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OHIO LEGISLATIVE SERVICE COMMISSION

Office of Research and Drafting

Legislative Budget Office

S.B. 95
133rd General Assembly

Fiscal Note & Local Impact Statement

Click here for S.B. 95's Bill Analysis

Version: As Reported by House Ways and Means

Primary Sponsors: Sens. Peterson and Kunze

Local Impact Statement Procedure Required: Yes

Philip A. Cummins, Senior Economist, and other LBO staff

Highlights

- The bill excludes from gross receipts subject to the commercial activity tax (CAT) a megaproject supplier's receipts from the sale of tangible personal property to a megaproject operator; a "megaproject" is a large development project that satisfies certain criteria outlined in the bill. The bill also doubles the length (from 15 to 30 years) of existing incentives that may be available to operators and suppliers of megaprojects. Those incentives include job creation tax credits (JCTCs) and property tax exemptions under the enterprise zone (EZ) and community reinvestment area (CRA) programs.
    - Excluding certain receipts from taxation under the CAT would reduce GRF revenue by undetermined amounts. The amount of any revenue losses would depend on Ohio Tax Credit Authority (OTCA) decisions regarding awarding JCTCs to megaproject suppliers.
    - Enhancing the existing JCTC for a megaproject would reduce GRF revenue by undetermined amounts. As with the CAT exclusion, the size of any revenue decreases will be dependent on decisions by OTCA. Any revenue losses from these enhancements would occur 15 or more years in the future. The JCTC may be claimed against the personal income tax, the financial institutions tax, and the CAT.
    - The extension of property tax exemptions under the EZ or CRA programs with a megaproject would reduce revenue to schools and other local governments. As with state taxes, the revenue loss is undetermined. The amounts involved would depend on decisions made by municipalities and counties regarding awarding such exemptions, and would occur 15 or more years in the future.
- The bill makes a number of changes to property tax law that may affect revenues or costs for local governments. Such changes include: specifying that a tax increment

financing (TIF) minimum service payment obligation is a covenant running with the land and allowing tenants to file property tax complaints in certain circumstances.

- The bill adds real property tax exemptions to subject matter to be reviewed in the Tax Expenditure Report and by the Tax Expenditure Review Committee. These changes may result in cost increases, likely minimal, for the Department of Taxation and the Legislative Service Commission, and possibly in cost increases for county auditors and treasurers to provide information if requested.
- The bill reinstates exemption from sales and use tax for sales of investment bullion and coins, reducing GRF tax revenue by approximately $5.8 million per year and revenue of counties and regional transit authorities by about $1.5 million.
- The bill exempts from state and local use taxes certain watercraft purchased outside the state and seasonally stored, maintained, or repaired in Ohio, reducing state and permissive county and transit authorities' use taxes by an undetermined amount.
- The bill reduces the withholding tax rate for certain pass-through entities to 3%, starting with tax years that begin on or after January 1, 2023. Taxpayer liabilities would be unchanged, but a one-time revenue loss estimated at $31.6 million in FY 2023 would result from the timing of payments during the fiscal year.
- GRF tax revenue losses from the bill would be shared under codified law by the state General Revenue Fund (GRF, 96.68%), the Local Government Fund (LGF, 1.66%), and the Public Library Fund (PLF, 1.66%). Funds deposited into the LGF and PLF are distributed to counties, municipalities, townships, parks and other special districts, and public libraries.

Detailed Analysis

The bill makes a number of tax changes. The discussion of the tax changes below is organized into four categories: (1) changes related to a megaproject, (2) property tax changes, (3) sales tax changes, and (4) pass-through entity withholding tax changes. Tax changes affecting the sales tax, the commercial activity tax (CAT), the income tax, and the financial institutions tax primarily affect GRF revenue. Bill provisions that change the amount of revenue from these GRF tax sources alter distributions through the Local Government Fund (LGF, Fund 7069) and the Public Library Fund (PLF, Fund 7065) to units of local government and libraries. In codified law, both funds receive 1.66% of GRF tax revenue.[1]

Changes related to a megaproject

The bill authorizes several enhanced tax incentives for operators and certain suppliers of a "megaproject," defined by the bill as a large-scale development that meets certain investment or payroll thresholds. Before a business may qualify for any of these enhanced incentives, it must either operate a "megaproject" or sell tangible personal property to one. In

[1] In FY 2020 and FY 2021, the LGF receives 1.68% of GRF tax revenue and the PLF receives 1.70%, under provisions of H.B. 166 of the 133rd General Assembly.

order to qualify for the enhanced tax incentives, a business must apply to the Director of Development Services and be awarded a job creation tax credit (JCTC).

A megaproject is a development project that satisfies several conditions listed in the bill, including requiring "unique sites, extremely robust utility service, and a technically skilled workforce." Also, the megaproject operator must compensate employees at 300% of the federal minimum wage or more and either make at least $1 billion in fixed-asset investments in the project or create at the project at least $75 million in annual Ohio employee payroll. In addition to the megaproject's operator, certain suppliers of a megaproject are also eligible for the bill's enhanced incentives. Any business that sells tangible personal property to a megaproject may qualify for the enhanced incentives if it makes at least $100 million in fixed-asset investments in Ohio and creates at least $10 million in annual Ohio employee payroll that it maintains throughout the term of the JCTC. LSC's bill analysis provides the list of requirements to qualify for the enhanced tax incentives.

The bill indexes the fixed-asset investment thresholds and the Ohio employee payroll thresholds for inflation, measured by the increase in the gross domestic product deflator. The Tax Commissioner is required to certify new thresholds every five years starting in 2025, to the Director of Development Services and the Tax Credit Authority. This requirement will add to costs of the Department of Taxation, by an amount no more than minimal.

Job creation tax credit

The bill increases the maximum number of years a JCTC may be awarded by the Ohio Tax Credit Authority (OTCA) from 15 to 30 years for a business that is a megaproject operator or qualifying megaproject supplier. As a condition of continuing to receive annual compliance certificates during the term of the JCTC, the bill specifically requires the operator or supplier to meet the megaproject qualifications. If a megaproject supplier is awarded an enhanced JCTC, the bill authorizes the JCTC agreement to allocate all or a portion of the supplier's credit to the operator of the megaproject to which the supplier sells tangible personal property. Ohio law includes a clawback mechanism for beneficiaries of certain tax incentives that do not fulfill terms of their agreement. As with other noncompliant projects, OTCA may reduce the term or amount of a noncompliant megaproject operator's or supplier's JCTC or may require the operator or supplier to repay credits already claimed.

Commercial activity tax exclusion

Continuing law imposes the CAT based on a business's taxable gross receipts from sales in Ohio. CAT is remitted on an annual or quarterly basis depending on the amount of taxable gross receipts, if they exceed $150,000 in a calendar year. The bill authorizes a qualifying megaproject supplier to exclude, in calculating the supplier's taxable gross receipts, any gross receipts from the sale of tangible personal property to a qualified megaproject operator.

In connection with the bill's CAT exclusion, each qualified megaproject operator is required to annually furnish to the Tax Commissioner a list of its qualifying megaproject suppliers and to update that list as needed. The Commissioner in turn is required to issue a certificate to the operator and each listed supplier containing the names of the operator and each such supplier. A supplier may qualify for the bill's CAT exclusion only if the supplier is listed on a certificate issued to the operator and its suppliers.

Property tax exemptions

The bill authorizes counties and municipal corporations to grant up to a 30-year enterprise zone (EZ) or community reinvestment area (CRA) property tax exemption to the site of a megaproject or a site owned and operated by a qualifying megaproject supplier. Under current law, EZ and CRA exemptions are generally limited to no more than a 15-year term. If either exemption is granted to a qualifying site, the property owner is required to annually certify to the county or municipal corporation that the megaproject operator or supplier holds a JCTC annual compliance certificate. If the operator or supplier does not hold such a certificate, the county or municipal corporation may terminate the exemption beginning with the tax year in which the termination decision is made.

Fiscal analysis

The CAT exclusion of gross receipts from sales of a megaproject supplier to a megaproject operator would result in a loss of revenue to the GRF and other state funds (see below). Any such revenue losses could appear within a year or two. In contrast, other fiscal effects from the bill would not appear for at least 15 years.

A JCTC is a refundable tax credit[2] that may be taken against the state's income tax, CAT, or financial institutions tax. Thus, the potential doubling of the number of years available for a JCTC will reduce revenues from those state taxes. The magnitude of tax revenue losses is indeterminate as it would be dependent on action of the OTCA and various operators and qualified suppliers of a megaproject. LBO cannot rule out the possibility that GRF fiscal losses could be substantial.

CAT receipts are deposited into the GRF (85%), the School District Tangible Property Tax Replacement Fund (Fund 7047, 13%), and the Local Government Tangible Property Tax Replacement Fund (Fund 7081, 2%). Distributions from Fund 7047 and Fund 7081 are used to make reimbursement payments to school districts and other local taxing units, respectively, for the phase-out of property taxes on general business tangible personal property and for reductions of assessment rates on utility personal property. Any receipts in excess of amounts needed for such payments are transferred back to the GRF.

The enhancement of property tax exemptions under the EZ or CRA programs would reduce revenue to schools and other local governments. Statewide, school districts account for about 65% of taxes on real property, and other units of local government receive about 35%. The potential revenue loss to schools and local governments is also undetermined.

[2] The credit equals a percentage of additional annual Ohio employee payroll that a business generates at an Ohio-based project above a baseline amount of payroll generated at the site in the 12 months before the site was approved for the credit. To obtain a JCTC, a business is required to apply to and enter into an agreement with OTCA which sets out specific terms and conditions a project is required to meet as a condition of receiving the credit.

Property tax changes

Tax increment financing service payments and subsequent property owners

Under continuing law, minimum service payments by property owners to political subdivisions ensure sufficient funding to finance improvements made under tax increment financing (TIF) arrangements. A TIF is an economic development tool used by a county, municipality, or township to finance public infrastructure improvements and, in certain circumstances, residential rehabilitation. With a TIF, property owners are granted an exemption from property taxes on the increased value of property, but instead make minimum service payments to the subdivision. The minimum service payments fund public improvements related to property development, and the improvements are often financed by issuing debt backed by receipts from future minimum service payments. The minimum service payments are collected like property taxes.

The bill specifies that all TIF minimum service payment obligation agreements are enforceable against subsequent property owners, stating specifically that such an obligation shall be a covenant running with the land. Continuing law provides that such payments are to be considered taxes for all purposes, including for lien priority and collection, but does not specifically provide that such a payment is a covenant running with the land. This provision only applies to obligations arising from an agreement between a property owner and a local government. In other words, the bill clarifies that there are separate enforcement provisions for service payment obligations prescribed by statute and those obligations arising from an agreement between the property owner and a local government. The absence of such language in current law reportedly has resulted in difficulties obtaining financing, sometimes blocking or delaying development projects, particularly larger ones for which financing was sought from insurance companies. In practice, many service payment agreements address this issue by including such a clause.

This provision of the bill may result in cost savings to local governments by avoiding costly delays in securing financing for development projects, and may in some cases allow projects sought by local governments to be undertaken that might not be financed in the absence of the provision.

Filing of property tax complaints by tenants

The bill authorizes certain tenants to file property tax complaints and counter-complaints who are not allowed under current law to do so. Only property owners, their representatives, and political subdivisions may file complaints currently. The bill would add tenants of commercial or industrial property to those allowed to file a complaint if the lease requires the tenant to pay the entire amount of taxes charged against the property and the owner has authorized the tenant to file the complaint.

By permitting additional parties to file property tax complaints, the bill may result in lower tax valuations and lower revenues to local governments. The situation that this provision of the bill addresses apparently is sufficiently common that the potential number of such complaints could be significant. The magnitude of resulting revenue losses appears uncertain. The change plausibly could result in additional filings with BORs and perhaps also increase appeals to the Board of Tax Appeals (BTA). Increases in complaints would tend to increase costs

of BORs and BTA, to lengthen delays and backlogs in considering complaints, or both. The magnitude of cost increases or delays appears uncertain. BTA expenditures are funded by the GRF.

Tax years to which property tax complaint determinations apply

The bill specifies that a determination on a property tax complaint applies only to tax years occurring in the same triennial period in which the complaint is filed. This specification appears to codify current practice and to have no fiscal effect. For further information, please see the LSC bill analysis.

Property tax exemption for housing used by certain individuals

The bill authorizes a property tax exemption for housing used by individuals or families of individuals diagnosed with mental illness or substance use disorder. To qualify:

1. The owner of the property must be a tax-exempt 501(c)(3) organization, or a pass-through entity whose controlling member either is a 501(c)(3) organization or is owned by one or more 501(c)(3) organizations, for which providing such housing is a primary purpose.
2. At least one of those 501(c)(3) organizations must receive some of its funding from the Department of Mental Health and Addiction Services; a county board of alcohol, drug addiction, and mental health services; or a local continuum of care as defined by federal law.

In addition, the property must be either (a) used by the owner to provide such housing, (b) leased to individuals with mental illness or substance use disorder and used by them as housing, or (c) leased to a charitable institution and used by that institution for charitable purposes. The bill applies to tax year 2020 and thereafter, as well as to exemption applications pending on the bill's effective date.

This bill appears to clarify tax treatment of qualifying properties, codifying long-standing practice, and to have no fiscal effect.

Review of property tax exemptions

The bill requires that the Department of Taxation's Tax Expenditure Report (TER) include specified information on property tax exemptions, and that the Tax Expenditure Review Committee include property tax exemptions in its review and report. The TER is published by the Department every two years and is included in the Governor's Blue Book for each biennial main operating budget. The Tax Expenditure Review Committee, a joint legislative body, is to review every eight years all tax expenditures and, under the bill, all real property tax exemptions, and issue a report on this ongoing review every two years.

Tax Expenditure Report

The bill adds real property tax exemptions to the scope of subject matter required to be covered by the TER. Currently, the report covers tax exemptions that reduce the state's GRF revenue. It includes estimates of the magnitude of these fiscal effects in each fiscal year of the current and upcoming biennia. The bill adds to these reporting requirements (1) the aggregate true value of exempted real property in the previous tax year, and (2) GRF payments in the

previous calendar year to reimburse political subdivisions for exemptions subject to reimbursement.

The Department already publishes the information required by the bill. A report called Valuation of Exempted Real Property by Class of Property, by County (Table PE-2) lists such exemptions for real property. Another report, Taxable Value of Real Property Exempted by Tax Abatements by Class of Abatement, by County (Table PE-3) shows additional detail on tax abatements. These two tables provide information responsive to requirement (1) above; though the information shown is taxable values of the property rather than true values, the Department could easily calculate the true values from the information provided. A third report, Real Property Tax Relief, by County (Table PD-1) includes the information required by (2) above. The cost of including this information in the TER would likely be negligible, and the timing required by the bill is in line with publication dates of recent reports. The bill requires disaggregation of real property tax exemptions by the following classifications: charitable or public worship, public or educational, local economic development, and other. Departmental costs arising from its role in overseeing property taxes in the state are paid from the Property Tax Administration Fund (Fund 5V80).

Tax Expenditure Review Committee

The Tax Expenditure Review Committee consists of three members from each of the House of Representatives and Senate, and is chaired by the Tax Commissioner or the Commissioner's designee. The bill's requirement that the Committee review and report on all property tax exemptions would add to the amount of work required of members. Current law, unchanged by the bill, tasks the Legislative Service Commission (LSC) with assisting the Committee. That obligation in the past has been met without additional resources, but the bill's expansion of the Committee's purview could lead to increased demands on LSC. Any fiscal effect on LSC would likely be minimal, though it would depend on the volume of assistance required and the timing of any related deadlines. LSC is funded almost entirely from the GRF.

The bill specifies that if the Committee requests information that it requires to do its job, county auditors and treasurers are to provide information in their possession. This requirement may increase costs of these local government officials.

Sales tax changes

Sales tax exemption for investment bullion and coins

The bill reinstates the sales and use tax exemption for sales of investment bullion and coins. The exemption was repealed in H.B. 166 of the 133rd General Assembly, the biennial budget bill. The exemption is expected to reduce GRF tax revenue by about $5.8 million per year and revenue from permissive sales and use taxes of counties and regional transit authorities by $1.5 million. Any FY 2021 revenue loss for the GRF would likely be much less than the full-year amount, as nearly half of the fiscal year has passed and the provision does not take effect until the first day of the month following the effective date of the bill.

Use tax exemption for certain watercraft

The bill exempts from state and local use taxes certain watercraft. The qualifying watercraft has to meet the following conditions: (1) the owner paid sales or use tax on the watercraft to another state or under R.C. section 5739.027, unless the watercraft is used and

titled or registered in a jurisdiction that does not impose a sales or use tax or similar excise tax on the ownership or use of the watercraft, (2) the watercraft is in Ohio only for storage and maintenance, (3) the watercraft is not used or stored in Ohio in May through September of the year, and (4) the watercraft is not required to be registered in Ohio under section 1547.54 of the Revised Code.

In general, use tax is imposed on items purchased outside Ohio and used and stored in the state if no Ohio sales tax was paid.[3] No information is available on the potential use tax avoidance by out-of-state boat owners or Ohio marinas or watercraft maintenance and repair shops; LBO has not been able to obtain relevant data to estimate state and permissive county and transit authority sales tax revenue losses that would result from the bill. However, LBO also believes that such revenue decreases may be relatively small, primarily because language in the bill requires that the watercraft owner would have already paid state taxes, where required, on the purchase of an exempted watercraft.

This assessment is based on the assumption that most watercraft potentially liable for Ohio use tax was purchased in a neighboring state, all of which have higher state sales and use tax rates than Ohio's rate of 5.75%, so any additional liability for out-of-state watercraft owners would likely be for use taxes for permissive local taxes.[4] When use tax is due on the purchase of motor vehicles or watercraft out of state, or for storage and use in Ohio, a credit allowance is given for the amount of sales and/or use tax legally required to be paid to another state. When the amount of tax paid to another state is established, it is to be deducted from the total amount of use tax due Ohio. If the credit equals or exceeds the Ohio use tax due, no additional tax payment is required; if not, the taxpayer is required to pay additional tax at the combined state and local sales tax rate on the purchase. However, compliance with use tax law is generally low, particularly for tangible property not required to be titled or registered with government agencies.

Sales and use taxation of watercraft

On January 1, 2000, Ohio sales tax law on personal watercraft changed. All personal watercraft sold on or after January 1, 2000, is required to be titled and sales/use tax required to be paid to the local clerk of courts, unless the purchaser is entitled to claim exception or exemption.[5] Prior to January 1, 2000, only dealer sales of personal watercraft were subject to Ohio sales/use tax, and the tax was required to be collected by the dealer and remitted directly to the Treasurer of State, not to the clerk of courts. Nondealer sales of personal watercraft made prior to January 1, 2000, were not subject to the sales/use tax since they were not

[3] This use tax requirement applies whether or not the tangible personal property is required to be registered or titled.

[4] State sales and use tax rates are 7% for Indiana, and 6% for Pennsylvania, Michigan, West Virginia, and Kentucky; however, Indiana, Michigan, and Kentucky do not have local sales taxes, unlike Ohio, so the combined state and local sales and use tax rate in certain Ohio counties may be higher than the sales tax rates in those states.

[5] For example, for purchases for resale or interstate commerce, purchases by political subdivisions and certain nonprofits, and transfers with no consideration (such as gifts).

required to be titled and they qualified for the "casual sale" sales and use tax exemption. According to the Ohio Administrative Knowledge System, in FY 2018 and FY 2019, state sales and use tax revenues from watercraft sales totaled $21 million and $23 million, respectively.

Titling of watercraft and outboard motors

According to R.C. sections 1548.01 and 1548.03, the following items require an Ohio certificate of title: an outboard motor of ten horsepower or greater, a watercraft 14 feet or greater in length, and a watercraft less than 14 feet in length with a permanently affixed mechanical means of propulsion of ten horsepower or greater (e.g., personal watercraft such as Jet Ski, SeaDoo, etc.). Boats with out-of-state titles must have an Ohio title written before the boat can be registered in Ohio. A number of watercraft are exempt from the titling requirement, including canoes and kayaks, boats from other countries, motors less than ten horsepower, and vessels documented by the United States Coast Guard.

Pass-through entity withholding tax rate reduction

The bill reduces withholding tax rates to 3% on certain pass-through entities (PTEs). PTEs include partnerships, S corporations, and limited liability companies. PTEs "pass through" the liability to pay tax on their income to their investors, thereby avoiding a second layer of taxes at the business entity level. Although income taxes are not owed by the PTEs themselves but are due instead from the investors in the PTEs, payments referred to as withholding taxes are made by some PTEs for which the investors in those entities can claim refunds or credits against taxes owed. This withholding tax helps reduce tax avoidance.

For certain out-of-state investors in PTEs that are not individuals or are various financial institutions and some others, the withholding tax rate falls from 8.5% to 3%.[6] For out-of-state investors in PTEs who are individuals and for trusts with beneficiaries who are out-of-state individuals, the withholding tax rate falls from 5% to 3%. The 3% rate equals the rate on taxable business income.

No state personal income taxpayer's tax liability is changed by the bill. Taxpayers are eligible for refunds of withholding tax paid in excess of tax due. However, timing differences between when the tax is withheld and when the refunds are paid will result in a one-time tax revenue loss from the reduction in withholding tax rates that LBO estimates at $31.6 million in FY 2023. This estimate is based on data provided by the Department of Taxation. The loss occurs because refunds (or final settlements) are paid in arrears, for the prior tax year, so adjust more slowly than cash flows from changes in the withholding tax. This remains the case even if the taxpayer owes no tax on the income for which withholding tax was paid. For example, a taxpayer eligible to deduct business income from the PTE that totals less than the maximum

[6] This part of the bill, amending R.C. 5733.41, applies with certain exceptions to non-Ohio domiciled entities including other PTEs; financial institutions; financial holding companies; bank holding companies; savings and loan holding companies; persons directly or indirectly owned by one or more financial institutions, financial holding companies, bank holding companies, or savings and loan holding companies; persons that solely facilitate or service securitizations by these entities; certain affiliates of insurance companies; and estates and trusts subject to the personal income tax.

allowed deduction of $125,000 for a married taxpayer filing separately and $250,000 for all other taxpayers would owe no tax on that income.

How such a loss would occur can be illustrated in the following way. Estimated withholding tax payments are due quarterly from PTEs affected by the bill, in the month following the end of the quarter. The bill specifies that the changes apply to qualifying taxable years beginning on or after January 1, 2023. This implies that reductions in the withholding tax will start in April 2023, for the January-March quarter. If, for example, for a specific investor the April 2023 withholding tax payment and each subsequent quarterly payment is reduced by $100, that investor's refund for tax year 2022, assumed to be paid in the first half of 2023, would be unaffected by the change. The change in the April withholding tax payment, for the 2023 first quarter, would not affect the investor's refund until 2024. In FY 2023 the state would receive $100 less for this investor, from the April withholding tax payment, and with the refund unchanged in that year, would incur a net revenue loss of $100. In FY 2024 and thereafter, assuming the change per quarter continues to be a reduction of $100, the state would receive $400 less for this investor, from the July, October, January, and April withholding tax payments, and would refund $400 less, for no net revenue loss.

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