

House Bill 3296

Sponsored by Representative LINDSAY; Representative BREWER

SUMMARY

The following summary is not prepared by the sponsors of the measure and is not a part of the body thereof subject to consideration by the Legislative Assembly. It is an editor's brief statement of the essential features of the measure **as introduced**.

Establishes subtraction for purposes of income and excise taxation for amounts included in federal taxable income as result of recognition of capital gain due to sale or exchange of property by certain business entities. Allows for adjusted basis in property if certain conditions are met.

Applies to tax years beginning on or after January 1, 2012.

Takes effect on 91st day following adjournment sine die.

A BILL FOR AN ACT

1
2 Relating to capital gains subtraction for certain business entity transactions; creating new pro-
3 visions; amending ORS 314.712; and prescribing an effective date.

4 **Be It Enacted by the People of the State of Oregon:**

5 **SECTION 1. Section 2 of this 2011 Act is added to and made a part of ORS chapter 316.**

6 **SECTION 2. (1) As used in this section:**

7 (a) "Active conduct of a trade or business" has the meaning given that term in the
8 Treasury Regulations adopted under section 179 of the Internal Revenue Code.

9 (b) "Business entity" means any entity that is treated as a business entity under section
10 301 of the Internal Revenue Code and section 301.7701-2(a) of the Treasury Regulations
11 adopted under section 301 of the Internal Revenue Code, including an entity that is disre-
12 garded as a separate entity for federal income tax purposes.

13 (c) "Capital gain" means gain that is treated as gain from the sale or exchange of a
14 capital asset or as a long-term capital gain under the Internal Revenue Code.

15 (d) "Ownership interest" means, with respect to any business entity, any interest in the
16 capital or profits of the business entity, other than as a creditor.

17 (e) "Parent-subsidiary controlled group" means all of the business entities in one or more
18 chains of business entities connected through ownership interests with a common parent
19 business entity if more than 50 percent of the interests in the capital and profits of each of
20 the business entities is owned by one or more of the other business entities and the common
21 parent business entity owns more than 50 percent of the interests in the capital and profits
22 of at least one of the other business entities.

23 (f) "Property" means property as described in section 351(a) of the Internal Revenue
24 Code.

25 (2) A business entity is a qualified business entity under this section for a period if,
26 during that period:

27 (a) More than 50 percent of the average adjusted tax basis of the property held by the
28 business entity (or by any other business entity that, for all of such period, is a member of
29 any parent-subsidiary controlled group of which the business entity is the common parent)
30 is attributable to property used in the active conduct of a trade or business (other than the

NOTE: Matter in **boldfaced** type in an amended section is new; matter [*italic and bracketed*] is existing law to be omitted.
New sections are in **boldfaced** type.

1 rental of real property) by the entity (or by any business entity that, for all of such period,
2 is a member of any parent-subsidiary controlled group of which the business entity is a
3 member); and

4 (b) More than 50 percent of the wages paid by the business entity (and any other member
5 of any parent-subsidiary controlled group of which the business entity is a member if both
6 the entity and the other business entity are members of the group for all of such period) are
7 paid to employees who perform more than 50 percent of their services in Oregon during such
8 period or reside in Oregon for more than 50 percent of the time that they are employed
9 during such period by the entity (or other members of the group).

10 (3) An ownership interest in a business entity is a qualified business entity interest under
11 this section if:

12 (a) The ownership interest is issued on or after January 1, 2011;

13 (b) For each complete or partial tax year of the business entity during which the tax-
14 payer held the ownership interest, the business entity is a qualified business entity; and

15 (c) The interest is acquired by the taxpayer from the entity, directly or through an
16 underwriter.

17 (4)(a) There shall be subtracted from federal taxable income 50 percent of the amount
18 included in federal taxable income for the tax year as a result of the recognition of capital
19 gain from the sale or exchange of a qualified business entity interest that was held for more
20 than one year as of the date of the sale or exchange.

21 (b) Any subtraction from federal taxable income pursuant to this subsection shall be
22 treated as a reduction in capital gain (and as a capital loss, to the extent the subtraction
23 exceeds the taxpayer's net capital gains for the tax year) for purposes of any provisions in
24 this chapter relating to capital gains and losses.

25 (5) If subsection (4) of this section applies to the sale or exchange of a qualified business
26 entity interest in a qualified business entity, the following rules shall apply in determining
27 the amount of gain recognized from the sale or exchange, solely for purposes of determining
28 the amount subtracted from federal taxable income pursuant to subsection (4) of this sec-
29 tion:

30 (a) If the taxpayer acquired the interest in exchange for a contribution of property in a
31 transaction in which gain or loss was not recognized, in whole or in part (including a trans-
32 action described in subsection (6) of this section), the amount of gain recognized from the
33 sale or exchange shall be determined as if the basis of the ownership interest, immediately
34 after the acquisition, was equal to the greater of:

35 (A) The fair market value of the contributed property at the time of the contribution;
36 and

37 (B) The adjusted tax basis of the contributed property at the time of the contribution.

38 (b) If the taxpayer contributed property to the qualified business entity, in a transaction
39 in which gain or loss was not recognized, in whole or in part (including a transaction de-
40 scribed in subsection (6) of this section), after the date on which the taxpayer acquired the
41 ownership interest, the amount of gain recognized from the sale or exchange shall be deter-
42 mined as if the adjusted basis of the ownership interest was increased by reason of the
43 contribution, in lieu of the increase required under section 358 of the Internal Revenue Code,
44 or section 722 of the Internal Revenue Code, as the case may be, by the greater of:

45 (A) The fair market value of the contributed property at the time of the contribution;

1 and

2 (B) The adjusted tax basis of the contributed property at the time of the contribution.

3 (c) Paragraphs (a) and (b) of this subsection do not apply to the contribution of a quali-
4 fied business entity interest in a business entity to another business entity unless a basis
5 adjustment pursuant to subsection (6) of this section occurs as a result of the contribution.

6 (6)(a) If a taxpayer contributes a qualified business entity interest in a business entity
7 to another business entity in exchange for an ownership interest in the other business entity,
8 or contributes the qualified business entity interest to the capital of another business entity,
9 in a transaction in which gain or loss is not recognized, and the taxpayer attaches to the
10 taxpayer's tax return for the tax year in which the contribution occurs a statement con-
11 taining the information described in paragraph (b) of this subsection, the taxpayer's adjusted
12 basis in the ownership interest received in the exchange, after applying section 358 or 722
13 of the Internal Revenue Code, as the case may be, shall be increased, for purposes of deter-
14 mining Oregon taxable income, by the amount that would have been subtracted from the
15 taxpayer's federal taxable income pursuant to subsection (4) of this section if gain had been
16 recognized in the transaction in an amount equal to the gain the taxpayer would have re-
17 cognized if the taxpayer had sold the qualified business entity interest for an amount equal
18 to its fair market value.

19 (b) The statement described in paragraph (a) of this subsection shall contain the follow-
20 ing information:

21 (A) The fair market value of the qualified business entity as of the time of the contri-
22 bution and facts supporting the taxpayer's determination of the fair market value; and

23 (B) Facts supporting the taxpayer's determination that the ownership interest is a qual-
24 ified business entity interest.

25 (c) The basis of property held by a business entity may not be adjusted by reason of any
26 increase in the basis of any qualified business entity interest in the business entity pursuant
27 to subsection (4)(a) of this section.

28 (d) For purposes of this subsection, a partnership shall be treated as a taxpayer and can
29 cause a basis increase to occur if the partnership transfers a qualified business entity in-
30 terest in a nonrecognition transaction.

31 (7)(a) For purposes of subsection (3) of this section, an ownership interest held by a
32 taxpayer on December 31, 2010, shall be treated as issued to the taxpayer on or after January
33 1, 2011, if the taxpayer elects to treat the ownership interest as if it had been sold by the
34 taxpayer on January 1, 2011, in a taxable transaction for an amount equal to its fair market
35 value as of January 1, 2011, and repurchased by the taxpayer on January 1, 2011, for that
36 amount.

37 (b) An election pursuant to this subsection shall include a statement containing facts
38 supporting the taxpayer's determination of the fair market value of the ownership interest
39 as of January 1, 2011.

40 (c) If a taxpayer makes an election pursuant to this subsection with respect to an own-
41 ership interest:

42 (A) There shall be added to the taxpayer's federal taxable income for the tax year that
43 includes January 1, 2011, an amount equal to the income or gain that would have been re-
44 cognized if the taxpayer had sold the ownership interest on January 1, 2011, for an amount
45 equal to its fair market value; and

1 (B) The adjusted basis of the ownership as of January 1, 2011, for purposes of determining
 2 Oregon taxable income, shall be equal to its fair market value.

3 (d) The basis of property held by a business entity may not be adjusted by reason of the
 4 transactions deemed to occur by reason of an election pursuant to this subsection.

5 **SECTION 3.** Section 4 of this 2011 Act is added to and made a part of ORS chapter 317.

6 **SECTION 4.** (1) As used in this section:

7 (a) "Active conduct of a trade or business" has the meaning given that term in the
 8 Treasury Regulations adopted under section 179 of the Internal Revenue Code.

9 (b) "Business entity" means any entity that is treated as a business entity under section
 10 301 of the Internal Revenue Code and section 301.7701-2(a) of the Treasury Regulations
 11 adopted under section 301 of the Internal Revenue Code, including an entity that is disre-
 12 garded as a separate entity for federal income tax purposes.

13 (c) "Capital gain" means gain that is treated as gain from the sale or exchange of a
 14 capital asset or as a long-term capital gain under the Internal Revenue Code.

15 (d) "Ownership interest" means, with respect to any business entity, any interest in the
 16 capital or profits of the business entity, other than as a creditor.

17 (e) "Parent-subsidiary controlled group" means all of the business entities in one or more
 18 chains of business entities connected through ownership interests with a common parent
 19 business entity if more than 50 percent of the interests in the capital and profits of each of
 20 the business entities is owned by one or more of the other business entities and the common
 21 parent business entity owns more than 50 percent of the interests in the capital and profits
 22 of at least one of the other business entities.

23 (f) "Property" means property described in section 351(a) of the Internal Revenue Code.

24 (2) A business entity is a qualified business entity under this section for a period if,
 25 during that period:

26 (a) More than 50 percent of the average adjusted tax basis of the property held by the
 27 business entity (or by any other business entity that, for all of such period, is a member of
 28 any parent-subsidiary controlled group of which the business entity is the common parent)
 29 is attributable to property used in the active conduct of a trade or business (other than the
 30 rental of real property) by the entity (or by any business entity that, for all of such period,
 31 is a member of any parent-subsidiary controlled group of which the business entity is a
 32 member); and

33 (b) More than 50 percent of the wages paid by the business entity (and any other member
 34 of any parent-subsidiary controlled group of which the business entity is a member if both
 35 the entity and the other business entity are members of the group for all of such period) are
 36 paid to employees who perform more than 50 percent of their services in Oregon during such
 37 period or reside in Oregon for more than 50 percent of the time that they are employed
 38 during such period by the entity (or other members of the group).

39 (3) An ownership interest in a business entity is a qualified business entity interest under
 40 this section if:

41 (a) The ownership interest is issued on or after January 1, 2011;

42 (b) For each complete or partial tax year of the business entity during which the tax-
 43 payer held the ownership interest, the business entity is a qualified business entity; and

44 (c) The interest is acquired by the taxpayer from the entity, directly or through an
 45 underwriter.

1 (4)(a) There shall be subtracted from federal taxable income 50 percent of the amount
 2 included in federal taxable income for the tax year as a result of the recognition of capital
 3 gain from the sale or exchange of a qualified business entity interest that was held for more
 4 than one year as of the date of the sale or exchange.

5 (b) Any subtraction from federal taxable income pursuant to this subsection shall be
 6 treated as a reduction in capital gain (and as a capital loss, to the extent the subtraction
 7 exceeds the taxpayer's net capital gains for the tax year) for purposes of any provisions in
 8 this chapter relating to capital gains and losses.

9 (5) If subsection (4) of this section applies to the sale or exchange of a qualified business
 10 entity interest in a qualified business entity, the following rules shall apply in determining
 11 the amount of gain recognized from the sale or exchange, solely for purposes of determining
 12 the amount subtracted from federal taxable income pursuant to subsection (4) of this sec-
 13 tion:

14 (a) If the taxpayer acquired the interest in exchange for a contribution of property in a
 15 transaction in which gain or loss was not recognized, in whole or in part (including a trans-
 16 action described in subsection (6) of this section), the amount of gain recognized from the
 17 sale or exchange shall be determined as if the basis of the ownership interest, immediately
 18 after the acquisition, was equal to the greater of:

19 (A) The fair market value of the contributed property at the time of the contribution;
 20 and

21 (B) The adjusted tax basis of the contributed property at the time of the contribution.

22 (b) If the taxpayer contributed property to the qualified business entity, in a transaction
 23 in which gain or loss was not recognized, in whole or in part (including a transaction de-
 24 scribed in subsection (6) of this section), after the date on which the taxpayer acquired the
 25 ownership interest, the amount of gain recognized from the sale or exchange shall be deter-
 26 mined as if the adjusted basis of the ownership interest was increased by reason of the
 27 contribution, in lieu of the increase required under section 358 of the Internal Revenue Code,
 28 or section 722 of the Internal Revenue Code, as the case may be, by the greater of:

29 (A) The fair market value of the contributed property at the time of the contribution;
 30 and

31 (B) The adjusted tax basis of the contributed property at the time of the contribution.

32 (c) Paragraphs (a) and (b) of this subsection do not apply to the contribution of a quali-
 33 fied business entity interest in a business entity to another business entity unless a basis
 34 adjustment pursuant to subsection (6) of this section occurs as a result of the contribution.

35 (6)(a) If a taxpayer contributes a qualified business entity interest in a business entity
 36 to another business entity in exchange for an ownership interest in the other business entity,
 37 or contributes the qualified business entity interest to the capital of another business entity,
 38 in a transaction in which gain or loss is not recognized, and the taxpayer attaches to the
 39 taxpayer's tax return for the tax year in which the contribution occurs a statement con-
 40 taining the information described in paragraph (b) of this subsection, the taxpayer's adjusted
 41 basis in the ownership interest received in the exchange, after applying section 358 or 722
 42 of the Internal Revenue Code, as the case may be, shall be increased, for purposes of deter-
 43 mining Oregon taxable income, by the amount that would have been subtracted from the
 44 taxpayer's federal taxable income pursuant to subsection (4) of this section if gain had been
 45 recognized in the transaction in an amount equal to the gain the taxpayer would have re-

1 **cognized if the taxpayer had sold the qualified business entity interest for an amount equal**
2 **to its fair market value.**

3 **(b) The statement described in paragraph (a) of this subsection shall contain the follow-**
4 **ing information:**

5 **(A) The fair market value of the qualified business entity as of the time of the contri-**
6 **bution and facts supporting the taxpayer's determination of the fair market value; and**

7 **(B) Facts supporting the taxpayer's determination that the ownership interest is a qual-**
8 **ified business entity interest.**

9 **(c) The basis of property held by a business entity may not be adjusted by reason of any**
10 **increase in the basis of any qualified business entity interest in the business entity pursuant**
11 **to subsection (4)(a) of this section.**

12 **(d) For purposes of this subsection, a partnership shall be treated as a taxpayer and can**
13 **cause a basis increase to occur if the partnership transfers a qualified business entity in-**
14 **terest in a nonrecognition transaction.**

15 **(7)(a) For purposes of subsection (3) of this section, an ownership interest held by a**
16 **taxpayer on December 31, 2010, shall be treated as issued to the taxpayer on or after January**
17 **1, 2011, if the taxpayer elects to treat the ownership interest as if it had been sold by the**
18 **taxpayer on January 1, 2011, in a taxable transaction for an amount equal to its fair market**
19 **value as of January 1, 2011, and repurchased by the taxpayer on January 1, 2011, for that**
20 **amount.**

21 **(b) An election pursuant to this subsection shall include a statement containing facts**
22 **supporting the taxpayer's determination of the fair market value of the ownership interest**
23 **as of January 1, 2011.**

24 **(c) If a taxpayer makes an election pursuant to this subsection with respect to an own-**
25 **ership interest:**

26 **(A) There shall be added to the taxpayer's federal taxable income for the tax year that**
27 **includes January 1, 2011, an amount equal to the income or gain that would have been re-**
28 **cognized if the taxpayer had sold the ownership interest on January 1, 2011, for an amount**
29 **equal to its fair market value; and**

30 **(B) The adjusted basis of the ownership as of January 1, 2011, for purposes of determining**
31 **Oregon taxable income, shall be equal to its fair market value.**

32 **(d) The basis of property held by a business entity may not be adjusted by reason of the**
33 **transactions deemed to occur by reason of an election pursuant to this subsection.**

34 **SECTION 5. ORS 314.712 is amended to read:**

35 314.712. (1) Except as provided in ORS 314.722 or 314.723, a partnership as such is not subject
36 to the tax imposed by ORS chapter 316, 317 or 318. Partnership income shall be computed pursuant
37 to section 703 of the Internal Revenue Code, with the modifications, additions and subtractions
38 provided in this chapter and ORS chapter 316. Persons carrying on business as partners are liable
39 for the tax imposed by ORS chapter 316, 317 or 318 on their distributive shares of partnership in-
40 come only in their separate or individual capacities.

41 (2) If a partner engages in a transaction with a partnership other than in the partner's capacity
42 as a member of the partnership, the transaction shall be treated in the manner described in section
43 707 of the Internal Revenue Code.

44 (3) If a partnership is an electing large partnership under section 775 of the Internal Revenue
45 Code, the modifications of law applicable to an electing large partnership for federal tax purposes

1 are applicable to the electing large partnership for purposes of the tax imposed by this chapter or
2 ORS chapter 316, 317 or 318.

3 **(4) A partnership may make an election as provided in section 2 (6) or 4 (6) of this 2011**
4 **Act with respect to interests the partnership owns in other entities.**

5 **SECTION 6. Sections 2 and 4 of this 2011 Act and the amendments to ORS 314.712 by**
6 **section 5 of this 2011 Act apply to tax years beginning on or after January 1, 2012.**

7 **SECTION 7. This 2011 Act takes effect on the 91st day after the date on which the 2011**
8 **regular session of the Seventy-sixth Legislative Assembly adjourns sine die.**

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