Senate Education Committee
Interested Party Testimony - House Bill 96
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Chair Brenner, Vice Chair Blessing, Ranking Member Ingram, and members of the Senate Education Committee, thank you for the opportunity to present testimony today on House Bill (HB) 96, the Fiscal Year (FY) 26-27 biennial budget. My name is Howard Fleeter, and I am the research consultant for the Ohio Education Policy Institute (OEPI). For those of you who are not familiar with my background, I have a PhD in Economics from the University of California, Berkeley, I spent 10 years as a Public Policy professor at The Ohio State University, and I have been researching school funding and education policy in Ohio for over 30 years. My career working with Ohio policymakers began when Governor Voinovich commissioned me to write my report "Equity, Adequacy and Reliability in Ohio Education Finance" which I completed in November 1992. My research on school funding in this report was cited in the landmark March 24, 1997 *DeRolph I* decision which ruled Ohio's school funding system unconstitutional. This ruling was reaffirmed in 3 subsequent Court decisions.

At this point in time it is fairly well understood that LSC simulations of the House version of the FY26-27 Budget have shown that none of Ohio's traditional school districts will experience a reduction in foundation formula funding over the FY26-27 biennium compared to current levels of funding, which is a significant improvement over the Executive version of the Budget where 349 school districts experienced a reduction in foundation over the FY26-27 biennium. The House version of the budget is certainly an improvement from the perspective of Ohio's traditional public schools, however, it is important to note that the House budget maintains the framework of the foundation funding formula proposed in the Executive Budget. This framework extended the phase-in of the formula to years 5 and 6 (FY26 and FY27) but did not update the input data used to compute the base cost. As shown in fairly exhaustive detail in my testimony provided in the House Education and House Finance committees in March, the failure to update the inputs and the subsequent decline in the state share of funding is the primary reason why so many districts lost funding under the Executive Budget.

Having said this, my testimony here today will not focus on the funding formula. That is not because I do not think that this issue is important, but rather because there is another issue of even greater importance. My objective here today is to discuss the 30% Cash Balance provision included in the House version of the budget and explain why I consider it to be one of the most problematic policy proposals that I have seen in the more than 30 years I have spent researching and analyzing school finance in Ohio.

The 30% Cash Balance Cap

While the concerns raised above about the future of the school foundation formula are certainly of fundamental importance, this is not, however, the item of greatest concern for Ohio school districts contained in the House version of the FY26-27 budget. The House budget includes a provision which would direct county budget commissions to reduce property tax millage rates by the amount necessary to reduce school property taxes by the dollar amount equal to the excess of district's cash balance beyond a maximum of 30% of operating expenditures. To be clearer, if a district's cash balance is $1 million more than the amount that would be equal to 30% of their expenditures then the budget commission is directed to lower property tax rates by the amount needed to reduce property tax revenues by $1 million.

This policy initiative is extremely problematic in several different ways.

A. Immediate Impact on District Property Taxes

Based on FY24 cash balance data, 485 districts have a cash balance above 30% of operating expenditures and these districts stand to lose $4.259 billion in property tax revenue. FY25 data shows 478 districts above 30% with $3.730 billion property tax revenues at risk. However, in both years the required cash balance reductions to get to the 30% maximum allowable share of expenditures is more than total property tax current expense collections in over 100 school districts. This means that the initial "Year 1" reduction in property taxes will be lower than the figures cited above, but it also means that over 100 districts will face a mandatory reduction in property taxes over the span of multiple years. Table 1 summarizes these figures.

Table 1: FY24 & FY25 Cash Balance Summary

	FY24 Actual	FY25 Estimated
Total Cash Balance	$10.472 Billion	$10.162 Billion
Current Year Expenditures	$22.699 Billion	$24.117 Billion
Statewide Avg. % Cash Balance	46.1%	42.1%
# of Districts Above 30%	485	478
Total Required Cash Balance Reduction	$4.259 Billion	$3.730 Billion
# of Districts Required Reduction Greater than Total Property Taxes	113	105
Cash Balance Reduction Year 1	**$3.753 Billion**	**$3.281 Billion**

Source: Calculations by Howard Fleeter for OEPI

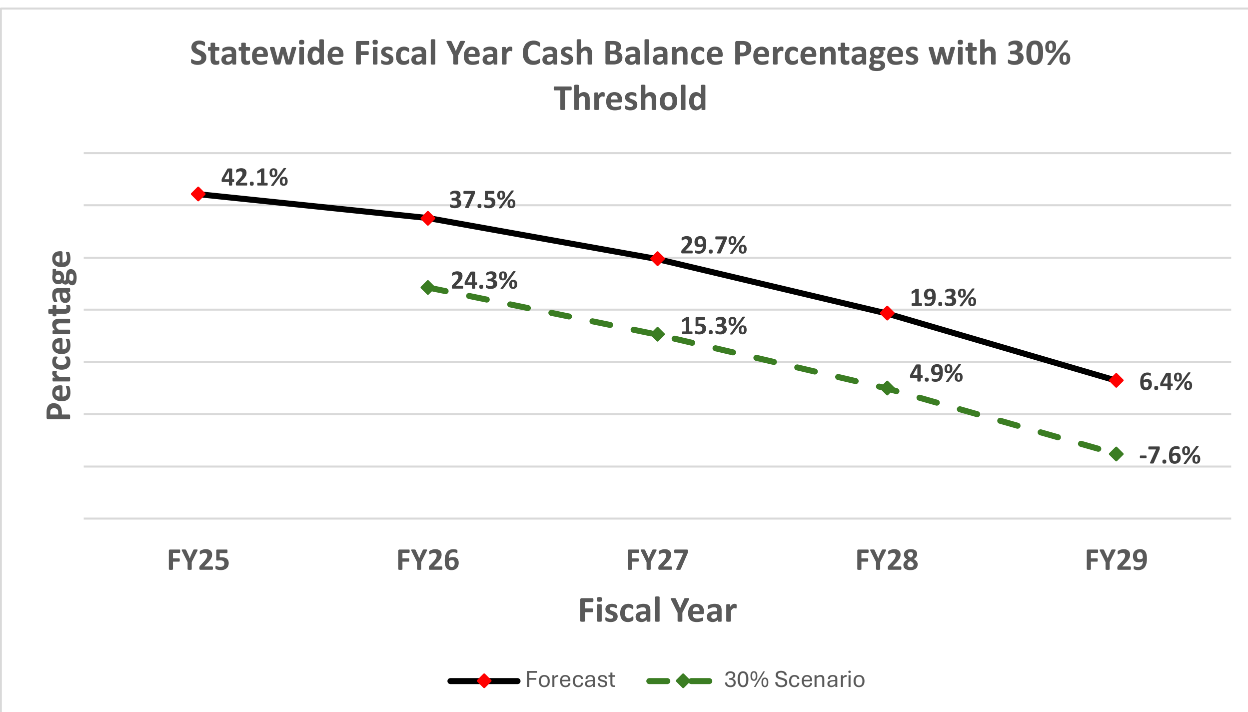
Table 1 shows that the estimated reduction in property taxes will be $3.753 billion in Year 1 if FY24 cash balances are used as the basis for the 30% cap. The estimated reduction in taxes will be $3.281 billion in Year 1 if FY25 cash balances are the basis for the reduction. ***Both of these local revenue loss figures dwarf the increase in state foundation formula funding provided in the House version of the budget***.

B. Ongoing Impact on District Property Taxes

The next point to understand is that the impact of the 30% cash balance maximum will persist over several years even in school districts where the mandatory property tax reduction occurs only in Year 1. The reason for this is that the reduction in tax revenues, which is designed to get each district in the position of having a cash balance not greater than 30% of their operating expenditures, will influence their cash balance situation in the subsequent years. This issue can be illustrated by using the FY25-FY29 cash balance and expenditure projections contained in the 5 Year Forecast submitted by all districts to DEW in October 2024.

Assuming that the 30% cash balance cap included in the House-passed version of the FY26-27 budget would use FY25 as the base year, OEPI estimated the impact of this provision from FY25 through FY29. The reduction in property taxes required for districts with an FY25 cash balance in excess of 30% of their FY25 expenditures will be felt in FY26 and the years after. OEPI subtracted the reduction in property taxes required to get to the 30% cash balance maximum from the estimated cash balance figures shown in each school districts 5 Year Forecast in FY26 and beyond. This reduced cash balance was then compared to forecast expenditures. The results of this analysis are shown in Figure 1 and Tables 2 and 3 below.

Figure 1: FY25-FY29 Statewide Percentage of Cash Balance to Expenditures, As Projected in 5 Year Forecast and Under 30% Cash Balance Cap Provision



Source: DEW Data Analyzed by OEPI

Figure 1 compares the statewide total cash balance as a percentage of total school district operating expenditures from FY25 through FY29 as projected in the most recent November 2024 5 Year Forecast and as projected by OEPI under the 30% cash balance cap. The solid line in Figure 1 shows that according to school district 5 Year Forecast projections, statewide total cash balance as a percentage of operating expenditures is projected to fall from 42.1% in FY25 to 6.4% by FY29. The dashed line in Figure 1 shows the OEPI projection of cash balance as a percentage of operating expenditures under the 30% cash balance cap. Figure 1 clearly shows that cash balances will be significantly lower under the 30% cap provision, with statewide total cash balances in FY29 becoming a negative number.

Table 2 shows the projected impact of the 30% cash balance cap from FY25 through FY29.

Table 2: Impact of 30% Cash Balance Cap, FY25-FY29

Measure	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**
# of Districts > 30% of Operating Expenditures	478	212	96	46	29
# of Districts < 30% of Operating Expenditures	131	397	513	563	580
# of Districts < 25% of Operating Expenditures	**87**	**235**	**397**	**496**	**541**

Source: Calculations by OEPI

The top row of Table 2 shows the number of districts estimated to be above the 30% cash balance maximum from FY25 through FY29. After the first year of required reductions, 212 districts remained above the 30% cash balance cap threshold in FY26. By FY29 the number of districts above the 30% maximum falls to 29. While this might appear to be a positive finding, that is not really the case as the 30% cap threshold is dangerously low and will create numerous problems, as detailed below.

The second row of Table 2 shows the number of districts below the 30% cash balance threshold in each year, while the 3rd row shows the number of districts with a cash balance below 25% of expenditures. By FY27 513 school districts are projected to have a cash balance below 30% of operating expenditures. Similarly, by FY27 nearly 400 districts are projected to have cash balances below 25% of operating expenditures, at total which increases to 580 districts (over 95% of all districts) by FY29.

The 25% cash balance threshold is important because bond rating agencies typically use a 25% cash balance as the minimum level required for the most favorable (AAA) bond rating. In FY26, 235 districts are below the 25% cash balance threshold and by FY29 this number is forecast to increase to 541 districts. ***Falling below the 25% cash balance threshold stands to increase the cost to districts of borrowing money, which is clearly not cost effective.***

Table 3 on the following page shows the projected impact of the 30% cash balance cap provision on the number of districts expected to be placed by DEW under Fiscal Caution, Fiscal Watch and Fiscal Emergency.

Table 3: FY25-FY29 Impact of 30% Cash Balance Cap, Number of Districts Projected to be in Fiscal Caution, Fiscal Watch & Fiscal Emergency

Measure	**FY25**	**FY26**	**FY27**	**FY28**	**FY29**
# of Districts Negative Cash Balance	2	5	36	**156**	**298**
# of Districts Fiscal Caution (-2%-8%)	0	2	9	**67**	**66**
# of Districts Fiscal Watch (-8%-15%)	2	1	10	**49**	**52**
# of Districts Fiscal Emergency (> -15%)	0	2	5	**40**	**166**
Total # of Districts in Fiscal Caution, Watch and Emergency	**2**	**5**	**24**	**156**	**284**

Source: Calculations by Howard Fleeter for OEPI

The top row of Table 3 shows the number of districts each year whose cash balance is projected to be a negative number. This means that the cash available is lower than district expenditures in that year which indicates the district will be running an operating deficit. Once a district is running an operating deficit it runs the risk of being placed in Fiscal Caution, Fiscal Watch or Fiscal Emergency. The operating deficit criteria for these three statuses are as follows:

- **Fiscal Caution:** Auditor of State certifies a **deficit between -2% and -8%** of prior year general fund revenue
- **Fiscal Watch:** Auditor of State certifies a **deficit between -8% and -15%** of prior year general fund revenue
- **Fiscal Emergency:** Auditor of State certifies a **deficit greater than -15%** of prior year general fund revenue

The bottom four rows of Table 3 show the number of districts estimated to be in Fiscal Caution, Watch and Emergency in each year from FY25 through FY29. In FY27 a total of 24 districts are expected to be placed in one of these 3 categories, however this total increases to 156 districts (25.6% of all districts) in FY28 with 67 in Fisal Caution, 49 in Fiscal Watch and 40 in Fiscal Emergency. By FY29 284 districts (46.6% of all districts) are projected to meet the criteria for Fiscal Caution, Watch or Emergency.

The finding that more than one fourth of Ohio's school districts stand to be identified at one of these levels of financial risk with in 3 years of the imposition of the 30% cash balance cap provision and nearly half of all districts within 4 years, indicates that 30% is far too stringent a criteria to impose.

C. Increased Need for School Levies

A major reason that districts build up cash balances is the "levy cycle". Because HB 920 rolls back millage rates of all voted levies school, districts that are not at the 20 mill floor must rely on the continual passage of new levies in order to generate additional local revenue merely to keep up with inflation. Because expenditures escalate from year to year, the typical "levy cycle" involves passing a levy for an annual amount which create more than current expenditures initially but less than projected future expenditures. In this way the levy will add enough additional revenue so that the district has more funds than necessary in the first several years and the district's cash balance will increase. Eventually annual expenditures will surpass the district's amount of annual revenue, and the district will begin spending down their cash balance. Districts in this position will typically have a levy cycle which involves placing a new levy before voters every several years.

However, under the 30% cash balance cap provision, school districts that have recently passed operating levies will likely see much of these revenues mandatorily returned to voters. Because the original need for the levy has not magically dissipated with the enactment of the cash balance cap, voters will likely be confused (and possibly angry) when these districts are then quickly forced to place a new levy on the ballot.

Furthermore, the presence of the cap will likely create an "oscillation effect" whereby a district places a levy on the ballot and exceeds the 30% cash balance threshold, then has some of the levy recaptured and then needs to place another levy on the ballot. The alternative is for the districts to place levies on the ballot nearly every year trying to stay as close to the cap as possible. ***Ohio already votes on school levies far more than any other state with nearly 13,000 operating levies (and an additional 6,000-7,000 capital levies) placed before voters since HB 920 was enacted in 1976. The 30% cash balance will serve to increase the number of school levies on the ballot in Ohio, not decrease it.***

D. Increased Difficulty in Paying for Permanent Improvements

Over 100 school districts do not have Permanent Improvement (PI) levies in place. These districts must save up money over time for these types of expenditures but will now see much of that savings eliminated by the mandated property tax reduction. Furthermore, even districts that have permanent improvement levies would be prudent to build up a cash balance beyond their PI fund in case unexpected expenses arise.

E. Illogical Approach to Property Tax Relief and Voter Confusion

While touted by legislative supporters as "property tax relief", ***the tax reductions mandated by the 30% cash balance cap provision would not be linked in any coherent way to increases in property taxes caused by the recent large increases in reappraisal property values across much of the state***. Instead, districts whose taxes and/or recent reappraisal increases may be relatively low but have carefully managed their assets over time to build up a cash balance fund will likely see a significant portion of their contingency fund wiped out, while other districts that have not managed their resources as carefully and have low cash balances would not be impacted, even if their residents have a higher tax burden or have recently experienced a large increase in their property taxes. ***Furthermore, this tax relief would be applied to all district taxpayers, including***

***businesses and public utilities*, not to just to residential and agricultural taxpayers who have been most impacted by the recent historically large property reappraisal increases.**

Additionally, in most school districts this tax relief will be a "one-time only" lump sum decrease, rather than ongoing property tax relief. This is likely to be very confusing to voters when taxes go down sharply for one year and then immediately go back up. Furthermore, it will be even more confusing in cases (as mentioned above) where the increase from the restoration in Year 2 of the prior level of taxation is compounded by a school levy request as a recently passed levy was the reason that the district exceeded the 30% cap.

Finally, the vast majority of Ohioans pay their property taxes through escrow which means that the payments are part of their monthly mortgage payment. It is unclear how different banks and mortgage servicing companies will approach the reduced property taxes mandated by the 30% cash balance cap which means that many taxpayers may not see an immediate decrease in their mortgage payment and thus not receive immediate tax relief. And because different taxpayers in the same school district will be served by a multitude of lenders, it will be extraordinarily confusing when one taxpayer has their mortgage lender immediately adjust their escrow while their neighbor's mortgage lender may not.

F. Gas Pipeline Settlement Payments, TIFs and COPs

In additional to the effects discussed above, the 30% cash balance cap will also impact a variety of other circumstances.

Gas Pipelines – Natural gas pipelines cross through over 100 school districts in Ohio. Constructed mainly within the last 10 years, the two largest pipelines (Nexus and Rover) have been in litigation for roughly 6 years each. Nexus and Rover have been contesting the property valuation assigned to their pipeline network by the State Tax Commissioner and withholding payments (as is their legal right) to the school districts in their territory.

Nexus recently settled its litigation and has made payments for roughly 6 years of unpaid taxes to the roughly 40 school districts in its territory. ***Under the 30% cash balance cap the Nexus districts would see their long-awaited and rightfully owed property tax settlement payments largely wiped out*. Not only is this unfair to the districts, but it would also result in an unwarranted shift in taxes away from Nexus and to other taxpayers who would receive a one-time tax reduction instead of the school district receiving the tax revenues they are owed.**

The Rover case is scheduled for oral arguments next month and will likely take 1-2 years to resolve. At that point districts will be owed settlement payments over an 8-year period. One district alone has already had more than $210 million in property tax payments withheld by Rover.

TIFs and COPs – *Tax Increment Financing, commonly known as a "TIF",* is a relatively complex but frequently used economic development tool in Ohio. TIFs work in a way where the project benefits from a property tax exemption but local school districts always retain the current "baseline" tax revenue and also receive additional property tax revenues derived from the new project. The tax rate fluctuations which will most certainly result from the 30% cash balance cap provision will cause existing TIFs to experience variable property tax revenue which will negatively impact not only the school district, but also any counties, municipalities, townships involved in the TIF agreement.

Lease purchase certificates of participation (commonly known as 'COPS") are a financing instrument based on a "lease to own" structure that is commonly used by many Ohio school districts. COPs are often used for school buildings, bus garages, athletic and performing arts facilities and other similar "big ticket" items. 222 Ohio school districts currently have outstanding COPs totaling $3.1 billion in principle. COPs are essentially a loan that is secured with expected property tax revenue. ***If the revenue is not available because the imposition of the 30% cash balance cap has severely constrained the district's property taxes the district is at risk of not being able to make its payments and essentially defaulting on the agreement. Again, this is hardly an efficient practice for the state to impose.***

Conclusion

Two rationales have been proposed as reasons for the imposition of the 30% cash balance cap. One is that districts have "too much" cash and it should be returned to taxpayers in the district. The other is that the cash balance limit is a desirable form of property tax relief. However, neither of these arguments hold water for the following reasons:

- The circumstances of Ohio's school districts are too varied and unique for a single cash balance threshold to be appropriate. This proposal is an axe where a scalpel would be the more appropriate tool.
- This proposal would be destabilizing to school district finances on an ongoing basis and create considerable confusion for taxpayers.
- This proposal will increase the number of school levies on the ballot in Ohio.
- This proposal will lower the bond ratings of hundreds of Ohio school districts, which is a completely unnecessary cost increase.
- This proposal will place hundreds of Ohio school districts in fiscal caution, watch and emergency if they cannot convince voters to pass new school levies within the next one to three years.
- This proposal is an irrational way to provide property tax relief, with reductions in taxes tied to the particulars of a school district's balance sheet rather than the property tax burdens of taxpayers. Further, this tax relief would be temporary rather than ongoing and will almost certainly require higher taxes in the future.
- This proposal will make it harder to plan for and pay for permanent improvements.
- This proposal will jeopardize gas pipeline settlement payments potentially worth hundreds of millions of dollars.
- This proposal will undermine the stability of TIF and COP agreements.

This concludes my testimony. Thank you for your time and I would be happy to answer any questions.