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Bill Analysis
Legislative Service Commission

H.B. 477
123rd General Assembly
(As Introduced)

Rep. Mottley

BILL SUMMARY

- Ensures that parsonage allowances are exempted from municipal income taxation.
- Ensures that most nonresidents are not taxed by a municipal corporation on income earned for performing work in the municipal corporation if the work is performed for 12 or fewer days in a year.
- Prescribes limits governing employers' responsibility for withholding municipal income taxes from employee compensation.
- Prescribes guidelines governing estimated tax payments.
- Requires municipal corporations to grant filing extensions to taxpayers upon request if the taxpayer has requested a federal income tax filing extension.
- Permits affiliated groups of corporations to file consolidated municipal income tax returns if they file consolidated returns for federal income tax purposes.
- Requires municipal corporations to accept "generic" municipal income tax forms.
- Requires municipal corporations to publish municipal income tax rules in an electronic form on an Internet-accessible site, and to provide electronic versions of municipal income tax forms on such a site.
- Requires the Tax Commissioner to establish an Internet-accessible site, on which municipal corporations may post electronic forms and publish rules

electronically, and to which municipal corporations may link their own electronic sites.

CONTENT AND OPERATION

Municipal income taxation--generally

Municipal corporations have the authority under their home rule powers to tax incomes, but this authority is subject to limitation by the legislature. Over the years, the legislature has limited this authority to some extent by restricting the forms of income that may be taxed; prescribing how business income must be allocated among municipal corporations so as to avoid taxation by multiple municipal corporations on the same business income; prescribing statutes of limitations on municipal income tax enforcement actions; requiring municipal corporations to pay interest on overpaid taxes; and requiring taxpayer information to be kept confidential. (See Chapter 718.) Otherwise, municipal corporations' authority to tax incomes is governed by local laws and rules, subject to any applicable limitations of the Ohio and U.S. Constitutions.

The bill places several new limitations and requirements on municipal corporations with respect to income taxation.

New exemptions

(secs. 718.01(F)(7) and (8) and 718.02(A)(2))

Parsonage allowances

The bill prohibits municipal corporations from taxing parsonage allowances. A parsonage allowance is an amount paid to a "minister of the gospel" in the form of a rental allowance paid as part of the minister's compensation, or the rental value of a residence furnished to the minister as compensation. Parsonage allowances are not taxed under either the federal or Ohio income tax. (See I.R.C. sec. 107.)

The exemption takes effect January 1, 2001.

Occasional entrants to a municipal corporation

The bill prohibits a municipal corporation from taxing compensation paid to nonresidents who are employed in the municipal corporation on an infrequent basis. Specifically, a municipal corporation may not tax compensation received by a person for personal services performed by that person in the municipal corporation if: (1) the services are performed on no more than 12 days in a

calendar year, (2) the person is not a resident of the municipal corporation, and (3) the principal place of business of the person or of his or her employer is outside the municipal corporation. Further, a business that employs such a person in a municipal corporation would not have to count that person's compensation in the payroll factor that is used to allocate the business' income to the municipal corporation.

The exemption does not apply to professional entertainers or professional athletes.

The exemption takes effect January 1, 2001.

Limits on withholding taxes from income

(sec. 718.03)

The bill limits the power of municipal corporations to require employers to withhold municipal income taxes. Currently, withholding is governed solely by municipal ordinances or regulations.

\$150 threshold

Under the bill, municipal corporations may not require an employer to deduct and withhold municipal income taxes from employees unless the total amount of tax to be withheld from all employees is more than \$150 for the calendar year. Once the amount to be withheld exceeds \$150 for a year, the employer is required to withhold tax for that year and all ensuing years, unless the amount falls below \$150 per year for three consecutive years. This provision applies to calendar years 2001 and thereafter.

Compensation against which taxes may be withheld

The bill limits the forms of compensation against which municipal corporations may require tax withholding. Beginning in 2001, municipal corporations may require an employer (or other person responsible for paying taxable compensation) to withhold tax only against compensation that is subject to Social Security and Medicare taxes (so-called "FICA" taxes, under the Federal Insurance Contribution Act) and supplemental unemployment compensation benefits. In the terms of the bill, this compensation is the allowable "withholding base." (The FICA tax part of the withholding base is to be determined without regard to the maximum amount of compensation that may be taxed under the Social Security component--\$72,600 in 1999.)

Thus, the bill in effect prohibits municipal corporations from requiring employers or others from withholding income taxes against various forms of "fringe benefits," including the following:

Employer-paid health plans	Qualified retirement plan contributions
Employer-paid 403b annuity contributions*	Simplified employee pension contributions*
Government deferred compensation	Cafeteria plans (nonwage)
Employer-paid FICA for domestic employees	Dependent care assistance payments
Group life insurance payments	Workers compensation

*Withholding may apply if paid through a salary reduction agreement.

Estimated tax payments

(sec. 718.08)

The bill prescribes a uniform schedule under which municipal corporations may require taxpayers to make estimated tax payments if estimated payments are required by the municipal corporation. Estimated payments may be required only on a quarterly basis, and may be required only in the following amounts no earlier than the following dates: not more than 22-1/2% of the estimated annual tax liability by April 30, 45% by July 31, 67-1/2% by October 31, and 90% by January 31.

Safe harbors

The bill prohibits municipal corporations from penalizing a taxpayer (by charging a penalty, interest, or similar charge) if the taxpayer pays estimated taxes equal to the taxpayer's reported tax liability for the preceding taxable year (as long as the preceding taxable year consisted of 12 months and the taxpayer actually filed a return for that year). Nor may a taxpayer be penalized if the taxpayer has not resided in the municipal corporation continuously since the first day of the year.

Filing extensions

(sec. 718.05)

The bill requires municipal corporations to grant tax return filing extensions to taxpayers that have requested a federal filing extension. Receiving a filing extension does not extend the payment due date unless the municipal corporation extends the payment due date. To receive a filing extension, a taxpayer must file a copy of the federal filing extension request with the municipal corporation not later than the normal return filing deadline. The request must be granted for at least the same period of the federal extension. But, the municipal corporation can

deny the request if the taxpayer is late in filing the request, does not file a copy of the federal extension request, or is delinquent in the payment of the municipal corporation's income tax (including any penalty, interest, assessment, or other charge).

Taxpayer appeals

(sec. 718.11)

The bill establishes a mandatory income tax appeals process for every municipal corporation that imposes an income tax.

The bill requires such municipal corporations to create a board of appeals to hear taxpayer appeals. Taxpayers are given the right to appeal decisions of the municipal tax administrator to the board, provided that the taxpayer filed required tax returns and documents. Requests for appeals must be filed with the board within 30 days after the tax administrator issues an appealable decision. The request must be in writing and state the alleged errors in the decision. Appeal boards must hear appeals within 45 days after receiving a request, unless the taxpayer waives a hearing. If a taxpayer waives a hearing, the board may hear the appeal on the record (including any documents filed by the taxpayer or the tax administrator); if a taxpayer does not waive a hearing, the taxpayer is entitled to appear before the board and be represented by an attorney at law, certified public accountant, or other representative. The board must issue a decision within 90 days after the final hearing, and send a notice of its decision to the taxpayer within 15 days after issuing the decision.

Each appeals board must adopt rules governing its procedures and keep a record of its transactions. The records are not open to public inspection under the state's public records law, and meetings of an appeals board are not subject to the state's open meetings law.

When issuing decisions that are appealable to the appeals board, tax administrators must inform taxpayers of their right to appeal and the manner in which the appeal must be filed with the board.

Consolidated corporation returns must be accepted

(sec. 718.06)

The bill requires municipal corporations to accept consolidated returns from groups of corporations that file consolidated federal corporation income tax returns beginning in 2003. Municipal corporations also must allow such corporate groups

to offset operating losses of some group members against operating profits of other group members.

Tax treatment of pass-through entities; credits

(sec. 718.14)

The bill requires each municipal corporation imposing an income tax that applies to income from a pass-through entity to declare how it taxes that income and to grant a credit to preclude multiple taxation of that income. (A pass-through entity generally is a noncorporate form of business organization that, for federal income tax purposes, is not taxed on its income as an entity; instead, income is taxed only in the hands of each individual owner according to that owner's share of the entity. Partnerships, S corporations, some limited liability companies, and some trusts are forms of a pass-through entity.)

Declaration of tax treatment

Currently, municipal corporations do not have to follow the federal tax treatment of pass-through entities: some may tax the income of those entities in the hands of the entity, while others may tax it in the hands of the individual owners.

Under the bill, beginning in 2003 each municipal corporation that taxes pass-through entity income must specify, by ordinance or resolution, whether the municipal corporation taxes pass-through entity income in the hands of the entity or in the hands of the individual owners.

Credits for taxes paid to another municipal corporation

Beginning in 2003, each municipal corporation that imposes a tax on pass-through entity income must grant a credit to residents for any municipal income tax paid on income from a pass-through entity that does not conduct business in the municipal corporation. The credit applies only if the entity is taxed by another municipal corporation in Ohio. The amount of the credit equals the resident's proportionate share of the tax paid by the entity to the other municipal corporation (i.e., if the resident owns 20% of the entity, the resident is entitled to a credit equal to 20% of the tax paid to the other municipal corporation). If a municipal corporation has a policy of granting only a partial credit to residents for income taxes paid to another municipal corporation (e.g., a credit of 80% of the taxes paid to a municipal corporation where the resident is employed), then the credit for taxes paid on pass-through entity income must be reduced to the same percentage (i.e., if the credit for taxes paid by a resident to another municipality is 80%, then

the credit for taxes paid on pass-through income to another municipality must be 80% of the taxes paid by the entity).

Generic tax returns and forms

(sec. 718.07)

Under the bill, municipal corporations must accept "generic" income tax returns and related documents beginning in 2001 if the returns and documents contain all of the information that the municipal corporation otherwise requires, and if the filer otherwise complies with the municipal corporation's filing requirements. For the purpose of the bill, a generic form is any electronic or paper form that is designed for reporting a municipal income tax but that is not prescribed by any particular municipal corporation.

Internet forms and publications; sites

(secs. 718.11 and 5703.49)

Beginning in 2001, any municipal corporation that requires taxpayers to file income tax returns or related documents is required by the bill to make available over the Internet blanks of their various income tax returns, forms, and instructions. For this purpose, each municipal corporation may adopt rules prescribing the format in which returns and other documents must be filed electronically; how electronic returns and documents must be signed; how the municipal corporation will acknowledge receiving returns and documents from a taxpayer; and how electronic returns and documents will be preserved. Municipal corporations also must publish income tax rules and ordinances electronically on a site accessible through the Internet. The published rules or ordinances must include those governing the tax rate, filing, withholding, penalties and interest, and appeal rights and procedures.

Before the end of 2001, each municipal corporation that imposes an income tax and requires taxpayers to file income tax returns must establish an Internet-accessible site linked to a central site that the Tax Commissioner must establish.

HISTORY

ACTION	DATE	JOURNAL ENTRY
Introduced H0477-I.123/jc	10-08-99	p. 1240