

Honorable Council
City of Newark, Ohio
September 1, 2015

The Ways and Means Committee met Monday August 31, 2015 in Council Chambers following the Capital Improvement Committee, with these members in attendance:

Ryan Bubb, Chair Doug Marmie
Jeremy Blake

We wish to report:

1. **Ordinance No. 15-25** amending chapter 890 of the codified ordinances of the City of Newark, Ohio regarding the levying and collection of municipal income taxes was considered.

Barb Jobs, City Tax Administrator- What you have before you is the amendment to the Newark Codified Ordinance Section 890 that was mandated by the 130th Ohio State Legislature. What I would like to do for you tonight is highlight the most important and challenging provisions in the Ordinance so you can understand what impact this Ordinance will have on the City and the income tax revenue. To give you a little background, in December 2014 the State Legislature passed and Governor Kasich signed House Bill 5 into law. What had started out as a bill to promote uniformity to the various municipalities and villages throughout the State became a tax reform bill which made sweeping changes to Ohio Revised Code 718 (ORC 718). ORC 718 is the State Code that governs the ability of municipalities to levy and collect municipal income tax. In order for any municipality to continue to collect municipal income tax after 2015, the State Code requires that all municipalities amend their local tax ordinances and adopt the amended ordinance by January 1, 2016. The State Code further mandates that no municipal legislative body may make any additions or changes to any language in the local ordinance that would add to or change the meaning of ORC 718 thus removing this Council's ability to make tax laws for our City. In other words, when you look at the State Code what you see is what we get. Before you is a Model Ordinance authored by members of the legal counsel for the Ohio Municipal League (OML) and members of OML's Tax Committee. The Tax Committee is comprised of tax administrator from across the state representing all different sized communities. I have been a member of this Committee for 5 years and I can assure you that we have worked hard fighting the legislation that passed and in writing the document I am presenting tonight. While creating the Model Ordinance, we had two goals in mind. First and foremost was uniformity. Throughout the battle against House Bill 5 and its predecessors, we were constantly bombarded by the opposition for uniformity. The Ordinance before

you has been distributed to all municipalities and villages throughout the State. With a few exceptions, all Councils such as this one will be presented with this same Ordinance. Our second goal was brevity. Much of the new State Code is made up of instructional language for the Tax Administrators. There is so much instructional language that the old ORC 718 was only 21 pages long. The new ORC 718 is 90 pages. Even leaving out the instructional language, the Newark Ordinance is going from 37 pages to 70. The Ordinance that I am presenting amends the current Ordinance and does not repeal any part of the old ordinance resulting in every municipality throughout the State having dual tax ordinance. According to the State Code, the previous Ordinance will remain in effect until all matters prior to the enactment of the new ordinance are resolved – this includes the payment of all taxes owed prior to January 1, 2016. The oldest tax balance we have due on our books is from 1982. Until that tax is paid, the old ordinance remains in effect. The taxpayer that owes the 1982 tax died in 1993 – it is going to be a long time before that is collected. The enforcement of dual ordinances is going to be cumbersome and costly to the City and confusing to taxpayers. The new Ordinance will take effect with the tax year beginning January 1, 2016. That means that starting January 1st, all withholding and estimated tax payments will be collected under the new Ordinance; however, the 2015 individual and business net profit returns filed in April of 2016 fall under the old Ordinance. It is going to be very difficult for the public to understand which tax filings are collected under each Ordinance. The cost of educating the public is just one of the many costs that the City will have to absorb. We will have to keep software updated since we will have 2 different sets of rules, minimum tax amounts due, penalty structures and, under the new Ordinance, changes to the interest rates annually. The most valuable asset that I believe the City has is a well trained staff; yet, it is also the most costly asset. The cost to train the current staff and future staff for the Tax Office obviously is going to increase. New employees will have to learn two Ordinances in depth enough that they can confidently explain the laws to the public and tax professionals. Due to the cyclical nature of our work, we know that it takes at least one year for a new employee to fully understand their job. With two Ordinances, it is logical that the needed training will double. There are three sections of the current Ordinance that remain unchanged in the new Ordinance: mandatory filing and registration, landlord reporting requirements and the fee for returned checks or electronic payments. All other sections of the current Ordinance are amended. The City will begin to be impacted by the new Ordinance in January 2016. Employers will need to be notified of changes to withholding thresholds and due dates by January 1st. Employers remitting withholding tax on a quarterly basis must mail their withholding payments 15 days earlier than they have in the past. The threshold for remitting the withholding tax on a monthly basis increases from \$100 per month to \$200 per month. These employers must pay their withholding before or on the due date. Employers remitting \$1,000 or more of withholding in a month will continue to pay their withholding on a semi-monthly basis but their due date was shortened from 5 business days to 3.

Employers remitting on a monthly and semi-monthly basis must also be notified that their payment requirements are different from those remitting on a quarterly basis. According to the new State Code, employers remitting quarterly must make their payments on or before the due date. For employers making monthly or semi-monthly payments, however, they are required to send their payments so that the payment is received by the tax office on or before the due date. The threshold for estimated tax for 2016 has been lowered. Under our current Ordinance, taxpayers are required to make quarterly estimated if their tax due is \$250 or more. This threshold has been reduced to \$200. The due dates for the estimated tax also change to match the Federal due dates making taxpayers payments due 45 days earlier. The penalty on late paid withholding and estimated tax payments also increase in 2016. Currently if a withholding payment is received 1 day late the penalty is 5% of the tax due. In 2016, that penalty increases to 50% of the tax due. The current penalty for late paid quarterly estimated tax is 5% but increases to 15% in 2016. Another change that must be implemented for 2016 is the Local Board of Tax Review. Currently this Board is comprised of the Mayor, the Treasurer and the City Auditor. The Board under the new Ordinance will be comprised of 2 members appointed by Council and 1 member appointed by the Mayor. The State Code specifies who can and cannot serve on the Board. The new Board must be in place on January 1, 2016 so you will want to read section 890.18 of the Ordinance regarding this Board. The most significant and costly change for 2016 is the Occasional Entrance Rule also known as the 20 Day Rule. Under the current State Code, if a business located outside the City sends a non-resident employee to a work site within the City, the employee is not obligated to pay Newark tax on the wages earned in the City if the employee works in Newark 12 or fewer days. The new State Code expands the period that the wages are not taxable for 12 to 20 days which equates to an entire month. The State Code further expands the 20 day period to include non-residents that are self-employed and working in Newark. This expanded number of days and the inclusion of self-employed non-residents will result in a loss of revenue for the City. An additional loss of revenue will result because the first 20 days the non-resident is working in the City are now tax-free. Under the old State Code, if the non-resident employee worked here more than 12 days, the tax liability was retroactive back to the first day the employee started working in the City. The new State Code specifically states that the tax liability begins on day 21 so the City loses the first 20 days of tax. Further revenue will be lost due to the Small Employer Exception included in the Occasional Entrance section. Any employer located outside the City of Newark whose gross income is less than \$500,000 per year will not be required to withhold any municipal taxes and their employees are exempted from municipal taxation regardless of where the employee is working. For example, a business owner has an office cleaning business that he operates out of his home in Hanover Township. He wins a contract to clean offices for a company located in Newark. The business owner hires 4 non-resident employees to clean the offices. As long as the business owner makes less than \$500,000 gross per year, the 4 employees working in

Newark do not have to pay any tax to the City even if they work here for forever. In addition to the lost revenue, the new Ordinance is going to also increase refunds. Under the new law, an employee can only work in 1 city per day. The employer is not required to determine how long the employee works in that City. The employers will withhold for the full 8 hour work day. The employee then has the right to request a refund from the City by providing the actual number of hours worked in the City. Refunds will further be increased due to the fact that an employer may choose to withhold tax for the city in which the employer has a fixed location. For example, a temporary service has their main office in Newark. They have 200 employees working throughout the state of Ohio. The employer can choose to withhold Newark tax for all 200 employees and not be obligated to withhold for the city where the employee is working. As a result, if none of the employees work in Newark, all 200 would be eligible to request that their Newark tax be refunded. All other provisions of the new Ordinance will be implemented in 2017. One provision that will be most contentious for taxpayers is the increase of the Late Filing Penalty from \$50 to \$150. The collection of this penalty is going to be costly and result in many cases going to the Board of Tax Review. Another loss of revenue for the City starting in 2017 will result from the increase in the minimum tax due. Currently, the minimum tax due under our current Ordinance is \$5. Statewide, cities are being asked to adopt the minimum tax due of \$10.01. The reason this is unclear is because the State Code gives three different minimums. In one section the Code it reads that no payments or refunds are due under \$10 which equates to \$9.99. In another section, the Code states no payments or refunds are due of \$10 or less which sets the minimum at \$10. In yet another section the State Code reads that payments and refunds are required on more than \$10 resulting in \$10.01. Tax Administrators throughout the Ohio have opted to use the \$10.01 threshold since the State Code is unclear and contradictory. The final provision from the new Ordinance will be implemented in 2018. Starting with the tax year 2018, any taxpayer with a net operating loss will be able to carry the loss forward for 5 years to offset any potential net profit. Under our current Ordinance, the City does not allow losses to be carried forward. If a business has a loss in one year, they pay no tax. If the same business has a net profit in the next year, they pay the tax on what they earned. Under the new Ordinance, the losses may be carried forward and the business will potentially never pay any tax. This was the most hotly debated provision in HB 5. The so-called compromise was to phase the loss carry forward in over a 5 year period and allowing only 50% of the previous year's loss to be used. As more than one member of both the House and Senate told me personally quote "They can only use 50% so that will lessen the blow". However, these legislators could not have understood the language in the bill since the 50% reduction is based on a declining balance. Here is an example of how the declining balance will work. Company X has a net loss in 2017 of \$50,000. When they file their 2018 tax return, they can use 50% of their 2017 loss or \$25,000 to reduce their taxable income. This is where the Declining Balance comes to play. When they file their return for 2019,

they will take the original \$50,000 loss; subtract what was used in 2018 resulting in a remaining loss balance of \$25,000. They can then multiply the \$25,000 by 50% and use \$12,500 of their 2017 loss to reduce their taxable income in 2019. This process is repeated for 2020, 2021 and 2022. So over the 5 year phase in period they will be able to use \$48,437 of the \$50,000 loss – that is 97% of the loss not 50%. What does the future hold? Unfortunately, the State Legislature is not finished with Municipal Tax Collections. When the 131st Ohio Legislature passed the biennial State budget in June of this year, there were 12 amendments to ORC 718 that they just passed last December. In addition, Senate Bill 198 was introduced in June that, if passed, will prevent all municipalities from taxing the income of non-residents. To offset the loss of income for the municipalities, we will no longer allow a 1% credit for residents. In an attempt to determine the impact of this bill, I analyzed the amount of withholding tax collected from just 10 companies located in the City. I used different sized employers from different industries. For 2014, these 10 employers paid \$5.7 million in withheld taxes to the City. Based on the information on the employees' W-2s, \$4.6 million of the \$5.7 million paid was from non-residents. That is 81% of the tax collected from these 10 employers. If that average holds true, which I believe it would, of the \$15.1 million of withholding paid to the City in 2014, if the City lost 81%, it would be roughly \$12 million in lost revenue. I would like to thank you for your time and would be happy to answer any questions.

Mr. Marmie- you kind of slid that in there a little bit about that 1% tax credit, so that is gone now?

Barb Jobs- it will be gone if Senate Bill 198 passes. I am not one to go doom and gloom but I wanted you to be aware it's out there because I think it is one we need to watch. A lot of people that have told me the State will never pass that are the same ones that told me the State would never pass House Bill 5.

Mr. Blake- what are the three additional groups you said are now exempt?

Barb Jobs- two groups are partnerships and one group is members of S Corporations

Mr. Marmie- S Corps is that way now unless it was enacted prior to that change, is that correct?

Barb Jobs- right but they carved out two other sections that move the tax level to the entity level not the owner level.

Mr. Marmie- as far as educating our taxpayer in the area what do we have or are we just going to give them the paperwork? You mentioned that it is going to be a daunting task for your team

Barb Jobs- we have already talked about that. I am going to do tutoring sessions. One on September 10th and one on September 24th then I'm planning on hosting a local seminar for the local tax preparers. I would go over the most critical sections for 2016 and then do the same thing in 2017 and 2018 so they can keep up and not try to understand all 90 pages.

Mr. Marmie- great that is good information

Rusty White, 1409 Residence Dr- did the cities have any input in any of this or was it just dictated to you?

Barb Jobes- the OML Tax Committee has been fighting this bill for at least three years. The proponents of the bill did set up a combined group that would take the arguments from the opponent side and the arguments of the proponent's side and put them together. Unfortunately once we thought we had a piece that was very well combining ideas and there were only three sticking points the State Legislators threw that out and made their own bill. So yes there was an effort to get input from the cities.

Rusty White- I thought that was all settled in 1776.

Law Director Sassen- I would just like to state for everybody in the audience and for the record and for this Council that I really appreciate the work Barb has done on this. I think she has done an excellent presentation tonight. This is an extremely complicated piece of legislation that I quite frankly could not get my head around without my eyes rolling back in my head. Barb did all of the work on this presentation and preparing this legislation. I reviewed it very simply. I appreciate that very much and I think Council should recognize the hard work that Barb has put in on this project.

Motion by Mr. Marmie to send to full Council, second by Mr. Blake

Motion passed by a vote of 3-0.

Ryan Bubb, Chair