Revenues

The Legislative Budget Office (LBO) of the Legislative Service Commission expects slower tax revenue growth for the remainder of fiscal year 2001 with an acceleration in growth for fiscal years 2002 and 2003. This pattern of revenue growth is dependent on the pattern of economic growth. Our economic forecast assumes that the current economic slowdown will last for approximately the next six months (through the remainder of fiscal year 2001). The economy is expected to pick back up sometime during the middle of calendar year 2001 (the start of fiscal year 2002).

The table below summarizes our tax revenue forecasts and provides information on revenue growth. The forecasts of the personal income tax, the sales and use tax, the corporate franchise tax, and the public utilities taxes assume that the proposed freeze on the amounts deposited into and distributed from the three local government funds is enacted. This freeze is estimated to add $68.7 million to the GRF in fiscal year 2002 and $144.2 million in fiscal year 2003. The 2.0 percent rate of tax revenue growth for fiscal year 2001 is much lower than the 5.7 percent average rate of growth for the preceding four fiscal years.

GRF Tax Revenues

Estimate for FY 2001, Forecast for FY 2002-03

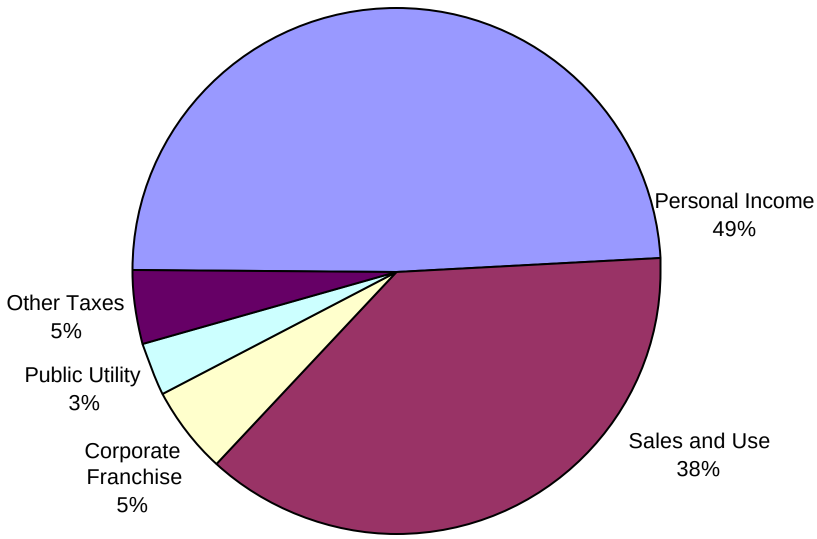
Dollar amounts in millions

	Tax Revenue			*Growth Rate*		
Revenue Source	**2001**	**2002**	**2003**	**2001**	**2002**	**2003**
Sales and Use	$6,041.1	$6,479.5	$6,844.3	2.2%	7.3%	5.6%
Personal Income	7,435.4	8,426.7	8,959.2	2.8%	13.3%	6.3%
Corporate Franchise	921.8	907.8	931.6	-4.9%	-1.5%	2.6%
Public Utility	653.1	551.4	571.1	1.7%	-15.6%	3.6%
Major Taxes	**$15,051.4**	**$16,365.4**	**$17,306.2**	**2.0%**	**8.7%**	**5.7%**
Foreign Insurance	247.4	242.4	242.6	-1.9%	-2.0%	0.1%
Domestic Insurance	90.2	104.1	115.6	2.3%	15.4%	11.0%
Business & Property	7.5	8.3	8.4	-13.8%	10.7%	1.2%
Cigarette	282.5	279.1	275.7	-1.8%	-1.2%	-1.2%
Alcoholic Beverage	56.3	58.0	59.6	1.8%	3.0%	2.8%
Liquor Gallonage	29.4	30.0	30.8	3.2%	2.0%	2.7%
Estate	160.0	95.5	60.6	14.3%	-40.3%	-36.5%
Other Taxes	**$873.3**	**$817.4**	**$793.3**	**1.5%**	**-6.4%**	**-2.9%**
Total Taxes	**$15,924.7**	**$17,182.8**	**$18,099.5**	**2.0%**	**7.9%**	**5.3%**

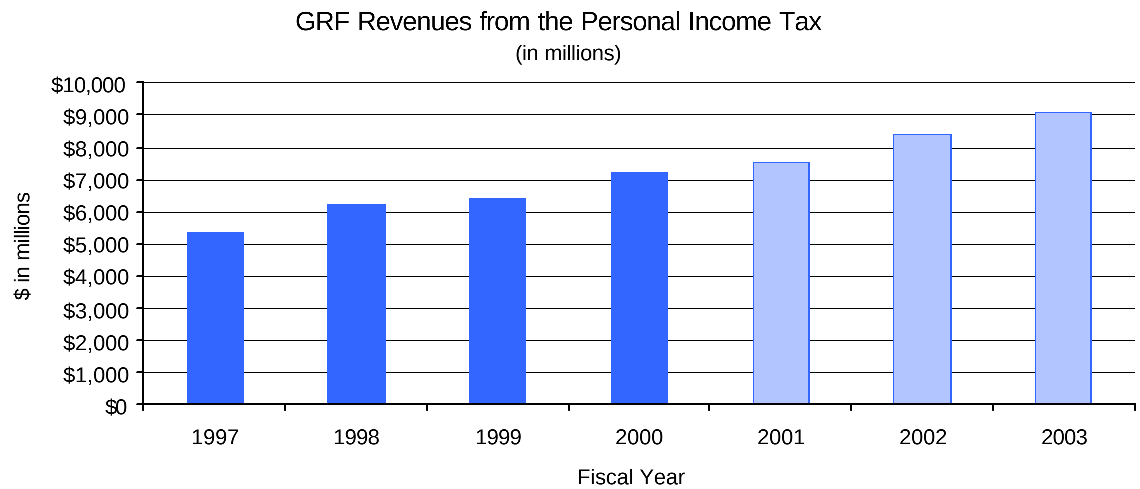
The GRF receives over 95 percent of its tax revenues from four taxes. The largest source is the personal income tax, which is forecasted to account for 49.3 percent of GRF tax revenues in the upcoming biennium. The sales tax is forecasted to account for 37.8 percent, the corporate franchise tax 5.2 percent, and public utilities taxes (the public utilities excise tax, the natural gas gross receipts tax, and the kilowatt hour tax) 3.2 percent. The chart below presents the distribution of GRF tax revenues by source for the upcoming biennium.

GRF Tax Revenues by Source

FY 2002-2003



Personal Income Tax



	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Personal Income	$5,382.3	$6,215.5	$6,416.8	$7,232.0	$7,435.4	$8,426.7	$8,959.2
	2.3%	*15.5%*	*3.2%*	*12.7%*	*2.8%*	*13.3%*	*6.3%*

The Personal Income Tax is levied on Ohio taxable income (the amount reported as federal adjusted gross income to the U.S. Internal Revenue Service plus or minus adjustments). After these adjustments are made, a taxpayer's tax liability before credits is obtained by applying Ohio's graduated tax rates to the taxpayer's Ohio taxable income. Certain credits may be subtracted from this amount to arrive at the taxpayer's final tax liability.

Major additions to FAGI in the determination of Ohio adjusted gross income include: state and local bond interest (except Ohio governments), federal bond interest exempt from federal tax but subject to state tax, and accumulation distribution from a complex trust. Major subtractions include: federal bond interest, disability and survivors' benefits included in FAGI, compensation earned in Ohio by residents of reciprocity states, social security and railroad retirement benefits included in FAGI, and state and municipal refunds.

Ohio taxable income is obtained by subtracting personal exemptions from Ohio adjusted gross income. Taxpayers may claim an exemption for the taxpayer, the taxpayer's spouse (if filing a joint return), dependent children, and others to whom the taxpayer provides support and claims on the taxpayer's federal return. For tax year 2000, the personal and dependent exemption is $1,100. This amount is indexed for inflation and is expected to increase each year.

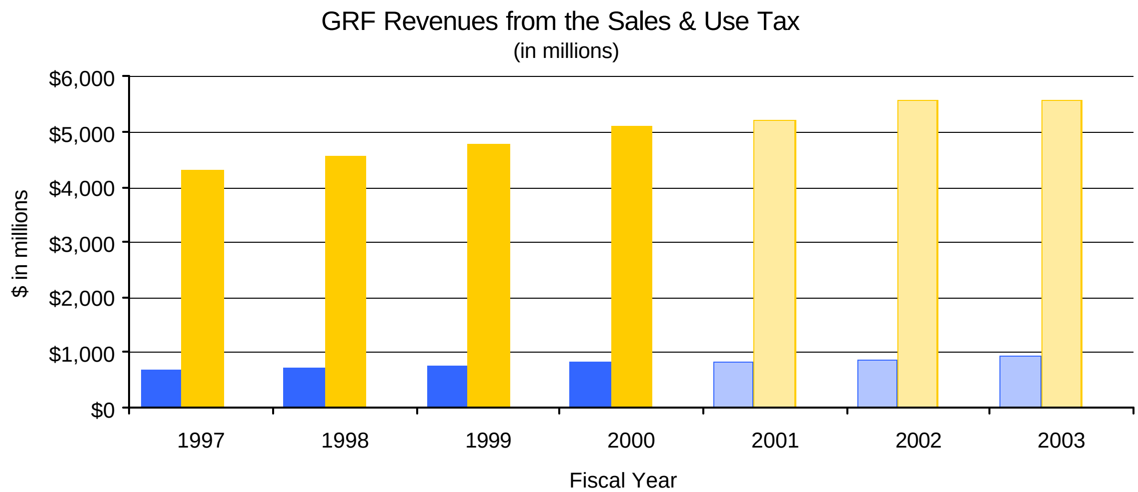
The taxpayer's tax liability before credits is obtained by applying graduated rates to the taxpayer's Ohio taxable income. Ohio's statutory tax rates range from 0.743 percent on the first $5,000 of Ohio taxable income to 7.5 percent on Ohio taxable income in excess of $200,000. These rates may be reduced by rate cuts paid for out of the Income Tax Reduction Fund (ITRF). The ITRF tax rebate mechanism is structured to give unanticipated surpluses back to taxpayers. Any rate reductions are largely the result of errors in forecasting revenues and spending, but underspending by state agencies that is not from forecasting errors is also a factor. For tax year 2000, $610.4 million is to be returned to taxpayers through a 6.929 percent rate cut. Approximately 85 percent ($518.8 million) of the reduction in tax revenue due to the rate cut will be felt in fiscal year 2001 with the remaining 15 percent ($91.6 million) impacting fiscal year 2002 revenues.

Major credits available to taxpayers include: the personal exemption credit of $20 per exemption, the senior citizen credit of $50 per return, the retirement income credit, the child and dependent care credit, various business credits, the displaced worker training credit, the political contribution credit, the adoption credit, and the joint filer credit for two working spouses (graduated based on income with a maximum credit of $650).

The revenue collected is disposed of as follows: 89.5 percent to the General Revenue Fund, 4.2 percent to the Local Government Fund, 0.6 percent to the Local Government Revenue Assistance Fund, and 5.7 percent to the Library and local Government Revenue Assistance fund.

The forecast of revenue is based mainly on expected growth in Ohio personal income. Adjustments were made to take into account temporary rate cuts, changes in the value of the personal and dependent exemption, and the effects of stock markets on employee compensation. We have not assumed any budget surplus for fiscal years 2001, 2002, and 2003, so we have not assumed any rate cuts for tax years 2001, 2002, and 2003. The forecasted revenues assume that the proposed freeze on the amounts deposited into and distributed from the three local government funds is enacted.

Sales and Use Tax



Sales & Use	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Auto	$673.7	$722.8	$760.4	$821.7	$815.5	$881.0	$926.4
	0.7%	*7.3%*	*5.2%*	*8.1%*	*-0.7%*	*8.0%*	*5.2%*
Non-Auto	$4,295.3	$4,542.7	$4,784.9	$5,092.0	$5,225.6	$5,598.5	$5,917.9
	5.5%	*5.8%*	*5.3%*	*6.4%*	*2.6%*	*7.1%*	*5.7%*
Total	$4,969.0	$5,265.5	$5,545.3	$5,913.7	$6,041.1	$6,479.5	$6,844.3
	4.8%	*6.0%*	*5.3%*	*6.6%*	*2.2%*	*7.3%*	*5.6%*

The state sales and use tax is levied at a rate of 5% on retail sales of tangible personal property, rental of some tangible personal property, and selected services. Major exemptions include: food for human consumption off the premises where sold; newspapers and magazine subscriptions sent by second class mail; motor fuel (taxed separately); sales of artificial and natural gas, electricity, and water when delivered through pipes, wires, or conduits; prescription drugs; property used primarily in manufacturing or used directly in mining or agriculture; and credit for trade-ins on new motor vehicles.

The revenue collected is disposed of as follows: 95.2% to the General Revenue Fund; 4.2% to the Local Government Fund; and 0.6% to the Local Government Revenue Assistance Fund.

For forecasting purposes, the tax is separated into two parts: Auto and Non-Auto. Auto includes revenue collected from the sale or use of automobiles and trucks. Non-auto includes all other sales and use tax collections. Taxes arising from auto leases are paid on a monthly basis during the lease period and are recorded under the non-auto tax, instead of the auto tax. As percentage of vehicles leased increases over the year, the auto tax will become more volatile.

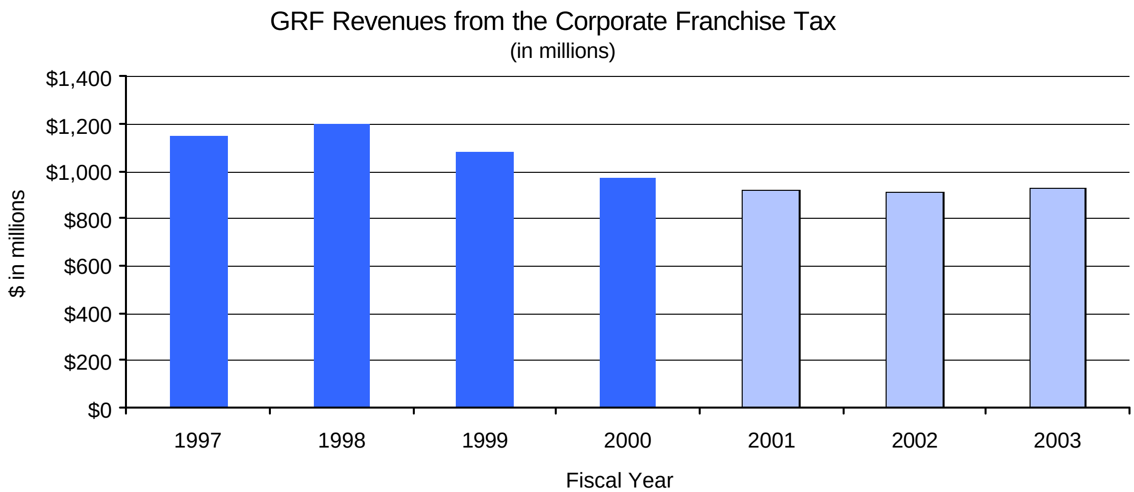
The forecast for the Sales and Use tax revenue is based primarily on expected growth in Ohio personal income. It shows a slow down in FY 2001 receipts with the auto portion of the sales tax declining. Growth will resume in FY 2002 and continue in FY

2003. The forecasted revenues assume that the proposed freeze on the amounts deposited into and distributed from the three local government funds is enacted.

Strong economic growth over the last few years has masked the rise of a phenomenon impacting the sales tax. As e-commerce has exploded, so have new concerns about the growing revenue loss induced by remote sales. Little empirical data exist on the key factors needed to calculate with precision associated revenue loss. A recent U.S. General Accounting Office (GAO) report indicates the magnitude of this uncertainty, the importance of developing better data about Internet commerce and understanding the limit of such data.[1]

[1] *Sales Taxes-Electronic Commerce Growth Presents Challenges; Revenue Losses Are Uncertain.* United States General Accounting Office Report to Congressional Requesters, June 2000. This report indicates that in 2000 State and local government losses from remote sales were between $108 and $375 million in Ohio.

Corporate Franchise Tax



	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Corporate Franchise	$1,150.8	$1,196.6	$1,084.1	$969.4	$921.8	$907.8	$931.6
	3.3%	*4.0%*	*-9.4%*	*-10.6%*	*-4.9%*	*-1.5%*	*2.6%*

The last two General Assemblies ushered major changes to the corporate franchise tax. Their effects will continue to be felt into the 2002-03 biennium. The franchise tax is becoming a less significant source of state revenue. More and more firms are taking advantage of alternative forms of business organization (such as the limited liability company), which are generally not subject to the corporate franchise tax. Instead, the owners of these “pass-through entities” pay the personal income tax on their share of the business net income. The trend in “un-incorporation” may continue. The Internal Revenue Service expects between CY2000 and CY2003 a 9-14 % increase in pass-through entities returns as opposed to a 3 percent increase in corporation returns.

LBO derives its forecasts of baseline corporate franchise tax (CFT) revenues from projections of U.S. corporate profits. Translating a corporate profits forecast into a franchise tax forecast is not straightforward because the dual base of the franchise tax (net worth or net income), the fact that corporations often have taxable years that do not coincide with calendar years, and corporations’ decisions on the timing and use of statutory tax credits. LBO has estimated from the historical data that the elasticity of franchise tax revenue with respect to U.S. corporate profits varies from year to year but averages less than 1. The average elasticity has been about 0.6 (that is, a 10 percent change in corporate profits produces a 6 percent change in tax revenue – possibly with a lag).

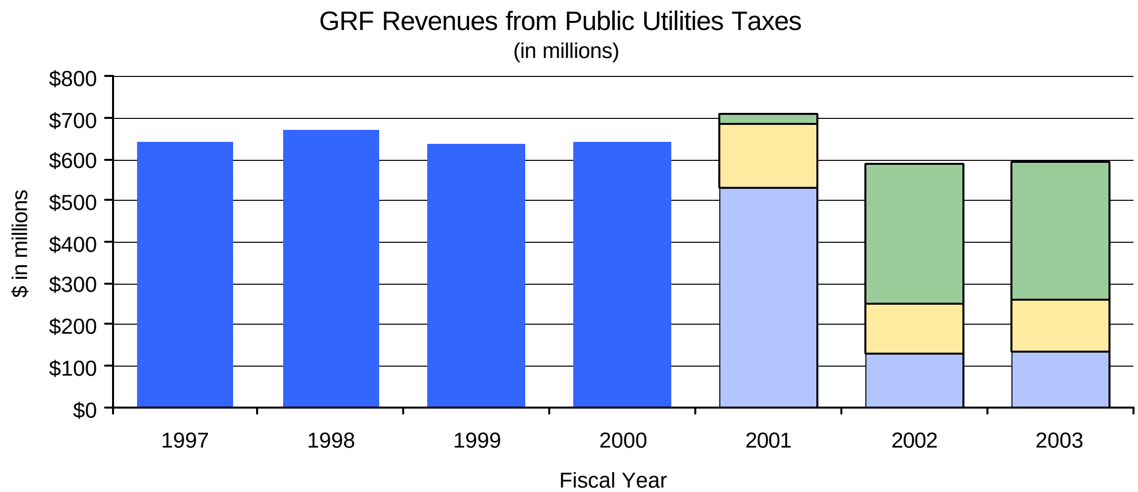
November 2000 estimates of the Governor’s Economic Advisory Council peg profit growth for calendar years 2001, 2002 and 2003 at 6.0 percent each year. Based on the elasticity estimates given above, Ohio corporate franchise tax revenues for fiscal years 2002 and 2003 are expected to move in the same direction, but with slightly lower magnitude. For example, the 0.6 elasticity estimate translates a 6.0 percent profit growth into a 3.6 percent growth in baseline revenues.

Corporate Franchise Tax Revenues (GRF only)

Fiscal Year	1999	2000	2001	2002	2003
Actual Revenues and Baseline	$1,084.1	$969.4	$1,049.7	$1,087.5	$1,126.6
Adjustments to Baseline			-$127.9	-$179.0	-$195.5
Estimated Revenue			$921.8	$908.5	$931.1
LGF Freeze				-$0.7	$0.5
Adjusted Revenue				$907.8	$931.6

The above table shows actual franchise tax revenue for FY 1999 and FY 2000, estimated revenue for FY2001, forecasted corporate franchise tax revenues for FY 2002-03 after taking into consideration previously enacted tax changes. The baseline is derived from the profit forecast and the elasticity estimate noted above. The results are then adjusted for the estimated impact of tax law changes. Adjustments to the baseline represent changes in the net worth and net income calculations, changes to the tax on financial institutions and the continuation of the investment tax credit and other credits. The forecasted revenues assume that the proposed freeze on the amounts deposited into and distributed from the three local government funds is enacted.

Public Utility Taxes

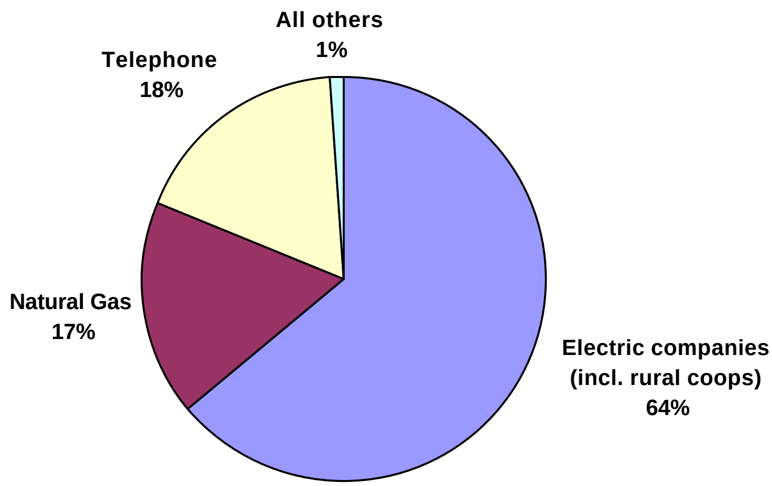


	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Public Utility Excise	$639.8	$673.0	$637.6	$642.1	$492.9	$96.9	$113.2
	2.9%	*5.2%*	*-5.3%*	*0.7%*	*-23.2%*	*-80.3%*	*16.8%*
Natural Gas Gross Receipts					$134.8	$100.2	$103.3
	xxx	*xxx*	*xxx*	*xxx*	*xxx*	*-25.7%*	*3.1%*
Kilowatt Hour					$25.4	$354.3	$354.7
	xxx	*xxx*	*xxx*	*xxx*	*xxx*	*1294.9%*	*0.1%*
Total	$639.8	$673.0	$637.6	$642.1	$653.1	$551.4	$571.2
	2.9%	*5.2%*	*-5.3%*	*0.7%*	*1.7%*	*-15.6%*	*3.6%*

The public utility excise tax – also known as the gross receipts tax – is a tax on the intrastate revenues of public utilities. The bulk of public utility excise tax revenues are derived from three types of utilities – electric companies, natural gas companies, and telephone companies. All three utilities are in various stages of restructuring – that is, moving from a regulation-based industry to a more competitive regime. In recognition of this restructuring process, the 123rd General Assembly made significant changes to the taxation of public utilities. H.B. 283 changed the way that the public utility excise tax on natural gas companies is calculated. S.B. 3 eliminated the public utility excise tax on electric companies and implemented a kilowatt-hour tax in its place. S.B. 287 made additional changes to the kilowatt-hour tax.

These changes first take effect in FY 2001 and are fully implemented in the FY 2002-2003 biennium. The traditional public utility excise tax still applies to local telephone companies (but not long-distance, wireless, or other telecommunications companies), pipeline companies, heating companies, waterworks and water transportation companies. In tax year 1999 electric companies and rural electric companies accounted for 64 percent of total certifications; natural gas companies accounted for an additional 17 percent. (See Chart 2.) Hence, the changes made in this biennium affect 82 percent of the public utility excise tax base. Telephone company receipts account for 96% of the remainder.

Chart 2 - 1999 Public Utility Excise Tax Certifications



As a result of these changes public utility tax revenues for FY 2001 through 2003 are composed of the following elements:

- Quarterly payments for the natural gas gross receipts tax beginning November 2001
- Final public utility excise tax payments of electric light companies and rural electric co-operatives for FY 2001 (plus the reconciliation payment in FY 2002)
- Kilowatt-hour tax payments of electric companies beginning in June 2001 and
- Public utility excise tax payments for telephone companies, pipeline companies, heating companies, waterworks and water transportation companies for FY 2001 through 2003

Revenues from each of these sources are discussed separately below.

Natural Gas Gross Receipts Tax

H.B. 283 law changes

H.B. 283 exempted natural gas companies from the existing public utility excise tax and subjected them to a new gross receipts tax at the same tax rate of 4.75%. The companies were moved from the prior definitions of "privilege year" and "tax year." Beginning FY 2001 they began filing quarterly returns and making quarterly payments for the previous calendar quarter. (Small companies – i.e., those with annual tax liability of less than $325,000 – will file annual returns and make annual payments beginning in February 2001.) Companies began paying the revised tax in November of 2000. That month's revenue of $29.6 million covered the gross receipts for the 5-month period from

May 2000 through September 2000. Subsequent payments will be based on a company's gross receipts over a 3-month period.

H.B. 283 ended the natural gas company payments of the “annual basis” tax with the payments associated with the May 1999-April 2000 tax year. The companies were required to make the payments for this tax period with the final payment being made in June 2000. However, the companies will ultimately receive a refundable credit for those payments against the new tax. The quarterly credit equals 1/60th of the total payments made for the May 1999-April 2000 tax year. Companies will begin taking the credit in November 2001 (FY 2002).

Revenues from the natural gas gross receipts tax are strongly influenced by changes in the market for natural gas – specifically, the increase in competition by non-utilities due to the expansion of the Natural Gas Choice program and the price changes due to changes in supply and demand for natural gas.

Expansion of choice program

Competition has made substantial in-roads in the Ohio natural gas industry. Industrial and larger commercial users of natural gas in Ohio have been buying from brokers or directly from producers in the Gulf of Mexico, rather than from their local distribution company (LDC) for quite some time. In 1996 industrial consumers purchased 95 percent of their total gas supplies from “non-jurisdictional” sources – i.e., not from their LDC. Non-jurisdictional sources accounted for 30 percent of purchases of commercial consumers and virtually zero percent of residential consumer purchases. These “non-jurisdictional” purchases escape the public utility excise tax and legally may be captured under the sales tax. In practice, most gas used by industrial customers apparently falls under the sales tax exemption for direct use in manufacturing and is therefore not taxed. It’s a different story for residential and commercial customers.

Beginning in 1997, increasing numbers of commercial and residential consumers began to purchase natural gas from non-jurisdictional sources. In 1997 several natural gas customer choice pilot programs were initiated in the state. These programs provided access to the competitive market to Ohio residential and small commercial customers for the first time. (A small commercial customer – or small business – is defined as one that uses less than 2,000 million cubic feet [mcf] per year.) The programs began in April of 1997 with the Columbia Gas Choice program in the greater Toledo area. By March of 1998, 31% of the eligible residential consumers and 46% of the eligible commercial consumers had signed up with an alternative supplier. The Columbia program was subsequently opened statewide and by December 1998, 19% of Columbia’s residential customers and 26% of commercial customers were obtaining gas from alternative suppliers.

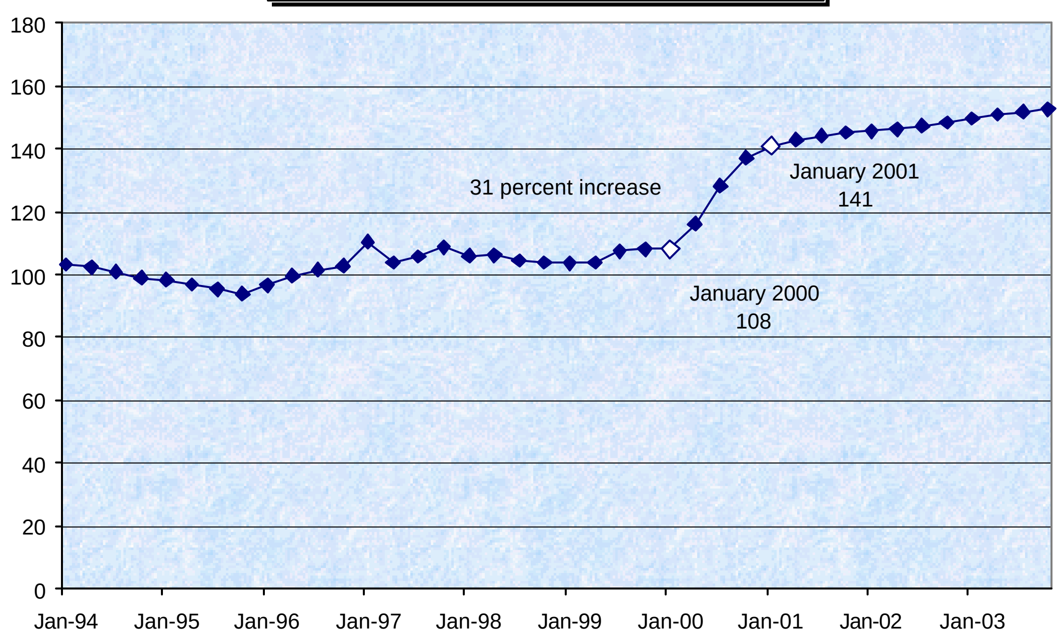
The choice program has continued to expand. By the end of calendar year 2000, all residential and commercial customers of Columbia, Cincinnati Gas & Electric, and Dominion East Ohio Gas, which together comprise approximately 90 percent of all residential and commercial customers statewide, are eligible to participate. Approximately 25 percent of those eligible currently participate.

As participation in these programs expands, natural gas gross receipts tax revenues will shrink (all other things equal). However, unlike sales to industrial consumers, sales to residential and commercial consumers will be picked up under the sales tax. Gas transportation services are still being provided by the LDCs to all natural gas consumers in their service territories. These sales of transportation services are included in the gross receipts tax base. However, revenues from transportation services account for only a small portion of the current excise tax base. (In 1999, for example, transportation services accounted for only 15 percent of total revenues from natural gas sales by LDCs. In 1995 transportation services accounted for only 5 percent – indicating the impact that open access has already had.)

Changes in the market for natural gas

At this time last biennium natural gas prices were low and were expected to stay low. Due to the low prices and warmer than normal winters, gas inventories were not completely replenished. However, since then demand has increased – fueled largely by the increase in demand from electric utilities with their construction of new peaking facilities, which are reliant on natural gas. Also colder than normal temperatures in November and December 2000 exacerbated price increases. Prices are now projected to remain at the higher level (approximately 9 cents per kilowatt-hour) for the foreseeable future (see Chart 3).

Chart 3 - Natural gas price index, household expenditures
January 1994-December 2003



It was originally thought when the tax changes were implemented in the last budget that, due to the choice program, the base changes would result in a loss of roughly $5 million to the state budget. To mitigate this loss in the current biennium, H.B. 283

called for the early payment of the tax due for the April through June 2000 quarter by any natural gas company that had at least 300,000 open access customers as of July 1, 1999. Such companies would pay $10.3 million in June 2001 rather than August 2001. The August payment would still be made; the $10.3 million would be refunded over time in the form of a tax credit. (It would be rolled into the tax credit for the tax year 2000 payments.) One company (Columbia Gas) did qualify for the early payment, so in addition to other revenues generated in FY 2001; the state will also receive an additional $10.3 million in June. However, the anticipated tax loss due to the erosion in the base has been partially offset by the higher than anticipated natural gas prices, so that FY 2001 revenues are expected to exceed the original June 1999 estimate of natural gas public utility excise tax revenues before the base change.

Revenue projections

Revenue projections for the FY 2001-2003 period are based on actual sales and tax data provided by the Public Utilities Commission and the Tax Department, respectively. Sales growth projections were based on Energy Information Agency estimates of sectoral demand for natural gas, adjusted for growth in the choice program. Revenue estimates were found by multiplying the sales figures by price estimates. The price estimates were derived from current PUCO sales and revenue data and natural gas prices indices obtained from WEFA and from the Energy Information Agency. The estimates assume “normal” weather patterns for the remainder of the year and for the upcoming biennium. Household and commercial gas prices are assumed to remain relatively high. Industrial prices are projected to fall; however, industrial gas sales are such a small part of the total that this is not expected to have a significant impact on tax revenues. The forecasted revenues assume that the proposed freeze on the amounts deposited into and distributed from the three local government funds is enacted.

Electric Company Revenues

The Kilowatt-hour Tax

S.B. 3 eliminated the public utility excise tax with respect to electric companies and established a kilowatt-hour tax to replace the lost revenue. S.B. 287 modified the kilowatt-hour tax with respect to large energy users. These changes will first have an impact in June 2001 (this fiscal year) when electric companies make their last payment of the gross receipts tax and begin paying the kilowatt-hour tax. In addition, H.B. 384 expanded the coal tax credit, which affects public utility excise tax reconciliation payments in November 2000 and 2001.

While electric competition is to begin this calendar year, it should have little impact on the kilowatt-hour tax base. The tax is levied on the distribution companies – which remain regulated – and is included in the rates that the distribution companies charge for distributing electricity. Moreover, the tax is based on the kilowatt-hours consumed – as opposed to the value of sales. So, for the most part, price changes should not greatly affect tax revenues – except to the extent that prices affect the amount of energy used. However, real economic factors – like production levels – and weatherrelated matters are assumed to have a much greater impact than price on the electricity usage in the state.

Although the kilowatt-hour tax is not levied on the electricity consumer, the tax rate varies in accordance with the consumption of each of an electric company's customers. The tax rate is equal to $.00465 per kilowatt-hour for the first 2,000 kWh consumed by any customer in a month's time. For the next 13,000 kilowatt-hours consumed in a month the tax rate is $.00415 per kilowatt-hour. And for all consumption in excess of 15,000 kilowatt-hours per month the rate is $.00363 per kilowatt-hour.

Large industrial users – that is, establishments that use more than 45 million kilowatt-hours per year – have the option of self-assessing. They would be taxed at a rate of $.00075 per kilowatt-hour up to 504 million kWh plus 4 percent of the total price.

The tax is to be remitted monthly by local distribution companies and self-assessing users. Tax liabilities would be based on the prior month's usage. Assuming that the tax generates at least $552 million in a year's time, the GRF would receive 59.976 percent of the total revenue from the tax. The remainder would be distributed to the local government fund, the local government revenue assistance fund, the school district property tax replacement fund, and the local government property tax replacement fund. If the tax did not generate at least $552 million, the GRF would receive less, in order to hold the other funds harmless.

Kilowatt-hour tax revenue projections were based on projected electricity sales growth of residential, commercial, and industrial consumers, weighted by each sector's relative contribution to tax year 1998 estimated revenue. Residential sales were based on WEFA's forecast of household energy consumption; commercial sales were based on forecasted GDP growth, and industrial sales were based on WEFA's forecast of primary metals manufacturing. Annual revenue projections were developed that were then shared down to monthly tax revenues based on prior year consumption data. Total estimated revenue for FY 2002 is $562 million; estimated revenue for FY 2003 is $563 million. Since both of these numbers exceed the $552 million threshold established by S.B. 3, the GRF would receive its full share of 59.976 percent of total revenue in both years.

Electric Company Public Utility Excise Tax Revenues

Electric companies and rural electric companies will continue to pay the gross receipts tax through June 2001. S.B. 3 provides for three payments for tax year 2001 (from May 1, 2000 to April 30, 2001); however, the third payment is only ¼ rather than 1/3 of the current estimated liability. In November 2001 tax year 2001 public utility excise tax payments (covering the May 1, 2000 to April 30, 2001 time period) are reconciled with tax year 2001 certifications. Included in the reconciliation are the expanded coal tax credits. (The cost of the credits in November 2001 is expected to be $53 million, of which $50.5 million would be a cost to the GRF.) Subsequent credits are to be taken against the corporate franchise tax. The forecasted revenues assume that the proposed freeze on the amounts deposited into and distributed from the three local government funds is enacted.

The Public Utility Excise Tax

Telephone companies, along with heating, pipeline, waterworks, and water transportation companies remain subject to the original public utility excise tax. Excise tax payments for each tax year are made in October, March and June. The payments are based on prior year certifications of tax liability. The actual payments are then reconciled with actual liabilities in November of the following year. For example, tax revenue in FY 2001 is based largely on utility sales for the period from May 1999 to April 2000. However, the November reconciliation payment introduces a wrinkle between the growth in liabilities and the growth in tax revenues.

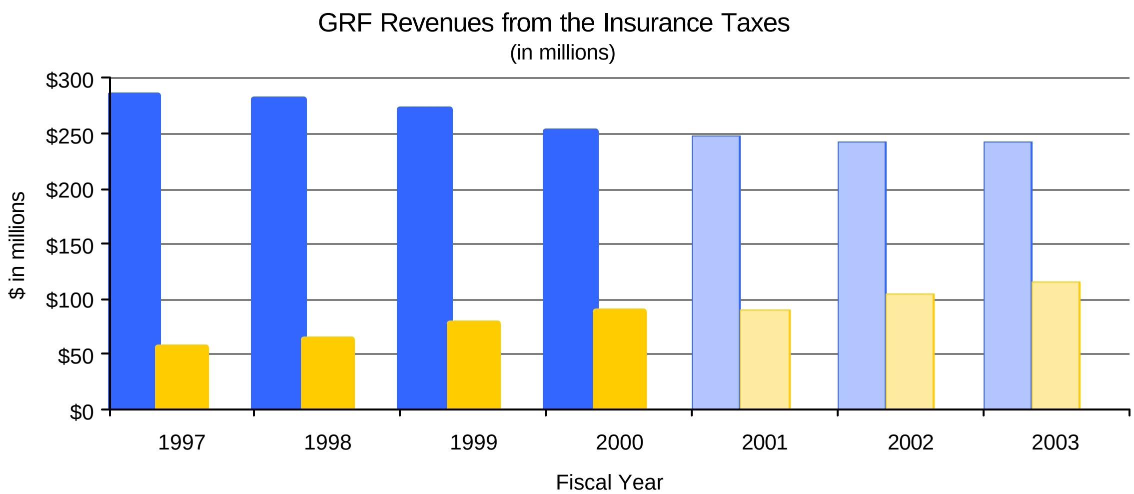
Telephone companies account for 96 percent of the base of the remaining public utility excise tax. The revenue estimate for FY 2001 to FY 2003 is based on the forecast of telephone company tax liabilities and all other utility tax liabilities. The GDP growth rate was used to estimate telephone company liabilities in FY 2001 to 2002. The growth in telephone company revenues is further discussed below. The "all other" category is expected to grow at the trend rate of 1.9 percent. Since this includes both heating companies and pipelines, both of which should have benefited from the colder than normal winter so far, this may slightly under estimate FY 2002 revenues. The forecasted revenues assume that the proposed freeze on the amounts deposited into and distributed from the three local government funds is enacted.

Telephone companies

In spite of the passage of the Telecommunications Act of 1996 and the increase in competition offered by wireless, competition has not had a significant impact on the local telecommunications market in Ohio. The traditional local exchange companies have not only held on to their markets, but have continued to grow. After remaining essentially flat from tax year 1996 to 1998, telephone company public utility excise tax certifications increased by 7.3 percent from 1998 to 1999 and by another 3.1 percent from tax year 1999 to 2000. Increasing personal income, demographic change, and the growth in home computer usage – inducing many households to install an additional phone line – may account for much of the growth. For example, according to the U.S. Census Bureau, U.S. household Internet use grew by 58.4 percent between 1998 and 2000. At the same time, the number of additional telephone lines for households with telephones grew by 12.6 percent between 1997 and 1998 and by 29.6 percent between 1998 and 1999. The growth rates for Ohio are probably less than that since Internet usage is lower than average in this state; that, however, merely suggests that there is even more room for growth in Ohio.

Whether the trend will hold remains to be seen. Increasing use of wireless and the wireless web, expansion of cable-based access to the Internet, increased use of phone cards (the purchase of which is subject to the sales and use tax rather than the gross receipts tax), and increased facilities-based competition could eventually cut into telephone company revenues. Currently, many households have simply expanded their telecommunications options; however, the economic slowdown may cause some to choose among telecommunications sources rather than continuing to depend upon an array of options.

Insurance Taxes



Insurance	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Foreign	$283.5	$280.9	$271.6	$252.3	$247.4	$242.4	$242.6
	2.7%	*-0.9%*	*-3.3%*	*-7.1%*	*-1.9%*	*-2.0%*	*0.1%*
Domestic	$56.4	$63.2	$77.5	$88.2	$90.2	$104.1	$115.6
	2.1%	*12.1%*	*22.6%*	*13.8%*	*2.3%*	*15.4%*	*11.0%*
Total	$339.9	$344.1	$349.1	$340.5	$337.6	$346.5	$358.2
	2.6%	*1.2%*	*1.5%*	*-2.5%*	*-0.9%*	*2.6%*	*3.4%*

House Bill 215 of the 122nd General Assembly reformed insurance taxes over a five-year transition period starting in fiscal year 1999. The phase-in schedule is presented in the table below.

Phase in Schedule for Insurance Tax Reforms

	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Foreign Insurers						
Rate applied to premiums	2.50%	2.30%	2.09%	1.84%	1.62%	1.40%
Domestic Insurers						
Weight applied to method						
Old Method	100%	79%	58%	40%	20%	0%
New Method	0%	21%	42%	60%	80%	100%
	Note: Old method for domestic tax is the lesser of a 2.5 percent tax on premiums or a 0.6 percent tax on capital and surplus. New method for domestic tax is premium tax at same rate as foreign tax.					
Small Insurer Credit						
Phase in percentage	0%	20%	40%	60%	80%	100%

The “domestic preference” that allowed Ohio-based insurers to pay the lesser of a 2.5 percent tax on premiums or a 0.6 percent tax on capital and surplus was eliminated. During the five-year transition period, all insurance companies, except “health insuring corporations” (HICs), have their taxes phased up or down to a 1.4 percent tax. By fiscal year 2003, all insurance companies, except HICs, will pay a basic tax of 1.4 percent of premiums. The tax rate applicable to foreign insurance companies is being phased down in uneven increments from the previous rate of 2.5 percent. During the transition period, domestic insurers pay a tax equal to a weighted average of what their tax would have been under the old tax structure and what it would be under the revised tax structure. The revised structure for domestic insurers is the same as that for foreign insurers. The tax rate for HICs is being phased up to one percent. HICs were exempt from the insurance tax under the old tax structure.

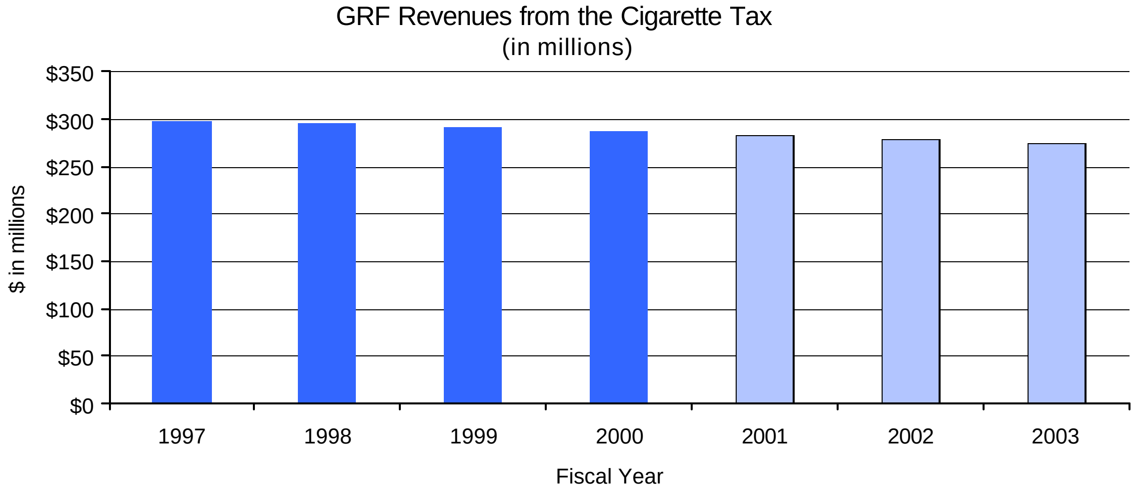
The changes act to reduce foreign insurance taxes and increase domestic insurance taxes. However, because of the way that state retaliatory taxes work, the total tax burden on domestic insurance companies, in the aggregate, should be reduced. Similarly, some foreign insurers will pay higher rates because of retaliatory taxes. In general, the retaliatory tax rate imposed is either the domestic rate of the state taxing the foreign insurer or the rate of the state in which the foreign insurer is incorporated, whichever is greater.

In the aggregate, the reduction in retaliatory taxes paid by Ohio insurance companies to other states is greater than the increase in premium taxes paid to Ohio. However, for some Ohio insurance companies, this may not be true, and these companies end up paying more total tax. To protect small insurers from large increases in their effective tax rate, a special small-company tax credit was included in the new structure. The credit applies to any company that has less than $75 million in premiums nationwide, or is a member of a group that has less than $75 million in premiums nationwide. The credit is also phased in and will have a maximum amount of $200,000 when fully phased in.

The forecasts of revenues from Ohio’s insurance taxes were obtained by adjusting the original estimates of the effects of the restructuring based on revenue collections for fiscal years 1999-2000.

The revenue collected from insurance taxes is deposited into the General Revenue Fund. An additional 0.75 percent tax is levied on the gross premium receipts derived from fire insurance and that portion of the gross premium for other coverage that is reasonably allocable to fire insurance. Revenue from this tax is deposited into the Fire Marshal’s Fund.

Cigarette and Tobacco Products Tax



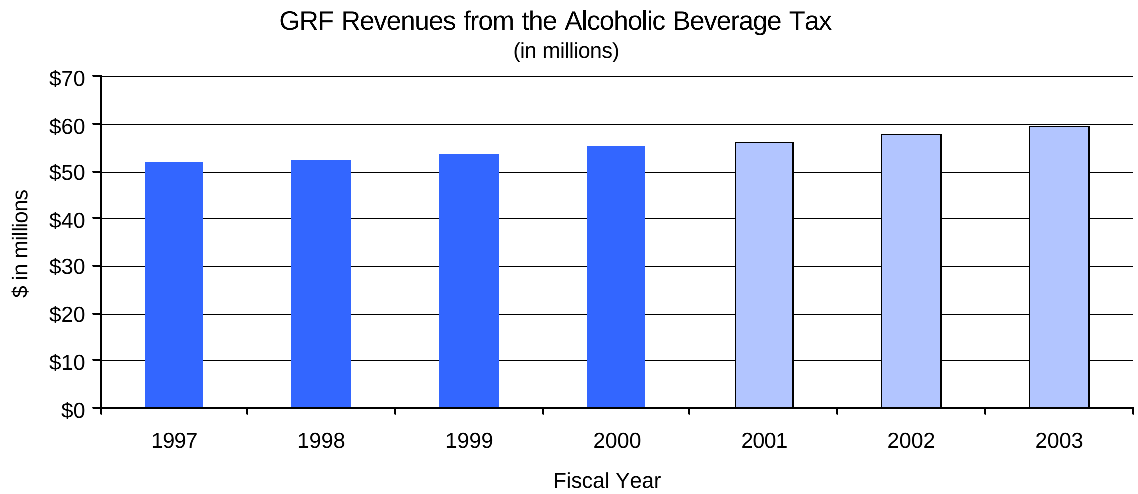
	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Cigarette	$298.4	$296.6	$290.6	$287.7	$282.5	$279.1	$275.7
	1.3%	*-0.6%*	*-2.0%*	*-1.0%*	*-1.8%*	*-1.2%*	*-1.2%*

The Cigarette and Other Tobacco Products Tax is levied on cigarettes, cigars, chewing tobacco, snuff, smoking tobacco, and other tobacco products. Cigarettes are taxed at a rate of 1.2 cents per cigarette or 24 cents per package of 20 cigarettes. Other tobacco products are taxed at 17 percent of their wholesale price.

Revenue collected from the tax is deposited into the General Revenue Fund.

The forecast for Cigarette and Tobacco product tax is primarily based on expected growth in Ohio Personal Income and cigarette prices. In order to pay for the settlement agreement with the states, tobacco products manufacturers have raised prices of cigarettes consistently, which has reduced consumption. Between 1997 and 2000, Ohio state minimum cigarette prices have increased by about 76 percent. Price increases on generic as well as name brand cigarettes are expected to continue both from a scheduled federal excise tax hike in January 2002 and tobacco manufacturers seeking to benefit from the oligopolistic nature of the industry, further reducing consumption and tax revenues. Higher cigarette prices may also encourage smuggling from major tobacco producing states and foreign countries, and lower tax revenues.

Alcoholic Beverage Tax



	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Alcoholic Beverage	$51.9	$52.4	$53.8	$55.3	$56.3	$58.0	$59.6
	2.3%	*1.0%*	*2.7%*	*2.8%*	*1.8%*	*3.0%*	*2.8%*

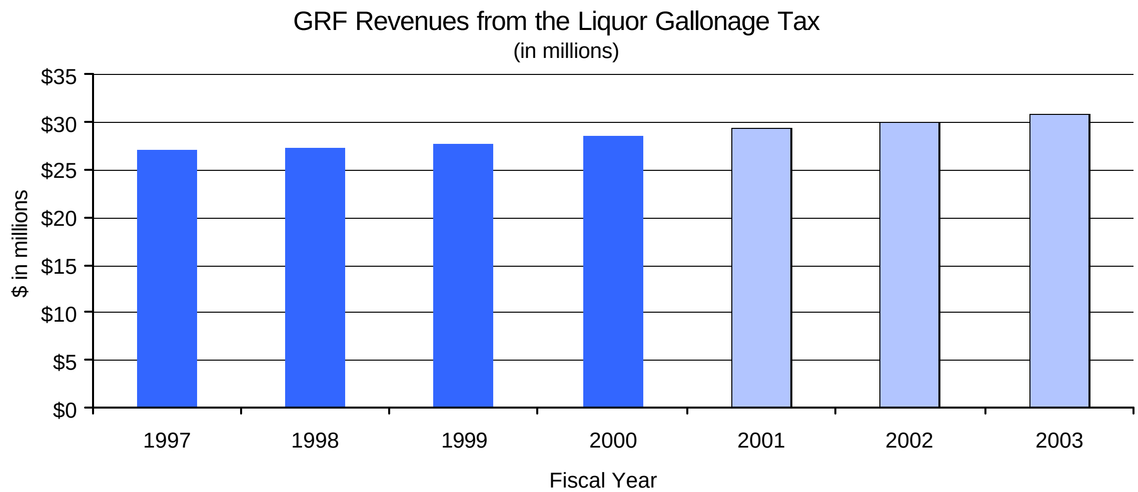
The Alcoholic Beverage Tax applies to sales of beer, malt beverages, wine, and mixed alcoholic beverages. The tax is based on a per-container rate depending on the type of beverage sold. Beer is taxed at varying rates that are equivalent to 0.14 cents per ounce. Wine less than 14 percent alcohol by volume is taxed at 33 cents per gallon. Wine between 14 percent and 21 percent alcohol by volume is taxed at $1.00 per gallon. Mixed beverages are taxed $1.20 per gallon.

Major exemptions to the tax are sacramental wine, sales to the federal government, and sales in interstate commerce.

Revenue is deposited in the General Revenue Fund with two exceptions. One percent of the tax is deposited in the Beverage Tax Administration Fund and five cents per gallon of wine is deposited into the Ohio Grape Industries Special Account.

The forecast is based on Ohio personal income. Population increase and growth in income appear to drive alcoholic beverage tax receipts.

Liquor Gallonage Tax

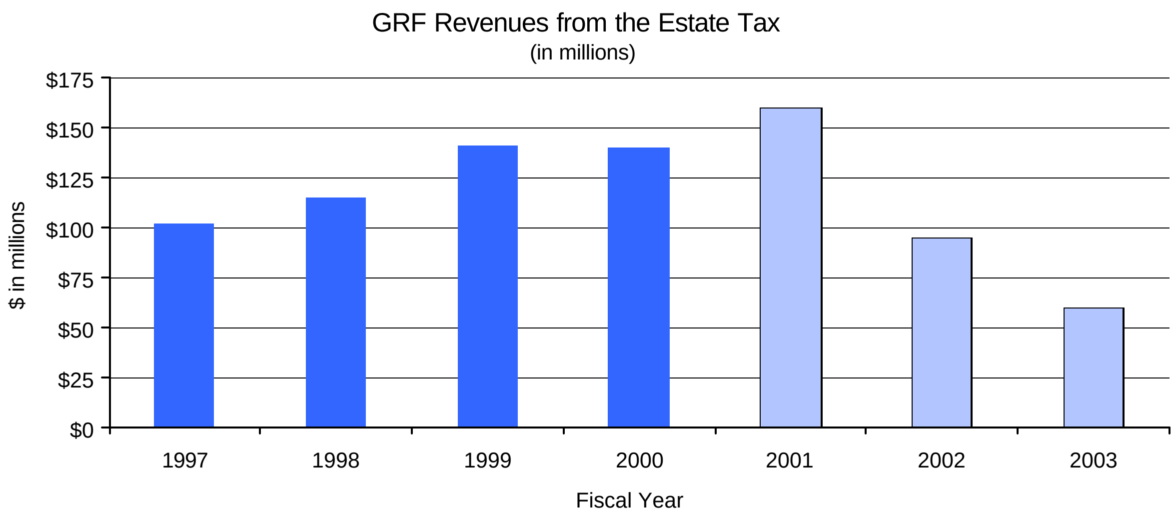


	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Liquor Gallonage	$27.1	$27.3	$27.7	$28.5	$29.4	$30.0	$30.8
	-0.7%	*0.7%*	*1.5%*	*2.9%*	*3.2%*	*2.0%*	*2.7%*

The Liquor Gallonage Tax is levied at the rate of $3.38 per gallon of spirituous liquor. Revenue is deposited into the General Revenue Fund.

Real prices of alcoholic beverages have been declining in the U.S. since 1978 and per capita consumption of alcohol has been generally declining over the same period. These trends seem to contradict the law of demand. However, important determinants of alcohol consumption change over time. Specifically, demographic shift to an older population-which consume less alcohol- may account for the decline in per capita consumption. However, the relative importance of disposable income as a determinant of demand for liquor may have increased, explaining year-over-year increases in tax receipts. The forecast of liquor gallonage tax is based on expected growth in Ohio personal income, changes in liquor prices and previous years consumption.

Estate Tax



	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Estate	$102.0	$114.8	$141.5	$140.0	$160.0	$95.5	$60.6
	13.4%	*12.5%*	*23.3%*	*-1.1%*	*14.3%*	*-40.3%*	*-36.5%*

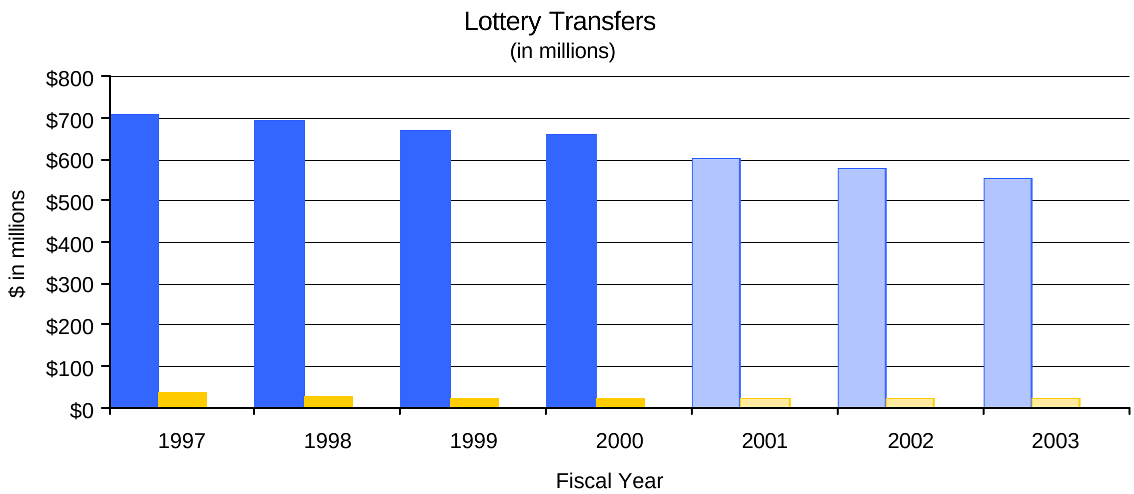
The Estate Tax is levied on the gross value of a decedent's estate less allowable deductions. A marital deduction is allowed in an amount equal to the net value of any assets passing from the decedent to the receiving spouse, but only to the extent that the assets are included in the value of the Ohio gross estate. Additionally, certain items are eligible to be deducted from the gross estate before calculating tax liability. These items include, but are not limited to: funeral expenses, costs of administering the estate, unpaid debts against the estate, and charitable bequests. The tax is progressive with marginal rates ranging from 2 percent of the taxable estate to 7 percent of the value of the taxable estate over $500,000. A nonrefundable credit (previously $500) is allowed against the tax.

Senate Bill 108 of the 123rd General Assembly increased the credit allowed against the tax. For estates of individuals dying on or after January 1, 2001 but before January 1, 2002 the credit is $6,600. This effectively exempts estates with net taxable value less than $200,000 (approximately 63 percent of estates) from the estate tax. For estates of individuals dying on or after January 1, 2002 the credit is $13,900. This effectively exempts estates with net taxable value less than $383,000 (approximately 76 percent of estates) from the estate tax.

Senate Bill 108 also changed the percentages used to allocate estate tax revenues between the state and local governments. Previously, the municipality or township in which the tax originates received 64 percent of the revenue and the state received 36 percent. The state's share of the estate tax is credited to the General Revenue Fund. For estates of individuals dying on or after January 1, 2001 but before January 1, 2002 the municipality or township in which the tax originates receives 70 percent of the revenue and the state receives 30 percent. For estates of individuals dying on or after January 1, 2002 the municipality or township in which the tax originates receives 80 percent of the revenue and the state receives 20 percent.

The Estate Tax is volatile in nature and difficult to predict. The baseline forecast is based mainly on adjusted trend analysis. The estimated impacts of the changes made by Senate Bill 108 were taken from the Fiscal Note for that bill. These estimates assumed that tax payments would be made within nine months of the decedent's death.

Lottery Transfers



Lottery Transfers	FY 1997	FY 1998	FY 1999	FY 2000	FY 2001	FY 2002	FY 2003
Operating Profits	$710.5	$695.2	$671.3	$661.0	$604.1	$579.2	$554.9
	-0.4%	*-2.2%*	*-3.4%*	*-1.5%*	*-8.6%*	*-4.1%*	*-4.2%*
Unclaimed Prizes	$38.0	$28.7	$25.0	$25.0	$25.0	$25.0	$25.0
	192.3%	*-24.5%*	*-12.9%*	*0.0%*	*0.0%*	*0.0%*	*0.0%*
Total	$748.5	$723.9	$696.3	$686.0	$629.1	$604.2	$579.9
	3.0%	*-3.3%*	*-3.8%*	*-1.5%*	*-8.3%*	*-4.0%*	*-4.0%*

The Ohio Lottery Commission operates to create profits to be transferred to the Lottery Profits Education Fund (LPEF) for use in programs benefiting primary, secondary, vocational, and special education in Ohio. The amount transferred comes largely from operating profits with occasional transfers made from the Unclaimed Prize Fund.

After a peak of $2.31 billion in sales in FY1996, Lottery sales have steadily declined to $2.15 billion in FY2000. Tickets sales will likely fall below $2 billion in FY 2001. Although incomes continue to grow and attitudes towards gaming remain generally favorable, increased competition in the gaming market, primarily from neighboring states, has decreased lottery ticket sales. Regular and riverboat casinos, racetracks video lottery terminals, multi-jurisdictional lotteries such as Powerball and the Big Game, and Internet gaming have all contributed to this decline. The table below presents a recent history of lottery sales, an estimate of sales for fiscal year 2001, and forecasts of sales for fiscal years 20002 and 2003.

Lottery Sales: Recent History and Forecast *(in millions)*

Fiscal Year	1997	1998	1999	2000	2001	2002	2003
Ticket Sales	$2,300.0	$2,195.7	$2,144.7	$2,150.4	$1,922.0	$1,853.4	$1,787.2

Lottery profits transfers are required by law to be at least 30 percent of sales. As ticket sales have declined, profits transfers have decreased from $713 million in fiscal year 1996 to $661 million in FY2000. Sale and profits are expected to be lower in FY2001, and the decline in profits transfers is expected to continue in the next biennium.

Sales and profits were estimated on a trend basis and assume no significant change in the current mix of games and no substantial increases in advertisement expenditures. It is important to note that changes in game structure do not always guarantee an increase in sales. In July of 2000, the Ohio Lottery introduced Super Lotto Plus to replace Super Lotto. In Super Lotto, a player had to match correctly 6 out of 47 numbers to win the big prize and the odds against a $1 bet winning the jackpot were 11 million to 1. The Super Lotto Plus is a 6 out of 49 game with the odds against a $1 bet winning the jackpot of 13 million to 1. In addition, jackpot increases in Super Lotto Plus are much lower than the automatic 4 million in Super Lotto. Super Lotto sales decline when the jackpot of multi-jurisdictional games such as Powerball is high. Higher jackpots induce "marginal" lottery players to purchase lottery tickets. Although the profitability of the game has improved, with longer odds and smaller increases in jackpots in the new version of Super Lotto, it is likely that revenue from this on-line game will be much lower in FY2001 than in FY2000.