Date March 28, 2011 Oregon Civic Justice Center
3:30 p.m. Melvin Henderson-Rubio Hearing Room
Salem, OR

OREGON LAW COMMISSION

MEMBERS PRESENT: Lane Shetterly, Chair
Prof. Bernie Vail, Vice Chair
Chief Judge David Brewer
Mark Comstock
John DiLorenzo, Jr.
Hardy Myers
Scott Shorr
Dean Symeon Symeonides
Prof. Dom Vetri
Justice Martha Walters (for Chief Justice DeMuniz)

MEMBERS EXCUSED: Rep. Chris Garrett
Julie McFarlane
Judge Karsten Rasmussen
Sen. Floyd Prozanski
Mary Williams (for Attorney General John Kroger)

STAFF PRESENT: Jeffrey C. Dobbins, Executive Director
Wendy J. Johnson, Deputy Director and General Counsel
Dexter Johnson, Legislative Counsel
David Heynderickx, Special Counsel to Legislative Counsel
Kate Tosswill, Deputy Legislative Counsel
Lisa Ehlers, Legal Assistant

GUESTS: Clint Bentz, Patrick Capper, Jeff Cheyne, Doug Cushing, Mazen Malik

MEASURE/ISSUES HEARD: Recommendations of Bills and Reports to 2011 Legislative Assembly:
HB 2541
SB 867

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<th>Speaker</th>
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<tr>
<td>Lane</td>
<td>Welcome everyone. Other Business, Wendy and Jeff please update bills and budget.</td>
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<td>Johnson</td>
<td>Review of our current bills. Summary report of</td>
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recommendations. Seven bills on the list, the first one we will be discussing, which is Inheritance Tax. Juvenile Summons bill had its hearing and was on the consent calendar in the House so it was moved over to the Senate. Art Consignment bill has a work session scheduled tomorrow in House Judiciary. The Elective Share update moved out of Senate Judiciary with a work session. Fitness to Proceed moved out of Senate Judiciary today with a work session and it goes to Ways and Means. This bill is going to take a lot of work because of the fiscal. The Uniform Real Property Transfer on Death Act, Senate Bill 815, is scheduled for a hearing on Thursday. Environmental Covenants Act will also be in a hearing on Thursday. All the bills are moving and seem to be in good shape.

Dobbins

We also have a few projects for the next biennium. HB 3277 was up for a hearing a couple of weeks ago and it would have added to the Administrative Procedure Act in Oregon and would have allowed arbitrary and capricious review of rule making in Oregon. During the hearing the Oregon Law Commission was mentioned as a possible group to look at this, so there is a possibility that we may get a corner of judicial review back. Uniform Partition of Heirs Property supporters called us after the bill was dropped and asked if we had any interest in it. We indicated that we would be happy to work with them. Another issue that came up was how to revoke an adoption. We may or may not be getting a proposal from the House on that issue. Also, the UCC Article 9 amendments if we have time to take that on. OJD record issue with respect to adoptions.

Lane

We probably want to schedule the Program Committee soon.

Hardy

The other OJD projects, will they be ready?

Johnson

Both the Juvenile and Adoption Record Issues have been approved and we are hoping so.

Shetterly

Let’s begin with the recommendation of the Inheritance Tax Work Group. Welcome Patrick, Mazen, Clint, and Kate who are on the work group.
Johnson

Emailed/handed out draft minutes and -4 and -5 amendments. I will be working from the -5s and the report. The report explains the history of Inheritance Tax, but focuses on the policy changes made by the work group and goes section by section at the end to explain the content. Here is some background on Inheritance Tax in Oregon. In 2001, EGTRA passed and it phased the credit out by 2005. We are still tied to this 2001 law, which is the main reason we were asked to tackle this. In 2007, Oregon passed our own National Resource Property credit. Being tied to the Feds and having our own wasn’t working. Also, our code had never been systematically reviewed. It was a mess. That is why we did the project.

Shetterly

Directives from the legislature were to create a standalone Oregon inheritance tax (name changed to estate tax) and to maintain revenue neutrality, not to raise or lower revenue.

Johnson

Page 7. This bill will connect to the December 2010 Federal Law, so we can tie this by definitions and structure. Otherwise it will be a standalone. This bill will increase our threshold to 1.5 million. Many reasons for the increase; it hadn’t been raised for awhile, we wanted to be closer to Washington’s threshold, easier to enforce, and eliminates a lot of the returns. Not a unanimous recommendation. Next issue is the tax rate computation, section 3 in the bill (rate table). That keeps us revenue neutral and competitive with Washington. Also, it is a progressive rate. Although 19% might seem on the high end, the net result is not 19% because you will get a Federal tax credit.

Page 8. We put in our own tax rate schedule and the Work Group thought it would be better to use a ramp over the threshold. Also a model that Washington uses.

Marital Property. Few changes, mostly technical, mostly we’re codifying some administrative rules.

Intangible Property – special work group worked on this and decided that we can’t tax intangibles of out-of-state residents. Can continue to tax Oregon residents on whole estate (including intangibles).

Johnson

Page 16. Interest and penalties section of present law. In keeping with how federal government keeps interest on deferred
payments. Nothing too significant.

Page 17. Clarifications on DOR’s authority, statute of limitation, and a lot of clean up. That leaves Natural Resources.

DiLorenzo What are the thresholds of our surrounding states?

Johnson Washington is the only other state in the Northwest with a tax.

DiLorenzo Remove taxability of intangibles. What happens if you establish stock brokerage and trust assets, then you move, is it in Oregon?

Johnson If the descendent has moved out of state, that would be considered intangibles.

DiLorenzo Even if the Trustee still lives in Oregon?

Shetterly It is all based on domicile. Defined in Section 3 of the bill.

Johnson Department of Revenue showed that the revenue from intangibles were not significant.

Pages 9-16. Natural Resources policy change. We redefined the three definitions focusing on businesses for farm, forestry, and fish. On page 10 you can see that we changed the formula. This is more stand-alone than what we have now. The formula for the natural resource credit is found in section 7 of the bill. It looks at the percentage of the estate that is natural resources. The alternate formula is in footnote 27. This bill will use a formula not a schedule. This does create a revenue impact. A reason this project was sent to us was to answer the question of what is working capital. The work group struggled on defining this, but came up with it being the rest of natural resource property up to 20% or 1.5 million at the most. We are calling this operating allowance instead of working capital.

Pages 12 - 13. Replacement Policy.

This was a big area of concern. Changed it so you can replace real property with real property and personal property with personal property. The look forward and look back says must use 5 of 8 years but only deals with real property. We made it more consistent and only require a look back. This bill makes it more enforceable if you don’t follow through. The heirs will
have to report each year until the five years is met.

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<th>Shetterly</th>
<th>Let’s go back to the formula for the tax credit. This was very difficult to maintain revenue neutrality.</th>
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<td>Dobbins</td>
<td>Looking at the sheet distributed today, one side is a bunch of sample estates. The other side adds perspective. Look at the sample estates gross estate. The first two lines under the double line look at what each estate would owe under current law and -3, -4 which is just like -5. All the way up until you get to the very largest estate, the amount owed is lower in the proposal than in current law. The highest estate would pay a little more. Then take into account the natural resource credit. Once the estate goes over 1.5 million, they are taxed on the amount that is above that NRCredit. NRC should be tied to the amount of property that your estate has in natural resources. There must be more than 50% natural resource property, but can claim less. The main source of uncertainty comes from the difference between the last 4 lines. It is much less because you’re getting 1.5 million off the top, and the NRC. This reinforces the effect of the 1.5 exemption. Mazen’s proposal credit is revenue neutral. The difficult part of the proposal is that you start and then take off the 1.5 million dollar credit. This is revenue neutral, but it looks very different. We need to stay neutral but the perceptions may not look great.</td>
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<td>Shetterly</td>
<td>Any questions?</td>
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<td>DiLorenzo</td>
<td>You recommendation would be to depart from -5?</td>
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<td>Dobbins</td>
<td>Yes. We would substitute footnote 27 for lines 22-27 on page 16. The work group didn’t go through with Mazen’s recommendation because they didn’t understand it.</td>
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<td>DiLorenzo</td>
<td>On page 3 of -5. Intangibles. What if I own a building and have been asked to create a LLC, would I then have no real estate? This is a very common practice for single asset entities. Establishing property and moving seems like a great advantage to move yourself and your capital out of state to avoid the tax.</td>
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<td>Johnson</td>
<td>The work group talked about how do you draw the line?</td>
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These minutes are in compliance with Senate and House Rules. Only text enclosed in quotation marks reports a speaker’s exact words. For complete contents, please refer to the recording.
Shetterly  Conceptually it is very difficult to capture. Clint and Jeff Cheyne – Please comment on this?

Bentz  We were trying to simplify the calculations and explanations. We have a lot of small estates and they have been really carrying the tax burden.

Cushing  My concern with the new formula is that it leaves the group of estates between 1.5-3 million ranges who wouldn’t get the benefit. For the relatively small number estates it seems that it is unfair.

Cheyne  I’m still struggling with footnote 27 formula. How am I going to explain this to clients? It does promote revenue neutrality, but how can we readily use it?

Dobbins  $130,000 less credit under the footnote than -5.

Shetterly  How about if we move -5 as given to us and recognize that we let the legislature look at the formula.

Hardy  So moved.

Shetterly  Walters abstained. Further discussion? None. Any objections? No. Motion carried.

Dobbins  Senate Bill 867 – UECA created a system for establishing long term interests and was offered to the legislature in 2005. We have a program that does a lot of this. We didn’t need to go with all of UECA, but took the best parts. Section 3(a) says these agreements cannot be overridden and sub 6 of section 3 says it is valid even if an agreement imposes institutional control.

Shetterly  John DiLorenzo would you like to speak on this?

DiLorenzo  Just want to say thanks to the staff and Chair. We discovered that Oregon was a pioneer with DEQ. We decided to borrow what was best of UECA that would further shore up DEQ’s authority.
Jeff- Did you make the one change to the report that we were discussing?

Dobbins

Yes, on page 10.

DiLorenzo

Move to adoption of -1 amendments to Senate Bill 867 and the report

Symeonides

Line 22 and 30 may lead to confusion. You may want to add to line 30 a reference that talks about a person who has interest that has been subsequently acquired.

Dobbins

I see, but section B is intended to go to the initial relationship.

Symeonides

Where does it state future owner?

Dobbins

We could borrow language about grantor and subsequent owners.

Symeonides

Use the same language on line 25.

Shetterly


Adjourned at 4:49 pm

Submitted By, Lisa Ehlers
Reviewed By, Wendy Johnson

Lisa Ehlers
Legal Assistant

Wendy Johnson
Deputy Director and General Counsel
EXHIBIT SUMMARY

HB 2541-5

Inheritance Tax Work Group Report

SB 867-1

Uniform Environmental Covenants Act/ Easements & Equitable Servitudes Work Group Report

Uniform Environmental Covenants Act