

ETPI

Facts and Figures

Education Tax Policy Institute

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Winter 2003 Edition

TAX POLICY INSTITUTE BEGINS SIXTH YEAR

The Education Tax Policy Institute—established in 1997—is now widely regarded as a leading authority on how tax issues affect education funding and local government services.

As an independent, data-driven organization, ETPI provides elected officials, local leaders, and the news media with projections on how tax changes impact revenues for public sector services.

Funding for ETPI projects is provided by memberships from more than 100 Ohio school districts and 11 state-level sponsoring organizations. Those organizations are:

Alliance for Adequate School Funding
County Commissioners' Association of Ohio
Ohio Association of Joint Vocational Schools
Ohio Education Association
Ohio Federation of Teachers
Ohio Municipal League

Buckeye Association of School Administrators
Ohio Association of Community Colleges
Ohio Association of School Business Officials
Ohio Coalition for Equity and Adequacy of School Funding
Ohio School Boards Association

ETPI's highly regarded research reports through the years have included detailed studies on topics such as: electric deregulation, effects of business tangible property reductions, funding for Ohio's urban districts, and a ten-year study of property taxes.

This winter edition of ETPI *Facts and Figures* is being mailed to all school board presidents, treasurers, and school superintendents. A membership form is included with this newsletter.

ETPI OFFICERS

John Brandt	President
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ETPI TAX CONSULTANTS

William Driscoll	Levin, Driscoll & Fleeter
Howard Fleeter	Levin, Driscoll & Fleeter
Richard Levin	Levin, Driscoll & Fleeter
Joanne Limbach	Limbach and Associates

THE ROOT OF A HOST OF PROBLEMS: HOUSE BILL 920

House Bill 920 is at the root of a string of problems that are plaguing Ohio school districts, according to Education Tax Policy Institute Consultant Dr. Howard Fleeter.

In his testimony before the Committee to Study State and Local Taxes, Fleeter clarified the effects of four property tax issues as they relate to the funding of schools in Ohio: impact of HB 920, the 20-mill floor, reappraisal phantom revenue, and the inventory tax phase-out. Related testimony was provided by Charles Swindler, Western Reserve superintendent; and Chuck Gossett, West Clermont treasurer.

- **HB 920 Is Fundamentally Flawed**

The rationale of insulating taxpayers from undue increases in their property tax bill in response to inflation in property values is sound, Fleeter said. But HB 920 (approved in 1976) is fundamentally flawed by constraining property tax revenues too severely.

On average, taxpayers see little increase in property taxes as a result of inflation, he noted. But there will be some taxpayers whose property taxes are reduced because their property increased in value at a lower rate than the district average.

- **Phantom Revenue: An Unintended Consequence**

Fleeter said reappraisal phantom revenue is an unintended consequence of HB 920. No other state in the nation, he pointed out, faces this issue which results from the complex interaction of Ohio's property tax laws and the school funding formula.

When a school system's property wealth increases, the district's contribution to the cost of education increases, as well. However, when the property wealth increase is due to inflation for reappraisal or update, the actual increase in local revenues is less than what is presumed by the state aid formula. Thus, Fleeter pointed out, the aid formula is attributing phantom local revenue to the school district—revenue it does not actually receive.

- **Implications of the Tangible Tax Phase-out**

Starting last year, the inventory portion of the tangible personal property tax began a 25-year phase-out period.

Fleeter in his testimony agreed that the inventory tax is inequitable to many businesses, but he noted that planned annual one percentage point decreases in the 25% listing percentage will present increasing problems for entities that rely on this source of revenue.

A "hold harmless" provision for schools, as stipulated in the electric deregulation statute, would protect districts from local revenue loss due to state policy tax change, Fleeter pointed out.

- **More Districts Placed at the 20-mill Floor**

A growing number of school districts are at the 20-mill floor, Fleeter testified. In tax year 2001, 241 districts were at the 20-mill floor for either Class 1 (residential and agricultural) property, Class 2 (business and commercial property), or both Class 1 and 2.

Another 74 districts were found to be within one tenth of a mill of 20 mills, suggesting that even minimal inflation at the next reappraisal or update would leave them with the equivalent of 20 inside mills.

STUDY PANEL LOOKS AT TAX REFORM

Lost in the heated debate about tax proposals in Governor Bob Taft's budget for the next two years is the fact that the recommendations are substantially based on the work of a study committee that has been holding hearings since last summer.

The Committee to Study State and Local Taxes, composed of three cabinet members and six legislators, issued its draft report on January 29—just days before the Governor's Fiscal Year 04/05 budget was unveiled.

The Committee considered five elements of a quality tax system as guidelines for tax policy: They were:

1. Simplicity
2. Equity
3. Stability
4. Neutrality
5. Competitiveness

In its draft report, the Committee embraced the principle that a tax structure should strive to use a broad tax base and low rates rather than a narrow base with high rates. In other words, special tax breaks, exemptions, or "carve-outs" from general application of a tax should be avoided, as much as possible.

Also, the Committee agreed that the current tax system is excessively reliant on property taxes and dependent on a sales tax that applies mainly to goods while the nation's economy has grown through the service sector.

Among the Committee's most sweeping options for change:

- Expand the base of the corporate franchise tax by repealing numerous special exemptions and favored tax treatments to increase the productivity of a source that yields relatively little revenue despite a high tax rate.
- Expand the base of the sales tax to "capture the broader economy" by increasing the number of services subject to tax and removing special interest "carve-outs."
- Restructure the income tax to remove very low-income people from tax rolls, reduce the top rate to be more competitive with other states, and eliminate indexing of brackets scheduled to begin in 2005.
- Eliminate the tangible property tax and replace it with a broad-based business tax based on either gross receipts or Ohio sales, property and payroll.

Only with regard to real estate taxes did the Committee not offer bold recommendations for reform, instead calling for a specific study.

The greatest differences between the Committee's report and the Governor's budget proposals appear in the tangible personal property tax.

Instead of opting to replace tangible property tax with an alternative broad-based business tax, the budget would accelerate the reductions for inventory property beginning in 2005 (without specifying any replacement revenues) and phase out the reimbursement to schools and local governments for \$10,000 tangible tax exemptions. These two proposals would adversely affect Ohio's school districts and other local governments dependent on tangible property tax revenues.

ADVISORY COUNCIL CONVENES IN MARCH

The ETPI Advisory Council is scheduled to meet in Columbus on March 3 at the Ohio School Boards Association headquarters. From the early days of ETPI, Advisory Committee members have provided input on research projects that later became the subject of studies issued by ETPI.

The periodic Advisory Committee sessions also provide school district representatives and officials from ETPI's state-level sponsoring organizations the opportunity to hear updates on emerging tax related issues.

A CALL FOR EDUCATION SPENDING APPROPRIATED AS A LUMP SUM

In his budget proposals, Governor Taft has recommended that all education spending for FY05 be appropriated as a lump sum. A "Blue Ribbon Task Force" would meet during FY04 to make recommendations for dividing the FY05 appropriation among various line items.

In the budget recommendations, certain programs have an appropriation amount for FY04 with no appropriation for FY05. Instead of an FY05 appropriation, the recommendation reads: "See Governor's Blue Ribbon Task Force."

According to the "Budget Blue Book," some of the items to be included in the scope of task force study include: formula aid, special education, ESEA Title I, pupil transportation, school lunch, field based professional development, DPIA, and non-public school payments.

THE ETPI TAX CONSULTANT TEAM FOR 2003

ETPI has sought out an experienced panel of experts in fiscal issues to continue issuance of a series of widely acclaimed research studies. In addition to compiling research documentation, the ETPI tax consultants are often asked to appear before state and local policy-makers to provide expert testimony on Ohio public sector revenue and expenditure issues.

ETPI's consultant team for 2003:

William P. Driscoll is a founding partner of Levin, Driscoll & Fleeter, a firm that specializes in tax and public sector revenue issues. Driscoll served as Deputy Tax Commissioner for the Legal Division in the Ohio Department of Taxation and was a research analyst for the Ohio Legislative Service Commission.

Dr. Howard Fleeter is a partner with Levin, Driscoll & Fleeter. He has served as a Professor of Public Policy at The Ohio State University and was a member of the School of Education faculty at the University of Massachusetts Amherst. Fleeter was Advisor for the Governor's Education Management Council.

Richard Levin, a founding partner of Levin, Driscoll & Fleeter, was Deputy Tax Commissioner for Policy and Research Director at the Ohio Department of Taxation. He also served in elective office as City Auditor of Bexley.

Joanne Limbach is president of Limbach and Associates. She is a former Commissioner for the Ohio Department of Taxation. Limbach has been a Dover classroom teacher, a New Philadelphia Board of Education member and a Tuscarawas County Commissioner.