*Bethany Boyd* *Legislative Service Commission*

# Am. Sub. H.B. 483

123rd General Assembly
(As Passed by the House)

**Reps. Mottley, Distel, Aslanides**

## BILL SUMMARY

- Prescribes Ohio corporate net income as the uniform municipal income tax base for electric light companies, which is to be apportioned among municipal corporations on the basis of property, payroll, and local municipal income tax rates.
- Prescribes uniform filing requirements whereby an electric light company files a single municipal income tax return with the state, and the state distributes the tax collections to municipalities.
- Prescribes unified procedures for collection, enforcement, and appeals regarding municipal income taxation of electric light companies, similar to those for the corporation franchise tax.
- The bill applies to municipal income taxes paid in 2002 and thereafter.

## CONTENT AND OPERATION

***Municipal income taxation of utilities***

(sec. 718.01(F)(6))

Under continuing law, a municipal corporation cannot tax the income of public utilities that are subject to the public utility excise (gross receipts) tax. But under the electric industry deregulation act (S.B. 3), electric light companies become subject to the corporation franchise tax beginning in 2002, and will no longer be subject to the public utility excise tax. Once the companies are no longer subject to that tax, municipal corporations are free to tax their income. The bill's uniform reporting and payment provisions apply to municipal income taxes paid *for* 2003; and since the bill requires estimated taxes to be reported and paid in

the year preceding the year for which taxes are paid, estimated taxes are to be paid under the bill's uniform provisions beginning in 2002.

The bill prescribes uniform procedures for administering municipal income taxes levied on electric light companies. Generally, the bill requires an electric light company to file a single tax return and pay taxes to the state, rather than filing separate returns and making separate tax payments to each municipal corporation where the company conducts business. A set of uniform procedures and enforcement remedies will apply in lieu of the various municipal procedures and remedies; the uniform procedures and remedies are substantially equivalent to those used to administer and enforce the corporation franchise tax.

***Companies covered under the bill***

(sec. 718.01(A)(7) and (8))

The bill applies to all companies known in the electric utility deregulation law (Chapter 4928.) as "electric light companies." This term encompasses not only electric utilities that generate, transmit, or distribute electricity, but nonutility companies that arrange for electricity to be supplied to a consumer through facilities owned by other companies. The bill also applies to so-called "combined companies"--those that have multiple lines of utility business such as natural gas and electricity supply--but only to the extent that such companies are in the business of supplying electricity. (Hereafter in this analysis, references to electric light companies should be understood to refer to the electricity-supplying part of a combined company.)

Nonprofit companies and municipal electric utilities are not subject to municipal income taxes (under the bill).

***Uniform tax base***

(secs. 718.01(A)(5) and (6) and 718.21(A))

Currently, each municipal corporation that levies an income tax on corporations may define taxable income in its own way, so a corporation doing business in several municipal corporations might have to compute the tax due to each municipal corporation in a different manner.

The bill prescribes a uniform tax base for electric light companies: an electric light company's net income for municipal income tax purposes is to be the same as that determined for the Ohio corporation franchise tax.

If a company conducts business in other states, municipal corporations may tax only the net income that is apportioned and allocated to Ohio. In determining

an electric light company's Ohio net income, the various adjustments to net income made for franchise tax purposes apply as well to the income that is taxable by municipal corporations. These include adjustments relating specifically to the electricity industry: how electricity sales are attributed to Ohio (sec. 5733.059), and how an electric light company is to be taxed on the disposal of its capital assets (sec. 5733.0510).

Each company's tax base will be determined over the same period as the company's net income for franchise tax purposes--i.e., over the company's fiscal year ending before the beginning of the "tax year" for which the tax is paid. (Thus, municipal income taxes paid for 2003 will be based on a company's net income for its fiscal year ending sometime in 2002.)

***Apportionment of income***

(secs. 718.02 and 718.21)

Under the bill, an electric light company's Ohio net income is apportioned by the Tax Commissioner among the various municipal corporations in which it owns property or employs persons. The amount of Ohio net income apportioned to a particular municipal corporation is proportionate to (1) the "property factor," which is the taxable value of the company's property in that municipal corporation as a percentage of the taxable value of the company's property throughout Ohio (including property rented or leased by the company), and (2) the "payroll factor," which is the compensation paid to employees for work performed in that municipal corporation as a percentage of the compensation paid to all employees for work performed throughout Ohio. If a company rents or leases property, the Tax Commissioner will determine how it is to be valued for the purpose of determining the property factor.

Each of these factors is given equal weight; in other words, half of a company's Ohio net income is multiplied by the property percentage, and the other half is multiplied by the payroll percentage, and the sum of those halves yields the amount of the company's Ohio net income that is taxable by the municipal corporation. Receipts from selling electricity are not a factor in the apportionment formula.

If a company is a combined company (i.e., in the business of supplying electricity and some other utility, such as natural gas), then only the electricity-supplying part of the company's operations are to be included in the property and payroll factors. In the case of property, this part is determined on the basis of how the taxable value of the property is attributed to the company's electricity operations for the purposes of utility property taxation (see sec. 5727.03). In the case of the payroll factor of a combined company, the factor includes only

compensation paid to employees for their work in the company's electricity-supplying operations.

The Tax Commissioner must determine the apportionment of net income among municipal corporations, and must certify a municipal corporation's apportionment to the electric light company and the municipal corporation. The certificate of apportionment must be sent no later than April 1. In order for the Tax Commissioner to apportion a company's income, each company must file an apportionment of income report annually by February 15. The report is made for the tax year that began on the preceding January 1, based on the company's payroll paid in the preceding year and on the taxable value of the company's property for the preceding year.

***Appealing the apportionment***

(sec. 718.29)

Municipal corporations have the right under the bill to appeal the Tax Commissioner's apportionment of an electric light company's net income. To appeal, the municipal corporation must file a petition with the Tax Commissioner within 30 days after the apportionment certificate is issued. The Tax Commissioner must hold an administrative hearing and make any correction in the apportionment that is warranted. Any correction must be certified to the electric light company and to all municipal corporations affected by the corrected apportionment. A municipal corporation may appeal the Tax Commissioner's finding to the Ohio Board of Tax Appeals.

***Tax determination; distribution of taxes to municipalities***

(sec. 718.21(D) and (E); Section 3)

An electric light company's Ohio net income, once apportioned to each municipal corporation, is then multiplied by the municipal corporation's tax rate to determine the tax owed to that municipal corporation. Municipal corporations must certify their tax rates to the Tax Commissioner by January 1 each year, beginning with the rate in effect for 2002, which must be certified by December 31, 2001. If a municipal corporation fails to certify its tax rate, 50% of the municipal corporation's distribution of revenue is withheld by the state until the rate is certified.

All tax collections are credited to the Municipal Income Tax Fund, which is created by the bill. Distributions to municipal corporations of their apportioned shares of the taxes are paid from this fund. All investment earnings from the fund are credited to it and apportioned among municipal corporations in proportion to

their respective payments from the fund. Payments made from the fund are adjusted to reflect estimated taxes already paid from the fund to a municipal corporation, and any estimated taxes paid directly to a municipal corporation by a company.

***Estimated tax payments***

(secs. 718.22 and 718.222)

***Payment and reporting of estimated taxes***

The bill requires electric light companies to choose annually between paying estimated taxes in a single payment to the state each quarter, or paying each municipal corporation as required by the laws of the municipal corporation. A company that chooses to pay estimated taxes to the state generally would have to pay 100% of its previous year's total municipal tax liability in four equal quarterly installments. In a given year, the first installment is payable on April 15; the second installment is payable June 15; the third is payable September 15; and the fourth is payable December 15. Estimated tax payments and reports must be submitted to the Tax Commissioner. If any payment exceeds $4,000, the company must remit the payment by electronic funds transfer in the same manner that several other state taxes are required to be paid.

If a company becomes subject to taxation by a particular municipal corporation, but its net income was not apportioned to that municipal corporation in the preceding year, the company must pay estimated taxes directly to that municipal corporation by the bill's quarterly due dates, but each payment must be based on the company's good faith estimate of what 25% of its liability to that municipal corporation will be for the current year, in lieu of its liability for the prior year.

If a company was not subject to any Ohio municipal corporation's income tax in the preceding year but is subject to at least one municipal corporation's tax in the current year (e.g., the company has just begun supplying electricity in Ohio), the company is permitted to file a declaration of estimated taxes and remit tax payments to the state on or before each of the quarterly due dates, but the amount paid must be based on the company's good faith estimate of its total municipal income tax liability for the current year, rather than its liability for the prior year. (This provision does not apply if a company chooses to report and pay estimated taxes directly to each municipal corporation, rather than report and pay taxes to the state.)

***Estimated payments in 2002 and 2003***

For the first two years that estimated taxes are due (2002 and 2003), the quarterly payments are calculated on the basis of a company's good faith estimate of its total municipal tax liability for 2003 and 2004. A company must pay 20% of this liability at each of the quarterly due dates. The bill incorporates a "safe harbor" provision that precludes penalties and interest being charged if, for tax years 2003 and 2004, a company pays at least 80% of its actual liability for tax year 2003.

***Distribution of estimated taxes***

No later than January 15, May 15, July 15, and October 15 each year, the Tax Commissioner must distribute the estimated tax payments to municipal corporations. The payments are calculated on the basis of the apportionment of income reports filed by companies.

***Tax reports***

(secs. 718.21(C) and (F) and 718.30)

Each electric light company subject to a municipal income tax must file an annual report with the Tax Commissioner between January 1 and March 31 each year. (If the company receives an extension for filing its Ohio corporation franchise tax report, the due date for the municipal report is extended for the same period.) The Tax Commissioner prescribes the form of the report; generally, it must elicit the same information as the corporation franchise tax report, except that it also must include the names of the municipal corporations in which the company does business. The Tax Commissioner may require companies to file reports in an electronic format.

Municipal corporations are prohibited from requiring electric light companies to file tax returns in addition to the state report. But municipal corporations may require companies to file reports of employee compensation paid for personal services rendered in the municipal corporation, and of the taxable value of property located in the municipal corporation.

If an electric light company's municipal income tax report must be altered as a result of a change in the company's federal income tax return or Ohio corporation franchise tax report, and that alteration affects the company's municipal income tax liability, the company must file with the Tax Commissioner an amended municipal income tax report within one year after the federal or state change is determined. The company must pay any tax underpayment resulting

from the alteration (plus accrued interest), and may request a refund (plus interest) for any overpayment resulting from the alteration.

***Administration and enforcement; penalties, interest, and refunds***

(secs. 718.21(D), (G), and (H), 718.23, 718.24, 718.25, 718.26, 718.27, and 718.28)

The Tax Commissioner is charged with administering and enforcing the bill's provisions. The Tax Commissioner must prescribe necessary forms, provide any required notices, and adopt any necessary rules.

Penalties and interest are charged in the same manner and for the same reasons as penalty and interest are charged under the corporation franchise tax. Money collected in the form of penalties and interest is distributed pro rata among all municipal corporations entitled to receive taxes from the electric light company.

The Tax Commissioner has the same powers to make assessments against electric light companies for municipal income taxes as for any corporation under the corporation franchise tax. The same three-year statute of limitations on assessments that applies under the franchise tax applies to assessments issued against electric light companies for municipal income taxes (there is no statute of limitation in cases of fraud or failure to file, as under the franchise tax). Electric light companies have the same right to appeal assessments as corporations have to appeal corporation franchise tax assessments (beginning with administrative appeals before the Tax Commissioner, which are appealable to the Board of Tax Appeals).

Refunds must be requested and paid in the same manner as refunds of corporation franchise taxes. Refunds are charged pro rata against all municipal corporations that receive taxes from the electric light company, and deducted from the municipal corporation's next distribution of taxes.

To defray the Tax Commissioner's costs of administering electric company municipal income taxes, 1-1/2% of the tax collections are credited to a Municipal Income Tax Administrative Fund created by the bill. Any money in the fund that is not necessary to defray those costs is credited back to the Municipal Income Tax Fund.

The Tax Commissioner may adopt rules regarding the retention of records by companies, including federal income tax returns and Ohio corporation franchise tax reports. Companies must make those records available to the Tax Commissioner for inspection during normal business hours. Companies must

retain records and other pertinent documents for three years after the applicable filing deadline (or the actual day it was filed, if later than the deadline), unless the Tax Commissioner allows the company to destroy the records earlier.

***Third-party administration***

(sec. 718.221)

The bill allows the Tax Commissioner to designate a third party agency to collect and administer municipal income taxes on electric light companies, in lieu of the Tax Commissioner performing those functions. The agency must represent all municipal corporations that impose a tax that applies to electric light companies, unless the Tax Commissioner determines that designating an agency that does not represent all of those municipal corporations is not likely to excessively impair taxpayers' ability to comply with the bill's centralized reporting and payment provisions.

A third party agency designated by the Tax Commissioner is responsible for apportioning companies' net income among municipal corporations; notifying companies and municipal corporations of the apportionment; prescribing tax report forms; receiving and processing the reports; and crediting tax payments to a fund for distribution to municipal corporations. The third party agency is an agent of the Department of Taxation, and is subject to the same confidentiality provisions that apply to other agents of the Department of Taxation, which prohibits them from disclosing taxpayer information except under prescribed circumstances.

***Confidentiality of taxpayer information***

(secs. 718.07 and 5703.21)

Under continuing law, taxpayer information gained by municipal officers and employees through the tax collection process is deemed to be confidential, and persons possessing such information are prohibited from disclosing it except under specified circumstances (such as in accordance with a court's order, or in performing an official act that is authorized by local law). There is no penalty prescribed by state law for violations.

Since the bill provides for electric light companies to file a single return that may cover its operations in several municipal corporations, the bill permits certain municipal representatives to gain access to annual reports and estimated tax reports filed with the state. For this purpose, the bill requires the Tax Commissioner, who keeps the reports, to adopt rules governing how the reports and related information are to be made available for inspection by municipal representatives. The rules must prohibit the disclosure of such reports or related information to anyone who

is not specifically authorized by the municipal corporation to gain access to taxpayer information, and must allow disclosure of only as much information as is necessary for an authorized municipal representative to determine the share of a company's income that is to be apportioned to that municipal corporation.

The bill provides that the disclosure of taxpayer information by an agent of the Department of Taxation in accordance with the Tax Commissioner's rules is not a violation of an existing law that prohibits those agents from disclosing taxpayer information (sec. 5703.21).

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## HISTORY

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