

OHIO STATE BAR ASSOCIATION TAXATION COMMITTEE
Sales/Use Tax Subcommittee Report
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Steven A. Dimengo, JD, CPA, MT
Richard B. Fry III, JD, MT
BUCKINGHAM, DOOLITTLE & BURROUGHS, LLC
3800 Embassy Parkway, Suite 300
Akron, OH 44333
(330) 258-6460
(330) 258-6423
sdimengo@bdbl.com
rfry@bdbl.com

I. EXEMPTIONS

A. Manufacturing

1. *Lafarge North America, Inc. v. Testa*, 2018-Ohio-2047. The taxpayer used bulldozers, loaders, and dump trucks to break up and transport slag from a slag mountain where it had been stored as a by-product from molten ore during steel making. The bulldozers ripped slag from the slag mountain, crushing it to form a pile. Then, front-end loaders transferred the crushed slag to dump trucks to be transported to a screening plant on the premises, where it was sorted by size and used in manufacturing steel. The taxpayer asserted this equipment was entitled to the manufacturing exemption since it changed the form of the slag (not for purposes of facilitating transportation from initial storage) and transported it as work-in-process.

The issue was when the manufacturing operation commenced – when the slag was broken up from the mountain or not until it had been transported to the screening plant? A manufacturing operation begins when raw materials are committed to the manufacturing process. Ohio Admin. Code 5703-09-21(B)(1). As relevant to these facts, raw materials are committed when some affirmative action is taken in furtherance of manufacturing, such as mixing, measuring, heating, or otherwise treating or preparing the materials for manufacturing.

The Supreme Court found that the slag, a raw material in steel production, was committed to manufacturing when it was broken up and cut from the slag mountain. At this point, the slag was transformed into smaller, marketable pieces to be transported to the screening plant and used in manufacturing steel. Therefore, the equipment at issue, including its fuel and repair parts, was exempt from Ohio use tax.

2. *E. Mfg. Corp. v. Testa*, 2018-Ohio-2923. A manufacturer of custom aluminum trucks asserted exemption for natural gas used to maintain portions of multiple buildings to a temperature of at least 50°F. Regulating the temperature was necessary to enable extensive welding throughout each trailer. Welding in this environment eliminated condensation on the aluminum and ensured a good welding bond. Although the areas in which welding occurred were not fully enclosed, the manufacturer asserted they were still special/limited areas of each building whose environments must be totally regulated for production.

Consistent with R.C. 5739.011(C)(5), the Court held that temperature regulation of an entire plant necessary for production is not exempt even if the focus is on a particular

area of the plant, akin to Example 48 (candy cane manufacturer) in Rule 5703-9-21. Temperature regulation is only exempt if it is restricted to a special/limited area of the plant (presumably meaning the area must be fully enclosed) and such total regulation in the confined environment must be essential for production to occur (i.e., all three requirements of the environmental control exemption are met). Since the heating constituted "*temperature regulation*" of entire buildings and not limited areas, any property used for such heating was excluded from the definition of "*thing transferred*" for use in manufacturing. Thus, exemption was not available as items necessary for production or gas used in production under R.C. 5734.011(B)(4) and (8). The Court Stated: "*R.C. 5739.011(C)(5) is a more specific provision that excludes from exempt status those items that are used for temperature control, even if those items would otherwise fall under the more general exempting language of R.C. 5739.011(B).*"

B. Construction Contracts (Real Property)

Palace Hotels, LLC v. Testa, Ohio BTA Case No. 2016-1300 (March 5, 2018). Resort hotel's waterpark improvements/amenities were real property. This included a roof/dome, fiberglass decks, plumbing, electric and concrete foundations. The Tax Commissioner accepted in-ground pools as real property. Relying upon its earlier decisions in ***Polaris Amphitheater*** (2007) and ***Inverness Club*** (2007), the Board noted that an item can have a commercial purpose and still be real property (rather than a business fixture). Moreover, professional engineering services were nontaxable, being a part of the price for the waterpark construction (i.e., real property improvements).

C. Oil/Gas Production

Stingray Pressure Pumping, LLC v. Testa, Ohio BTA Case No. 2015-1465 (January 17, 2018). Taxpayer engaged in hydraulic fracturing operations was denied exemption for equipment used to mix liquids and materials before being pumped into wells for fracturing. This consisted of sand kings, sand silos, and associated t-belts which supply sand to the blender unit where all of the fracturing liquids/materials are mixed prior to being pumped into the well for fracturing. Similar to the manufacturing exemption, the equipment was adjunct to the drilling process, not used directly in mining.

II. TAXABLE SERVICES

Employment Services

Career Staffing, LLC v. Testa, Ohio BTA Case No. 2016-2617 (August 2, 2108). Employees provided to a meat processor/packager involving a physically demanding employment environment including severe cold and wet conditions were permanently assigned despite fluctuation in the number of leased personnel provided. The fluctuation in leased employees was not due to seasonality or short term workload needs, but rather unique circumstances of employment. The intent was to provide permanent employees despite the frequent turnover. Moreover, the difficult employment environment causing such turnover was further supported by the fact that the particular lessee/customer used three separate employment agencies to fill its positions, but still could never satisfy its staffing needs.

III. PROCEDURE

A. Refund

Clerac, LLC v. Testa, Ohio BTA Case No. 2018-216 (September 10, 2018). Sales tax refund not allowed due to lack of evidence that full purchase price was refunded.

B. Responsible Party Liability

Singh v. Testa, Ohio BTA Case No. 2017-1160 (September 10, 2018). Assessment affirmed since convenience store liquor license was in individual's name who continued to be associated with the business as a responsible party/owner.

Derouchie v. Testa, Ohio BTA Case No. 2017-1264 (September 5, 2018). Assessment affirmed since individual did not contest status as responsible party, but only asserted that corporate assessment was erroneous. Per Ohio Supreme Court precedent, the BTA did not have jurisdiction to address merits of underlying corporate assessment.

C. Transient Use Exemption

Guile v. Testa, Ohio BTA Case No. 2017-2115 (September 5, 2018). Transient use exemption (R.C. 5741.02(C)(4)) not available for Ohio resident's purchase of vehicle driven by him from Ohio dealer to Montana residence. Only non-residents are entitled to exemption.

IV. LEGISLATION

A. Oil/Gas Production:

H.B. 430 clarifies the exemption for property used in the production of, or exploration for, crude oil and natural gas. Technological advancements (specifically fracking operations) facilitated the need to clarify and identify certain property and activities that are exempt, but may not have been contemplated when the exemption was enacted decades earlier.

The legislation specifies the following activities and equipment relating to oil and gas production are exempt:

- Construction of permanent access roads, well sites, and temporary impoundments;
- Equipment used to create a wellbore pathway to underground reservoirs;
- Drilling and services used within a subsurface well;
- Casing, tubes, and float and centralizing equipment;
- Well completion services and equipment used in providing such services;
- Wireline evaluation, mud logging, and perforation, and equipment used in providing such services;
- Pressure pumping and artificial lift equipment; and
- Wellhead and well site equipment used to separate, stabilize, and control hydrocarbon phases and control water.

The amendment also lists several types of oil and gas property that is not exempt. The list of exempt and nonexempt equipment is set forth in R.C. 5739.02(B)(42)(q). As a clarification of existing law, this amendment applies to pending audits and appeals.

B. Permanent Sales Tax Holiday

S.B. 226 makes sales tax holidays permanent beginning the first Friday through Sunday in August each year. Sales tax holiday was held August 3 – 5, 2018 and will occur from August 2-4, 2019. The sales tax holiday applies to: (1) school supplies priced \$20 or less; (2) school instructional materials priced \$20 or less; and (3) clothing priced \$75 or less. R.C. 5739.02(B)(56).

V. OHIO ADMINISTRATIVE CODE

- A. Ohio Admin. Code § 5703-9-44 (Bad debts) – To qualify for the bad debt deduction when the vendor assigns account receivables or uses a third party to facilitate financing, the claimant must be the vendor and the bad debt deduction must appear on the vendor's books and records. Effective June 14, 2018.
- B. Nonsubstantive changes to the following Ohio Admin. Code Sections effective June 14, 2018:
- 5703-9-39 (Interstate commerce)
 - 5703-9-40 (Sales of personalty belonging to another)
 - 5703-9-41 (Person engaged in advertising)
 - 5703-9-42 (Installation or sale of septic tanks)
 - 5703-9-43 (Books, manuals, bulletins, lists or similar materials)
 - 5703-9-45 (Sales; alleged exempt sales; submission of additional evidence)
 - 5703-9-46 (Sales and use taxes; automatic data processing, computer services, and electronic information services)
 - 5703-9-48 (Sales tax: purchases made with food stamp coupons) – updated to conform with Federal law.
 - 5703-9-50 (Registration using central registration system).

VI. DEPARTMENT OF TAXATION GUIDANCE

- A. Wayfair Response: Communications Director, Gary Gudmundson released the following statement concerning the effect of the *Wayfair* decision: “Today's decision does not have an immediate, direct impact on Ohio. The Court ruled on the laws in another state; not on Ohio's tax laws. We anticipate that we'll see some out-of-state retailers begin to voluntarily charge and collect Ohio sales tax, but otherwise the sales tax rules and laws in Ohio will stay the same until the General Assembly decides whether or not to change them.”
- B. New Address for Sales / Use Tax Refund Applications (per 4/2/18 notice):

Ohio Department of Taxation
Audit Division – SUT REF
PO Box 183050
Columbus, OH 43218-3050