Multistate Tax
EXTERNAL ALERT

Ohio Governor Kasich signs biennial budget bill

July 8, 2015

Overview

Ohio Governor John Kasich recently signed into law Substitute House Bill No. 64 (HB 64),[1] which makes various changes to Ohio's tax laws in the areas of individual income tax, sales and use tax, and municipal income tax. In this Tax Alert we provide an overview of some of the more significant provisions of the new law.

Individual income tax reductions and credit limitations

HB 64 provides for a rate reduction of 6.3 percent for all individual, trust, and estate income tax rates in all brackets for taxable years beginning in 2015 on income other than business income. This reduces the top marginal tax rate upon Ohio adjusted gross income from 5.333 percent to 4.997 percent.[2]

Beginning in 2013, Ohio granted individuals an "Ohio Small Business Investor Income Deduction" (Small Business Deduction) equal to 50 percent of the first $250,000 of net Ohio-sourced business income ($125,000 maximum deduction).[3] In 2014 this Small Business Deduction was increased to 75 percent of the first $250,000 of net Ohio-sourced business income ($187,500 maximum deduction). Under the statute in effect for 2013 and 2014, the definition of "Ohio small business investor income" specifically referenced income apportioned or allocated to Ohio.[4] HB 64 favorably modifies the Small Business Deduction for 2015 and subsequent taxable years. For taxable years beginning in 2015, the deduction equals the lesser of 75 percent of Ohio business income or $187,500.[5] For taxable years beginning in 2016 and thereafter, the deduction equals the lesser of business income or $250,000.[6] It should be noted that HB 64 eliminated the statutory definition of "Ohio small business investor income" previously in effect, and the currently applicable definitional sections do not reference Ohio apportionment or allocation. This raises some ambiguity regarding the intended scope of the Small Business Deduction benefit.

For 2015 and forward, HB 64 also provides that Ohio adjusted gross income excludes all business income to the extent not otherwise deducted or excluded in computing federal or Ohio adjusted gross income for the year.[7] Individual income tax is imposed on "taxable business income" at a flat 3 percent rate.[8] "Taxable business income" is defined as all business income reduced by deductions, including the Small Business Deduction, with the applicable deduction amount varying by year.[9] Similar to the ambiguity noted above with respect to the scope of the Small Business Deduction, the provisions in HB 64 that reference the tax base subject to the flat 3 percent rate do not specify that the rate is limited to Ohio-apportioned or allocated income. It is yet to be seen how this uncertainty will be interpreted by the Ohio Department of Taxation.

HB 64 also restricts the retirement income credit, the lump-sum retirement credit, the lump-sum distribution credit, and the senior citizen credit to taxpayers whose individual or joint adjusted gross income (less personal exemptions) for the taxable year is less than $100,000.[10]

---

[1] Substitute HB 64, 131st Gen. Assemb., Reg. Sess. (Ohio Jun. 30, 2015). A copy of the adopted law is accessible **here**.
[2] Substitute HB 64, amending Ohio Rev. Code §5747.02(A)(3).
[3] See Ohio Rev. Code §5747.01(A)(31) in effect prior to the enactment of HB 64.
[4] *Id.*
[5] Substitute HB 64, adding Ohio Rev. Code §5747.01(HH)(1).
[6] Substitute HB 64, adding Ohio Rev. Code §5747.01(HH)(2).
[7] Substitute HB 64, amending Ohio Rev. Code §5747.01(A)(31).
[8] Substitute HB 64, adding Ohio Rev. Code §5747.02(A)(4).
[9] Substitute HB 64, adding Ohio Rev. Code §5747.01(HH).
[10] Substitute HB 64, amending Ohio Rev. Code §5747.055(E), (F), and (G).

Sales and use tax nexus

Effective July 1, 2015, HB 64 broadens the indices for determining when a seller has "substantial nexus" with Ohio for purposes of registration and collection of Ohio sales and use tax. The new law amends the existing nexus provision to create a presumption of "substantial nexus" with Ohio when:[11]

(1) The seller uses an office, distribution facility, warehouse, storage facility, or similar place of business in Ohio operated by the seller or another person, other than a common carrier.
(2) The seller regularly uses employees, agents, or other persons in Ohio to: (a) conduct the seller's business, (b) use trademarks or trade names in Ohio that are the same as or similar to those used by the seller, or (c) engage in a business with the same or similar industry classification as the seller selling a similar product as the seller.
(3) The seller uses any person, other than a common carrier, to receive or process orders, promote, advertise, or facilitate customer sales; perform maintenance, delivery, and installation services for the seller's Ohio customers; or facilitate delivery by allowing Ohio customers to pick up property sold by the seller.
(4) The seller has an "affiliated person"[12] that has substantial nexus with Ohio.
(5) The seller enters into an agreement to pay one or more Ohio residents to refer potential customers to the seller, whether by a link on a website or otherwise, if gross sales to customers referred to the seller by all such residents exceed $10,000 during the preceding 12 months.

The presumption of "substantial nexus" is rebuttable. To rebut the presumption of nexus under items (1)-(4) above, a seller must demonstrate that the applicable activities conducted by a person in Ohio are not significantly associated with the seller's ability to establish or maintain an Ohio market for the seller's sales.[13] To rebut the presumption of nexus under item (5) above, a seller must prove that each Ohio resident the seller engaged to refer potential customers did not engage in activity in Ohio significantly associated with the seller's ability to establish or maintain an Ohio market during the preceding 12 months.[14]

Commercial Activity Tax receipts exclusion and credit provision

Retroactive to the July 1, 2005 inception of the Commercial Activity Tax (CAT), HB 64 excludes from the CAT taxable base receipts from sales or packaging of personal care, health, beauty, or aromatic products, including candles.[15] The exclusion applies only to transactions among businesses or retailers within an "integrated supply chain."[16]

The new law also provides for a credit against CAT for owners of a historic rehabilitation tax credit certificate if the taxpayer cannot claim the credit against another tax and the certificate became effective after 2013 but before June 30, 2017.[17]

[11] Substitute HB 64, amending Ohio Rev. Code §5741.01(I)(2). HB 64 did not change that a seller is also presumed to have "substantial nexus" if the seller is making regular deliveries of tangible personal property (TPP) into Ohio by means other than a common carrier; or owns TPP that is rented or leased by an Ohio consumer or offering TPP, on approval, to Ohio consumers. This presumption is rebuttable pursuant to Substitute HB 64, amending Ohio Rev. Code §5741.01(I)(3).
[12] The new law defines an "affiliated person" as "any person that is a member of the same controlled group of corporations as the seller or any other person that, notwithstanding the form of the organization, bears the same ownership relationship to the seller as a corporation that is a member of the same controlled group of corporations." See Substitute HB 64, adding Ohio Rev. Code §5741.01(I)(6)(a).
[13] Substitute HB 64, amending Ohio Rev. Code §5741.01(I)(3).
[14] Substitute HB 64, amending Ohio Rev. Code §5741.01(I)(4).
[15] Substitute HB 64, adding Ohio Rev. Code §5751.01(F)(2)(jj).
[16] *Id.* An "integrated supply chain" is defined as two or more businesses that are primarily involved in manufacturing, assembling, or packaging of retail goods. Integrated supply chain businesses do not share a common owner and have a location within a 100-500 acre parcel or parcels of land within counties that have a population between 150,000 and 200,000 people. Currently, the following Ohio counties qualify: Clermont, Delaware, Greene, Licking, Medina, and Portage.
[17] Substitute HB 64, amending Ohio Rev. Code §757.170.

Financial Institutions Tax exemptions

HB 64 clarifies that production credit associations and agricultural credit associations are exempt from the Financial Institutions Tax (FIT).[18] Taxpayers not subject to the FIT are subject to the CAT unless otherwise excluded.[19]

Municipal income tax revisions

HB 64 provides for several new municipal income tax provisions as well as modifications to certain provisions enacted last year in House Bill 5 of 2014 (HB 5).[20] Generally, the changes would apply to taxable years beginning on or after January 1, 2016, and include the following:

- A publicly traded partnership may elect to be taxed as a C corporation for municipal income tax purposes.[21]
- Changes the annual return filing deadline for municipal income taxpayers that are not individuals to the 15th day of the fourth month following the end of the taxpayer's taxable year.[22]
- Requires a municipal tax administrator to grant a taxpayer a six-month filing extension for a municipal income tax return, even if the taxpayer did not request a corresponding federal extension.[23]
- Provides for municipal taxing jurisdictions to tax compensation that is earned outside of the United States, and that is either included in the taxpayer's gross income for federal income tax purposes or would have been included in the taxpayer's gross income for such purposes if the taxpayer did not elect to exclude the income under IRC §911.[24]

Effective January 1, 2016, HB 5 requires all municipalities to allow a net operating loss (NOL) deduction, but temporarily reduces by 50 percent the deduction otherwise allowed for any NOL incurred after 2016 and claimed for taxable years 2018 through 2022.[25] HB 64 clarifies that for any NOL incurred after 2016 that is carried forward to the 2019 through 2022 taxable years, the annual 50 percent limitation continues to apply to the amount carried forward.[26]

Jobs Creation and Job Retention Tax Credits modifications

HB 64 makes several revisions to the computation and administration of the Jobs Creation Tax Credit (JCTC) and the Job Retention Tax Credit (JRTC). The new law revises the computation of the JCTC and JRTC such that the amount of the credit would equal an agreed-upon percentage of the taxpayer's Ohio employee payroll minus baseline payroll. Similarly, the new law revises the calculation of the JRTC such that the amount of the credit would equal an agreed-upon percentage of the taxpayer's Ohio employee payroll.[27] Previously, the computation of these credits was tied to an employer's Ohio income tax withholdings, regardless of the tax rate at which the withholdings were applied.

Contacts

If you have questions regarding these Ohio tax law changes or other Ohio tax matters, please contact any of the following Deloitte Tax LLP professionals:

David Adler
Director
Deloitte Tax LLP, Columbus
+1 614 229 4687

Brian Hickey
Director
Deloitte Tax LLP, Cincinnati
+1 513 784 7171

Courtney Clark
Senior Manager
Deloitte Tax LLP, Columbus
+1 614 229 5924

[18] Substitute HB 64, amending Ohio Rev. Code §5726.01(B)(7).
[19] Ohio Rev. Code §5751.01(D) and (E)(3).
[20] HB 5, 130th Gen. Assemb., Reg. Sess. (Ohio Dec. 19, 2014); summarized in our Multistate Tax Alert dated Dec. 19, 2014, available **here**.
[21] Substitute HB 64, adding Ohio Rev. Code §718.01(D)(4).
[22] Substitute HB 64, adding Ohio Rev. Code §718.05(G)(1)(b).
[23] Substitute HB 64, adding Ohio Rev. Code §718.05(G)(2)(b).
[24] Substitute HB 64, amending Ohio Rev. Code §718.01(R)(2)(f)(i).
[25] Ohio Rev. Code §718.01(E)(8)(c)(1).
[26] Substitute HB 64, amending Ohio Rev. Code §718.01(E)(8)(e).
[27] Substitute HB 64, amending Ohio Rev. Code §122.17 and §122.171.