

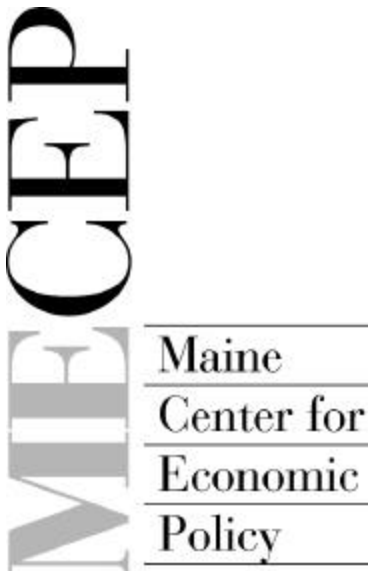
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IDEAS FOR SHARED PROSPERITY

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The Circuit Breaker Provides Relief for Maine's Property Tax Burden

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Richard G. Woodbury



Widespread attention has been directed to the burden of property taxes in Maine. It has led to calls for legislative action, citizen referenda, consideration of tax and spending caps, and broader discussions of tax fairness and tax reform. The burden of property taxes inspired the appointment of a special legislative panel in late-2004 and the highly publicized passage of LD1 as the first order of business in Maine's 2005 legislative session. Property tax reform continues as a leading topic of policy discussions and political debate throughout the state.

While the median household in Maine pays about 4 percent of their income in property taxes, the variability in property tax burdens across households is considerable. Roughly one third of Maine homeowners pay less than 3 percent of their income in property taxes; about a third pay between 3 and 6 percent of their income; and

a third pay more than 6 percent. At the extreme, about 11 percent of households pay between 10 and 20 percent of their income in property taxes; and 7 percent pay more than 20 percent of their income. The wide variability in tax burdens

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is enhanced
substantially by the
LD1 reforms
enacted in 2005.***

across households raises questions of fairness, and points to policies like the circuit breaker as potential tools to make property tax burdens more equitable.

The Maine circuit breaker program, also known as the Property Tax and Rent Refund program, makes property tax

refunds available to most resident homeowners who are paying more than 4 percent of their income in property taxes. For high tax burden households, these refunds have the potential to reduce - in some cases dramatically - the net burden of property taxes. The goal of this paper is to analyze the impact of the circuit breaker on property tax burdens before and after the 2005 reforms.

How the Circuit Breaker Works

The Maine circuit breaker program is a two-tiered system. Eligible homeowners can receive property tax refunds equal to half the amount by which their property taxes exceed 4 percent of income, up to 8 percent of income, plus all of the amount by which their property taxes exceed 8 percent of income. For example, consider a retired couple with an income of \$30,000 and a property tax bill of \$3,000. Four percent of their income is \$1,200; 8 percent of their income is \$2,400. They would qualify for a refund of half the amount of their taxes between \$1200 and \$2400 (or \$600), plus all of the amount of their taxes

over \$2,400 (an additional \$600), for a total circuit breaker refund of \$1,200. Once they receive their refund, the net burden of their property taxes is reduced from \$3,000 to \$1,800, or from 10 percent of their income to 6 percent of their income.

An important implication of the two-tiered formula in Maine is that it creates the equivalent of a 6 percent-of-income tax cap for most households. Qualifying

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households must pay only for the first 4 percent of their income in property taxes, plus half of the next 4 percent - or a total of no more than 6 percent. After that, the refund rate is 100 percent.

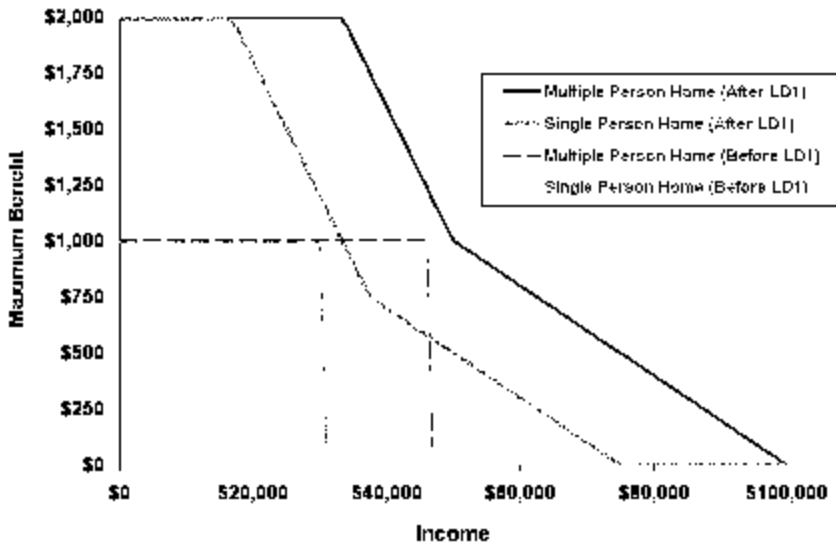
There are, however, two important limitations to the program, both of which were

changed as part of the LD1 reforms. First, Maine has a maximum refund amount - set at \$1,000 before the LD1 reforms, and increased to \$2,000 as part of the LD1 reforms. Second, Maine has either explicit (before LD1) or implicit (after LD1) income eligibility restrictions.

Before LD1, households qualifying for circuit breaker benefits were required to have an income of no more than \$30,300 (for single person households) or \$46,900 (for multiple person households). These limits were increased annually for inflation. LD1 replaced the explicit income eligibility limits with a limit on the amount of property taxes that can be used to determine eligibility for the program. The limit on property taxes that qualify for circuit breaker relief was set at \$3,000 for single-person households and \$4,000 for multiple-person households.

The implication and policy rationale for this reform was to phase-out the maximum benefit of the program at higher income levels. Figure 1 shows how the maximum benefit phases down to

Figure 1
Maximum Circuit Breaker Refunds



zero at income levels of \$75,000 (for single-person households) or \$100,000 (for multiple-person households).

The Effect of the Circuit Breaker on Net Property Tax Burdens

The primary analytical goal of this paper is to estimate the impact of the circuit breaker in moderating property tax burdens for those homeowners whose burden is highest. The calculations are made using the most recent property tax and income data available to Maine Revenue Services, and applying the relevant benefit criteria (before and after LD1) to the same database. This

enables us to isolate the effect of the circuit breaker, and the circuit breaker expansion, independent of other property tax reforms. The analysis also concentrates on the tax reduction that households are

eligible to receive - through circuit breaker refunds - setting aside the question of actual participation rates among those who are eligible. In other words, the analysis focuses on the impact of the circuit breaker if it is fully used as intended - with full participation of eligible homeowners.

The basic findings are illustrated in Figure 2. Without circuit breaker refunds, 33 percent of Maine households have a gross property tax burden that exceeds 6 percent of their income. Using the benefit criteria in the pre-LD1 circuit breaker, and assuming full participation in the program, the proportion of Maine households with a tax burden that exceeds 6

Figure 2
Effect of Circuit Breaker on Property Tax Burden

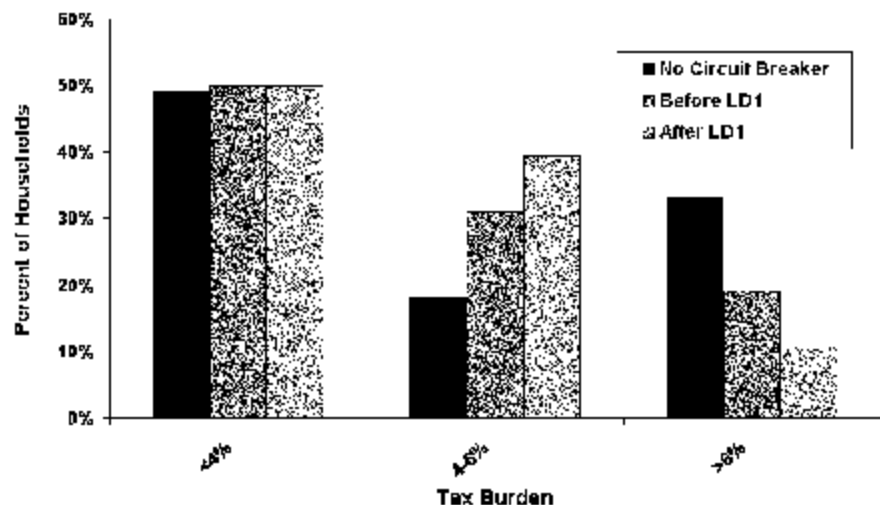
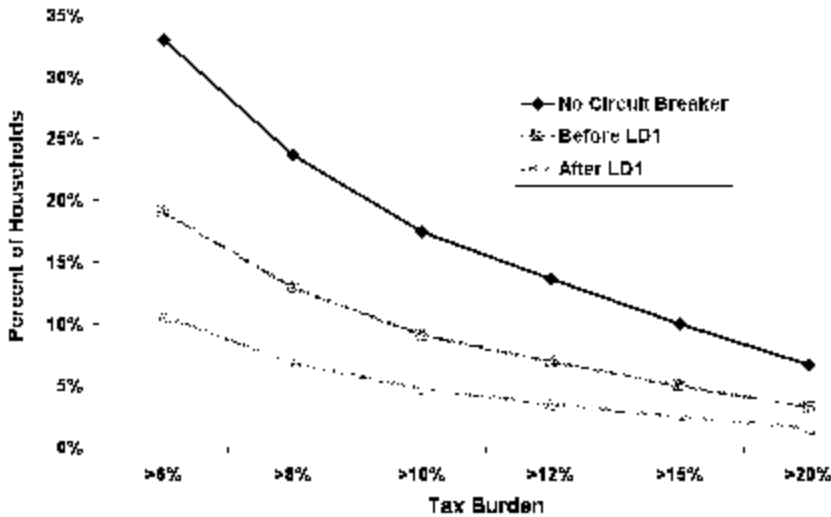


Figure 3
Effect of Circuit Breaker on High Burden Households



percent of income is reduced from 33 percent to 19 percent. Using the enhanced circuit breaker provisions in effect after the LD1 reforms, the proportion of Maine households in the high tax burden category is reduced from 33 percent to 11 percent. Two-thirds of Maine households who are in the highest tax burden category - paying more than 6 percent of their income in gross property taxes - can have their net tax burdens reduced to 6 percent or less as a result of the current circuit breaker refunds.

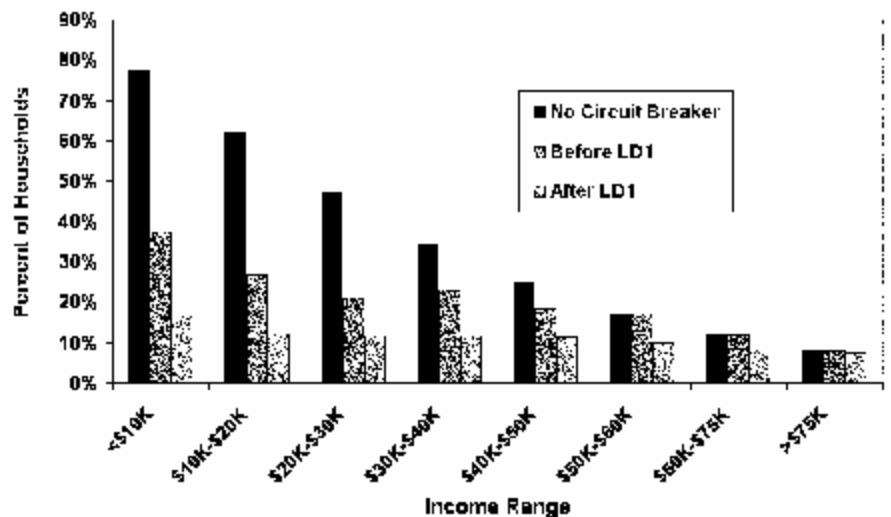
Figure 3 contains additional analysis of those households with the highest property tax burden in

Maine; and how they are affected by the circuit breaker, both before and after LD1. The circuit breaker reduces the percentage of households with a net tax burden greater than 10 percent of income

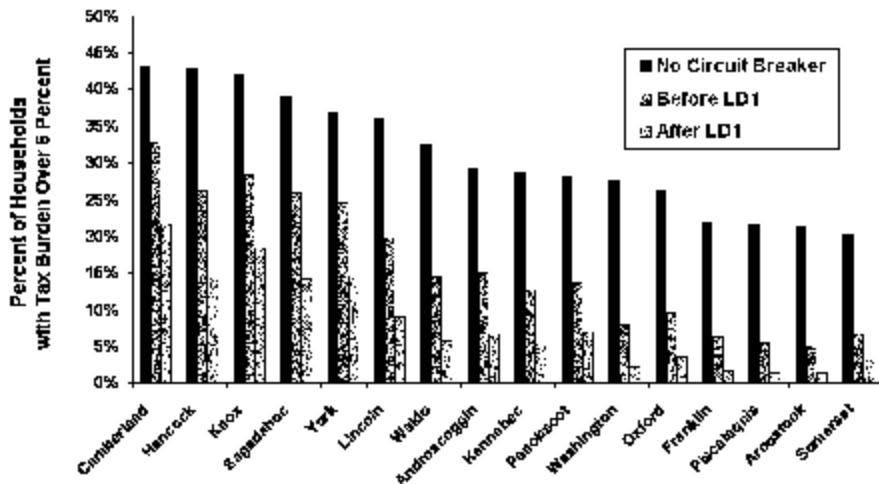
- from 17 percent of households (with no circuit breaker) to 9 percent (with the old circuit breaker), and to 5 percent (with the LD1 circuit breaker). The percentage of households with a tax burden greater than 20 percent of income is reduced from 7 percent (with no circuit breaker) to 3 percent (with the old circuit breaker) to less than 2 percent (with the LD1 circuit breaker).

Figure 4 looks at how the circuit breaker impacts households in different income categories. The first thing to note is that many more low income households have a high burden of property taxes, compared with higher income

Figure 4
Percent of Households with Burden Above 6%



**Figure 5
Effects of Circuit Breaker by County**



households. As a result, the benefits of the circuit breaker program are concentrated among lower income households. For example, among households with income of less than \$30,000, more than 60 percent have a gross tax burden over 6% of income. With the LD1 circuit breaker, however, only 13 percent of these households have a net tax burden over 6% of income. The portion of homeowners who benefit from the circuit breaker decreases at higher incomes.

Finally, Figure 5 looks at the impact of the circuit breaker across counties. While property tax burdens vary across Maine’s geography, every county has at

least 20 percent of households paying more than 6 percent of their income in property taxes. In some counties, such as Washington, Oxford, Franklin, Piscataquis, Aroostook, and Somerset counties, the circuit breaker provides sufficient refunds, so that very few households (about 2 percent) still have a net tax burden of more than 6% of income. In Cumberland, Hancock, Knox, Sagadahoc, and York counties, on the other hand, there are still 18 percent of households with a net property tax burden over 6 percent of income, even after the circuit breaker refunds. Still, tax burdens are reduced substantially in all counties.

Discussion

It is clear that the circuit breaker has a very substantial impact in reducing property tax burden in Maine. The effectiveness of the circuit breaker in reducing property tax burdens is enhanced substantially by the LD1 reforms enacted in 2005. Two thirds of households with a gross property tax burden above 6% of income can have a net property tax burden at or below 6% of income - as a result of the circuit breaker program. If all households eligible for circuit breaker benefits applied for them, the number of Maine households with a property tax burden over 6 percent of income would drop from 125,000 to 40,000. The number of households with a property tax burden over 10 percent would drop from 66,000 to 18,000. The number of households with a property tax burden over 20 percent would drop from 25,000 to 6,000.

How does the circuit breaker fit into broader discussions of tax reform? The circuit breaker is not a program that noticeably lowers overall tax burdens in Maine; it

uses money raised from state revenue sources (primarily income and sales taxes) to provide targeted relief in property taxes. It leads to a modest rebalancing in the overall mix of sales, income and property taxes - though the dollar magnitudes are small, when compared with revenue sharing or school funding. What the circuit breaker does well, however, is to contain the burden for those whose burden is highest. It does more than any other form of

property tax policy to assure that people can afford the out-of-pocket burden of paying their property taxes.

While the 2005 reforms contained significant enhancements to the program, further expansions are possible. For example, one could raise the maximum refund to a level higher than \$2,000 and/or raise the amount of property tax that is eligible for benefits. Even in its current form, however, the circuit

breaker is found to decrease quite dramatically the number and percentage of households with the highest burden of property taxes.

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