



**Proponent Testimony
Tax Commissioner Joe Testa
Senate Bill 22
February 20, 2018**

Chairman Schaffer, Vice Chairman Scherer, Ranking Member Rogers, and members of the House Ways & Means Committee, I am Joe Testa, Commissioner of the Ohio Department of Taxation. Thank you for the opportunity to provide testimony in support of Senate Bill 22, legislation that incorporates certain federal tax changes into the Ohio Revised Code.

As you may recall from last year, House Bill 11 was enacted to incorporate into Ohio law changes to the Internal Revenue Code made from February 14, 2016 to March 8, 2017. Since H.B. 11's enactment, federal income tax law has been further amended and S.B. 22 is necessary to conform Ohio law with those changes.

The following two federal changes apply to Ohio income taxes for Tax Year 2017 (the returns currently being filed with the Department):

- “Combat Zone” designation for military services in the Sinai Peninsula of Egypt
- Temporary 100% expensing for *used* business assets

The Bipartisan Budget Act of 2018, signed February 9, 2018, contains several provisions that apply to Ohio income taxes for Tax Year 2017, but the provisions are simply extensions of deductions, exclusions, and waivers that otherwise would have expired after Tax Year 2016.

Ohio's income tax, like nearly all state income taxes, relies heavily on coordination with federal tax law. The first line of the Ohio income tax form asks taxpayers to enter their Federal Adjusted Gross Income (FAGI) from the Federal Form 1040. Having the same starting definition of income as the federal government greatly simplifies the preparation and administration of state income tax for taxpayers, tax preparers, state tax officials, and school districts that impose income taxes.

In the absence of enactment of S.B. 22, taxpayers would be required to make adjustments when filing their Ohio income tax returns to resolve the discrepancy between current and prior federal law. The taxpayer's FAGI would be too low, necessitating the add back of the disallowed federal deductions and exclusions on the “miscellaneous federal tax adjustments” line on the Ohio return. Such adjustments would introduce complexity and thus potentially taxpayer errors. They also would result in revenue gains from increased Ohio income tax.

Significant federal tax law changes were also recently made for Tax Years 2018 to 2025. The Tax Cuts and Jobs Act of 2017 (“H.R. 1”) was passed in late December 2017. H.R. 1 makes major changes to federal corporate and individual income taxes.

Ohio no longer has a corporate income tax which means the corporate changes have no impact on Ohio. While Ohio does have an individual income tax, many income tax changes contained in H.R. 1 have little to no impact on Ohio’s income tax.

In determining which federal changes impact Ohio’s revenue from individual income tax, the key issue is whether the change impacts the calculation of FAGI. The items that are “above the line” impact FAGI (page one of the Federal Form 1040); those items that are “below the line” (page two of the Federal Form 1040) do not impact FAGI, and thus **do not** impact Ohio’s income tax. Examples of changes that **do not** impact Ohio’s income tax include:

- Increase of the “standard deduction” amounts
- Reduction in individual income tax rates
- The federal deduction for pass-through entity income

One issue that could impact Ohio income tax revenue is the temporary change affecting federal personal exemptions. Under H.R. 1, personal exemptions are suspended for Tax Years 2018 through 2025; therefore no dependents will be claimed on the federal tax return. State law requires a dependent be claimed on the federal return in order to be claimed on the Ohio return. The Department is proposing an amendment to similarly suspend this state requirement in order to prevent an increase in Ohio personal income tax liability.

H.R. 1 also expanded the definition of eligible higher education expenses to include tuition for kindergarten through 12th grade. The Ohio Tuition Trust Authority administers Ohio’s 529 plan, a federal program. The Department of Higher Education has requested language to be included so that Ohio’s definitions match the new federal definitions. Remember that, under current Ohio law and beginning with Tax Year 2018 to be filed in Calendar Year 2019, taxpayers can deduct up to \$4,000, per beneficiary, in contributions made to an Ohio 529 plan. With the expansion of eligible expenses, the number of Ohio taxpayers making contributions to the Ohio 529 plan and taking the Ohio tax deduction is expected to grow.

The Department is also requesting language addressing three other provisions:

- The Internal Revenue Service has revised its Publication 1075, *Tax Information Security Guidelines for Federal State and Local Agencies, Safeguards for Protecting Federal Tax Returns and Return Information*. Specifically, under Internal Revenue Code Section 6103(p)(4)(C), any individual who accesses federal taxpayer information (FTI) must undergo a background investigation utilizing the fingerprinting program run by the Federal Bureau of Investigation (FBI). This mandate applies to certain employees who perform various functions involving FTI at the Ohio Department of Taxation, the Ohio Department of Job and Family Services, the Ohio Department of Medicaid, the Ohio Department of Administrative Services, and the Ohio Attorney General’s Office. The FBI requires agencies to have statutory authority to request background checks. No such

authority currently exists. The proposed language would be added to ORC Chapter 124: Department of Administrative Services – Personnel and would apply to any and all state employees with access to FTI.

- Streamlining business income deduction filing. When determining whether an individual is entitled to take the business income deduction, the Department must establish that the individual holds an ownership interest of 20% or more in the business. That information is not currently provided when the Ohio Form 1040 is filed. For example, in situations where a pass-through entity (PTE) investor is paid wages or guaranteed payments by a professional employer organization (PEO), the investor’s tax return would suspend in processing because of the conflict between the reported W-2 wages and the business income deduction, resulting in correspondence between the Department and the investor, requesting proof of the investor’s ownership in the PTE. Requiring the investor to submit an Ohio Form K-1 at the time of filing the tax return claiming the business income deduction will eliminate the need for correspondence related to proof of ownership and will prevent the delay in processing the tax return and payment of any refund due.
- Clean-up language for both the aviation fuel tax and motor fuel tax.
 - The Federal Aviation Administration has required states to report on how much state and local tax is derived from the sale of aviation fuel and subsequently show how much state and local funding is provided to the airports in total. Aviation fuel dealers are now required to file Schedule 10B (Sold to Propel Aircraft) which is due the 23rd of each month, however this date does not match the filing date for the motor fuel tax return (the last day of the month). The population of taxpayers is the same; to make filing more convenient and efficient for the aviation fuel dealers, the Department requests these dates be harmonized.
 - Current law incorrectly states that aviation fuel dealers who purchase aviation fuel for **consumption** are required to file the new monthly schedule; it should read for **resale**. The language also does not have the same “failure to file” language as statute provides for motor fuel dealers.
 - In last year’s introduced version of the transportation budget, there was a provision that moved the incidence of the motor fuel tax to the “rack” or terminal from the wholesale level. This provision was stripped, but two definitions remained. The definitions for “terminal” and “consumer” need to be reinstated to their prior definitions.

S.B. 22 conforms to federal tax law changes that were signed into law - since the enactment of the last conformity bill, H.B. 11. These changes merely update Ohio tax law to reflect current federal tax provisions used in the computation of FAGI. In the absence of conformity, some Ohio taxpayers’ liability would increase. By conforming to federal changes, you will keep tax preparation and administration efficient. The attachment to this testimony summarizes the fiscal impact of the major items. The impact of three additional items cannot be determined; however, two of these items are expected to have a revenue loss for Ohio. Accepting the other recommended amendments would also achieve greater efficiency and clarity.

Thank you for your time and consideration.