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EXECUTIVE SUMMARY

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The QPAI Deduction in HB 2542-A:
A tax break for out-of-state investment and accounting gimmicks

by Michael Leachman and Charles Sheketoff

The American Jobs Creation Act of 2004 included the largest single tax cut for corporate America in years, a new deduction for "qualified production activities income," or QPAI. Under current law, the Legislative Assembly must choose to "connect" to this tax break before companies can use it. In early April, the House voted to allow the QPAI deduction as part of HB 2542-A.

- If Oregon connects to it, the QPAI deduction will cost the state $18.6 million in the upcoming 2005-07 budget cycle. In 2011-13, the first budget cycle in which the deduction will be fully phased-in at the federal level, the cost to Oregon will total $54.3 million.
- Fourteen states and the District of Columbia have already decoupled from the QPAI deduction.
- If Oregon connects to the QPAI tax cut, companies would get the full benefit of the QPAI deduction regardless of where in the U.S. their production occurs.
- Many corporations with major production facilities in Oregon will not benefit much from the QPAI deduction because Oregon is already eliminating or nearly eliminating their corporate income taxes through a previously enacted tax cut.
- Companies can increase their benefit from the QPAI deduction simply by changing their accounting practices.
- The Internal Revenue Service says QPAI will produce "a significant increase in controversies between taxpayers. This will increase the number of IRS appeals cases and litigated tax cases." If Oregon passes the QPAI deduction, the state may become similarly embroiled in related legal battles at taxpayer expense.
- The Internal Revenue Service says, "Many businesses, particularly small businesses, will find it difficult to understand and comply with these complex new [QPAI] rules . . . ."
- Corporate lobbyists sell the QPAI deduction as a tax break to make up for the loss of an illegal export subsidy Oregon must eliminate. In truth, the QPAI deduction reduces taxes for a grab-bag of businesses, not just exporters. The QPAI deduction will cost almost twice as much as eliminating the illegal export subsidy in the upcoming 2005-07 budget cycle.
- Staying disconnected from the QPAI deduction would require simple majority votes.
- If the Legislative Assembly wants to pass a tax cut to improve Oregon's economy, it would be wiser to expand Oregon's Earned Income Credit (EIC) than to offer the QPAI deduction.