



## Year in Review

The Ohio Department of Taxation (ODT) under Tax Commissioner Joe Testa began Fiscal Year (FY) 2014 focused on several priorities, resulting from the continuing efforts of Ohio Governor John R. Kasich and the Ohio General Assembly to boost an already growing Ohio economy and provide a state tax system that promotes economic growth and job creation. Chief among these priorities were:

- Implementing tax reform initiatives fostered in House Bill 59 (H.B. 59), the biennial budget bill for FY 2014-2015. This bill delivered \$2.7 billion in tax cuts to individuals and to nearly all small business taxpayers over three years, the largest tax decrease of any state in the country.
- Successfully resetting the State Taxation Accounting and Revenue System (STARS) computer project which will replace ODT's existing and outdated technology infrastructure. Once implemented, STARS will integrate all tax information into one database providing cost- and time-savings to ODT, state taxpayers and local governments that interact with Ohio's tax system.
- Reaffirming ODT's commitment to improve taxpayers' experience with the state's tax system by continuing to review, simplify and streamline processes, systems and procedures.

As FY 2014 progressed, ODT was called upon to research and develop additional tax reform proposals intended to further Ohio's economic momentum and enhance the state's job creation potential.

### Implementing the Tax Cuts and Reforms from HB 59

The most prominent of the H.B. 59 tax reforms called on ODT to immediately engage and implement two primary tax cut initiatives; one focused on individuals, the other on small businesses and both lessening Ohio's income tax burden over the next three years.

**10 Percent Personal Income Tax Cut** – effective with the 2013 tax year, personal income tax rates have been reduced by 8.5 percent, 9.0 percent in 2014, and 10.0 percent (see H.B. 483 on pg. 7) in 2015. This three-year reduction will cumulatively deliver nearly \$2.7 billion in tax relief.

**50 Percent Small Business Deduction** – also effective beginning with the 2013 tax year, small business owners/investors can exclude from their state income tax returns half of their net business income up to a cap of \$250,000. This is keeping more than \$1.6 billion

in the hands of Ohio small business owners to use to grow their businesses.

Of the numerous other tax law changes contained in H.B. 59, many had significant impact on tax revenues and reform, involving income, sales, commercial activity and real property taxes. Other changes brought improvements and simplification to Ohio's tax system. Please note that some of the income tax changes effectuated through H.B. 59 were further modified in the Mid-Biennium Budget Review Process.

The changes implemented include:

#### Income Tax

- Updating employer withholding tables to reflect the lower income tax rates.
- Assisting lower income Ohioans by introducing an Ohio Earned Income Tax Credit that will benefit an estimated 475,000 eligible taxpayers with tax reductions of up to \$302.
- Establishing a means test limiting the \$20 personal exemption tax credit to taxpayers with Ohio taxable income less than \$30,000.
- Temporarily freezing for three years the annual inflation adjustments to the income tax brackets and the personal and dependent exemptions.

#### Sales Tax

- As part of Ohio's tax reform plan to lower income tax rates that pose a barrier to job creation, the state sales tax rate was adjusted from 5.5 percent to 5.75 percent.
- Broadened the sales tax base to include digital goods (e.g., books, music, videos) and magazine subscriptions purchased online to ensure equal treatment with the way in which those products are taxed in retail stores.

#### Commercial Activity Tax (CAT)

- Changed the annual minimum tax from a flat rate of \$150 to a variable amount tied to the level of business receipts.
- Switched motor fuel refineries, terminals and other suppliers from the CAT to the new Petroleum Activity Tax (PAT). The PAT is a tax for the privilege of doing business, measured by the gross receipts related to the first sale of motor fuel in Ohio.

#### Real Property Tax

- Returned the homestead exemption to its former and long-standing status as a means-tested program. Seniors currently eligible for the

program will continue to receive the exemption; those turning 65 years old in 2014 and beyond are subject to an eligibility limit of \$30,000 of Ohio Adjusted Gross Income (OAGI). Social security benefits and some individual retirement account and pension benefits do not count toward the \$30,000 limit as they are not included in OAGI. The \$30,000 OAGI limit is adjusted annually for inflation; it was adjusted to \$30,500 for 2014 applications. The program had been opened to all seniors in 2007 vastly increasing the costs of the program from \$70 million in 2006 to \$428 million in 2013.

- Removed the state subsidy for certain new levies meaning residential property owners will pay the full tax related to those new levies instead of being subsidized by all taxpayers in Ohio. The subsidy reimburses local governments for the non-business and owner-occupied credits.

#### Other Tax Changes

- Changed the Other Tobacco Products tax rate on 'little cigars' to one comparable to the rate imposed on cigarettes.
- Repealed an income tax deduction for gambling losses that was to be effective in 2013.
- Requires CAT, severance and financial institutions taxpayers to file returns electronically.
- Eliminated a loophole which allowed both a parent and their child to claim a dependent credit for that same child on their respective income tax returns.

#### Mid-Biennium Budget Review Process Delivers More Tax Cuts for Ohioans

Continuing a practice begun with his first biennial budget, Governor Kasich again launched a budget and policy review of state government prior to the mid-point of the current two-year budget. This mid-biennium budget review coincided with an improving Ohio economy and the realization of greater efficiencies achieved at ODT and other departments across state government. The confluence of efficient management of state government and strengthening state revenues gave Governor Kasich and the General Assembly an opportunity to make additional tax cuts. The result: the Governor in June, 2014 signed HB 483 and its package of expanded tax cuts into law. Those tax reductions total \$402 million.

For tax year 2014, the personal income tax deduction on small business income gets a one-time temporary boost from 50 percent to 75 percent, freeing up funds for private sector job creators to further invest in growing their businesses. Ohio is also accelerating the last phase of the 10 percent personal income tax cut, authorized in the FY14-15 budget bill (H.B. 59), to make it effective for all of tax year 2014. That cut was originally set to begin in January 2015. Employer

withholding rates have also been adjusted to align with the 10 percent reduction in the income tax.

Furthermore, there is additional tax relief for low- and middle-income Ohioans with increases in the earned income tax credit (EITC) and state income tax personal and dependent tax exemption. The EITC doubles from 5 to 10 percent of the federal credit. The personal and dependent exemption increases from \$1,700 to \$2,200 for Ohioans with OAGI less than \$40,000 a year and from \$1,700 to \$1,950 for those with OAGI between \$40,000 and \$80,000.

The legislation also contained a number of tax system improvements, including:

- Addressing the issue of when payments and documents are considered to have been filed, which is especially important given the increase in electronic payments and requirements for more returns to be filed electronically. This provision clarifies that the time stamp assigned by the first electronic system receiving the payment or document determines the point at which the filing occurred. For documents and payments that are mailed, the postmark date will continue to serve as the filing date.
- Allowing ODT to more expeditiously share information with the Development Services Agency (DSA) relating to taxpayers that are applying for tax credits as part of an agreement with DSA. The change facilitates this important process to ensure that a tax credit applicant is in good standing with regard to their tax obligations before a tax benefit is extended.
- Carrying the job creation and job retention tax credits (JCTC and JRTC) from the CAT to the new PAT. H.B. 59 carved motor fuel tax receipts out of the CAT base and placed them into the PAT. During that shift, the JCTC and JRTC were not carried over from the CAT to the PAT. This change is a matter of fairness to those taxpayers that previously entered into JCTC or JRTC agreements.
- Moving the sale of cigarette tax stamps from the Treasurer's Office to ODT to be more in step with online-filing capabilities and ODT's tobacco enforcement responsibilities and to provide a one-stop-shop for cigarette wholesalers.
- Allowing ODT to pay interest on refunds, and not just charge interest on delinquent billings, for kilowatt-hour and natural gas distribution taxes, and the replacement tire fee.

#### Fixing the Flaw: Tax Overpayments by Businesses

With the enactment of Senate Bill 263 (S.B. 263), Ohio permanently abolished a long-time, anti-business practice of deliberately not informing business taxpayers of tax overpayments. This law ensures that business taxpayers are treated fairly going forward. If they pay too much, ODT will be obligated to return the extra amount that was paid or apply the overpay-

ment to existing or future tax liabilities. Fixing this problem sends the right signal to job creators.

SB 263 follows an initiative by ODT to return overpayments to business taxpayers who were previously unaware of them. This occurred after the Tax Commissioner found out about a departmental practice that treated business taxpayers differently than individual taxpayers. While individual taxpayers receive refunds expeditiously, business taxpayers had to identify and ask for the return of their overpayments. Although this practice complied with the law, the approach made it difficult for businesses to get refunds as ODT had an unwritten policy of not informing most business taxpayers of overpayments that may have been refundable. If taxpayers did not formally request the refund within the statute of limitations, filing the correct form and stating the precise amount, they forfeited the money.

In December 2012, ODT began contacting business taxpayers about their credit balances. To date, ODT has returned more than \$30.2 million to Ohio businesses that likely would have never claimed the overpayments had this initiative not been taken.

### **STARS Success**

ODT launched a new era in FY 2014 with the successful implementation of the first three of eight scheduled releases which will collectively constitute the STARS computer system. This year's roll-outs cover the administration of employer withholding, natural gas distribution and sales and use taxes, as well as the replacement tire fee. Ultimately STARS will integrate all tax information into one database and, once launched department-wide, will completely replace an outdated and fragmented technology support structure.

STARS is not only making ODT more efficient, it is also simplifying processes at other levels of government and for taxpayers. For example, STARS allows county auditors' offices to issue sales tax vendor's licenses more efficiently. Someone standing at the county auditor's counter can now immediately apply for and receive a vendor's license. In the past, the process was completely paper-driven with a turnaround of about ten days.

### **Financial Institutions Tax (FIT)**

In 2014, ODT began administering the new FIT, a tax on banks, savings and loans and other financial institutions. This tax replaced the previous fragmented system of taxing these businesses. The creation of the FIT made it possible to eliminate the dealers in intangibles tax and to finalize the phase-out of the corporate franchise tax. There are three tax rates for the FIT depending on the amount of equity a financial institution has in Ohio. The FIT helped cut taxes for most smaller community banks and closed loopholes that had allowed very large banks to significantly reduce taxable income through corporate planning.

### **Cutting Costs/Increasing Efficiency**

ODT is continuously trying to create more uniformity and streamlining within the tax system. Beginning in 2011, ODT has been processing more revenue with less overhead. Since then, total revenues collected have grown 18 percent while the number of employees and operating expenses decreased by more than 22 percent with the close of FY 2014.

ODT conducted a comprehensive review of forms in FY 2014 with the goal of reducing the nearly 550 forms used both internally by employees and externally by taxpayers and other government entities. As a result, 45 external forms were recommended for consolidation and 100 external forms were recommended for elimination. Thirty-two internal forms were eliminated. Ten additional internal forms were transformed so they can now be filled out and submitted electronically on ODT's intranet site. The forms page on the intranet site lists all internal forms alphabetically by division, which makes it easier for employees to locate.

Other efficiencies and accomplishments achieved during FY 2014 are described below:

- Transferred wireless 9-1-1 fee administration from the Public Utilities Commission of Ohio to ODT, with the addition of a point-of-sale fee to gain equity with the customers of post-sale fees for pre-paid cell phone services (from wireless service provider to vendor point-of-sale).
- Implemented electronic filing through the Ohio Business Gateway (OBG) for employer withholding for payroll processors like ADP and Paychex.
- Created a portal for county auditors to use to verify the income of homestead exemption applicants. Since the portal became operational in February 2014, it has been used by 74 counties to make approximately 5,000 income verification inquiries.
- Mandated electronic filing for CAT annual filers effective May 2014, either through OBG or Telefile.
- Instituted an automated refund claim process for the CAT to notify taxpayers of overpayments stemming from amended returns.
- Ohio became a full member of the Streamlined Sales Tax Project. It had been an associate member since the project began in 2005.
- E-mailed a reminder notice to a pilot group of taxpayers that they had not remitted payment when they filed their personal income and/or school district income tax return. This is a new communication and compliance step taken before sending a billing notice.
- Created ODT's first mobile phone application. Check My Refund went live in the spring of 2014.

**Ohio Virtual Tax Academy (OVTA)**

ODT expanded its educational outreach with the launch of OVTA. Governor John Kasich has made helping small business a priority and has supported and encouraged the development of OVTA. This program provides tax-related information to small business owners to help them succeed. Attorneys and accountants are also invited to attend and earn free continuing professional and legal education credits. Participants can attend the event in person or view it from anywhere as an online webinar. The inaugural OVTA event was held in Columbus in March 2014, with 448 people attending either the live session or participating online. The third and latest OVTA event in December 2014 was an online-only event and had 842

virtual attendees. ODT plans to host these types of seminars at least twice a year.

**Ohio Department of Taxation Overview**

ODT, under the Ohio Tax Commissioner, is responsible for administering and collecting most state and several local taxes as well as supervising the real property tax. These responsibilities include making tax assessments, valuations, findings and determinations; promulgating rules and regulations, auditing tax returns, issuing and overseeing certain licenses and distributing revenues from certain taxes to various units of local government.

In FY 2014, ODT collected approximately \$26.0 billion in state and local taxes. ODT's actual expenditures, from all funds, totaled approximately \$125.7 million.

Table 1

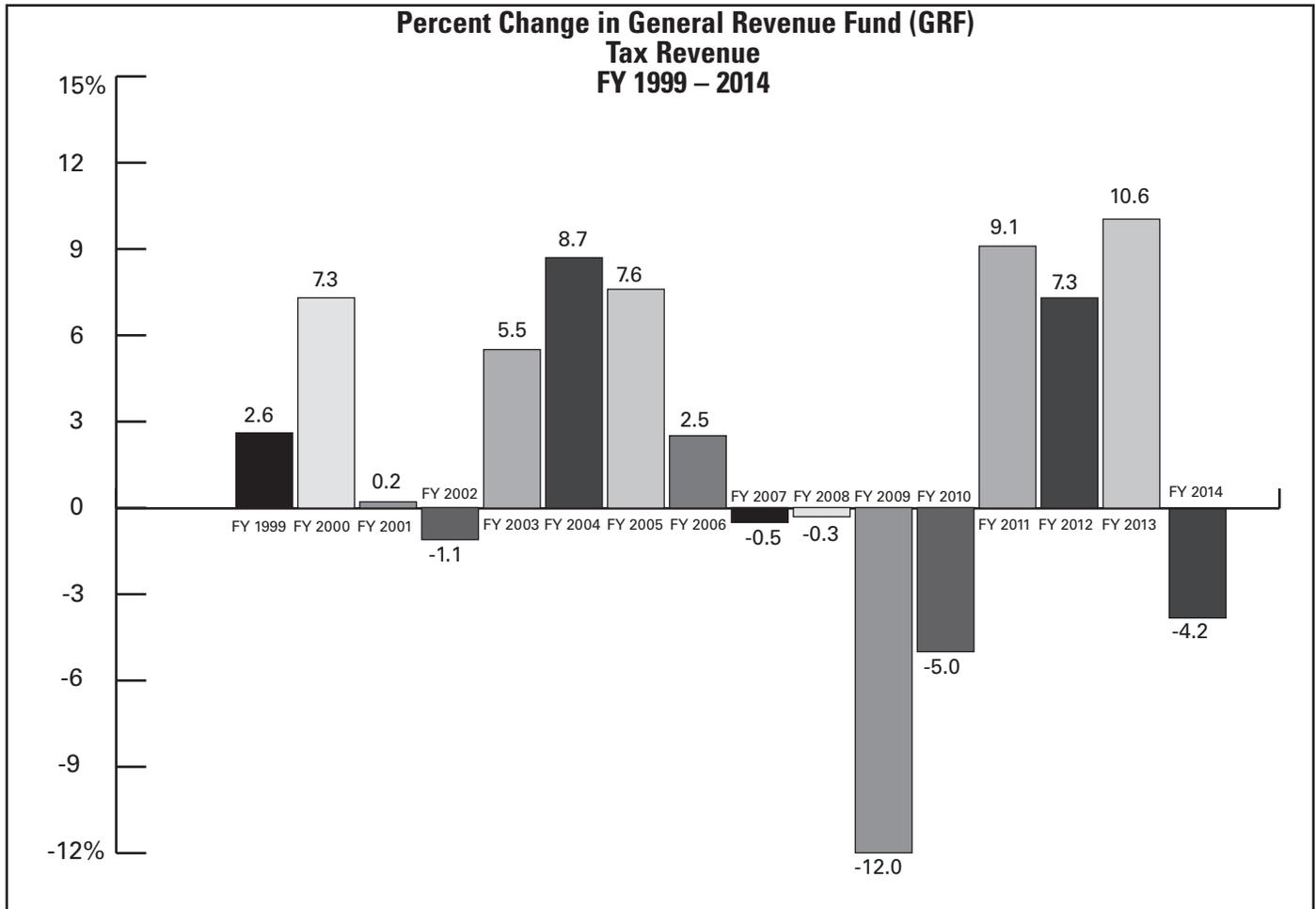


Table 2

GRF Tax Revenue, 2007 - 2014 (figures in millions)		
Fiscal Year	Revenue	% Change
2007	\$19,468.9	-0.5%
2008	\$19,419.5	-0.3%
2009	\$17,093.7	-12.0%
2010	\$16,233.6	-5.0%
2011	\$17,706.1	+9.1%
2012	\$19,005.2	+7.3%
2013	\$21,015.7	+10.6%
2014	20,134.4	-4.2%

Table 3

## Collections for Taxes Administered by the Ohio Tax Commissioner

This table shows both gross and net tax collections for state-collected and locally-collected taxes. For state collected taxes, gross tax collections are equal to total taxes collected, including taxes which were later refunded. Net tax collections are equal to gross collections, less all refunds. Note: because the data for state-collected taxes is from the state accounting system contained within the Ohio Administrative Knowledge System (OAKS), the figures will differ slightly from data shown elsewhere in the report. Other tables in this report frequently represent taxes reported as shown on tax returns filed during the fiscal year, rather than actual collections during the fiscal year or for specific funds (like the state's General Revenue Fund). For locally-collected taxes, collections are shown on a calendar year basis, rather than a fiscal year basis.

State-Collected Taxes	Gross Tax Collections		Net Tax Collections		Percent
	FY 2013	FY 2014	FY 2013	FY 2014	Change, 13-14
State Sales and Use	\$8,701,147,686	\$9,465,531,587	\$8,625,426,589	\$9,344,575,216	8.34%
Local Sales and Use	2,005,468,152	2,134,302,887	2,005,468,152	2,134,302,887	6.42%
Resort Area Excise	1,094,065	1,165,978	1,094,065	1,165,978	6.57%
State Individual Income	11,174,351,040	10,116,735,182	9,869,817,561	8,425,116,548	-14.64%
Municipal Income Tax for Electric Light Companies	9,905,416	8,796,853	9,905,416	8,796,853	-11.19%
School District Income	390,372,689	408,357,723	368,577,221	386,666,212	4.91%
Corporation Franchise <sup>1</sup>	341,802,018	72,629,614	262,226,256	(11,171,983)	N/A
Commercial Activity Tax	1,671,853,550	1,829,164,711	1,594,848,533	1,685,787,403	5.70%
Financial Institutions Tax <sup>6</sup>	0	197,931,125	0	197,837,292	N/A
Dealers in Intangibles <sup>1</sup>	38,455,459	480,388	38,429,463	475,979	-98.76%
Motor Vehicle Fuel	1,742,705,818	1,844,815,403	1,725,000,270	1,825,528,042	5.83%
Motor Fuel Use	32,686,515	34,523,106	32,133,587	34,013,939	5.85%
Public Utility Excise	96,910,788	106,050,399	96,665,733	106,011,927	9.67%
Kilowatt-Hour Excise	547,544,113	544,779,979	547,544,113	544,630,705	-0.53%
Natural Gas Consumption	57,804,017	76,109,967	57,804,017	76,109,967	31.67%
Cigarette Excise	828,854,094	815,722,596	827,440,021	813,983,559	-1.63%
Local Cigarette Excise <sup>3</sup>	19,850,492	18,937,553	19,808,032	18,859,778	-4.79%
Alcoholic Beverage Excise <sup>2</sup>	57,790,655	56,697,412	57,632,015	56,564,921	-1.85%
Local Alcoholic Beverage <sup>2,3</sup>	5,372,056	5,499,710	5,371,520	5,434,788	1.18%
Replacement Tire Fee	7,107,983	7,668,409	7,047,554	7,649,409	8.54%
Horse Racing	6,246,801	5,526,549	6,246,801	5,526,549	-11.53%
Severance	12,307,593	15,037,950	12,307,593	15,037,950	22.18%
Estate Tax <sup>1</sup>	105,202,436	39,391,459	105,202,436	39,391,459	-62.56%
Casino Gross Revenue Tax	225,438,259	273,393,331	225,438,259	273,393,331	21.27%
Wireless 911 <sup>6</sup>	0	15,760,376	0	15,752,244	N/A
<b>Total State-Collected Taxes</b>	<b>\$28,080,271,695</b>	<b>\$28,095,010,246</b>	<b>\$26,501,435,206</b>	<b>\$26,011,440,953</b>	<b>-1.85%</b>
	Tax Collections		Percent Change, 2013-14		
Locally-Collected Taxes	CY 2013	CY 2014			
Public Utility Property <sup>4</sup>	\$862,109,396	\$934,646,188	8.41%		
Estate <sup>1,5</sup>	340,503,355	167,496,346	-50.81%		
<b>Total Locally-Collected Taxes</b>	<b>\$1,202,612,751</b>	<b>\$1,102,142,534</b>	<b>-8.35%</b>		

<sup>1</sup>These taxes are no longer in effect. Tax year 2013 was the last for the Corporation Franchise Tax (taxpayers began paying Financial Institutions Tax). Estate Tax was repealed for estates with dates of death on or after January 1, 2013. The Dealers in Intangibles Tax ceased on January 1, 2013 (most taxpayers began paying the Commercial Activity Tax). Only residual revenues and refunds are applicable going forward.

<sup>2</sup> Excludes tax on liquor since it is administered by the Ohio Department of Commerce, Division of Liquor Control.

<sup>3</sup> Collected for Cuyahoga County.

<sup>4</sup> Consists of taxes levied on the tangible personal property of public utilities in 2013 and collected in 2014.

<sup>5</sup> CY 2013 data is from County Auditor estate tax settlements for the August 2012 and February 2013 periods; CY 2014 data is from the settlements for the August 2013 and February 2014 periods.

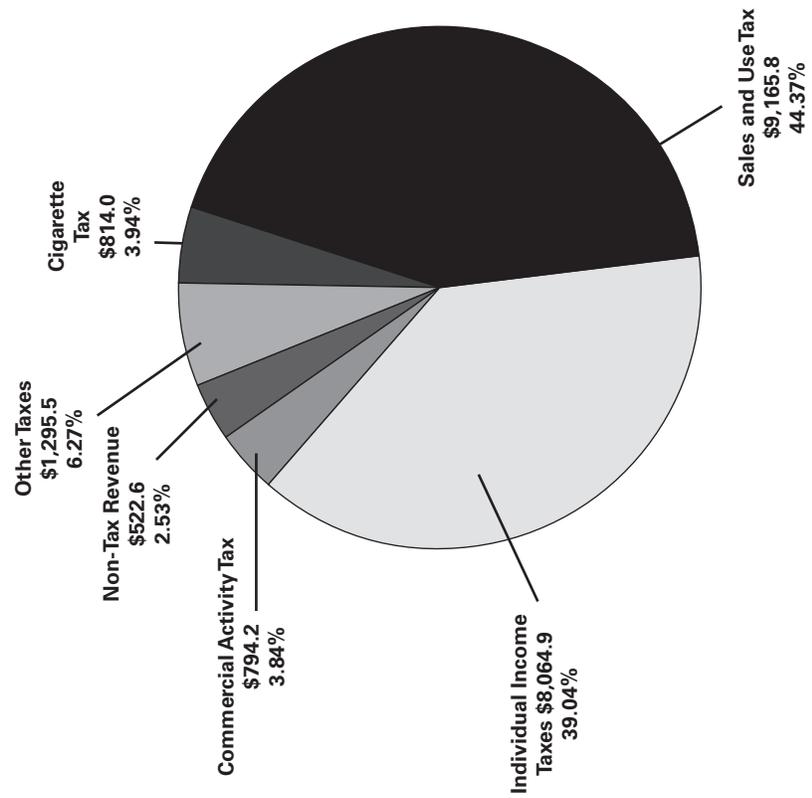
<sup>6</sup> New taxes administered by the Tax Commissioner.

Sources: Fiscal Year 2013 and 2014 data on state-collected taxes was extracted from the state accounting system (OAKS). Data on locally-collected taxes is based on the Department of Taxation's own data sources.

# General Revenue Fund Sources, Fiscal Year 2014 (excluding federal aid) (dollars in millions)

Chart 1

Major Taxes:	Collections	Percent of Total
Sales and Use Tax	\$9,165.8	44.37%
Individual Income Tax	8,064.9	39.04%
Cigarette Tax	814.0	3.94%
Commercial Activity Tax	794.2	3.84%
<b>Total Major Taxes</b>	<b>\$18,838.9</b>	<b>91.20%</b>
<b>Miscellaneous:</b>		
Kilowatt-Hour Excise Tax	\$306.3	
Foreign Insurance Tax	286.5	
Financial Institutions Tax <sup>1</sup>	197.8	
Domestic Insurance Tax	196.9	
Public Utility Excise Tax	106.0	
Alcoholic Beverage Taxes (including liquor gallonage)	97.4	
Natural Gas Distribution Tax	76.1	
Estate Tax	39.4	
Dealers in Intangibles Property Tax	0.5	
Corporation Franchise Tax	(11.4)	
<b>Total Tax Revenue</b>	<b>\$1,295.5</b>	<b>6.27%</b>
<b>Non-Tax Revenue:</b>		
Earnings on Investment	\$17.3	
Liquor Profits	-	
Miscellaneous <sup>2</sup>	505.2	
<b>Total Non-Tax Revenue</b>	<b>\$522.6</b>	<b>2.53%</b>
<b>Total</b>	<b>\$20,656.9</b>	<b>100.00%</b> <sup>3</sup>



Source: Ohio Office of Budget and Management.

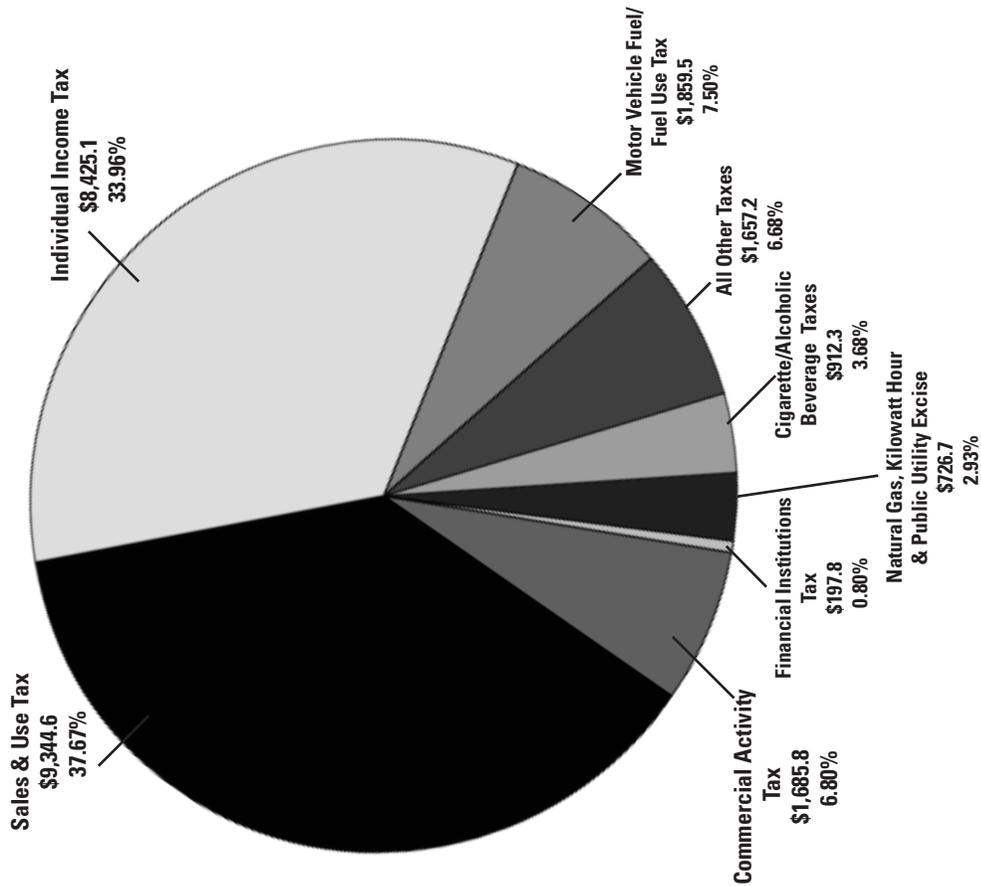
<sup>1</sup> Collections represent estimated payments for tax year 2014 only.

<sup>2</sup> Includes certain transfers into the general revenue fund, licenses and fees and other income.

<sup>3</sup> Because of rounding, total percentage sums to 99.99%.

# All State Tax Sources, Fiscal Year 2014 (excluding federal aid) (dollars in millions)

Chart 2



Major Taxes:	Collections	Percent of Total
Sales and Use Tax	\$9,344.6	37.67%
Individual Income Tax	8,425.1	33.96%
Motor Vehicle Fuel and Fuel Use Tax	1,859.5	7.50%
Commercial Activity Tax	1,685.8	6.80%
Cigarette/Alcoholic Beverage Taxes <sup>1</sup>	912.3	3.68%
Natural Gas, Kilowatt Hour and Public Utility Excise	726.7	2.93%
Financial Institutions Tax	197.8	0.80%
All Other Taxes	1,657.2	6.68%
<b>Total</b>	<b>\$24,809.0</b>	<b>100.00%**</b>
<b>Other Taxes:</b>		
Motor Vehicle License	\$800.9	
Foreign Insurance Tax	\$308.0	
Casino Gross Revenue Tax	\$273.4	
Domestic Insurance Tax	\$202.3	
Estate Tax	\$39.4	
Wireless 9-1-1	\$15.8	
Severance	\$15.0	
Replacement Tire	\$7.6	
Horse Racing	\$5.5	
Dealers in Intangibles Property Tax	\$0.5	
Corporation Franchise Tax	\$(11.2)	
<b>Total All Other Taxes</b>	<b>\$1,657.2</b>	

Source: Ohio Office of Budget and Management and Department of Taxation Records.

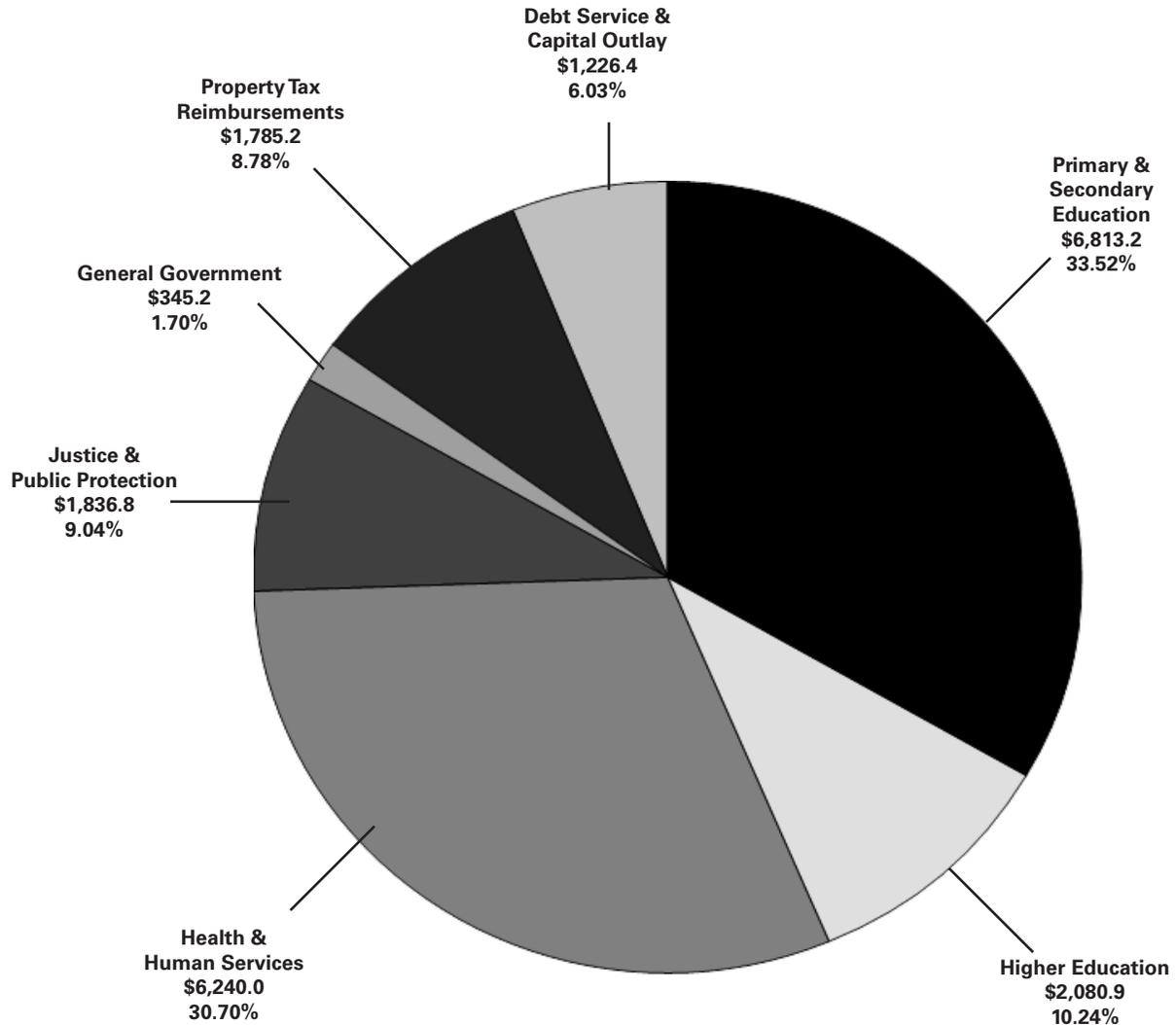
<sup>1</sup>Includes tax on liquor of \$41.8 million, which is administered by the Department of Commerce

\*\* Because of rounding, total percentage sums to 100.02%.

## General Revenue Fund Expenditures Fiscal Year 2014 (excluding federal aid)

Chart 3

(dollars in millions)



Category	FY 2014 Expenditures	Percentage of Total
Primary, Secondary and Other Education	\$6,813.2	33.52%
Higher Education	\$2,080.9	10.24%
Health and Human Services (including Medicaid)	\$6,240.0	30.70%
Justice and Public Protection	\$1,836.8	9.04%
General Government	\$345.2	1.70%
Property Tax Reimbursements	\$1,785.2	8.78%
Debt Service & Capital Outlay	\$1,226.4	6.03%
<b>Total</b>	<b>\$20,327.9</b>	<b>100.00%</b>

Source: Office of Budget and Management financial reports and Ohio Department of Taxation calculations

## Tax Burden Comparisons Among the States

The table on this page compares the overall state and local tax burden in Ohio to that of nine other states. The comparisons rely on data compiled by the U.S. Census Bureau documenting tax collections during fiscal year 2011. Tax burdens are compared both on a per capita basis and as a percentage of income. The rankings – 1 through 51 – indicate the states' standing in comparison to all other 50 states as well as the District of Columbia.

States were included in this table either because they neighbor Ohio or because, like Ohio, they are large, economically important states. The same nine states are used for comparisons throughout this book.

State	Taxes per capita		Taxes as % of Personal Income	
	Total	Rank	Percentage	Rank
Georgia	\$3,173	46	9.0	41
Indiana	3,553	33	10.0	28
Kentucky	3,333	41	9.9	32
Mass.	5,425	8	10.2	21
Mich.	3,655	30	10.1	27
Ohio	3,910	27	10.4	18
Pa.	4,376	19	10.2	22
Tenn.	2,981	48	8.25	50
Texas	3,542	34	8.99	42
W. Va.	3,760	28	11.46	9

Source: U.S. Dept. of Commerce: U.S. Census Bureau, Bureau of Economic Analysis