

# Fiscal Note & Local Impact Statement

## 125<sup>th</sup> General Assembly of Ohio

Ohio Legislative Service Commission  
77 South High Street, 9<sup>th</sup> Floor, Columbus, OH 43215-6136 ✦ Phone: (614) 466-3615  
✦ Internet Web Site: <http://www.lsc.state.oh.us/>

BILL: **Sub. H.B. 204** DATE: **May 12, 2004**

STATUS: **As Enacted – Effective November 5, 2004** SPONSOR: **Rep. Wolpert**  
**(Section 4 to 9 effective August 5, 2004)**

LOCAL IMPACT STATEMENT REQUIRED: **Yes**

CONTENTS: **Provides for the use of electronic records and signatures by county offices if specified security procedures are adopted, requires the Auditor of State to audit electronic record security procedures adopted by the counties, and creates a single definition of "Internet" to be used throughout the Revised Code; delays the effective date of certain sales and use tax sourcing laws**

### State Fiscal Highlights

STATE FUND	FY 2005	FY 2006	FUTURE YEARS
<b>General Revenue Fund</b>			
Revenues	- 0 -	- 0 -	- 0 -
Expenditures	Potential minimal increase	Potential minimal increase	Potential minimal increase
<b>Fund 442, Public Audit Expense</b>			
Revenues	- 0 -	- 0 -	- 0 -
Expenditures	Potential minimal increase	Potential minimal increase	Potential minimal increase

Note: The state fiscal year is July 1 through June 30. For example, FY 2005 is July 1, 2004 – June 30, 2005.

- Expenses may increase for the Auditor of State due to the requirement placed on the Auditor to audit electronic record security procedures in county offices. However, these expenses would likely be minimal. Audit expenses are paid by a combination of state and local funds.
- Creates the Ohio Privacy/Public Record Access Study Committee. The committee is to prepare a report of its findings on several specified issues. Although it is assumed that there would be minimal administrative expenses as a result, the bill does not specify who is responsible for committee expenses. The bill does not specify whether the 23 members are to be reimbursed for their expenses.
- Expands the payment methods by which taxes, fees, and other payments can be made to the state. Allowing more types of transactions to be classified as "financial transaction devices" may reduce transaction costs. There may be initial costs involved for any computer software or hardware necessary to set-up an electronic payment system.



- Delays the effective date of destination-based sourcing for sales and use tax purposes to July 1, 2005, from January 1, 2005. However, certain vendors may still choose to apply the new sourcing rules anytime after January 1, 2005. This change has a minimal fiscal effect.

## ***Local Fiscal Highlights***

<b>LOCAL GOVERNMENT</b>	<b>FY 2004</b>	<b>FY 2005</b>	<b>FUTURE YEARS</b>
<b>Counties</b>			
Revenues	- 0 -	- 0 -	- 0 -
Expenditures	Potential increase in expenses to upgrade unprotected systems	Potential increase in expenses to upgrade unprotected systems	Potential increase in expenses to upgrade unprotected systems

Note: For most local governments, the fiscal year is the calendar year. The school district fiscal year is July 1 through June 30.

- Potential increase in expenses to counties engaged in electronic commerce to install or upgrade security programs to meet the requirements of the bill. Costs would apply in specific cases if a county were engaged in a form of electronic commerce without the required security programs in place.
- Allows counties or townships to participate in contract offerings from the General Services Administration within the federal government, as well as other cooperative purchasing programs sponsored by national or state organizations that represent political subdivisions, and sets conditions for exempting these entities from competitive selection requirements. Counties and townships have the option of entering into contracts to purchase supplies or services from another party outside of those participating in a national or state association of political subdivisions. This can be done if the vendor can offer a price lower than those participating in the association of political subdivisions. Depending on the services or goods to be acquired, this may reduce purchase costs for counties or townships. However, the main effect would be to expand the procurement choice beyond those currently available to political subdivisions.
- Delays the effective date of destination-based sourcing for sales and use tax purposes to July 1, 2005, from January 1, 2005. However, certain vendors may still choose to apply the new sourcing rules anytime after January 1, 2005. This change has a minimal fiscal effect.

---

## ***Detailed Fiscal Analysis***

### **County Electronic Records**

House Bill 204 stipulates that county security software/systems must provide security in four ways: (a) signature verification, (b) verification of records, (c) verification of a performance of a specific person, and (d) detection of changes and errors. The bill identifies that security procedures would minimally include (a) the use of algorithms or other codes, (b) identification of words and numbers, (c) encryption, (d) callback or other acknowledgment procedures.

Counties that are already engaged in electronic commerce may already have software that has security measures, firewalls, etc. in place because security programs may have been built into the customized programming and applications at the time these products were installed. However, in any case where a county might be engaged in e-commerce without the required security measures, the county would incur costs to bring security up to the required level. In such a case, the costs to the county could potentially be significant.

The two general security categories addressed by the bill are (a) signature verification and (b) record integrity. If a software engineer/consultant were to start with a client's existing commercial system and modify or enhance the system to perform these required functions, the costs would vary with the degree of work required and the complexity of the functions the system must perform. For example, to modify a system to securely handle the sale of a license would cost much less than to modify a system to securely handle something much more complex such as processing property tax payments.

Using an example of the county auction, either a reverse auction or a forward auction, one would see that they require the acceptance of a bid, and in some cases, the verification of a signature. In the electronic domain, there are essentially two options available to assure electronic signature verification: (a) customized software designed specifically for the customer, in which case the customer assumes the liability and costs for the security systems, or (b) web-based services, within which the security costs are pre-built. The costs of web-based services may range from \$0 to \$20,000 per year. Generally, web-based options carry lower costs than custom-designed and programmed products.

The bill allows counties or townships to participate in contract offerings from the federal government including, but not limited to, from general services administration. Acquisition of equipment, supplies, or services by a county or township, through participation in a contract of another county or township is exempt from competitive selection, if the contract was awarded pursuant to a publicly solicited request for proposal. Acquisition of supplies, equipment, or services pursuant to participating in contract offerings from the federal government as listed in (A)(3) in the bill is exempt from competitive selection. A county or township eligible to participate in a joint purchasing program operated by or through a national or state association of political subdivisions in which the purchasing county or township is eligible for membership may purchase supplies or services from another party, instead of through participation in contracts authorized in (A)(2) of the bill. In order to do so, the county or

township must show that the other party can provide the supply or service upon equivalent terms, conditions, and specifications, but at a lower price than the providing party in the previous contracts. Purchases made under these terms are exempt from competitive selection procedures. Presumably, such a process would allow these political subdivisions to acquire goods or services at a lower price, and thereby lower costs.

### **Technical Variables – A Wide Range of Costs**

If a county government needed to revise the infrastructure of their chosen electronic commerce activity in order to meet the provisions of the bill (rather than upgrade their current system), several factors would need to be taken into consideration. While some programs are free to government, some service providers charge relatively large fees. Overall, costs could vary from \$0 to more than \$20,000 per year, with the choice in the hands of the county.

#### **Hosts**

A county or other entity could contract with a secured hosting service such as Verisign, and for under \$100 a month in charges, complete up to 1,000 transactions a month by electronic card or check.

#### **Template Sites**

In some cases, a county may be able to complete a county auction of surplus materials by leasing a secured “template site” specifically for auction purposes from a company like Yahoo at a cost of approximately \$60 per month.

#### **Web Design**

Costs could be incurred if a county chose to contract with a web designer for development of a customized web site. Rates for web site designers range from \$50 to \$100 per hour and a basic web site could require at least two to four weeks (or 80 to 160 hours) to complete.

#### **Technical Support**

Charges could be incurred if the county elected to contract for technical support services through a company such as Sarcom. Technical support costs could vary widely depending upon the frequency and type of technical issues that required attention.

#### **Bandwidth**

If a county contracted with a company like Yahoo, the costs for use of necessary bandwidth would be included. However, if not leasing with a company like Yahoo, the county would need a permanent high speed circuit with a dedicated line at a cost of approximately \$600 per month.

### *Added Charges*

Some electronic procurement/electronic commerce tools are known to charge a percentage of each transaction in addition to the initial and/or monthly charges.

### *Disposing of County Records*

When the Ohio Historical Society is informed that public records of a county are to be disposed of, the county records commission must notify the county historical society and certain other organizations. Then the county historical society and other organizations may select records of continuing historical value. This provision could result in minimal cost increases for counties for county record commissions to make notifications.

### *Ohio Privacy/Public Record Access Study Committee*

The bill creates the Ohio Privacy/Public Record Access Study Committee. The committee consists of 23 members, both public officials and private industry representatives. The President of the Senate appoints 3 members. The Speaker of the House appoints 3 members as well. The Governor appoints the remaining 16. The committee is to study the following:

1. The concerns associated with the dissemination of personal information contained in public records.
2. The legitimate uses of personal information contained in public records by businesses, governments, the legal community, and others.
3. The costs to state and local governments associated with placing restrictions on access to personal information contained in public records.
4. The impact on legitimate businesses, law enforcement, the legal community, government agencies, and others.
5. The impact of protecting disclosure of personal information contained in public records.
6. Electronic, Internet, and bulk access to personal information contained in public records.
7. Current and potential future misuse, fraud, harassment, and identity theft prevention and detection efforts.
8. Existing criminal and civil penalties for misuse of personal information contained in public records.

The committee must submit a report of its findings to the President of the Senate, Speaker of the House, Minority Leader of the Senate, Minority Leader of the House, the Governor, and the Chief Justice of the Supreme Court no later than 12 months after the appointment of all the members of the committee. Presumably, there would be minimal administrative costs in preparing this report. The bill does not mention whether the committee members are to be compensated for their expenses related to the committee's business.

## **Financial Transaction Devices**

The bill expands the options by which fees, taxes, penalties, and other such payments due the state can be made. The specific guidelines are to be prepared by the State Board of Deposit. The bill expands the definition of what is considered a financial transaction device to include automated clearinghouse network credit, debit, or e-check entry that includes, but is not limited to, accounts receivable and Internet-initiated, point of purchase, and telephone-initiated applications. Any surcharge or convenience fee that is imposed must follow the guidelines of the financial institution, issuer of financial transaction devices, or processor of financial devices. Although there might be some initial start-up costs, this expansion of what is considered a financial transaction device could potentially lower the administrative costs associated with the payment of state expenses.

## **Sales and Use Tax Sourcing Law**

Uniform sourcing standards for the taxation of sales, which must be adopted by all member states, are an important piece of the streamlined sales tax agreement (the Agreement) and the streamlined sales tax project (SSTP). The SSTP is an effort by states and private retailers to simplify and modernize sales and use tax administration and collections throughout the United States. The recommendations of the SSTP are contained in the Agreement that must be adopted by member states. States such as Ohio are required to adopt the destination-based sourcing of sales to participate fully in the next phases of the SSTP. Beginning in January 1, 2005, Ohio law adopts the Agreement's sales tax sourcing provisions. Under current law and until that date, sales of tangible personal property and services are generally deemed to occur at the seller's place of business, even if the property or service is received or delivered elsewhere (an origin-based or a point of sale sourcing of sales). Under the Agreement, for sales that are delivered or received elsewhere than the seller's place of business (e.g., remote sales), a sale of property or service is sourced at the point of destination (destination-based sourcing), where the buyer actually receives the property or the service. The change in the sourcing of sales does not substantially change revenues from the taxation of motor vehicles, watercraft, and outboard motors that are titled. In those transactions, buyers pay the tax based on the sales and use tax rate in effect in their locality of residence. Am. Sub. H.B. 95 of the 125th General Assembly delayed the effective date of previously adopted (in S.B. 143 of the 124th General Assembly) destination-based standards for sales and use tax purposes until January 1, 2004. That effective date was further delayed until January 1, 2005, under Sub. H.B. 127 of the 125th General Assembly.

Adopting the destination-based sourcing standards would result in both gains and losses to local jurisdictions as the location of certain sales for tax purposes shifts from retail outlets to where sales are delivered. Generally, most sales are taxed at the rate in effect at the point of sale (customer leaves the business location with the item) or the items are delivered within the same taxing jurisdiction. However, whenever the location of the sale and the delivery are in different counties, local sales tax rates may be different. Few studies on the effects of sales tax sourcing changes have been conducted. A report from the Department of Revenue for the state of Washington<sup>1</sup> estimates that approximately 15% of that state local sales tax base is affected by the Agreement. Ohio nonauto taxable base was about \$114 billion in FY 2003. Assuming that 10% to 20% of this taxable base is affected by the change to from point-of-

---

<sup>1</sup> *Streamlined Sales and Use Tax Agreement Sourcing Study*. Washington State Department of Revenue, December 2003.

sale to destination-based sourcing of sales, the value of goods and services that would change location for local sales tax purposes may be \$11.4 billion to \$22.8 billion. Applying an average local tax rate of 1.1% in Ohio, \$125 million to \$251 million per year in sales tax revenue might be redistributed among counties as a consequence of the destination-based sourcing standards.

When this shifting occurs, an individual local jurisdiction may incur net revenue losses if the value of purchases from businesses inside its boundaries but delivered elsewhere exceeds the value of deliveries within the local jurisdiction's boundaries from outside purchases. Local jurisdictions will have a net gain if the opposite occurs. However, the change to destination-based sourcing of sales generally affects the redistribution of sales tax revenues to local governments, but does not substantially change the total amount of revenue collected by all local governments within the state, at least until the Agreement is effective and provide additional revenue from enhanced tax collections.

The bill postpones the effective date of the application of destination-based sourcing to July 1, 2005. However, the bill also allows any vendor to switch to destination-based sourcing anytime after January 1, 2005 and before July 1, 2005. Once the switch is made, the vendor is not allowed to revert back to the origin-based sourcing of sales. This change has a minimal fiscal effect, although the six-month transition period during which vendors use different sourcing of sales might create some practical issues in the administration of sales and use tax in the Department of Taxation.

*LSC fiscal staff: Terry Steele, Budget Analyst  
Carol Robison, Budget Analyst  
Jean Botomogno, Economist*

*HB0204EN/arc*