Ohio Legislative Service Commission

Final Analysis

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Am. S.B. 28

130th General Assembly
(As Passed by the General Assembly)

Sens. Obhof, Hite, Schaffer, Tavares, Beagle, Coley, Faber, Hughes, Oelslager, Peterson, Sawyer, Seitz, Uecker

Reps. Boose, Letson, Barnes, McClain, Patmon, Rogers, Sprague, J. Adams, Amstutz, Beck, Bishoff, Buchy, Conditt, Milkovich, O'Brien, Pillich, Scherer, Smith, Winburn, Batchelder

Effective date: Emergency, March 22, 2013

ACT SUMMARY

- Incorporates into Ohio income tax law changes to federal tax law taking effect since December 20, 2012.
- Allows suppliers of a distribution center to qualify for the existing commercial activity tax (CAT) exclusion for receipts from sales to qualified distribution centers (QDC) if the QDC does not currently meet the exclusion requirements but expects to meet those requirements in three years.
- Adjusts penalties that an operator of a QDC must pay for qualified distribution receipts improperly excluded by suppliers.
- Requires the Tax Commissioner to notify a qualified distribution center's suppliers after an exemption certificate is issued to the center's operator and removes the obligation of the operator to notify such suppliers.

CONTENT AND OPERATION

Incorporation of Internal Revenue Code changes

The act incorporates into Ohio tax law recent changes to the Internal Revenue Code (IRC) or other federal law taking effect after December 20, 2012.[1] The changes

[1] R.C. 5701.11.

being incorporated are those enacted by the "American Taxpayer Relief Act of 2012," which took effect January 2, 2013. 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 act incorporates are the following income tax provisions:

- Elementary and Secondary School Teacher Deduction
- Qualified Tuition Expenses Deduction
- Student Loan Interest Deduction
- Exclusion of IRA Distributions for Charitable Purposes
- Exclusion for Employer-Provided Educational Assistance
- Exclusion of National Health Service Corps and Armed Forces Scholarships
- Increased Depreciation for Certain Qualified Leasehold Improvements, Restaurant Property, and Retail Improvement Property
- Bonus Depreciation Deductions and Enhanced Expensing (Ohio departs from federal income tax law and generally requires taxpayers to spread the immediate tax reductions from Bonus Depreciation and Enhanced Expensing in equal parts across six years)
- Exclusion of 100% of Gain on Certain Small Business Stock
- Exclusion of Discharge of Principal Residence Indebtedness for Individuals
- Parity for Exclusion for Employer-Provided Mass Transit and Parking Benefits
- Dependent Care Credit

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

Most of the foregoing provisions are extensions of pre-2013 federal provisions. Many of them are extended only for a limited period of time. (For more information about the federal amendments, see the "Estimated Revenue Effects Of the Revenue Provisions Contained In An Amendment In The Nature Of A Substitute To H.R. 8, The 'American Taxpayer Relief Act Of 2012,' As Passed By The Senate On January 1, 2013," January 3, 2013 by The Joint Committee on Taxation, available at www.jct.gov).

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 had 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 2013 and thereafter. (For 2012, taxpayers who applied the adjustments in computing their federal tax would have had to add these amounts back to compute Ohio taxes if the adjustments had not been incorporated.)

The act also revises Ohio tax law with respect to an election available to taxpayers whenever federal amendments become incorporated. Prior law authorized a taxpayer whose taxable year ended after March 7, 2011, and before December 20, 2012, to irrevocably elect to apply to the taxpayer's state tax calculation the federal tax laws that applied to that taxable year. (The March and December dates are the dates of the two preceding 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 act updates this election so that it may be made for a taxpayer's taxable year ending after December 20, 2012, but before the act'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.

Repeal of Ohio federal estate tax credit "pick-up" taxes

The act also has the effect of conclusively repealing Ohio's federal estate tax credit "pick-up" taxes, often referred to as "sponge" taxes. Ohio enacted, as supplements to its general estate tax, an additional estate "sponge" tax and a generation-skipping "sponge" tax, which provided revenues to state and local governments drawn from federal estate tax credits for amounts paid by estates for state estate taxes that until 2005 had been allowed against federal estate and generation-skipping taxes.[3] Both federal credits were phased out by Congress, and the General Assembly subsequently incorporated the federal phase-out. The federal credits were scheduled to revive in 2013 and possibly with them Ohio's "sponge" taxes, but Congress permanently eliminated the credits in the American Taxpayer Relief Act, effective January 2, 2013. The act conforms state law to reflect the permanent elimination of the federal credits and thus conclusively repeals both of Ohio's "sponge" taxes.

Qualified distribution center requirements

The act allows suppliers of a distribution center to qualify for the existing commercial activity tax (CAT) exclusion for receipts from sales to a "qualified distribution center" (QDC) if the QDC does not currently meet the exclusion requirements but expects to meet those requirements in three years. The act additionally adjusts the penalties that an operator of a QDC must pay for qualified distribution receipts improperly excluded from the CAT base by suppliers. Previously, the operator was liable for the tax, interest, and penalties on the excluded receipts, but, under the act, the operator is instead subject to a flat penalty of $500,000 for each year supplier receipts were improperly excluded.

Tax base

The CAT is an annual excise tax imposed on businesses for the privilege of doing business in Ohio. The tax base or measure for the CAT is "taxable gross receipts." Generally, taxable gross receipts are a company's gross receipts that are attributed to the company's Ohio business activity as prescribed under the "situsing" or attribution rules. Taxable gross receipts are derived from a company's "gross receipts," which is defined broadly to include all amounts realized that contribute to the production of gross income. There are currently over 35 categories of receipts that are at least partly excluded from the gross receipts base from which taxable gross receipts is derived.[4]

Exemption for qualifying distribution center receipts

Continuing law provides one such exclusion for a percentage of receipts derived from property shipped to a QDC. A QDC includes a warehouse or other similar facility in Ohio that has obtained a certificate from the Tax Commissioner indicating that the facility's suppliers qualify for the exemption. Every applicant for the certificate must substantiate to the Commissioner's satisfaction that, during a 12-month period (July to June), all persons operating the center had more than 50% of the cost of the property

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[3] R.C. 5731.18 and 5731.181.

[4] R.C. 5751.01(F) and (G).

shipped from the center sitused to a location outside Ohio, using existing CAT situsing rules. An applicant must also substantiate that the distribution center had cumulative costs from its suppliers equal to or exceeding $500 million for the period. A $100,000 application fee must accompany each application.

The Commissioner may approve an application and issue a certificate for the QDC that covers a 12-month period between July and June. To qualify for the exclusion, a supplier must deliver property to the QDC certificate holder solely for further shipping by the center to another location inside or outside Ohio. The property may be stored or repackaged into smaller or larger bundles, but may not be subjected to further manufacturing or processing at the distribution center.

Only a percentage of a QDC supplier's receipts from delivered property is exempt from taxation. The percentage exempted equals the percentage of property shipped by the distribution center to locations outside Ohio during a 12-month period ("Ohio delivery percentage"). Under continuing law, the Commissioner is required to calculate the Ohio delivery percentage, and the operator may appeal the Commissioner's determination of a QDC's Ohio delivery percentage. Prior law required, 30 days after the exhaustion of all appeals, that the QDC operator notify the operator's suppliers of the suppliers' duty to file amended CAT reports to account for the Commissioner-determined Ohio delivery percentage. Under the act, the operator instead must provide a list of such suppliers to the Commissioner, who must notify the suppliers of the requirement to file amended CAT reports.[5]

Expansion of exclusion to transitioning distribution centers

The act authorizes the Tax Commissioner to issue a certificate that would allow suppliers to a distribution center that does not meet the requirements of a QDC to qualify for the exclusion if the center's operator demonstrates that the center's operations will change so that the center will be eligible for the certificate within 36 months after the date the operator applies for the certificate. If, at the end of this period, the distribution center still does not meet the requirements of a QDC, the operator is subject to an appealable penalty of $500,000 for each year the center received a certificate. For each year the distribution center was issued a certificate, the operator must pay the $100,000 annual application fee and submit an updated business plan to the Commissioner showing the progress the center made toward meeting the requirements of a QDC during the previous year.[6]

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[5] R.C. 5751.01(F)(2)(z)(iii).

[6] R.C. 5751.01(F)(2)(z)(ii)(II).

The operator of the distribution center must make a good faith estimate of the center's Ohio delivery percentage that the operator estimates will apply at the end of the 36-month period. The estimated percentage is multiplied by 1.75, and the result is the center's Ohio delivery percentage for the 12-month period. If the distribution center's Ohio delivery percentage under this calculation would exceed 49%, the Ohio delivery percentage is set at 49%; if less than 5%, the percentage is set at 5%.[7]

Penalties for improperly excluded qualified distribution center receipts

Under continuing law, if a distribution center is new and not open for the entire July-June 12-month period, the operator may nevertheless request and receive a certificate for the entire period. Under prior law, if the Commissioner determined that less than 50% of the qualified property was not delivered outside of Ohio or the operator had average monthly costs from its suppliers of less than $40 million, the operator was liable for all tax, interest, or penalties on the amounts claimed by suppliers as excluded receipts.

The act requires an operator to pay a $500,000 penalty for each year rather than having to pay tax, interest, or penalties on improperly excluded receipts.[8]

Similarly, prior law imposed on a certificate holder liability for any tax, interest, and penalties for receipts excluded by suppliers in years in which the certificate should not have been issued because the certificate holder did not meet statutory requirements, but in which the suppliers relied in good faith on an issued certificate. The act instead requires certificate holders in such instances to pay a $500,000 penalty for each year that the certificate should not have been issued.[9]

HISTORY

ACTION	DATE
Introduced	02-12-13
Reported, S. Ways & Means	02-28-13
Passed Senate (33-0)	03-05-13
Reported, H. Ways & Means	03-19-13
Passed House (94-1)	03-20-13
Senate concurred in House amendments (33-0)	03-20-13

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[7] R.C. 5751.01(F)(2)(z)(iv).

[8] R.C. 5751.01(F)(2)(z)(ii)(I).

[9] R.C. 5751.01(F)(2)(z)(v).