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This is additional background on the application of the Ohio sales and use taxes to automatic data processing (ADP) and electronic information services (EIS) as defined by Ohio law.[1] The Ohio tax base was expanded back in 1983 for essentially the same reason that a Study Group of the Multistate Tax Commission is considering a new definition that may expand the sales and use tax base today: to address technological changes arising from the increasing role of computers in transactions.[2]

Because the Ohio tax on certain services provided by computer has been in place for more than 40 years, the manner in which the interpretation of the Ohio statute has been impacted by technological changes can inform how a new sales and use tax statute would apply to future technologies. The Ohio statute has been controversial in its application to new technologies that were unforeseen at enactment. But the Ohio statute warrants attention because its longevity provides an illustration of how statutory language applies to changing technologies.

To understand the language used by the Ohio General Assembly, it is useful to examine how Ohio case law applied earlier sales-tax statutes to transactions involving the use of computers before the 1983 enactment and thereby reveal the goals the Ohio General Assembly had when it explicitly imposed the tax on such transactions. Although the operative words in the

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[2] "Computer services" is another category of transactions subjected to tax in Ohio but has limited application and is disregarded for this presentation.

Ohio statute seem archaic today, derived as they were from the technology of the 1970s and 1980s, that language is routinely being applied to technologies never contemplated in 1983.

In a series of cases before ADP or EIS transactions were addressed legislatively, the Ohio Supreme Court concluded that transactions that would be taxable absent computer involvement were not immunized because of the presence of computers. The fact patterns in these cases ultimately influenced the language employed in the Ohio sales tax statute relating to ADP and later EIS.

For audit periods prior to 1976, the application of the sales tax to data processing was addressed in the context of the transfer of tangible personal property, as services generally were not taxable. Issues arose with respect to services performed by data processors including inputting and verifying the client's information, computerizing that information by summarizing, computing, extracting, sorting and sequencing the data, and producing, for example, printouts, payroll reports, or financial statements. See, e.g., *Miami Citizens National Bank & Trust Company v. Lindley*, 50 Ohio St.2d 249 (1977) (pre-1976 audit regarding taking of information from a customer's records, reorganizing, computerizing and returning the information to the customer in printed form was subject to sales tax because transferring the printout for consideration was the sale of tangible personal property).

Also, entities that processed their own data, such as universities and larger companies, made their computers available to others in what was known as "time-sharing" of the computer. These providers of "centralized" sources of computing were also deemed to be engaged in making taxable transfers of property. See *Babcock & Wilcox Co. v. Kosydar,* 48 Ohio St.2d 251(1976) (use of a computer by the taxpayer's engineering department personnel for purposes of conducting calculations and design functions was a license to use the remote computer and therefore a taxable transaction as the use of tangible personal property); see also *Citizens Financial Corp.*

v. Kosydar, 43 Ohio St.2d 148 (1975) (data processing company was making taxable sales when it provided bank-account data to its clients irrespective of whether the data was provided to the customer by hard copy (computer printouts) or provided "on-line" via the data processor's equipment).

In 1976, the Ohio General Assembly enacted Amended House Bill Number 1347 of the 111th General Assembly, 136 v. H 1347 (1976)). This amendment provided the following definition of "sale" and "selling" in R.C. 5739.0l(B):

> The transfer of title or possession, or both, of tangible personal property, or the granting of a license to use or consume tangible personal property, by an electronic data processor in conveying the results of electronic processing of others' data by such processor is not a sale, and the electronic data processor is deemed to be rendering a service.

On August 1, 1976, the Tax Commissioner in a Directive explained the effect of the statute:

> The change in the definition of "sale" and "selling" provides for the classification of data processing transactions as services if (1) the data processor is converting data supplied by the client for the client; and (2) the tangible personal property and license to use or consume is charged to the supplier of the data (client); and (3) such tangible personal property and license to use or consume is used in conveying the results of the electronic processing of client's data to the client.

In short, this amendment had the effect of reversing the earlier decisions of the Ohio Supreme Court that treated computer-provided reports (off-line) and licenses to use computers (on-line) as taxable and declared these transactions to be excluded from tax. This policy was short lived.

In 1983, the General Assembly reinstated the tax on transactions that had been exempted in 1976, placing the computer-generated reports and computer time- sharing (access to computers)[3] on the same footing as the receipt of other written reports and traditional rentals

[3] *Perplexity* describes a time-sharing system as one allowing multiple users to access a single powerful mainframe computer from remote terminals with all processing centralized in the main user computer room. Last visited May 31, 2025.

of tangible personal property. The legislation effectively reinstated the pre-1976 decisions. The new tax status, however, was not based on the finding of the delivery of tangible personal property to support the tax. Instead, the service of "automatic data processing" became subject to tax as a service. This statute, R.C. 5739.0l(B)(3)(e), after amendments and before the 1993 legislation to be discussed below, provided as follows:

> (B) 'Sale' includes[s] all of the following transactions for a consideration:
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> …
>
> (3) All transactions by which:
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> …
>
> (e) Automatic data processing and computer services are or are to be provided for use in business when the true object of the transaction is the receipt by the consumer of automatic data processing or computer services rather than the receipt of personal or professional services to which automatic data processing or computer services are incidental or supplemental….

In addition, former R.C. 5739.0l(Y)(l) provided:

> "Automatic data processing" * * * means: * * * processing of others' data, including keypunching or similar data entry services together with verification thereof; providing access to computer equipment for the purpose of processing data or examining or acquiring data stored in or accessible to such computer equipment. …"Automatic data processing["] ... shall not include personal or professional services.

In 1993, the General Assembly separated EIS from the remainder of ADP so that an entity that provided EIS would qualify for an incentive in the form of a refund of twenty-five percent (25%) of the sales and use tax it paid on that equipment. The archetype of an electronic information service provider was LexisNexis, then based in Dayton, Ohio. The statute did not expand the reach of the tax on ADP but classified certain transactions that formerly were ADP to be EIS and provided a refund opportunity for EIS while denying the refund to those providing ADP as more narrowly defined. The ADP and EIS services separately defined by the 1993 legislation were in essence components of the ADP definition before the amendment.

Reflecting the 1993 change, the operative language of R.C. 5739.01 became as follows:

> (B) "Sale" and "selling" include all of the following transactions for a consideration in any manner, whether absolutely or conditionally, whether for a price or rental, in money or by exchange, and by any means whatsoever:
>
> …
>
> (3) All transactions by which:
>
> …
>
> (e) Automatic data processing, computer services, or electronic information services are or are to be provided for use in business when the true object of the transaction is the receipt by the consumer of automatic data processing, computer services, or electronic information services rather than the receipt of personal or professional services to which automatic data processing, computer services, or electronic information services are incidental or supplemental. ....
>
> (Y)(1)(a) "Automatic data processing" means processing of others' data, including keypunching or similar data entry services together with verification thereof, or providing access to computer equipment for the purpose of processing data.
>
> (c)"Electronic information services" means providing access to computer equipment by means of telecommunications equipment for the purpose of either of the following:
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> (i) examining or acquiring data stored in or accessible to the computer equipment;
>
> (ii) placing data into the computer equipment to be retrieved by designated recipients with access to the computer equipment.

Applying the Ohio Tax on ADP and EIS Over Time

During the long period of time during which the ADP/EIS regimes have been part of the Ohio tax code, many technological changes have occurred. But for our purposes, it is useful to focus on two major developments. In particular, the focus is on the use of remote (off-site) computers. The 1983 amendments specifically addressed the use of time-sharing by which multiple users obtained access to a single mainframe computer from remote terminals with all processing centralized in the main user computer data center.

Then over time, computing became dispersed meaning that individual companies could acquire computers and software to perform the needed data processing on-site and no longer needed to connect to remote computers through the time-sharing model. Fewer transactions would qualify as ADP/EIS after time-sharing was phased out.

Decades later, the "Cloud" arrived. Microsoft describes the Cloud as "a global network of remote servers that store and process data for devices and computers."[4] The Ohio Tax Department takes the position that the ADP/EIS provisions make software as a service (SaaS), infrastructure as a service (IaaS) and platform as a service (PaaS) subject to tax. These services were not foreseeable in 1983 or 1993. The author does not know of a pending challenge to this position. Those newer products would seem to be similar to the time-sharing concept that prompted the 1983 amendment. What is striking about the application of the Ohio tax on ADP/EIS is that the scope of the statute could be said to have contracted because new technology superseded time-sharing, but the tax base later substantially expanded to encompass the services provided by the Cloud. Both modifications of the tax base occurred without any change in the statute or applicable administrative rule.

Should a taxing statute be applied to new technology when the statute by its express terms is found to apply to the new technology, but that technology did not exist (nor could it have been contemplated) at the time of enactment? There appears to be little or no discussion of this issue in the tax cases. Support exists for applying an old statute to new technology. The U.S. Supreme Court through Justice Reed addressed the issue as follows: "Old laws apply to changed

[4] https://azure.microsoft.com/en-us/resources/cloud-computing-dictionary/what-is-the-cloud#:~:text=The%20cloud%20is%20a%20global,data%20for%20devices%20and%20computers. Last visited May 30, 2025

situations…. While a statute speaks from its enactment, even a criminal statute embraces everything which subsequently falls within its scope."[5] The late Justice Antonin Scalia and Bryan Garner in *Reading Law* at 85-87 argue that even when applying the fixed meaning canon in which words must be given the meaning they had when the text was adopted, a general statute can be applied to new technology.

The durability of the Ohio tax on computer-provided services designated as ADP/EIS suggests that the drafters of new tax legislation should reasonably contemplate that the new statute may be the law for the adopting states for an extended period of time. Because new technology may be subject to tax even when that technology is not within the contemplation of the drafters, the drafting process should be less focused on the technology but focused instead on the bedrock features of a well-designed retail sales tax including proper input exemptions and the novel issues of administration and interpretation of the law that can be expected to arise.

The natural byproduct of the adaptability of the Ohio statute to changing technologies is that considerable uncertainties have been created for many service providers and contentious issues are presented in many audits. But there have been no meaningful amendments to the law since 1993. It would be surprising if senior officials of the Ohio Tax Department were not consistently responding to inquiries about the scope of the tax on ADP/EIS.

Taxing Services That Formerly Were Exempt as Personal or Professional Services

The Ohio statute taxing ADP/EIS has always specifically excluded personal and professional services. This exclusion is expressed in the following terms:

(Y)(1)(d) "Automatic data processing,… or electronic information services" shall

[5] *Browder v. United States*, 312 U.S. 335, 339-340 (1941), footnote omitted.

not include personal or professional services.

(Y)(2) As used in divisions (B)(3)(e) and (Y)(1) of this section, "personal and professional services" means all services other than automatic data processing, computer services, or electronic information services, including but not limited to:

(a) Accounting and legal services such as advice on tax matters, asset management, budgetary matters, quality control, information security, and auditing and any other situation where the service provider receives data or information and studies, alters, analyzes, interprets, or adjusts such material;

(b) Analyzing business policies and procedures;

(c) Identifying management information needs;

(d) Feasibility studies, including economic and technical analysis of existing or potential computer hardware or software needs and alternatives;

(e) Designing policies, procedures, and custom software for collecting business information, and determining how data should be summarized, sequenced, formatted, processed, controlled, and reported so that it will be meaningful to management;

(f) Developing policies and procedures that document how business events and transactions are to be authorized, executed, and controlled;

(g) Testing of business procedures;

(h) Training personnel in business procedure applications;

(i) Providing credit information to users of such information by a consumer reporting agency, as defined in the "Fair Credit Reporting Act," 84 Stat. 1114, 1129 (1970), 15 U.S.C. 1681a(f), or as hereafter amended, including but not limited to gathering, organizing, analyzing, recording, and furnishing such information by any oral, written, graphic, or electronic medium;

(j) Providing debt collection services by any oral, written, graphic, or electronic means;

(k) Providing digital advertising services;

(l) Providing services to electronically file any federal, state, or local individual income tax return, report, or other related document or schedule with a federal, state, or local government entity or to electronically remit a payment of any such individual income tax to such an entity. For the purpose of this division, "individual income tax" does not include federal, state, or local taxes withheld by an employer from an employee's compensation.

The services listed in divisions (Y)(2)(a) to (l) of this section are not automatic data processing or computer services.

The Ohio Tax Department applied the personal and professional provisions as an

exemption meaning that one analyzed first whether the transaction qualified as ADP/EIS and then determined whether the transaction was exempt from the tax as a personal or professional service. The Ohio Supreme Court, however, rejected that analysis and found that the list of personal and professional services were not exemptions in the following terms:

> {¶24} When the General Assembly decided to impose sales tax on ADP and EIS, it defined and carved out these computer-related services as taxable while leaving "personal or professional services" outside the ambit of the tax. Anticipating cases in which different services could be bundled in one transaction, the legislature conditioned the taxability of the whole transaction on determining its true object: a transaction is taxable only when the consumer's true object is to obtain the work performed by computer systems – ADP or EIS - rather than to obtain personal and professional services that are coupled with the work that is performed by computer systems. Accordingly, instead of setting forth a list of exemptions, R.C. 5739.01(Y)(2)(a) through (k)[now (l)] identify a few of the many personal and professional services that may be bundled with ADP and EIS in a particular transaction.[6]

The definition being considered by the Study Group is set up analytically as a definition with an exception in the following terms:

> "Automated digital product" - an item, including software or a service or a right to access or use the item regardless of duration, that is provided in a binary format and for which additional human intervention required to produce the same or a substantially similar item for additional customers is minimal.

The proposed definition under consideration by the MTC Study Group provides a broad description of a taxable automated digital product and an exception for personal or professional services. There are two important considerations raised by this approach.

First, the personal service exclusion is fading away. A stark exposition of this phenomenon is the Arizona court of appeals decision in *ADP, LLC v. Ariz. DOR,* 524 P.3d 278 (2023) in which the company, ADP, LLC, a human resource service provider, whose services were not subject to the Arizona Transaction Privilege Tax later was required to account for the

[6] *Cincinnati Federal Savings & Loan Company v. McClain*, 168 Ohio St.3d 123, 2022-Ohio-725 at ¶24. Bracketed material added.

tax after ADP, LLC substituted an automated system for use by its customers rather than using human employees. to provide that service. This substitution of automation for human labor is prevalent in the modern economy. Moreover, the increased use of AI will almost certainly find increasing instances of automation replacing human labor.

Second the rationale for taxing digital products has been that these products substitute for formerly taxable tangible products. The proposed Study Group amendment under consideration will result in taxing services that traditionally have not been subject to tax.

A case can be made that expanding the sales and use tax bases to include more services is appropriate in light of changes in the economy and the need to preserve the tax bases. But upon subjecting new services to a retail sales tax, the administrative and policy implications of taxing these new services must be considered. It is a mistake to tax personal and probably some professional service under the guise of taxing automated digital products without acknowledging the impact of new services being subject to tax. The experience of Florida and other states attempting to expand the tax base to include services shows the importance of addressing issues of proper administration before enactment.