

**Oregon Legislative Assembly – 2017 Session
Senate Committee on Finance and Revenue
Testimony of Richard B. Solomon, CPA, Regarding SB 165
(relating to Pass-Through Entity Reduced Income Tax Rate)**

DATE: February 16, 2017

Chair Hass, Vice-Chair Boquist and Members of the Committee, thank you for the opportunity to address you today. For the record, my name is Richard B. Solomon. I am a Certified Public Accountant who has practiced in Portland for over 40 years. My work is limited to tax planning and preparation of tax returns, primarily for high net worth individuals and professionals like doctors and lawyers. I am here at the request of Chairman Hass and represent only myself.

By way of background, you may recall that on September 21, 2016, I testified before the committee regarding the PTE Reduced Tax Rate. At that time, I testified that I opposed the reduced tax rate for pass-through entities because I felt:

- a) it was a waste of the State's resources, and
- b) it was unfair because it favored some business entities, such as S-Corporations, partnerships and multi-member LLCs over other forms including sole proprietorships, single member LLCs and C-Corporations.

I continue to oppose the concept of reduced tax rates for owners of pass-through entities but I am here today to support Senate Bill 165.

Positives of SB165

The original intent of HB 3601, which created the reduced PTE tax rate, was to encourage job growth. But the costly program does not currently require employers who benefit from the reduced rate to actually increase employment. SB 165 corrects that by requiring businesses benefiting from the reduced income tax rate to increase their number of full-time equivalent employees as well as increase the employees' average hourly wage. Consequently, as a result of SB 165, the tax benefit would at least be *somewhat* aligned with the objective of increased employment.

But, even with the reforms of SB 165, it seems that the PTE preferential tax rate is a roundabout and inefficient means to promote employment. A better way to spend tax dollars might be to provide employers a credit against any increase in state unemployment tax. Such a credit would be a direct offset to employers' additional costs; and a credit would not discriminate based on the employer's form of business entity, which currently advantages S-Corps and multi-member LLCs over C-Corps and sole proprietorships.

Downsides of SB165

But there are downsides to SB165. The proposed change is cumbersome and may add significant complexity to the preparation of tax returns. For many employers, it is no easy task to determine if there is a net increase in FTEs and average hourly wage.

Additionally, the state provided tax benefit to employers may greatly exceed the employer's added payroll cost. Let's take an example: A professional partnership of 50 lawyers would be able to get an

Oregon tax break if they increased their staff's pay by only 1% and added only one new clerk. The reduction in the company's income tax might dwarf their additional payroll cost.

There bill also does not address how the provision would be interpreted. For example, suppose a ten partner medical practice divided into two five partner firms. Would they be treated as two new firms with zero prior year payrolls, so both firms would be eligible for the Oregon tax break even though there is no net increase in staff?

SB 164

Before finishing, I also want you to know that I strongly support SB 164 which would extend the PTE benefit to taxpayers filing an amended return. That bill, which is not being considered today, is a needed reform because it eliminates a trap for many taxpayers who prepare their own returns or who don't have knowledgeable accountants.

Summary

In summary, while I continue to oppose HB 3601, which established the preferential rate for income from pass-through entities, I do support SB 165.

Thank you for the opportunity to address you today. I am happy to answer your questions.