Ohio Legislative Service Commission

Bill Analysis

Mackenzie Damon

Sub. H.B. 58*

129th General Assembly

(As Reported by S. Ways and Means and Economic Development)

Reps. Beck, J. Adams, Boose, Blair, Derickson, Hackett, Hollington, Martin, Uecker, Amstutz, Stautberg, Letson, McClain, R. Adams, Anielski, Ashford, Baker, Balderson, Brenner, Bubp, Buchy, Burke, Butler, Carey, Carney, Coley, Combs, Damschroder, DeGeeter, Dovilla, Duffey, Fedor, Garland, Gonzales, Goodwin, Grossman, Hall, Hayes, Henne, Huffman, Johnson, Landis, Lundy, Maag, Mallory, McKenney, Mecklenborg, Milkovich, Newbold, O'Brien, Peterson, Phillips, Roegner, Rosenberger, Ruhl, Schuring, Sears, Slaby, Sprague, Stebelton, Thompson, Wachtmann, Young, Batchelder

Sens. Patton, Schaffer

BILL SUMMARY

- Incorporates into Ohio income tax law changes to federal tax law taking effect since December 15, 2010.

- Temporarily changes the formula used to trigger state extended unemployment benefits based on the total unemployment rate for the current time period the federal government is fully paying for those benefits for claimants of most private sector employers.

- Expands the existing job retention tax credit program to include a new, refundable job retention credit available to businesses that meet existing program requirements and additional criteria.

- Requires recipients of the new refundable credit to have received an offer of financial incentives from another state in 2010 that may induce the recipient to relocate and to have agreed to invest at least $25 million and retain at least 1,000 employees in Ohio.

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* This analysis was prepared before the report of the Senate Ways and Means and Economic Development appeared in the Senate Journal. Note that the list of co-sponsors and the legislative history may be incomplete.

- Authorizes the new credit only temporarily by limiting eligibility to projects the Director of Development, Director of Budget and Management, Tax Commissioner, and, if necessary, Superintendent of Insurance recommend before July 1, 2011.
- Limits the total of such credits to $8 million in any calendar year.
- States that municipal corporations may provide a similar refundable job retention tax credit against the municipal income tax.
- Declares an emergency.

CONTENT AND OPERATION

Incorporation of Internal Revenue Code changes

The bill incorporates into Ohio tax law recent changes to the Internal Revenue Code (IRC) or other federal law taking effect after December 15, 2010.[1] The changes being incorporated are those enacted by the "Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010," which took effect December 17, 2010. The incorporation applies to only general, undated references to the IRC or other federal laws, and does not apply to references that specify a date.

Ohio tax law incorporates by reference parts of the IRC and other federal laws. Periodic amendments to federal law do not become part of Ohio law unless they are incorporated by an act of the General Assembly.[2]

The principal amendments to the IRC that the bill incorporates are the following income tax provisions:

- Elementary and Secondary School Teacher Deduction
- Qualified Tuition Expenses Deduction
- Exclusion of IRA Distributions for Charitable Purposes
- Exclusion for Employer-Provided Educational Assistance
- Increased Deduction for Certain Environmental Remediation Expenditures

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[1] R.C. 5701.11.

[2] *Cf. State of Ohio v. Gill* (1992), 63 Ohio St.3d 53.

- Increased Depreciation for Certain Qualified Leasehold Improvements, Restaurant Property, and Retail Improvement Property
- Bonus Depreciation Deductions[3]
- Enhanced Expensing of Small Business Property
- Exclusion of National Health Service Corps and Armed Forces Scholarships
- Exclusion of Employer-Provided Adoption Assistance
- Dependent Care Credit

Most of the foregoing provisions are extensions of pre-2011 federal provisions. Many of them are extended only for a limited period of time. (For more information about the federal amendments, see the "Technical Explanation Of the Revenue Provisions Contained In The 'Tax Relief, Unemployment Insurance Reauthorization, And Job Creation Act of 2010' Scheduled For Consideration By The United States Senate," December 10, 2010, by The Joint Committee on Taxation, available at www.jct.com.)

Effect of incorporation

All but one of the federal amendments relate to exclusions or deductions affecting a taxpayer's federal adjusted gross income (or taxable income for trusts and estates), the starting number for determining the taxpayer's Ohio adjusted gross income or Ohio taxable income. If these amendments were not incorporated, a taxpayer would have to add these exclusions or deductions to the taxpayer's federal adjusted gross income or taxable income for purposes of computing the taxpayer's Ohio tax liability for taxable years beginning in 2011 and thereafter. (For 2010, taxpayers who applied the adjustments in computing their federal tax must add these amounts back to compute Ohio taxes because the adjustments were not incorporated.)

With respect to bonus depreciation deductions (IRC §168(k)) and enhanced expensing of small business property (IRC §179), ongoing Ohio law requires a taxpayer

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[3] The bill incorporates an extension of federal bonus depreciation deductions through January 1, 2013 (or January 1, 2014, depending on the type of property), as well as a temporary expansion of the deduction from 50% to 100% of the cost of qualifying property placed in service between September 8, 2010 and January 1, 2012 (January 1, 2013 for certain property). The bill also incorporates an expansion of small business property expensing provisions. However, the bill does not affect current Ohio law that, unlike federal law, requires taxpayers to claim bonus depreciation and small business property expensing over six years (see discussion under "**Effect of incorporation**").

to claim the additional deductions over six years.[4] In the first taxable year an asset is depreciated, or in the taxable year an item that may be expensed is purchased, Ohio law requires the taxpayer to add five-sixths of the bonus depreciation or enhanced expense to taxable income, permitting the taxpayer to receive only one-fifth of the bonus depreciation or enhanced expense. The remaining five-sixths of bonus depreciation or enhanced expense may be claimed in equal amounts over the ensuing five taxable years, in effect spreading out the enhanced deductions over six years.

The bill also revises Ohio tax law with respect to an election available to taxpayers whenever federal amendments become incorporated. Current law authorizes a taxpayer whose taxable year ended after October 16, 2009, and before December 15, 2010, to irrevocably elect to apply to the taxpayer's state tax calculation the federal tax laws that applied to that taxable year. (The October and December dates are the date of the two most recent incorporations.) The election was available to taxpayers who were subject to the corporation franchise tax or personal income tax and to electric companies that are subject to municipal income taxes.

The bill updates this election so that it may be made for a taxpayer's taxable year ending after December 15, 2010, but before the bill's effective date. The act retains a provision specifying that similar elections made under prior versions of the law remain effective for the taxable years to which the previous elections applied.

Extended unemployment benefits

The bill temporarily extends the look-back period from two years to three years for determining whether a state "on" indicator exists based on the total unemployment rate (TUR). When a state "on" indicator exists, claimants may be eligible to receive state extended unemployment compensation benefits. The change under the bill is in effect for compensation for weeks of unemployment beginning after December 17, 2010, and ending on or before December 31, 2011 (the date the current full federal funding discussed below expires).[5]

Ohio's Unemployment Compensation Law contains two triggers for purposes of state extended benefits – one based on the insured unemployment rate and one based upon the TUR. Currently, the state "on" indicator exists based upon the TUR, and the federal government is currently fully funding state extended unemployment benefits for claimants of contributory employers (most private sector employers). Because the TUR trigger is based, in part, on a comparison of that rate from the previous two years,

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[4] R.C. 5747.01(A)(20) and (21) and (S)(14).

[5] Section 3.

and because Ohio's unemployment rate has been high for an extended period of time, a possibility exists that Ohio will trigger "off" state extended benefits during the time period the federal government is fully funding the state extended benefits based upon the current method of calculating the state "off" indicator.

Background – state extended benefits

Unemployment compensation benefits are funded through a federal-state partnership. If an employer makes contributions to an approved state system, the employer receives almost a 90% tax credit on the employer's federal unemployment tax. The U.S. Department of Labor approves state systems, and approval involves state adherence to strict federal law requirements and Department regulations.[6]

Under Ohio's Unemployment Compensation Law, a claimant generally is eligible for unemployment compensation benefits for a period of 26 weeks. However, during times of economic difficulty, a claimant may be eligible for an additional 13 weeks of benefits, the cost of which is divided between the state and the federal government. Generally, the 50% paid by Ohio is charged to the account of a contributory employer, although reimbursing employers (public employers and some nonprofit companies) are charged the full amount of extended benefits. Under certain circumstances, the federal government pays the costs of state extended benefits, and contributory employers' accounts are not charged for that payment. Currently, as mentioned above the federal government is paying the costs of those benefits, and will continue to do so until the end of 2011 so long as the "state 'on' indicator" for extended benefits is triggered. The federal act that recently extended the federal funding for state extended benefits allows states to change the look-back period from two years to three years for purposes of determining whether a state "on" indicator exists.[7]

An extended benefit period, under continuing law, means a period that begins with the third week after a week for which there is a state "on" indicator and ends with either of the following weeks, whichever occurs later: (1) the third week after the first week for which there is a state "off" indicator, or (2) the 13th consecutive week of such period. However, no extended benefit period may begin by reason of a state "on" indicator before the 14th week following the end of a prior extended benefit period which was in effect with respect to Ohio.

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[6] See 26 U.S.C. 3301 *et seq*.

[7] See Sections 501 and 502 of the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010, P.L. 111-312.

Extended benefit period triggers using the TUR

The Director of Job and Family Services determines the state "on" indicator and the state "off" indicator in accordance with formulas specified in continuing law that are based on Ohio's insured unemployment rate or TUR. Under the bill, with respect to extended benefits triggered by the TUR, for weeks of unemployment beginning on or after December 17, 2010, and ending on or before December 31, 2011, a "state 'on' indicator" exists for Ohio for a week if the Director determines both of the following are satisfied:

(1) That the average TUR, seasonally adjusted, as determined by the U.S. Secretary of Labor, for the period consisting of the most recent three months for which data for all states are published before the close of that week equals or exceeds 6.5%;

(2) That the average TUR, seasonally adjusted, as determined by the Secretary, for the three-month period described in (1) immediately above, equals or exceeds 110% of the average for any or all of the corresponding three-month periods ending in the three (increased from two under current law) preceding calendar years.

Under the bill, for weeks of unemployment beginning on or after December 17, 2010, and ending on or before December 31, 2011, a "state 'off' indicator" exists for a week if the Director determines, in accordance with the Secretary's regulations, that for the period consisting of that week and the immediately preceding 12 weeks, the TUR, seasonally adjusted, under the Unemployment Compensation Law, was less than 110% of such average for any or all of the corresponding three-month periods ending in the three (increased from two under current law) preceding calendar years, and was less than 6.5%.[8]

Benefit amounts

Under continuing law, the Director is required to make the appropriate public announcement whenever an extended benefit period is to become effective in Ohio, as a result of a state "on" indicator, or an extended benefit period is to be terminated in Ohio as a result of a state "off" indicator. An individual qualifies for extended benefits if the individual has exhausted the individual's regular benefits and otherwise satisfies the requirements under the Unemployment Compensation Law to receive benefits. Under an extended benefit period triggered due to the insured unemployment rate, the total extended benefit amount payable to any eligible individual with respect to the individual's applicable benefit year is the lesser of the following amounts:

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[8] Section 3 and R.C. 4141.301(A), not in the bill.

(1) 50% of the total amount of regular benefits, including dependents' allowances, which were payable to the individual under the Unemployment Compensation Law, in the individual's applicable benefit year;

(2) 13 times the individual's weekly benefit amount, including dependents' allowances, which was payable to the individual under the Unemployment Compensation Law, for a week of total unemployment in the applicable benefit year; provided, that in making this computation, any amount that is not a multiple of one dollar is rounded to the next lower multiple of one dollar.

The amount of total extended benefits paid during an extended benefit triggered by the TUR is the same as those paid during an extended benefit triggered by the insured unemployment rate under continuing law, except during a "high-unemployment period." Continuing law defines "high-unemployment period" as a period during which an extended benefit period would be in effect if the TUR described in (1) under "**Extended benefit period triggers using the TUR**" above were applied by substituting "8%" for "6.5%."

Effective with respect to weeks beginning in a high-unemployment period, the total extended benefit amount payable to an eligible individual with respect to the applicable benefit year must be the lesser of the following amounts:

(1) 80% of the total amount of regular benefits that were payable to the individual pursuant to the act in the individual's applicable benefit year;

(2) 20 times the individual's average weekly benefit amount that was payable to the individual pursuant to the act for a week of total unemployment in the applicable benefit year.[9]

Refundable job retention tax credit

Credit eligibility

Existing law allows eligible businesses involved in significant capital investment projects to claim a nonrefundable job retention tax credit (JRTC) against the income tax, commercial activities tax, insurance company premiums tax, or corporation franchise tax. Qualifying businesses receive a credit measured as a percentage of the state income taxes withheld from full-time employees working at the project site. The bill expands the JRTC to permit businesses that meet existing JRTC requirements to claim a new, refundable tax credit if the business also meets the following criteria:

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[9] R.C. 4141.301(E) and (F), not in the bill.

(1) The Tax Credit Authority, which reviews and approves JRTC applications, must receive a recommendation to grant the refundable credit to the eligible business from the Director of Development, Director of Budget and Management, Tax Commissioner, and Superintendent of Insurance (in the case of an insurance company) before July 1, 2011;

(2) The business must employ and retain at least 1,000 "full-time equivalent employees." Under current law, a business' number of "full-time equivalent employees" is calculated by dividing its total employee-hours at the project by 2,080, which is the number of hours in a 40-hour-per-week, 52-week work year.

(3) The business must make a capital investment of at least $25 million at a project site over a period of three years that includes the year for which the credit is granted;

(4) In 2010, the business must have received a written offer of financial incentives from another state, and the Director of Development must have determined that the offer is sufficient inducement for the business to relocate to that other state.[10]

Differences between new refundable and existing nonrefundable JRTCs

Refundability

Under current law, a business may not claim a JRTC in excess of the business' annual tax liability. The excess, however, may be carried forward for up to three years. The bill permits a business that qualifies for a refundable JRTC to claim the full amount of the credit in one year; if the amount of the credit exceeds tax liability, the business would be entitled to a refund.[11]

Employee retention and capital investment requirements

In order to qualify for the nonrefundable JRTC under existing law, a business need only employ and retain at least 500 full-time equivalent employees. The bill requires that a recipient of a refundable JRTC employ and retain at least 1,000 such employees.

Under the bill, to be considered an "eligible business" for the purposes of either credit, the business must invest at least $50 million in assets for manufacturing operations or $20 million in assets for "significant" corporate administrative functions. However, as noted above, businesses applying for the new refundable JRTC would

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[10] R.C. 122.171(A) and (B).

[11] R.C. 122.171(B).

need to demonstrate a capital investment of at least $25 million regardless of investment type. For either credit, the required capital investment must involve capitalized costs of basic research or new product development, or the acquisition, construction, renovation, or repair of buildings, machinery, or equipment.[12]

Credit amount and term

As under existing law, the bill requires that the amount and term of a refundable JRTC be specified in an agreement between the eligible business and the Tax Credit Authority. The amount of either credit may equal up to 75% of the state income taxes withheld from eligible full-time employees. An eligible business may receive either credit for a period of up to 15 years; however, under existing Department of Development regulations, the Tax Credit Authority may not grant a JRTC for a term longer than ten years unless the Authority determines that there is "significant retention" of employees associated with the project.[13]

Credit application and agreement

The bill requires recipients of a refundable JRTC to comply with the same application procedures, agreement provisions, and reporting measures required of recipients of the existing nonrefundable JRTC. Under either program, an eligible business must apply to the Tax Credit Authority to enter into a tax credit agreement. The agreement must describe the capital investment project that is the subject of the agreement and require the business to retain a specified number of full-time equivalent employees (at least 1,000 in the case of the refundable JRTC proposed in the bill). The agreement must also require that the business maintain operations at the project site for at least the greater of (1) the term of the credit plus three years, or (2) seven years. In order to continue receiving either credit, the business must file annual reports with the Department of Development and receive a certification verifying the accuracy of the reports.[14]

If a business fails to comply with any of the conditions specified in a tax credit agreement, the Tax Credit Authority may amend the agreement to reduce the percentage or term of the credit.[15]

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[12] R.C. 122.171(A) and (B).

[13] R.C. 122.171(B); O.A.C. 122:16-1-04.

[14] R.C. 122.171(C) and (E).

[15] R.C. 122.171(F).

Aggregate credit limits

Current law limits the total amount of nonrefundable tax credits issued in any calendar year. In 2010, the limit was $13 million; this amount will increase every year between 2011 and 2024 by $13 million over the previous year's amount until the total reaches $195 million.

The bill limits the total amount of refundable tax credits at $8 million in any calendar year.[16]

Municipal income tax credit

Under current law, municipal corporations are expressly permitted to provide a nonrefundable credit against its income tax to businesses that qualify for the state JRTC. The bill states that municipal corporations also may provide a refundable credit for businesses that meet the requirements of the proposed refundable JRTC.[17]

Emergency clause

The bill declares an emergency, causing the bill to become effective immediately and exempting it from the referendum.

HISTORY

ACTION	DATE
Introduced	01-26-11
Reported, H. Ways & Means	02-10-11
Passed House (89-7)	02-15-11
Reported, S. Ways & Means & Economic Development	---

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[16] R.C. 122.171(M).

[17] R.C. 718.151. Since municipal corporations impose income taxes pursuant to their constitutional home rule powers (subject to limitation by the General Assembly), it is not clear that they need authorization from the legislature to grant job retention tax credits under current law or under the bill.