

June 2003

As required by Indiana Code 4-12-1-12, the State Budget Agency hereby transmits to Governor Frank O'Bannon, Auditor of State Connie Nass and each member of the Indiana General Assembly:

- A list of appropriations made during the 2003 Regular Session of the Indiana General Assembly, and
- A report on how these appropriations will affect the fiscal status and affairs of the State.

Revenues:

The U.S. economy entered a recession in March, 2001. As a result, General Fund and Property Tax Replacement Fund revenues declined by 1.0% in FY 2001 and 3.8% in FY 2002 – the first back-to-back declines in recorded history. General Fund and Property Tax Replacement Fund revenues were forecasted to increase by 13.4% in FY 2003, by 8.3% in FY 2004, and by 4.7% in FY 2005. Removing the revenue increase measures enacted as part of HEA 1001-2002(ss) reveals that April, 2003 revenue forecast is for a slow recovery in state revenues. Without these revenue measures, the forecast would have been for General Fund and Property Tax Replacement Fund revenues to increase by 1.3% in FY 2003, by 3.1% in FY 2004, and by 4.5% in FY 2005.

Expenditures:

Permanent reductions from the Deficit Management Plan implemented in March, 2002 have continued for most areas included in this budget. Payment delays for the public schools, higher education, and local governments, totaling \$702.1 million continue with passage of HEA 1001-2003.

Education

Funding for elementary and secondary education comprises the largest component of Indiana's state budget. The General Assembly appropriated \$3.66 billion in FY 2004 (an increase of 3.5% over the FY 2003 appropriation in P.L. 291-2001) and \$3.70 billion in FY 2005 (an increase of 1.1% over the FY 2004 appropriation) for tuition support. There were four notable changes made to the school formula: (1) The at-risk grant was eliminated and the at-risk index was disaggregated and separate dollar amounts were assigned to each component of the index within the formula, (2) a new ISTEP remediation grant was added to the tuition support categorical grants, (3) school corporations were given authority to pay expenditures for utilities and property insurance out of their capital projects funds and to increase their local capital projects fund levy to cover those costs, (4) the state appropriated \$30M in FY 2004 and \$30M in FY 2005 to the Teachers Retirement Fund (TRF) to reduce the payments necessary from school corporations for the cost of the employer contributions to the Post 1996 Teachers' Retirement Fund. School corporations operate on a calendar year accounting system, so all these increases translate into a 3.3% increase in total state and local formula support,

including the capital projects funds spending authority and TRF contributions, for calendar year 2004 and a 2.9% increase for calendar year 2005.

Higher Education

Total state appropriations for higher education increased \$29.5 million (2.0%) for FY 2004 over the appropriations in P.L. 291-2001, and an additional \$7.9 million (0.5%) for FY 2005. The budget includes \$11.3 million in FY 2004 and \$19.6 million in FY 2005 for quality improvement programs for each of the seven state colleges and universities designed to promote economic development throughout the state. In addition to the appropriations above, the General Assembly approved \$275 million in bonding authority for capital projects for the state's colleges and universities. If all of these projects are approved during the 2004-2005 biennium, with fee replacement starting in FY 2006, the fee replacement appropriation necessary for FY 2006 would increase by 33% over FY 2005.

Economic Development

State appropriations for economic development programs totaled \$98.9 million for FY 2004 and \$97.9 million for FY 2005. Of these annual totals \$3.2 million was appropriated to the Office of the Commissioner of Agriculture, \$85.5 million to the Department of Commerce, \$5.2 million to the Governor's Council on Community Service, and \$3.9 million for the Department of Workforce Development. The Department of Commerce received an additional appropriation of \$1.0 million for FY 2004 to be used to publicize corporate tax restructuring. An additional \$42.2 million in economic development related leases have been transferred from the operating budget to the capital budget.

The budget also includes Energize Indiana, a bipartisan job-creation plan. The job-creation plan, if funded for 10 years, will help create 200,000 high-wage, high-skill jobs in four high-tech business sectors - the life sciences, advanced manufacturing, information technology and high-tech distribution. It also authorizes university construction projects, immediately creating high-wage construction jobs and ultimately providing much-needed space for research and other purposes. In addition to several tax and revenue provisions, the budget includes several appropriations related to Energize Indiana including: 21st Century Research & Technology, Value Added Research, Rural Development, Technology Development Grants, infrastructure upgrades and development for the Gary/Chicago Airport, and the I-Light Fiber Optic System.

Health and Human Services

State appropriations for health and human services totaled \$2.06 billion for FY 2004 and \$2.05 billion for FY 2005, with the Family and Social Services Administration (FSSA) receiving nearly 98% of these funds. Health and human services state appropriations will decrease by \$21.7M from FY 2003 to FY 2004 and \$30.2M from FY 2003 to FY 2005, reflecting the permanent cuts from the Deficit Management Plan.

The Medicaid program received appropriations of \$1.27 billion for FY 2004 and \$1.27 billion for FY 2005. Medicaid appropriations include the Office of Medicaid Policy and

Planning Administration, Medicaid Administration, Medicaid-Current Obligations, and Medicaid Disability Exams. General Fund appropriations for Medicaid increased by \$17.6 million (1.4%) for FY 2004 over the 2003 appropriation level of \$1.25 billion and an additional \$17.6 million (1.4%) in FY 2005. The appropriation increases occurred in the Medicaid Administration and Office of Medicaid Policy and Planning Administration line items. The Medicaid-Current Obligations appropriation was not increased from its FY 2003 funding level. The Children's Health Insurance Program (CHIP) received an appropriation from the Tobacco Master Settlement Agreement Fund of \$23.8 million for FY 2004 and \$26.2 million for FY 2005.

State Appropriations for the disabled, aged, children, and mentally ill were effectively maintained from FY 2003 to FY 2004 with minimal or no decreases. \$211.6 million was appropriated to Developmentally Disabled Client Services for the 2004-2005 biennium. Of this, \$42.6 million was appropriated from the Tobacco Master Settlement Fund with the remaining \$169.0 million from the general fund. This reflects an \$8.98 million (4.1%) decrease in appropriation from the 2002-2003 biennium.

The General Fund appropriations for the Indiana State Department of Health (ISDH), Special Institutions, and Veterans' Affairs total \$51.3 million in FY 2004 and \$51.5 million in FY 2005. The General Assembly shifted several ISDH appropriations from the General Fund to the Tobacco Master Settlement Agreement Fund, totaling \$32.6 million in FY 2004 and FY 2005. This represents a shift of 50% of the ISDH budget from the General Fund to the Tobacco Master Settlement Agreement Fund. As in the 2002-2003 biennium, the ISDH budget includes appropriations from the Tobacco Master Settlement Agreement Fund for Local Health Maintenance, Community Health Centers, and the Local Health Department Account.

Additional appropriations from the Tobacco Master Settlement Agreement Fund include \$8 million in FY 2004 and FY 2005 for the Indiana Prescription Drug Program, known as "Hoosier Rx," and \$10.8 million in FY 2004 and FY 2005 for the Tobacco Use Prevention and Cessation Board.

General Government

The budget includes funding to provide the required state match for the federal funds appropriated to Indiana for the implementation of the Help America Vote Act of 2002 (HAVA). These funds will be used to replace voting systems, and improve voting registration and procedures.

The General Assembly added the new model Interstate Compact for Adult Offender Supervision to Indiana's statute. The budget appropriates \$65,707 in FY 2004 and \$53,158 in FY 2005 to the Indiana Judicial Center which will be responsible for offenders on probation and other administrative functions related to operating the compact in Indiana.

General Fund appropriations include \$89.0 million for the biennium for the Personal Services/Fringe Benefits Contingency Fund.

Public Safety

The 2004-2005 biennium budget appropriates approximately \$1.2 billion for the operation of the state correctional system. These funds will provide for the incarceration of approximately 23,000 adult and juvenile offenders and participation in Community Corrections, including Forensic Diversion and Faith Based Programs. There was no increase in Department of Correction appropriations for a projected increase in offender population in either institutional care or for community corrections.

The budget also appropriates a total of \$274.5 million for the operations of the State Police, including increased funding for laboratory services, in the 2004-2005 biennium. The budget provides \$3 million for capital expenditures.

To better serve the public, the \$0.50 Technology fee applied to certain license branch transactions was made permanent. This fee allows the Bureau of Motor Vehicles to maintain and upgrade its information technology needs including all license branches throughout the state.

Conservation and Environment

The budget includes \$568.8 million for the operation of conservation and environmental programs in the 2004-2005 biennium. This is an increase of approximately 5% over the last biennium, and includes additional funds for the opening of Prophetstown State Park.

The budget includes language to authorize a phase in of new Federal Safe Drinking Water Act fees. These annual fees, which begin July, 2004, support public water system operations for the Department of Environmental Management.

Transportation

The 2004-2005 biennium budget includes \$3.8 billion in general, dedicated and federal funding for Indiana transportation needs. This is a 4.8% increase over the previous biennium. Appropriations for the Indiana Department of Transportation's highway construction program in the 2004-2005 budget total \$1.9 billion for a 10.4% increase from the previous biennium. This increase is due to a 2 cent per gallon gas tax increase, which went into effect January 1, 2003 and provides both an increased ability to bond construction projects and also additional revenue for overall program needs. An additional 1 cent per gallon gas tax increase was dedicated to local units of government and is expected to annually generate \$33 million for local roads and streets.

Capital and Construction

The capital budget for the 2004-2005 biennium represents a strong commitment to the preservation of basic infrastructure. This includes \$39.4 million for preventive maintenance, \$154.7 million for repair and rehabilitation projects, \$238.0 million for lease payments, and \$25.6 million for university projects.

While the appropriation for agency preventive maintenance increased slightly over the 2002-2003 biennium, the appropriation for agency repair and rehabilitation decreased by

about 12%. Lease payment appropriations increased by almost 9% as a result of the increase in the number of facilities requiring bond payments. Appropriations for repair and rehabilitation at universities were decreased by almost 64% from the previous biennium. Overall, capital appropriations were decreased by 10% in the 2004-2005 biennium from the 2002-2003 biennium.

The capital budget provides funding for preventive maintenance, which was flat lined at the FY 2002-2003 appropriation level for most state facilities. It includes full funding for lease rentals for bonded facilities. Funding for repair and rehabilitation projects was either held at the FY 2002-2003 levels or reduced.

The Department of Correction capital budget includes funding for Local Area Network Infrastructure, roof replacement at the Indiana State Prison, rehabilitation of maximum security systems at the Putnamville Correctional Facility, cottage renovations at the Plainfield Juvenile Correctional Facility, roof replacement at the Westville Correctional Facility, and construction of program space at the Wabash Valley Correctional Facility.

The capital budget for the Department of Natural Resources includes funding for drinking water and wastewater projects at state parks, continued development at Prophetstown, Charlestown, and Fort Harrison state parks, inn expansion projects, and Lake Shafer Dredging.

Funding is also included in the capital budget for the Little Calumet River Basin Development Commission to match federal funds, INDOT airport development federal matching funds, Gary/Chicago Airport infrastructure upgrades, Family and Social Services Administration's master plan for regional facilities, the Indiana-Purdue Fort Wayne – Northeast Indiana Innovation Center, and the State Health and Safety Contingency Fund.

Outside Acts

The General Assembly enacted several measures that will impact General Fund and Property Tax Replacement Fund revenues over the biennium. Updating the State's income tax laws to conform to federal law will reduce revenues by \$26 million in FY 2003 and increase revenues by \$7.8 million in FY 2004 and by \$16.7 million in FY 2005. Amending the State's sales tax laws to conform to the requirements of the Streamlined Sales Tax Project will reduce revenues by \$3.0 million in FY 2003, \$5.9 million in FY 2004, and \$8.8 million in FY 2005. Legislation clarifying the State's Prison Investment Tax Credit will reduce revenues by \$40,000 in FY 2004.

In addition, the General Assembly appropriated \$17.2 million in the Outside Bill Contingency appropriation to fund enrolled acts with a General Fund impact. A complete listing of the revenue and expenditure acts with a General Fund or a Property Tax Replacement Fund fiscal impact is located in section E of this document.

Reserve Balances

The Budget Agency estimates that the General Fund balance will be slightly less than \$34 million at the beginning of the biennium and grow to \$64.3 million at the end of the biennium. The combined balances, including the tuition reserve account, the Medicaid reserve account, and the Rainy Day Fund are estimated at \$543.4 million at the beginning of the biennium and \$360.7 million at the end of the biennium. In order to maintain this minimal reserve balance, \$380 million of Pension Stabilization funds will be used early to pay current teacher retirement benefits, \$136.9 million of dedicated funds will be transferred to the state General Fund, \$54 million of delinquent county juvenile payments are assumed to be collected, and an additional \$165 million will be transferred from the lottery and gaming revenues to the state General Fund.

In addition to dedicated fund transfers and new revenue, the minimal reserve balances were maintained by appropriating less than forecasted expenditures for Medicaid and not funding the forecasted population increases of the Department of Correction. The Medicaid shortfall is expected to be manageable due to the increases in the federal match rates contained in the federal Jobs and Growth Tax Relief Reconciliation Act of 2003 and, if necessary, additional cost containment savings. A solution to the Department of Correction's funding shortfall is less clear; however, the Department and the State Budget Agency are committed to using community corrections and other alternative sentencing programs to reduce the population growth that is currently forecasted.

A Combined Statement of Net Actual and Estimated Unappropriated Reserve (a Reserve Statement) follows this cover letter. This Reserve Statement is intended to reflect the reserve based on the facts known at the time of the budget's enrollment. Consequently, changes in revenue estimates (i.e. the recently passed federal relief act) are not reflected.

Respectfully submitted,

Marilyn F. Schultz
State Budget Director