

# The Consequences of Maine's Income Tax Cuts

## Recent Tax Cuts Increase Costs for Municipalities, the Poor, and the Middle Class

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### Introduction

Governor LePage and the 125th Maine Legislature used cuts to income, pension, and estate taxes to transfer tens of millions of dollars to the richest Mainers. To pay for these tax cuts, lawmakers passed other measures that hurt low- and middle-income Mainers and shift the costs of education, road maintenance, fire and police protection, emergency assistance to families, and other basic services to Maine's cities and towns. This will result in higher property taxes for many low- and middle-income Mainers, making an already unfair state and local tax system even worse.

The Maine Center for Economic Policy (MECEP) estimated the property tax increase resulting from cuts to property tax relief and state aid to municipalities and local schools. Comparing the cost of this property tax increase to the benefits of the income tax cut enacted in 2011, MECEP projects that 270,000 families—40% of Maine's taxpayers—will see an increase in their total state and local tax bill. These are low- and lower middle-income families who can least afford to pay more taxes.

This is the wrong direction for Maine. Instead of cutting taxes to benefit the wealthy, we need to move toward a fair tax system and invest more in schools, roads, health care, and other basic services that strengthen communities and make our economy more competitive.

### Summary of Findings

Low- and middle-income families already pay more than their fair share in state and local taxes. For every dollar earned, the richest 1%—those earning over \$323,000 per year—paid 10 cents in state and local taxes. The middle 20%—those earning between \$23,000 and \$42,000 per year—paid 12 cents on the dollar, and the bottom 20%—those earning less than \$12,000 per year—paid 17 cents.

Property and sales taxes hit low- and moderate-income taxpayers hardest. Dollar for dollar, 4 out of 5 Mainers would be better off with an across-the-board property tax cut than an income tax cut like the one enacted by Maine's 125th Legislature in 2011.

Recent state tax cuts shift costs to towns and municipalities and low- and middle-income Mainers in several ways:

- **Less property tax relief:** Some 75,000 taxpayers who receive property tax refunds under the Maine Residents Property Tax and Rent Refund Program will pay more in property taxes because the legislature withheld over \$9.3 million from the program.

- **Less money for towns and cities:** The 125th Legislature eliminated more than \$84 million in state aid intended to reduce property taxes. If local governments increase property taxes to cover 50% of the \$44 million cost shift in 2013, property tax bills for households with annual incomes between \$20,000 and \$27,000 will go up by about \$16 on average.

- **Less money for educating kids:** As a result of expiring federal support and tax and budget policies adopted

by the 125th Maine Legislature, the state will contribute \$25 million less for local K-12 education in 2013 than it did in 2011 and \$76 million less than in 2009. Despite Maine voters' mandate for the state to fund 55% of the total cost for K-12 education, the state share will drop to 45.1% in 2013, lower than it was in 2006.

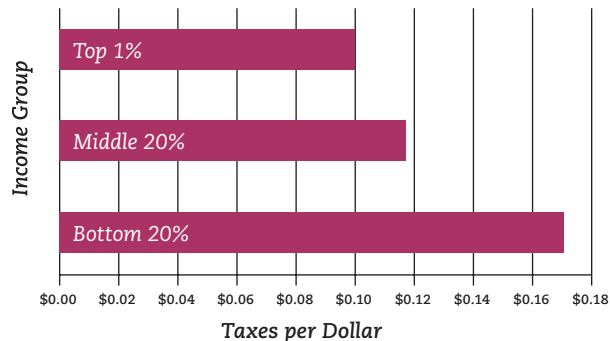
MECEP estimates that as a result of cost shifts from state to local government due to the 125th Maine Legislature's income, pension, and estate tax cuts, 40% of Mainers (270,000 families with annual incomes of \$27,000 or less) will pay more in combined state and local taxes.

## Low- and Middle-Income Families Already Pay More than Their Fair Share in State and Local Taxes

Maine's state and local tax system has long favored the highest earners. In 2009, the latest year for which full data are available, middle- and low-income Mainers paid a greater share of their incomes in taxes than high-income Mainers (Figure 1).

For every dollar earned, the richest 1%—those earning over \$323,000 per year—paid 10 cents in state and local taxes. The middle 20%—those earning between \$23,000 and \$42,000 per year—paid 12 cents on the dollar. Meanwhile, the bottom 20%—those earning less than \$12,000 per year—paid 17 cents.<sup>1,2</sup>

FIG.1: THE MORE YOU EARN, THE LESS YOU PAY PER DOLLAR State and Local Taxes per Dollar of Income, 2009



Source: Maine Revenue Services Tax Incidence Study, 2009

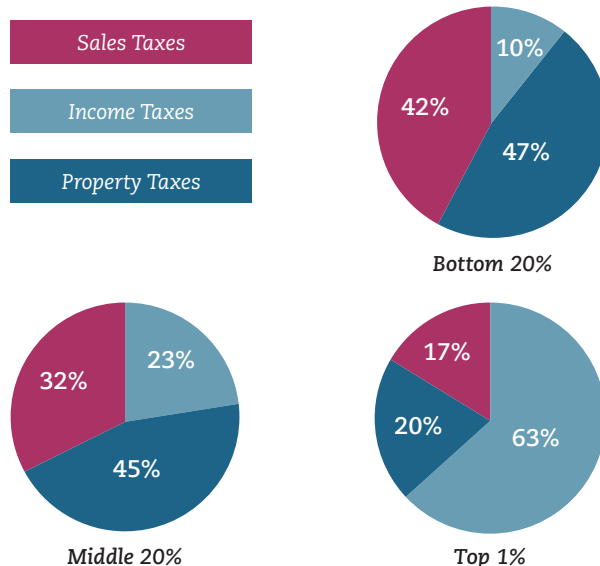
Dollar for dollar, 4 out of 5 Mainers would be better off with an across-the-board property tax cut than recent income tax cuts.

## Property Taxes Hit Low- and Middle-Income Families Hardest

The vast majority of Maine's state and local taxes falls into three categories: income taxes (including those paid by corporations and individuals), sales taxes (including various excise taxes), and property taxes. Historically, Maine's income tax rate has increased with income. Sales and property taxes, on the other hand, constitute the biggest share, by far, of the total state and local tax bill for low- and middle-income earners: 90% for the lowest-earning Mainers, compared to 37% for the highest-income Mainers<sup>3</sup> (Figure 2).

For low- and middle-income Mainers, the biggest slice of their state and local tax bill is property taxes, with sales taxes a close second. For high-income Mainers, the biggest slice is income taxes. This means that an increase in property tax rates or sales tax rates has a greater impact on middle- and low-income people than an increase in income tax rates. High-income earners benefit most from income tax cuts. Dollar for dollar, 4 out of 5 Mainers would be better off with an across-the-board property tax cut than an income tax cut like the one enacted by Maine lawmakers in 2011.

FIG.2: PROPERTY AND SALES TAXES HIT LOW- AND MIDDLE-INCOME TAXPAYERS HARDEST



Source: Maine Revenue Services Tax Incidence Study, 2009  
Note: Due to rounding, figures may not sum to 100%.

1. Maine Revenue Services Tax Incidence Study (2009) ([http://www.maine.gov/legis/ofpr/taxation\\_committee/interim\\_schedule/MRS\\_Tax\\_Incidence\\_Study.pdf](http://www.maine.gov/legis/ofpr/taxation_committee/interim_schedule/MRS_Tax_Incidence_Study.pdf)).  
2. See the appendix for a table of income groups used in Figures 1 and 2.  
3. Maine Revenue Services Tax Incidence Study (2009) ([http://www.maine.gov/legis/ofpr/taxation\\_committee/interim\\_schedule/MRS\\_Tax\\_Incidence\\_Study.pdf](http://www.maine.gov/legis/ofpr/taxation_committee/interim_schedule/MRS_Tax_Incidence_Study.pdf)).

## Three Ways Recent State Tax Cuts Increase Local Property Taxes

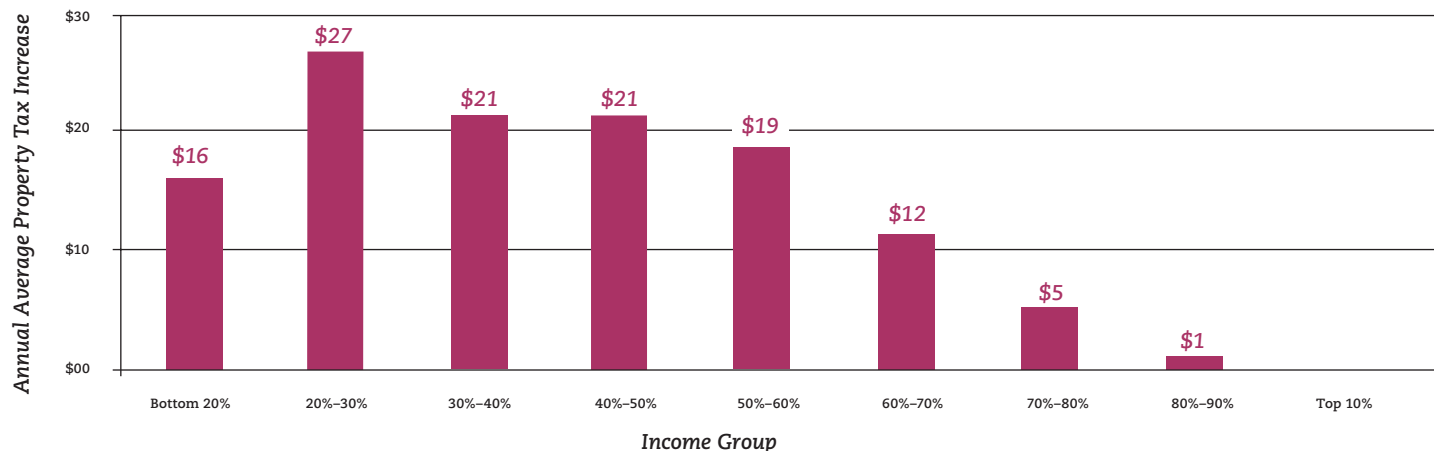
To help pay for the income, pension, and estate tax cuts, lawmakers passed other measures that hurt low- and middle-income Mainers.

### 1 Less Relief for Property Taxpayers

First, legislators cut property tax relief for non-elderly households<sup>4</sup> (Figure 3). Some 75,000 taxpayers who receive property tax refunds will pay more in property taxes because the legislature withheld over \$9.3 million in property tax relief from the Maine Residents Property Tax and Rent Refund Program. Most of the benefits of

this program—70%—go to households earning less than \$30,000 per year.<sup>5</sup> At the same time, lawmakers restored \$5 million in annual property tax relief for businesses. Nearly 60% of these benefits go to 20 major corporations, including Wal-Mart, General Electric, and Nestle.<sup>6</sup>

FIG. 3: \$9.3 MILLION REDUCTION IN PROPERTY TAX RELIEF RAISES TAXES FOR LOW- AND MIDDLE-INCOME HOUSEHOLDS



Source: MECEP analysis of Maine Revenue Services Maine Residents Property Tax and Rent Refund Program data

### 2 Less Money for Towns and Cities

Another way the governor and legislature paid for income tax cuts was by eliminating more than \$84 million in state aid to towns and cities, known as revenue sharing, over the two-year state budget.<sup>7</sup> Property taxes will rise as a result since these funds are intended to directly reduce property taxes assessed by towns and cities. They also help pay for road maintenance, fire and police protection, recycling and solid waste disposal, and other services households and businesses need.

These state cuts are part of a trend that has shifted more of the costs of services onto

towns and cities. Figure 4 shows how the legislature has cut aid to towns and cities by siphoning money from the municipal revenue sharing fund.

Towns and cities respond to revenue shortfalls by cutting spending, reducing reserves, or increasing fees or property taxes. After four years of recession and stagnation, local governments have already deeply cut spending on services like libraries and recreation programs. Property tax increases are more likely as residents balk at cuts that require firing teachers, taking cops off the street, or deferring road maintenance.

The property tax increases that result from these cuts to state support will fall hardest on low- and lower middle-income Mainers. To illustrate, if local governments use property tax increases to cover 50% of the legislature's \$44 million raid on revenue sharing, households with annual incomes between \$20,000 and \$27,000 would see their property tax bills go up by about \$16 on average (Figure 5). High-income Mainers would also see an increase, but it would represent a smaller percentage of their incomes.

4. See the appendix for a table of income groups used in Figures 3 through 9.

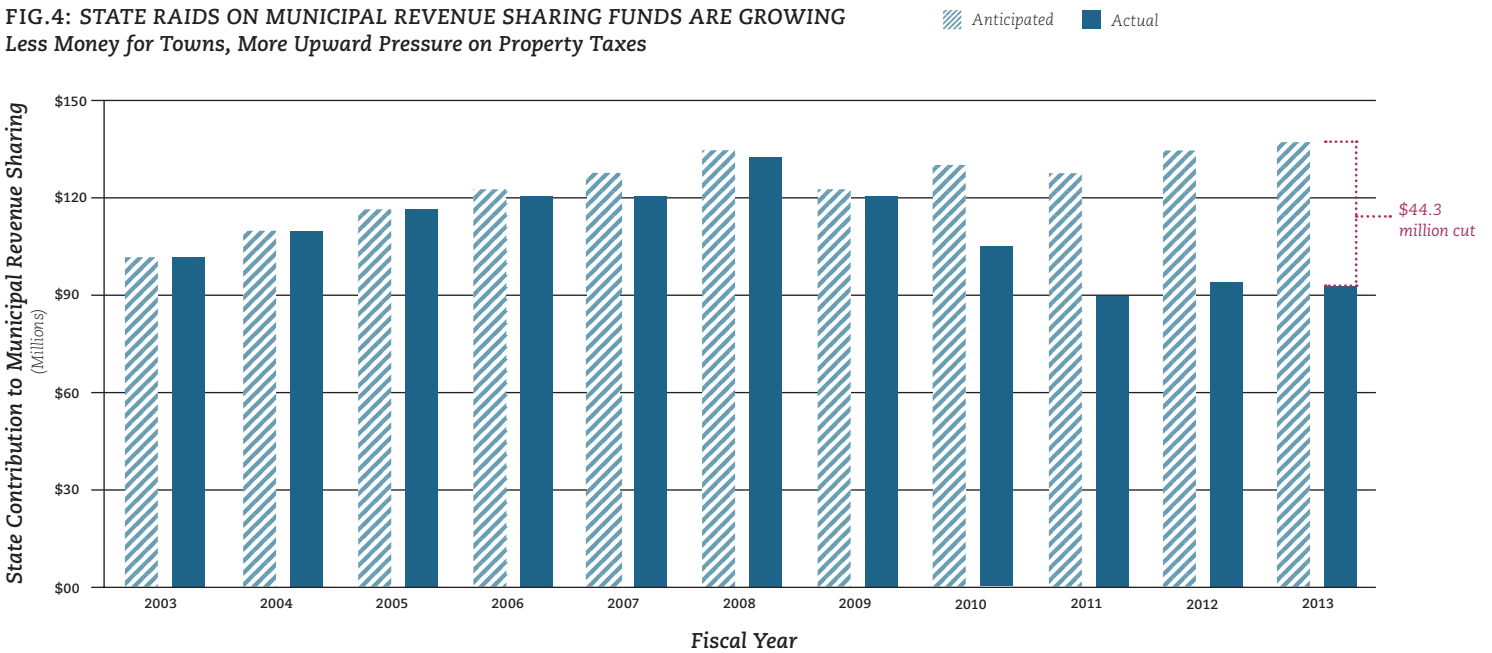
5. MECEP analysis of Maine Revenue Services Maine Residents Property Tax and Rent Refund Program data.

6. MECEP analysis of 2011 Economic Development Incentives Report ([https://www.maine.gov/revenue/research/edic\\_rep11.pdf](https://www.maine.gov/revenue/research/edic_rep11.pdf)).

7. Maine Legislature, Office of Fiscal and Program Review.

8. Maine Revised Statutes, Title 36, § 714 (<http://www.mainelegislature.org/legis/statutes/36/title36sec714.html>).

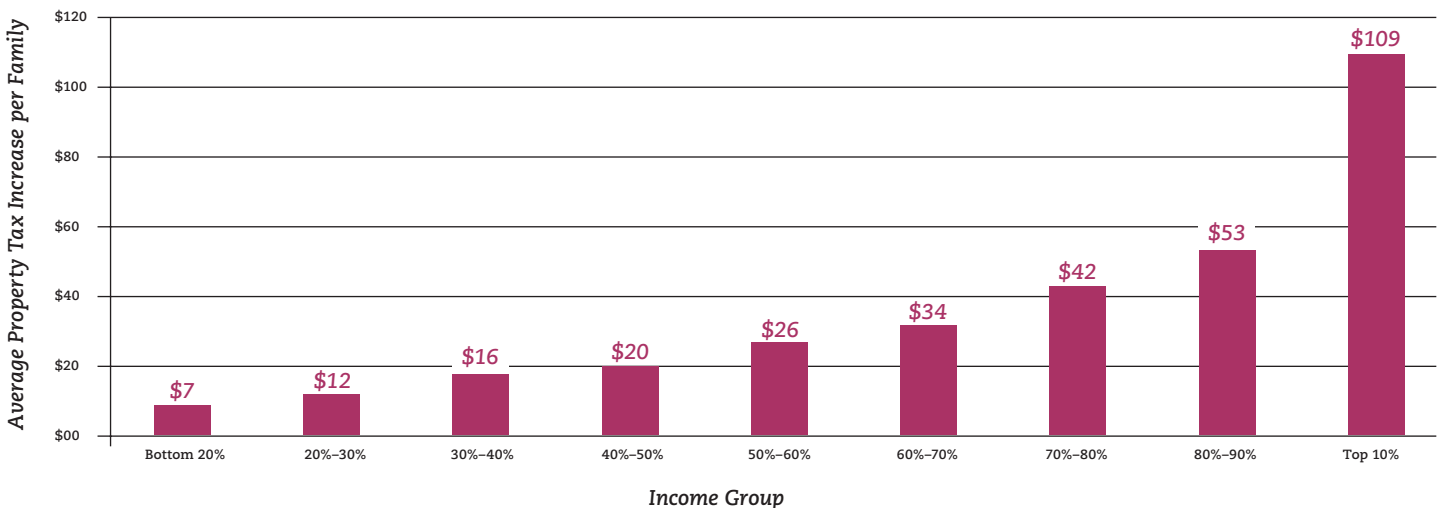
**FIG. 4: STATE RAIDS ON MUNICIPAL REVENUE SHARING FUNDS ARE GROWING**  
Less Money for Towns, More Upward Pressure on Property Taxes



Source: Maine Legislature, Office of Fiscal and Program Review  
Note: "Anticipated" state contribution to municipal revenue sharing is defined by law (PL 1987, Ch. 737).

These state cuts are part of a trend that has shifted more of the costs of services onto towns and cities... property taxes will rise as a result since these funds are intended to directly reduce property taxes assessed by towns and cities.

**FIG. 5: SHIFTING COSTS TO MUNICIPALITIES RAISES PROPERTY TAXES FOR EVERYONE**  
Estimated Property Tax Increases Resulting from the \$44 Million Raid on State Aid to Towns and Cities in FY 2013



Source: MECEP analysis of Maine Revenue Services and Maine Legislature, Office of Fiscal and Program Review data  
Note: This illustration assumes that municipalities raise property taxes to cover 50% of the annual loss in revenue sharing.

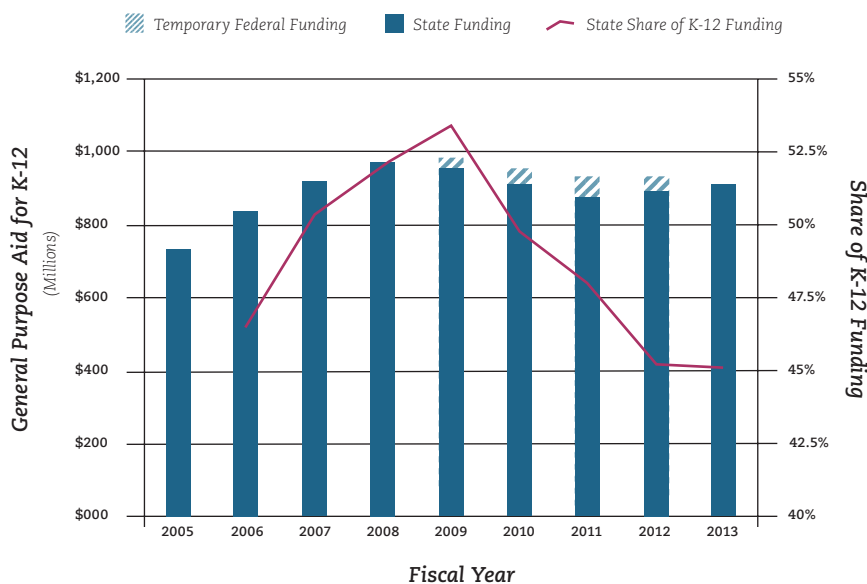
### 3 Less Money for Educating Kids

The 125th Legislature put even more pressure on property taxes by cutting funding for K-12 education.

In 2005, Maine citizens passed a law that requires the state to cover 55% of the cost of K-12 education. From FY 2006 to FY 2009 the state made progress in meeting this goal, increasing its share of funding for K-12 from 46.5% to 52.9%. Revenue drops during the recession—and lawmakers' unwillingness to temporarily raise state taxes—reversed this trend. Including temporary federal funds, Maine will contribute \$25 million less for local K-12 education in 2013 than it did in 2011 and \$76 million less than in 2009 (Figure 6). As a result, the state share of funding for K-12 will drop to 45.1% in 2013, lower than it was in 2006.<sup>9,10</sup>

While the decline in funding for K-12 began with the recession, the 125th Legislature made the problem worse by choosing to cut income taxes instead of restoring funding for schools. Across the state, schools have responded differently to the \$25 million reduction in federal and state funding from FY 2011 to FY 2013. While we don't know the exact combination of spending cuts and

FIG. 6: MAINE LAWMAKERS ARE DEFYING THE VOTER MANDATE TO FUND K-12 EDUCATION Combined State and Federal Funding Peaked in 2009



Source: Maine Department of Education  
Note: The 125th Legislature reduced the targets for the state share of K-12 funding and changed how the state share of K-12 funding is calculated, artificially increasing the apparent state share of K-12 funding. These changes were made after the Maine Department of Education published the data shown in this chart.

local tax increases that schools have used to compensate for the reduction in funding, we know that education costs continue to rise and that schools have already cut sports, music, and other programs and services over three years of recession and stagnation. To illustrate, if schools seek increased funding through

property taxes to offset 50% of the reduction in state aid, households with annual income between \$20,000 and \$27,000 would see their property tax bills go up by about \$9 on average (Figure 7). High-income Mainers would also see an increase, but it would represent a smaller percentage of their incomes.

FIG. 7: SHIFTING COSTS TO LOCAL SCHOOLS RAISES PROPERTY TAXES FOR EVERYONE  
Estimated Property Tax Increase Resulting from the \$25 Million Reduction in State Aid to K-12 Schools from FY2011 - FY2013



Source: MECEP analysis of Maine Revenue Services Tax Incidence data  
Note: This illustration assumes that communities use property tax increases to cover 50% of the cut in state and federal funding for education.

9. Maine Department of Education (<http://www.maine.gov/budget/streamlining/20111006/Education%20Spending%202010-4-11.pdf>)  
10. Note: The 125th Legislature reduced the targets for the state share of K-12 funding and changed how the state share of K-12 funding is calculated, artificially increasing the apparent state share of K-12 funding. These changes were made after the Maine Department of Education published the data cited in this report.

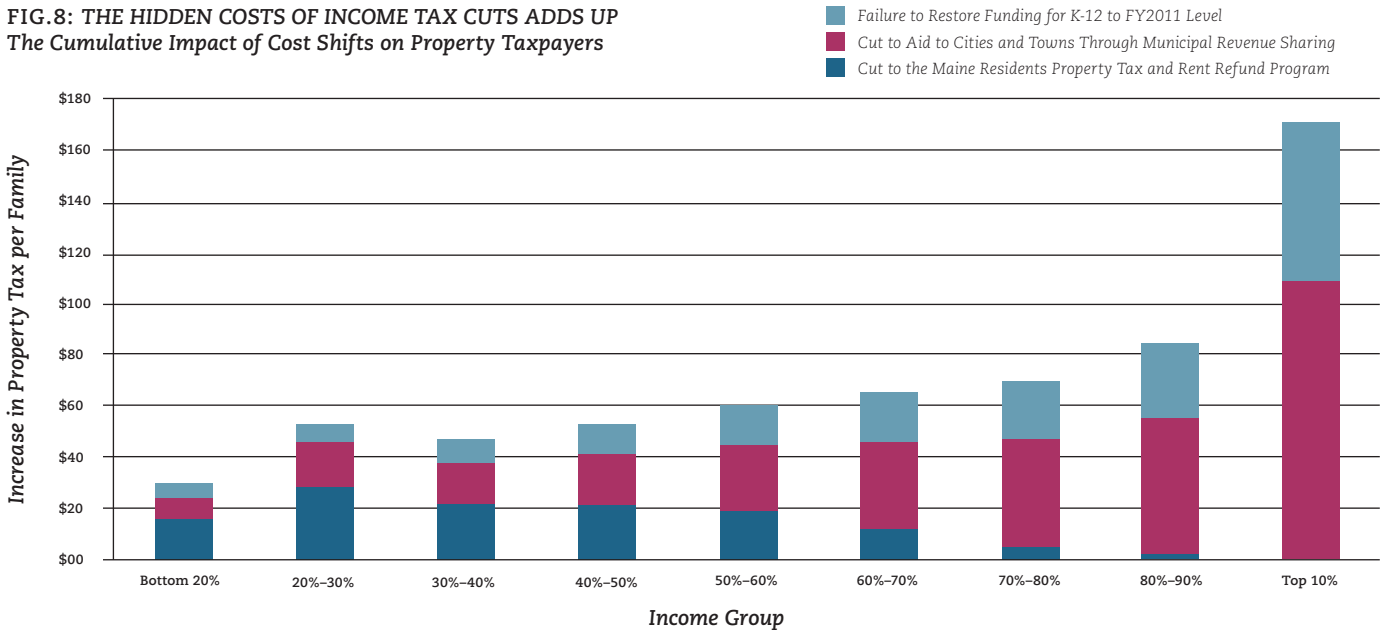
## Those Who Can Least Afford It Will Pay More

For the typical taxpayer, income tax cuts quickly add up to higher property taxes. Figure 8 illustrates the cumulative impact of reductions in property tax relief and aid to municipalities and K-12 schools. Again, the combination of spending cuts and local tax increases that local communities use to compensate for the reduction in funding varies across the state. The estimates shown here are based on the assumption that communities, on average, use property tax increases to cover 50% of the

loss. Regardless, local property taxpayers also pay for the remainder through cuts to services, increases in fees, and use of emergency reserves.

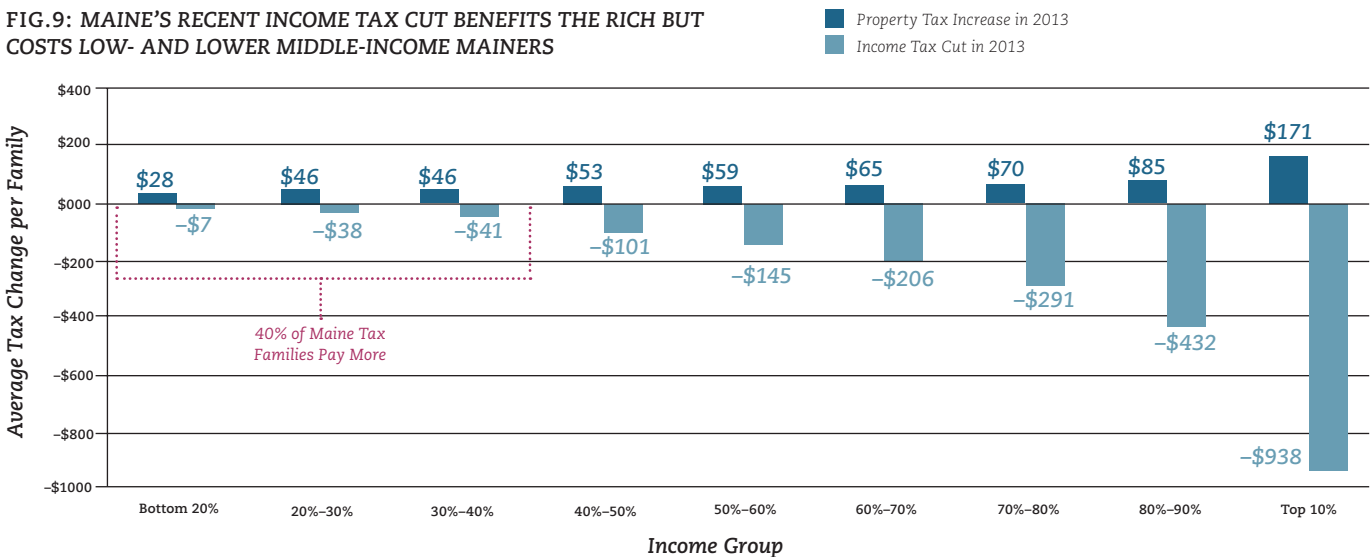
Comparing the cost of these estimated shifts with the benefits of the income tax cuts shows that 40% of Mainers (270,000 families with annual incomes of \$27,000 or less) will pay more in taxes (Figure 9).

**FIG. 8: THE HIDDEN COSTS OF INCOME TAX CUTS ADDS UP**  
 The Cumulative Impact of Cost Shifts on Property Taxpayers



Source: MECEP analysis of Maine Revenue Services Tax Incidence data  
 Note: This illustration assumes that communities use property tax increases to cover 50% of the cut in state and federal funding for education.

**FIG. 9: MAINE'S RECENT INCOME TAX CUT BENEFITS THE RICH BUT COSTS LOW- AND LOWER MIDDLE-INCOME MAINERS**



Source: MECEP analysis of data from Maine Revenue Services and Maine Legislature, Office of Fiscal and Program Review  
 Note: This illustration assumes that communities use property tax increases to cover 50% of reductions in state aid. It does not include the \$48 annual tax on all private health insurance policies included in the recent state health insurance reform law (PL 2011, Ch.90).



## Going Backwards

Income tax cuts reduce state revenue and force cities and towns to increase property taxes to pay for schools, road maintenance, fire and police protection, emergency assistance to families, and other basic services. Property tax increases hit low- and lower middle-income taxpayers hardest and outweigh the benefits they get from the 2011 income tax cut that mostly benefits the wealthy.

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We need an overall state and local tax system that is fair and raises enough revenue to make necessary investments in education, research and development, transportation, and other areas that will create jobs and grow our economy.

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The costs add up quickly: the overall state and local tax bill for the bottom 40% of Mainers will increase by an estimated average of \$14. These are the Mainers who can least afford to see their taxes increase and whose financial health is critical for Maine's economy.

In cities and towns that choose to raise property taxes to make up for all of the cuts in municipal revenue sharing and K-12 funding, middle-class Mainers will also see the modest benefits of income tax cuts wiped out by property tax increases. This analysis does not include the impact of cuts the 125th Legislature made to vital state and local services like health care, child care, and emergency assistance for families, or the impact of other tax cuts for Maine's wealthy, including pension and estate tax cuts (see the appendix for a summary). It also does not include the \$48 annual tax on all private health insurance policies included in the recent state health insurance reform law (PL 2011, Ch. 90).

Improving Maine's economy requires strengthening the middle class and enabling lower-income families to become middle-class families. To accomplish that, we need an overall state and local tax system that is fair and raises enough revenue to make necessary investments in education, research and development, transportation, and other areas that will create jobs and grow our economy. Most of the tax policies enacted by the 125th Legislature move Maine in the opposite direction.

## About the Authors

MECEP Executive Director **Garrett Martin** is a graduate of the University of North Carolina with a master's degree in public affairs from Princeton University. He has also worked as Director of Program Strategy at the Maine Community Foundation and as Associate Director at the Genesis Community Loan Fund and currently serves on the Community Development Advisory Committee of the Federal Reserve Bank of Boston.

MECEP Policy Analyst **Joel Johnson** has a BA in psychology from Grinnell College and an MS in resource economics and policy from the University of Maine where he specialized in econometric/statistical analysis. He has worked as an economist at the Maine State Planning Office where he served as the primary staff member for the state's Consensus Economic Forecasting Commission.

## About MECEP

The Maine Center for Economic Policy advances public policies that help Maine people prosper in a strong, fair, and sustainable economy. We advance this mission through high-quality research, analysis, citizen education, and coalition building. MECEP is an independent, nonpartisan organization founded in 1994.

## Appendix

### Income Ranges for Figures 1 and 2

Income Group	Tax Families	Income Range
Bottom 20%	134,767	Less than \$12,167
Middle 20%	134,041	\$23,374 to \$41,668
Top 1%	6,738	More than \$323,242

### Summary of Policy Changes Included in this Analysis

#### 2011 INCOME TAX CUT AND CONFORMITY WITH FEDERAL LAW

**Summary:** Reduced the tax rate for the top income tax rate from 8.5% to 7.95%, changed the 2% rate to 0%, changed the 4.5% and 7% rates to 6.5%, and amended the income tax code to conform with federal law.

**Total cost:** \$158 million in FY 2014, \$169 million in FY 2015.

**Impact:** 42.5% of the benefit goes to the top 10% of earners. Average annual tax cut for selected income groups: Bottom 20% = \$7; middle 20% = \$123; top 20% = \$685; top 1% = \$2,810.

**Source:** Maine Revenue Services and Maine Legislature, Office of Fiscal and Program Review.

#### CUT TO THE PROPERTY TAX RELIEF AND RENT REFUND PROGRAM

**Summary:** Did not restore a 20% cut in property tax relief available mostly to low- and middle-income homeowners and renters.

**Total cost to property taxpayers:** \$20 million per biennium.

**Impact:** 70% of the benefits of this program go to families earning less than \$30,000. This policy means that those families who benefit from the program will see their property taxes increase an average of \$123.

**Source:** MECEP analysis of Maine Revenue Services data.

#### CUT IN STATE AID FOR CITIES AND TOWNS THROUGH MUNICIPAL REVENUE SHARING

**Summary:** The 125th Legislature reduced the state contribution to cities and towns through revenue sharing by \$40.4 million in FY 2012 and \$44.3 million in FY 2013. This transfer from the municipal revenue sharing fund to the state's General Fund forces municipalities to increase property taxes, cut funding for services, or deplete reserves.

**Source:** Maine Legislature, Office of Fiscal and Program Review.

### Income Deciles for Figures 3 Through 9

Decile	Tax Families	Income Range
Bottom 20%	135,104	Less than \$14,246
20%–30%	67,515	\$14,246 to \$20,399
30%–40%	67,538	\$20,399 to \$27,312
40%–50%	67,543	\$27,312 to \$35,211
50%–60%	67,535	\$35,211 to \$47,255
60%–70%	67,540	\$47,255 to \$62,920
70%–80%	67,539	\$62,920 to \$83,783
80%–90%	67,539	\$83,783 to \$119,420
Top 10%	67,540	More than \$119,420

### Other Major Changes Not Included in this Analysis

#### PENSION TAX CUT

**Summary:** Maximum amount of tax exempt retirement income increased from \$6,000 to \$10,000 and definition of retirement income expanded to include taxable individual retirement account income.

**Total cost:** \$8 million in 2014, \$22 million in FY 2015.

**Impact:** 32% of the benefit goes to the richest 10%. Average tax cut for selected income groups: Bottom 20% = \$0.02; middle 20% = \$16; top 20% = \$89; top 1% = \$77.

**Source:** Maine Revenue Services and Maine Legislature, Office of Fiscal and Program Review.

#### ESTATE TAX CUT

**Summary:** Increased the estate tax exemption to \$2 million from \$1 million.

**Total Cost:** \$24 million in FY 2014, \$27 million in FY 2105.

**Impact:** Will cut taxes for about 550 estates of \$1 million or more.

**Source:** Maine Revenue Services and Maine Legislature, Office of Fiscal and Program Review.

#### LD 849 (2012 INCOME TAX CUT)

**Summary:** Uses 20% of any annual surplus revenues to reduce the top income tax rate to 4% over time.

**Total cost:** \$604.5 million per year when fully implemented.

**Impact:** 60% of the benefit goes to the richest 10%. Average annual tax cut for selected income groups: Bottom 20% = \$1; middle 20% = \$241; top 20% = \$3,456; top 1% = \$21,638.

**Source:** Maine Revenue Services.