



Ohio Society of CPAs
Testimony on Tax Provisions in HB 64
Before the Ohio House Ways and Means Committee
February 25, 2015

Chairman McClain, Vice Chair Scherer, Ranking Member Cera and members of the House Ways and Means Committee, thank you for this opportunity to speak on behalf of 21,000 members of The Ohio Society of CPAs regarding the tax components contained in HB 64. I'm Scott Wiley, President and CEO of The Ohio Society.

To begin, I applaud Governor Kasich and all members of the House and Senate for your past efforts to improve Ohio's economy and to make our great state not only as competitive as possible, but also a place where people want to grow their business and raise a family. The Ohio Society has supported many of the initiatives you have adopted that have improved Ohio, and we look forward to continuing to work with you to explore opportunities to improve our state even more.

Where HB 64 and its proposed tax provisions are concerned, there are certainly some positive concepts contained in the package. For example, we agree that reducing the tax burden can help to make our state more competitive, and allowing taxpayers to keep more of their own money enables them to invest those dollars back into the economy however they see fit. However, as with anything, the devil is in the details and we do have concerns about some of the tax provisions.

I must preface these comments with the reality this is a very busy time of year for many Ohio CPAs, and getting their collective feedback during tax season can be a challenge. We are wrapping up a member survey of CPA business owners, CPAs serving as corporate officers and members of our Tax Section concerning the tax reform package before you. (We had to wait until the bill was introduced to be able to share specific language.) While results aren't final, I can share what we have heard to date, as well as our established positions on taxation in general.

Commercial Activity Tax

Since its creation in 2005, OSCPA has been a strong supporter of the CAT. We often hear from Ohio CPAs that the beauty of the CAT is its very low rate combined with its simplicity and ease of compliance. The simpler a tax, the more likely taxpayers can comply with filing requirements on their own. We have consistently opposed exemptions and credits to the CAT because they add complexity, pick winners and losers, and at some point you will need to drive up the rate due to lost revenue – just as is being proposed in HB 64.

Last session, concerns about taxes paid by pass-through entities were addressed through the 50% income tax reduction on up to \$250,000. While we agree that small businesses are critical to our state and represent a significant portion of the Ohio economy, medium-sized and large businesses are also very important. We question the fairness of largely eliminating tax on one class of business taxpayer (pass-through entity businesses under \$2 million in gross receipts will pay no income tax on business

income, and a flat \$150 in CAT) at the expense of another (those larger than \$2 million in gross receipts). Under HB 64, bigger businesses would pay a 23% higher rate than they now are for the CAT. The increase would particularly impact manufacturing investment and jobs, as well as larger retailers and high-volume, low margin businesses.

Sales Tax

OSCPA also has significant concerns about the proposed new taxes on services. Because so very few states have a broad sales tax on services, Ohio businesses providing the targeted services in HB 64 would be at a competitive disadvantage to professionals in most other states. It isn't uncommon for an Ohio professional services firm specializing in a particular area to have clients from across the country -- meaning those out-of-state clients could easily just switch to service providers in any of the 46 other states that don't tax the services. Our survey results found that 88% of respondents believe the proposed new sales taxes will have a negative impact on Ohio's business economy. Further, the definition of "management consulting service" is extremely broad as it includes any activity that provides advice and assistance to businesses and other organizations on business issues. The laundry list of services that may be considered business issues ensures how difficult it will be for professionals to differentiate what part of their business is management consulting and therefore subject to collection of sales tax.

The issue of situsing where the benefit of service is provided is particularly challenging. Some services, such as lawn mowing, clearly are provided at a fixed location and there is no confusion about what the provided service is. Other professional services, however, are less well defined and can be provided to and from anywhere: electronically, over the phone, by mail, and even from another state or country.

Consider this example: three CPA professionals – one in Ohio, one in New York and a third in England – are meeting with a business via conference call. The client is in Chicago, but also has operations in Ohio. The CPAs are discussing forthcoming financial statements they are preparing, interspersed with what might be considered "advice and assistance". How would they figure out what portion of the discussion should be taxed and what portion benefits a business in Ohio? What about if all the professionals on the call were in Ohio serving an Indiana client? Or a Canadian firm was working with a business with Ohio ties? Would they literally need to pull out a stopwatch to calculate how many minutes possibly could be "advice and assistance" and divide it by the portion of business physically located in Ohio? Realistically, will an out of state "management consultant" actually collect and remit the sales tax, or Ohio businesses consistently pay the use tax? Plus they would need to consider the added factor of varying rates across the state - a challenge if you have people from multiple Ohio locations potentially benefiting from the service. You could have similar scenarios with attorneys, human or public relations advisors, construction or real estate experts, financial advisors, and many others as the definition includes – but isn't limited to – 22 different services that might be used by a business.

The sales tax proposal would also come into play with related party transactions, such as one entity providing any of the listed services to other members of a consolidated group. Also, the language does not exempt business-to-business services.

OSCPA is also concerned about the broadly worded inclusion of “lobbying.” While most people think of lobbying in terms of interaction with government agencies and elected officials, the definition contained in HB 64 goes far beyond that to include “any activity that serves to influence the behavior or opinion of an individual, an industry or an organization.” This means the work of independent sales representatives could trigger the sales tax, as could advertising or any other activity that tries to influence behavior or opinions of others.

The confusion that comes with taxing professional services is a big reason that only three states broadly tax nearly all services – and none are in the Midwest. In fact, South Dakota is the only one that imposes a true sales tax on a broad array of services. The other two, Hawaii and New Mexico, impose a gross receipts tax on services at a rate and in a manner that in many ways looks like a sales tax but is not a true sales tax. Michigan and Florida previously adopted a broad professional services sales tax but quickly repealed their laws when they discovered how difficult implementation was. Just a few of years ago, Massachusetts enacted a sales tax on the design of computer software, but quickly repealed it when they realized how it would disadvantage the tech industry and related growth in their state.

Lastly, I would be remiss if I didn’t point out that small businesses are more likely to need to use outside professionals than larger companies because they can’t afford to have in-house CPAs, attorneys, HR experts, etc.

While OSCP is still evaluating results of its member survey, a consistent message that is coming through is that many businesses believe they will end up paying more in tax than they pay under the current tax system.

Further, if we have money to invest in the future of Ohio businesses, almost half said they would like at least some of it to go toward paying down – if not off – Ohio’s remaining \$1.38 billion unemployment compensation fund debt to the federal government. According to the Ohio Department of Jobs and Family Services’ report on “Unemployment Compensation: Overview and Current Issues,” Ohio businesses have already paid \$555 million in FUTA penalties during the first three years of default, just paid approximately \$377 million in January for the 2014 obligation, and the offset credit reduction is projected to rise to \$472 million due in January 2016. At the current claim levels and tax collections, the loan is not expected to be paid off until 2017.

If the overall goal of HB 64 is to drive economic development and job creation in our state, our members believe increasing the sales and CAT rates and creating a sales tax on services that countless businesses use to improve their operations or comply with government mandates is not the right approach.

Thank you again for this opportunity to share the concerns of Ohio’s CPA community and the thousands of businesses they work with. I’d be happy to answer any questions you might have.