Oregon is one of nine states that currently allow taxpayers to claim federal income taxes paid as a deduction on personal income tax forms. Under current law, Oregon taxpayers can deduct up to $3,000 of federal personal income tax on their Oregon tax returns. This analysis assesses the impact of two possible changes to the current deduction on elderly Oregonians. One possible change would increase this limit from $3,000 to $5,000. A second alternative would eliminate the limit altogether, allowing Oregon taxpayers to deduct all of their federal personal income tax.

### Distributional Effects of a Deduction for All Federal Personal Income Tax

The following table shows the distributional consequences, for elderly Oregonians in 2000, of removing the $3,000 limit on the deduction for federal personal income taxes paid. More than three-fourths of the resulting tax reduction for the elderly would be received by the wealthiest 6 percent of elderly Oregon residents—those with incomes over $100,000. Their average tax cut would be over $4,000. The lowest-income 73 percent of elderly Oregon residents would receive an average tax cut of four dollars. Only 25 percent of elderly Oregon taxpayers would see any reduction in their Oregon personal income tax from the removal of the $3,000 limit.

#### Effect of Increasing the Deductibility of Federal Income Taxes

<table>
<thead>
<tr>
<th>Oregon Elderly Residents by Income Group, 2000</th>
<th>Deduction Limited to $5,000</th>
<th>Unlimited Deduction</th>
</tr>
</thead>
<tbody>
<tr>
<td>Income Group</td>
<td>Average Tax Cut</td>
<td>% of Total Tax Cut</td>
</tr>
<tr>
<td>Less than $25,000</td>
<td>46%</td>
<td>0%</td>
</tr>
<tr>
<td>$25,000-$50,000</td>
<td>27%</td>
<td>7%</td>
</tr>
<tr>
<td>$50,000-$75,000</td>
<td>15%</td>
<td>98%</td>
</tr>
<tr>
<td>$75,000-$100,000</td>
<td>6%</td>
<td>171%</td>
</tr>
<tr>
<td>Over $100,000</td>
<td>6%</td>
<td>177%</td>
</tr>
<tr>
<td>Addendum: Under $50,000</td>
<td>73%</td>
<td>3%</td>
</tr>
</tbody>
</table>

Source: ITEP Microsimulation Tax Model, October 2, 2000

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1. This analysis includes all families and individuals in which at least one filer is over 65 years old.
The table above also shows the distributional effects of increasing the cap on the federal income tax deduction from the current $3,000 to $5,000. While the distribution of the tax cuts from such a change would be less regressive, this tax cut would also disproportionately benefit higher-income Oregonians.

The lowest-income 73 percent of elderly Oregonians would receive only 5 percent of the tax cut from this change, and their average tax cut would be $3. The best-off 6 percent of Oregonians over 65 would receive thirty percent of the benefit. And three quarters of elderly Oregonians would receive no tax cut at all from such a change.

Relatively few states allow an income tax deduction for federal taxes paid, and only three states allow taxpayers to deduct the full amount of their federal income tax liability. When fully implemented, expanding this deduction would carry a substantial price tag—eliminating the cap entirely would cost more than $750 million annually, while increasing the cap would cost over $120 million annually—and would deliver little tax relief to most elderly Oregonians. The vast majority of elderly Oregonians would be completely unaffected by an increase in the federal tax deduction because their federal tax burden is less than $3,000.
ITEP METHODOLOGY

The Institute on Taxation & Economic Policy has engaged in research on tax issues since 1980, with a focus on the distributional consequences of both current law and proposed changes. ITEP’s research has often been used by other private groups in their work, and ITEP is frequently consulted by government estimators in performing their official analyses. Over the past several years, ITEP has built a microsimulation model of the tax systems of the U.S. government and of all 50 states and the District of Columbia.

What the ITEP Model Does

The ITEP model is a tool for calculating revenue yield and incidence, by income group, of federal, state and local taxes. It calculates revenue yield for current tax law and proposed amendments to current law. Separate incidence analyses can be done for categories of taxpayers specified by marital status, the presence of children and age.

In computing its estimates, the ITEP model relies on one of the largest databases of tax returns and supplementary data in existence, encompassing close to three quarters of a million records. To forecast revenues and incidence, the model relies on government or other widely respected economic projections.

The ITEP model’s federal tax calculations are very similar to those produced by the congressional Joint Committee on Taxation, the U.S. Treasury Department and the Congressional Budget Office (although each of these four models differs in varying degrees as to how the results are presented). The ITEP model, however, adds state-by-state estimating capabilities not found in those government models.

Below is an outline of each area of the ITEP model and what its capabilities are:

The Personal Income Tax Model analyzes the revenue and incidence of current federal and state personal income taxes and amendment options including changes in:

- rates— including special rates on capital gains,
- inclusion or exclusion of various types of income,
- inclusion or exclusion of all federal and state adjustments,
- exemption amounts and a broad variety of exemption types and, if relevant, phase-out methods,
- standard deduction amounts and a broad variety of standard deduction types and phase-outs,
- itemized deductions and deduction phase-outs, and
- credits, such as earned-income and child-care credits.

The Consumption Tax Model analyzes the revenue yield and incidence of current sales and excise taxes. It also has the capacity to analyze the revenue and incidence implications of a broad range of base and rate changes in general sales taxes, special sales taxes, gasoline excise taxes and tobacco excise taxes. There are more than 250 base items available to amend in the model, reflecting, for example, sales tax base differences among states and most possible changes that might occur.

The Property Tax Model analyzes revenue yield and incidence of current state and local property taxes. It can also analyze the revenue and incidence impacts of statewide policy changes in property tax— including the effect of circuit breakers, homestead exemptions, and rate and assessment caps.
The Corporate Income Tax Model analyzes revenue yield and incidence of current corporate income tax law, possible rate changes and certain base changes.

Local taxes: The model can analyze the statewide revenue and incidence of aggregate local taxes (not, however, broken down by individual localities).

Addendum: Data Sources

The ITEP model is a “microsimulation model.” That is, it works on a very large stratified sample of tax returns and other data, aged to the year being analyzed. This is the same kind of tax model used by the U.S. Treasury Department, the congressional Joint Committee on Taxation and the Congressional Budget Office. The ITEP model uses the following micro-data sets and aggregate data:

Micro-Data Sets:

Partial List of Aggregated Data Sources:
Miscellaneous IRS data; Congressional Budget Office and Joint Committee on Taxation forecasts; other economic data (Commerce Department, WEFA, etc.); state tax department data; data on overall levels of consumption for specific goods (Commerce Department, Census of Services, etc.); state specific consumption and consumption tax data (Census data, Government Finances, etc.); state specific property tax data (Govt. Finances, etc.); American Housing Survey 1990; 1990 Census of Population Housing; etc.

A more detailed description of the ITEP Microsimulation Tax Model can be found on the ITEP internet site at www.ctj.org\itep\.