OREGON DEPARTMENT OF REVENUE

Legislative Testimony

Senate Finance & Revenue Committee **February 6, 2017**

SB 30 – Allowing Department of Revenue to Consider U.S. Corporations' Relationships with Related Foreign Corporation When Determining If U.S. Affiliates Conduct Single Trade or Business

Summary

SB 30 proposes an amendment to ORS 317.705 that allows the Department of Revenue to consider U.S. corporations' relationships to a foreign corporation owned or controlled by the same interests for the purpose of determining whether the U.S. corporations included in an Oregon return are engaged in a single or "unitary" trade or business with each other.

Current Law

U.S. corporations filing a federal consolidated tax return that conduct part of their unitary business in Oregon generally must file an Oregon consolidated tax return. Under current law, the department may not consider facts about the U.S. consolidated group's connections with a related foreign corporation when determining if the U.S. group is engaged in a unitary business, unless there is tax evasion or the foreign corporation itself does business in the U.S.

Background

Under the unitary business principle, only corporations that comprise a unitary business may be treated as a single economic enterprise. Consistent with U.S. Supreme Court cases, a unitary business is defined in ORS 317.705 as a business enterprise in which there exists directly or indirectly between the members or parts of the enterprise a sharing or exchange of value as demonstrated by: centralized management or a common executive force; centralized administrative services or functions resulting in economies of scale; or a flow of goods, capital resources or services demonstrating functional integration.

Before 1986, Oregon taxed a corporation doing business in Oregon based on its share of the combined worldwide income of all domestic and foreign corporations engaged in the same unitary business. Effective in 1986, Oregon moved from a "worldwide" to a "water's-edge" approach by tying the Oregon unitary group's return to the federal consolidated return, which generally excludes foreign corporations. Federal consolidated income of those U.S. corporations not part of the unitary business must be "backed out" of the Oregon return.

To determine when to "back out" U.S. consolidated group members' non-unitary income, ORS 317.705(3)(c) currently directs the department to ignore related foreign corporations' connections with the U.S. companies, except in special circumstances.

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SB 30 addresses two problems created by ignoring U.S. corporations' ties to related foreign corporations owned or controlled by the same interests. First, in 2013, Oregon adopted a limited exception to "water's-edge" reporting by requiring the unitary income of a corporation formed in a foreign listed jurisdiction to be added to the income of the U.S. unitary group. The amendment to ORS 317.705 makes clear that the U.S. corporation's connections to the listed jurisdiction corporation may be considered in determining whether they are unitary.

Second, SB 30 addresses problems created by corporate inversions and foreign companies' acquisition of U.S. businesses. Ignoring facts about U.S. corporations' relationships to a foreign corporation controlled by the same interests results in uneven tax treatment of domestically-controlled U.S. businesses compared to foreign-controlled U.S. businesses. In corporate "inversions," for example, there may continue to be the same flow of value among the parts of the U.S. business after U.S. headquarters moves abroad, except that the flow of value between the U.S. corporations may occur in part through the foreign parent instead of a domestic headquarters. Ignoring the role of the foreign corporation in the U.S. corporations' activities may result in finding that the U.S. corporations filing a federal consolidated return are no longer unitary with each other. This amendment to SB 30 does not deviate from water's-edge reporting, but allows the department to consider economic relationships between a consolidated group of U.S. corporations and a foreign corporation owned or controlled by the same interests in determining whether the U.S. group members are unitary with each other.

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