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Tim Schaffer

State Representative, 77th House District

Senate Ways and Means Committee House Bill 430—Sponsor Testimony Wednesday, February 28, 2018

Chairman Eklund, Vice Chairman Terhar, Ranking Member Williams, and members of the Senate Ways and Means Committee, thank you for the opportunity to present sponsor testimony on House Bill 430.

House Bill 430 addresses a critical and time sensitive issue for the Ohio oil and gas industry by re-affirming statute since 1934 and practice, clarified in 1960, on the collection of sales tax on oil and gas operations. This bill clarifies and narrows the scope of already existing exemptions.

In 1960, the Ohio Department of Taxation reached out to the Ohio Oil and Gas Association in an effort to better understand what had been subject to sales tax and what had not. At that time, the Ohio Department of Taxation determined that items used directly in the exploration of oil and gas are exempt from sales tax collection. This determination reaffirmed the intent of the sales tax code created in 1934, as well as a 1958 report, which treated the oil and gas industry similar to other business ventures where sales tax is assessed and collected at the final point of sale--not before. The result of this conversation was a memorandum, written by DoT Commissioner Stanley Bowers at the time, which clarified and detailed what oil and gas industry transactions are sales tax eligible and what are exempt.

So what's changed, necessitating today's legislation? The Ohio Department of Taxation changed its sales tax doctrine on its own and has begun auditing this industry just recently. It is now assessing sales tax at various points of oil and gas production contrary to the 1960 DoT Memorandum. I have heard reports of operators being assessed substantial sales tax bills, for not only the current year, but also six years in arrears.

This reinterpretation of the Ohio Revised Code and the 1960 DoT Memorandum will have dramatic negative impacts on the oil and gas industry. All operators are being assessed new sales tax collections. This hits not only the unconventional shale operators, but also the conventional "mom and pop" drillers, which in many instances are multi-generational, family-owned small businesses in our hometowns.

These businesses have faithfully followed the law and paid their sales taxes to the state for required transactions according to the 1960 DoT Memorandum and the Revised Code since 1934. Now, because of an unapproved, unlegislated reinterpretation by

staff at the Ohio Department of Taxation, the industry is facing the reality that just one assessment could force their business to close due to burdensome tax bills.

For example, three key items are now being assessed a sales tax, even though historically the Department of Taxation has not assessed such a tax in the past. These items include oil/water separators, brine disposal equipment, and private roadways.

More specifically, in the past for construction projects, which involved private roadways from county roads across farmland and other rural land to the well site and to other locations on the farms, were treated as real property. The contractor would be responsible for paying sales tax on the material that went into the roads and on the equipment (bulldozers/backhoes) to construct the roads. However, neither the landowner nor the driller was charged tax on the sale price it paid for the roads. The Tax Commissioner has an administrative rule on this subject, which treats such roads as nontaxable real property. Although this has been the historic position and the position of the rule, the Ohio Department of Taxation is currently treating such roads as the purchase of taxable personal property.

This is why I am before you today. House Bill 430 does not change Ohio statute on the way sales tax has traditionally been collected for the industry. This bill simply reaffirms what we've been doing for decades—it clarifies the Ohio Revised Code, as intended by the Ohio General Assembly, and the Ohio Administrative Code that these direct sales are treated as nontaxable. The purpose is not to expand the scope of the current exemptions or exclusions; rather it is to aggregate and clarify them.

The oil and gas industry is a key economic driver in the state of Ohio. Resolving this pressing issue is important to the oil and gas producing areas of the state, this industry, its employees, their families and their associated businesses. We cannot have these businesses living in an uncertain and unfair tax climate. Like any business tax, certainty and fairness are critically important.

Thank you once again, Chairman Eklund, and the members of the committee, for the opportunity to present this issue to you today. I will be pleased to answer any questions that the committee may have.