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II

Ohio Personal Property Tax

Kenneth G. Humer

THE SUBJECT OF personal property taxation contains three major areas of interest for the tax attorney: (1) the method of computation of the personal property tax; (2) the procedure available to the taxpayer for claiming a reduction in his tax basis; and (3) the advantages obtainable through the so-called federal election. It is the purpose of this article to analyze these areas of concern and to give special emphasis to the important recent developments in each area.

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I. COMPUTATION OF THE PERSONAL PROPERTY TAX

A. *Rate of Taxation*

All personal property located and used in business in Ohio is subject to taxation.¹ Generally, tangible personal property is listed and assessed at seventy per cent of its "true value in money," while personal property used in business is listed and assessed at fifty per cent of its "true value in money."²

Personal property is "used" within the meaning of "used in business" when (1) it is employed or utilized in connection with ordinary or special operations; (2) it is acquired or held as a means or instrument for carrying on the business; (3) it is kept and maintained as a part of a plant capable of operation; or (4) it is stored or kept on hand as material, parts, products, or merchandise.³

B. *Tax Basis*

Generally, the basis used for the taxation of property in Ohio has been the property's true value in money. The true value of personal property has usually been equated to the full cash value of the property. In addition to the problems surrounding the com-

¹ OHIO REV. CODE § 5709.01.

² OHIO REV. CODE § 5711.22.

³ OHIO REV. CODE § 5701.08(A).

putation of the full cash value of a chattel or intangible, recent attacks on this mode of computation have raised questions even as to its constitutionality.

(1) *True Value in Money*.—Historically, tangible personal property has been assessed for tax purposes at fixed percentages of full cash value, whereas land and improvements thereon have been taxed by uniform rule according to value.⁴ Prior to 1965, the Ohio Revised Code provided that the "auditor shall assess all the real estate situated in the county at its true value in money."⁵ In applying this statutory provision, it has become customary for auditors to assess real property at approximately forty per cent of its alleged true value in money.

Since the Ohio Constitution confined the traditional uniformity rule to real estate, it impliedly permitted classification of personal property. As a result, provisions were made for assessing various classes of tangible personal property at fixed percentages of true value in money of either fifty or seventy per cent.⁶ Until recently, no truly direct attack had been made upon this method of valuation. However, the Ohio Supreme Court has recently rendered a decision in a case which challenged the present method of assessing personal property.⁷

In *Continental Can Co. v. Schneider*,⁸ the appellant company included with its 1963 return a claim for deduction from book value. By this claim it sought, for purposes of taxation, to have its taxable tangible personal property valued at forty per cent of its net depreciated book value. This percentage was the approximate statewide average ratio between assessed valuations for real property tax purposes and market values, as determined by the Ohio Board of Tax Appeals in sales ratio studies conducted by it. To the value thus determined, Continental then applied either the fifty per cent or seventy per cent rate, with the result that certain property was listed for taxation at twenty to twenty-eight per cent of true value.

Continental's claim was disallowed, and the property was assessed

⁴ OHIO CONST. art. XII, § 2.

⁵ OHIO REV. CODE § 5713.01. In November, 1965, this section was amended twice. It now reads, in part: "The auditor shall assess all the real estate situated in the county at its taxable value in accordance with sections 5713.03 and 5715.01. . . ." OHIO REV. CODE § 5713.01 (Supp. 1965).

⁶ OHIO REV. CODE § 5711.22.

⁷ *Continental Can Co. v. Schneider*, 3 CCH STATE TAX REP. *Ohio* ¶ 200-603 (B.T.A. 1965), *aff'd sub nom.*, *Continental Can Co. v. Donahue*, 5 Ohio St. 2d 224, 215 N.E.2d 400 (1966).

⁸ *Ibid.*

at fifty to seventy per cent of its true value in money. The company filed an application for review and redetermination, in which it made four major contentions. It urged, first, that the owners of real and personal property had been placed by the legislature in the same statutory class for purposes of taxation, since "true value in money" was the criterion employed to describe the basic measure of assessment for both types of property. It therefore concluded, second, that the company should have been assessed at the same percentage of "true value in money" as the owners of real property. Third, it alleged that the systematic practice by tax authorities of using different percentages of full "true value in money" in arriving at assessable valuations for purposes of real and personal property taxation was discriminatory and unconstitutional. Finally, the company emphasized that the Tax Commissioner has the statutory power and duty to assess the applicant's personal property at the same percentage of true value, *i.e.*, forty per cent, as prevails in the assessment of real property.

Thus, the essential issue raised in the *Continental Can Co.* case was whether the term "true value in money" should have the same meaning when it is applied to the valuation of tangible personal property for taxation purposes as it has when applied to real property.

At the hearing on Continental's application for review and redetermination, the Tax Commissioner found that, as an administrative official, he was forced to presume the validity and constitutionality of statutory enactments and was without authority to judge that issue.⁹ The company then perfected its appeal to the Ohio Board of Tax Appeals. The Board found that "tangible personal property" had been classified separately from real property by the legislature and that this classification was both reasonable and constitutional. It further pointed out that there is no constitutional requirement that real property be valued at its "true value in money," since this requirement is purely statutory.¹⁰ Without deciding the question of whether the uniformity rule is equally applicable to personal and real property, the Board held that the terminology "true value in money" is a constitutional term and that the failure of the statute to further define the term does not render the statute so vague

⁹ He relied on *S. S. Kresge v. Bowers*, 170 Ohio St. 405, 166 N.E.2d 139 (1960); *Risk & Co. v. Bowers*, 114 Ohio App. 429, 183 N.E.2d 786 (1961); *McCreary v. Bowers*, 106 Ohio App. 445, 155 N.E.2d 224 (1958).

¹⁰ *Carney v. Board of Tax Appeals*, 169 Ohio St. 445, 160 N.E.2d 275 (1959).

or indefinite as to be meaningless."¹¹ The Board, in effect, found that Continental had not shown that its property had been valued at more than its "true value in money." Thus, it sustained the Tax Commissioner and ignored the real issue. The Ohio Supreme Court, in affirming the decision of the Ohio Board of Tax Appeals, held that there was no violation of either the United States or the Ohio Constitutions.¹²

(2) *Calculation of Full Cash Value.*—"True value in money" in the case of machinery and equipment is ordinarily the taxpayer's depreciated book value. However, in many instances the Department of Taxation requires the taxpayer to use its own schedule of depreciation rates for valuation purposes. This schedule, known as a "302 Computation Directive," states that "in valuing equipment used in business, the Department of Taxation will adhere to the following composite depreciation rates. Such rates are *prima facie* only and are subject to adjustment in all cases where special or unusual circumstances or conditions of use are shown to exist."¹³

As a practical matter, even though these composite rates are *prima facie* only, the present policy of the Department of Taxation is to make their use mandatory by the examining agent. Thus, the taxpayer who uses rates for book purposes different from the "302 rates" can only obtain relief from strict observance of "302 rates" through a hearing before the Tax Commissioner or a court.

Since depreciation rates are predicated upon a taxpayer's experience, it is submitted that the requirement that an examining agent strictly adhere to the "302 rates" is not only arbitrary but has the effect of requiring the taxpayer to go through unnecessary procedural expense and delay in order to bring about those special circum-

¹¹ *Continental Can Co. v. Schneider*, 3 CCH STATE TAX REP. *Ohio* ¶ 200-603 (B.T.A. 1965), *aff'd sub nom.*, *Continental Can Co. v. Donahue*, 5 Ohio St. 2d 224, 215 N.E.2d 400 (1966).

¹² 5 Ohio St. 2d 224, 215 N.E.2d 400 (1966). The court stated in syllabus 3: The fact that *tangible personal* property is valued for tax purposes at full "true value in money," pursuant to Section 5711.22, Revised Code, whereas *real property* in the state is customarily assessed at a percentage of the statutorily required (true value in money) valuation as provided for by Section 5713.01, Revised Code, cannot be made the basis for a valid claim for a tax reduction by the owner of tangible personal property upon the ground that this constitutes a violation of the Fourteenth Amendment to the United States Constitution or Section 2 of Article I or Section 2 of Article XII of the Ohio Constitution. *Id.* at 225, 215 N.E.2d at 401.

¹³ Directive of Dep't of Taxation (July 1, 1965). A subcommittee of the taxation committee of the Ohio Bar has been appointed for the purpose of studying depreciation as it relates to personal property taxes, in the hope of achieving a more realistic approach to this problem.

stances that would result in a change in rate. In a judgment area such as this administrative rules should not be inflexible, and examining agents should be able to exercise independent judgment.

Although equipment is to be assessed at "true value in money," it cannot be depreciated below twenty per cent of original cost as long as the property is held for use in business.¹⁴ Where the "302" computation is being used and the taxpayer disposes of equipment used in business, the cost basis of acquisitions for the respective years is reduced. However, those taxpayers who do not account for disposals on an individual asset basis by eliminating the value of the unit sold from cost, but rather credit the sales proceeds to their reserve for depreciation account, will find themselves paying personal property taxes on equipment no longer in use. This result, while certainly not contemplated by the law, appears to be unavoidable, since the Board of Tax Appeals has held that the taxpayer's book-keeping methods must conform to the regulations imposed by the Tax Commissioner if the taxpayer wishes to secure the tax advantages which the law allows.¹⁵

In 1963, Ohio Revised Code section 5711.22(B) was amended to provide for the listing and assessment of personal property of merchants which is sold or held for sale for the use and consumption of purchasers, which is not for resale, and which must be returned on an average basis.¹⁶ Two tax categories were established — a lower one to include up to the first 100,000 dollars in value of the personal property, and a higher one to include all such property exceeding 100,000 dollars assessed at "true value in money." Certain percentages of true value in money were listed and assessed for each category.¹⁷

In *Kroger Co. v. Schneider*,¹⁸ the Kroger Company alleged that the aforementioned provisions resulted in unequal tax burdens which were conditioned upon the quantity of inventory owned by specific taxpayers. The company therefore claimed that these provisions

¹⁴ OHIO REV. CODE § 5711.22.

¹⁵ *Siebler Tailoring Co. v. Peck*, 1 CCH STATE TAX REP. *Ohio* § 20-326.37 (B.T.A. 1952).

¹⁶ *Kroger Co. v. Schneider*, 205 N.E.2d 603 (Ohio C.P. 1964), *rev'd*, 4 Ohio App. 2d 226, 212 N.E.2d 76 (1965) (syllabus).

¹⁷ As to personal property in the lower category, the following percentages of true value in money pertain: in 1964, 66%; in 1965, 62%; in 1966, 58%; in 1967, 54%; and in 1968 and each following year, 50%. As to personal property in the higher bracket, such property shall be uniformly listed and assessed at 70% of its true value in money, during the entire period. *Ibid.*

¹⁸ 205 N.E.2d 603 (Ohio C.P. 1964), *rev'd*, 4 Ohio App. 2d 226, 212 N.E.2d 76 (1965).

violated the constitutional guarantee of equal protection of the law. The Franklin County Court of Common Pleas found that "the Federal 'due process' and 'equal protection' clauses and the Ohio 'equal protection of law clause' all forbid a state from levying *any taxes directly on property* at graduated or progressive rates,"¹⁹ except as expressly allowed by other portions of the constitutions. As a result, section 5711.22(B) was declared void and unenforceable because it:

(a) imposes an unequal burden of taxation on like personal property, used for the same purpose, owned by taxpayers similarly situated, and engaged in the same types of enterprise; (b) it is a purported classification of taxpayers, not property; and (c) it is based upon an unreasonable and arbitrary classification not having any fair or substantial relation to the object of legislation. . . .²⁰

On appeal,²¹ the court found that the provisions of section 5711.22(B) did not violate the equal protection of the law guarantees of either the state or federal constitutions, were not unreasonable, capricious, or discriminatory, and did not impose an unjust burden of the cost of government upon taxpayers in either bracket or division.²² Thus, unless this decision is reversed by the Ohio Supreme Court, the method of listing and returning retail inventories will follow the statutory provisions of section 5711.22(B) and will be different from that of manufacturing inventories which are listed upon an average basis and assessed at fifty per cent of their true value in money.²³

With respect to inventories, it is important to note that new taxpayers who engage in business after the beginning of any taxable year are required to file a return within ninety days therefrom and to estimate the average value of inventory to be used in the business.²⁴ Too often, new taxpayers estimate the value of their inventories ultra-conservatively, with the result that the tax which is paid is considerably less than the amount that would have been paid had these figures been more realistically estimated.

In the case of *Doraty Rambler, Inc. v. Schneider*,²⁵ it was held that the Tax Commissioner may revise the estimates of taxable inventory values on the basis of actual experience. There the company had been engaged in the retail sale of used automobiles from

¹⁹ *Id.* at 605.

²⁰ *Id.* at 607.

²¹ *Kroger Co. v. Schneider*, 4 Ohio App. 2d 226, 212 N.E.2d 76 (1965).

²² *Id.* at 227, 212 N.E.2d at 77.

²³ OHIO REV. CODE § 5711.22(C).

²⁴ OHIO REV. CODE § 5711.03.

²⁵ *Doraty Rambler, Inc. v. Schneider*, 4 Ohio St. 2d 37, 212 N.E.2d 580 (1965).

1958 until May, 1960, at which time its inventory was liquidated, and the company moved from its location. In January, 1961, the company again engaged in the retail automobile business at a new location. In filing its corporate return of taxable personal property for 1961, it listed estimated monthly inventory values for that calendar year. Subsequently, it requested a refund based upon the use of actual inventory figures for the eight months (September, 1959 through April, 1960) of the preceding fiscal year to the time that operations were suspended. The Tax Commissioner, upon audit of Doraty's 1961 tax return, made his assessment based upon the actual inventory figures for the calendar year 1961. The Ohio Supreme Court found that a taxpayer is not entitled to use his prior year's inventory as his personal property tax basis unless such taxpayer was a "merchant" engaged in the same line of business on tax listing day.²⁶ Accordingly, it affirmed the action of the tax commissioner.

II. CLAIM PROCEDURE

Last year the Ohio legislature modified the procedure for a taxpayer's claim of a deduction from book value.²⁷ This was probably a result of the numerous claims for such a deduction.

As in the past, a taxpayer may claim a deduction from book value by filing a "902 claim" with the return. If the claim is disallowed, the taxpayer may file an application for review and redetermination within thirty days from the date on which the notice of disallowance was mailed.²⁸ Once the Commissioner has made a final determination, an appeal may be made to the Board of Tax Appeals.²⁹

Under the revised system, effective as of June 29, 1965, the taxpayer must pay the disputed tax.³⁰ If it is finally determined that this tax was not owed, the amount paid will be applied to any future taxes which may accrue or will be refunded. Thus, if a claim for deduction from depreciated book value for 1965 and 1966 has been denied, and an application for review and redetermination filed, the tax assessment will be made without the allowance.

It should be noted that timely application for review and redetermination by the taxpayer is essential. Failure to comply with the thirty-day time limitation will result in forfeiture of all legal rights

²⁶ *Id.* at 43, 212 N.E.2d at 584.

²⁷ OHIO REV. CODE § 5711.311 (Supp. 1965).

²⁸ OHIO REV. CODE § 5711.31.

²⁹ OHIO REV. CODE § 5717.02.

³⁰ OHIO REV. CODE § 5711.311 (Supp. 1965).

and remedies. The Ohio Department of Taxation has recently issued a notice which contains two samples of statements which may be submitted with, and inserted in, 1966 personal property tax returns. This should be done at the time of filing and will be accepted as a claim in writing in lieu of executed form 902.³¹

III. FEDERAL ELECTION

In listing intangible personal property, taxpayers have the right to elect to use the federal election form 912.³² This form includes a summary of the items reported for federal income tax purposes which are also taxable for Ohio personal property tax purposes. Use of this form involves certain definite disadvantages. Any taxpayer who elects to use the federal election form must continue to use that form for a period of not less than three years in listing his income-yielding investments. After the three-year period, if the taxpayer can show good cause, the Tax Commissioner may authorize a change in the filing method.³³ It should be noted, however, that the Department of Taxation has repeatedly refused to permit the change where the only reason given was that the taxpayer would save taxes if permitted to list separately investments yielding income. Therefore, it appears that the taxpayer will be permitted to change forms only if the amount of taxes would be approximately the same under both methods of computation.

Under certain circumstances, the use of the federal election does have advantages. For example, any security held for investment purposes that has not been outstanding for the entire year is treated as a non-productive investment, reported at its true value in money, and taxed at two mills on the dollar.³⁴ However, in the case of an individual taxpayer, if the federal election form is used, the taxpayer is not required to report the item as unproductive, provided he has received some income on that investment during the year.³⁵

This advantage will be offset, however, if the taxpayer choosing to use the federal election form owns shares of stock in a corporation electing not to be taxed pursuant to the provisions of Subchapter S of the Internal Revenue Code.³⁶ In essence, under these pro-

³¹ 39 OHIO BAR 497 (April 25, 1966).

³² Dept. of Taxation Rule No. 206, 1 CCH STATE TAX REP. *Ohio* § 21-022.

³³ OHIO REV. CODE § 5711.10 (Supp. 1965).

³⁴ OHIO REV. CODE § 5711.22(A).

³⁵ *Pickrel v. Bowers*, 3 CCH STATE TAX REP. *Ohio* § 200-490 (B.T.A. 1963).

³⁶ INT. REV. CODE OF 1954, §§ 1371-77.

visions, the entire amount of the income of the corporation is includable in the federal income tax return of the shareholder on the basis of his pro rata ownership of the corporation's stock. The Department of Taxation originally espoused the position that the total amount of this income, distributed or undistributed, constituted the income yield on the shares of stock in the Subchapter S corporation for personal property tax purposes.³⁷ Subsequently, as a result of the decision in *Michael v. Bowers*,³⁸ the Department of Taxation reversed its position and held that, under the ordinary listing method, only the amount paid is reported as income yield. However, where the taxpayer uses the federal election, the entire amount will be treated as yield for personal property tax purposes.

The federal election will also be disadvantageous to those taxpayers who receive income from patents and copyrights. If it is utilized in that situation, the entire amount of the royalty income must be reported as opposed to the necessity of reporting only a percentage thereof under normal circumstances.³⁹

IV. CONCLUSION

The importance of recent decisions in most of the areas discussed in this article makes it imperative that the tax attorney acquaint himself with these new developments. Of primary importance is an understanding of the effect which these decisions will have on Ohio personal property tax law.⁴⁰ Cases such as *Continental Can Co. v. Schneider*⁴¹ and *Kroger Co. v. Schneider*⁴² offer a continuing challenge to the ability of tax attorneys to adjust to the changes in the area of personal property taxation.

³⁷ Letter from Ohio Tax Commissioner, Nov. 14, 1958. See also 1 CCH STATE TAX REP. *Ohio* § 20-330.

³⁸ *Michael v. Bowers*, 174 Ohio St. 169, 187 N.E.2d 890 (1963).

³⁹ OHIO REV. CODE § 5701.10(G).

⁴⁰ It should be pointed out that claims for refund of federal income tax are also included within the definition of "other taxable intangibles." *Glidden Co. v. Glander*, 151 Ohio St. 344, 86 N.E.2d 1 (1949). In *Aeronca Mfg. Corp. v. Schneider*, 3 CCH STATE TAX REP. *Ohio* § 200-659 (1965), the issue presented was whether the "right" of the taxpayer to make a claim for a federal income tax refund at the close of the taxable year was includable as "other taxable intangibles." The Ohio Board of Tax Appeals found that if the manufacturer's refund claim had not been filed with the federal government on Ohio property tax assessment day, the amount of this claim must be included as "other taxable intangibles."

⁴¹ 3 CCH STATE TAX REP. *Ohio* § 200-603 (B.T.A. 1965), *aff'd sub nom.*, *Continental Can Co. v. Donahue*, 5 Ohio St. 2d 224, 215 N.E.2d 400 (1966).

⁴² 205 N.E.2d 603 (Ohio C.P. 1964), *rev'd*, 4 Ohio App. 2d 226, 212 N.E.2d 76 (1965).