Policy Matters Ohio

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Budget

Investing for growth

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Introduction

Policymakers in Ohio have cut taxes for the wealthy at the expense of paying for services that help our communities thrive. Common-sense tax restorations on those who can afford to pay more could instead allow direct investments in schools, local governments, aid for college and public transit systems. Such investments have a high return. When we fund communities, money returns to the economy and jobs and wages increase. A new analysis finds if policymakers implemented a fairer tax system and invested the revenue in people and communities, in 2020 the state would add 39,601 more full- and part-time jobs, wages would increase by $1.7 billion, and state gross domestic product (GDP) would grow by $2 billion. Those gains would be in addition to the direct benefits of public services. This analysis does not account for longer-term benefits of better educating Ohioans and funding services that help communities prosper.

A tax system should raise revenues fairly and fund needed services and infrastructure. After years of income-tax cuts that have disproportionately favored the wealthiest, Ohio's tax system is upside down. It rewards the wealthy at the expense of low- and middle-income Ohioans. Under the current system, low-income Ohioans pay nearly twice the share of income in state and local taxes as the top 1 percent, who earn more than $1 million a year on average. The income-tax cuts the wealthiest 1 percent of Ohioans have enjoyed in most years since 2005 average more than $40,000 a year.[1]

State tax cuts have not helped the economy. Ohio job growth since they began has been slower in most years than the national average, as is our median wage growth.[2] Since 2005, Ohio job growth was just 4.4 percent compared to national growth of 12.2 percent. Meanwhile, Ohio's public services from education to public transit are underfunded.

In *Overhaul: A plan to rebalance Ohio's income tax*, Policy Matters Ohio proposes a tax plan to restore state income tax rates on the highest brackets of income earned by the most affluent Ohioans and close a big, unproductive tax breaks. As the state cut taxes on the wealthiest, it raised sales and other taxes that weigh most heavily on low-income families. To rebalance the tax system, the Policy Matters plan would also strengthen the state Earned Income Tax Credit (EITC), a tax credit for working, low-income Ohioans with children.

Working with the Institute on Taxation and Economic Policy (ITEP) to develop the revenue plan, and with the Regional Economic Models Inc (REMI) to model the economic impact of investing raised revenues into public services, Policy Matters developed estimates of the impact this plan would have on the statewide economy. The model considers public spending increases and how they cycle through the economy, but it also considers the fact that some filers will owe more in taxes and have less to spend elsewhere in the economy. This allows a comprehensive assessment of both the costs and benefits of these investments. However, because it doesn't consider long-term positive economic effects from education or reduced poverty, it understates the benefits of this plan.

[1] Zach Schiller and Wendy Patton, "Overhaul: A Plan to Rebalance Ohio's Income Tax" (Policy Matters Ohio), accessed November 9, 2018, https://bit.ly/2Q7MHwu.
[2] "Economic Policy Institute Analysis of Current Population Survey Data."

The revenue plan

The state can generate $2.6 billion in revenue by enacting a few common-sense changes to the state income tax:

- Restore the 7.5 percent income-tax rate on income over $217,400 approved in 1992 under Gov. George Voinovich;[3]
- Add a new 8.5 percent rate on income over $500,000;
- Repeal the business income deduction enacted in 2013, which is draining more than $1 billion a year from state revenues with little discernible impact on jobs or small-business growth; and
- Make our state EITC refundable, remove a cap that reduces the amount many Ohioans receive, and raise it to 20 percent of the federal amount.

Making the state tax system stronger and more equitable

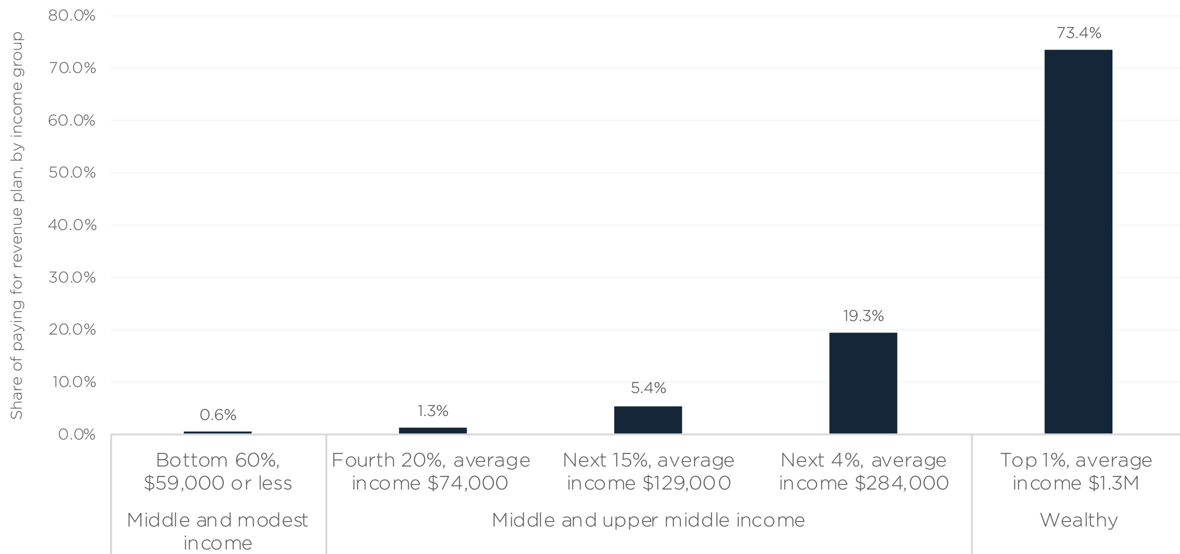
Figure 1 shows the distributional impact of the personal income tax changes recommended above. The top 1 percent, those earning more than $480,000 with an average income of nearly $1.3 million a year, would pay 73 percent of the increase. The next 4 percent, earning more than $194,000, pay 19.3 percent of the cost. Very few people in the bottom 60 percent of Ohio earners, making less than $59,000 a year, would pay more; in all, the amount paid by these tax filers adds up to less than 1 percent of the total (Figure 1).

Even under the Policy Matters plan, all Ohioans will be paying less in taxes, on average, than they did before the 2005 cuts. The wealthiest– the top 1 percent – paid $40,790 less in state taxes in 2018 compared to what they would have paid in 2005. Under the revenue plan proposed here, they'd still be paying $2000 a year less than they would have in 2005. Middle income Ohioans would, on average, pay tiny bit less in state taxes (-$30), which would offset the tiny increase in average taxes (+$10) since 2005. The expanded EITC in the revenue proposal would, on average, offset the average increase in taxes paid by the lowest-income Ohioans since 2005. (Figure 2).

[3] Ohio's income-tax brackets change each year based on inflation, so originally, this bracket began at $200,000. The $218,250 amount is the Institute on Taxation and Economic Policy's estimate from earlier in 2018 for where the top bracket in the income tax would be for 2018, adjusting for inflation from the 2017 amount of $213,350. The actual top bracket will begin at $217,400, according to the Ohio Department of Taxation.

Figure 1

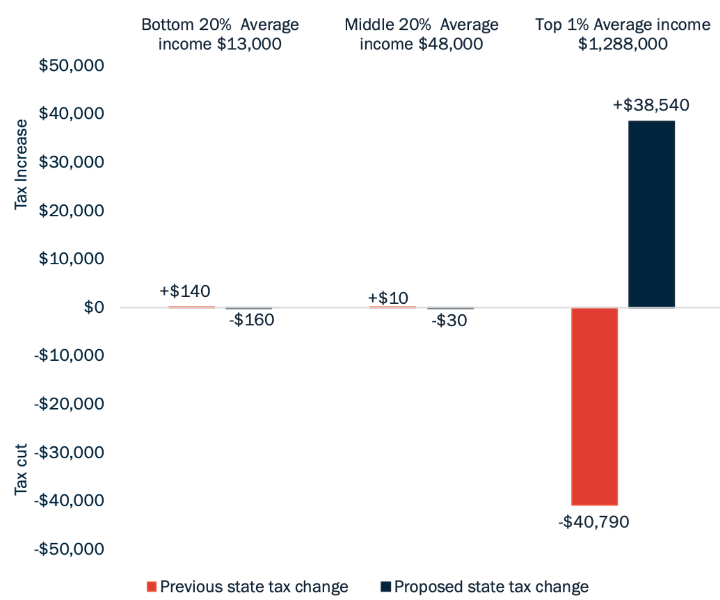
Share of the cost of proposed revenue plan, by income group



Source: Policy Matters Ohio based on data provided by ITEP May 2018 data covers Ohio residents only at 2018 income levels

Figure 2

Proposed state revenue plan: Average state tax since 2005 compared to proposed tax changes, 2018



Source: Policy Matters Ohio based on data provided by ITEP May 2018, data covers Ohio residents at 2018 income levels

Earned Income Tax Credit

In 2017, more than 1.6 million Ohioans lived in poverty — more than the populations of Cleveland, Columbus and Cincinnati combined. Of these, more than half a million were children.[4] The Earned Income Tax Credit (EITC) is designed to help low-income working people. Despite high need, Ohio has one of the weakest EITCs in the nation.

The federal government and 24 states have an EITC. It is one of the nation's most effective anti-poverty programs. Ohioans are eligible for the state EITC if they receive the federal credit and have earned income within set guidelines. Three elements of Ohio's EITC make it less effective: it has an income cap, the credit is smaller than average state credits, and it is not refundable.

Because of the income cap claimants with taxable income over $20,000 can only claim half their total income tax liability as their EITC, even if they are otherwise eligible for more. Lack of refundability means workers do not get the full value of the credit. For example, the average Ohio EITC for people earning between $23,000 and $40,000 is $120. If the claimant has $100 in tax liability, then the remaining $20 of EITC is simply lost. In a refundable state, the $20 would be returned as part of a tax refund. Only four states, including Ohio, make their credits nonrefundable. The value of Ohio's credit is only 10 percent of the federal credit. The credit is so low 95 percent of the poorest Ohioans get nothing.[5]

Policy Matters proposed a plan that makes Ohio's EITC refundable, removes the cap, and raises it to 20 percent of the federal amount. These reforms would provide low-income working families with an additional $424 million to spend in Ohio's economy. The cost of the EITC is paid for by the revenue generated from the progressive tax plan

[4] U.S Census Bureau, "QuickFacts Population Estimates Cincinnati City, Ohio; Columbus City, Ohio; Cleveland City, Ohio," July 1, 2017, https://www.census.gov/quickfacts/fact/table/cincinnaticityohio,columbuscityohio,clevelandcityohio/PST045218
[5] Hannah Halbert, "Refundable Tax Credits for Working Families Put Kids First" (Policy Matters Ohio, November 9, 2018), https://www.policymattersohio.org/research-policy/quality-ohio/revenue-budget/tax-policy/refundable-tax-credits-for-working-families-put-kids-first

The investment plan

According to an analysis by the Institute for Taxation and Economic Policy, the proposed tax plan would generate $2.6 billion a year, including the cost of expanding the EITC. Policy Matters recommends the additional revenue be used to fund important public services. We will detail many of these proposals in our forthcoming Investment Budget paper. The key investment areas are local government, K-12 education, public pre-school, need-based financial aid for college students (the Ohio College Opportunity Grant), and public transit (see Table 1), all of which have either long been underfunded or have seen their funding slashed.

Table 1

Investment areas

Investment Area	Amount
Local government	$860,000,000
K-12 education	$830,000,000
Pre-school	$440,000,000
Ohio College Opportunity Grant	$300,000,000
Public Transit	$145,000,000
Total	$2,575,000,000

Source: Policy Matters Ohio

Restoring funding for local governments

Over the past decade, state lawmakers have starved local governments of revenue needed to perform basic services. From 2010 to 2017, Ohio's local governments lost $1.2 billion adjusted for inflation. In the 2012-13 state budget, state policymakers cut the local government fund in half, abolished the estate tax and accelerated a phase-out of tax reimbursements for local business taxes abolished previously[6] In the 2018-19 budget, local governments and transit agencies lost $207 million as a result of the elimination of a Medicaid provider tax, the Managed Care Organization tax (MCO tax), which had been in the base of the sales tax since 2009. While lawmakers provided some backfill from surplus revenues, they did not create a long-term fix for the revenue loss.[7]

These deep cuts make it harder for local governments to provide essential services. Local government needs proper funding to repair roads and bridges, ensure safe and lead-free water, re-open recreation centers and swimming pools and support public safety.

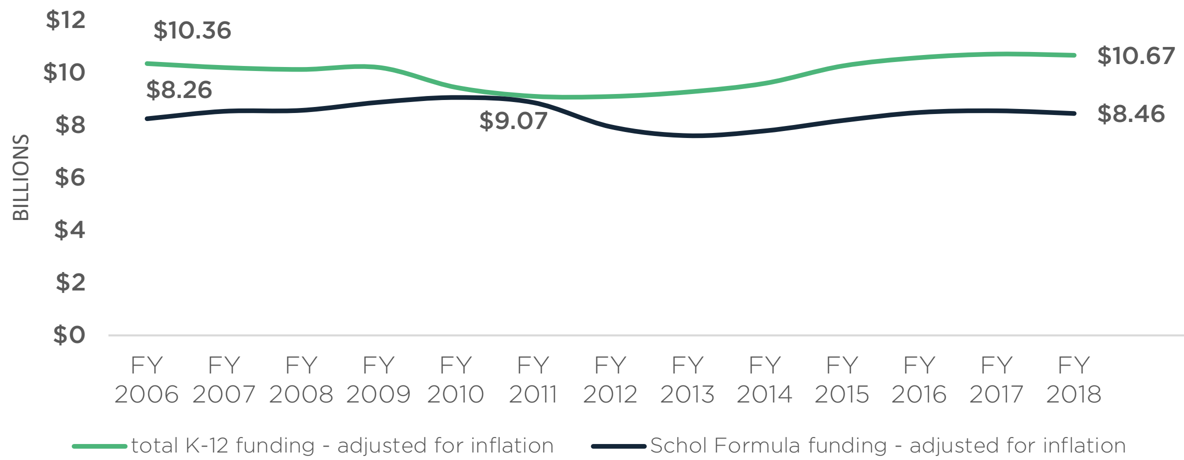
Increasing funding for K-12 education

For the 2018-19 budget, 221 of 610 school districts are flat funded and 147 lose funding. There are 242 school districts that gain between 0.1 percent to 5.9 percent in funding. State policymakers increased K-12 funding by only 2.7 percent over the last two-year budget. When adjusted for inflation, the state is actually investing less in aid for school districts than it did in Fiscal Year 2016. Underfunding has been a long-term trend. Total K-12 funding and school formula funding barely increased from 2006 to 2018 adjusted for inflation (see Figure 3).

[6] Wendy Patton, "State Cuts Sting Ohio Localities" (Policy Matters Ohio), accessed November 9, 2018, https://bit.ly/2MEX4GM
[7] Wendy Patton, "Post 2018-2019 Budget Bite: Local Governments" (Policy Matters Ohio, October 26, 2017), https://bit.ly/2A4YmG8

Figure 3

Total state aid for school districts and school formula funding from 2006 to 2018 adjusted for inflation



Source: Policy Matters Ohio based on LSC historical expenditure table: state-source GRF, LGF and ELPF

Total state aid for school districts consists of foundation funding paid through the General Revenue Fund and the State Lottery Fund as well as reimbursements for the loss of local tangible personal property taxes (TPP).[8] These cuts have real consequences. From 2005 to 2015, Ohio schools lost 3,269 educators – primarily librarians and art, music and physical education teachers.[9] School funding should be increased to reflect the actual cost of educating students and the cost of providing wraparound services such as mental health counselors, social workers and school nurses. Ohio needs a school funding formula that directs significantly more resources to the schools educating the neediest students.

Additionally, traditional public schools lost over $800 million in state aid in fiscal year 2019 to charter schools,[10] which do not perform better than traditional public schools.[11] The funding for charter schools is deducted from state and local funding for traditional public schools. In 2016, policymakers also sunk $236.6 million into vouchers despite those students performing worse than their peers in public school.[12] Four out of five voucher programs are funded by deductions in state aid to voucher recipients' school district of residence.[13] Only EdChoice Expansion is funded through a line item in the budget. Charter schools and vouchers should

[8] Victoria Jackson, "Post 2018-2019 Budget Bite: K-12 Education" (Policy Matters Ohio, October 10, 2017), https://bit.ly/2Go9RhJ.
[9] Victoria Jackson, "Number of Ohio's Vital School Professionals Dwindling" (Policy Matters Ohio, December 15, 2016), https://www.policymattersohio.org/research-policy/quality-ohio/revenue-budget/budget-policy/number-of-ohios-vital-school-professionals-dwindling.
[10] "Community School Funding Report FY 2019" (Ohio Department of Education, n.d.), http://education.ohio.gov/Topics/Finance-and-Funding/School-Payment-Reports
[11] "2017-2018 Annual Report on Ohio's Community Schools" (Ohio Department of Education, December 31, 2018), http://education.ohio.gov/getattachment/Topics/Community-Schools/Annual-Reports-on-Ohio-Community-Schools/2017-2018-Community-Schools-Annual-Report.pdf.aspx?lang=en-US
[12] David Figlio and Krzysztof Karbownik, "Evaluation of Ohio's EdChoice Scholarship Program: Selection, Competition, and Performance Effects" (Thomas B. Fordham Institute, July 7, 2016), https://edexcellence.net/publications/evaluation-of-ohio%E2%80%99s-edchoice-scholarship-program-selection-competition-and-performance.
[13] Philips, Jason, Jason Glover, Anthony Kremer, and Alexandra Vitale. "Redbook LSC Analysis of Executive Budget Department of Education." Legislative Service Commission, February 2017.

be funded separately from traditional public schools. Investing $860 million in public schools will help schools rehire lost educators and devote more resources to students.

Preschool for low-income three- and four-year-olds

Ohio needs $440 million to expand public preschool to all low-income three and four-year-olds. Ohio lags the nation in low-income children's access to preschool. Nationally, 29 percent of 4-year-olds and 5 percent of 3-year-olds from low-income families are in preschool. In Ohio, just 5 percent of such 4-year-olds and 2 percent of 3-year-olds are.[14] Preschool helps students learn to read. Children who attend preschool are better prepared for kindergarten than children who do not. The benefits are even more pronounced for low-income students, disadvantaged students and English learners.[15]

Ohio now provides $4,000 per child for public preschool for low-income students with family incomes at our below 200 percent of the poverty level, or $42,660 for a family of three.[16] Although many more qualify, only about 18,000 students are helped by the grant – $440 million would extend preschool to almost 97,000 more Ohioans. This should be expanded to all eligible children to ensure every child is prepared for kindergarten.

Expanding need-based aid for college

Ohio's only need-based financial aid for college, the Ohio College Opportunity Grant (OCOG), is woefully underfunded. In 2019, funding for OCOG will be $122 million less than in 2008 even before inflation (see Figure 4). In 2010, when the legislature replaced the Ohio Instructional Grant (OIG) and the OIG part-time grant with OCOG, the goal was to invest $250 million per year in aid. In 2008-09 we came close to the target by spending down the remaining OIG funds. With inflation increases that number would be significantly higher than $250 million today.

Community college students and regional campus students are excluded from OCOG because OCOG is a "last-dollar" grant for tuition and fees only. This means other aid, like Pell Grants, must be applied to tuition and fees before OCOG awards are determined. Full-time public university students are awarded $1,500 per academic year in OCOG. About 92,000 students at community colleges and 22,500 at regional four-year campuses would be eligible for OCOG based on their expected family contribution determined by the Free Application for Federal Student Aid (FAFSA). Restoring OCOG to full- and part-time students at these institutions would cost about $105 million a year. It would cost about $300 million a year to expand OCOG to community and regional campus students and increase the award to $2,068 for all eligible full- and part-time public college and university students, including Central State University.

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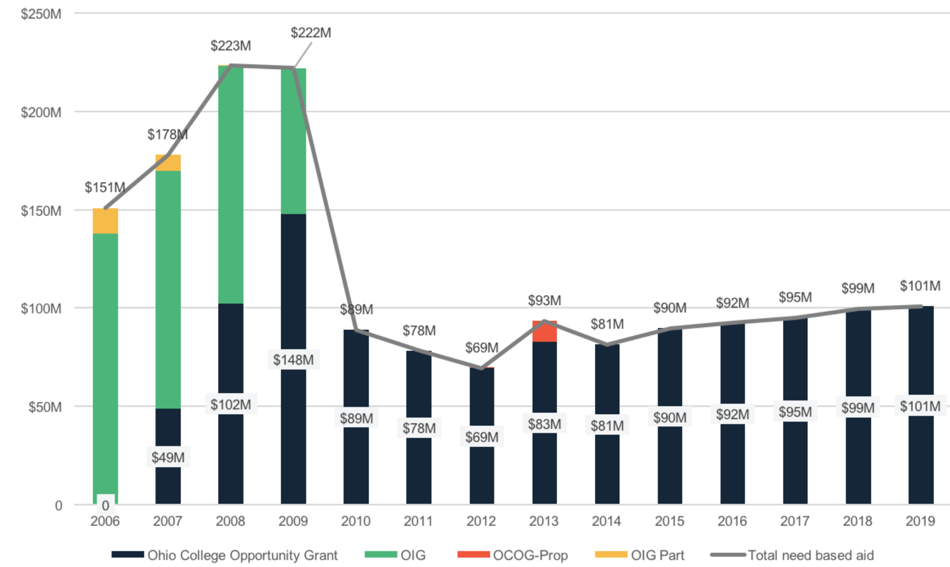
[14] https://www.policymattersohio.org/research-policy/quality-ohio/revenue-budget/budget-policy/budget-bite-early-care-investment-uncertain

[15] Claudio Sanchez, "Benefits Of Preschool: Kids Who Attend Public Preschool Are Better Prepared For Kindergarten : NPR Ed : NPR," National Public Radio, May 3, 2017, https://n.pr/2yixUFm

[16] "U.S. Federal Poverty Guidelines Used to Determine Financial Eligibility for Certain Federal Programs" (U.S. Department of Health & Human Services, November 23, 2015), https://aspe.hhs.gov/poverty-guidelines.

Figure 4

State support for need-based financial aid by year



Source: 2018-19 state budget, as enacted. FY 2017 actual OCOG spending. 2006-2016 are spending actuals reported in the Catalogue of Budget Line Items. OIG actuals higher than appropriated amounts because of phase-out spending. OIG-Part was need-based aid for part-time students in degree-seeking programs. OCOG-Prop is casino licensing fee revenue used on need-based aid for proprietary schools. Only included as a separate funding line in 2012-13 biennium budget, this added $10.6 million to total need-based aid funding that year. All unadjusted dollar. Excludes additional need-based aid support from federal sources.

Improving and expanding public transit

According to the 2015 Ohio Department of Transportation transit needs study, Ohio needed to invest an additional $125 million in public transit that year, and $185 million by 2025, to replace vehicles that are beyond their useful life, expand service to rural areas without transit, and preserve transit systems.[17] Currently, the state spends a meager $40 million on public transit, less per person than 44 other states and less than we spent in 1976.[18]

Public transit is an important work support. In Ohio, six of the 10 most common occupations pay too little to eliminate the need for food assistance for a family of three.[19] Working people who struggle to afford food likely struggle to pay for a car. As Ohioans age, public transit is important for getting to doctor's appointments and staying independent. In 2015, public transit across Ohio provided 115 million rides, but failed to meet market demand by 37.5 million rides. People in rural areas are especially harmed: There are 27 counties in Ohio without any transit service. An estimated one million rural Ohioans would be helped by expanding public transit into rural communities.[20]

[17] Ohio Department of Transportation, "Ohio Statewide Transit Needs Study," 2015
[18] Wendy Patton and Victoria Jackson, "How Ohio Funds Public Transit" (Policy Matters Ohio, May 26, 2017), https://www.policymattersohio.org/research-policy/sustainable-communities/transit/how-ohio-funds-public-transit
[19] Hannah Halbert, "Working for Less: Too Many Jobs Pay Too Little" (Policy Matters Ohio, April 30, 2018), https://www.policymattersohio.org/research-policy/fair-economy/work-wages/state-of-working-ohio/working-for-less-too-many-jobs-pay-too-little
[20] Wendy Patton and Victoria Jackson, "How Ohio Funds Public Transit" (Policy Matters Ohio, May 26, 2017), https://www.policymattersohio.org/research-policy/sustainable-communities/transit/how-ohio-funds-public-transit

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Findings and conclusion

In addition to the direct benefit to communities, spending in the key areas described above results in more jobs, higher wages, and a larger gross domestic product.

Policy Matters worked with the National Education Association to forecast how Ohio's economy would be affected if the state implemented the revenue and investment plans outlined here.[21] The analysis was prepared using the Regional Economic Models, Inc. (REMI) system, an economic modeling software that tests the economic effects of public policies. The REMI analysis projects gains in employment, wages and GDP as a result of the $2.6 billion investment in local government, K-12 education, pre-school, Ohio College Opportunity Grant, and public transit. It includes the reduced spending by individuals that would result from effects of the tax increases along with the additional spending.

Public investments in communities cause a ripple effect that increases total employment, salaries and wages, and gross domestic product (GDP). In 2018, Ohio's total full- and part-time employment was 7.1 million. Salaries and wages totaled $301.2 billion. GDP, a measure of the total amount of goods and services produced in a year, was $633.4 billion in 2018.

The analysis found that total employment would increase by over 37,000 jobs a year with the proposed revenue and investment plan from 2020 to 2025. Salaries and wages are projected to grow by around $2 billion a year. Ohio's GDP would rise by over $2 billion a year during the same time (see Table 2).[22]

Table 2

Increase in total employment, wages, and GDP as a result of Policy Matters' tax and investment plan

	2020	2021	2022	2023	2024	2025
Increase in total employment	39,601	39,667	39,358	38,906	38,202	37,304
Increase in wages	$1.7 billion	$1.9 billion	$2 billion	$2.1 billion	$2.1 billion	$2.2 billion
Increase in GDP	$2 billion	$2.1 billion	$2.1 billion	$2.2 billion	$2.2 billion	$2.2 billion

Source: Policy Matters Ohio based on REMI analysis conducted by the National Education Association

Investing in people spurs economic growth and yields long-term benefits that make Ohio stronger. By requiring the wealthy and corporations to pay their fair share of taxes, the state can generate much-needed revenue to invest in education, public transit, and local governments.

[21] The content and recommendations in this report are the work of Policy Matters Ohio. The progressive tax plan proposal used to generate the revenue for the REMI analysis, as well as the specific investment areas and investment amounts, were provided by Policy Matters Ohio. The National Education Association assisted Policy Matters Ohio with the REMI analysis.
[22] REMI analysis of Policy Matters Ohio's tax proposal

Appendix

The report reviews the economic impact of investing progressively generated tax revenue in education, local governments and public transit. It reviews the total number of jobs created, changes in salaries and wages, and Ohio's economic activity (that is, the gross state product).

Method

The purpose of this analysis is to examine the economic and employment consequences of bolstering Ohio's income tax system and investing in public services.

The REMI analysis cannot provide specific tax increases. The analysis only provides a total (aggregate) increase of $3 billion from personal income taxes. REMI calculates the EITC amount within a category called transfer payments.

Investment: For the investment of the tax increase, the REMI model assumed four distributions instead of the five above as follows:

- The Ohio College Opportunity Grant expenditure is a single category in the model.
- The pre-k and k-12 expenditures were combined in the model under state output.
- Public transit expenses are a single category.
- Local government investment is a single category.

Data for this analysis was provided by Policy Matters Ohio based on analysis from the Institute on Taxation and Economic Policy and Policy Matters Ohio. Using these inputs, a Regional Economic Models, Inc. (REMI) report for Ohio was created by the National Education Association using a structural macroeconomic model to quantify the impact of key public services with revenue generated for a progressive income tax plan on the broader Ohio economy.

REMI's models have been used in thousands of national and regional economic studies, including studies of health care reform and health care issues around the United States. The model used in this analysis covers the state of Ohio and includes 70 industry sectors.

For the REMI analysis, we thank Mike Petko of the National Education Association. For the tax plan analysis, we are grateful to the Institute on Taxation and Economic Policy. We appreciate the support of the George Gund Foundation, the Saint Luke's Foundation, the Fowler Family Foundation, the Raymond John Wean Foundation and the Ford Foundation for our work on investing in communities.