

# **Columbus Area Tax Administrators**

## **Annual Tax Presentation**

January 22, 2014

### ***Ohio Municipal Income Tax Hot Topics***

# What We Shall Cover

- ❖ Municipal Income Tax Legislation – A Sampling of Changes Proposed by Substitute House Bill 5, 130th Ohio General Assembly, As Passed by the Ohio House of Representatives on Nov. 13, 2013
- ❖ Reminder – *Servicemembers Civil Relief Act* and Spouses of Military Members
- ❖ Municipal income tax case law update

# Substitute House Bill 5, 130th Ohio General Assembly

- ❖ Introduced January 30, 2013 by  
Representatives Cheryl L. Grossman and  
Michael Henne
- ❖ Assigned to the House Ways and Means  
Committee Chaired by Representative  
Peter Beck
- ❖ Passed by the House on Nov. 13, 2013  
(bi-partisan vote: 56 - 39)

# Sub. H.B. 5 – What's In It?

❖ A LOT!

❖ Amends all but two of the twenty-three existing sections of Ohio Revised Code chapter 718 and adds twenty new sections to that chapter.

# Lottery and Gambling Winnings

- ❖ Sub. H.B. 5, As Amended – all lottery and gambling winnings are taxable. Only professional gamblers may take deductions.
- ❖ Current treatment – lottery and gambling winnings are taxable as determined by the municipality.
- ❖ Municipalities – agree w/ uniformity

# Individuals Under 18 Years Old

- ❖ Sub. H.B. 5, As Amended – income is exempt if exempted by municipal ordinance or resolution adopted by January 2, 2015.
- ❖ Current treatment – most municipalities exempt the income of individuals under the age of 18 from tax.
- ❖ Municipalities – do not oppose uniformity provision

# Net Operating Loss Carryforward

- ❖ Sub. H. B. 5, As Amended – mandates a five year NOL carryforward to be phased in over six years. NOL cfd's are calculated on a pre-apportionment basis.
- ❖ Current treatment – net operating loss carryforward set by municipal ordinance.
- ❖ Municipalities – limit NOLs to 0, 1, 3 or 5 yr. Subsequent new taxing authorities (except JEDD/JEDZ) must permit 5 yr. NOL.

# Municipal Residency/Domicile

- ❖ H. B. 5, As Introduced – must meet the State of Ohio’s “bright line test” for residency.
- ❖ Current treatment – domicile determined by common law indicators, developed from case law.
- ❖ Municipalities (and Sub. H.B. 5, as amended) – replaces the “bright line test” with codification of common law factors to determine domicile.



# Enforcement and Compliance

- ❖ H. B. 5, As Introduced – requires municipalities to follow an assessment process similar to that used by the State of Ohio.
- ❖ Current treatment – municipalities may utilize civil or criminal proceedings to enforce the provisions of the ordinance.
- ❖ Municipalities (and Sub. H.B. 5 as amended) – retain current treatment; add tolling of statute while appeals are pending; add list of documents required when filing.

# Occasional Entrant Rule

- ❖ Sub. H. B. 5, As Amended – increases to 20 the number of days an individual must spend in a community before the employer must withhold; withholding begins on the 21<sup>st</sup> day; provides guidance on defining a day; exclude “small” employers (<\$500,000 gross receipts for preceding taxable year) having a permanent place of business in Ohio.
- ❖ Current treatment – the withholding threshold is 12 days and “goes back” to the 1<sup>st</sup> day.
- ❖ Municipalities – blend 20 day threshold w/ current “goes back” treatment; keep definition of a day; address construction employers and exclude “small” employers. <sup>10</sup>

# Withholding Due Dates and Amounts

- ❖ Sub. H. B. 5, As Amended – establishes uniform withholding thresholds and due dates.
- ❖ Current treatment – withholding due dates and thresholds are set by each municipality.
- ❖ Municipalities – minor modifications to H.B. 5, As Introduced, but otherwise agree with what was introduced.

# De Minimis Payments and Refunds

- ❖ Sub. H. B. 5, As Amended – sets a de minimis of \$10/\$10.01 for payments or refunds; amounts under \$10/\$10.01 need not be paid or refunded.
- ❖ Current treatment – de minimis amounts set by municipal ordinance.
- ❖ Municipalities – agree w/ \$5 threshold as introduced in H.B. 5, As Introduced

# Minimum Estimates

- ❖ H. B. 5, As Introduced – estimated payments need not be made to a municipality if the estimated tax liability is less than \$200 for the year.
- ❖ Current treatment – minimum estimates are set by municipal ordinance.
- ❖ Municipalities (and Sub. H. B. 5, as amended) – propose that the threshold be reduced to \$100.

# Penalty and Interest

- ❖ H. B. 5, As Introduced – sets the penalty and interest rates that may be charged by a municipality for late filing, late or nonpayment of tax and for failure to make estimated payments.
- ❖ Current treatment – penalty and interest rates are set by municipal ordinance.
- ❖ Municipalities (and Sub. H. B. 5, as amended) – agree with H.B. 5 concept of uniformity, but modifies the P & I rates from what was introduced (interest rate will be federal short-term rate plus 5%).

# Pass-Through Entities

- ❖ The muni. net profits tax will be imposed on the PTE at the entity level.
- ❖ Municipalities can tax non-S corporation PTE income that passes through to resident, individual owners (and may provide a credit for muni. tax which the PTE has paid on such income).
- ❖ Municipalities can tax S corporation income passing through to resident, individual owners -- but only to the extent municipalities are currently so taxing (most municipalities are not currently taxing residents on their income from S corporations).

# Current Year Gain and Loss Offsets

- ❖ Gains and losses generated by (i) a taxpayer's different PTE's and (ii) the taxpayer's own efforts – other than qualifying wages – will offset each other.
- ❖ Losses cannot offset qualifying wages.
- ❖ Special rules for S corp. losses
- ❖ Current law: most municipalities will not allow the taxpayer to offset gains with losses to the extent the losses are generated in other municipalities imposing income tax.



Provisions in H.B. 5, As Introduced  
which are not in Sub. H.B. 5, As  
Passed by the Ohio House of  
Representatives

- ❖ Requiring each municipality to have a problem resolution officer.

Provisions in H.B. 5, As Introduced  
which are not in Sub. H.B. 5, As  
Passed by the Ohio House of  
Representatives

- ❖ Requiring the creation of a state-wide municipal tax policy board.

Provisions in H.B. 5, As Introduced  
which are not in Sub. H.B. 5, As  
Passed by the Ohio House of  
Representatives

- ❖ Denying a deduction for “Form 2106” expenses.

# Provisions in H.B. 5, As Introduced which are not in Sub. H.B. 5, As Passed by the Ohio House of Representatives

## ❖ Repealing the “throw-back” rule.

However, with respect to deliveries made from within a municipal corporation to a location outside the municipal corporation, Sub. H.B. 5 does situs to the destination municipal corporation such sales as long as the T/P is “regularly engaged” in solicitation in the destination municipal corporation.

# Provisions in H.B. 5, As Introduced which are not in Sub. H.B. 5, As Passed by the Ohio House of Representatives

## ❖ Repeal of the “throw-back” rule.

However, per Sub. H.B. 5 no longer will solicitation in the destination municipal corporation have to be performed by employees of the T/P in order for the sale to be sitused to the destination muni. corp.

# Provisions in H.B. 5, As Introduced which are not in Sub. H.B. 5, As Passed by the Ohio House of Representatives

## ❖ Repeal of the “throw-back” rule.

**Q:** per Sub. H.B. 5 will advertising directed to residents/businesses located in the destination municipal corporation be sufficient in order for the sale to be sitused to the destination municipal corporation?

Provisions in H.B. 5, As Introduced  
which are not in Sub. H.B. 5, As  
Passed by the Ohio House of  
Representatives

- ❖ Providing a net profits return filing exemption for businesses having a de minimis presence in the municipality.

Provisions in H.B. 5, As Introduced  
which are not in Sub. H.B. 5, As  
Passed by the Ohio House of  
Representatives

- ❖ Allowing nonprofessional gamblers to deduct gambling losses against gambling winnings.



# Provisions in H.B. 5, As Introduced which are not in Sub. H.B. 5, As Passed by the Ohio House of Representatives

- ❖ Allowing municipalities to file statutory liens (as does the State of Ohio) – rather than requiring the municipalities to initiate court actions to collect unpaid tax

Provisions in H.B. 5, As Introduced  
which are not in Sub. H.B. 5, As  
Passed by the Ohio House of  
Representatives

- ❖ Providing a “Taxpayer Bill or Rights” (extremely similar to the Ohio income tax “Taxpayer Bill of Rights”)

Provisions in H.B. 5, As Introduced  
which are not in Sub. H.B. 5, As  
Passed by the Ohio House of  
Representatives

- ❖ Requiring the “losing party” to pay the “winning party’s” legal fees

# Provisions in H.B. 5, As Introduced which are not in Sub. H.B. 5, As Passed by the Ohio House of Representatives

- ❖ Expressly stating that the amount of the patronage dividend deduction available for federal income tax purposes is not added back for municipal income tax purposes.

# Provisions in H.B. 5, As Introduced which are not in Sub. H.B. 5, As Passed by the Ohio House of Representatives

- ❖ Requiring that every municipality that imposes an income tax must tax each resident on her/his proportionate share of income from S corporations (and must allow S corp. losses to be deducted against PTE income)

# *Servicemembers Civil Relief Act –* Spouses of Military Members

- ❖ Provides income tax relief for the spouse of military service personnel living/working outside of his/her domicile because of the military service personnel's military orders.

# Case Law Updates

*MacDonald v. City of Shaker Heights, et al*,  
Case No. 13 AP 00071 Tenth District  
Court of Appeals – Pending

At issue in this case is the appropriate municipal income tax treatment of the taxpayer's Supplemental Executive Retirement Plan, a nonqualified deferred compensation plan.

# Case Law Updates

## **Ohio Board of Tax Appeals – Pending**

*MacDonald v. City of Cleveland* –  
appropriate municipal income tax  
treatment of a supplemental executive  
retirement plan.



# Case Law Updates

## **Ohio Board of Tax Appeals – Pending** *Nationwide Mutual Insurance v. City of Columbus*

Appropriate municipal income tax treatment and withholding requirements of supplemental executive retirement plans.

# Case Law Updates

## Ohio Supreme Court – Recent Decision

*Gessler v. City of Worthington Income Tax Board of Appeals*

Issue: does state law (Ohio Revised Code) prevail or does the city ordinance prevail?

# Case Law Updates

Ordinance (subsequently revised):

*. . . “net profit” for a taxpayer who is an individual means the individual's profit, **other than** amounts required to be reported on Schedule C, Schedule E, or Schedule F. (emphasis added)*

# Case Law Updates

Ordinance (subsequently revised):

*. . . “net profit” for a taxpayer who is an individual means the individual's profit, **other than** amounts required to be reported on Schedule C, Schedule E, or Schedule F. (emphasis added)*

Division (G)(1) of Ohio Revised Code section 718.01:

“. . . no municipal corporation may tax or use as the base . . . an amount other than the net profit required to be reported by the taxpayer on schedule C or F . . .”.

# Case Law Updates

Excerpts from the Ohio Supreme Court's decision:

Worthington chose not to tax Schedule C income, and the General Assembly cannot limit or restrict a power of taxation that Worthington did not exercise.

# Case Law Updates

Excerpts from the Ohio Supreme Court's decision:

Moreover, in this circumstance, the General Assembly is not exercising power to limit or restrict municipal taxing authority, but rather is directing imposition of a tax on Schedule C income.

# Case Law Updates

Excerpts from the Ohio Supreme Court's decision:

Thus, the General Assembly cannot command Worthington to impose a tax on Schedule C income when Worthington has chosen not to tax that income, because such a requirement is not an act of limitation.

# Case Law Updates

Excerpts from the Ohio Supreme Court's decision:

In the absence of any statute that functions as an “express act of restriction by the General Assembly,” . . . the former ordinance excluding Schedule C income from the definition of net profits is a valid exercise of the city’s municipal power to tax.



# Case Law Updates

Just for fun.....

*Middletown v. Myers*, 193 Ohio App.3d 632  
(12<sup>th</sup> Dist. 2011)

Issue of Domicile: City of Middletown or  
“God’s earth”?

# Questions???

Faye Gibson, Administrator  
Dublin Income Tax Department

Kevin Robison, Assistant Administrator  
Columbus Income Tax Department

Jeffrey P. Sherman  
Assistant Legal Counsel, RITA