

OHIO STATE BAR ASSOCIATION TAXATION COMMITTEE

Sales/Use Tax Subcommittee Report

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I. EXEMPTIONS

A. Public Utility Service

Epic Aviation, LLC v. Testa, Ohio Supreme Court, No. 2016-Ohio-3392 (June 15, 2016). The taxpayer sold jet fuel to a consumer who used it in a multiple transportation services, including package delivery at published times and schedules. The Court reversed the BTA, finding the consumer to be a common carrier with respect to this portion of its business because it transported at pre-published times/places and at reasonable/non-discriminatory prices (i.e., not operating as a contract carrier). The consumer's separate contract carrier/charter operations did not qualify for exemption. The case was remanded to the Tax Commissioner to determine the portion of fuel purchases used for the exempt package delivery purposes as a common carrier.

Contrary to the BTA / Tax Commissioner's determinations, the taxpayer was sufficiently regulated to qualify as a public utility even though it did not have a "*Certificate of Public Convenience and Necessity*". The relevant statutory provisions allowing exemption for property used in rendering a public utility service (R.C. 5739.02(B)(42)(a) and 5739.01(P)) did not preclude exemption simply because the provider lacked a Certificate, but rather automatically allowed exemption for taxpayers having such a Certificate.

B. Manufacturing

Lafarge North America, Inc. v. Testa, Ohio BTA Case No. 2015-763 (June 21, 2016); Supreme Court appeal pending (Case No. 2016-1074). Taxpayer manufactured pellet-size slag, serving as a dump facility for several different steel manufacturing facilities in the Youngstown area. The base/raw material slag had accumulated on the site over many years. A bulldozer was used to cut and crush larger pieces of slag, breaking them up into smaller pieces that a front end loader subsequently placed onto a truck to be taken to the taxpayer's screening plant/mill where it was separated by size. The issue was when the taxpayer's manufacturing process commenced. The BTA held that cutting and crushing slag prior to its transport to the screening plant was not part of the manufacturing process. This breaking up was primarily for a transportation purpose. The slag was not committed until after the material handling from initial storage had ceased – when the slag pieces arrived at the mill prior to screening.

C. Transportation for Hire

Dumpsters, Inc. v. Testa, Ohio BTA Case No. 2015-1279 (May 27, 2016). Affirmed assessment due to failure to support or provide proof that truck was used for

transportation of property of others for consideration. For same result, *see, Two Star Leasing, LLC v. Testa*, Ohio BTA Case No. 2015-1358 (June 6, 2016).

D. Oil and Gas Production

Keller v. Testa, Ohio BTA Case No. 2015-1749 (July 6, 2016). Case remanded to determine whether taxpayer's off-road vehicle was exempt based upon use in oil and gas production. The taxpayer asserted the truck was used for purposes of carrying: (1) a welder to different well locations for use in repairs; and (2) a generator used in the drilling, grinding and performing other repairs. Since this argument had been preserved but not considered by the Tax Commissioner, the case was remanded for such consideration.

E. Real Property.

Pep Boys – Manny, Moe & Jack of Delaware, Inc. v. Testa, Ohio BTA Case No. 2015-706 (April 4, 2016). Assessment affirmed with respect to burglar/fire alarms, outdoor illuminated sign, electrical wiring and switches, a security surveillance system, store remodeling, and an air compressor. Although the Tax Commissioner acknowledged that some of the items assessed as “*store remodelers*” may be real property, there was insufficient evidence since the taxpayer did not attend the hearing.

II. TAXABLE SERVICES

A. Employment Services

Seaton Corp v. Testa, Ohio BTA Case No. 2015-224 (July 13, 2016); Supreme Court appeal pending (Case No. 2016-1188). A staffing service (Seaton) providing manual labor for a manufacturer (Kal Kan), operating its production line, was found not to be providing an employment service. The workers were not under the direct control of Kal Kan (i.e., contractor / subcontractor exception), even though Kal Kan controlled the entire manufacturing process/production lines. Rather, Seaton provided “*on-site management operations*”, including hiring, training and managing/supervising the workers being provided. Critical to this finding was that Seaton:

- Monitored productivity and safety, while communicating any new procedures to the workers.
- Maintained the exclusive right to control all of its workers (while Kal Kan supervisors had no interaction with Seaton workers on the job floor unless the worker was committing a safety violation that could harm the worker or manufacturing process/product).
- Maintained an attendance policy.
- Maintained an on-site dedicated office (equipping the space with its own office supplies).
- Provided all “*on-site supervision that is responsible for all shift management of the contractor employees*” (including worker orientation, worker performance management, worker coaching and counseling, interfacing with workers, processing time cards / payroll, and enforcement of workplace rules).

- Performed pre-employment activities consisting of pre-screening, interviewing and testing of work candidates as well as job orientation/training, including safety issues.
- Provided its workers with uniforms and safety equipment at Seaton’s expense.

Conversely, neither Kal Kan nor Seaton could direct or oversee the activities of the other’s workforce. Seaton was responsible for achieving the production goals as communicated to it from Kal Kan, providing the appropriate staff.

B. Automatic Data Processing

Dayton Physicians, LLC v. Testa, Ohio Ct. App., Dkt. No. 26881 (August 12, 2016). Affirming the BTA, the Court of Appeals found medical transcription services to be taxable ADP. The purchaser’s sole objective was to create a verbatim record of the physician’s dictation, while the transcriptionist did not apply any cognitive skills or analytical thought to study, alter, analyze, interpret or adjust the data so as to become personal or professional services.

C. Building Maintenance and Janitorial Services.

Champion Cleaning Specialists, Inc. v. Testa, Ohio BTA Case No. 2015-788 (April 6, 2016). Taxpayer provided taxable cleaning services pertaining to kitchen exhaust hoods and ventilation equipment (but did not provide tangible personal property used to clean property used in the food service operation, as had been asserted, which would be exempt under R.C. 5739.02(B)(27)(c)).

III. PROCEDURE

A. Mark-up Audits

Castle’s Gas & Deli, LLC v. Testa, Ohio BTA Case No. 2015-311 (January 11, 2016). This is one of the few favorable BTA decisions at least initially rejecting the Tax Commissioner’s mark-up analysis when the vendor (convenience store operator) could support it had relevant records that were not considered – those records that reflected total daily taxable sales. There appeared to be conflicting evidence as to whether the records detailed the specific items sold. More importantly, the Tax Commissioner asserted such records did not identify all of the sold inventory (i.e., presumably, additional imputed unreported cash sales were not captured). Regardless, the BTA found that all “*appropriate*” records should have been considered. Since there was no evidence the vendor’s records were deficient, the case was remanded back to the Tax Commissioner for full consideration of the vendor’s “*sales tax records*” to determine the accuracy of the amount assessed.

However, in a second case, the BTA affirmed a second assessment against this vendor because it failed to provide any new documentary evidence challenging the assessment or the mark-up methodology (and the record was complete as to all of the evidence the auditor considered in arriving at the mark-up liability). *See Castle’s Gas & Deli, LLC v. Testa*, Ohio BTA Case No. 2016-1477 (June 29, 2016).

Baker v. Testa, Ohio BTA Case No. 2015-1479 (June 24, 2016). Mark-up audit of a dance/entertainment nightclub / bar was affirmed because the taxpayer provided only bare assertions as to the incorrectness of the assessment. When contesting the Tax Commissioner’s determination, the Taxpayer has the burden to establish his “*actual tax*

liability”, as well as other errors in the assessment through “*competent, probative*” evidence. *See also, Saim Inc. v. Testa*, Ohio BTA Case No. 2015-317 (January 22, 2016).

B. Lodging Tax

Evans v. City of Avon, Ohio Ct. App., Dkt. No. 15CA010879 (August 22, 2016). Affirming the trial court’s decision, the Court of Appeals held that the City’s additional 3% lodging tax violated R.C. 5739.09(B)(1). After the county properly enacts such a tax, neither a municipal corporation nor township are allowed to levy an additional lodging tax under the 1980 law permitting counties to levy an additional 3% tax. The General Assembly intended for only one political entity to levy a lodging tax under the 1980 law. Moreover, Avon’s ordinance was not a proper exercise of its Home Rule authority.

C. Responsible Party Liability

Painter v. Testa, Ohio BTA Case No. 2015-111 (February 26, 2015). President / sole shareholder was found liable as responsible party since fiscal duties were within his responsibility even though he delegated management under separate management agreements with potential buyer.

Cruz v. Testa, Ohio BTA Case No. 2013-1010 (December 29, 2015). Upon remand of the Supreme Court’s earlier decision in *Cruz* solely to determine whether there had been proper service of multiple corporate sales tax assessments, the BTA found that the underlying corporate sales tax assessments had been properly served. As a result, the BTA affirmed the corresponding assessments against the individual taxpayer as a responsible officer.

D. Penalty and Interest Abatement

J&T Washes, Inc. v. Testa, Ohio BTA Case No. 2015-470 (March 14, 2016). The taxpayer failed to establish that the Tax Commissioner abused his discretion by not remitting the entire penalty. The BTA had no statutory authority to address abatement of interest.

IV. LEGISLATION

A. Exemption for Digital Advertising Services - H.B. 466:

“*Digital advertising*” services are now expressly excluded from an otherwise taxable electronic information services. R.C. 5739.01(Y)(2)(k). This is defined as: “*providing access, by means of telecommunications equipment, to computer equipment that is used to enter, upload, download, review, manipulate, store, add, or delete data for the purpose of electronically displaying, delivering, placing, or transferring promotional advertisements to potential customers about products or services or about industry or business brands.*” R.C. 5739.01(RRR).

The legislation now clearly exempts inventory advertising services and portions of mass email-services that had been determined to be taxable by the Tax Commissioner (Information Release ST 1999-04 - On-Line Services and Internet Access Revised Dec. 2015). Exemption applies on a prospective basis.

B. Exemption for Natural Gas Sold by Municipal Gas Companies – H.B. 390

Sales of natural gas by a municipal gas utility are exempt from tax. R.C. 5739.01(RRR) and 5739.02(B)(7).

C. Exemption for Investment Bullion and Coins – S.B. 172

Investment metal bullion and investment coins are exempt from tax. R.C. 5739.02(B)(54). “Investment metal bullion” has the same meaning as in I.R.C. § 408(m)(3)(B) and “investment coins” are coins primarily composed of gold, silver, platinum or palladium.

D. Sales Tax Holiday – S.B. 264

Back to school sales tax holiday was held August 5th through 7th. Purchases of the following were exempt from tax during this period:

1. Clothing less than \$75;
2. School supplies less than \$20; and
3. School instructional materials less than \$20.

V. DEPARTMENT OF TAXATION GUIDANCE

A. RAGRET Publication Revised – Ohio Department of Taxation Info. Release No. ST 2008-03 (Aug. 2016).

Effective September 29, 2015, Resort Area Gross Receipts Excise Tax (RAGRET) may be separately stated on the customer’s invoice. However, RAGRET is part of the price for determining sales tax to be collected. RAGRET should not be included in the line for sales tax, but should be separately identified on the invoice as resort tax. The Release includes examples of proper RAGRET collection. Alternatively, the business may incorporate the RAGRET into the price charged to the customer.

B. Nexus Information Release – Ohio Department of Taxation Info. Release No. ST 2001-01 (Aug. 2016)

Incorporates changes made to R.C. 5741.01(I) by H.B. 64, including the addition of click-through and affiliate nexus presumptions. The definition of “affiliate person” was updated in accordance with R.C. 5741.01(I)(6) and “gross receipts” was defined to mean total receipts from the sale, lease or rental of property held for sale in the ordinary course of business, and gross income from all other sources. The Release also removes registration with the Secretary of State as creating nexus, while adding that sellers and their affiliates making sales to state agencies must register to collect tax.

C. Guidance on Direct Pay Permit Program – Ohio Department of Taxation Info. Release ST 2003-01 (March 2016).

Explains direct pay permit program implemented by Department in May, 2015. This includes periodic (typically every 4 years) review and validation of the taxpayer’s continued need for a direct pay permit and compliance with the direct payment agreement. Also, taxpayers receiving benefits under R.C. 122.175 for eligible computer data centers are required to obtain a direct pay permit.

D. Sales of Motor Vehicles to Ohio Nonresidents – Ohio Department of Taxation Info Release ST 2007-04 (Feb. 2016).

Explains procedure for collecting Ohio tax on sales of motor vehicles to nonresidents. The Release was updated to provide that a trade-in allowance is applicable for sales to Michigan residents.

E. Natural Gas – Ohio Department of Taxation Info. Release ST 1998-01 (Jan. 2016).

The Release was updated to include a reference to Info. Release ST 2007-02 which provides that delivery charges are included in the taxable price of natural gas sold by non-utility gas suppliers.

F. Proposed Administrative Rule revisions:

- As part of the five year rule review, revisions to several sales tax regulations were proposed to primarily provide ministerial updates / corrections, such as updating cross-references and correct form references.
- O.A.C. 5703-9-15: Updates definition of “gift card” and provides several additional examples.
- O.A.C. 5703-9-23: Clarifies scope of exemption for property used in farming, agriculture, horticulture or floriculture.
- O.A.C. 5703-9-29: Adds electronic boards to the regulation concerning outdoor advertising, which are treated as nontaxable advertising services.