

An Analysis of Projected Financial Impacts of a Possible Sylvania Township - City of Sylvania Merger

Executive Summary



January, 2007

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Prepared for Sylvania Community Improvement Corporation (CIC)
January, 2007

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Introduction

This study by the Urban Affairs Center (UAC) at The University of Toledo was commissioned by the Sylvania Community Improvement Corporation (CIC) to examine financial impacts of a possible merger between the City of Sylvania and Sylvania Township. In conducting the study, we have focused on projected changes in revenues and expenditures associated with a merger, in particular, property and income tax collections and costs of local government services; we have also estimated the likely effects of these changes on major community stakeholders: city and township residents, and businesses and workers in the city and township. In limiting our analysis to financial concerns, we do not imply that these are more important than other concerns.

Our research for this study began in July 2006. In preparing this report, we drew upon data from multiple sources, consulted with many public officials and community leaders, and met regularly with members of the CIC to respond to questions and ensure that we were addressing the issues that were important to them.

The first step in our research was to conduct background interviews with officials of the City of Sylvania and Sylvania Township to familiarize ourselves with their perspectives on the important financial concerns raised by a merger. Next, we explored the experience of other Ohio communities, through academic research and telephone interviews, to identify factors associated with positive or negative merger outcomes, and similarities and differences between those communities and Sylvania. Insights from this background investigation guided our examination of the likely effects of a merger on expenditures and revenues; we began by compiling budget information, then conducted interviews with city, township, county and state officials to investigate the effects of a merger on service levels and costs.

Estimation of revenue sources for a merged community proved to be the most difficult part of our research, due to the data limitations outlined below; consequently, we have the most reservations about revenue projections and their impacts on key stakeholders. Despite the cooperation of officials in all the government agencies contacted, we were unable to obtain accurate data on all of the financial elements associated with a merger. An accurate projection of income tax revenues for a merged community requires information on business profits and size of payrolls in Sylvania Township as well as the number of residents who do not currently pay income tax to any municipality. Neither the U.S. Census nor the Ohio Department of Taxation compiles such information, so we were forced to estimate income tax revenues by various indirect means. Similarly, in estimating intergovernmental revenues and shared revenues from the state and county, we believe our estimates are correct unless there are changes in the current formulas for distributing the affected revenues.

Acknowledgements

It would have been impossible to complete this study without the assistance of numerous individuals who shared their knowledge and insights about legal, financial, and other aspects of local government mergers.

From the initial stages of our research to the final draft, the following officials of the City of Sylvania and Sylvania Township contributed time from their pressing duties to provide valuable background information and review of the factual accuracy of the final draft.

Craig Stough, Mayor, City of Sylvania
Barbara Sears, President, Sylvania City Council
John Plock, Finance Director, City of Sylvania
Jeffrey Balmer, Director of Public Service, City of Sylvania
James Moan, Director of Law, City of Sylvania
Judge Scott Ramey, Sylvania Municipal Court
George Eichenauer, Treasurer, City of Sylvania
Carol Contrada, Sylvania Township Trustee
Pamela Hanley, Sylvania Township Trustee
Dave Simko, Sylvania Township Clerk
Hugh Thomas, Sylvania Township Administrator
Gregory Huffman, Public Works Manager, Sylvania Township

Pat Nowak, Executive Director, Sylvania Area Chamber of Commerce, assisted us with estimates of business membership and employment for the City of Sylvania and Sylvania Township. David Gedeon, Transportation Project Manager, Toledo Metropolitan Area Council of Governments, provided detailed data on places of residence of workers in Sylvania Township and the City of Sylvania from the Census Transportation Planning Package that was invaluable in projecting income tax revenues.

The following Lucas County, State of Ohio, and other officials provided information on costs of services, tax structure, and other intergovernmental revenue and expenditure issues:

Keith Early, Lucas County Engineer
Dan Hiskey, Lucas County/City of Toledo administrator
Larry Vesko, Lucas County Health District
Thomas Nichter, Chief Deputy, Lucas County Auditor
Jan Merrit, Appeals Division, Lucas County Auditor
Kevin Helminski and Jim O'Neil, Lucas County Sheriff Department
Cheryl Kizaur, Lucas County Office of Management and Budget
Don Wonnell, Labor Market Analyst, NW Region, Ohio Job and Family Services
Layth I Stefan, Highway Management Administrator, ODOT Region 2
Michael Cochran, Executive Director, Ohio Township Association
John Mahoney, Deputy Director, Ohio Municipal League

Edward Albright, Senior Legislative Assistant, Ohio Municipal League

We also benefited greatly from the insights on the merger experiences of other Ohio communities provided by the following officials:

David Rowlands, City Manager, City of Clayton
Ted Gudorf, former Mayor, City of Clayton
Joyce Deitering, Mayor, City of Clayton
Kenneth Curp, Mayor, City of Riverside
Lois Singleton, Clerk of Council, City of Trotwood
Don Robart, Mayor, City of Cuyahoga Falls
Sheilah H. McAdams, Law Director, City of Maumee
David C. Hazard, Finance Director /Municipal Clerk, City of Maumee

We are grateful to members of the Sylvania Community Improvement Corporation and the Merger Feasibility Study Committee for their invaluable feedback as the report was developed.

Ultimately, however, the responsibility for the analysis in this report, the interpretation of data, and for any errors and omissions rests with the authors.

Executive Summary

This study examines the financial implications of a possible merger between Sylvania City and Sylvania Township. Its purpose is to provide objective information which leaders and residents of these communities can use as the basis of determining whether, and if so how, to proceed with a proposed merger between the two existing jurisdictions. Through the use of available data, we will clarify the costs and benefits to each of the identifiable parties in the city and township.

There are three sections in the study, each of which deals with important questions for a proposed merger and presents the information that is available to answer them. Section I reviews the experiences of other communities which have considered mergers and presents their lessons for this specific situation. Section II examines the financial consequences of a merger to determine the advantages and disadvantages of a merger to each community. Section III examines the effects that a merger would likely have on the different stakeholders in both communities.

Section I

Both professionals and academics have largely ignored analyzing the procedures and results of the merger process in Ohio. The two state associations representing municipalities and townships, The Ohio Municipal League and the Ohio Township Association, provide little guidance to their members about the pros and cons of mergers. The only academic literature we discovered was a graduate paper from Ohio State University (OSU), which was very helpful but only covered the period through 1996. The author did, though, provide a useful summary of reasons communities considered a merger and the issues that developed during the merger process. The first of these are *reasons for considering a merger*:

- The most important reason was to prevent annexation of township lands by a larger community. This does not appear to be a relevant argument for considering merger between Sylvania City and Township, unless it takes the form of preventing piecemeal annexation over a long period or if an actual annexation threat by Toledo occurs.
- The second most common reason reported for considering a merger was economic development, in some cases separate from annexation, and in other cases as an extension of annexation concerns. It allows two separate political entities to combine their resources to more effectively compete with other communities rather than with each other.
- The third important reason was to protect the funding and tax basis for the school system, which does not appear to be relevant for this case, since they already have a combined system. Other reasons cited, though, might be relevant, including managing growth in the area, funding services with the income tax, and the unity of being one community.

The second aspect of proposed mergers covered in the OSU graduate paper was the issues that developed during the merger process, particularly the political, legal, financial, and operational impacts of a merger.

- The form of government that the merged community would take is an obvious issue.
- The kind and level of services to be provided and the means of financing these are a second issue.
- The loss of identity as a rural township is another issue which is not likely to be significant if this merger process continues
- Job security and employee benefits in turn is likely to be an issue which would complicate the merger process between Sylvania City and Township, particularly since the latter has more employees than other townships which have been involved in merger attempts.
- Educating the public so that voters have objective information about both the positive and negative consequences of the proposed merger is important for refuting misinformation distributed through anonymous rumors.

Our review of other mergers or merger attempts confirmed the importance of these issues, and suggested specific lessons for the Sylvania Township-City of Sylvania case:

- Because the township and city already have high levels of service and both already finance two of the most expensive services—police and fire protection—it is possible to more accurately estimate expenditure needs of a merged community.
- The most expensive remaining service is the road servicing provided by the County Engineer and ODOT.
- Because Sylvania Township has a large number of public employees, their job security could become a driving issue in a merger attempt.
- In contrast to a number of merger attempts, Sylvania City and Township are both urban and have a long history of close cooperation.
- It is important that the merger process be open and transparent so that false rumors and distrust do not gain credibility.
- Similarly, proponents of a merger should be cautious about overselling the advantages of a merger, particularly in presenting an unjustifiably optimistic financial scenario.

Section II

Section II examines the financial consequences of a merger in order to determine the financial advantages and disadvantages of a merger to each community. We utilized budgeted revenues and expenditures for 2006 and actual revenues and expenditures and other financial data for 2005. The revenue and expenditure estimates are based on the following assumptions:

- Alterations in the life style and service level of each community would be as minimal as permitted by state law and local conditions, such as public health and safety.
- The merged community would assume the financing instruments of the current city and reduce as much as is financially feasible the property taxes currently collected by the township.
- The merged community would shoulder the costs of township services previously borne by Lucas County and the State of Ohio.

We emphasize that these assumptions are not intended to be interpreted as recommendations but rather as a basis or a starting point for discussions and decisions by the actual stakeholders in a merger decision. Using these assumptions, we first examine probable expenditure changes in a merged community and then review the revenue changes that will be needed to cover these expenditures.

A. Expenditure Analysis.

Public sector finance utilizes funds, which limit designated receipts to specific disbursement activities. Not all funds used by the city and township correspond. Because the merged community would be a municipality, we have used the City's classification, and have noted the sources of revenue that would replace "township-only" funds.

- The most significant changes in expenditures resulting from a merger between the City of Sylvania and Sylvania Township are in the areas of street construction maintenance and repair, engineering services, capital improvements, courts and corrections, refuse collection, income tax administration, and pension funds.
- Should the city and township merge, the newly formed city would take over the following additional **street construction, maintenance and repair (SCM&R)** and related public works responsibilities: 1) current county engineer responsibility for maintenance of county roads (including signals and other related matters), ditches, and engineering services in the township; 2) current ODOT responsibility for maintenance of the portions of US 23, Central Avenue, Monroe Street, Reynolds Road and Alexis Road that are currently within the township boundaries. The Lucas County Engineer estimates the operating, maintenance, and capital costs for the County responsibilities that would be transferred to a merged community at **\$2,832,000**, including engineering, maintenance, and capital costs. The estimated cost of maintaining the portions of US 23, Central Avenue, Monroe Street, Reynolds Road and Alexis Road that are currently within the township boundaries is **\$565,000**.
- The Lucas County Engineer estimates that additional **capital improvement expenditures** for township areas are **\$1,718,000** (included in the previous total). We estimate additional capital improvement expenditures for township areas currently maintained by ODOT at **\$334,000**.
- Expenditures for **courts and corrections** could involve a significant financial commitment that is difficult to predict. In a merged community, the city would likely assume responsibilities for the costs of prisoners now covered by Lucas

County. The current additional cost to the merged community is estimated at **\$400,000**.

- The City of Sylvania provides a three-container limit **garbage and refuse pick up** for its citizens. The fees charged for this service are paid into the general fund and do not cover the expenditures, so the deficit would increase by approximately **\$300,000** in the event of a merger.
- The **income tax division** will likely be required to double its personnel in order to process the increased demand if the income tax is extended to current township residents and employers. We estimate additional expenditures at **\$320,000**.
- The costs of **engineering services** will increase as the merged community assumes responsibility for those services provided by the Lucas County Engineer to Sylvania Township and by the Ohio Department of Transportation (ODOT) for the state highway system located within the Township. The County Engineer estimates current expenditures for this service at **\$441,000**, and we estimate the ODOT costs at **\$86,000**. These amounts are included in the previous totals.
- In the case of a merger, the new community would continue to fund fire and police pensions at least at current levels, with additional costs of approximately **\$90,000** to bring Township contributions up the state mandated level for municipalities. However, these would be financed by earmarked property taxes.

Our analysis indicated that minimal changes would occur in other areas of expenditure:

- In the **general fund** the aggregate for the following areas will remain relatively unchanged if the communities merge:
 - City expenditures for **parks and forestry** and **swimming pools and concessions** would initially remain relatively unchanged, but could increase if facilities were developed in the current township and if additional personnel were hired to provide new services. Aggregate expenditures for **zoning** also could increase if additional personnel are needed for this function.
 - Expenditures for **police services** in a merged community can be expected to remain close to the aggregate of these two totals. We assume that the township budgeted police pension expenditures would be covered by special property taxes rather than transferred from the general fund, reducing police expenditures from the general fund by this amount.
 - The cost of **fire services** for both communities is known, since they are provided by a joint fire district. Again, we assume that the budgeted pension expenditures would be covered by special property taxes rather than from the general fund.
 - Expenditures for **street cleaning** are financed from the general fund in the city and from the streets department budget in the township. We assume that in a merged community, these expenditures would also be financed by the general fund.

- **Special assessments** are charges imposed on real property to help pay for a local improvement that benefits the property. The City of Sylvania currently maintains three special assessment funds: for street lighting, tree maintenance, and ditches and drains. Sylvania Township only has a street lighting fund. The **street lighting funds** for the city and the township are financed by a front foot assessment of property. Since this study assumes minimum changes of existing practices in case of a merger, and these funds are self-supporting, they are not included in our calculations.
 - The **tree maintenance fund** of the city is financed almost entirely by an assessment of \$.30 per front foot of property. If applied in a merged community, this assessment is estimated to generate approximately **\$434,000** annually in additional revenue. It is the consensus of the City Public Service Director and the Township Public Works Manager that the amount raised by extending the special assessment will be sufficient, if barely, to cover the additional costs for tree maintenance in the merged city.
 - The **ditches & drains fund** of the city has two sources of financing: another \$.30 front foot assessment and transfers from the Sewer Fund. Ditches and drains in the Township are currently the responsibility of both the County Engineer and the Township Road Department. Since these units do not distinguish ditches and drain expenditures from other responsibilities, the current costs of these services cannot be calculated. Revenues from extending this assessment throughout a merged community might not be sufficient to adequately cover this service.

Summary of Expenditures. We estimate that in the case of a merger, total expenditures in all funds will be greater than the current combined expenditures of these funds in the existing city and township: the general fund by \$514,000, SCM&R by \$800,000, special assessments by \$868,000, capital improvements by \$2,052,000, and employer contributions to the police pension fund by \$90,000.

B. Revenue Analysis

- For the City, most of the **general fund** is financed by the 1.5% income tax and a 3 mill property tax. The Township general fund has more diverse revenue sources, the largest of which is a .5 mill property tax currently levied in both the city and township, as well as various intergovernmental sources. The major revenue change that can be anticipated in the case of a merger would be the increase in income tax revenue as it is applied to businesses, employees, and residents of the township.

Assuming the 1.5% **income tax** of Sylvania City would be applied to a merged community, we estimate that the result would yield an additional \$12 million in revenue, for approximately \$20,000,000 as currently budgeted. Revenue would be greater if the merged community taxed at a higher rate or allowed only partial

credit for income taxes paid to other jurisdictions. It would be lower if the rate were to be reduced.

- Increased revenue from the income tax will likely permit the elimination of the 7.40 mill **property tax** which currently funds the fire district for the city and the township. This increased revenue also can likely replace the 9.70 mill property tax which finances the township police department. In addition, both the township and the city levy a property tax paid into their respective general funds. The township tax of .50 mills, which also applies to the city, could be eliminated. It would still be necessary to retain all or part of city's 3.0 mill property tax and extended it to the current township; general fund revenues would increase by an estimated \$2.7 million if the 3 mill tax were applied to township property.
- As indicated above, we assume that the city would continue its three-container limit **garbage and refuse pick up** and extend it into the current township. The revenues from the fees charged are projected to increase from \$345,000 to \$805,000, with a deficit increase of from \$219,355 to \$510,000.
- Both jurisdictions currently receive revenue from Lucas County's local **government fund and local government assistance fund**, and the current total would not likely increase, at least in the immediate future.
- In addition, the **Sylvania Municipal Court** would retain the amounts now paid to the Sylvania Township Trustees and the \$35,000 paid to the Lucas County Law Library.
- The **street construction, maintenance, and repair (SCM&R)** functions in both communities are financed by state shared revenue of the gasoline tax and vehicle registrations, as well as permissive license taxes that each assesses on vehicles registered in their respective communities. In addition, the township levies a 2.30 mill property tax earmarked for streets, and the city transfers some funding from the general fund to support SCM&R. The following changes can be anticipated in case of a merger.
 - **Shared Revenues** from the **gasoline tax** and **vehicle license fee** are calculated with complex formulas based on vehicle registration, and the formula differs between municipalities and townships. The formula favors municipalities, so the revenues from these two sources can be expected to exceed the current total of that of the two jurisdictions. Also, each jurisdiction assesses an additional **permissive tax** on vehicles registered, \$10 by the city and \$5 by the township; we assume that the \$10 tax would be applied throughout the merged community. We project that increased revenues from these sources in a merged community to be approximately \$1.4 million.
 - The township levies a 2.30 mill **property tax** earmarked for roads. If it is reduced to 2.0 mills and extended to property throughout the merged

community, it would generate an estimated \$2.7 million in revenue, sufficient to cover added SCM&R obligations.

- Increases in the **capital improvements fund** are dependent on the increase in income tax revenues in a merged community. By state law the first ¼% (of the 1.5 percent income tax) or 1/6 of the income tax revenues, must be earmarked for capital improvements. If income tax revenues increased by \$12 million, this would amount to an increase of \$2 million.
- A significant change for both jurisdictions, in case of a merger, would be in financing police and fire pensions. Municipalities in Ohio are required to assess a .30 mill property tax each earmarked for fire and police **pension trust funds**. However, state mandated pension benefits exceed the yield from this tax, and municipalities can cover the deficit either from additional taxes or transfers from the general fund. Sylvania City assesses an .80 mill property tax in addition to the .30 mill tax for its police pension fund, for a total of 1.10 mills, which covers the police pension expenditures. Since fire services are provided by the township, the city does not collect the .30 mill tax for fire pensions. Sylvania Township finances its police and fire pension expenditures from its police and fire levies.

In the event of a merger, we estimate that the yield from applying the .30 mill for police and fire pensions as well as the .80 additional voted millage in the merged community should produce sufficient revenue to cover the pension fund requirements of the combined police and fire departments.

Section III

In Section III, we summarize the financial impacts of a possible merger and examine their likely effects on the various stakeholders in the two communities. The changes with the greatest potential impact are:

- Extension of city services into the former township
- Financing of services for a merged community
- Share of the tax burden borne by current township and city residents and businesses

The major stakeholder groups affected by these changes are city and township residents, businesses and their employees in the city and the township, and elected officials and employees of the city and township.

Extending Municipal Services

Since Sylvania Township already provides most of the expensive urban services to its residents, a merger would bring only a few new services and small changes in the level of some current services. Administrative costs for a merged community, however, would exceed the current total administrative expenditures, largely because the new city would likely assume responsibility for services currently financed by Lucas County and

ODOT. The estimated cost of these additional service responsibilities totals \$5.2 million.

Financing existing and new services

In the event of a merger, we assume that the existing methods of financing City of Sylvania services would replace Township financing instruments. Current Township residents would be affected by the following:

- The 1.5% municipal income tax
- The city's \$111 per year garbage and refuse collection fee
- The \$.30 front foot special assessments each for tree maintenance and ditches and drains
- An additional \$5 vehicle registration tax
- City property taxes extended to the current township
- Elimination of all but one township property tax

For current city residents, the following changes in property tax rates would apply:

- Elimination of the current township property taxes
- An additional property tax earmarked for the road and bridge fund and an additional .30 mill property tax for the fire pension fund.

A merger would shift financing of city services from a reliance on property taxes to a predominant reliance on the income tax. This shift would transfer costs of city services from property owners, primarily residents, to employed persons, primarily non-residents, and decrease reliance on a static financing source. We estimate that this change would reduce property tax rates to current city residents by 5.60 mills and to current township residents by 13.50 mills. For a residence valued at \$200,000, this would represent an annual savings of \$227 in the current city and \$491 in the current township, including special assessments. Current residents and businesses of the city would save over \$700,000 in property taxes, and current residents and businesses of the township would save over \$8 million in reduced property taxes.

While a merger would result in reduced property tax payments for all property owners in both the current city and the township, the addition of an income tax would only affect the current township residents employed in the current township or in another jurisdiction not levying an income tax. Income taxes would not increase for current city residents, current township residents employed in Sylvania City or in another jurisdiction levying an income tax, or retired persons.

The persons most affected by extending the city income tax to the current township would be non-residents. Almost 80% of employed persons in the township do not live in either the township or the city. We estimate that of the additional \$12 million anticipated increase in income tax revenue from the current township, only approximately \$5 million would be paid by current township residents. Subtracting this income tax increase from

estimated property tax reductions results in a net tax reduction of \$3 million in tax payments for current township residents.

Property Taxes versus Income Taxes

In Ohio, income taxes as a revenue source have a major advantage over property taxes. Income taxes are more elastic, since revenues generally increase as incomes increase. Ohio property tax revenues, however, do not automatically increase in response to increased property values because of what is known as the reduction factor. Population growth and residential development in Sylvania Township have consistently added new taxable property over the past decades, making it possible to support higher levels of services than is typical for townships in Ohio. However, this rapid growth will likely end in approximately five years as the Township will have developed most of its usable land area by then. Without the addition of new property to tax rolls, property tax revenues are unlikely to keep pace with increases in the cost of township services.

Financial Impacts on Businesses

The two changes in the tax structure resulting from a merger that would have the greatest impact on businesses in the township are:

- Reduction of property taxes by a nominal rate of 13.50 mills and an effective rate of 9.4 mills (after applying the reduction factor).
- Addition of a city income tax of 1.5% on some profits of businesses in the current township.

Without detailed information on the types and sizes of businesses in Sylvania Township, it is not possible to estimate the impacts of a merger and the extension of an income tax on the location choices of these businesses.

Effect on Current City and Township Employees

A proposed merger between the Sylvania City and Township is not likely to require a reduction in the current total city and township workforce and therefore would not result in significant personnel savings. The increased size of the community and the expansion of some services would likely require retaining existing personnel and hiring additional personnel in some areas.

The affected city and township employees include four important groups: administrative personnel, fire department employees, police department employees, and public works employees.

Administrative Personnel

Administrative personnel for both jurisdictions would need to be retained because of their specialized knowledge of each jurisdiction. Some expanded administrative responsibilities will require hiring new personnel, particularly in the income tax division.

Fire Department Employees

Since the Fire District currently covers both jurisdictions and responsibilities would not change, its personnel needs would not be affected by a merger.

Police Department Employees

The number of police personnel in both departments is consistent with national standards for officer/population ratios. The two issues which would likely be most problematic are deciding bargaining unit representation and equalizing the slight difference in salaries and benefits between the two departments.

Public Works Employees

Estimating wage differentials for Road Department workers in the Township and Public Service employees in the City is more difficult because job titles are not comparable.

Elected Officials

In the merger cases we reviewed, current and previous elected officials from both jurisdictions were among the most intense supporters and opponents of a proposed merger. Assuring elected officials that a merger would not end their public service careers helps make motives more transparent, plus provides continuity in leadership during a period of significant change in both communities.