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SB 1 – Local Government Finance

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Executive Summary

- SB 1 provides significant new property tax relief for homeowners by phasing up the homestead deduction to 2/3 of homestead AV and providing a new tax credit for up to $300 or 10% of their final tax bill, whichever is less.
    - This change represents the bulk of the fiscal impact to local units and will limit property tax revenue growth significantly over the coming years, especially in communities that are heavily residential.
- The bill also raises the BPPT exemption to $2M and eliminates the 30% depreciation floor on all new equipment.
- This change will reduce revenue on BPPT significantly but does leave the majority of the tax intact, a significant improvement over the complete elimination of BPPT that passed out of the House Ways & Means Committee but then scaled back significantly on 2nd reading. The bill gives the opportunity to offset some revenue losses by restructuring LIT, raising the expenditure rate cap from 2.5% to 2.9% and allowing cities and towns to adopt their own LIT rate.
    - The bill does shift some local tax burden from property tax to income tax as a matter of policy which will require difficult votes and local decisions in the coming years.
- The bill places significant limits on some of the drivers of significant property tax increases in recent years, specifically by limiting short-term

debt issuances, capping Fire Territory rates at 0.4%, and moving all referenda to general election years where they pass less frequently.
  - The debt caps and fire territory caps will have significant impacts on certain communities throughout the state that are currently relying on them, however the majority of the debt limitations will limit school tax rates and may have positive circuit breaker impacts on cities and towns.
- The bill also eliminates excess levy growth appeals for fast growing units.
  - This is the only escape valve that fast-growing communities have to right-size their levies with their growing service costs. These communities will now have to rely on LIT changes to manage their growth.
- **SB 1 represents a significant negative fiscal impact on local government,** however, given how conversations started this session it is a manageable reform package that includes revenue replacement options. The fact that the proposal improved so much over the course of the session is a testament to the continued engagement from Aim's membership.

Business Personal Property Tax

<u>Summary</u>

- Increases the de minimis BPPT exemption over several years (currently set at $80,000) to $2 Million in 2026.
- After January 1, 2025, exempts new business personal property from the 30% depreciation floor
- Protects TIF bonds by requiring that all BPP placed into effect in existing allocation areas as of January 1, 2025, will still be subject to the 30% floor for the life of the TIF area

<u>Comments</u>

- The new BPPT exemption is very large and will have a fiscal impact, but this exemption number came from the tax study conducted by the Indiana Chamber of commerce that indicated **with an exemption of around $2M approximately 90% of payers would be exempt while keeping around 85% of the assessed value.**

- Removing the 30% floor will have a significant fiscal impact especially for those communities that are heavily industrial. However, it only applies to new property so it will be slowly phased in over time.
- Ensuring economic development bonds are protected will support many of the new investments in Indiana in new battery manufacturing, data centers, and any other large industrial project coming online in Indiana communities.
- This proposal, although not optimal, was a significant improvement over the proposed complete phaseout of the BPPT.

Local Income Taxes (LIT)

<u>Summary</u>

- Raises the county-wide expenditure rate cap to 2.9% starting in 2027
    - 1.2% of the rate is reserved for county services
    - 0.4% of the rate is reserved for fire protection and EMS services
    - 0.2% of the rate is reserved for nonmunicipal taxing units (like conservancy districts, solid waste management districts, libraries etc.)
    - 1.2% of the rate is reserved for general revenue for municipalities under 3,500 in population (distributed by population)
    - Allows municipalities over 3,500 in population to adopt a LIT rate up to 1.2% for general purpose revenue.
- Eliminates the current property tax relief credit (PTRC) rate, which currently uses LIT to fund property tax deductions for residential property in both the 1% and 2% category and replaces it with a maximum of 0.3% for property tax relief.
- Provides a process for non-municipal units and towns under 3,500 to petition the county for LIT distribution and requires the county to distribute LIT revenue to all requesting municipalities pro-rated based on population. The county is not required to adopt a municipal rate.

<u>Comments</u>

- Aim supports a framework that allows municipalities to adopt their own LIT rate. This framework will need to be refined to be workable.
- More work may need to be done on the specifics of how the rates are broken up to ensure equitable revenue sharing.

- Eliminating PTRC will put a significant amount of assessed value back on the property tax rolls to counteract the AV cuts elsewhere in the bill, but it will vary significantly by county as each county has a very different PTRC rate.
- The money from the PTRC rate is currently going to local governments, so it will need to be replaced by the new LIT rates, which will mitigate negative numbers seen in the fiscal impact analysis.
- More work will need to be done to ensure the process functions to guarantee that municipalities under 3,500 will be able to receive a LIT rate from the county.

Property Tax Deductions

Summary

- Phases down the standard homestead deduction (currently $48,000 or 60%, whichever is less):
  - $40,000 in 2026
  - $30,000 in 2027
  - $20,000 in 2028
  - $10,000 in 2029
  - Eliminated in 2030
- Phases up the supplemental homestead deduction (currently 35%)
  - 40% in 2026
  - 46% in 2027
  - 52% in 2028
  - 57% in 2029
  - 62% in 2030
  - 66.7% in 2031 and every year thereafter
- Adds a new property tax deduction for all property in the 2% property tax bucket (agriculture land and non-homestead residential property):
  - 6% in 2026
  - 12% in 2027
  - 19% in 2028
  - 25% in 2029
  - 30% in 2030 and 2031
  - 33% in 2032 and every year thereafter
- Adds a new property tax credit of $150 for all homeowners aged 65 or over.
- Adds a new property tax credit of $125 for disabled homeowners.

- Raises the homestead property tax credit from 7.5% or $200 to 10% or $300
- Raises the agricultural base rate capitalization rate by 1 point.
- Provides for a new property tax deferral program that can be voluntarily adopted by counties.

Comments

- These new credits and deductions are clearly added to blunt the increase in assessed value for the 1% and 2% taxpayers from the repeal of PTRC.
- In most counties, these new deductions will be a significant net loss in assessed value and an increase in the property tax rates.
- This revenue loss would have to be offset by increased LIT rates, but more analysis needs to be done before we know which communities have the LIT base to do so.

TIF Neutralization

Summary

- Allows DLGF to neutralize significant increment increases for TIFs resulting from large rate increases stemming from the AV cuts in this bill.
- Allows DLGF to adjust TIF rates to guarantee bonds that could be impaired by AV cuts in the bill, particularly with personal property.

Comments

- Considering how these changes would affect TIFs is a good policy goal.
- This language may be necessary for certain TIFs that are reliant on apartment buildings as new deductions for apartments may otherwise reduce TIF revenue.

Referendum

Summary

- Moves local referenda to even numbered years in line with the general election.
- Changes the referendum language to specify both the proposed rate and the proposed amount of money to be raised for a specific purpose.
- A school cannot place a controlled project referendum on the ballot the year a current referendum is expiring.

Comments

- Moving the referenda to the general election means that there is only one opportunity to pass a referendum every two years. This could create problems timing capital referenda for controlled projects as the current referendum timelines already sometimes create project delays.

Debt and Excess Levy Appeals

Summary

- Eliminates the excess levy 3-year growth appeals.
- Provides a 1-year cooling off period for all short-term debt issuances under 5 years after they expire.
- Provides that all municipal property tax debt-backed projects are controlled projects if the total debt service rate for the unit exceeds:
  - 0.25% for the remonstrance process
  - 0.4% for the referendum process
- Continues the 4% MLGQ cap in 2026.

Comments

- Excess levy growth appeals are the only mechanism fast-growing communities have to attempt to right-size their property tax levies with their growing service costs.
- Eliminating this tool means that fast-growing communities will only be able to rely on income tax increases to track growing service costs. More conversation with lawmakers on the importance of these appeals will be necessary.
- The new controlled projects debt service rate threshold is relatively low and will capture more municipalities than under current law.
- Limiting the rate impacts of debt from overlapping units, especially school corporations that issue the majority of general obligation debt in the state, may have positive revenue impacts by lowering rates and reducing circuit breaker loss.

Budget Procedures

Summary

- Requires that public notice for the budget hearing must include the proposed increase in the tax rates and tax levies in proposed budgets.

- Requires an additional public hearing prior to the budget adoption wherein the only item on the agenda must be the amount the tax rate and tax levy are increasing from the prior year.

Comments

- The local budget process already requires the local unit to have public hearings and adopt a new tax levy and tax rate publicly each year.
- This procedure adds an additional public hearing onto the process wherein just the change in rate from the prior year is discussed, which will make the process excessively bureaucratic.

Fire Territories

Summary

- Caps Fire Territory tax rates at 0.4%
- Requires the county to approve all fire territory LIT distributions

Comments

- Fire territories are an important tool for consolidation and increasing professional fire and EMS coverage.
- Many fire territories have rates over 0.4% currently and those rates are set based on how much DLGF determines the territory needs to operate when they are formed. Arbitrarily capping this reduces the effectiveness of the fire territory.

Transparency

Summary

- Directs DLGF to maintain a property tax transparency portal through which they can compare property tax liability versus proposed property tax liability and provide feedback on the proposed rates.

Comments

- Adding new features to the public Gateway website and making it more user-friendly and transparent is a good thing.