OREGON DEPARTMENT OF REVENUE

2020

Executive summary

GILTI Report

December 1, 2020

150-800-550 (Rev. 12-01-20) GILTI Report

Executive summary

Senate Bill (SB) 1529, Section 37 (2018), requires the Department of Revenue to submit a report by December 1, 2020 that compares the relative efficacy of Oregon Revised Statute (ORS) 317.716 (listed jurisdiction addition) and Internal Revenue Code (IRC) 951A (global intangible low-taxed income, or GILTI). The department understands the report seeks to answer three questions:

1. What income is taxed by GILTI versus the listed jurisdiction law?
2. Are countries identified by the listed jurisdiction law equally affected by the GILTI law?
3. What is the relative tax effect of GILTI versus the listed jurisdiction law?

The department has encountered challenges regarding tax return information for tax year 2018 being available from taxpayers before the due date of this report. Because most corporate tax filers with a GILTI reporting obligation file their tax returns using a fiscal tax year, the first complete year of GILTI data became available shortly before the due date of this report. At least two full years of data with sufficient time to analyze and verify tax return data is needed to compare the tax effect of the two policies fully. Accordingly, the department believes a report that provides such a comparison envisaged in Question 3 is not currently achievable.

The department has previously raised concerns about the report due date and lack of available tax return data at the time the report is due to the legislative committees related to revenue. As a result, SB 1531, Section 27 (2020), would have moved the report due date to January 2, 2023 to allow the department time to gather enough tax return data to produce a thorough report. However, SB 1531 was waiting for a final floor vote in the second chamber upon adjournment, so SB 1531 appears to have had bipartisan support.

The department understands a key requirement is to report on whether GILTI requires the inclusion of the same income in Oregon taxable income as the listed jurisdiction law. One implied aspect of this reporting requirement is to determine the amount of tax paid on account of GILTI in tax year 2018 (the first tax year GILTI applied to taxpayers) and to compare the amount of GILTI-related tax to that which would have been paid had the listed jurisdiction law remained in effect for tax year 2018. In response to the requirements of SB 1529, Section 37, and in consideration of the tax return data challenges, the department respectfully submits this report, which can be obtained by contacting the Department of Revenue agency government relations manager or on the department's legislative reports webpage.

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Introduction

Senate Bill 1529, Section 37 (2018), requires the Department of Revenue to submit a report by December 1, 2020 that compares the relative efficacy of ORS 317.716 (listed jurisdiction addback) and IRC 951A (global intangible low-taxed income, or GILTI). The department understands the report seeks to answer three questions:

1. What income is taxed by GILTI versus the listed jurisdiction law?
2. Are countries identified by the listed jurisdiction law equally affected by the GILTI law?"
3. What is the relative tax effect of GILTI versus the listed jurisdiction law?

Regarding the third question, the department has encountered challenges regarding available tax return data for tax year 2018 because of fiscal-year filers. Due to those challenges, and as explained below, the department believes a report that provides such a comparison is not currently achievable.

Please note that the ORS 317.716 listed jurisdiction law only applied to corporate excise taxpayers. Accordingly, this report focuses solely on corporate excise taxpayers. Some personal income taxpayers may be required to include GILTI in their federal taxable income, which will flow through to Oregon taxable income. However, the experience of personal income taxpayers with GILTI is irrelevant to this report because the report compares the efficacy of the listed jurisdiction law with GILTI.

Differences between GILTI and listed jurisdiction law

It's useful to begin by comparing GILTI with the listed jurisdiction law to shed light on the goals and mechanics of each law.

A listed jurisdiction was defined as a jurisdiction that imposed no, or minimal, taxes and exhibited characteristics that facilitated tax avoidance.[1] This repealed Oregon law (ORS 317.717) notes one common characteristic that facilitates tax avoidance: allowing a taxpayer to make use of the listed jurisdiction without a local substantive presence. Generally, a tax rate of between 0 percent and 5 percent represented a minimal tax rate when the department reviewed jurisdictions for possible inclusion as a listed jurisdiction.[2] The department was charged with recommending inclusion or removal from the group of listed jurisdictions in a biennial report due in advance of each odd-year legislative session.

The listed jurisdiction law required an Oregon filer to include the net income or loss of a unitary affiliate corporation in the Oregon filer's Oregon taxable income, if the unitary affiliate corporation was incorporated in a listed jurisdiction. In other words, the listed jurisdiction law represented an Oregon addition to federal taxable income for income taxed at a lower rate in a foreign jurisdiction. The Oregon filer was generally allowed sales factor representation for the business activity of the listed jurisdiction corporation. This meant that the sales of the listed jurisdiction corporation were included in the denominator of the Oregon sales factor. This had the effect of reducing the amount of the listed jurisdiction's net income that was apportioned to Oregon. However, this outcome aligned with the general policy of granting sales factor representation to the business income of a unitary affiliate.

GILTI, on the other hand, is a federal law that requires a U.S. shareholder[3] to include the tested net income of a controlled foreign corporation (CFC) to the extent the tested net income of the CFC exceeds a 10 percent rate of return, on the basis of the CFC's tangible business assets used to produce income in the federal taxable income of the U.S. shareholder. Whether Oregon statutory law allows sales factor representation for a GILTI inclusion depends on various factors and circumstances, as provided in Oregon statutory apportionment provisions.[4] In general, U.S. shareholders receive sales factor representation for sales in the ordinary course of a shareholder's trade or business.

GILTI is not limited by geography because a CFC giving rise to a GILTI inclusion can be located anywhere outside the United States. In fact, GILTI applies to all jurisdictions, including those in the identified listed jurisdictions. In short, a GILTI inclusion is required whenever the CFC realizes net income exceeding a 10 percent rate of return

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[1] ORS 317.717 (2015).

[2] ORS 317.716(1)(b) (2015).

[3] Tested net income refers to a special computation of net income calculated for purposes of determining the IRC 951A GILTI inclusion.

[4] ORS 314.605 to ORS 314.675.

on the qualified business assets of the CFC. However, a GILTI inclusion is not required if the CFC is taxed by a foreign jurisdiction at a rate exceeding 18.9 percent. (90 percent of the U.S. corporate tax rate of 21 percent.)[5]

Both GILTI and the listed jurisdiction law are aimed at addressing tax avoidance. Currently, all income formerly subject to the listed jurisdiction law, minus a 10 percent rate of return on the tangible business assets of the listed jurisdiction corporation, is also subject to GILTI. Because listed jurisdictions typically don't require a substantive presence in the jurisdiction, it's relatively unlikely that a corporation incorporated in a listed jurisdiction will have substantial tangible business assets. It follows that this threshold is relatively unlikely to occur with respect to income that would have been reported under the listed jurisdiction law, although without tax return data this is just an assumption. In addition, GILTI applies to all foreign jurisdictions.

On early analysis, it appears that GILTI would generally be easier for the department to administer than the listed jurisdiction law. All other things being equal, a law that is easier to administer and enforce is more likely to accomplish the goals of the law in question. First, the department wouldn't need to identify foreign tax avoidance in order to identify listed jurisdictions, nor would it need to prepare a biennial report for the Legislature. Second, GILTI is included as a component of federal taxable income, so the department will benefit from the IRS auditing activities for the GILTI inclusion.

Discussion

It appears that the goal of the GILTI law is to cause U.S. taxpayers to change behavior by locating more operations in the United States. Some evidence suggests that GILTI has not changed taxpayer behavior to date. Namely, some data indicates that taxpayers record just as many profits in foreign subsidiaries as they have in the past. However, the source of this data indicates that GILTI represented a big change to the U.S. tax code, and it takes time for behavior to change as taxpayers learn and understand incentives set forth in new laws and react accordingly.[6]

With regard to corporate excise taxpayers, a report providing a quantitative comparison of the listed jurisdiction addback and GILTI can't be compiled at this time for the following reasons:

- GILTI is reported beginning with tax year 2018 returns. All timely filed 2018 tax year returns will not be received until October 15, 2020 because most corporate taxpayers with a GILTI reporting obligation file on a fiscal year. Tax year 2018 may end as late as November 30, 2019 for many taxpayers. Most corporate taxpayers file their tax return on extension, due to the complexity of corporate taxation. As a result, the last of the 2018 tax year returns were filed on October 15, 2020 after a six-month extension to file a tax return.

  Tax year 2019 information will not be completely received until October 15, 2021. Two consequences result from this situation. First, the department doesn't have enough time to analyze 2018 return information between October 15, 2020 (the due date of the returns) and December 1, 2020 (the due date of the report). Second, only one year of complete tax information will be available as of December 1, 2020, and this would only include timely filed returns.

  One year of tax return data is not a good sample from which to draw conclusions, especially if that year is the first year of a new law. When a new law passes, there are typically errors in filing due to misunderstanding of the new law. Given the relative complexity of GILTI, the department expects the trend of filing errors to hold true in this instance as well.

- Review of the returns received to date indicates that many taxpayers who file their Oregon tax return on paper have not also enclosed Form 5471. Form 5471 is needed to calculate the amount that the listed jurisdiction addition would have been in tax year 2018. To compile a sufficient tax return data set, the department must request Form 5471 from taxpayers. This information gathering will require cooperation from taxpayers in providing the necessary information during the COVID-19 pandemic. As a result of the COVID-19 pandemic, more taxpayers than usual have opted to request extensions to produce records.

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[5] Guidance Under Sections 951A and 954 Regarding Income Subject to a High Rate of Foreign Tax, Internal Revenue Service. July 23, 2020. https://www.federalregister.gov/documents/2020/07/23/2020-15351/guidance-under-sections-951a-and-954-regarding-income-subject-to-a-high-rate-of-foreign-tax

[6] Economic Analysis: New Data Show So Far, No Post-TCJA Profit Shifting to US. Tax Notes. August 25, 2020 located at https://www.taxnotes.com/beps-expert/base-erosion-and-profit-shifting-beps/economic-analysis-new-data-show-so-far-no-post-tcja-profit-shifting-us/2020/08/25/2cwbd

- Many taxpayers with GILTI in tax year 2018, who have filed to date, reported their GILTI using uncategorized or erroneous codes. This creates a risk that taxpayers who use uncategorized codes won't be identified. On the other hand, taxpayers who mistakenly use a GILTI code to report non-GILTI income will result in a "false positive." To compile an accurate tax return data set, the department will have to identify taxpayers with GILTI manually.
- Review of the returns received to date indicates that sales factor information related to GILTI will need to be reviewed. Some taxpayers may be giving sales factor representation to GILTI while other taxpayers may not. This is important because correct sales factor representation has a direct correlation with how much tax is owed to Oregon.

The department has previously mentioned concerns about the report due date and the lack of available tax return data when the report is due to the committees on revenue. SB 1531, Section 27 (2020), would have moved the due date for this report to January 2, 2023 to allow the department time to gather enough tax return data from taxpayers to produce a thorough report. However, the bill did not pass before the Legislature adjourned.

Summary

For the department to adequately compare the relative efficacy of the listed jurisdiction law and GILTI, the department would need time to review tax year 2018 and 2019 returns. In any case, taxpayer cooperation will be an indispensable condition to preparing an adequate GILTI report. More than one tax year of information will lend a firmer factual foundation for policy making by the Oregon Legislature. In response to the requirements of SB 1529, Section 37, and in consideration of the tax return data challenges, the department respectfully submits this report, which can be obtained by contacting the Department of Revenue agency government relations manager or on the department's legislative reports webpage.