$7 Billion In Ohio Tax Breaks,
and Nobody's Watching

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Executive Summary

The General Assembly should pay close attention to the new tax expenditure report. Prepared by the Ohio Department of Taxation (ODT) and sent to the legislature with the rest of Gov. John Kasich's budget, this report examines credits, deductions and exemptions in the tax code that reduce the amount of revenue the state would otherwise receive.

The taxation department estimated that in both Fiscal Years 2012 and 2013, 128 such exemptions and credits amounted to more than $7 billion in foregone revenue to the state's General Revenue Fund. "Tax expenditures result in a loss of tax revenue to state government, thereby reducing the funds available for other government programs," ODT noted in the report. "In essence, a tax expenditure has the same fiscal impact as a direct government expenditure." The report estimates foregone revenue, which is not necessarily what the state would get if a tax expenditure was repealed.

Most tax expenditures remain in effect indefinitely with little or no scrutiny by policy makers. No committee of the General Assembly holds hearings on tax expenditures or systematically examines them as part of the budget process. Remarkably, Gov. Kasich has not proposed to limit or eliminate a single tax expenditure in his budget proposal. This is despite huge reductions in aid to local governments and proposed cutbacks to public education and higher education spending, programs for children, and most other items in the budget

A number of other states have a regular review process for tax expenditures. Since Ohio does not, we have no idea if the breaks are accomplishing their purpose or in some instances even what that purpose might be. This contradicts Gov. Kasich's stated intention to crack down on corporate welfare.

Among the highlights in the new report are:

- The number of tax expenditures has grown. It increased to 128, from 122 in the previous biennium.
- Most of the exemptions, credits and deductions go to businesses. Seventy-three of the tax expenditures, accounting for just over half of the total value in FY12 or $3.7 billion, go for business assistance and economic development.
- Sales-tax expenditures account for the largest share of the total: 56, adding up to $4.8 billion in FY12 and more than $5 billion in FY13.
- Credits against the commercial activity tax (CAT) will amount to $456.7 million in FY12, compared to estimated tax collections of $1.47 billion.
- Five business tax credits against the commercial activity tax – four economic development incentives and a credit against past losses – are estimated to add up to more than $100 million in annual tax credits. This tax was created in 2005 in part to cut down on loopholes that had existed in the corporate income tax it replaced.

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- The state continues to provide special-interest tax exemptions and credits such as one for wealthy buyers of time shares in jet aircraft. That sales tax cap is worth more than the $500,000 a year by which the governor's budget proposal would reduce aid to foodbanks. Eliminating the sales-tax exemption for pollution-control equipment purchased by utilities – most of it mandated – could reduce the cut to libraries by 21 percent.

Even while existing tax expenditures are going unexamined, the General Assembly is adding new ones. The recently approved transportation budget includes an exemption under the CAT for certain exchanges of motor fuel. ODT estimated its cost at $5 million to $10 million a year, not including a clause making it retroactive. It was approved despite opposition from business groups, which saw it compromising the broad base of the tax.

The General Assembly should closely review the tax expenditure report, and reduce or eliminate unneeded loopholes. It should set a target – 10 percent of the $7.4 billion estimated for FY12 would make a good starting point – for temporary or permanent annual reductions as part of the FY12-FY13 budget. This could include reductions in tax credits, as other states have undertaken.

The General Assembly should set up a schedule to review all tax expenditures on a permanent basis. The purpose of each of the 128 tax expenditures identified in the report should be spelled out, so that the review can determine whether that purpose is being met. New tax expenditures should have automatic sunsets, so they only continue after their worth has been proven.

Not all tax breaks and loopholes are covered in the tax expenditure report. For instance, lobbyists don't collect sales taxes; the sales tax only covers services if they are specifically named in the law. A new income-tax deduction for gambling losses is not included because it won't affect collections in the FY12-13 biennium. These tax breaks don't make sense.

While it does not provide a comprehensive list of loopholes, Ohio's tax expenditure report provides a beginning point for analysis and action on this important element of the state budget. Now, it is up to the General Assembly to get started.