

Starting Session with a \$1.5 Billion “Surprise”, Indiana Dips Below 10% Reserve for First Time Since Pandemic

The Indiana General Assembly returns on January 8, 2024, for a “Short Session”. Historically these sessions do not include the development of a traditional state budget, but are often fiscal issues still arise. This year, there are a few complications, laid bare in last month’s [revenue forecast presentation](#) to the State Budget Committee, that fiscal leaders will likely discuss. These include an unexpected overspend of \$1 billion in Medicaid spread over state Fiscal Years (FYs) 23-25 and a revised revenue forecast that reduced anticipated revenue collection by \$500 million – these two factors combined to drain quite a bit of Indiana’s state reserves.

How many reserves were impacted? According to the State Budget Agency, Indiana will have an estimated \$2.3 billion in surplus for FY 2024[1], which equates to roughly 10.7% of yearly expenditures, and \$2.1 billion in surplus estimated FY 2025, or 9.4% of yearly expenditures. In comparison, during July 2023, these balances were expected to be closer to \$2.9 billion, which would be more than 13% of expenditures.

As a reminder, many fiscal leaders believe that an [appropriate amount of reserves](#) is somewhere between 10% and 15% of a state’s expected revenues. The 9.4% figure is the lowest since the pandemic.

Indiana’s Economy and Changing Demographics

The state’s [economy is still solid](#), despite continued concerns over inflation, global turmoil, and a consistently tight labor market. The housing market is calming, and the Hoosier auto manufacturing sector remains strong.

Lost in the economic update last month was an acknowledgement of general demographic trends in Indiana. IFPI and the Indiana Business Research Center partnered in Summer 2023 to outline demographic trends in Indiana. The big picture is that Indiana is graying, which will have a direct impact on services for the growing elderly population.

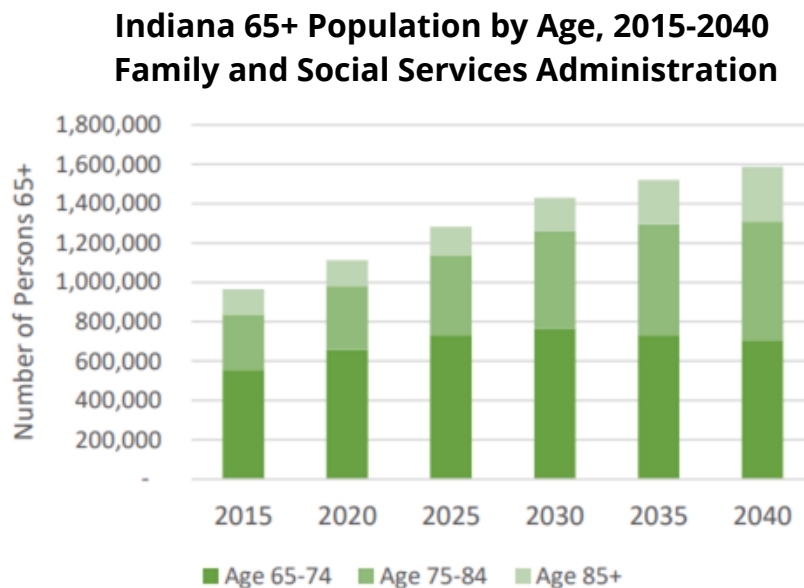
Like the rest of the nation, Indiana is experiencing a significant population change due to the aging of the Baby Boomer generation. By the year 2025, this entire generation will be 60 and over, with the largest population growth occurring in those 85 and older. [By 2025, in total nearly 19% of all Hoosiers will be age 65 or older.](#)

[1] FY 2023 = July 1, 2022 – June 1, 2023. FY 2024 = July 1, 2023 – June 1, 2024. FY 2025 = July 1, 2024 – June 1, 2025. For this purpose, “surplus” means the actual General Fund surplus plus all other sources and uses of cash reserves.

Continued Growth in Medicaid

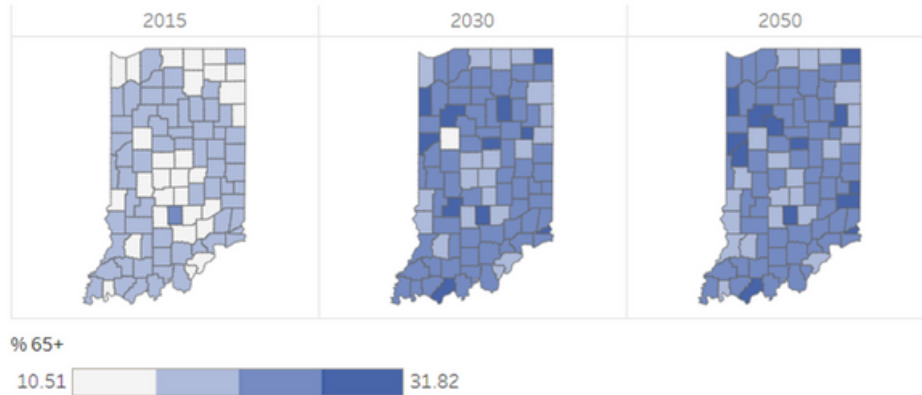
The “unexpected” growth in Medicaid spending is due to increased utilization and recent rate increases for Medicaid providers. Specifically, the increased utilization comes from home and community-based care (waivers) catching up with unmet need that existed in the system prior to the pandemic, combined with the aforementioned aging population.

The flexibility around community and home based care that began during the public health emergency has now made the system somewhat volatile for many states, due to the high demand and increased costs associated with many of these services. As a general rule, many Hoosier seniors would prefer to age in place and new programs such as the PathWays program that takes effect in February of this year will make it easier for seniors to maximize their benefits while living as independently as possible, for as long as possible.



But the growth in Medicaid is not simply due to the aging Hoosier population. The \$1 Billion variance is also due to nursing facility cost increases, hospital cost increases, and Applied Behavior Therapy (ABA) rate increases for children diagnosed with Autism Spectrum Disorder (ASD). All these rate increases have been approved and or discussed by the Indiana General Assembly and the Medicaid Oversight Committee. There was also a large increase in enrollment – even after many participants lost their eligibility when the public health emergency ended. In fact, there is expected to be a net growth of 370,000 individuals – the largest impacted population was Hoosier children (not seniors), with net growth of over 100,000.

Percent of Population Ages 65 and Older by County Indiana Business Research Center



It is important to remember that Medicaid is an entitlement. This means that Indiana must spend what is required to serve eligible individuals under the program. If Medicaid spending is not addressed by the General Assembly, or if there is not a retroactive appropriation made for the Medicaid budget, the State Budget Agency will need to identify funding in other state accounts in order to pay for these services.

Indiana Medicaid Snapshot

Est Medicaid Spending	Shortfall	Enrollment
<ul style="list-style-type: none"> • \$17.9 B in FY 2023 • \$19.4 B in FY 2024 • \$20.6 B in FY 2025 • Indiana pays for 1/3 of this cost, 2/3 is paid for by federal government 	<ul style="list-style-type: none"> • \$271.2 M in FY 2023 • \$255.2 M in FY 2024 • \$457.9 M in FY 2025 	<ul style="list-style-type: none"> • Expected May 2024 Enrollment of 1.857 Million Hoosiers • 1 out of 4 Hoosiers • 370k Net Growth from Pandemic Expansion • Over 100k of Growth are Children

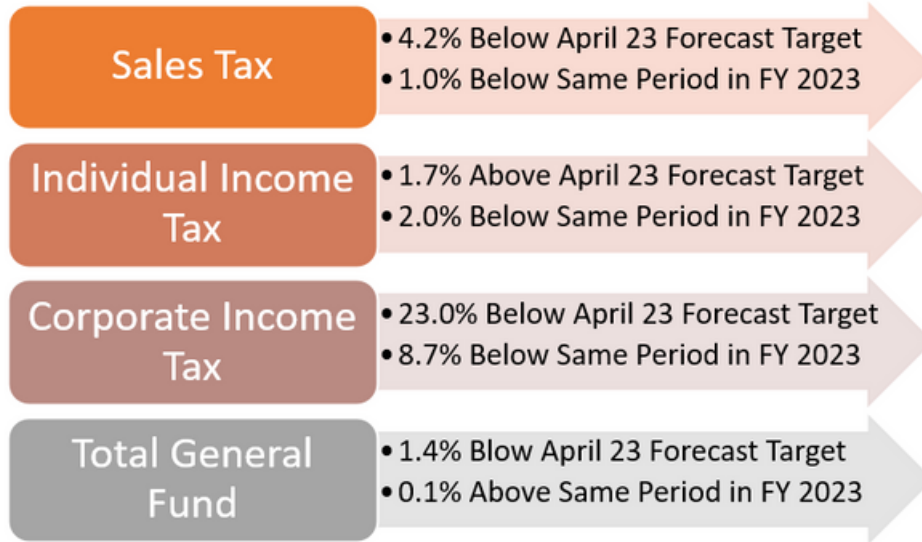
Disparities in Revenue Forecast

In Indiana, 91% of all revenue is generated from the individual income tax, corporate tax, and sales taxes. Known as the “Big 3”, their combined revenue was down 1.4% from the April 2023 forecast. One reason for this differential was legislative changes in the state budget passed in Spring 2023. A few of the legislative changes that impacted the revised revenue forecast include: Indiana Earned Income Tax Credit is now 10% of federal EITC, the passage of a tax exemption for military pay, and a credit for the Indiana Pass Through Entity Tax (PTET). Despite the continued lowering of the individual income tax rate, income tax revenues came in \$50 million higher than the April forecast, due to higher wages.

In all, the state will take in almost \$500 million less over the biennium. Technically, the difference has already been made whole through estimated structural surpluses of \$328.7M in FY 24 and \$231.6M in FY 25. It is still possible that leaders may opt to cut spending or, when building the budget for FY 25-27, institute straight line spending, which is, in effect, a reduction in spending.

Performance of Major Revenue Sources Year-To-Date Through November 30, 2023 FY 2024

Indiana Revenue Forecast Committee



Total Indiana General Fund Revenue Forecast Fiscal Years 2024 and 2025 December 19, 2023 (in Millions) Indiana Revenue Forecast Committee

	FY 2022	FY 2023	FY 2024					FY 2025				
	Actual 2022	Actuals 2023	April 2023 Forecast	Updated Forecast	Year over Year Growth	\$ Diff vs Prior Forecast	% Diff vs Prior Forecast	April 2023 Forecast	Updated Forecast	Year over Year Growth	\$ Diff vs Prior Forecast	% Diff vs Prior Forecast
			2024	2024	2024	2024	2024	2024	2025	2025	2025	2025
Major Taxes												
Sales & Use	9,991.0	10,464.7	10,815.2	10,455.3	-0.1%	-359.9	-3.3%	11,100.6	10,916.9	4.4%	-183.7	-1.7%
Individual Income	8,181.2	7,575.7	7,507.4	8,012.0	5.8%	104.6	1.3%	8,240.3	8,283.6	3.4%	43.4	0.5%
Corporate - AGI, URT, USUT, FIT	1,539.5	1,230.6	1,358.4	1,146.7	-6.8%	-211.8	-15.6%	1,378.8	1,202.5	4.9%	-176.4	-12.8%
Riverboat Wagering	311.2	348.8	296.9	315.6	-9.5%	18.7	6.3%	294.8	309.0	-2.1%	14.2	4.8%
Racino Wagering	141.1	139.8	142.0	135.7	-2.9%	-6.3	-4.4%	143.1	138.2	1.8%	-4.9	-3.5%
Subtotal Major Taxes	20,164.1	19,759.6	20,519.9	20,065.3	1.55%	-454.7	-2.2%	21,157.6	20,850.2	3.9%	-307.4	-1.5%
Other Revenue												
Cigarette	221.4	217.4	218.3	204.0	-6.2%	-14.3	-6.6%	213.0	197.8	-3.0%	-15.2	-7.1%
Insurance	251.9	261.8	272.6	274.0	4.7%	1.4	0.5%	276.8	280.8	2.5%	4.0	1.4%
Inheritance	0.0	0.1	0.0	0.0	N/A	0.0	N/A	0.0	0.0	N/A	0.0	N/A
Alcoholic Beverages	21.1	23.1	21.7	23.1	0.2%	1.4	6.5%	22.2	23.7	2.6%	1.5	6.8%
Riverboat Supplemental Wagering Tax	7.8	11.5	9.7	10.1	-12.8%	0.4	3.7%	9.6	9.9	-1.9%	0.3	2.8%
Interest	33.9	287.2	290.0	393.5	37.0%	103.5	35.7%	220.0	407.3	3.5%	187.3	85.1%
Motor & Commercial Vehicle Excise	288.5	284.1	301.7	296.6	4.4%	-5.2	-1.7%	309.6	304.4	2.7%	-5.2	-1.7%
Miscellaneous Revenue	202.0	213.3	229.1	232.7	9.1%	12.5	5.7%	223.2	239.3	2.9%	16.2	7.3%
Subtotal Other Revenue	1,026.6	1,298.6	1,334.2	1,433.9	10.4%	99.7	7.5%	1,274.3	1,463.2	2.0%	188.9	14.8%
Total General Fund	21,190.7	21,058.2	21,854.1	21,499.2	2.1%	-354.9	-1.6%	22,431.9	22,313.3	3.8%	-118.6	-0.5%

Impact on Fiscal Policy

Legislative leaders insist that this loss in surplus will not impact the work of the State and Local Tax Review Task Force. However, legislative leaders will lean on the Medicaid Oversight Committee (which made no recommendations in 2023, just weeks before the revelations of the Medicaid shortfall became known) to provide oversight and guidance to FSSA and their administration of the program. FSSA leaders promised forecast process improvements (utilizing real-time data) and cost containment but emphasized that enrollment policies and processes will not be impacted.

Legislative leaders have indicated that they have misgivings about recent rate increases, given the \$1 Billion shortfall. They have also indicated that no spending bills and no expansion of Medicaid will be entertained during the Short Session. For those that follow the Indiana General Assembly, fiscal leaders will have to balance several competing priorities this year to be on solid fiscal footing for the 2025 Budget Session.

About the Indiana Fiscal Policy Institute

The Indiana Fiscal Policy Institute is Indiana's only independent statewide source of continuing research into the impact of state taxing and spending policies in Indiana. The IFPI is privately supported by a variety of organizations, corporations, associations, and individuals in Indiana and surrounding states. 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 issues and the consequences of state and local decisions. The Institute makes a significant contribution to the important, ongoing debate over the appropriate role of government. The Institute does not lobby, support, or oppose candidates for public office. Instead, it relies on objective research evidence as the basis for assessing sound state fiscal policy. Learn more at www.indianafiscal.org