

**Written Statement – Appealing the Final Determination Letter
from the Administrator of the Multnomah County ITAX.**

**From: Thomas A. Turja
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**To: The Multnomah County Commission
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RECEIVED
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The reasons the Administrators determination is incorrect:

The ITAX initiative unlawfully discriminates against Multnomah County residents, who are taxpayers, and are not a PERS/FERS retiree. This initiative is unconstitutional, as will be proven in the following text.

The correct determination should be:

We appreciate your insight, and we now understand the County ITAX is unconstitutional. The County must find other options to generate revenue, or cut costs to balance our budget.

cc: Hardy Myers, Attorney General, Salem Office
Gordon Smith, Oregon Senator, Washington, D.C. Office
Ron Wyden, Oregon Senator, Washington, D.C. Office

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Introduction

In May of 2003, Multnomah County voters approved *measure 26-48*. This initiative imposes a three-year 1.25% income tax on county residents. The County Board adopted this measure in June 2003 by *ordinance 1012*.

The money raised on this temporary income tax measure is to go to county schools, health and senior care, public safety, and 5% to administer the program. The Oregon Constitution under *Article VI, Section 10* grants county voters authority to adopt a county charter, and Multnomah County *Charter 2.10* grants the county legislative authority "over matters of county concern to the fullest extent permitted by the constitutions and laws of the United States and the State of Oregon."

In November of 2004, County citizens voted against *measure 26-64* that would have repealed the temporary county income tax for the years of 2004 and 2005.

It's good to know that voters of Multnomah County understand the importance of funding schools. This is not my complaint.

The concern began when an article came out in the Portland Tribune dated Jan. 27, 2004. This article was written by Don Hamilton (Tribune Staff), and was titled "Public retirees excused from tax." (**Attachment 1**). Dave Boyer, the county's finance officer, and temporary ITAX Administrator commented in this article.

His quote was:

"When preparing the income tax measure last year, county officials thoroughly researched the tax code, but didn't find the PERS exemption."

The county admitted having limited experience in dealing with income tax issues, so they hired the law firm Ball Janik to explore the question. Ball Janik attorney Neil Kimmelfield quotes:

"The county could probably find legal grounds to argue in favor of taxing PERS benefits, but there is a substantial possibility that the courts would reject that argument."

Taxation issues have high visibility. How a tax administrator operates the measure directly reflects the character of the government agency. The collector must enforce a fair tax system evenly, or it will be seen as unfair and corrupt.

A good tax system will have few fluctuations and a high-degree of stability. With a state income tax system, the fluctuations can be quite large when the business cycle has a downturn. A downturn hit Multnomah County residents hard the past few years. The county sustained one of the highest unemployment rates in the nation for more than three years. This makes one understand the need to raise more money to balance the budget.

Creating a fair and equal tax system

Article IX Section 1 of the Oregon Constitution Requires:

That all taxes be levied and collected under general laws operating uniformly throughout the State.

Personal income tax under the Oregon Revised Statutes (*ORS*) is defined in *ORS 316*. The goals of the personal income tax are defined under *ORS 316.003* and they are stated here:

316.003 Goals.

(1) The goals of the Legislative Assembly are to achieve for Oregon's citizens a tax system, which recognizes:

- (a) Fairness and equity as its basic values; and
- (b) That the total tax system should use seven guiding principles as measures by which to evaluate tax proposals.

(2) The guiding principles are:

- (a) Ability to pay;
- (b) Fairness;
- (c) Efficiency;
- (d) Even distribution;
- (e) The tax system should be equitable where the minimum aspects of a fair system are:
 - (A) That it shields genuine subsistence income from taxation;
 - (B) That it is not regressive;
 - (C) That it imposes approximately the same tax burden on all households earning the same income;
- (f) Adequacy; and
- (g) Flexibility

(3) To meet those goals of Oregon's tax system, any tax must be considered in conjunction with the effects of all other taxes on Oregonians. *[199] C.457 1a)*

The ITAX violates the goals dictated under *ORS 316.003*. Multnomah County residents already pay more taxes per student than the State of Oregon allocates to the schools in the county. (*Oregonian May 8, 2005*). This is before the ITAX initiative. This tax is based on the income of county residents. It violates the fairness of that residency. The money is required for the county to provide services, for safety and welfare of the people of the county. ***Article IX Section 1, requires uniformity of taxes throughout the State.***

All residents/households should be taxed in the same manner. **By exempting PERS/FERS, it violates the basic values of ORS 316.003. This tax initiative fails to tax all county households in the same manner.** The goals of this tax, in addition, do not abide by the rule of ability to pay. Quoted under Multnomah County's, *FY 2005 adopted budget*, under budget manager's message 9 (**Attachment 2**).

The Manager Quotes:

"There are a couple of reasons why collections are expected to fall short of original estimates. One factor that has a significant impact is the decision to exempt state and federal retirees from paying this tax. This represents approximately \$5 million that was assumed in the original forecast. We also discovered that the data used to develop estimates of the tax revenue in Multnomah County included taxpayers who filed from a Portland address but actually reside in other counties. Given that many of those taxpayers live in high-income areas of Portland we believe that could account for another \$5 million in "lost" tax revenue."

Two very important issues pop out:

First, the word "decision" used to exempt state and federal retirees. Remember, the Ball Janik attorney stated:

"The county can probably find legal grounds in favor of taxing PERS benefits." **This decision made by Multnomah County to exempt that group was "Arbitrary."** In fact, the intent of this initiative was not to exclude any resident.

The word "Arbitrary" is defined in the Oxford Dictionary – American Edition, as, **(based on uninformed opinion or random choice)**. Synonyms listed under this definition include the following words – erratic, uncertain, inconsistent, unpredictable, whimsical, irrational, and subjective. Multnomah County Administrators were subjective when the "decision" was made to exempt PERS/FERS from paying this tax.

Second, is the \$5 million of "lost" tax revenue.

Taxpayers that live in high-income areas should not be filing from a Multnomah County residence if they lived elsewhere. The budget manager knows exactly which taxpayers were given immunity from their 2003 actual income tax returns. The budget manager even puts the word "lost" in parenthesis. These are wealthy residents with second homes. The county has no ability and no desire to stop this evasion of taxation.

When you combine both the exempt PERS/FERS with the wealthy evaders, the total is \$10 million or about 8% of the total budgeted receipts. Then the county adds another 5% or approximately \$6 million a year to administrate the tax. All this

adds up to about \$16 million or 13% of total receipts per year. This is definitely a material amount of loss. The goals of taxation stipulate to aim at taxpayers with the "ability to pay." **This violates that goal.** The 8% that is exempted from paying, comes from a representation of the public that definitely has the ability to pay.

Instead the county is demanding payment from a group that lost the most from this unfortunate business cycle downturn, "the unemployed." There is no ethical reason for this decision.

The ITAX Administrator defines unemployment as the replacement of taxable wages. If it replaces taxable income, why did unemployment benefits max out at \$405 per week? I made over three times that amount before the factory shut down. Unemployment income was approximately \$50,000 a year less than my prior salary. That's not replacing my taxable wages. Furthermore, this federal subsistence was extended, twice, to help out the unfortunate workers that lost their jobs. On the other hand, the benefit increase that does replace full and complete taxable wages is *Or Laws 1995, 569*. This legislative act increased all PERS members income (before tax) to offset their pension taxation. That issue will be discussed later in the text.

ORS 316.003(2)(e) states:

The tax should be equitable where the minimum aspects of a fair system are: (A) that it shields genuine subsistence income from taxation; (B) that it is not regressive; (C) that it imposes approximately the same tax burden on all households earning the same income.

This tax does not try to shield the tax burden from victims of this economic downturn, nor does it impose approximately the same tax burden on all households earning the same income. **This violates ORS 316.003.**

As a government body, Multnomah County may not violate either the state or federal constitutions. The county and its commissioners can be held liable if they engage in any activity that violates either constitution. ((*See 42 USC 1983*) (*Section 1983*) *ORS 30.265*)

All County Commissioners are required to take an oath to support both the state and federal constitution. (*See ORS 204.005, ORS 204.020*) The county commission has a duty to act in compliance with the constitution. This applies even when a court has not yet found a particular statute or government action unconstitutional. (*See Cooper & Eugene School District, 45, 301 Or 358, 364-65, 723 P2d 298 (1986)*)

This tax "rewards" more residents that have the ability to pay than those that do not. It was put together haphazardly, where equality rights are broken and there is no enforcement of wealthy taxpayer loopholes.

The ITAX violates Article IX Section 1, of the Oregon Constitution.

PERS Contract v. Constitution

PERS members have no valid reason to receive additional tax benefits

Much of this section will quote facts of *document N. 8267 (Attachment 3)*, written by Oregon State Attorney General, Hardy Myers.

First, lets understand the PERS contract with the State of Oregon:

The original purpose of [the tax exemption of PERS benefits] was to reduce payroll costs to the State of Oregon. The State would reduce current salaries paid to its employees in exchange for exempting the same employees' retirement benefits from state income taxes. *Simpson v. Dept. of Rev., 12 OTR 455 (1993)*.

Before 1991, Oregon exempted all income from state taxes for pension income of PERS. *ORS 316.680(1)(d)(1989)*. Federal retirees had a dollar limit for an exemption.

In 1989, under *Davis v. Michigan Dept. of Treasury, 489 US 803, 109 S ct 1500, 103 L Ed2d 891 (1989)*, the U.S. Supreme Court held that federal statutory and constitutional principles of intergovernment tax immunity prohibit a state from providing a tax exemption for state and local pension benefits without providing a similar exemption for federal pension benefits.

In 1991, to comply with *Davis*, the Oregon Legislature repealed the state income tax exemption for PERS and local government pension income. They also increased PERS retirement income benefits by up to 4% to partially offset the loss of the exemption. *Or Laws 1991, ch 796*.

After further law suits (including *Hughes v. state of Oregon, 314 Or*), legislature enacted PERS benefit increases that were designed to fully compensate PERS members for the loss of the tax exemption for benefits attributable to service performed before September 29, 1991. *Or Laws 1995, ch569*.

Federal retirees challenged the 1995 benefit increase, and were judged to receive the same state income tax benefits PERS members received prior to September 29, 1991.

Under the PERS Contract with the State of Oregon, the PERS members received full compensation for their taxed pensions. **There is no valid reason they should receive any additional income tax benefits (including grossing-up) from the State or any sub-section within Oregon.** The State had a contract with PERS indicating no county or city could further tax them. Multnomah County was obligated to cancel the ITAX measure at that point. *Article 1, Section 21* of the Oregon Constitution prohibits any law being passed that impairs the obligation of contracts, the plain language of *ORS 238.445* exempts PERS benefits from taxation by counties.

Multnomah County was forced to exempt PERS/FERS retirees, but in turn it made the ITAX more complex and violated the equality rights of taxation. The county was required to stop at that point and cut costs or find resources that abided by Oregon law.

Furthermore, *Senate Bill 497*, passed during the 73rd Oregon Legislative Assembly eliminated the special benefits to any PERS retiree that does not pay Oregon income tax. This legislative action applies to any PERS retiree that has moved to another state and is not an Oregon resident. This action was obviously adopted because PERS retirees were already compensated (in terms of income) with the vast majority.

Huckaba v. Johnson, 281 Or 23, 26, 573 P2d 305 (1978)

The Multnomah County Administrator, in his final determination letter, identifies this case for the reason the county is constitutional by exempting PERS/FERS retirees. He actually quotes: *"singling out of one particular class for taxation or exemption infringe upon no constitutional limitations."* That's a bold statement. It's totally misleading and has since been addressed in the courts. That's all that needs to be said about that.

In *Huckaba*, a federal retiree challenged an Oregon statute that provided an income tax exemption for up to \$2400 of federal retirement income. Military retirement income received this benefit only after age 65. The reasoning being that military personnel generally enter the armed forces at an early age and are more likely to retire at an early age and get a second career. This gives it some rational.

Preceding cases upholding laws of the privileges and immunity clause have been issues relating to; non-residents verses residents, federal pensions verses state pensions, public pensions verses private pensions, and even individuals versus corporations. But, no cases have been filed between one equal taxpaying resident verses another equal taxpaying resident. **No government agency has ever attempted discrimination based solely on residency alone, until now.**

Article 1, Section 20, of the Oregon Constitution requires:

No law shall be passed granting to any citizen or class of citizens privileges, or immunities, which, upon the same terms, shall not equally belong to all citizens.

A violation of this constitutional provision requires there to be (1) a privilege or immunity, (2) which is denied to an individual or class of citizens, (3) without a rational foundation in light of the purposes of the law or programs at issue.

For the county to change intent merely to become constitutional with *Article 1, Section 21*, their devious action does not fill the requirement of complying with rational basis.

In the ITAX measure, there is a privilege or immunity given to the PERS/FERS retirees, which is denied to an individual or class of citizens, and it has no rational foundation in light of the purpose for the law being issued.

The administrator stated in the final determination that:

The equal protection clause of the Fourteenth Amendment to the United States Constitution provides that 'No State shall deny any person within its jurisdiction the equal protection of the law. The equal protection of the laws required by the Fourteenth Amendment does not prevent States from resorting to classifications for the purposes of legislation and they have a wide range of discretion in that regard.

That statement was put on the final determination letter. (**Attachment 4**). However, the Administrator for some reason left out this next quote from *document N. 8267*, from Hardy Myers, Oregon State Attorney General:

"If the classification is reasonable, not arbitrary and rests upon some ground of difference having a fair and substantial relation to the object of the legislation so that persons similarly situated shall be treated alike."

No government body is entitled this wide of discretion to abuse power. This goes way too far when it comes to fair constitutional rights. Multnomah County officials know better.

Exempting PERS retirees' has no substantial relation to a residential income tax.

The Oregon Supreme Court has held that tax classifications survive constitutional scrutiny if there is a rational basis for the classification. However, it is not sufficient to merely point out differences between groups of taxpayers for divergent treatment. The differences justifying the attempted classification must bear a reasonable relationship to the legislative purpose.

The purpose of this measure is to tax residents for services provided. It has no relationship to the State of Oregon's contract with PERS members.

Even when an identifiable class exists, the courts generally have rejected attacks on class legislation "whenever the law leaves it open to anyone to bring himself or herself within the favored class on equal terms. *State v. Clark, 291 Or 231, 240-41, 630 P2d 810 (1981); See also Wilson v. Dept. of Rev., 302 Or at 132.*

No one has the ability to put themselves into the favored class. Either you are a PERS/FERS retiree or you are not.

This simply violates equal privileges that all residents are required under the Oregon Constitution (taxation issues or not).

Horizontal Equity

Multnomah County violates the horizontal equity of taxation.

Horizontal Equity is the most basic of applications of equal justice. In all government divisions big or small, if a person can prove that they are just like another, almost no one will deny that person a strong case for equality under all laws applying to the two of them. One would think if income were the only measure of a person, then two people with equal incomes would be treated as equals.

Income exclusions designated for an age group violate horizontal equity by benefiting taxpayers on the basis of age instead of the amount of income. Horizontal equity requires that those with equal status should be treated the same. They should pay the same amount of tax and receive the same amount of benefits. In other words, those starting as equals with the same before tax income should end up with the same after tax income.

Oregon gives private pension retirees as much as a 9% credit on the state income tax return. It does the same for federal and state retirees. Therefore, Oregon treats all pension income the same.

In 1995, *Or Laws 1995, Ch529 (House Bill 3349)*, authorized a 9.8 percent PERS increase to cover the amount of taxes that would be collected, so in essence, state and local government retirees did not lose any money out-of-pocket. The statute also expressly announces that the increase is paid "in compensation for damages suffered by members of PERS, by reason of subjecting PERS benefits to Oregon personal income taxation," it is intended as "full" complete and final payment of all members of the system.

That made all taxable income in Oregon equal. However, Multnomah County ITAX excludes federal and state retirees from paying.

The county will not win a constitutional ruling in this case. The constitution was adopted generations before this temporary ITAX. It will also be around generations after this temporary ITAX. Abiding by the laws of the constitution comes first, no matter how strongly an individual or government agency feels about a certain issue or how important that issue is.

This ITAX violates the horizontal equity of taxation and the equal privilege rights of the vast majority of taxpayers in Multnomah County.

Oregon Constitution Article 1, Section 32 – Taxes and duties, uniformity of taxation

Section 32 requires:

No tax or levy shall be imposed without the consent of the people or their representatives in the Legislative Assembly, and all taxation shall be uniform on the same class of subjects within the territorial limits of the authority levying the tax.

There is no contending that the tax did get the consent of the people. However, the county should have disclosed the PERS immunity “decision” on the title page of ballot measure 26-64 to appeal the ITAX in 2004-05. It wasn’t mentioned at all.

What is being contested is the uniformity on the same class of subjects within the territorial limits of the authority levying the tax.

In fact, if you look at *Article 1, Section 20*; *Article 1, Section 32*; and *the U.S. Fourteenth Amendment* together, this issue becomes unambiguous. Common sense supports only one plausible interpretation. **The ITAX is not equitable.**

This is an income tax on residents of a territory. It goes to schools within the territory, to health and senior care within the territory, and to public safety for the territory. No one can deny that all people within that territory equally benefit from those services.

The U.S. Supreme Court allows a high degree of flexibility in classifying taxpayers. The Federal Government will let states handle their own tax affairs, as long as no federal worker or retiree gets unusual benefits. It will not tolerate any State income tax system that gives federal employees or retiree’s favoritism over a majority of taxpayers.

Federal law dominates or “trumps” State law, so State equality and uniformity provisions cannot conflict with the Equal Protection Clause. States can decide to exempt a select group from paying a tax. As long as a State [*Davis v. Michigan Dept. of Treasury* 489 US, 803, 823] income tax draws no distinction between the federal employees or retirees and the vast majority.

If there is discrimination by a state against federal employees, it’s just a matter of indifference to the Federal Government. As long as it can fairly be said that [*Davis* 489 US, 803, 824] federal employees are treated like other ordinary residents of the state.

Multnomah County’s interest in adopting this discriminatory tax, no matter how substantial, is simply irrelevant to the nature of the two classes receiving inconsistent treatment. **This income tax of Multnomah County, gives special treatment to federal retirees over the vast majority of county taxpayers, it conflicts with federal law.**

Conclusion

To be equitable is to be just, and justice means lawfulness. This relationship concludes that equity is the highest of principles in both law making and law administration.

The Multnomah County Board of Commission as a government actor may not violate either the federal or state constitutions. In fact, the county and its commissioners may be held liable for engaging in activity that is in violation of either constitution. *(See 42 USC 1983 "Section 1983"; ORS 30.265 (authorizing lawsuits against counties for violations of section 1983)).*

The Multnomah County residential income tax initiative is one of the most basic discriminatory legislative acts ever attempted. Two of the most basic rights people have are citizenship and equality. There is no common sense to treat residents as not equals in this case.

The PERS/FERS classification exists merely as a motive not to breach the contract and violate *Article 1, Section 21* of the Oregon Constitution. There is no other legislative purpose to omit PERS/FERS from taxation on this initiative. This is a residential tax for services for all citizens to receive.

In short, PERS/FERS members have won every prior lawsuit that justifies their pensions as **full** and **complete** compensation for their retirement. For the State of Oregon, or Multnomah County, to give any additional benefits to PERS/FERS members, without equal benefits to the ordinary taxpayer is **totally unacceptable by law.**

I Appeal these violations:

- 1) *Article IX, Section 1*, of the Oregon Constitution; violations include:
 - a) *ORS 316.003(1)(a)* Fairness & Equality.
 - b) *ORS 316.003(2)(a)* Ability to pay.
 - c) *ORS 316.003(2)(b)* Fairness.
 - d) *ORS 316.003(2)(d)* Even distribution.
 - e) *ORS 316.003(2)(e)(A)* Shields subsistence income.
 - f) *ORS 316.003(2)(e)(C)* Imposes same tax burden on all households.
 - g) *Article IX Section 1* – All taxes shall be levied under general laws operating uniformly throughout the state.
- 2) *Article 1, Sections 20 and 32*, of the Oregon Constitution; violations include:
 - a) Equality of taxation rights
 - b) It was an "Arbitrary decision" to exempt PERS/FERS retirees.
 - c) There was no rational basis to exempt PERS/FERS.
 - d) The exemption bears no relationship to the legislative purpose.
 - e) The non-favored class cannot put themselves into the favored class.

3) Federal law violations:

- a) Special treatment is given to federal retirees over the ordinary taxpayers.
- b) Horizontal equity tax rights are violated.
- c) The legality of taxing the federal funded unemployment subsistence income.
- d) The moral rights for a county, to add a new tax, and subject the unemployed workers to the tax, while deciding to let their own public retirees off the hook.

4) The administrator states: "the Oregon legislature to promote the security of the Oregon employee retirement system prohibits counties from taxing Oregon PERS retirement benefits".

I'm not sure if the legislature actually says this, but please explain what the administrator means by: "to promote the security of the Oregon employee retirement system". This statement needs more clarification.

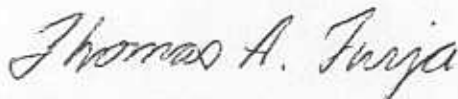
Each Multnomah County Commissioner is required by state law to take an oath to support both the federal and state constitutions. (*See ORS 204.005, ORS 204.020*). The County's duty to act in compliance with the constitution applies even when a court has not yet found a particular statute or government action unconstitutional. (*See Coopers & Eugene School District, 4J, 301 Or 358, 364-65, 723 P2d 298 (1986)*).

In essence, government officials have a duty to follow the constitution regardless of whether a court has ruled on the constitutionality of a particular issue. I emphasize to each one of you, carefully make the proper decision. If the decision is to reject my appeal, please advise me of my circuit court options and the timeframe allowed to file a lawsuit.

Finally at this time, what ever side the County Commission takes, I give my written request for privacy. This request is hereby submitted under *OR Law Chapter 192.445(2)(b)(E)*.

This request asks for: *Nondisclosure of home address, home telephone number, and electronic mail address.*

Thank you very much,



Thomas A. Turja

Multnomah County Resident and Citizen

Attachment 1
Pg 1

PortlandTribune

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Public retirees excused from tax

Income tax loophole puts PERS benefits off-limits to county

By DON HAMILTON Issue date: Tue, Jan 27, 2004
The Tribune

Many retired public employees won't be required to pay Multnomah County's new income tax on their pension benefits, county officials discovered recently.

A little-known 1989 state law exempts Public Employees Retirement System benefits from being taxed by local government. Federal pensions won't face the county tax, either, because a U.S. Supreme Court ruling requires jurisdictions to tax state and federal pensions the same way.

The financial impact remains uncertain. Dave Boyer, the county's finance officer, said the hit might be more than \$1 million out of the \$128 million the county hopes to raise annually under the three-year tax.

"It's probably not substantial," said Bob Gravely, the county's income tax information director. "It won't blow a hole in the county tax."

The discovery of the special exemption comes as voters decide on Measure 30, the income tax increase passed by the Legislature in August to help balance the state's 2003-05 budget. The mail-in ballots are due Feb. 3.

Last May, Multnomah County voters established Oregon's first county income tax, earmarked for schools and other services cut by the state. The tax requires any Multnomah County resident who pays Oregon income taxes to file an additional county tax return.

But on Dec. 1, a retired assistant attorney general wrote county officials, citing the law and challenging their right to tax her PERS retirement income. The law says PERS benefits "shall be exempt from garnishment and all state, county and municipal taxes" except for the state income tax.

The law was part of a broader PERS reform that required PERS recipients to pay state income taxes on their benefits. PERS benefits had been exempt from state income taxes before then, although federal pension benefits were taxed. A 1989 U.S. Supreme Court ruling prohibited tax collectors from treating the pensions differently.

Boyer said that when preparing the income tax measure last year, county officials thoroughly -researched the tax code but didn't find the PERS exemption.

"It's a state law, and we were not aware of it," he said. "It was not in the income tax laws. We did our due diligence but missed it."

Other interest groups are exempt from some local taxes. For example, the Legislature exempted real estate agents from local business taxes, Boyer said.

The county, having limited experience in dealing with income tax issues, hired the law firm Ball Janik to explore the question. In a Dec. 31 memo, Ball Janik attorney Neil Kimmelfield said the county could probably find legal grounds to argue in favor of taxing PERS benefits, but "there is a substantial possibility that the courts would reject that argument."

"The plain language of ORS 238.445," he wrote, "exempts PERS benefits from income taxation by counties."

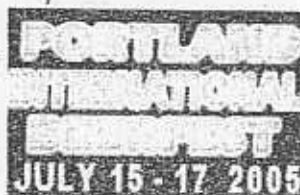
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Attachment 1
Pg 2

So the county decided to exempt the retirees from the tax. Multnomah County Attorney Agnes Sowle said losing in court could be expensive. First, the county would need an outside law firm with tax expertise. And, if it lost, it would have to refund the tax plus interest and could be required to pay penalties and the opponent's legal bill.

Louie Waldon, a retired Teamster living in Portland, doesn't think it's fair that some retirees pay while others don't.

"I don't mind paying the tax, but if I'm going to pay it, I prefer that everyone else is going to have to pay it, too," Waldon said. "I think we ought to have a new election on it."

County tax forms have already been printed, but the Web site tax form is being revised. It involves nothing more complicated than adding an extra line where taxpayers can subtract their PERS or federal pension income from their Oregon taxable income. Only then will the tax be calculated.

More than 10,000 taxpayers have made early payments on the tax, but refunds will be mailed to anyone whose tax is dropping because of the change.

For more information, call the Multnomah County tax line at 503-988-4829.

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Budget Manager's Message

ITAX Comparison FY 2004 to FY 2005

Department	FY 2004 ITAX	FY 2005 ITAX	Difference
DA	2,112,000	2,112,000	-
MCSO	6,249,000	6,249,000	-
DCJ	5,900,000	5,900,000	-
OSCP	200,000	200,000	-
DCHS	14,410,000	14,410,000	-
Health	3,092,000	3,092,000	-
BCS	6,855,000	5,318,000	(1,537,000)
Total	38,818,000	37,281,000	(1,537,000)

The \$1.5 million difference is a result of one-time-only start-up expenses incurred in FY 2004 and unnecessary in FY 2005.

BM 30 & ITAX

The State did not release the final details of its BM 30 cuts prior to Multnomah County's June budget adoption. As such, we may be required to reopen the budget at a later time to reflect the reductions as we learn about them.

Because ITAX programs backfilled state programs which were reduced or eliminated, the BM 30 cuts will force us to reexamine the validity of the funding framework and distribution of ITAX revenues. The Board has indicated its commitment to meet the intent of the voters and the legal requirements of the Temporary Personal Income for Public Schools, Public Safety and Human Services.

We now have a fairly accurate picture of the status of ITAX revenue collections. Revenue estimates were made in an environment of uncertainty, due to a lack of historical experience. Through May we have received gross revenue of nearly \$100 million from 2003 tax returns. We ultimately expect to collect anywhere from \$115 - \$118 million when all 2003 tax collections are tallied.

There are a couple of reasons why collections are expected to fall short of original estimates. One factor that has a significant impact is the decision to exempt state and federal retirees from paying the tax. This represents approximately \$5 million that was assumed in the original forecast. We also discovered that the data used to develop estimates of tax revenue in Multnomah County included taxpayers who filed from a Portland address but actually reside in other counties. Given that many of those taxpayers live in high income areas of Portland we believe that could account for another \$5 million in "lost" tax revenue.

No. 8267

This opinion is issued in response to a question from Jon Yunker, Director, Oregon Department of Administrative Services, concerning the state personal income tax treatment of private pension income.

QUESTION PRESENTED

Does Oregon unlawfully discriminate in taxing private pension income while:

1. Providing a pension benefit increase to Public Employees' Retirement System (PERS) retirees that is the functional equivalent of a rebate of Oregon personal income taxes attributed to their PERS pension income, and
2. Not taxing federal pension income?

ANSWER

No.

DISCUSSION

I. Background

Before 1991, Oregon exempted from state taxable income all pension income received from PERS. ORS 316.680(1)(d) (1989). The law further exempted all pension income received by retirees and their surviving spouses from non-PERS public retirement systems maintained by public employers within Oregon. ORS 316.680(1)(c) (1989). There was a limited exemption for pension income from federal retirement systems, subject to a maximum dollar limit. *Id.* There was no exemption for private pension income.

In 1989, the United States Supreme Court held that federal statutory and constitutional principles of intergovernmental tax immunity prohibit a state from providing a tax exemption for state and local government pension benefits without providing a similar exemption for federal pension benefits. *Davis v. Michigan Dept. of Treasury*, 489 US 803, 109 S Ct 1500, 103 L Ed2d 891 (1989). To comply with *Davis*, the 1991 Oregon legislature repealed the state income tax exemptions for PERS and local government pension income. Or Laws 1991, ch 823, § 3.¹ The legislature also increased PERS retirement benefits by up to 4 percent to partially compensate PERS members for the loss of the tax exemption. Or Laws 1991, ch 796.

PERS members immediately commenced a lawsuit challenging the repeal of the tax exemption. The Oregon Supreme Court held that the repeal breached the employment contract between participating public employers and PERS members to the extent it required taxation of benefits attributable to services performed before September 28, 1991, the effective date of the repeal. *Hughes v. State of Oregon*, 314 Or 1, 36, 838 P2d 1018 (1992). The *Hughes* court declined to comment on the appropriate remedy for the breach, noting that "[t]he legislature is the most appropriate branch of government in the first instance to choose among the available remedies." *Id.* at 33 n 36.

In 1993 and 1994, PERS members filed two lawsuits, subsequently consolidated, to recover damages for the breach of their employment contract. After several years of litigation, the case was settled. Pursuant to the settlement agreement, the legislature enacted PERS benefit increases that were designed to fully compensate PERS members for the loss of the tax exemption for benefits attributable to service performed before September 29, 1991. Or Laws 1995, ch 569; Or Laws 1997, ch 175.¹

Federal retirees challenged the 1995 benefit increase, alleging that it was a tax rebate that illegally favored state and local government retirees over federal retirees. The Oregon Supreme Court held that the 1995 increase was the functional equivalent of a tax rebate and that, under *Davis*, the state could not provide such a rebate without providing similar tax treatment to federal retirees.¹ *Vogl v. Dept. of Rev.*, 327 Or 193, 208, 960 P2d 373 (1998). The court declined to direct a remedy, but remanded the case to the Tax Court for further proceedings. *Id.* at 212. On remand, the case was certified as a class action and the parties agreed to a stipulated judgment, which was entered by the court. The judgment requires the Oregon Department of Revenue to refund state personal income taxes paid by members of the class to the extent those taxes were attributable to federal pension income based on services performed before September 29, 1991. In addition, the Department of Revenue must allow class members to exclude from their taxable income in future tax years all federal pension income attributable to services performed before September 29, 1991.

II. Legality of Providing Unequal Tax Treatment to Private Pension Income

Attachment 3
Pg 2

State legislative power is plenary subject only to limitations imposed by the state and federal constitutions and preemptive federal statutes and regulations. *See, e.g., Latourette v. Clackamas Co. et al*, 131 Or 168, 170, 281 P 182 (1929). Accordingly, our review is confined to determining whether the disparate tax treatment afforded private pension income violates a limitation found in one of those authorities.

No federal statutes or regulations prohibit the states from treating public and private pension income differently for tax purposes. Therefore, the scope of our inquiry is limited to whether such different treatment violates any state or federal constitutional provision. Disparate tax treatment potentially implicates three constitutional limitations: (a) the tax uniformity requirements of Article I, section 32, and Article IX, section 1, of the Oregon Constitution; (b) the equal privileges and immunities guarantee in Article I, section 20, of the Oregon Constitution; and (c) the equal protection guarantee of the Fourteenth Amendment to the United States Constitution.

We begin by analyzing the state constitutional limitations. *See, e.g., Sterling v. Cupp*, 290 Or 611, 614, 625 P2d 123 (1981); *Cooper v. OSAA*, 52 Or App 425, 432, 629 P2d 386 (1981), *rev den* 291 Or 504, 634 P2d 1347 (1981) (citing *State v. Spada*, 286 Or 305, 594 P2d 815 (1979)). *See also* Linde, *First Things First, Rediscovering the State's Bill of Rights*, 9 Bal L Rev 379 (1980).

A. Tax Uniformity Provisions Under the Oregon Constitution

Two provisions in the Oregon Constitution require uniform taxation.¹ Article I, section 32, provides, in part, that:

all taxation shall be uniform on the same class of subjects within the territorial limits of the authority levying the tax.

Article IX, section 1, provides:

The Legislative Assembly shall, and the people through the initiative may, provide by law uniform rules of assessment and taxation. All taxes shall be levied and collected under general laws operating uniformly throughout the State.

The Oregon Supreme Court has held that tax classifications survive constitutional scrutiny under these provisions if there is a rational basis for the classification. The court explained:

What is required in assessing a constitutional challenge to classification for tax benefit is a review of the grounds for the classification to determine if it rests upon a rational basis. The legislature may make distinctions of degree having a rational basis, and when subjected to judicial scrutiny they must be presumed to rest on that basis if there is any conceivable state of facts which would support it. * * * It, however, is not sufficient to merely point out differences between the groups of taxpayers for divergent treatment. The differences justifying the attempted classification must bear a reasonable relationship to the legislative purpose.

Huckaba v. Johnson, 281 Or 23, 26, 573 P2d 305 (1978) (citations omitted).

In *Huckaba*, a federal retiree challenged an Oregon statute that provided an income tax exemption for up to \$2,400 of federal retirement income other than military retirement income. Military retirees were eligible for this exemption only after reaching age 65. Moreover, the exemption for military retirees was reduced, dollar for dollar, by any earned income received by the retiree during the taxable year. ORS 316.067(1)(c) and (3) (1975). The Department of Revenue argued that the reason for this disparate treatment was that military personnel, unlike other federal employees, were eligible for retirement after 20 years of service, regardless of age. Because military personnel generally enter the armed forces at a relatively early age, they are more likely than other federal employees to retire while still young enough to pursue a second career and to earn additional retirement benefits in that career. The court held that this rationale established a reasonable basis for the challenged law and, therefore, the disparate treatment afforded military retirees did not violate Article I, section 32, or Article IX, section 1, of the Oregon Constitution.¹ 281 Or at 28-31. The *Huckaba* court emphasized that a tax classification need not be narrowly drawn, but may instead be a general one based on characteristics typical of the affected class:

General rules are essential if a system of the magnitude and complexity of the Personal Income Tax Act is

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to be administered with a modicum of efficiency, even though application of the rule may produce seemingly arbitrary consequences in some cases. A nonmilitary federal retiree may, in fact, after retirement obtain employment and create an additional retirement fund. Or conversely an Armed Forces retiree may be unable to enter a new career and be required to subsist on his military retirement pay. Making these determinations would require individualized proof as each income exclusion was claimed. The legislature could reasonably choose between a system of individualized inquiry and a general rule based on the source of the retirement benefit. The former method would introduce complexities in the administration of an already complex tax system and increase the expense of administration. The choice between these competing policies is a legislative determination and the decision to accord the benefit on the basis of an easily ascertainable criterion does not offend constitutional principles.

Id. at 30-31.

More recently, the courts have upheld Oregon's taxation of public retirement benefits paid by the state of Alaska from 1985 through 1990, even though PERS benefits were exempt from tax during that time period. *Simpson v. Dept. of Rev.*, 12 OTR 455 (1993), *aff'd* 318 Or 579, 870 P2d 824 (1994). The taxpayer in *Simpson* had argued that the failure to exempt benefits paid by Alaska's pension plan violated, among other things, Article I, section 32, of the Oregon Constitution. 12 OTR at 456. The tax court rejected the taxpayer's argument, noting:

The purpose of [the tax exemption for PERS benefits] is to reduce payroll costs to the State of Oregon. The state can reduce current salaries paid to its employees in exchange for exempting the same employees' retirement benefits from state income taxes; this is certainly within the legislature's power. This court has previously found such purpose is a "rationale [sic] predicate" for the classification.

Id. at 457-8 (footnote omitted) (citing *Lindau v. Dept. of Rev.*, 10 OTR 92, 93 (1985)). The tax court further observed that the taxpayers did not challenge the taxation of retirement benefits received from private pension plans, "recognizing that they may be substantially different." 12 OTR at 457 n 3. On appeal, the Oregon Supreme Court affirmed the tax court's holding, stating that the taxpayers "have not advanced any viable legal basis supporting their contentions." 318 Or at 581.

Under *Huckaba*, the state has broad discretion to establish tax classifications as long as the distinction supporting the classifications rests on a rational basis, which "any conceivable state of facts" would support. *Huckaba*, 281 Or at 26. *Simpson* stands for the further proposition that the state may rationally decide to compensate Oregon public employees by providing a tax exemption instead of additional cash compensation or other employee benefits, while taxing non-PERS pension income. 12 OTR at 457-8, *aff'd* 318 Or 579; *see also Lindau v. Dept. of Rev.*, 10 OTR at 93. The same rationale applies to the 1995 and 1997 PERS benefit increases, which compensated PERS members for the loss of the tax exemption. Thus, we conclude that Oregon's constitutional tax uniformity provisions do not require equal tax treatment of PERS benefits and private pension income.

Under *Davis*, discussed above, federal principles of intergovernmental immunity require equal treatment of Oregon government and federal pension income. The state's decision not to tax federal pension income attributable to services performed before September 29, 1991, was for the purpose of correcting a violation of those federal law principles and complying with the terms of a court judgment. Under the circumstances, the state's decision not to tax federal pension income was manifestly rational. In contrast, the federal intergovernmental immunity principles do not require equal tax treatment of public and private pension income. Accordingly, we conclude that the state does not violate Oregon's constitutional tax uniformity provisions in providing a tax exemption for federal pension income without providing a similar exemption for private pension income.

To summarize, we conclude that the state's taxation of private pension income does not violate Article I, section 32, or Article IX, section 1, of the Oregon Constitution.

B. Equal Privileges and Immunities Under the Oregon Constitution

Article I, section 20, of the Oregon Constitution provides:

No law shall be passed granting to any citizen or class of citizens privileges, or immunities, which, upon the same terms, shall not equally belong to all citizens.

A violation of this constitutional provision requires there to be (1) a privilege or immunity, (2) which is denied to an individual or class of citizens, (3) without a rational foundation in light of the purposes of the law or program at issue.

1. Privilege or Immunity

To establish a violation of Article I, section 20, the plaintiff must first show that there is a privilege or immunity that someone else is receiving. *State v. Scott*, 96 Or App 451, 455, 773 P2d 394 (1989). Recipients of private pension income are taxed on that income, while recipients of PERS and federal pension income either are not taxed or are compensated for the tax by a commensurate increase in their pension income. Thus, private retirees are denied a privilege that is provided to PERS and federal retirees.

2. Discrimination Against a Class

The next issue is whether the taxation of private pension income constitutes a denial of a privilege to a cognizable "class" of citizens within the meaning of Article I, section 20. The Oregon Supreme Court has consistently held that laws establishing classifications do not automatically violate Article I, section 20.

[T]his court will not invalidate a law on the simple grounds that the law classifies individuals or groups of individuals. "[E]very law itself can be said to 'classify' what it covers from what it excludes." *State v. Clark*, *supra*, 291 Or at 240. Article I, section 20, prohibits those schemes that classify "persons or groups by virtue of characteristics which they have apart from the law in question."

Wilson v. Dept. of Rev., 302 Or 128, 131-32, 727 P2d 614 (1986).

Generally, to be cognizable under Article I, section 20, a class must be identifiable by virtue of social or personal characteristics that exist apart from the classification created by the challenged government action; classes that are created solely by the challenged law itself "are entitled to no special protection and, in fact, are not even considered to be classes for the purposes of Article I, section 20." *Sealey v. Hicks*, 309 Or 387, 397, 788 P2d 435 (1990); *see also Greist v. Phillips*, 322 Or 281, 292, 906 P2d 789 (1995); *Hale v. Port of Portland*, 308 Or 508, 524-26, 783 P2d 506 (1989). Even when an identifiable class exists, the courts generally have rejected attacks on class legislation "whenever the law leaves it open to anyone to bring himself or herself within the favored class on equal terms." *State v. Clark*, 291 Or 231, 240-41, 630 P2d 810 (1981); *see also Wilson v. Dept. of Rev.*, 302 Or at 132.

Although these principles are easily articulated, their application to specific cases can be problematic. The Supreme Court's analysis of "true classes" under Article I, section 20, has not been entirely clear or consistent. *See Neher v. Chartier*, 124 Or App 220, 225-26 n 3 (summarizing cases), 862 P2d 1307 (1993), *rev'd* 319 Or 417, 879 P2d 156 (1994). Based on the current status of the law, we believe it is an open question whether the Supreme Court would consider such groups as "private retirees," "federal retirees" and "PERS retirees" to be "true classes." Compare *State ex rel Huddleston v. Sawyer*, 324 Or 597, 932 P2d 1145 (1997) and *Wilson v. Dept. of Rev.*, 302 Or 128, with *Sealey v. Hicks*, 309 Or 387. We need not step into this quagmire because our analysis of the third element of Article I, section 20, is determinative. Therefore, we will assume, solely for purposes of reaching an analysis of the third element, that these groups are cognizable classes under Article I, section 20.

3. Rational Basis Test

We next consider whether anything about the source of the private retirees' pension income justifies the discriminatory tax treatment. A discriminatory classification violates Article I, section 20, only if it "either is impermissibly based on persons' immutable characteristics and reflects 'invidious' social or political premises or has no rational foundation in light of the enabling statute's purposes." *Northwest Advancement v. Bureau of Labor*, 96 Or App 133, 142, 772 P2d 943, *rev den* 308 Or 315 (1989). The tax classification at issue here is based on the source of the taxpayer's pension income and therefore does not constitute "invidious" discrimination based on immutable personal characteristics of the disfavored class. *See* Letter of Advice dated October 14, 1985, to Raymond P. Thorne, Administrator, Employment Division (OP-5878) at 3 (distinction based upon tax rates does not create suspect class). The issue, therefore, is whether the classification lacks a rational foundation in light of its purposes. *See Huckaba v. Johnson*, 281 Or at 26.

For the reasons discussed in Part IIA above, there is a rational basis for providing favorable tax treatment to federal and PERS pension income while taxing private pension income. The Oregon Supreme Court has applied the same rational basis test to determine whether discriminatory tax treatment of pension income violates Article I, section 20. *Huckaba*, 281 Or 23. Because there is a rational basis for the disparate tax treatment afforded private retirees, we conclude that the disparity does not violate Article I, section 20, of the Oregon Constitution.

C. Equal Protection Under the United States Constitution

The Equal Protection Clause of the Fourteenth Amendment to the United States Constitution provides that "No State shall * * * deny to any person within its jurisdiction the equal protection of the laws." The Oregon Supreme Court has noted:

The equal protection of the laws required by the Fourteenth Amendment does not prevent states from resorting to classifications for the purposes of legislation and they have a wide range of discretion in that regard * * * if the classification is reasonable, not arbitrary and rests upon some ground of difference having a fair and substantial relation to the object of the legislation, so that persons similarly situated shall be treated alike. *This latitude is notably wide in classifications for purposes of taxation.*

Dutton Lbr. Corp. v. Tax Com., 228 Or 525, 539, 365 P2d 867 (1961) (citations omitted, emphasis added) (citing *Royster Guano Co. v. Virginia*, 253 US 412, 40 S Ct 560, 64 L Ed 989, 990 (1920)).

Oregon courts generally find a classification to be constitutional under the federal equal protection clause if it is constitutional under Article I, section 20, of the Oregon Constitution. *See, e.g., State v. Freeland*, 295 Or 367, 370, 667 P2d 509 (1983) ("The test of unequal treatment under Or. Const. art. I, § 20, is not always the same as the tests articulated from time to time under the federal equal protection clause, although the clauses are sufficiently similar that compliance with article I, section 20 usually will also satisfy the 14th amendment"); *State v. Clark*, 291 Or at 243 ("for most purposes analysis under Article I, section 20 and under the federal equal protection clause will coincide"); *Cooper v. OSAA*, 52 Or App at 432 (scope of Article I, section 20, and the federal equal protection clause are generally the same). For the reasons discussed above, we find that the tax classification at issue here rests on a rational basis, and we therefore conclude that the disparate tax treatment afforded private pension income does not violate the Equal Protection Clause of the Fourteenth Amendment to the United States Constitution.

HARDY MYERS
Attorney General

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The ITAX Administrator has reviewed your protest under the provisions of ITAX Administrative Rule § 11-614(A) and has denied your protest and issues this Final Letter of Determination.

The Oregon Constitution Article VI, section 10 grants county voters authority to adopt a county charter.

Multnomah County Charter Section 2.10 grants the county legislative authority "over matters of county concern to the fullest extent permitted by the constitutions and laws of the United States and the State of Oregon." Multnomah County has authority to enact laws taxing incomes to pay for county services required for the health, safety and welfare of the people of the county.

On May 20, 2003, Multnomah County voters approved Measure 26-48 imposing a three year 1.25% income tax for county schools, health and senior care and public safety. On June 19, 2003, by Ordinance 1012, the Board adopted the voter-approved Measure.

In addition, the Oregon legislature to promote the security of the Oregon employee retirement system prohibits counties from taxing Oregon PERS retirement benefits in ORS 238.445(1). Multnomah County, like the United States and Oregon taxes unemployment insurance because it replaces taxable wages. It's not unconstitutional for Oregon not to tax Social Security benefits but to tax unemployment benefits. It also not unconstitutional for Multnomah County not to tax social security or PERS benefits, but to tax unemployment benefits.

Equal protection of the laws as required by the Fourteenth Amendment or the Oregon privileges and immunities clause does not prevent the state of Oregon or Multnomah County from resorting to classifications for the purpose of legislation and they have a wide range of discretion. That latitude is notably wide in classifications for purposes of taxation. Inequalities that result from singling out of one particular class for taxation or exemption infringe upon no constitutional limitations. *Huckaba v. Johnson*, 281 Or 23 (1978).

Consequently, the Administrator has determined that the Multnomah County personal income tax is constitutional and was properly adopted.

You have 30 days from the date of this letter to pay this billing or to file a written notice of appeal. If you file a written notice of appeal within the 30 days allowed by the administrative rules, you must then file a written statement with the facts and legal issues relating to your appeal to the Multnomah County Board of Commissioners within 90 days from the date of this letter. You may refer to "Your Right to Appeal" for information regarding the content of this statement or call the Help Desk at (503) 988 - ITAX (4829) for any clarification.

Approved:

David A. Boyer
 ITAX Administrator
 Chief Financial Officer
 Multnomah County, Oregon

Dated: April 20, 2005