Municipal Income Tax: What You Really Should Know

Local Government Officials Conference
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Donald W. Smith, CPA
Executive Director

Background
Background


- Toledo – 1st Ohio municipality to enact income tax – 1946

- Ohio cities and villages begin to adopt income tax – Late 1960s/Early 1970s

Background

- The municipal income tax applies to **Individuals** who:
  - **Earn taxable income** in one or more Ohio municipalities, and
  - **Live in** a Ohio municipality.

- It also applies to **Businesses earning taxable income** in one or more Ohio municipalities.
**Background**

- **Businesses owe** municipal income tax to the municipality(ies) in which they earn their income.

- **Individuals owe** municipal income tax to the municipality(ies) in which they earn their income, AND may also owe municipal income tax to the municipality where they live.

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**Time Out: Example**
Example

- Individuals may be subject to **two municipal taxes**
  - **Workplace** – tax where earned by taxpayer
  - **Residence** – tax where taxpayer resides

- This may result in a taxpayer having a higher effective tax rate

Example

- John worked in Columbus and lived in Bexley for all of 2017. John earned **$50,000** where **$1,250** Columbus city tax was withheld.

<table>
<thead>
<tr>
<th></th>
<th>Tax Rate</th>
<th>Tax Credit</th>
<th>Credit Limit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bexley</td>
<td>2.50%</td>
<td>65.00%</td>
<td>2.50%</td>
</tr>
</tbody>
</table>

- John files his Bexley return showing that he owes Bexley $1,250 (2.5%), but may only take **credit for 65%** of the $1,250 he paid to Columbus.
- John owes Bexley an additional **$437.50** ($1,250 - $812.50)
Example

- Although Bexley’s stated rate is 2.5% John’s effective rate is higher:

\[
\frac{(\$1,250 + \$437.50)}{\$50,000} = 3.375\%
\]

(Columbus)      (Bexley)                              (Total)

Contrary to Popular Belief…

- There is no RITA Tax

- RITA is not a municipality
  - RITA is a “Regional Council of Governments”, formed under State Law to administer municipal income taxes for its member municipalities
Background (Cont.)

Ohio municipal income tax is primarily located in Chapter 718 of the Ohio Revised Code, the “ORC” or “RC”

- Requires municipalities to levy a **flat tax**
  - Must be uniformly applied to both individuals and businesses

- Limits the types of income that municipalities may tax
  - Municipality may determine its own rate and credit
Background
A series of “Uniformity Bills” have modified ORC 718

<table>
<thead>
<tr>
<th>Bill</th>
<th>Year</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>HB 477/483</td>
<td>2000</td>
<td>Generic forms, Safe harbor, 12-day occasional entrant</td>
</tr>
<tr>
<td>HB 95</td>
<td>2003</td>
<td>Qualifying wages, Adjusted federal taxable income, Ohio Business Gateway, S-Corps taxable, Non-qualified deferred compensation</td>
</tr>
<tr>
<td>HB 224</td>
<td>2008</td>
<td>Due dates tied to federal, Tax preparer authorization, Tax appeal options, Credit for tax paid to wrong municipality</td>
</tr>
<tr>
<td>HB 5</td>
<td>2014</td>
<td>De Minimis thresholds, Taxpayer bill of rights, 20-day occasional entrant, Small employer, Penalty and interest, Lottery &amp; gambling, Residency, NOL Carryforward</td>
</tr>
<tr>
<td>HB 49</td>
<td>2017</td>
<td>Eliminate sales throw-back, Opt-in net profit tax w/ ODT</td>
</tr>
</tbody>
</table>
Background

Case Law

- **What** municipalities can tax and how municipalities enforce their taxes **has also been impacted** by decisions of:
  - Common Pleas Courts
  - Ohio Board of Tax Appeals
  - County Courts of Appeals
  - Ohio Supreme Court
  - Federal courts

### Case Law

**Firestone v. Neusser** 1987
Contributions to tax-deferred retirement savings plans are not exempt from municipal income tax because of ERISA.

**Springfield v. Hicks** 1988
Where payment of muni income tax is delinquent, statute of limitations does not begin until an income tax return is properly filed.

**Fairlawn v. Billington** 1991
Municipal tax for R/E agents is based on situs of agent not the sale. (Reversed by HB 5)

**Cincinnati v. Bawtenheimer** 1992
Municipality has right to request copy of Federal Form 1040 with municipal return. (Incorporated in law by HB 5)

**Springfield v. All Am. Food Specialists** 1993
Resident employer cannot be compelled to withhold tax on a resident taxpayer working in another jurisdiction.
Background

Court Decisions that have impacted Municipal Tax

<table>
<thead>
<tr>
<th>Decision</th>
<th>Year(s)</th>
<th>Impact</th>
</tr>
</thead>
<tbody>
<tr>
<td>Columbus v. Reckless</td>
<td>1995</td>
<td>Municipality may require self-employed taxpayers to pay equal quarterly installments of estimated tax.</td>
</tr>
<tr>
<td>Fisher v. Neusser</td>
<td>1996</td>
<td>Municipality has the power to levy an income tax on lottery winnings received by its residents. (Incorporated in law by HB 5)</td>
</tr>
<tr>
<td>E. Cleveland v. Landingham</td>
<td>1994</td>
<td>Clarified definition of resident</td>
</tr>
<tr>
<td>Bedford v. Dalton</td>
<td>2004</td>
<td></td>
</tr>
<tr>
<td>State v. Dalton</td>
<td>2005</td>
<td></td>
</tr>
<tr>
<td>Boyer v. St. Bernard</td>
<td>2009</td>
<td>Stock options are taxable when exercised.</td>
</tr>
<tr>
<td>Ochsner v. Cincinnati</td>
<td>2011</td>
<td>Severance pay is taxable income.</td>
</tr>
</tbody>
</table>

Background

ORC 718

- Today, ORC 718 provides uniform requirements for:
  - Taxable employee compensation (Qualifying wages ≈ Medicare wage)
  - Annual tax return due dates
  - Estimated tax payment thresholds and due dates
  - Taxpayer appeal rights and requirements
  - Statute of limitations on collecting delinquent taxes (3-6 years) and paying refunds (3 years)
  - Litany of other uniform administrative regulations (Board make-up, assessments, etc.)
Background

• Wherever ORC 718 is silent, municipal tax ordinances may dictate
  • Rules and Regulations may clarify the ordinance
    • These are not mandatory
  • Instructions for filing may clarify the Rules & Regulations
Third-Party Administrators (TPA)

58% of Taxing Jurisdictions in OH

<table>
<thead>
<tr>
<th></th>
<th>Full Members</th>
<th>JEDDs</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cleveland – CCA</td>
<td>48</td>
<td>14</td>
<td>62</td>
</tr>
<tr>
<td>RITA</td>
<td>294</td>
<td>28</td>
<td>322</td>
</tr>
<tr>
<td></td>
<td>342</td>
<td>42</td>
<td>384</td>
</tr>
</tbody>
</table>

What Lies Ahead?
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- **Court Decisions**
  - Throw-back provision
  - Opt-in with ODT – Home Rule

- **Legislation**
  - SERP & Other Non-Qualified Plans
  - Mandatory 100% Credit
  - Further Erosion of Home Rule / Centralized Collection

Questions? / Contact / Thank You!

RITAOhio.com  RITAperspectives.com

Donald W. Smith, CPA
Executive Director, RITA
10107 Brecksville Rd.
Brecksville, OH 44141

Phone: 440-526-0900
dsmith@RITAOhio.com
For which municipality does Ohio Revised Code section 718.011 require withholding for the day?

**Notes:**
1. (a) and (c) are municipalities under Ohio Revised Code section 718.011(A).
2. For each employee working in at least one taxing municipality on a day, the employer will withhold for only one municipality for that entire day. However, there will be no required withholding at all for employees of any small employer if the small employer's fixed location in Ohio is in a jurisdiction not imposing municipal income tax.
3. An employer does not have to withhold for any qualifying wages paid to any employee for work the employee performs in a locale where there is no municipal income tax.
4. An employer who is not a small employer (see the employee's principal place of work) can choose to disregard the Occasional Entrant Rules one week from the first day on all wages earned for work performed in an "occasional entrance" municipality.
5. For qualifying wages for which no withholding is required per the flowchart, the employer must keep clear and convincing documentation to support that no withholding was required.
6. Even though withholding may not be required per the flowchart, the employer can elect to withhold for the municipality in which the employee's principal place of work (for present purposes) is located.

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**Flowchart**

**START**

Is the employee an employee of an air, water, motor, or rail carrier who regularly performs duties in 2 or more states? If No, see Note 6 above.

- Yes

- No

Prior to this day did the employee work in a petroleum refinery in Municipality X for more than twelve days, which need not be consecutive, during this calendar year?

- Yes

- No

Special rule applies to employees working at a petroleum refinery. See division (D) of ORC 718.011.

Does the employee work for a small employer?

- Yes

- No

A small employer is an employer that has gross revenue of less than $500,000 in the preceding tax year and if the employee works in the permanent place of business in Ohio. "Gross revenue" includes reimbursements the employer receives from any party.

Under the rules for counting days shown in the information box to the right, did the employee work in any municipality other than Municipality X on the day in question?

- No

- Yes

Repeat the flowchart for any other municipality in which the employee worked on that day.

Principal Place of Work

An employer's principal place of work ("PPP") is the Ohio fixed location to which the employee regularly reports for duties. If an Ohio fixed location does not exist, then the employer's home is the Ohio location at which the employee spends the greatest number of days in a calendar year performing services for his or her employer. If an employee is not required to report for employment duties on a regular and ordinary basis to either an Ohio fixed location or an Ohio location, then the PPP is the location at this state in which the employee spends the greatest number of days in a calendar year performing services for his or her employer.

An employee spends a day at an Ohio location working on or in an enterprise location other than Ohio than any other location. If the employee spends an equal amount of time in two municipalities, the employee will have two principal places of work, and the employer will have to split the withholding on a rational basis.

For some employees their principal place of work will change during the year and not be accurately known until late in the year. An employer in this position who is not a small employer with a fixed location in Ohio can choose one of the two following solutions: (1) disregard the Occasional Entrant Rules and withhold from the first day on all wages earned for work performed in a RITA municipality or (2) determine the employee's present principal place of work as of the end of each pay period and withhold accordingly for that pay period. Note that in the end of each pay period "time in the calendar period" includes the period beginning on Jan. 1 of the year and ending on the last day of the most current pay period.

Counting Days

Counting days for purposes of the Occasional Entrant Rule is not as simple as it sounds. If during a day an employee spends more time performing services in one taxing municipality than the employee spends performing services in any other taxing municipality, then for purposes of counting days for the Occasional Entrant Rule the employee spent the entire workday in that taxing municipality. If the employee spent the most time performing services that day:

- For purposes of counting days, the following times are considered to be time spent performing services at the employer's principal place of work.
  1. Traveling to the location at which the employer will perform first services for the day, from the employer's last location at which the employer was performing services for any other location;
  2. Traveling from any location to another location in order to pick up or load, for the purpose of transportation or delivery, property that has been purchased, sold, assembled, fabricated, repaired, refurbished, processed, remanufactured, or improved by the employer's employee;
  3. Traveling or delivering property described in (1), above, if the employee does not temporarily or permanently affect the property to real estate owned, used, or controlled by a person other than the employee's employer.

Under the rules for counting days shown in the information box to the right, did the employee work in any municipality other than Municipality X on the day in question?

- No

- Yes

Under the rules for counting days shown in the information box, has the employee worked in Municipality X for at least 20 days prior to the day in question?

- No

- Yes

The employer must withhold Municipality X tax on all qualifying wages earned this day in any and all municipalities imposing municipal income tax.

Is the employee being paid in his or her capacity as a professional athlete, professional entertainer, or public figure?

- Yes

- No

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Occasional Entrant Rule

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Warning

Failure to withhold from the Principal Place of Work would violate the employer's protection under the Occasional Entrant Rule. No withholding is required on compensation earned in any location (not imposing a municipal income tax). See Note 6 above.

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Professional Athletes, Professional Entertainers, & Public Figures

A professional athlete is an employee who is paid to participate in professional athletic events.

A professional entertainer performs in the professional performing arts and is paid on a per event basis. An entertainer who is paid on the season regardless of whether or not he or she performs at a specific event is not a professional entertainer.

A public figure is any person of prominence, such as a politician, entertainer, athlete, college football coach, farmers having event promoters, or any person having locale in Ohio whom it is necessary for them to perform at an event such as a speech, public appearance, graduation ceremony, or similar event.
S-Corp. Rules for RITA Member Municipalities

S-Corp. distributive shares are taxable, regardless of participation or origin and should be reported on Form 37.

FAIRPORT HARBOR   PERRY   RIVERSIDE
PAINESVILLE   RICHMOND HEIGHTS   YELLOW SPRINGS

The Ohio S-Corp distributive shares are taxable and should be reported on Form 37.

AVON   EAST PALESTEINE   MACEDONIA   SOLON
AVON LAKE   EASTLAKE   MAPLE HEIGHTS   SOUTH EUCLID
BOSTON HEIGHTS   FREMONT   MENTOR   STREETSBORO
BROOKLYN HEIGHTS   GAHANNA   NORTH CANTON   TWINSBURG
CAMPBELL   HIGHLAND HEIGHTS   OAKWOOD   VALLEY VIEW
CHAGRIN FALLS   HOLLAND   POWELL   WICKLiffe
CHardon   JACKSON CENTER   SEVEN HILLS   WILLOUGHBY
CLEVELAND HEIGHTS   JOHNSTOWN   SHEFfield LAKE   WILLOUGHBY HILLS
CUYAHOGA HEIGHTS   LAKEMORE   SHEFFIELD VILLAGE   WOODMERE

S-Corp distributive shares that do not represent wages are generally not taxable and should not be reported on Form 37.

ABERDEEN   FAYETTE   MIDVALE   RIO GRANDE
ADDYSON   FELICITY   MIFFLIN   RIPLEY
ADELPHI   FORT JENNINGS   MILAN   ROCKY RIVER
AMANDA   FOSTORIA   MILFORD   ROSSFORD
AMSTERDAM   FREDERICK TOWN   MILFORD CENTER   SABINA
ANDOVER   GALENA   MILLER CITY   SAINT CLAIRESVILLE
ANTWERP   GALION   MILLERSPORT   SAINT PARIS
ARLINGTON HEIGHTS   GARFIELD HEIGHTS   MINERAL CITY   SALINEVILLE
ASHLEY   GETTYSBURG   MINERVA PARK   SANDUSKY
ASHVILLE   GIRARD   MINGO JUNCTION   SARDENIA
AURORA   GLENWILLOW   MOGADORE   SEBRING
BALTIC   GRAFTON   MORELAND HILLS   SHAKER HEIGHTS
BALTIMORE   GRANDVIEW HEIGHTS   MORRAL   SHAWNEE HILLS
BARNESVILLE   GRATIS   MOUNT STERLING   SHERWOOD
BAY VILLAGE   GREENHILLS   MOUNT VICTORY   SILVER LAKE
BEACHWOOD   GROVE CITY   MT HEALTHY   SILVERTON
BEAVERTOWN   HANOVER   NEW ALBANY   SMITHFIELD
BEDFORD HEIGHTS   HARRISON   NEW BAVARIA   SOUTH SOLON
BELL CENTER   HARRIS   NEW FRANKLIN   SOUTH VIENNA
BELLEFONTAINE   HASKINS   NEW RICHMOND   ST. LOUISVILLE
BELLEVUE   HILLARD   NEW RIEGEL   STEUBENVILLE
BELPRE   HIRAM   NEW WASHINGTON   STOUTSVILLE
BENTLEYVILLE   HOPEDALE   NEW WATERFORD   STRATTON
BEREA   HUDSON   NEWBURGH HEIGHTS   STRONGSVILLE
BETHEL   HURON   NEWCOMERSTOWN   SUGAR GROVE
BETTSVILLE   INDEPENDENCE   NEWTON FALLS   SUGARCREEK
BEXLEY   JEFFERSON VILLAGE   NEWTONSVILLE   SUNBURY
BLOOMDALE   JERRY CITY   NEWTON   SWANTON
BLOOMINGDALE   JEWETT   NEY   SYCAMORE
BRECKSVILLE   KENT   NILES   TALLMADGE
BREMN   KILLBuck   NORTH LEWISBURG   THURSTON
BROADVIEW HEIGHTS   KIRKSVILLE   NORTH OLIMET   TIRO
BROOKLYN   KIRTLAND   NORTH RIDGELIVE   TONTOGANY
BUCKLAND   LAGRANGE   NORTH ROBINSON   TORONTO
CAIRO   LAKELINE   NORTH ROYALTON   TREMONT CITY
CAMDEN   LEETONIA   NORTHFIELD VILLAGE   TRIMBLE
CARDINGTON   LITHOPOLIS   NORWALK   UHRICHSVILLE
CARROLL   LOCKBOURNE   OAK HILL   UNIVERSE HEIGHTS
CATAWA   LOCKLAND   OBERLIN   UPPER ARLINGTON
CECEL   LODI   OLMSTED FALLS   VERMILION
CEDARVILLE   LOVELAND   ORANGE   WADSWORTH
CENTERBURG   LOWELLvILLE   OSTRANDER   WAME
CIRCLEVILLE   LYONHURST   OTTAWA   WASHINGTONVILLE
CLARESVILLE   LYONS   OXFORD   WATERVILLE
CLINTON   MADISON VILLAGE   PATASKALA   WAYNESVILLE
COMMERCIAL POINT   MAINEVILLE   PATERSON   WELLINGTON
CONESVILLE   MANCHESTER   PENINSULA   WELLSTON
CONTINENTAL   MARINGO   PEPPER PIKE   WEST ELKTON
CORWIN   MARTINS FERRY   PIKETON   WEST LAFAYETTE
DANVILLE   MAYFIELD HEIGHTS   PLAIN CITY   WEST MANSFIELD
DARRYSVILLE   MAYFIELD VILLAGE   PLEASANT HILL   WESTLAKE
DEGRAFF   MCLAUREL   PLEASANTLAKE   WESTON
DENNIS   MCCLINTON   PORTAGE   WILLIAMSBURG
EAST CLEVELAND   MECHANICSBURG   POTHATAN POINT   WILLIAMSPORT
EATON   MEDINA   QUINCY   WILLOWICK
EDGERTON   MELROSE   RAVENNA   WINTERSVILLE
ELMORE   METAMORA   REMINDERVILLE   WOODSTOCK
ELYRIA   MIDDLE POINT   REYNOLDSBURG   WORTHINGTON
FAIRBORN   MIDDLEBURG HEIGHTS   RICHWOOD   YOUNGSTOWN
FAIRVIEW PARK   MIDDLEPORT   RIDGWAY

as of 1.1.2018

S-Corp. distributive shares are taxable, regardless of participation or origin and should be reported on Form 37.