

MEMORANDUM

TO: House Committee on Revenue and Rep. Ben Unger

FROM: Chuck Sheketoff, executive director

DATE: May 1, 2013

RE: HB 3477 – Closing the out-of-state bank loophole

I am following up on information requested and discussed at the public hearing.

I have checked with colleagues in other states and while they are more familiar with tax policy than state banking laws, none of them knew of another state that afforded a complete exemption from taxes along the lines as Oregon for banks doing business in the state. I was particularly interested in Pennsylvania and Ohio and my colleagues there said out-of-state banks do not enjoy the same loophole.

I also checked with the banking division at DCBS and while they do not have data on other states' statutes that might be similar to Oregon's, the banking division does not know of any other states that have a similar tax exemption for out-of-state banks.

I was also curious about Rep. Davis's comments about state law and questions about why this exemption would be necessary. The ORS Chapter 60 provisions that Rep. Davis was referring to have to do with registration to conduct business with the Secretary of State's corporation division. This bill does not have an impact on those requirements.

The exemption this bill addresses has to do with whether a business has substantial nexus and is conducting business in Oregon for the purposes of taxation. Beginning on the next page I have reprinted the state's Department of Revenue rules regarding nexus and doing business. HB 3477 would close the loophole that allows these banks to avoid these rules and Oregon's corporate income and excise tax.

OAR 150-317.010 — Substantial Nexus Guidelines

(1) The State of Oregon imposes taxes on or measured by net income to the extent allowed under state statutes, federal Public Law 86-272, and the Oregon and U.S. Constitutions. For purposes of determining whether Oregon has jurisdiction to impose an excise tax for the privilege of doing business in the state under ORS Chapter 317 or tax on income from sources within this state under ORS Chapter 318, there must exist a substantial nexus between the state and the activity or income it seeks to tax.

(2) “Substantial nexus” for corporate excise and income tax jurisdiction purposes, under the Commerce Clause of the U.S. Constitution, does not require a taxpayer to have a physical presence in Oregon. Substantial nexus exists where a taxpayer regularly takes advantage of Oregon’s economy to produce income for the taxpayer and may be established through the significant economic presence of a taxpayer in the state.

(3) In determining whether a taxpayer has a substantial nexus with Oregon the department may consider whether the taxpayer:

(a) Maintains continuous and systematic contacts with Oregon’s economy or market;

(b) Conducts deliberate marketing to or solicitation of Oregon customers;

(c) Files or is required to file reports or returns with Oregon regulatory bodies;

(d) Receives significant gross receipts attributable to customers in Oregon;

(e) Receives significant gross receipts attributable to the use of taxpayer’s intangible property in Oregon; or

(f) Receives benefits provided by the state, such as:

(A) Laws providing protection of business interests or regulating consumer credit;

(B) Access to courts and judicial process to enforce business rights, including debt collection and intellectual property rights;

(C) Highway or transportation system access for transport of taxpayer's goods or services;

(D) Access to educated workforce in Oregon; or

(E) Police and fire protection for property in Oregon that displays taxpayer's intellectual or intangible property.

(4) The list of possible facts in section (3) that the department may consider in determining whether a taxpayer has a substantial nexus with Oregon is meant to be nonexclusive, and those facts should be considered only to the extent they are relevant. The department may consider any other relevant facts and circumstances.

(5) The provisions in sections (1) through (4) of this rule, as well as the provisions in OAR 150-314.620-(A), 150-314.620-(B), and 150-314.620-(C), must be applied in determining if a taxpayer has substantial nexus in a state other than Oregon.

Example 1: Credit Card Company (CC) has, for several years, provided credit card lending services over the internet and by mail to over 25,000 Oregon customers. Solicitations for such credit cards have been mailed three or four times a year for the last three years to prospective Oregon customers in six Oregon cities. CC has substantial nexus in Oregon.

Example 2: IS Company (IS), headquartered in San Francisco, operates a website supporting internet sales, primarily to Asian country customers. IS made approximately 50 sales, at \$6.95 per sale, to residents of Oregon during the tax year. IS contracts with an Oregon mailing service to make deliveries of the merchandise in Oregon (all sales are final). IS does not have substantial nexus in Oregon. Even though activities in greater volume might be sufficient for nexus, the amount of sales is de minimis.

Example 3: WB Distributing Company (WB) has for many years distributed wine and beer throughout Oregon, through Oregon licensed distributors with whom WB has distribution agreements. WB is required to obtain and maintain a wholesaler's license from the Oregon Liquor Control Commission (OLCC). A condition of the license is that WB must make monthly reports of sales volumes to the OLCC. WB also periodically seeks advice and approval from the OLCC for special event activities in Oregon, at which no sales are solicited by the corporation. WB has substantial nexus in Oregon.

Example 4: IP Company (IP), organized under Delaware law and wholly owned by FP Company (FP) a foreign parent, owns intellectual property including trade marks, trade names, and logos. RS Company (RS), also wholly owned by FP but not unitary with IP, operates retail stores in Oregon that prominently and beneficially use the intellectual property owned by IP. By agreement, RS pays IP five percent of its gross sales for the right to use the intellectual property. IP has substantial nexus in Oregon.

OAR 150-317.010(4) — Definition: "Doing Business"

(1) A taxpayer is doing business when it engages in any profit-seeking activity in the State of Oregon. What transaction or transactions need be entered into within this state in the course of such an activity to constitute the doing or carrying on of business within the state is primarily a question of fact, depending upon the circumstances in each case.

Example 1: The taxpayer is clearly doing business within this state if it occupies, has, maintains or operates an office, shop, store, warehouse, factory, agency or other place within this state where some of its affairs are systematically and regularly carried on, notwithstanding the fact that it may also enter into transactions outside this state.

Example 2: A corporation engaged in the sale of tangible personal property is doing business within this state if sales activities are regularly carried on within this state by an employee or agent of the seller, and if either a stock of goods is maintained within this state, or an office or other place of business where affairs of the corporation are regularly carried on is maintained within this state.

Example 3: A foreign corporation consigns goods to one or more consignees within Oregon who then sell the goods. The foreign corporation is doing business in Oregon since it has sales activity and a stock of goods within Oregon.

(2) A foreign corporation whose business is providing services is "doing business" in this state if it has employees providing those services in Oregon. It does not matter whether the services are provided on the client's property or on the corporation's own property since it is engaged in a profit seeking activity in Oregon.

(3) If a foreign corporation's business activities in this state are confined to purchase and storage of personal property incident to shipment outside the state, the corporation is not deemed to be doing business for corporation excise tax purposes if the following conditions are met:

(a) The personal property remains in the exact state or form as it was when purchased during the time it is located within Oregon.

(b) The foreign corporation is not an affiliate of another foreign or domestic corporation, as defined in section 1504 of the Internal Revenue Code, which is doing business in Oregon.

(4) A foreign or extranational banking corporation, or foreign association is not deemed to be "doing business" and is not subject to an Oregon tax measured by or imposed upon net income on account of taking, acquiring, holding and enforcing notes secured by real estate mortgages or trust deeds. However, such company is "doing business" when it acquires real property covered by such mortgages or trust deeds and is subject to the Oregon corporation excise tax. Section 2, Chapter 30, Or Laws 1999.

(5) The fact that a corporation has no employees in Oregon does not mean the corporation is not doing business in this state. If activities are performed in Oregon by a third party on behalf of the corporation, and the activities are not protected under Public Law 86-272, the corporation is doing business in Oregon.

Example 4: The provision of in-state repair and warranty services by an independent contractor for a direct marketing computer company, advertised as part of its standard warranty or as an option that can be separately purchased, contribute significantly to the company's ability to establish and maintain its market for computer hardware sales in Oregon. Therefore, the computer company is doing business in Oregon. The extension of immunity for activities by independent contractors under Public Law 86-272 does not include repair and warranty service.

(6) A corporation that is not "doing business" in Oregon may still be subject to tax in this state. The Oregon corporation income tax under ORS Chapter 318 imposes tax on corporations that have income derived from sources within Oregon. See OAR 150-318.020(2) for a list and description of the activities that, if conducted in Oregon, will result in a corporation being subject to the corporation income tax.