

Filling the Holes in Governor’s Budget

Tax Panel Recommends Temporary Suspension of Income Tax Breaks

For the last several weeks the Taxation Committee has been reviewing a clutch of bills that would raise state revenue in one way or another and simultaneously developing the Committee’s final “report back” letter to the Appropriations Committee. This last letter to Appropriations identifies the Committee’s recommendations for addressing proposed cuts in the Governor’s two year budget bill that the Committee would like to see restored with tax revenue.

The letter contains three proposals rather than a single “consensus” recommendation. A lack of unanimity should come as no surprise given the sharp divides in the State House during this home stretch of the legislative session. The majority report is authored by the seven Committee Democrats and endorsed by the Committee’s lone unenrolled legislator, Rep. Joe Brooks of Winterport. The other recommendation, which splits in two directions, is authored by the Committee’s five Republicans.

With that said, there is not as much divisiveness in this letter as the average State House observer might expect. Between the two reports, there is some overlap.

Overlap #1. The Democrats’ report describes its goal as providing options for the Appropriations Committee to consider as “an alternative to the property tax increases proposed in the Governor’s biennial budget” because “The Governor’s proposed changes to Municipal Revenue Sharing, the Homestead Program and the ‘Circuit Breaker’ would result in tremendous property tax shifts to Maine taxpayers.”

The Republicans’ report states that they “agree that restoring the homestead

exemption, the ‘Circuit Breaker’ program and revenue sharing should be priorities for the Legislature.”

As to how to achieve those similar goals, the two reports have some big differences. Two of the five Republicans in their report say that the three property tax programs should be restored by enacting unspecified spending cuts, and they are opposed to all tax increases. In contrast, the Democrats’ report lists out a number of possible income and sales tax increases

that they believe would be much more equitable than the property tax increases triggered by Governor’s proposed elimination of all or most of those three tax relief programs.

Partial Overlap #2. Which brings us to the other point of overlap between the two reports, or at least partial overlap. Two of the five Republicans in their report identify the comprehensive tax reform legislation (LD 1496, An Act to Modernize

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Municipal Street Light Programs

The Energy, Utilities and Technology (EUT) Committee held its public hearing on May 2 on LD 1251, *An Act To Lower Costs to Municipalities and Reduce Energy Consumption through Increased Competition in the Municipal Street Light Market*, sponsored by Representative Mary Nelson of Falmouth. On Monday, May 20 the Committee approved compromise language the street light team of Falmouth Town Manager Nathan Poore, Rockland City Councilor Larry Pritchett, and Director of Planning and Economic Development for the City of South Portland Tex Haeuser struck with Central Maine Power’s Director of Public Affairs, David Allen, and Jim Cohen of Verrill Dana (on behalf of the Maine Public Service Company and Bangor Hydro Electric Company). By accepting the amended language, the EUT Committee opened the door for municipalities to take a positive step forward with respect to their street lighting programs.

If finally enacted, municipalities will

have three options for street lighting programs: the “utility-provided services” option, the “municipally owned, utility-installed” option, or the “municipally owned, installed and maintained” option.

The amended version of this legislation cedes the determination of many of the finer details to the Public Utilities Commission (PUC). The PUC will now approve power transmission and distribution utility charges. These charges include the cost of lighting equipment, power delivery, and mounting hardware or power supply wire connection and repairs. The PUC will also establish criteria for the placement of the lighting hardware on the utility pole. Criteria governing the management of safety issues will be set by the PUC, too.

Pole attachment fees were a major sticking point in the amendment deliberations. The utilities’ position is that other entities attaching infrastructure to their poles pay what is essentially a rental fee in exchange for the privilege of using that

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Tax Reform Plan Shifts Gears

Two-year phase-in proposed, some property tax components jettisoned

The Taxation Committee met in work session on Tuesday this week to further review LD 1496, *An Act to Modernize and Simplify the Tax Code*. Senator Richard Woodbury (Cumberland Cty.), the principal author of the plan, provided a more detailed version of the bill to the Committee and laid out its proposed implementation. LD 1496 is the comprehensive tax reform bill that was described in detail in the May 3 and May 17 editions of the Legislative Bulletin.

As it is now being proposed, there are some changes to the plan that impact its implementation with respect to the property tax, sales tax and income tax components of the reform.

In brief summary, the plan would now be phased in over a two-year period.

Sales taxes. The sales tax rate changes and some of the more easily definable sales tax base expansions would be implemented first, in December 2013, in order to begin raising the revenue to implement the income tax and property tax components of the plan. A working group would be formed for the purpose of developing a second phase of sales tax base expansions dealing with expansions that need to be carefully defined to avoid pyramiding and to focus as much as possible on consumer transactions. The working group's recommendations, if approved by the Legislature, would be implemented on Jan. 1, 2015.

Income taxes. Following the revenue generated by the phased-in sales tax in-

creases, the income tax changes would be implemented in two steps. The first step would reform the income tax code to a "flat rate" system with two credits for Maine residents (sales tax fairness and property tax circuitbreaker) and set the rate at 5% beginning on Jan. 1, 2014. The second phase would drop the rate to 4% starting Jan. 1, 2015 and implement the elimination of the estate tax. The reductions to the corporate income tax as originally proposed are no longer part of the plan.

Property taxes. For the FY 14 fiscal year, there would be a "status quo" property tax system. Municipal revenue sharing would be set at 3.5% of state sales and income taxes, which is essentially equivalent to what was distributed during the current fiscal year, and the \$10,000 homestead exemption would apply. The \$50,000 homestead exemption would be implemented on April 1, 2014, and the revised "Rev II" revenue sharing program would begin on July 1, 2014.

Also on the property tax side, two elements of the plan in its concept draft form have been either substantially set-aside or jettisoned.

The bill no longer provides that relatively high value tax-exempt properties must make some level of property tax contribution. Instead, issues associated with tax exempt property, the Tax Increment Financing (TIF) system, and the Tree Growth program would be given over to the working group to develop future recommendations, without any particular guidance. Because the proposal no longer expands the municipal tax base by requiring some contribution from tax exempt institutions, the mill rate increases associated with the expanded homestead exemption and amended revenue sharing program would be somewhat greater than originally projected, particularly in communities with high concentrations of tax exempt property.

Also, the plan no longer provides that municipalities would get tax jurisdiction over two-way, interactive telecommunications programs.

These are not inconsequential changes. Under the original plan, at least part of

the contraction of the tax base associated with a large homestead exemption was set off by an expansion of the tax base in other areas. Those compensating set-off elements are no longer part of the plan.

Now that the bill has been printed in detail, the Taxation Committee has asked Maine Revenue Services to perform a "distributional" analysis that will describe how the tax burden among various income groups will be changed by this bill relative to current law. That analysis, scheduled to be presented to the Committee sometime next week, might also provide information about the degree to which the tax burden is successfully "exported" under this plan; that is, shifted away from state residents in a way to make Maine residency more attractive, which is the policy goal.

The next work session on the plan is scheduled next Thursday, May 30 at 1:00 p.m.

Governor's Budget (cont'd)

and Simplify the Tax Code) as "*a viable alternative to the cuts proposed in the Governor's budget and, more importantly, much needed long term tax reform that will stimulate economic growth, provide property tax relief and collect a fairer share of taxes from non-residents.*" Those two Republicans are joined by two Democrats and Rep. Brooks, all expressing strong support for LD 1496.

Majority Report, First Tier Option. Overlaps aside, a simple three-year suspension of the income tax reductions enacted in the last biennial budget received the most support from members of the Taxation Committee.

Coincidentally, ironically, fortuitously, serendipitously or however else it may be described, the suspension of the income tax reductions provides almost exactly the \$400 million needed over the biennium to avoid eliminating municipal revenue sharing and nearly eliminating the Homestead exemption and Circuitbreaker programs as the Governor proposes. As pointed out in the report, "*This property tax increase is primarily the result of the*

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Mandate Watch Update

An article was published in last week's edition of the Legislative Bulletin describing several bills that propose to shift additional costs and administrative burdens onto municipalities. What follows is an update on the status of any legislation described in that article that moved in any way in the last week, as well as the addition of other mandate bills or "watch bills" MMA will be following closely. Municipal officials are encouraged to contact their legislators if they have concerns or input.

Progress on Previously Listed Mandate Bills

LD 235 – Firefighters and "Tone-to-Tone" Workers' Compensation. The amended bill provides that a firefighter or emergency medical services provider – whether professional, "call" or volunteer – who gets injured after receiving a toned notification of an emergency is presumed to have suffered a workplace-related injury and therefore eligible for Workers' Compensation coverage even if the injury occurs in his or her home or other private property unassociated with the emergency. Under the bill, the burden of proof is put on the municipal employer to prove otherwise. **Update:** The bill was approved by the Senate this week by a vote of 18 to 17. LD 235 will be debated by the members of the House next week.

LD 965 – Dig Safe. The primary thrust of LD 965 would be to mandate that all publicly owned water and wastewater utilities be members of the "Dig Safe" system or some parallel system. Municipalities may voluntarily join Dig Safe as members, but mandatory municipal membership is not required in Maine or any other New England state. **Update:** On Thursday, the EUT Committee decided to carry this bill over to the second session of the 126th Legislature.

LD 1303 – Establishing a Right to Hunt and Fish. As most recently amended, this resolution constitutes a local government preemption rather than a mandate. This bill would send out to the voters a proposed constitutional amendment, the wording of which is

changing on a daily basis. In its most recent iteration, the Constitution would be amended to forever preserve the heritage of hunting and fishing for the purposes of harvesting wildlife for personal use. Part of that required preservation effort would limit all forms of governmental regulation affecting the privilege to harvest fish and wildlife to the Legislature only, rather than any other level of government and rather than the voters directly through their right of initiative. The obvious municipal concerns involve the various types of local ordinances that may be viewed as illegal or unenforceable under this amendment because of their alleged impingement on this newly created constitutional right. **Update:** LD 1303 has yet to make it to the floor of the House or Senate.

New Mandate & "Watch" Bills

LD 1150 – Prevailing Wage. Under existing law, the state must pay "prevailing wages", as those wage rates are determined by the Maine Department of Labor, on state public works contracts that exceed \$50,000 in value. As amended by a majority of the Labor, Commerce, Research and Economic Development Committee, LD 1150 extends the "prevailing wage" requirement to municipal and school construction projects that are funded entirely or in part with state revenues. **Current status:** LD 1150 has yet to make it to the floor.

LD 1342 – Sewer Rate Mediation. As now amended, LD 1342 creates a framework for establishing a mediation program when sewer district customers object to proposed rate increases. The bill authorizes the Public Advocate to act as mediator in any disputes that go to mediation. The bill also establishes a petitioning system which allows customers concerned about proposed rate increases to present petitions to the treasurer of the sewer district and the Public Utilities Commission that are signed by at least 15% of the customer base or 1,000 customers, whichever is less. The bill further provides that upon receipt of a valid petition, the petition-

ers and the sewer district can agree to take the dispute to mediation, but both parties must agree to enter mediation in order for mediation to occur. Given the authority of the sewer district to opt out, the mandatory elements of LD 1324 would be associated with properly managing the petition (i.e., determining that the signatories were customers and the signatures are valid). **Current status:** LD 1342 has yet to make it to the floor.

LD 890 – Buy American. This bill requires that every contract for the construction, reconstruction, alteration, repair, improvement or maintenance of a public building or public works that is let by a public agency, including municipalities, school systems and other political subdivisions, must contain a provision that the iron, steel and manufactured goods used or supplied in the performance of the contract must be manufactured in the United States. Various exceptions are written into the bill, including the determination that the contract clause would cause the project's cost to be unreasonable, as determined by the Governor. **Current status:** LD 890 has yet to make it to the floor.

Street Lights (cont'd)

pole space. Municipalities requested an attachment fee exemption on the premise that those other entities typically operate on a for-profit basis, and that municipalities do not charge the utilities for the privilege of placing their poles in the municipal right-of-way. The amendment ultimately allows the PUC to determine fair attachment fees, while directing the PUC to consider this municipal right-of-way ownership as well as the municipal interest in serving the general public.

LD 1251 is currently incorporated into the EUT Committee's "Omnibus" energy bill, and the fate of that bill is unclear for reasons entirely unrelated to the street light legislation. From here on out, MMA's efforts will be to protect this solid agreement between the municipalities and electric utilities and find clear steerage to its enactment.

unfunded tax cuts passed in the 125th legislature, which total over \$400 million in the coming biennium.”

Specifically, the majority report recommendation would:

- Suspend for three years almost all of the personal income tax reductions that were enacted as part of the two-year state budget enacted in 2011. Those adjustments in income tax brackets and overall reduction in rates went into effect Jan. 1, 2013, and this recommendation would put them into effect, instead, on Jan. 1, 2016 and thereafter. The element of that income tax reduction package that this proposal would not suspend is the part that took households with incomes in the lowest of the 4-bracket system that used to be in place off the tax rolls entirely.

- Also suspend for three years the change in Maine's estate tax law, also enacted in 2011. That change increased the value of an estate not subject to the estate tax from the first \$1 million to the first \$2 million, also beginning on Jan. 1,

2013. This proposal would suspend that change until Jan. 1, 2016.

Majority Report, Second Tier Options. Finally, back-up options are listed out in the majority report in case the suspension of the income tax reduction package is “not possible.” These are presented in a menu approach; that is, the following six bulleted proposals are not being proposed as a package of changes but, rather, a smorgasbord to choose from as the Appropriations Committee deems appropriate. All six of these proposals were presented in one form or another to the Taxation Committee as separate legislative proposals this session:

- Impose an assessment on the income tax obligation of individuals within the state's top 1% income bracket so that their ultimate income tax obligation is somehow calibrated to the statewide average effective tax rate. The revenue implications have not been determined as of yet.

- Increase the sales tax rate on meals

and lodging purchases from the current 7% to either 9% or 10%, raising from \$120 to \$180 million over the biennium.

- Apply a temporary 1% increase to the sales tax rate on general merchandise (from 5% to 6%) with a built-in sunset provision, raising \$300 million over a biennium. This approach was done in the early 1990s.

- Assign a task force to find \$30 million in revenue by eliminating tax loopholes and ineffective tax exemptions.

- Enhance the state's capacity to require Internet retailers to collect and remit the state's sales taxes for e-purchases, raising less than \$1 million over the biennium. (Note: a significantly greater amount of revenue would be generated if and when federal-level “e-fairness” legislation is enacted.)

- And, increase the cigarette excise tax from \$2 to \$3.50 per pack, either all at once or in staged 50-cent intervals, raising approximately \$140 million over the biennium if enacted at full throttle.