Indiana’s Property Tax, Choice, and Accountability Reforms: Their Consequences for Funding and Student Achievement

Dale Chu

With contributions from Benjamin Scafidi

December 2019
Introduction

Many factors potentially influence school quality and student success in the public education system. The amount of school funding and the equity of funding across public school districts are two of these potential factors. In the United States, the responsibility for school funding falls primarily to states and local districts, with state legislatures often assigning required levels of district effort, and federal Title programs adding resources to support low-income students and students with special needs. Each state sets its own school funding policy, and each has a unique system for doing so.

Nationally, approximately $257 billion—or 81 percent—of local revenues for public school districts derive from local property taxes. One sees the dilemma immediately: because property tax revenues are tied to a community’s wealth, districts with lower levels of property wealth per student must tax themselves at higher rates in order to provide their students with a level of resources equal to those districts with higher levels of property wealth per student. Federal and state funding programs endeavor to make up the difference, but sometimes not to the extent that some equity advocates desire. The problem is compounded by middle-class families’ rational choice to move to “better” school districts, purchasing or renting more expensive dwellings, and removing much-needed social capital from lower-performing schools in the process.

While the scope of school-funding inequities is often debated and routinely litigated, in practice, reforming the state funding system for public schools has been proven easier said than done.

---

1 The Johns Hopkins Institute for Education Policy and Dale Chu would like to thank participants in the October 1 round table discussion; their comments guided our final version. Specifically, we thank Tori Bell (Philanthropy Roundtable); Patrick Brown (Joint Economic Committee); Pat Burke (Philanthropy Roundtable); Michelle Burris (The Century Foundation); Andrew Byers (Charles Koch Foundations); David Casalaspi (National Governors Association); Halli Faulkner (American Federation of Children); Checker Finn and Mike Petrilli (The Thomas B. Fordham Institute); Phyllis Jordan and Brooke LePage (FutureEd); Jessica Sutter (DC Board of Education); Ramin Taheri (Chiefs for Change); and Peter Zamora (CCSSO), for their contributions.

2 The extent to which the amount of funding per student matters, and in what ways it could matter, is a matter of intense debate. For a summary of recent research please see: Alanna Bjorklund-Young, “Does Money Matter? Hanushek, Jackson, and the Questions We Ask” (Baltimore, MD: Johns Hopkins Institute for Education Policy, November 6, 2017), https://edpolicy.education.jhu.edu/does-money-matter-hanushek-jackson-and-the-questions-we-ask/. Differences in funding levels across public schools and districts may differentially impact the quality of education offered to students to the extent it impacts their ability to recruit and retain quality staff, for example Benjamin Scafidi, David Sjoquist, and Todd Stonebrickner, “Race, Poverty, and Teacher Mobility,” *Economics of Education Review* 26, no. 3 (April 2007): 145–59.

3 Beginning in the 1970s, teams of lawyers and experts have sued virtually every state in order to ask state courts to require that state legislatures provide more funding to all public schools and/or ensure that total amounts spent across public schools are more equitable. These lawsuits have often been successful. See, for example, San Antonio Independent School District v. Rodriguez and https://www.law.cornell.edu/supremecourt/text/411/1 and Hanushek and Lindseth (2009), https://www.amazon.com/Schoolhouses-Courthouses-Statehouses-Funding-Achievement-Americas-ebook/dp/B002IT4VPQ/ref=sr_1_1. Also, here is a list of school finance litigation.


5 EdBuild has a number of informative resources on school funding inequities, https://edbuild.org/content/resource-inequality-2014.


Several candidates in the 2020 Democratic presidential primary support reforms in school funding. Specifically, they have criticized the inequities created by today’s heavy reliance on property taxes. However, none of them have articulated a mechanism by which reform might occur — a hesitation sponsored perhaps from the ongoing philosophical debate over the federal government’s role in improving schools, and the risk of losing political support from suburban families who expended substantial resources to live within the boundaries of “good” school districts (Fischel, 2005).

However, while reforming state funding formulas is difficult, it is by no means impossible, as Indiana’s case indicates. The property tax reforms the state undertook in 2008 did not aim to redesign school funding, but they resulted in a transfer of fiscal responsibility from district to state funding for public schools and a decoupling of property wealth from the amount of funds local public school districts have to spend. These reforms resulted in greater district fiscal accountability and made it more feasible to move the state toward an education system where parents were allowed to exercise more choices.

This paper provides an insider’s look into Indiana’s overhaul of its property tax system, the increases in choice and accountability, and the resulting impact on the state’s schools and students. From 2009 to 2013, lead author Dale Chu served as the Assistant Superintendent for Innovation and Improvement at the Indiana Department of Education, and had a front-row view of the reforms’ impact. In summer 2019, Mr. Chu conducted structured interviews with other state and local officials who were participants in the debates, passage, and implementation of these reforms. He also examined research and news items during and subsequent to the reform period. This paper explains Indiana’s historic change to its system of state taxpayer funding for public schools; the politics at play that allowed for a move away from property-based funding; the passing of the 2008 property tax law and the school funding changes that resulted; changes in school choice and accountability policies that soon followed, and lessons from the Hoosier State upon which other states might draw.

The contributing author, Ben Scafidi, served as the education policy advisor to the governor of Georgia from 2003 to 2005. During that time, state policymakers created a commission that endeavored to change the state formula for funding public schools. There was also a second effort at that time: legislation to create a property tax reform similar to what later passed in Indiana. Neither effort came close to becoming law in Georgia. At that time, there was not a perceived crisis in Georgia, as was the case in Indiana.

**Prelude to the Indiana Property Tax Reforms**

What were the conditions under which Indiana was able to forge meaningful, bi-partisan

---


9 The eight interviewees spoke with the author on the condition of anonymity. The interviewees were either state or local officials in Indiana during the time period under study. All of the interviews were conducted via telephone and occurred in July and August 2019.
revisions to its property tax laws in 2008? Property tax reform became urgent for two key reasons: a significant increase in homeowners’ property taxes dating to 2007, and the economic distortions borne from “high variability” in tax rates between counties across the state.

*Homeowners’ property tax rates.* In 2006, the last year prior to the 2008 reforms for which full data existed, 78% of the state’s population owned homes; the remaining 22% were renters. From 2003 to 2007, property tax payments increased by more than 30%, with “statewide growth in property taxes [remaining] at between twice and four times the rate of inflation.” Why? A major re-assessment in 2007 had, with a new 100% deduction in business inventories, “resulted in large shifts of the property tax burden from business property to residential property in some parts of the state.” Such rising rates inspired protests at the state capital and calls to abolish property taxes altogether. As Nobel Laureate Milton Friedman surmised years ago, “(The property tax) is not unpopular for good economic reasons. It’s unpopular in my opinion for one simple reason: it’s the only tax left on the books for which people have to write a big check.” Given that those big property tax checks for Indiana homeowners got significantly larger over a very short period of time, it is not surprising that the 78% of the adult population who owned homes were angry—and that their anger created a political crisis for Indiana policymakers.

*Horizontal variation in rates.* There was a longstanding second reason why Indiana homeowners, and businesses, were angry about property taxes: the unfairness with how they were implemented in the Hoosier State. By 2008, Indiana had more than 1,000 property tax assessment offices, each of which applied significantly different standards to assign property values. In addition to leading to large differences in property tax payments across these tax jurisdictions—even for similar properties, this variability was viewed as a causal factor in the state’s economic decline. As a report presented at the 101st annual meeting of the National Tax Association (2008) noted,

> Simply crossing the Muncie City line into several adjacent townships will result in a 65% drop in taxes for identical properties. This translates into a savings of $1,157 annually for the median priced home in Indiana. These stark border effects are rare nationwide. Their effect is exaggerated in Indiana through the multiplicity of townships that dramatically increase the

---

10 Property taxes had been the locus of significant contention in Indiana for some decades. For a detailed history, see Robert S. Michael, Terry E. Spradlin, and Fatima R. Carson, “Changes in Indiana School Funding,” Education Policy Brief (Bloomington, IN: Center for Evaluation & Education Policy, Summer 2009), http://www.ceep.indiana.edu/finance/PDF/PB0013_School%20Funding_020212.pdf.
11 In polling data, property taxes have long been the most hated tax in America. However, economists tend to like property taxes as a means of generating government revenue because, among other reasons, it represents a revenue source that is more stable through business cycles relative to income taxes and, especially, sales taxes. Nevertheless economists and others also recognize the inequity of funding local public schools with property taxes, given the differences in property wealth per student across school districts, [https://www.bloomberg.com/opinion/articles/2017-11-28/why-economists-love-property-taxes-and-you-don-t](https://www.bloomberg.com/opinion/articles/2017-11-28/why-economists-love-property-taxes-and-you-don-t).
14 Bohanon, Faulk, and Hicks, “Property Tax Restructuring in Indiana.”, 243.
number of residential and business locations affected by large border rate differentials.\textsuperscript{16}

The authors of the study suggested that stabilizing property taxes (both in terms of growth rates and variability between jurisdictions) would likely have a positive effect upon economic growth.\textsuperscript{17}

These two factors conspired to cause a decline in economic prospects. Many businesses had left the state, and the state government’s credit rating dropped twice between 2002 and 2004.\textsuperscript{18} This decline resulted in lower state revenues and thus lower state support for local governments, which then led locals to raise property taxes to an unprecedented level. \textit{The Wall Street Journal} described the scenario in 2010:

\textit{The Indiana debate reflects concerns about property taxes among homeowners nationwide. As the recession has slashed income and sales tax revenues, states have cut funds for local governments. In response, some cities, towns and school districts have raised property taxes—their main source of revenue—to partially fill gaps, even as property values have fallen... A 2007 spike in Indiana’s property tax bills led to a protest, the ousting of the mayor of Indianapolis, and a 2008 law limiting property taxes.}\textsuperscript{19}

By 2004, the state’s budget was $700 million in the red following seven consecutive years of unbalanced budgets. Concerns about the state’s fiscal health contributed to the election of Indiana’s first Republican governor in 16 years, Governor Mitch Daniels, who assumed office in 2004 after winning 53.2 percent of the vote.

Daniels set out a four-step plan: Balance the budget, pay off debts, build a reserve fund, and cut taxes. During his tenure (2005-2013), which coincided with the worst recession since the Great Depression, the $700 million deficit became a $1.8 billion surplus.\textsuperscript{20}

\textbf{The politics}

In 2008, Indiana’s government was divided: Republicans controlled the Senate 33-17, and Democrats controlled the House 52-48. Republicans have held the upper chamber since 1978. The Indiana House has been more volatile, and had switched majorities frequently in the prior decades (See Figure 1).\textsuperscript{21} The declining economic circumstances and constituents’ intense dissatisfaction made bipartisan legislation possible.

\textsuperscript{16} Bohanon, Faulk, and Hicks, “Property Tax Restructuring in Indiana.”, 243.
\textsuperscript{17} Bohanon, Faulk, and Hicks., 246.
\textsuperscript{18} Between 2002 and the end of 2004, while the national macroeconomy was expanding, the unemployment rate in Indiana increased from 5.4% to 5.6%: Bureau of Labor Statistics, “Indiana Economy at a Glance,” United States Department of Labor, accessed November 13, 2019, https://www.bls.gov/eag/eag.in.htm.
\textsuperscript{20} Ryan Streeter, “The Aspirational State: Indiana as a Guide for Reformers” (Sagamore Institute, December 2011).
\textsuperscript{21} However, Republicans gained the lower chamber during the 2010 midterms and have held undivided government until the present day.
**Historical background to school funding**

Since 1949, at the state level, Indiana has employed a student-based funding system known as the Foundation Program; it is one of thirty-eight states to do so. The mechanism includes three essential elements: (1) a minimum foundation amount known as the Foundation Level, which is established during each biennial budget session by the Indiana General Assembly; (2) the student count taken twice a year, known as Average Daily Membership; and (3) the share of students eligible for federal food stamps and welfare benefits, known as the Complexity Index, which can lead to increased funding above the Foundation amount. Despite changes in how the state calculates the funding formula, Indiana has maintained a progressive model that allows more dollars to flow to those in greater need. The seven-billion-dollar question (i.e., the annual amount of state tuition support) is how to fund schools fairly across all types of districts—urban, suburban, and rural—when facing increasing or decreasing enrollment numbers. The Foundation Program has been at the heart of this effort.

A second source of state funding comes in the form of categorical grants via the Depart-

---

22 Ballotpedia, "Indiana Property Tax Cap Amendment, Public Question 1 (2010)," Ballotpedia, accessed September 25, 2019, [https://ballotpedia.org/Indiana_Property_Tax_Cap_Amendment,_Public_Question_1_(2010)].
ment of Treasury’s General Fund. For instance, districts may apply for “General Fund” grants based on their number of special education students, students taking career and technical education courses, or those graduating with an advanced diploma. This fund is the primary source that covers operating costs for Indiana school districts. (The General Fund also supports other governmental activities; its 2019 allocation, for instance, includes 44.8% for K-12 and also 14.8% for Medicaid, 5.5% for Child Services, and 4.4% for Corrections.23)

But the state’s funding for operating costs – or lack thereof – were not the only problem some had with school-funding mechanisms. Capital-cost projects for school facilities were potentially unlimited, further straining local resources without necessarily improving academic results.24

The Property Tax Reform and its Consequences for School Funding

The economic and political conditions described above made it possible for policymakers to support two related changes to the state’s property taxes, one legislative, the other constitutional. The most important impacts on school funding were a) the end of local responsibility for the operating costs (“General Fund”) for schools; b) the assumption of all school operating costs by the state. The state accomplished this through an increased sales tax, which was channeled into the Treasury Department’s General Fund. The General Fund post-2008 assumed 100% of the school operating expenses – up from 85% before the reforms.

Legislative. Daniels outlined four objectives as part of his property tax reform plan:

• Immediate and significant relief for all property taxpayers.
• Permanent protection against future tax increases.
• Meaningful controls on local government spending.
• Improved accuracy and fairness in the assessment of property values.

The passage of this reform plan would address all four objectives, and had substantial ramifications for the state’s school finance system. On March 14, 2008, the Indiana General Assembly passed Public Law 146 (P.L. 146) (House Enrolled Act 1001-2008) with support of 82-17. The main feature of the law was a cap on homeowner property taxes at one percent of the home’s assessed value. Rental properties and farms were capped at two percent, and business property at three percent. To offset these revenue reductions, the state’s sales tax was raised from six to seven percent.

The final house bill was more than 800 pages and had been “negotiate[ed]” by “majority House Democrats and Senate Republicans.” While Senate Tax Chairman Luke Kenley,

23 Indiana Department of Treasury, “Biennial General Fund Expenditures,” Indiana Department of Treasury, 2019, https://www.in.gov/sba/files/AP_2019_1_1_1_7_Biennial_GF_Appropriations.pdf.
R-Noblesville, noted that “the homeowners and the taxpayers are the winners,” House Speaker Patrick Bauer, D-South Bend, called it “a compromise all the way through,” because renters and low-income seniors also received tax breaks.25 Both parties supported leaders who were willing to expend significant political capital to make reform possible.

The new law’s major provisions, as set out in the Association of Indiana Counties’ April 2008 document, included: 26

- **Property Tax Relief:**
  - Additional Homestead Credit (reduced 2008 tax bills).
  - New Homestead Credit.
  - Increased renter’s deduction from $2500 to $3000.
  - Increased Earned Income Tax Credit from 6 to 9% and repeals expiration date.

- **Property Tax Caps (exception for Lake and St. Joseph Counties)**
  - Homesteads: 2008 2%; 2009, 1.5%; 2010 1%.
  - Agricultural land, rentals, long-term care: 2009 2.5%, 2010 2%.
  - All other real and personal property: 2008 3.5%, 2010 3%.

- **Relief for schools through the General Fund:**
  - “Provides $120 Million to offset the revenue loss for schools that have an impact of greater than 2%of their levy” ($50M in 2009, $70M in 2010).
  - “Allows schools to have a referendum to offset the impact of the Property Tax Caps.”

- **Sales tax increase and levy pick-up**
  - $0.01 increase in 2008.
  - Sales tax, income tax, gaming taxes placed into State General Fund to pay for levies.

- **State assumes many of local governments’ costs such as Medicaid and child welfare (see slide below).**

...and:

The law also brought compensatory protections for schools, such as a new State Tuition Reserve Fund, and new accountability for schools, such as:

- Requiring school boards to adopt budgets on a fiscal year basis; and
- Restricting school capital investments to $10M and $20M for Grades K-8 and 9-12 buildings, respectively, unless a local referendum is passed;
- Requiring the Indiana Department of Education to establish protocols for schools’ capital projects.

The law also imposed fiscal restraints upon other county and city projects and changed the property evaluation process to be appointed rather than elected.

Finally, the law rationalized the property evaluation process, by reducing the number of assessing bodies from 1100 to fewer than 100 and boosting the certification requirements

---

for would-be assessors.27

The shifting of fiscal responsibility from local governments to the state was extensive, as two slides explaining the changes indicate.

**State Assumption of Levies & Costs**

- State Assumes Full Cost for Remaining School General Fund & Pre-school Special Education
- State Assumes Full Cost for Child Welfare Levies
  - County Family & Children Fund
  - Medical Assistance to Wards (MAW)
  - Children’s Residential Psychiatric Treatment Fund (CRPT)
  - Children with Special Health Care Needs
- County Income Tax & Excise Tax Distributions Protected when State Assumes Levies.
- County is obligated to pay for welfare services delivered before January 1, 2009.
- Excess money in Family & Children Fund and CRPT Fund shall be deposited in the county’s Levy Excess Fund.
- Excess money in the MAW Fund and Children with Special Health Care Needs Fund shall be transferred to the state.
- Eliminates all State Property Tax Levies (State Fair, DNR Forestry)

**State Assumption of Levies & Costs**

- State assumes full cost for incarceration of juveniles in State Correctional Facilities*
- State assumes full cost for Hospital Care for the Indigent (HCI)*
  - Includes $40 Million for Marion County Health & Hospital Corporation since Marion County does not have an HCI Levy.
- State will aid cities by making pre-1977 pension, survivor and disability benefit payments*
- *Levies will be reduced by the amount of cost assumed by state

**Constitutional.** A second plank of the tax reforms amended the state constitution to render the property tax reform permanent. Indiana’s constitutional amendment protocol is quite constrained;28 only the legislature may initiate an amendment, and it must be approved by two successive sessions of the Indiana General Assembly with an intervening election, before being put forward for a public vote. The significant momentum behind the tax-reform amendment, and the electorate’s urgency for structural change, however, made the process possible. The final ballot measure, which was put to the public in 2010,

---

27 Bohanon, Faulk, and Hicks, “Property Tax Restructuring in Indiana.”, 244.
28 In contrast to the process in Arizona, California, and Ohio, which allow for constitutional amendments through an initiative process. See here.
read:

SHALL PROPERTY TAXES BE LIMITED FOR ALL CLASSES OF PROPERTY by amending the Constitution of the State of Indiana to do the following: (1) Limit a taxpayer’s annual property tax bill to the following percentages of gross assessed value: (A) 1% for an owner-occupied primary residence (homestead); (B) 2% for residential property, other than an owner-occupied primary residence, including apartment; (C) 2% for agricultural land; (D) 3% for other real property; and (E) 3% for personal property. The above percentages exclude any property taxes imposed after being approved by the voters in a referendum. (2) Specify that the General Assembly may grant a property tax exemption in the form of a deduction or credit and exempt a mobile home used as a primary residence to the same extent as real property?  

The constitutional ballot passed in November 2010, with 72 percent of voters approving. This amendment was seen as a necessary step to support long-term stability.

Opposition to the reforms

Objections to the property tax reforms came from a few sources. Among them, the state’s farm bureau questioned why farmers should pay higher property tax rates than others given agriculture’s significant contribution to the state’s business climate. The state chamber of commerce also expressed concerns about businesses shouldering the highest tax rates. Interestingly, local governments did not take issue with the loss of budgetary powers — likely because the state assumed many costs for which local jurisdictions had been responsible — but they did raise concerns about fiscal shortfalls, as did some citizens who feared that the measures would create severe budgets cuts and reduced public services. However, the voters’ agitation about property taxes — represented by common news stories of senior citizens’ losing their homes because they could not pay the property tax — gave hesitant legislators the impetus to vote for the reforms.

Notably, the fact that the reforms targeted property tax revenues rather than education funding, meant that middle-class families did not object. A potential reaction, that is, resistance from suburban enclaves to their schools receiving less property tax revenues, did not materialize in any substantive way. Overwhelming support for the constitutional ballot measure trumped everything else.

To further illustrate how public pressure created unlikely advocates for property tax reform, a Democratic state legislator who is considered a leader within the caucus, and is a farmer by trade, was one of many Democrats who ended up voting in favor of the bill. Daniels himself was also remarkably effective at selling the property tax overhaul to the general public.

The strongest opposition to the plan came from groups who usually agreed with Daniels: fiscal hawks who wanted to abolish property taxes outright. Daniels determined this position to be both impractical (property taxes would still be used for ancillary school services

29 Ballotpedia, “Indiana Property Tax Cap Amendment, Public Question 1 (2010).”
such as capital costs and transportation) and politically implausible.

### The Property Tax Reform’s Results

The results of the property tax reforms are five-fold. First, they amounted to a significant property tax cut for Hoosier households. In fact, a total of $870 million stayed with taxpayers during the first year.\(^{30}\)

Second, the increased sales tax bolstered revenues to the General Fund, the largest source of school funding, in 2009—from $3.8 billion to $6.3 billion, with constant increases from then on (see Figure 2).\(^{31}\)

### Figure 2. State and Local Share of General Fund Revenue, 1993-2009\(^ {32}\)

![Figure 2](image)

Third, the state’s assumption of full responsibility for the General Fund (for K-12 education) helped low-income districts, and required high-income districts to be more judicious in their spending.

We report two basic metrics to show that the property tax reform along with the state’s assumption of funding the entirety of the K-12 “General Fund” increased equity in Indiana’s system of school finance. First, we consider the amount of state and local revenues for districts with below-median and above-median local revenues per student. In 2006-07, before the tax and spending reform, the median local revenue per student was $3,618.\(^ {33}\)


\(^{31}\) Andrew Jackson, “Effects of the Elimination of Indiana General Fund Property Tax and Other Local Sources of Revenue on Student Transfer Policies” (Doctoral Dissertation, December 17, 2011), http://cardinalscholar.bsu.edu/handle/123456789/195134.

\(^{32}\) Michael, Spradlin, and Carson, “Changes in Indiana School Funding,” 3.

\(^{33}\) Revenue and expenditure data for Indiana school corporations are from data reported annually by the Indiana Department of
For school districts below this median in 2006-07, state and local funding per student increased by $3,241 between 2006-07 and 2015-16, the most recent data available. For districts with above-median local revenue per student, state and local funding increased by $2,223 per student during this time period, which translates to a 31% smaller increase for these wealthier districts. Thus, districts with lower levels of local funding before the reforms received 31% larger increases in state and local funding over the eight-year period after the reforms. These figures are not adjusted for inflation—we make that adjustment later in the report.

Figure 3. Nominal Change in State and Local Per-Student Revenues 2006-07 to 2015-16

To further illustrate the increase in equity that results from Indiana’s reforms, we report the 90-10 ratio—the ratio of total expenditures per student for the 90th percentile highest spending district to the district spending in the 10th percentile—a district with very low expenditures per student. In 2006-07, the 90th percentile district in Indiana had expenditures per student that were a full 50% higher than the district in the 10th percentile. By 2015-16, eight years after the property tax reform, this gap had fallen to only 32%—a large increase in equity in a very short period of time.

34 Author calculations from data reported annually by the Indiana Department of Education to the National Center. National Center for Education Statistics.
A more detailed analysis released by the Urban Institute also shows that Indiana’s funding system has become more progressive over time—providing greater funding levels to more disadvantaged students relative to wealthier students. In Figure 5 below, the x-axis shows the progressivity or regressivity of school funding systems in 1994-95, while the y-axis contains that information for 2013-14. Indiana is one of the states that has had a progressive education funding system over time, and the state’s funding system was more progressive in 2013-14 relative to 1994-95.

35 Author calculations from data reported annually by the Indiana Department of Education. National Center for Education Statistics.

Indiana’s reforms also placed more financial “accountability” with respect to local funding on high-wealth school districts—more accountability to local taxpayers. Instead of filling budgets to meet the available property tax funding, wealthy districts now had to work the other way around. They could no longer raise operating costs via property tax revenues without a public referendum.

To illustrate the before-and-after contrast, there had been only six local tax referenda for operating costs prior to 2008, only three of which had passed. Since 2008, there have been 120 tax referenda for operating costs, and 82 have passed (See Figure 6)\(^{37}\). For many districts, this financial accountability became the single most important consequence of the reforms. While for low-wealth districts, the increased funding was surely welcomed, residents of wealthy districts benefited from the increase in local financial accountability.

![Figure 6. Operating Cost Referenda](image)

Fourth, the new law placed statutory limits on how much districts could ask for when issuing bonds for capital improvements to schools. This was a notable change given the large-scale spending some districts had previously undertaken with regard to facilities. This limit on capital expenditures appears to have had some effect. Between 2006 and 2016, expenditures per student for capital and debt service decreased by 20% in Indiana—compared to a 16% decrease in the nation as a whole (See Figure 7):

\(^{37}\) Data provided via email by Larry DeBoer.
In some respects, the referendum component of these reforms has helped to redefine the meaning of local control in Indiana. Requiring a public vote of confidence before major expenditures has enabled greater fiscal accountability—to local voters and taxpayers. Local leaders must be diligent and deliberate as never before in order to successfully advance a referendum among their constituents.

Fifth, as an unintended consequence, the reforms made inter-district school transfers easier. It had been the case that parents who wanted to enroll their children in schools outside their districts, were charged transfer tuition. Once the state assumed 100 percent of the General Fund contribution, even many low-income students could enroll outside their neighborhoods and districts because the tuition bill dramatically dropped as the district share of funding decreased. One insider described the benefits of the property tax reforms to inter-district school choice as a “happy accident.” This sentiment was echoed by several others interviewed for this report.

Did the changes in school funding produce an obvious impact upon academic outcomes? Did the reforms improve the productivity of Indiana’s public school system? Some performance measures have trended positively (see the final section below). However, the presence of concurrent educational reforms makes it difficult to draw a straight line between the new funding system and student results.

**Concurrent Educational Reforms**

Several other changes in Indiana’s school systems coincided with the property tax reforms. Three of these moved Indiana toward a more pluralist education system:

---

38 Author calculations from data reported annually by the Indiana Department of Education. National Center for Education Statistics, “ELSI - Elementary and Secondary Information System.”
- The creation of the Indiana Choice Scholarship Program.
- An elimination of the cap on the number of charter schools.
- An inadvertent increase in the ease in which families could exercise inter-district choice within the public education system.

One of the cornerstone reforms that happened concurrently was the enactment and launch of the state’s voucher program in 2011, known as Indiana’s Choice Scholarship Program. The enabling legislation passed largely along party lines, with Democrats in both chambers voting against the measure. The state teachers’ association unsuccessfully fought against it. It is now one of the largest in the country, with more than 36,000 participating students. The means-tested program was initially limited to very low-income students, but has since been expanded to the point at which 50 percent of students are eligible statewide. The state’s property tax reform made the size of these scholarships larger than they would have been absent the reform, as these scholarships are funded by the state in a manner that is tied to state support for public school students. As state support per public school student increased, the size of these scholarships increased as well—and this relationship between funding for the scholarship and state support for public school students is statutory.

With a removal of the cap on the number of charter schools, charter school enrollment grew significantly during this time period as well. While there has been a decrease in the number of charter school students in recent years, between 2006 and 2018, the number of Indiana students enrolled in a charter school increased from 7,000 to 38,000.

The state’s transition to a full-state (General) funding model for K-12 public schools not only helped to engender a more equitable funding system, it also created, albeit unintentionally, an environment more conducive to school choice within the public education system. By relying less on property taxes for school funding, Indiana’s system leveled the playing field and empowered more families to seek out the options that work best for their children within the traditional public education system. In 2008, Tony Bennett was elected to State Superintendent of Public Instruction. His team worked with Daniels to outline how the state’s assumption of school operating costs would facilitate a true open enrollment system.

One could argue that the move toward more state funding—and less reliance on local funding—for public schools was a move toward centralization and away from local control. In Indiana, however, the shift to state funding was counterintuitively a step toward more local control – in the form of parent rather than district choices. District-school choice (both within and between school districts) is significantly larger than it was prior to the reform, at nearly 60,000 participating students in 2019. The reform also increased

the size of scholarships given to families under the Indiana Choice Scholarship Program. For each student who elects to transfer, the receiving district receives the state’s per pupil allotment for the receiving district—even if that amount is higher than the state’s per pupil allotment for the sending district. Thus, some local officials are concerned that there is no state provision for addressing any funding gap between sending and receiving districts. Even with no funding gaps, local stakeholders appear to be mindful of the inevitable shifts in enrollments. For example, it is not uncommon for district schools to market themselves.\(^{42}\) The pressure from open enrollment has also spurred some districts to expand their programming in an effort to differentiate themselves. As an example, one southern Indiana district opened a charter-like high school employing the New Tech Model as an attempt both to recruit and to retain students.\(^{43}\)

Of course, school districts will always prefer more state funding, but these marketing and management efforts suggest that many districts are working to improve their offerings to be the schools of choice for Indiana families, even in the presence of funding gaps between sending and receiving districts.

Further, economic research suggests that public school districts have significant variable costs—and therefore can reduce some costs when they lose students.\(^{44}\) This ability to reduce costs seems to be the case in Indiana school districts. Between 2006 and 2016, more than 79% of Indiana school districts experienced a decline in enrollment. For these districts that lost enrollment, the changes in per-pupil spending were almost identical to changes in per-pupil spending in districts that experienced enrollment growth—$993 increase in current expenditures per student in districts with declining enrollments and a $1,013 increase for districts with increasing enrollments.\(^{45}\) (These figures are not adjusted for inflation.) Thus, changes in per-student resources have been invariant to changes in district-wide student enrollments.

By 2018, nearly 130,000 Indiana students were enrolled in schools of choice—schools that were not their traditional neighborhood public school. As shown in Figure 8, these students were enrolled in a traditional public school in another district, a charter public school, or a private school via the Indiana Choice Scholarship Program. The net result has been a significant pluralization of educational options for families in the Hoosier State.

---


\(^{45}\) Current expenditures include all expenditures except those for capital and debt service. Of course, districts with increasing enrollments will need to build more or expand existing school buildings. For this reason, we excluded expenditures on these items to make this point that changes in resources for students are approximately invariant to changes in enrollment.
There were two additional reforms during this time period that may have impacted the performance of Indiana’s public schools.

First, in 2010, Indiana moved to an A-F letter grading system of all schools. Unlike other states that offer private school choice, Indiana’s A-F accountability system applies to both public and non-public schools—making it the most comprehensive in the nation (See Figure 9). All participating non-public schools receive a letter grade, and all students in private schools that participate in the voucher program—including those students who do not receive a voucher—are required by law to take state tests. Readers from outside Indiana should note, however, that many private schools already had administered the state test and received letter grades prior to the voucher program. This was required in order to receive state accreditation, a prerequisite for participation in the state’s high school athletics association.

Finally, in 2013, Indiana added a second annual student-count date after ending rolling averages—famously known as the “de-ghoster” or “re-ghoster” program—as a means to count students two years earlier. The legislature made both changes statutorily in an effort to ensure that funding followed the student. These changes brought additional accountability into the school budgeting process.

In general, the widespread allowance and use of a variety of schooling options, the state’s robust accountability program, and the decoupling of school funding from property taxes which brought more equity in funding across public schools, bring Indiana closer to a pluralist ideal, where families are empowered to choose among different schools regulated by the government but not necessarily provided by the local public school district.46

Academic results? Productivity? Before considering whether this suite of reforms has led to changes in achievement for Indiana students or improvements in productivity for Indiana schools, we must consider the issue of changes in total funding in public schools. We have noted that the 2008 property tax reform caused a swap of state funding in lieu of local funding for the school funding formula’s “General Fund” operating costs. Critics were worried that this reform would cause school funding to decline over time. We cannot attribute the drop in funding to the reforms—because macroeconomic and state budget factors matter as well. Nevertheless, funding per student—including federal, state, and local dollars and adjusted for inflation—did decline in Indiana in the period after the property tax reform. To be clear, this decline in funding may have occurred anyway—even absent the reform—because of longstanding economic and demographic challenges in Indiana and the heartland of the United States.

While public schools in the United States as a whole experienced an inflation-adjusted increase in funding of $915 per student between 2006 and 2016, Indiana public schools saw a decline in funding of $977 per student during this time period.\textsuperscript{49}

Advocates of the property tax reform; funding equity; increases in choice to private, charter, and neighboring district public schools; A-F letter grades and academic accountability; and the financial accountability reforms believe that these would increase student achievement. However, some researchers and some education advocates would argue that the overall funding decreases should lead to a decrease in academic performance.

Let’s “look at the back of the baseball card” to see what the statistics on student achievement say occurred during this era of reform in the K-12 education system in Indiana.

The sheer number of reforms makes inferences about any one of these reforms or about the decrease in funding impossible. That said, we can use the National Assessment of Educational Progress (NAEP) to evaluate whether these reforms and funding changes—as a package—had any impact on student learning.\textsuperscript{50} For NAEP scores, we compare changes in Indiana to changes in the national average. From 2007 to 2017, gains in performance of Indiana public school students exceeded the national average for all public school students in reading and mathematics for both grades four and eight.

\begin{figure}
\centering
\includegraphics[width=\textwidth]{figure10.png}
\caption{Real (Inflation-Adjusted) Changes in Current Expenditures per Student 2005-06 to 2015-16}
\end{figure}

\textsuperscript{49} We use current expenditures per student for this comparison and adjust for inflation using the headline Consumer Price Index (CPI-U). https://data.bls.gov/cgi-bin/surveymost?bls
\textsuperscript{50} NAEP is considered the “Nation’s Report Card” and the gold standard of assessments and is given periodically to a large sample of students from every state.
Figure 11. A Comparison of 2007-2017 NAEP Gains Between Indiana and the National Average

Change in NAEP 4th Grade Reading Scores, 2007-2017

Change in NAEP 8th Grade Reading Scores, 2007-2017

For both grades in both subjects, Indiana students experienced larger learning gains relative to the national average—despite real decreases in total funding per student. Thus, we conclude that this suite of reforms—property tax reform, more equitable funding across districts, more choice for families to private, charter, and other public school districts, and academic and financial accountability—appear to have led to strong learning gains in reading and modest gains in math for Indiana students.\(^{52}\)

Parents who exercise choice to private and charter schools routinely report that their children are better off in ways not captured by test scores—more likely to pursue and succeed in higher education, better safety, more respect for their values, etc. (see, for example, Kelly and Scafidi, 2013). [https://www.edchoice.org/wp-content/uploads/2015/07/More-Than-Scores.pdf](https://www.edchoice.org/wp-content/uploads/2015/07/More-Than-Scores.pdf) If these benefits are
Winners and losers. In hindsight, Indiana’s reforms were a boon to school districts with entrepreneurial leadership. District superintendents who recognized the opportunity quickly seized it by marketing to neighboring jurisdictions and sending buses across district boundaries to transport newly recruited students and thus new dollars. Those who didn’t mobilize—in some cases because they didn’t understand the provisions of the new laws—initially struggled in the face of market pressures, and likely experienced enrollment declines.

Another winner is families who could now exercise even more control over their children’s schooling. We can guess the marketing pitch that economic developers now use to recruit companies to Indiana: If you come to the Hoosier state, your employees will be able to choose their children’s public schools in your chosen district, public schools in neighboring districts, charter public schools, and—if they qualify—private schools with a state scholarship. Indiana has become a model in providing an array of educational options. One could also argue that the state as a whole has emerged a winner, both because NAEP scores initially rose relative to the national average, despite decreases in funding, and because market pressure has been applied to a sector that had previously never been subject to them.

The increase in achievement when total funding declined indicates an increase in the productivity of the K-12 education system in Indiana.

At the time of writing this report, changes to the mechanics of the state’s A-F letter grading are being implemented, with the final result uncertain. It will be interesting to see to what extent these changes have an impact on student achievement gains for Indiana’s students.53

Conclusions

Were Indiana’s reforms sui generis, or are they possible elsewhere?

Did Indiana need all of these choice and accountability reforms, or would equalizing school spending have been enough?

Political context for Indiana’s reforms. Political context matters. Strong leadership is essential. Governor Daniels was a popular governor and also among the most highly-regarded state executives in the nation.54 Daniels amassed significant political capital, which among other things engendered a public flirtation with running for president in 2011, a contest he ultimately declined to enter. Following on the heels of the landmark property tax reforms, Daniels supported Bennett in expanding parental choice.

But if leadership is essential, so too, is timing. Marguerite Roza, director of Georgetown University’s Edunomics lab and a national expert on school finance, once said, “The window may be only open every two to three decades in a state to do education finance re-


form. So if you’re in the window, do it right, because that thing is going to close and you’re going to be in 2030 before it opens again.”55 Or as Rahm Emanuel succinctly put it, “You never want a serious crisis to go to waste.”56 This principle certainly pertained in Indiana; the large property tax increases and accompanying economic decline enabled bi-partisan legislation.

Preparation is also critical. Indiana’s economic and educational reformers spent significant amounts of time laying groundwork for the 2008 property tax reforms and the 2011 choice and accountability reforms that followed. The process required innumerable meetings and long-term patience. As one insider put it, an endeavor as “astronomical” as what the state undertook requires gradual preparation, and also concerted efforts to find consensus among the decision-makers.

Technical expertise is also essential. Legislative fiscal analysts and staff at the state’s Office of Management and Budget provided substantial attention to detail. Seasoned district leaders gave behind-the-scenes advice and counsel to Bennett, and helped him translate his agenda for greater accountability and choice in the field. Bennett also successfully recruited the former top statehouse lobbyist of the state teachers’ association, who, critically, helped navigate the legislative and regulatory changes required for the educational changes.

That the state provided a significant share (85%) of the General Fund revenue prior to the 2008 property tax reforms made it easier for Indiana to shift further away from property-based school funding. However, this approach might not be viable, or might require substantially more effort, in states that are more deeply reliant on local funding sources.

Indiana’s approach does provide evidence that students and families, as well as school districts, would be better served if states, rather than local governments, shouldered more of the burden for school funding—accompanied by the suite of choice and accountability reforms that were also enacted into law. This is a point worth underscoring: equity for students and families, plus greater accountability on the part of school districts, are the “both/and” that can bring all sides together.

Another consideration for states is the implications for school funding reform in light of the “Baby Bust.” Since the Great Recession, the nation’s birthrate has been on the decline. In fact, it’s now at a 32-year low. For a number of reasons, Americans are having fewer children. What implications might this have for schools and funding? Although Indiana has seen modest enrollment increases over the years, many states have not. Notably, states with the greatest enrollment declines have seen the greatest increases in per-pupil spending (See Figure 12). This trend could present an opportunity to move away from property-based school funding and to make funding formulas more equitable.

We note that there may be signs of financial trouble ahead for the nation. As in the years leading up to the 2008 recession, the last few years have seen strong growth for school budgets. With the possibility of state revenues’ stumbling in the near future, states might do well to couch any efforts to reform school finance within the context of preparing for harder times. This is especially important in states with schools that are more reliant on state funding such as New Mexico, North Carolina, or Vermont.\footnote{Marguerite Roza, “Dear Districts: These Are the Glory Days. Are You Ready for Tomorrow’s Financial Pain?,” Flypaper at the Thomas B. Fordham Institute (blog), January 30, 2019, https://fordhaminstitute.org/national/commentary/dear-districts-these-are-glory-days-are-you-ready-tomorrows-financial-pain.}

Indiana’s three key ingredients—the movement toward more of a state-based funding model, the expansion of public and non-public school choice, and a robust A-F accountability system that holds both private and public education sectors to account—is a rare triumvirate among states today. These specific features might be challenging to replicate in other jurisdictions, but the development of an overarching framework to more equitably ensure all students access to a constantly improving—even excellent—education merits consideration from policymakers and elected officials of all stripes. There are certainly tensions that have arisen from Indiana’s decision to shoulder the responsibility for school funding, but these tradeoffs have made the education system better as a whole, and continue to fuel the state’s pursuit of educational equity, excellence, and opportunity.

Were the choice and accountability reforms needed in Indiana?

Consider the case of Michigan. In 1996, Michigan implemented a school finance reform that significantly increased state aid to low-spending school districts and limited spending increases in wealthier districts, which led to more equal spending across school districts. Using data on student performance on state tests in the years just prior and just after Michigan’s 1996 reform, Roy (2011) finds that there were learning gains in more disadvantaged districts, but the reforms “may have had a negative effect on student performance in the highest spending districts.” As shown below, any learning gains in Michigan during the 1996-2001 period on their state tests appear to have not translated to future performance on the NAEP.

The reforms undertaken in Indiana and Michigan were similar in that they both increased state aid to school districts and reduced disparities in spending across districts. But that is where the similarities end. Indiana also significantly increased choice in education for families and implemented both academic and financial accountability policies. Also, Indiana made it more difficult for wealthier districts to increase local spending—by making these spending increases more accountable to voters—but Michigan did not disallow these local spending increases. As shown previously, spending per student in Indiana public schools also declined significantly during the era of these reforms, by $977 per student. Nevertheless, Indiana students experienced learning gains that exceeded the national average in the years immediately after these reforms.

During this same time period, Michigan’s performance on the NAEP was mixed when compared to the national average—Michigan 4th graders experienced modest learning declines from 2007 and 2017 on reading and mathematics (-2 points in both), and learning gains for Michigan 8th graders exceeded the national average by one point in both subjects. Spending per student, adjusted for inflation, declined by $377 per student in Michigan during this time period—a significantly smaller decline than the $977 decrease experienced by Indiana public school students. Based on the comparison with Michigan, it would be difficult to conclude that the choice and accountability reforms were not related to the learning gains made in Indiana during this time period.

Finally, we want to underscore that we are able to evaluate only the entire suite of reforms implemented in Indiana and not any single feature of the reform package. Therefore, policymakers, educators, parents, and interested citizens should consider the package of reforms passed in Indiana and relate them to the K-12 policy landscape in their states.

Authors

Dale Chu is an independent consultant on education programs and policy. From 2009-2013, he served as the Assistant Superintendent for Innovation and Improvement at the Indiana Department of Education, where he helped to develop and implement all of the state’s key education reform initiatives. Dale is a Senior Visiting Fellow at the Thomas B. Fordham Institute, an education think tank in Washington, D.C., a board member for the Colorado League of Charter Schools, and serves on the President’s Advisory Council for Communities in Schools.

Ben Scafidi is a professor of economics and director of the Education Economics Center at Kennesaw State University. Previously, he served as the Education Policy Advisor to Governor Sonny Perdue, a staff member to both of Governor Roy Barnes’ Education Reform Study Commissions, and as an expert witness for the state of Georgia in school funding litigation.

The Johns Hopkins Institute for Education Policy is dedicated to integrating research, policy, and practice to achieve educational excellence for all of America’s students. Specifically, we connect research to the policies and practices that will ensure all children have access to intellectually challenging curricula, highly-effective educators, and school models that meet students’ diverse needs. By delivering the strongest evidence to the policymakers who set the course and the practitioners who teach and lead, we hope to serve the American children who enter our classrooms every day. Learn more at http://edpolicy.education.jhu.edu


Background


DeBoer, L. (2019, July 31). Personal interview.


Huston, T. (2019, August 1). Personal interview.


Kitchell, R. (2019, August 8). Personal interview.


