



TESTIMONY BEFORE THE OHIO HOUSE FINANCE COMMITTEE

HB49, BIENNIAL STATE OPERATING BUDGET

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MARCH 30, 2017

Chairman Smith, Vice Chair Ryan, Ranking Member Cera, my name is Kent Scarrett and I am the Executive Director of the Ohio Municipal League. On behalf of our 734 members, I appreciate the opportunity to speak with you today and offer this testimony as a brief overview of the issues we see with the current budget proposal.

First, the budget promises more money to fight the heroine epidemic and we hope to see that money effectively reach our local departments who are on the front lines of that battle. As this committee knows, the opioid epidemic has impacted every community to one degree or another and not only is a tragic story of lost potential in individuals but is a serious threat to the economic recovery and future stability of the state. Second, the budget does seem to move some more money into projects that we are encouraged by.

You could say that our guiding principal at the Municipal League and for our members could be boiled down to one basic concept of government: “the government closest to the people serves the people best.” This is a quote from Thomas Jefferson, who said this during a debate in 1788 over the 10th Amendment to the U.S. Constitution.

The 10th Amendment reserves rights not given to the federal government to the state and people. Our members have dedicated their work to this federalist principle. Traditionally, the State of Ohio, through its General Assembly, has respected local government and even supported it with local government revenue sharing. Unfortunately, the principle of “home rule” and adherence for local governance has eroded in recent years.

Through this budget, Ohio has an opportunity to help rebuild the traditional partnership between state government and Ohio’s municipal corporations. That partnership is important because municipalities provide foundational services for businesses and the nearly 9 million citizens who call a city or village home. The vast majority of municipal budgets go to public safety and infrastructure.

In 1968, two-thirds of Ohio's state operating budget was public safety and infrastructure spending. Today, two-thirds of our budget is Medicaid and education. Meanwhile, many of Ohio's cities and villages are slowly losing the ability to provide the basic services they have traditionally provided, especially in mid-sized rural cities.

Ohio's municipalities are the state's strongest engine of economic development and are doing great things. One example is the national recognition Ohio and numerous municipalities recently received through the annual Site Selection Magazine "Governor's Cup Award." Ohio ranked 2nd, for the third time in a row nationally for the number of new projects and 3rd in the category of projects per capita. *(The Governors Cups reflect yearly project totals as tracked by the Conway Projects Database. Qualifying projects must meet one or more of these criteria for inclusion in the database: a minimum capital investment of \$1 million, 20 or more new jobs created, and 20,000 or more square feet of new space.)*

In the survey, numerous Ohio cities were recognized for their "pro-business" efforts through local economic development efforts. Cincinnati, in the category of municipalities with populations greater than 1 million, came in fifth and Columbus ranked 8th as the best cities nationally for attracting new facilities; Dayton was recognized as 3rd and Toledo came in at 7th place for communities with populations between 200,000 to 1 million; and Findlay won first place for attracting new facilities in the category of "rural areas" while Wooster came in third, followed by Celina, Defiance and Portsmouth tied for the tenth spot.

In the new "information economy" businesses of the future are looking for "Millennials", young, well-educated and skilled employees. Those employees generally prefer to live in well-developed metropolitan areas that are safe, fun, have good parking, recreational spaces, and robust economic development. That simply cannot be done without strong, independent municipalities.

This budget continues the trend of making that development and the tradition of Ohio's strong local government more and more challenging. In Ohio, our municipalities are blessed with the ability to administer their own tax system, which gives our cities and villages the ability to serve their constituents better. The independence of revenue sources is the most fundamental element to any institution; business, governmental, family, or otherwise. At the end of the day, the municipal income tax incentivizes municipalities to ensure people in its jurisdiction enjoy their maximum earning potential.

There are two very large problems this budget presents relative to these principles. First, the budget proposes making significant changes to the municipal income tax including the removal of the "Throwback" rule and the proposal to have the Ohio Department of Taxation and the state administer the municipal net profits tax on businesses.

Second, the budget proposes several changes to the Local Government Fund negatively impactful to cities and villages. Those areas include the new proposal to means-test the LGF through a challenging methodology that attempts to identify "capacity" based markers which will lead municipalities across the state with the unenviable task of raising taxes to make-up for redirected state aid. Also, HB49 would take \$24 million from the municipal LGF distribution and divert it to townships and very small villages and eliminates \$10 million in revenue that is a supplemental distribution earmarked for municipalities that administered an income tax.

State policies that result in revenue shortfalls to municipalities only further limits the ability of cities and villages to provide dependable services businesses and residents expect every day and curtails opportunities for greater economic development. Revenue sharing reductions by the state have resulted in \$453 million loss in CY 2015 alone.

We believe that is not in keeping with Ohio's tradition of promoting strong communities.

Beyond the principled reasons, we have laid out the more technical and specific arguments against the central collection of municipal taxes in great detail in previous testimony. We believe local tax departments can and do serve constituents better and more efficiently than the state; the Ohio Business Gateway (OBG) system is not currently prepared to handle the administration of hundreds of thousands of municipal net profit filings and the critical management and redistribution of \$600 million in municipal revenue and we have deep reservations that the system will be fully functional by January 1st. But there is hope; through the state budget, an appropriation is being made to rebuild the system to "OBG 3.0" and we believe once the portal is fully functional and capable of interfacing with tax preparer software and can process required filing attachments, businesses will use the Gateway as an alternative to working with local tax professionals, if they prefer.

The current proposal would mandate that all businesses with municipal net filing obligations file their local tax through the state. We believe and testimony offered in the House Ways and Means committee confirmed that this should not be considered a "pro-business" move. Flexibility and access to practical options are the hallmarks of a good business model.

Cities are the main driver of economic development from the public standpoint in Ohio and have every incentive to accommodate present and future businesses. That is why 80% of businesses in Ohio are located in a municipality. Businesses vote with their feet and have the option to move to an unincorporated area if the municipal income tax were such a burden to the success of their operations.

Next, the Local Government Fund is part of an agreement between the state and its local partners going back to 1934. Its purpose is to share revenue that the local governments lost when the state began to impose its sales tax. It is challenging for our local leaders to be expected to accept the continued tinkering of this Fund and be agreeable to turning it into a means-tested state redistribution as a viable policy alternative to address inadequacies of previous revenue sharing changes. It is distressing at best and we ask that the language be jettisoned from the budget.

Furthermore, the "taxation capacity" formula the administration put forward has produced a number of absurdities. We do not think any formula will actually capture the nature of every city and village, as many have varying tax capacities within their own borders. Further, there are always winners and losers in such arrangements, as we know from other policy areas that have attempted these types of approaches.

In FY 2006-2007 and for years before then, the LGF funding earmark percentage was 3.68% of the state GRF. After years of transitional change, the current funding percentage is 1.66%. In light of the state's economic recovery and the restoration of the state's Budget Stabilization Fund having reserves topping \$2 billion and the contributions of Ohio's local governments to achieve that feat, the Ohio Municipal League asks that the LGF be restored to its previous 3.68% percentage level. This reinvestment in Ohio's hometowns will relieve the effects of previous state policy decisions which have resulted in "tax shifting" to the local level. Since 2011, over 80 municipalities have raised their income tax rates.

We are hopeful that the municipal tax language included in HB49 will be removed from the bill and inserted into future legislation that is being discussed to address areas of concern that remain related to the municipal income tax including issues that have presented themselves as a result of the enactment of HB5 from the 130th General Assembly. The league greatly appreciates the efforts

of Rep. Scherer and the representatives of business organizations and tax preparers who have joined us in meetings to talk about muni tax issues that will go beyond the enactment of this budget bill. We look forward to continuing our meetings to find solutions to challenges taxpayers have and remedies to make the administration of local taxes more efficient.

Thank you for your time and consideration of the concerns of Ohio's cities and villages, as it relates to some of the main challenges included in the budget before you. I would be happy to answer any questions.