

**INFORMATIONAL:**  
**CAPITAL GAINS DEFERRAL ñ DEPT. OF REVENUE**  
**WORK SESSION: HB 2363**  
**WORK SESSION: DISCUSSION OF TAX CREDITS,**  
**SUBTRACTIONS, & EXEMPTIONS**  
**TAPES 109, 110 A/B**

## **HOUSE REVENUE COMMITTEE**

**MARCH 30, 1999 ñ 8:30 A.M. - HEARING ROOM A - STATE CAPITOL BUILDING**

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Members Present: Rep. Ken Strobeck, Chair

Rep. Anitra Rasmussen, Vice Chair

Rep. Deborah Kafoury

Rep. Jeff Merkley

Rep. Diane Rosenbaum

Rep. Lane Shetterly

Rep. Jim Welsh

Rep. Max Williams

Rep. Bill Witt

Staff: Paul Warner, Legislative Revenue Officer

Ed Waters, Economist, Legislative Revenue Office

Barbara Guardino, Committee Assistant

Witnesses: Brian Reeder, Oregon Dept. of Revenue

Deborah Buchanan, Oregon Dept. of Revenue

**TAPE 109, SIDE A**

007 Chair Strobeck Called meeting to order at 8:40 a.m. Opened informational meeting on Capital Gains Deferral relating to 1995 SB 323.

**INFORMATIONAL: CAPITAL GAINS DEFERRAL**

026 Brian Reeder Began review of Oregon's Capital Gains Deferral Program - An Evaluation of the First Two Years (**EXHIBIT 1**). Also, referred to summary of program - see 1995 SB 323: Capital Gains Deferral (**EXHIBIT 2**). Commented on Dept. of Revenue's review of Capital Gains Deferral law, passed in 1995 as SB 323. Primary goal of SB 323 was to stimulate investment in Oregon companies. Three parts:

1. Shortage of "risk capital" in Oregon for new companies (venture capital and angel capital)
2. Capital is fleeing to Clark County, Washington to avoid paying taxes on Oregon's capital gains
3. "Lock-in effect", disincentive to realize gain by selling, so investors leave money in investments when prudent investing would dictate moving it to higher return investment

072 Reeder SB 323 tried to alleviate these problems by providing a deferral to capital gain. Dept. of Revenue found that, in first two years that very few investors took advantage of program.

095 Reeder Exhibit 1, Page 1, Table 1: Shows that only 24 investors took advantage of program in 1996; 41 in 1997. Dept. of Revenue has concluded that SB 323 did little to alleviate the problems. There is a shortage of risk capital in Oregon. Reasons are not primarily related to taxation, they are related to the way capital markets work and the way venture funds are established and operated.

Evidence supports belief that investors are moving to Clark County. Most striking evidence is, capital gains of investors moving to Clark County was eight times as high as Oregon residents who did not move. It is not clear whether these people take their money with them when they move. Much of their money is common stocks from multi-national companies. Also, individuals who sell a business in Oregon can then move to Washington and avoid capital gain. They sell their stock and can invest in Oregon while they avoid capital gains tax.

169 Reeder Addressed "lock-in effect". This is function of total tax rate paid on any gain. Since the total tax rate is higher than Oregon's, any movement out of Oregon or deferral of Oregon's tax still leaves a relatively high federal capital gains tax. Appears SB 323 has had little effect.

185 Reeder Reviewed chart, page 9, Table 4: Assets Sold and Acquired by Type of Business Activity.

Based on this chart, DOR concluded that law has done very little the law has done very little to stimulate investment and has created few if any jobs.

224	Rep. Rosenbaum	Asked if this law has a sunset date.
233	Reeder	It expires this year.
235	Rep. Shetterly	Is this a "bad bill?"
239	Reeder	Not prepared to comment whether SB 323 is a "bad bill," although it did not stimulate employment. Dept. of Revenue's task was not to make recommendations, it was to evaluate the employment effects of the bill.
263	Chair Strobeck	Despite flight of investors to Clark County, there does not appear to be a reduction in capital investment. Is the net effect that they avoid Oregon taxes? Follow-up questions.
271	Reeder	That is correct. Believes much of investments is in common stocks. Also, business owners retire and cash out.
296	Chair Strobeck	What is the next step? Only way to avoid having people leave is to end capital gains tax in Oregon. Then state wouldn't collect taxes anyway.
307	Rep. Witt	If capital gains tax were lowered, wouldn't that lessen this flight?
314	Reeder	Yes, it would reduce incentive for people to leave. How much reduction is hard to answer.
329	Ed Waters	Directed members' attention to report (exhibit 1), pages 10-11: References capital gains exclusion and rollover. These programs allow taxpayers to exclude certain portions of their capital gains or defer at federal taxable income level. Taxpayers taking advantage of these federal exclusions wouldn't need the Oregon program. This could be one reason for drop-off in participation in Oregon program.
345	Chair Strobeck	Directed members' attention to Tax Expenditure Report, page 104. (See March 24 minutes, State of Oregon 1999-2001 Tax Expenditure Report, exhibit 9.) Capital Gains Deferral Program will sunset December 31, 1999. Asked for suggestions over the next few days as to how to deal with this program.
385	Vice Chair Rasmussen	Suggested allowing it to sunset.
407	Rep. Witt	SB 323 is too restrictive and is discriminatory in that it applies only to investments made

in Oregon. If Oregon is going to have an investor-friendly state, it needs to recognize that capital gains tax is way too high.

Federal government has already reduced its capital gains tax. Oregon needs to reduce it too.

447 Rep. Shetterly Would be interested in hearing from those who advocated the bill in 1995, including Associated Oregon Industries.

#### **TAPE 110, SIDE A**

028 Vice Chair Rasmussen The software industry shares its stocks with its employees. Then when the company is sold, the employees have capital gains due to buyouts. Maybe legislature should address this employee-investor model next session.

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#### **WORK SESSION: DISCUSSION OF TAX CREDITS,**

#### **SUBTRACTIONS, & EXEMPTIONS**

067 Ed Waters Continued discussion of summary, Individual and Corporation Tax Credits (See March 24 minutes, exhibit 7).

Alternate Energy Devices (Residential), page 144 of 1999-2001 Tax Expenditure Report (see March 24 minutes, exhibit 9).

095 Chair Strobeck Flagged for future discussion.

103 Waters Business Energy Facilities, page 146 of report. Chair flagged for future discussion.

110 Chair Strobeck Explained that flagged credits will be combined into one amendment and returned to committee.

163 Waters Energy Conservation Lender's Credit, page 147 of report. Questions and discussion. Chair flagged for future discussion.

183 Waters Geothermal Heating System Connection, page 148 of report. Sunset in 1996.

205 Waters Reforestation, page 149 of report. Questions and discussion. Bulk of credit goes to large industrial timber growers.

243 Waters Fire Insurance Credit, page 150 of report. Questions and discussion. At request of Vice

Chair Rasmussen, needs sunset date.

- 328 Chair Strobeck Flagged for future discussion and for sunset dates:  
Fire Insurance Credit  
Assessments on Workers' Compensation  
Assessments Paid to Oregon IGA: General  
Assessments Paid to Oregon Life and Health IGA
- 332 Waters Political Contribution Credit, page 154 of report. Needs sunset date. Chair flagged for future discussion.
- 343 Waters Personal Exemption Credit, page 155 of report. Rep. Witt expressed interested in increasing this exemption, not in eliminating it.
- 360 Waters Retirement Income Credit, page 155 of report. Needs sunset date.
- 392 Waters Directed members' attention to Individual and Corporation Exemptions and Subtractions (**EXHIBIT 3**). Subtractions are not credits, they are an exclusion of certain income before tax rates are applies.  
Jobs Plus Programs, page 98 of Tax Expenditure Report. Rep. Rasmussen noted, needs sunset date. Chair flagged.
- 452 Waters Medical Savings Accounts (Oregon), page 99 of report. Questions and discussion. Rep. Witt suggested leaving this exclusion alone. Needs sunset date. Chair flagged for future discussion.

**TAPE 109, SIDE B**

- 046 Waters Physicians in Medically Disadvantaged Areas, page 100 of report. Credit has not been used. Flagged for deletion.
- 060 Waters Additional Deduction for Elderly or Blind, page 100. No action.  
Additional Medical Deduction for Elderly, page 101. No means test. Rep. Witt would object to a means test. Chair flagged for sunset date.
- 105 Waters Social Security Benefits (Oregon), page 102. No action.

112	All	More discussion on means tests for deductions for elderly.
154	Vice Chair Rasmussen	Would like to set aside a day to discuss the aging population in Oregon and its implications. State should encourage baby boomers to save for long-term care.
174	Waters	Donations of art by the artist, page 103 of report. Chair flagged for future discussion.
182	Waters	Capital Gains from Oregon Reinvestment, page 104 of report. Currently under discussion by committee.
187	Waters	Local Private Activity Bond Interest, page 105 of report. Chair flagged for future discussion.
204	Waters	Service in Vietnam on Missing Status, page 106. Not currently used. Chair flagged for deletion.
224	Waters	Oil Tank Cleanup Costs, page 106 of report. Not currently used. Rep. Welsh noted, Water and Environment Committee is reviewing this exemption. Chair flagged for future discussion.
241	Waters	Underground Storage Tank Cleanup Costs, page 107. Chair flagged for future discussion.
240	Waters	Cash Payments for Energy Conservation, page 108 of report. Also see <b>EXHIBIT 4</b> . Questions and discussion. Chair flagged for future discussion.
287	Waters	Wet Marine and Transportation Insurance Policies, page 109. Questions and discussion. Will be part of another discussion on insurance.
302	Waters	Income Earned in "Indian Country", page 110. No further discussion required. Federal Pension Income, page 110. No further discussion required.
332	Waters	Oregon State Lottery Prizes, page 111. Rep. Witt has introduced a bill that would lower \$600 tax threshold to \$200. Vice Chair Rasmussen noted exemption needs sunset. Chair flagged for future discussion.

- 399 Waters Federal Income Tax Deduction, page 112 of report. No further discussion.
- 417 Waters Military Active Duty Pay, page 112. Exemption refers to Persian Gulf. Vice Chair Rasmussen suggested expanding language to include recent military activities. Chair flagged for future discussion.
- 459 Waters Interest and Dividends on U.S. Government Obligations, page 113. No further discussion.

**TAPE 110, SIDE B**

- 027 Chair Strobeck Directed members' attention to page 274 of 1999-2001 Tax Expenditure Report: Gift Packets (cigarette taxes do not apply to cigarettes that distributed as free samples). Flagged for sunset.
- 035 Vice Chair Rasmussen Asked committee to look at Federal and Veteran Institutions, page 275 of report. Chair flagged for further discussion.
- 040 Chair Strobeck Asked committee to study property tax section of Tax Expenditure Report, Chapter 2: Property Tax, page 157, and make suggestions.  
  
Noted testimony correction from Frank McNamara (**EXHIBIT 5**) concerning testimony of March 29.
- 056 Chair Strobeck Adjourned meeting at 10:05 a.m.

Submitted by, Reviewed by,

Barbara J. Guardino Kim T. James

Committee Assistant Revenue Office Manager

Exhibit Summary:

1. Informational, Reeder, Oregon's Capital Gains Deferral Program, An Evaluation of the First Two Years, 23 pp.
2. Informational, Reeder, 1995 SB 323: Capital Gains Deferral, 1 p.
3. Informational, Waters, Individual and Corporation Exemptions and Subtractions, 4 pp.
4. Informational, Waters, Cash Payments for Energy Conservation, 2 pp.
5. HB 2982, McNamara, Testimony Correction, Frank McNamara, Confederation of Oregon School Administrators, COSA Opposition to HB 2982, 1 p.