

Department of Taxation

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- Commercial Activity Tax implemented
- SSR funds appropriation increased to provide necessary funding due to freeze in GRF funding level

OVERVIEW

The Ohio Department of Taxation is responsible for the administration and enforcement of over 20 state and locally levied taxes. The Tax Commissioner administers all state taxes except for the insurance taxes and the motor vehicle license tax. Under the categories of administration and enforcement, the Department performs such duties as registering taxpayers, processing tax returns, determining tax liabilities, issuing refunds and assessments, conducting audits, and enforcing Ohio tax laws. In addition, the Department oversees the administration of the real property tax by local governments.

Beginning July 1, 2005, the Department is also responsible for the administration and enforcement of the new commercial activity tax (CAT), which was enacted in Am. Sub. H.B. 66 of the 126th General Assembly (H.B. 66). This new tax will be phased in over five years, with the first CAT returns required to be filed by February 10, 2006.

The Department of Taxation is also responsible for determining the amounts of various revenue distributions to local governments, including motor fuel tax distributions, reimbursement of local governments for property tax relief, permissive sales and use tax distributions, and allocations to counties from the Library and Local Government Support Fund (LLGSF), Local Government Fund (LGF), and Local Government Revenue Assistance Fund (LGRAF).

Agency in Brief

Agency In Brief					
Number of Employees*	Total Appropriations-All Funds		GRF Appropriations		Appropriation Bill(s)
	2006	2007	2006	2007	
1,586	\$2.10 billion	\$2.17 billion	\$539.97 million	\$515.22 million	Am. Sub. H. B. 66

* Employee count obtained from the Department of Administrative Services (DAS) payroll reports as of June 2005.

The Department of Taxation does not plan to hire additional FTEs in FY 2006 and FY 2007. In the FY 2004-2005 biennium, the Department hired over 80 new employees and reorganized various divisions.

The appropriations for GRF administrative funding are \$91,511,742 for FY 2006. This amount is \$7,029,078 (8.3%) higher than the actual GRF expenditures in FY 2005. The appropriation for GRF administrative funding for FY 2007 is \$91,511,742. This amount is the same as the FY 2006 appropriation for GRF administrative funding. The two line items that account for GRF administrative funding are 110-321, Operating Expenses and 110-412, Child Support Administration. These

appropriations do not include GRF moneys (such as property tax relief) that are simply distributed by the Department.

The total administrative appropriation for FY 2006 is \$148,242,893. This amount is \$27,065,360 higher than the total actual administrative expenditures in FY 2005, an increase of 18.3%. The total appropriation for administrative funding for FY 2007 is \$141,094,162. This amount is \$7,148,731 lower than FY 2006, a decrease of 4.8%. These amounts also do not include funds that are simply distributed by the Department.

Total appropriations for the Department are \$2,102,301,496 for FY 2006 and \$2,169,207,345 for FY 2007. This represents an increase from the previous year of 6.4% and 3.2%, respectively. (These amounts include Property Tax Relief funds that are distributed by the Department, \$448,458,603 in FY 2006 and \$423,713,183 in FY 2007.)

Summary of FYs 2006-2007 Budget Issues

Administration of the Commercial Activity Tax

H.B. 66 made permanent law changes related to the Department's general administration of the new commercial activity tax (CAT), particularly tax payments procedure, tax assessments, penalties and interest, refunds, record keeping, and challenging the legality of tax application procedures. H.B. 66 provides spending authority for the implementation and ongoing administration of the CAT.

Every legal taxpayer subject to the CAT is required to register with the Tax Commissioner by November 15, 2005 or within 30 days after first becoming subject to the tax. The registration must be made on a form provided by the Commissioner. A one-time \$15 or \$20 registration fee will be imposed. An additional fee of up to \$100 per month, up to \$1,000 total, will be charged if a taxpayer registers after the due date. Taxpayers that would otherwise be subject to the tax but begin business after November 30 in any year are exempt from the fee, as are taxpayers that do not surpass the \$40,000 taxable gross receipts threshold as of December 1. The registration fee may be waived by the Commissioner. Fee collections are credited to a fund to defray the costs of administering the CAT, including promoting awareness of the tax during its initial implementation.

The estimated costs to implement the CAT are included in line item 110-628, Tax Reform System Implementation in the Department of Taxation. Revenue from the proposed one-time fee is assumed to cover these costs.

In addition, the enacted bill provides for taxpayer appeals directly to the Ohio Supreme Court when the Commissioner issues a final determination in response to a taxpayer's challenge of an assessment under the CAT when the primary issue raised by the taxpayer arises under certain constitutional provisions governing (1) the General Assembly's power to tax incomes and to levy excise and franchise taxes, (2) the manner in which the General Assembly may use moneys derived from motor vehicle license and fuel taxes, or (3) the General Assembly's power to tax food for human consumption. The bill also prescribes the legal proceedings against taxpayers failing to report and pay the CAT, similar to the provisions for the corporate franchise tax and the personal income tax. Constitutional challenges to the "bright-line presence" standard for determining nexus under the CAT may also be appealed directly to the Ohio Supreme Court.

Authorization to Require Identifying Information from Persons Filing Tax Documents

H.B. 66 authorizes the Tax Commissioner to request that persons filing tax documents with the Commissioner provide any identifying information including a social security number, employer identification number, or other identification number needed to efficiently administer the tax with respect to which the document is filed. Taxpayers are required to update the Commissioner of any changes with respect to that information prior to, or at the time of, filing the next tax document requiring identifying information. The Commissioner is required to maintain the confidentiality of individuals' social security numbers.

The Commissioner may impose penalties for failure to comply with the request for identifying information and failure to update identifying information. Penalties in addition to criminal penalties may be imposed with respect to any false or fraudulent identifying information knowingly submitted by a person to the Commissioner.

Transmission of Sales and Use Taxes Collected by Clerks of Court

The enacted bill establishes procedures for the transmission of sales and use taxes collected by the clerks of court to the Treasurer of State. The clerks are to transmit sales and use taxes and remittance reports from sales of motor vehicles, off-highway vehicles, all-purpose vehicles, and titled watercraft and outboard motors during a week on or before the Friday following the close of that week. If, on any Friday, the offices of a clerk of court or the state are closed, the tax must be forwarded to the Treasurer on or before the next day on which the offices are open. The Tax Commissioner is required to determine the form of the remittance report. Upon receiving a tax remittance and a report, the Treasurer is required to date stamp the report and forward it to the Commissioner. The Treasurer may require the clerks of court to transmit tax collections and remittance reports electronically.

If the tax due for any week with respect to titled watercraft and outboard motors is not remitted by a clerk of court in accordance with the procedures outlined in the bill, the clerk must forfeit the poundage fees collected for sales made during that week. If the tax due for any week with respect to motor vehicles, off-highway vehicles, and all-purpose vehicles is not remitted by a clerk of court in accordance with the bill's procedures, the Tax Commissioner may, but is not required to, compel the clerk to forfeit the poundage fees collected by the clerk for sales made during that week.

Tax Amnesty Program

H.B. 66 requires that the Tax Commissioner administer a temporary tax amnesty program from January 1, 2006 through February 15, 2006. Under this program, taxpayers who voluntarily pay outstanding state taxes, tangible personal property taxes, county and transit authority sales taxes, and school district income taxes are not required to pay penalties associated with those outstanding taxes, are excused from having to pay one-half of the interest accruing on the taxes, and are immune from criminal and civil actions in connection with the taxes.

The enacted budget bill requires a transfer of \$2,000,000 from the Tax Reform System Implementation Fund (Fund 228) to appropriation item 110-630, Tax Amnesty Promotion and Administration (Fund 5BW). It also creates a new appropriation item, 110-630, Tax Amnesty Promotion and Administration (Fund 5BW), to implement and pay for expenses incurred in promoting and administering the tax amnesty program. The Director of Budget and Management is required to transfer the first \$2,000,000 of revenue received from the tax amnesty program to the Tax Reform System

Implementation Fund, the next \$10,000,000 to the General Revenue Fund, and any remaining excess fund balance to the Budget Stabilization Fund.

Miscellaneous Budget Issues

Tax Reform Implementation Fund

H.B. 66 creates the Tax Reform System Implementation Fund (Fund 228) to pay the expenses of the Department to provide an integrated tax system that will accommodate the needs of tax reform and allow for improved customer service, processing efficiency, compliance, enforcement, and reporting. The Director of Budget and Management is required to transfer and credit residual cash to the fund on July 2, 2005 or as soon as possible.

Computation of Transfers to the Property Tax Administration Fund

H.B. 66 changes the calculation of transfers to the Property Tax Administration Fund (Fund 5V8) in the State Special Revenue Fund group. This fund is used to defray Department of Taxation costs to administer property taxes. The current charge of 0.3% against the amount of the 10% real property tax rollback is raised to 0.33% for FY 2006, and to 0.35% for FY 2007 and thereafter. Current charges of 0.15% against public utility tangible personal property taxes and 0.75% against tangible personal property taxes are changed to 0.5% for FY 2006, to 0.56% for FY 2007, and to 0.6% for FY 2008 and thereafter. Charges in each fiscal year are based on the preceding tax year; for example, FY 2006 charges are based on tax year 2005.

Tire Tax Administration

H.B. 66 reduces the Department's share of money collected from the Scrap Tire Management program from 4% to 2% (the remainder goes to the Ohio EPA's Scrap Tire Management Fund). The Department uses its share for administration of the tire tax.

Interest Rate on Estate Tax and Personal Property Tax Overpayments and Underpayments

H.B. 66 reduces the rate at which interest accrues on estate tax and personal property tax overpayments and underpayments.

Semiannual Reports on Tourism-Related Tax Revenues

H.B. 66 requires the Tax Commissioner to prepare semiannual reports summarizing tax revenue associated with the travel and tourism industry. The reports must contain information on travel and tourism industries included in the industrial classification system used by the Commissioner in preparing the report. The Commissioner is required to adopt rules necessary to administer the reporting requirement.

Centralized Tax Filing and Payment Fund

H.B. 66 requires the Director of Budget and Management to transfer \$4.5 million in the biennium from the GRF to the Centralized Tax Filing and Payment Fund (Fund 5W4), in the General Services Fund group in the Department of Taxation's budget.

International Registration Plan Audit

H.B. 66 appropriates line item 110-616, International Registration Plan (Fund 4C6), in the Department of Taxation's State Special Revenue Fund group for the audits of persons with vehicles registered under the International Registration Plan.

Litter Control Tax Administration Fund

H.B. 66 authorizes some corporate franchise tax revenues to be deposited into the Litter Control Tax Administration Fund (Fund 437).

Homestead Exemption, Property Tax Rollback, and Tangible Tax Exemption

H.B. 66 appropriates GRF line item 110-901, Property Tax Allocation – TAX, to pay the state's costs incurred due to the Homestead Exemption, the Manufactured Home Property Tax Rollback, and the Property Tax Rollback. It also earmarks GRF appropriation item 110-906, Tangible Tax Exemption – Taxation, to pay the state's cost incurred due to the tangible personal property tax exemption. These moneys are distributed to county auditors, who distribute the appropriate amounts to the local taxing districts.

Municipal Income Tax

H.B. 66 appropriates line item 110-901, Municipal Income Tax (Fund 095), in the Agency Fund Group, to make payments to municipal corporations for the municipal income tax on electric companies. This local tax is collected and distributed by the Department of Taxation.

Tax Refunds

H.B. 66 appropriates any additional amounts that are needed to pay tax refunds for taxes or fees that have been overpaid or illegally or erroneously assessed and collected. The funds are transfers from current receipts of the same tax or fee from which the refund arose.

Travel Expenses for the Streamlined Sales Tax Project

H.B. 66 allows the Tax Commissioner to use funds from appropriation item 110-607, Local Tax Administration (Fund 435), to pay for travel costs to meetings of the Streamlined Sales Tax Project.

Taxation of Railroad Tracks

Real property of railroads that is not used in railroad operations is to be assessed by county auditors. The Tax Commissioner is to continue to assess real property used in railroad operations and tangible personal property of railroads.

Vetoed Provisions**Joint Legislative Tax Reform Impact Study Committee**

H.B. 66 proposed the creation of a joint legislative study committee with ten members to study the effects on school districts and other local taxing units of the bill's phase-out of tangible personal property taxes, the revenue impact of the commercial activity tax, and the revenue effects of reclassifying

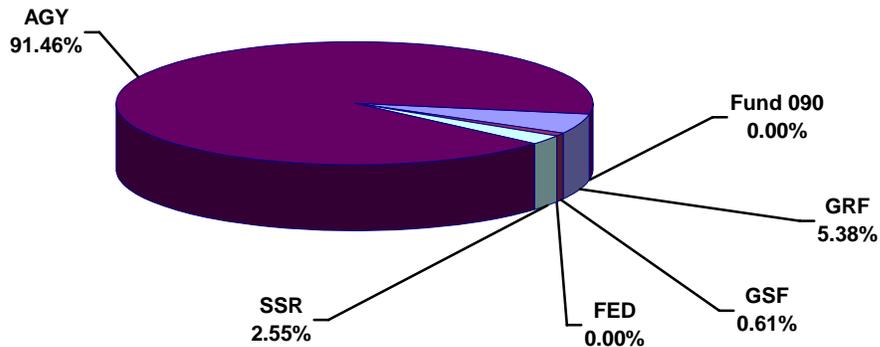
rental real property having more than three units as residential/agricultural real property instead of as nonresidential/agricultural real property.

Estate Tax Penalty and Enforcement

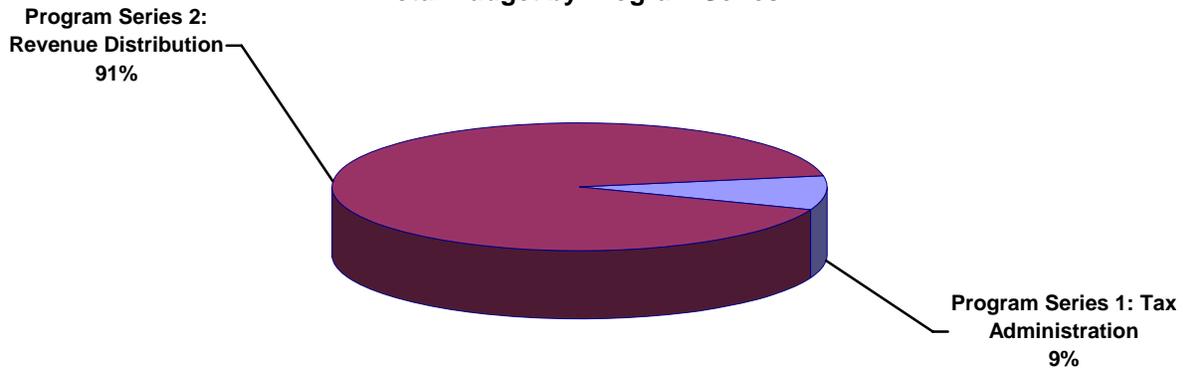
H.B. 66 proposed an increase in the penalty for late estate tax payments and filings and authorized county auditors to forgive such penalties for good cause.

Table 1: Total Budget By Program Series		
Program Series	FY 2006	FY 2007
Subtotal Program 1: Tax Administration	\$148,242,893	\$141,094,162
Subtotal Program 2: Revenue Distribution	\$1,505,600,000	\$1,604,400,000
Subtotal Program 3: Property Tax Relief	\$448,458,603	\$423,713,183
Grand Total	\$2,102,301,496	\$2,169,207,345

Total Budget by Fund Group*



Total Budget by Program Series*



ANALYSIS OF THE ENACTED BUDGET

Program Series 1

Tax Administration

Purpose: To administer the state's tax laws to ensure compliance in filing and payment of taxes and to determine tax liability.

The following table shows the line items that are used to fund the Tax Administration program series.

Fund	ALI	Title	FY 2006	FY 2007
General Revenue Fund				
GRF	110-321	Operating Expenses	\$91,439,754	\$91,439,754
GRF	110-412	Child Support Administration	\$71,988	\$71,988
General Revenue Fund Subtotal			\$91,511,742	\$91,511,742
State Special Revenue Fund				
5N5	110-605	Municipal Income Administration	\$265,000	\$265,000
437	110-606	Litter Tax and Natural Resources Administration	\$625,232	\$625,232
435	110-607	Local Tax Administration	\$15,880,987	\$16,394,879
436	110-608	Motor Vehicle Audit	\$1,350,000	\$1,350,000
438	110-609	School District Income Tax	\$2,599,999	\$2,599,999
4R6	110-610	Tire Tax Administration	\$65,000	\$65,000
639	110-614	Cigarette Tax Enforcement	\$168,925	\$168,925
688	110-615	Local Excise Tax Administration	\$300,000	\$300,000
4C6	110-616	International Registration Plan	\$706,855	\$706,855
5N6	110-618	Kilowatt Hour Tax Administration	\$85,000	\$85,000
5V7	110-622	Motor Fuel Tax Administration	\$4,268,345	\$4,397,263
5V8	110-623	Property Tax Administration	\$12,758,643	\$12,967,102
5BQ	110-629	Commercial Activity Tax Administration	\$6,000,000	\$500,000
State Special Revenue Fund Subtotal			\$45,073,986	\$40,425,255
General Services Fund				
433	110-602	Tape File Account	\$96,165	\$96,165
5W4	110-625	Centralized Tax Filing & Payment	\$2,500,000	\$2,000,000
5W7	110-627	Exempt Facility Administration	\$36,000	\$36,000
228	110-628	Tax Reform System Implementation	\$7,000,000	\$7,000,000
5BW	110-630	Tax Amnesty Promotion and Administration	\$2,000,000	\$0
General Services Fund Subtotal			\$11,632,165	\$9,132,165
Federal Special Revenue Fund				
3J6	110-601	Motor Fuel Compliance	\$25,000	\$25,000
Federal Special Revenue Fund Subtotal			\$25,000	\$25,000
Total Funding: Tax Administration			\$148,242,893	\$141,094,162

This analysis focuses on the following specific programs within the Tax Administration program series:

- **Program 1.1: Taxpayer Services**
- **Program 1.2: Tax Processing**
- **Program 1.3: Tax Compliance**
- **Program 1.4: Tax Policy And Analysis**
- **Program 1.5: Local Government Services**

Program 1.1: Taxpayer Services

Program Description: To administer Ohio's tax laws efficiently and cost effectively. Administration involves registering taxpayers, processing tax returns, determining tax liabilities, issuing refunds and assessments, and enforcing Ohio tax laws. The Taxpayer Services program provides the delivery of services to taxpayers as a means of increasing tax compliance.

Funding Source: GRF

Implication of the Enacted Budget: The enacted budget provides the Taxpayer Services program with total GRF funding of \$26,060,329 each in FY 2006 and FY 2007.

Program 1.2: Tax Processing

Program Description: This program provides for all processing services of tax returns and related documents.

Funding Sources: The Tax Processing program is funded by GRF line item 110-321, Operating Expenses and line item 110-606, Litter Tax and Natural Resources Administration Fund (Fund 437)

Implication of the Enacted Budget: The enacted budget provides the Tax Processing program with total funding of \$17,998,785 for both FY 2006 and FY 2007.

Program 1.3: Tax Compliance

Program Description: This program conducts audits of taxpayers' returns and records for mathematical accuracy, evaluates the substantial correctness (which identifies areas of underpayment or overpayment of tax), and issues notices and assessments to taxpayers who have not paid tax liabilities. This program also provides for the matching of persons delinquent in child support payments with taxpayers due an Ohio income tax refund. This program also reviews appeals of Tax Commissioner findings in tax disputes. The Department provides the first level of appeal. Determinations of the Department may then be appealed to the Board of Tax Appeals. Tax compliance also includes enforcement and investigation activities associated with the investigation of fraud, coordinated efforts with other enforcement agencies, tracking of evidence, and testimony for trial cases.

Funding Sources: State GRF, federal grants for fuel tax collection and enforcement, percentages of local taxes (sales and use, school district income, and proposed percentages of real property taxes, public utility property taxes, and tangible personal property taxes, etc.), cigarette license taxes, International Registration Plan (IRP) fees, and motor vehicle title fees and portions of the receipts from the motor fuel taxes

Implication of the Enacted Budget: The enacted budget provides the Tax Compliance program with total funding of \$52,446,021 for FY 2006 and \$52,574,939 for FY 2007. The enacted budget includes funding of \$7 million in each fiscal year for the new tax reform projects. The enacted budget also provides the necessary funding from various special revenue funds to offset the "freeze" in GRF funding levels in FY 2006 and FY 2007. The funding for activities that are performed by the Tax Administration program series in support of administrative and compliance responsibilities related to various special funds are funded from specified special revenue funds.

Program 1.4: Tax Policy and Analysis

Program Description: This program provides administrative, advisory, and technical assistance to the legislative and executive branches, while working closely with industry, trade groups, professional organizations, and the media. The program also facilitates tax policy, monitors and analyzes tax legislation, and provides legal counsel necessary for the management of tax related legal issues and bankruptcy cases.

Funding Source: GRF

Implication of the Enacted Budget: The enacted budget provides the Tax Policy and Analysis program with total GRF funding of \$9,143,976 in each of FYs 2006 and 2007. This program is fully funded by the GRF.

Program 1.5: Local Government Services

Program Description: This program provides information and assistance to local governments and school districts. This program also provides for the administration of some local taxes.

Funding Sources: GRF, GSF, and SSR

Implication of the Enacted Budget: The enacted budget provides the Local Government Services program with total funding of \$34,593,782 for FY 2006 and \$34,816,133 for FY 2007. The enacted budget provides the offset costs associated with various local government tax and fee administration and the funding needed to modernize the computer systems, methods of filing, and taxpayer services.

Program Series 2**Revenue Distribution**

Purpose: To distribute revenue by law to the intended parties.

The following table shows the line items that are used to fund the Revenue Distribution program series.

Fund	ALI	Title	FY 2006	FY 2007
State Special Revenue Fund				
SSR	110-613	Ohio Political Party Distribution	\$600,000	\$600,000
State Special Revenue Fund Subtotal			\$600,000	\$600,000
Agency Fund				
AGY	110-901	Municipal Income Tax	\$21,000,000	\$21,000,000
AGY	110-635	Tax Refunds	\$1,483,900,000	\$1,582,700,000
Agency Fund Subtotal			\$1,504,900,000	\$1,603,700,000
Holding Account Redistribution Fund				
R10	110-611	Tax Distributions	\$50,000	\$50,000
R11	110-612	Miscellaneous Income Tax Receipts	\$50,000	\$50,000
Holding Account Redistribution Fund Subtotal			\$100,000	\$100,000
Total Funding: Revenue Distribution			\$1,505,600,000	\$1,604,400,000

This analysis focuses on the following specific program within the program series:

■ **Program 2.1: Revenue Accounting**

Program 2.1: Revenue Accounting

Program Description: There are five line items under this program series: Ohio Political Party Distributions, Municipal Income Tax, Tax Refunds, Tax Distributions, and Miscellaneous Income Tax Receipts.

Line item 110-613, Ohio Political Party Distributions, provides qualifying political parties quarterly payments based upon checkoffs made by taxpayers on their state income tax returns. For each qualifying party, one-half of the receipts goes to the treasurer of the state executive committee of the party and one-half goes to the treasurers of the county executive committees. The Department of Taxation determines each county committee's share by the ratio of the number of checkoffs in that county to the statewide number of checkoffs.

Line item 110-901, Municipal Income Tax, holds the receipts from the municipal income tax on electric companies collected by the Department of Taxation and wholly distributed to applicable municipalities that impose the city income tax after the deduction of an administrative fee paid to the Department.

Line item 110-635, Tax Refunds, is used to pay refunds for taxes or fees that have been overpaid or illegally or erroneously assessed and collected. The refunds are paid from current receipts of the same tax or fee from which the refund arose.

Line items 110-611 and 110-612, Tax Distributions and Miscellaneous Income Tax Receipts, are holding accounts for the Department of Taxation. They are used to temporarily hold checks for sales tax or personal income tax when there is uncertainty as to the proper disposition of the tax payment. The distributions from these funds vary greatly from year to year.

Funding Sources: SSR, AGY, and Fund 090 (Holding Account Redistribution Fund)

Implication of the Enacted Budget: The enacted budget provides the Revenue Accounting program with total funding of \$1,505,600,000 for FY 2006 and \$1,604,400,000 for FY 2007. All of the funds are nonoperating funds and used only for the distribution of refunds, local revenue, payments to political parties, and misdirected payments.

Program Series 3

Property Tax Relief

Purpose: To reimburse local governments (other than schools) for state property tax relief programs.

The following table shows the line items that are used to fund the Property Tax Relief program series.

Fund	ALI	Title	FY 2006	FY 2007
General Revenue Fund				
GRF	110-901	Property Tax Allocation – TAX	\$430,102,680	\$409,946,241
GRF	110-906	Tangible Tax Exemption – TAX	\$18,355,923	\$13,766,942
General Revenue Fund Subtotal			\$448,458,603	\$423,713,183
Total Funding: Property Tax Relief			\$448,458,603	\$423,713,183

This analysis focuses on the following specific program within the program series:

■ **Program 3: Property Tax Relief**

Program Description: The two line items under this program series provide for the reimbursement to local governments other than school districts for the revenues lost due to property tax relief programs.

Funding Source: GRF

Implication of the Enacted Budget: All of the funding is used for the distribution of property tax relief to local governments.