

Property Taxes and School Funding in Ohio

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When it comes to education, the United States Constitution is silent. The Tenth Amendment declares that, “The powers not delegated to the United States by the Constitution...are reserved to the states respectively, or to the people,” thus making education a state responsibility. As a result, there is much variation across the states on how public education is provided. However, when it comes to financing public education, there are some similarities among the states. Forty-one states employ “foundation aid” programs. These programs are characterized by a partnership between the state and local districts in which foundation formulas guarantee a minimum level of funding per student based on a combination of state and local effort. Under these formulas property-poor districts typically receive more state aid than property-wealthy districts. Six states use a “guaranteed tax base” or “power equalization” approach that ensures that each district can raise the same amount of per pupil revenue for each \$1 per \$1,000 of assessed property value. Two states use a “flat grant” approach which provides a fixed amount of state revenue per pupil to all local school districts. Hawaii is unique in that it operates a state school system (Maxwell & Sweetland, 2008).

Property Taxes

Common to all of the approaches described above is the property tax. Property taxes are generally classified as *real property* (land and buildings) or *personal property* (inventory, machinery, equipment, stocks and bonds). Historically, the property tax constitutes the majority of local tax revenues levied for the support of public schools (Brimley & Garfield, 2008). As a result, property taxation and school funding are closely linked in the United States. Nearly half of all property tax revenue is used for public elementary and secondary education (Kenyon, 2007). In Ohio, nearly 70% of all local property taxes are earmarked for the support of public schools (Maxwell & Sweetland, 2008).

According to Kenyon (2007) the following states are the most reliant on property taxes when expressed as a percent of all state and local taxes:

- New Hampshire - 61.4%
- New Jersey - 45.1%
- Texas - 43.8%

Ohio (28.7%) ranks 30th among all the states.

Kenyon (2007) has noted that:

There is an active policy debate across the country regarding the degree to which schools should be funded with property tax dollars. Some policymakers and analysts call for a reduced reliance on property taxation and an increased reliance on state funding; others claim that the property tax is a critical ingredient in effective local government (p.2)



Advantages of Property Tax

- Stable tax; not as volatile as income tax or sales tax, especially during times of recession (Kenyon, 2007).
- Highly visible tax, providing a direct linkage between services provided by local schools and the cost of those educational services (Brimley & Garfield, 2008).
- Associated with more community involvement (Fischel, 2001) and higher student achievement (Ladd & Hansen, 1999) than in states where districts rely more heavily on state aid than on local property taxes.



Disadvantages of Property Tax

- May not be as accurate a measure of people's wealth as it once was (Brimley & Garfield, 2008).
- When used as the basis for a state's foundation funding formula, it can create wide disparities in educational funding levels between districts. Such disparities usually result in property-wealthy districts being able to spend significantly more on students and programs than property-poor districts.

In his latest budget proposal, Governor Strickland (2008) forecast that the state's share of funding public schools would rise to 59% by 2017.

Property Tax vs. State Aid

If the alternative to property tax is increased state aid, local school districts should be aware that there can be a downside to becoming more reliant on the state. Local districts would likely:

- ◆ have less control over the amount of revenue they receive.
- ◆ be more vulnerable to reductions in state aid during economic downturns or shifting state policies (Murray & Ruben, 2007).¹
- ◆ experience increased reliance on state funding, resulting in less community involvement in local schools.²
- ◆ experience lower levels of student achievement (Ladd & Hansen, 1999).
- ◆ encounter a loss of local control.

These disadvantages have led many scholars of school finance to conclude that, "The ultimate goal for most states should be reducing reliance on local property tax while increasing state funding" (Carr & Griffith, 2005, p. 168). Carr and Griffith (2005) recommend that state government provide at least 60% of the financial support for public schools. In 2004-2005, twelve states met or exceeded this percentage (Kenyon, 2007).

Clearly, the cost and benefits associated with replacing local property taxes with increasing levels of state aid needs more study. However, this process

may solve some problems; chiefly, spending disparities between school districts and the onerous effects of property taxes on the poor and elderly.

The History of School Funding in Ohio

In 1997 the Ohio Supreme Court, in the *DeRolph* case, found the system of funding Ohio's public schools unconstitutional largely on the grounds that the foundation formula was overly reliant on property taxes (McKinley, 2005, p. 311). This overreliance resulted in wide disparities in per pupil expenditures across the state with property-wealthy districts being able to provide many more services and programs than property-poor districts. According to Brimley and Garfield (2008, p.62) these spending disparities between school districts in Ohio ranged from \$4,000 per pupil to \$12,000 per pupil. Only Texas (\$2,112 to \$19,333) and North Dakota (\$2,085 to \$11,743) had greater per pupil expenditure disparities. In spite of *DeRolph*, these disparities and Ohio's reliance on local property taxes still exist today.

¹ Local districts in Michigan - a state that replaced local property taxes with state aid funded through statewide sales tax in 1993 - are experiencing how a severe recession can severely diminish state funding at the school district level (Christoff & Bell, 2007).

² According to Fischel (2001) "...there is evidence that loss of local property taxation reduced civic engagement generally" (p. 161).



Governor Strickland's Plan: Reduce "Charge Off" and Offer "Conversion Levies"

When Ted Strickland was elected governor of Ohio, he vowed that no matter what else he accomplished as governor, his term would be considered a failure if he did not fix the school funding system in Ohio (Smith, 2008). On January 28, 2009, Governor Strickland unveiled his plan to fix the system (Strickland, 2009). Overall, his plan calls for spending nearly \$1 billion more in state aid for public schools than the previous budget. According to the plan, the new Ohio Evidence Based Model (OEBM) funds the foundation formula by using "research to identify educational components that result in academic success, thereby defining adequacy. It incorporates real financial data and socioeconomic factors to fund resources and implement proven school programs according to student need to achieve educational adequacy" (Strickland, 2009).

While the governor's plan certainly provides more state funding for Ohio's schools, it may not address the "overreliance" on property tax issue that was the basis of the *DeRolph* decision a decade earlier. Gov. Strickland's funding model contains several features that have an impact on local property taxes. The current funding formula guarantees a basic funding level of \$5,720 per student, a combination of local property tax and state aid. In districts with lower property wealth, increased state aid would be used to maintain the prescribed basic funding level.



= 10 mills

In Ohio property taxes are calculated in mills. One mill is equal to 1/10 of a cent and is calculated as .001 times the assessed value of the property. If a property has an assessed value of \$100,000 and the school district collects the state minimum of 20 effective mills (.020), the property owner would pay a basic tax of \$2,000 on the property. Every school district in Ohio must levy a minimum of 20 mills in support of schools. Twenty mills equals a 2% tax rate.

Currently, the local district's share of the state foundation formula is 23 mills of the total assessed property value of all the property within the district. The governor's proposal calls for lowering the 23 mill local "charge off" to 20 mills. In so doing, the state would pick up the 3 mill difference, increasing the state's share of the foundation formula. The school district thus saves the taxable value of 3 mills of property valuation and local tax payers save 3 mills worth of property taxes.

While there is no question that reducing the local "charge off" to 20 mills could provide direct tax relief to local property owners, the more likely outcome is that local districts may not have to go to the ballot as frequently. Reducing the local charge off by 3 mills will, by its very nature, benefit property-wealthy districts more than property-poor districts. This provision could actually contribute to an even wider disparity in per pupil spending between rich and poor districts; 3 mills in a property-wealthy district raises significantly more tax dollars than 3 mills in a property-poor district.

Another provision of Gov. Strickland's budget proposal is a local property tax levy option referred to as a

"conversion levy." Under

Ohio state law when property values rise

through reappraisal, millage rates are reduced so that a levy never raises more revenue than it did when it was passed.

When property values rise as a result of revaluation, districts receive less state aid through the state foundation formula, but no additional local property tax revenue to make up the difference. This phenomenon is referred to as "phantom revenue" and explains why districts in Ohio are on the ballot so frequently. Districts must go on the ballot for additional funding to replace lost state revenue due to rising property values. Due to phantom revenue, it has been said that "there are only two types of districts in Ohio; those that are on the ballot and those that will be" (Johnson, 2008, p. 45).



According to Ohio law, school districts must levy a minimum of 20 mills in support of schools. Under this requirement, once a district's effective millage rate is reduced to 20 mills, the district will henceforth receive revenue growth on 20 mills every time property values rise during reappraisal. As a result, school districts have figured out that being at the 20 mill floor is a desirable place to be and about two-thirds of the districts are already there. Under his new plan, the governor is proposing to give districts with effective millage rates above 20 mills an opportunity to place on the ballot a conversion levy that would essentially set the district's effective millage rate at the 20 mill floor without a subsequent loss in property tax revenues. Once at this floor, the district would automatically receive revenue growth on 20 mills of property valuation every time properties are reappraised and values rise; essentially if voters pass a conversion levy, their property taxes would rise every reappraisal if property values increase. However, a conversion levy provides no property tax relief for tax payers. If approved by voters, it would actually add to the local property tax burden.



Policy Recommendations for Ohio:

So, are there policies that can be put in place to address these issues? Are there policies that could lessen the impact of property taxes on the elderly? Are there policy options that could reward districts for their property tax efforts that might further reduce the per pupil spending disparities between districts? In response to these questions, three policy recommendations come to mind:

- ◆ **Property tax “circuit breakers”:** Property tax circuit breakers provide tax relief to low income and elderly residents whose taxes exceed a given percentage of income, in the same way a circuit breaker offers protection from an electrical overload (Allen & Woodberry, 2006). These programs exist in 34 states and are funded at the state level so that they do not reduce local school district tax collections (Bowman, 2008). While the specific policy provisions vary from state to state, generally benefits decline as income rises and most are aimed at senior citizens (Haveman & Sexton, 2008).
- ◆ **Property tax deferral programs:** These programs are designed to allow eligible homeowners the option of delaying the payment of property taxes until the home is sold or the owner’s estate is settled and are typically targeted to the elderly and the disabled (Haveman & Sexton, 2008). According to Baer (2005), twenty-five states have some type of tax deferral program.
- ◆ **Tax effort incentives:** This recommendation involves providing an incentive to those districts that support their local school district beyond what their ability to pay would suggest. There is a misconception that property-poor districts do not support education because tax levies are hard to pass in such communities. The Ohio Department of Education calculates an index that sheds another light on this misconception. Referred to as the Local Tax Effort Index, it tends to reflect the extent of effort residents of school districts make in support of public primary and secondary education. The index is calculated in the context of residents’ ability to pay in terms of the portion of their income devoted to supporting public education. The formula takes into account any school income taxes, residential property taxes and federal adjusted gross income; this formula generates the Local Tax Effort Index. Examination of this index reveals that low levels of property and income wealth are often associated with higher levels of local tax effort on the part of school district residents. Expenditures per pupil tend to be higher in high wealth districts, but this does not always translate into a higher tax effort index score. A funding mechanism that would provide increased incentive in the form of additional state aid for those districts that show the most local tax effort relative to their wealth may remedy this. Such an incentive would serve as a reward to those communities that truly value education and are willing to make economic sacrifices to support it. If paying local property taxes strengthens the connection between the local community and the schools, then let tax policy support that connection.



Summary:

Given the historic reliance on the local property taxes and in spite of a state Supreme Court ruling that Ohio’s school funding formula is over reliant on their use, it seems unlikely that Ohio is poised to move away from them to any great degree in the near future. Besides, there are those who believe that paying local property taxes keep citizens connected to their local schools. There are some policy considerations that might help make the burden of property taxes more fair and equitable, especially for senior citizens. Those policy options include property tax circuit breaker programs and property tax deferral programs. In addition, it appears that reliance on property values to drive the school funding foundation program has resulted, in part, in wide disparities in pupil expenditures between property-poor and property-wealthy districts in Ohio. One possible remedy to reduce these disparities is a provision to the current foundation formula that would provide additional funding for school districts that demonstrate greater local tax effort.

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