Ohio Legislative Service Commission

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Fiscal Note & Local Impact Statement

Bill: H.B. 473 of the 131st G.A.

Date: May 2, 2016

Status: As Introduced

Sponsor: Rep. Amstutz

Local Impact Statement Procedure Required: Yes

Contents: To permit certain bad debt deductions and refunds for sales tax vendors and cigarette tax wholesalers, to allow employees of affiliated entities to be counted for purposes of the InvestOhio income tax credit, and to require voter approval for a county's utilities service tax

State Fiscal Highlights

STATE FUND	FY 2017	FY 2018	FUTURE YEARS
General Revenue Fund			
Revenues	Loss of up to $13.1 million from ongoing bad debt deductions and income tax credit; additional loss of several millions of dollars from the sales tax refund provision	Loss of up to $13.1 million from ongoing bad debt deductions and income tax credit; additional loss of several millions of dollars from the sales tax refund provision	Loss of up to $13.6 million annually from ongoing bad debt deductions and income tax credit
Expenditures	- 0 -	- 0 -	- 0 -

Note: The state fiscal year is July 1 through June 30. For example, FY 2018 is July 1, 2017 – June 30, 2018.

- The bill allows certain bad debt deductions and refunds for unpaid private label credit card debts. The bad debt deduction for sales tax vendors may potentially decrease revenue from the sales and use tax by up to $9.3 million per year on an ongoing basis. However, the initial fiscal cost of the bill is likely to be several millions above that amount due to refunds from bad debts realized before the enactment of the bill. The amount of refunds is uncertain.
- The bill allows certain bad debt deductions and refunds of cigarette excise taxes remitted by wholesalers. This provision will decrease cigarette tax receipts by an indeterminate amount, between $1.7 million and $3.3 million per year.
- Under the bill, counting employees of affiliated entities would allow additional firms and their investors to qualify for the InvestOhio personal income tax credit, and thus would reduce revenue from the personal income tax. The reduction in personal income tax receipts is likely to be less than $1 million per year in FY 2017 and FY 2018, but may grow in future years.

- State sales and use tax, personal income tax, and cigarette tax receipts are deposited in the GRF which would bear the majority of the revenue loss. 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 funds receive distributions from GRF tax receipts.

Local Fiscal Highlights

LOCAL GOVERNMENT	FY 2016	FY 2017	FUTURE YEARS
Counties, municipalities, townships, and public libraries (LGF and PLF)			
Revenues	Potential loss	Potential loss up to $0.5 million from ongoing bad debt deductions and income tax credit; additional loss from the sales tax refund provision	Potential loss up to $0.5 million annually from ongoing bad debt deductions and income tax credit
Expenditures	- 0 -	- 0 -	- 0 -
Counties and Transit Authorities			
Revenues	Potential loss	Loss of up to $2.3 million from ongoing bad debt deductions; additional loss from the sales tax refund provision	Loss of up to $2.3 million annually from ongoing bad debt deductions; additional loss from the sales tax refund provision
Expenditures	- 0 -	- 0 -	- 0 -
Cuyahoga County			
Revenues	Potential loss of up to $80,000 for cigarette tax from bad debt deduction	Potential loss of up to $80,000 for cigarette tax from bad debt deduction	Potential loss of up to $80,000 for cigarette tax from bad debt deduction
Expenditures	- 0 -	- 0 -	- 0 -

Note: For most local governments, the fiscal year is the calendar year. The school district fiscal year is July 1 through June 30.

- The sales tax provisions in the bill reduce revenue from local permissive county and transit authority sales taxes. Those taxes share the same base as the state sales and use tax.
- Receipts from the state sales and use tax, income tax, and cigarette tax are deposited in the GRF. A share of GRF tax revenues is distributed under permanent law to the LGF and PLF. Thus, any reduction to GRF tax receipts would also reduce the amount distributed to the LGF and PLF.
- The bad debt deduction or refund for cigarette wholesalers may decrease Cuyahoga County cigarette tax receipts by up to $80,000 annually.
- Requiring voter approval for county utilities service taxes has no direct fiscal effect on counties.

Detailed Fiscal Analysis

The bill makes changes pertaining to the sales tax, cigarette tax, and individual income tax, and also alters the procedure for a county levy on utility services tax.

Sales tax deductions and refunds for bad debts on private label credit cards

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 card lender or other persons. The deduction applies to bad debts charged off on or after July 1, 2014. The bill defines a private label credit card as a charge card, credit card, or charge account bearing a vendor's name or logo. A typical (but not all) private label credit card arrangement might involve a retailer contracting with a bank 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 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; and the retailer remits 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, 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. 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 that acquired the card 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 bad debt deduction provision in the bill may decrease revenue from the sales and use tax by up to $9.3 million per year on an ongoing basis. However, the initial fiscal cost of the bill is likely to be several millions above that amount due to the refund provision. Potential sales tax refunds for bad debts realized after July 1, 2014, but prior to the enactment of the bill, are unknown and likely to be several millions of dollars. This estimate is based on consumer data from a Federal Reserve Payments Study published in 2013, 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, issues the cards, or collects the payments from cardholders. The Federal Reserve estimated the value of transactions for consumer private label credit cards accounts at about $170 billion nationwide in 2012. Federal data were adjusted using Ohio's share of the Gross Domestic Product for the retail trade industry. The charge-off rate on bad debts was assumed to be 3.5%. 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 over the last few 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 the amount estimated by the Federal Reserve in 2012, future tax revenue losses may be understated. Please note that the estimate above excludes transactions 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 cards. 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.

Cigarette tax and other tobacco products collections credited for bad debts deduction

H.B. 473 would permit wholesale dealers of cigarettes and other tobacco products to apply to the Tax Commissioner for a refund of the net value of cigarette and tobacco taxes that are part of the bad debt of the dealer. However, TAX could not refund any amount for bad debt unless the dealer has charged off the bad debt on its books as worthless or uncollectible, and claimed it as a federal income tax deduction. The refund request and the supporting evidence must be filed within three years after the date the bad debt became uncollectible. The refund would be payable from receipts of the state tax, and, if applicable, from Cuyahoga County cigarette tax. In lieu of granting a refund, TAX may allow a wholesale dealer to claim a credit of the amount of refundable tax on the return for the period during which the tax became refundable or against the purchase of tax stamps or payment of other tobacco products tax.

This provision will reduce annual state cigarette and other tobacco product tax receipts by an indeterminate amount, likely to be between $1.7 million and $3.3 million, according to the Department of Taxation. If refunds are applicable to the Cuyahoga County cigarette tax, the potential reduction in revenue for the county may be up to $80,000 per year.

Changes to InvestOhio Program

InvestOhio provides a nonrefundable personal income tax (PIT) credit to investors that provide cash to acquire an ownership interest in a qualifying Ohio firm. Current law requires that the firm does not exceed $50 million in assets or $10 million in sales, and generally employs at least 50 full time equivalent employees in Ohio. The firm is required to reinvest that infusion of cash into one of five categories of allowable expenses within six months of its receipt. The investor must retain his or her ownership interest for a two-year holding period before the tax credit may be claimed; and the business must similarly retain the property purchased from the cash infusion for the entire holding period. The tax credit, which represents 10% of the amount invested, is limited to $1 million per person. Current law also specifies that tax credit claims against the PIT cannot exceed $100 million per fiscal biennium.

The bill expands the type of employees that would qualify a firm for the InvestOhio Program. The bill specifies that the employees of all of an enterprise's related or affiliated entities, including shared employees of a professional employer organization (PEO) and a client employer, shall be included in the calculation of the number of employees for purposes of the tax credit. A shared employee is defined as an individual employed by a PEO assigned to a client of the PEO on a permanent basis (duration of not less than 12 months per the agreement between the two parties). By expanding the number of employees that can qualify for the tax credit, the bill increases the potential revenue loss from the InvestOhio Program. However, the potential revenue loss from the bill is uncertain. From FY 2014 to date, 1,827 certificates have been issued totaling nearly $20 million according to the Development Services Agency, and the Department of Taxation estimated income tax revenue losses of less than $1 million per year in the current biennium. The Department of Taxation also estimates that this provision may reduce income tax revenue by $0.2 million in FY 2017, and $0.4 million in FY 2018. The revenue loss may grow to $1.0 million by FY 2020.

Voter approval now required for utilities service tax

Existing law permits counties to levy an excise tax on the charge for every utility service to customers within the county at a rate not to exceed 2% of utility charges. Current law allows this utilities service tax to be adopted by a resolution of the county Board of Commissioners. H.B. 473 would require that the adopting resolution be subject to an election as a ballot question. If a majority of electors vote in favor of the tax, then it would apply to all utility bills rendered at least 60 days after the effective date of the resolution. H.B. 473 prohibits utility bills from being rendered out of the ordinary course of business to avoid payment of the tax. It appears no county currently levies this tax, and this provision has no state fiscal effect.

Overall fiscal effect of the bill

Receipts from the state sales and use tax, cigarette tax, and the personal income tax are deposited into the GRF. Under permanent law, a portion of GRF tax receipts is subsequently transferred to the Local Government Fund (LGF) and the Public Library Fund (PLF), with each local fund receiving 1.66% of GRF tax revenue.[1] Potential revenue loss from the sales tax, cigarette, and personal income tax provisions would be up to $13.6 million per year on an ongoing basis. Thus, the potential annual revenue loss to the GRF would be up to $13.1 million, while the combined reduction in tax revenue to the LGF and PLF would total $0.5 million per year. However, as mentioned above, the GRF and the local government funds will sustain additional revenue

[1] H.B. 64 (the operating budget bill for the current biennium) specified the PLF share to be 1.70% for FYs 2016-2017.

reductions of several millions 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.

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 $2.3 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.

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