Final Report
of the
Local Government
and
Library
Revenue Distribution
Task Force

Senator Gary Cates
and
Representative Larry Wolpert
Co-Chairs

November 29, 2006

Local Government and Library Revenue Distribution Task Force Report

Background on the Creation of the Task Force

House Bill 66, the biennial budget bill for the FY 06 – FY 07 biennium, required a task force to review the revenue streams which fund the three local government funds. The task force was to make recommendations, in keeping with the tax reform components of HB 66, that would allow growth and provide stability to the funds. The three funds being reviewed were: the Local Government Fund (LGF), the Library and Local Government Support Fund (LLGSF), and the Local Government Revenue Assistance Fund (LGRAF).

This report, presented to the Governor and the General Assembly, contains the findings of the task force.

Committee Members (voting)

Representative Wolpert, co-chair (R-23)	Senator Cates, co-chair (R-4)
Representative Daniels (R-86)	Senator Grendell (R-18)
Representative Uecker (R-66)	Senator Schuring (R-29)
Representative Sayre (D-96)	Senator Fedor (D-11)
Representative Chandler (D-68)	Senator Zurz (D-28)

Committee Members (non-voting)

Susan Cave, Ohio Municipal League
Michael Cochran, Ohio Township Association
Larry Long, County Commissioners Association
Lynda Murray, Ohio Library Council
Larry Peck, Ohio Parks & Recreation Association

The language from HB 66:

SECTION 503.12. *(A) There is hereby created the Local Government and Library Revenue Distribution Task Force consisting of the following members:*

(1) Five members of the House of Representatives to be appointed by the Speaker of the House of Representatives, at least two of whom shall be from the minority party;

(2) Five members of the Senate to be appointed by the President of the Senate, at least two of whom shall be from the minority party;

(3) One nonvoting member to be appointed by the Ohio Library Council;

(4) One nonvoting member to be appointed by the County Commissioners' Association of Ohio;

(5) One nonvoting member to be appointed by the Ohio Municipal League;

(6) One nonvoting member to be appointed by the Ohio Township Association;

(7) One nonvoting member to be appointed by the Ohio Parks and Recreation Association.

All appointments shall be made within thirty days after the effective date of this section. Vacancies on the Task Force shall be filled in the same manner as the original appointments. The Task Force shall designate one of the members to serve as chairperson. The initial meeting to organize the Task Force shall be called by the Tax Commissioner.

(B) The Task Force shall study potential sources of state funding for the Local Government Fund, the Library and Local Government Support Fund, and the Local Government Revenue Assistance Fund that have the capacity to allow for growth in funding levels and to provide stability in funding levels. In addition, the Task Force shall consider changes to the codified funding formulae for the Local Government Fund, the Library and Local Government Support Fund, and the Local Government Revenue Assistance Fund that reflect the reform to Ohio tax code.

(C) The Task Force shall receive staff assistance from the Tax Commissioner and may request assistance from the Legislative Service Commission. The Task Force shall also seek the input and testimony of interested parties.

(D) Not later than December 1, 2006, the Task Force shall submit a report to the Governor and to the General Assembly setting forth its recommendations for sources of funding for the funds specified in division (B) of this section, together with suggested legislation to implement the recommendations.

(E) The Task Force shall cease to exist upon issuing its report.

Background on the Creation and Funding of the Local Government Funds

Local Government Fund (§5747.03)

The LGF was created alongside the initial state sales & use tax, which was enacted in 1934.

State revenue for the LGF has been appropriated since 1939 to the eighty-eight counties in the form of an "undivided local government fund" which is then distributed via county budget commissions to eligible political subdivisions. {The county budget commission is comprised of the county auditor, the county treasurer, and the prosecuting attorney. §5705.27 ORC}

The revenue that accrues to the LGF is distributed to the counties based upon a formula using municipal valuation and county population data. That formula has been in place since 1945.

Political subdivisions that are eligible to receive a portion of the county's LGF: the county, municipal corporations, park districts, and townships.

Senate Bill 114 of the 108th General Assembly created two methodologies for county distribution of the undivided LGF based upon "need," a statutory method (§5747.51 & §5747.52 ORC) and an alternative method allowing a county to develop a specific formula for itself. According to the latest available data from the Department of Taxation, only five counties were found to be on the statutory formula: Coshocton, Harrison, Morgan, Perry, and Paulding.

The LGF is comprised of: 4.2% of the state income tax, the sales & use tax, the corporate franchise tax, and the public utility tax; and 2.646% of the kilowatt-hour tax. {HB 94 of the 124th General Assembly replaced this percentage-of-tax-source method in temporary law with a frozen appropriation amount. The freeze was continued in HB 95 of the 125th General Assembly and HB 66 of the 126th General Assembly.}

Additional information may be found at the Ohio Department of Taxation's website:

http://www.tax.ohio.gov/divisions/communications/publications/annual_reports/documents/local_government_funds_state_county.pdf

Local Government Revenue Assistance Fund (§5747.61)

In response to a legislative study of the LGF, the LGRAF was created by HB 171 of the 117th General Assembly.

The LGRAF is distributed based upon a methodology where each county receives a proportional share based upon its percentage of the state's population using US Census data. This formula was enacted in HB 111 of the 118th General Assembly.

The county budget commission authorizes the distribution to political subdivisions.

The LGRAF is comprised of 0.6% of the state income tax, the sales & use tax, the corporate franchise tax, and the public utility tax; and 0.378% of the kilowatt-hour tax.

{As with the LGF, HB 94 of the 124th General Assembly replaced this percentage-of-tax-source method in temporary law with a frozen appropriation amount, and the freeze was continued in the two subsequent biennial budget bills.}

Library and Local Government Support Fund {§5747.03 & §5747.46}

The LLGSF was created following the elimination of the intangibles tax in HB 291 of the 115th General Assembly. That tax had been a primary source of funding for public libraries, so the LLGSF was proposed by a committee HB 291 created to replace the foregone revenue.

The Public Library Financing and Support Committee's recommendation was included in HB 146 of the 116th General Assembly. The fund became operational in calendar year 1986.

The fund creates a guaranteed share and an equalization share which are blended together to total each county's entitlement. The guarantee share is the previous year plus inflation; the equalization share is based upon county population as a percentage of the total state population. The LLGSF total for the county is then distributed by the county budget commission.

After a formula freeze in the early 1990's, the LLGSF revenue stream was set at 5.7% of the state income tax. {As with the LGF and LGRAF, the LLGSF receipts were frozen by HB 94 of the 124th General Assembly and the freeze was maintained through the end of FY 07 by the budgets that followed.}

Additional information on the LLGSF may be obtained from the Ohio Department of Taxation's website:

http://www.tax.ohio.gov/divisions/communications/publications/annual_reports/documents/library_local_gov_support_fund.pdf

Recommendations

New Revenue Formula – Revenue Assistance Partnership (the RAP)

To ensure predictability and stability, and in order to allow for growth, the task force recommends the replacement of the percentage-of-tax methodology with a percentage-of-tax-receipts formula; provided, however, that no entity receiving funding through LGF, LGRAF, or LLGSF funds for FY 08-09, FY 09-10, FY 10-11, and FY 11-12 shall receive less than the amount of such funds received by that entity for FY 07. Rather than allocating percentages of individual tax source proceeds (a piece of the income tax, a piece of the public utility tax, etc…), the task force proposes that the three local government funds receive in statute a percentage of the general revenue fund tax receipts in total collected by the state

Only tax receipts slated to be deposited into the GRF would be used in the calculation. For example, the portion of commercial activities tax receipts which are used to reimburse local governments and schools for the tangible personal property tax phase out would not be included in this formula; the portion of the commercial activities tax receipts which are slated to go into the GRF would be part of the formula calculation. Non-tax receipts, such as earnings on investments, federal funds, and intrastate transfers, would not be included.

{Note: in order to assure that this formula provides the amount intended, budget planners will need to add the revenue now going to the three local government funds to the GRF tax receipts total. Currently, the

LGFs receive an "off the top" portion of the tax sources that provide them with revenue, and those proceeds are not counted as part of the GRF tax receipts. See the attached spreadsheet (Chart 1) for detail.}

The task force recognizes that the recently enacted State Appropriation Limitation (SB 321) places a ceiling on GRF appropriations; however, as the current local government funds are appropriated through non-GRF revenue distribution funds and are not included in the limit, the new methodology would be treated the same way. Hence, the proceeds of the combined state tax receipts flowing into the local government funds would continue to be outside of the State Appropriation Limitation, and should continue to be appropriated via non-GRF line items.

To achieve this recommendation, the statutory percentages now in place, though frozen by temporary law, would need to be replaced by new percentages reflecting this report's proposal. Growth in state GRF tax receipts would be shared by the local government funds via this mechanism. The effect of state tax reforms may have a drastic impact on individual tax sources (as when the intangibles tax was repealed in the 1980's). The effect of reforms on local government funds is blunted by creating a revenue-sharing package that carves out a percentage of the whole. The state and the local government funds will rely on GRF tax receipts in total rather than the local funds having to seek reimbursement or replacement offsets every time a specific tax source has a significant change.

The task force further acknowledges that a preferred outcome for the local governmental entities receiving funds from this recommendation would include growth in the first year. To that end, the task force recommends that **a 3% increase be incorporated into the first year of the new formula**, rather than starting from the freeze level as a base. According to the Department of Taxation, to achieve the goal of the freeze amount plus 3%, the statutory share of GRF tax receipts percentage for FY 06, had this formula been in place, would have been:

LGF: 3.28%
LGRAF: 0.47%
LLGSF: 2.27%

(Late summer 2006 estimates looking forward into FY 08 indicate the following estimated percentages: LGF – 3.26%; LGRAF – 0.47%; LLGSF – 2.26%. *The local government funds would receive* ***5.98%*** *off the top of the GRF tax receipt sources using these estimates.* See Chart 1 for detail.)

In the distribution/appropriation of LGF, LGRAF, or LLGSF funds in accordance with the above new formula for FY 08, FY 09, FY 10, and FY 11, entities receiving such funds shall receive the greater of (1) the amount determined according to the new formula, or (2) the amount that such entity received from the applicable fund for FY 07.

OBM should provide the 127th General Assembly and the Governor with its estimates for the FY 08 – FY 09 tax receipts and the Department of Taxation should adjust the above percentages accordingly, as revenue estimates become more refined, to achieve the task force's goal: the FY 08 allocation would equal the FY 07 local government fund appropriations multiplied by 103%. For each subsequent year, the local governmental entities would receive their statutory percentage share of the state GRF tax receipt sources.

While this new approach will provide true revenue-sharing and incentivize state and local entities to partner in their efforts to generate additional economic growth for the betterment of Ohioans, it is important to note that external developments could threaten this formula. **If non-legislative entities were to successfully amend the Ohio Constitution or to create an initiated statute that would earmark GRF tax receipts, the viability of this formula would be jeopardized.** As the state and local governments will share the benefits of increased economic activity producing greater revenue, they also would need to share the burden of revenue diversions. Future governors and General Assemblies will need to review the fiscal impact of any revenue earmarking proposals.

It is the formal recommendation of this task force that the new formula and accompanying law changes be made in the FY 08- FY 09 biennial budget.

Effect of Moving from a Freeze to a Formulaic Distribution:
Why transitioning back to the formulas will create short-term "winners and losers."

As local government participants have pointed out during discussions on moving forwards to the new system envisioned by this report, the distribution formulas for the LGF and the LGRAF will not uniformly apportion increases in funding. The Department of Taxation was asked to comment on this phenomenon and produced the following explanatory text:

"*As a result of a temporary uncodified law provision enacted by Am. Sub. HB 66 (126th General Assembly), during fiscal years 2006 and 2007 the distributions made from the LGF, LGRAF and LLGSF are "frozen" at their fiscal year 2005 levels. That is, each county undivided LGF, county undivided LGRAF, and county undivided LLGSF (and each municipality receiving a direct distribution from the LGF)[1] receives the same monthly distribution it received during such month of the previous year (dealer in intangibles tax distributions excepted). Beginning in August 2007, however, the "freeze" is scheduled to expire, to be replaced by the statutory allocation formulas that exist for each of the respective funds. Because of its statutory structure, which includes a county "guaranteed share," the LLGSF will experience no significant distributional changes when the transition to permanent law occurs; all counties will receive at least what they received in calendar year 2006 (under the assumption that overall LLGSF funding does not decline). However, such is not the case for the LGF and LGRAF: unless permanent or transitional changes are made to the distribution formulas, only inordinate increases in LGF and LGRAF funding will prevent some recipients from experiencing a decrease in their distributions.*

The basic reason for the LGF and LGRAF distribution decrease for some counties (and increases for others) is that the permanent allocation formulas have not been used since mid-2001, when the current freeze first went into effect (Am. Sub. HB 94, 124th GA). ***During the six-year span between the enactment of the freeze and its assumed mid-2007 termination, some counties will have experienced relatively high population growth (the factor affecting the LGRAF formula) and relatively high growth in urban property valuation (the main factor affecting the LGF formula); others have experienced relatively low growth or even declines in those factors.*** (emphasis added) *Those six years' worth of population and valuation changes will drive the outcomes of the LGF and LGRAF formulas when the formulas go back into effect in August 2007, substantially changing the counties' percentage shares of the funds. For many counties, the changes will be significant enough that modest (single-digit percentage point) growth in the overall funding of the LGF and LGRAF will not prevent a decline in their distributions relative to calendar year 2006. In essence, for these counties, the decline in the county share of the total state LGF and/or LGRAF will outweigh the increase in the state LGF and/or LGRAF amount."*

The next Administration and General Assembly, should they choose to advance this report's recommendations, will have to consider whether or not to address this issue. A hold harmless mechanism could be put into place to prevent decreases in funding, but that could have the effect of merely forestalling the

[1] The remainder of this discussion will be framed in terms of the county undivided funds although a similar distributional dynamic will affect the municipalities that receive a direct distribution from the state LGF.

transition back to the statutory distribution formulas. In addition, it would require supplemental appropriations or transfers of funds beyond the new formula amount.

In any case, the Task Force believes it is vital that stakeholders understand this dynamic: even if the suggested 3% first-year increase is incorporated in a legislative proposal, there will be, due to population shifts and valuation changes, local governmental entities that initially receive less funding than the freeze amounts if no supplemental, hold harmless is adopted.

“*Outside of Scope” Recommendations*

In reviewing the history of Ohio’s state/local revenue sharing, other issues were raised that, while outside the direct charge of this task force, should be studied further. These supplemental recommendations follow and should be given consideration during future legislative budget hearings…

- Disbursement of the LGF at the county level – as so many counties have chosen an alternative formula for distribution, rather than the statutory formula, the ORC could be revised to simply permit the County Budget Commission of each county to establish a disbursement plan of its own each year. This could be considered a third option.

- Public Library coordination – libraries should be encouraged to eliminate duplicative systems to allow for seamless usage of any public library in the state with any Ohio public library card. Regardless of home address, Ohioans should be able to access materials at their most convenient location. Such consolidation would save tax money by eliminating administrative overhead, and would simultaneously improve patron services. This could also encourage a consolidation of library districts within counties for further administrative savings.

- Estate Tax – Since January of 2002 Ohio’s estate tax has been split so that 80% of the revenue goes to local governments and 20% of the revenue goes to the state. Any studies or proposals dealing with the reduction or elimination of the Ohio estate tax should include review of how local governmental entities would be effected by the foregone revenue.

Representative Larry Wolpert
Co-Chairman

Representative David Daniels

Representative Joseph Uecker

Representative Allan Sayre

Representative Kathleen Chandler

Senator Gary Cates
Co-Chairman

Senator Timothy Grendell

Senator J. Kirk Schuring

Senator Teresa Fedor

Senator Kimberly Zurz

Addendum to Local Government and Library Revenue Distribution Task Force

It is the intent of Senator Zurz, Senator Fedor, Senator Schuring, Representative Chandler, and Representative Sayre to recommend to the Task Force that an **at least 3%** increase be incorporated into the first year of the new formula, rather than starting from the freeze level as a base. When considering this Task Force's Report during Biennium Budget deliberations, the undersigned legislators would like to ensure **that nothing less than a 3%** increase to the new formula be considered as a base level.

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Kimberly A. Zurz
State Senator, 28th District

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Teresa Fedor
State Senator, 11th District

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Kirk Schuring
State Senator 29th District

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Kathleen Chandler
State Representative, 68th District

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Allan Sayre
State Representative, 96th District

County Commissioners Association of Ohio

Lenny Eliason, President
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Ohio Library Council

Craig Miller, President
Holmes County District Public Library

Doug Evans, Executive Director

Lynda Murray, Director, Government Relations

Ohio Municipal League

Thomas J. George, President
Mayor, City of Lakewood

Susan J. Cave, Executive Director

Ohio Parks & Recreation Association

Kim Conrad, President
Director, Grove City Parks and Recreation

Michelle Park, Executive Director

Ohio Township Association

Larry Johns, President
Moulton Township/Auglaize County

Michael H. Cochran, Executive Director

Local Government and Library Revenue Distribution Task Force Report

On behalf of the local government fund stakeholder groups, we would like to offer our appreciation for the Local Government and Library Revenue Distribution Task Force Report. The three local government funds (Local Government Fund (LGF), Local Government Revenue Assistance Fund (LGRAF) and Library & Local Government Support Fund (LLGSF)) provide essential everyday services in our communities, large and small. It is critical that the state and local partnership facilitated by these funds continue.

The stakeholder groups advocated for the establishment of the Task Force to help move the funding of the local government funds forward, given that tax reform enacted last year eliminated and reduced revenue sources to the funds. The Task Force has fulfilled this goal.

The stakeholder groups are appreciative of the recommendations set forth in this report. The report recommends a predictable and stable funding source for the local government funds by replacing the current percentage-of-tax-source methodology with a tax source proceeds method. Specifically, the local government funds will receive a percentage of the general revenue fund tax receipts in total collected by the state. This embodies the concept of sharing in state revenues in a manner that reflects both good and bad times.

The report also recommends that a three percent increase be incorporated into the first year of the formula to increase the base from FY 2007 freeze level. We believe moderate growth in the local government funds is reasonable and appreciate this initial step by providing a benchmark that establishes growth in the first year following recent freezes. Through the budget process we will continue to strive to move the funds forward.

Additionally, the report recommends a hold harmless provision to help transition from the current freeze levels to the new revenue formula. With the proposed 3 percent increase in state fiscal year 2008, there would be 42 counties under LGF and 33 counties under LGRAF that would receive less than the prior year to distribute to local governments and park districts. If those funds had not been frozen in recent years and been able to share in state revenue growth, there would have been a general increase to the funds annually. In addition, since the funds have been frozen for an extended time period, the cumulative impact of six years of formula changes would be realized in just one year.

We appreciate all of the hard work and time that went into the production of this report, and we especially thank Co-chairs Cates and Wolpert along with their staffs for their efforts. While we understand that this report is merely a recommendation, the members of our associations look forward to working with the new administration and the 127th General Assembly in addressing the funding of the Local Government Funds.

Sincerely,

Larry Long, Executive Director
County Commissioners Association of Ohio

Lynda Murray, Director, Gov't Relations
Ohio Library Council

Susan J. Cave, Executive Director
Ohio Municipal League

Larry Peck, Legislative Chair
Ohio Parks and Recreation Association

Michael H. Cochran, Executive Director
Ohio Township Association