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State of Maine
ONE HUNDRED AND TWENTY-SIXTH LEGISLATURE
COMMITTEE ON TAXATION

June 5, 2013

Senator Dawn Hill, Senate Chair
Representative Margaret R. Rotundo, House Chair
Members, Joint Standing Committee on Appropriations and Financial Affairs

RE: LD 1496, An Act to Modernize and Simplify the Tax Code.

Dear Senator Hill and Representative Rotundo:

The Taxation Committee has spent the last few weeks and 5 work sessions considering the tax reform proposed in *LD 1496, An Act to Modernize and Simplify the Tax Code*. While the Committee unanimously voted ONTP, all members appreciate the work of the sponsors and believe it is important to share the perspectives conveyed during our deliberations.

For ease of reference, we have 3 categories representing our viewpoints on LD 1496. However, members are in different stages of personal consideration and the perspectives in this letter may not reflect a member's position or vote if further action is taken on any part of the proposal.

Perspective 1

Representatives Knight, Stanley, Libby, Marean and Brooks recommend that the Appropriations Committee give serious consideration to comprehensive tax reform as an alternative to a narrower one-time fix to the biennial budget. In our work on LD1496, we have refined a bipartisan, budget-neutral tax reform plan that is designed to draw an increasing share of tax revenues from non-residents, while lowering the state's income tax rate to 4 percent and relieving homestead property taxes.

The plan was calibrated, so that the fiscal note estimates are very close to budget neutral, relative to the Governor's budget proposal, while eliminating the property tax increases that are implicit in that proposal. That means that if the Appropriations

Committee can come to an agreement on a balanced budget that deals with everything in the Governor's budget proposal *except* the suspension of revenue sharing, and the elimination of the homestead exemption and circuit breaker programs, then this comprehensive tax reform package can be inserted as a *budget neutral add-on* that relieves property taxes rather than increases them.

Once fully phased-in, the plan is anchored by a \$50,000 homestead exemption for all Maine residents (up to 50% of their home's value) and a maximum income tax rate of 4% with most deductions and many credits eliminated.

The property tax reforms are phased in over two years. In FY2014, the "status quo" from FY2013 is restored, giving municipalities time to plan for the larger reforms. In FY2015, the full \$50,000 homestead exemption is implemented. The income tax reform is phased-in over three years; a 4.95% tax rate in 2014, a 4.5% tax rate in 2015, and the 4% tax rate in 2016. The phase-down in rate is necessary to maintain budget neutrality in each fiscal year of the phase-in period. But even in the phase-down, the plan does not increase the structural deficit in the general fund.

The plan also expands the sales tax base and raises a number of sales and excise tax rates, including the general sales tax rate. These provisions are what enable the plan to draw more revenues from non-residents. For residents, the plan has been designed with "fairness credits" that offset sales taxes paid by lower and middle income households, and that moderate the overall regressivity of sales and property taxes. The sales tax fairness credit is refundable up to \$400 for a single taxpayer and \$800 for a married couple, plus \$100 per dependent and \$100 per person age 65 and older. The circuit breaker program is converted to a property tax fairness credit on the income tax return. It is also refundable up to \$1000.

The preliminary distributional analyses on the bill are not as clear or as definitive as we had hoped, because they reflect a comparison of the reform with "current law," which assumes full 5% revenue sharing, full circuit breaker benefits, and the \$10,000 homestead exemption – none of which are funded in the Governor's budget proposal. However, we know from plan simulations that income taxes would be reduced for nearly all resident taxpayers. The homestead exemption will reduce property taxes on primary residences by an average of roughly \$500 statewide. And the sales tax fairness credits will offset increases in sales taxes for many resident families. While not perfect, we believe the bill is reasonably calibrated as it is currently drafted.

Most importantly, we think this is a rare opportunity for bold reform, and we encourage you to embrace that opportunity. Rather than tinkering, we recommend transformative tax reform. While the plan makes some very large changes to Maine's tax system, we eliminated from earlier versions those changes that were more difficult to define or administer. As structured now, Maine Revenue Services believes they can implement this plan, and have recommended only minor adjustments to the drafted statutory language, which is available on-line. We have attached a summary version of the restructured bill.

Perspective 2

Senator Haskell, Senator Millett and Representatives Goode, Tipping-Spitz and Moonen appreciate the thoughtful work that went into LD 1496 and support some of the concepts presented in this bill. However, we have concerns about how tax cuts are distributed, taxing necessities of life and whether the sales tax fairness credit can truly offset a regressive sales tax increase and broadened sales tax base.

It is common knowledge that LD 1496 came to the Taxation Committee late in the legislative session. The initial concept draft was not turned into legislative language until after the deadline for committee meetings. During the final week in May, committee members received initial analysis from Maine Revenue Service. While there are more opportunities for further analysis, some of the committee members opposed to moving forward with LD 1496 at this time were concerned about the resulting net tax cuts for various groups within the distributional analysis. Maine Revenue Service's analysis showed a significant tax cut for the top 1% of tax families, those making over \$324,000 adjusted gross income per year. Tax families with the lowest income are estimated to get a cut of just a few dollars. Projections for middle income tax families show a modest tax decrease for some and a tax increase of others.

Should members of the Joint Standing Committee on Appropriations and Financial Affairs give serious consideration to LD 1496, we encourage committee members to work to adjust the legislation in a way that ensures any reduction in taxes benefits middle and low income earners. Cutting taxes for those who earn more than \$324,000 while we are simultaneously cutting health care, retiree pensions and failing to meet our commitments to education does not make sense.

While the sales and property tax fairness credits attempt to mitigate any regressivity within the income tax and sales tax changes, we believe there are other ways to achieve property tax fairness without adding sales taxes to necessities. We share the goals of identifying opportunities within the sales tax code to export taxes to the wealthy and out of staters. Improving sales tax laws in this way is fair. We question the benefit of increasing sales tax on necessities of life, many of which are often used by Mainers and rarely used by out of staters. Adding a sales tax on food, funerals, haircuts and car repair services seem to cover items that are purchased with regularity by low and moderate income Mainers and we are unsure of the level to which they are exportable.

We believe that any proposal of this magnitude should have a public hearing on fully drafted statutory language and there just isn't enough time for that in this Session. We had a beneficial public hearing on a concept draft in mid-May. We are unable to have a public hearing on the language of the bill that we received in the last week of May. Should the ideas of LD 1496 become incorporated in the budget, we would encourage the Appropriations Committee to hold a public hearing.

Members of the public who testified against or neither-for-nor against the legislation often praised the bi-partisan support for LD 1496. Committee members

approached the bill with an open mind, and often echoed the praise of the work done to bring these new changes forward. As we worked through LD 1496, it became clear that there was also bi-partisan opposition to bringing LD 1496 forward for a vote in either chamber at this time.

Perspective 3

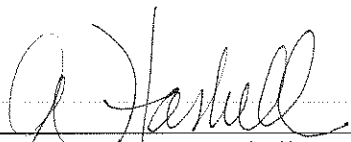
Senator Thomas, Representative Jackson and Representative Bennett would like to thank those who spent so much time on LD 1496. We believe it made the Tax Committee take a fresh look at how we raise enough money to fund government in Maine.

In the end the plan was too big for anyone to understand this late in the session. Not enough time has passed since the failed attempt to reform taxes 3 years ago that was defeated by a peoples veto. Many of us were a little skittish to tackle something so similar. We don't believe we need tax reform that is this drastic, but rather small incremental change is more in order. Also, we have serious concerns about the idea of high taxes on the necessities of life and will oppose any plan to implement them.

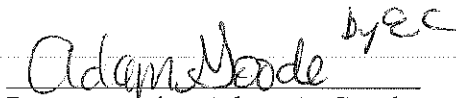
The best plan to reform taxes is to lower them. We are from the school that believes if we were to lower taxes in Maine we would see more economic growth and more government revenue. Just like many businesses can lower prices and increase volume. Other states have used this method to increase their standard of living. This plan is a huge tax increase that many of us think would be bad public policy, especially considering we are just beginning to recover from the worst recession in our lifetime.

The Taxation Committee members appreciate the opportunity to express our different viewpoints. Please feel free to contacts with questions.

Sincerely,



Senator Anne M. Haskell
Senate Chair



Representative Adam A. Goode
House Chair