Ohio Legislative Service Commission

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Office of Research and Drafting

Legislative Budget Office

H.B. 223
134th General Assembly

Fiscal Note & Local Impact Statement

Click here for H.B. 223's Bill Analysis

Version: As Introduced

Primary Sponsor: Rep. Hillyer

Local Impact Statement Procedure Required: Yes

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Highlights

Fund	FY 2022	FY 2023	Future Years
State General Revenue Fund			
Revenues	Potential loss from ongoing bad debt deductions; potential additional loss from bad debt carryforwards	Loss of up to $14.5 million from ongoing deductions; additional loss from carryforwards	Loss of up to $14.5 million per year from ongoing deductions; additional loss from carryforwards
Local Government and Public Library funds (counties, municipalities, townships, and public libraries)			
Revenues	Potential loss from ongoing deductions and from bad debt carryforwards	Loss of up to $0.5 million from ongoing deductions; additional loss from carryforwards	Loss of up to $0.5 million per year from ongoing deductions; additional loss from carryforwards
Counties and transit authorities			
Revenues	Potential loss from ongoing deductions and from bad debt carryforwards	Loss of up to $3.7 million from ongoing deductions; additional loss from carryforwards	Loss of up to $3.7 million per year from ongoing deductions; additional loss from carryforwards

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 for unpaid private label credit account debts may reduce state sales tax revenue by up to $15.0 million per year.
- Bad debt deductions 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 2022-FY 2023 biennium, the state sales tax revenue loss would be shared 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, and public libraries according to statutory formulas and decisions by county budget commissions.

Detailed Analysis

The bill allows sales tax vendors to deduct 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. Under current law, a sales tax vendor may claim a 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 deduction applies to debt charged off as uncollectible on the books of lenders on or after July 1, 2021.

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.

A vendor may claim the deduction in current law for debt that has 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. Thus, the bill expands an existing sales tax deduction for bad debts by allowing vendors to take a deduction 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 expanded bad debt deduction without regard to the vendor reporting period during which the debt became worthless or uncollectible relative to the period between a vendor's returns.[1] Unlike the existing deduction for a vendor's own bad debts, if the bill's expanded deduction exceeds the vendor's taxable sales

[1] For the debt to be deductible under Ohio's sales tax, the debt must be deductible for federal income tax purposes as determined with respect to the lender.

for the month due to the lender's bad debts, the sales tax vendor may carry forward and apply the difference to a future tax liability. There is no limit on the number of carryforward months.

Fiscal effect

The bad debt deduction may decrease revenue from the sales and use tax by up to $15.0 million per year on an ongoing basis. Receipts from the state sales and use tax are deposited into the GRF. Under codified law, the revenue loss would be shared by the GRF (96.68%), Local Government Fund (LGF, 1.66%), and Public Library Fund (PLF, 1.66%). Thus, the potential annual revenue loss to the GRF would be up to $14.5 million, while the combined reduction in tax revenue distributed to the LGF and PLF would total $0.5 million per year. 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 $3.7 million per year. The GRF, the local government funds, and county and transit authorities will sustain additional revenue reductions due to accumulated prior bad debts that may be deducted from current sales tax payments by vendors and possibly carried forward against future vendor tax liability, if the bill's expanded deduction exceeds the vendor's taxable sales for the month. LBO has no data on the total amount of qualifying existing bad debts on lenders' books. Potential revenue loss in FY 2022 would depend on the effective date of the bill.

This estimate is based on consumer data from a Federal Reserve Payments Study conducted in 2018, 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 $239 billion nationwide in 2018. 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 4.0% on estimated Ohio transactions valued at about $6.5 billion, or potential total bad debts of up to $260 million. Applying the state sales tax rate of 5.75% to that amount yields roughly $15 million.

Please note that the charge-off rate would vary with economic conditions. The 2008-2009 economic recession pushed up the charge-off rate to above 10% in 2010, and the rate gradually came down afterwards. Thus, in years where the charge-off rate is higher than assumed above, the annual revenue loss would potentially increase. Alternatively, if the charge-off rate is less, the estimated annual revenue loss would decrease. Also, if the value of transactions on private label credit cards increases substantially from amounts estimated by the Federal Reserve in 2018, tax revenue losses may be understated. Please note that the estimate above excludes private label retail credit cards transactions made by businesses. The estimation also excludes consumer transactions made with 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.

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