Office of Budget and Management
Timothy S. Keen, Director

Governor John R. Kasich

Department of Taxation
Joseph W. Testa, Commissioner

February 2015

Resuming the Phase-out of the Tangible Personal Property Tax and Public Utility Deregulation Replacement Payments

Introduction – Replacement payments Prior to HB 153

As part of the various law changes that accompanied electric utility and natural gas deregulation in 1999-2000, property tax assessed value for electric generating equipment and natural gas property were reduced. This reduced public utility tangible property (PUTP) tax revenues to school and local governments. The Ohio General Assembly put into law a program whereby school districts and local governments were compensated for these lost revenues, although the replacement payments were to be phased out over time. Then in the 2005 biennial budget bill, HB 66, the tangible personal property (TPP) tax was gradually repealed as part of a sweeping reform package meant to stimulate economic growth, particularly in manufacturing. Once again, school districts and local governments lost property tax revenue, and once again, the General Assembly put into place a property tax replacement payment program. As with electric and gas deregulation replacement payments, these were scheduled to eventually be phased out.

As a result of these developments, when the Kasich administration first took office in 2011, the administration inherited two very costly legacy programs to reimburse schools and local governments for local property taxes that were eliminated due to state law changes. The costlier of the two replacement programs, by far, was the TPP tax reimbursement program. The repeal of the TPP tax resulted in $1.65 billion in lost property tax revenue to school districts and local governments (plus an additional loss of almost $200 million in repealed property taxes on telecommunications providers, which had before the 2005 tax reform been classified as public utility tangible property taxes). The bill which repealed the TPP tax, HB 66, originally established a five-year “hold harmless” period (2006-2010), during which school districts and local governments would be fully reimbursed for lost property taxes. At the same time, the new commercial activity tax (CAT) was being phased in, with CAT revenues earmarked to pay for the reimbursements. In the early years of the program, the CAT did not generate sufficient revenues to make the required reimbursement payments, and so the GRF had to subsidize the reimbursement payments in FY 2009-02011.

The second program, to replace PUTP taxes lost due to electricity and natural gas deregulation, made reimbursement payments of about $144 million to schools and local governments in FY 2011/tax year 2010. The utility deregulation payments did not need to be subsidized by the GRF, as the kilowatt-hour (KWH) and natural gas distribution (MCF) taxes generated sufficient revenues to make all the necessary payments.

While HB 66 created a reimbursement mechanism for lost TPP taxes to schools and to local governments, it also provided for the eventual elimination of those payments. School districts were to have their payments gradually reduced beginning in FY 2012, with payments falling to zero in FY 2019. Local governments were to have their payments gradually reduced beginning in tax year 201, with payments falling to zero in tax year 2018. Set fractions of reimbursement were to be eliminated each year.

The utility deregulation payment phase-out was more complex than the TPP phase-out. Beginning in FY 2007, school district reimbursements were subjected to a test of whether growth in state education aid since FY 2002 was greater than the payment. Once state aid growth exceeded the reimbursement payment, the reimbursement payment was terminated. By FY 2011, only 133 of the then 614 school districts were still receiving utility deregulation replacement payments. For local governments, there was a different, also complicated mechanism where payments were divided up into per-capita amounts and pro-rate amounts based on proportion of PUTP tax revenue losses.

The table below summarizes the original TPP tax reimbursement phase-out plan established by HB 66 for fixed-rate levies, which were the most numerous and accounted for the largest dollar amount of the total reimbursement.

Table 1 - Original TPP Tax Replacement Schedule for "Fixed-Rate" Levies										
	FY 10	FY 11	FY 12	FY 13	FY 14	FY 15	FY 16	FY 17	FY 18	FY 19
TPP Tax Replacement to Schools										
Percentage of direct payment guaranteed to district: HB 66 (replaced in 2009)	100%	100%	14/17	11/17	9/17	7/17	5/17	3/17	1/17	0
		Tax Year 2010	Tax Year 2011	Tax Year 2012	Tax Year 2013	Tax Year 2014	Tax Year 2015	Tax Year 2016	Tax Year 2017	Tax Year 2018
TPP Tax Replacement to Local Governments										
Percentage of payment guaranteed to district: HB 66 (replaced in 2009)		100%	14/17	11/17	9/17	7/17	5/17	3/17	1/17	0

HB 153 Brief Summary

HB 153, the FY 2012-2013 budget bill, greatly altered the structure of the existing TPP and utility deregulation phase-out payments. Instead of eliminating set fractions of reimbursement per year, or subjecting reimbursement to a state aid test, HB 153 introduced the concept of phasing out payments based on how reliant a school district or local government was on those payments. Some school districts or local governments would have their payments eliminated earlier than under the original HB 66 schedule, but more heavily reliant districts would have their payments continue longer than under HB 66.

For this purpose, a calculation of school district or local government resources was made, and the replacement payment amounts were compared to those resources. Furthermore, distinctions were made among levy types in implementing the phase-out.

School Districts and Local Governments: Fixed rate, current expense property tax levies

For school districts, total resources included total property tax receipts (including rollback credits and homestead exemption subsidies), school district income tax revenues, total TPP and public utility reimbursements, and state foundation funding. Districts whose fixed rate payments were 2% or less of the total resources were considered low reliance districts. For these districts, the fixed rate reimbursement payments were eliminated in fiscal year 2012. If a district's fixed rate reimbursement was over 2% of total resources, then the annual reduction was limited to no more than 2% of base year total resources.

For local governments the total resources calculation was dependent on what revenues the local government received. For municipalities, municipal income tax revenues were the largest share of resources, although municipalities do receive property tax revenues and other revenues. For counties, property tax revenues were the largest portion of calculated local resources, but permissive sales tax revenues were also significant.

Counties received special consideration under the phase-out because their operations and their levy funding have a somewhat different character from other local governments. That is, many of their programs and the levy dollars to support them are distinct rather than commingled. In recognition of that fact, the HB 153 reimbursement allocations compared county reimbursements to county resources by function, rather than comparing total county resources to total county reimbursements. So, county general fund reimbursements, county MH/DD levy reimbursements, county children's services levy reimbursements, county public health services levy reimbursements, and county senior services levy reimbursements were all subjected to separate reliance tests.

The same methodology applied to both TPP and public utility deregulation replacement payments for fixed-rate current expense levies. However, the phase-out tests were applied separately to the two sets of payments, so a school district or local government that was receiving both TPP and utility deregulation reimbursements could theoretically lose 4% of its resources each year in lost reimbursement payments.

Although the administration proposal would have continued the reliance-based phase-out of payments until the payments were eliminated, the legislature suspended the reliance-based phase-out after two years, FY 2012 and FY 2013. School district reimbursements have been frozen at their FY 2013 levels since then.

For local governments, which operate (with a few exceptions) on calendar-year based tax years, the phase-out continued through tax year 2013, meaning that it was suspended after three years of operation. Currently local governments are receiving reimbursements frozen at their tax year 2013 levels.

School Districts and Local Governments: Fixed rate, non-current expense property tax levies

Replacement payments for fixed rate, non-current expense levies, which were much smaller amounts than the payments for current expense levies, were subjected to a much simpler phase-out schedule. They were scheduled to be phased out at 25% per year relative to FY2011 reimbursement payments. Again, the administration proposal would have phased out these reimbursements entirely, but the legislature suspended the phase-out after two years, when the school districts reimbursements had been reduced by 50%. Municipalities, which are the only type of local government receiving reimbursements for these sorts of levies, had their reimbursement reduced for three tax years (75%) before they too were frozen.

School Districts and Local Governments: Fixed sum levies

Fixed sum levies (those whose rate adjusts each year, as taxable value changes, to raise a fixed amount of money) include bond and emergency levies. These levies were not affected by the HB 153 law changes. That is, they remained under the original HB 66 law.

Under the original HB 66 law, bond levies were reimbursed at the initially calculated level as long as the levy was in effect, until the debt was retired. This remains the law today.

Under the HB 66 law, school district emergency levies would continue to be reimbursed at the initially calculated level as long as the district continues to impose the qualifying emergency levy. Renewal levies also qualify for reimbursement. Furthermore, an emergency levy is considered a "renewal" if the district has an emergency levy for at least the same amount of revenue generated by the originally qualifying emergency levy. However, emergency levy reimbursement, rather than being gradually phased out, goes to zero all at once in either tax year 2017 (for utility deregulation reimbursements) or tax year 2018 (for TPP tax reimbursements).

Finally, inside (unvoted) millage debt levies, while not fixed-sum levies, were also unaffected by HB 153, and were thus left under the original HB 66 law. These debt levies have been and will be fully reimbursed at the base year amount for tax years 2006-2017 (there is no phase out), as long as the inside millage continues to be levied for debt purposes. However, no reimbursement will be made in 2017 (for utility deregulation) or FY 2019 (for TPP) or thereafter, i.e. the reimbursement goes away all at once.

FY 2016-2017 Phase-Out Proposal

In the broadest terms, the executive budget proposal, rather than leaving the reimbursements frozen as in current law for fixed-rate current expense or other purposes levies, or eliminating them all at once as in current law for school district emergency levies, would return to gradually phasing out reimbursements based on the reliance calculations from HB 153. Of course, the computation of school district and local government resources has been updated from the 2010 data that was used for HB 153 to 2014 data (or the latest year available) for the current proposal.

There are some key differences between the HB 153 proposal and the current executive budget proposal, which are highlighted below:

(1) The utility deregulation and TPP reimbursement phase-out calculations are combined, rather than separate as they were for HB 153. That is, a district's combined utility deregulation and TPP reimbursement will be reduced by a maximum of 2% of its local resources per year, rather than having each type of reimbursement potentially decline by 2% of resources per year;
(2) The school district combined reimbursements are not phased down by a uniform 2% of resources per year. Instead, the school district phase-down depends upon the district's revenue capacity. Based on a measure of district revenue capacity calculated by the Ohio Department of Education (ODE), districts will be assigned to quintiles (fifths), from poorest (quintile 1) to richest (quintile 5). School districts in quintile 1 will have only 1% of their resources subtracted from their reimbursement payments each year. For school districts in quintile 2 the subtraction will be 1.25%; for quintile 3, 1.50%; for quintile 4, 1.75%; and for quintile 5, 2.0%.

(3) School district emergency levy reimbursements, rather than going away all at once, will be gradually phased out according to the following schedule:

Proposed Emergency Levy Reimbursement Phase-Out		**Current Law**	**Proposed Law**
Utility Deregulation	2016	100%	No change
TPP	2016	100%	No change
Utility Deregulation	2017	0	80% * Dereg2016
TPP	2017	100%	No change
Utility Deregulation	2018	0	60% * Dereg2016
TPP	2018	0	80% * TPP2017
Utility Deregulation	2019	0	40% * Dereg2016
TPP	2019	0	60% * TPP2017
Utility Deregulation	2020	0	20% * Dereg2016
TPP	2020	0	40% * TPP2017
Utility Deregulation	2021	0	0
TPP	2021	0	20% * TPP2017
Utility Deregulation	2022	0	0
TPP	2022	0	0

(4) Reimbursement for school district and local government fixed-rate levies for non-operating purposes are reduced by 50% in FY 2016 and eliminated for FY 2017 and thereafter.

The executive budget proposal would maintain the HB 66 treatment of bond levies, i.e. reimbursement continues as long as the levy is in effect, until the debt is retired. It would also maintain the HB 66 treatment of inside millage debt levies, i.e. reimbursement goes to zero in either FY 2017 (for utility deregulation) or FY 2019 (for TPP).Table 2 below summarizes the estimated impacts, both for the dollar amount of reimbursement and the number of districts receiving reimbursement, for FY 2016-2017.

Table 2 - TPP and Utility Deregulation Reimbursement: Summary of Executive Budget Proposal Impacts							
Current Law - milions of dollars					**Current Law - Numbers of districts**		
	FY 2015	**FY 2016**	**FY 2017**		**FY 2015**	**FY 2016**	**FY 2017**
School Fixed-Rate Operating	$420.1	$420.1	$420.1		260	**	**
Emergency Operating	$39.6	$39.6	$39.5		155	**	**
Total School Fixed-Rate and Emergency Operating Reimbursement	$459.7	$459.7	$459.5		326	**	**
School Fixed-Rate non-Operating	$13.4	$13.4	$13.4		460	**	**
School Bond and Inside Debt Reimbursemen	$24.5	$24.5	$24.5		198	**	**
JVS all levy types	$11.9	$11.9	$11.9		6	**	**
Total School and JVS Reimbursement	$509.5	$509.5	$509.3				
County	$70.4	$70.4	$70.4		83	**	**
Muni	$16.8	$15.9	$9.8		433	**	**
Township	$27.6	$27.6	$27.6		379	**	**
Special District	$17.5	$17.5	$17.5		174	**	**
Total Local Reimbursement	$132.2	$131.3	$125.2				
Total School and Local Reimbursement	$641.7	$640.8	$634.6				
** The current-law numbers of districts receiving reimbursements in FY 2016-2017 are expected to be very similar to the numbers in FY 2015. They may decrease slightly if qualifying levies expire and are no longer reimbursed, and the district therefore has no more reimbursed levies.							
Proposal					**Proposal - Numbers of districts**		
	FY 2015	**FY 2016**	**FY 2017**		**FY 2015**	**FY 2016**	**FY 2017**
School Fixed-Rate Operating	$420.1	$284.5	$184.3		260	203	136
Emergency Operating	$39.6	$39.6	$39.5		155	155	155
Total School Fixed-Rate and Emergency Operating Reimbursement	$459.7	$324.1	$223.7		326	283	232
School Fixed-Rate non-Operating	$13.4	$6.7	$0.0		460	460	0
School Bond and Inside Debt Reimbursemen	$24.5	$24.5	$24.5		198	198	198
JVS all levy types	$11.9	$5.6	$1.5		6	4	2
Total School Reimbursement	$509.5	$360.9	$249.8				
County	$70.4	$34.7	$17.8		83	70	55
Muni	$16.8	$1.4	$1.1		430	106	89
Township	$27.6	$19.8	$15.1		379	246	172
Special District	$17.5	$10.1	$6.2		174	128	93
Total Local Reimbursement	$132.2	$65.9	$40.2				
Total School and Local Reimbursement	$641.7	$426.8	$289.9				

Afterword

The estimates contained in this paper of the impacts of the resumption of the phase out of property tax replacement payments that was begun four years ago are based on the best information available to the administration at this time. Some of the underlying data are still being revised or updated, and so the amounts shown in the summary tables in this document may differ from detailed tables that are eventually released. The administration believes that the revisions will not be large and will not change the conclusions reached herein.

Prepared by:

Ohio Office of Budget and Management
www.obm.ohio.gov

Ohio Department of Taxation
www.tax.ohio.gov

February 6, 2015