OHIO'S JOBS BUDGET 2.0

JOBS. MOMENTUM. TRANSFORMATION.

Reforms Book

The State of Ohio Executive Budget
Fiscal Years 2014-2015

Governor John R. Kasich

Office of Budget and Management
Director Timothy S. Keen

Ohio's Jobs Budget 2.0

Jobs • Momentum • Transformation

Governor John R. Kasich

Reforms Book

Ohio's Jobs Budget 2.0, Governor John Kasich's Executive Budget for fiscal years 2014 and 2015, continues important momentum that began with his administration's first Jobs Budget in 2011 and the Mid-Biennium Review in 2012. Those prior efforts were based on four fundamental principles, in which the budget:

- Is a Means to an End = Economic Development and Growth
- Retains Structural Balance and Strengthens Ohio's Financial Footing
- Is Based on a Comprehensive Review of All Agencies, Programs and Line Items
- Continues to Reform and Restructure State Government and Services

Guided by those same principles, *Ohio's Jobs Budget 2.0* lowers taxes, helps ensure better schools and more college graduates, reforms Medicaid and provides a stable funding stream for Ohio highways. Each of those key reform initiatives – and the hundreds of other state-agency reforms and efficiencies contained in the Governor's Executive Budget for Fiscal Years 2014 and 2015 – is focused squarely on one over-arching goal. That is to provide better opportunities and a better future for every Ohioan through a stronger, jobs-creating economy. This volume provides an expanded analysis of four reform initiatives contained in the Executive Budget.

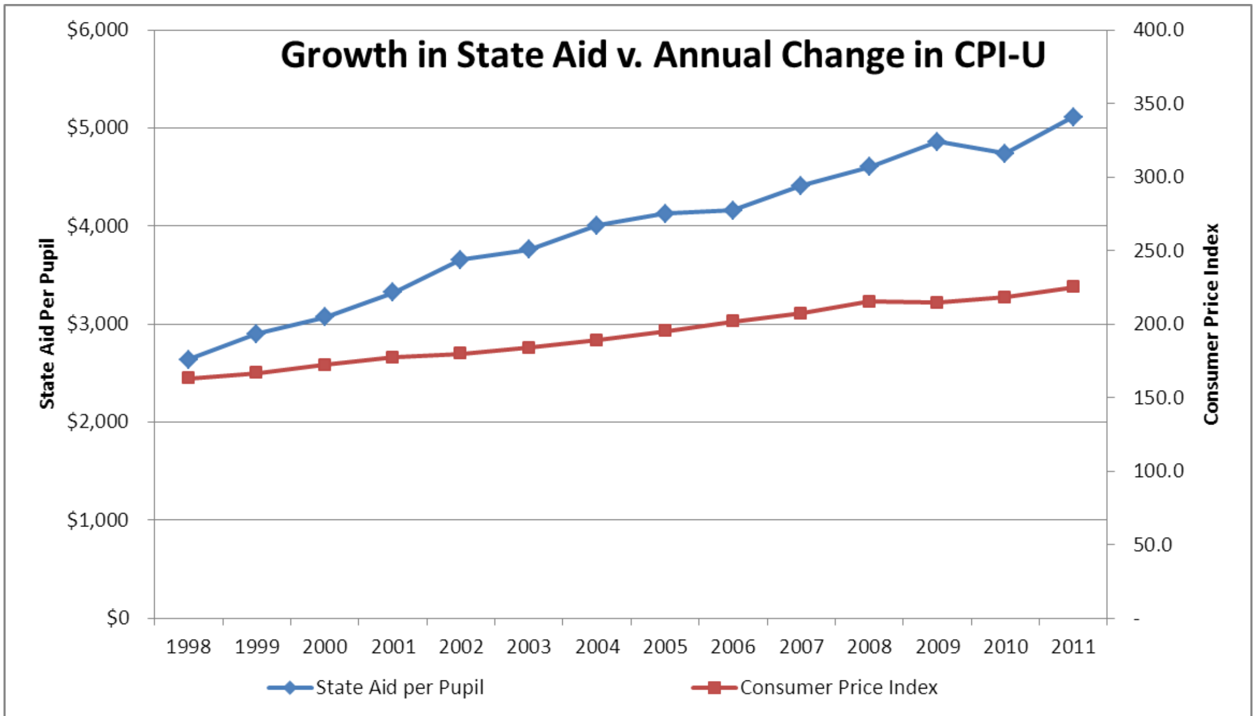
February 4, 2013

Appendix updated February 8, 2013

Achievement Everywhere
Common Sense for Ohio's Classrooms

State organization and tax support for public education in Ohio began in 1825 when the General Assembly established common schools and adopted a half mill property tax to help support public schools in the state.[1] The Ohio Constitution of 1851 included a clause calling for the General Assembly to "secure a thorough and efficient system of common schools throughout the state." This has placed education in a preeminent status among the public policy work of state government and has resulted in the state standards for what students are expected to learn and the basic structure and operations for schools throughout the state. Over time, Ohio's shared system of funding our public schools has developed.

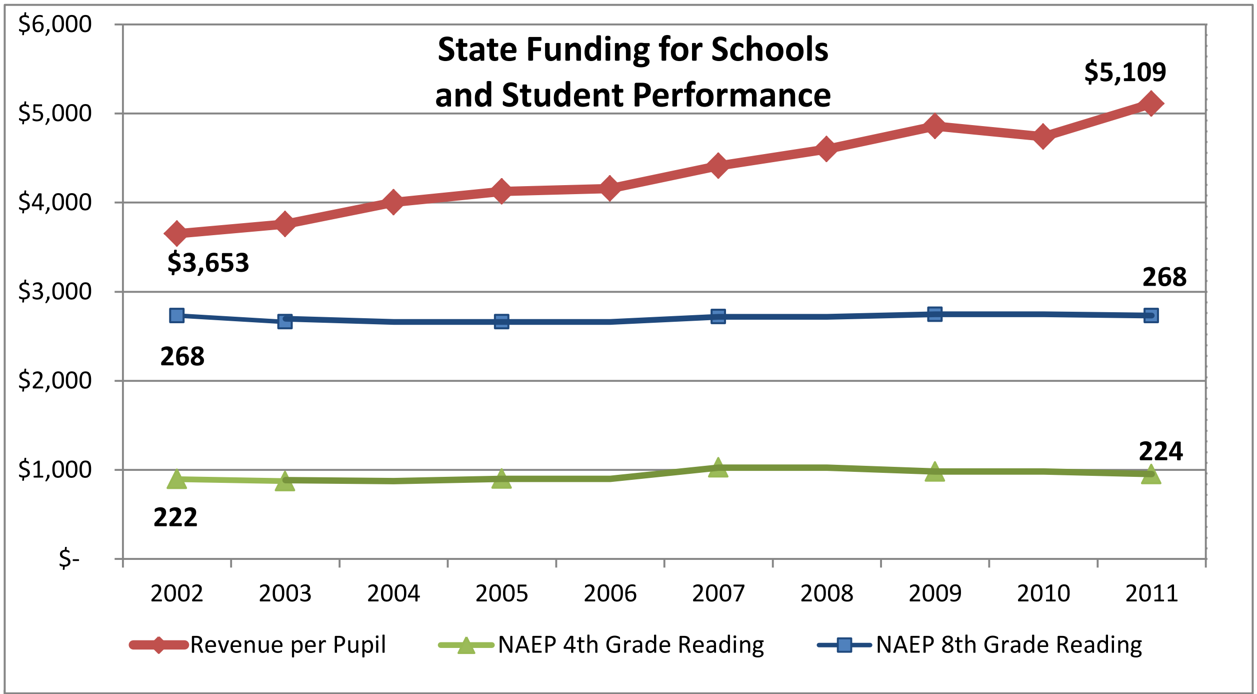
Since the Supreme Court ruling in DeRolph v. State of Ohio[2], state leadership has focused efforts on solving a school funding problem. By a measure of sheer volume, the state funding problem has been solved. Funding for schools has more than doubled since 1997 and has grown faster than the rate of inflation in nearly every year since[3].



This chart illustrates the percentage increase in the CPI for all urban consumers (CPI-U) as compared to the per pupil state revenue for school districts. The cumulative change in the CPI-U during the period is 40 percent; the cumulative change in state funding is 105 percent.

[1] "Public Education", Ohio History Central, July 1, 2005, http://www.ohiohistorycentral.org/entry.php?rec=1537
[2] *DeRolph v. State* (1997), 78 Ohio St.3d 193, 677 N.E.2d 733
[3] CPI-U data downloaded on January 27, 2013; ftp://ftp.bls.gov/pub/special.requests/cpi/cpiai.txt

At the same time, measures of student performance have only barely inched upward. As we directed more dollars into the education system, the ability of our students to compete for jobs and master basic educational skills has not kept up.



The chart illustrates the increase in state support for schools and the performance of Ohio's fourth and eighth grade students on the National Assessment of Educational Progress.

State standards and structures outlined for public schools in Ohio have also grown and become more complex. The state has adopted statutes or rules that far exceed setting basic standards for student learning and school operations. This complexity has created an environment where creativity and originality are stifled and the teacher must struggle to engage the active imagination of students.
Revisions to a funding system alone will not resolve these problems. Funding must be undertaken within a systematic review of state policy objectives and the statutory environment. By doing so, we enable creative and innovative learning opportunities to be implemented.

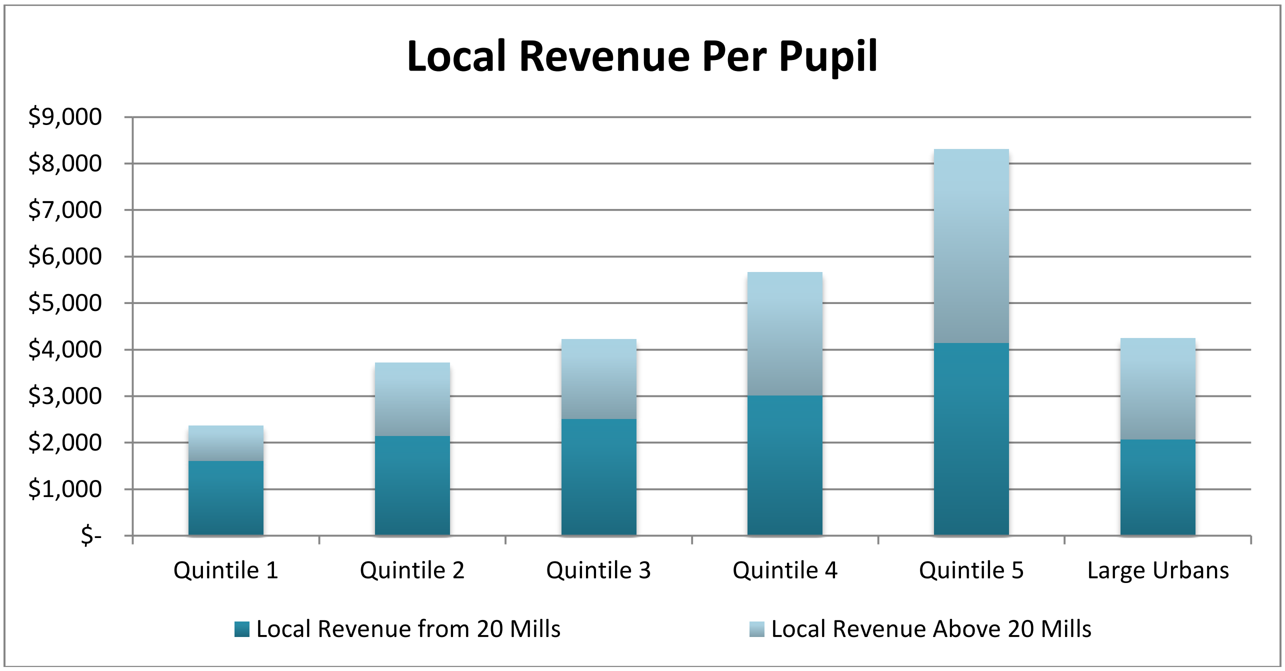
Supporting students as they grow and learn is a key policy objective of the Kasich administration. In today's world, the diversity of learning a student requires in an increasingly complex and globally connected society has pushed against the confines of the traditional school systems and models. Within this framework, the administration has embarked on a comprehensive plan to provide a fair method of distributing funding along with opportunities to invest in new and creative learning systems, ensure accountability for how the funds are used, and decrease the burden of unnecessary mandates.

Much work has already been completed through revisions to the accountability system, a strengthened commitment to developing reading skills in our early learners, teacher and principal evaluations, teacher preparation and the launch of Teach for America. In addition, programs were developed to introduce students to the connections between learning and careers and strengthening career technical education through an appropriate accountability system will better link student experiences in elementary and high schools to the life they will lead once they graduate high school. In preparation of this biennial budget, further review was conducted on the core funding systems, the rules and regulations defining school operations, ways to encourage transformative instructional programs, and the ability to evaluate school performance.

Through a commitment to provide resources to succeed, rewarding good ideas, free our teachers and leaders to achieve, and investing in what works, this budget presents a new approach to the state's commitment to the common schools of Ohio.

Resources to Succeed

A system of common schools will allow each student in Ohio to have access to an appropriate learning environment tailored to the needs of the student and the community he/she resides in. The diversity of opportunity in Ohio is immense – from large urban centers housing large industries and preeminent universities to isolated rural communities fueled by cottage industries and small learning communities. Across Ohio, the average local tax revenue per pupil for the districts in the lowest quintile of property wealth is a little over $2,000, while the average local tax revenue per pupil for the districts in the highest quintile of property wealth is over $8,000.

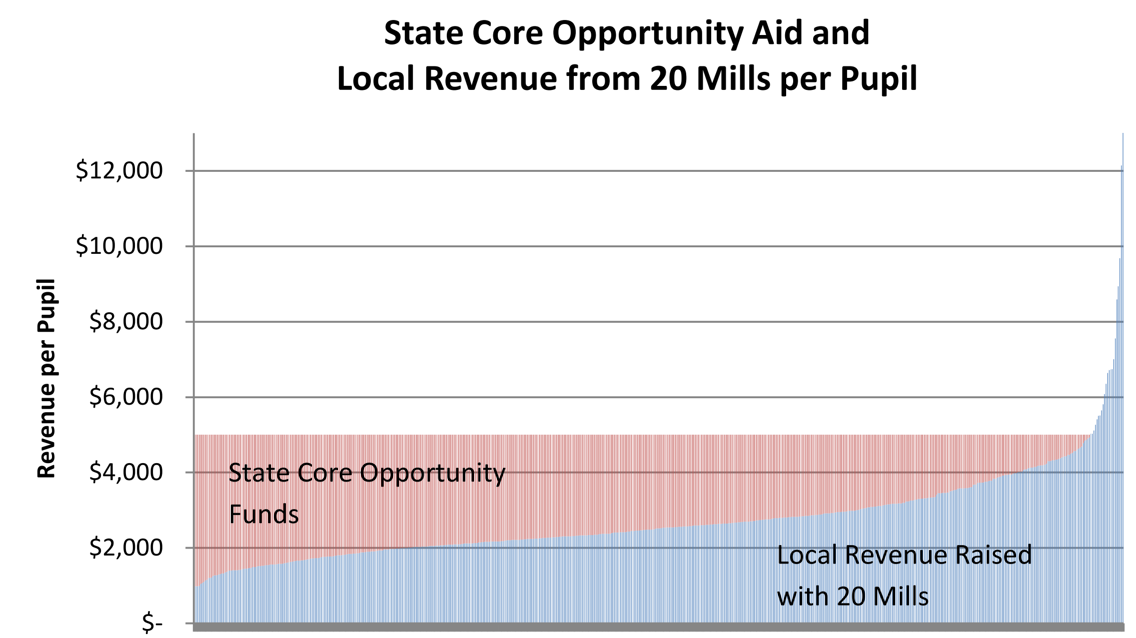


With the large urban districts in one group and the remaining districts divided into quintiles based on the local property tax base per pupil, the following chart displays the amount of local revenue districts raise on a per pupil basis. The chart distinguishes between the revenue raised on the first required 20 mills of property and revenue raised with taxes above 20 mills.

No funding system can entirely resolve the differences in the abilities of communities to access local resources, but it can ensure that sufficient funds are available to support the students as they progress from kindergarten to post-secondary opportunities. The state's role in this system is to allocate resources across the spectrum of school communities and provide each student with the opportunity to engage in an educational experience that will meet state standards.

The Governor's budget proposal reduces the local revenue disparity between districts and meets the needs of each individual child. We begin with a base that equalizes the revenue raised on the first 20 mills of local property taxes. For many years, the state has required school districts to levy 20 mills of local property taxes in order to participate in the state funding program. The amount of revenue generated from these funds vary significantly across the state as the poorest district in the state has a tax base of less than $50,000 per pupil and the wealthiest district has a tax base of over $700,000 per pupil. This means that the poorest district in the state will raise a little over $900 per pupil while the wealthiest will raise over $14,000 per pupil on these required 20 mills.

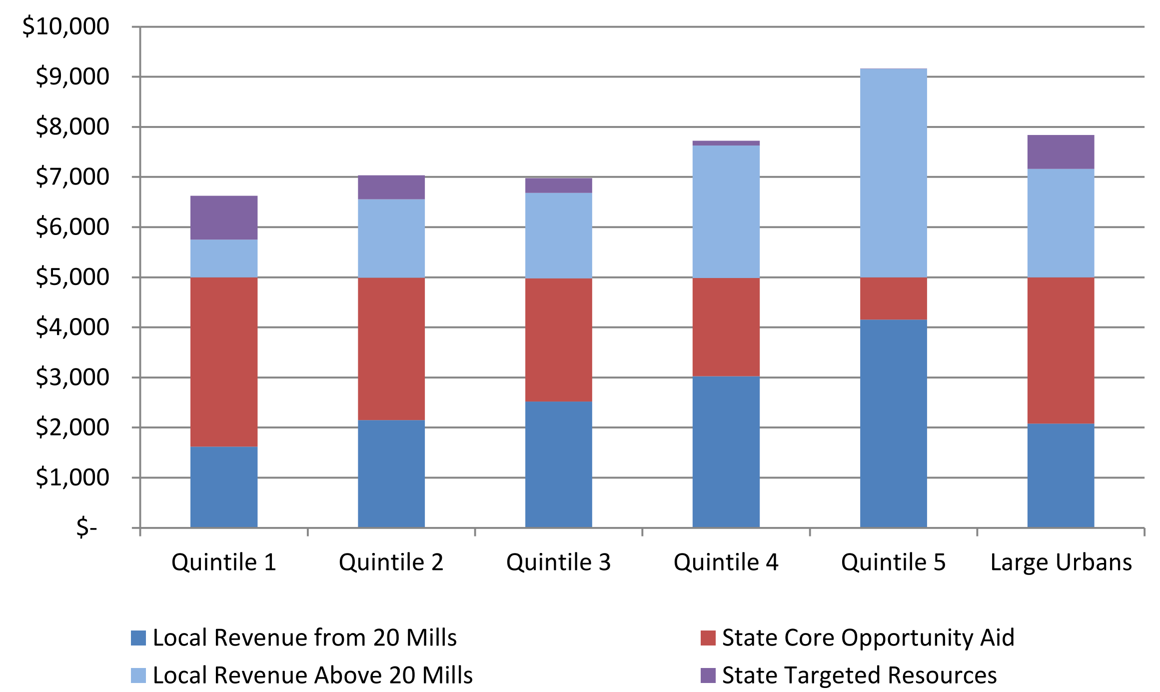
While the difference between the extreme ends of the property wealth spectrum is very large, the majority of districts have a tax base of less than $250,000 per pupil. In fact, only 24 districts have a tax base over $250,000 per pupil and are clearly the outliers in terms of property wealth. To provide capacity to those school districts with the lowest tax base, the Governor's proposal will ensure that all districts with a tax base less than $250,000 will raise the same amount of funds when local and state aid is combined.



This chart arrays local school districts[1] from the lowest property tax base to the highest and shows the amount of revenue raised per pupil on the required 20 mills of property tax in blue. The red area above the blue illustrates the impact of the base funding. As can be seen, every district in the state has at least $5,000 per pupil in combined state and local revenue for the required 20 mills of property taxes.

Targeted Resources: Most districts levy more than the required 20 mills; for the 20 percent of districts with the largest tax base, tax revenue generates an additional 15 mills. But the capacity of a district to raise additional funds is dependent not only on the value of the property tax base but also on the household income level of its residents. Most of the districts with the lowest property tax base also have households with lower income and many districts with average or above average property values have households with below average income. For example, Warrensville Heights in Cuyahoga County appears to be wealthy when only property values are used as the wealth measure due to a mall located in the district. But household incomes are below average, making it difficult for residents to support higher tax rates.

To provide additional assistance to those districts with the least capacity for levying millage above the 20 mills, the Governor is proposing ***targeted resources*** using an average of the property value and household income to create an overall wealth measure. For districts that are below the top 20 percent in wealth, additional state funding is provided by multiplying the difference between a districts wealth and the wealth of the district at the 80th percentile by a millage rate between 5 and 15 mills. The millage rate used is also dependent on the relative wealth of the district to the statewide average wealth – the poorest districts will receive the highest millage and the rate will decline as the wealth of the district increases. No district is required to levy additional mills to receive this aid – it is provided regardless of total tax rate a district has levied.



With the large urban districts in one group and the remaining districts divided into quintiles based on the local property tax base per pupil, this chart illustrates the impact of the Targeted Assistance Funding. The first two blocks in each bar show the local and state revenue per pupil in core opportunity funding. The light blue blocks show the average revenue raised per pupil above the required 20 mills of property tax. The targeted assistance funds are shown in the purple blocks and can be seen to help close some of the disparity between the lowest wealth districts in the first bar and the higher wealth in the fourth bar

Many student come to school with unique characteristics which require additional supports for the students to fully engage in classroom learning. They may need adaptations in order to hear and understand their teacher's lessons; they may need help catching up with their peers because of family struggles, or they may need more challenging course work. Teachers need assistance in their classrooms to help meet these needs and the Governor's proposal includes resources for the unique needs of students to support our students and teachers.

Students with Disabilities: All public schools are required to provide students with disabilities with a free and appropriate public education and must provide students with disabilities with the necessary support that allows them to engage in the educational programs of the school. The amount of services and supports required will vary depending on the severity of the disability. The Ohio Coalition for Students with Disabilities has completed cost studies that estimate the cost by disability category under the current rules governing the provision of services. Additional research was completed by Nathan Levinson, a national expert on education funding, that proposed alternatives for the delivery of special education services and the standards set by the state[4]. Based

[4] "Applying Systems Thinking to Improve Special Education in Ohio", Thomas B. Fordham Foundation, September 5, 2012, http://www.edexcellence.net/publications/applying-systems-thinking-to-improve-special-education-in-ohio.html

on the research conducted by these groups, a per-pupil amount of additional funding is provided for students based on the severity of the disability. Each district is provided aid based on the capacity of the district to provide additional resources from local tax revenues. However, no district is provided less than five percent of the amount calculated. The table below provides the per pupil amount for each category of disabled students.

Category	Description	Amount
1	Speech Only	$1,902
2	Cognitive Disabilities, Specific Learning Disability, Other Health Impaired (Minor)	$4,827
3	Hearing Impaired, Emotional Disturbance	$11,596
4	Visual Impairment, Other Health Impaired (Major)	$15,475
5	Multiple Disabilities, Orthopedic	$20,959
6	Deaf-Blind, Autism, Traumatic Brain Injury	$30,896

Some disabled students require extensive supports to engage in the educational programs at school and the cost of providing these supports can strain the budget of the school and reduce the opportunities offered to other students. From the funds calculated for the districts, an ***exceptional cost*** pool is created to reimburse schools when the cost to provide services to an individual student significantly exceeds the cost of services to other students in the disability category. This pool will allow districts to submit requests for reimbursement when the cost of providing services to an individual student in categories two through six exceeds certain thresholds.

English Language Learners: For those students who are not yet proficient with the English language, engaging in the educational programs at school first requires mastery of the English language and also frequently requires a district to provide translated communications to the student's family. As the student gains mastery of the English language, the amount of support necessary will decline. Therefore, $1,500 per English language learner is provided for the first year a student attends school in the United States and then decreases over the next two years by twenty-five percent. Once this transition period expires, funding continues to be provided to support interpreters and translation services when the student's family are not English speakers. Each district is provided aid based on the capacity of the district to provide additional resources from local tax revenues. However, no district is provided less than five percent of the amount calculated.

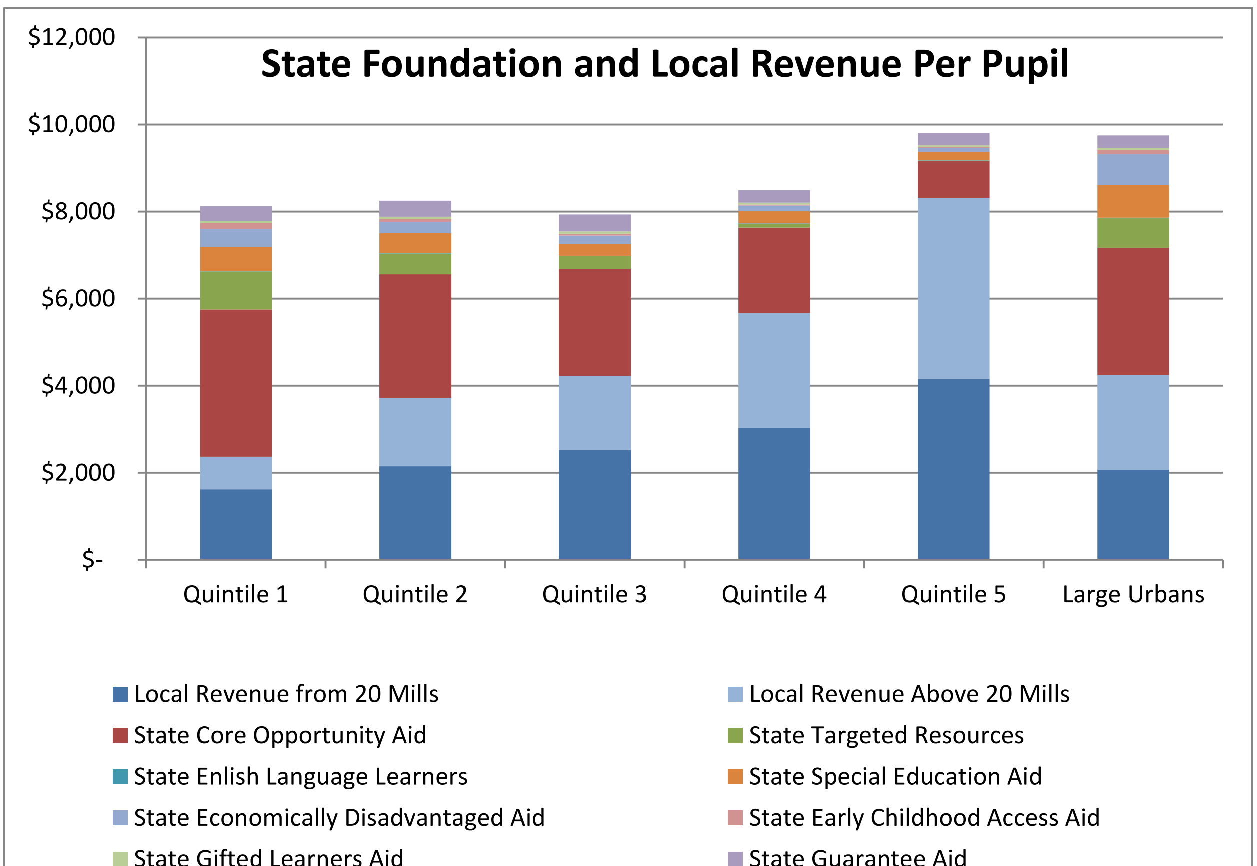
Economically Disadvantaged Students: Students from economically disadvantaged homes (as measured by eligibility for a free or reduced price lunch) frequently require additional supports, particularly in those districts with high concentrations of students living in poverty. Funding of $500 per disadvantaged student is provided for a district with a percentage of students equal to the statewide average poverty rate. This amount is adjusted higher for districts with above average poverty rates and decreases for districts with below average poverty rates. All districts are eligible for this aid.

Preschool Access: Access to quality early childhood programs has been proven to improve educational outcomes for disadvantaged students. A measure of access to early childhood programs was developed by comparing the availability of preschool programs in a district or its surrounding community to the state average access. A districts with an above average poverty rate and an access measure that is 50 percent of the statewide measure is eligible for these funds. A funding target of $600 for the estimated number of preschool students is set and adjusted up or down based on the access measure.

Gifted and Talented Students: Many students have special talents that can best be nurtured through alternative or more challenging instruction. Funding of $50 per pupil is provided for each student in the district to allow the schools to serve gifted students through the identification of gifted and talented students and by providing their teachers with the supports needed to modify instruction for these exceptional children.

Guarantees: These components represent the state resources necessary to help students succeed. However, over the course of the last 15 years, there have been significant and repeated changes to school funding in Ohio. Each of these changes included components that held districts harmless from changes related to the formula. These "guarantees" maintained funding levels or limited funding losses, regardless of a district's declining enrollment or increased taxing capacity. However, these guarantees are neither fair nor sustainable in the long term. As implementation of our funding formula without continued temporary assistance could destabilized a district's finances, each district is ensured the same level of funding for these core resources as was received in the prior year. It is important to note that the guarantee represents $880 million over the biennium and will represents 7.4 percent of FY 2014 foundation funding to traditional public school districts.

Final Funding Limitations: Over the course of the four prior fiscal years, increases in enrollment and/or declines in the taxing capacity of a district have had only a small part in the calculation of state aid to districts. As a result, districts with increasing enrollment or significant declines in property values have been underfunded. However, just as declining revenues can cause instability in district finances, sudden increases can also create disruptions in the budgeting process. Thus, for any district where the increase in aid above the core opportunity funds would result in an increase that is more than 25 percent of the prior year's state aid or 10 percent of the district's total resources, state aid growth is limited to the lower of these two tests.



With the large urban districts in one group and the remaining districts divided into five equal groups based on the local property tax base per pupil, the following chart illustrates the degree that state resources fill in when a local district does not have the capacity to raise local revenues.

The core funding components are focused on the needs of students in kindergarten through twelfth grade while engaged in core academic programs. However, other programs that schools offer are also addressed in the Governor's proposal.

Preschool Special Education: In addition to students in grades kindergarten to twelfth, districts are required to provide services to three and four-year olds with disabilities. Currently, the state provides support to schools that allows them to operate a classroom based on the minimum teacher salary in place prior to 2002. The administration's proposal provides $4,000 per preschool pupil plus one half of the special education funds per the categories listed above and adjusted for the district's capacity to raise local revenue.

Career Technical Education: The goal of Ohio's primary and secondary education system is to prepare students for life after graduation. Many of the opportunities that attract our students are careers in specialized trades and industries. Career technical programs allow students to tailor coursework in a way that allows students to learn specialized trades while mastering the core subject areas all students are required to learn. However, specialized instruction in the industry and trade fields require investments in specialized equipment and frequently require much smaller classes to maintain a safe learning environment. Additional funding is provided for each student in a career technical program depending on the type of program.

All students deserve an opportunity to explore career opportunities and experience career technical coursework. To ensure this opportunity exists, all public schools in Ohio serving middle and high school students, including community schools and STEM schools, will be required to join a career technical planning district. Supplemental funding for career technical courses will be distributed to the planning district to ensure equal opportunity is provided to all students attending member schools. The following table provides the per pupil amount for each category of career technical programs.

Category	Career Fields	Amount
1	Environmental & Agricultural Systems, Construction Technologies, Engineering & Science Technologies, Finance, Health Science, Information Technology, Manufacturing Technologies	$2,900
2	Business & Administrative, Hospitality & Tourism, Human Services, Law & Public Safety, Transportation Systems	$2,600
3	Career Based Intervention	$1,650
4	Arts & Communications, Education & Training, Marketing, Workforce Development Academics, Career Development	$1,200
5	GRADS, Family and Consumer Sciences	$900

In addition to the programs offered through the career technical planning districts, the U.S. Department of Labor registers apprenticeship programs that provide training in industries such as construction, manufacturing, information technology/networking, and health care which are sponsored by individual employers, joint employer and labor groups, and/or employer associations. The Governor's proposal calls for the Ohio Department of Education, the Governor's Office of Workforce Development and the career technical planning districts to develop joint programs with apprenticeship sponsors in Ohio which will allow high school students to begin work toward journeyman certification in the registered programs while still in high school. For each student that receives a journeyman certification upon graduation, the career technical planning district will receive $500.

College Credit Plus: For students planning to enter college after completing high school, the completion of college-level work while still in high school provides an opportunity to transition to post-secondary course work while still having access to the support of the high school community. Students earn both high school and college credit for these courses which can reduce the overall cost of higher education. However, under today's current structure, some students attend courses free of charge while other students must pay a reduced tuition rate for the same course. The barriers of the current system must be eliminated so that all students have the opportunity to participate in postsecondary opportunities while they are in high school if they are ready. To accomplish this, the Governor proposes a standard funding mechanism for all courses so that there are uniform opportunities for all students. All public high schools and colleges will be required to participate in these programs, with high schools required to provide all students with information on the post-secondary or dual-credit opportunities available, including programs offered through the career technical planning districts.

Boards of Developmentally Disabled: Many of the county boards of developmentally disabled provide programs for school aged children with more severe disabilities. The Governor's proposal will provide a per pupil amount that is adjusted for the disability categories listed above.

Early Learning Programs: The Race to the Top Early Learning Challenge Grant provided Ohio with funds to evaluate early learning programs and implement quality ratings for all preschool programs in the state. As the evaluation data becomes available in fiscal year 2015, the Governor is proposing a $2 million increase in Early Learning Funds to increase the number of preschool students served by our highest performing preschools.

Community School Facility Support: The Governor's proposal includes the acknowledgement that community schools do not have the access to permanent improvement funds like many school districts, and provides $100 per student attending a site-based publicly funded community school to offset the cost of maintaining healthy and safe facilities.

Safety and Security: To increase the safety and security of our schools, the Governor is proposing to make available funds to reimburse schools for the cost of retrofitting a school entrance with buzzers and security cameras and to purchase MARCS radio that will allow for instant 911 notification to local law officials if assistance is required.

Parental Choice: Students of families at or below 200 percent of the federal poverty guidelines entering kindergarten in FY 2014 will be eligible for an Educational Choice scholarship to attend a chartered non-public school. This pilot program, which will be paid by the state and not impact school district finances, will expand to first grade students in FY 2015. Additionally, students in kindergarten to third grade in schools that consistently fail to receive a C grade on the early learning component of the report card will eligible for an EdChoice scholarship.

Freedom to Succeed

Developing a system of common schools requires that the state develop rules and regulations that provide an outline of the educational programs offered across all schools – schools must be safe and healthy places of learning and a student from any district in the state should receive the same core curriculum. Thus, rules that require fire escapes and staff background checks are necessary for ensuring a safe and healthy environment. Rules that require students to master a common knowledge base in order to graduate from high school are necessary for ensuring our students can leave high school prepared for a career or higher education.

Common sense tells us that the rules and regulations which define the state standards for common schools should not limit the ability of a teacher to actively engage students in learning or find creative alternatives to the structure of the learning environment. When the state requires that a student must spend a fixed number of hours in a classroom in order to receive a high school credit, it fails to allow the student and teacher to explore alternative learning paces. Thus, we accelerate students by grade level instead of allowing students and their teachers to set a pace needed to master a subject and move on to more challenging material when they are ready.

The Governor's proposal calls for the State Board of Education to review and revise the operating standards set for schools to make sure that the standards do not set requirements that exceed what is needed to ensure students attend safe and healthy places of learning and receive the same core curriculum. In addition, state statutes were reviewed to remove legislative requirements that exceed these expectations, including the following:

- **Alternative School Years:** Traditional schools and district must currently set a schedule with a minimum number of days. This often hinders the implementation of creative learning environments. Allowing schools and districts to define the length of school days, weeks and years will allow them to meet the needs of their students. It is proposed that schools be required to offer at least 920 hours for elementary students and 1,050 hours for high school students.
- **Remove the Requirement to Pay a Fixed Amount per Pupil to an Educational Service Center (ESC):** Currently, many of our local districts are required to pay an ESC a per pupil amount and additional funds for the ESC to provide certain supervisory services. By removing these requirements, districts and ESCs can develop agreements that meet the needs of their students.
- **Remove Minimum Staffing for Speech Pathologists and School Psychologists:** Under law, districts are required to serve students who require speech therapy or psychological services and further requires one speech pathologist per 2,000 students and one school psychologist per 2,500 students. Requiring staffing levels without regard to the needs of the students creates a disconnect between the opportunity to provide each student with the resources they need to succeed and hiring or maintaining staff levels. Frequently, schools then employ to the standard, so that a school with 3,000 students will not hire an additional speech pathologist until there are 4,000 students in the school even when students need the surfaces. To ensure a safe and healthy learning environment for our students, we must allow schools to employ staff based on student needs.
- **Require Salary Schedules without Defining Structures:** Under current law, each school district must adopt salary schedules for teachers which are either based on training and experience, on level of licensure, on whether the teacher is highly qualified, and on performance evaluation ratings. None of these methods allows a school district to develop salary schedules (as opposed to supplemental contracts) that provide for differentiated teaching roles such as mentors for new teachers, instructional coaching, high school teachers who are approved by colleges to teach dual credit courses, or student organization advisors. This change will allow school districts and their bargaining units to design salary schedules that support the priorities of the community.

Straight A Fund –
The grandparents of today's kindergartners may have never used a computer through high school or college; the parents of today's kindergartners probably used the computer station in their classroom as a reward for completing assignments; today's kindergartners may have a laptop or tablet that they are well adept at using. Technology today will allow a teacher in China to teach Chinese to students in Ohio in real time. Students no longer need to wait for two weeks for a letter from a pen pal, the classroom they partner with in another country can be Skyped. As the ability to break down barriers of time and place has flourished, students have come to expect that answers will be instantaneously available, accessible from multiple sources, and can be copied and sent via text messaging to a classmate.

Yet, for the most part, our schools still rely on clothbound text books and learning to fit within the confines of a five to six hour day. Students are expected to rely on just two sources of data for most of the day – the teacher and the textbook. Common sense tells us that unless we begin to change education at a pace that can keep up with changes in technology, students will lose interest in school and it will become increasingly more difficult to ensure our students receive the educational experience they need in order to thrive after leaving high school.

But finding the right changes that will engage students, capture the creativity of teachers, and be supported by the larger community may require an investment that diminishes the ability to maintain the current programs as new approaches to instruction are tested and evaluated. To help districts implement new instructional models, the administration is proposing the *Straight A Fund* to provide districts with grants to implement creative and transformative instructional practices.

Schools, districts, and consortiums can apply for *Straight A Funds* for creative programs that will be sustainable once the startup grant is exhausted. The grant process will be overseen by a committee appointed by the Governor and General Assembly with a subcommittee that is responsible for reviewing and recommending the applications received. Similar to the Ohio Third Frontier Program, this program is intended to allow schools to create programs that will best prepare students for their post-secondary careers or education.

Investing in Success

With the revisions to the academic report cards passed by the Ohio General Assembly in 2012, students, parents and communities will have an easy-to-understand report on how well schools are preparing students academically. Left out of the report will be information that answers whether these services are being provided efficiently. The relationship between academic performance and school expenditures is difficult to discern and there is very little correlation between the amount spent per pupil and the academic performance of the students.

The Center for American Progress published a report[5] that attempted to evaluate the productivity of school districts across the states. By developing a performance measure, the authors created a simple way to compare whether or not the dollars spent for academic achievement created a good return on taxpayer investments. Information about the return on educational investment allows parents, teachers, administrators and the community to evaluate the ability of a school or district to use their resources effectively. By understanding how a district compares to other similar districts, the community can determine if additional investment may be warranted.

Currently, the Ohio Department of Education publishes a variety of reports that provide information on the academic and financial status of each school district. These reports range from an academic report card to district financial profiles. The District Benchmarking Report[6] provides a combination of academic and fiscal data that attempts to tease out the relationship between the needs of students and the efficiency of non-academic programs. This report also benchmarks their performance against similar districts, other districts in the county, as well as state averages and can be the basis for a return on investment comparison across the state.

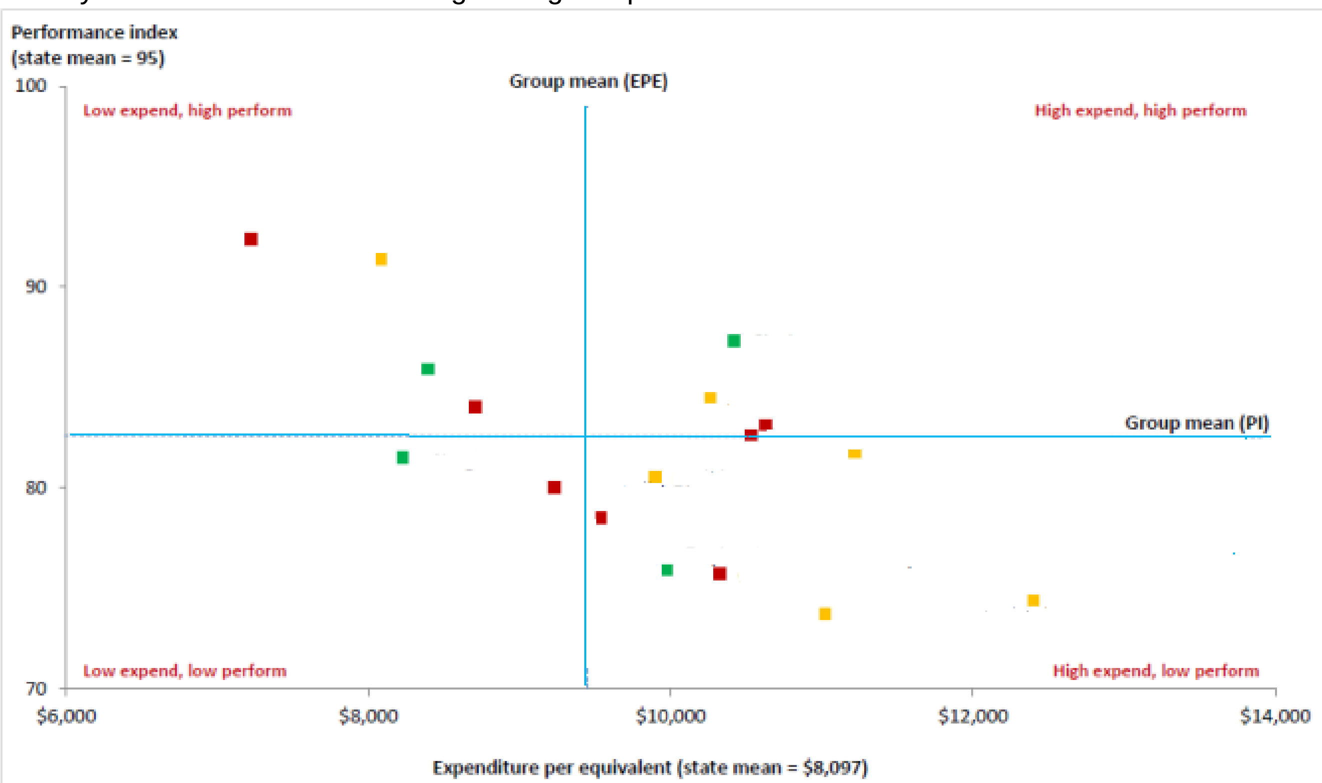
The Governor is proposing the creation of a data analytic website to provide comparison of academic performance and financial investments for each public district in the context of their twenty closest peer

[5] Boser, Ulrich; "Return on Educational Investment, A district-by-district evaluation of U.S. educational productivity;" January, 2011; http://www.americanprogress.org/issues/education/report/2011/01/19/8902/return-on-educational-investment/

[6] http://education.ohio.gov/GD/Templates/Pages/ODE/ODEDetail.aspx?page=3&TopicRelationID=1438&ContentID=48701&Content=129802

districts. By connecting academic and financial data, students, teachers, principle, parents and taxpayers will have an easily accessible site providing transparent and comprehensive data on financial, school and student performance. The following chart is an example of the information to be displayed on the site.

The chart displays information for a group of 20 similar districts; in this example, 20 urban districts are shown. The horizontal axis measures the expenditure per pupil after adjusting for the higher costs associated with students with special needs. The vertical axis measures the performance index for each district. The performance index is compiled by granting points for each student taking a state assessment – the better a student does on an assessment, the more points a district receives. A district with every student scoring at the top level of the assessments could earn 120 points. By dividing the graph into four quadrants, it becomes easy to identify which districts are achieving the highest performance with the dollars invested.



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Conclusion

Achievement Everywhere builds upon school improvement initiatives, such as the Third Grade Reading Guarantee and A-to-F Report Card, which Ohio is implementing in order to better educate Ohio's children and prepare them for successful careers. By taking on Ohio's persistent education disparities with $1.2 billion in new funds that help every student achieve—regardless of where they live—and by prioritizing classroom needs from early childhood to higher education, *Achievement Everywhere* advances the tradition of Ohio's strong partnership with independent local schools so that the next generation of Ohioans can realize their potential and lift our state to new heights.

Medicaid Transformation

Medicaid is the state/federal health-care program that provides health coverage to more than 2.3 million Ohioans with low incomes. Medicaid represents a large share of state budgets in six Ohio departments (Health, Mental Health, Alcohol and Drug Addiction Services, Developmental Disabilities, Aging and Job and Family Services). Medicaid currently represents approximately 25 percent of the state share of the general revenue fund (GRF), approximately 45 percent of GRF when the federal reimbursement is added. The program historically has been associated with high growth rates due to demographic and economic factors that impact the number of people covered and to health care inflation rates that greatly impact the cost of their services.

This Budget Builds off of Reforms from the Past Two Years

In the three years prior to Governor Kasich taking office, Medicaid spending increased 33 percent from $13.5 billion in state fiscal year (SFY) 2008 to $18.0 billion in SFY 2011. This rate of growth, which did not add any new populations to coverage, was unsustainable and threatened to crowd out other state budget and policy priorities, such as primary and secondary education.

Faced with these daunting budget trends and an overall state budget imbalance approaching $8 billion, Governor Kasich took action and created the Office of Health Transformation to immediately address Medicaid spending issues, plan for the long-term efficient administration of the Ohio Medicaid program, and act to improve overall health system performance (Executive Order 2011-02K). The new office quickly organized existing staff in all of the Medicaid-related agencies to advance the Administration's Medicaid modernization and cost-containment priorities in the operating budget. The goal of the Governor's first budget (HB 153) was transformational change—achieving better health outcomes, better care and cost savings through improvement.

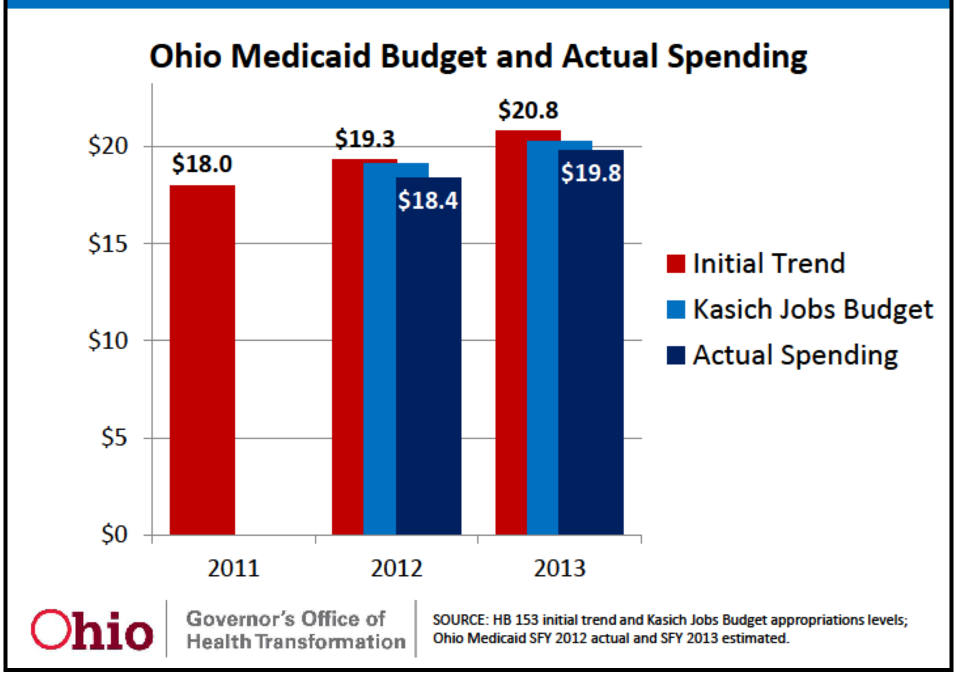
Improved Care Coordination. HB 153 improved how Medicaid coordinates care for sick and vulnerable beneficiaries, leading to better health outcomes for Ohioans and cost savings for Ohio taxpayers. For example, the budget launched an Integrated Care Delivery System (ICDS) to coordinate care for 114,000 Ohio seniors and people with disabilities who are eligible for both Medicare and Medicaid. By improving how we serve these vulnerable individuals, who account for 14 percent of the Medicaid population but roughly one-third of all Medicaid spending, Ohio's seniors and people with disabilities will live healthier lives and taxpayers will save money.

Rebalanced Long-Term Care. HB 153 allocated $532 million more for home- and community-based services over the biennium, allowing more Ohioans to live with dignity at home rather than in an institution, and it enacted measures to improve the quality of care in nursing homes by tying more of the nursing home rate to meeting quality measures.

Improved and Integrated Behavioral Health Services. HB 153 stopped years of declining funding for mental health and substance abuse services. By transitioning the financial responsibility for the non-federal share of Medicaid matching funds for alcohol and drug treatment and mental health carve-out benefits from community behavioral health boards to the state, the budget freed up millions in local levy dollars that county boards could use for other priorities. Ohio Medicaid and the Ohio Department of Mental Health also designed and launched a person-centered system of care, called a health home, to improve care coordination for high-risk Medicaid beneficiaries with serious and persistent mental illness, leading to better health outcomes and cost savings.

Reformed Payments and Spending Control. Governor Kasich's first budget proposed spending $500 million less than the trend in 2012 and $942 million less in 2013. At the same time, the budget introduced new tools to improve care coordination, integrate behavioral and physical health care, rebalance long-term care spending, and modernize reimbursement to reward value instead of volume. Ohio Medicaid used these tools to drive Medicaid program improvements and deliver *additional* savings, resulting in actual spending nearly $1 billion below the initial trend *in both years* (Figure 1).

Figure 1.



SFY 2014-2015 Budget

Budget Impact

The total Medicaid "baseline" – what the Medicaid program would cost in the upcoming biennium assuming current eligibility, benefit, and payment policies remain unchanged – is projected to grow 13.3 percent to $22.4 billion in FY 2014 and grow 4.5 percent to $23.4 billion in FY 2015 (Figure 2). There are several factors that account for this high baseline growth:

ACA Woodwork Enrollment Increase. The federal Patient Protection and Affordable Care Act (ACA) individual mandate to purchase health insurance is expected to result in some individuals seeking health coverage who were not previously seeking it, and some who might have been seeking it might not have found it. Under either circumstance, given the greater awareness of the need to have health coverage and the availability of Medicaid, more individuals who are currently eligible for Medicaid but are not enrolled are likely to do so. This is commonly referred to as the "woodwork effect." Given the fact that they will enroll without any changes in state policy, they must be included in the baseline estimates. Ohio Medicaid estimates more than 230,000 "woodwork" individuals will enroll in Medicaid by June 2015. This increases GRF baseline estimates by $531 million ($186 million state share) in FY 2014 and by $996 million ($335 million state share) in FY 2015.

ACA Physician Fee Increase. Another ACA-related impact on the baseline budget is the mandated increase in physician fees that began on January 1, 2013. Although this required two-year increase of Medicaid rates to the level of Medicare receives 100 percent federal reimbursement, it still requires estimated GRF appropriations of $321 million in FY 2014 and $262 million in FY 2015.

Health Transformation Initiatives. There are a few initiatives underway in the current biennium that have not been fully implemented and will continue being implemented in the next biennium, including implementation of health homes for people with serious mental illness, and enrolling disabled children in health plans. The most notable example is that the implementation of the Integrated Care Delivery System (ICDS) will not be fully implemented in FY 2013 due to a delay in federal approval of our waiver request. ICDS was authorized in House Bill 153 and is intended to better coordinate the care of certain individuals who are enrolled in both Medicaid and Medicare. This initiative is expected to reduce the rate of spending growth after full implementation is achieved, but it has initial start-up costs associated with paying the "run-out" of fee-for-service claims at the same time prospective payments are made to the health plans that will provide integrated care. Although the state has since received federal approval and has selected health plans through a competitive process, and enrollment is projected to begin this July, the "run-out" cost was originally expected to largely occur in FY 2013 but is now delayed until FY 2014. This is a contributing factor to the under-spending in this fiscal year and must be accounted for in the baseline for the upcoming biennium.

Savings and Cost Avoidance. The Medicaid baseline growth rates described above are not sustainable. While such rates would be of concern under any circumstances, they are particularly troubling after all of the Medicaid modernization and cost containment efforts in the current biennium that helped return Ohio's budget to structural balance. Therefore, the Executive Budget includes a number of cost avoidance initiatives intended to again emphasize value and establish the right incentives for cost-effective, quality care. These initiatives, generally payment methodology changes, are largely targeted at providers that benefit the most from the projected enrollment growth, such as health plans and hospitals. This package of savings and cost avoidance totals $517 million ($191 million state share) in FY 2014 and $801 million ($296 million state share) in FY 2015 (Figures 2 and 3).

Extend Medicaid Coverage. Governor Kasich's decision to extend Medicaid eligibility to adult Ohioans with income up to 138 percent of poverty will increase overall Medicaid appropriations but decrease the state share of GRF. The new income eligibility test will result in approximately 366,000 Ohioans becoming "newly eligible" for Medicaid, but it will also result in approximately 91,000 Ohioans who are eligible for Medicaid today moving off the program (they will have the option to seek coverage on the new federal Health Insurance Exchange). These enrollment changes are expected to increase Medicaid spending $500 million in FY 2014 and $1.9 billion in FY 2015 (Figure 2) – but the state share actually *decreases* $23 million in FY 2014 and $68 million in FY 2015 because the state saves from current enrollees leaving the program and the federal government covers 100 percent of the cost of the newly eligible population (Figure 3).

Executive Budget Appropriations. After factoring in baseline projects, savings and cost avoidance, and eligibility changes that will result in 545,000 more Ohioans receiving health insurance coverage through Medicaid, the Executive Budget increases overall Medicaid spending 13.2 percent to $22.4 billion in FY 2014 and 9.6 percent to $24.5 billion in FY 2015 (Figure 2). The state share-only GRF appropriations reflect projected growth of 10.8 percent to $5.6 billion in FY 2014 and growth of 2.7 percent to $5.8 billion in FY 2015. Savings and cost avoidance, coupled with eligibility changes, were able to reduce state share GRF appropriations by $213 million in FY 2014 and by $365 million in FY 2015 relative to baseline projections.

Figure 2. Ohio Medicaid Spending (All Funds in millions)

All Funds	SFY2012	SFY 2013	%	SFY 2014	%	SFY 2015	%	SFY 2014/15
Initial Trend in 2011	$ 19,342	$ 20,797						
HB 153 Appropriations [1]	$ 19,154	$ 20,298						
Actual /Estimate	$ 18,438	$ 19,768						
Initial Program Trend in 2013	**$ 18,438**	**$ 19,666**	**6.7%**	**$ 20,723**	**5.4%**	**$21,477**	**3.6%**	**$ 42,200**
Health Transformation Initiatives In Progress (HB 153)								
ICDS		$ -		$ 493		$ 298		$ 791
Health Homes		$ 25		$ 215		$ 303		$ 519
ABD Kids MCP Expansion		$ -		$ 87		$ 41		$ 128
Balancing Incentive Program		$ -		$ 27		$ 25		$ 52
Subtotal		**$ 25**		**$ 822**		**$ 667**		**$ 1,490**
ACA Mandates								
Woodwork		$ -		$ 531		$ 996		$ 1,527
Physician Fee Increase		$ 77		$ 321		$ 262		$ 583
Subtotal		**$ 77**		**$ 852**		**$ 1,258**		**$ 2,110**
Baseline Total	**$ 18,438**	**$ 19,768**	**7.2%**	**$ 22,397**	**13.3%**	**$23,402**	**4.5%**	**$ 45,799**
Savings & Cost Avoidance								
Health plan changes				$ (270)		$ (376)		$ (646)
Hospital changes				$ (163)		$ (337)		$ (500)
Nursing Facility changes				$ 15		$ 21		$ 36
HCBS changes				$ 4		$ 27		$ 31
Fight Fraud and Abuse				$ (33)		$ (41)		$ (74)
Other Provider Changes				$ (70)		$ (95)		$ (165)
Subtotal				**$ (517)**		**$ (801)**		**$ (1,318)**
Baseline Less Savings & Cost Avoidance		**$ 19,768**	**7.2%**	**$ 21,880**	**10.7%**	**$22,601**	**3.3%**	**$ 44,481**
Simplify Eligibility/ACA								
Eligibility Changes				$ (62)		$ (184)		$ (246)
Newly Eligible Enrollment (Pre Rebate)				$ 562		$ 2,111		$ 2,673
Newly Eligible Enrollment (Net)				**$ 500**		**$ 1,927**		**$ 2,426**
Executive Budget	**$ 18,438**	**$ 19,768**	**7.2%**	**$ 22,380**	**13.2%**	**$24,528**	**9.6%**	**$ 46,907**

[1] *Note: Amounts adjusted from $18.8B in SFY12 and $19.8B in SFY13 to include the budget for Medicare Part D and UPL appropriations*

Figure 3. Ohio Medicaid Spending (State Share of General Revenue Funds in millions)

GRF - State Share	SFY2012	SFY 2013	%	SFY 2014	%	SFY 2015	%	SFY 2014/15
Initial Trend in 2011	$ 5,336	$ 5,680						
HB 153 Appropriations [1]	$ 5,108	$ 5,293						
Actual /Estimate	$ 4,936	$ 5,079						
Initial Program Trend in 2013	**$ 4,936**	**$ 5,081**	**2.9%**	**$ 5,520**	**8.6%**	**$ 5,733**	**3.9%**	**$ 11,253**
Health Transformation Initiatives In Progress (HB 153)								
ICDS		$ -		$ 182		$ 110		$ 292
Health Homes		$ (3)		$ (17)		$ 10		$ (7)
ABD Kids MCP Expansion		$ -		$ 32		$ 15		$ 47
Balancing Incentive Program		$ -		$ (60)		$ (60)		$ (120)
Subtotal		**$ (3)**		**$ 136**		**$ 76**		**$ 212**
ACA Mandates								
Woodwork		$ -		$ 186		$ 335		$ 521
Physician Fee Increase		$ -		$ -		$ -		$ -
Subtotal		**$ -**		**$ 186**		**$ 335**		**$ 521**
Baseline Total	**$ 4,936**	**$ 5,079**	**2.9%**	**$ 5,842**	**15.0%**	**$ 6,144**	**5.2%**	**$ 11,986**
Savings & Cost Avoidance								
Health plan changes				$ (100)		$ (139)		$ (239)
Hospital changes				$ (60)		$ (125)		$ (185)
Nursing Facility changes				$ 6		$ 8		$ 13
HCBS changes				$ 2		$ 10		$ 11
Fight Fraud and Abuse				$ (12)		$ (15)		$ (28)
Other Provider Changes				$ (26)		$ (35)		$ (61)
Subtotal				**$ (191)**		**$ (296)**		**$ (487)**
Baseline Less Savings & Cost Avoidance		**$ 5,079**	**2.9%**	**$ 5,652**	**11.3%**	**$ 5,847**	**3.5%**	**$ 11,499**
Simplify Eligibility/ACA								
Eligibility Changes				$ (23)		$ (68)		$ (91)
Newly Eligible Enrollment (Pre Rebate)				$ -		$ -		$ -
Newly Eligible Enrollment (Net)				**$ (23)**		**$ (68)**		**$ (91)**
Executive Budget	**$ 4,936**	**$ 5,079**	**2.9%**	**$ 5,629**	**10.8%**	**$ 5,779**	**2.7%**	**$ 11,408**

[1] *Note: Amounts adjusted from $4.8B in SFY12 and $5.0B in SFY13 to include the budget for Medicare Part D*

Transformation Priorities

The Executive Budget includes an aggressive package of Medicaid reforms developed by the Governor's Office of Health Transformation. It aligns policy and funding priorities across all Medicaid-related agencies to:

(1) Simplify and automate eligibility determination;
(2) Pay providers based on the value, not volume, of the services they deliver;
(3) Enable seniors and people with disabilities to live with dignity in the settings they prefer; and
(4) Share services across government jurisdictions to create operational efficiencies and improve outcomes.

These priorities leverage Medicaid to act on opportunities to keep people as healthy as possible instead of reacting only after they get sick, prevent chronic disease whenever possible and, when it occurs, coordinate care to improve quality of life for individuals and reduce costs. These changes create win-win opportunities for Medicaid enrollees (better care) and Ohio taxpayers (cost savings through improvement).

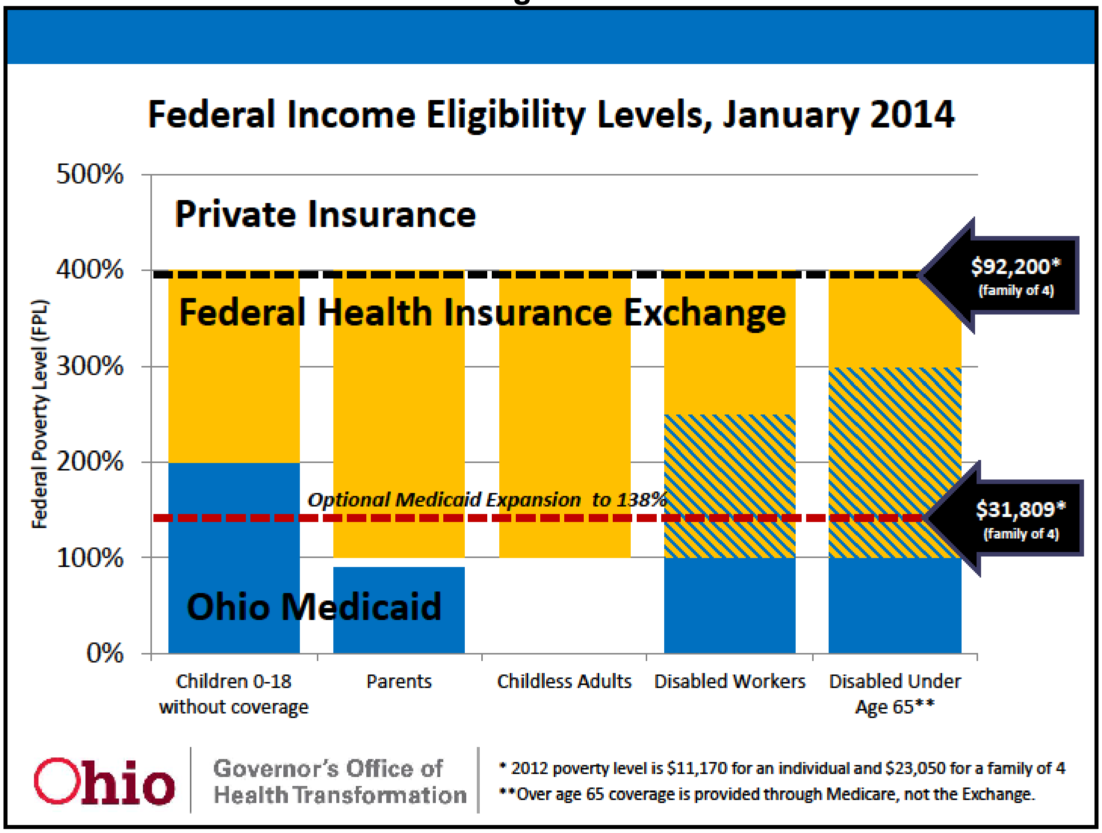
Simplify and Automate Eligibility Determination

Eligibility determination for health and human services programs in Ohio is fragmented, overly complex and relies on outdated technology. For example, Ohio has more than 150 categories of eligibility just for Medicaid. Variation in Medicaid income eligibility creates gaps in coverage that result in unnecessary costs for local government, uncompensated costs for hospitals and cost-shifting to private sector insurance premiums, all of which are paid for by taxpayers and businesses. Eligibility reforms in the budget have the potential to significantly improve care for vulnerable Ohioans, increase program efficiencies and reduce costs for Ohio's taxpayers.

Current Medicaid Eligibility Policies Leave Gaps in Coverage. Approximately 1.5 million Ohioans do not have health insurance, most of them from working families, some of them very poor. Medicaid plays a critical role in protecting the health of low-income Ohioans, but it leaves out many people. Like many states, Ohio does not extend Medicaid coverage to adults unless they have children or are disabled. Beginning in January 2014, the federal government will establish a Health Insurance Exchange to offer tax credits for insurance premiums to Ohioans with incomes between 100 percent and 400 percent of the federal poverty level (FPL),[7] but no credits will be provided below 100 percent FPL. As a result, parents between 90 percent and 100 percent FPL and childless adults with income below 100 percent FPL will be caught in a "coverage gap" without access to Medicaid or tax credits on the Exchange (Figure 4).

[7] In 2012, the federal poverty level was $11,170 for an individual and $23,050 for a family of four.

Figure 4.



Federal Funding is Available to Eliminate the Coverage Gap. In June 2012, a U.S. Supreme Court ruling gave states the option to increase Medicaid eligibility for all adults to 138 percent FPL,[8] with the federal government paying 100 percent of the costs for the newly eligible population during the first three years, decreasing to 90 percent by 2020. States have the flexibility regarding whether and when to extend coverage, although the years of federal funding are fixed.[9] In December, the federal government clarified that enhanced federal funding is not available for a partial Medicaid expansion.

Federal Funding also is Available to Simplify and Automate Eligibility Systems. In August 2011, the federal government announced a time-limited opportunity for states to use enhanced (90 percent) federal matching funds to integrate eligibility determination functions across programs based on income eligibility. The new policy allows health and human services programs—including Temporary Assistance for Needy Families, Supplemental Nutrition Assistance Program and Child Care and Development Fund—to utilize systems designed for determining a person's Medicaid eligibility

[8] The Affordable Care Act requires eligibility for adults to be set at 133 percent FPL but also establishes a 5 percent income disregard, which as a result sets the effective eligibility level up to 138 percent FPL.
[9] The federal medical assistance percentage (FMAP) for the expansion is fixed at 100 percent in 2014, 2015 and 2016, and then decreases to 95 percent in 2015, 94 in 2018, 93 in 2019, and 90 percent in 2020 and beyond.

without sharing in the common system development costs, so long as those costs would have been incurred to develop systems for Medicaid. States may access the 90 percent enhanced federal funding up to but not after December 31, 2015.

<u>This Budget Takes the Next Step to Modernize Eligibility.</u> Governor Kasich's first budget (HB 153) directed Ohio Medicaid "to reduce the complexity of the eligibility determination processes for the Medicaid program caused by different income and resource standards for the numerous Medicaid eligibility categories." The current budget includes a comprehensive package of reforms to simplify eligibility based on income, streamline state and local responsibility for eligibility determination and update eligibility systems technology. The goal is for enrollees to become eligible for Medicaid and other programs based on income tax information without needing to undergo any additional eligibility tests. The two major features of the plan are to simplify eligibility policy and to automate eligibility determination systems.

- ***Consolidate Medicaid eligibility into three basic groups.*** As a first step, Ohio will map the state's current 150+ Medicaid eligibility categories into three groups: (1) children and pregnant women, (2) individuals who are age 65 or older, who have Medicare coverage, or who need long-term services and supports, and (3) community adults (non-pregnant adults who do not need long-term services and supports), including individuals eligible as parents or caretaker relatives. The eligibility criteria and standards for the first two simplified groups will not change (income, resources, spend-down, disability determination, and other creditable coverage will be treated the same). Only the third group, community adults, will see significant changes in eligibility standards for Medicaid. All three groups will benefit from simplified processes, including for most applicants conversion to a new federally mandated modified adjusted gross income (MAGI) standard that will allow for real-time eligibility determination.

- ***Extend Medicaid coverage to more adults.*** Beginning January 1, 2014, community adult applicants will qualify for Medicaid with MAGI at or below 138 percent FPL. There will be no application of spend-down processes, no resource test, and no state or federal disability determination requirement, although there will be other qualifying criteria such as legal residency. The new policy is expected to impact the following populations:

    - **Newly eligible.** Community adults with MAGI below 138 percent FPL, including parents with MAGI between 90 percent and 138 percent FPL, will be newly eligible to enroll in Medicaid. Ohio Medicaid estimates 366,000 individuals will enroll, including 270,000 previously uninsured Ohioans (Figure 5). The total cost of services for this group is estimated to be $2.6 billion over the biennium, all of which will be paid by the federal government. In some cases, state and local government will see savings result when Ohioans who are covered by other programs move onto Medicaid. For example, the Ohio Department of Rehabilitation and Correction estimates it will save $27 million over the biennium on inpatient hospital costs for prisoners, and the county community mental health and addiction services system is expected to save $105 million over the biennium on services that shift to Medicaid.

    - **Currently eligible but not enrolled.** Some people who are currently eligible but not yet enrolled in Medicaid are expected to enroll in January 2014, regardless of whether eligibility expands. This "woodwork effect" results from the new federal requirement to have health insurance, easier access to insurance through the federal Health Insurance Exchange and increased awareness about the availability of health coverage. Ohio Medicaid estimates an additional 92,000 children, 88,000 parents and 51,000 seniors will enroll in Medicaid as a result of the woodwork effect. Ohio will receive the regular federal match rate for this population, resulting in higher state Medicaid costs. Ohio Medicaid estimates the cost of these individuals will be $1.5 billion ($521 million state share) over the biennium. The woodwork effect is not included in the estimated cost of eligibility simplification and automation because it is expected to occur with or without changes in Medicaid income eligibility policy.

- **Previously eligible.** Some community adults qualify for Medicaid today at income levels above 138 percent FPL as a result of income disregards, transitional medical assistance, and other exceptions. Ohio Medicaid estimates that 90,863 individuals who would have qualified for Medicaid under current policies will not under the new MAGI policy (Figure 5). However, these individuals will have access to tax credits on the Health Insurance Exchange, up to 400 percent FPL. Ohio Medicaid estimates the savings from not covering this group on Medicaid will be $246 million over the biennium, and because the state would have paid the regular match for this population, the state will save $91 million over the biennium (Figure 6).

Figure 5.
Estimated Medicaid Enrollment from Eligibility Simplification

Newly Eligible Population	Estimated Gain/(Loss) as of June 2015
Previously uninsured	270,097
Previously had other insurance	95,519
Subtotal new enrollment	***365,616***
Previously had Medicaid	(90,863)
Total change in enrollment	**274,753**

Eligibility simplification will result in some Ohioans becoming newly eligible for Medicaid, and some who would have been eligible under the old rules not being eligible in the future (Figure 5). The federal, state and local financial impact of these changes is summarized in Figure 6.

Figure 6.
Estimated Financial Impact Resulting from Eligibility Simplification

Source of Funds	SFY14-15 Costs/(Savings)
Federal	
Newly eligible enrollment cost	$2.6 billion
Previously eligible enrollment savings	$155 million
Total	$2.4 billion
State	
Newly eligible enrollment cost	$0
Previously eligible enrollment savings	($91 million)
State inpatient hospital for prisoners	($27 million)
HIC and sales tax revenue (net)	($117 million)
Total	($235 million)
County	
Service costs that shift to Medicaid	($105 million)
Sales tax revenue (net)	($25 million)
Total	($130 million)

- ***Require personal responsibility from Ohioans who benefit from Medicaid.*** In order to ensure individuals in the Medicaid program take personal responsibility for their health care services and also become ready to move off of Medicaid and into private insurance, Medicaid is proposing new cost sharing requirements for every adult above 100 percent of poverty, consistent with proposed federal regulations on cost sharing. Ohio will require an $8 co-payment for use of an emergency room for non-emergency conditions, $8 co-pays for non-preferred drugs and $3 co-pays for preferred drugs. Certain long-term maintenance drugs (such as insulin) will have no co-pay. Under the new federal rule, a provider can deny a service if the person does not pay the co-pay. For example, a pharmacist could deny the person the non-preferred drug for not paying the $8 co-pay but offer the preferred drug at the $3 co-pay.

- ***Opt out if federal funding is reduced.*** The federal government has made it clear that states may opt in and out of covering newly eligible populations at any time. The Executive Budget codifies an automatic opt-out trigger so that if for any reason the federal government reduces its financial participation for expanded coverage, then the program for newly eligible populations shuts down and Ohio taxpayers are not stuck with the bill.

<u>This Budget Updates Eligibility Systems and Processes.</u>

- ***Replace Ohio's 34-year-old eligibility determination system.*** Ohio's Enhanced Client Registry Information System (CRIS-E) provides intake and eligibility determination support for several of Ohio's health and human services programs, and provides some case management functions for several Ohio Department of Job and Family Services programs. When CRIS-E was implemented in 1978, it was able to meet the needs of the counties by allowing for 18,000 users to manually enter cases for Ohio citizens. As time went by, many processes were added to allow the original application to do more, but all of the additions were built on the original foundation, which could only extend so far and long ago reached its limit of new applications. The problem is so severe that Ohio Medicaid estimates more than 60 percent of cases are manually adjusted to ensure that system insufficiencies do not result in erroneous eligibility denials. Rather than building more on an aging foundation, a new foundation needs to be laid down that will adapt to the changing needs of Ohio's programs and citizens.

  The Ohio Department of Administrative Services is contracting with a vendor to replace CRIS-E with an integrated, enterprise solution that supports both state and county operations. The new system will provide the technology necessary for integrated eligibility and business intelligence across all of Ohio's health and human services agencies. The project will focus first on Medicaid eligibility (including MAGI standards and processes for newly eligible populations), then expand to other programs that depend on CRIS-E (this phase will retire CRIS-E), and finally expand to support all health and human services programs, even those not currently supported by CRIS-E. The new system will give individuals and families an option to apply online, without the need to report to a local office, and provide real-time determination for most people who apply. The Executive Budget includes $230 million for this project, with the state paying only $26 million of this total because of enhanced federal match.

<u>Reset Payment Rules to Reward Value Instead of Volume</u>

Eliminate Fraud and Abuse

Fraud accounts for approximately 10 percent of all health-care waste, so fighting fraud and maximizing accountability in Medicaid is a key to improving efficiency. Ohio will expand its efforts to improve program integrity through a series of reforms, saving $74 million over the biennium.

<u>Increase Medicaid's Audit Capacity.</u> Medicaid will develop additional program integrity capacity, allowing more on-site monitoring of Medicaid providers and increasing the amount of Medicaid overpayments that are recouped to the state.

<u>Speed Nursing Home Claims Processing and Terminations.</u> Ohio will implement a new claims review process to resolve overpayment issues more efficiently for nursing homes and the state, and new authority will improve quality of care by enhancing the state's ability to terminate homes with a history of poor quality.

Validate Providers. The budget will authorize Medicaid to revalidate providers more frequently, creating more accurate information on providers, consistent with federal law.

Capture Reimbursements from Consumers. The budget will enable Medicaid to improve collection of payments if a Medicaid beneficiary has a trust and recover payments when an individual has other insurance coverage, providing relief for taxpayers.

Reduce Prescription Abuse. The budget clarifies that Ohio Medicaid "shall" (not "may") have access to the Ohio Automated Rx Reporting System (OARRS) and specifies that Medicaid is able to see information about prescriptions that were not paid for through Medicaid. This access will allow Medicaid to confirm that if a consumer is assigned to a specific provider through the coordinated services program to curtail prescription drug abuse, the provider is not allowing the recipient to receive controlled substances outside the Medicaid program.

Reform Provider Payments

Reform Health Plan Payments. Managed care plans oversee the benefits for approximately three of every four Medicaid beneficiaries. This public-private partnership between the state and Ohio health plans improves care coordination for beneficiaries and grows Ohio jobs in the private sector. To continue to drive quality improvement, Ohio Medicaid will double the amount of managed care payments that are tied to meeting quality measures, and it will implement a performance-based payment structure for plans in the new ICDS. The budget also proposes to adjust the rate paid by the state to managed care plans by reducing the administrative component of the rate, reducing the prescription drug component of the rate and capping the overall growth in capitation rates. Given the maturity in Ohio's Medicaid market and recent reforms that will make the Medicaid managed care program more efficient, plans will be able to adjust to these changes through efficiencies and without impacting client services.

Reform Hospital Payments. The Executive Budget includes several provisions that impact hospitals. It reauthorizes temporary assessment programs and supplemental payment programs that would otherwise expire, makes several significant changes in hospital payment policy, and expands Medicaid eligibility to adults with income below 138 percent of the federal poverty level, many of whom might otherwise be a source of uncompensated care for hospitals.

- ***Continue hospital assessment programs.*** The current budget is supported by health care-related provider fees that generate matching funds for Medicaid program spending. The Executive Budget reauthorizes the hospital franchise permit fee program, which otherwise would sunset June 30, 2013. The budget incorporates the franchise fee allocation methodology developed by the Ohio Hospital Association, which collects $524 million in annual fees that are used to draw federal funds and make payments back to hospitals totaling $840 million. The budget also reauthorizes the Ohio Hospital Care Assurance Program (HCAP), which provides additional payments to hospitals that provide care to a disproportionate share of indigent patients. The budget reauthorizes HCAP until October 2015, which will result in hospitals receiving approximately (depending on federal allotments) $1.1 billion in DSH payments over the biennium, $726 million net of HCAP assessments. (Note: The federal Affordable Care Act will reduce HCAP reimbursements beginning in 2014.)

- ***Improve hospital payment strategies.*** The Executive Budget makes the following changes in hospital payments, which will create incentives for hospitals to improve quality, reduce waste and improve efficiencies. These changes reduce overall hospital spending 3.8 percent in FY 2014 and 7.4 percent in FY 2015.

  - ***Create a children's' hospital quality improvement program.*** The Executive Budget redirects the temporary special children's hospital funding that was authorized in the last budget (line item 600-537) to financially support delivery system changes that improve outcomes for children enrolled in Medicaid.

  - ***Reduce hospital re-admissions.*** The Executive Budget will limit Medicaid payments to hospitals for re-admissions within 30 days by establishing percentage-based benchmarks for readmission reductions. If hospitals meet the benchmark each year, re-admissions will be reduced by 44 percent in total and result in substantially fewer program payments for re-admissions.

  - ***Eliminate the five-percent rate add-on for inpatient and outpatient services.*** The Executive Budget will allow the temporary five percent rate increase for hospitals authorized in the last budget to expire on December 31, 2013. Ohio currently uses franchise fee proceeds to fund the rate add-on.

  - ***Improve direct medical education.*** The Executive Budget does not change the current level of Medicaid direct graduate medical education funding – about $200 million over the biennium – but it does propose to target those funds to support health sector workforce priorities related to primary care and recruiting minorities into health professions.

  - ***Reduce the rate taxpayers pay for hospital capital projects.*** The budget will reduce inpatient capital rates from 100 percent of cost to 85 percent of cost for both fee-for-service and Medicaid managed care plans.

  - ***Adjust DRG-exempt hospital rates.*** The Executive Budget will align Medicaid reimbursement for DRG-exempt hospitals with other inpatient hospital services that are subject to the DRG system.

  - ***Control cost of outpatient services.*** The Executive Budget will set fixed prices for all outpatient services currently reimbursed at cost. Reimbursement for independently billed drugs and medical supplies will be set at 60 percent of costs, and the hospital laboratory fee schedule will be recalibrated to align payment rates to prescribed Medicare ceilings.

- ***Impact of federal changes.*** Expanded Medicaid coverage will convert some otherwise uncompensated care into Medicaid payments. Ohio Medicaid estimates that, as a result of increased enrollment from more currently eligible individuals coming onto the program (woodwork) and Ohio's decision to extend Medicaid coverage to adults with income below 138 percent of poverty, hospitals will receive an additional $1.6 billion in Medicaid payments over the biennium.

Taking into account the net impact of the franchise fee, payment reforms, and new revenue from woodwork and Medicaid expansion populations, overall Medicaid hospital spending increases 15 percent in FY 2014 and 28 percent in FY 2015.

Reform Nursing Home Payments. HB 153 increased the quality incentive payment for nursing homes from 1.7 percent of the rate to 9.7 percent and replaced business-focused quality measures with new measures that are directly tied to residents' needs. The Governor's budget continues efforts begun in the last budget to link funding to quality, and it invests an additional $35 million in nursing homes over the biennium.

- ***Maintain the current rate structure.*** The budget keeps the current price-based rate structure for nursing homes and continues flat rate pricing for low-acuity individuals.

- ***Modify peer groups.*** Ohio will shift facilities in Stark and Mahoning Counties into a more appropriate peer group, better aligning provider rates in those counties with the business environment and costs impacting their operations.

- ***Revise quality measures.*** The budget will upgrade the measures tied to the quality incentive rate component, based on recommendations of a legislative commission. The revised measures, which will require facilities to earn at least one clinical quality point to qualify for the maximum quality incentive, reflect a strategy of continuous improvement.

- ***Provide additional funding for critical access facilities.*** The Executive Budget gives a five percent rate boost to critical access facilities, recognizing the critical role these facilities play in their communities and their heavy reliance on Medicaid as a payer.

- ***Remove custom wheelchairs from the nursing facility rate.*** The Executive Budget defines custom wheelchairs and removes custom wheelchairs from the calculation of the nursing facility per diem. The budget also gives Medicaid the authority to use alternative purchasing models for custom wheelchairs, including selective contracting, competitive bidding or a manufacturer's rebate program, ensuring that individuals in nursing facilities have access to medically necessary custom wheelchairs while giving Medicaid the tools to effectively manage utilization and expenditures.

Reform Payments to Other Non-Institutional Providers.

- ***Limit Medicare Part B crossover payments.*** Ohio will reimburse only up to the Medicaid maximum, rather than the full Medicare share, for Medicare crossover claims for individuals who are dually enrolled in both Medicare and Medicaid.

- ***Increase electronic prescribing.*** The state will enhance the use of e-prescribing, enabling prescribers to better access Medicaid eligibility and drug prescribing policies, eliminating delays in patient therapy and reducing costs.

- ***Reduce payments for unnecessary image procedures.*** Ohio will reduce payments for multiple MRIs and other images, eliminating wasteful scans and tests for patients and taxpayers.

- ***Consider service location in pricing.*** Consistent with Medicare reimbursement policy, Medicaid will adjust payments to certain providers for services that are delivered outside of their normal practice site. In these instances, the provider should be reimbursed at a lower rate because Medicaid is separately paying a fee to the facility where the service is performed.

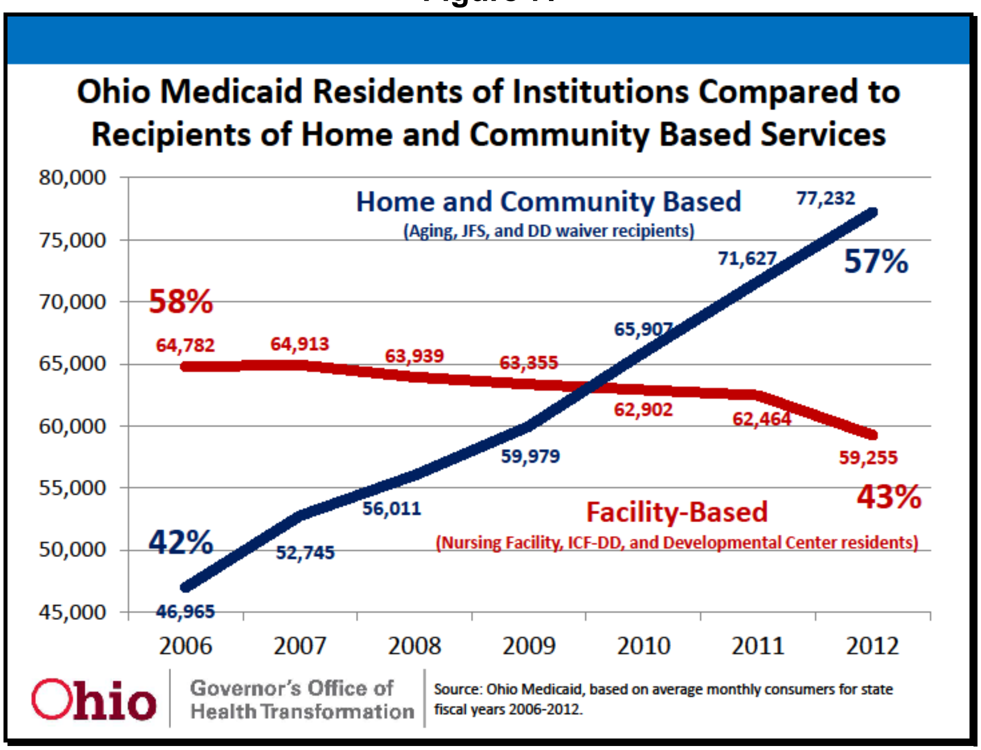
- ***Close payment loopholes.*** The budget eliminates an outdated, enhanced reimbursement rate that was implemented more than 20 years ago to launch a single clinic in an under-served area of the state.

Enable Seniors and People with Disabilities to Live in Settings they Prefer

Prioritize Home- and Community-Based Services

Governor Kasich's first budget increased spending on home- and community-based services for seniors and people with disabilities $200 million over two years. As a result, an additional 7,600 Ohioans will receive Medicaid long-term care in their own home or community setting. This accelerates a trend that, over the past six years, reversed the proportion of residents in institutions compared to recipients of home and community based services—from 58 percent institutional in 2006 to 57 percent home- and community-based in 2012 (Figure 7).

Figure 7.



The Executive Budget increases Medicaid payments related to home- and community-based long-term services and supports (LTSS) by $30.8 million ($11.4 million state share) over the biennium. It also aligns other related initiatives to ensure Ohioans have access to LTSS in the settings they prefer, and to provide better care while also reducing costs.

Increase Rates for Aide and Nursing Services. The Executive Budget increases aggregate spending for Medicaid aide and nursing services three percent in SFY 2015. The increase will take into account labor market data, education and licensure status of providers, whether providers are independent or home health agencies and the length of time of service visits. As part of the rate design, Ohio Medicaid will create incentives to improve the quality of clinical care by paying in a way that better assures appropriate involvement of registered nurses when licensed practical nurses are providing care.

Increase Rates for Adult Day Care. In the continuum of long-term services and supports, adult day services (ADS) and assisted living serve a critical function for individuals who choose not to receive care in a nursing facility. The demand for these programs is increasing but, absent a rate increase, the supply of providers is likely to decrease, particularly in ADS. The Executive Budget increases ADS rates 20 percent in the Ohio Department of Aging's PASSPORT and Choices programs to mirror the current rate for ADS in Medicaid's Home Care Waiver ($49.47 for an enhanced full day and $64.94 for an intensive full day). The budget increases assisted living rates three percent (to $49.93 for the first tier, $59.95 for the second tier and $69.96 for the third tier). The budget also requires Ohio Medicaid and the Ohio Department of Aging to study and potentially overhaul the assisted living reimbursement structure.

Make Changes in Patient Liability. Nursing facility residents are required to contribute to their nursing facility costs, but they may retain an amount of their personal funds for items not covered by Medicaid, such as clothing, personal items and newspapers. The current needs allowance, $40 per month, has not been increased or adjusted since 1997. The Executive Budget increases the personal needs allowance to $45 per month in calendar year 2014 and $50 per month in calendar year 2015.

Limit the Daily Rate for a Caregiver Living with a Consumer. It is not uncommon for a provider in a home- or community-based setting to be a consumer's relative or live-in friend. Operational and administrative expenses for a provider living with a consumer are lower than other providers of similar services, so the budget establishes a unique daily rate for a caregiver living with a consumer.

Implement a Shared Savings Initiative for Home Health. In late 2010, the Ohio Council for Home Care and Hospice began a campaign to reduce avoidable hospitalizations, and participating agencies demonstrated they were able to reduce hospitalizations. Ohio Medicaid estimates that as much as 12 percent of the cost of hospital care provided to certain recipients of home- and community-based services and other Medicaid home health benefits may be avoidable. Based on this evidence, the Executive Budget authorizes Ohio Medicaid to implement a quality incentive program to reduce the number of avoidable admissions to hospitals or nursing facilities for individuals receiving home- and community-based waiver services and other Medicaid home health benefits. Half of the savings from this incentive program will be returned to participating providers.

Commit to the Balancing Incentive Payment Program (BIPP). Federal law allows Ohio to earn approximately $70 million per year in additional federal funds through the BIPP program if it implements specific program improvements to help seniors and people with disabilities access home-and community-based services and improve their quality of life. The budget provides Ohio the tools it needs to improve care for these vulnerable individuals and generate substantial new revenue for home-based services.

Update Provider Regulations to be More Person-Centered and Ensure Safety. The budget continues to drive quality improvements in services that are administered in the community and in institutional settings.

- ***Ensure safety in home care.*** The Governor's Mid Biennium Review legislation greatly enhanced protocols for background checks and disqualifying criminal convictions for workers who provide services in patients' homes, but Ohio still lacks a standard program to train, test or certify home- and community-based direct-care workers. The budget will ensure that direct-care workers meet core competency standards, providing extra safety for thousands of Ohioans who receive health care service in their homes.

- ***Improve nursing home monitoring.*** The budget will enhance quality in nursing homes by: (1) improving the process for administering and responding to plans of correction in response to survey deficiencies, (2) creating consistent standards for specialized units in the Long-Term Care Consumer Guide and (3) making the licensure process and standards more focused on the needs of residents.

Provide Post-Acute Care in the Most Appropriate Setting. Ohio will change Medicaid policy and modify payment incentives to rebalance the service delivery options for individuals in need of post-acute rehabilitation. By providing more post-acute services in skilled nursing homes, instead of more expensive rehab hospitals and long-term acute care hospitals, Ohio will provide targeted care in a more appropriate environment, saving taxpayers approximately $500 per patient day at full implementation.

Rebuild Community Behavioral Health System Capacity

When Governor Kasich took office, Ohio's publicly funded system of mental health and addiction services was in turmoil. Significant cuts in state support for mental health and addiction services, paired with increased demand for services in a period of dramatic economic recession, significantly limited access to care for individuals in need of treatment. Governor Kasich's first budget increased state funding for mental health by 5.7 percent ($26.8 million) over two years, reversing a downward trend since 2008 in which state funding was reduced nearly 20 percent ($112.4 million). This allowed the state to hold all-funds spending for mental health close to 2011 levels, which were inflated that year with $32.6 million in one-time federal stimulus funds. Other changes Ohio has made—such as freeing local systems from Medicaid match responsibility, creating Medicaid medical homes for people with severe mental illness, making mid-biennium investments to address mental health "hot spots" and consolidating functions of the Departments of Mental Health and Alcohol and Drug Addiction Services—helped to further stabilize Ohio's behavioral health funding and services structure.

This budget includes the most significant changes in community mental health and addiction services in decades. After years of erosion, it represents a genuine opportunity to restore prevention, early intervention and treatment capacity, as well as to sustain those objectives with a stronger foundation for the future. The result has been a paradigm shift for Ohio's behavioral health system that will enable greater integration with physical health care and transition to an outcome based, person-centered focus.

Expand Medicaid and Redirect Existing Resources to Address Recovery Support Gaps*.* Governor Kasich's decision to expand Medicaid will have a direct benefit on Ohio's behavioral health system. Most uninsured Ohioans who receive services from county boards of mental health and addiction services will become eligible for Medicaid under the expansion. Once these newly eligible Ohioans are enrolled, Medicaid coverage for clinical services[10] will annually free up an estimated $70 million statewide in county levy or subsidy dollars from the state, allowing counties to spend these funds on other recovery-oriented priorities such as housing and employment supports. Currently, most Ohio communities do not have sufficient resources to meet these basic needs, which are not part of the Medicaid benefit. By expanding Medicaid, local communities will, over time, be able to redirect existing state subsidy and local resources (as available) to fill gaps in the local service continuum, reduce waiting lists, place a greater emphasis on wellness and prevention, and improve overall health outcomes within the community.

Make Additional Targeted Investments in Community Mental Health. The budget will formally complete the consolidation of mental health and addiction services. The new state department will promote a combined system of care that is centered on the best outcomes for the individual who needs care. The consolidation of ODADAS and ODMH is anticipated to save Ohio taxpayers $1.5 million annually, all of which is being redirected to a new Community Innovations Program. The new Ohio Department of Mental Health and Addiction Services (ODMHAS) will use these resources to invest in targeted demonstrations that promote collaboration between partners and result in savings for other parts of government.

Assist Nursing Home Residents Who Want to Move Back into the Community. Currently, Ohio Medicaid spends $102,500 per year (on average) for Medicaid services in a nursing home for an individual under age 60 who is physically healthy but has a diagnosis related to severe and persistent mental illness. Many of these individuals could be served in less restrictive, clinically appropriate settings at lower taxpayer expense. A series of initiatives in the budget—called *Recovery Requires Community*—transitions funds to community-based services, achieving significant long-term savings and allowing more people to move out of nursing homes and into the settings they prefer. The initiatives in this budget will: (1) allow money to follow the person from a nursing home into the community; (2) increase access to safe and affordable housing; (3) improve care coordination in adult care facilities; and (4) reduce inappropriate admissions into nursing homes.

Enhance Community Developmental Disabilities Services

Governor Kasich's first budget continued the developmental disability system transformation that began in 2001, providing tools that allow people with disabilities to move seamlessly from one setting of care to another. Despite significant progress, challenges remain. For example, despite individuals'

[10] Clinical services included within Ohio's community Medicaid behavioral health benefit include assessment, individual/group counseling, ambulatory detoxification, crisis intervention, intensive outpatient, partial hospitalization, pharmacologic management, laboratory urinalysis and several other services.

preferences for home-based care, Ohio has more people living in large private institutional facilities than any state in the nation, and Ohio ranks seventh in the number of public intermediate care facilities. The Executive Budget promotes further downsizing of large institutions, the conversion of institutional beds to home and community based waiver settings, an emphasis on supported employment and an increase in autism services.

Set a Flat Rate for Residents of Institutions who are Less Profoundly Disabled. The Executive Budget authorizes Ohio Medicaid to pay a flat rate for all individuals residing in an intermediate care facility for individuals with intellectual disabilities (ICF/IID) who are less profoundly disabled than other residents. By prescribing a flat rate to be paid for the least resource-intensive individuals, this provision allows funds to flow to those most in need and encourages facilities to actively consider the opportunity for those individuals with less profound needs to receive home- and community-based services instead of receiving services in an institution.

Provide a Financial Incentive to Convert Institutional Beds into HCBS Waiver Services. The Executive Budget authorizes the Department of Developmental Disabilities (DODD) to create a payment incentive for ICF/IDDs to downsize or convert to smaller facilities. It also allows DODD to redirect savings that result from an institutional downsizing or conversions to additional home- and community-based services. This change reflects the goal of improving the quality of service while connecting resources to the appropriate level of need.

Increase Rates for Providers Serving Former Residents of Institutions. The Executive Budget permanently extends a temporary $2.08 per hour rate increase that was enacted in the Mid-Biennium Review legislation for home- and community-based waiver providers if the individual they are serving was a resident of a public hospital, developmental center or converted ICF/IID facility immediately prior to enrollment in the waiver. This change extends the financial incentive to provide individualized service packages as an alternative to institutions.

Support Employment First. The Executive Budget authorizes additional strategies to eliminate barriers to employment. It improves data collection, makes permanent the Governor's Employment First Taskforce, and creates a presumption that all individuals with developmental disabilities can work unless determined otherwise. The budget also encourages local county boards to create Employment First policies and creates a new Employment First line item in DODD to fund these efforts.

Increase Access to Autism Services. Building on the Governor's commitment to improving care for individuals with autism, the Executive Budget includes $100,000 for the Ohio Center for Autism and Low Incidence (OCALI) to continue providing technical assistance to the Interagency Workgroup on Autism (IWGA). This will continue to encourage state agencies and other partners to work together to coordinate autism services throughout the lifespan of an individual.

Share Services and Streamline Programs

Create a Medicaid Department

The Executive Budget establishes Medicaid as a cabinet-level department effective July 1, 2013. This decision is consistent with previous Medicaid reviews and recent actions taken by the Kasich Administration, described above. The effective date is one year earlier than originally planned because the work to separate Medicaid functions from ODJFS has gone so well that both agencies agreed to pull forward the effective date.

The creation of a cabinet-level Medicaid agency will bring about many changes, but it is not intended to reduce the workforce or reduce Medicaid-related financial resources that are available to counties. The purpose behind creating a new department is to release the creative potential of the state's Medicaid team to push forward reforms already underway, and to position the program within state government commensurate with Medicaid's responsibility to improve overall health system performance, improve care for vulnerable Ohioans, and control costs for Ohio's taxpayers.

Combine the Departments of Mental Health and Addiction Services

Forty-seven of 53 county board systems administer both mental health and alcohol and drug addiction services. Many providers are certified for both types of services and a significant percentage of consumers interact with providers in both systems. However, at the state level these services are administered through two separate state agencies. The budget bill will formally consolidate ODADAS and ODMH into the Department of Mental Health and Addiction Services, providing additional efficiencies and improving support for local government partners, providers and clients who are participating in two treatment systems.

Implement Public Health Futures

The Mid-Biennium Review legislation established a committee of stakeholders and legislators to examine current local public health capacity, services and jurisdictional structure and assess opportunities for improvement. The budget operationalizes the recommendations of the Public Health Futures Committee, providing the following tools for shared services and operational efficiencies in local public health.

- ***Regionalize grant administration.*** Beginning in July 2013, ODH will release a request for proposals to regionalize several targeted grants. These regional RFPs will be awarded in January 2014 and consolidate 180 separate grants into 47 regional awards. Later phases of implementation will involve working with federal partners to "block grant" these programs.

- ***Require continuing education for board of health members.*** The budget requires each member of a board of health to complete eight continuing education units annually. The Budget also requires each Board of Health to include an executive officer or medical director of a hospital or the largest medical facility in the district, to facilitate community health planning.

- ***Require public health accreditation.*** The Executive Budget authorizes the ODH director to require general or city health districts to be accredited beginning in 2018 as a condition for receiving funding from ODH. Beginning July 2013, accreditation standards will be incorporated into all regional grant deliverables to assist LHDs build capacity and knowledge of the accreditation process and prepare for successful accreditation.

- ***Require food sanitarians to be certified.*** The budget requires sanitarians of a city or general health district who perform inspections of food service operations or of retail food establishments to obtain and maintain certification from the United States Food and Drug Administration. Local health departments meeting this requirement will receive less frequent surveys from ODH. Later phases of implementation will include similar standards for other mandated programs.

- ***Encourage shared services.*** Beginning in July 2014, ODH will expect local health departments to demonstrate movement toward regional shared service hubs for foundational capabilities such as human resources, payroll processing, information technology, and financial management. This item will be included in the fiscal monitoring activities included in regional grants, and applications that fail to demonstrate movement or contractual relationships with the regional hubs will result in points off in scoring.

- ***Allow shared services among non-contiguous cities or counties.*** Current law limits certain cross-jurisdictional sharing opportunities to "two or more contiguous" health districts "not to exceed five." The Executive Budget includes provisions to remove these restrictions. Also, the budget authorizes permissive multi-county levy authority for public health services.

- ***Require county-level public health planning.*** The Executive Budget requires the health commissioner of a general health district to develop a comprehensive community assessment for the county, in collaboration with city health districts, private health care providers, hospitals, other medical facilities or medical services, behavioral health providers, and members of the general public.

Coordinate Workforce Programs

The Executive Budget includes several initiatives to coordinate health sector workforce programs. These initiatives prioritize advanced primary care and prioritize underrepresented minorities in health professions. They accelerate efforts already underway through the Governor's Office of Workforce Transformation (OWT) and Office of Health Transformation (OHT) to coordinate 16 state agencies to identify health sector workforce needs, align existing workforce programs, reform higher education training programs, and change payments for health services to support workforce priorities.

- ***Provide comprehensive health sector workforce data.*** The Ohio Department of Health (ODH) is leading an initiative to obtain comprehensive state-level health sector workforce data. ODH will work with OWT and OHT to develop an advanced primary care workforce forecasting model to assist in planning for health professions education programs and recruitment and retention strategies.

- ***Define core competencies in the direct care workforce.*** Currently, no standardized certification program exists for direct care workers providing care in the homes and residences of consumers receiving home and community based services reimbursed by Medicaid. The Executive Budget establishes a process to define core competencies for direct care workers across all of Ohio's health and human services agencies.

- ***Target scholarship, training and loan repayment programs to support workforce priorities.*** OWT and OHT will coordinate priorities and resources across existing scholarship and training programs, including Choose Ohio First Scholarships for primary care, Medicaid Technical Assistance and Policy Program Healthcare Access Initiative, and combined Board of Regents line items for family medicine, geriatric medicine, primary care residencies, and the Area Health Education Center program.

- ***Target direct medical education to support workforce priorities.*** The Executive Budget does not change the current level of Medicaid direct graduate medical education funding – about $200 million over the biennium – but it does propose to target those funds to support health sector workforce priorities.

- ***Support training in promising models of care.*** The existing state-funded Patient-Centered Medical Home (PCMH) Education Pilot Project provides technical assistance to convert 50 primary care practices, some in underserved areas, to PCMH status and use those sites for training in advanced primary care. The budget authorizes ODH to adopt standards and procedures for certifying PCMH, eligibility requirements for providers, and uniform health care quality and performance measures.

- ***Primary care rate increase.*** The federal government requires states to raise Medicaid fees at least to Medicare levels for family physicians, internists and pediatricians for many primary care services. In Ohio, primary care physicians will see their Medicaid payments increase 82 percent on January 1, 2013, and receive an estimated $700 million more in Medicaid payments over the two-year period ending December 31, 2014, all of which is federally funded.

- ***Home and community based services rate increase.*** The Executive Budget holds the line on spending for institutional services, but increases payment for home and community based services. The budget increases Medicaid aide and nursing services three percent, increases adult day service rates 20 percent in the Ohio Department of Aging's PASSPORT and Choices programs, and increases assisted living rates three percent.

Conclusion

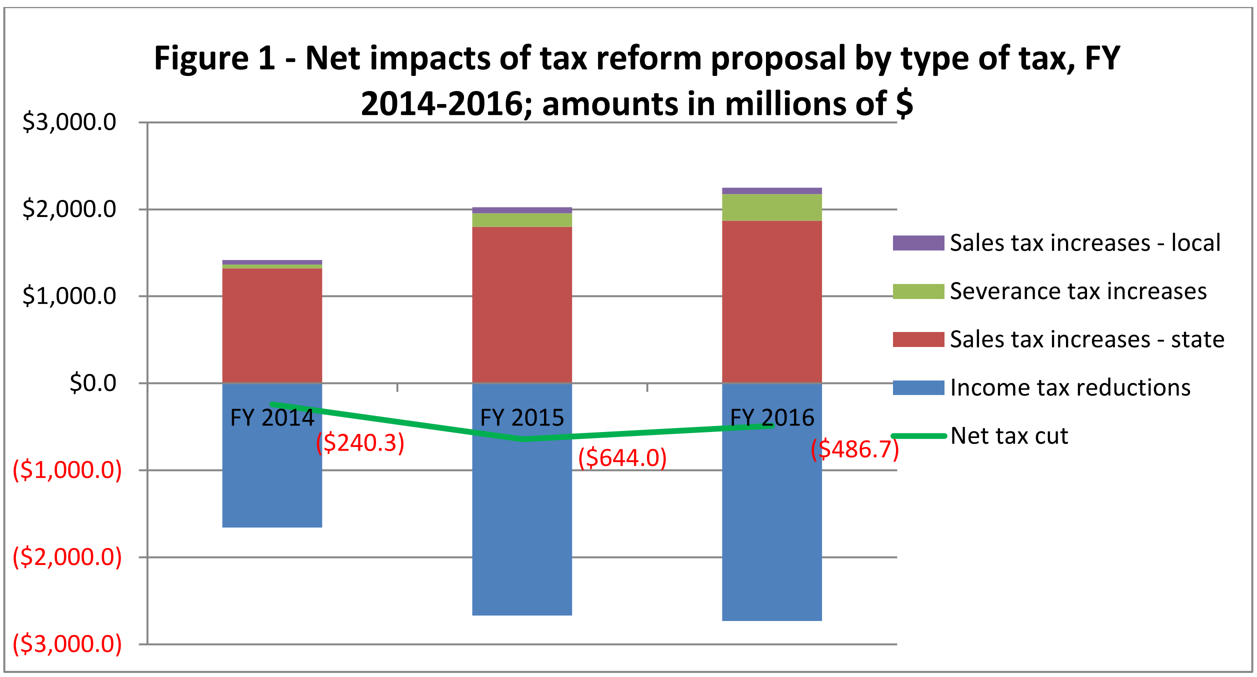
The Governor's Medicaid budget will continue the nationally recognized transformation of Ohio's Medicaid program by improving care for vulnerable Ohioans, reducing costs for taxpayers and businesses and making Ohio more attractive to job creators. The Medicaid budget is challenging but fair. It achieves savings on a scale similar to Governor Kasich's first budget, and it fulfills the state's responsibility to provide health coverage for vulnerable citizens while also working to ensure taxpayers get the best possible value for their money.

Moving from Income Taxes to Sales and Severance Taxes

Tax Reform to Promote Job Growth, Equity, and Efficiency

Governor Kasich is concerned that the current Ohio state and local tax system relies too heavily on the income tax, and contains fundamental inequities in the sales tax. The heavy reliance on the income tax harms Ohio in its competition with other states for jobs and investment. The inequitable structure of the sales tax, where the vast majority of goods are taxed but where only a minority of services are taxed, does not reflect the modern economy where services are almost two thirds of all consumption spending, and it distorts consumption decisions between goods and services. There is evidence, discussed in more detail later, that the narrow sales tax base has had the impact of pushing up sales tax rates on those items that are taxed. Finally, the taxation of most goods but relatively few services may also make the burden of the sales tax fall more heavily on lower income families, who tend to consume more goods than services. The administrations reform proposal would reduce the state income tax in order to improve Ohio's competitive position relative to other states and to improve incentives for work and investment, thus leading to faster economic growth in the future. Broadening the sales tax base by including many services that are currently untaxed, and by increasing severance tax rates on oil, gas, and other hydrocarbons extracted from horizontal wells, still allows for a net tax cut of hundreds of millions of dollars each fiscal year. Finally, Governor Kasich's tax reform proposal would also reduce both the state sales tax rate and local sales tax rates in keeping with the principle that broader based and lower rate taxes are more efficient (less distortive of individual choices) than taxes with narrower bases and higher rates.

The end result of the proposal is to provide a net tax cut to Ohio taxpayers, and to restructure the tax system so that it relies less on income and more on consumption and resource extraction. The shift from taxing income to consumption is expected to have positive impacts on efficiency and growth. The additional tax revenues from oil and gas are expected to be at least partly exported to residents of other states, without adverse impacts on Ohio's economy.



Reducing the State Income Tax – Rate Reduction and Targeted Small Business Relief

Part 1 – Reducing All Income Taxes

In Ohio, it has been recognized for at least a decade that Ohio's high marginal tax rates are a problem for interstate competition for jobs and investment. In response to the report of the 2003 Ohio Committee to Study State and Local Taxes (CSSLT), the 2005 Ohio tax reform/budget bill (HB 66 of the 126th General Assembly) reduced state income tax rates by 21 percent over five years. The Commission report stated that:

"The highest marginal state income tax rate of 7.5%, combined with the average city tax rate of 1.5%, and perhaps combined with the school district income tax in some areas, places Ohio at a competitive disadvantage in attracting high-paying jobs." [11]

Although most of the discussion of negative economic impacts of income taxation is to the federal level, there is some academic work that has been done on negative effects of state-level income taxes. A recent paper from economists at the New Jersey Department of the Treasury finds that New Jersey's so-called "millionaires tax" on high-income households caused outmigration of households to other states. More specifically, the authors estimated the migration impact on a state of having higher income tax rates than other states and then applied those general results to New Jersey. They found that "…average marginal tax rates had a small but significant effect on migration decisions in the U.S. and in New Jersey. We estimate that higher New Jersey income taxes after 2003 were associated with a reduction of more than 20,000 taxpayers…" [12]

Professor Mark Rider of Georgia State University wrote a literature review paper in 2006 where he discussed prior work on the negative economic incentives and effects of state-level income taxes. [13] In that paper he reviews prior studies that show measurable negative economic impacts of high state personal income tax rates. He finds that high personal income tax rates can have negative impacts across a variety of economic variables. Specifically, Rider finds:

"…high state PIT rates have a negative effect on the plant and facilities location decision, foreign direct investment, capital investment, and firm location…high PIT rates discourage entrepreneurs from investing in new capital equipment."

Rider also finds two other published studies that concur with the New Jersey treasury economists that high PIT rates encourage out-migration from a state. Finally, looking specifically at studies that have examined the impact of high income tax rates on small business, Rider finds a study of sole proprietorships that finds that decreasing tax rates on sole proprietors increases the growth of the business and thus the pre-tax income, and he finds a study on small business entry and exit that finds that increasing taxes on small business owners decreases entrepreneurial entry (start-ups) and increases exit (causes start-ups to be closed).

Many more economists produce estimates of federal impacts of income tax rates than state and local impacts – the rates are higher, the impacts are easier to measure, and the data (coming from one source rather than 42 states with broad-based income taxes) is easier to collect. Here, too recent work provides some interesting

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[11] For a brief discussion of the possible disincentives associated with the highest published state income tax rate, see page 39 of Richard Woodbury, "The Struggle for Tax Reform in Maine, 2003-2009," Federal Reserve Bank of Boston, New England Public Policy Center Discussion Paper 9-2, October 2009.

[12] "The Effects of Marginal Tax Rates on Interstate Migration in the U.S. " Andrew Lai, Roger Cohen, and Charles Steindel , New Jersey Department of the Treasury - Office of the Chief Economist/Office of Revenue and Economic Analysis, October 2011.

[13] "The Effect of Personal Income Tax Rates on Individual and Business Decisions – A Review of the Evidence," Mark Rider, Georgia State University International Studies Program, Working Paper 06-15, April 2006.

insight. A paper by Christina Romer and David Romer at the University of California at Berkeley that examined federal income tax rates in the inter-war period concludes that:
"We find no evidence that cuts in marginal rates increased machinery investment or business construction, but suggestive evidence that they increased business formation." [14]

This finding in the Romer and Romer paper is thus consistent with the finding in the Bruce and Gurley paper cited by Rider that reducing income taxes increases small business formation, which logically should have a jobs impact because most job creation is in new businesses.[15]

With regard to where Ohio's income tax rates are relative to other states, the CSSLT report contained a table that showed that in 2002 Ohio's then-top rate of 7.5% was 11th highest among the states, and its combined state and city top rate of 9.0% was tied for third highest.

Since 2002, income tax rates across the country have changed substantially. In a number of states the top rate has increased since 2002 (in a smaller number of states the top rate has decreased). In Ohio the HB 66 tax reform reduced all state marginal rates by 21 percent, so that the top rate is now 5.925% (Ohio's current marginal tax rates for all nine income brackets are shown in the table below). Ohio's top state rate is now 27th among states rather than 11th. However, if one adds a 1.5% city tax rate to the top state tax rate, as the table in the 2003 report did, then Ohio's combined state and local top rate is 14th highest (see Appendix). [16]

One item of note is that, while Ohio's state tax rates alone are 27th highest nationally, its rates are higher than those of three of its neighboring states with whom it competes for jobs and investment, namely Pennsylvania, Indiana, and Michigan.

If one looks at income tax burdens, by measuring income tax collections as a percentage of income, one finds much the same story – Ohio has improved as a result of the HB 66 tax reform, but its state and local collections are still relatively high. For total taxes, Ohio's state-only taxes for 2010 (the most recent year available) as a percentage of income were 31st highest in the nation. However, Ohio's local-only taxes were 13th highest, and as a result, its combined state and local taxes were 18th highest. For income taxes alone, where one may clearly see the outsized influence of the municipal income tax, Ohio's state-only income taxes as a percentage of personal income were 29th highest. Ohio's local income taxes, on the other hand, were either third highest (if one includes Washington, D.C.), or second highest (trailing only Maryland). The high local ranking was enough to push Ohio's combined state and local income tax ranking to 8th highest (see Appendix).

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[14] "The Incentive Effects of Marginal Tax Rates: Evidence from the Interwar Era," Christina D. Romer and David H. Romer. University of California, Berkeley, May 2012

[15] "Taxes and Entrepreneurial Activity: An Empirical Investigation Using Longitudinal Tax Return Data," Donald Bruce and Tami Gurley , SBA Office of Advocacy, March 2005.

[16] If one uses the 2010 municipal income tax data to calculate a weighted average statewide municipal income tax rate, one would find that it is 1.9%, not 1.5%. (Municipal income tax rates in 2010 ranged from a low of 0.40% in Indian Hill to a high of 3.0% in Parma Heights.) However, since the base of the municipal income tax is narrower than the base of the state income tax (the municipal tax mostly excludes investment income, which is a large share of income for the highest-bracket taxpayers), 1.5% seems like a better estimate of the additional city tax burden to be added to the top marginal state tax rate.

Table 1 - Ohio State Income Tax Rates					
Current Law compared to 20% cut					
Income Brackets and Base Amounts are for Tax Year 2012 – 2015 brackets and base amounts cannot be known until 2015 due to future inflation adjustments					
Lower Limit	Upper Limit	Base amounts for 2012	Rates	Base amounts after 20% cut	Rates After 20% Cut
$0	$5,200	$0.00	0.587%	$0.00	0.470%
$5,200	$10,400	$30.52	1.174%	$24.42	0.939%
$10,400	$15,650	$91.57	2.348%	$73.26	1.878%
$15,650	$20,900	$214.84	2.935%	$171.87	2.348%
$20,900	$41,700	$368.93	3.521%	$295.14	2.817%
$41,700	$83,350	$1,101.30	4.109%	$881.04	3.287%
$83,350	$104,250	$2,812.70	4.695%	$2,250.16	3.756%
$104,250	$208,500	$3,793.96	5.451%	$3,035.16	4.361%
$208,500	$0	$9,476.63	5.925%	$7,581.29	4.740%

Table 1 updated February 5, 2013

The current tax reform proposal would further reduce state marginal rates in all nine brackets over a three year period (see Appendix). The reductions would be 7.5% in tax year 2013, 15.0% in tax year 2014, and 20.0% in tax year 2015 (each year's tax reduction is calculated from the tax year 2012 base year – the incremental rate reductions would thus be 7.5%, 7.5%, and 5.0%). Ohio's top marginal tax rate would drop to 4.74%, which would place it 36th highest (if all other states' rates stayed constant). Even adding in 1.5% for the impact of municipal income taxes, Ohio's new combined highest rate of 6.24% would drop from 14th to 24th (if all other states' rates stayed constant).

The proposed reform would reduce personal income tax revenues by $1.66 billion in FY 2014, $2.67 billion in FY 2015, and $2.73 billion in FY 2016. The large jump in the revenue loss from FY 2014 to FY 2015, and the very small increase in FY 2016, is a function of when employer withholding rates are cut under the proposal. For more detail on the estimated revenue impacts of the income tax reductions, please see the Appendix.[17]

Part 2 – Reducing Small Business Income Taxes

The centerpiece of the tax reform program of reducing state income taxes is to provide additional tax relief directly to small businesses.[18] A 2010 paper from the federal Small Business Administration (SBA) shows that small businesses accounted for between 65% and 90% of net new jobs created for the 1993-2006 or 1993-

[17] Employer withholding rates are proposed to be cut in September 2013, July 2014, and January 2015.The January 2015 cut would move some of what otherwise would be FY 2016 revenue loss into FY 2015.

[18] There is some dispute in the economics literature about whether the bulk of job creation comes from small businesses or new businesses, but in reality most new businesses are small, so the distinction is largely academic. The U.S. Census Bureau's Statistics of U.S. Businesses (SUSB) data shows that over the last 20 years, about 95 percent of new employer firms started with fewer than 20 employees. See "An Analysis of Small Business and Jobs,"
Brian Headd , Small Business Administration Office of Advocacy Brian, March 2010.

2008 period.[19] The tax reform proposal would reduce the state tax burden on small business with the expectation that the reduced tax burden would free up dollars for additional hiring and thus increase Ohio's rate of job growth.

The way this is implemented in the tax reform package is to provide the tax relief to the owners of what are known as pass-through entities (PTEs). PTEs are those businesses that are not taxed, under either federal or most state tax systems, at the business level, but where instead the business owners pay taxes on the profit that "passes through" to them. So, Subchapter S corporation owners, partners in partnerships, owners of limited liability companies (LLCs), and owners of sole proprietorships all pay personal income tax on the income that flows to them from the business entity. [20]

The tax relief being proposed is a deduction of 50 percent of the business income to the owner/investor in calculating the Ohio income tax.[21] So, for example, two people who each own 50 percent of an LLC (LLC owners are called "members" for tax purposes) that earns $300,000 in profit during a year, and who thus get $150,000 each in net income distributions, would get to exclude half that income in computing their Ohio income tax. So, each member would receive a deduction for $75,000 of the $150,000 in net income it received from the LLC.[22]

In practice, although most small businesses are organized as PTEs, and most PTEs are small businesses, PTEs are not synonymous with small businesses. There are PTEs which are quite large, in terms of gross receipts, net income, employment, or whatever measure one would care to apply. Conversely, there are small businesses which are organized as C corporations and which pay the federal corporate income tax (the corporate income tax in Ohio was eliminated as part of the HB 66 tax reform).
Recognizing that not all PTEs are small businesses, the tax reform proposal caps the amount of owner/investor income eligible for the deduction at $750,000 annually. Since the deduction is 50 percent of income, the deduction itself is capped at $375,000 annually. The cap is based on relationships that the Ohio Department of Taxation (ODT) found between firm size (measured by gross receipts) and the size of taxpayer PTE income. ODT found that for taxpayers with over $750,000 in PTE income, the majority of their PTE income came from firms with over $10 million in annual gross receipts. Firms with over $10 million in annual gross receipts are not small – they represent the largest 2% of all PTEs. So, capping the eligible income for deduction at $750,000 per owner/ investor is a proxy for capping the deduction in order to make it be connected to small business income.

The proposed deduction will result in over $14 billion (estimated) in PTE income becoming exempt from state taxation. At an estimated average effective tax rate of 5% on this income, this will save between $600 million and $650 million annually in Ohio taxes.

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[19] The differences in the estimated shares of net job creation resulting from small businesses are the result of using different definitions of small business. In particular, the answer depends on whether a business is classified according to its starting employment size or its eventual employment size.

[20] There are a few states, such as Kentucky and Michigan, where tax is imposed at the business entity level.

[21] A deduction at the level of the business is not practical – the business is not liable for the tax, the owners are. For businesses with multiple owners, it would not be possible for the Ohio Department of Taxation to allow a deduction at the business level and then try to track the use of the deduction by each business owner to ensure that it was appropriate.

[22] Multi-member LLCs send each member a schedule K-1 reporting that member's share of the LLC net income, just as in a partnership. The LLC also files an informational Form 1065 with the IRS, just like a partnership.

Table 2 - Small Business Deduction Tax Savings for Tax Year 2013 / FY 2014				
amounts in millions of $				
		estimated PTE business income deduction (50%, capped at $750,000 of income)		
	estimated PTE business income	Ohio residents	Non-resident investors	Total
Income and Deduction Amounts	$25,676,250,000	-$11,226,000,000	-$2,806,500,000	-$14,032,500,000
Tax savings		-$561,300,000	-$140,325,000	-$701,625,000
Note: The "scoring" of the small business deduction shown in the Appendix shows an estimated revenue loss of less than $701 million. That is because the loss associated with the deduction gets smaller as the tax rates for all Ohio taxpayers are decreased.				

To understand the operation and impact of the small business deduction proposal, it may be helpful to see an example of how the deduction would affect a hypothetical small business. We provide such an example in Table 3, below. The hypothetical business in this case is an Ohio LLC with 3 owners (members), each of whom have one-third ownership of the company. The company produces rubberized cases for tablet computers like the Apple iPad, which it sells to retailers around the country. Let us assume that this is a profitable business, with net income for taxable year 2015 of $1.5 million.

The $1.5 million in business net income is divided three ways, with each of the owners receiving $500,000. To simplify the calculations, let us assume that each owner has no other income, and that each owner has a spouse and two children, for a total of four exemptions for the family. Since for simplicity's sake the spouse is assumed to have no income, the couple has no "joint filer credit," although they file a joint federal and Ohio income tax return.

As one can see from Table 3, each owner of the LLC receives a tax cut both from the proposed rate reductions and the proposed deduction for small business income. The deduction impact is about $12,000 per year per taxpayer, while the rate cut impact is about $5,000 per year per taxpayer, for a net savings of about $17,000 per year per taxpayer. Collectively, the three LLC owners receive a tax cut of slightly over $50,000 per year, with that money being freed up for hiring or capital investment in the business.

Table 3 - Example of Tax Savings from Small Business Deduction						
LLC with 3 equal share owners and $1.5 million in net income						
	Net income	Income tax at current rates, no deduction	Income tax at proposed 20% rate cuts, no deduction	Income tax at proposed 20% rate cuts, with 50% deduction	Total tax savings	Tax savings as % of original tax
Owner 1	$500,000	$26,265	$20,996	$9,146	$17,119	65%
Owner 2	$500,000	$26,265	$20,996	$9,146	$17,119	65%
Owner 3	$500,000	$26,265	$20,996	$9,146	$17,119	65%

Restructuring the State and Local Sales Tax – Base Broadening and Rate Reduction

Ohio's state sales tax, like many state sales taxes, has its origins in the 1930s, when the Great Depression drastically reduced property values and property tax revenues, and the demands on state government for relief programs for the poor skyrocketed. The economy of the 1930s was one where commercial transactions were mostly the exchange of goods ("tangible personal property," or TPP in taxation nomenclature). In 1935, the first year that the Ohio sales tax was in effect (at a 3 percent tax rate), goods were estimated to be 56.5 percent of all U.S. personal consumption expenditures (PCE), and services were estimated to be 43.5 percent of PCE. In 2011, by contrast, goods were 33.8 percent of U.S. PCE, and service had grown to 66.2 percent of PCE. Since U.S. PCE in 2011 was $10.7 trillion, this change in shares represents about $2.4 trillion shifted from goods consumption to services consumption because of the shift in the shares of goods and services.

In the years since the 1930s, the states – Ohio among them – have made efforts to broaden the sales tax base and in particular to include services. Most of these attempts have resulted in a few services being added to the tax base, but not to sweeping change. Those states with broad sales tax bases (such as New Mexico and Hawaii) have typically included most services in those broad bases for decades, often since the inception of the tax. Wide broadening of the tax base to services has not been accomplished in recent decades. The most recent known case of an adopted and maintained expansive services tax base is South Dakota, where the base was expanded to services twice, in 1965 and 1979. In most states that tax a variety of services (but well short of all services), the sales tax base has been expanded in an incremental fashion, adding several new services at a time.

Governor Kasich's reform proposal does not simply enumerate additional services to be subject to the sales tax. Instead, it changes the entire structure of the tax that has been in effect since the 1930s. Current law presumes that exchanges of TPP are taxable unless specifically exempted, but that services are exempted unless specifically enumerated as taxable. The reform proposal would put services on the same basis as TPP: that is, service transactions would be taxable unless specifically exempted.

The proposal excludes major categories of services that one may consider to be essentials for modern life. That is, health care, construction services, rental of residential property (essential because of its connection to providing shelter), and education services would all be exempt. The proposal would also exempt social assistance services, day care services, insurance premiums, residential trash removal, oil and gas drilling services (for more discussion of this exemption, please see the severance tax section). The Appendix contains a comparison of how many services are taxable now in Ohio, how many would be taxable under the proposal, and how many are taxable in other states, according to research by ODT and the Federation of Tax Administrators (FTA).

The history of the sales tax over the past several decades, in Ohio and other states, has been one of a narrowing tax base and increasing tax rates. The tax base has been shrinking due to the change in consumer purchasing patterns from goods to services, and also due to the change in purchasing methods, from buying things at a physical store to buying them from a "remote seller." A remote seller can be either a catalog retailer or an Internet retailer. Many remote sellers claim that they do not have physical presence in Ohio – or in most states – they are free to not collect state and local sales taxes under the U.S. Supreme Court decision in *Quill Corp. v North Dakota* (1992).[23]

In response to the narrowing of the tax base, Ohio and other states have raised state sales tax rates in order to prevent revenue erosion. Ohio's sales tax rate was three percent from 1935 to 1967. In 1967 the state tax rate was increased to four percent, and the legislature authorized county governments to levy "piggyback" sales taxes. In 1974 transit authorities received authority to levy piggyback sales taxes (subject to voter approval). In 1981, the state sales tax rate was increased again, to five percent. In 2003 the state sales tax rate was temporarily increased to six percent for two fiscal years, FY 2004-2005. Finally, the HB 66 tax reform changed the state sales tax rate to 5.5 percent, where it is today.[24]

The Ohio experience is not uncommon among the states. In a 2001 paper dealing mostly with sales tax revenue losses from electronic commerce, professors Fox and Bruce of the University of Tennessee noted that, in response to narrowing tax bases, state sales tax rates had been on a steady path upward. The median state sales tax rate (without factoring in local taxes) had increased from 3.25 percent in 1970 to 4.0 percent in 1980 and 5.0 percent in 1990.[25] Our own calculations, using FTA data, show that the median state sales tax rate has risen to 6.0 percent for 2012, so that it is nearly double what it was in 1970.

From a tax policy perspective, none of these movements in state sales taxes is positive. Public finance economists generally agree that good tax policy involves the use of broader tax bases and lower tax rates, not narrow bases and high rates.[26] This is true for all taxes. With regard to sales taxes specifically, numerous authors have argued for expansion of the sales tax base to include most or all services. Many economists condition their support for base expansion by stating than an "ideal" sales tax would tax all consumer services but not tax any business inputs. However, Professors William Fox and LeAnn Luna point out that while this may be the theoretical ideal, in practice this would be quite difficult to implement:

[23] The Quill decision has spawned a number of state-level Supreme Court (or highest court, if it goes by a different name) cases about who has physical presence and is required to collect sales tax from a state's consumers. See for example *Borders Online LLC v State Board of Equalization* (California Court of Appeals, 2005). The *Quill* decision has also caused numerous state legislative acts meant to define such concepts as 'affiliate nexus," and resulted in a more than 10-year interstate project to simplify and coordinate state sales tax systems (the Streamlined Sales Tax project), thereby reducing the administrative burden on retailers and potentially changing the Court's or Congress's mind about allowing states to compel remote sellers to collect sales tax. A number of federal bills have also been proposed to allow states to require sales tax collection, in exchange for simplification and standardization measures in state and local sales taxes. A full treatment of all the sales tax issues involving remote sellers is beyond the scope of this paper.

[24] This summary omits temporary sales tax changes in 1980-1981.

[25] "State and Local Sales Tax Revenue Losses from E-Commerce: Updated Estimates," Donald Bruce and William Fox, Center for Business and Economic Research, University of Tennessee, September 2001.

[26] See for example the testimony of Leonard Burman, Syracuse University professor of public affairs, before the U.S. Senate Budget Committee on March 1, 2012: "…the standard prescription of broad base and lower rates can be a win-win for fairness and growth."

"…in addition to compliance burdens, exempting business-to-business transactions can create opportunities for tax evasion. Both businesses and consumers use many goods and services, including computers and vehicles. [If business to business transactions are exempted] Individuals can buy items tax-free through a legitimate business (or an inactive business with a still-valid exemption certificate) and convert the items to personal use." [27]

Professors Fox and Luna go on to point out that a broad sales tax base and low rates are advantageous even if some business to business transactions are still taxed:
"Empirical literature on the taxation of consumer purchases supports the policy advice offered by analysts – broad consumption tax bases with low tax rates are more efficient and encourage economic growth even if the states continue to tax many business to business transactions."
State Base Expansion and Rate Reduction

The Ohio tax reform proposal would go against the long-term national trend in that it would both substantially broaden the state sales tax base and cut both state and local sales tax rates. The proposed base expansion would increase the tax base by about $53 billion for the first full year that it is in effect, which is FY 2015. This would represent a base expansion of slightly more than 30 percent of the current law tax base, which is expected to be $175 billion for FY 2015. In response, the reform proposal would cut the state tax rate from the current 5.5% to 5.0%, restoring the state tax rate that was in effect from late 1981 to mid-2003. The reform proposal would also cut local tax rates (county and transit authority), which currently average about 1.3% across the state. The local rates are cut differentially, depending on estimated base broadening by county (see the following section for more detail about cutting local tax rates).

Without the reduction in the state tax rate, the $53 billion increase in the sales tax base would, all else constant, increase state tax revenues by about $2.9 billion. The reform proposal would tax the proposed increased tax base, and the current-law tax base, at 5.0 percent rather than 5.5 percent. This has two effects. First, the revenue gain from the sales tax base expansion becomes $2.65 billion, rather than $2.9 billion, in FY 2015. Second, the rate reduction on the current-law FY 2015 tax base of $175 billion reduces state sales tax collections by $875 million. In FY 2016, after forecasted growth in both the expanded tax base and the current-law tax base, the base expansion increases revenues by $2.76 billion while the rate cut reduces revenues by $917 million.

[27] "How Broad Should State Sales Taxes Be? A Review of the Empirical Literature, William Fox and LeAnn Luna, State tax Notes, September 4, 2006.

Table 4 - Summary of Sales and Use Tax Reform Proposal at the State Level			
amounts in millions of $ - tax base amounts rounded to nearest hundred million			
	3/4 impact	full-year impact	full-year impact
	FY 2014	FY 2015	FY 2016
Base expansion to include services	$38,400	$53,000	$55,300
revenue gain from service expansion at 5% state tax rate	$1,920	$2,650	$2,765
Current-law tax base	$124,200	$175,100	$183,400
revenue loss from 0.5% cut in state tax rate	($621)	($876)	($917)
Net impact on state revenue of base broadening and rate reduction	$1,299	$1,775	$1,848
In FY 2014 the proposal has only 3/4 of a full fiscal year impact. This is because the base expansion and rate cuts begin in September 2013, and due to the one month lag in most collections, the impacts will be felt only for the 9 month period of October through the next June.			

More detail on the estimated increase in the tax base for broad classes of services is included in table 5, below.

Table 5 - Increases in Tax base and State Revenue gain at 5.0% Tax Rate		
amounts in millions of $		
	FY 2015 - full year impact	
	Tax Base	Tax Revenue
Transportation services (intrastate)	$5,260	$263
Information services - motion picture production, cable broadcasting, Internet publishing, etc.	$7,200	$360
Financial services fee income (no interest income); insurance-related services (excluding premiums); and real estate services (lessors of nonresidential buildings; agents, brokers and managers; appraisers)	$11,680	$584
Legal and accounting services	$4,980	$249
Architectural, engineering, and design services (including computer systems design); and other professional services (management consulting, scientific research, advertising, marketing, lobbying, etc.)	$13,220	$661
Administrative and support services (collection agencies, credit rating services, travel agencies, etc.); waste management and remediation services	$6,400	$320
Arts, entertainment, and recreation	$1,700	$85
Miscellaneous other services (e.g. parking lots and garages, coin operated laundries, etc.) and non-profit adjustment	$2,600	$130
All Proposed Newly-Taxed Services	$53,040	$2,652

Local Sales Tax Rate Reductions and State Guarantee Payments

The expansion of the sales tax base potentially creates an enormous additional burden on taxpayers, with local sales taxes paid to counties and transit authorities that levy "piggyback" sales taxes increasing 30 percent. For example, in FY 2016, if the statewide average local tax rate of 1.3 percent were applied to the estimated $55.3 billion additional tax base (see table 4), then local tax collections, all else constant, would increase by $715 million. This is an increase so large that, were it allowed to occur, it would make the FY 2016 reform package a net tax increase to taxpayers rather than a $437 million tax cut (see Figure 1). Although state taxes would still be cut significantly, local taxes would increase enough to more than offset the state tax cut.

The reform proposal would allow counties and transit authorities to benefit from the sales tax base broadening, but in a way that limits the additional local tax burden. Just as the state sales tax rate is reduced, local rates would also be reduced. However, the reduction in local rates is meant to be done in such a way that counties and transit authorities will still see a modest revenue increase due to base broadening. Local tax rates will be reduced to cap that increase.

Although the mechanics and the calculations of the local rate reductions are somewhat involved, the concept is relatively straightforward. New county rates will become effective in September 2013, when the expanded sales tax base goes into effect. Because there will be no actual data on how base broadening will affect county and transit authority tax bases, this first set of new rates will be based on estimates by ODT of how much the base expansion will be in each county or transit area (these estimates will be based on the current-law services tax base amounts by county). The counties will be classed into four groups based on their variation from the mean amount of the currently-taxed services tax base. [28] Each group will then receive a calculated percentage reduction in its tax rates, with the calculated rate then being rounded to the nearest 0.05 percent (i.e. a county may have a new tax rate of 1.05%, but not 1.03%).

This first set of new tax rates will not be calculated in such a way as to hold the county revenues equal before and after base expansion. Instead, they will be calculated to provide the counties with some additional revenue growth due to base expansion. For example, for FY 2014, statewide sales tax revenues, without tax reform impacts, are expected to grow by about 6.5 percent. Any county or transit authority whose revenue growth matches that of the state would therefore also be expected to have revenues increase by 6.5 percent. The new local tax rates are to be calculated so as to provide the counties and transit authorities with 10 percent revenue growth for the first year that they are in effect

The way that this rate reduction is calculated is not intended to limit growth on the existing tax base. Rather, the rate reduction is calculated to offset most of the revenue growth that arises solely from the new tax base. So, with a growth target of 10 percent and estimated growth in the underlying sales tax base (including the additional revenue from additional managed care premiums being subject to tax), the rates are calculated so that the additional tax base provides only an additional 3.5 percent annual growth. To the extent that the growth rate of an individual county from the existing tax base exceeds the estimated statewide 6.5 percent growth, the county can realize higher revenue growth than 10 percent.

The estimated statewide average tax rate reduction for counties and transit authorities in order to reach the 10 percent growth target is approximately 20 percent. Of the five groups, the group with the lowest estimated tax base increase would receive tax rate reductions of only 11 percent. The group with the highest estimated tax

[28] The expected tax base expansion was computed by using county-level data on currently taxed services. Although the county level data for the services that are proposed to be taxed is incomplete, for those counties and services where it was available it showed a strong correlation with the county tax base for services that are taxable under current law. In other words, those counties with relatively high per-capita services tax bases under current law are likely to also have relatively high per-capita amounts for the proposed services.

base increase would receive rate reductions of 35 percent. Currently, the range of local tax rates runs from 0.25 percent for four transit authorities to 1.50 percent for 48 counties. Under the reform proposal, the lowest rates would be 0.20 percent (for the same four transit authorities) to 1.35 percent (for 1 of the 489 counties currently at 1.50 percent).

The setting of the new local tax rates would be inherently subject to errors due to the imperfect data that underlies the calculation. The county level data on revenue by type of service is not robust enough to ensure precisely calibrated initial tax rates. For that reason, the reform proposal would also provide monthly state guarantee payments. Since the sales tax base expansion would go into effect in September 2013, the first full tax collections by the state from vendors would be in October 2013, and the first distribution of permissive tax collections to counties and transit authorities would be in December 2013. For December 2013 through November 2014, counties and transit authorities would be guaranteed to receive each month what they received in the same month in 2012 or 2013, plus an additional 10 percent (or the three year average growth rate, if that is higher). So, for example, if local sales tax revenues in a given county were only 3 percent above the base period revenues, the state would provide an amount of guarantee payment equal to the unrealized 7 percent revenue growth.

For the December 2014 through June 2015 permissive sales tax distributions, the state guarantee is increased to equal 105 percent of the December 2013 through June 2014 guarantee levels. The rationale here is that this period is more than one year after the base calculation period, so the counties and transit authorities are guaranteed an additional 5 percent growth on top of the first year's 10 percent growth. The ending of guarantee payments in June 2015 is meant to coincide with the last month of distributions under the initial set of local tax rates (see below).

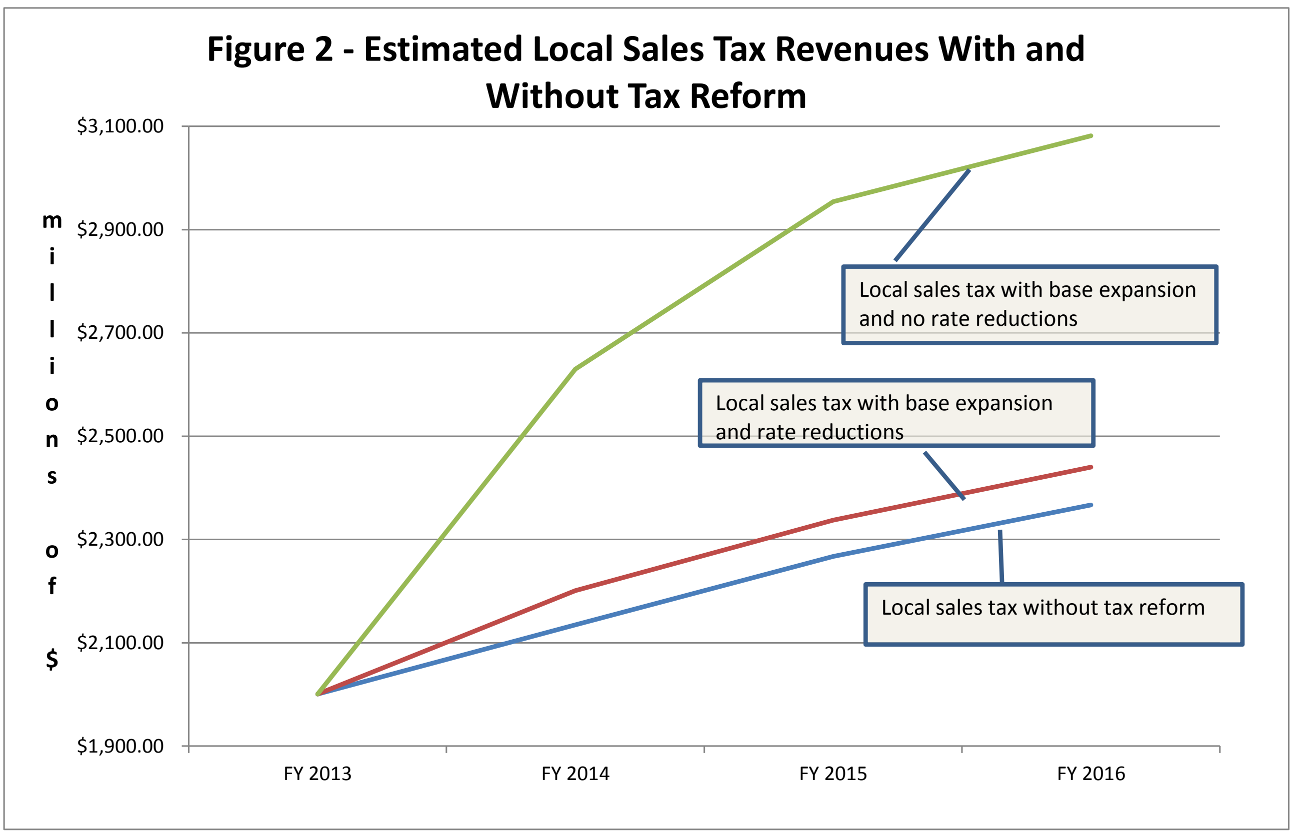
Since the original set of new local rates is subject to error because the data available is old and incomplete, and because local economies change in unpredictable ways, the tax rates would be reset once there is some actual local experience with how base expansion has affected local revenues. The reform proposal would therefore have ODT calculate a second set of local tax rates based on the actual experience with the January 2014 through December 2014 distributions of permissive sales tax revenue. This second set of rates would be designed to fix any errors in the first set of rates, i.e. cases where tax rates were set too low to allow sufficient revenue growth due to base expansion, or cases where rates were set too high and local revenue growth exceeded the 10 percent or three year average target. This second set of tax rates would be calculated by ODT in January 2015, so that notice of rate changes could be published by February 1, 2015, and the new rates could then take effect (after the statutory 60-day waiting period) by April 1, 2015. Tax collections under the second set of rates would begin in May 2015, and the first distributions to counties and transit authorities under that second set of local tax rates would occur in July 2015 (the beginning of state FY 2016).

Finally, since there is the possibility that even the second set of rates will have errors in them, due to exceptional circumstances distorting the first period of collections under the second set of rates, or due to systematic changes in behavior related to the services tax base expansion – suppose, for example, that compliance with the expansion by service providers is weak at first but dramatically improves over time – there is a third and final set of local tax rates computed by ODT. This set will follow essentially the same timeline as the second set of rates. ODT will compute the new tax rates in January 2016, give notice of the new rates by February 1, 2016, and the new rates will go into effect April 1, 2016. The first distributions of permissive tax collections under this third and final set of state-determined local tax rates will take place in July 2016. This third and final set of rates will, once again, be determined by a retrospective look at how much the local tax base produced; they will be set at levels that would have generated the calendar year 2015 revenue "target" as a combination of (a) 105 percent of the January-June period target and (b) the amount of actual sales tax revenue produced and distributed in the July-December period.

The fiscal impacts of the tax rate reductions and state guarantee payments are twofold. First, taxpayers will pay some additional local sales tax under the reduced rates, just as they will pay some additional state sales tax under the reduced 5.0 percent state rate. However, the revenue growth will be lower than it would have been without the rate reductions (See Figure 2). The administration estimates that this amount will be $50 million in FY 2014 (3/4 year impact), $70 million in FY 2015, and $73 million in FY 2016.

Two additional points about the county and transit tax rates should be made. During the period from October 2013 through June 2016, no additional county or transit sales and use taxes can be levied. It would essentially be impossible for ODT to correctly recalibrate county and transit tax rates for the base broadening impacts if at the same time county and transit tax rates are changing for other purposes. Second, the existing county maximum tax rate of 1.5 percent will be reduced by the smallest group-based tax rate reduction, which is estimated to be 10 percent, so that the maximum county rate would decline to 1.35 percent.

The size of the state guarantee payments will essentially be a function of the errors made in the estimation of the tax rates. The guarantee payments will run for 19 months, beginning in December of 2013 (7 months in FY 2104) and ending in June 2015 (12 months in FY 2015). To estimate the size of the guarantee payments, one must make an assumption about how large the estimating errors will be. One way to do this would be to assume that the errors have a mean of zero and are symmetrical about the mean. Since the county and transit authority sales tax levies are expected to generate about $2 billion for state FY 2013, this assumption means that about $1 billion of tax could be expected to have overestimating errors and $1 billion could be expected to have underestimating errors. In the cases where the actual tax falls short of the target (overestimating errors), if the average error is 5 percent, then the necessary state supplement would be about $50 million per year, or $4.17 million per month over 19 months. This would amount to about $79 million over FY 2014-2015 combined. An estimating error of 10 percent would double the expected subsidy payments to $158 million over the FY 2014-2015 biennium.



Restructuring the Severance Tax – New Tax Structure for Output of Horizontal Wells

The extraction of oil, gas, and other hydrocarbons from new wells drilled in the Marcellus and Utica/Point Pleasant Shale formations in eastern Ohio is fundamentally different from the extraction of oil and gas from conventional vertical wells in Ohio. The technology to extract the oil and gas from the shale formations is different – in that the horizontally drilled wells extract hydrocarbons from a significantly larger cross section of the geologic formation. This technology has the potential to produce significantly more product than a vertical well completed in the same shale formations. For example, the Utica formation is expected to produce large volumes of natural gas liquids (NGLs: products such as ethane, propane, and butane). Ohio's conventional vertical wells either do not produce NGLs or they produce them in such low volumes that they are negligible from a commercial perspective, and data about their production is not even captured. Utica shale wells are also expected to produce a fairly large amount of condensate, or natural gasoline that is liquid at ambient temperature and pressure. Once again, condensate, which trades at a somewhat lower price than crude oil, is either not present in many of Ohio's conventional wells or is simply reported as oil. Finally, the volumes of natural gas and oil from the early horizontal Utica wells dwarf the production from Ohio's conventional vertical wells. For example, the Buell well drilled in the Utica formation in Harrison County produced 1.52 million MCF of gas in 2011, in only 198 days of operation.[29] If production were to continue at the same rate per day for all 365 days of the year, annual gas production would be 2.81 million MCF. In contrast, the largest non-Utica gas production in 2011 was from a Muskingum county well that produced just over 500,000 MCF of gas.

All these factors support the creation of a new, separate tax structure for the production from Ohio's newer horizontal oil and gas wells, and the tax reform proposal creates such a new severance tax structure. Rather than a tax based on volumes of oil and gas extracted, which is how the severance tax on vertical well production is structured, the severance tax on horizontal well production will be based on the value of the extracted resources (the product of price and volume). The basic structure of the tax will be a two-tiered rate regime, with natural gas taxed at 1.0 percent of market value and NGLs, oil, and condensate taxed at 4.0 percent of market value. [30] However, for the first year of production from horizontal wells, while producers are recovering the cost of the original investment, a lower tax rate of 1.5 percent will apply to oil, condensate, and NGLs. [31]

The tax structure on the products of conventional vertical wells also changes, in a way that gives tax reductions to the owners of those wells. The effective tax on natural gas, which is currently $0.03 per MCF, is changed to be the lesser of 1 percent of market value or $0.03 per MCF. At prices below $3 per MCF (which was the case for much of 2012), this would result in a tax reduction relative to the current $0.03 per MCF tax rate. Finally, gas wells where the average production is less than 10 MCF per day based on a daily average per quarter would be exempt completely from the Ohio severance tax. This will exempt the output of nearly 45,000 conventional vertical gas wells in Ohio.[32]

[29] An MCF is one thousand cubic feet of gas.

[30] For the sake of simplicity, this analysis does not cover the BTU factors involved in calculating the tax due on horizontal well products.

[31] This does not mean that it will necessarily take one year to recover well drilling costs – recent data indicate that cost recovery may be shorter than one year. Nevertheless, the tax structure allows one year at the lower tax rate for cost recovery.

[32] This estimate is based on an analysis of 2011 oil and gas well production, using numbers from the ODNR Web site.

The difference between the old and new severance tax structures is summarized in Table 6 below.

Table 6 - Comparison of Old and Proposed New Severance Tax Structure			
		New Proposed Severance Tax	
	Current Severance Tax on all wells	Vertical Wells	Horizontal Wells
Product	Tax Rate	Tax Rate	Tax Rate
Gas *	$0.03 per MCF	Lesser of 1% of value of $0.03 per MCF; no tax if production is less than 10 MCF per day	1% of value
Oil *	$0.20 per barrel	$0.20 per barrel	1.5% of value during 1-year cost recover; 4.0% of value thereafter
NGL	No separate tax	No separate tax	1.5% of value during 1-year cost recover; 4.0% of value thereafter
Condensate	Taxed as oil	Taxed as oil	1.5% of value during 1-year cost recover; 4.0% of value thereafter
* Current severance tax rates shown include both the severance tax and the "regulatory cost recovery assessment" that began in 2010.			

The disposition of tax revenue generated from the new horizontal wells is also different than from the conventional vertical wells. Whereas for the conventional vertical wells the tax revenue goes to regulatory funds within the Ohio Department of Natural Resources (ODNR), for the horizontal wells the tax revenue will go to the state GRF and in effect be used to offset some of the cost of the income tax reductions.

Even at the higher proposed severance tax rates on horizontal well output, an Ernst & Young (E&Y) study for the Ohio Business Roundtable found that Ohio's overall taxes, including taxes other than severance, would still rank lowest among the eight states included in the study in terms of overall effective tax rates. The E&Y study examined all major state and local taxes, for two types of wells: wells producing both dry natural gas and NGLs, and wells producing dry natural gas and oil. The seven comparison states in the study were Ohio's resource-extracting neighbors, Michigan, Pennsylvania, and West Virginia, and four other oil and gas dependent states: Arkansas, North Dakota, Oklahoma, and Texas. All seven of those states either already have substantial horizontal well extraction or are expected to have such extraction in the near future. The E&Y study found that Ohio's overall effective tax rate (ETR) on the output from the two types of wells would be 40% or 48% below the average ETR in the other 7 states, depending on the type of well output.

The expected revenue from the new severance tax structure is expected to be small in the first years of the tax reform but to grow quickly, resulting in a significant amount of GRF tax revenue by FY 2016, when the income tax rate cuts are fully phased in.

The revenue that will be raised under the proposed tax structure from the horizontal shale wells is, of course, subject to uncertainty. There are constraints on how quickly the oil and gas can be extracted and sold, and these constraints derive from both how quickly wells can be drilled and put into production and how quickly pipeline capacity can be built to transport the product. The estimated severance tax revenue from horizontal wells for FY 2014-2017 is presented in the table below. Although the estimates for the other reform proposal elements have only been shown through FY 2016, the severance tax estimates are shown through FY 2017 because production is still ramping up substantially between FY 2016 and FY 2017, so that the FY 2016 estimate is still not close to the potential peak revenue gain.

Table 7 - Estimate of Horizontal Well Severance Tax Revenues

Product Type	FY 2014	FY 2015	FY 2016	FY 2017
Gas Severance Tax	$12,600,000	$26,000,000	$32,000,000	$38,000,000
Total NGL Severance	$11,800,000	$24,000,000	$54,000,000	$99,000,000
Total Condensate Severance	$14,500,000	$75,000,000	$156,000,000	$195,000,000
Total Oil Severance	$6,000,000	$31,000,000	$65,000,000	$81,000,000
Grand Total Severance by Year	$44,900,000	$156,000,000	$307,000,000	$413,000,000

Conclusion

This paper has essentially explained the tax reform by explaining in some detail each of its discrete elements: income tax reduction, sales tax base expansion and rate reduction, and severance tax restructuring. When viewed as a whole, however, the reform package represents not only a net tax cut, but a shift in the state tax structure away from income and towards consumption and, to a lesser extent, resource extraction.

In summary, the proposed tax reform is designed to promote efficiency, equity, and growth through its various elements. The income tax rate reductions should promote efficiency and growth by reducing the distortion of the after-tax rates of return on capital and improving Ohio's ability to attract investment and growth relative to other states. The sales tax base broadening and rate reduction should improve efficiency and equity by reducing the distortion of consumer choices between goods and services and reducing the tax rates on goods consumption. The severance tax rate restructuring both generates revenue that helps pay for the income tax rate reductions and may export some of the tax burden to residents of other states, reducing the burden on Ohio residents per dollar of tax generated.

Transforming Higher Education

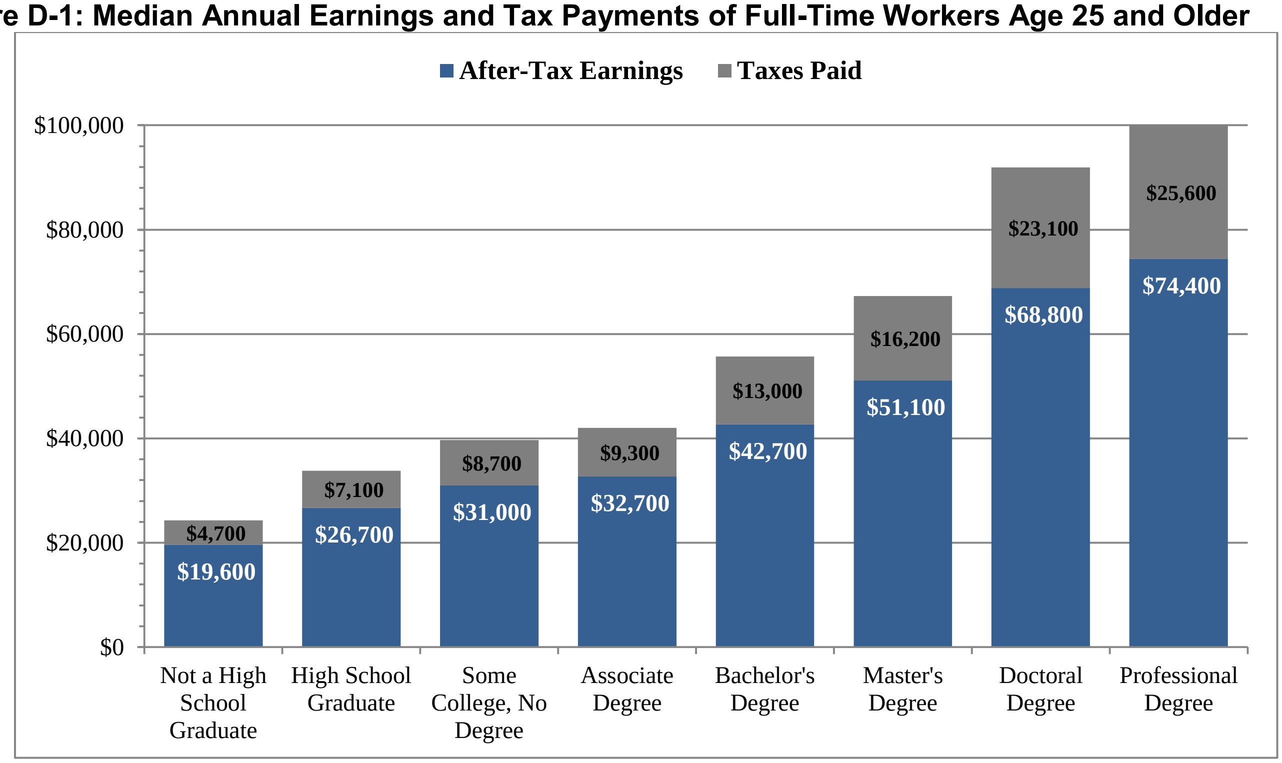
Collaborating for Results: A New Model for Higher Education

The University System of Ohio (USO) is one of the largest comprehensive public systems of higher education in the nation, serving almost 600,000 students and offering a full range of options from a GED to a Ph.D. The system includes 14 universities (with 24 regional campuses), 23 community colleges, and over 120 adult workforce education and training centers across the state. Because of a groundbreaking collaborative approach between Governor Kasich and Ohio's 37 public college and university presidents, the Executive Budget for fiscal years 2014-2015 contains bold policy reforms to the way in which higher education funding is allocated to our public institutions of higher education. Collectively, these reforms position Ohio as a national leader in performance-based funding for higher education. This Special Analysis provides a brief discussion of the benefits associated with higher education, an overview of Ohio's current higher education funding model, and a detailed review of the extensive policy reforms that are recommended to the funding model as a result of Governor Kasich's innovative approach to higher education collaboration.

The Critical Role of Higher Education in Ohio's Economic Recovery

The graduates produced by Ohio's institutions of higher education are a tremendous catalyst for job creation and economic growth. Nationally, as shown in Figure D-1, individuals with higher levels of education earn correspondingly higher annual incomes. In fact, median annual earnings of bachelor's degree recipients working full-time, year-round in 2008 were $55,700, compared to $33,800 for high school graduates [Education Pays 2010, The College Board].

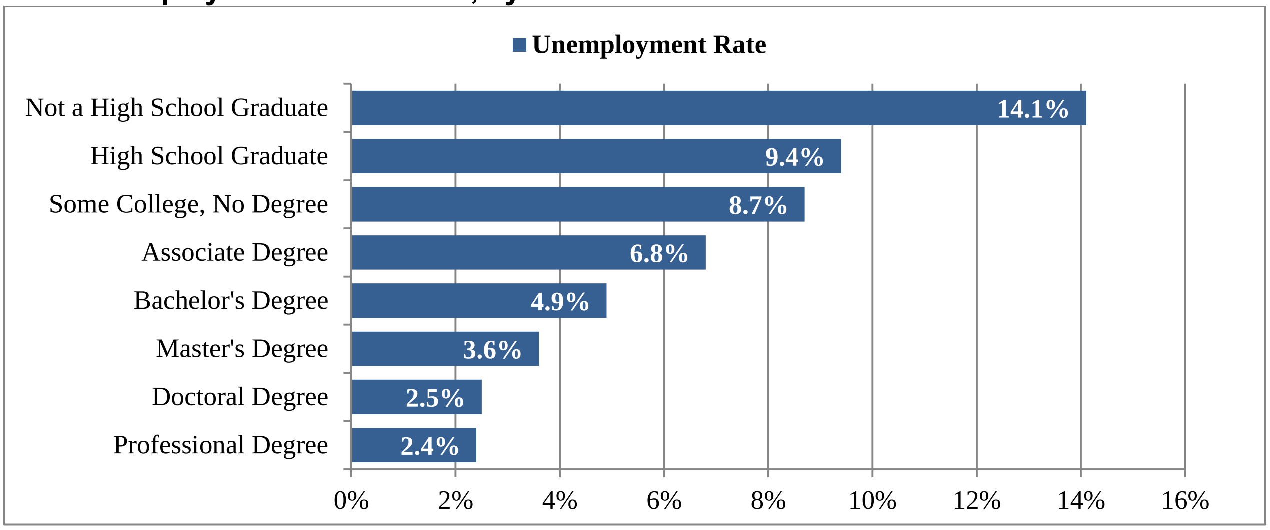
Figure D-1: Median Annual Earnings and Tax Payments of Full-Time Workers Age 25 and Older



Note: Taxes paid include federal income, Social Security, Medicare, state and local income, sales, and property tax. Source: Education Pays 2010, The College Board

Additionally, college-educated workers are more likely to be employed than non-college-educated workers, as shown in Figure D-2. The national unemployment rate for high school graduates in 2011 was almost double that of bachelor's degree recipients [U.S. Bureau of Labor Statistics].

Figure D-2: Unemployment Rate in 2011, by Education Level



Source: U.S. Bureau of Labor Statistics

The employment distinction was even greater for young adults between the ages of 20 and 24 in the fourth quarter of 2009, when the unemployment rate for high school graduates was more than 2.5 times higher than that of college graduates [Education Pays 2010, The College Board].

In addition to producing residents who earn higher incomes and are more likely to be employed than non-college graduates, public higher education also makes a significant contribution to Ohio's total economy through substantial research and development expenditures. According to the most recent national data published by the National Science Foundation [Fifth Report on the Condition of Higher Education in Ohio, 2012], the state's public universities rank sixth nationally in total research funding with combined annual research and development expenditures in FY 2010 totaling more than $2 billion. The Ohio State University ranked second nationally among all universities in terms of industry-funded research, with $120 million in annual research and development expenditures from industrial sponsors.

The quality job opportunities that public institutions of higher education offer for thousands of Ohioans also have a significant economic impact, particularly in rural communities, where a public college or university may be the largest employer in the region.

Beyond the economic benefits cited above, higher education creates the potential for the following positive outcomes:

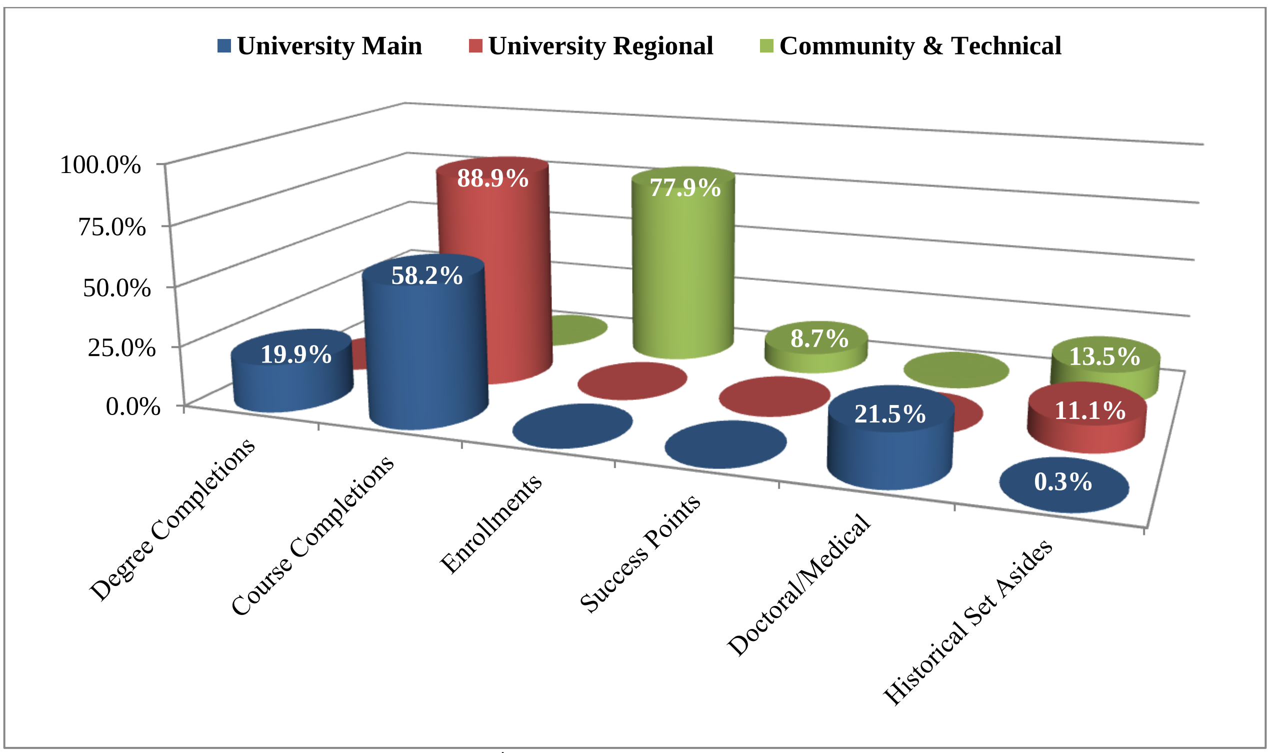
- College-educated adults are more likely to receive better benefits from their employers, and to be satisfied with their jobs;
- A college education leads to healthier lifestyles, reducing health care costs for individuals and for society;
- Federal, state, and local governments receive increased tax revenues from college graduates and spend less on them for income support programs [Education Pays 2010, The College Board].

Higher Education Funding in Ohio: An Overview of the Current Model

The Board of Regents (BOR), led by the Governor's appointed Chancellor, is the state agency that coordinates higher education in Ohio and is responsible for allocating state-appropriated funding to all public institutions of higher education. In FY 2013, BOR's total estimated expenditures are $2,374.4 million, of which $2,308.0 million (97 percent) is comprised of General Revenue Fund (GRF) appropriations. The State Share of Instruction (SSI) is the single line item in BOR's budget that provides unrestricted operating support to the state's 37 public colleges and universities for the purpose of subsidizing educational and general expenses associated with providing subsidy-eligible students with a college education. The SSI is allocated according to distribution formulae that are prescribed by un-codified law in each biennial operating budget. Among BOR's GRF appropriations, after removing debt-service line items, the SSI accounts for $1,751.2 million (85 percent) of BOR's total GRF budget.

The SSI in FY 2013 is allocated within the three public college and university sectors (1-university main, 2-university regional, 3-community and technical) according to sector-specific formulae that distribute funds to each institution based upon factors such as the number of successful course completions, number of enrollments, "success point" benchmarks, doctoral/medical activity, and historical set asides. Figure D-3 provides an overview of the manner by which SSI funding is distributed among each factor within the three public college and university sectors in FY 2013.

Figure D-3: FY 2013 State Share of Instruction (SSI) Formulaic Distribution



Source: Am. Sub. H.B. 153 of the 129th General Assembly

The Challenge Facing Ohio

Until recently, the SSI was allocated almost exclusively according to an enrollment-based formula whereby the state provided a subsidy to each institution based upon the number of students enrolled. Performance-based factors were not included in the formula's distribution and allocations were not tied to the institution's ability to achieve desirable outcomes. The first Kasich Administration budget made progress in this area by allocating an increasing portion of the SSI to student outcomes.

However, despite this recent progress, data clearly indicate that more work needs to be done if Ohio is to produce enough quality graduates with the skills needed to meet the new and changing needs of Ohio businesses. Currently, more than half of all Ohioans who enroll in college fail to earn a degree [Ohio Board of Regents]. Unfortunately, many of the students who fail to earn a degree also leave college with a significant amount of student loan debt. In addition, the percentage of Ohio adults with a bachelor's degree or higher is less than 25 percent, well below the national average [U.S. Census Bureau]. The degree-completion issue is exacerbated by the fact that nearly 60 percent of Ohio's projected job openings by 2020 will require some form of education and training credential beyond high school [Complete College America, Ohio 2011 data]. In fact, one study estimates that Ohio's colleges and universities will need to increase the number of degrees conferred by 10 percent annually to meet workforce needs for 2018 [Georgetown University Center on Education and the Workforce]. These statistics highlight Ohio's challenge and make it clear that our public colleges and universities must improve their graduation rates and increase the overall number of students who earn a degree in order to produce more students with the qualifications needed to enter the workforce.

Governor Kasich's Call for Collaboration

Recognizing the importance of these issues and their direct correlation to Ohio's economic outlook, Governor Kasich met with the leaders of Ohio's public colleges and universities in the fall of 2012 and asked them to work together to envision the SSI not simply as a state subsidy, but rather as a strategic source of funding. It was his goal that this new approach would dramatically incentivize student success as well as increased course and degree completions while holding public institutions accountable for results. The Governor's call-to-action for higher education leaders to collaborate, rather than compete, demonstrates his innovative partnership with higher education. It also demonstrates the Governor's belief that higher education leaders are equipped with the knowledge, insight, and desire necessary to engage in a collaborative process to re-design the SSI formula in ways that incentivize desirable outcomes, prioritize student success, and achieve state goals.

Expanding upon the successful collaboration among higher education leaders that was achieved in the most recent capital appropriations bill (Sub. H.B. 482 of the 129th General Assembly), these leaders were re-convened as the Higher Education Funding Commission and charged with re-designing the SSI formula to respond to the Governor's new challenge. The Commission's first step was to collectively adopt the following Guiding Principles in order to clearly articulate the overarching principles that would guide their collaborative work in re-designing the SSI formula:

1. Incentivize colleges and universities to improve graduation rates, the number of graduates and the time it takes to graduate in order to produce more students ready to enter the workforce.
2. Increase Ohio's competitive advantage by capitalizing on our existing strengths.
3. Strengthen our ability to respond to new or increased workforce development opportunities in the state.
4. Raise participation rates in higher education among Ohio high school graduates.
5. Attract the best and brightest students from Ohio and elsewhere to learn and work in Ohio.
6. Encourage colleges and universities to attract, prepare and graduate non-traditional and at-risk students.
7. Ensure that college is affordable for students and families.

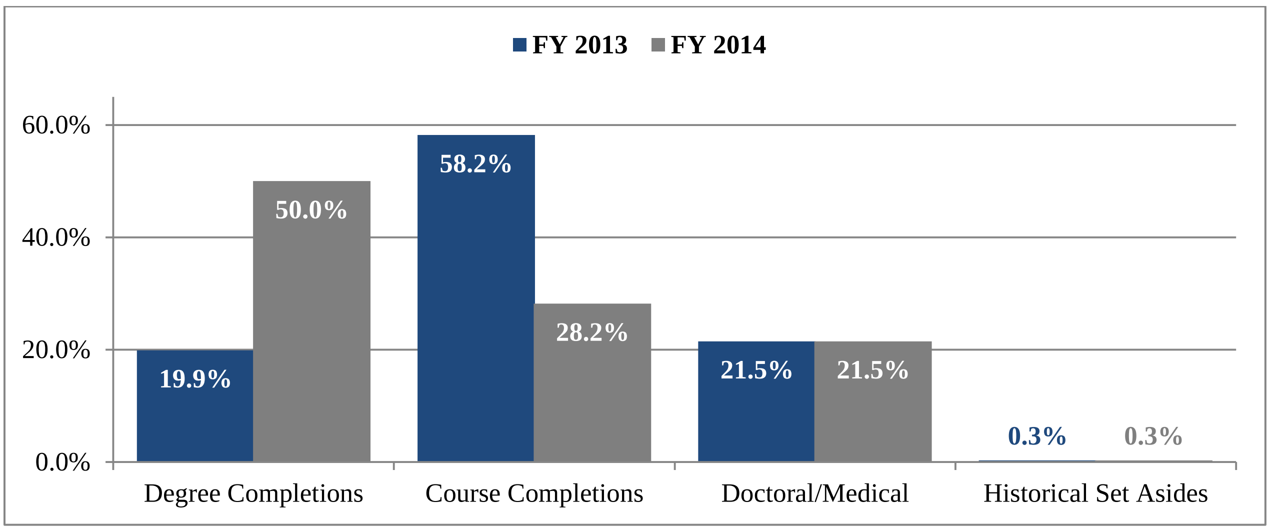
Policy Changes within the Re-Designed SSI Formula

After several months of deliberation among higher education leaders throughout the state, the Higher Education Funding Commission responded to the Governor's challenge by submitting a final report, signed by every public college and university president in the state, recommending numerous policy changes to the SSI formula. The recommendations of the Commission were strongly endorsed by Governor Kasich and are included in the Executive Budget for fiscal years 2014-2015. The following pages provide a detailed review of the most significant university and community college funding reforms contained within the budget.

University Formula Changes

Perhaps the most significant formulaic change proposed for universities in the fiscal years 2014-2015 biennium is the allocation of 50 percent of the total university funding for degree completions. This means that 50 percent of the funding available to universities within the SSI will be awarded according to the number of students who actually complete a degree at the university. This single change sends a strong message that our public universities understand that producing an increasing number of quality graduates must be their top priority if Ohio is to respond to changing workforce demands while remaining competitive in a global economy. Figure D-4 provides a comparative overview of the way in which university funding is allocated among the various formulaic factors between the current formula (FY 2013) and the proposed formula (FY 2014).

Figure D-4: University Formula Changes, FY 2013 to FY 2014



Sources: Am. Sub. H.B. 153 of the 129th General Assembly; Recommendations of the Higher Education Funding Commission, November 2012

In addition to prioritizing degree completions, other significant policy changes are contained within the proposed university formula for FY 2014. All of the formulaic changes were designed under the philosophy of simplifying the formula while holding institutions accountable for results, incentivizing course and degree completions, and eliminating historical earmarks and artificial safeguards that protect underachieving institutions. Highlights include the following:

- Eliminate the Stop Loss
  - This re-distributive mechanism, which reduces university allocations in each fiscal year in order to mitigate funding losses at poor-performing institutions, is eliminated.
- Eliminate Historical Set Asides
  - Two outdated earmarks for university regional campuses, the Access Challenge and square-foot-based plant operation and maintenance (POM), are eliminated. These previously earmarked funds, totaling more than $12.9 million in FY 2013, will now reward performance-based outcomes by flowing through the formula. The same two earmarks for university main campuses will be eliminated in FY 2016.
- Adopt a Standard Three-Year Average

- In FY 2013, several different methods of averaging are used throughout the formula. In FY 2014, a standard three-year average is used consistently to reduce unnecessary confusion and facilitate appropriate planning at the campus level.

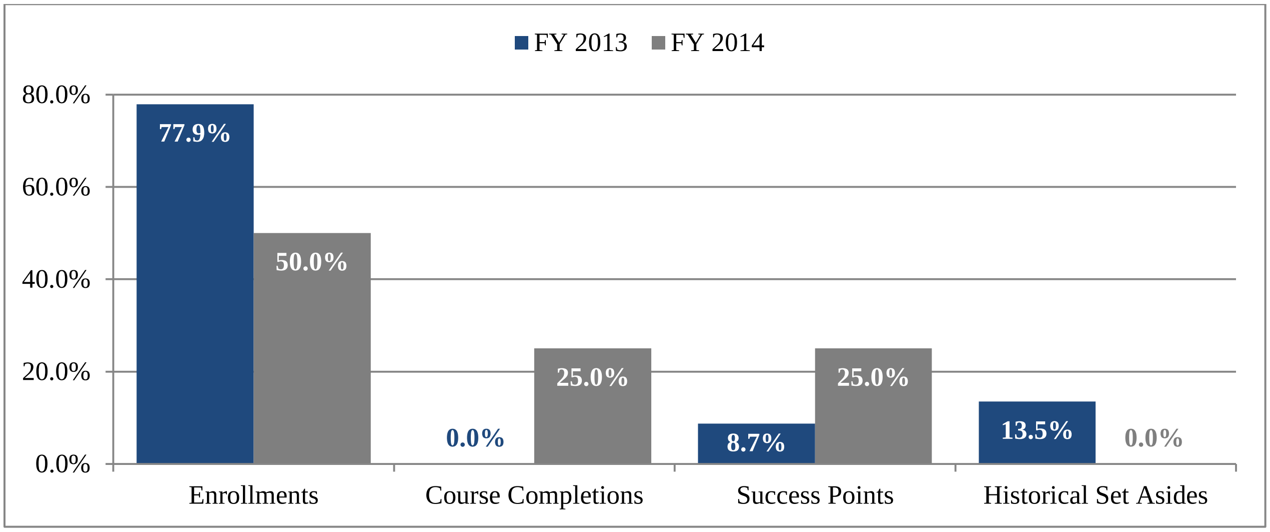
Using a phased-in approach, the following formulaic changes will be implemented beginning in FY 2015:

- Proportional Credit for Transfer Students
  - In FY 2013, degree completion funding is awarded entirely to the institution from which a student graduates, regardless of the amount of credits actually taken at that institution. In FY 2015, degree funding will be awarded proportionally to multiple universities at the time of a student's graduation, based on the actual amount of credits taken at that university.
- Apply At-Risk Weights at the Student Level
  - At-risks weights recognize the various factors that make it more challenging for a student to complete a degree and reward institutions when those factors are overcome and the student graduates. These weights will no longer be applied at the campus level through a general campus index, and will instead be applied at the individual student level based on the student's precise level of at-risk factors.
- Remove the Separate Funding Formula for Regional Campuses
  - Funding will no longer be set aside in the formula and distributed separately for regional campuses. Instead, all students in the university sector will be treated the same, regardless of where they are located.
- Out-of-State Undergraduates
  - In FY 2013, out-of-state undergraduate students are treated the same as Ohio undergraduates in terms of the amount of funding the institution receives when the student graduates. In FY 2015, institutions will be eligible for 50 percent of the degree completion funding for out-of-state undergraduates, but only if the student remains in Ohio for one year after graduation.
- Award Credit for Associate Degrees
  - In FY 2013, only a small number of main campuses earn credit for awarding associate degrees. In recognition of the value that associate degrees hold in contributing to a diverse and highly trained workforce, the new formula provides funding for associate degrees earned at all university regional and main campuses.

Community College Formula Changes

Like their university counterparts, community college leaders embraced the Governor's challenge to re-design a formula that would promote meaningful change and reward outcomes rather than inputs. As a result, the community college formula will transition in the fiscal years 2014-2015 biennium from a system where the majority of funding is allocated based on the number of enrolled students and historically guaranteed set asides to a system that funds the completion of classes, certificates, and degrees. Figure D-5 provides a comparative overview of the way in which community college funding is allocated among the various formulaic factors between the current formula (FY 2013) and the first year of the newly proposed formula (FY 2014). The enrollment-based funding factor will be completely eliminated in FY 2015 and all of the community college funding will be allocated among 1) degree completions, 2) course completions, and 3) success points. The specific percentages allocated according to these three factors for FY 2015 will be determined during FY 2014 by community college leaders, in consultation with the Chancellor, for implementation in FY 2015.

Figure D-5: Community College Formula Changes, FY 2013 to FY 2014



Sources: Am. Sub. H.B. 153 of the 129th General Assembly; Recommendations of the Higher Education Funding Commission, November 2012

Other significant policy changes within the proposed community college formula for FY 2014 include the following:

- Eliminate Historical Set Asides
  - Two outdated earmarks for community colleges, the Access Challenge and Supplemental Tuition Subsidy, are eliminated. These previously earmarked funds, totaling almost $54.5 million in FY 2013, will now reward performance-based outcomes by flowing through the formula.
- Adopt a Standard Three-Year Average
  - In FY 2013, several different methods of averaging are used throughout the formula. In FY 2014, a standard three-year average is used consistently to reduce unnecessary confusion and facilitate appropriate planning at the campus level.

Using a phased-in approach, the following formulaic changes will be implemented beginning in FY 2015:

- Eliminate the Stop Loss
  - This re-distributive mechanism, which reduces community college allocations in each fiscal year in order to mitigate funding losses at poor-performing institutions, is eliminated.
- Develop a Degree Completion Incentive
  - Enrollment-based funding will be completely eliminated in FY 2015 and a new provision will be introduced, at the recommendation of community college leaders, to reward the successful completion of an associate degree or certificate. Once implemented, 100 percent of community college funding will be awarded based upon completion-based factors.
- Review Success Points
  - The current Success Point incentive system, which ties community college funding to established measures of student achievement, will be reviewed and revised accordingly to ensure that the system accurately recognizes the range of activities that lead to course and degree completion.
- Develop a New At-Risk Formula Weight
  - In order to protect the access mission of Ohio's community colleges, a new formula weight will be introduced to reward schools that are successful in enrolling and educating non-traditional and at-risk student populations.

Conclusion and Next Steps

As detailed in this Special Analysis, the SSI formula will experience significant performance-based improvements in the fiscal years 2014-2015 biennium, with a focus on incentivizing increased course and degree completions while holding institutions accountable for results. Perhaps most remarkable is the fact that these reforms were affirmed and recommended by every one of the 37 public college and university presidents in recognition of the challenges facing Ohio and the critical role that higher education can and will play in contributing to Ohio's economic recovery. The policy reforms contained in the Executive Budget for fiscal years 2014-2015 represent the culmination of an unprecedented collaborative approach to higher education funding reform. As a result of their willingness to collaborate for the good of the state, the higher education community has positioned Ohio in a national leadership role in public funding reform for colleges and universities.

The Kasich Administration is grateful to Ohio's college and university leaders for the valuable partnership that has developed throughout this endeavor. As the extensive SSI policy reforms are implemented during the fiscal years 2014-2015 biennium, Governor Kasich will continue to engage the Higher Education Funding Commission and the Board of Regents in strategic conversations to monitor the impact and success of these reforms. The partners will also be asked to consider additional initiatives that leverage the SSI to produce increased course and degree completions, a diverse and highly trained workforce, and continuing economic growth for Ohio.

Appendix A - Personal Income Tax

Income Tax Interstate Rate Comparisons

STATE INDIVIDUAL INCOME TAXES

(Tax rates for tax year 2012 – as of January 1, 2012)

Ohio shown at current-law tax rates			**Ohio shown after proposed 20% cut**		
State	Top Tax Rate (percent)	Rank of top state tax rate	State	Top Tax Rate (percent)	Rank of top state tax rate
HAWAII	11.00	1	HAWAII	11.00	1
CALIFORNIA	10.3	2	CALIFORNIA	10.3	2
OREGON	9.9	3	OREGON	9.9	3
IOWA	8.98	4	IOWA	8.98	4
NEW JERSEY	8.97	5	NEW JERSEY	8.97	5
VERMONT	8.95	6	VERMONT	8.95	6
DIST. OF COLUMBIA	8.95	7	DIST. OF COLUMBIA	8.95	7
NEW YORK	8.82	8	NEW YORK	8.82	8
MAINE	8.5	9	MAINE	8.5	9
MINNESOTA	7.85	10	MINNESOTA	7.85	10
IDAHO	7.8	11	IDAHO	7.8	11
NORTH CAROLINA	7.75	12	NORTH CAROLINA	7.75	12
WISCONSIN	7.75	13	WISCONSIN	7.75	13
ARKANSAS	7.0	14	ARKANSAS	7.0	14
SOUTH CAROLINA	7.0	15	SOUTH CAROLINA	7.0	15
MONTANA	6.9	16	MONTANA	6.9	16
NEBRASKA	6.84	17	NEBRASKA	6.84	17
DELAWARE	6.75	18	DELAWARE	6.75	18
CONNECTICUT	6.7	19	CONNECTICUT	6.7	19
WEST VIRGINIA	6.5	20	WEST VIRGINIA	6.5	20
KANSAS	6.45	21	KANSAS	6.45	21
GEORGIA	6.0	22	GEORGIA	6.0	22
KENTUCKY	6.0	23	KENTUCKY	6.0	23
LOUISIANA	6.0	24	LOUISIANA	6.0	24
MISSOURI	6.0	25	MISSOURI	6.0	25
RHODE ISLAND	5.99	26	RHODE ISLAND	5.99	26
OHIO state rate only	5.925	27	VIRGINIA	5.75	27
VIRGINIA	5.75	28	MARYLAND	5.5	28
MARYLAND	5.5	29	MASSACHUSETTS	5.3	29
MASSACHUSETTS	5.3	30	OKLAHOMA	5.25	30
OKLAHOMA	5.25	31	ALABAMA	5.0	31
ALABAMA	5.0	32	MISSISSIPPI	5.0	32
MISSISSIPPI	5.0	33	ILLINOIS	5.0	33
ILLINOIS	5.0	34	UTAH	5.0	34
UTAH	5.0	35	NEW MEXICO	4.9	35
NEW MEXICO	4.9	36	OHIO	4.74	36
COLORADO	4.63	37	COLORADO	4.63	37
ARIZONA	4.54	38	ARIZONA	4.54	38
MICHIGAN	4.35	39	MICHIGAN	4.35	39
NORTH DAKOTA	3.99	40	NORTH DAKOTA	3.99	40
INDIANA	3.4	41	INDIANA	3.4	41
PENNSYLVANIA	3.07	42	PENNSYLVANIA	3.07	42
ALASKA	No State Income Tax	43	ALASKA	No State Income	43
FLORIDA	No State Income Tax	44	FLORIDA	No State Income	44
NEVADA	No State Income Tax	45	NEVADA	No State Income T	45
NEW HAMPSHIRE	State Income Tax of 5% on Dividends and Interest Income Only	46	NEW HAMPSHIRE	State Income Tax of 5% on Dividends and Interest Income Only	46
SOUTH DAKOTA	No State Income Tax	47	SOUTH DAKOTA	No State Income	47
TENNESSEE	State Income Tax of 6% on Dividends and Interest Income Only	48	TENNESSEE	State Income Tax of 6% on Dividends and Interest Income Only	48
TEXAS	No State Income Tax	49	TEXAS	No State Income	49
WASHINGTON	No State Income Tax	50	WASHINGTON	No State Income	50
WYOMING	No State Income Tax	51	WYOMING	No State Income	51

Source: The Federation of Tax Administrators from various sources, author's calculations

Appendix A - Personal Income Tax - Page 2

STATE INDIVIDUAL INCOME TAXES

(Tax rates for tax year 2012 – as of January 1, 2012)

Ohio shown at current-law tax rates with 1.5% municipal income tax added. Local income taxes added in four other states also.

State	Top Tax Rate (percent)	Rank of top state tax rate
HAWAII	11.00	1
CALIFORNIA	10.3	2
OREGON	9.9	3
IOWA	8.98	4
NEW JERSEY	8.97	5
VERMONT	8.95	6
DIST. OF COLUMBIA	8.95	7
NEW YORK	8.82	8
MAINE	8.5	9
MINNESOTA	7.85	10
IDAHO	7.8	11
NORTH CAROLINA	7.75	12
WISCONSIN	7.75	13
OHIO state plus local rate	7.425	14
MARYLAND	7.07	15
ARKANSAS	7.0	16
SOUTH CAROLINA	7.0	17
MONTANA	6.9	18
NEBRASKA	6.84	19
DELAWARE	6.75	20
KENTUCKY	6.74	21
CONNECTICUT	6.7	22
WEST VIRGINIA	6.5	23
KANSAS	6.45	24
GEORGIA	6.0	25
LOUISIANA	6.0	26
MISSOURI	6.0	27
RHODE ISLAND	5.99	28
VIRGINIA	5.75	29
MASSACHUSETTS	5.3	30
OKLAHOMA	5.25	31
ALABAMA	5.0	32
MISSISSIPPI	5.0	33
ILLINOIS	5.0	34
UTAH	5.0	35
NEW MEXICO	4.9	36
COLORADO	4.63	37
ARIZONA	4.54	38
MICHIGAN	4.35	39
INDIANA	4.04	40
NORTH DAKOTA	3.99	41
PENNSYLVANIA	3.85	42
ALASKA	No State Income Tax	43
FLORIDA	No State Income Tax	44
NEVADA	No State Income Tax	45
NEW HAMPSHIRE	State Income Tax of 5% on Dividends and Interest Income Only	46
SOUTH DAKOTA	No State Income Tax	47
TENNESSEE	State Income Tax of 6% on Dividends and Interest Income Only	48
TEXAS	No State Income Tax	49
WASHINGTON	No State Income Tax	50
WYOMING	No State Income Tax	51

Ohio shown after proposed 20% cut with 1.5% municipal income tax added. Local income taxes added in four other states also

State	Top Tax Rate (percent)	Rank of top state tax rate
HAWAII	11.00	1
CALIFORNIA	10.3	2
OREGON	9.9	3
IOWA	8.98	4
NEW JERSEY	8.97	5
VERMONT	8.95	6
DIST. OF COLUMBIA	8.95	7
NEW YORK	8.82	8
MAINE	8.5	9
MINNESOTA	7.85	10
IDAHO	7.8	11
NORTH CAROLINA	7.75	12
WISCONSIN	7.75	13
MARYLAND	7.07	14
ARKANSAS	7.0	15
SOUTH CAROLINA	7.0	16
MONTANA	6.9	17
NEBRASKA	6.84	18
DELAWARE	6.75	19
KENTUCKY	6.74	20
CONNECTICUT	6.7	21
WEST VIRGINIA	6.5	22
KANSAS	6.45	23
OHIO	6.24	24
GEORGIA	6.0	25
LOUISIANA	6.0	26
MISSOURI	6.0	27
RHODE ISLAND	5.99	28
VIRGINIA	5.75	29
MASSACHUSETTS	5.3	30
OKLAHOMA	5.25	31
ALABAMA	5.0	32
MISSISSIPPI	5.0	33
ILLINOIS	5.0	34
UTAH	5.0	35
NEW MEXICO	4.9	36
COLORADO	4.63	37
ARIZONA	4.54	38
MICHIGAN	4.35	39
INDIANA	4.04	40
NORTH DAKOTA	3.99	41
PENNSYLVANIA	3.85	42
ALASKA	No State Income Tax	43
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TENNESSEE	State Income Tax of 6% on Dividends and Interest Income Only	48
TEXAS	No State Income Tax	49
WASHINGTON	No State Income Tax	50
WYOMING	No State Income Tax	51

Source: The Federation of Tax Administrators from various sources, Tax Foundation (local income taxes), OBM calculations

The four states to which local income taxes are added, other than Ohio, are Indiana, Kentucky, Maryland, and Pennsylvania

Appendix A - Personal Income Tax - Page 3

Income Tax Interstate Tax Burden Comparisons

State Income Tax as a Percent of Personal Income, 2010				
State	State income tax amount	Personal income	Income tax as pct of income	Rank
New York	34,751,382	952,673,131	3.65%	1
Oregon	4,945,538	137,820,653	3.59%	2
Massachusetts	10,128,035	335,264,289	3.02%	3
California	45,646,436	1,564,209,194	2.92%	4
Connecticut	5,768,846	198,177,832	2.91%	5
Minnesota	6,458,111	225,853,125	2.86%	6
North Carolina	9,133,689	330,825,526	2.76%	7
Hawaii	1,527,790	55,832,057	2.74%	8
Maine	1,303,370	48,620,161	2.68%	9
Wisconsin	5,791,991	216,338,590	2.68%	10
West Virginia	1,521,895	58,979,760	2.58%	11
Virginia	8,659,470	354,127,225	2.45%	12
Kansas	2,687,542	110,205,217	2.44%	13
Delaware	853,107	35,474,593	2.40%	14
Utah	2,104,641	89,152,008	2.36%	15
New Jersey	10,322,943	443,741,546	2.33%	16
Iowa	2,650,037	115,547,890	2.29%	17
Kentucky	3,154,488	141,302,143	2.23%	18
Arkansas	2,091,082	94,581,100	2.21%	19
Maryland	6,200,292	281,304,904	2.20%	20
Idaho	1,068,754	49,577,319	2.16%	21
Nebraska	1,514,831	72,189,707	2.10%	22
Montana	714,814	34,093,509	2.10%	23
Georgia	7,016,412	335,370,808	2.09%	24
Rhode Island	909,674	44,207,139	2.06%	25
Missouri	4,326,507	218,278,293	1.98%	26
Vermont	489,107	24,870,824	1.97%	27
Colorado	4,089,948	212,545,078	1.92%	28
Ohio	7,886,802	414,567,053	1.90%	29
Pennsylvania	9,352,287	514,351,774	1.82%	30
South Carolina	2,673,000	149,283,181	1.79%	31
Indiana	3,868,093	220,865,747	1.75%	32
Oklahoma	2,224,783	133,616,459	1.67%	33
Michigan	5,488,962	339,043,905	1.62%	34
Alabama	2,589,249	161,314,102	1.61%	35
Illinois	8,510,000	539,680,018	1.58%	36
Mississippi	1,352,481	91,600,117	1.48%	37
New Mexico	956,600	68,050,198	1.41%	38
Louisiana	2,286,500	168,704,348	1.36%	39
Arizona	2,416,324	216,589,552	1.12%	40
North Dakota	303,764	28,646,144	1.06%	41
New Hampshire	82,365	57,897,613	0.14%	42
Tennessee	172,459	223,165,735	0.08%	43
Alaska	0	31,243,303	0.00%	44
District of Columbia	(X)	43,082,099	0.00%	45
Florida	0	722,368,152	0.00%	46
Nevada	0	96,751,471	0.00%	47
South Dakota	0	32,302,753	0.00%	48
Texas	0	965,236,295	0.00%	49
Washington	0	283,367,864	0.00%	50
Wyoming	0	25,604,496	0.00%	51
United States Total	235,994,401	12,308,496,000	1.92%	

Appendix A - Personal Income Tax - Page 4

Local Income Tax as a Percent of Personal Income, 2010				
State	Local income tax	Personal income	Local income tax as pct of income	Rank
District of Columbia	1,107,139	43,082,099	2.57%	1
Maryland	3,802,209	281,304,904	1.35%	2
Ohio	4,149,051	414,567,053	1.00%	3
New York	7,741,967	952,673,131	0.81%	4
Pennsylvania	4,018,293	514,351,774	0.78%	5
Kentucky	1,035,221	141,302,143	0.73%	6
Indiana	1,557,901	220,865,747	0.71%	7
Delaware	54,146	35,474,593	0.15%	8
Missouri	287,258	218,278,293	0.13%	9
Michigan	381,725	339,043,905	0.11%	10
Iowa	96,512	115,547,890	0.08%	11
Alabama	107,859	161,314,102	0.07%	12
Kansas	3,663	110,205,217	0.00%	13
Oregon	905	137,820,653	0.00%	14
Alaska	0	31,243,303	0.00%	15
Arizona	0	216,589,552	0.00%	16
Arkansas	0	94,581,100	0.00%	17
California	0	1,564,209,194	0.00%	18
Colorado	0	212,545,078	0.00%	19
Connecticut	0	198,177,832	0.00%	20
Florida	0	722,368,152	0.00%	21
Georgia	0	335,370,808	0.00%	22
Hawaii	0	55,832,057	0.00%	23
Idaho	0	49,577,319	0.00%	24
Illinois	0	539,680,018	0.00%	25
Louisiana	0	168,704,348	0.00%	26
Maine	0	48,620,161	0.00%	27
Massachusetts	0	335,264,289	0.00%	28
Minnesota	0	225,853,125	0.00%	29
Mississippi	0	91,600,117	0.00%	30
Montana	0	34,093,509	0.00%	31
Nebraska	0	72,189,707	0.00%	32
Nevada	0	96,751,471	0.00%	33
New Hampshire	0	57,897,613	0.00%	34
New Jersey	0	443,741,546	0.00%	35
New Mexico	0	68,050,198	0.00%	36
North Carolina	0	330,825,526	0.00%	37
North Dakota	0	28,646,144	0.00%	38
Oklahoma	0	133,616,459	0.00%	39
Rhode Island	0	44,207,139	0.00%	40
South Carolina	0	149,283,181	0.00%	41
South Dakota	0	32,302,753	0.00%	42
Tennessee	0	223,165,735	0.00%	43
Texas	0	965,236,295	0.00%	44
Utah	0	89,152,008	0.00%	45
Vermont	0	24,870,824	0.00%	46
Virginia	0	354,127,225	0.00%	47
Washington	0	283,367,864	0.00%	48
West Virginia	0	58,979,760	0.00%	49
Wisconsin	0	216,338,590	0.00%	50
Wyoming	0	25,604,496	0.00%	51
United States Total	24,343,849	12,308,496,000	0.20%	

Appendix A - Personal Income Tax - Page 5

State and Local Income Tax as a Percent of Personal Income, 2010				
State	State and local combined income tax	Personal income	State and local income tax as pct of income	Rank
New York	42,493,349	952,673,131	4.46%	1
Oregon	4,946,443	137,820,653	3.59%	2
Maryland	10,002,501	281,304,904	3.56%	3
Massachusetts	10,128,035	335,264,289	3.02%	4
Kentucky	4,189,709	141,302,143	2.97%	5
California	45,646,436	1,564,209,194	2.92%	6
Connecticut	5,768,846	198,177,832	2.91%	7
Ohio	12,035,853	414,567,053	2.90%	8
Minnesota	6,458,111	225,853,125	2.86%	9
North Carolina	9,133,689	330,825,526	2.76%	10
Hawaii	1,527,790	55,832,057	2.74%	11
Maine	1,303,370	48,620,161	2.68%	12
Wisconsin	5,791,991	216,338,590	2.68%	13
Pennsylvania	13,370,580	514,351,774	2.60%	14
West Virginia	1,521,895	58,979,760	2.58%	15
District of Columbia	1,107,139	43,082,099	2.57%	16
Delaware	907,253	35,474,593	2.56%	17
Indiana	5,425,994	220,865,747	2.46%	18
Virginia	8,659,470	354,127,225	2.45%	19
Kansas	2,691,205	110,205,217	2.44%	20
Iowa	2,746,549	115,547,890	2.38%	21
Utah	2,104,641	89,152,008	2.36%	22
New Jersey	10,322,943	443,741,546	2.33%	23
Arkansas	2,091,082	94,581,100	2.21%	24
Idaho	1,068,754	49,577,319	2.16%	25
Missouri	4,613,765	218,278,293	2.11%	26
Nebraska	1,514,831	72,189,707	2.10%	27
Montana	714,814	34,093,509	2.10%	28
Georgia	7,016,412	335,370,808	2.09%	29
Rhode Island	909,674	44,207,139	2.06%	30
Vermont	489,107	24,870,824	1.97%	31
Colorado	4,089,948	212,545,078	1.92%	32
South Carolina	2,673,000	149,283,181	1.79%	33
Michigan	5,870,687	339,043,905	1.73%	34
Alabama	2,697,108	161,314,102	1.67%	35
Oklahoma	2,224,783	133,616,459	1.67%	36
Illinois	8,510,000	539,680,018	1.58%	37
Mississippi	1,352,481	91,600,117	1.48%	38
New Mexico	956,600	68,050,198	1.41%	39
Louisiana	2,286,500	168,704,348	1.36%	40
Arizona	2,416,324	216,589,552	1.12%	41
North Dakota	303,764	28,646,144	1.06%	42
New Hampshire	82,365	57,897,613	0.14%	43
Tennessee	172,459	223,165,735	0.08%	44
Alaska	0	31,243,303	0.00%	45
Florida	0	722,368,152	0.00%	46
Nevada	0	96,751,471	0.00%	47
South Dakota	0	32,302,753	0.00%	48
Texas	0	965,236,295	0.00%	49
Washington	0	283,367,864	0.00%	50
Wyoming	0	25,604,496	0.00%	51
United States Total	260,338,250	12,308,496,000	2.12%	

Appendix B - Income Tax Relief

Ohio Individual Income Tax

Current vs. Proposed Law by income group*

Fiscal Year 2016: Reflects fully phased in 20% rate reduction**

		Current Law			After Proposed 20% Rate Reductions			
Ohio Taxable Income Group	**Number of Filers**	**Tax Under Current Law (millions $'s)**	**Average Liability Per Taxpayer**	**Share of Total Income Tax Liability**	**Tax After Rate Reductions (millions $'s)**	**Average Liability Per Taxpayer**	**Share of Total Income Tax Liability**	**Percent Change in Liability**
$0 - $5,000	610,755	No Tax Liability			No Tax Liability			N/A
$5,000 - $10,00	445,740							N/A
$10,000 - $15,000	417,450	$41.3	$99	0.4%	$31.9	$76	0.4%	-22.9%
$15,000 - $20,000	384,150	$85.4	$222	0.8%	$64.7	$169	0.8%	-24.2%
$20,000 - $40,000	1,208,752	$838.1	$693	7.8%	$652.6	$540	7.6%	-22.1%
$40,000 - $80,000	1,251,531	$2,396.9	$1,915	22.4%	$1,910.7	$1,527	22.3%	-20.3%
$80,000 - $100,000	308,777	$1,080.5	$3,499	10.1%	$865.7	$2,804	10.1%	-19.9%
$100,000 - $200,000	443,163	$2,609.9	$5,889	24.4%	$2,097.1	$4,732	24.5%	-19.6%
More than $200,000	144,222	$3,638.0	$25,225	34.0%	$2,929.2	$20,310	34.3%	-19.5%
Total	5,214,540	$10,690.0	$2,050	100.0%	$8,552.0	$1,640	100.0%	-20.0%

*Hypothetical incomes are assumed to contain no business or pass through investment income.

**Base data for this simulation is TY10. Above simulation assumes income distributions in TY15 are roughly equivalent to those in TY10 filing data grown to estimated TY12 income levels.

APPENDIX C – SALES AND USE TAX (STATE AND LOCAL TAXES)

The Changing Composition of U.S. Consumption Spending, 1935-2012						
Amounts in billions of dollars						
	1935	1955	1975	1990	2000	2012
Personal consumption expenditures	$55.9	$258.8	$1,033.8	$3,835.5	$6,830.4	$11,119.5
Goods	$31.6	$147.4	$491.3	$1,491.3	$2,459.1	$3,781.8
Services	$24.3	$111.4	$542.5	$2,344.2	$4,371.2	$7,337.7
Goods % of PCE	56.5%	57.0%	47.5%	38.9%	36.0%	34.0%
Services % of PCE	43.5%	43.0%	52.5%	61.1%	64.0%	66.0%

Table Revised (2012 Column) February 12, 2013

State and Local Sales and Use Tax - Impact of Rate Reductions at Different Household Income Levels			
	$40,000 income	$70,000 income	$100,000 income
State sales tax			
Estimated sales tax: current tax base and current state tax rates	$689	$1,100	$1,317
Estimated sales tax: current tax base and 5.0% tax rate	$626	$1,000	$1,198
Estimated reduction in state sales tax	-$63	-$100	-$120
Local sales tax			
Estimated sales tax: current tax base and current avg local tax rate (1.3%)	$163	$260	$311
Estimated sales tax: current tax base and assumed local tax rate (1.0%)	$125	$200	$240
Estimated reduction in state & local sales tax	-$38	-$60	-$72
State & local sales tax			
Estimated sales tax: current tax base and current tax rates	$851	$1,360	$1,629
Estimated sales tax: current tax base and revised tax rates	$751	$1,200	$1,437
Estimated reduction in state & local sales tax	-$100	-$160	-$192
Current state & local sales tax as % of income	2.1%	1.9%	1.6%
Tax at current sales tax base and proposed rates as % of income	1.9%	1.7%	1.4%
Reduced state & local sales tax as % of income	0.3%	0.2%	0.2%

Appendix C - Sales and Use Tax (State and Local Taxes) - Page 2

Estimated Ohio purchases of services proposed to be taxed, and state & local sales tax paid on such services: Impact on selected industries

Calculations using U.S. data in 2002 Input-Output tables produced by U.S. Department of Commerce Bureau of Economic Analysis

Ohio estimates are generated from national I-O amounts using Ohio/U.S. GDP shares by industry

(Figures in millions)

Note: Figures have not been projected beyond calendar year 2002

	Estimated Ohio purchases by indicated industries of services proposed to be taxed, and potential sales tax on such services (a)					
	Manufacturers	Retailers	Banks and other financial services (a)	Health care (b)	Accomodation and food service	Professional, scientific and technical services
Purchases of services proposed to be taxed	$9,691	$4,599	$2,318	$2,087	$1,779	$3,658
All other costs (wages, materials, etc.)	190,863	25,465	19,580	30,801	11,944	8,862
Total industry costs	$200,554	$30,064	$21,898	$32,888	$13,724	$12,520
Purchases of services proposed to be taxed as % total industry costs	4.8%	15.3%	10.6%	6.3%	13.0%	29.2%
Estimated sales tax on services proposed to be taxed (assumes average 6% tax rate: 5% state and 1% local)	$581	$276	$139	$125	$107	$219
Estimated new sales tax as % current total industry costs (d)	0.3%	0.9%	0.6%	0.4%	0.8%	1.8%

(a) The Ohio figures shown in this table are rough estimates. They have not been adjusted to reflect potential compliance issues, exempt transactions, and other factors that are expected to dilute tax collections. Therefore, the figures shown here do not constitute final estimates of the expanded services sales tax base and revenue from that expanded tax base. Since the taxable purchases estimates have not been adjusted downward for exempt transactions or non-compliance, they probably overstate the impact of the sales tax base expansion on industry costs.

(b) Includes all depository and nondepository credit institutions, and other financial activities.

(c) For this table, purchases by hospitals are excluded from services proposed to be taxed. This is because the majority of such facilities are IRC section 501(c)(3) entities whose purchases are exempt under Ohio sales tax law.

(d) This table reflects the potential "first-stage" effects from taxing business services, i.e., the sales tax charged to the purchaser.

Appendix C - Sales and Use Tax (State and Local Taxes) - Page 3

SALES AND USE TAX (LOCAL TAXES)

Proposed County and Transit Authority Tax Rates for September 1, 2013 through March 31, 2015

County	Tax Rate	County	Tax Rate
Adams	1.35%	Licking	1.20%
Allen	0.80%	Logan	1.10%
Ashland	1.00%	Lorain	0.60%
Ashtabula	0.80%	Lucas	1.00%
Athens	1.10%	Madison	1.00%
Auglaize	1.20%	Mahoning	0.80%
Belmont	1.20%	Marion	0.80%
Brown	1.35%	Medina	0.80%
Butler	0.60%	Meigs	1.35%
Carroll	0.90%	Mercer	1.20%
Champaign	1.20%	Miami	1.00%
Clark	1.20%	Monroe	1.20%
Clermont	0.80%	Montgomery	0.75%
Clinton	1.20%	Morgan	1.35%
Columbiana	1.20%	Morrow	1.35%
Coshocton	1.20%	Muskingum	1.20%
Crawford	1.20%	Noble	1.35%
Cuyahoga	0.80%	Ottawa	1.00%
Darke	1.20%	Paulding	1.20%
Defiance	0.80%	Perry	1.35%
Delaware	0.80%	Pickaway	1.20%
Erie	0.65%	Pike	1.20%
Fairfield	0.80%	Portage	0.80%
Fayette	1.20%	Preble	1.20%
Franklin	0.50%	Putnam	1.20%
Fulton	1.20%	Richland	1.00%
Gallia	1.00%	Ross	1.20%
Geauga	0.75%	Sandusky	1.20%
Greene	0.80%	Scioto	1.20%
Guernsey	1.20%	Seneca	1.20%
Hamilton	0.65%	Shelby	1.10%
Hancock	0.75%	Stark	0.40%
Hardin	1.35%	Summit	0.35%
Harrison	1.35%	Trumbull	0.80%
Henry	1.20%	Tuscarawas	0.80%
Highland	1.20%	Union	1.00%
Hocking	1.10%	Van Wert	1.20%
Holmes	0.80%	Vinton	1.35%
Huron	1.20%	Warren	0.65%
Jackson	1.20%	Washington	1.20%
Jefferson	1.20%	Wayne	0.60%
Knox	0.80%	Williams	1.20%
Lake	0.75%	Wood	0.75%
Lawrence	1.35%	Wyandot	1.20%

Transit Authority	Tax Rate
Greater Cleveland Regional Transit Authority	0.65%
Central Ohio Regional Transit Authority	0.30%
Laketran Transit Authority	0.20%
Metro Regional Transit Authority	0.35%
Miami Valley Regional Transit Authority	0.35%
Portage Area Regional Transit Authority	0.20%
Stark Area Regional Transit Authority	0.20%
Western Reserve Transit Authority	0.20%

SUMMARIZED TIMELINE FOR LOCAL RATE CHANGES

- September 2013: State sales tax base and rate changes take effect. Counties and transit authorities not permitted to pass resolution to change tax rates through June 2016. The new county & transit authority sales tax rates also take effect this month.
- December 2013: Counties and transit authorities will start receiving “guaranteed-growth” sales tax payments, equal to the greater of actual sales tax collections or a specified growth percentage. The guaranteed-growth payments will last for 19 months (December 2013 through June 2015). During the December 2013 to November 2014 period, counties and transit authorities will receive the greater of: an amount equal to 110% of what was received during such month of the prior year (December 2012-November 2013); an amount equal to prior-year’s tax collections multiplied by a growth percentage based on average percentage growth in the county or transit authority’s tax collections during the prior two years; or the county or transit authority’s sales and use tax collections.
- December 2014: Beginning this month and continuing through June 2015, the guaranteed-growth payments to counties and transit authorities will increase: they will receive at least 115% of the amount received during such month of the base year (December 2012-June 2013).
- January 2015: A set of recalibrated county and transit tax rates will be computed in this month. In January 2015 actual county sales tax data will finally be available for an entire year, providing a sufficient basis to recalibrate the tax rates such that the rates will produce revenues reasonably close to desired outcomes. The new rates will be based on dividing (1) the greater of 110% of the “base year” collections or the “base year” collections multiplied by three-year annual percentage growth factor by (2) computed taxable sales.
- April 2015: Recalibrated tax rates take effect.
- June 2015: Final month for guaranteed-growth payments.
- January 2016: A final recalibration of the county and transit sales tax rates will be computed.
- April 2016: Final recalibrated tax rates tax effect.
- July 2016: Counties and transit authorities permitted to change tax rates beginning this month.

Appendix D - Local Sales Tax Plan

<table>
<tr><th>Plan</th><th colspan="3">2013</th><th colspan="3">2014</th><th colspan="4">2015</th><th colspan="4">2016</th></tr>
<tr><th>Component</th><th>July</th><th></th><th>December</th><th>January</th><th></th><th>December</th><th>January</th><th>April</th><th>July</th><th>December</th><th>January</th><th>April</th><th>July</th><th>December</th></tr>
<tr><td>Rate Re-calculation</td><td colspan="3">Rate 1: (Rates are reduced to 0.60% to 1.45%, as provided in statute)</td><td colspan="3"></td><td colspan="4">Rate 2: (Target Revenue CY 2014/ computed taxable sales CY 2014) ODT Recalculates January 2015</td><td colspan="2">Rate 3: (Target Revenue CY 2015/ computed taxable sales CY 2015) ODT Recalculates January 2016</td><td colspan="2">Rate 4: Counties can Recalculate their rate after July 2016 following the same process</td></tr>
<tr><td>Rate in effect</td><td>Current (.75% to 2.25%)</td><td colspan="6">Rate 1: September 2013 until March 2015</td><td colspan="4">Rate 2: April 2015 until March 2016</td><td colspan="3">Rate 3: April 2016 until tbd?</td></tr>
<tr><td>Distribution</td><td colspan="2">Current Rates until November 2013</td><td colspan="6">Rate 1: December 2013 until June 2015</td><td colspan="4">Rate 2: July 2015 until June 2016</td><td colspan="2">Rate 3: July 2016 until TBD</td></tr>
<tr><td>Revenue Targets</td><td colspan="3"></td><td colspan="3">CY2014 Target = CY 2013 Distributions + Growth (10% Jan-Nov & 15% for December)(1)</td><td colspan="4">CY2015 Target = 105% of Jan-June 2014 target plus Actual July-December 2015 Distributions</td><td colspan="4"></td></tr>
<tr><td>State Guarantee</td><td colspan="2"></td><td colspan="3">Guarantee #1: 10% Growth December 2013 through November 2014 over previous 12 month distribution (or equal to (1) below)</td><td colspan="3">Guarantee #2: December 2014 through June 2015 payments will be at least 5% larger than December 2013 to June 2014 payments</td><td colspan="6">State Guarantee Payments End July 2015</td></tr>
</table>

Notes:

(1) An enhanced revenue target is allowed for the relatively few number of counties that experienced average annual revenue growth in excess of 10% during the two years preceding the changes. For such counties, the revenue target is based on their average annual growth rate instead of the 10% growth rate

Appendix E - Net Impact of Tax Reform

Tax Reform Package Scoring - All Funds			
Income Tax	FY 2014	FY 2015	FY 2016
Eliminate deduction for dependents on two returns (stop "double-dipping")	$3.8	$3.8	$3.8
Deduction for gambling losses - repeal	$30.0	$30.0	$30.0
Small business tax relief: 50% exclusion for up to $750,000 of income	($647.5)	($624.8)	($617.4)
Income tax rate reductions for all 9 brackets: 7.5%, 15%, 20% - basic loss due to liability change	($729.0)	($1,524.0)	($2,138.0)
Income tax rate reductions for all 9 brackets: 7.5%, 15%, 20% - loss due to withholding changes (cuts in Jul-2013, Jul-2014, Jan-2015)	($315.0)	($553.0)	($12.0)
Total income tax impacts	**($1,657.7)**	**($2,668.0)**	**($2,733.6)**
Sales and Use Tax (Increases shown at 5.0% tax rate)			
Explicitly subject digital goods and services to sales tax	$15.0	$15.0	$15.0
Repeal exemption for magazine subscriptions	$7.4	$7.5	$7.5
Impose sales tax on broad categories of services at new 5% state tax rate	$1,921.4	$2,652.0	$2,763.4
Detail			
Transportation services (intrastate)	$190.5	$263.0	$274.0
Information services - motion picture production, cable broadcasting, Internet publishing, etc.	$260.8	$360.0	$375.1
Financial services fee income (no interest income); insurance-related services (excluding premiums); and real estate services (lessors of nonresidential buildings; agents, brokers and managers; appraisers)	$423.1	$584.0	$608.5
Legal and accounting services	$180.4	$249.0	$259.5
Architectural, engineering, and design services (including computer systems design); and other professional services (management consulting, scientific research, advertising, marketing, lobbying, etc.)	$478.9	$661.0	$688.8
Administrative and support services (collection agencies, credit rating services, travel agencies, etc.); waste management and remediation services	$231.8	$320.0	$333.4
Arts, entertainment, and recreation	$61.6	$85.0	$88.6
Miscellaneous other services (e.g. parking lots and garages, coin operated laundries, etc.)	$40.6	$56.0	$58.4
Adjustment for non-profit services	$53.6	$74.0	$77.1
Local sales tax increase due to combined impacts of base broadening and rate reductions. This is the additional amount borne by taxpayers, not the state subsidy payments	$50.0	$70.0	$73.0
State sales tax rate reduction from 5.5% to 5.0% on currently taxed goods and services	($621.4)	($875.5)	($917.0)
Total state and local sales and use tax impacts	**$1,372.4**	**$1,869.0**	**$1,941.9**
Severance Tax			
Create new severance tax rate structure for products from horizontal wells: oil, natural gas (methane), natural gas liquids	**$45.0**	**$155.0**	**$305.0**
Net Impact of All Provisions	**($240.3)**	**($644.0)**	**($486.7)**
State-only Impact	**($290.3)**	**($714.0)**	**($559.7)**
State GRF Impact	**($280.5)**	**($690.0)**	**($540.9)**

Appendix F - Sales taxability of services

Governor John R. Kasich
JOBS Budget 2.0
Sales taxability of services

The following spreadsheet compares the taxability of services before and after Jobs Budget 2.0. The services listed here are services used in a 2007 survey on sales taxation of services among the states by the Federation of Tax Administrators (FTA) and additional services reflected in the *North American Industry Classification System* (NAICS) classifications. The spreadsheet is for illustrative purposes only. It does not constitute a legal opinion. Each statutory exemption has specific requirements that must be met in order to qualify for exemption. The cited statutory exemption applies only if the taxpayer meets all the requirements set forth in the referenced statute.

Legend

E = Exempt from taxation

Gray = Remains exempt from sales tax

Blue = Service already subject to sales tax

	Before	After	Legislation	Current law (R.C.)	*Proposed law (R.C.)
State Sales Tax Rate	5.50%	5.00%			

Services currently subject to sales taxation

900 Number services (calls to 900 numbers)	5.50%	5.00%	H.B. 298 (1991)	5739.01(B)(3)(i)	5739.01(X)
Aircraft rental to individual pilots, long term (without operator)	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Aircraft rental to individual pilots, short term (without operator)	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Armored car services	5.50%	5.00%	H.B. 298 (1991)	5739.01(B)(3)(h)	5739.01(X)
Auto service	5.50%	5.00%	H.B. 694 (1981)	5739.01(B)(3)(c)	5739.01(X)
Automotive road service and towing services	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(3)(s)	5739.01(X)
Automotive storage	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(9)	5739.01(X)
Automotive washing and waxing	5.50%	5.00%	H.B. 694 (1981)	5739.01(B)(3)(c)	5739.01(X)
Bulldozers, draglines and const. mach., long term (without operator)	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Bulldozers, draglines and const. mach., short term (without operator)	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Carpet and upholstery cleaning	5.50%	5.00%	H.B. 904 (1993)	5739.01(B)(3)(j)	5739.01(X)
Cellular telephone services	5.50%	5.00%	S.B. 143 (2002)	5739.01(B)(3)(f)	5739.01(X)
Cold storage	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(9)	5739.01(X)

Appendix F - Sales taxability of services - Page 2

Commercial linen supply (rental)	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Custom fabrication labor	5.50%	5.00%	H.B. 694 (1937)	5739.01(B)(5)	5739.01(B)(7)
Data processing services (only if used in business)	5.50%	5.00%	H.B. 291 (1983)	5739.01(B)(3)(e)	5739.01(X)
Diaper service	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(3)(d)	5739.01(X)
Employment agencies	5.50%	5.00%	H.B. 904 (1993)	5739.01(B)(3)(l)	5739.01(X)
Exterminating (includes termite services)	5.50%	5.00%	H.B. 904 (1993)	5739.01(B)(3)(m)	5739.01(X)
Fur storage	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(9)	5739.01(X)
Garment services (altering & repairing)	5.50%	5.00%	1935	5739.01(B)(3)(a)	5739.01(X)
Health, recreation, sports clubs	5.50%	5.00%	H.B. 904 (1993)	5739.01(B)(3)(n)+(o)	5739.01(X)
Heating oil (other than motor vehicle fuel)	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Hotels, motels, lodging houses	5.50%	5.00%	S.B. 376 (1959)	5739.01(B)(2)	5739.01(B)(2)
Household goods storage	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(9)	5739.01(X)
Information services (only if used in business)	5.50%	5.00%	H.B. 291 (1983)	5739.01(B)(3)(e)	5739.01(X)
Installation charges - other than seller of goods	5.50%	5.00%	H.B. 694 (1981)	5739.01(B)(3)(b)	5739.01(X)
Installation charges by persons selling property	5.50%	5.00%	H.B. 694 (1981)	5739.01(B)(3)(b)	5739.01(X)
Internet Service Providers-Dialup (only if used in business)	5.50%	5.00%	H.B. 291 (1983)	5739.01(B)(3)(e)	5739.01(X)
Internet Service Providers-DSL or other broadband (only if used in busine	5.50%	5.00%	H.B. 291 (1983)	5739.01(B)(3)(e)	5739.01(X)
Interstate telephone & communications (subject to sourcing rules)	5.50%	5.00%	H.B. 171 (1987)	5739.01(B)(3)(f)	5739.01(X)
Intrastate chartered flights (with pilot)	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(3)(r)	5739.01(B)(5)
Intrastate telephone & communications	5.50%	5.00%	H.B. 171 (1987)	5739.01(B)(3)(f)	5739.01(X)
Intrastate transportation of persons	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(3)(r)	5739.01(X)
Labor charges - repairs other tangible property	5.50%	5.00%	H.B. 694 (1981)	5739.01(B)(3)(a)	5739.01(X)
Labor charges - repairs to intrastate vessels	5.50%	5.00%	H.B. 694 (1981)	5739.01(B)(3)(a)	5739.01(X)
Labor charges on repairs delivered under warranty	5.50%	5.00%	H.B. 694 (1981)	5739.01(B)(3)(a)	5739.01(X)
Labor charges on repairs to motor vehicles	5.50%	5.00%	H.B. 694 (1981)	5739.01(B)(3)(a)	5739.01(X)
Labor on radio/TV repairs; other electronic equip.	5.50%	5.00%	H.B. 694 (1981)	5739.01(B)(3)(a)	5739.01(X)
Landscaping services (including lawn care)	5.50%	5.00%	H.B. 298 (1991)	5739.01(B)(3)(g)	5739.01(X)
Laundry and dry cleaning services, non-coin op	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(3)(d)	5739.01(X)
Limousine service (with driver)	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(3)(r)	5739.01(B)(5)
Long term automobile lease (without operator)	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Mainframe computer access and processing serv. (only if used in business)	5.50%	5.00%	H.B. 291 (1983)	5739.01(B)(3)(e)	5739.01(X)
Maintenance and janitorial services	5.50%	5.00%	H.B. 904 (1993)	5739.01(B)(3)(j)	5739.01(X)
Marina Service (dry docking, storage, cleaning, repair)	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(9)	5739.01(X)
Massage services (without medical prescription)	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(3)(q)	5739.01(X)

Appendix F - Sales taxability of services - Page 3

Membership fees in private clubs	5.50%	5.00%	H.B. 904 (1993)	5739.01(B)(3)(o)	5739.01(X)
Mini storage	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(9)	5739.01(X)
Online data processing services (only if used in business)	5.50%	5.00%	H.B. 291 (1983)	5739.01(B)(3)(e)	5739.01(X)
Personal care services	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(3)(q)	5739.01(X)
Personal property, long term (generally)	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Personal property, short term (generally)	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Photo finishing	5.50%	5.00%	S.B. 376 (1959)	5739.01(B)(4)	5739.01(X)
Photocopying services	5.50%	5.00%	S.B. 376 (1959)	5739.01(B)(4)	5739.01(X)
Printing	5.50%	5.00%	S.B. 376 (1959)	5739.01(B)(4)	5739.01(X)
Private investigation (detective) services	5.50%	5.00%	H.B. 298 (1991)	5739.01(B)(3)(h)	5739.01(X)
Rental of hand tools to licensed contractors	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Rental of video tapes for home viewing	5.50%	5.00%		5739.01(B)(1)	5739.01(B)(1)
Repair labor, generally	5.50%	5.00%	H.B. 694 (1981)	5739.01(B)(3)(a)	5739.01(X)
Repair material, generally	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Satellite TV & radio (direct to consumers)	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(3)(p)	5739.01(X)
Security services	5.50%	5.00%	H.B. 298 (1991)	5739.01(B)(3)(h)	5739.01(X)
Service contracts sold at the time of sale of TPP	5.50%	5.00%	H.B. 298 (1991)	5739.01(B)(7)	5739.01(X)
Shoe repair	5.50%	5.00%	1935	5739.01(B)(3)(a)	5739.01(X)
Short term automobile rental (without operator)	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Sign construction and installation	5.50%	5.00%	1935	5739.01(B)(3)(b)	5739.01(X)
Software - pre-written	5.50%	5.00%	Administrative rule	5739.01(B)(1)	5739.01(B)(1)
Software - pre-written & downloaded	5.50%	5.00%	Case law	5739.01(B)(3)(e)	5739.01(X)
Swimming pool cleaning & maintenance	**5.50%	5.00%	H.B. 904 (1993)	5739.01(B)(3)(j)	5739.01(X)
Tanning parlors	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(3)(q)	5739.01(X)
Taxi operations	5.50%	5.00%	H.B. 95 (2003)	5739.01(B)(3)(r)	5739.01(B)(5)
Taxidermy	5.50%	5.00%	1935	5739.01(B)(1)	5739.01(B)(1)
Temporary help agencies	5.50%	5.00%	H.B. 904 (1993)	5739.01(B)(3)(k)	5739.01(X)
Tire recapping and repairing	5.50%	5.00%	1935	5739.01(B)(3)(a)	5739.01(X)
Window cleaning	5.50%	5.00%	H.B. 904 (1993)	5739.01(B)(3)(j)	5739.01(X)

Services subject to exemptions including health and well-being

Adult and child day care services	E	E			5739.01(X)(6)
Carpentry, painting, plumbing and similar trades (real property)	E	E			5739.01(X)(3)
Consumer lease/rental of consumer's primary residence	E	E			5739.01(X)(4)

Appendix F - Sales taxability of services - Page 4

Custom meat slaughtering, cutting and wrapping	E	E			5739.01(B)(42)(n)
Dentists	E	E			5739.01(X)(1)
Electricity	E	E			5739.02(B)(7)
Food storage	E	E			Ohio Const. XII § 3
Funeral services	E	E			5739.01(X)(11)
Interstate air courier (billed in-state)	E	E			5739.02(B)(10)
Labor - repairs or remodeling of real property	E	E			5739.01(X)(3)
Labor - repairs to commercial fishing vessels	E	E			5739.02(B)(42)(d)
Labor charges - repairs to interstate vessels	E	E			5739.01(B)(10)
Labor charges on repair of aircraft	E	E			5739.02(B)(49)
Labor charges on repairs to railroad rolling stock	E	E			5739.02(B)(14)
Local transit (intra-city) buses	E	E		5739.01(B)(3)(r)	5739.01(B)(5)
Medical and health care services	E	E			5739.01(X)(1)
Medical test laboratories	E	E			5739.01(X)(1)
Metal, non-metal and coal mining services	E	E			5739.01(X)(8)
Natural gas (sold by public utility)	E	E			5739.02(B)(7)
Nursing services out-of-hospital	E	E			5739.01(X)(1)
Oil field services	E	E			5739.01(X)(8)
Personal instruction (dance, golf, tennis, etc.)	E	E			5739.01(X)(2)
Physicians	E	E			5739.01(X)(1)
Preschool through twelve, post-secondary, and tutoring	E	E			5739.01(X)(2)
Radio & television, national advertising	E	E			5739.02(B)(10)
Real property construction services	E	E			5739.01(X)(3)
Residential trash pick-up and disposal	E	E			5739.01(X)(9)
Seismograph & geophysical services	E	E			5739.01(X)(8)
Services used directly in producing oil and gas	E	E			5739.01(X)(8)
Social assistance services	E	E			5739.01(X)(7)
Soil prep., custom baling, other ag. services	E	E		5739.02(B)(42)(n)	5739.02(B)(42)(n)
Transactions by which consumer obtains insurance	E	E			5739.01(X)(5)
Typesetting & platemaking for the print trade	E	E		5739.02(B)(42)(f)	5739.02(B)(42)(f)
Veterinary services (livestock)	E	E		5739.02(B)(42)(n)	5739.02(B)(42)(n)
Water (including sewer)	E	E			5739.02(B)(7)
Water well drilling (real property)	E	E			5739.01(X)(3)

Appendix F - Sales taxability of services - Page 5

Services added as taxable services

Accounting and bookkeeping	E	5.00%			5739.01(X)
Admission to cultural events	E	5.00%			5739.01(X)
Admission to professional sports events	E	5.00%			5739.01(X)
Admission to school and college sports events	E	***5.00%			5739.01(X)
Advertising agency fees (other than ad placement)	E	5.00%			5739.01(X)
Amusement park admission & rides	E	5.00%			5739.01(X)
Architectural, engineering, and related services	E	5.00%			5739.01(X)
Attorneys	E	5.00%			5739.01(X)
Bail bond fees	E	5.00%			5739.01(X)
Billiard parlors	E	5.00%			5739.01(X)
Books - downloaded	E	5.00%			5739.01(B)(6)
Bowling alleys	E	5.00%			5739.01(X)
Cable TV services	E	5.00%			5739.01(X)
Call center	E	5.00%			5739.01(X)
Check & debt collection	E	5.00%			5739.01(X)
Circuses and fairs -- admission and games	E	5.00%			5739.01(X)
Coin operated video games	E	5.00%			5739.01(X)
Commercial art and graphic design	E	5.00%			5739.01(X)
Credit information, credit bureaus	E	5.00%			5739.01(X)
Credit rating svc	E	5.00%			5739.01(X)
Cutting, coloring, styling of hair	E	5.00%			5739.01(X)
Data mining services	E	5.00%			5739.01(X)
Dating services	E	5.00%			5739.01(X)
Debt counseling	E	5.00%			5739.01(X)
Fishing and hunting guide services	E	5.00%			5739.01(X)
Horse boarding and training	E	5.00%			5739.01(X)
Insurance services (insurance policy purchases remain exempt under 5739.01(X)(5))	E	5.00%			5739.01(X)
Interior design and decorating	E	5.00%			5739.01(X)
Intrastate courier service	E	5.00%			5739.01(X)
Investment counseling	E	5.00%			5739.01(X)
Land surveying	E	5.00%			5739.01(X)
Laundry and dry cleaning services, coin-op	E	5.00%			5739.01(X)

Appendix F - Sales taxability of services - Page 6

Legal services	E	5.00%			5739.01(X)
Loan broker fees	E	5.00%			5739.01(X)
Lobbying and consulting	E	5.00%			5739.01(X)
Magazine subscriptions	E	5.00%			5739.01(X)
Mailbox rentals	E	5.00%			5739.01(X)
Mailroom services	E	5.00%			5739.01(X)
Marine towing service (incl. tugboats)	E	5.00%			5739.01(X)
Marketing	E	5.00%			5739.01(X)
Movies/digital Video - downloaded	E	5.00%			5739.01(B)(6)
Music - downloaded	E	5.00%			5739.01(B)(6)
Other electronic goods - downloaded	E	5.00%			5739.01(B)(6)
Packing and crating	E	5.00%			5739.01(X)
Pari-mutuel racing events.	E	5.00%			5739.01(X)
Parking lots & garages	E	5.00%			5739.01(X)
Pet grooming	E	5.00%			5739.01(X)
Pinball and other mechanical amusements	E	5.00%			5739.01(X)
Process server fees	E	5.00%			5739.01(X)
Property sales agents (real estate or personal)	E	5.00%			5739.01(X)
Public relations, management consulting	E	5.00%			5739.01(X)
Real estate management fees (rental agents)	E	5.00%			5739.01(X)
Real estate title abstract services	E	5.00%			5739.01(X)
Refuse collection (industrial)	E	5.00%			5739.01(X)
Rental of films and tapes by theaters	E	5.00%			5739.01(X)
Sales of advertising time or space:					
Billboards	E	5.00%			5739.01(X)
Magazine	E	5.00%			5739.01(X)
Newspaper	E	5.00%			5739.01(X)
Radio & television, local advertising	E	5.00%			5739.01(X)
Secretarial and court reporting services (excludes temporary hiring)	E	5.00%			5739.01(X)
Service charges of banking institutions	E	5.00%			5739.01(X)
Software - custom programs - programming	E	5.00%			5739.01(X)
Software - modifications to pre-written programs	E	5.00%			5739.01(X)
Sound recording	E	5.00%			5739.01(X)
Stenographic services	E	5.00%			5739.01(X)

Appendix F - Sales taxability of services - Page 7

Tax return preparation	E	5.00%			5739.01(X)
Telemarketing services on contract	E	5.00%			5739.01(X)
Telephone answering service	E	5.00%			5739.01(X)
Test laboratories (excluding medical)	E	5.00%			5739.01(X)
Tickertape reporting (financial reporting)	E	5.00%			5739.01(X)
Trailer parks - overnight	E	5.00%			5739.01(X)
Travel agent services	E	5.00%			5739.01(X)

*Sales tax is imposed on services under proposed R.C. 5739.01(B)(3) and proposed R.C. 5739.01(X) defines "service."

**Indoor swimming pool cleaning and maintenance is currently taxable.

***R.C. 5739.02(B)(9)(a) + (b) concerns exemptions for sales of certain services by churches, charities, and school organizations that will continue under proposed law.

Corrected and Reformatted: February 13, 2013