



Tax Committee

April 20, 2016

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OMA Tax Committee Meeting Sponsor:





OMA Tax Policy Committee

April 20, 2016

AGENDA

Welcome & Self-Introductions:

Michele Kuhrt, Chairman
Lincoln Electric

Guest Speakers

Carolyn Lee, Senior Director, Tax Policy
National Association of Manufacturers

Pete Turner, Clark Schaefer Hackett

OMA Counsel's Report

Mark Engel, Bricker & Eckler LLP

OMA Public Policy Report

Rob Brundrett, OMA Staff

Please RSVP to attend this meeting (indicate if you are attending in-person or by teleconference) by contacting Denise: dlocke@ohiomfg.com or (614) 224-5111 or toll free at (800) 662-4463.

Additional committee meetings or teleconferences, if needed, will be scheduled at the call of the Chair.

Thanks to Today's Meeting Sponsor:



Carolyn Lee

Senior Director, Tax Policy



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Carolyn Lee is Senior Director of Tax Policy at the National Association of Manufacturers (NAM), the nation's largest industrial trade association. In this role Carolyn is responsible for portions of the NAM's tax portfolio including pass-through taxes, energy taxes and capital cost recovery. Prior to joining the NAM in the fall of 2011, Lee served as the Director of Legislative and Government Affairs at the Telecommunications Industry Association, Manager of State and Federal Government Affairs for 3M Company and in various positions on Capitol Hill including as Legislative Director for former U.S. Senator Olympia Snowe (R-ME), and as a senior legislative staff member for former U.S. Rep. Sue Kelly (R-NY). Carolyn is a graduate of Gettysburg College in Gettysburg, Pennsylvania graduating with a B.A. in Political Science and lives in Northern Virginia with her husband and three children.

Pete Turner, Clark Schaefer Hackett

Biography

Pete Turner is an attorney who has worked in the tax consulting profession in Ohio since 2001. Pete assists clients with complex state and local tax issues involving income and franchise taxes, indirect taxes, and property taxes. His general focus is on return reviews, audit defense, voluntary disclosure agreements, multistate concerns such as nexus studies and sourcing of receipts, and documentation regarding tax planning and filing positions.

Pete also specializes in securing economic development incentives for clients. He has extensive experience with income and franchise tax credits, cash grants, tax abatements, and public financing options. Prior to joining Clark Schaefer Hackett, Pete previously spent 12 years in state and local tax consulting at a national firm.

Education

JD, The Ohio State University College of Law
BA, BBA, Southern Methodist University

Certification & Licensure

Licensed Attorney – Ohio



OBM

April 11, 2016

MEMORANDUM TO: The Honorable John R. Kasich, Governor
The Honorable Mary Taylor, Lt. Governor

FROM: Timothy S. Keen, Director **TK**

SUBJECT: Monthly Financial Report

ECONOMIC SUMMARY

Economic Performance Overview

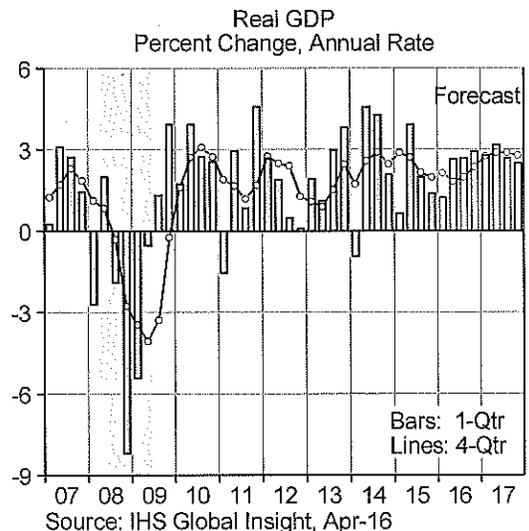
- Fourth-quarter real GDP growth was revised up to 1.4%, compared with 2.0% in the third quarter. Recent economic data indicate that economic growth remained modest in the first quarter.
- Ohio nonfarm payroll employment increased by 12,400 jobs in February and is up by 78,700 jobs over the past 12 months (1.5%). The unemployment rate was unchanged at 4.9%.
- Leading economic indicators weakened further, but continue to point toward uninterrupted economic expansion. Recent data indicate that growth is continuing at a slow pace in the first quarter.

Economic Growth

Fourth-quarter **real GDP** growth was revised up to 1.4% from the previous report of 1.0%, compared with 2.0% in the third quarter and up only 2.0% from the year earlier. At 1.7%, second-half growth was below the average annualized growth rate of 2.1% from the beginning of the current expansion, which has been the weakest of the four post-war expansions that have lasted at least as long as the current one.

The **increase in fourth-quarter** real GDP primarily reflected increases in personal consumption expenditures, residential fixed investment, and federal defense expenditures. Nonresidential fixed investment, exports, private inventory investment, and state and local government spending subtracted from growth during the quarter. Imports, which are automatically included in these individual categories and then subtracted as a separate category, decreased (which is a net positive for GDP).

The **deceleration during the fourth quarter** reflected decreases in nonresidential fixed investment and state and local government spending, a deceleration in personal



consumption expenditures (in goods, not services), and a downturn in exports. The smaller decrease in private inventory investment, the decrease in imports, and the acceleration in federal government defense spending partly offset these negative factors.

Concerns about a near-term recession appear to have abated somewhat among analysts despite the lackluster patterns of **leading economic indicators**. The Leading Economic Index (LEI) from the Conference Board, for example, increased just 0.1% in February after two consecutive monthly decreases and three decreases in the previous five months. Only four of the ten components made positive contributions in the most recent month, led by initial claims for unemployment compensation and the interest rate spread. Yet, on balance, leading indicators still point to uninterrupted expansion.

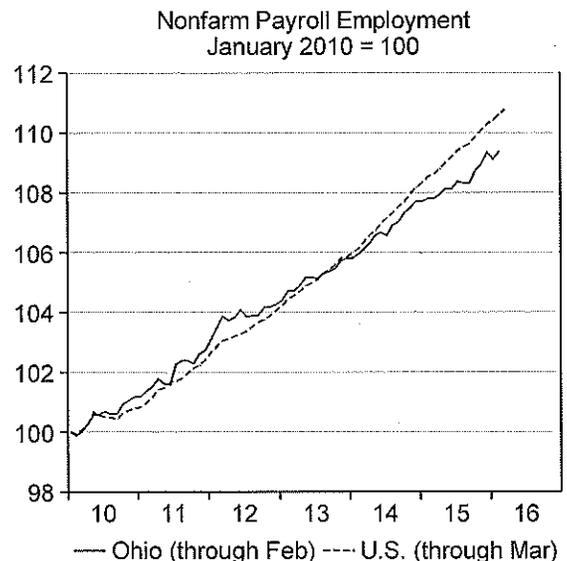
The year-over-year rate of change in the LEI stabilized near 2.3% in the most recent months after an abrupt slowdown from late 2014-early 2015, remaining consistent with continued economic expansion. In contrast, the rate of change in the index regularly has turned negative in advance of recessions in the past. The weakness so far during this cycle appears to be related to manufacturing activity, which has been affected by the strength of the dollar, weaker demand growth overseas, and the sharp pullback in the energy industry. Strength in labor markets and benefits from lower energy costs appear to be bolstering consumer income and spending.

The **consensus of forecasters** is that economic growth will proceed throughout 2016 at a modest pace that is somewhat faster than during the second half of last year. Predictions center on 2.0% for the first quarter of 2016 and 2.5% for the second quarter, according to the Survey of Professional Forecasters (SPF) conducted by the Philadelphia Federal Reserve. A widely followed tracking estimate of GDP that is compiled by the Atlanta Federal Reserve Bank estimated growth of only 0.4% in early April. Many commentators recently have raised concerns about a near-term recession, but the odds of a quarter-to-quarter decline in real GDP were recently deemed to be below 20% by the SPF.

Employment

Labor markets continued to strengthen in March. **U.S. nonfarm payrolls** increased by 215,000 jobs during the month. Employment growth during the two previous months was revised modestly lower. The March increase was roughly in line with expectations. Job growth averaged 228,000 jobs per month during the previous three months. The average job gain per month has been 223,000 for the most recent twelve months, including March.

Employment gains were very widespread **across industries**, led by education and health services (+51,000), where health care and social assistance contributed 44,000 jobs. Also making significant contributions to the increase were retail trade



(+47,700) and leisure and hospitality (+40,000). Notably, construction added 37,000 jobs, marking the seventh consecutive monthly gain of at least 10,000 jobs in that sector.

The only major month-over-month decreases in employment occurred in manufacturing (-29,000) and mining and logging (-12,000). The mining and logging sector, in which employment has declined in each of the most recent eighteen months (with total job losses of 184,000 over that period), continues to be buffeted by the steep decline and low level of energy prices. The decline in manufacturing employment was the second monthly setback in a row, and contradicts other measures of manufacturing activity, such as industrial production and the ISM survey of purchasing managers, which have improved recently.

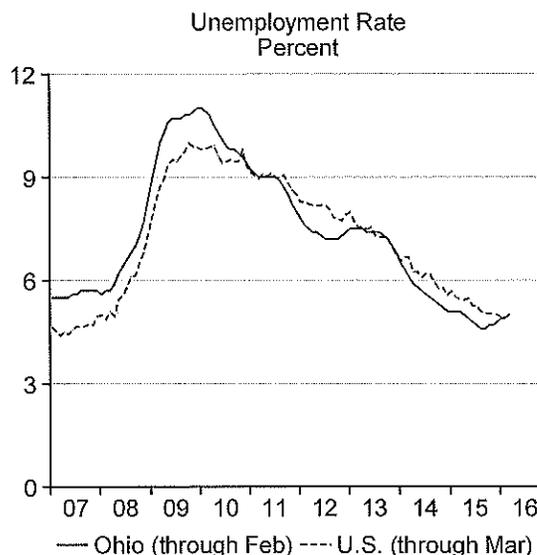
In addition to the monthly employment report, the recent pattern in weekly **initial claims** for unemployment compensation remains consistent with sound labor market fundamentals and an expanding overall economy. The 4-week average of initial claims fell below 260,000 during each of the first three weeks of March, the lowest levels of claims since December 1973. The recent pattern and current level are consistent with a healthy and expanding labor market and overall economy.

The **U.S. unemployment rate** edged higher to 5.0% in March – the first uptick since last May – as a 246,000 increase in the total number of people employed did not keep up with the 396,000 person increase in the labor force. The total number of unemployed people increased by 151,000. The broadest measure of unemployment – the U-6 unemployment rate – also edged higher by 0.1 point to 9.8%. The U-6 unemployment rate includes those who want to work but have stopped looking because they believe they cannot find a job, as well as those working part-time who would prefer full-time work.

Ohio nonfarm payroll employment increased by 12,400 jobs in February, and is up by 2,300 jobs year-to-date. Over the last 12 months, Ohio employment has increased by 78,700. The month-over-month increase was led by trade, transportation, and utilities (+5,800), local government (+5,400), educational and health services (+4,300), and financial activities (+3,900). Nonfarm payroll employment decreased in state government (-2,800), manufacturing (-2,300), and leisure and hospitality (-2,200).

The largest employment gains during the twelve months ended in February occurred in education and health services (+21,800), leisure and hospitality (+17,600), trade, transportation, and utilities (+16,100), and construction (+10,900). The only employment declines year-over-year occurred in mining (-3,200) and professional and business services (-1,700).

Among the **contiguous states**, year-over-year employment growth was strongest in Michigan (+2.2%), followed by Indiana (+1.7%), Ohio



(+1.5%), Kentucky (+1.5%), and Pennsylvania (+0.9%). Employment declined from a year earlier in West Virginia (-1.5%). Year-over-year growth in manufacturing employment was 0.7% in Ohio. Among the contiguous states, manufacturing employment increased 2.2% in Michigan, 1.7% in Kentucky, and 0.1% in Indiana and decreased 0.4% in West Virginia and 1.0% in Pennsylvania.

The **Ohio unemployment rate** was unchanged at 4.9% in February, up from the low for the expansion of 4.6% in September. The number of unemployed people increased by 5,334 in February, while the number of employed people increased by 28,603, and the labor force increased by 33,937 people. If the data is not revised later, the February increase will be the largest one-month Ohio labor force increase in 40 years. The February increase follows a January increase of 25, 845, which was also the highest in 40 years.

Compared with a year ago, unemployment is down by 6,761 people and the number of employed people is up by 54,012, while 47,251 people have joined the labor force. The unemployment rate is down 0.2 percentage points from a year ago, and is less than one-half its peak level of 11.0% reached in January 2010.

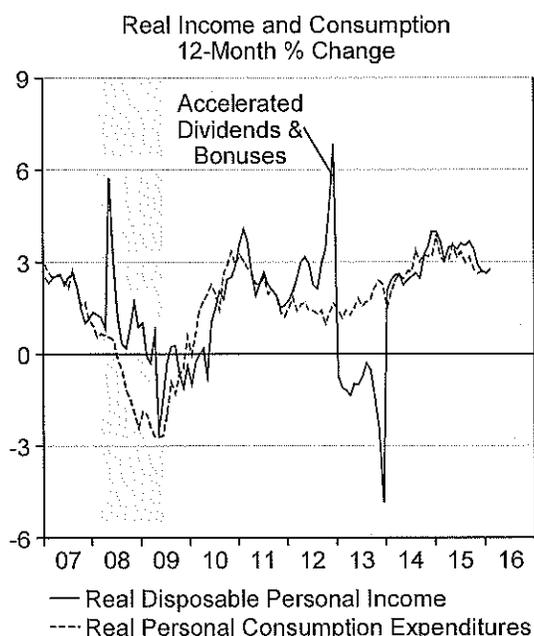
Across the country in February, the unemployment rate decreased by a statistically significant amount in nine states, increased in three states, and was not statistically different from the month before in 38 states. The unemployment rate was lower than a year earlier by a statistically significant margin in 20 states and higher only in Wyoming.

Consumer Income and Consumption

Personal income slowed in February and consumer spending growth remained modest. **Personal income** increased 0.2% after a jump of 0.5% in January and 0.3% in each of the two previous months. **Wage and salary disbursements** – the largest single component of personal income – decreased by 0.1% after a 0.5% increase the month before. Compared with a year earlier, personal income was higher by 4.0% and wage and salary disbursements were up 4.3%.

The slower growth in spending than in income – consumption grew by only 0.1% in February – pushed up the saving rate to 5.4%. The rate recently reached a low of 4.9% in November. Households appear to be using the income freed up by lower gasoline and other energy prices at least partly to pay down debt or increase saving.

Ohio personal income slowed to a 3.5% increase in the fourth quarter, and the third-quarter rate was revised down from 5.5% to 4.0%. Growth in **Ohio wage and salary disbursements** followed the opposite pattern, accelerating to 5.2% in the fourth quarter while third-



quarter growth was revised down from 5.7% to 3.3%. Compared with a year earlier, Ohio personal income was higher by 3.0% and wage and salary disbursements were higher by 2.9%.

Inflation remains low, providing some support to consumer spending. The **Consumer Price Index (CPI)** decreased 0.2% in February after no change the month before, in part reflecting a 13.0% decrease in the price of gasoline. The CPI is unchanged since July and up by just 1.0% from a year earlier. Nonetheless, analysts expect inflation to move higher in coming months as the steep decrease in energy prices that started more than a year ago drops out of year-over-year comparisons.

Excluding the volatile food and energy categories as a means of assessing the underlying trend, the CPI increased 0.3% in February to 2.3% above its year earlier level. The Median CPI from the Federal Reserve Bank of Cleveland – an alternative measure of the trend in inflation – continued to track even higher at 2.4% year-over-year. The measure of inflation that is most closely watched by the Federal Reserve, the personal consumption expenditure (PCE) deflator, excluding food and energy (also known as the “core” PCE deflator) increased 0.1% in February to 1.7% above its year earlier level.

Personal consumption expenditures increased by less than incomes, rising 0.1% in February for the third month in a row. The January gain was revised down from an initially reported increase of 0.5%. Spending on services increased 0.4%, while spending on durable goods increased only 0.1% and spending on non-durable goods fell 1.1% for the third monthly decrease in a row. The increase in spending on durable goods occurred despite essentially no change in the sales pace of **light motor vehicles**. Vehicle sales slid almost one million units at an annual rate in March, telegraphing a likely decrease in spending on durable goods when March data are published. The recent weakness in spending on non-durable goods reflected the lower prices for food and fuel.

Consumer confidence was mixed in March, as the Conference Board measures bounced part of the way back from moderate February declines and the Reuters/University of Michigan measures were little changed from February. The apparently temporary weakness during February might have been in part related to the steep decrease in stock prices through mid-month, which has since fully reversed. In general, consumer confidence indexes are at relatively high levels that are consistent with sustained growth in consumer spending in the months ahead.

Manufacturing

Manufacturing activity showed signs of firming in the first quarter, even as the headwinds from the stronger dollar, slower growth in foreign economies, and lower energy prices remain. Recent economic trends are consistent with overall economic expansion and possibly a modest strengthening in manufacturing activity as the year unfolds.

Industrial production decreased 0.5% in February after a 0.6% increase in January, reflecting modest gains in manufacturing that have been swamped by large weather-related and energy-price-related effects. **Mining output** decreased 1.8% in February for the sixth straight monthly decline. **Utility output** decreased 4.1% in February after a 4.0% increase in January – both

related to weather. **Manufacturing output** posted a modest increase of 0.1% following a 0.4% gain in January to only 1.0% above the year earlier level. Industrial production data were revised back to 1972 based on newly available source data, lowering rates of change during 2011-2015, especially in 2014 and 2015.

Reports from **purchasing managers** improved encouragingly during March. The PMI[®] increased by 2.3 points to 51.8 – the first reading above the neutral 50 level since last August. The New Orders index jumped from 51.5 to 58.3, in part reflecting the better reading on New Export Orders, which increased from 46.5 to 52.0. The Production index increased from 52.8 to 55.3, reaching its highest level since January 2015. The Backlog of Orders Index and Supplier Delivery Index both edged above neutral.



Despite the improvement in manufacturing conditions reported by purchasing managers, follow-through in subsequent months will be necessary to draw the conclusion that the lull in manufacturing is drawing to a close. The volatile New Orders Index account for more than one-half of the increase in the PMI[®], and manufacturing payroll employment decreased in March for the second consecutive month, suggesting that employers might see a different picture. In addition, factory shipments fell in February for the eighth month in a row, while new orders declined for the fifth month out of the last seven.

Of the 18 industries tracked by the Manufacturing ISM[®] *Report on Business*, twelve reported growth in March. Among the industries with a disproportionate effect on Ohio manufacturing employment, the machinery, fabricated metal products, and primary metals industries expanded, according to purchasing managers. Activity in the transportation equipment industry contracted. One respondent in the machinery industry noted that “requests for proposals for new equipment [are] very strong.” A representative of the primary metals industry reported that “business is still going strong,” and a purchasing manager in fabricated metal products said that “capital equipment sales are steady.”

Analysts anticipate that the recent rebound in the price of oil and the depreciation of the dollar will support manufacturing activity increasingly as the year progresses unless those trends reverse.

Construction

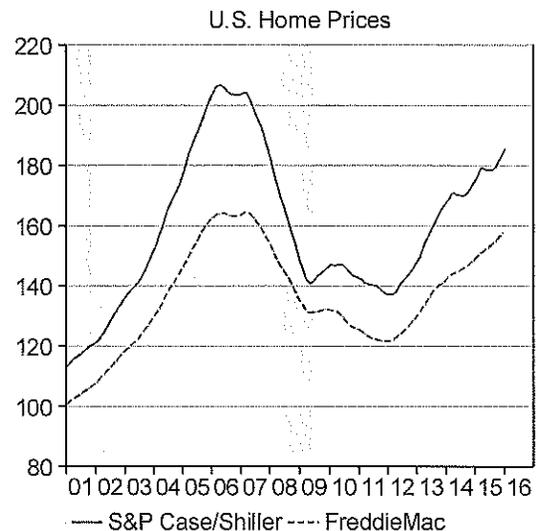
Construction put-in-place retreated by 0.5% in February, but the January gain was revised upward from 1.5% to 2.1%. Private construction decreased 0.1% while public construction decreased 1.7%. The setback in total construction put-in-place primarily reflected decreases in both private and public non-residential construction put-in-place

Private nonresidential construction put-in-place decreased 1.3% in February for the third monthly decline in four months. Large declines in manufacturing and commercial construction were only partly offset by increases in office, education, and health care construction. Compared with a year earlier, activity was 10.6% higher. **Private residential** construction put-in-place increased 0.9% in February, reflecting a 1.2% increase in single-family and a 0.9% increase in multi-family. Improvements increased by 0.5%. Compared with a year earlier, activity was higher by 10.7%.

Housing starts edged higher by 0.1% in February on a 3-month moving average basis after a 1.4% increase in January that was revised higher from 0.8%. A 3.0% decrease in multi-family starts essentially offset the 1.6% rise in single-family starts. Midwest starts increased 2.7% in February and the January decline was revised higher from -7.4% to -4.3%. Single-family starts were very strong in February (+13.1%) and multi-family starts were very weak (-24.6%).

Housing permits dropped 2.8% in February on a 3-month moving average basis, reflecting a 7.6% drop in multi-family permits, which more than offset a small rise in single-family permits. Permits in the Midwest followed the same pattern, with a large decline in multi-family permits swamping a moderate rise in single-family permits.

Existing home sales and **new home sales** were lackluster in February, both in the Midwest and across the country. Inventories of homes for sale remained in line with the current pace of sales. The **Pending Homes Sales Index** – which measures housing contract activity for single-family homes, condos, and co-ops, and usually leads existing home sales by a month or two – moved modestly higher in February both across the country and the Midwest.



Home prices across the country posted their 48th consecutive increase in January, rising by 0.5% to 5.4% above the year earlier level, according to the Case-Shiller index. The rate of increase picked up markedly in the second half of last year. The pattern of the FreddieMac home price index has been similar, rising 6.2% during the year ending in December.



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BRICKER & ECKLER LLP

201 East Fifth Street
Suite 1110
Cincinnati, OH 45202
MAIN: 513.870.6700
FAX: 513.870.6699

www.bricker.com
info@bricker.com

Mark A. Engel

513.870.6565
mengel@bricker.com

Ohio Manufacturers' Association

Tax Counsel Report

April 20, 2016

By Mark A. Engel
Bricker & Eckler LLP

Administrative Actions:

The Department revised Information Release ST 1999-04 – *On-line Services and Internet Access* – January 1999, Updated December 2015, supposedly to provide examples of transactions that would be viewed as electronic information services that are subject to sales tax. The transactions are claimed to be based upon actual audit situations. Perhaps the provision that has generated the greatest amount of conversation is the discussion about advertising services on page 3 of the release. In light of the fact that advertising has historically been viewed as a personal or professional service that is not subject to tax, the position that on-line advertising is subject to tax seems to be an end-around on that position. A copy of the Release is attached. In response to this position, H.B. 466 has been introduced that would specifically include electronic advertising as one of the examples of professional services that are not taxable electronic information services.

The Department revised Information Release ST 2003-01 – *Direct Payment Authority Program* – March 2016, which supersedes the original release in December 2004. It provides an updated summary of the direct payment permit program in question and answer format.

Legislative Actions:

House Bill 235 proposes an exemption from real property taxation for “newly developable property” and “redevelopment property” between certain triggering dates and the dates on which development of the properties begins. “Newly developable property includes property included in a plat for the subdivision of land on which construction of one or more commercial or industrial buildings or structures is planned, but has not yet commenced. “Redevelopment property” means a parcel on which one or more commercial or industrial buildings or structures are located, no operations are currently being conducted, and construction or reconstruction of new buildings or structures are planned but not yet commenced. The exemptions begin when either the plat is approved, or the owner of the building or structure when operations most recently ceased transfers title to another, and lasts until the year prior, or the year in which, construction begins.

House Bill 491 provides for a credit against the CAT for certain amounts spent in (i) workforce hiring or training, (ii) capital investment, or (iii) undertaking

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initiatives to increase exports of goods or services produced, all at a location in an activated foreign trade zone.

Senate Bill 288 substantially revises the taxation of pass-through entities and their owners who are not residents in the state of Ohio. Please see the summary attached to this report.

Judicial Actions:

Ohio Supreme Court

In *Copley-Fairlawn City Sch. Dist. v. Summit Cty. Bd. of Revision*, Slip Op. No. 2016-Ohio-1485, the Court held that where a BOR changed the value of property based on an appraisal report, it was error for the BTA to ignore the report and revert to the auditor's valuation where the report was prepared for financing purposes, opined a value as of a date other than tax lien date, and for which the appraiser did not testify. The Court noted the appraisal was prepared for business purposes and was relied upon by the parties for those purposes. Since the BOR had determined value based upon the report, the BTA should have used the evidence, including the report, to make an independent determination of value.

In *Rural Health Collaborative v. Testa*, Slip Op. No. 2016-Ohio-508, the Supreme Court rejected an argument of the Tax Commissioner that a real property exemption case involving land owned by a kidney dialysis clinic that was a lessee of a different property, in a different tax year, was not "controlling precedent" for the current case. The BTA had reviewed the record in the current case and reached a different conclusion as to the exempt nature of the clinic lessee. The Supreme Court agreed that in a new case, the BTA had to base its decision on the record presented in the current case, rather than be bound by the prior case. On remand, the BTA determined that the entity using the property was not a charitable institution and denied the exemption.

In *Columbus City Schools Bd. of Edn. v. Franklin Cty. Bd. of Revision*, Slip Opinion No. 2016-Ohio-757, the Court held that the testimony and written report of an appraiser that contained information of changes in the general market could be used to rebut the presumption that the price paid in a sale of the property, occurring two years prior to tax lien date, was recent. In this case, the appraiser was able to point to sales of properties that actually demonstrated changes in the market during the interim period.

In *ShadowArt Productions, Inc. v. Testa*, Slip Opinion No. 2016-Ohio-511, the Court held that while R.C. 5715.27 permitted a lessee under a 30-year lease to file an application for exemption for real property, the strictures for an exemption that apply to an owner still apply. Thus, where the owner of the property was a for-profit entity, the property was not entitled to a charitable use exemption notwithstanding the fact the lessee may have been a charitable entity.

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In *Veolia Water North America Operating Service, Inc. v. Testa*, Slip Opinion No. 2016-Ohio-756, the court affirmed the BTA and Tax Commissioner in finding that only a portion of a water pollution control facility qualified for exemption. The facility treated both residential and industrial effluent. By flow, industrial use made up only 17 percent of the pollution treated at the facility. Therefore, the Court rejected the argument that the entire facility was intended to be used for industrial water pollution control, and affirmed the decision to examine each separate piece of equipment to see whether it qualified for exemption.

Ohio Court of Appeals

Nothing to report.

Ohio Board of Tax Appeals

In *Lexmark International, Inc. v. Testa*, BTA No. 2014-3669 & 3771 (Dec. 23, 2015), the BTA struck down most of a motion filed by the Tax Commissioner to quash certain subpoenas. The Tax commissioner argued the subpoenas were overbroad and burdensome and had been issued for an improper purpose. The BTA noted that some of the subpoenas were issued to individuals that the Tax Commissioner had identified as knowledgeable about the issues in the case. Another subpoena was held to be over-broad with respect to documents that were requested, but appropriate as to compelling a witness to testify generally about the subject matter.

In *Hilliard City Schools Bd. of Edn. v. Franklin Cty. Bd. of Revision*, BTA No. 2015-530 (Feb. 8, 2016), the BTA held that a sale subject to a number of contingencies that were not fulfilled until after tax lien date was too remote to establish the value of the property.

In *Columbus City Schools Bd. of Edn. v. Franklin Cty. Bd. of Revision*, BTA No. 2015-408 (Feb. 9, 2016), the BTA held that a sale through bankruptcy was forced sale that did not establish the value of the property. Therefore, where the BOR erroneously reduced value based upon that sale, it was proper to reinstate the auditor's original valuation.

In *Columbus City Schools Bd. of Edn. v. Franklin Cty. Bd. of Revision*, BTA No. 2015-369, the BTA held that it was property to determine the percentage of completion for a property under construction with reference to the testimony of an appraiser, rather than merely based on the AIA payments made in relation to the total contract price. The appraiser explained how he arrived at his calculation and the BOE failed to demonstrate that the portion of the payments made was a better indicator of value. *See also Residences at Riverpointe Place LLC v. Franklin Cty. Bd. of Revision*, BTA Nos. 2014-4846 and 4862 (January 22, 2016).

In *Easy Stop I Inc. v. Franklin Cty. Bd. of Revision*, BTA No. 2014-4962 (Feb. 26, 2016), the BTA held that oral testimony that the acquisition of real estate included the acquisition of the

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inventory and equipment of an on-going business, together with an appraisal of the real estate, was sufficient to overcome the presumption that the price paid for the property was its value.

Tax Commissioner Opinion

No opinions to report.

Other

In *McLane/Midwest, Inc. v. Ohio Dept. of Taxation*, Case No. 14CVH09-9159 (March 28, 2016), the court of common pleas over-ruled motions of the Department to dismiss a declaratory judgment brought by Plaintiffs to declare the Ohio Unfair Cigarette Sales Act inapplicable to its sales of cigarettes to another wholesaler. The Court ruled that it had jurisdiction to hear a declaratory judgment action; that Plaintiffs were not required to exhaust their administrative remedies, that there was a justiciable controversy between the parties, and that there was no equally serviceable remedy available to Plaintiffs.

The Economics Center of the University of Cincinnati prepared a study indicating the benefits of Ohio's experimental three-day sales tax holiday for back to school purchases. The study, performed at the request of a group supporting the holiday, concluded that over-all retail sales increased by 6.45 percent, and that Ohio experienced an increase in sales tax revenue for the month (August 2015) of about \$8 million, while foregoing about \$3.3 million in excepted goods during the holiday. It also concluded that border counties experienced an increased collection of 15.48 percent in local sales tax revenues, which it attributed to residents of adjacent states coming to Ohio to take advantage of the holiday.

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Ohio S.B. 288 Proposes to Change Taxation of PTEs and Their Owners

By Mark A. Engel, Esq.
Bricker & Eckler LLP

Under current law, pass-through entities (PTEs) and their owners are subject to multiple and varied tax filing and payment provisions. Senate Bill 288 proposes to require all PTEs to file either a composite return or an informational return, and to make tax payments with respect to certain owners included in the composite return. The bill also changes the rate at which tax is computed. If enacted, the changes made by the bill would apply to taxable years ending on or after January 1, 2017.

Under current law, PTEs may elect to file a composite return on behalf of their nonresident owners pursuant to R.C. 5747.08(D). PTEs not making that election must withhold from distributions paid to their nonresident owners and pay a tax on those distributions. In both cases, while the individual owner may claim a credit for any tax paid on its behalf if it files an individual return, the applicable tax rates are 4.997 percent in the case of a composite return, and 5 percent in the case of the withholding tax. On neither return may the PTE take advantage of the \$250,000 business income deduction.

S.B. 288 attempts to simplify the filing process and reduce the cash implications to the individual owners. The composite return provisions of R.C. 5747.08(D) are repealed, as are the existing provisions of R.C. 5747.40 through 5747.43 relating to the withholding tax. In their place, new R.C. 5747.41 provides that all PTEs having nexus with this state must file a composite return on behalf of its investors and compute and pay the tax due unless either all the investors in the PTE are residents, or none of the investors is either (i) a PTE, or (ii) a person otherwise subject to the personal income tax. In addition, each PTE having nexus with this state shall file an informational return unless (x) the PTE is required to file a composite return; (y) none of the investors is subject to the personal income tax; or (z) all the investors are resident individuals and the entity did not claim any business credits. Each return must contain identifying information for each investor, investor ownership and distribution percentages, whether the investor is exempt from certain calculations (detailed below), the allocation percentages of any business credit earned by the PTE, and any other information required by the tax commissioner.

Any nonresident individual investor included on a return may still file an individual return, and no resident individual investor is excused from filing an individual return by virtue of being included on the PTE return.

In the case of a composite return, the PTE must compute the tax due with respect to its director investors that are PTEs, estates, trusts, or nonresident individuals. As set forth in new R.C. 5747.40(A), the PTE starts with the distributive shares of each investor, and then makes a number of adjustments. These adjustments include expenses or losses related to transactions

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involving related members; guaranteed payments and compensation made to investors who, at any time during the taxable years owned at least 20 percent of the ownership interest of the PTE; interest, and dividends associated with various obligations that are otherwise exempt from federal taxation; and gains or losses resulting from the sale or exchange of public obligations. The result is then multiplied by the rate applicable to taxable business income in R.C. 5747.02(A)(4)(b).¹

Investors included on the composite return are not entitled to the personal exemption, and may claim a distributive share of the business tax credits specified in R.C. 5747.40(D) and (E). This provision is no different from existing law.

If an investor provides documentation to the PTE that the investor is neither subject to the personal income tax, nor is a PTE, the PTE is not required to include these calculations for that individual on the return. If a PTE receives that documentation and provides it to the tax commissioner, then the PTE is not subject to any interest or penalties for failing to include amounts relating to that investor on the return or its payment of estimated taxes. Under proposed R.C. 5747.41(D), however, a PTE is subject to any additional tax, penalties and interest if the tax commissioner finds the PTE has not reported or paid the correct tax of the investors included on the return. This provision does not excuse any investor from payment of the tax owed by that investor.

Proposed R.C. 5747.42 provides that a PTE shall make payment of any tax by means of a single check, provided that no payment is required if the total tax due is \$250 or less. The PTE must also make estimated payments, and any investor included on the composite return may claim a refundable credit for the tax paid on its behalf.

Proposed R.C. 5747.43 provides that a PTE is not excused from filing returns and paying the tax if it retires from business or dissolves. In addition, if a PTE sells its business or stock of merchandise, or quits its business, any taxes required to be paid prior to that time are immediately due and payable and a final return must be filed within 30 days after the filing due date of the entity's final federal tax return.

There are other minor conforming revisions made by the law. One of the more significant such changes involves the amendment of R.C. 5747.21 and its allocation and apportionment provisions. Under current law, reference is made to the provisions contained in the franchise tax chapter. The bill eliminates the reference and expressly incorporates all the language previously found under the franchise tax law.

¹ The bill makes reference to the rate found in division (A)(2)(b) of section 5747.02; this reference appears to be in error.

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Similarly, the bill expressly incorporates the definition of a PTE that was previously found in the franchise tax law. The definition includes a subchapter S corporation, or a partnership, limited liability company or any other person other than an individual, trust, estate, or disregarded entity if the corporation, partnership, LLC, or other person is not taxed as a corporation for federal income tax purposes.

It does not appear that a PTE filing a composite return is entitled to consider the business income deduction provided by R.C. 5747.01(A)(29)(b) (formerly division (A)(31)(b)) in the calculation of the tax liability of investors included on the return.

If passed, the provisions would be effective with any taxable year ending on or after January 1, 2017.

TO: OMA Tax Policy Committee
FROM: Rob Brundrett
SUBJECT: Tax Public Policy Report
DATE: April 20, 2016

Overview

Major tax issues will not be considered in the near term. The General Assembly is largely focused on a new capital bill and a medical marijuana bill which were both recently introduced. The Governor indicated in his state of the state address that he would continue to pursue major income tax changes during the remainder of his term. The Senate President indicated that the state may need to fill a budget deficit of \$600 million due to federal dollars disappearing. This could be a major issue in the next state operating budget.

State Financial Condition

Fourth quarter real GDP growth was revised up to 1.4%, compared with 2.0% in the third quarter. Recent economic data indicate that economic growth remained modest in the first quarter.

Ohio nonfarm payroll employment increased by 12,400 jobs in February and is up by 78,700 jobs over the past 12 months (1.5%). The unemployment rate has moved up to 5.1%. This is due to more people entering the workforce after sitting out much of the past few years.

Leading economic indicators weakened further, but continue to point toward uninterrupted economic expansion. Recent data indicate that growth is continuing at a slow pace in the first quarter.

Tax Legislation

2020 Tax Policy Study Commission

The Study Commission continues to hold monthly hearings to discuss the various aspects of Ohio's tax climate. The OMA has testified twice before the committee. First the OMA testified on general tax conditions and impacts on manufacturing. The second time, the OMA testified specifically on tax credits.

The Study Commissions plans to have some recommendations for the next budget. The OMA tax committee should consider providing a white paper to the Study Commission with its suggestions and observations.

House Bill 9 – tax expenditure review committee

HB 9 was introduced by Representative Boose (R-Norwalk). The bill creates a Tax Expenditure Review Committee that would periodically review existing and proposed tax expenditures. The Senate had a watered down version of this committee operate during the budget process. The OMA testified several times in front of the committee to discuss why certain tax expenditures were important and why others should be removed from Ohio's tax code. The bill had its third hearing in the Senate in February.

Senate Bill 88 – CAT credit

Sponsored by Sen. Charleta Tavares (D-Columbus) would create tax credits, including CAT credits, for the employment of individuals who have been convicted of criminal offenses. The bill has not had any hearings. Nor is it expected to move.

House Bill 102 – CAT credit

House Bill 102 sponsored by Reps. Niraj Antani (R-Miamisburg) and Hearcel Craig (D-Columbus), would provide a bid preference for state contracts to a veteran-owned business and would have authorized a personal income and CAT credit for a business that hires and employs a veteran for at least one year. However the sponsors introduced a substitute version of the bill at its first hearing removing the CAT provisions from the bill. The bill only received a first hearing for sponsor testimony last year.

House Bill 176 – CAT credit

House Bill 176 sponsored by Reps. Hall (R-Millersburg) and O'Brien (D-Bazetta) creates the Gaseous Fuel Vehicle Conversion Program. The bill allows a credit against the income or commercial activity tax for the purchase or conversion of alternative fuel vehicle. It reduces the amount of sales tax due on the purchase or lease of a qualifying electric vehicle by up to \$500. It applies the motor fuel tax to the distribution or sale of compressed natural gas. The bill also authorizes a temporary, partial motor fuel tax exemption for sales of compressed natural gas used as motor fuel. The bill was introduced in the previous General Assembly, but stalled in the legislative process. Earlier this year it was passed out of House Ways and Means Committee. The bill was re-referred to Finance Committee and voted out of committee last November.

House Bill 182 – JEDDs reorganization

House Bill 182 sponsored by Representative Schuring (R-Canton) would revise the law governing the creation and operation of joint economic development districts (JEDDs) and enterprise zones. Amongst the changes the bill establishes a procedure permitting the owner of a business operating in the unincorporated territory of a JEDD to apply for exemption from the JEDD income tax on behalf of the business and its employees. The bill passed the House in February and is waiting its first hearing in Senate Ways and Means Committee.

Senate Bill 198 – non-resident municipal income tax

SB 198 was introduced by Senator Jordan (R-Ostrander). The bill prohibits municipal corporations from levying an income tax on nonresidents' compensation for personal services or on net profits from a sole proprietorship owned by a nonresident. This bill has opposition from Ohio's cities and villages. The bill had one hearing last fall. It is not expected to move.

Senate Bill 208 / House Bill 326 – budget income tax correction bills

The House and Senate passed a corrections bill in the fall that repaired an error in the business tax deduction passed in the state budget last summer.

The intent was to help small businesses reduce their taxes by creating a 75% income tax deduction on the first \$250,000 of pass-through business income, then charge a 3% flat tax on income greater than \$250,000. But the budget bill language did not match the intent and would actually cause a tax increase for some businesses.

Companion bills SB 208 and HB 326 were drafted to correct the error.

Unfortunately for the CAT the bills included a provision that allows one integrated supply chain in the state an exemption from the commercial activity tax. The tax continuous to be under assault from individuals attempting to get special tax treatment in Ohio.

House Bill 232 – seller use tax collection

HB 232 was introduced by Representatives Grossman (R-Grove City) and Scherer (R-Circleville). The bill prescribes new criteria for determining whether sellers are presumed to have substantial nexus with Ohio and therefore required to register to collect use tax to allow sellers presumed to have substantial nexus rebut that presumption, and to require a person, before the person enters into a sale of goods contract with the state, to register, along with the person's affiliates, to collect use tax. The bill has not had a hearing.

Senate Bill 235 – increased value property tax

Senate Bill 235 was introduced by Senators Beagle (R-Tipp City) and Coley (R-Liberty Township) and would exempt from property tax the increased value of property on which industrial or commercial development is planned until construction of new commercial or industrial facilities at the property commences. The bill has had several hearings and is supported by local chambers of commerce.

Senate Bill 246 / House Bill 398 – change the CAUV computation

Senator Hite (R-Findley) and Representative Hill (R-Zanesville) introduced companion bills to require that the computation of the capitalization rate for the purposes of determining CAUV of agricultural land be computed using a method that excludes appreciation and equity buildup and to stipulate that CAUV land used for a conservation practice or enrolled in a federal land retirement or conservation program for at least three years must be valued at the lowest of the values assigned on the basis of soil type.

The bill is proving to be controversial due to the fact that agriculture land is already taxed at a reduced rate compared to residential and commercial property.

Senate Bill 264 / House Bill 454 – permanent holiday sales tax

Last year Ohio passed a pilot project to exempt sales tax during one week of back to school shopping. There is interest in making that a permanent tax break. The Ohio Senate quickly passed its version earlier this year.

Senate Bill 288 – income tax for pass through entities reform

SB 288 was introduced by Senator Eklund (R-Munson Township). The bill revises the law governing how taxes on income from pass-through entities is to be reported and paid by the entities and their investors. The bill has had one official hearing.

Senate Bill 289 / House Bill 475 – increase the motion picture tax credit

The motion picture tax credit companion bills sponsored by Senator Patton (R-Strongsville) and Representative Schuring (R-Canton) would expand the current motion picture tax credit. The bills would be applied against the current credit against the commercial activity tax.

Senate Bill 310 – capital appropriations

SB 310 was introduced by Senator Oelslager (R-Canton). The capital bill is expected to move quickly. It is scheduled to leave the Senate this week after only one week of

hearings. It is expected to have strong bi-partisan support. The bill provides funding for capital projects across the state and in all the legislative districts.

House Bill 343 – remove sale tax on temp employees

HB 343 was introduced by Representatives Romanchuk (R-Mansfield) and Young (R-Leroy Township). The bill would exempt employment services and employment placement services from sales and use tax.

This is a priority tax issue for manufacturers who in Ohio must pay sales tax on their temporary employees. The OMA has strongly advocated for this tax relief for manufacturers over the past two budget cycles.

The bill has had seven hearings and continuous to run into opposition from both local government and social advocates. There is resistance among some Republicans on the committee to pass the bill. Taxation continues to argue against any more tax credits. The OMA is continually looking for opportunities to advance the manufacturing portion of the bill.

The OMA and members Whirlpool and Cargill testified in support of the measure last fall.

House Bill 355 – employee misidentification

Rep. Wes Retherford (R – Hamilton) has introduced a bill, HB 355, that would turn the Bureau of Workers' Compensation (BWC) into an agency that would police businesses in their classifications of employees and independent contractors.

Under the bill, the BWC would be authorized to enter and inspect all of the offices and job sites maintained by an employer who is the subject of a complaint that an employer is misclassifying an employee. The BWC would be authorized to issue stop work orders and fines.

For many many years, organized labor has attempted to create a de facto Department of Labor at the state level. That's what this one is after. It is a really bad idea.

There have been two interested stakeholder meetings regarding the bill. The OMA has weighed in on several occasions regarding the provisions in the bill.

House Bill 394 – unemployment compensation reform

HB 394 was introduced last November by Representative Sears (R-Monclova Township). The bill is a priority for the OMA and its business community allies. Ohio is one of two states that continue to carry debt owed to the federal government due to its insolvent unemployment trust fund. The bill offers a balanced package of reforms to pay off the debt and build solvency in the system to prevent another major solvency issue in the next recession.

The bill has had multiple hearings in the House Insurance Committee. The OMA and its business allies hired a national expert to testify and set the record straight regarding the provisions of the bill to the General Assembly.

House and Senate leaders have established a six person work group to tackle the issue with a promise of passing the bill in the lame duck session after the elections.

House Bill 467 – unemployment compensation debt

HB 467 was introduced by Representative Butler (R-Oakwood). The bill establishes a loan from the Budget Stabilization Fund to the Unemployment Compensation Fund, to require the Director of Job and Family Services to recommend a program to incentivize the purchase of private unemployment insurance, and to require a study on the solvency of the Unemployment Compensation Fund. However, while the bill finds a way to pay off the debt prior to November 2016, it does nothing to address the long term solvency issues of the fund. The bill had its first hearing this week.

House Bill 473 – utility service tax levy

HB 473 was introduced by Representative Amstutz (R-Wooster). The bill would require voter approval before a county may levy a new utilities services tax among other issues. The bill is in response to a controversy that occurred in Hamilton County when the commissioners attempted to legally levy the tax without the input of the voters.

House Bill 491 – CAT tax credit pilot program

HB 491 was introduced by Representative Anielski (R-Walton Hills). The bill creates a five-year pilot program whereby taxpayers with facilities in this state with activated foreign trade zone status may claim a nonrefundable commercial activity tax credit equal to the amount redeployed by the taxpayer to job creation or other specified projects.

Tax News

Tax Foundation Rankings – Ohio 19th in State & Local Tax Rates

According to recently released data from the Tax Foundation, Ohio's combined state and local tax rate is 7.14%. That ranks us 19th among the states (higher ranking = lower rates).

The highest rate in the land? Tennessee at 9.46%. The lowest? Alaska at 1.78%.

The foundation calculates a population-weighted average of local sales taxes as of January 1, 2016 in an attempt to give a sense of the average local rate for each state.

CAT Amicus

The OMA worked with allies in filing an amicus brief on behalf of the state. The issue revolves around three online/catalogue retailers who have failed to pay CAT although they do business in the state of Ohio. The coalition is producing a brief outlining the importance of the CAT to Ohio and Ohio businesses. A real threat exists if these types of companies are excluded from the CAT; the base erodes and more pressure is put on the low rate, resulting in a possible rate increase. These cases have now been scheduled for oral argument on May 3, 2016.

Navistar Amicus

Earlier this summer the Ohio Supreme Court issued a decision favorable to businesses, (Navistar v. Testa), finding that the deadline for notifying the Tax Commissioner of the amount a taxpayer intended to claim as a credit against the commercial activity tax (CAT) for net operating losses (NOLs) accrued under the former franchise tax, did not preclude the tax commissioner from adjusting the amounts reflected in the notice.

However the Board of Tax Appeals must consider all the evidence, including that submitted by the taxpayer, in determining whether an error was made.

The OMA filed an amicus brief with the court. The court used much of the OMA's analysis set forth in its amicus brief in its written decision, which signals a win ultimately for manufacturers.

This was an important case regarding the CAT, and the OMA's involvement factored into the outcome.



**BEFORE THE 2020 TAX POLICY STUDY COMMISSION OF THE OHIO GENERAL
ASSEMBLY**

SENATOR BOB PETERSON AND REPRESENTATIVE JEFF MCCLAIN

CO-CHAIRMEN

**TESTIMONY
OF
MARK ENGEL
BRICKER & ECKLER LLP
OMA TAX COUNSEL**

JANUARY 20, 2016

Mr. Chairman and members of the Committee, my name is Mark Engel. I'm the Partner in charge of Bricker & Eckler's Cincinnati-Dayton office; my practice is focused on taxation issues, with concentrated experience in all aspects of state and local taxation, including tax planning, compliance, and litigation in sales and use, income, commercial activity, public utility, and property taxation as well as economic development. I also serve as tax counsel for The Ohio Manufacturers' Association (OMA). I'm testifying today on behalf of OMA. The OMA was created in 1910 to advocate for Ohio's manufacturers. Its mission is to protect and grow Ohio manufacturing.

For Ohio to be successful in a global economy, the state's tax structure must encourage investment and growth and be competitive nationally and internationally. A globally competitive tax system is characterized by (a) certainty, (b) equity, (c) simplicity and (d) transparency. Economy of collections and convenience of payment also are important considerations.

Generally, manufacturers support efforts to broaden the business tax base, which enables lower rates. To preserve the integrity of the broad tax base and ensure fairness, credits and exemptions should be reduced and discouraged. The objects of taxation must be clearly defined. Where needed, government incentives are best structured as grants rather than as tax credits. And, in general, earmarking and dedicating general tax revenues to specific purposes should be discouraged.

It is poor tax policy to single out any one segment of the economy or group of taxpayers to bear the cost of tax relief for the general population. Similarly, except to resolve existing inequality, or in cases of other policy imperatives, Ohio tax policy should not create a windfall for any group of taxpayers at the expense of other groups of taxpayers.

Compliance and administration of any tax should be as simple and inexpensive as possible for taxpayers and tax administrators alike.

Good tax policy also generates necessary revenues to support the essential functions of government. To ensure transparency regarding the true cost of government and the rate of its growth, however, funding government programs with fee revenue instead of general fund revenue should be discouraged. Good budgeting and spending restraint at all levels of government are vital to ensure a competitive tax environment.

Major tax reforms approved by the Ohio General Assembly in 2005 and additional reforms from 2011-2015 have led to significant improvements to a tax system that was for many years widely regarded as outdated. Reforms included reducing overall tax rates, eliminating tax on investment, broadening the tax base, providing more stable and predictable revenues, and simplifying compliance.

The elimination of the tangible personal property tax, the corporate franchise tax, and the estate tax has strengthened the competitiveness of Ohio's tax system. So has the reduction of the personal income tax rate as well as the creation of a broad-based, low-rate commercial activity tax.

2005 Tax Reform

Prior to 2005, Ohio's tax structure was essentially unchanged since the 1930s. At that time, Ohio's economy was driven by agriculture and manufacturing. Its tax structure reflected that economy. The major taxes were the real property tax, the sales and use taxes, the tax on tangible personal property used in business, and the corporation franchise tax measured on net worth. However, the franchise tax and the tangible personal property tax, especially, both hit capital-intensive industries harder than others and had to be paid whether the entity made, or lost, money. Thus, the manufacturing sector paid an inordinately high level of state tax when compared with other segments of the economy.

As services made up a larger share of Ohio's economy over the years, the inequality in the state tax burden between manufacturing and other segments of the economy was exacerbated. Many service sector concerns operate without a significant investment in capital; hence, their tangible personal property and net worth franchise tax liabilities were minimal. Many of these services can manipulate their finances to minimize income; as a result, little income tax was generated. In addition, many of these new service entities were organized as pass-through entities that were not subject to the franchise tax. As the demand for state services grew, the only recourse was to raise existing tax rates on existing taxpayers. In many cases, that meant an increasing tax burden for Ohio manufacturers.

Paradoxically, Ohio continued to add exemptions from, and exceptions to, the various taxes during this time. As a result, Ohio was saddled with a number of taxes that had high nominal rates, but struggled to raise sufficient levels of revenue for governmental operations. The discrepancies between taxpayers and economic segments also increased and compliance with the existing taxes became more complicated.

Calls for Reform

During the 1960s, calls for reform in Ohio's tax structure began. Over the years, various band aids were applied to Ohio's tax structure in order to attempt to reduce its inequalities. At the same time, Ohio continued to enact exemptions from, or exceptions to, the various taxes, thereby creating increasing disparity and complexity.

With the dawn of a new millennium, calls for tax reform increased. Dr. Ned Hill of Cleveland State University independently conducted a study that examined the impact of state tax policy on Ohio's economy and called for the elimination of the tangible personal property tax and existing dual-based franchise tax, to be replaced with a broad-based, low-rate tax based on payroll. The study demonstrated how capital-intensive segments of the economy, such as manufacturing, construction, and mining, paid anywhere from three to 11 times more state taxes than did members of many service industries.

Tax Reform Enacted

Finally, in early 2005, true tax reform was proposed. The goals of tax reform were:

- Eliminate tax on investment and shift to the taxation of consumption;

- Broaden the over-all business tax base;
- Reduce over-all business tax rates;
- Provide a more stable and predictable flow of revenue; and
- Simplify compliance.

The result was a comprehensive overhaul of Ohio's tax system by H.B. 66. As enacted, the bill:

- Eliminated the tangible personal property tax on new investment in manufacturing and phased out the tax on all general business property over 4 years;
- Phased out the corporation franchise tax for most corporations over 5 years;
- Phased in a 21 percent reduction in personal income tax rates ratably over 5 years (the last reduction was delayed 2 years in 2009 in an effort to balance the state budget, but was implemented in 2011); and
- Enacted the commercial activity tax ("CAT"), a broad-based, low-rate tax measured by gross receipts from virtually all business activities and entities.

H.B. 66 became law in June 2005. Although generally opposed to gross receipts taxes because of their compounding nature, the broad base due to limited exclusions and the low rate caused many skeptical taxpayers to warm to the tax as the net savings over the former franchise and personal property taxes became clear. In addition, compliance costs were slashed as taxpayers no longer had to undertake the arduous process of preparing personal property tax returns or corporation franchise tax reports.

Results of Tax Reform

Due to the phased implementation of the provisions of H.B. 66 and the general economic slowdown that has gripped the country over the past few years, questions have been raised regarding the effectiveness of the tax reform efforts. OMA has been at the forefront in demonstrating that, indeed, the effort was worthwhile.

- In 2009, Ohio won Site Selection magazine's "Governor's Cup" for an unprecedented fourth consecutive year. The Governor's Cup is awarded annually to the state having the most major business expansions in the nation.
- A January 2009 Ernst & Young study indicated that Ohio's business tax burden rated between 18th and 23rd best among states on three different scales of comparison. Another Ernst & Young study conducted for the Ohio Business Development Coalition showed that Ohio had the lowest effective tax rates on new capital investment in the Midwest.
- The Small Business & Entrepreneurship Council's Business Tax Index in 2008 rated Ohio's state tax system as 14th best nationally.

- In March 2010 the Federation of Tax Administrations released an analysis of new data from the U.S. Census Bureau showing that for FY 2009, Ohio's per capita state tax burden was the 16th lowest; as a percentage of personal income, the burden was the 18th lowest.
- In April 2011, Ernst & Young and the Council on State Taxation issued a report entitled "Competitiveness of State and Local Business Taxes on New Investment" in which they concluded that Ohio had the third lowest rate of state and local taxation on new business investment. The report laid this result directly at the feet of the 2005 tax reform law.
- In early 2013, Site Selection Magazine honored Ohio as having the 5th most favorable tax climate for mature firms and the 3rd most favorable tax climate for new firms for fiscal year 2012.
- Finally, according to the Ohio Department of Taxation, Ohio is one of only six states that do not tax corporate profits, and one of 10 that do not tax business personal property.

Commercial Activity Tax

Much has been debated regarding the commercial activity tax (CAT). For manufacturers, while the tax is not perfect, it has done much to spur growth and investment in Ohio's largest industry.

According to Ohio Department of Taxation Fiscal Year 2014 Commercial Activity Tax Returns data, manufacturers made up the second-largest group of CAT taxpayers, representing 10.2 percent of all taxpayers (retail trade is the largest).

And, manufacturers pay 26.8 percent of the state's total – far more than any other group (in terms of CAT revenues based only on the 0.26 percent CAT rate for gross receipts in excess of \$1 million).

In addition, CAT filers with taxable gross receipts of \$1 million or less accounted for 66.7 percent of all filers in fiscal year 2014, but only 0.7 percent of the total liability for that period.

As noted above, some of the most important aspects of the CAT are its broad base, its low rate, and its broad application to business entities. Those attributes can only be maintained when the state stands firm against pleas for individual carve-outs and exemptions.

When it was first enacted, there were few exclusions from the CAT and only four credits. The tax expenditure associated with those exclusions in 2009, the first year the tax was fully phased in, was approximately \$300 million. Those exclusions were built into the tax as enacted and the 0.26 percent rate was established with those exclusions in mind.

In its fiscal year 2014 tax expenditure report, the Department of Taxation lists a larger number of exclusions and credits to the CAT. The total cost of those expenditures is over \$600 million! Thus, in just 10 years, additional credits and exclusions were added to the tax that doubled the amount of the tax expenditure.

The CAT is a stable tax. Although it is a gross receipts tax that pyramids along the economic chain, it is tolerated because of its broad base and low, low rate. However, in less than 10 years, tax expenditures associated with the tax have doubled. One wonders how much longer chipping away at the base can continue before the calls to increase the rate become too loud to ignore. Ohio traveled down this path before with the franchise and personal property taxes. The trip was a disaster. Ohio should not venture down that path again with the CAT.

The CAT was enacted as a tax on commercial activity. All enterprises engaged in such activity should be paying the CAT; in fact, equality in the burden of taxation demands that they all remain subject to the tax.

Personal Income Tax

As noted earlier, sound tax policy dictates that any tax should have a broad base, a low rate, and few exclusions in order to minimize economic distortion. OMA applauds recent efforts to reduce Ohio's personal income tax rates. However, it is concerned that those efforts have typically been tied to a proposal to increase the sales tax, particularly on business consumption. This tax-shifting is not beneficial and may be counter-productive as businesses and consumers adjust to higher and higher sales tax rates. Rather, if income tax rates are to be reduced further, exclusions and exemptions from the personal income tax ought to be re-examined. If rates are reduced, the need for those exclusions and exemptions disappears. This would provide a broader base and a lower rate for all taxpayers, reduce overall taxes, and avoid the problems of tax-shifting.

Ohio currently relies upon a number of taxes of general application to fund its operations. Tax-shifting and other efforts to reduce or increase reliance on any of those taxes should be considered with great caution. One only needs to consider the crisis in Nevada in 2008, or the current crisis in Alaska, to recognize the problems of over-reliance on any one tax. Just as a broad base is important for any single tax, a broad base of general taxes is equally important for the fiscal welfare of Ohio.

Sales and Use Taxes

Ohio's sales tax was first enacted as a temporary measure in the depths of the Great Depression in the 1930s. At that time, it was conceived as a tax on final personal consumption of tangible goods. One year after initial enactment, the use tax was enacted; the two taxes were made permanent and the first exemption for machinery and equipment used to produce tangible personal property for sale by manufacturing was added. Similar exclusions were made for other activities that, similarly, resulted in the production of goods that would be subject to the tax upon final sale.

The rationale for these exclusions is simple: The taxes are intended to be imposed upon the final consumption of goods and, now, those selected services that are subject to tax. Intermediate transactions prior to the final sale of the product, including the acquisition of machinery and equipment and the raw materials that are incorporated into the final product, are not intended to be taxed. The basis for this is four-fold:

First, imposing the tax on intermediate transactions (sometimes called business inputs) causes the tax to be imposed at each step in the production of a good. This causes the tax to pyramid at each step of the economic ladder, resulting in an effective tax rate that may be much higher than the statutory rate. For example, in conjunction with the 1994 tax study commissioned by the General Assembly, the staff provided an example in which a sales tax rate of 6.5 percent applied to two stages of production resulted in an effective tax rate of 9.5 percent at the time of the final retail sale.¹

Second, imposing the tax on business inputs increases the cost of doing business through the higher prices that result from the tax. Business generally will respond to higher costs in a combination of three ways: It may decide to charge higher prices; it may pay lower wages to workers (or expatriate those positions elsewhere); or it may provide a lower return on investment to owners.²

Third, direct inputs lead to the production of more valuable goods that are ultimately subject to the tax.

Fourth, the provision has economic development implications. Every single state that surrounds Ohio has a sales tax. Every one of those states has some sort of exemption from the tax for machinery and equipment used in the production of tangible goods to be sold by manufacturers. Moreover, the *1994 Study* also found that lower rates of taxation on business equipment increase the rate of business formation of smaller firms. Thus, imposing the sales tax on manufacturing machinery and equipment puts Ohio at a disadvantage from an economic development perspective.³

The application of sales and use taxes to business inputs has been the subject of comment on at least two prior occasions in Ohio. In 1982, the *Final Report and Recommendations of the Joint Committee to Study State Taxes* (114th General Assembly, December 1982), pp. 15-16 concluded that the taxes should be imposed broadly on consumer spending, but very selectively on business spending. Similarly, the *1994 Study* at p. 5-4 and the 1994 Staff Report at p. 27 both recognized that the sales tax should only be imposed upon the final consumer and that business inputs should not be taxed at all. The taxation of business inputs should be avoided because doing so leads to multiple levels of taxation and economic disadvantages. Moreover, the *1994 Report* concluded that if the sales tax is extended to services, there should be liberal exemptions for transactions between businesses.

However, this does not mean that manufacturers do not pay sales and use taxes in Ohio. Manufacturers purchase and use many goods and services that are not included in the manufacturing exemptions. Those items include machinery and equipment that is used before manufacturing begins, or after it ends; cleaning equipment and supplies; maintenance and repair equipment and supplies; storage facilities; most safety items; and office supplies and

¹ Roy Bahl, Ed., *Taxation and Economic Development: A Blueprint for Tax Reform in Ohio* (Battelle press 1994), p. 277-278 (“1994 Staff Report.”).

² *Taxation and Economic Development in Ohio: A Blueprint for the Future*, final Report of the Commission to Study the Ohio Economy and Tax Structure (December 23, 1994), p. iii (“1994 Study”).

³ *Id.*, at p. 5-4.

equipment and motor vehicles. As a result, manufacturers pay millions of dollars in sales and use taxes annually to the state of Ohio.

According to the 2014 Annual Report of the Ohio Department of Taxation, manufacturers as an economic segment paid more than \$410,000,000 in sales and use taxes directly to the state of Ohio. This is in addition to the untold millions of tax dollars that were paid to, and reported by, vendors and retailers located in Ohio. It appears that in terms of tax directly owed to the state, as opposed to tax that is collected from others, manufacturing is one of the largest payers of sales and use taxes in the state.

Since 2005, Ohio has attempted to move away from the taxation of business investment. It eliminated the tax on business tangible personal property. It eliminated the net worth base of the corporation franchise tax. And, it excludes from the commercial activity tax, receipts in the nature of a return on investment. As noted earlier in my remarks, the purchase of machinery and equipment by manufacturers is not final consumption. Rather, it reflects an investment in the business. The sales tax exemption for manufacturing machinery and equipment is consistent with this policy.

Imposing the sales tax on business inputs, including manufacturing machinery and equipment (and labor) is contrary to sound tax policy. As previous tax study commissions have concluded,⁴ good tax policy is based on simplicity, equity, stability, neutrality and competitiveness. Removing the exemption and subjecting those purchases to tax will render the tax more opaque, more complex, and less fair as final consumers who are less economically advantaged will pay an even higher proportion of their family income in sales taxes. Removing the exemption violates the principles of neutrality and competitiveness as it results in higher costs, which may influence economic decisions and competitiveness. Taken together, all these factors may in fact render the tax less stable.

Exclusion of Tax on Services as Manufacturing Inputs

There are two specific cases in which the sales or use tax should be amended to exclude specific manufacturing service inputs. I'll briefly describe the recommendations:

Ohio does not impose sales or use taxes (or the CAT) on the wages paid to employees. Just as wages are not subject to such taxes; and business inputs, such as ingredients, machinery and equipment, are exempted from the sales and use taxes, so too should amounts paid for temporary employees engaged in manufacturing activities that are otherwise exempt from the tax. Such employees are a business input; the sales tax should not apply to transactions by which such labor is obtained.

House Bill 343 currently pending in the House would address this issue for all employers. However manufacturers have especially solid policy reasons for this exclusion.

Effective January 1993 in order to fill a hole in the state budget, employment services were added as a taxable service by a conference committee facing a midnight deadline to reach

⁴ 1994 Study, p. 5-1; *Report of the Committee to Study State and Local Taxes* (March 1, 2003), p. 6.

agreement on a new budget. A taxable “employment service” includes any transaction in which a person provides personnel to perform work under the supervision or control of another, whether on a short- or long-term basis, where the personnel are paid by the person who provided them. The entire amount paid for the service serves as the base on which the tax is calculated.

Many manufacturers assumed that the existing manufacturing exemption, which exempted purchases of machinery and equipment used to produce tangible personal property for sale in a continuous manufacturing operation, would also cover workers on the manufacturing floor that operated the exempt equipment. Manufacturers and other purchasers of employment services also believed that in appropriate circumstances the services would be resold. After protracted litigation, they were disabused of both notions.

Another area that served fertile for litigation was the exclusion for employees that were “permanently assigned” to the purchaser. As noted previously, there were two conditions to this exclusion. First, the employees had to be provided pursuant to an agreement of a least a year in duration. Second, the agreement had to “specify” that the employees were provided to the purchaser on a “permanent” basis.

This provision likewise resulted in a flood of litigation.

The Department of Taxation continues to pursue employment services aggressively. It argues that employee turnover is a sign that the employees are not permanently assigned. It also takes the position that an agreement must set forth the name of every single employee covered by the agreement, and that if any of the employees provided under an agreement are not provided on an indefinite basis, then the entire agreement is tainted and none of the employees qualify for the exclusion.

In recent audits, the Department takes the position that virtually any transaction involving personnel is a taxable employment service. Thus, transactions in which outside consultants are retained to provide services, such as computer and software design, engineering, or a skilled trade, are routinely picked up on audit as employment services.

The Tax on Employment Services Should Be Repealed

House Bill 343 proposes to do away with the tax on employment services completely. The bill deletes “employment services” from the list of taxable transactions in R.C. 5739.01(B)(3)(k); it deletes the definition of “employment services” found in R.C. 5739.01(JJ); and deletes reference to the provision in other statutes.

Repeal of this provision reflects sound policy.

First, repeal is consistent with the recent efforts of Ohio’s tax policy to move away from the taxation of economic investment and towards personal consumption. Manufacturers invest in manufacturing machinery and equipment in order to expand or maintain their capacity to provide jobs and to produce a product for sale, a product that in most cases will be subject to the sales and use taxes when it is sold and used. Similarly, it invests in workers for the same reasons.

Since 2005, Ohio has attempted to move away from the taxation of business investment. It eliminated the tax on business tangible personal property. It eliminated the net worth base of the corporation franchise tax. And, it excludes from the commercial activity tax, receipts in the nature of a return on investment, including labor costs. Repealing the sales tax on employment services is consistent with this policy.

Second, imposing the sales tax on business inputs such as manufacturing machinery and equipment and labor is contrary to sound tax policy. As previous tax study commissions have concluded, good tax policy is based on simplicity, equity, stability, neutrality and competitiveness. Subjecting employment services to tax renders the tax more opaque, more complex, and less fair as final consumers who are less economically advantaged pay an even higher proportion of their family income in sales taxes. The tax on employment services violates the principles of neutrality and competitiveness as it results in higher costs, which may influence economic decisions and competitiveness. Taken together, all these factors may in fact render the tax less stable.

Just as wages are not subject to sales and use taxes; and business inputs, such as ingredients, machinery and equipment, are exempted from the sales and use taxes, so too should amounts paid for temporary employees engaged in manufacturing activities be excluded from the tax. Employees are a business input; the sales tax should not apply to transactions by which such labor is obtained.

Third, the provision has generated more and more litigation as the Department has taken increasingly aggressive positions with respect to it. The provision is neither clear, nor is it easy to administer.

An additional issue is that Ohio also taxes industrial janitorial and maintenance services. Manufacturers' production facilities and the equipment components of their production processes require continuous repair and maintenance. Without the required cleaning, repairs and maintenance the machinery breaks down and fails to produce acceptable products for sale to customers. Cleaning industrial assets is absolutely critical to the manufacturing process. It is a necessary business input and sales tax should not apply.

Severance Tax

While I am sure this commission will be taking a deeper dive into the severance tax issue, the OMA would like to take a couple of brief moments to touch on the issue.

The OMA recognizes that Ohio's current severance tax structure makes Ohio very competitive, one of the most competitive and drilling-friendly states according to provided data. We note the severance tax provisions in Ohio law, having first been enacted in 1971, are 40 years old and have not been materially updated. More extensive benchmarking of effective tax rates on the measure of energy severed would be helpful to inform policy decisions.

Even though new manufacturing investment does not qualify for cost recovery, the OMA recognizes the commonplace nature of cost recovery offered by other states to the oil and gas industry and does not object to some competitive level of cost recovery to spur new investment.

We note that a severance tax is an excise tax. An excise tax is typically upon a specified activity in order to help defray some special costs associated with that activity. In the case of the severance tax, those special costs might include regulatory, environmental, and health concerns, as well as infrastructure concerns for the communities in which the activity takes place. However, good tax policy demands that such a tax should not be used to fund a wide-scale reduction in some other tax of general application.

Conclusion

The OMA supports tax policy that supplies sufficient revenue for the execution of necessary state services in a manner that stimulates economic growth, investment and job creation. Tax policy should encourage growth of capital, and growth in jobs in Ohio.

Manufacturing is the largest contributor to the state's GDP, contributing more than 17.5 percent. The success of Ohio manufacturing – through its vast network of in-state customers and suppliers - large global firms and their local supply chains - enhances the economic vitality of all other Ohio industries and Ohioans' quality of life. Reducing tax rates in a manner that treats all taxpayers fairly should be encouraged.

Thank you very much for the opportunity to comment and provide input to this commission. Ohio's manufacturers are prepared to help improve the business climate in the state. We look forward to continuing our partnership with the administration and the General Assembly.

I'll be pleased to answer any questions you may have.



**BEFORE THE 2020 TAX POLICY STUDY COMMISSION OF THE OHIO GENERAL
ASSEMBLY**

**SENATOR BOB PETERSON AND REPRESENTATIVE JEFF MCCLAIN
CO-CHAIRMEN**

**TESTIMONY
OF
MARK ENGEL
BRICKER & ECKLER LLP
OMA TAX COUNSEL**

FEBRUARY 24, 2016

Senator Peterson, Representative McClain and members of the Commission, my name is Mark Engel. I'm the Partner in charge of Bricker & Eckler's Cincinnati-Dayton office. My practice is focused on taxation issues, with concentrated experience in all aspects of state and local taxation, including tax planning, compliance, and litigation in sales and use, income, commercial activity, public utility, and property taxation as well as economic development. I also serve as tax counsel for The Ohio Manufacturers' Association (OMA). I'm testifying today on behalf of OMA regarding tax expenditures and the Commercial Activity Tax (CAT). The OMA was created in 1910 to advocate for Ohio's manufacturers; today, it has 1400 members. Its mission is to protect and grow Ohio manufacturing.

Background:

For Ohio to be successful in a global economy, the state's tax structure must encourage investment and growth and be competitive nationally and internationally. A globally competitive tax system is characterized by (a) certainty, (b) equity, (c) simplicity and (d) transparency. Economy of collections and convenience of payment also are important considerations.

Prior to 2005, Ohio's tax structure was essentially unchanged since the 1930s. The major taxes were the real property tax, the sales and use taxes, the tax on tangible personal property used in business, and the corporation franchise tax measured on net worth. However, the franchise tax and the tangible personal property tax, especially, both hit capital-intensive industries harder than other industries and had to be paid whether the entity made, or lost, money. Thus, the manufacturing sector paid an inordinately high level of state tax when compared with other segments of the economy.

As services made up a larger share of Ohio's economy over the years, the inequality in the state tax burden between manufacturing and other segments of the economy was exacerbated. Many service sector concerns operate without a significant investment in capital; hence, their tangible personal property and net worth franchise tax liabilities were minimal. Many of these services operate on more slender margins or can manipulate their finances to minimize income; as a result, little income tax was

generated. In addition, many of these new service entities were organized as pass-through entities that were not subject to the franchise tax. As the demand for state services grew, the only recourse was to raise existing tax rates on existing taxpayers. In many cases, that meant an increasing tax burden for Ohio manufacturers.

Paradoxically, Ohio continued to add exemptions from, and exceptions to, the various taxes during this time. As a result, Ohio was saddled with a number of taxes that had high nominal rates, but struggled to raise sufficient levels of revenue for governmental operations. The discrepancies between taxpayers and economic segments also increased and compliance with the existing taxes became more complicated.

The large and increasing number of exemptions and exclusions, added over the years in order to render the franchise, personal property and sales and use taxes less onerous, narrowed the bases of those taxes. Accompanied by the relentless rise in tax rates, the taxes were not only inefficient, but also discriminatory against businesses with heavy investment in capital.

Tax Reform Enacted

Over the years, calls increased to reform Ohio's tax system to render it more fair and competitive. Finally, in early 2005, true tax reform was proposed. The goals of tax reform were:

- Eliminate the taxation of investment and shift to the taxation of consumption;
- Broaden the over-all business tax base;
- Reduce over-all business tax rates;
- Improve fairness;
- Provide a more stable and predictable flow of revenue; and
- Simplify compliance.

The result was a comprehensive overhaul of Ohio's tax system by H.B. 66. As enacted, the bill:

- Eliminated the tangible personal property tax on new investment in manufacturing and phased out the tax on all general business property over 4 years;
- Phased out the corporation franchise tax for most corporations over 5 years;
- Phased in a 21% reduction in personal income tax rates ratably over 5 years (the last reduction was delayed 2 years in 2009 in an effort to balance the state budget, but was implemented in 2011); and
- Enacted the commercial activity tax ("CAT"), a broad-based, low-rate tax measured by gross receipts from virtually all business activities and entities.

H.B. 66 became law in June 2005. Although generally opposed to gross receipts taxes because of their compounding nature, taxpayers warmed to the CAT as the net savings over the former franchise and personal property taxes became clear due to the broad base, limited exclusions, and the low rate.¹ In addition, compliance costs were slashed as taxpayers no longer had to undertake the arduous process of preparing personal property tax returns or corporation franchise tax reports.

Many tax expenditures spring from the desire of policymakers to manage the economy, control economic behavior, or provide special favors through taxation. Regardless of how well-intentioned those efforts may be, tax expenditures can and do create undesirable consequences. They often reduce certainty, as many create questions as to who may benefit from them, and the extent of the benefit. They reduce equity, resulting in government picking winners and losers. Tax expenditures increase complexity and reduce transparency as taxpayers and tax administrators attempt to implement them. In short, they are bad tax policy and their use should be minimized. In fact, by minimizing them, the base is broadened and the need for special treatment is reduced.

¹ Manufacturers remain the largest category of CAT taxpayers. See Exhibit A, attached.

CAT Tax Expenditures:

Tax reform notwithstanding, Ohio has continued on its relentless march towards more tax exclusions, even as it enacted the CAT, raised sales tax rates and broadened the base, and continued to cut income tax rates. As noted many times, some of the most important aspects of the CAT are its broad base, its low rate, and its broad application to virtually all business entities. Those attributes can only be maintained when the state stands firm against pleas for individual carve-outs and exemptions.

When it was first enacted, there were approximately 25 exclusions from the CAT and only four credits. The tax expenditure associated with those exclusions in 2010, the first year the tax was fully phased in, totaled approximately \$300 million. Those exclusions were built into the tax as enacted and the 0.26 percent rate was established with those exclusions in mind.

In its fiscal year 2014 tax expenditure report, the Department of Taxation lists a larger number of exclusions and credits to the CAT. The CAT now lists approximately 36 exclusions and is subject to 7 credits. The total cost of those expenditures, without consideration of the credits, is over \$600 million! Thus, in just 10 years, additional credits and exclusions were added to the tax that doubled the amount of the tax expenditure.

The CAT is a stable tax. Although it is a gross receipts tax that pyramids along the economic chain, it is tolerated because of its broad base and low, low rate. However, in less than 10 years, tax expenditures associated with the tax have doubled. One wonders how much longer chipping away at the base can continue before the calls to increase the rate become too loud to ignore. Ohio traveled down this path before with the franchise and personal property taxes. The trip was a disaster. Ohio should not venture down that path again with the CAT.

The CAT was enacted as a tax on commercial activity. All enterprises engaged in such activity should be paying the CAT; in fact, equality in the burden of taxation demands

that they all remain subject to the tax. Exemptions, exclusions and credits violate the rule of equality and render the tax less clear and more complicated.

Sales and Use Tax Expenditures

Ohio's sales tax was first enacted as a temporary measure in the depths of the Great Depression in the 1930s. At that time, it was conceived as a tax on the final personal consumption of tangible goods. One year after initial enactment, the use tax was enacted, the two taxes were made permanent and the first exemption for machinery and equipment used to produce tangible personal property for sale by manufacturing was added. Similar exclusions were made for other activities that, similarly, resulted in the production of goods that would be subject to the tax upon final sale.

The rationale for these exclusions is simple: The taxes are intended to be imposed upon the final personal consumption of goods and, now, those selected services that are subject to tax. Intermediate transactions prior to the final sale of the product, including the acquisition of machinery and equipment and the raw materials that are incorporated into the final product, are not intended to be taxed.² The economic basis for this principle is four-fold:

First, imposing the tax on intermediate transactions (sometimes called business inputs) causes the tax to be imposed at each step in the production of a good. This causes the tax to pyramid at each step of the economic ladder, resulting in an effective tax rate that may be much higher than the statutory rate. For example, in conjunction with the 1994 tax study commissioned by the General Assembly, the staff provided an example in which a sales tax rate of 6.5 percent applied to two stages of production resulted in an effective tax rate of 9.5 percent at the time of the final retail sale.³

Second, imposing the tax on business inputs increases the cost of doing business through the higher costs that result from the tax. Business generally will respond to

² The exclusion for business inputs does not mean that manufacturers do not pay significant amounts of sales and use taxes. See Exhibit B, attached.

³ Roy Bahl, Ed., *Taxation and Economic Development: A Blueprint for Tax Reform in Ohio* (Battelle Press 1994), p. 277-278 (the "1994 Staff Report").

higher costs in a combination of three ways: It may decide to charge higher prices; it may pay lower wages to workers (or expatriate those positions elsewhere); or it may provide a lower return on investment to owners.⁴ Such an impact by taxes on economic decisions should be minimized.

Third, direct inputs lead to the production of more valuable goods that are ultimately subject to the tax. Thus, the tax on the final product is maximized.

Fourth, the provision has economic development implications. Every single state that surrounds Ohio has a sales tax. Every one of those states has some sort of exemption from the tax for machinery and equipment used in the production of tangible goods to be sold by manufacturers. Moreover, the *1994 Study* also found that lower rates of taxation on business equipment increase the rate of business formation of smaller firms. Thus, imposing the sales tax on manufacturing machinery and equipment puts Ohio at a disadvantage from an economic development perspective and may actually reduce small business formation.⁵

The application of sales and use taxes to business inputs has been the subject of comment on at least two prior occasions in which taxes in Ohio were studied. In 1982, the *Final Report and Recommendations of the Joint Committee to Study State Taxes* (114th General Assembly, December 1982), pp. 15-16 concluded that sales and use taxes should be imposed broadly on consumer spending, but very selectively on business spending. Similarly, the *1994 Study* at p. 5-4 and the *1994 Staff Report* at p. 27 both recognized that the sales tax should only be imposed upon the final consumer and that business inputs should not be taxed at all. The taxation of business inputs should be avoided because doing so leads to multiple levels of taxation and economic disadvantages. Moreover, the *1994 Report* concluded that if the sales tax is extended to services, there should be liberal exemptions for transactions between businesses.

⁴ *Taxation and Economic Development in Ohio: A Blueprint for the Future*, Final Report of the Commission to Study the Ohio Economy and Tax Structure (December 23, 1994), p. iii (“*1994 Study*”).

⁵ *Id.*, at p. 5-4.

The taxes are intended to apply to final, personal consumption. When the taxes were conceived, that meant primarily the purchases of tangible personal property by individuals. While some business purchases, such as office equipment and supplies, were subjected to taxation, business inputs that contributed to the production of a product, the sale of which would subsequently be subject to sales or use tax, were excluded. Other than the sale of food, few other exemptions existed.

Over the years, a number of exclusions have been added to the taxes. While many of them represent transactions involving business inputs, a majority of them represent exclusions of another nature. Today, R.C. 5739.02(B) contains 53 subdivisions providing for exclusions from the tax. One subdivision alone, subdivision (B)(42), contains 15 separate exclusions! Other exclusions are scattered throughout the Revised Code. And, this does not include the number of consumer services that are not even included in the tax base.

Business consumption is taxed under the CAT. The sales and use taxes are intended to apply to personal consumption of final goods and services. If the bases of those taxes are broadened accordingly, especially with respect to services, and exclusions and exemptions are limited, the rates can be lowered, further reducing the need for additional exclusions.

Personal Income Tax Expenditures

The personal income tax was enacted in the early 1970s as an additional, stable source of revenue. Over the years, the number of exclusions and credits has mushroomed as well, and the rates were driven upwards. Even though rates have dropped about 35 percent since the 2005 tax reform, R.C. 5747.01(A) still provides for about 22 deductions or exclusions for calculating Ohio taxable income. R.C. 5747.98 lists 38 separate credits that may be taken against the tax.

Many exclusions and deductions to the sales and income taxes have a social basis. The personal income tax credit for retirement income and medical premiums are just two examples. Many exclusions serve laudatory purposes, but the result is a system of

taxes that is complicated, favors some taxpayers over others, and results in ever-higher tax rates on those who are left paying the bills. Ohio may be further ahead to lower the rates and let everybody help pay for the government services that they all use.

Summary:

Since the enactment of tax reform in 2005, OMA has maintained a principled, consistent approach to tax policy in Ohio. That approach insists on certainty, equity, simplicity, and transparency. The erosion of the tax reform legislation, in the form of carve-outs, exclusions, and ear-marks, reduces certainty, creates disparity by selecting winners and losers, renders the tax code more complicated, and reduces transparency as it becomes more difficult to determine who is entitled to which exclusions.

Everybody has a story; everybody has a reason why one tax or another is not fair to them. However, one cannot have an efficient and fair tax system that is different for every taxpayer. Nor is it fair to tax some segments of the economy at levels that are 10 times higher than those imposed on other segments. The 2005 tax reform legislation was directed at trying to reduce that inequity on a tax system-wide basis. Every time an exclusion or exemption from the CAT, the sales and use taxes, or the personal income tax is created, that increases the tax burden on everybody else. The solution isn't a tax system made of Swiss cheese; we tried that already, and it didn't work.

It is time to stop the madness. Rather than continuing to enact exclusions that render the taxes less and less fair, more and more complicated, and result in higher and higher tax rates for taxpayers, OMA suggests that a better approach may be to broaden the bases as appropriate, reduce the number of exclusions and reducing over-all tax rates. If rates are reduced, the necessity for the special tax treatment afforded by exclusions that are not economically based, and that are contrary to the very purpose of the tax, is reduced significantly. The result is a tax system that comprises one or more taxes with a broad base, a low rate tax, that is simple to enforce and simple to follow, and that treats all taxpayers the same.

Thank you very much for the opportunity to appear here today. I'd be pleased to answer any questions that any of you might have.

EXHIBIT A

CAT and Manufacturers:

According to Ohio Department of Taxation Fiscal Year 2015 Commercial Activity Tax Returns data, manufacturers made up the second-largest group of CAT taxpayers, representing 10.5% of all taxpayers (retail trade is the largest).

And, manufacturers pay 26.1% of the state's total – far more than any other group (in terms of CAT revenues based only on the 0.26% CAT rate for gross receipts in excess of \$1 million).

In addition, CAT filers with taxable gross receipts of \$1 million or less accounted for 66.3% of all filers in fiscal year 2014, but less than 1% of the total liability for that period.

EXHIBIT B

Sales Tax and Manufacturers:

Despite the exemption for machinery and equipment enjoyed by manufacturers, this does not mean that manufacturers do not pay sales and use taxes in Ohio.

Manufacturers purchase and use many goods and services that are not included in the manufacturing exemptions. Those items include machinery and equipment that is used before manufacturing begins, or after it ends; cleaning equipment and supplies; maintenance and repair equipment and supplies; storage facilities; most safety items; and office supplies and equipment and motor vehicles. It also includes automatic data processing, computer and electronic information services, and temporary employment and employment placement services. As a result, manufacturers pay millions of dollars in sales and use taxes annually to the state of Ohio.

According to the 2015 Annual Report of the Ohio Department of Taxation, manufacturers as an economic segment paid more than \$426,000,000 in sales and use taxes directly to the state of Ohio. This is in addition to the untold millions of tax dollars that were paid to, and reported by, vendors and retailers located in Ohio. It appears that in terms of tax owed to the state, as opposed to tax that is collected from others, manufacturing is one of the largest payers of sales and use taxes in the state.



Foregone Revenue from CAT Exclusions, Deductions and Credits

Below are estimates of revenue foregone in FY 2017 by the state General Revenue Fund from various CAT exclusions, deductions and credits.¹ Dollar amounts are millions.

Exclusion of first \$1 million of taxable gross receipts	\$267.8
Qualified distribution center receipts exclusion	\$164.6
Job creation credit	\$88.1
Job retention tax credit	\$29.6
Credit for increased qualified research and development expenses	\$28.6
Agricultural receipts	\$14.0
Casino receipts in excess of "gross casino revenue"	>\$10.0 ²
Credit for net operating loss carry forwards and other deferred tax assets	\$7.1
Professional employer organization exclusion	\$5.4
State and federal cigarette tax exclusion	\$3.5
Consumer product integrated supply chain exclusion	\$3.0 ³
Motor vehicle transfer exclusion	\$2.0
Exclusion of certain services to financial institutions	\$1.9
Exclusion of real estate brokerage gross receipts not retained	\$1.5
Research and development loan program credit	\$1.5
State and federal alcoholic beverage excise tax exclusion	\$1.1
Exemption for pre-1972 trusts	<\$1.0 ⁴
Anti-neoplastic drug exclusion	<\$1.0
Horse racing taxes and purse exclusion	<\$1.0
Receipts from sale of uranium from qualifying uranium enrichment zone	<\$1.0
Providing public services exclusion	No Estimate Available
Petroleum receipts ⁵	No Estimate Available
Motion picture credit	No Estimate Available
Estimated Total Foregone Revenues	More than \$629.7 million

NOTE: Actual total foregone revenues will be higher than estimated total foregone revenues, which reflect indefinite revenues for casino receipts and undetermined revenues for the public services exclusion, petroleum receipts and motion picture credit.

¹ Unless otherwise noted, the source for the data listed above is the Ohio Department of Taxation Tax Expenditure Report (Fiscal Years 2016-2017).

² Ohio Legislative Service Commission estimates foregone revenue from casino receipts in excess of "gross casino revenue" will be "tens of millions of dollars."

³ Ohio Legislative Service Commission, Senate Bill 208 Fiscal Note as Enacted, 2015.

⁴ The Ohio Department of Taxation Tax Expenditure Report provides only general "less than \$1 million" estimates for six items in this list (rather than precise estimates as provided for the other items). For this reason, we have chosen not to include any foregone revenue for the six items with estimated foregone revenues of less than \$1 million each.

⁵ Motor vehicle fuel dealers pay a one-time tax of 0.65% on their sales of petroleum products.

October 19, 2015

Memorandum

From: Mark A. Engel, Esq.
Bricker & Eckler LLP

To: Rob Brundrett
The Ohio Manufacturers' Association

Subject: CAT exemption for manufacturer, supplier, or distributor of beauty, health, personal care, or aromatic products

As originally enacted, the exclusion related to receipts from transactions between qualified integrated supply chain vendors, and it related to equipment that essentially touched the product incorporated into the finished goods, as well as work in process inventory.

This amendment broadens the exclusion, first, by including a retailer within the group of persons who qualify for the exclusion. That means that receipts from transfers to retailers will be excluded from the CAT; as enacted, those receipts are taxable receipts. See division (F)(2)(jj)(i), (iii), page 20. It also includes anybody that may be included in the retailer's consolidated elected or combined taxpayer group. See division (F)(2)(jj)(vii), page 21.

A second way the exclusion is broadened is that parts used to "hold, contain, package, or dispense" qualified products no longer are limited to qualified products that are incorporated into the item sold at retail. See division (F)(2)(jj)(ii)(I), page 20. I'm not sure the extent of this broadening, but since the items no longer have to be incorporated into the final product, that potentially opens up a lot of things to the exclusion.

Third, the amendment brings finished goods within the scope of "qualified property" the receipts from which are excluded from the CAT. See division (F)(2)(jj)(ii)(III), page 20.

By including the retailer within the scope of the exemption, the "integrated supply chain" is expanded to include essentially any service provider to the retailer, such as an advertiser or other business consultant. See the definition of integrated supply chain in section (F)(2)(jj)(v).

Bottom line is that this provision picks a winner and gives it a huge advantage over its competition: The CAT no longer applies to intermediate transactions, thereby lowering its prices. There is no reason this model couldn't, or shouldn't, be implemented for any other nonintegrated manufacturing operation. There goes the CAT.



Ohio Legislative Service Commission

Bill Analysis

Mackenzie Damon

S.B. 235

131st General Assembly
(As Introduced)

Sens. Beagle and Coley

BILL SUMMARY

- Authorizes a property tax exemption for the increase in value of property planned for commercial or industrial development while the property is in the pre-development stage.

CONTENT AND OPERATION

Property tax exemption for land in the pre-development stage

The bill authorizes a property tax exemption for land in the pre-development stage. The exemption applies to (1) parcels included in a plat subdividing land that has not yet been, but will be, developed for commercial or industrial uses and (2) existing commercial or industrial property that is no longer in use, but for which redevelopment is planned.

With respect to undeveloped property, the bill exempts any increase in the value of such property beginning with the tax year in which the plat subdividing the land is approved, and ending with the last tax year before development of the property begins. With respect to existing commercial or industrial property, the bill exempts the increase in the value of the property beginning with the tax year in which title is transferred from the person that held title to the property when it was last used for commercial or industrial purposes, and ending with the tax year in which redevelopment of the property begins.¹

¹ R.C. 5709.45.

The bill first applies to the 2015 tax year.²

HISTORY

ACTION	DATE
Introduced	10-27-15

S0235-I-131.docx/ks

² Section 2.





Ohio Legislative Service Commission

Bill Analysis

Mackenzie Damon

S.B. 288

131st General Assembly
(As Introduced)

Sens. Eklund, LaRose, Seitz, Patton

BILL SUMMARY

- Removes the imposition of a direct tax on pass-through entities (PTEs) – which effectively causes them to "withhold" income taxes on the distributive shares of their nonresident investors – while maintaining the requirement that PTEs remit taxes on such investors' behalf.
- Lowers the tax rates at which PTEs must remit taxes on investor income to equal the tax rate that would apply if the investor filed an individual income tax return.
- Consolidates the two existing PTE filing options into one return.
- Repeals and consolidates multiple obsolete or duplicative provisions of the law governing pass-through entity investor taxation.
- Removes the imposition of a direct tax on trusts that causes them to withhold income tax on certain types of distributions made to nonresident beneficiaries.
- Modifies the apportionment method for the investment income of certain trusts.
- Makes nonrefundable, rather than refundable, the income tax credit that allows taxpayers that own a pass-through interest in a financial institution to offset the owner's share of the entity's financial institutions tax (FIT) liability.
- Repeals some expired provisions of the Corporation Franchise Tax and Income Tax Law.

CONTENT AND OPERATION

Pass-through entity taxation

The Ohio income tax applies to income received by an owner or investor in a pass-through entity (PTE) from the PTE's business activities in the state. (Pass-through entities include S corporations, partnerships, and limited liability companies treated for federal income tax purposes like S corporations or partnerships.) Under current law, in order to ensure collection of the tax from nonresident individuals and entities – which may not otherwise be required to file an individual tax return – a PTE is required to withhold the income tax due from its nonresident investors. This "withholding tax" is imposed directly on the PTE, even though the underlying tax liability belongs to the investors.

The bill makes several changes to the mechanism for collecting tax on PTE investor income. First, the bill maintains the requirement that PTEs remit taxes on behalf of nonresident investors, but removes language directly imposing a tax on PTEs as a means of "withholding" those investors' taxes. Accordingly, references in the Revised Code to a "pass-through entity withholding tax" are removed. Second, the bill lowers the rates at which PTEs remit taxes on investor income to equal the tax rate that would apply if the investor filed an individual return. Third, the bill repeals and consolidates multiple provisions in an effort to streamline the law governing taxation of pass-through entity income.¹

Filing requirements

Under current law, a PTE required to file a tax return on behalf of its nonresident investors has a choice between two different returns – the IT 1140 (the income tax withholding return) or the IT 4708 (a composite return). The bill consolidates these two returns into one.² Because the bill eliminates the "withholding tax," the new return requirements more closely resemble the requirements for the existing IT 4708. The following table outlines the key features of the existing and new PTE income tax returns:

¹ R.C. 5747.01, 5747.059, 5747.03, 5747.08, 5747.082, 5747.11, 5747.13, 5747.132, 5747.14, 5747.15, 5747.20, 5747.21, 5747.212, 5747.22, 5747.231, 5747.28, 5747.30, 5747.331, 5747.40, 5747.41, 5747.42, 5747.43, 5747.44, 5747.45, 5747.451, 5747.98, and 5748.01 and Section 3.

² R.C. 5747.08, 5747.40, 5747.41, and 5747.42.



	IT 1140 (R.C. 5747.42)	IT 4708 (R.C. 5747.08(D))	Proposed law
Type of return(s)	<p>Withholding tax return only.</p> <p>Both resident and nonresident investors still must separately file IT 1040 individual tax returns.</p>	<p>Composite tax return.</p> <p>Resident investors, and nonresident investors with other Ohio income, are still required to file IT 1040 individual tax returns. Nonresident investors with no other Ohio income may, but are not required to, file an IT 1040 individual tax return.</p>	<p>Composite tax return.</p> <p>Same as IT 4708.</p>
Who must file	<p>All PTEs with Ohio "nexus," unless:</p> <p>(a) The PTE files an IT 4708 for all of its nonresident investors, (b) all of the PTE's investors are residents or are not subject to the income tax (e.g., corporations), or (c) all of the PTE's investors are other PTEs with investors described in (b).³</p> <p>Some forms of PTEs do not have to file, including mutual funds, REITs, REMICs, nonprofit organizations, pension plans, colleges and universities, public utilities, publicly traded partnerships, and insurance companies.</p>	<p>No PTE is required to file an IT 4708. The return is optional.</p> <p>Note: A PTE may file an IT 1140 for some investors and an IT 4708 for the other investors in the same taxable year. Also, a person invested in two PTEs may be listed on an IT 1140 by one PTE and on an IT 4708 by the other PTE.</p>	<p>All PTEs with Ohio nexus, unless:</p> <p>(a) All of the PTE's investors are residents or (b) all of the PTE's investors are persons other than other PTEs or entities not subject to the income tax (e.g., corporations).</p> <p>Note: PTEs that are not required to a file a composite tax return must instead file an informational return with the Department of Taxation, unless:</p> <p>(a) None of the PTE's investors is subject to the income tax or (b) all of the PTE's investors are residents and the PTE will not claim any business tax credits.</p>

³ "Nexus" is not defined by current statute or the bill. In the context of the income tax, it has been construed by courts to be a threshold level of contacts between the taxing state and a person or entity sufficient to permit the state to tax the person's or entity's income derived from business activity in the state. See *Agley v. Tracy*, 87 Ohio St.3d 265 (1999).

	IT 1140 (R.C. 5747.42)	IT 4708 (R.C. 5747.08(D))	Proposed law
Investors included on return	All investors, other than full-year residents and specified exempt entities, such as nonprofit organizations, pension plans, colleges and universities, public utilities, publicly traded partnerships, and insurance companies. Nonresident investors are not included if the PTE includes those investors on an IT 4708.	The PTE may include all investors other than C corporations or other PTE investors that have a C corporation as an investor.	All investors.
Tax base	<p>The total of investors' distributive shares of the PTE's net income, with some additions and deductions (known as the "adjusted qualifying amount").</p> <p>The withholding tax base does not include investment-type income earned by an "investment pass-through entity."⁴ However, such income is taxable on the investor's IT 1040 individual tax return.</p>	<p>Substantially similar to IT 1140 (but includes only the shares of investors reported on the composite return).</p> <p>N/A.</p>	<p>Substantially similar to IT 1140 and IT 4708.</p> <p>N/A.</p>
Limitations	N/A. Because each individual investor is required to file an IT 1040 individual return, the investor may claim the small business income deduction, personal exemptions, and nonbusiness credits on that form.	Investors cannot claim the small business income deduction, personal exemptions, or nonbusiness credits unless the individual investor files an IT 1040 individual return.	Same as IT 4708.

⁴ R.C. 5733.401. An "investment pass-through entity" is a PTE that has 90% of its assets in the form of intangible assets and that receives 90% of its gross income from investment-related activity (dividends, interest, capital gains, management fees, loan fees, financing fees, and similar forms of income).

	IT 1140 (R.C. 5747.42)	IT 4708 (R.C. 5747.08(D))	Proposed law
Payment threshold	No payment due if "adjusted qualifying amount" is less than \$1,000.	N/A.	No payment due if the amount of tax due after application of business credits is less than \$250.
Quarterly estimated taxes	Required if total "adjusted qualifying amounts" exceed \$10,000.	Required if total tax due exceeds \$500. (The same threshold applicable to individual income taxpayers.)	Same as IT 4708.

Tax rates

Current law

Under current law, different tax rates apply to pass-through entity income depending on the annual form the PTE files:

Form 1140: If a PTE files an IT 1140 withholding tax return, the PTE must withhold tax on its investors' "adjusted qualifying amount" at the rate of 5% for individuals and 8.5% for trusts and investors that are themselves pass-through entities. Both of these rates are higher than the statutory tax rate on business income, which, for 2016, is 3%. However, because each individual investor is required to file an IT 1040 individual tax return, the individual may calculate the individual's business income tax rate at 3% on that return and receive a refund for any difference between the amount withheld and the amount actually due.

Form 4708: If a PTE files an IT 4708 composite return, the PTE must remit tax on the investor's taxable business income at "the highest tax rate" specified in the Income Tax Law, which, for 2016, is the highest nonbusiness income tax rate of 4.997%. Individual investors included on the IT 4708 may file an IT 1040 individual tax return to receive a refund of any difference between the amount paid on the IT 4708 and the amount actually due.

Proposed law

Under the bill, a PTE must remit taxes on behalf of the investors included on the return at the business income tax rate of 3%.⁵ (Nevertheless, nonresident individual investors may elect to file an IT 1040 individual return in order to claim the small business income deduction, a personal exemption, and any nonbusiness credits.)

⁵ R.C. 5747.40(A)(4). (Note that the bill includes an erroneous cross-reference to the applicable tax rate.)



Look-through provisions

Current law

Under current law, a PTE is not required to remit tax on the distributive shares of income that pass through to another PTE if the other, "investor" PTE irrevocably acknowledges that it has nexus with the state for the entire taxable year. For example:

Blue LLC is owned 100% by Purple LLC. Purple LLC is owned 100% by Jack and Jill. Blue LLC would not be required to remit tax on behalf of Purple LLC (if Purple LLC irrevocably acknowledges it has nexus with Ohio); Purple LLC would remit the tax.⁶

Proposed law

Under the bill, a PTE with an investor that is also a PTE is required to remit the tax due on the distributive share of the investor PTE, and the investor PTE may claim a credit for taxes paid by the lower-tier PTE. For example:

Blue LLC is owned 100% by Purple LLC. Purple LLC is owned 100% by Jack and Jill. Blue LLC would remit the tax due on the income passed-through to Purple LLC. When Purple LLC files its annual return, it may claim a credit for the tax paid by Blue LLC.⁷

In this example, Jack and Jill, direct investors in Purple LLC and indirect investors in Blue LLC, also may claim a credit for the taxes remitted by Blue LLC, but only if Purple LLC does not claim the credit.

Taxation of trusts

Under continuing law, an individual may be liable for income tax on the distributions the individual receives as the beneficiary of a trust to the extent included in the individual's federal adjusted gross income, and trusts are taxed on the portion of

⁶ R.C. 5733.402. An exception to this rule applies to investment pass-through entities. If an investment PTE owns all or part of another PTE, that other PTE is required to remit the tax on behalf of the investment PTE (and, accordingly, the investment PTE's investors) – but only if the investment PTE provides to the other PTE the contact information of its investors. R.C. 5747.401.

In the above example, if Purple LLC is an "investment pass-through entity," then Blue LLC would be required to remit the tax on behalf of Purple LLC (if Purple LLC provides Blue LLC with the contact information of Jack and Jill).

⁷ R.C. 5747.42(C).

the trust's undistributed taxable income that is apportioned or allocated to Ohio. The trust tax is computed by multiplying the allocated and apportioned income of the trust by the personal income tax rates.

Repeal of trust withholding tax

The bill repeals a requirement that trusts withhold income tax on certain types of distributions made to their nonresident beneficiaries. (As with the pass-through entity withholding tax, the purpose of the trust withholding tax is to ensure collection of the tax from beneficiaries who might otherwise not be required to file an individual Ohio tax return.) The withholding tax applies to distributions that directly or indirectly relate to either real estate located in Ohio or tangible personal property located in Ohio.

Apportionment of certain trust investment income

In general, there are three methods of apportioning or allocating trust income, depending on the source of income: (1) capital gains (or losses) from the sale of certain assets ("the qualifying trust amount") are apportioned based on the proportion of the value of the asset located in Ohio as compared to everywhere, (2) business income – excluding such capital gains or losses – is apportioned under a three-factor formula (sales, property, and payroll), and (3) nonbusiness income – excluding such capital gains or losses – is allocated to Ohio to the extent the income is produced by trust assets that compose the Ohio resident part of the trust under trust residency rules.

The bill removes an exception to this general rule for certain types of investment income. Under current law, the exception applies to certain investment income received by a trust that was in existence before June 5, 2002 (the date the tax on undistributed trust income took effect) or that, if it did not then exist, was composed almost entirely (80%) of assets owned by related persons or another trust satisfying certain criteria. In general, current law requires that such income be apportioned in the same manner as business income (under the sales, property, and payroll three-factor formula), rather than being allocated as nonbusiness income, if the income is attributable to the trust's ownership of a "qualifying investment pass-through entity." An "investment pass-through entity," for this purpose, is a PTE that has 40% of its assets in the form of intangible assets, that receives 40% of its income from investment-related activity, and that was also formed before June 5, 2002.⁸ The effect of the bill's change is to cause a trust's income that currently is regarded as qualifying investment income to be apportioned or allocated in the same manner as the trust's business income and nonbusiness income, depending on whether the investment income is business or nonbusiness income.

⁸ R.C. 5747.01(BB), 5747.011, 5747.012, and 5747.02.



Refundability of income tax credit offsetting FIT liability

Continuing law allows an individual, estate, or trust that owns a pass-through interest in a financial institution to claim an income tax credit that offsets the owner's share of the entity's financial institutions tax (FIT) liability. The FIT is a business privilege tax on financial institutions, e.g., banks.

Under current law, the tax credit is refundable; so, if the credit amount allowed for a year exceeds the taxpayer's tax liability for that year, the taxpayer may receive a refund of the excess. The bill makes the credit nonrefundable; however, if the credit exceeds the taxpayer's liability for a particular year, the bill allows the excess to be carried forward to future tax years until fully used.

The bill also requires that, if the credit amount is affected by a change in the entity's FIT liability, the taxpayer must report the change within 60 days. If the change is not reported before that deadline, the Tax Commissioner may assess the taxpayer for the difference.⁹

Repeal of expired provisions

The bill removes language in the Revised Code that:

- Required PTEs with a business presence in Ohio to withhold corporation franchise taxes on the distributive shares of nonresident investors. The withholding tax is no longer required, as the corporation franchise tax was completely phased out in 2013.¹⁰
- Authorized an income tax credit for investment in a certified ethanol production plant. The last year in which the credit could be awarded was 2012, and – due to a three-year carryforward allowance – the last year in which the credit could be claimed was 2015.¹¹
- Required an adjustment to a trust beneficiary's adjusted gross income when the beneficiary received an accumulation distribution. This language was relevant only for taxable years before 2002, when the income tax applied only to trust distributions to beneficiaries, rather than

⁹ R.C. 5747.01, 5747.65, and 5747.98.

¹⁰ R.C. 5733.01, 5733.04, 5733.057, 5733.0611, 5733.09, 5733.12, 5733.40, 5733.401, 5733.402, 5733.41, and 5733.98.

¹¹ R.C. 901.13, 5747.75, and 5747.98.



to both distributions and undistributed trust income (as it has since 2002).¹²

Miscellaneous changes

The bill makes various changes to move definitions and other language among different Revised Code sections – for example, moving definitions for "related member," "qualifying controlled group," "disregarded entity," "distributive share," "investor," and language prescribing computation of the three-factor formula for apportioning business income – and makes numerous changes to conform existing law to the bill's substantive amendments.

Regarding the definition of "related member," the bill makes a slight change but declares that it "is intended to clarify and be declaratory of" current law's definition.¹³ The change is to the rules governing how ownership of stock or other ownership interests are to be attributed to individuals, PTEs, estates, trusts, or corporations for the purpose of determining whether any two such persons are related. In the PTE taxation provisions of the bill and current law, the ownership relation between persons affects the computation of the tax base on which PTEs must remit tax. The tax base ("adjusted qualifying amount") includes two adjustments intended to discount the effects of transactions between two related members: one effectively negates deductions for excess expenses paid to a related member and the other negates losses incurred from transactions between related members. (Either kind of transaction can be used to shift net income between related persons.) Current law states that, for the purpose of the tax base adjustments, an ownership interest will be attributed to a person in some cases if that person owns 40% or more of an entity.¹⁴ The bill applies different attribution rules to those cases (I.R.C. sec. 318) that specify a 50% ownership threshold.¹⁵

Effective date

The bill applies to taxable years ending on or after January 1, 2017.¹⁶

¹² R.C. 5747.01(A)(6).

¹³ Section 3.

¹⁴ R.C. 5733.042(A)(6) and 5733.40(P).

¹⁵ R.C. 5747.01(DD)(2).

¹⁶ Section 4.



HISTORY

ACTION

DATE

Introduced

03-02-16

S0288-I-131.docx/ks





**BEFORE THE ECONOMIC AND WORKFORCE DEVELOPMENT COMMITTEE
THE OHIO HOUSE OF REPRESENTATIVES
REPRESENTATIVE NAN BAKER, CHAIR**

**HOUSE BILL 343
TESTIMONY
OF
LUKE HARMS
SENIOR MANAGER, GOVERNMENT RELATIONS
WHIRLPOOL CORPORATION**

NOVEMBER 18, 2015

Chair Baker and members of the Committee, my name is Luke Harms. I'm Senior Manager of Government Relations at Whirlpool Corporation. Whirlpool is the number one appliance manufacturer in the world, with approximately 100,000 employees and 70 manufacturing and technology centers. Here in Ohio, Whirlpool has five manufacturing facilities with approximately 10,000 employees.

I'm testifying here today on behalf of The Ohio Manufacturers' Association (OMA) with respect to House Bill 343, which proposes to repeal the sales tax on employment services. The OMA was created in 1910 to advocate for Ohio's manufacturers; today, it has 1400 members. Its mission is to protect and grow Ohio manufacturing.

Today I will provide you with background information about the existing sales tax exemption provided to manufacturers with respect to the purchase and use of machinery and equipment used in a manufacturing operation to produce tangible personal property for sale. I will cover the sound policy reasons to extend such tax treatment to employment services.

Ohio's Sales and Use Taxes

Ohio's sales tax was first enacted as a temporary measure in the depths of the Great Depression in the 1930s. At that time, it was conceived as a tax on final personal consumption of tangible goods. One year after initial enactment, the use tax was enacted; the two taxes were made permanent and the first exemption for machinery and equipment used to produce tangible personal property for sale by manufacturing was added. Similar exclusions were made for other activities that, similarly, resulted in the production of goods that would be subject to the tax upon final sale.

The rationale for these exclusions is simple: The taxes are intended to be imposed upon the final consumption of goods and, now, those selected services that are subject to tax. Intermediate transactions prior to the final sale of the product, including the acquisition of machinery and equipment and the raw materials that are incorporated into the final product, are not intended to be taxed. The basis for this is four-fold:

First, imposing the tax on intermediate transactions (sometimes called business inputs) causes the tax to be imposed at each step in the production of a good. This causes the tax to pyramid at each step of the economic ladder, resulting in an effective tax rate that may be much higher than the statutory rate. For example, in conjunction with the 1994 tax study commissioned by the General Assembly, the staff provided an example in which a sales tax rate of 6.5 percent applied to two stages of production resulted in an effective tax rate of 9.5 percent at the time of the final retail sale.¹

Second, imposing the tax on business inputs increases the cost of doing business through the higher prices that result from the tax. Business generally will respond to higher costs in combination of three ways: It may decide to charge higher prices; it may pay lower wages to workers (or expatriate those positions elsewhere); or it may provide a lower return on investment to owners.²

Third, direct inputs lead to the production of more valuable goods that are ultimately subject to the tax.

Fourth, the provision has economic development implications. Every single state that surrounds Ohio has a sales tax. Every one of those states has some sort of exemption from the tax for machinery and equipment used in the production of tangible goods to be sold by manufacturers. Moreover, the *1994 Study* also found that lower rates of taxation on business equipment increase the rate of business formation of smaller firms. Thus, imposing the sales tax on manufacturing machinery and equipment puts Ohio at a disadvantage from an economic development perspective.³

The application of sales and use taxes to business inputs has been the subject of comment on at least two prior occasions in Ohio. In 1982, the Final Report and Recommendations of the Joint Committee to Study State Taxes (114th General

¹ Roy Bahl, Ed., *Taxation and Economic Development: A Blueprint for Tax Reform in Ohio* (Battelle Press 1994), p. 277-278 (the "1994 Staff Report").

² *Taxation and Economic Development in Ohio: A Blueprint for the Future*, Final Report of the Commission to Study the Ohio Economy and Tax Structure (December 23, 1994), p. iii ("1994 Study").

³ *Id.*, at p. 5-4.

Assembly, December 1982), pp. 15-16 concluded that the taxes should be imposed broadly on consumer spending, but very selectively on business spending. Similarly, the *1994 Study* at p. 5-4 and the *1994 Staff Report* at p. 27 both recognized that the sales tax should only be imposed upon the final consumer and that business inputs should not be taxed at all. The taxation of business inputs should be avoided because doing so leads to multiple levels of taxation and economic disadvantages. Moreover, the *1994 Report* concluded that if the sales tax is extended to services, there should be liberal exemptions for transactions between businesses.

Manufacturing Exemptions for Tangible Personal Property Is Not Absolute

Manufacturers enjoy exemption for three categories of purchases:

- Machinery and equipment used primarily during and in the manufacturing process
- Ingredients and materials that are incorporated into the final product that is produced for sale
- Packages and packaging equipment

However, this does not mean that manufacturers do not pay sales and use taxes in Ohio. Manufacturers purchase and use many goods and services that are not included in the manufacturing exemptions. Those items include machinery and equipment that is used before manufacturing begins, or after it ends; cleaning equipment and supplies; maintenance and repair equipment and supplies; storage facilities; most safety items; and office supplies and equipment and motor vehicles. As a result, manufacturers pay millions of dollars in sales and use taxes annually to the state of Ohio.

According to the 2014 Annual Report of the Ohio Department of Taxation, manufacturers as an economic segment paid more than \$410,000,000 in sales and use taxes directly to the state of Ohio. This is in addition to the untold millions of tax dollars that were paid to, and reported by, vendors and retailers located in Ohio. It appears that in terms of tax directly owed to the state, as opposed to tax that is collected from others, manufacturing is one of the largest payers of sales and use taxes in the state.

The Tax on Employment Services

Effective January 1993, in order to fill a hole in the state budget, employment services were added as a taxable service by a conference committee facing a midnight deadline to reach agreement on a new budget. A taxable “employment service” included any transaction in which a person provides personnel to perform work under the supervision or control of another, whether on a short- or long-term basis, where the personnel are paid by the person who provided them. The entire amount paid for the service served as the base on which the tax was calculated.

Originally, four categories of transactions were excluded from the definition. Those four categories include:

- Transactions between members of an affiliated group;
- Persons providing medical and health care services;
- Persons providing contracting and subcontracting services; and
- Persons assigned to another pursuant to a contract of at least a year in duration that specifies that each employee covered by the agreement is “permanently” assigned to the purchaser.

A fifth category, involving services that were resold, was later added to the statute.

The tax generated a great deal of revenue, more than was expected, and the Department became more and more aggressive when it came to auditing the issue. The result was increased uncertainty on the part of business and increased time and expense in litigation responding to the aggressive enforcement activities of the Department.

For example, many manufacturers had begun employing temporary labor as a means of providing extra flexibility in meeting their workforce needs. Whether on a “temp-to-hire” basis, or as a means of meeting temporary up-ticks in production activities, manufacturers increasingly turned to vendors of temporary employees to fill those needs. Not surprisingly, many of those manufacturers assumed that the existing manufacturing exemption, which exempted purchases of machinery and equipment

used to produce tangible personal property for sale in a continuous manufacturing operation, would also cover workers on the manufacturing floor that operated the exempt equipment. Manufacturers and other purchasers of employment services also believed that in appropriate circumstances the services would be resold. After protracted litigation, they were soon disabused of both notions.

Another area that served fertile for litigation was the exclusion for employees that were “permanently assigned” to the purchaser. As noted previously, there were two conditions to this exclusion. First, the employees had to be provided pursuant to an agreement of a least a year in duration. Second, the agreement had to “specify” that the employees were provided to the purchaser on a “permanent” basis.

This provision likewise resulted in a flood of litigation involving issues such as

- Whether the agreement had to be written, or whether an oral agreement would suffice.
- The length of the term of the agreement, especially those that renewed or were cancelable at will.
- The meaning of the requirement that employees be “permanently assigned” to the purchaser.
- Whether the mere recitation of language in a service agreement that employees were permanently assigned was sufficient; or whether the course of conduct between the parties also had to establish that the positions were indeed indefinite.

The Department of Taxation continues to pursue employment services aggressively. It argues that employee turnover is a sign that the employees are not permanently assigned. It also takes the position that an agreement must set forth the name of every employee covered by the agreement, and that if any of the employees provided under an agreement are not provided on an indefinite basis, then the entire agreement is tainted and none of the employees qualify for the exclusion.

In recent audits, the Department takes the position that virtually any transaction involving personnel was a taxable employment service. Thus, transactions in which outside consultants are retained to provide services, such as computer and software design, an engineer, or a skilled tradesperson, are routinely picked up on audit as employment services.

The Tax on Employment Services Should Be Repealed

House Bill 343 proposes to do away with the tax on employment services completely. The bill deletes “employment services” from the list of taxable transactions in R.C. 5739.01(B)(3)(k); it deletes the definition of “employment services” found in R.C. 5739.01(JJ); and deletes reference to the provision in other statutes.

Repeal of this provision reflects sound policy.

First, repeal is consistent with the recent efforts of Ohio tax policy to move away from the taxation of economic investment and towards personal consumption. Manufacturers invest in manufacturing machinery and equipment in order to expand or maintain their capacity to provide jobs and to produce a product for sale, a product that in most cases will be subject to the sales and use taxes when it is sold and used.

Since 2005, Ohio has attempted to move away from the taxation of business investment. It eliminated the tax on business tangible personal property. It eliminated the net worth base of the corporation franchise tax. And, it excludes from the commercial activity tax, receipts in the nature of a return on investment, including labor costs. Repealing the sales tax on employment services is consistent with this policy.

Second, imposing the sales tax on business inputs, including manufacturing machinery and equipment and labor is contrary to sound tax policy. As previous tax study commissions⁴ have concluded, good tax policy is based on simplicity, equity, stability, neutrality and competitiveness. Subjecting employment services to tax renders the tax more opaque, more complex, and less fair as final consumers who are less

⁴ 1994 Study, p. 5-1; *Report of the Committee to Study State and Local Taxes*, March 1, 2003, p. 6.

economically advantaged pay an even higher proportion of their family income in sales taxes. The tax on employment services violates the principles of neutrality and competitiveness as it results in higher costs, which may influence economic decisions and competitiveness. Taken together, all these factors may in fact render the tax less stable.

Just as wages are not subject to sales and use taxes; and business inputs, such as ingredients, machinery and equipment, are exempted from the sales and use taxes, so too should amounts paid for temporary employees engaged in manufacturing activities be excluded from the tax. Employees are a business input; the sales tax should not apply to transactions by which such labor is obtained.

Third, the provision has generated more and more litigation as the Department has taken increasingly aggressive positions with respect to it. The provision is neither clear, nor is it easy to administer.

Temporary employment services play a critical role for manufacturers. At Whirlpool, temporary employees help the company manage seasonal demand changes for appliances. For example, our KitchenAid small appliance factory in Greenville has much higher shipment levels in the months leading up to the holiday season and our major appliance factories in Clyde, Marion, Findlay and Ottawa also see a significant uptick in shipments in the summer, driven by increased home construction and renovations. Temporary employment services not only help us avoid layoffs, but they help recruit skilled workers, many of whom eventually become Whirlpool employees. We compete in a competitive global environment. The products we produce here in Ohio must compete every day with imported appliances from Mexico, China and many other countries.

In conclusion, the impact of H.B. 343, to repeal the imposition of sales and use taxes on temporary employment services is not only founded on sound tax and economic policy, but will help Ohio manufacturers like Whirlpool to remain globally competitive. The sales and use taxes are intended to be taxes on ultimate household consumption; they are not intended to apply to business inputs or to intermediate transactions. Applying

the taxes to transactions involving the investment in labor, especially in labor to operate manufacturing machinery and equipment increases the cost of the goods that are produced, negatively impacts economic decisions, and may place Ohio at a disadvantage when it comes to economic development. That isn't good policy. It ought not to be the policy of Ohio.

Thank you. I'll be pleased to answer any questions you may have.



House Bill 394: Selected Major Provisions at Glance

House Bill 394 offers a reasonable, balanced package of unemployment insurance law reforms designed to address the current insolvency of Ohio's Unemployment Insurance Trust Fund (UI Trust Fund). The bill contains a combination of unemployment tax, benefit and integrity provisions that in the aggregate will improve solvency by tightening alignment of benefit costs and contribution revenues while building a significant fund balance, over time, that will be sufficient to avoid subjecting Ohio to increased federal taxes and penalties related to unemployment insurance.

Among the major reforms proposed in the legislation are the following:

- **Temporary Increase in State Unemployment Tax Base.** HB 394 would increase the state unemployment tax base from \$9,000 to \$11,000 when the UI Trust Fund balance is below 50 percent of the 1.0 Average High Cost Model solvency level and continue the increase until the UI Trust Fund reaches 1.0 Average High Cost Model. The state tax base will be reduced back to \$9,000 when the UI Trust Fund equals or exceeds the 1.0 AHCM solvency level. If the balance dips below 50 percent of the solvency level in future years, the tax base will automatically return to the \$11,000 level.
- **Reduction of Number of Potential Weeks of Unemployment Insurance.** HB 394 would change the determination of the total number of weeks of unemployment compensation potentially available to twice a year, based on Ohio's seasonally adjusted three-month total unemployment rate, before January and June. A sliding scale would set the number as low as 12 weeks when the rate is 5.5 percent or below, and up to 20 weeks if the rate is 9 percent or above. Ohio currently uses a sliding scale ranging from 20 to 26 weeks.
- **Temporary Freeze on the Maximum Weekly Benefit Amount.** HB 394 would effectively freeze maximum weekly benefit dollar amounts at a level not to exceed 50 percent of the statewide average weekly wage for the first year that the UI Trust Fund was less than the Minimum Safe Level (MSL), and would continue those maximums until the year after the UI Trust Fund was at or above the MSL.
- **Dependency.** To align with the majority of states, HB 394 would repeal Ohio's current dependency provision that increases the weekly benefit amount provided to claimants who have higher wages and dependents.
- **Drug Testing.** HB 394 provides language under which the Ohio Department of Job and Family Services may (a) request information of applicants for unemployment compensation about the results of past drug tests, (b) conduct drug tests for controlled substances, and (c) disqualify individuals within the narrow limitations of federal law.

HB 394 addresses a number of additional issues that impact UI Trust Fund solvency, including constructive lockout exceptions in labor disputes, standards for determining just cause for termination and quits without just cause, coordination of unemployment compensation benefits with Social Security retirement benefits, enhanced fraud penalties and collection, and improved non-fraud overpayment collection, among others. Collectively, the HB 394 reforms position Ohio in line with surrounding states and states with whom we compete for investment and jobs.



The Case for Unemployment Insurance Reform in Ohio

EXECUTIVE SUMMARY

Introduction

Ohio's unemployment insurance (UI) system is in a state of crisis. The Ohio Unemployment Insurance Trust Fund, which is funded by employers and pays out benefits to qualifying jobless workers, is insolvent. The benefits the system pays out are substantially out of balance with the tax receipts it takes in to fund it. The system is nearly \$775 million in debt to the federal government – money it borrowed to keep paying benefits during and after the Great Recession of 2008. As a result, Ohio's system is dangerously unstable and a deterrent to economic development. Reforms are urgently needed to update and strengthen Ohio's UI program for the benefit of Ohio's employers, employees and economy. Most specifically, Ohio's Unemployment Insurance Trust Fund is not likely to recover solvency before the next recession unless the state takes action to pay off its outstanding federal unemployment compensation loan balance and better aligns benefits with contributions to build a balance.

How the System Works¹

The Social Security Act of 1935 (SSA) created a federal-state unemployment insurance program to (a) provide temporary, partial wage replacement to individuals out of work, generally through no fault of their own, and (2) promote economic stability by maintaining a steady flow of dollars throughout the economy even when there is widespread unemployment.² The UI system historically has been forward funded – i.e., a sufficient positive balance is needed in the state unemployment trust fund to avoid having to borrow to pay benefits resulting from a reasonably foreseeable economic downturn.

To be eligible for unemployment benefits, jobless workers must demonstrate “workforce attachment,” usually measured by a work requirement (e.g., number of weeks of work) and/or a wage requirement (e.g., dollar amount of wages earned). Individuals also must be able, available and actively seeking work. Each state has a different formula for determining the amount of workforce attachment needed to obtain UI benefits from the state.

The UI program is a federal-state partnership conforming to federal requirements and administered by state agencies under state law. The Office of Unemployment Insurance Operations at the Ohio Department of Job and Family Services (ODJFS) administers Ohio's UI program. Administrative funds for ODJFS are allocated by the federal government from federal payroll taxes employers pay to the Internal Revenue Service.

¹ This section of the document borrows heavily from a U.S. Department of Labor publication, *Unemployment Compensation: Federal-State Partnership*, April 2015.

² <http://www.bizfilings.com/toolkit/sbg/office-hr/managing-the-workplace/unemployment-benefits-system-info.aspx>

Financing the Program

Unemployment compensation paid to unemployed workers is financed largely through both federal and state unemployment taxes paid by employers. Just three states – Alaska, New Jersey and Pennsylvania – collect UI taxes from employees.

UI taxes are based on various factors, including the wages employers pay their employees, the type and size of the business, and the number and amount of unemployment claims filed against the business.

- At the federal level, the Federal Unemployment Tax Act (FUTA) imposes a single flat rate payroll tax on the first \$7,000 of wages employers pay each employee in a year. The current FUTA tax rate is 6.0 percent. However, employers can earn credits against their FUTA tax to reflect the state employment taxes they pay. Employers who pay their State Unemployment Tax Act (SUTA) taxes in a timely manner under an approved state unemployment compensation program can earn a credit of up to 5.4 percent against the 6.0 percent, resulting in an effective tax rate of 0.6 percent. These states are also eligible to receive federal grants to cover the costs of administering the program through federal appropriations. Additionally, funds from the FUTA-funded Federal Unemployment Account reimburse the state unemployment trust fund for 50 percent of charges for “extended” unemployment benefits when extended benefits are triggered by periods of high unemployment.
- At the state level, each state determines its own SUTA tax rates. Some states apply various formulas to determine the taxable wage base; others use a percentage of the state’s average annual wage; and a few simply follow the FUTA wage base of \$7,000. In 2014, SUTA tax rates ranged from 0.0 percent to 2.6 percent for minimum rates, and from 5.4 percent to 10.89 percent for maximum rates. All but a handful of states’ wage bases exceeded the FUTA minimum requirement of \$7,000. In 2014, Ohio’s SUTA base was \$9,000, with a minimum contribution rate of 0.3 percent and a maximum contribution rate of 8.60 percent.

The state assigns or computes a specific individually determined UI tax rate for each employer annually. Every state uses some kind of “experience rating” system to determine the rate. Generally, the fewer the claims, the lower the rate the business pays in state UI taxes.

States lacking sufficient funds to pay their required unemployment benefits are authorized by Title XII of the SSA to request advances (i.e., loans) from the FUTA’s federal loan fund account, the Federal Unemployment Account. If not repaid, these loans carry interest that must be paid from sources other than the state UI trust fund.

Impact of the Great Recession

The Great Recession of 2008 was the nation’s longest and deepest since the Great Depression of the 1930s. A majority of states did not have sufficient balances in their state unemployment trust funds to pay benefits without requesting advances (i.e., loans) from the federal government to assure that unemployment compensation benefits were paid. Ohio was among the states hardest hit by the recession.

The Recession was much greater than expected, wiping out positive unemployment trust fund balances across the country and in Ohio. Automatic tax trigger provisions in Ohio law designed

to address a milder recession were insufficient to meet the increased benefit payout. The size of the deficit after the Recession was too great to make up with benefit cuts or tax increases alone and even years after the Recession, benefit payments each year continue to be nearly as high as unemployment contribution revenue.

The unemployment insurance tax burden in Ohio generally increased as a result of the Recession as claims experience increased, the payroll against which experience was determined was reduced, and Ohio became subject to the FUTA offset credit reductions under federal law. As the economy slowly recovered with increased payrolls and reduced claims experience, experience rates improved and the average state unemployment insurance contribution was reduced. ***However, the FUTA tax has continued to increase as Ohio's Title XII loan has not been repaid.***

The impact in Ohio has been severe. Ohio's unemployment trust fund balance has been a negative number as of the end of the second quarter every year since 2009. ***Today, the Ohio Unemployment Insurance Trust Fund is insolvent.***

Responses to Insolvency

In response to the threat of insolvency, states have taken various actions to bolster tax revenue and reduce benefit outlay, including the following:

- Eliminating outstanding loan debt to the federal government by obtaining bank loans and/or using bonds to finance the debt through the private sector
- Enacting solvency legislation with a combination of benefit cuts and tax increases to eliminate Title XII debt and better align benefit costs with revenue over the long term
- Reducing the number of potential weeks of unemployment compensation
- Increasing tax bases
- Revising contribution rate schedules
- Reducing maximum weekly benefit amounts
- Enacting more aggressive integrity measures to identify and collect additional revenue through benefit overpayment recovery and contribution collection improvements

Ohio, however, is one of a small number of states with significant outstanding federal debt that have chosen not to enact solvency measures, instead allowing automatic FUTA penalties to continue to increase to provide the revenue needed to reduce the state's outstanding debt.

This is a dangerous path to follow. Failure to pay off a state's outstanding FUTA debt has costly consequences. Under federal law, if a state has an outstanding Title XII loan balance on January 1 for two consecutive years, and the full amount of the loan is not repaid by November 10 of the second year, the 5.4 percent FUTA tax credit for employers in that state will be reduced annually by 0.3 percent for each succeeding year until the loan is repaid. From the third year onward, additional reductions in the FUTA offset credit may be imposed. States that continue to have outstanding loan balances over five years in a row are subject to an even greater FUTA tax increase as a penalty for not having addressed solvency through increases in taxes and/or cuts in benefits.

Why Ohio Needs Unemployment Insurance Reform

Currently, Ohio ranks poorly on many important unemployment insurance program metrics. For example:

- Ohio's Unemployment Insurance Trust Fund is insolvent.
- Ohio's outstanding Title XII debt is approximately \$775 million – nearly equal to the cost of unemployment insurance benefit payments for an entire year. Only California has a larger unpaid Title XII loan debt balance.
- Ohio is one of a small number of states with significant outstanding federal debt that have chosen not to enact solvency measures.
- Employers in Ohio currently pay higher total costs associated with unemployment compensation than employers in most other states, while benefit payment amounts in Ohio are higher than the national average. This makes Ohio a high-cost, high-benefit state.
- The FUTA tax paid by Ohio employers has continued to increase as Ohio's Title XII loan has not been repaid.
- Ohio is one of just four states currently subject to higher FUTA penalty rates and potentially subject to an additional Benefit Cost Rate (BCR) penalty in 2015 for having outstanding loan balances five years in a row and failing to address insolvency.
- Ohio failed to pay off the state's outstanding FUTA debt before November 10, 2015, triggering an additional reduction in the FUTA offset credit for employers in Ohio. This will result in Ohio employers paying higher FUTA taxes for 2015 – at least an additional \$105 per employee, on top of the normal \$42 per employee.

Ohio's UI trust fund is not likely to recover solvency before the next recession unless the state takes action to pay off its outstanding federal loan balance and better align benefits with contributions to build a balance in anticipation of the next recession.

Conclusion

Ohio's Unemployment Insurance Trust Fund must be made solvent before the next recession – not only to manage the repayment of Ohio's remaining Title XII loan balance but also to align benefit and contributions to build an adequate unemployment trust fund balance. The best solvency plan is one that also includes a focus on job creation because increased employment not only increases contributions but also reduces benefit payout. For that reason, rates also should be in line with surrounding states and states with which Ohio competes to attract and retain new business.

Unemployment insurance policy reform priorities should focus on eliminating the state's current unemployment trust fund debt, aligning benefit payout with contribution revenue, and building a balance in the unemployment trust fund sufficient to avoid triggering automatic FUTA tax increases that have significantly increased unemployment taxes for Ohio employers since the Great Recession of 2008. A vital first step for Ohio should be to pay off of the remaining Title XII loan balance to eliminate the FUTA tax increase as soon as possible.

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CINCINNATI | DAYTON
MARIETTA

BRICKER & ECKLER LLP
201 East Fifth Street
Suite 1110
Cincinnati, OH 45202
MAIN: 513.870.6700
FAX: 513.870.6699

www.bricker.com
info@bricker.com

Mark A. Engel
513.870.6565
mengel@bricker.com

MEMORANDUM

To: Robert Brundrett, Ohio Manufacturers' Association
From: Mark A. Engel, Bricker & Eckler LLP
Date: April 4, 2016
Re: House Bill 491

House Bill 491 proposes to enact a credit against the commercial activity tax ("CAT") for taxpayers that incur certain costs at facilities located in activated foreign trade zones within the state. The credit is nonrefundable and equals the amounts that the taxpayer spends on specified activities during the tax period.

Proposed R.C. 5751.15(A)(1) defines a "foreign trade zone" as any general or special purpose zone for which a permit has been granted and remains active, and includes special purpose subzones.

"Qualifying training or continuing education" means "career enrichment lectures, activities, or self-study programs" that are tailored to an employee's current job, a job to which the employee aspires, or the industry in which the employee works."

The credit is available to taxpayers maintaining operations within an active foreign trade zone. The credit equals the amount spent by the taxpayer on the following four categories at the activated trade zone facility in Ohio:

1. Creating additional employment positions;
2. Providing qualifying training or continuing education for employees;
3. Making capital investments, including expenditures for renewable energy resources; and
4. Undertaking initiatives to increase its exports of goods or services produced.

The credit is limited to the amount of tax otherwise due on the basis of gross receipts derived from activities at the facility.

There is no provision for unused credit amounts to carry forward. The credit expires January 1, 2022.

Just a couple of observations about the bill.

February 26, 2016

Page 2

The credit is based on the expenses made; that is, the expenses are not tax-affected. If a taxpayer spends \$1 million, its credit equals \$1 million; its credit is not 0.26 % off \$1 million.

The definition of “qualifying training or continuing education” is pretty broad. Lectures and self-study programs can be very general, and the jobs for which such training is obtained may include virtually any job, whether with the employer or not.

Expenses to undertake initiatives to increase exports of goods and services produced at the facility are likewise very broad and vague. General advertising campaign expenses could qualify for the credit.

All in all, this seems to be a *very* generous credit. It might be interesting to know the taxpayer on whose behalf this bill was introduced.

OMA PUBLIC POLICY FRAMEWORK FOR ACTION

The Ohio Manufacturers' Association

ohiomfg.com



Public Policy Framework for Action

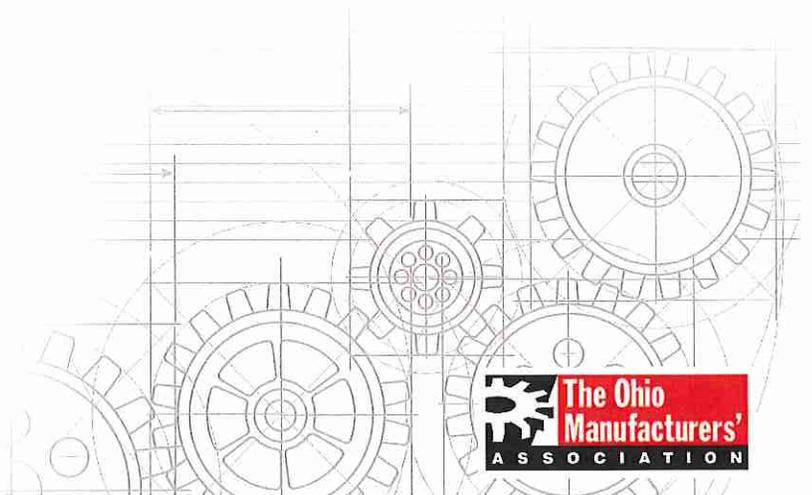
Manufacturing is responsible for 17% of Ohio's Gross Domestic Product; this is greater than the contribution of any other Ohio industry sector. Manufacturing is the engine that drives Ohio's economy.

In the competitive domestic and global economies, every public policy decision that affects Ohio's business climate affects Ohio's manufacturing competitiveness. In turn, Ohio's manufacturing competitiveness determines the ability of the state to grow its economy and create jobs.

Ohio manufacturers require public policies that attract investment and protect the state's manufacturing legacy and advantage. These policies apply to a wide variety of issues that shape the business environment within which manufacturers operate.

MAJOR POLICY GOALS INCLUDE THE FOLLOWING:

- **An Efficient, Competitive Tax System**
- **A Lean, Productive Workers' Compensation System**
- **Access to Reliable, Economical, Diverse Energy Resources**
- **A Fair, Stable, Predictable Civil Justice System**
- **Science-based, Technologically Achievable, and Economically Reasonable Environmental Regulations**
- **A Modern Public Resource Infrastructure**
- **An Educated, Highly Skilled Workforce**



Policy Goal:

An Efficient, Competitive Ohio Tax System

For Ohio to be successful in a global economy, the state's tax system must encourage investment and growth. It must be competitive nationally and internationally. A globally competitive tax system is characterized by (a) certainty, (b) equity, (c) simplicity and (d) transparency. Economy of collections and convenience of payment also are important attributes.

Generally, manufacturers support efforts to broaden the tax base, which enables lower rates. To preserve the integrity of the broad tax base and ensure fairness, credits and exemptions should be reduced and discouraged. Where needed, government incentives are best structured as grants rather than as tax credits. And, in general, earmarking and dedicating tax revenues should be discouraged.

Good tax policy also generates necessary revenues to support the essential functions of government. Good budgeting and spending restraint at all levels of government are vital to a competitive tax environment.

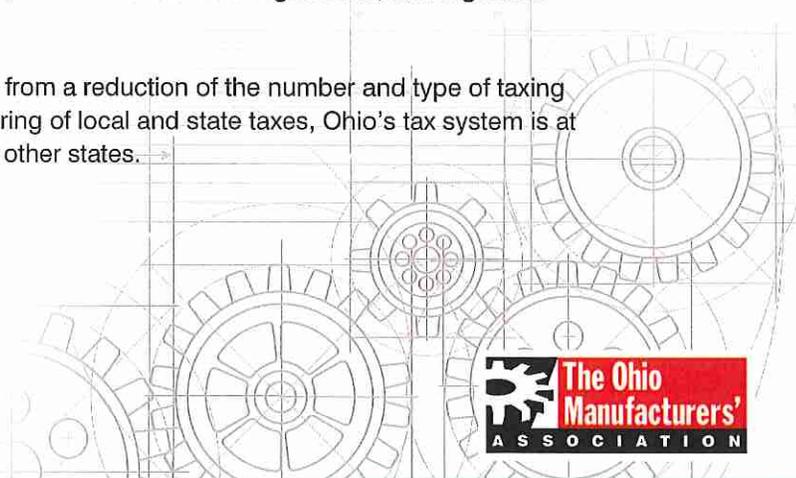
Major tax reforms approved by the Ohio General Assembly in 2005 and additional reforms in 2011 through 2014 have led to significant improvements to a tax system that was for many years widely regarded as obsolete. These reforms reduced overall tax rates, eliminated tax on investment, and broadened the tax base, all of which provide more stable and predictable revenues, and simplify compliance.

The elimination of the tangible personal property tax, the corporate franchise tax, and the estate tax has strengthened the competitiveness of Ohio's tax system. So has the reduction of the personal income tax rate as well as the creation of a broad-based, low-rate commercial activity tax.

Going forward, these tax policy gains must be protected. Tax bases should be protected against erosion by granting narrow special interests credits and carve-outs, in order to protect the productivity of the taxes. Where possible and reasonable, tax bases should be expanded, and tax rates reduced.

In addition, the state should continue its negotiations with Ohio municipalities to streamline the collection of municipal income tax by creating a uniform statewide municipal tax code, with uniform definitions of taxable income, consistent rules and regulations, and a generic municipal income tax form.

The state's tax system would also benefit from a reduction of the number and type of taxing jurisdictions. Because of its complex layering of local and state taxes, Ohio's tax system is at a competitive disadvantage compared to other states.



Tax

[New CAT Credit Bill Introduced](#)

April 8, 2016

Last month, Rep. [Marlene Anielski](#) (R-Walton Hills) introduced House Bill 491 to establish a five-year pilot program whereby taxpayers with Ohio facilities in an active foreign trade zone may claim a nonrefundable commercial activity tax (CAT) credit equal to the amount invested by the taxpayer in job creation and a number of other specified activities.

OMA tax counsel Mark Engel of Bricker & Eckler wrote this [summary of the bill](#) and concluded: "All in all, this seems to be a very generous credit."

[What is TaxBrain?](#)

April 8, 2016

It is an interface for open source economic modeling of tax policy analysis. It has been developed by the [Open Source Policy Center](#) of the American Enterprise Institute.

You can use [TaxBrain](#) to model any number of tax policy parameters and their budgetary and economic effects.

The aim of the Open Source Policy Center is to break open the black box of policy modeling that takes place in our nation's capital, where data and analytics are often obscure and hidden.

The center's aim is "making policy analysis more transparent, accessible, and innovative by harnessing open source methods to build cutting edge economic models and a webapp for accessing those models."

[Facts About the Section 199 Tax Deduction](#)

April 1, 2016

OMA Connections Partner, GBQ Partner LLC, indicates that the Section 199 deduction, also referred to as "the domestic production deduction," or the "domestic production activities deduction" or "the manufacturers' deduction" is often overlooked. [Here's more from GBQ.](#)

["Work Opportunity Tax Credit" Filing Extended](#)

March 25, 2016

The IRS has recently granted an extended deadline to eligible employers who are planning to claim the Work Opportunity Tax Credit (WOTC). Employers now have until June 29, 2016 to file a form necessary to claim the credit for certain eligible workers.

The Protecting Americans from Tax Hikes Act of 2015 (the PATH Act) extended the WOTC through 2019. The credit is for employers that hire individuals who are members of a "target group." The PATH Act also expanded the credit beginning this year to apply to employers that hire qualified individuals who have been unemployed for 27 weeks or more.

[Read more](#) from OMA Connections Partner, Clark Schaefer Hackett.

[Ohio 19th in State & Local Tax Rates](#)

March 18, 2016

According to [recently released data](#) from the Tax Foundation, Ohio's combined state and local tax rate is 7.14%. That ranks us 19th among the states (higher ranking = lower rates).

The highest rate in the land? Tennessee at 9.46%. The lowest? Alaska at 1.78%.

The foundation calculates a population-weighted average of local sales taxes as of January 1, 2016 in an attempt to give a sense of the average local rate for each state.

[New Form 1095-C Due to Employees by March 31, 2016](#)

March 11, 2016

OMA Connections Partner, RSM, [reminds us](#): "Employers with at least 50 full-time or full-time equivalent employees are required to provide a new Form 1095-C for 2015 to each employee by March 31, 2016. The form contains information about the employee's enrollment in the employer's health plan. If the employer's health plan is self-insured, the form also reports coverage information for the employee's spouse and dependents. The form may be furnished to employees by hand delivery, first-class mail or electronic delivery. If an employer wishes to use the electronic-delivery method, it must first obtain affirmative consent from the employee.

"Employees use the information on the forms as supporting documentation when completing their

individual income tax returns. However, the IRS has indicated that individuals may file their 2015 income tax returns prior to receiving Form 1095-C.

“Employers are also required to submit Forms 1095-C to the IRS by May 31, 2016 (if filed on paper) or by June 30, 2016 (if filed electronically). Employers face penalties of up to \$500 per employee for failing to furnish the form to its employees and the IRS.”

[FASB’s New Lease Requirement Standards Could Impact Your Financial Statements](#)

March 11, 2016

OMA Connections Partner, Clark, Schaefer, Hackett, reports that the Financial Accounting Standards Board (FASB) has issued its long-awaited update revising the proper treatment of leases under U.S. Generally Accepted Accounting Principles (GAAP). This will affect companies that lease real estate, vehicles, construction and manufacturing equipment, and other assets. The standard requires these businesses to recognize most leases on their balance sheets, potentially inflating their reported assets and liabilities. [Read more here.](#)

[OMA Provides Insight to 2020 Tax Policy Study Commission](#)

February 26, 2016

The General Assembly’s 2020 Tax Study Policy Commission held a hearing this week focused on tax expenditures. Tax expenditures are revenues that the state forgoes due to tax exclusions, credits and deductions.

OMA tax counsel, [Mark Engel](#) of Bricker & Eckler, provided a historic review of Ohio business tax policy and OMA’s perspective on tax expenditures.

In his testimony Mr. Engel explained how tax carve outs and credits taken against the commercial activity tax (CAT) have more than doubled from \$300 million to more than \$600 million since the CAT’s enactment in 2005. He said, “The erosion of the tax reform legislation, in the form of carve-outs, exclusions, and ear-marks, reduces certainty, creates disparity by selecting winners and losers, renders the tax code more complicated, and reduces transparency as it becomes more difficult to determine who is entitled to which exclusions.”

His testimony also supported the tax policy and principles of the manufacturing exemption to the sales and use tax: “The taxation of business inputs should be avoided because doing so leads to multiple levels

of taxation and economic disadvantages.” [You can read all of Mr. Engel’s testimony here.](#)

[Eligible Businesses Can Claim Research Credit to Offset Alternative Minimum Tax](#)

February 5, 2016

If your business is working to create new or improved products or processes, and has historically been susceptible to the alternative minimum tax, 2016 may just be a game changing year for your research credit. [Read more](#) from OMA Connections Partner, Tax Credits Group.

[Bill to Eliminate Sales Tax on Temp. Employment Services Gets More Support](#)

January 29, 2016

This week, the House Economic and Workforce Development Committee heard more proponent testimony for House Bill 343, which would eliminate sales tax on temporary employment services. [NFIB](#) and the [Associated Builders and Contractors](#) offered their support of the bill.

This is sound policy. Use the easy email tools at the [OMA Manufacturing Advocacy Center](#) to ask House committee members to advance the bill.

[OMA Testifies on Ohio Tax Policy](#)

January 22, 2016

OMA tax counsel, [Mark Engel](#) of Bricker & Eckler, testified [this week](#) before the House 2020 Tax Committee, which is charged with taking a long-term view of Ohio tax policy and opportunities to improve it.

Reflecting on tax policy reforms of the past few years, Engel said: “Major tax reforms approved by the Ohio General Assembly in 2005 and additional reforms from 2011-2015 have led to significant improvements to a tax system that was for many years widely regarded as outdated. Reforms included reducing overall tax rates, eliminating tax on investment, broadening the tax base, providing more stable and predictable revenues, and simplifying compliance.

“The elimination of the tangible personal property tax, the corporate franchise tax, and the estate tax has strengthened the competitiveness of Ohio’s tax system. So has the reduction of the personal income tax rate as well as the creation of a broad-based, low-rate commercial activity tax.”

He reviewed Ohio's mix of business taxes and urged caution in paying for lowering one type of tax by raising another. He also called for elimination of the sales tax on employment services and on industrial janitorial and maintenance services.

FASB's Technical Agenda for 2016

January 15, 2016

Upcoming changes to the accounting standards might affect the information you report on your company's financial statements, including how it's presented and what details are disclosed.

The Financial Accounting Standards Board (FASB) establishes the standards for public and private companies to follow when they issue financial statements in accordance with U.S. Generally Accepted Accounting Principles (GAAP).

[Here's an overview](#) from OMA Connections Partner, Clark, Schaefer, Hackett, of what the FASB is currently working on.

Congress Makes R&D Tax Credit Permanent

January 8, 2016

OMA Connections Partner, Tax Credit Group, [reported](#) that after more than three decades of year-to-year uncertainty, Congress has made the R&D tax credit permanent as the result of passage of the [Protecting Americans from Tax Hikes \(PATH\) Act of 2015](#).

The congressional deal also brings back the concept of an "AMT turnoff" which allows small businesses to take the R&D tax credit against their alternative minimum tax liability.

And Gives this Sack of Business Tax "Gifts"

January 8, 2016

OMA Connections Partner, Clark Schaefer Hackett, [breaks down](#) several provisions in particular of the Protecting Americans from Tax Hikes Act of 2015 (the PATH Act) that may produce significant tax savings for businesses in 2015 and beyond. President Obama signed the act into law on December 18, 2015.

Many popular tax breaks — including some highly valued by businesses — become permanent, while others are extended through 2016 or 2019.

OMA members who manufacture medical devices will appreciate the halt of the 2.3% excise tax on the sale of medical devices in 2016 and 2017.

2015 ACA Reporting Deadlines Extended

January 8, 2016

And, OMA Connections Partner, Clark, Schaefer, Hackett (CSH), reports that, on December 28, the IRS issued [a notice](#) that extends the 2015 due dates for information that insurers and self-insured employers are required to report to comply with the Affordable Care Act (ACA).

Specifically, the notice provided the following extensions:

- The due date for providing the 2015 forms 1095-B and 1095-C to full-time employees has been extended from January 31, 2016, until March 31, 2016.
- The due date for filing the 2015 forms 1094-B, 1095-B, 1094-C, and 1095-C with the IRS has been extended from February 29, 2016, to May 31, 2016 if not filing electronically, and from March 31, 2016, to June 30, 2016 if filing electronically.

Here's a [webinar-on-demand from CSH](#) about ACA reporting requirements.

The IRS has posted [eight facts about the new ACA information statements](#) that will be issued for insurance offer and coverage by employers and health care coverage providers.

Blank Forms W-2, W-3 & 1099 No Longer at Taxpayer Assistance Centers

January 8, 2016

The IRS says: Don't wait until the last minute to get blank Forms W-2, W-3 or 1099. The demand for paper tax products is declining because of an increase in e-filing and the availability of products online. Therefore, the IRS will no longer stock Forms W-2, W-3 and 1099 in Taxpayer Assistance Centers. The forms, which are used by small business owners, can be ordered online or by telephone and mailed directly to the taxpayer's home or business address.

To order online, go to the IRS' Online Ordering for Information Returns and Employer Returns [website](#). To order by phone, call the IRS at: 1-800-829-3676.

The Social Security Administration also offers an online option to create and file electronic Forms W-2.

File Forms W-2/W-2c and W-3/W-3c electronically by visiting the Social Security Administration's Employer Reporting Instructions and Information [website](#) to create and file electronic fill-in versions of Forms W-2 and W-3.

[JobsOhio and Farm Bureau Talk Taxes to 2020 Tax Policy Commission](#)

December 18, 2015

This week the 2020 Tax Policy Commission, established by the General Assembly, continued hearings on the state's overall tax climate. JobsOhio and the Ohio Farm Bureau offered testimony about how their constituents are impacted by Ohio tax policy.

John Minor, President and CIO of JobsOhio, [said](#), "... we target industries that help drive the state's economy and provide job growth opportunities; industries like advanced manufacturing, biohealth, food processing, IT, automotive and aerospace, financial services and shale energy."

Brandon Kern, Director of State Policy, Ohio Farm Bureau [provided an overview](#) of how various Ohio taxes impact farmers. He used the opportunity to describe how the Current Agricultural Use Valuation tax (CAUV), which measures the value of land for its agricultural use, could be improved. Mr. Kern noted that most Ohio farmers are not excessively negatively impacted by the commercial activity tax.

[Taxpayers Rejoice over Proposed R&D Credit Legislation](#)

December 18, 2015

OMA Connections Partner, Tax Credit Group, reports that the Consolidated Appropriations Act of 2016 contains a provision for a permanent research and development tax credit. In addition, new rules would allow taxpayers with gross receipts less than \$50 million dollars to utilize the credit to offset Alternative Minimum Tax liability.

Also, for certain startup phase businesses, the credit could be used to offset payroll tax liability. ([Click here to learn more about the proposed legislation.](#))

With these new provisions included in this legislation, there will be a massive expansion of companies who can now take advantage of this incentive. [Read more](#) from Tax Credit Group.

Additionally, OMA Connections Partner, GBQ Partners, [reports which provisions](#) may become permanent or just extended.

[House Continues to Debate Sales Tax on Temporary Workers](#)

December 4, 2015

This week the House Economic and Workforce Development Committee continued its debate on [House Bill 343](#). The bill, supported by the OMA, would eliminate the state sales tax on temporary employees.

Opponents, including local governments, liberal think tanks, and social advocates, offered testimony this week. They expressed concerns ranging from an increase in the temporary workforce to less funding for local governments. Here's the opponent testimony of [Policy Matters Ohio](#) and the [County Commissioners Association of Ohio](#).

Committee members pushed back and questioned why the tax was ever assessed in the first place and reiterated it is harmful to Ohio's competitiveness.

Taxation Legislation

Prepared by: The Ohio Manufacturers' Association
Report created on April 15, 2016

- HB9** **TAX EXPENDITURE REVIEW COMMITTEE** (BOOSE T) To create a Tax Expenditure Review Committee for the purpose of periodically reviewing existing and proposed tax expenditures.
Current Status: 2/23/2016 - Senate Ways and Means, (Third Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-9>
- HB12** **TIF-INCENTIVE DISTRICTS** (BUTLER, JR. J, BURKLEY T) To establish a procedure by which political subdivisions proposing a tax increment financing (TIF) incentive district are required to provide notice to the record owner of each parcel within the proposed incentive district before creating the district.
Current Status: 2/16/2016 - House Ways and Means, (Third Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-12>
- HB19** **INTERNAL REVENUE CODE** (SCHERER G) To expressly incorporate changes in the Internal Revenue Code since March 22, 2013 into Ohio law and to declare an emergency.
Current Status: 4/1/2015 - **SIGNED BY GOVERNOR**; eff. 4/1/2015
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-19>
- HB26** **COIN SALES-USE TAX EXEMPTION** (MAAG R, HAGAN C) To exempt from sales and use taxes the sale or use of investment metal bullion and coins.
Current Status: 11/18/2015 - Senate Ways and Means, (First Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-26>
- HB32** **AIRCRAFT-MOTOR FUEL EXCISE TAX** (PERALES R) To subject the receipt of motor fuel used to operate aircraft to the motor fuel excise taxes rather than the sales and use taxes and to require a percentage of motor fuel excise tax revenue to be used for airport improvements.
Current Status: 2/10/2015 - Referred to Committee House Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-32>
- HB64** **OPERATING BUDGET** (SMITH R) To make operating appropriations for the biennium beginning July 1, 2015, and ending June 30, 2017, and to provide authorization and conditions for the operation of state programs.
Current Status: 6/30/2015 - **SIGNED BY GOVERNOR**; eff. 6/30/15; certain provisions effective 9/29/2015, other dates
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-64>
- HB65** **TAX-EXPENDITURE APPRAISAL** (DRIEHAUS D) To provide for the periodic appraisal of the effectiveness of tax expenditures.
Current Status: 3/24/2015 - House Ways and Means, (First Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-65>

- HB84** **MUNICIPAL TAX-CIVIL ACTIONS** (SPRAGUE R, SWEENEY M) To require civil actions by taxpayers related to municipal income taxes be brought against the municipal corporation imposing the tax rather than the municipal corporation's tax administrator.
Current Status: 3/24/2015 - House Ways and Means, (First Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-84>
- HB99** **INCOME TAX-SCHOOL FUNDING** (CURTIN M) To require that an amount equal to state income tax collections, less amounts contributed to the Ohio political party fund via the income tax checkoff, be distributed for the support of elementary, secondary, vocational, and special education programs.
Current Status: 5/5/2015 - House Ways and Means, (Second Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-99>
- HB102** **VETERAN-OWNED BUSINESSES** (CRAIG H, ANTANI N) To provide a bid preference for state contracts to a veteran-owned business and to authorize a personal income and commercial activity tax credit for a business that hires and employs a veteran for at least one year.
Current Status: 4/28/2015 - House Ways and Means, (First Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-102>
- HB162** **SEVERANCE TAX RATES** (CERA J) To change the basis, rates, and revenue distribution of the severance tax on oil and gas, to create a grant program to encourage compressed natural gas as a motor vehicle fuel, to authorize an income tax credit for landowners holding an oil or gas royalty interest, and to exclude some oil and gas sale receipts from the commercial activity tax base.
Current Status: 5/12/2015 - House Ways and Means, (First Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-162>
- HB176** **GAS-FUEL CONVERSION PROGRAM** (HALL D, O'BRIEN S) To create the Gaseous Fuel Vehicle Conversion Program, to allow a credit against the income or commercial activity tax for the purchase or conversion of an alternative fuel vehicle, to reduce the amount of sales tax due on the purchase or lease of a qualifying electric vehicle by up to \$500, to apply the motor fuel tax to the distribution or sale of compressed natural gas, to authorize a temporary, partial motor fuel tax exemption for sales of compressed natural gas used as motor fuel, and to make an appropriation.
Current Status: 11/18/2015 - **REPORTED OUT**, House Finance, (First Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-176>
- HB232** **SELLER-USE TAX COLLECTION** (GROSSMAN C, SCHERER G) To prescribe new criteria for determining whether sellers are presumed to have substantial nexus with Ohio and therefore required to register to collect use tax, to allow sellers presumed to have substantial nexus to rebut that presumption, and to require a person, before the person enters into a sale of goods contract with the state, to register, along with the person's affiliates, to collect use tax.
Current Status: 6/2/2015 - Referred to Committee House Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-232>

- HB269** **INCOME TAX-SOUND RECORDING** (SMITH K, LATOURETTE S) To authorize a refundable income tax credit for individual investors in a sound recording production company equal to a portion of the company's costs for a recording production or recording infrastructure project in Ohio.
Current Status: 2/16/2016 - House Ways and Means, (Second Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-269>
- HB280** **BALANCED BUDGET COMPACT** (KRAUS S, KOEHLER K) To adopt the Compact for a Balanced Budget and to declare an emergency.
Current Status: 6/30/2015 - Introduced
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-280>
- HB308** **TEXTBOOKS-TAX EXEMPTION** (DUFFEY M, STINZIANO M) To exempt from sales and use tax textbooks purchased by post-secondary students.
Current Status: 10/21/2015 - House Ways and Means, (First Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-308>
- HB326** **TAX LAW-JOINT FILING** (AMSTUTZ R, MCCLAIN J) To make technical changes to the state income tax law, to modify the requirements for receiving the joint filing credit, and to provide that, for the 2015 taxable year, any taxable business income under \$125,000 for married taxpayers filing separately or \$250,000 for other taxpayers is subject to the graduated tax rates applicable to nonbusiness income, while business income in excess of those amounts remains subject to the existing 3% flat tax.
Current Status: 10/26/2015 - House Ways and Means, (Fifth Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-326>
- HB343** **EMPLOYMENT SERVICES-TAX EXEMPT** (YOUNG R, ROMANCHUK M) To exempt employment services and employment placement services from sales and use tax.
Current Status: 2/24/2016 - House Economic and Workforce Development, (Seventh Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-343>
- HB358** **TAX DEDUCTION-SAVINGS ACCOUNTS** (DEVER J, CONDITT M) To allow an income tax deduction for contributions to ABLE savings accounts.
Current Status: 4/19/2016 - House Ways and Means, (Second Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-358>
- HB369** **BALANCED BUDGET COMPACT** (KOEHLER K, HAMBLEY S) To adopt the Compact for a Balanced Budget and to declare an emergency.
Current Status: 2/9/2016 - House Government Accountability and Oversight, (Second Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-369>
- HB390** **NATURAL GAS-TAX EXEMPTION** (SCHAFFER T, RETHERFORD W) To exempt the sale of natural gas by a municipal gas company from the sales and use tax.

Current Status: 4/12/2016 - Referred to Committee Senate Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-390>

HB398 CAUV COMPUTATION (HILL B) To require that the computation of the capitalization rate for the purposes of determining CAUV of agricultural land be computed using a method that excludes appreciation and equity buildup.

Current Status: 4/19/2016 - House Government Accountability and Oversight, (First Hearing)

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-398>

HB454 SALES TAX HOLIDAY-PERMANENT (PATTERSON J) To provide for a permanent three-day sales tax "holiday" each August during which sales of back-to-school clothing and school supplies are exempt from sales and use taxes.

Current Status: 2/23/2016 - Referred to Committee House Ways and Means

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-454>

HB466 TAX-EXEMPT-DIGITAL ADVERTISING (SMITH R) To specifically exempt digital advertising services from sales and use tax.

Current Status: 4/12/2016 - House Ways and Means, (First Hearing)

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-466>

HB467 UNEMPLOYMENT COMPENSATION FUND (BUTLER, JR. J) To establish a loan from the Budget Stabilization Fund to the Unemployment Compensation Fund, to require the Director of Job and Family Services to recommend a program to incentivize the purchase of private unemployment insurance, and to require a study on the solvency of the Unemployment Compensation Fund.

Current Status: 4/13/2016 - Referred to Committee House Insurance

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-467>

HB473 UTILITY SERVICE TAX-LEVY (AMSTUTZ R) To require voter approval before a county may levy a new utilities services tax, to allow small businesses to count employees of related or affiliated entities towards satisfying the employment criteria of the business investment tax credit, to permit a bad debt refund for cigarette and tobacco product excise taxes paid when a purchaser fails to pay a dealer for the cigarettes or tobacco products and the unpaid amount is charged off as uncollectible by the dealer.

Current Status: 4/13/2016 - Referred to Committee House Ways and Means

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-473>

HB475 MOTION PICTURE-TAX CREDIT (SCHURING K) To authorize motion picture companies to transfer the authority to claim refundable motion picture tax credits to other persons, to adjust how the credit is calculated, to increase the total amount of credits that may be awarded per year, to remove the limit on the maximum credit amount that may be awarded to a motion picture, and to create a job training program for resident film crew members.

Current Status: 4/13/2016 - Referred to Committee House Finance

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-475>

- HB484** **TAX-EXEMPT PRODUCTS** (SYKES E, CERA J) To exempt from sales and use tax the sale of nonprescription human drugs, feminine hygiene products associated with menstruation, and disposable baby diapers, to reimburse the Local Government Fund and Public Library Fund and county and transit sales and use tax collections for any revenue lost due to those exemptions, and to create the Legislative Commission on Middle Class Economic Strength to study proposed income, sales, or use tax legislation that changes the proportionate tax burden among income classes or other classes.
Current Status: 4/13/2016 - Referred to Committee House Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-484>
- HB485** **INCOME TAX DEDUCTION-TUITION** (RAMOS D) To reinstate the state income tax deduction for qualified higher education tuition and fee payments that expired December 31, 2005.
Current Status: 4/13/2016 - Referred to Committee House Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-485>
- HB489** **MINE FUNDS** (CERA J) To credit a portion of the money derived from the Kilowatt-Hour Tax Receipts Fund to the Abandoned Mine Reclamation Fund, the Acid Mine Drainage Abatement and Treatment Fund, and the Mine Safety Fund and to make other changes to those funds.
Current Status: 4/13/2016 - Referred to Committee House Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-489>
- HB491** **TAX CREDIT-PILOT PROGRAM** (ANIELSKI M) To establish a five-year pilot program whereby taxpayers with facilities in this state with activated foreign trade zone status may claim a nonrefundable commercial activity tax credit equal to the amount redeployed by the taxpayer to job creation or other specified projects.
Current Status: 4/13/2016 - Referred to Committee House Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-491>
- HB492** **CAPITAL IMPROVEMENT-PILOT** (ROGERS J, DRIEHAUS D) To create the Supplemental State Capital Improvements Pilot Program funded by a temporary transfer from the Budget Stabilization Fund and to make an appropriation.
Current Status: 4/13/2016 - Referred to Committee House Finance
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-492>
- HB515** **HEATING FUELS-SALES TAX** (PATTERSON J, CERA J) To exempt from sales and use taxation the bulk sale of firewood and certain other heating fuels, and to reimburse the Local Government Fund and Public Library Fund and county and transit sales tax collections for the resulting revenue losses.
Current Status: 4/12/2016 - Introduced
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-HB-515>
- SB2** **INTERNAL REVENUE SERVICE-INCORPORATE CHANGES** (PETERSON B) To expressly incorporate changes in the Internal Revenue Code since March 22, 2013, into

Ohio law, and to declare an emergency.

Current Status: 2/14/2016 - **SIGNED BY GOVERNOR**; eff. 2/14/2016

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-2>

- SB12** **INCOME TAX CREDIT-SCIENCE RELATED DEGREE (HOTTINGER J)** To grant an income tax credit to individuals who earn degrees in science, technology, engineering, or math-based fields of study.
Current Status: 2/4/2015 - Referred to Committee Senate Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-12>
- SB18** **TAX CREDIT-NATIONAL GUARD EMPLOYMENT (GENTILE L)** To authorize a refundable income tax credit for employers that hire one or more qualified veterans or members of the National Guard or reserves.
Current Status: 2/4/2015 - Referred to Committee Senate Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-18>
- SB21** **EARNED INCOME TAX CREDIT RESTRICTION (SKINDELL M)** To remove the income restriction on the earned income tax credit and to make the credit refundable beginning in 2015.
Current Status: 2/4/2015 - Referred to Committee Senate Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-21>
- SB40** **ECONOMIC DEVELOPMENT TAX CREDIT (BEAGLE B)** To authorize tax credits for contributions of money to economic and infrastructure development projects undertaken by local governments and non-profit corporations.
Current Status: 6/10/2015 - Senate Ways and Means, (First Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-40>
- SB41** **NEW MARKETS TAX CREDIT QUALIFICATIONS (BEAGLE B, TAVARES C)** To modify the qualifications for the New Markets Tax Credit and the schedule for receiving the credit.
Current Status: 6/3/2015 - Senate Ways and Means, (First Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-41>
- SB52** **AIRCRAFT FUEL EXCISE TAX (BEAGLE B)** To subject the receipt of motor fuel used to operate aircraft to the motor fuel excise taxes rather than the sales and use taxes and to require a percentage of motor fuel excise tax revenue to be used for airport improvements.
Current Status: 2/18/2015 - Referred to Committee Senate Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-52>
- SB88** **FELON EMPLOYMENT TAX CREDIT (TAVARES C, THOMAS C)** To create a tax credit for the employment of individuals who have been convicted of criminal offenses.
Current Status: 3/4/2015 - Referred to Committee Senate Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-88>

- SB100 SALES TAX HOLIDAY-ENERGY STAR (BROWN E)** To provide a three-day sales tax "holiday" each April during which sales of qualifying Energy Star products are exempt from sales and use taxes.
Current Status: 3/4/2015 - Referred to Committee Senate Ways and Means
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-100>
- SB198 NON-RESIDENT MUNICIPAL INCOME TAX (JORDAN K)** To prohibit municipal corporations from levying an income tax on nonresidents' compensation for personal services or on net profits from a sole proprietorship owned by a nonresident.
Current Status: 9/29/2015 - Senate State and Local Government, (First Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-198>
- SB208 STATE INCOME TAX (BEAGLE B)** To make technical changes to the state income tax law, to modify the requirements for receiving the joint filing credit.
Current Status: 11/15/2015 - **SIGNED BY GOVERNOR**; Eff. 2/15/2016, Certain provisions effective 11/15/2015
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-208>
- SB209 OHIO RURAL JOBS ACT (HITE C)** To enact the "Ohio Rural Jobs Act" which authorizes a nonrefundable tax credit for insurance companies that invest in rural business growth funds, which are certified to provide capital to rural and agricultural businesses.
Current Status: 12/8/2015 - House Agriculture and Rural Development, (Second Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-209>
- SB235 INCREASED VALUE-PROPERTY TAX (BEAGLE B, COLEY W)** To exempt from property tax the increased value of property on which industrial or commercial development is planned until construction of new commercial or industrial facilities at the property commences.
Current Status: 4/20/2016 - Senate Ways and Means, (Fifth Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-235>
- SB246 CAUV COMPUTATION-CAPITALIZATION RATE (HITE C)** To require that the computation of the capitalization rate for the purposes of determining CAUV of agricultural land be computed using a method that excludes appreciation and equity buildup.
Current Status: 4/20/2016 - Senate Ways and Means, (Third Hearing)
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-246>
- SB260 CAPITAL REAPPROPRIATIONS (COLEY W)** To make capital appropriations for the biennium ending June 30, 2018.
Current Status: 2/21/2016 - **SIGNED BY GOVERNOR**; eff. 7/1/2016
State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-260>
- SB288 INCOME TAX-PASS THROUGH ENTITIES (EKLUND J)** To revise the law governing how taxes on income from pass-through entities is to be reported and paid by the entities and

their investors.

Current Status: 4/13/2016 - Senate Ways and Means, (Second Hearing)

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-288>

SB289 **MOTION PICTURE TAX CREDIT (PATTON T)** To increase the overall cap on the motion picture tax credit from \$40 million per fiscal biennium to \$100 million for the current fiscal biennium and \$160 million for all subsequent biennia.

Current Status: 4/12/2016 - Referred to Committee Senate Ways and Means

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-289>

SB302 **PROPERTY TAX EXEMPTION-MILITARY VETERANS-DISABLED (SCHIAVONI J, GENTILE L)** To exempt from property taxation the primary residence of military veterans who are disabled.

Current Status: 4/12/2016 - Referred to Committee Senate Ways and Means

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-302>

SB305 **TAX CERTIFICATES-SALE PROHIBITION (WILLIAMS S)** To prohibit the sale of tax certificates for parcels owned by a person sixty-five years of age or older and that include the primary residence of the owner.

Current Status: 4/12/2016 - Referred to Committee Senate Ways and Means

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-305>

SB310 **CAPITAL APPROPRIATIONS (OELSLAGER S)** To make capital appropriations and changes to the law governing capital projects for the biennium ending June 30, 2018.

Current Status: 4/19/2016 - Senate Finance, (Second Hearing)

State Bill Page: <https://www.legislature.ohio.gov/legislation/legislation-summary?id=GA131-SB-310>