

Tax Reform Hangs In Balance Between House and Senate

For the municipalities the legislative session began six months ago with school reform and it will end next week with comprehensive tax reform.

Or it won't.

Ten days ago a well balanced and comprehensive tax reform package was reported out of the Taxation Committee with very strong, bipartisan "ought to pass" recommendations. The tax reform package comes in two parts — a statutory tax reform plan (LD 1925) and a companion bill that contains three proposed constitutional amendments (LD 1819). A complete description of the tax package is provided in a separate article in this edition of the *Legislative Bulletin*.

On Wednesday this week, the statutory plan received a big boost in support from the House when by a vote of 87-49, Maine's State Representatives endorsed the long overdue modernization of the state's tax code...a tax system that has not undergone what on the municipal level would be called a "revaluation" in 40 years.

The House support for the statutory reform package was counter-matched by its disinclination to approve the companion constitutional amendments. In particular, the House rejected the constitutional amendment to require "supermajority" House and Senate votes before enacting any state tax rate increases. The House also jettisoned the proposed amendment to authorize local option sales taxes to fund property tax relief.

As might be expected, the day following the House vote was marked by

a State House rally staged by the tax reform opponents including the Maine State Chamber of Commerce, nearly every contract lobbyist in Augusta and various other opponents such as ski resort employees who engaged in some summer slaloming among the throngs on the third floor of the Capitol sporting "NO TAX SHIFT" stickers on their lapels.

The entire matter is now squarely before the Senate, but the momentum of the bill was slowed down on Thursday when there were reportedly discussions occurring between some members of legislative leadership and the Governor's Office. Although the Tax Committee has been developing a reform package for five months, the

Governor's position on tax reform is not publicly known.

As was pointed out on the floor of the House during Wednesday's debate, this tax reform package is not "perfect" because no comprehensive legislation that fundamentally restructures the status quo can be entirely "perfect", but this is the most thoughtfully developed, carefully crafted and principle-based tax reform package that might ever be presented to the Legislature, and if it is ultimately rejected, the realistic chances of ever enacting comprehensive tax reform sink to zero.

Municipal officials supporting comprehensive tax reform should redouble their efforts to communicate to their legislators this weekend.

Final Vote on Informed Growth Act Imminent

On Thursday this week, the Legislature nearly completed its work on LD 1810, *An Act to Enact the Informed Growth Act*. Generally speaking, the bill prohibits municipalities from issuing land-use permits for certain large-scale retail development projects if the projects cause "undue adverse economic or community impact." As detailed in the June 8th edition of the *Legislative Bulletin*, the community-impact element of the mandatory study focuses on the impact the proposed development will have on municipal

services, such as traffic, public safety, sewer infrastructure, etc. The economic-impact element of the study focuses on such issues as supply and demand of the proposed development in the regional marketplace, the number of jobs created and lost, the salaries and fringe benefits of those jobs, etc.

While both the House and Senate agree on the general purpose of the Informed Growth Act (IGA), the version of the bill supported by the House is

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The Tax Reform Package

General overview. The proposed legislation is the product of five months of labor by the Taxation Committee. Throughout this process, the Tax Committee set a very positive example of how any group of policy makers might engage in a major public policy deliberation such as tax reform. The process could not have been more careful, deliberative, open, thoughtful and bipartisan. It was so bipartisan, in fact, it slipped at some point into nonpartisanship.

The tax reform plan provides a revenue-neutral package that moves Maine's tax code from its heavy reliance on Maine residents' income and property values and "exports" \$140 million of that annual burden onto non-residents. Within the overall revenue neutrality of the package, the relief to Maine residents is provided primarily by reducing the income and property taxes that Mainers pay, and then covering those reductions in state revenue by expanding the base of the sales tax (which both residents and non-residents pay) and by increasing the rate of the Real Estate Transfer Tax, which is also assessed against non-residents in no small measure.

This plan gives the state a chance to take some tax burden off Maine's residents using sound tax policy principles that are actively used by other states to reduce the burden on their residents.

Here are the details of the statutory plan (LD 1925).

Income Tax. The centerpiece of

the income tax change is a significant reduction of the highest marginal income tax rate and a simplification of the entire code whereby all exemptions, deductions and existing credits are redesigned.

The income tax changes reduce this line of state revenue by approximately \$190 million a year.

Details. The current bracketed rate structure with the top rate at 8.5% is converted to a flat rate structure at 6%. Reducing Maine's top marginal income tax rate has long been a goal of the business community and tax policy experts who believe the high income tax rate is a detriment to business relocation to Maine.

Under the 6% flat rate, the current state income tax deduction system is redesigned to preserve some progressivity. Taxpayers are given a choice between two options.

Option 1. A refundable tax credit is created for all taxpayers equal to \$750 for single filers, \$1450 for joint filers and \$1000 for head-of-household filers, and the credit is increased by \$125 for each exemption. The tax credit begins to phase out when the income level reaches a certain point (e.g., \$67,500 for a joint filers).

Option 2. The taxpayer may deduct 10% of the federal adjusted itemized deduction as adjusted for state purposes, with a cap of \$1300 for single filers, \$3000 for joint filers, and \$2000 for head-of-householders.

Property Tax. There are four elements to the property tax relief strategy: (1) doubling the Homestead exemption, (2) expanding the Circuit Breaker program, (3) supplementing the revenue sharing program by returning some sales tax revenue to the municipalities where the sales tax revenue was generated, and (4) creating a property tax deferral program for the elderly. The cost of the total property tax package is approximately \$50 million a year.

Homestead Exemption. The centerpiece of the property tax relief component of the Committee's reform plan

is a doubling of the Homestead property tax exemption from \$13,000 to \$26,000, which would be 50% reimbursed by the state. As is noted below under the description of the constitutional amendments, the voters in municipalities would be given the choice (if the constitutional amendment is adopted) to opt-out of the unreimbursed half of the homestead exemption. If the "opt-out" is taken, the homestead exemption would be \$13,000, fully reimbursed.

Circuit Breaker Expansion. The "Circuit Breaker" property tax and rent rebate program would be expanded both in its breadth (i.e., how many people it serves) and in its depth (the size of the benefit). Under current law, Circuit Breaker benefits kick-in when an applicant's property taxes (up to the first \$4,000) begin to exceed 4% of household income. At that point, 50% of the applicant's property tax bill within the range of 4%-to-8% of household income is provided as a benefit. If the property tax bill exceeds 8% of household income, a second trigger is pulled and the applicant receives 100% reimbursement for the portion of the property tax bill that exceeds 8% of household income, up to a maximum benefit of \$2,000.

Under this legislation (with changes underlined), Circuit Breaker benefits would kick-in when an applicant's property taxes (up to the first \$5,000) begin to exceed 3.5% of household income. At that point, 50% of the applicant's property tax bill within the range of 3.5%-to-7% of income would be provided as a benefit. 100% reimbursement would be provided for that portion of the property tax bill that exceeds 7% of household income, up to a maximum benefit of \$2,500.

Sales Tax Revenue to Municipality of Origin. The tax reform plan also initiates a sales tax-based supplement to the municipal revenue sharing program. For the purposes of this program,

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TAX REFORM (cont'd)

Fiscal Year 2009 is the base year and during that year Maine Revenue Services is directed to keep track of the sales taxes collected within each municipality. In the subsequent fiscal years, each municipality would become eligible to receive 10% of the sales tax revenue generated within that municipality over the base-year amount.

Elderly Tax Deferral Program.

The final property tax relief strategy in the tax reform plan is the reconstitution of the Elderly Tax Deferral Program that operated in the late 1980s and early 1990s until it was discontinued by the Legislature in 1993. Under the Elderly Tax Deferral Program, any Maine resident eligible for the Homestead property tax exemption may apply for and receive a property tax deferral that would be administered by the state. After completing the application, the state would pay the applicant's property taxes (or whatever share of the property taxes the applicant wanted to defer), and the state would assume a lien on the applicant's estate to cover the value of the deferred taxes at a flat 6% interest rate. Under this type of deferral program, no elderly person on a fixed income needs to fear losing his or her primary residence because of escalating property valuations.

In an apparent companion piece to the Elderly Tax Deferral Program, another provision of the bill would remove the tax lien foreclosure process on the municipal level for any homesteader 65 years or older who has lived in the homestead for at least 10 years. In other words, all homesteaders at least 65 years of age (with 10 year tenure) would be able to not pay their property taxes and the ramifications would simply be an ongoing aggregation of the lien (apparently at customarily-calculated interest rates) which could only be foreclosed at the time the property is transferred by deed or the homesteader dies.

Sales Tax. As has been noted, the income tax relief costs the state \$190 million a year and the property tax relief costs the state \$50 million a year. Under this tax reform plan, that relief – totally concentrated on Maine income

taxpayers and Maine property taxpayers – is paid for by expanding the state's sales tax base and Real Estate Transfer Tax in the following ways:

The applicable sales tax rate would be applied to the following purchases:

- Non-staple “prepared foods”, soft drinks and candy
- Meals, lodging and car rental purchases by non-profits
- Vending machine sales
- Newspapers and magazines
- For-profit summer camps
- Telecommunication, cable and satellite t.v. services
- Transportation, delivery and common carrier services
- Personal care services
- Personal property and certain real property services
- Installation, repair and maintenance services
- Amusement and recreation services

For each of the “services” included above, detailed lists are written into the law to identify the actual services covered.

For example, “personal care services” are defined as “*services related to the human body including hair care and maintenance, body piercing, tattooing, tanning, massage, nail care, foot care, reflexology, spa treatments and electrolysis; memberships or fees paid for fitness training, health clubs and spas; and elective cosmetic medical procedures.*”

“Personal property services” are defined as “*services related to personal property, including dry cleaning; laundry and diaper services not including self-service laundry services; embroidery and monogramming; car washing; pressure cleaning and washing; pet services such as exercising, sitting, training, grooming and boarding for nonmedical purposes; picture framing; domestic services, including house cleaning, painting, papering and furniture and rug cleaning; janitorial services; interior decoration; meal preparation, butchering; art restoration; and warehousing and storage, including storage rental units, warehouse space rental, moving services, vehicle towing, boat mooring and storage of recreation equipment.*”

There are similarly detailed definitions of “amusement and recreation services”, “installation, repair or maintenance services”, “real property services”, etc. As is evident, the Taxation Committee crafted the definitions of each taxable service very carefully.

Beyond repealing certain sales tax exemptions, the sales tax plan would also increase the meals and lodging sales tax rate from 7% to 8% and the short-term auto rental rate from 10% to 15%.

Finally, the Committee plan would increase the Real Estate Transfer Tax (RETT) rate by applying a graduated range of rates depending on the sales value of the property. The current RETT rate is \$4.40 per thousand dollars of sales value. The graduated RETT rates under the tax reform plan would be:

Primary Residences:

- First \$250,000 of value — \$6/thousand
- Next \$250,000 of value — \$8/thousand
- Next \$500,000 of value — \$10/thousand
- Over \$1,000,000 in value — \$15/thousand

Non-primary residences:

- Less than \$1 million in value — \$10/thousand
- \$1 million or more in value — \$15/thousand

Non residential property/open land — \$10/thousand

Proposed Constitutional Amendments (LD 1819). In addition to the statutory tax reform plan as described above, the overall package includes a companion bill that includes three proposed constitutional amendments. Although the companion bill will be presented to the Legislature as a single bill, if it receives the necessary two-thirds “supermajority” vote from both the House and the Senate, the proposed constitutional amendments would be presented to the voters in November as three ballot questions.

The three proposed constitutional amendments would:

- Require a 2/3 “supermajority” vote in both the House and the Senate in order to increase the income tax

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DOE Sets Regional Meeting Schedule

What follows is a reproduction of the Department of Education’s schedule of school regionalization/consolidation meetings. As enacted by the Legislature last week, the school consolidation plan requires the Department to organize and hold informational meetings in each of the state’s 26 Career and Technical Education regions by July 15, 2007.

With fast approaching deadlines, it is important that

municipal and school officials and members of the general public are made aware of this opportunity to learn about the regionalization/consolidation process and provide input and feedback to the Department of Education officials who are presenting this information. We encourage you to make this schedule available to your residents.

This schedule and other information is available on the DOE’s website: www.maine.gov/education

Date	Time	Location
Monday, June 18	7:00 p.m.	Cony High School/Performing Arts Center, Augusta
Monday, June 18	7:00 p.m.	Lake Regional High School / Auditorium, Naples
Tuesday, June 19	7:00 p.m.	Deering High School/Auditorium, Portland
Tuesday, June 19	7:00 p.m.	Messalonskee High School/Performing Arts Center, Oakland
Wednesday, June 20	7:00 p.m.	Biddeford Middle School/Auditorium, Biddeford
Wednesday, June 20	7:00 p.m.	Caribou High School/Performing Arts Center, Caribou
Thursday, June 21	7:00 p.m.	Bangor High School/Peaks Auditorium, Bangor
Thursday, June 21	7:00 p.m.	Brunswick High School/Crooker Theater, Brunswick
Thursday, June 21	7:00 p.m.	Fort Kent High School/Gymnasium, Fort Kent
Tuesday, June 26	7:00 p.m.	Mattanawcook Academy/Cafetorium, Lincoln
Tuesday, June 26	7:00 p.m.	Oxford Hills Comprehensive High School/Auditorium, Oxford Hills
Wednesday, June 27	7:00 p.m.	Dexter Regional High School/Cafetorium, Dexter
Wednesday, June 27	7:00 p.m.	Mt. Valley High School/Auditorium, Rumford
Wednesday, June 27	7:00 p.m.	Presque Isle High School/Auditorium, Presque Isle
Thursday, June 28	7:00 p.m.	Woolwich Central School/Gymnasium, Woolwich
Thursday, June 28	7:00 p.m.	Holiday Inn, Ellsworth
Thursday, June 28	7:00 p.m.	Waldo County Tech Center – Region 7, Waldo
Monday, July 9	7:00 p.m.	Sanford Memorial Gymnasium, Sanford
Monday, July 9	7:00 p.m.	Westbrook High School/Auditorium, Westbrook
Monday, July 9	7:00 p.m.	Miller Arena, Houlton
Tuesday, July 10	7:00 p.m.	Calais High School/Cafetorium, Calais
Tuesday, July 10	7:00 p.m.	Rockland District High School/Auditorium, Rockland
Wednesday, July 11	7:00 p.m.	Mt. Blue High School/Auditorium, Farmington
Wednesday, July 11	7:00 p.m.	UM Machias/Science 102, Machias
Thursday, July 12	7:00 p.m.	Lewiston Middle School/Auditorium, Lewiston
Thursday, July 12	7:00 p.m.	Skowhegan Area High School/Auditorium, Skowhegan

GROWTH (cont'd)

currently in conflict with the version supported in the Senate.

As supported by the House, the bill attempts to mitigate the “one-size fits all” nature of LD 1810 by enabling municipalities to adopt locally tailored economic and community impact study ordinances. A municipality that adopts a version of the IGA would not be required to apply the specific procedures of the Informed Growth Act detailed in LD 1810. It appears that the intent of the amendment is to provide municipalities with some level of control over the impact study process. Although it is unclear how a municipality would actually trigger the exemption standard, we assume that a section of the municipality’s land use ordinance would need to closely resemble or be at least as strict as the system detailed in LD 1810. Although some members of the Senate during the debate on LD 1810 questioned how a community would trigger the exemption, the question was left unanswered. Without any clarification, it appears that the standard used to trigger the exemption would be first decided by the municipality and ultimately decided by the courts.

As supported by the Senate, the bill includes the exemption provision found in the House version as well as an additional waiver option. As provided in the Senate-amended version of LD 1810, by a vote of the local legislative body (i.e., council or town meeting) a municipality would be authorized to waive the need to conduct the mandated impact study on an application-by-application basis. In other words, the council or the town meeting would be authorized to vote to exempt a particular application from the LD 1810 impact study requirement.

The ball is now in the Senate’s court. The Senate appears to have two procedural options available: 1) to “insist” that the House adopt the Senate’s version of LD 1810; or 2) to “recede” from its position and support the more limited local flexibility that characterizes the version of LD 1810 adopted by the House. Neither version of the bill currently before the Legislature is as

administratively straight forward and respectful of community-based decision making as the “opt-in” approach supported by municipal officials, which would have written the IGA process into law and allowed any community that deems the use of that process necessary to adopt the system “by reference”. That being said, the municipal community supports the Senate’s version of LD 1810, as it provides municipalities with more flexibility when trying to implement the state mandated “Informed Growth Act” locally.

TAX REFORM (cont'd)

rates, sales tax rates and motor vehicle excise tax rates;

- Authorize the voters at the mu-

nicipal level to provide additional property tax relief by implementing a local option sales tax, with a strict requirement that the local sales tax revenue be used to reduce property taxes; and

- Authorize the voters at the municipal level to decide whether to accept only the fully-reimbursed half of the homestead property tax exemption or the full exemption with the 50% state reimbursement.

- As noted in the companion article regarding the present status of the tax reform debate, the House voted on Wednesday to strip out the first two proposed constitutional amendments and so LD 1819, as now amended, will go to the Senate with just one proposed constitutional amendment, authorizing municipalities to “opt out” of the unreimbursed homestead exemption.

Bulletin Incorrectly Identified Sponsor

Last week’s *Legislative Bulletin* incorrectly identified the sponsor of LD 172, *An Act to Increase the Property Tax Exemption for Veterans* as Senator Richard Nass (York Cty.). The actual sponsor of the bill was Representative Joan Nass (Acton). LD 172, which was incorporated into the state budget bill and has now been enacted into law, increases the



general veterans’ property tax exemption, currently a \$5,000 property tax exemption, to \$6,000 effective on April 1, 2008.

Our apologies to Representative Nass.