
Detailed Fiscal Analysis

House Bill 165

Under current law, a vendor that sells a taxable good or service to a person is required to collect the Ohio sales tax and any sales or use tax imposed by the state and the county or transit authority where the sale is deemed to be taxable under "situs" or sourcing rules. Since 2003, vendors have been required to use a new set of sourcing rules called destination-based sourcing for determining where a sale is taxable. Under these rules, a sale generally is taxable where the consumer takes possession of the goods, at the consumer's address, or where the service is performed. Because the destination-based sourcing rules do not assign the tax to the point of sale, a vendor selling to multiple taxing jurisdictions (including other states) must determine the use tax rates of those other jurisdictions. To assist vendors with this effort, the Streamlined Sales and Use Tax Agreement (SSTA) authorizes vendors to use certified service providers, which calculate the appropriate tax, collect it, and remit it to the appropriate state on the vendor's behalf.

Changes to the sourcing rules

To provide time for vendors to convert to the destination-based sourcing rules and for certified service provider services to be established, Ohio law provided a transition period. The general deadline for conversion to the destination-based rules was May 1, 2006, subject to a significant exception: for vendors whose sales to consumers in other jurisdictions are less than \$30 million per year, the deadline to start the new sourcing rules was extended until December 31, 2007.

The bill repeals the conversion deadline. Businesses that have not converted to the destination-based rules by the bill's effective date are required to continue using the origin-based sourcing rules. LSC assumes that most vendors that have not converted are those vendors falling under the \$30 million per year exception. The bill allows, but does not require, vendors that had already converted to return to the origin-based sourcing rules.

Vendor compensation

Under the bill, vendors using destination-based sourcing on the bill's effective date may continue to apply for and receive financial assistance for converting to destination-based sourcing under ongoing law. Under continuing law, financial assistance is available for vendors converting to the destination-based rules if the vendor was licensed prior to May 1, 2006. The financial assistance is provided for six months and equals the amount of tax the vendor collects per county, per month for sales of tangible personal property delivered to each county in which the vendor does not have a fixed place of business and in which the vendor does not, or is not required to, hold a vendor's license for that business. Compensation is limited to the lesser of the vendor's costs of conversion or \$25 per county, per month.

Uniform state and local tax rate

The bill requires the Tax Commissioner to develop a plan to allow in-state and out-of-state vendors to elect to collect and remit Ohio and local use taxes at a uniform rate, instead of at the several rates applying in the various counties. The Commissioner's plan also must address how revenue generated from the local portion of the tax would be distributed among counties and transit authorities. Currently, revenue from sales and use taxes levied by a county or transit authority is returned to the county or transit authority less a fee of 1% to fund the state's administrative costs. The bill requires the Tax Commissioner to submit the plan to the General Assembly by January 31, 2008.

Fiscal impact

Direct effect

The bill has no direct fiscal effect on state revenue. However, the bill may create local indirect effects as certain businesses change the situsing of taxation of goods and services sold.

The bill creates a hybrid system where both an origin-based sourcing system and a destination-based sourcing system for situsing sales for tax purposes co-exist. Requiring certain vendors to continue and allowing others to revert to origin-based sourcing may result in both gains and losses to local jurisdictions as the tax location of certain sales may shift from vendor outlets to where sales are delivered, or from where sales are delivered to the point of purchase of goods and services. 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. For such sales, the bill would have no fiscal effect. However, whenever the location of the sale and the delivery are in different counties, although the state rate is the same, local sales tax rates may be different. When this shifting occurs, an individual local jurisdiction may incur a net revenue gain or loss depending on the value of purchases at businesses inside its boundaries and delivered elsewhere, the value of purchases by its residents in other jurisdictions and delivered at their residences, and whether the vendors apply origin-based or destination-based sourcing rules. Thus, the bill generally affects the redistribution of certain sales tax revenues to local governments, but does not substantially change the total amount of revenue collected by all local governments within the state.

The number of vendors that would choose to convert back to origin-based sourcing rules is uncertain. Also, the magnitude of the potential shifting of taxable sales, and the net fiscal effect on various jurisdictions is indeterminate. Large vendors that have already converted to destination-based sourcing may have little incentive to convert back as a result of the bill. Smaller vendors may find it more cost efficient to convert back to origin-based sourcing. Current law does not provide for compensation when a vendor converts back to origin-based sourcing. Thus, allowing vendors to continue to apply for and receive financial assistance for converting to destination-based sourcing is expected to have a minimal state fiscal effect on the General Revenue Fund. The requirement of the Tax Commissioner to develop a plan to allow in-state and out-of-state vendors to elect to collect and remit Ohio and local use taxes at a uniform rate has no direct fiscal impact on revenues or expenditures.

Potential future indirect effects

The elimination of the requirement for all vendors to convert to destination-based sourcing might prevent Ohio from becoming a party to the Streamlined Sales and Use Tax Agreement and a full member of the Streamlined Sales Tax Governing Board. Destination-based sourcing of taxable purchases is required under Section 310 of the Agreement. Also, the use tax (imposed on Ohio residents when they make remote purchases outside Ohio) may not be collected and remitted to Ohio if remote vendors (located in other states) choose not to apply destination-based sourcing for Ohio purchases because the state is not a member of the SSTA. Thus, Ohio may potentially forego the benefit of the SSTA and potential revenue gains from the taxation of certain remote sales.

The bill does not address whether local governments may be required to change their tax rates to conform to a potential statewide local rate. This may have a future fiscal impact on local governments, unless local governments are made whole under a redistribution of receipts from a statewide local sales and use tax rate.

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