

Date: January 24, 2018

To: Board of Directors

From: Neil McFarlane 

Subject: **ORDINANCE NO. 348 OF THE TRI-COUNTY METROPOLITAN TRANSPORTATION DISTRICT OF OREGON (TRIMET) AMENDING CHAPTER 14 OF THE TRIMET CODE TO REVISE THE DEFINITION OF “NET EARNINGS FROM SELF-EMPLOYMENT” (FIRST READING)**

1. Purpose of Item

This Ordinance contains an update of the TriMet Code definition for “net earnings from self-employment.” This Ordinance brings TriMet Code Chapter 14 concerning the tax on net earnings from self-employment into conformity with the Internal Revenue Code.

2. Type of Agenda Item

- Initial Contract
- Contract Modification
- Other Ordinance

3. Reason for Board Action

State laws require the TriMet Board of Directors (Board) to act by ordinance on tax matters.

4. Type of Action

- Resolution
- Ordinance 1st Reading
- Ordinance 2nd Reading
- Other _____

5. Background

TriMet’s self-employment and payroll taxes are required to conform to the state laws that govern transit district taxes. State law defines most of the terms used in the TriMet tax ordinances. In addition, ORS 267.380(1)(d) freezes the meaning of “net earnings from self-employment” to the definition under Section 1402 of the Internal Revenue Code of 1986, as in effect on December 31, 1988. However, ORS 267.380(1)(d) also gives TriMet the authority to adopt its own definitions of the terms that are used in the federal definition of “net earnings from self-employment.”

TriMet historically has chosen to incorporate by reference the federal definitions of the terms used in defining “net earnings from self-employment” in nearly all cases. Federal tax law changes continually, however, and Oregon’s Constitution prohibits any local government from simply adopting future amendments of federal law in local ordinances. Therefore, it is necessary to update TriMet’s ordinance to “reconnect” to the federal definitions of the terms used in the definition of “net earnings from self-employment” as of a specific date.

Stoel Rives LLP, on behalf of TriMet, reviews recent federal tax legislation to determine whether there have been significant changes to federal law that could affect TriMet's self-employment tax. Since the Board's adoption of Ordinance No. 344 (adopting a reconnection date of December 31, 2016), there was significant federal tax legislation enacted in December 2017, but the provisions in that legislation that may measurably affect TriMet's self-employment tax generally do not go into effect until January 1, 2018. Therefore, we believe it is prudent to update the current reconnection date from December 31, 2016 to December 31, 2017, so that taxpayers can readily understand that the amounts shown on their 2017 federal income tax returns generally apply for purposes of the TriMet self-employment tax for 2017.

Congress also could enact changes to federal law in early 2018 that could apply retroactively to the 2017 tax year. At TriMet's request, Stoel Rives is monitoring those developments, and TriMet's General Counsel will advise the General Manager about any further recommended Board action if appropriate.

In addition, there is a change to Oregon state tax law (applicable to tax years beginning on or after January 1, 2018) that may impact TriMet's self-employment tax. As background, for purposes of state and local taxation, income is subject to a jurisdiction's taxing authority generally if it is earned (or "apportioned," in tax terminology) within that authority's jurisdictional boundaries. The tax rules used to determine whether income is apportioned inside or outside of a taxing jurisdiction's boundaries are commonly referred to as "sourcing" rules. State law requires TriMet to follow the state's sourcing rules.

The 2017 Oregon legislature adopted a law (Senate Bill 28) that modifies Oregon's sourcing rules beginning in 2018. This necessarily will modify TriMet's sourcing rules, also beginning in 2018. The new law provides that a taxpayer's income from performing services is sourced to the location where the services are delivered (i.e., generally where the customer receives the benefit)—this is referred to as "market-based sourcing." Thus, if a self-employed taxpayer performs services for a customer located inside of TriMet's jurisdiction, the income generally is subject to TriMet's self-employment tax under market-based sourcing. Before 2018, income from services generally is sourced to the location where the greater proportion of costs were incurred in performing the services (i.e., often where the service provider was physically located when performing the service)—this is referred to as sourcing based on "costs of performance."

The attached TriMet ordinance need not address the state law shift from sourcing based on costs of performance to market-based sourcing. TriMet's Code already requires taxpayers to apportion "consistently" with the state's rules (*see* TriMet Code 14.10.B). Thus, there is no need for the ordinance to revise or update any TriMet Code provision based on the change in state law, and the market-based sourcing rules generally will go into effect for purposes of TriMet's self-employment tax beginning in 2018.

6. Financial/Budget Impact

This ordinance does not have a direct budgetary impact, but would be expected to contribute to the efficient administration of TriMet's self-employment tax.

7. Impact if Not Approved

Because this matter is a required housekeeping item to keep our tax ordinance in line with changes to the Internal Revenue Code, the only realistic option available to the Board is to reconnect by ordinance, as in prior years.

ORDINANCE NO. 348

ORDINANCE OF THE TRI-COUNTY METROPOLITAN TRANSPORTATION DISTRICT OF OREGON (TRIMET) AMENDING CHAPTER 14 OF THE TRIMET CODE TO REVISE THE DEFINITION OF "NET EARNINGS FROM SELF-EMPLOYMENT"

THE BOARD OF DIRECTORS OF THE TRI-COUNTY METROPOLITAN TRANSPORTATION DISTRICT OF OREGON (TRIMET), pursuant to the authority granted to it under ORS 267.380 and 267.385, does hereby ordain and decree the following ordinance:

Section 1 – Amendment of Chapter 14 of the TriMet Code.

Revision of Definition of "Net Earnings from Self-Employment". Section 14.05C of the TriMet Code is amended to read in its entirety as follows:

"Net Earnings from Self-Employment" has the same meaning as the term "net earnings from self-employment" in Section 1402 of the Internal Revenue Code of 1986 (the "IRC"), as that section was in effect and operative on December 31, 1988. In applying IRC Section 1402 for purposes of this Chapter, the words "gross income," "deductions" and "distributive share," and any other words used in IRC Section 1402 to define "net earnings from self-employment," shall have the same meaning that those words had for purposes of IRC Section 1402 under federal income tax laws in effect and operative on December 31, 2017, provided, however, that the phrase "deductions allowed by this subtitle which are attributable to such trade or business" shall not include the deduction contained in IRC Section 199 (related to domestic production activities). The purpose of these definitions is to incorporate any relevant changes in the Internal Revenue Code of 1986 made and in effect on or before December 31, 2017 except for changes in IRC Section 1402 made after December 31, 1988. For the purposes of this Section, the term "net earnings from self-employment" is not limited in any way by IRC Section 1402(b).

Notwithstanding the foregoing, "net earnings from self-employment" does not include income which would be wages under Section 3121 of the Internal Revenue Code, as amended and in effect on December 31, 1990, but for the provisions of Section 3121(b)(8)(A) of the Internal Revenue Code."

Section 2 – Effective Date.

This Ordinance shall take effect thirty days after the date of its adoption. This ordinance shall apply to individuals' taxable years starting on or after January 1, 2017.

Dated: January 24, 2018

Attest:

Recording Secretary

Presiding Officer

Approved as to Legal Sufficiency:



Legal Department