2023 Session
Legislative Revenue Office
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Corporate Income Apportionment in Oregon

Background

When a corporation operates in multiple states, the U.S. Constitution allows a tax on income that is "fairly apportioned" to the state. It is generally not possible to know exactly what part of its profit comes from any one state. Each of the 44 states that tax corporate net income uses a formula to estimate the amount of income attributable to the state and subject to the state's tax.

Not all income is divided among states using the apportionment formula. The income that is apportioned using the apportionment formula is income that is generated by or for the corporation's trade or business, if the income is not from the trade or business it is allocated to a specific state[1].

General Apportionment Formula

For apportionable income, Oregon uses a "single sales factor" apportionment formula.

$$Apportioment\ Percent = \frac{Oregon\ Sales}{Everywhere\ Sales}$$

Almost 30 states use single sales factor apportionment in 2023. The remaining states with corporate income taxes use three factors, adding property and payroll factors to the sales factor. Some states take the simple average of the three factors, while others give extra weight to the sales factor. Oregon adopted the single sales factor apportionment method in 2005, as many states were moving toward giving the sales factor extra weight.

Throwback Sales and 100% Taxability

The goal of apportionment as adopted by most states is to divide 100 percent of income among states that have jurisdiction to tax the income. Generally, states have jurisdiction to tax income if there is a substantial connection between the corporation and the state (known as nexus)[2].

Oregon has a "throwback rule" for sales of tangible personal property[3] that intends to move income from

[1] See Oregon Administrative Rule 150-314-0335 for details and examples.
[2]The requirement for substantial nexus between a state and business to exist before a state can impose a tax on the business is primarily contained in the US Constitution. There is also one federal law limiting state's ability to tax net income of a business that otherwise has nexus with the state is Public Law 86-272. Passed in 1959, the law prohibits states from imposing an income tax on sales of tangible goods in the state if the only activity of the business in the state is soliciting sales of tangible personal property.
[3] The provision is part of the Uniform Division of Income for Tax Purposes Act (UDITPA). For Oregon, the

states without taxing jurisdiction back to states that do have jurisdiction. The throwback rule adds sales to the numerator of the apportionment formula in two circumstances where the income would not be taxable at its destination. The first category of throwback sales is product shipped from Oregon into a destination state that does not have jurisdiction to tax the seller. The second category is product shipped from Oregon to the United States government.

$$Apportioment\ Percent = \frac{Sales\ in\ Oregon + Throwback\ Sales}{Everywhere\ Sales}$$

The effect of a throwback rule is to increase the apportionment percent by increasing the numerator of the apportionment formula. An alternate approach, known as a "throwout rule" reduces the denominator by removing the throwback sales. For tangible property sales, twenty-two states currently have a throwback rule, and three states have a throwout rule.

Note that the goal of the throwback rule in apportionment is not to ensure 100 percent of a corporation's income is taxed, it is to ensure 100 percent is *taxable*. So, whether a state imposes a corporate income tax or not does not affect the calculation of throwback sales. That is, if a state could tax a corporation's income sales into that state are not thrown back even if the state does not impose a corporate income tax.

The division of income also will not be exactly 100% if a corporation is taxed in states with differing apportionment formulas, which could result in over or under-apportionment.

Unitary Combined Reporting Sales Factor (Joyce and Finnigan)

Corporations that include multiple affiliated corporations in a consolidated federal tax return must file a consolidated Oregon tax return as well. Apportioning earnings of a unitary group where some members have nexus and others don't introduces complexity as to which sales by group members should be included in the apportionment formula. There are two methods described in decisions by the California Board of Equalization, known as the Joyce method and the Finnigan method.

Under a Joyce method, only the sales of group members with nexus are included in the numerator of the sales factor. That is, under a Joyce method the decision is made for each individual group member. The Finnigan method is to include the sales of all group members in the numerator of the sales factor if any one member has nexus, essentially treating the group as a single taxpayer.

Oregon uses the Joyce method, which is used by about two-thirds of states that require combined reporting.

UDITPA statutes are ORS 314.605 through 314.675, and the throwback rule is ORS 314.665.