Testimony to the State and Local Tax Review Task Force
January 10, 2024

Thank you Chairman Holdman and members of the Task Force for the opportunity for the public to testify on this issue that affects all Hoosiers.

My name is Andrew Bradley, and I am Policy Director for Prosperity Indiana, the statewide association for community economic development, the non-profit, public, and private organizations and individuals who work every day to strengthen Indiana's communities and build economic opportunity for Hoosiers.

I am also here today as Board President of the Indiana Coalition for Human Services, a nonpartisan coalition of advocacy and human service organizations that engages, educates and mobilizes decision-makers, its stakeholders and the public on fact-based, equitable public policies resulting in quality outcomes for all Hoosiers.

Those organizations are part of a group of partners who co-released a new report released on January 9 that will be very pertinent to this committee's work. But before discussing that new data, I want to briefly set the stage with how Indiana's tax structure impacts Hoosiers' take-home pay.

New data released by the Bureau of Economic Analysis in December show that, even including regional price parities that account for cost of living, Hoosiers' incomes have consistently run behind the U.S. average and the average of Midwest states. Indiana's real per capita personal income in 2022 was $54,811, compared to the $64,468 Midwest average. So, even accounting for cost of living, Hoosiers are able to buy less per year — by almost $10,000 — compared to the typical Midwesterner.

For the Hoosiers that Prosperity Indiana members serve, that deficit compared to our neighbors means over10 months of fair market rent for a 2-bedroom apartment (at $988 month). This contributes to Indiana's housing affordability shortage and creates a backlog in homeownership, contributing to disparities in intergenerational wealth growth. These are problems that reveal themselves in Indiana's high rates of evictions and overreliance on predatory lending that Prosperity Indiana members face every day.

But what does this have to do with Indiana's tax structure, you might ask?

Some eschew comparisons in wages, even when accounting for cost of living, looking instead at the disposable personal income, that is, individuals' and households' take-home pay *after taxes*, as a more reliable indicator of economic thriving.

But here again, Indiana is consistently and increasingly trending behind not only the U.S. average but that of the Midwest, when it comes to per capita disposable personal income, according to the most recent data of this indicator from the Bureau of Economic Analysis. So while in 2000 Hoosiers' after-tax incomes were $1,044 behind the average Midwesterner's, by 2022 that gap had grown to $2,394, a 229% increase since the turn of the century.

And despite Indiana's changes to its state and local tax system over the past two decades, Hoosiers' buying power and after-tax incomes remain far behind most states nationwide and here in the Midwest. These disparities create some of the pressures that Hoosiers have to make due with, and that community economic development and human services organizations here in Indiana have to grapple with, in ways that they don't in most neighboring states.

This leads to the new report co-released by national tax experts and four Indiana organizations that can shed light on how this Task Force can act to remedy these disparities and the effects they have on Hoosiers' lives.

The seventh edition of the 'Who Pays?' report was released yesterday nationally by the Institute for Taxation and Economic Policy, whose staff testified to this Task Force in October.

The Indiana report of 'Who Pays?' was co-released with ITEP and Prosperity Indiana, the Indiana Coalition for Human Services, the Indiana Assets & Opportunities Network, and the Indiana Community Action Poverty Institute.

These state partners are all statewide networks share a similar vision of an Indiana where all Hoosiers have equitable access to economic and social opportunity and work every day to empower Hoosiers striving to reach their full potential. All state partners have also included improving the equity of Indiana's tax system in their 2024 policy agendas.

This new edition of 'Who Pays?' provides updates to the information that ITEP presented to this Task Force last October. The report is unique in that it is the only distributional analysis of tax systems in all 50 states and D.C. 'Who Pays?' provides analysis of how state and local tax policies affect taxpayers at all levels of the income spectrum, and how features of those systems work to widen or close racial and economic disparities.

The Indiana report also offers recommendations that align with the experience of state partners and their priorities for 2024. Many findings from the new edition of 'Who Pays?' confirm that Indiana's tax system shares some of the same characteristics and challenges as other states. This includes that:

- Most states require low- and middle-income families to pay higher effective tax rates than the wealthy
- States (like Indiana) described as "low tax" are often high tax for low- and middle-income families.
- Heavy reliance on sales and excise taxes makes tax systems more regressive.

- Heavy tax cuts deprive state coffers of adequate revenue for schools, health care, and colleges – programs and services that build opportunity and improve well-being for families and communities.

I was particularly struck by the finding from 'Who Pays?' that income disparities for Hoosiers are actually larger *after* state and local taxes are collected than before. This, in part is because the lowest-income 20% of Hoosier taxpayers face a state and local tax rate that is 115% higher than the top 1% of households. Indeed Indiana is one of 42 states that tax the top 1% less than every other income group, and one of 35 states that tax their poorest residents at a higher rate than any other group. This adds up to Indiana having one of the most regressive state & local tax systems in the U.S. and among the very highest tax burdens on the lowest income households in the Midwest.

'Who Pays?' finds that Indiana has the 14th most regressive tax system in the nation. (3rd most regressive in Midwest, above only Illinois and South Dakota. And in fact, Indiana also has the 5th-highest effective tax rate paid by the lowest 20% of earners at 13.3%. In the Midwest, only Illinois requires its poorest residents to pay a larger percentage of their incomes in state and local taxes.

In fact, low- and middle-income Hoosiers bear the highest state & local tax burdens

Here you see illustrated Indiana's policy that the lowest-income 20% of Hoosier taxpayers must pay a state and local tax rate that is 115% higher than the top 1% of households, who face the lightest tax burden as a percentage of income in the state.

Several components of Indiana's tax system result in the state's disproportionately high burden on low- and middle-income Hoosiers. Here you can see that in both sales & excise and property taxes, the lowest fifth of Hoosier earners pay the highest tax rates, while the top 1% pay the smallest share of all in the state.

Prosperity Indiana members and our partners in the human services sector work every day with Hoosiers living paycheck to paycheck, and for whom the heavier burden of these sales, excise, and property taxes means that they are closer to a small emergency, like a flat tire, meaning they must choose between getting to work or paying the rent. In this way, what may seem like small tax policies add to larger income gaps and economic consequences.

This is why the big picture of Indiana's disproportionate state and local tax burden on low- and middle-Hoosiers, and the way we compare with other state tax systems, is so important to the kinds of economic opportunity that Indiana offers to those Hoosiers. And it also points to ways Indiana can build on successes for the future.

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‘Who Pays?’ identifies a couple of positive features in Indiana’s tax system that help keep Indiana above 13 other states regarding regressivity. In addition to a state sales tax base that excludes groceries, a key feature that Indiana has that some states do not is a refundable state Earned Income Tax Credit.

Indiana’s state EITC is a critical resource for Hoosiers to reach financial stability, encouraging work by providing a wage subsidy in the form of a tax credit, and has provided millions of dollars to hardworking individuals and families. Just this past session, the General Assembly strengthened Indiana’s EITC by recoupling the state credit back to the federal credit, providing additional relief to married couples, foster parents, parents of three or more children, and families with income disparities.

However, Indiana could make our state EITC even more effective by increasing the state percentage of the federal credit. A bill to increase that percentage from the current 10% to 12% was considered but did not pass last session.

‘Who Pays?’ also identifies several regressive features that place a high tax burden on low- and middle-income Hoosiers, and that contribute to Indiana’s ranking of 14th most regressive in the U.S. and 3rd-most regressive in the Midwest. These include:

- No property tax ‘circuit breaker’ credit for low-income taxpayers
- Does not use combined reporting as part of our corporate income tax
- The comparatively low state EITC as previously mentioned
- Does not levy a tax on estates or inheritances
- Comparatively low-income tax exemptions
- The fact that personal income tax uses a flat rate
- And, critically, no Child Tax Credit, a tool that has been proven to slash child poverty and increase economic opportunity for children and families

Regarding Indiana’s recent and ongoing flat tax cuts, the ‘Lookahead’ feature of the new ‘Who Pays?’ report shows that by 2027, the cuts will have little effect on inequality, and thus will not improve the regressivity of Indiana’s tax system or burden on low- and moderate-income Hoosiers. These flat percentage cuts, which provide a much higher dollar benefit to a relatively small number of the wealthiest Hoosiers, will not improve the income disparities Indiana faces compared to our Midwestern neighbors.

The ‘Lookahead’ feature in the new ‘Who Pays?’ report also show that eliminating Indiana’s state income tax would actually exacerbate the existing inequality in Indiana's tax structure. Doing so would mean the lowest-income 20% of Hoosier taxpayers would face a state and local tax rate that is 213% higher than the top 1% of households. Eliminating Indiana’s state income tax would result in Indiana dropping from the 14th most regressive state tax system in the nation to the 9th most regressive.

The 'Lookahead' feature of the 'Who Pays?' report aligns with testimony that ITEP provided to this Task Force last October, finding that some proposals would actually *increase* the taxes on the lowest income Hoosiers who already bear the state's greatest tax burden.

For example, replacing half of the state personal income tax with a 9.5% sales tax rate would result in a nearly $30,000 tax cut to households in the top 1% of income earners, who have an average annual income of $1.5 million.

However, Hoosiers in the bottom 20% of the income spectrum, which the new 'Who Pays?' report confirms already face a state and local tax rate that is 115% higher than the top 1% of households, would see a $62 tax *increase* under this scenario – a difference of $29,569 between the two ends of the income spectrum.

With this new data in mind, we have three broad recommendations to guide the Tax Task Force's work for the following year:

First, do no harm. It's clear that eliminating the personal income tax, or partly replacing it with a sales tax hike, will only put more burden on the Hoosiers who already pay the largest portion of their incomes on taxes. The Task Force should cross that off the list of possibilities, along with any recommendations to restrict state or local revenue and force cuts to critical services that would put average working Hoosiers further behind our Midwest peers.

Next, we would like to offer opportunities for this Task Force to consult those who work closest with the Hoosiers left out of the national recovery. I know that the partners who co-released this new report are ready and eager to provide examples of how the state's current upside-down tax system stifles economic opportunity for the Hoosiers and communities they serve, and what proposals would have the most positive impact.

Finally, this Task Force and the General Assembly can act together to address regressive tax features ID'd in 'Who Pays?' (i.e. Indiana's lack of a Child Tax Credit and property tax circuit breaker) and re-imagine how Indiana's tax and budget structure can work together to unlock the potential of all Hoosiers by fully funding needed services, such as affordable housing, universal child care, and tuition-free technical education, all possible for less than the loss of revenue from lopsided tax cuts.

Let's not miss this opportunity to protect and expand Indiana's revenue base and invest in needed shared public commitments. This is Indiana's chance to regain true competitiveness in the Midwest and the U.S. for state prosperity, built on thriving Hoosiers. Thank you.

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