Testimony to the Oregon State Legislature House Committee on Revenue

Concerns with House Bill 2099: Relating to tax reporting of multinational corporations

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Chairman Barnhart, Vice-Chair Bentz, Vice-Chair Vega Pederson, and Members of the Committee, thank you for the opportunity to provide testimony today on behalf of the Council On State Taxation (COST) regarding our concerns with H.B. 2099, a bill to modify, and generally expand, the list of purported "tax haven" countries singled out for inclusion in the Oregon corporate income tax base. This legislation follows actions taken by the Oregon State Legislature in 2013 to designate certain jurisdictions as tax havens. Once this process is undertaken, we believe it is only a matter of time until some of the United States' key trading partners are unilaterally "blacklisted" in an attempt to form federal tax policy at the state level. Because of the inherent flaw in the state tax haven approach – an approach the U.S. Government has never embraced – COST respectfully urges this Committee to abandon this effort to further target U.S. trading partners for discriminatory treatment and instead look for more precise and equitable methods to address any perceived tax avoidance.

About COST

COST is a nonprofit trade association based in Washington, DC. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce and today has an independent membership of approximately 600 major corporations engaged in interstate and international business. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities.

Tax Haven Lists are Arbitrary and Misleading

As COST stated in June 2013 when the original tax haven proposal was still under consideration by the Oregon State Legislature, the branding of specific nations as "tax havens," thereby penalizing companies merely doing business or incorporated there, is a counterproductive tax policy. "Blacklisting" specific countries is overly broad, and it may result in double taxation of legitimate business activities. In fact, the blacklisting approach has been almost universally rejected as a means of dealing with tax avoidance strategies; of the few states with any "tax haven" provisions, only Montana and Oregon have taken the "blacklist"

approach of designating specific countries as tax havens through legislation. It is instructive that the California Legislature conducted an extensive examination of such a "tax haven" approach and rejected it.[1]

The "tax haven" lists are derived largely from a list created over 15 years ago by the Organization for Economic Co-operation and Development (OECD) to encourage countries to adopt greater transparency and information sharing about tax issues, not to broaden the tax base of member countries. As of today, no countries remain on the OECD's list of uncooperative tax jurisdictions. Moreover, neither the United States nor any other OECD nation has ever adopted the "tax haven" list approach as a means for defining their income tax base. Neither state legislatures nor state revenue departments are equipped to make determinations the U.S. Government declined to exercise.

The greatest flaw in the "tax haven" listing approach, however, is perhaps demonstrated by the choice now facing this Committee: whether and how to adjust the list.

The Oregon Department of Revenue, in its January 1, 2015 report to the Legislature, applied certain criteria developed by the Multistate Tax Commission (MTC) against its understanding of the tax regimes in certain countries. As a result of this exercise, several new jurisdictions, including The Netherlands and Switzerland, are recommended for inclusion in Oregon's statutory list. It is not clear why certain countries (such as Ireland, which is included in a Montana proposal left in committee, S.B. 167, and a current Maine proposal, L.D. 341) are not examined in the Oregon Department of Revenue's report. Instead, certain countries are selected for evaluation under the MTC criteria, which are in turn taken from the aforementioned OECD approach. Other testimony to this Committee, from affected nations and from foreign direct investors in Oregon, reflects the grave concerns with expanding the tax haven list to these countries. However, we wish to highlight this exercise is itself arbitrary and, if taken to its logical conclusion, would put Oregon in a difficult position as it courts investment from abroad.

The Slippery Slope to Worldwide Unitary Combination

Tax haven lists apply, on a selective country-by-country basis, the discredited "worldwide" combination method for the state taxation of multinational businesses. State attempts in the 1970s to tax the income of the worldwide unitary group, including entities with no U.S. presence, created considerable apprehension among both foreign governments and foreign and domestic multinational business enterprises, instigating what many thought would be an international tax war. Indeed, in 1985, the United Kingdom took the unprecedented approach of approving legislation that would have allowed the U.K. Treasury to penalize multinational companies with operations in any U.S. state employing worldwide combination. A Presidential Working Group agreed to forestall federal intervention if states limited unitary combination to a domestic water's-edge approach.[2] Tax haven legislation undermines the 30-year consensus

[1] See the California report here: http://caleuropeantrade.senate.ca.gov/sites/caleuropeantrade.senate.ca.gov/files/Waters_Edge_CA_Jobs_and_International_Investment_Opportunities_5-19-2010.pdf

[2] Final Report of the Worldwide Unitary Taxation Working Group, Chairman's Report and Supplemental Views (August 1984).

among the states to limit their income tax base to the "water's-edge" and avoid the taxation of income earned outside the United States. The blacklisting of designated "tax haven" countries also interferes with U.S. foreign relations, threatening our nation's ability to "speak with one voice" in its dealings with our key trading partners. This interference in foreign affairs raises constitutional concerns, and state tax haven statutes likely will be subject to judicial challenge in the coming years.

Tax Haven Lists Unsuitable to Address Tax Avoidance Concerns

While the international community searches for solutions to the issue of base erosion and profit shifting (called "BEPS"), it should be noted that instituting a tax haven list is not being, and has not been, considered by the OECD. Further, U.S. states have extensive experience in shoring up the corporate tax base and addressing tax avoidance. These methods include participating in information-sharing with the IRS, adjusting intercompany income (*e.g.*, I.R.C. Section 482 powers), asserting alternative apportionment, applying common-law doctrines and state statutory standards of business purpose and economic substance, and requiring the "addback" of otherwise deductible expenses for certain payments (*e.g.*, interest and/or royalties) to related parties. The wisdom of such actions aside, they all reflect a focus on specific transactions or corporate arrangements, rather than casting a blanket aspersion on entire nations and their international trade. Tax haven designations invite retaliatory action by other countries and, at a minimum, work to decrease investment in adopting states by both foreign-based businesses and U.S. domestic businesses engaged in multinational operations. While the states' desire to address complexities of global commerce and instances of tax evasion are understandable, tax haven lists are a clumsy and ineffective method detrimental to states' own interests.

COST respectfully urges this Committee to reject H.B. 2099 and instead examine policy options that are coherent and effective in addressing clearly articulated concerns with income shifting and tax avoidance. I welcome any questions from the Committee, and thank you for hearing COST's concerns this afternoon.