Ohio Legislative Service Commission

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Fiscal Note & Local Impact Statement

Bill: H.B. 334 of the 131st G.A.

Date: February 24, 2016

Status: As Reported by House Ways and Means

Sponsor: Rep. Buchy

Local Impact Statement Procedure Required: Yes

Contents: Exempts memberships to gyms and recreational facilities operated by 501(c)(3) nonprofit organizations from the sales and use tax

State Fiscal Highlights

STATE FUND	FY 2016	FY 2017	FUTURE YEARS
General Revenue Fund			
Revenues	- 0 -	Loss of $6.7 million	Loss of $7.3 million
Expenditures	- 0 -	- 0 -	- 0 -

Note: The state fiscal year is July 1 through June 30. For example, FY 2016 is July 1, 2015 – June 30, 2016.

- The bill reduces the sales and use tax base, and thus decreases sales tax revenue. The actual revenue loss would be dependent on rate of membership sales growth or decline at the affected establishments.
- The majority of the estimated loss would be due to memberships to nonprofit fitness and recreational centers such as YMCA and YWCA facilities.
- State sales tax receipts are deposited into the GRF which would bear the majority of the revenue loss.

Local Fiscal Highlights

LOCAL GOVERNMENT	FY 2016	FY 2017	FUTURE YEARS
Counties, municipalities, townships, and public libraries (LGF and PLF)			
Revenues	Loss of $90,000	Loss of $260,000	Loss of $260,000
Expenditures	- 0 -	- 0 -	- 0 -
Counties and transit authorities			
Revenues	Loss of $0.6 million	Loss of $1.9 million	Loss of $1.9 million
Expenditures	- 0 -	- 0 -	- 0 -

Note: For most local governments, the fiscal year is the calendar year.

- Any reduction to GRF tax receipts would also reduce the amount distributed to the Local Government Fund (LGF) and Public Library Fund (PLF) as these local funds receive distributions from GRF tax receipts.
- The bill reduces revenue from permissive county and transit authority sales taxes. Those taxes share the same base as the state sales and use tax.

Detailed Fiscal Analysis

The bill exempts sales of memberships to physical fitness facilities and recreation and sports clubs from the sales and use tax if the organization is exempt from taxation under section 501(c)(3) of the Internal Revenue Code. Memberships to all physical fitness facilities and recreation and sports clubs were originally subjected to the sales and use tax in 1992 by Am. Sub. H.B. 904 of the 119th General Assembly. The exemption would begin on July 1 after the effective date of the bill. The Ohio Revised Code[1] specifies physical fitness facilities and recreation and sports clubs to include athletic clubs, health spas, gymnasiums, aviation clubs, gun or shooting clubs, yacht clubs, card clubs, swimming clubs, tennis clubs, golf clubs, country clubs, riding clubs, amateur sports clubs, or similar organizations.

The majority of these types of businesses fall under the North American Industry Classification System (NAICS) code of 7139, which is labeled "Other Amusement/ Recreation Industries." Based on the 2012 Economic Census,[2] there are two subsets of this classification that include a substantial number of Ohio businesses which are exempt from federal taxation: (1) "fitness and recreational sports centers" and (2) "golf courses and country clubs." Additionally, there are a small number of Ohio establishments which are exempt from federal taxation that are classified under a third subset labeled "other miscellaneous amusement and recreation services."[3] Based on a review of tax returns[4] from various nonprofit golf and country clubs in Ohio, the majority appear to be exempted from federal taxation under sections other than 501(c)(3) and therefore would not be affected by the bill.[5] For the purposes of our

[1] R.C. 5739.01(MM) and (NN).

[2] The U.S. Census Bureau conducts the Economic Census every five years. Not all survey results of the 2012 version have yet been released.

[3] The detailed NAICS codes for the subsets referenced in this section are 713940 (fitness and recreational sports centers), 713910 (golf courses and country clubs), and 713990 (other miscellaneous amusement and recreation services).

[4] Organizations that are exempt from federal taxation must make their annual returns available for public inspection and copying.

[5] The exemption under section 501(c)(3) is reserved for nonprofit charitable organizations only. Other tax-exempt organizations may qualify under sections 501(c)(4) through 501(c)(9) of the Internal Revenue Code. Most exempted golf and country clubs qualify under section 501(c)(7).

estimates, we limited our use of the Economic Census data to Ohio nonprofit fitness and recreational sports centers, most of which classify under section 501(c)(3) and would be affected by the bill.

Fiscal effects

According to the Economic Census, Ohio nonprofit fitness and recreational sports centers generated approximately $243 million of total receipts in 2012. During the same year, memberships[6] were estimated to be 45%[7] of total receipts at all similarly classified establishments nationwide. If Ohio nonprofits have a similar percentage of sales from memberships, the relevant tax base in 2012 was approximately $109 million. Additional revenues from nonprofit gym and recreational center memberships classified in the "other miscellaneous" section adds $3.5 million to the 2012 tax base, bringing the total to approximately $113 million. Based on historical data and projections by Global Insight (a private economic forecasting firm), nominal consumer spending growth in recreation services between 2012 and 2016 nationally is estimated to be about 4% annually. Based on that estimate, the tax base would be $132 million in 2016.

Applying a 5.75% state sales tax to this base, annual state revenue lost from nonprofit fitness and recreational centers would be approximately $7.6 million. Permissive county and transit authority sales taxes share the same tax base as the state sales tax, and are approximately 24.5% of state sales tax revenues. Thus, the annual revenue loss to local governments from county and transit authority sales and use taxes on nonprofit gym and recreational center memberships would be approximately $1.9 million. Receipts from the state sales and use tax are deposited into the GRF. Under permanent law, a portion of GRF tax receipts is subsequently transferred to the LGF and the PLF. In the current biennium, the LGF and the PLF receive 1.66% and 1.70% of GRF tax revenue, respectively.[8] Therefore, the estimated annual revenue loss to each of these local funds would be approximately $130,000.

Sales and use tax payments are made monthly based on the preceding month's sales receipts. The changes made by the bill are to begin July 1 after the effective date of the bill, so the majority of the state revenue effect would first influence sales tax receipts in August 2016. For this analysis, we assume the bill takes effect on July 1, 2016, which would affect 11 of 12 monthly sales tax receipts in state FY 2017. State FY 2018 would be

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[6] As categorized by U.S. Census Product Lines Statistics.

[7] Based on other estimates and input from YMCA executives, the actual percentage of revenues from memberships at nonprofit gym and recreational centers may be higher. The percentage estimated by the Census may be low due to nonfitness and recreational centers that misclassified themselves in the NAICS category and do not offer fitness and recreational sports center memberships. This discrepancy should not affect the estimate of the size of the tax base to be changed by this bill.

[8] H.B. 64, the current operating budget act, temporarily increases the PLF share to 1.70% for FYs 2016 and 2017. In the absence of future action by the General Assembly, the PLF share will return to 1.66% for FY 2018 and beyond.

the first complete year affected by the bill. For local governments, we assume the fiscal year is the calendar year. Transfers from the GRF to the LGF and PLF are made based on the previous month's tax receipts. Sales taxes levied by counties and transit authorities are collected by the state and transferred to the local authorities within 45 days after the end of the month. Therefore, local governments and transit authorities' revenues would be impacted in four months of local FY 2016 and FY 2017 would be the first complete year affected by the bill.

Limitations of the data used for this analysis could cause estimated losses to be different than projected here. The Economic Census provides data on revenue from businesses that are exempt from federal taxation, but does not provide information about the type of exemption (e.g., 501(c)(3)), which determines applicability of this bill. Additionally, the Census data is based on the NAICS system, in which businesses self-classify themselves based on industry. The Census data used in the analysis likely captures some businesses that will not be affected by the bill, either because they are exempt from federal taxation under a section of the Internal Revenue Code other than 501(c)(3), or they were incorrectly classified by industry.

Similarly, there are likely some businesses that are a "physical fitness facility" or a "recreation and sports club" as defined by current Ohio law and also qualify as a 501(c)(3) organization and therefore could be affected by the bill, but are not counted here due to the limitations of the Census data. Based on our review of some Ohio nonprofit business tax returns, included in this category are many amateur sports clubs,[9] some swimming clubs, and even an occasional hunting club. However, in order to be impacted, an organization would also have to have ownership or long-term control of the facilities used by its members, have revenues from memberships (not program fees or facility rentals), and currently be collecting sales tax with the payment of membership fees or dues. Given all this, it seems reasonable to assume the fiscal impact from the bill as related to this group of establishments is likely to be minimal, and the net effect of NAICS misclassifications on the estimates to be negligible.

Other issues affecting the estimation of the fiscal effect of the bill are sales growth rate assumptions and the possible indirect effects of a price change. Since the Economic Census is done only every five years, and even some data from the most recent, in 2012, is not yet available, assumptions about membership sales growth had to be made to apply this data to FY 2016 and beyond. The 4% nominal annual rate of growth for sales in the sector was estimated by Global Insight, but how sales have actually changed since 2012, and especially how they change in the future will affect the actual revenue loss.

[9] The largest of these by revenue were the Ohio High School Athletic Association and the intercollegiate Mid-American Athletic Conference, but the majority are much smaller, local youth leagues.

In regard to the indirect effects of the bill, it is possible that the lower effective cost to consumers of the memberships at the affected establishments could stimulate movement in memberships from similar for-profit entities to nonprofit competitors. It is also possible that for-profit competitors will lower their rates in some cases to maintain the same market share. Either situation would result in additional sales tax revenue lost, however the amount lost would be dependent on the price elasticity of demand for the memberships, and relevant cross-price elasticities of demand, estimates of which are difficult to determine.

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