OHIO LEGISLATIVE SERVICE COMMISSION

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Office of Research and Drafting

Legislative Budget Office

S.B. 188
133rd General Assembly

Fiscal Note & Local Impact Statement

Click here for S.B. 188's Bill Analysis

Version: As Introduced

Primary Sponsors: Sens. Schaffer and Roegner

Local Impact Statement Procedure Required: Yes

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Highlights

Fund	FY 2020	FY 2021	Future Years
State General Revenue Fund			
Revenues	Potential loss from ongoing bad debt deductions; potential additional loss from tax refunds	Loss of up to $12.7 million from ongoing bad debt deductions; additional loss of several millions from tax refunds	Loss of up to $12.7 million annually from ongoing bad debt deductions; potential additional loss from tax refunds
Local Government and Public Library funds (counties, municipalities, townships, and public libraries)			
Revenues	Potential loss from ongoing bad debt deductions; potential additional loss from tax refunds	Loss of up to $0.4 million from ongoing bad debt deductions; additional loss from tax refunds	Loss of up to $0.4 million annually from ongoing bad debt deductions; potential additional loss from tax refunds
Counties and transit authorities			
Revenues	Potential loss from ongoing bad debt deductions; additional loss from tax refunds	Loss of up to $3.2 million from ongoing bad debt deductions; additional loss from tax refunds	Loss of up to $3.2 million annually from ongoing bad debt deductions; potential additional loss from tax refunds

Note: The state or school district fiscal year runs from July 1 through June 30 and is designated by the calendar year in which it ends. For other local governments, the fiscal year is identical to the calendar year.

- Allowing certain bad debt deductions and sales tax refunds for unpaid private label credit account debts may reduce state revenue by up to $13.1 million per year on an ongoing basis. However, the initial fiscal cost of the bill could be several millions above that amount due to refunds from existing delinquent credit accounts that are declared “bad debts” after the enactment of the bill. The amount of refunds is uncertain.
- Bad debt deductions and refunds also reduce revenue from local permissive county and transit authority sales taxes (which share the same tax base as the state sales and use tax) which were imposed on relevant purchases.
- In the FY 2020-FY 2021 biennium, the state sales tax revenue loss would be shared by the state General Revenue Fund (GRF, 96.62%), the Local Government Fund (LGF, 1.68%), and the Public Library Fund (PLF, 1.70%). Funds deposited into the LGF and PLF are distributed to counties, municipalities, townships, and public libraries according to statutory formulas and decisions by county budget commissions.

Detailed Analysis

The bill allows sales tax vendors to deduct or apply for a refund of sales tax remitted for bad debts on private label credit cards used to make purchases from the vendor, even though the debt is charged off on the books of a credit account lender, as defined by the bill. The bill defines a private label credit account as a credit account that carries, refers to, or is branded with the name of a vendor. A typical private label credit card arrangement (though not all) might involve a retailer contracting with a bank or a lender to issue a card labelled with the retailer’s name; the card is used to make purchases at the store on credit; and the bank or the lender extends the credit, processes the credit purchases, bills customers, and remits payments, including sales tax, to the retailer in exchange for retaining a fee from the store. The retailer would then remit the sales tax to the state. If the customer does not pay the credit card balance, unpaid bills are thus a debt held by the bank or the lender, not the store.

Under current law, a sales tax vendor may claim the bad debt deduction or refund on the basis of sales tax the vendor previously remitted only if bad debts are charged off as uncollectible on the vendor’s books. The debt must have remained uncollected for at least six months, and the deduction may be obtained only for debts that have become worthless or uncollectible during the most recent sales tax reporting period and that the vendor may deduct for federal income tax purposes. The deduction is applied against the vendor’s sales tax remittances. A refund is available if a vendor’s bad debt for a reporting period exceeds the vendor’s taxable sales for that period. Thus, the bill expands an existing sales tax deduction for bad debts by allowing vendors to take a deduction or claim a refund of sales tax remitted for bad debts on accounts for private label credit cards even though the debt is charged off as uncollectible on the books of the vendor’s affiliates, the lender, or any other person (e.g., debt collector) that acquired the credit accounts or receivables arising from such accounts. The bill permits the deduction or refund claim without regard to the vendor reporting period during which the debt became worthless or uncollectible to the lender or another person. The bill also specifies that the bad debt deduction or refund applies only to bad debt arising from purchases at the retailer on the card logo (thus will not apply to other purchases if made on co-branded credit cards).

The bad debt deduction provision in the bill may decrease revenue from the sales and use tax by up to $13.1 million per year on an ongoing basis. However, the initial fiscal cost of the bill is likely to be above that amount due to the refund provision. Potential sales tax refunds from delinquent credit accounts that become bad debts are unknown and due to lack of data, LBO economists cannot rule out the potential for this revenue loss from refunds to be several tens of millions of dollars. Receipts from the state sales and use tax are deposited into the GRF. In the FY 2020-FY 2021 biennium, the state sales tax revenue loss would be shared by the state General Revenue Fund (GRF, 96.62%), the Local Government Fund (LGF, 1.68%), and the Public Library Fund (PLF, 1.70%).[1] Thus, the potential annual revenue loss to the GRF would be up to $12.7 million, while the combined reduction in tax revenue to the LGF and PLF would total $0.4 million per year. However, as mentioned above, the GRF and the local government funds will sustain additional revenue reductions totaling several millions of dollars due to the sales tax bad debt refund provision in the bill, most likely in the first year or two after the bill becomes effective. Potential revenue loss in FY 2020 would depend on the effective date of the bill.

The bill will also reduce revenue from local permissive county and transit authority sales taxes. Those local taxes share the same tax base as the state sales tax, and were imposed on taxable purchases made with the credit cards, and would be returned. At about 24.5% of state sales tax collections, the revenue reduction to permissive county and transit authorities' governments would total up to $3.2 million per year. However, the sales tax refund provision is likely to result in outsized revenue losses in the first years after enactment of the bill. All revenue estimates are subject to uncertainty, and actual revenue loss from the bill may be less than estimated.

This estimate is based on consumer data from a Federal Reserve Payments Study conducted in 2017, which provides net purchase transactions and dollar volume for private label credit card processors, and statistics on charge-off rates on consumer credit cards, also from the Federal Reserve. The estimate assumes that the sales tax vendor (retailer) does not issue or manage the private label card, or collect the payments from cardholders. The value of transactions for consumer private label credit accounts may have been up to $228 billion nationwide in 2017. Federal data were adjusted using Ohio's share of the gross domestic product for the retail trade industry. Other adjustments were made for transactions that may not give rise to sales tax collections. The charge-off rate on bad debts was assumed to be 3.5% on estimated Ohio transactions valued at about $6.4 billion, or potential total bad debts of up to $228 million.

Please note that the charge-off rate would vary with economic conditions. The last economic recession pushed up the charge-off rate to above 10% in 2010, but that rate has gradually come down since the recession; it has now drifted upward in the last couple of years. Thus, in years where the charge-off rate is higher than assumed above, the annual revenue loss would potentially increase. In addition, if the value of transactions on private label credit cards increases substantially from amounts estimated by the Federal Reserve, future tax revenue losses may be understated. Please note that the estimate above excludes transactions with

[1] H.B. 166 (operating budget act) for the biennium. Under codified law, the revenue loss would be shared by the GRF (96.68%), LGF (1.66%), and PLF (1.66%).

prepaid private label credit cards or debit cards on the likelihood of few or no defaults on those types of accounts, or transactions involving co-branded credit accounts. Finally, the bill may plausibly increase the likelihood that certain delinquent accounts may be determined to become worthless earlier than would otherwise be the case. This potential change in behavior of holders of bad debts is not taken into account in the fiscal note.

SB0188IN/zg