

## **Revision Notice**

# **2005 Corporation Franchise Tax Instructions**

### **Recent Developments in the *Cuno* Decision**

The U.S. Court of Appeals for the Sixth Circuit announced in late January 2005 that the court had denied the state of Ohio's petition for an *en banc* rehearing of the court's September 2004 decision in *Cuno v. DaimlerChrysler*, 04a0293p.06, United States Court of Appeals for the Sixth Circuit, September 2, 2004. However, the court did agree to postpone enforcement of the September 2004 decision pending the state of Ohio's appeal to the U.S. Supreme Court. Because of these developments, the tax commissioner has revised his information release. Set forth below in its entirety is the revised information release:

#### **CFT 2004-03**

#### **CORPORATE FRANCHISE TAX INFORMATION RELEASE – Questions Regarding Ohio's New Manufacturing Machinery and Equipment Tax Credit – R.C. 5733.33 & 5747.31 – Issued September 2004; Revised February 2005**

This information release addresses questions the Ohio Department of Taxation (ODT) has received regarding Ohio's tax credit for purchases of new manufacturing machinery and equipment for use in Ohio. At the present time, taxpayers may continue to claim (i) the Ohio tax credit for such new manufacturing machinery and equipment as provided by Ohio Revised Code sections (R.C.) 5733.33 and 5747.31 and (ii) all other tax credits that ODT directly or indirectly administers.

In *Cuno v. DaimlerChrysler, Inc.* (Sept. 2, 2004), a three-judge panel of the U.S. Sixth Circuit Court of Appeals issued an opinion holding that the Ohio tax credit for new manufacturing machinery and equipment violates the Commerce Clause of the U.S. Constitution and enjoined enforcement of the credit. The state of Ohio then petitioned the court for a rehearing (*en banc*), but on January 18, 2005 the full U.S. Sixth Circuit Court of Appeals denied the state's petition. The state of Ohio will soon petition the U.S. Supreme Court for it to review the U.S. Sixth Circuit Court of Appeals' decision in *Cuno* (a writ of certiorari).[See endnote #1.]

Because the state of Ohio will soon be petitioning the U.S. Supreme Court to review the U.S. Sixth Circuit Court of Appeals' decision in *Cuno*, the state of Ohio recently petitioned the U.S. Sixth Circuit Court of Appeals to stay the issuance of the mandate, that is, to postpone putting into effect its earlier decision that enjoined enforcement of the credit. On January 31, 2005 the U.S. Sixth Circuit Court of Appeals did, in fact, agree to stay the issuance of the mandate. [See endnote #2.] Because the U.S. Sixth Circuit Court of Appeals did stay the mandate, ODT is not currently enjoined from administering the tax credit. As such, taxpayers may continue claiming the credit for purchases of new manufacturing machinery and equipment qualifying for the credit under Ohio law.

ODT will issue future notifications to taxpayers and practitioners as the situation warrants. If you have questions regarding the legal implications of continuing to claim this tax credit or other tax credits, ODT urges you to seek advice from tax counsel.

#### **Endnotes:**

1. If the U.S. Supreme Court issues to the U.S. Sixth Circuit Court of Appeals a writ of certiorari, then the U.S. Supreme Court will hear the state of Ohio's appeal of the U.S. Sixth Circuit Court of Appeals' *Cuno* decision. Federal law does not require that the U.S.

Supreme Court issue the writ of certiorari; issuing the writ is discretionary. If the U.S. Supreme Court does not issue the writ of certiorari, then there are no further appeals, and the U.S. Sixth Circuit Court of Appeals' *Cuno* decision (which "enjoined enforcement of the credit") becomes final.

2. The order in its entirety states as follows: "Upon consideration of the appellees' motion to stay mandate, It is ORDERED that the mandate be stayed to allow time to file a petition for a writ of certiorari, and thereafter until the Supreme Court disposes of the case, but shall promptly issue if the petition is not filed within ninety days from the date of final judgment by this court." United States Court of Appeals for the Sixth Circuit, Case No. 01-3960, order filed January 31, 2005.

## Recent Legislation

When the Department of Taxation originally posted the 2005 franchise tax instructions to its website, Substitute House Bill 362 (HB 362), 125<sup>th</sup> General Assembly was pending before the Ohio General Assembly. Containing several tax provisions, HB 362 was subsequently passed and signed by the governor on December 30, 2004. Set forth below is a summary of the franchise tax provisions of this new law. See also, the tax commissioner's December 2004 information release entitled "Income and Franchise Tax Updates" ([http://tax.ohio.gov/divisions/communications/information\\_releases/cft200404.stm](http://tax.ohio.gov/divisions/communications/information_releases/cft200404.stm)), which summarizes HB 362 and provides additional year-end information unrelated to the new law.

**Substitute House Bill 362 (HB 362), 125<sup>th</sup> General Assembly.** This new law enacted the following franchise tax provisions, which are effective December 30, 2004:

- 1. Job Training Credit – R.C. section 5733.42.** The amendment to the job training credit eliminates the first-come, first-served basis of distributing the \$20 million of available credit and allows the director of the Ohio Department of Job and Family Services to adopt a rule that establishes criteria and procedures for distribution of the credit. For additional information on the credit and the proposed rule please visit the Department of Job and Family Services' website at <http://www.odjfs.state.oh.us/ottc/info/>.
- 2. Federal taxable income before net operating loss deduction and special deductions.** By amending R.C. section 5733.04, the Ohio General Assembly adopted for franchise tax purposes the changes to the Internal Revenue Code (IRC) enacted by Congress since R.C. section 5733.04 was previously amended (IRC section 5733.04 was previously amended by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly, effective for taxable years ending on or after June 26, 2003). As a result of HB 362's amendment to R.C. section 5733.04, franchise taxpayers are not required to reverse the effects of the changes to the IRC enacted before December 31, 2004. Were it not for the amendment, Ohio franchise taxpayers would be required to compute their federal taxable income "starting point" on their Ohio franchise tax by applying the IRC as it existed on June 26, 2003. Set forth below is the Department of Taxation's analysis of the Ohio Supreme Court's decision in the case of *State v. Gill* (1992), 62 Ohio St 3d 53.

The amendment to R.C. section 5733.04 applies to taxable years ending on or after the December 30, 2004 effective date of HB 362 (see *Lakengren v. Kosydar* (1975), 44 Ohio St.2d 199). However, section 5 of the bill specifically allows taxpayers whose taxable year ended in 2004 but prior to the effective date of HB 362 to irrevocably elect to apply the amendment to the taxpayer's taxable year ending in 2004. A fiscal year-end taxpayer makes the irrevocable election merely by filing its 2005 franchise tax report reflecting federal taxable income without adjustment to reverse the effects of the federal changes enacted after June 26, 2003.

If the taxpayer's taxable year for the 2005 franchise tax report ended before December 30, 2004 and the taxpayer does not make the election described in section 5 of the bill, then the taxpayer must adjust its federal taxable income starting point on its 2005 franchise tax report to reverse the effects of the changes to the Internal Revenue Code enacted after June 26, 2003 and before December 30, 2004. If the adjustment increases income, make the adjustment as a miscellaneous federal tax adjustment on Schedule B, line 1(e). If the adjustment decreases income, make the adjustment as a miscellaneous federal tax adjustment on Schedule B, line 2(i).

**Caution to calendar year-end taxpayers that made a tsunami donation in January 2005:** In January 2005 Congress enacted P.L. 109-1. This new federal law allows taxpayers that in January 2005 made a cash charitable contribution for the relief of victims in areas affected by the December 26, 2004, Indian Ocean tsunami, to treat that contribution as if it were made on December 31, 2004. Applying the *Gill* decision (see below), taxpayers, which for their taxable year ending December 31, 2004 compute their federal taxable income by claiming such a deduction on their federal income tax return, must increase the federal taxable income starting point on their 2005 franchise tax return by the amount of the tsunami deduction claimed on the 2004 federal income tax return. Make the adjustment as a miscellaneous federal tax adjustment on Schedule B, line 1(e).

***Analysis of the Ohio Supreme Court's decision in State v. Gill (1992), 62 Ohio St 3d 53 as it applies in determining the federal taxable income starting point of the Ohio franchise tax report.***

- R.C. section 5733.04(G) defines the term "Internal Revenue Code" as used throughout Chapter 5733 as meaning "the 'Internal Revenue Code of 1986,' 100 Stat. 2085, 26 U.S.C.A. 1, as amended."
- In applying that definition for purposes of determining the federal taxable income starting point for Ohio franchise tax purposes, each time the Ohio General Assembly amends R.C. section 5733.04 the Ohio General Assembly adopts the IRC as it exists on the date of enactment of the amendment to R.C. 5733.04. It is that version of the IRC that applies in determining Ohio taxable income until the next time the Ohio General Assembly amends R.C. section 5733.04. As such, amendments to the IRC made after the amendment to R.C. section 5733.04 do not apply in determining Ohio taxable income (and the related federal taxable income starting point on the Ohio franchise tax report) until the Ohio General Assembly again amends R.C. section 5733.04 and thereby adopts the federal changes.
- Application of new federal income tax law to the Ohio franchise tax without the Ohio General Assembly's amending R.C. section 5733.04 would violate Section 1, Article II of the Ohio Constitution. Section 1, Article II prohibits the Ohio General Assembly from delegating its state legislative authority to any other body (by allowing the charitable contribution deduction without amending R.C. section 5733.04, the Ohio General Assembly would be unconstitutionally delegating its legislative authority to the U.S Congress).
- Because the Ohio General Assembly has yet to amend R.C. section 5733.04 following the January 2005 amendment to the IRC by P.L. 109-1, the federal amendment does not yet apply in computing federal taxable income for Ohio franchise tax purposes. Therefore, franchise taxpayers having a December 31, 2004 taxable year end and claiming on their federal income tax return for that taxable year a deduction for a charitable contribution made in January 2005 for victims of the tsunami must increase the federal taxable income starting point on their franchise tax report by the amount of such deduction.



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# 2005



## Ohio Corporation Franchise Tax Report Instructions

# Contents

	Page
<b>Recent franchise tax legislation and court decisions</b> .....	1
<b>General instructions</b> .....	3
1. Who must file .....	3
2. Entities exempt from the franchise tax .....	5
3. Tax rates and minimum fee .....	6
4. Nexus .....	7
5. Impact of Public Law 86-272 .....	7
6. Dissolution or surrender of license .....	7
7. Exit tax .....	8
8. Accounting period – taxable year .....	9
9. Method of computing tax .....	10
10. Time, place, and method for filing and payment .....	10
(A) Filing date, payment date, declaration of estimated tax .....	10
(B) Extension and additional extension .....	10
(C) Place .....	11
(D) EFT method of payment .....	11
11. Interest on underpayments and overpayments .....	11
12. Penalties for late payment, failure to file, or late filing .....	11
13. Penalty safe-harbor for estimated payments .....	11
14. Officers, statutory agent, and signature .....	12
15. Reporting federal changes .....	12
16. Amounts reported from federal tax return .....	12
17. Methods of accounting .....	12
18. Rounding-off to whole dollar amounts .....	13
19. Records retention .....	13
20. Holding companies of insurance companies, public utilities, and financial institutions .....	13
21. Qualifying holding company .....	13
22. High-tech start-up company .....	13
23. Combined report .....	14
24. Enterprise zone tax benefits .....	15
25. Assessments .....	15
26. Application for refund and petition for reassessment .....	16
27. Taxpayer's Bill of Rights – requests for an opinion of the tax commissioner .....	19
28. Sham transaction, economic reality, substance over form, and step transactions .....	20
29. Tax commissioner's right to offset refund .....	20
<b>Line instructions</b>	
<b>Schedule A</b>	
Line 1 – Federal taxable income .....	20
Line 9 – Income (loss) from transferor corporation .....	20
Line 12 – Ohio net operating loss deduction .....	21
Line 21 – Overpayment carryforward from 2004 .....	22
Line 23 – Refundable new jobs credit and refundable credit for tax withheld by the Ohio lottery commission .....	22
Lines 29 and 30 – Overpayment credited to 2006 estimated tax and/or overpayment to be refunded .....	22
<b>Schedule B – Adjustments to federal taxable income</b> .....	22
Lines 1(a) and 2(b) – Valuation limitation on gains and losses from capital assets and 1231 assets .....	23
Lines 1(b) and 2(f) – Losses from the sale of Ohio public obligations; interest on public obligations and purchase obligations and gains from the sale of Ohio public obligations .....	23
Line 1(c) – Amounts claimed as a credit for taxes paid by a qualifying pass-through entity .....	24
Lines 1(d) and 2(h) – Net loss from an “exempted investment” in a public utility and net income from an “exempted investment” in a public utility .....	24
Lines 1(e) and 2(i) – Depreciation expense adjustment from Schedule B-4 .....	24
Line 2(c) – Dividends received .....	25
Line 2(d) – Adjustment for targeted jobs tax credit or work opportunity credit .....	25
Line 2(e) – Net interest income from exempt U.S. obligations .....	25

**Schedule B – Adjustments to federal taxable income – continued**

Line 2(g) – Contributions to an individual development account program .....	25
--	----

<b>Schedule B-2 – Foreign source income deduction .....</b>	<b>25</b>
---	-----------

<b>Schedule C – Allocable income .....</b>	<b>26</b>
--	-----------

Line 1 – Bonus depreciation adjustment .....	26
--	----

Line 2 – Nonbusiness income .....	27
-----------------------------------	----

<b>Schedules D and D-2 – Apportionment ratio .....</b>	<b>29</b>
--	-----------

Property factor .....	30
-----------------------	----

Payroll factor .....	31
----------------------	----

Sales factor .....	31
--------------------	----

<b>Schedules D-2 – Net worth base apportionment formula .....</b>	<b>32</b>
---	-----------

<b>Schedule E – Balance sheet .....</b>	<b>33</b>
---	-----------

<b>Schedule F – Computation of taxable value .....</b>	<b>33</b>
--	-----------

Line 1 – Net worth (assets minus liabilities) .....	33
---	----

Line 2 – Qualifying amount (if the taxpayer is a related member to a qualifying holding company) .....	33
--	----

Line 4 – Exempted assets .....	34
--------------------------------	----

Line 6 – Ohio apportionment ratio .....	34
---	----

<b>Schedule G –Tax Computation .....</b>	<b>34</b>
--	-----------

<b>Schedule A-1 – Nonrefundable credits .....</b>	<b>35</b>
---	-----------

1. Credit for taxes paid by a qualifying pass-through entity .....	35
--	----

2. Credit for qualifying affiliated groups .....	35
--	----

3. Credit for recycling and litter prevention donations .....	36
---	----

4. Credit for maintaining railroad crossing warning devices .....	36
---	----

5. Job retention credit .....	36
-------------------------------	----

6. Second credit for purchases of new manufacturing machinery and equipment (7.5%–13.5% credit) .....	36
---	----

7. Job training credit .....	39
------------------------------	----

8. Credit for qualified research expense .....	40
--	----

9. Credit for eligible new employees in an enterprise zone .....	40
--	----

10. Credit for eligible costs associated with a voluntary action (Brownfield site clean-up) .....	41
---	----

11. Credit for employers that establish on-site child daycare center .....	41
--	----

12. Ethanol plant investment credit .....	41
---	----

13. Credit for grape production property .....	41
--	----

14. Export sales credit .....	41
-------------------------------	----

15. Technology investment credit .....	41
--	----

16. Enterprise zone day-care credit and enterprise zone training credit .....	42
---	----

17. Research and development loan repayment credit .....	42
--	----

<b>Schedule B-3 – Related entity adjustments and related member adjustments .....</b>	<b>42</b>
---	-----------

Related entity adjustments .....	43
----------------------------------	----

Related member adjustments .....	44
----------------------------------	----

**Tables**

Tax commissioner rules applicable to the Ohio corporation franchise tax .....	46
---	----

Franchise tax information releases .....	46
--	----

Ohio franchise tax forms .....	48
--------------------------------	----

Nonrefundable credits, credit carryforward periods and code sections .....	49
--	----

Years in which O.R.C. section 5733.33 manufacturer's credit 1/7 <sup>th</sup> amounts must be used .....	50
--	----

Bonus depreciation and/or IRC section 179 add-back years and deduction years .....	51
--	----

1972 – 2005 Schedule of franchise tax rates, litter tax rates, interest and penalty .....	52
---	----

Taxpayer assistance addresses and phone numbers .....	53
---	----



## 2005 Franchise Tax Instructions

In our effort to serve Ohio taxpayers in a cost-effective manner with limited resources the Department of Taxation did not mail this franchise tax instruction booklet with the tax form. Instead, this booklet is available on the Department of Taxation's Web site: [www.tax.ohio.gov](http://www.tax.ohio.gov). For those taxpayers that do not have access to the Internet, printed instructions can be obtained by calling toll-free 1-800-282-1782.

If any of the preprinted information on the form (i.e. the corporation's legal name, Ohio license/charter number or federal employer identification number) is incorrect, please contact us with the correct information at any of the telephone numbers listed in the back of this booklet.

Unless otherwise stated, all references are to the Ohio Revised Code (O.R.C.). Links to the Ohio Revised Code, Administrative (Tax Commissioner) Rules, the department's information releases, tax forms and other information are available on our Web site. We encourage you to visit our Web site at:

[www.tax.ohio.gov](http://www.tax.ohio.gov)

### Notice: The Ohio Tax Department Will Follow I.R.S. Notice 2004-54.

I.R.S. Notice 2004-54 provides for alternative preparer-signature procedures for federal income tax paper returns that paid practitioners prepare on behalf of their clients. Paid preparers can follow those same procedures with respect to the following Ohio paper returns: Ohio school district and individual income tax returns, Ohio withholding tax returns (employer and pass-through entity) and Ohio corporation franchise tax reports. Statutory authority: O.R.C. sections 5703.262(B) and 5747.08(F).

### Recent Legislation and Significant Court Decisions

#### Legislation

**Please see  
Revision Notice  
at the front  
of this booklet.**

#### Decisions

##### U.S. Sixth Circuit Court of Appeals

*Cuno v. DaimlerChrysler*, 04a0293p.06, United States Court of Appeals for the Sixth Circuit, September 2, 2004.

As a result of the *Cuno* decision, the tax commissioner issued franchise tax information release CFT 2004-03 in September 2004 and revised the information release in February 2005.

**Please see  
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of this booklet.**

#### Ohio Supreme Court Decisions

None

#### Court of Appeals Decisions

None

#### Board of Tax Appeals Decisions

*Federated Department Stores v Zaino*, BTA No. 2002-V-103 (1-9-2004). The Department of Taxation appealed the board's decision to the Ohio Supreme Court.

*Issue:* Following the taxpayer's emergence from Chapter 11 reorganization on February 4, 1992 and the taxpayer's adoption of "fresh-start reporting," should the taxpayer's 1993 franchise tax net worth base reflect the taxpayer's higher net worth "fresh-start" values determined in accordance with Generally Accepted Accounting Principles (GAAP) and reported to the Securities and Exchange Commission (SEC) on form 10-K and to shareholders in the taxpayer's annual report? Or, instead, should the taxpayer's 1993 franchise tax net worth base reflect the taxpayer's lower net worth "pre-fresh-start" historical values also prepared in accordance with GAAP and included in a balance sheet within the "notes" to the annual report to shareholders?

*Holding:* The board stated that the issue before it was not to choose from alternative sets of books (one set of books utilized by the taxpayer in its annual report and SEC form 10-K, and another set of books depicting the taxpayer's fiscal situation before emerging from bankruptcy and adopting fresh-start reporting). Rather, the issue was whether the books upon which the taxpayer relied in reporting its net worth values on the 1993 franchise tax report were consistent with

GAAP. The board then agreed with the taxpayer that the earliest date that the taxpayer could have adopted fresh-start reporting was February 4, 1992. So, the taxpayer's use of the lower net worth amount was correct, and the "1993 corporation franchise tax report, which was prepared in conformance with generally accepted accounting principles, accurately reflects its book values as of February 1, 1992."

*Facts and discussion:*

- The taxpayer has a January 31 fiscal year end. Therefore, for purposes of the 1993 franchise tax report net worth base, the value of the taxpayer's issued and outstanding shares is determined as of February 1, 1992, the beginning of the taxpayer's annual accounting period that includes January 1 of tax year 1993. See O.R.C. section 5733.05.
- On October 28, 1991 the taxpayer submitted a plan of reorganization to the bankruptcy court, which was modified and approved by the court on January 10, 1992.
- The taxpayer emerged from Chapter 11 bankruptcy reorganization on February 4, 1992.
- The independent auditor's report accompanying the taxpayer's 1991 annual report stated in relevant part: "On February 4, 1992 the Company emerged from bankruptcy. . . the company accounted for the reorganization as of February 1, 1992 and adopted 'fresh-start reporting' . . ." (*emphasis added*).
- Note 1 of the taxpayer's 1991 annual report provides in relevant part: "As of February 1, 1992, in accordance with AICPA Statement of Position 90-7 . . . the Company adopted 'fresh-start reporting' and reflected the effects of such adoption in the financial statements for the 52 weeks then ended" (*emphasis added*).
- AICPA Statement of Position 90-7 (SOP 90-7) sets out reporting principles for the financial statements of entities that have emerged from Chapter 11 reorganization. SOP 90-7 provides that such entities should apply those principles "as of the confirmation date or as of a later date when all material conditions precedent to the plan's becoming binding are resolved" (*emphasis by the board*).
- AICPA Auditing Standard 560 (AU 560) entitled "Subsequent Events" requires disclosure of events or transactions subsequent to the balance sheet date, but prior to the issuance of the financial statements. Paragraph 5 of AU 560 states in relevant part as follows: "Occasionally such events may be so significant that disclosure is best made by supplementing the historical statements with pro forma financial data giving effect to the event as if it had occurred on the date of the balance sheet" (*emphasis by the board*). In preparing its 1991 annual report the taxpayer concluded that AU 560 required the taxpayer to present fresh-start reporting on its balance sheet as of February 1, 1992 as if the taxpayer emerged from bankruptcy by that date.
- On its 1993 franchise tax report the taxpayer reported negative net worth in the amount of \$334,536,641 based

upon the taxpayer's February 1, 1992 net worth values prior to its reorganization and adoption of fresh-start reporting. The taxpayer paid the 1993 franchise tax minimum fee of \$50.

- Upon audit of the taxpayer's 1993 franchise tax report the tax commissioner assessed the taxpayer based on the February 1, 1992 fresh-start values reflected in the taxpayer's 1991 Annual Report to shareholders and the taxpayer's 10-K report to the SEC.

The taxpayer argued that pursuant to SOP 90-7 the earliest date that it could implement fresh-start reporting was February 4, 1992, the date it emerged from bankruptcy. The taxpayer testified that it did not actually adopt fresh-start reporting until February 4, 1992 because all of the material conditions to the reorganization plan had not become binding before that date. Accordingly, the taxpayer argued that its 1993 franchise tax report correctly reported the taxpayer's February 1, 1992 lower net worth pre-fresh-start values, and the taxpayer asked that the board not rely on the taxpayer's representations made in portions of its 1991 annual report and SEC form 10-K.

*First National Bank of Lebanon v Zaino*, BTA No. 2003 M-627 (3-19-2004).

*Issue:* Is a corporation that made an S election effective January 1, 1998 exempt from the 1998 franchise tax based on the corporation's taxable year ending in 1997 during which taxable year the S election was not in effect?

*Holding:* The Board of Tax Appeals held that First National Bank of Lebanon was subject to the franchise tax for tax year 1998 because the S election was not in effect for its taxable year ending in 1997. The board stated that First Federal ". . . remains a corporation exercising its franchise during the calendar year in which the franchise is payable." The board then noted that the S election made on January 1, 1998 exempted the corporation from the 1999 franchise tax based on the taxable year ending in 1998, the first taxable year for which the S election was in effect.

*Statute:* Franchise tax is charged against every corporation exercising its franchise "during the calendar year in which that amount is payable." See R.C. section 5733.01.

"A corporation that has made an election under subchapter S, chapter one, subtitle A, of the Internal Revenue Code for its taxable year under such code is exempt from the tax imposed by section 5733.06 of the Revised Code that is based on that taxable year." See O.R.C. section 5733.09(B).

"'Taxable year' means the period prescribed by division (A) of section 5733.031 of the Revised Code upon the net income of which the value of the taxpayer's issued and outstanding shares of stock is determined under division (B) of section 5733.05 of the Revised Code or the period prescribed by division (A) of section 5733.031 of the Revised Code that immediately precedes the date as of which the total value of the corporation is determined under division (A) or (C) of section 5733.05 of the Revised Code." See R.C. section



5733.031. **Note:** The above-quoted definition of “taxable year” applies to the taxable year here at issue. Although that definition was subsequently amended, the amendment has no impact on the issue or the decision.

“Tax year” means the calendar year in and for which the tax imposed by section 5733.06 of the Revised Code is required to be paid.” See O.R.C. section 5733.04(F).

### General Instructions and Information

**This instruction booklet applies to taxpayers other than financial institutions.** This instruction booklet does not apply to financial institutions because the law applicable to financial institutions differs substantially from that applicable to other corporations. The franchise tax instructions for financial institutions are contained in a separate instruction booklet available on the Department of Taxation’s Web site. Financial institutions must file franchise tax form FT 1120FI.

**This instruction booklet applies to telephone companies, electric companies and combined electric companies.** However, because local exchange telephone companies, electric companies and combined electric companies are subject to franchise tax deduction, add-back, apportionment, credit and tax computation provisions that do not apply to other franchise taxpayers, we have prepared supplemental schedules and instructions for those companies. **The supplemental instructions are not included in this instruction booklet. Rather, the supplemental schedules and instructions are available in a separate file on our Web site.** Electric companies and combined electric companies are subject to the franchise tax for tax years 2002 and thereafter. Local exchange telephone companies are subject to the franchise tax for tax years 2005 and thereafter.

The Ohio corporation franchise tax is an excise tax imposed on both domestic and foreign corporations for the privilege of doing business in Ohio, owning capital or property in Ohio, holding a charter or certificate of compliance authorizing the corporation to do business in Ohio, or otherwise having nexus with Ohio during a calendar year. Unless an exemption applies (see general instruction #2), a corporation is subject to the franchise tax for each calendar year (tax year) that on the first day of January of that calendar year the corporation holds an Ohio charter, does business in Ohio, owns or uses a part or all of its capital or property in Ohio, holds a certificate of compliance authorizing the corporation to do business in Ohio, or otherwise has nexus with Ohio under the Constitution of the United States.

**Tax year and taxable year. The calendar year in and for which the tax is paid is called the “tax year.”** The tax year is also referred to as the “report year.” The franchise tax for tax year 2005 is paid for the privilege of doing business in Ohio during the calendar year 2005. **The accounting period on which the tax is based is called the “taxable year”** and is defined as “. . . a period ending on the date immediately preceding the date of commencement of the corporation’s annual accounting period that includes the first day of January of the tax year.” Generally, a corporation’s taxable year for

franchise tax purposes is the same as the corporation’s taxable year for federal income tax purposes. However, a franchise tax taxable year may consist of an aggregation of more than one federal taxable year and can exceed one year in length. The franchise tax for tax year 2005 is based upon the taxpayer’s activity during its taxable year ending in 2004. See O.R.C. sections 5733.031(A) and 5733.04(E), Tax Commissioner Rules 5703-5-01 through 5703-5-04 and general instruction #8.

The franchise tax is levied on the value of a corporation’s issued and outstanding shares of stock. Generally a taxpayer corporation must determine the value of its issued and outstanding shares of stock under both the net income base and the net worth base and pay the tax on the base that produces the greater tax. However, different rules apply to financial institutions, qualifying holding companies and certain high-tech start-up companies:

- Financial institutions are not subject to the tax on the net income base, but are subject to the tax on the net worth base at a higher rate than other taxpayers. See general instruction #1 C.
- Qualifying holding companies and certain high-tech start-up companies are not subject to the tax on the net worth base but are subject to the tax on the net income base. See general instructions #21 and #22.

Although a corporation that dissolves its Ohio charter or surrenders its license to conduct business in Ohio during 2004 is not subject to the franchise tax for tax year 2005, such corporation may be subject to the “exit tax” (see general instruction #7 and O.R.C. section 5733.06(H)) or the corporation’s income may be required to be included in the income of a transferee corporation (see O.R.C. section 5733.053 and the instructions for Schedule A, line 9).

## 1. WHO MUST FILE

### A. Corporations

Unless an exemption applies (see general instruction #2), each for-profit domestic corporation (a corporation organized for-profit under the laws of Ohio) and each Chapter 1729 corporation (agricultural cooperative) organized not-for-profit under the laws of Ohio is subject to the Ohio franchise tax. In addition, unless an exemption applies each foreign corporation (a corporation organized under the laws of another state, a possession or instrumentality of the United States or a foreign country) organized for-profit, and each not-for-profit foreign agricultural cooperative organized or operating in the same or similar manner as a Chapter 1729 agricultural cooperative, for the privilege of doing business in Ohio, owning or using part or all of its capital or property in Ohio, holding a certificate of compliance with the laws of Ohio authorizing it to do business in Ohio, or otherwise having nexus with Ohio under the Constitution of the United States is subject to the franchise tax.

A corporation that is subject to the franchise tax must file an Ohio corporation franchise tax report. Financial institutions must file form FT 1120FI; all other C corporations must file form FT 1120. Although S corporations (including S corporations that are financial institutions) and qualified subchapter S subsidiaries are generally not subject to the franchise tax, they must file a Notice of S Corporation Status, form FT 1120S (see general instruction #2).

## B. Entity classification

Any entity that is treated as a corporation for federal income tax purposes is also treated as a corporation for franchise tax purposes. Thus, if a business trust, partnership or limited liability company (LLC) is treated as a corporation for federal income tax purposes, it also will be treated as a corporation for franchise tax purposes. See the Income Tax Audit Division's information release entitled "IRS 'Check-the-box' Entity Selection Regulations" dated August 19, 1997 (available on the Department of Taxation's Web site). Also see O.R.C. section 5733.01 as amended by Amended Substitute House Bill 215, 122nd General Assembly and section 222 of the Bill.)

**Disregarded entity.** For purposes of Chapter 5733 the term "disregarded entity" means an entity that for its taxable year is by default, or has elected to be, disregarded as an entity separate from its owner pursuant to 26 C.F.R. 301.7701-3. **Any entity that is treated as a "disregarded entity" for federal income tax purposes is also treated as a disregarded entity for franchise tax purposes.** Accordingly, a single member LLC that is treated as a division of its corporate member for federal income tax purposes will be treated as a division of the corporation for franchise tax purposes. That is, for franchise tax purposes:

- If the disregarded entity has nexus with Ohio, then the owner has nexus with Ohio.
- An interest in a disregarded entity is treated as ownership of the assets and liabilities of the disregarded entity itself.
- A disregarded entity's income, including gain or loss, is included in the owner's O.R.C. chapter 5733 net income.
- Any sale or other disposition of an interest in a disregarded entity is treated as a sale or other disposition of the disregarded entity's underlying assets or liabilities and the gains and losses from such sales are included in the owner's Chapter 5733 net income.
- A disregarded entity's property, payroll and sales are included in the owner's property, payroll and sales factor computations.

See O.R.C. sections 5733.01(F) and 5745.01(D).

Nevertheless, a single member LLC is a pass-through entity as defined in O.R.C. section 5733.04(O), and the corporate member is a qualifying investor whose distributive share includes the sum of the income, gain, expense or loss of a disregarded entity (see O.R.C. section 5733.40(S)). So, a single member LLC with Ohio nexus is subject to the pass-through entity tax imposed by O.R.C. section 5733.40 unless the corporate member files a franchise tax report and includes in its income the income and apportionment data of the LLC. O.R.C. section 5733.41 provides that the pass-through entity tax imposed by that section does not apply if all the members of the pass-through entity are taxpayers for purposes of O.R.C. section 5733.04 without regard to O.R.C. section 5733.09. **Accordingly, if the corporation files the required franchise tax report and does not claim that the corporation lacks nexus with Ohio, then the single member LLC is excepted from the pass-through entity tax.** Regardless of whether or not the corporate single member complies and files a franchise tax report, the Department of Taxation maintains that if the LLC has nexus with Ohio, the corporate single member has nexus with Ohio, and the department will pursue and enforce that position against the corporation. See the amendments to O.R.C. sections 5733.01 and 5733.40 as enacted by Amended Substitute Senate Bill 261, 124<sup>th</sup> General Assembly effective June 5, 2002 and the department's July 3, 2002 information release entitled "Pass-through Entity Tax: Certain Estimated Tax Payments Due September 16, 2002."

See general instruction #2A for the treatment of qualified subchapter S subsidiaries.

## C. Financial Institutions

A financial institution is not subject to the tax on the net income base but is subject to the tax on the net worth base at a higher rate than other taxpayers. Financial institutions must file form FT 1120FI. The instructions for form FT 1120FI are contained in a separate instructions booklet. O.R.C. section 5725.01 defines a "financial institution" as any of the following:

- A national bank organized and existing as a national bank association pursuant to the "National Bank Act," 12 U.S.C. 21;
- A federal savings association or federal savings bank that is chartered under 12 U.S.C. 1464;
- A bank, banking association, trust company, savings and loan association, savings bank, or other banking institution that is incorporated or organized under the laws of any state;
- Any corporation organized under 12 U.S.C. 611 to 631;
- Any agency or branch of a foreign depository as defined in 12 U.S.C. 3101;

- A company licensed as a small business investment company under the Small Business Investment Act of 1958, 72 Stat. 689, 15 U.S.C. 661, as amended; or
- A company chartered under the Farm Credit Act of 1933, 48 Stat. 257, 12 U.S.C. 1131(d), as amended.

Specifically excluded from the definition of “financial institution” (and from the definition of “dealer in intangibles”) are insurance companies, credit unions and corporations or institutions organized under the Federal Farm Loan Act and amendments thereto. In addition, for franchise tax purposes a production credit association is not a financial institution.

## 2. ENTITIES EXEMPT FROM THE FRANCHISE TAX

### A. S Corporations and Qualified Subchapter S Subsidiaries

An S corporation generally is not subject to the Ohio corporation franchise tax. See O.R.C. section 5733.09 and the Department of Taxation’s July 31, 1994 information release entitled “Taxation of S Corporations and Their Shareholders,” which sets forth the department’s policy interpretation of Ohio franchise tax law applicable to S corporations. (The information release is available on the department’s Web site.) However, an S corporation is subject to the franchise tax and must file an Ohio Corporation Franchise Tax Report (form FT 1120) if the S corporation was a C corporation during any portion of a taxable year ending in 2004. See *First National Bank of Lebanon v. Zaino*, BTA Case No. 2003, M-627, March 19, 2004 and *Sanders Health & Fitness Inc. v. Limbach*, BTA Case No. 88-E-559, June 21, 1991. Furthermore, an S corporation must file form FT 1120 and is subject to the franchise tax on the income attributed to it from a C corporation if the S corporation was the survivor of a merger with another corporation that was subject to the Ohio corporation franchise tax and the S corporation was a transferee as defined in O.R.C. section 5733.053(A)(3). See the Department of Taxation’s September 24, 1992, franchise tax information release “Application of Ohio Revised Code Section 5733.053 (Transferor Statute) to the Merger of a C Corporation into an S Corporation.” The information release is available on the department’s Web site.

If a corporation is an S corporation for any portion of calendar year 2004, the S corporation must file a Notice of S Corporation Status (form FT 1120S) by June 30, 2005. **The due date of the notice does not change even if the S corporation has an extension to file the federal 1120S after that date.**

A “qualified subchapter S subsidiary” (QSSS), as defined in IRC section 1361(b)(3)(B), is exempt from the franchise tax that is based on the taxable year for which the parent S corporation makes the election under I.R.C. section 1361(b)(3)(B)(ii). A QSSS is

exempt because its separate legal existence is ignored for purposes of the franchise tax. If a corporation is a QSSS for any portion of 2004, the corporation must file by June 30, 2005 a notice of S Corporation Status separate from the Notice of S Corporation status filed by its parent S corporation.

**Note 1: S corporations and the pass-through entity tax.** For taxable years beginning after 1997 an S corporation that does business in Ohio or otherwise has nexus with Ohio is subject to the tax on pass-through entities enacted by Am. Sub. H.B. No. 215, 122nd General Assembly (Budget Bill) if one or more shareholders of the S corporation is a nonresident for any portion of the S corporation’s taxable year and the S corporation does not file a composite Ohio income tax return (form IT 4708) on behalf of all the nonresident shareholders.

**Note 2: QSSS’s and the pass-through entity tax.** For taxable years ending after June 4, 2002, a QSSS that does business in Ohio or otherwise has nexus with Ohio must pay the pass-through entity tax if its parent S corporation has shareholders that are not residents of Ohio. However, the various exemptions applying to S corporations also apply to QSSS’s. Accordingly, a **QSSS is not subject to the pass-through entity tax if either: (1) the S corporation owner/shareholder irrevocably acknowledges that the S corporation has nexus with Ohio, includes in its income the income of the QSSS, and makes a good faith and reasonable effort to comply with Ohio’s pass-through entity tax or (2) the S corporation files a composite Ohio income tax return (form IT 4708) on behalf of all nonresident shareholders and includes on that composite return the nonresident shareholder’s proportionate share of the income of the QSSS.** See the following: (1) O.R.C. sections 5733.402 and 5733.41; (2) the Department of Taxation’s July 3, 2002 income tax information release entitled “Pass-through entity tax: certain estimated tax payments due September 16, 2002”; and (3) the instructions for form IT 1140, Tax Return for Pass-through Entities. All of the above are available on the department’s Web site.

### B. Public Utilities, Insurance Companies, Credit Unions and Dealers in Intangibles

- Any corporation, whether foreign or domestic, owning and operating a public utility required to file reports and pay an excise tax upon its gross receipts or gross earnings under O.R.C. chapter 5727 is not subject to the franchise tax. Railroads are subject to the franchise tax for tax years 1993 and thereafter. Electric companies and combined electric companies are subject to the franchise tax for tax years 2002 and thereafter. Local exchange telephone companies are subject to the franchise tax for tax years 2005 and thereafter.



- Insurance, fraternal, beneficial, bond investment, health maintenance organizations and other corporations required by law to file annual reports with the Superintendent of Insurance are not subject to the franchise tax.
- Credit unions and dealers in intangibles are not subject to the franchise tax.

### C. REITs, RICs and REMICs

An entity, whether organized as a corporation or business trust, defined to be a real estate investment trust (REIT) under I.R.C. section 856, a regulated investment company (RIC) under I.R.C. section 851, or a real estate mortgage investment conduit (REMIC) under I.R.C. section 860D is not subject to the franchise tax **if the REIT, RIC or REMIC provides to the tax commissioner by March 31, 2005 the report of the entity's investors required by O.R.C. section 5733.09(C). Except for closely held or privately held REITs, RICs and REMICs**, the tax commissioner by administrative journal entry dated June 28, 2004 has waived the investor report for such entities for tax year 2005. **The tax commissioner did not waive the new reporting requirements if either the REIT, RIC or REMIC is a related member to the taxpayer or the taxpayer is a related member to the REIT, RIC or REMIC.** See the tax commissioner's administrative journal entry at the following address: [http://tax.ohio.gov/divisions/corporation\\_franchise\\_filing\\_exemptions.stm](http://tax.ohio.gov/divisions/corporation_franchise_filing_exemptions.stm).

Each closely held REIT, RIC or REMIC for which the tax commissioner did not waive the reporting requirements must submit to the tax commissioner by March 31, 2005 the name of the entity with a list of the names, addresses and social security or federal identification numbers of all investors, shareholders and other similar investors who owned any interest or invested in the entity during the preceding calendar year. Taxpayers having questions regarding this matter should contact the Department of Taxation at 614-433-7862.

Send the report to the following address:

Ohio Department of Taxation  
Corporation Franchise Tax Unit  
REIT-RIC-REMIC Report  
P.O. Box 2619  
Columbus, Ohio 43216-2619

### D. Corporations in Bankruptcy

A corporation in bankruptcy proceedings under Chapter 7 of the U. S. Bankruptcy Code is not liable for the franchise tax for that portion of the tax year during which the corporation's franchise is impaired because of the Chapter 7 bankruptcy proceedings. See O.R.C. section 5733.06(E). A corporation in Chapter 7 bankruptcy is not exempt from the minimum fee. A corporation in reorganization proceedings under Chapter 11 of the U.S. Bankruptcy Code is not exempt

from the franchise tax because a corporation in reorganization is not equivalent to a corporation that has been adjudicated bankrupt or for which a receiver has been appointed. See *Vought Industries, Inc. v. Tracy* (1995), 72 Ohio St. 3d 261.

### E. Corporations Exempt Under Federal Law

Certain corporations are exempt from state tax because Congress has expressly granted them immunity as a "federally chartered instrumentality." For example, federal land bank associations are exempt from state taxes under Section 2098, Title 12, U.S. Code. Certain other corporations are exempt because the United States Constitution's Supremacy Clause grants implied immunity to private corporations that actually stand in the federal government's shoes and are so closely connected to the government that the two cannot realistically be viewed as separate entities, at least insofar as the activity being taxed is concerned. An Agricultural Credit Association (ACA) is not immune from state taxation as a "federally chartered instrumentality" because (i) Congress has not expressly granted immunity to ACAs, and (ii) the Supremacy Clause of the United States Constitution does not grant implied immunity to ACAs. See *Farm Credit Serv. of Mid-America v. Zaino* (2001), 91 Ohio St.3d 564.

### 3. TAX RATES AND MINIMUM FEE

The tax rates as set forth in O.R.C. section 5733.06 are as follows:

- The first \$50,000 of Ohio net income is subject to tax at a rate of 5.1%. However, corporations that meet the ownership requirements to file a combined report must share the \$0 to \$50,000 tax bracket amount to which the 5.1% rate applies regardless of whether or not they actually file combined. Related taxpayers must prorate the \$0 to \$50,000 bracket amount on form FT OTAS. Related taxpayers may prorate the \$0 to \$50,000 bracket amount in any amount they choose, but a taxpayer's pro-rata amount may not be less than zero. The proration, however made, applies to both the franchise tax and the litter tax.
- Ohio net income in excess of \$50,000 is subject to tax at a rate of 8.5%.
- The net worth rate for corporations other than financial institutions is 4 mills. In addition, the maximum net worth tax is \$150,000 per taxpayer. The \$150,000 limit applies separately to each member of a combined report; there is not an overall net worth limit for a combined group of taxpayers.
- The net worth rate for financial institutions is 13 mills, and the \$150,000 net worth tax limit does not apply to financial institutions. Financial institutions are exempt from the net income base.
- The minimum franchise tax fee is \$1,000 if (i) the sum of the taxpayer's gross receipts from its activities within

and without Ohio during the taxable year equals or exceeds \$5 million, or (ii) the total number of the taxpayer's employees within and without Ohio at any time during the taxable year equals or exceeds 300. In determining whether or not the taxpayer's gross receipts and number of employees equal or exceed those thresholds, the taxpayer must include its proportionate share of the gross receipts of any pass-through entity in which the taxpayer has a direct or indirect ownership interest and its proportionate share of the number of employees of the pass-through entity. Furthermore, the term, gross receipts, as used here, includes receipts that generate nonbusiness income and receipts from the sale of capital assets and IRC section 1231 assets whether those sales generate business income or nonbusiness income.

The minimum fee is \$50 for taxpayers whose gross receipts and whose number of employees are less than the thresholds discussed above. See O.R.C. section 5733.06(E) as amended by Amended House Bill 95, 125<sup>th</sup> General Assembly.

#### 4. NEXUS

Unless an exemption applies, a corporation that has nexus in or with Ohio under the Constitution of the United States is subject to the franchise tax. A corporate investor in a pass-through entity that does business in Ohio or otherwise has nexus in or with Ohio under the Constitution of the United States is itself doing business in Ohio and has nexus with Ohio. Accordingly, a foreign corporation is subject to the franchise tax even if the corporation's only connection with Ohio is as (i) a partner or limited partner in a partnership that has nexus with Ohio or (ii) as a member of a limited liability company that has nexus with Ohio. (A pass-through entity is defined as an S corporation, partnership, limited liability company or any other person, other than an individual, trust or estate, if the partnership, limited liability company or other person is not classified for federal income tax purposes as an association taxed as a corporation. See the following: (1) O.R.C. section 5733.04(O); (2) the Department of Taxation's September 2001 information release describing the standards the department will apply to determine whether an out-of-state corporation is subject to the franchise tax; and (3) the department's March 15, 2001 information release entitled "Corporation Franchise Tax Nexus for Nonresident Limited Partners Following the UCOM Decision." The information releases and the Ohio Revised Code are available on the department's Web site.

#### 5. IMPACT OF PUBLIC LAW 86-272

Public Law 86-272, 15 U.S.C. 381-384, is federal law that restricts Ohio and all other states from imposing a tax on or measured by income derived by an out-of-state company within the state's borders if the only business activity of the company within the state consists of the solicitation of orders for sale of **tangible personal property**. This restriction is limited to orders sent outside

the state for acceptance or rejection and, if accepted, filled by shipment or delivery from a point outside the state.

P.L. 86-272 does not prohibit Ohio from asserting that an out-of-state corporation has nexus with Ohio. In fact, implicit in the application of P.L. 86-272 is that an out-of-state corporation does have nexus. P.L. 86-272 merely prohibits the imposition of the Ohio corporation franchise tax based on net income in certain situations. Those situation are listed in issue IV (A) of the Department of Taxation's information release entitled "Corporation Franchise Tax – Nexus Standards" issued in September 2001 and revised May 19, 2003. Because the net worth base of the corporation franchise tax is not a tax on or measured by income, **P.L. 86-272 offers no protection from the Ohio corporation franchise tax based on net worth.**

The issue of whether or not P.L. 86-272, Section 381, Title 15, U.S. Code prohibits the imposition of franchise tax measured by the net income base is determined by the taxpayer's activities during the taxable year in which the taxpayer earned that income – not by the taxpayer's activities during the tax year following the taxable year or on January 1 of the tax year. If the taxpayer's activities in Ohio during the taxable year exceeded the activities protected by P.L. 86-272 but in the related tax year the taxpayer's activities did not exceed the protected activities, then P.L. 86-272 offers no protection for the tax year, and for that tax year the corporation is subject to the franchise tax on the net income base. Conversely, if the taxpayer's activities in Ohio during the taxable year did not exceed the activities protected by P.L. 86-272 but in the related tax year the taxpayer's activities did exceed the protected activities, P.L. 86-272 does offer protection for the tax year, and for that tax year the corporation is not subject to the franchise tax on the net income base. See *LSDHC Corp. v. Zaino*, 98 Ohio St.3d 450, 2003-Ohio-1911.

#### 6. DISSOLUTION OR SURRENDER OF LICENSE

Each corporation seeking dissolution of its charter or surrender of its license to transact business in Ohio must submit to the Ohio Secretary of State a filing fee along with various affidavits or documents evidencing that the corporation has paid or adequately guaranteed various taxes and fees. For further information regarding the requirements of dissolving a corporation's charter or surrendering a corporation's license to conduct business in Ohio, please contact the office of the Ohio Secretary of State, 180 East Broad Street, 16th Floor, Columbus, Ohio 43215 or telephone that office at (614) 466-3910 or call toll free at 1-877-767-3453. For specific information regarding obtaining a tax release from the Ohio Department of Taxation, please contact the Ohio Department of Taxation, Dissolution Unit, P.O. Box 182382, Columbus, Ohio 43218-2382 or call 614-995-4422 or 1-888-405-4039.

The mere termination of business activities or voluntary dissolution does not exempt a corporation from the franchise tax. A corporation that on January 1 of the tax



year holds a charter or license to transact business in Ohio is subject to the Ohio franchise tax for that tax year even if prior to the beginning of the tax year it has ceased all business activities in Ohio and has applied for certificates showing the payment or adequate guarantee of all required taxes. See O.R.C. section 5733.17.

**A corporation that previously had nexus with Ohio but is not a franchise taxpayer on January 1 of the tax year (for example, because the corporation dissolved, merged out of existence or surrendered its license to conduct business in Ohio prior to January 1 of the tax year) may be subject to an income-based tax on its Ohio net income that was not reported on an earlier franchise tax report. See “Exit Tax” below.**

## **7. EXIT TAX – O.R.C. SECTION 5733.06(H)**

An exiting corporation is a corporation that previously had nexus with Ohio but is not a franchise taxpayer for the tax year (for example, because the corporation dissolved, merged out of existence or surrendered its license to conduct business in Ohio prior to January 1 of the tax year). Nevertheless, if a transferee corporation (see O.R.C. section 5733.053 and the instructions for Schedule A, line 9) is required to include in its Ohio taxable income the income of a transferor corporation that would otherwise be an exiting corporation, then the transferor is not an exiting corporation and the exit tax does not apply. An “exiting corporation” is subject to an income-based exit tax on its unreported Ohio net income that was earned in the two calendar years prior to the tax year to the extent that such income was not previously included on the corporation’s franchise tax report. The exit tax does not apply to an exiting financial institution.

An exiting corporation is not subject to the minimum fee and is not subject to the tax on the net worth base or to the litter tax on the net worth base. However, an exiting corporation is subject to the litter tax on the net income base. An exiting corporation is subject to the O.R.C. section 5733.052 combination provisions and all deductions and credits applicable to franchise taxpayers. An exiting corporation must compute its exit tax on the franchise tax form applicable to the tax year following the calendar year during which the corporation exits Ohio. The corporation must file the report by May 31 of the year following the year the corporation exits Ohio. However, upon request by the exiting corporation, the tax commissioner can extend the date for filing the report, but not the date for paying the tax.

**The relationship between the exit tax and the transferor statute.** Amended Substitute Senate Bill 287, 123rd General Assembly amended both the exit tax (O.R.C. section 5733.06(H)) and the transferor statute (O.R.C. section 5733.053) and established the following relationship between the two:

(1) If on January 1 following the transfer of substantially all the transferor’s assets to the transferee the

transferor remains in existence, then the transferor is subject to the franchise tax and the transferor statute does not apply to the transferee. See O.R.C. section 5733.053(B): *“The transferee shall add such income in computing its tax for the same tax year or years that such income would have been reported by the transferor if the transfer had not been made. The transferee shall add such income only to the extent the income is not required to be reported by the transferor for the purposes of the tax imposed by divisions (A) and (B) of section 5733.06 of the Revised Code.”*

(2) If on January 1 following the transfer of substantially all the transferor’s assets to the transferee the transferor is not subject to the franchise tax (because, for example, the transferor merged into the transferee), and if for federal income tax purposes the transfer qualifies for nonrecognition of gain and loss, then the O.R.C. section 5733.053 transferor statute applies to the transferee and the exit tax does not apply to the transferor. That is, the transferee is required to add to its income the income of the transferor and the franchise tax attributes of the transferor pass to the transferee.

(3) If on January 1 following the transfer of substantially all the transferor’s assets to the transferee the transferor is not subject to the franchise tax imposed by divisions (A) and (B) of O.R.C. section 5733.06 (because, for example, the transferor merged into the transferee), and the O.R.C. section 5733.053 transferor statute does not apply to the transferee (because, for example, the merger is not a tax free reorganization) and if all other conditions of an exiting corporation apply, then the exit tax applies to the transferor. See O.R.C. sections 5733.06(H)(1)(d) and 5733.06(H)(6).

**Note:** The changes to the transferor statute and the exit tax, as set forth above, were originally to have been effective with the 2002 franchise tax report (see Section 13 of Am Sub SB 287). However, Amended Substitute House Bill 94, 124<sup>th</sup> General Assembly amended the effective date of the changes to the transferor statute and the exit tax statute made by Amended Substitute Senate Bill 287. Amended Substitute House Bill 94 provides that the amendments to the exit tax and to the transferor statute made by Am Sub SB 287 do not apply to any transfer for which negotiations began prior to January 1, 2001, and that was commenced in and completed during calendar year 2001, unless the transferee makes an election prior to December 31, 2001, to apply those amendments.

An exiting corporation that has a fiscal year end must include on one franchise tax report all of its unreported net income even if the income would have been included on two franchise tax reports had the corporation remained subject to the franchise tax. See O.R.C. section 5733.06(H).

**EXAMPLE:**

ABC Inc. is chartered in another state and has operated in Ohio since 1989. ABC has a January 31 fiscal year end and filed its 2004 franchise tax report based on the fiscal year beginning February 1, 2002 and ending January 31, 2003. ABC shut down its Ohio operations and legally withdrew from Ohio on December 1, 2004. ABC is not a "transferor" as defined in O.R.C. section 5733.053 because ABC did not transfer substantially all its assets or equity to another corporation in a tax-free reorganization. Although ABC is not a franchise taxpayer on January 1, 2005, ABC is nevertheless subject to the exit tax on its unreported Ohio net income earned during the 22-month period beginning February 1, 2003 and ending December 1, 2004 (the date that it withdrew from Ohio).

ABC must report its income for the entire 22-month period from February 1, 2003 to December 1, 2004 on a 2005 franchise tax report even though income for the period from February 1, 2004 to December 1, 2004 would have been reported on a 2006 franchise tax report if ABC would have had nexus with Ohio on January 1, 2006 and remained subject to the franchise tax. ABC's 2005 tax report is due by May 31, 2005, and all exit tax due is payable at that time notwithstanding other provisions of Chapter 5733 to the contrary. However, upon the taxpayer's request the tax commissioner may grant an extension of time to file the report (but the law contains no provision for an extension of time to pay).

**8. ACCOUNTING PERIOD – TAXABLE YEAR**

For franchise tax purposes a corporation's taxable year is a period ending on the date immediately preceding the date of commencement of the corporation's annual accounting period that includes the first day of January of the tax year. Generally, a corporation's taxable year for franchise tax purposes is the same as the corporation's taxable year for federal income tax purposes. If a corporation's taxable year is changed for federal income tax purposes, the corporation's franchise tax taxable year is changed accordingly.

A franchise tax taxable year may consist of an aggregation of more than one federal taxable year and can exceed one year in length. For example, a franchise tax taxable year can consist of two (or more) federal taxable years and can exceed one year in length in certain instances where the taxpayer changes its federal taxable year or the taxpayer is acquired by another corporation and then changes its taxable year.

In addition, the law gives the tax commissioner authority to write rules prescribing an appropriate period as the taxable year for the following: (a) a corporation that has changed its taxable year for federal income tax purposes; (b) a corporation that as a result of a change of ownership has two or more short federal taxable years; and (c) a new taxpayer that would otherwise not have a taxable year.

The tax commissioner has adopted the following rules regarding franchise taxpayers' taxable years and change of accounting period:

- 5703-5-01 – Definitions Applicable to Rules 5703-5-01 to 5703-5-05 of the Administrative Code
- 5703-5-02 – Date as of Which the Value of a Taxpayer's Issued and Outstanding Shares of Stock is Determined
- 5703-5-03 – Dates on Which a Taxpayer's Taxable Year Begins and Ends
- 5703-5-04 – Changes of a Taxpayer's Annual Accounting Period. **Note: Effective for taxable years ending after December 31, 2003, Rule 5703-5-04 eliminates income proration for taxable years that exceed one year in length. In addition, the amended rule clarifies that if, as the result of a change of ownership, a taxpayer has two short-period federal taxable years because of the taxpayer's inclusion in one or more consolidated federal income tax returns, and if the year-end of the taxpayer's annual accounting period remains the same after the change of ownership as it was before the change, then for purposes of this rule there is not a change of the taxpayer's annual accounting period.**

Important features of these rules are as follows:

- Generally, a taxpayer's taxable year begins on the date immediately following the end of the taxpayer's prior taxable year and ends on the date immediately preceding the beginning of the taxpayer's annual accounting period that includes the first day of January of the tax year.
- If a taxpayer changes its annual accounting period, there is (i) no period that is not subject to tax, and (ii) no period that is subject to tax in more than one tax year.
- A franchise tax "taxable year" under certain circumstances may be more than or less than one year in length.

Except for taxpayers that have changed their accounting period and taxpayers that have two or more federal taxable years that ended in calendar year 2004, taxpayers must determine the value of their issued and outstanding shares of stock under the net income basis and the net worth basis as follows:

**For report year 2005 taxpayers that have a calendar year end: Use the period ending December 31, 2004.**

**For report year 2005 taxpayers that have a fiscal year end: Use the fiscal period ending in 2004.** However, taxpayers filing their first report should see below.

**For report year 2005 taxpayers that are filing their first report: Use the applicable period set forth below:**

- A. If a taxpayer incorporated in Ohio during 2004 and adopted a fiscal period ending in 2004, then the taxpayer must use the accounting period commencing on the date of incorporation and concluding with the last day of the fiscal period ending in 2004.
- B. If the taxpayer is a foreign corporation and first became an Ohio taxpayer during 2004 (that is, during 2004 the corporation began doing business in Ohio, began owning or using part or all of its capital or property in Ohio, obtained a license authorizing it to do business in Ohio or otherwise established nexus with Ohio under the Constitution of the United States) and after it became an Ohio taxpayer its fiscal year ended in 2004, then the taxpayer must use the accounting period commencing on the earliest of the following: (i) the date that it began doing business in Ohio; (ii) the date that it began owning or using a part or all of its capital or property in Ohio; (iii) the date that it obtained a license authorizing it to do business in Ohio; or (iv) the date that it established nexus with Ohio under the Constitution of the United States. The accounting period will end on the taxpayer's fiscal year ending in 2004.
- C. All other new taxpayers will use the accounting period commencing with the earliest of the four dates set forth in B above, and concluding with December 31, 2004. See paragraphs (E)(2) and (E)(4) of Tax Commissioner Rule 5703-5-03.

**If the corporation changed its taxable year in 2003 or 2004 or if the corporation had more than one federal taxable year that ended in calendar year 2004, please see the rules referred to above in determining your taxable year. For a copy of the rules visit our Web site.**

## 9. METHODS OF COMPUTING TAX

In determining the Ohio franchise tax due, taxpayers other than financial institutions and qualifying holding companies and certain high-tech start-up companies must compute the tax on both the net worth base and the net income base and pay the tax on the base that produces the greater tax. Financial institutions are not subject to the tax on the net income base, and qualifying holding companies and certain high-tech start-up companies are not subject to the tax on the net worth base. In any event franchise taxpayers are subject to a minimum fee.

Although an "exiting corporation" is not subject to the franchise tax, it may be subject to an income based exit tax. An exiting corporation is not subject to the minimum fee. See general instruction #7.

## 10. TIME, PLACE AND METHOD FOR FILING AND PAYMENT

Except as otherwise provided, if a payment or document is mailed on or before the due date but delivered after the required date, the postmark date is deemed the date of delivery. If the due date of the report or the due date of an extension or payment falls on a Saturday, Sunday or legal holiday, then the report, extension, or payment may be made on the next succeeding day which is not a Saturday, Sunday or legal holiday. Certain large taxpayers must pay by electronic funds transfer (see general instruction #10 D).

### A. Filing Date; Payment Date; Declaration of Estimated Tax

The filing and payment of the Ohio franchise tax for report year 2005 is due between January 1 and March 31, 2005. However, if by January 31 the taxpayer did not file the Ohio corporation franchise tax report and if by January 31 the taxpayer did not make full payment of the tax, then by January 31 the taxpayer must file form FT 1120E, Declaration of Estimated Corporation Franchise Tax and must pay one-third of the estimated tax, but not less than the minimum fee.

### B. Extension

The tax commissioner will grant an extension of time for filing the report until May 31 if by March 31 the taxpayer submits form FT 1120ER together with payment of the second one-third of the estimated tax due.

### Additional Extension

The tax commissioner will grant an additional extension of time for filing the report beyond May 31 if the corporation has been granted an extension by the IRS and by May 31 the taxpayer submits form FT 1120EX together with the balance of the tax due. The second extension extends the filing date to the 15th day of the month following the month for which the IRS has granted an extension for filing the corporation's federal income tax return. The taxpayer must attach a copy of the federal extension to the franchise report, form FT 1120, when filed.

The following table lists the latest possible due dates for filing the 2005 franchise tax report for the various taxable years ending in 2004. The table assumes the following:

- If the taxpayer's taxable year ended on or after August 31, 2004, the taxpayer has the maximum allowable federal extension,
- The taxpayer timely filed franchise tax forms FT 1120E, FT 1120ER, and, if applicable, FT 1120EX, and
- The taxpayer has timely made all estimated franchise tax payments.



<b>Taxable Year Ending In 2004</b>	<b>Latest Possible Due Date for Filing the 2005 Franchise Tax Report</b>
01/31/04 through 7/31/04	05/31/2005
08/31/2004	06/15/2005
09/30/2004	07/15/2005
10/31/2004	08/15/2005
11/30/2004	09/15/2005
12/31/2004	10/15/2005

**Note: Payment of all franchise tax for tax year 2005 is due by May 31, 2005, even if the taxpayer has an extension to file after that date. Each member of a combined franchise tax report must file its own separate forms FT 1120E, FT 1120ER and FT 1120EX.**

#### **C. Place**

File the franchise tax report with the Ohio Department of Taxation, P.O. Box 27, Columbus, Ohio 43216-0027.

**However, if the report is an amended report, please do not send it to the address above. Rather, an amended report that reflects a balance due or no change in liability should be mailed to the following address:**

**Ohio Department of Taxation  
Corporation Franchise Tax Unit  
P.O. Box 2476  
Columbus, Ohio 43216-2476**

**On the other hand, an amended report that reflects an overpayment should be mailed along with an Application for Corporation Franchise Tax Refund (form FT REF) to the following address:**

**Ohio Department of Taxation  
Audit Division  
P.O. Box 530  
Columbus, Ohio 43216-0530**

**Please indicate that a report is an amended report by checking the box on the front of the report.**

#### **D. EFT Method of Payment**

A taxpayer must pay by electronic funds transfer (EFT) if the taxpayer's total franchise tax liability after reduction for nonrefundable credits exceeded \$50,000 for the second preceding tax year. Nevertheless, payments made with an amended report can not be made by EFT. For further EFT information see the Department of Taxation's July 31, 1994 franchise tax information release entitled "Recently Enacted Legislation Revises the Requirements for Corporations Paying Corporate Franchise Tax by Electronic Funds Transfer (EFT)." The information release is available on the department's Web site. Please direct questions regarding the EFT payment program to the Ohio Treasurer of State's office at 30 East Broad Street, 9<sup>th</sup>

floor, Columbus, Ohio 43215 or telephone that office toll free at 1-877-EFT-Ohio (338-6446).

#### **11. INTEREST ON UNDER- AND OVERPAYMENTS**

If a corporation fails to pay the tax by the due date, interest accrues on the unpaid tax. Interest on tax due is charged in addition to any penalties that may be incurred for late filing and late payment or failure to file. The period of the underpayment runs from the date the tax payment was required to be made to the date on which such payment is made. **There is no safe-harbor from interest on the underpayment of estimated tax.**

Interest on franchise tax overpayments runs from whichever of the following dates is the latest until the date the refund is paid:

- the date of payment,
- the 90th day after the final date the franchise tax report was required to be filed, or
- the 90th day after the date that the franchise tax report was filed.

Interest on an overpayment resulting from a net capital loss carryback is payable from the due date plus extensions for the report in which the loss arises (rather than from the report year to which the loss is carried back).

The interest rate on underpayments is the same as the interest rate on overpayments. **During calendar year 2005 interest on both underpayments and overpayments will accrue at the rate of 5% per annum.**

#### **12. PENALTIES FOR LATE PAYMENT, FAILURE TO FILE, OR LATE FILING**

- Penalty may be imposed for failure to timely pay the tax (including estimated tax – see estimated tax safe harbor, below). Late payment penalty may not exceed 15% of the delinquent payment. See O.R.C. section 5733.28(A)(2) as amended by Senate Bill 200, 124<sup>th</sup> General Assembly. Under prior law the O.R.C. section 5733.28(A)(2) penalty for late payment could not exceed twice the interest charged under O.R.C. section 5733.26(A).
- Penalty may be imposed for failure to file or to timely file a report. The penalty imposed may not exceed the greater of (i) \$50 per month up to \$500 or (ii) 5% per month of the tax due shown on the report up to 50%.
- Additional penalties may be imposed for filing a fraudulent report and for filing a fraudulent refund claim.

#### **13. PENALTY SAFE-HARBOR FOR ESTIMATED PAYMENTS**

Substitute Senate Bill 200 (Taxpayer Services II), 124<sup>th</sup> General Assembly, effective September 6, 2002 enacted the following safe-harbor applicable to penalty on underpayment of estimated tax.

- With respect to estimated payments, the O.R.C. section 5733.28(A)(2) failure to pay penalty applies to two periods: (1) "any period of delinquency ending prior to the first day of June of the tax year" and (2) "any period of delinquency commencing the first day of June of the tax year and concluding on the extended due date." See O.R.C. section 5733.021.
- For purposes of determining the O.R.C. section 5733.28(A)(2) failure to pay penalty for any period of delinquency ending prior to the first day of June of the tax year, the commissioner may charge penalty on the delinquent portion of the estimated tax and estimated tax means the lesser of 100% of last year's tax or 90% of this year's tax. See O.R.C. section 5733.021(C)(1)(c).
- For purposes of determining the O.R.C. section 5733.28(A)(2) failure to pay penalty for any period of delinquency commencing the first day of June of the tax year and concluding on the extended due date, the commissioner may charge penalty on the delinquent portion of the estimated tax and estimated tax means 90% of this year's tax. See O.R.C. section 5733.021(C)(2)(c).

**Note:** In addition to creating the above noted safe-harbor, Senate Bill 200 amended the O.R.C. section 5733.28(A)(2) penalty computation. The O.R.C. section 5733.28(A)(2) failure to pay penalty now provides that the penalty may not exceed 15% of the delinquent payment. Prior law provided that the failure to pay penalty could not exceed twice the interest charged under O.R.C. section 5733.26(A).

#### 14.OFFICERS, STATUTORY AGENT AND SIGNATURE

All franchise tax reports must be signed by one of the following: the president, vice-president, secretary, treasurer, general manager, superintendent, or managing agent of such corporation in Ohio. If a domestic corporation has not completed its organization, one of its incorporators must sign the report. In addition, each taxpayer must list its president, secretary and treasurer along with the name and address of its statutory agent.

#### 15.REPORTING FEDERAL CHANGES

If as a result of amendment or adjustment to the taxpayer's federal income tax return by the taxpayer or by the Internal Revenue Service or, if as a result of any other recomputation or redetermination a change occurs in the taxpayer's federal tax liability or any item entering the computation of the taxpayer's federal taxable income as reported for federal income tax purposes, the taxpayer must report such change to the Ohio Department of Taxation in the form of an amended report by the earliest of the following dates:

- One year after final determination of the adjustment for federal income tax purposes,
- One year after the taxpayer paid the additional federal income tax as a result of the adjustment (whether or not the adjustment was agreed to) or

- One year after the taxpayer received a federal income tax refund as a result of the adjustment.

This provision applies even if the three-year statute of limitations has passed and applies to amended reports that reflect overpayments as well as to amended reports that reflect underpayments. If the amended report reflects an underpayment, the amended report must be accompanied by payment of any additional tax and interest. If the amended report reflects an overpayment, the amended report must be accompanied by either form FT REF, Application for Refund, or by a statement that sets forth the full and complete reason for the overpayment. See *Abitibi-Price Corporation and Subsidiaries v. Tracy*, BTA No. 98-N-401 (3-12-01) and refer to general instruction #26.

**Upon completing an amended report, please check the amended report box on the front of the report and, as explained below, send the report to the appropriate address. Please do not send an amended report to P.O. Box 27 (the address on the form). Rather, an amended report that reflects a balance due or no change in liability should be mailed to the following address:**

**Ohio Department of Taxation  
Corporation Franchise Tax Unit  
P.O. Box 2476  
Columbus, Ohio 43216-2476**

**On the other hand, an amended report reflecting an overpayment should be mailed with form FT REF or a statement explaining the reason for the overpayment to the following address:**

**Ohio Department of Taxation  
Audit Division  
P.O. Box 530  
Columbus, Ohio 43216-0530**

#### 16.AMOUNTS REPORTED FROM FEDERAL TAX RETURN

Amounts reported from the federal form 1120 or 1120A, as well as Ohio adjustments, apportionment and allocations are subject to verification and audit by the Ohio Department of Taxation.

#### 17.METHODS OF ACCOUNTING

A taxpayer's method of accounting under the net income base must be the same as its method of accounting for federal tax purposes. If the taxpayer changes its method of accounting for federal income tax purposes, the taxpayer must also change its method of accounting under the net income base. In the absence of any method of accounting for federal income tax purposes, income must be computed under such method as the tax commissioner deems proper.

The tax on the net worth base must be determined from the books of the corporation that the taxpayer must keep in accordance with a generally recognized and approved



accounting system. The tax-basis method of accounting is a generally recognized and approved accounting system. See *Gray Horse, Inc. v. Limbach* (1993), 66 Ohio St. 3d 631. If a taxpayer keeps its books both in accordance with regulatory accounting principles and in accordance with generally accepted accounting principles, the value of the taxpayer's issued and outstanding shares of stock under the net worth base (O.R.C. section 5733.05(C)) must be based upon those books kept in accordance with generally accepted accounting principles. See Tax Commissioner Rule 5703-5-08.

## 18. ROUNDING OFF TO WHOLE DOLLAR AMOUNTS

The money items of form FT 1120 and accompanying schedules must be shown as whole dollar amounts by eliminating amounts less than 50 cents and increasing amounts from 50 cents to 99 cents to the next highest dollar.

## 19. RECORDS RETENTION

Every corporation must maintain books and records that substantiate the information reported on its Ohio corporation franchise tax report. These books and records must be available for inspection by agents of the Ohio Department of Taxation for a period of four years from the later of (a) the date the taxpayer filed the franchise report or (b) the date the taxpayer was required to file the report. See the line instructions for Schedule A, line 12 for records to be maintained pertaining to net operating loss carryforwards.

## 20. HOLDING COMPANIES OF INSURANCE COMPANIES, PUBLIC UTILITIES AND FINANCIAL INSTITUTIONS

A taxpayer that owns at least 25% of the issued and outstanding shares of common stock of one or more financial institutions as defined in O.R.C. chapter 5725 or a taxpayer that owns at least 80% of the issued and outstanding shares of common stock of one or more public utilities or insurance companies as defined in O.R.C. chapters 5727 and 5725, respectively, must exclude from its sales factor the receipts from sales to such financial institutions, public utilities or insurance companies. The sales factor exclusion does not apply to receipts from sales to electric companies and combined electric companies and for tax years 2005 and thereafter, receipts from sales to local exchange telephone companies. See O.R.C. section 5733.05(B)(2)(c).

In addition, a taxpayer that owns at least 80% of the issued and outstanding shares of common stock of one or more public utilities or insurance companies may deduct, to the extent not otherwise allowed, dividends received from such public utilities and insurance companies. This deduction does not apply to dividends received from electric companies, combined electric companies or for tax years 2005 and thereafter local exchange telephone companies. For purposes of this deduction, the term "public utility" means a public utility as defined in O.R.C. chapter 5727 whether or not the public utility is doing business in Ohio and the term "insurance company"

means an insurance company that is taxable under O.R.C. chapters 5725 or 5729. See O.R.C. sections 5733.04(l)(7) and (8).

## 21. QUALIFYING HOLDING COMPANY

For tax years 1999 and thereafter a qualifying holding company is exempt from the net worth base of the franchise tax (but not the net income base). A qualifying holding company is any corporation that satisfies all six of the following requirements:

- The corporation's "intangible assets ratio" equals or exceeds 90%,
- The corporation's "investment in related members ratio" equals or exceeds 50%,
- During the taxable year the corporation's "gross income from intangible assets ratio" equals or exceeds 90%,
- The corporation is not a financial institution on the last day of the taxable year ending prior to the first day of the tax year,
- The corporation's related members adjust their net worth and debt for purposes of computing their franchise tax on the net worth base, such that the related members' debt-to-equity ratio equals the consolidated debt-to-equity ratio of the "qualifying controlled group." (A "qualifying controlled group" is defined in O.R.C. section 5733.04(M) as two or more corporations that satisfy the O.R.C. section 5733.052(A) ownership and control requirements to file a combined report.), and
- The corporation elects to be treated as a qualifying holding company for the tax year by filing form FT QHC.

For further information see form FT QHC and O.R.C. sections 5733.04(L), 5733.05(C)(2), and 5733.06(C).

## 22. HIGH-TECH START-UP COMPANIES

A corporation organized not more than three years before the March 31 unextended due date of each of the 2003, 2004, 2005, 2006 or 2007 franchise tax reports is not subject to the net worth base of the franchise tax or to the net worth base of the litter taxes if the corporation:

- Conducted business during its entire taxable year as a *qualified trade or business*;
- Uses more than 50% of its assets located in Ohio (based on net book value) solely to conduct activities that constitute a qualified trade or business; and
- During the taxable year is not a related member (as defined in O.R.C. section 5733.042 and modified by O.R.C. section 5733.06(C)(2)(d)) to another person treated as a corporation.

The term "qualified trade or business" means any trade or business that primarily involves research and development, technology transfer, bio-technology, information technology or the application of new

technology developed through research and development or acquired through technology transfer.

**So, if the corporation was organized after March 30, 2002 and meets the additional requirements set forth above, it can claim exemption from the net worth base as a high-tech start-up company (the statute refers to such corporations as “eligible corporations”) by checking the box at the top of page 1 of the franchise tax report. Do not complete Schedule F and do not complete lines (d), (i), or (l) of Schedule G. See O.R.C. sections 5733.06(C) and 122.15.**

### 23.COMBINED REPORTS

A *taxpayer* that on January 1 of the tax year owns or controls either directly or indirectly more than 50% of the voting stock of another *taxpayer* corporation may elect to combine net income with that corporation. A “taxpayer” is a corporation subject to the franchise tax. Taxpayers whose voting stock is more than 50% owned or controlled either directly or indirectly by another corporation or by related interests may also elect to combine net income. Brother-sister taxpayer corporations owned by an individual may elect to combine, and brother-sister taxpayer corporations owned by a parent corporation may elect to combine without inclusion of the parent corporation. However, where an election to combine is made by less than all eligible taxpayer corporations, the combined group must attach an explanation of the reason for the nonparticipation by such eligible taxpayer corporations.

An elected combination may include only taxpayers that have income [either positive income or negative income (loss)], other than dividend income, from sources within Ohio. “Income from sources within Ohio” means income that would be allocated or apportioned to Ohio if the taxpayer were not included in a combined report. Those taxpayer groups that elected to combine in prior tax years must amend their combinations to delete taxpayers that do not have income, other than dividend income, from sources within Ohio during the taxable year.

Taxpayers that elect to combine must do so in a timely filed franchise tax report. A timely filed report is a report filed within the time prescribed by O.R.C. sections 5733.02 and 5733.13. Only one member of a combined franchise tax group must satisfy the O.R.C. section 5733.052(B) timely election requirement. A combination is timely elected if any member of the combination has complied with all of the franchise tax report deadlines even if other members have not complied timely. Thus, a taxpayer that fails to make timely estimated payments and fails to file timely extension requests may file in combination with other corporations after the due date of the taxpayer’s report if another corporation in the combined group has timely made its estimated payments, has timely filed its extension requests, and has timely elected to file in combination with the taxpayer. See *Roxane Laboratories, Inc. v. Tracy* (1996), 75 Ohio St. 3d 125. Taxpayers that

first filed separately may not elect to combine by filing an amended report after the due date of the report even if the amended report is filed within the three year refund statute of limitations. See *Olan Mills Inc. of Tenn. v. Limbach* (1990), 56 Ohio St. 3d 70.

Each member of a combined franchise tax report must separately file a Declaration of Estimated Tax (form FT 1120E) and Request(s) for Extension (forms FT 1120ER and FT 1120EX). See general instructions #10 A and #10 B. Members of a combined report that fail to comply with the filing deadlines are subject to the applicable penalty and interest charges.

An election to combine may not be changed either in amended reports or in reports for future years without the written consent of the tax commissioner. The addition of a new member to a previously elected combination and the deletion of a member that was previously included (other than a corporation that does not satisfy the income or ownership requirements) is a change in that election. Accordingly, taxpayers that seek to add or delete member(s) to an already existing combination must receive the tax commissioner’s consent. See O.R.C. section 5733.052(B) and *Tranzonic Companies and Subs. v. Tracy*, BTA Case No. 90-M-1443, December 4, 1992. Taxpayers that request such consent must file form FT COM, Request for Permission to File or to Amend a Combined Corporation Franchise Tax Report.

If the above-discussed 50% ownership requirements are met, the tax commissioner may require or permit a taxpayer and one or more other corporations (whether or not such corporations are taxpayers and whether or not such corporations have income from sources within Ohio) to combine their net income. A combination of this type will not be required or permitted unless it is necessary because of intercorporate transactions to properly reflect income and the tax liability.

The Department of Taxation will generally pursue combinations or expanded combinations only in those situations where the failure either to combine or to expand the combination will result in the filing of a corporation franchise tax report that does not properly reflect income and does not properly reflect the tax liability imposed by O.R.C. section 5733.06. A timely conducted I.R.C. section 482-type study conforming with the requirements set forth in I.R.C. section 482 and in the U.S. Treasury regulations issued under section 482 will avoid this department’s seeking either a combination or an expanded combination. See the Department of Taxation’s June 23, 2000 information release entitled, “I.R.C. Section 482 Study: Safe Harbor to Avoid Ohio Corporate Franchise Tax Report Required or Expanded Combinations.” The information release is available on the department’s Web site. Taxpayers that request the tax commissioner’s permission to include in the combined report corporations that are not subject to the franchise tax must file form FT COM.

Corporations that file combined franchise tax reports must prorate combined apportioned net income to each member in the group (see form FT 1120C). Each corporation must then compute its own Ohio taxable income and net income-based tax on its own form FT 1120. Each taxpayer in a combined report must separately determine its tax on the net worth base. Net worth is not combined.

Corporations that on January 1 of the tax year meet the ownership requirements to file a combined report must share the \$0 to \$50,000 tax bracket amount to which the 5.1% rate applies regardless of whether or not they actually file combined. Related taxpayers must prorate the \$0 to \$50,000 bracket amount on form FT OTAS.

## 24. ENTERPRISE ZONE TAX BENEFITS

**Amended Substitute House Bill 95th, 125<sup>th</sup> General Assembly (Budget Bill) extends through October 15, 2009 the authority for local governments to enter into enterprise zone agreements.** See O.R.C. section 5709.62 as amended by the bill.

Businesses that establish, expand, renovate or occupy a facility pursuant to an enterprise zone agreement and that create new jobs in a certified enterprise zone without reducing employment elsewhere in Ohio may be entitled to a series of tax benefits on their Ohio corporation franchise tax report (see O.R.C. sections 5709.64 and 5709.65). Among these benefits are an employee training credit, a day-care credit (see credit #16 in the instructions for Schedule A-1), and exclusion of qualifying property and payroll from the numerators of the net income base property and payroll factors.

To qualify for franchise tax enterprise zone benefits, businesses must hold for the taxable year a Tax Incentive Qualification Certificate (issued by the Department of Development) and must hire new employees to fill nonretail positions at the facility. Also, at the time of employment at least 25% of the new employees must have been at least one of the following:

- Unemployed persons who had resided at least six months in the county in which the enterprise's project site is located;
- Job Training Partnership Act eligible employees who had resided at least six months in the county in which the enterprise's project site is located;
- Recipients of aid to dependent children, general relief or unemployment compensation benefits who had resided at least six months in the county in which the enterprise's project site is located;
- Handicapped persons, as defined under O.R.C. section 3304.11(A), who had resided at least six months in the county in which the enterprise's project site is located;
- Residents for at least one year of a zone located in the county in which the enterprise's project site is located. See O.R.C. sections 5709.64 and 5709.65.

In addition to the enterprise zone franchise tax benefits described above, a taxpayer may apply to the director of the Ohio Department of Development for an "employee tax credit certificate" for each eligible new employee the enterprise hires after June 30, 1994 at the facility to which the enterprise zone agreement applies provided that the taxpayer is complying with an enterprise zone agreement and has not closed or reduced employment at any place of business in Ohio within the 12 months preceding the application. For more information on the Credit for Eligible New Employees in an Enterprise Zone see credit #9 in the instructions for Schedule A-1.

For a further discussion and summary of Ohio's enterprise zone program see Stempfer, "Economic Development Program Opportunities In Ohio, Summary and Update Focusing on Recent Tax-Related Legislation," *Ohio Tax Review*, vol. 8.3 (1994).

## 25. ASSESSMENTS

The tax commissioner may issue an assessment against the taxpayer for any deficiency within three years after the later of the following dates:

- The final date the report subject to assessment was required to be filed, or
- The date the report was filed.

However, both the assessment statute of limitations and the refund statute of limitations may be extended for an agreed upon period if both the taxpayer and the tax commissioner consent in writing to the extension by signing form FT WAIVER. **Furthermore, if the tax commissioner disregards a sham transaction, the assessment statute of limitations is doubled.** See general instruction #28 and O.R.C section 5703.56 as enacted by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly.

An amended franchise tax report filed as a result of an adjustment to the corporation's federal income tax return (see general instruction #15) is deemed a report subject to assessment. However, the amended report does not reopen those facts, figures, computations or attachments from a previously filed report no longer subject to assessment or refund that are not affected, either directly or indirectly, by the adjustment to the corporation's federal income tax return. Furthermore, once the three-year refund statute of limitations has passed, the taxpayer may not offset the additional franchise tax resulting from IRS audit adjustments against franchise tax that the taxpayer erroneously overpaid due to errors or mistakes unrelated to the federal adjustments. See *Gen. Motors Corp. v. Limbach* (1993), 67 Ohio St. 3d 90.

The statute of limitations does not prohibit either the tax commissioner or the taxpayer from adjusting the net operating loss carried forward from a year closed to assessment or refund to a year still open to assessment or refund; nor does the statute of limitations prohibit either the tax commissioner or the taxpayer from adjusting the



unused credits carried forward from a year closed to assessment or refund to a year still open to assessment or refund. See *Consumer Direct v. Limbach* (1991), 62 Ohio St. 3d 180.

If the taxpayer does not pay the assessment within 60 days of receipt of the assessment, and does not file a petition for reassessment within 60 days of receipt of the assessment, interest accrues on the assessment at the rate prescribed in O.R.C. section 5703.47 from the date the tax commissioner issues the assessment until the taxpayer pays the assessment.

If the taxpayer disagrees with an assessment, the taxpayer may object to the assessment by filing a petition for reassessment. See general instruction #26.

## **26.APPLICATION FOR REFUND AND PETITION FOR REASSESSMENT**

Franchise taxpayers may request a refund by filing either prescribed form FT REF, **Application for Corporation Franchise Tax Refund**, or by filing an amended report accompanied by the full and complete reason for the refund claim. **Please do not file an application for refund if the claimed overpayment is shown on the originally filed franchise tax report.**

Franchise taxpayers may initiate review proceedings pertaining to a franchise tax assessment issued by the Department of Taxation by filing form FT PR, Petition for Reassessment.

### **Application for Corporation Franchise Tax Refund.**

Form FT REF applies to claimed overpayments by a taxpayer, whether made voluntarily or as the result of the payment of an assessment issued by the Ohio Department of Taxation. If the overpayment is not the result of an IRS adjustment and the statute of limitations has not been extended by form FT WAIVER (see general instruction #25), then the department must receive the application for refund or an amended report accompanied by the full and complete reason for the refund claim within three years of the date of the illegal, erroneous or excessive payment. See *Abitibi-Price Corporation and Subsidiaries v. Tracy*, BTA No. 98-N-401 (3-12-01).

**Please mail your completed form FT REF (or an amended franchise tax report along with a complete explanation of the amendment) to the following address:**

**Ohio Department of Taxation  
Audit Division  
P.O. Box 530  
Columbus, Ohio 43216-0530**

Effective September 6, 2002 for purposes of the refund statute of limitations, payment made before the due date or extended due date for filing the report to which the payment relates are deemed to have been made on the due date or extended due date (see O.R.C. section 5733.12 as amended by Substitute Senate Bill 200

(Taxpayer Services Bill II), 124<sup>th</sup> General Assembly, effective September 6, 2002). (Under prior case law payments remitted with the estimated tax report (form FT 1120E) and extension requests (forms FT 1120ER and FT 1120EX) were deemed to have been made on the earlier of the date the Ohio corporation franchise tax report was filed or the due date of the report including extensions. Thus, if a franchise tax report was filed before its extended due date, the three year refund statute of limitations began to run on the date the report was filed rather than the later extended due date. See *Hanna Mining Co. v. Limbach* (1985), 20 Ohio St. 3d 3 and *Athena Manor, Inc. v. Limbach*, BTA Case No. 91-Z-12, February 26, 1993.)

If the claimed overpayment is the result of a change in federal taxable income, then the department must receive the claim for refund within the later of the following: (a) the three-year time period set forth above or (b) the one-year period set forth in general instruction #15. However, if the refund claim is filed outside the three year refund statute of limitations and the statute of limitations has not been extended by form FT WAIVER (see general instruction #26), the refund claim can include only the direct and indirect effects of the federal adjustments. See *Gen. Motors Corp. v. Limbach* (1993), 67 Ohio St. 3d 90 and *The First Federal Savings Bank v. Tracy*, BTA Case No. 94-T-1353, August 23, 1996.

Regardless of the above provisions to the contrary, a franchise tax refund claim that is based on a capital loss carryback is timely if the refund claim is filed within three years from the due date of the franchise tax report (including extensions thereof) for the taxable year in which the capital loss arose. See *Prechter v. Tracy*, BTA Case No. 95-M-1214, April 4, 1997.

A taxpayer may not appeal an assessment by filing a claim for refund unless the taxpayer has paid the assessment. For example, if the taxpayer fails to file a petition for reassessment within 60 days of receipt of the assessment, then the taxpayer cannot file a refund claim protesting the assessment until after the taxpayer has paid the assessment.

**Uniform application for refund procedure.** Substitute Senate Bill 200, 124<sup>th</sup> General Assembly, effective June 7, 2002 enacted O.R.C. section 5703.70 to establish a uniform application for refund procedure applicable to franchise tax and various other taxes (but not to individual income tax, school district income tax, withholding tax or pass-through entity tax). If a taxpayer properly files an application for refund under a law that specifies that the O.R.C. section 5703.70 uniform procedure applies and the commissioner determines that the amount of the refund to which the applicant is entitled is less than the amount claimed, then the tax commissioner and the taxpayer must proceed as follows:

1. If the commissioner determines that the amount of the refund to which the applicant is entitled is less than

the amount that the applicant claimed, the commissioner must notify the applicant in writing by ordinary mail of the disallowed portion of the claimed refund.

2. The applicant has 60 days from the date the commissioner mails the notification to provide additional information to the commissioner and/or to request a hearing.
3. If the applicant neither requests a hearing nor provides additional information within the 60-day period described in #2 above, the commissioner will take no further action and the refund amount denied becomes final. That is, the taxpayer may not appeal to the Board of Tax Appeals the denied portion of the refund.
4. If the applicant requests a hearing within the 60-day period described in #2 above, the commissioner must assign a time and place for a hearing. After the hearing, the commissioner may make such adjustments to the refund as the commissioner finds proper and must issue a final determination. The taxpayer may appeal the commissioner's final determination to the Board of Tax Appeals pursuant to O.R.C. section 5717.02.
5. If the applicant does not request a hearing within the 60-day period described in #2 above but does provide additional information within that period, the commissioner must review the information, may make such adjustments to the refund as the commissioner finds proper, and must issue a final determination. The taxpayer may appeal the commissioner's final determination to the Board of Tax Appeals pursuant to O.R.C. section 5717.02.

**Petition for Reassessment.** Form FT PR applies only to assessments issued by the Ohio Department of Taxation. **The amount of an assessment that may be refunded under a timely filed petition for reassessment is limited to the amount of the assessment that the taxpayer paid. No portion of the amount paid with the filing of the franchise tax report is available for refund under the O.R.C. section 5733.11 petition for reassessment statute because there is no provision within O.R.C. section 5733.11 that grants the commissioner the authority to refund any amount greater than the amount that the taxpayer paid toward the assessment. The fact that the taxpayer raises additional objections to the assessment prior to the tax commissioner's final determination and the fact that the taxpayer mentions in those objections that the taxpayer is overpaid with respect to amounts paid with the original report does not convert a petition for reassessment into a timely filed refund claim with respect to amounts paid with the original report. See *International Business Machines Corp. v. Zaino* (2002), 94 Ohio St.3d 152.**

A taxpayer must file its petition within 60 days of receipt of the assessment. If the taxpayer sends the petition by certified mail, the date of postmark is considered the date

filed. If the taxpayer sends the petition by regular mail, the date the Department of Taxation receives the petition is considered the date filed. The petition must specify the items of the assessment objected to and the reasons for those objections. However, a taxpayer that has timely filed a Petition for Reassessment may raise additional written objections to the assessment at any time prior to the date of the tax commissioner's final determination. If a taxpayer fails to file the petition for reassessment within the 60-day period described above, the tax commissioner will dismiss the petition because the tax commissioner has no jurisdiction to consider a late-filed petition.

The portion of an assessment that must be paid upon the filing of a Petition for Reassessment is as follows:

1. If the sole item objected to is the assessed penalty or interest, the assessed corporation must pay the entire assessment except for the penalty.
2. If prior to the date of issuance of the assessment the assessed corporation failed to file (i) the annual report required by section 5733.02 of the Revised Code; (ii) any amended report required by O.R.C. section 5733.031(C) for the tax year at issue; or (iii) any amended report required by O.R.C. section 5733.067(D) to indicate a reduction in the amount of the credit provided under that section, the assessed corporation must pay the entire assessment except for the penalty.
3. If prior to the date of issuance of the assessment the assessed corporation filed (i) the annual report required by O.R.C. section 5733.02, (ii) all amended reports required by O.R.C. section 5733.031(C) for the tax year at issue, and (iii) all amended reports required by O.R.C. section 5733.067(D) to indicate a reduction in the amount of the credit provided under that section, and if a balance of the taxes shown due on the reports as computed on the reports remains unpaid, the assessed corporation must pay only that portion of the assessment representing any unpaid balance as shown on those reports together with all related interest.
4. If the assessed corporation does not dispute that it is a taxpayer but claims the protections of section 101 of Public Law 86-272, 73 Stat. 555, 15 U.S.C.A. 381, as amended, the assessed corporation must pay only that portion of the assessment representing any unpaid balance of taxes shown due on the corporation's annual report.
5. If none of the conditions specified in (1), (2), (3) or (4) above apply, or if the assessed corporation claims that it is not a taxpayer (that is, if the assessed corporation disputes that it is subject to the franchise tax), the assessed corporation is not required to pay any portion of the assessment.

However, any unpaid portion of the assessment which upon final determination is found to be correct bears



interest at the rate prescribed in O.R.C. section 5703.47 from the date the Department of Taxation issues the assessment until the date the taxpayer pays the assessment. See O.R.C. section 5733.11 as amended by Amended Substitute House Bill No. 215 (Budget Bill), 122nd General Assembly and section 213 of the Budget Bill. If the taxpayer decides to pay the assessment in full, such payment is not acknowledgment of agreement and will not prejudice the final determination of the petition, and the taxpayer will receive interest on any refund found due. See general instruction #11 for interest on underpayments and overpayments.

**Uniform petition for reassessment procedure.** Substitute Senate Bill 200, 124<sup>th</sup> General Assembly enacted O.R.C. section 5703.60 to establish a uniform petition for reassessment procedure and a uniform assessment correction procedure applicable to franchise tax, individual income tax, pass-through entity tax, withholding tax, school district income tax and various other taxes. If the taxpayer has filed a proper petition for reassessment for a tax whose statute specifies that the uniform reassessment procedure applies, this law permits the tax commissioner, upon receipt of additional information from the taxpayer, to correct an assessment without issuing a final determination and without a hearing. In addition, this law permits the commissioner to correct an assessment even if the taxpayer did not properly file a petition for reassessment or did not file a petition for reassessment. Set forth below is a more in-depth summary of the law.

**A. Uniform Procedure if the Taxpayer Properly Files a Petition for Reassessment**

If a taxpayer objects to an assessment by properly filing a petition for reassessment under a law that specifies that the O.R.C. section 5703.60 petition for reassessment procedure applies, then the tax commissioner and the taxpayer are to proceed as follows:

1. Upon review of the taxpayer's properly filed petition for reassessment, the commissioner must either:
  - a. Issue a **final determination** that affirms, increases, cancels or reduces (without canceling) the assessment; or
  - b. Issue a **corrected assessment** that increases, cancels or reduces (without canceling) the assessment. However, if the party assessed has requested in writing that the tax commissioner not use the corrected assessment procedure, then the tax commissioner may not issue a corrected assessment; instead, after a hearing, if the taxpayer so requests, the commissioner must issue a final determination.

**Note: A cancelled assessment is an assessment that the tax commissioner has reduced to zero by issuing either a corrected**

**assessment or a final determination. If the tax commissioner cancels an assessment, the corrected assessment or final determination is *not* subject to further administrative review or appeal.**

2. If upon review of the taxpayer's properly filed petition for reassessment (and after a hearing if the taxpayer so requests) the tax commissioner issues a final determination, the final determination may cancel, reduce, affirm or increase the assessment. The taxpayer may appeal the tax commissioner's final determination (other than a final determination that cancels the assessment) to the Board of Tax Appeals.

**Note: The tax commissioner's final determination can increase the assessment even if the tax commissioner issues the determination outside the normal assessment statute of limitations period (three years for corporations; four years for individual income tax, pass-through entity tax and withholding tax).**

3. If upon review of the taxpayer's properly filed petition for reassessment the tax commissioner issues a corrected assessment, then (a) the corrected assessment nullifies the taxpayer's original petition, and (b) the original petition is not subject to further administrative review and may not be appealed to the Board of Tax Appeals. The tax commissioner must send the corrected assessment by ordinary mail. (Unlike the corrected assessment, the tax commissioner must send the original assessment by certified mail or must hand deliver it.)

**Note: If the tax commissioner timely issued the original assessment, then the commissioner's corrected assessment is deemed timely issued even if the corrected assessment increases the original assessment outside the normal assessment statute of limitations period.**

4. If upon review of the taxpayer's properly filed petition for reassessment the tax commissioner issues a corrected assessment, the taxpayer may file a new petition for reassessment. If the taxpayer files a new petition, the taxpayer must do so within 60 days after the commissioner mails the corrected assessment. (Unlike a new petition for reassessment, the taxpayer must file its original petition within 60 days of receipt of the original assessment. In all other respects, a franchise taxpayer must file the new petition in the same manner as provided in O.R.C. section 5733.11 for filing the original petition, and an individual income taxpayer in the same manner as provided in O.R.C. section 5747.13.)
5. If upon review of the taxpayer's properly filed petition for reassessment the tax commissioner issues a corrected assessment and the taxpayer does not file a new petition within the 60-day period described

in #4 above, then the corrected assessment becomes final. That is, the corrected assessment is not subject to further administrative review, may not be appealed to the Board of Tax Appeals, and is due and payable.

6. If upon review of the taxpayer's properly filed petition for reassessment the tax commissioner issued a corrected assessment that does not cancel the original assessment, and in response to the tax commissioner's corrected assessment the taxpayer files a new petition within the 60-day period described in #4 above, then upon review of the new petition and upon completion of the hearing (if the taxpayer requests a hearing) the commissioner must either:

- a. Issue a **final determination** that affirms, increases, decreases or cancels the first corrected assessment. The taxpayer may appeal the tax commissioner's final determination (other than a final determination that cancels the assessment) to the Board of Tax Appeals; or
- b. Issue a **second** corrected assessment that cancels the first corrected assessment in its entirety. If the commissioner cancels the first corrected assessment, the commissioner must send the cancellation by ordinary mail and the cancelled assessment is not subject to further administrative review or appeal.

**Note: The commissioner may *not* issue a second corrected assessment that reduces but does not cancel the corrected assessment, and the commissioner may *not* issue a second corrected assessment that increases the first corrected assessment.**

#### **B. Uniform Procedure if the Taxpayer Fails to File a Petition for Reassessment or if the Taxpayer Fails to File a Proper Petition for Reassessment**

The commissioner, on the commissioner's own motion, may issue a corrected franchise tax assessment. That is, the commissioner may issue a corrected assessment even if the taxpayer did not file a petition for reassessment or the taxpayer's petition is not timely or is otherwise invalid. However, this provision applies only if: (a) the assessment has not been certified to the attorney general for collection, or (b) the taxpayer has not appealed the commissioner's final determination to the Board of Tax Appeals.

If the commissioner issues a corrected assessment on the commissioner's own motion, the corrected assessment may not **increase** the tax, penalty or additional charge unless the assessment statute of limitations period is still open at the time the tax commissioner issues the corrected assessment. (Unlike a corrected assessment issued on the commissioner's own motion, a corrected assessment

issued in response to the taxpayer's petition, may increase the original assessment outside the assessment statute of limitations period (see A. 2., above)). The commissioner must send a corrected assessment issued on the commissioner's own motion by ordinary mail.

#### **C. Refunds of Amounts Paid toward an Assessment**

If (a) the tax commissioner issues a corrected assessment or final determination, (b) the corrected assessment or final determination reduces the assessment **below** the amount the taxpayer has already **paid** toward that assessment, and (c) the reduction is made as a result of the taxpayer's properly filed petition for reassessment or other written request, then the commissioner may certify any overpayment as a refund only to the extent that a refund could have been claimed at the time the party assessed made the written request. If the tax commissioner reduces an assessment on the commissioner's own motion, then the commissioner will certify any overpayment only to the extent a refund could have been claimed at the time the commissioner made the reduction.

#### **27. TAXPAYER'S BILL OF RIGHTS — REQUESTS FOR AN OPINION OF THE TAX COMMISSIONER**

The Taxpayer's Bill of Rights (Senate Bill 147, 118th General Assembly) established and amended certain administrative procedures relating to Department of Taxation audits and assessments. The law provides that at or before the commencement of an audit the Department of Taxation must provide to the taxpayer a written description of the roles of the department and the taxpayer during an audit and a statement of the taxpayer's rights.

A brochure that discusses the Department of Taxation's interpretation of this law is available on the department's Web site. In addition, this law permits the tax commissioner to issue binding opinions regarding the taxation of proposed activities of the taxpayer. As set forth in Ohio Administrative Code (Rule) 5703-1-12, a request for an opinion of the tax commissioner must comply with the following:

- Be in writing;
- Explicitly request an "Opinion of the Tax Commissioner";
- Specifically refer to O.R.C. section 5703.53;
- State all the facts of the activity or transaction for which the opinion is requested;
- Identify the parties involved in the activity or transaction about which the opinion is requested;
- Set out the specific legal questions for which the opinion is requested; and
- Be signed by an officer of the corporation authorized to act on its behalf.

For further information see Tax Commissioner Rule 5703-1-12, "Requests for an Opinion of the Tax Commissioner," available on the Department of Taxation's Web site.

## **28. SHAM TRANSACTION, ECONOMIC REALITY, SUBSTANCE OVER FORM AND STEP TRANSACTIONS**

The tax commissioner has authority to apply the doctrines of "economic reality," "sham transaction," "step transaction" and "substance over form." Generally the tax commissioner bears the burden of establishing by a preponderance of the evidence that these doctrines should apply. However, with respect to transactions between members of a controlled group, the taxpayer bears the burden of establishing that a transaction or series of transactions between members of the controlled group was not a sham transaction. **If the tax commissioner disregards a sham transaction, the assessment statute of limitations is doubled.**

For purposes of this provision the term "controlled group" means two or more persons related in such a way that one person directly or indirectly owns or controls the business operations of another member of the group. In the case of persons with stock or equity, one person owns or controls another if it directly or indirectly owns more than 50% of the other person's common stock with voting rights or other equity with voting rights. The term "sham transaction" means a transaction or series of transactions without economic substance because there is no business purpose or expectation of profit other than obtaining tax benefits. See O.R.C. sections 5733.111 and 5703.56 as enacted by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly.

**Note:** House Bill 95, 125<sup>th</sup> General Assembly law repealed the franchise tax sham transaction provision contained in O.R.C. section 5733.111 (see section 2 of the bill) and replaced it with the more encompassing provision set out above. The new law applies on or after June 26, 2003 to all taxes and fees administered by the tax commissioner to all years open to the statute of limitations.

## **29. TAX COMMISSIONER'S RIGHT TO OFFSET REFUND**

The tax commissioner may apply a taxpayer's franchise tax refund against the taxpayer's indebtedness to the State of Ohio for any tax or fee and any charge, penalty or interest arising from such a tax or fee that is administered by the tax commissioner and paid to the state or to the Clerk of Courts. In addition, the tax commissioner may apply a taxpayer's franchise tax refund in satisfaction of the corporation's indebtedness to Ohio for workers' compensation premiums, unemployment compensation contributions or unemployment compensation payments in lieu of contributions and interest on such amounts. The offset can be made only if those debts have become "final." See O.R.C. section 5733.121 as amended by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly.

## **LINE INSTRUCTIONS SCHEDULE A**

If the taxpayer is a member of a **combined** franchise report (form FT 1120C), please:

- See general instruction #23 and the instructions for form FT 1120C – Combined Report;
- Skip lines 2 through 5 of Schedule A, form FT 1120;
- Enter on line 6 of Schedule A, form FT 1120 the taxpayer's separate company apportionment ratio; and
- Enter on line 7 of Schedule A, form FT 1120 the taxpayer's apportioned income from Schedule B (Combined), line 7 of the combined report, form FT 1120C.

A taxpayer must compute its Ohio taxable income for its taxable year (see general instruction #8).

### **Line 1 – Federal taxable income.**

Enter the taxpayer's federal taxable income before net operating loss deduction and special deductions from federal form 1120, line 28 or federal form 1120A, line 24. **If the taxpayer is a member of a consolidated federal return, compute the taxpayer's federal taxable income as if the taxpayer filed a separate federal return. The Department of Taxation maintains that the federal consolidation rules do not apply in determining federal taxable income for purposes of the franchise tax.**

### **Line 6 – Ohio apportionment ratio.**

Enter the taxpayer's apportionment ratio from Schedule D, line 4 determined on a separate company basis. Enter the taxpayer's separate company apportionment ratio even if the taxpayer is a member of a combined franchise tax report.

### **Line 9 – Income (loss) from transferor corporation.**

A taxpayer-**transferee** that receives substantially all of the assets or equity of a **transferor** corporation must include in its own Ohio taxable income the transferor's Ohio taxable income **if following the transfer the transferor is not subject to the franchise tax and the transfer qualifies for nonrecognition of gain and loss under the Internal Revenue Code (I.R.C.). If the transferor statute applies to the transferee, then the transferor's Ohio net operating losses, unused credit amounts and other franchise tax attributes transfer to the transferee** subject to the limitations set forth in I.R.C. sections 381 and 382.

The Ohio taxable income of a transferor corporation is determined in the same manner as if the transfer had not been made and the transferor remained subject to the franchise tax. Thus, the federal taxable income of a transferor corporation is subject to the same adjustments and must be allocated and apportioned in the same manner as if the transferor remained subject to the franchise tax. The taxpayer-transferee must include such income in computing its tax for the same tax year or years that such income would have been reported by the transferor if the transfer had not been made and the transferor had remained subject to the



franchise tax. If the transferor was previously included in a combined report, the income of the transferor must be determined as if the transferor remained in the combined report.

If a taxpayer that is subject to O.R.C. section 5733.053 subsequently becomes a transferor, then any income that the taxpayer would have been required to add to its income under O.R.C. section 5733.053 is included in its income as a transferor and any credits or deductions that the taxpayer would have been entitled to under this section are available to the taxpayer as a transferor. See O.R.C. section 5733.053 and Sections 13(A) and 13(C) of Amended Substitute House Bill 111, effective July 1, 1989.

**Note:** Amended Substitute House Bill 94, 124<sup>th</sup> General Assembly (budget bill) limits the transferor statute provisions to those transfers and distributions which qualify for nonrecognition of gain and loss under the I.R.C.

Amended Substitute Senate Bill 287, 123<sup>rd</sup> General Assembly (Am Sub SB 287) amended both the transferor statute (O.R.C. section 5733.053) and the exit tax statute (O.R.C. section 5733.06(H)). The changes to the transferor statute and the exit tax, as enacted by Am Sub SB 287 and summarized below, were originally to have been effective with the 2002 franchise tax report (see Section 13 of Am Sub SB 287). However, Amended Substitute House Bill 94, 124<sup>th</sup> General Assembly (the Budget Bill) later amended the effective date of the changes to the transferor statute and the exit tax statute made by Am Sub SB 287. Amended Substitute House Bill 94 provides that the amendments to the exit tax and to the transferor statute made by Am Sub SB 287 do not apply to any transfer for which negotiations began before January 1, 2001, and that was commenced in and completed during calendar year 2001, unless the transferee makes an election before December 31, 2001, to apply those amendments.

The law defines the terms *transfer*, *transferor* and *transferee* as follows:

- “**Transfer**’ means a transaction or series of related transactions in which a corporation directly or indirectly transfers or distributes substantially all of its assets or equity to another corporation.” O.R.C. section 5733.053(A)(1).
- “**Transferor**’ means a corporation that has made a transfer.” O.R.C. section 5733.053(A)(2).
- “**Transferee**’ means a corporation that received substantially all the assets or equity of a transferor in a transfer.” O.R.C. section 5733.053(A)(3).

Amended Substitute Senate Bill 287 also established the following relationship between the transferor statute (O.R.C. section 5733.053) and the exit tax (see general instruction #7 and O.R.C. section 5733.06(H)):

- (1) If on January 1 following the transfer of substantially all the transferor’s assets to the transferee the transferor remains in existence, then the transferor is subject to

the franchise tax and the transferor statute does not apply to the transferee. See O.R.C. section 5733.053(B): “*The transferee shall add such income in computing its tax for the same tax year or years that such income would have been reported by the transferor if the transfer had not been made. The transferee shall add such income only to the extent the income is not required to be reported by the transferor for the purposes of the tax imposed by divisions (A) and (B) of section 5733.06 of the Revised Code.*”

- (2) If on January 1 following the transfer of substantially all the transferor’s assets to the transferee the transferor is not subject to the franchise tax (because, for example, the transferor merged into the transferee), and if for federal income tax purposes the transfer qualifies for nonrecognition of gain and loss, then the O.R.C. section 5733.053 transferor statute applies to the transferee and the exit tax does not apply to the transferor. That is, the transferee is required to add to its income the income of the transferor and the franchise tax attributes of the transferor pass to the transferee.
- (3) If on January 1 following the transfer of substantially all the transferor’s assets to the transferee the transferor is not subject to the franchise tax imposed by O.R.C. sections 5733.06(A) and (B) (for example, because, the transferor merged into the transferee), and the O.R.C. section 5733.053 transferor statute does not apply to the transferee (because, for example, the merger is not a tax-free reorganization) and if all other conditions of an exiting corporation apply, then the exit tax applies to the transferor. See O.R.C. sections 5733.06(H)(1)(d) and 5733.06(H)(6).

#### **Line 12 – Ohio net operating loss deduction.**

An Ohio net operating loss is calculated in the same manner as positive Ohio net income is calculated. That is, in determining the Ohio net operating loss generated in a particular taxable year the same adjustment, allocation and apportionment provisions apply as in determining positive Ohio taxable income (before the net operating loss deduction). Any net operating loss is applied to subsequent net income to reduce that income to zero or until the net operating loss has been fully used as a deduction.

For net operating losses incurred in taxable years ending on or after January 1, 1982 and before August 6, 1997 the designated carryover period is 15 consecutive taxable years following the taxable year in which the net operating loss occurs. For net operating losses incurred in taxable years beginning on or after August 6, 1997, the designated carryover period is 20 consecutive taxable years following the taxable year in which the net operating loss occurs. For purposes of calculating the carryforward period, the first year of the carryforward period is the taxable year following the taxable year in which the loss should have been reported.

A surviving corporation in a merger is permitted to use the Ohio net operating losses of a merged corporation provided that the surviving corporation for federal income tax purposes

is permitted to use the federal net operating losses, if any, of the merged corporation. I.R.C. sections 381 and 382 apply with respect to the allowable loss. A merged corporation has no Ohio net operating loss for a period if it is not subject to the Ohio franchise tax measured by income from that period. See *Litton Industrial Products, Inc. v. Limbach* (1991), 58 Ohio St. 3d 169 and *American Home Products Corporation, nka Wyeth, as successor in interest to A.H. Robins Company, Incorporated v. Tracy*, Court of Appeals, Tenth Appellate District, No. 02AP-759 (3-27-03). Also, see the instructions for Schedule A, line 9, Income (loss) from transferor corporation, above.

Each corporation filing as a member of a combined franchise tax group will have its own net operating loss deduction since each will compute its own Ohio taxable income on its own franchise tax report, form FT 1120.

For each year in which the taxpayer uses any portion of a net operating loss carryforward please attach to the franchise tax report a schedule which shows when the loss was generated, the amount of loss that was used in earlier years and the remaining carryforward amount. The taxpayer must maintain information regarding a net operating loss carryforward for at least four years after the later of the filing date or the due date of the report in which any portion of the carryforward is claimed.

The statute of limitations does not prohibit either the tax commissioner or the taxpayer from adjusting the net operating loss carried forward from a tax year closed to assessment to a year still open to assessment or refund. See *Consumer Direct v. Limbach* (1991), 62 Ohio St. 3d 180.

#### **Line 21 – Overpayment carryforward from 2004.**

Enter the overpayment carryforward shown on the originally filed 2004 franchise tax report which was credited to estimated tax payments for tax year 2005. **Note:** An overpayment shown on an **amended** report may not be credited toward a payment for another year. If an amended report reflects an overpayment, the taxpayer must also submit form FT REF, Application for Corporation Franchise Tax Refund, or a statement that sets forth the full and complete reason for the overpayment. See *Abitibi-Price Corporation and Subsidiaries v. Tracy*, BTA No. 98-N-401 (3-12-01), and refer to general instruction #26.

#### **Line 22 – Estimated payments made in 2005.**

Enter the estimated payments paid during tax year 2005 with form FT 1120E, Declaration of Estimated Franchise Tax; form FT 1120ER, Application for Automatic Extension; and form FT 1120EX, Request for Additional Extension.

#### **Line 23 – Refundable credits.**

**Refundable new jobs credit.** Enter the new jobs credit as provided by O.R.C. sections 5733.0610 and 122.17 and attach a copy of the certificate of verification issued by the Department of Development. The refundable new jobs credit is considered a payment made on January 1 of the tax year. The amount of the credit equals the amount of Ohio income tax the taxpayer withheld from compensation paid to “new employees” during the taxpayer’s taxable year multiplied by

the percentage specified in the taxpayer’s agreement with the Tax Credit Authority.

The term “new employee” means a full-time employee first employed by the taxpayer in the project that is the subject of the tax credit agreement after the taxpayer enters into the agreement. New employees include employees hired after the Tax Credit Authority approves the taxpayer’s project but before the taxpayer signs the tax credit agreement with the Tax Credit Authority as long as the taxpayer signs the agreement within 60 days after receiving the agreement from the Department of Development. If the authority determines that it is appropriate, a “new employee” also may include an employee rehired or called back from lay-off to work in a new facility or on a new product or service.

If a taxpayer claims the refundable new jobs credit with respect to an employee, the taxpayer may not claim the nonrefundable O.R.C. section 5709.66 enterprise zone new employee credit with respect to that same employee.

The Tax Credit Authority and the Ohio Department of Development administer this credit. Tax Credit Agreement application forms are available from the Ohio Department of Development, Economic Development Division, Office of Tax Incentives, P.O. Box 1001, Columbus, Ohio 43216-1001 or call 614-466-4551 or 1-800-848-1300. The street address for the Ohio Department of Development is 77 S. High Street, 28th floor, Columbus, Ohio 43215.

**Refundable credit for tax withheld by the Ohio Lottery Commission.** Enter the amounts that the Ohio Lottery Commission withheld from its payments to the taxpayer pursuant to O.R.C. section 5747.062(B)(2). For additional information see O.R.C. sections 3770.072(B), 5747.062(B)(2) and 5733.98(A)(27).

#### **Line 26 – Interest and Penalty.**

Enter any interest and penalty as explained in general instructions #11, #12 and #13.

#### **Lines 29 and 30 – Overpayment to be credited to year 2006 estimated tax and/or overpayment to be refunded.**

Enter the amount of overpayment to be refunded and/or to be credited against next year’s tax liability. **Note:** An overpayment shown on an **amended** report cannot be credited against the tax liability for any other year. If an amended report reflects an overpayment, the taxpayer must also submit form FT REF, Application for Corporation Franchise Tax Refund, or a statement that explains the full and complete reason for the overpayment. See *Abitibi-Price Corporation and Subsidiaries v. Tracy*, BTA No. 98-N-401 (3-12-01), and refer to general instruction #26.

### **SCHEDULE B ADJUSTMENTS TO FEDERAL TAXABLE INCOME**

**Note 1:** The “aggregate” (conduit) theory of taxation applies to the franchise tax. That is, the character of all income and deductions (and adjustments to income and deductions) realized by a partnership or other pass-through entity in which the taxpayer has a direct or indirect interest retains that



character for purposes of the franchise tax when recognized by the investor in the pass-through entity. For example, a partner's distributive share of partnership net interest income from exempt federal obligations is considered net interest income from exempt federal obligations when recognized by the partner and is therefore deductible. Furthermore, the taxpayer-partner's proportionate share of partnership property, payroll and sales must be included in the taxpayer-partner's apportionment formula. See *Mead Properties, Inc. v. Limbach*, BTA Case Nos. 85-D-791, 85-E-792, 85-C-793, 85-B-794, April 21, 1989. Effective for taxable years ending on or after September 29, 1997, Amended Substitute House Bill No. 215 (Budget Bill), 122nd General Assembly codified into the franchise tax statute the conduit theory (see O.R.C. section 5733.057).

**Note 2:** Ohio may not tax a foreign corporation's non-unitary interest income from short-term investments acquired, managed and controlled outside of Ohio. The taxpayer has the burden of showing that the income is non-unitary. See *American Home Products Corp. v. Limbach* (1990), 49 Ohio St. 3d 158.

**Note 3:** The corporation franchise tax on gains from the sale of interest bearing federal obligations is not prohibited by either section 3124, Title 31, U.S. Code or the constitutional doctrine of intergovernmental immunity. Furthermore, the franchise tax does not impermissibly discriminate against federal obligations in favor of state obligations. See *NACCO Industries, Inc. v. Tracy* (1997), 79 Ohio St. 3d 314.

**Note 4:** If the taxpayer is an electric company or a combined electric company as defined in O.R.C. section 5733.04(P) please complete supplemental Schedule B for electric companies. **The supplemental schedule and instructions are available on the Department of Taxation's Web site.** An electric company is any person engaged in the business of generating, transmitting, or distributing electricity within Ohio for use by others, but excludes a rural electric company, as defined in O.R.C. section 5727.01(C).

**Lines 1(a) and 2(b) – Valuation limitation on gains and losses from capital assets and 1231 assets.**

A corporation must add any loss and deduct any gain resulting from the sale or other disposal of a capital asset, or an asset described in section 1231 of the Internal Revenue Code, to the extent that such loss or gain occurred prior to the beginning of the first day of the taxpayer's Ohio corporation franchise tax taxable year that ended on or after December 20, 1971 on which the tax provided for in O.R.C. section 5733.06 is computed on the corporation's net income. The taxpayer has a choice of two methods in determining the amount of such prior loss or gain (valuation limitation):

- The amount of such prior gain or loss is the difference between the original cost or other basis of the asset and its fair market value as of the beginning of the first taxable year on which the tax provided for in O.R.C. section 5733.06 is computed on the corporation's net income. However, such prior period gain or loss calculated under

this method may not exceed the gain or loss reported on the federal return.

- Alternatively, the amount of such prior period gain or loss is determined by multiplying the gain or loss by a fraction, the numerator of which is the number of months from the acquisition of the asset to the beginning of the first taxable year on which the tax provided in O.R.C. section 5733.06 is computed on the corporation's net income, and the denominator of which is the number of months from the acquisition of the asset to the sale or other disposal of such asset.

Corporations that are required to make this adjustment must file form FT 1120VL, which applies only to gains and losses to which the valuation limitation applies.

**Lines 1(b) and 2(f) – Losses from the sale of Ohio public obligations; interest on public obligations and purchase obligations and gains from the sale of Ohio public obligations.**

A corporation must add any loss resulting from the disposition of public obligations to the extent such losses have been deducted in determining federal taxable income. The term "public obligation" is defined below.

A corporation may deduct interest income from both purchase obligations and public obligations to the extent such amounts are included in federal taxable income. The terms "purchase obligations" and "public obligations" are defined below.

A corporation may deduct gains from the disposition of public obligations to the extent such gains are included in federal taxable income.

For purposes of these adjustments the following definitions apply:

"Purchase obligations" means interest-bearing obligations of the State of Ohio and local public or governmental entities in the State of Ohio where these obligations require payments under installment sale, lease, lease purchase, or similar agreements.

"Public obligations" means:

- Public securities such as bonds, notes, certificates of indebtedness, and commercial paper issued by the state of Ohio and local public or governmental entities in Ohio which evidence the obligation of the state or local public or governmental entity to repay borrowed money.
- Fractionalized interests in purchase obligations, i.e. shares or participations evidencing ownership of interests in purchase obligations. Fractionalized interests in purchase obligations are separate from purchase obligations themselves and do not include interests or shares in a unit trust, investment trust, grantor trust or regulated investment company.
- Any obligation to pay interest on public securities or on fractionalized interests in purchase obligations.

Public obligations do not include purchase obligations.

“Interest” means payments that represent consideration for forbearing the collection of money, or for deferring the receipt of payment of money to a future time as determined for federal income tax purposes. Interest includes those portions of a qualified investment trust’s distributions to its shareholders or beneficial owners that are attributable to the trust’s receipt of interest or interest equivalent.

“Qualified Investment Trust” or “Trust” means a unit investment trust, grantor trust, or a regulated investment company if at all times at least 50% of the value of the total assets of the trust consists of public securities or purchase obligations, or similar obligations of other states or their local public or governmental entities.

For more specific information see O.R.C. section 5709.76.

**Line 1(c) – Amounts claimed as a credit for taxes paid by a qualifying pass-through entity.**

A corporation that claims the franchise tax credit for taxes paid by a qualifying pass-through entity in which the corporation is an investor must add to the corporation’s federal taxable income the amount claimed as a credit to the extent that the amount was deducted or excluded from the corporation’s federal taxable income. See O.R.C. section 5733.04(I)(14). For an explanation of the tax on qualifying pass-through entities see the instructions for form IT 1140, Ohio Pass Through Entity Tax Return. For an explanation of the credit for taxes paid by a qualifying pass-through entity see the line instructions for Schedule A-1, Nonrefundable credits on page 35 of these instructions.

**Lines 1(d) and 2(h) – Net loss from an “exempted investment” in a public utility and net income from an “exempted investment” in a public utility.**

A franchise taxpayer must adjust its net income or loss to the extent that the taxpayer’s income or loss would include, were it not for this law, the taxpayer’s proportionate share of such income or loss attributable to the taxpayer’s direct or indirect ownership interest in an “exempted investment.” Similarly, a taxpayer must adjust its apportionment factors and its credits to the extent that the taxpayer’s apportionment factors and credits would include, were it not for this law, the taxpayer’s proportionate share of such amounts attributable to the taxpayer’s direct or indirect ownership interest in an “exempted investment.”

An exempted investment is the taxpayer’s direct or indirect investment in a pass-through entity or a “disregarded entity” (a single member LLC that is treated as a division of its owner) which is a public utility subject to the Ohio public utility excise tax on its gross receipts.

The exempted investment adjustments apply only if the taxpayer-investor in the public utility directly or indirectly owns the investment in the public utility for the public utility’s entire taxable year ending with or within the taxpayer’s taxable year ending immediately prior to the taxpayer’s tax year. Furthermore, the adjustments apply only to the extent that

the adjustments directly relate to owning and operating a public utility in Ohio by a pass-through entity that is subject to the Ohio public utility gross receipts tax or a disregarded entity that is subject to the Ohio public utility gross receipts tax. See O.R.C. section 5733.058.

**Lines 1(e) and 2(i) – Depreciation expense adjustment from Schedule B-4 and miscellaneous federal tax adjustments.**

On line 1(e) enter the sum of (i) 5/6 of the IRC section 168(k) bonus depreciation amount deducted in determining federal taxable income for the taxable year, and (ii) 5/6 of the “qualifying section 179 depreciation expense” deducted in determining federal taxable income for the taxable year as shown on line 1 of Schedule B-4 – Bonus Depreciation and Section 179 Adjustment. “Qualifying section 179 depreciation expense” means the difference between (i) the amount of depreciation expense directly or indirectly allowed to the taxpayer under section 179 of the Internal Revenue Code, and (ii) the amount of depreciation expense directly or indirectly allowed to the taxpayer under section 179 of the Internal Revenue Code as that section existed on December 31, 2002 (see O.R.C. section 5733.04(I)(17)(a)(ii) as enacted by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly).

On line 2(i) enter the amount shown on line 10 of Schedule B-4 – Bonus Depreciation and Section 179 Adjustment.

**Caution:**

**See “Recent Legislation” in the Revision Notice at the beginning of this instruction booklet.**

**Note 1:** The **Schedule B** depreciation expense adjustment applies whether or not the depreciation expense relates to allocable income or to apportionable income. To the extent that the bonus depreciation adjustment or qualifying section 179 adjustment relates to income allocated in Schedule C, the taxpayer must also make the same adjustments in Schedule C as are made in Schedule B. See Schedule B-4 – Bonus Depreciation and Section 179 Adjustment.

**Note 2:** The depreciation add-back and deductions have **no effect on the basis** of the assets depreciated. Thus, upon the sale of an asset on which the taxpayer claimed bonus depreciation or additional 179 expense, the gain or loss for Ohio purposes will equal the gain or loss for federal purposes whether or not at the time of sale the 5/6 amount has been fully recovered. In addition, if at the time of sale the taxpayer has not fully recovered the 5/6 add-back, the taxpayer can continue to make the depreciation deduction after the sale.

**Note 3:** The depreciation adjustment applies not only to assets that the taxpayer owns but also to depreciable assets owned by the taxpayer’s disregarded entities and to depreciable assets owned by pass-through entities in which the taxpayer holds an at least 5% ownership interest.

**Note 4:** If the taxpayer is an equity investor in a pass-through entity which has claimed I.R.C. section 168(k) bonus depreciation or qualifying I.R.C. section 179 expense and if, because of the federal passive activity loss limitation rules or the at-risk limitation rules, the taxpayer is unable to fully deduct a loss passing through from the pass-through entity, then to the extent that the taxpayer does not recognize the loss the taxpayer can defer making the “5/6 add-back” until the taxable year or years for which the taxpayer deducts the pass-through entity loss and receives a federal tax benefit from the bonus depreciation or qualifying 179 amount claimed by the pass-through entity. Of course, the corporation cannot begin claiming the related deductions until the first taxable year immediately following the taxable year for which the corporation makes the 5/6 add-back.

For further information please see the following: (i) the Department of Taxation’s July, 2002 information release entitled “Recently Enacted Ohio Legislation Affects Depreciation Deductions for Taxable Years Ending in 2001 and Thereafter”; (ii) the department’s November 2002 information release entitled “Ohio Bonus Depreciation Adjustment and the Internal Revenue Code’s Passive Activity Loss, Basis Limitation and At-Risk Rules”; (iii) O.R.C. section 5733.04(I)(17) and (18); and (iv) section 4 of Amended Substitute Senate Bill 261, 124<sup>th</sup>, General Assembly.

**Line 2(c) – Dividends received.**

Enter the sum of the following: (1) the dividend deduction provided by I.R.C. section 243, and (2) to the extent not otherwise allowed by the I.R.C. section 243 dividends received deduction: (a) dividends received from an insurance company if the taxpayer owns at least 80% of the outstanding common stock of the insurance company and (b) dividends received from a public utility, except an electric company, if the taxpayer owns at least 80% of the outstanding common stock of the public utility. See O.R.C. section 5733.04(I)(4), (I)(7) and (I)(8).

**Line 2(d) – Adjustment for targeted jobs tax credit or work opportunity tax credit.**

Deduct the wage and salary expense not otherwise deducted for federal tax purposes because of the targeted jobs tax credit and/or the work opportunity tax credit. See O.R.C. section 5733.04(I)(10).

**Line 2(e) – Net interest income from exempt U.S. obligations.**

Deduct net interest on obligations of the United States and its territories and possessions or of any authority, commission or instrumentality of the United States. “Net federal interest” is defined as federal interest less any expenses taken on the federal tax return that would not have been allowed under I.R.C. section 265 if such interest were exempt from federal income tax. See O.R.C. section 5733.04(I)(11).

A January 9, 1992 Ohio Department of Taxation information release lists federal obligations, the interest from which is deductible. The information release is available on the department’s Web site. Generally interest income generated from repurchase agreements secured by federal obligations

is not interest from federal obligations and therefore is not deductible. See *Nebraska Department of Revenue v. Lowenstein*, 513 U.S. 123 (1994), 115 S. Ct. 557, 1994 US Lexis 8802. Also see *Associated Estates Corp., AEC Management Co. and Hirsch Electric Co. v. Limbach*, BTA Case Nos. 87-H-743, 87-G-774 and 87-D-756, May 11, 1990.

**Line 2(g) – Contributions to an individual development account program.**

Deduct the amount that the taxpayer contributed during the taxable year to an individual development account program established by a county Department of Human Services pursuant to O.R.C. sections 329.11 to 329.14 for the purpose of matching funds deposited by program participants. See O.R.C. section 5733.04(I)(15). The individual development account program applies to low-income residents of a county who enter an agreement with the fiduciary organization selected to administer the program. Program participants must abide by the terms and conditions of the agreement and may use money in an individual development account only with the approval of the fiduciary organization.

**SCHEDULE B-2  
FOREIGN SOURCE INCOME DEDUCTION  
O.R.C. SECTION 5733.04(I)(2)**

**Deductible foreign source income other than dividends, I.R.C. section 78 income and I.R.C. section 951 subpart F income must generally be reduced by certain percentages (set out below) which are deemed to be the expenses attributable to the foreign income.** However, to the extent that the taxpayer shows by clear and convincing evidence a lesser amount of actual expenses attributable to deductible gross foreign source income, the taxpayer may deduct a greater amount. To the extent that the tax commissioner shows by clear and convincing evidence more actual expenses attributable to deductible foreign source income, the tax commissioner may reduce the deduction.

**Line 1 – I.R.C. Section 78 and 951 Income.**

Enter the I.R.C. section 78 foreign dividend gross-up and I.R.C. section 951 subpart F income. This income is fully deductible.

**Line 2 – Foreign dividends.**

Enter dividends received from a subsidiary, associate or affiliated corporation that neither transacts any substantial portion of its business nor regularly maintains any substantial portion of its assets within the United States. This income is fully deductible. See *Emerson Elec. Co. v. Tracy* (2000), 90 Ohio St.3d 157 and O.R.C. section 5733.04(I)(2) as amended by Amended Substitute Senate Bill 261, 124<sup>th</sup> General Assembly.

**Line 3 – Foreign royalties.**

Multiply by 90% the royalties received from sources outside the United States. Royalties are received from sources outside the United States to the extent that the property that generated the royalty was used outside the United States.

**Line 4(a) – Income from technical and other services.**

Enter amounts received for mechanical, industrial, scientific,



practical and other services performed outside the United States. Income from technical services performed in the United States for a foreign customer does not qualify for the foreign source income deduction. The situs of the service performed determines the source of service income. See *Rio Indal, Inc. v. Lindley* (1980), 62 Ohio St. 2d 283. If technical service on a project is performed both within and without the United States, income from the project must be reasonably allocated within and without the United States.

**Line 4(b) – Reimbursed expenses for personal services performed for subsidiaries.**

Enter the amount of any reimbursed expenses for technical or other services performed by employees of the taxpayer for its subsidiary, associate, or affiliated corporations.

To the extent that the taxpayer shows by clear and convincing evidence a lesser amount of actual expenses attributable to deductible gross foreign source income, the taxpayer may deduct a greater amount. To the extent that the tax commissioner shows by clear and convincing evidence more actual expenses attributable to deductible foreign source income, the tax commissioner may reduce the deduction.

**The instructions for Schedule B-3 – RELATED ENTITY AND RELATED MEMBER ADJUSTMENTS begin on page 42 of this booklet.**

**The instructions for Schedule B-4 – BONUS DEPRECIATION AND SECTION 179 ADJUSTMENT are included on that schedule.**

**SCHEDULE C  
ALLOCABLE INCOME  
O.R.C. SECTION 5733.051**

**Caution: For taxable years ending on or after June 26, 2003, Ohio franchise tax law distinguishes business income from nonbusiness income and with the exception of the bonus depreciation deduction (see Schedule B-4 and line 1, below) only nonbusiness income is allocated. Furthermore, for taxable years ending on or after June 26, 2003, all income, gain, loss and expense is presumed to be apportionable business income. A taxpayer reporting any allocable income (other than amounts from Schedule B-4, lines 15 and 17) must attach to the report (i) a detailed statement setting forth support that rebuts the presumption, (ii) a list of the states for which the taxpayer treats the income as business income and (iii) the reasons for such treatment in the other state(s).**

- **“Business income** means income arising from transactions, activities, and sources in the regular course of a trade or business and includes income from real property, tangible personal property, and intangible personal property if the acquisition, rental, management, and disposition of the property constitute integral parts of the regular course of a trade or business operation. ‘Business income’ includes income, including gain or loss, from a partial or complete liquidation of a business, including, but not limited to,

gain or loss from the sale or other disposition of goodwill.” See O.R.C. section 5733.04(Q) as enacted by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly.

- **“Nonbusiness income** means all income other than business income.” See O.R.C. section 5733.04(R) as enacted by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly.

**Note 1:** The “aggregate” (conduit) theory of taxation applies to the franchise tax. That is, the character of all income and deductions (and adjustments to income and deductions) realized by a pass-through entity retains that character for purposes of the franchise tax when recognized by the investor in the pass-through entity. For example, a partner’s distributive share of partnership net rental income is considered rental income when recognized by the partner. See O.R.C. section 5733.057 and *Mead Properties, Inc. v. Limbach*, BTA Case Nos. 85-D-791, 85-E-792, 85-C-793, 85-B-794, April 21, 1989.

**Note 2:** If the taxpayer is an electric company or a combined electric company, as those terms are defined in O.R.C. section 5733.04(P), please complete supplemental Schedule C for Electric Companies. An “electric company” is any person engaged in the business of generating, transmitting, or distributing electricity within Ohio for use by others. However, the term “electric company” as used in O.R.C. chapter 5733 does not include a “rural electric company”, as defined in O.R.C. section 5727.01(C). See O.R.C. section 5733.04(P).

**Line 1 – Bonus depreciation adjustment.**

In the Ohio column enter the amount from Schedule B-4, line 15. In the everywhere column enter the amount from Schedule B-4, line 17. The instructions for Schedule B-4 are on that schedule.

**Note:** To the extent that the bonus depreciation and qualifying section 179 add-back and deduction adjustments made in Schedule B relate to nonbusiness income allocated within or without Ohio, the taxpayer must make the same adjustments in Schedule C (see O.R.C. sections 5733.04(I)(17)(c) and (I)(18)(b)).

If on the 2002, 2003 and/or 2004 franchise tax report the taxpayer made a 5/6 bonus depreciation add-back and allocated that add-back to Ohio in Schedule C (because, for example, the depreciation add-back was attributed to property that generated rental income which the taxpayer allocated to Ohio), then in the five years following the add back years the taxpayer is entitled to allocate to Ohio the bonus depreciation deductions related to the 2002, 2003 and 2004 add-backs on that same equipment. This is so, even if that same rental property generates apportionable business income on the 2005 report.

Similarly, if on the 2002, 2003 and/or 2004 franchise tax report the taxpayer made a 5/6 bonus depreciation add-back and allocated that add-back outside Ohio in Schedule C (because, for example, the depreciation add-back was attributed to property that generated rental income which the taxpayer



allocated outside Ohio), then in the five years following the add back years the taxpayer is required to allocate outside Ohio the bonus depreciation deductions related to the 2002, 2003 and 2004 add-backs on that same equipment. This is so, even if that same rental property generates apportionable business income on the 2005 report.

**Line 2 – Nonbusiness income.** Allocate within and without Ohio the sum of the following amounts when nonbusiness income.

(A) **Nonbusiness net rents.** Nonbusiness net rents from real property located in Ohio are allocable to Ohio. Nonbusiness net rents from tangible personal property are allocable to Ohio to the extent such property is utilized in Ohio.

(B) **Nonbusiness net royalties.** Nonbusiness net royalties from real property located in Ohio are allocable to Ohio. Nonbusiness net royalties from tangible personal property are allocable to Ohio to the extent such property is utilized in Ohio.

(C) **Nonbusiness capital gains and losses and depreciation recapture.** Nonbusiness capital gains and losses and 1231 gains and losses from the sale or other disposition of real property located in Ohio are allocable to Ohio.

Nonbusiness capital gains and losses and 1231 gains and losses from the sale or other disposition of tangible personal property are allocable to Ohio to the extent the property was used in Ohio prior to the sale.

Gains from the sale or other disposition of depreciable real property and depreciable tangible personal property, taxed as ordinary (recapture) income for federal income tax purposes, are considered capital gains and capital losses for purposes of allocation. See *Borden, Inc. v. Limbach* (1990), 49 Ohio St. 3d 240. Upon the sale of a depreciable asset, the amount of recapture income allocable to Ohio is not limited to the accumulated depreciation expense (on the asset sold) that the taxpayer had apportioned to Ohio in previous years because the statute contains no overt language which would serve to limit depreciation recapture in such a manner. See *Harsco Corp. v. Tracy* (1999), 85 Ohio St.3d 382.

Nonbusiness capital gains and losses from the sale or other disposition of intangible property which may produce dividend income are allocated on the same basis as set forth in the section below dealing with dividends but substituting *the day of the sale or disposition* for *the day on which the payor pays the dividend or makes the distribution*. However, if the location of the physical assets described in the section below addressing dividends is not available to the taxpayer, such gains and losses are apportionable. Nonbusiness capital gains and capital losses from the sale or other disposition of all other intangible personal property are apportioned.

(D) **Nonbusiness dividends (not otherwise deducted and not apportionable).**

As used below, the term *payor's year* means the payor's fiscal or calendar year ending immediately before or when the payor pays the dividend or makes the distribution. For taxable years ending on or after June 26, 2003, nonbusiness dividends, other than dividends or distributions from a domestic international sales corporation, are allocated to Ohio by multiplying the dividend by a fraction. The denominator of the fraction is the sum of the amounts determined in #1 and #2 below:

1. The book value of the dividend payor's physical assets everywhere at the end of the *payor's year*. So, if the payor makes a dividend payment on any date other than its year end, then the payor's physical assets are determined as of the last day of the payor's year that ended before it made payment, and if the payor makes payment on the last day of the payor's year, the payor's physical assets are determined on the payment date (rather than the last day of the payor's year that ended before it made payment).

a. If on the last day of the payor's year the payor or any member(s) of the qualifying controlled group of which the payor is a member, separately or cumulatively own, directly or indirectly, more than 50% of the equity of a pass-through entity, then the payor is deemed to own its proportionate share of the physical assets that the pass-through entity directly or indirectly owns. The book value of the pass-through entity's physical assets is determined on the last day of the pass-through entity's fiscal or calendar year ending with or within the payor's year.

b. The statute and these instructions refer to a pass-through entity that owns an interest in another pass-through entity as an upper-level pass-through entity, and to the upper-level pass-through entity's investee as the lower level pass-through entity. For purposes of #1 and #1(a.), if an upper-level pass-through entity, a portion of whose physical assets the payor's subsidiary is deemed to own as set out in 1(a.) above, owns an interest in a lower-level pass-through entity on the last day of the upper level pass through entity's fiscal or calendar year ending with or within the payor's year, then the upper-level pass-through entity is deemed to own its proportionate share of the physical assets of the lower level pass-through entity on the last day of the lower level pass-through entity's fiscal or calendar year ending within or with the last day of the upper level pass-through entity's fiscal or calendar year ending with or within the payor's year.

However, if on each day of the upper-level pass-through entity's fiscal or calendar year in which or with which ends the fiscal or calendar year of the lower-level pass-through entity the upper-level

pass-through entity directly and indirectly owns less than 50% of the equity of the lower-level pass-through entity and if, based upon clear and convincing evidence, complete information about the location and cost of the physical assets of the lower-level pass-through entity is not available to the upper-level pass-through entity, then for purposes of #1 and #1(a.), the upper level pass-through entity is deemed as owning no equity of the lower-level pass-through entity for each day during the upper-level pass-through entity's calendar or fiscal year in which or with which ends the lower level pass-through entity's fiscal or calendar year.

2. The book value of the physical assets of each corporation more than 50% of whose capital stock with voting rights the dividend payor directly or indirectly owns on the last day of the payor's year (whether or not those corporations are taxpayers and whether or not those corporations are included in a combined Ohio franchise tax report with the payor). These instructions refer to a corporation more than 50% of whose capital stock with voting rights the dividend payor directly or indirectly owns on the last day of the payor's year as the payor's subsidiaries; the statute refers to the payor along with its direct and indirect subsidiaries as a "modified qualifying controlled group." The book value of each such subsidiary's physical assets is determined on the last day of the subsidiary's calendar year or fiscal year ending with or within the payor's year.

a. For purposes of #2, if on the last day of the payor's year the payor or any member(s) of the qualifying controlled group of which the payor is a member, separately or cumulatively own, directly or indirectly, more than 50% of the equity of a pass-through entity, then in determining the book value of physical assets, each subsidiary of the payor is deemed to own its proportionate share of the physical assets that the pass-through entity directly or indirectly owns. The book value of the pass-through entity's physical assets is determined on the last day of the pass through entity's fiscal or calendar year ending with or within the payor's year.

b. For purposes of #2 and #2(a.), if an upper-level pass-through entity, a portion of whose physical assets the payor's subsidiary is deemed to own as set out in #2(a.) above, owns an interest in a lower-level pass-through entity on the last day of the upper level pass-through entity's fiscal or calendar year ending with or within the payor's year, then the upper-level pass-through entity is deemed to own its proportionate share of the physical assets of the lower level pass-through entity on the last day of the lower level pass-through entity's fiscal or calendar year ending within or with the last day of the upper level pass-through entity's fiscal or calendar year ending with or within the payor's year.

However, if on each day of the upper-level pass-through entity's fiscal or calendar year in which or with which ends the fiscal or calendar year of the lower-level pass-through entity the upper-level pass-through entity directly and indirectly owns less than 50% of the equity of the lower-level pass-through entity and if, based upon clear and convincing evidence, complete information about the location and cost of the physical assets of the lower-level pass-through entity is not available to the upper-level pass-through entity, then for purposes of #2 and #2(a.), the upper level pass-through entity is deemed as owning no equity of the lower-level pass-through entity for each day during the upper-level pass-through entity's calendar or fiscal year in which or with which ends the lower level pass-through entity's fiscal or calendar year.

The numerator of the fraction is the sum of the within Ohio book value amounts determined in the same manner.

**Note: If the book values of physical assets necessary to determine the within Ohio to total everywhere fraction are not "available" to the taxpayer, then the nonbusiness dividends and the nonbusiness capital gains and losses from the sale or other disposition of dividend producing property described above are apportionable. The term "available," as used here, means information is such that a person is able to learn of the information by the due date plus extensions, if any, for filing the report for the tax year immediately following the last day of the taxable year.**

**(E) Nonbusiness net patent and copyright royalties and technical assistance fees.**

Nonbusiness net technical assistance fees along with nonbusiness net rents and royalties from intangible property are allocable to Ohio to the extent that the activity of the payor thereof giving rise to the payment takes place in Ohio.

A "technical assistance fee" is defined as "payment for mechanical, industrial, scientific or practical aid, expertise or services." See *Holiday Inns, Inc. v. Limbach* (1990), 48 Ohio St. 3d 34 and *Stanley Steamer International, Inc., v. Tracy*, BTA Case No. 91-K-1650, August 20, 1993.

**(F) Nonbusiness state lottery income.**

The following amounts are allocable to Ohio when that income is nonbusiness income: (i) amounts paid by the Ohio Lottery Commission to a prize winner, and (ii) a *transferee's* "earnings, profit, income and gain from the sale, exchange or other disposition of lottery prize awards" earned as a result of a *transfer* from a transferor/ winner the right to receive the future installments of an Ohio lottery prize.

A “transfer” means any form of sale, assignment, or redirection of payment of all or any part of a lottery prize award for consideration” (O.R.C. section 3770.10(E)). A transfer agreement between the “transferor” (the prize winner) and the “transferee” (the purchaser of the winner’s right to future lottery payments) must contain a statement signed by the transferee irrevocably agreeing that the transferee corporation is subject to the franchise tax with respect to gain or income which the transferee will recognize as a result of the transfer. A transferee having no nexus with Ohio other than as a party to the transfer agreement is subject to the franchise tax on the income that the transferee will recognize as a result of the transfer even if the transferee is exempt from franchise tax under O.R.C. section 5733.09 and even if the transferee is otherwise exempt from the net income base. The Ohio Lottery Commission is required to withhold 3.5% from the amounts that it pays to the transferee and such withholding may be claimed as a refundable credit on the transferee’s franchise tax report. See O.R.C. sections 3770.072(B), 5747.062(B)(2) and 5733.98(A)(27).

- (G) **Other nonbusiness income.** Allocate entirely to Ohio all nonbusiness income from sources other than those listed in A through F except to the extent the allocation of any such item of net nonbusiness income entirely to Ohio is not within the taxing power of this state under the Constitution of the United States. To the extent such allocation entirely to Ohio is not within the taxing power of this state under the Constitution of the United States, any such items of nonbusiness income are apportionable.

### **SCHEDULES D and D-2 APPORTIONMENT RATIO O.R.C. SECTION 5733.05(B)(2)**

**Schedules D and D-2 apply as follows:**

- **Schedule D** applies in apportioning **net income**.
- **Schedule D** applies in apportioning **net worth if the taxpayer does not have nonbusiness income**.
- **Schedule D-2** applies in apportioning **net worth** only if **the taxpayer has nonbusiness income**.

**Net income apportionment.** For taxable years ending on or after June 26, 2003, Ohio franchise tax law distinguishes business income from nonbusiness income and **the net income base property, payroll and sales factors specifically exclude that portion of property, payroll and sales to the extent that the portion relates to, or is used in connection with, the production of nonbusiness income allocable under O.R.C. section 5733.051.** For example, for taxable years ending on or after June 26, 2003, real property that generates allocable nonbusiness rental income is excluded from the numerator and the denominator of the net income base property factor. See O.R.C. section 5733.05(B)(2) as amended by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly. **In apportioning net income**

**for taxable years ending before June 26, 2003, prior law and case law apply.**

**Net worth base apportionment.** For taxable years ending on or after June 26, 2003, the net worth base property, payroll and sales factors specifically include that nonbusiness property, payroll and sales excluded from the net income base factors under the above paragraph. If the taxpayer had nonbusiness income, then in apportioning net worth for taxable years ending on or after June 26, 2003 see the following: Schedule D-2, the instructions for Schedule D-2 (beginning on page 32 of this booklet), and O.R.C. section 5733.05(C)(2) as amended by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly.

**In apportioning net worth for taxable years ending on or after June 26, 2003, use the net income apportionment ratio without adjustment if the taxpayer does not have nonbusiness income. Complete the form FT 1120 Schedule D apportionment ratio on a separate company basis. The separate company apportionment ratio applies to the net worth base even if the taxpayer is a member of a combined report, form FT 1120C. See O.R.C. section 5733.05(D)(3) which states that the taxpayer’s net worth is multiplied by the net income base apportionment formula computed “. . . without regard to section 5733.052 of the Revised Code.” The taxpayer’s apportionment ratio on the combined report (Schedule D – Combined) applies only to the net income base, not to the net worth base.**

**Note 1: The “aggregate” (conduit) theory of taxation applies to the franchise tax.** That is, the character of all income and deductions (and adjustments to income and deductions) realized by a pass-through entity retains that character when recognized by the investor in the pass-through entity. Furthermore, the investor’s proportionate share of the pass-through entity’s property, payroll and sales must be included in the investor’s apportionment formula. See O.R.C. section 5733.057 and *Mead Properties, Inc. v. Limbach*, BTA Case Nos. 85-D-791, 85-E-792, 85-C-793, 85-B-794, April 21, 1989.

**Note 2:** A taxpayer must adjust its net income (or loss), its apportionment factors and its credits to the extent that the taxpayer’s income (loss), apportionment factors and credits would include, were it not for this law, the taxpayer’s proportionate share of such amounts attributable to the taxpayer’s direct or indirect ownership interest in an “exempted investment.” An exempted investment is the taxpayer’s direct or indirect investment in a pass-through entity or a “disregarded entity” (a single member LLC that is treated as a division of its owner) which is a public utility subject to the Ohio public utility excise tax on its gross receipts (see O.R.C. section 5733.058).

**Note 3: Deviation from standard allocation and apportionment.** A taxpayer may request deviation from the statutory allocation and apportionment provisions on an original report, on an amended report filed within the statute of limitations, or on a timely-filed petition for reassessment.



The request for deviation must be in writing. An alternative method will be effective only with approval by the tax commissioner. See O.R.C. section 5733.05(B)(2)(d).

**Note 4: Factors weighted.** The apportionment ratio's property, payroll, and sales factors are weighted 20%, 20% and 60%, respectively. The 20%, 20%, 60% weighting does not apply to financial institutions. See O.R.C. section 5733.05(B)(2).

**Note 5:** The term “**qualified research**” as used below in the property and payroll factors means laboratory research, experimental research and other similar types of research; research in developing or improving a product; or research in developing or improving the means of producing a product. Qualified research does not include market research, historical research, literary research, consumer surveys, efficiency surveys, management studies and ordinary testing or inspection of materials and products for quality control. “Product” as used in this paragraph does not include services or intangible property.

**Note 6:** If the taxpayer is an electric company or combined electric company, see the “supplemental franchise tax schedules and instructions for electric companies and combined electric companies available on the Department of Taxation’s Web site. Sales of electricity and sales of electricity transmission and distribution services are situated in accordance with O.R.C. section 5733.059.

#### **Schedule D Property Factor**

The property factor is a fraction the numerator of which is the average value of the corporation’s includable real and tangible personal property owned or rented, and used in the trade or business in this state during the taxable year, and the denominator of which is the average value of all the corporation’s includable real and tangible personal property owned or rented, and used in the trade or business everywhere during such year.

For taxable years ending on or after June 26, 2003, Ohio franchise tax law distinguishes business income from nonbusiness income. In addition, for taxable years ending on or after June 26, 2003, the property factor specifically **includes** real property and tangible personal property that the corporation rents, subrents, leases or subleases to others if the income or loss from such rentals, subrentals, leases or subleases is business income. Furthermore, for taxable years ending on or after June 26, 2003, Ohio franchise tax law specifically excludes from the factor property relating to, or used in connection with, the production of nonbusiness income allocated under O.R.C. section 5733.051.

**Property owned by the corporation is valued at its original cost average value. Average value is determined by adding the cost values at the beginning and at the end of the taxable year and dividing the total by two. The tax commissioner may require the use of monthly values during the taxable year if such values more reasonably reflect the average value of the corporation’s property.**

In determining average value do not include in either column 1 (within Ohio) or in column 2 (total everywhere) the following:

- Construction in progress.
- Property relating to, or used in connection with, the production of nonbusiness income allocable under O.R.C. section 5733.051. See O.R.C. section 5733.05(B)(2) as amended by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly, applicable to taxable years ending on or after June 26, 2003.
- The original cost of property within Ohio with respect to which the state of Ohio has issued an Air Pollution, Noise Pollution or an Industrial Water Pollution Control Certificate. See O.R.C. section 5733.05(B)(2)(a).
- The original cost of real property and tangible property (or in the case of property that the corporation is renting from others, eight times its net annual rental rate) within Ohio that is used exclusively during the taxable year for qualified research.

Do not include in column 1 but do include in column 2 the original cost of qualifying improvements to land or tangible personal property in an enterprise zone for which the taxpayer holds a Tax Incentive Qualification Certificate issued by the Department of Development. See general instruction #24.

#### **Line 1(a), column 1 – Owned property within Ohio.**

Enter the average value of the corporation’s real property and tangible personal property, including leasehold improvements, owned and used in the trade or business in Ohio during the taxable year.

#### **Line 1(a), column 2 – Owned property - total everywhere.**

Enter the average value of all the corporation’s real property and tangible personal property, including leasehold improvements, owned and used in the trade or business everywhere during the taxable year.

#### **Line 1(b) – Rented property.**

Enter the value of the corporation’s real property and tangible personal property rented and used in the trade or business in Ohio (column 1) and everywhere (column 2) during the taxable year. Property rented by the corporation is valued at eight times the annual rental rate (annual rental expense less subrental receipts).

#### **Line 1(c) – Total Property Within Ohio and Everywhere.**

Add lines 1(a) and 1(b) for column 1, (within Ohio) and column 2 (total everywhere).

#### **Line 1(c), column 3 – Property ratio.**

Enter the ratio of property within Ohio to total everywhere by dividing column 1 by column 2.

#### **Line 1(c), column 5 – Weighted property ratio.**

Multiply the property ratio on line 1(c), column 3 by the property factor weighting of 20%.



## Schedule D Payroll Factor

The payroll factor is a fraction, the numerator of which is the total amount paid in this state during the taxable year by the taxpayer for compensation, and the denominator of which is the total compensation paid both within and without this state during the taxable year. As used below, the term “compensation” means any form of remuneration paid to an employee for personal services. Do not include in column 1 (within Ohio) or in column 2 (total everywhere) the following:

- Compensation paid in Ohio to employees who are primarily engaged in qualified research.
- **Compensation paid to employees to the extent that the compensation relates to the production of nonbusiness income allocable under O.R.C section 5733.051. See O.R.C. section 5733.05(B)(2) as amended by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly, applicable to taxable years ending on or after June 26, 2003.**

Do not include in column 1 but do include in column 2 compensation paid in Ohio to certain specified new employees at an urban job and enterprise zone facility for which the taxpayer has received a Tax Incentive Qualification Certificate issued by the Department of Development (see general instruction #24).

### Line 2, column 1 – Payroll within Ohio.

Enter the total amount of the corporation’s compensation paid in Ohio during the taxable year. Compensation is paid in Ohio if any of the following apply:

- The recipient’s service is performed entirely within Ohio; or
- The recipient’s service is performed both within and without Ohio, but the service performed without Ohio is incidental to the recipient’s service within Ohio; or
- Some of the recipient’s service is performed within Ohio and either the recipient’s base of operations, or if there is no base of operations, the place from which the recipient’s service is directed or controlled is within Ohio, or the base of operations or the place from which the service is directed or controlled is not in any state in which some part of the service is performed, but the recipient’s residence is in Ohio.

Compensation is paid in Ohio to any employee of a common or contract motor carrier corporation who performs his regularly assigned duties on a motor vehicle in more than one state in the same ratio by which the mileage traveled by such employee within Ohio bears to the total mileage traveled by such employee everywhere during the taxable year. The statutorily required mileage ratio applies only to contract or common carriers. Thus, without approval by the tax commissioner a manufacturer or merchant who operates its own fleet of delivery trucks may not situs driver payroll based upon the ratio of miles traveled in Ohio to miles traveled everywhere. See *Cooper Tire and Rubber Co. v. Limbach* (1994), 70 Ohio St. 3d 347.

### Line 2, column 2 – Payroll total everywhere.

Enter the total amount of the corporation’s compensation paid everywhere during the taxable year.

### Line 2, column 3 – Payroll ratio.

Enter the ratio of payroll within Ohio to total everywhere by dividing column 1 by column 2.

### Line 2, column 5 – Weighted payroll ratio.

Multiply the property ratio on line 2, column 3 by the payroll factor weighting of 20%.

## Schedule D Sales Factor

The sales factor is a fraction whose numerator is the taxpayer’s includable business income receipts in Ohio during the taxable year and whose denominator is the sum of the taxpayer’s within Ohio and without Ohio includable business income receipts during the taxable year. **The sales factor specifically excludes receipts attributable to nonbusiness income allocable under O.R.C section 5733.051** (see O.R.C. section 5733.05(B)(2) as amended by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly and the tax commissioner’s April 2004 information release entitled “Sales Factor Situsing Revisions”).

The following receipts are not includable in either the numerator or the denominator of the sales factor even if the receipts arise from transactions, activities and sources in the regular course of a trade or business (see O.R.C. section 5733.05(B)(2)(c) as amended by Substitute House Bill 127, 125<sup>th</sup> General Assembly):

- Interest or similar amounts received for the use of, or for the forbearance of the use of, money;
- Dividends;
- Receipts along with any related gains or losses from the sale or other disposal of intangible property other than trademarks, trade names, patents, copyrights and similar intellectual property;
- Receipts along with any related gains and losses from the sale or other disposal of tangible personal property or real property where that property is a capital asset or an asset described in I.R.C. section 1231. For purposes of this provision the determination of whether or not an asset is a capital asset or a 1231 asset is made without regard to the holding period specified in the I.R.C.; and
- Receipts from sales to: (a) an at-least 80% owned public utility other than an electric company, combined electric company, or telephone company, (b) an at-least 80% owned insurance company, or (c) an at-least 25% owned financial institution.

**Note:** Income from receipts excluded from the sales factor is not presumed to be nonbusiness income. For taxable years ending on or after June 26, 2003, all income, gain, loss and expense is presumed to be apportionable business income – even if the related receipts are excluded from the sales factor. A taxpayer reporting any allocable income (other than

amounts from Schedule B-4, lines 12 and 14) must attach to the report (i) a detailed statement setting forth support which rebuts the presumption, (ii) a list of the states for which the taxpayer treats the income as business income, and (iii) the reasons for such treatment in the other state(s).

For taxable years ending on or after December 11, 2003, the law specifically **includes** in the sales factor the following amounts when arising from transactions, activities and sources in the regular course of a trade or business: (1) receipts from sales of tangible personal property, (2) receipts from the sale of real property inventory (such as lots developed and sold by a real estate developer), (3) rents and royalties from tangible personal property, (4) rents and royalties from real property, (5) receipts from the sale, exchange, disposition, or other grant of the right to use trademarks, trade names, patents, copyrights and similar intellectual property, (6) receipt from the sale of services and other receipts not expressly excluded from the factor. These amounts are situsable to Ohio as set out below.

### **Line 3, column 1 – Sales within Ohio.**

Enter the total of gross receipts from sales not excludable from the numerator and the denominator of the sales factor, to the extent the includable gross receipts reflect business done in Ohio. Sales within Ohio include the following:

- **Receipts from sales of tangible personal property, less returns and allowances, received by the purchaser in Ohio.** In the case of delivery of tangible personal property by common carrier or by other means of transportation, the place at which such property is ultimately received after all transportation has been completed is considered as the place at which such property is received by the purchaser. Direct delivery in Ohio, other than for purposes of transportation, to a person or firm designated by a purchaser constitutes delivery to the purchaser in Ohio, and direct delivery outside Ohio to a person or firm designated by a purchaser does not constitute delivery to the purchaser in Ohio, regardless of where title passes or other conditions of sale. Customer pick-up sales are situsable to the final destination after all transportation (including customer transportation) has been completed. See *Dupps Co. v. Lindley* (1980), 62 Ohio St. 2d 305.
- Revenue from servicing, processing, or modifying tangible personal property is situsable to the destination state as a sale of tangible personal property. See *Custom Deco, Inc. v. Limbach*, BTA Case No. 86-C-1024, June 2, 1989.
- **Receipts from sales of real property inventory in Ohio.**
- **Rents and royalties from tangible personal property to the extent the property was used in Ohio.**
- **Rents and royalties from real property located in Ohio.**
- **Receipts from the sale, exchange, disposition, or other grant of the right to use trademarks, trade names, patents, copyrights and similar intellectual property are situsable to Ohio to the extent that the receipts are based on the amount of use of that property in Ohio.**

If the receipts are not based on the amount of use of that property, but rather on the right to use the property and the payor has the right to use the property in Ohio, then the receipts from the sale, exchange, disposition, or other grant of the right to use such property are situsable to Ohio to the extent the receipts are based on the right to use the property in Ohio.

- **Receipts from the performance of services and receipts from any other sales not excluded from the sales factor** and not otherwise situsable within or without Ohio under the above situs provisions are situsable to Ohio in the proportion to the purchaser's benefit, with respect to the sale, in Ohio to the purchaser's benefit, with respect to the sale, everywhere. The physical location where the purchaser ultimately uses or receives the benefit of what was purchased is paramount in determining the proportion of the benefit in Ohio to the benefit everywhere. **For taxable years ending on or after December 11, 2003, the "cost of performance" provision is no longer the law.**

### **Line 3, column 2 – Sales everywhere.**

Enter the total of such includable gross receipts, less returns and allowances, from sales everywhere.

### **Line 3, column 3 – Sales ratio.**

Enter the ratio of sales within Ohio to total everywhere by dividing column 1 by column 2.

### **Line 3, column 5 – Weighted sales ratio.**

Multiply the sales ratio on line 3, column 3 by the sales factor weighting of 60%.

## **SCHEDULE D-2 NET WORTH BASE APPORTIONMENT FORMULA O.R.C. SECTION 5733.05(C)(2)**

**Schedule D-2 applies in apportioning net worth only if the taxpayer had nonbusiness income.**

**Net worth base apportionment.** For taxable years ending on or after June 26, 2003 for purposes of net worth apportionment, the numerator and the denominator of the net income base property, payroll and sales factors must be adjusted to include the portion of any real property and tangible personal property, payroll and sales, respectively, relating to, or used in connection with, the production of nonbusiness income allocated under O.R.C. section 5733.051. That is, for purposes of net worth apportionment the net income base factors must be adjusted to include that property, payroll and sales relating to nonbusiness income which property, payroll and sales have been excluded from the net income basis factors. See O.R.C. section 5733.05(C)(2) as amended by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly.

Example: Real property that generates nonbusiness rental income allocated to Ohio is excluded from the numerator and the denominator of the Schedule D net income base property factor, but for net worth base apportionment the property factor must be adjusted to include such property.

Furthermore, rental receipts from real property that generates nonbusiness rental income allocated to Ohio is excluded from the numerator and the denominator of the Schedule D net income base sales factor, but for net worth base apportionment the sales factor must be adjusted to include such rental receipts.

**Note: Complete the form FT 1120 Schedule D-2 apportionment ratio on a separate company basis. The separate company apportionment ratio applies to the net worth base even if the taxpayer is a member of a combined report, form FT 1120C. See O.R.C. section 5733.05(D)(3), which states that the taxpayer's net worth is multiplied by the net income base apportionment formula computed ". . . without regard to section 5733.052 of the Revised Code." The taxpayer's apportionment ratio on the combined report (Schedule D – combined) applies only to the net income base, not to the net worth base.**

On Schedule D-2, lines 1(a), 1(c), 2(a), and 3(a) enter the property, payroll and sales amounts from Schedule D, lines 1(a), 1(b), 2, and 3, respectively. On Schedule D-2 lines 1(b), 1(d), 2(b) and 3(b), add the portion of property, payroll and sales, respectively, that the taxpayer excluded from the net income base apportionment factors because it was related to the production of nonbusiness income allocated in Schedule C.

Enter on line 1(e) the sum of lines 1(a) through 1(d), on line 2(c) the sum of lines 2(a) and 2(b), and on line 3(c) the sum lines 3(a) and 3(b).

## **SCHEDULE E BALANCE SHEET**

**Attach to the franchise tax report a balance sheet that reflects the books of the taxpayer on a separate company basis as of the beginning and the end of the taxpayer's taxable year.**

A taxpayer must keep its books in accordance with a generally recognized and approved accounting system. The tax-basis method of accounting is a generally recognized and approved accounting system. See *Gray Horse, Inc. v. Limbach* (1993), 66 Ohio St. 3d 631. If a taxpayer keeps its books both in accordance with regulatory accounting principles and in accordance with generally accepted accounting principles, the value of the taxpayer's issued and outstanding shares of stock under the net worth basis (O.R.C. section 5733.05(C)) is based upon those books kept in accordance with generally accepted accounting principles. See Tax Commissioner Rule 5703-5-08.

## **SCHEDULE F COMPUTATION OF TAXABLE VALUE O.R.C. SECTION 5733.05(C)**

The net worth base value of issued and outstanding shares of stock is determined from the books of the corporation as of the beginning of the taxpayer's annual accounting period

that includes the first day of January of the tax year. See O.R.C. section 5733.05. For example, assume that an Ohio franchise taxpayer has a taxable year beginning July 1, 2003 and ending June 30, 2004. For tax year 2005 the taxpayer's franchise tax net value of stock for purposes of the net worth base is determined as of July 1, 2004 which is the beginning of the taxpayer's annual accounting period that includes the first day of January of the 2005 tax year. Generally, the net worth base value at the beginning of the taxpayer's annual accounting period that includes the first day of January of the tax year (in this example, July 1, 2004) will be the same as the net worth base value at the end of the taxable year concluding prior to January 1 of the tax year (in this example, June 30, 2004).

For taxpayers other than financial institutions the net worth base equals assets minus liabilities adjusted by the "qualifying amount" less exempted assets (discussed below). "Reserves," except for those reserves that are considered appropriations of retained earnings under generally accepted accounting principles, are not included in the net worth computation. Thus, accounts such as unearned income and deferred federal income tax are not added to (or deducted from) net worth. In addition, the following "exempted assets" (under prior law) may not be deducted from net worth: goodwill, appreciation, abandoned property, investments in production credit associations and property within Ohio used exclusively in qualified research.

For taxpayers other than financial institutions the tax rate on the net worth base is four mills (.004) and the net worth base tax is limited to \$150,000 per taxpayer. The \$150,000 limit applies separately to each member of a combined report (there is not an overall net worth base limit for a combined group of taxpayers). At the net worth tax rate of four mills a "taxable value" of \$37,500,000 will result in the maximum net worth tax of \$150,000.

**Qualifying holding company (QHC).** A corporation that meets the requirements to be treated as a qualifying holding company, as defined in O.R.C. section 5733.04(L), and elects to be treated as a QHC by filing form FT QHC, Qualifying Holding Company Election, is not subject to the franchise tax on the net worth base and is not required to complete Schedule F. (A QHC is subject to the franchise tax on the net income base.) A corporation that elects to be treated as a qualifying holding company must attach form FT QHC to its franchise tax report and must check the box at the top of the front page of the franchise tax report indicating the corporation has elected to be treated as a qualifying holding company. For further information see general instruction #21, O.R.C. sections 5733.04(L), 5733.05(C)(2), and 5733.06(C) and form FT QHC, Qualifying Holding Company Election.

### **Line 1 – Net worth (assets minus liabilities).**

Enter the taxpayer's net worth (assets minus liabilities) as reflected on the taxpayer's books.

**Line 2 – Qualifying amount (if the taxpayer is a related member to a qualifying holding company)** O.R.C. section 5733.05.



If the taxpayer is a related member to a qualifying holding company (see above), the taxpayer must adjust its net worth and debt by the “qualifying amount.”

The **qualifying amount** is the amount that, when added to the taxpayer’s net worth (assets minus liabilities) and subtracted from the taxpayer’s liabilities or when subtracted from the taxpayer’s net worth and added to the taxpayer’s liabilities, will result in the taxpayer’s debt-to-equity ratio equaling the consolidated debt-to-equity ratio of the **qualifying controlled group** of which the taxpayer is a member. The consolidated debt-to-equity ratio is computed in accordance with generally accepted accounting principles on the last day of the taxpayer’s taxable year ending prior to the first day of the tax year. The qualifying amount that is added to the taxpayer’s net worth and subtracted from the taxpayer’s liabilities may not exceed the amount of the taxpayer’s liabilities owed to related members. Furthermore, the taxpayer’s net worth after adjustment by the qualifying amount may not exceed the net book value of the corporation’s assets. If the qualifying amount will be subtracted from the taxpayer’s net worth, enter the qualifying amount in parenthesis. See O.R.C. section 5733.05(C)(2).

The term “**qualifying controlled group**” means two or more corporations that meet the O.R.C. section 5733.052(A) ownership and control requirements to file a combined franchise tax report (whether or not the corporations actually file a combined report and whether or not the corporations are subject to the franchise tax). See O.R.C. section 5733.04(M).

The term “**related member**” is defined in the instructions for Schedule B-3, line 6.

#### **Line 4 – Exempted assets.**

**Note: The net worth exempted assets deduction no longer applies to air, noise, and water pollution control facilities for which the State of Ohio has issued an exemption certificate or to coal gasification facilities, coal conversion demonstration facilities, energy conversion facilities, solid waste energy conversion facilities, or thermal efficiency improvements facilities for which the State of Ohio has issued an exemption certificate.** See O.R.C. section 5709.25(B)(3) and 5709.20, as amended by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly.

- a. Enter the net book value of civil defense shelters within Ohio for which the State of Ohio has issued a civil defense certificate. See O.R.C. section 5502.49.
- b. Enter the net book value of “land devoted exclusively to agricultural use as of the first Monday of June in the corporation’s taxable year as determined by the county auditor of the county in which the land is located pursuant to section 5713.31 of the Revised Code.”

#### **Line 6 – Ohio apportionment ratio.**

If the taxpayer did not have nonbusiness income, enter the taxpayer’s Ohio apportionment ratio determined on a separate company basis from Schedule D, line 4.

If the taxpayer had nonbusiness income, enter the taxpayer’s Ohio apportionment ratio determined on a separate company basis from Schedule D-2, line 4.

**The taxpayer’s net worth base apportionment ratio must be determined on a separate company basis even if the taxpayer is a member of a combined report. See O.R.C. section 5733.05(D)(3) which states that the taxpayer’s net worth is multiplied by the net income base apportionment formula computed “. . . without regard to section 5733.052 of the Revised Code.”**

### **SCHEDULE G TAX COMPUTATION**

**Tier One Litter Tax** (O.R.C. section 5733.066) – All taxpayers except family farm corporations as defined in O.R.C. section 4123.01 and minimum fee taxpayers are subject to the tier one litter tax. The maximum tier one tax that a corporation (or a group of corporations filing a combined franchise tax report) must pay is \$5,000.

**Tier Two Litter Tax** (O.R.C. section 5733.065) – Corporations that manufacture or sell litter stream products in Ohio are subject to the second tier of the litter tax with the following limitations:

- a. If a corporation manufactures “litter stream products,” the corporation is subject to the second tier litter tax only if the corporation’s sales of litter stream products in Ohio during the taxable year exceed 5% of its total sales in Ohio during the taxable year or if its sales of litter stream products in Ohio during the taxable year exceed \$10 million.
- b. If a corporation sells litter stream products in the same form that the corporation obtains the products, the corporation is subject to the second tier litter tax only if its sales of litter stream products in Ohio during the taxable year exceed 5% of its total sales in Ohio during the taxable year.
- c. If a corporation sells food or beverages that are prepared at the premises where sold for consumption off the premises and transfers possession of litter stream products in the form of sacks, bags, lids, straws, plates, wrappings, boxes or containers that contain the food or beverages, the corporation is subject to the second tier litter tax only if such sales for off premises consumption exceed 5% of the corporation’s total sales during the taxable year.
- d. The maximum tier two tax that a corporation (or a group of corporations filing a combined franchise tax report) must pay is \$5,000.

Litter stream products are defined as follows:

- a. Intoxicating liquor, beer, malt beverages, wine, mixed beverages or spirituous liquor;
- b. Soft drinks;



- c. Glass, metal, plastic or fiber containers with a capacity of less than two gallons sold for the purpose of containing the beverages listed in sections a. and b. above;
- d. Container crowns and caps sold for the purpose of capping the containers in section c. above;
- e. Packaging materials used to pack or contain the beverages in sections a. and b. above when they are sold at retail;
- f. Packaging or serving materials used or received when obtaining food to carryout, such as sacks, bags, cups, lids, straws, plates, wrappings, boxes or containers of any type. The food or beverages that are for take-out must have been prepared for human consumption by a restaurant or take-out food outlet at the premises where sold at retail, and delivered to the purchaser for consumption off the premises where such food or beverages are sold;
- g. Cigarettes, cigars, tobacco, matches, candy and gum.

### SCHEDULE A-1 NONREFUNDABLE CREDITS

Set out below is a summary of each of the credits available to franchise taxpayers in the order in which they are listed in O.R.C. section 5733.98. O.R.C. section 5733.98 lists the order in which franchise tax nonrefundable credits and unused credit carryforward amounts must be used. The table on page 49 lists the nonrefundable credits in the order in which you must claim them (as prescribed in O.R.C. section 5733.98) as well as the carryforward period of each credit and the sections of the Ohio Revised Code that authorize the credits. A lower-ranking credit must be used before any higher-ranking credit is used. The order is important if the corporation is entitled to more than one nonrefundable credit and the corporation is unable to use some portion of the total credit amount in the year the credits were generated (because the total credit amount exceeds the tax due before the credit). Nonrefundable credits that are not used in the year generated can generally be carried forward to future years. However, the carryforward period is limited and varies from credit to credit. Any credit amount that remains unused after the carryforward period for that credit has expired is lost. The unused amount of a particular credit that is carried forward to a later year is used after any lower numbered credit listed in O.R.C. section 5733.98 but prior to the same credit generated in the later year and prior to any higher numbered credit on the list.

A nonrefundable credit may be used to reduce the tax liability (before considering any payments) to the minimum fee but a nonrefundable credit may not reduce the tax liability (before considering any payments) below the minimum fee.

**Note 1:** The new jobs credit and the credit for tax withheld by the Ohio Lottery Commission are not included below

because these credits are refundable credits which are considered payments of the tax. See line instructions for Schedule A, line 23.

**Note 2:** Unless otherwise stated all credit computations under O.R.C. chapter 5733 are to include the taxpayer's proportionate share amounts from any pass-through entity in which the taxpayer has a direct or indirect interest. See O.R.C. section 5733.057.

**Note 3:** The Credit for Losses on Loans Made to the Ohio Venture Capital (OVC) Program enacted by Amended Substitute House Bill 180, 124<sup>th</sup> Ohio General Assembly, effective April 9, 2003, does not appear on the 2005 Ohio franchise tax report or on the 2004 individual income tax return because the law specifically provides that taxpayers may not claim the credit during the first four years of the Ohio Venture Capital program measured from the date the Ohio Venture Capital Authority established its investment policy. (The OVC Authority established its investment policy on June 13, 2004.) The purpose of the credit is to provide OVC lenders and investors some security against losses on their loans to the program. See O.R.C. sections 150.01 to 150.10, 5733.49, 5733.98, 5747.80 and 5747.98.

**1. Credit for Taxes Paid by a Qualifying Pass-Through Entity** (O.R.C. section 5733.0611) – A corporation that is a qualifying investor in a qualifying pass-through entity can claim a nonrefundable credit equal to the corporation's proportionate share of the tax paid by the qualifying pass-through entity. However, in determining Ohio taxable income, a corporation that claims this franchise tax credit must add to federal taxable income the amount claimed as a credit to the extent that the amount was deducted or excluded from the corporation's federal taxable income. To claim this credit the qualifying investor must attach to its franchise tax report a copy of the IRS form K-1 that indicates the qualifying investor's proportionate share of the amount of the pass-through entity tax for which the qualifying investor seeks to claim a credit. For an explanation of the tax on qualifying pass-through entities see the instructions for form IT 1140, Tax Return for Pass-Through Entities and Trusts.

**Caution:** Do not claim this credit as a refundable credit or as a payment. This credit must be claimed as a nonrefundable credit on Schedule A, line 19.

**2. Credit for Qualifying Affiliated Groups** (O.R.C. section 5733.068) – If, as a result of the related entity and related member adjustments (see Schedule B-3), an affiliated group will pay over \$3.5 million more franchise tax than the members of the group otherwise would have paid had the members of the group not made the related entity and related member adjustment, then the members of the affiliated group may claim a credit equal to the difference between the additional tax and \$3.5 million. However, the credit is limited to \$1.5 million for the affiliated group (even if the additional tax exceeds \$5 million).

3. **Credit for Recycling and Litter Prevention Donations**

(O.R.C. section 5733.064) – A taxpayer may claim a credit for the taxpayer's cash donations made during the taxable year to: (a) municipal corporations, counties, townships, park districts and boards of education that have received litter control and recycling grants from the Division of Recycling and Litter Prevention under O.R.C. section 1502.05 and (b) Ohio corporations organized prior to January 1, 1987 that have been determined to be nonprofit corporations by the Internal Revenue Service and whose sole purpose is to promote and encourage recycling. The credit equals the lesser of half of the amount of the cash donation or half of the sum of the tier one and tier two litter taxes. For information on the litter tax see the line instructions for Schedule G.

4. **Credit for Maintaining Railroad Crossing Warning Devices** (O.R.C. section 5733.43) – Railroad companies

can claim a credit for maintaining signs, signals, gates and other electrical warning devices at public highway-railway crossings in Ohio at common grade. The credit equals 10% of the sum of the annual maintenance expenditures for each active grade crossing warning device in Ohio for which such expenditures were made during the taxable year. The credit is not to exceed \$200 for each device in Ohio for which such expenditures were made during the taxable year. Unused credit amounts may not be carried forward. This new credit applies to taxable years beginning after December 31, 2000 – thus, the credit first applies to the 2002 franchise tax report.

5. **Job Retention Credit** (O.R.C. 5733.0610(B) and 122.171) – The purpose of this new temporary nonrefundable credit is to encourage large Ohio manufacturers to retain jobs in Ohio. The credit applies to (1) taxpayer-manufacturers that make a capital investment of at least \$200 million at a single Ohio project site during three consecutive calendar years in the period January 1, 2002 and ending December 31, 2006 and to (2) taxpayers that make a capital investment of at least \$100 million at a single Ohio project site during three consecutive calendar years in the period January 1, 2002 and ending December 31, 2006 provided that the average wage of all full-time employment positions at the project site is greater than 400% of the federal minimum wage.

Credit applicants must apply to the Ohio Tax Credit Authority for approval of the capital investment project. As a prerequisite, the taxpayer must employ an average of 1,000 full-time employees at the project site during each of the 12 months preceding application. In addition, the taxpayer must retain at least 1,000 full-time employees at the project site for the entire term of the credit agreement. The amount of the credit equals a percentage of the Ohio income tax withheld from the taxpayer's employees at the project site as set forth in the agreement between the taxpayer and the Ohio Tax Credit Authority. However, the credit percentage may not exceed 75%. The credit began in tax year 2003 and is limited to a term of fifteen years. The Ohio Tax Credit Authority and the Ohio Department of Development administer this credit.

For additional information please contact the Ohio Department of Development's Office of Tax Incentives at (614) 466-4551.

This credit was amended by Amended Substitute House Bill 405, 124<sup>th</sup> General Assembly, effective December 13, 2001 and by Amended Substitute House Bill 95, 125<sup>th</sup> General Assembly effective June 26, 2003.

6. **Second Credit for Purchases of New Manufacturing Machinery and Equipment (7.5%–13.5% Credit – O.R.C. section 5733.33) – Caution:**

In *Cuno v. DaimlerChrysler*, 04a0293p.06, United States Court of Appeals for the Sixth Circuit, September 2, 2004, a three-judge panel of the U.S. Sixth Circuit Court of Appeals issued an opinion holding that this credit violates the Commerce Clause of the U.S. Constitution and enjoined its enforcement. The State of Ohio has sought review of the court's decision. Because a review of the decision is being made, the Department of Taxation is not currently enjoined from administering the tax credit. The department is currently allowing taxpayers to claim the credit in those circumstances where purchases of new manufacturing machinery and equipment qualify for the credit under Ohio law. The department will continue to monitor the situation and issue future notifications to taxpayers and practitioners as the situation warrants. If you have questions regarding the legal implications of continuing to claim this or other tax credits, the department urges you to seek advice from tax counsel.

**Manufacturers** may claim a credit for "new manufacturing machinery and equipment" purchased during the period July 1, 1995 to December 31, 2015 provided that the manufacturer installs the equipment in Ohio by the required date, explained below. The credit also applies to taxpayers that have an interest in pass-through entities (limited liability companies and partnerships) that during the same period purchase new manufacturing machinery and equipment provided that the pass-through entity is a manufacturer and the pass-through entity installs the machinery and equipment in Ohio by the required installation date.

**Required installation date:** New manufacturing machinery and equipment purchased during the qualifying purchase period must be installed in Ohio no later than December 31, 2016.

**"New manufacturing machinery and equipment"** means manufacturing machinery and equipment, the original use in this state of which commences with the taxpayer or with a partnership of which the taxpayer is a partner. . . ." (see O.R.C. section 5733.33(A)(2)). Thus, for purposes of this credit, **used equipment is "new" if the taxpayer or pass-through entity is the first to use the equipment in Ohio.** Furthermore, although the taxpayer must purchase the equipment during the qualifying purchase period and the equipment's original use in Ohio must begin with the taxpayer, the original use in Ohio is not limited to the qualifying purchase period. Accordingly,

manufacturing machinery and equipment that the taxpayer purchased during the qualifying purchase period upon exercising an option in a lease agreement is new manufacturing machinery and equipment for purposes of the credit even though the original use of the equipment in Ohio began with the taxpayer-manufacturer prior to the qualifying purchase period as a lessee under an operating lease. See *Duramed Pharmaceuticals, Inc. v. Zaino*, BTA No. 2002-V-164 (3-7-03), discussed below.

In *Duramed* the Department of Taxation argued that Duramed, a pharmaceuticals manufacturer, was not entitled to the credit on manufacturing equipment that Duramed began using as a lessee under an operating lease in 1994 (prior to the qualifying purchase period) and upon exercising an option in the lease agreement in 1997 (during the qualifying purchase period) Duramed purchased from the lessor, Ortho-McNeil Pharmaceutical Corporation. According to the department, Duramed was not entitled to the credit on such equipment because the equipment, when purchased in 1997, was not “new manufacturing machinery and equipment,” as defined in O.R.C. section 5733.33(A)(2).

Finding no evidence to suggest that the lease was in substance a purchase in 1994 and noting that “the evidence also establishes that **the original use of the machinery and equipment in Ohio was by Duramed in 1994**,” the board agreed with Duramed and held that Duramed was entitled to the credit on the equipment purchased from the lessor, Ortho-McNeil, in 1997 because Duramed purchased “new manufacturing machinery and equipment” during the qualifying purchase period. According to the board, “the definition of ‘new machinery’ under R.C. 5733.33(A)(2) is unambiguous and requires only that the original use in Ohio is by Duramed, and such original use is not restricted or limited to the qualifying period.”

The *Duramed* decision lends support to the following position: **The credit does not apply to a lessor that purchases new manufacturing machinery and equipment and leases that equipment to a manufacturer** (other than a manufacturer that is a member of the lessor’s qualifying controlled group – see the consolidated credit provision in O.R.C. section 5733.33(1)). Reason: *The original use in this state* can begin with only one person. Because the Board of Tax Appeals held that the original use in Ohio of equipment that Ortho-McNeil purchased and leased to Duramed began with Duramed, the original use of the equipment in Ohio could not have begun with Ortho-McNeil, the original purchaser and lessor, and thus the equipment was not “new” as to Ortho-McNeil. Accordingly, a lessor that purchases manufacturing machinery and equipment and leases that equipment to a manufacturer, other than to a member of the lessor’s qualifying controlled group, is not entitled to the credit because, as to the lessor, the manufacturing machinery and equipment is not “new manufacturing machinery and equipment” as defined in O.R.C. section 5733.33(A)(2).

Conversely, if the lessor, Ortho-McNeil, had been the original user of the equipment in Ohio, then Duramed would have been a subsequent user. And, as a subsequent user, Duramed would not have been entitled to the credit because Duramed would not have purchased “new” equipment. In any event, Ortho-McNeil’s entitlement to the credit was not an issue in *Duramed*, and under the facts of the case Ortho-McNeil was not entitled to the credit because Ortho-McNeil purchased the equipment in 1994, prior to the beginning of the qualifying purchase period.

**Correction to information release.** The Department of Taxation recently issued a correction to its September 22, 1995 information release regarding the “Second Credit for Purchases of New Manufacturing Machinery and Equipment.” Specifically, the department removed from page 3 under “Purchase” the following language indicated with strikeover: If for federal income tax purposes ~~or if under generally accepted accounting principles~~ a “lease” of qualifying equipment is considered a purchase of the equipment, the lease is also considered a purchase for purposes of the credit.

**Date of purchase.** New manufacturing equipment that is manufactured or assembled primarily by the taxpayer for the taxpayer’s own use is deemed to have been purchased on the date the taxpayer places the property in service in the county for which the taxpayer will calculate the credit. New manufacturing machinery and equipment not manufactured or assembled primarily by the taxpayer is deemed to have been purchased on the date which the agreement to acquire the property becomes binding.

**Credit is separately determined for each county and each purchase period.** A taxpayer must separately determine the credit for each Ohio county with respect to the qualifying equipment that the taxpayer (or a pass-through entity in which the taxpayer has an interest) purchases for use in that county during each of 21 separate qualifying purchase periods that comprise the period July 1, 1995 to December 31, 2015. The 21 separate qualifying purchase periods are the six-month period July 1, 1995 to December 31, 1995 and each of the calendar years 1996 through 2015. The credit is based on purchases made during the calendar year even if the taxpayer (or pass-through entity in which the taxpayer has an interest) has a fiscal year end.

**Credit rate and computation:** For those Ohio counties not designated as “eligible areas” the credit equals 7.5% of the amount by which the cost of qualifying equipment purchased during a qualifying period for use in an Ohio county exceeds the “base investment” for that county. “Eligible areas” are those Ohio counties and municipalities annually designated and certified by the director of the Ohio Department of Development based upon the economic criteria set forth in the law. For those Ohio counties designated as eligible areas, the credit equals 13.5% of the amount by which the cost of qualifying equipment purchased during a qualifying period for use in the county exceeds the base investment for the county.



For those Ohio counties that are not designated as eligible areas but contain eligible areas within their boundaries, the credit equals the sum of the following:

- 13.5% of the lesser of: (a) the cost of qualifying equipment purchased during the calendar year for use in the eligible areas of the county, or (b) the county excess (the cost of qualifying equipment purchased during the calendar year for use in the entire county minus the taxpayer's base investment for that county) and
- 7.5% of the amount by which the county excess is greater than the cost of the new manufacturing machinery and equipment purchased during the calendar year for use in the eligible areas in the county.

**Eligible areas:** To determine whether a county or area is an "eligible area" please call the Ohio Department of Development at 1-800-848-1300. The Department of Development has also prepared a map of "eligible areas" that is available on their Web site: <http://www.odod.state.oh.us> (click on: 1) "For Business"; 2) "Business Incentives"; 3) "Tax Credits"; and (4) "Priority Investment Area" under Ohio manufacturing machinery and equipment investment tax credit.

**Base investment.** The "base investment" for a county is determined by adding the cost of new manufacturing machinery and equipment purchased for use in the county during each of three "base years" and dividing the total by three. The base years, like the purchase years, are calendar years – regardless of whether the taxpayer has a fiscal year end.

The purchase periods along with their corresponding base years are as follows:

Calendar Year of Purchase	Base Years
7/1/95 – 12/31/95	1992, 1993, 1994
1996	1992, 1993, 1994
1997	1992, 1993, 1994
1998	1992, 1993, 1994
1999	1993, 1994, 1995
2000	1994, 1995, 1996
2001	1995, 1996, 1997
2002	1996, 1997, 1998
2003	1997, 1998, 1999
2004	1998, 1999, 2000
2005	1999, 2000, 2001
2006	2000, 2001, 2002
2007	2001, 2002, 2003
2008	2002, 2003, 2004
2009	2003, 2004, 2005
2010	2004, 2005, 2006
2011	2005, 2006, 2007
2012	2006, 2007, 2008
2013	2007, 2008, 2009
2014	2008, 2009, 2010
2015	2009, 2010, 2011

**Credit for equipment purchased by a pass-through entity that is a manufacturer.** The credit for qualifying equipment purchased by a pass-through entity is not computed at the pass-through entity level and then passed through to the taxpayers that have an interest in the pass-through entity. Instead, each taxpayer having an interest in a pass-through entity during a qualifying period in which the pass-through entity purchased qualifying equipment must claim the taxpayer's proportionate share of the cost of such equipment and a proportionate share of the pass-through entity's base investment in the county for which the qualifying equipment was purchased. For each qualifying period and for each county the proportionate share amounts are then added to the proportionate share amounts from other pass-through entities in which the taxpayer has an interest and to the taxpayer's own purchases of qualifying equipment and base investment. Each taxpayer then computes the credit after aggregating its proportionate share amounts with the taxpayer's own purchases and the taxpayer's own base investment.

**Qualifying controlled group must compute consolidated credit.** For new machinery and equipment purchased after December 31, 2000 a "qualifying controlled group" (a group of corporations related by more than 50% direct or indirect stock ownership – see O.R.C. sections 5733.04(M) and 5733.052(A)) must compute the credit **for each county** as if all taxpayers of the group were a consolidated, single taxpayer in that county. (**The consolidation provision does not eliminate the requirement to determine the credit on a county-by-county basis.**) The consolidation provision applies both to the equipment purchased after December 31, 2000 on which the taxpayer will claim the credit and to base year purchases that determine the threshold above which the credit applies. The qualifying controlled group may allocate the consolidated credit in any manner the group chooses and the group may amend that allocation anytime before the refund statute of limitations expires. See O.R.C. section 5733.33(I) as amended by Amended Substitute House Bill 640, 123<sup>rd</sup> General Assembly.

For new machinery and equipment purchased before January 1, 2001 a qualifying controlled group may elect to compute the credit as if the group were a consolidated, single taxpayer. The election can be made by filing an amended report and an application for refund anytime before the statute of limitations expires. Also, the election can be made by timely filing a petition for reassessment. The election, if made, applies to the credit computation for each county for all purchases of machinery and equipment made before January 1, 2001 and to all base years used to determine the threshold above which the credit applies for each county. That is, if a qualifying controlled group makes this election, the "consolidated, single taxpayer" computation also applies to all purchases of machinery and equipment made in earlier calendar years with respect to which the taxpayer has already filed tax reports. The election is irrevocable. The group is not required to allocate the remaining 1/7 credit amounts (the



1/7 credit amounts that must be claimed in future years) at the time the group makes the election. Rather, the group can allocate the unused 1/7 credit amounts in the tax years the group must utilize the credit.

The Department of Taxation maintains that for purposes of the consolidated credit calculation the members of a qualifying controlled group of corporations are determined as of January 1 of the tax year immediately following the calendar year in which the taxpayers purchased the equipment for which they claim the credit. That is, **for equipment purchased after December 31, 2000 the members of the qualifying controlled group as of January 1 of the tax year immediately following the purchase year must compute the credit on a consolidated basis regardless of whether those same corporations were members of the qualifying controlled group during the baseline years, during the purchase year, or during the remaining tax years over which the taxpayers will claim the credit.**

**Claiming the 1/7 credit amounts.** A taxpayer must claim 1/7 of the credit in each of the seven tax years following the calendar year in which the taxpayer purchased the equipment. However, for qualifying equipment purchased during the period July 1, 1995 to December 31, 1995 a taxpayer could not begin to claim the 1/7 credit amounts until tax year 1997. Each 1/7 credit amount that is not used in the year in which it otherwise could have been claimed may be carried forward for three years. The unused carryforward amount is used before the 1/7 amount for the subsequent year. See the table on page 50, which for each purchase year shows the base years and tax years in which the 1/7 credit amounts are claimed.

**Credit on equipment that is sold or moved from the county.** If the taxpayer either sells equipment purchased prior to January 1, 2001 or moves such equipment from the county for which the credit was originally computed, the taxpayer is not allowed any remaining 1/7 credit amounts on the equipment sold or moved. If the taxpayer either sells equipment purchased after December 31, 2000 or moves such equipment from the county for which the credit was originally computed, the taxpayer is not allowed any remaining 1/7 credit amounts on the equipment sold or moved unless the equipment is fully depreciated for federal income tax purposes at the time the equipment is sold or moved. However, under certain limited circumstances, the purchaser of a "large manufacturing facility" may claim the unused credits of the seller of the manufacturing equipment located at that manufacturing facility. See O.R.C. section 5733.33(C)(5)(b).

**Spreadsheet to calculate credit.** The Department of Taxation has prepared a computerized spreadsheet to calculate the credit. The spreadsheet is available only through the Internet. To access the spreadsheet and download the file to your computer, visit the department's Web site at:

<http://www.tax.ohio.gov>

Then click on "Tax Forms." Under "Tax Type" select "Corporate Franchise Tax." Under "Tax Year" select 2005. Click on "Search." Click on "Worksheet for 7.5% and

13.5% Manufacturer's Credit under O.R.C. sections 5733.33 and 5747.31 – 2005 (Rev. 9/04)."

**Notice of Intent.** Taxpayers who intend to claim this credit must file a "Notice of Intent" form with the Ohio Department of Development. Please send your request for the "Notice of Intent" form to the Ohio Department of Development, Economic Development Division, Office of Tax Incentives, P.O. Box 1001, Columbus, Ohio 43216-1001 or call 614-466-4551 or 1-800-848-1300. The street address for the Ohio Department of Development is 77 S. High Street, 28th floor, Columbus, Ohio 43215. The "Notice of Intent" form is also available on the Ohio Department of Development's Web site at:

<http://www.odod.state.oh.us>

Click on: (1) "For Business," (2) "Business Incentives," (3) "Tax Credits," (4) "Ohio Manufacturers Manufacturing Machinery and Equipment Investment Tax Credit," and (5) "Notice of Intent" for the applicable year.

**Additional information.** For additional information please see O.R.C. section 5733.33 and the Ohio Department of Taxation's September 22, 1995, May 6, 1996, May 7, 1996 and June 18, 1996 information releases available on the department's Web site.

- 7. Job Training Credit** (O.R.C. section 5733.42). Administered by the Ohio Department of Job and Family Services, this temporary credit is available for franchise tax report years 2001, 2004, 2005 and 2006. The credit applies to taxpayers that have incurred "**eligible training costs**" and have received from the director of the Ohio Department of Job and Family Services a tax credit certificate with respect to an "**eligible training program**" for "**eligible employees.**" For report years 2001, 2004, 2005 and 2006 the total credit available for distribution among all taxpayers is limited to \$20 million per year.

**New Law: Substitute House Bill 362, 125<sup>th</sup> General Assembly** effective December 30, 2004. Among other provisions, this new law amended the job training credit by eliminating the first come, first serve basis of distributing the \$20 million of available yearly credit and by allowing the director of the Ohio Department of Job and Family Services to adopt a rule establishing criteria and procedures for distributing the credit. **For additional information and to apply for this credit, visit the Ohio Department of Job and Family Services' Web site at [www.odjfs.state.oh.us/ottc/info/](http://www.odjfs.state.oh.us/ottc/info/).**

The credit also applies to individuals and to investors in pass-through entities that incur eligible training costs and received a tax credit certificate from the director of Jobs and Family Services with respect to an "eligible training program." Each investor in a pass-through entity on December 31 prior to the investor's tax year may claim a proportionate share of the pass-through entity's credit.

For tax year 2005 the amount of the credit equals half of the average of the eligible training costs paid or incurred by the taxpayer during calendar years 2002, 2003 and

2004. For tax year 2006 the amount of the credit equals half of the average of the eligible training costs paid or incurred by the taxpayer during calendar years 2003, 2004 and 2005. (The credit is based upon costs incurred during a calendar year regardless of whether the taxpayer has a fiscal year end.) The credit claimed by a taxpayer each tax year may not exceed \$100,000 and for each tax year is not to exceed \$1,000 for each eligible employee on account of whom eligible training costs were paid or incurred by the taxpayer during the calendar years applicable to that tax year.

**“Eligible training program”** means a program to provide job skills to **eligible employees** who are unable to function effectively on the job due to skill deficiencies or who would otherwise be displaced because of their skill deficiencies or inability to use new technology or to provide job skills to eligible employees that enable them to perform other job duties for the taxpayer. Eligible training programs do not include executive, management or personal enrichment training programs or training programs intended exclusively for personal career development.

**“Eligible training costs”** are the sum of the following amounts: (1) direct instructional costs, such as, instructor salaries, materials and supplies, textbooks and manuals, videotapes and other instructional media and training equipment used exclusively for the purpose of training “eligible employees,” and (2) wages paid to eligible employees for time devoted exclusively to an “eligible training program” during normal paid working hours.

**“Eligible employees”** are individuals who are employed full-time by the taxpayer in Ohio and have been so employed by the taxpayer for at least 180 consecutive days before the day an application for the credit is filed. “Eligible employees” do not include executive or managerial personnel except for the immediate supervisors of nonexecutive, nonmanagerial personnel, employees for whom the taxpayer claims the enterprise zone training credit pursuant to O.R.C. section 5709.65(A) or employees that are not full-time employees. See credit #16 for a summary of the enterprise zone training credit.

A taxpayer that proposes to conduct an eligible training program for which the taxpayer intends to claim the credit must apply to the director of Jobs and Family Services for a tax credit certificate for each tax year with respect to a calendar year in which the taxpayer incurred eligible training costs. The director may charge an application fee to cover the expenses incurred in administering the credit program, and the director may adopt rules to implement and administer the credit.

Upon receipt of an application the director of Jobs and Family Services may authorize a credit by granting the applicant a tax credit certificate if the director determines that all of the following conditions are satisfied:

i. The proposed training program is an “eligible training program,” as defined above;

- ii. The proposed training program is economically sound and will benefit the people of Ohio by improving work force skills and strengthening the economy of Ohio;
- iii. Receiving the credit is a major factor in the taxpayer’s decision to implement the program;
- iv. Authorization of the credit is consistent with the following:
  - The aggregate amount of credits authorized may not exceed \$20 million per calendar year;
  - No more than \$10 million in credits per calendar year may be authorized for corporations engaged primarily in manufacturing;
  - No less than \$5 million per calendar year will be set aside for corporations engaged primarily in activities other than manufacturing and having fewer than five hundred employees.

**If the director issues the taxpayer a tax credit certificate and later determines that the training program fails to meet the above requirements, the director may reduce the amount of the credit previously granted.** If the director reduces the credit, the director must certify the reduction to the tax commissioner, and the tax commissioner will reduce the credit accordingly. The taxpayer can appeal the reduction or denial of the credit to the director of the Department of Jobs and Family Services and can appeal the director’s determination to the Board of Tax Appeals.

Taxpayers must use the credit in the order established in O.R.C. section 5733.98 and may carry forward unused credit amounts for three tax years following the tax year for which the credit is computed.

The Legislature significantly amended the credit in Amended Substitute Senate Bill 287, 123<sup>rd</sup> General Assembly.

8. **Credit for Qualified Research Expense** (O.R.C. section 5733.351) – For tax years 2004 and thereafter the credit equals 7% of the amount by which the taxpayer’s “qualified research expense” incurred in Ohio during the taxable year exceeds the taxpayer’s average annual qualified research expenses incurred in Ohio for the three preceding taxable years. The term “qualified research expense” has the same meaning as in I.R.C. section 41.

9. **Credit for Eligible New Employees in an Enterprise Zone** (O.R.C. section 5709.66) – A taxpayer may apply to the director of Development for an “employee tax credit certificate” for each eligible new employee the enterprise hires after June 30, 1994 at a facility located in a “central city of a metropolitan statistical area” (as defined by the United States office of management and budget) or located in the “Appalachian region” (as defined by the Appalachian Regional Development Act of 1965) to which an enterprise zone agreement applies provided that the taxpayer is complying with the enterprise zone agreement

and has not closed or reduced employment at any place of business in Ohio within the 12 months preceding the application. A taxpayer who is issued a tax credit certificate for an eligible employee may claim a \$1,000 nonrefundable credit for each taxable year covered under the enterprise zone agreement during which the eligible employee is employed by the taxpayer. An "eligible employee" is a new employee who at the time the employee was hired to work at the facility was a recipient of aid to dependent children or general assistance and resided for at least one year in the county in which the facility is located.

If a taxpayer claims an enterprise zone new employee tax credit with respect to an employee, the taxpayer may not claim the O.R.C. section 122.17 new jobs credit with respect to that employee.

Credit application forms are available from the Ohio Department of Development, Economic Development Division, Office of Tax Incentives, P.O. Box 1001, Columbus, Ohio 43216-1001 or call 614-466-4551 or 1-800-848-1300. The street address for the Ohio Department of Development is 77 S. High Street, 28th floor, Columbus, Ohio 43215.

- 10. Credit for Eligible Costs Associated with a Voluntary Action (Brownfield Site Clean-Up)** (O.R.C. section 5733.34) – A taxpayer who participated in the Ohio Environmental Protection Agency's (OEPA) Voluntary Action Program and who received and maintained a "covenant not to sue" from the OEPA could apply to the director of Development for this credit, which was intended to encourage the private sector cleanup and reuse of properties contaminated by hazardous substances. Those taxpayers that have been granted the credit can claim 1/5 of the credit in each of five tax years beginning with the tax year immediately following the calendar year in which the taxpayer and the director of Development reached a credit agreement. Each 1/5 credit amount that is not used in the year in which it otherwise could have been claimed may be carried forward for three years. The authority for the director of Development to grant tax credits under this program expired on June 30, 1999. So, **except for carryforward amounts this credit cannot be claimed after tax year 2004.** For additional information please contact the Ohio Department of Development, Economic Development Division, Office of Tax Incentives, P.O. Box 1001, Columbus, Ohio 43216-1001 or call 614-466-4551 or 1-800-848-1300. The street address for the Ohio Department of Development is 77 S. High Street, 28th floor, Columbus, Ohio 43215.

- 11. Credit for Employers that Establish On-Site Child Daycare Centers** (O.R.C. section 5733.37) – A taxpayer that establishes an Ohio licensed day-care center that serves only children of the taxpayer's employees and is located at the employees' worksite may claim a credit equal to the lesser of \$100,000 or 50% of the amount the taxpayer incurred for equipment, supplies, labor, and real

property, including renovation of real property, to establish the day-care center. The taxpayer can claim the credit only for the tax year immediately following the taxable year in which the child daycare center begins operations, and the taxpayer can claim the credit only for tax years 1999, 2000, 2001, 2002 or 2003. Accordingly, **no new credit is generated for tax year 2004 and thereafter. However, the credit amount that the taxpayer did not use in the tax year claimed may be carried forward for five taxable years.** But, if the taxpayer ceases to operate the center within the five-year carryforward period, any unused portion of the credit is lost.

- 12. Ethanol plant investment credit** (O.R.C. sections 5733.46 and 901.13) – This nonrefundable franchise tax and individual income tax credit equals 50% of the amount of money that the taxpayer invests in O.R.C. section 901.13 certified ethanol plants in the calendar year preceding the tax year (the investment period is the calendar year preceding the tax year regardless of whether the taxpayer's taxable year is a calendar year). The credit is limited to \$5,000 per taxpayer per certified ethanol plant regardless of the number of years in which the taxpayer makes such investments. The credit applies to tax years 2003 through 2013. Credits not used in the tax year following the calendar year in which the taxpayer makes the investment may be carried forward for three tax years.
- 13. Credit for Grape Production Property** (O.R.C. section 5733.32) – Grape producers may claim a credit equal to 10% of the cost of qualifying property purchased on or after January 1, 1994. Qualifying property is any property, plant, or equipment used in growing, harvesting or producing grapes in Ohio. Unused credit amounts may be carried forward for seven tax years. The credit is subject to recapture if the taxpayer disposes of the property or ceases to use it as qualifying property within seven years after placing it in operation.
- 14. Export Sales Credit** (O.R.C. section 5733.069) – A taxpayer that increases its export sales and also increases either its Ohio property or its Ohio payroll may claim a credit for tax years 1993 through 2005. **However, for tax years 2001 to 2005 no new credit is generated. For tax years 2001 to 2005 only unused carryforward credit amounts from tax years 1993 to 2000 can be claimed.** If the taxpayer is claiming an export sales credit carryforward from tax year 2000 or earlier, please attach to the franchise tax report a schedule which shows the year(s) in which the credit was generated, the years in which the credit was used and the remaining carryforward amount.

Additional information is available upon request from the Ohio Department of Taxation, Corporation Franchise Tax Unit, Attn: Export Credit, P.O. Box 2476, Columbus, OH 43216-2476.



**15. Technology Investment Credit** (O.R.C. section 5733.35) – **The Department of Taxation previously referred to this credit as the Edison Center Credit for Research and Development Investors. The Department of Development, which administers this credit, refers to the credit as the “Technology Investment Tax Credit.” In order to avoid confusion and for the sake of consistency we have renamed the credit consistent with the name given by the Department of Development.**

Investors that provide capital to certain qualifying small, Ohio-based research and development or technology transfer companies may be eligible for a nonrefundable credit equal to 25% of the taxpayer's at-risk investment. An investor or group of investors that proposes to invest in a qualifying small, Ohio-based research and development company or technology transfer company and seeks to claim the credit must apply to one of the state's seven Edison Centers for approval of the proposed investment. The credit application fee for a single investor is \$200 and for a group of investors is \$800. The credit is evidenced by a tax credit certificate and is administered by the Ohio Department of Development along with the industrial technology and enterprise advisory council.

**Note:** Amended Substitute House Bill 1, 125<sup>th</sup> General Assembly (effective July 9, 2003) amended this credit by increasing the credit percentage to 30% in the case of investments in certain qualifying small, Ohio-based research and development or technology transfer companies in distressed areas of the state and in EDGE business enterprises. An “EDGE business enterprise” is an “Ohio entity” certified by the director of administrative services as a participant in the encouraging diversity, growth, and equity program established by the governor's executive order 2002-17T.

For additional information please see O.R.C. sections 122.15, 122.151, 122.152, 122.153, and 122.154 as amended by Amended Substitute House Bill No. 1 and contact the Ohio Department of Development, Technology Division, 77 S. High Street, P.O. Box 1001, Columbus, OH 43216-1001, or call (614) 466-3887 or 1-800-848-1300. The street address for the Ohio Department of Development is 77 S. High Street, 28th floor, Columbus, Ohio 43215.

**16. Enterprise Zone Day-Care Credit** (O.R.C. section 5709.65(A)) – If a taxpayer has received a Tax Incentive Qualification Certificate from the Ohio Department of Development and if the taxpayer reimburses certain new employees (see general instruction #25 and O.R.C. section 5709.64(A)(2)(a) to (e)) for all or part of the cost of day-care services necessary to enable the employees to be employed at the facility for which the certificate is issued, the taxpayer may claim a credit. The credit equals the amount so reimbursed for the taxable year in which the taxpayer makes the reimbursement, up to a maximum of \$300 for each child or dependent receiving the day-care services.

**Enterprise Zone Training Credit** (O.R.C. section 5709.65(A)) – If a taxpayer has received a Tax Incentive Qualification Certificate from the Ohio Department of Development and if the taxpayer pays or reimburses all or part of the cost of a qualified training program for certain new employees (see general instruction #24 and O.R.C. section 5709.64(A)(2)(a) to (e)) the taxpayer may claim for each new employee a credit equal to the amount paid or reimbursed or \$1,000, whichever is less. The taxpayer may claim the credit in the taxable year in which the new employee completes ninety days of subsequent employment.

**17. Research and Development Loan Repayment Credit** (O.R.C. sections 5733.352, 5747.331, and 166.17 through 166.21) – The amount of the credit equals the borrower's qualified research and development loan payments during the calendar year immediately preceding the tax year (regardless of whether the taxpayer's taxable year is a calendar year or a fiscal year). The term *qualified research and development loan payments* means payments of principal and interest on a loan made to the borrower from Ohio's research and development fund administered by the Ohio Department of Development.

The borrower's credit generated as a result of its qualified research and development loan payments made during a calendar year may not exceed \$150,000 per loan. The credit amount not used in the tax year immediately following the calendar year in which the credit was generated can be carried forward until fully used. A borrower is eligible to receive the tax credit regardless of whether the borrower is subject to the corporation franchise or income tax. Furthermore, the borrower, whether or not it is subject to the franchise tax, can assign the tax credit to any of the following: (i) the borrower's related member; (ii) the owner or lessee of the eligible research and development project; or (iii) a related member of the owner or lessee of the eligible research and development project. If the borrower is a pass-through entity and the taxpayer is a partner or member of the pass-through entity-borrower, the taxpayer can claim a proportionate share of the pass-through entity-borrower's credit.

**SCHEDULE B-3  
RELATED ENTITY AND  
RELATED MEMBER ADJUSTMENTS  
O.R.C. SECTIONS 5733.04(I)(12) & (I)(13)  
O.R.C. SECTIONS 5733.042, 5733.054, & 5733.055**

**Note:** If the taxpayer is included in a combined franchise tax report, complete Schedule B-3 (Combined) on form FT 1120C (rather than Schedule B-3 on form FT 1120). Nonbusiness capital gains and capital losses attributed to a member of a combined report from a related entity's sale or other disposition of dividend producing property are separately allocable by each member. All other related entity and related member adjustments are apportionable and are computed on a combined basis. See the May 6, 1992, franchise tax information release “Schedule B-3 (Combined)”

– Related Entity and Related Member Adjustments for Corporations Included in a Combined Franchise Tax Report.” The information release is available on the Department of Taxation’s Web site.

### **Related Entity Adjustments**

#### **Line 1 – Related entity gains (losses) from sale of investments.**

A taxpayer must add to (and deduct from) federal taxable income, line 28 of federal form 1120 or line 24 of federal form 1120A, the taxpayer’s proportionate share of a nontaxpayer related entity’s gains (and losses) from sales of investments in the stock or debt of another entity if at any time during the 24-month period commencing 12 months prior to the date of sale and ending 12 months after the date of sale the taxpayer and its related entities owned at least 50% of the stock or debt of the entity whose stock or debt was sold.

The term “related entity” means any of the following:

- An individual stockholder, or a member of the stockholder’s family enumerated in I.R.C. section 318, if the stockholder and the members of the stockholder’s family own directly or indirectly in the aggregate at least 50% of the value of the taxpayer’s outstanding stock;
- A stockholder, or stockholder’s partnership, estate, trust or corporation, if the stockholder and the stockholder’s partnerships, estates, trusts and corporations own directly or indirectly, beneficially, or constructively, in the aggregate, at least 50% of the value of the taxpayer’s outstanding stock;
- A corporation, or a party related to the corporation in a manner that would require I.R.C. section 318 attribution of stock from the corporation to the party or from the party to the corporation, if the taxpayer owns directly or indirectly in the aggregate at least 50% of the value of the corporation’s outstanding stock.

The I.R.C. section 318 attribution rules apply to the above.

A taxpayer is a corporation subject to the Ohio corporation franchise tax. A nontaxpayer is an entity not subject to the Ohio corporation franchise tax.

Upon audit you may be asked to provide a schedule containing the following information for each gain and each loss attributed to the taxpayer and recognized by a nontaxpayer-related entity from the related entity’s sales, exchange or other disposition of stock or debt described above:

- a. The name of the related entity which sold the stock or debt;
- b. The name of the entity whose stock or debt was sold by the related entity and a description of the property sold;
- c. The amount of gain or loss recognized for federal income tax purposes by the related entity from each sale or other disposition;

- d. The amount of the taxpayer’s proportionate share of the related entity’s gain or loss from the sale of stock or debt based upon the taxpayer’s direct, indirect, beneficial or constructive ownership of the outstanding stock of the related entity immediately prior to the direct or indirect sale, exchange, or other disposition; and

- e. A description of the ownership relationship between the taxpayer and the related entity which sold the stock or debt and a description of the ownership relationship between the related entity and the entity whose stock or debt was sold by the related entity.

Enter on line 1 the total net gain or net loss from all transactions described above.

#### **Line 2 – Related entity gains (losses) from sale of other intangible property.**

A taxpayer must add to (and deduct from) federal taxable income, line 28 of federal form 1120 or line 24 of federal form 1120A, its proportionate share of a nontaxpayer related entity’s gains (and losses) from sales of intangible property other than stock, securities and debt if the intangible property was owned or used at any time prior to the sale by either the taxpayer or by a related entity that was a taxpayer at any time during the related entity’s ownership or use of the property.

Enter on line 2 the total net gain or net loss from all transactions described above. Upon audit you may be asked to provide a schedule containing information similar to that described in line 1 for each gain and each loss attributed to the taxpayer and recognized by a nontaxpayer-related entity from the related entity’s sale, exchange or other disposition of intangible property other than stock, securities and debt.

#### **Line 4 – Allocable portion of total related entity gains (losses).**

Enter on line 4 the total related entity net capital gain or net capital loss that is allocable.

For taxable years ending on or after June 26, 2003, capital gains and capital losses attributed to the taxpayer from a related entity’s sale, exchange, or other disposition of intangible property that may produce dividend income are allocable within and without Ohio only if that income is nonbusiness income. See the instructions for Schedule C, line 2.

#### **Line 10 – Related entity gains (losses) allocable to Ohio.**

Enter on line 10 the total related entity net capital gain or net capital loss which is attributed to the taxpayer and allocable to Ohio.

**As noted in the instructions for line 4 above, for taxable years ending on or after June 26, 2003, capital gains and capital losses attributed to the taxpayer from a related entity’s sale or other disposition of intangible property that may produce dividend income are allocable within and without only if that income is nonbusiness income. If the income attributed to the taxpayer is nonbusiness**

**income, allocate the income using the instructions for Schedule C, line 2.**

**Line 11 – Add excess related entity loss.**

Add each related entity loss deducted from federal taxable income on lines 1 and 2 of this schedule to the extent that the loss actually allocated and apportioned to Ohio and to other states that impose a tax on or measured by net income exceeds the total loss. The addition is limited to that portion of the loss actually allocated to Ohio on line 10 or apportioned to Ohio on line 9.

A taxpayer claiming a deduction for related entity losses on line 1 or 2 of Schedule B-3 may be required upon audit to furnish a schedule containing the following information for **each** loss deducted:

- The name of each state in which the loss was deducted for purposes of computing a tax on or measured by net income;
- The apportionment ratio in each state in which the loss was deducted;
- The amount of the loss actually allocated or apportioned to each state that imposes a tax on or measured by net income;
- The amount of the loss actually allocated or apportioned to Ohio;
- The amount by which the loss allocated and/or apportioned to Ohio and to other states exceeds the total loss; and
- The smaller of the amount from line **d** or line **e**, above.

Enter on Line 11 as a positive number the sum of the amounts from **f**, above.

**Line 12 – Deduct excess related entity gain.**

Line 12 grants relief in those circumstances where the related entity gain subjected to tax by Ohio and by other states exceeds the total gain. On line 12 a taxpayer may deduct each gain added to federal taxable income on lines 1 and 2 of this schedule to the extent that the gain actually taxed by Ohio and by other states that impose a tax on or measured by net income exceeds the total gain. The deduction is further limited to the portion of the gain that is actually allocated to Ohio on line 10 or apportioned to Ohio on line 9.

A taxpayer claiming a deduction on line 12 may be required upon audit to furnish a schedule containing the following information for **each** gain for which the deduction is claimed:

- The name of each state that imposed on the gain a tax on or measured by net income;
- The apportionment ratio in each state that imposed a tax on the gain;
- The amount of the gain actually allocated or apportioned to each state that imposed tax on the gain;
- The amount of the gain actually allocated or apportioned to Ohio;

e. The amount by which the gain allocated and/or apportioned to Ohio and to other states exceeds the total gain; and

f. The smaller of the amount from line **d** or line **e**, above.

Enter on line 12 the sum of the amounts from line **f**, above.

**Related Member Adjustments**

**Line 6 – Interest expense and intangible expense paid to related members.**

Enter on line 6 the sum of (i) interest expense paid or accrued to all related members described in A through F below, (ii) intangible expenses paid or accrued to all related members described in A through F below and (iii) excess interest paid or accrued to related members described in G, below.

**Definitions for purposes of this adjustment**

- “**Related member**” means a person that, with respect to the taxpayer during all or any portion of the taxable year, is any of the following: (i) a “related entity” as defined in division (I)(12)(c) of O.R.C. section 5733.04 (summarized in the instructions for line 1, above), (ii) a “component member” as defined in I.R.C. section 1563(b) or (iii) a person to whom or from whom there is attribution of stock ownership in accordance with I.R.C. section 1563(e) except that “20%” shall be substituted for “5%” wherever “5%” appears in I.R.C. section 1563(e).
- “**Interest expense**” includes but is not limited to amounts deducted under I.R.C. section 163.
- “**Intangible expenses**” are expenses and costs for the use of intangible property. Such expenses include but are not limited to losses from factoring transactions and discounting transactions and royalty, patent, technical and copyright fees, licensing fees and other similar expenses deducted for purposes of determining taxable income under the I.R.C..
- An “**excess interest rate**” is an interest rate that exceeds by more than 3% the greater of (i) the annual interest rate prescribed by O.R.C. section 5703.47 in effect at the time of the origination of the indebtedness or (ii) the annual interest rate prescribed by O.R.C. section 5703.47 in effect at the time the taxpayer paid, accrued, or incurred the interest expense.

A taxpayer must add to its federal taxable income the following: (i) all interest expense and intangible expenses which the taxpayer paid or accrued to related members described in A through F, below, and (ii) excess interest paid to related members described in G, below:

- A related member whose activities in any one state are primarily limited to the maintenance and management of (i) intangible investments or (ii) intangible investments of corporations, business trusts or other similar entities;
- A related member that is a personal holding company as defined in I.R.C. section 542 without regard to the stock



ownership requirements set forth in I.R.C. section 542(a)(2);

- C. A noncorporate related member that is directly or indirectly owned in whole or in part by a personal holding company as defined in I.R.C. section 542 without regard to the stock ownership requirements set forth in I.R.C. section 542(a)(2);
- D. A related member that is an I.R.C. section 552 foreign personal holding company;
- E. A noncorporate related member that is directly or indirectly owned in whole or in part by an I.R.C. section 552 foreign personal holding company; and
- F. A related member if that related member or another related member directly or indirectly paid or accrued interest expenses or intangible expenses. However, this portion of the law is applicable only if within a 120-month period commencing three years prior to the beginning of the tax year and ending seven years after the beginning of the tax year the related member directly or indirectly paid or accrued such amounts to one of the five related members listed in A through E directly above.
- G. Any related member other than those described in A through F, above, to which the taxpayer paid interest at an "excess interest rate."

**Example:** The annual rate prescribed by O.R.C. section 5703.47 for 2004 is 4%. If during 2004 a taxpayer paid or accrued interest expense to a related member not described in A through F, above, at the rate of 13% on indebtedness that originated in 2004, the excess interest rate is 6% (the 13% actual rate minus the sum of the 4% O.R.C. section 5703.47 rate and the 3% O.R.C. section 5733.042 allowance). The taxpayer must add to federal taxable income only the excess interest expense. In this example the excess interest expense is the difference between the interest paid or accrued to the related member at the actual 13% rate and the interest that would have been paid or accrued had the rate been 7%.

The interest expense and intangible expense adjustments do not apply to the extent that the taxpayer's increased tax would have been avoided by filing a combined franchise tax report with the related member to which the taxpayer paid the interest expense or intangible expense. In addition, the interest expense and intangible expense adjustments do not apply where both of the following conditions are met: (i) the transaction did not have as a principal purpose the avoidance of Ohio franchise tax and (ii) the related member to whom the taxpayer paid interest expense and/or intangible expense, during the same taxable year directly or indirectly paid, accrued, or incurred such amounts to persons who were not related members.

**If the taxpayer's additional franchise tax attributable to the related member adjustments is not paid within one year after the date the report is filed, the tax commissioner may charge a penalty equal to twice the**

**interest charged. However, the penalty does not apply if the additional tax (i) is less than 10% of the total franchise tax and (ii) is less than \$50,000. This penalty is in addition to any other applicable penalties and charges.**

If the taxpayer is required to enter an amount on line 6, the taxpayer may be required upon audit to provide a schedule containing the following information with respect to each related member:

- Whether the related member is (i) a related member described in A through F or (ii) a related member described in G;
- For related members described in A through F to which the taxpayer paid intangible expense, (i) the amount paid and (ii) a description of the intangible property that the taxpayer paid the related member to use;
- For related members described in A through F to which the taxpayer paid interest expense, (i) the amount paid, (ii) the amount of the taxpayer's indebtedness to the related member at the beginning and at the end of the taxpayer's taxable year, (iii) the interest rate on the indebtedness and (iv) the date the indebtedness originated;
- For related members described in G to which the taxpayer paid excess interest expense, (i) the excess interest paid, (ii) the total interest paid, (iii) the actual interest rate on the indebtedness, (iv) the amount of the taxpayer's indebtedness to the related member at the beginning and at the end of the taxpayer's taxable year, and (v) the date the indebtedness originated.

**Line 13 – Deduct related members' net interest income and net intangible income taxed by other states.**

A taxpayer may deduct an amount equal to the sum of each related member's "net interest income" (defined below) and "net intangible income" (defined below) actually allocated and apportioned to other states that impose a tax on or measured by income. The deduction is limited to the increase in Ohio taxable income resulting from the adjustments required by Schedule B-3, line 6.

**Net interest income** is the excess of interest received by a related member from the taxpayer over interest expenses and costs paid or accrued by the related member to another related member described in A through G, above (see instructions for line 6).

**Net intangible income** is the excess of income received by a related member from the taxpayer for the taxpayer's use of intangible property over intangible expenses paid or accrued by the related member to another related member described in A through G, above.

For purposes of this deduction, related members receiving such income from the taxpayer and paying such expenses are limited to those related members described in A through G, above.

Taxpayers who are claiming a deduction on line 13 may be required upon audit to furnish a schedule containing the following additional information for each related member that received from the taxpayer interest income or income for the use of intangible property:

- a. The names of all other states that imposed on the related member a tax on or measured by income. For purposes of this deduction the term "other states" does not include those states under whose laws the taxpayer files or could have elected to file with the related member, or the related member files or could have elected to file with another related member, a combined income tax report or return, a consolidated income tax report or return, or any other report or return where such report or return is due because of the imposition of a tax measured on or by income and such report or return results in the elimination of the tax effects from transactions directly or indirectly between either the taxpayer and the related member or between the related member and another corporation if such other corporation, during a 120-month period commencing three years prior to the beginning of the tax year and ending seven years after the beginning of the tax year, directly or indirectly paid, accrued or incurred intangible expenses and costs or interest expenses and costs to an entity described in A through E, above. See instructions for line 6;
- b. the related member's interest expense that it paid or accrued to other related members described in A through G, above;
- c. the related member's intangible expenses that it paid or accrued to other related members described in A through G, above;
- d. the related member's net interest income (defined above);
- e. the related member's net intangible income (defined above);
- f. the related member's apportionment ratio in each state listed in (a), above; and
- g. the related member's net interest income and net intangible income that it actually allocated or apportioned to each state which imposed tax on the income.

Enter on line 13 the smaller of the following:

- The sum of all related members' net interest income and net intangible income actually allocated and apportioned to other states that imposed a tax on or measured by income or
- The taxpayer's increase in Ohio taxable income resulting from the adjustments required by O.R.C. section 5733.042 (that is, the amount on line 6 of this schedule multiplied by the taxpayer's Schedule D, Ohio apportionment ratio.)

For further information regarding the related entity and related member adjustments, please contact the Department of

Taxation, Corporation Franchise Tax, P.O. Box 2476, Attn: Related Entity/Related Member, Columbus, Ohio 43216-2476.

### Tax Commissioner Rules Applicable to the Ohio Corporation Franchise Tax

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|------------|--|
| 5703-1-12  | Requests for an opinion of the tax commissioner  |
| 5703-5-01  | Definitions applicable to rules 5703-5-01 to 5703-5-05 of the Administrative Code  |
| 5703-5-02  | Date as of which the value of a taxpayer's issued and outstanding stock is determined  |
| 5703-5-03  | Dates on which a taxpayer's taxable year begins and ends   |
| 5703-5-04* | Changes of a taxpayer's annual accounting period   |
| 5703-5-06  | Combined reporting of the corporation franchise tax  |
| 5703-5-08  | Books from which the value of issued and outstanding shares of stock is determined under the net worth basis of the corporation franchise tax  |
| 5703-5-09  | Allocating and apportioning income of airlines<br><b>Note:</b> Rule 5703-5-09 was rescinded effective March 21, 2002 as a result of the Board of Tax Appeals decision in <i>Delta Airlines, Inc. v. Tracy</i> , BTA No. 96-T-471 & 96-T-472 (1-12-2001). |
| 5703-5-10  | Corporate franchise tax; accounts maintained under Statement of Financial Accounting Standards No. 106   |

**\*Note: Effective for tax years 2005 and thereafter, the department amended Rule 5703-5-04 to clarify when a taxpayer's annual accounting period changes and to eliminate income proration for franchise taxable years that exceed one year in length.**

### Information Releases

Since 1991 the Corporation Franchise Tax Division has issued the following information releases:

- "Income and Franchise Tax Updates," December 2004
- "Questions Regarding Ohio's New Manufacturing Machinery and Equipment Tax Credit – R.C. 5733.33 and 5747.31," issued September 2004; revised February 2005.
- "The franchise tax effects of the IRC section 338(h)(10) election," June 2004
- "Sales Factor Situsing Revisions," April 2004
- "Ohio Bonus Depreciation Adjustment and the Internal Revenue Code's Passive Activity Loss, Basis Limitation and At-Risk Rules," November 2002

- “Recently Enacted Ohio Legislation Affects Depreciation Deductions for Taxable Years Ending in 2001 and Thereafter” July 2002
- “Pass-through Entity Tax: Certain Estimated Tax Payments Due September 16, 2002,” July 3, 2002
- “Corporate Franchise Tax – Nexus Standards,” September 2001
- “Corporation Franchise Tax Nexus for Non-resident Limited Partners Following the UCOM Decision,” March 15, 2001
- “I.R.C. Section 482 Study: Safe Harbor to Avoid Ohio Corporate Franchise Tax Report Required or Expanded Combinations,” June 23, 2000
- “Withdrawal of Special Instructions,” October 31, 1997
- “Am. Sub. H.B. No. 215, 122nd General Assembly (Budget Bill), Summary of Franchise Tax and Income Tax Provisions,” September 18, 1997
- “IRS ‘Check the Box’ Entity Selection Regulations,” August 19, 1997
- “Revisions to May 6, 1996 Information Release,” June 18, 1996
- “Alternative 20 Percent Credit,” May 7, 1996
- “Examples Setting Forth the Division’s Interpretation of O.R.C. Sections 5733.33 and 5747.31, ‘Second Credit for Purchases of New Manufacturing Machinery and Equipment,’ ” May 6, 1996
- “Second Credit for Purchases of New Manufacturing Machinery and Equipment,” September 22, 1995
- “20 Percent Threshold Test Credit for Purchases of New Manufacturing Machinery and Equipment,” September 21, 1995
- “Newly Enacted Investment Tax Credit Law,” October 14, 1994
- “Recently Enacted Legislation Revises the Requirements for Corporations Paying Corporate Franchise Tax by Electronic Funds Transfer (EFT),” July 31, 1994
- “Taxation of S Corporations and Their Shareholders,” July 31, 1994
- “New Legislation Requires Certain Corporations to Pay Corporate Franchise Tax by Electronic Funds Transfer,” October 29, 1993
- “Safe Harbor Leases: Franchise Tax Policy Change,” November 10, 1992
- “Application of Ohio Revised Code Section 5733.053 (Transferor Statute) to the Merger of a C Corporation into an S Corporation,” September 24, 1992
- “Schedule B-3 (Combined) – Related Entity and Related Member Adjustments for Corporations Included in a Combined Franchise Tax Report,” May 6, 1992
- “Exempt Federal Interest,” January 9, 1992
- “Credit for Investment in Qualified Subsidiaries,” July 16, 1991
- “Taxpayer Elected Franchise Tax Combinations,” May 15, 1991
- “Foreign Technical Service Fee Deductions,” May 15, 1991.

Tax information releases are not Opinions of the Tax Commissioner within the meaning of O.R.C. section 5703.35. Nevertheless, the releases do reflect the Department of Taxation’s interpretation of the law. Information releases are available on the department’s Web site.



<b>Ohio Franchise Tax Forms</b> <b>Many of the department's forms are available on the Internet at: <a href="http://www.tax.ohio.gov">http://www.tax.ohio.gov</a></b>		
		<b>Revision Date</b>
FT COM	Request for Permission to File or to Amend a Combined Corporation Franchise Tax Report	7/00
FT 1120E	Declaration of Estimated Corporation Franchise Tax	12/04
FT 1120ER	Application for Automatic Extension	12/04
FT 1120EX	Request for an Additional Extension of Time for Filing Corporation Franchise Tax Report	12/04
FT 1120	Corporation Franchise Tax Report	12/04
FT 1120VL	Valuation Limitation on Gains and Losses from Sales or Exchanges of Property	7/00
FT 1120C	Corporation Franchise Tax (Combined Report)	12/04
FT WAIVER	Consent to Extend the Time to Assess or Refund the Ohio Corporation Franchise Tax	5/02
FT OTAS	Ohio Taxpayers' Affiliation Schedule	12/04
FT EXPORT	Corporation Franchise Tax Credit for Increasing Export Sales	12/99
FT 1120FI	Corporation Franchise Tax Report for Financial Institutions	12/04
FT 1120S	Notice of S Corporation Status	12/04
FT REF	Application for Corporation Franchise Tax Refund	12/02
FT PR	Petition for Reassessment	11/02
FT HELP	Special Handling Notice	11/04
FT QHC	Qualifying Holding Company Election	No revisions
FT ELECTRIC	Supplemental Schedules for Electric Companies	12/04
FT TELCO	Supplemental Schedule for Local Exchange Telephone Companies	12/04

Rank	Nonrefundable Credit	Carryforward Period	O.R.C. Section
1.	Credit for Taxes Paid by a Qualifying Pass-Through Entity	Unlimited*	5733.0611
2.	Credit for Qualifying Affiliated Groups (due to Related Entity and Related Member Adjustments)	Not Applicable	5733.068
3.	Credit for Recycling and Litter Prevention Donations	None	5733.064
4.	Credit for Maintaining Railroad Crossing Warning Devices	None	5733.43
5.	Job Retention Credit	Three years	5733.0610(B) & 122.171
6.	Second Credit for Purchases of New Manufacturing Machinery and Equipment (7.5 Percent/13.5 Percent Credit)	Three years	5733.33
7.	Job Training Credit	Three years	5733.42
8.	Credit for Qualified Research Expense	Seven years	5733.351
9.	Credit for Eligible New Employees in an Enterprise Zone	Three years	5709.66
10.	Credit for Eligible Costs Associated with a Voluntary Action (Brownfield Site Clean-Up)	Three years	5733.34 & 122.19
11.	Credit for Employers that Establish On-site Child Day-care Centers (no new credit – carryforward amounts only)	Five years	5733.37
12.	Ethanol Plant Investment Credit	Three years	5733.46 & 901.13
13.	Credit for Grape Production Property	Seven years	5733.32
14.	Export Sales Credit (no new credit – carryforward amounts only)	1994-2005	5733.069
15.	Technology Investment Credit (formerly known as the Edison Center Credit for Research and Development Investors)	Fifteen years	5733.35, 122.15, 122.151, 122.152, 122.153 & 122.154
16.	Enterprise Zone Daycare and Training Credits	Unlimited*	5709.65(A)
17.	Research and Development Loan Repayment Credit	Unlimited*	5733.352 & 166.17 thru 166.21
*Unused credit amounts may be carried forward until fully utilized.			

## Second Credit for Purchases of New Manufacturing Machinery and Equipment (O.R.C. Section 5733.33)

Calendar year in which qualifying equipment is purchased	Franchise tax years (report years) in which 1/7 credit amounts are claimed																										
	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017	2018	2019	2020	2021	2022	
7/1/95 – 12/31/95	1/7	1/7	1/7	1/7	1/7	1/7	1/7																				
	1/7	1/7	1/7	1/7	1/7	1/7	1/7																				
1996		1/7	1/7	1/7	1/7	1/7	1/7	1/7																			
1997			1/7	1/7	1/7	1/7	1/7	1/7	1/7																		
1998			1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7																	
1999				1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7																
2000					1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7															
2001						1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7														
2002							1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7													
2003								1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7												
2004									1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7											
2005										1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7										
2006											1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7									
2007												1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7								
2008													1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7							
2009														1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7						
2010															1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7					
2011																1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7				
2012																	1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7			
2013																		1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7		
2014																			1/7	1/7	1/7	1/7	1/7	1/7	1/7	1/7	
2015																					1/7	1/7	1/7	1/7	1/7	1/7	1/7

**Note:** The taxpayer claims 1/7 of the credit in each of the seven years following the purchase year. Each 1/7 credit amount that is not used in the year in which it otherwise could have been claimed may be carried forward for three years. The unused carryforward amount is used before the 1/7 amount for the subsequent year.

Calendar Year of Purchase	Base Years
7/1/95 – 12/31/95	1992, 1993, 1994
1996	1992, 1993, 1994
1997	1992, 1993, 1994
1998	1992, 1993, 1994
1999	1992, 1993, 1994
2000	1993, 1994, 1995
2001	1994, 1995, 1996
2002	1995, 1996, 1997
2003	1996, 1997, 1998
2004	1997, 1998, 1999
2005	1998, 1999, 2000
2006	1999, 2000, 2001
2007	2000, 2001, 2002
2008	2001, 2002, 2003
2009	2002, 2003, 2004
2010	2009, 2010, 2011

- The taxpayer must claim 1/7 of the credit in each of the seven years following the purchase year. Each 1/7 credit amount that can not be used in the year in which it otherwise could have been claimed may be carried forward for three years. The amount carried forward is used before the 1/7 amount for the subsequent year.
- The credit is separately computed for each Ohio county for each purchase year;
- The credit is based upon purchases of qualifying equipment during a calendar year (the purchase year) even if the taxpayer has a fiscal year end;
- For purchases after 12/31/00 a "qualifying controlled group" must compute the credit on a consolidated basis for each county. For purchases on or before 12/31/00 a qualifying controlled group can elect to compute a consolidated credit for each county;
- If before the end of the seven year period over which the taxpayer claims the credit the taxpayer sells the equipment or moves it out of the county for which it claims the credit and the equipment is not fully depreciated, the remaining 1/7 credit amounts are lost;
- A pass-through entity (PTE) does not compute the credit. Instead, a PTE's qualifying purchases and base investment flow through to the PTE's investors, each of whom computes the credit.



Bonus Depreciation and/or I.R.C. Section 179 Add-Back Years and Deduction Years												
Add-Back Tax Year*	Franchise Tax Years (Report Years) during which 1/5 of the Bonus Depreciation and/or I.R.C. section 179 Add-Back is Deducted											
	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014
2002	1/5	1/5	1/5	1/5	1/5							
2003		1/5	1/5	1/5	1/5	1/5						
2004			1/5	1/5	1/5	1/5	1/5					
2005				1/5	1/5	1/5	1/5	1/5				
2006					1/5	1/5	1/5	1/5	1/5			
2007						1/5	1/5	1/5	1/5	1/5		
2008							1/5	1/5	1/5	1/5	1/5	
2009								1/5	1/5	1/5	1/5	1/5
* The “add-back tax year” is the franchise tax report year in which the taxpayer added back 5/6 of the I.R.C. section 168(k) bonus depreciation amount and/or 5/6 of the taxpayer’s “qualifying section 179 depreciation expense.”												

1972-2005 Schedule of Franchise Tax Rates, Litter Tax Rates, Interest and Penalty

Franchise Tax Year	Taxable Year Ending On or Between Dates Shown	Franchise Tax Rate			Surtax	Schedule K's Litter Tax Rates					Interest Rate	Addition to Tax Penalty
		Franchise Tax Rate				Tier One		Tier Two				
		Net Income Basis		Net Worth Basis		Net Income Basis		Net Worth Basis	Net Income Over \$50,000 (Over \$25,000 prior to 1989 Report)			
		First \$50,000 (First \$25,000 prior to 1989 Report)	Over \$50,000 (Over \$25,000 prior to 1989 Report)			First \$50,000 (First \$25,000 prior to 1989 Report)	Over \$50,000 (Over \$25,000 prior to 1989 Report)					
1972-1979	Prior to 1979	\$ 50	4.0%	8.0%	0.005	N/A	N/A	N/A	N/A	N/A	6%	25%
1980	1/01/79-12/31/79	\$ 50	4.0%	8.0%	0.005	N/A	N/A	N/A	N/A	N/A	6%	25%
1981	1/01/80- 7/14/80	\$ 50	4.0%	8.0%	0.005	N/A	N/A	N/A	N/A	N/A	6%	25%
	7/15/80-12/18/80	\$ 50	4.0%	8.0%	0.005	N/A	0.0022	0.0022	0.00014	0.0022	6%	25%
1982	12/19/80-12/13/80	\$ 50	4.0%	8.0%	0.005	15%	0.0011	0.0022	0.00014	0.0022	6%	25%
	1/01/81-11/14/81	\$ 50	4.0%	8.0%	0.005	15%	0.0011	0.0022	0.00014	0.0022	6%	25%
	11/15/81-12/18/81	\$150	4.6%	8.7%	0.0055	0	0.0011	0.0022	0.00014	0.0022	6%	25%
	12/19/81-12/31/81	\$150	4.6%	8.7%	0.0055	20.75%	0.0011	0.0022	0.00014	0.0022	6%	25%
1983	1/01/82-12/31/82	\$150	4.6%	8.7%	0.0055	5.75%	0.0011	0.0022	0.00014	0.0022	10%	25%
1984	1/01/83- 6/30/83	\$150	4.6%	8.7%	0.0055	5.75%	0.0011	0.0022	0.00014	0.0022	9%	25%
	7/01/83-12/31/83	\$ 50	5.1%	9.2%	0.00582	5.4%*	0.0011	0.0022	0.00014	0.0022	9%	25%
1985	1/01/84-12/31/84	\$ 50	5.1%	9.2%	0.00582	5.4%*	0.0011	0.0022	0.00014	0.0022	9%	25%
1986	1/01/85-12/31/85	\$ 50	5.1%	9.2%	0.00582	5.4%*	0.0011	0.0022	0.00014	0.0022	8%	25%
1987	1/01/86-12/31/86	\$ 50	5.1%	9.2%	0.00582	2.7%*	0.0011	0.0022	0.00014	0.0022	6%	25%
1988	1/01/87-12/31/87	\$ 50	5.1%	8.9%	0.00582	N/A	0.0011	0.0022	0.00014	0.0022	10%	See Note **
1989	1/01/88-12/31/88	\$ 50	5.1%	8.9%	0.00582	N/A	0.0011	0.0022	0.00014	0.0022	11%	Below
1990	1/01/89-12/31/89	\$ 50	5.1%	8.9%	0.00582	N/A	0.0011	0.0022	0.00014	0.0022	11%	
1991	1/01/90-12/31/90	\$ 50	5.1%	8.9%	0.00582	N/A	0.0011	0.0022	0.00014	0.0022	11%	
1992	1/01/91-12/31/91	\$ 50	5.1%	8.9%	0.00582	N/A	0.0011	0.0022	0.00014	0.0022	10%	
1993	1/01/92-12/31/92	\$ 50	5.1%	8.9%	0.00582	N/A	0.0011	0.0022	0.00014	0.0022	7%	
1994	1/01/93-12/31/93	\$ 50	5.1%	8.9%	0.00582	N/A	0.0011	0.0022	0.00014	0.0022	7%	
1995	1/01/94-12/31/94	\$ 50	5.1%	8.9%	0.00582	N/A	0.0011	0.0022	0.00014	0.0022	9%	
1996	1/01/95-12/31/95	\$ 50	5.1%	8.9%	0.00582	N/A	0.0011	0.0022	0.00014	0.0022	9%	
1997	1/01/96-12/31/96	\$ 50	5.1%	8.9%	0.00582	N/A	0.0011	0.0022	0.00014	0.0022	9%	
1998	1/01/97-12/31/97	\$ 50	5.1%	8.9%	0.00582	N/A	0.0011	0.0022	0.00014	0.0022	9%	
1999	1/01/98-12/31/98	\$ 50	5.1%	8.5%	0.004	N/A	0.0011	0.0022	0.00014	0.0022	8%	
2000	1/01/99-12/31/99	\$ 50	5.1%	8.5%	0.004	N/A	0.0011	0.0022	0.00014	0.0022	8%	
2001	1/01/00-12/31/00	\$ 50	5.1%	8.5%	0.004	N/A	0.0011	0.0022	0.00014	0.0022	9%	
2002	1/01/01-12/31/01	\$ 50	5.1%	8.5%	0.004	N/A	0.0011	0.0022	0.00014	0.0022	7%	
2003	1/01/02-12/31/02	\$ 50	5.1%	8.5%	0.004	N/A	0.0011	0.0022	0.00014	0.0022	6%	
2004	1/01/03-12/31/03	\$1,000 or \$50***	5.1%	8.5%	0.004	N/A	0.0011	0.0022	0.00014	0.0022	4%	
2005	1/01/04-12/31/04	\$1,000 or \$50***	5.1%	8.5%	0.004	N/A	0.0011	0.0022	0.00014	0.0022	5%	

\*Effective for taxable years ending after 6/30/83, the surtax is only applicable if the net income basis exceeds the net worth basis.

\*\*For each month or fraction of a month that the Ohio Corporation Franchise Tax Report (form FT-1120) was delinquent, the corporation is liable for the Failure to File (or timely file) penalty. This penalty is the greater of \$50 per month up to \$500 or 5% per month (50% maximum) of the net tax due shown on the delinquent report. All delinquent reports, including reports which (1) indicate an overpayment or no balance due or (2) an informational report (FT-1120S), are subject to the "Failure to File" penalty.

In addition to the above penalty, there is also a penalty for failure to pay (or timely pay) the tax computed on the delinquent report. The penalty is not to exceed 15% of the delinquent payment.

For additional information on delinquencies, please contact the office on the delinquency notice.

\*\*\*Effective for taxable years ending after June 25, 2003, the minimum fee is \$1,000 if (1) the sum of the taxpayer's gross receipts from activities within and without Ohio during the taxable year equals or exceeds \$5 million, or (2) the total number of the taxpayer's employees within and without Ohio during the taxable year equals or exceeds 300.

For more information, see instructions on the department's web site at [www.tax.ohio.gov](http://www.tax.ohio.gov).

# Taxpayer Assistance

## By Internet



**Ohio Department of Taxation**  
**Internet Web site – [www.state.oh.us/tax/](http://www.state.oh.us/tax/)**

**Tax Forms**  
**Instructions**  
**Information Releases**  
**E-mail us**

## By Phone



### **Toll Free Telephone Numbers:**

Toll Free **Business Taxpayer Service** 1-888-405-4039  
Toll Free **Form Requests** 1-800-282-1782  
Toll Free **Registration Unit** 1-888-405-4089

## Written



### **Ohio Department of Taxation** **Taxpayer Services Mailing Address:**

Ohio Department of Taxation  
Taxpayer Services Division  
Taxpayer Services Contact Center  
P.O. Box 182382  
Columbus, Ohio 43218-2382

## Walk-in



### **Ohio Department of Taxation** **Taxpayer Service Locations:**

**Taxpayer Service Center Hours**  
Office hours: 8:00 a.m. – 5:00 p.m.  
Monday through Friday  
***See location listing in next column.***

### **Ohio Department of Taxation** **Taxpayer Service Centers**

**Akron Taxpayer Service Center**  
161 S. High St., Suite 501  
Akron, OH 44308-1600

**Cincinnati Taxpayer Service Center**  
900 Dalton Ave. at W. 8th St.  
Cincinnati, OH 45203-1171

**Cleveland Taxpayer Service Center**  
615 W. Superior Ave.  
Fifth Floor, Rm. 570  
Cleveland, OH 44113-1891

**Columbus Taxpayer Service Center**  
800 Freeway Drive North  
Columbus, OH 43229  
**OR**

30 East Broad St., 20th Floor  
Columbus, OH 43215

**Dayton Taxpayer Service Center**  
Centre City Offices  
40 S. Main St., 5th Floor  
Dayton, OH 45402-2043

**Toledo Taxpayer Service Center**  
One Gov't. Center, Suite 1400  
Toledo, OH 43604-2232

**Youngstown Taxpayer Service Center**  
242 Federal Plaza West, Suite 402  
Youngstown, OH 44503-1294

**Zanesville Taxpayer Service Center**  
601 Underwood St.  
Zanesville, OH 43701-3786

**For the Deaf, Hearing Impaired or Speech Impaired Who Use TTY or TDD Only:** Please contact the Ohio Relay Service at 1-800-750-0750 and give the communication assistant the Department of Taxation phone number that you wish to contact.

**Volunteer Tax Assistance Program (VITA) and Tax Counseling for the Elderly (TCE):** These programs help older, disabled, low-income and non-English speaking people fill in their state and federal returns. For locations in your area, call the Internal Revenue Service at 1-800-829-1040. If you received an Ohio and/or federal income tax package in the mail, take them with you when you go for help.