

Ohio Senate Finance Committee

Governor DeWine's Executive Budget Proposal

Fiscal Years 2020 and 2021

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Ohio Office of Budget & Management

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Chairman Dolan, Vice Chair Burke, Ranking Member Sykes, and members of the Finance Committee, my name is Kim Murnieks, and I am Director of the Office of Budget and Management. I am pleased to be with you today to present Governor DeWine's Executive Budget for fiscal years 2020 and 2021.

I want thank Governor DeWine and his staff, Lt. Governor Husted, all members of the Governor's cabinet, and especially the staff of OBM who worked extremely hard during a short period of time to develop the budget that I am happy to present today.

As we introduce this budget, the state is in strong fiscal condition, now in the final quarter of fiscal year 2019 with revenues exceeding expenditures, maintaining a significant balance in the Budget Stabilization Fund, and continuing to operate with a balanced budget. We seek to run Ohio like a high-performing business. In every business, there comes a time to cut back – and then a time to reinvest to achieve success. Now is the time to invest in our great state. Our strong fiscal position allows Ohio leaders to boldly address important issues facing the citizens of Ohio, with a budget that supports Governor DeWine's vision of *Investing in Ohio's Future*.

In my testimony today I will describe Governor DeWine's budget that:

- Invests in families and children,
- Invests in our workforce and innovation,
- Invests in our local communities,
- Invests in Ohio's recovery from addiction, and
- Invests in our natural wonders.

This budget is conservatively forecast, balanced, and does not raise taxes. I will discuss our current economic conditions and the revenue assumptions that form the basis for the budget, and then I will outline the major policies that are the Governor's primary focus.

ECONOMIC OVERVIEW AND FORECAST

OBM's Ohio income forecast for FY 2019-2021 is more conservative than the IHS forecast

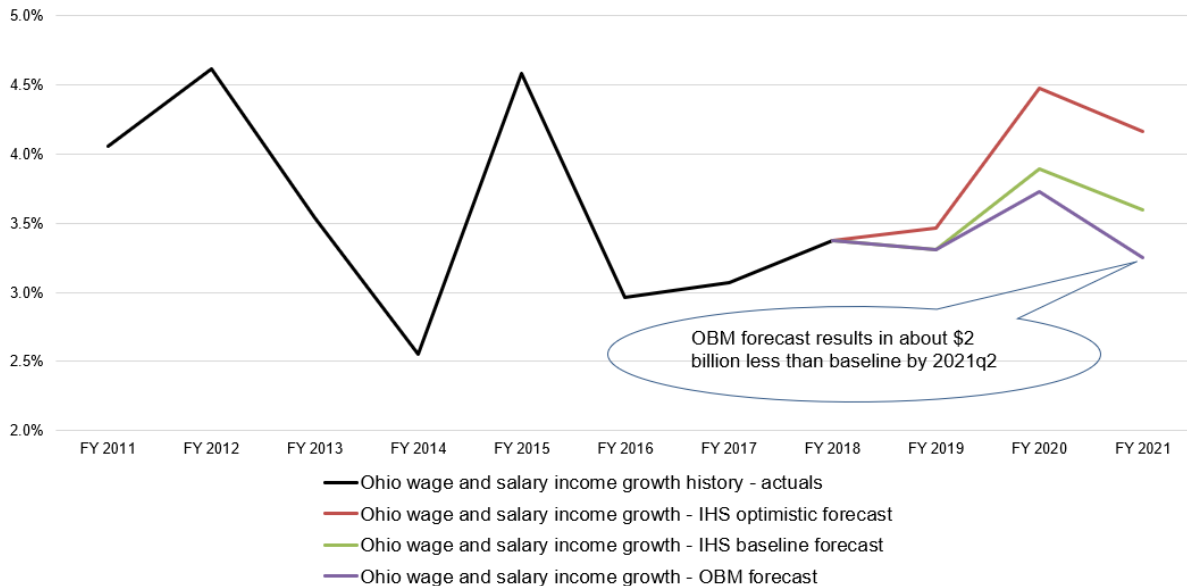


Figure 1

The economic forecast that forms the underlying basis for our revenue forecasts assumes continued economic growth, both nationally and in Ohio. After a recent burst of faster growth, where US real Gross Domestic Product (GDP) rose by 4.2 percent, 3.4 percent, and 2.6 percent in the second through fourth quarters of 2018, OBM expects growth to moderate, averaging 1.9 percent over the ten quarters from 2019 quarter 1 through 2021 quarter 2. This is equal to or very close to most estimates of long-run potential growth in US GDP, including the estimates of the Congressional Budget Office (1.8 percent to 2.0 percent) and IHS Markit (1.9 percent). IHS Markit is OBM's primary supplier of national and state economic forecasts. Our association with this highly respected firm of economists goes back for more than 30 years, back to when the firm emerged from the Wharton School of Business.

The fundamentals for the US economy remain sound.

- Recent gains in wealth, employment, and compensation, along with still-elevated consumer confidence, support solid growth of consumer spending;
- A further increase in housing starts is necessary to accommodate annual household formations, projected at nearly 1.4 million annually;
- Foreign growth has peaked but should still be enough to support U.S. exports (although there is obviously continuing tariff risk to exports);

- Interest rates, while they have risen, remain low, and the Federal Reserve seems to have shifted to a position that is more inclined to keep rates low for longer. This has helped the equity market rebound from its December sell-off, which in turn provides a boost to household consumption.

On the policy side, the federal *Tax Cuts and Jobs Act* is still providing some support to aggregate demand as is the *Bipartisan Budget Act of 2018*. These fiscal policy supports to US growth will continue into early 2020, but soften after that point, becoming one of the factors that leads to a more normalized growth rate forecast for the nation and Ohio in fiscal year 2021 and thereafter.

The current economic expansion, including March, now stands at 117 months. The record for U.S. expansions, according to calculations of the National Bureau of Economic Research (NBER) is 120 months, from March 1991 to March 2001. Our current expansion, if it continues, will thus break the record for the longest US expansion in July of 2019, the first month of our new biennium.

While the length of the expansion may be seen as a warning to some observers, modern economic theory posits that there is no automatic limit to economic expansions. As former Federal Reserve chair Janet Yellen said in late 2015, “I think it's a myth that expansions die of old age.” One of the reasons that economists used to believe that expansions were likely to “die of old age” was the credit lending cycle. For example, there was a belief that as expansions grew longer, memories of the last recession dimmed, lending grew too easy, bad investments were made, defaults occurred, and financial market instability and then a recession followed.

Again, modern economic theory argues that this progression of events is not inevitable, and in fact, I will briefly discuss later that lending does not seem to have become “too easy” as this current expansion has progressed.

Recent History and Forecast: Readers of [OBM's Monthly Financial Report](#) will know that growth in this expansion has been below the average for postwar expansions. Through the first quarter of 2018, GDP growth over the first 35 quarters of the expansion had averaged only 2.2 percent, well below the postwar quarterly average (including recessions) of 3.2 percent. Both growth in the labor force and growth in productivity were relatively low over this expansion, making GDP growth low by historical standards during an expansion. For the last three quarters of 2018, growth shifted upward, averaging 3.4 percent over those quarters, the best three-quarter average since early 2015. The 2.9 percent growth rate for calendar year 2018 tied with 2015 for the best growth rate since 2006.

The consensus among economists is that potential GDP growth is well below the actual 2018 growth rate, and that GDP growth will slow and roughly equal potential growth beginning in 2019.

Federal tax and spending policy was strongly supportive of consumer spending and overall economic growth in calendar year 2018 (consumer spending accounted for 1.8

percent of the 2.9 percent increase in GDP). Federal tax cuts are estimated to have reduced household tax liability by about \$125 billion in 2018, equal to about 1 percent of consumer spending. Even if one assumes that spending did not increase dollar for dollar with the tax reduction, presumably the tax cuts boosted spending by something between 0.5 percent and 1.0 percent. In addition, IHS estimates that increased federal discretionary spending due to the Bipartisan Budget and Consolidated Appropriations Acts of 2018 lifted real GDP growth by about 0.5 percent in 2018.

Taken together, federal tax and spending policy are estimated to have increased growth by about 1.0 percent to 1.5 percent in 2018. If the number was about 1.0 percent, then growth in the absence of stimulative federal policy would have been about 1.9 percent, or what CBO and IHS estimate to be the economy's long-run potential. As the federal spending and tax cut stimulus fades in calendar year 2019, U.S. growth will move back toward its long run rate and this is incorporated in our revenue projections.

Financial Markets: Recent volatility in financial conditions seems to have been fed by slipping confidence in the strength of the global expansion. That stems in part from signs of slowing growth abroad, rising uncertainty over trade barriers, and heightened fears that US interest rate increases would slow growth more than previously expected, perhaps culminating in a recession.

While there is reason for US investors to be concerned about rising risks of a downturn after 2019, the worsening in financial conditions seen in late 2018 appears in hindsight to have been “too much too early” as US growth prospects in 2019 are still solid. Accordingly, equities have rebounded, a rebound which has been helped by the Federal Reserve taking a “wait and see” approach to further interest rate hikes, rather than being inclined to raise rates at predetermined intervals.

Labor Markets and Inflation: IHS and other forecasters expect US labor markets to tighten somewhat further, with the US unemployment rate expected to reach a cyclical – and near-historic – low of 3.6 percent in early 2019, before gradually rising as growth drops below trend. Despite widespread expectations that such a low unemployment rate would lead to very fast wage growth and then to faster price inflation, slowing global growth, weak commodity prices, and steady inflation expectations have been keeping inflation in check. In fact, inflation by a variety of measures slipped from the first half of last year to the second half, thanks in part to steady-to-declining oil prices, after a jump from 2017 levels, and slowing import price inflation as the dollar rose over the year.

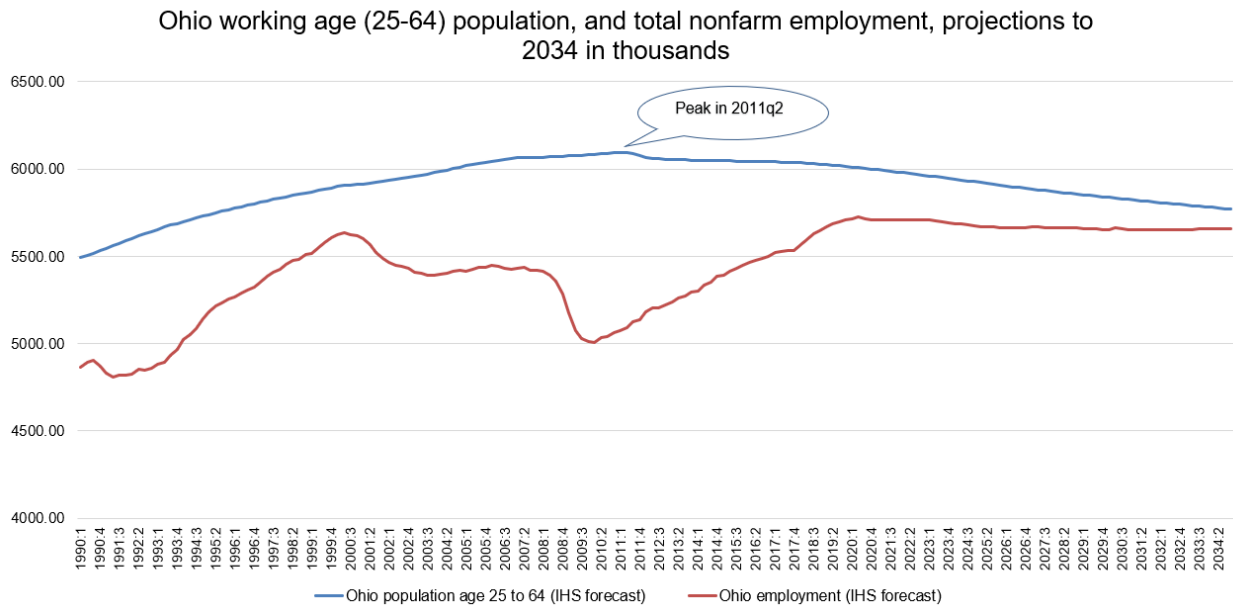


Figure 2

Financial markets were alarmed by the disappointing nonfarm employment gain of only 20,000 in February, as initially reported. However, concerns eased when the March employment gain was reported at 196,000 jobs and the February gain was revised upward to 33,000. Overall, the recent performance of the US labor market has been solid. Even including the weak February, employment gains over the last three months have averaged 180,000 per month, and over the last six months they have averaged 207,000 per month. Both these averages are far above the roughly 100,000 that is needed to keep pace with current growth in the labor force. Although employment growth may be moving to a slower trajectory, growth is still expected to average well above 100,000 per month for the rest of calendar year 2019. In 2020-2021, IHS sees employment growth slowing below 100,000 per month and the unemployment rate rising slightly.

The Bureau of Labor Statistics (BLS) annual benchmark revisions to state labor market data reflected much slower Ohio employment growth in calendar year 2018 than was first reported. Before the benchmark revisions, which were released on March 11th, Ohio nonfarm employment was estimated to have grown by about 116,000 jobs, or 2.1 percent in 2018. That growth was revised downward to only 45,000, or 0.8 percent. Over the last three years, Ohio employment growth has moderated: for 2010-2015, in the first part of the expansion, Ohio job growth averaged 75,000 per year. Over the last three years growth has averaged 42,000 per year. The workforce priorities outlined later in my testimony are a response to this trend.

Interestingly, this slower job growth was forecasted by IHS two years ago. At that time, IHS predicted Ohio job growth of only about 0.5 percent for calendar years 2018 and 2019. The growth of 45,000 jobs in 2018 actually beat that forecast, at 0.8 percent. The reasons behind that slower job growth forecast still hold true today: the Ohio

unemployment rate is very close to what is estimated to be full employment for the state; Ohio is a slow-population growth state; and Ohio's population skews older than the nation's, and so Ohio is more affected by the demographic trend of older workers retiring. These facts about our population and workforce inspire several of the significant policy proposals in Governor DeWine's budget that I will discuss this morning.

The good news is that Ohio income growth and income tax withholding have not been hurt by slower employment growth because average wages per worker have increased enough to offset slower employment growth, and this is forecasted to continue in the upcoming biennium.

Risks to the Forecast: While the baseline economic outlook is for continued growth, and recession probabilities from IHS and other professional forecasters are still relatively low, I would like to briefly discuss the risks to this forecast.

Ongoing trade negotiations with China remain a key risk to the outlook. While the overall effect on the economy from back-and-forth tariff increases and threats appears to have been relatively small thus far, many industries, businesses, and people have been negatively affected. Two recent studies of the impact of US tariffs on imports and retaliatory tariffs by other countries on US exports have found:

- a \$40 billion estimated annual drop in US exports to China as a result of Chinese retaliatory tariffs (from the Institute of International Finance);
- import tariffs were costing US consumers and the firms that import foreign goods an additional \$3 billion per month in added tax costs and another \$1.4 billion dollars per month in deadweight welfare (efficiency) losses.

A speedy resolution to disagreements with China would have a positive influence on the economy, whereas a broadening and escalation in tariffs would likely undermine economic growth. Given the pronounced role of manufacturing and agriculture in Ohio's economy, our state could experience outsized negative impacts from serious and sustained trade tensions and retaliatory actions; conversely, Ohio could greatly benefit from the resolution of trade tensions and the imposition of long-term trade reforms.

Secondly, overseas economic growth has weakened recently, reducing foreign demand for US-made goods and services. The economy of China slowed to 6.6 percent growth in 2018 – the slowest since 1990 – as US tariffs had an impact and as policymakers made efforts to deal with high debt levels. Similarly, the European Commission reduced its growth forecast for the Eurozone in 2019 from 1.9 percent to 1.3 percent, while the timing and nature of Brexit hangs over the region.

Third, monetary policy in the US tightened during 2018. The Federal Reserve raised the range for its policy rate by a full percentage point, to between 2.25 percent and 2.50 percent. It continues to slowly reverse Quantitative Easing by not replacing all the bonds that mature in its portfolio. Federal Reserve officials have indicated that they do not expect to make additional policy changes in the near-term and ultimately will make adjustments in response to developments in the economy. For the time being, inflation

is low and stable and economic growth appears to be moderating, suggesting that no major monetary policy changes are likely soon.

Finally, there is risk from flat or declining asset prices reducing consumer spending growth. Wealthier households are feeling uneasy about the possibility of the long bull market in stocks petering out. Stock prices peaked last fall and have been roughly flat over the past year.

In a rising market, the stock wealth effect on consumption is estimated to be about 1.5 cents—the increase in consumer spending from a \$1 increase in stock wealth. Homeowners are likely also nervously watching the recent slowing in house price growth. The run-up in mortgage rates last year was combined with high house prices in many markets, undermining affordability and demand. House prices have since suffered. When house prices are rising, the housing wealth effect is estimated to be near 3 cents per dollar of appreciation.

When the tailwind to spending from rising stock prices and housing values was at its peak in calendar year 2018, it probably added about 0.5 percentage points to consumer spending growth. This tailwind appears to have been lost and will become a headwind if asset prices decline. The stock and housing wealth effects are substantially larger when prices are falling, a combined 12 cents per dollar of depreciation in value as opposed to the 4.5 cents per dollar of appreciation that I cited above.

This is in part because Baby Boomers, who are retired or approaching retirement, are quick to reduce spending if their retirement savings are reduced. As I alluded to earlier, lenders have remained disciplined in extending credit since the financial crisis. Debt owed by households is increasing but still lags the growth in household income. Households that are tempted to increase their borrowing to finance more spending will find it tough to do so.

Detailed Near-Term Outlook: OBM relies primarily on two sources for the macroeconomic forecasts that underlie our forecasts of GRF tax revenues for this budget. The first source is the forecast of the national and Ohio economies by the economic research and forecasting firm IHS Markit, whose work I have already referenced numerous times. The second source is also an economic research and forecasting firm, Moody's economy.com. The two sets of macroeconomic forecasts used as the foundation of the revenue forecasts were generally in agreement for this budget. For the past several budgets, IHS forecasts of Ohio income growth have been more conservative and generally closer to actual growth, and so OBM chose to use the IHS baseline forecast, as it has done consistently since the FY 2012-2013 budget. It is the IHS baseline forecasts, with certain modifications, that provide the projections of the independent variables that are used in our GRF revenue forecasting equations.

There are thousands of national and state variables in the IHS economic forecasts. OBM pays particular attention to a relatively small group of key variables that either summarize the broad economy or are directly used in the equations that are used to forecast GRF tax revenues. The fiscal years 2019-2021 forecasts for those variables, along with the history for fiscal years 2016-2018, are summarized in the table below.

As noted in table 1, the income variables, which are very important in the forecasting equations for both the auto and non-auto sales tax, and for income tax withholding, have been reduced below the IHS baseline in both fiscal year 2020 and fiscal year 2021.

OBM thought it prudent to hedge the revenue forecasts for major taxes against downside risk by assuming conservative income growth, specifically by assuming Ohio wage and salary income growth would not grow at a faster rate than Ohio gross state product in nominal dollars.

History and IHS/Global Insight Baseline Forecast of Key Economic Variables, FY 2016-2021						
Annual percent change unless otherwise indicated						
	FY 2016 Actual	FY 2017 Actual	FY 2018 Actual	FY 2019 Estimate	FY 2020 Forecast	FY 2021 Forecast
Output						
U.S. Real GDP	1.8	1.9	2.6	2.9	2.2	1.7
Ohio Real GDP	0.2	1.5	1.5	2.2	1.6	0.9
Income						
U.S. nominal personal income	3.5	3.4	4.5	4.3	4.7	4.4
Ohio nominal personal income	2.8	2.6	3.5	3.6	4.2	3.8
Ohio nominal personal income **	2.8	2.6	3.5	3.6	4.0	3.4
Ohio nominal wage and salary income	3.0	3.1	3.4	3.3	3.9	3.6
Ohio nominal wage and salary income (adjusted) **	3.0	3.1	3.4	3.3	3.7	3.2
Employment						
U.S. nonfarm employment	1.9	1.7	1.5	1.6	1.2	0.7
Ohio nonfarm employment ***	1.3	1.0	0.6	1.7	0.7	0.05
U.S. unemployment rate (percentage)	5.0	4.7	4.1	3.7	3.6	3.8
Ohio unemployment rate (percentage)	4.9	5.1	4.9	4.5	4.16	4.23
Consumer Spending						
U.S. real personal consumption expenditure	3.0	2.6	2.5	2.9	2.3	2.1
U.S. nominal personal consumption expenditure	3.6	4.2	4.4	4.7	4.5	4.4
U.S. retail and food service sales	2.6	3.7	5.0	4.8	4.2	3.7
Ohio retail and food service sales	0.5	2.4	4.9	3.5	3.3	3.1
U.S. light vehicle sales (millions of units)	17.52	17.29	17.24	17.00	16.67	16.54
U.S. light vehicle average price (thousands)	\$31.41	\$32.22	\$32.97	\$34.02	\$35.87	\$37.39
** indicates variables from a forecast reduced below the baseline						
*** Ohio employment growth forecasts will be revised lower in the wake of downward revisions to employment growth for FY 2018						

Table 1

GENERAL REVENUE FUND FORECAST

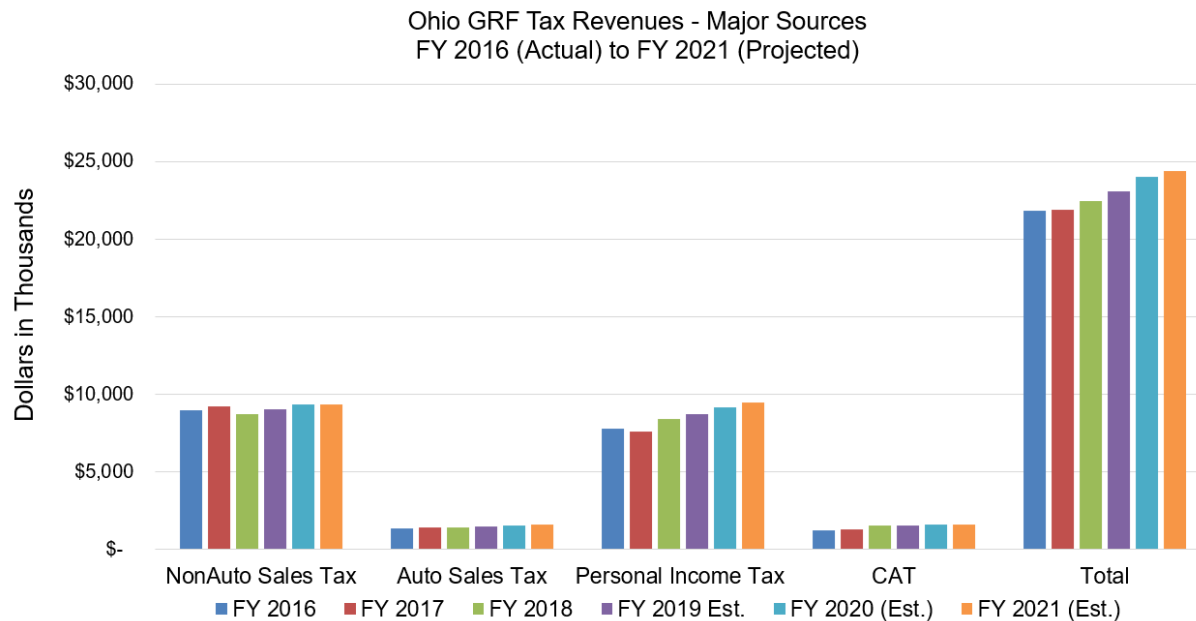


Figure 3

Based on the economic forecast that I have described above, OBM staff, in conjunction with the Department of Taxation, developed the baseline GRF tax revenue forecasts, and then the final GRF tax revenue forecasts after proposed policy changes. These final forecasts support the appropriations in the budget. The baseline revenue forecast provides an estimate of what tax revenues would be if current laws remain unchanged. This is done to isolate the impact of economic changes on the forecasts, as distinct from the impacts of any proposed law changes. Later, I discuss why even the baseline forecast must be adjusted to truly represent economic impacts alone.

The policy proposals that affect tax revenues in this budget are limited, with a small estimated net impact on GRF revenues in fiscal years 2020 and 2021. I will discuss those proposals and their estimated impacts at the end of this section of my testimony. Now I would like to discuss the baseline forecasts.

The baseline GRF tax revenue forecasts would be \$24.02 billion in fiscal year 2020 and \$24.45 billion in fiscal year 2021. The forecasted annual growth rates are 4.0 percent for fiscal year 2020 and 1.8 percent for fiscal year 2021. However, I must discuss three factors that, while they are not strictly law changes within this budget, have a significant impact on revenues that is not due to economic forces and which therefore make the revenue amounts or the growth rates different from what they would be if we considered only economic impacts.

First, a new sales tax exemption that was passed in 2017 with a delayed effective date first affects revenues in fiscal year 2020. This provision exempts eyeglasses and contact lenses from the sales tax, leading to estimated revenue losses of \$43 million in

fiscal year 2020 and \$49 million in fiscal year 2021. Since this was part of existing law, these impacts were included in our baseline forecast.

Second, the previous administration cut income tax withholding rates on January 1, 2019, which creates a *one-time* estimated GRF revenue loss of approximately \$148 million in current fiscal year 2019. While this does not impact forecasted fiscal year 2020 or 2021 revenues directly, it does impact the fiscal year 2020 growth rate, since fiscal year 2019 revenues are lower than they otherwise would have been, which therefore inflates the calculated fiscal year 2020 growth rate.

The third and largest impact is that a federal law change in 2016 with a delayed effective date prevents Ohio (and 6 other states) from continuing to collect sales tax on Internet access charges beginning in fiscal year 2021 (Ohio was collecting sales tax only on business Internet access charges). The estimated GRF loss from this provision is approximately \$188 million in fiscal year 2021 and thereafter.

If not for these state and federal impacts on the income and sales tax in fiscal year 2019-2021, the baseline GRF tax revenue growth rates would have been 3.6 percent, 3.5 percent, and 2.6 percent, respectively, which accords with the economic forecast of continued growth but a slowing in that growth in the second half of fiscal year 2020 and all of fiscal year 2021.

It has been frequently observed that the biggest challenge in forecasting Ohio's baseline GRF tax revenues is forecasting the personal income tax, and that is true once again for this budget. After a difficult fiscal year 2017, employer withholding bounced back in fiscal year 2018, growing by 4.5 percent and finishing \$138 million over estimate. Through the first nine months of fiscal year 2019, withholding growth has remained strong at 4.5 percent and collections are \$82 million over estimate.

Based on the economic forecast of continuing but moderating Ohio income growth, withholding is projected to grow by 4.2 percent in fiscal year 2020 and 3.6 percent in fiscal year 2021. These are what the growth rates would have been in the absence of the recent withholding rate cuts which, as already mentioned, inflate the fiscal year 2020 growth rate.

The most challenging part of forecasting income tax revenue is forecasting non-withholding collections that are based on non-wage income – these include the taxable income streams such as capital gains, interest, dividends, other forms of investment income, and partnership and sole proprietor income (not otherwise deducted under Ohio law).

Data on non-wage income is received from the Internal Revenue Service with a considerable lag. At present, the most recent data that we have is from tax year 2016, while the state is currently receiving revenues based on what happened in tax year 2018. To forecast revenue for this budget, OBM and the Department of Taxation must forecast future non-wage income, and also estimate what income is at present, because as mentioned above the IRS data is two years old. Thus, there is no return data

available to help explain the drop in estimated payments in December and January of this fiscal year.

As described in recent editions of the OBM Monthly Financial Report, estimated payments have fallen 22 percent from last year and are \$157 million below estimate. This drop in estimated payments from a year ago is a widespread phenomenon among the states but was not observed in federal revenues. This suggests that the estimated payment drop in the states is at least in part tied to the new \$10,000 limitation on the state and local tax deduction in federal law, since this affects taxpayer behavior at the state level but not the federal level.

OBM and the Department of Taxation have been working with colleagues in other states, with CPAs, and with economists at the Congressional Budget Office to estimate how much of the estimated payment decline might be from a change in taxpayer behavior related to the state and local tax deduction limit and how much might be due to other factors such as the December stock market selloff and its impact on capital gains income in taxable year 2018. So far, neither we in Ohio nor analysts in other states have come to firm conclusions on this question. It is possible that some of the estimated payment shortfall from December and January may be made up in larger than estimated April payments of tax due. Early April collections show tax due payments running well above last year, but refunds are coming in above last year's levels as well.

Going forward, for fiscal years 2020 and 2021, OBM has chosen to use conservative forecasts of the various components of non-wage income to hedge the overall income tax forecasts against downside risk. OBM's income tax revenue forecast is for baseline revenues to grow 4.9 percent in fiscal year 2020 and 3.4 percent in fiscal year 2021. Again, as I have mentioned before, due to the withholding rate cut, the fiscal year 2020 growth appears to be much higher, at 6.8 percent, but this is because the withholding cut depresses fiscal year 2019 revenues below where they otherwise would have been.

Throughout fiscal year 2019, both the non-auto sales tax and the auto sales tax have been running well above estimate, in part because the fiscal years 2018-2019 estimates were quite conservative due to the poor performance of the non-auto tax in fiscal year 2017. After adjusting for the repeal of the sales tax on Medicaid managed care premiums at the end of fiscal year 2017, non-auto sales tax revenue growth in fiscal year 2019 has been running at about 5 percent, or 2.0 percent above estimate, since the forecasted growth rate was in the 3 percent to 3.5 percent range. While this has been a pleasant surprise, OBM does not expect growth of 5 percent to continue. The expected growth of wage and salary income for fiscal years 2020-2021 is in the 3.2 percent to 3.7 percent range, and it seems unreasonable to expect sales tax revenue to outstrip income growth by more than a percent over an extended period.

OBM and the Department of Taxation suspect that the reduction in federal withholding tax rates that began in February 2018 has boosted personal spending and sales tax revenues for the last year, but that spur to growth rates is likely to fade, since the year-to-year comparisons now include lower withholding rates in the prior year.

One wild card in the non-auto revenue forecasts is the impact of Internet sales, especially in the wake of the U.S. Supreme Court ruling in *Wayfair vs. South Dakota* in June 2018. Ohio has not passed an economic nexus statute like that of South Dakota for sales tax, so it is not mandatory for all out-of-state sellers to remit Ohio sales tax. Still, OBM has noticed that tax collections from out-of-state sellers have grown by double digits in the July through February period.

Thus, at least temporarily, Internet sales seem to have flipped from being a drag on overall sales tax revenues – due to many of them not being taxable and taking market share from brick and mortar sales - to now being a boost. How long this impact may persist would be speculation at this point, and so OBM has chosen to be conservative in its forecast of non-auto sales tax growth over the biennium.

Before adjusting for the new optical aids exemption and the expected loss from the repeal of the tax on Internet access charges, OBM's baseline growth rates for the non-auto sales tax were 3.5 percent in fiscal year 2020 and 2.6 percent in fiscal year 2021, consistent with the view that the national and Ohio economies both will grow more moderately over the course of the biennium.

Auto sales tax growth rates, which need no adjusting to get an accurate picture of the baseline, have also been growing by between 4.5 percent and 5 percent in fiscal year 2019, despite a drop in unit sales of new vehicles. Auto tax revenues have been boosted by a switch from cars to higher priced light trucks, which now make up approximately 70 percent of new unit sales, and increases in the average price of used vehicles. OBM sees growth in the auto sales tax slowing as well, declining to 3.6 percent in fiscal year 2020 and 3.0 percent in fiscal year 2021. This is still good performance given that unit sales have probably peaked for this economic cycle.

The final GRF tax forecast that I would like to discuss in some detail this morning is the commercial activity tax, or the CAT. After a slow start to fiscal year 2019, CAT revenues have done very well, and are now \$30 million over estimate and have grown by 7.0 percent from last year. Growth in the second and third quarters of the fiscal year has been very strong, above 10 percent, and the CAT has been growing at over 5 percent annually since the first quarter of 2015.

As I have described with the income and sales taxes, OBM's analysis indicates that current performance is a peak, from which growth will continue to level-off in the upcoming biennium. CAT revenues are expected to grow by 2.8 percent and 1.9 percent in fiscal years 2020 and 2021, respectively. One of the reasons that OBM is cautious in its forecast of CAT revenue growth is that tax credits against the CAT have grown sharply in fiscal year 2019.

Although this fiscal year growth in the tax base has been strong enough to lead to growth of over 5 percent in net tax after credits, this is likely not sustainable in the longer run if credit growth continues.

OBM's overall forecast for GRF tax revenue growth in fiscal year 2020 is 4.0 percent, with growth falling to 1.8 percent in fiscal year 2021. Once again, that sharp decrease in

fiscal year 2021 is partly the result of the expected \$188 million revenue loss due to the elimination of the sales tax on Internet access charges. Without that change, and without the new exemption for optical aids and the withholding rate cut in the second half of fiscal year 2019, forecasted GRF tax revenue growth would have been 3.5 percent and 2.6 percent, closely aligned with the expected slowdown in overall economic growth.

Before leaving the discussion of revenues, I would briefly like to discuss proposed policy changes and their expected impact on GRF tax revenues. There are four policy changes that affect GRF tax revenues, two are changes to tax law and two do not affect tax law *per se* but will have revenue impacts. Two of these four proposals are aimed directly at improving the health of Ohioans, particularly young Ohioans.

With regards to tobacco, the budget contains one proposal that affects GRF tax revenues, an increase in the age at which Ohioans can legally buy tobacco products and vapor products from 18 to 21. The increase in the purchase age from 18 to 21, a proposal which has been adopted in at least 450 local jurisdictions and twelve states, is expected to reduce tobacco and sales tax revenues, by \$17.1 million in fiscal year 2020 (3/4 year impact) and \$22.7 million in fiscal year 2021.

The second proposed health policy change affecting GRF tax revenues is an income tax credit for lead abatement. This proposed credit would apply to expenses incurred by individuals for the assessment and abatement of lead existing within the painted surfaces of homes. Credit-eligible dwellings must have been placed into service before 1960 and must be occupied by a child under the age of six or by a woman of child bearing age. Credit application would be made with the Director of the Department of Health, who would administer the tax credit in conjunction with the Tax Commissioner. The tax credit is nonrefundable, and the total amount of annually-issued credits is capped at \$5 million, which is therefore our annual estimated revenue loss.

The third proposed policy change is a nonrefundable personal income tax credit on investments by individuals into qualified Opportunity Funds operating within Ohio Opportunity Zones – there are over 300 of these zones across Ohio.

The proposal builds upon the new federal Opportunity Zone tax incentive to leverage additional investment into areas of Ohio that have experienced economic challenges. The federal incentive is most beneficial to investors who put money into the zones now and then hold the investment for 10 years. Creating a state-level credit in the near future will provide an important inducement to steer investments to Ohio zones. Communities nationwide are competing for these investments, most of which will be made in the near-term. Tax credit applications will likely follow a similar pattern, with most investors applying in the first year. The first and largest impact of this tax credit would be in fiscal year 2021, and OBM conservatively estimates a \$30 million reduction in taxes.

The fourth and final policy proposal with a revenue impact is the simplest, namely allowing the Public Library Fund (PLF) to continue to receive 1.68 percent of GRF-deposited tax revenues rather than reverting to 1.66 percent as scheduled under current

law. This proposal would decrease GRF revenues and increase PLF revenues by \$5.0 million per year in fiscal years 2020-2021.

The estimated net impacts of these four proposals are tax reductions of \$27.0 million in fiscal year 2020 and \$62.8 million in fiscal year 2021. These net changes are enough to reduce the GRF growth rates by a tenth of a percent each year, from 4.0 percent and 1.8 percent to 3.9 percent and 1.7 percent. Again, because the income tax withholding tables were adjusted recently, the percent change from 2019 to 2020 is inflated due to a one-time reduction in current fiscal year 2019.

The resulting forecasted total state GRF tax revenues for this budget are \$23.99 billion in fiscal year 2020 and \$24.39 billion in fiscal year 2021.

TRANSPORTATION BUDGET IMPACT ON THE OPERATING BUDGET STATE APPROPRIATION LIMITATION CALCULATION

Since the introduction of House Bill 166, Amended Substitute House Bill 62, the fiscal years 2020-21 transportation budget, was enacted, and it includes provisions that affect the GRF framework for the operating budget. These changes were not anticipated in the as-introduced version of House Bill 166, so it is now appropriate to address the opportunity for updating calculations.

The Executive Budget document, “the Blue Book,” included the required calculation of the State Appropriation Limitation, sometimes called “the SAL.” As a refresher, the SAL was enacted 2006 and seeks to limit the growth of most GRF appropriations to 3.5 percent. The limit is “recast” every fourth year based on the previous fiscal year’s General Revenue Fund appropriations. Fiscal Year 2020 is a SAL “recast” year, and thus our current fiscal year 2019 is the year used as the base for the next four-year period.

HB 62 includes a provision permitting the OBM Director to adjust fiscal year 2019 appropriations to account for the 27th pay period for state employees. This is a pay period that occurs during fiscal year 2019 but, because of how the state processes payroll, was originally scheduled to be paid in fiscal year 2020. OBM is currently working to make the allowable adjustment to fiscal year 2019 appropriations, which will result in approximately \$83.1 million in additional GRF paid this year; OBM assesses that it would be appropriate to increase the fiscal year 2019 SAL base by this amount to account for updating the fiscal year 2019 GRF appropriation.

House Bill 62 also includes \$70 million in GRF appropriations per year for public transportation and \$35 million in GRF appropriations in fiscal year 2021 for Highway Patrol Operating Expenses. The statute for the SAL allows for the limit to be adjusted

when expenses are moved from non-GRF to GRF appropriations in certain instances. In reviewing this statute and examining the HB 62 changes, OBM concludes that it would be appropriate for the SAL to be increased by \$33 million of the \$70 million annual appropriation for public transportation for fiscal years 2020 and 2021 and by the entire \$35 million in fiscal year 2021 appropriation for Highway Patrol in accordance with ORC 107.033 (D). As each of these items was previously funded by non-GRF sources, the SAL could be adjusted accordingly.

Taken together, the changes made in the transportation budget change the SAL calculation by increasing the base. When these adjustments to the SAL base are taken into consideration, the recommended GRF appropriations in HB 166 remain below the limit in fiscal years 2020 and 2021.

The final provision that was included in the transportation budget that has operating budget implications is a change to the state earned income tax credit (EITC). In HB 62, the state EITC was increased from 10 percent to 30 percent of a taxpayer's federal EITC, and a provision was repealed that limited the credit to be no more than 50 percent of the tax liability of taxpayers with taxable income over \$20,000. OBM estimates these changes to the state EITC will reduce state GRF income tax revenue by \$38.7 million in fiscal year 2020 and \$39.4 million in fiscal year 2021.

FISCAL YEARS 2020-2021 BUDGET PRIORITIES

Ohio's strong economy and the forecast for steady, but moderating, growth provide us with a key opportunity to invest in Ohio today for a stronger, self-sufficient tomorrow. I will now shift from discussing our economic and revenue forecasts to a discussion of the priorities outlined in Governor DeWine's Executive Budget.

Recommended appropriations are made across 813 funds that are grouped by similarity of purpose into 14 budget fund groups. The largest budget fund group by far consists of only one fund, the General Revenue Fund. The GRF receives most general-purpose tax revenues of the state and is the fund where the state has the most discretion in resource allocation. The second largest fund group is Federal, which receives the state's federal revenue, with the notable exception of federal revenue for Medicaid expenditures paid from the GRF which are deposited back into the GRF.

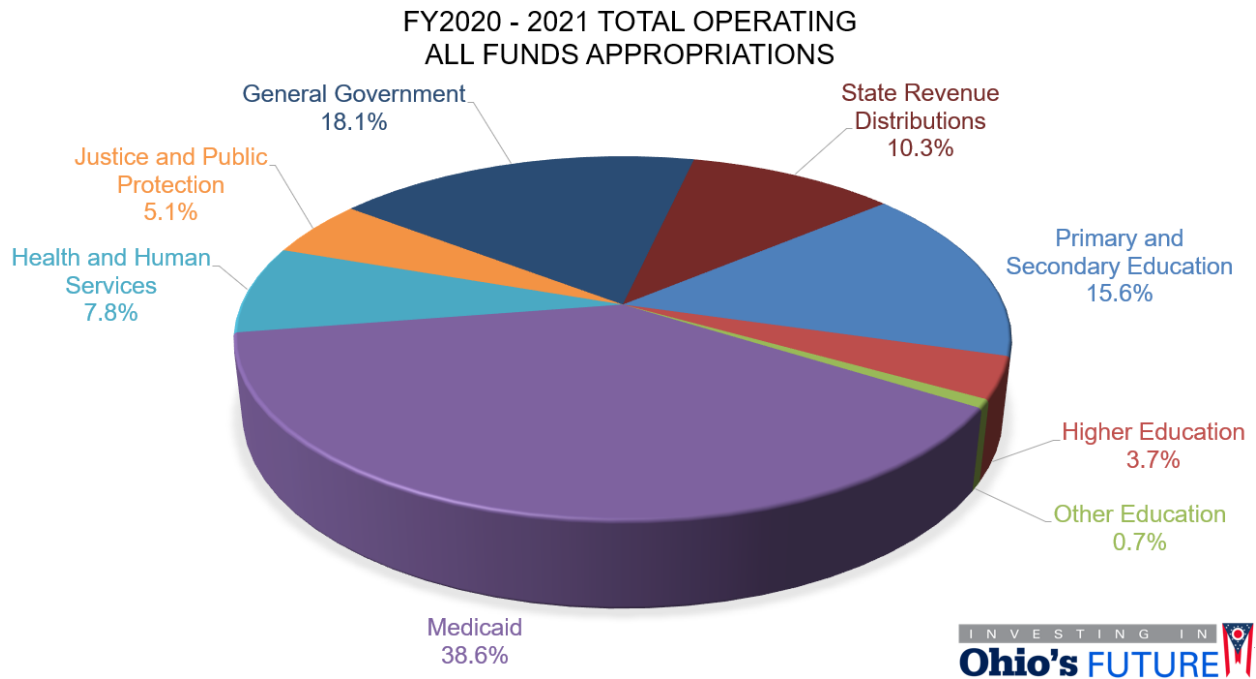


Figure 4

Figure 4 summarizes budget appropriations for all funds by category. The budget recommends total agency appropriations of \$74.3 billion in fiscal year 2020, and \$76.1 billion in fiscal year 2021. In dollar terms, the “all funds” budget grows by \$3.3 billion in fiscal year 2020 and \$1.8 billion in fiscal year 2021. About 41 percent of the growth in the all funds budget is in the Medicaid program.

As you can see, the largest category of all-funds expenditures is the Medicaid program at 38.6 percent, followed by General Government, and Primary and Secondary Education.

FY2020 - 2021 OPERATING BUDGET
TOTAL GENERAL REVENUE FUND APPROPRIATIONS

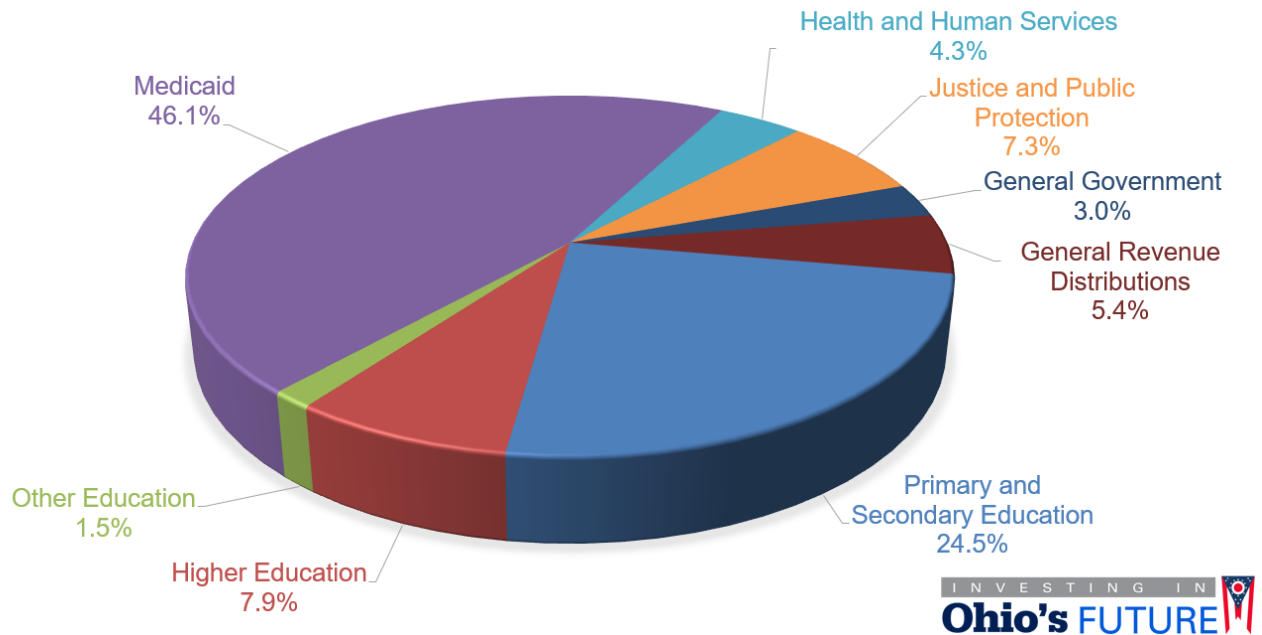


Figure 5

GRF Funds Appropriations (dollars in millions)

Function	FY 2019 Estimate	FY 2020 Rec	% Change	FY 2021 Rec	% Change
Primary and Secondary Education	\$ 8,117.5	\$ 8,431.5	3.9%	\$ 8,441.4	0.1%
Higher Education	\$ 2,596.9	\$ 2,686.8	3.5%	\$ 2,774.0	3.2%
Other Education	\$ 505.4	\$ 519.9	2.9%	\$ 531.0	2.1%
Medicaid	\$ 14,825.6	\$ 15,213.5	2.6%	\$ 16,569.3	8.9%
Health and Human Services	\$ 1,350.5	\$ 1,464.5	8.4%	\$ 1,496.1	2.2%
Justice and Public Protection	\$ 2,314.6	\$ 2,491.3	7.6%	\$ 2,575.7	3.4%
General Government	\$ 975.4	\$ 1,030.1	5.6%	\$ 1,052.0	2.1%
General Revenue Distributions	\$ 1,814.8	\$ 1,845.1	1.7%	\$ 1,863.6	1.0%
Total	\$ 32,500.6	\$ 33,682.8	3.6%	\$ 35,303.0	4.8%

Table 2

The budget recommends GRF agency appropriations of \$33.7 billion in fiscal year 2020 (a 3.6 percent increase over fiscal year 2019 estimated spending), and \$35.3 billion in fiscal year 2021 (4.8 percent). In dollar terms, the GRF budget grows by \$1.2 billion in fiscal year 2020 and \$1.6 billion in fiscal year 2021. As discussed in detail later in my testimony, the two largest areas of growth in the GRF budget are Medicaid and Primary and Secondary Education.

Note that total GRF appropriations in figure 5 and table 2 include the federal Medicaid revenue that is deposited into the GRF.

Finally, for the clearest picture of how this budget allocates our discretionary resources, we must examine the State Only GRF appropriations, depicted in figure 6 and table 3. As you can see, when the Federal Medicaid revenues are removed from the picture, it is clear that this budget directs the largest proportion of discretionary funds towards Primary and Secondary Education (34.6 percent). On a percentage basis, the largest increase is for Health and Human Services (8.4 percent change from fiscal year 2019 to fiscal year 2020), largely for priorities investing in Ohio’s children and families.

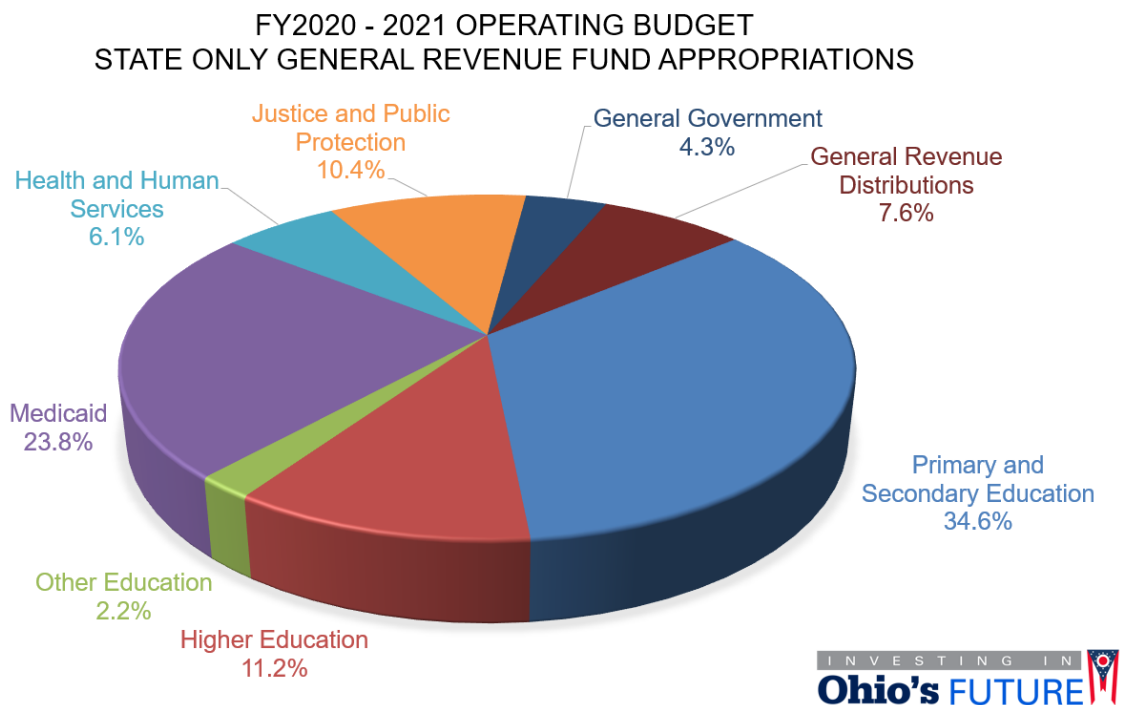


Figure 6

State Only GRF Appropriations (dollars in millions)

Function	FY 2019 Estimate	FY 2020 Rec	% Change	FY 2021 Rec	% Change
Primary and Secondary Education	\$ 8,117.5	\$ 8,431.5	3.9%	\$ 8,441.4	0.1%
Higher Education	\$ 2,596.9	\$ 2,686.8	3.5%	\$ 2,774.0	3.2%
Other Education	\$ 505.4	\$ 519.9	2.9%	\$ 531.0	2.1%
Medicaid	\$ 5,192.7	\$ 5,517.5	6.3%	\$ 6,113.2	10.8%
Health and Human Services	\$ 1,350.5	\$ 1,464.5	8.4%	\$ 1,496.1	2.2%
Justice and Public Protection	\$ 2,314.6	\$ 2,491.3	7.6%	\$ 2,575.7	3.4%
General Government	\$ 975.4	\$ 1,030.1	5.6%	\$ 1,052.0	2.1%
General Revenue Distributions	\$ 1,814.8	\$ 1,845.1	1.7%	\$ 1,863.6	1.0%
Total	\$ 22,867.7	\$ 23,986.9	4.9%	\$ 24,846.9	3.6%

Table 3

Primary and Secondary Education Recommendations: Governor DeWine’s budget invests in all Ohio children by continuing to provide over \$8 billion per year in foundation funding, and adds new, targeted funding of [\\$250 million](#) in fiscal year 2020 and \$300 million in fiscal year 2021 to support student wellness and success in schools. Schools will receive additional funding for mental health counseling, “wraparound” supports, mentoring, after school programs, and more. Schools will be encouraged to partner with local organizations including Alcohol, Drug, and Mental Health Boards; Educational Service Centers; County Boards of Developmental Disabilities; community-based mental health treatment providers; local health departments; local Department of Job and Family Services; and non-profits with experience serving children. By addressing barriers to success and providing these targeted resources, we can give all our students the opportunity for a brighter future.

Funding will be distributed to schools on a per pupil basis determined by census poverty data. The per pupil dollar amounts will range on a sliding scale from \$20 to \$250 in fiscal year 2020 and from \$25 to \$300 in fiscal year 2021. Each school district, joint vocational school district, and community school will receive a minimum of \$25,000 in fiscal year 2020 and \$30,000 in fiscal year 2021.

This budget also continues to support school options for students and families, including funding to expand the existing Ed Choice program that provides income-based scholarships for students in poverty to attend private schools. The increase of \$9.5 million in fiscal year 2020 and \$13.8 million in fiscal year 2021 will allow program to expand to sixth grade in fiscal year 2020 and to seventh grade in fiscal year 2021.

This budget will allow the Department of Mental Health and Addiction Services to work with the Department of Education and our schools to consistently and continually educate children in Kindergarten through 12th grade on the dangers of drug, alcohol, and tobacco use and teach them the skills — through a much-needed focus on social-emotional learning — on how to make healthy decisions throughout their lives.

This budget recognizes that our students today are our highly-skilled workforce of tomorrow. We owe it to our high school students to provide them with pathways to high-skill, in-demand jobs. There are currently over 148,000 open jobs on [Ohiomeansjobs.com](#), 81,000 of which pay over \$50,000 per year. The budget allocates \$50 million over the biennium for high school students to earn industry credentials to dramatically grow the number of high school students that graduate job-ready with this key to success. These life-changing skills enable 10,000 students to be self-sufficient, productive adults – this is the future workforce that our employers desperately seek.

Some Ohio schools lack qualified teachers to teach computer science and coding classes. These important courses prepare our kids for the future and expose them to different job opportunities. This budget dedicates \$1.5 million to develop training and subsidize teachers to become certified computer science educators.

This budget also funds a high school technology-related internship program to expose high school students to technology professions like coding, data analytics, entrepreneurship and innovative problem-solving. Development Services Agency will

recruit companies and high school students and extend the matchmaking process that has been successful in other internship programs. Companies that take on an intern will receive reimbursement. This initiative will expand upon an earlier program by including high school students, creating opportunities for young people who may never have known these jobs even existed. This program will be particularly focused on students with diverse backgrounds.

Higher Education: This Executive Budget invests in students. We know that providing the appropriate education or training and making it accessible and affordable is paramount to success. Our future depends on our ability to ensure that students of all backgrounds can learn about and become skilled in high-demand areas, including computer science and STEM disciplines. That is why our higher education budget invests an additional \$46 million to prioritize access to a college education for our neediest students through increased financial aid. Our investments directly to students through the Ohio College Opportunity Grant will raise the per-student awards by \$400 in fiscal year 2020 and \$500 in fiscal year 2021.

But even with this boosted assistance for tuition, oftentimes students continue to struggle, due in some part to the substantial cost of textbooks. Of the \$46 million added to OCOG, \$6 million will be allocated for qualifying students to purchase textbooks and instructional materials.

This budget also targets funds to approximately 2,500 additional students enrolled in the critical STEM disciplines – science, technology, engineering, math, and medicine – by doubling the Choose Ohio First Scholarship, this budget prioritizes awards for underrepresented populations.

Medicaid Program: As you know, Medicaid spending occurs through the Department of Medicaid and seven “sister agencies:” the Departments of Aging, Developmental Disabilities, Health, Job and Family Services, Mental Health and Addiction Services, Education, and the Pharmacy Board. While all eight agencies support the administration of the program, the majority of Medicaid expenditures are made by the Department of Medicaid.

The recommended all-funds appropriations for the Medicaid program total \$28.38 billion in fiscal year 2020, or 4 percent higher than the fiscal year 2019 estimate. The fiscal year 2021 recommended all-funds appropriations total \$29.67 billion, or 4.5 percent over fiscal year 2020. These amounts account for all cost drivers such as program enrollment in the managed care, fee-for-service, and premium assistance programs; program costs per-member-per-month (PMPM); and other expenses not directly related to enrollment or PMPM.

These include managed care pay-for-performance expenses, the hospital care assurance program (HCAP), hospital and hospital-based physician upper payment limit (UPL) program costs, and program administration.

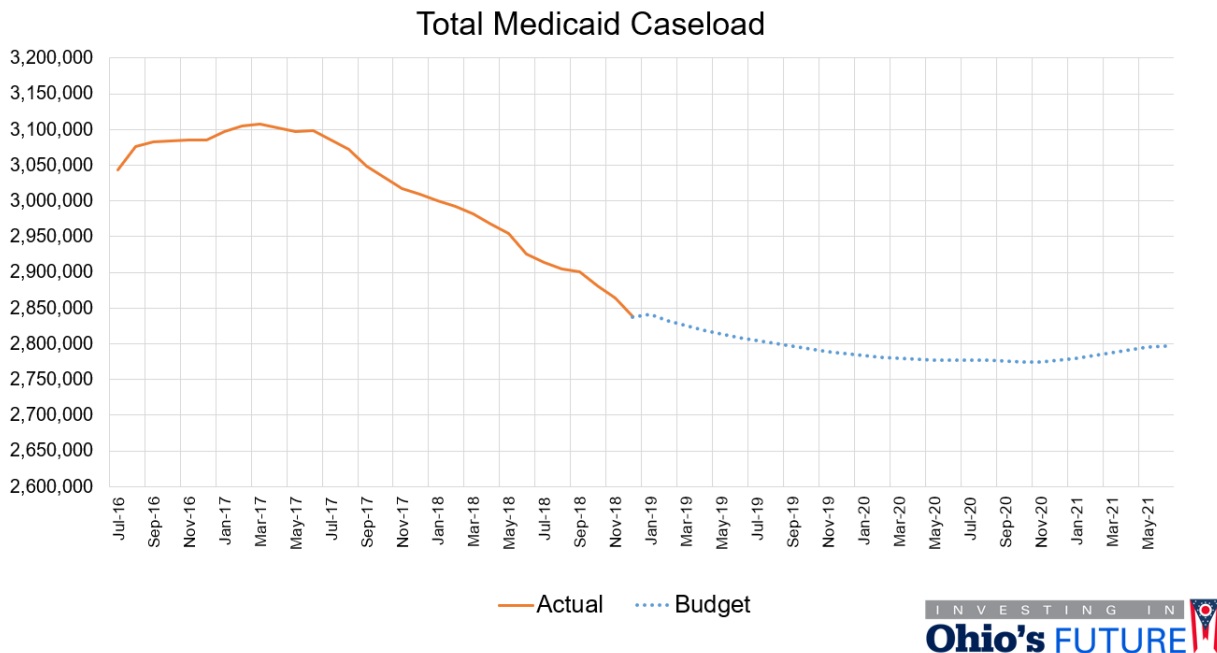


Figure 7

The recommended state-share GRF Medicaid appropriation is \$5.52 billion in fiscal year 2020, or 6.3 percent higher than the fiscal year 2019 estimate; and \$6.11 billion in fiscal year 2021, or 10.8 percent higher than fiscal year 2020. These annual percent changes, greater than the all-funds annual percent changes, reflect two important factors in the coming biennium.

First is the greater financial responsibility of the state due to lowering federal medical assistance percentage, or FMAP, for the Children’s Health Insurance Program and the Affordable Care Act Expansion population, also known as Group VIII, in both fiscal years 2020 and 2021. Second is the decelerating of revenue growth in the second year of the coming biennium in state dedicated purpose funds which are used to off-set GRF spending.

Across all Medicaid agencies, the state was responsible for 31.7 percent of all Medicaid expenditures in fiscal year 2018. In fiscal year 2019, this percentage remains relatively stable at an estimated 31.6 percent. However, in fiscal year 2020, it is estimated to rise to 32.5 percent and to 33.2 percent in fiscal year 2021.

Medicaid enrollment, also called caseload, is made up of two large groups: those who are eligible due to their family income – these include covered families and children, and the Group VIII expansion population – and persons eligible due to their health condition, generally referred to as the aged, blind and disabled (ABD).

Although the ABD caseload is generally not influenced by economic conditions, the remainder of the Medicaid caseload is inversely correlated to economic performance. As the economy improves, the caseload decreases and vice versa. While the caseload has been declining with the improved economy over the last few years, economic

forecasts do not indicate continued decline. The budget assumes continued declines in caseload, but at a more moderate rate, with a small increase at the end of the second year of the biennium. This is in line with the macroeconomic forecasts used for the revenue forecasts that I discussed earlier this morning.

The Department of Medicaid, along with its sister agencies, will engage in several program improvements in the coming biennium. These initiatives, which Medicaid Director Corcoran will describe in detail during her upcoming testimony, will include healthy moms and babies' initiatives, expanding the use of telehealth in schools, developing strategies and programs to better serve at-risk youth who are being served by multiple government programs, and expanding behavioral health care coordination.

To help manage program costs, the budget includes eliminating a Revised Code section that allows for the nursing facility per diem rates to be inflated with a Medicare skilled nursing facility market basket of services index beginning in fiscal year 2020. Eliminating this requirement is expected to save \$75 million in fiscal year 2020, and \$165 million in fiscal year 2021.

In addition, the Department of Medicaid's Bureau of Program Integrity is proposing a series of rule and procedure changes that are designed to eliminate inconsistencies in fee-for-service billing, streamline financial reporting and audits, improve communications between health care providers and the Department, and expand the use of data analysis to discover fraud and waste.

Pursuant to the Revised Code, the Medicaid director must submit a budget that limits the growth of the program on a per member, per month basis to a rate established by the Joint Medicaid Oversight Committee or a three-year average of the consumer price index, whichever is lower. In December, JMOC established the rates for fiscal years 2020 and 2021 at 3.3 percent and 3.4 percent, respectively. These rates were determined after the committee received a report from its actuary firm which projected Medicaid program growth over this period.

I am very happy to report to this Committee today that the Executive Budget complies with this requirement.

Workforce and Innovation:

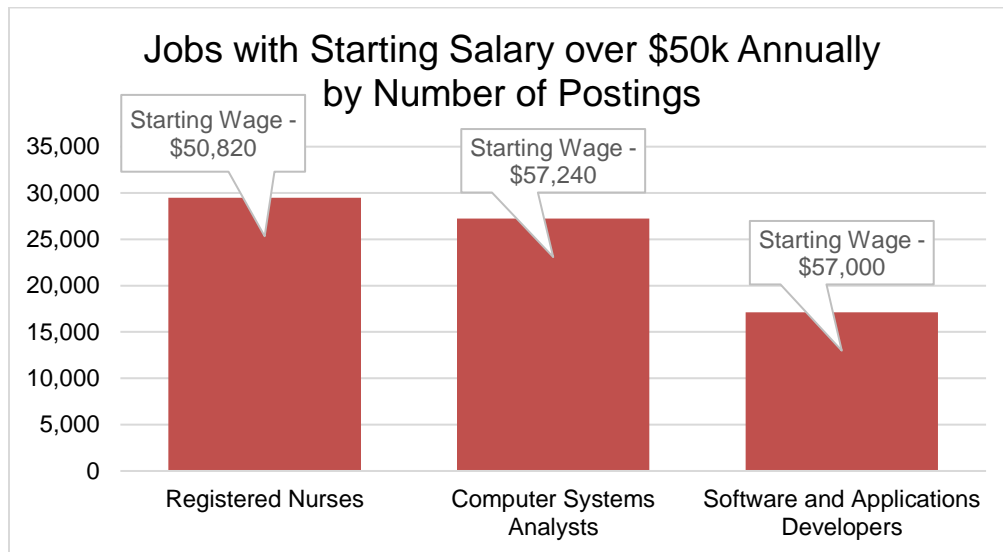


Figure 8

Governor DeWine’s budget is focused on knocking down the barriers that stand in the way of a better life for all Ohioans. We focus on creative, new strategies to restore hope and increase opportunity, and technology is the key that unlocks this door. The DeWine Administration will lead an aggressive, innovative path to build a better Ohio by encouraging job training and workforce innovations, streamlining regulations and modernizing the way government operates, and encouraging research, investment, and development.

We are aggressively investing in our workforce. Our budget dedicates \$15 million in each year of the biennium for an aggressive workforce and retraining effort. Our goal is for at least 10,000 Ohioans to achieve new in-demand industry certifications over each of the next two years. These certificate programs, sometimes called “short-term” certificates – take just a few weeks to a few months to achieve and are focused on jobs that our employers need – often in the medical or technology fields. As I mentioned earlier in my testimony, Ohio currently has over 81,000 open jobs that pay over \$50,000 per year. Now is the time to invest in our workforce to compete nationally and internationally in the markets of today and the future. In the past, the biggest impediment for businesses seeking to locate or to expand in Ohio was our tax structure; however, today the biggest challenge is hiring qualified, skilled workers for these high-paying jobs.

This budget also seeks to invest \$2.5 million per year through the Development Services Agency in Industry Sector Partnerships to establish regional job-training partnerships with local businesses, education providers, and community leaders. These partnerships will give people the skills they need to compete and win in the 21st century. Currently, there are more than 75 job training programs across 12 state agencies. The Administration will work to better coordinate these efforts so we can improve services and funding streams.

Through workforce programming and collaborative inter-agency partnerships, we will also eliminate employment barriers for persons with disabilities. Ohio has a shocking number of citizens with disabilities who are unemployed or underemployed. This is unacceptable. One of Governor DeWine's first acts was to issue an Executive Order that establishes Ohio as a Disability Inclusion State and model employer of individuals with disabilities. Our goal, through this budget, is to encourage and support individuals with disabilities to fully participate in the social and economic life of Ohio and engage in integrated employment. This budget invests \$5.0 million into new initiatives that increase employment opportunities for approximately 3,822 persons with disabilities, matching an additional \$28 million in federal funds.

This budget also improves government services and efficiencies. InnovateOhio, led by Lieutenant Governor Husted, looks at every state service through the eyes of our customers -- Ohio citizens and job creators. InnovateOhio is taking a leading role in technology projects across the state as we invest considerable resources to improve state agency operations to reduce inefficiencies in state government. It will coordinate projects across our administration and use data to change the way we solve problems.

InnovateOhio already is working to better collect and use data across agencies in important areas involving the opioid crisis, workforce development, and children's initiatives. For an investment of \$25 million across the biennium, InnovateOhio will continue its important work to make Ohio a state that attracts talent, business, and new investment and development.

We will also continue to focus on eliminating redundant governmental regulations by reviewing business-impacting rules and helping businesses navigate regulatory obstacles. Ohio's best tech companies and creative entrepreneurs will modernize state and local government, improve customer service and save tax dollars - which will benefit every Ohioan.

Investing in our Local Communities: Governor Mike DeWine understands that local governments are our partners in providing critical services to our citizens. That is why the budget expands state funding for indigent defense by \$60 million per year to help ensure that individuals charged with a crime receive counsel as is their Constitutional right. Governor DeWine recognizes the state shares that responsibility with our local partners to ensure that there is justice for all, which is why he is proposing unprecedented support for indigent defense.

Providing this substantial support for counties addresses a pressing need in the criminal justice system while also alleviating budget pressures by freeing-up county general funds to be used for other purposes.

The proposed budget will boost the state's child protective services allocation by \$30 million per year for a total of \$90 million annually. [As reported by The Columbus Dispatch in March](#), county child welfare agencies have borne a disproportionate share of the burden of the drug epidemic. Counties are stretched thin because of the rapid increase in the number of children in the system because of the substance use disorder

crisis. These local agencies have asked us for help, and Governor DeWine has prioritized this investment in this budget.

The budget proposes funding for maintaining existing drug task forces and creating three new drug task forces that will be focused on cartel trafficking. Spending for existing task forces will improve from \$8 million per year to \$13.9 million in 2020 and 2021. Funding is also provided for local law enforcement to expand the number of investigations conducted on sexual assault kit testing results.

The proposed budget will also provide funding for courts that do not have their own probation departments to establish local probation departments in lieu of utilizing state parole officers. This allows for local control and operation of probation departments and for probation departments to better address the specific needs within their local criminal justice system.

Authorizing local governments to extend Tax Increment Financing (TIFs) terms up to an additional 30 years for larger, high impact developments is also included in the budget proposal. TIFs redirect additional real estate taxes created by new development to construct infrastructure needed by that development. Extensions are not automatic – it is ultimately up to the local legislative body to extend a TIF that meets all qualifications for extension.

RecoveryOhio: Governor DeWine has made it clear that one of his priorities is to repair Ohio's broken system for treating those with mental health and substance use disorders. Currently, every county in Ohio and every city, town and village – urban and rural – is affected by the current drug epidemic. One study indicates the impact of the drug epidemic costs Ohio nearly \$9 billion a year.

The DeWine Administration through this budget, and with guidance from the RecoveryOhio Advisory Council, is proposing to invest more than \$200 million in new initiatives over the biennium that will increase the access and efficacy of prevention and treatment resources across the state; that will continue Governor DeWine's support of Ohio's criminal justice system; and that will provide the supports necessary for Ohioans to remain in recovery and continue their active roles in society.

Governor DeWine's budget proposes investing more than \$50 million in new funding over the biennium in support of prevention related initiatives and resources. As I mentioned earlier when discussing Primary and Secondary Education, the budget proposes investing \$20 million over the biennium in a partnership with the Department of Mental Health and Addiction Services, the Ohio Department of Education, and local partners to provide evidence-based K-12 prevention materials and curriculum to Ohio's schools and students. By teaching kids age-appropriate lessons, this Administration knows that Ohio can get ahead of the current drug epidemic.

In addition to support at school, Governor DeWine wants to expand early intervention programs that target families and children at home. This budget proposes investing an additional \$12 million over the biennium to expand the OhioSTART (Sobriety, Treatment, and Reducing Trauma) program. OhioSTART emphasizes intervention with

the whole-family, with a focus on children, and provides critical wrap-around services that help ensure Ohio's affected families stay together and stay at home.

The budget proposes investing \$28 million over the biennium to create new and amplify existing education, treatment, and prevention campaigns across the state; expand Mental Health First Aid certified Ohioans; and to provide support for local law enforcement who respond to mental health crisis situations by developing additional crisis intervention teams.

This proposal invests more than \$80 million over the biennium in support of treatment services for those suffering from substance use disorder. This includes \$22 million over the biennium to develop and expand crisis services infrastructure and to provide flexible funding resources to local communities to invest in direct crisis stabilization and crisis prevention supports. By improving access and strengthening community linkages, these additional resources will assist local communities in their efforts to help families respond to the strains caused by behavioral health issues.

While expanding access to treatment, this budget also proposes addressing Ohio's shortage of critical specialists to ensure that there are capable individuals in the workforce who can treat Ohioans affected by mental illness and substance use disorder. This budget proposes developing a student loan forgiveness program for critical specialists who complete their studies at Ohio universities and spend time working in the addiction field in Ohio.

While providing treatment and prevention services are crucial components to combating the drug epidemic, Governor DeWine's budget proposal also continues the State's efforts to support the role of the criminal justice system and the various initiatives designed to assist and empower local law enforcement in the fight against the drug crisis as well as efforts to divert non-violent drug offenders to proven treatment programs rather than jail.

The budget also seeks to expand investments in proven criminal justice reform efforts by proposing an investment of an additional \$7.0 million over the biennium to create and support at least 30 more specialized docket courts across Ohio, ensuring participation in effective behavioral health treatment while diverting non-violent drug offenders from Ohio's prisons.

Children and Families: Governor Mike DeWine cares deeply about Ohio's children and is committed to ensuring that all children have opportunities for success. Young Ohioans should reach adulthood with the tools to be self-sufficient, with the skills to hold high-wage jobs, and with the opportunity to seek better education.

Tragically, more children than ever before are facing abuse and neglect, often due to a parent's struggle with substance abuse. These kinds of adverse childhood experiences are linked to a heightened likelihood of depression, substance abuse, and even decreased life expectancy.

This budget will nearly double state funding for family and children's services by increasing our investment from \$77 million to \$151 million annually. This investment

demonstrates Governor DeWine’s strong commitment to making sure all kids grow and succeed. Governor DeWine wants to invest in evidence-based home visiting programs to give children the best possible start in life. More participation in these proven programs will lower infant mortality rates, improve kindergarten readiness, and enhance parenting skills.

The budget proposes investing an additional \$30 million over the biennium, bringing the total state funding for home visiting to \$50 million. For every dollar invested in Home Visiting Programs, there is an estimated \$6 in return. Strong children grow into strong adults, so an investment in these proven programs is an investment in our state’s future.

Finally, as Governor DeWine has addressed numerous times, Ohio needs to do more to protect children from lead exposure. Every year, thousands of Ohio children under the age of six test positive for unsafe lead levels. Undoubtedly, there are countless more who have never been tested at all and would test positive. Governor DeWine recommends a multi-pronged approach to dealing with lead exposure including holding providers and managed care organizations accountable for testing all eligible children. Currently just 60 percent of Medicaid-eligible children are tested each year. Lead screenings for eligible children will continue to be a Medicaid-billable service. This budget also invests an additional \$24 million for the Department of Developmental Disabilities’ Early Intervention Program to help provide physical, speech, and occupational therapy services to children who have dangerously high levels of lead in their blood. And as I mentioned in the discussion of tax credits earlier in my testimony, this budget creates a lead abatement income tax credit with a maximum of up to \$10,000 for eligible individuals who have incurred expenses to make their homes lead-safe.

Ohio’s Natural Wonders: I would like to end my testimony this morning with a discussion of Ohio’s natural resources. As Governor DeWine emphasized in his State of the State address, Ohio is blessed with natural wonders and we must invest in their preservation and protection –including Lake Erie and all our lakes and rivers. From aging infrastructure to failing septic systems to nutrient pollution to lead contamination, communities throughout Ohio face significant and complex water problems. Our water problems have compounded over many years, and it will take a dedicated, long-term commitment to achieve real solutions.

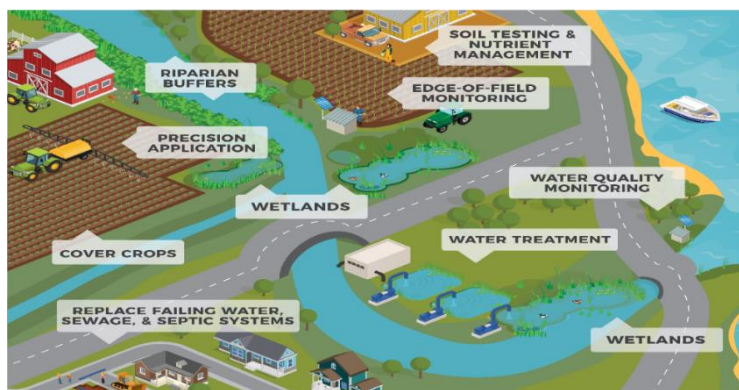


Figure 9

To protect Ohio’s water resources, the Executive Budget creates the H₂Ohio Fund. This new fund will provide the resources necessary to plan for, develop, and implement targeted, long-term solutions to ensure safe and clean water across the State of Ohio. The fund will focus on new and continuing efforts in the Western Lake Erie Basin and support water initiatives all across our great state. Efforts from the Ohio River on our southern border to Lake Erie to our north will include land management practices; green infrastructure, including wetlands redevelopment; community clean water projects; and the research and monitoring necessary to track progress and enable investment in efforts that deliver results.

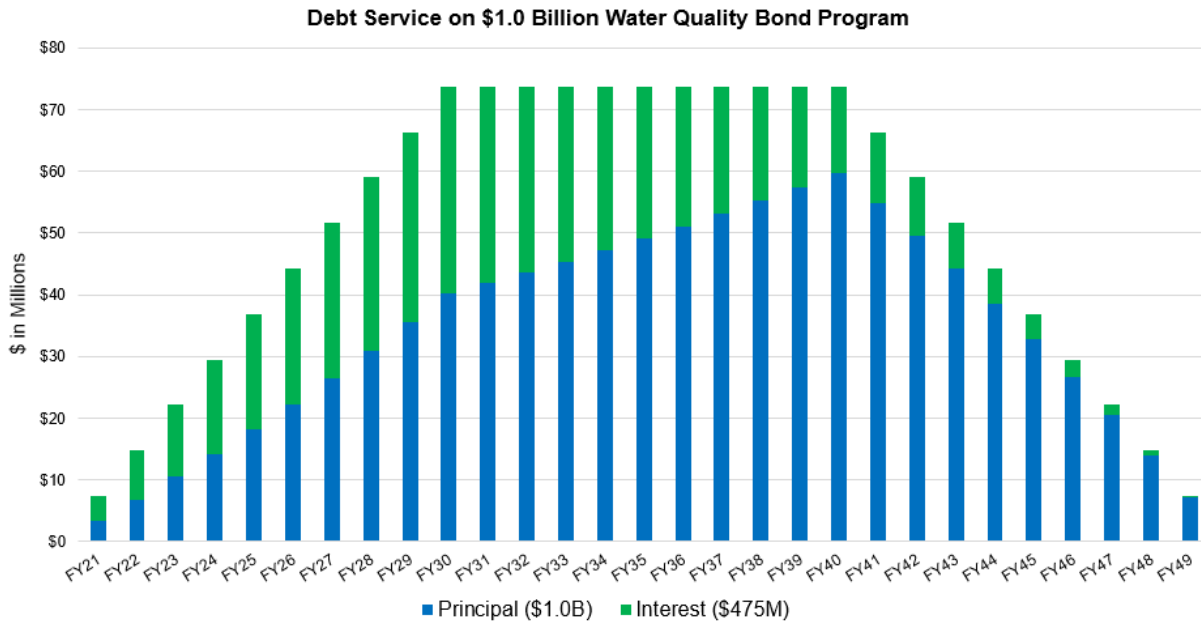


Figure 10

House Bill 166, as introduced, includes estimated deposits of \$903.6 million over the next three fiscal years from unobligated ending year cash balances (surpluses). By establishing a dedicated purpose fund for this critical economic resource, we assure all Ohioans that we will have the funds necessary to address these issues over the next decade. We will use science – not politics – to determine the future investments that will make the most difference. The proposal to direct these funds to the H₂Ohio program is a conservative affordability-based funding approach that offers significant savings relative to alternative funding proposals based on debt financing. If Ohio were to instead elect to issue \$1 billion in bonds for this purpose, the interest payments would total almost \$475 million over the life of the bonds. Clean, safe water is critical to our health and to our future economic development and now is the time to protect our water quality. These natural resources drive our economy.

CONCLUSION

Mr. Chairman, members of the Committee, I appreciate the opportunity to review *Investing In Ohio's Future*, Governor DeWine's Executive Budget for fiscal years 2020 and 2021. This is a conservative, balanced budget with no new taxes.

To reiterate our revenue forecast, each of the major taxes except the income tax are forecasted to be essentially flat or to experience more measured forecasted growth rates in fiscal year 2020 compared to fiscal year 2019:

- the non-auto sales tax slows from 3.9 percent to 2.9 percent,
- the auto sales tax slows from 4.2 percent to 3.6 percent,
- the CAT growth rate stays almost the same, going from 2.7 percent to 2.8 percent.
- The income tax, after adjusting for the fiscal year 2019 withholding loss, accelerates from 4.0 percent to 4.9 percent.

OBM's track record for forecasting GRF tax revenues is to be consistently conservative. Our forecast is not aggressive. In fact, average revenue growth for fiscal years 2011 through 2018 was 4.2 percent per year (this factors-in each of the tax cuts during that period). If not for the state and federal impacts on the income and sales tax in fiscal year 2019-2021 that I discussed in detail, the baseline GRF tax revenue growth rates would have been 3.6 percent, 3.5 percent and 2.6 percent, respectively, which accords with the economic forecast of continued growth – but a slowing in that growth in the second half of fiscal year 2020 and all of fiscal year 2021.

This measured, steady growth provides the foundation for the key strategic investments in Governor DeWine's budget priorities that I have outlined today. With these investments, Ohio's economy will remain strong and grow stronger in the future for our children and for generations to come. It is imperative that we address these priorities today to solidify our workforce and economic base for future growth.

I know that my testimony today has provided but a brief overview of the important investments included in this budget. Each member of the Cabinet and I look forward to working together with each of you as the Senate considers the budget proposal. I thank you for your time and consideration. As Governor DeWine said in his State of the State Address – now is the time to tackle our unfinished business. Now is the time to invest.

I am happy to answer any questions you may have today.

Actual and Estimated Revenues for the General Revenue Fund
Fiscal Years 2018 to 2021
(dollars in millions)

Revenue Source	Actual			Estimated			
	FY 2018	FY 2019	% Chg	FY 2020	% Chg	FY 2021	% Chg
<u>Tax Revenue</u>							
Auto Sales and Use	\$1,440.5	\$1,501.4	4.2%	\$1,555.0	3.6%	\$1,601.8	3.0%
Non-Auto Sales and Use	8,707.6	9,050.0	3.9%	9,317.0	2.9%	9,364.2	0.5%
Subtotal Sales and Use	10,148.2	10,551.4	4.0%	10,872.0	3.0%	10,966.0	0.9%
Personal Income	8,411.0	8,600.0	2.2%	9,179.0	6.7%	9,472.0	3.2%
Corporate Franchise	2.2	0.0	-100.0%	0.0	N/A	0.0	N/A
Financial Institutions Tax	201.1	211.0	4.9%	200.0	-5.2%	200.0	0.0%
Commercial Activity Tax	1,522.8	1,564.6	2.7%	1,608.4	2.8%	1,639.6	1.9%
Petroleum Activity Tax	7.8	8.0	2.0%	8.0	0.0%	8.0	0.0%
Public Utility	119.2	138.0	15.7%	135.0	-2.2%	135.0	0.0%
Kilowatt Hour Tax	342.4	353.0	3.1%	337.7	-4.3%	331.1	-2.0%
Natural Gas Consumption	69.6	69.5	-0.1%	69.5	0.0%	69.5	0.0%
Foreign Insurance	276.5	277.0	0.2%	277.0	0.0%	277.0	0.0%
Domestic Insurance	278.4	289.6	4.0%	301.2	4.0%	313.2	4.0%
Business and Property	0.2	0.0	-100.0%	0.0	N/A	0.0	N/A
Cigarette	939.8	927.4	-1.3%	895.1	-3.5%	873.4	-2.4%
Alcoholic Beverage	55.7	55.0	-1.2%	56.0	1.8%	56.0	0.0%
Liquor Gallonage	48.1	49.0	1.8%	50.0	2.0%	51.0	2.0%
Estate	0.2	0.0	-85.0%	0.0	-100.0%	0.0	N/A
Total of Tax Revenue	22,423.2	23,093.5	3.0%	23,988.9	3.9%	24,391.8	1.7%
<u>Non-Tax Revenue</u>							
Earnings on Investments	64.2	100.0	55.7%	110.0	10.0%	130.0	18.2%
Licenses and Fees	59.2	58.3	-1.4%	58.3	0.0%	58.8	0.8%
Other Income	250.4	74.7	-70.2%	77.7	4.0%	78.3	0.8%
Interagency Transfers	15.7	15.8	0.9%	13.2	-16.6%	9.0	-31.8%
Total of Non-Tax Revenue	389.5	248.8	-36.1%	259.2	4.2%	276.1	6.5%
<u>Transfers In</u>							
Transfers In	188.6	309.6	64.2%	250.9	-19.0%	291.7	16.3%
Total Sources Excl. Federal Grants	23,001.3	23,652.0	2.8%	24,498.9	3.6%	24,959.6	1.9%
Federal Grants	9,469.9	9,615.8	1.5%	9,679.5	0.7%	10,437.5	7.8%
Total Sources	32,471.2	33,267.8	2.5%	34,178.5	2.7%	35,397.1	3.6%

Appendix 1

BASELINE General Revenue Fund Tax Revenues
Fiscal Years 2018 - 2021
(dollars in millions)

Note: FY20 and FY21 "baseline" amounts do not include the Executive Budget tax policy proposals.

Tax Revenue Source	Actual FY 2018	Estimated FY 2019	FY18-19 % Chg	Baseline FY 2020	FY19-20 % Chg	Baseline FY 2021	FY20-21 % Chg
Auto Sales and Use	\$1,440.5	\$1,501.4	4.2%	\$1,555.0	3.6%	\$1,601.8	3.0%
Non-Auto Sales and Use *	8,707.6	9,050.0	3.9%	9,322.2	3.0%	9,370.7	0.5%
Personal Income	8,411.0	8,600.0	2.2%	9,184.0	6.8%	9,507.0	3.5%
Commercial Activity Tax	1,522.8	1,564.6	2.7%	1,608.4	2.8%	1,639.6	1.9%
Kilowatt Hour Tax	342.4	353.0	3.1%	340.2	-3.6%	333.6	-1.9%
Foreign Insurance	276.5	277.0	0.2%	277.0	0.0%	277.0	0.0%
Domestic Insurance	278.4	289.6	4.0%	301.2	4.0%	313.2	4.0%
Cigarette and Other Tobacco	939.8	927.4	-1.3%	909.4	-1.9%	892.1	-1.9%
Other Taxes	504.1	530.5	5.2%	518.5	-2.3%	519.5	0.2%
Total *	\$22,423.2	\$23,093.5	3.0%	\$24,015.9	4.0%	\$24,454.5	1.8%

PROPOSED General Revenue Fund Tax Revenues
Fiscal Years 2018 - 2021
(dollars in millions)

Note: FY20 and FY21 "proposed" amounts include the Executive Budget tax policy proposals.

Tax Revenue Source	Actual FY 2018	Estimated FY 2019	FY18-19 % Chg	Proposed FY 2020	FY19-20 % Chg	Proposed FY 2021	FY20-21 % Chg
Auto Sales and Use	\$1,440.5	\$1,501.4	4.2%	\$1,555.0	3.6%	\$1,601.8	3.0%
Non-Auto Sales and Use *	8,707.6	9,050.0	3.9%	9,317.0	2.9%	9,364.2	0.5%
Personal Income	8,411.0	8,600.0	2.2%	9,179.0	6.7%	9,472.0	3.2%
Commercial Activity Tax	1,522.8	1,564.6	2.7%	1,608.4	2.8%	1,639.6	1.9%
Kilowatt Hour Tax	342.4	353.0	3.1%	337.7	-4.3%	331.1	-2.0%
Foreign Insurance	276.5	277.0	0.2%	277.0	0.0%	277.0	0.0%
Domestic Insurance	278.4	289.6	4.0%	301.2	4.0%	313.2	4.0%
Cigarette and Other Tobacco	939.8	927.4	-1.3%	895.1	-3.5%	873.4	-2.4%
Other Taxes	504.1	530.5	5.2%	518.5	-2.3%	519.5	0.2%
Total *	\$22,423.2	\$23,093.5	3.0%	\$23,988.9	3.9%	\$24,391.8	1.7%

*Although reflected in the baseline and proposed amounts shown above, there are two fiscally significant, previously-enacted tax policy changes scheduled to take effect during the fiscal year 2020-2021 biennium. Taking effect in fiscal year 2020 is a sales tax exemption for purchases of prescription eyeglasses and contact lenses, amounting to an estimated \$43 million revenue loss in fiscal year 2020 and \$49 million revenue loss in fiscal year 2021. In addition, effective in fiscal year 2021 is a provision in a federal law enacted in 2016 (P.L. 114-125) that prohibits a state or local government from subjecting internet access charges to sales tax. Ohio has been one of seven states allowed to continue to tax such services (via a "grandfather clause") because these states' taxes on such services had pre-dated the original Internet Tax Freedom Act (P.L. 105-277) enacted in 1998. The grandfather clause was repealed by the 2016 federal law, although such repeal was delayed until July 2020. Exempting such transactions from taxation is expected to reduce GRF non-auto sales tax revenue by \$187.5 million in fiscal year 2021. If not for these two enacted policy changes, total baseline GRF tax revenues would have grown by an estimated 4.2 percent in fiscal year 2020 and 2.6 percent in fiscal year 2021, and total proposed GRF tax revenues would have grown by an estimated 4.1 percent in fiscal year 2020 and 2.5 percent in fiscal year 2021.

Appendix 2

Expenditures and Appropriations by Budget Fund Group
FYs 2019, 2020, 2021

Budget fund groups are categories used to group similar funds for reporting purposes. Ohio's funds are categorized according to their revenue sources and the purposes for which they are used. Budget Fund Group definitions can be found on Ohio's Interactive Budget website (interactivebudget.ohio.gov).

Budget Fund Group	FY 2019 Estimate	FY 2020 Executive Recommendations	% Change	FY 2021 Executive Recommendations	% Change
General Revenue	\$ 32,500,599,515	\$ 33,682,848,698	3.6%	\$ 35,302,977,008	4.8%
Federal	\$ 15,219,973,722	\$ 15,863,969,321	4.2%	\$ 15,821,847,056	-0.3%
Fiduciary Funds	\$ 7,372,586,184	\$ 7,876,822,732	6.8%	\$ 8,047,798,746	2.2%
Dedicated Purpose	\$ 5,842,689,081	\$ 6,358,596,151	8.8%	\$ 6,239,260,413	-1.9%
Highway Operating	\$ 2,763,158,834	\$ 3,566,987,698	29.1%	\$ 3,610,952,391	1.2%
Revenue Distribution Funds	\$ 2,419,162,791	\$ 2,175,599,080	-10.1%	\$ 2,168,786,773	-0.3%
State Lottery	\$ 1,481,468,398	\$ 1,500,225,454	1.3%	\$ 1,556,653,052	3.8%
Debt Service	\$ 1,245,092,422	\$ 1,294,465,929	4.0%	\$ 1,346,005,462	4.0%
Internal Service Activity	\$ 1,014,452,155	\$ 1,052,956,439	3.8%	\$ 1,060,399,333	0.7%
Highway Safety	\$ 539,943,162	\$ 584,693,868	8.3%	\$ 593,007,136	1.4%
Capital Projects	\$ 370,986,777	\$ 107,994,491	-70.9%	\$ 123,209,947	14.1%
Bond Research and Development	\$ 122,310,250	\$ 122,310,250	0.0%	\$ 122,310,250	0.0%
Holding Account	\$ 72,701,483	\$ 70,989,479	-2.4%	\$ 70,989,479	0.0%
Facilities Establishment	\$ 37,500,000	\$ 37,500,000	0.0%	\$ 37,500,000	0.0%
Grand Total	71,002,624,774	74,295,959,589	4.6%	76,101,697,046	2.4%

Appendix 3