Multistate Tax Update -- March 26, 2015

| Thursday, March 26, 2015

Ohio raises the bar with improvement in its online checkbook

Ohio's Treasurer, Josh Mandel, had been promising to put Ohio's checkbook online since at least 2013. That year, he said that the basic idea is to "allow citizen auditors to easily examine the state's purchases, from paper clips and hotel rooms to consulting work. Ultimately, the checkbook would allow people to search, among other things, which vendors get the most money and how spending on certain services compares from one agency to another."

Late last year, Mandel's promise went live, as numerous outlets reported on Dec. 2, 2014. Describing **OhioCheckbook.com**, 10tv reported that the online checkbook shows 112 million transactions over the past seven years, and that it took a year and half to put together all the numbers. OhioCheckbook.com contains easy-to-read pie graphs revealing the various agencies' and departments' expenditures.

It also allows users to see total state spending ($61 billion in fiscal year 2014), what the largest expense types are (medical services, at $15 billion in fiscal year 2014), and the highest paid companies (United Health Care, at $313 million in fiscal year 2014), as well as other things. The site also contains a year-to-date spending pie chart, but it does not yet contain any figures for fiscal year 2015, which began July 2014.

At the end of the 2014 calendar year, the Public Interest Research Group's (PIRG) publication *Following the Money 2014: How the 50 States Rate in Providing Online Access to Government Spending Data* gave Ohio a D-, largely because the database was not searchable.

PIRG awarded top scores, A- ranks, to eight states (n order by rank, Indiana, Oregon, Florida, Texas, Massachusetts, Iowa, Vermont, and Wisconsin) for sites that offered spending transparency, user friendliness, accessibility, and the ability to "download and analyze the entire checkbook dataset." The nine states that received D range ranks (in descending order, Minnesota, Delaware, South Carolina, Rhode Island, North Dakota, Alabama, Nevada, Ohio, and Kansas) had less accessible data and users could not download and analyze the entire data set.

What a difference three months make. PIRG's *Following the Money 2015* now ranks Ohio at #1 with an A+ rating. PIRG asserts that transparency is critical because it helps governments save millions in taxpayer money "through more efficient government administration, less staff time spent on information requests, and the posting of contracts enabling potential new vendors to identify opportunities to win lower-cost bids or offer higher-quality goods and services." In addition, PIRG asserts that transparency reduces abuse and misspending by government officials because they are aware that the public is watching.

PIRG explains that Ohio's meteoric rise is based on the site's use of user-friendly features normally found on cutting edge, non-government webpages. The search function is easy and "akin to searching with a high-performance web tool thanks to Google-style contextual search functionality." This, along with the "Share" and "Help" buttons contributes to OhioCheckbook.com's "topflight standards for user-friendliness, creating a portal that feels like many search websites citizens use every day."

OhioCheckbook.com cost $814,000 to get up and running and its ongoing operations are funded by the existing budget. In late January of 2015, Seth Unger in the Ohio Treasurer's Office reported that there had already been 100,000 searches.

PIRG applauds Ohio for having “taken accountability to the next level by establishing a new best practice of providing a phone number and email address for the most appropriate human point of contact alongside every line of data.” The next step is to include municipal and county level data, and detailing all the public-private partnerships.

Ultimately, PIRG proclaims that Ohio has set a new standard for user-friendliness and accountability.

Kentucky drives economic development with tax credits

The Land of the Thoroughbred has been making great strides with its economic development efforts, and the nation is taking notice. In early March, the Cabinet for Economic Development (CED) announced that the state had placed first nationally in Atlanta-based magazine *Site Selection’s* annual Governor’s Cup rankings for new and expanded industry activity per capita in 2014. Projects qualified if they involved a capital investment of at least $1 million, created 50 or more jobs, or added at least 20,000 square feet of new floor space.

That year, Kentucky’s economic activity reached an all-time high; the state saw over $3.7 billion in new investment encompassing 350 new location and expansion projects anticipated to create nearly 15,000 jobs, which is more business investment than ever before. The CED attributed much of that economic growth to the expansion of companies already present; nearly 70 percent of the state’s announced new investment and new jobs came from the expansion of existing Kentucky businesses.

Economic development activity like this is linked to Kentucky’s precipitous drop in unemployment. The current 5.7 percent unemployment rate is the lowest in seven years, and down from 10.7 percent in 2008.

Angel Investment Fund Tax Credit

One of Kentucky’s tools for encouraging business growth and job creation is its **Angel Investment Fund Tax Credit** (Tax Credit). The Tax Credit allows people who provide capital for start-up companies to receive a tax credit of up to 50 percent of their investment in counties with high unemployment rates, or enhanced counties, and 40 percent in all other counties. Before last year, only groups of angel investors (with fund managers) could take advantage of the credits.

The Office of Entrepreneurship (OoE) within the Kentucky Cabinet for Economic Development administers the Tax Credit program. Earlier this month, the OoE trumpeted the astounding response from investors while warning those who wish to apply to do so fast because two-thirds of the 2015 funds to be allocated are almost gone. In just the first two months, 64 angel investors announced plans to invest $5.4 million in 17 Kentucky businesses, which makes them eligible for $2.1 million in angel investment tax credits after making their approved investments.

Besides the large tax credit, another reason for the high demand is that out-of-state investors are eligible to participate, even though they may not have any Kentucky tax liability. Such investors can sell their tax credit to someone within the state, thereby recovering some portion of the investment.

ThinkKentucky.com offers useful links to the fact sheet, applications, and other useful information, including the following guidelines:

- A qualified small business is a legal entity registered and in good standing with the Kentucky Secretary of State and has no more than 100 full-time employees;
- The business must be engaged in bioscience; environmental and energy technology; health and human development; information technology and communications; materials science and advanced

manufacturing; or other new economy knowledge based activity;
- A qualified investor holds no more than 20 percent ownership in, and is not employed by, the qualified small business prior to making a qualified investment in that business;
- A qualified investment is a minimum cash investment of $10,000 made by a qualified investor in a qualified small business;
- Tax credits may be transferred to an individual taxpayer and can be carried forward for up to 15 years.

Kentucky has allocated $3 million each calendar year on the Tax Credit, and the maximum credit that any individual qualified investor is allowed to receive is $200,000 in aggregate in any calendar year.

Kentucky Small Business Tax Credit

Another tool that Kentucky has deployed to spur growth is the **Kentucky Small Business Tax Credit** (KSBTC).

Any small business that creates and maintains at least one qualifying job, and purchases $5,000 or more in qualifying equipment, may be eligible to receive a state income tax credit in an amount determined, in part, by the number of jobs created and the amount of equipment purchased.

The KSBTC fact sheet points out that the state has a limit of $3 million to award per fiscal year. Qualified applicants are eligible to receive a tax credit in an amount not to exceed the lesser of: 1) $3,500 per eligible position; or 2) the total dollar amount invested in qualifying equipment or technology. Applicants are also subject to a $25,000 maximum tax credit cap per applicant for each calendar year.

Companies that have 50 or fewer full-time employees at the time of the application are eligible. In addition, the fact sheet sets out requirements for employment, wage, and investment minimums. For instance, with respect to the qualifying jobs, they must be filled for 12 months, pay at least 150 percent of the federal minimum wage, and be subject to the individual income tax imposed by statute.

In addition, an applicant must spend $5,000 or more on qualifying equipment or technology, defined as "tangible property purchased by the applicant business for use in the business (not for resale or personal use), with a per-unit cost of$300 or more and expected useful life of more than one year." Examples of qualifying equipment or technology include, but are not limited to: computers, equipment, furniture, fixtures, furnishings (excluding artwork), and vehicles titled in the legal name of the business. Real property, buildings, and consumable supplies do not qualify.

The Kentucky Investment Fund Act

A third growth device employed by Kentucky is the **Kentucky Investment Fund Act** (KIFA). KIFA offers a 40 percent tax credit to certain personal and corporate investors in approved investment funds. After the Kentucky Economic Development Finance Authority (KEDFA) allocates the credits to a fund, they are proportionately granted to the fund's investors upon its completion of qualified investments.

The minimum fund size is $500,000. An eligible qualified investment is one in a Kentucky-based small business that is actively and principally engaged in a "qualified activity" within Kentucky that meets the following criteria at the time of investment:

- 50 percent of the company's assets, operations, and employees are located in Kentucky;
- The company's net worth is less than $5 million (or $10 million, if it is a knowledge-based business) or its net income in each of the prior two years is less than $3 million; and

- The company has no more than 100 employees.

A qualified activity includes any industrial, manufacturing, mining, mining reclamation for economic development, commercial, healthcare, agricultural enterprise, or agribusiness activity.

The total amount of tax credits available to any single investment may not exceed, in aggregate, $8 million for all investors and all taxable years.

Virginia extends sunset date for gas severance tax

In mid-March, Virginia Governor Terry McAuliffe approved **SB 1308**, which extends the sunset date of the local gas severance tax by three years, from Dec. 31, 2015, to Jan. 1, 2018.

This tax revenue is allocated into two different areas:

First, three-quarters of the revenue is to be allocated to the local Coal and Gas Road Improvement Fund. Twenty-five percent of those funds may be used to fund the construction of natural gas service lines or the construction of new water or sewer systems and lines in areas with natural water supplies that are of insufficient quality or quantity.

Second, one quarter of the revenue is allocated to the Virginia Coalfield Economic Development Fund, whose mission is to help enhance and diversify the region's economy by encouraging new job creation.

In 2014, the Independent Fiscal Office for the state of Pennsylvania released a study comparing natural gas extraction between the states. Pennsylvania has a long history of natural gas production and in 2012 was ranked third, behind Texas and Louisiana, but it only began levying a fee (not a tax) in early 2012. Following that policy change, the state studied the various taxes and fees charged by states producing the most natural gas, and those in close proximity to Pennsylvania. Virginia ranked #16.

In 2013, the National Conference of State Legislators (NCSL) reported that county or city governing bodies in Virginia are authorized to impose a 1.5 percent gross severance tax on oil and a one percent gross severance tax on coal or gas. In addition, counties and cities can levy additional maximum one percent gross tax on gas, and also may adopt a maximum one percent gross tax on every person engaged in the business of severing coal or gas.

As of that year, 32 states produced natural gas, according to the NCSL. Maryland, New York, and Pennsylvania were the only natural gas producers without a severance tax. Thirty-four states have enacted fees or taxes on oil and gas production, and three of these states (North Carolina, Idaho, and Wisconsin) have taxes on oil and gas production despite lacking commercial gas and oil wells.

There are numerous methods to tax oil and gas production, and states differ in the imposition of the taxes. Most often, states tax the market value, though some tax the volume produced, and others tax a combination of both.

Naturally, there is controversy surrounding the taxation methods. Opponents argue that the imposition of a tax deters production. On the other hand, the fees generate substantial revenues that proponents of the tax claim are necessary to offset negative impacts on the environment and infrastructure.

For additional information regarding these subjects, or any other multistate tax issues, please contact:

David M. Kall
216.348.5812

dkall@mcdonaldhopkins.com

David H. Godenswager, II
216.348.5444
dgodenswager@mcdonaldhopkins.com

Susan Millradt McGlone
216.430.2022
smcglone@mcdonaldhopkins.com

Multistate Tax Services

Businesses must be vigilant and careful in managing their state and local tax liabilities and exposures. We understand this can be a daunting task. McDonald Hopkins Multistate Tax Services provides a broad range of state and local tax services including tax controversy, tax evaluation, tax planning, and tax policy. With professionals who have worked both inside and outside government agencies, our multistate tax team leverages its knowledge and experience to help clients control their complex multistate taxes.