

**OHIO STATE BAR ASSOCIATION TAXATION COMMITTEE**  
**Sales/Use Tax Subcommittee Report**  
**September 28, 2017**

**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@bdblaw.com](mailto:sdimengo@bdblaw.com)  
[rfry@bdblaw.com](mailto:rfry@bdblaw.com)

**I. EXEMPTIONS**

A. Resale

*Pi In The Sky, LLC v. Testa*, Ohio BTA Case No. 2015-2005 (January 19, 2017), appeal pending before Ohio Supreme Court, Case No. 2017-0236. A single member limited liability company (“SMLLC”) purchased an airplane for lease to its sole member. The BTA disregarded the lease, concluding it lacked substance, thereby denying the SMLLC’s claim to the resale exemption. Factors supporting the lack of any real substance to the leasing relationship included the following:

- The lessee (an operating company) was the sole member of the SMLLC lessor.
- The same person executed the lease agreement on behalf of both lessor and lessee.
- There was no other lessee of the aircraft, and the SMLLC had no other activities.
- The loan for the purchase of the aircraft was not entered into on behalf of the SMLLC, but executed by the individual owner of the lessee.
- There was no advertising with respect to leasing the aircraft.
- The lessor had no business location; and
- The aircraft was leased for \$80/hour under a “dry lease” (i.e., lessee was responsible for all operating costs, taxes, etc.).

The BTA found that the lease had no factual or economic substance and, therefore, the lessor was not engaged in the business of leasing and did not qualify for the resale exemption.

Is this an aberration? Hopefully yes, as form usually predominates substance in the Ohio sales and use tax arena, even though there is a specific statutory provision that allows application of the sham transaction doctrine. *See* R.C. 5703.56(A). Moreover, it did not help that the taxpayer waived the BTA evidentiary hearing in this manner, making it easier to accept all of the Tax Commissioner’s assertions since no new evidence was presented to the BTA.

*The Cincinnati Reds, LLC v. Testa*, Ohio BTA Case No. 2015-1707 (May 22, 2017), appeal pending before Ohio Supreme Court Case No. 2017-0854. A professional baseball team was denied the resale exemption for purchases of promotional items (e.g., bobbleheads) provided to game attendees. The taxpayer asserted the promotional items were resold as part of the price of the admission tickets and, thus, exempt under the resale exemption. Even though the BTA acknowledged that the promotional items induced ticket purchases, it found that the promotional items were not resold because no separate,

distinct consideration was received since ticket prices did not vary based upon whether a promotional item was provided (i.e., there was no flex pricing). Patrons paid the same price for game tickets on giveaway days even if they did not actually receive an item due to limited supply. Accordingly, the BTA found the promotional items were gifts (i.e., no consideration) and taxable to the Reds.

## B. Manufacturing

*East Manufacturing Corp. v. Testa*, Ohio BTA Case No. 2016-2111, appeal pending before Ohio Supreme Court Case No. 2017-0666. 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.

The BTA made the following factual findings:

- *“East maintains all/portions of its facility’s six buildings at a specific temperature to create the necessary temperature conditions for the extensive welding that takes place in its manufacturing facilities.”*
- *“All aluminum materials to be welded, and the tools used to weld them, must be kept at 50 degrees or warmer, to avoid the accumulation of condensation and ensure a good weld ... and in order to avoid affecting a paint’s color or drying time.”*
- *“East custom builds its trailers, which can be large and unwieldly, e.g., 53 feet long, which requires the manufacturing space to be flexible and not confined by interior walls that would impede the movement of \*\*\* work-in-process.”*
- *“Allowing each building to be heated entirely, even though necessary, is less expensive than such additional costs associated with adding walls to contain the heat.”*
- *“Not only would the actual construction of walls add costs, but additions to the manufacturing process necessary to ‘work around’ the walls, e.g., equipment to move lengthy trailers-in-process around the walls would be necessary, also creating extra expenses.”*
- Reference to *“special/limited sub-areas of its buildings”*.

Accordingly, the BTA accepted: 1) temperature regulation was necessary for welding aluminum trailers; and 2) the welding only occurred in portions/sub-areas of the buildings (asserted to be the special/limited sub-areas). The only issue was whether the exemption for regulating a special / limited controlled environment (R.C. 5739.011(C)(5)) was conditioned upon the areas being defined by walls. The manufacturer asserted that literal application of the statute does not impose such requirement. The BTA disagreed, holding that the natural gas used to maintain the temperature to at least 50°F was taxable since the manufacturing areas at issue were not enclosed, self-contained, sealed or in some way separated from the entire manufacturing facility. Accordingly, they were not “special and limited” areas.

The natural gas did not qualify for exemption under R.C. 5739.011(B)(4) as being necessary for the continuation of manufacturing operation since it was found to serve a quality control function. For the same reason, it did not qualify as a substance used in the manufacturing operation exempt from tax under R.C. 5739.011(B)(8).

## II. TAXABLE SERVICES

### A. Building Maintenance and Janitorial

*Great Lakes Bar Control, Inc. v. Testa*, Ohio BTA Case No. 2016-34 (April 14, 2017), appeal pending before Ohio Supreme Court, Case No. 2017-0655. The taxpayer serviced its customers draft beer systems by monitoring and inspecting the systems, unclogging lines when necessary (applying cleansing solutions), and other measures to “ensure that the draft system is operating at its optimum performance.” Since cleaning was only a small/incidental aspect of the regular monitoring/inspection service, which included more than simply clearing the beer lines of clogging deposits, the BTA held that the services were not taxable building maintenance and janitorial services. Therefore, when the removal of dirt and contaminants is ancillary to a nontaxable monitoring/inspection service, the service is *not a* taxable building maintenance and janitorial service.

### B. Electronic Information Services

*America’s Pizza Co., LLC v. Testa*, BTA Case No. 2016-1551 (September 5, 2017). A vendor (pizza restaurant) was taxed on services involving an Internet-based food ordering system. The system was used to receive, price and transmit orders placed by customers originating from a web browser filled by businesses that provided carryout food or delivery services. The food vendor (taxpayer) placed all of its information (i.e., menu, price specials, coupon and delivery time information) into its own computer equipment for purposes of being acquired by the service provider for its use in creating, updating or changing the taxpayer’s order site. The services were taxable electronic information services because the service provider received food order data from customers via computer equipment and such data was accessible to the taxpayer’s computer equipment. A hearing before the BTA was not held.

## III. PROCEDURE

### A. Refund Claim

*Pride of Cleveland Scooters, LLC v. Testa*, Ohio BTA Case No. 2016-375 (April 11, 2017). Vendor asserted it overpaid sales tax for three years due to an error resulting from its sales being inflated on its sales tax returns. It filed refund claims for three years and submitted evidence supporting the actual sales amounts, including profit and loss statements, explanatory spreadsheets, and receipts from the Ohio Bureau of Motor Vehicles. The Tax Commissioner granted the refund claims for two years, but inexplicitly denied the refund for 2013, claiming the vendor failed to provide sufficient evidence supporting its amended sales tax return. The BTA held that “sufficient evidence [was] provided [to the Tax Commissioner] to determine whether the Taxpayer’s request for refund was proper”. The evidence included a month-by-month summary of sales transactions, including receipt number, customer name and transaction date, as further supplemented by testimony of the vendor’s accountant.

### B. Responsible Party Status

*Maysalum Samad v. Testa*, Ohio BTA Case No. 2016-952 (June 8, 2017). The Tax Commissioner filed a motion to dismiss because prior to issuance of the Final Determination appellant did not object in writing to asserted responsible party status, although she did orally object during the administrative appeal hearing before the Tax Commissioner. On such basis, the BTA was prepared to dismiss the appeal. However, since the Tax Commissioner actually

addressed responsible party status in the Final Determination, the BTA found that the Commissioner assumed jurisdiction over the issue which also gave the BTA jurisdiction. Nonetheless, the BTA affirmed responsible party status since the appellant identified herself as “president” of the company, and there was no testimony to support lack of responsible party status (i.e., only written statements accompanying the notice of appeal which could not be verified).

C. Mark-Up Audit

*Willard Drive Thru v. Testa*, Ohio BTA Case No. 2016-16 (January 19, 2017). A convenience store mark-up audit was affirmed. The four core deemed sale categories (beer, wine, liquor/other alcohol and cigarettes) were determined by the state statutory minimum pricing, while the mark-ups for other products fell within the ranges of the vendor’s own product checklist (as well industry standards).

D. Writ of Mandamus

*State ex rel. Repeal the Lorain Cty. Permissive Sales Tax Committee v. Lorain Cty. Bd. Of Elections*, Ohio Supreme Ct. 2017-1181 (September, 15, 2017). Writ of Mandamus seeking to compel the Lorain County Board of Elections to certify an initiative petition (to repeal a county permissive sales tax) for the November ballot was denied, as the Court held that R.C. 5739.022(A) did not provide the legal right to the relief sought since the petition was not enacted as an emergency measure.

#### IV. LEGISLATION

A. H.B. 49 – Budget Bill – Effective September 29, 2017

1. Substantial Nexus Presumption Expanded – Sellers with greater than \$500,000 of Ohio sales in the current or preceding calendar year are presumed to have nexus for use tax collection purposes if the seller either: (i) uses in-state software to make taxable sales to Ohio consumers (e.g., cookies); or (ii) provides or uses a content distribution network using servers in Ohio to accelerate or enhance delivery of seller’s website to Ohio consumers. R.C. 5741.01(I)(2)(h) and (i).
2. Jukebox Exemption – Purchases of digital audio sold through a single-play commercial machine that accepts direct payments (i.e., jukebox) are exempt from tax. R.C. 5739.02(B)(55).
3. Direct Mail – Adopts definitions of “advertising and promotion direct mail” and “other direct mail” to conform with the Streamline Sales and Use Tax Agreement. Advertising and promotional direct mail is sourced to where it is delivered to the recipient, if such information is provided by the consumer. If delivery information is not provided (and the consumer does not provide an exemption certificate or direct pay permit), the sale is sourced to the location from which it was shipped. Other direct mail is sourced to the consumer’s location maintained by the direct mail vendor in the ordinary course of business. R.C. 5739.033(F).
4. Vendor’s License Database – The Tax Commissioner must maintain an online system allowing county auditors to issue vendor’s licenses and publish the list of active and inactive vendor’s licenses. R.C. 5739.18.

5. Suspension of Vendor's License – The Tax Commissioner can suspend a vendor's license based upon the failure to pay employer withholding taxes under R.C. 5747.07. Further, a suspended vendor's license may not be reinstated until all returns have been filed and taxes paid (including penalties and related charges) required under R.C. 5747.07. R.C. 5739.30(C) and (D).
  6. 2018 Sales Tax Holiday – Purchase of certain items (clothing less than \$75, school supplies less than \$20, and school instructional materials less than \$20) are exempt from tax August 3-5, 2018. Similar to 2017 sales tax holiday. Uncodified Section 757.120.
  7. EIS / ADP Amendment vetoed – R.C. 5739.01(B)(3). Governor's Veto Message, Item 42 cited revenue loss of \$115 million in FY 2018.
- B. PROPOSED H.B. 116 – Sales tax exemption for prescription eyeglasses, frames and contacts. Overwhelmingly passed by the House and is now pending before the Senate. This exemption was passed in the Budget Bill, but vetoed by Gov. Kasich. Veto Message Item 43.

## V. OHIO ADMINISTRATIVE CODE

### A. Five-Year Rule Review – Effective 9/23/17

Technical changes to Ohio Admin. Code §§ 5703-9-07 (refund applications), 5703-9-31 (florists), 5703-9-35 (purchases as liquidator of closed financial institutions), and 5703-9-38 (photocopying and blue prints).

### B. PROPOSED Amendments

1. Ohio Admin. Code § 5703-9-21 (manufacturing)
  - a. Agitating or heating raw materials to maintain same form as received, or measuring materials to verify quantity upon receipt, would not constitute commitment. New Example 65 provides application for an asphalt manufacturer.
  - b. Incorporates application of manufacturing exemption to providers of laundry and dry cleaning services and CIP equipment used in dairy product production. See R.C. 5739.011(B)(12) and (13).
  - c. Amends Example 2 – Aggregate used in concrete production is committed when measured and deposited on the conveyor from initial storage.
  - d. Amends Example 54 – CAD system (including software) is qualified research and development equipment when it is capitalized.
  - e. Adds Example 65 – As applied to an asphalt manufacturer, a scale weighing incoming sand and stone to verify the correct quantity is taxable. Likewise, the initial storage tank that churns and heats asphalt cement to maintain the product in its original form is taxable. Conveyors that move sand and stone to be classified by size are taxable because the raw materials are not committed until reaching the screening grate.

- f. Adds Example 66 – Special ventilation and exhaust system in a manufacturing facility used to supply fresh air and remove harmful fumes from a welding process is taxable. The system is not incorporated into manufacturing equipment, does not qualify as excepted safety equipment, and does not totally regulate the environment in a limited area essential for production to occur.
2. Ohio Admin. Code § 5703-9-44 (bad debts) – Amended to add: “In situations where the vendor has assigned the account receivables to a third party or where the vendor was uses [sic] a third party to facilitate the financing of the taxable sale, to qualify for the bad debt deduction, the claimant must be the vendor and the bad debt deduction must appear on the books and records of the vendor.”
  3. Ohio Admin. Code § 5703-9-48 (food stamp purchases) – Updated to specify that purchases pursuant to the supplemental nutrition assistance program are exempt.
  4. Ohio Admin. Code § 5703-9-49 (responsible party) – Rewrites rule to provide that responsible party liability may be imposed upon: (i) any employee with control or supervision over, or charged with the responsibility of, filing returns or making payments; or (ii) any person that is an officer, member, manager, or trustee responsible for the taxpayer’s fiscal responsibilities.
    - a. “Person” specifically contemplates non-individuals.
    - b. Among other situations, responsible party liability could be imposed upon any person: (i) with direct or delegated authority to sign checks or initiate electronic funds transfer on the taxpayer’s behalf; or (ii) who’s “position is one that would ordinarily be responsible for any fiscal duty, including but not limited to those listed in this paragraph [(B)(3)], even if the person does not actually participate in or supervise such duty.”
    - c. Additionally, personal liability may imposed be upon any person who, directly or indirectly, supervises, manages, or has authority over any person described in paragraph (B)(3).
  5. Ohio Admin. Code § 5703-9-50 (central registration system) – updated to incorporate a form adopted by the Streamline Sales Tax Governing Board.

## **VI. DEPARTMENT OF TAXATION GUIDANCE**

### **A. Change in Motor Vehicle Definition – Info. Release ST 2017-01**

The definition of “motor vehicle” was amended as of January 1, 2017 to exclude under-speed vehicles and mini trucks. Therefore, the casual sale of under-speed vehicles (including golf carts) and mini trucks are exempt from tax and the trade-in of such items does not reduce the tax base of a new motor vehicle.