Policy Matters Ohio

TESTIMONY
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Tax & Budget

Testimony to the Tax Expenditure Review Committee

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Good morning, Chairman Oelslager and members of the committee. I am Zach Schiller, research director at Policy Matters Ohio, a nonprofit, nonpartisan research institute with the mission of creating a more prosperous, equitable, sustainable and inclusive Ohio. Thank you for this opportunity to testify today. As we have said earlier, we are pleased to see the implementation of House Bill 9 of the 131st General Assembly, which established a formal review of Ohio's $9 billion in annual tax expenditures, commonly known as tax breaks.

We have some specific points about the sales-tax breaks you are hearing testimony on today. However, in addition to the recommendations we made at your April 11 hearing, we suggest there are broader issues you should consider that go beyond the specifics of each tax break being reviewed at today's hearing or the others you have.

House Bill 9, the statute that created this committee, provided that any bill proposing to enact or modify a tax expenditure should include a statement explaining the objectives and the sponsor's intent. Legislative history and sponsor's intent are both cited in the statute as among the things the committee may consider as part of reviewing the public policy objectives that might support the tax expenditure. While the LSC has said that it is unable to state why a tax exemption was enacted, or the extent to which it is meeting its original intent, that does not remove the need for the committee to examine those questions. The purpose of many tax expenditures may appear self-evident, but in others it is not. Every tax expenditure should have a specific, known, valid purpose or it should not exist. The committee should adopt a mechanism for determining the explicit purpose and if one cannot be ascertained, you should recommend elimination.

We were glad to see the LSC estimates of the revenue losses to counties and transit authorities for the first five sales-tax breaks on your list. Just those five amounted to a total of $792.4 million for the current fiscal year. You should ask the Department of Taxation to break that down for each sales tax exemption by county and transit agency. Residents and local officials should watch these hearings with a clear understanding of how state tax breaks affect local budgets as well.

Some tax expenditures, such as the LLC loophole (otherwise known as the passthrough tax break for business owners), are unproductive and should be scrapped. We hope that you will see fit to recommend such reductions. But the committee also should make recommendations on how the review of tax expenditures should be integrated into the regular biennial budget process. Beyond providing a copy of your reports to the governor, legislative leaders and the public, you should provide alternatives on capping or otherwise reducing tax expenditures. For instance, last year, when the General Assembly was forced to shave hundreds of millions of dollars from the 2018-2019 biennial state budget, the reduction of tax expenditures should have figured prominently in the discussion. Spending is spending whether it is through the tax code or the budget; tax expenditures should not be off limits when spending must be cut. The committee should make recommendations on how to best accomplish such cuts, apart from changes you recommend to specific tax breaks.

The committee also should make recommendations on reporting requirements for businesses receiving the benefit of tax expenditures. The law provides that, "For each expenditure reviewed, the committee may recommend accountability standards for the future review of the expenditure." We previously urged you to document where feasible the number, wage levels and compliance with state law of firms benefitting from each individual tax break. The state should also take other steps to ensure that companies with tax breaks are benefitting Ohio and Ohioans. Companies should have to disclose major layoffs, as already required in WARN notices; should disclose production shifts to foreign locations; should explain whether their actions have made any employees eligible for Trade Adjustment Assistance; and should describe impact on all affected communities if a plant or operation benefitting from a tax break is being moved from one location in the state to another.

Tax expenditures aimed at economic development represent only one of the state's tools. While the current budget provides for a bit more transparency, we still lack a full accounting of the state's investments and policies promoting economic development. These range from grants and loans to road-building and electricity discounts. All of these should be brought together in a unified economic development budget so the public and lawmakers can understand what is working and what is not.

Regarding the five sales-tax breaks that you are hearing testimony on today:

- 1.06, Sales of tangible personal property to electricity providers. This tax break was established in 2000 in connection with an overhaul of Ohio's regulation of the electricity market. In light of the major upheaval and possible changes in that industry, we recommend that you schedule this tax expenditure for future review.
- 1.07, Tangible personal property used or consumed in agriculture and mining. This section of the law would be modified under House Bill 430, which has been approved by the House and now is in the Senate Ways & Means Committee. Under current law, companies that produce oil and gas in Ohio already enjoy an exemption from the sales tax for purchase of tangible personal property "directly used in production" of oil and gas. House Bill 430 removes the qualification that that property be used "directly" in such production. This is a key definition long used in other sales tax exemptions, like the manufacturing tax exemption. Governor Kasich vetoed a similar bill that would have broadened the tax exemption for the oil and gas industry, warning that it would create an uneven playing field, and other industries would also seek to broaden definitions in similar exemptions – like some of the ones you are examining today and the ones you heard about last week. Commissioner Testa repeated this caution in the hearing on House Bill 430 last week. This illustrates how the General Assembly broadens tax breaks over time.
- 1.08, Agriculture land tile and portable grain bins. This exemption, approved in 1985, covers what would otherwise be considered real estate as opposed to tangible personal property, and not eligible for the agriculture exemption. Thus, it represented a broadening of the exemption.

- 1.09 and 1.10, These two exemptions, covering tangible personal property used to produce printed materials and in storing, preparing and serving food, each overlap with the manufacturing exemption. It is our understanding that these exemptions were part of the tax exemption for tangible personal property related to direct retail sales, which is no longer in place. As part of your review, you should examine that history.

As this shows, a careful analysis of each tax expenditure, including how it came to be and how it fits into other existing tax expenditures, should be a part of the committee's work. This includes tax expenditures that have been broadened since they were first enacted. The General Assembly should appropriate funds to dedicate staff to this undertaking.

Even as this committee has begun its work, tax breaks and proposals for additional ones have been proliferating. These have included expanding the income-tax deduction for business owners; a $45 million rural jobs credit; a sales-tax exemption for prescription eyeglasses; expansion of college savings accounts to cover tuition at private K-12 schools and a permanent sales-tax holiday. Bills now under active consideration include not only the expansion of the sales-tax exemption for the oil and gas industry, but a gigantic increase in the movie tax credit and a new "transformational mixed use development credit" that could cost $50 million for a single Cleveland project.

Before approving new tax breaks for oil and gas companies, insurers, movie producers and others, the General Assembly should make sure that its mechanism for reviewing existing ones is working. Adding new special-interest breaks is ill-conceived when this committee has barely started looking at the tax exemptions and credits we have now. When the General Assembly thinks about giving away tens of millions for new business tax breaks, it should consider whether we have the money to pay for them, and whether the funds would be better spent educating young Ohioans, cutting our high infant-mortality rate, or fighting the opioid epidemic.

Ultimately, the General Assembly should add sunsets to all of Ohio's tax expenditures so that each would require regular approval. Tax expenditures should not be continued indefinitely any more than the other spending you approve in the capital, transportation and operating budgets.

Thank you for this opportunity to testify. I will be glad to answer questions.