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ARCHIVES DIVISION
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NOTICE OF PROPOSED RULEMAKING
INCLUDING STATEMENT OF NEED & FISCAL IMPACT

CHAPTER 150
DEPARTMENT OF REVENUE

FILED
04/27/2021 5:02 PM
ARCHIVES DIVISION
SECRETARY OF STATE

FILING CAPTION: Repeal Subtraction for Qualified Investment of Severance Pay Rule; Amend Withholding Penalty and Statements Rule.

LAST DAY AND TIME TO OFFER COMMENT TO AGENCY: 05/25/2021 5:00 PM

The Agency requests public comment on whether other options should be considered for achieving the rule's substantive goals while reducing negative economic impact of the rule on business.

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Filed By:
Katie Thiel
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HEARING(S)

Auxiliary aids for persons with disabilities are available upon advance request. Notify the contact listed above.

DATE: 05/25/2021

TIME: 9:00 AM

OFFICER: Robert Oakes

ADDRESS: Remote Hearing -

Video/Conference Call

955 Center Street NE

Salem, OR 97301

NEED FOR THE RULE(S):

150-316-0640 The rule is being repealed because the subtraction for qualified investment of severance pay has sunset.

150-316-0284 Amends rule to reference "withholding statement" and "exemption certificate" per changes in statute from HB 2119 (2019). Adds definition for "reasonable basis" as referred to in ORS 316.177. Adds definition for "frivolous position." Clarifies when penalty is applied and there is no reasonable basis for an incorrect withholding statement or exemption certificate. Removes "first time" from rule to apply penalty when employees continue to use a frivolous position to avoid withholding.

150-316-0290 Amends rule to delete the term "withholding exemption certificate" and instead reference "withholding statement" and "exemption certificate" per changes in statute from HB 2119 (2019). Removes reference of "exemption" and "allowances" to provide for future changes to OR-W-4 and potentially moving away from allowances in the withholding rate calculation. Ties the definition of "reasonable basis" to the definition in OAR 150-316-0284. Defines

“materially deficient” withholding for purposes of this rule and OAR 150-316-0284. Eliminates the need for employers to send copies of form OR-W-4. Allows the department to adjust withholding without first receiving copies of W-4s from employers when it has determined a taxpayer’s withholding rate is “materially deficient.” Clarifies that individuals must have a personal or financial change affecting their tax situation for the department to consider a withholding redetermination and instructs taxpayers how to request a redetermination. Instructs employers how to handle OR-W-4 submissions by the employee after DOR has sent a withholding determination to the employer and employee.

DOCUMENTS RELIED UPON, AND WHERE THEY ARE AVAILABLE:

Oregon Revised Statutes: 316.177, 316.182, 316.856, available online at the Legislature’s website
https://www.oregonlegislature.gov/bills_laws/Pages/ORS.aspx
House Bill 2119 (2019) <http://olis.leg.state.or.us/liz/2019R1/Downloads/MeasureDocument/HB2119>

FISCAL AND ECONOMIC IMPACT:

There is no fiscal or economic impact due to this rule change.

COST OF COMPLIANCE:

(1) Identify any state agencies, units of local government, and members of the public likely to be economically affected by the rule(s). (2) Effect on Small Businesses: (a) Estimate the number and type of small businesses subject to the rule(s); (b) Describe the expected reporting, recordkeeping and administrative activities and cost required to comply with the rule(s); (c) Estimate the cost of professional services, equipment supplies, labor and increased administration required to comply with the rule(s).

(1) The repeal of OAR 150-316-0640 will have no impact to state agencies or on the counties and the public. The amendment of OAR 150-316-0284 and 150-316-0290 will decrease the administrative burden on employers and provide additional instruction to employees.

(2)(a) Oregon has approximately 123,000 small businesses with fewer than 250 employees that employ 81% of the state's workforce. Oregon has approximately 105,646 small businesses with fewer than 100 employees. Based on this information and information from tax returns reporting number of employees, we estimate Oregon has approximately 91,848 small businesses with fewer than 50 employees that would be subject to the rules. The repeal of OAR 150-316-0640 will have no cost of compliance effect on these small businesses. The amendment of OAR 150-316-0284 will have no cost of compliance on small businesses because the penalty applies to the employee. The amendment of OAR 150-316-0290 will decrease the cost of compliance on small businesses with employees because it removes the requirement to submit copies of withholding statements and exemption certificates to the department.

(2)(b) 150-316-0640 Repealing this rule has no impact to projected reporting, recordkeeping or other administrative activities or costs.

150-316-0284 The rule amendment will have no reporting or recordkeeping impact on any business.

150-316-0290 The rule amendment will decrease the reporting requirements for businesses with employees.

(2)(c) No known or foreseen need for increase in equipment, supplies, labor, and administration.

DESCRIBE HOW SMALL BUSINESSES WERE INVOLVED IN THE DEVELOPMENT OF THESE RULE(S):

150-316-0640 - The department did not seek specific stakeholder feedback for repealing OAR 150-316-0640. This rule is being repealed as the subtraction for qualified investment of severance pay had a sunset of 1/1/2014 per ORS

316.856.

150-316-0284 - The department solicited feedback from the Oregon State Bar Tax Section, Oregon Bankers Association, Oregon Association of Tax Consultants, Oregon Board of Tax Practitioners, and the Oregon Collectors Association, most of which have small businesses as clients. The Oregon Banker's Association provided feedback that they have no concerns with the proposed amendments. No other external stakeholder feedback was received.

150-316-0290 - The department solicited feedback from the Oregon State Bar Tax Section, Oregon Bankers Association, Oregon Association of Tax Consultants, Oregon Board of Tax Practitioners, and the Oregon Collectors Association, most of which have small businesses as clients. Response was received from the Oregon Banker's Association with concern that a requirement to submit a rejected withholding statement or exemption certificate to the department would unduly burden employers. The department responded by removing the rule requirement to submit the rejected statement or certificate. In addition, the amended rule provides employers with the option to accept a new withholding form or withhold at a flat 8 percent. No other external feedback was received.

WAS AN ADMINISTRATIVE RULE ADVISORY COMMITTEE CONSULTED? NO IF NOT, WHY NOT?

The Department of Revenue did not use a formal advisory committee for these rules; however, we did seek and receive input from groups of industry representatives. No administrative rule advisory committee was consulted because the above groups were contacted, and they have the interest and expertise necessary to provide adequate feedback on the proposed rules; therefore, a committee is unlikely to provide further benefit.

RULES PROPOSED:

150-316-0284, 150-316-0290, 150-316-0640

AMEND: 150-316-0284

RULE SUMMARY: Amends rule to reference "withholding statement" and "exemption certificate" per changes in statute from HB 2119 (2019). Adds definition for "reasonable basis" as referred to in ORS 316.177. Adds definition for "frivolous position". Clarifies when penalty is applied and there is no reasonable basis for an incorrect withholding statement or exemption certificate. Removes "first time" from rule to apply penalty when employees continue to use a frivolous position to elude withholding.

CHANGES TO RULE:

150-316-0284

Penalty ¶

~~(1) A penalty is assessable against an employee who files an erroneous withholding statement claiming:¶~~

~~(a) More than 10 withholding exemptions for federal or state income tax withholding; or~~
~~Definitions for the purposes of ORS 316.177 and this rule:¶~~

~~(a) "Frivolous position" includes, but is not limited to:¶~~

~~(bA) Exemption from withholding and the employee's income is expected to exceed \$200 per week for both federal and state purposes; or~~
~~Reference to a spurious constitutional argument:¶~~

~~(B) Reliance on a "gold standard" or "war tax" deduction:¶~~

~~(cC) Exemption from withholding for state purposes but not for federal purposes; and~~
~~An argument that wages or salaries are not includable in taxable income:¶~~

~~(dD) As of the time an argument that the staSixtment was made there was no reasonable basis for the statement. h~~
~~Amendment to the United States Constitution was not properly adopted; or¶~~

~~(2E) The penalty shall not be assessed against employes who have a reasonable basis for the erroneous statement.~~

An argument that "unenfranchised, sovereign, free men or natural persons" are not subject to the tax laws.¶

(b) "Reasonable basis" includes, but is not limited to the following situations:¶

(a) An employee in good faith files an erroneous W-4 for the first time.¶

(A) An employee filed a withholding statement or exemption certificate for the first time, and attempted, but failed, to correctly calculate the withholding rate in accordance with the instructions on the withholding statement or exemption certificate;¶

(b) The employee computed the number of withholding allowances rate in accordance with the instructions on the Form W-4, but due to unforeseen events, the number of allowances claimed is incorrect;¶

(c) The erroneous W-4 was filed with withholding statement or exemption certificate, but due to unforeseen events, the withholding rate claimed is incorrect. Unforeseen events are events that could not have reasonably been anticipated and affect the taxpayer's taxable income or deductions for the tax year;¶

(C) An employee filed a withholding statement or exemption certificate because the employee relied upon the advice of an individual who is qualified to practice law or public accounting in this state or an individual who is licensed by the State Board of Tax Practitioners and the employee supplied the individual with complete information connected with the advice given.¶

(32) The penalty shall be assessed against an employee filing an erroneous W-4 for the first time in reliance on a frivolous position when:¶

(a) The employee claims exemption or from with the apparent intent to delay or impede the administration of the income tax laws of this state (or holding and the employee does not meet the exemption requirements provided in OAR 150-316-0237 and the federal government).¶

(4) As used in this section, a "frivolous position" includes, but is not limited to: department has determined there is no reasonable basis for such a claim; or¶

(a) Reference to a spurious constitutional argument;¶

(b) Reliance on a "gold standard" or "war tax" deduction;¶

(c) An argument that wages or salaries are not includable in taxable income;¶

(d) An argument that the Sixteenth Amendment to the United States Constitution was not properly adopted; or The department has determined the employee's withholding is materially deficient, as defined in OAR 150-316-0290, and the withholding rate is corrected by notice to the employer and employee under OAR 150-316-0290.¶

(3) A penalty shall not be assessed against an employee who, at the time the withholding statement or exemption certificate is filed, has a reasonable basis for the withholding statement or exemption certificate. ¶

(e) An argument that "unenfranchised, sovereign, free men or natural persons" are not subject to the tax laws exemption certificate in reliance on a frivolous position or with the apparent intent to delay or impede the administration of the income tax laws of this state.

Statutory/Other Authority: ORS 305.100

Statutes/Other Implemented: ORS 316.177

AMEND: 150-316-0290

RULE SUMMARY: Amends rule to delete the term "withholding exemption certificate" and reference "withholding statement" and "exemption certificate" per changes in statute from HB 2119 (2019). Removes "exemption" reference or "allowances" to provide for future changes to OR-W-4 and potentially moving away from allowances in the calculation of withholding rates. Refers the definition of "reasonable basis" to OAR 150-316-0284. Defines "materially deficient" withholding in reference to this rule and in OAR 150-316-0284. Eliminates the need for employers to send us copies of form OR-W-4 as previously required. Allows the department to adjust withholding without first receiving copies of W-4s from employers when we have determined a taxpayer's withholding rate is "materially deficient." Clarifies that an individual must have a personal or financial change affecting their tax situation for the department to consider a withholding redetermination and instructs how to request a redetermination. Instructs employers how to handle OR-W-4 submissions by the employee after DOR has sent a withholding determination to the employer and employee.

CHANGES TO RULE:

150-316-0290

Procedure for Correcting the Filing of Withholding Certificates ¶

~~(1) Except as provided by paragraph (2) an employer shall not use a withholding exemption certificate for state income tax withholding purposes if:~~ For the purposes of this rule, "materially deficient" withholding includes, but is not limited to:¶

~~(a) When the employee has filed an exemption certificate with the employer and the department determines the employee does not meet the exemption requirements given in OAR 150-316-0237;¶~~

~~(ab) The certificate claims an exempt status for state~~ When the employee has filed a withholding statement with the employer and the department has determined the employee incorrectly calculated their withholding purposes but not federal purposes; or¶

~~(b) The certificate is rate with no reasonable basis for the calculation, or has claimed a frivolous position, as defined with the employer for use in determining both state and federal in OAR 150-316-0284.¶~~

~~(c) When the employee has not filed an Oregon personal income tax return and the department has assessed tax owing, after withholding, and the Internal Revenue Service estimated payments are credited, in two of the past three filing tax years under ORS 305.265(10);¶~~

~~(d) When the employee has notified the employer that the certificate is materially defective an Oregon personal income tax return for the past three filing tax years and owed more than \$1,000 in net tax to pay, after withholding and estimated payments are credited, for each of those tax years.¶~~

(2) An employer may use a ~~withholding~~ exemption certificate that claims an exempt status for state purposes when the employee's compensation is exempt from Oregon tax under a provision of federal or state law. Examples meets the exemption requirements provided in OAR 150-316-0237. ¶

(3) An employer shall not use a withholding statement of ~~r~~ exempt compensation include those described in certificate for state income tax withholding purposes in:¶

(a) Public Law 101-322, the Amtrak Reauthorization and Improvement Act of 1990, relating to certain rail carrier and motor carrier employees (Title 49 USC 11502 and Title 49 USC 14503, respectively);¶

(b) ORS 316.127(8), relating to federal employees of hydroelectric facilities on the Columbia River;¶

(c) Public Law 96-193, the Aviation Safety and Noise Abatement Act of 1979, relating to certain aircraft The certificate claims an exempt status for state withholding purposes and the employer determines the employee does not meet the exemption requirements provided in OAR 150-316-0237; or¶

(b) The withholding statement or exemption certificate is filed with the employer for use in determining state withholding, and the Department of Revenue has instructed the employer to change the employee's (Title 49 USC 40116);¶

(d) ORS 316.777 (relating to earnings of enrolled tribal members) withholding statement or exemption certificate under section (5) of this rule.¶

~~(34)~~ If subsection ~~(43)~~ of this rule applies; ¶

~~(a) the employer shall withhold as if the employee was single claiming zero exemptions, until such time as the employee files a new certificate. The employer shall give prompt notice to the employee of the employer's action flat rate of eight percent of taxable wages until such time as the employee files a new withholding statement. The employer shall give prompt notice to the employee that an exemption certificate claiming an exempt status for state purposes only is not acceptable because there is no applicable provision under state or federal law for such exempt status; or ¶~~

~~(4b) The employer shall submit to the department a copy of any withholding certificates which are: ¶~~

~~(a) Certificates which claim more than 10 withholding exemptions for state purposes; or ¶~~

~~(b) Certificates which claim exemption from withholding and the employee's income is expected to exceed \$200 per week for both federal and state purposes; or ¶~~

~~(c) Certificates which claim exemption from withholding for state purposes but not federal purposes. The copy shall be submitted within 20 days of the employer's receipt of the certificate. ¶~~

~~(5) If, after receipt of a copy of the certificate, tIn the event the department has instructed the employer to change the employee's withholding statement or exemption certificate under section (5) of this rule, the employer shall withhold at the rate determined by the department. ¶~~

~~(5) The department may makes a written request to the employee for verification of the statements in the certificate, and after 20 days does not receive such verification, the department shall notify change in an employee's withholding statement or exemption certificate when it determines that the employer ine's writing of the lack of verification. If the department makes a determination to change the withholding certificate based on available information, thholding is materially deficient as defined in section (1) of this rule. The department shall notify the employer and employee in writing of the change. Upon receipt of the notice, the employer shall withhold according to the department's determination. ¶~~

~~(a) If the employee files a new certificate with the employer claiming more exemptions than the determination made by the department, or exemption from state withholding The employee may appeal the action of the department as provided in ORS 305.275. ¶~~

~~(a) If the employee seeks to have less withholding than allowed by the department or wants to submit an exemption certificate for state withholding purposes, the employee must provide satisfactory evidence of a personal or financial change affecting their tax situation. To report the change that affects their tax situation and to request that the department consider the new information, the employee shall also submit a copy of the newly filed new withholding statement or exemption certificate to the department requesting a redetermination. The certificate swithould have the word "Redetermination" written on the top of the newly filed certificateing statement or exemption certificate shall be accompanied by all information required by the department. The employer shall continue to withhold according to the department's most recent determination until the department authorizes a subsequent change in withholding or fully releases the withholding determination for the employee. ¶~~

~~(b) If the employee files a new certificate with the employer claiming fewer exemptiwithholding statement with the employer requesting more withholding for Oregon than the determination made by the department, the employer may withhold according to the newly filed certificate. Twithholding statement. Once a new withholding statement that increases Oregon withholding is accepted by the employee may appeal the action of the department as otherwise provided by lawr, the employer shall not honor subsequent withholding statements that seek to lower withholding below the department's determination unless the employee has followed the process given in section (5)(a) of this rule and the department has authorized the reduced withholding.~~

Statutory/Other Authority: ORS 305.100

Statutes/Other Implemented: ORS 316.182

REPEAL: 150-316-0640

RULE SUMMARY: The rule is being repealed as the subtraction has sunset.

CHANGES TO RULE:

~~150-316-0640~~

~~Subtraction for Qualified Investment of Severance Pay~~

~~(1) Definitions.~~

~~(a) "Invest" means to exchange cash for equity, debt, convertible debt, or management responsibilities, accompanied by terms that substantiate ownership or control of an interest in a business. "Invest" does not mean to make a loan to a business.~~

~~(b) "Material participation" means regular, continuous, and substantial participation in the small business. A taxpayer is considered to have materially participated in the small business if the taxpayer:~~

~~(A) Worked for the small business for more than 500 hours in each of the 12 month periods required under section 2(b) of this rule;~~

~~(B) Worked for the small business for more than 100 hours in each of the 12 month periods required under section 2(b) of this rule and at least as much as any other owner or employee; or~~

~~(C) Performed substantially all the work in the small business.~~

~~(c) "Severance pay" means compensation payable, other than back wages, vacation pay or sick pay, on voluntary termination or involuntary termination of employment based on length of service, a percentage of final salary, a contract between the employer and the employee, or some other reasonable method. "Severance pay" does not include retirement income as defined in ORS 316.127(9).~~

~~(d) "Small business" means a corporation, partnership, sole proprietorship or other legal entity formed for the purpose of making a profit, which is independently owned and operated from all other businesses and which has 50 or fewer employees.~~

~~(2) Qualifications. Severance pay that a taxpayer receives during the tax year and invests in a new or existing small business in Oregon may be subtracted from federal taxable income if:~~

~~(a) The investment occurs on or before the due date of the return, including extensions, for the first tax year in which the subtraction may be claimed;~~

~~(b) The investment continues for at least 24 consecutive calendar months following the termination of employment (for example - July 13, 2010 through July 12, 2012);~~

~~(c) The small business is not the employer that paid the severance pay and does not have any owner in common with the employer that paid the severance pay;~~

~~(d) No subtraction has previously been claimed under this section;~~

~~(e) The taxpayer completes a form provided by the department that is attached to the return of the taxpayer or is otherwise maintained or filed pursuant to form instructions; and~~

~~(f) The taxpayer materially participates in the small business for the period required under subsection (b) of this section.~~

~~(3) The taxpayer must demonstrate to the department's satisfaction that the small business is carrying on an activity for profit. If requested, the taxpayer must provide documentation to that effect to the department. In making such a determination, the department may consider the following nonexclusive list of factors:~~

~~(a) Whether the small business keeps and maintains a detailed business plan that includes strategies or methods to make a profit or improve profitability;~~

~~(b) Whether separate books, records and bank account(s) are maintained for the small business;~~

~~(c) Whether the taxpayer carries on the activity in a businesslike manner.~~

~~(4) Severance pay received as an annuity. Only cash invested on or before the due date of the return, including extensions, qualifies for this subtraction. Any severance pay invested after the return is filed does not qualify for a subtraction under this section.~~

~~(5) Severance pay received as stock options. All stock options must be converted to cash before being invested to qualify for a subtraction under this section.~~

(6) The subtraction may not exceed the lesser of:¶¶

(a) The minimum balance of principal that remains invested by the taxpayer in the small business at the close of any month during the 24 consecutive calendar months following the termination of employment; or¶¶

(b) \$500,000.¶¶

(7) Interest accrues as provided in ORS 305.220 on any unpaid tax attributable to any disallowance or withdrawal of principal.¶¶

Example 1: Maggie was terminated from employment on October 1, 2010, and received severance pay of \$50,000 as a condition of her termination. On April 1, 2011, Maggie filed her personal income tax return, for which she had not requested an extension of time to file. On August 11, 2011, Maggie invested the severance pay in a qualifying small business. Maggie does not qualify for the subtraction because she did not invest the severance pay by the due date of the return.¶¶

Example 2: Joe was terminated from employment on July 1, 2010, and received severance pay of \$20,000 as a condition of his termination. Joe invested the entire \$20,000 in Company A, which qualifies as a small business, on September 1, 2010, and took a \$20,000 subtraction on his 2010 return. On January 30, 2012, Joe withdrew the entire \$20,000 he invested. Joe must file an amended return for tax year 2010 to remove the \$20,000 subtraction (and pay any additional tax and interest that may be due) because he did not continue the investment for at least 24 consecutive months following the termination of employment.¶¶

Example 3: Alicia was terminated from employment on October 1, 2010, and received severance pay of \$80,000 as a condition of her termination. Alicia invested the entire \$80,000 in Company B, which qualifies as a small business, on December 1, 2010. Alicia took an \$80,000 subtraction on her 2010 personal income tax return. On July 30, 2012, Alicia withdrew \$20,000 of principal from her initial investment for personal use. Alicia must amend her 2010 return to remove \$20,000 of the subtraction (and pay any additional tax and interest that may be due).¶¶

Example 4: Ryan was terminated from employment on October 1, 2010. He received severance pay in the form of a \$1,000 a month annuity over 5 years beginning in October of 2010. Ryan accumulated his severance payments for 6 months and invested the \$6,000 in a small business. He claimed a subtraction of \$6,000 on his return he filed on April 1, 2011. Ryan continues to accumulate his severance pay for the next year and invests another \$12,000 in the small business on March 1, 2012. Ryan cannot claim a subtraction for the additional severance pay he invested because it was invested after the return was filed.¶¶

(8)(a) If the small business is doing business both in Oregon and some other place outside of Oregon, the amount of the subtraction allowed is generally determined by multiplying the total qualifying amount of severance pay invested by the sales factor determined under ORS 314.665 and associated administrative rules.¶¶

(b) The taxpayer may present an alternative method of calculating the amount of the qualified subtraction if the calculation under subsection (a) does not result in a reasonable reflection of the extent of the business activity in Oregon. To be considered reasonable, the method of calculation must take into account the business activity taking place within Oregon versus the activity taking place outside of Oregon. The method must be fully described in an attachment to the taxpayer's return on which the subtraction is claimed.¶¶

[Publications: Publications referenced are available from the agency.]

Statutory/Other Authority: ORS 305.100, 316.856

Statutes/Other Implemented: ORS 316.856