REVENUE IMPACT OF PROPOSED LEGISLATION

74th Oregon Legislative Assembly
2007 Regular Session
Legislative Revenue Office

Bill Number:	SB 179-A
Revenue Area:	Income
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Date:	5-31-2007

Measure Description:

Allows insurance companies to petition the Department of Revenue, and authorizes the department, to use a modified apportionment formula if the current formula does not produce a fair and equitable apportionment of income. Allows potential modifications to include the exclusion of any one or more factors, the inclusion of one or more additional factors, the inclusion of reinsurance premiums in the insurance sales factor, or any other method to achieve a fair and equitable apportionment of the taxpayer's income. Defines "total net income received from real property" for purposes of the real estate income and interest factor. Changes the apportionment formula for insurance companies from an equally weighted three factor formula to a single factor formula based on insurance sales beginning with tax year 2007.

Revenue Impact:

($ Millions)	2007-08	2008-09	2007-09 Biennium	2009-11 Biennium
General Fund	**$0.8**	**$0.6**	**$1.4**	**$1.5**
Insurers Headquartered in Oregon				
Excise Tax	-$2.2	-$2.1	-$4.3	-$4.4
Insurers Headquartered Elsewhere				
Excise Tax	$9.5	$9.2	$18.7	$19.3
Retaliatory Tax	-$6.5	-$6.5	-$13.1	-$13.4

Impact Explanation:

Current law requires multi-state insurance companies to apportion their income to Oregon according to an equally weighted 3-factor formula consisting of real estate income and interest, wages and salaries, and insurance sales. Current law also requires that if one or more of the factors does not exist, then it is to be removed from the formula. This revenue impact is an estimate of the difference between current law and the use of the single sales factor formula.

In general, the impact on individual companies depends on their specific characteristics such how much of their sales and operations are inside Oregon or in other states. Another significant factor that would determine the affect of the proposed policy on specific taxpayers is whether they are domestic (headquartered in Oregon) or foreign (headquartered outside Oregon). Foreign insurers are subject to Oregon's retaliatory tax while domestic insurers are not.

Domestic insurers that operate only in Oregon would not be affected by the policy change. The impact on those that operate in multiple states would depend on the difference between their sales factor and other factors. For example, if a company has a sales factor of 45% and a 3-factor apportionment percentage of 55%, then the proposed law would result in a tax reduction.

In contrast, if a company has a sales factor of 45% and a 3-factor apportionment percentage of 35%, the bill would lead to a tax increase for the company. In aggregate, domestic insurers are expected to have a reduction in excise tax liability by using a single sales factor. This tax reduction is shown in the table contained in this statement.

The impact on foreign insurers is complicated by the interaction between the excise tax and the retaliatory tax. Insurers whose excise tax would increase under a single sales factor would likely experience a reduction in their retaliatory tax, up to a dollar-for-dollar reduction. Similarly, insurers whose tax liability would decrease under a single sales factor would experience a similar increase in their retaliatory tax. An analysis of each foreign insurer for tax years 2002-2004 revealed that, on average, only 70% of the aggregate increase in excise taxes was offset by a reduction in aggregate retaliatory taxes.

An additional complicating factor is the distribution of tax liability among the roughly 1,100 insurance companies that are subject to both the excise tax and the retaliatory tax. Most companies (roughly 80%) are unaffected by the proposed policy; the aggregate impact is driven by the remaining 20% of insurers. Historical simulations of the proposed policy for tax years 2002-2004 resulted in two years with a net total increase in taxes and one year with a net total decrease in taxes. In each year the magnitude of the impact was significantly affected by just a few companies.

The concentration among taxpayers who experienced a reduction in taxes was greater than among taxpayers who experienced an increase in taxes. One consequence of this kind of distribution is that the performance of very few companies can have a disproportionate impact on the revenue stream. An analysis of the policy impact controlling for the outliers revealed that the impact remained slightly positive. While in any given year the revenue impact may be positive or negative, the analyzed data suggest that the long-term average revenue impact to be slightly positive.