



The Ohio Department of Taxation (ODT) recently launched an initiative to identify businesses that are subject to use tax but aren't filing and remitting the tax. The ODT estimates that up to 380,000 companies may owe use tax, and collecting it is now more important than ever with the state budget stretched beyond its limit. As part of the initiative, the ODT introduced the Use Tax Education Program (UTEP) to educate businesses and provide an avenue for compliance with filing and paying their required use tax. It is a staged program with some amnesty built in, but that amnesty period ends August 1, 2011. The biennial Ohio State Budget Bill passed at the end of June contains an Amnesty Program for businesses that are not currently registered to pay use tax. With these programs available, it is important to get in compliance now.

So what is use tax?

Use tax is a tax on the storage, use or other consumption of tangible personal property and certain taxable services in Ohio. Use tax is assessed when a taxable purchase is made, but no sales tax is collected. For example, your dealership purchases computers from an out of state supplier or online vendor, and sales tax is not charged on the order, you must self assess and remit a use tax on the value of the computers. As this is a self-reported tax, it's clearly an area of interest and concern for the ODT to find businesses that are not self reporting and paying use tax as required by law.

Is use tax different for auto dealers?

It's not different, but rather it reaches beyond the typical goods and services purchase example noted above. Use tax for auto dealers comes into play with different types of vehicle purchase transactions and vehicle uses. You need to look not only at the purchase of a vehicle, but how often a vehicle is used in a particular way and whether or not fees are collected from a user. A vehicle could be used as a parts trade, demo for customer test drives, salesman demo, dealer/operator demo, or even provided to a charity for their use. There are also special conditions that apply with warranty service work, internet vehicle sales and vehicles with negative equity.

Do I pay use tax on a car I lease from a manufacturer?

No. In this transaction, the manufacturer is responsible to collect sales tax from you and remit it to their tax agency. No use tax is required to be remitted as sales tax is collected by the lessor. However, if the lessor fails to collect sales tax on the monthly lease payment, then you would be required to pay use tax.

What if I purchase a car from the manufacturer, another dealer or take a car from inventory for use by my dealership as a service loaner?

If the vehicle is purchased from a manufacturer, another dealer or moved from inventory, whether or not tax is due depends on how the dealer uses the vehicle. If the vehicle will be

used as a loaner and no rental fee is charged, the dealer must pay sales tax on the vehicle when it is titled in the dealership's name. However, if a rental fee is charged to the customer, the dealer will be required to collect sales tax on the rental fee and will not pay sales tax on the vehicle at the time it is titled in the dealership's name.

The vehicle is used as a demo. What's the use tax?

This is a common situation for auto dealerships and it is subject to use tax because a share of the vehicle's value is consumed as it's used for demonstration purposes. That portion of the value used must be included in the monthly use tax calculation for the dealer. Here's a sample calculation from the ODT:

Example – New Vehicle

For the purpose of determining the value of the temporary use of a new vehicle from inventory, where no market lease or rental price exists, there is a simple method to determine the vehicle usage.

Dealer cost (invoice) \$30,000 x 2.4 % = **\$720.00 monthly value**

Multiply the monthly value by the local sales tax rate to determine the use tax to pay:

\$720.00 x 7.75% (Cuyahoga County) = \$55.80 use tax

For **Used Vehicles**, you take the dealer cost plus any repairs made to the vehicle and multiply by 2.4% to determine the monthly value.

The vehicle is used for test drives part of the time. Do I have to pay use tax on the full value of the vehicle?

No. You can prorate the use tax if the car is not used every day for test drives or other similar purposes. For example, if the demo is available for test drive for 20 days out of the month with each day being a 10 hour day, then the vehicle would be available for test drive for 200 hours in a month. Assuming a 31 day month, there are 744 hours in a month. The value of the vehicle subject to Ohio use tax would be prorated by multiplying the calculated value by 544/744. From our sample calculation above, the monthly value of the car is:

Full monthly value \$720.00 x 544/744 = \$526.39 monthly value

What if I take a vehicle out of inventory or convert a demo for dealership use?

If you record the vehicle as a fixed asset of the dealership, you are the ultimate owner of the vehicle and are subject to sales tax, just as you would be if you purchased the car from the manufacturer.

On the other hand, if a demo is moved back to inventory for sale as a used vehicle, the ultimate buyer of that vehicle is responsible for the sales tax at time of purchase.

You mentioned that a special condition applies to use tax on warranty service work. What is the rule?

Warranty work performed by a dealer and charged back to the warrantor of the vehicle is NOT subject to use tax based on the July 1, 1994 rule currently in effect. However, dealerships must obtain properly completed exemption certificates from the warrantors indicating “used or consumed in the fulfillment of a warranty, maintenance or service agreement” in order to document the exempt nature of the transaction.

If I sell a vehicle to a resident in another state is there a sales tax obligation?

With the increasing frequency of internet vehicle sales, knowing sales and use tax obligations by state is important. If the ultimate consumer is a resident of Arizona, California, Florida, Indiana, Massachusetts, Michigan, South Carolina or Washington and they purchase a vehicle from an Ohio dealer and register that vehicle in their home state, they are required to pay Ohio sales tax. Internet sales to residents of other states do not require that the dealer collect sales tax.

Is there sales tax on negative equity when it's part of a vehicle trade-in or loan payoff?

When negative equity is included in the total vehicle price as part of a trade-in allowance or loan payoff, it is subject to sales tax. If it is not included in the total vehicle price but added to the balance due or amount financed, no sales tax is charged on the negative equity amount.

How do I get compliant with the ODT on my use tax filing?

Work with your accounting and legal advisors to determine your use tax obligation. You may wish to consider the Voluntary Disclosure program in effect through August 1, 2011, so you must act quickly!

Through August 1, 2011, businesses may sign a Voluntary Disclosure Agreement (VDA) and pay their use tax bill, limited to a three year look back period, plus interest, but without the typical 15% penalty. With an aggressive push on audits, it's in the best interest of dealers who have previously registered to pay use tax, but are currently not in compliance to take advantage of the VDA and limit their liability.

The Ohio Biennial Budget Bill signed into law at the end of June contains a Use Tax Amnesty Program that will run from October 1, 2011 through May 31, 2013. This program is only available for businesses that have not registered to pay use tax prior to June 1, 2011. If eligible for amnesty, a business will be able to limit their exposure to the period from January 1, 2009 through the current period. In addition, the state will not charge penalty or interest on the past due use tax.

As you can see, the state has made an effort to improve use tax compliance among Ohio businesses by offering certain incentives. The opportunity to limit exposure, penalties and interest is a unique opportunity for Ohio businesses. The auto dealer team at Apple Growth Partners is eager to work with you and your legal advisors to determine the best course of action for your auto dealership. If you have any questions regarding the information in this update, please contact Stan Apple or Brett Mangon of Apple Growth Partners at sapple@applegrowth.com or bmangon@applegrowth.com.