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Budget Footnotes

A NEWSLETTER OF THE OHIO LEGISLATIVE BUDGET OFFICE JANUARY, 1999

FISCAL OVERVIEW

— Frederick Church

The state's financial picture at the halfway point of FY 1999 looks bright. Tax revenue is slightly above the revised estimate, while spending is well below the revised estimate, particularly in the important welfare categories. On the tax side, the personal income tax leads the overages, finishing the first half of the year $30.3 million over estimate. Furthermore, early January data indicates that the state may be headed for a big final estimated payment for taxable year 1998, pushing FY 1999 revenues even further above estimate. The foreign insurance tax, estate tax, and auto sales tax also have significant overages. On the negative side, the corporate franchise tax and the public utility excise tax have the only significant shortfalls.

Now that the issue of the Treasurer of State (TOS) crediting refunds has been resolved, the corporate tax is $16.3 million below estimate. The first of the three major payments against this tax in FY 1999 is due at the end of January. The fact that the state has paid so many refunds against FY 1998 taxes leads us to be concerned about revenues for the remainder of the year.

Once the adjustment for the non-auto sales tax is made, the revenue trouble spot is in the public utility excise tax. Revenues there are $27.0 million below estimate, mostly on the basis of the reconciliation of tax year 1998 taxes being a net negative number. The one advance payment of tax year 1998 taxes that the GRF has received so far was slightly below estimate, but the shortfall was much smaller than for the reconciliation.

Non-tax revenue is also above estimate at the halfway mark, led by a $27.8 million overage in investment earnings. Also, federal revenue has come relatively close to catching up with the estimates: the shortfall through December is only $22.6 million below estimate. December's grant figure was actually above the estimate, cutting what had been a sizable gap down to a relatively small amount (1.3 percent of the estimated year-to-date total). In a complete reversal from last year, the shortfall is now smaller than one would expect on the basis of the underspending in human services (see below).

On the disbursement side, spending excluding transfers is $479.8 million below estimate, and has increased by only 2.5 percent from last year. Once again, the driver is human services spending, which is $294.6 million below estimate, and which has fallen by 1.2 percent from a year

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STATUS OF THE GRF

QUARTERLY LOTTERY REPORT

ISSUES OF INTEREST

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Budget Footnotes examines the fiscal position of the state GRF on a monthly basis. Each issue also contains summaries of Controlling Board actions that have policy implications, and articles on fiscal issues of current interest.

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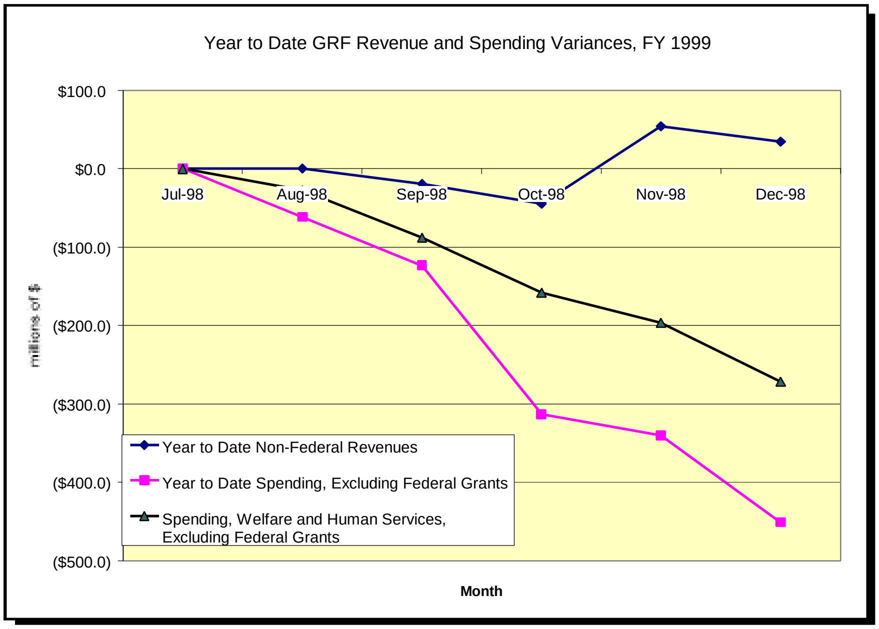


ago. Medicaid has the largest underspending figure, at $139.0 million, but TANF and Other Welfare also have very large variances, at $78.2 million and $53.4 million respectively.

There are still three main culprits in Medicaid underspending: HMOs, nursing homes, and the "all other" category, meaning things other than HMOs, nursing homes, hospitals, physician care, ICF/MR care, and the Medicare buy-in. TANF underspending continues to grow as caseloads plummet toward the "core" of hard-to-employ recipients, whatever that number might be.

Outside of welfare, the big variances are in K-12 education and justice and corrections. K-12 education spending is $88.4 million below estimate. The education spending variance actually shrank some in December, which was to be expected since the Department of Education finally began to disburse state aid via the new SF-3 formula in late October. Presumably K-12 spending will gradually catch up to the estimate as payments are made under the SF-3 framework, which affects not only the foundation amounts but also such programs as Disadvantaged Pupil Impact Aid (DPIA), power equalization, and the charge-off supplement.

Just as the K-12 education variance is shrinking, the justice and corrections variance is growing. With a half year completed, justice and corrections spending is $86.9 million below estimate, almost double the gap from November. It still appears that the bulk of the underspending in this area is due to timing matters that will be sorted out by year's end.

We reiterate that in both the text and the tables, LBO's comparison of actual and estimated revenues and spending, both monthly and year-to-date, are based on OBM's revised forecasts, not the original projections. Thus, when we say that revenues are above the estimate and that spending is below, it is with respect to the revised forecasts. The variances would be even larger if the original estimates were being used.

As Table 1 shows, the GRF's cash balance is now higher than at the same point last year, but the unobligated fund balance is still slightly lower. Encumbrances and accounts payable are $308 million more than at the same point in FY 1998. As one can see in the analysis of Department of Education spending in the disbursements section, much of the encumbered money is being spent rather slowly. ❑

TABLE 1
General Revenue Fund
Simplified Cash Statement
($ in millions)

	Month of December	Fiscal Year 1999 to Date	Last Year	Difference
Beginning Cash Balance	($440.2)	$1,649.0		
Revenue + Transfers	$1,374.2	$8,306.6		
Available Resources	$934.0	$9,955.5		
Disbursements + Transfers	$1,431.7	$10,453.2		
Ending Cash Balances	**($497.7)**	**($497.7)**	**($742.1)**	**$244.4**
Encumbrances and Accts. Payable		$895.0	$587.0	$308.1
Unobligated Balance		**($1,392.7)**	**($1,329.0)**	**($63.7)**
BSF Balance		$906.9	$828.3	
Combined GRF and BSF Balance		**($485.8)**	**($500.7)**	**$14.9**

TRACKING THE ECONOMY

— Frederick Church

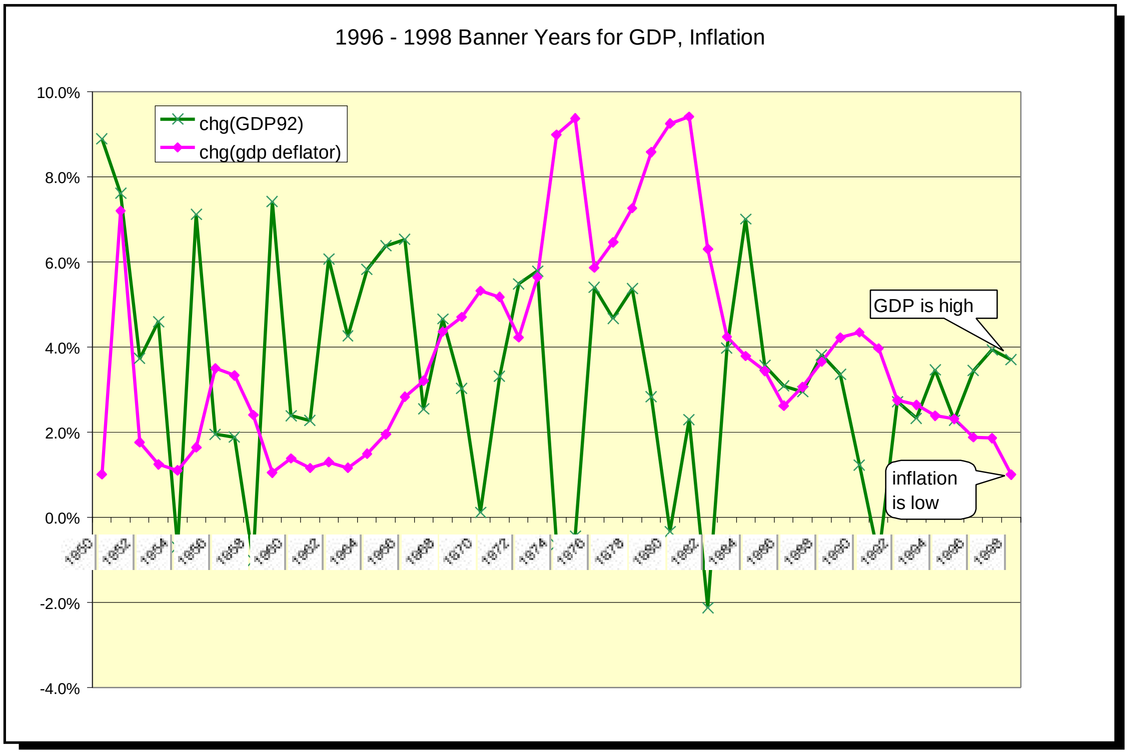
The consensus forecast among analysts for the 4th quarter growth rate in real GDP seemed to be 4.3 percent. Instead, the economy roared to a 5.6 percent growth rate. The fourth quarter surge was led by both business investment and consumer spending. Real GDP growth for CY 1998 as a whole was an eye-opening 3.9 percent. The U.S. economy managed this despite falling exports, in a world where trouble in other countries led to weak demand and the U.S. dollar strengthened its claim on being the world's key currency.

CY 1998's 3.9 percent GDP growth followed 3.9 percent growth in 1997 and 3.4 percent growth in 1996. This is the best 3-year growth since 1984-1986. What is unusual is that this latest bout of robust growth occurred relatively late in an expansion, particularly a peacetime expansion. Furthermore, inflation not only remained in check in CY 1998, it actually decelerated somewhat. The GDP deflator increased by only 1.0 percent, while the CPI-U increased by 1.6 percent. The GDP inflation number was the lowest since 1959.

CY 1998's remarkable economic performance has surprised many economists, both inside and outside the forecasting profession. All year the professionals have been predicting that economic troubles in Asia (particularly Japan), Russia and Latin America would drag the economy down. In fact, turmoil in those areas has hurt U.S. exports and the balance of trade. U.S. exports grew by only 1.5 percent in CY 1998, the weakest growth in 15 years. This has depressed commodity prices and hurt the regions of the U.S. that depend on agriculture and energy. On the whole, however, the U.S. economy has weathered the foreign storms incredibly well due to great domestic strength.

After such a strong fourth quarter, most forecasters are backpedaling away from their prediction that the economy will slow significantly in the first quarter of CY 1999. The slowdown has been pushed back into the second quarter. The current expansion — 93 months through December 1998 — is the longest peacetime expansion on record. The longest previous peacetime expansion was the one right before the last recession: 92 months over the December 1982 through July 1990 period. If the economy makes it through 1999 without a downturn, it will threaten the longest expansion in wartime; 106 months over the March 1961 to December 1969 period.

The engines of growth in CY 1998 were consumer spending and domestic capital investment. Real consumer spending increased by 4.8 percent, the fastest increase in 14 years. Housing construction, already at a



high level, rose 10.4 percent, also the biggest increase in 14 years. Business investment in new equipment increased by 16.7 percent, offsetting a 0.7 percent decline in nonresidential construction. If the trade balance had not deteriorated so much, real GDP growth might have topped 5 percent. The last year of GDP growth equal to or above 5 percent was 1984 (coinciding with the previous peaks in consumer spending and housing).

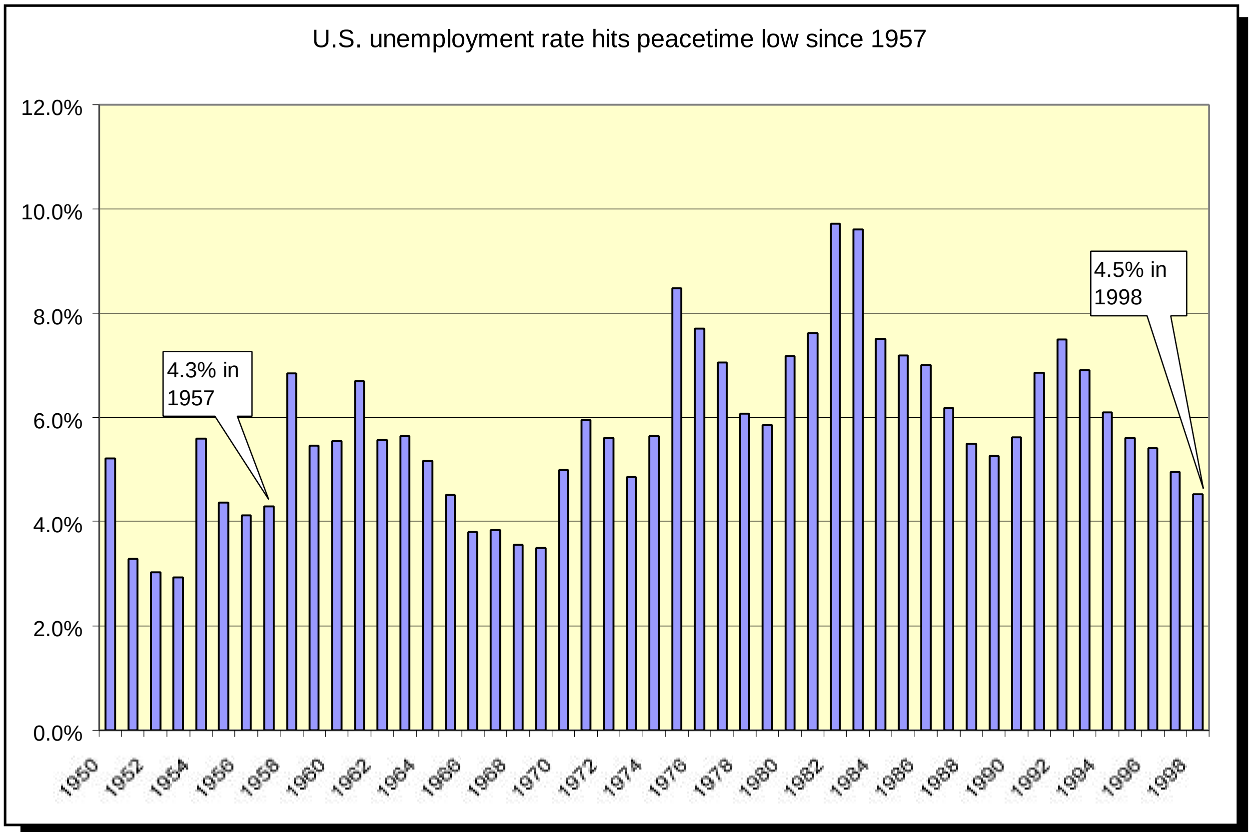
Much has been made of the low U.S. savings rate. Although real consumer spending increased 4.8 percent in CY 1998, real disposable income increased only 3.1 percent. This increase in consumption has been financed by borrowing, and by appreciation in asset prices. Savings as a share of after-tax income hit some historic lows last year:

(i) The U.S. savings rate was negative for two months in a row, and will probably be negative for the entire 4th quarter. The monthly negative saving rate is the first since 1934, in the midst of the Great Depression.
(ii) The savings rate for CY 1998 was 0.5 percent, the lowest since 1933.

Obviously, households have been financing part of their consumption out of increases in wealth resulting from increases in asset prices, particularly stock prices. Using the theory that households have wealth targets for retirement, college tuition, and other goals, and thus decrease saving from current income as asset prices appreciate, DRI estimates that the increase in the household net worth to income ratio of 4.5 to 6.0 has reduced the measured personal saving rate by 3.75 percentage points.

The lowest mortgage rates in three decades have also played a part. Many consumers have refinanced their mortgages and are now spending a part of their home equity.

The low saving rate is not the cause for alarm that some analysts have taken it to be. First of all, the national saving rate is more important than the personal savings rate. Second, changes to the National Income and Product Accounts (NIPA) have reduced the measured savings rate by about 1.0 percent, even with behavior unchanged. Third, the Bureau of Economic Analysis (BEA) does not include capital gains in personal income. If income were adjusted for capital gains, the measured saving rate would be higher. Finally, changing corporate behavior has skewed the measured savings rate. Dividends are at an all time low, so measured income is reduced. At the same time, increased corporate retained earnings have led to increases in share prices and



higher capital gains — not counted as income — and higher income tax payments. The measured savings rate deducts these tax payments from income, leading to a "double whammy" for the measured savings rate.

In CY 1999, as stock price growth slows due to reduced earnings, households will probably have to trim consumption growth back to equal income growth, which will slow, but not stop, the current expansion.

Finally, the labor market news has been very good, although rising wages and benefits are something of a double-edged sword. The combination of increasing labor costs and stable world output prices is squeezing U.S. profits. That aside, the jobs reports have been remarkable. There were three months during CY 1998 where the U.S. unemployment rate was 4.3 percent, the lowest rate since 1970.

For the year, unemployment averaged 4.5 percent, the lowest since 3.5 percent in 1969 during the Vietnam War. The 1998 mark was the lowest peacetime rate since 1957, when it averaged 4.3 percent. Employment increased by 2.9 million jobs in 1998, below the 3.4 million figure of 1997, but remarkable in the face of low world demand that caused job losses of almost 300,000 in mining and manufacturing.

The January outlooks of WEFA and DRI, which were released before the fourth quarter numbers became available, both have fairly high recession risks, although the risks are lower than during the autumn overseas financial crises. WEFA puts the probability of recession at 30 percent, with a start date at the end of CY 1999. DRI also has a 30 percent chance of a recession beginning in late 1999. WEFA places an additional 10 percent probability on a slow growth scenario where the economy does not actually go into recession, but slows sharply in CY 1999 and has extremely low growth in CY 2000. It will be interesting to see of the strong growth numbers from the end of the year change WEFA's or DRI's forecast of the probability, timing, or magnitude of a downturn. ❑

Status of the General Revenue Fund

REVENUES

— Frederick Church

At the halfway mark of FY 1999, tax revenues are $12.4 million over the revised estimate, with growth from last year of 5.8 percent. The personal income tax is $30.3 million over the revised estimate, with growth of 8.9 percent. The foreign insurance premium tax is $11.8 million over estimate, and the estate tax is $10.1 million over estimate. On the negative side, the corporate franchise tax is $16.3 million below estimate, and the public utility excise tax is $27.5 million below estimate.

In non-tax revenue, investment earnings are $27.8 million above estimate, and have increased by 30.4 percent from last year. Total non-federal revenue is $34.8 million above estimate, up 6.1 percent from last year.

Finally, federal grants are $22.6 million below estimate, but this is actually a smaller number than one would expect given the magnitude of the underspending in welfare and human services programs. Also, federal grants have risen 4.7 percent from last year despite the fact that welfare and human services spending has declined by 1.2 percent.

All in all, the revised forecasts up to this point have been quite accurate. Non-federal revenues are 0.5 percent higher than the estimate, and tax revenues deviate by only 0.2 percent.

Personal Income Tax

Growth in employer withholding revenue rebounded from a relatively anemic 6.1 percent in the first quarter of FY 1999 to 8.5 percent in the second quarter. Much of this growth actually came in one month — November was exceptionally strong (15.7 percent growth from last year), while October and December were rather weak. For CY 1998 as a whole, withholding growth was also 8.5 percent. This is quite a strong result considering that through No-

Table 2
General Revenue Fund Income
Actual vs. Estimate
Month of December, 1998
($ in thousands)

REVENUE SOURCE

TAX INCOME	Actual	Estimate*	Variance
Auto Sales	$54,444	$49,612	$4,832
Non-Auto Sales & Use	441,487	418,440	23,047
Total Sales	$495,931	$468,052	$27,879
Personal Income	$556,016	$561,550	($5,534)
Corporate Franchise	(67,737)	(20,021)	(47,716)
Public Utility	(508)	0	(508)
Total Major Taxes	**$983,702**	**$1,009,581**	**($25,879)**
Foreign Insurance	$3	$0	$3
Domestic Insurance	0	0	0
Business & Property	14	53	(39)
Cigarette	25,405	26,730	(1,325)
Soft Drink	0	0	0
Alcoholic Beverage	4,382	4,056	326
Liquor Gallonage	2,234	3,312	(1,078)
Estate	612	7,350	(6,738)
Racing	0	0	0
Total Other Taxes	$32,650	$41,502	($8,852)
Total Taxes	**$1,016,352**	**$1,051,082**	**($34,730)**
NON-TAX INCOME			
Earnings on Investments	$40,233	$23,000	$17,233
Licenses and Fees	871	2,000	(1,129)
Other Income	6,765	6,216	549
Non-Tax Receipts	$47,869	$31,216	$16,653
TRANSFERS			
Liquor Transfers	$14,000	$14,000	$0
Budget Stabilization	0	0	0
Other Transfers In	0	2,098	(2,098)
Total Transfers In	$14,000	$16,098	($2,098)
TOTAL INCOME less Federal Grants	**$1,078,221**	**$1,098,396**	**($20,175)**
Federal Grants	$295,979	$260,625	$35,354
TOTAL GRF INCOME	**$1,374,199**	**$1,359,021**	**$15,178**

* July, 1998 estimates of the Office of Budget and Management.

Detail may not add to total due to rounding.

Employer Withholding	CY 1998	CY 1999
January	595,270	554,290
February	477,040	450,091
March	461,910	415,432
April	465,902	406,725
May	441,799	427,697
June	474,384	406,658
July	474,062	465,449
August	472,641	424,206
September	451,672	428,164
October	475,912	469,423
November	513,446	443,963
December	544,958	500,814
Total	**5,848,996**	**5,392,912**
	8.5%	

vember, nonagricultural employment in Ohio had increased by only about 1.4 percent from last year. Clearly, the increase in withholding revenue is being fueled by wage increases, and perhaps by other forms of compensation such as stock option income. It also may be true that Ohio employment growth has been understated. The Ohio Bureau of Employment services (OBES) has made significant revisions in some prior years.

In spite of the rebound in withholding growth, that's not where the year-to-date overage lies. Withholding revenue is actually $1.0 million below estimate for the year. As the table below should make clear, the surplus so far is the result of very strong quarterly estimated payments and annual returns. Lower than anticipated refunds have also contributed to the overage.

As we mentioned in last month's issue of this report, the final quarterly estimated payment against taxable year 1998 liability (due January 15th) often serves as a bellwether for tax filing season revenues. If taxpayers look back on 1998 and realize that there non-wage income was greater than originally anticipated, and so they owe additional tax, then the final quarterly payment will be higher than estimated. In that case, it is also often true that annual returns will also exceed the estimate and that refunds will fall short of the estimate. However, if the converse is true and the final quarterly payment comes in low because taxpayers have received a negative surprise in their income, then generally the filing season tax collections are disappointing also. Based on the early return data for January, the final estimated payment is going to exceed even the revised estimate. LBO, OBM, and the Department of Taxation all estimated strong increases in estimated payments for FY 1999, with the final figure being 16.4 percent for the whole year. It now appears that even this optimistic estimate was too low. If past patterns hold, this indicates a strong filing season and another overage for the income tax by year's end.

Corporation Franchise Tax

First of all, December franchise tax receipts were -$67.7 million. The estimate had assumed negative revenues for the month, but only -$20.0 million. So, December showed a whopping $47.7 million shortfall. Last month's issue of ***Budget Footnotes*** described in some detail how the Treasurer of State (TOS) had been charging franchise tax refunds against the non-auto sales tax. The correction came in December. In reality, the franchise tax overages that had appeared up until December were illusory, and several months worth of refunds were packed into one month.

FY 1999 Income Tax Collections, by Component
amounts in milions of dollars

Component	Actual	Estimate	Variance	Yr-Over-Yr Growth
Employer withhholding	$2,933.8	$2,934.8	($1.0)	7.3%
Quarterly estimated payments	$390.8	$371.8	$19.0	16.4%
Annual Tax Payments	$75.6	$60.5	$15.1	24.2%
Refunds	($67.3)	($72.5)	$5.2	-9.9%
Total Major Components	$3,332.8	$3,294.6	$38.2	
Total All Components	$3,350.4	$3,311.7	$38.7	8.9%
Total GRF Amount	$2,994.1	$2,963.8	$30.3	8.9%

The result of the refunds is that year-to-date revenues are $16.3 million below estimate. At this point in the year, we usually say that any shortfall or surplus in the corporate franchise tax is insignificant. The reason is that revenues in the July through December period are from late payments and audit findings, with refunds subtracted out. So, everything in the

Table 3
General Revenue Fund Income
Actual vs. Estimate
Fiscal Year-to-Date 1999
($ in thousands)

REVENUE SOURCE					
TAX INCOME	Actual	Estimate*	Variance	FY 1998	Percent Change
Auto Sales	$375,119	$367,296	$7,823	$355,485	5.52%
Non-Auto Sales & Use	2,377,753	2,380,880	**(3,127)**	2,273,628	4.58%
Total Sales	$2,752,871	$2,748,176	**$4,695**	$2,629,113	4.71%
Personal Income	$2,994,126	$2,963,822	**$30,304**	$2,750,026	8.88%
Corporate Franchise	4,925	21,235	(16,310)	7,622	-35.38%
Public Utility	201,960	229,500	**(27,540)**	229,151	-11.87%
Total Major Taxes	$5,953,882	$5,962,733	($8,851)	$5,615,911	6.02%
Foreign Insurance	$148,332	$136,500	$11,832	$146,908	0.97%
Domestic Insurance	39	237	(198)	435	-91.03%
Business & Property	137	598	(461)	455	-69.97%
Cigarette	138,777	138,699	78	137,564	0.88%
Soft Drink	2	0	2	0	1400.00%
Alcoholic Beverage	27,369	26,676	693	26,464	3.42%
Liquor Gallonage	13,635	14,409	(774)	13,437	1.48%
Estate	57,857	47,775	10,082	49,941	15.85%
Racing	0	0	0	0	#N/A
Total Other Taxes	$386,147	$364,895	$21,252	$375,204	2.92%
Total Taxes	**$6,340,029**	**$6,327,628**	**$12,401**	**$5,991,115**	**5.82%**
NON -TAX INCOME					
Earnings on Investments	$85,270	$57,500	$27,770	$65,402	30.38%
Licenses and Fees	16,293	18,780	(2,487)	17,303	-5.84%
Other Income	46,836	49,718	(2,882)	55,457	-15.55%
Non-Tax Receipts	$148,398	$125,998	$22,400	$138,162	7.41%
TRANSFERS					
Liquor Transfers	$48,000	$46,000	$2,000	$46,000	4.35%
Budget Stabilization	0	0	0	$0	#N/A
Other Transfers In	16,313	18,348	(2,035)	1,928	746.11%
Total Transfers In	$64,313	$64,348	($35)	$47,928	34.19%
TOTAL INCOME less Federal Grants	**$6,552,740**	**$6,517,974**	**$34,766**	**$6,177,205**	**6.08%**
Federal Grants	$1,753,816	$1,776,422	($22,606)	1,675,307	4.69%
TOTAL GRF INCOME	**$8,306,555**	**$8,294,396**	**$12,159**	**$7,852,512**	**5.78%**

* July, 1998 estimates of the Office of Budget and Management.

Detail may not add to total due to rounding.

July through December period reflects prior tax year activity. The payments against tax year 1998 liability will come at the end of January, March, and May. Revenues received so far this fiscal year reflect reconciliations of liability from taxable year 1997, and from even earlier years.

This year, however, the shortfall in the franchise tax may be a bellwether for a disappointing fiscal year. The reason is that when these recent refunds are subtracted from FY 1998 payments, net growth over FY 1997 is close to zero. If FY 1998 had zero payment growth while CY 1997 before-tax U.S. corporate profits grew 8.0 percent, what can we expect in FY 1999? CY 1998 before-tax profits are estimated to have fallen by 1 percent to 2 percent. Does this mean that FY 1999 baseline franchise tax payments will decline? Also, there were a number of franchise tax changes in the last budget bill (HB 215) that reduced franchise tax revenues. Of particular interest is the cap on the net worth base for the tax. Without the net worth base to fall back on when net income

Changes in Public Utility Taxes Owed, Tax Years 1997 - 1998

UTILITY CLASS	1997 Tax	1998 Tax	Change
Electric Light	$435,441,740	$432,592,427	($2,849,313)
Rural Electric	$17,183,490	$17,409,671	$226,181
Total Electric Power	$452,625,230	$450,002,098	($2,623,132)
Natural Gas	$124,902,926	$115,771,587	($9,131,339)
Pipeline	$485,962	$495,712	$9,750
Total Natural Gas	$125,388,888	$116,267,299	($9,121,589)
Telephone	$107,893,555	$107,670,677	($222,878)
All Other	$4,097,952	$4,088,052	($9,900)
Grand Total	$690,005,625	$678,028,126	($11,977,499)

The five enumerated classes of utility accounted for over 99% of public utility excise tax owed for tax year 1998.

Source: Ohio Department of Taxation

declines, franchise tax revenues will become more volatile. At this point it seems that the expected overage in the personal income tax may be partly offset by a shortfall in the franchise tax.

Public Utility Excise Tax

The public utility excise tax is $27.5 million below estimate, and the shortfall will probably get somewhat bigger by year's end. The shortfall has two components, a shortfall in the estimated payments against tax year 1999 liability, and negative reconciliations of tax year 1998 liability (i.e. refunds) with tax year 1998 estimated payments.

GRF public utility tax revenues were -$14.9 million in November and December (including LGFs, the amount was -$15.6 million). This was because the certified tax liability for tax year 1998 (May 1997 through April 1998 for utilities other than telephone and telegraph companies) was lower than for tax year 1997. So, the estimated payments that utilities made for tax year 1998, which were for the most part based on their tax year 1997 liability amounts, were too high. The reconciliation of estimated payments with what was actually owed resulted in $14.9 million in net refunds.

The first of the three estimated payments against tax year 1999 liability, made in October (the others are due at the beginning of March and of June) was also below the estimate. A strict reading of the law says that utilities should have made their first tax year 1999 payment equal to 1/3 of their actual tax year 1997 taxes. However, as in past years, it appears that the first payment actually was closer to 1/3 of the lower 1998 tax liability amount. Because tax liability fell in tax year 1998, we can expect the last two estimated payments for FY 1999 to be slightly below estimate also. It appears likely that the public utility tax will end the year roughly $35 million below estimate.

The table below shows how the amount of tax owed by different classes of utilities changed from 1997 to 1998.

As one can see, all of the "Big Three" industries declined in tax year 1998, with the biggest fall coming in natural gas. Based on the available quarterly energy price data, it appears that price declines between tax year 1997 and tax year 1998 contributed to reducing gross receipts tax revenues from natural gas. ❑

DISBURSEMENTS

*— Jeffrey E. Golon**

Table 4
General Revenue Fund Disbursements
Actual vs. Estimate
Month of December, 1998
($ in thousands)

USE OF FUNDS			
PROGRAM	Actual	Estimate*	Variance
Primary & Secondary Education (1)	$432,911	$398,912	$33,999
Higher Education	$177,955	$155,611	$22,344
Total Education	$610,866	$554,523	$56,343
Health Care/Medicaid	$433,261	$446,144	($12,883)
Temporary Assistance to Needy Families	$82,630	$93,361	($10,731)
General/Disability Assistance	$3,296	$4,874	($1,578)
Other Welfare	$29,740	$32,646	($2,906)
Human Services (2)	$71,919	$83,839	($11,921)
Total Welfare & Human Services	$620,845	$660,865	($40,019)
Justice & Corrections	$101,906	$144,742	($42,836)
Environment & Natural Resources	$9,233	$6,513	$2,720
Transportation	$7,580	$2,524	$5,056
Development	$14,743	$10,560	$4,183
Other Government (3)	$24,172	$30,468	($6,296)
Capital	$206	$612	($406)
Total Government Operations	$157,840	$195,419	($37,579)
Property Tax Relief (4)	$42,025	$96,484	($54,459)
Debt Service	$0	$0	$0
Total Program Payments	**$1,431,576**	**$1,507,291**	**($75,716)**
TRANSFERS			
Local Govt Distribution	$0	$0	$0
Budget Stabilization	$0	$0	$0
Other Transfers Out	$100	$0	$100
Total Transfers Out	$100	$0	$100
TOTAL GRF USES	**$1,431,676**	**$1,507,291**	**($75,616)**

(1) Includes Primary, Secondary, and Other Education.
(2) Includes Mental Health, Mental Retardation and Developmental Disabilities, and Other Human Services.
(3) Includes Regulatory and Nonregulatory agencies, Pension Subsidies, and Reissued Warrants.
(4) Includes property tax rollbacks, homestead exemption, and tangible property tax exemption.

* August, 1998 estimates of the Office of Budget and Management.

Detail may not add to total due to rounding.

Juxtaposed in dramatic contrast to Ohio's wintering citizenry — which has been alternately enjoying and enduring an uneven mix of balmy temperatures, heavy rains, and snowy deep freezes perpetrated by disruptions in the ocean-atmosphere system in the tropical Pacific — is the state's GRF budget, which has been basking in the relative comfort of Belize. Now, what could that possibly mean? It means that state GRF spending as a whole has not bounced between positive and negative monthly disbursement variances as a month or two of overages self-corrects for a month or two of underages, or vice versa. Instead, the state has ridden through a five-month parade of negative disbursement variances that have allowed it to accumulate a year-to-date underage in GRF spending that now totals $479.8 million. As the state motors through the latter half of FY 1999, some pieces of this year-to-date underage will dissipate, while others will gather steam. We fully expect, however, that the latter force (steam) will outgun the former force (dissipation). The net effect of that disbursement battle will be that the year-to-date underage will continue to grow, which should in turn considerably strengthen the state's cash flow as we head into the next millennium.

December Variance. Excluding transfers, December closed with a negative disbursement variance of $75.7 million, considerably smaller than that number would have otherwise been had it not been for a

$56.3 million overage chipped in from the Education program category. Two components of state spending dominated the December underage — Property Tax Relief ($54.5 million) and the Department of Rehabilitation and Correction ($36.4 million) — and alone produced underspending totaling $90.9 million. When combined with a host of smaller underages totaling $40.0 million in the Welfare and Human Services program category, led by Healthcare/Medicaid ($12.9 million) and the Temporary Assistance to Needy Families (TANF) program ($10.7 million), December underspending attributable to certain areas of the state budget totaled over $130 million. The underages in Property Tax Relief and Department of Rehabilitation and Correction disbursements were essentially no more than matters of timing, while the Medicaid and TANF programs appeared to generate some amount of true savings as declines in certain human services caseloads continued to constrain spending below expectations. Some elements of the monthly underage in Medicaid were also timing-based in service categories related to payments to HMOs and physicians.

As noted, a $56.3 million overage in the Education program category managed to somewhat dilute the eventual size of December's underage. Two state agency budgets lodged within the Education program category were responsible for what were timing-based monthly overages: the Department of Education ($34.0 million) and the Board of Regents ($22.3 million).

Table 4, on the previous page, provides the larger picture of December disbursement variances by program category.

Year-to-Date Variance. December's underspending pushed the negative year-to-date disbursement variance, excluding transfers, up to yet another high-water mark for FY 1999: $479.8 million.

There were six principal contributors to the year-to-date underage: (1) the HealthCare/Medicaid program ($138.9 million); (2) Primary and Secondary Education ($88.4 million), most specifically the Department of Education ($90.2 million); (3) Justice & Corrections ($86.9 million), mostly from the Department of Rehabilitation and Correction ($70.3 million); (4) the Temporary Assistance to Needy Families (TANF) program ($78.2 million); (5) the Other Welfare program category, which consists entirely of the Department of Human Services exclusive of the Medicaid, TANF, and General/Disability Assistance programs ($53.4 million); and (6) the Other Government program category ($36.6 million), largely emanating from the Department of Administrative Services ($23.8 million). The disbursement variances associated with the departments of Education, Human Services, and Justice & Corrections were principally the result of timing. In the case of the Medicaid and TANF programs and the Department of Administrative Services, issues of timing were most likely mixing with true spending reductions to produce underages. Declining caseloads in certain service areas of the Medicaid and TANF programs were holding some spending in check, while other underages in these two programs were timing-based. And in the matter of the Department of Administrative Services, underspending largely reflected a combination of savings in expected debt service and other building operating payments, as well as unexpectedly sluggish disbursements relative to various computing and communications projects.

A more detailed picture comparing fiscal year-to-date variances by program category is provided for the reader in Table 5, which appears on the following page.

Federal Money. Of the year-to-date underspending in the TANF and Medicaid programs combined ($217.1 million), 57.9 percent, or $125.7 million, was in the federal share of these two human services programs that are jointly funded by the state and federal government. Furthermore, roughly two-thirds of this underspending in the federal share — $80.9 million (64.4 percent) — was exclusively attributable to Medicaid. Once the federal money associated with TANF and Medicaid was backed out, the year-to-date underspending in non-federal state money was reduced to $354.1 million from $479.8 million.

The usual caveat applies to this discussion of federal money. Any federal TANF money unspent at fiscal year's end really represents money the state will have earned by meeting its required maintenance of effort (MOE). On the other hand, an underage in Medicaid really signals a loss of anticipated revenue since the state will not have spent the money necessary to earn financial reimbursement from the federal government.

Table 5
General Revenue Fund Disbursements
Actual vs. Estimate
Fiscal Year-to-Date 1999
($ in thousands)

USE OF FUNDS

PROGRAM	Actual	Estimate*	Variance	FY 1998	Percent Change
Primary & Secondary Education (1)	$2,474,424	$2,562,843	(88,419)	$2,359,307	4.88%
Higher Education	1,229,303	1,210,998	18,304	1,156,985	6.25%
Total Education	$3,703,727	$3,773,841	(70,115)	3,516,292	5.33%
Health Care/Medicaid	$2,622,420	$2,761,389	(138,969)	$2,614,700	0.30%
Temporary Assistance to Needy Families	426,504	504,682	(78,179)	464,988	-8.28%
General/Disability Assistance	29,301	38,486	(9,185)	30,215	-3.02%
Other Welfare	216,878	270,273	(53,395)	236,592	-8.33%
Human Services (2)	618,493	633,346	(14,853)	615,171	0.54%
Total Welfare & Human Services	$3,913,595	$4,208,178	(294,583)	$3,961,666	-1.21%
Justice & Corrections	$812,459	$899,363	(86,904)	$773,924	4.98%
Environment & Natural Resources	79,789	75,184	4,605	78,515	1.62%
Transportation	17,326	13,339	3,987	11,360	52.51%
Development	68,480	68,016	464	66,340	3.23%
Other Government (3)	210,853	247,403	(36,550)	201,762	4.51%
Capital	2,133	3,247	(1,114)	2,341	-8.87%
Total Government Operations	$1,191,041	$1,306,552	(115,512)	$1,134,242	5.01%
Property Tax Relief (4)	$535,585	$535,102	483	$511,312	4.75%
Debt Service	91,503	91,553	(51)	81,170	12.73%
Total Program Payments	**$9,435,450**	**$9,915,227**	**(479,777)**	**$9,204,682**	**2.51%**
TRANSFERS					
Capital Reserve	$0	$0	0	$0	——
Budget Stabilization	44,184	44,184	(0)	34,400	28.44%
Other Transfers Out	973,579	967,560	6,019	723,235	34.61%
Total Transfers Out	$1,017,763	$1,011,744	6,019	$757,635	34.33%
TOTAL GRF USES	**$10,453,213**	**$10,926,971**	**(473,758)**	**$9,962,317**	**4.93%**

(1) Includes Primary, Secondary, and Other Education.
(2) Includes Mental Health, Mental Retardation and Developmental Disabilities, and Other Human Services.
(3) Includes Regulatory and Nonregulatory agencies, Pension Subsidies, and Reissued Warrants.
(4) Includes property tax rollbacks, homestead exemption, and tangible property tax exemption.

* August, 1998 estimates of the Office of Budget and Management.

Detail may not add to total due to rounding.

For those readers who care to venture ahead, additional details on certain areas of state spending await your scrutiny.

Primary & Secondary Education

Education. The Department of Education closed the month of December with a $32.5 million spending overage, 8.3 percent above the estimate. This was the first monthly overage posted by the department in FY 1999, the practical effect of which was to chisel its year-to-date underspending from a high-water mark of $122.7 million, just set in November, down to $90.2 million. While timing was the key factor behind the December spending surge, delays in implementing the new SF-3 foundation payment formula continued to be the main force behind the negative year-to-date disbursement variance. On the latter matter, the department worked over the course of the first four months of FY 1999 on the installation of

Table 6
Detailed FY 1999 School Foundation Payment Underage
($ in millions)

Line Item Number	Line Item Name	Estimated Disbursement	Actual Disbursement	Disbursement Variance	Percent Variance
200-500	School Finance Equity	$68.3	$66.5	-$1.8	-2.5%
200-501	Base Cost Funding	$1,536.7	$1,530.0	-$6.7	-.0.4%
200-502	Pupil Transportation	$127.4	$93.9	-$33.5	-26.3%
200-520	DPIA	$192.3	$176.0	-$16.3	-8.4%
200-521	Gifted Pupil	$17.8	$17.6	-$0.2	-0.8%
	Total	$1,942.5	$1,884.0	-$58.5	-3.0%

the SF-3 funding formula. In the interim, foundation payments to school districts were disbursed based on their FY 1998 funding amounts, which temporarily constrained foundation spending below expectations. The significant programming efforts required by the new foundation formula also slowed disbursements on some other non-foundation programs as well. In late October, the department began to disburse foundation payments via the SF-3 funding formula, which means that underspending ascribed to the new formula implementation delays should largely resolve itself in the second half of FY 1999.

Monthly Overages. The nonpublic administrative cost reimbursement and bus purchase allowance programs combined to land a $72.0 million overage in the month of December. This was an expected spending spike rather than a surprise discovery. As the reader may recall, we noted in the October and November/December issues of ***Budget Footnotes***, an estimated $28.0 million in school bus purchase subsidy funding (line item 200-503, Bus Purchase Allowance) was not disbursed in September as originally planned. And then in the November/December issue of ***Budget Footnotes***, we also called attention to the fact that the entire $44.3 million FY 1999 appropriation for nonpublic administrative cost reimbursement (line item 200-532, Nonpublic Administrative Cost Reimbursement) was not released in November as planned. As a result, the Controlling Board ended up approving release of these two pools of funding at its early December meeting, later than was originally assumed. This delayed action triggered the significant spending overages we witnessed in these two programs for the month of December.

Monthly Underages. The effect of this rather massive $72.0 million December overage attributable to the nonpublic administrative cost reimbursement and the school bus purchase allowance programs on the department's monthly disbursement variance was in turn almost halved by underspending posted in the pupil transportation and post-secondary/adult vocational education programs. Due to timing, these latter two programs chipped in a combined underage of $33.1 million in December.

Line item 200-502, Pupil Transportation, contains $231.6 million in FY 1999 to reimburse school districts for a portion of the costs they incur in the transportation of students to and from school; in FY 1997, the state's reimbursement funding covered, on average, about 32 percent of a school district's total pupil transportation cost. Within the line item in FY 1999, up to $27.0 million is set aside for handicapped transportation. The disbursement of this earmarked handicapped transportation funding did not occur in December as originally anticipated. Instead, the handicapped transportation funding is likely to be disbursed in February.

Line item 200-514, Post-Secondary/Adult Vocational Education, provides $20.7 million in FY 1999 funding in support mostly of full-time and part-time adult vocational training programs targeting three types of persons: (1) those who have completed secondary education and have entered the job market; (2) those who are experienced, but in need of short-term technical skill upgrading; or (3) those that have reentered the workforce after long absences. School districts, joint vocational school districts, and other educational institutions are eligible for funding. The funding is distributed via a unit formula. One unit is composed of 900 hours of program services and receives $20,000 in state funding. The department generally makes payments on a quarterly basis, with an adjustment at the end of a fiscal year. This fiscal year's second quarter payment, estimated in excess of $5 million, did not occur in December as planned. A January disbursement date now seems very likely.

Year-to-date Underage. Unsurprisingly, the five SF-3 foundation payment line items were major contributors to the department's $90.2 million year-to-date underage, contributing $58.5 million worth in underspending that is detailed in Table 6, which appears on the previous page. Pupil transportation cost reimbursement (line item 200-502) alone accounted for more than 55 percent of the year-to-date foundation payment underage.

DPIA Kindergarten Update. As indicated in the November/December issue of ***Budget Footnotes***, the falling Ohio Works First (OWF) caseload was not the factor in the DPIA underspending. Instead, timing played a key role in this matter too. The DPIA program was restructured by the 122nd General Assembly and the funding was also increased substantially over the FY 1998 level. The first quarter FY 1999 payments, however, were made based on the FY 1998 funding amounts. This was why the DPIA spending was under the year-to-date estimate by $16.3 million. As of this writing, the department is planning to do a catch-up DPIA payment in January, which should reduce the year-to-date underage in the DPIA program.

The appropriation for the all-day and everyday kindergarten program was made by assuming that all 104 eligible school districts would provide all-day and everyday kindergarten at the 100 percent level. An eligible school district, however, receives funding based on its actual all-day and everyday kindergarten percentage. Therefore, based on the current actual all-day and everyday kindergarten percentage data reported by school districts, it appeared that appropriations might exceed the needed funding for all-day and everyday kindergarten program by approximately $17 million in FY 1999. Meanwhile, the department has recently sent out surveys to see why some eligible districts opt for providing less than 100 percent or zero percent of all-day and everyday kindergarten. The survey information should be available in the near future. (For additional information on DPIA kindergarten, see the article in this issue authored by our colleague Wendy Zhan.)

Other Underages. Some other non-foundation line items contributing to the department's year-to-date underspending were discovered as follows: (1) $6.8 million in line item 200-507, Vocational Education; (2) $5.4 million in Post-Secondary/Adult Vocational Education; (3) $5.2 million in line item 200-504, Special Education; (4) $4.7 million in line item 200-540, Special Education Enhancements; (5) $3.9 million in line item 200-558, Emergency Loan Interest Subsidy; (6) $3.4 million in line item 200-546, Charge-off Supplement; (7) $3.3 million in line item 200-545, Vocational Education Enhancements; and (8) $3.1 million in line item 200-547, Power Equalization.

Funding for school districts' special and vocational education programs has been merged into line item 200-501, Base Cost Funding, beginning with FY 1999. Line items 200-507, Vocational Education, and 200-504, Special Education, carried only prior years' encumbrances. The underspending in these two line items was largely due to the fact that the department has not yet made the final FY 1998 foundation payment (SF-12) adjustments. These two items were part of the foundation (SF-12) items in FY 1998. The department is currently planning to perform the final calculation adjustments in February.

Both the charge-off supplement and power equalization line items displayed limited year-to-date disbursement activity. As both line items are tied to newly enacted programs, finding signs of underspending in these two programs was not surprising, nor particularly troubling. The underspending in these two programs should be reduced in the second half of FY 1999.

The Emergency Loan Interest Subsidy Program. The emergency loan interest subsidy (line item 200-558) is another newly established program. After six months, we still have not seen any disbursement activity in this line item. Although new programs typically have a slow start, it appeared that this particular item had a statutory problem too. The law requires the department to use the funding ($8.5 million in FY 1999) to distribute a subsidy to every district that, during the **preceding calendar year**, paid and was obligated to pay interest on an existing emergency school loan in excess of two percent simple interest. However, the emergency school loans were obtained on the **fiscal year** basis. It also appeared that the original legislative intent was to make payments based on the **current fiscal year**. As of this writing, the department is not planning to make any payment until the 123rd General Assembly clarifies the program statute. Therefore, this program is likely to continue to be a contributor to the department's monthly and year-to-date underspending in the next few months.

Health Care/Medicaid

Medicaid's December spending totaled $433.3 million, which represented a negative deviation of $12.9 million, or 2.9 percent, from the estimated monthly total of $446.1 million. This negative monthly disbursement variance further boosted Medicaid's year-to-date GRF underage to $138.9 million, or 5.0 percent, below the estimate at the half-year mark of FY 1999. (For more detail on monthly and year-to-date Medicaid spending, as well as a comparison to FY 1998 spending, see Tables 7 and 8, respectively.)

Buy-In. Although Medicaid's total underspending for the month was relatively small, it was in fact masked by a catch-up payment made for the Medicare Buy-In. As we had anticipated, a previously delayed Medicare Buy-In payment occurred in December. If this Buy-In payment had been made earlier as planned, then Medicaid's December underspending would actually have been about $10.0 million higher.

December Underage. In December, the service category tied to HMO payments again contributed the single largest amount ($16.1 million) to underspending, as it has all year. Also contributing to Medicaid's December underspending were the service category payments tied to Nursing Homes ($4.4 million) and Physicians ($2.3 million).

Year-to-date Underage. Medicaid's year-to-date underage was primarily the result of $91.1 million in underspending in the HMO payment service category, accounting for 65.5 percent of the total underage. A surprising twist in Medicaid's year-to-date underage was a $35.8 million contribution tossed in by the Nursing Homes payment service category. (As seasoned Medicaid watchers know, this negative disbursement variance in the Nursing Homes service category can easily be wiped out in a single month, which means we will keep a close eye on this itemized expense in the months ahead.)

Eligibles. At FY 1999's halfway mark, the Medicaid eligible caseload continued its downward trend. The six-month average number of Medicaid eligibles in FY 1999, 1.04 million persons, represented a decline of 2.1 percent from the average monthly number of Medicaid eligibles for all of FY 1998. When compared to the same six-month period in FY 1998, the six-month average number of Medicaid eligibles in FY 1999 had dropped by 2.7 percent.

Table 7
Medicaid (400-525) Spending in FY 1999

	December '98				Year-to-Date Spending	
Service Category	**Actual**	**Estimate**	**Variance**	**Percent Variance**	**Actual** ** **thru' Dec.**	**Estimate** ** **thru' Dec.**
Nursing Homes	$166,187,902	$170,611,171	($4,423,269)	-2.6%	$991,044,978	$1,026,832,951
ICF/MR	$28,439,005	$28,215,985	$223,020	0.8%	$171,916,122	$169,560,807
Hospitals	$89,314,591	$87,400,608	$1,913,983	2.2%	$607,870,497	$594,893,202
Inpatient Hospitals	$66,326,202	$67,967,569	($1,641,367)	-2.4%	$464,491,047	$461,589,464
Outpatient Hospitals	$22,988,388	$19,433,039	$3,555,349	18.3%	$143,379,450	$133,303,738
Physicians	$19,084,973	$21,416,626	($2,331,653)	-10.9%	$141,287,043	$143,406,803
Prescription Drugs	$53,712,414	$54,897,707	($1,185,293)	-2.2%	$293,045,048	$298,361,651
Payments	$54,374,304	$56,023,932	($1,649,629)	-2.9%	$356,689,976	$356,831,626
Rebates	$661,890	$1,126,225	($464,335)	-41.2%	$63,644,929	$58,469,975
HMO	$29,164,771	$45,229,558	($16,064,787)	-35.5%	$180,036,891	$271,104,979
Medicare Buy-In	$20,258,440	$9,431,094	$10,827,346	114.8%	$60,750,227	$56,193,075
All Other***	$28,965,643	$28,941,239	$24,404	0.1%	$178,336,138	$201,040,891
TOTAL	$435,127,738	$446,143,987	($11,016,250)	-2.5%	$2,624,286,944	$2,761,394,360
CAS	$433,260,650		($12,883,337)	-2.9%	$2,622,419,657	
Est. Federal Share	$253,374,882	$259,789,644	($6,414,762)		$1,528,122,288	$1,607,959,936
Est. State Share	$181,752,856	$186,354,343	($4,601,487)	-2.5%	$1,096,164,657	$1,153,434,424

* This table only includes Medicaid spending through Human Services' 400-525 line item.

** Includes spending from FY 1998 encumbrances in service categories for July & in the All Other category for August & September.

*** All Other, includes all other health services funded by 400-525.

Source: BOMC 8300-R001 Reports, Ohio Department of Human Services.

Table 8
FY 1999 to FY 1998 Comparison* of Year-to-Date Spending

Service Category	FY 1999[1] Yr.-to-Date as of Dec. 98	FY 1998 Yr.-to-Date as of Dec. 97	Variance	Percent Variance
Nursing Homes	$991,044,978	$962,971,317	$28,073,661	2.9%
ICF/MR	$171,916,122	$164,768,161	$7,147,961	4.3%
Hospitals	$607,870,497	$577,725,690	$30,144,807	5.2%
Inpatient Hospitals	$464,491,047	$446,320,150	$18,170,897	4.1%
Outpatient Hospitals	$143,379,450	$131,405,540	$11,973,910	9.1%
Physicians	$141,287,043	$138,874,560	$2,412,483	1.7%
Prescription Drugs	$293,045,048	$257,885,552	$35,159,496	13.6%
Payments	$356,689,976	$308,392,805	$48,297,171	15.7%
Rebates	$63,644,929	$50,507,253	$13,137,676	26.0%
HMO	$180,036,891	$283,426,776	($103,389,885)	-36.5%
Medicare Buy-In	$60,750,227	$71,459,475	($10,709,248)	-15.0%
All Other***	$178,336,138	$157,588,851	$20,747,287	13.2%
TOTAL	$2,624,286,944	$2,614,700,382	$9,586,562	0.4%
Est. Federal Share	$1,528,122,288	$1,527,638,698	$483,589	0.0%
Est. State Share	$1,096,164,657	$1,087,061,684	$9,102,973	0.8%

* This table only includes Medicaid spending through Human Services' 400-525 line item.
1. Includes FY 1998 encumbraces of $54 million.

The driving force behind the falling caseload has been the significant drop in the largest subset of the Medicaid eligible population best described as Ohio Works First (OWF), non-Healthy Start (HS) eligible, who account for roughly one-half of the Medicaid eligible population. This OWF, non-Healthy Start eligible population has declined by 12.0 percent from FY 1998 levels to a monthly average of 511,111 persons. When compared to the same six-month period in FY 1998, the six-month average of OWF, non-Healthy Start eligibles in FY 1999 declined by 15.1 percent.

Of the average number of monthly OWF, non-Healthy Start eligibles in FY 1999 (511,111), about 170,919, or 33.4 percent, were in "transitional status," now referred to as "low-income" Medicaid eligibles.

For the first six months of FY 1999, the second largest segment of the Medicaid eligible population, the Aged, Blind and Disabled, who account for approximately 30.0 percent of the Medicaid eligible population, posted a monthly average caseload that was only 1.4 percent smaller than the average monthly caseload for all of FY 1998.

The decline in cash assistance recipients in Ohio Works First (OWF) has resulted in a change in the composition of the Medicaid caseload. The Aged, Blind, and Disabled (ABD) eligible population, who comprised less than 28.0 percent of the more than 1.2 million Medicaid eligible population in FY 1996, generated over 70.0 percent of Medicaid's spending. By 1998, however, the ABD population comprised 32.0 percent of the nearly 1.1 million Medicaid eligible population and generated about 76.0 percent of Medicaid's spending. This change in composition resulted in a higher cost per Medicaid eligible. The cost of long-term care was the primary reason for the relatively higher expense associated with the ABD population. This increase in the ABD population was a result of a natural shift and not the result of any policy changes.

The importance of this shift is that, as the OWF population, which accounted for about 30.0 percent of Medicaid spending, has declined rapidly, it has contributed significantly to slowing the growth of Medicaid costs, as evidenced by underspending in the HMO service category, a service category where all but a handful of the recipients are part of the OWF population. The ABD group, on the other hand, heavily utilizes some of the services with the fastest growing costs, such as prescription drugs, which have held fairly stable so far.

In sum, we have experienced a favorable slowing in the growth of Medicaid expenditures, but, as a result of the program's changing caseload composition, we could see some big increases triggered in the not-too-distant future.

TANF

TANF posted its fourth consecutive negative monthly disbursement variance with a December underage of $10.7 million, which was 11.5 percent below the monthly estimate. This disbursement variance was due largely to the continued decline in the cash assistance caseload. The number of cash recipients fell by over 6,000 in December, and has dropped by about 47,000 recipients since the beginning of the fiscal year. Year-to-date, TANF spending stood at $78.2 million below the estimate, which amounted to a negative disbursement variance of 15.5 percent.

General/Disability Assistance

For the month of December, the General/Disability Assistance (GA/DA) program registered disbursements that were $1.6 million below the monthly estimate, which represented a 32.4 percent negative variance. A rather sizeable chunk of this underage stemmed from an accounting adjustment in which close to $1 million was returned to the GA/DA line item 400-511. These GRF funds had been temporarily tapped in October to cover a federal grant that was unexpectedly late.

Year-to-date, the disbursement variance was $9.2 million, or 23.9 percent, below the estimate. The bulk of the year-to-date variance was due largely to the fact that the estimate assumed $6.1 million would be disbursed in September to settle the Taber lawsuit. That planned disbursement has yet to occur, and will not until later in the fiscal year. (For a more detailed discussion of the Taber lawsuit, see our July/August, 1998 issue.)

The remainder of the underage in the GA/DA program was attributable to the steady decline in the DA caseload. At the close of December, the DA caseload was hovering at just over 10,200 recipients, down from approximately 11,500 at the beginning of the fiscal year. This represented a caseload reduction of 11.3 percent, or 1,300 recipients.

Other Welfare

The Other Welfare component of the Welfare and Human Services program category is composed entirely of all of the Department of Human Services' operating expense and subsidy programs, exclusive of Medicaid, TANF, and General/Disability Assistance, which are tracked as separate components under the Welfare and Human Services program category as well. This month we thought it appropriate to check up on a food stamp program that the department initiated roughly one year ago.

Stamps Traded for Services. A new GRF-funded food stamp program was created in January 1998 to serve a portion of Ohio's immigrant population who lost food stamp assistance as a result of changes in federal law. This money was made available for the new program through a Controlling Board-authorized transfer of $1.0 million and $4.0 million in FY 1998 and FY 1999 appropriation authority, respectively, from the Disability Assistance line item (400-511) to a new line item 400-414, State Option Food Stamp Program. (For a more detailed discussion of the establishment of this program, see the article entitled "Controlling Board Approves State Food Stamp Program" authored by our colleague Steve Mansfield that appeared in the February, 1998 issue of ***Budget Footnotes***.)

The program began operation on April 1, 1998 and managed to disburse only $315,294 in the last three months of FY 1998, which left $684,706 in line item 400-414's available balance at the close of the fiscal year.

In late June 1998, President Clinton signed an agriculture bill that restored food stamps to certain legal immigrants (children, senior citizens, refugees, and disabled people) who were in the country prior to August 22, 1996 (the date of the passage of the welfare reform bill, HR 3734, The Personal Responsibility and Work Opportunity Reconciliation Act). The restoration of federally funded food stamps for this portion of the legal immigrant population was effective November 1, 1998.

In the intervening period of July through October 1998, there were no funds disbursed from the State Option Food Stamp Program.

In December 1998, the Controlling Board approved the transfer of $1.8 million in FY 1999 appropriation authority from the State Option Food Stamp Program (line item 400-414) to create new line item 400-510, State Refugee Services. These transferred funds were to be used to expand the basic services being provided to eligible refugees and immigrants under the existing federal Refugee Social Services program, including targeting intensive job training and English as a second language in an effort to move this population into the workforce. In line to gain this additional subsidy funding were six of the state's major urban counties: Cuyahoga, Franklin, Hamilton, Lucas, Montgomery, and Summit.

At month's end, approximately $2.1 million still sat in line item 400-414's available balance for FY 1999 and we were unaware of any concrete plans to tap it prior to the end of the fiscal year.

Other Human Services

Employment Services. Year-to-date, the Bureau of Employment Services was running a relatively small overage of 3.9 percent, or $749,505, fueled by line item 795-407, OBES Operations, last seen in the spending spurge noted in our prior November/December, 1998 issue. As this line item's available appropriation comprised over 75.0 percent of the bureau's total available GRF appropriation authority in FY 1999, its spending pattern has had an unsurprisingly great impact on the bureau's month-to-month disbursement variances. This line item's spending slowed substantially in December, signaling what we believe to be a self-correction that will reduce the bureau's overage and draw actual year-to-date disbursements much closer to the estimate.

Turning then to the smaller GRF pieces in the bureau's budget, there were some line items that have exhibited a pattern of sluggish disbursements that are consistent with their historical pattern or the fact that they typically spend the bulk of their appropriations in the second half of a fiscal year. It was still too early for us to discern whether these variances will mimic historical patterns and spending will accelerate, or underages will continue to accumulate, thus leaving unexpected (albeit, small) year end balances.

In December, the spending logjam was broken in one of these smaller GRF budgetary pieces as a result of a Controlling Board action that transferred, pursuant to a bureau request, the unencumbered FY 1999 balance from line item 795-416, Veterans' Programs, and into the Ohio Veterans' Home's GRF operating budget. The FY 1999 appropriation in the bureau's line item was $69,249, of which $32,130 was actually transferred over to the Veterans' Home. The purpose of the bureau's line item was to fund activities associated with the Ohio Veterans' Hall of Fame, which honors outstanding veterans for successful endeavors following military service. The Controlling Board transfer was initiated in order to comply with an executive order previously signed by the Governor that shifted responsibility for the Hall of Fame from the bureau to the Veterans' Home.

Health. Lying behind the Department of Health's year-to-date underage of $5.4 million were two subsidy line items: (1) 440-501, Local Health Districts; and (2) 440-505, Medically Handicapped Children. In the case of the former, $3.9 million was appropriated in FY 1999 to provide subsidies that aid the roughly 150 local health districts in the state. Roughly one-half of that FY 1999 appropriation was to be disbursed in December 1998, with the remaining one-half going out-the-door in June 1999. The December disbursement was not made as originally assumed, and, if history is any guide, the June 1999 distribution will most likely not happen until sometime next fall.

What's the hang-up? During December and January of each year, and again in June and July, the department receives reports from the local health districts that are used to determine the amount of subsidy funding that each will receive from the state. And, until every local health district has submitted its report, absolutely none of this subsidy funding is disbursed. A five-to-six month or so delay in releasing this subsidy funding would not be surprising, or uncommon.

While the local health district subsidy was victimized by timing, something other than that appeared to be behind the $1.2 million year-to-date underage in the Medically Handicapped Children line item, which pays for the diagnosis, treatment, and supportive services provided to handicapped children meeting certain medical and economic eligibility criteria. The department told us that they have witnessed a drop in this program's caseload and that two of the reasons behind that drop could be: (1) that more families are being directed to the Medicaid program if the department thinks they are eligible; and (2) that Medicaid's new Healthy Start/CHIP program has increased the size of its eligible population as well.

Mental Health. The Department of Mental Health (DMH) registered a December underage of $12.0 million that was largely attributable to three subsidy line items: (1) 334-408, Community Mental Health and Hospital Services; (2) 335-502, Community Mental Health Programs; and (3) 335-508, Services for Severely Mentally Disabled Persons. As a group, these three line items account for 86.0 percent of the department's GRF budget. Disbursements from these line items were approximately $7.0 million, $1.8 million, and $2.6 million under estimate in December, respectively.

The department disburses the majority of the subsidy funding lodged in these three line items to community mental health boards on a quarterly basis and allows each local board to choose which month in each quarter that they would like to receive each of these allocations.

For the second quarter of FY 1999, it was expected that local boards would request 46.6 percent of these funds in October, 25.7 percent in November, and 27.7 percent in December. The actual percentage of funding disbursed, however, amounted to only 25.8 percent in October, a whopping 56.3 percent in November, and 17.9 percent in December. In terms of dollars, combined disbursements for these three line items were $23.8 million under estimate in October, $30.8 million over estimate in November, and $11.4 million under estimate in December. Despite these big misses relative to the monthly disbursement estimates for these line items, actual disbursements hit only $10.3 million, or 0.6 percent, under the year-to-date estimates.

Mental Retardation. The Department of Mental Retardation and Developmental Disabilities closed December with a year-to-date underage of $10.9 million. Not to sound like a broken record, but as discussed in our previous issue of ***Budget Footnotes***, the culprit behind this underage was prior years' encumbrances in line item 322-413, Residential and Support Services, which totaled $17.9 million at the start of FY 1999. Year-to-date, the negative disbursement variance in this line item was $7.5 million.

The funding appropriated to line item 322-413 represents waiver match dollars that the department holds on behalf of the county boards of mental retardation and developmental disabilities. Once the department is sure that all charges by providers have been made, it will reconcile the line item and then return funds to the county funds. A provider has 365 days to make a claim for payment to the department, which is the main reason why the department has not been able to reconcile all bills. According to a staff person with the department, the lion's share of these encumbered funds should be disbursed in January 1999.

Justice & Corrections

Halfway through FY 1999, the Justice and Corrections program category was holding a negative year-to-date disbursement variance of $86.9 million. In excess of 80 percent of that variance, or $70.3 million, was attributable to timing-based underages in one state agency: the Department Rehabilitation and Correction. Other year-to-date underages were also notable in the Department of Youth Services ($8.4 million) and the Judicial Conference of Ohio ($7.7 million). The results of our exploration of these three underages are presented in the three relatively brief paragraphs that follow.

Judicial Conference. The slice of the state's judicial branch of government known as the Judicial Conference of Ohio ended the first half of FY 1999 with an eye-opening year-to-date underage of $7.7 million. Perhaps even more dramatic was the fact that the conference's year-to-date disbursements were 92.7 percent below the estimate. That said, in our November/December, 1998 issue, we first drew attention to this relatively sizeable underage and traced its source back to line item 018-502, Court Security Subsidy, a new $11.25 million biennial pot of GRF funding created for the purpose of assessing and improving the security level of court facilities throughout the state. This line item has been plagued by underspending virtually from its inception in FY 1998 and will warrant closer scrutiny to see how much of this funding the conference can push out the door with only six months left before the close of the biennium.

Rehabilitation & Correction. The Department of Rehabilitation and Correction (DRC) rounded the FY 1999 halfway mark with two large underages dominating their disbursement landscape: $36.4 million for the month of December and $70.3 million year-to-date. These underages clearly loomed large on first blush, but upon closer scrutiny were not particularly alarming. The source of these underages was essentially DRC's payroll, which includes in excess of 14,000 GRF-funded staff. When the estimates for DRC's FY 1999 GRF operating expenses were built, two critical assumptions had to be made: (1) how and when funding for employee compensation increases would hit DRC's budget; and (2) how many of DRC's 26 pay periods, each covering two working weeks, would be disbursed in each month from July 1998 through June 1999. Reality landed counter to these assumptions, thus throwing the month of September and then December well off the mark that the estimates for those months led us to expect. That said, these two whopping monthly underages were believed to be no more than matters of timing that should in all likelihood sort themselves out over the course of FY 1999's latter half.

Youth Services. For December, the monthly disbursement estimate for line item 470-401, Care and Custody — a $130-plus million funding stream that supports the Department of Youth Services' flagship program known as RECLAIM Ohio — was $14.8 million. The actual monthly disbursement was $10.5 million. The resulting negative monthly disbursement variance of $4.3 million was the primary culprit behind the department's overall underspending of $5.3 million posted for December. The department has largely attributed the December underspending to a roughly $3.6 million payroll distribution that was originally expected to occur in very late December that actually occurred in very early January, which means that we should see an overage in the Care and Custody line item next month as a result of this payroll shifting. This line item has also been a major player in the department's year-to-date disbursement variance picture as well by contributing approximately $6 million to a year-to-date underage that now totaled $8.4 million.

Transportation

ODOT. For the month of December, the Department of Transportation posted a positive disbursement variance of $5.1 million, traceable back to line item 775-451, Public Transportation — State, by far the dominant force in its GRF budget. The line item started FY 1999 with a total appropriation authority of $43.8 million, out of a departmental total of $67.2 million, for the purpose of providing capital and operating assistance to 50-plus transit systems around the state operating fleets that consist of busses, vans, light transit vehicles, automobiles, and rail cars. The December overage that occurred in this line item was not in the least bit surprising, as history has repeatedly demonstrated the difficulty in predicting with much certainty when, and how much, transit systems will draw from this pool of state financial assistance.

Development

Development. For the second quarter of FY 1999, disbursements for the Department of Development continued in their "business-as-usual" fashion. Most operating line items had disbursed approximately one-half of their appropriated amounts, while most subsidy line items retained the bulk of their appropriations (75 percent or more), reflecting the typical lag time or gap between the state' fiscal year and the realities of how the department's grant and loan programs operate.

December. That said, however, there were two disbursements most noticeable for their relative size in the month of December: (1) a $4.9 million release of funds for the Thomas Edison Program (line item 195-401); and (2) a $2.2 million release in funds for the Industrial Training Program (line item 195-434). In the case of the Thomas Edison funding, this release brought the total disbursed from the program up to $15.2 million of the current year's funding, or 66.0 percent of the FY 1999 appropriation; not particularly disturbing though as the picture this painted for the first six months of FY 1999 was consistent with the program's FY 1998 spending pattern. Striking a much different note, though, was the monthly release from the Industrial Training Program funds, which was extremely unusual. This particular release was traceable to the economic development incentive package for the Chrysler-Jeep project in Toledo (July 1997), which included a $6.0 million commitment in training funds over a period of three years, beginning in FY 1999.

Year-to-Date. The department's disbursement of FY 1999 appropriations totaled just over $16.4 million for the second quarter, bringing the six-month total to $48.7 million, or about one-half of Development's $100-plus million in current year's funding. Additionally, approximately $16.3 million in past years' encumbrances for certain Development programs were disbursed as well in the second quarter, which brought the year-to-date disbursement of prior years' encumbrances up to $26.3 million. For comparison's sake, at this time last year, a total of $15.6 million in prior years' encumbrances had been disbursed. This apparent acceleration in the disbursement of prior years' encumbrances can be expected to continue for another quarter or two as the department attempts to close the books on various economic development deals initiated by the prior administration.

Other Government

Administrative Services. The year-to-date negative disbursement variance registered by the Other

Government program category ($36.6 million) continued to be propelled by underspending in the Department of Administrative Services' budget ($23.8 million) that was a function of: (1) lower than expected payments for rent and operating costs on state-owned buildings, including the State of Ohio Computer Center; and (2) slower than expected disbursements on computing and communications services to other state agencies. Much of this underspending in fact occurred some time ago during the months of August and September, a fact we previously discussed in our October issue. Year-to-date, state building rent and operating costs has contributed $11.0 million to the department's underage, with $6.8 million alone coming from smaller than anticipated debt service payments to the Ohio Building Authority (line items 100-447 and 100-448). Four components of the department's computer and communications services program have tossed a $10.2 million underage into the mix as well: (1) Year 2000 Assistance (line item 100-430); (2) Multi-Agency Radio Communication System/MARCS (line item 100-417); (3) State of Ohio Multi-Agency Communications Systems/SOMACS (line item 100-419); and (4) Strategic Technology (line item 100-416).

Leading the underages in the computer and communications services program was the Year 2000 line item with $4.6 million, $4.4 million of which represented underspending in the FY 1999 appropriation and the remainder (around $200,000) represented unspent FY 1998 encumbrances. The reason behind this underage was the unexpectedly slow utilization of technical assistance contracts; however, the pace of disbursements has picked up over the last two to three months. Year-to-date, of the line item's $10.8 million FY 1999 appropriation, a total of $6.0 million, or 55.6 percent, has either been disbursed or encumbered. We sensed that the balance of the line item's available FY 1999 appropriation, $4.8 million, was being held back for emergency technical assistance that the department expects will arise as the year 2000 approaches and some state agencies discover that they still have unresolved Y2K compliance issues.

The second leading underage in the computer and communications services program was the MARCS line item with $2.4 million, $2.3 million of which represented underspending in the FY 1999 appropriation and the remainder (around $125,000) represented unspent FY 1998 encumbrances. Year-to-date, of the line item's $6.3 million FY 1999 appropriation, approximately $973,000, or 15.4 percent, has been either disbursed or encumbered. Also keep in mind that, in September the Controlling Board transferred $2.1 million of the unused FY 1998 MARCS appropriation into FY 1999. The building and roll-out of this state-of-the-art, statewide communications system has hit obstacles along the way, but was supposed to be picking up steam as we move through the second half of FY 1999.

A last item of note was the Strategic Technology line item, which posted a year-to-date underage of $1.7 million, of which roughly 20.0 percent was attributable to unspent FY 1998 encumbrances. Funding for this line item was provided to: (1) expand the Electronic Data Interchange (EDI) initiative, a program that will allow state agencies to conduct business electronically with vendors; (2) continue the Data Linkage project, a program that supports the on-line state benefit eligibility verification system used by the Bureau of Employment Services, the Department of Human Services; and the Bureau of Workers' Compensation; and (3) establish contracts with computer consulting firms to provide research and information on computing technologies for all state agencies. The EDI initiative was moved into a non-GRF account, a "smartcard" involving the Department of Human Services was not pursued, and the development of other state agency technology projects has been very slow.

Auditor. The Auditor of State rounded FY 1999's halfway mark carrying a year-to-date underage of $4.6 million, which we fully expect to grow, thus producing the intentional return or "lapsing" of $5-plus million in GRF funding to the state treasury. Like last fiscal year, the primary force behind the Auditor's negative disbursement variance was the $30-plus million line item 070-321, Operating Expenses, which covers personnel, maintenance, and equipment costs. This underage reflected a calculated strategy that the Auditor implemented three fiscal years ago wherein GRF operating expenses are kept on a tight leash, some of which is accomplished by charging costs, when possible, to two non-GRF line items (Funds 109 and 422) that collect payments made by state and local governments for the costs of audits performed by the Auditor.

Budget & Management. We last reported on the funds that the Office of Budget and Management

Table 9
Central State's Anticipated Fiscal Needs

Expense Item	Estimated Fiscal Need
Technology and library upgrades	$ 650,000
Payment to financial supervisor	$ 250,000
Outstanding bills (City of Xenia, Ameritech, Gourmet Food)	$ 1,350,000
Teacher's retirement system incentive lump sum payment	$ 800,000
Re-accreditation	$ 200,000
Collective bargaining unit salary adjustment	$ 2,900,000
Recruitment campaign	$ 250,000
Health and safety	$ 100,000
Academic computing and resource needs	$ 300,000
Total	$ 6,800,000

(OBM) has on-hand for aiding Central State University (CSU) in its extraction from a fiscal nightmare (line item 042-407, Central State Deficit Reduction) in our July/August issue. At that point in time, OBM was still carrying $4.9 million in encumbered FY 1997 CSU funds on the books slated for disbursement sometime during FY 1999. Halfway through FY 1999, although only about $400,000 in encumbered CSU funds had been disbursed, OBM was still expecting the entire $4.9 million to spent by fiscal year's end.

According to OBM, the underage is at least partly due to the fact that CSU had not been seeking expedient reimbursement for expenses that the university had already incurred. OBM estimates that more than $1 million in reimbursable expenditures have been made for which CSU has not yet turned in the paperwork necessary to trigger release of the state's deficit reduction assistance. In addition, an arbitration agreement with the faculty union has yet to finalized. Once this agreement is reached a significant portion of the line item, in the range of $2.0 million to $3.0 million, will be disbursed.

OBM recently revisited their expectations relative to the nature and amount of fiscal assistance that CSU may require, which we have captured in Table 9, Central State's Anticipated Fiscal Needs, which appears above. Clearly, OBM will not be able to fully reimburse CSU in the range of the estimated total need as it exceeds the remaining appropriation, which means that OBM's disbursements will have to be adjusted to reflect that reality.

The biggest expected expense item in question is how much OBM will reimburse CSU for its soon-to-be-finalized collective bargaining agreement with the faculty union. The total settlement is expected to cost CSU about $2.9 million: $2.4 million would be a one-time back payment to faculty and staff; and $500,000 would cover permanent salary adjustments that will elevate the university's reoccurring annual operating expenses.

OBM reimbursement for reoccurring expenses would not be possible except for Am. Sub. H.B. 850, the capital and corrective budget bill of the 122nd General Assembly. While Am. Sub. H.B. 215, the main appropriations act of the 122nd General Assembly, permitted only $1.0 million of the CSU Deficit Reduction line item be used for reoccurring operating expenses in FY 1998, Am. Sub. H.B. 850 lifted that limitation so that any of the funds not needed for non-recurring expenses may be used for reoccurring operating expenses.

Property Tax Relief

The property tax relief program will disburse approximately $1 billion back to school districts, counties, municipalities, townships, and other special taxing districts as compensation for credits or exemptions provided to taxpayers under existing state law. The timing of the state's distribution of this funding depends heavily on how quickly the settlement process goes at the local level and when county auditors apply to the state for property tax relief payments.

Table 10, Property Tax Relief Disbursement Percentages, which appears on the following page, focuses on the months of July through December and provides some selected disbursement details associated with the line items in the departments of Education and Taxation that fund the state's property tax relief payments. The table shows: (1) the percentage amount of appropriated FY 1999 personal and business property tax relief funding estimated to be disbursed monthly from July 1998 through December 1998; (2) the percentage amount of appropriated FY 1999 personal and business property tax relief funding actually disbursed monthly from July 1998 through December 1998; and (3) a comparison of the estimated disbursement percentages to the actual disbursement percentages for the total six month period, which appears in the last column of the table.

This year's unexpectedly rapid settlement process continued to exercise its profound effect on the state's property tax relief distribution activity in December.

Table 10
Property Tax Relief Disbursement Percentages
(July, 1998 - December, 1998)

Disbursements			July	August	September	October	November	December	Total
Education	Personal	FY 1999 Estimate	0.00%	5.50%	15.00%	17.50%	5.50%	5.00%	48.50%
		FY 1999 Actual	0.00%	3.21%	19.14%	12.78%	13.16%	0.00%	48.29%
	Business	FY 1999 Estimate	0.00%	0.00%	0.00%	0.00%	42.50%	53.00%	95.50%
		FY 1999 Actual	0.00%	0.00%	0.00%	0.00%	43.97%	55.19%	99.16%
Taxation	Personal	FY 1999 Estimate	0.25%	4.00%	19.25%	19.25%	5.00%	6.00%	48.50%
		FY 1999 Actual	0.25%	2.84%	11.80%	11.80%	11.12%	0.00%	47.80%
	Business	FY 1999 Estimate	0.00%	0.00%	18.00%	18.00%	30.00%	50.00%	98.00%
		FY 1999 Actual	0.00%	0.00%	21.72%	21.72%	52.81%	22.33%	96.86%

In prior months, we had witnessed a cycle of sizeable underages and overages in the state's property tax relief distribution activity, and December was no exception. It was most noticeable in the personal property component of the state's tax relief program, which posted a monthly underage of almost $50.0 million. A monthly underage in the business property component of the state's tax relief program was also posted, but of a much smaller magnitude — around $5.0 million. None of this was surprising and was solely attributable to one of our usual suspects: timing. ❑

LBO colleagues developing material that anchored this article include, in alphabetical order, Ogbe Aideyman, Laura Bickle, Sybil Haney, Sharon Hanrahan, Alexander C. Heckman, Steve Mansfield, Jeffery T. Petry, Chuck Phillips, Jeffrey M. Rosa, Corey Schaal, Katherine B. Schill, and Wendy Zhan.

Lottery Profits Quarterly Report

LOTTERY TICKET SALES AND PROFITS TRANSFERS SECOND QUARTER, FY 1999

— Allan Lundell

A record setting December boosted sales for the second quarter of FY 1999 to the highest level since the fourth quarter of FY 1996. Five Ohio Lottery records were set in December:

- ***Largest monthly transfer to education*** - $70.4 million
- ***Highest total monthly sales*** - $257.8 million
- ***Highest total weekly sales*** - $68.1 million for the week ending December 19, 1998
- ***Highest weekly sales of instant tickets*** - $32 million for the week ending December 26, 1998
- ***Highest daily sales of instant tickets*** - $6.5 million on December 24, 1998

Sales were helped to record levels by strong Super Lotto sales driven by a $45 million jackpot and strong holiday instant ticket sales. Advertising played an important role in achieving record sales levels. Instant ticket sales were promoted by game specific advertisements for the lottery's three key holiday instant games. Super Lotto sales were promoted by "jackpot alert" spots that were run as the jackpot grew.

Total sales for the second quarter of FY 1999 were $610.8 million, up 20.4 percent over first quarter sales and up 4.2 percent over sales for the second quarter of FY 1998. Year to date sales through the second

Table 1, FY 1999 Lottery Ticket Sales and Transfers to LPEF, millions of dollars

	Ticket Sales	Actual Transfers	Projected Transfers	Dollars Variance	Percentage Variance	Transfers as a Percentage of Sales
Jul 98	$165.81	$53.62	$57.37	$-3.75	-6.54%	32.34%
Aug 98	171.65	55.31	57.04	-1.72	-3.02%	32.22%
Sep 98	169.91	55.11	56.34	-1.23	-2.18%	32.43%
Q1 99	**507.38**	**164.04**	**170.75**	**-6.70**	**-3.92%**	**32.33%**
Oct 98	177.34	56.71	56.40	0.31	0.54%	31.98%
Nov 98	175.67	57.05	57.72	-0.67	-1.17%	32.47%
Dec 98	257.85	70.41	59.72	10.69	17.91%	27.31%
Q2 99	**610.86**	**184.16**	**173.83**	**10.33**	**5.94%**	**30.15%**
Year to Date	**$1,118.23**	**$348.21**	**$344.58**	**$3.63**	**1.05%**	**31.14%**

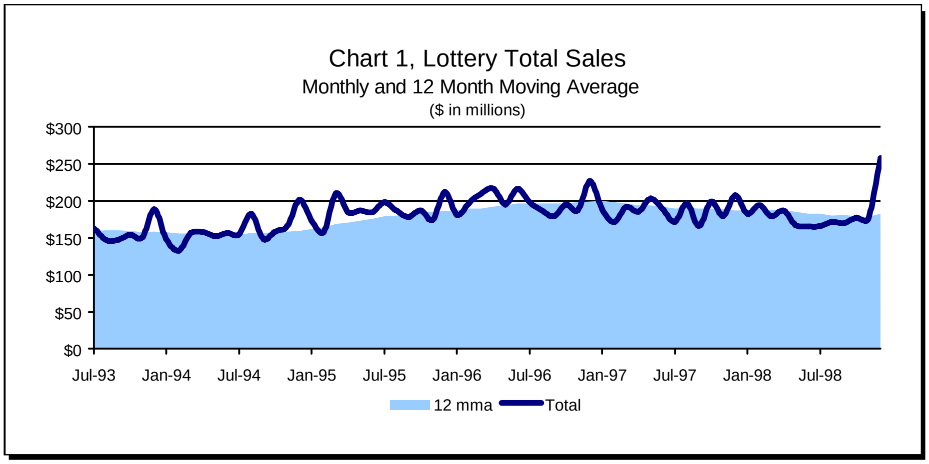
Table 2, FY 1999 Lottery Ticket Sales by Game, millions of dollars

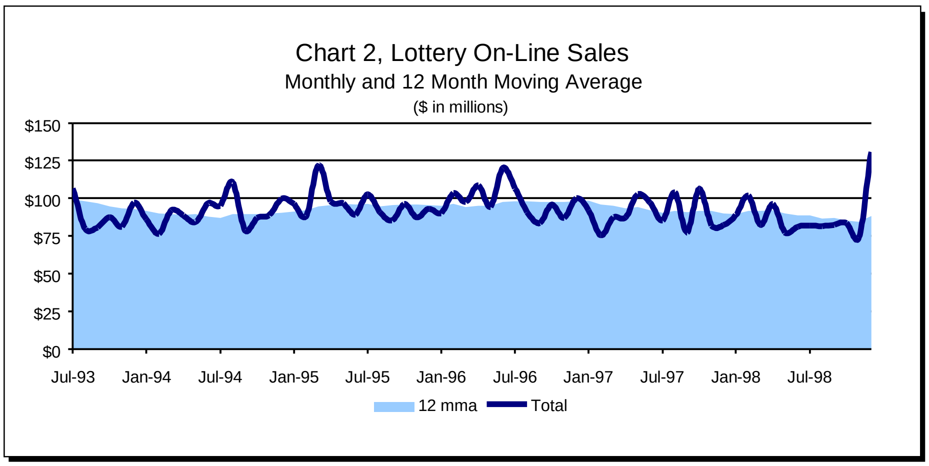
	Pick 3	Pick 4	Buckeye Five	Kicker	Super Lotto	On-Line Sales	Instant Tickets	Total Sales
Jul 98	$33.46	$10.40	$6.31	$4.51	$27.24	$81.92	$83.89	$165.81
Aug 98	32.10	10.01	6.05	4.68	28.67	81.50	90.15	171.65
Sep 98	31.74	10.04	5.88	4.79	30.01	82.45	87.46	169.91
Q1 99	**97.29**	**30.45**	**18.23**	**13.98**	**85.92**	**245.87**	**261.50**	**507.38**
Oct 98	32.76	10.63	6.16	4.73	29.28	83.55	93.78	177.34
Nov 98	31.09	9.90	5.76	3.85	22.94	73.55	102.11	175.67
Dec 98	34.57	10.85	5.79	8.95	70.40	130.55	127.30	257.85
Q2 99	**98.42**	**31.38**	**17.71**	**17.53**	**122.62**	**287.66**	**323.20**	**610.86**
Year to Date	**$195.71**	**$61.83**	**$35.94**	**$31.51**	**$208.54**	**$533.53**	**$584.70**	**$1,118.23**

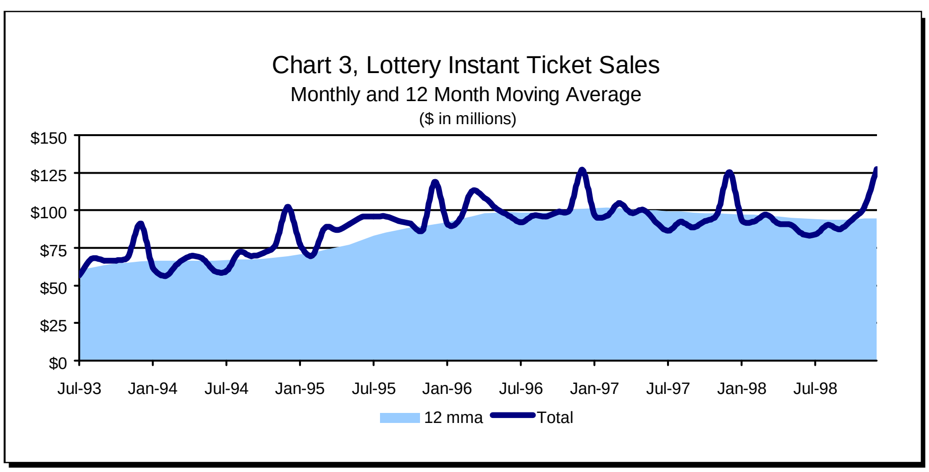
quarter of FY 1999 ($1,118.2 million) are slightly lower than year to date sales through the second quarter of FY 1998 ($1,119.7 million). Although lower than the previous fiscal year, FY 1999 year to date sales are slightly ahead of forecast. Sales are forecasted to be $2,101.4 million for FY 1999. In recent years, sales through the second quarter have averaged 51 percent of total fiscal year sales. Applying this percentage to the forecast for FY 1999 yields a forecast of sales through the second quarter of $1,071.7 million. Year to date sales are 4.3 percent above forecast.

FY 1999 sales and transfers are summarized in Table 1. The record transfers made in December brought transfers from behind to slightly ahead of projected levels. For the second quarter of FY 1999, transfers totaled $184.1 million. Year to date transfers are $2.5 million less than transfers made through the second quarter of FY 1998, but are $3.6 million above the amounts projected for this point in FY 1999.

Table 2 summarizes sales information for the first two quarters of FY 1999. Total sales were up 20.4 percent from first quarter FY 1999 levels. The only game experiencing a decline in sales was Buckeye 5, which fell 2.9 percent. Super Lotto sales increased by 42.7 percent, Kicker sales by 25.4 percent, Pick 4 sales by 3.1 percent, and Pick 3 sales by 1.2 percent. Combined on-line sales increased by 17.0 percent. Sales of Instant Tickets increased by 23.6 percent over first quarter levels. The quarterly sales total was significantly enhanced by the record sales recorded in December. A comparison of mid-year sales for FY 1999 and FY 1998 shows that while total sales are slightly lower than last year, the experiences of the individual games vary widely. Total sales after the first two quarters of FY 1999 are 0.13 percent less than total sales at the mid-point of FY 1998. Sales of Instant Tickets are 0.34 percent higher and on-line sales are 0.65 percent lower. Super Lotto sales are 6.56 percent higher and Kicker sales are 2.63 percent higher. Pick 4 sales are 0.38 percent higher. Pick 3 sales are 7.94 percent lower and Buckeye 5 sales are 1.29 percent lower. The record sales of December kept sales from being even further below FY 1998 levels.







The record sales of December 1998 were an exception to recent lottery sales. Total sales peaked at $2,314.7 million in FY 1996, declined to $2,299.9 million in FY 1997, and fell to $2,195.8 in FY 1998. Sales were forecasted to be $2,101.4 million in FY 1999. Sales are expected to continue to fall due to the maturing of the Ohio Lottery and increased competition for Ohio's gaming dollars (riverboats in Indiana and Kentucky; casinos in Michigan and Canada; enhanced racetracks in West Virginia; and Powerball).

Charts 1,2, and 3 provide pictures of lottery sales since FY 1994. The peaks in on-line sales correspond to large Super Lotto jackpots. Sales of Instant Tickets peak every December. The shaded areas representing 12 month moving average (12 mma) are indicators of the long-term trends. Total sales increased steadily since July 1993, reaching a high point in FY 1996, remaining fairly flat through FY 1997, and declining since FY 1997. On-line sales have tended to decline during the time period depicted. Occasional runs of large Super Lotto jackpots have acted to counter this decline, but the decline has continued. Sales of instant tickets increased rapidly starting in FY 1995. The increase continued until FY 1997. During FY 1997, sales of instant tickets started a decline that has continued through the first half of FY 1999. ❑

LOTTERY PROFITS EDUCATION FUND DISBURSEMENTS

DISBURSEMENTS OF FISCAL YEAR 1999 PROFITS

— *Wendy Zhan*

Lottery Profits Education Fund (LPEF) year-to-date disbursements in fiscal year 1999 totaled $289.3 million. The bulk of disbursements ($267.3 million or 92.3 percent) occurred in appropriation item Base Cost Funding (200-612). Table 1 shows the LPEF and Lottery Profits Education Reserved Fund (LPERF) appropriation and disbursement summary as of December 31, 1998.

Base Cost Funding. Approximately 40.1 percent of the base cost funding appropriation was disbursed in the first six months of fiscal year 1999. The $666.0 million lottery profits appropriation blends with the General Revenue Fund (GRF) base cost funding (line item 200-501) appropriation ($2,987.0 million) to, among other things, provide equalized subsidies to school districts to guarantee $3,851 in per pupil funding of combined state and local revenues at 23 mills. With the combination of GRF and LPEF moneys, base cost funding ($3,653 million), the biggest education subsidy item, represents about 61.1 percent of Department of Education's GRF and LPEF budget components.

Lease Rental. The lease rental appropriation ($32.8 million) is to be transferred to GRF to support the GRF appropriation for item 230-428, Lease Rental Payments, of the School Facilities Commission (SFC). Total GRF appropriation for the lease rental payments is $57.2 million in FY 1999. These moneys are used to pay bond service charges on obligations issued for the classroom facilities assistance program. While no actual transfer has yet been made, SFC has so far disbursed $20.3 million from item Lease Rental Payments to pay the debt service on $110 million bonds issued in FY 1999.

Other Programs Supported by LPEF and LPERF

Base cost funding and the lease rental payments have historically been the two major education programs partially supported by the lottery moneys. However, the 122nd General Assembly also used the lottery moneys to fund several other programs. The following is an update on four other programs supported by LPEF or LPERF moneys.

Textbook/Instructional Materials Subsidy. In FY 1999, $15 million in LPEF moneys was transferred to the Textbook/Instructional Materials Fund (5F8) to combine with $10 million from FY 1998 GRF ending balance to support the $25 million appropriation for the State Special Revenue Fund item Textbook/Instructional Materials (5F8, 200-645). These moneys were distributed to school districts with valuation per pupil less than $200,000 on a per pupil basis. The FY 1999 per pupil subsidy amount is about $16.30. School districts are required to use these moneys for textbooks, instructional software, and instructional materials.

Bus Purchase One-time Supplement. In FY 1998, the $10 million appropriation from excess cash in LPEF was made to provide a one-time school bus

Table 1: FY 1999 LPEF (017) and LPERF (018) Appropriation/Disbursement Summary
As of December 31, 1998

Agency	Fund	Line Item	Line Item Name	FY 1999 Appropriation	FY 1999 Disbursement	Appropriation Balance
EDU	017	200-612	Base Cost Funding	$ 666,093,028	$ 267,300,608	$ 398,792,420
EDU	017	200-682	Lease Rental	$ 32,780,000	$ 0	$ 32,780,000
EDU	017		Transfer to Textbooks/Instructional Materials Fund (5F8)	$ 15,000,000	$ 15,000,000	$ 0
EDU	017	200-694	Bus Purchase One Time Supplement	$ 9,208,579	$ 4,770,482	$ 4,438,097*
NET	017	228-690	SchoolNet Electrical Infrastructure	$ 27,000,000	$ 2,248,915	$ 24,751,085
			Total LPEF	**$ 750,081,607**	**$ 289,320,005**	**$ 460,761,602**
SFC	018	230-649	Disability Access Project	$ 4,925,420	$ 1,207,490	$ 3,717,930

purchase supplement. Of this amount, approximately $9.2 million was transferred into FY 1999. The year-to-date disbursement amounted to $4.4 million. The remaining $4.2 million was encumbered. The state provides on-going GRF bus purchase subsidies to school districts, educational service centers, and county MR/DD boards. Buses purchased and identified as "nonpublic or handicapped" are fully reimbursed by the state assuming they have met the mileage requirements, with the funding priority starting with buses having the highest mileage. The bulk of the bus purchase funding are distributed to school districts based on a complex formula that includes a per pupil or per mile base reimbursement, a rough road factor, and an equalization component.

SchoolNet Electrical Infrastructure – "Power-up For Technology." The need for electrical upgrades has been identified as the most pervasive obstacle for implementing SchoolNet and SchoolNet Plus initiatives. While school districts are allowed to use up to 10 percent of their SchoolNet Plus subsidies for electrical upgrade, the problem is more costly than this for many school districts. As another step toward resolving the problem, the 122nd General Assembly earmarked $30 million in LPEF moneys in FY 1998 for electrical service upgrades. Of this amount, $3 million was earmarked for the University of Akron to complete the Medina Achievement Center/Medina Educational Support Center Link-up project and the remaining $27 million was transferred into FY 1999. As of December 31, 1998, $2.2 million was disbursed.

The SchoolNet Office is to distribute the funding through three rounds of the competitive grant application processes. School districts with a valuation per pupil less than $200,000 are eligible for the funding. The maximum grant amount for a single district is $1 million. In the first round, 18 school districts were awarded amounts totaling $7.4 million in October, 1998. The office is currently reviewing applications for the second round of grants. The last round of grants will be awarded in summer 1999.

Disability Access Project. The 122nd General Assembly appropriated $5 million in LPERF moneys to be awarded in $100,000 grants for disability access projects to school districts. The responsibilities for reviewing and awarding these grants were transferred to SFC from the Department of Education on December 31, 1997. A school district that is not one of the state's 21 urban districts and that has a valuation per pupil of less than $200,000 is eligible for the funding. The district is also required to pay a percent of the project cost equal to the percentile in which the district is ranked. The 53 lowest equity districts' applications are currently being funded. The grant amount totaled $4.6 million for these 53 districts. ❑

Issues of Interest

THE TAXING ISSUE OF ELECTRIC RESTRUCTURING

DORIS MAHAFFEY

Storm Clouds on the Horizon

On November 6, 1998, the Board of Tax Appeals (BTA) issued a ruling in *Duquesne Light Co. v. Tracy*, a case involving the taxable value of Perry Nuclear Power Plant in Lake County, Ohio. Perry is jointly owned by 5 electric utilities – Cleveland Electric Illuminating (CEI), the managing operator, Ohio Edison, Toledo Edison, Pennsylvania Power Company and Duquesne Light Co. Together these five companies form the Central Area Power Coordinating Group (CAPCO), an entity that coordinates the operations of the generating facilities owned by the member utilities. Three of the CAPCO companies are Ohio utilities - providing electricity to Ohio consumers and regulated by the Ohio Public Utilities Commission (PUCO). The latter two are Pennsylvania companies and are not regulated by the PUCO.

The CAPCO companies began construction on Perry in 1974. Construction was scheduled to take 6 years. After numerous delays – many due to the increased level of regulatory scrutiny that took place after the Three Mile Island incident in 1979 – Unit 1 of Perry was completed in November 1987, and the Perry plant was first subject to property taxation in 1988. Plans for a second generating unit at Perry were abandoned.

Duquesne v. Tracy involves the valuation of Perry and of Duquesne's share of Perry for tax years 1992 and 1993. It also involves the value of certain pollution control equipment for tax years 1988 to 1991. If allowed to stand, the BTA's ruling could cost school districts and local governments in Ohio $24 million in refunds to Duquesne. (This takes into consideration that the ruling would also be applied to subsequent tax years.) It would set the stage for similar rulings on behalf of the other owners of Perry, resulting in additional revenue losses. It could significantly affect the apportionment of Perry. In addition, it could have a bearing on the valuation of other utilities in the state, so that the ultimate cost could be in the hundreds of millions, if not billions, of dollars.

A central issue in *Duquesne v. Tracy* is the definition of true value of electric generation equipment. Although the case is not a product of electric restructuring legislation – the case deals with tax years 1992 and 1993, whereas the PUCO Roundtable discussions on electric restructuring did not begin until the end of 1994 – it does highlight the tax problems associated with electric restructuring in Ohio. The case and others like it have the potential to greatly complicate the issues arising from electric restructuring legislation – and *vice versa*.

Electric Restructuring

Electric restructuring – also known as retail wheeling or electric "dereg" – generally refers to the introduction of competition in the retail electric power market, although it also refers to the actions that electric utilities are taking to prepare for this competitive market. The move toward retail competition began in 1992, when Congress enacted the Energy Policy Act (EPACT). EPACT called for competition in the wholesale market. The wholesale electricity market involves sales between utilities and other suppliers. The retail market involves sales of electricity to ultimate consumers – including industrial and commercial energy users, as well as residential customers. A major step toward the implementation of EPACT was taken in 1996 when the Federal Energy Regulatory Commission (FERC) issued orders 888 and 889 to facilitate wholesale electric competition. Since then 13 states (Arizona, California, Connecticut, Illinois, Maine, Massachusetts, Montana, Nevada, New Hampshire, Oklahoma, Pennsylvania, Rhode Island, and Virginia) have enacted legislation providing for retail competition in the electric industry. In an additional five states (Maryland, Michigan, New Jersey, New York, and Vermont), the state regulatory agency has issued a comprehensive order providing for retail competition. Competition has, in fact, begun in California and Pennsylvania.

Ohio is considering the issue.

The problem of electric restructuring in Ohio is complicated by tax and revenue issues. Ohio utilities are major taxpayers in the state. Electric utilities pay combined state and local taxes of $1 billion per year. Individual investor-owned utilities are the largest single taxpayer in 41 of 88 counties.

For tax purposes electric utilities include electric companies and rural electric co-operatives owning property or conducting business in the state. Table 1 lists electric companies subject to Ohio's public utility taxes.

Utilities are subject to different taxes than general business corporations in Ohio. Rather than pay the corporate franchise tax for the privilege of operating in Ohio, they pay a tax on gross receipts, known as the public utility excise tax. Because utilities pay this gross receipts tax, sales of electricity are not subject to the state sales and use tax. The income of public utilities is also exempt from the municipal income tax. The personal property of electric utilities is taxed in accordance with the public utility property tax, while that of general businesses is taxed in accordance with the tangible personal property tax.

This different tax treatment raises competitive and legal issues in the light of potential competition in electric power supply. It also raises revenue issues, since either continuing to tax utilities as they currently are being taxed or taxing them as other businesses in Ohio are taxed would probably cause revenue losses in a deregulated electric power market.

The dependence of Ohio schools and local governments on electric utility property taxes poses a major problem as Ohio struggles with electric restructuring. It is generally agreed that electric restructuring legislation in Ohio will include provisions that change the way that Ohio taxes electric companies. It is further agreed that such changes will be revenue neutral and that – for a time, at least – replacement revenues will be provided for those taxing districts that suffer a loss in their tax base due to the tax law changes. Even in the absence of any court cases, this could prove to be a challenge. There are over 2,000 separate taxing districts within the state. Due to the apportionment of public utility property, all are affected by the value of electric generating facilities. However, schools and other taxing districts vary greatly in their dependence on electric utility tax revenues. For example, in 1995 New Richmond Exempted Village School District (EVSD) in Clermont County received 73% of its total property tax revenues from electric utilities. At the same time, 340 school districts out of a total of 611 received less than 10 percent of their total property

Table 1 - Electric utilities subject to public utility taxes in Ohio (excluding rural electric co-operatives)

Utility	**Holding company**, *Headquarters*
American Municipal Power-Ohio, Inc. (AMP-Ohio)	*Columbus, Ohio*
Cincinnati Gas and Electric Co.	**CINergy,** *Cincinnati, Ohio*
Cleveland Electric Illuminating	**FirstEnergy,** *Akron, Ohio*
Columbus Southern Power	**AEP (American Electric Power),** *Columbus, Ohio*
Dayton Power and Light Co.	**DPL, Inc.,** *Dayton, Ohio*
Duquesne Light Co.	**DQE,** *Pittsburgh, PA*
Monongahela Power Co.	**Allegheny Power,** *Fairmont, WV*
Ohio Edison Co.	**FirstEnergy,** *Akron, Ohio*
Ohio Power Company	**AEP (American Electric Power),** *Columbus, Ohio*
Ohio Valley Electric Co.	**OVEC**
Pennsylvania Power Co.	**FirstEnergy,** *Akron, Ohio*
Toledo Edison Co.	**FirstEnergy,** *Akron, Ohio*

tax revenues from ***all*** public utility property. Table 2 shows the 15 school districts with the greatest dependence on electric utility property taxes.[1] These are all school districts which have electric generating facilities.

The problem is that legislation is not the only thing likely to affect the value of public utility property. Court cases and other actions that utilities take to reduce their costs and rationalize their operations in the face of looming competition will also affect property values. The selling and trading of assets, the shutting down of generation facilities, and the spinning off of subsidiaries all have the ability to greatly affect property values and likewise greatly complicate the tax issues.

Table 2 - School districts most dependent on personal property tax revenues from electric utilities (Based on 1995 data)

School district	*County*	*Electric utility revenue as % of total property tax revenue*
New Richmond EVSD	Clermont	73%
Gallia County LSD	Gallia	64%
Edison LSD	Jefferson	64%
Benton-Carroll-Salem LSD	Ottawa	57%
Ohio Valley LSD	Adams	56%
Wolf Creek LSD	Washington	54%
Fort Frye LSD	Washington	53%
Perry LSD	Lake	52%
River View LSD	Coshocton	45%
Shadyside LSD	Belmont	44%
Three Rivers LSD	Hamilton	37%
Southern LSD	Meigs	34%
Edgewood CSD	Butler	33%
Carlisle LSD	Warren	26%
Buckeye LSD	Jefferson	24%

Taxation of Electric Utilities in Ohio

Electric utilities pay two main taxes in Ohio: the public utility excise tax and the public utility property tax. Table 3 shows the revenues from these sources in 1997.[2]

Table 3 - Revenues from major taxes on electric utilities - 1997

	Public Utility Excise Tax	*Public Utility Property Tax (personal property only)*
Electric companies	$435,441,740	$544,630,062
Rural electric cooperatives	$17,183,490	$16,522,773
Total	$452,625,230	$561,152,835

The Public Utility Excise Tax

The public utility excise tax is largely a state tax, with 95.2 percent of revenues deposited in the state General Revenue Fund (GRF). The remainder is deposited in the local government funds (4.2% to the local government fund [LGF] and 0.6% to the local government revenue assistance fund [LGRAF]). The tax is based on the ***intrastate*** revenues of utilities. Competition is expected to increase the amount of electricity purchased from out-of-state. Such electricity would be exempt from the tax. This would cause state revenues to fall. In fact, electric utility excise tax revenues for tax year 1998 declined by 0.7 percent. (Currently public utility excise tax revenues from electric utilities comprise approximately 3 percent of all GRF revenues from state sources.) This is also a competitiveness issue, since electric companies located in Ohio would have to pay the tax on a large portion of their sales in Ohio, but companies located out-of-state could more easily avoid the tax.

Even without deregulation some tax erosion is occurring. Municipal utilities do not pay the tax directly. However, the tax is included in the cost of electricity purchased from any in-state utility (including AMP-Ohio). Moreover, many municipal utilities have long-term contracts with in-state utilities. But not all. They can escape the tax by purchasing power from out-of-state. As time passes more municipal utilities are likely to avail themselves of this opportunity, resulting in tax revenue losses.

The Public Utility Property Tax

Of greater concern, however, are the potential local tax revenue losses from the public utility property tax. Actually, utilities pay two property taxes – the tax on real property and the tax on personal property. Both are a source of revenues for local governments. In the case of public utilities, the personal property tax is the larger and more problematic of the two, but the real property tax has also been the focus of some tax reduction efforts.

Table 4 - Ohio Personal Property Tax Assessment Rates, 1998

Class of property	*Assessment rate*	*Cost of reducing rate to 25%**
Electric company property		
Generating equipment	100%	$189.8 million
Transmission and distribution property	88%	$218.6 million
All other taxable property	88%	$24.5 million
Rural electric company property		
All taxable property	50%	$8.1 million
Tangible property used in business		
All taxable property	25%	*Not applicable*

**Property tax loss estimates based on 1996 property values and millage rates*

Real vs. Personal Property

The ***real property*** of public utilities is treated like the real property of all other industries in the state. It is locally assessed by the county auditor at 35 percent of its true value. It also receives the 10 percent rollback. Nevertheless, several utilities have filed applications for reductions in the value of their real property with the boards of revision in several counties where their generating property is located. Any reductions in the value of such property will require the school districts and other local governments where the property is located to pay tax refunds – some of which could be substantial.

The ***personal property*** of public utilities is ***not*** treated like the personal property of other businesses. While it is subject to the same tax rates as other personal property in the same taxing district, it is assessed at higher rates. This difference has been discussed at length in the context of electric restructuring.[3] Table 4, compares the assessment rates on tangible personal property with different types of electric utility property. It also gives estimates of the annual property tax loss of reducing the assessment rate on electric utility property.

However, any change in the assessment rate would come about through legislation; and the restructuring legislation will provide a revenue source to make up for the local revenue lost as a result of the assessment rate reductions. Of course, current court cases and other restructuring activities may result in valuation changes that could complicate the issue of exactly how much revenue should be "replaced" in each taxing district.

There are many ***other*** differences in the treatment of electric utility property which could have tax consequences without any legislative change. These differences include assessment procedures, apportionment, and the definition of true value.

Different Assessment Procedures

Public utility property is centrally assessed by the Tax Department; whereas, the personal property of non-utilities is self-assessed. Consequently, a utility must first pay taxes on any value under dispute and then file a complaint with the Tax Department in order to get a refund. A successful complaint may result in taxing districts' making substantial refunds to public utilities. And since a complaint generally takes many years to resolve through litigation, any ensuing refunds could be for several years of excessive tax payments. A non-utility would simply not list the disputed value and would pay later (after being audited). This results in occasional windfalls to taxing districts.[4]

Apportionment

Public utility property is apportioned, whereas the property of non-utilities is taxed where it is located. In the case of most electric generation equipment, 70 percent of the value of the generating plant is allocated to the district where the plant is located. The remainder is apportioned, along with the rest of the company's tangible property, in accordance with the location of the company's transmission and distribution property. However, for generation facilities with a book value in excess of $1 billion dollars - that is, for Perry Nuclear Power Plant – the apportionment formula is somewhat different.

For Perry only the first $400 million of valuation is apportioned in accordance with the 70 percent rule. The rest is apportioned in accordance with the location in Ohio of the transmission and distribution systems of the five companies which are part owners of Perry. As a result, $300 million of the valuation of Perry that would under the general apportionment formula be apportioned to Perry Local School District (LSD) in Lake County is instead shared with 317 other school districts throughout the state. All 318 school districts which contain some of the transmission and distribution property belonging to the CAPCO companies would be affected by any change in the taxable value of Perry. In fact, reducing the assessment rate on generation to 25 percent would reduce Perry's taxable value to less than $400 million; so that any revenue that school districts (or other taxing districts) are now receiving due to the special apportionment formula would be lost. The districts would then lose 75 percent of the value that they would have received under the basic 70/30 apportionment scheme, as well.

Theory of Public Utility Taxation Under Regulation

Utilities have been taxed differently from other businesses for quite some time. Why all the concern now?

Under traditional public utility regulation, utilities do not really pay taxes. They collect taxes. The taxes that are assessed against utilities are passed on to their customers in the form of higher rates. Thus the taxes do not affect the utilities' overall profit levels or rates of return.

Since the utilities' customers are "captive" and cannot go elsewhere to purchase electricity, the customers pay the higher rates. If taxes are raised, the utilities get a rate increase to cover their increased taxes. The utility has no incentive to try to reduce or avoid taxes because they can easily pass them on to their customers. Other costs are treated similarly. And, in fact, if a cost item is part of the utility's "rate base," the utility may have some incentive to increase it rather than decrease it.

However, the real world even under regulation does create incentives for utilities to cut costs. Since rate cases are not continuous, there is a "lag" between cases during which utilities can benefit from cutting costs. Taking rates as "fixed" for a certain time period, utilities can increase their profits by reducing costs below those used in calculating their rates. This incentive is ordinarily not too great however, because at the next rate case, rates will be adjusted to reflect reduced costs.

Changing incentives for electric utilities under incipient competition

What if there isn't going to be another rate case? What if electric deregulation looms on the horizon? Electric utilities now have more of an incentive to try to reduce their costs. And in the case of FirstEnergy whose component companies are operating under a "rate freeze," the incentives to reduce costs are even greater.

Under the terms of the rate freeze, the FirstEnergy operating companies can keep any savings that they generate. Tax reductions would not be "refunded" to customers via rate reductions. So the utilities do have a powerful incentive to reduce costs - including taxes. That is, after all, one of the premises of the rate freeze. The problem, however, is that taxes are in some ways a relatively easy cost to attempt to reduce.

Moreover, the Tax Department generally treats subsidiaries as separate entities for tax purposes, including apportionment. Consequently, if a utility were to spin off a generation plant into a subsidiary, this would also affect the tax revenue not only of the taxing district where the generation facility is located. It would also affect the tax revenue of many taxing districts throughout the state. A non-utility spinning off part of its operations into a subsidiary would conceivably have no property tax consequences whatsoever.

Definition of True Value

Finally, the *Revised Code* contains some specific provisions regarding the definition of true value of electric utility property. For example, the true value of generating property is set equal to 50 percent of the book value. This definition has been the subject of much on-going litigation. It is one of the central issues in *Duquesne Light Co. v. Tracy*, discussed below.

Cost Cutting Activities of Electric Utilities Affecting Taxes

Outstanding Property Tax Valuation Cases

There are currently numerous public utility property valuation cases pending in the Ohio courts. These cases deal with the definition of true value, the value of different exemptions, the treatment of intangibles, the problem of "used-in-business" (*i.e.*, excess capacity), and the issues of equal protection and retroactivity, among other things. If the State were to lose all cases involving electric utility property taxes pending in Ohio Courts as of December 31, 1997, schools and local governments in the state would owe a total of $1,359.4 million in tax refunds plus an additional $259 million in associated interest expense. If it were to lose all public utility property cases, the cost could be in excess of $2.7 billion.[5] The Tax Department does not anticipate losing all the cases, but it is likely that it will lose some. Schools and local governments would be responsible for refunding whatever tax "overpayments" were made, based on the court rulings. Due to the apportionment rules, again, not just districts with generating plants but any taxing district with transmission or distribution property of an owner of a generating plant whose tax value was reduced as a result of such a case would be liable for some portion of the refund.

In the Matter of *Duquesne Light Co. v. Tracy*

Duquesne v. Tracy is the consolidation of three separate appeals before the BTA involving Perry Nuclear Power Plant.[6] The first (Case No. 95-K-40) involves an air pollution control facility exemption for tax years 1988 to 1991, and the main issue is retroactivity. The second and third (No.'s 95-K-71 and 95-K-72) dispute the Tax Commissioner's valuation of Perry for tax years 1992 and 1993. Duquesne claims that the Tax Department's definition of true value included certain costs that should be excluded – such as the value of certain architectural drawings, retired equipment, certain non-property expenditures and intangibles. The Tax Department argued that the exclusion of these items was already taken into consideration in the definition of true value.

According to the Tax Department, the definition of true value of electric generating property is clearly defined in section 5727.11 of the *Revised Code*. Specifically the true value is equal to "the equipment's or property's cost as capitalized on the company's books and records less fifty per cent of that cost as an allowance for depreciation and obsolescence." The cost is calculated with reference to certain accounts that public utilities are required by FERC to maintain.

The public utility property tax law also provides for two exemptions in calculating the true value of electric generating property:

1) an allowance for funds used during construction (AFUDC), and
2) the value of pollution-control facilities.

These costs are duly exempted. The value of AFUDC is based on PUCO proceedings; while the value of pollution-control facilities is established by a certificate issued by the Ohio Environmental Protection Agency. Hence, the process of determining the true value of electric generating equipment is relatively straight-forward.

The BTA disagreed with the Tax Department's interpretation. According to the BTA, section 5727.11 does not define the true value of electric generating property, it defines the method of valuation, as indicated by the section's caption.[7] The BTA's definition of true value hinges on the definition of what is taxable property. It finds that that definition in turn hinges on the definition of tangible property. Tangible property is not defined under the public utility tax law. However, based on the 1994 Supreme Court decision in *United Tel. Co. v. Limbach*, the BTA argues that what is considered tangible property in the tangible personal property tax is tangible property in the public utility property tax. It, therefore, looks to the definition of tangible property in section 5701.03 of the *Revised Code* and finds the exemption for drawings. The next question becomes what is the value of the exemption?

The Tax Department does not contest the point that architectural and engineering drawings are not taxable under the public utility property tax; only that, in this case, the point is irrelevant because *per Revised Code* section 5727.11, the true value of electric generation equipment is treated differently. The BTA disagrees, stating that "Nowhere within R.C. 5727.11 is there a suggestion that the valuation method set forth therein was intended by the General Assembly to supplant the above-cited statutes defining taxable property and according exemptions and exclusions to various types of property."[8] However, S.B. 449 of the 117 General Assembly, which originally enacted this provision (in then-section 5727.12), states in section 3 of uncodified law that this was a codification of existing practice:

> The amendments in this act to sections 5727.10 and 5727.12 of the Revised Code, defining the method of determining the true value of the production equipment of an electric company, are intended as a codification of the existing practices of the valuation of such production equipment, and not as a substantive change to the law....[9]

So, it is quite likely that at least the original intent of the section was as the Tax Department argued.

As for the value of the drawings, CEI - the managing partner of CAPCO - invested a great deal of time and money in obtaining estimates of the labor costs that must have gone into the creation and continual adjustments of the disputed drawings. It apparently did not keep specific records of the costs involved. The Tax Department argued that it needed specific records, such as invoices, not estimates in order to exempt the value of the property. This is consistent with its approach to AFUDC and pollution-control equipment, as noted above. Since the value of these exemptions are both determined in

Table 5 - *Duquesne v. Tracy*
Property Values Exempted by BTA

Tax year	*Type of exemption*	*Exempted value*
1988	Pollution control facilities	$45.6 million
1989	Pollution control facilities	$45.6 million
1990	Pollution control facilities	$45.6 million
1991	Pollution control facilities	$45.6 million
1992	Engineering drawings	$23.5 million
	Retired units	$5.0 million
	Non-property costs	*Exemption not granted*
	Intangibles	$21.1 million
	Total	**$49.6 million**
1993	Engineering drawings	$23.4 million
	Retired units	$5.7 million
	Non-property costs	*Exemption not granted*
	Intangibles	$21.0 million
	Total	**$50.1 million**

accordance with well-defined procedures, it seems that the granting of a questionable exemption for architectural drawings based on cost estimates is not precisely in keeping with the spirit of the law.

Needless to say, the BTA for the most part found in favor of Duquesne. Table 5 shows the values of the separate exemptions granted by the BTA. To determine the cost of these exemptions, one must determine how much of each of the now-exempted values was apportioned to which taxing districts in each tax year. After determining the apportioned value, one must determine the appropriate tax rate on public utility property for each taxing district in each tax year. The required refund for each district would equal the change in taxable value times the applicable tax rate. (Plus the accumulated interest.)

The Tax Department has appealed the ruling to the Ohio Supreme Court. However, if the ruling is allowed to stand, the immediate cost to schools and local governments (in terms of refunds) is estimated to be $24 million.[10] That is only the beginning. Duquesne represents only 13.74 percent of the ownership of Perry. The exemptions granted would most likely be extended to the other owners of Perry. FirstEnergy reportedly expects refunds in excess of $230 million on the basis of the *Duquesne* ruling.[11]

Moreover, the *Duquesne* ruling would set a precedent for valuation cases. What, then, is the meaning of section 5727.11 of the *Revised Code* as it applies to electric generation property? Is it just to deal with the issues of obsolescence, depreciation, and AFUDC? To define that whatever book value is established at, true value is 50 percent of that? Is that what the original lawmakers who enacted the provision had in mind? Perhaps, the point is to send a message to the current lawmakers working on electric restructuring legislation: *Be careful; be very careful*.

One aspect of the *Duquesne* case that the BTA did not rule on involves the issue of equal protection. Duquesne argued that since it was not regulated by the PUCO, it did not receive the AFUDC exemption received by the Ohio utilities. As a result, Duquesne's share of the tax burden for Perry greatly exceeded its ownership share. While the BTA heard evidence on this matter, it could not rule on it because it is a constitutional issue. That is left up to the Ohio Supreme Court. A ruling in favor of Duquesne on this issue would further increase the cost of the property tax refunds.

Issues for Electric Restructuring

The *Duquesne* case (as well as those that follow in its wake) raises two important issues in the context of electric restructuring. First is the matter of the refunds. Second is the problem of property tax replacement revenues - both how much and who gets them.

The Matter of Refunds

The *Revised Code* provides some financial assistance to certain school districts who must make substantial property tax refunds. It makes no such provisions for other local governments. In accordance with section 3317.026 of the *Revised Code*, the state will pay a qualifying school district the foundation aid that the district originally lost because its property was overvalued. However; this assistance only helps those school districts that are on the foundation formula (currently, most districts are); and it only helps them for the first 23 mills of the value subject to refund.[12]

The *Revised Code* also allows both schools and local governments 5 years to make any required refund. Public utilities generally make two property tax payments per year. Instead of paying the refunded amount all at once, the local governments may make the payment by deducting one-tenth of the refund from any taxes due from the utility for a period of 5 years (comprising 10 local property tax payments). But what happens if the utility is no longer a taxpayer in that local government's jurisdiction?

This is a probable scenario for certain local governments with respect to any future tax refunds made to Duquesne Light Co. According to a FirstEnergy press release dated October 15, 1998, FirstEnergy and Duquesne have agreed to an asset transfer.[13] Accordingly, Duquesne would transfer 1,436 megawatts (MW) of generating capacity at 8 generating units to FirstEnergy in exchange for 1,298 MW at three generating plants owned by FirstEnergy. The point of the exchange is to rationalize ownership and control of the operating units which are currently jointly owned and operated by CAPCO.

Under the agreement FirstEnergy will acquire Duquesne's interest in the W.H. Sammis plant in Stratton, Ohio (Jefferson County), the Eastlake plant in Eastlake, Ohio, (Lake County), and the Perry nuclear power plant in Perry, Ohio (Lake County), along with five plants in Pennsylvania. In exchange, Duquesne would acquire FirstEnergy's ownership share of the Avon Lake plant in Avon, Ohio (Lorain County), the Niles plant in Niles, Ohio (Trumbull County), and one plant in Pennsylvania.

Furthermore, Duquesne has announced plans to auction off its generating assets, including those in Ohio, so it is possible that any school district or local government required to refund tax dollars to Duquesne Light Co. would have to make the refund outright.

Value of Replacement Revenues

As noted above, if the legislature passes a bill reducing the assessment rate on electric utility property, the bill will provide replacement funds to local governments that lost property values. The question is, what value? The value of the property before the *Duquesne* decision or after it? School and local government advocates would argue in favor of the before-*Duquesne* values. Such a fix would partially mitigate the problems raised by *Duquesne*. Property values have fallen, and local governments must make refunds; but in the long run, they receive a stream of funds based on the higher pre-*Duquesne* value.

Under this scenario, the utilities will benefit because they get the refunds. The school districts and local governments will benefit because they get the higher stream of replacement revenues. Ohio's utility consumers - as ratepayers and as taxpayers - are the losers. As ratepayers they lose because they paid rates which included taxes which were ultimately returned to the utility; but their rates did not adjust to reflect these reduced taxes. As taxpayers they may end up paying twice for the same services – once through the utility (via the taxes embedded in the utility rates) and the second time to cover the refund to the utility. Moreover, in order to provide the same level of services in the future, the local government may have to seek additional taxes. And utility consumers as taxpayers may pay higher replacement taxes to fund the payments to schools and local governments.

Other Electric Utility Restructuring Activities With Tax Consequences

Formation of a Transmission Subsidiary

In addition to the asset transfer with Duquesne, FirstEnergy has announced other structural changes to enhance its operations. On October 8, 1998, it announced that it was forming a transmission subsidiary.[14] The formation of a separate transmission subsidiary will not affect the taxable value of FirstEnergy's plant and equipment, but it will greatly affect apportionment, creating some winners and some losers among taxing districts. Essentially, the 30 percent of generating plant that is apportioned in accordance with transmission and distribution will for the most part be apportioned in accordance with distribution facilities only. Taxing units hosting the distribution network of the utility would gain, while those hosting generation would most likely lose somewhat. Those taxing districts that contained only FirstEnergy transmission lines would lose all FirstEnergy non-transmission value that is currently apportioned to them.

Since AEP is contemplating joining FirstEnergy in the formation of a Transco, it may eventually spin off its transmission, as well. This would have a similar impact on apportionment in those areas currently receiving property tax revenue from either Ohio Power or Columbus Southern Power.

Formation of a Nuclear Operating Company

On October 14, FirstEnergy announced that it was forming a nuclear operating company.[15] The subsidiary would operate the Davis-Besse and Perry nuclear power plants. Unlike the transmission subsidiary, apparently FirstEnergy does not plan – at this time – to transfer its nuclear generating assets to the subsidiary. Hence, there should be no tax consequences – at this time. If, however, FirstEnergy were to transfer its nuclear power plant to such a subsidiary, the move would have major tax consequences. Again, the taxable value of the two plants would not change. However, it would be allocated totally to the taxing districts where the plants were located. *I.e.*, Lake County and Perry LSD would receive 100% of the value of Perry and Ottawa County and Benton-Carroll-Salem LSD would receive 100% of the value of Davis-Besse.

Interaction Between Legislative and Nonlegislative Structural Change

Finally, potential interaction between legislative and non-legislative structural changes should be addressed. For example, if the structural separation that is likely to be required by restructuring legislation results in the formation of subsidiaries – that own as well as operate electric power equipment – whether the subsidiaries are for generation, transmission, or distribution, current apportionment provisions could be rendered meaningless. Schools and other taxing districts with power plants would be the gainers in such a scenario.

This may turn out to be all to the good, as those districts are the ones likely to be the greatest "losers" as far as their property tax base goes with respect to assessment rate reductions.[16] It does, however, raise the flag again regarding any revenue-replacement proposal. How do you determine how much revenue needs to be replaced in any district? Under some proposals it is quite likely that two different taxing districts could legitimately claim the same lost electric utility property values. ❑

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1 Based on data available from the Ohio Department of Taxation and data gathered by Professor Howard Fleeter. For the latter, see Fleeter, "Analysis of the Impact of Reducing the Assessment Rate of Electric Utility Tangible Personal Property on Education Funding," a report submitted to the Ohio School Boards Association, August 15, 1996. See also Rich Levin and Bill Driscoll, "Electric Utility Deregulation and its Potential Tax Impact on Ohio School Districts with Electric Generating Plants," a report prepared for the Ohio School Boards Association, August 9, 1996.

2 Figures are based on data obtained from the Ohio Department of Taxation. See in particular, Ohio Department of Taxation, *Annual Report*, 1998.

3 See, for example, the Joint Committee on Electric Utility Deregulation, "Final Report," February 18, 1998, co-chairs Rep. Priscilla Mead and Sen. Bruce Johnson. See also the testimony to the Joint Committee, summarized in "Topic VI: Tax Issues."

Also see Education Tax Policy Institute, "School District and Local Government Property Tax Losses and Electric Utility Deregulation," Westerville, Ohio, 1998, as well as Fleeter, *op. cit.*, and Levin and Driscoll, *op. cit*.

4 The *Texas Eastern* case is a recent example where local governments in 20 counties, including 69 school districts, made substantial property tax refunds to a public utility. The case is discussed in Doris Mahaffey, "Refundin', Recalculatin', and 'Rithmetic: The New Three R's?" *Budget Footnotes*, Volume *21*, Number 2, October, 1997, pp. 36-39. The article also discusses the consequences of the different assessment procedures for public utility versus tangible personal property.

5 Based on a presentation made on June 23, 1998, by Fred Nicely, director of the public utility division of the Ohio Tax Department.

6 *Duquesne Light Company v. Tracy*, 1998, Ohio Board of Tax Appeals (Case Nos. 95-K-40, 95-K-71, 95-K-72) November 6, 1998. http: //www.state.oh.us/bta/981106dk.htm. Appeal filed November 9, 1998, Ohio Supreme Court 98-2365.

7 *Ibid.*, p.18. Section captions are, however, not part of the legislation when it is passed, so it is difficult to see where that has the force of law.

8 *Ibid*., p. 22

9 State of Ohio, *Laws of Ohio Including Appropriation Acts*, 142, Part I for 1987-1988, p.1635

10 "Duquesne wins Perry Nuclear tax valuation case; could cost schools, local governments million," *Ohio Report No. 215*, Volume *67*, Gongwer News Service, November 9, 1998. http://www.gongwer-oh.com/reports/1998/11/110998i.html (12/22/98). The estimated loss assumes that the exemptions for 1992 and 1993 will be extended for the 1994 through 1998 tax years.

11 "Groups see different impacts of Perry nuclear plant tax decision on deregulation," *Ohio Report No. 217*, Volume *67*, Gongwer News Service, November 12, 1998. http://www.gongwer-oh.com/reports/11/111298b.html

12 The average school district tax rate on tangible property in 1988 was about 40 mills; the average tax rate in 1997 was about 48 mills. So, the foundation replacement is only 48% to 52% of the revenue loss. For a discussion of section 3317.026, see Mahaffey, *op cit*.

13 "FirstEnergy Reaches Asset Transfer Agreement with Duquesne Light," FirstEnergy, October 15, 1998. http://access.ohioedison.com/fe/latestdevelopments.nsf/archivesweb?OpenView

14 "FirstEnergy Corp. Creates Transmission Subsidiary," FirstEnergy, October 8, 1998. http://access.ohioedison.com/fe/latestdevelopments.nsf/archivesweb?OpenView

15 "FirstEnergy Creates Nuclear Operating Company," FirstEnergy, October 14, 1998. http://access.ohioedison.com/fe/latestdevelopments.nsf/archivesweb?OpenView

16 On the other hand, should any generation facility shut down altogether, the taxing district would bear the full brunt of the tax revenue loss.

DPIA ALL-DAY AND EVERYDAY KINDERGARTEN FUNDING UPDATE

WENDY ZHAN

The 122nd General Assembly completely revised the disadvantaged pupil impact aid (DPIA) program. The program now includes funding for all-day and everyday kindergarten, K-3 class size reduction, and safety and remediation programs. As a result of the program expansion, FY 1999 DPIA formula funding has increased by approximately 37.9 percent over the FY 1998 funding level, from $267 million to $368.4 million. These changes were contained in House Bills 650 and 770 adopted in 1998.

To minimize the fluctuation in DPIA funding as a result of declining Ohio Works First (OWF) caseloads, beginning in FY 1999, funding is distributed based on each district's DPIA index. A district's DPIA index, which measures the district's relative concentration of poverty, is determined by comparing the district's ADC/OWF percentage to the statewide average ADC/OWF percentage. When a district's ADC/OWF student counts and the statewide ADC/OWF student counts decrease at the same time, the district's DPIA index could remain unchanged or could change but by a smaller magnitude. Therefore, the funding stability increases as a result of tying a district's funding level to the index.

Under the current DPIA program, if a district's DPIA index is one or greater, or its three-year average formula ADM exceeds 17,500, the district is eligible for all-day and everyday kindergarten funding. In other words, a school district with at least the statewide average ADC/OWF percentage is eligible for all-day and everyday kindergarten funding. Based on the most recent available data, the statewide average ADC/OWF percentage is 14.66 percent and 104 school districts are eligible for all-day and everyday kindergarten funding in FY 1999.

The FY 1999 DPIA appropriation contains approximately $96.6 million in all-day and everyday kindergarten funding for 104 eligible school districts. The appropriation was made by assuming that all 104 school districts would provide all-day and everyday kindergarten for all their kindergarten students. However, the actual funding amount is based on each district's percentage of kindergarten students actually receiving this service. The formula to determine a district's actual funding amount in FY 1999 is as follows:

FY 1999 Kindergarten ADM x Actual All-day & Everyday Kindergarten % x 50% x $3,851

(The other 50% of kindergarten ADM are included in formula ADM to qualify for base cost funding.)

An eligible school district is required to certify its all-day and everyday kindergarten percentage to the Department of Education by August 1. Based on the data reported by these 104 school districts, 72 (or 69.3 percent) districts are currently providing all-day and everyday kindergarten at the 100 percent level and 18 (or 17.3 percent) districts provide all-day and everyday kindergarten at levels ranging from four percent to 95.6 percent. The remaining 14 (13.4 percent) districts do not provide all-day and everyday kindergarten in FY 1999 (see Table 2).

The appropriation for the all-day and everyday kindergarten program assumed the 100 percent level of all-day and everyday kindergarten for every one of the 104 eligible districts. However, the district would only receive the amount of funding based on its actual all-day and everyday kindergarten percentage. Therefore, based on the current actual all-day and everyday kindergarten percentage data, it appears that the appropriation might exceed the needed funding for the program by approximately $17 million in FY 1999. Meanwhile, the department has recently

Table 1: DPIA All-day and Everyday Kindergarten Funding for Major Urban School Districts							
Name of School District	**County**	**DPIA Index FY99**	**Projected Kindergarten ADM FY99**	**Funding @ 100% of All-day Kindergarten FY99**	**Actual All-day Kindergarten % FY99**	**Funding @ Actual All-day Kindergarten % FY99**	**Funding Difference (100% vs. actual %)**
Cleveland City SD	Cuyahoga	4.17	7,061	$ 13,595,725	100.0	$ 13,595,725	$ -
Columbus City SD	Franklin	2.42	6,045	$ 11,639,763	100.0	$ 11,639,763	$ -
Cincinnati City SD	Hamilton	2.84	4,355	$ 8,385,057	100.0	$ 8,385,057	$ -
Toledo City SD	Lucas	2.70	3,363	$ 6,475,615	69.3	$ 4,487,601	$ 1,988,014
Akron City SD	Summit	2.29	2,838	$ 5,465,479	100.0	$ 5,465,479	$ -
Dayton City SD	Montgomery	2.98	2,231	$ 4,296,628	77.0	$ 3,308,404	$ 988,224
South-Western City SD	Franklin	0.73	1,517	$ 2,921,402	-	$ -	$ 2,921,402
Youngstown City SD	Mahoning	3.90	1,078	$ 2,076,141	100.0	$ 2,076,141	$ -
Canton City SD	Stark	2.12	1,063	$ 2,045,879	60.0	$ 1,227,527	$ 818,352
Total			***29,552***	***$ 56,901,691***		***$ 50,185,699***	***$ 6,715,992***

sent out surveys to see why some eligible districts opt for providing less than 100 percent, or zero percent of all-day and everyday kindergarten. The survey information should be available in the near future.

Table 1 shows funding information on the all-day and everyday kindergarten service provided by major urban (Big Eight plus South-Western City) school districts in FY 1999. The appropriation ($56.9 million) for these nine districts represents about 75.6 percent of the total appropriation ($96.6 million) for the all-day and everyday kindergarten program. It can be seen from the table that South-Western City is the only major urban district that is not providing any all-day and everyday kindergarten service in FY 1999. The actual all-day and everyday kindergarten percentages for Toledo City, Dayton City, and Canton City are 69.3 percent, 77 percent, and 60 percent, respectively. Cleveland City, Columbus City, Cincinnati City, Akron City, and Youngstown City provide all-day and everyday kindergarten service to all of their students. The actual funding ($50.2 million) for these nine urban districts represents about 63.3 percent of total funding ($79.2 million) for the all-day and everyday kindergarten program in the state.

Table 2 details each of 104 districts' DPIA Index, projected kindergarten ADM, funding at the 100 percent level of all-day and everyday kindergarten, actual all-day and everyday kindergarten percentage, funding at the actual all-day and everyday kindergarten percentage, and the funding difference between the 100 percent and the actual all-day and everyday kindergarten percentage in FY 1999. ❑

Table 2: DPIA All-day and Everyday Kindergarten Funding for 104 Eligible School Districts, FY 1999								
OBS	**Name of School District**	**County**	**DPIA Index FY99**	**Projected Kindergarten ADM FY99**	**Funding @ 100% of All-day Kindergarten FY99**	**Actual All-day Kindergarten % FY99**	**Funding @ Actual All-day Kindergarten % FY99**	**FY99 Funding Difference (100% vs. actual %)**
1	Ohio Valley Local SD	Adams	1.39	426	$ 819,506	100.0	$ 819,506	$ -
2	Lima City SD	Allen	2.05	544	$ 1,047,564	100.0	$ 1,047,564	$ -
3	Perry Local SD	Allen	1.03	65	$ 124,989	75.0	$ 93,742	$ 31,247
4	Ashtabula Area City SD	Ashtabula	1.66	407	$ 783,561	23.0	$ 180,219	$ 603,342
5	Alexander Local SD	Athens	1.06	108	$ 208,882	100.0	$ 208,882	$ -
6	Athens City SD	Athens	1.02	211	$ 406,528	-	$ -	$ 406,528
7	Federal Hocking Local SD	Athens	1.49	105	$ 201,618	100.0	$ 201,618	$ -
8	Nelsonville-York City SD	Athens	1.89	103	$ 198,780	100.0	$ 198,780	$ -
9	Trimble Local SD	Athens	2.13	81	$ 156,443	-	$ -	$ 156,443
10	Bellaire City SD	Belmont	1.88	131	$ 252,161	100.0	$ 252,161	$ -
11	Bridgeport Ex Vill SD	Belmont	1.70	62	$ 118,811	100.0	$ 118,811	$ -
12	Martins Ferry City SD	Belmont	1.79	95	$ 182,039	100.0	$ 182,039	$ -
13	Union Local SD	Belmont	1.08	122	$ 234,686	100.0	$ 234,686	$ -
14	Hamilton City SD	Butler	1.29	828	$ 1,594,763	100.0	$ 1,594,763	$ -
15	Middletown City SD	Butler	1.06	793	$ 1,526,129	-	$ -	$ 1,526,129
16	New Miami Local SD	Butler	1.48	62	$ 119,478	22.1	$ 26,381	$ 93,097
17	Springfield City SD	Clark	1.84	826	$ 1,590,039	60.0	$ 954,024	$ 636,016
18	Felicity-Franklin Local SD	Clermont	1.27	95	$ 182,588	100.0	$ 182,588	$ -
19	East Liverpool City SD	Columbiana	1.79	261	$ 503,238	100.0	$ 503,238	$ -
20	Wellsville City SD	Columbiana	1.46	85	$ 164,287	100.0	$ 164,287	$ -
21	Coshocton City SD	Coshocton	1.06	140	$ 268,818	100.0	$ 268,818	$ -
22	Cleveland City SD	Cuyahoga	4.17	7,061	$ 13,595,725	100.0	$ 13,595,725	$ -
23	Cleveland Hts-Univ Hts City SD	Cuyahoga	1.06	441	$ 849,738	100.0	$ 849,738	$ -
24	East Cleveland City SD	Cuyahoga	3.59	534	$ 1,027,883	62.0	$ 637,288	$ 390,596
25	Euclid City SD	Cuyahoga	1.02	465	$ 894,766	-	$ -	$ 894,766
26	Warrensville Heights City SD	Cuyahoga	1.72	202	$ 388,932	100.0	$ 388,932	$ -
27	Sandusky City SD	Erie	1.51	319	$ 614,277	100.0	$ 614,277	$ -
28	Columbus City SD	Franklin	2.42	6,045	$ 11,639,763	100.0	$ 11,639,763	$ -
29	South-Western City SD	Franklin	0.73	1,517	$ 2,921,402	-	$ -	$ 2,921,402
30	Gallia County Local SD	Gallia	1.67	183	$ 353,206	100.0	$ 353,206	$ -
31	Gallipolis City SD	Gallia	1.65	159	$ 305,353	100.0	$ 305,353	$ -
32	Cambridge City SD	Guernsey	1.28	258	$ 497,440	-	$ -	$ 497,440
33	Cincinnati City SD	Hamilton	2.84	4,355	$ 8,385,057	100.0	$ 8,385,057	$ -
34	Lockland City SD	Hamilton	1.91	58	$ 112,476	-	$ -	$ 112,476
35	Mount Healthy City SD	Hamilton	1.34	291	$ 560,697	-	$ -	$ 560,697
36	Norwood City SD	Hamilton	1.35	270	$ 520,293	100.0	$ 520,293	$ -
37	St Bernard-Elmwood Place City	Hamilton	1.18	95	$ 183,720	-	$ -	$ 183,720
38	Harrison Hills City SD	Harrison	1.11	165	$ 317,345	100.0	$ 317,345	$ -
39	Oak Hill Union Local SD	Jackson	1.27	105	$ 201,241	85.0	$ 171,055	$ 30,186
40	Wellston City SD	Jackson	1.37	153	$ 294,403	100.0	$ 294,403	$ -
41	Buckeye Local SD	Jefferson	1.32	190	$ 365,404	100.0	$ 365,404	$ -
42	Edison Local SD	Jefferson	1.00	218	$ 420,639	100.0	$ 420,639	$ -
43	Indian Creek Local SD	Jefferson	1.04	173	$ 333,803	100.0	$ 333,803	$ -
44	Steubenville City SD	Jefferson	2.82	176	$ 339,478	100.0	$ 339,478	$ -
45	Toronto City SD	Jefferson	1.28	80	$ 153,716	100.0	$ 153,716	$ -
46	Painesville City SD	Lake	1.43	243	$ 467,595	-	$ -	$ 467,595
47	Chesapeake Union Ex Vill SD	Lawrence	1.71	104	$ 199,831	100.0	$ 199,831	$ -
48	Dawson-Bryant Local SD	Lawrence	1.55	107	$ 205,744	100.0	$ 205,744	$ -
49	Fairland Local SD	Lawrence	1.11	126	$ 242,073	100.0	$ 242,073	$ -
50	Ironton City SD	Lawrence	2.11	136	$ 261,161	100.0	$ 261,161	$ -
51	Rock Hill Local SD	Lawrence	2.11	144	$ 277,331	100.0	$ 277,331	$ -
52	South Point Local SD	Lawrence	1.82	170	$ 326,995	100.0	$ 326,995	$ -
53	Symmes Valley Local SD	Lawrence	1.76	67	$ 128,125	100.0	$ 128,125	$ -
54	Clearview Local SD	Lorain	1.37	102	$ 195,678	100.0	$ 195,678	$ -

Table 2: DPIA All-day and Everyday Kindergarten Funding for 104 Eligible School Districts, FY 1999								
OBS	Name of School District	County	DPIA Index FY99	Projected Kindergarten ADM FY99	Funding @ 100% of All-day Kindergarten FY99	Actual All-day Kindergarten % FY99	Funding @ Actual All-day Kindergarten % FY99	FY99 Funding Difference (100% vs. actual %)
55	Elyria City SD	Lorain	1.23	716	$ 1,377,906	33.3	$ 459,256	$ 918,650
56	Lorain City SD	Lorain	2.13	920	$ 1,770,759	76.0	$ 1,345,777	$ 424,982
57	Toledo City SD	Lucas	2.70	3,363	$ 6,475,615	69.3	$ 4,487,601	$ 1,988,014
58	Campbell City SD	Mahoning	2.28	97	$ 186,949	100.0	$ 186,949	$ -
59	Struthers City SD	Mahoning	1.41	154	$ 296,483	-	$ -	$ 296,483
60	Youngstown City SD	Mahoning	3.90	1,078	$ 2,076,141	100.0	$ 2,076,141	$ -
61	Marion City SD	Marion	1.14	521	$ 1,002,953	4.0	$ 40,118	$ 962,835
62	Eastern Local SD	Meigs	1.31	68	$ 130,517	100.0	$ 130,517	$ -
63	Meigs Local SD	Meigs	1.91	175	$ 337,650	100.0	$ 337,650	$ -
64	Southern Local SD	Meigs	1.79	57	$ 109,436	100.0	$ 109,436	$ -
65	Switzerland Of Ohio Local SD	Monroe	1.16	195	$ 376,287	100.0	$ 376,287	$ -
66	Dayton City SD	Montgomery	2.98	2,231	$ 4,296,628	77.0	$ 3,308,404	$ 988,224
67	Jefferson Township Local SD	Montgomery	1.82	40	$ 76,285	100.0	$ 76,285	$ -
68	Northridge Local SD	Montgomery	1.76	190	$ 366,419	100.0	$ 366,419	$ -
69	Trotwood-Madison City SD	Montgomery	1.67	321	$ 617,744	100.0	$ 617,744	$ -
70	Morgan Local SD	Morgan	1.16	200	$ 385,896	100.0	$ 385,896	$ -
71	Zanesville City SD	Muskingum	1.76	374	$ 720,885	100.0	$ 720,885	$ -
72	Crooksville Ex Vill SD	Perry	1.12	99	$ 190,420	-	$ -	$ 190,420
73	New Lexington City SD	Perry	1.23	160	$ 307,119	-	$ -	$ 307,119
74	Southern Local SD	Perry	1.54	75	$ 144,358	100.0	$ 144,358	$ -
75	Eastern Local SD	Pike	1.59	78	$ 149,872	100.0	$ 149,872	$ -
76	Scioto Valley Local SD	Pike	1.83	139	$ 268,524	100.0	$ 268,524	$ -
77	Waverly City SD	Pike	1.19	148	$ 284,242	100.0	$ 284,242	$ -
78	Western Local SD	Pike	2.29	71	$ 137,067	100.0	$ 137,067	$ -
79	Windham Ex Vill SD	Portage	1.40	60	$ 116,235	100.0	$ 116,235	$ -
80	Mansfield City SD	Richland	1.97	524	$ 1,008,281	100.0	$ 1,008,281	$ -
81	Chillicothe City SD	Ross	1.29	286	$ 551,186	95.6	$ 526,933	$ 24,252
82	Huntington Local SD	Ross	1.09	105	$ 201,763	100.0	$ 201,763	$ -
83	Paint Valley Local SD	Ross	1.04	84	$ 160,840	100.0	$ 160,840	$ -
84	Scioto Valley Local SD	Ross	1.37	80	$ 153,256	100.0	$ 153,256	$ -
85	Bloom Local SD	Scioto	2.16	104	$ 200,851	80.0	$ 160,681	$ 40,170
86	Clay Local SD	Scioto	1.33	46	$ 89,343	-	$ -	$ 89,343
87	Green Local SD	Scioto	1.70	62	$ 118,905	100.0	$ 118,905	$ -
88	Minford Local SD	Scioto	1.08	103	$ 197,415	100.0	$ 197,415	$ -
89	New Boston Local SD	Scioto	3.39	47	$ 89,937	100.0	$ 89,937	$ -
90	Northwest Local SD	Scioto	1.69	134	$ 258,376	100.0	$ 258,376	$ -
91	Portsmouth City SD	Scioto	2.95	263	$ 506,625	100.0	$ 506,625	$ -
92	Valley Local SD	Scioto	1.80	100	$ 193,381	80.0	$ 154,705	$ 38,676
93	Washington Local SD	Scioto	2.06	118	$ 226,963	100.0	$ 226,963	$ -
94	Wheelersburg Local SD	Scioto	1.06	113	$ 216,905	100.0	$ 216,905	$ -
95	Fostoria City SD	Seneca	1.06	164	$ 316,459	44.9	$ 142,090	$ 174,369
96	Alliance City SD	Stark	1.59	291	$ 560,999	37.0	$ 207,569	$ 353,429
97	Canton City SD	Stark	2.12	1,063	$ 2,045,879	60.0	$ 1,227,527	$ 818,352
98	Massillon City SD	Stark	1.10	376	$ 724,012	100.0	$ 724,012	$ -
99	Akron City SD	Summit	2.29	2,838	$ 5,465,479	100.0	$ 5,465,479	$ -
100	Barberton City SD	Summit	1.58	351	$ 675,836	100.0	$ 675,836	$ -
101	Girard City SD	Trumbull	1.11	118	$ 228,082	100.0	$ 228,082	$ -
102	Niles City SD	Trumbull	1.21	192	$ 369,971	31.5	$ 116,430	$ 253,541
103	Warren City SD	Trumbull	2.67	650	$ 1,252,402	100.0	$ 1,252,402	$ -
104	Vinton County Local SD	Vinton	1.22	173	$ 333,006	100.0	$ 333,006	$ -
	Total			***50,176***	***$ 96,614,744***		***$ 79,234,203***	***$ 17,380,541***

IS WELFARE REFORM WORKING?

MEASURING THE OUTCOMES OF WELFARE REFORM

STEVE MANSFIELD

This article is the second part of a two-part series that looks at the progress of implementing Ohio's welfare reform program, Ohio Works First (OWF). The focus of the first article in the series was on the programmatic changes being introduced—the basic principles of the reform, the "devolution" of program authority to county government, and transformation of the program toward workforce development.[1] This second installment will look at the outcome and implementation studies and other reports required by Am. Sub H.B. 408, the changing characteristics of the welfare population, some measures of program outcomes, and along the way briefly consider the policy implications raised by those changing characteristics and outcomes.

An important set of changes in Ohio's welfare program was introduced in 1995 with the passage of H.B. 167. These changes shifted the guiding principles of Ohio's welfare program toward increasing the incentives to move off welfare and toward "self-sufficiency." The basic principles underlying H.B. 167 were that assistance was to be temporary and that finding work was to take priority over job-training or education. Ohio Am. Sub. House Bill 408, passed and implemented in 1997, refined and extended the "work first" strategy of welfare reform. It required applicants to agree to a self-sufficiency contract, including requirements on participating in job search or other forms of participation, accepting subsidized or unsubsidized employment, and cooperating with child support collection. Failure to sign the self-sufficiency contract is grounds to deny assistance, and failure to keep the terms of the contract subjects the recipient to sanctions.

Among the central goals of Ohio's welfare reform are ending dependence, increasing self-sufficiency, and reducing the caseload. To judge the extent to which those goals are being met requires information and data on what happens to the existing caseload and what happens to recipients after they leave the rolls. This article begins with an examination of the reporting requirements imposed by H.B. 408 on ODHS, and how these requirements are being met. The article also describes and analyzes data from the CRIS-E reporting system to see how the characteristics of OWF recipients have changed as the caseload declines. The article also contains a brief examination of data from two reports on closed cases that have been presented by the ODHS Office of Research. Along the way, several of the policy implications that are raised by the information are briefly discussed.

State Imposed Reporting Requirements

Am. Sub. H.B. 408 established a number of reporting and program evaluation requirements in the operation of OWF. In particular, sec. 5101.80 of the Revised Code requires the Ohio Department of Human Services to:

(9) Contract with a private entity to conduct an independent on-going evaluation of the Ohio Works First program and the Prevention, Retention, and Contingency program. The contract must require the private entity to do all of the following:

(**A**) examine issues of process, practice, impact, and outcomes;

(**B**) study former participants of Ohio Works First who have not participated in Ohio Works First for at least one year to determine whether they are employed, the type of employment in which they are engaged, the amount of compensation they are receiving, whether their employer provides health insurance, whether and how often they have received assistance or services under the Prevention, Retention, and Contingency program, and whether they are successfully self sufficient.

These requirements are being met by ODHS with two evaluation and outcomes studies—the Ohio Works First Evaluation, and the Closed Cases Study—which are to be conducted by outside entities. The next two sections outline the details of these two studies.

Ohio Works First Evaluation

A contract to perform the Ohio Works First Evaluation was awarded to MACRO International Inc., in September, 1998. The research and reporting will take place over the course of SFY 1999-2003, for a total contract amount including renewals, of about $1.7 million. ODHS has secured a federal grant that will pay for 95 percent of this cost. MACRO International has previous experience in evaluation of ODHS programs, having conducted an evaluation study of Ohio's Learnfare program.

The purpose of the contract is to conduct a process and impact study of OWF that evaluates a number of policy questions related to the implementation, operation, and structure of the program, and evaluates OWF's impact on helping welfare recipients achieve greater self-sufficiency and personal responsibility.

The impact portion of the study will be based on a number of different data collection and analysis techniques. One of the main features of the study will be a time series analysis of CRIS-E data as it relates to services provided, client characteristics, and client behaviors. Another key feature of the study will be longitudinal surveys of current and former OWF recipients, and also surveys with administrators, representatives of advocacy groups and community organizations, staff, and private sector employers. The first interim report of the impact study is due October 30, 2001.

The process study will focus on how processes implemented at the county level contribute to explaining client behaviors, attitudes, and perceptions. An intense multiple-site case study of 10 counties will provide in-depth analysis of the relationship between specific features of county practices and impacts on participants.

The process study is to have three basic components: an outcomes study for the Legislature, a cost analysis, and an implementation analysis.

The outcomes study for the Legislature will focus on former OWF participants who have not been involved with the program for at least one year. The outcomes study must address the specific questions posed in Section 5101.80(A)(9): whether these former participants are employed, the type of employment they have, the amount of compensation they are receiving, whether their employer provides health insurance, how often they have received assistance or services from the PRC program, and whether they are self-sufficient. MACRO has proposed a sample of about 1300 former recipients who were participating in OWF at its inception on October 1, 1997 and subsequently left the program, and have not been involved in the program for more than one year. In addition to the specific questions noted, above, MACRO will look at outcomes for various subgroups of recipients formed by such variables as work history, education level, age, household type, family size, race, sanctioning history, urbanicity, and the like. This report is due October 15, 1999.

The cost analysis will identify how OWF and PRC funds are spent and how the funds are related to program outcomes. This will involve developing a costing system on a county-by-county basis, and then estimating the costs of particular service outcomes. According to MACRO's proposal, the costing system will generate average cost figures for PRC services, work activities (like job search and placement services), developmental activities (e.g., training or education), alternate work activities (subsidized employment, work experience program), and support services (like child care and transportation). The results of this cost analysis will enable ODHS to most effectively deliver program services in future years.

The implementation analysis will focus on the structure and operation of the program at the county level. This part of the study will conduct a multi-site case study (apparently ten counties will provide the basis for the implementation study[2]) to examine "who receives what services; the intensity, duration and time of services; who provides the services or actions taken; and how these services or actions are linked to program outcomes."[3] The implementation study thus provides the explanation to the results or lack of results reported by the impact study. The first interim reports on the cost and the implementation analyses are due October 30, 2000.

Closed Cases Study

For the Closed Cases Study a RFP was publicized November 20, 1998. The purpose of the RFP was to produce a contract with a state-assisted university or college to develop and implement survey research among two populations of former welfare recipients—those who have left the Food Stamps Program (FSP) and those who have left the OWF program. The RFP indicates the need for this research by noting that, "while the recent strong economy has probably enabled many former welfare recipients to move from the welfare rolls to the workplace, little beyond anecdotal information indicates what happens to these groups once they leave FSP and/or OWF."[4] In addition to these two populations, county members of county staff and community groups will also be surveyed. A letter of intent to award the contract for the Closed Cases Study is scheduled to be issued February 3, 1999. A preliminary report of the results of the surveys is scheduled for May 31, 2000, with the final report for the results of the whole study scheduled for August 31, 2000.

Among the OWF population, three groups will be studied: 1) families and individuals who leave OWF; 2) families and individuals who apply for OWF but are never enrolled because they were diverted to other programs such as Healthy Start or the PRC program; 3) families and individuals with dependent children who applied and were eligible to enroll in OWF but did not enroll and were not diverted to other programs.

The study is not a statewide sample but rather a multi-site case study that will develop comparisons among counties of different sizes and location as well as comparisons of the effects of different county implementation policies on these populations. The sample, therefore, will be not be conducted statewide, but will be drawn from twelve sites, (pending approval from each county director). The proposed twelve study sites were selected because they allow comparisons among:

1) cross metropolitan sites (cities of Cleveland and Columbus),
2) intra-county urban sites (Cleveland, Euclid and Parma),
3) medium size counties that are located within urban areas, i.e., are within a Standard Metropolitan Statistical area (SMSA) (Clark and Allen),
4) medium sized Appalachian counties that are within SMSAs (Washington and Scioto),
5) two small Appalachian counties (Meigs and Vinton) with high poverty rates and another Appalachian county with a lower poverty rate (Noble),
6) two Appalachian counties with a high poverty rate (Meigs and Vinton) and a non-Appalachian county also with a high poverty rate (Ashtabula).

This multi-site case study will examine program effects not just along size, location, and poverty variables, but will also take into account differences in implementation policies.[5] The outcome variables to be studied include common reasons why recipients leave OWF and specific outcomes like "recidivism," employment, income, family formation and stability, household composition, home environment, well-being of children, dependence on relatives, and use of public and community programs. The study will also develop indicators of success in areas of income, housing, and food security for those who leave OWF. This will enable the study to also develop a profile of those recipients most likely to succeed and those who are most at risk of failure.

Additional State Reporting Requirements

In addition to the requirements just discussed, sec. 5101.80 (A)(10)(D) of the ORC requires the Ohio Department of Human Services to:

(D) not later than March 1, 1998, and the first day of each September and March thereafter until September 1, 2001, prepare a county by county report concerning individuals who cease to participate in Ohio Works First that contains the reasons the individuals ceased to participate, including employment, marital status, and relocation.

While this reporting requirement has not yet been met, a representative of ODHS has informed the author that a report satisfying this requirement is undergoing internal review, and will be released in the immediate future.

An additional reporting requirement for the future is established by H.B. 408 in sec. 5101.80 (A)(11) of the ORC. It requires ODHS to begin reporting January 2001, and every 6 months thereafter a county-by-county breakdown of individuals who cease to participate in Ohio Works First and the reasons the individuals ceased to participate, including exhausting the time limits, and those individuals who have been exempted from the time limits and the reasons for the exemption.

Caseload Analysis

There are two key ODHS sources for data on the OWF caseload that have been reported consistently both before and after the effective date of the introduction of OWF. These are the Department's monthly demographic and actual expenditures reports.[6] A number of important demographic and caseload statistics from these two sources are presented in Table 1. Table 1 summarizes key statistics from three significant points in time: September in each of 1996, 1997, and 1998. This presentation of caseload and demographic data enables a picture that compares the situation one year before the introduction of OWF to the situation immediately before the introduction of OWF, and to a point one year after the introduction of welfare reform.

There are a number of significant changes in the size and characteristics of the caseload that can be seen in Table 1. First, the caseload declined in size, losing 36,459 cases in the year before the introduction of OWF and 41,584 in the year after OWF started, according to the expenditures report (GRP342RA). The demographics report (GRP172RB) shows a reduction of 36,697 cases in the year before OWF and 45,920 in the year after OWF started. Looking at data from both reports, these declines represent a range of 17.5 to 18.1 percent in the year before OWF, and 25.1 to 26.9 percent in the year after OWF started. Hence OWF might be seen, all other factors being equal, as leading to an acceleration of between 39 to 54 percent, depending on which report is relied on, in the rate of decline in the year after introduction.[7] An important question that we will turn to later is whether the introduction of OWF has lead to, or can be connected with, an increase or decrease in the rate of case closures and an increase or decrease in the rate of application and application approval.

OWF Recipient Demographics

HUM Report		Sept., 1996	Sept., 1997	Sept., 1998
GRP342RA	**Recipients**	541,055	433,820	319,912
	Assistance Groups (Cases)	201,945	165,486	123,902
	Child-Only Cases	49,667 (24.6%)	48,039 (29.0%)	35,643 (28.8%)
	Cases by County Size			
	Urban (8 largest counties)	64.1%	65.7%	71.8%
	Non-Urban	35.9%	34.3%	28.2%
	Recipients by Designation			
	Regular	85.8%	87.8%	89.4%
	Unemployed	10.6%	8.7%	6.1%
	Incapacitated	3.5%	3.5%	4.5%
	Recipients by Age			
	Adults	30.5%	29.0%	29.0%
	Children	69.5%	71.0%	71.0%
GRP172RB	**Recipients**	545,479	431,786	311,117
	Assistance Groups (Cases)	210,094	170,397	124,477
	Cases by Group Size			
	1 Person	19.6%	22.7%	25.4%
	2 Persons	34.9%	33.8%	32.5%
	3 Persons	24.1%	23.1%	21.8%
	4+ Persons	21.4%	20.4%	20.3%
	Recipients by Sex			
	Female	62.4%	62.1%	61.9%
	Male	37.6%	37.9%	38.1%
	Recipients by Race/Ethnicity			
	African-American	43.5%	47.0%	52.4%
	Caucasian (non-Hispanic)	51.9%	48.4%	43.0%
	Other	4.6%	4.6%	4.6%
	Adult Education Level			
	H.S./GED	57.0%	56.1%	54.1%
	No H.S./GED	43.0%	43.9%	45.9%
	Adult Recipients w/ Earnings	14.1%	17.6%	24.2%
	Avg. hours employed per mo.	108	112	120

The caseload demographics also reveal some significant changes. The caseload is increasingly urban, going from about 64 percent urban one year prior to OWF to almost 72 percent urban one year after OWF. The findings from a 1998 Briefing Report from the Center on Urban Poverty and Social Change, at Case Western Reserve University, titled, "Welfare Reform: Using Local Labor Market Data for Policy and Analysis and Program Planning," deserve mention here. Among the major findings about the distribution of welfare recipients and entry-level job opportunities in Cuyahoga County were the following points:

- OWF recipients are highly concentrated in certain portions of the metropolitan area, most within the city of Cleveland.
- About 80 percent of entry-level job opportunities are in suburban areas.

- Only 8 to 15 percent of entry-level job opportunities can be reached in a twenty-minute commute by public transportation from many inner-city neighborhoods.
- Only 3.8 percent of 1990 employment in suburban job clusters consisted of individuals commuting by automobile from the central city; only 0.2 percent consisted of individuals commuting by bus from the central city.
- Affordable housing in proximity to suburban job clusters is scarce. Although the metropolitan area ratio of affordable housing units to entry-level job openings is 7 to 4, in the outer suburbs it drops to 1 to 6. Relatively more affordable housing is available in proximity to the inner suburbs, where the ratio is 4 to 1.

With over 70 percent of the OWF caseload now being composed of recipients in the top six urban counties, issues related to the geographic gaps between transportation and housing resources and entry-level job opportunities are increasingly significant. As the authors of the Briefing Report just discussed point out, the information from their or similar studies can be used to plan job training and job search assistance programs, to plan for the provision of public transportation services, and to plan various work support interventions, such as the location of job training programs and child care facilities.

The data also show that as the caseload declines it is becoming more concentrated in Appalachian counties with high poverty and unemployment rates.[8] Recipients in these areas would face a similar lack of proximity to job opportunities.

The average size of assistance groups has declined significantly. The most important development being the increase in the one person group, which are largely "child-only" cases. "Child Only" cases occur when adults in the household are ineligible for OWF benefits or they are recipients in other programs. The relationship of non-recipient adults in the household is most often a grandparent, other relative, natural parent, or foster parent. Such cases are exempt from time limits and work requirements. "Child only" cases now compose nearly 30 percent of the total caseload.[9]

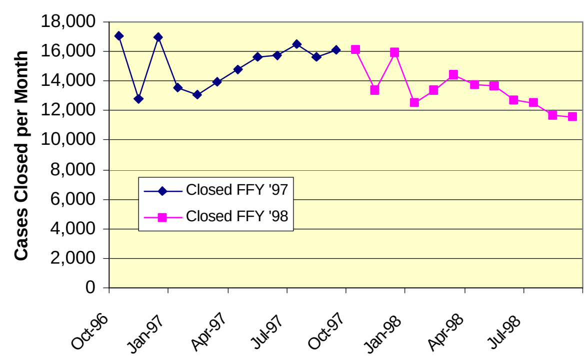
Another very significant change is the racial composition of the caseload. Whereas non-Hispanic Caucasians made up 52 percent of the caseload one year before OWF, this group constituted only 43 percent of the caseload one year after OWF. This trend of increasing racial and ethnic minority make-up of recipients has been seen throughout the nation, and may be explained, in Ohio, in large degree by the increasing urban composition of the caseload.[10]

We also see in Table 1 that there has been a substantial increase in the percentage of adults with earnings, and that the average hours per month of those who are employed has risen significantly. This shift seems to be due to the work requirements imposed by H.B. 167 and H.B. 408, and to the change in the increase in the time period when earned income up to a certain limit is disregarded in calculating benefit amounts.[11]

There is also a small decline in adult recipients with a high school degree or GED. The percent of adult recipients with high school or GED went from 57 percent one year prior to OWF to 54.1 percent one year after the introduction of OWF. As might be expected, this indicates that those adults who have completed high school or a GED leave the caseload at a slightly higher rate that those who are less educated.

Figure 1 is derived from data that ODHS reports to the federal government regarding the number of closed cases and the reasons for closure. Calculations from this data indicate that there is a decrease in the case closure rate, resulting in over 20,000 fewer cases being closed in the year after the implementation of OWF than in the year before OWF. Yet, instead of this resulting in an increase in the overall caseload, the overall caseload in the year after OWF

Figure 1
OWF Cases Closed per Month, FFY 1997 and FFY 1998



started was reduced by some five to six thousand more cases (depending on the report, as we saw in Table 1) than in the year prior to introduction. Two important questions are immediately suggested by these observations: what causes the case closure rate to slow down after the implementation of H.B. 408? What are the reasons for the overall increase in the rate of decline of the caseload? These two questions indicate there are both entry and exit effects that need explanation.

Among entry effects that could explain the accelerated rate of caseload decline along with a lower rate of case closure are a decrease in applications, or a decrease in applications approved. Unfortunately, there is not a lot of reliable data on application and application denial rates. While there is an ODHS report that purports to tally both applications and denials, this author has been advised by the ODHS Office of Research that this report does not report these statistics reliably. Examination of the denial rate of applications is thus prevented by the lack of information. However, ODHS does report in the September 1998, Ohio Works First Progress Report that the monthly application rate had decreased by more than 11 percent in the course of the year from May 1997 to May 1998. This observation suggests that a very significant reduction in applications has occurred and that this could be responsible for most of the caseload reduction. This possibility can only be borne out, however, when and if reliable historical data on applications and application denials becomes available.

A related question on the entry effects side is whether the PRC program is related to fewer applications being filed as a result of potential applicants being "diverted" by PRC benefits. An examination of statewide PRC expenditures shows that there has not been any significant increase during the first year of operation of PRC when compared to expenditures in the Emergency Assistance program, which PRC replaced.[12] It, therefore, seems likely that what accounts for most of the decline in the application rate changes is the change in program requirements for participants, along with a very strong economic climate, the increase in real wages for low-income workers, the expanded use of the federal Earned Income Tax Credit, and the declining real value of the cash benefit that is paid to recipients,[13] rather than the introduction of the PRC program.

The exit effect seen in Figure 1, during the first year of operation of OWF, indicates a substantial decrease in the case closure rate. This decrease could have several causes. For example, a change in program incentives could encourage recipients to stay on the caseload longer. The increase in the time period in which the earned income disregard can be used by recipients (from 12 to 18 months), may stretch out the period of transition off welfare. Another possibility is that, as the caseload has declined in size, adult recipients who were most employable have already left the program in substantial numbers, and those remaining adult recipients have more barriers to employment, thus exiting at a slower rate. At the present time it is not possible to develop a clear understanding of the exit effect. The reports on closed cases required by H.B. 408 will, hopefully, provide some clear answers.

ODHS, Office of Research, OWF Closed Case and Wage Match Study

The ODHS Office of Research has, to-date, presented data and follow-up information on individuals who have had their cases closed during October, 1997, November, 1997, and January, 1998, respectively. The study on cases closed in January employed a random sample from the whole population of closed cases. However, the sample size (116 cases from one month's closed cases in a sample designed to be drawn over the course of twelve months) was so small as to yield results with margins of error that were beyond broadly accepted research standards. However, the analysis of the October and November '97 cohorts was conducted on the whole population of closed cases. The November '97 cohort of closed cases was also matched to the Ohio Bureau of Employment Services (OBES) wage records. Following are some of the significant findings from the analysis of the October and November '97 cohorts of closed cases:

- 84.4 percent of the adults in closed cases from October '97 were Caucasian, while only 48 percent of all recipients were Caucasian.
- 28.6 percent of the adults in closed cases from October '97 were married, almost twice the percentage of all adults recipients.
- Only 23 percent of the adults whose cases were closed in October '97 were employed at the time when the case was closed.

- 45 percent of the cases closed in October '97 were re-opened within 9 months. About half of these were re-opened within the first month after being closed.

- 49. 4 percent of the cases closed in November '97 were re-opened within 10 months.

- Of all the adults who left the caseload in November '97, only 36.3 percent were found in the wage match to have earnings in the first full quarter after they had left OWF.

- Of those adults who left the caseload in November '97, and who had stayed off consistently as of September '98, only 42.7 percent were found in the wage match to have earnings in the first full quarter after they had left OWF.

What kind of jobs do former recipients get? How long do former recipients keep those jobs? What kind of earnings do former recipients have? These questions remain to be answered. As noted above, the studies undertaken in compliance with the provisions of ORC Sec. 5101.80 (9) should provide answers to these questions. However, the first results of any of these studies will not be available until later this year, with many of the initial results of some portions of these studies scheduled for release in 2000 and 2001.

In the meantime, the county-by-county report required by ORC 5101.80 (10)(D) on the number of individuals who cease to participate in OWF, and the reasons why, will be available in the immediate future, according to ODHS. In addition, ODHS is working with a group of "stakeholders" who are in the process of developing a set of indicators that can be readily gathered to assess areas in the state experiencing comparative difficulties in various aspects of the process of helping recipients achieve greater self-sufficiency. These indicators can then be used to guide special interventions or shifts in implementation strategies to address the difficulty.

This article has outlined the steps that will be taken to measure the outcomes of welfare reform. Evaluation of the transition from a program that has been designed for the purpose of "income maintenance" to a program that serves the "workforce development" needs of the poorest segment of our population is absolutely essential to the success of the effort. As the reader of this and the previous article in this series is sure to have surmised, welfare reform is and has been an exceedingly large and difficult task that has an extensive past, has seen a number of significant goals accomplished already, but has a number of steps yet to go. ❑

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1 Steve Mansfield, "Is Welfare Reform Working? Implementation of Welfare Reform," *Budget Footnotes*, Nov.-Dec. 1998, pp. 91-96.

2 See MACRO International, Technical Proposal, in response to RFP 98-012, July 10, 1998, p. 100.

3 Ohio Department of Human Services, RFP 98-012, May 15, 1998, p. 13.

4 Ohio Department of Human Services, RFP 98-020, November 20, 1998, p. 1.

5 In this respect the Closed Cases Study seems to overlap with the implementation analysis of the Ohio Works First Evaluation.

6 These are the ODHS, "Statistics for OWF Recipients" Report I.D. GRP172RB and monthly "Summary of Actual Expenditures" report generated from the GRP342RA database. A new report, the "OWF Demographics Report," which contains a more comprehensive set of statistics, has been available only since June, 1998.

7 This analysis differs significantly from ODHS analysis which saw a near doubling in the rate of decline, even when comparing the year prior to the start of OWF to the first nine months under OWF. See ODHS, Ohio Works First Progress Report, September 16, 1998, p. 3.

8 See the summary of data on caseload concentration in Appalachian counties in ODHS, Ohio Works First Progress Report, September 16, 1998, p. 5.

9 For data on the historical trend in "child only" cases in Ohio, see, Steve Mansfield, "'Child Only' Cases Constitute a Significant Portion of OWF Caseload," *Budget Footnotes, Ohio Facts Extra*, Oct. 1998, p. 56.

10 See also, ODHS, Ohio Works First Progress Report, September 16, 1998, pp. 4-5.

11 See Steve Mansfield, "Percentage of ADC/OWF Adults with Reported Earned Income Reflects Implementation Dates of Federal and State Welfare Reform," *Budget Footnotes, Ohio Facts Extra*, March 1998. p. 149.

12 See Steve Mansfield, "Is Welfare Reform Working? Implementation of Welfare Reform," *Budget Footnotes*, Nov.-Dec. 1998, p. 92.

13 While Ohio's nominal monthly benefit for a family of 3 has risen 54 percent since 1978, when inflation is taken into account, the real value of the maximum monthly benefit for such a family has declined by 38 percent.

CHECKING IN ON E-CHECK
OHIO'S AUTO EMISSIONS TESTING PROGRAM

ERICA THOMAS

During the Controlling Board meeting on December 20, 1998, modifications were approved for the contract with MARTA Technologies and the automobile emissions testing program (E-Check) in the State of Ohio. The following article describes the events which led to that Controlling Board request and the expected results.

E-Check Background

In response to the federal Clean Air Act (CAA) amendments of 1990, Ohio was required to implement an automobile emissions testing program. Specifically, the CAA required that "moderate" ozone non-attainment areas implement a "basic" emissions testing program in fourteen (14) counties which included the Cleveland/Akron, Dayton/Springfield and Cincinnati metropolitan areas. In addition to the mandate for basic testing, the Clean Air Act also mandated a 15 percent reduction in smog-causing emissions in these areas. In response to these federal mandates, the Ohio General Assembly passed legislation that gave local elected officials two options for compliance with the Clean Air Act. The first option was a basic testing program along with some type of additional air pollution control program (i.e. alternative fuels) implemented in their areas. The other option was an enhanced automobile testing program that would eliminate the need for additional air pollution control programs. In each area, the local officials chose the enhanced testing option.

In the mandated counties, all vehicles that are 10,000 pounds or lighter, and 25 years old and newer are required to undergo the E-Check test every other year before the vehicle registration can be renewed. New vehicles registered to their original owners are exempt from testing for the first two years of ownership. Used vehicles require a test before they can be registered to a new owner unless the previous vehicle owner supplies the new owner with a valid E-Check certificate.

The cost for an E-Check inspection is $19.50. The Ohio Environmental Protection Agency (OEPA) Motor Vehicle Inspection and Maintenance Fund (Fund 602) receives a fee of approximately $1.65 for each vehicle tested.

What Changes Were Needed?

MARTA Technologies was selected as the contractor to operate the facilities in the Cincinnati area through a Request for Proposal process. The original cost proposal submitted by MARTA Technologies in 1995 projected the cost of the contract to be $114,636,869 for a ten-year period. The contract is effective from January 1996 through December 2005. A total of thirteen facilities located throughout Butler, Clermont, Hamilton and Warren counties were constructed with a total of 53 lanes.

In January 1996, the E-Check program started and motorists were required to comply with the biennial inspection prior to registering their vehicles with the Ohio Bureau of Motor Vehicles. During the start-up in 1996, motorists in the affected counties experienced unacceptable delays, damage to vehicles, and poor customer service. In an effort to diminish dissatisfaction with the program, Ohio EPA implemented many improvements in the program such as: temporary and hardship extensions, a repair spending cap and the payment of test fees by check.

As a result of MARTA Technologies' failure to perform key elements in the contract for the E-Check program in Cincinnati, OEPA proposed to terminate the contract in August 1996. In response to OEPA's proposed termination, MARTA Technologies filed an injunction. The Franklin County Common Pleas Court ruled in September 1996 that OEPA could not prevent MARTA Technologies from operating the program and that problems experienced by MARTA Technologies were not uncommon for the start-up period.

From mid-August 1996 through December 1997, the E-Check program did not operate in the Cincinnati area. During this period, MARTA Technologies was exploring two options: 1) subcontracting the emissions testing program in Cincinnati to a third party; and 2) continuing negotiations with OEPA for getting the program operational in southwest Ohio in order to comply with the federal mandate for an emissions testing program. OEPA was unsure whether Cincinnati would be able to reach attainment for the federal ozone standard, therefore operation of the E-Check program was critical to maintaining air quality. MARTA agreed in October 1997 to re-start the E-Check program in January 1998.

MARTA Technologies subsequently re-started the program in January 1998 for motorists whose registrations expired in February. OEPA initiated an intensive oversight program for approximately four months to provide increased customer service and monitor performance by the contractor. Additionally, OEPA has been meeting with MARTA Technologies several times a month to discuss technical issues for improving the program.

In the interim, MARTA filed a lawsuit in December 1997 against the State of Ohio for $39 million in damages which MARTA claimed they incurred as a result of the proposed termination action initiated by OEPA. That following July, OEPA and MARTA Technologies began technical settlement discussions to explore options of converting the current I/M 240 enhanced program to a less intrusive enhanced Acceleration Simulation Mode (ASM) test. As a result of these discussions, MARTA Technologies agreed to convert to ASM and settle the $39 million lawsuit with OEPA.

Changes Authorized for Contract

The Controlling Board gave approval to modify the current I/M 240 program in the Cincinnati area to offer motorists a less intrusive, quicker emissions inspection. The Acceleration Simulation Mode test offers advantages such as testing vehicles at a steady speed of 25 miles per hour, rather than varying speeds up to 57 miles per hour. In May 1998, OEPA had agreed to a similar settlement with the state's other E-Check contractor, Envirotest Systems. Envirotest converted the E-Check program to ASM in the Cleveland/Akron and Springfield/Dayton Areas. This new test will be used in all 14 counties where E-Check is required, now that the new test will be implemented in the four-county Cincinnati area. Approval of the Controlling Board request allows all testing areas to operate the same test procedures and standards. Additionally, OEPA anticipates reduced instances of damage to vehicles compared to the I/M 240 inspection.

The conversion to the ASM test will take place in two phases, beginning March 1, 1999. To allow for a smooth transition to new equipment and software, the change will begin with a new "quick test." On January 3, 2000, the test will be converted to the ASM 25/25 test, which is very similar to the "quick test." Both use a dynamometer, a set of rollers on which the vehicle is driven. But vehicles are accelerated only to a steady 25 or 30 miles per hour, as opposed to being tested on a range of driving speeds up to 57 miles per hour with the I/M 240 test. The test fee will remain $19.50.

In addition to the test change, the settlement will allow MARTA Technologies to operate the E-Check stations 55 hours a week instead of 65. MARTA Technologies also will be able to close the stations on every state holiday instead of only the major holidays. This will be consistent in all of the areas affected by E-Check. In addition, MARTA Technologies will close three lanes in the Ridgewood station after a throughput analysis and capacity study showed that this station was underutilized.

The Results of Contract Changes

The ASM test will provide for approximately 93 percent of the VOC emissions reductions initially anticipated with the I/M 240 test. Ohio will remain in compliance with federal requirements. OEPA expects to compensate MARTA Technologies with $2,420,630 for the conversion to ASM. The Air Pollution Control Administration Fund (Fund 696) will be responsible for $1 million of this compensation, and the Motor Vehicle Inspection and Maintenance Fund (Fund 602) will be responsible for $1,420,630.

The Motor Vehicle Inspection and Maintenance Fund receives approximately $1.65 from each E-Check test fee. The Air Pollution Control Administrative Fund receives fines collected from civil penalties imposed for violations of the state's air pollution control law. ❑

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