Andre Imbrogno *Legislative Service Commission*

H.B. 112

125th General Assembly
(As Introduced)

Reps. **Gilb, Grendell, Fessler, Jolivette, Young, Faber, Raga, Brinkman, Olman**

BILL SUMMARY

- Eliminates Ohio's progressive income tax structure and establishes a single, "flat" income tax rate of 3.5%.
- Eliminates most existing income tax deductions, exemptions, and credits.
- Establishes a $30,000 exemption for every joint income tax return filed and a $15,000 exemption for every single or separate return filed.
- Establishes a $2,000 income tax exemption for each of a taxpayer's dependents.
- Provides that each year, beginning in 2005, the Tax Commissioner must adjust the exemption amounts established in the bill to account for general price inflation.
- Provides that a taxpayer does not have to file an income tax return if, after taking all of the exemptions to which the taxpayer is entitled, the taxpayer would owe no tax.
- Grants husbands and wives the option of filing separate or joint income tax returns regardless of how they file their federal income tax returns.
- Applies to taxable years beginning on or after January 1, 2004, but does not preclude taxpayers from claiming any credit carry forward to which they are entitled on December 31, 2003.

CONTENT AND OPERATION

Existing structure of the Ohio income tax--graduated income tax rates

Currently, the Ohio personal income tax is applied at a graduated rate to all income and compensation earned by Ohio residents and to all income earned in Ohio by nonresidents. Ohio's income tax is a progressive tax--the tax rate increases as income level increases.

Under current law, there are nine income tax brackets, each with a different tax rate. The rate at which the income tax is imposed ranges from .743% to 7.5% depending upon the applicable income tax bracket. The current income brackets and applicable tax dollar amounts and tax rates for each bracket is as follows:

$5,000 or less	.743%
More than $5,000 but not more than $10,000	$37.15 plus 1.486% of the amount in excess of $5,000
More than $10,000 but not more than $15,000	$111.45 plus 2.972% of the amount in excess of $10,000
More than $15,000 but not more than $20,000	$260.05 plus 3.715% of the amount in excess of $15,000
More than $20,000 but not more than $40,000	$445.80 plus 4.457% of the amount in excess of $20,000
More than $40,000 but not more than $80,000	$1,337.20 plus 5.201% of the amount in excess of $40,000
More than $80,000 but not more than $100,000	$3,417.60 plus 5.943% of the amount in excess of $80,000
More than $100,000 but not more than $200,000	$4,606.20 plus 6.9% of the amount in excess of $100,000
More than $200,000	$11,506.20 plus 7.5% of the amount in excess of $200,000

Current law allows exemptions of $1,050 for each taxpayer, the taxpayer's spouse (if the taxpayer's status is "married filing jointly"), and each qualifying dependent. Husbands and wives who file separate tax returns must each claim their own exemption. A taxpayer may also claim a $20 credit for each exemption allowed for the taxpayer, the taxpayer's spouse, and dependents. Current law also provides for a number of different credits against the income tax.

Restructuring of the Ohio income tax

Single, "flat" income tax rate established, existing exemptions eliminated, $20 exemption credit eliminated, and new exemptions created

(R.C. 5747.02, 5747.022 (repealed), 5747.025 (repealed), and 5747.08)

The bill replaces the existing graduated tax rate structure with a single, "flat" income tax rate. Under the bill, every taxpayer pays tax on the taxpayer's taxable income at a rate of 3.5%.

The bill eliminates the $1,050 exemption for taxpayers, their spouses, and dependents. The bill also eliminates the $20 exemption credit. The bill replaces the exemptions and the $20 exemption credit with a $2,000 exemption for each dependent.[1] The bill also creates an exemption for each return filed by a taxpayer. The amount of the exemption depends upon the type of return filed. The exemption amount is $30,000 for each joint return and $15,000 for each single or separate return. The bill provides that a taxpayer does not have to file an income tax return if, after taking all of the exemptions to which the taxpayer is entitled under the bill, the taxpayer owes no taxes.

Exemption amounts adjusted for inflation

(R.C. 5747.02)

The bill requires that the Tax Commissioner annually adjust the $2,000 dependent exemption and the $15,000 and $30,000 filing exemptions to account for general price inflation. The adjustments are to occur in July of each year beginning in 2005. (The 3.5% income tax rate is not adjusted.)

New filing rules for married couples

(R.C. 5747.08)

Under existing law, a husband and wife who file a joint federal income tax return must file a joint Ohio return. Likewise, if a husband and wife file separate federal returns, then they must file separate Ohio returns. Under the bill, husbands

[1] *The amount of the dependent exemption ($2,000) was mistakenly omitted from the bill.*

and wives may elect to file separate or joint Ohio returns regardless of how they file their federal returns.

Existing deductions for individuals eliminated

(R.C. 3924.66, 3924.68, 3924.71 (repealed), 5733.40, 5747.01, and 5747.11)

The basis used to determine an individual's income tax liability is the individual's federal adjusted gross income. To compute Ohio income tax liability, taxpayers make several additions to, and deductions from, their federal adjusted gross incomes. The bill eliminates most of the existing deductions. Specifically, the bill eliminates the following:

(1) The deduction for disability and survivor's benefits;

(2) The deduction for social security and railroad retirement benefits;

(3) The deduction for the amount of wages and salaries that would have been allowable as a deduction in computing federal adjusted gross income had the targeted jobs credit under the Internal Revenue Code not been in effect;[2]

(4) The deduction for contributions to variable college savings program accounts;[3]

(5) The deduction for the purchase of tuition credits from the Ohio Tuition Trust Authority under the Ohio College Savings Program;

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[2] *The "targeted jobs credit" is also commonly known as the Work Opportunity Tax Credit (WOTC). The WOTC is a credit against the federal income tax for a portion of the first-year wages paid to an employee who is a member of a "targeted" group. Targeted groups include, among others, veterans, ex-felons, and high-risk youths. In calculating their federal income tax liabilities, employers may take a deduction for wages and salaries paid to their employees. Federal law requires that employers reduce these deductions by the amount of the WOTC. (Internal Revenue Code Section 51.) Unlike federal income tax law, Ohio law currently permits employers who receive the WOTC to deduct wages and salaries paid to employees (R.C. 5747.01(A)(7) and (S)(5)). The bill eliminates this deduction.*

[3] *A person may enter into an agreement with the Ohio Tuition Trust Authority (OTTA) under which the person opens an account with the OTTA on behalf of a beneficiary to pay for future tuition and other education expenses of the beneficiary. The OTTA contracts with insurance companies, banks, and other financial institutions to act as the OTTA's agents in investing moneys in these accounts. (R.C. Chapter 3334.)*

(6) The deduction for amounts paid for medical care insurance and qualified long-term care insurance for the taxpayer, the taxpayer's spouse, and dependents;

(7) The deduction for amounts paid by the taxpayer for medical care for the taxpayer, the taxpayer's spouse, and dependents;

(8) The deduction for amounts deposited to medical savings accounts and for the net investment earnings of medical savings accounts;[4]

(9) The deduction for amounts contributed to an individual development account program established by a county department of job and family services;[5] and

(10) The deduction for qualified tuition and fees paid to an eligible institution for the taxpayer, the taxpayer's spouse, or dependents.

Existing deductions for estates and trusts eliminated

(R.C. 5747.01)

For estates and trusts, income tax liabilities are calculated on the basis of federal taxable income. To compute their Ohio income tax liabilities, estates and trusts make a series of additions to, and deductions from, their federal taxable incomes. The bill eliminates several of the existing deductions. Specifically, the bill eliminates the following:

(1) The deduction for the amount of wages and salaries that would have been allowable as a deduction in computing federal taxable income had the

[4] *A medical savings account is an account opened by or on behalf of a person to pay the person's medical expenses or to pay the eligible medical expenses of a spouse or dependent. A taxpayer may deduct the taxpayer's total deposits in such accounts up to $3,000. (R.C. 3924.61 to 3924.74.) Because the bill eliminates the deduction for amounts deposited to medical savings accounts, the bill also eliminates the required addition for moneys withdrawn from medical savings accounts and used for purposes other than to pay eligible medical expenses. Similarly, the bill eliminates the required addition of amounts distributed from closed medical savings accounts.*

[5] *An individual whose household income does not exceed 150% of the federal poverty line is eligible to participate in an Individual Development Account Program. County departments of job and family services establish these programs, which are administered by nonprofit fundraising organizations. The accounts consist of moneys contributed by the participants and matching funds from other entities, including the county department. (R.C. 329.11 to 329.14.)*

targeted jobs credit under the Internal Revenue Code not been in effect (see footnote 2 under "***Existing deductions for individuals eliminated***" above); and

(2) The deduction for amounts, net of related expenses deducted in computing federal taxable income, which a trust is required to report as farm income on its federal income tax return.

Interest and interest equivalent on public obligations

(R.C. 5747.01)

Existing law allows taxpayers to take a deduction for interest and interest equivalent on public obligations to the extent that the interest or interest equivalent is included in federal adjusted gross income or federal taxable income. Similarly, existing law requires taxpayers to add any loss or deduct any gain resulting from the sale, exchange, or other disposition of public obligations to the extent the loss or gain has been taken into account in computing federal adjusted gross income or federal taxable income. The bill provides that these adjustments should only be made with respect to public obligations issued on or before the bill's effective date.

Existing credits eliminated

(R.C. 9.66, 122.152, 122.16, 122.17, 122.171, 150.07, 150.10, 901.13, 5703.05, 5709.65, 5709.66, 5733.33, 5733.42, 5747.05, 5747.051 (repealed), 5747.054 (repealed), 5747.055 (repealed), 5747.057 (repealed), 5747.058 (repealed), 5747.081 (repealed), 5747.21, 5747.211, 5747.212, 5747.26 (repealed), 5747.261 (repealed), 5747.27 (repealed), 5747.28 (repealed), 5747.29 (repealed), 5747.30 (repealed), 5747.31 (repealed), 5747.32 (repealed), 5747.33 (repealed), 5747.34 (repealed), 5747.35 (repealed), 5747.36 (repealed), 5747.37 (repealed), 5747.38 (repealed), 5747.39 (repealed), 5747.70 (repealed), 5747.75 (repealed), 5747.80 (repealed), 5747.98 (repealed))

The bill eliminates most of the existing income tax credits. In addition to eliminating the $20 personal exemption credit, the bill also eliminates the following:

(1) The $50 credit for taxpayers 65 years of age or older and the alternative credit for taxpayers 65 years of age or older who receive a lump sum distribution from a pension, retirement, or profit sharing plan;[6]

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[6] *An eligible taxpayer who elects to receive the alternative credit receives a credit equal to $50 times the taxpayer's expected remaining life as shown by annuity tables issued under the Internal Revenue Code.*

(2) The credit for taxpayers who are not 65 years of age or older but who receive a lump sum distribution from a pension, retirement, or profit sharing plan;[7]

(3) The joint filing credit;

(4) The credit for investment in property used in refining or manufacturing;

(5) The dependent care credit;

(6) The credit for taxpayers who receive retirement income;

(7) The credit for businesses that increase their sales to purchasers outside the United States (export sales);

(8) The credit for creating or retaining Ohio jobs;

(9) The credit for purchasing new manufacturing machinery or equipment;

(10) The credit for displaced workers who pay for job training;

(11) The credit for grape producing businesses that purchase property used in the grape production process;

(12) The credit for contributions to candidates for statewide office or the General Assembly;

(13) The credit for individuals or estates that purchase new manufacturing machinery and equipment;

(14) The credit for the economic redevelopment of a voluntary environmental clean-up site;[8]

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[7] *The credit is equal to $50 times the taxpayer's expected remaining life as shown by annuity tables.*

[8] *A person may undertake a "voluntary action" to identify and address potential sources of contamination on the person's property and to establish that the property meets applicable pollution standards. When the person undertaking a voluntary action determines that the property meets applicable standards, the person may seek a "no further action" letter from an environmental expert and a covenant not to sue regarding the property from the Director of Environmental Protection. A person issued a covenant not to sue may apply to the Director of Development to enter into an agreement with the Department of Development under which the applicant agrees to economically redevelop the property (i.e., use the property in a manner that will create employment opportunities) in exchange for tax credits against the corporation franchise and income taxes. (R.C. Chapter 3746. and 5747.32.)*

(15) The credit for investing in eligible Ohio research and development and technology transfer companies;

(16) The credit for pass-through entities that contract with a child day-care center to provide day-care services to their employees' children;

(17) The credit for pass-through entities that establish a day-care center;

(18) The credit for pass-through entities' reimbursement of their employees' day-care expenses;

(19) The credit for adopting a minor child;

(20) The credit for the costs associated with equipping a multi-wheel agricultural tractor with lights and reflectors;

(21) The credit for pass-through entities' eligible employee training costs;

(22) The credits for businesses that locate in enterprise zones;[9]

(23) The credit for investment in a certified ethanol plant; and

(24) The credit for losses on loans made under the Ohio Venture Capital Program.[10]

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[9] *Municipal corporations and counties may designate certain areas within the municipality or county as "enterprise zones." A municipality or county may enter into an enterprise zone agreement with a business for the purpose of fostering economic development in the enterprise zone. Under an enterprise zone agreement, the business agrees to establish or expand its operations within the enterprise zone, or to relocate its operations to the zone, in exchange for tax credits and other incentives. (R.C. 5709.61 to 5709.66.)*

[10] *The Ohio Venture Capital Program is a program designed to increase the amount of private investment capital available in Ohio for (1) Ohio-based businesses that are in seed or early stages of business development and (2) established Ohio-based businesses that are developing new methods or technologies. Under the program, moneys in a "program fund" are invested in venture capital funds, which in turn invest in the businesses described in (1) and (2) above. The program fund is funded through investments by private investors. Some of the profits from the program fund are put into the Ohio Venture Capital Fund (OVCF), which is used to secure the private investors against losses. To the extent the moneys in the OVCF are inadequate to secure an investor against losses, the investor is eligible for a tax credit against the income tax or other taxes to cover the portion of losses not covered by the OVCF. (R.C. Chapter 150.)*

Miscellaneous exemptions and $1 political contribution eliminated

(R.C. 5747.023 (repealed), 5747.024 (repealed), 5747.081 (repealed), and 5747.30 (repealed))

Currently, nonresident taxpayers are granted a tax exemption for their commercial printing activities in this state. The bill eliminates this exemption.

The bill also eliminates exemptions available to military personnel and civilian employees of the federal government who are killed in combat or as the result of a terrorist attack on foreign soil. Similarly, the bill repeals the existing exemption for all military pay and allowances received by members of the armed services.

Finally, existing law permits taxpayers to specify on their returns that $1 of their state income tax liability is to go to the Ohio Political Party Fund, the moneys of which are divided equally among Ohio's major political parties. The bill eliminates taxpayers' option of contributing to this fund.

Resident/nonresident credit maintained

(R.C. 5747.05)

Under existing law, a nonresident's Ohio income tax is computed in the same manner as a resident's, but a credit is allowed for that portion of the nonresident's income that is not earned in Ohio. Similarly, a resident is allowed a credit for income taxes paid to another state. The bill maintains these existing credits.

Effective date and credit carry forward provisions

(Sections 3 and 4)

The bill applies to taxable years beginning on or after January 1, 2004. However, taxpayers may claim any credit carry forward to which they are entitled on December 31, 2003. So, for example, if on December 31, 2003, a taxpayer has an unused portion of a credit that existing law permits the taxpayer to carry forward, the taxpayer may carry the credit forward into taxable year 2004 even if the credit is one of the credits repealed by the bill for taxable years beginning in 2004 and beyond.

HISTORY

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Introduced	03-11-03	p. 217

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