

MUNICIPAL INCOME TAX FOR ELECTRIC LIGHT COMPANIES & TELEPHONE COMPANIES

The Ohio Revised Code Chapter 5745 municipal income tax was enacted in 2000 by Substitute House Bill 483, 123rd General Assembly and took effect on January 1, 2002. The tax applies only to “electric light companies” and (local exchange) telephone companies and is administered by the Department of Taxation (rather than by each Ohio municipality that has enacted a municipal income tax and in which the taxpayer has taxable nexus). The term “electric light company” includes “electric companies” and certain electing marketers and brokers of electricity. The statute refers to a marketer or broker of electricity as “an electric light company that is not an electric company.”

Electric companies were first subject to the Chapter 5745 municipal income tax for the taxable year that included January 1, 2002. For taxable years prior to the taxable year that included January 1, 2002, electric companies were exempt from municipal income tax. Local exchange telephone companies were first subject to the Chapter 5745 municipal income tax taxable years that begin on or after January 1, 2004.

The tax generated \$40.9 million in revenue in calendar year 2005. Tax returns for calendar year 2006 will be reported in April 2007.

An “electric light company that is not an electric company” can under certain circumstances elect to be a Chapter 5745 taxpayer (see Section 7 of Senate Bill 287, 123rd General Assembly). Unlike an “electric company,” an “electric light company that is not an electric company” was not exempt from municipal income tax for taxable years prior to the taxable year that included December 31, 2002.

A municipality that has enacted an income tax may not require a Chapter 5745 municipal income taxpayer to file a municipal income tax return for that municipality. However, to the extent necessary for a municipality to compute a taxpayer’s property, payroll, and sales factors for that municipality, the municipality may require the taxpayer to report to the municipality the value of the taxpayer’s real and tangible personal property situated in the municipality, the taxpayer’s compensation paid to its employees in the municipality, and the taxpayer’s sales made in the municipality (see R.C. 5745.03 (E)).

TAXPAYER (OHIO REVISED CODE 5745):

The term “taxpayer” means an entity that is subject to the Chapter 5745 municipal income tax. Taxpayers include:

- **Electric companies.** A person is an electric company when engaged in the business of generating, transmitting, or distributing electricity within Ohio for use by others; a rural electric company is excluded (see R.C. 5727.01 (D) (3));
- **Combined companies.** A person is a combined company when engaged in the activity of an electric company or rural electric company, and in the activity of a heating company or a natural gas company, or any combination thereof (see R.C. 5727.01 (L));
- **Certain marketers or brokers of electricity** that meet the requirements and make the election set out in R.C. 5745.031; and
- **(Local exchange) telephone companies.** A person is a “telephone company” when primarily engaged in the business of providing local

exchange telephone service, excluding cellular radio service, in this state (R.C. 5727.01 (D) (2)).

TAX BASE (R.C. 5745):

The “starting point” for Chapter 5745 municipal income taxpayers is federal taxable income after certain adjustments (see below). In determining the Chapter 5745 municipal income tax, the municipal income taxpayer’s adjusted federal taxable income is first multiplied by the taxpayer’s Ohio apportionment ratio to determine Ohio income. Then, Ohio income is multiplied by the taxpayer’s municipal apportionment ratio and tax rate for each Ohio municipality which has enacted a municipal income tax, and in which the taxpayer has taxable nexus.

Taxable Year:

For Chapter 5745 municipal income tax purposes a municipal income taxpayer’s taxable year is the same as the taxpayer’s taxable year for federal income tax purposes, regardless of when during the taxable year the taxpayer first entered Ohio and regardless of when during the taxable year the municipal income taxpayer first became subject to the Chapter 5745 tax in a particular municipality.

1. Adjustments to Federal Taxable Income:

Prior to the enactment of Amended Substitute House Bill 530 (see **Recent Legislation**), R.C. 5745.01 (H) defined “Internal Revenue Code” for purposes of the Chapter 5745 municipal income tax as the Internal Revenue Code (I.R.C.) as it existed on December 31, 2001. Therefore, prior law required municipal income taxpayers to adjust their federal taxable income before a net operating loss (NOL) deduction and special deductions for purposes of the municipal income tax by reversing the effects of amendments to the Internal Revenue Code enacted by Congress after December 31, 2001. The new law as enacted by H.B. 530 requires Chapter 5745 taxpayers to compute their federal taxable income starting point by applying the I.R.C. as it existed on March 30, 2006.

If amendments to the I.R.C. enacted after March 30, 2006 affect the taxpayer’s federal taxable income, then the taxpayer must recompute federal taxable income before a net operating loss deduction and special deductions by applying the I.R.C. as it existed on March 30, 2006. Such taxpayers must enter on line 2 the difference between the following amounts: (1) the taxpayer’s federal taxable income before NOL deduction and special deductions as it would have been computed under the I.R.C. as it existed on March 30, 2006; and (2) the taxpayer’s federal taxable income as shown on the taxpayer’s federal income tax return.

H.B. 530 also enacted special transition rules applicable to taxable years ending in 2005 and taxable years ending in 2006 before March 30 (see **Recent Legislation** for new legislation described above).

2. Net intangible income (R.C. 5745.01 (G) (1) and (G) (2)).

Deduct the taxpayer’s intangible income as defined in R.C. 718.01, less expenses incurred in the production of such intangible income to the extent that the income and expenses are used in determining federal taxable income.

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3. Book-tax difference for electric companies (R.C. 5745.01 (G) (3)).

Add or subtract the net book-tax difference on "qualifying assets." For electric companies the term "qualifying assets" is defined in R.C. 5733.0510 (B) (3) as any asset on the taxpayer's books as of December 31, 2000 sold or disposed of in taxable transactions during the taxable year. If the net book-tax difference is a positive amount (that is, the assets' net book value on December 31, 2000 is greater than the assets' adjusted basis on that date), enter it in parentheses and deduct it from federal taxable income. If the net book-tax difference is a negative amount (that is, the assets' net book value on December 31, 2000 is less than the assets' adjusted basis on that date), enter it as a positive amount and add it to federal taxable income.

4. Book-tax difference adjustment for telephone companies (R.C. 5745.01 (G) (5)).

For each of the ten taxable years ending in 2009 through 2018, local exchange telephone companies are eligible for a book-tax difference adjustment. For each of those years the adjustment equals one-tenth of the difference between the book value of a qualifying telephone company's assets on December 31, 2003, in accordance with generally accepted accounting principles (GAAP), and the federal adjusted basis of such assets on December 31, 2003. The book-tax difference may be a negative number. R.C. 5733.0511 (A) defines "qualifying telephone company" and "qualifying telephone company asset."

Ohio Apportionment Ratio (R.C. 5745.02):

The Chapter 5745 municipal income tax Ohio apportionment ratio is computed in a manner similar to the Chapter 5733 Ohio corporation franchise tax apportionment ratio.

Municipal Apportionment Ratio (R.C. 5745.02 (C)):

For purposes of determining the taxpayer's apportionment ratio for each municipality, the Chapter 5745 municipal income taxpayer's payroll, sales, and property are generally situated consistent with the franchise tax siting provisions. However, for purposes of the municipal payroll factor, compensation is situated based upon the amount of compensation that during the taxable year is earned in the municipality by the taxpayer's employees for services performed for the taxpayer, and that is subject to income tax withholding by the municipality.

RATES (R.C. 5745.03 (F)):

In determining the tax payable to each municipality for the taxpayer's taxable year, the taxpayer must use the certified tax rate in effect for that municipality on the first day of January of the taxpayer's taxable year. If a taxpayer's taxable year is for a period of less than twelve months and that taxable year does not include the first day of January, the tax rate used is the tax rate in effect in a municipality on the first day of January of the preceding taxable year.

CREDITS (R.C. 5745.06):

If the taxpayer has an interest in a pass-through entity that is also subject to, and paid, the Chapter 5745 municipal income tax for Chapter 5745

taxpayers, then the taxpayer may claim as a credit against the taxpayer's own Chapter 5745 municipal income tax, for a particular municipality, the taxpayer's proportionate share of the tax paid by the pass-through entity to that same municipality. The credit equals the qualifying taxpayer's proportionate share of the lesser of the Chapter 5745 tax due from, or the Chapter 5745 tax paid, by the qualifying pass-through entity to that municipality for the pass-through entity's taxable year ending in the taxpayer's taxable year. The taxpayer must claim the credit for the taxpayer's taxable year in which the pass-through entity's taxable year ends.



Taxpayer Elections and Alternative Apportionment Methods

(R.C. 5745.031, 5745.01 (C), 5745.02 (F)):

1. An "electric light company that is not an electric company" can elect to be a taxpayer under Chapter 5745 if during the company's most recently concluded taxable year, at least 50 percent of the company's total sales in Ohio, as determined under R.C. 5733.059, consist of sales of electricity and other energy commodities. The company must make the election in writing to the Tax Commissioner before the first day of the first taxable year to which the election is to apply. The election is effective for five consecutive taxable years and, once made, is irrevocable for those five years. An "electric light company that is not an electric company" that does not meet the requirements to make the election, or meets the requirements but does not make a timely election, is subject to the filing and payment requirements of each municipality which has enacted an income tax and in which the company has taxable nexus.
2. If a taxpayer is a qualified subchapter S subsidiary as defined in I.R.C. section 1361 or a disregarded entity, the company's parent S corporation or owner is the taxpayer for the purposes of the municipal income tax.
3. If the taxpayer is a "combined company," it must adjust the numerator of its municipal property, payroll, and sales factors (but not the numerator of its Chapter 5745 Ohio property, payroll, and sales factors) to include only the company's activity as an electric company, because "for a combined company, only the income attributed from the activity of an electric company shall be subject to taxation by a municipal corporation" (see R.C. 1701.18 (F) (6)).
4. Alternative apportionment methods may also be available to taxpayers (see R.C. 5745.02 (E)). If the provisions for apportioning adjusted federal taxable income to Ohio or for apportioning Ohio net income to an Ohio municipality do not fairly represent business activity in Ohio or in a municipality, the Tax Commissioner may adopt rules for apportioning such income by an alternative method that does fairly represent business activity in Ohio or Ohio's municipalities. In addition, if the above provisions for apportioning adjusted federal taxable income to Ohio or for apportioning Ohio net income to an Ohio municipality do not fairly represent the extent of a taxpayer's business activity in Ohio or Ohio's municipalities, the taxpayer may request, or the Tax Commissioner may require, that the

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taxpayer's adjusted federal taxable income or Ohio net income be determined by an alternative method, including any of the alternative methods enumerated in R.C. 5733.05 (B) (2) (d). A taxpayer requesting an alternative method must make the request in writing to the Tax Commissioner either with the annual report, a timely filed amended report, or a timely filed petition for reassessment.

following the end of their taxable year, the taxpayer must nevertheless pay any remaining tax due by that date.

Tax payment by electronic funds transfer (R.C. 5745.03 (E), 5745.04 (E) and 5745.041):

If any remittance of estimated Chapter 5745 municipal income tax is for \$1,000 or more or the amount payable with the report exceeds \$1,000, the taxpayer must make the remittance by electronic funds transfer (EFT).

DISPOSITION OF REVENUE (R.C. 5745.05):

Prior to the first day of March, June, September, and December, the Tax Commissioner must certify to the Director of Budget and Management the amount to be paid to each municipal corporation, as indicated on the declaration of estimated tax reports and annual reports received, less any amounts previously distributed and the net of any audit adjustments made by the Tax Commissioner. Not later than the first day of March, June, September, and December, the Director of Budget and Management must provide for payment of the amount certified to each municipal corporation from the Municipal Income Tax Fund, plus a pro rata share of any investment earnings accruing to the fund since the previous payment.

The Department of Taxation receives 1.5 percent of collections into the Municipal Income Tax Administration Fund to defray the costs of administering the tax.

ADMINISTRATION (R.C. 5745):

The municipal income tax for electric light companies and local exchange telephone companies is administered and enforced by the Department of Taxation, rather than by the various Ohio municipalities that have enacted a municipal income tax.

OHIO REVISED CODE CITATIONS:

Chapters 5745, 113, 718, 4928, 5703, 5727, and 5733.



(R.C. 5745.02-.04, 5745.041):

Remittances are payable to the Treasurer of State.

Estimated payment requirements for taxable years beginning in 2003 and each taxable year thereafter:

As used below, the term "combined tax liability" means the total of the taxpayer's income tax liabilities to all Ohio municipalities for a taxable year. For each taxable year, each taxpayer must file a declaration of estimated tax report and make payment as follows:

1. Not later than the 15th day of the fourth month after the end of the preceding taxable year, the taxpayer must pay at least 25 percent of the combined tax liability for the preceding taxable year, or 20 percent of the combined tax liability for the current taxable year.
2. Not later than the 15th day of the sixth month after the end of the preceding taxable year, the taxpayer must pay at least 50 percent of the combined tax liability for the preceding taxable year, or 40 percent of the combined tax liability for the current taxable year.
3. Not later than the 15th day of the ninth month after the end of the preceding taxable year, the taxpayer must pay at least 75 percent of the combined tax liability for the preceding taxable year, or 60 percent of the combined tax liability for the current taxable year.
4. Not later than the 15th day of the 12th month after the end of the preceding taxable year, the taxpayer must pay at least 100 percent of the combined tax liability for the preceding taxable year, or 80 percent of the combined tax liability for the current taxable year.

Extension to file return:

Without an extension, the annual Chapter 5745 municipal income tax return for a taxpayer is due by the 15th day of the fourth month following the end of the taxpayer's taxable year. The due date of the annual municipal income tax return is extended to the 15th day of the month following the due date of the taxpayer's federal income tax return if, by the 15th day of the fourth month following the end of its taxable year, the taxpayer filed with the Tax Commissioner a copy of the taxpayer's federal extension. The granting of an extension does not extend the last day for paying taxes without penalty unless the Tax Commissioner extends the payment date. So, if the taxpayer does not file their municipal income tax return by the 15th day of the fourth month

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included in Title 57.) The new law defines the term “Internal Revenue Code ‘as amended’ ” as being the Internal Revenue Code as it existed on March 30, 2006, the effective date of R.C. 5701.11 as enacted by H.B. 530. Thus, for municipal income tax purposes the taxpayer’s federal taxable income must be redetermined by applying the I.R.C. as it existed on March 30, 2006.

H.B. 530 also enacted special transitional rules. In computing federal taxable income for purposes of the municipal income tax the new law specifically provides that for taxable years ending in 2005 and for taxable years ending in 2006 before March 30, each Chapter 5745 taxpayer can make an irrevocable election to apply the Internal Revenue Code in effect for those taxable years (without adjustment to reverse the effects of changes to the Internal Revenue Code enacted after December 31, 2001).

Amended Substitute House Bill 530, 126th Ohio General Assembly, (effective March 30, 2006). R.C. 5745.01 (H):

H.B. 530 amended the definition of “Internal Revenue Code” (I.R.C.) by eliminating reference to a date specific and by adding “as amended.” H.B. 530 also enacted new R.C. section 5701.11 which defines the term “Internal Revenue Code ‘as amended’,” for all of Title 57 of the Ohio Revised Code. (Chapter 5745 is

TABLE

REVENUE FROM MUNICIPAL INCOME TAX FOR ELECTRIC LIGHT COMPANIES AND TELEPHONE COMPANIES, CALENDAR YEARS 2002 - 2005 (IN MILLIONS)

Calendar Year	Total
2002	\$12.3 (1)
2003	15.4 (2)
2004	30.9 (3)
2005	40.9 (4)

(1) Includes \$0.6 million distributed to the Municipal Income Tax Administration Fund.
 (2) Includes \$0.5 million distributed to the Municipal Income Tax Administration Fund.
 (3) Includes revenue from telephone companies. Also includes \$0.2 million distributed to the Municipal Income Tax Administration Fund.
 (4) Includes revenue from telephone companies. Also includes \$0.6 million distributed to the Municipal Income Tax Administration Fund.