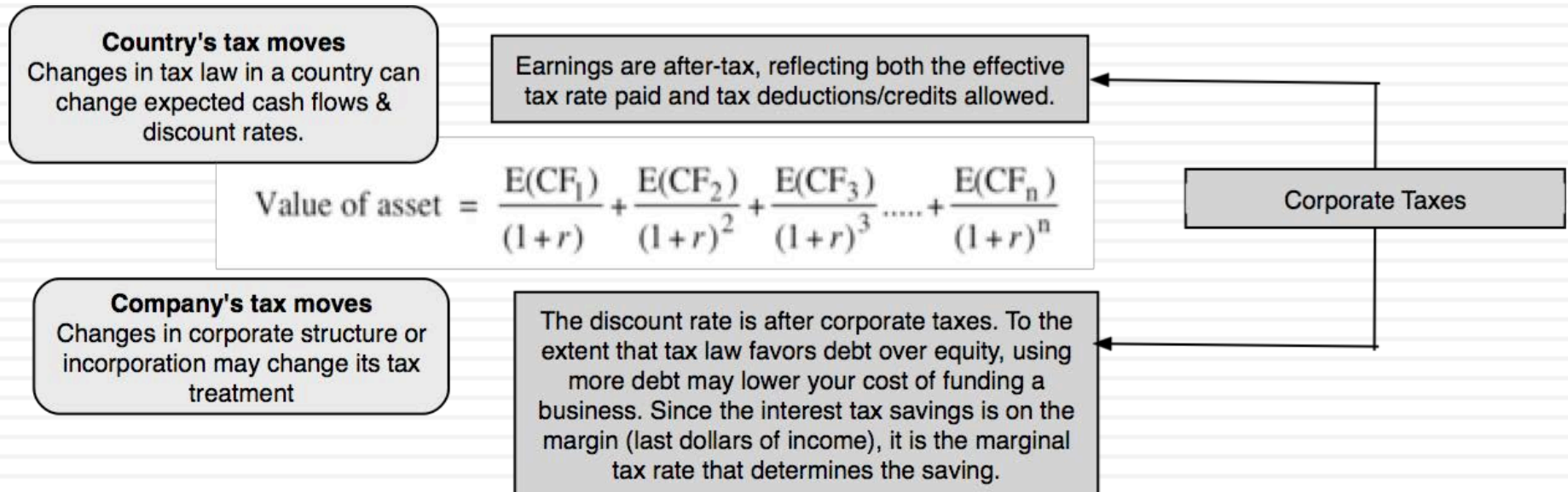




DATA 2017 UPDATE 5: A TAXING YEAR AHEAD?

Aswath Damodaran

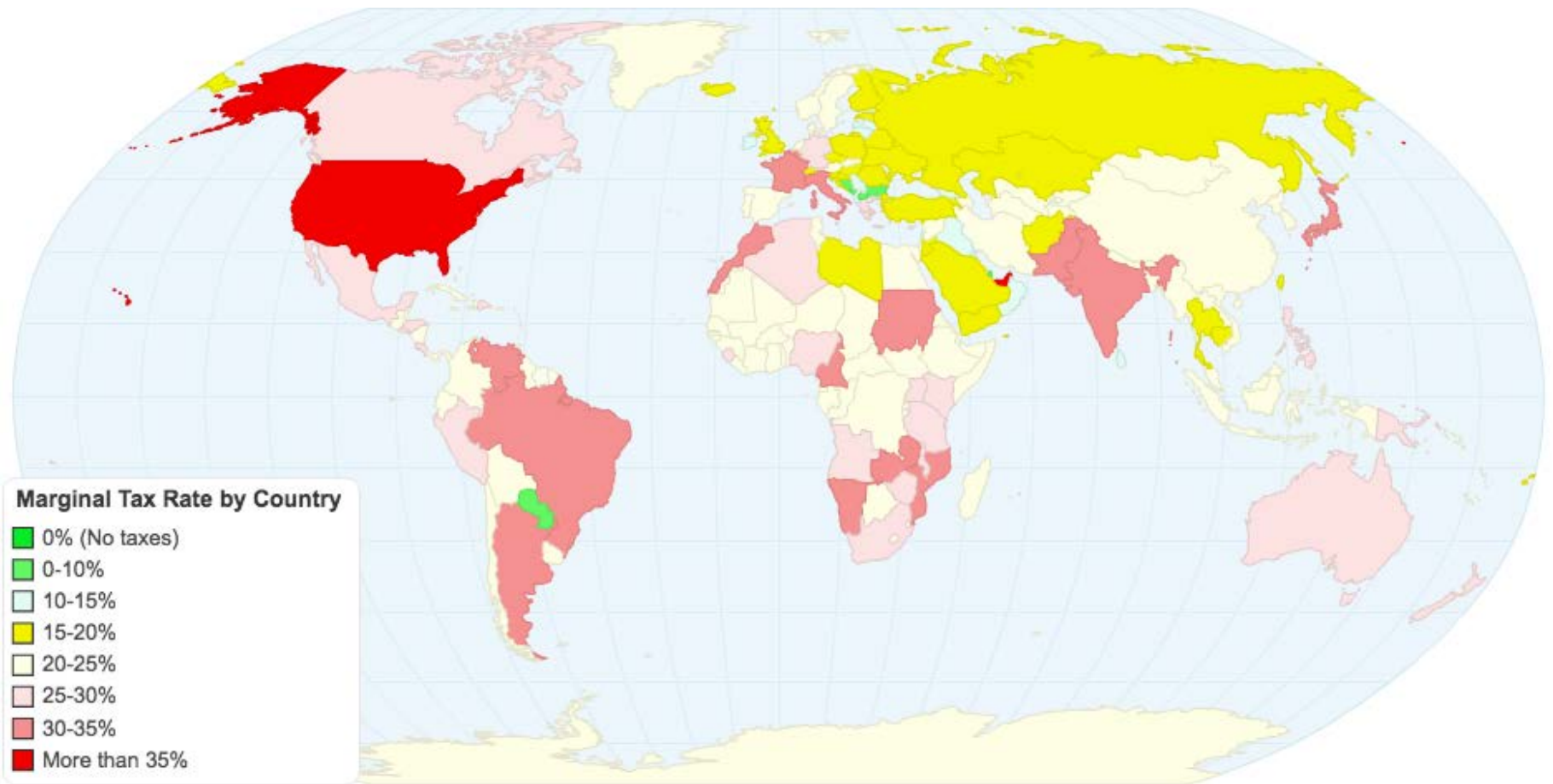
The Tax Effect on Value



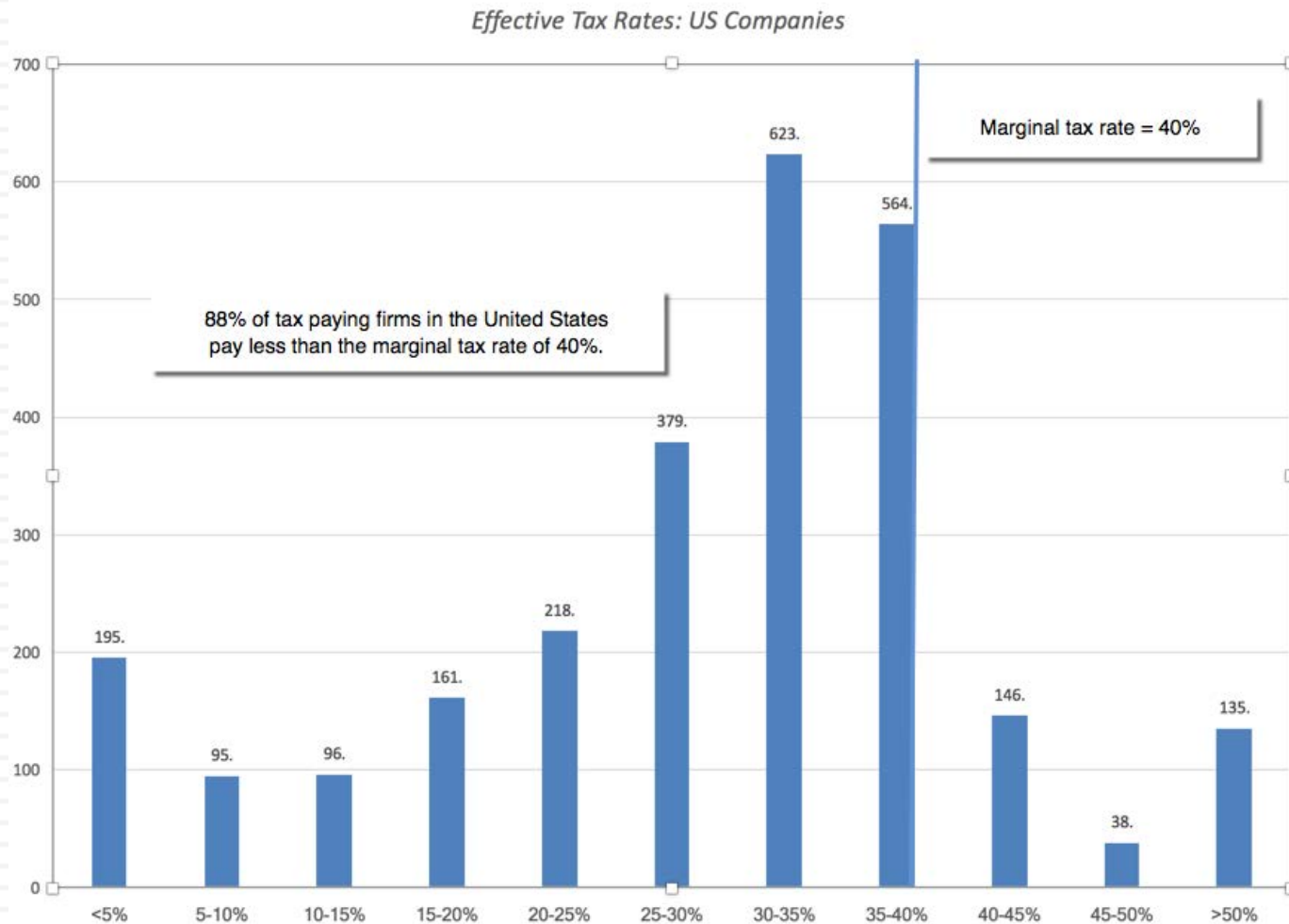
Tax Rate Specifics

Tax Rate Measure	Computed as	Used in
Marginal Tax Rate	The tax rate on your last dollars of income, usually obtained from the tax code (not the company financials)	Computing after-tax cost of debt and levered beta, in computing the tax savings from interest expenses
Effective Tax Rate	Taxes from Income Statement/ Taxable Income from Income Statement; it is an accrual number, reported in financials	Computing after-tax earnings as a starting point to get to taxes. Difference between accrual and cash taxes shows up as a working capital change.
Cash Tax Rate	Cash Taxes Paid/ Taxable Income. Usually requires calculation.	Not used.

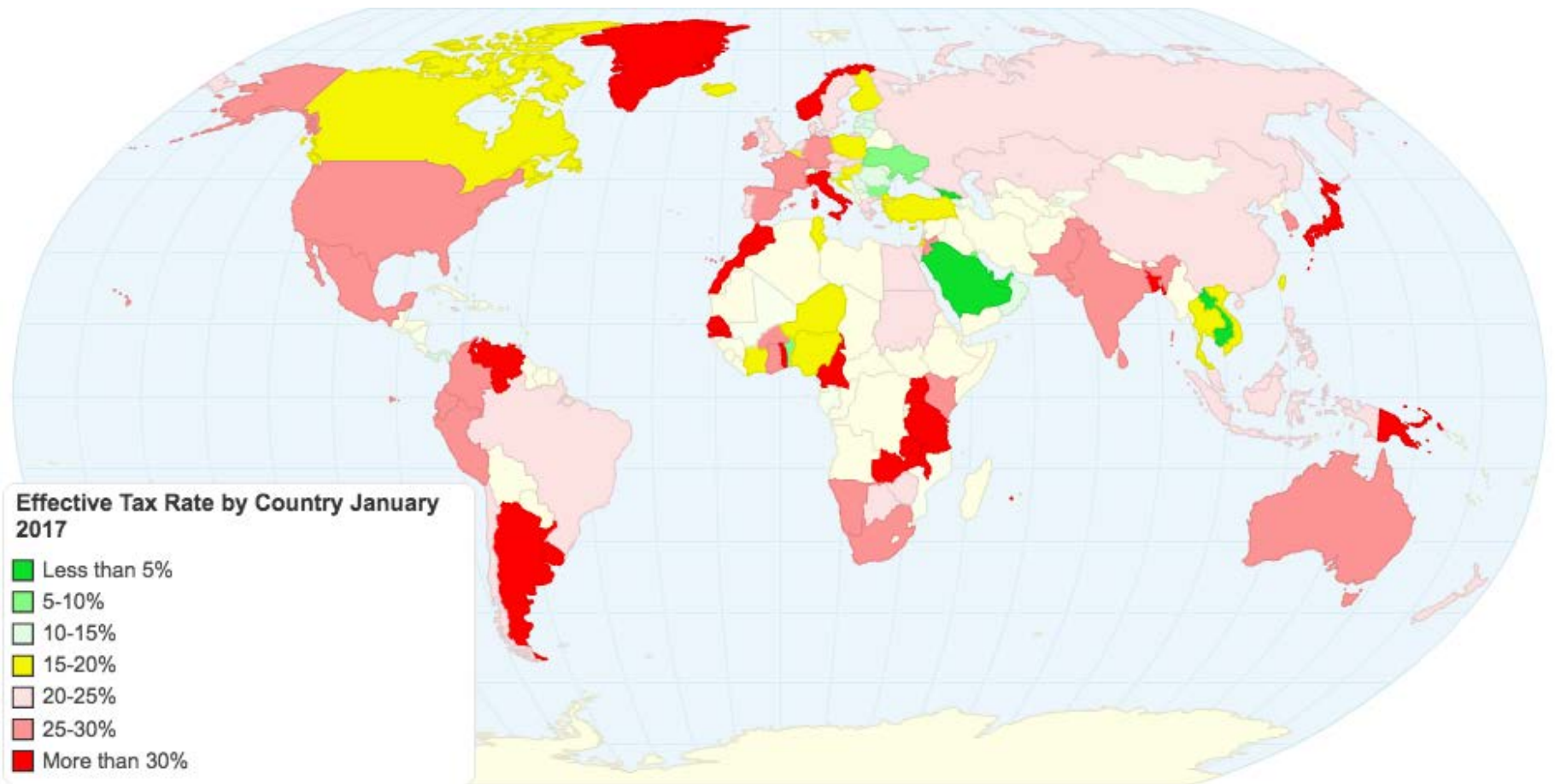
The Marginal Tax Rate



Effective Tax Rate Distribution: US companies



The Effective Tax Rate by Country



Paying their fair share?

<i>Sub Group</i>	<i>Effective Tax Rate</i>
Africa and Middle East	15.48%
Australia & NZ	26.76%
Canada	19.68%
China	21.72%
EU & Environs	23.03%
Eastern Europe & Russia	19.88%
India	27.65%
Japan	31.07%
Latin America & Caribbean	22.91%
Small Asia	21.59%
UK	22.26%
United States	26.22%

Effective Tax Rate by Industry Group

<i>Lowest tax-paying Industries</i>			<i>Highest tax-paying Industries</i>		
<i>Industry Name</i>	<i>Average Effective Tax Rate (Money Makers)</i>	<i>Aggregate Effective Tax Rate</i>	<i>Industry Name</i>	<i>Average Effective Tax Rate (Money Makers)</i>	<i>Aggregate Effective Tax Rate</i>
Coal & Related Energy	0.69%	NA	Business & Consumer Services	35.45%	38.64%
R.E.I.T.	2.16%	NA	Environmental & Waste Services	35.55%	36.03%
Software (Entertainment)	6.79%	NA	Retail (Automotive)	35.73%	35.77%
Oil/Gas (Production and Exploration)	7.08%	NA	Transportation (Railroads)	35.87%	35.87%
Oil/Gas Distribution	7.78%	3.44%	Shipbuilding & Marine	36.76%	NA
Oil/Gas (Integrated)	8.01%	NA	Cable TV	37.20%	20.65%
Chemical (Diversified)	11.56%	11.33%	Trucking	37.49%	37.28%
Hotel/Gaming	12.10%	15.99%	Telecom (Wireless)	37.72%	NA
Paper/Forest Products	12.58%	6.48%	Healthcare Support Services	38.15%	38.27%
Auto & Truck	12.66%	9.10%	Retail (Building Supply)	38.63%	39.21%

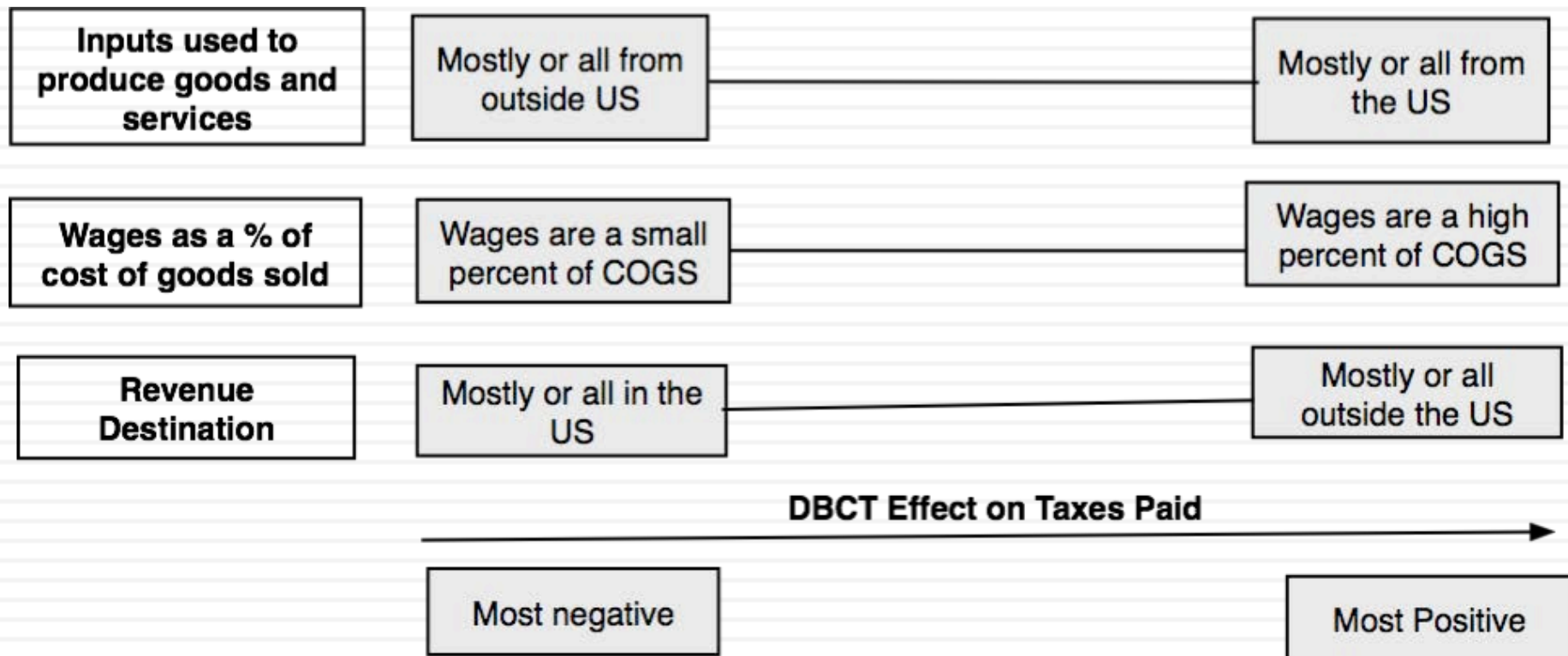
Tax Law Changes? Existing System tweaks

- Tweaks to existing tax system: The marginal tax rate is lowered, with some tax deductions/credits taken away and changes to how foreign income gets taxed (a partial move to a regional tax system).
- Winners and Losers
 - Winners: Companies that pay high effective tax rates and use little debt.
 - Losers: Companies that pay low effective tax rates, using deductions that will be lost, and use lots of debt in funding operations.

Tax Law Changes: Radical Alterations?

- Replace the current corporate income tax with a "Destination Based Cash-flow Tax" (DBCT), a value added tax system, with a deduction for wages. The tax rate that you pay as a company will be a function of how much of your input you import and where you sell your output.
- Winners and Losers
 - Winners: Companies with products and services that are entirely US-based that then export these goods and services.
 - Losers: Companies that are heavily reliant on imported inputs that sell their products in the United States would pay the most in taxes..

The DBCT Effect on taxes at a US firm



Advice for the tax law writers

- Keep it simple: When tax law gets complex, bad corporate behavior seems to follow. Unfortunately, the way legislative processes work seems to conspire against simplicity, as legislators trying to protect specific industries try to make sure that their ox does not get gored.
- The tax code is not an effective behavior modifier for businesses: I understand the desire of some to use tax law as a corporate behavior modification tool but it is not a very effective one.
- Make it predictable: There are enough uncertainties for a company to deal with. Adding uncertainty about future taxes only makes it worse.