SMART GROWTH COALITION

February 26, 2018

Chair Phil Barnhart
House Revenue Committee
900 Court Street NE
Salem, OR 97301

Dear Chair Barnhart and Members of the Committee,

Thank you for the opportunity to submit written comments on the behalf of the Smart Growth Coalition regarding the contents of SB 1529 and the proposed -A9 amendment.

About the Smart Growth Coalition

The Smart Growth Coalition is a consortium of tax professionals representing multistate and multinational taxpayers located in Oregon. Our coalition was formed in 1999 to add technical expertise to state legislative proceedings regarding proposed reforms to state tax law affecting businesses. Our members are unified in their commitment to help promote sound tax policies that encourage local investment and provide technical simplicity and clarity to the state tax code.

SB 1529-A is an appropriate response to the new federal tax law

The recently enacted overhaul of the federal tax code substantially changes the domestic and international rules used to calculate corporate income taxes. These rules broaden the tax base to offset the costs of lowering the federal corporate income tax rate. Since states rely on the federal definitions of income but not the rates, most states will pick up substantial additional revenue or receive a "windfall." Oregon will particularly benefit from this expanded tax base because of its rolling connection to federal taxable income. In fact, the preliminary estimate released by the Legislative Revenue Office (LRO) suggests the expansion of the corporate tax base attributed to the domestic rules will result in an additional $1.5 billion in taxes over a ten-year period.

The new international tax rules, while complex in their nature, will bring the U.S. out of the dark-ages of worldwide taxation and closer to a territorial tax regime. These rules, especially the carrot and stick approach to incentivizing local investments (new IRC § 250 and IRC § 951A), expand the reach of the

tax base to include tax planning strategies and transactions that minimize liabilities through so-called "tax havens." The transition tax, often referred to as the tax on deemed repatriation, will address previous deferrals (going back to 1986) and start the U.S. on a clean slate moving forward.

SB 1529-A addresses conformity issues in two areas that would otherwise become problematic without legislative action.

Oregon is already decoupled from the federal dividends received deduction and substitutes the federal deduction with a state equivalent after requiring the addback of the federal deduction. The state law never anticipated the transition tax and the absence of an addback requirement of the federal deduction may result in a taxpayer picking up both the federal and state deductions. This is counterintuitive to the premise of the transition tax and it makes sense for the state to require an addback and treat the income similarly to other dividend deductions as part of the broader conformity response.

SB 1529-A also addresses the interaction of the new international rules and existing state law. The transition tax is designed to capture previously untaxed income held abroad, including income held in countries Oregon has listed as a so-called "tax haven" under ORS § 317.716 and ORS § 317.717. It is necessary to address this interplay as part of the conformity response to avoid unconstitutional double taxation. Moving forward, this income will be included in the new international rules designed to prevent (and penalize as necessary) tax planning structures in no- or low-tax rate jurisdictions. The legislation addresses these constitutional issues by providing a credit against the transition tax for taxes already paid to the state and repeals the state tax law in future tax years. Repealing the tax havens law is an essential conformity step and averts legal challenges that could endanger previous and future taxes collected under the policy.

Our members believe this legislation is the appropriate response to conforming with the new federal tax law and provides clarity for both taxpayers and tax administrators.

Proposed changes to SB 1529 add unnecessary legal and compliance complexities

The proposed (A9) amendment maintains the changes to the state's dividends received deduction but fails to repeal the tax havens law. Maintaining that law is a risky gamble for the state. In March 2017, LRO reported the large number of active audits pertaining to the policy suggest the state is at risk of taxpayers challenging the constitutional grounds of the law, which would put

the revenues generated by the policy in jeopardy.[1] Continuing the policy while conforming to the new international rules only increases the likelihood of a legal challenge. This is because the state would impose its tax on the same income twice by including the income as federal taxable income and then again through the tax haven policy.

The constitutional concerns regarding the tax haven policy are abundant. The U.S. Constitution prohibits the states from regulating foreign commerce and reserves international taxing authority to the federal government. Therefore, discriminatory actions of a state against a foreign jurisdiction or taxpayer operating in a foreign jurisdiction are very likely to be held unconstitutional. This would put any and all state revenues generated by the policy at risk.

LRO has also suggested the tax havens law serves as a "blunt policy tool" predisposed to collecting income not attributable to the U.S. and sends an unwelcoming message for international investment and trade.[2] Repealing this controversial state tax law and relying on the new international rules is the only appropriate conformity response. The new international rules bypass the constitutional concerns and ease the administrative responsibilities for the Oregon Department of Revenue. Repealing the law also prevents costly litigation, for both the state and its taxpayers, and simplifies compliance for multinational taxpayers, all while raising additional funds to support vital state services.

We respectfully ask the committee to pass SB 1529-A as it was passed by the Senate. Thank you again for the opportunity to submit these comments for the public record.

Sincerely,

Jeff Newgard
Executive Director
Smart Growth Coalition

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[1] Legislative Revenue Office. "An Assessment of Oregon's Listed Jurisdiction Policy and Its Cost Effectiveness." March 2017. Report #4-17.

[2] Ibid