City of Findlay, Ohio

Income Tax Department

Annual Report

2010

Structure, Purpose, and Composition

The Income Tax Department is comprised of an Administrator, three full-time staff members, and one part-time staff member who are responsible for administering and enforcing the Income Tax Ordinance and the Rules and Regulations. The Department's mission is to respectfully encourage the highest level of voluntary compliance by assisting, educating, and informing customers and stakeholders efficiently, effectively, and accurately.

The Administrator is appointed by and reports to the Mayor, who serves as Chairman of the Income Tax Board. The Administrator reports also to this board, which was designed to depoliticize the Income Tax Department and to protect it from improper influence. The other Board members include the Law Director, Treasurer, Auditor, and Council's Appropriations Committee Chairman, who are responsible for offering oversight and counsel to the Income Tax Department and initiating most legislation during a minimum of four quarterly public meetings each year to ensure the department's funding, accountability, independence, and objectivity. The Tax Administrator is neither a voting, nor a non-voting member of the Income Tax Board.

The Mayor, Law Director, and Treasurer each appoint an elector for lifetime service to the Board of Review, whose purpose is to rule on taxpayers' initial formal appeals. The Board of Review members are Mayoral appointment Martin Terry, Law Director appointment Douglas W. Huffman, and Treasurer appointment John W. Pinksi, CPA.

2010 **Tax Department Staff**	2010 **Board of Review**	2010 **Income Tax Board**
Andrew Thomas	Martin Terry	Mayor Pete Sehnert
Angie Stewart	Douglas W. Huffman	David Hackenberg
Cindi Kimmet	John W. Pinski, Jr. CPA	Jim Staschiak II
Julia Nulton		Robert C. Sprague
Tonya Stillberger		Randy Ward

Income Tax Department Activities

I. Software Search

We have been using a software package developed, supported, and maintained specifically for Findlay since October 2003. In 2010, after an unsuccessful attempt to transfer the software to a new server, we were informed that the existing software is not compatible with the newer versions of Microsoft Window's Operating System and SQL Database. We are reviewing and evaluating as many solutions as possible including existing packages from at least three vendors, a rewrite, a joint venture, and also virtual server and virtual PC that will enable the department to use the existing software for a few more years. City Council set aside $150,000 for the project.

II. Mandatory Filing

For the second consecutive, but final year, we suspended resident individual mandatory filing as a budget-cutting measure. This enabled us to save on postage costs, printing expenses, and labor. We highlighted actual figures in a previous annual report. For additional savings, we excluded from the annual tax return package mailing any taxpayer who had their return prepared by a practitioner who provided a form as part of the provided service. In each of the last two annual mailings, we excluded over 5,000 packages.

III. Equipment Purchases

The department purchased four PCs and monitors to replace aging equipment.

IV. NWOTCA and OML

The department continues its active participation in the Ohio Municipal League Income Tax Committee and, one of its regional arms, the Northwest Ohio Tax Commissioners Association. Members of the NWOTCA generally meet monthly in the northwest Ohio area to offer training and interdependent assistance and to discuss tax policies and procedures as well as current and emerging legislative issues. The NWOTCA also hosts a biannual municipal income tax seminar for area tax professionals. The next seminar is slated for 2012.

The Ohio Municipal League Income Tax Committee is comprised of income tax administrators and commissioners from each of the major cities and from several other communities across the State. The committee functions in a similar fashion as the regional groups, but works directly with the OML.

V. Village of Arlington

The Tax Department has completed its eighth year of administering the income tax on behalf of the Village of Arlington. The process continues to proceed smoothly and routinely. The Tax Department administers approximately 125 employer withholding accounts and approximately 750 individual and business accounts, of which nearly one-half are returns in which the tax liability equals the Arlington tax withheld or equals the Arlington credit allowed. In the first six years, Arlington has contributed over $70,000 toward the Tax Department's operating budget. Arlington incurs their own costs for refunds, tax forms, and court costs.

We continue to find the practice beneficial to both municipalities. As anticipated, we have a greater opportunity to serve a wider range of Findlay taxpayers—non-residents who are employed within our City limits. Notably, we estimate that Findlay derives 40 to 50 percent of its employer withholding revenue from non-residents. Considering the nation's climate toward state and local taxes—particularly in Ohio over the past several years, it is vital for municipalities statewide to diligently and comprehensively serve the interests of non-residents who pay municipal income taxes to the communities where they work.

In 2009, the Village of Arlington adopted the relevant and compatible portions of Findlay's Income Tax Ordinance and the Rules and Regulations that were effective January 1, 2010. The issues in which the Village experienced changes include:

1. Imposition of tax on lottery winnings.
2. Rates and application of penalties and interest changed.
3. The minimum gross monthly rental charge threshold before a rental is recognized as a business went from $100 to $300.
4. Refund-tax due threshold increased from $2 to $5.
5. An Arlington Income Tax Board was established, but with a different composition than the City of Findlay's.

Arlington is prohibited from imposing tax on resident shareholders' distributive shares from S corporations. Bills originating in both the Ohio House and the Senate established voting requirements available only to communities that were imposing tax on this income by ordinance, rule, or regulation as of December 2002, which the Village was not. Senate Bill 180 of the 124th Ohio General Assembly established a November 2003 voting requirement for distributions from *interstate* S corporations, followed by House Bill 127 of the 125th Ohio General Assembly that established a November 2004 voting requirement for distributions from *intrastate* S corporations. As a result, Arlington can impose tax on S corporations only at the entity level.

VI. Credit Card Payments

Beginning in March 2006, the Income Tax Department partnered with Official Payments to allow taxpayers to pay taxes using Visa®, MasterCard®, American Express®, and Discover® credit and debit cards. Taxpayers can visit www.officialpayments.com directly or through a link on the City's Internet site, or they can call 1-800-2PAYTAX℠ and use an assigned jurisdiction code (4553). Official Payments charges the users a convenience fee for its electronic transaction services. There is no expense to the City.

VII. Ohio Business Gateway

The Income Tax Department continued to receive a growing number of extension requests, estimate payments, income tax return filings, and employer withholding remittances through the Ohio Business Gateway. The employer withholding remittances began for all Ohio municipal income tax departments in 2007. The Ohio Business Gateway is administered, primarily, by an arm of the Ohio Department of Taxation in conjunction with several other participating State agencies. This year, OBG administrators announced attempts to make the system more user friendly for tax practitioners by enabling them to process multiple-client transactions with only one sign in.

Ballot Issues, Ordinances, and Federal & State Legislation

I. City of Findlay

Findlay City Council passed Resolution 36-2010 to eliminate an exemption for untaxed distributive shares to resident individual limited partners of limited partnerships and to allow the losses. The change was prompted by a Board of Review hearing during which a taxpayer's representatives contested that the characteristics of limited partnerships that gave rise to the exemption are not confined to limited partnerships.

In 1998, the Income Tax Department consulted a major business and the area tax practitioners during an attempt to rewrite the Income Tax Rules and Regulations regarding partnerships, limited liability companies, and S corporations, or "pass-through" entities. One participant mentioned the topic of publicly-traded limited partnerships and their characteristics that may render these entities' distributive shares non-taxable *intangible* income to resident owners. The characteristics discussed were that (1) any one partner's ownership share is typically very low, (2) the change in ownership is publicly traded, and (3) the partners do not materially participate in the management or operations of the businesses.

The Ohio Revised Code does not permit municipalities to impose tax on intangible income, which is currently defined in 718.01(A)(5) as "income of any of the following types: income yield, interest, capital gains, dividends, or other income arising from the ownership, sale, exchange, or other disposition of intangible property including, but not limited to, investments, deposits, money, or credits as those terms are defined in Chapter 5701 of the Revised Code, and patents, copyrights, trademarks, tradenames, investments in real estate investment trusts, investments in regulated investment companies, and appreciation on deferred compensation." In light of the ORC's definition of intangible income, as it read at the time, an exemption was adopted by Findlay for the untaxed distributive shares of resident limited partners of limited partnerships.

In practice, the arrangement worked extremely well. The Federal Schedules K-1 of Form 1065, on which distributive shares of partnerships are reported, had a separate check box entitled "limited partner." Preparers and Tax Department staff could easily identify the nature of the partner and the type of the partnership.

In 2001 however, the Ohio Supreme Court ruled in a fairly similar situation that ordinary business income to a pass-through entity "retains its status as it passes through to the" owners. (Tetlak vs. Village of Bratenahl) As a result, a partnership's ordinary business income and rental real estate income does not change to a status of non-taxable *intangible* income as it passes to the owner even if the owner's intent is merely to invest in the partnership.

Further, a 2004 Internal Revenue Service design change to Schedule K-1 compromised the Income Tax Department's ability to effectively administer the exemption. The check box entitled "limited partner" was combined with the title of another check box so that the identification of a limited partner is no longer distinguishable from any other partner or member of any partnership or LLC.

The issue culminated in a July 2010 Board of Review hearing at which Certified Public Accountants from a local accounting firm contested on behalf of their client that the three characteristics of limited partnerships that initially gave rise to Findlay's exemption are not confined to this type of partnership, but rather they exist for general partnerships and limited liability companies as well. The City acknowledged the same, but countered with the aforementioned Ohio Supreme Court decision and stated that the City of Findlay is perhaps the only Ohio community that offers this exemption. Moreover, the Ohio Revised Code does not allow Findlay to exempt the income of any partnership owners by language in 718.01(D)(1), which states that "except as otherwise provided in this section, no municipal corporation shall exempt from a tax on income compensation for personal services of individuals over eighteen years of age or the net profit from a business or profession."

The CPAs, the two City representatives, and the two eligible Board of Review members agreed that the best solution is to eliminate the exemption for resident individual limited partners of limited partnerships and to tax all resident individual partnership and LLC owners alike.
We approached the Income Tax Board with this decision at the August 4 meeting. The Board approved the amendment to Article III(A)(4)(b.) and the repeal of Article III(A)(4)(b.)(.3) of the Income Tax Rules and Regulations to be effective January 2011.

Adoption of this resolution will have minimal impact on tax revenue, aligns Findlay with perhaps all communities in Ohio that have an income tax, and corrects the conflict with ORC 718.01(D)(1) that prohibits municipalities from exempting individuals' net profits from businesses and professions.

Despite potential Ohio municipal tax applications and similarities, Federal income tax terms such as earned income, unearned income, passive income, nonpassive income, and portfolio income are not used in the Income Tax Ordinance, in the Rules and Regulations, or in Chapter 718 of the Ohio Revised Code. Conversely, the term intangible income defined in ORC 718 for Ohio municipal income tax purposes is generally not used in the same context by the IRS for Federal income tax purposes.

II. State of Ohio

On November 19, 2009 Representative Tyrone Yates (D-33rd District) introduced Ohio HB 378 (128th General Assembly) "to eliminate the authority of municipal corporations to exempt stock options and nonqualified deferred compensation from municipal income taxation." The bill was assigned to the House Ways and Means Committee, of which Mr. Yates was a member. On January 21, 2010, then Governor Ted Strickland appointed Mr. Yates to the bench of Hamilton County Municipal Court. No action has been taken and the bill will likely have to be reintroduced in the 129th General Assembly.

III. United States Congress

In April 2009, U. S. Representative Henry C. Johnson of Georgia introduced House Resolution 2110 in the 111th Congress "to limit the authority of States to tax certain income of employees for employment duties performed in other States." Officially dubbed the "Mobile Workforce State Income Tax Fairness and Simplification Act," the measure would limit states' "taxation of the wages or other remuneration of any employee who performs duties in more than one state to: (1) the state of the employee's residence; and (2) the state in which the employee is present and performing employment duties for more than 30 days," unless the 'employee' is a professional athlete, entertainer, or public figure. The bill was referred to the Subcommittee on Commercial and Administrative Law, where it resides. Representative Jim Jordan, from Ohio's fourth Congressional District, is one of the 15 cosponsors. This essentially replaced House Resolution 3359 introduced by Representative Johnson in the 110th Congress.

Income Tax Board Activities

The Income Tax Board's activities relate to legislative issues that are discussed in part 1 of the section above entitled *Ballot Issues, Ordinances, and Federal & State Legislation*.

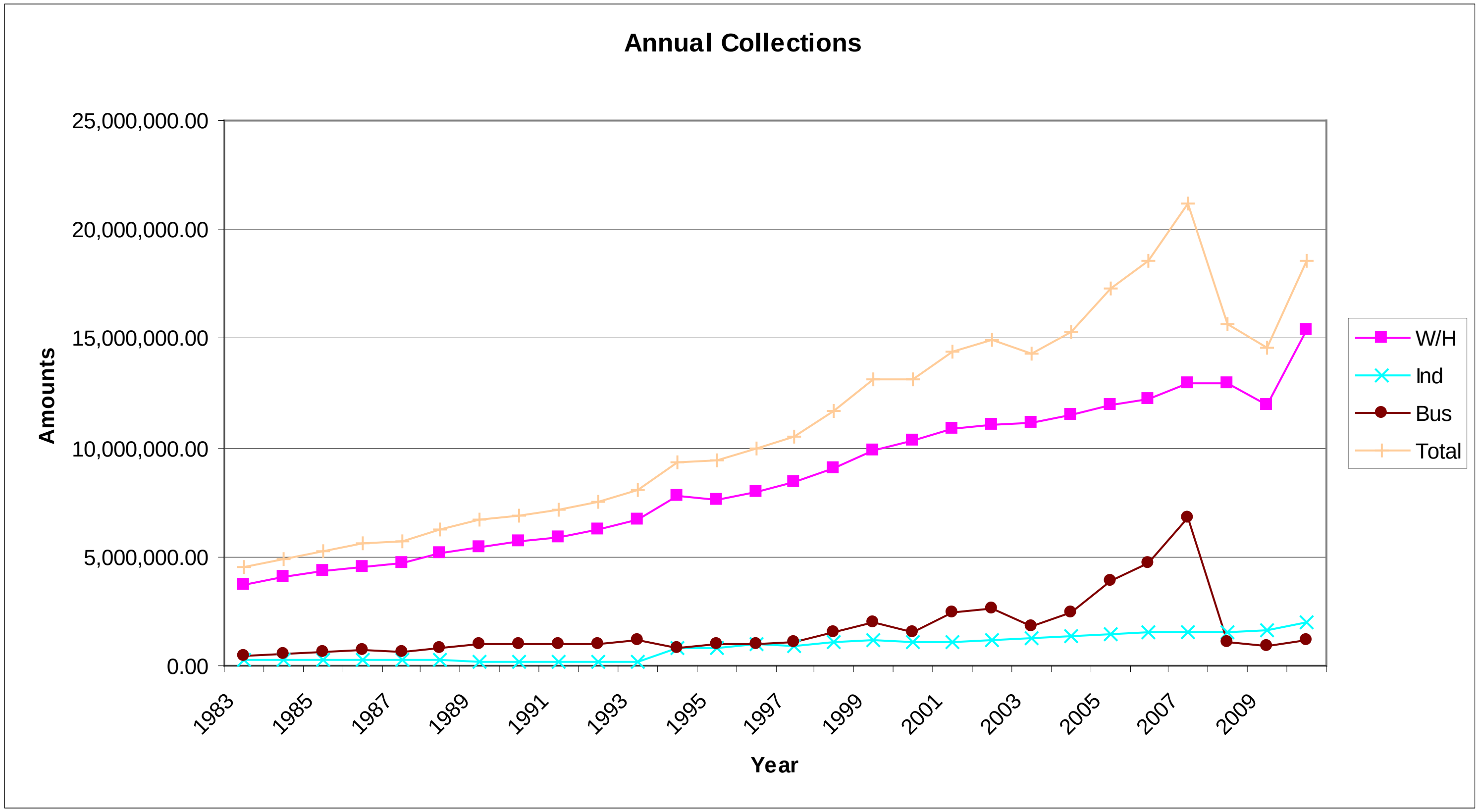
2010 Collections

In November 2009, residents approved the first tax increase since Findlay's income tax was enacted in 1967. By 6,393 votes to 5,336, the rate went from 1 percent to 1.25 percent for tax years 2010 through 2012.

Due to the new rate, 2010 overall collections increased 27.412 percent from the prior year to $18,577,553.39. Even without the rate increase, collections in all three categories increased respectably, but actual overall collections barely trumped the 2006 total of $18,542,994.46. Individual collections were further aided by the 2009 elimination of the credit allowed to residents who work and pay tax in other communities. The individuals' fourth period 2009 estimate payments and their reconciling payments that accompanied their 2009 income tax returns were both received in 2010.

The average annual increase in total collections since 1983 increased slightly from 2009 to 4.67 percent, after factoring out the one-quarter percent rate increase.

Year	Withholding	Individuals	Business	Penalty	Interest	Court Costs	Annual Total	Percent Change
1983	3,759,023.38	256,561.98	492,979.21	10,343.79	7,712.11		4,526,620.47	
1984	4,099,910.71	261,778.12	500,817.35	18,472.18	8,775.69		4,889,754.05	8.022%
1985	4,319,335.66	266,777.96	597,036.91	19,363.93	9,217.38		5,211,731.84	6.585%
1986	4,535,912.71	280,826.24	735,800.80	23,635.45	10,229.30		5,586,404.50	7.189%
1987	4,742,921.72	277,580.70	669,662.73	22,763.67	8,740.45		5,721,669.27	2.421%
1988	5,163,757.03	226,986.09	848,066.77	25,897.25	9,846.35		6,274,553.49	9.663%
1989	5,476,502.70	170,799.84	979,710.34	26,058.96	10,949.12		6,664,020.96	6.207%
1990	5,675,101.72	188,207.58	1,025,850.19	24,888.77	9,346.84		6,923,395.10	3.892%
1991	5,931,941.86	166,208.66	1,010,756.14	27,302.08	10,643.97		7,146,852.71	3.228%
1992	6,289,451.95	186,443.83	988,063.95	33,152.40	9,890.77		7,507,002.90	5.039%
1993	6,684,164.38	205,929.18	1,155,081.49	9,493.19	6,478.25		8,061,146.49	7.382%
1994	7,758,133.70	799,090.40	795,075.82	5,872.52	9,425.80		9,367,598.24	16.207%
1995	7,575,764.07	840,226.83	1,009,398.45	8,527.82	12,019.63	2,007.15	9,447,943.95	0.858%
1996	7,980,004.16	953,301.40	998,036.93	8,179.61	16,439.74	2,192.61	9,958,154.45	5.400%
1997	8,428,257.21	940,620.66	1,114,185.32	28,090.57	17,095.17	2,443.46	10,530,692.39	5.749%
1998	9,072,423.87	1,052,110.75	1,570,677.71	9,235.34	13,624.36	2,288.12	11,720,360.15	11.297%
1999	9,898,733.34	1,200,636.61	1,984,944.09	13,131.96	22,186.85	3,293.53	13,122,926.38	11.967%
2000	10,349,064.23	1,124,236.26	1,579,555.77	15,574.38	24,984.17	3,861.17	13,097,275.98	-0.195%
2001	10,824,788.06	1,083,722.97	2,409,620.03	15,791.53	22,365.10	4,404.67	14,360,692.36	9.646%
2002	11,081,952.87	1,158,561.01	2,640,371.74	16,413.76	25,945.33	7,461.63	14,930,706.34	3.969%
2003	11,168,674.96	1,265,421.63	1,844,708.55				14,278,805.14	-4.366%
2004	11,487,765.80	1,353,537.81	2,424,514.11				15,265,817.72	6.912%
2005	12,000,950.29	1,461,004.10	3,869,817.42				17,331,771.81	13.533%
2006	12,266,197.92	1,561,949.10	4,714,847.44				18,542,994.46	6.988%
2007	12,926,239.03	1,511,186.46	6,748,538.47				21,185,963.96	14.253%
2008	12,988,959.04	1,582,588.29	1,114,157.16				15,685,704.49	-25.962%
2009	11,990,526.45	1,640,212.82	949,911.69				14,580,650.96	-7.045%
2010	15,385,538.83	1,973,146.33	1,218,868.23				18,577,553.39	27.412%


Annual Collections
25,000,000.00
20,000,000.00
15,000,000.00
10,000,000.00
5,000,000.00
0.00
Amounts
1983
1985
1987
1989
1991
1993
1995
1997
1999
2001
2003
2005
2007
2009
Year
W/H
Ind
Bus
Total