

Sales and Use Tax Amendments

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No legislative session in Ohio would be complete without some effort to amend the sales tax law, and the recent general session of the 99th General Assembly was no exception. The legislative answer to the recommendations of the Tax and Revenue Study Commission¹ and of the Governor was the Mechem bill which made substantial changes in the law but did not alter its fundamental character.²

The widespread interest in this piece of legislation can best be understood against the background of the recommendations of the Tax and Revenue Study Commission. In substance, it recommended the substitution of what was popularly called a "gross sales tax" for our present prepaid consumers' sales tax. Actually, its recommendation contemplated the retention in substance of the present sales tax structure, but the abolition of the prepaid tax receipts system. With the abolition of the prepaid tax receipts or coupons there would have been eliminated the vendors' discount,³ commissions to the Treasurer's agents⁴ and redemption of tax coupons by religious and charitable organizations.⁵

There can be no valid administrative objections whatever to the substitution of a gross sales tax for Ohio's present sales tax system, provided the substitute is a true gross sales tax and provided greatly increased appropriations also are made available for administrative and enforcement purposes. Under a gross sales tax, however, the term "gross" has tremendous significance and must not be ignored. It means that the tax is applied to all, or substantially all, sales and not to selected transactions. By this test, the Study

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¹ A fifteen-member tax and revenue study commission was created by the 98th General Assembly with instructions to study the tax and revenue system of the state and to submit its report by January 15, 1951. Am. Sen. Bill No. 42, effective October 28, 1949.

² Am. Sen. Bill No. 111, amending Sections 5546-2, 5546-5, 5546-8, 5546-26a and 6290-5 of the Ohio General Code. This bill was presented to the Governor on May 8, 1951, and was neither signed nor returned to the Senate wherein it originated within ten days after being so presented, exclusive of Sundays and the day it was presented. The bill was filed in the office of the Secretary of State on May 22, 1951 and, being a law providing for a tax levy, it became immediately effective in accordance with Article II, Section 1d of the Ohio Constitution.

³ OHIO GEN. CODE § 5546-8.

⁴ OHIO GEN. CODE § 5546-7.

⁵ OHIO GEN. CODE § 5546-26a.

Commission had not recommended a gross sales tax at all. It would have eliminated the stamp or coupon system, but would have retained practically all the numerous exemptions which in fact have constituted our law a selective sales tax as distinguished from a gross sales tax. Herein existed the administrative weakness of its proposal.

It may be argued, and it is readily admitted, that the coupon system is an expensive device in tax administration. It may also be argued that the Department of Taxation, in all likelihood, might make better use in an expanded field audit program of money now expended for the coupon system. It would be folly, however, to conclude that the mere abandonment of the stamp system, and nothing more, would result in increased revenues to the state.

Under a sales tax law such as ours which, in addition to at least fifteen specific exemptions,⁶ excepts sales to farmers, manufacturers, processors, public utilities, merchants, and other commercial and industrial users,⁷ a variety of enforcement devices is both necessary and desirable. We have three such devices under our existing law: audit of vendors' records and assessment of tax deficiencies thus disclosed;⁸ prosecution of vendors who, among other things, fail to deliver prepaid tax receipts to consumers;⁹ and redemption of prepaid tax receipts which are surrendered primarily by religious and charitable organizations.¹⁰

All of these enforcement devices have been employed in the past by the Tax Commissioner; yet, under the Study Commission's proposal, both the second and third devices would have been discarded and the Tax Commissioner confined to audits as the sole means of enforcement. An audit program would be sufficient under a true gross sales tax. It is likely to be inadequate, however, under a law containing numerous exemptions or exceptions.

The reasons for this view are simply stated. There are approximately 240,000 licensed vendors in the State of Ohio—almost a quarter of a million. The maximum number of audits the Department has been able to make in one year with legislative appropriations available was about 8,000. We have a four year statute of limitations.¹¹ This means that under the most favorable circumstances the Department has been able to audit at the rate of but 32,000 of the 240,000 licensed vendors within the statutory period

⁶ OHIO GEN. CODE § 5546-2.

⁷ OHIO GEN. CODE § 5546-1.

⁸ OHIO GEN. CODE §§ 5546-9a, 5546-9b, 5546-9c, 5546-12, 5546-12a and 5546-12b.

⁹ OHIO GEN. CODE §§ 5546-13, 5546-13a, 5546-13b, 5546-15, 5546-16 and 5546-17.

¹⁰ OHIO GEN. CODE § 5546-26a.

¹¹ OHIO GEN. CODE § 5546-9d.

open for audit. Now, of course, it is unnecessary and impractical to have an audit force that would enable the Department to check every taxpayer within the statute of limitations. A very large proportion of business is done by little more than half the licensed vendors and, in general, the concentration of the audit program must be in that sector. But even if a greatly enhanced audit force were provided in Ohio, the elimination of tax coupons would not necessarily be justified, because it is the existence of the exemptions in our law which really complicates and slows down the process of auditing. So long as these exemptions remain, enforcement devices in addition to auditing are advantageous. Prosecution of vendors for failure to issue coupons as well as redemption of coupons are important additional enforcement devices under a selective sales tax law.

It should be emphasized that the abolition of the coupon system alone will not assure an increased yield from the Ohio sales tax. The yield of our tax, when broken down on a per capita level rate basis, is substantially lower than that of other large states where comparable economic conditions prevail. The per capita yield of each 1% of tax in each of the states indicated below was reported by the Federation of Tax Administrators¹² as follows:

California	10.57
Illinois	9.58
Iowa	10.54
Michigan	10.69
Ohio	5.58

The primary reason for this low yield in Ohio is the existence of more numerous exemptions under our law. Consequently, even under a sales tax system which excludes coupons the yield of the Ohio tax would be substantially lower than that of comparable states because of the restricted nature of the sales tax base in Ohio.

An added reason for the low per capita yield in Ohio is the lack of sufficient auditors or examiners. The most effective part of a sales tax organization for insuring compliance with the law is the field audit staff. There is considerable variation among the states in the relative size of the staffs maintained, much of the difference being due to the reluctance of legislatures to appropriate sufficient funds. The following table, also compiled by the Federation of Tax Administrators, shows the relationship between licensed vendors and audit staff work-loads in the five states above referred to:

¹² Special report prepared for the Tax Commissioner of Ohio, dated January 26, 1951, and not published for general distribution. The Federation of Tax Administrators is the official organization of tax administrators in the several states and has its offices at 1313 East 60th Street, Chicago, Illinois.

	<i>Accounts per Auditor</i>
California	307
Illinois	1074
Iowa	1030
Michigan	556
Ohio	1533

It is an interesting fact, and incidentally a good illustration of the way in which expenditures can be channelled into the most productive activities, that sufficient field auditors can be maintained in California to service approximately 275,000 accounts (1950 estimate) on a basis of one auditor for every 300 (a ratio five times the coverage reported for Ohio) at an annual cost of about \$4,500,000. This sum is only about \$900,000 more than the auxiliary costs of the coupon system in Ohio (agents' fees, redemption, printing). In the last fiscal year this field audit program in California produced deficiency assessments of \$9,758,950. The total amount of tax assessed as the result of both office and field audit programs together was \$10,648,485. The predominance of the field audit program is thus emphasized.¹³

The foregoing views, of course, are those of the writer and do not constitute an argument either for or against the coupon system of sales tax administration. It was and is his conclusion that if the General Assembly should decide to abolish the coupon system it should also abolish substantially all, if not all,¹⁴ exemptions now in our law; that if the General Assembly should decide to retain existing exemptions, or substantially all of them, it should also retain the coupon system; and, in either case, that it should provide sufficient funds to finance an adequate field audit program. After all, an adequate audit program is the best means of securing uniform and consistent taxpayer compliance; and we should never forget that where appropriations for an adequate audit program are not available, the honest and conscientious vendor as well as the public do not receive the protection to which they are entitled.

Whether the General Assembly was conscious of the foregoing considerations or not, the fact remains that it did not choose to adopt the recommendations of the Tax and Revenue Study Commission which, as pointed out, fell short of a true gross sales tax law. Instead, it enacted certain amendments designed to increase the yield of the sales and use taxes and to make possible more adequate enforcement of the law.

¹³ *Ibid.*

¹⁴ The General Assembly is undoubtedly powerless to remove the food exemption contained in Ohio General Code Section 5546-2(2) because of constitutional limitations. Article XII, Section 12 of the Constitution of Ohio provides that "On and after November 11, 1936, no excise tax shall be levied or collected upon the sale or purchase of food for human consumption off the premises where sold."

The first amendment of consequence pertains to the casual sale of motor vehicles. Prior to the amendment, the sales tax law exempted casual and isolated sales by a vendor who is not engaged in the business of selling tangible personal property.¹⁵ A similar exemption existed under the use tax act.¹⁶ The amendment provides that these exemptions shall not apply to casual and isolated sales of motor vehicles and house trailers.¹⁷

Heretofore, as a means of enforcing compliance with the tax law in respect of the sale of automobiles other than casual sales, the statute provided that the clerk of courts shall refuse to accept for filing any application for certificate of title and shall refuse to issue certificate of title when the motor vehicle was transferred in the State of Ohio unless prepaid tax receipts were presented with the application.¹⁸ This provision of law was amended to permit the applicant in appropriate cases to submit with the application payment of the tax by cash, certified check, draft or money order payable to the clerk of courts who is required to issue a receipt therefor in the form prescribed by the Tax Commissioner. Such receipts are deemed to be consumers' portions of prepaid tax receipts for the purposes of the statute and are subject to redemption in the same manner and at the same rate as therein provided with respect to the redemption of consumers' portions of prepaid tax receipts.¹⁹ This amendment was designed to adapt existing law to the casual sale of motor vehicles and house trailers.

Likewise, in respect of the casual sale of motor vehicles and house trailers, the new tax provides that the purchase price for the purpose of determining the tax by the clerk of courts shall be the purchase price on an affidavit executed and filed with the clerk of courts by the vendee and shall be prima facie evidence of the amount for the purpose of determining the tax, in a form to be prescribed by the Tax Commissioner.²⁰

¹⁵ OHIO GEN. CODE § 5546-2(7).

¹⁶ OHIO GEN. CODE § 5546-26(3).

¹⁷ OHIO GEN. CODE § 5546-2(7), Am. Sen. Bill No. 111, § 1. Ohio General Code Section 5546-26(3) was not rewritten but a provision was inserted in the amendment of Section 5546-2 to the effect that Section 5546-26(3) shall not apply to the purchase of motor vehicles or house trailers for storage, use or other consumption in this state. It would have been better legislative form to have added this language to Section 5546-26(3) directly.

¹⁸ OHIO GEN. CODE § 6290-5.

¹⁹ OHIO GEN. CODE § 6290-5, Am. Sen. Bill No. 111, § 1. The Tax Commissioner, under date of May 29, 1951, revised Rule No. 143 to provide for remittances to the Treasurer of State of sales and use taxes collected under this section of the law as amended.

²⁰ *Ibid.* The Tax Commissioner has promulgated appropriate forms for this purpose and the Division of Sales and Excise Taxes has issued circular instructions with reference thereto.

In order to relieve the casual sale vendor of the requirements of law as to vendors' licenses and semi-annual returns,²¹ the amendment provides that when the vendor is not regularly engaged in the business of selling motor vehicles or house trailers he shall not be required to purchase a vendor's license or make reports for and concerning such sales.²²

For his services in receiving and disbursing sales and use taxes paid to him, the clerk of courts, under the new law, is allowed to retain a poundage fee of 1%, to be paid into the general fund of the county.²³

The second legislative amendment of substance provides that the Tax Commissioner shall employ a sufficient number of auditors for the purpose of auditing vendors' sales tax accounts and records, not fewer in number than one auditor for each one thousand vendors' certificates (licenses) outstanding.²⁴ This requirement falls short of the prevailing policy in California and Michigan, as heretofore shown, but it does place Ohio in line with Illinois and Iowa and represents a decided step forward in enforcement policy. Of course, the requirement is and will continue to be subject to legislative appropriations. It is the writer's belief, however, that this new provision, if faithfully observed, will mean much more to the state by way of increased revenue than the provision for taxing casual sales of motor vehicles or any other provision of the new law.

The third amendment was directly designed to reduce administrative costs incident to the prepaid tax receipt system. Heretofore, the law has provided for the sale of prepaid tax receipts to licensed vendors by the treasurer of state, his agents, and the county treasurer at a discount of not to exceed three per centum of the face value thereof, as a commission for handling and cancelling such prepaid tax receipts; but, under the amendment, this discount was cut to two per centum.²⁵

Finally, the General Assembly sought to tighten the law by preventing abuse of its provisions for redemption of prepaid tax receipts. The statute has provided that no redemption of consumers' portions of prepaid tax receipts shall be made when presented by a vendor or seller, and the amendment restricts this prohibition by adding the words "directly or indirectly".²⁶ The Department of

²¹ OHIO GEN. CODE §§ 5546-10 and 5546-12b.

²² OHIO GEN. CODE § 6290-5, Am. Sen. Bill No. 111, § 1. Again it would have been better legislative form to have amended the appropriate sections of the sales tax law.

²³ OHIO GEN. CODE § 6290-5, Am. Sen. Bill No. 111, § 1.

²⁴ OHIO GEN. CODE § 5546-5, Am. Sen. Bill No. 111, § 1.

²⁵ OHIO GEN. CODE § 5546-8, Am. Sen. Bill No. 111, § 1.

²⁶ OHIO GEN. CODE § 5546-26a, Am. Sen. Bill No. 111, § 1.

Taxation has always so construed the law as a matter of administrative policy, and hence the amendment merely carries that administrative policy into statutory law.

In the interest of completeness, it should be pointed out in closing that the General Assembly, by separate enactment, amended the provisions of the sales tax act pertaining to the "local government fund" which is made up of monies derived from sales tax revenues in amounts specifically credited by the General Assembly.²⁷ This enactment credits to the fund twelve million dollars for the year beginning July 1, 1951 and eighteen million dollars for the year beginning July 1, 1952. It also contains a section providing for the distribution to local governments and school districts, in amounts of 30 per cent each, of any net collection of revenues accruing to the general revenue fund of the state during the fiscal year 1950-51 in excess of estimated revenues, exclusive of educational bequests and miscellaneous and student fees, in the amount of \$260,357,000.²⁸

²⁷ Am. Sub. House Bill No. 605, amending Sections 5546-18 and 5546-20 of the General Code. This bill was approved by the Governor on June 13, 1951, and was filed in the office of the Secretary of State on June 14, 1951. By specific provision written into the Act, however, it became effective on July 1, 1951.

²⁸ Am. Sub. House Bill No. 605, § 2.