Ohio Legislative Service Commission

Russ Keller

Fiscal Note & Local Impact Statement

Bill: S.B. 247 of the 130th G.A. **Date**: April 25, 2014

Status: As Introduced **Sponsor**: Sen. Kearney

Local Impact Statement Procedure Required: Yes

Contents: To authorize a refundable income tax credit for residential landlords who improve a rental unit's energy efficiency

State Fiscal Highlights

STATE FUND	FY 2015	FY 2016	FUTURE YEARS
General Revenue Fund			
Revenues	Loss between $16.6 million and $92.1 million per year	Loss between $16.6 million and $92.1 million per year	Annual loss between $16.6 million and $92.1 million per year
Expenditures	- 0 -	- 0 -	- 0 -

Note: The state fiscal year is July 1 through June 30. For example, FY 2015 is July 1, 2014 – June 30, 2015.

- Authorizing a refundable income tax credit for rental property energy efficiency improvements will reduce GRF revenues between $16.6 million and $92.1 million per year. Revenue from the personal income tax is deposited in the GRF.
- The (discontinued) Survey of Residential Alterations and Repairs, which was conducted by the U.S. Census Bureau, showed irregular spending activity over the previous decades, which is partly indicative of the cyclical nature of the rental improvement and repair industry. Annual GRF losses are likely to occur in irregular patterns, too.

Local Fiscal Highlights

LOCAL GOVERNMENT	FY 2014	FY 2015	FUTURE YEARS
Counties, municipalities, townships, and public libraries (LGF and PLF)			
Revenues	Loss between $0.6 million and $3.2 million per year	Loss between $0.6 million and $3.2 million per year	Annual loss between $0.6 million and $3.2 million per year
Expenditures	- 0 -	- 0 -	- 0 -

Note: For most local governments, the fiscal year is the calendar year. The school district fiscal year is July 1 through June 30.

- Authorizing a refundable income tax credit for rental property energy efficiency improvements will reduce Local Government Fund (LGF) and Public Library Fund

(PLF) revenues by a combined total of between $0.6 million to $3.2 million per year. Both the LGF and PLF each receive 1.66% of GRF tax receipts.

Detailed Fiscal Analysis

S.B. 247 authorizes a refundable income tax credit for rental property "energy efficiency improvements." The term is already defined elsewhere in the Revised Code as "energy efficiency technologies, products, and activities that reduce or support the reduction of energy consumption, allow for the reduction in demand, or support the production of clean, renewable energy and that are or will be permanently fixed to real property."

The bill permits a taxpayer who is an investor in a pass-through entity (PTE) that owns residential rental property to claim a refundable credit if, on or after January 1, 2013, the entity purchases and installs in the rental property an "energy-saving device" or the entity improves the rental property with an energy efficiency improvement installed by a person who is accredited by the building performance institute. PTEs, defined elsewhere in the Revised Code,[1] are generally businesses organized as S-corporations, partnerships, limited liability companies, limited liability partnerships, certain trusts (including real estate investment trusts[2]), or sole proprietorships. Sole proprietorships are explicitly included as PTEs by S.B. 247 for the purposes of this bill.

The bill defines an "energy-saving device" as "a residential washer, dryer, range, refrigerator, freezer, water heater, dishwasher, trash compactor, air conditioner, furnace, or other similar product used for regulating air or water temperature, cooking, sanitary purposes, or other household purposes, or a window or door on an outside wall of a home, if the device carries the energy star label indicating that it meets the efficiency criteria of the energy star program established by the U.S. Department of Energy and the U.S. Environmental Protection Agency." However, the bill specifically prohibits any television or other appliance used primarily for entertainment from the definition of energy saving device.

Fiscal effect

Data limitations hinder the estimation of this potential tax expenditure with a high degree of certainty. The U.S. Census Bureau of the Department of Commerce used to report expenditures for improvements and repairs of residential properties. However, the U.S. Census Bureau discontinued the Survey of Residential Alterations and Repairs (SORAR) after 2007. For years 2001 to 2007, the share of alterations

[1] R.C. 5733.04(O).

[2] Real estate investment trusts (REITs) invest in and own properties such as shopping malls, office buildings, apartments, warehouses, and hotels. Individuals that invest in REITs by purchasing their shares presumably would be able to benefit from the bill.

(inclusive of remodeling and major replacements), maintenance, and repairs incurred by owners of rental properties was 30% to 61% of the total spent by owner-occupied property owners.

The U.S. Government Accountability Office (GAO) estimated the underlying spending for the federal nonbusiness energy property credit. The Energy Policy Act of 2005 (EPACT05) created two new temporary tax credits for homeowners who made energy-efficiency improvements to their homes; however, the nonbusiness energy property credit is applicable to a wider base of taxpayers than the residential energy-efficient property credit because the latter is only applicable to property that used solar energy to generate electricity. GAO analyzed Internal Revenue Service data and concluded that $25.57 billion was spent on residential energy property that qualified for the nonbusiness energy property credit.

Table 1. Range of Estimated Tax Base and Resulting PIT Revenue Loss of S.B. 247

(amounts in millions, $)	Low Estimate	High Estimate
U.S. expenditures for nonbusiness energy property by homeowners	$25,567	$25,567
Residential rental property owners' estimated share of alterations, maintenance, and repair	30%	61%
Estimated dollar value of residential rental property owners' share of alterations, maintenance, and repair	$7,638	$15,673
Ohio's estimated share of residential rental property expenditures on nonbusiness energy property	3.0%	4.5%
Estimated dollar value of Ohio's share of residential rental property expenditures on nonbusiness energy property	$229	$705
Share of Ohio residential rental-property income earned by taxpayers that file PIT returns	50%	90%
Estimated dollar value of Ohio residential rental-property income earned by taxpayers that file PIT returns	$115	$635
PIT revenue loss (credit value equals 15% of the purchase and installation costs of the device or improvement)	$17.2	$95.2
GRF share of PIT revenue loss	$16.6	$92.1
LGF and PLF share of PIT revenue	$0.6	$3.2

Applying the percentages learned from discontinued Census data, 30% to 61%, to the expenditures that qualify for the nonbusiness energy property credit yields a range of $7.6 billion to $15.7 billion. Ohio's share of these aggregate amounts can be anywhere from 3.0% to 4.5%, depending on the metric used to evaluate Ohio's proportion of U.S. totals.

Not all residential property owners are organized as PTEs that are subject to the PIT. Some have a different business structure that makes them subject to the Commercial Activity Tax (CAT) rather than the PIT. It is possible that some income taxpayers that own residential rental properties will not qualify for the PTE exemption, but as long as the taxpayer includes their rental property income on Schedule C or

Schedule E of their federal income tax return, the PIT taxpayer should qualify for the credit in S.B. 247.

Data limitations prevent LSC from determining how many residential property owners in Ohio file the PIT as PTEs (inclusive of sole proprietors). For the purposes of this analysis, LSC will use between 50% and 90% of the residential property owners, but this is a data-free generalization. In applying these percentages to estimates in Table 1, LSC concludes that between $115 million and $635 million in PTE expenditures will qualify for the proposed PIT credit. S.B. 247 sets the credit value equal to 15%, so the resulting tax expenditure is between $17 million and $95 million per year.

The (discontinued) Survey of Residential Alterations and Repairs, which was conducted by the U.S. Census Bureau, showed irregular spending activity over the previous decades, which is partly indicative of the cyclical nature of the rental improvement and repair industry. Annual GRF losses are likely to occur in irregular patterns, too.

The personal income tax is a GRF tax, and the Local Government Fund (LGF) and Public Library Fund (PLF) each receive 1.66% of GRF receipts. Reducing PIT revenues through the refundable credit proposed by S.B. 247 will reduce the LGF and PLF by a combined total of between $0.6 million to $3.2 million per year.

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