# Ohio Legislative Service Commission

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# Fiscal Note & Local Impact Statement

**Bill**: S.B. 155 of the 128th G.A.

**Date**: September 22, 2009

**Status**: As Introduced

**Sponsor**: Sens. Carey and D. Miller

**Local Impact Statement Procedure Required**: No

**Contents**: To partially decouple Ohio law from recent federal income tax changes, to require the Department of Job and Family Services to operate the Disability Medical Assistance Program in the same manner the Program was operated as of June 30, 2009 and to make appropriations

## State Fiscal Highlights

| STATE FUND | FY 2010 | FY 2011 | FUTURE YEARS |
|---|---|---|---|
| **General Revenue Fund** | | | |
| Revenues | $17.3 million gain in federal reimbursement<br>Potential gain of $34.9 million from the partial decoupling from federal income tax law | $15.3 million gain in federal reimbursement<br>Potential gain of $9.8 million from the partial decoupling from federal income tax law | Potential loss of $44.7 million from the partial decoupling from the federal income tax law |
| Expenditures | $37.3 million increase | $35.3 million increase | - 0 - |

Note: The state fiscal year is July 1 through June 30. For example, FY 2010 is July 1, 2009 – June 30, 2010.

- The bill increases existing GRF appropriations by $37.3 million in FY 2010 and $35.3 million in FY 2011. The increase in spending will allow the state to receive $17.3 million in federal reimbursement in FY 2010 and $15.3 million in FY 2011.
- State income tax revenue is distributed primarily to the GRF (94.1%). The partial decoupling of Ohio income tax law from federal income tax law is estimated to yield GRF receipts of $34.9 million in FY 2010 and $9.8 million in FY 2011. Those potential gains will be reversed in future years.

## Local Fiscal Highlights

| LOCAL GOVERNMENT | FY 2010 | FY 2011 | FUTURE YEARS |
|---|---|---|---|
| **Counties, municipalities, townships, and public libraries** | | | |
| Revenues | Potential gain of $2.1 million | Potential gain of $0.6 million | Potential loss of $2.7 million |
| Expenditures | - 0 - | - 0 - | - 0 - |

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

- State income tax revenue is distributed to the Local Government Fund (LGF, 3.68%) and the Public Library Fund (PLF, 2.22%). The partial decoupling of Ohio income tax law from federal income tax law potentially increases state income tax revenues during the biennium, thus increasing distributions to the two local government funds. The reversal of state income tax gains in future years will also decrease receipts from the tax to the two local government funds.

# Detailed Fiscal Analysis

## Income Tax

Am. Sub. H.B. 1 (the operating budget act) expressly incorporated into Ohio's personal income tax law changes made to federal income tax law since December 30, 2008, and allowed a taxpayer whose taxable year ended after that date but before the effective date of the incorporated changes, to elect to apply federal law as it existed before that date. The American Recovery and Reinvestment Act of 2009 (ARRA) – the federal "stimulus" bill – was the principal federal act whose tax law changes were incorporated. The calculation of Ohio personal income tax begins with federal adjusted gross income (FAGI); thus, federal tax changes that modify gross income also have the potential to change Ohio income tax when Ohio law conforms to the federal tax changes. From the various provisions in ARRA, three had the potential to materially reduce Ohio income tax revenues: (1) the exclusion of up to $2,400 of unemployment insurance benefits from gross income for taxable year 2009, (2) the deferral of income from discharge of certain indebtedness, and (3) the extension of the carryback period from three to five years for taxpayers with 2008 gross receipts of $15 million or less. The bill reverses H.B. 1's treatment of the deferral of income from discharge of certain indebtedness, i.e., the bill restores such income to Ohio adjusted gross income, and it delays any refunds arising from the extended carryback period until July 1, 2011.

## Deferral of income from discharge of certain indebtedness

ARRA allowed a business to defer income if it reacquires its own debt at a discount in 2009 and 2010. Such income was to be recognized (included in income) in five successive taxable years beginning in 2015. This provision was expected to benefit a number of firms whose debt obligations degraded during the downturn in credit and real estate markets.[1] Because Ohio's corporate income tax has been eliminated, except for financial corporations, this provision would affect only those taxpayers that are pass-through entities, such as S-corporations, limited liability corporations, and partnerships. The bill requires such pass-through entities to recognize the income from discharge of debt for Ohio income tax purposes, instead of deferring that income as proposed in the federal income tax. Therefore, the bill accelerates the timing of future tax payments into the current biennium and the owners of the pass-through entities will forgo tax gains on their Ohio income tax in FYs 2010-2011 (if they choose to defer recognition of income in their federal income tax returns). The bill also specifies that, in future years, when the pass-through entities recognize the deferred income for federal

[1] Under existing federal law, if a business that has borrowed funds (issued debt) takes steps to buy back such debt at less than the issue price, the difference between the original price and the debt's current value becomes taxable income, and it is taxed during the year in which such reacquisition occurs. Under certain circumstances such as a bankrupt firm, income from discharged debt is not taxable.

tax purposes, they must subtract that income when determining Ohio adjusted gross income, which creates a corresponding revenue loss in future years.

### Extended carryback of 2008 net operating losses

Under current federal law, when most income taxpayers realize a net operating loss (NOL) during a given year, the loss may generally be deducted against positive income achieved during the two most recent prior taxable years, by filing amended returns for those years. This is described as an NOL "carryback." If a carryback does not eliminate the entire NOL, then the loss may be carried forward to be deducted in a future taxable year (not to exceed 20 years). Compared to an NOL carryforward, the NOL carryback deduction provides more immediate benefits to taxpayers and produces a tax refund (unless there are outstanding tax liabilities still owed on that year). ARRA extended the carryback period to five years for taxpayers with 2008 gross receipts of $15 million or less. Only those losses realized for the taxable year beginning or ending in 2008 were eligible for this extended carryback treatment. S.B. 155 defers until the next biennium the payment of any income tax refunds resulting from an election in federal taxes to apply a 2008 NOL against profits reported in the additional previous three taxable years. Thus, the bill potentially delays the potential income tax revenue loss from those refunds to FY 2012, at the earliest.

State income tax revenue is distributed to the General Revenue Fund (GRF, at 94.1%), the Local Government Fund (LGF, 3.68%), and the Public Library Fund (PLF, 2.22%). For FYs 2010-2011, distributions of tax revenues to the GRF are increased to 94.35% and those to the PLF are reduced to 1.97%. Table 1 provides estimated revenue gains from S.B. 155 to the GRF, the LGF, and the PLF in FYs 2010-2011. Note that these gains will be reversed in future years, starting in FY 2012 for the payment of refunds from the extended carryback period of NOLs. Revenue losses from the exclusion in Ohio tax returns of income included in federal income tax (from the deferral of certain indebtedness) are to start in FY 2015. Estimates are from the Department of Taxation.

**Table 1: Estimated Income Tax Revenue Gain from S.B. 155 (in millions)**

| | FY 2010 | | | FY 2011 | | |
|---|---|---|---|---|---|---|
| **Item** | **GRF** | **LGF** | **PLF** | **GRF** | **LGF** | **PLF** |
| Deferral of Income from Discharge of Debt | $20.0 | $0.8 | $0.4 | $12.8 | $0.5 | $0.3 |
| Extended Carryback of NOL | $14.9 | $0.6 | $0.3 | ($3.0) | ($0.1) | ($0.1) |
| **Total** | **$34.9** | **$1.4** | **$0.7** | **$9.8** | **$0.4** | **$0.2** |

### Disability Medical Assistance Program

The bill requires the Ohio Department of Job and Family Services (ODJFS) to operate the Disability Medical Assistance (DMA) Program in the same manner the program was operated as of June 30, 2009. The DMA Program provides a limited health care benefit package to non-Medicaid eligible individuals based on income, resources, and severity of disability. DMA is completely funded with state revenue. Expenditures for the DMA Program are not eligible for federal reimbursement because the recipients are either not Medicaid eligible or have not been determined to be Medicaid eligible. Although it is not part of Medicaid, DMA is funded out of GRF appropriation item 600525, Health Care/Medicaid. The program supports individuals while they are applying for long-term federal disability benefits. The benefit package is a limited version of the primary and acute-care services offered to consumers through Medicaid, and all services are received through the fee-for-service delivery system. Covered services includes certain inpatient and outpatient physician services, prescription drugs, certain medical supplies, certain laboratory and x-ray services, and dental extractions and related x-rays. Hospital services for this population are provided through the Hospital Care Assurance Program.

ODJFS froze enrollment beginning in July 2003. Under the freeze, ODJFS allowed no new enrollment and denied coverage to those who missed their eligibility redeterminations. Enrollment was open for a limited time early in FY 2005 and then closed again in order to keep costs within the $64 million GRF allocated to operate the program that year. In recent years, due to severe funding limitations, enrollment in DMA was closed to new enrollees. Consequently, the caseload has decreased from almost 28,000 individuals in FY 2003 to about 1,500 individuals in May 2009.

Am. Sub. H.B. 1 of the 128th General Assembly, the budget act, eliminates DMA.

## Appropriations

The bill increases GRF appropriations by $37.3 million in FY 2010 and $35.3 million in FY 2011. The total increase breaks down as follows:

- $6 million in each fiscal year in appropriation item 725502, Soil and Water Districts, in the Department of Natural Resources' budget;
- $6 million in each fiscal year in appropriation item 600525, Health Care/Medicaid, in ODJFS's budget; and
- $25.3 million ($8 million state share and $17.3 million federal share) in FY 2010 and $8 million state share and $15.3 million federal share in FY 2011 in appropriation item 600528, Adoption Services, in ODJFS's budget.

The state will receive $17.3 million in federal reimbursement in FY 2010 and $15.3 million in FY 2011 for expenditures on adoption services.

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