



Multi-State Update for Service Business Clients

There have been many changes in multi-state taxation for service businesses over the past several years. Starting with 2018 tax years, Oregon has changed the rules for apportioning taxable income between states.

Every business needs to ask themselves if they are doing business in other states. If you are in a service business, you may say to yourself that your business is only in Oregon because your only office is in Oregon, but that may not be the case.

Revenue from services is sourced to a state other than your home state under two general methodologies. The following example illustrates this issue:

Consulting Inc. has one office located in downtown Portland and performs all work in their local offices.

Under the “Cost of Service” methodology, you look to where the revenue producing work is performed, so that revenue is considered to be Oregon revenue since the work was performed in Oregon.

Under the “Market Based” (also referred to as “Economic Benefit”) methodology, you must look to the client and question where the client benefits from the activity. If the client is in California, then that revenue is California sourced revenue because they received the economic benefit of those services in California. Therefore, while you may have believed you were not doing multi-state business, because your client is in a Market Based state you have to deal with the possibility of filing multistate tax returns.

So under these two methodologies, you get exact opposite answers. Currently, over half of the states that have income taxes have adopted the Market Based methodology of sourcing income. Oregon has historically been a Cost of Service state. However, that is changing and starting in tax years beginning on or after January 1, 2018, revenue Oregon will source income using the Market Based sourcing rules. Note that City of Portland/Multnomah County has not yet changed their rules and are using the Cost of Service methodology.

California has been using Market Based revenue sourcing for numerous years, as has Washington State for their B&O (Business & Occupation) tax.

The good news is that some states that have adopted Market Based revenue sourcing have adopted some sort of de minimis rule where you have to have a fairly substantial amount of revenue in that state before you are considered to be subject to taxes in that state. So if your business has clients with activity outside of Oregon, all applicable state revenue sourcing rules must be analyzed keeping your clients in mind to determine your potential multi-state filing requirements.

We can assist you with multi-state analysis and associated tax filings. Please contact us for consultation if based on the above discussion, you have multi-state activity.