



# Ohio Legislative Service Commission

## Final Analysis

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**Reps.** Grossman and Henne, Amstutz, Beck, J. Adams, Blair, Brenner, Buchy, DeVitis, C. Hagan, Hood, Maag, Retherford, Roegner, Ruhl, Scherer, Sears, Terhar, Thompson, Young, Batchelder

**Sens.** Burke, Coley, Eklund, Faber, Jones, Jordan, Peterson, Schaffer, Seitz

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## ACT SUMMARY

### Imposition of new law and rules

- Requires municipal corporations levying an income tax as of January 1, 2016, and that intend to continue levying the tax thereafter to amend their existing income tax ordinances to include certain statements incorporating the act's limitations; amended ordinances continuing a pre-existing tax rate above 1% do not require further voter approval.
- Expressly allows a municipal corporation to offer a credit to residents for tax paid by residents to other municipal corporations, including tax paid by pass-through entities owned by the resident.
- Expressly prohibits municipal corporations and tax administrators from adopting rules to administer a municipal income tax that conflict with statutory limitations on the tax.

### Computation of taxable income

- Establishes a uniform tax base applicable to all municipal corporations levying an income tax (with a few exceptions) by further defining the forms of income that municipal corporations must tax and the forms that they may not tax.

- Specifically adds to the income tax base of individuals certain deferred compensation and stock option-related income unless grandfathered by local ordinance, and self-employment income of religious leaders.
- Specifically excludes from the tax base, in addition to the current mandatory exclusions: alimony and child support received; compensation for personal injuries or property damage (e.g., from insurance) except for punitive damages or lost wages; dues received by certain kinds of organizations; gains from involuntary conversions; interest on federal obligations; and nonbusiness income of a decedent's estate.
- Requires all municipal corporations to allow businesses to deduct new net operating losses and to allow a five-year carryforward of such losses, reducing the requirement for five years for certain municipal corporations; and permits pre-existing losses to continue to be carried forward if pre-existing ordinances allow.
- Modifies the pre-existing deduction for unreimbursed employee business expenses.

### **Residency and exemptions**

- Allows a municipal corporation to treat an individual as a resident for municipal income tax purposes only if the individual is domiciled there, and prescribes standards for determining an individual's domicile for municipal income tax purposes.
- Modifies the "casual" or "occasional" entrant exemption to increase the number of days, from 12 to 20 per year, that an individual may work in a municipal corporation without incurring income tax liability there, to define how such days are to be counted, and to further define how the exemption does not apply to professional athletes, entertainers, and public figures.
- Provides that the occasional entrant exemption does not apply to employees of businesses with less than \$500,000 in annual revenue, and instead creates a separate exemption that prohibits the taxation of income of such employees by any municipality other than the municipality where the business' fixed location is located or the municipality of residence.
- Grandfathers petroleum refinery employees under prior law's 12-day occasional entrant exemption from the employer withholding requirement.
- Allows an employee to receive a refund of taxes withheld under the occasional entrant or small business employer exemption on the basis that the employee did not actually perform services in the municipality for which the taxes were withheld.



## **Apportionment and allocation of net profit**

- Modifies and further specifies how the "sales" and "payroll" factors are to be computed in the formula used to apportion income for taxpayers that have income from both within and outside a municipal corporation.
- Authorizes taxpayers to use an alternative method of apportioning income and expressly allows tax administrators to require the use of an alternative method if the statutory formula does not fairly represent the extent of the taxpayer's business activity in a municipal corporation.
- Allows individuals with net profit from rental activity to elect to use separate accounting to calculate their net profit from rental activity.

## **Withholding taxes at source**

- Prescribes a uniform income tax employer withholding schedule for all municipal corporations that depends on recent withholding amounts.
- Expressly permits municipal corporations to require electronic remittance of withheld taxes if electronic remittance is required for federal income tax purposes.
- Expressly permits employers to withhold income tax for a municipal corporation where an employee resides if so requested by the employee.
- Modifies and clarifies the law governing municipal income tax withholding by casinos and video lottery terminal operators.

## **Tax filing and payment**

- Requires all municipal corporations levying an income tax to comply with a uniform annual tax return filing schedule, with some exceptions.
- Requires municipal corporations to allow any taxpayer subject to the tax on net profit to file a municipal income tax return extension by using the Ohio Business Gateway.
- Requires municipal corporations to grant income tax payment and filing extensions for active duty military personnel and civilian support personnel and persons who request a federal income tax extension.
- Requires municipal income taxpayers to file an amended return if adjustments to the taxpayer's federal income tax return affect the taxpayer's municipal income tax liability.



- Prescribes more specific rules for the filing of consolidated income tax returns by affiliated groups of corporations, including a requirement that such returns be prepared in the same manner as consolidated federal income tax returns.
- Requires taxpayers to report and pay estimated taxes if the estimated annual tax liability, after subtracting for amounts to be withheld from the taxpayer's compensation, will be more than \$200, unless the taxpayer is a member of an exempted class or the tax administrator waives the requirement.
- Prohibits a municipal corporation from penalizing a taxpayer for the underpayment of estimated taxes if the taxpayer has paid at least 90% of the amount due in the current year, while maintaining similar safe harbor for taxpayers who were not living in a municipality at the beginning of a year or who have made payments equal to 100% of the taxpayer's total tax liability for the previous year.
- Authorizes the Governor to appoint up to two additional municipal tax administrators to the Ohio Business Gateway Steering Committee selected from nominees of the Ohio Municipal League.

### **Refunds and assessments of liability**

- Provides that a municipal income taxpayer may receive a refund of overpaid taxes only if the amount overpaid is more than \$10.
- Requires tax administrators to either approve a request for a tax refund or deny the request in writing, but retains the authority of the tax administrator to require taxpayers to substantiate refund claims.
- Establishes procedures for the issuance of assessments against taxpayers who allegedly fail to pay municipal income tax or file a return.
- Specifies the manner by which assessments may be appealed.
- Prohibits civil actions to collect municipal income taxes after three years or, if an appeal was made, one year and 60 days after the appeal is finalized and all opportunities for further appeal are exhausted or expired.
- Limits the amount of penalties and interest that may be charged for the failure to file returns or pay taxes on time.
- Renames boards of appeal "local boards of tax review."
- Extends the deadlines for filing an appeal to a local board of tax review and for the board to schedule a hearing.



- Requires hearings of a local board of tax review to be completed within 120 days.
- Prescribes the membership of local boards of tax review and revises the procedural and notice requirements that apply to the boards.

### **Tax administration, collection, and enforcement**

- Prescribes how and under what circumstances a tax administrator may compromise a claim or agree to a pay-over-time arrangement to, for example, provide relief to an innocent spouse.
- Requires a municipal corporation to deliver assessments to taxpayers in accordance with requirements similar to those applicable to the delivery of state income tax notices.
- Prescribes municipal income tax audit procedures, limitations on the conduct of audits, and rights and remedies available to taxpayers subject to an audit.
- Requires municipal income taxpayers to retain tax-related records for six years, authorizes municipal tax administrators to require taxpayers to retain the records beyond that six-year period, and allows taxpayers to destroy the records sooner upon written consent of the tax administrator.
- Prohibits a tax administrator from engaging an agent on a contingency basis to inspect a person's records, and requires agents to display credentials upon request.
- Permits municipal income taxpayers to request official opinions from tax administrators regarding prospective tax liability, specifies procedures for the issuance of such opinions, and states the extent to which they are binding.
- Requires a person to notify a tax administrator of any change to the person's personal identifying information, such as a Social Security number, if the tax administrator requires a person to submit such information.
- Requires tax administrators to take necessary steps to protect taxpayers' Social Security numbers and prohibits the display of a Social Security number on the outside of a mailed envelope.
- Modifies existing protections for confidential municipal income tax information to prohibit anyone from accessing the information without a proper judicial order and outside the scope of official business.
- Prescribes minimum penalties for any person who unlawfully accesses or discloses confidential municipal income tax information.



- Authorizes the exchange of confidential municipal income tax information among tax administrators.
- Imposes a uniform standard of justiciability on actions for municipal income tax-related damages brought by taxpayers against municipal corporations or tax administrators.
- Specifies that the proper measure of damages available to taxpayers in such actions is compensatory damages along with reasonable costs of litigation and attorneys' fees.
- Permits courts of common pleas to impose a penalty of up to \$10,000 on a taxpayer who brings a frivolous action against a tax administrator or a municipal corporation.
- Prohibits knowing involvement with false or fraudulent tax documents submitted to a tax administrator or with records upon which such documents are based with intent to defraud a municipal corporation or a tax administrator.

### **Other provisions**

- Revises the required contents of the annual report of municipal income tax revenues to the Tax Commissioner.
- Specifies that, if a portion of the revenue from a municipal income tax levy will be shared with a school district, the levy may not take effect until the year following the year in which voters approved the levy.
- Creates a 13-member temporary committee to quantify and recommend ameliorations for the potential fiscal impact to municipal corporations of requiring each to allow net operating losses to be carried forward for five years.
- Creates a 12-member temporary committee to study the feasibility of requiring municipal corporations to separately report income tax revenue paid by resident and nonresident individuals.

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## CONTENT AND OPERATION

### Background

Municipal corporations' authority to levy taxes is an aspect of their home rule powers conferred by Article XVIII, Section 3, Ohio Constitution.<sup>1</sup> Although the General Assembly does not grant municipal corporations the authority to tax, it may limit their taxing authority or prohibit municipal taxes by express acts; however, it cannot command a municipal corporation to impose a tax when the municipal corporation chooses not to do so.<sup>2</sup> The limits on municipal income taxes are codified in Chapter 718.

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<sup>1</sup> See *Zielonka v. Carrel*, 99 Ohio St. 220 (1919), and *Cincinnati Bell Tel. Co. v. City of Cincinnati*, 81 Ohio St.3d 599 (1998).

<sup>2</sup> Article XIII, Section 6 and Article XVIII, Section 13, Ohio Constitution; *City of Franklin v. Harrison*, 171 Ohio St. 329 (1960), *Gesler v. Worthington Income Tax Bd. of Appeals*, 138 Ohio St.3d 76 (2013), and *Cincinnati Bell Tel. Co., supra*.





of the Revised Code. The act modifies many of the limits previously codified in that chapter and imposes new limits and procedures.

The effects of the act's changes will vary among municipal corporations to the extent that a municipal corporation's ordinances are not in compliance with the act's new or modified limitations.<sup>3</sup> Some municipal ordinances may already comply with the act's provisions to some degree.

### **Amendment of pre-existing tax ordinances**

Beginning on January 1, 2016, every municipal income tax levied in the state must comply with the limitations specified in the act.<sup>4</sup> Municipal corporations are prohibited from enforcing any ordinance that conflicts with the law as amended by the act.<sup>5</sup> The act requires all income tax ordinances to specify that the tax is levied on the municipal taxable income of every person residing or earning income in the municipal corporation. As under prior law, the municipal corporation must levy the tax at a uniform rate and, similar to prior law, may offer a credit to residents who earn income in another municipality. The credit, if offered, may apply to tax paid by the resident to other municipal corporations and, additionally, to tax paid by a pass-through entity owned by the resident, on the resident's share of the entity's income. The income tax ordinance must specify whether, and to what extent, such a credit is allowed.

Although continuing law requires that voters approve any new income tax levied at a rate above 1%, the act allows a municipal corporation that levied a tax above that rate before January 1, 2016, to continue to levy its tax at the voter-approved rate without an additional vote.<sup>6</sup>

The act's changes apply to joint economic development districts (JEDDs) and zones (JEDZs) in which a municipal income tax is levied.<sup>7</sup>

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<sup>3</sup> Throughout this analysis, references to ordinances include resolutions if resolutions are the form by which a municipal legislative authority adopts its laws.

<sup>4</sup> R.C. 718.04 and Section 6.

<sup>5</sup> R.C. 718.04(F) of the act; Section 6. The act also applies these provisions to "withholding taxes," which, although not defined for this purpose, presumably refers to the imposition of tax withholding obligations on employers, casinos, video lottery terminal operators, and other persons that are required to withhold municipal income taxes owed by a taxpayer and remit those taxes to the municipal corporation as a trustee of a municipal corporation.

<sup>6</sup> R.C. 718.04.

<sup>7</sup> R.C. 718.01(AA).



## Municipal rule-making authority

The act expressly prohibits a municipal legislative authority or tax administrator from adopting any rule to administer its municipal income tax that is inconsistent with limitations contained in state law.<sup>8</sup>

## Taxable income

The act establishes uniform definitions of taxable income that must be adopted by all municipal corporations that intend to continue levying an income tax after 2015. For individuals, the tax base includes compensation, net profit from business activities minus net operating loss carryforward, and prizes and winnings from lotteries, gambling, and similar activities.<sup>9</sup> A nonresident individual's compensation is included in the base only if earned for work in the taxing municipal corporation, and a nonresident's net profit is included only to the extent it is assignable to the taxing municipal corporation under the act's apportionment and allocation provisions (described below).

For corporations, pass-through entities such as partnerships, S corporations, and limited liability companies (LLCs), and other business entities, the tax base is net profit, which equals federal taxable income after several adjustments (described below) and after apportionment and allocation.<sup>10</sup> The act's taxation of the net profits of all pass-through entities contrasts with the taxation of pass-through entities under prior law. Under prior law, municipal corporations could tax pass-through entity net profits at either the entity level or the owner level (but not both). And, the municipal corporation could make that choice separately for each class of entity (e.g., tax partnerships and LLCs at the partner or member level, and tax S corporations at the entity level).<sup>11</sup>

In the case of all taxpayers, certain forms of income must be exempted, as described below.

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<sup>8</sup> R.C. 718.30.

<sup>9</sup> R.C. 718.01(B).

<sup>10</sup> The act specifically excludes trusts, estates, and grantors of grantor trusts from its definition of "pass-through entity." (Under federal income tax law's grantor trust rules, a person, usually the grantor of the trust, is treated as the direct owner of the trust's assets, and therefore must include the trust's income items in that person's own taxable income, if that person or a nonadverse party has unrestricted power to dispose of the trust's assets. See I.R.C. secs. 671 to 679.)

<sup>11</sup> R.C. 718.14(D) of prior law, repealed by the act.



The following table summarizes the tax base for individuals and for business entities. The components of the base and the determination of taxable income are described after the table.

<b>H.B. 5 Income Tax Base</b>	
Resident individuals	<p>--Compensation from any source unless specifically exempted by the act</p> <p>--Net profit, including distributive shares of pass-through entity net profit (except for S corporations, unless allowed under a grandfathered ordinance), from Form 1040 Schedule C, E, or F, minus net operating loss carryforward</p> <p>--Lottery, gambling, prizes, and similar winnings (minus wagering losses for professional gamblers)</p> <p>--Alternatively, certain municipal corporations may use Ohio adjusted gross income minus amounts exempted by the municipal corporation and plus deductions excluded, if the municipal corporation adopted that tax base before 2014. The "qualified" municipal corporation may exempt income earned by nonresident individuals and the net profits of persons not wholly located within the qualified municipal corporation from the tax and corresponding withholding obligations</p>
Nonresident individuals	<p>--Compensation for work in the taxing municipal corporation unless specifically exempted</p> <p>--Net profit (as defined for resident individuals) after apportionment and allocation (not including the nonresident's distributive shares of any pass-through entity net profit)</p> <p>--Lottery, gambling, prizes, and similar winnings (minus wagering losses for professional gamblers)</p>
Corporations, pass-through entities, and other business organizations	<p>--Net profit (adjusted federal taxable income as defined by the act) after apportionment and allocation</p>

### **Compensation**

Compensation, although not defined by the act, includes "qualifying wages" and salaries, commissions, and "other" compensation. In effect, if compensation is received by an employee, it is taxable only if it is included in "qualifying wages" because any employee compensation not included in qualifying wages is tax-exempt under both the act and prior law.



## Qualifying wages

Qualifying wages closely approximates the Medicare ("FICA") tax withholding base (i.e., IRS Form W-2, Box 5) with several adjustments. In comparison to the compensation subject to state and federal income taxes, it is broader, including such items as employee contributions to 401(k) plans and some other qualified retirement or deferred compensation plans, salary-reduction contributions to some other retirement plans, and severance pay.<sup>12</sup>

The act makes several changes to the qualifying wage base.<sup>13</sup> Under both the act and prior law, nonqualified deferred compensation or employee stock option-related compensation is subtracted from the Medicare wage base if the municipal ordinance permits. But, under the act, the deduction of such nonqualified deferred compensation and stock option-related compensation will be permissible after 2015 only if allowed by ordinance adopted before 2016. If a municipal corporation does not exempt employee stock option income by ordinance before 2016, taxpayers must add the ordinary income component of that income (i.e., noncapital gain) to the Medicare wage base in computing qualifying wages. This addition was also required by prior law, but with no time limit on the adoption of an ordinance exempting such income.<sup>14</sup>

The act also requires religious leaders to add amounts they receive for religious duties that are considered net earnings from self-employment for federal income tax purposes (under I.R.C. sec. 1402). Prior law did not require such an addition, but a municipal corporation could have required the addition by ordinance.

Under prior law, payments on account of sickness or accident disability were subtracted from the Medicare wage base to compute qualifying wages. The act retains this deduction but modifies it to cover "payments on account of a disability related to sickness or an accident" and only if the payment is made by someone unrelated to the employer.

Under continuing law, employee contributions and deferrals to 401(k) retirement and 457 deferred compensation plan accounts are added to the extent not included in the Medicare wage base. The act additionally requires employee contributions to a 403(b) plan to be added, which is a retirement plan available for public education organizations, some nonprofit employers, cooperative hospital service organizations,

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<sup>12</sup> Internal Revenue Code sec. 3121(a).

<sup>13</sup> R.C. 718.01(R) of the act; R.C. 718.03 of prior law.

<sup>14</sup> R.C. 718.01(R).



and self-employed ministers.<sup>15</sup> The act requires a taxpayer to add any employee compensation not otherwise included in the Medicare wage base that is nevertheless included in the taxpayer's gross income for federal income tax purposes, that did not or will not constitute Medicare wages for any previous or succeeding taxable year, and that has not otherwise been added to qualifying wages.

Otherwise, the act retains prior law's adjustments to the Medicare wage base. Cash or noncash compensation under a cafeteria plan must be subtracted. Supplemental unemployment benefits and compensation received by pre-April 1986 hires must be added to the extent not included in the Medicare wage base. (Many state and local government employees hired before April 1986 are not subject to the Medicare hospital insurance tax, so their pay is excluded from the Medicare wage base for federal Medicare tax purposes.)

### **Net profit**

Net profit is the basis for taxing business income, and the act defines net profit for business organizations and for individuals. For business organizations, the act's definition of net profit is the same as under prior law, except that municipal corporations are required to permit taxpayers to deduct and carry forward net operating losses (NOLs) for five years, as described below, and deduct or add the net profit or loss, respectively, of any pass-through entity included in the taxpayer's adjusted gross income unless the taxpayer includes the pass-through entity as part of the taxpayer's affiliated group filing a consolidated corporate return (see below).<sup>16</sup> The definition applies to "C" corporations (i.e., corporations not making the federal "S" election for pass-through tax treatment) and to partnerships, S corporations, LLCs, and other pass-through entities other than those entities that are disregarded as a separate taxpayer for federal tax purposes. In the case of pass-through entities, they must compute net profit as if they were a C corporation, except they are not allowed to deduct guaranteed payments and similar amounts paid or accrued to an owner or former owner or to deduct payments or accruals to a qualified self-employed retirement plan, health insurance plan, or life insurance plan for owners or owner-employees (however, this exception does not prohibit a partnership from deducting guaranteed payments to partners for the use of capital treated as the payment of interest under federal law).

For individuals who have net profit from a trade, profession, or business, net profit is defined as the profit required to be reported for federal income tax purposes on

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<sup>15</sup> Internal Revenue Code 403(b).

<sup>16</sup> R.C. 718.01(D)(1) and (E) of the act; R.C. 718.01(A)(7) and (D)(2) of prior law.



the Form 1040 Schedule C (sole proprietor profit and loss), Schedule E (supplemental income from pass-through entities, rental, royalties, etc.), and Schedule F (farming profit and loss), as under prior law.<sup>17</sup> But unlike prior law, the act requires NOL deductions and carryforwards (as described below), allows professional gamblers who report winnings as business income to deduct the gambler's wagering losses, and eliminates former local option deductions for health savings account contributions and for sole proprietors' family health insurance premiums.

### **Residents' net operating loss offset**

The act also contains provisions specific to the taxation of the net profit of resident individuals. For resident individuals, the act authorizes any NOL shown on a taxpayer's federal tax return from an investment as a partner in a pass-through entity to be deducted against any other of the resident's net profit reported on Schedule C, E, or F in the same taxable year and the five ensuing years. Similarly, any NOL incurred by the resident may be deducted from any profits earned by a pass-through entity in which the resident is a partner in the same taxable year and the five ensuing years. This offset is not available to nonresident individuals, whose net profit from a distributive share in a pass-through entity is taxed only at the entity level. The offset is not allowed with respect to a resident's share of the profit or loss of an S corporation if the municipal corporation is not authorized to tax the resident's shares thereof. To prevent the same NOLs from being deducted by a resident individual twice, the act disallows NOLs used to offset residents' net profit from also being carried forward for use in future taxable years, as described below. Additionally, to prevent the same NOLs from being deducted by both a pass-through entity and a resident individual, the act requires residents to report their distributive share of pass-through entity net profit by disregarding NOLs carried forward from a preceding taxable year and used by the entity to reduce its net profit for the current year. (As described above, a pass-through entity is subject to taxation on the basis of the entity's net profit.)<sup>18</sup>

### **Net operating losses**

Generally, the act requires all municipal corporations to permit taxpayers to deduct net operating losses (NOLs) and to carry excess NOLs forward for deduction for five subsequent years.<sup>19</sup> Under prior law, municipal corporations could allow NOL

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<sup>17</sup> R.C. 718.01(D)(2) of the act; R.C. 718.01(A)(7), (E)(2) and (3), and (H)(9) of prior law.

<sup>18</sup> R.C. 718.01(B)(1)(a), (b), (c), and (d).

<sup>19</sup> R.C. 718.01(E)(8).



deductions and carryforwards but were not required to; if they allowed carryforwards, the maximum carryforward period was set by ordinance.<sup>20</sup>

For municipal corporations levying a tax before 2016, the act's new five-year carryforward rule applies only to NOLs incurred in taxable years beginning after 2016. For NOLs incurred earlier, an NOL deduction and carryforward is allowed only if an ordinance adopted before 2017 permits the deduction and carryforward. The carryforward may continue for as many years as allowed by the pre-existing ordinance. If a taxpayer is allowed to deduct carryforwards under such an ordinance, the deduction must be taken before deductions for NOLs incurred in taxable years beginning after 2016. For municipal corporations that levy an income tax for the first time in or after 2016, the act's five-year carryforward rule applies to NOLs incurred in taxable years beginning on or after the effective date of the tax.

For the purposes of the act's NOL deduction, NOL does not include loss resulting from basis, at-risk, or passive activity loss limitations, which are generally losses that cannot be deducted from adjusted gross income in a given taxable year because of certain limitations imposed by federal law.<sup>21</sup>

#### **Reduced NOL deduction for first five years**

For municipal corporations levying a tax before 2016, the amount of NOLs incurred in taxable years beginning after 2016 that may be deducted and carried forward is reduced for taxable years beginning in 2018 to 2022 – the first five years to which the five-year carryforward applies. The NOL deduction (including carryforwards) for taxable years beginning in each of those years cannot exceed 50% of the full amount otherwise allowed. For taxable years beginning after 2023, the full deduction is allowed. The temporary 50% limit does not apply to NOLs incurred in taxable years beginning before 2017 and deductible under a pre-2016 ordinance. A taxpayer may carry forward NOL the taxpayer was precluded from deducting or carrying forward because of the 50% limit for taxable years beginning after 2023, but for no more than five years.<sup>22</sup>

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<sup>20</sup> R.C. 718.01(K) of prior law.

<sup>21</sup> R.C. 718.01(GG).

<sup>22</sup> R.C. 718.01(E)(8)(c) and (e).





## Exempt income

The act adds certain forms of income to those that are already exempted under continuing law from municipal income taxes and employer withholding.<sup>23</sup> The act also eliminates an exemption allowed under prior law for transit employees' occasional passage through a municipal corporation.

The following table shows the forms of income that must be exempted from all municipal corporations' income taxes under prior law and under the act. In addition to being exempt from municipal income tax, exempt income is subtracted from qualifying wages, thereby reducing the wage withholding base by the amount of exempt income.<sup>24</sup> And the act specifies that exempt income in the hands of an individual is exempt income in the hands of a pass-through entity.<sup>25</sup>

<b>Forms of Tax-exempt Income</b>		
<b>Form of income</b>	<b>Prior law</b>	<b>H.B. 5</b>
Employee compensation that is not "qualifying wages"	Exempt	Exempt
Intangible income	Exempt except in a few grandfathered municipal corporations	Exempt except in those grandfathered municipal corporations
Military pay	Exempt	Exempt
Social Security benefits, retirement benefits, pensions, disability benefits, unemployment compensation, sickness, accident, or liability insurance proceeds	Not specifically exempt, but could be exempted under local ordinance	Exempt
Alimony and child support	Not specifically exempt, but could be exempted under local ordinance	Exempt
Parsonage allowance	Exempt	Exempt
Precinct election officials' pay	Exempt up to \$1,000 annually	Exempt up to \$1,000 annually

<sup>23</sup> R.C. 718.01(C) of the act.

<sup>24</sup> R.C. 718.01(R).

<sup>25</sup> R.C. 718.01(C).





<b>Forms of Tax-exempt Income</b>		
<b>Form of income</b>	<b>Prior law</b>	<b>H.B. 5</b>
Transit employees' pay for occasional passage	Exempt	Not specifically exempt, but potentially exempted under new occasional entrant exemption
Personal injury or property damage compensation	Not specifically exempt, but could be exempted under local ordinance	Exempt unless compensating for lost wages or punitive damages
Wages of nonresidents employed at Air Force base (Wright-Patterson)	Exempt	Exempt
S corporation shareholders' net profits	Exempt unless grandfathered by local election	Exempt except in those grandfathered municipal corporations
Public utilities' income	For-profit electricity and telephone companies may be taxed, other utilities are exempt	Same as prior law
Religious, educational, charitable, scientific, fraternal, and literary institutions' income	Exempt if derived from tax-exempt property or tax-exempt activities	Same as prior law
Dues and contributions received by labor unions, lodges, or religious, educational, charitable, fraternal, or literary institutions	Not specifically exempt, but could be exempted under local ordinance	Exempt
Estate income	Not specifically exempt, but could be exempted under local ordinance	Exempt unless trade or business income
Gains from involuntary conversions, interest on federal bonds, and state-taxable income exempted by law from municipal taxes	Not specifically exempt, but could be exempted under local ordinance	Exempt
Compensation for working at site owned by political subdivision added to municipal corporation by expedited type II annexation	Exempt	Exempt
Income of minors	Not specifically exempt, but could be exempted under local ordinance	Exempted to the extent, if any, allowed under an ordinance adopted before 2016



<b>Forms of Tax-exempt Income</b>		
<b>Form of income</b>	<b>Prior law</b>	<b>H.B. 5</b>
Nonwage compensation earned in a nonresident municipality	Exempt if services are performed for 12 or fewer days in a calendar year (see, " <b>Occasional entrant exemption</b> ," below)	Generally, exempt if services are performed for 20 or fewer days in a taxable year
Compensation paid to (1) a member or employee of the General Assembly for services as such a member or employee or (2) a judge sitting by assignment of the Chief Justice or an appeals court justice serving in multiple locations for their judicial services	Exempt from taxes imposed by any municipal corporation other than the one, if any, where the member, employee, or judge resides	Same as prior law
Compensation paid to Supreme Court justices for their judicial services	Exempt from taxes imposed by any municipal corporation other than Columbus and the one, if any, where the justice resides	Same as prior law

### **Employee business expense deduction**

The act modifies a pre-existing requirement that municipal corporations permit individuals to deduct unreimbursed employee business expenses that the individual deducted for federal income tax purposes (e.g., for business vehicle use, travel, meals, and entertainment). Previously, all municipal corporations were required to allow individuals to deduct such expenses at least to the extent reported on IRS Form 2106 and deducted for federal income tax purposes.<sup>26</sup>

The act requires all municipal corporations to allow individuals to deduct the amount of the individual's Form 2106 expenses that the individual deducted for federal income tax purposes, subject to the limitation imposed by the Internal Revenue Code that limits a taxpayer's ability to deduct miscellaneous itemized deductions, including Form 2106 expenses, for any taxable year to the extent that the aggregate of those deductions exceeds 2% of the individual's adjusted gross income. A taxpayer may deduct all such expenses for the individual's municipal corporation of residence but may deduct those expenses for a nonresident municipal corporation only to the extent

<sup>26</sup> R.C. 718.01(A)(4) and (F) of prior law.



the expenses are related to the taxpayer's performance of personal services in that municipal corporation.<sup>27</sup>

## Residency

The act permits municipal corporations to treat an individual as a resident for municipal income tax purposes only if the individual is domiciled in the municipal corporation under standards outlined in the act. An individual is presumed to be domiciled in a municipal corporation if a tax administrator reasonably concludes that the individual is domiciled in that municipality or if the individual was domiciled in the municipality on the last day of the preceding taxable year. The individual may rebut this presumption by showing by a preponderance of the evidence that he or she was not domiciled in the municipality.

The act sets forth 25 factors that may be used in determining, or rebutting the presumption of, an individual's domicile. The act's factors consider the location of the following:

- (1) Financial institutions used by the individual or individual's spouse;
- (2) Issuers of credit cards or installment loans to the individual or spouse;
- (3) Institutional lenders that loaned money to the individual or spouse;
- (4) Investment facilities and advisors used by the individual or spouse;
- (5) Insurance companies or agents that sold a policy to the individual or spouse;
- (6) Attorneys or accountants used by the individual or spouse;
- (7) Health care professionals used by the individual or spouse;
- (8) Charitable organizations to which the individual or spouse donates or for which the individual or spouse serves on the board of directors;
- (9) Burial plots owned by the individual or spouse;
- (10) Business ventures or entities of which the individual or spouse owns over 25% or over which the individual exercises significant control;
- (11) A recitation in an estate planning document such as a will;

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<sup>27</sup> R.C. 718.01(A)(2).

(12) The individual's friends, dependents, family members, and divorced or separated spouse;

(13) Educational institutions attended by the individual's dependents, provided a dependent's tuition is based on the residency of the individual or spouse in the municipality where the institution is located;

(14) Fiduciaries named in the individual's or spouse's estate planning documents;

(15) Businesses at which the individual or spouse shop;

(16) The individual's marriage;

(17) Recipients of political contributions made by the individual or spouse;

(18) Any "contact periods" the individual has with a municipality (contact periods are determined similarly to how they are determined for determining residency for the state income tax – an individual has a contact period with a municipality if the individual is away overnight from the individual's home located outside of the municipal corporation and while away overnight spends at least some portion of each of two consecutive days in the municipal corporation);

(19) The individual's domicile in past taxable years;

(20) Where the individual is registered to vote;

(21) The address on the individual's driver's license;

(22) Real estate for which the individual claims a tax benefit on the basis of the individual's residence;

(23) Homes owned or leased by the individual;

(24) Where the individual declares to be the individual's residency; and

(25) Where the individual is primarily employed.

No factor other than these 25 may be used in determining, or rebutting the presumption of, an individual's domicile.<sup>28</sup>

Under the act, municipal residency determines the extent to which income is included in an individual's taxable income base (described above in the "**Taxable**

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<sup>28</sup> R.C. 718.01(J) and 718.012.

**income**" section), whether an individual qualifies for any credit given for income taxes paid to another municipal corporation on the same income, and, in certain cases, whether an individual is subject to taxation by a municipal corporation.

Prior law did not address qualifications for municipal income tax residency. Residency was determined under municipal ordinances, many of which employ common law determinations of domicile depending on various indications of where a person intends to stay (e.g., maintaining a home, voting records, motor vehicle registration), similar to or the same as those prescribed by the act.

## **Occasional entrant exemption**

### **Prior law**

Under prior law, the "occasional entrant rule" prohibited a municipal corporation from taxing the compensation paid to a nonresident individual who worked in the municipal corporation for 12 days or fewer in a year, or from requiring employers to withhold taxes against such individuals' wages.<sup>29</sup> This exclusion did not apply if (1) the individual's employer had its principal place of business in another municipal corporation that imposed an income tax and (2) that other municipal corporation would not tax the compensation earned on those 12 or fewer days. Another exception, largely retained by the act, excluded professional entertainers, professional athletes, or promoters of professional entertainment or sports events and their employees, as reasonably defined by a municipal corporation, from the rule's operation.

### **Changes to the occasional entrant rule**

The act makes several changes to the casual occasional rule.<sup>30</sup> First, for employees of larger businesses and individuals receiving nonwage compensation, the act expands the exemption by increasing the number of days a nonresident may work in a municipal corporation without incurring liability for the municipal corporation's income tax, from 12 to 20 in a calendar year. Second, for nonresident employees of smaller businesses, the act creates a new rule that prohibits the taxation of the employee's income by any municipality other than the municipality where the business' fixed location is located. Third, the act creates two exceptions to both of these provisions: one for workers at petroleum refineries, and one that allows any employee to receive a refund of taxes on the basis that the employee did not actually perform services in the municipality for which the taxes were withheld.

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<sup>29</sup> R.C. 718.011 of prior law.

<sup>30</sup> R.C. 718.01(C)(16) and (17) and 718.011 of the act.



## **Extension of occasional entrant rule for certain employees and individuals**

For employees of businesses with annual revenue of \$500,000 or more and individuals receiving compensation other than "qualifying wages," the act increases the occasional entrant exemption period from 12 to 20 days.

### **Qualifying wages**

The new 20-day rule applies with respect to qualifying wages paid to employees of large businesses only if: (1) the employee's "principal place of work" is not located within the municipal corporation where the employee worked on the 20 or fewer days, (2) the employee is not providing services at a "presumed work location," (3) the employer does not withhold taxes on the compensation for the municipal corporation where the employee worked on the 20 or fewer days, but instead only for the municipal corporation where the employee's principal workplace is located, and (4) the employee does not request a refund of the taxes withheld to the municipal corporation where the employee's principal workplace is located. A "presumed worksite location" is a temporary worksite at which the employer provides services that can reasonably be expected (based on the nature of the services or the terms of an agreement with a customer) to last more than 20 days in a calendar year.

In general, an employee's "principal place of work" is the location in Ohio to which the employee reports for work duties on a regular and ordinary basis. The location may be a permanent location, such as an office or warehouse, or, if the employee does not regularly report to a permanent location, a temporary location that is not also the employee's home. If the employee does not report to one location on a regular and ordinary basis, the employee's "principal place of work" is the location where the employee spends the greatest number of days in a calendar year.

An employee has more than one "principal place of work" if, in the process of determining the municipal corporation in which they spent the greatest number of days, the employee calculates an identical number of days in two or more municipal corporations and that number is greater than the number of days spent in any other municipal corporation. In the case of an employee with more than one "principal place of work," the employee is required to allocate wages among the two or more municipal corporations where the employee spent the greatest number of days by a "fair and reasonable method" (e.g., equal allocation among the municipal corporations, allocation based on time spent, or allocation based on sales made).

Under the act, if a nonresident employee works in a municipal corporation for more than 20 days in a year, the employer may choose to withhold taxes for the first 20 days only for the municipal corporation where the employee's principal workplace is located or to both that municipality and the one where the work was performed. If the



employer withholds taxes for both municipalities, the employee's compensation is taxable in both municipalities. However, as discussed below, the employee may seek a refund of the taxes withheld for the municipality where the employee's principal workplace is located.

### **Other compensation**

The 20-day rule applies with respect to individuals receiving nonwage compensation only if the individual's "base of operation" is not located within the municipal corporation where the individual worked on the 20 or fewer days. In general, an individual's "base of operation" is an office, storefront, or similar facility to which the individual regularly reports and performs services for compensation. Nonwage compensation exempted under the occasional entrant rule is treated as earned or received at the individual's base of operation.

### **Small business employer rule**

The act requires employers with under \$500,000 in annual revenue to withhold and remit taxes on all nonresident employee compensation only to the municipal corporation in which the employer has its sole fixed location. This rule applies regardless of the number of days that an employee works in other municipalities in a year. However, as discussed below, an employee that works in other municipalities may receive a refund of taxes withheld on compensation paid for work performed in the other municipalities.

With respect to both the small business employer rule and the 20-day rule, a business' annual revenue includes any receipts received by the business during the prior taxable year. A tax administrator may require a small business employer to submit its prior year federal income tax return to establish eligibility under the small business employer rule.

### **Employee refunds**

If a nonresident individual's employer withholds taxes under the 20-day rule for the municipal corporation in which the individual's principal workplace is located, the individual may receive a refund of those taxes on the basis that the employee did not work in that municipality. Similarly, if a small business employer withholds taxes for a nonresident employee for the municipal corporation in which the employer has its fixed location, the employee may receive a refund of those taxes to the extent that the taxes were withheld on compensation earned for work performed in a different municipality. If an employee receives a refund in either case, the compensation upon which the refund is based becomes taxable in the municipality in which the work was performed.





## **Allocation of employee time**

The act introduces a test for determining when an employee has spent a "day" within a municipal corporation. Prior law did not provide guidance for making this determination. Under the act's test, an employee spends a day in a municipality only if, on that day, the employee spent more time working in that municipality than in any other municipality. Consequently, for purposes of the occasional entrant rule, an employee may work a "day" in no more than one municipality.

This test is also applied to determine when an employee has worked, or reported to, a particular location for purposes of assigning the employee's "principal place of work" (which may or may not be within a municipal corporation). The act further specifies that time spent performing certain activities is considered time spent at an employee's principal place of work. Those activities include time spent doing any of the following: traveling to work at the beginning of a day, traveling from work at the end of a day, traveling to pick up or load the employer's products, transporting or delivering those products (unless the product is then affixed to real estate owned, used, or controlled by a person other than the employer), and traveling from an employee's final delivery drop-off or pick-up location at the end of a day.

## **Petroleum refinery employees**

Qualifying wages paid to individuals working at a petroleum refinery must continue to be withheld according to prior law's 12-day rule. Employers are required to withhold taxes from such an employee only if the employee works at the refinery for 12 or more days in a calendar year. If an employee does work at the refinery for more than 12 days in a year, taxes must be withheld from wages paid for the first 12 days and every day thereafter.<sup>31</sup>

## **Application of rule to athletes, entertainers, and public figures**

Continuing law provides that the occasional entrant exclusion does not apply to professional athletes and entertainers. However, whereas prior law allowed municipal corporations to define who fits within these categories, the act provides more specific definitions for both. A professional athlete is a person who is paid to perform services in a professional athletic event. A professional entertainer is a person who is paid on a per-event basis to perform services in the professional performing arts.

The act adds "public figures" as a category of people whose compensation cannot be exempt from taxation under the occasional entrant rule. Under the act, a "public

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<sup>31</sup> R.C. 718.011(G) of the act.





figure" is a person of prominence who is paid on a per-event basis to perform services such as making speeches or public appearances.

The act applies the occasional entrant rule to promoters of professional sports and entertainment events and their employees, whereas under prior law such promoters and their employees were, like professional athletes and entertainers, not covered by the rule.

### **Employer agreements**

The act expressly allows a tax administrator and an employer to enter an agreement authorizing the employer to withhold taxes for occasional entrant employee compensation in a manner other than that required by the act.

### **Taxation of disregarded entities**

The act specifies that entities that are disregarded for federal income tax purposes ("disregarded entities"), including limited liability companies (LLCs) that have a single member (i.e., only one direct owner), may not be taxed at the entity level on their net profits. The net profits are taxable only to the direct owner of the entity.<sup>32</sup> Under federal income tax law, a disregarded entity is treated as the same taxpayer as its owner (i.e., the entity is disregarded as a separate taxpayer) unless the entity elects to be treated as a corporation for income tax purposes. The disregarded entity treatment generally means the owner reports the income items of the entity as the owner's own items (for individuals, this would be on Schedules C, E, and F).

Under continuing law, single member LLCs that are "disregarded entities" for federal tax purposes may be treated as separate from their single members for municipal income tax purposes if the single member is also an LLC and they satisfied certain conditions and made an election before 2005.<sup>33</sup>

### **Apportionment and allocation of net profit**

A business whose operations are not confined to one municipal corporation must apportion or allocate its net profit for income tax purposes. A three-factor formula based on a business' payroll, sales, and property is used to determine the portion of the business' net profit attributable to a municipality. The act makes several changes to this formula and to other rules governing the apportionment and allocation of net profits.<sup>34</sup>

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<sup>32</sup> R.C. 718.01(D)(3) of the act.

<sup>33</sup> R.C. 718.01(L) of the act and prior law.

<sup>34</sup> R.C. 718.02.

## Modification of three-factor formula

### Payroll factor

The "payroll factor" compares the compensation a business pays to its employees for services performed within a municipal corporation to the total compensation paid to its employees everywhere. The act limits the scope of this comparison by providing that only compensation paid for work at specific locations is included in the calculation of the factor.<sup>35</sup> The specific locations are:

(1) A location that is owned, controlled, possessed, used, or rented by (a) the employer, (b) a vendor, customer, client, or patient of the employer, or a related member of such a person, or (c) a vendor, customer, client, or patient of a person described in (b), or a related member of such a person;

(2) A location where a trial, hearing, investigation, or similar administrative, judicial, or legislative proceeding is held, if the employee performs services for the employer at the location or if the employee's presence at the location benefits the employer;

(3) Any other location if the tax administrator finds that the employer directed an employee to work at that location in lieu of a location described in (1) or (2) solely in order to avoid municipal income taxation. If the tax administrator makes such a determination, the employer may dispute the finding by establishing, by a preponderance of the evidence, that the finding was unreasonable.

Similar to prior law, compensation that is not subject to tax withholding under the "occasional entrant rule" (see "**Occasional entrant exemption**") is not included in the calculation of a business' payroll factor.

### Sales factor

Under continuing law, the "sales factor" compares a business' receipts from goods and services sold in a municipal corporation to the business' total receipts from all such sales. A sale of goods is made in a municipal corporation when the goods are any of the following:

(1) Shipped and delivered within the municipal corporation;

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<sup>35</sup> R.C. 718.02(C).

(2) Delivered within the municipal corporation, but shipped from elsewhere, if employees of the business regularly solicit sales within the municipal corporation and the sale of the goods results from that solicitation;

(3) Shipped from the municipal corporation, but delivered elsewhere, if the business, through its own employees, does not regularly solicit sales at the location where the goods are delivered. (This final criterion is known as a "throw-back" provision.)

The act further specifies that income from the sale of services is assigned to a municipal corporation based on the extent to which the services were performed within the municipality.

In addition, the act expands the scope of the "sales factor" to expressly include a business' income from renting property and from selling real property. Income from the sale or rental of real property, and royalties from real property, are assigned to the municipal corporation where the property is located. Income from the rental of tangible personal property or royalty income is assigned to a municipal corporation based on the extent to which the property is used in the municipality.<sup>36</sup>

### **Property factor**

Under continuing law, the "property factor" compares the value of all real and tangible personal property owned or used by a business within a municipal corporation to the total value of all of the business' property. Continuing law specifies that this calculation includes the value of real property that the business rents or leases. The act adds that the calculation must also include the value of rented or leased tangible personal property.<sup>37</sup>

### **Treatment of disregarded entities**

Under the act, if a taxpayer is the owner of a disregarded entity, the calculation of the taxpayer's payroll, sales, and property factors must include the payroll, sales, and property of the disregarded entity.<sup>38</sup>

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<sup>36</sup> R.C. 718.02(D).

<sup>37</sup> R.C. 718.01(A)(1).

<sup>38</sup> R.C. 718.02(H).



## Approval of an alternative formula

Under prior law, a municipal corporation could allow a taxpayer to use an alternative apportionment formula if the three-part formula did not "produce an equitable result." The act instead allows a taxpayer to request to use an alternative apportionment method, and provides that a municipal corporation may require a taxpayer to use an alternative formula, if the three-part formula does not "fairly represent the extent of the taxpayer's business activity" in the municipal corporation.<sup>39</sup> An alternative formula may involve separate accounting, the exclusion or modification of one of the three factors, or the inclusion of a different factor.

A taxpayer's request to use an alternative formula must be submitted in writing with the taxpayer's return, amended return, or appeal of an assessment. The tax administrator may deny the request only by issuing an assessment. For a tax administrator to require a taxpayer to use an alternative formula, the tax administrator must issue an assessment. (See "**Assessments of tax liability**," below.)

The act also provides that any agreement approving an alternative formula that is entered into before January 1, 2016, may continue in effect after that date.

## Rental income

Continuing law provides that, if a person receives income from rental activity but is not in the business of renting property, the person's net profit is subject to taxation where the property is located (in addition to the person's municipal corporation of residence). The act removes the condition that the person's rental activity not constitute a business or profession, but, to similar effect, specifies that the rule applies only to individuals (not business entities). The act also expressly limits the application of the rule only to renting real property and to net profit that an individual receives from renting real property owned directly by the individual or by a disregarded entity owned by the individual (e.g., a limited liability company owned only by the individual).

The act also allows an individual with such net profit to elect to use separate accounting to calculate the individual's net profit from such activity.<sup>40</sup>

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<sup>39</sup> R.C. 718.02(B).

<sup>40</sup> R.C. 718.02(E).

## **Real estate commissions and profits**

The act prescribes specific rules for the apportionment of real estate agent and broker income.<sup>41</sup> Under the formula, the net profit of an agent or broker is apportioned to a municipal corporation based upon the proportion of the commissions that the agent or broker earned from the sale, purchase, or lease of property located in the municipal corporation as compared to the agent's or broker's total commissions in that year. Commissions from the sale, purchase, or lease of real estate are assigned to the municipal corporation in which the real estate is located.

Under the act, an individual must file a return reporting all of the individual's net profit from "real estate activity" with the individual's municipal corporation of residence if that municipal corporation levies an income tax. However, that municipal corporation may offer a credit to the individual for the amount of taxes the individual paid on such net profit to other municipal corporations.

## **Tax withholding at source**

The act prescribes uniform municipal income tax employer wage withholding requirements and schedules and modifies the withholding of taxes from gambling winnings.

### **Employer withholding**

Under the act, employers must withhold municipal income taxes from employees according to a fixed schedule whereby the frequency of the withholding depends on the withholding amount for the municipal corporation in the preceding year.<sup>42</sup> The act also specifies that the amount that must be withheld equals each employee's "qualifying wages" (described above) for the withholding period multiplied by the applicable municipal income tax rate. Withholding must be done at the time an employee is directly, indirectly, or constructively paid or when wages are credited to the benefit of an employee. The amount an employer is required to withhold and remit to a tax administrator is deemed to be held in trust for the state whether or not the employer actually withholds and remits the amount. Employers must withhold tax for any municipal corporation in which the employer does business, but may withhold tax for an employee's resident municipal corporation at the employee's request.

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<sup>41</sup> R.C. 718.02(F).

<sup>42</sup> R.C. 718.03. The withholding requirement applies not only to employers but to an employer's agent (e.g., a payroll processing company) and to "other payers," which include anyone other than an employer or employer's agent that pays an individual an amount that is included in federal gross income (as under prior law).

Withholding is not required for employees whose compensation is not taxable under the 20-day occasional entrant provision (described above).

Under prior law, no schedule or amount of wage withholding was prescribed for municipal corporations, thus leaving it to each municipal corporation to devise its own schedule and withholding amounts.

**Schedule and due dates**

The act's wage withholding schedule depends on either the total amount the employer was required to withhold during the preceding year or the amounts the employer was required to withhold during any single month in the preceding quarter, as follows:

<b>H.B. 5 Employer Mandatory Withholding Schedule</b>	
<b>Preceding period's withholding</b>	<b>Remittance frequency</b>
Annual amount of \$2,399 or less, and no month in preceding quarter of \$200 or more	Quarterly, due by the 15th day after the quarter's end
Annual amount more than \$2,399, or any month in preceding quarter more than \$200	Monthly, due by the 15th day of following month

In addition to the foregoing schedule, the act expressly authorizes a municipal corporation to require semimonthly remittance if an employer's preceding year withholding requirement exceeded \$11,999 or if in any month in the preceding year the requirement exceeded \$1,000. If such withholding and remittance is required, taxes withheld during the first 15 days of a month must be remitted within three banking days after the 15th day of the month, and taxes withheld after the 15th day of the month must be remitted within three banking days after the last day of that month.

**Reporting and remittance**

Failure to report and remit taxes on time and in the amount required subjects a person to a penalty equal to 50% of the amount of the deficiency, and interest may accrue on unpaid amounts at the federal short-term interest rate plus 5%.<sup>43</sup>

The act requires each employer subject to the withholding requirements to file an annual report with the appropriate tax administrators. The report must list the names, addresses, and Social Security numbers of employees for whom tax withholding was made for the preceding year, the amount withheld, the amount of qualifying wages

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<sup>43</sup> R.C. 718.27(C). The computation of the interest rate is described in the "**Penalties and interest**" section of this analysis.



paid, the name of every other municipal corporation for which the employer withheld taxes during the preceding year, all other information required for federal income tax reporting purposes and any other information the tax administrator requires. A municipal corporation may require an employer (or agent or other payer) to remit withheld taxes electronically if the employer is required to remit its employees' federal income tax withholdings electronically. The report is due by the last day of February.<sup>44</sup>

The act continues prior law's provisions specifying that failure by an employer to properly withhold taxes does not relieve the employee of liability for the tax, and that failure by an employer to remit withheld taxes does relieve the employee of liability unless the employee and employer colluded.<sup>45</sup>

The act expressly provides that, when an employee does not live and work in the same municipal corporation, the employee may request that the employer (or its agent or another payer) also withhold municipal income tax for the employee's municipal corporation of residence. Such voluntary withholding must comply with all the act's requirements for mandatory withholding and remittance.<sup>46</sup>

#### **Wage withholding base**

As under prior law, "qualifying wages" is the basis on which the amount withheld and the frequency of withholding is determined. The act continues two of prior law's exemptions from withholding. First, taxes need not be withheld against "disqualifying dispositions" of an employee incentive stock option if at the time of the disposition the recipient is not an employee of the employer-corporation. The act adds that the disposition must not have occurred while the recipient was employed by a successor to that employer. (A disqualifying disposition occurs – and favorable federal tax treatment is lost – when the recipient sells the stock acquired through the option within the minimum holding periods prescribed by federal law.) Second, taxes need not be withheld against any compensation deferred before June 26, 2003, that does not satisfy the definition of qualifying wages when the deferred compensation is paid or distributed. (June 26, 2003, is the effective date of H.B. 95 of the 125th General Assembly, which enacted the withholding exemption for such deferred compensation.)<sup>47</sup>

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<sup>44</sup> R.C. 718.03(B)(2)(b) and (H).

<sup>45</sup> R.C. 718.03(E).

<sup>46</sup> R.C. 718.03(A)(2) and (K).

<sup>47</sup> R.C. 718.03(D) and (F).





## **Employee tips**

The act adds a specific rule for the withholding of tax from employee tips. Under the rule, taxes need not be withheld from employees' tips unless the customer paid the tip by credit card, debit card, or other electronic means, or if the customer paid the tip directly to the employer for subsequent remittance to the employee.<sup>48</sup>

## **Responsible party personal liability**

The act imposes personal liability on any individual employee or officer of an employer who has control or direct supervision over withholding, reporting, and remitting taxes from employees' wages and who fails to do so, even if the employer dissolves. The same personal liability applies to employers' agents and "other payers."<sup>49</sup> These provisions are substantially similar to provisions incorporated in the law governing state income tax and other state taxes that are collected by one party from another and held in trust for the state until remitted. Prior law did not address such personal liability for municipal income taxes, but municipal corporations could have adopted such a policy.

## **Gambling and video lottery withholding**

Under the bill, municipal corporations must apply their income taxes to gambling and lottery winnings.<sup>50</sup> Taxes must be imposed by a municipal corporation on its residents' winnings or by a municipal corporation where a casino or video lottery terminal (VLT) operator is located on patrons, whether a resident or nonresident.

The act modifies and clarifies the law governing municipal income tax withholding requirements placed on casinos and VLT operators. Continuing law requires casinos and VLT operators to withhold municipal income taxes from casino gambling and VLT winnings if they are in such an amount that federal income tax reporting is required.<sup>51</sup> The withholding is done for the municipal corporation where the casino or VLT facility is located. The tax is deducted from the winnings at the municipal income tax rate and reported and remitted to the appropriate municipal tax administrator. Casino and VLT operators must file monthly electronic withholding reports and make monthly remittances to the municipal corporations where the

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<sup>48</sup> R.C. 718.03(J).

<sup>49</sup> R.C. 718.03(I).

<sup>50</sup> See "**Taxable income**," above.

<sup>51</sup> R.C. 5747.063 and 5747.064 of prior law and R.C. 718.031 of the act.





facilities are located, and file annual reports and reconciliation remittances. Tax administrators prescribe the required forms.

The act modifies the continuing law's casino and VLT withholding requirements for municipal income taxes. Some of the modifications address apparent inconsistencies in prior law.<sup>52</sup> First, the act requires municipal income taxes withheld and remitted by a casino or VLT operator to be credited against the taxpayer's municipal income tax liability, not the taxpayer's state income tax liability as provided in prior law.<sup>53</sup> Second, the act clarifies that the law governing municipal tax assessments, not the law governing state income tax assessments, applies when a casino or VLT operator fails to withhold and remit taxes as the act requires. (An assessment is a formal notification of an alleged outstanding tax liability. Once it is issued, certain collection and appeals procedures and taxpayer rights are invoked.)

Third, the act removes a provision that requires casinos to issue receipts to patrons showing the amount of municipal income tax withheld from the patron's winnings. Under prior law, casinos had to make these receipts available to tax administrators upon request. The act does not remove a similar provision imposing this requirement on VLT operators.

Finally, the act changes the penalties for the failure to report or remit taxes withheld from gambling and VLT winnings. If a casino or VLT operator does not remit withheld taxes or remits such taxes late, the municipal corporation may impose a penalty equal to 50% of the withheld tax. If a casino or VLT operator fails to file a return or files a return late, the penalty is \$500 per return. Prior law imposed a penalty of up to \$1,000 for failure to report and remit such taxes.

## **Return filing**

The act prescribes procedures and deadlines for filing municipal income tax returns, including the annual return, filing extensions, amended returns, and consolidated corporation returns.

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<sup>52</sup> R.C. 718.031.

<sup>53</sup> R.C. 5747.063(D) and 5747.064(E) of prior law. H.B. 386 of the 129th General Assembly appears to have erroneously stated that withheld municipal income taxes are to be credited against state income tax liability and that state income tax assessment procedures were to be applied to municipal income tax withholding.

## Annual returns

The act requires all taxpayers subject to a municipal income tax to file annual tax returns unless their liability does not exceed certain thresholds, prescribes specific deadlines and forms and procedures for filing annual returns, and prescribes maximum penalties for failure to file returns properly or on time.

Prior law did not require tax returns of all taxpayers. Whether a return was required depended on each municipal corporation's ordinances or rules. No specific filing deadline was prescribed, but prior law did prohibit filing deadlines that fell before the federal return filing deadline for the corresponding federal tax reporting period.<sup>54</sup> Minimum filing and payment thresholds were not prescribed, but municipal corporations could have established their own.

### Form of return

The act requires each taxpayer required to file an annual return to complete and file the return on a form prescribed by the tax administrator or on a generic form that contains all the information required by ordinance, resolution, or rules adopted by the municipal corporation or tax administrator.<sup>55</sup> Filed returns must contain the taxpayer's signature or the signature of the taxpayer's authorized representative and of any tax preparer. The return must also include the taxpayer's Social Security number or taxpayer identification number.<sup>56</sup>

Under the act, a tax administrator may require a taxpayer to submit certain additional documentation with the taxpayer's annual return, amended return, or request for refund, but the act limits what forms of documentation a taxpayer may be required to file. Individual taxpayers may be required to submit only copies of the taxpayer's W-2 "Wage and Tax Statement" forms and their federal 1040 return. Other taxpayers may be required to submit only federal forms 1041, 1065, 1120, 1120-REIT, 1120F, or 1120S. In addition, the tax administrator may require either type of taxpayer to provide information necessary to support a refund request or any adjustments made in an amended return.

A tax administrator cannot require that any other additional forms be filed with an annual return, amended return, or refund request; however, after a return has been

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<sup>54</sup> R.C. 718.05(B) of prior law.

<sup>55</sup> R.C. 718.05(A) and (L) of the act.

<sup>56</sup> R.C. 715.05(F)(1).



filed, the administrator may request any additional documentation necessary to verify the taxpayer's tax liability.

The act requires the Department of Taxation to prescribe a method by which nonindividual taxpayers filing net profit returns may submit the supplemental information along with the return through the Ohio Business Gateway (see "**Ohio Business Gateway Steering Committee**," below). The method must be developed and made available to taxpayers by January 1, 2016.<sup>57</sup>

### **Filing deadlines**

Under the act, the deadline for filing annual returns for all municipal corporations is established as the same filing deadline for Ohio individual income tax returns – i.e., April 15.<sup>58</sup>

### **Extensions**

The act permits a taxpayer that requests a federal income tax filing extension to receive an automatic extension for the same period to file annual municipal returns.<sup>59</sup> If an Ohio income tax filing extension is granted to all taxpayers, the municipal filing deadline is extended for the same period.<sup>60</sup>

Prior law only addressed filing extensions when a taxpayer requested an extension for filing a federal income tax return.<sup>61</sup> The extension for filing a return does not extend the last date for paying the tax without penalty unless the municipal corporation grants an extension of that date.

The act also requires municipal corporations to allow a taxpayer subject to a municipal tax on net profit to file a municipal income tax return extension electronically by using the Ohio Business Gateway (see "**Ohio Business Gateway Steering Committee**," below). Under continuing law, such taxpayers may file net profit and estimated net profit returns and make related payments through the Gateway.<sup>62</sup>

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<sup>57</sup> R.C. 715.05(F)(2), (3), and (4).

<sup>58</sup> R.C. 718.05(G)(1); R.C. 5747.08(G), not in the act.

<sup>59</sup> R.C. 718.05(G)(2).

<sup>60</sup> R.C. 718.05(G)(3).

<sup>61</sup> R.C. 718.05(D) and 718.051 of prior law.

<sup>62</sup> R.C. 718.051 of the act.



### **Extension for military personnel**

The act permits active-duty National Guard members and military reservists to request municipal income tax filing and payment extensions that continue for the period of active duty status and for 180 days after termination of active duty.<sup>63</sup> The active duty must result from either a Presidential executive order or Congressional act. The extension permission also applies to civilian support personnel serving in a combat zone or contingency operation. The extension must be applied for with the appropriate tax administrator, and the administrator may require supporting documentation. Once the extension ends, taxes are payable under an installment arrangement. The tax administrator may prescribe the terms of the installment arrangement as the administrator considers appropriate.

A filing and payment extension also is granted to active-duty National Guard members, active-duty reservists, and support personnel serving in a combat zone or contingency operation who receive a federal extension. The extension is for the same length of time as the federal extension.

An individual may qualify for both extensions. In either case, no interest or penalty may be applied to the tax due during the extension. If an individual and the individual's spouse file jointly, the extension applies to the spouse as well. Both types of extension are substantially similar to existing state income tax extensions for such individuals.<sup>64</sup>

Under prior law, a municipal corporation could grant extensions independent of federal extensions for an individual, but was not required to.

### **Minimum filing and payment thresholds**

Under the act, if a taxpayer owes \$10 or less to a municipal corporation with an annual return for individual income or for net profits, the taxpayer is not required to pay the tax, but is not relieved of filing the return.<sup>65</sup>

If a municipal corporation grants its residents a credit for taxes paid to another municipal corporation and a resident's credit exceeds the liability to the municipal corporation of residence, the resident is not required to file a return with that municipal

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<sup>63</sup> R.C. 718.052.

<sup>64</sup> See R.C. 5747.026, not in the act.

<sup>65</sup> R.C. 718.05(G)(1) and (H).

corporation unless the municipal corporation provides otherwise by ordinance or resolution.<sup>66</sup>

### **Return for nonresident employees**

If an individual's only taxable income is qualifying wages earned in a municipal corporation where the individual does not reside, and the employer withheld the proper amount of tax, the individual does not have to file an annual return unless that municipal corporation requires such taxpayers to file an annual return.<sup>67</sup> Nothing under prior law limited the authority of municipal corporations to excuse or require returns for such taxpayers.

### **Joint returns**

The act specifies that municipal corporations may not deny spouses the ability to file joint returns.<sup>68</sup> Prior law did not address joint returns, thereby leaving it to each municipal corporation to allow or disallow joint filing and to determine the eligibility of individuals to file jointly.

### **Amended returns**

The act requires taxpayers to file an amended return with the appropriate tax administrator if any of the information required to compute a taxpayer's municipal income tax liability is altered as the result of an adjustment to the taxpayer's federal income tax return. If a final determination of federal or state income tax liability affects a taxpayer's municipal income tax liability, the taxpayer must file an amended return "based on" the final determination. If a taxpayer filed a consolidated return, the taxpayer must notify the tax administrator before filing an amended consolidated return.<sup>69</sup>

The act requires amended returns to be accompanied by payment of any additional tax due plus any penalty and accrued interest unless the tax due is \$10 or less.<sup>70</sup> A request for a refund on an amended return must be filed within 60 days after

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<sup>66</sup> R.C. 718.04(D) and 718.05(A).

<sup>67</sup> R.C. 718.03(C).

<sup>68</sup> R.C. 718.05(E).

<sup>69</sup> R.C. 718.12(E) and 718.41.

<sup>70</sup> R.C. 718.12(E).



the adjustment to the taxpayer's federal return is made. Municipal corporations are not required to issue refunds of \$10 or less.<sup>71</sup>

The act specifies that the filing of an amended return generally does not reopen facts, figures, computations, or attachments that are not directly or indirectly affected by the adjustment of the taxpayer's federal or state income tax return. However, the act allows those facts, figures, computations, and attachments to be reopened if the applicable statute of limitations for collection actions or filing for refunds has not ended. Regardless, the act specifies that taxpayers cannot be required to pay additional tax exceeding the amount that would have been due had all facts, figures, computations, and attachments been reopened. And any refund arising from the amended return may not exceed the refund that would have been due if all facts, figures, computations, and attachments were reopened.<sup>72</sup>

Previously, municipal corporations could establish their own ordinances or rules governing the filing of amended returns.

#### **Consolidated corporation returns**

The act imposes uniform standards with respect to the filing of consolidated municipal income tax returns by affiliated groups of corporations. Under the act, "affiliated group of corporations" has the same meaning as in the Internal Revenue Code, except that, if an affiliated group includes one or more incumbent local telephone exchange companies whose primary business is providing local exchange service in Ohio, the group must exclude every incumbent local telephone exchange company that would otherwise be included in the group. Consequently, the income or loss of such companies must be excluded from the income or loss of the group for municipal income tax purposes.<sup>73</sup>

#### **Electing consolidated filers**

The act requires municipal corporations levying an income tax to allow an affiliated group of corporations to file a consolidated tax return for any taxable year beginning on or after January 1, 2016, if the group filed a consolidated federal income tax return for the taxable year and at least one member of the group is subject to the municipal income tax. Under prior law, a municipal corporation had to accept a consolidated income tax return from any affiliated group of corporations that was

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<sup>71</sup> R.C. 718.41(C).

<sup>72</sup> R.C. 718.41.

<sup>73</sup> R.C. 718.06 of the act. An incumbent local telephone exchange company is a company that provided local exchange service when the federal Telecommunications Act of 1996 was enacted.



subject to the municipal corporation's tax if that affiliated group filed a consolidated federal income tax return for that taxable year.<sup>74</sup>

Under the act, if an affiliated group of corporations elects to file a consolidated municipal income tax return, the election is binding for the succeeding five years and is renewed for consecutive five-year periods until the group formally elects to discontinue filing a consolidated return. The group may request permission from the tax administrator to discontinue filing a consolidated return before the end of a five-year period. The tax administrator must approve the request for good cause shown.

An election to discontinue filing a consolidated return is binding for five years following the first taxable year of the election. An election to file a consolidated return or to discontinue filing a consolidated return is binding on all members of the affiliated group of corporations subject to a municipal income tax.<sup>75</sup>

Before filing an amended consolidated return or amending separate returns into a consolidated return, the taxpayer is required to notify the tax administrator.<sup>76</sup>

#### **Mandatory consolidated filers**

The act authorizes the tax administrator of a municipal corporation to require a taxpayer to file a consolidated return if the taxpayer is a member of an affiliated group that filed a federal consolidated return and the tax administrator determines, by a preponderance of the evidence, that intercompany transactions are not at arm's length and there is a distortive shifting of income or expenses with regard to the allocation of net profits to the municipality. Once the tax administrator makes such a determination, the taxpayer is required to continue filing a consolidated municipal income tax return for all subsequent taxable years unless the taxpayer receives written permission from the tax administrator to file a separate return or the taxpayer has experienced a "change in circumstances."<sup>77</sup>

#### **Calculation of net profit**

Under the act, an affiliated group's consolidated municipal income tax return must be prepared in the same manner as its consolidated federal income tax return.<sup>78</sup>

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<sup>74</sup> R.C. 718.06 of prior law.

<sup>75</sup> R.C. 718.06(B).

<sup>76</sup> R.C. 718.41(A).

<sup>77</sup> R.C. 718.06(C).

<sup>78</sup> R.C. 718.06(D).



The group's net profit within the municipal corporation is calculated in the same manner as a single corporation's net profit, with adjustments for items of income or deductions that were consolidated or eliminated on the group's federal tax return.

In calculating net profit, the group must either include or exclude the net profit or loss of a pass-through entity that is included in the consolidated federal taxable income of the group. If the group directly or indirectly owns at least 80% of the pass-through entity, the group may choose whether to include or exclude the entity's profit or loss. If the group does not own at least 80% of the pass-through entity, the group is required to exclude the entity's profit or loss.

When the net profit or loss of a pass-through entity is excluded from the group's net profit, the pass-through entity is subject to municipal income tax as a separate taxpayer on that portion of the excluded net profits. Where the net profit or loss of a pass-through entity is included in the group's net profit, the pass-through entity is not subject to municipal income tax as a separate taxpayer on the portion of net profits included in the consolidated federal taxable income of the affiliated group.<sup>79</sup>

#### **Joint and several liability**

The act specifies that each member of an affiliated group is jointly and severally liable for any taxes, interest, or penalties due with a consolidated return.<sup>80</sup>

#### **Existing consolidated filing arrangements**

If a group of corporations and their affiliates elected or entered into an agreement to file consolidated or combined tax returns before January 1, 2016, the act allows the group to continue to file consolidated or combined returns according to that election or agreement after January 1, 2016.<sup>81</sup>

### **Estimated tax payments**

#### **Estimated tax payment requirements and schedule**

Prior law did not require municipal corporations to collect estimated taxes, but it did limit the amounts and due dates for any municipal corporation that did require estimated payments.<sup>82</sup> If a municipal corporation required estimated tax payments,

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<sup>79</sup> R.C. 718.06(E).

<sup>80</sup> R.C. 718.06(G).

<sup>81</sup> R.C. 718.06(H).

<sup>82</sup> R.C. 718.08, repealed and re-enacted by the act.





those payments had to be made on a quarterly basis according to a uniform schedule. For individuals, the municipal corporation could require taxpayers to pay not more than 22.5% of the taxpayer's estimated annual tax liability (before any reduction for credits, estimated payments, or withheld taxes) by April 30, 45% by July 31, 67.5% by October 31, and 90% by January 31. For other taxpayers, the same threshold amounts applied, but the payments were generally due on the fifteenth day of the fourth, sixth, ninth, and twelfth months of the taxable year. (For calendar year taxpayers, those dates were April 15, June 15, September 15, and December 15.)

The act requires every taxpayer whose estimated annual tax liability, after subtracting amounts to be withheld from the taxpayer's qualifying wages, will be at least \$200 to report and pay estimated taxes unless an exemption applies. The payments must be made quarterly and in the same percentages as those specified in prior law (i.e., 22.5%, 45%, 67.5%, and 90%). However, for all taxpayers, the payments are due on the fifteenth day of the fourth, sixth, ninth, and twelfth months of a taxable year. (For calendar year taxpayers, those dates are April 15, June 15, September 15, and December 15.)<sup>83</sup>

Under prior law, amounts withheld from an individual's compensation were credited towards the payment of the individual's estimated tax in equal amounts for each of the quarterly due dates. The act maintains this general rule, but specifies that, if a taxpayer establishes the actual date the amounts were withheld, those amounts are considered to have been paid on the date they were withheld.

The act also specifies that tax overpayments applied as credits to a subsequent taxable year are considered to have been paid on the date the taxpayer mailed or electronically transmitted the payment. In addition, taxes withheld from winnings by a casino operator or by a lottery sales agent are considered to have been paid on the date the taxes are withheld.<sup>84</sup>

### **Safe harbor provisions**

Under continuing law, a municipal corporation may not penalize a taxpayer for the underpayment of estimated taxes (e.g., by charging a penalty or interest) if (1) the taxpayer is a resident individual but was not domiciled in the municipal corporation at the beginning of the year or (2) the taxpayer paid estimated taxes for the current taxable year equal to 100% of the taxpayer's total tax liability for the preceding taxable year.

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<sup>83</sup> R.C. 718.08(C).

<sup>84</sup> R.C. 718.08(B).



The act maintains these two "safe harbor" provisions, but specifies that the first provision applies only if the resident was not domiciled in the municipal corporation on January 1 of the calendar year that includes the first day of the resident's taxable year. The act additionally prohibits municipal corporations from penalizing a taxpayer for the underpayment of estimated taxes if the taxpayer has paid at least 90% of the amount due for the current year.<sup>85</sup> If a taxpayer fails to make estimated payments or meet any of the safe harbor criteria, the municipal corporation may charge interest on the unpaid tax. The interest accrues from the date the estimated payment was due until the date the full amount is paid.<sup>86</sup>

### **Declaration of estimated tax filing requirement**

Taxpayers required to make estimated payments under the act must file a declaration of estimated taxes. The declaration must be filed on or before the due date for municipal income tax returns (April 15 for individuals and other calendar year taxpayers), on or before the fifteenth day of the fourth month of a taxpayer's fiscal year (for fiscal year taxpayers), or on or before the fifteenth day of the fourth month after a taxpayer first becomes subject to the municipal corporation's tax. Taxpayers who file joint returns must file a joint declaration of estimated taxes.<sup>87</sup>

The act allows tax administrators to waive the declaration filing requirement for any class of taxpayers if the administrator finds that the waiver is reasonable and proper in light of administrative costs and "other factors." The act also specifies that a municipal corporation may waive the requirement for all taxpayers.<sup>88</sup>

### **Ohio Business Gateway Steering Committee**

The act authorizes the Governor to appoint additional municipal tax administrators to the Ohio Business Gateway Steering Committee – the body charged with overseeing and guiding the operations of the Ohio Business Gateway ("the Gateway"). The Gateway is the state-administered online computer network system that allows businesses to electronically file business and tax forms with state agencies. Under law generally retained by the act, the Committee consists of not more than four representatives of the business community, one representative of municipal tax administrators, and two tax practitioners, all appointed by the Governor and approved by the Senate. Additionally, the Committee consists of the following ex officio members

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<sup>85</sup> R.C. 718.08(E).

<sup>86</sup> R.C. 718.08(D).

<sup>87</sup> R.C. 718.08(B).

<sup>88</sup> R.C. 718.08(F).

or their designees: the highest officer of each state agency that uses the Gateway for the filing of tax documents, the Secretary of State, the Treasurer of State, the Director of Budget and Management, the state Chief Information Officer, the Tax Commissioner, and the Director of Development Services.

The act increases the maximum number of appointed members who may represent municipal tax administrators from one to three. The act requires that representatives of municipal tax administrators be selected from a list of candidates provided by the Ohio Municipal League.<sup>89</sup>

### **Municipal contact information**

The act requires that all correspondence from certain tax administrators include the name and contact information of an individual who is designated to receive inquiries related to the correspondence.<sup>90</sup> The designated individual may be the tax administrator or an employee of the tax administrator. The requirement applies to tax administrators of municipal corporations having a population greater than 30,000, multiple-municipality collection agencies (Regional Income Tax Agency and Central Collection Agency), and any person retained by a municipal corporation, regardless of population, to administer its income tax.

### **Tax refunds**

Under prior law, a municipal income taxpayer was entitled to a refund of all overpaid taxes regardless of the amount overpaid.<sup>91</sup> Interest accrued on the refund amount beginning on the day the taxpayer made the overpayment or the day the taxpayer's annual return is due, whichever was later, and ending on the day the refund was made. Under law retained by the act, no interest is paid if the taxpayer receives the refund within 90 days after the taxpayer filed the annual return or after that return was due, whichever is later.

Under the act, a taxpayer may receive a refund only if the amount overpaid is more than \$10 (similarly, taxes of \$10 or less do not have to be paid).<sup>92</sup> Interest accrues on the refund amount in a similar fashion as under prior law, except that interest may

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<sup>89</sup> R.C. 5703.57.

<sup>90</sup> R.C. 718.39.

<sup>91</sup> R.C. 718.12(C) and (D).

<sup>92</sup> R.C. 718.19.

begin to accrue only from the date of the overpayment, not from the annual return due date.<sup>93</sup>

Requests for a refund must be filed with the municipal corporation's tax administrator within three years after the date the tax was due or paid, whichever is later.<sup>94</sup> A tax administrator may require that a taxpayer provide substantiating documentation in support of a refund claim.<sup>95</sup>

Under continuing law, if tax or withholding is paid to a municipality and the time period for seeking a refund of the amounts paid lapses, a second municipality imposing a tax on that income or wages must allow a nonrefundable credit for the amounts paid to the first municipal corporation. If the tax rate in the second municipality is less than the tax rate in the first municipality, the credit is calculated on the basis of the second municipality's tax rate.

The act further specifies that if the tax rate in the second municipal corporation is greater than the tax rate in the first municipal corporation, then the tax due in excess of the credit afforded must be paid to the second municipal corporation, along with any penalty or interest accruing during the period of nonpayment. Under continuing law, the credit based on erroneous payment to another municipality cannot be carried forward.<sup>96</sup>

### **Assessments of tax liability**

The act specifies procedures for how municipal corporations are to formally notify taxpayers, employers, and others allegedly owing taxes of the person's liability, and for how those persons must respond if they intend to challenge the finding. The procedures are initiated by the issuance of an assessment to a taxpayer. The act defines "assessment" as a written finding by a tax administrator that a person has underpaid municipal income tax or owes penalty and interest.<sup>97</sup> The assessment must have "ASSESSMENT" printed at the top of its first page in all capital letters.

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<sup>93</sup> R.C. 718.12(D).

<sup>94</sup> R.C. 718.12(C). The three-year statute of limitations may be extended if the taxpayer files a refund request with an amended return after the end of the three-year period under R.C. 718.41.

<sup>95</sup> R.C. 718.19(B).

<sup>96</sup> R.C. 718.121.

<sup>97</sup> R.C. 718.01(PP) and 718.12. Only "taxpayers" will be referred to in the remainder of this section, but the term should be read to include employers or others that might have an alleged liability for income taxes withheld from employees.

The act specifies that the following items or actions are not assessments: billing statements notifying taxpayers of current or past-due balances, requests for additional information, or notices of mathematical errors. The denial of a request for refund is an assessment unless the request is made on an original annual return. In the case of the denial of a refund requested with the original annual return, the tax administrator must issue a notice denying the refund request, and the taxpayer may, in response, request that the tax administrator issue an assessment.<sup>98</sup>

The issuance of an assessment in compliance with the act's procedures initiates the time period within which a taxpayer may contest the assessment. A taxpayer contesting the assessment must file an appeal with the municipal corporation's local board of tax review within 60 days after the assessment is issued.<sup>99</sup> When an assessment is issued, the tax administrator also must provide the taxpayer with written notice of the taxpayer's right to appeal, the manner in which it may be appealed, and the address to which the appeal request must be sent.<sup>100</sup> These requirements are similar to those of prior law, but prior law did not refer to assessments [*per se*].

### **Delivery of assessments**

The act requires that assessments be issued to a taxpayer by either personal service, certified mail, or a delivery service approved by the state Tax Commissioner.<sup>101</sup> A taxpayer may consent to delivery of an assessment by alternative means such as secure email.

If the tax administrator's initial attempt to deliver an assessment fails because the mailing is returned as undeliverable to the taxpayer's last known address, the tax administrator must attempt to find the taxpayer's new address "by reasonable means," including the Postal Service's change of address service. If the new address is not found, the tax administrator must send the assessment again by ordinary mail (presumably to the original address). The act states that this mailing effectuates service of the assessment on the taxpayer. If the ordinary mailing fails because of an undeliverable address, the postmark date of that mailing establishes the 60-day appeal period. The act also states that "delivery" by any of the foregoing means is *prima facie* (i.e., rebuttable) evidence that delivery of the assessment is complete.

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<sup>98</sup> R.C. 718.01(PP)(2) and 718.19(B).

<sup>99</sup> R.C. 718.11(C).

<sup>100</sup> R.C. 718.11(B).

<sup>101</sup> R.C. 718.18.



If delivery by certified mail fails for some reason other than being returned because of an undeliverable address, the tax administrator is required to resend the assessment by ordinary mail. The assessment must show the date of the ordinary mailing and must include a statement, specified in the act, informing the addressee that the 60-day appeal period for the assessment begins ten days from the date of the mailing. The mailing is prima facie evidence that the delivery was completed ten days after the mailing and that the assessment was served, unless the mailing is returned because of an undeliverable address. If the ordinary mailing is returned because of an undeliverable address, the tax administrator must proceed as if the original certified mailing had been returned because of an undeliverable address.

A person may dispute the presumption that delivery of an assessment was successful by showing, by a preponderance of evidence, that the person was not associated with the address where the mailing was sent when the assessment was sent. If a person appeals an assessment on the basis that delivery was not made to an address associated with the person, and the assessment is not otherwise applicable but is subject to collection, the person must appeal within 60 days after initially being contacted.

### **Limits on collection actions**

As under prior law, the act generally requires civil actions to collect municipal income taxes to be brought within three years after the tax due date or the date the return was actually filed (whichever is later). However, the act specifically provides a potentially longer period if the taxpayer contests the finding that unpaid taxes are due by filing an appeal with the local board of tax review. If such an appeal is filed, the time limit on civil actions begins when the appeal is filed and ends one year and 60 days after the appeal, and any subsequent appeal, is finally decided and all further opportunities for appeal are exhausted or expire. If this period ends before the expiration of the three-year period, the limit on actions is three years after the tax payment or return filing due date. (The act defines the period between the appeal filing date and 60 days after the appeal is finally decided as the "qualifying deferral period." The time limit on the civil action ends one year after this period.) No action may be filed by a municipal corporation to collect tax, penalties, or interest that is being appealed or can still be appealed.<sup>102</sup>

By mutual consent, in writing, a taxpayer and tax administrator may extend the foregoing time limits. If such an extension is agreed to, the time limit on the taxpayer making a related refund claim is extended by the same period. (See "**Tax refunds**," above.)

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<sup>102</sup> R.C. 718.12(A), (B), and (G).

The act does not change the law that requires criminal prosecutions regarding municipal income tax ordinances to be brought within three years after the offense, or six years in cases of fraud, failing to file returns, or omitting at least 25% of reportable income.

## **Penalties and interest**

The act specifies the amount of penalties and interest that municipal corporations may impose for failure to file returns or pay taxes on time. Under prior law, municipal corporations were authorized to establish their own penalty and interest impositions. The act's limits on penalty and interest apply to returns and tax payments (including tax withholding remittances and estimated payments) due after January 1, 2016.<sup>103</sup>

The civil penalties and interest that a municipal corporation may impose are as follows:

- The rate of interest that must be charged on unpaid taxes is the average yield on marketable securities issued by the United States government that mature within three years (which the act defines "federal short-term rate"), plus 5%. Each municipal corporation is required to publish this rate of interest annually.<sup>104</sup>
- For unpaid taxes and estimated taxes, a penalty of 15% of the unpaid amount.
- For unremitted wage withholdings, a penalty of 50% of the unpaid amount.
- For each late return other than an estimated tax return, \$25, increasing by \$25 for each month the return remains unfiled, up to \$150.<sup>105</sup>
- For unremitted withholding from casino or VLT winnings, a penalty of up to 50% of the unpaid amount.
- For late filing or failure to file a casino or VLT withholding return, a penalty of \$500 per return, and interest accruing at the federal short-term rate plus 3%.

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<sup>103</sup> R.C. 718.27(B) and (D).

<sup>104</sup> See R.C. 718.27(A), (C), and (F) and 5703.47.

<sup>105</sup> R.C. 718.27(C).





The act also provides that any person that fails to remit withheld taxes is guilty of a first degree misdemeanor and subject to a fine of up to \$1,000 or imprisonment for up to six months, or both. This statutory penalty applies unless the violation is punishable by a municipal ordinance that imposes a greater penalty or requires dismissal from office, discharge from employment, or both, in which case the offender is penalized under the municipal ordinance.<sup>106</sup>

The act does not prohibit a municipal corporation from fully or partially abating (i.e., forgiving) the civil penalties at the discretion of the tax administrator. The act does not prohibit a municipal corporation from charging the post-judgment costs of collecting taxes, interest, and penalties, including attorney's fees.<sup>107</sup>

### **Local boards of tax review**

The act modifies existing minimum procedural requirements regarding municipal income tax appeals. The requirements apply only to municipal corporations that impose an income tax.

Continuing law requires a municipal corporation to create a board of appeals within 180 days after a municipal income tax takes effect.<sup>108</sup> Taxpayers may appeal decisions of the tax administrator to the board, provided that the taxpayer filed required tax returns and documents pertaining to the municipal income tax obligation at issue. The act renames boards of appeal as "local boards of tax review" and extends taxpayers' right of appeal to assessments issued by the tax administrator.

### **Composition of the board**

Under prior law, each municipal corporation imposing an income tax had authority to determine the composition of its board of appeals. The act rescinds that authority and requires each local board of tax review to consist of three members, two of which are appointed by the municipal legislative authority and one of which is appointed by the top municipal administrative official. The two legislatively appointed board members must not be employees, elected officials, or contractors with the municipal corporation at any time during their terms or in the five years immediately preceding the date of appointment. These board members serve a term of two years. There is no limit to the number of terms a legislatively appointed member may serve if the member is reappointed at the expiration of a term. The board member appointed by

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<sup>106</sup> R.C. 718.99(A).

<sup>107</sup> R.C. 718.27(E) and (G).

<sup>108</sup> R.C. 718.11.



the top administrative official may be, but is not required to be, an employee of the municipal corporation. This board member may not be the tax administrator, the director of finance or equivalent officer, an employee or other similar official directly involved in municipal tax matters, or any direct subordinate of such an officer, employee, or administrator. This board member serves at the discretion of the top administrative official.

The act specifies that any member of the local board of tax review who ceases to meet the qualifications for the position resigns immediately by operation of law. Legislatively appointed board members may be removed by the legislative authority of the municipal corporation before the expiration of a term for malfeasance, misfeasance, or nonfeasance in office. The legislative authority must afford such a member due process by giving the member a copy of the charges against them and allowing the member the opportunity to be publicly heard in person or by counsel in the member's defense upon at least ten days' notice. A decision by the legislative authority to remove a member of the board of tax review is final and may not be appealed.

If a member is temporarily unable to serve on the board due to a conflict of interest, illness, or other absence, the legislative authority or administrative official that appointed the member must appoint a temporary replacement. The same requirements that apply to the appointment of a permanent member apply to the appointment of the member's temporary replacement.

The act requires any permanent vacancy in an unexpired term to be filled within 60 days after the vacancy is created. Appointments to fill vacancies on the board must be made in the same manner as initial appointments. Board members appointed to fill a vacancy hold office for the remainder of the unexpired term.<sup>109</sup>

### **Notice to taxpayers**

Prior law required tax administrators to provide written notice to taxpayers of the right to appeal and the procedure for pursuing an appeal when issuing a "decision regarding a municipal income tax obligation" that was appealable. The act eliminates this general notice requirement but requires notice when a tax administrator issues an assessment or denies a refund claim.<sup>110</sup>

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<sup>109</sup> R.C. 718.11(A).

<sup>110</sup> R.C. 718.11(B).



## **Procedural requirements**

The act requires requests for appeals to be filed with the local board of tax review within 60 days after the taxpayer receives the assessment. Under prior law, taxpayers were required to file requests for appeal within 30 days after the tax administrator issued an appealable decision. Continuing law requires that the request be in writing and state the alleged errors in the decision. The act eliminates the former requirement that the taxpayer filing the appeal must have filed all the required returns and documents pertaining to the municipal income tax obligation at issue.

Under prior law, the board was required to schedule hearings within 45 days after receiving a request unless the taxpayer waived a hearing. The act extends the hearing deadline to 60 days after receiving a request and, in addition to waiver, the act allows the board to delay a hearing if the taxpayer requests additional time to prepare or if the parties jointly agree to a continuance. If the parties agree to a continuance, the act stipulates that the hearing must be completed within 120 days after the first day of the hearing, unless the parties agree to a different time frame. Under continuing law, the board must issue a decision within 90 days after the final hearing, and send notice of its decision to the taxpayer within 15 days after issuing the decision.<sup>111</sup>

## **Compromise of claims and payment plan agreements**

For any income tax and related amounts owed to a municipal corporation, the act specifies that nothing prevents the tax administrator from either compromising a claim or entering into an extended payment plan ("pay-over-time plan") with the taxpayer. Furthermore, the act sets standards for such compromises or payment plans. A tax administrator may consider any reasonable standard when deciding whether to compromise a claim or enter into a pay-over-time plan, including the practical difficulty of collecting the amount due, the likelihood that the taxpayer would be entitled to a refund of the amount due, economic hardship, or, if the claim is a joint liability of two spouses, that compromising the claim would protect the spouse not responsible for causing the claim ("innocent spouse"). A spouse is rebuttably presumed to be an innocent spouse if the spouse was granted similar relief against a joint assessment by the Internal Revenue Service.

A compromise or pay-over-time plan does not extinguish the liability of anyone other than the parties to the agreement. A tax administrator's decision to reject a person's offer to compromise a claim or enter into a pay-over-time plan may not be appealed. A compromise or pay-over-time plan is void if a taxpayer defaults under a term of the compromise or plan or if the compromise or plan was obtained by fraud or

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<sup>111</sup> R.C. 718.11(C), (D), and (E).

by misrepresentation of a material fact. In the event a compromise or plan becomes void, any unpaid amounts remain due, and interest that would have accrued in the absence of the compromise or plan continues to accrue.<sup>112</sup>

Prior law did not address the authority of municipal tax administrators to compromise income tax claims or enter into pay-over-time agreements. Any such authority would have been governed by municipal ordinance or rule.

## **Audit procedures**

The act prescribes procedures and limits for auditing taxpayers for municipal income tax purposes. Prior law did not govern or otherwise regulate how such audits were conducted; instead, it stated that nothing in Chapter 718. limited or removed the ability of each municipal corporation to administer, audit, and enforce the provisions of its income tax.<sup>113</sup> The act's audit provisions are similar to those that apply to audits for state tax liability.<sup>114</sup>

The act defines an audit as "the examination of a person or the inspection of the books, records, memoranda, or accounts of a person for the purpose of determining liability for a municipal income tax."<sup>115</sup>

The act requires tax administrators to provide taxpayers with certain information before beginning an audit. Specifically, the administrator must provide a written description of the roles of the tax administrator and of the taxpayer during an audit and a statement of the taxpayer's rights. This writing must include notice of any right of the taxpayer to obtain a refund of an overpayment of a tax. Furthermore, the taxpayer is entitled to be informed of the date when the audit is considered to have begun.

Unless criminal activity is suspected, the act requires audits to be conducted during regular business hours and only after "reasonable notice" is given to the taxpayer. If a taxpayer is unable to comply with the audit time proposed by the tax administrator, that taxpayer is required to offer reasonable alternative dates.

The act entitles taxpayers to assistance or representation by an attorney, accountant, bookkeeper, or other tax practitioner at all stages of the audit process. A taxpayer may refuse to answer any questions asked by the person conducting an audit

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<sup>112</sup> R.C. 718.28.

<sup>113</sup> See R.C. 718.01(A)(1) and 718.051(I) of prior law.

<sup>114</sup> See R.C. 5703.51.

<sup>115</sup> R.C. 718.01(UU).



until the taxpayer has an opportunity to consult with an attorney, accountant, bookkeeper, or other tax practitioner. The act requires tax administrators to provide a form allowing the taxpayer to designate a representative or advisor for any proceedings resulting from actions by the tax administrator. The tax administrator may accept other evidence that a person is the authorized representative of a taxpayer only if the taxpayer has not submitted such a form.

Under the act, a tax administrator may not prohibit a taxpayer from recording an audit examination.

A tax administrator who fails to substantially comply with municipal income tax audit regulations prescribed by the act is required to excuse the taxpayer from penalties and interest arising from the audit if the taxpayer applies to be so excused. However, failure to comply with municipal income tax audit regulations does not cure any procedural defect in a case brought by the taxpayer or excuse a taxpayer from payment of any taxes owed.<sup>116</sup>

## **Record retention**

Under the act, a tax administrator may require any person to keep records that the administrator considers necessary to show the extent of the person's liability for municipal income tax. The act also authorizes a tax administrator to inspect a taxpayer's records for up to six years after the taxable year to which the records relate. A taxpayer may destroy records before the end of that six-year period with written consent of the tax administrator. A tax administrator may require taxpayers to maintain the records beyond that time.<sup>117</sup>

## **Opinions on prospective tax liability**

### **Municipal tax administrators' opinions**

The act permits persons to ask a tax administrator to issue an official opinion with respect to that person's prospective municipal income tax liability.<sup>118</sup> The provision is similar to one in state tax law permitting taxpayers to ask the state Tax Commissioner for an opinion regarding prospective tax liability.<sup>119</sup> Nothing in prior law prevented a municipal corporation from implementing the same or similar rules by ordinance.

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<sup>116</sup> R.C. 718.36.

<sup>117</sup> R.C. 718.23.

<sup>118</sup> R.C. 718.38.

<sup>119</sup> See R.C. 5703.53.

The act requires a request for an opinion of a tax administrator be a written document that fully and accurately describes the specific facts or circumstances relevant to a determination of the taxability of the income, source of income, activity, or transaction at issue. If the request concerns an activity or transaction, the taxpayer must identify all parties involved by name, location, or other pertinent facts. The request must relate to the income tax imposed by the municipal corporation. If the request does not meet any of the foregoing criteria, or if the tax administrator's response is not written, signed, and designated as an "opinion of the tax administrator," the opinion is not binding. The act specifies that ordinary correspondence of the tax administrator does not constitute an opinion of the tax administrator.

A tax administrator may refuse to respond to any request for an opinion with respect to municipal tax liability. If the tax administrator issues an opinion, the act requires the document to provide reference to the reasons the opinion may be subject to change and inform the taxpayer of the taxpayer's duty to be aware of any such changes. Unless the requesting taxpayer asks that the text of the opinion remain confidential, the tax administrator is obligated to remove all taxpayer identifying information and make the opinion available to the public.

An opinion issued by a tax administrator on or after January 1, 2016, is binding with respect to the taxpayer who requested it and protects that person from liability for any taxes, penalty, or interest otherwise chargeable if the taxpayer reasonably relied on it. However, no taxpayer is relieved of liability if the request for the opinion contains any misrepresentation or omission of one or more material facts. An opinion of the tax administrator does not bind the tax administrator of any other municipal corporation, and may not be appealed.

Under the act, the tax administrator may revoke an opinion by sending a written revocation by certified mail, return receipt requested. The effective date of such a revocation is either the date the taxpayer received the revocation or one year from the date the opinion was issued, whichever is later. An opinion of the tax administrator ceases to provide protection to the requesting taxpayer upon the effective date of any of the following:

- (1) An amendment or enactment of a relevant section of state law or the municipal corporation's income tax ordinance that substantially changes the analysis and conclusion of the opinion;
- (2) A court-issued opinion establishing or changing relevant case law with respect to state law or the municipal corporation's income tax ordinance;



(3) If relevant, a change in federal statutes or regulations, or a court-issued opinion establishing or changing relevant case law with respect to federal statutes or regulations;

(4) Any change in the taxpayer's material circumstances;

(5) The expiration of the opinion, if specified.

### **Identifying taxpayer information**

If a tax administrator requires a person filing a tax document to provide identifying information, such as a Social Security number, the act requires that person to notify the tax administrator of any change to the required information before or upon filing the next tax document requiring the information.<sup>120</sup>

If a person does not notify the tax administrator that the person's information has changed, or if the person fails to comply with a request of the tax administrator to furnish identifying information within 30 days, the tax administrator may impose a monetary penalty on the person or any penalty provided by municipal ordinance. Additionally, a person that provides fraudulent identifying information is guilty of a fifth degree felony.<sup>121</sup>

### **Social Security number protection**

The act requires a tax administrator, when transmitting or otherwise using a tax document that contains a person's Social Security number, to take all reasonable measures to ensure that the number is not capable of being viewed by the general public, by masking the information or by other means. The tax administrator is prohibited from placing a person's Social Security number on the outside of any material mailed to the person.<sup>122</sup>

### **Confidentiality of municipal income tax information**

Continuing law stipulates that all information gained as a result of returns, investigations, hearings, or verifications required in connection with municipal income taxes is confidential and prohibits the disclosure of such information except in accordance with a judicial order or in connection with official municipal business as

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<sup>120</sup> R.C. 718.26(A).

<sup>121</sup> R.C. 718.26(C).

<sup>122</sup> R.C. 718.26(B).





authorized by state law or local ordinance or charter.<sup>123</sup> The prohibition does not prohibit tax administrators from providing copies of municipal income tax returns to the Tax Commissioner or the Internal Revenue Service, or from publishing statistics if in doing so they do not disclose particular taxpayer information and if an ordinance permits.

The act extends this prohibition to persons accessing such confidential information unless authorized under one of the existing exceptions. The act also extends the exceptions by allowing a designee of a tax administrator to furnish copies of municipal income tax returns, regardless of how the returns were received, and to furnish other related information to the Internal Revenue Service, the Tax Commissioner, or other tax administrators. And the act specifies that municipal corporations are not prohibited from disclosing statistical information so long as the information does not disclose information about particular taxpayers.

The act also prescribes minimum penalties for persons who unlawfully access or disclose confidential information. The disclosure of confidential information received from the Internal Revenue Service is a fifth degree felony punishable by a fine of not more than \$5,000 plus the costs of prosecution or imprisonment for up to five years, or both. The unlawful access or disclosure of any other confidential municipal income tax information is a first degree misdemeanor punishable by a fine of \$1,000 or imprisonment for up to six months, or both. In both cases, the statutory penalty applies unless the violation is punishable by a municipal ordinance that imposes a greater penalty or requires dismissal from office, discharge from employment, or both, in which case the offender is penalized under the municipal ordinance. Each instance of unlawful access or disclosure constitutes a separate offense for penalization purposes.<sup>124</sup>

Prior law did not prescribe minimum penalties for unlawful disclosure of confidential municipal income tax information. Instead, the penalties were left to the discretion of municipal corporations.

### **Action for damages by taxpayer**

The act implements a uniform standard by which taxpayers may seek damages for an action or omission of a tax administrator, an employee of a tax administrator, or an employee of a municipal corporation relating to the laws and rules governing municipal income taxes.<sup>125</sup> Prior law did not prohibit such actions, but the conduct that

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<sup>123</sup> R.C. 718.13.

<sup>124</sup> R.C. 718.99(B) through (D).

<sup>125</sup> R.C. 718.37.



invoked liability on the part of a tax administrator or a municipal corporation, the availability of damages, and the penalties for frivolous lawsuits were left to the authority of the municipal corporation imposing the income tax.

Under the act, an action for damages against a tax administrator, municipal corporation, or both is permissible if both of the following apply:

(1) An applicable state law or an instruction of the tax administrator is frivolously disregarded by the tax administrator, an employee of the tax administrator, or an employee of the municipal corporation. The act defines "frivolous" as conduct that obviously serves merely to harass or maliciously injure the taxpayer or that is not warranted under existing law and cannot be supported by a good faith argument for an extension, modification, or reversal of existing law.

(2) The action or omission challenged by the taxpayer occurred with respect to an audit or assessment and the review and collection proceedings connected with that audit or assessment.

A taxpayer is not permitted to seek damages from the office of the tax administrator or the municipal corporation based on actions or omissions of the tax administrator, an employee of the tax administrator, or an employee of the municipal corporation that are manifestly outside the scope of employment or performed with malicious purpose, bad faith, or in a wanton or reckless manner. Presumably, a taxpayer could seek damages from the individual who perpetrated the action or omission in such a situation. Furthermore, the act stipulates that opinions of the tax administrator or other information functions of the tax administrator are not subject to legal challenge by taxpayers.

Under the act, the proper forum for a taxpayer seeking damages from a tax administrator or municipal corporation is the court of common pleas of the county in which the municipal corporation is located. Upon a finding of liability on the part of the municipal corporation or the tax administrator, the court may award compensatory damages as well as reasonable costs of litigation and attorneys' fees. The act requires the court to consider any negligent actions or omissions on the part of the taxpayer that may have contributed to the taxpayer's damages in calculating the judgment, but specifically states that a court "shall not be bound by" existing law providing for a defendant to assert the plaintiff's contributory fault and its effect on compensatory damage awards.

The act permits the court to impose a penalty on a taxpayer who brings a frivolous action. The court may also impose a penalty on the taxpayer if the action appears to be an attempt to merely harass or maliciously injure the tax administrator,



the municipal corporation, or employees of the tax administrator or the municipal corporation. The penalty may not exceed \$10,000. The proceeds arising from the penalty are paid to the general fund of the municipal corporation.

The act's provisions respecting actions for damages by taxpayers are substantially similar to continuing law that authorizes actions for damages against the state Tax Commissioner and employees of the Department of Taxation.<sup>126</sup>

## **False or fraudulent tax documents**

The act prohibits any person, with intent to defraud a municipal corporation or a tax administrator, from knowingly making or presenting a false or fraudulent report or related records or documents or knowingly changing such records or documents. It also prohibits any person from knowingly assisting or advising someone else in such an undertaking. Violators are guilty of a first degree misdemeanor and subject to a fine of up to \$1,000, imprisonment for up to six months, or both. If the applicable municipal ordinance imposes a greater penalty or requires dismissal from office, discharge from employment, or both, the violator is penalized under the ordinance.<sup>127</sup>

This provision is substantially similar to R.C. 5703.26, which applies to items submitted to the Department of Taxation, the Treasurer of State, a county auditor, a county treasurer, or a county clerk of courts with intent to defraud the state or any of its subdivisions.

## **Tax administrator functions**

In addition to the various duties and functions of tax administrators described in other sections of this analysis, the act expressly authorizes tax administrators to perform several of the same general functions that the Tax Commissioner performs in relation to the state income tax:<sup>128</sup>

- Require the production of books, papers, records, or federal income tax returns for inspection by the tax administrator or authorized agent. The act specifies that any person retained to audit or inspect the documents of

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<sup>126</sup> See R.C. 5703.54.

<sup>127</sup> R.C. 718.35 and 718.99.

<sup>128</sup> R.C. 718.23, 718.24, and 718.31. Cf. R.C. 5703.04, 5703.05, and 5703.20. As indicated in the "**Background**" section of this analysis, under the home rule powers granted municipalities by the Ohio Constitution, tax administrators do not need statutory authorization to perform the functions described in the act. The act does clarify that, absent an express limitation in the Revised Code, no provision of R.C. Chapter 718. should be construed to limit the ability of administrators to perform the described functions.

a taxpayer may not be paid on a contingency basis (i.e., based on the amount of money the person may discover for recovery).

- Take other investigative actions related to the tax administrator's duties, including issuing subpoenas to compel testimony, examining persons under oath, and administering oaths. A person compelled to attend a hearing or examination may be represented by an attorney or other tax professional.
- Approve agreements to simplify a taxpayer's withholding obligations.
- Perform other administrative duties, including appointing agents, cooperating with other local, state, and federal officials, destroying old tax returns and other tax documents, issuing refunds, and making and correcting findings.

## **Reporting income tax revenue**

Under continuing law, a municipal corporation levying an income tax is required to report to the Tax Commissioner by August 31 of each year the income tax revenue collected by the municipal corporation in the preceding calendar year. The Commissioner may withhold direct disbursements from the Local Government Fund that are otherwise available to every municipal corporation levying an income tax in 2007 from a municipal corporation that fails to report this information.

The act specifies additional information to be included in the municipal corporation's annual report to the Commissioner. Specifically, the municipal corporation must report income tax revenue collected and the amount of refunds awarded by a municipal corporation during the preceding calendar year, both arranged, when possible, according to the "type of income" from which the tax originated. Additionally, each municipal corporation must report the amount of income tax revenue collected and refunded on behalf of a JEDD or a JEDZ that levies an income tax administered by the municipal corporation and the amount distributed to contracting parties during the preceding calendar year.<sup>129</sup>

### **Municipal Income Tax Revenue Reporting Study Committee**

The act creates the Municipal Income Tax Revenue Reporting Study Committee to examine the feasibility of requiring municipal corporations to separately report the portion of income tax revenue paid by resident individuals compared to the portion paid by nonresident individuals. The act states that the General Assembly intends to

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<sup>129</sup> R.C. 5747.50(D).



promote transparency with regard to the source of municipal income tax receipts without imposing a significant burden on municipal corporations that levy such taxes.

The Committee is a public body consisting of 12 members. The act requires that such members be appointed within 30 days of the act's 90-day effective date. The members of the committee are as follows:

- Three members of the Senate – two appointed by the Senate President and one appointed by the Senate Minority Leader;
- Three members of the House of Representatives – two appointed by the Speaker and one appointed by the House Minority Leader;
- Six individuals representing business interests or municipal corporations that levy an income tax – two appointed by the Senate President, two appointed by the Speaker, one appointed by the Senate Minority Leader, and one appointed by the House Minority Leader.

Members of the Committee are not compensated for their time or reimbursed for their expenses.

The act requires the Committee to issue a report of its findings and recommendations by May 1, 2015. The report is sent to the Governor, the President and Minority Leader of the Senate, and the Speaker and Minority Leader of the House of Representatives. The Committee dissolves by operation of law on May 1, 2015.<sup>130</sup>

### **Municipal-school district revenue sharing agreements**

Under continuing law, if a school district substantially overlaps with one or more municipal corporations, the district and the municipal corporations may agree to share the revenue from municipal income taxes.<sup>131</sup> To enter such an agreement, the territories of the school district and the municipal corporations must overlap such that at least 95% of the municipal territory is within the school district and at least 95% of the school district territory is within the municipal corporation or corporations. An agreement is also permissible if at least 90% of the school district territory is within the municipal corporation or corporations and the remainder is within another municipal corporation that has a population of 400,000 or more.

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<sup>130</sup> Section 5.

<sup>131</sup> R.C. 718.09 and 718.10.



Continuing law requires that municipal-school district revenue sharing agreements allocate at least 25% of the income tax revenue to the school district. A municipal income tax levied pursuant to such an agreement is subject to voter approval and may not apply to nonresidents.

The act stipulates that municipal income taxes levied pursuant to a municipal-school district revenue sharing agreement may not be collected until the year after voters approve the tax levy. All of the act's new limitations and requirements respecting municipal income taxes apply to taxes levied pursuant to such an agreement.

### **Net Operating Loss Review Committee**

The act creates the Municipal Income Tax Net Operating Loss Review Committee to evaluate and quantify the potential financial impact of requiring municipal corporations to allow NOLs to be carried forward for five years. The 11-member committee consists of two House members and two Senators from different political parties appointed by the respective chamber's leader; three persons representing municipal income taxpayers appointed by the Speaker of the House; three persons representing municipal corporations levying income taxes in 2016, at least two of which did not allow net operating loss carryforward under prior law, appointed by the Senate President; and one person appointed by the Governor, who serves as the Committee's chairperson. Members are not compensated or reimbursed for their expenses, and all members must be appointed by March 1, 2015.

Before September 30, 2016, each municipal corporation that levied an income tax in 2011, 2012, and 2013 is required to report to the Committee the difference between the municipal corporation's actual or projected revenue for years 2012 to 2018 under its pre-H.B. 5 treatment of NOL carryforwards and the revenue that would have resulted in each of those years if the municipal corporation had allowed NOLs to be carried forward for five years, as required by the act. To arrive at this difference, the municipal corporation is required to use a method prescribed by the Committee. The Committee is required to formulate this method by November 30, 2015.

If the Committee receives reports from at least 13 municipal corporations – including at least three with a population of more than 250,000, five with a higher ratio of business taxpayers than the state average, and five with a higher ratio of individual taxpayers than the state average – then the Committee is required to calculate the total revenue impact reported by municipal corporations. A majority of the Committee is required, by May 1, 2017, to issue a report of the Committee's findings and recommendations to address any revenue shortfalls, which may include using



supplemental funds from the Local Government Fund to mitigate those shortfalls. After issuing the report, the Committee ceases to exist on May 1, 2017.<sup>132</sup>

### Statement of purpose and legal authority

The act explicitly states that it is an exercise of the legislature's constitutional power to limit the taxation powers of municipal corporations "[i]n order to ensure a fair, stable, and efficient system of local taxation."<sup>133</sup> (See "**Background**" section of this analysis.)

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## HISTORY

ACTION	DATE
Introduced	01-30-13
Reported, H. Ways & Means	11-07-13
Passed House (56-41)	11-13-13
Reported, S. Ways & Means	12-03-14
Passed Senate (23-8)	12-03-14
House concurred in Senate amendments (60-32)	12-09-14

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<sup>132</sup> Section 4.

<sup>133</sup> Section 6.

