1.001 SCHOLARSHIP AND FELLOWSHIP INCOME

Internal Revenue Code Section: 117
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$5,900,000	$5,900,000
1999–01 Revenue Impact:	Not Applicable	$6,700,000	$6,700,000

DESCRIPTION: Scholarships and fellowships are excluded from personal taxable income to the extent that they cover tuition and course-related expenses of individuals who are candidates for degrees.

PURPOSE: Originally, grants were included in gross income unless it could be proven that the money was a gift. This provision was enacted to clarify the status of grants to students and provide equitable treatment among taxpayers. It has also been defended on the grounds that it reduces the cost of higher education.

WHO BENEFITS: Individuals receiving scholarship or fellowship income, or reduced tuition. Students attending private schools benefit the most because tuition and course-related fees are likely to be greater than at public schools.

EVALUATION: This tax expenditure achieves its purpose as well as reducing the cost of higher education for students receiving these grants. This provision allows the maximum use of these funds to go toward direct educational costs, rather than having some of the funds collected by the government and used to fund other programs. It keeps more money available for these students and facilitates the recipients' opportunity to successfully complete their education with minimal debt or need for extending the time in school. The economic and societal returns on the investment in higher education are very high. Aside from the benefits of a well-educated population, increasing levels of education ultimately lead to increasing levels of income. These incomes result in a growing national tax base which, in turn, generates increasing levels of government revenue.

It is a fiscally effective method of achieving its purpose. Controlling costs has become increasingly important as tuition rates have exceeded the rate of inflation in recent years. [*Evaluated by the System of Higher Education.*]

1.002 INTEREST ON EDUCATION SAVINGS BONDS

Internal Revenue Code Section: 135
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1988

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$100,000	$100,000
1999–01 Revenue Impact:	Not Applicable	$100,000	$100,000

DESCRIPTION: The interest earned on U.S. Series EE savings bonds purchased and owned to finance higher education for the taxpayer, their spouse or dependents is excluded from personal taxable income. The bonds must be purchased and owned by people age 24 or over and must have been issued after 1989. They must be used for qualified higher education expenses at certain institutions in the same year in which they are redeemed. Qualified higher education expenses include tuition and fees, but not room and board expenses. In 1997, a full exclusion was allowed if income was less than $50,850 if single and $65,850 if married. The exclusion phased out through incomes of $76,250 (single) and $106,250 (married) at which point no exclusion was allowed.

PURPOSE: To help compensate for increasing college costs that have risen faster than the general rate of inflation and faster than the income of many Americans.

WHO BENEFITS: Taxpayers with incomes below a certain level who are pursuing higher education or who have a dependent pursuing higher education.

EVALUATION: It is too early to determine if this tax expenditure achieves its purpose. While this exclusion expands the opportunities for investing in higher education by providing a targeted incentive, its financial impact to date has been minimal; however, given the long-term nature of this investment for children who may not be attending college for ten more years, this is not surprising. [*Evaluated by the System of Higher Education.*]

1.003 EARNINGS ON EDUCATION IRAs

Internal Revenue Code Section: 530
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1997

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$2,400,000	$2,400,000
1999–01 Revenue Impact:	Not Applicable	$5,300,000	$5,300,000

DESCRIPTION: Taxpayers may establish trust or custodial accounts for the exclusive purpose of paying the qualified higher education expenses of a named beneficiary. Annual contributions are limited to $500 per beneficiary and may not be made after the beneficiary reaches age 18. The contribution limit is phased out for contributors with income between $95,000 and $100,00 if single ($150,000 and $160,000 if married).

Earnings on contributions to the accounts are not subject to tax. Distributions from the accounts may be excludable from gross income to the extent that they do not exceed the qualified education expenses of the beneficiary. If a HOPE or Lifetime Learning credit is claimed in a given year, then a distribution from an education IRA is allowed but the exclusion is not granted. Tax-free and penalty-free transfers or rollovers from an education IRA of one beneficiary to an education IRA of another beneficiary are allowed provided that the new beneficiary is a family member of the old beneficiary.

PURPOSE: To encourage higher education by reducing the cost.

WHO BENEFITS: Families or individuals who assume responsibility for paying tuition for themselves, or beneficiaries such as children or grandchildren.

EVALUATION: It is too early to determine the impact of this tax expenditure. This exclusion expands the opportunities for investing in higher education by providing a tax avoidance incentive. The financial impact has been minimal to date; however the impact will be more evident as beneficiaries begin to attend college in the future. This method of savings has been nationally proclaimed to assist families as they seek to access post-secondary opportunities. [*Evaluated by the System of Higher Education.*]

1.004 PUBLIC ASSISTANCE BENEFITS

Revenue Rulings, Internal Revenue Code Section 61 (defines gross income)
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1930s

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$6,300,000	$6,300,000
1999–01 Revenue Impact:	Not Applicable	$7,100,000	$7,100,000

DESCRIPTION: Public assistance benefits in the form of cash payments or goods and services, whether provided for free or at an income-scaled charge, are not included in the personal taxable income of the recipient. Some examples include Aid to Families with Dependent Children (AFDC), Supplemental Security Income (SSI) for the aged, blind or disabled, and State-local programs of General Assistance (GA).

PURPOSE: To recognize the low ability to pay taxes of people receiving public assistance and to reduce the cost to government of providing such assistance.

WHO BENEFITS: Those people receiving public assistance benefits above the income level where taxation begins. It should be noted that many welfare recipients, however, have incomes below this threshold and would have no tax liability even without the exemption.

EVALUATION: This tax expenditure achieves its purpose. Families receiving public assistance benefits are living below the poverty level and, as a result, generally are incurring debts beyond their ability to pay or are deferring necessary expenses until they can find a family wage job and become self-sufficient. It would be counterproductive to add welfare benefits to their taxable income, thereby reducing their ability to overcome the effects of poverty.

This is a fiscally effective means of achieving its purpose. By implementing this low-income benefit as an income exclusion under state and federal income tax programs, there is less cost to administer it than would result from a separate means tested program. [*Evaluated by the Adult and Family Services Division.*]

1.005 CERTAIN FOSTER CARE PAYMENTS

Internal Revenue Code Section: 131
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1982

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$100,000	$100,000
1999–01 Revenue Impact:	Not Applicable	$100,000	$100,000

DESCRIPTION: Payments made by a state, local, or state-licensed tax exempt child-placement agency to a foster care provider for the purpose of caring for a foster individual in the provider's home is excluded from personal taxable income of the foster care provider.

PURPOSE: To encourage individuals to assume the responsibility of caring for foster children and to relieve foster care providers from maintaining complex records that might deter families from accepting foster children or prevent them from claiming their full tax benefit.

WHO BENEFITS: Foster care providers.

EVALUATION: This tax expenditure achieves its purpose. Without this exclusion, foster parents would deduct the relevant expenses from the foster care payments when calculating taxable income. In order to deduct these expenses however, they would need to maintain extensive records of those expenses. The payments to foster parents for room and board, clothing replacement, and personal incidentals are estimated to be less than 60 percent of what the average family spends on raising a child. Consequently, deductions for expenses are likely to be greater than the payments received so tax liability (for the foster care income) is likely to be zero. Having the exclusion does not significantly decrease revenue to Oregon but does improve the recruitment and retention of foster parents. [*Evaluated by the Office for Services to Children and Families.*]

1.006 EMPLOYEE ADOPTION BENEFITS

Internal Revenue Code Section: 23 and 137
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: 12-31-01
Year Enacted in Federal Law: 1996

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	Less than $50,000	Less than $50,000
1999–01 Revenue Impact:	Not Applicable	Less than $50,000	Less than $50,000

DESCRIPTION: Benefits received under employer-sponsored adoption assistance programs are excluded from personal taxable income. The maximum exclusion is $5,000 per child or $6,000 in the case of a child with special needs. Expenses may be incurred over several years. Employer-provided adoption assistance must be received under an established employer-sponsored adoption assistance program. The exclusion is phased out at incomes between $75,000 and $115,000.

PURPOSE: To encourage and facilitate adoption.

WHO BENEFITS: Adoptive parents.

EVALUATION: Nationally and within Oregon, considerable focus has been placed on achieving permanent homes for children who are waiting in foster care. This includes the Adoption and Safe Families Act at the federal level and Oregon's SB 689.

Some employers have developed programs to encourage and support their employees in adopting waiting children. This is one of several programs which provide incentives to adoption, and it is difficult to measure the direct impact of this specific program. However, it is one of the few ways in which private, non-governmental resources are contributing to a national goal.

Since the exclusion is phased out at higher income levels, it encourages and sometimes makes it possible for lower income families to adopt. This exclusion is not, however, limited to those who adopt U.S. children, and is not limited to the adoption of the "harder to place" children. International adoptions, private adoptions, and independent adoptions, if covered by the specific employer adoption assistance program, could also claim this exclusion.

This exclusion does not significantly decrease revenue to Oregon but does improve the ability of Oregon families to adopt children needing permanent homes. [*Evaluated by the Office for Services to Children and Family.*]

1.007 CAFETERIA PLAN BENEFITS

Internal Revenue Code Section: 125
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1974

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$42,500,000	$42,500,000
1999–01 Revenue Impact:	Not Applicable	$53,400,000	$53,400,000

DESCRIPTION: Employer-paid benefits under cafeteria plans, where employees are offered a choice between taking monetary compensation or qualified benefits (such as health insurance) are not included in the employee's personal taxable income. The employee pays no tax when choosing the benefits but does pay tax when choosing the cash.

PURPOSE**:** To encourage employers to include a flexible benefits package as part of a compensation package; and employees to utilize such non-taxable qualified benefit options.

WHO BENEFITS: Employees receiving employer-paid cafeteria plan benefits. Employers may benefit by using flexible benefit plans as an incentive in recruiting high quality employees.

EVALUATION: This tax expenditure achieves its purpose and offers employees flexibility not present when an employer simply offers health insurance coverage. Employees are free to choose the option that is most beneficial to them, whether non-taxed health benefits or taxed monetary compensation. When choosing benefits, employees often receive benefit packages that are worth more than the foregone cash amount due to the advantages of group-based purchasing. Employers also benefit from the choice of health benefits instead of cash payments. [*Evaluated by Oregon Health Plan Policy & Research.*]

1.008 EMPLOYER PAID MEDICAL BENEFITS

Internal Revenue Code Sections: 105 and 106
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1918

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$369,900,000	$369,900,000
1999–01 Revenue Impact:	Not Applicable	$424,000,000	$424,000,000

DESCRIPTION: Employer payments for health insurance and other employee medical expenses are not included in the employee's personal taxable income.

PURPOSE: To encourage employers and employees to include health insurance coverage in compensation packages.

WHO BENEFITS: Employees, their spouses, and dependents receiving employer-paid health benefits. Employers may benefit from offering highly valued health services as a recruitment and retention tool for high quality employees. Employers will also benefit from having a healthier work force.

EVALUATION: This tax expenditure has achieved its purpose. While not entirely responsible for the fact that 66 percent of Oregon workers received employer offered health benefits, it is a major incentive for employers to offer such benefits.

This tax expenditure benefits workers on a differential basis depending on industry and wage levels. Many of the fastest growing industries, such as retail trade, construction and services, are less likely to offer coverage to employees. Workers earning between 100–200 percent of the federal poverty level are less likely to be offered employer paid medical benefit coverage. [*Evaluated by Oregon Health Plan Policy & Research.*]

1.009 PENSION CONTRIBUTIONS AND EARNINGS

Internal Revenue Code Sections: 401–407, 410–418E, and 457
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$523,200,000	$523,200,000
1999–01 Revenue Impact:	Not Applicable	$565,900,000	$565,900,000

DESCRIPTION: Employer contributions to pension plans are not included in the employee's personal taxable income in the year of contribution. Certain amounts contributed by employees are excluded from income as well. Taxation on contributions and earnings are deferred until distribution, when withdrawals are included in taxable income. The estimated tax benefit is a net figure, i.e. the revenue foregone in a given year offset by the amount of tax paid on withdrawals in that year.

PURPOSE: To promote saving for retirement and to tax income when it is received.

WHO BENEFITS: Employees receiving employer-paid pension benefits, although lower income workers are less likely to be covered by these plans. Employers may benefit by paying lower wages than would be paid if these benefits were not offered.

EVALUATION: This tax expenditure achieves its purpose. It is likely that pensions result in greater savings, thereby reducing the amount of government assistance needed by retirees. The tax deferral on contributions is particularly favorable to employees because earnings accrue to the amounts that would otherwise be paid in taxes, significantly increasing earning over the life of the plan. It should be noted however, that current projections suggest that the rate of retirement savings must increase three-fold from present levels for future retirees to maintain their current living standards. Insufficient retirement savings could have a dramatic impact on government service programs, especially as the population age distribution shifts. [*Evaluated by the Senior and Disabled Services Division.*]

1.010 HOSPITAL INSURANCE (PART A)

Internal Revenue Service Ruling 70-341, 1970-2 Cumulative Bulletin page 31
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1965

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$98,600,000	$98,600,000
1999–01 Revenue Impact:	Not Applicable	$123,200,000	$123,200,000

DESCRIPTION: Part A of Medicare pays for certain in-patient hospital care, skilled nursing facility care, home health care, and hospice care for eligible individuals age 65 or over or who are disabled; these benefits are not included in the personal taxable income of the recipient. The subsidy equals the benefits that exceed an individual's lifetime contributions through payroll tax. The tax expenditure equals the subsidy multiplied by the recipient's marginal tax rate.

PURPOSE: To ensure consistent treatment with non-taxed social security benefits and to avoid imposing taxes during a period of illness.

WHO BENEFITS: Recipients of the medical services provided through Part A of Medicare.

EVALUATION: This tax expenditure achieves its purpose and lowers the direct cost of hospital care for the elderly. The costs associated with serious illness can be quite large and it is generally considered neither fair nor good public policy to tax people at a time they are most vulnerable. Also, it is difficult to determine the value of benefits received exceeding an individual's contributions. The primary recipients of these subsidized benefits are people who became eligible for the program in its earliest years, who had low taxable wages, who qualified as a spouse with little or no contributions of their own, and who have a longer-than-average life expectancy. Over time, the amount of these subsidized benefits is expected to decline as future recipients will have made greater contributions over their lifetimes. [*Evaluated by the Senior and Disabled Services Division.*]

1.011 SUPPLEMENTARY MEDICAL INSURANCE (PART B)

Internal Revenue Service Ruling 70-341, 1970-2 Cumulative Bulletin page 31
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1970

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$43,600,000	$43,600,000
1999–01 Revenue Impact:	Not Applicable	$57,300,000	$57,300,000

DESCRIPTION: For those who elect to pay the required monthly premiums ($43.80 in 1997), Part B of Medicare covers certain doctors' services, outpatient services, and other medical services for people who are age 65 and over or who are disabled. The portion of the program's costs that are paid with governmental general revenues are not included in the personal

taxable income of recipients. Currently, these costs account for 75 percent of the program's costs. Under current law, annual increases in the Part B premium is limited to the percentage increase in the social security cost of living allowance.

PURPOSE: To ensure the consistent treatment with non-taxed social security benefits.

WHO BENEFITS: Recipients of the medical services provided through Part B of Medicare.

EVALUATION: This tax expenditure achieves its purpose and lowers the direct cost of hospital care for the elderly. While it may be possible to assign a value to these non-taxed subsidies according to individual use, it is generally considered neither fair nor good public policy to tax people at a time they are most vulnerable. However, because this subsidy is not means tested, it is argued that the exclusion benefits higher income retirees. Congress has recognized this issue in discussions on health reform. While no conclusions have been reached, the merits of incorporating gross income thresholds that would raise the premiums for higher income retirees have been debated. [*Evaluated by the Senior and Disabled Services Division.*]

1.012 SOCIAL SECURITY BENEFITS (FEDERAL)

Internal Revenue Code Section: (various and multiple Revenue Rulings)
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted: 1938

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$166,600,000	$166,600,000
1999–01 Revenue Impact:	Not Applicable	$176,800,000	$176,800,000

DESCRIPTION: Only a portion of social security and railroad retirement benefits are considered nontaxable at the federal level while the state of Oregon extends the tax exemption to the full amount of benefits. As a result there are two tax expenditures pertaining to these benefits. This tax expenditure pertains to those benefits that are exempt at the federal level. The tax expenditure pertaining to the portion of benefits that are taxed at the federal level but are exempt in Oregon is Social Security Benefits (Oregon) (1.093).

The amount of benefits subject to taxation depends on the amount of "provisional income" above certain thresholds. "Provisional income" is adjusted gross income plus one-half of social security benefits and otherwise tax-exempt interest income (i.e. interest from tax-exempt bonds). Taxpayers with "provisional income" under $25,000 (if single) or $32,000 (if married filing jointly) pay no tax.

If "provisional income" is above these thresholds but below $34,000 (single) or $44,000 (joint) then the amount of benefits subject to tax is the lesser of: (1) 50 percent of benefits or (2) 50 percent of income in excess of the first threshold. If income is above the second threshold, the amount of benefits subject to tax is the lesser of: (1) 85 percent of benefits or (2) 85 percent of income above the second threshold, plus the smaller of $4,500 if single ($6,000 if a couple) or 50 percent of benefits. For couples filing separately, taxable benefits are the lesser of 85 percent of benefits or 85 percent of "provisional income."

PURPOSE: The Congressional Research Service cited three reasons for the original exclusion: (1) congress did not intend for these benefits to be taxed, (2) the benefits were intended to be in the form of "gifts" and (3) taxing these benefits would defeat their intended purposes.

WHO BENEFITS: The number of Oregon taxpayers who receive some nontaxable social security and railroad retirement benefits has ranged from approximately 120,000 to 137,000 between 1990 and 1996. In 1996, the average amount of benefit was slightly over $7,000.

EVALUATION: This tax expenditure achieves its purpose; however, the issue continues to be the focus of significant national discussions and debate. While this tax exclusion provides the recipients with more disposable income, there are severe concerns over the viability of the social security benefits system in the long term. Current retirement index data forecasts that current retirement programs and savings patterns of persons aged 30–48 are not adequate to maintain these individuals at a living standard commensurate with their current living standards. Projections suggest that the rate of retirement savings must increase three fold from present standards in order to accomplish this future parity. The inability to achieve this parity will cause greater numbers of people to look to government service programs to assist them. The present population of those age 30–48 is substantial and this program could have a dramatic impact when they reach the retirement age. [*Evaluated by the Senior and Disabled Services Division.*]

1.013 ACCELERATED DEPRECIATION OF BUILDINGS

Internal Revenue Code Sections: 167 and 168
Oregon Statutes: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

	Corporation	Personal	Total
1997–99 Revenue Impact:	$10,100,000	$7,000,000	$17,100,000
1999–01 Revenue Impact:	$6,200,000	$4,200,000	$10,400,000

DESCRIPTION: In general, taxpayers may deduct from corporation and personal taxable income the depreciation of buildings based on a "straight line" method where equal amounts are deducted in each period. This tax expenditure represents the impact of depreciation methods accelerated over the straight-line method.

PURPOSE: To promote investment in business buildings.

WHO BENEFITS: This expenditure directly benefits owners of buildings used in a trade or business. Indirect beneficiaries include employees, customers, and the building construction and demolition industry.

EVALUATION: This expenditure appears to achieve its purpose. By reducing the cost of new and young buildings below what it would be under straight-line depreciation, this tax expenditure tends to increase the supply of new or younger buildings relative to older buildings. In doing so, it may reduce the financial incentive to remodel and re-use older buildings in favor of demolishing them and replacing them with new buildings. Therefore, the exemption may favor industrial modernization and high-density development. [*Evaluated by the Economic Development Department.*]

1.014 ACCELERATED DEPRECIATION OF EQUIPMENT

Internal Revenue Code Sections: 167 and 168
Oregon Statutes: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

	Corporation	Personal	Total
1997–99 Revenue Impact:	$117,700,000	$49,500,000	$167,200,000
1999–01 Revenue Impact:	$130,500,000	$55,200,000	$185,700,000

DESCRIPTION: In general, taxpayers may deduct from corporation and personal taxable income the depreciation of equipment based on a "straight line" method where equal amounts are deducted in each period. This tax expenditure represents the impact of depreciation methods accelerated over the straight-line method.

PURPOSE: To promote investment in business equipment.

WHO BENEFITS: Owners of equipment used in a trade or business benefit directly. Indirect beneficiaries include employees, customers, and the equipment manufacturing industry.

EVALUATION: This expenditure appears to achieve its purpose. By reducing the cost of new and young equipment below what it would be under straight-line depreciation, this tax expenditure tends to increase the demand for new or younger equipment relative to older equipment. In doing so, it may reduce the financial incentive to repair and re-use older equipment in favor of scrapping it and replacing it with new equipment. Therefore, the exemption may favor industrial modernization and productivity. [*Evaluated by the Economic Development Department.*]

1.015 INCOME EARNED ABROAD BY U.S. CITIZENS

Internal Revenue Code Section: 911
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1926

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$12,900,000	$12,900,000
1999–01 Revenue Impact:	Not Applicable	$14,900,000	$14,900,000

DESCRIPTION: U.S. citizens who live abroad may exclude from personal taxable income up to $70,000 earned from private sector employment overseas. The limitation increases in increments of $2,000 each year beginning in 1998, until it reaches $80,000 in 2002. Individuals can also exclude certain expenditures for overseas housing.

PURPOSE: To encourage U.S. exports by encouraging U.S. citizens to work abroad. It is argued that U.S. citizens working abroad play an important role in promoting the sale of U.S. goods abroad. The exclusion is also to compensate for higher living costs overseas, and to compensate for the fact that the individual living overseas may pay taxes to the foreign country that are often higher than U.S. taxes.

WHO BENEFITS: Individuals who live and work abroad, and indirectly the companies they work for, and the consumers of their products or services.

EVALUATION: This expenditure appears to achieve its purpose. It would appear that a relatively large number of Oregonians (or U.S. citizens who work for Oregon companies) are working overseas. This not only benefits Oregon exports, but also helps Oregon attain an international frame of mind as many of these individuals return to Oregon. [*Evaluated by the Economic Development Department.*]

1.016 INCOME OF FOREIGN SALES CORPORATIONS

Internal Revenue Code Sections: 921–927 and 991–997
Oregon Statute: 317.013 (Connection to federal corporation taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1984

	Corporation	Personal	Total
1997–99 Revenue Impact:	$7,400,000	Not Applicable	$7,400,000
1999–01 Revenue Impact:	$8,900,000	Not Applicable	$8,900,000

DESCRIPTION: This provision permits U.S. exporters to exempt a portion of their export income from corporate taxable income. To qualify, exports must be sold through specially defined Foreign Sales Corporations that are organized in a foreign country and that meet certain requirements designed to ensure a minimal presence in a foreign location.

PURPOSE: To encourage U.S. firms to export and secondarily to locate their operations in the United States rather than abroad.

WHO BENEFITS: Corporations engaged in exporting goods, and indirectly their suppliers, customers, and employees.

EVALUATION: This expenditure may be effective in encouraging Oregon exports. It is unclear the degree to which exports would decline without this provision. [*Evaluated by the Economic Development Department.*]

1.017 INVENTORY PROPERTY SALES SOURCE-RULE EXCEPTION

Internal Revenue Code Sections: 861–863 and 865
Oregon Statute: 317.013 (Connection to federal corporation taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

	Corporation	Personal	Total
1997–99 Revenue Impact:	$17,400,000	Not Applicable	$17,400,000
1999–01 Revenue Impact:	$18,500,000	Not Applicable	$18,500,000

DESCRIPTION: In general, for U.S. corporations that have foreign operations, the income from sales of personal property must be considered U.S. rather than foreign-source income. This tax expenditure provides an exception to that rule for inventory property, which may be sourced in the country where the sale occurs. This special provision governing the source of income from inventory sales interacts with the foreign tax credit provisions in a way that can effectively exempt a portion of a firm's export income from corporate taxable income.

PURPOSE: To encourage U.S. exports, and to promote "just-in-time" supply to the buyer.

WHO BENEFITS: Corporations involved in the sale of exports benefit directly. Indirect beneficiaries include their suppliers, customers, and employees.

EVALUATION: This provision may have had some effect on the increase in Oregon exports over the past ten years, and thus may achieve its purpose. It probably provides the additional benefit of moving inventory closer to the customer and thereby increases U.S. firms' competitive advantage over countries that do not have a similar provision. It fosters "just-in-time" supply. [*Evaluated by the Economic Development Department.*]

1.018 MAGAZINE, PAPERBACK, AND RECORD RETURNS

Internal Revenue Code Section: 458
Oregon Statutes: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1978

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Available	Not Available	$100,000
1999–01 Revenue Impact:	Not Available	Not Available	$100,000

DESCRIPTION: Generally, if a buyer returns goods to the seller, the seller's income is reduced in the year in which the items are returned. An exception has been granted to publishers and distributors of magazines, paperbacks, and records, who may exclude from corporate or personal taxable income in one year the sale of goods that are returned after the close of that year. This allows publishers and distributors to sell more copies to wholesalers and retailers than they expect will be sold to consumers.

There are two reasons for this overstocking of inventory. First, it is difficult to predict consumer demand for particular titles. Second, overstocking is used as a marketing strategy that relies on the conspicuous display of selected titles.

PURPOSE: To encourage the purchase of printed materials and promote the business of those involved in publishing and distributing those materials.

WHO BENEFITS: Publishers and distributors of magazines, paperbacks and records benefit directly. Indirect beneficiaries include their suppliers, customers, and employees.

EVALUATION: This expenditure appears to achieve its purpose by promoting increased sales of materials. The removal of this provision might cause irritating back-orders of popular materials and reduce sales of published materials due to an insufficient number of copies to allow for conspicuous display. However, the provision probably also encourages the over-printing of copies and the resultant waste. [*Evaluated by the Economic Development Department.*]

1.019 CASH ACCOUNTING, OTHER THAN AGRICULTURE

Internal Revenue Code Sections: 446 and 448
Oregon Statutes: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1916

	Corporation	Personal	Total
1997–99 Revenue Impact:	$100,000	$700,000	$800,000
1999–01 Revenue Impact:	$100,000	$700,000	$800,000

DESCRIPTION: Certain small businesses and personal service corporations are allowed to use the cash method of accounting, rather than the accrual method, for tax purposes. This effectively defers corporation and personal income tax by allowing qualifying businesses to record income when it is received rather than when it is earned.

PURPOSE: To simplify record keeping for small businesses and to eliminate an additional drain on the working capital of small businesses.

WHO BENEFITS: Small businesses and personal service corporations benefit directly. Some of the benefits are probably passed along to the small businesses' employees, customers, and suppliers.

EVALUATION: This expenditure achieves its purpose by helping to reduce working capital constraints often faced by small business. Startup businesses often fail for lack of sufficient investment monies to maintain an adequate level of working capital. Ongoing successful businesses can have temporary unforeseen downturns or periods of rapid growth that can use up precious working capital and threaten the business' survival. This expenditure helps small businesses by allowing them to pay income tax only on income received rather than on income promised in the future due to a sale in the present. This provision also simplifies the record keeping of small businesses by allowing them to recognize costs and income for tax purposes in the same manner as for their own record keeping.

This is a fiscally effective method to simplify record keeping and to help eliminate the shortage of working capital for small businesses. No other more efficient method is apparent. [*Evaluated by the Economic Development Department.*]

1.020 REGIONAL ECONOMIC DEVELOPMENT INCENTIVES

Internal Revenue Code Sections: 38(b), 39(d), 45A, 168(j), 280C(a), and 1391–1397D
Oregon Statutes: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date Date: None
Year Enacted in Federal Law: 1993

	Corporation	Personal	Total
1997–99 Revenue Impact:	Less than $50,000	Less than $50,000	Less than $50,000
1999–01 Revenue Impact:	Less than $50,000	Less than $50,000	Less than $50,000

DESCRIPTION: The original federal legislation specified that nine empowerment zones and 95 enterprise communities would be designated to receive special tax benefits. The largest of those benefits are provisions for deducting certain expenditures in the year made rather than depreciating them over a number of years, and the benefits derived from tax-exempt financing. Designated areas must satisfy eligibility criteria including poverty rates and population and geographic size limits, and will be eligible for benefits for 10 years. The main benefits of designation are social service block grants from the U.S. Department of Housing and Urban Development or the U.S. Department of Agriculture.

In 1997 new legislation expanded the program. Two additional empowerment zones can be established with the same tax incentives as the original zones. In addition, 20 new empowerment zones can be designated which receive partial tax benefits.

Oregon currently has no empowerment zones, but does have two enterprise communities, one rural and one urban. In addition, Oregon has requested the designation of two potential empowerment zones under the new expanded program. Enterprise communities receive expanded tax exempt financing for zone businesses. (Empowerment zone businesses receive additional tax incentives including wage credits and equipment expensing allowances.) Tax exempt bonds for any one community cannot exceed $3 million.

PURPOSE: To revitalize economically distressed areas.

WHO BENEFITS: Businesses and employees within the designated areas and holders of bonds nationwide.

EVALUATION: This expenditure appears to achieve its purpose. Research indicates that enterprise zones in general have been fairly successful at stimulating economic recovery in high-need areas. Removing the Oregon tax exempt status of these bonds would reduce their attractiveness to potential bondholders and increase the rate that bond issuers would expect to pay for financing, which in turn would reduce benefits. [*Evaluated by the Economic Development Department.*]

1.021 INCOME OF CONTROLLED FOREIGN CORPORATIONS

Internal Revenue Code Sections: 11(d), 882, and 951–964
Oregon Statute: 317.013 (Connection to federal corporation taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1909

	Corporation	Personal	Total
1997–99 Revenue Impact:	$5,600,000	Not Applicable	$5,600,000
1999–01 Revenue Impact:	$6,200,000	Not Applicable	$6,200,000

DESCRIPTION: When a U.S. firm earns income through a foreign subsidiary, the income is exempt from U.S. corporate taxes as long as it is in the hands of the foreign subsidiary. At the time the foreign income is repatriated, the U.S. parent corporation can credit foreign taxes paid by the subsidiary against U.S. taxes. Because the deferral principle allows U.S. firms to delay any residual U.S. taxes that may be due after foreign tax credits, it provides a tax benefit for firms that invest in countries with low tax rates.

PURPOSE: To encourage the purchase and operation of foreign subsidiaries by U.S. firms, thereby increasing these firms' penetration into foreign markets and their global competitiveness.

WHO BENEFITS: U.S. multinational firms benefit directly, while their suppliers, customers, and employees benefit indirectly.

EVALUATION: This expenditure appears to achieve its purpose. Encouraging companies to purchase and operate foreign subsidiaries may result in a short-term reduction in employment in the United States as production is moved to the foreign country where production costs may be cheaper than in the U.S. However, this move is likely to make the parent company more competitive worldwide, so that its remaining operations and employment in the United States become more secure in the long-term. If a company were to maintain all its production facilities in the United States, it might not be able to compete successfully with foreign-based companies and thus would not even employ the technical staff, marketers, corporate executives, and others that it currently employs in the United States. [*Evaluated by the Economic Development Department.*]

1.022 EMPLOYER PAID GROUP LIFE INSURANCE PREMIUMS

Internal Revenue Code Sections: 79, 105, and 106
Legal Opinion 1014, 1920-2 Cumulative Bulletin page 8
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1920

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$13,200,000	$13,200,000
1999–01 Revenue Impact:	Not Applicable	$14,500,000	$14,500,000

DESCRIPTION: Employer payments for employee life insurance (up to $50,000 in coverage) and death benefits are not included in the employee's personal taxable income.

PURPOSE: To encourage employers and employees to incorporate life insurance benefits into compensation packages.

WHO BENEFITS: Employees who do not have to purchase their own life insurance and the dependents of employees who would not otherwise be insured. Employers may benefit by paying lower wages than would be paid if these benefits were not offered. Higher income individuals are more likely than lower income individuals to benefit from this exclusion because they are more likely to have this benefit.

EVALUATION: This tax expenditure achieves its purpose and is an effective way of providing employee security. It is an important component of the total benefits package in terms of attracting and retaining Oregon workers. In the increasingly competitive national labor market there is merit in retaining incentives that are available in other states. In addition, the tax expenditure is structured so that it does not discriminate in favor of select employees. The life insurance itself provides heirs with a greater sense of stability and reduces the potential for future public assistance. [*Evaluated by the Employment Department.*]

1.023 EMPLOYER PAID ACCIDENT AND DISABILITY INSURANCE

Internal Revenue Code Sections: 105 and 106
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$1,400,000	$1,400,000
1999–01 Revenue Impact:	Not Applicable	$1,400,000	$1,400,000

DESCRIPTION: Employer payments for employee accident and disability insurance premiums are not included in the employee's personal taxable income.

PURPOSE: To encourage employers and employees to incorporate accident and disability insurance into compensation packages.

WHO BENEFITS: Employees who do not have to purchase their own accident and disability insurance and the dependents of employees who would not otherwise be insured. Employers may benefit by paying lower wages than would be paid if these benefits were not offered. Higher income individuals are more likely than lower income individuals to benefit from this exclusion because they are more likely to have this benefit.

EVALUATION: This tax expenditure achieves its purpose and is an effective way of providing employee security. As is the case with Employer Paid Group Life Insurance (1.022), it is an important component of the total benefits package in terms of attracting and retaining Oregon workers. In the increasingly competitive national labor market there is merit in retaining incentives that are available in other states. In addition, the tax expenditure is structured so that it does not discriminate in favor of select employees. Accident, disability and supplemental unemployment benefits allow an employee to maintain a standard of living through short term transitions. [*Evaluated by the Employment Department.*]

1.024 EMPLOYER PROVIDED DEPENDENT CARE

Internal Revenue Code Section: 129
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1981

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$6,600,000	$6,600,000
1999–01 Revenue Impact:	Not Applicable	$8,100,000	$8,100,000

DESCRIPTION: Employer payments for dependent care through a dependent care assistance program, and employee contributions (up to $5,000 per year) to a dependent care account are not included in the employee's personal taxable income.

PURPOSE: To promote the provision of dependent care benefits by employers and to reduce the costs of dependent care for employees.

WHO BENEFITS: Most of the benefit goes to employees making contributions to tax-free dependent care accounts set up by their employers. A relatively small share goes to employees receiving employer-paid dependent care benefits because those benefits are not widespread.

EVALUATION: This tax expenditure achieves its purpose. For employee contributions to dependent care accounts, dependent care costs are reduced because they are paid for with pre-tax dollars. Employees whose employer does not offer dependent care accounts can qualify for a dependent care credit against their federal and Oregon income tax.

For employer-provided benefits, the typical practice is that the benefit is part of a cafeteria plan (1.007 Cafeteria Plan Benefits) in which employees can choose from various taxable or non-taxable benefits. Consequently, those choosing this option would be meeting specific needs so the tax expenditure is well-targeted. It also has the potential for reducing the need for public funds in providing the needed care. Further, in the increasingly competitive national labor market there is merit in retaining the incentives that are available in other states. While any one benefit may not appear significant by itself, it is an important piece in the total benefits package in terms of attracting and retaining Oregon workers. [*Evaluated by the Employment Department.*]

1.025 MISCELLANEOUS FRINGE BENEFITS

Internal Revenue Code Sections: 132 and 117(d)
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1984

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$41,800,000	$41,800,000
1999–01 Revenue Impact:	Not Applicable	$47,400,000	$47,400,000

DESCRIPTION: Certain fringe benefits are exempt from personal income tax. These benefits include no-additional-cost services (such as free stand-by flights for airline employees), qualified

employee discounts, working condition fringe benefits, and de minimis fringe benefits (such as providing coffee to employees or allowing them occasional personal use of an office copy machine). Also included are subsidized parking and eating facilities and provision of on-premises athletic facilities. The provision of these fringe benefits must meet certain nondiscrimination rules to qualify. The benefits must be provided solely to employees, their spouses and dependent children, retired employees, or the widows or widowers of former employees.

PURPOSE: To codify the traditional treatment of these benefits as not contributing to taxable income and to avoid the difficulty of monitoring and assigning values to them.

WHO BENEFITS: Employees receiving fringe benefits. Employers may benefit by paying lower wages than would be paid if these benefits were not offered.

EVALUATION: This tax expenditure achieves its purpose and is a benefit to varying degrees, depending on the industry involved. For some occupations, this benefit may be specifically relevant to those employees who are willing to accept lower wages in exchange for these benefits. It is also difficult to establish a dollar amount for these items without an elaborate accounting system to monitor use. Consequently, the tax expenditure provides a benefit by preventing the need to establish such a system. [*Evaluated by the Employment Department.*]

1.026 EMPLOYEE MEALS AND LODGING (Nonmilitary)

Internal Revenue Code Sections: 119 and 132(e)(2)
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1918

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$4,900,000	$4,900,000
1999–01 Revenue Impact:	Not Applicable	$5,700,000	$5,700,000

DESCRIPTION: Employees do not include in personal taxable income the fair market value of meals furnished by employers if the meals are furnished on the employer's business premises and for the convenience of the employer. In certain situations, this includes the value of meals provided to an employee at a subsidized eating facility operated by the employer.

Fair market value of lodging provided by the employer can also be excluded from income, if the lodging is furnished on business premises for the convenience of the employer, and if the employee is required to accept the lodging as a condition of employment.

PURPOSE: To eliminate record-keeping difficulties and to acknowledge that the fair market value of employer provided meals and lodging may be difficult to measure.

WHO BENEFITS: Employees and their employers in those occupations or sectors in which the provision of meals and/or lodging is common.

EVALUATION: This tax expenditure achieves its purpose and provides a benefit to both the employer and the employee. In many cases provided meals and lodging are a condition of hire. An example is the individual who is hired to tend an oil derrick in the Gulf of Mexico. It is not

practical to have the individual ferry back and forth between the derrick and shore when a shift changes. The employee has no option but to accept the room and board if they wish to take the job. In the case of apartment house managers, free apartment rent is likely a significant factor in accepting the position. This tax expenditure simplifies the bookkeeping process associated with tracking this benefit. [*Evaluated by the Employment Department.*]

1.027 EMPLOYEE STOCK OWNERSHIP PLANS

Internal Revenue Code Sections: 133, 401(a)(28), 404(a)(9), 404(k), 415(c)(6), 1042, 4975(e)(7), 4978, and 4979A
Oregon Statute: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1974

	Corporation	Personal	Total
1997–99 Revenue Impact:	$3,600,000	$300,000	$3,900,000
1999–01 Revenue Impact:	$4,100,000	$300,000	$4,400,000

DESCRIPTION: An Employee Stock Ownership Plan (ESOP) is a defined-contribution plan that is required to primarily invest in the stock of the sponsoring employer. These plans contain several tax exemptions. Employer contributions may be deducted from corporation taxable income as a business expense. An employer may also deduct dividends paid on stock held by an ESOP if the dividends are paid to plan participants. Employees are not taxed on employer contributions or the earnings on invested funds until they are distributed. A benefit is also available to certain lenders. Qualified lenders may exclude from taxable income 50 percent of the interest earned on an ESOP loan if the ESOP owns over 50 percent of the company's stock. Under certain circumstances, a stockholder may defer the recognition of the gain from the sale of stock to an ESOP. The estimated tax benefit is a net figure, i.e. the revenue foregone in a given year offset by the amount of tax paid on distributions in that year.

PURPOSE: To broaden employee stock ownership and provide employees with a source of retirement income.

WHO BENEFITS: Employers and employees of participating companies.

EVALUATION: This tax expenditure achieves its purpose as well as promoting stability and loyalty in business organizations. These plans create a sense of ownership among employees which, in turn, enhances performance. The success of this tax expenditure may be measured in future company growth resulting in more tax revenue for the state. The tax expenditure also promotes a means of accumulating retirement funds. In the increasingly competitive national labor market there is merit in retaining incentives that are available in other states. This particular incentive could be an integral piece in terms of recruiting and/or retaining Oregon workers. [*Evaluated by the Employment Department.*]

1.028 EMPLOYEE AWARDS

Internal Revenue Code Sections: 74(c) and 274(j)
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$700,000	$700,000
1999–01 Revenue Impact:	Not Applicable	$700,000	$700,000

DESCRIPTION: Awards given to employees for length of service or for safety are excluded from personal taxable income. The amount of the exclusion is usually limited to $400 but may be as much as $1,600. There are certain qualification requirements to ensure that the awards do not constitute disguised compensation.

PURPOSE: To encourage longevity in employment and safety practices on the job.

WHO BENEFITS: Employees who receive length of service or safety awards and employers who save costs related to training and time loss injuries.

EVALUATION: This tax expenditure achieves its purpose while recognizing bona fide achievements. The exclusion promotes such positive goals as loyalty and safety. It also helps stabilize the workforce. As a result, it has a positive impact in reducing unemployment and workers compensation claims. Productivity is likely to increase thus contributing to future growth and greater tax revenue for the state. [*Evaluated by the Employment Department.*]

1.029 EMPLOYER PROVIDED DEATH BENEFITS

Internal Revenue Code Section: 101(b) Reg. §1.101.2
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1951

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$100,000	$100,000
1999–01 Revenue Impact:	Not Applicable	$100,000	$100,000

DESCRIPTION: The first $5,000 paid by or on behalf of an employer due to an employee's (or former employee's) death is excluded from the personal taxable income of the employee's beneficiaries or estate. This pertains only to certain noninsured employer-provided death benefits. (Employers may provide insured death benefits of up to $50,000 tax free.)

PURPOSE: To treat these benefits identical to those paid by insurance companies.

WHO BENEFITS: Beneficiaries of employees who receive noninsured employer-provided death benefits.

EVALUATION: This tax expenditure achieves its purpose and maximizes the amount of transitional money for those who may not otherwise have a benefit available. It reduces the need for public assistance while families pull their lives together during difficult times. These benefits are often used as seed money for training or as a temporary cushion for living expenses. This tax expenditure is of particular importance to those who lack life insurance. [*Evaluated by the Employment Department.*]

1.030 EMPLOYER PROVIDED EDUCATION BENEFITS

Internal Revenue Code Section: 127
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: 5-31-00
Year Enacted in Federal Law: 1997

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$1,700,000	$1,700,000
1999–01 Revenue Impact:	Not Applicable	$1,100,000	$1,100,000

DESCRIPTION: Employer provided educational assistance benefits, up to $5,250 annually, are excluded from the personal taxable income of the recipient. For the exclusion to apply, certain requirements must be satisfied. Educational assistance includes the payment of tuition, fees, books, supplies and equipment; it excludes items such as meals, lodging and transportation. The exclusion does not apply to education pertaining to sports, games or hobbies.

Prior law contained an exclusion for employer provided assistance for undergraduate and graduate education. That exclusion expired. This expenditure extends the exclusion for employer provided undergraduate assistance only.

PURPOSE: To promote the provision of educational benefits by employers.

WHO BENEFITS: Employees receiving employer provided educational assistance. Employers may benefit by paying a lower wage than would be paid if these benefits were not offered. Employers also benefit from a better educated and trained work force.

EVALUATION: This tax expenditure achieves its purpose and provides a benefit to both the employer and the employee. The exclusion promotes improved job skills for the employee and a better educated work force for the employer. In the increasingly competitive national labor market there is merit in retaining the incentives that are available in other states. *[Evaluated by the Employment Department.]*

1.031 ACCELERATED DEPRECIATION RENTAL HOUSING

Internal Revenue Code Sections: 167 and 168
Oregon Statutes: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1954

	Corporation	Personal	Total
1997–99 Revenue Impact:	$4,700,000	$5,200,000	$9,900,000
1999–01 Revenue Impact:	$4,600,000	$5,000,000	$9,600,000

DESCRIPTION: In general, taxpayers may deduct from corporation and personal taxable income the depreciation of rental housing based on a "straight line" method where equal amounts are deducted in each period. This tax expenditure represents the impact of depreciation methods accelerated over the straight-line method.

PURPOSE: To promote investment in rental housing by effectively deferring taxes paid on those investments.

WHO BENEFITS: Owners of rental housing.

EVALUATION: This expenditure appears to achieve its purpose. As described by Congressional Research Service, accelerated depreciation is intended as "a general stimulus to investment." There are likely instances where the tax deferral represented by accelerated depreciation provides a critical incentive to developers and investors in making decisions regarding construction or purchase of rental property. However, rental housing is not the only item that receives some form of preferential tax treatment. It is difficult to ascertain the fiscal effectiveness.

A further impact of accelerated depreciation is discussed by Congressional Research Service. When rental property is eventually sold, the relatively larger gain is taxed at a potentially lower capital gains rate. Under straight line depreciation, the gain to which this preferential treatment could be applied would be smaller and less depreciation would have been used to reduce ordinary income over the life of the asset. [*Evaluated by the Housing and Community Services Department.*]

1.032 CAPITAL GAINS ON HOME SALES

Internal Revenue Code Section: 121
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1997

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$59,000,000	$59,000,000
1999–01 Revenue Impact:	Not Applicable	$63,700,000	$63,700,000

DESCRIPTION: Homeowners may exclude from personal taxable income up to $250,000 (single taxpayers) or $500,000 (married taxpayers filing joint returns) of capital gain realized on the sale of their principal residence. The exclusion is allowed each time a taxpayer meets the eligibility requirements, but generally not more than once every two years.

This expenditure replaces two tax expenditure provisions from prior law, the "deferral of capital gains on sales of principal residences," and "exclusion of capital gains on sales of residences for persons aged 55 and over".

PURPOSE: To promote home ownership by reducing the after-tax cost.

WHO BENEFITS: Homeowners

EVALUATION: This exclusion achieves its purpose of reducing the tax burden on individuals selling their principal residence. According to the Congressional Research Service,

> Congress believed that taxing capital gains from the sale of principal residences imposed a "hardship," because capital gains may reflect only a general rise in housing prices, in which case, the tax on the gain would reduce the...ability to replace the home they had sold.

Although this does amount to preferential treatment compared with other capital investment opportunities, the justification is that "much of the profit from the sale of a personal residence represents inflationary gains, and because the purchase of a principal residence is less of a profit-motivated investment than other types of investments."

As previously noted, this law replaces a commonly used deferral, and one time capital gains exclusion for taxpayers aged 55 or older. The 1997 law increases the amount eligible for exclusion from $125,000 to $250,000 ($500,000 if married filing a joint return).

Allowing the exclusion for taxpayers under age 55, and permitting the exclusion to be used more than once achieves certain policy objectives. The deferral could only be fully utilized if the taxpayer purchased a new principal residence of equal or greater value than the one being sold. Therefore, the prior law may have encouraged some taxpayers to purchase more expensive homes based solely on tax consequences. Prior law may also have discouraged older taxpayers from selling their homes, if they had already used the exclusion. The new law removes this constraint.

Finally, the law change simplifies what had been "among the most complex tasks faced by a typical taxpayer." To claim the exclusion under the prior law, many taxpayers had to determine the basis of each home they owned, and adjust the basis of their current home to reflect any untaxed gains. This involved making determinations of "improvements" that added to the basis (as compared to "repairs" which do not) and retaining related records for several years. "By excluding from taxation capital gains on principal residences below a relatively high threshold, few taxpayers will have to refer to records in determining income tax consequences of transactions related to their house." [E*valuated by Housing and Community Services Department*.]

1.033 VETERANS' BENEFITS AND SERVICES

38 U.S. Code Section 3101
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1917

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$15,000,000	$15,000,000
1999–01 Revenue Impact:	Not Applicable	$15,900,000	$15,900,000

DESCRIPTION: All benefits paid by the Veterans Administration are excluded from the personal taxable income of recipients, including disability compensation, pensions, and GI bill benefits.

PURPOSE: To recognize the service and sacrifices made by veterans for the country and to compensate veterans for reductions in civilian earning capacity due to disabilities.

WHO BENEFITS: Veterans and their families receiving benefits from the Veterans Administration. In addition to the on-going benefits described above, the Oregon Department of Veterans' Affairs recently opened the first Veterans Retirement Home in Oregon. Located in The Dalles, 151 veterans will reside in the retirement home when it is fully occupied.

EVALUATION: This expenditure has achieved the purpose for which it was enacted.

- Service-connected disability compensation helps to compensate veterans who have mental or physical disabilities as a result of their service. This compensation assists in raising the standard of living in Oregon, brings federal funds into the state and, in many cases, keeps recipients off other social assistance programs.

- Veterans' pensions help to compensate veterans for their service to state and nation. Without this income supplement, some of these recipients would most likely utilize other social services.

- Federal educational benefits assist returning veterans in furthering their education. This falls within many of the Oregon Benchmarks. The more citizens who are educated to their potential, the better off the State of Oregon.

All three programs have achieved their purpose in a fiscally effective manner. [*Evaluated by the Department of Veterans' Affairs.*]

1.034 AGRICULTURE COST-SHARING PAYMENTS

Internal Revenue Code Section: 126
Oregon Statute: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1978

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Available	Not Available	$100,000
1999–01 Revenue Impact:	Not Available	Not Available	$100,000

DESCRIPTION: Under certain federal and state programs, governments make payments to taxpayers that represent a share of the costs of certain improvements to the land made by the taxpayer. These programs generally are designed to promote conservation, protect the environment, improve forests, or provide habitats for wildlife. Payments made under these programs are not included in the corporation or personal taxable income of the recipient. To qualify for the exclusion, the payment must not produce a substantial increase in the annual income from the property.

PURPOSE: To promote the conservation of soil and water resources and the protection of the environment.

WHO BENEFITS: Because these payments cannot be used to make improvements that increase the income-earning capacity of the property, the major beneficiaries are the general public to the extent they value conservation and improvements in the environment.

EVALUATION: This expenditure achieves its purpose. Numerous state and federal government grant and cost-sharing programs provide funds for land-related projects that will improve the environment. Some programs are geared to improving a land condition which has developed over a long period of time. Others relate to improving land which has been damaged in a specific storm event. Many projects may be too expensive for the landowner to afford alone. The cost-sharing and other assistance programs make these improvements possible.

Nearly all conservation-related cost-sharing programs in the state require or expect match dollars or in-kind services for each project. The match dollars and in-kind service dollars often exceed a 2:1 ratio. In this respect the program is working well. Additionally, it is likely that many of the conservation improvement projects that are presently being done on private land would not be possible without the assistance of the tax expenditure. The federal program for improving land or restoring it to its pre-storm condition, the Emergency Watershed Protection program, requires that a landowner provide 25 percent of the cost of the improvement or restoration work. The federal agencies that oversee the program are the Natural Resources Conservation Service of the U.S. Department of Agriculture and the U.S. Army Corps of Engineers. All Emergency Watershed Protection projects require a local sponsor which, in Oregon, has been the local soil and water conservation districts. The Emergency Watershed Protection projects that have been conducted, in response to the February 1996 flood, have all been successful. [*Evaluated by the Department of Agriculture.*]

1.035 CANCELLATION OF DEBT FOR FARMERS

Internal Revenue Code Sections: 108 and 1017
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1986

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$700,000	$700,000
1999–01 Revenue Impact:	Not Applicable	$700,000	$700,000

DESCRIPTION: The cancellation of debt for farmers is not included in taxable income. For other industries, the cancellation of debt is considered income that is taxable.

PURPOSE: To reduce the tax burden on farmers and to avoid forcing farmers to sell their farmland in order to pay large tax liabilities on income arising from canceled debt.

WHO BENEFITS: Farmers who have debt canceled by lenders.

EVALUATION: This tax expenditure achieves its purpose. There is little likelihood that farmers experiencing financial difficulty would have the ability to pay taxes on the canceled debt without selling the income-generating asset (i.e., the land) that is the livelihood of the operator. Unmeasurable benefits are stability in rural communities during severe economic downturns in the agriculture industry.

The benefits are well-targeted. It is unlikely that a qualified insolvent or bankrupt farmer would not utilize the exemption, and since the exemption is applicable only to producers who are in bankruptcy or insolvent, it is unlikely that any benefits are going to unintended recipients. [*Evaluated by the Department of Agriculture.*]

1.036 ENERGY CONSERVATION SUBSIDIES

Internal Revenue Code Section: 136
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1992

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	Included in 1.100	Included in 1.100
1999–01 Revenue Impact:	Not Applicable	Included in 1.100	Included in 1.100

DESCRIPTION: Residential energy customers can exclude from personal taxable income subsidies provided by electric and gas utilities for the purchase or installation of an energy conservation device. The part of the program that applied to businesses was repealed in 1996. Oregon legislation excluding these subsidies from taxation was enacted in 1981, so these payments would be exempt from Oregon's income tax even in the absence of the federal exclusion.

PURPOSE: To encourage customers to install energy-conserving devices.

WHO BENEFITS: Energy users who install conservation devices.

EVALUATION: See the evaluation of 1.100 Cash Payments for Energy Conservation.

1.037 CONTRIBUTIONS IN AID OF CONSTRUCTION FOR UTILITIES

Internal Revenue Code Section: 118(c),(d)
Oregon Statute: 317.013 (Connection to federal corporation taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1996

	Corporation	Personal	Total
1997–99 Revenue Impact:	$200,000	Not Applicable	$200,000
1999–01 Revenue Impact:	$200,000	Not Applicable	$200,000

DESCRIPTION: Contributions in aid of construction received by regulated water and sewage disposal utilities are not included in the utilities' gross income if the contributions are spent for the construction of new facilities within two years. Contributions in aid of construction are charges paid by utility customers, usually builders or developers, to cover the cost of installing facilities to service housing subdivisions, industrial parks, etc.

This tax treatment allows the utility to treat the contributed plant as a tax-free contribution to its capital rather than treating it as taxable income.

PURPOSE: To encourage the modernization of water and sewage facilities.

WHO BENEFITS: Oregon water utilities and ultimately their customers benefit because the utilities are better able to attract capital through contributions in aid of construction rather than from debt or equity financing sources.

EVALUATION: Prior to enactment, the federal corporation income tax liability on contributions in aid of construction was a serious drawback to utilities accepting contributions. For tax purposes, the utility was responsible for paying taxes on contributions in aid of construction. For ratemaking purposes, however, the income tax on contributed capital was not allowed to be recovered from customers through regulated utility rates.

After enactment, the utility benefits because the contribution is no longer considered taxable income for tax purposes. The change in the law did not directly affect regulated utility ratemaking. Ultimately, customers also benefit by having the utility add investment through contributions in aid of construction rather than an increased need to issue debt or equity. [*Evaluated by the Public Utility Commission.*]

1.038 EMPLOYER PAID TRANSPORTATION BENEFITS

Internal Revenue Code Section: 132(f)
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1992

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$17,000,000	$17,000,000
1999–01 Revenue Impact:	Not Applicable	$17,000,000	$17,000,000

DESCRIPTION: Employer payments for employee parking, transportation in a commuter highway vehicle, and transit passes are excludable from the personal taxable income of the employees. Parking facilities provided free of charge by the employer are also excludable from income. The Transportation Equity Act for the 21st Century (P.L. 105–178) passed in June 1998 includes several changes in qualified transportation benefits. Effective in tax year 1998, employees are allowed to elect taxable cash compensation in lieu of qualified transportation fringe benefits. Effective in taxable year 1999, the maximum exclusion for parking will be increased from $155 to $175 per month and the maximum exclusion for transit and commuter transportation will be increased from $60 to $65 per month. The maximum exclusion amounts will be indexed for inflation in five dollar increments after 1999. The exclusion for transit and commuter transportation will increase to $100 per month in 2002.

PURPOSE: To codify the standard practice of not taxing this benefit. The ceiling was established for parking benefits in order to limit that long standing subsidy. The exclusions for mass transit and commuter transportation were introduced to encourage mass commuting.

WHO BENEFITS: The subsidy provides benefits to both employees (more are employed and they receive higher total compensation) and to their employers (who have lower wage costs). The parking exclusion is more likely to benefit higher income individuals than do the transit and vanpool subsidies.

EVALUATION: Overall, this expenditure appears to achieve its purpose. The exclusion recognizes long-standing and generally accepted treatment of benefits by employees, employers and the Internal Revenue Service as not giving rise to taxable income. For Oregon, the exclusion also recognizes the difficulty of disconnecting the Oregon income tax from federal code.

The exclusion subsidizes employment in businesses and industries in which transportation fringe benefits are feasible and commonly used. Since these benefits are not equally feasible and common in all industries, the exclusion creates inequities in tax treatment among different employees and employers. For example, employer-provided parking is commonly provided at no cost to employees at suburban work sites; free parking is less common in developed central cities. Free employee parking also significantly underprices the cost of commuting, leading to more auto travel than would be the case otherwise.

Employer-provided transit passes and vanpools can be effective methods of encouraging the use of mass transit services rather than commuting by personal auto, thereby reducing traffic congestion and improving air quality. However, employer-provided transit passes and vanpools are common only in areas with well-developed public transportation systems. [*Evaluated by the Department of Transportation.*]

1.039 LIFE INSURANCE INVESTMENT INCOME

Internal Revenue Code Sections: 72, 101, 7702, and 7702A
Oregon Statutes: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1913

	Corporation	Personal	Total
1997–99 Revenue Impact:	$5,400,000	$147,700,000	$153,100,000
1999–01 Revenue Impact:	$6,000,000	$157,500,000	$163,500,000

DESCRIPTION: The investment income of life insurance and annuity contracts is not included in corporation or personal taxable income as it accrues or when it is received by beneficiaries upon the death of the insured.

PURPOSE: To promote the welfare of insurance beneficiaries.

WHO BENEFITS: Policyholders who purchase both life insurance and annuities for financial security for their families and themselves.

EVALUATION: This expenditure achieves its purpose. Often an annuity or life policy serves as an important retirement planning tool that underpins the financial welfare of Americans. Some people underestimate the financial loss their deaths could cause and so tend to be underinsured. If this is the case, some encouragement of the purchase of life insurance is warranted. A current income tax on these products would discourage ownership of adequate amounts of permanent insurance protection, which in turn could put more strain on government social services programs. Taxing this investment income might also reduce overall savings levels.

The practical difficulties of taxing this investment income and the desire not to add to the distress of heirs by taxing death benefits have discouraged many tax reform proposals covering life insurance. Taxing at the company level as a proxy for individual income taxation has been a suggested alternative. [*Evaluated by the Department of Consumer and Business Services.*]

1.040 WORKERS' COMPENSATION BENEFITS

Internal Revenue Code Section: 104(a)(1)
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1918

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$26,800,000	$26,800,000
1999–01 Revenue Impact:	Not Applicable	$29,000,000	$29,000,000

DESCRIPTION: Workers' compensation benefits to disabled workers, and to their families in cases of work-related death, are not included in personal taxable income. Benefits received through private accident, health, or disability insurance are not considered income and also are not taxed. The figure above is for workers' compensation only.

PURPOSE: To help compensate for the economic hardship imposed by injury, sickness, or death. Also to be consistent with the tax treatment of court awarded damages, which also are not taxed.

WHO BENEFITS: Workers receiving workers' compensation benefits. Under the provisions of Social Security law, workers' compensation benefits can be counted as income in determining Social Security benefits, so recipients of workers' compensation payments who also receive Social Security income may have their Social Security benefits reduced.

EVALUATION: This expenditure achieves its purpose. Generally, workers' compensation benefits paid to injured workers or their beneficiaries are less than wages earned by the worker prior to disability. By exempting injured workers' disability benefits from taxation, this tax expenditure essentially increases the replacement wage to injured workers. A similar outcome could be accomplished in other ways. For example, injured worker benefits could be increased, and be subject to taxation in such a manner that the effective after-tax replacement wage is commensurate with the tax-exempt benefit. Removal of the exemption without benefit increases would effectively reduce the injured workers' or beneficiaries' replacement wages. Consequently, the State of Oregon might spend more in social services to meet needs of injured workers or their beneficiaries. [*Evaluated by the Department of Consumer and Business Services.*]

1.041 CREDIT UNION INCOME

Internal Revenue Code Section: 501(c)(14)
Section 122 Fed. Credit Act (RVSC Sec. 1768)
Oregon Statute: 317.013 (Connection to federal corporation taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1951

	Corporation	Personal	Total
1997–99 Revenue Impact:	$3,600,000	Not Applicable	$3,600,000
1999–01 Revenue Impact:	$4,100,000	Not Applicable	$4,100,000

DESCRIPTION: Credit unions without capital stock and organized and operated for mutual purposes and without profit are exempt from corporation income taxation.

PURPOSE: Prior to 1951, the income of mutual banks, savings and loans, and credit unions were not taxed. In 1951, the exemption from mutual banks and savings and loans was removed, but credit unions retained their exemption. The rationale for the continued exemption for credit unions was not made explicit in the legislation. According to the Congressional Research Service, the reason may be that credit unions serve a unique niche in financial markets. They are non-profit cooperatives organized by people with a common bond that distinguishes them from the general public. They also are thought to be more likely to provide services to low-income individuals at rates lower than other financial institutions.

WHO BENEFITS: Members of credit unions, primarily by receiving services at lower rates than are available from other financial institutions. In Oregon the exemption affects 126 credit unions who have $55.8 billion in total assets and include over a million people as members.

EVALUATION: This expenditure achieves its purpose. Historically, credit unions were conceived to provide basic financial services to members who were typically out of the mainstream financial service lanes. They were generally lower income people. Today's average members are more affluent. The National Credit Union Administration is actively promoting a program to appeal to the under-served in an attempt to get back to their roots. Member benefits include lower interest rates on loans than in traditional markets, as well as higher interest rates on savings. It is not likely that these benefits could be provided as efficiently in a direct spending program. [*Evaluated by the Department of Consumer and Business Services.*]

1.042 LIFE INSURANCE COMPANY RESERVES

Internal Revenue Code Sections: 803(a)(2), 805(a)(2), and 807
Oregon Statute: 317.013 (Connection to federal corporation taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1984

	Corporation	Personal	Total
1997–99 Revenue Impact:	$8,800,000	Not Applicable	$8,800,000
1999–01 Revenue Impact:	$10,100,000	Not Applicable	$10,100,000

DESCRIPTION: In calculating corporation taxable income, most businesses cannot deduct expenses until the company becomes liable for paying them. Life insurance companies, however, can deduct additions to reserve accounts for future liabilities. This effectively allows them to offset current income with expenses that will not actually be paid until some future time period.

PURPOSE: To make tax rules consistent with standard industry accounting practices. For most regulated industries the tax code was written to be consistent with the accounting rules already used in those industries (in most cases dictated by state regulation). In the insurance industry it is common practice to use some form of reserve accounting in estimating net income, and those methods were adopted into the tax code when life insurance companies first became taxable in 1909.

WHO BENEFITS: Competitive pressures in the life insurance industry probably result in the benefits being passed on to policyholders in the form of lower premiums.

EVALUATION: This expenditure achieves its purpose. Life insurance companies incur expenses in the current year for underwriting and acquisition of business. In addition, they are allowed to deduct from current income those expenses that they expect to pay out as benefits in the future. This is a timing issue. This is the standard method of accounting for insurance regulatory purposes, where the primary goal is to assure that a company will be able to pay its promised benefits. Ultimately, if this tax expenditure were repealed, costs would be higher for life insurance companies. This could result in reductions in policyholder dividends and excess interest credits, or reductions in services to policyholders. [*Evaluated by the Department of Consumer and Business Services.*]

1.043 IMPUTED INTEREST RULES

Internal Revenue Code Sections: 163(e), 483, 1274, and 1274A
Oregon Statute: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1964

	Corporation	Personal	Total
1997–99 Revenue Impact:	$100,000	$1,400,000	$1,500,000
1999–01 Revenue Impact:	$100,000	$1,400,000	$1,500,000

DESCRIPTION: For debt instruments that do not bear a market rate of interest, the Internal Revenue Service assigns or "imputes" a market rate to them to estimate interest payments for tax purposes. The imputed interest must be included as income to the recipient and is deducted by the payer. There are several exceptions to the general rules for imputing interest on these debt instruments. Debt associated with the sale of property when the total sales price is no more than $250,000, the sale of farms or small businesses by individuals when the sales price is no more than $1 million, and the sale of a personal residence are not subject to the imputation rules at all. Debt instruments for amounts not exceeding an inflation-adjusted maximum (currently about $3 million), given in exchange for real property, may not have imputed to them an interest rate greater than nine percent. This tax expenditure is the revenue loss caused by these exceptions.

PURPOSE: To reduce the tax burden on the sales of homes, small businesses, and farms.

WHO BENEFITS: Sellers of residences, small businesses, and farms who structure the sales to defer income to later years.

EVALUATION: According to the Congressional Research Service, the imputed interest rules relating to property sales were enacted to prevent taxpayers from overstating the price, and understating the interest rate, to take advantage of the lower tax rate on capital gains. The Tax Reform Act of 1986 removed the preferential treatment of capital gains, greatly reducing such abuses. The Taxpayer Relief Act of 1997, however, reduced the tax rates for capital gains, so the imputed interest rules are again viewed as a needed tool to discourage taxpayers from overstating the price and understating the interest rate when selling property. [*Evaluated by the Department of Revenue.*]

1.044 GAIN ON NON-DEALER INSTALLMENT SALES

Internal Revenue Code Sections: 453 and 453A(b)
Oregon Statute: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

	Corporation	Personal	Total
1997–99 Revenue Impact:	$2,300,000	$2,800,000	$5,100,000
1999–01 Revenue Impact:	$2,300,000	$2,800,000	$5,100,000

DESCRIPTION: Persons who do not deal regularly in selling property (i.e., non-dealers) are allowed to report some sales of property for corporation and personal tax purposes under a special method of accounting called the installment method. Under the installment method, gross profit from the sale is prorated over the years during which the payments are received. This conveys a tax advantage compared to being taxed in full in the year of sale because the taxes are deferred to future years.

PURPOSE: To match the timing of tax payments to the timing of the cash flow generated by the sale of the property. Requiring an up-front payment of taxes by a seller who won't receive the bulk of payments for the property until the future can place a heavy burden on infrequent sellers of property.

WHO BENEFITS: Infrequent sellers of property who sell the property on an installment basis.

EVALUATION: The installment sales rules have always been pulled between two opposing goals: taxes should not be avoidable by the way a deal is structured, but they should not be imposed when the money to pay them is not available.

Trying to collect taxes from taxpayers who do not have the cash to pay is administratively difficult and strikes many as unfair. After having tried many different ways to balance these goals, lawmakers have settled on a compromise that denies the advantage of the method to taxpayers who would seldom have trouble raising the cash to pay (retailers, dealers in property, investors with large amounts of sales) and continues to permit it to small, non-dealer transactions.

According to the Congressional Research Service, present law results in modest revenue losses and probably has little effect on economic incentives. [*Evaluated by the Department of Revenue.*]

1.045 GAIN ON LIKE-KIND EXCHANGES

Internal Revenue Code Section: 1031
Oregon Statute: 316.048 and 317.013 (Connections to federal personal and corporation taxable incomes)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

	Corporation	Personal	Total
1997–99 Revenue Impact:	$1,800,000	$2,100,000	$3,900,000
1999–01 Revenue Impact:	$1,800,000	$2,100,000	$3,900,000

DESCRIPTION: Like-kind exchanges are exchanges of properties that are of the same general type, but that may be of very different quality and use, such as real estate. No gain or loss is recognized as corporation or personal taxable income on the exchange so no tax is paid.

PURPOSE: To recognize that the investment in the new property is much like a continuation of the investment in the old and, therefore, is not a taxable event.

WHO BENEFITS: Taxpayers who engage in exchanges of like properties. This type of activity is concentrated in the real estate sector.

EVALUATION: According to the Congressional Research Service, this provision is used primarily by investors in real estate to alter their holdings without paying tax on their appreciated gain. Allowing these tax-free exchanges somewhat reduces the "lock-in" effect that the current tax treatment of capital gains creates, but it is hard to justify restricting the like-kind exchange rules to relatively sophisticated real estate transactions. By favoring real estate over other types of assets, this provision may result in unequal treatment of taxpayers and slower economic growth. [*Evaluated by the Department of Revenue.*]

1.046 ALLOWANCES FOR FEDERAL EMPLOYEES ABROAD

Internal Revenue Code Section: 912
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1943

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$400,000	$400,000
1999–01 Revenue Impact:	Not Applicable	$400,000	$400,000

DESCRIPTION: U.S. federal civilian employees working abroad are allowed to exclude from personal taxable income certain special allowances that are primarily for the costs of living abroad: such as the costs of housing, education, and travel.

PURPOSE: To offset the extra living costs of working abroad and to encourage employees to accept these assignments.

WHO BENEFITS: Federal civilian employees working abroad.

EVALUATION: This tax expenditure achieves its purpose. It provides an inducement to federal employees who might otherwise choose not to work in foreign countries. It is likely that employees would not endure the challenge of living abroad without offsetting adjustments. The tax expenditure also eliminates the need for assigning value to and accounting for the costs of living abroad as compared to the U.S. [*Evaluated by Employment Department.*]

1.047 INTEREST ON OREGON STATE AND LOCAL DEBT

Internal Revenue Code Sections: 103, 141, 142, 143, 144, 145, 146, and 501(c)(3)
Oregon Statutes: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1913

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$78,900,000	$78,900,000
1999–01 Revenue Impact:	Not Applicable	$83,700,000	$83,700,000

DESCRIPTION: Oregon does not include interest income from Oregon state or local government obligations in personal taxable income (it is included in corporation taxable income). These obligations are primarily bonds issued by the State of Oregon and local government taxing districts such as cities, counties, and school districts.

These bonds fall into two categories. First, there are "governmental" bonds where the bond proceeds generally are used to build capital facilities that are owned and operated by governmental entities and serve the general public interest, such as highways, schools, and government buildings. The majority of the tax benefit falls in this category.

Second, there are qualified "private activity" bonds where a portion of the bond benefits accrue to individuals or businesses rather than to the general public. These are specifically listed in code and include the following state and local government bonds: industrial development bonds for energy production facilities; sewage, water and hazardous waste facilities bonds; bonds for owner-occupied housing; bonds for rental housing; small-issue industrial development bonds; bonds for high-speed rail; bonds for private airports, docks, and mass-commuting facilities; student loan bonds; bonds for private nonprofit hospital facilities; and bonds for veterans' housing. Many of these bonds are subject to the state private activity bond annual volume cap.

Interest income on these qualified private activity bonds is exempt from federal income tax as well as Oregon income tax. There are other non-qualified private activity bonds. The interest earned on these bonds is taxable at the federal level but not at the state level (1.096 Local Private Activity Bond Interest).

The tax benefit estimates above are based on the excluded interest income on both the governmental bonds and the qualified private activity bonds.

PURPOSE: To lower the cost of borrowing for Oregon state and local governments.

WHO BENEFITS: In 1996, approximately 64,000 Oregon taxpayers received roughly $440 million in interest on Oregon state or local government debt obligations, or an average of $6,850 per return. Investors holding such debt instruments may claim this income tax-free. However, financial markets compensate for the tax-free status of state and local government debt by reducing the rate of return on that debt. Therefore, the primary beneficiaries are the State of Oregon and local governments, whose cost of borrowing is reduced.

EVALUATION: This tax expenditure achieves its purpose. Borrowing costs for the state of Oregon and Oregon local governments are reduced because of the exemption from state income taxes on interest earned on bonds issued by these public bodies. The lower costs associated with lower bond interest rates benefits Oregon citizens by reducing the costs of public investment in, for example, such infrastructure needs as, schools, roads, sewers, water systems, colleges and correctional facilities among many other projects.

Investors who are subject to an Oregon state income tax liability are willing to accept lower interest rates on Oregon state and Oregon local government bonds because the interest income they earn from these investments are excluded from state income taxes.

The State income tax exclusion for interest on Oregon bonds helps to create demand for these securities which improves their marketability and attracts not only in-state investors, but also national institutional and other national investors who wish to purchase tax-exempt bonds which have a strong market demand and reputation.

Even though most of these national investors are not subject to Oregon state income taxes, they are willing to pay higher prices and accept lower interest rates because of the good market performance of Oregon bonds. Oregonians benefit from these out-of-state purchases because Oregon governments can finance needed public activities at lower costs and state level income tax revenue flows are not affected. [*Evaluated by the State Treasury.*]

1.048 CAPITAL GAINS ON INHERITED PROPERTY

Internal Revenue Code Sections: 1001, 1002, 1014, 1023, 1040, 1221, and 1222
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$194,400,000	$194,400,000
1999–01 Revenue Impact:	Not Applicable	$225,100,000	$225,100,000

DESCRIPTION: When property is transferred upon death, any capital gains accrued but not recognized on the property during the decedent's ownership are excluded from personal taxable income. The new basis for the heir is set to the market value on the date of the decedent's death.

PURPOSE: To provide tax relief to heirs who inherit property. A rationale may be that estates are subject to taxation at the federal level.

WHO BENEFITS: Heirs who inherit property.

EVALUATION: This expenditure achieves its purpose of providing tax relief to heirs. According to the Congressional Research Service, however, the failure to tax capital gains at death is probably one of the primary causes of the lock-in effect, where taxpayers hold particular assets longer than they otherwise would specifically to avoid the tax consequences of selling the assets. The lock-in effect causes investors to base their investment decision on the tax consequences rather than on the inherent economic soundness of the investments, resulting in slower economic growth.

There are, however, several problems with taxing capital gains at death. There are administrative problems, particularly for assets held a long time where the heirs do not know the basis. In addition, taxing capital gains at death may often force heirs to sell the assets in order to pay the taxes. [*Evaluated by the Department of Revenue.*]

1.049 CAPITAL GAINS ON GIFTS

Internal Revenue Code Sections: 1001, 1002, 1015, 1221, and 1222
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$19,300,000	$19,300,000
1999–01 Revenue Impact:	Not Applicable	$20,700,000	$20,700,000

DESCRIPTION: When a gift is made, any capital gain accrued on the property while held by the donor is excluded from personal taxable income until the recipient disposes of the property. The recipient is taxed on the capital gains at the time of sale of the property.

PURPOSE: To allow the transfer of property as a gift without imposing a tax burden on the donor who, without selling the property, may not be able to pay the tax.

WHO BENEFITS: Donors and recipients of gifts.

EVALUATION: Not Evaluated.

1.050 GAIN ON INVOLUNTARY CONVERSIONS IN DISASTER AREAS

Internal Revenue Code Section: 1033(h)
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1996

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$100,000	$100,000
1999–01 Revenue Impact:	Not Applicable	$100,000	$100,000

DESCRIPTION: When a taxpayer is reimbursed for damaged property, by insurance for example, it is possible for the recovery to exceed the taxpayer's basis in the property. In those cases the property is "involuntarily converted" into cash and is generally taxed unless the proceeds are used to replace the damaged property with similar property within a specified period.

This deferral of gain provides special rules for a taxpayer's principal residence or any of its contents when involuntarily converted if the property is located in a Presidentially declared disaster area. In the case of unscheduled personal property (property that is not specified but is insured), no gain is recognized as a result of any insurance proceeds. In addition, the replacement period is increased from two years to four years.

PURPOSE: To defer or reduce the tax burden for taxpayers who experience large losses due to a natural disaster.

WHO BENEFITS: Taxpayers in Presidentially declared disaster areas who experience an involuntary gain as a result of being reimbursed for damaged property.

EVALUATION: Not Evaluated.

1.051 VOLUNTARY EMPLOYEES' BENEFICIARY ASSOCIATIONS

Internal Revenue Code Sections: 419, 419A, and 501(c)(9)
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1928

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$3,500,000	$3,500,000
1999–01 Revenue Impact:	Not Applicable	$3,900,000	$3,900,000

DESCRIPTION: A Voluntary Employees' Beneficiary Association (VEBA) provides life, sickness, accident, and other insurance and fringe benefits to its employee members, their dependents, and their beneficiaries; these benefits are not included in personal taxable income. Also, employer contributions to fund future benefit payments are deductible.

PURPOSE: To promote the provision of life, sickness, accident, and other insurance and fringe benefits and treat VEBA benefits identical to employer provided benefits.

WHO BENEFITS: Recipients of the program benefits and employers who contribute.

EVALUATION: This tax expenditure achieves its purpose and is one means of providing critical benefits. The tax expenditure has the potential for relieving reliance on the state to provide these benefits to uninsured people. An employer that does not directly purchase life, health, or disability insurance may provide those benefits through a VEBA. The benefit to the employer involves certain tax advantages pertaining to contributions, within specified limits. This tax expenditure increases insurance coverage among taxpayers in a non-discriminatory manner and who would otherwise not purchase or could not afford such coverage. [*Evaluated by the Employment Department.*]

1.052 RENTAL ALLOWANCES FOR MINISTERS' HOMES

Internal Revenue Code Section: 107
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1921

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$2,100,000	$2,100,000
1999–01 Revenue Impact:	Not Applicable	$2,500,000	$2,500,000

DESCRIPTION: Ministers can exclude from personal taxable income the fair rental value of a church-owned or church-rented home furnished as part of his or her compensation, or a cash housing allowance paid as part of the minister's compensation.

PURPOSE: To avoid the difficulty in putting a value on the provision of a church-provided rectory and to provide equal treatment between ministers who receive a cash allowance and those who have their home included in their compensation package.

WHO BENEFITS: Ministers who receive a housing allowance or who live in a church provided home.

EVALUATION: Not Evaluated.

1.053 MILITARY DISABILITY BENEFITS

Internal Revenue Code Section: 104(a)(4)
Oregon Statute: 316.048 (Connection to federal personal taxable income)
Federal Law Sunset Date: None
Year Enacted in Federal Law: 1942

	Corporation	Personal	Total
1997–99 Revenue Impact:	Not Applicable	$700,000	$700,000
1999–01 Revenue Impact:	Not Applicable	$700,000	$700,000

DESCRIPTION: Members of the armed forces on or before September 24, 1975 are eligible for the exclusion of disability pay from personal taxable income. The amount of disability pay is calculated as the greater of:

- The percentage of disability multiplied by the terminal monthly basic pay; or
- The terminal monthly basic pay multiplied by the number of service years times 2.5.

Only the amount calculated under the first method is excluded from taxable income.

Members of the armed forces who joined after September 24, 1975, may exclude Department of Defense disability payments equivalent to disability payments they could have received from the Veterans Administration. Otherwise, disability pensions may be excluded only if the disability is a combat-related injury.

PURPOSE: To treat veterans' disability benefits the same as compensation for injuries and sickness such as workers' compensation payments.

WHO BENEFITS: For veterans joining on or before September 24, 1975, those who retire on disability. For all others, only those who retire due to a combat-related injury. During fiscal years 1995 and 1996, eight Oregon National Guard soldiers and airmen received this benefit with total compensation paid just over $112,000. It is not precisely known how many Oregon veterans from other branches of the military receive this benefit.

EVALUATION: This tax expenditure achieves its purpose and is a valuable benefit to members of the Oregon National Guard, both Army and Air, as well as other military personnel. National Guard members may receive these benefits because of injuries incurred while performing Inactive Duty Training whereas Active Guard Reserve soldiers may have incurred injuries at any time during their tour of duty and are no longer capable of performing their jobs. While these compensation payments may not be a great deal of money, they may be the only income these soldiers and airmen have because their injuries prevent them from obtaining adequate full-time employment. The federal tax code excludes from taxation disability compensation from the Veterans' Administration as it results of personal injury or sickness from duty in the armed forces. The state of Oregon should continue to treat these benefit payments the same as the Internal Revenue Service. [*Evaluated by the Military Department.*]