

## MMA's Structural Tax Reform Proposal

There is a bill being proposed by Governor Baldacci and some members of legislative leadership that would prospectively repeal the personal property tax. Governor Baldacci's version of that bill is LD 1660. A new version of essentially the same bill, re-authored by some legislative leaders, will soon be printed and it will have an "LD" number in the 2000 series. For the purposes of this article, we will refer to the bill that repeals the personal property tax as LD 1660, but municipal officials should be aware that the old wine of LD 1660 is being put into a new bottle. In a couple of weeks we may be talking about a different bill by number...but it's the same old wine.

Repealing a major part of the municipal tax base prospectively tends to mask the negative impacts on the short term. The longer-term impacts are quite evident, however, because the 10-year life of the Business Equipment Tax Reimbursement program (BETR) creates a living model.

If LD 1660 had been enacted ten years ago instead of BETR, and no reimbursement revenues were provided to the affected towns and cities, the aggregate annual municipal tax revenue loss would be approaching \$80 million today – the annual BETR price tag. In ten more years, that annual loss would be twice as much – in the \$150 – \$160 million range. Maine's Constitution provides that municipalities are entitled to 50% of their property tax losses whenever the Legislature creates a new property tax exemption, so the municipal revenue losses under LD 1660 would likely be \$40 million a year ten years out and nearly \$80 million a year in lost tax revenue 20 years out.

LD 1660 contains two statutory re-

imbursement systems designed to supplement the constitutional 50% reimbursement for the first several years after the exemption, as the municipalities "adjust to" or "absorb" their losses. Few people

believe the statutory reimbursements will be honored over time.

LD 1660 is definitely a bad deal for municipal government and the non-in-

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### Tax Reform Fizzles

MMA's "Question 1A" initiative was called *The School Finance and Tax Reform Act of 2003*. By its design, the initiative was supposed to require a sharp increase in state funding for K-12 education which, in turn, would compel the Legislature to engage in comprehensive, revenue-neutral tax reform.

The Legislature responded with LD 1, which phases in the increases to education aid over a four-year period and establishes the spending limitation systems which go hand-in-hand with tax reform. Unfortunately, tax reform itself was not included in the Legislature's package. By phasing in the required increases for school aid over a four-year period, the Maine's lawmakers avoided having to redesign the state's tax code.

A number of well-meaning tax reform efforts were introduced to this Legislature over a year ago, during its First Regular Session. The Taxation Committee spent a considerable amount of time last session working on those bills, and one of them – LD 1595 by number – emerged from the Committee on a party line vote toward the end of the session last year. After a brief but robust debate in the House one evening late last spring, LD 1595 was sent back to Committee where it and the three other "reform" bills were "carried over" into this Second Regular Session.

On Wednesday this week, the Taxation Committee snuffed them out.

For all of that effort, just one tangible idea emerged. On what appears to be another party line vote, the Taxation Committee is considering putting forward an advisory referendum that would go out to the voters next November. The referendum ballot would include a simple yes-or-no question that would read:

*Do you favor the elimination of certain sales tax exemptions in order to reduce income and property taxes in a revenue neutral manner?*

Advocates of this proposal on the Tax Committee believe that if the voters support this question with a 'yes' vote, it will give the Legislature the necessary directive to get the job done. With the question before the voters during the political campaign season, the argument goes, the newly-elected legislators will come into the 2007 legislative session with a renewed sense of obligation to get the task done and a lot of locally-provided input about the specific shape of a tax reform package.

Tax Committee members opposed to the idea argued that the question lacks the necessary specifics for the voters to make an informed judgment and that the Legislature shouldn't need to be constantly directed to accomplish tax reform. If the need for tax reform is so great, this argument goes, the Legislature should merely do it and not keep polling for support from the electorate.

## REFORM (cont'd)

dustrial taxpayers that pay for municipal, school and county services with their property tax payments. Some towns may think they're off the hook with respect to this proposal because they don't have much personal property in their tax base. Those towns are mistaken. County taxes and school aid are affected not only by your town's valuation *but also by the relative change in valuation of every other town and city in the county or state*. When you pull billions of dollars of taxable value out of the aggregate municipal tax base, as LD 1660 would do, the negative impacts are felt by each and every municipality, even those that are presently taxing very little personal property.

With that background, and as discussed in last week's edition of the *Legislative Bulletin*, a working group of municipal officials was convened by MMA for the purpose of responding to a request from legislative leadership to craft a way to enact the exemption in a way that would not harm the municipalities. "Harming the municipalities" is a term that more than anything else means not causing a shift in property tax burden from the newly exempted property owners (typically large manufacturing facilities) to residential and small business property taxpayers.

Here is a description of the plan developed by the MMA working group. The MMA proposal can be divided into two parts.

**Scope of the exemption.** First, the MMA plan would break from the all-inclusive nature of the personal property that would be made exempt by LD 1660. Over time, almost all personal property

would become exempt under the Governor's proposal because LD 1660 relies on the sweeping eligibility of the BETR program. In contrast, the MMA proposal would target the tax exemption to real manufacturing machinery and equipment, high-tech industrial property, the personal property used by the state's natural resources-based industries and the type of business and industrial uses already targeted by the Pine Tree Zone program.

The core argument of the proponents of LD 1660 is that a sweeping tax exemption is necessary to convince manufacturing industries to locate in Maine rather than elsewhere. That argument doesn't work for:

- retail chain stores like WalMart, Target, Rite Aid, etc.;
- chain restaurants like Pizza Hut, Olive Garden, Arby's, MacDonalds, etc.;
- supermarkets like Hannafords or Shaws; or
- with respect to the personal property inventories of law firms, accounting firms, professional offices, mail packaging centers, and so on.

None of those businesses are making locational decisions on the basis of property tax obligations; indeed, they generally promote themselves in a community because their presence will lift some local burden off the residential tax base. LD 1660 would do away with all that.

When the BETR program was created, the 1995 Legislature seemed to accept the idea that the state should automatically reimburse the personal property taxes paid by almost any business, whether it was a major industrial facility or a corporate law office or a national big box retail chain. If the state wants to reimburse those retail and service-oriented businesses for their property tax liabilities, that's the state's business. Municipal officials, however, don't support doling out unsolicited tax breaks to national chain retailers, law firms and lobbying firms, the owners of soft drink and snack vending machines, etc. just so the residential taxpayers can pick up the slack.

**Managing the exemption.** The major goal of the MMA proposal would be to manage the exemption in a way to prevent the property tax break to busi-

nesses from being translated into property tax increases for residents, small businesses, landlords and others.

The second major goal of the MMA proposal would be to link the targeted property tax exemption to important structural reform that would reorganize the way some governmental services are both financed and delivered in Maine to achieve efficiencies, and that includes efficiency in the administration of the new system.

It is fair to describe the MMA plan as a reform-driven proposal. In contrast, LD 1660 is anti—reform. It does nothing more than further narrow the tax base, increase the property tax rate, and continue to contribute to the state's property tax problem.

As described above, LD 1660 is designed to exempt 10% of the municipal tax base prospectively — a cut of a thousand knives that depresses normal growth in the municipal tax base for industrial and service center municipalities, making local governments more dependent on charity reimbursement from Augusta. History tells us that reimbursements from Augusta, sooner or later, will be cut back and then eliminated.

An alternative approach is to simply bite the bullet and exempt from taxation the more-narrowly defined property "overnight" so the economically important, targeted types of property would be exempt from taxation all at once. If that were to happen, there would be number of impacts. The "reform" elements of the MMA proposal recognize that it is entirely possible to manage those impacts in a manner that would also advance a number of valuable outcomes.

Here's the coincidence. Speaking in round numbers, if the personal property of bona-fide manufacturing property were made exempt from taxation overnight, Maine's municipalities in the aggregate would lose roughly \$80 million a year in tax revenue. By the same exemption, the state would save \$80 million in reimbursement obligations because it would no longer have to pay the businesses back under the BETR program for the property taxes that are no longer paid.

\$80 million is also the aggregate assessment Maine's 16 counties levy

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# Three Eminent Domain Bills Debated by Committee

This session's three eminent domain bills were discussed at a Judiciary Committee panel on the general subject of eminent domain held Tuesday. Two of the bills are "emergency" bills introduced during this second session: LD 1870, *An Act To Clarify Laws Governing Eminent Domain* and LD 1904, *An Act To Protect Businesses from Unnecessary Eminent Domain Takings*. Their public hearings were on Thursday. The third bill is a carryover from the First Session, LD 1297, *An Act to Provide Just Compensation for Established Businesses During Eminent Domain Proceedings*.

The two new bills were filed in response to the U.S. Supreme Court decision in *Kelo v. City of New London, Conn.* case which was released this past summer. In the *Kelo* decision, the Court narrowly upheld the City's taking of private property for the purpose of redeveloping the property commercially.

Following the dissenting opinion, many politicians of all stripes have stated that they believe the decision was incorrect and that the constitutional requirement that property be taken for a "public use" does not include taking the property of A and giving it to B for B's use, even if that use is more productive for the community as a whole. The two new bills were selected from a field of seven or eight "anti-Kelo" bills that were introduced for this Second Session.

Neither bill appears to radically alter or diminish municipal eminent domain authority; in fact, neither bill appears to accomplish much of anything. LD 1904, filed by Representative Barbara Merrill (Appleton), does two things. It states that property may not be taken "unless the taking is an absolutely necessity." Further, when property of a business is taken, only the "minimum amount of property neces-

sary" may be taken so as to "maximize the ability of the business to continue."

While these expressions of sentiment are appealing, they are also current law. Maine's Constitution requires that there be a "necessity" before property is taken and property can't be taken unless for a "public purpose." Accordingly, it would appear that the bill simply restates the Constitution. There can be a problem with this type of bill which is that no one really knows if it is intended to go beyond the current Constitutional requirements.

The second new bill is LD 1870, which is a more detailed anti-Kelo bill. It would prohibit takings for three purposes: (1) commercial development, (2) the enhancement of tax revenue and (3) in order to transfer the property to another non purely governmental entity. It purports to protect current eminent domain authority for properties which are "blighted", for utility companies and for other governmental purposes.

Again, this bill was not that objectionable to municipal officials. One concern is that the third prohibition on transfers is seemingly too broad. It forbids transfers to non-profits and public-private partnerships. It would appear that this might include a non-profit library that was separately incorporated from the municipality, or a separately incorporated fire company. It would certainly prohibit a transfer of taken property to a private land trust or other conservation group. MMA suggested that the Committee look hard at this prohibition.

The second municipal concern was that a well-intentioned attempt in the bill to protect other legitimate government takings might actually cause more harm than good. The bill contains a very short list of examples of types of takings that continue to be protected. Any bill that attempts to list legitimate

eminent domain takings would need to be several pages long and fairly broad in its language. Otherwise, an attorney somewhere will argue that since the Legislature did not include a particular taking on this list, it must not be allowed. Accordingly, MMA encouraged the Committee to keep this protection of other government takings short and sweet.

Lastly, there is an eminent domain carryover bill, LD 1297, which would increase benefits to properties which are taken. It would both add or increase so-called relocation benefits which the Department of Transportation is obligated to provide to the owners of property it takes. Municipalities would be obligated to provide these benefits for the first time under this bill. The benefits can range from \$10,000 - \$50,000.

The more radical element in the bill would force the government to pay more to the business which had its real estate taken by eminent domain. Somehow, the lost value, if any, of a business' "goodwill" would need to be calculated and then paid. Very few states provide this kind of benefit and for good reason. "Goodwill" is difficult to calculate and like the nature of business itself, is speculative and uncertain. Many other policy and technical issues are raised by this proposal.

The municipal position underlying all three of these bills is that they are not needed. In Maine, unlike other parts of the country, eminent domain is simply not exercised very frequently. A recent survey of over 300 Maine municipalities found that approximately 93% haven't used, or even tried to use, eminent domain once in at least five years. Of those that have tried, many failed (e.g., town meeting refused to grant the request) or they have used it for very non-controversial takings like road expansions or "confirmatory takings" that are used only to clear any title clouds on town-owned property.

It is hoped that the Legislature will focus on the reality of Maine and the fact that Maine municipalities have been very responsible stewards of their eminent domain power. While tempting to jump on the anti-Kelo bandwagon sweeping the country, that is not a sound reason to enact changes to Maine policy.

# Public Sector Labor Unions

In previous issues of the *Legislative Bulletin* there have been articles about the proposal in Governor Baldacci's budget bill (LD 1968) to mandate a minimum salary for Maine's school teachers of \$30,000 a year. The current average starting salary is \$27,000 a year. The proposal will increase some school budgets in the short term wherever there are any school teachers earning less than \$30,000, and the budget bill proposes to cover those short-term impacts for the first year. There are, obviously, much larger and more long-lasting financial implications associated with the Governor's proposal. Thus far, neither the Governor's budget bill nor the Essential Programs and Services (EPS) school funding model recognize any additional financial impacts associated with mandating a minimum salary. The Governor's proposal also interferes directly with the principles of labor contract negotiations by mandating a minimum salary, which obviously asserts an upward influence on every other step in every school system's teacher salary matrix. To the best of our knowledge, there is no other profession in the state of Maine which has a minimum salary established by law. Typically, minimum wage law is established to provide a minimum baseline wage for employees who are not otherwise represented by labor unions, which is obviously not the case for Maine's schoolteachers.

LD 1968 is not the only bill working its way through the Legislature that provides a very significant advantage to public sector labor unions. Two other such bills are described below.

## Negotiating over "educational policy"

LD 430, *An Act to Modify the Obligation to Bargain Under the Municipal Public Employees Labor Relations Law* is sponsored by Rep. Jackie Norton of Bangor. The bill was first submitted in 2005 as a "concept draft", although the "concept" of the bill was left undescribed beyond what was implied by its title.

After being formally introduced and referred to the Labor Committee, LD 430

went subterranean and was "carried over" into this legislative session. The reason for all the delay around LD 430 was apparently for the purpose of allowing a specially-created *Teacher Workload Task Force* to study public schoolteachers' workload concerns, develop recommendations and use LD 430 as the legislative vehicle to implement its recommendations. As a result of the Task Force's work, the concept draft has been replaced with a concrete proposal seeking an expansion of the list of issues over which teachers can negotiate.

Currently, schoolteachers can negotiate over wages, hours, working conditions and grievance procedures, but cannot negotiate over "educational policies", such as the number of school days in a year. "Educational policy" issues such as the length of the school year and the length of the school day are, under current law, allowed to be established by the "employer", which is essentially the general public that is purchasing the public educational services. LD 430 proposes to significantly shift the line between employer and employee decision-making authority by expanding the "working conditions" definition. As proposed, the teachers' union wants their members to be able to negotiate over:

- 1) scheduling of planning and preparation time;
- 2) length of the teacher work day;
- 3) length of the school year;
- 4) number of days teachers must work when students are not in attendance;
- 5) issues that impact work hours or workload that may be influenced by Maine's Learning Results system, Maine's student assessment requirements, and the federal No Child Left Behind Act; and
- 6) any other issue that may impact a teacher's workload.

At its February 16<sup>th</sup> meeting, MMA's Legislative Policy Committee voted to oppose LD 430. Municipal officials believe that the existing law appropriately defines what issues should be the sole responsibility of the school board to determine (representing the general public

employer), and the non "educational policy" issues that are appropriately the subject of negotiation between the employer and the teachers.

Although the concept draft received an initial public hearing on February 24, 2005, now that the details associated with the proposed concept are available, the Labor Committee has scheduled a public hearing on the amended bill for Thursday, March 2<sup>nd</sup>.

## Defined Benefit Health Insurance for Retired Police and Full-time Firefighters

In 2003, the 121<sup>st</sup> Legislature created the *Task Force to Study Parity and Portability of Retirement Benefits for State Law Enforcement Officers, Municipal and County Law Enforcement Officers and Firefighters*. The eight member Task Force, represented by four legislators, three law enforcement officers (one each representing state, county and local government) and one municipal firefighter, was charged with reviewing the differences in the retirement benefits provided to state, county and municipal public safety service providers. The Task Force was also charged with developing recommendations for providing parity and increasing the portability of benefits provided to state, county and municipal public safety employees.

The Task Force concluded that changes in the way benefits are currently provided to county and local law enforcement officers were necessary to ensure that municipalities and counties could compete with the state to attract and retain law enforcement officials. Without a uniform retirement plan, the Task Force concluded that municipalities and counties would continue to have difficulties keeping law enforcement officials on local payrolls. It is implied in the Task Force's report that the inequity in the level of benefits provided by local and state employers is the predominant reason law enforcement officials are leaving municipal and county departments to join the State Police.

As a result of the Task Force's findings, LD 1021, *An Act to Implement Task Force Recommendations Relating to*

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## REFORM (cont'd)

against the property tax base to operate the 15 county jails. Given willing political participants, it would be relatively straightforward to execute a three-way swap whereby municipalities would simultaneously lose both \$5 billion in tax base and the need for \$5 billion in tax base, because the state would use its \$80 million in savings to finance the county jails.

### The Revenue Sharing Equalizer.

On the individual municipal level, the proposed “county swap” requires some additional management. For some towns, the annual county tax bill is much greater than any lost revenue associated a personal property tax exemption. For others, the opposite is true and they would suffer a net loss – in some cases a severe loss – in the swap between the county bill and lost tax revenue. All of those differentials can be managed to the penny in the first year of implementation by redistributing \$70 million of existing revenue sharing resources. Specifically, each municipality’s revenue sharing could be decreased or increased by the exact difference between that municipality’s county tax obligation and the lost tax revenue associated with personal property tax exemption. Each town and city could be made perfectly whole in the first year.

At that point, the system could essentially self-operate. The annual value of revenue sharing grows with the economy, and so would the annual value of this designated pool of revenue sharing. That pool of roughly 65% of all revenue sharing funds could annually be distributed on a formula that takes into account the value of the property that is being exempted from taxation in each individual municipality relative to the total amount of exempt property statewide. No municipality would have to continue assessing the exempted property unless it wanted to continue monitoring the assessing records to make sure that its constitutionally-guaranteed reimbursement levels were being honored. In rough numbers, the revenue sharing-based reimbursement system would keep municipalities whole without requiring the ongoing management of essentially obsolete assessing functions.

**Conclusion.** There are additional elements to the MMA proposal, but the core element is the “county swap”. Pages of additional material could be added to describe the opportunities for a healthier, restructured relationship between municipalities and county government that this plan could create, where the services that counties provide that would be funded off the property tax base would be services directly requested, contracted for, and supported by the municipalities utilizing those services.

Pages of additional material could also be added to describe the opportunities for a more rationally designed community-based corrections system if the state and county governments were directly connected with respect to Maine’s prison and jail system.

Unfortunately, at this point, the additional advocacy for this reform plan appears unwarranted. The convention of legislative leadership that asked for MMA’s recommended approach to exempting the personal property tax has elected to stick with the narrow exemption as provided in LD 1660. Forget about targeting the exemption more narrowly. Forget about the “county swap” idea. Forget about linking anything to structural reform. The leadership folks were polite. They called the plan “intriguing” and “outside the box”. Ultimately, however, the plan was rejected as “politically unviable”, “dead on arrival”, a “non-starter”.

In short, it seems headed the way of all reform.

## UNIONS (cont'd)

*Parity and Portability of Benefits for Law Enforcement Officers and Fighters* was submitted to the 122<sup>nd</sup> Legislature. As proposed, LD 1021, sponsored by retired firefighter Rep. Robert Duplessie of Westbrook, would create a state subsidy for the health insurance benefits provided to retired municipal police officers and firefighters, provided that the employee participated in a Maine State Retirement System plan. As originally drafted, a 0.5% premium tax on all property and casualty insurance policies issued in Maine (including homeowners insurance), and a 1.5% tax on the salaries of participating active municipal and

county law enforcement officers and firefighters would be assessed to cover the cost of the subsidy. According to a fiscal note prepared by the Legislature’s Office of Fiscal and Program Review, the insurance premiums tax would raise \$7.7 million in 2007; that is, residents and businesses purchasing property and casualty insurance in Maine would be assessed an additional \$8 million each year to cover the retirees’ health insurance guarantee.

From the perspective of Maine’s elected municipal officers, the most significant problem with LD 1021 is that it is moving toward a system that guarantees a level of benefits upon retirement (“defined benefit”), while most employers — both public and private — are moving toward a “defined contribution” system. Under a defined contribution system, employers invest an agreed-to amount of funds into an account which is made available to the employee upon retirement. Through the defined cost contribution approach, the employer is certain of both the short-term and long-term financial exposure and the future costs can’t spiral out of control and create the huge unfunded liabilities that seem to be invariably generated whenever future defined benefits are guaranteed. If adopted, the Legislature will be responsible for finding a sustainable revenue source to appropriately fund this long-term commitment. Shifting those costs onto the municipalities would be the inevitable next step.

Municipal officials are also concerned that providing law enforcement officers and firefighters a guaranteed retirement package will erode the employer-employee negotiation process. If the state is subsidizing certain benefits, the same teachers’ salary dynamic is created that is discussed above; namely, the union negotiators can work on both the local level and the state level, effectively negotiating two non-integrated contracts for a dynamically larger total benefit. Also, the proposal to fund the retiree program through the assessment of a tax on insurance premiums would shift the costs to all municipalities that purchase property and casualty insurance, many of whom do not have police departments

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## **UNIONS (cont'd)**

or full-time firefighters.

As might be expected, the insurance industry raised concerns with the bill's proposal to fund a majority of the retiree subsidy program on the backs of insurance policy subscribers. It is because of this opposition that the bill is now in limbo.

According to Labor Committee Senate Chair, Ethan Strimling (Cumberland Cty.), the bill has been indefinitely tabled until a funding source can be identified. Some proponents of the bill thought the retirees' health insurance program would be funded in the Governor's supplemental budget, but that was not the case in the printed bill (LD 1968). The proponents are now trying to find a funding mechanism that does not rely on a surcharge on insurance premiums or General Fund revenues. Apparently, some of the LD 1021 proponents are exploring taxes and fees as potential sources of revenues.

### **No Hearings**

There will be no public hearings for the week of February 20th as the Legislature will be on vacation.