Indiana Fiscal Policy Institute Session Report No. 1:

Shifting sales tax on gasoline without new revenue leaves less for roads and nothing for education, other programs

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As the Indiana General Assembly continues its deliberations on providing additional funding for transportation maintenance and new construction, a plan offered by the Americans for Prosperity proposes (1) redirecting the sales tax on gasoline from the State's General Fund; (2) utilizing the estimated $1 billion in new revenue projected in the December revenue forecast to be available to the state from growth on existing taxes for road funding and replacing the redirected sales tax; (3) freezing the remainder of the budget at existing levels; and (4) no tax increases.[1] The proposal raises a difficult question: What are the implications of "freezing" the state budget and what new revenues would actually be available to meet transportation needs?

The short answer is not enough; here are the reasons why. Projections for the annual amount of money necessary to meet the 20-year road-funding plans range from $900 million a year to $1.2 billion. In the scenario proposed by Americans for Prosperity about $600 million would be available for the roads plan over the course of the next two-year budget. If the General Assembly followed the proposal, according to our analysis, lawmakers would not be able to increase appropriations for education – both K-12 and higher education, the opioid crisis or any other spending, except for increases in Medicaid and teacher's retirement. The analysis in this article is based on Gov. Eric Holcomb's proposed budget. The House Republican's version is expected to be release in the next few days. We will use the governor's budget in this analysis and update it with that of the House Republicans when it is released.

Two of the primary components of the state budget – the match for Federal Medicaid funding and the payment of Teacher Retirement obligations are cost centers for which the budget-makers have little control. Therefore, the FY 2018 and FY 2019 allocations will be used for our purposes. Otherwise, all other components of the general fund operating budget will be frozen at the FY 2017 level. The governor's budget projects increased Medicaid state spending of slightly more than $2 billion in FY 2018 and slightly more than $2.3 billion in FY 2019. It also anticipates higher payments for teacher retirement obligations. The additional amounts would be $866 million in FY 2018 increasing to $892 million in FY 2019.[2]

The FY 2017 general fund operating budget for FY 2017 is $15.6 billion.[3] Adding in the proposed increases for Medicaid and the Teacher's Retirement obligations, the "mostly frozen" FY 2018 budget would be $15.44 billion and the FY 2019 "mostly frozen" budget would be $15.92 billion. Based on the December, 2016 state Revenue Forecast[4], there should be $15.48 billion in revenue available to support the FY 2018 budget and $16.09 billion available to support the FY 2019 budget.

The next thing to consider is the effect of moving the sales tax revenue from gasoline out of the General Fund. The effect of shifting the sales tax revenue from the General

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[1] Testimony in Opposition to Gas Tax Hike provided by Justin Stevens, Americans for Prosperity – Indiana to the joint meeting of the House Roads and Transportation and Ways and Means Committee on January 25, 2017

[2] Fiscal Impact Statement for HB 1001 (2017) prepared January 10, 2017

[3] Fiscal Impact Statement for HEA 1001(2015) prepared on May 6, 2015

[4] State Revenue Forecast – Total General Fund Revenue Forecast, December 15, 2016

Fund means an estimated reduction of $305 million in FY 2018 and $299 million in FY 2019.[5] If those revenues are redirected to dedicated highway functions as proposed, the revenues available to support the FY 2018 and FY 2019 budgets become $15.18 billion and $15.78 billion respectively. The net result then is a projected budget deficit of $267 million in FY 2018 and of $129 million in FY 2019.

The budget freezing proposal outlined above appears to provide $305 million of new dedicated transportation funding for FY 2018 and $299 million for FY 2019. Moving the sales tax on gasoline from the General Fund, however, creates a gap in funding. To fill the gap, it will be necessary to find an additional $267 million in FY 2018 budget cuts and $129 million in cuts to the FY 2019 budget. To accomplish this, the Governor's FY 2018 budget will require cuts in the amount of approximately $270 million to the FY 2018 proposed budget and approximately $760 million to the FY 2019 proposed budget.

House Bill 1002, as passed by the Committee on Ways and Means, calls for the redirection of the above sales tax revenue for use on transportation projects. It also includes new revenues from an increase in the gasoline tax and other transportation-related taxes and fees. The new taxes and fees are expected to generate $521 million in FY 2018 and $568 million in FY 2019.[6] Coupled with the redirected sales tax revenue the total for transportation is about $826 million in FY 2018 and $867 million in FY 2019. The amounts available under the budget freezing proposal set forth above are substantially less at an estimated $305 million in FY 2018 and $299 million in FY 2019. Given these circumstances, the General Assembly would only be able to fund two necessary increases—Medicaid and Teacher's Retirements—and a reduced version of the roads proposal. Of course, lawmakers could draw money from the state's reserves to cover these shortfalls. That would, however, represent an unbalanced budget in the eyes of many and certainly could not be sustained over subsequent years. It simply does not represent sound fiscal management.

It appears that the "mostly frozen" budget option as outlined above would necessitate some modest cuts to the Governor's proposed FY 2018 budget and more substantial cuts to the proposed FY 2019 budget. It would leave no revenue available to continue to build the state surplus. And it would provide only modest new revenues for state, and perhaps local, road funding but nothing on the magnitude that has been discussed in recent months.

[5] Fiscal Impact Statement for HB 1002 (2017) prepared on February 9, 2017

[6] Fiscal Impact Statement for HB 1002 (2017) prepared on February 9, 2017

About the Author

John Stafford is the interim director of the Community Research Institute at Indiana-Purdue University Fort Wayne. He has served in various positions in local government in Elkhart and Allen counties. He received the Ivan Brinegar Municipal Management Award in 1999 given by the Indiana Association of Cities and Towns. Stafford has authored several papers and reports for the Indiana Fiscal Policy Institute.

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The Indiana Fiscal Policy Institute (IFPI), formed in 1987, is a private, non-profit government research organization. The IFPI's mission is to enhance the effectiveness and accountability of state and local government through the education of public sector, business and labor leaders on significant fiscal policy questions, and the consequences of state and local decisions. The IFPI makes a significant contribution to the important, on-going debate over the appropriate role of government. The IFPI does not lobby and does not support or oppose candidates for public office. Instead it relies on objective research evidence as the basis for assessing sound state fiscal policy.

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