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2020 Tax Ballot Measures: Portland Area Voters Prefer Taxes Targeted at the "Wealthy" Over Taxes with a Broader Base, Journal of Multistate Taxation and Incentives, Feb 2021

SHOP TALK

2020 Tax Ballot Measures: Portland Area Voters Prefer Taxes Targeted at the "Wealthy" Over Taxes with a Broader Base

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In the primary election on May 19, 2020 and the general election on November 3, 2020, the ballots for voters in and around Portland, Oregon contained three tax measures: a personal income tax and business income tax (primary election), a personal income tax (general election), and a tax on employers measured by wages (general election). The personal income taxes only applied to higher earners. The wage tax, on the other hand, applied to all businesses with over 25 employees. Portland-area voters approved the personal income taxes (and the business net income tax) and rejected the wage tax.

Metro Personal Income Tax and Business Net Income Tax

Metro is a regional government authority for three counties in the greater Portland area: Clackamas County, Multnomah County, and Washington County. On May 19, 2020, Metro voters approved Ballot Measure 26-210. The measure creates new personal and business income taxes in the tri-county Metro region, beginning with the 2021 tax year.

- Personal Income Tax. The measure imposes a one percent (1%) personal income tax on taxable income over $200,000 for joint filers and over $125,000 for taxpayers filing singly—no personal income tax applies to a taxpayer's net income below these thresholds. A Metro nonresident must pay this tax, but only if the nonresident has taxable income derived from sources within Metro above the thresholds. The measure adopts a policy of following Oregon state laws and the Oregon Department of Revenue's administrative rules related to the Oregon personal income tax.
- Business Income Tax. The measure imposes a one percent (1%) tax on the net income of each person doing business in the Metro district that has total gross receipts over $5 million. The measure refers to this tax a "business profits tax." This tax applies to the entire net income of businesses subject to the tax, not just net income over the $5 million. The measure adopts a policy of following the Multnomah County business income tax (the "MBIT") rules and procedures as guidance.

Metro will use the proceeds from the taxes to fund collection of the taxes,[1] the creation of plans to combat homelessness within the Metro district (Metro went to voters before developing a proposal for how to spend the money), and the implementation of these plans.

The measure leaves numerous questions regarding the taxes unanswered, including:

- Pass-Through Entities and Possible Double Taxation. The measure does not contain any provision concerning imposition of the personal income tax on flow-through income from a business subject to business income tax. Further, the policies of following Oregon personal income tax for the personal income tax and the MBIT for the business income tax provide no guidance. The Oregon personal income tax generally follows federal income law regarding the inclusion of income from pass-through entities on personal returns. The MBIT, on the other hand, is paid at the entity level, including single-member LLCs treated as disregarded entities, partnerships, and S corporations. If the state personal income tax rules are applied to the Metro personal income tax and the MBIT rules are applied to the business profits tax, the income of a pass-through entity that flows through to its members could be subject to both taxes.
- Small Business Exemption. The measure does not address whether the exemption for small businesses (those with total gross receipts "from all business income" of $5 million or less), will be applied on (i) an entity-by-entity basis, or (ii) a consolidated or combined basis. The MBIT contains an exemption for businesses with gross receipts of less than $50,000, measured on a consolidated basis. Metro likely will adopt similar rules for its exemption.
- Apportionment of Income. Nothing in the measure explicitly limits the business profits tax to Metro district-source net income, although the MBIT does so. To avoid federal constitutional issues, and in light of the measure's reference to the rules for the MBIT, Metro likely will adopt rules to provide that, in the case of an entity that does business both within and outside of Metro, the tax will be based on income apportioned to Metro.

- Sourcing Rules. The measure lacks rules for sourcing income for either tax. Metro likely will adopt the sourcing rules used for the Oregon personal income tax for the personal income tax, and the sourcing rules used for the MBIT for the Metro business income tax. The MBIT sourcing rules differ in some material respects from the Oregon sourcing rules applicable to businesses pursuant to Oregon's version of the Uniform Division of Income for Tax Purposes Act (UDITPA). For example, for sales other than sales of tangible personal property, the MBIT uses costs of performance, while the Oregon UDITPA uses market-based sourcing. This could result in the same income being apportioned differently to calculate the taxable income of a flow-through business and the taxable income of the individual owners of that business.
- Estimated Taxes/Wage Withholding. The measure does not address whether Metro may require payment of estimated taxes or personal income tax withholding. The MBIT requires estimated tax payments and withholding on wages is required for the Oregon personal income tax.

Multnomah Personal Income Tax

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Portland, Oregon is in Multnomah County. As noted above, however, the Portland metro area also includes Clackamas County and Washington County, with many of the individuals working in Multnomah County (Portland) residing in these two other counties (or the state of Washington). On November 3, 2020, Multnomah County voters approved Measure 26-214. The measure creates a personal income tax on Multnomah County residents and taxable income of nonresidents derived from Multnomah County beginning with the 2021 tax year.

The new personal income tax applies to taxable income over $200,000 for joint filers and over $125,000 for taxpayers filing singly—no tax applies to a taxpayer's net income below these thresholds. The tax rate is 1.5 percent but increases to 2.3 percent with the 2026 tax year. The 1.5 percent rate (before 2026) and the 2.3 percent rate (in and after 2026) increase to 3.0 percent and 3.8 percent, respectively, on taxable income over $400,000 for joint filers and over $250,000 for taxpayers filing singly.

Multnomah will use the proceeds from the new tax to establish a tuition-free preschool program for children who have parents or legal guardians who reside in Multnomah County. The preschool system is scheduled to begin in September 2022. All families in Multnomah County will be eligible to apply for the program. However, Multnomah County will prioritize families that have the least access to high-quality preschool.[2]

The Multnomah measure directs the county financial administrator to adopt rules generally consistent with the Oregon personal income tax rules. The measure leaves open the same unanswered questions as the measure imposing the Metro personal income, including:

- Pass-Through Entities and Possible Double Taxation. As discussed above, Multnomah imposes the MBIT, which applies to pass-through businesses (*e.g.*, partnerships, S corporations and sole proprietorships). The measure does not contain any provision concerning imposition of the new personal income tax on flow-through income from a business subject to the MBIT.
- Sourcing Rules. The measure lacks sourcing rules for determining a nonresident's taxable income derived from Multnomah County, including flow-through income from a business. As noted above, the MBIT uses different sourcing rules than the Oregon version of UDITPA that can apply for Oregon personal income tax purposes. Further, Oregon personal income tax law generally sources wages based on where the employee performed the services, without applying the so-called “convenience of the employer” test.[3] As discussed below, Multnomah may prefer a rule based on the location of the employer's office.[4]
- Estimated Taxes/Wage Withholding. The measure does not address whether Multnomah County may require payment of estimated taxes or personal income tax withholding.

Multnomah has a history of imposing a personal income tax. In a special election in May 2003, Multnomah voters approved Measure 26-48, which included a temporary, graduated personal income tax that sunset after three years. That personal income tax, however, only applied to residents of Multnomah—the tax did not apply to nonresidents who worked in Portland (including Multnomah residents who moved to Clackamas County and Washington County before the tax went into effect). The newly enacted tax solves for this by taxing nonresidents on income derived from Multnomah County. However, with the increased use of remote working prompted by the COVID-19 pandemic, nonresidents may find a benefit in using a schedule that divides working from home and the office in a manner that ensures that income derived from Multnomah remains below the income thresholds. This assumes that Multnomah will use a sourcing rule similar to the Oregon personal income tax for wages.

Rejected Metro Wage Tax

On November 3, 2020, Metro voters rejected Ballot Measure 26-218. The measure would have imposed a tax on employers with more than 25 employees (other than state and local governments) of up to 0.75 percent of wages, beginning with the 2022 tax year. The tax would have funded transportation improvements.

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[1] Metro currently does not impose a personal income tax or business net income tax. However, the City of Portland administers both its business income tax (the Business License Tax) and the Multnomah County business income tax. Metro and Portland entered into an agreement pursuant to which Portland will administer these new Metro taxes.

[2] At first blush, it may seem problematic that nonresidents of Multnomah County pay the tax, but their children cannot participate. The prioritization of families with the least access to high-quality preschool, however, likely means that none of the taxpayers (resident and nonresident) will have children who can attend the new preschool system.

[3] *See* OAR 150-316-0165(1)(a) ("Except as provided in section (2) of this rule, the gross income of a nonresident (who is not engaged in the conduct of the nonresident's own trade or business, but receives compensation for services as an employee) includes compensation for personal services only to the extent that the services were performed in this state.") (Emphasis added)).

[4] For example, New York State recently announced an aggressive position for sourcing to New York wages earned by nonresident employees working from home during the COVID-19 pandemic for a New York-based employer. *See* New York Department of Taxation and Finance FAQ (*available at* https://www.tax.ny.gov/pit/file/nonresident-faqs.htm#telecommuting).

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