



OHIO CONSTITUTIONAL MODERNIZATION COMMISSION

MINUTES OF THE FINANCE, TAXATION, AND ECONOMIC DEVELOPMENT COMMITTEE FOR THE MEETING HELD THURSDAY, JUNE 9, 2016

Call to Order:

Chair Douglas Cole called the meeting of the Finance, Taxation, and Economic Development Committee to order at 11:51 a.m.

Members Present:

A quorum was present with Chair Cole and committee members Amstutz, Asher, Clyde, Davidson, Mills, and Peterson in attendance.

Approval of Minutes:

The minutes of the May 12, 2016 meeting of the committee were approved.

Committee Discussion:

Chair Cole began the meeting by indicating that three reports and recommendations that had been issued by the committee at its last meeting were approved by the Coordinating Committee and would be forwarded to the Commission for a first reading.

Chair Cole then stated, with regard to the committee's review of Article VIII, Sections 4, 5, 6, that the state is involved in a lawsuit challenging the JobsOhio program that is related to those sections of the constitution. He said, in the interests of full disclosure, that, as a private practice attorney, he represents JobsOhio and is lead counsel.

Chair Cole further disclosed that attorney Gregory W. Stype, of Squire Patton Boggs (US) LLP, who is one of the presenters appearing before the committee, is also counsel for JobsOhio. Chair Cole said the legal representation does not prevent either attorney from presenting or participating, but, he said, the committee will want to be careful to hear all viewpoints on Article VIII, Sections 4, 5, and 6.

Presentations:

Gregory W. Stype
Squire Patton Boggs (US) LLP

Chair Cole introduced Mr. Stype, who represents the Ohio Public Facilities Commission (OPFC) as bond counsel. Chair Cole indicated Mr. Stype would be presenting to the committee on the topic of Article VIII, Sections 4, 5, and 6, related to the credit of the state, the assumption of debt by the state, and the prohibition against local governments becoming stockholders.

Mr. Stype began by noting that the core aspects of Sections 4 and 6 are the same: they limit the power of the state in Section 4, and limit the power of local governments in Section 6, to lend aid in credit or to become a joint actor with private enterprise. He said, in the 1851 constitution, those sections, as well as Section 5, sprung out of the troubled financial history of the railroads and canals. Mr. Stype noted that the version of Section 6 that is now in the constitution results from an amendment in 1912 to add the five lines that do not prohibit joining with insurance companies to insure property and risk. He said, while that provision seems unrelated, the logic becomes clear if it is considered that insurance was an evolving industry at that time and the language was believed necessary to protect that institution in the constitution.

Mr. Stype said Section 5, which restricts the state from assuming the debts of any political subdivision unless the debt was created for the purpose of addressing civil unrest, is often overlooked. He further noted the constitution does not stop with Sections 4, 5, and 6 in addressing lending aid in credit because express exceptions have been put in place.

Mr. Stype continued that, through action by voters or by the courts, the language has been illuminated and additional amendments have refined the meaning of the sections.

He noted that Section 13, adopted in 1965 and amended in 1975, allows the issuance of industrial development bonds and resulted from an Ohio Supreme Court ruling in 1964 that, even though a proposed test bond issue did not put any of the state's resources at risk, Section 4 precluded that kind of bond issue.¹ Thus, Section 13 provides that bonds can be issued and loans made for projects for industry, commerce, distribution, and research, with an important proviso that monies raised by taxation may not be obligated or pledged to the payment of those bonds. He said the amendment is designed to allow industrial development bond financing to convert federal tax benefits to the projects, but not to commit state tax dollars.

Chair Cole asked whether the state is viewed as a conduit or guarantor in that situation. Mr. Stype indicated that if the state is a guarantor, it can only do so from nontax revenue sources. He gave as an example that when the state made pledges of abandoned deposits that were collected by the Department of Commerce through its banking division. He added there are programs for loans being made and payments received back in circumstances where there is a large and predictable revenue stream that can be leveraged through bonds and loans made. He said an example of that type of program is the Ohio Turnpike. He said the turnpike tolls are not taxes,

¹ *State ex rel. Saxbe v. Brand*, 176 Ohio St. 44, 197 N.E.2d 328 (1964).

and so that money is not a debt of the state, does not invoke the state taxing power, and all payments come from turnpike users.

Chair Cole asked Mr. Stype to provide an example of a project for which bonds are issued under Section 13. Mr. Stype said this option is used less frequently because federal tax law has become more constrained, but, he added, there are bonds that have federal tax benefits for air and water pollution control at private industrial facilities. He said those bonds are going to be repaid by those companies, but the bonds could not be issued absent Section 13.

Committee member Herb Asher asked, with regard to Section 4, whether universities can become co-owners with private sector entities. Mr. Stype answered that, as a general proposition, state universities are subject to the same restrictions as other state agencies, but structures have been created to allow projects such as making land available to build private residence halls. He said, generally, if a project is in the service of a public purpose and the state taxing power is not being exposed to risk, then a project has Section 13 ramifications.

Representative Ron Amstutz asked what category liquor sales profits fall into. Mr. Stype said those are out of the state's taxing power, as established by the Ohio Supreme Court in *State ex rel. Duerk v. Donahey*, 67 Ohio St.2d 216, 423 N.E.2d 429 (1981).

Mr. Stype continued his presentation by noting Section 14, adopted in 1982, authorized loans for housing in Ohio, an amendment that was driven by a 1976 Ohio Supreme Court decision concluding that, despite Section 13, the words "industry, commerce, distribution, and research" did not encompass housing. Thus, the Court said, if voters wanted to create that benefit the constitutional section specifically would need to indicate housing. *State ex rel. Brown v. Beard*, 48 Ohio St.2d 290, 358 N.E.2d 569 (1976).

Mr. Stype described Section 15, adopted in 1985, as authorizing the state to issue bonds to fund loans for coal research and development purposes, allowing the state to share in the returns from the bonds.

Mr. Stype said Section 16, adopted in 1990, broadened the loans-to-lenders regime that existed under Section 14, opening the door to a wider variety of housing loans.

Mr. Stype noted that, in 1993, Section 21 was adopted to authorize general obligation bonds for capital improvements for parks, land, and water recreational facilities. He said that section also says Sections 4 and 6 do not apply.

With regard to the adoption of Section 20 in 2000, he said in 2008 that provision was extended and enlarged in terms of its amount. He said that section authorizes issue of general obligation bonds for environmental and related conservation and revitalization purposes.

Chair Cole asked whether the state can become a joint owner. Mr. Stype said that would not be possible, but that the practice has been for the state to get the loan for the revitalization project and partner with local communities. He noted that owners of "brownfield" sites that require

revitalization cannot qualify for state assistance if they are the ones who created the dirty site; rather, it is the subsequent owner who qualifies for state assistance.

Chair Cole asked whether the state can participate in the profit stream, or whether the money is awarded as a grant. Mr. Stype said that type of assistance is primarily designed to provide grants, but there is also a limited amount of loans.

Rep. Amstutz asked, regarding Section 2o, whether there is an interpretation that the conservation provision could allow for some participation in some of the conservation practices that would prevent or curtail pollution, such as wastewater treatment. Mr. Stype said that might fall under Section 2o or under some other constitutional provision.

Mr. Stype noted the last set of exceptions to Sections 4, 5, and 6, are found in Section 2p, the “Third Frontier Amendments,” that were originally adopted in 2005, and extended in 2010. He said Third Frontier projects are those for which there is state authorization to issue general obligation bonds to fund research and development, and for sites and facilities for support of Ohio industry, commerce, research, distribution, and development. He noted “shovel ready sites” was the title that was used, meaning property that is ready and prepared for development. He said these moneys were invested in ways that allowed private industry to be part of the picture, so there had to be an exception to Sections 4 and 6. He said, with a couple of exceptions, all bond issues are subject to General Assembly authorization and are often subject to limitations in terms of the amount that can be issued in a given year, outstanding, or in total, or are subject to the five percent debt service limitation. So, he said, there are restrictions on these bonds.

Mr. Stype then reviewed case law relating to Sections 4, 5, and 6. He identified one case, *Grendell v. Ohio Environmental Protection Agency*, 146 Ohio App.3d 1, 764 N.E.2d 1067 (9th Dist. 2001), involving contracting for services, as one of the best cases for a history of Sections 4 and 6. In that case, the Ninth District Court of Appeals determined it was acceptable under Sections 4 and 6 for the state to contract with private vendors to implement an automobile e-check system, holding that hiring a private vendor is not same as joining together in enterprise.

Mr. Stype also indicated *State ex rel. Dickman v. Defenbacher*, 85 Ohio App. 398, 86 N.E.2d 65 (10th Dist. 1948), held the state can appropriate moneys out of the general fund, even where the state could not issue debt for that purpose. He said a current appropriation is not a long-term commitment of the state’s financial resources and not a debt. Regarding public purpose themes, he said, in 2006, another case examined the purpose of public education, while another case dealt with health care. *State ex rel. Ohio Congress of Parents & Teachers v. State Bd. of Educ.*, 111 Ohio St.3d 568, 2006-Ohio-5512, 857 N.E.2d 1148 (2006); *State ex rel. Taft v. Campanella*, 51 Ohio App.2d 237, 368 N.E.2d 76 (8th Dist. 1977). Mr. Stype described another case dealing with intergovernmental arrangements, *Bazell v. Cincinnati*, 13 Ohio St.2d 63, 233 N.E.2d 864 (1968), which related to a stadium construction project.

Mr. Stype said some cases recognize that if the goal is to accomplish a public purpose through nonprofit corporations, Sections 4 and 6 do not prevent those kinds of arrangements. Mr. Stype said an early case standing for that principle, in 1922, held the state could give money to

agricultural fairs. *State ex rel. Leaverton v. Kerns*, 104 Ohio St. 550, 136 N.E. 217 (1922). He said a 1983 case involving housing for the homeless determined that it is appropriate for a political subdivision to contract with a nonprofit corporation to provide services to the inhabitants of the political subdivision that could be provided by the municipality itself as a public service. *Franklinton Coalition v. Open Shelter, Inc.*, 13 Ohio App. 3d 399, 469 N.E.2d 861 (10th Dist. 1983).

Mr. Stype identified only two cases interpreting Section 5: *Butler Cty. Transp. Improvement Dist. v. Tracy*, 120 Ohio App.3d 346, 697 N.E.2d 1089 (12th Dist. 1997), and *Long v. Ohio State University*, 24 Ohio App. 261, 157 N.E. 395 (10th Dist. 1926). In both cases, the Court upheld the financing arrangements as falling outside the prohibition created by Section 5.

Mr. Asher noted a state revenues program linked to a deposit program out of the state treasurer's office, wondering if that program required a special statutory or constitutional provision to allow the treasurer to do that or whether, instead, the treasurer has the power to make decisions to invest. Mr. Stype said that program was authorized by statute.

There being no further questions for Mr. Stype, Chair Cole thanked him for his presentation.

Jonathan Azoff
Director of Office of Debt Management and Senior Counsel
Office of the Ohio Treasurer

Chair Cole recognized Jonathan Azoff, director of the Office of Debt Management and Senior Counsel to the Ohio Treasurer of State. Mr. Azoff presented to the committee on the topic of a state constitutional provision giving the Ohio treasurer the responsibility of reporting on State debt.

Mr. Azoff said currently the treasurer's office fulfills three core functions relating to state debt. He said, first, the treasurer is the issuer of debt, specifically, the state's general obligation highway debt, its Grant Anticipation Revenue Vehicle (GARVEE) transportation bonds, and its lease-appropriation debt. He said the treasurer also serves as a conduit issuer for the state's federal and state infrastructure bank programs, the Ohio Enterprise Bond Program, and the Community College Intercept Program, as well as performing certain duties as a member of the OPFC in connection with OPFC issuances.

Mr. Azoff said, as a second core function, the treasurer's office ensures the timely payment of the state's approximately \$11 billion in outstanding debt, acting as paying agent and bond registrar for all general obligation debt and coordinating debt payments via corporate bond trustees for revenue and special obligation debt. He added that the treasurer's office calculates payments on state-issued swap agreements and evaluates remarketing agent performance on the State's outstanding variable rate obligations.

Mr. Azoff described the treasurer's third core function in relation to debt is to report on the state's debt.

In relation to constitutional provisions creating a sinking fund and a sinking fund commission, Mr. Azoff said there is significant overlap between the treasurer's debt-related duties and responsibilities delegated to the commissioners of the sinking fund. He noted, while the commissioners of the sinking fund have not met since 2008, the sinking fund commission's constitutionally-delegated duties are being performed. With regard to duties delegated to the treasurer, Mr. Azoff said for at least the last 47 years, the treasurer has prepared the semi-annual report, distributing it twice a year to the governor and all members of the General Assembly. He said the report details general obligation bond activity for the preceding six-month period, providing extensive financial information regarding the state's ten types of outstanding general obligation bonds.

In addition to that reporting function, Mr. Azoff described that the treasurer also fulfills the sinking fund commission's duty to pay interest and redeem the principal on the state's general obligation debt, and does so in the capacity of the "Commissioners of the Sinking Fund." He said the "Commissioners of the Sinking Fund" receive appropriations in every state operating budget for this purpose, noting that in fiscal year 2016, the "Commissioners of the Sinking Fund" were appropriated more than \$1.1 billion. He said the Office of Debt Management at the treasurer's office transacts business using these funds as the "Commissioners of the Sinking Fund" in the state's accounting system, timely paying the state's outstanding debt from the designated bond service funds.

Mr. Azoff emphasized the treasurer does not have independent legal authority to perform many of these tasks, relying instead on the legal framework set out in the constitution. He said if Article VIII, Sections 7 through 11 are repealed, a replacement will be required.

Mr. Azoff advocated for a constitutional amendment providing for the state treasurer to report on the state's debt. He said creating such an amendment would continue the historical tradition of the semi-annual report, and retain an important constitutional principle requiring publicly-elected officials to demonstrate accountability for the money the state borrows, which taxpayers are ultimately responsible to repay.

Mr. Azoff said the committee should not stop there but should also recommend an amendment that would expressly charge the treasurer's office with the responsibility for paying the state debt.

Mr. Azoff said the "archaic Commissioners of the Sinking Fund can be modernized without removing the Constitutional accountability for statewide elected officials that was put in place at the Constitutional Convention of 1851. There has not been testimony indicating that that safeguard is no longer necessary." Mr. Azoff concluded, saying it is important to continue the practice of holding statewide elected officials accountable in the constitution for the management, reporting, and payment of the state's debt.

Chair Cole asked where the treasurer's reporting function is reflected in the law and whether there is statutory authority for this function. Mr. Azoff said there is statutory authority that does not specifically reference the sinking fund but rather references the sinking fund commission.

Chair Cole said he thought the OPFC was doing many of the functions that had been assigned to the sinking fund commission. Mr. Azoff said, with regard to issuance of debt, the reporting on debt is prepared by the treasurer under the seal of the sinking fund commission, and there is a semiannual report prepared by the treasurer in the capacity of the office of the sinking fund.

Chair Cole asked what gives the treasurer the authority to do that if the sinking fund is not meeting. Mr. Azoff said the statute permits the sinking fund to issue the report, allowing appointment of a clerk, who is the treasurer.

Chair Cole asked if there is anything that would prevent the General Assembly from creating a statute to address this procedure. Mr. Azoff said there is not, but there is value in keeping the treasurer's role in the constitution. He added he is not aware of any statutory authority for preparing the report.

Committee member Fred Mills asked whether Mr. Azoff is suggesting that there should be independent authority in the constitution if the committee recommends elimination of sinking fund. He noted those functions should be given to the treasurer as an alternative, but wondered if that provision must be in the constitution.

Mr. Azoff said the overarching point is, if the sinking fund is out of date but the function is not, Ohio would be losing some safeguards.

Discussion:

With regard to addressing the sinking fund, Chair Cole noted that the committee already voted to issue a report and recommendation that the sinking fund provisions, Article VIII, Sections 7, 8, 9, 10, and 11, be repealed. He said that action does not prevent adopting a separate provision that constitutionally assigns the reporting duties to the treasurer or anyone else. Chair Cole said the committee should consider whether to move forward with formulating a new provision that would assign the duties currently assigned to the sinking fund commission and the treasurer to another government official.

Chair Cole said the committee is not yet in a position to discuss Sections 4, 5, and 6, so that discussion would be saved for another meeting.

Chair Cole said the benefit of the constitutional provisions relating to the sinking fund was that they required participation by the five statewide elected officials.

Committee member Jo Ann Davidson noted the reporting requirement could be in legislation rather than in the constitution. She said the issue is whether the committee needs to provide some way the reports can legitimately be made in the constitution or whether that function is subject to statute.

Chair Cole observed that, for the last 170 years, the reporting function was in the constitution. He said there is a potential for the possibility that if it is not in the constitution, there will be no statute assigning the reporting duty.

Mr. Asher said if the requirement is in the constitution, it gives it greater standing or sends a message to the public, but, on the other hand, requiring the treasurer to issue a report sounds more like a statutory issue. He said it might be important to have flexibility to change the requirement, which is easier if it is statutory.

Ms. Davidson noted the OPFC is doing some of this task, and the OPFC is subject to statutory change, suggesting that it makes more sense to her to marry those two together, rather than to put one provision in the constitution and the other not.

Chair Cole said one benefit is that the sinking fund provision requires the statewide officeholders to participate. He said there is no reason the General Assembly could not fix that in the statute.

Mr. Azoff noted payment on the debt function is enshrined in the constitution, and is done by the treasurer.

Chair Cole asked what role the OPFC plays. Kurt Kauffman, acting assistant director of the Office of Budget and Management (OBM), who was present in the audience, answered that OBM coordinates with the treasurer's office. He said OBM is the staff for the OPFC, and aligns the debt service payments.

Chair Cole asked Mr. Kauffman if OBM has a view on whether issuance, reporting, and payment functions should be in the constitution. Mr. Kauffman said, on the issuance side, OBM has benefited from the flexibility in the current constitutional approach. He said, on the reporting side, OBM Director Timothy Keen asked that the committee consider whether reporting should be in the constitution, agrees the treasurer is the appropriate entity, and would also support a legislative solution to that. He said, regarding the payment function, the view is that role is not worthy of a constitutional provision but rather is administrative and would be better left to statute.

Chair Cole asked whether all three functions should be in the constitution.

Mr. Azoff said his proposal reflects the treasurer's view that, in terms of priority, it seems the two functions would represent a change from constitutional tradition, and there is no need to make a wholesale change.

Mr. Asher asked how other states approach issuance, reporting, and payment functions, wondering whether they approach it constitutionally. Shari L. O'Neill, counsel to the Commission, noted that research was provided to the committee regarding other states' constitutional provisions relating to the duties of the treasurer. Chair Cole agreed that information would be useful, but asked that it be supplemented by research indicating states that address the treasurer's role by statute, and comparing the constitutional versus the statutory approach. Staff agreed that this research would be provided to the committee at a future meeting.

Chair Cole announced at its next meeting the committee would talk further about Sections 4, 5, and 6, as well as considering the role of the treasurer and whether that should be reflected in a constitutional provision.

Adjournment:

With no further business to come before the committee, the meeting was adjourned at 12:59 p.m.

Approval:

The minutes of the June 9, 2016 meeting of the Finance, Taxation, and Economic Development Committee were approved at the November 10, 2016 meeting of the committee.

/s/ Douglas R. Cole

Douglas R. Cole, Chair

/s/ Karla L. Bell

Karla L. Bell, Vice-chair