OHIO STATE BAR ASSOCIATION TAXATION COMMITTEE
Sales/Use Tax Subcommittee Report
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I. EXEMPTIONS

A. Resale/Affiliated Group -Employment Service/Casual Sale Exemptions

Karvo Paving Co. v. Testa, Ohio Ct App., 9th Dist., C.A. No. 28930 (September 30, 2019). The Court upheld the BTA's finding that Karvo leased traffic maintenance property, such as barrier walls, traffic signs, etc., to ODOT during road paving contracts. ODOT possessed this property while Karvo performed its contracts because ODOT specified the type, quantity, and placement of the equipment, while Karvo had no interaction with the property after it was installed. Further, this property was used by ODOT to fulfill its public duty to safely maintain traffic on Ohio's highways. Accordingly, the traffic maintenance property was entitled to the resale exemption upon Karvo's purchase.

The Court also upheld the BTA's finding that leased employees provided to Karvo by a related company were exempt under the affiliated group exemption of R.C. 5739.01(JJ)(4). The Tax Commissioner contended that the companies were not affiliated because Mr. Karvounides owned 100% of Karvo and his wife owned a majority (55%) of the other company, K&H Excavating. Although there was no "common" ownership, they were still affiliated because the statutory definition of affiliated group includes companies owned ***or controlled*** by the same person. Mr. Karvounides controlled both companies.

Finally, the Court considered Karvo's assignment of error that the BTA incorrectly held that a lease of property could not qualify for the casual sale exemption. K&H leased equipment to Karvo which K&H had previously used in its excavating business, before its operations were wound down. The BTA had ruled the casual sale exemption could not apply to a lease since the lessor (K&H) was solely engaged in the business of leasing the property during the audit period. However, the Court noted that the definition of casual sale only requires that the property had been: (1) acquired for the person's own use, at least initially; and (2) previously subject to any state's taxing jurisdiction. Both conditions were satisfied since K&H previously acquired and actually used the property in its excavation operations, at which time the property was subject to Ohio tax (although an exemption applied). Thus, the Court held that the leased property in this case could qualify for the casual sale exemption. Further, Karvo need not establish that tax had previously been paid on the property. This issue was remanded to the BTA for further proceeding as to availability of the casual sale exemption consistent with the Court's guidance.

A conflict has been certified to the Ohio Supreme Court regarding the Ninth District's jurisdiction to hear this appeal, which conflicts with the Tenth District's previous decision in *Stines v. Limbach*, 61 Ohio App.3d 461 (10th Dist. 1988).

B. Transportation for Hire Exemption

N.A.T. Transportation, Inc. v. McClain, Ohio BTA Case No. 2018-55 (December 23, 2019). Consistent with existing Supreme Court precedent, exemption was not available for trucks primarily used to transport waste since it does not "*belong to others*", as the waste generators relinquished control. However, the BTA acknowledged that exemption would have been available if the taxpayer had established the customer controlled the destination of its transportation.

C. Real Property

Nationwide Mutual Insurance Co. v. McClain, Ohio BTA Case No. 2018-313 (October 22, 2019). Installation of industry-standard communication lines (CAT-5 and CAT-6 cabling) constituted nontaxable real property improvements, rather than taxable business fixtures. Despite a previous ruling (discussed below) that such cabling was a business fixture, the BTA found this type of high-speed computer cabling was not a business fixture because it was no longer unique to specific businesses and is common in any commercial property. The parties stipulated that if Nationwide abandoned the buildings where the cabling was installed, any business could use the cabling for its voice and internet communications. Common building elements, including electrical and communication lines, are excluded from the definition of "*business fixture*." R.C. 5701.03(B).

Accordingly, certain improvements once taxable as business fixtures may evolve into nontaxable real property improvements. In the 1990s, the BTA held internet cable installations were taxable business fixtures because they were not common in every building and primarily benefited the specific business occupant instead of the realty. *See Newcome Corp. v. Tracy*, BTA No. 97-M-320 (Dec. 11, 1998). Now, this type of high-speed computer cabling is so commonplace that any subsequent business occupying the property would use the installed cabling for its own benefit. The BTA noted that when *Newcome* was decided the type of high-speed communication cable installations were tailored to the specific customers' business, as the existing cabling was rarely used when systems were upgraded, and similar cabling was not found in every commercial building nor usable by other building occupants. Although the BTA noted there might be some specialized cable installations that constitute business fixtures, that was not the case here where only industry standard cabling was installed.

D. Oil and Gas Exemption

Stingray Pressure Pumping, LLC v. Tax Commr. of Ohio, *2019-Ohio-5198.* The Tenth District Court of Appeals applied a statutory amendment clarifying the oil & gas exemption retroactively. Interestingly, as discussed below, while this appeal was pending at the BTA, the legislature amended the statute to clarify the scope of the exemption for fracking equipment.

The issue was whether exemption applied to certain equipment used by Stingray Pressure Pumping, LLC in the production of crude oil and natural gas by fracking. The BTA initially denied exemption for equipment used to mix liquids and materials before being pumped into wells. Under previous case law, this type of property was taxable since it was considered *adjunct* to the drilling process, rather than used *directly* in the production of oil and gas. *See Indep. Frac Serv. v. Limbach,* No. 1989-J-863 (June 28, 1991); *Lyons v. Limbach,* 40 Ohio St.3d 192 (1988); and *Kilbarger Constr., Inc. v. Limbach,* 37 Ohio St.3d 234 (1988).

However, while Stingray's appeal of the BTA's decision was pending, the General Assembly amended R.C. 5739.02(B)(42) to clarify the scope of the exemption for fracking equipment by identifying certain exempt property and activities that may not have been contemplated when the sales tax exemption was originally enacted decades earlier. *See* H.B. No. 430; R.C. 5739.02(B)(42)(q). Although legislation is generally applied prospectively, this amendment was remedial and expressly stated that it clarified existing law and applied retroactively, including to current appeals. The BTA did not have the opportunity to apply the clarified statute and, therefore, the Court remanded the appeal to the BTA to determine the taxability of the equipment under the clarified scope of the sales tax exemption.

II. PROCEDURE

A. Tax Base: Feminine Hygiene Products

Rowitz v. McClain, 10th App. Dist., Dkt. Nos. 18AP-191-194 (December 31, 2019). Feminine hygiene products, such as tampons and menstrual pads, not made or dispensed with a prescription are taxable. The Federal and Ohio Equal Protection Clauses were not violated since a fundamental right was not infringed (meaning the tax met the rational basis test, being rationally related to a legitimate government purpose of raising tax revenue). The sales tax is "*gender-neutral*" falling within the broad statutory provisions (and any potential disparity against women was incidental). In addition, the Federal Medical Device Amendments to the Food, Drug, and Cosmetic Act did not preempt the taxing statute since it was connected to safety issues.

Note: This decision on the merits is now moot as Ohio enacted an exemption for feminine hygiene products effective April 1, 2020 (presented below).

B. Imputed Price

Kniffen v. McClain, Ohio BTA Case No. 2019-530 (December 31, 2019). The tax base for cab rides included $2.50 charge for candy (consumed off premises) that the customer paid for his/her "free" cab ride. Applying R.C. 5703.56, sham transactions can be re-characterized consistent with their economic reality when the transaction lacks a business purpose or profit expectation (other than tax benefits). The true object of the transaction was the cab ride so that the amount paid was allocated thereto and taxable.

III. LEGISLATION

S.B. 26 – Effective April 1, 2020, the following are exempt from sales / use taxes: (1) feminine hygiene products, which means tampons, panty liners, menstrual cups, sanitary napkins, and other similar tangible personal property designed for feminine hygiene in connection with the

human menstrual cycle, but excludes grooming and hygiene products; and (2) prescription diapers and incontinence underpads for the benefit of a Medicaid recipient with a diagnosis of incontinence, provided that the Medicaid program covers such products as an incontinence garment. R.C. 5739.01(TT); R.C. 5739.02(B)(56) and (B)(57).

IV. DEPARTMENT OF TAXATION GUIDANCE

A. Updated Nexus Standards Information Release: Describes application of economic nexus standards enacted as part of FY 2020-21 Budget Bill effective August 1, 2019 which presumes an out-of-state vendor has nexus and is required to collect Ohio use tax if in the current or previous calendar year it has: (1) gross receipts from Ohio sales in excess of $100,000; or (2) 200 or more separate transactions delivered to Ohio. These thresholds apply to both sales of TPP and services (all services, not just taxable services). The duty to register and commence collecting tax begins with the month that includes the first day on which the taxpayer exceeds the nexus standard. The previous click-through nexus was removed. Info. Release No. ST 2001-02 (11/1/19).

B. Updated Treatment of Computer Cabling: Explains change in treatment of the sale and installation of high-speed computer cabling as a result of *Nationwide Mutual Ins. Co. v. McClain*, BTA Case Nos. 2018-313, 315, 316, 317, 318 (10/22/19). "It is now clear that computer cabling for VoIP and internet communications are industry standard and incorporated into real property." The change in the Department's position was effective 10/22/19. For past transactions, the treatment as real property will be respected if, at the time of the transaction, the contractor did not collect tax as a vendor nor pay tax as a contractor. The Department also reminds those who sell and install computer cabling to incur use tax on their cost of cabling, including if seeking a refund on a past transaction, unless the customer requires specialized networks to meet a technical requirement. Info. Release No. ST 1999-01 (12/1/19).

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