

The Idea That Would Not Die: Beyond Oregon's Measure 97

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In this edition of Skookum Tax News, DeLappe and Brant report on the latest proposals for gross receipts taxes in Oregon.

Oregon Sen. Mark Hass (D), chair of the Senate Finance and Revenue Committee, is best characterized as a focused and persistent legislator. Together with Rep. Mark Johnson (R), a member of the Oregon House Revenue Committee, Hass proposed a broad-based gross receipts tax styled after Ohio's commercial activities tax. The two legislators have presented a gross receipts tax as the key to addressing the volatility of Oregon's current tax system. They hoped it would serve as a compromise to Measure 97, a competing proposal that they recognized as being seriously flawed. When they presented it during the 2016 short session, they of course understood they would likely not achieve such radical tax reform

that year. Rather, their goal was to start the conversation and to present an alternative to the drastic gross receipts tax that a coalition of public spending advocates, Our Oregon, put on the ballot as Measure 97.

Oregon voters would appear to have spoken on November 8, 2016, in defeating by a clear margin Measure 97's ill-designed amendments to the Oregon corporate minimum tax regime.¹ Flaws in Measure 97, some of which have been discussed in an earlier edition of this column,² included the following:

- The measure contained a corporate alternative tax based on Oregon gross receipts, which has no relationship to profits.
- For a gross receipts tax, its rate of 2.5 percent was extremely high.
- The corporate alternative tax was to apply to C corporations only. S corporations, entities taxed as partnerships, and Oregon benefit companies would have escaped the proposed tax altogether.
- Though Oregon benefit companies would have escaped the proposed tax, benefit companies formed in other states would have been subject to the tax. As a result, Measure 97 clearly conflicted with the interstate commerce clause.

Even though most people would take the defeat at the polls as the death knell for a gross receipts tax in Oregon, these legislators did not take that tack. Hass vowed even before the November 2016 election that he would not take the defeat of Measure 97 as the end of the

¹ Or. Rev. Stat. section 317.090.

² Michelle DeLappe, "Time to Decide on an Oregon Gross Receipts Tax," *State Tax Notes*, May 30, 2016, p. 699.

discussion about adopting a gross receipts tax. In the same vein as his statements for the last several years about tax policy in Oregon,³ his website opens with the goal of reforming Oregon's tax system:

This Legislative Session, I am focusing my efforts on reforming Oregon's tax system to make it more fair, practical and effective. As chair of the Senate Revenue Committee, I'm extremely familiar with volatility in the Oregon tax code. We need to stabilize our revenue and simplify the complexities. We need a system that funds education and other services in good times and bad times. Tax reform is one of the most difficult policy issues in the legislature. But in the wake of last year's divisive debate over Ballot Measure 97, I think my colleagues and Oregonians are ready to make some changes — as long as they are reasonable and bipartisan.⁴

Sure enough, Hass and Johnson are now working hard to revive the concept of a gross receipts tax in Oregon.

Enter L.C. 3548, S.J.R. 41, and H.B. 2230

On February 13 Hass released Legislative Concept 3548 (L.C. 3548) to Oregon lawmakers. L.C. 3548 proposed a legislative referendum to amend the state constitution to create a business privilege tax based on gross receipts.⁵ Shortly after its release, he introduced it as Senate Joint Resolution 41 (S.J.R. 41). In the House, Johnson introduced a much more detailed proposal: H.B. 2230, which would create a commercial activity tax based on gross receipts, the effective date of which would be tied to the voters' passage of House Joint Resolution 4 (H.J.R. 4), a constitutional amendment removing a reporting requirement for the state's system of education.⁶ Both these new tax proposals resemble Measure 97, but there are several key

differences. For a comparison of the main similarities and differences, see Table 1. In broad strokes, the new proposals broaden the tax base and lower the tax rate proposed in Measure 97.

Where the Rubber Hits the Road

Another way to compare these proposals is to view a few examples of how the tax would affect two hypothetical taxpayers compared with current law, as shown in Table 2. (Because the details on S.J.R. 41 are simply too fuzzy to allow us to calculate the tax, it is excluded from this comparison.) For purposes of this example, both taxpayers have Oregon gross sales of \$150 million for the year and a net operating loss of \$25,000 after allowable deductions.

The different treatment of C corporations and S corporations under the current regime is odd. Measure 97 would have greatly exacerbated that discrepancy, while H.B. 2230 would eliminate it. On the other hand, like Measure 97, H.B. 2230 would require a business that is operating at a loss to pay a significant amount in tax. This is one of the problems inherent in the gross receipts tax.

Back Door to a Sales Tax in Oregon?

H.B. 2230 prohibits passing the gross receipts tax through to the purchaser, but it would allow the seller to increase the price charged to allow the seller to recover the amount of tax.⁷ Basically, as long as the seller hides the tax on the sale, the seller would be in compliance with the proposed law.

³ See, e.g., Mark Hass, "Hass Named to Lead Senate Finance and Revenue Committee, Spearhead Tax Reform," Dec. 12, 2014.

⁴ Sen. Mark Hass, Oregon State Legislature.

⁵ Draft language made available by the Council On State Taxation.

⁶ H.B. 2230 and H.J.R. 4.

⁷ H.B. 2230, section 7.

Table 1.			
	Measure 97	S.J.R. 41	H.B. 2230
Name of Tax	Minimum Tax	Business Privilege Tax	Commercial Activity Tax
Tax Incidence	Gross receipts derived from Oregon sales above \$25 million during the year	Gross receipts derived from Oregon sales	Gross receipts derived from Oregon sales, rents, and royalties of property, goods, and services ^a
Affected Taxpayers	Limited to C corporations reporting over \$25 million during the year	All types of business entities	Appears to apply to all persons doing business in Oregon, though the bill's definition of doing business applies only to corporations and national banking associations ^b
Excluded Taxpayers	Not applicable to S corporations, Oregon benefit corporations, other types of business entities, or C corporations with \$25 million or less in Oregon sales in the year	Not applicable to businesses with Oregon gross receipts less than \$150,000 (subject to adjustment for inflation)	Not applicable to list of excluded persons, e.g., certain nonprofit organizations and certain insurance companies; ^c also not applicable to businesses with gross receipts of \$1 million or less ^d (NB: certain groups of taxpayers are treated as a single taxpayer) ^e
Tax Rate	2.5 percent	To be determined, but not to exceed 0.7 percent	0.7 percent ^f
Flat Tax Component	\$30,001 on Oregon sales under \$25 million in addition to percentage tax	\$250 on businesses with less than \$5 million (subject to adjustment for inflation) in Oregon gross receipts instead of percentage tax	n/a
Other Corporate Taxes	Instead of corporate minimum tax	Unclear	Expressly in addition to other corporate taxes ^g <i>but</i> repeals corporate excise and income taxes

^aH.B. 2230 sections 7, 9.

^bH.B. 2230 section 1(3), 1(6), 7.

^cH.B. 2230 section 1(4).

^dH.B. 2230 section 8(2).

^eH.B. 2230 section 4.

^fH.B. 2230 section 8(1).

^gH.B. 2230 section 7(1) ("The tax imposed under this section is in addition to any other taxes or fees imposed under the tax laws of the state").

All three of these tax proposals are vulnerable to the criticism that they are essentially a hidden sales tax. As the Institute on Taxation and Economic Policy has observed, “The main difference between a traditional sales tax and a GRT [gross receipts tax] is that the former generally applies only to retail sales, while the latter applies to the sales made by companies at every stage of the production process. In other words, a GRT is a sales tax that applies to more types of transactions.”⁸ This criticism has particular weight in Oregon where voters have repeatedly and overwhelmingly defeated ballot measures that would have imposed a sales tax.⁹ Opponents to Measure 97 wielded this criticism successfully, calling for voters to “defeat the tax on Oregon sales.”

Oregon voters will not likely adopt a sales tax, given the significant (that is, 9.9 percent) state personal income tax. A reduced personal income tax (for example, 5 to 7 percent) and a statewide retail sales tax (for example, 3 to 4 percent) might prove a more attractive option, but only if clear curbs were to be put in place to prevent increases in either tax rate in future years. The absence of any curb is likely the reason Oregon voters have consistently opposed each and every attempt of lawmakers to adopt a sales tax. Although Oregon’s governor and many legislators recognize the need for reforming Oregon’s tax system, hardly anyone¹⁰ appears interested in incurring voter wrath by even so much as mouthing the words “sales tax.”¹¹

Whether voters rejected Measure 97 as a disguised sales tax or because they recognized its many other flaws remains unclear. What does seem clear, however, is that Hass and Johnson are betting on the latter. They are still proposing a disguised sales tax, just like all gross receipts taxes.

Put the Issue to the Voters . . . or Not

S.J.R. 41 contemplates a constitutional amendment to be submitted to voters for approval or rejection at a special election on May 16. As we saw with Measure 97, where dueling campaigns in favor and against the measure together spent more than \$42 million, a costly fight would likely erupt if either of these proposals were actually to go to a referendum.

S.J.R. 41, as drafted, is simply a way for the Senate to continue its discussion about a gross receipts tax. Paul Warner, Oregon’s Legislative Revenue Officer, confirmed that the work group dedicated to this issue has not yet prepared a report on the fiscal effect of the proposal or of H.B. 2230 and, given the pace of events during the legislative session, would not likely be able to prepare anything before April. As of the date of writing, no report is available yet. So it appears legislators are merely in a brainstorming stage, not close to making a concrete proposal to Oregon voters.

The reason S.J.R. 41 was styled as a constitutional amendment without an accompanying Senate bill is simply due to a procedural requirement in Oregon’s constitution: Bills for raising revenue must originate in the House of Representatives, not the Senate.¹² For the Senate to safely discuss the legislative proposal without risk that it will evolve into a bill that could later be claimed to be unconstitutional for having originated in the Senate, senators prepared it as a proposed constitutional amendment.

⁸Institute on Taxation and Economic Policy, “Broad-Based Gross Receipts Taxes: A Worthwhile Alternative?” (Mar. 1, 2007).

⁹See, e.g., Billy Hamilton, “Searching for Plan B in Oregon,” *State Tax Notes*, Jan. 9, 2017, p. 221. Hamilton discusses the nine times Oregon voters have rejected sales tax ballot measures.

¹⁰A few legislators have introduced a proposed amendment to adopt a sales tax. See H.J.R. 20 and S.J.R. 7.

¹¹This has long been true in Oregon. A 1972 law review article opens, “Practical people say it is political suicide to advocate a general sales tax in Oregon.” Milton L. Ray, “An Oregon Sales Tax Primer,” *Or. L. Rev.* 3 (Fall 1972).

¹²Or. Const., Art. IV, section 18. See, e.g., *City of Seattle v. Department of Revenue*, 357 Or. 718, 357 P.3d 979 (2015) (discussing this requirement).

	Minimum Tax Under ORS 317.090	Minimum Tax Under Measure 97	Tax Under H.B. 2230
C Corporation	\$100,000	\$3,155,001	\$1,050,000
S Corporation	\$150	\$150	\$1,050,000

If any legislative proposal for a gross receipts tax gets enacted, it will likely start as a bill in the House. The legislature can only adopt a bill raising revenue with the support of 60 percent of the members of each legislative chamber.¹³ If adopted, unless 4 percent of Oregon voters demand a referendum to approve or reject the tax, it could become effective without a direct vote by the people.¹⁴ But the power of the Oregon voter to invoke a referendum cannot be overlooked: As one former governor observed, “Of all the states, Oregon is the most limited in its public revenue potential, for every revenue measure at all levels is subject to referendum and possible veto by the people.”¹⁵

Weighting Strengths and Weaknesses of Gross Receipts Taxes — And Other Options

A recent Legislative Revenue Office presentation to the House and Senate revenue committees compared value added taxes, gross receipts taxes, and corporate income taxes in terms of a number of strengths and weaknesses (based on the work of three public finance economists, Robert Ebel, LeAnn Luna, and Matthew Murray). In its list of the gross receipts tax’s strengths, the presentation cited its broad base, its destination sourcing, the fact that Public Law 86-272 nexus standards do not apply, and recent examples of states moving toward this type of tax (the presentation noted Ohio, Nevada, and Texas). It recognized as weaknesses its pyramiding nature and partial shifting of the tax to consumers. Several other weaknesses should have been noted; for example, the inherent lack of transparency of gross receipts taxes is a concern because the tax on sales is hidden from consumers. Also absent is any acknowledgement of the lack of

fairness to low-margin businesses (such as the grocery industry) and businesses suffering losses that must still pay tax.

Conclusion

Though Hass and Johnson offer a bit more palatable path to reform than Our Oregon, the two latest legislative proposals pose serious concerns for the business community. Though the state’s needs are pressing, business leaders are also concerned about the level of public spending. Sen. Betsy Johnson (D) recently reported from her conversations with business leaders that they have asked legislators to “simultaneously look at the expenditure side of the ledger. Are you doing everything you can to spend money efficaciously and beneficially?”¹⁶ The business leaders emphasized that a conversation about the state’s pension liability must be part of any discussion on tax reform. Associated Oregon Industries lobbyist J.L. Wilson views the legislature as having no appetite for spending cuts or tax increases. So at this stage, Oregon’s legislators have many options on the table, but they have a long way still to go to bring those options closer to becoming law. One thing seems certain: The idea of a gross receipts tax in Oregon is far from dead. ■

¹³ Or. Const., Art. IV, section 25.

¹⁴ Or. Const., Art. IV, section 1.

¹⁵ Ray, *supra* note 11, at 37 n.79 (quoting Gov. Tom McCall).

¹⁶ Pete Danko, “State Sen. Betsy Johnson on Being a ‘Pro-Business Democrat’ and Calling the Russians Cheaters to Their Face,” *Portland Business Journal*, Feb. 8, 2017.