Senate Bills 1523, 1527, 1528 and 1529 Tax Issues

Testimony for Senate Finance and Revenue – Jody Wiser – 2.6.2018

The Pass-through Business Tax Breaks

There are now three different bills discussing tax breaks for business owners. What action should the legislature take?

SB 1527 or SB 1528 -1 or another bill should be used to end, or <u>deeply</u> restrict, the current Oregon tax break for the pass-through income of certain business owners.

No current proposal goes far enough in restricting its use and each has a flaw.

1) **The same benefit accrues to average Joe business owners as to those with millions** of pass-through income. The benefit should be only for those less than **$250k/$125k of pass through income.**

2) **There is a marriage penalty** in each current bill. A single filer can apply the reduced rate on up to $250,000 of income, just the same as joint filers. This gives single filers a potential benefit of ~ $6100 while joint filers' maximum benefit would be ~ $5000. This occurs because joint filers reach the 9.9% tax rate at $250,000 of taxable income while single filers reach it at $125,000. **Correct this by allowing the reduced rate for $250,000 of business income for joint filers and $125,000 for all others**.

Disconnect from the big tax break for pass-through income that Congress passed in December with SB 1529. Legislators should be clear in the final language in SB 1529 that Oregon will not give business owners – on their Oregon taxes – tax breaks for either passive or non-passive income business income.

This $600 million can and should be put to better uses. Tax Fairness Oregon would support it being used to pay down the PERS unfunded liability or to staff up our human services, fish and wildlife, DEQ, DOR and other state departments. Funding these are the Legislature's responsibilities, income tax breaks for business owners are not.

SB 1528-3: The SALT Provision

This provision needs to be amended to deliver better equity. As designed, the General Fund will be picking up far too much of the cost. The bill as written would deliver a tiny amount to the Department of Revenue for auctioning tax credits, but nothing to them for writing rules, instructions and forms, informing the public and CPAs of the provision, or increased auditing and computer programming. The bill provides nothing to the Higher Education Coordinating Commission for receiving and acknowledging donations to the new Opportunity Grant Fund or for identifying, hiring and managing a marketer. And it provides nothing to the AG's office for the inevitable defense of the law from Oregon taxpayers, marketers and the federal government. At least 1% of each donation should be collected to cover these costs, i.e. each donor would be issued tax credits for 99% of their donation as our handling fee. Any taxpayer in the top federal tax brackets of 32% to 37% would still be benefitted, just not 100%.

SECTIONS 2 – 11 of the bill is for taxpayers with state and local property and income taxes (SALT) of more than $10,000 a year. It creates a work-around for the SALT provision in the new federal law. They can donate amounts equal to their excess of $10,000, to a new Opportunity Grant Fund and get a marketable tax credit in exchange. If they wish, the state will sell the tax credit for them at auction. That is well and good, but the cost for this is laid upon the state's General Fund, not those benefitting.

As drafted, donations to the Opportunity Grant Fund need to be made during the calendar year. Similar programs like Oregon's 529 plan allow contributions up to April 15th when taxpayers are more likely to know their tax liability for the year is. December 31st is a tough deadline. Is it necessary because these will be charitable contributions?

SB 1528 -3 The Personal Income Tax Rate Reduction

SECTIONS 16 – 18 provide a tax break for all Oregonians by reducing Oregon's bottom two rates, but gives the greatest benefit to those with the highest income. It reduces the current 5, 7, 9 and 9.9% rates to 4, 6, 9 and 9.9%.

A college student with $2000 of taxable income would get a $20 tax break
A student with $4000 of taxable income would get a $40 tax break
At PCC teacher with $20,000 of taxable income would get a $50 tax break
While the research professor with $125,000 or more would get a $130 tax break

But inequity is not the worst of it.

With nearly two million returns, if the average tax break is $40, the cost to the General Fund would be $80 million a year, $160 million a biennium.

This is not the way to buy votes! And since it's difficult to imagine Republicans who don't want a SALT solution, why do we need a provision costing ~ $160 million to get votes? This is as nonsensical as needing in 2013 to give the Pass-through and IC-DISK tax breaks to get Republicans to agree to PERS reforms.

Would changing the tax rates require a supermajority vote?

SB 1523 and SB 1527(Sections 1-9) The Broadcasters Pilot Extension

This "pilot" program was started in 2014. An extension was considered in 2017 and did not move forward, apparently because broadcasters were challenging provisions in the pilot which lacked clarity.

Among the issues needing to be address were:

Lack of clarity regarding which companies are interstate broadcasters;
Which activities create nexus;
Which portions of a company's income are subject to apportionment.

Since the language in the original bill was likely influenced by the businesses when it was written, were the issues to be resolved in court designed into the original bill? We can imagine that among issues to be resolved, is the question "Is Hulu a broadcaster?" An additional question is, since the LLC's headquarters are in California, do they have Oregon nexus if they are a broadcaster. As they are jointly owned by an array of businesses (Disney, 21st Century Fox, Comcast, and Time Warner), it would be difficult for LRO and DOR to sort out their tax situation under the two tax approaches.

An additional questions is: did the state receive more or less revenue from the broadcasters after or before the court cases and were the changes in this bill proposed by DOR or the lobby?

Are the ambiguities resolved in today's language to the advantage or disadvantage of the state General Fund and clear enough that we'll avoid the cost of court cases in the future?

This bill asks to extend the pilot another four years. **But where is the research on the effect of the pilot? Before a decision to proceed, shouldn't you see some research?**

Recommendation: a bill that asks LRO and the DOR to identify 10 businesses across the range of effected broadcasters and distributors and require public disclosure of these broadcasters 2016 taxes under the pilot and their 2017 taxes under our base system which taxes based on audience, then you would perhaps have the basis for a decision. The ten might be CNN, NBC, Comcast, Charter, Direct TV, Verizon, Hulu, Netflix, Amazon and a satellite operator.

Alternatively, you could ask that all companies prepare and submit their 2017 taxes under both methods and give you the opportunity to see how it effects each business. They are starting to prepare their 2017 taxes now under our pre-pilot tax system, so this information could be available by the next session for most businesses.

If the businesses involved aren't willing to have disclosure, then surely the pilot is not working to the benefit of the public good.

Nowhere Income and Why Throwback Rules Are Necessary

The existence of states without throwback rules creates a clear tax avoidance opportunity for multi-state corporations. These companies can reduce their state taxes by locating their property and payroll in states that don't have a throwback rule and then making sales to customers in states in which the company does not have nexus. Companies aggressively pursuing this "nowhere income" tax avoidance strategy can reduce their state tax bill far below what they ought to pay — and far below the taxes paid by competing companies.

Nowhere income arises when a company is not subject to a corporate income tax in one of the states into which it makes sales, either because that state does not levy such a tax or because the company doesn't have a sufficient level of activity in the state to be subject to the tax, a concept known as "nexus". Having property or payroll in a state is always sufficient to constitute nexus, but making sales into a state is not. A little known federal statute, Public Law 86-272, stipulates that making sales into a state is not sufficient to generate nexus if:

(1) the company's activities in the state are limited to soliciting sales of tangible personal property;

(2) the orders for the company's sales are taken outside of the state, and;

(3) all such sales are delivered from outside of the state.

Given these restrictions, companies may be able to avoid establishing nexus in some of the states into which they make sales and thus generate nowhere income that is untaxed in any state.

Oregon must retain its throwback rules.

We read the bills and follow the money