Ohio Corporation Franchise Tax
Electric Company and Combined Company
Instructions for Supplemental Schedules
Tax Year 2009

Because of their unique nature, electric companies and combined companies are subject to Ohio corporation franchise tax deduction, add-back, apportionment, credit and tax computation adjustments that do not apply to other taxpayers. These supplemental franchise tax schedules and instructions reflect the franchise tax provisions that are unique to electric companies.

An "electric company" is defined as any person engaged in the business of generating, transmitting or distributing electricity within Ohio for use by others, but excludes a "rural electric company." See R.C. 5733.04(P), 5727.01(D)(3) and 5727.01(C).

A "rural electric company" is defined as any nonprofit corporation, organization, association, or cooperative engaged in the business of supplying electricity to its members or persons owning an interest therein in an area the major portion of which is rural. See R.C. 5733.04(P), 5727.01(D)(3) and 5727.01(C).

A "combined company" is defined as any person engaged in the activity of an electric company or rural electric company that is also engaged in the activity of a heating company or a natural gas company, or any combination thereof. See R.C. 5733.04(P) and 5727.01(L). The term "combined company," as used throughout these supplemental instructions, is not to be confused with a company that is a member of a combined franchise tax return pursuant to R.C. 5733.052. Unless otherwise stated in these supplemental instructions, the term "electric company" refers to both an electric company and a combined company.

Electric companies and combined companies were first subject to the Ohio Revised Code (R.C.) Chapter 5733 corporation franchise tax for tax year (privilege year) 2002. **As a result of the franchise tax phase-out, electric companies will not be subject to the franchise tax after tax year 2009.** See R.C. 5733.09 and 5733.01(G)(2).

Except for those adjustments that are specifically covered by these instructions, please refer to the 2009 Ohio corporation franchise tax report (form FT 1120) and the 2009 franchise tax instructions. Attach the completed supplemental schedules to form FT 1120. Form FT 1120, the franchise tax instruction booklet and supplemental schedule A-1 are available on our Web site:

tax.ohio.gov

- **Please indicate that the taxpayer is an electric company by checking the appropriate box on page one (the top right side) of form FT 1120.**
- Electric companies must complete supplemental schedules B, C and A-1 rather than the corresponding schedules on the 2009 Ohio corporation franchise tax report, form FT 1120.
- Electric companies must complete the sales factor of the form FT 1120 schedule D apportionment ratio by situsing proceeds from sales of electricity and proceeds from sales of transmission and distribution services based on the instructions on page 3 of these supplemental instructions.
- Combined companies should compute the tax on Ohio franchise tax form FT 1120, schedule A, line 17 based on the instructions on page 4 of these supplemental instructions.

Adjustments for Book-Tax Differential

As explained in detail below, upon the sale or other taxable disposition of any asset shown on Dec. 31, 2000 on an electric company's books and records kept in accordance with generally accepted accounting principles (GAAP), an electric company must increase or decrease its income by the difference between the asset's net book value on Dec. 31, 2000 and the asset's federal adjusted basis on Dec. 31, 2000.

Assets shown on an electric company's GAAP books and records on Dec. 31, 2000 are known as "qualifying assets." The sale or other taxable disposition of a qualifying asset is a "qualifying taxable event." The difference between a qualifying asset's net book value on Dec. 31, 2000 and such asset's adjusted basis on Dec. 31, 2000 is the asset's "book-tax differential." (The statutory definitions of the terms "qualifying asset," "qualifying taxable event" and "book-tax differential" begin on page 2 of these supplemental instructions.)

Book-tax differential = NBV* – Federal adjusted basis

*NBV = Net Book Value

An asset's book-tax differential can be either positive or negative. If an asset's book-tax differential is negative (that is, the asset's net book value on Dec. 31, 2000 is less than the asset's adjusted basis on that date), then in determining Ohio taxable income the book-tax differential is added to federal taxable income as a positive number upon the sale or other taxable disposition of the asset. If an asset's book-tax differential is positive (that is, the asset's net book value on Dec. 31, 2000 is greater than the asset's adjusted basis), then in determining Ohio taxable income the book-tax differential is deducted from federal taxable income upon the sale or other taxable disposition of the asset.

As noted above, although a qualifying asset's book-tax differential is determined as of Dec. 31, 2000, the book-tax differential adjustment to income is not made until the qualifying asset is sold or disposed of in a qualifying taxable event (because a transaction resulting in the recognition of gain or loss for federal income tax purposes). **The book-tax differential adjustment is not made on the disposal of a qualifying asset in a transaction in which gain or loss is deferred** (a transaction that results in the deferral of gain or loss is not a qualifying taxable event). Thus, if after Dec. 31, 2000 an electric company trades-in a qualifying asset for a replacement asset and the gain or loss is deferred for federal income tax purposes, then the book-tax differential is not recognized at that time. However, the replacement asset then becomes a qualifying asset, and the book-tax differential of the replacement asset equals the book-tax differential of the asset traded-in (the book-tax differential for the replacement asset does not include any additional consideration paid for the replacement asset). Upon the sale or other disposition of the replacement asset in a qualifying taxable event, an electric company must adjust its net income for the replacement asset's book-tax differential (that is, the carryover book-tax differential from the asset traded-in).

The book-tax differential adjustment applies to the sale of a qualifying asset in a transaction in which gain or loss is recognized for federal income tax purposes. However, if no gain or loss is recognized on the sale or other disposition of a qualifying asset in a qualifying taxable event solely because at the time of disposition the amount realized equals the asset's adjusted basis, the book-tax differential adjustment nevertheless applies (see R.C. 5733.0510(B)(4)). Furthermore, if for federal income tax purposes an electric company uses the installment method of accounting in recognizing gain from the sale of a qualifying asset, the franchise tax book-tax differential adjustment for that asset must be made in proportion to the gain recognized for federal income tax purposes in each corresponding taxable year in which the gain is recognized.

The book-tax differential adjustment applies only if either (1) the electric company was subject to and paid the Ohio excise tax for gross receipts received during the period May 1, 2000 through April 30, 2001, or (2) the electric company received the asset in a tax-free reorganization from an electric company that was subject to and paid the excise tax for gross receipts received during the period May 1, 2000 through April 30, 2001. Assets acquired by the taxpayer from another electric company that was a party to the reorganization and that was subject to and paid the excise tax for gross receipts received during the period May 1, 2000 through April 30, 2001 have a carryover book-tax differential and are deemed to have been acquired by the taxpayer on the same date as actually acquired by the other electric company.

If the gain or loss from the sale or other taxable disposition of a qualifying asset is business income, then the asset's book-tax differential is apportionable. On the other hand, if the gain or loss from the sale or other taxable disposition of a qualifying asset is nonbusiness income allocable to Ohio, then the book-tax differential is allocable to Ohio. If the gain or loss from the sale or other taxable disposition of a qualifying asset is nonbusiness income allocable **outside Ohio,** then the book-tax differential adjustment does not apply with respect to that asset.

Caution: All income, gain, loss and expense is presumed to be apportionable business income. Accordingly, for taxable years ending on or after June 26, 2003 an electric company's gains and losses from the sale of capital assets and Internal Revenue Code (I.R.C.) section 1231 assets along with the asset's book-tax differential adjustment will generally be apportioned as business income. A taxpayer reporting any allocable income must attach to the report (i) a detailed statement setting forth support which rebuts that presumption, (ii) a list of the states for which the taxpayer treats the income as business income and (iii) the reasons for such treatment in the other state(s).

Supplemental Schedule B

Line 1(e) – Addition for book-tax differential (for qualifying assets whose book-tax differential is negative and apportionable) – If the recognized gain or loss with respect to a qualifying asset sold or disposed of during the taxable year in a qualifying taxable event is apportionable business income or loss and the asset's book-tax differential is negative (that is, if the asset's book value as of Dec. 31, 2000 determined in accordance with GAAP is less than the asset's adjusted basis as of that date), then the electric company must increase its income by the absolute value of the amount of the book-tax differential for that qualifying asset. The adjustment applies regardless of the asset's location at the time of the qualifying taxable event and regardless of the asset's location on Dec. 31, 2000. Enter on line 1(e) as a positive number the sum of the negative book-tax differential amounts for those qualifying assets for which the gain or loss from the sale or other taxable disposition during the taxable year is apportionable.

Line 2(j) – Deduction for book-tax differential (for qualifying assets whose book-tax differential is positive and apportionable) – If the recognized gain or loss with respect to a qualifying asset sold or disposed of during the taxable year in a qualifying taxable event is apportionable business income or loss and the asset's book-tax differential is <u>positive</u> (that is, if the asset's book value as of Dec. 31, 2000 determined in accordance with GAAP exceeds the asset's adjusted basis as of that date), then the electric company must reduce its income by the amount of the book-tax differential for that qualifying asset. The adjustment applies regardless of the asset's location at the time of the qualifying taxable event and regardless of the asset's location on Dec. 31, 2000. Enter on line 2(j) as a positive number the sum of the positive book-tax differential amounts for those qualifying assets for which the gain or loss from the sale or other taxable disposition during the taxable year is apportionable.

Supplemental Schedule C
Allocable Income

Line 2 – Allocable negative book-tax differential – If the recognized gain or loss with respect to a qualifying asset sold or disposed of during the taxable year in a qualifying taxable event **is nonbusiness gain or loss <u>allocable to Ohio</u>** and the asset's book-tax differential is <u>negative,</u> then the electric company must increase its net income allocable to Ohio by the absolute value of the book-tax differential for that qualifying asset. Enter on line 2 as a **positive number** in column 1 (within Ohio) the sum of the negative book-tax differential amounts for those qualifying assets the gain or loss from whose sale or other taxable disposition during the taxable year is allocable to Ohio. Make no entry in column 2 (total everywhere).

Line 3 – Allocable positive book-tax differential – If the recognized gain or loss with respect to a qualifying asset sold or disposed of during the taxable year in a qualifying taxable event is **nonbusiness gain or loss <u>allocable to Ohio</u>** and the asset's book-tax differential is <u>positive,</u> then the electric company must decrease its net income allocable to Ohio by the book-tax differential for that qualifying asset. Enter on line 3 as a **negative number** in column 1 (within Ohio) the sum of the positive book-tax differential amounts for those qualifying assets the gain or loss from whose sale or other taxable disposition during the taxable year is allocable to Ohio. Make no entry in column 2 (total everywhere). As stated earlier, **all income, gain, loss and expense is presumed to be apportionable business income.**

Note: If gain or loss with respect to the sale or other taxable disposition of a qualifying asset is nonbusiness gain or loss **allocated outside Ohio,** the book-tax differential adjustment does not apply with respect to that asset.

Definitions applicable to book-tax differential adjustment (R.C. 5733.0510(A))

"Qualifying taxpayer" means either of the following:

(a) a person that is an electric company or a combined company, but only if the person was subject to and paid the tax imposed by R.C. 5727.30 for gross receipts received during the period of May 1, 2000 through April 30, 2001; or

(b) any taxpayer not described in division (A)(1)(a) [see the paragraph above] of this section if a person described in division (A)(1)(a) of this section transfers all or a portion of its assets or equity directly or indirectly to the taxpayer, the transfer occurred as part of an entity organization or reorganization, or subsequent entity organization or reorganization, and the gain or loss with respect to the transfer is not recognized in whole or in part for federal income tax purposes under the I.R.C. on account of a transfer as part of an equity organization or reorganization, or subsequent organization or reorganization. See R.C. 5733.0510(A)(1).

"Qualifying asset" means any asset shown on the qualifying taxpayer's books and records on Dec. 31, 2000, in accordance with generally accepted accounting principles, including the cost of, or any portion of the cost of, any asset acquired after Dec. 31, 2000, where such asset was acquired as a result of a tax-free or tax-deferred exchange of a qualifying asset. See R.C. 5733.0510(A)(3).

"Qualifying taxable event" means any event resulting in the recognition for federal income tax purposes of gain or loss in connection with any direct or indirect sale, direct or indirect exchange, direct or indirect transfer, or direct or indirect retirement of any qualifying asset. See R.C. 5733.0510(A)(2).

"Book-tax differential" means the difference, if any, between an asset's net book value shown on the qualifying taxpayer's books and records on Dec. 31, 2000, in accordance with generally accepted accounting principles, and such asset's adjusted basis on Dec. 31, 2000. The book-tax differential may be a negative number. See R.C. 5733.0510(A)(5).

"Qualifying regulatory asset" means those qualifying assets that, as of Dec. 31, 2000, are no longer included in federal energy regulatory commission uniform system of accounts 101 through 106 or are deferred expenses for operation or maintenance, or deferred costs associated with leaseback transactions on generating units, that have been authorized by a regulatory agency for recovery from customers in a future period and that, as of Dec. 31, 2000, are subject to transition cost recovery under R.C. Chapter 4928 or similar laws of another state. See R.C. 5733.0510(A)(6).

Note: The "qualifying regulatory assets" associated with a qualifying asset are consider disposed of on the same date that the "qualifying asset" is disposed of. Thus, the book-tax differential for qualifying regulatory assets is recognized for franchise tax purposes on the same date that the book-tax differential is recognized for the associated qualifying assets even though the qualifying regulatory assets may not have been sold or disposed of in a taxable transaction.

Supplemental Schedule B – Valuation Limitation Adjustment

Lines 1(a) and 2(b) – Valuation limitation on losses and gains from capital assets and 1231 assets – Make no valuation limitation entry on schedule B, lines 1(a) or 2(b). The R.C. 5733.04(I)(3) "valuation limitation" adjustment applicable to IRC section 1231 assets and capital assets does <u>not</u> apply to "qualifying assets." That is, in determining its net income, an electric company may not deduct that portion of the gain (and is not required to add-back that portion of a loss) from the sale of qualifying assets that are 1231 assets or capital assets. (Valuation limitation is that portion of a gain or loss from the sale of 1231 assets and capital assets occurring prior to the first taxable year on which the tax provided for in R.C. 5733.06 is computed on the corporation's net income.) Furthermore, the valuation limitation adjustment does <u>not</u> apply to an electric company's assets that are not qualifying assets because those assets will <u>not</u> have been acquired ". . . prior to the first taxable year on which the tax provided for in 5733.06 of the Revised Code is computed on the corporation's net income" (the taxable year ending in 2001). See R.C. 5733.04(I)(3).

Schedule D Apportionment

Sales factor. Although the supplemental schedules for electric companies do not include a supplemental schedule D apportionment schedule, there are special sales factor situsing provisions applicable to sales of electricity and to sales of transmission and distribution services (see R.C. 5733.059). Please follow the instructions below to situs on schedule D the company's revenue from sales of electricity and from sales of transmission and distribution services.

1. Revenue from electricity sales:
   - Sales of electricity are sitused within and without Ohio based on where the customer consumes the electricity. That is, sales of electricity are sitused to Ohio to the extent that the customer <u>consumes</u> the electricity in Ohio.
   - If the taxpayer sells the electricity to a related member[1]and the related member sells the electricity to a customer, the taxpayer's sale to the related member is sitused to Ohio to the extent that the related member's customer <u>consumes</u> the electricity in Ohio.
   - Sales of electricity are sitused to Ohio if the seller or the seller's related member <u>delivers</u> the electricity to a location in Ohio or delivers the electricity exactly to the border of Ohio and another state.
   - Sales of electricity are sitused to Ohio if the seller or the seller's related member <u>directs the delivery</u> of the electricity to a location in Ohio or directs the delivery of the electricity exactly to the border of Ohio and another state.

2. Sales revenue from the <u>transmission</u> of electricity is sitused within and without Ohio based on the ratio of wire miles of the taxpayer's transmission lines within Ohio to wire miles of the taxpayer's transmission lines everywhere. Transmission wire miles are weighted for the voltage capacity of each line.

3. Sales revenue from the <u>distribution</u> of electricity is sitused within and without Ohio based on the ratio of wire miles of the taxpayer's distribution lines within Ohio to wire miles of the taxpayer's distribution lines everywhere. However, unlike transmission line wire miles, distribution line wire miles are not weighted for the voltage capacity of each line.

4. If a contract for the sale of electricity includes the seller's or the seller's related member's obligation to transmit or distribute the electricity and the sales contract <u>separately identifies</u> the price charged for the transmission or distribution services, the price charged for the transmission and distribution of electricity is sitused within and without Ohio in accordance with the provisions for situsing transmission and distribution revenue set forth in #2 and #3, above. The remaining portion of the sales price, that is, the sale of the electricity itself is sitused within and without Ohio in accordance with electricity sales provision set forth in #1, above.

5. If a contract for the sale of electricity includes the seller's or the seller's related member's obligation to transmit or distribute the electricity and the sales contract does <u>not</u> separately identify the price charged for the transmission or distribution services, the entire price charged is sitused within and without Ohio in accordance with electricity sales provision set forth in #1, above.

Sales, other than sales of electricity and transmission and distribution services are sitused within and without Ohio in accordance with R.C. 5733.05(B)(2)(c) and the sales factor instructions in the franchise tax instruction booklet.

Supplemental Schedule A-1 – Nonrefundable Credits and Grants

With two notable exceptions, an electric company is entitled to the same franchise tax credits and grants as other taxpayers:

- An electric company is entitled to a credit for using Ohio coal at its coal-fired electric generating units. The credit for using Ohio coal is not available to taxpayers that are not electric companies.
- The R.C. 122.172 and 122.173 7.5% – 13.5% grant for purchases of new manufacturing machinery and equipment (formerly the R.C. 5733.33 7.5% – 13.5% manufacturer's credit) has only limited applicability to electric companies.

Electric Company Credit for Using Ohio Coal (R.C. 5733.39) –
Note: Among other provisions, House Bill 119, 127th Ohio General Assembly extended the credit available to electric companies for using Ohio coal to generate electricity. The credit now applies to Ohio coal burned in a coal-fired electric generating unit before Jan. 1, 2010 (under prior law the credit applied to Ohio coal burned in a coal-fired electric generating unit before Jan. 1, 2008). For tax years 2006, 2007, 2008 and 2009 the credit is computed at the rate of $1 per ton of Ohio coal burned during the taxable year ending immediately preceding the tax year.

The credit is allowed only if both of the following conditions are met during such taxable year:

1. The coal-fired electric generating unit is owned and used by the company claiming the credit or leased and used by that company under a sale and leaseback transaction.
2. A compliance facility, as defined in R.C. 5733.39(A), is attached to, incorporated in or used in conjunction with the coal-fired generating unit.

Credit amounts not used in the tax year following the taxable year in which the credit was generated can be carried forward for three taxable years. Enter the credit on supplemental schedule A-1, line 11.

The 7.5% – 13.5% Grant for Purchases of New Manufacturing Machinery and Equipment (R.C. 5733.33, 122.172 and 122.173). The 7.5% – 13.5% manufacturer's grant does not apply to transmission and distribution equipment, and the grant does not apply to generating equipment if 50% or more of the electricity that the property generates is consumed, during the 120-month period commencing with the date the property is placed in service, by persons that are not related members to the person who generates the electricity. For additional information regarding the grant, please refer to the 2009 franchise tax instructions for schedule A, line 23.

Schedule A – Computation of Total Tax

Although the supplemental schedules for electric companies do not include a supplemental schedule A, combined electric companies are entitled to tax computation-reductions that do not apply to other taxpayers.

Schedule A, line 17 – Tax due – If the electric company is <u>not</u> a combined company, enter on schedule A, line 17 the greater of the amount shown on schedule A, line 14 or the amount shown on schedule A, line 16, but not less than the minimum fee.

If the electric company is a combined company that paid Ohio public utility excise tax on its gross receipts as a natural gas company or as a heating company, then the taxpayer is entitled to a franchise tax reduction (see R.C. 5733.06(J)). The reduction applies to the tax on the net income base and to the tax on the net worth base as follows:

1. Net Income Base

A. Multiply the tax on the net income base (schedule A, line 14) by the ratio of total taxable gross receipts from public utility activity, other than as an electric company, to total gross receipts from all sources; and

B. Reduce the tax on the net income base (schedule A, line 14) by the lesser of the amount computed in 1.A. above, or the excise tax paid for the year upon which the taxable gross receipts are measured immediately preceding the tax year.[2]

2. Net Worth Base

A. Multiply the tax on the net worth base (schedule A, line 16) by the ratio of total taxable gross receipts from public utility activity, other than as an electric company, to total gross receipts from all sources; and

B. Reduce the tax on the net worth base (schedule A, line 16) by the lesser of the amount computed in 2.A. above, or the excise tax paid for the year upon which the taxable gross receipts are measured immediately preceding the tax year.

3. Enter on schedule A, line 17 the greatest of the following:

A. The amount determined in 1.B. above;
B. The amount determined in 2.B. above; or
C. The minimum fee.

Combined Franchise Tax Report – Form FT 1120C

An electric company can join in the filing of a combined franchise tax report (form FT 1120C) with related corporations whether or not those related corporations are electric companies provided that the ownership requirements set forth in R.C. 5733.052 and on form FT 1120C are met.

Although the department has not developed a combined report form or combined report schedules specifically applicable to electric companies that make the book-tax differential adjustments, electric companies included in a combined report can nevertheless make those adjustments on form FT 1120C, schedule B (combined) by lining out any unused addition and any unused deduction and substituting the book-tax differential adjustment.

Please note that the franchise tax deduction, add-back, apportionment, credit and tax computation adjustments set forth in these supplemental instructions for electric companies do not apply to those members of a combined franchise tax report that are not electric companies. For example, the book-tax differential adjustment does not apply to any member of the combined report that is not an electric company. (However, the effects of the electric company's book-tax differential adjustment are prorated to all members of the combined report by virtue of the "proportionate share of the factors" mechanism set forth in R.C. 5733.052(E)).

Endnotes

[1] "'Related member' means a person that, with respect to the taxpayer during all or any portion of the taxable year, is a 'related entity' as defined in division (I)(12)(c) of R.C. 5733.04, is a component member as defined in I.R.C. section 1563(b), or is a person to or from whom there is attribution of stock ownership in accordance with I.R.C. section 1563(e) except, for purposes of determining whether a person is a related member under this division, '20%' shall be substituted for '5%' wherever '5%' appears in I.R.C. section 1563(e)." See R.C. 5733.042(A)(6).

[2] For example, the year upon which the taxable gross receipts are measured immediately preceding franchise tax year (privilege year) 2009 is the year May 1, 2007 to April 30, 2008 even if the public utility has a calendar year end taxable year. Thus, the franchise tax reduction for tax year 2009 is limited to the excise tax that was paid for gross receipts measured during the period May 1, 2007 to April 30, 2008.