

TAX REFORM IN OHIO

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Tax Reform

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Overview

From the vantage point of early 2003, the fiscal situation looks dark for state governments across the country. Tax revenues fell precipitously when the economy moved into the recent recession, and they have yet to recover. State spending on Medicaid continues to soar. Spending for prisons and education is growing rapidly. To balance their budgets, states have spent their rainy day balances, used one-time money such as tobacco funds, increased some taxes, and significantly cut spending. Even after all that, they continue to face huge deficits in the next two fiscal years. Recent surveys suggest that the average state deficit for FY 2004 is in the range of 13 percent to 18 percent of general fund revenues.

After this litany of woes, the prospect is not entirely grim. The flip side of these budget challenges is opportunity. As they meet the current crisis, states have an opportunity to get their fiscal houses in order for the long term. One of the ways that they can do so is to reform and modernize their tax systems. The time for fundamental tax reform in the states, including Ohio, has arrived.

At this point in our history, Ohio's tax system, like those in many states, remains firmly rooted in the prior century. It was built to reflect an economy that traded almost exclusively in goods; an economy where capital had limited mobility and sophisticated tax-planning techniques had not evolved; and an economy where individual industries had their own peculiar accounting practices and regulatory structure and so required special tax treatment.

The economy, accounting practices, financial practices, and business structure have all changed radically from the time when the structure of Ohio's tax system was created. Much more of the value generated in today's economy emanates from services. Capital is mobile between states and even between countries. As recent disclosures of corporate practices have revealed, corporate structure has become much more complicated. In today's economy, a web of affiliated corporations, partnerships, and other business entities make it easy for businesses to enter into sophisticated transactions in such a way as to dramatically minimize their tax liability. Many of the regulatory and accounting barriers that existed between industries have fallen through the deregulation process. Now, services that were once the exclusive domain of a particular type of company are provided by various types of companies, many of which did not exist when Ohio's tax structure was designed. Finally, business is more mobile and fast-paced.

What is the result of the changes in the economy, in accounting practices, in financial practices, and in business structure, without parallel changes in the tax system?

- Some sectors of the economy - e.g., goods-producing sectors - are relatively overtaxed, while the ever-growing service sector is lightly taxed;
- Some corporations pay high income taxes while other corporations, through the use of complicated structures and sophisticated transactions, pay very little or no tax;
- Different companies that provide the same services are taxed differently; and
- The tax system fails to generate sufficient revenues to pay for the government services that the public desires and expects.

Overall, the Ohio tax system no longer meets the five guiding principles of a quality state and local tax structure: simplicity, equity, stability, neutrality, and competitiveness. Ohio's tax system should take into account and balance the following principles, widely accepted as key elements of a quality tax system.

- **SIMPLICITY.** Our tax system should facilitate taxpayer compliance by being easy to understand and easy to administer. It should also minimize compliance costs for taxpayers and administrative costs of state and local governments.
- **EQUITY AND FAIRNESS.** Our tax system should promote horizontal equity by imposing similar tax burdens on similarly situated taxpayers. It should also promote vertical equity by recognizing differing abilities to pay. Further, it should fairly distribute tax liabilities across all sectors of the economy.

- **STABLE AND SUFFICIENT REVENUE.** Our tax system exists to provide revenues that fund government services. It should provide adequate revenues to fund those services in both good and bad economic times.
- **NEUTRALITY.** Our tax system should not unduly influence economic behavior, causing taxpayers to make economic decisions primarily due to tax reasons.
- **COMPETITIVENESS.** Our state's tax system represents a meaningful part of a state's living, working, and business environment. It should not impose an excess burden on taxpayers, particularly as compared to the tax systems of other states.

At times these principles may conflict or compete with each other. For example, we may sacrifice some simplicity in the interest of equity. Other over-riding policy considerations may take precedence over one or more of these principles in any particular case. Still, these principles of a quality tax system provide the basic standard for the consideration of reforming and modernizing Ohio's tax law.

This budget starts Ohio on the path of fundamental tax reform. The overriding theme of this reform is *to broaden the tax base and lower the tax rates.* This approach satisfies all five of the guiding principles of a quality tax system. A broader tax base simplifies the tax system by eliminating hard to understand exceptions about the applicability of the tax system. This also enhances equity, because special interest carve-outs, favoring one industry over another or one set of taxpayers over another are eliminated. The stability of the revenue system is improved because a broader base is less subject to economic pressures and cycles. By adopting a broader tax base and lower tax rate, the incentive to enter into complex legal structures and sophisticated tax planning is mitigated. Finally, a broader base and lower tax rates makes Ohio more competitive with other states that currently impose lower tax rates.

The specific tax reform proposals in this budget are concentrated in four primary areas.

1. **Corporation Franchise Tax Reform:** The tax reform package seeks to shore up the eroding corporate franchise tax, making it fairer—particularly among corporations of different sizes and compositions—and more productive. In the long term, the base broadening efforts are combined with tax rate reductions.
2. **Sales & Use Tax Reform:** The tax reform package seeks to ensure the long-term integrity of the sales and use tax system by modernizing the tax and capturing a portion of the growing service economy.
3. **Personal Income Tax Reform:** The tax reform package seeks to broaden the personal income tax base and reduce all state income tax rates. This will ensure the ability of Ohio to attract high-wage jobs, which benefits all Ohioans and Ohio's overall economy.
4. **Municipal Income Tax Reform & Simplification:** The tax reform package seeks to reduce the anti-competitive aspects of Ohio's municipal income tax system while preserving the local authority for cities to enforce their tax laws and enact their own tax rates.

As part of this tax reform, various special tax treatments for particular industries are eliminated in an effort to modernize the tax code and place members of these industries on more equal tax footing. Other parts of the tax system are also improved by providing a series of administrative changes to improve Ohio's tax system.

Corporation Franchise Tax Reform

Nowhere is the need for tax reform that is rooted in base broadening and rate reduction so stark as in the state's corporation franchise tax. A telling statistic supporting this view was brought up during the deliberations of the Committee to Study State and Local Taxes. FY 1999 data from the U.S. Bureau of the Census shows that Ohio's state and local corporate taxes on income equaled \$67 per capita, while the national average was \$124 per capita. All of Ohio's five neighboring states have higher per-capita corporate income tax collections, despite the fact that Indiana and Kentucky have lower top rates. Clearly, Ohio's current corporate income tax has fairly high rates but relatively low revenue production.

The corporation franchise tax has also been steadily dwindling as a percentage of total tax revenue. Despite industry rhetoric that the decline in the franchise tax is due to low profitability, a look at collections over 25 years shows that the revenue production of the tax is in the late stages of a long-term decline. Corporation franchise tax revenue has declined from about 16 percent of total General Revenue Fund (GRF) revenue in FY 1977 to less than 5 percent in FY 2002.

There are a number of ways that tax reform could conceivably broaden the tax base. The proposed reform package concentrates on disallowing the tax benefit from various types of complex legal structures and sophisticated tax

planning transactions. Currently, multi-state corporations are using these tax planning techniques to shift income earned in Ohio out of state. For example, under Ohio's current tax structure, larger businesses with multiple tiers of affiliated corporations can effectively pick and choose which affiliates pay Ohio taxes.

The current system advantages large corporate taxpayers with money to spend on sophisticated tax planning, leaving midsize and small corporate taxpayers to "pick up the tab" for the franchise tax. By making changes that essentially disallow these sorts of shifting of income among related corporations for tax planning purposes, the proposed reform improves the fairness of the corporate franchise tax and significantly broadens the base of the tax. Rather than adopting a unitary tax base, the tax reform proposal permits corporations to include in their tax return the same entities included in their federal consolidated tax returns. If a taxpayer does not want to make this "Federal Consolidated Return Election," the group may file on a separate legal entity basis. However, if filing separately, related entity expenses are disallowed. The impact of the disallowance is limited to the tax incurred "as if" the related members filed a combined tax return. Research shows that other states with broad based approaches to corporate taxation, such as in this proposal, are not disadvantaged when it comes to attracting and retaining businesses in the state.

The tax base is also expanded by modernizing the tax code to reflect current economic realities. For example, the tax reform proposal strives to place members of recently deregulated industries, such as the telecommunication industry, on a level playing field for tax purposes by treating local telephone companies in a manner consistent with their competitors. Similarly, it strives to place the financial industry on equal footing by eliminating the antiquated dealers in intangibles tax.

The tax reform proposal adopts the Uniform Division of Income for Tax Purposes Act to apportion and allocate corporate income. With this change, business income is apportioned using a business' property, payroll and sales; nonbusiness income is allocated to the location the income is generated. Currently, most states adopt this approach for corporate tax purposes. Further, Ohio uses this method for businesses taxed under the personal income tax (i.e., S corporations, partnerships and other flow-through entities). As a result, the proposal places corporations and flow-through entities on a level playing field for tax purposes.

The reform package offsets the expansion of the corporate income tax base with tax rate reductions. The current top rate of 8.5% would be reduced to 8.0% in taxable year 2004, 7.5% in taxable year 2005, and 7.0% in taxable year 2006. The corporate tax rate would thus be slightly higher than the top personal income tax rate (see section on Personal Income Tax Reform). Making the top rates of the corporate tax and the personal income tax roughly equal should remove the tax rate differential as an issue in choosing the form of business organization. That is, the rate should no longer be a driving factor in a business's decision to be a C corporation, an S corporation, a partnership, or an LLC. This improves the neutrality of the tax system. Further, the proposal shifts to a flat rate system by eliminating the 5.1% tax rate bracket. Only 12 other states use a bracketed tax system for corporate income tax purposes.

The tax reform package also improves the net worth component of the corporation franchise tax. The current system, in which all taxpayers paying on the net worth basis pay the same tax rate, but the largest taxpayers have their tax capped, is unfair to small and mid-size net worth taxpayers. The proposal increases the net worth cap from \$150,000 to \$500,000, but also decreases the net worth tax rate on the vast majority of net worth taxpayers. The proposed change improves the stability of the tax and enhances both the horizontal equity and vertical equity of the tax structure. This change also improves the competitiveness of small start-up companies that are vital to the state's future economic growth.

Finally, the tax reform package adjusts the minimum tax imposed by the corporation franchise tax. The minimum tax is only imposed on corporations that have zero (or close to zero) liability under both the net income and net worth tax calculation. In 1960, the minimum tax rate was set at \$50. By applying annual inflation since 1960, the minimum tax is reset to \$300.

Sales and Use Tax Reform

The proposed sales and use tax reform conforms Ohio's system to the five guiding principles of a quality tax system. The sales tax reform proposal broadens the tax base in two ways:

- Eliminates a number of existing exemptions and special interest carve-outs; and
- Extends the sales and use tax to a wider group of services.

Both of these efforts, particularly the inclusion of additional services, change the tax system to more closely match the economy of today, rather than the economy of 65 years ago (the tax was enacted in the mid-1930s). The federal Bureau of Economic Analysis (BEA), in a paper in the March 2001 issue of the *Survey of Current Business*, reported the following findings:

- Services' share of U.S. consumer spending rose from 40 percent in 1959 to 58 percent in 2000. The increase was primarily in medical care services, financial services, recreation services, and education and research services;
- The increased share of spending for recreation services partly reflects increased affluence of households, which supports spending for newly available services like cable television;
- Nondurable goods' share of U.S. consumer spending fell from 47 percent in 1959 to 30 percent in 2000;
- Durable goods share of U.S. consumer spending fell only slightly, from 13 percent in 1959 to 12 percent in 2000, although spending changed quite a bit within the durable goods category.

The proposed sales tax reform protects from taxation medical care, education, or research services. Instead, it generally concentrates on extending the sales tax to recreation services and financial services, and eliminates many special interest exemptions and exceptions from the tax.

With a broader tax base and the adoption of the Streamlined Sales Tax System, Ohio's sales and use tax system is greatly simplified.

The proposed reform enhances neutrality by partially rectifying the current distortions that arise from having most of the goods sector subject to the sales tax, while most of the service sector is exempt. While the average combined state and local sales tax rate of 6 percent is not particularly high, the difference in treatment between the goods and services sectors distorts decision making by economic actors, favoring the purchase of services over the purchase of goods.

The proposed reform enhances equity in two ways. With respect to horizontal equity, taxpayers who currently have similar income levels, but who have different purchasing patterns (e.g. some taxpayers purchase more goods and some purchase more services) are treated differently under the sales tax. By applying the sales tax to more services, the proposed reform ameliorates this inequity. With respect to vertical equity, the imposition of the tax on additional services will reduce the regressivity of the current sales tax structure, because services generally comprise a higher percentage of spending for higher income households.

Broadening the tax base will also have a positive impact on local governments and ensure their fiscal stability.

While the proposal does not incorporate a reduction of the sales and use tax rate, it does forestall future tax rate increases. Indeed, the recent history of state and local governments across the country has been to narrow the sales and use tax base and increase the rates. This history of narrowing bases and increasing rates is described clearly in a September, 2001 paper by Professors William Fox and Donald Bruce of the University of Tennessee. Their research contains the following findings:

- State and local sales tax bases are shrinking for three reasons: the expanded use of untaxed services, the increased use of sales tax exemptions, and the growth of remote sales. Remote sales include e-commerce (Internet), telephone, and catalogue sales.
- States have responded to the narrowing tax bases by raising tax rates, although the extent of a direct relationship has not been carefully studied. For the average sales-taxing state, the tax base equaled 51.4 percent of the state's personal income in 1979, but had fallen to 42.0 percent in 2000.
- The median state sales tax rate increased from 3.25 percent in 1970 to 4.0 percent in 1980 and to 5.0 percent in 1990.

In Ohio, the state sales tax rate increased from 3 percent to 4 percent in 1967, and to 5 percent in 1981 during a more recent Ohio fiscal crisis. **The proposed sales tax reform is a huge step toward forestalling another tax rate increase in Ohio, thereby ensuring Ohio's future competitiveness.**

Personal Income Tax Reform

The personal income tax reform proposal both broadens the tax base and lowers the tax rates for all Ohioans.

To ensure the broadest tax base, the proposal makes the taxation of trust income permanent. After 30 years, Ohio recently joined all the other states with broad-based income taxes in taxing the income of trusts that is not distributed in the current year. Under prior Ohio law, the income held in trusts and then distributed in later years was escaping taxation. As a result, wealthier taxpayers could establish trusts to shelter their income from Ohio tax. Recently enacted Am. Sub. S.B. 261 ensured the fairness of Ohio's personal income tax by imposing the tax on this accumulated trust income through tax year 2004.

The income tax reform proposal also reduces all of the state income tax rates over a four-year period.

- In tax year 2005, all but the highest two tax rates are reduced by rounding them down to the nearest 0.1 percent.
- The top income tax rate of 7.5% is phased-down to 6.9% beginning in tax year 2006 and ending in tax year 2008.
- In tax year 2006, the current personal exemptions and \$20 credits are eliminated in favor of a universal credit per return of \$105 (\$210 for married taxpayers) and an additional credit of \$80 per dependent.
- In tax year 2006, the brackets of the joint filer credit are favorably adjusted upward (from \$50,000 and \$75,000 to \$60,000 and \$85,000).
- In tax year 2007, these credits become indexed to inflation.

This dramatic change to Ohio's personal income tax system has the following impacts:

- No taxpayer with Ohio Adjusted Gross Income under \$10,000 will pay income tax.
- 550,000 - 600,000 low-income taxpayers will no longer have any tax liability.
- The highest percentage tax cuts go to the lowest income taxpayers, especially low-income seniors.
- 95% of seniors currently with liability get relief (650,000 taxpayers).
- Over 97% of single parent households currently with liability get relief (480,000 taxpayers).

The plan strives to balance competitiveness and fairness. The Committee to Study State and Local Taxes heard testimony that Ohio's top marginal tax rate of 7.5%, combined with the average city income tax rate of 1.5% percent and any school district income tax, is anti-competitive to Ohio, especially for those looking to do business in Ohio. (Businesses that are not C corporations do not pay the corporation franchise tax; instead their owners pay tax on the business income through the personal income tax system.) The Federation of Tax Administrators (FTA) reports that in 2002 there were only 11 states with top income tax rates above Ohio's top state tax rate of 7.5%.

High income tax rates create an impediment for Ohio to attract high-wage jobs. When Ohio attracts high-wage jobs, all Ohioans benefit from the corresponding growth of the overall economy. However, to ensure that tax relief from the reform proposal is not disproportionately weighted to taxpayers with the highest incomes, the \$105/\$210 per return credit is gradually phased out for taxpayers whose income exceeds \$100,000 (\$200,000 for joint filers). This ensures that the highest percentage tax cuts apply to the lowest-income taxpayers.

The income tax reform plan also enhances neutrality. As stated earlier in the discussion of the corporate tax reform plan, reducing the top corporate tax rate to 7% percent and the top income tax rate to 6.9% substantially eliminates the tax advantages between organizing a business as a C Corporation or as one of the various forms of flow-through business entities (S corporations, partnerships, etc.). Thus, the new tax system will encourage entrepreneurs to choose the best form of business organization for non-tax reasons.

Finally, the proposed income tax rate reductions are a substitute for indexing the tax brackets. The administration took to heart this admonition of the 1982 Ohio Tax Study Committee: "...the Committee rejects indexing of the income tax. Instead, it recommends that the General Assembly periodically review the state's income tax structure to ensure that the effects of inflation do not unfairly distort its burden on taxpayers." Directly reducing the tax rates, then indexing the newly created credits and raising the income brackets for the joint filer credit actually provides more total tax relief than the bracket indexing provision in current law. Further, this accomplishes the significant tax policy objective of making Ohio's personal income tax system more competitive by lowering the tax rates.

Municipal Income Tax Reform & Simplification

Ohio businesses that operate in any number of the 541 Ohio cities and villages that have an income tax face an onerous compliance burden, multiple filing deadlines, differing tax rates and inconsistent rules. In some cases, the

cost of compliance exceeds the tax liability. This burden is not only borne by larger businesses with multiple locations throughout Ohio, but also by smaller businesses that provide services throughout an urban area (such as construction contractors, repair services, etc.).

The tax reform proposal makes a number of common sense reforms that will reduce the compliance burden for business taxpayers without significantly impacting the fiscal ability of Ohio's 541 municipal corporations that levy the tax.

The tax reform proposal would make the following reforms to the municipal income tax:

- Institute a common definition of taxable income for the municipal net profits tax.
- Institute a common definition of the withholding tax base, which employers use with regard to their employees' withheld personal income tax.
- Institute a uniform due date of April 15 for tax returns, with extensions to run until October 31.
- Allow business taxpayers to file and remit their municipal net profits tax returns through the *Ohio Business Gateway*, starting in taxable year 2005. Revenues would be distributed directly to each municipality, and each municipality would retain all administrative, audit and enforcement responsibilities.
- Similarly, allow business taxpayers to file and remit their municipal withholding tax through the *Ohio Business Gateway*, starting in taxable year 2007. Revenues would be distributed directly to each municipality, and each municipality would retain all administrative, audit and enforcement responsibilities.
- Allow centralized electronic filing of extension requests by businesses through the *Ohio Business Gateway*, that would be accessible to all Ohio municipalities for compliance review purposes.
- Reform municipal income tax appeal procedures to conform to other state and local taxes. Appeals would first go to the required municipal administrative appeal, then to the Board of Tax Appeals, and then to the State District Court of Appeals or to the Ohio Supreme Court.
- Protect municipal income tax revenues by instituting an anti-passive investment company (anti-PIC) add-back for the municipal net profits tax. This measure is necessary to thwart aggressive tax planning techniques and is analogous to the anti-PIC add-back in state tax law.
- Institute uniform treatment of net operating loss carryforwards.

Any reduction in tax revenues resulting from the uniform definitions will be offset by the anti-PIC addback requirement and the addition of new municipal income tax taxpayers that were previously exempt from the tax (i.e., local telephone companies, dealers in intangibles, etc.).

The tax reform proposal also contains a variety of other changes, including incentives for the filing of paperless tax returns; more resources and compliance tools for the Ohio Department of Taxation to ensure fair enforcement of Ohio's tax laws; elimination of the burden for businesses with less than \$10,000 of property to file personal property tax returns; a reduction in the 10% rollback on commercial property; and a cap on the application of the 10%/2.5% rollback on homes valued above \$1 million.

The following pages contain a much more detailed and all-inclusive list of changes proposed in this tax reform package.

List of Changes Proposed in the Ohio Tax Reform

Corporation Franchise Tax - General Business

[Changes are effective for taxable years ending on or after the effective date of the bill, unless otherwise noted.]

1. Increase Minimum Tax

- The current minimum tax on net income is \$50.
- This proposal would increase the minimum tax to \$300. (The public utility excise taxes that use the same minimum payment as the corporation franchise tax would also increase. In 1960, the minimum corporation franchise tax was \$50. ODT estimates that based on inflation the minimum tax imposed in 1960 should be \$300. (The General Assembly increased the minimum tax in 1981 to \$150; it reduced the tax to \$50 in 1983.)

Final status: Enacted, changed from original proposal -- Minimum tax for corporations with more than \$5 million in annual sales or at least 300 employees raised to \$1,000.

2. Increase Net Worth Cap

- The current net worth cap is \$150,000 and the tax rate is 4 mills. Under this system, net worth in excess of \$37.5 million is not subject to tax.
- This proposal would increase the net worth cap to \$500,000. Under this system, net worth in excess of \$37.5 million but not exceeding \$125 million would become subject to tax.
- This proposal would also create two new rate brackets below the present rate of 4 mills. (Net worth < \$1 million, 2 mills. Net worth from \$1 million to \$2.5 million, 3 mills. Net worth above \$2.5 million, 4 mills.)
- The \$150,000 cap was enacted in 1997 (effective in 1999). The cap contributes significantly to the poor productivity of the tax during periods of slow economic growth. Increasing the cap would be made in conjunction with progressive three-bracket rate structure actually providing tax relief to smaller net worth taxpayers.

Final status: No change enacted

3. Lower the Rate

- Currently, the top marginal rate is 8.5%
- This proposal would reduce the top marginal rate from 8.5% to 8.0% in taxable year 2004 (Fiscal Year 2005). Further reduce the rate to 7.5% in taxable year 2005 (Fiscal Year 2006) and 7.0% in taxable year 2006 (Fiscal Year 2007).
- Base broadening, proposed below, allows for a rate reduction.

Final status: No change enacted

4. Eliminate Lowest Bracket of \$50,000

- Currently, corporations pay 5.1% on the first \$50,000 of income.
- This proposal would eliminate the lower bracket in taxable year 2004 (Fiscal Year 2005).
- Eighty-six percent of corporate taxpayers will benefit from the corresponding reduction in the (current) top rate.

Final status: No change enacted

5. Business versus Non-business Approach (Adopt UDITPA)

- Currently, Ohio does not use the business versus non-business approach in determining what income is apportioned versus allocated. Rather under Ohio law certain specified items of income are allocated and all remaining items of income are apportioned.
- This proposal would adopt the business/non-business approach.
- The Ohio personal income tax uses a business/non-business approach to allocate and apportion income generated by businesses, as do most other states. Therefore, change will make Ohio tax law more internally consistent and more like other states.

Final Status: Enacted

6. Allocable Non-business Income Loophole Closing

- Currently, when a corporation recognizes a gain or loss from the sale of stock the corporation is required to allocate the gain/loss based on the percent of the investee's physical assets in Ohio. Many times, the investee is a holding company having no physical assets in Ohio, but the investee's wholly-owned subsidiaries often have significant physical assets in Ohio.
- This proposal would create a "look through" mechanism allowing non-business gains or losses to be situated to Ohio based upon the percent of physical assets of the entire affiliated group of which the investee is a member. This would close a loophole concerning allocation with respect to corporate groups having "at the top" a holding company with no Ohio assets and with little or no physical assets (relative to the corporate group as a whole). This provision applies to (a) non-business capital gains and losses from the sale of stock, and (b) non-business dividend income.

Final status: No change enacted

7. Lottery Income "Ease of Reading" Simplification

- Currently, this corporation franchise tax statute addressing the allocation of lottery income provides a cross reference to personal income tax (R.C. 5747.20).
- This proposal would simply replace a statutory reference with the pertinent language from that personal income tax section.
- No substantive change is involved with this item.

Final status: Enacted

8. Sales Apportionment Factor Federal Taxable Income

- Currently, the federal law allows corporations to exclude from net income profits relating to certain sales made to overseas customers. However, those sales are still included in the denominator of the sales factor - thus reducing the Ohio sales factor.
- This proposal would eliminate these sales to overseas customers from the denominator of the sales apportionment factor.
- Since the profit from such sales is not subject to tax, the sales generating the profit should not be in the sales apportionment factor.

Final status: No change enacted

9. Apportionment Throwback

- Currently, a sale with a destination outside of Ohio is excluded from the numerator of the sales apportionment factor -- even if the taxpayer is not subjected to tax in the destination state. In those situations where the goods are shipped from Ohio to a state where the taxpayer is not subject to an income tax (either because the state does not levy a tax or the taxpayer does not have nexus there), current law results in "nowhere" income. That is, a portion of the corporation's profit is not taxed in any state.
- This proposal would include the sales of goods shipped from Ohio in the numerator of the sales factor if the goods were shipped to a state in which the corporation is not subject to a tax measured on or by income, or if the goods were shipped to the U.S. government.
- Like many other states, sales made to states where the corporation does not have to pay income tax or to the federal government would be treated as the home state's sales, as opposed to being considered "nowhere" sales.

Final status: No change enacted

10. Apportion Sales Using the "Market" Approach Not "Cost of Performance"

- Currently, for sales of services, a sale is situated based on where the majority of the costs of performance are incurred -- where the work is done.
- This proposal would replace the "cost of performance" approach with the "market" approach on sales of services. Accordingly, Ohio would situate such sales to where the benefit of the service is received.
- An increasing number of states are moving to the "market" approach treatment for where sales of services are situated. Ohio took this approach in the mid-1990s with respect to the sale of banking services.

Final status: No change enacted

11. Federal Consolidated Filing Election

- Currently, Ohio law permits certain corporations to file on a combined basis. Typically, taxpayers elect this option only if it results in tax savings. The Tax Commissioner can require a combination if separate filing creates a distortion in income. However, requiring a combination is a very time-consuming and audit intensive activity, and is generally unsuccessful at limiting sophisticated tax planning.
- This proposal would permit corporations to elect to file on a consolidated basis with the same related entities as on their federal consolidated return. Taxpayers that do not make such an election must file separately. Furthermore, in filing separately, expenses and payments between related entities generally would be disallowed. However, the tax owed by the separately filing related entities on account of the disallowance could not exceed the tax that would be owed if the related entities were required to file on a combined basis.
- The consolidated net worth cap would equal \$500,000 multiplied by the number of Ohio taxpayers in the consolidated group.
- This proposal would significantly mitigate the impact of sophisticated tax planning transactions.

Final status: No change enacted

12. Alternative Methods for Special Circumstances

- Currently, corporations who wish to request a deviation from the statutory methods for apportioning and allocating income do not need prior approval from the Tax Commissioner. The corporation may file based on the alternative method, and attach a notice that the taxpayer is seeking alternative treatment.
- This proposal would expand the availability of alternative methods and require that the taxpayer seeking a deviation from the statutory method receive approval before using the alternative method. If not obtained prior to the date the return is filed, the taxpayer must compute and pay the tax by the statutory method and then request alternative treatment with a refund application.
- This proposal would also address a Board of Tax Appeals decision, *Delta Airlines* (Case No 96-T-471 1/12/2001), to continue to allow both corporations and the Tax Commissioner to use alternative methods when allocating income. In addition, it gives the Tax Commissioner the authority to prescribe allocation and apportionment methods that apply to specific classes of corporations or corporations within a specified industry.

Final status: No change enacted

13. Passive Investment Company (PIC) Reform

- Currently, PIC law includes several “limiters” to make sure that it is not over-reaching. The main limiter, which is not recommended for repeal, states that the additional tax due to the PIC addback can be no greater than if the corporate taxpayer filed a combined return with the PIC. The other limiters were added out of an abundance of caution, however, taxpayers are using these to justify not paying any PIC tax and to seek refunds of millions of dollars of tax already paid.
- This proposal would repeal three of the limiters.
- The repeal is necessary to carry out the original intent of the 1997 Net Worth Reform Package by not allowing for unintended refunds. ODT’s revenue estimates for the Package did not envision taxpayers using these sections to seek refunds.

Final status: No change enacted

14. Eliminate Deduction for Income Taxes Paid to Non-Ohio Jurisdictions

- Currently, the “starting point” for calculating the Ohio corporation franchise tax is the corporation’s federal taxable income before special deductions. Federal law allows corporations to deduct, when computing federal taxable income before special deductions, taxes paid to other states and their local instrumentalities. Current Ohio law does not require that corporations add back such deductions.
- This proposal would require corporations to add back any deductions with respect to income taxes paid to other states or locals.
- Ohio is one of only 12 states that presently offer this benefit.

Final status: No change enacted

15. LLCs Technical Change

- Currently, an LLC can be taxed as a corporation for federal and state income tax purposes. However, the Ohio corporation franchise tax does not clearly apply all of the provisions of the corporation franchise tax to LLC’s. For example, an LLC cannot join (and cannot be required to join) a combination of corporations.
- The proposal would more uniformly extend various franchise tax provisions to all LLCs that are taxed as corporations.
- Most LLCs are taxed as partnerships and are not affected by this change.

Final status: No change enacted

16. “Pass Through Entity” Tax Codification of Current Treatment

- Currently, the pass through entity (PTE) tax imposes a tax withholding requirement on the distributions of PTE profits to nonresident owners and shareholders. The law requires that most PTE expense payments to related members be apportioned for purposes of the PTE tax. However, current law states that only related member compensation expense, and not most expenses, is apportioned for purposes of the nonresident credit. These provisions conflict. Also, the PTE statutes regarding distributive shares include the income, gain, expense, or loss of a disregarded entity, but this law does not expressly state that a distributive share includes the profit of a qualified subchapter S subsidiary.
- This proposal would provide that the PTE expense payments to related members are apportioned for both the PTE tax and the nonresident credit. It also specifies that the PTE tax applies to the profit of a qualified subchapter S subsidiary. This second item codifies long-standing ODT policy.

Final status: No change enacted

17. Tighten Manufacturing & Equipment Investment Tax Credit

- Currently, there is a credit for machinery and equipment purchased by *manufacturers*. One-seventh of the credit is claimed in each of the seven years after the qualifying purchase is made.
- This proposal would expressly limit the credit (both new credits and remaining 1/7th amounts) to manufacturers only.
- This provision clarifies that nonmanufacturer-lessors (generally banks and their leasing subsidiaries), electric companies, and service companies do not qualify for the credit.

Final status: No change enacted

18. Reduce the Coal Tax Credit

- Currently, a tax credit is allowed for electric companies using Ohio coal in coal-fired electric generating plants. The credit equals three dollars per ton of Ohio coal used between May 1, 2001 and December 31, 2004.
- This proposal would reduce the credit.
- In 1999, the General Assembly increased this credit from one dollar per ton to three dollars per ton.

Final status: No change enacted

19. Eliminate 22 Other Special Interest Carveouts

- Currently, there are a number of credits, exemptions, and deductions that individually have a minimal impact to the State GRF and are claimed by relatively few taxpayers.
- This proposal would eliminate many of these items from the tax code.
- Eliminating numerous credits, exemptions, and deductions with only limited utilization broadens the corporation franchise tax base and simplifies the tax.

Final status: No change enacted

20. Tighten Appreciation Exemption for Financial Institutions

- Currently, financial institutions are able to reduce their net worth by “appreciation.” Under current law, “appreciation” is not defined.
- This proposal would expressly limit the appreciation deduction to appreciation attributable to the equity method of accounting.
- Under this change financial institutions could no longer deduct from their net worth the increase in value from such things as employee pension plan investments in stocks and bonds.

Final status: No change enacted

Personal Income Tax

21. Make the Trust Tax Permanent

- Currently, the taxability of trust income is enacted for only three taxable years – 2002, 2003, and 2004.
- This proposal would make the income tax on trusts permanent and clarify the definition of resident trust.
- Senate Bill 261 (124th General Assembly) subjected the income of trusts to the income tax only through taxable years beginning in 2004. Prior to that Ohio was the only state with a broad-based income tax that did not apply to trusts.

Final status: No change enacted

22. Tax Rate Reduction Plan

- Currently, Ohio has nine brackets and numerous credits, deductions, and exemptions.
- This proposal would lower the rates and replace the personal exemption and exemption credit with a flat credit per return plus an additional credit per dependent, both indexed for inflation.
- These changes would provide tax relief to most taxpayers. The changes would expand the number of low-income taxpayers that would owe no tax and who would not have to file tax returns. The restructuring would be phased in starting in 2005 and be complete by 2008.

Final status: No change enacted

23. Resident Credit Computation Technical Correction

- Currently, residents are permitted to claim a resident credit for income taxes paid to another state. Long-standing Ohio Department of Taxation policy is that the credit only applies to income taxes that are itemized deductions and not to income taxes that are deducted in computing FAGI.
- This proposal would codify current Ohio Department of Taxation policy.

Final status: No change enacted

24. Delay Bracket Indexing

- Currently, the personal income tax brackets will be indexed annually beginning in taxable year 2005.
- This proposal would delay the implementation of the bracket indexing.
- The bracket indexing, enacted in Senate Bill 261 (124th General Assembly), would be replaced by the broader plan to reform the personal income tax.

Final status: No change enacted

25. Eliminate Reciprocity Agreements

- Currently, Ohio has reciprocity agreements with all its border states. Under these reciprocity agreements, individuals residing in Ohio's border states but employed in Ohio do not pay Ohio income tax. Instead, they pay taxes to their state of residence. Similarly, Ohio residents employed in border states do not pay income tax to those states.
- This proposal would suspend for taxable years 2003-2008 the authority to enter into reciprocity agreements, making Ohio residents who work out of state subject to taxation in the state where they work and making non-residents who work in Ohio subject to Ohio tax.
- Because Ohio is a net importer of workers, these agreements have a net cost to the State GRF. (All states imposing an income tax provide a credit for residents that pay income taxes to other states.)

Final status: No change enacted

Real Property Tax

26. Limit 10% and 2.5% Rollbacks on Homesteads to the First \$1 Million in Market Value

- Currently, there are two rollback programs, 10% for all real property and an additional 2.5% percent for owner-occupied homesteads. The State reimburses local governments for the cost of the rollback programs. The reimbursements cost the State over one billion dollars per year. Real property tax rollback reimbursements are among the fastest growing line items in state government. They are open-ended appropriations outside the control of the administration or the legislature and historically grow at a rate of 5% to 7% per year.
- This proposal would cap the amount of both the 10% rollback and the 2.5% rollback that homestead real property can receive, limiting it to the first \$1 million in market value. This proposal would begin in tax year 2003.
- While the rollbacks are tax relief mechanisms, they are not limited to taxpayers that necessarily need tax relief. By way of contrast, the homestead exemption tax relief provided to senior citizens and disabled homeowners is closely tied to need.

Final status: No change enacted

27. Reduce the Rollback for Business Property

- This proposal would cut the real property 10% rollback for business in half, reducing it from 10% to 5%. This proposal would begin in tax year 2003.
- The 10% rollbacks were created in the early 1970's. Since then, the business share of tax revenues has been falling. This proposal helps mitigate that decline in the business share.

Final status: No change enacted

Personal Property Tax

28. Inventory Tax Phase-out Acceleration

- Currently, the listing percentage on inventory property is 23% and decreasing at a rate of 1% per year if certain criteria are met. Beginning in tax year 2007, the annual 1% reduction to the listing percentage will be automatic.
- This proposal would reduce the assessment rate by 2% per year rather than 1% per year, starting in tax year 2005.

Final status: Enacted

29. Eliminate \$10,000 Filing Requirement

- Currently, the first \$10,000 of tangible personal property assessed value is exempt from the tax. The State reimburses local taxing districts for the cost of this exemption. To provide the information enabling the state reimbursement, taxpayers with less than \$10,000 of assessed value must file an “informational” tax return.
- This proposal would eliminate the filing requirement for approximately 280,000 taxpayers beginning in tax year 2004.
- In addition, this proposal calls for the elimination of the State’s reimbursement of the cost of the exemption over a ten-year period. Because returns would no longer be required, the reimbursement would be paid based on the last returns filed, at 90%, then 80%, etc.
- Eliminating the filing requirement would decrease compliance costs for businesses by approximately \$20 million.

Final status: Enacted

Sales Tax

[Changes are effective on the effective date of the bill, unless otherwise noted.]

30. Electronic Information Services

- Currently, there is a 25% sales tax refund for purchases of equipment used to provide electronic information services (EIS).
- This proposal would specify that the refund is only available to persons that make sales of EIS to non-affiliates and not to equipment used to provide EIS to members of an affiliated group.
- The proposed language would also delete obsolete language that references purchases made on and after July 1, 1993 since equipment purchased that long ago would not be eligible for the partial refund.

Final status: No change enacted

31. Streamlined Sales Tax and Related Technical Changes

- Currently, Ohio, as a participant in the Streamlined Sales Tax Project, is working with other member states to create common definitions and minimize the burden to sellers to comply with the sales and use taxes imposed across the nation.
- This proposal would make a number of changes that Ohio needs to make to sales and use tax statutes to conform with the Streamlined Sales Tax Agreement. The first changes involve corrections, modifications, and additions necessary for language adopted in the Streamlined Sales Tax legislation, Am. Sub. S.B. 143 (124th General Assembly), that are now in effect. Second, the proposal includes additional changes needed to comply with the Streamlined Agreement. These items involve definition changes to such things as “food and food ingredients,” “sale price,” “purchase price,” “drugs,” and “prescription,” to name a few. Further, changes are needed to convert some exceptions to exemptions; conform bad debt language; modify registration, filing and remittance provisions; and change rounding.
- Effective dates would be delayed until July 1, 2005.

Final status: Enacted

32. LLC s Technical Changes

- Currently, the transfer of all the stock of a corporation whose sole asset is a recreational asset is a sale of the asset and subject to sales tax.
- This proposal would give similar treatment to sales of the ownership interest in an LLC whose sole asset is the same type of property.
- LLCs were not authorized under Ohio law when the provision concerning corporations was enacted.

Final status: No change enacted

33. Tiered Discount

- Currently, when vendors timely remit their sales tax collections to the State they can retain .75% of the amount of tax collected. This amount is typically referred to as the “vendor discount.”
- This proposal would increase the amount of the discount for smaller vendors to 1%, while the discount for larger vendors would be decreased to .5%.
- Not all states provide for a discount. Some that do allow a discount cap it or have a tiered discount. This proposal recognizes that there are economies of scale in performing the sales tax collection responsibility.

Final status: Discount temporarily increased to 0.9%

34. Affiliated Nexus

- Ohio’s current affiliated nexus language is outdated. Affiliated nexus is requiring a business, such as a catalog company that has a sister corporation physically doing business in this state with retail locations, to collect Ohio’s sales/use tax if they use similar names, accept returns, etc.
- This proposal would specify more events that create nexus for an out-of-state seller to be required to collect Ohio’s sales/use tax.

Final status: No change enacted

35. Eliminate 14 Other Special Interest Carveouts

- Currently, there are a number of credits, exemptions, deductions, etc. with a minimal impact to the State GRF and are claimed by relatively few taxpayers.
- This proposal would eliminate many such items from the tax code.
- Eliminating numerous credits, exemptions, deductions, etc., which may only have limited utilization, broadens and simplifies the sales tax base.

Final status: Exemptions for vanpooling and TPP used in mine reclamation repealed

36. Admissions

- Currently, the State does not tax admissions; some cities do tax admissions.
- This proposal would subject admissions to the sales tax. Covered events and activities would include professional entertainment and sporting events, theaters, concerts, movies, amusement parks, and other similar events.
- Local taxes would not be preempted.

Final status: No change enacted

37. Personal Storage and Parking Facilities

- Currently, personal storage and parking facilities are not subject to the sales tax.
- This proposal would subject personal storage rents, such as self-storage units and safety deposit boxes, to taxation. The tax would not apply to business storage charges (warehouses). The sales tax would also apply to charges for parking, whether on an hourly, daily, or monthly basis. Parking provided by public entities would not be excluded from tax.

Final status: Enacted, excluding parking

38. Personal Care

- Currently personal care services are not subject to the sales tax.
- This proposal would subject certain personal care services to the sales tax. While the tax would not apply to haircuts, it would apply to tanning, tattooing, nail care, skin care, and spa services including massages.

Final status: Enacted

39. Cable, Satellite, and Pay-Per-View

- Currently, cable TV service (including satellite) and pay per view programming are not subject to the sales tax (although rental of certain equipment provided in the service can be subject to the tax).
- This proposal would subject these services to the sales tax. This proposal would apply tax to all service and rental charges, provision of premium channels, pay-per-view and special services, installation, and repair charges.

Final status: Tax on satellite TV enacted, being challenged in court

40. Lobbying and Public Relations Services

- Currently, lobbying and public relations services are not subject to the sales tax.
- This proposal would impose sales tax on such services.

Final status: No change enacted

41. Interior and Landscape Design

- Currently, interior design and landscape design services are not subject to the sales tax.
- This proposal would subject these services to the sales tax. This proposal does not include architectural services.

Final status: No change enacted

42. Dry Cleaning and Laundry

- Currently, only industrial laundry cleaning services (which includes commercial supply of floor mats, uniforms, and linens to business) are subject to the sales tax.
- This proposal would subject all dry cleaning and laundry related services to the sales tax, excluding coin-operated operations.

Final status: Enacted

43. Real Estate Agents

- Currently, services provided by real estate agents are not subject to the sales tax.
- This proposal would subject these services to the sales tax. These activities include buying, selling, and brokering in connection with the transfer of realty. The proposal specifically excludes service that constitutes the practice of law.

Final status: No change enacted

44. Real Estate Title Search

- Currently, title search services are not subject to the sales tax.
- This proposal would subject these services to the sales tax.

Final status: No change enacted

45. Real Estate Management

- Currently, real estate management services are not subject to the sales tax.
- This proposal would subject to the sales tax real estate management services.

Final status: No change enacted

46. Replace the WATS and 800 Exemption with a Call Center Exemption

- Currently, there is a sales tax exemption for WATS and 800-type telecommunication services.
- This proposal would eliminate the existing exemption for WATS and 800 services and create an exemption for call-centers.
- When the WATS and 800 exemptions were created they applied to certain high volume, business long distances services. As the industry and marketplace have evolved, essentially all business long distance services fall into one of these categories, and are therefore exempt. At the same time, individuals are subject to sales tax on long distance. This change restores the original policy to provide exemption only for a portion of high volume, business long distance services.

Final status: Enacted

47. Delivery Charges

- Currently, shipping and handling charges, when separately shown on an invoice for the sale of tangible personal property are not taxed.
- This proposal would impose sales tax on shipping and handling charges associated with the sale of tangible personal property, whether separately stated or not.

Final status: Enacted

48. Intrastate Water Transportation, Taxis, Limos, and Charters

- Current law includes an exemption from the sales tax for the transportation of persons or property. This exemption specifies that charges for travel by taxis, boats owned by water transportation companies, and chartered buses are not subject to tax.
- This proposal would subject to the sales tax only the wholly intrastate transportation of persons. This includes the taxation of taxi, limo and charter bus service, water transportation services and may include some charter aircraft service. The transportation of property is not subjected to tax.

Final status: Enacted, but water transportation excluded

49. Debt Collection

- Currently, debt collection services are not subject to the sales tax.
- This proposal would subject to the sales tax debt collection services.

Final status: No change enacted

50. Transportation for Hire Loophole

- Generally, the “transportation for hire” exemption applies to the trucking industry. The exemption covers trucks and tractors used in providing transportation for hire, and applies to independent owner-operator truckers and the trucking fleets that provide services to the general public. These entities were formerly regulated as public utilities.
- The proposal would preclude entities from claiming the transportation for hire exemption when they primarily provide the transportation service to related entities.
- Under current law, businesses that have their own internal delivery fleets (for example, to deliver items to their own stores) have been separately incorporating the delivery operation in order to take advantage of this exemption.

Final status: No change enacted

51. Vehicle Trade-in Allowance

- Currently, the price of a new car is reduced, for sales tax purposes, by the value of a car that is taken in trade as a part of the transaction. There is a similar allowance for trade-ins on the purchase of new or used watercraft and outboard motors. Ohio law does not otherwise provide any type of allowance for items traded-in toward the price of a purchase. Most notably, the trade-in allowance does not apply in the case of a used car purchase.
- This proposal would modify the trade-in allowance. Under the proposal, the price of a new car or of watercraft and outboard motor would be reduced, for sales tax purposes, by one-half of the value of the item taken in trade.

Final status: No change enacted

52. Disallow Related Entity Resale Exemption

- Currently, purchases for resale are exempt from taxation. The basic theory behind this exemption is that the sales tax should fall on the final consumer and not intermediate transactions.
- This proposal would eliminate the purchase for resale exemption where the item is purchased for resale to a related entity that will use or consume the item.

Final status: No change enacted

53. Eliminate Exemption for Items Used in Food Preparation

- Currently, items used in preserving, preparing, or serving food in a commercial food service operation and the materials for maintaining or cleaning those items are exempt from the sales tax. This exemption covers grills, refrigerators, dishes, and tableware.
- This proposal would eliminate the food service operation exemption.
- The Ohio Constitution precludes taxation of food purchased for consumption off the premises. Yet, businesses that produce this food can claim sales tax exemptions for the items used to produce food for tax exempt sales.

Final status: No change enacted

54. Eliminate the Resale and Manufacturing Exception for Items Used in Food Preparation for Immediate Consumption

- Currently, items purchased for resale or used in manufacturing are exempt from the sales tax.
- This proposal would specify that such purchases for food preparation for immediate consumption do not qualify as purchases for resale. Also food preparation for immediate consumption is not considered manufacturing.

Final status: No change enacted

55. Eliminate Exemption for Newspapers

- Currently, newspapers that are published at least bi-weekly are exempt from the sales tax.
- This proposal would repeal the exemption and subject such items to the sales tax.

Final status: No change enacted

56. Eliminate Exemption for Magazine Subscriptions

- Currently, magazine subscriptions are exempt from the sales tax.
- This proposal would repeal the exemption and subject such items to the sales tax.
- Magazines purchased at brick-and-mortar establishments are subject to taxation.

Final status: No change enacted

Miscellaneous

57. Repeal DIT Tax

- Currently, stockbrokers and entities making loans that do not have deposits are subject to an 8-mill tax on their net worth. Referred to as “dealers in intangibles,” these businesses are not subject to the corporation franchise, the tangible personal property, or municipal income tax. Generally, repeal of the dealers in intangibles tax would make dealers subject to these taxes.
- This proposal would repeal the dealers in intangibles tax.
- The dealers in intangibles tax is the last remnant of Ohio’s former “intangibles tax.” This tax, which is unique to Ohio, is obsolete and does not equitably tax this sector of the financial services industry. It works to the disadvantage of some taxpayers, and creates unfair tax planning opportunities for others.

Final status: No change enacted

58. Pipeline Tax Reform

- Currently, interstate business is exempt from Ohio taxation under the public utility excise tax on gross receipts. This creates a large exclusion for pipeline companies, which by their nature, operate nearly exclusively in an interstate context. The gross receipts tax rate is 6.75%.
- This proposal would replace the exemption with an apportionment requirement, treating some portion of the pipeline company’s receipts as Ohio receipts based on Ohio presence. It would also reduce the tax rate from 6.75% to 4.75%, in line with other public utilities.

Final status: No change enacted

59. Water Transportation

- Currently, water transportation companies are subject to the public utility excise tax on their gross receipts. Transportation services in general are not subject to sales/use taxation. Companies subject to the public utility excise tax are not subject to the corporation franchise tax.
- This proposal would remove water transportation companies from the public utility excise tax for receipts received on and after July 1, 2003. The sales/use tax would be imposed on intrastate water transportation services. Further, these companies would be subject to the corporation franchise tax.
- Overall, the proposal would shift water transportation companies from being taxed as public utilities to being taxed as general business.

Final status: No change enacted

60. Telecom Reform

- Currently, telephone companies (local telephone) are subject to Ohio’s public utility excise tax on their gross receipts. Companies subject to the public utility excise tax are not subject to the corporation franchise tax or municipal income tax, and their services are not subject to sales taxation. However, other providers of other telecommunications services, such as long distance and wireless telecommunications companies, are subject to the corporation franchise tax and municipal income tax, and their services are subject to sales taxation. (Cable television tax treatment varies from both of these two general categories.)
- This proposal would remove the telephone companies from the public utility excise tax for charges billed on and after July 1, 2004. The sales tax would first apply beginning in January 2004. Telephone companies would also become subject to the corporation franchise tax and municipal income tax in taxable year 2004. The proposal would also clarify that providers of mobile telecommunications are eligible for the sales tax exemption provided to telecommunications service providers.
- The telecommunications industry has evolved from a small group of monopolistic, highly regulated companies to a diverse group of businesses providing myriad competing services. The tax law treats different portions of the industry—and their customers—differently. This proposal would create greater uniformity in the taxation of the telecommunications services and providers.

Final status: Enacted

Municipal Income Tax Reform

61. Uniform Definition of Taxable Income for Business Net Profits Tax

- Currently, there are 541 municipalities in Ohio that levy an income tax, yet there is not a standard definition of taxable income for the business net profits tax. Taxpayers operating in multiple jurisdictions must be familiar with several different ordinances determine what income is taxable by each jurisdiction.
- This proposal would establish a uniform definition of income (including a PIC adjustment), and would require municipalities levying a business net profits tax to use this standard definition of income without deviation beginning in tax year 2004.
- This would create a single definition of income that all municipalities would use when taxing business profits. This proposed tax base would be substantially as broad as the tax base currently used by most municipal corporations.

Final status: Enacted

62. Uniform Definition of Withholding Tax Base

- Currently, there is not a standard definition of the tax base for employers to use with respect to withholding municipal income taxes from their employees' income.
- This proposal would create a uniform withholding tax base beginning in tax year 2004.

Final status: Enacted

63. Appeals to Board of Tax Appeals and Ohio Supreme Court

- Currently, taxpayer appeals from municipal income tax administrative decisions are taken to County Courts of Common Pleas.
- Beginning in tax year 2004, this proposal would require appeals (beyond the current administrative appeal within each municipality's tax agency) to go first to the Ohio Board of Tax Appeals and then to either the court of appeals or to the Ohio Supreme Court.
- This would result in uniform application of the tax statewide.

Final status: Enacted

64. Revised Due Dates

- Currently, some municipalities have an April 15th due date and some have an April 30th due date. Furthermore, some municipalities allow an extension to file to extend to October 15th and some allow it to extend to October 31st.
- Beginning in tax year 2004, this proposal would require that the due date for the returns be April 15th and would require the extension time period to run until October 31st.

Final status: Enacted

65. Eliminate 3-year Requirement on Reporting for Withholding Purposes

- Currently, an employer may be required to withhold municipal income tax from its employees for a particular municipality if the total withheld amount for all employees reaches \$150 in that municipality for a particular year. The employer must withhold for the next three years, regardless of the taxable amount of income of its employees for the intervening years.
- This proposal would immediately eliminate the three-year "lock-in" and would change the rule to a year-to-year test for determining withholding requirements.

Final status: Enacted

66. Centralized Filing for Business Net Profits Tax at the Taxpayer's Option (*Ohio Business Gateway*)

- Currently, the *Ohio Business Gateway* provides businesses a single portal for filing certain business taxes and specific other information required by various state agencies.
- This proposal would add a municipal business net profits tax filing option (at the taxpayer's option) to the *Ohio Business Gateway* beginning in tax year 2005.
- This proposal would also add a municipal withholding tax filing option (at the taxpayer's option) to the *Ohio Business Gateway* beginning in tax year 2007.
- The State would pay the cost of adding this option to the *Ohio Business Gateway* system, which would immediately deposit the revenue directly into municipal checking accounts. Further, all necessary filing data would be immediately sent to each municipality. Municipalities would retain all administrative and audit responsibilities.

Final status: Enacted

67. Internet-based Request for Extension of Time to File Tax Returns

- Currently, municipalities generally grant a request for an extension of time to file municipal tax returns if the taxpayer has been granted the federal income tax extension. A taxpayer is required to file a copy of the federal extension with each municipality to which the taxpayer owes tax.
- Beginning in tax year 2005, this proposal would create an Internet-based method (using the *Ohio Business Gateway*) for taxpayers to file one extension request that would be valid for and available to all municipalities.

Final status: Enacted

68. Anti-PIC Add Back

- Currently, municipalities generally may not tax intangible income. Certain taxpayers use a planning mechanism whereby the taxpayer establishes a related entity passive investment company (PIC) to which the taxpayer pays royalty fees and/or other intangible expenses in order to avoid municipal income tax. This is a concept that is similar to the Ohio PIC planning technique, but does not even require the expense be paid outside the taxing municipality. (The related PIC could be within the same municipality because of the statutory provision that disallows municipalities from taxing intangible income.)
- Beginning in tax year 2004, this proposal would require an add back of certain expenses paid to related PICs.
- This proposal would eliminate planning mechanisms used to shelter income with respect to intangible income and broaden the municipal income tax base, thereby offsetting any reduction to the base that might arise due to the uniformity provisions above.

Final status: No change enacted

69. Uniform Treatment of Net Operating Losses (NOLs)

- Currently, some municipalities permit the carryforward of NOLs while other municipalities do not permit a carryforward. Further, of those municipalities permitting NOL carryforwards, no consistent carryforward period exists.
- This proposal would permit the carryforward of NOLs for a five year period.
- A uniform treatment of NOLs is a necessary complement to providing a uniform tax base for business tax purposes.

Final status: No change enacted

Tax Administration

70. Late Payment Penalty Remission

- Currently, penalties for late payment of real and personal property taxes may only be remitted if one of four narrowly defined statutory reasons is satisfied. With respect to personal property taxes, the county auditor, in consultation with the county treasurer, makes the initial decision regarding remission of personal property tax late payment penalties, with the first appeal going to the tax commissioner. With respect to real property and manufactured or mobile home late payment penalties, the tax commissioner makes the initial determination, with the first appeal going to the Board of Tax Appeals. Finally, there is no limit on the time a taxpayer has to appeal the auditor's denial of personal property late payment penalties to the tax commissioner.
- This proposal would create a fifth condition upon which a penalty can be remitted: namely "good cause." The proposal also seeks to synchronize the procedure to request remission of real property and manufactured home tax late payment penalties with the procedure currently in place for remission of personal property late payment penalties. Finally, the proposal would create a 60-day filing deadline for the appeal of the auditor's decision to the tax commissioner.

Final status: Enacted, modified from original proposal

71. Remove Community Reinvestment Areas (CRAs) from the Tax Commissioner's Jurisdiction

- Currently, local authorities grant CRA exemptions. The Tax Commissioner has no role in this process.
- This proposal would explicitly exclude the Tax Commissioner from the CRA complaint process and make technical corrections. This proposal would also include a temporary law section to allow the Tax Commissioner to address a large volume of last-minute complaints that may be filed with the ODT, which would undermine the proposal.
- This proposal would reaffirm the Tax Commissioner's long-standing policy regarding complaints against continued CRA exemptions. This counters the Ohio Supreme Court's 2001 decision, *Gahanna-Jefferson Local School Dist. Bd. Of Educ. V. Zaino*, in which the court ruled the Tax Commissioner had jurisdiction to grant CRA exemptions and hear CRA complaints. Since that ruling, the Commissioner has been required to review and possibly rescind exemptions that were granted by local authorities. ODT should not be in the position of rescinding exemptions granted according to local interpretations of the law, when local governments consider these incentives to be vital to their economic development. The technical corrections are necessary to create consistency within the respective sections.

Final status: Enacted

72. Permit Access to Electronic Records

- Currently, ODT is unable to require taxpayers to provide electronic records as part of audit.
- This proposal would permit ODT to require records in electronic form, where the records already exist electronically.
- This change will improve audit efficiency.

Final status: No change enacted

73. Disallow Sham Transactions

- Currently the Tax Commissioner can apply the doctrines of "economic reality," "sham transaction," "step doctrine," and "substance over form" in making corporation franchise tax assessments. On a very limited basis it also applies to the up-front sales tax paid on certain leases. The Tax Commissioner bears the burden of proof that the doctrines should apply.
- This proposal would expand application of these doctrines to all taxes and fees administered by the Tax Commissioner.
- Addressing sham transactions provides ODT not only with an audit tool, but also assists with voluntary compliance by allowing ODT to disregard transactions that have no economic value except to avoid a specific tax result.

Final status: Enacted, modified from original proposal

74. Electronic Returns/Expansion of Electronic Payment

- Currently, certain taxes have a requirement for the larger taxpayers to make payments electronically. The Tax Commissioner has discretion to prescribe forms for all taxes, but the law does not specifically address electronic returns.
- This proposal would extend to April 30 the due date for personal income tax returns that are filed electronically. The proposal would establish 10th of the month due dates for sales tax returns unless they are filed electronically.
For all other returns, the Tax Commissioner would have discretion to extend due dates if taxpayers file electronically.

Final status: No change enacted

75. Sales Tax Personal Liability

- Currently, an employee responsible for filing sales tax returns or making sales tax payments can be held personally responsible for any unpaid sales tax owed by the employing corporation.
- This proposal would clarify that direct pay permit holders under R.C. 5739.031 are subject to personal liability.
- This proposal also subjects out-of-state sellers that are registered or required to be registered to collect Ohio's use tax to the same personal liability as a corporation located in this state.

Final status: Enacted

76. Vendor License Issuance by ODT

- Currently, most vendor licenses are issued by the counties.
- This proposal would also enable ODT to electronically issue vendors licenses beginning in 2005.

Final status: No change enacted

77. Pollution Control and Energy Conservation

- Currently, there are several pollution control and energy conservation property exemption programs (air, water, noise, thermal efficiency, solid waste, and energy conversion). Authority for the different programs rests with ODT and either the Department of Development or Environmental Protection Agency. Accordingly, dissimilar procedures exist among the programs.
- This proposal would synchronize the application procedures for the various pollution control and energy conservation exemptions. This includes reorganizing the authority into a single chapter of the Revised Code, establishing uniform appeals procedures to the Board of Tax Appeals, and imposing a \$1000 application fee to help cover administrative costs. (Currently only the water program has a fee - \$500.) Other changes would clarify what property is in fact exempt, prevent frivolous applications, and prevent taxpayers from seeking refunds for closed tax years.

Final status: Enacted

78. Adjustment for Water Added to Motor Fuel

- Currently, Ohio law defines "diesel fuel" as "any liquid fuel capable of use in discrete form or as a blend component in the operations of engines of the diesel type ..." Thus, water intentionally added to diesel fuel to reduce nitrogen oxide emissions and particulate emissions is subject to Ohio's motor fuel tax. There is no provision to provide a refund of motor fuel taxes based solely on water being intentionally added to motor fuel.
- This proposal would allow a motor fuel tax refund on water that is intentionally added to motor fuel.

Final status: Enacted

79. Establish a Forfeiture Fund

- Currently, there is no mechanism for ODT's Enforcement Division to receive proceeds from items seized and forfeited as part of a criminal investigation.
- This proposal would establish a fund and enable the receipt of forfeiture proceeds.
- ODT's Enforcement Division assists federal, state, and local criminal investigative task forces that often have agreements between the participating agencies for the dissemination of forfeited funds and proceeds from forfeited contraband.

Final status: Enacted, modified from original proposal

80. Motor Fuel Enforcement

- Currently, ODT's Enforcement Division conducts dyed fuel inspections, but lacks the authority to investigate other potential violations discovered during those inspections.
- This proposal would allow for the enforcement of other laws within existing authority at the time of dyed fuel inspections.
- ODT began an enforcement program in 2001 related to use of untaxed or "dyed" fuel that was illegally used for over-the-road transportation.

Final status: Enacted

Items Not Proposed by Administration but Enacted by General Assembly

Increase sales tax by one cent.

Subject vehicle towing to sales tax.

Subject snow removal services to sales tax.

Exempts from sales tax parts and services used in repairing and maintaining aircraft with fractional share ownership.

Caps the sales tax on fractional shares of aircraft.

Increase the threshold for sales tax accelerated payments and reduce from three to two accelerated payments.