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OHIO LEGISLATIVE SERVICE COMMISSION

Office of Research and Drafting

Legislative Budget Office

S.B. 33
134th General Assembly

Final Fiscal Note & Local Impact Statement

Click here for S.B. 33's Bill Analysis

Primary Sponsors: Sens. Hottinger and Brenner

Local Impact Statement Procedure Required: Yes

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Highlights

- Expanding the applicability of an existing personal income tax (PIT) deduction for the state-sponsored college savings plan to include investment offerings of other states would reduce PIT revenue beginning in FY 2024, when taxpayers file income tax returns for tax year 2023.
- Two other states, Kansas and Montana, enacted similar legislation, which increased the number of tax returns claiming their respective state tax deductions by about 50%. A similar increase in Ohio would decrease annual GRF tax receipts by $9.9 million or more, depending on Ohio taxpayers' behavior. However, it remains unclear whether the experiences in those two states can be generalized to Ohio. A third state, Missouri, enacted analogous legislation in 2008, but does not have taxpayer data to enable an evaluation of the behavioral effect.
- The GRF would bear 96.68% of any PIT revenue loss starting in FY 2024 under current law, while the Local Government Fund and Public Library Fund would each bear 1.66% of any such revenue loss.
- The bill modifies laws governing community reinvestment areas (CRAs) and the terms under which property may be exempted from taxation in these areas. Effects of the changes vary, with many tending to reduce costs for municipalities and counties establishing a CRA and to reduce revenues for school districts and other political subdivisions. The dollar amounts of most of these effects appear indeterminate.
- The bill eliminates a CRA fee, reducing revenue to a state fund, the Tax Incentives Operating Fund, by approximately $100,000 per year. This fund is used by the Department

of Development (DEV) to monitor economic development tax credits and CRA and enterprise zone designations.

- The bill reduces the role of the state in the creation of new CRAs, which may reduce costs to the state.

Detailed Analysis

Personal income tax deduction

Continuing Ohio law allows a state income tax deduction for contributions to Ohio's 529 plan, which is a tax-preferred education savings program administered by the Ohio Tuition Trust Authority (OTTA). The bill extends the deduction so that it would also apply to contributions to any 529 plan established by another state or by an educational institution beginning with tax year (TY) 2023.

A 529 college savings program is a state-operated investment plan named after the section of the federal Internal Revenue Code (IRC) that specifies the various tax advantages of participating in the program. These tax advantages include tax-free growth while the value of the account accumulates, and withdrawals that are exempt from both federal and state income taxes if the distributions are used to pay for qualified higher education expenses. The qualified expenses include tuition, room and board, and any other fees or costs that are required for enrollment or attendance at the college or university. Funds invested in the CollegeAdvantage Savings Plan, which is the 529 savings plan administered by OTTA, may be used at any college in the country.

Federal tax law changes made in the Tax Cuts and Jobs Act (TCJA), H.R. 1 of the 115th Congress, permitted 529 account owners to use distributions from 529 plans to pay public or private elementary and secondary school ("K-12") tuition and related educational expenses. Annual withdrawals for K-12 expenses were capped at $10,000 per student by the TCJA. S.B. 22 of the 132nd General Assembly conformed state law to the federal government's expanded definition of eligible 529 plan expenditures. Consequently, taxpayers may claim a personal income tax (PIT) deduction on their state tax return in TY 2018 and years thereafter for contributions supporting previously ineligible education expenses.

Fiscal effect of PIT deduction modification

A handful of states permit a state income tax deduction on behalf of contributions to other states' 529 plans. LBO research indicates that Kansas, Missouri, and Montana enacted laws with provisions analogous to S.B. 33, which expanded their state's eligibility to all qualified tuition savings plans authorized by section 529 of the IRC. On the other hand, Arizona, Arkansas, Minnesota, and Pennsylvania permit deductions for contributions to other states' 529 plans, but multistate eligibility was enacted at the inception of their states' respective tax deduction policies. Therefore, the behavioral response of taxpayers to the bill's policy change can only be observed from Kansas (TY 2007), Missouri (TY 2008), and Montana (TY 2013) beginning with the year their respective state laws changed. LBO contacted officials in Missouri about their income tax data, but they recently implemented new database software and could not provide detailed statistics about their tax deduction claims in prior years.

State Income Tax Deductions Claimed for 529 College Savings Plan Contributions, As Reported by Other States Enacting Legislation Similar to S.B. 33 of the 134th General Assembly		
	Kansas	Montana
Number of tax returns (three-year average) claiming deduction, prior to law change	13,890	2,113
Number of tax returns (three-year average) claiming deduction, after law change	21,100	3,300
Increase after law change	**7,210 (51.9%)**	**1,187 (56.2%)**

Note: Kansas only published state tax deduction statistics about 529 plan contributions for two years prior to changing its law to permit deductions for contributions to plans sponsored by other states.

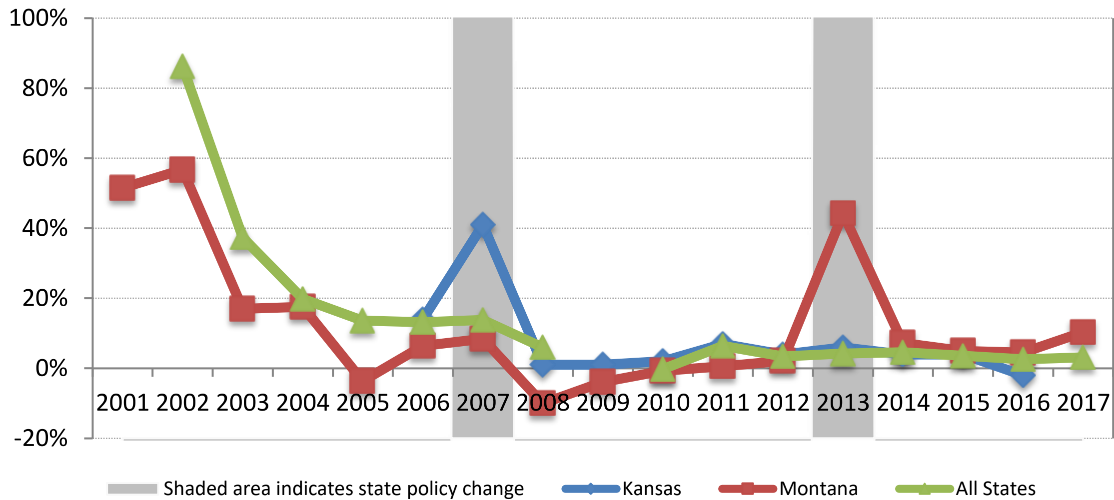
Prior to TY 2018, contributions to college savings plans could only be withdrawn without penalty for college tuition and other associated expenses. As mentioned above, the TCJA and S.B. 22 expanded the definition of eligible expenditures to include K-12 tuition. For this reason, the TY 2017 statistics may be the best baseline against which S.B. 33 should be estimated. In that year, PIT data shows that 114,103 tax returns claimed $334.6 million in deductions, or $2,932 per return. The TY 2017 returns were largely filed during FY 2018, reducing GRF receipts by $12.4 million due to the existing college savings plan deduction.[1]

If the experiences in Kansas and Montana were replicated in Ohio, S.B. 33 would spur an additional 59,228 tax returns to claim the college savings plan deduction. However, the college savings plan deduction was limited to $2,000 per beneficiary in TY 2017 whereas the current limit in continuing law is $4,000 per beneficiary. LBO previously estimated the annual GRF loss for the provision[2] that increased the contribution limit to $4,000 per beneficiary to be approximately $6.7 million. Therefore, the estimated annual revenue loss incurred for all tax deductible contributions to college savings plans is nearly $19.1 million per year. This estimate is fairly close to the most recent Tax Expenditure Report, which was released in February 2021, in which the Department of Taxation reports an estimated GRF revenue loss from the current deduction of $18.8 million in FY 2022. If S.B. 33 increases the number of tax returns by 52%, the bill could decrease GRF receipts by $9.9 million per year.

[1] Estimate according to the Tax Expenditure Report, which is released in conjunction with the executive budget proposal.

[2] Refer to the comparison document for H.B. 49 of 132nd General Assembly.

Annual Growth in Number of Tax Returns Claiming State Tax Deduction for 529 Contributions, as Compared to National Growth in Number of 529 Accounts



Note: "All states" number of 529 accounts collected prior to 2009 is not comparable due to change in methodology, from collegesavings.org/529-plan-data/.

Potential revenue losses could be higher depending on the behavioral response of those taxpayers that claim the college savings plan deduction for K-12 contributions after the enactment of the TCJA. Statistics concerning this behavioral response are not yet conclusive. It can take several years for a behavioral response to be widely adopted by targets of a broad-based tax incentive. If there is an interactive effect between the TCJA impact and the college savings behaviors spurred by S.B. 33, it may increase the PIT revenue loss beyond amounts estimated in this fiscal note.

Additional qualitative factors about Ohio's state-sponsored college savings plans are not explicitly incorporated in this revenue estimate. However, the experiences in Montana and Kansas may not be entirely comparable, as Ohio's CollegeAdvantage 529 Savings Plan is highly rated by independent analysts. Morningstar, which publishes research and recommendations for financial investments, annually evaluates college savings plans sponsored by states across the country. In its 2020 report, Morningstar "identified 35 best-in-class offerings, recognizing these programs with Analyst Ratings of Gold, Silver, or Bronze."[3] The CollegeAdvantage 529 Savings Plan issued by OTTA was among 11 plans to be rated "Silver," and only three plans earned the higher "Gold" rating. Neither Kansas nor Montana had plans rated as highly as Ohio. The implication for S.B. 33 is that Ohio taxpayers may not favor out-of-state plans much more than OTTA's offerings. Since Ohio's plan is highly rated and usable at any college in the country, the behavioral response to the bill may be diminished, as compared to experiences in Kansas and Montana.

The immediate beneficiaries of the bill may be those Ohio taxpayers that previously opened 529 accounts sponsored by other states. Taxpayers may have established these accounts

[3] morningstar.com/articles/1006084/the-top-529-college-savings-plans-of-2020.

when previously living in a different state or instead elected to contribute to other state-sponsored plans based on their individual preferences.

The bill first applies to TY 2023, so its fiscal effect will begin in FY 2024 once state income tax returns are filed. Under codified law, the GRF would bear 96.68% of any PIT revenue loss during fiscal years beginning July 1, 2023, while the Local Government Fund (LGF) and Public Library Fund (PLF) would each bear 1.66%.

Community reinvestment areas

Overview

A CRA is an economic development tool available to local governments. It is a geographic portion of a municipal corporation's territory or of the unincorporated part of a county, for which the legislative authority of the municipal corporation or county has adopted a resolution describing the boundaries of the area. The resolution must state that housing facilities or structures of historical significance are located in the area and new housing construction and repair of existing facilities or structures are discouraged. Historical or architectural significance, designated by the municipality or county, is based on age, rarity, architectural quality, or previous designation by a historical society, association, or agency.

Within the CRA, new residential, commercial, or industrial structures or the increased value of existing structures after remodeling began may be granted exemption from a percentage, up to 100%, of real property taxation for a specified number of years. For residential property, the exemption percentage and term are specified in the resolution creating the CRA. For commercial and industrial property, the exemption percentage and term are negotiated for each project. An owner of real property in a CRA may apply for tax exemption of the value of a new structure or of the increase in value of an existing structure after the start of remodeling. Commercial or industrial property owners pay a state application fee of $750 to be in a CRA.

Over 1,000 CRA identifying numbers are assigned, as indicated by data posted on the Department of Development's (DEV's) website. Whether all remain active is unclear. Use of CRAs is concentrated in the larger urban counties.

Fiscal effects of CRA modifications

School districts

A CRA tax exemption for commercial or industrial property may only be granted under continuing law if approved by the board of education of a school district with territory in the CRA, unless one or the other of two conditions is met. First, the school board may waive this right. Alternatively, approval is not needed if tax revenues for the property made partially tax exempt plus any payments to the school district equal or exceed a specified percentage of the amount that tax revenues would be in the absence of any exemption. In current law the percentage is 50%.

The bill would lower this percentage to 25%, i.e., school board approval is not needed if tax revenues plus any payment equal or exceed 25% of the amount of taxes if there were no exemption. This decrease would tend to make approval of tax exemption easier and might tend to increase tax revenue losses to school districts and other political subdivisions. The magnitude of such revenue losses would depend on future actions of municipal corporations and counties.

The bill amends a requirement in current law that municipalities share half of municipal income tax revenue from new employees at a commercial or industrial project in a CRA with the school district that has territory in the CRA, if the additional payroll of new employees is $1 million or more, increasing the threshold to $2 million and indexing the threshold for inflation.[4] This compensation is only required if the legislative authority establishing the CRA is unable to negotiate a compensation agreement with the school board. This change would tend to benefit municipal corporations and counties at the expense of school districts.

Limited home rule townships

The bill extends the authority to designate CRAs to townships that have adopted limited home rule government. Under current law, only a municipality or a county may designate an area within its jurisdiction as a CRA. In general, a township may become a limited home rule township, which grants it additional powers, if it has a township administrator, a population of at least 2,500 in its unincorporated territory, and a budget of at least $3.5 million. In some instances, voters must also approve its formation.

This change may result in exemption of additional areas from property taxes.

Elimination of CRA fees

The bill eliminates two CRA-related fees from the law. These fees pay for some of the administrative costs to local governments and to DEV in oversight of CRAs.

First, the bill repeals an annual fee payable by the property owner to the local government of 1% of taxes exempted, but no less than $500 or more than $2,500. However, the repealed section allows the legislative authority to reduce or waive the fee. So the repeal may reduce local fee income, though imposition of the fee currently appears to be discretionary for the local government creating the tax exemption.

Second, the bill repeals the authority for DEV to impose a state fee, currently set by rule at $750, on commercial and industrial property owners applying to join a CRA. The fee, under codified law, is determined by DEV based on the cost of administering the CRA Program, and is deposited in the Tax Incentives Operating Fund (Fund 5JR0). According to DEV, the eliminated CRA fee generated approximately $120,000 in revenue in FY 2020, and nearly $90,000 in each of FY 2018 and FY 2019. Fund 5JR0 is used to administer several tax credit programs, plus CRA and enterprise zone classifications.

Other fiscal effects

The bill reduces from five years to three years the wait required after discontinuation of a CRA commercial or industrial project before the project's owner becomes eligible for exemption in another CRA or in an enterprise zone. This change may increase revenue losses from tax exemptions.

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[4] Current law's threshold applicable to other, non-CRA exemptions remains unchanged by the bill at $1 million or more in employee payroll.

The bill eliminates a requirement that proposed CRAs must receive a determination from the Director of Development that the territory of the CRA is eligible for tax exemption prior to the legislative authority granting such exemptions. This change may reduce costs to the state.

The bill makes changes to required content and recipients of CRA annual reports. It also repeals a requirement that a municipal corporation or county notify DEV of zoning restrictions, instead providing this notice through the annual report. LBO expects little or no fiscal effect from these changes.

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