

Supplemental Ohio Corporation Franchise Tax Instructions and Supplemental Schedule A-1 for Telephone Companies Tax Year 2006

These supplemental instructions, along with the 2006 Supplemental Schedule A-1 – Nonrefundable Credits for Telephone Companies, were revised on May 10, 2006 to reflect the amendments enacted by Amended HB 530 (HB 530), 126th Ohio General Assembly, effective June 30, 2006. See Note 1, below.

Note 1: HB 530 amended the Ohio Revised Code (R.C.) section 5733.56 telephone company credit for providing programs to aid the communicatively impaired as follows:

- The credit now applies only to tax years (report years) 2005 through 2008. Under prior law the credit applied to report years 2005 and thereafter.
- The credit is now refundable for report years 2006, 2007 and 2008. The 2005 credit, along with unused credit amounts carried forward from 2005, remain nonrefundable. Under prior law the credit was entirely nonrefundable.

Note 2: If on the taxpayer's 2005 franchise tax report the taxpayer claimed the R.C. 5733.56 nonrefundable credit for providing programs to aid the communicatively impaired and if the taxpayer's 2005 franchise tax report does not reflect full recovery of that credit (that is, the adjustment permitted by section 557.04 of Amended Substitute House Bill 66, 126th Ohio General Assembly), the taxpayer may be entitled to a 2005 refund. See on our Web site "New Law Effective June 30, 2005" on the first page of the 2005 Supplemental Ohio Corporation Franchise Tax Instructions for Telephone Companies.

Local exchange telephone companies are subject to the R.C. chapter 5733 corporation franchise tax for tax years (privilege years) 2005 through 2009 (see R.C. 5733.09(A)(3) and 5733.01(G)(2)). The term "telephone company," as used through-out these instructions, means any person "primarily engaged in the business of providing local exchange telephone service, excluding cellular radio service, in this state" (see R.C. 5727.01). Because of their unique nature, telephone companies are subject to franchise tax deduction, add-back, apportionment and credit provisions that do not apply to other taxpayers.

These supplemental franchise tax instructions reflect those franchise tax provisions that apply only to telephone companies. **Except for those items that are specifically covered by these instructions, please refer to the 2006 Ohio corporation franchise tax report (form FT 1120) and the 2006 franchise tax instruction booklet available on our Web site. Attach the completed supplemental schedule A-1 to form FT 1120.**

- **Please indicate that the taxpayer is a telephone company as defined in R.C. 5727.01 by checking the appropriate box in the top right corner of page 1 of form FT 1120.**
- Telephone companies are allowed a "book-tax difference" adjustment equal to the difference between the net book value of the company's asset on Dec. 31, 2003 and the federal adjusted basis of those assets on that date. The adjustment is to be claimed equally in each of the 10 franchise tax years 2010 through 2019. However, because the franchise tax phase-out applies to telephone companies and because the book-tax difference is not scheduled to begin until the tax is fully phased out, the adjustment will never apply unless the law is amended. Since the book-tax difference adjustment does not apply to the 2006 franchise tax, it is not included on the 2006 franchise tax form FT 1120.
- Telephone companies can claim three franchise tax credits not available to other taxpayers:
- The R.C. 5733.57 nonrefundable credit for small telephone companies;

- The R.C. 5733.55 nonrefundable credit for eligible non-recurring 9-1-1 charges; and
- The R.C. 5733.56 credit for providing programs to aid the communicatively impaired. As noted above, this credit is now refundable for report years 2006, 2007 and 2008, but remains nonrefundable for report year 2005. See R.C. 5733.56 as amended by House Bill 530.

The above adjustments and credits are explained in more detail below.

Book-Tax Difference Adjustments

Note: Under current law, the book-tax difference adjustments explained below will never apply to telephone companies because the franchise tax is scheduled to be fully phased-out by tax year 2010 (for those taxpayers, such as telephone companies, that are subject to the phase-out), and the book-tax difference adjustment does not apply until tax year 2010. For more information on the franchise tax phase-out, see "Recent Legislation" beginning on page 1 of the 2006 franchise tax instruction booklet.

- The R.C. 5733.0511 book-tax difference adjustment for telephone companies applies only if (i) the telephone company was subject to R.C. 5727.30 public utility tax for gross receipts received during the period from July 1, 2003 to June 30, 2004 and (ii) for tax years 2003 through 2006 the telephone company's property subject to taxation under R.C. chapter 5727 is assessed using the true value percentages provided for in R.C. 5727.111(B).
- The term "book-tax difference" means the difference, if any, between a qualifying telephone company asset's net book value shown on the qualifying telephone company taxpayer's books and records on Dec. 31, 2003, in accordance with generally accepted accounting principles, and such asset's adjusted basis on Dec. 31, 2003. The book-tax difference may be either a positive number or a negative number.
- If as of Dec. 31, 2003 the net book value of the telephone company's assets exceeds the federal adjusted basis of the assets, then in each of the 10 tax years 2010 through 2019 the telephone company must reduce net income by 1/10 of the book-tax difference. On the other hand, if as of Dec. 31, 2003 the federal adjusted basis of the telephone company's assets exceeds the net book value of its assets, then in each of the 10 years beginning with tax year 2010 the telephone company must increase net income by 1/10 of the absolute value of the book-tax difference. As noted above, under current law the book-tax difference adjustment will never apply to telephone companies.
- The book-tax difference adjustment applies regardless of when the telephone company disposes of its Dec. 31, 2003 assets.

Apportionment and allocation of income. Telephone companies must apportion business income and allocate nonbusiness income by using the same apportionment and allocation provisions applicable to other taxpayers. Thus, for sales factor purposes a telephone company's proceeds from sales of telecommunications services are situsable to Ohio in the proportion to the purchaser's benefit, with respect to the sale, in Ohio to the purchaser's benefit, with respect to the sale, everywhere.

Supplemental Schedule A-1 – Nonrefundable Credits

As noted above, in addition to the nonrefundable credits allowed other taxpayers, telephone companies may claim the following three nonrefundable credits:

1. The credit for small telephone companies with 25,000 or fewer access lines. See R.C. 5733.57 and Supplemental Schedule A-1, line 15;
2. The credit for eligible nonrecurring 9-1-1 charges. See R.C. 5733.55 and Supplemental Schedule A-1, line 16;; and
3. The credit for providing programs to aid the communicatively impaired not used on the 2005 report and carried forward to this report. See R.C. 5733.56 and Supplemental Schedule A-1, line 17.

Like all nonrefundable credits, the above credits must be claimed in the order required by R.C. 5733.98 as set out on supplemental schedule A-1.

Line 15 – Credit for small telephone companies. For report years 2005 through 2009 a “small telephone company” can claim a franchise tax credit equal to a percentage of the amount by which the telephone company’s franchise tax before credits exceeds the public utility gross receipts tax that would have been charged had the law not been changed. Specifically, the credit equals the “applicable percentage” for the tax year (see table below) multiplied by the difference between (1) the franchise tax (including the litter tax) for the tax year before all credits, and (2) the public utility gross receipts tax that would have been charged (had the law not been amended) for the measurement year that ended on June 30 of the calendar year before the franchise tax year.

A small telephone company is a telephone company that (i) existed on Jan. 1, 2003, (ii) had 25,000 or fewer access lines as shown on the company’s annual report filed with the public utilities commission for the calendar year preceding the tax year, and (iii) is an incumbent local exchange carrier under 47 U.S.C. 251(h).

Applicable percentage. The following table list the applicable percentage for the corresponding tax year:

Franchise Tax Year	Applicable %
2005	100%
2006	80%
2007	60%
2008	40%
2009	20%
2010 and thereafter	0%

Of course, there is no credit if the gross receipts tax (that would have been charged had the law not been changed) exceeds the franchise tax. Credit amounts not used in the year generated may not be carried forward or carried back to another year.

Line 16(a) – Credit for eligible nonrecurring 9-1-1 charges. A telephone company is allowed a nonrefundable franchise tax credit equal to the amount of the company’s eligible nonrecurring 9-1-1 charges as defined in R.C. 5733.55(A)(3). A telephone company must claim this credit for the company’s taxable year in which the 9-1-1 service for which it claims the credit becomes available for use. Credit amounts not used in the year generated can be carried forward until fully utilized. See R.C. 5733.55.

The cumulative sum of the 9-1-1 credit amounts allowed for all franchise taxpayers for all franchise tax years is limited to \$15 million. In the franchise tax year in which that limit would be exceeded, each taxpayer claiming the credit will be allowed a uniform percentage of the credit claimed, so that the cumulative credit allowed does not exceed the \$15 million limit. The Department of Taxation will notify telephone companies (through these supplemental franchise tax instructions) of the year in which the department anticipates the limit will be reached.

The franchise tax credit for eligible nonrecurring 9-1-1 charges is substantially the same as the credit for eligible nonrecurring 9-1-1 charges granted under the public utility excise tax (compare R.C. 5733.55 to R.C. 5727.39).

Line 16(b) – Carryforward of unused R.C. 5727.39 credit for eligible nonrecurring 9-1-1 charges. Enter the taxpayer’s unused R.C. 5727.39 credit carryforward remaining after its last public utility excise tax payment for the period of July 1, 2003, through June 30, 2004. A telephone company that was entitled to apply the R.C. 5727.39 credit carry forward against its public utility excise tax liability can claim that amount as a credit against its chapter 5733 corporation franchise tax liability. Because the R.C. 5727.39 credit carryforward is not considered in determining the R.C. 5733.55 \$15 million credit limit, taxpayers must separately list the R.C. 5727.39 credit carryforward on line 16(b).

Line 17 – Credit for providing programs to aid the communicatively impaired. Unused carryforward from 2005. If on its 2005 franchise tax report the taxpayer claimed this credit for costs incurred in providing the telephone service program during its taxable year ending in 2004 and the taxpayer was unable to utilize the credit or a portion of the credit on its 2005 report, the unused 2005 credit amount can be claimed as a non-refundable credits for 2006. Do not claim the unused portion of the 2005 nonrefundable credit as a 2006 refundable credit.

Note: If the taxpayer is claiming this credit for costs incurred for providing the telephone service program during its taxable year ending in 2005, the credit is refundable. See the instructions for Schedule A, line 26 below.

Schedule A, line 26 – Refundable Credits.

Credit for providing programs to aid the communicatively impaired. In addition to the refundable credits available to other taxpayers, telephone companies that provide a telephone service program to aid the communicatively impaired in accessing the telephone network under R.C. 4905.79 can claim a refundable credit equal to the cost incurred by the company for providing the telephone service program during its taxable year.

Note: The R.C. 5733.56 credit for providing programs to aid the communicatively impaired can be claimed as a refundable credit only for tax years 2006, 2007 and 2008. The credit is non-refundable for report year 2005 and for amounts carried forward from 2005 to 2006. See R.C. 5733.56 as amended by Amended Substitute House Bill 530, 126th Ohio General Assembly, effective June 30, 2006. This credit is substantially the same as the credit granted under the public utility excise tax (compare R.C. 5733.56 to R.C. 5727.44).