OREGON STATE BAR

Taxation Section

VOLUME 16, NUMBER 1 Winter 2013

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Left Coast Economic Nexus

Valerie H. Sasaki

In the computer hardware area, Moore's law observes that the number of transistors on integrated circuits doubles every two years. The number of mechanisms that state and local governments employ to assert taxable nexus against our clients has only increased at a slightly slower rate. The changing standards are typically adopted in reaction to changing business practices and perceived abuses. As most states will assert their ability to tax a business or transaction to the full extent of constitutional law, the *Complete Auto Transit* four prong test is very relevant to this inquiry. 430 US 274 (1976). In *Complete Auto*, the United States Supreme Court held that a tax survives Commerce Clause scrutiny if the tax: (1) is applied to business or activity that has "substantial nexus" to the taxing state; (2) is fairly apportioned among the states; (3) does not discriminate against interstate commerce; and (4) is fairly related to services that the taxing state provides. Of these, taxing agencies and practitioners have wrestled with what constitutes "substantial nexus".

Given the condition of the economy, it is not surprising that the recent trend is towards a more expansive definition of the activities that give rise to substantial (read: taxable) nexus. States want to increase the number of taxpayers that pay into their jurisdictions and they are more than happy to export that burden to taxpayers located outside of their borders. Expanding the nexus standards is not an inherently bad thing. Nexus with, and the ability to source a transaction to, a low rate jurisdiction beats paying tax on that transaction in a higher rate jurisdiction. However, a problem arises where a taxpayer's footprint (the jurisdictions where they have nexus) expands faster than their ability to keep track of where they need to be filing returns. Thus, the first inkling a taxpayer may have that they are taxable in a particular state is when they receive an innocuous-looking questionnaire from a state where they have customers. A problem also may arise where inconsistent sourcing rules could cause the transaction to be taxed twice.

The nexus trends that have received the most publicity in the last several years are many states' implementation of agency and affiliate nexus rules. These states implemented so-called "Amazon" rules to address the perceived abuse of an out-of-state company using an in-state, non-employee affiliate to drive sales to an online vendor that didn't otherwise have taxable presence in the state. This is a classic example of state revenue authorities responding to the new (in this case technological) ways that business is conducted.

In the Pacific Northwest, practitioners received many phone calls this summer from Oregon businesses worried that their sales to Washington customers could subject them to Washington sales/use and Business and Occupation tax ("B&O"). In some cases, they were utilizing an agent to deliver products across the river to their customers. Depending on the client's facts, the use of a Washington based agent to develop and maintain a market may create taxable nexus with Washington.

A trend that has received significantly less press, perhaps because the incidence of taxation falls on businesses more frequently than individuals, is the significant increase in the number of states that are implementing factor presence, also known as economic nexus, standards.

Economic Nexus

In *Quill Corporation v. North Dakota*, the U.S. Supreme Court held that a taxpayer had to have a physical presence in North Dakota as a pre-requisite to sales tax nexus.[1] Courts since *Quill* have narrowly construed that case to only apply to the application of a state's sales tax.[2]

Several interesting state tax planning strategies that came out of the mid-1990s were designed to separate economic activity from taxable nexus. These strategies sought the holy grail of tax planning – so-called "nowhere" income, which is income that would entirely escape state tax. State taxing authorities were generally appalled at these nexus-isolation strategies and implemented various rules to combat the perceived abuse.

One of the early cases in response to this planning trend involved a Toys R Us structure that isolated intellectual property in a second-tier affiliate ("Geoffrey") that only had taxable nexus in very limited jurisdictions.[3] Geoffrey licensed the intellectual property to the operating company, Toys R Us. Toys R Us opened stores in South Carolina and deducted royalty payments to Geoffrey on its state tax return. South Carolina was a separate filing jurisdiction, so Geoffrey was not included in the Toys R Us state return. South Carolina took a dim view of this and sought to compel Geoffrey to pay South Carolina tax on the royalty payment. The courts held that Geoffrey had purposefully directed its activities towards and sought the economic benefit of the use of the intangibles in the state. The court also held that the presence of intangible property in a jurisdiction was sufficient to create taxable nexus.

The Multistate Tax Commission Steps In

The Multistate Tax Commission (www.mtc.gov) is a member organization of state Departments of Revenue. In response to the nexus isolation structures that taxpayers were implementing, the MTC proposed and approved factor presence or "economic" nexus standards on October 17, 2002. This proposal said that substantial nexus is established if a taxpayer exceeds the following bright-line thresholds during a single tax period:

- $50,000 of property;
- $50,000 of payroll;
- $500,000 of sales; or
- 25 % of total property, total payroll, or total sales.[4]

The proposal also utilized a fairly typical sourcing mechanism to determine whether a particular sale should be considered a sale that was includable in a particular state's factor.

Washington and Oregon are both full compact members, as was California until it dropped out of the compact, in anticipation of the recent opinion(s) in ***Gillette v. Franchise Tax Board***.[5]. Thus, it was not surprising that all three states have adopted economic nexus rules to expand the nexus parameters for taxpayers who have "substantial nexus" with that state.

Washington

The Washington legislature implemented an economic nexus statute effective June 1, 2010. This law does not apply to all taxpayers, only to out-of-state businesses that fall into the "service or other" B&O tax classification (including, as it happens, most law firm activities) and that provide specific, enumerated services to Washington customers, or that receive royalty payments for licensing intangible property to Washington customers. A taxpayer who is subject to the new economic nexus standards will be required to register and pay Washington B&O tax if it has:

- More than $50,000 of property in Washington;
- More than $50,000 of payroll in Washington;
- More than $250,000 of receipts in Washington; or,
- More than 25% of that taxpayer's total property, payroll, or sales in Washington.[6]

The Washington Department of Revenue may adjust these thresholds if the Consumer Price Index changes by five percent or more from the effective date of the law. Interestingly, the Washington Department of Revenue stated that there is an effective "safe harbor" for out-of-state businesses that may have physical presence nexus with Washington but that do not meet any of the economic nexus thresholds.[7] Taxpayers that are not in the B&O tax categories subject to economic nexus are still subject to physical presence nexus rules.

Sourcing rules are utilized to determine what constitutes Washington property, payroll, and sales. For out-of-state sellers with no physical property or payroll in Washington, the rules governing sourcing of sales and royalties are most important. Sales of services are sourced first to where the purchaser receives the benefit of the service then where the benefit of the service is primarily received (if in multiple states). If neither of those are ascertainable, the sale is sourced, in order, to the jurisdiction where: (1) the service was ordered; (2) the bill is sent; (3) where the customer sends the payment from; (4) the customer's address in the seller's records; and finally (5)

1 *Quill Corporation v. North Dakota*, 504 US 298 (1992).

2 *See, e.g., J.C. Penny National Bank v. Johnson*, No. M1998-00497-COA-R3-CV (Tenn. Ct. App. Dec. 17, 1999).

3 *Geoffrey, Inc. v. South Carolina Tax Commission*. 437 SE 2d 13, *cert den*. 510 US 992 (1993).

4 http://www.mtc.gov/uploadedFiles/Multistate_Tax_Commission/Uniformity/Uniformity_Projects/A_-_Z/FactorPresenceNexusStandardBusinessActTaxes.pdf

5 Cal. Ct. App., DKT A130803(July 24, 2012 and October 2, 2012), *See* Cal. SB 1015 (June 27, 2012)

6 RCW 82.04.067 (1), WAC 458-20-19401(3).

7 http://dor.wa.gov/Content/FindTaxesAndRates/BAndOTax/EconomicNexusQnA.aspx

to the seller's commercial domicile. The royalty sourcing rules are similar.

It is worth noting, as has been said before in this publication, that Washington does have a trailing nexus statute.[8] Thus, if a taxpayer meets the nexus thresholds described above, Washington will consider that taxpayer to have taxable presence in Washington for the current and immediately following tax years.

To illustrate how this may play out, take a hypothetical law firm, XYZ, LLP, in Portland, Oregon. Partner X represents Husky, Inc., a Vancouver manufacturer. X performs substantial legal services from her office in Portland, Oregon but never crosses the bridge into Vancouver. Husky, Inc. receives the value of those services in Vancouver, Washington. If Partner X collects $250,000 from Husky, Inc. for her firm, the Washington Department of Revenue may assert that XYZ has taxable nexus with Washington for the current and immediately following years.

Oregon

In the wake of several non-Oregon, high-profile cases that involved financial institutions with substantial customer bases but no in-state physical presence,[9] the Oregon Department of Revenue determined that it needed the additional tool an economic nexus law would provide to tax that type of economic activity.

Despite several proposals, the Oregon Department of Revenue was not successful in persuading the state legislature to adopt an economic nexus statute. Thus, effective May 5, 2008, the Department adopted an administrative rule, OAR 150-317.010, under the general "doing business" statute at ORS 317.010. This rule asserts that "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 the taxpayer in the state."[10] The Department's website is even more oblique, referring merely to "An economic presence through which the taxpayer regularly takes advantage of Oregon's economy to produce income."[11] Although the rule provides several factors that the Department may consider, the rule does not have a bright line test, such as the thresholds the MTC proposed, or define what constitutes "significant economic presence".

Oregon's economic nexus rule applies to all business income/excise taxpayers. Thus, an Illinois widget manufacturer that receives "significant gross receipts attributable to customers in Oregon" may have taxable nexus with Oregon.[12] More unexpectedly, an entity that files reports or returns with Oregon regulatory bodies may also have economic nexus. The regulation presents the example of an out-of-state wine distributor that is required to obtain and maintain a wholesaler's license through the Oregon Liquor Control Commission ("OLCC"). A condition of the license is regular reports to the OLCC. In that case the taxpayer also asks the OLCC for advice and approval related to events in Oregon. The rule concludes that the distributor has taxable nexus in Oregon.

California

The California legislature adopted Revenue and Tax Code Section 23101, which implemented economic nexus, effective January 1, 2011. That statute provides that an out of state entity is considered to be doing business in California if it has:

- More than $50,000 of property in California;
- More than $50,000 of payroll in California;
- More than $250,000 of receipts in California; or,
- More than 25% of that taxpayer's total property, payroll, or sales in California.

This seems very much like the MTC's bright-line test. However, the California Franchise Tax Board ("FTB"), which administers the state's corporate income tax, muddied the water somewhat by asserting on their website that "a taxpayer is doing business in California if it actively engages in any transaction for the purpose of financial or pecuniary gain or profit in California *or* if [any of the bright line tests are met]."[13] In contrast with Washington, the FTB provides the following example:

> "Partnership A, an out-of-state partnership, has employees who work out of their homes in California. The employees sell and provide warranty work to California customers. Partnership A's property, payroll and sales in California fall below the threshold amounts. Is Partnership A considered to be doing business in California?
>
> "Yes. Partnership A is considered doing business in California even if the property, payroll and sales in California fall below the threshold amounts. Partnership A is considered doing business in California through its employees because those employees are "actively engaging" in transactions for profit on behalf of Partnership A."[14]

Depending on the type of business, this may fall within the B&O tax classification of "service and other." Thus,

8 RCW 82.04.220.

9 *See, e.g., Tax Commissioner of the State of West Virginia v. MBNA America Bank, N.A.*, 640 SE 2d 226 (W. Va. 2006).

10 OAR 150-317.010(2).

11 http://www.oregon.gov/dor/bus/Pages/ic-102-695.aspx

12 OAR 150-317.010(3)(d).

13 https://www.ftb.ca.gov/businesses/New_Rules_for_Doing_Business_in_California.shtml (emphasis added); *See*, Daniel De Jong, "California's Not So Bright-Line Nexus Test" http://www.tei.org/news/stateandlocalblog/Lists/Posts/Post.aspx?ID=196

14 https://www.ftb.ca.gov/businesses/New_Rules_for_Doing_Business_in_California.shtml

the same Partnership A could operate in Washington and California with substantially identical facts and have a completely different tax result.

Also effective for tax years beginning on or after January 1, 2011, the California legislature adopted Revenue and Tax Code section 25136, which changes the way that California sources receipts from services. This statute moved California from "cost of performance" (where the sale is sourced to wherever the seller incurred the greatest cost to perform the service) to "market" (where the sale is sourced to the customer location). Receipts relating to the sale of intangibles are also now subject to market sourcing. This can create a problem for a taxpayer that may have traditionally provided services remotely to customers where the greater cost of performing the services occurs outside of California, compared with another jurisdiction. These clients may not be aware that their service sales to California customers are now sourced to California and may rise to the level of the new economic nexus thresholds.

So what?

This may all sound terribly grim, but it is important to recognize that the determination of whether a taxpayer has nexus in a taxing jurisdiction is only one of several threshold questions we must evaluate to determine whether our clients have tax exposure in a particular state. Others include:

- Is what the taxpayer doing taxable? If not, then we would still advise them to consult with us before engaging in other activities that may be taxable.
- Is the taxpayer selling tangible personal property? If a taxpayer's only activities in a jurisdiction are the solicitation of orders for sales of tangible personal property which are sent outside the state for approval or rejection, then the Public Law 86-272 safe harbor may apply in jurisdictions that impose a net income tax, like Oregon and California, and those states may not impose their income tax on that entity or individual. As Washington's tax is based on gross receipts, Public Law 86-272 should not apply.

The law in this area is a moving target. Therefore, we generally encourage our clients to regularly work with us to review their jurisdictional footprint and update their understanding of where they may have tax nexus (economic or otherwise). Clients don't always choose to file in every jurisdiction where they have nexus. They may choose instead to reserve against the exposure that a non-filing position creates. However, with regular review the result is an informed choice and not an unpleasant surprise discovered in an audit.

Attorney Fees in the Oregon Tax Court

By Hertsel Shadian

The Oregon Tax Court has authority to award reasonable attorney fees and expenses (including expert witness fees) to prevailing parties in certain cases. Among the statutory authority for an award of attorney fees in the Oregon Tax Court are ORS 20.105(1) and ORS 305.490(3) and (4);[1] Oregon Tax Court Rule 68C sets out the procedures to request the award of attorney fees in the Oregon Tax Court. The award of attorney fees generally is limited to a "prevailing party," whether the taxpayer or the Department of Revenue,[2] and generally is subject to a set of discretionary factors set out in ORS 20.075 which the court must review and analyze in making its decision to award attorney fees and expenses.

Oregon Revised Statutes 20.105(1) provides that in any civil action, suit or other proceeding in the Oregon Tax Court, "the court shall award reasonable attorney fees to a party against whom a claim, defense or ground for appeal or review is asserted, if that party is a prevailing party in the proceeding and to be paid by the party asserting the claim, defense or ground, upon a finding by the court that the party willfully disobeyed a court order or that there was no objectively reasonable basis for asserting the claim, defense or ground for appeal." As separate authority for attorney fees and expenses, ORS 305.490(3)(a) further provides that an award of reasonable attorney fees and reasonable expenses may be allowed in any proceeding before the tax court judge (and for the prior proceeding in the matter, if any, before the magistrate) which involve "taxes upon or measured by net income in which an individual taxpayer is a party, or involving inheritance or estate taxes, [if] the court grants a refund claimed by the executor or taxpayer or denies in part or wholly an additional assessment of taxes claimed by

1 Breithaupt and Tanner, "*The Oregon Tax Court at Mid-Century*," 48 Willamette L. Rev. 147, 163-65 (Winter, 2011).

2 The Tax Court has held that a prevailing taxpayer is one who improves his or her position. *See, Martin v. Dept. of Revenue*, 9 Or. Tax 1, 2, n.1 (1981) (applying this definition of "prevailing party" to former ORS 305.490(2) (current ORS 305.490(3)) to deny an award of fees in an action in which the Department of Revenue voluntarily conceded its arithmetical error and granted the taxpayer its requested refund); *see also, Ormsby v. Dept. of Revenue*, 18 Or. Tax 146, 182 (2004) (explaining the conditions for an award of fees under former ORS 305.490(2) (current ORS 305.490(3)) and ORS 20.105, denying fees to the taxpayers and awarding fees to the Dept. of Revenue); *Pendell v. Dept. of Revenue*, 847 P.2d 846, 852 (Or. 1993) (denying award of attorney fees to taxpayers, holding that award of fees under ORS 305.447 and former ORS 305.490(2) (current ORS 305.490(3)) was discretionary). However, the Tax Court also has pointed out that ORS 305.490 specifically does not have a "prevailing party" requirement: so long as the taxpayer obtains any relief, the court may award fees. *See, Waterbury v. Dept. of Revenue*, 11 Or. Tax 314, 315-16 (1989); *Dept. of Revenue v. Rakocy*, 15 Or. Tax 389, 391 (2001).

the Department of Revenue to be due from the estate or taxpayer." (For purposes of ORS 305.490(3)(a), reasonable expenses include "accountant fees and fees of other experts incurred by the executor or individual taxpayer in preparing for and conducting the proceeding before the tax court judge and the prior proceeding in the matter, if any, before the magistrate.") In addition, ORS 305.490(4)(a) provides that an award of reasonable attorney fees and reasonable expenses also may be allowed in any proceeding before the tax court judge (and for the prior proceeding in the matter, if any, before the magistrate) which involve "ad valorem property taxation, exemptions, special assessments or omitted property," if the court finds in favor of the taxpayer. (For purposes of ORS 305.490(4)(a), reasonable expenses similarly include "fees of experts incurred by the individual taxpayer in preparing for and conducting the proceeding before the tax court judge and the prior proceeding in the matter, if any, before the magistrate.")

The award of attorney fees to a prevailing party is subject to a set of discretionary factors set out in ORS 20.075 which the court must review and analyze in making its decision whether to award attorney fees and expenses. Pursuant to ORS 20.075(1), in determining whether to award attorney fees in any case in which an award of attorney fees is authorized by statute and in which the court has discretion to decide whether to award attorney fees, a court must consider the following factors:

(a) The conduct of the parties in the transactions or occurrences that gave rise to the litigation, including any conduct of a party that was reckless, willful, malicious, in bad faith or illegal.

(b) The objective reasonableness of the claims and defenses asserted by the parties.

(c) The extent to which an award of an attorney fee in the case would deter others from asserting good faith claims or defenses in similar cases.

(d) The extent to which an award of an attorney fee in the case would deter others from asserting meritless claims and defenses.

(e) The objective reasonableness of the parties and the diligence of the parties and their attorneys during the proceedings.

(f) The objective reasonableness of the parties and the diligence of the parties in pursuing settlement of the dispute.

(g) The amount that the court has awarded as a prevailing party fee under ORS 20.190.

(h) Such other factors as the court may consider appropriate under the circumstances of the case.

Additional factors are set out in ORS 20.075(2) to determine the amount of reasonable attorney fees to be awarded, which include: the time and labor required in the proceeding, the novelty and difficulty of the questions involved in the proceeding and the skill needed to properly perform the legal services; the likelihood, if apparent to the client, that the acceptance of the particular employment by the attorney would preclude the attorney from taking other cases; the fee customarily charged in the locality for similar legal services; the amount involved in the controversy and the results obtained; the experience, reputation and ability of the attorney performing the services; and whether the fee of the attorney is fixed or contingent. Obviously, the practitioner seeking attorney fees and expenses should set out in his or her fee petition all the facts that support each factor weighing in the favor of the taxpayer, focusing in particular on facts that demonstrate any unreasonableness in the Department of Revenue's position or appeal, and factors that support the reasonableness of the amount of the attorney fee and expense request.

In the review of requests for awards of attorney fees in the Oregon Tax Court Regular Division, the court generally has focused on the "objective reasonableness" of an appeal by the losing party from a decision of the Oregon Tax Court Magistrate's Division, where such party subsequently loses again on the merits of the case in the Regular Division.[3] In applying its discretion under ORS 305.490, the tax court has adopted a standard that it generally will award attorney fees and expert witness fees so long as the taxpayer has acted reasonably, at least in cases involving tax disputes of general application.[4] Where the dispute is one involving only the parties, such as a property valuation dispute, then the court generally has not awarded fees.[5] The Oregon Supreme Court has adopted a slightly different guideline under ORS 305.447, where it generally will award fees only when the taxpayer acts reasonably and the Department of Revenue has not. Where the Department has acted reasonably in bringing a claim or appeal, the Supreme Court usually will not award fees (even if the Department is wrong).[6] In abrogating the tax court's prior decision in ***Dept. of Revenue v. Wheeler***, the Supreme Court also recently applied this standard in fee

3 *See, e.g., Dept. of Revenue v. Wheeler*, 18 Or. Tax 129 (2004), *Patton v. Dept. of Revenue*, 18 Or. Tax 111 (2004) (Patton I), and *Patton v. Dept. of Revenue*, 18 Or. Tax 256 (2005) (Patton II).

4 *See, Romani v. Dept. of Revenue*, 10 Or. Tax 64, 72-74 (1984); *see also, Waterbury v. Dept. of Revenue*, 11 Or. Tax 314, 316 (1989); *Johnson v. Dept. of Revenue*, 1996 WL 622215, *2 (1996); *Dept. of Revenue v. Rakocy*, 15 Or. Tax 389, 391-94 (2001); *Dept. of Revenue v. Wheeler*, 18 Or. Tax 129, 137-40 (2004), *on recons*., 18 Or. Tax 232 (2005), abrogated by *Clackamas County Assessor v. Village at Main St. Phase II, LLC*, 352 Or. 144, 282 P.3d 814 (Or. 2012); *Clackamas County Assessor v. Village at Main St. Phase II, LLC*, 2010 WL 2377828, *1 (2010), *decision rev'd*, 352 Or. 144, 282 P.3d 814 (Or. 2012).

5 *See, Allen v. Dept. of Revenue*, 17 Or. Tax 427, 435-36 (2004).

6 *See, Swarens v. Dept. of Revenue*, 890 P.2d 1374, 1377 (Or. 1995); Preble v. Dept. of Revenue, 19 P.3d 335, 336 (Or. 2001).

awards under ORS 305.490 in its decision in *Clackamas County Assessor v. Village at Main Street Phase II, LLC*.[7]

The tax court previously established a standard that on an appeal from the Magistrate's Division, the court—in determining whether to award attorney fees—would consider whether the non-prevailing party received a "reasoned decision" from the Magistrate.[8] To wit, in awarding attorney fees to the Department as a prevailing party, the court stated in *Patton v. Dept. of Revenue* (Patton I) as follows:

> Of substantial importance is the fact that the magistrate, in a reasoned decision, previously considered and rejected taxpayer's arguments. This court has rendered a fee award against the department in such a situation. Although the standards for fee awards against a taxpayer under ORS 20.105 differ from those for awards in favor of a taxpayer under ORS 305.490, the court will nonetheless consider the arguments made to a magistrate, the treatment of those in the magistrate's decision, and the nature of the arguments in this division….those considerations are important in determining whether a taxpayer has an objectively reasonable position at the time proceedings in this division are commenced. (citations omitted.) [9]

However, it is the "reasoned decision" language that the Oregon Supreme Court specifically rejected in its recent decision in *Clackamas County Assessor v. Village at Main Street Phase II, LLC*.[10] In its decision, the Supreme Court stated as follows:

> ORS 20.075(1)(h) permits the court to consider "such other factors as the court may consider appropriate under the circumstances of the case." The problem with the Tax Court's reasoning in Wheeler I, however, is that whether the government sought review of a magistrate's well-reasoned decision is not an "appropriate" basis for awarding fees. As the Tax Court itself recognized in its decision on reconsideration, "'well reasoned' does not mean 'reasonable' or 'correct'; rather, it means well explained." No legitimate objective of the statute permitting an award of attorney fees is served by requiring a party to pay attorney fees simply because the magistrate's decision was well explained. (Citations omitted.)[11]

Accordingly, the Oregon Tax Court's prior decisions in which the court refers to a magistrate's "reasoned decision" in its reasonableness analysis presumably no longer is applicable as an appropriate standard. Notwithstanding the abrogation of the tax court's prior opinion in Wheeler, the tax court likely will continue to "nonetheless consider the arguments made to a magistrate, the treatment of those in the magistrate's decision, and the nature of the arguments in this division….those considerations are important in determining whether a taxpayer has an objectively reasonable position at the time proceedings in this division are commenced" as the court stated in Patton I.

As a final note, magistrates may not award attorney fees and expenses. [12] However, if a case is appealed to the Regular Division, that division may award fees for the entire proceedings in the tax court, including those before a magistrate.[13] Also, ORS 305.490(3) and ORS 305.447 do not authorize fee awards to corporations or government agencies.[14] Those two statutes also do not authorize fees in property tax cases; ORS 305.490(4) does that.[15]

John H. Draneas Wins Oregon State Taxation Section Award of Merit

By Kelvin Adkins-Heljeson

John H. Draneas has been awarded the OSB Taxation Section Award of Merit. The award recognizes and honors those who exemplify professionalism in the practice of tax law in the State of Oregon. "It is a great honor to have been recognized and given the Section's Award of Merit," he said. A founding partner of Draneas & Huglin, P.C. and a Certified Public Accountant, John received his J.D. *cum laude*, from Willamette University and his M.B.A and B.S. from the University of California at Berkeley.

John is an active member of the OSB Tax, Business, and Estate Planning and Administration Sections. John has

7 *Clackamas County Assessor v. Village at Main St. Phase II, LLC*, 352 Or. 144, 282 P.3d 814 (Or. 2012), rev'g 2010 WL 2377828, *1 (2010), and abrogating the decision in Dept. of Revenue v. Wheeler, 18 Or. Tax 129 (2004).

8 *Dept. of Revenue v. Wheeler*, 18 Or. Tax 129, 138-39 (2004), on recons., 18 Or. Tax 232 (2005).

9 *Patton v. Dept. of Revenue*, 18 Or. Tax 111, 128 (2004) (Patton I).

10 *Clackamas County Assessor v. Village at Main St. Phase II, LLC*, 352 Or. 144, 282 P.3d 814 (Or. 2012), rev'g 2010 WL 2377828, *1 (2010), and abrogating the decision in *Dept. of Revenue v. Wheeler*, 18 Or. Tax 129 (2004).

11 *Clackamas County Assessor v. Village at Main St. Phase II, LLC,* 352 Or. 144, 154-55, 282 P.3d 814 (Or. 2012).

12 *See, Ellibee v. Dept. of Revenue*, 2003 WL 21241328, at *3 (2003) (magistrate denied Dept. of Revenue's request for attorney fees).

13 *See, Allen v. Dept. of Revenue*, 17 Or. Tax 427, 432 (2004); *Dept. of Revenue v. Wheeler*, 18 Or. Tax 129, 140 (2004).

14 *See, Portland Gen. Elec. v. Dept. of Revenue*, 1988 WL 126215, *1-2 (1988) (holding that the former version of ORS 305.490(3) only applies to "natural persons"); *Martin v. Dept. of Revenue*, 9 Or. Tax 1, 2 n.1 (1981) (holding that former version of ORS 305.490(3) does not apply to corporations or government agencies); *Sch. Dist. No. 1 v. Multnomah Cnty.*, 9 Or. Tax 362, 370 (1983) (nor to school districts); *Martin v. Dept. of Revenue*, 9 Or. Tax 100, 111 n. 34 (1981) (noting that ORS 305.447 applies to individuals), rev'd on other grounds, 655 P.2d 168 (Or. 1982).

15 *See, Port of Coos Bay v. Dept. of Revenue*, 691 P.2d 100, 105 n. 5 (Or. 1984) (rejecting claim that ORS 305.447 applies to property tax cases); *see also, Dept. of Revenue v. Kelly*, 2010 WL 1256058, *2-3 (2010) (interpreting ORS 305.490(4) to include all property tax cases).

also served as the Chair of the OSB Tax Section. He has a lengthy record of giving back to the legal community. John has been a driving force in the Oregon Tax Institute, which is now in its 12th year, and has recruited a number of nationally recognized speakers for the event. John has been a frequent speaker and program planner for OSB CLEs. Finally, he has written numerous articles, testified before the legislature on pending legislation, and provided pro bono service. He has previously been recognized by the Oregon Society of Certified Public Accountants for his service.

John is an active contributor to the Estate Planning and Administration Section list-serv, and sees it both as an opportunity to learn, and an opportunity to teach. "Mentoring was not necessarily something I had by going out on my own. It is a struggle to find mentors, but I have made some great friendships and partnerships through the years. The list-serv comes down to forming alliances with other attorneys."

His practice focuses on business, tax, and estate planning. "Our clients define our practice. I feel that I have been fortunate to represent a lot of talented people." In addition to providing clients exemplary business, tax, and estate planning services, he has developed a niche market in classic car collector law. He has published numerous articles on the subject, and is a renowned expert in the field. He is a past-president of the Oregon region of the Porsche Club of America and a founder of the Friends of PIR, a 501(c)(3) organization dedicated to the preservation and improvement of the Portland International Raceway. He also races in the Sports Car Club of America, and has been a frequent top-10 finisher.

John is a member of the OSB, ABA, OSCPA, and the Estate Planning Council of Oregon. He is also a Fellow in the American College of Trusts and Estates Counsel (ACTEC), and has been recognized by his peers as an Oregon Super Lawyer every year since 2007.

About the award: Any active OSB member in good standing is eligible to receive the OSB Tax Section Award of Merit. The Award is granted to the candidate whom the Executive Committee believes to best personify the OSB's Statement of Professionalism, and best serves as a role model for other lawyers. Factors considered include reputation, conduct, leadership activities and service within the bar or the community in general, and pro bono service. The candidate's accomplishments must fall within the tax field.

Treasury Proposes Necessary and Long-Awaited Amendments to Circular 230 – Written Advice Disclaimers May Be a Thing of the Past

By: Larry J. Brant and Jonathan Cavanagh***

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**Jonathan Cavanagh is an Associate in the law firm of Garvey Schubert Barer, P.C.

I. Introduction[1]

Pursuant to 31 U.S.C. § 330, the Department of the Treasury ("Treasury") is authorized to issue regulations governing practice before the Internal Revenue Service ("IRS" or "Service"). The bulk of the regulations issued under this authority are contained in Circular 230 ("C230").[2]

C230 defines "practice before the Service" and provides:

> PRACTICE BEFORE THE INTERNAL REVENUE SERVICE COMPREHENDS ALL MATTERS CONNECTED WITH PRESENTATION TO THE INTERNAL REVENUE SERVICE OR ANY OF ITS OFFICERS OR EMPLOYEES RELATING TO A TAXPAYER'S RIGHTS, PRIVILEGES, OR LIABILITIES UNDER LAWS OR REGULATIONS ADMINISTERED BY THE INTERNAL REVENUE SERVICE. SUCH PRESENTATIONS INCLUDE, BUT ARE NOT LIMITED TO, PREPARING AND FILING DOCUMENTS, CORRESPONDING AND COMMUNICATING WITH THE INTERNAL REVENUE SERVICE, AND REPRESENTING A CLIENT AT CONFERENCES, HEARINGS, AND MEETINGS.

C230 applies to attorneys, certified public accountants, enrolled agents, enrolled actuaries, registered tax return preparers, enrolled retirement plan agents, and all other persons representing taxpayers before the Service (collectively "Tax Advisors"). It is broad in scope and generally covers:

- Rules relating to who may practice before the IRS;
- Duties and restrictions relating to practice before the IRS;
- Sanctions for rule violations; and
- Discipline of Tax Advisors.

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1 This Article is for educational purposes only and should not be relied upon as tax or legal advice. Another version of this Article was previously published. Treasury Proposes Long-Awaited Amendments to Circular 230, *The Oregon Certified Public Accountant,* November/December 2012.

2 31 CFR part 10.

II. Evolution of C230

Treasury and the Service have consistently echoed the same theme – Tax Advisors must meet minimum standards of conduct relative to the rendering of written tax advice. Those who do not meet these standards will be subject to disciplinary action, including censure, suspension or disbarment. In furtherance of these principles, Treasury has, from time to time, amended C230 to keep pace with the ever changing field of tax.

1984

In February 1984, Treasury amended C230 in response to the proliferation of tax shelters ("1984 Amendments"). The 1984 Amendments required any Tax Advisor opining on a tax shelter to do the following: exercise responsibility regarding the accuracy of the relevant facts; apply the law to the particular facts; ensure all material federal tax issues are considered; if possible, provide an opinion about the likely outcome of each material tax issue; evaluate which of the material tax benefits, in the aggregate, will be realized; and ensure the tax shelter opinion is accurately described in the offering materials.

2001

In 2001, again in response to tax shelters, Treasury proposed amendments to C230 ("2001 Amendments"). The 2001 Amendments addressed practice before the IRS and expanded the rules on written tax shelter opinions. While the proposed amendments relating to practice before the IRS were eventually finalized, the proposed amendments relating to tax shelter opinions were not.

2003

On December 30, 2003, Treasury took another stab at modifying the standards for tax shelter opinions ("2003 Amendments"). The 2003 Amendments included best practices for Tax Advisors and modifications of the standards on tax shelter opinions. In addition, Treasury set the stage for future expansion of C230. The 2003 Amendments made it clear Treasury might impose standards for written advice on matters that had the potential for tax avoidance or evasion.

2004, 2005 and 2006

In response to numerous public scandals involving unscrupulous tax and accounting practices (such as those involving Enron, Global Crossing, ImClone, WorldCom, Qwest, Tyco, Lucent, HealthSouth, Adelphia, and the collapse of Arthur Anderson),[3] Treasury made significant broad-reaching revisions to the 2001 and 2003 Amendments when it issued final regulations ("Final Regulations"). The Final Regulations were published in December 2004,[4] but amended in May 2005[5] before their effective date ("2005 Amendments").

The American Jobs Creation Act of 2004 ("AJCA") was signed into law by President George W. Bush on October 22, 2004. One of the provisions of the AJCA gave Treasury authority to impose standards for written advice relating to matters that have the potential for tax avoidance or evasion.[6] In addition, it gave Treasury authority to impose monetary penalties against Tax Advisors who violate C230.[7] Neither the Final Regulations nor the 2005 Amendments incorporated these provisions of the AJCA. Nevertheless, given the government's strong campaign aimed at extinguishing unscrupulous behavior by Tax Advisors, it was clear that future regulations would give Treasury the authority to impose monetary penalties against Tax Advisors and their firms for violating C230.

Treasury seized the opportunity. In February 2006, Treasury published proposed regulations ("2006 Proposed Amendments"), further overhauling C230. The 2006 Proposed Amendments, if adopted, would have expressly granted Treasury the authority to impose monetary penalties against Tax Advisors (and their firms) for C230 violations.

The Final Regulations were aimed at two specific goals:

- Deterring taxpayers from engaging in abusive transactions by limiting or eliminating their ability to avoid penalties via inappropriate reliance on advice of Tax Advisors; and
- Preventing unscrupulous Tax Advisors and promoters from marketing abusive transactions and tax products to a large number of customers based upon an opinion that fails to adequately consider all the relevant facts.

Most Tax Advisors support these goals. In traditional fashion, however, Treasury used nuclear weaponry to combat the problem facing our federal tax system when a less lethal approach would have been adequate. The Final Regulations go way beyond the stated goals. Most Tax Advisors believe the Final Regulations (even as amended by the 2005 Amendments and the 2006 Proposed Amendments) are so strong and overbroad that they in fact constrain federal tax advice. Consequently, Treasury has been bombarded with written commentary from individual Tax Advisors, bar associations, accounting societies, law firms, accounting firms, securities dealers, industry groups, and other interested persons, complaining about the Final Regulations. Following are the most significant features of the Final Regulations (as amended by the

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3 Cono R. Namorato, Director of the Service's Office of Professional Responsibility from December, 2003, until his departure in 2005, reflected on these scandals, and the Service's response to them, in a recent interview: "There was a perspective that there were a lot of abuses in the [tax] profession during the 1990s…A voluntary tax system cannot function without scrupulous tax practitioners." WebCPA.com, *Former OPR Chief Aimed to Make it Visible, Effective,* Aug. 7, 2006, http://www.WebCPA.com.

4 T.D. 9165, 69 Fed. Reg. 75839 (Dec. 20, 2004).

5 T.D. 9201 70 Fed. Reg. 28824 (May 19, 2005).

6 P.L. 108-357, § 822(b).

7 P.L. 108-357, § 822(a).

2005 Amendments and 2006 Proposed Amendments): they create aspirational "Best Practices" standards for Tax Advisors; they set forth stringent requirements for "Covered Opinions" and other "Written Advice" given by Tax Advisors; they attempt to deter taxpayers from engaging in abusive transactions by limiting or eliminating their ability to avoid penalties via inappropriate reliance on advice of Tax Advisors; and they curb the ability of promoters to market abusive transactions and tax products to a large number of customers based upon an opinion of a Tax Advisor that fails to adequately consider all relevant facts or law.

The outcry from the tax community focused primarily on provisions in Section 10.35 of C230. These provisions relate to "Covered Opinions" (a subset of "Written Advice"). Tax Advisors have criticized these rules for being expensive and difficult to apply, and for applying to types of written communications that some believe the government does not really intend to regulate.[8] In fact, Cono Namorato, past Director of the Office of Professional Responsibility ("OPR"), has publicly stated: "My personal opinion today is that we don't need Section 10.35 in Circular 230. This is a conclusion I came to halfway through my tenure as OPR director. It is so complicated as to be almost unenforceable from an OPR point of view."[9]

As a result of Section 10.35, the world has witnessed the proliferation of disclaimers in all types of written communications. Out of an abundance of caution and due to the overbroad language used in C230, the disclaimers have not been limited to communications containing tax advice.

Finally, Treasury and the Service have acknowledged the tax community's concerns. In fact, they have concluded that the Covered Opinion rules are overbroad, are burdensome to apply, provide minimal taxpayer protection, and that the benefits of the rules are insufficient to justify the resulting compliance costs.

2012

On September 17, 2012, Treasury published proposed regulations ("2012 Proposed Regulations"). The 2012 Proposed Regulations address most of the tax community's concerns about C230.

8 Stephen Joyce "Little Progress Made in Considering Written Advice Standards Changes, Practitioners Say," *BNA Daily Tax Report*, No. 181. G-6 (Sept. 19, 2006). In that article, Cono Namorato, then-director of the Office of Professional Responsibility, was quoted as follows: "[C]omponents of Section 10.354 are 'too broad and sweep in unintended and uncontroversial tax advice. My advice is let's be patient while we consider [practitioner] concerns. In the interim, let's all use common sense in interpreting this rule.'"

9 WebCPA.com, *Former OPR Chief Aimed to Make it Visible, Effective*, Aug. 7, 2006, http://www.WebCPA.com. Based on Mr. Namorato's comments and his term of office (December 2003 to 2005), he would have come to this realization sometime in 2004.

III. 2012 proposed regulations

The 2012 Proposed Regulations[10] will, if adopted in final form, dramatically overhaul C230 by:

- Eliminating the complex rules in Section 10.35 that govern covered opinions;
- Expanding and clarifying the requirements in Section 10.37 for written tax advice;
- Withdrawing the proposed amendments to regulations governing state and local bond opinions in Section 10.39;[11]
- Broadening in Section 10.36 the scope of procedures to require a Tax Advisor with principal authority for overseeing a firm's federal tax practice to take reasonable steps to ensure the firm has adequate procedures in place for complying with C230;
- Clarifying in Section 10.35 that Tax Advisors must exercise competence when practicing before the IRS;
- Prohibiting a Tax Advisor from negotiating or endorsing a check issued to a taxpayer by any means (including electronic) (Section 10.31);
- Clarifying the expedited suspension procedures in Section 10.81; and
- Articulating the role of the Office of Professional Responsibility in Section 10.1.

Elimination of the Covered Opinion Rules in Section 10.35

Sections 10.35 and 10.37 contain rules about Written Advice. Section 10.35 currently provides specific rules for "Covered Opinions." Covered Opinions include Written Advice about any of the following: (1) a listed transaction, (2) a transaction with the principal purpose of tax avoidance or evasion, and (3) a transaction with a significant purpose of tax avoidance or evasion if the advice is a reliance opinion, marketed opinion, subject to conditions of confidentiality, or subject to a contractual protection.

The rules governing Covered Opinions are complex and highly technical. In addition, they result in higher costs to the consumers of tax services. As a result, many Tax Advisors try to circumvent the most onerous rules by including prominent disclaimers stating that the Written Advice cannot be relied upon for penalty protection.

The 2012 Proposed Regulations eliminate the Covered Opinion rules. Instead, all Written Advice will be subject

10 Proposed regulations are issued in advance of final regulations and are based on the IRS's position on a particular topic. Taxpayers generally may not rely on proposed regulations. Once proposed regulations are issued, the public is given the opportunity to comment on the proposed regulations as part of the "notice and comment" period before final regulations are issued. Formal comments were required to be submitted to Treasury by November 16, 2012. A public hearing was held on December 7, 2012.

11 This proposed change is beyond the scope of this Article.

to streamlined standards set forth in Section 10.37 of the 2012 Proposed Regulations.

New Requirements for Written Tax Advice in Proposed Section 10.37

All Written Advice will be subject to regulation under Section 10.37 of the 2012 Proposed Regulations. Specifically, proposed Section 10.37 sets forth the standards a Tax Advisor must adhere to when providing Written Advice by requiring that he/she:

- Base all written tax advice on reasonable factual and legal assumptions, including assumptions about future events;
- Reasonably consider all relevant facts that he/she knows or should know;
- Use reasonable efforts to identify and ascertain the facts relevant to the Written Advice on each federal tax matter;
- Not rely on representations, statements, findings, or agreements (including projections, forecasts, or appraisals) if reliance would be unreasonable; and
- Not take into account the possibility that a tax return will not be audited or that a matter will not be raised on audit.

Reliance on representations, statements, findings, or agreements is unreasonable if the Tax Advisor knows or should know that one or more representations (or assumptions on which a representation is based) are incorrect or incomplete. Further, a Tax Advisor may only rely on the advice of another Tax Advisor if the advice is reasonable and reliance is in good faith. Reliance is not reasonable when:

- The Tax Advisor knows or should know that the opinion of another Tax Advisor should not be relied on;
- The Tax Advisor knows or should know that the other Tax Advisor is not competent or lacks the necessary qualifications to provide the advice; or
- The Tax Advisor knows or should know that the other Tax Advisor has a conflict of interest.

Normally, under proposed Section 10.37(c)(1), the Service will apply a reasonableness standard in determining whether a Tax Advisor has complied with proposed Section 10.37, taking into account "all facts and circumstances, including, but not limited to, the scope of the engagement, the type and specificity of the advice sought by the client." Under proposed Section 10.37(c)(2), however, the Service will apply a heightened standard of review for Written Advice when the Tax Advisor knows or has reason to know that the Written Advice will be used to promote, market, or recommend a transaction and a significant purpose of the transaction is the avoidance or evasion of any tax imposed by the Code.

Proposed Section 10.37 does not require that Written Advice include particular elements, such as a description of the relevant facts, assumptions, or representations, analysis of how the law applies to the facts, or specific conclusions about material tax issues.

No More Circular 230 Disclaimers?

Most Tax Advisors currently include a C230 disclaimer in every email or other writing to avoid the application of current Section 10.35. The removal of current Section 10.35 will make C230 disclaimers a thing of the past, provided the 2012 Proposed Amendments are finalized as currently proposed.

Compliance Procedures

Proposed Section 10.36 pertains to Tax Advisors who have, or share, principal authority and responsibility for overseeing a firm's C230 practice. This includes the provision of federal tax advice, and the preparation of federal tax returns, claims for refund, and any other document submitted to the IRS. Proposed Section 10.36 requires the responsible person(s) to take reasonable steps to ensure the firm has adequate procedures for all members, associates, and employees to comply with C230. The responsible person(s) will be subject to discipline for failing to comply with proposed Section 10.36 if:

- The person through willfulness, recklessness, or gross incompetence does not take reasonable steps to ensure the firm has adequate procedures to comply with C230 and one or more persons associated with the firm are engaged in a pattern of practice non-compliant with C230; or
- The person knows, or should know, that one or more persons who are associated with the firm are engaged in a pattern of practice non-compliant with C230 and the person, through willfulness, recklessness, or gross incompetence, fails to take prompt action to correct the noncompliance.

General Standard of Competence

Proposed Section 10.35 requires that a Tax Advisor exercise competence when practicing before the IRS. Specifically, a Tax Advisor must possess the knowledge, skill, thoroughness, and preparation necessary for the matter for which he/she is engaged.

Electronic Negotiation of Taxpayer Refunds

Proposed Section 10.31 prohibits a Tax Advisor from endorsing or otherwise negotiating any check (including directing or accepting payment, by any means) issued to a client by the government as it relates to a federal tax liability. This proposed change is aimed at Tax Advisors who attempt to manipulate the electronic funds process to defraud their clients and the IRS.

Expedited Suspension Procedures

Current Section 10.82 authorizes immediate suspension of a Tax Advisor who has engaged in certain egregious conduct. Proposed Section 10.82 extends expedited discipline to Tax Advisors who "willfully failed to comply" with their own Federal tax filing obligations. Satisfaction of the "willfulness" standard can be demonstrated by failing to file a Federal return for four of five years, or failing to file a return required to be filed more frequently than annually during five of seven periods. Proposed Section 10.82 also clarifies the procedures surrounding expedited suspensions.

Office of Professional Responsibility

Proposed Section 10.1 clarifies that the Office of Professional Responsibility has exclusive responsibility for matters relating to discipline, including proceedings and sanctions.

IV. Conclusion

Long overdue, the 2012 Proposed Regulations will finally overhaul C230. Treasury should be commended for listening to the tax community's input and suggestions. The changes, if finalized, will remove much of the complexity, unnecessary confusion, and overreaching rules that Tax Advisors have been subject to under C230. Finally, the silly disclaimers we see in many written communications will disappear.

Credits Against the Oregon Corporate Minimum Tax Under *Con-Way, Inc. & Affiliates v. Department of Revenue*

By Thomas M. Karnes
Ater Wynne LLP

In December 2011, the Oregon Tax Court released its decision in *Con-Way, Inc. & Affiliates v. Department of Revenue*.[1] The dispute between Con-Way, Inc. ("Con-Way") and the Oregon Department of Revenue ("ODOR") stemmed from whether a taxpayer may use an Oregon Business Energy Tax Credit ("BETC") to offset amounts owed under Oregon's corporate excise minimum tax as set forth in Oregon Revised Statute ("ORS") 317.090. Although limited to the BETC, the issue of offsets against Oregon's corporate minimum tax extends to a variety of other statutory credits, including credits for biomass production, pollution control, and others.[2] Con-Way argued that the BETC is valid satisfaction of amounts owed under Oregon's corporate minimum tax. The ODOR, on the other hand, took the position that the corporate minimum tax can be satisfied only through cash payment. The Tax Court sided with Con-Way, concluding that the Oregon revenue statutes allow a taxpayer to satisfy with a BETC amounts owed in Oregon corporate minimum tax. The ODOR has since appealed Tax Court's decision to the Oregon Supreme Court.

This article first summarizes the factual and statutory background associated with the *Con-Way* decision. The following sections describe the principal arguments offered by Con-Way and the ODOR in their respective Oregon Tax Court pleadings. Finally, the remaining portions of this article outline the Oregon Tax Court's decision as to the appropriate interpretation of the Oregon corporate minimum tax relative to the BETC, as well as the ODOR's appeal to the Oregon Supreme Court and the ODOR's position pending a final Oregon Supreme Court decision.

Factual background on Con-Way and the ODOR.

In February 2008, the Oregon Department of Energy issued Con-Way a final certificate for a BETC that Con-Way acquired through the pass-through partner program. The final certificate was for $75,000.

For Con-Way's 2009 tax year, the company reported a $75,000 corporate minimum tax liability pursuant to ORS 317.090. Con-Way applied its BETC against its $75,000 reported Oregon tax liability in its 2009 corporate excise tax return. Con-Way had also made estimated Oregon corporate excise tax payments of $50,000 in 2009, which Con-Way claimed was an overpayment eligible for a refund. The ODOR disallowed Con-Way's application of the BETC against its Oregon obligation and declined Con-Way's overpayment claim. The ODOR further assessed Con-Way for a deficiency of $25,000, as well as related penalties and interest, in a Notice of Assessment for the 2009 tax year.

Con-Way appealed the Notice of Assessment to the Magistrate Division of the Oregon Tax Court in February 2011. In April 2011, Judge Breithaupt of the Oregon Tax Court designated the case for a hearing with the Regular Division of the Tax Court. Between July and August of 2011, both Con-Way and the ODOR filed motions for summary judgment.[3]

Statutory background involving the Oregon corporate minimum tax and BETC.

The *Con-Way* decision addresses primarily two statutes: the Oregon corporate minimum tax as set forth in ORS 317.090 (and as approved by referendum in Measure 67 in January 2010) and the BETC as set forth in ORS 315.354. ORS 317.090(2) provides that "Each corporation or affiliated group of corporations filing a return under ORS 317.710 shall pay annually to the state … a minimum tax …." ORS 317.090(3) further states that "The minimum tax … is payable in full …." With respect to the BETC, ORS 315.354(1) allows that "A credit is allowed

1 *Con-Way, Inc. & Affiliates v. Department of Revenue*, TC 5003 (December 27, 2011).

2 ORS 315.141 (biomass production), 315.304 (pollution control), 315.331 (energy conservation projects), 315.514 (file production), 315.521 (university venture development).

3 *Con-Way, Inc. & Affiliates v. Department of Revenue, supra,* Stipulation of Facts (June 6, 2011).

against the taxes otherwise due under ORS chapter 316 (or, if the taxpayer is a corporation, under ORS chapter 317 or 318) ….”

Con-Way’s position regarding Oregon’s corporate minimum tax and BETC.

Both Con-Way and the ODOR approached the *Con-Way* dispute as one of statutory interpretation and construction, focusing largely on how the Oregon legislature intended for taxpayers to satisfy amounts owed under the Oregon corporate minimum tax. Con-Way’s principal argument in its motion for summary judgment and related pleadings was that under a plain reading of ORS 315.354(1), which allows a “credit … against the taxes otherwise due under ORS chapter 316 (or, if the taxpayer is a corporation, under ORS chapter 317 or 318) …[,]” a corporate taxpayer like Con-Way will be allowed to use the BETC as a credit “against the taxes otherwise due” under ORS chapter 317.[4] In Con-Way’s view:

> Because ORS 315.354(1) does not contain an exception (or ‘carve-out’) for ORS 317.090, a taxpayer may use the BETC to satisfy its Oregon corporate excise liability, even if [that liability] is solely attributable to the ORS 317.090 calculation.[5]

Imposing a carve-out for the corporate minimum excise tax under ORS 317.090 would, according to Con-Way, amount to inserting language into the statute that does not otherwise exist.[6] That kind of constructive insertion of language omitted by the legislature would be contrary to the statutory interpretation rules in ORS 174.010, which directs courts in construing a statute “… not to insert what has been omitted ….”[7]

After outlining an argument based on the text of ORS 315.354 and 317.090, Con-Way engaged the context of those provisions. Specifically, Con-Way highlighted other portions of ORS 315.354 in which the Oregon legislature provided that certain credits were not eligible against taxes otherwise due under ORS 317.090.[8] As examples, Con-Way pointed to credits for computer or scientific equipment for research to educational organizations under ORS 317.151(a) and the corporate “kicker” credit under ORS 291.349(3), both of which expressly state that the credit “shall not be allowed against the tax imposed under ORS 317.090.”[9] To quote Con-Way’s motion for summary judgment:

> The legislature and the people of Oregon have demonstrated an ability to carve out a ‘minimum tax’ generally, or the ORS 317.090 tax liability specifically, when drafting the text of a credit provision.[10]

In light of that context, according to Con-Way, the legislature’s failure to include a carve out in ORS 315.354(1) for ORS 317.090 was intentional.[11]

Con-Way also urged the Tax Court to view the BETC as a tax expenditure intended to advance particular policy goals, and that limiting the ability of taxpayers, particularly taxpayers such as Con-Way who acquired a BETC through the pass-through partner program, would impede those goals.[12] Con-Way further argued that, according to federal court opinions and rulings, a purchaser of state tax credits is not “reducing” its state tax liability when it uses a credit, but rather “satisfying its state tax liability by liquidating a capital asset” (i.e., the tax credit).[13]

The ODOR’s position regarding Oregon’s corporate minimum tax and BETC.

As with Con-Way, the ODOR focused its arguments on interpreting the Oregon legislature’s intent with respect to taxpayers satisfying the corporate minimum tax. The ODOR’s principal argument in its motion for summary judgment and related pleadings was that the Oregon corporate excise minimum tax under ORS 317.090 is “just that—a ‘minimum’ that each corporate excise taxpayer must ‘pay’”.[14] In the ODOR’s view, allowing the BETC to reduce the minimum excise tax in ORS 317.090 would render “ORS 317.090 of no effect, since the ‘minimum’ tax under ORS 317.090 would be greater than the least amount that is ‘payable in full’ if the BETC is allowed as a credit against the amount under ORS 317.090.”[15]

As to occasional instances in ORS chapter 317 in which the legislature expressly addresses and prohibits taxpayers from using a credit to offset amounts owed under the Oregon minimum tax, the ODOR encouraged ‘the Tax Court to view those references as the legislature’s way of saying, “‘And we really mean it[,]’” thereby emphasizing the “general understanding that credits may not be taken against minimum tax.”[16]

The ODOR also asked the Tax Court to afford due weight to the ODOR’s historical practice as to the Oregon corporate minimum tax. Specifically, ODOR emphasized that the department’s Forms 20, on which taxpayers report corporate excise taxes, had for decades required payment

4 Pl.’s Mot. for Summ. J. and Resp. to Mot. to Dismiss 4 (July 5, 2011).

5 *Id.*

6 *Id.*, at 4-5.

7 ORS 174.010.

8 *Id.*, at 5.

9 *Id.*; Pl.’s Reply and Resp. to Def.’s Cross-Mot. for Summ. J. 1-4 (August 22, 2011).

10 Pl.’s Mot. for Summ. J. and Resp. to Mot. to Dismiss 5 (July 5, 2011).

11 *Id.*, at 6.

12 *Id.*, at 7.

13 *Id.*, at 8 (citing *Virginia Historic Tax Credit Fund 2001, LP v. Commissioner*, 107 AFTR2d (RIA), 2011 US App Lexis 6364 (4th Cir. 2011); *Tempel v. Commissioner*, 136 T.C. 15 (2011); PLR 200951024 (Sept. 10, 2009); CCA 200445046 (Oct. 29, 2004); PLR 200348002 (Aug. 28, 2003); Pl.’s Reply and Resp. to Def.’s Cross-Mot. for Summ. J. 6-8 (August 22, 2011).

14 Def.’s Cross-Mot. for Summ. J. 1 (August 2, 2011).

15 *Id.*, at 3.

16 *Id.*, at 12.

of a net excise tax after credits that is not less than the minimum tax.[17]

The Oregon Tax Court's decision in favor of Con-Way.

The Tax Court viewed its task as principally one of statutory construction. In the Tax Court's view, Con-Way and the ODOR disagreed as to:

> whether the minimum tax provided for under ORS 317.090 is a minimum obligation that may be satisfied through application of a credit or whether ORS 317.090 dictates that the taxpayer with an obligation arising under ORS 317.090 must make a cash payment to the state in the amount calculated under the statute of a given year.[18]

Quoting ORS 317.090 in relevant part:

> Each corporation or affiliated group of corporations filing a return under ORS 317.710 shall pay annually to the state, for the privilege of carrying on or doing business by it within this state, a minimum tax.[19]

The BETC is found in ORS 315.354(1), which provides a tax credit "against taxes otherwise due under … ORS chapter 317.[20] As articulated by the Tax Court, "The tax due under ORS 317.090 is obviously a tax due under ORS chapter 317."[21]

The Tax Court described the ODOR's position as asserting that the pertinent statutory "language requires a cash payment each year in the amount of any liability calculated under ORS 317.090."[22] Con-Way, according to the Tax Court, acknowledged "that they have a liability under the statute for a minimum tax, but argue[d] that they may satisfy that minimum tax liability by application of their BETC."[23]

According to the Tax Court, "…the [ODOR] asks the court to add words to the statute so that it reads that there is an obligation to pay 'in cash and without regard to any tax credit otherwise available to the taxpayer.'"[24] The Tax Court continued:

> Not only does the statute not contain those words, the context of the revenue laws as a whole indicates that when the legislature desires to prevent a tax credit from being used to satisfy a minimum tax obligation, it knows how to say so and has, in fact said so.[25]

The Tax Court then pointed to other credit provisions in the Oregon revenue statutes in which the legislature stated that "no credit shall be allowed against tax liability imposed by ORS 317.090[,]" including the "kicker" credit for corporations.[26]

The Tax Court also addressed the ODOR's position that ORS 317.090 requires that the minimum tax is "payable in full." The Tax Court viewed the obligation to pay the minimum tax as "no different from the obligation under ORS 317.070 to pay to the state the 'regular' tax."[27] Oregon statutes allow taxpayers to apply credits against the regular tax, and the legislature did not indicate that it intended any different meaning for the minimum tax in ORS 317.090. Looking to the sentence in ORS 317.090 in its entirety, the Tax Court also interpreted the "payable in full" phrase in ORS 317.090 as the legislature's intent to prevent a taxpayer from "prorating its liability in the event it is subject to tax for only a portion of the year[,]" not to prevent taxpayers from using the BETC to satisfy amounts owed under the corporate minimum tax.[28]

Finally, the Tax Court addressed the ODOR's request for deference to the department's "long standing interpretation ..., reflected in its forms, that credits are not applicable to the minimum tax."[29] Notably, the Tax Court concluded that the ODOR's historical position "cannot displace the intent of the legislature."[30]

The ODOR's appeal to the Oregon Supreme Court and position pending appeal.

The DOR appealed the Tax Court's decision to the Oregon Supreme Court in February 2012.[31] The Oregon Supreme Court has yet to calendar a hearing on the appeal. Pending final resolution of that appeal, that ODOR has indicated that it will maintain its position that, in the ODOR's words, "taxpayers cannot use tax credits to reduce the corporate minimum tax."[32] Notwithstanding that posture, the ODOR has stated that taxpayers "may file protective claims with the [ODOR] to secure the right to a refund pending the [Oregon] Supreme Court proceedings."[33] The ODOR will defer action on those refund claims until the Oregon Supreme Court renders a final decision.

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17 *Id.*, at 18.

18 *Con-Way, Inc. & Affiliates v. Department of Revenue, supra*, at 3 (December 27, 2011).

19 *Id.,* at 4.

20 *Id.*

21 *Id.*

22 *Id.*

23 *Id.*

24 *Id.*, at 4-5.

25 *Id.,* at 4.

26 *Id.,* at 5.

27 *Id.*

28 *Id.,* ("The minimum tax shall not be apportion able ... but shall be payable in full for any part of the year during which a corporation is subject to tax.").

29 *Id.*

30 *Id.,* at 6.

31 Oregon Supreme Court S060141 (February 16, 2012).

32 Oregon Department of Revenue, Corporate Taxes, available at: http://www.oregon.gov/DOR/BUS/Pages/corp-tax_main.aspx.

33 *Id.*

Upcoming Events

Feb 04, 2013
New Tax Lawyer Committee: New Tax Lawyer Meeting
Hosted by Jennifer Woodhouse, Schwabe Williamson & Wyatt PC

Feb 06, 2013
New Tax Lawyer Committee: New Tax Lawyer Social
5:30 - 6:30 p.m. at The Original

Feb 19, 2013
New Tax Lawyer Committee: Mentor Program Kick-Off Event
Hosted by Dan Eller, Schwabe Williamson & Wyatt PC

Feb 19, 2013
Mid-Valley Tax Forum Luncheon Series: Lessons Learned: Recent Cases and Rulings in Federal Tax Law
Presenter: Gwendolyn Griffith, Tonkon Torp LLP

Feb 21, 2013
Portland Luncheon Series: The Nuts and Bolts of the Federal Audit Controversy Process
Presenter: Jeffrey M. Wong, Attorney

Mar 04, 2013
New Tax Lawyer Committee: New Tax Lawyer Meeting
Hosted by Jeremy Babener, Lane Powell PC

Mar 06, 2013
New Tax Lawyer Committee: New Tax Lawyer Social
5:30 - 6:30 p.m. at Southpark

Mar 14, 2013
Portland Luncheon Series: A Dash of SALT: Planning Opportunities and Recent Developments
Presenters: Michael Millender and Mark LeRoux, Tonkon Torp LLP

Mar 19, 2013
Mid-Valley Tax Forum Luncheon Series: Oregon Estate Tax
Presenter: Clint Bentz, Boldt, Carlisle & Smith, LLC

Apr 01, 2013
New Tax Lawyer Committee: New Tax Lawyer Meeting
Hosted by TBD

Apr 18, 2013
Portland Luncheon Series: Helping Start-Ups Navigate Sections 83 and 409A
Presenter: Ryan R. Nisle, Miller Nash LLP

May 06, 2013
New Tax Lawyer Committee: New Tax Lawyer Meeting
Hosted by TBD

May 16, 2013
Portland Luncheon Series: Recent Developments in the World of S Corporations
Presenter: Larry J. Brant, Garvey Schubert Barer

May 21, 2013
Mid-Valley Tax Forum Luncheon Series: Helping Start-Ups Navigate Sections 83 and 409 A
Presenter: Ryan Nisle, Miller Nash, LLP

Jun 03, 2013
New Tax Lawyer Committee: New Tax Lawyer Meeting
Hosted by TBD

Jun 06, 2013
Oregon Tax Institute: Oregon Tax Institute
Multnomah Athletic Club

Jun 07, 2013
Oregon Tax Institute: Oregon Tax Institute
Multnomah Athletic Club

Jun 20, 2013
Portland Luncheon Series: What to Know About Exempt Organizations
Presenter: Cynthia Cumfer, Attorney