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THE GRADUATED PERSONAL INCOME TAX ASSESSMENT: FREQUENTLY ASKED QUESTIONS

1. How does the graduated income tax assessment work?
It is calculated as a percentage of total state income taxes paid. Total taxes include withholding, estimated quarterly payments and final payments when the return is filed minus refunds. The percentage increase varies from 0 to 9% of taxes based on the adjusted gross income of the taxpayer. Under the assessment, taxpayers would figure their state taxes just as they do now. Total tax liability (the number taken from the tax tables minus credits) would then be adjusted by the graduated assessment rate. For example, a taxpayer with a tax liability of $2,000 and an assessment rate of 5% (this would be the rate for a single filer with income between $35,000 and $50,000) would pay an additional $100 per year.

The following table shows how the assessment rate is linked to taxpayer income and filing status.

Tax Bracket **(SINGLE)** (Adjusted Gross Inc)	**Assessment Rate**	Tax Bracket **(JOINT)** (Adjusted Gross Inc)
Below $10,000	0%	Below $20,000
$10,000 - $20,000	1%	$20,000 - $40,000
$20,000 - $25,000	2%	$40,000 - $50,000
$25,000 - $30,000	3%	$50,000 - $60,000
$30,000 - $35,000	4%	$60,000 - $70,000
$35,000 - $50,000	5%	$70,000 - $100,000
$50,000 - $70,000	6%	$100,000 - $140,000
$70,000 - $90,000	7%	$140,000 - $180,000
$90,000 - $120,000	8%	$180,000 - $240,000
Above $120,000	9%	Above $240,000

2. How does the assessment differ from an income tax surcharge?
The assessment is a form of income tax surcharge. This is because it applies to taxes paid rather than income. For example, an assessment rate of 5% means 5% of taxes paid. This differs from an income tax rate change. Income tax rates are applied to taxable income. A 10% surcharge is equivalent to a 1% rate increase for a taxpayer paying 10% of her taxable income in taxes. The assessment differs from a standard surcharge because it is graduated, with higher assessment rates applied to those with higher income levels. A standard surcharge is a fixed percentage increase based on taxes paid.

3. How does the graduated assessment differ from the "surcharge" approved by the Legislature in 1982 during the last major state budget crisis?
In 1982 Oregon had 5 different income tax rates ranging from 4% to 10% of taxable income. The Legislature bumped up each of the 5 rates for a three year period (1982-84). The increases were larger for the higher rates. The 4 % rate was increased to 4.2 % and the 10 % rate was temporarily increased to 10.8%. Since the increases applied to taxable income and not to tax owed, the 1982 "surcharge" was really a graduated rate adjustment and not a surcharge.

4. How does it differ from Measure 28?
Measure 28, rejected by voters in January of 2003, was a rate increase and not a surcharge. It proposed raising the top Oregon income tax rate from 9 % to 9.5%. Unlike the 1982 tax increase, Measure 28 left the two lower rates (5% and 7%) unchanged.

5. How much money is the graduated assessment expected to raise for the state?
The state budgets on a two-year basis. The current budget started on July 1, 2003 and will end June 30, 2005. The graduated income tax assessment will generate an estimated $544.6 million for the two year period. This is about 5% of the state's General Fund budget for the coming two years. The General Fund is used primarily for education, human services and public safety.

6. How long will the assessment last?
It applies to the 2003, 2004 and probably 2005 tax years. Returns due on April 15 following these years will reflect the assessment. The third year of the assessment—2005—is automatically revoked if the state's revenue forecast rises sufficiently. The forecast released in December of 2004 will be compared with the forecast used for the Legislature's just finished budget. If it shows a projected ending balance exceeding 4% of General Fund expenditures, the assessment will not be applied to the 2005 tax year. The ending balance is currently projected to be less than 1%.

7. Is the personal income tax assessment the only major tax change approved by the Legislature this past session?
The personal income tax assessment is part of a larger tax package designed to balance the state budget for the 2003-05 budget period. Most of these other components are included in the same piece of legislation that contains the income tax assessment. These other elements include an increase in the corporate income and excise minimum tax, a 3-year reduction in all corporate income tax credits, a reduction in corporate export tax incentives, a smaller deduction for corporate dividends received from subsidiaries, a smaller discount for early payment of property taxes, a phase-out of Oregon's expanded elderly medical deduction as income rises and the elimination of favorable state tax treatment of SUV purchases made by businesses. These other elements combined are expected to raise $246.5 million for the current two-year budget period.

8. How does this tax package affect Oregon's overall tax burden compared to other states?
Lags in data from the other states prevent a direct answer to this question, but historical data can be used to shed light on this issue. The most accurate way to measure overall tax burden is to sum all state and local taxes and then divide by total personal income of Oregon residents. Unfortunately, the latest combined state and local data for all states is for the 1999-2000 fiscal year. Oregon taxes accounted for 10.6 % of personal income for that year. 39 states had a higher tax burden at that time. State only tax data is more timely. Oregon's total state taxes were 5.3% of personal income for the year ending June 30, 2002. This gave Oregon the 44th highest tax burden among the states in 2001-02. Taking the September 2003 revenue forecast and adjusting the personal and corporate income tax for the components of the legislatively approved tax

package would raise Oregon's state tax burden to 5.95 %. The higher rate is due to an assumed bounce back in revenue as well as the effects of the new law. If all the other states maintained the same tax burden as a percentage of their income, Oregon's rank would move to number 34 for the 2003-04 fiscal year. This ranking should be viewed skeptically because a number of states have raised taxes in response to their individual budget crisis. This may affect Oregon's ultimate ranking for the 2003-04 year.

9. How do the mechanics of the graduated assessment compare with Oregon's famous 2 % kicker law?

The 2% surplus kicker works like a surcharge in reverse. After the two-year budget period ends, the state compares General Fund revenue (primarily personal and corporate income taxes) with the forecast made by the State Economist at the time the budget was approved by the Legislature. If actual revenue exceeds the forecast by more than 2%, a refund is calculated. The refund is determined by dividing the amount of revenue above the forecast (as long as it exceeds 2%) by the estimated total tax liability for the year. The result is a percentage that is then applied to each taxpayer's taxes paid for that year. This is the same way a traditional surcharge works only it is used for a temporary refund rather than temporary tax increase. The graduated assessment is based on a percentage of taxes paid just like the kicker. But unlike the kicker, which is a fixed percentage for all taxpayers regardless of income, the assessment percentage is then adjusted for income.

10. Why are single taxpayers charged a higher assessment than joint taxpayers with the same income?

The assessment rate applies to income brackets. The brackets used for taxpayers who file jointly are exactly double the brackets for single taxpayers. For example, the 1% rate applies to single taxpayers with income between $10,000 and $20,000. It applies to married couples with joint income between $20,000 and $40,000. This is consistent with Oregon's current 5, 7 and 9% tax brackets. The income levels that these rates are applied to are exactly double for married couples. This prevents the problem of a "marriage penalty" in which two taxpayers living together would pay less in state taxes if they were not married. It does mean that a single taxpayer will pay more than a joint taxpayer with the same income.

11. Can the state income tax assessment be deducted from my federal tax return?

Yes, all state and local income taxes can be deducted from adjusted gross income for purposes of calculating federal taxes. However, taxpayers must itemize their deductions on their federal return to receive the deduction. Those that use the standard deduction would not be able to deduct the additional state income tax assessment. Federal deductibility will offset about 17% of the assessment. However, the effect on individual taxpayers depends on their federal tax bracket. The higher the bracket the more valuable deductibility becomes. For example, for the taxpayer in the 35% federal tax bracket, each dollar deducted reduces federal taxes by 35 cents. For the taxpayer in the 15% bracket, each dollar deducted reduces federal taxes by 15 cents.

12. Does the state income tax assessment offset the effects of the recently approved federal income tax reductions?

Congress passed and the President signed the Jobs and Growth Tax Relief Reconciliation Act of 2003 in May of this year. The federal tax package will reduce federal taxes paid by Oregon residents by almost exactly $1 billion in the 2003 tax year. The state income tax assessment, including the effects of federal deductibility, will increase taxes for Oregon residents by about $173 million. This means that the assessment will offset about 17.3% of the federal tax reduction in the current tax year. Put alternatively, it means Oregon taxpayers will receive about 83% of

their federal tax reductions after netting out the effects of the state assessment. In nearly all cases, taxpayer's federal tax reduction will exceed their graduated assessment. For example, the average joint taxpayer with adjusted gross income of $60,000 can expect to receive an average federal tax reduction of $475 in 2003 while paying an additional $98 through the state income tax assessment.

13. How much more will the average tax payer have to pay under the assessment?
The average state tax burden will rise by $133 for the 2003 tax year. Increased federal deductions will reduce the net increase for the average taxpayer to $111. However, it is important to keep in mind that the average includes taxpayers in very different circumstances. High paid corporate executives and professional athletes are included in the average along with teenagers working part-time in the food service industry. The average for joint returns is a better measure of how the assessment will affect families. The average joint return is expected to report $59,335 in adjusted gross income for the 2003 tax year. These filers are expected to pay an additional $98 in state taxes and $10 less in federal taxes due to increased deductions. This leaves a net annual increase of $88 for the average taxpayer filing jointly.

14. How will the graduated assessment affect taxpayers in different circumstances?
The assessment will vary considerably among taxpayers because of its graduated structure. The assessment rate rises with the income of the taxpayer. This means that higher income taxpayers will pay proportionately more. The amount of the assessment will depend on taxes paid (the base) and adjusted gross income which determines the rate. The best way to look at how the assessment affects different taxpayers is to look at examples. When considering the examples it is important to keep in mind that situations vary considerably even for taxpayers with the same income.

The following examples are intended to be illustrations. They do not include the specific credits and sources of income that complicate many returns. The total assumed amount of deductions includes federal taxes paid (up to $3,500) and either itemized deductions or the standard deduction. Those that use the standard deduction will not be able to deduct the additional state income tax caused by the graduated assessment. The calculations apply to the 2003 tax year. For purposes of calculating the impact of the income tax assessment the two key factors are Oregon tax liability (last year's tax would be a good indication if income hasn't changed much) and adjusted gross income. These two factors will determine the income tax assessment for each taxpayer.

Example 1
Filing Status: Single with no dependents
Adjusted Gross Income (AGI): $31,000
Deductions: Standard
Oregon Tax Liability: $2,077
Income Tax Assessment: $83

Example 2
Filing Status: Single with no dependents
Adjusted Gross Income (AGI): $60,000
Deductions: Itemized @ $15,000
Oregon Tax Liability: $3,724
Income Tax Assessment: $223
Increased Federal Deduction: $56
Net Tax Change: $167

Example 3
Filing Status: Single/Head of Household with one dependent
Adjusted Gross Income (AGI): $25,000
Deductions: Standard
Oregon Tax Liability: $1,269
Income Tax Assessment: $13

Example 4
Filing Status: Joint with two dependents
Adjusted Gross Income (AGI): $38,000
Deductions: Standard
Oregon Tax Liability: $2,661
Income Tax Assessment: $27

Example 5
Filing Status: Joint with two dependents
Adjusted Gross Income (AGI): $80,000
Deductions: Itemized @ $17,000
Oregon Tax Liability: $4,732
Income Tax Assessment: $237
Increased Federal Deduction: $36
Net Tax Change: $201

Example 6
Filing Status: Joint with two dependents
Adjusted Gross Income (AGI): $150,000
Deductions: Itemized @ $23,000
Oregon Tax Liability: $11,080
Income Tax Assessment: $776
Increased Federal Deduction: $194
Net Tax Change: $582

Example 7
Filing Status: Joint with no dependents
Adjusted Gross Income (AGI): $250,000
Deductions: Itemized @ $23,000
Oregon Tax Liability: $19,450
Income Tax Assessment: $1,751
Increased Federal Deduction: $578
Net Tax Change: $1,173