Legislative BULLETIN

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Highway Fund Budget Impacts on URIP

On Thursday this week, the Transportation Committee continued its work on the FY 2010-2011 Highway Fund budget (LD 333). Of particular interest to municipal officials are the elements of the bill that impact state aid to municipalities for local roads, now referred to as URIP (Urban/Rural Initiative Program).

In 1999, the 119th Legislature enacted a bill that converted the then flat-funded Local Road Assistance Program into the fixed percentage-based URIP system. After months of negotiations, a group of municipal and state officials developed a funding proposal that focused state aid for roads on capital projects, only. Before URIP was enacted, municipalities could use state road funds for equipment and materials purchases, but with the advent of URIP, and in exchange for being required to use state road revenue on capital projects only, the funds dedicated to the municipal program were to be based on a fixed percentage of the revenue dedicated to the state for its highway and bridge program. Under this funding mechanism, 10% of the Department of Transportation (DOT) revenues used to improve and maintain state roads and bridges are now dedicated to local road assistance, or URIP.

With the enactment of this law ten years ago, municipalities forged a partnership with the state, which until this year has been completely honored.

Without communicating in any way with the municipal community, DOT included in its FY 2010-2011 budget a proposal to deappropriate $5 million from URIP funding in FY 2011, a 20% reduction.We have learned that it is apparently the case that DOT intends to replace the $5 million cut with the same amount of borrowed money if a DOT transportation bond is approved by the voters in November 2009.

On Tuesday this week, the Transportation Committee adopted the portion of the proposed FY 2010-2011 Highway Fund budget that would reduce local road assistance funding by $5 million in FY 2011. As a result of that vote, MMA sent an “action alert” to municipal officials asking them to contact members of the Transportation Committee regarding the URIP deappropriation. Concerned municipal officials from all corners of the state have contacted members of the Legislature on this issue.

In the action alert, we correctly stated that the bonding repayment proposal had not been articulated in the proposed budget. DOT has since provided a copy of its *MaineDOT Biennial Capital Work Plan*, which was published and posted

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Simplifying Revenue Sharing: Municipal Revenue Sharing Impacts

Embedded within the developing state budget, there will be language that is designed to simplify the administration of the revenue sharing program. The purpose of the language is to make revenue sharing easier to administer by both the state financial agencies that directly manage the program and the Legislature’s Office of Fiscal and Program Review. The creation of the “Rev. II” system in 2000, the 2% Efficiency Fund set-aside, and other changes this decade to the revenue sharing law have made the program difficult to administer and too complicated to easily calculate the tax and revenue sharing impacts within the state’s budgeting process.

The simplification plan is designed to be revenue-neutral; that is, it is designed to provide the same amount of revenue sharing over the next biennium that would be provided under the current system, given all the proposed cuts to revenue sharing that are being moved into the proposed state budget by the Appropriations Committee.

The major elements of the simplification plan are:

1. Under current law, the $100 million each year that is used to pay BETR reimbursement and Circuit Breaker benefits is not considered income tax revenue in the state’s General Fund and, therefore, 5.1% of that income tax revenue is not transferred to revenue sharing’s “Local Government Fund”. The placement of this revenue “over the line” and outside of revenue sharing occurred several years ago. Under this simplification proposal, that income tax revenue would once again be placed in the pool of state revenues against which revenue sharing is calculated. <u>That change, by itself, would add approximately $5 million a year to revenue sharing.</u>

2. In order to make that change “revenue neutral”, the revenue sharing percentage, which is now (at least technically) 5.2% of all state sales and income

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on its website on April 2, 2009. Found on page 5 of the plan is the statement that "*bond funding in this Work Plan also provides $5 million to support the state's Urban-Rural Initiative Program (URIP*)." What this report fails to mention is that the these borrowed funds are not intended to supplement the URIP program; instead, they are meant to merely replace the $5 million that is being cut out of the URIP program by the Legislature at DOT's recommendation.

In addition to this proposed cut to URIP revenue in 2011, state revenue reprojections show that in FY 10, URIP funding will be down by $2.9 million relative to previous projections. In 2011, URIP funding is projected to be below projections by $1.6 million. In summary, due to the reduction in fuel tax revenues, over the next two years state funding for local roads will be reduced by $4.5 million merely as a result of the negative economy.

Since funding for URIP is based on the revenue dedicated to DOT for its highway and bridge programs, municipal officials understand that when Highway Fund revenues are down, reductions in URIP funding will follow. What is difficult to understand is why the state needs to take an additional $5 million of local road money with the promise to replace it with bond revenue.

When municipal officials decided to support the URIP program in 2000, it was in large part due to the fact that local funding would be directly tied to a fixed percentage of state highway funding. If the state believes that the policy should be revisited, that would be one thing, but simply taking the revenue without having the policy discussion demonstrates the serious unpredictability of state financial support systems

Although the Transportation Committee reconvened on Thursday of this week to work on the Highway Fund Budget, it did not revisit the URIP issue. The Committee's next Highway Fund work session is scheduled for today (Friday, May 15th).

MMA will continue to keep municipal officials apprised of the Transportation Committee's work through action alerts and updates in the *Legislative Bulletin*. Please stay tuned.

Legislative Bulletin

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REVENUE (cont'd)

tax revenues, would be reduced to a straight 5%. That change, by itself, reduces revenue sharing by approximately $5 million.

3. The 2% transfer of revenue sharing funds to the Local Government Efficiency Fund would be repealed, starting immediately. That change, by itself, adds about $2.6 million a year to regular revenue sharing. The Legislature, however, will take that money over each year of the next biennium because law enacted last year already diverted that money to the General Fund. Those funds would be released back to revenue sharing beginning in FY 2012.

4. The so-called "Revenue Sharing I" and "Revenue Sharing II" split would no longer be calculated by the complicated and manipulated "cap-and-overflow" system. Instead, beginning in FY 2010, the Rev I share would be 85% of all distributable revenue sharing and the Rev II share would be 15%. The 85:15 ratio represents the ratio of distribution under current law after the most recent reprojection. The ratio is proposed to phase to an 80% (Rev I): 20% (Rev II) ratio over a five-year period to reflect where the ratio is currently projected to be five years from now under current law.

5. Outside of the 85:15 split, the "BETE" law annual transfers to the Rev II distribution would continue. Those transfers, designed to cover communities with higher-than-average personal property bases in light of the personal property exemption enacted in 2006, are $2 million in FY 2010 graduating up to $4 million in FY 2014.

It would appear that the Office of Fiscal and Program Review, which designed the simplification plan, has done a good job of simplifying the revenue sharing law while holding the fiscal impacts very close to pure neutrality. "Revenue neutrality" means that there is no meaningful financial benefit in this plan for the municipalities, but the simplification should result in a few positive outcomes.

• Predictability of cash flow. Under this system, every municipality will get a revenue sharing check each month of the year, and there will no longer be those end-of-the-year uncertainties.

• End of Efficiency Fund diversion. The totally inappropriate diversion of revenue sharing through the Local Government Efficiency Fund and then back into the General Fund will be discontinued starting in 2012.

• Ease of projection. It will be much easier for all concerned (State Treasurer, MMA, others) to forecast revenue sharing projections after each new forecast of state revenue by the Revenue Forecasting Committee.

Treasurer to increase administration fees. For all the benefits of the simplification plan, there is some irony in the fact that the State Treasurer is intending to subtract between $10,000 and $25,000 from actual revenue sharing distribution to the towns and cities in FY 2010 to cover "software upgrades" that are allegedly necessary to implement the simplification. MMA is able to calculate revenue sharing distribution by means of a simple Excel spreadsheet system. For reasons that are unclear, the state needs an expensive software upgrade.

18.5% Cut to Revenue Sharing: town-by-town impacts. The process of detailing the revenue sharing simplification proposal also provided some clarity to the cumulative revenue sharing cuts that have been proposed by the Governor and accepted by the Appropriations Committee.

In summary, the two revenue sharing cuts have been consolidated into a single "transfer" whereby a specific amount of revenue would be transferred out of the revenue sharing account ("Local Government Fund") and into the state's General Fund each year. That amount of money is approximately $25

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Tax Committee Votes to Increase Veterans' Property Tax Exemption

On Tuesday this week the Tax Committee voted nearly unanimously "ought to pass" on LD 71, *An Act to Raise the Property Tax Exemption for Veterans.* As printed, LD 71 would increase the value of the veterans' property tax exemption from $6,000 to $7,000. As amended by Committee, the bill would increase the value of the veterans' exemption each year by 5%, so that the exemption would be valued at $6,300 on April 1, 2010 and $6,615 on April 1, 2011, and so on.

The fiscal impact of the amended bill would be about $100,000 a year to the state in increased municipal reimbursement to cover 50% of the lost tax revenue, as required by the Constitution. The other 50%, obviously, would be picked up by the municipalities to the tune of $100,000. The state's fiscal impact would not be felt during this biennium, however, because several years ago the Legislature "pushed" the state's obligation to reimburse for the veterans' exemption into the subsequent fiscal year, a year after the actual financial impacts are experienced at the municipal level. (Note: Maine's Constitution, which calls for "annual reimbursement", does not seem to countenance this type of delay.) In any event, the fiscal note on LD 71 will reflect an increased state financial obligation outside the next biennium, in FY 2012, when a newly-elected legislature will be stuck with dealing with it.

The Committee's debate on LD 71 was interesting. The proponents of the increased exemption offered two arguments.

The strategic argument was that even though these are tough economic times and the state obviously has no money to pay for expanded benefits, a bill with a relatively small fiscal note — or a fiscal note that does not impact this budget biennium — might have a chance of sneaking through the "Appropriation's Table" funding process. In high-low poker, the argument goes, a low hand is worth a shot.

The other argument is that because the Legislature will be cutting back so significantly in the areas of revenue sharing, homestead exemption, circuit breaker benefits, school subsidy, etc., property taxes are bound to increase and so the retired veterans should receive an expanded benefit to soften the blow. (That the expanded benefit to the veterans works to exacerbate the negative property tax impact on everyone else was not mentioned.)

Representative Linda Valentino (Saco) expressed an alternative point of view. According to Rep. Valentino, it would be entirely incongruous to approve deep, across-the-board cuts in property tax relief programs with one hand, and then with the other hand approve an increase in property tax benefits of any amount for just a single constituency. (It should not go unnoticed that the veteran's exemption was increased by a full 20% just last year.)

With respect to the issue of legislative responsibility, Rep. Valentino suggested that there was something not right about taking an easy vote for a favored constituency at the Tax Committee level, thereby pushing the responsibility for true fiscal prioritization either to the Appropriations Committee or, given the pushed-out fiscal note, to a future legislature not-yet elected.

After taking into account those observations, the Committee nonetheless voted overwhelmingly in support of the increased property tax benefit, with only Rep. Valentino and Rep. Mark Bryant (Windham) voting not to advance a bill that cannot be responsibly funded.

State Budget Update: Teachers' Retirement

As the Appropriations Committee works to finalize the state budget, amendments are offered by various Committee members, either individually or in teams, to help close the budget gap. After being reviewed, those amendments are either "moved in" or "moved out" of the budget document according to votes of the full Committee. From an observer's point of view, the tail end of the process, when the ad hoc amendments are flying, represents the least predictable or organized part of the budget development process.

On Thursday this week, the Committee apparently "moved in" an amendment to the provision in the budget regarding the creation of a "streamlining commission". Two weeks ago, the Governor submitted a number of budget proposals that were designed to close a $440 million hole in the biennial budget created by the most recent reprojection of state revenues. One of those proposals was to create a commission made up of Appropriation Committee members and state agency commissioners that would be charged with finding $37 million worth of savings over the biennium by streamlining the operations of state government.

The Appropriations Committee's new amendment to that proposal is to also charge the commission with the new specific task of identifying what amount of the state's contribution to school teacher retirement premiums should be included in the calculation of the Essential Programs and Services (EPS) school funding model. If that occurs, obviously, the costs of funding some of the teacher retirement premiums, for the so-called "normal costs" and possibly the "unfunded actuarial liabilities", would be transferred from the state level to the property tax level.

No rational school system in modern times would establish a retirement system along the lines of the defined-benefit model which the Legislature has been providing for school teachers. The size of the unfunded liabilities that have accrued under that plan are breathtakingly enormous, in the multi-billion dollar range. This new charge to the "streamlining commission" to determine what amount of that financial liability, "if any", should be moved into the EPS school funding model represents a step toward shifting to the property taxpayers the financial liabilities associated with a benefit the Legislature chose long ago to bequeath to a favored constituency.

Legislature Supports Firefighter's Rebuttable Cancer Presumption

On Thursday, the House of Representatives decisively voted to support LD 621, *An Act Allowing Workers' Compensation Benefits for Firefighters Who Contract Cancer.* The bill will make it much easier for certain firefighters who contract cancer to receive workers compensation benefits. Currently, firefighters with cancer are able to receive workers compensation benefits if they can establish that the cancer was caused by their employment as a firefighter.

Based upon all available evidence, no firefighter in Maine has ever done so. The stated purpose of LD 621 is to change that fact by flipping the 'burden of proof' to the employers – Maine's cities and towns – to prove that firefighting did not play a material role in the firefighter's development of cancer. A very difficult legal challenge.

Conflicting evidence was presented regarding the cost of this bill to the legislature. The primary argument put forth by dozens of firefighters, aided by lobbyists from the Workers Compensation Board (even though the Board took no position on the bill), was that the bill will have no fiscal impact on municipalities. This simply doesn't pass the straight face test. Firefighter lobbyists didn't spend hundreds of hours lobbying this bill for no benefit. Their argument was that since other states have had this law, and since MMA did not produce evidence of cost increases from these other states, the law must have no impact.

MMA did provide unrefuted evidence that this bill has cost municipalities in California millions of dollars where the law has been in place for two decades.

In addition, the Legislature has created an Office of Fiscal and Program Review to assess the impacts of legislation. This Office received all the evidence put forward by both sides on LD 621 and it concluded that this bill will have a "significant" cost impact to municipalities statewide.

Legislators who would have you believe that they received no evidence that LD 621 would impose additional municipal costs apparently did not read the fiscal note that was attached to the bill. The Office the Legislature created to provide them with information about the fiscal impact of bills they review made it explicitly clear that this bill will increase municipal costs. Failing that, simple common sense should have been enough to inform them that this bill will cost municipalities money.

If it was a bill that affected the state's treasury, it would most certainly not have been enacted.

It is one thing during these tough economic times for municipalities to experience very significant cuts in state financial support.

To have additional costs and legal obligations imposed on the property taxpayers on top of that is something else altogether.

REVENUE (cont'd)

million in each year of the biennium. That sum represents the so-called "15% cut" to revenue sharing, as well as the 2% set-aside originally intended for the Local Government Efficiency Fund which the Legislature has been taking for the General Fund ever since the Efficiency Fund was adopted by the voters in 2004. Because the "15% cut" to revenue sharing was calculated before state revenues were re-projected downwards, the $25 million annual "transfers" out of municipal revenue sharing actually represent an 18.5% cut to revenue sharing each year of the biennium compared to what would be provided if a 5.1% of state income and sales tax revenues were distributed to the municipalities… distributed simply, in the straightforward way the revenue sharing program used to be distributed before the program was overcomplicated and manipulated over the course of this decade.

MMA's Kate Dufour has prepared a town-by-town projection of revenue sharing distributions for FY 2010 based on the most recent re-projection of state revenues and the distribution methodology associated with the revenue sharing simplification plan described above. The spreadsheet compares the projected FY 2010 revenue sharing distribution with the revenue sharing distribution that was originally estimated to be distributed to each municipality during the current fiscal year (FY 09).

That spreadsheet is now posted on MMA's website (www.memun.org).