

The CAT Still Has Sharp Teeth, but the Oregon Department of Revenue Has Temporarily Dulled Them a Bit

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Background

As [previously reported](#), the new Oregon Corporate Activity Tax (the "CAT") went into effect on January 1, 2020. The new law is quite complex and arguably not very well thought out by lawmakers. Although the Oregon Department of Revenue (the "DOR") has worked hard to bring clarity to the CAT through rulemaking, many questions remain, including application of the many exemptions and computation of the required tax estimates. Despite pleas by small businesses to repeal or at least put the CAT in hibernation until the uncertainties resulting from the COVID-19 pandemic have been alleviated, both Oregon's Governor and the state's lawmakers have proclaimed in so many words that **the show must go on** - the CAT will remain in place, even during these horrific times.

As a side note, it is interesting that some of Oregon's lawmakers have stated that the CAT does not impact "small business," and further, that it only impacts the most "profitable businesses." Statements to that effect are not accurate; in fact, they are the furthest from reality. For one, the CAT is a gross receipts tax; the resulting tax has absolutely nothing to do with profitability. Also, it significantly impacts small business. The following illustrates these points:

EXAMPLE: ABC Corporation is owned by John and Mary Smith and employs 12 individuals. It has gross revenues of \$4.5 million for Year 1. After ordinary, necessary and reasonable business expenses, ABC Corporation has a net operating loss of \$250,000 for income tax purposes. After allowable deductions from gross receipts for CAT purposes (i.e., the greater of 35 percent of labor costs or costs of goods sold), it ends up with gross receipts of \$3.9 million. The resulting CAT liability in Year 1 for ABC Corporation is \$16,780 ($\$250 \text{ plus } .57 \text{ percent of } [\$3.9 \text{ million less } \$1 \text{ million}] = \$16,780$). First, ABC Corporation is a small business. Second, it actually sustained a loss for Year 1, but it has a resulting CAT liability. During times such as the ones we are experiencing today with COVID-19, businesses like the ABC Corporation may not have the resources to pay the CAT.

Taxpayers doing business in Oregon are rightfully concerned about being able to comply with the CAT, including properly computing the complex and somewhat arcane tax, making timely and sufficient estimated tax payments, and the imposition of penalties and interest for noncompliance (especially inadvertent noncompliance).

Since the CAT is not being repealed or placed in hibernation during these challenging economic times, taxpayers must make quarterly CAT payments based on estimates of their CAT liability. Liability for the CAT is based on receipts less numerous exemptions and subtractions. Determination of taxpayers' CAT liability has been problematic in light of the poorly defined and constantly changing landscape, especially in this first year of the CAT's existence.

The prospect of facing potential penalties in the face of a moving target in the first year of the CAT was bad enough. Overlaying a worldwide pandemic that has changed the business landscape dramatically has made it untenable.

At the heart of the problem is ORS 317A.161, which applies only for 2020. See HB 3427, § 78. ORS 317A.161(1) provides that the DOR "may not impose any interest or penalty that would otherwise apply to taxes due if the interest or penalty is based on underpayment or underreporting that results solely from the operation of ORS 317A.100 to 317A.158" (the rest of the CAT statute). The statute goes on to provide that a "taxpayer shall pay at least 80 percent of the balance due for any quarter or [the DOR] may impose a penalty as provided in ORS 314.400(3)." ORS 317A.162(2).

There has been considerable debate about what these poorly worded provisions mean. We understand that the Oregon legislature (before COVID-19 interrupted daily life) intended to clarify these provisions. However, that never happened. Oregon Governor Kate Brown made several statements recently regarding a relaxation of the penalty regime, but no official guidance was issued. Life changed a bit yesterday! The DOR offered some limited reprieve.

Eased Requirements

The DOR [announced in an email](#) that it is adjusting the requirements for businesses making estimated quarterly CAT payments.

Effective **immediately**, the DOR is revising the language in OAR 150-317-1300 to double the threshold for making required estimated CAT payments from \$5,000 of annual CAT liability to \$10,000 for 2020. Consequently, any taxpayer with less than \$10,000 of annual CAT liability for 2020 will not be required to make any quarterly estimated CAT payments during this year. Of course, to apply this relaxed rule, taxpayers need to be able to determine if their

annual CAT liability will be less than \$10,000.

The DOR also stated that it will not assess penalties for underestimating quarterly CAT payments or for failing to make a quarterly CAT payment, if a taxpayer does **not** have the financial ability to make such payment. Unfortunately, the DOR gives us no guidance on what it means to not have the financial ability to make CAT payments.

According to the DOR, if a taxpayer knows it will have CAT liability of at least \$10,000 in 2020 and is able to make estimated quarterly CAT payments, it should make such payments to the fullest extent that it can.

The DOR further stated that it updated information and a worksheet for calculating quarterly CAT payments on [its website](#) in light of the increased threshold.

The DOR reports that it will respect a taxpayer's good-faith efforts to comply with the CAT, and that it will not assess penalties if a taxpayer documents its compliance efforts. Such documentation should include how COVID-19 has impacted the taxpayer's business, such as:

- Its inability to make a quarterly CAT payment due to insufficient funds as a result of COVID-19;
- Its inability to reasonably compute a quarterly CAT payment or its annual CAT liability due to the impact of COVID-19; and
- Its lack of knowledge regarding whether it will have CAT liability due to COVID-19 impacts, after taking into account exclusions and subtractions.

The DOR further provided that a taxpayer will not be penalized if it is uncertain about its economic future due to the COVID-19 crisis or if it has been closed during the crisis and has no ability to determine its CAT liability for 2020.

Conclusion

The DOR's announcement is welcome news to taxpayers and tax professionals. Taxpayers who have been negatively impacted by COVID-19 and who believe they can take advantage of the DOR's guidance are advised to document their situation. In addition to the above items, taxpayers should document any decline in business, any indications of future business declines (e.g., notices from customers that they will not be able to complete future projects or will have to cancel pending orders), market or industry forecasts, and any other matters negatively impacting finances or ongoing operations.

We will continue to update you with additional CAT-related guidance as it comes out.

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