



Office of Multnomah County Auditor

Steve March
County Auditor

501 SE Hawthorne Room 601
Portland, Oregon 97214
Phone: (503) 988-3320

Fran Davison
Judith DeVilliers
Nicole Dewees
Craig Hunt
Jennifer McGuirk
Marc Rose
Mark Ulanowicz

MEMORANDUM

Date: February 28, 2013

To: Chair Cogen; Commissioners Kafoury, Smith, Shiprack, and McKeel
Chief Financial Officer Campbell

From: Steve March, Multnomah County Auditor

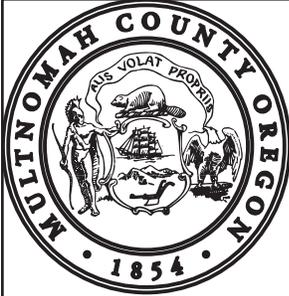
Re: Special Study of Multnomah County Business Income Tax (MCBIT) & Vendor Compliance

This special MCBIT study looks at compliance of vendors who did \$1,000 or more business with the County from FY04-05 through FY11-12. In general compliance among those businesses was very good and only 34 did not file a MCBIT return or exemption. In total \$58,600 was collected from those businesses that did owe taxes over that period; compared to the over \$52 million brought in by MCBIT in FY11-12, it represents about one-tenth of one percent of the amount.

County Purchasing changed boilerplate in contracts and independent contractor forms to better inform new vendors of the requirement to pay local taxes, and Finance and Risk Management will work closely with the Revenue Bureau of the City of Portland (who administers MCBIT for the County) to identify businesses that should be filing these returns.

We wish to thank both Purchasing and Finance for their assistance and active response to this study, as well as the cooperation of the Revenue Bureau of the City of Portland. Craig Hunt of our office conducted this special study. The response from the Chief Financial Officer may be found at the end of this report.

Cc: Joanne Fuller, COO
Brian Smith, Purchasing
Karyne Kieta, Deputy Director DCM



Steve March
Multnomah County Auditor
501 SE Hawthorne, Room 601
Portland, Oregon 97214
503-988-3320

Audit Staff
Craig Hunt

Special Study: MCBIT
February 2013

Executive Summary

The objective of this special study was to determine if County vendors fulfilled their business income tax responsibilities. All businesses that are doing business in the County are required to file a Multnomah County Business Income Tax (MCBIT) return or Annual Exemption Request. The City of Portland Revenue Bureau administers the County's business income tax.

We provided a listing of businesses from the County's master vendor file to the City so that it could be compared to the MCBIT tax roll. The City found 34 vendors that were doing \$1,000 or more business with the County during FY04-05 through FY11-12 did not file a MCBIT return. As of November 2012, the City collected \$58,600 in additional MCBIT revenues from these vendors.

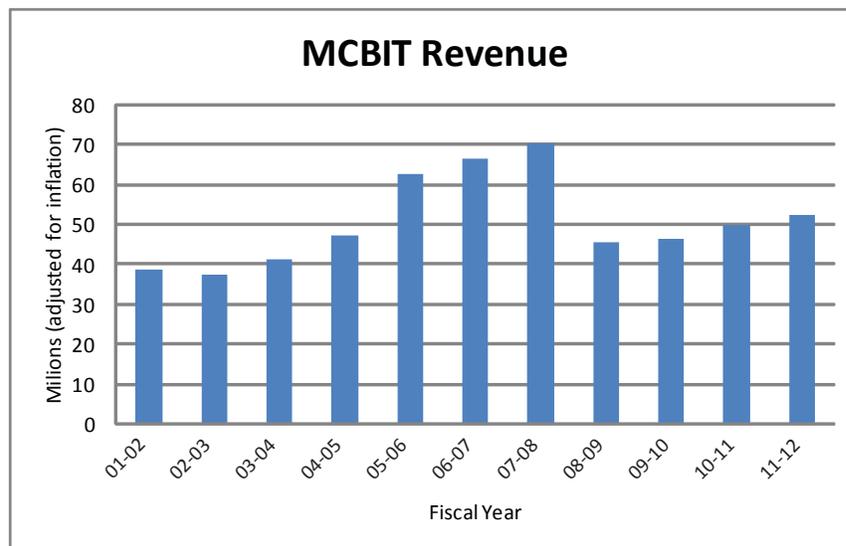
To better alert vendors to file their MCBIT returns, the County's Purchasing Unit changed the boilerplate contract and independent contractor form.

Background

All businesses that are doing business in the County are required to file a Multnomah County Business Income Tax (MCBIT) return or Annual Exemption Request. Currently, there are over 44,000 non-exempt business accounts on the County's business income tax roll. The City of Portland Revenue Bureau administers the County's business income tax along with its business license tax. Since 1993, businesses use one form to file both their City and County tax returns.

All revenues generated from MCBIT go to the County's general fund. In FY11-12, total revenues from business income taxes were \$52.25 million. A total of about 10% of these funds are distributed to Gresham, Troutdale, Wood Village, and Fairview. Another portion of MCBIT revenues pays for the City of Portland to administer the tax. Exhibit 1 shows the history of MCBIT revenues (adjusted for inflation) by fiscal year over the last 11 years. The drop in FY08-09 reflects the magnitude of the economic downturn during that time.

Exhibit 1



Source: Auditor's Office Analysis

Businesses do not have to be located in Multnomah County to owe MCBIT taxes. A large portion of MCBIT taxes are from companies that are located outside of County boundaries but are doing business in the County. In this case income should be apportioned. In cases where total gross income is less than \$50,000, businesses only file an Annual Exemption Request. If businesses are not exempt, the tax is the greater of 1.45% of net business income or a \$100 minimum fee. There is also an owner's compensation allowance of 75% of net income up to \$87,000 per owner.

The following examples illustrate these points. If a company based in Texas owns a retail store in the County and does over \$50,000 business at that location it is required to file a MCBIT tax return. A consultant living in Portland who makes \$20,000 will only have to file an Annual Exemption Request. In both cases, the businesses should be on the MCBIT tax roll. A Combined Tax Return for Individuals is included in Appendix A.

Results

Some County vendors did not file a MCBIT return

We used the County's master vendor file to identify vendors that have not filed their MCBIT return. The master vendor file is a record of all vendors who have done business with the County.

In December 2009 we provided a listing of 4,525 businesses from the County's master vendor file to the Revenue Bureau's Unlicensed Compliance Team (UCT) to compare to the County's MCBIT filers. We provided an updated listing to the UCT in December 2011. The City has a structured collection process to identify potential non-filers, determine whether a return should be filed and collect any tax revenues due. Any non-filers doing business within the City of Portland boundaries may also have to pay a business license tax.

According to the City, 34 vendors on the County's master vendor file doing \$1,000 or more business with the County during FY04-05 through FY11-12 did not file their MCBIT return as required. As of November 2012 the City collected \$141,700 in additional revenues from these vendors. Approximately \$58,600 of this amount is MCBIT revenues and the remaining \$83,100 is City business license tax revenues.

There are a number of reasons that could explain why businesses that should have filed a MCBIT return or Request for Annual Exemption did not do so.

- Apportionment. If the business is located outside of the County, the owner(s) may not understand that the tax is on income generated in the County and the income may need to be apportioned.
- Exemption on gross receipts. Some business owners with limited activity in the County may think that they do not need to file because of the exemption on the first \$50,000 of gross receipts. In this case, an Annual Exemption Request is still required.
- Owner's compensation allowance. The owner's compensation allowance up to \$87,000 per owner may also keep businesses from filing. In this case, businesses would still have to file a MCBIT return.

Some businesses may simply misunderstand the law. It is also possible that businesses choose not to file a return. MCBIT information is readily available. As part of the responsibility of operating a business, owners are obligated to be aware of and to comply with the tax laws.

During FY09-10, the Purchasing Unit changed the contract boilerplate language so that contractors will be on notice to file all of their local taxes. The Purchasing Unit also changed the Certificate Statement for Corporation or Independent Contractor form to include similar language. These two changes will help alert contractors to file their MCBIT return.

Looking forward, the County could periodically provide its new vendors to the City of Portland Bureau of Licenses for comparison to the business income tax roll.

Objective Scope and Methodology

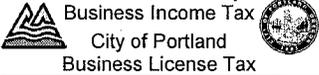
The objective of this special study was to determine if vendors on the County's master vendor file fulfilled their business income tax responsibilities.

We worked with the City of Portland Bureau of Licenses Unlicensed Compliance Team to identify vendors who did not file a business income tax return. We provided a listing of businesses from the County's master vendor file to the City. The City compared the listing to the County business income tax roll to see whether individual businesses had filed a return. The City also will put businesses who may not have filed into their compliance process.

We conducted this special study in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

Appendix

**COMBINED TAX RETURN
FOR INDIVIDUALS**



FORM SP-2011
2011 CALENDAR YEAR
DUE DATE: APRIL 17, 2012

TAXABLE YEAR From: 1/1/2011 to 12/31/2011 (Attach explanation if not a calendar year filer.)	
ACCOUNT #	SOCIAL SECURITY #
FEDERAL BUSINESS CODE	FEIN #

THIS IS A 2D BARCODE. DO NOT ERASE IT OR WRITE ON IT.

NAME _____

MAILING ADDRESS (Notify the Revenue Bureau if business location address changes)	CITY	STATE/PROV OR	ZIP CODE
--	------	---------------	----------

AMENDED RETURN? No	CEASED PORTLAND/MULTNOMAH BUSINESS? No (attach explanation)	CHECK ALL THAT APPLY <input type="checkbox"/> SOLE PROPRIETORSHIP <input type="checkbox"/> 1 MEMBER LLC <input type="checkbox"/> JOINT VENTURE / TENANT-IN-COMMON (PARTIAL OWNER)
MAILING ADDR CHANGE? No		

ATTACH PAGE 1 OF FEDERAL FORM 1040

INCOME	1. Net Income or (Loss) from Federal Schedule C (Attach all Schedule Cs)	1	\$0
	2. Business Income Tax & Business License Tax Add Back.....	2	\$0
	3. Net Income or (Loss) from Federal Schedule E, D, etc. (Attach Schedule E, D, etc.)	3	\$0
	4. Subtract 1/2 SE tax (see instructions)	4	\$0
	5. Adjusted Net Income (total lines 1, 2, 3 and 4).....	5	\$0
	6. Compensation Allowance Deduction (see instructions) (# of owners <u>1</u>)	6	(\$0)
	7. Subject Net Income (line 5 minus line 6)	7	\$0

Multnomah County Business Income Tax Average Sum of Multnomah Employees in 2011: _____		
8a. County Gross Income = _____	8c = (8a ÷ 8b) Cannot be more than 100% →	8c 0.0000%
8b. Total Gross Income* = _____	<i>*If less than \$50,000, the taxpayer is exempt and should complete the Annual Exemption Request (see instructions if tenant-in-common)</i>	
9. County Apportioned Net Income (line 7 x line 8c) .	9	\$0
10. Net Operating Loss Deduction (max 75% of line 9)	10	(\$0)
11. Income Subject to Tax (line 9 minus line 10)	11	\$0
12. Tax (line 11 x tax rate of 1.45%) MINIMUM \$100 ..	12	\$100
13. Prepayments	13	(\$0)
14. Penalty	14	\$0
15. Interest	15	\$0
16. Balance Due or (Overpayment)	16	\$100
17. REFUND: \$0 CREDIT: \$0 TRANSFER TO PORTLAND: \$0		

City of Portland Business License Tax Average Sum of Portland Employees in 2011: _____		
18a. Portland Gross Income = _____	18c = (18a ÷ 18b) Cannot be more than 100% →	18c 0.0000%
18b. Total Gross Income* = _____	<i>*If less than \$50,000, the taxpayer is exempt and should complete the Annual Exemption Request (see instructions if tenant-in-common)</i>	
19. Portland Apportioned Net Income (line 7 x line 18c)	19	\$0
20. Net Operating Loss Deduction (max 75% of line 19)	20	(\$0)
21. Income Subject to Tax (line 19 minus line 20)	21	\$0
22. Tax (line 21 x tax rate of 2.2%) MINIMUM \$100	22	\$100
23. Prepayments	23	(\$0)
24. Penalty	24	\$0
25. Interest	25	\$0
26. Balance Due or (Overpayment)	26	\$100
27. REFUND: \$0 CREDIT: \$0 TRANSFER TO MULT CO: \$0 DONATE TO "WORK FOR ART": \$0		

28. **COMBINED AMOUNT DUE WITH REPORT** (total lines 16 and 26) Check # .. **28 \$200**

Make check payable to City of Portland, 111 SW Columbia St., Suite #600, Portland, OR 97201-5840.
The undersigned declares that the information given on this report is true. The undersigned is authorized to act as a representative of the filer. Filers of incomplete returns (including returns that have not reported the Average Sum of Employees) may be subject to civil penalties of up to \$500.

Signature of Filer _____ Filer's Daytime Phone _____
Signature of Preparer _____ Date _____
Preparer's Name/Address _____ Telephone _____

REVENUE BUREAU (503) 823-5157 FAX (503) 823-5192 TDD (503) 823-6868

The Revenue Bureau administers both the City of Portland Business License Tax Program and the Multnomah County Business Income Tax Program. Request further information or forms as needed from the Bureau at 111 SW Columbia, Suite #600, Portland, OR 97201-5840 or go to www.portlandonline.com/licenses. Lessors of 9 or fewer units of residential real estate may be exempt under PCC 7.02.400(F) and MCC 12.400(F).

INSTRUCTIONS FOR INDIVIDUAL RETURN - 2011

Note: Please enter your business code below your FEIN. You may find this code in Section B of your Schedule C. (Residential lessors limited to Schedule E and D enter a business code of 53111. Commercial lessors enter a business code of 53112.)

1. Net Income is income after deductions for business expenses. Enter the sum of net income amounts from the federal 1040 Schedule C line 31 or Schedule C-EZ line 3.
2. Add back Multnomah County and City of Portland business income/license tax and other taxes measured by net income deducted to arrive at net income (line 1).
3. Enter the total income or (loss) from federal Schedule E line 26 (rental and royalty income). Gain and losses from sales of business assets (Schedule D and Form 4797), interest earned on installment contracts (Schedule B), and miscellaneous business incomes (from non-compete contracts, director fees, etc.) should also be included on this line.
4. Adjust for the following business expenses: Subtract $\frac{1}{2}$ self-employment tax, qualified retirement plan payments and health care premium deductions (Form 1040 lines 27, 28 and 29) and add (or subtract) any Oregon modifications directly related to business activities.
6. A deduction of up to 75% of the total income (line 5) is allowed but cannot exceed \$87,000 per owner. You may have two owners if both husband and wife materially participate in the business or if they jointly own rental property. No deduction is allowed if line 5 is a loss.

Apportionment (line 8 and line 18) **Multiple factor apportionment methods are not allowed.**

Gross income includes all income (gross receipts, service income, interest, dividends, income from contractual agreements, gross rents and gains on sale of business property) from activity within the City or County. With few exceptions, income in the City is also in Multnomah County. Income may be apportioned only if there is regular business activity outside the City/County. Services performed outside the City/County may be apportioned based upon percentage of performance outside the applicable jurisdiction. Sales of tangible personal property may be apportioned only if a business has payroll or property outside the jurisdiction.

MULTNOMAH COUNTY BUSINESS INCOME TAX

Multnomah Employees: Enter average sum of full-time and part-time employees working in Multnomah County during tax year (including owner).

8. County gross income includes income from all activity within the County (see apportionment instructions above). Enter the gross income within the County as the numerator of the fraction and gross income everywhere as the denominator of the fraction. Divide to determine the rate that Subject Net Income is apportioned to Multnomah County. Round apportionment rate to six places.
10. Net Operating Losses (as previously reported on line 9 of prior combined returns) are allowed a maximum carryforward of five (5) years. The annual deduction cannot exceed 75% of the apportioned income for the current year.
13. Enter all prepayments (quarterly, extension payments and credit carried forward from prior years).
14. Enter all late and/or underpayment penalties that apply (see penalty calculation instructions below).
15. Interest on taxes not paid by the original due date (April 17 for calendar year taxpayers) is calculated at 10% per annum (.00833 x no. of months). Calculate interest from original due date to the 15th day of the month following the date of payment.
16. Total lines 12, 13, 14 and 15 to determine balance due or (overpayment) for Multnomah County Business Income Tax.
17. Overpayments may be refunded, credited forward or transferred between programs.

Penalty calculation (line 14 and line 24)

A penalty of 10% (5% late penalty plus 5% underpayment penalty) of the tax must be added if the report and tax are filed and paid past the due date. An additional penalty of 20% of the tax must be added if the report is more than four months past due. Any report which is delinquent three or more consecutive years accrues an additional 100% of the tax as penalty. No late penalty is due if a timely extension is filed with the Bureau and a return is filed by the extended due date. No underpayment penalty is due if a timely prepayment is made which is at least 90% of the total tax on line 12 (County) and at least 90% of the tax on line 22 (City), or 100% of the prior year's tax.

CITY OF PORTLAND BUSINESS LICENSE TAX

Portland Employees: Enter average sum of full-time and part-time employees working in Portland during tax year (including owner).

18. Portland gross income includes income from all activity within Portland (see apportionment instructions above). Enter the gross income in Portland as the numerator of the fraction and gross income everywhere as the denominator of the fraction. Divide to determine the rate that Subject Net Income is apportioned to City of Portland. Round apportionment rate to six places.
20. Net Operating Losses (as previously reported on line 19 of prior combined returns) are allowed a maximum carryforward of five (5) years. The annual deduction cannot exceed 75% of the apportioned income for the current year.
23. Enter all prepayments (quarterly, extension payments, credit carried forward from prior years).
24. Enter all late and/or underpayment penalties that apply (see penalty calculation instructions above).
25. Interest on taxes not paid by the original due date (April 17 for calendar year taxpayers) is calculated at 10% per annum (.00833 x no. of months). Calculate interest from original due date to the 15th day of the month following the date of payment.
26. Total lines 22, 23, 24 and 25 to determine balance due or (overpayment) for the City of Portland Business License Tax.
27. Overpayments may be refunded, credited forward or transferred between programs. You may also apply a portion or all of your overpayment as a donation to the "Work for Art" program.* Transfers between programs occur as of the postmark date of request.
28. **If payment is due, make check payable to City of Portland.** Also include additional Work for Art donations on line 27.
*A donation to "Work for Art," a program of the Regional Arts & Culture Council, may be made by reducing your refund due or by paying an amount in addition to the combined amount due. Any designated donation is final. Go to www.workforart.org for additional information.

Tenant-in-common (TIC) arrangements and other joint ventures must consider the gross income of the entire activity to determine whether the gross receipts exemption applies. TICs and other joint ventures are not entitled to the residential rental exemption.

(If you choose to pay by check, you authorize the City of Portland, Revenue Bureau to convert your check to an electronic debit. Funds may be withdrawn from your account upon receipt, and you will not get your check back. Please call with questions, or to permanently opt out.)

ATTACH DETAILED SCHEDULES FOR NOL DEDUCTIONS OR OTHER DEDUCTIONS FROM INCOME

Response



Department of County Management
Finance & Risk Management

Office of the Chief Financial Officer
501 SE Hawthorne Blvd, Suite 531
Portland, Oregon 97214

Joseph "Mark" Campbell
Chief Financial Officer

Phone: 503-988-6229
Email: mark.campbell@multco.us

January 31, 2013

Steve March
Multnomah County Auditor
501 SE Hawthorne, Room # 601
Portland, OR 97214

Dear Auditor March:

Thanks to you and your staff for your special study on the Multnomah County Business Income Tax (MCBIT). The study provides some good background information and is very succinct in its presentation.

As you note, the MCBIT generated over \$52 million in FY 2011-12 and it is the largest source of revenue in the General Fund other than Property Taxes. In the tough economic times we have experienced lately maximizing tax collections has been a top priority for us.

The City of Portland administers the MCBIT under an intergovernmental agreement. The City's Revenue Bureau collects both the MCBIT and the City's Business License Tax (BLT). Many, if not most, of the 44,000 non-exempt businesses that pay MCBIT also pay the BLT. Compliance efforts have been increased in recent years but achieving complete compliance for income taxes on business entities is a goal yet to be realized.

Your study points out several of the reasons why a business may not file a tax return. The IGA with the Revenue Bureau provides for outreach, education, and auditing of business tax filers. We appreciate the exchange of information that your office provided to the Revenue Bureau. While the number of vendors doing business with the County who did not file a tax return was small (less than one-tenth of one percent) every dollar of MCBIT collected helps to support direct County services.

Going forward we will work closely with the Revenue Bureau to identify businesses that should be filing tax returns. As the recession fades it is likely that new business entities will emerge and existing businesses may regain profitability. We will want to ensure that outreach and education efforts are maintained at a high level. We are also looking into including a brief "FAQ" sheet along with the MCBIT forms in County bid package information. The timing of your study is particularly good – the IGA with the Revenue Bureaus expires at the end of the current fiscal year and we will begin negotiations on a new agreement within the next month or so.

Regards,

Mark Campbell
Chief Financial Officer