

Ohio Commission on Local Government Reform and Collaboration

Subcommittee to recommend a more innovative system of local taxation that drives economic development and reduces negative competition

Draft Report

April 29, 2010

What is the desired outcome of these recommendations?

The goal of the subcommittee is to recommend changes in Ohio law, allowing local regions to develop more innovative local tax structures for the purpose of:

1. increasing economic development,
2. reducing negative competition among jurisdictions within a region
3. potentially lowering the local tax spend to save taxpayer dollars or to allow investment in other critical areas at the local level.

Current issues of local tax structure:

1. **Not every part of Ohio will need the same solutions for local tax issues. We're not suggesting one-size-fits-all solutions.** In other words, what works in Akron, may not work in West Chester, due to the fact that Ohio has diverse regions with diverse needs. The intent of this report is to provide more tools, more flexibility to local jurisdictions that will help local regions meet the desired outcome of the subcommittee, as stated above, which could also result in more collaboration to fit the mission of the commission.
2. **Our system of local taxation is operating off rules that do not necessarily fit the current economic environment.** Local revenue sources have been in place for many years with little fundamental changes. Several years ago, our state government made changes to Ohio's tax structure for the purpose of making us more competitive nationally for economic development and business retention, but we have done little to encourage innovation with regards to taxation at the local level.
3. **Existing revenue sources inhibits Ohio's local governments from achieving their maximum potential for regional economic development.** Ohio's local governments have different sources of income that serve as the main drivers of their budgets.
 - i. counties rely on sales tax,
 - ii. cities on income tax, and
 - iii. townships rely on property taxes.

This mishmash of revenue sometimes results in jurisdictional competition where communities fight each other for the same pool of economic development, when in fact, local jurisdictions should be reaching for regional economic development strategies that make us more competitive with the rest of the country, and the rest of the world.

- iv. For example, under the current structure of local taxation, companies may decide to leave an income taxing zone (cities) for a non-income taxing zone within the same region, resulting in no net gain for that region. How we get our revenue as localities can often influence behavior on the part of local companies, as they understandably try to maximize their total tax spend; in the process, however, significant time and dollars are often spent on keeping those companies in the region with no net economic gain for that region.
4. **Our current system of local taxation is harmful to business.** Due to the disparate revenue systems, and the multiple collection points in Ohio's local governments, tax payment is not simple enough for businesses and it hurts our ability to keep and attract companies. In addition, companies have to pay significant sums of money to ensure compliance.
5. **Because of the layers of local taxation, Ohio is the 9th highest local tax per percentage of income in the nation.** More innovation in local tax structures—more cooperation—could potentially lower the overall tax spend at the local level, while making jurisdictions more collaborative. Public services cost money—whether it's fire, police protection, economic development, or community infrastructure—but if we maximize those total expenditures, and move away from the current structure where some communities win and some lose, depending on their revenue sources, within a region, that entire region could become more affluent and stronger economically. Communities like Louisville, Kentucky, have less complex, and stronger economies due to this philosophy and structure.

Testimony relevant to this issue:

Myrita Craig—Executive Director, Agenda 360, Cincinnati USA Regional Chamber:

“...the second strategy that Agenda 360 embraces is multi-jurisdictional revenue sharing. We all know the challenges of collaboration when money is in the mix. If the state could create ways to incent revenue sharing, again, I believe positive collaboration would follow.

Phil Parker—President and CEO, Dayton Chamber of Commerce (comments on record)

....another point of emphasis for Mr. Parker was what he described as a convoluted tax structure on the local level. Taxes paid in core municipalities can rarely be used to pay for public services in newer suburbs. This has created an environment in which the central city and first-tier suburbs are burdened with a tax structure that is unappealing to new business....

Mayor William Currin, City of Hudson (from Regional Prosperity Initiative written report)

“Communities across Northeast Ohio have competed with one another for new businesses and job growth to enhance their own economic tax base. This unhealthy competition between communities results in duplication of services, frictions of governments across jurisdictions, and an unhealthy ‘winner-takes-all’ mentality. As the economies of the region, state, and nation have evolved into global competition for economic development, the current system is expensive, duplicative, and inherently unsustainable for communities across the region.....

Deborah Feldman, Montgomery County Administrator

“...In most cases when discussions of local government reform takes place proponents make an efficiency case. They state that consolidation of governments will result in less duplication and therefore lower costs to the taxpayers. They cite the number of police and fire departments, they reference the disparities between services provided by wealthy and financially stressed communities and they firmly believe that there is a better way to organize local government. Although this argument has merit in many cases, I don not believe it is the most critical reason to look at the organization of local governments. The most pressing problem we face as local managers/elected officials is to maintain and growing of our tax base. Economic Development has become critical to the financial viability of most communities. Governments are dependent on their tax base to fund vital services for their residents. This dependence on revenue growth together with the large number of local governments which characterize Ohio and the variety of taxes unique to each type of local government have resulted in an excessively competitive and in some case destructive situations in which communities compete against their neighbors for companies. The outcome of this competition between communities is often a win-lose environment which is confusing for the very businesses we are trying to attract. It also creates winners and losers among communities which is extremely damaging to the success of other service collaborations....

....another unintended consequence of the structure of local governments on economic development in Ohio is how difficult it is to develop and effectively drive a regional economic development strategy. With the unevenness of local tax benefit, it is often hard to convince all jurisdictions within a region that they should remain loyal to a regional economic development strategy that often times results in no direct gain for their citizens. This challenge is much greater in a time of low or declining growth...

...Ohio’s existing local government revenue structure has the unintended consequence of influencing jurisdiction’s economic development strategies and companies’ business location decisions. Counties rely on sales tax, cities on the income tax, and townships on the property tax. The most significant impact on economic development increasingly comes from the local options income tax. Generally, the core cities and older first tier suburbs rely heavily on the income tax to support local services. In most cases, financially stressed core communities (and counties) face significant spending demands driven by concentrations of poverty, resulting crime, deterioration of housing stock, older infrastructure, etc. The effect is a heavy reliance on the income tax resulting often times in the highest rates in the region. This cause and effect often creates a disincentive for business to locate in the urban core, and is exacerbated by ‘income tax free zones’, mostly townships. Consequently, as companies face an increasingly competitive business environment, they are attracted more and more frequently to communities in which they and/or employees pay no income tax.....

Ohio Tax Commissioner Richard Levin (source: Powerpoint presentation to Commission May 2009)

According to Director Levin’s presentation of Principles of Taxation.....(as endorsed by the 2002 Committee to study state and local taxes, created by the Ohio General Assembly...)

Equity—“Horizontal equity exists when the tax system imposes similar burdens on similarly situated taxpayers. Vertical equity exists when the tax system recognizes differing abilities of various taxpayers to pay.”

Neutrality—“The tax system should interfere with private sector decision making as little as possible and not unduly influence economic behavior. The economy and the marketplace, not the government’s tax policy, should drive business decisions.”

Simplicity—“The tax system should facilitate taxpayer compliance by being easy to understand. Simplicity helps to minimize both the compliance costs imposed on taxpayers and the government expense of administration and enforcement.”

Recommended changes in the local tax structure to drive economic development, reduce negative competition.

Again, one solution does not fit the needs of all communities. The list of recommendations below would be “tools in the toolbox” for local jurisdictions. The overall theme here is flexibility for jurisdictions to create new programs that further collaboration.

- **Incentivize the establishment of local tax collection structures that make it easier for business to pay:** Jurisdictions should be incentivized in some way to move to a single point of collection for income taxes, to make it simpler for the business community.
- **Help clear up the legislative questions raised in HB 920, Ohio Constitution.** Clarify HB 920 to determine if changes are needed to allow for the sharing of new growth revenue. Determine if language in the Ohio Constitution in Article 12, Section 5 indeed prohibits revenue sharing, or if the practice allows flexibility, depending on the interpretation. (Currin)
- **Help communities who have not done so, to develop regional economic development plans that leverage that region’s economic strengths.** Many regions already have a strategic plan with regard to economic development. Some may not. Without some kind of larger strategy, regions may miss the opportunity to target dollars to the greatest need.
- **Incentivize revenue sharing of new growth in the tax base across regions to support regional economic development strategies.** Incentive money from the state to act as a carrot for multi-jurisdictional revenue sharing resulting from new revenue—that pot could be tied directly to economic development, and it should be used to reinforce development under that communities’ regional economic development strategies.
- **Ohio Department of Taxation and Ohio Department of Development create a Revenue Sharing on new Growth Pilot Program: (Fairly Bold)**Support—in the form of research, cheerleading, and project management-- from the Ohio Department of Taxation together with Ohio Dept. of Development to support several pilot projects involving innovative systems of local revenue sharing to promote economic development. Communities could either take an existing model, like Montgomery County’s ED/GE program, or the proposed program by northeast Ohio’s Regional Prosperity Initiative, or design their own. The incentive dollars could take the pressure

off jurisdictions when a program begins, to see how it unfolds until they can be comfortable enough to put their own shared resources into the mix.

- **Ohio Department of Taxation and Ohio Department of Development assist in the creation of a pilot program for innovative local tax systems inclusive of and/or possibly beyond revenue sharing (More Bold)** Over the course of our testimony, we heard several proposals to even out the tax structure to mitigate location decisions by businesses due to uneven tax structures within a single region (ie :”moving the deck chairs”). For example, Dr. Mark Partridge from Ohio State University in a discussion at the Greater Ohio conference in September 2008 suggested the state should incentivize regions that set up regional tax-sharing pools for local earnings taxes—possibly 1% with revenue redistributed on a per-capita basis. Dr. Partridge and others believe this could move communities toward working with each other rather than the current system of tug and pull based on revenue generation due to tax differences; further, if when companies are given incentives to move within the same region, and given tax breaks to do it, you have a situation where there’s not only no net job creation for the region, but less overall tax revenue for that region. This kind of idea , if properly looked at in a systematic way , if properly looked at in a systematic way, could, according to Dr. Partridge, yield overall lower taxes for a region due to minimization of this kind of practice. But you need a laboratory to make a sound judgement.
- **Steering Committee to implement pilots.** Some kind of steering committee that would make sure the pilot actually happened with legislative mandated due dates made up of Ohio Chamber, Ohio County Commissioners Association, Ohio Municipal League, Ohio Township Association, Ohio Tax Department, Ohio Department of Development, and maybe Greater Ohio and Buckeye Institute—that would help buffer some of the political tension that may come up—and give it some lift to see if it works.