

**MINUTES OF THE
UTAH TAX REVIEW COMMISSION**

Thursday, August 25, 2016 – 2:00 p.m. – Room 445 State Capitol

Members Present:

Mr. Curtis Trader, Chair
Sen. Jim Dabakis
Sen. Lyle W. Hillyard
Rep. Joel K. Briscoe
Rep. Daniel McCay
Mr. Kelly J. Applegate
Ms. Emily D. Bagley
Mr. Phil Dean
Ms. Kathleen Howell
Mr. Troy K. Lewis
Mr. Gregory G. Prawitt
Comm. John L. Valentine
Mr. Lawrence C. Walters

Members Excused:

Sen. Deidre M. Henderson
Rep. Steve Eliason
Mr. K. Tim Larsen

Staff Present:

Mr. Bryant R. Howe, Deputy Director
Mr. Leif G. Elder, Policy Analyst
Ms. Andrea Valenti Arthur, Associate General Counsel
Ms. Bree Frehner, Legislative Assistant

Note: A list of others present, a copy of related materials, and an audio recording of the meeting can be found at www.le.utah.gov.

1. Commission Business

Chair Trader called the meeting to order at 2:00 p.m. Sen. Henderson and Mr. Larsen were excused from the meeting.

MOTION: Mr. Lewis moved to approve the minutes of the June 30, 2016, meeting. The motion passed unanimously. Rep. Briscoe, Rep. McCay, and Mr. Dean were absent for the vote.

2. Apportionment of Business Income Under the Utah Corporate Income Tax and Sales and Use Tax Exemption of Purchases of Manufacturing Equipment

Mr. Jay Blaine, Director of Policy and Research, Utah Education Association, expressed concern regarding tax changes that may reduce funding for education. He questioned the real benefits of changing to a single sales factor apportionment formula for all taxpayers under the Utah corporate income tax and emphasized the importance of a quality education system in creating a well-trained and productive workforce. Mr. Blaine responded to questions from the commission.

Mr. Derek Monson, Director of Public Policy, Sutherland Institute, stated support for expansion of the single sales factor apportionment formula. He recognized that there are legitimate concerns about expanding single sales factor apportionment. He recommended that the commission consider all tax policy options as a whole. Mr. Monson responded to questions from the commission.

Mr. Michael Parker, Director of Public Policy, Salt Lake Area Chamber of Commerce, said that the priority public policy concerns of the chamber include training a qualified workforce, enhancing and preserving Utah's premier business climate, and having a long-term vision of economic development.

Mr. Parker outlined the chamber's general perspective on tax policy and noted how tax laws interrelate and how tax policy relates to other factors in creating a state's business climate. He discussed the rigidity of current law that precludes certain industries from using the single sales factor apportionment formula, requiring other industries to use it, and providing other businesses the option to use it. Mr. Parker encouraged improving optionality to increase "business friendliness" and aligning tax policy with

economic development objectives. He commented on the option of making expansions performance based. Mr. Parker responded to questions from the commission.

Responding to a question from Sen. Hillyard, Mr. Parker discussed the options of increasing individual income tax rates and expanding the availability of the single sales factor apportionment formula.

Responding to a question from Sen. Dabakis, Mr. Parker explained the long-term perspective that the chamber holds on "business friendly" tax policy and education funding. In response, Chair Trader referenced "Apportionment of Corporate Income: 2000, 2008, and 2014" and "State Apportionment of Corporate Income: 2014 Tax Foundation" to highlight trends in other states regarding apportionment of business income.

Mr. Ryan Alexander, Certified Public Accountant, Utah Association of Certified Public Accountants, stated that certain industries, such as those that rely on natural resources, are less impacted by changes to the apportionment formula due to limitations on availability of a natural resource. He noted that to incentivize businesses to invest in Utah, the state should consider changes to the sales throwback rule as well as apportionment formula changes. He agreed with past presenters that apportionment changes should not be considered in isolation. Mr. Alexander responded to questions from the commission.

Mr. Howard Headlee, President and Chief Executive Officer, Utah Bankers Association, commented on the strength of the banking industry in Utah. He stated that a survey of the association's members showed that while some banking institutions would benefit from moving to a single sales factor apportionment formula, others would not. Therefore, it is important to keep the election component. He provided the commission with "Testimony by Howard M. Headlee, President & CEO, Utah Bankers Association." Mr. Headlee responded to questions from the commission.

Following a discussion with commission members, Mr. Headlee cautioned against generalizing a bank's tax policy preferences based on its size.

Chair Trader discussed the effects on taxpayers from different state business income apportionment formulas. He distributed "Corporate Franchise and Income Tax – Income Apportionment" and explained three scenarios that demonstrated how corporations could pay tax on more or less than 100% of business income.

Comm. Valentine commented that the Utah State Tax Commission has seen instances of a corporation paying taxes on more than 100% of its income and is working to address this problem, on an individual taxpayer basis, with the Multistate Tax Commission.

Chair Trader reminded commission members that it is the commission's charge is to recommend sound tax policy. He recommended that the commission continue its evaluation of single sales apportionment, stating that he does not think the commission is ready to make a recommendation. Commission members discussed past public comment and suggestions for future study and action.

Sen. Dabakis and Rep. Briscoe commented on the impossibility of making a tax policy recommendation in isolation from other fiscal and revenue considerations.

Sen. Hillyard stated that single sales apportionment should not be mandatory and proposed post-performance evaluations to ensure that cutting taxes in fact leads to increased economic development. Comm. Valentine expressed interest in a performance-based option but pointed out the costs of administering such evaluations.

Commission members agreed that they were not ready to make a recommendation on the question of apportionment of business income.

MOTION: Comm. Valentine moved that the commission defer further action, if any, on the issue of apportionment of business income until a future meeting. The motion passed unanimously. Sen. Hillyard, Rep. McCay, and Mr. Lewis were absent for the vote.

3. Pass-Through Entity Payment or Withholding of Tax and Pass-Through Entity Audits

Chair Trader distributed and reviewed "Governor Letter with Utah Tax Review Commission Study Request," which requests that the commission study and provide recommendations on: (1) pass-through entity withholding equity issues and (2) pass-through entity audit regulations at the state and federal level.

Mr. Nathan Runyan, Holland and Hart, distributed and discussed "Tax Review Commission Study Request," which provides background on pass-through entity withholding and identifies the concern that certain pass-through entities are unable to claim the withholding waiver option when the taxable year and filing return date of the pass-through entity taxpayer differs from that of the pass-through entity. He also distributed "Pass-Through Withholding Credit" and explained the example it provided.

Comm. Valentine presented "Tax Review Commission Presentation" and distributed "Multi-tiered Partnership Structure," which diagrams an audit structure that gives rise to pass-through entity withholding equity issues. He proposed three possible modifications to the Utah approach:

1. Refund process available to pass-through entities of withholding in excess of 5% of Utah source income.
2. Refundable credit claimable on pass-through entity return of withholding in excess of 5% of Utah source income.
3. Modification of the withholding waiver requirements to allow entities without the same tax year as their parent to qualify.

Chair Trader recounted his experience with pass-through entity tax policy and withholding equity issues.

In response to questions from Sen. Dabakis, Chair Trader discussed with Comm. Valentine and Mr. Runyan why the commission has been asked to study the equity issue of pass-through entity withholding.

Chair Trader asked the presenters to return at a future meeting with recommendations on modifications.

MOTION: Mr. Dean moved that the commission open a commission bill file to address the pass-through entity withholding equity issue. The motion passed with Sen. Dabakis voting in opposition. Sen. Hillyard, Rep. McCay and Mr. Lewis were absent for the vote.

4. Other Items/Adjourn

Chair Trader adjourned the meeting at 4:25 p.m.