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H.B. 157
134th General Assembly

Bill Analysis

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Version: As Passed by the House

Primary Sponsors: Reps. Jordan and Edwards

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SUMMARY

- Modifies and extends, until December 31, 2021, a temporary municipal income taxation rule for employees who are working from home due to COVID-19.
- Temporarily shields employers from certain penalties associated with withholding municipal income tax as long as the employer withholds such tax for an employee's principal place of work.

DETAILED ANALYSIS

Municipal income taxation during the COVID-19 pandemic

The bill modifies and extends, until December 31, 2021, a temporary rule governing the municipal income taxation of employees who are working at a temporary worksite – including their home – due to the COVID-19 pandemic.¹

Under the temporary rule, if an individual has to work at a temporary worksite because of the COVID-19 pandemic, that employee is still considered to be working at his or her regular place of employment, or principal place of work. This treatment affects which municipality the employer must withhold income taxes for, which municipality may tax the employee's pay, and whether and how much of the employer's own income is subject to a municipality's income tax.

Temporary rule extension

The temporary rule, by its own terms, expires 30 days after the end of the Governor's COVID-19 emergency declaration.² Under recently enacted provisions of S.B. 22 of the 134th

¹ Section 1. The temporary rule was enacted in Section 29 of Am. Sub. H.B. 197 of the 133rd General Assembly.

² The current state of emergency was declared in Executive Order 2020-01D, issued on March 9, 2020.

General Assembly, the General Assembly could end that emergency declaration on or after that act's effective date (June 23, 2021) by adopting a concurrent resolution to do so or, if the General Assembly does not act to extend the declaration, the emergency is scheduled to end by operation of law on July 23, 2021.³ Alternatively, if the Governor rescinds the declaration before that date, the rule could end sooner.

The modified provision (which has a 90-day effective date that would fall after July 2021) states that the emergency rule applies until December 31, 2021. In addition, the bill removes the requirement in the current rule that the offsite work arrangement be required by the employer as a result of the emergency declaration. Under the bill, the rule would apply to employees who are working at another location "in response to the COVID-19 pandemic," without regard to whether or not the employer requires the employee to do so.

Effect of temporary rule on tax withholding and tax liability

Under the temporary rule, considering an employee's income to be earned at their principal place of work potentially allows the employer to avoid withholding taxes for that employee in the municipality where the employee's temporary worksite is located and prevents the employer from becoming subject to that municipality's income tax. It also potentially prevents the employee from being taxed on that income by that municipality, unless the employee is a resident of that municipality. (Resident municipalities may tax individual taxpayers on their entire income, regardless of where the income is earned.⁴) The full effect of the current provision is not clear, however, because courts have generally found that a municipality cannot tax a nonresident's income that is not earned in that municipality and that taxpayers are entitled to a refund of tax withheld on that income.⁵ This prohibition arises from due process protections – the Ohio Supreme Court has held that a municipal corporation taxing nonresident income may violate constitutional due process if there is no "fiscal relation" between the tax and the protections, opportunities, and benefits provided by the taxing municipality to the nonresident (e.g., police and fire protection).⁶

The bill states that, beginning on January 1, 2021, the temporary rule applies only for the purposes of municipal income tax withholding and the situsing of an employer's net profits, and not for the purpose of determining the employee's actual tax liability. In effect, the bill requires municipalities to approve an employee's request for a refund of taxes withheld under the temporary rule on and after January 1, 2021, on the due process basis described above.⁷

³ Section 3 of S.B. 22 of the 134th General Assembly.

⁴ R.C. 718.01(A)(1)(b), not in the bill.

⁵ See, e.g., *Miley v. City of Cambridge*, No. 96 CA 44, 1997 Ohio App. LEXIS 3243 (5th Dist. June 25, 1997) (granting refund where city ordinance was held unconstitutional because it taxed nonresidents for work outside the city if the employer's principal place of work was in the city).

⁶ *McConnell v. Columbus*, 172 Ohio St. 95, 99-100 (1961).

⁷ Division (D) of Section 29 of H.B. 197 of the 133rd General Assembly; Section 4.

The bill further provides that its modifications to the temporary rule are not intended to affect the interpretation of the rule to taxes withheld in 2020. The issue of whether municipalities are required to approve requests for “due process” refunds of taxes withheld under the temporary rule is already the subject of litigation.⁸

If an employee requests a refund of any taxes withheld under the temporary rule, the bill also prohibits a municipal tax administrator from requiring the employer to provide any documentation to support the refund claim, other than a statement verifying the number of days the employee worked at the employee’s principal place of work and that the employer did not refund any withheld taxes directly to the employee.⁹

Employer liability

The bill also provides that, if an employer withheld municipal income tax to an employee’s principal place of work between March 9, 2020 (when the temporary rule took effect), and December 31, 2021, a tax administrator may not assess taxes, penalties, or interest against that employer for the failure to withhold those taxes to the municipality in which the employee actually worked or for the failure to situs the employee’s wages to that municipality for purposes of the employer’s net profit tax liability. This “safe harbor” applies regardless of whether the employee worked in the other municipality because of the COVID-19 pandemic or by order of their employer.¹⁰

Under continuing law, a tax administrator may assess taxes, penalties, and interest against an employer that improperly withholds tax from an employee’s income or that improperly pays its municipal net profits tax.¹¹

Preexisting law governing transitory employees

Under continuing law, a nonresident employee may work in a municipality for up to 20 days per year without the employer becoming subject to that municipality’s tax withholding requirements and the employee becoming subject to that municipality’s income tax. And, if an employee does not exceed the 20-day threshold, that employee’s pay is not counted toward the business’s payroll factor, one of three factors – along with property and sales – that determines whether, and the extent to which, an employer’s own income is subject to the municipality’s tax on net profits.¹²

⁸ See, e.g., *Buckeye Institute v. Kilgore*, Franklin County Court of Common Pleas Case No. 20-CV-4301 (2020).

⁹ Section 5.

¹⁰ Section 3.

¹¹ R.C. 718.27, not in the bill.

¹² R.C. 718.01(C)(16) and (17), 718.011, 718.02, and 718.82, not in the bill.

HISTORY

Action	Date
Introduced	02-25-21
Reported, H. Ways & Means	05-19-21
Passed House (63-31)	05-26-21
