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OHIO LEGISLATIVE SERVICE COMMISSION

Office of Research and Drafting

Legislative Budget Office

H.B. 157
134th General Assembly

Fiscal Note & Local Impact Statement

Click here for H.B. 157's Bill Analysis

Version: As Introduced

Primary Sponsors: Reps. Jordan and Edwards

Local Impact Statement Procedure Required: Yes

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Highlights

- The bill repeals a temporary rule governing the municipal income taxation of employees working at a temporary worksite – including their homes – due to the COVID-19 pandemic. The temporary rule allowed for employee income tax withholding to continue as it did before the Governor's emergency declaration of March 2020.
- The bill would likely have a fiscal impact on most municipalities, if the emergency declaration were still in place after the bill was enacted. The impact would vary considerably from one municipality to another, with many losing revenue, though some may be unaffected and some may gain revenue. Statewide, there would be a revenue loss, with losses potentially totaling several tens of millions of dollars, though losses would be more limited if the Governor's declaration expired soon after the bill became effective.

Detailed Analysis

The bill repeals a temporary rule governing the municipal income taxation of employees who are working at a temporary worksite – including their home – due to the COVID-19 pandemic. This temporary rule was enacted in Section 29 of H.B. 197 of the 133rd General Assembly and is set to expire 30 days after the end of the Governor's COVID-19 emergency declaration. If the bill has a fiscal effect, it would be on municipalities that levy an income tax; whether there would be such an effect depends entirely on when the Governor's declaration ends, which is unknown at the time of this writing. If there is a fiscal effect, there would be a net statewide revenue loss for municipalities, totaling potentially several tens of millions of dollars, depending on the timing of enactment. If the bill were enacted after the emergency declaration is lifted, the bill would have no fiscal impact.

In the following sections, this fiscal note will discuss current municipal income tax law, available information on pandemic-related commuting changes, and potential taxpayer savings from H.B. 157.

Municipal income tax law

Under codified law, a nonresident employee may work in a municipality for up to 20 days per year without the employer becoming subject to that municipality's tax withholding requirements and the employee becoming subject to that municipality's income tax. And if an employee does not exceed the 20-day threshold, that employee's pay is not counted toward the business's payroll factor, one of three factors – along with property and sales – that determines whether, and the extent to which, a firm's own income is subject to the municipality's tax on net profits.

Municipalities levy a municipal income tax on wages, salaries, and other compensation earned by residents of the municipality and by nonresidents working in the municipality, and on the net profits of businesses attributable to their activities in the municipality. Most municipalities allow a partial or full credit to residents for municipal income taxes paid to another municipality where they are employed. A few municipalities do not allow any credit, so residents of those municipalities who work in another municipality pay an additional tax to their place of residence. Administration of the municipal income tax is strictly local, either by the cities and villages themselves or by central collection agencies under contract with various municipalities. Businesses generally remit employees' withholding taxes to municipalities in which they do business. Businesses may also remit income tax withholding to their employees' municipality of residence, though that is not a requirement.[1]

In calendar year (CY) 2018, the latest data available from the Department of Taxation, 642 municipalities (242 cities and 400 villages) levied the tax. Municipal income tax collections statewide were estimated at $5.60 billion, ranging from approximately $9,715 in the village of Cecil (in Paulding County) to approximately $864.6 million in Columbus (Franklin).

Data on working from home (WFH)

Prior to CY 2020, estimates from the U.S. Census Bureau suggested that less than 4% of Ohio workers worked from home. The pandemic upended employment-related commuting patterns as many employees switched to WFH at the behest of governments and employers who implemented such policies. WFH is not uniformly available to all employers and employees, varying greatly by the type of work performed and the type of industry. In 2020, the share of employees able to work from home was estimated by the U.S. Bureau of Labor Statistics to be as

[1] Businesses operating in multiple municipalities may opt to remit taxes to the Department of Taxation which will distribute the amounts to the various cities. Under H.B. 49 of the 132nd General Assembly, firms may file one municipal net profit tax return through the Ohio Business Gateway. The tax department handles all administrative functions for those centrally filed returns and distributes payments to the appropriate municipalities.

high as 81% for the financial industry, to lows of 20% for leisure and hospitality.[2] Researchers at the National Bureau of Economic Research (NBER) found that, nationwide, of those employed pre-COVID-19, about half were working from home in the spring of 2020, including 35.2% who reported they were commuting and recently switched to working from home.[3] Currently, however, the share of employees WFH is likely to be less than the level registered last year, as the most stringent COVID-related restrictions have been lifted. No reliable estimates of WFH for each Ohio municipality exist, though available research suggests the impact of WFH policies would be greater on municipalities with a higher concentration of workers in the "knowledge" economy and a higher percentage of nonresident workers that commute into that municipality from surrounding areas. On the other hand, the impact of WFH would be lower for municipalities whose industrial mix is dominated by warehousing, manufacturing, and production of goods.

The H.B. 197 temporary rule

Under the temporary rule, if an individual has to work at a temporary worksite because of the COVID-19 emergency, that employee is still considered to be working at his or her regular place of employment. This treatment affects the municipality (1) for which the employer must withhold income taxes, (2) that may tax the employee's pay, and (3) that may tax (whether and how much) the employer's own income. Therefore, the temporary rule prevented employers from applying codified law to wages of workers who suddenly were working away from their regular place of employment. From a practical perspective, H.B. 197 ensured that employers would not have to modify their employee withholding accounting setup or modify the municipality to which they would file and remit tax withholdings and net profit taxes, as long as the Governor's COVID-19 emergency remained in place. Thus, H.B. 197 allowed the employer to not withhold taxes for that employee in the municipality where the employee's temporary worksite (home) was located and prevented the employer from becoming subject to income tax by the employee's municipality.

Fiscal effects of H.B. 157

By repealing the H.B. 197 temporary rule, the bill potentially requires employers, in many cases, to change the municipalities to which they remit income tax withholding and net profits taxes. Whether it in fact does so depends on whether the bill became effective prior to the expiration of the Governor's declaration. Municipal tax revenues depend on a variety of factors, including the payroll of workers in the municipality (residents and nonresidents) which give rise to municipal income tax withholding remitted to the city of work, income earned by the municipality's residents that work elsewhere, and the type of industries located in the municipality (which determines the employment base and municipality net profits tax base). Repeal of the temporary rule could have an immediate fiscal impact on municipalities by reducing tax withholdings for nonresidents WFH and affecting net profits taxes.

[2] The percentage was even lower, 8%, for the agriculture, fishing, forestry, and hunting occupations. Data available at https://www.bls.gov/opub/mlr/2020/article/ability-to-work-from-home.htm.

[3] Brynjolfsson, Erik, et al. *COVID-19 and Remote Work: An Early Look at U.S. Data*, NBER Working Paper 27344, http://www.nber.org/papers/w27344.

LBO is unable to quantify the revenue effects of the bill, both because LBO staff do not know when the Governor's declaration will expire and due to lack of detailed and accurate data for each municipality on payrolls and employees' residency and commuting behavior. If the bill does have a fiscal effect, on net statewide there would likely be a revenue loss to municipalities, totaling potentially several tens of millions of dollars (potential losses would be lower if the Governor's declaration expired shortly after the bill's enactment).

The fiscal effects can be described in general terms based on municipal income tax data, including tax bases and tax rates from the Department of Taxation, and worker commuter flow data, primarily derived from two Census Bureau data products: The American Community Survey (ACS) and the Longitudinal Employer-Household Dynamics Origin-Destination Employment Statistics (LODES).[4] Pre-COVID-19 commuter flow data indicate that large municipalities generally have a net positive commuter flow, meaning the number of nonresident employees in the municipality exceeds the number of residents working in another municipality. Municipalities in this situation could lose revenue under the bill; for the largest municipalities the potential revenue loss could measure in the millions.[5]

More generally, changes to municipal tax revenues would depend on incomes earned by nonresident workers in that municipality, income earned by the municipality's residents that work elsewhere, residence tax credits for taxes paid elsewhere,[6] and the prevalence of WFH (and therefore the type of industries in the municipality and municipality net profits tax base). No municipality will experience a revenue gain or loss from residents WFH who usually worked at another location in the same municipality, and municipalities without a residence tax credit will not gain revenue from residents that are now working at home. In addition, taxpayers WFH due to the pandemic may experience lower tax liabilities as a result of the bill, if their usual work location was in another municipality with higher tax rates than their residence city; and residents of municipalities with a piggyback municipal income tax may only have to pay that tax, instead of both a tax in the municipality of work and a tax in their municipality of residence. Such scenarios, which result in taxpayer savings, also likely result in an overall decrease in municipal income tax collections.

Township residents will also experience tax savings if their temporary work location is their home, if they usually work in a municipality that levies an income tax. Generally, townships

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[4] These datasets are compiled from different source data, contain different levels of complexity, and have differing strengths and weaknesses. The fiscal note makes no inference on permanent or long-term changes to WFH across industries.

[5] As an illustration, if the WFH percentage for nonresidents employed within the city of Columbus was 10% and the bill's provision were in effect, the reduction in income tax withholdings might be up to $86 million, based on the amount of income taxes collected in 2018, depending on the length of the Governor's emergency declaration.

[6] If available in municipal tax ordinances, these are income tax credits offered by a municipality to residents who pay tax in other municipalities. They affect the fiscal impact because what a municipality potentially gains from residents shifting to permanently WFH is the difference between the municipality's full tax rate and the tax a resident would typically pay, which would be reduced by a resident credit.

do not impose municipal income taxes, except in limited circumstances.[7] In 2000, 50% of all township residents lived in one of 155 townships with populations of 5,000 or more; and those townships were generally located around the largest urban areas of the state, Cincinnati-Hamilton, Cleveland-Akron, Dayton-Springfield, and Toledo. Those urban areas collect the large majority of Ohio municipal income taxes. Statewide, township residents with "regular" workplaces located within those large urban regions may realize income tax savings of millions of dollars.

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[7] A Joint Economic Development District (JEDD) is an arrangement whereby a municipality and a township agree to work together to develop township land for commercial or industrial purposes. The benefit to the municipality is that they get a portion of the taxes levied in the JEDD without having to annex it. The benefits to the township are that it can still collect property taxes as well as a portion of the income tax collected.