

Corporate Apportionment for Taxable Income

House Interim Committee on Revenue

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Outline

- Methods of Determining Income Taxed by Each State
- Federal Limits Affecting Taxation and Apportionment
- Brief National Background (UDITPA)
- Example of Factor-Based Apportionment Formula for one Business
- Brief Oregon History
- Implications of Apportionment Calculation
- U.S. States' Apportionment Factors

Methods of Determination of Income taxed by States

Income tax is based on Net Income (analogous to profit)

- Tax base is Taxable Revenue minus Allowed Deductions

How Much Income of A Multistate business is taxed by each state?

Separate Accounting by State

- A business with locations in multiple states calculates the income for each state separately
- States have moved away from this because of vulnerability to tax avoidance

Apportionment of Business Income to States using a Formula

- Unitary Business Principle (Treat multiple businesses that act as single economic unit as single unit)
- Apportionment Factors can include
 - Property
 - Payroll
 - Sales
- States have moved toward higher-weights on Sales Factor to avoid discouraging additional property and payroll in state
- Some income (completely unrelated to business) is allocated to specific states and not apportioned

Federal Limits on State Taxes*

* As described by an economist (not a lawyer)

Combined Restrictions

- **Substantial Nexus** – Requires a meaningful connection between the state and taxpayer activity/property subject to tax
- **Fair Apportionment**
 - If every state used same method, no more than 100% of income apportioned
 - Apportionment formula must reasonably reflect income-generation within the state
- **Non-Discrimination**
 - Tax applies neutrally to in-state and out-of-state businesses
 - Rational basis for different tax treatment (e.g. different treatment by industry is allowable if it serves a governmental interest)
- **Public Law 86-272** limits state ability to tax a business that is only soliciting sales of tangible personal property in the state

Sources of Restrictions

- Constitutional
 - Due Process
 - Commerce Clause
 - Equal Protection
- Public Law 86-272

Uniform Division of Income for Tax Purposes Act (UDITPA)

UDITPA is model legislation aimed at standardizing apportionment

- **Provided calculation of Payroll, Property, and Sales factors for apportionment**
- **Recommended equally weighted 3-Factor Formula**

States began adopting UDITPA model legislation in late 1950s.

Prior to adoption of UDITPA, states used variable methods

- Led to compliance burdens
- Potential double taxation by states

Congressional Intervention became likely

- P.L. 86-272 passed in 1959

UDITPA Goals

- Distinguish apportionable and non-apportionable income
- States (can) tax exactly 100% of apportionable income
- Uniformity for simpler compliance and administration
- Tax business income where business activity occurs
- Avoid federal preemption and operate within federal limits

Example of Factor-Based Apportionment

Example Business

	\$ Millions		
	Property	Payroll	Sales
Oregon	\$10.0	\$30.0	\$20.0
Washington	\$15.0	\$20.0	\$50.0
California	\$5.0	\$10.0	\$30.0
Total	\$30.0	\$60.0	\$100.0

Oregon Factors

Property	Payroll	Sales
33%	50%	20%

Hypothetical Oregon Apportionment Percentages

Even-weighted factor:	34.4%
Double-weighted sales factor:	30.8%
Single-Sales Factor:	20.0%

Brief Oregon History with Most Significant Updates

Oregon Adopted UDITPA in 1965

Oregon moved to “Single Sales Factor” Apportionment

Apportionment Formula Weights			
Tax Year Range	Sales Weight	Payroll Weight	Property Weight
12/31/1990 and earlier	33%	33%	33%
1/1/1991 to 4/30/2003	50%	25%	25%
5/1/2003 to 6/30/2005	80%	10%	10%
7/1/2005 to current	100%	0%	0%

Sales in Oregon (for both goods and services) is the numerator for the sales factor.

In 2017, Oregon changed determination of location of sales of services to be where the service is received, rather than where the costs were incurred (“cost of performance” to “market”)

- Example: Software Consulting business performing their work at a location out-of-state selling services to Oregon customers
 - Market Based (current law): Sales treated as Oregon Sales because Oregon is the Market
 - Cost-of-Performance: Sales would NOT be Oregon Sales because costs incurred outside Oregon

Implications of Tax Calculation

Federal Taxable Business Income

+ Oregon Additions

- Oregon Subtractions

= Oregon Tax Base Before Apportionment
X Multiplied by Apportionment Percent

Income Apportioned to Oregon

- Oregon Net Loss Deduction

= Oregon Taxable Income

- (By Design) Differences between Oregon and Federal Tax base are included before apportionment.
- Most corporate tax incentives are implemented as credits. Otherwise, the benefit is “diluted” by apportionment

Apportionment Methods of Other States

- 33 States use single sales factor
- 4 states use equal-weighted
- 2 states use double-weighted sales
- 6 states use other methods
(usually, option between single sales and double-weighted sales)
- 5 have no relevant state tax
(NV, OH, SD, WA, WY)

Source: [Federation of Tax Administrators \(2023\)](#) with update for TN

Thank You

