

Supplemental Ohio Corporation Franchise Tax Instructions and Supplemental Schedule A-1 for Telephone Companies Tax Year 2007

Note: If on the taxpayer's 2006 franchise tax report the taxpayer claimed the Ohio Revised Code section (R.C.) 5733.56 credit for providing programs to aid the communicatively impaired and if the taxpayer's 2006 franchise tax report does not reflect 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 2006 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 and thereafter (see R.C. 5733.09(A)(3)). The term "telephone company," as used throughout 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 2007 Ohio corporation franchise tax report (form FT 1120) and the 2007 franchise tax instruction booklet available on our Web site. Attach the completed supplemental schedules to form FT 1120.**

- Please show 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. Since this adjustment does not apply to the 2007 franchise tax, it is not included on the 2007 franchise tax form FT 1120.

Note: Unless there is a law change, the book-tax difference adjustment explained below will never apply to telephone companies because under current franchise tax law telephone companies are subject to the franchise tax phase-out and the CAT phase-in; the book-tax difference adjustment is not scheduled to begin until tax year 2010; the franchise tax is scheduled to be fully phased-out by tax year 2010. For more information on the franchise tax phase-out, see "Recent Legislation" beginning on page 1 of the 2007 franchise tax instruction booklet

- Telephone companies can claim three franchise tax credits not applicable to other taxpayers. Telephone companies claiming one or more of these credits must complete "supplemental franchise tax schedule A-1 nonrefundable credits for telephone companies" (rather than the schedule A-1 included on the 2007 Ohio corporation franchise tax report, form FT 1120). Supplemental schedule A-1 is included in these supplemental instructions.

The above adjustments are explained in more detail below.

Book-Tax Difference Adjustments

The telephone company book-tax adjustment applies equally to each of the ten franchise tax years 2010 to 2019. However as noted above, by tax franchise tax year 2010 the franchise tax will be fully phase-out for

telephone companies (and for other companies subject to the franchise tax phase-out and CAT phase-in). So, under current law the book-tax difference adjustment as computed below will never apply to telephone companies:

- 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 Chapter 5727 of the Revised Code 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 years beginning in tax year 2010 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 ten 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.
- 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 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

In addition to the 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;
2. The credit for eligible nonrecurring 9-1-1 charges. See R.C. 5733.55; and
3. The credit for providing programs to aid the communicatively impaired. See R.C. 5733.56.

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

Line 15 – Credit for small telephone companies. For franchise tax 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 prior to the franchise tax year.

A small telephone company is a telephone company that existed on Jan. 1, 2003 and 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 is an incumbent local exchange carrier under 47 U.S.C. 251(h).

Applicable percentage. The following table lists 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 that claims the credit will be allowed a uniform percentage of the credit claimed, such 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 on schedule A-1, line 16(b) the taxpayer's unused R.C. 5727.39 credit carryforward. A telephone company that was entitled to carry forward a credit against its public utility excise tax liability under 5727.39 of the Revised Code is entitled to carry forward any amount of that credit remaining after its last public utility excise tax payment for the period of July 1, 2003, through June 30, 2004, and claim that amount as a credit against its Chapter 5733 corporation franchise tax liability. Because the R.C. 5727.37 credit carryforward is not considered in determining the R.C. 5733.55 \$15 million credit limit, taxpayers must separately list the R.C. 5727.37 credit carryforward on line 16(b).

Line 17 – Credit for providing programs to aid the communicatively impaired. A telephone company that provides a telephone service program to aid the communicatively impaired in accessing the telephone network under R.C. 4905.79 can claim a nonrefundable credit against the Chapter 5733 corporation franchise tax. The amount of the credit is the cost incurred by the company for providing the telephone service program during its taxable year, excluding any costs incurred before July 1, 2004. Credit amounts not utilized in the year generated can be carried forward until fully utilized.

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).