ANNUAL REPORT
OF THE
COMMISSION ON
STATE TAX AND FINANCING POLICY

Indiana Legislative Services Agency
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Indianapolis, Indiana 46204-2789

November 2006

INDIANA LEGISLATIVE COUNCIL
2006

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Commission on State Tax and Financing Policy

Membership Roster

November 2006

A copy of this report is available on the Internet. Reports, minutes, and notices are organized by committee. This report and other documents for this Commission can be accessed from the General Assembly Homepage at http://www.in.gov/legislative/.

FINAL REPORT

Commission on State Tax and Financing Policy

I. STATUTORY AND LEGISLATIVE COUNCIL DIRECTIVES

The Commission on State Tax and Financing Policy is established under IC 2-5-3. Specifically, IC 2-5-3-5 directs the Commission to study and investigate the following:

(1) the present state, county, and city tax structure of the state of Indiana;

(2) its revenue-producing characteristics and effects upon the economy of the state of Indiana;

(3) its equalities and fairness;

(4) the enforcement policies and administrative practices related to that tax structure; and

(5) the costs of collection in relationship to the burden of the tax.

IC 2-5-3-5 also authorizes the Commission to examine overall administrative matters, fiscal matters, and procedural problems of the various departments of the state, county, and city governments as they relate to tax and financing policy.

In addition, IC 2-5-3-5 authorizes the Legislative Council to refer by resolution any tax or financing problems and correlated matters to the Commission for study and research. Under Legislative Council Resolution 06-01 (as adopted June 13, 2006), the Legislative Council assigned the following additional topics to the Commission:

(1) Study eligibility requirements for certain military benefits. (SR 46-2006)

(2) Expanding eligibility for the property tax deduction for low-income senior citizens by removing AV criteria. (SR 49-2006)

(3) Child welfare system and funding. (Rep. Espich)

(4) Issues pertaining to public transportation and commerce. (SCR 67-2006)

II. INTRODUCTION AND REASONS FOR STUDY

The reasons for the study of the issues considered by the Commission include the following:

Military Benefits

Senator Mike Delph, Senator Thomas Wyss, and Senator Luke Kenley introduced SR 46-2006 requesting a study of eligibility of certain military benefits. Specifically, the resolution requested a study of the following topics:

(1) the 0% disability threshold for statutory fee remission for educational benefits;
and

(2) eligibility of the active component of the armed forces for grants from the Military Family Relief Fund.

Current statute, IC 20-12-19-1(b)(3), provides for tuition and fee assistance at public colleges and universities for children of disabled or deceased Indiana military veterans. Tuition and fee assistance under this provision is applicable to children of veterans with a disability rating ranging from 0% to 100%. In accordance with the 2006-2007 biennial budget bill (P. L. 246-2005), new applicants who were the children of veterans with a 0% disability rating were not accepted to the program during the 2005-2006 academic year. This restriction was eliminated by P. L. 58-2006.

The Military Family Relief Fund was also established by P. L. 58-2006 to provide need-based financial assistance to reservists and National Guard members experiencing hardship as a result of mobilizations. Assistance from the Fund is, however, not available to active duty personnel in the Armed Forces.

Property Tax Deduction for Low-Income Senior Citizens

Senator Richard Young introduced SR 49-2006 requesting a study of the issue of eliminating the assessed value (AV) limitation for the property tax deduction for the residence of a low-income individual who is at least 65 years of age.

2% Property Tax Cap

Pursuant to its authority under IC 2-5-3-5 to study the present state, county, and city tax structure in Indiana, the Commission conducted a hearing relating to the expected impact of the 2% property tax cap enacted during the 2006 legislative session in P. L. 162-2006. The Commission also requested that LSA provide an estimate of the potential fiscal impact of the 2% cap. The cap provides that certain taxpayers receive a credit against their property tax bill if the net tax due exceeds 2% of the gross assessed value (AV).

Child Welfare System and Funding

At the request of Representative Jeffrey Espich, the Legislative Council directed the Commission to study the issue of the current child welfare system in Indiana and the current funding scheme for this system.

Public Transportation and Commerce

Senator Robert Meeks introduced SCR 67-2006 requesting a study of issues pertaining to public transportation and commerce.

III. SUMMARY OF WORK PROGRAM

The Commission met three times in Indianapolis. At the first meeting on August 29, 2006, the Commission received presentations from the State Student Assistance Commission of Indiana and the Indiana Department of Veterans' Affairs regarding eligibility for the college tuition and fee assistance for children of veterans with a 0% disability rating. The Commission also received a presentation from the Indiana Department of Veterans' Affairs about the structure and purpose of the Military Family Relief Fund established by legislation during the 2006 legislative session.

At the second meeting on September 26, 2006, the Commission heard testimony on three topics. The Commission received a presentation from the Legislative Services Agency as to the potential fiscal impact of changing the income and assessed value limits on the property tax deduction for low-income senior citizens. The Commission received a presentation from the Legislative Services Agency as to the potential fiscal impact of the 2% property tax cap enacted during the 2006 legislative session. The Commission also heard testimony from local public officials and other interested parties regarding the fiscal impact. The Commission received a presentation from the Department of Child Services of information as to the structure and financing of the current child welfare system in Indiana. The Commission also heard testimony from interested parties on this topic.

At the third meeting on October 23, 2006, the Commission received presentations from leaders of national and state public transportation organization and public transportation systems in Indiana. The presentations highlighted the current state of public transportation systems and funding nationally and in Indiana. Presentations also focused on the economic rationale for public transportation and the economic benefits of public transportation systems and funding.

The Commission adopted its final report at the October 23, 2006, meeting by a majority of the members appointed to serve as voting members on the Commission.

IV. SUMMARY OF TESTIMONY

The Commission heard testimony from 24 witnesses. The Commission received testimony on the following topics.

Military Benefits

Current statute, IC 20-12-19-1(b)(3), provides for tuition and fee assistance at public colleges and universities for children of disabled or deceased Indiana military veterans. Tuition and fee assistance under this provision is applicable to children of veterans with a disability rating ranging from 0% to 100%. While the Indiana Department of Veterans' Affairs determines eligibility for the tuition and fee assistance program, funding for the program is administered by the State Student Assistance Commission of Indiana (SSACI).

The 2006-2007 biennial budget bill (P. L. 246-2005) limited eligibility for tuition and fee assistance to children of disabled veterans beginning in 2005-2006 academic year. The legislation provided that the Department of Veterans' Affairs only consider new applications for the tuition and fee assistance program to children of disabled veterans having a disability rating exceeding 0%. However, while the legislation prohibited approval of new 0% disability-related applications, it did allow payment of tuition and fee assistance for students already in the assistance program who were children of 0%-rated veterans. Thus, existing participants who were children of 0% disabled veterans were allowed to remain in the program. The anticipated savings from eliminating all participation by children of 0% disabled veterans (existing and new recipients) was estimated at about $1.5 M annually. As a result, funding to SSACI for the statutory fee remission programs was reduced to account for expected program savings. However, since existing recipients were allowed to continue to receive assistance, resultant funding for the biennium has been inadequate.

The eligibility issue was resolved by P. L. 58-2006, which essentially restored tuition and fee assistance to new applicants who are children of 0% disabled veterans beginning with the 2006-2007 academic year. However, the legislation did not restore funding for these recipients that was eliminated by P. L. 246-2005.

The Military Family Relief Fund also was established by P. L. 58-2006. The Fund was established to provide assistance with food, housing, utilities, medical services, basic transportation, and other essential family support expenses that have become difficult to afford for families of members of a reserve component of the armed forces or the National Guard and who were called to active duty after September 11, 2001. The Director of the Department of Veterans' Affairs is to administer the Fund, which consists of the following: (a) appropriations made by the General Assembly, (b) donations, (c) interest, (d) money transferred to the Fund from other funds, (e) annual supplemental fees collected from the Hoosier Veteran and Support Our Troops license plates, and (f) money from any other source. Money in the Fund currently cannot be used to provide financial assistance to full-time active duty members of the Armed Forces.

Property Tax Deduction for Low Income Senior Citizens

Under current statute (IC 6-1.1-12-9), a homeowner is entitled to a deduction of $12,480 (up to one-half of AV) against the home's gross AV if: (1) the homeowner is at least 65 years of age; (2) the home is owner-occupied; (3) the home's AV does not exceed $144,000; and (4) the homeowner's income does not exceed $25,000.

The fiscal impact of the following changes was provided to the Commission:

(1) Eliminating the AV cap could potentially result in additional deductions totaling $68 M statewide, which could result in a statewide property tax shift of about $834,000 in 2008.

(2) Eliminating the income cap could potentially result in additional deductions totaling $1,401 M statewide, which could result in a statewide property tax shift of about $21.1 M in 2008.

(3) Eliminating both the AV cap and the income cap could potentially result in additional deductions totaling $1,667 M statewide, which could result in a statewide property tax shift of about $24.5 M in 2008.

2% Property Tax Cap

P. L. 162-2006 provided that certain taxpayers will receive a credit against their property tax bill if the net tax due exceeds 2% of the gross AV. The credit effectively limits a taxpayer's net tax bill to 2% of the value of the taxpayer's property. In 2007, the credit applies only in Lake County. All residential property owners in Lake County will receive the credit unless the Lake County Council adopts an ordinance by December 31, 2006, limiting the credit to homesteads only. In 2008 and 2009, the credit will be effective in all counties and will apply to all forms of residential property (homesteads, apartments, and other residential rental property). Beginning in 2010, the credit will apply to all real and personal property in all counties.

The credits directly reduce property tax revenue flowing to the affected taxing units, and taxing units are prohibited from increasing their tax levies or issuing debt to compensate for the revenue loss. Credits could potentially total an estimated $19 M to $31 M in 2007 when the 2% cap applies only in Lake County. Credits could potentially total $58 M in 2008 and 2009, once the 2% cap is effective statewide for all residential property. This could potentially increase to $459 M in 2010 when the 2% cap applies statewide to all real and personal property.

Child Welfare System and Funding

The child welfare system in Indiana is administered by the state through the Department of Child Services (DCS). Decisions as to treatment and care of children entering the system are made by juvenile judges at the county level. In addition, the cost of treatment and care of these children is assumed by the counties through county property tax levies. Counties levy property taxes for county welfare funds and debt service funds. However, the county welfare personnel are state employees.

Children who receive treatment and care enter the child welfare system upon determination that they are delinquent or a "child in need of services" (CHINS). If the county juvenile judge determines a child is delinquent or CHINS, the child becomes a ward of the court. The county juvenile judges are elected locally and are responsible for deciding the appropriate treatment for children determined to be delinquent or CHINS. The juvenile judge relies on the recommendations of child caseworkers or probation officers when making the treatment determination for the delinquent or CHINS child.

There are two fiscal issues that surround the child welfare system. The first relates to the funding burden and growth in cost being incurred by counties to support the child welfare system. It is argued that the child welfare system is an unfunded mandate where counties pay for services ordered by the state. It is also argued that the state does not have a financial incentive to determine whether the cost of treatment ordered by a juvenile judge is excessive or if less expensive and effective treatment is available. As a result, this has exacerbated the continuing growth in child welfare levies. According to DCS, child welfare expenditures statewide increased by an annual average of about 5.8% from FY 2003 to FY 2005. The average increase in statewide child welfare expenditures totaled about $379.2 M in FY 2004, an increase of about 7.8% over FY 2003. Expenditures increased to about $421.4 M in FY 2005, up about 11.1% over FY 2004. Moreover, certified child welfare budgets increased by about 14.4% for FY 2006, with an increase of almost 5% for FY 2007. Projections by DCS suggest that child welfare budgets could potentially increase by an average of about 6.6% annually from FY 2007 to FY 2012.

A second issue with the current child welfare system involves county and regional variation in service provision. Since funding and treatment decision making occurs at the county levels, there could potentially be substantial inequity in treatment depending upon where a child resides. County and regional treatment differences are highlighted by case length statistics reported by DCS. DCS divides the state into 18 regions with the regional average length of treatment in days ranging from a low of about 411 days in Region 9 (comprising Boone, Hendricks, Montgomery, Morgan, and Putnam Counties) to a high of about 771 days in Region 3 (comprising Elkhart, Kosciusko, Marshall, and St. Joseph Counties). In comparison, the statewide average length of treatment is about 615 days. Within region differences also can be significant. Treatment length in Region 3 ranges from about 529 days in Kosciusko County to about 885 in Elkhart County. Meanwhile, the variation is somewhat lower in Region 9, ranging from about 342 days in Hendricks County to about 498 days in Morgan County.

Public Transportation and Commerce

The Commission conducted a hearing to obtain information regarding the status of public mass transportation in Indiana and current state funding for public mass transit purposes. The hearing also facilitated presentations and discussion of system expansions, new mass transit systems, and new operating schemes that could potentially arise in the future. Currently, there are 79 public mass transit systems in Indiana, with 43 county systems, 18 rural city systems, and 18 urban systems. There are also 14 counties in which mass transit feasibility studies are currently being conducted. Typically, funding to defray capital and operating expenses of these systems comes from a mix of fares paid by riders and funds from local, state, and federal government sources. Economic impact studies suggest that mass transit systems potentially provide a number of local and regional economic benefits, including relief of traffic congestion leading to improvements in commute times for individuals and increased mobility of individuals with limited or no access to automobiles. The studies also suggest that mass transit systems may generate significant benefits by facilitating development or redevelopment of areas. As for potential benefits to business, reductions in congestion could potentially reduce transit times for business shipping and service delivery, translating into reductions in production costs and increased productivity.

Currently, the state provides funding for public mass transit through three funds: the Public Mass Transportation Fund (PMTF), the Commuter Rail Service Fund (CRSF), and the Electric Rail Service Fund (ERSF). The largest of the funds is the PMTF, which receives a distribution of 0.635% of state Sales and Use Tax revenue. Revenue in the PMTF is distributed for the purpose of promoting and developing public mass transportation in Indiana. About $34.1 M in Sales Tax revenue was distributed to the PMTF in FY 2006, an increase of 6.6% over the FY 2005 distribution. The distribution to the PMTF has increased by an average of 4.2% annually since FY 1996. However, it's reported that since 1996, the number of transit systems receiving money from the PMTF has almost doubled, increasing from 32 to 59. The money in the CRSF and the ERSF is distributed to the Northwest Indiana Commuter Transportation District (NICTD), which operates the South Shore interurban line between South Bend and Chicago. The CRSF receives revenue from the state Sales and Use Tax (0.14% annually) and from the state property tax on railroad car companies. The distributions to the CRSF totaled almost $11.7 M in FY 2006, a 13.3% increase from FY 2005. Sales and Use Tax distributions to the CRSF have increased by about 3.0% annually since FY 2000 (the first year of this distribution). The annual distributions to the CRSF have increased by an average 9.3% annually since FY 1996. The ERSF receives revenue from the state property tax on railroad companies. The distribution in FY 2006 totaled only about $110,000. This distribution has actually declined by an average of about 0.9% per year since FY 1996.

V. COMMITTEE FINDINGS AND RECOMMENDATIONS

The Commission made no findings or recommendations.

W I T N E S S L I S T

Christine Altman
Hamilton County Commissioner
Chairwoman of the Central Indiana Regional Transportation Authority

Thomas Applegate, Director
Indiana Department of Veterans' Affairs

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Jacque Clements, Auditor
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Steve Luecke, Mayor
City of South Bend

Husain Mahmoud, Controller
City of Gary

Jim Merton
City Securities Corporation

Judge Marilyn Moores
Marion Superior Court

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Dennis Obergfell, Deputy Director
State Student Assistance Commission of Indiana

Judge James Payne, Director
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