EXECUTIVE SUMMARY

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Revised May 27, 2005

Corporate Tax Dodge:

The Decline of the Oregon Corporate Income Tax and the Shift to Individual Taxpayers

by Michael Leachman

Oregon's state corporate income tax has dropped to very low levels, both as a share of the economy and as a share of all income taxes paid in Oregon.

- In the upcoming budget cycle, corporations operating in Oregon will pay 71 percent less in state corporate income taxes as a share of the economy than they did in the late 1970s.
- In the 1973-75 budget cycle, corporations paid 18.5 percent of all income taxes. In the upcoming 2005-07 budget cycle, corporations are expected to pay just 4.6 percent of Oregon's income taxes. By 2009-11, corporations are expected to pay just 4.4 percent of Oregon income taxes.
- If corporate income taxpayers still paid the same share of income taxes they paid in 1973-75, state revenue for the upcoming budget cycle would be $1.8 billion higher than is now expected.
- Because corporate taxpayers have not sustained the 18.5 percent share of income taxes they paid in 1973-75, Oregon has lost a total of $10.9 billion since that time. By 2009-11, the figure will reach $15.2 billion.
- Over the current decade, as corporate income taxes fall by $192 million, personal income tax revenues are projected to grow another $4 billion.

The long-term decline in corporate income taxes is primarily because corporations have won a number of tax breaks, and because corporations have grown aggressive about employing abusive tax shelters that lawmakers never enacted or intended to allow.

- Of the 49 income tax breaks Oregon specially offers corporations, 40 were created since 1980.
- A tax break for companies with few Oregon sales but significant property and payroll in Oregon will cost Oregon $73 million in the upcoming budget period and keep Oregon corporate income tax collections flat for the rest of this decade.
- Corporate use of abusive tax shelters has exploded. A study by the Multistate Tax Commission estimated the impact on Oregon at between $66 million and $94 million for fiscal year 2001 alone.

Multistate corporations enjoy the lion's share of potentially taxable profits collected in Oregon and hence are the primary beneficiaries of the declining corporate income tax. As the tax burden has shifted from corporations to individual taxpayers, low-income taxpayers have been the hardest hit with increases.

Neither the growth in "pass-through" businesses nor the growth in fees is responsible for the decline in corporate taxes.

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Oregonians who winced as they wrote checks to state and local governments on tax day last month may have wondered why their tax payments are inadequate to produce quality schools and universities, safe neighborhoods, and effective family support programs. One key reason is that, over the last generation, Oregon has shifted more of the costs of public investments to households and away from large multistate corporations.

Oregon's state corporate income tax has dropped to very low levels, both as a share of the economy and as a share of all income taxes paid in Oregon.

The long-term decline in corporate income taxes is primarily because corporations have won a number of tax breaks, and because corporations have grown aggressive about employing abusive tax shelters that lawmakers never enacted or intended to allow.

The decline is not due to a slide in corporate profits. As a share of the economy, pre-tax corporate profits nationally were 8.7 percent of Gross Domestic Product during the 1970s, and 9.2 percent in 2001-04. Last year, the figure reached 10.1 percent.

The main beneficiaries of the corporate income tax's decline are large multistate companies, who collect most of the profit earned by companies operating in Oregon. Among the losers are personal income taxpayers in Oregon, including small businesses and families, who must either pick up the slack from declining corporate income tax revenues or endure reductions in funding for public services benefiting the common good. Oregon's lowest income families have been hardest hit. Unlike other Oregon households, these families have seen their taxes increase as a share of income since 1989, while also being hit hard by cuts to public services.

Some have argued that corporate income tax reductions are a good thing because they improve Oregon's business climate. But corporations operating in Oregon depend critically on investments of public funds in schools and universities, roads, health care coverage, worker training, parks, and the court system. In the long run, tax cuts that endanger the state's ability to fund these services will make Oregon a less attractive location for big multistate corporations and, just as importantly, will make Oregon a less attractive place for individuals and small business owners to live and work.

Lower corporate taxes do not equal economic growth

Corporate lobbyists often claim that lowering state corporate income taxes will produce more economic growth because companies will have more money to invest. This belief is at best too simple and at worst simply wrong.

State and local taxes are a small part of the costs to businesses, and therefore have little effect on investment decisions. State and local taxes nationally account for only about 0.8 percent of business costs.[1]

When making investment location decisions, businesses are much more concerned about the proximity of their markets and suppliers, as well as the quality and cost of labor, utilities, and transportation and communication infrastructures. Quality public investments in these areas improve the business climate and save companies money in the long run. If lowering corporate income taxes results in reductions in the quality or quantity of public investments, the impact of lower taxes may be slower economic growth, not stronger. An analysis of the existing research literature on this topic found "little grounds to support tax cuts and incentives – especially when they occur at the expense of public investment – as the best means to expand employment and spur growth."[2]

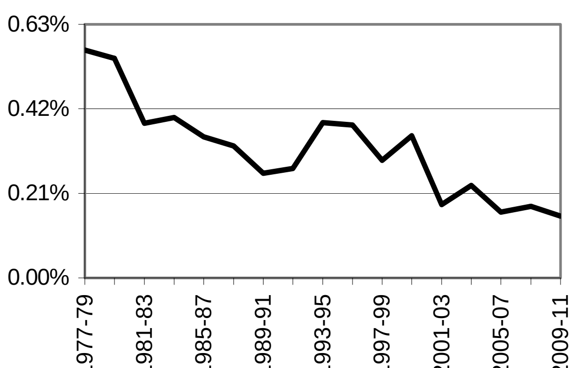
Corporate income taxes decline sharply as a share of the Oregon economy

Corporate income taxes have declined sharply over the last generation as a share of Oregon's economy. In the upcoming budget cycle, corporations operating in Oregon will pay 71 percent less in state corporate income taxes as a share of the economy than they did in the late 1970s.

In 1977-79, the first years with data available for Oregon, corporate income tax revenues equaled 0.57 percent of Gross State Product (GSP). Just two budget cycles later, in 1981-83, back-to-back recessions had pushed corporate income tax revenue down to just 0.38 percent of GSP (Figure 1).

Corporate income tax revenues have fallen from 0.57 percent of Gross State Product in 1977-79 to a projected 0.16 percent of GSP in 2005-07, a decline of 71 percent.

Figure 1: Oregon corporate income tax revenues as percent of Gross State Product



Source: Oregon Center for Public Policy analysis of Legislative Revenue Office data and May Economic and Revenue Forecast.
Note: OCPP estimated GSP for 03-05 and beyond at 13.4 percent growth, the average biennial growth from 1977-79 to 2001-03.

Even after the boom years of the 1990s, corporate income tax revenues remained at these lower levels. In 1999-01, at the peak of the economic expansion, corporate income tax revenue was just 0.35 percent of gross state product. Then, when the economic downturn hit in 2001, corporate income tax revenues collapsed nearly in half as a share of the economy, reaching a new low for the last generation at 0.18 percent of GSP (Figure 1).

Analysis of projected corporate income tax revenues shows that six years of economic growth will not reverse the trend. Assuming that the economy grows over the next several budget cycles at its average rate of growth for the 13 budget cycles starting in 1977-79, forecasted corporate income tax revenues will equal just 0.15 percent of Gross State Product by the end of this decade (Figure 1).[3] By 2009-11, corporate income tax revenues relative to the economy will have dropped 73 percent, compared to 1977-79.

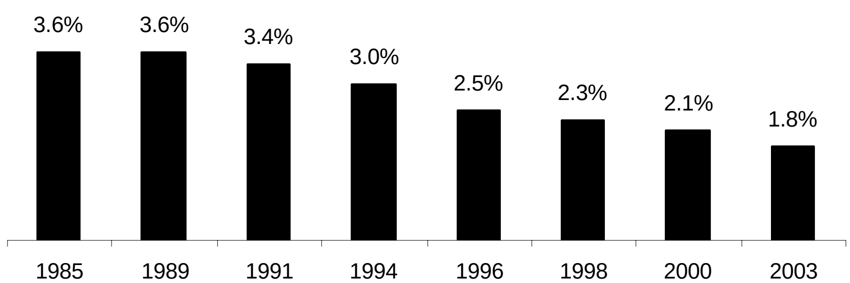
Including other types of corporate taxes does not change the picture

The decline in corporate income taxes in Oregon is indicative of a general decline in business taxes.

As a share of the economy, total business taxes in Oregon have been cut in half since 1985, according to a study by the Utah State Tax Commission.[4] In 1985, businesses in Oregon paid 3.6 percent of Gross State Product in taxes, including property taxes, unemployment insurance taxes, income taxes, tourist taxes, estate taxes, severance taxes, and excise taxes. By 2003, these taxes paid by Oregon businesses totaled just 1.8 percent of GSP (Figure 2).

OCPP's analysis of the Utah study's findings indicate that if in 2003 Oregon businesses still paid taxes at 1985 levels, they would have paid about $2.5 billion more in taxes than they did, in 2003 alone.

Figure 2: Total taxes on Oregon businesses as percent of Gross State Product



Source: Utah State Tax Commission

As a share of the economy, *total* business taxes in Oregon have been cut in half since 1985, according to a study by the Utah State Tax Commission.

Oregon business taxes among lowest in the nation

The Utah State Tax Commission's study mentioned above found that Oregon has the lowest business taxes as a share of Gross State Product of the seven Western states examined.[5]

A study written by the accounting firm Ernst & Young and published by the Council on State Taxation (COST) found that in 2004 the effective state and local tax rate on businesses in Oregon ranked 47th in the nation. As a share of all state and local taxes, business taxes in Oregon ranked 50th among the states and the District of Columbia.[6] COST is an association of over 500 multistate corporations that works to influence state tax policies. It is an outgrowth of and is still associated with the Council of State Chambers of Commerce.

This sharp decline in corporate tax revenues is also evident when total personal income is used as a measure of Oregon's economy. As a percentage of personal income, corporate tax revenues have fallen from 0.7 percent in 1977-79 to 0.4 percent in 1999-01, the peak of the economic expansion. In 2009-01, corporate tax revenues will be only 0.2 percent of projected personal income.

The decline of the corporate income tax in Oregon mirrors declines in other states. A study by Citizens for Tax Justice and the Institute on Taxation and

Economic Policy of the 252 Fortune 500 companies that report state-level corporate income tax liabilities found that between 2002 and 2004, corporations on average paid 38 percent less in state income taxes as a share of Gross Domestic Product than they paid between 1978 and 1989.[7] The study also found that if the 252 large corporations had paid the average state corporate income tax rate (6.8 percent) on all the U.S. profits they reported to shareholders in the 2001-03 period, they would have paid $67.1 billion in state income taxes. Instead, these companies paid just $25.4 billion. That is, the total amount in taxes these companies paid over the three years is $41.7 billion less than if they had paid the average state corporate income tax rate on all U.S. profits.[8]

Corporate income taxes decline as a share of all income taxes

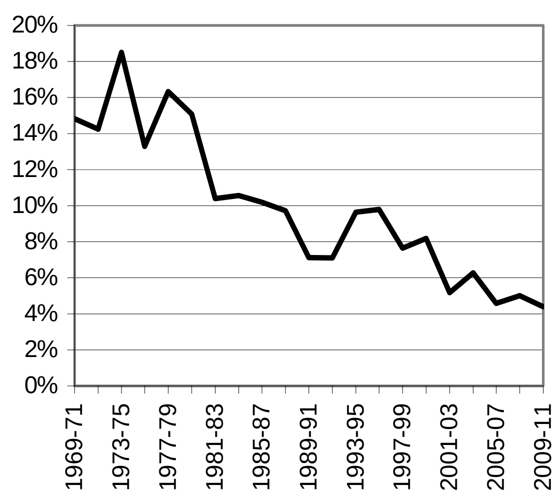
As a result of the corporate income tax's diminishing yield as a share of the economy, a bigger share of the state's income tax burden is being shouldered by working families and small businesses.

Oregon's state economist projects that corporations operating in Oregon will pay about $487 million in income taxes in the upcoming 2005-07 budget cycle. Personal income taxpayers, by contrast, will pay $10.1 billion.[9] In other words, corporations are expected to pay just 4.6 percent of Oregon's income taxes, while personal income taxpayers will pay 95.4 percent.

Individual Oregonians did not always pay such a disproportionate share of Oregon income taxes. In the 1970s, the share of income taxes paid by corporations hovered around 15 percent. In the 1973-75 budget cycle, corporations paid 18.5 percent of all income taxes (Figure 3).

In the upcoming 2005-07 budget cycle, corporations are expected to pay just 4.6 percent of Oregon's income taxes. In 2009-11, the figure is projected to be 4.4 percent.

Figure 3: Corporate income tax as a percent of all Oregon income taxes collected



Source: Oregon Center for Public Policy analysis of data from Legislative Revenue Office; Office of Economic Analysis, May Economic & Revenue Forecast.

The shift in income taxes away from corporations is driven primarily by corporate tax cuts and tax sheltering. It has occurred even though corporate profit growth nationally has kept pace with personal income growth (see *Corporate profits rising as fast as personal income,* on page 8). It is not driven primarily by the rise of "pass through" entities such as S-corporations and "limited liability companies' (see *Rise in "pass-through" companies is not driving the decline*, on page 18).

Corporations will continue to pay a decreasing share of Oregon income taxes into the foreseeable future. Oregon's state economist projects corporate income tax revenues will not recover from the recent economic downturn, which began in 2001, until some time after 2009-11. In 1999-01, before the downturn hit, corporate income taxes totaled $778 million. By 2009-11, the state economist projects them to be at $587 million, a decline of $192 million from before the economic downturn (Table 1). The projections indicate that corporations operating in Oregon in 2009-11 will pay less in aggregate corporate income taxes than they are expected to pay in the current 2003-05 biennium, even though the state economist predicts continued economic growth over the next several years.

The primary reason corporate income taxes will remain so low through the current decade is Oregon's phase-in of a major tax break aimed at reducing corporate income taxes for multistate companies with large amounts of property and payroll in Oregon, but few in-state sales, such as Intel and Nike. The tax break involves a change in the formula multistate corporations use to determine their corporate income tax bill in Oregon (see *Single-sales factor: the silent robber baron,* on page 10.)

Over the current decade, as corporate income taxes fall by $192 million, personal income tax revenues are projected to grow another $4 billion.

Table 1: Changes in Oregon income tax revenues, including projections, various periods

Projected change from:	Personal income tax revenues (millions)	Corporate income tax revenues (millions)
1999-01 to 2009-11	+$4,038	-$192
2003-05 to 2009-11	+$3,781	-$16

Source: OCPP analysis of data from Legislative Revenue Office and data from May Economic & Revenue Forecast.

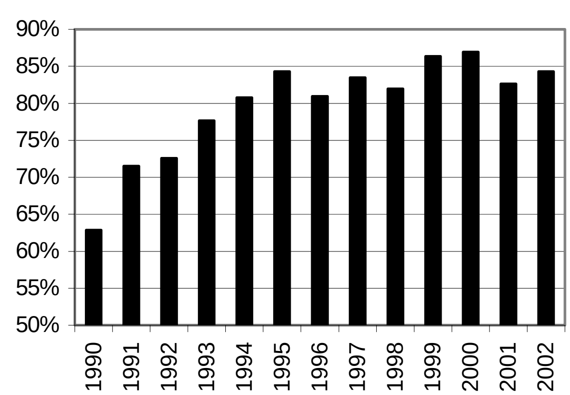
With corporate income taxes declining, personal income taxpayers end up paying for a disproportionate share of the cost of government. Over the current decade, as corporate income taxes fall by $192 million, personal income tax revenues are projected to grow another $4 billion (Table 1). As a result, corporate income taxes are projected to fall from 8.2 percent of all income tax revenue at the beginning of the decade to just 4.4 percent by 2009-11.

Large corporations operating beyond Oregon are the primary beneficiaries

In 2002, multistate firms collected 84 percent of all taxable profits reported in Oregon, up from 63 percent in 1990.

Multistate corporations enjoy the lion's share of potentially taxable profits collected in Oregon and hence are the primary beneficiaries of the declining corporate income tax. In 2002, multistate firms collected 84 percent of all taxable profits reported in Oregon.

Figure 4: Percent of total corporate taxable profits reported by multistate corporations, Oregon



Source: Legislative Revenue Office.

Large multistate corporations are increasing their presence in Oregon, in part because of consolidation in several industries. Between 1990 and 2002, the number of corporations operating only in Oregon fell by 15 percent, while the number of multistate corporations rose by 42 percent.[10]

Multistate firms still make up only about a third of all Oregon corporations, but they collect an increasing share of the profit. In 1990, multistate companies collected 63 percent of all taxable profits reported in Oregon. Just a decade later in 2000, the figure had reached 87 percent. While the recession pushed the percentage down to 84 percent in 2002, the long-term trend seems to be toward more dominance by multistate firms (Figure 4).

With multistate companies collecting 84 cents of every dollar of taxable profit reported in Oregon, the state corporate income tax will be healthy only if it effectively taxes the profits of large multistate firms.

Most corporations pay the minimum corporate income tax

Oregon requires that all corporations operating in Oregon at least pay a minimum corporate income tax of $10. Oregon first set the corporate minimum tax at $25 in 1929, then lowered it to $10 in 1931. It has not changed since then.

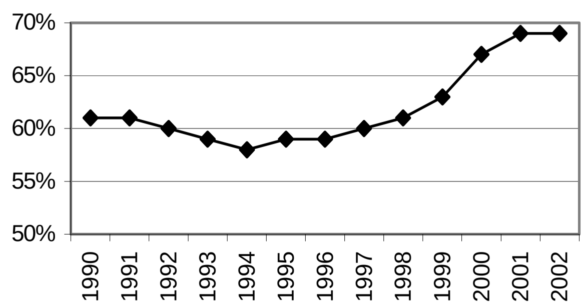
Corporations paying the $10 minimum claim no tax liability in Oregon, but that does not mean that these companies are failing or without profits. Many corporations that are profitable pay the minimum tax.

In 2002, the most recent year with available data, 69 percent of Oregon corporations paid the $10 minimum. Among corporations with Oregon sales over $25 million, 51 percent paid $10.

The large majority of corporations paying $10 report zero or minimal profits, or a loss. It is not clear how many of these companies actually were unprofitable, because loopholes in state tax law allow companies to hide profits from taxation. We do know how many profitable corporations reduce their tax bills by applying losses from prior years when determining tax liability in profitable future years. Oregon allows prior year losses to be carried forward for 15 years. Of those companies paying $10 in 2002, 21 percent would have paid more than the minimum if they had not carried forward losses from prior years. Another way that profitable companies end up paying $10 is by taking advantage of tax credits. In 2002, a total of 241 corporations used credits to lower their tax liability to $10. That's about one percent of the total number of corporations paying the minimum tax.

The percentage of corporations paying the minimum corporate income tax has increased since the early 1990s, reaching 69 percent in 2001.

Figure 5: Percentage of C-corporations paying Oregon's $10 minimum corporate income tax



Source: OCPP analysis of Legislative Revenue Office data.

The percentage of corporations paying the minimum corporate income tax has increased since the early 1990s, when Oregon underwent a modest recession. In 1990, 61 percent of corporations operating in Oregon paid the minimum. After dipping slightly in the mid-1990s, the percentage steadily increased in the last half of the decade, reaching 69 percent after the economic downturn hit in 2001 (Figure 5).

Slide in corporate income taxes will cost $1.8 billion in 2005-07

If corporate income taxpayers still paid the same share of income taxes they paid in 1973-75, state revenue for the upcoming budget cycle would be $1.8 billion higher than is now expected.

Table 2: Lost revenue in Oregon due to decline in share of state income taxes paid by corporations

Budget cycle	If corporations paid share of income taxes paid in 1973-75 (millions)	If corporations paid share of income taxes paid in 1999-01 (millions)
1975-77	$77	
1977-79	$48	
1979-81	$93	
1981-83	$239	
1983-85	$276	
1985-87	$299	
1987-89	$360	
1989-91	$580	
1991-93	$688	
1993-95	$648	
1995-97	$748	
1997-99	$1,029	
1999-01	$1,207	
2001-03	$1,329	$266
2003-05	$1,441	$199
2005-07	$1,814	$415
2007-09	$1,981	$413
2009-11	$2,316	$551
Total through 2005-07	**$10,874**	**$879**
Total through 2009-11	**$15,171**	**$1,843**

Source: OCPP analysis of data from Legislative Revenue Office and data from May Economic & Revenue forecast.

Oregon is losing large amounts of revenue as the corporate income tax erodes. If corporate income taxpayers still paid the same share of income taxes they paid in 1973-75, state revenue for the upcoming budget cycle would be $1.8 billion higher than is now expected. Revenue would have been $1.4 billion higher in the current 2003-05 budget cycle, and $1.3 billion higher in the 2001-03 biennium (Table 2). That is, if only corporate income taxpayers were still paying the share of income taxes they paid in the early 1970s, Oregonians would have better-funded schools, courts, and family and senior support services, without having to pay a dime more in personal income taxes.

In total, because corporate taxpayers have not sustained the 18.5 percent share of income taxes they paid in 1973-75, Oregon has lost a total of $10.9 billion. By the end of this decade, the figure will reach $15.2 billion (Table 2).

Even if Oregon simply stopped the further collapse of corporate income tax revenue that has occurred since the recent recession hit in 2001, the state would receive substantial and crucial revenues to pay for state and local services in upcoming years. In 1999-01, prior to the economic downturn, corporate income taxpayers paid 8.2 percent of all income taxes. If Oregon simply asked corporate taxpayers - mainly large multistate companies - to sustain this level of revenues for the remainder of the decade, the state would have $415 million more for the upcoming budget cycle, $413 million more for 2007-09, and $551 million more for 2009-11 (Table 2). On the other hand, if corporate income taxes are not changed, Oregon will either have to shift the costs of these revenue losses to other taxpayers, mainly individual Oregonians, or watch state services deteriorate further.

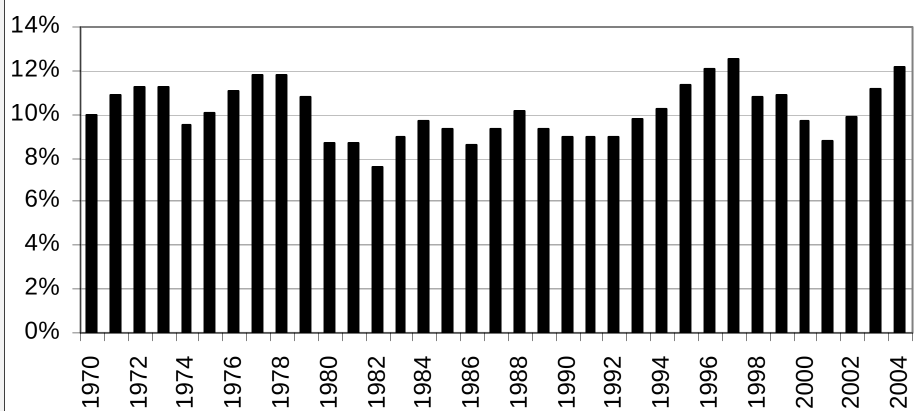
Corporate profits rising as fast as personal income

In the U.S. as a whole, as in Oregon, individual income taxpayers now pay a higher share of income taxes relative to corporate taxpayers than in the 1970s, even though corporate profits have risen as quickly as personal income.

Since 1970, pre-tax corporate profits have hovered generally between eight and twelve percent of personal income (Figure 6).[11] Last year, corporate profits surged to equal 12.2 percent of personal income. Corporate profit growth is keeping up with personal income growth.

Since 1970, pre-tax corporate profits have hovered generally between eight and twelve percent of personal income. Last year, corporate profits surged to equal 12.2 percent of personal income. Corporate profit growth is keeping up with personal income growth.

Figure 6: U.S. pre-tax corporate profits, as a percent of personal income



Source: OCPP analysis of Bureau of Economic Analysis data. Includes BEA's adjustments for variations in how companies account for inventory withdrawls and depreciation.

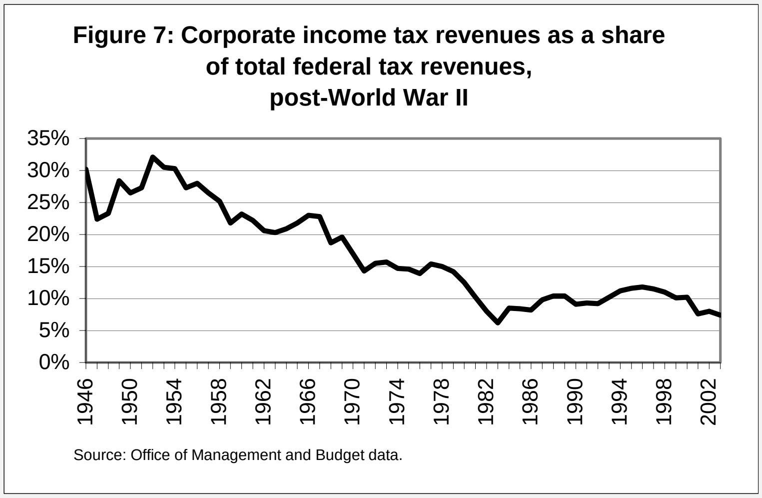
Thanks to the decline in corporate taxes, corporate profits *after tax* have grown relative to personal income after tax. In 1973-75, after-tax corporate profits equaled 6.9 percent of disposable (after-tax) personal income nationally. Between 2001 and 2003, despite the economic downturn, after-tax profits equaled 8.7 percent of disposable income. In 2004, as the economy strengthened, corporate profits surged again and the figure reached 10.6 percent.

The story is similar if corporate profits are examined as a share of the economy. In an average year during the seventies, pre-tax corporate profits equaled 8.7 percent of Gross Domestic Product. From 2001 to 2004, despite the economic downturn, pre-tax corporate profits averaged 9.2 percent of GDP. Last year, the figure reached 10.1 percent.

The trend in profits *after tax* as a share of the economy is unmistakable; after-tax profits are up from 5.3 percent of GDP in the seventies to 7.8 percent of GDP last year.

No data are available for profits made only by companies operating in Oregon.

Federal corporate income tax revenues have also fallen



The federal corporate income tax has collapsed since the 1950s and has slid to historically low levels in recent years. In 2003, federal corporate income tax revenues had plummeted to 1.2 percent of Gross Domestic Product, the lowest level since 1934, the earliest year on record, with the single exception of 1983.[12] Congressional Budget Office projections indicate that corporate tax revenues will remain at historically low levels over the next decade.[13]

As with state corporate income tax revenues, the decline at the federal level is evident both as a share of the economy and in comparison to other funding sources. In 2003, corporate revenues as a share of all federal tax revenue were also at their lowest level on record, with the single exception of 1983.[14] Federal corporate income tax revenues peaked in 1952 at 32 percent of federal receipts. They declined gradually through the 1970s, before falling sharply in the early 1980s. After remaining at low levels but rising slightly during the boom years of the 1990s, corporate income tax revenue as a percent of all federal revenue fell off again beginning in 2001. In 2003, they stood at just 7.4 percent of all federal receipts (Figure 7).

In 2003, corporate revenues as a share of all federal tax revenue were at their lowest level on record, with the single exception of 1983.

Oregon taxes up for low income taxpayers, down for the wealthiest

As Oregon has shifted more of the costs of public services away from multistate corporations and on to Oregon's families, certain families – those with the lowest incomes - have been affected more than others.

Total state and local government taxes have declined in Oregon for all income groups except lower-income taxpayers. In 2003, the average Oregon household paid 6.8 percent of its income in state and local taxes, down from 7.4 percent in 1989. Taxpayers with incomes under $16,000, though, saw their taxes rise between 1989 and 2002 from 7.2 percent of income to 9.4 percent of income (Table 3).

State and local taxes declined most sharply for the richest one percent of Oregon taxpayers – those with incomes over $672,000. Their taxes fell between 1989 and 2002 from 6.5 percent of income to 6.1 percent (Table 3).

Taxpayers with incomes under $16,000 saw their taxes rise between 1989 and 2002 from 7.2 percent of income to 9.4 percent of income.

Table 3: Oregon state and local taxes as share of income

	Lowest 20%	Second 20%	Middle 20%	Fourth 20%	Next 15%	Next 4%	Top 1%
Income Range	Less than $16,000	$16,000 to $27,000	$27,000 to $44,000	$44,000 to $71,000	$71,000 to $132,000	$132,000 to $308,000	Above $308,000
Average	$9,300	$21,100	$34,200	$56,100	$90,900	$182,200	$672,400
1989	7.2%	7.7%	8.0%	8.0%	8.3%	6.9%	6.5%
2002	9.4%	8.9%	8.1%	7.9%	7.3%	6.7%	6.1%

Source: Institute on Taxation and Economic Policy. Taxes include value of federal offset.

Low-income households now pay a higher share of their income in state and local taxes than in 1989 primarily because Oregon increased the cigarette tax and eliminated low-income property relief programs. Property tax reform in Measures 5 and 50 cut and capped property taxes but also led to the downsizing and elimination of property tax relief programs for low-income and elderly Oregonians.[15]

In tax year 2004, a family of four in Oregon with an income of $24,139 (125 percent of the poverty line) will pay $771 in state income taxes. That's more than they would pay in any other state but one – Kentucky.

Table 4: Oregon's 2004 state income tax on working-poor and near-poor families.

	Income	State income tax	Oregon rank (#1 is highest tax)
Families of four:			
With income at poverty line	$19,311	$289	7th
With minimum wage earnings	$14,664	$0	-
With income at 125% of poverty	$24,139	$771	2nd
Families of three:			
With income at poverty line	$15,071	$103	8th
With minimum wage earnings	$14,664	$64	5th
With income at 125% of poverty	$18,839	$463	6th

Source: Center on Budget and Policy Priorities. Rankings are among the 42 states with a state income tax.

Oregon demands more in state income taxes from poor and near-poor families than most of the 42 states with income taxes. In tax year 2004, a family of four in Oregon with an income of $24,139 (125 percent of the poverty line) will pay $771 in state income taxes. That's more than they would pay in any other state but one – Kentucky (Table 4).[16]

What's causing the shift?

The corporate income tax's decline has been wrought primarily by a variety of state and federal tax cuts and tax breaks, and by an increase in the use by corporations of abusive tax shelters that lawmakers never enacted or intended to allow. Over the last generation, Oregon has:

- Lowered taxes for multistate companies with large shares of their property and payroll in Oregon by changing the formula used to calculate the taxes they owe
- Created an automatic tax cut for corporations that kicks in when the state economist's projections of corporate income tax revenues are even slightly off

- Lowered corporate tax rates
- Increased spending on corporate tax breaks

At the same time, beginning in the 1990s, corporations nationally grew much more aggressive about tax planning and sheltering. By taking advantage of loopholes in state and federal corporate income tax systems, corporations were able to report less income on their state income tax returns relative to the income they reported to shareholders.

The combination of more aggressive corporations and more accommodating corporate income tax laws has produced, not surprisingly, lower corporate income tax receipts.

Single-sales factor: the silent robber baron

According to the state economist, the primary reason why Oregon's corporate income tax collections will be stagnant for the rest of this decade is that Oregon is phasing in a major tax cut for companies with large portions of their property and payroll in Oregon, and relatively few sales in-state.[17]

The tax cut involves a change in the formula corporations operating in more than one state must use to determine how much of their profits to apportion to each state. Most states require a formula based on the share of a corporation's property, payroll, and sales located in the state.

Until 1991, Oregon used a formula that equally weighted the three factors (property, payroll, and sales). That year, Oregon switched to a formula that "double-weighted" the sales factor. Oregon sales as a percent of sales in all states now drove half the formula, rather than just one-third. The change produced a tax break for companies that had a high share of their property and payroll in Oregon but a small share of their total sales in the state. Companies with sales in Oregon but little property and payroll here saw their taxes increase.

The change from an equally weighted formula to a double-weighted sales factor formula cost Oregon about $5 million per biennium in the mid-1990s.[18]

Between 2003 and 2008, Oregon is phasing in a "single-sales factor" formula (Table 5).[19] The formula for apportioning profit will be based on one factor only, in-state sales as a percent of sales in all states. Companies with large portions of their property and payroll in Oregon, and few sales, will reap extremely large cuts in their corporate income taxes.

Between 2003 and 2008, Oregon is phasing in a "single-sales factor" formula. Companies with large portions of their property and payroll in Oregon, and few sales, will reap extremely large cuts in their corporate income taxes.

Table 5: The changing formula for apportioning corporate income, Oregon			
	Property	Payroll	Sales
Three factor (pre-1991)	33%	33%	33%
Double-weighted sales (1991)	25%	25%	50%
Super-weighted sales (2003)	10%	10%	80%
Super-weighted sales (2006)	5%	5%	90%
Single-sales factor (2008)	0%	0%	100%

Source: Table format from Oregon Department of Revenue

While some companies operating in Oregon – those with sales here but little property or payroll – will see their taxes increase, the overall revenue impact is significantly negative. The Legislative Revenue Office estimates that Oregon will spend $73 million on this tax break in the upcoming 2005-07 budget cycle. Based on this estimate, the single-sales factor will reduce corporate income tax revenues next biennium by 13.3 percent (Table 6).[20]

As a share of projected corporate income tax revenues, the revenue loss from the switch to a single-sales apportionment formula will remain significant well into the future. Revenues in 2009-11 will be 12 percent lower than they would have been without the switch to the single-sales factor formula (Table 6).

The single-sales factor will reduce corporate income tax revenues next biennium by 13.3 percent.

Table 6: Projected revenue losses from single-sales factor				
Budget cycle	2003-05	2005-07	2007-09	2009-11
Projected corporate income tax revenues (millions)	$600	$472	$564	$560
Revenue loss from switch to single-sales (millions)	$71	$73	$75	$76
Percent lost	10.5%	13.3%	11.7%	12.0%

Source: OCPP analysis of Legislative Revenue Office data.

The single-sales factor will produce an extraordinarily deep, permanent tax cut for large, multistate companies with major production facilities or other property and payroll located in Oregon, such as Intel and Nike. A hypothetical firm with 20 percent of its property and payroll in Oregon, and one percent of their sales, would see its annual taxes fall by more than 90 percent thanks to the formula change (Table 7).

Table 7: Effect of change to "single-sales factor," selected hypothetical companies

	Large retailer headquartered out-of-state	Regional business	Large manufacturer with major production facilities in Oregon
Sales	1.0%	33.0%	1.0%
Property	0.5%	33.0%	20.0%
Payroll	0.5%	33.0%	20.0%
Percent of Profits Subject to Oregon Tax			
Equal-weighted (Pre-1991)	0.7%	33.0%	13.7%
Double-weighted sales (1991-2003)	0.8%	33.0%	10.5%
Super-weighted sales (2003-2006)	0.9%	33.0%	4.8%
Super-weighted sales (2006-2008)	1.0%	33.0%	2.9%
Single-sales factor (2008-onward)	1.0%	33.0%	1.0%
Percent change from double-weighted	33.3%	0.0%	-90.5%
Percent change from equal-weighted sales	50.0%	0.0%	-92.7%

Source: OCPP

A hypothetical firm with 20 percent of its property and payroll in Oregon, and one percent of sales, would see its annual taxes fall by more than 90 percent thanks to the formula change.

The revenue loss from the single-sales factor is exacerbated when corporations locate distribution centers in states with low or no corporate income taxes on sales, such as Nevada. A company with such an arrangement could apportion all or most of its sales to Nevada, leaving few or no sales to report in Oregon.[21] Since Nevada has no corporate income tax, and Oregon will soon base its entire corporate income tax on sales apportioned to Oregon, this hypothetical firm would owe no corporate income tax in either Oregon or Nevada. Since Oregon has a minimum corporate income tax - $10 – the company would, however, have to pay roughly the cost of one fourth-grader's textbook each year.

Oregon's move to a single-sales factor apportionment formula also means that if Oregon convinces multistate manufacturers in growing fields like nanotechnology or biotechnology to locate in Oregon, corporate income tax revenues will not increase much. Google, which recently announced the purchase of land in The Dalles for a new technology infrastructure facility, is likely to be a $10 corporate income taxpayer in Oregon for years to come because of the single-sales factor apportionment formula. The same goes for Yahoo, which recently announced plans to for a customer service center in Hillsboro.

Corporate tax rate was increased in late 1970s, then cut in 1987

Another reason why corporate income tax collections have declined since the 1970s is that the statutory corporate income tax rate was cut in 1987.

In the last half of the 1970s, Oregon's Legislative Assembly raised the state corporate income tax rate for corporations to 7.5 percent, an increase from the 6 percent rate that previously applied to all corporations except financial corporations.[22] Prior to the changes, financial corporations paid 8 percent of their income (Table 8).

Oregon lowered the state corporate income tax rate from 7.5 percent to 6.6 percent in1987. The rate remains at 6.6 percent today.

Table 8: Corporate tax rates, 1929 to present		
Year	**Tax rate**	**Type of corporation**
1929	5.0%	All Corporations
1932	8.0%	All Corporations
1955	4.0%	All Corporations
1957	6.0% 7.0% 9.0%	Regular Corporations Public Utilities Financial Corporations
1959	6.0% 6.0% 9.0%	Regular Corporations Public Utilities Financial Corporations
1963	6.0% 6.0% 8.0%	Regular Corporations Public Utilities Financial Corporations
1976	6.5% 6.0% 6.5%	Regular Corporations Public Utilities Financial Corporations
1977	7.0%	All Corporations
1978	7.5%	All Corporations
1987	6.6%	All Corporations

Source: Oregon Department of Revenue, *Oregon Corporate Excise and Income Tax: Characteristics of Corporate Taxpayers, 2004 Edition*, p. 1-4.

Following a major revision of the federal corporate tax structure in 1986 that included reductions in the federal corporate tax rate, Oregon lowered the state corporate income tax rate from 7.5 percent to 6.6 percent, effective on January 1, 1987.[23] The rate remains at 6.6 percent today.

The rate cut produced a permanent and significant corporate tax cut. To put the size of the cut in perspective, if in the upcoming 2005-07 budget cycle corporate income tax revenues were increased in line with the size of the 1987 rate cut, revenues would rise by $66 million.[24]

Growth in corporate tax breaks has also cut revenues

Corporations operating in Oregon enjoy a total of 101 different corporate income tax credits and other subtractions. About half of these breaks (52) are contained in the federal corporate income tax code. Oregon chose to allow corporations operating in Oregon to receive these breaks. The other half (49) are subtractions, credits, and other breaks offered specially by the State of Oregon.

Of the 49 corporate income tax breaks Oregon specially offers corporations, 40 were created since 1980.

Table 9: Oregon-specific corporate income tax breaks, by year created	
Year created	**Number of Oregon-specific tax breaks**
Before 1980	9
1980-89	13
1990-99	11
2000-03	16
1980-03	40
1995-03	25
TOTAL	**49**

Source: OCPP analysis of Oregon Department of Revenue data.

The total cost of all Oregon-specific tax breaks combined will be $66.6 million in the upcoming budget cycle. The growing cost of new Oregon-specific credits and subtractions created over the last generation has contributed to the corporate income tax's slide.

Of the 49 corporate income tax breaks Oregon specially offers corporations, 40 were created since 1980. More than half were created since 1995 (Table 9).

The most expensive of Oregon's tax credits is the Qualified Research Activities credit, for investments in research and development in Oregon. This credit, commonly known as the R&D credit and originally created in

1989, is projected to cost Oregon $21.6 million in the upcoming budget cycle. Its costs are increasing because Oregon legislators approved a 50 percent increase in the maximum size of the credit corporations may take. Beginning in 2006, corporations will be eligible for a maximum credit of $750,000, up from $500,000 today.[25]

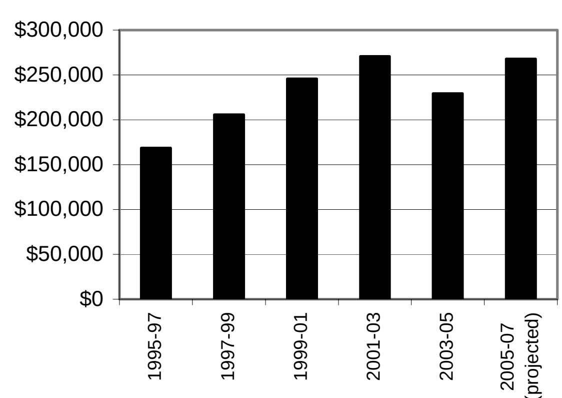
At the federal level, the largest corporate income tax break by far is the one that allows corporations to depreciate the value of equipment more quickly than the equipment's value actually depreciates. This tax break cost Oregon $110.4 million in 1999-01, prior to the economic downturn. During the downturn, the cost of this break soared, reaching $208.9 million in 2001-03, because in two separate pieces of legislation Congress allowed corporations to depreciate the value of equipment purchased between September 2001 and December 2004 even more rapidly than normal.

In total, the 52 federal corporate income tax breaks affecting Oregon will cost the state another $229.6 million in 2005-07, a large amount but substantially lower than the cost of federal corporate tax breaks in the previous two budget cycles when the special equipment depreciation schedules were in effect. In 2001-03, federal corporate tax breaks cost Oregon $401.1 million.

Oregon did not begin keeping tabs on the cost to Oregon of state and federal tax breaks until the mid-1990s, when the state began to produce biennial "tax expenditure reports."[26] No data are available on the total costs of tax breaks in Oregon prior to the 1995-97 budget cycle, the first biennium covered by the tax expenditure reports. This lack of data makes it impossible to precisely measure the growth in tax breaks over the last generation.

The available data make clear, however, that excluding the equipment depreciation tax cut, the cost to Oregon of all corporate income tax breaks – Oregon and federal combined – rose steadily during the late 1990s boom and has remained at high levels since. The total cost of all federal and Oregon-specific tax credits, deductions, and subtractions, excluding the equipment depreciation tax break, stood at $168.5 million in 1995-97, rose steadily to $270.7 million in 2001-03, and is projected to remain at $267.9 million in 2005-07 (Figure 8).

Figure 8: Cost to Oregon of all federal and Oregon-specific corporate income tax credits, deductions, and subtractions*



* Excluding federal tax cut allowing accelerated depreciation of equipment.
Source: OCPP analysis of State of Oregon Tax Expenditure Reports

Excluding the equipment depreciation tax cut, the cost to Oregon of all corporate income tax breaks rose steadily during the late 1990s boom and has remained at high levels since.

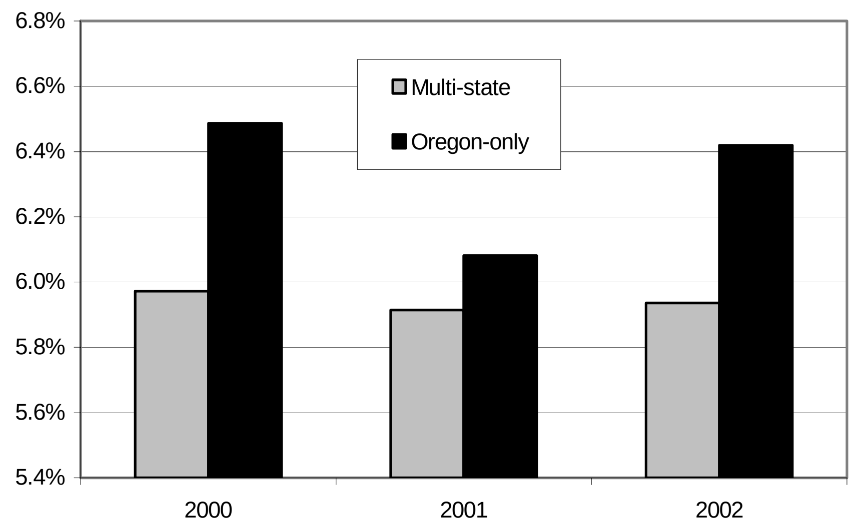
Oregon tax credits help multistate corporations more than in-state firms

Corporate use of tax credits like the credit for Qualified Research Activities and the Pollution Control Tax Credit lower corporate income tax bills below Oregon's 6.6 percent rate.[27] Compared to in-state companies, multistate corporations have taken more advantage of such credits in recent years.

In 2002, multistate corporations paid 5.9 percent of their taxable income in corporate income taxes. Companies operating only in Oregon by contrast paid 6.4 percent. This disparity was also evident in 2000 and 2001, though the gap narrowed in 2001 when the recession hit (Figure 9).

In 2002, multistate corporations paid 5.9 percent of their taxable income in corporate income taxes. Companies operating only in Oregon by contrast paid 6.4 percent.

Figure 9: Taxes paid as a % of Oregon taxable income, multistate vs. Oregon-only corporations



Source: OCPP analysis of Oregon Department of Revenue data.

The lower tax rates for multistate firms suggest that these companies took more advantage of tax credits in 2000 through 2002. With these larger firms increasingly dominating Oregon's corporate income tax base, these credits are now more expensive than if Oregon's corporate mix had not changed.

In the next few years, the gap in tax rates between multistate and Oregon-only corporations will likely widen, as Oregon institutes the single-sales factor apportionment formula. The 2000-02 data precedes the phase-in of the single-sales factor formula. By substantially reducing the amount of income that is taxable in Oregon, the single-sales formula will increase the value of tax credits. Companies with lower taxable incomes in the future due to the single-sales formula will benefit more from tax credits, since the credits will equal a higher percentage of their taxable income.

Kicker worth more to corporations than personal income taxpayers

The state corporate income tax is also in decline thanks to a break offered by no other state except Oregon. Known as the "kicker," this unusual tax cut was created by Oregon legislators in 1979. If the amount of Oregon income taxes collected exceeds the state economist's projections (from a forecast two years prior) by two percent or more, the entire excess is returned to the taxpayer. Individuals receive a refund check; corporations receive a tax credit on the tax return for the tax year in which the biennium ends.

The corporate kicker assures that if corporate profits grow a little more quickly than expected, corporate income tax revenues will not rise accordingly. The kicker is partly responsible for assuring that Oregon's corporate income tax never recovered from the early 1980s recession, even during the boom years of the 1990s.

Not long after the corporate kicker was created in 1979, the state and national economy fell into back-to-back recessions in the early 1980s. Corporate profits slumped, so the kicker was not triggered. Then, following each of the three budget cycles from 1983-85 to 1987-89, as the economy began to grow again, the kicker started kicking. The 1980s kicker tax breaks cost Oregon a total of $56 million (Table 10).

Table 10: History of Oregon's corporate kicker

Budget cycle	Corporate kicker (in millions)	Percent cut in corporate income tax revenues in subsequent biennium
1979-81	None	n/a
1981-83	None	n/a
1983-85	$13	4.2%
1985-87	$7	2.1%
1987-89	$36	10.8%
1989-91	None	n/a
1991-93	$18 (suspended)	n/a
1993-95	$167	19.6%
1995-97	$203	25.6%
1997-99	None	n/a
1999-01	None	n/a
2001-03	None	n/a
2003-05	$63 (projected)	11.4% (projected)
TOTAL	**$489**	

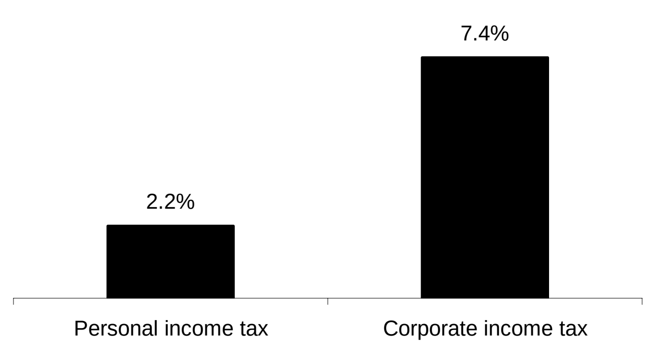
Source: OCPP analysis of data from the Oregon Department of Revenue and the Office of Economic Analysis, May 2005 Economic and Revenue forecast.

Oregon companies will have received a total of $489 million since the kicker was established in 1979.

Following the mild recession of the early 1990s, the corporate kicker started kicking again. At the end of the 1991-93 budget cycle, the kicker would have delivered another $18 million to Oregon corporations, but the 1993 legislature refused to allow the kicker tax cut, in part because of revenue losses from the passage of the Measure 5 property tax cut in 1990. This suspension is the only time in its history that legislators have disallowed the corporate kicker.

Over the next two budget cycles, the size of the corporate kicker exploded. Following the 1993-95 budget cycle, corporations received $167 million in credits from the kicker. Then, after the 1995-97 biennium, corporations got another $203 million. This huge kicker tax break lowered corporate income tax collections by one-fourth in the subsequent budget cycle (Table 10).

Figure 10: Cut in income taxes due to kicker, as a share of all income tax revenue, 1979-81 through 2003-05



Source: OCPP analysis of Legislative Revenue Office data. Note: Corporate income tax kicker data includes projected $62.6 million kicker for 2003-05.

The corporate kicker has been more valuable to corporations than it has to personal income taxpayers.

The corporate kicker has not kicked since, but the state economist currently projects it will kick this biennium. Projections of revenue for the current 2003-05 budget cycle indicate that corporations will receive another $62.6 million in kicker tax credits later this year. If this projection holds, and the legislature does not suspend the kicker, Oregon companies will have received a total of $489 million since the kicker was established in 1979 (Table 10). Unlike corporate income taxpayers, personal income taxpayers are not expected to receive a kicker tax rebate this year.

As a share of income tax revenue, the corporate kicker has been more valuable to corporations than it has to personal income taxpayers. The $489 million corporate income taxpayers have collected from the kicker (including the kicker projected for this biennium) have reduced corporate income taxes by 7.4 percent since the kicker's inception. By contrast, the kicker has cut personal income taxes by 2.2 percent since its inception (Figure 10). Personal income taxpayers have collected $1.4 billion from the kicker since its inception, but paid $64.8 billion.

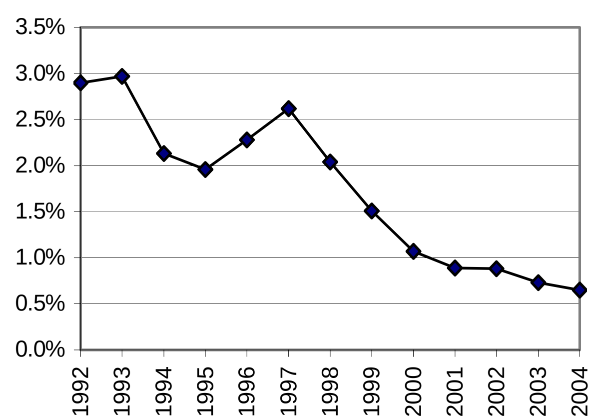
Increasing use of abusive corporate tax shelters

Since the early 1990s, corporations have become much more aggressive in pursuing abusive tax shelters, highly complex transactions that deliberately exploit loopholes in the tax laws to improperly avoid paying taxes on large amounts of profit.

While it is impossible to determine precisely how much revenue Oregon has lost as a result of the explosion in tax sheltering, a study by the Multistate Tax Commission estimated the impact at between $66 million and $94 million for fiscal year 2001 alone.[28] This estimate includes revenue lost when companies shelter income overseas and revenue lost when companies abuse loopholes in state corporate income tax laws. The study estimated Oregon lost $44 million in 2001 alone to international tax shelters, such as when corporations incorporate in tax haven countries or manipulate their books to shift income away from the United States. The study also estimated corporate abuse of loopholes in state corporate income tax laws cost Oregon between $22 and $50 million in 2001.

In 1992, the IRS audited nearly three percent of all corporations. In 2004, just 0.65 percent of corporations faced audits.

Figure 11: Percent of all U.S. corporations audited by the IRS



Source: Transactional Analysis Research Clearinghouse

Both the U.S. Department of the Treasury and the Internal Revenue Service believe abusive tax shelters to be a large and growing problem, amounting to federal revenue losses in the "tens of billions of dollars" annually.[29]

Corporate tax sheltering exploded in the 1990s thanks to the convergence of a number of factors.[30] Changes in corporate culture produced more focus on demonstrating value to shareholders, and less respect for government, particularly tax laws. Also, as more corporations used shelters, circumventing the law seemed increasingly acceptable. The increased sophistication of financial management made possible by computers lowered the cost, as did an enlarged pool of available tax shelter specialists created when Congress closed some personal income tax loopholes in 1986.

In addition, the chance of the Internal Revenue Service auditing a given corporation has declined sharply. In 1992, the IRS audited nearly three percent of all corporations. In 2004, just 0.65 percent of corporations faced audits (Figure 11).[31] For corporations with assets over $250 million, the audit rate fell from 55 percent in 1992 to 29 percent in 2003. While the audit rate for these large corporations rose to 38 percent in 2004, the IRS may be expanding the number of audits by reducing their quality. Data available for the first half of 2004 indicate that the IRS had sharply reduced the number of hours spent auditing large corporations compared to 2003.[32]

Rise in "pass-through" companies is not driving the decline

In the last twenty years, more businesses have opted to form for tax purposes under structures that allow business profits to be "passed through" to shareholders. The growth in these "pass-through" businesses, though, is responsible for only a small portion of the decline in corporate taxes.

S-corporations not central to declining corporate taxes

Businesses choosing to incorporate must elect whether to be C-corporations or S-corporations for tax purposes. C-corporations pay both federal and state corporate income taxes on their profits regardless of whether their profits are passed on to shareholders in the form of dividends. The profits of S-corporations, by contrast, are all passed on to shareholders. These shareholders pay federal and state personal income taxes on their share of S-corporation profits. S-corporations do not pay federal or state corporate income taxes.[33] Both C- and S-corporations enjoy personal liability protection from the state, and access to corporate tax credits.

Generally, only smaller corporations are eligible to elect S-corporation status. S-corporations must be domestic corporations with one class of stock and 100 or fewer shareholders.[34]

Table 11: Total income reported by Oregon S-corporations & C-corporations

Year	Total S-corporation income	Total C-corporation income	C-corporation income as % of all corporate income
1990	$736,964	$2,062,662	74%
2000	$1,792,437	$6,262,312	78%
2002	$1,398,199	$4,591,988	77%

Source: Legislative Revenue Office.

In 2002, C-corporations accounted for 77 percent of all income reported by corporations operating in Oregon, up from 74 percent in 1990.

Growth in S-corporations following federal law changes in 1986 may have somewhat reduced corporate income tax revenue coming from smaller companies, but large C-corporations still collect the bulk of income reported by Oregon corporations.[35]

In fact, C-corporations are collecting a higher share of all income reported by Oregon corporations than they were in 1990, despite the growth in S-corporations. In 2002, C-corporations accounted for 77 percent of all income reported by corporations operating in Oregon, up from 74 percent in 1990 (Table 11).

Limited liability companies not causing major corporate tax declines

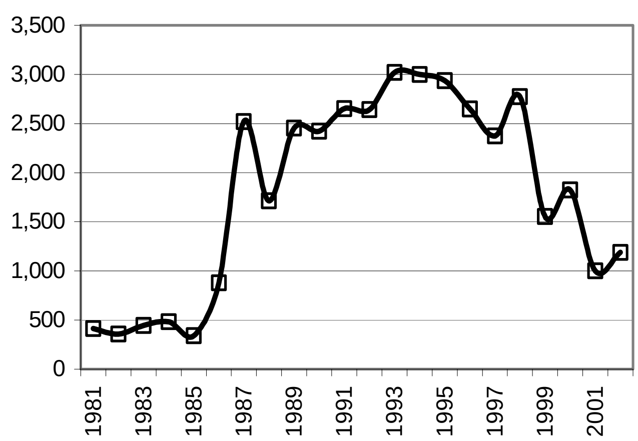
Since 1993, Oregon has allowed businesses to form as "limited liability companies," or LLCs. Except when corporations own the LLCs, the profits of LLCs are passed along to LLC shareholders as income that is taxed through the personal income tax.

LLCs are an increasingly popular choice for Oregon businesses. However, most of the companies forming as LLCs in Oregon today would have formed previously as partnerships, other unincorporated businesses, or as S-corporations – not as C-corporations. As such, the growth in LLCs is not a primary cause of the corporate income tax's decline.

LLCs have certainly slowed the growth of S-corporations. For most smaller businesses, the LLC form is more attractive than an S-corporation form, since it offers the major S-corporation benefit – limited liability protection – without the major S-corporation restrictions – limits on the numbers and types of shareholders. Not surprisingly, then, annual growth in the number of Oregon S-corporations has fallen off sharply since 1993, when LLCs were first allowed in Oregon. Growth in the number of S-corporation filings in Oregon fell from 3,020 in 1993 to 1,187 in 2002 (Figure 12).

Annual growth in the number of Oregon S-corporations has fallen off sharply since 1993, when LLCs were first allowed in Oregon.

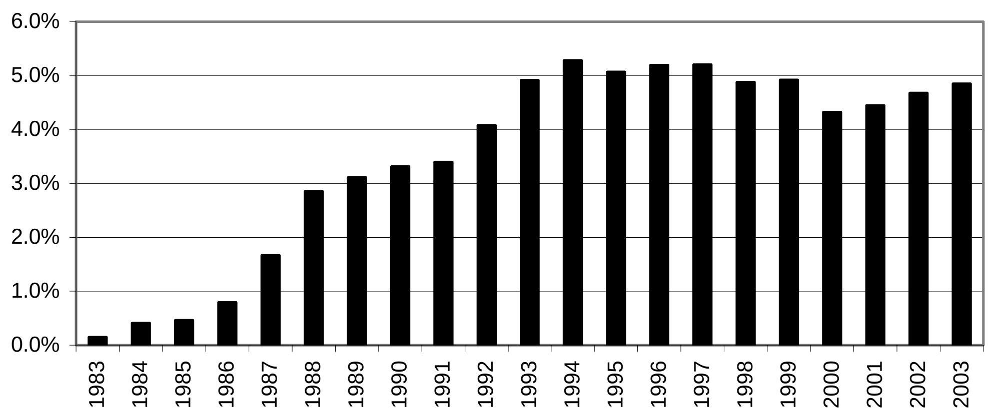
Figure 12: Annual growth in S-corporation filings in Oregon



Source: OCPP analysis of Oregon Dept. of Revenue data.

If a large number of C-corporations were selecting LLC status, one would expect Oregon personal income taxpayers to report a sharp increase in business income. This does not appear to be happening. Since 1993, income reported on Schedule E, which includes income from LLCs and S-corporations, has declined slightly as a share of all income in Oregon (Figure 13). Schedule E income rose quickly in the late 1980s and early 1990s, suggesting that rapid S-corporation growth following the 1986 changes to the federal tax code produced personal income tax growth during this period. Since then, however, Schedule E income has been flat, declining slightly as a share of all income.

Figure 13: Schedule E income, including income from S-corporations and LLCs, as a percent of total reported income, Oregon



Source: Oregon Office of Economic Analysis

Since 1993, income reported on Schedule E, which includes income from LLCs and S-corporations, has declined slightly as a share of all income in Oregon.

This evidence is not conclusive, since Schedule E income also includes income from rental properties and other income, but the extraordinary growth in LLCs has clearly not produced a remotely equivalent increase in reported personal income. Given this, it is unlikely that a large number of C-corporations are choosing to form as LLCs.

C-corporations do appear increasingly likely to form subsidiaries as LLCs, however. Over the 1990s, corporations nationally owned an increasing amount of total LLC and other partnership income, according to an analysis by the Center on Budget and Policy Priorities.[36] Oregon corporations owning LLC subsidiaries pay corporate income taxes on income earned by these subsidiaries. In such cases, the establishment of LLCs will not reduce Oregon's corporate income tax revenues.

Corporate share of state and local fees has not increased

Faced with voter antipathy to higher taxes and sustained voter interest in decent public services, Oregon's state and local governments have increasingly relied upon fees to cover the costs of providing services. As a percent of all general revenues, fees increased from 14 percent in 1991-92 to 18 percent in 2001-02. Other states are relying slightly more on fees, but Oregon has more sharply increased its fee dependence. Nationally, fees accounted for 15 percent of all state and local general revenues in 2001-02, up slightly from 14 percent in 1991-92.

Oregon's increased reliance on fees, however, does not account for the decline in corporate income tax revenue. Fee growth since the early 1990s has been driven by increased revenues primarily in three areas: college tuition and other higher education fees, state and county hospital revenues, and sewer fees. Together, these three fee categories account for 78 percent of all fee growth in Oregon between 1991-92 and 2001-02 (Table 12).[37]

Fee growth since the early 1990s has been driven by increased revenues primarily in three areas: college tuition and other higher education fees, state and county hospital revenues, and sewer fees.

Table 12: Revenue from fees and other charges, Oregon

Category	1991-92	2001-02	Change	As % of all change
Institutions of higher education	$414,200	$931,983	$517,783	33.9%
Hospitals	$383,951	$744,813	$360,862	23.6%
Sewerage	$213,798	$524,763	$310,965	20.3%
Airports	$52,221	$149,730	$97,509	6.4%
Natural resources	$58,357	$154,767	$96,410	6.3%
Highways	$7,676	$65,229	$57,553	3.8%
Other education	$49,383	$84,268	$34,885	2.3%
Housing and community development	$21,592	$55,424	$33,832	2.2%
Parks and recreation	$68,378	$92,745	$24,367	1.6%
School lunch sales	$40,872	$56,880	$16,008	1.0%
Parking facilities	$14,928	$28,627	$13,699	0.9%
Sea and inland port facilities	$82,127*	$79,678	-$2,449	-0.2%
Solid waste management	$81,870	$49,745	-$32,125	-2.1%
TOTAL	**$1,489,353**	**$3,018,652**	**$1,529,299**	**100.0%**

* This figure is for 1992-93. No data are available for "Sea and inland port facilities" for 1991-92.
Source: OCPP analysis of U.S. Census Bureau data.

None of these three categories of fees are primarily borne by corporate income taxpayers.

Individual students and their families pay the biggest single driver of fee revenue increases since the early 1990s - increases in tuition and other fee revenue collected by state universities and local community colleges. These fees account for nearly one-third (33.9 percent) of all fee growth in Oregon between 1991-92 and 2001-02.

Another 23.6 percent of the growth in fee revenue since 1991-92 results from increases in the revenues collected by state and county hospitals for health care services received by patients.[38] Patients are individuals, not corporations. Some of the revenue collected by state and county hospitals is paid through employer-provided health insurance plans, but such insurance is a form of employee compensation.

Another 20.3 percent of all fee growth since 1991-92 is due to increased revenues for local governments from sewer fees. Owners of both residential and commercial property pay sewer fees based on how much they use the system. In the City of Portland, residential customers make up 92 percent of all accounts billed for sewer use.[39]

Businesses in Portland do not appear to be paying a higher share of sewer charges. According to estimates prepared by Portland's Bureau of Environmental Services, between 1995 and 2005 revenues from sewer-related user fees paid by residential customers rose 169 percent, while revenues from businesses rose 156 percent.[40]

Besides higher education fees, state and county hospital charges, and sewer fees, individual Oregonians and Oregon businesses pay a wide range of other fees, but these other fee categories combined total only a little over a quarter of all state and local government fee revenues.

Businesses pay fees including airport landing fees, business license fees, and port-related fees. Businesses also typically purchase the timber sold off state lands, which is counted as a "charge" by the Census Bureau.

Individuals also pay a wide range of fees including co-payments to the Oregon Health Plan, library fees, school lunch fees, state and local park and recreation fees, and public housing rent charges. Both businesses and individuals pay some fees such as parking fees and court fees.

It is not possible to precisely determine the share of all fee revenue paid by corporations or the share paid by individuals. However, the available data suggest that corporations are not bearing a disproportionate share of fees or fee increases.

Conclusion

Oregon's corporations are paying less of the bill for Oregon's public investments in quality schools, courts, public safety, and family supports than they were a generation ago. As a result, more of the cost of state and local services has shifted to individual taxpayers. Low-income taxpayers have been hit the hardest. Large, multistate corporations have benefited the most from the collapse of the state corporate income tax.

The strength of public investment programs in Oregon will significantly shape Oregon's economic health over the long-term. Paying for these investments will continue to fall heavily and increasingly on individual households in Oregon unless legislators and the public insist that large, multistate corporations renew their commitment to Oregon's future by increasing the amount of taxes they pay.

Endnotes

[1] Lynch, Robert. Rethinking *Growth Strategies: How State and Local Taxes and Services Affect Economic Development*. 2004. Economic Policy Institute, p. 4-6.
[2] Ibid, p. vii.
[3] OCPP examined Gross State Product data back to the 1977-79 budget cycle because 1977 is the first year for which Gross State Product data for Oregon is available on the BEA website.
[4] Utah State Tax Commission, Western States' Tax Burdens, Fiscal Year 2002-2003: Initial State and Local Tax Burdens for Selected Western States, Revised February 3, 2004. Available at http://tax.utah.gov/esu/burdens/WTB_2003.pdf. The Utah Tax Commission's study focuses on the initial incidence of taxes (i.e. who gets the bill), except in cases where final incidence can be clearly determined. The Commission has felt that attempting to assess the final incidence of taxes would be both difficult and cost-prohibitive. Because it is based on initial incidence, however, the study includes as "business" taxes some taxes most economists agree are not fully borne by owners of capital, such as unemployment insurance and property taxes on rental property. The Utah State Tax Commission is currently reviewing its approach with respect to property taxes on rental property.
[5] The seven states included in the study were Oregon, Utah, Colorado, California, Arizona, Idaho, and Washington.
[6] Cline, Robert, et. al., *Total State and Local Business Taxes*, Council On State Taxation, April 12, 2005. Available at http://www.statetax.org/Content/ContentGroups/Home_Page_Content/Right_Column_Area/2005TotalStateAndLocalBusinessTaxes.pdf. The COST study emphasizes that state and local business taxes nationally rose more quickly than household taxes between 2000 and 2004. The study neglects to mention that corporate profits rose much more quickly than personal income over this period. Between 2000 and 2004, corporate profits nationally grew 44.5 percent, while personal income was up just 14.7 percent. The COST study focuses on the initial incidence of taxes (i.e. who gets the bill). As a result, the study includes as "business" taxes a broad range of taxes most economists agree are not fully borne by owners of capital, such as unemployment insurance and property taxes on rental property. COST also classifies property taxes paid by businesses such as farmers on their personal, owner-occupied homes and telecommunications taxes that are directly billed to consumers, as "business" taxes. In addition, COST considers all non-profit organizations as "businesses," thus adding their taxes to the business tax burden.
[7] McIntyre, Robert S. and T. D. Coo Nguyen, *State Corporate Income Taxes, 2001-2003*, February 2005, a Joint Project of Citizens for Tax Justice and the Institute on Taxation and Economic Policy.
[8] The average statutory state corporate income tax rate is 6.8%, after adjusting for each state's share of GDP. The amount of corporate income taxes corporations actually pay to the states collectively may differ somewhat from the amount of state corporate income taxes reported to the Securities and Exchange Commission, from which the CTJ study drew its data. The differences are likely to be minor in most cases and largely attributable to timing differences between tax and financial reporting concepts.
[9] State of Oregon Office of Economic Analysis, *Oregon Economic and Revenue Forecast, May 2005*, Volume XXV, No. 2. Available at http://www.oea.das.state.or.us/DAS/OEA/docs/economic/forecast0605.pdf.
[10] Legislative Revenue Office, *2005 Oregon Public Finance Basic Facts*, Research Report #1-05, January 7, 2005, p. C2. Available at http://www.leg.state.or.us/comm/lro/LRO_1-05.pdf
[11] All data on corporate profits in this text box are based on an OCPP analysis of data from the Bureau of Economic Analysis, and include BEA's adjustments in corporate profits data for variations in how companies account for inventory withdrawls and depreciation.
[12] Friedman, Joel. *The Decline of Corporate Income Tax Revenues*, Center on Budget and Policy Priorities, revised October 24, 2003, p. 5. Available at http://www.cbpp.org/10-16-03tax.pdf.
[13] CBO projects corporate income taxes will rise slightly to 1.8 percent of GDP in 2005, then gradually decline, reaching 1.5 percent of GDP in 2011 and remaining at 1.5 percent of GDP through 2015, the last year projected. Congressional Budget Office, *The Budget and Economic Outlook: Fiscal Years 2006 to 2015*, January 2005. See Table 4-1. Available at http://www.cbo.gov/showdoc.cfm?index=6060&sequence=5.
[14] Office of Management and Budget, "Historical Tables: Budget of the United States Government, Fiscal Year 2005," Washington, D.C.: U.S. Government Printing Office, Table 2:2, p. 31-32. Available at http://www.whitehouse.gov/omb/budget/fy2005/pdf/hist.pdf. Joel Friedman includes this fact in his paper *The Decline of Corporate Income Tax Revenues*, written for the Center on Budget and Policy Priorities, revised October 24, 2003, and available at http://www.cbpp.org/10-16-03tax.pdf.
[15] For example, the Homeowners and Renters Refund Program (HARRP) provided a minimum refund of $750 to household with incomes below $17,500 up through 1990-91, but was reduced in 1991-92 and eliminated in 1992-93. Property tax relief programs provided nearly $75 million in relief as late

as 1988-89, but provided no relief by 1997-98. 2004 *Oregon Public Finance: Basic Facts*, Legislative Revenue Office, Research Report #1-04.

[16] Llobrera, Joseph and Robert Zahradnik, *The Impact of State Income Taxes on Low-Income Families in 2004*, Center on Budget and Policy Priorities, April 12, 2005. Available at http://www.cbpp.org/4-12-05sfp.pdf.

[17] The March 2005 Economic and Revenue Forecast states, "Beginning with the 2008 corporate tax year, the apportionment of federal taxable income to Oregon will be based solely on relative sales in the state. This reduces Oregon tax liability relative to the current, three-factor formula. As a result, corporate collections are expected to remain virtually flat, declining a slight 0.7 percent to $560.3 in 2009-11." State of Oregon Office of Economic Analysis, *Oregon Economic and Revenue Forecast, March 2005*, Volume XXV, No. 1, p. 54. Available at http://www.oea.das.state.or.us/DAS/OEA/docs/economic/forecast0305.pdf.

[18] The September 1993 Economic and Revenue Forecast estimated that double weighting the sales factor would cost Oregon $1.92 million in FY94, $2.607 million in FY95, $2.598 million in FY96, $2.606 million in FY97. Information contained in email to author from Michael Kennedy, Office of Economic Analysis, May 2, 2005.

[19] House Bill 2281, passed in 2001, implemented a "super sales factor" formula, under which in-state sales would account for 80 percent of the apportionment formula, beginning in 2003. House Bill 3183, passed in 2003, phased in the single-sales factor formula, under the schedule described in Table 5.

[20] The Legislative Assembly unfortunately has not yet required an analysis of the actual revenue impact of the single-sales factor in future biennia. However, under ORS 314.647, Oregon must "carry out a comprehensive review of business income apportionment whenever federal legislation changes the nexus standard for state imposition of taxes based on business activity within state borders."

[21] *Oregon Revised Statutes* 314.665, sections 2(a) and 2(b), and section 4.

[22] In 1976, Oregon changed to a single rate for all corporations of 6.5 percent. The single rate increased to 7 percent in 1977 and 7.5 percent in 1978. Oregon Department of Revenue, *Oregon Corporate Excise and Income Tax: Characteristics of Corporate Taxpayers, 2004 Edition*. Report No. 150-102-405 (Rev. 12-04), p. 1-4. Available at http://egov.oregon.gov/DOR/STATS/docs/102-405-FY04/102-405-FY04.pdf.

[23] Ibid.

[24] The 1987 cut reduced rates by 13.6 percent, relative to the current 6.6 percent rate. Corporate income tax revenues in the 2005-07 budget cycle are projected to be $487 million. Taking 13.6 percent of $487 million yields $66.2 million, an estimation of the rate cut's impact on the upcoming budget cycle.

[25] In 2002, just 70 companies benefited from this credit. In previous biennia, the number of corporations benefiting has ranged as high as 120. If a corporation cannot fully use the credit because it does not owe enough taxes may use the remaining credit in later years, for up to five years. This "carry forward" feature was instituted in 1993.

[26] The Budget Accountability Act of 1995 established the requirement that the Governor produce tax expenditure reports. See *Oregon Revised Statutes* 291.190, 291.195, 291.201, and 291.203.

[27] Credits are primarily responsible for the difference between actual corporate tax rates on Oregon taxable income and the 6.6 percent rate. However, some of the difference is also because companies must pay taxes on any interest they owe on certain installment sales and also because corporations must pay taxes on net long-term capital gains from farm property. Companies with these additions will see their tax rate on Oregon taxable income increase. In addition, under IRS rules corporations switching from C-corporations to S-corporations may have to pay additional taxes because of differences in how inventories are valued under C- vs. S-corporation rules. Oregon allows these companies to subtract a portion of these additional taxes from Oregon taxable income after credits. Hence, companies taking the subtraction will see their tax rate on Oregon taxable income lowered as a result. Companies falling into one of these three categories may need to pay additional taxes, pushing up their effective tax rate on Oregon taxable income.

[28] Multistate Tax Commission, *Corporate Tax Sheltering and the Impact on State Corporate Income Tax Revenue Collections*, July 15, 2003.

[29] Bostek, Michael, *Internal Revenue Service: Challenges Remain in Combating Abusive Tax Shelters*. U.S. General Accounting Office, Testimony before the Committee on Finance, U.S. Senate, October 21, 2003. GAO-04-104T. Available at http://www.gao.gov/new.items/d04104t.pdf. The GAO changed its name in July 2004 from the General Accounting Office to the General Accountability Office.

[30] United States Department of the Treasury. *The Problem of Corporate Tax Shelters: Discussion, Analysis, and Legislative Proposals*, July 1999, pp. 25-31. Available at http://www.ustreas.gov/offices/tax-policy/library/ctswhite.pdf.

[31] Transactional Analysis Research Clearinghouse (TRAC), "Corporate Audit Rates – Wide Disparities Found for Different Industries," released on April 11, 2005. Currently available at http://trac.syr.edu/tracirs/latest/current/.

[32] David Burnham, Transactional Research Analysis Clearinghouse. Phone conversation with author, April 11, 2005.
[33] S-corporations in Oregon must pay the $10 minimum corporate income tax.
[34] All S-corporation shareholders must be U.S. residents and must be either individuals, estates, or certain trusts and exempt organizations For the latest Internal Revenue Service rules on S-corporation election, see http://www.irs.gov/pub/irs-pdf/i2553.pdf
[35] The federal Tax Reform Act of 1986 raised the statutory corporate income tax rate above the statutory personal income tax rate for the first time in the modern history of the income tax, encouraging smaller C-corporations to switch to S-corporations to lower their tax bills.
[36] Mazerov, Michael. "The Declining Trend in Corporate Taxes," Presentation to the Federation of Tax Administrators, Revenue Estimation/Tax Research Conference, September 30, 2002. Center on Budget and Policy Priorities.
[37] This analysis does not include those charges listed as "other" charges by the Census Bureau. According to Jane Moreland at the State Controller's Division, Oregon Department of Administrative Services, all or nearly all of these "other" charges are internal to the functioning of state and local government, collected when one agency charges another for services rendered. Hence, individual Oregonians and businesses do not pay these fees. Phone conversation with author April 6, 2005.
[38] The US Census Bureau, which collects the data used here, counts as fee revenue payments made to state and local hospitals by private insurance companies, patients without insurance, and Medicare. Payments made by Medicaid are not included, as they are considered by the Census Bureau to be transfers from the federal government, not fees for service.
[39] City of Portland Bureau of Environmental Services, *FY 2005 Sewer System Rate Study*, July 2004, p. 12. Available at http://www.portlandonline.com/shared/cfm/image.cfm?id=36070
[40] OCPP analysis of data sent by email to author from Dan Vizzini, City of Portland Bureau of Environmental Services, April 27, 2005. The difference may be due largely to businesses being more successful than homeowners at finding ways to conserve water use. Basic sanitary sewer charges, which account for about two-thirds of all sewer related revenue, have risen at roughly the same rate for homeowners and businesses over the last decade. Despite this, sanitary sewer revenue from residential customers grew 11.35 percent annually between 1995 and 2005 on average, while businesses saw annual growth averaging just 9.5 percent. The other major set of sewer-related charges - stormwater management charges - have risen somewhat more quickly for businesses. Between 1990 and 2005, stormwater management charges in Portland rose $3.76 per 1,000 square foot per month for residential customers and $4.28 for businesses.

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