Executive Summary
April 14, 2006

The Great Corporate Tax Shift:
Undercutting Oregon's Economy and Quality of Life

by Michael Leachman

This tax day, ordinary Oregonians are paying more than their share of taxes because corporations are paying less.

Over the last generation, Oregon has shifted income taxes away from large multi-state corporations at the expense of Oregon families and small businesses.

- In the next budget cycle (2007-09), corporations will pay just 4.5 percent of Oregon's income taxes, while personal income taxpayers will pay 95.5 percent. In the 1973-75 budget cycle, corporations paid 18.5 percent of all income taxes. In the current 2005-07 biennium, corporations are expected to pay 6.3 percent of Oregon's income taxes, while personal income taxpayers will pay 93.7 percent.

- Over the current decade, as corporate income taxes are projected to fall by $24 million, personal income tax revenues are projected to grow another $4.6 billion.

- The decline in corporate income taxes is primarily because Oregon gives corporations numerous tax breaks and because corporations are employing abusive tax shelters that lawmakers never enacted or intended to allow. Multi-state corporations have increasingly dominated Oregon's corporate income tax base and are the primary beneficiaries of the income tax decline.

Oregon has shifted property taxes away from business property, including property owned by large corporations, and onto Oregon homeowners.

- A generation ago, in 1978-79, households paid 50 percent of all property taxes in Oregon. Businesses paid the other half. In 2003-04, households paid 60 percent of property taxes, compared to 40 percent for businesses.

- The difference is costly to Oregon homeowners. If households still paid half of total property taxes, instead of 60 percent, they would have saved nearly $500 million in 2004 alone.

- The shift in property taxes away from business property and toward households is primarily the result of Measure 50 - a property tax cut passed in 1997. Measure 50 disconnected property taxes from real property values at a time when business property values were lagging behind residential property values.

Oregon's future – our economic strength and quality of life – depends upon critical public investments in schools and universities, roads, health care coverage, worker training, parks, and the court system. These investments make good business sense for companies that value Oregon as a place to do business in the future. Over the last generation, the taxes that fund these investments have shifted too heavily to households. Unless Oregon restores a fairer tax balance between corporations and families, the Great Corporate Tax Shift will continue to exacerbate Oregon's fiscal problems and undermine Oregon's future economic strength and quality of life.

The Great Corporate Tax Shift:
Undercutting Oregon's Economy and Quality of Life

By Michael Leachman

This tax day, ordinary Oregonians are paying more than their share of taxes because corporations are paying less. Over the last generation, Oregon has shifted income taxes away from large multi-state corporations at the expense of Oregon families and small businesses. In addition, Oregon has shifted property taxes away from business property, including property owned by large corporations, and onto Oregon homeowners. It's no wonder if Oregonians are cranky this tax day; they are victims of the Great Corporate Tax Shift.

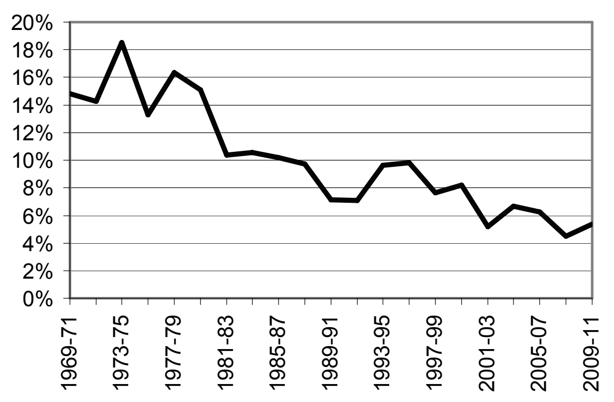
The decline in corporate income taxes is primarily because Oregon gives corporations numerous tax breaks and because corporations are employing abusive tax shelters that lawmakers never enacted or intended to allow. Multi-state corporations have increasingly dominated Oregon's corporate income tax base.

The shift in property taxes away from business property and toward households is primarily the result of Measure 50 - a property tax cut passed in 1997. Measure 50 disconnected property taxes from real property values at a time when business property values were lagging behind residential property values.

Oregon's future – our economic strength and quality of life – depends upon critical public investments in schools and universities, roads, health care coverage, worker training, parks, and the court system. These investments make good business sense for companies that value Oregon as a place to do business in the future. Over the last generation, the taxes that fund these investments have shifted too heavily to households. Unless Oregon restores a fairer tax balance between corporations and families, the Great Corporate Tax Shift will continue to exacerbate Oregon's fiscal problems and undermine Oregon's future economic strength and quality of life.

Income taxes: Corporate share has eroded over last generation

Figure 1: 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, and data from March 2006 Economic & Revenue Forecast.

As both a share of the economy and as a share of the State's income taxes, corporate income tax collections have eroded over the last generation.

OCPP's analysis of the March 2006 Economic and Revenue Forecast reveals that corporations operating in Oregon will pay 72 percent less in state corporate income taxes as a share of the economy in the next budget cycle, 2007-09, than they did in the late 1970s.[1]

Corporations also pay a smaller portion of state income taxes today than they used to; and, as a result, individuals now carry a bigger share of the load. Oregon's state economist projects that corporations operating in Oregon will pay about $533 million in income taxes in the

2007-09 budget cycle. Personal income taxpayers, by contrast, will pay $11.3 billion.[2] In other words, corporations will pay just 4.5 percent of Oregon's income taxes, while personal income taxpayers will pay 95.5 percent.[3] This biennium corporations are expected to pay 6.3 percent of Oregon's income taxes, while personal income taxpayers will pay 93.7 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 averaged 15 percent. In the 1973-75 budget cycle, corporations paid 18.5 percent of all income taxes (Figure 1). The shift in income taxes to individual taxpayers, and away from corporations, is the first component of Oregon's Great Corporate Tax Shift.

Over the current decade, as corporate income taxes fall by $24 million, personal income tax revenues are projected to grow another $4.6 billion.

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 $24 million, personal income tax revenues are projected to grow another $4.6 billion.

Lower corporate taxes do not equal growth

Corporate tax 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.[4]

When making investment 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."[5]

The kicker will blow a hole in corporate income taxes in the next budget cycle

A projected corporate kicker tax credit will slash corporate income taxes in 2007 by 55 percent, which will exacerbate the problem of low corporate income taxes in 2007-09.[6]

The March 2006 Oregon Economic and Revenue Forecast predicts that when the current budget cycle ends in June 2007, unanticipated revenues will exceed the May 2005 forecast by more than two percent for both personal and corporate income taxes, triggering the kicker tax cut. While the final kicker amount (if any) will not be established until the September 2007 "close of session" forecast, the State's economists currently project that personal income tax kicker refund checks in November 2007 will total $460.5 million and corporate income tax kicker credits for 2007 will total $205.4 million.

In total, the two kickers are projected to cost $666 million. A recent OCPP issue brief, *Income Tax Kickers Disproportionately Benefit Multistate Corporations and Wealthy*

Oregonians, shows how the kicker tax cuts are distributed among corporations of different sizes and individuals of different income groups.[7]

The 55 percent corporate kicker projected for 2007 comes on the heels of a 36 percent corporate kicker for profitable companies against their 2005 income taxes. Valued at $101 million in the "close of session" forecast in September 2005, the State now estimates the 2005 corporate kicker credit will cost $133.5 million.[8] The cost of the 2005 kicker has increased, and may continue to increase, since companies are reporting higher-than-expected profits for the 2005 tax year.

Valued at $101 million in the "close of session" forecast in September 2005, the State now estimates the 2005 corporate kicker credit will cost $133.5 million.

The corporate kicker punches a deep hole in corporate income tax revenues, but the kicker is not the only cause of low corporate taxes in the next budget cycle. If the 2007 corporate kicker were eliminated, corporations would still pay just 6.1 percent of Oregon income taxes in 2007-09, about one-third of what they paid a generation ago.[9] Moreover, in the subsequent budget cycle, 2009-11, corporations are projected to pay just 5.4 percent of all state income taxes.

Single-sales factor – the silent robber baron

Certain multi-state corporations are paying much less in corporate income taxes today because Oregon has changed the way multi-state firms calculate their state income taxes.

Most states determine how much of the profits of multi-state corporations to tax using a formula that considers the share of a corporation's property, payroll, and sales located within the state. Prior to 1991, Oregon used a formula that equally weighted the three factors – property, payroll, and sales. In 1991, Oregon switched to a formula that "double-weighted" the sales factor. 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.

In 2001, Oregon began phasing in a "single-sales factor" formula. Under this formula, only in-state sales matter in determining how much of a company's profits are taxable in Oregon. The Legislative Assembly in 2005 cut short the phase-in process and fully implemented the single sales factor formula on July 1, 2005.

Companies with large portions of their property and payroll in Oregon, and few in-state sales, reaped and continue to reap, large cuts in their corporate income taxes because of the change to a single-sales factor formula. A hypothetical firm with 20 percent of its property and payroll in Oregon, and one percent of its sales, would see its annual taxes fall by more than 90 percent as a result of the formula change.[10]

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 hypothetical company with such an arrangement could apportion all or most of its sales to Nevada, leaving few or no sales to report in Oregon.[11] Since Nevada has no corporate income tax, and Oregon now bases 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 $10 minimum corporate income tax, the company would, however, have to pay $10 - roughly the cost of a single fourth-grade textbook - each year.

Other reasons for the corporate income tax decline

Tax breaks

In addition to the corporate kicker and the switch to a single-sales factor formula for computing the taxable income of multi-state firms, Oregon has created a number of new income tax breaks for corporations that have eroded the corporate tax system.

Of the 49 income tax breaks that Oregon specially offers corporations, 40 were created since 1980. More than half were created since 1995.

Corporations operating in Oregon enjoy a total of 101 different income tax credits and other tax loopholes that reduce corporate income tax liability. About half of these tax breaks (52) are contained in the federal corporate income tax code. Oregon chose to allow corporations operating in Oregon to receive these breaks on their state taxes as well. The other half (49) are tax breaks offered specially by the State of Oregon. Of the 49 income tax breaks that Oregon specially offers corporations, 40 were created since 1980. More than half were created since 1995.

Besides giving certain corporations tax breaks, Oregon gave all corporations a tax cut in 1987 by lowering the statutory corporate tax rate from 7.5 percent to 6.6 percent.

Tax shelters

Oregon's corporate income tax collections have also declined because corporations have become much more aggressive in pursuing abusive tax shelters through 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 to Oregon at between $66 million and $94 million for fiscal year 2001 alone.[12] This estimate includes revenue lost when companies shelter income overseas and when companies abuse loopholes in state corporate income tax laws.

Multi-state corporations are more capable than Oregon-only companies at sheltering profits from taxation by utilizing other states' tax laws to their advantage. Those multi-state corporations with overseas operations can also hide profits from Oregon taxation. Because multi-state corporations have grown more important to Oregon's corporate income tax base over at least the last 15 years. Oregon's income tax base has become more dependent on corporations that are more capable of sheltering profits from taxation.

New corporate forms

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. Oregon has seen strong growth in these "pass-through" entities, such as S-corporations and "limited liability companies" (LLCs).

Businesses choosing to incorporate must elect whether to be C-corporations or S-corporations for tax purposes. Both C- and S-corporations enjoy personal liability protection from the state, and access to corporate credits. S-corporations do not pay federal or state corporate income taxes.[13]

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.[14] Sales and profits are not criteria in determining corporate form, so some firms with large amounts of profits may still form as S-corporations.

Growth in S-corporations following federal law changes in 1986 may have somewhat reduced corporate income tax revenue coming from smaller companies, but C-corporations still collect the bulk of income reported by Oregon corporations.[15] C-corporations collected nearly three-fourths (73 percent) of all the income reported by Oregon corporations between 2001 and 2003, the most recent year for which data are available. The share of corporate income collected by C-corporations is about the same as it was in 1990 (when it was 74 percent). Hence, the growth in S-corporations since 1990 has not resulted in a notably higher share of corporate income collected by "pass through" S-corporations.

Limited liability companies, or 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 decline.

Some of the growth in LLCs is due to C-corporations forming subsidiaries as LLCs. 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.[16] Oregon corporations owning LLC subsidiaries pay corporate income taxes on income earned by these subsidiaries. Thus, the establishment of these corporate-owned LLC subsidiaries did not reduce Oregon's corporate income tax revenues.[17]

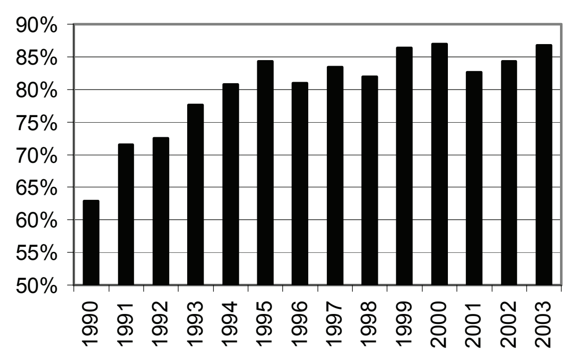
Multi-state corporations are the primary beneficiaries

Multi-state corporations are the primary beneficiaries of the declining corporate income tax because they collect most of the taxable profit.

Multi-state corporations are increasing their presence in Oregon, in part, because of consolidation in several industries. Between 1990 and 2003, the number of corporations operating solely in Oregon fell by 17 percent, while the number of multi-state corporations rose by 44 percent.[18]

Multi-state firms still make up only about a third of all Oregon corporations, but they collect an increasing share of the profit. In 1990, multi-state 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 economic downturn that began in 2001 temporarily pushed the percentage down, in 2003 the figure returned to 87 percent. The long-term trend is toward the increasing dominance of multi-state firms (Figure 2).

Figure 2: Percent of total corporate taxable income reported by multi-state corporations, Oregon



Source: OCPP analysis of Legislative Revenue Office data.

In 1990, multi-state companies collected 63 percent of all taxable profits reported in Oregon. Just a decade later in 2000, the figure had reached 87 percent.

With multi-state companies collecting 87 cents of every dollar of taxable profit reported in Oregon, state corporate income tax revenues will be healthy only if Oregon effectively taxes the profits of multi-state firms.

Most corporations pay the minimum corporate income tax

Oregon requires that all corporations operating in Oregon pay at least a minimum income tax of $10. Oregon first set the corporate minimum tax at $25 in 1929. It lowered it in 1931 to $10, where it remains today.[19]

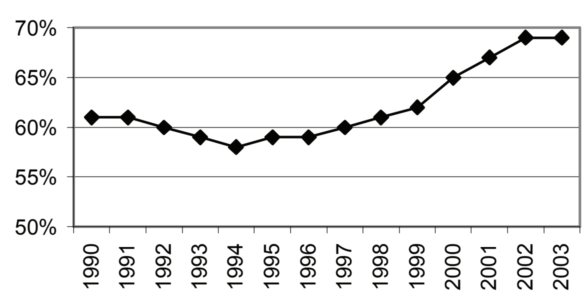
Corporations paying the $10 minimum claim no tax liability in Oregon, but this does not mean that these companies are failing businesses or have no profits. In fact, many corporations that are profitable pay the minimum tax. In 2003, the most recent year of available data, 69 percent of Oregon corporations paid the $10 minimum. Among corporations with Oregon sales over $25 million, 52 percent paid $10.[20]

The large majority of corporations paying $10 report zero or minimal profits, or report 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 that many profitable corporations reduce their tax bills by applying losses from prior years when determining tax liability in profitable future years. This is because Oregon allows corporations to carry prior year losses forward for 15 years. Of those companies paying $10 in 2003, 22 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 2003, a total of 235 profitable 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 of $10 tax has increased since the early 1990s.

Figure 3: Percentage of C-corporations paying Oregon's $10 minimum corporate income tax



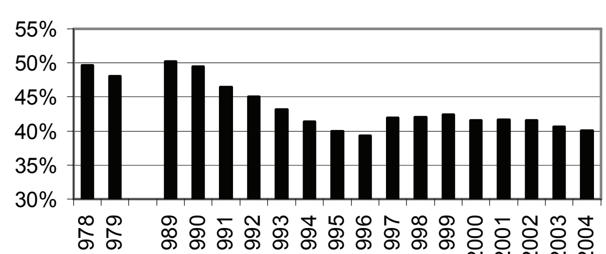
Source: OCPP analysis of Legislative Revenue Office data.

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 in 2002 and 2003 (Figure 3).

Property taxes: Businesses benefited more than individuals from the 1990s tax cuts

In 1978-79, households paid 50 percent of all property taxes in Oregon. Businesses paid the other half. In 2003-04, households paid 60 percent of property taxes, compared to 40 percent for businesses.

Figure 4: Share of property taxes paid by businesses in Oregon



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

After income taxes, local property taxes are Oregon's second largest source of tax revenue.[21] Unfortunately for Oregon families, businesses are not only paying a smaller share of state income taxes, they are also paying a smaller share of local property taxes. The shift in property taxes to households is the second component of Oregon's Great Corporate Tax Shift.

A generation ago, in 1978-79, households paid 50 percent of all property taxes in Oregon. Businesses paid the other half.[22] In 2003-04, households paid 60 percent of property taxes, compared to 40 percent for businesses (Figure 4). The difference is costly to Oregon homeowners. If households still paid half of property taxes, instead of 60 percent, they would have saved nearly $500 million in 2004 alone. That savings, instead, has gone to Oregon businesses, including large corporations who own property here.

The property tax shift happened in the early 1990s

Between 1990-91 and 1994-95, the real market value of homes in Oregon rose by 85 percent, more than twice as fast as industrial and commercial property.

The property tax shift to households occurred in the first half of the 1990s following Oregon's passage of Measure 5, a ballot measure that sharply reduced property tax rates. During this time, residential property values rose much more quickly than business property values. Between 1990-91 and 1994-95, the real market value of homes (including tract and mobile homes) in Oregon rose by 85 percent, more than twice as fast as industrial and commercial property (including multi-family housing), which rose by just 34 percent.

The rapid rise in single-family home values in the early 1990s resulted from strong population growth. Between 1990 and 1995, Oregon's population grew well over two percent annually, more than double the rate of growth during all other years between 1980 and 2005.[23] An economic slowdown in California in the early 1990s, combined with Oregon's relatively cheap housing market coming out of the economically difficult 1980s, helped fuel the early 1990s' home price boom.

Business property values did not grow as rapidly as home values during the first half of the 1990s for a combination of reasons. First, commercial property values slowed following a period of strong growth during the 1980s. Between fiscal years 1978-79 and 1990-91, commercial property values in Oregon rose 14 percent a year on average, while residential property values grew just 10 percent a year. It may be that commercial property values in the 1980s were catching up with Oregon's strong population growth during the 1970s, as businesses took advantage of the new market opportunities created by population growth. Also, the severe economic downturn that hit Oregon in the early 1980s may have hampered residential price growth more than commercial growth.

In addition, over the last generation, Oregon's manufacturing and timber-related industries have declined, and job growth has been concentrated in the services and retail business sectors. As a result, industrial properties are now a smaller share of Oregon's property tax base. In 1978-79, industrial properties accounted for nearly 12 percent of Oregon's real market property value. By 1990-91, industrial property totaled just eight percent of Oregon's property tax base. While the pace of growth in industrial property values picked up in the early and mid-1990s compared to the sluggish 1980s, the improvement was not enough for industrial property values to keep pace with gains enjoyed by other types of property. In 1996-97, industrial property values equaled just six percent of total taxable property value in Oregon, making it only about half as important to Oregon's tax base as it had been a generation earlier.

Measure 50 locked in the shift

Two property tax cuts passed during the 1990s – Measures 5 and 50 – have slashed Oregon property taxes and harshly squeezed the State's capacity to invest in its education system and other public services. The tax cuts, moreover, have delivered more of their benefits to businesses operating in Oregon – including large corporations doing business here – than to Oregon homeowners.

In November 1990, Oregon passed Measure 5, capping property tax rates. The measure phased in over five years a cap of $15 for every $1,000 in property value. It also established that property taxes generally would fall into one of two categories – those dedicated to schools and those dedicated to other government operations. Taxes for schools were capped at $5 for every $1,000 in property value, or a 0.5 percent rate, and taxes for other government operations were capped at $10 for every $1,000 in property value, or a one percent rate. Rates were reduced incrementally beginning in fiscal year 1991-92 until the full reduction was reached in 1995-96.

The rate cuts imposed by Measure 5 were sharp. On July 1, 1991, the first day under Measure 5, the average property tax rate in Oregon was $22.74 per $1,000 of value, significantly higher than the total allowed rate of $15 per $1,000 of value imposed by Measure 5 when fully phased in.[24]

Despite the sharp rate cuts, residential property taxes in Oregon rose in the years after Measure 5 passed. The early and mid-1990s boom in home values was so strong that much of the impact of Measure 5 was hidden from homeowners. Aggregate property taxes on residential properties still rose by about eight percent between 1991 – when Measure 5 passed – and 1996.

With some voters upset that their property taxes had increased despite the passage of Measure 5, Oregonians passed another property tax cut in November 1996, Measure 47. Subsequently, the Legislative Assembly referred to voters a substitute measure that cleaned up some drafting errors in Measure 47. Voters passed this legislative referral, Measure 50, in May 1997.

Measure 50 established that property taxes are based not on market value, but on assessed value (the value as determined by government property assessors), and then forced cuts in assessed values, thereby decreasing taxes. The measure set the maximum assessed value of property for the 1997-98 fiscal year at 90 percent of real market value in 1995-96 and then capped the growth in maximum assessed value to three percent per year.

Measure 50 locked into place the shift in property taxes from businesses to households that occurred in the first half of the 1990s. Measure 50 disconnected property taxes from real property values at a propitious moment in history for business because business property values were lagging behind residential property

The surge in residential property values slowed during the second half of the 1990s. The median home price of existing single-family homes in the Portland area grew by ten percent a year between 1990 and 1996, but by just five percent a year – half as fast – between 1996 and 1999, and then slowed even further between 1999 and 2001.[25]

Data from Multnomah County shows that commercial and industrial real market property values rose more quickly than residential real market values in the years after Measure 50 locked in lower rates for businesses.

Data from Multnomah County shows that commercial and industrial real market property values rose more quickly than residential real market values in the years after Measure 50 locked in lower rates for businesses. In 1998, commercial and industrial property values in Multnomah County rose twice as fast as residential property values. Data for 1999 are not available, but in 2000 and 2001 commercial and industrial values exploded, rising 40 percent while residential values rose just 11 percent.[26] The available statewide data have not been evaluated by the Oregon Department of Revenue for accuracy, but suggest that in the State as a whole commercial property values also rose more quickly than residential values between 1996 and 2001.[27] If Oregon had not passed Measure 50 when it did, surging business property values could have reversed the property tax shift, leaving businesses and households paying closer to the same share of property taxes they paid a generation ago.

Measure 5 and 50 combined slashed business taxes by 65 percent

The combined effects of Measure 5 and Measure 50 have produced sharply lower property taxes in Oregon for both homeowners and business property owners. If Oregon still taxed the real market value of property at 1990's average statewide tax rate (as if Measures 5 and 50 had not passed) total property tax collections would have been $5 billion more than they actually were in fiscal year 2004-05 alone. Cumulatively, since the passage of Measure 5, local governments have lost nearly $41 billion since 1990-91 because of the changes wrought by Measures 5 and 50.

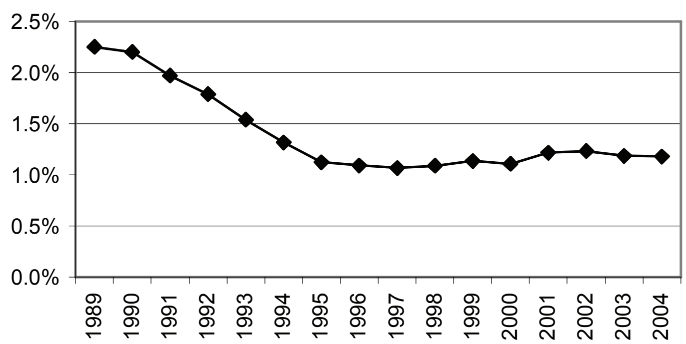
Businesses have benefited more than households from these tax cuts. If Oregon still taxed real property values at the average statewide 1990 tax rate, and if businesses still paid the same share of property taxes they paid in 1990-91, businesses would have paid $2.8 billion more in property taxes than they did in 2003-04. Households, by contrast, would be paying $2.2 billion more.

In other words, property taxes on businesses have fallen more than property taxes on households since Measure 5 passed in 1991. Property taxes on business properties are 65 percent lower than they would have been without the tax shift and Measures 5 and 50. Property taxes on residences, by contrast, are 49 percent lower.

Oregon's economy boomed during the 1990s, but taxes on business property fell. Despite the economic growth of the 1990s and all the associated new construction and renovation, Oregon business owners cumulatively did not pay as much in property taxes as they did in 1990-91 until over a decade later, in 2001-02, even without adjusting for inflation or economic growth.[28]

As a share of the economy, business property taxes plummeted in the early 1990s and have remained low ever since. Taxes paid on business property fell from 2.2 percent of Gross State Product in 1990-91 to 1.2 percent in 2004-05, a decline of 46 percent (Figure 5).

Figure 5: Property taxes on business property, as a share of Gross State Product



Source: OCPP analysis of Oregon Dept. of Revenue and Bureau of Economic Analysis data.

Taxes paid on business property fell from 2.2 percent of Gross State Product in 1990-91 to 1.2 percent in 2004-05, a decline of 46 percent.

Strategic Investment Program further cuts property taxes

Another reason why property taxes on business property dropped in the 1990s was the adoption of the Strategic Investment Program (SIP) in 1993. The SIP property tax cut exempts for 15 years new investment valued at over $100 million if the project is located in a metropolitan area, or $25 million if it is located in a rural area.[29] Firms pay an annual fee equal to 25 percent of the property tax that would otherwise have been due. The fee cannot exceed $2 million in metropolitan areas, or $50,000 in rural areas.[30]

Since the SIP was created in 1993, only seven SIP tax breaks have been granted. Washington County has given four SIP tax breaks to Intel. Three other companies have each received one SIP break. All seven SIP tax breaks were given by either Washington County or Multnomah County. In the current 2005-07 budget cycle, the SIP will reduce property taxes to these two counties by about $159 million.[31]

In 2005, Washington County approved the most recent SIP tax break, which will reduce Intel's property taxes in future years, beginning as soon as 2008 and as late as 2013. The tax break will reduce Intel's property taxes to Washington County by $579 million over the 15-year life of the SIP.

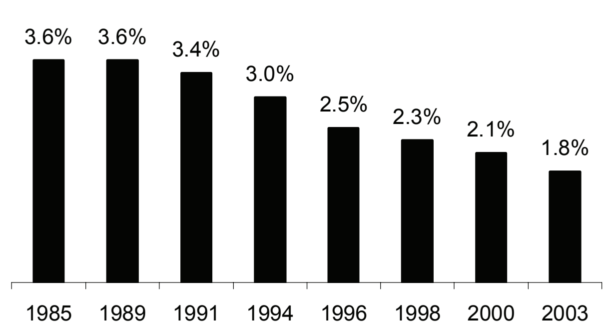
Intel apparently convinced county officials that the tax break was necessary to ensure the company would continue to invest in its Washington County campus. It is unlikely, though, that the tax cut made a difference to Intel's investment decisions. The property taxes Intel saved from the SIP tax cut amount to only about one-tenth of one percent of their annual expenses. Plus, Intel is now paying very little in corporate income taxes to Oregon because the company was a major beneficiary of Oregon's switch to a "single-sales factor" formula for apportioning the profits of multi-state firms (see page 3), and Oregon's expansion of a corporate tax credit for research and development expenses. For Intel, the SIP tax cut was probably just icing on a cake the company was already planning to bake.

Oregon business taxes are low compared to other states

Some policy makers and others believe comparisons with other states are useful. While cross-state rankings are interesting trivia, they do not allow Oregonians to determine whether Oregon's level of spending is desirable or affordable. Oregon's ability to afford state and local government spending is dependent upon the income of Oregonians, not the standards that residents of other states set for their own public goods and services. The fact that your neighbor does not mow his own lawn does not mean that you cannot afford to mow your own.

In 1985, businesses in Oregon paid 3.6 percent of Gross State Product in taxes. By 2003, taxes paid by Oregon businesses totaled just 1.8 percent of GSP.

Figure 6: Total taxes on Oregon businesses as percent of Gross State Product



Source: Utah State Tax Commission

One reason that tax and spending rankings matter little in policy debates is that they ignore important differences in the circumstances and the ways that different states approach policy issues. Oregon has seaports, Kansas doesn't. Oregon enacted a "tough on crime" Measure 11, other states didn't.

That said, recent studies that have considered a broad array of state and local taxes have found that Oregon business taxes are low and are declining.

According to a study by the Utah State Tax Commission, total business taxes in Oregon as a share of the economy have been cut by half since 1985.[32] 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 6).

The Utah study also found that Oregon has the lowest business taxes as a share of Gross State Product of the seven Western states examined. 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. [33]

A study written by the accounting firm Ernst & Young and published by the Council on State Taxation (COST) found that in 2005 state and local taxes on businesses as a share of private-sector economic activity in Oregon was the 48th lowest in the nation, among the states and the District of Columbia. As a share of all state and local taxes, business taxes in Oregon ranked 50th among the states and the District of Columbia.[34] COST is an association of over 500 multi-state 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.

Conclusion

As Oregon has lowered taxes for corporations, Oregonians and their families have picked up more of the tab. Those Oregonians most reliant on public services, including schoolchildren and their families, university students, laid-off workers and others lacking health insurance, and seniors in nursing homes, have paid dearly through cuts to the quality and availability of services.

Compared to a generation ago, Oregon households are paying a larger share of income taxes as corporations have grown more aggressive about sheltering profits from taxation and as corporations won from Oregon governors and legislators a number of tax cuts.

Oregon households are also paying a larger share of property taxes than they were a generation ago because Measure 50 locked in lower property taxes for business property relative to residential property.

Hence, both of Oregon's two largest sources of tax revenue have shifted more onto the backs of Oregon households. Oregonians have fallen victim to the Great Corporate Tax Shift.

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Endnotes:

1 This budget period, even with greater than anticipated profits and taxes, corporations are expected to pay 58 percent less in income taxes as a share of the economy than they did in the late 1970s. Their income taxes as a share of the economy will fall to 72 percent less than late 1970s levels in the next biennium because corporations are currently expected to receive a $205 million kicker tax credit in the 2007 tax year. See Oregon Stuck in Doonesbury (http://www.ocpp.org/cgi-bin/display.cgi?page=iss060405doonesb) and Income Tax Kickers Disproportionately Benefit Multistate Corporations and Wealthy Oregonians (http://www.ocpp.org/cgi-bin/display.cgi?page=issue060328kick).

2 State of Oregon Office of Economic Analysis, Oregon Economic and Revenue Forecast, March 2006, Volume XXVI, No. 1. Available at http://www.oea.das.state.or.us/DAS/OEA/docs/economic/forecast0306.pdf.

3 In 2007-09 corporate income taxes as a share of all income taxes will return to less than five percent. The increase to slightly above 6 percent this biennium (2005-07) is temporary and wiped out by the corporate kicker. The projection for 2009-11 is 5.4 percent.

4 Lynch, Robert. Rethinking Growth Strategies: How State and Local Taxes and Services Affect Economic Development. 2004. Economic Policy Institute, p. 4-6.

5 Ibid, p. vii.

6 Email to author from Michael Kennedy, Oregon Office of Economic Analysis, March 7, 2006.

7 Available at http://www.ocpp.org/2006/issue060328%20kicker.pdf.

8 Oregon Office of Economic Analysis, Oregon Economic and Revenue Forecast, March 2006, Appendix B, Table B-3, p. 87.

9 This assumes the personal income tax kicker is not also suspended. If both 2005-07 kickers are suspended, corporations will pay just 5.9 percent of Oregon income taxes (based on the March 2006 Economic & Revenue Forecast).

10 Oregon is about one percent of the national economy. Thus, a multi-state corporation with nationwide sales on average sells one percent of is products or services in Oregon.

11 Oregon Revised Statutes 314.665, sections 2(a) and 2(b), and section 4.

12 Multistate Tax Commission, Corporate Tax Sheltering and the Impact on State Corporate Income Tax Revenue Collections, July 15, 2003.

13 S-corporations in Oregon must pay the $10 minimum corporate income tax.

14 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.

15 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.

16 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.

17 Corporations sometimes form LLCs as part of a strategy to hide profits from state income taxation. The impact of such tax sheltering is less in states (including Oregon) that require "combined reporting" of multi-state corporations. Under "combined reporting" all related corporate

entities that operate as a single business enterprise are essentially treated as one taxpayer for apportioning the profits of multi-state firms. See Fox, William and LeAnn Luna, Does the Advent of LLCs Explain Declining State Corporate Tax Revenues? Unpublished working paper, University of Tennessee, January 16, 2003. This paper finds that LLC growth, primarily driven by corporations seeking to hide profits from taxation, is responsible for as much as one-third of the decline in state corporate income taxes nationally, but also finds that combined reporting can offset nearly half (44 percent) of the revenue losses associated with LLC growth.

18 Legislative Revenue Office, 2006 Oregon Public Finance: Basic Facts, February 24, 2006, p. C13.

19 The 2003 Legislature tried to change the corporate minimum tax as part of an omnibus tax measure that was ultimately referred to the ballot by citizens as Measure 30 in 2004 and rejected by the voters.

20 OCPP analysis of data from Legislative Revenue Office, 2006 Oregon Public Finance: Basic Facts, Research Report #1-06, February 24, 2006, p. C-18.

21 According to the Legislative Revenue Office, Oregon collected $4.7 billion in personal income taxes and $3.8 billion in local property taxes in fiscal year 2004-05. The next largest source of revenue, Unemployment Insurance taxes, totaled $727 million in 2004-05. Legislative Revenue Office, 2006 Oregon Public Finance: Basic Facts, February 24, 2006, p. A4.

22 The OCPP followed a method of dividing business and household property taxes employed by the Governor's Tax Review Technical Advisory Committee in its Review of Oregon's Tax System, released in June 1988. This method includes the following classes of property as business property: industrial, commercial (including multi-housing), farm, forest, personal business, utility, recreational, and "other" property. The Council on State Taxation appears to have used a similar method in its report, Total State and Local Business Taxes, released in March 2006. If farm, forest, recreational, and "other" property are not included as business properties, but instead placed in an "other" category (not household or business), the trend in business property taxation still holds. Business property defined as only commercial, industrial, personal business, and utility property declines from 41 percent to 31 percent of the property tax base between 1978-79 and 2004-05.

23 OCPP analysis of population data in the March 2006 Economic and Revenue Forecast.

24 Legislative Revenue Office, 2006 Oregon Public Finance: Basic Facts, February 24, 2006, p. D4.

25 See Thompson, Jeff and Michael Leachman, Boom, Bust, and Beyond: The State of Working Oregon 2002, Oregon Center for Public Policy, October 2002, p. 98. Available at http://www.ocpp.org/2002/nr021103.htm.

26 OCPP analysis of data emailed to author by John Riles, Multnomah County Division of Assessment and Taxation, April 7, 2006. Data for 1999 are not available due to a change in how the county counted property values in Urban Renewal areas. Between 2001 and 2005, residential property values in Multnomah County grew twice as fast as commercial and industrial property values.

27 The statewide data are compiled by the Oregon Department of Revenue from reports sent from the counties. The data have not been evaluated by ODR for accuracy, and therefore are not fully reliable. According to the data, real market commercial property values rose 87 percent between 1996 and 2001, close to three times as fast as real market residential property values, which rose 31 percent. While the data have not been evaluated for accuracy by ODR, it is unlikely that any county reporting errors were not large enough to change the overall story (supported by the data from Multnomah County) that the growth in commercial values outpaced the growth in residential values in the years immediately following Measure 5's passage.

28 OCPP estimates that business property owners paid $1.26 billion in property taxes in 1990-91, and did not exceed that level until 2001-02, when business property owners paid $1.36 billion in property taxes.

29 Oregon Revised Statutes 307.123 and 285C.606, section 1(c).

30 Additional fees may be negotiated. Oregon Revised Statutes 285C.609, section 4(b).

31 Oregon Department of Revenue and Oregon Department of Administrative Services, State of Oregon 2005-2007 Tax Expenditure Report, pp. 266-67.

32 Macdonald, Douglas Aird. Western States' Tax Burdens, Fiscal Year 2002-2003. Economic and Statistical Unit, Utah State Tax Commission. Research Publication 2003-31. February 3, 2004. Available at http://tax.utah.gov/esu/burdens/WTB_2003.pdf. The Utah study focuses on the initial incidence of taxes (i.e. who gets the bill). Because individuals own, manage, operate and patronize businesses, individuals ultimately pay all taxes. Just which individuals ultimately pay for business taxes varies by circumstance. Shareholders may pay in the form of lower share prices; corporate executives may pay in the form of smaller compensation packages; line workers may pay in the form of reduced pay or benefits; and/or customers may pay in the form of higher prices.

33 The seven states included in the study were Oregon, Utah, Colorado, California, Arizona, Idaho, and Washington.

34 Cline, Robert, et. al., Total State and Local Business Taxes, Council On State Taxation, March 2006. The COST study emphasizes that state and local business taxes nationally rose more quickly than total state and local taxes between 2002 and 2005. The COST study focuses on the initial incidence of taxes (i.e. who gets the bill). Because individuals own, manage, operate and patronize businesses, individuals ultimately pay all taxes. Just which individuals ultimately pay for business taxes varies by circumstance. Shareholders may pay in the form of lower share prices; corporate executives may pay in the form of smaller compensation packages; line workers may pay in the form of reduced pay or benefits; and/or customers may pay in the form of higher prices.