TESTIMONY IN SUPPORT OF HOUSE BILL 466

Ohio Senate Ways & Means Committee
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Good afternoon Chairman Peterson, Vice Chairman Beagle, Ranking member Tavares and members of the committee. Thank you for receiving this testimony offered in support of H.B. 466. My name is Tony Ehler and I represent both The Ohio Automobile Dealers Association and The Ohio Association of Broadcasters. I am a tax attorney at the Vorys Law Firm in Columbus where I chair the State and Local Tax Group. I have practiced professionally in the area of Ohio sales tax law for nearly 30 years. I have served as chairman of the taxation committees for both the Columbus and Ohio State Bar Associations. I advise clients nearly every day on Ohio sales tax matters and I am a frequent speaker at sales tax seminars.

The sales tax is Ohio's primary source of state tax revenue. In FY 2015, it raised over $10 billion. Approximately 20% of this goes to Ohio counties and transit authorities. It is a valuable revenue tool that funds the common good. But, the sales tax can lose its effectiveness if it is permitted to morph in ways that undermine the very economic activity on which it relies…that is, when it is applied in a way that chills retail sales. We support H.B. 466 because it continues Ohio's promotion of retail sales. We support it because it counters the Department of Taxation's interpretation of a statute in a way that taxes digital advertising.

We believe some contextual background would help in understanding the current need for H.B. 466. Ohio sales tax applies only to the last transaction in a line of sales that brings goods and services to retail customers. When a purchaser intends to resell a thing that is purchased, then the purchase is not taxable because it was intended to be resold in some form.

E.g., R.C. 5739.01(E) and 5739.02(B)(42)(a). Ohio's tax system imposes sales tax only on the final retail sale. R.C. 5739.02. It is easy to understand that this retail sale carries the highest price (and thereby generates the most sales tax) because it includes all labor, material and profit that has been added along the path of commerce. This system helps avoid a pyramid effect of the sales tax.

This structure of the Ohio sales tax has been shaped and guided by legislation with various objectives including: growing and protecting Ohio jobs; promoting business growth and commerce; exempting select necessities of life such as food, rent, pharmaceuticals and public utility services. Ohio's tax code historically has encouraged retail sales which has allowed the state to collect the sales tax revenue that results. It's a tax code that reflects choices made by the General Assembly to balance social and economic factors with governmental needs and the rules of the road are well established.

One such rule is that advertising services have never been subject to Ohio sales tax. The policy reason for this "no tax" result is clear. The expense for placing advertisements invariably finds its way into the retail price of the things advertised and on which Ohio generally imposes a sales tax. Thus, that value is taxed when the retail sale of the advertised item is taxed.

Despite the extra cost, advertising promotes consumer demand and fuels retail sales. By not taxing advertising services, Ohio avoids pyramiding the tax. It also encourages commerce and it promotes retail sales. This is good for competition in the market, consumer selection and it increases sales. As such, advertising increases sales tax revenue relied on by state and county governments for the common good. This has been the purpose and design of the Ohio sales tax since its first day and it reflects the balance struck by the General Assembly between encouraging commerce and taxing it.

In December 2015, the Ohio Department of Taxation announced a revised interpretation of a 25 year old statute that undermines this balance. The Department announced that it believes fees charged for digital advertising accessed by consumers via the internet is taxable as an "electronic information service." R.C. 5739.01(Y)(1)(c). *Compare* Ohio Dept. of Taxation Information Release ST1999-04, On-line Services and Internet Access, January, 1999 *with* Updated Version, December, 2015. Fees for placing advertising on television and radio and in print remain nontaxable.

This recent interpretation of statutory language by the Department focusing on digital advertising is highly debatable as a technical language matter. But, beyond that, the Department's recent tax interpretation is based on a statute that is 25 years old. Indeed, this interpretation comes nearly 17 years after the Department's first Informational Release on the same statute which was completely silent on this specific topic. This raises the practical question of the Department's moral and legal authority to impose a tax 25 years after the fact.

To be fair, what we probably are seeing in the Department's interpretation is an attempt to address changes in advertising placement. Prior to 2000, there was very little digital advertising. The Department's current interpretation focuses on changes in advertising delivery over the internet.

But, despite some delivery changes, the essence of digital advertising is not really new. The art and goal of delivering messages from advertisers to potential customers is centuries old. In Ohio, fees for advertising placement have never been treated by the General Assembly as a taxable service. Digital advertising on the internet has been around for well over a decade. Yet, it was only five months ago that the Department issued its revised Informational Release.

It appears further that the Department is interpreting the tax code in a manner inconsistent with its previous treatment of other technology changes. For example, Ohio has always treated canned software as tangible personal property for sales tax purposes. This is important because the sales tax applies to retail sales of tangible personal property. And, in previous times, software was delivered on tape or disk with a paper copy of the code. These items combined to form tangible personal property no different than a CD or a hard cover book and gave the Department the right to impose sales tax. However, when the paper delivery was eliminated and software purchasing shifted to delivery via computer downloads instead of tapes, the Department pivoted and announced that canned software would continue to be treated as tangible personal property and taxed as such regardless of the method of delivery. The delivery method of the software did not change its essence for sales tax purposes.

The same should be true for advertising services. These services have never been subject to sales tax. The method of delivering the advertising message does not change its essence or true object as an advertising service. Similarly, the method of delivery should not change policy that encourages retail sales and avoids tax pyramiding and it should not change the "no-tax" result that always has applied to advertising services.

H.B. 466 is necessary to clarify Ohio's sales tax laws and to prevent an unintended tax. H.B. 466 continues the policy of encouraging commerce and promoting retail sales. This is good both for the marketplace and consumer choice. It generates more retail sales and produces more sales tax.

The Ohio Automobile Dealers Association and the Ohio Association of Broadcasters asks the Committee to preserve the intent and balance of the tax code by passing

H.B. 466 and keeping digital advertising placement services as nontaxable the same no-tax position granted to advertising in television, on radio and in print.

Thank you.