structurally deficient, and 45% of Americans lack access to transit.² As a percentage of gross domestic product (GDP), the United States spends less on infrastructure today than at any point in the last 50 years. We now spend just 2.4% of our GDP on public infrastructure.³ Meanwhile, China spends 8.5%.⁴

The Highway Trust Fund (HTF) plays a critical role in providing funding to American infrastructure, ranging from roads and bridges to mass transit. In general, the HTF consists of two accounts, one for highways and one for mass transit. Much of the revenue required to maintain the nation's transportation system is generated by excise taxes on motor fuels—consisting of an 18.3 cent per gallon tax on gasoline (also known as the gas tax) and a 24.3 cent per gallon tax on diesel fuels—which have not been increased since 1993. Receipts from the gas and diesel tax now constitute over 85% of the fund's total revenue with the remainder of taxes coming from a combination of taxes on the sale of heavy vehicles, truck tires and other taxes.

Under current law, the HTF cannot incur negative balances, nor can it borrow to cover unmet obligations. If the HTF is unable to make payments to states, projects could be halted and hundreds, if not thousands, of important construction jobs could be frozen. The Department of Transportation (DOT) estimated last year that the HTF insolvency could cost the United States 700,000 jobs and create road hazards and increased driving times for millions of drivers⁵. We believe this is unacceptable.

For several decades, the HTF's account balance was relatively stable or growing. However, since 2001, outlays from the HTF have exceeded tax revenues and the fund's balance has

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https://www.asce.org/uploadedFiles/Issues_and_Advocacy/Our_Initiatives/Infrastructure/Content_Pieces/failure-to-act-economic-impact-summary-report.pdf

² <http://www.infrastructurereportcard.org/bridges/>;
https://www.whitehouse.gov/sites/default/files/docs/economic_analysis_of_transportation_investments.pdf

³ <https://www.cbo.gov/publication/49910>

⁴ <http://www.wsj.com/articles/benefits-of-infrastructure-spending-not-so-clear-cut-economists-say-1422819575>

⁵ Remarks by Gregory Nadeau, Deputy Administrator, FHWA American Society of Civil Engineers Transportation and Development Institute Congress Orlando, Florida Tuesday, June 10, 2014
<http://www.fhwa.dot.gov/pressroom/re140610.cfm>

fallen almost every year since, according to the Congressional Budget Office (CBO). In short, this gap is projected to increase over the long term because revenues for the HTF are expected to remain flat while spending is expected to rise. For example, the HTF will collect approximately \$39 billion in revenue this fiscal year. But it is projected to distribute \$52 billion in projects over the same period, leading to a projected shortfall of \$13 billion.⁶

How bad is it? The failure of these dedicated revenues to keep pace with spending is projected to cause the HTF to have a cumulative shortfall of roughly \$168 billion from FY2015 through FY2025, according to the CBO.

In large part, the shortfall continues to grow because revenues, specifically those generated from the gas tax, are projected to decline due to a combination of drivers traveling fewer total miles, improved overall fleet fuel economy (which could be due to increased fuel prices and/or the mandated increases in corporate average fuel economy standards, or CAFE standards) and an increase in alternative fuel vehicles. Additionally, since most HTF obligations involve capital projects that take years to complete, if states were given no further authority to spend, it would take roughly three years of revenues (Federal motor fuel excise taxes equal roughly \$35 billion per year) just to meet the HTF's current obligations. The transit account, likewise, supports projects that can take years to complete. Collections of almost five years' worth of taxes, at about \$5 billion a year, would be required just to meet current obligations.⁷ In effect, the majority of the current funding sources, specifically the gas tax, could erode more quickly than previously thought and are not sustainable in the long term.

Because of looming shortfalls in funding, lawmakers have transferred over \$65 billion since 2008 from the U.S. Treasury's general fund to the HTF. In private meetings and roundtables, stakeholders have continually told our working group that the lack of agreement on a structural fix creates periodic funding crises, causing states to scramble for funding for temporary construction or at worse abandon projects; putting infrastructure projects and construction jobs at risk. This is no way for state and local governments to plan adequately. These short-term crises provide little confidence to stakeholders that the federal government will be able to support projects over the long term.

In addressing a solution for the HTF, the working group considered all options, including but not limited to a national vehicle registration fee, maintaining the existing user-fee model but adjusting it for inflation, designating other sources of revenue to *replace* the existing taxes of the HTF, and reducing spending. The working group analyzed countless

⁶ Congressional Budget Office, Projections of Highway Trust Fund Accounts-CBO's March 2015 Baseline (March 2015), <https://www.cbo.gov/sites/default/files/cbofiles/attachments/43884-2015-03-HighwayTrustFund.pdf>.

⁷ Congressional Budget Office, Testimony: The Status of the Highway Trust Fund and Options for Financing Highway Spending (May 2014), www.cbo.gov/publication/43135.

legislative proposals, CBO and the Joint Committee on Taxation (JCT) reports, infrastructure tax reform options as listed in the Senate Finance Committee staff discussion draft issued April 25, 2013, and the recommendations suggested by the National Surface Transportation Infrastructure Financing Commission. Our working group benefited from extensive input from a wide array of experts, continued discussions with the Administration, including Secretaries Jack Lew and Anthony Foxx, lawmakers, stakeholders and tax-writing staff.

In evaluating each proposal, our working group asked the following questions:

- How can we find a sustainable funding source for a medium-term authorization that removes Congress from this cycle of short-term highway patches;
- How do we begin a conversation on a sustainable, long-term funding source; and
- How does each option promote efficiencies while maintaining a similar framework of the current user-fee system?

Each of the working group members had their preferences toward a certain option. However, the overall goal of the working groups was to find a *bipartisan solution* in the context of fundamental tax reform.

The working group co-chairs hope that fundamental tax reform can provide an opportunity to address the fiscal solvency of American infrastructure. Accordingly, we offer a bipartisan option that could bring the HTF into solvency while addressing fundamental tax reform. The working group co-chairs also recognize that while such change will neither occur overnight nor will be easy, transportation investments, which are in critical need, cannot afford to wait.

This report represents a cautious consensus of opinion about strategies. We believe these options can provide a useful road map, both in the interim and potentially in the long term, to address our crisis in infrastructure funding while responding to the urgent need to do fundamental tax reform.

We appreciate the opportunity to serve as co-chairs of the working group and hope that these options will aid lawmakers and the Administration's efforts to ensure the sustainability and solvency of the Highway Trust Fund.

The remainder of the report, the Appendix, contains the current law of four areas that the working group focused on during these past few months: infrastructure financing, tribal issues, community development tax incentives and energy. There is also further background on the funding for the Highway Trust Fund. Although our group was not able to reach bipartisan recommendations in each of these areas, we feel each of these parts should be heavily focused on as fundamental tax reform moves forward. Our working group would be happy to relay additional input, which we received from stakeholders and

lawmakers, as this process moves forward. Given the substantial amount of work and time put into these working groups, both co-chairs may release bipartisan legislative proposals in the near term.

Interim Option:

As stated above, a key principle that our working group established early on was finding a solution that ensured the sustainability and solvency of the Highway Trust Fund. At the same time, as lawmakers, tax writers, and taxpayers, we understand the need to overhaul the tax code. Addressing both of these issues is critically important to providing certainty and competitiveness to American businesses and taxpayers.

Recent estimates indicate that U.S. multinationals have over \$2 trillion of deferred earnings in controlled foreign corporations (CFCs). In transitioning to a competitive international tax system as part of comprehensive tax reform, lawmakers may want to eliminate the deferral of tax on the \$2 trillion of past foreign earnings of U.S. multinationals. The foreign earnings could be “deemed repatriated” to the U.S. multinational parent entity. Eliminating this corporate tax expenditure on pre-existing foreign earnings could be coupled with an overhaul of the tax code, and payable over several years, to allow businesses sufficient time to comply with the new legislation.⁸

Both former Ways and Means Chairman Dave Camp and the Administration have proposed using a one-time transition tax on all previously untaxed foreign earnings and profits (E&P) to pay for long-term infrastructure spending as a part of an overhaul of the tax code.

Depending on the rate and how the transition fee was structured, various proposals for deemed repatriation have indicated that substantial revenue could be raised.

We realize this option may not be a permanent solution, but we believe it could provide an interim measure to addressing some of our nation’s most critical needs. It was our understanding, when our working group discussions began, that a six-year infrastructure solution would be both a realistic goal and one in which both lawmakers and the Administration backed. CBO has estimated that it would require roughly \$90 billion through 2021 to close the shortfall. It is important to note that the Senate Environment and Public Works Committee recently approved, by a unanimous vote, the reauthorization of the Federal-aid highway program for six years at an increased funding level. This funding amount aims to create a modern, 21st century highway system.

⁸ Certain working group members would have concerns with deemed repatriation legislation unless it was considered in conjunction with fundamental tax reform which broadened the base and lowered tax rates.

In the context of tax reform, deemed repatriation could play a very important role to achieving a bipartisan solution to fix America's roads and bridges, while also overhauling our broken tax code. We hope fundamental tax reform embraces key principles outlined by Chairman Hatch earlier this year, such as promoting economic growth, simplicity, permanence and competitiveness. And our working group option could provide a funding bridge to achieving proper long term solutions on both issues.

Long Term Option:

Another key principle our working group discussed was ensuring users and direct recipients of infrastructure systems pay the cost of their use.

A mileage-based tax system, also known as a vehicle miles traveled tax, or VMT, generally taxes users based on the number of miles travelled. A VMT has the potential to improve the efficiency of highway financing because the tax can be calibrated closely to the costs that vehicles impose in terms of road damage and congestion.⁹ Additionally, the tax could be calculated based on time of day, congestion, type of road, type of vehicle, etc.

However, evaluating the experiences of VMTs has been limited to date. Two substantial pilot VMT programs were put in place in Oregon. With respect to the last pilot, it was concluded that a VMT system can protect privacy, allow for multiple reporting and payment choices, and be easy to use. Based on that conclusion, the Oregon Legislature authorized a 5,000 volunteer Road Usage Program to take effect later this summer. A number of states have passed laws creating similar pilot programs or are undertaking feasibility studies to see a VMT's potential revenue impact. Additionally, both sides of the country, with the Western Road Usage Charge Consortium and the I-95 Coalition, are considering moving forward with various degrees of a VMT. The goals of these discussions at a state level are generally to *replace* their fuel tax with a VMT.

Deemed repatriation is not a long-term solution to the HTF. As previously stated, it does not correct the declining revenues of the gas tax, nor does it address the increase in emerging technologies among vehicles today. Implementation of a pilot nationwide VMT program with 5,000 volunteers, for example, could be considered as an option to address the long-term sustainability of the Highway Trust Fund. We would work with both the Secretary of Transportation and the relevant authorizing committees to structure the program.

⁹ See generally, Congressional Budget Office, *Alternative Approaches to Funding Highways* (March 2011) at 17; Joint Committee on Taxation, *Long-Term Financing of the Highway Trust Fund*, (JCX-92-15), June 15, 2015 at 14.

Some considerations of a pilot nationwide program could be:

- The VMT would *replace* and refund a volunteer's existing federal fuel taxes so that a user is not double-taxed;
- Provide several options to individuals signing up, including High-Tech (GPS) and Low-tech (non-GPS device that reports out mileage); and
- Provide strict policies that employ every possible method to protect privacy.

Various administrative issues would need to be considered, including the type of VMT program adopted, who would implement the program and which specific technologies would be chosen to track and report mileage, among others.

In discussions with stakeholders, a nationwide program could take up to a decade to fully implement. Our proposed pilot program, as well as experiences in other states, could inform lawmakers about the practicality and challenges of adopting such a system. That being said, the working group co-chairs would urge lawmakers not to wait to address the long term solvency of the HTF.



Appendix

THE APPENDIX TO THIS REPORT WAS PREPARED WITH THE SUBSTANTIAL ASSISTANCE OF THE STAFF OF THE JOINT COMMITTEE ON TAXATION.

I. HIGHWAY TRUST FUND

Overview

Six separate excise taxes are imposed to finance the Federal Highway Trust Fund program. Three of these taxes are imposed on highway motor fuels, and these three generate the substantial majority of the revenues dedicated to the Highway Trust Fund. The remaining three are a retail sales tax on heavy highway vehicles (trucks, trailers and certain tractors), a manufacturers' excise tax on heavy vehicle tires, and an annual use tax on heavy vehicles.

The highway motor fuels taxes consist of an 18.3 cents per gallon tax on gasoline, a 24.3 cents per gallon tax on diesel fuel and kerosene, and a tax of 18.3 or 24.3 cents per gallon tax on alternative fuels depending on the type of fuel.¹⁰

A 12-percent retail sales tax is imposed on the first retail sale of heavy trucks (over 33,000 pounds), trailers (over 26,000 pounds) and certain highway tractors.¹¹

Tires are taxed at a rate of 9.45 cents for each 10 pounds of maximum rated load capacity over 3,500 pounds.¹² For biasply tires, and super single tires (other than those designed for steering), the rate of tax is half the regular rate, 4.725 cents for each 10 pounds of maximum rated load capacity over 3,500 pounds.¹³

An annual use tax is imposed on heavy highway vehicles over 55,000 pounds. The tax is \$100 plus \$22 per 1,000 pounds over 55,000 pounds, capped at \$550 for vehicles over 75,000 pounds.

The majority of revenues for the Highway Trust Fund come from the motor fuels taxes. Figure 1, below, shows the projected taxes for fiscal year 2015.

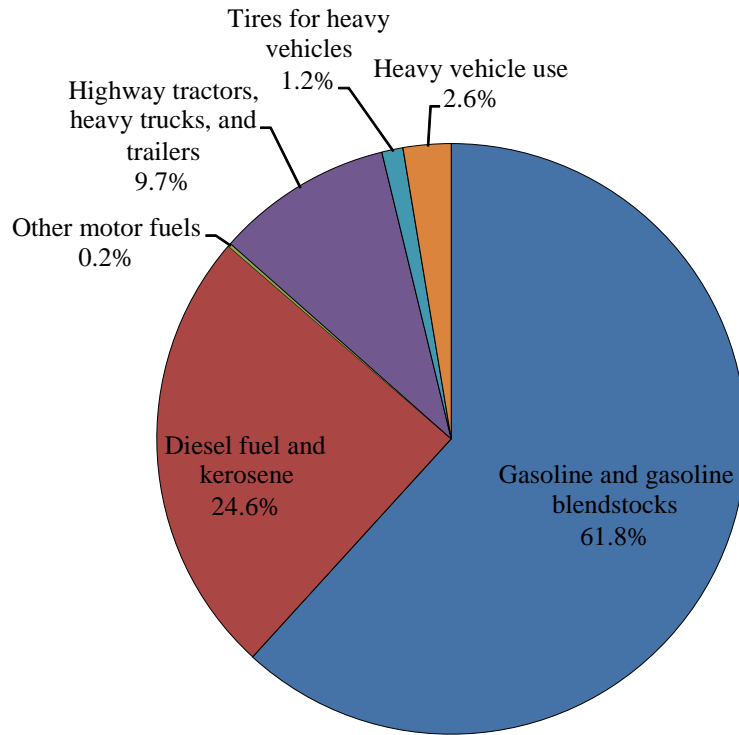
¹⁰ The rate of tax is 24.3 cents per gallon in the case of liquefied natural gas, any liquid fuel (other than ethanol or methanol) derived from coal, and liquid hydrocarbons derived from biomass. Other alternative fuels sold or used as motor fuel are generally taxed at 18.3 cents per gallon. For purposes of this pamphlet "alternative fuel" includes compressed natural gas. The rate for compressed natural gas is 18.3 cents per energy equivalent of a gallon of gasoline. See sec. 4041(a)(2) and (3).

¹¹ Sec. 4051. The tax does not apply to tractors weighing 19,500 pounds or less that, in combination with a trailer or semitrailer, has a gross combined weight of 33,000 pounds or less.

¹² Sec. 4071(a). In general, these parameters would exclude tires for passenger automobiles and light trucks.

¹³ Sec. 4071(a). The term "biasply tire" means a pneumatic tire on which the ply cords that extend to the beads are laid at alternative angles substantially less than 90 degrees to the centerline of the tread. A "super single tire" means a single tire greater than 13 inches in cross section width designed to replace two tires in a dual fitment. It does not include any tire designed for steering.

Figure 1.—Projected Highway Trust Fund Taxes, FY2015



Source: CBO March 2015 Updated Budget Projections 2015 to 2025

Under the March 2015 CBO baseline projections, revenues from gasoline taxes dedicated to the Highway Trust Fund are estimated to fall from \$24.3 billion in FY 2015 to \$20.3 billion in FY 2025. This is a decrease of about 16 percent over a decade. The decline in revenue is due to a number of factors, including a decline in total miles driven, improved overall fleet fuel economy, and modest growth in vehicles that are powered by fuels not subject to the Highway Trust Fund taxes (e.g. natural gas) or by electricity; currently, less than 0.5% of U.S. vehicles run on alternative fuels or electricity. Additionally, the motor fuel taxes are not indexed. Had the gasoline and diesel fuel taxes been indexed since 1993, in 2015 the gasoline tax rate would have been 31.0 cents per gallon and the diesel fuel rate would have been 41.2 cents per gallon.

As Table 1, below, shows, CBO projects the Highway Trust Fund will have a cumulative shortfall of roughly \$168 billion from FY 2015 through FY 2025. Through FY 2020, the cumulative shortfall is \$69 billion and through FY 2021 the cumulative shortfall is \$87 billion.

**Table 1.—Estimates of Revenue and Outlays for the Highway Trust Fund
Fiscal Years 2014-2025**
[billions of dollars]

	2014	2015	2016	2017	2018	2019	2020	2021	2022	2023	2024	2025
Highway Account												
Start-of-Year Balance	4	11	2	a	a	a	a	a	a	a	a	a
Revenues & Interest ^b	34	34	35	35	35	35	35	35	35	35	34	34
Intragovernmental Transfers ^c	18	0	0	0	0	0	0	0	0	0	0	0
Outlays	45	44	45	45	46	46	47	48	48	49	50	50
End of Year Balance**	11	2	a	a	a	a	a	a	a	a	a	a
Transit Account												
Start-of-Year Balance	2	3	1	a	a	a	a	a	a	a	a	a
Revenues and Interest ^b	5	5	5	5	5	5	5	5	5	5	5	4
Intragovernmental Transfers ^c	4	0	0	0	0	0	0	0	0	0	0	0
Outlays ^d	8	8	8	8	8	9	9	9	10	10	9	10
End-of-Year Balance	3	1	a	a	a	a	a	a	a	a	a	a
Memorandum												
Cumulative Shortfall ^a												
Highway Account	n.a.	n.a.	-8	-19	-29	-41	-52	-65	-79	-93	-108	-125
Transit Account	n.a.	n.a.	-3	-6	-9	-13	-17	-22	-27	-32	-37	-43

Notes: Details may not add to totals because of rounding.
n.a. = not applicable.

a. Beginning in fiscal year 2015, CBO projects, revenues credited to the highway and transit accounts of the Highway Trust Fund will be insufficient to meet the fund's obligations. Under current law, the trust fund cannot incur negative balances, nor is it permitted to borrow to cover unmet obligations presented to the fund. Under the Balanced Budget and Emergency Deficit Control Act of 1985, however, CBO's baseline for highway and transit spending must incorporate the assumption that obligations incurred by the Highway Trust Fund will be paid in full. As a result, the cumulative shortfalls shown here are estimated on the basis of spending that would occur if obligations from the fund each year were equal to the obligation limitations enacted for 2014, adjusted for projected inflation. To meet obligations as they come due, the Department of Transportation estimates, the highway account must maintain a cash balance of at least \$4 billion and the transit account must maintain a balance of at least \$1 billion.

b. Some of the taxes that are credited to the Highway Trust Fund are scheduled to expire on September 30, 2016, among them the taxes on certain heavy vehicles and tires and all but 4.3 cents of the federal tax on motor fuels. However, under the rules governing baseline projections, these estimates reflect the assumption that all of the expiring taxes credited to the fund continue to be collected.

c. Sections 40201 and 40251 of the Moving Ahead for Progress in the 21st Century Act (Public Law 112-140) and section 2002 of the Highway and Transportation Funding Act of 2014 (Public Law 113-159) required certain intergovernmental transfers, mostly from the general fund of the Treasury, to the Highway Trust Fund CBO's baseline does not reflect an assumption that additional transfers from the general fund would occur.

d. Outlays include amounts transferred between the highway and transit accounts. CBO estimates that those amounts would total about \$1 billion annually.

II. FINANCING

BACKGROUND AND PRESENT LAW: BONDS AND PUBLIC-PRIVATE PARTNERSHIPS

Bonds

In general

Present law generally involves three different structures to deliver Federal borrowing subsidies on State and local governmental bonds:

1. tax-exempt bonds (in which the State and local governmental borrowing cost is lower because the interest income is tax-exempt to the investor and thus the investor is willing to accept a lower interest rate);
2. tax-credit bonds (in which the State and local governmental borrowing cost is lower because investors receive Federal tax credits to replace a prescribed portion of the interest cost on the taxable bonds); and
3. tax-credit bonds issued as “direct-pay bonds” (in which the State or local governmental borrowing cost is lower because the Federal Government makes direct payments to issuers to cover a prescribed portion of the interest cost on the taxable bonds, for example the now expired Build America Bonds program and certain specified tax-credit bonds).

Tax exempt bonds

Tax-exempt bonds issued by State and local governments may be classified as either governmental bonds or private activity bonds. Present law does not limit the types of facilities that can be financed with governmental bonds. Thus, State and local governments can issue tax-exempt governmental bonds to finance a broad range of transportation infrastructure projects, including highways, railways, airports, etc.

While the types of projects eligible for governmental bond financing are not circumscribed, present law imposes restrictions on the extent to which private parties may benefit from tax-exempt financing. State and local governments may issue qualified private activity bonds for certain transportation infrastructure such as airports, port facilities, mass commuting facilities, high-speed intercity rail facilities and qualified highway or surface freight transfer facilities.

Over the period 2002 through 2011, State and local governments have issued on average \$384 billion in tax-exempt bonds. As of 2014, State and local governments had total municipal security liabilities of nearly \$3 trillion.

Below are the general tax expenditures for the governmental and certain qualified private activity bonds:

Tax Expenditure Estimates for Exclusion of Interest on Governmental and Qualified Private Activity Bonds, Fiscal Years 2014 - 2018 [1]

[Billions of Dollars]

Provision	Corporations					Individuals					Total 2014-18
	2014	2015	2016	2017	2018	2014	2015	2016	2017	2018	
Public purpose State and local government bonds.....	9.3	9.7	9.8	10.1	10.3	23.8	25.6	26.0	26.7	29.1	179.6
Qualified private activity bonds for:											
Private nonprofit and qualified public educational facilities.....	0.9	1.0	1.0	1.0	1.1	2.3	2.6	2.6	2.8	2.9	18.3
Private nonprofit hospital facilities.....	0.6	0.7	0.7	0.7	0.7	1.6	1.8	1.8	2.0	2.0	12.5
Owner-occupied housing [2].....	0.3	0.3	0.4	0.4	0.4	0.9	0.9	0.9	1.0	1.1	6.6
Rental housing.....	0.3	0.3	0.3	0.3	0.3	0.7	0.7	0.7	0.8	0.8	5.2
Private airports, docks, and mass-commuting facilities.....	0.2	0.2	0.3	0.3	0.3	0.6	0.7	0.7	0.7	0.7	4.7
Student loans.....	0.1	0.2	0.2	0.2	0.2	0.4	0.4	0.4	0.4	0.5	2.9
Sewage, water, and hazardous waste facilities.....	0.1	0.1	0.1	0.1	0.1	0.3	0.3	0.3	0.3	0.4	2.2
Small-issue.....	0.1	0.1	0.1	0.1	0.1	0.3	0.3	0.3	0.3	0.3	2.0
Highway projects and rail-truck transfer facilities.....	[3]	[3]	[3]	[3]	0.1	0.1	0.1	0.1	0.1	0.1	0.5
Veterans' housing.....	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	0.3
Energy production facilities.....	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	0.2
Green buildings and sustainable design projects.....	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	0.1
High-speed intercity rail facilities.....	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	[3]	0.1

Joint Committee on Taxation

NOTE: Details may not add to totals due to rounding.

[1] Reflects legislation enacted by June 30, 2014.

[2] Estimate includes effect of credit for interest on certain home mortgages (Section 25).

[3] Positive tax expenditure of less than \$50 million.

Direct-pay bonds

The income exclusion of interest on tax-exempt bonds provides a Federal subsidy to borrowers but, in practice, some of the subsidy accrues to the bond investors. Because there are not enough high tax bracket buyers in the market, issuers must offer higher interest rates on their bonds to attract investors in the lower tax brackets. The issuers do not have different interest rates for each investor so the high tax bracket investor benefits from the existence of lower tax-bracket purchasers and the State or local government pays a higher rate of interest than it would have in an ideal world where all investors are high tax bracket investors. This leakage of benefit to higher tax-bracket investors is why tax-exempt bonds are called by some as being inefficient. Direct-pay bonds address this inefficiency by providing the subsidy directly to the State or local government issuer. Therefore the degree of subsidy is not dependent on the tax bracket of the bond investor. Direct-pay bonds are thought to be a more efficient delivery mechanism of the Federal subsidy to the States.

Build America Bonds (“BABs”) were created by the American Recovery and Reinvestment Act of 2009 (“ARRA”) as a new form of State and local governmental bond. The interest income on a BAB is taxable to the bondholder and the issuer receives a refundable credit (a Federal government payment) equal to 35 percent of the interest payments on the bond. The provision applied to bonds issued after April 1, 2009, and on or before December 31, 2010. During this period over \$182 billion of BABs were issued, including \$117 billion in 2010. In 2010, BABs accounted for approximately 28 percent of the total volume of long-term State and local governmental bond issuance. There have been numerous proposals to extend BABs or create alternative direct-pay instruments.

Public Private Partnerships

Another mechanism for financing infrastructure is through the use of public-private partnerships.

In general

The Department of Transportation defines public-private partnerships broadly to include “contractual agreements formed between a public agency and a private sector entity that allow for greater private sector participation in the delivery and financing of transportation projects.”¹⁴ The private sector historically has participated in the design and construction of U.S. highways, most commonly as contractors to the public sector. A public-private partnership, however, generally is understood as shifting more of the economic risks (and attendant rewards) of a transportation project to the private sector than would be the case in a traditional public owner-private contractor relationship. For example, a public-private partnership might contemplate a private firm taking on all the design and construction risks for a new project, or a private firm operating a project for a period of years following construction, and obtaining an economic return based on the relative success of its management. State and local governments have shown increasing interest in public-private partnership arrangements as a means of shifting the

¹⁴ U.S. Department of Transportation, Federal Highway Administration, *Innovative Program Delivery*, “P3 Defined” <http://www.fhwa.dot.gov/ipd/p3/defined/default.aspx>.

increasing costs and risks of infrastructure development and maintenance to private parties, in exchange for those private parties receiving some economic benefit.¹⁵

Examples of public-private partnerships¹⁶

Long-term leases of existing infrastructure assets

Some private firms have acquired economic interests in the financing, maintenance, and operation of public highways after they are built.¹⁷ Two arrangements, involving the Chicago Skyway and the Indiana Toll Road, illustrate how the public-private partnership concept can be applied to transfers of economic interests in existing highways from the public sector to private firms. The Chicago Skyway and Indiana Toll Road deals are structured as very long-term arrangements: 99 years in the former case, and 75 years in the latter case. For tax purposes, each transaction can be seen as comprising three operating relationships, each of which in turn runs for the length of the overall arrangement:

1. A lease of the existing infrastructure (the highway itself and associated improvements) from the public owner to the private firm;
2. A grant by the public owner to the private firm of a right of way on the public lands underlying that infrastructure; and
3. A grant of a franchise from the public entity permitting the private party to collect tolls on the highway.

In return, the private party paid a large up-front amount to the public owner, and agreed to operate and maintain the road, to invest specified amounts in future improvements, and to

¹⁵ For background on infrastructure investment, see Congressional Budget Office, *Issues and Options in Infrastructure Investment* (May 2008) (public-private partnership discussion pp. 32-33). See also, Department of the Treasury, Office of Economic Policy, *Expanding our Nation's Infrastructure through Innovative Financing* (September 2014), available at http://www.treasury.gov/press-center/press-releases/Documents/Expanding_our_Nation's_Infrastructure_through_Innovative_Financing.pdf.

¹⁶ For purposes of discussion, this pamphlet focuses on public-private partnerships involving long-term leases of infrastructure assets by a private party, as well those involving the responsibility to design, build, finance, operate, and maintain new infrastructure assets by a private party. The Department of Transportation classifies public-private partnerships into seven categories. For new build facilities, there are five categories: private contract fee services, design-build, design-build-operate-maintain, design-build-finance, and design-build-finance-operate-maintain-concession. For existing facilities, there are two categories: operations and maintenance ("O&M") concession, and long-term lease concession. U.S. Department of Transportation, Federal Highway Administration, *Innovative Program Delivery*, "P3 Defined" <http://www.fhwa.dot.gov/ipd/p3/defined/default.aspx>.

¹⁷ For background on public-private partnerships, see CRS Report R43410, *Highway and Public Transportation Infrastructure Provision Using Public-Private Partnerships (P3s)*, by William J. Mallett (March 5, 2014); U.S. Government Accountability Office, *Highway Public-Private Partnerships, More Rigorous Up-front Analysis Could Better Secure Potential Benefits and Protect the Public Interest*, GAO-08-44 (Washington, DC: February 2008).

accept restrictions on the maximum tolls it could charge.¹⁸ An umbrella concession agreement sets out the long-term rights and obligations of each party including dispute resolution mechanisms.

More specifically, in 2004, the City of Chicago leased the Chicago Skyway, a 7.8 mile toll road south of downtown Chicago that connects two major highways, in the first long-term lease of an existing toll road in the United States. Under the 99-year concession agreement with Skyway Concession Company Holdings LLC, a joint venture between Cintra of Madrid, Spain, and Macquarie of Sydney, Australia,¹⁹ the City of Chicago received a \$1.8 billion up-front payment in exchange for granting the private concessionaire the exclusive right to use, possess, operate, manage, maintain, rehabilitate, and collect tolls from the Chicago Skyway.

In 2006, the Indiana Finance Authority (“IFA”) entered into a 75-year concession agreement with ITR Concession Company LLC (“ITR”), also a joint venture between Cintra and Macquarie, in respect of the Indiana Toll Road. IFA received a \$3.8 billion up-front payment in exchange for granting ITR the exclusive right to operate, manage, maintain, rehabilitate, and collect tolls from the Indiana Toll Road.

Design, build, finance, operate, and maintain new infrastructure assets

Alternatively, some private firms take on all the design and construction risks for a new project (in accordance with standards specified by the public agency), as well as the financing, maintenance, and operation of the infrastructure assets after they are built. Two arrangements in Colorado, an approximately 40-mile commuter rail project (the “Eagle P3”) and the Colorado U.S. 36 Express Lanes Project (“U.S. 36 P3”) are examples of a private-public partnership where the public sector transferred the responsibilities to design, build, finance, operate, and maintain the project to the private firm. This type of public-private partnership arrangement can be seen as comprising an exclusive right to design and build new public-use infrastructure assets in accordance with the public agency’s specified standards, and a lease of the new infrastructure assets from the public owner to the private firm for the term of the concession agreement. Unlike public-private partnerships involving long-term leases of previously existing infrastructure assets, the private party in a design-build-finance-operate-maintain (“DBFOM”) concession arrangement does not pay a large up-front amount to the public owner. Rather, the costs of construction are generally funded with equity capital, third-party debt, tax-exempt financing, federal loans, and/or federal grants. In return for operating and maintaining the infrastructure assets, the private party agrees to collect fees for the term of the agreement (*e.g.*, tolls from end users or availability payments from the public owner), which are structured to meet the debt service requirements, costs of operating and maintaining the infrastructure assets,

¹⁸ See summaries of these arrangements at U.S. Department of Transportation, Federal Highway Administration, *Innovative Program Delivery* “Project Profiles,” http://www.fhwa.dot.gov/ipd/p3/project_profiles/.

¹⁹ “Cintra” and “Macquarie” refer to these companies generally. In the case of Skyway Concession Company Holdings LLC, the investment is owned, indirectly, by Cintra Concesiones de Infraestructuras de Transporte, SA and Macquarie Infrastructure Group.

and payments to equity investors. An umbrella concession agreement sets out the long-term rights and obligations of each party including dispute resolution mechanisms.²⁰

More specifically, in 2010, Denver’s Regional Transportation District (“RTD”) entered into a 34-year concession agreement with Denver Transit Partners (“DTP”), a partnership between Fluor Enterprises, Inc., Denver Rail (Eagle) Holdings, Inc., and Aberdeen Infrastructure Investments (No. 4) USA LLC to expand and operate commuter rail transit across the Denver metro region (*i.e.*, approximately 40 miles of commuter rail lines). The Eagle P3 is a \$2.2 billion project, including \$1.03 billion in federal funding and \$450 million in private financing. Under the 34-year concession agreement, DTP will collect availability payments from RTD to operate and maintain the commuter rail system based on established performance standards for the operation and maintenance of the project (*e.g.*, incident management, days the infrastructure is available for use, closures, snow removal, *etc.*), while RTD will retain ownership of the assets, set fares and fare policies, and keep project revenues.²¹

²⁰ See summaries of these arrangements at U.S. Department of Transportation, Federal Highway Administration, *Innovative Program Delivery* “Project Profiles,” http://www.fhwa.dot.gov/ipd/p3/project_profiles/.

²¹ Note that in the case of the Eagle P3, the rights of way are granted to RTD by railroad companies (*i.e.*, RTD entered into rights of way with: Union Pacific for the East Corridor Line, BNSF Railway Company for the Gold Line, and BNSF Railway Company for the Northwest Electrified Segment).

III. OVERVIEW OF DOMESTIC ENERGY AND ENERGY TAX PROVISIONS

Background

The Internal Revenue Code plays a significant role in the domestic energy market. Depending on the method used for counting, there are over 40 distinct energy tax provisions in the Code, not including fuel taxes and other special levies, such as the gas guzzler tax. These provisions include special cost recovery rules, credits, bonds provisions, deductions, capital gains treatment, and pass-through rules.

About half of the current energy tax provisions expire, are capped, or are otherwise temporary. Many of these temporary provisions expired at the end of 2014. Most of the provisions relating to fossil fuels are permanent law, and many of them are more than 60 years old (although Congress has modified them from time to time). On the other hand, most of the provisions relating to renewable and alternative sources of energy are temporary and are less than 25 years old.

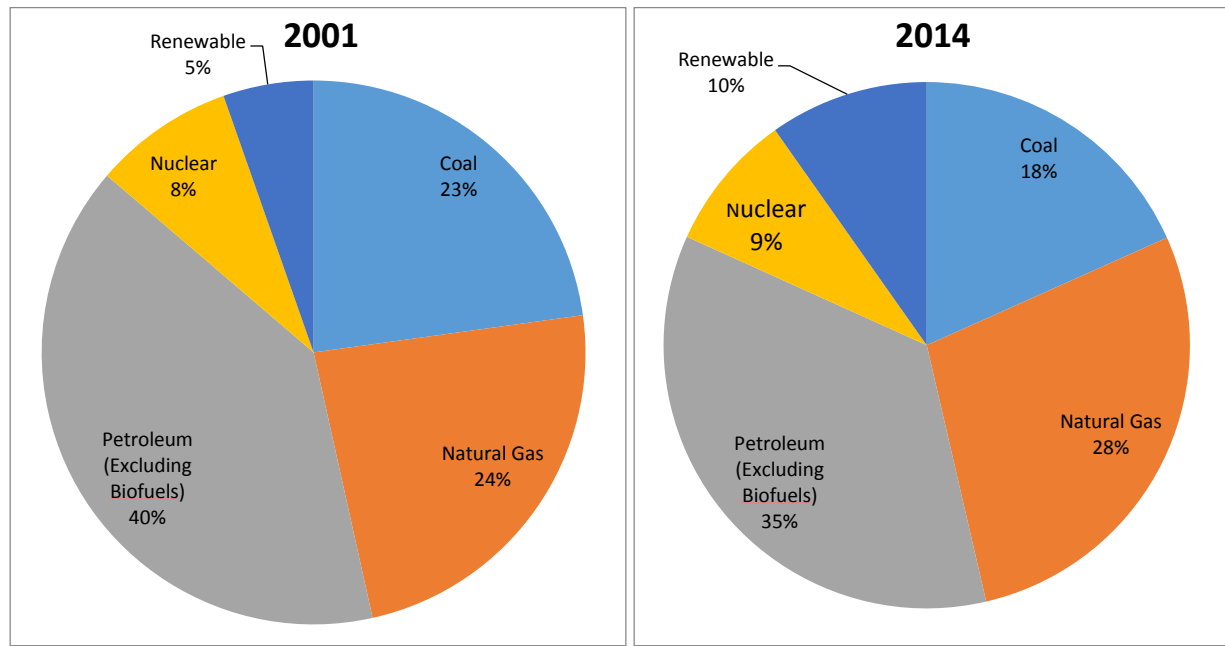
What is the Current Makeup of the Industry?

In 2014, over 80 percent of U.S. energy consumption came from fossil fuels while only about 10 percent of U.S. energy consumption came from renewable sources (including 2.6 percent from conventional hydroelectric power), with the remainder coming from nuclear power.²² That being said, in recent years there has been increased interest in, and adoption of, tax subsidies for conservation of energy and for development of renewable sources of energy. In part as a result of these subsidies, renewable energy production has grown significantly in recent years. For example, net power generation from wind energy has increased more than tenfold over the past decade, from 17.8 terawatt-hours in 2005 to 181.8 terawatt-hours in 2014.²³

²² Energy Information Administration, *Monthly Energy Review*, August 2014, Table 1.3, p. 6.

²³ Energy Information Administration, *Electric Power Monthly*, May 2015, Table 1.1.A.

The following table illustrates the changing make-up of the energy industry over the past decade.



Generating using data from the Energy Information Administration, *Monthly Energy Review*, April 2015.

Given the number of energy tax provisions, their general complexity and the ever-changing make-up of the energy industry, efforts at consolidation and reform may make sense in this area. To the extent any tax reform initiative addresses energy-related tax provisions, several guiding principles could be considered:

1. Provide stability to developing industries, by providing certainty to select temporary tax provisions;
2. Consolidate and simplify the energy-related tax expenditures;
3. Make such tax expenditures fairer and more efficient;
4. Encourage energy independence through a comprehensive approach;
5. Carefully consider whether and how to address any positive or negative externalities.

The following table provides a ranking of select energy tax expenditures, from highest to lowest cost:

Energy Provision	2014-18
Credits for electricity production from renewable resources (section 45):	15.7
Wind.....	13.8
Open-loop biomass.....	1.9
Excess of percentage over cost depletion, fuels:	8.7
Oil and gas.....	7.4
Expensing of exploration and development costs, fuels:	6.5
Oil and gas.....	6.0
Section 199	5.9
Exceptions for publicly traded partnership with qualified income derived from certain energy-related activities.....	5.8
Residential energy-efficient property credit.....	4.3
Energy investment tax credit (section 48).....	2.9
Solar.....	2.3
Depreciation recovery periods for electric distribution/transmission property.....	2.0
10-year MACRS for smart electric distribution property.....	1.0
15-year MACRS for certain electric transmission property.....	1.0
Amortization of air pollution control facilities.....	1.8
Five-year MACRS for certain energy property (solar, wind, etc.).....	1.4
Credit for plug-in electric vehicles.....	1.1
Special rule to implement electric transmission restructuring.....	1.0
Last In First Out Accounting.....	N/A

Joint Committee on Taxation

NOTE: Details shown for selected components only.

^[1] Reflects legislation enacted through June 30, 2014.

Note: The Joint Committee on Taxation has estimated the FY2015 Administration proposal to repeal the domestic production deduction for oil and natural gas activities would raise approximately \$5.9 billion over the 2014-2018 period.

Present Law: Energy Tax Expenditures

Nonbusiness energy property credits (sec. 25C)

A thirty percent credit is available through 2014 for certain (1) insulation, (2) energy efficient window, doors, skylights, and roofs, (3) advanced main air circulating fans, (4) natural gas, propane, or oil furnace or hot water boilers, (5) electric heat pump, natural gas, propane, or oil water heaters, (6) central air conditions, or (7) wood stoves. The maximum total credit is \$1,500.

Residential energy efficient property credits (sec. 25D)

A 30-percent credit is available through 2016 for residential (1) solar water heating or solar electric property, (2) small wind property, (3) geothermal heat pump property, and (4) fuel cell property placed in service.

Fuel cell vehicles (sec. 30B)

A credit is available through 2014 for vehicles propelled by chemically combining oxygen with hydrogen and creating electricity. The base credit is \$4,000 for vehicles weighing 8,500 pounds or less. Heavier vehicles can get up to a \$40,000 credit, depending on their weight. An additional \$1,000 to \$4,000 credit is available to cars and light trucks to the extent their fuel economy exceeds the 2002 base fuel economy set forth in the Code.

Credit for alternative fuel refueling property (sec. 30C)

A 30-percent credit is available through 2014 for property that dispenses alternative fuels, including ethanol, biodiesel, natural gas, hydrogen, and electricity. The credit may not exceed \$30,000 per location for business property and \$1,000 for property installed at a principal residence.

Plug-in electric-drive motor vehicles (sec. 30D)

A credit is available for four-wheeled vehicles (excluding low speed vehicles and vehicles weighing 14,000 or more) propelled by a battery with at least 4 kilowatt-hours of electricity that can be charged from an external source. The base credit is \$2,500 plus \$417 for each kilowatt-hour of additional battery capacity in excess of 4 kilowatt-hours (for a maximum credit of \$7,500). Each manufacturer is subject to a 200,000 vehicle cap.

Second generation biofuel credit (secs. 40, 6426, and 6427)

A \$1.01 credit is available through 2014 per gallon of second generation biofuel (cellulosic and algae) produced and sold or used as a fuel.

Agri-biodiesel and biodiesel (secs. 40A, 6426, and 6427)

A one dollar credit is available through 2014 per gallon of agri-biodiesel and biodiesel sold or used as a fuel, plus 10 cents per gallon for small producers of agri-biodiesel.

Renewable diesel (secs. 40A, 6426, and 6427)

A one dollar credit is available through 2014 per gallon of renewable diesel sold or used as a fuel or so sold or used as part of a qualified mixture.

Energy research credit (sec. 41(a)(3))

A 20-percent credit is available through 2014 for payments made to energy research consortia for qualified energy research (including research related to fossil fuels as well as to renewable energy technologies).

Credit for enhanced oil recovery (“EOR”) costs (sec. 43)

A 15-percent credit is available for expenses associated with an EOR project. An EOR project is generally a project that involves the use of one or more tertiary recovery methods to increase the amount of recoverable domestic crude oil. The credit is reduced as the price of oil exceeds a certain threshold and is currently phased-out.

Credit for electricity from certain renewable resources (sec. 45)

A production tax credit is available for electricity produced from certain renewable resources during the 10-year period beginning after the related renewable power facility has been placed in service. The credit rate for 2015 is 2.3 cents per kilowatt hour for power produced at wind, closed-loop biomass, and geothermal facilities, and 1.2 cents per kilowatt hour for power produced at open-loop biomass, small irrigation power, municipal solid waste, marine/hydrokinetic, and certain hydropower facilities. The construction of qualified facilities must have begun before December 31, 2014.

Indian coal production credit (sec. 45)

A \$2-per-ton credit (adjusted for inflation; \$2.317 for 2014) is available through 2014 for coal produced at facilities placed in service before 2009 that produce coal from reserves that on June 14, 2005 were owned by (or held in trust on behalf of) an Indian tribe.

Credit for producing oil and gas from marginal wells (sec. 45I)

A production credit is available for crude oil or natural gas produced from marginal wells or wells that have an average daily production of not more than 25 barrel-of-oil equivalents per day. The credit rate (adjusted for inflation from 2004) is \$3 per barrel of oil or 50 cents per 1,000 cubic feet of natural gas. The credit is currently phased out.

Credit for production of electricity from qualifying advanced nuclear power facilities (sec. 45J)

A production tax credit available for the production of nuclear power from new facilities that use modern designs and have received an allocation from the Secretary (who may allocate up 6,000 megawatts of credit-eligible capacity). The credit rate is 1.8 cents per kilowatt-hour for

the eight year period starting when the facility was placed in service. Qualified facilities must be placed in service by December 31, 2020.

New energy efficient home credit (sec. 45L)

A credit is available through 2014 for homes placed in service that exceed certain efficiency standards. The credit is \$1,000 for homes that exceed the standard by thirty percent and \$2,000 for homes that exceed the standard by fifty percent.

Credit for costs incurred in training qualified mine rescue team employees (sec. 45N)

Through 2014, an eligible employer may claim a general business credit against income tax with respect to each qualified mine rescue team employee equal to the lesser of: (1) 20 percent of the amount paid or incurred by the taxpayer during the taxable year with respect to the training program costs of the qualified mine rescue team employee; or (2) \$10,000.

Carbon dioxide sequestration credit (sec. 45Q)

A credit is available for the sequestration of industrial source carbon dioxide produced at qualified U.S. facilities. Qualified facilities must capture at least 500,000 metric tons of CO₂ per year. The credit rate is \$10 per ton for carbon dioxide used as a tertiary injectant and then permanently sequestered and \$20 per ton for carbon dioxide permanently sequestered without being first used as tertiary injectant. The credit expires at the end of the year in which the Secretary determines that 75 million tons of carbon dioxide have been captured and sequestered.

Investment tax credit energy production incentives (sec. 48)

A ten percent investment credit is available for equipment placed in service that produces, uses, or distributes energy from geothermal deposit. A ten percent credit is also available through 2016 for geothermal heat pump, microturbine, and combined heat and power property placed in service. A thirty percent investment credit is available through 2016 for solar electric/solar hot water (drops to 10 percent after 2016), fuel cell, and small wind property.

Credit to holders of clean renewable energy bonds (sec. 54C)

Gives a tax credit for holders of clean renewable energy bonds in lieu of interest. New CREBs may be issued to finance “qualified renewable energy facilities.” Qualified renewable energy facilities are facilities that: (1) qualify for the tax credit under section 45 (other than Indian coal and refined coal production facilities). The credit rate is 70 percent of the rate that permits issuance of bonds without discount and interest cost to the issuer. Qualified issuers include electrical cooperatives, clean renewable energy bond lenders, public power providers, State and local governments (including Indian tribes), and not-for-profit electric utilities which have a loan or loan guarantee under the Rural Electrification Act. The program is volume limited (\$2.4. billion) all of which has been allocated by the Secretary of the Treasury.

Credit to holders of qualified energy conservation bonds (sec. 54D)

The provision gives a tax credit for holders of qualified energy conservation bonds in lieu of interest. Bond issuance must be used for “qualified conservation purposes.” The credit rate is 70 percent of the rate that permits issuance of bonds without discount and interest cost to the issuer. The program is volume limited (\$3.2 billion) and allocated by the Secretary of the Treasury generally in proportion to State population.

Exclusion of interest on State and local government bonds for energy production facilities (sec. 103)

The provision allows the issuance of tax-exempt governmental bonds for certain energy production facilities. The provision is not volume limited.

Exclusion of energy conservation subsidies provided by public utilities (sec. 136)

Energy conservation subsidies provided by public utilities are excluded from gross income.

Exclusion of interest on certain energy-related private activity bonds (secs. 141 and 142)

Tax-exempt qualified private activity bond may be used for financing certain exempt facilities including privately owned and/or operated utility facilities (local district heating and cooling facilities, certain private electric and gas facilities, and hydroelectric dam enhancements) as well as qualified green building and sustainable design projects. Such bond issuances are generally subject to a private activity volume cap.

Safe harbor from arbitrage rules for prepaid natural gas (sec. 148)

Tax-exempt bonds may be used to finance prepaid natural gas contracts without application of the otherwise applicable arbitrage rules.

Amortization of geological and geophysical expenditures associated with oil and gas exploration (sec. 167(h))

Geological and geophysical (G&G) expenditures incurred by independent producers and smaller integrated oil companies in connection with domestic oil and gas exploration may be amortized over 24 months. G&G expenditures incurred by major integrated oil companies are amortized over seven years.

Five-year MACRS for certain energy property (solar, wind, etc.) (sec. 168(e)(3)(B)(iv))

A five-year MACRS recovery period is generally provided for equipment using solar and wind energy to generate electricity, to heat or cool (or provide hot water for use in) a structure, or to provide solar process heat; equipment using solar energy to illuminate the inside of a structure using fiber-optic distributed sunlight; equipment used to produce, distribute, or use energy derived from a geothermal deposit; and qualified fuel cell property.

A five-year MACRS recovery period is provided for certain biomass property, including (i) a boiler, the primary fuel for which will be an alternate substance; (ii) a burner (including necessary on-site equipment to bring the alternate substance to the burner) for a combustor other than a boiler if the primary fuel for such burner will be an alternate substance; (iii) equipment for converting an alternate substance into a qualified fuel; and (iv) certain pollution control equipment.

Seven-year MACRS for natural gas gathering lines and Alaskan natural gas pipelines (sec. 168(e)(3)(C))

A seven-year MACRS recovery period and 14-year class life is provided for natural gas gathering pipelines placed in service after April 11, 2005 and for any Alaskan natural gas pipelines.

10-year MACRS for smart electric distribution property (sec. 168(e)(3)(D), (i)(18), and (19))

Provides a 10-year recovery period and 150 percent declining balance method for any qualified smart electric meter and any qualified smart electric grid system.

15-year MACRS for certain electric transmission property (sec. 168(e)(3)(E)(vii))

Provides a 15-year recovery period for property used in the transmission of electricity for sale at 69 kilovolts and above for which original use of the property begins with the taxpayer after April 11, 2005.

50-percent expensing of cellulosic biofuel plant property (sec. 168(l))

Provides an additional first-year depreciation deduction equal to 50 percent of the adjusted basis of qualified cellulosic biofuel plant property acquired by a taxpayer by purchase and placed in service by the taxpayer before January 1, 2014, provided original use begins with the taxpayer.

Amortization of air pollution control facilities (sec. 169 and 291)

A taxpayer may elect to recover the cost of any certified pollution control facility over a period of 60 months. A corporation taxpayer must reduce the amount of basis otherwise eligible for the 60-month recovery by 20 percent.

Deduction for energy efficient commercial building property (sec. 179D)

For property placed in service before 2015, a taxpayer may take an additional deduction of \$1.80 per square foot of commercial property that exceeds certain energy efficiency standards.

Partial expensing of investments in advance mine safety equipment (sec. 179E)

Taxpayers may elect to treat 50 percent of the cost of any qualified advanced mine safety equipment property as an expense for both regular tax and AMT purposes in the taxable year in which the equipment is placed in service.

Expensing of tertiary injectants (sec. 193)

Taxpayers engaged in petroleum extraction activities may generally deduct qualified tertiary injectant expenses used while applying a tertiary recovery method.

Full or partial expensing of exploration and development costs (secs. 263(c), 291, 616(a) and 617(a))

Oil and gas - Taxpayers may elect to currently deduct intangible drilling costs (IDCs) paid or incurred with respect to the development of an oil or gas property located in the United States. For an integrated oil company that has elected to expense IDCs, 30 percent of the IDCs on productive wells must be capitalized and amortized over a 60-month period.

Coal - Taxpayers generally may elect to deduct amounts paid or incurred during the tax year (a) in ascertaining the existence, location, extent, or quality of any deposit of ore, provided the amounts are paid or incurred prior to the beginning of the development stage of the mine (“exploration costs”), and (b) for the development of a mine or other natural deposit (other than an oil or gas well) if paid or incurred after the existence of ores or minerals in commercially marketable quantities has been disclosed (“development costs”). However, 30-percent of such amounts paid or incurred must be capitalized and amortized ratably over 60-months.

Deferral of gains from the sale of electric transmission property (sec. 451(i))

For sales occurring before 2015, a taxpayer may elect to recognize gain from ratably over an eight year period for gains on the disposition of certain electric transmission property.

Special rules for nuclear decommissioning costs and nuclear decommissioning reserve funds (sec. 468A)

Taxpayers may elect to claim a current tax deduction for contributions to a qualified nuclear decommissioning fund. Income earned by such a fund is taxed at a 20-percent rate.

Excess of percentage over cost depletion for oil, gas and other fuels (secs. 611 - 613A)

Depletion is available to any person having an economic interest in a producing oil and gas property. There are generally two types of depletion--cost and percentage depletion. Cost depletion is limited to the taxpayer’s basis in the property, whereas percentage depletion is not limited by the basis, but is subject to limitations based on net income derived from the property and taxable income. Percentage depletion for producing oil and gas property (15 percent rate) is available only to independent producers and royalty owners. Generally, an integrated oil company is a producer of crude oil that engages in the refining or retail sale of petroleum products in excess of certain threshold amounts.

Fossil fuel capital gains treatment (sec. 631(c))

In the case of the disposal of coal (including lignite) mined in the United States, held for more than one year prior to disposal, by the owner in a form under which the owner retains an economic interest in such coal, the excess of the amount realized from the sale over the adjusted depletable basis of the coal (plus certain disallowed deductions) is treated as the sale of property used in the owner's trade or business (i.e., the sale of section 1231 property). If the owner's net section 1231 gains, including royalties from eligible coal disposals, exceed its section 1231 losses, the royalties are treated as capital gains.

Alternative fuel and alternative fuel mixture credits (secs. 6426 and 6427)

For fuel sold before 2015, a 50-cent per gallon (or gasoline-gallon-equivalent for non-liquid fuels) credit is available for alternative fuels produced. Alternative fuels consist of liquefied petroleum gas, P Series Fuels, compressed or liquefied natural gas, liquefied hydrogen, any liquid fuel derived from coal through the Fischer-Tropsch process, compressed or liquefied gas derived from biomass, or liquid fuel derived from biomass. Alternative fuel mixtures are alternative fuels blended with gasoline, diesel, or kerosene.

Exceptions for publicly traded partnership with qualified income derived from certain energy-related activities (sec. 7704)

A publicly traded partnership is generally taxable as a C corporation. An exception is provided for partnerships for any taxable year in which 90 percent of the partnership's gross income consists of "qualifying income." Section 7704(d)(1)(E) provides that qualifying income includes, *inter alia*, income and gains derived from the exploration, development, mining or production, processing, refining, transportation (including pipelines transporting gas, oil, or products thereof), or the marketing of any mineral or natural resource (including fertilizer, geothermal energy, and timber), industrial source carbon dioxide, or the transportation or storage of certain fuels.

IV: PRESENT LAW RELATED TO COMMUNITY TAX INCENTIVES

The Code contains three tax credit provisions which were created to incentivize certain activity -- affordable rental housing in the case of the low-income housing tax credit, the rehabilitation or preservation of historic buildings in the case of the rehabilitation tax credit, and investments in projects in low-income communities in the case of the new markets tax credit. The present law description of each of these credits follows.

Low-income housing tax credit

In general

The low-income housing tax credit (“LIHTC”), created by the Tax Reform Act of 1986, may be claimed over a 10-year period for the cost of building rental housing occupied by tenants having incomes below specified levels.²⁴ Credits are often used to raise equity for the projects from corporate institutional investors, such as banks. The amount of the credit for any taxable year in the credit period is the applicable percentage of the qualified basis of each qualified low-income building. The applicable percentage is designed to produce a credit with a present value equal to a fixed percentage of the qualified basis of the building. Any building must meet all the requirements of a qualified low-income housing project for a 15-year compliance period.

Qualified low-income housing project

To qualify for the low-income housing tax credit, the incomes of the tenants must satisfy certain targeting rules. Under the LIHTC rules, a project is a qualified low-income housing project if 20 percent or more of the residential units in such project are both rent-restricted and occupied by individuals whose income is 50 percent or less of area median gross income (the “20-50 test”). Alternatively, a project is a qualified low-income housing project if 40 percent or more of the residential units in such project are both rent-restricted and occupied by individuals whose income is 60 percent or less of area median gross income (the “40-60 test”). The owner must elect to apply either the 20-50 test or the 40-60 test. A residential unit is rent-restricted if the gross rent with respect to such unit does not exceed 30 percent of income. Operators of qualified low-income housing projects must annually certify that such project meets the requirements for qualification, including meeting the 20-50 test or the 40-60 test. In practice, many projects have every unit satisfy the income targeting rules so that the entire project qualifies for the credit.

Allocation of credits

A low-income housing tax credit is allowable only if the owner of a qualified building receives a housing credit allocation from the State or local housing credit agency. Generally, the aggregate credit authority provided annually to each State for calendar year 2015 is \$2.30 per resident, with a minimum annual cap of \$2,680,000 for certain small population States.²⁵ These

²⁴ Sec. 42.

²⁵ Rev. Proc. 2014-61, 2014-47 I.R.B. 860 (November 17, 2014).

amounts are indexed for inflation. Projects that also receive financing with proceeds of tax-exempt bonds issued subject to the private activity bond volume limit do not require an allocation of the low-income housing credit, but the related use of tax-exempt bonds is subject to limitation.

Temporary minimum low-income housing tax credit applicable percentage

Under a temporary special rule, the applicable percentage for calculating the amount of credit is set at a minimum of 9 percent for newly constructed non-Federally subsidized buildings placed in service after July 30, 2008, and before January 1, 2015.

Tax expenditure estimate

The tax expenditure estimate for the low-income housing tax credit for fiscal years 2014-2018 is \$40.5 billion.

New markets tax credit

In general

A federal income tax credit is allowed in the aggregate amount of 39 percent of a taxpayer investment in a qualified community development entity (CDE).²⁶ In general, the credit is allowed to a taxpayer who makes a “qualified equity investment” in a CDE which further invests in a “qualified active low-income community business.” CDEs are required to make investments in low income communities (generally communities with 20 percent or greater poverty rate or median family income less than 80 percent of statewide median). The credit is allowed over seven years, five percent in each of the first three years and six percent in each of the next four years. The credit is recaptured if at any time during the seven-year period that begins on the date of the original issue of the investment the entity (1) ceases to be a qualified CDE, (2) the proceeds of the investment cease to be used as required, or (3) the equity investment is redeemed. Investments are allocated to CDEs annually and \$40 billion has been allocated since inception of the credit. The maximum annual amount of qualified equity investments was \$3.5 billion for calendar years 2010, 2011, 2012, 2013, and 2014. The new markets tax credit expired on December 31, 2014. No amount of unused allocation limitation may be carried to any calendar year after 2019.

Additional information related to the use of markets tax credit

The Department of Treasury’s Community Development Financial Institutions Fund (“CDFI”), which allocates the new markets tax credits (“NMTCs”) to CDEs, provides data for all projects (3,499 qualified active low-income community businesses, “QALICBs”) between fiscal year 2003 and 2011 broken down alphabetically by State and zip code.²⁷ The CDFI has prepared

²⁶ Section 45D was added by section 121(a) of the Community Renewal Tax Relief Act of 2000, Pub. L. No. 106-554.

²⁷ That information is available at: http://www.cdfifund.gov/news_events/CDFI-2013-32-CDFI_Fund_Releases_Public_Data_on_New_Markets_Tax_Credit_Investments.asp.

a short report on their dataset which includes some macro-level geographic breakdowns (metro/non-metro, levels of economic distress, etc).²⁸ According to the report, 45 percent of the total QALICBs were involved with the development or leasing of real estate, 53.3 percent of the total QALICBs were operating businesses, and 1.7 percent of the total QALICBs were the beneficiaries of loans or investments made by CDEs through other unrelated CDEs without allocations. The report also indicates that 85.3 percent of investments occurred in metropolitan areas, and 76.4 percent of investments occurred at least partly in a census tract that experienced at least one criteria of severe distress.

In addition, the NMTC Coalition, an advocacy organization, prepared a 2012 report providing NMTC project profiles in the 50 states and the District of Columbia²⁹. According to the report, “about 60 percent of NMTC investments have gone to real estate businesses, commercial and industrial facilities, retail space, and mixed-use facilities. Most often these investments are in the form of loans with below-market terms and conditions. Other NMTC investments include small business loan funds and financing for equipment upgrades.” The report notes that some of the projects include “a steel factory in Washington State, a library in Texas, a community center in New York, a family and children’s center in California, micro-loan programs in Oregon and Rhode Island, and a seafood processing plant in Alaska.”

Tax expenditure estimate

The tax expenditure estimate for the new markets tax credit for fiscal years 2014-2018 is \$5.2 billion.

Rehabilitation tax credit

In general

A version of the rehabilitation tax credit was first enacted in the Revenue Act of 1978,³⁰ and was modified to its current form by the Tax Reform Act of 1986.³¹

Present law provides a two-tier tax credit for rehabilitation expenditures.³²

A 20-percent credit is provided for qualified rehabilitation expenditures with respect to a certified historic structure. For this purpose, a certified historic structure means any building that is listed in the National Register, or that is located in a registered historic district and is certified

²⁸ That report is available at:

<http://www.cdfifund.gov/docs/nmtc/2014/FY%202012%20NMTC%20Data%20Release%20Narrative.pdf>.

²⁹ That report is available at: <http://nmtccoalition.org/wp-content/uploads/NMTC-At-Work-in-Communities-Across-America.pdf>. The NMTC Coalition also has an interactive map which contains these project profiles and other projects, available at: <http://nmtccoalition.org/map/>.

³⁰ Pub. L. No. 95-600.

³¹ Pub. L. No. 99-514.

³² Sec. 47.

by the Secretary of the Interior to the Secretary of the Treasury as being of historic significance to the district.

A 10-percent credit is provided for qualified rehabilitation expenditures with respect to a qualified rehabilitated building, which generally means a building that was first placed in service before 1936 (50 years before the modifications enacted in 1986). The pre-1936 building must meet requirements with respect to retention of existing external walls and internal structural framework of the building in order for expenditures with respect to it to qualify for the 10-percent credit. A building is treated as having met the substantial rehabilitation requirement under the 10-percent credit only if the rehabilitation expenditures during the 24-month period selected by the taxpayer and ending within the taxable year exceed the greater of (1) the adjusted basis of the building (and its structural components), or (2) \$5,000.

The provision requires the use of straight-line depreciation or the alternative depreciation system in order for rehabilitation expenditures to be treated as qualified under the provision.

Tax expenditure estimate

The tax expenditure estimate for the rehabilitation tax credit, both for historic structures and other than historic structures, for fiscal years 2014-2018 is \$5.4 billion.

V: PRESENT LAW RELATED TO INDIAN TRIBES AND TRIBAL MEMBERS

Background

Although Native Americans make up less than one percent of the U.S. population, they make up a much larger percentage of the population in States in the West, Southwest, Northern Plains and Alaska. Thirty percent of Native Americans live on reservations.³³

The figure on the next page shows the Native American population rate as a percentage of county population. This map further reinforces the fact that the Native American population is concentrated in the West, Northern Plains, Southwest, and Alaska.

According to 2010 U.S. Census data, the median income of a Native American household was \$35,062, compared to \$50,046 for the U.S. population as a whole.³⁴ Among those living on Indian reservations and eligible to work, 49 percent were unemployed in 2005; 29 percent were employed but had annual earnings below the poverty line. Overall, 27 percent of Native Americans lived in poverty in 2009, compared to 14 percent for the U.S. white population.³⁵

In regards to the tax code, Indian tribes generally are exempt from Federal income tax.³⁶ With limited exceptions, enrolled members of Indian tribes are subject to Federal income tax. Indian tribes have an inherent sovereign power to tax transactions that occur on certain Indian lands and that significantly involve the Indian tribe or its members.

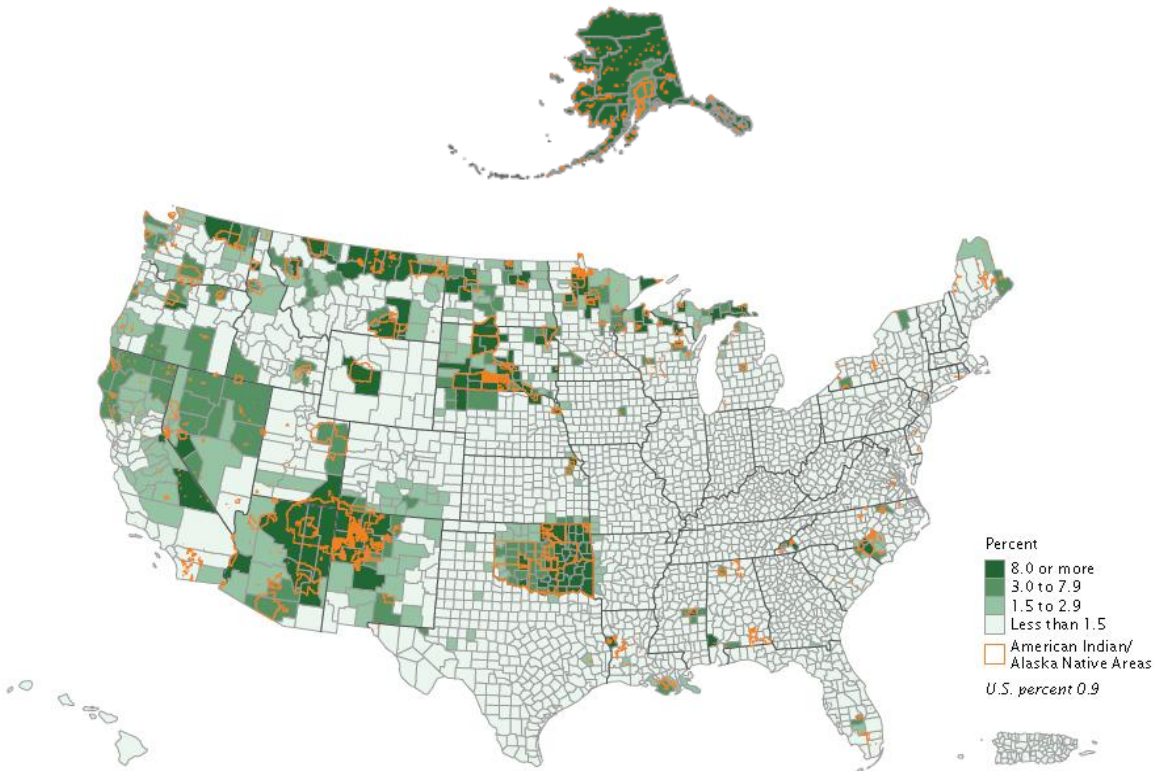
³³ Census Bureau (2012), *The American Indian and Alaska Native Populations by Selected Tribal Groupings: 2010*. Detailed Tables B02001 and B02010. For additional information, see Joint Committee on Taxation, *Overview of Federal Tax Provisions and Analysis of Selected Issues Relating to Native American Tribes and Their Members* (JCX-40-12), May 14, 2012.

³⁴ Census Bureau, *2010 American Community Survey Data*, Table S1903, “Median Income in the Past 12 Months (in 2010 Inflation-Adjusted Dollars),” available at http://factfinder.census.gov/faces/tableservices/jsf/pages/productview.xhtml?pid=ACS_10_1YR_S1903&prodType=table.

³⁵ Census Bureau (2012), *Selected Characteristics of Racial Groups and Hispanic/Latino Population: 2010*, Table 36.

³⁶ For additional information, see Joint Committee on Taxation, *Overview of Federal Tax Provisions and Analysis of Selected Issues Relating to Native American Tribes and Their Members* (JCX-40-12), May 14, 2012.

Native American Population as a Percentage of County Population in 2010



Source: Census Bureau, 2010 Census Redistricting Data (Public Law 94-171) Summary File, Table P1.

The Code contains certain provisions designed to encourage economic development on Indian reservations. Below are present law descriptions of three tax provisions which have all expired: (1) the Indian employment tax credit; (2) accelerated depreciation rules for property on Indian reservations; and (3) credit for the production for Indian coal.³⁷

Indian employment credit

In general, a credit against income tax liability is allowed to employers for the first \$20,000 of qualified wages and qualified employee health insurance costs paid or incurred by the

³⁷ There are other tax provisions in the Code that may also encourage economic development on Indian reservations. For example, the new markets tax credit contained in section 45D which provides a tax credit to taxpayers who invest in low-income communities has been found to benefit some tribal organizations. Urban Institute, *New Markets Tax Credit (NMTTC) Program Evaluation*, Final Report, April 2013, available at <http://www.taxpolicycenter.org/UploadedPDF/412958-new-markets-tax-final.pdf> (the Urban Institute surveyed projects from 2003-2007 and found that two percent of projects involved “tribal or other governmental organizations”).

employer with respect to certain employees.³⁸ The credit is equal to 20 percent of the excess of eligible employee qualified wages and health insurance costs during the current year over the amount of such wages and costs incurred by the employer during 1993. The credit is an incremental credit, such that an employer's current-year qualified wages and qualified employee health insurance costs (up to \$20,000 per employee) are eligible for the credit only to the extent that the sum of such costs exceeds the sum of comparable costs paid during 1993. No deduction is allowed for the portion of the wages equal to the amount of the credit.

Qualified wages means wages paid or incurred by an employer for services performed by a qualified employee. A qualified employee means any employee who is an enrolled member of an Indian tribe or the spouse of an enrolled member of an Indian tribe, who performs substantially all of the services within an Indian reservation, and whose principal place of abode while performing such services is on or near the reservation in which the services are performed. An "Indian reservation" is a reservation as defined in section 3(d) of the Indian Financing Act of 1974³⁹ or section 4(10) of the Indian Child Welfare Act of 1978.⁴⁰ For purposes of the preceding sentence, section 3(d) is applied by treating "former Indian reservations in Oklahoma" as including only lands that are (1) within the jurisdictional area of an Oklahoma Indian tribe as determined by the Secretary of the Interior, and (2) recognized by such Secretary as an area eligible for trust land status under 25 C.F.R. Part 151 (as in effect on August 5, 1997).

An employee is not treated as a qualified employee for any taxable year of the employer if the total amount of wages paid or incurred by the employer with respect to such employee during the taxable year exceeds an amount determined at an annual rate of \$30,000, as adjusted for inflation in the manner described (which is \$45,000 for 2013). In addition, an employee will not be treated as a qualified employee under certain specific circumstances, such as where the employee is related to the employer (in the case of an individual employer) or to one of the employer's shareholders, partners, or grantors. Similarly, an employee will not be treated as a qualified employee where the employee has more than a five percent ownership interest in the employer. Finally, an employee will not be considered a qualified employee to the extent the employee's services relate to gaming activities or are performed in a building housing such activities.

The wage credit is available for wages paid or incurred in taxable years that begin on or before December 31, 2014.

³⁸ Sec. 45A. This provision was enacted by the Omnibus Reconciliation Act of 1993, Pub. L. No. 103-66, sec. 13322(b). The provision originally applied to wages paid or incurred after December 31, 1993 and applied to taxable years beginning before January 1, 2014. However, the provision was extended to apply to taxable years beginning before January 1, 2005, 2006, 2008, 2010, 2012, 2013, and 2014 as follows: Pub. L. No. 107-147, sec. 613(a); Pub. L. No. 108-311, sec. 315; Pub. L. No. 109-432, sec. 111(a); Pub. L. No. 110-343, Division C, sec. 314(a); Pub. L. No. 111-312, sec. 732(a); Pub. L. No. 112-240, sec. 304(a); and Pub. L. No. 113-295, Division A, sec. 114(a).

³⁹ Pub. L. No. 93-262.

⁴⁰ Pub. L. No. 95-608.

Tax expenditure estimate

The tax expenditure estimate for the Indian employment credit for fiscal years 2014-2018 is \$.1 billion.

Accelerated depreciation for business property on Indian reservations

With respect to certain property used in connection with the conduct of a trade or business within an Indian reservation and placed in service prior to January 1, 2015, depreciation deductions under section 168(j)⁴¹ are determined using the following recovery periods:

Table 1.—Comparison of Applicable Recovery Periods

MACRS	Indian Reservation Property
3-year property	2 years
5-year property	3 years
7-year property	4 years
10-year property	6 years
15-year property	9 years
20-year property	12 years
Residential real property (27.5 years)	27.5 years (same)
Nonresidential real property (39 years)	22 years

“Qualified Indian reservation property” eligible for accelerated depreciation includes property described in the table above which is: (1) used by the taxpayer predominantly in the active conduct of a trade or business within an Indian reservation; (2) not used or located outside the reservation on a regular basis; (3) not acquired (directly or indirectly) by the taxpayer from a person who is related to the taxpayer;⁴² and (4) not property placed in service for purposes of conducting gaming activities.⁴³ Certain “qualified infrastructure property” may be eligible for

⁴¹ This provision was enacted by the Omnibus Reconciliation Act of 1993, Pub. L. No. 103-66, sec. 13321(a). The provision originally applied to property placed in service on or after January 1, 1994 and before January 1, 2004, but was extended to property placed in service before 2005, 2006, 2008, 2010, 2012, 2013, and 2014 as follows: Pub. L. No. 107-147, sec. 613(b); Pub. L. No. 108-311, sec. 316; Pub. L. No. 109-432, Division A, sec. 112(a); Pub. L. No. 110-343, Division C, sec. 315(a); Pub. L. No. 111-312, sec. 739(a); Pub. L. No. 112-240, sec. 313(a); and Pub. L. No. 113-295, Division A, sec. 124(a). The Taxpayer Relief Act of 1997, Pub. L. No. 105-34, sec. 1604(c)(2), clarified the definition of “Indian reservation” as pertaining to the State of Oklahoma, effective as if included in the Omnibus Reconciliation Act of 1993.

⁴² For these purposes, related persons is defined in section 465(b)(3)(C).

⁴³ Sec. 168(j)(4)(A).

the accelerated depreciation even if located outside an Indian reservation, provided that the purpose of such property is to connect with qualified infrastructure property located within the reservation (e.g., roads, power lines, water systems, railroad spurs, and communications facilities).⁴⁴

An “Indian reservation” means a reservation as defined in section 3(d) of the Indian Financing Act of 1974 or section 4(10) of the Indian Child Welfare Act of 1978.⁴⁵ For purposes of the preceding sentence, section 3(d) is applied by treating “former Indian reservations in Oklahoma” as including only lands that are (1) within the jurisdictional area of an Oklahoma Indian tribe as determined by the Secretary of the Interior, and (2) recognized by such Secretary as an area eligible for trust land status under 25 C.F.R. Part 151 (as in effect on August 5, 1997).

The depreciation deduction allowed for regular tax purposes is also allowed for purposes of the alternative minimum tax.

Tax expenditure estimate

The tax expenditure estimate for accelerated depreciation for business property on Indian reservations for fiscal years 2014-2018 is not available.

Credit for the production of Indian coal

A credit is available for the production of Indian coal sold to an unrelated third party from a qualified facility for a seven-year period beginning January 1, 2006, and ending December 31, 2014.⁴⁶ The amount of the credit for Indian coal is \$1.50 per ton for the first four years of the seven-year period and \$2.00 per ton for the last three years of the seven-year period. Beginning in calendar years after 2006, the credit amounts are indexed annually for inflation using 2005 as the base year. The credit amount for 2014 is \$2.317 per ton.

A qualified Indian coal facility is a facility placed in service before January 1, 2009, that produces coal from reserves that on June 14, 2005, were owned by a Federally recognized Indian tribe or were held in trust by the United States for an Indian tribe or its members.

The credit is a component of the general business credit,⁴⁷ allowing excess credits to be carried back one year and forward up to 20 years. The credit is also subject to the alternative minimum tax.

⁴⁴ Sec. 168(j)(4)(C).

⁴⁵ Sec. 168(j)(6).

⁴⁶ The Indian coal provisions (secs. 45(c)(9), 45(d)(10), and 45(e)(10)) were enacted by the Energy Policy Act of 2005, Pub. L. No. 109-58, Title XIII (Energy Tax Incentives Act of 2005), sec. 1301(d)(1).

⁴⁷ Sec. 38(b)(8).

Tax expenditure estimate

The tax expenditure estimate for the credit for the production of Indian coal for fiscal years 2014-2018 is \$.1 billion.