



THE HEART OF CUYAHOGA COUNTY

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MEMORANDUM

To: Mayor Gregory P. Kurtz
Members of Council

From: Finance Director Vernon Blaze

Date: Friday, March 24, 2023

Re: Finance Office and Related Topic Updates

House Bill 1 (H.B. 1)

House Bill 1 (H.B. 1) was introduced earlier this year in Columbus. Two of the main provisions of the Bill as introduced are:

- Eliminate most state income tax brackets for nonbusiness income and impose a marginal tax rate of 2.75% on income in excess of \$26,050.
- Reduce the property tax assessment rate on real property in Ohio from the current 35% to 31.5% and then index the assessment rate to inflation in subsequent years.

While on the face of it these two provisions would appear to lower both income and property taxes, opponents of the Bill fear the consequences of the loss of revenue to cities, villages, townships, and school districts across the state.

Some Columbus “insiders” feel that H.B. 1 as it is currently drafted will not garner enough support to pass, but that *“some type of property tax reform and/or income tax cut will be part of this year’s Budget Bill.”*

There sure are a lot of macro forces for local government public administrators to monitor and assess the impact of lately – remote-hybrid work trends impacting income tax receipts, massive interest rate increases and the impact of those increases on banking liquidity, and thusly, the safety of deposits, supply-chain issues, government legislation, etc.

Interest Rates

Speaking of interest rates, the Wall Street Journal recently reported that local governments and school districts that have short-term debt (typically notes with maturities of one-year or less) on their books have had their finances squeezed some because of those significantly higher interest rates.

Good credit-rated municipalities and school districts that were paying as low as 0.21% for a one-year loan in early 2022 are now paying in the 3.16% range here in early 2023 – a 1,400% increase in one year!

On the investing side, these higher interest rates have significantly increased interest income here in 2023. But as noted above, on the borrowing side, these higher interest rates have been difficult for borrowers.

This even applies to consumers too who have credit card balances, home equity loans and/or lines-of-credit. All three of these instruments have interest rates that fluctuate with the Federal Reserve's benchmark "prime rate." So as that rate has gone from under 0.50% to 5.0% in the last 12 months, the interest rates on credit cards, home equity loans and lines-of-credit have also increased materially too.

The City made the conscious decision in 2020 to get away from adjustable-rate debt (one-year notes) and lock in all its debt at long-term fixed rates. The timing of that decision proved excellent, as it turns out that was at/near the time of record low interest rates, and the City was able to lock in just over \$15 million in debt at an all-in interest rate of just under 1.60%.

Pensions

Anyone following what's been happening in France regarding its pension systems has to wonder if that's just the first shoe to drop with pension systems in other countries with advanced economies.

The problem in France is the same problem in many Western countries right now – *"As people live longer and the population grows older, the number of active workers who fund each pension check is shrinking."*

France had four workers for every retiree in the 1960's but was down to just 1.7 active workers for every retiree in 2020. Based on current demographic trends, that 1.7 active workers for every retiree ratio is projected to decline even further – the same demographic trend that exists in many Western countries with advanced economies.

That significant decline in the number of active workers compared to retirees along with overly optimistic actuarial assumptions about future returns on investment portfolios are what caused French President Emmanuel Macron to propose increasing France's retirement age from 62 to 64.

President Macron has taken blistering heat for first proposing this pension system change and then for forcing it through in the face of a tremendous public outcry.

While people in other countries may believe that this does not impact them, here in the United States, the Social Security system faces very similar challenges.

It is largely a “pay-as-you-go” system where “*current workers shoulder the benefits paid to retirees.*” With the above-noted ratio of active workers to retirees declining here in the United States too, Social Security’s costs started to exceed its income in 2021, and projections anticipate that combined reserves will be depleted by 2035 unless changes to the system are made.

Agree or disagree with the proposed change, President Macron has to at least be given credit for bringing attention to this issue before it’s a crisis. **It’s human nature not to embrace change until some kind of crisis occurs. Attempting to deal with a real and major issue before it reaches crisis mode is leadership, and leaders often take arrows in the back for not only being able to see problems around corners before they occur, but for also attempting to ward them off before actually happening and becoming crises.**

President Macron’s one regret over this whole issue? “*That I have not succeeded in convincing the people of the necessity of this reform.*”

Some More Quotes and Lessons from Secretary of Treasury and State George Shultz

From a book titled In The Nation’s Service, The Life and Times of George P. Shultz by Phillip Taubman

- Subsume the ego and stay loyal to the principal. President Lyndon Johnson told Schultz that “*if you have a good idea and its your own idea, it’s not going to go very far. But if it becomes my idea, it just might go somewhere. Do I make myself clear?*”
 - While working as nation’s top diplomat, Shultz would say “*I don’t have a foreign policy. President Reagan has one. My job is to help him formulate it and help him carry it out.*”
- “*Don’t be afraid to show respect when respect is deserved. That adds credibility to your views, including critical ones.*”
- As Secretary of State, Shultz would host a farewell meeting in his office for ambassadors heading abroad. He’d produce a globe, give it a whirl, and ask the diplomat to point to his or her country. Invariably the new ambassador would put his or her finger on where he or she was heading. Shultz’s response: “***Wrong – your country is the United States. Don’t ever forget it.***” Powerful lesson!