

Moving Maine Students to the Head of the Class

Shoring up state funding for schools by cleaning up Maine's tax code will promote opportunity for all Maine children

Introduction

Good schools are a cornerstone for a strong economy and thriving communities. In recent years, costly and poorly targeted income tax cuts reduced Maine's capacity to fund schools. Shortchanging schools at the state level is a recipe for increasing inequality between Maine's communities and hampers our ability to educate a workforce that is prepared to grow the economy.

As the state shifts more education costs onto towns, deficient state education funding forces communities throughout Maine to make up the difference by raising property taxes or cutting funding for schools and other services. Communities with more property wealth have greater capacity to make up the difference in funding by raising property taxes. Communities with less property wealth do not and are more likely to respond with both increases in property taxes and cuts that enlarge class sizes and limit academic and enrichment opportunities for students. When some communities have weakened capacity to help their students acquire the education and skills necessary to succeed in the future workforce, learning inequities widen, future earnings decline, and the economy suffers.

This November, Maine voters will consider a ballot initiative (Question 2) that rolls back recent tax breaks for the wealthy and dedicates this revenue toward additional state level resources for schools. In this brief, the Maine Center for Economic Policy explores the context for this initiative, its potential to promote tax fairness, and its capacity to improve educational outcomes and workforce readiness of Maine students.

The Maine Center for Economic Policy finds that a three percent tax on income above \$200,000 dedicated to K-12 education will increase state funding for schools, promote tax fairness, help promote greater opportunity for low-income students, and level the playing field between property-poor and property-rich towns. It will have a positive impact for students, businesses, and Maine families, strengthening Maine's economy.

State Education Funding Falls Short

In 2004, Maine voters passed a ballot initiative pledging the state to fund 55 percent of the statewide cost of educating students to Maine's proficiency standards.¹ The initiative aimed to create a better school funding balance between property taxes collected at the local level and income and sales taxes collected by the state.

Moving Maine Students to the Head of the Class

Since Mainers voted to enact this measure, the state’s share of education funding peaked at 52.86 percent in 2009 and has since declined to 47.18 percent for fiscal year 2017.²

As the state’s contribution to education has decreased, local costs have increased. Since 2011, communities have had to raise over a billion dollars in property taxes—an average of \$180 million each year—toward education to compensate for the state underfunding its share of education costs.

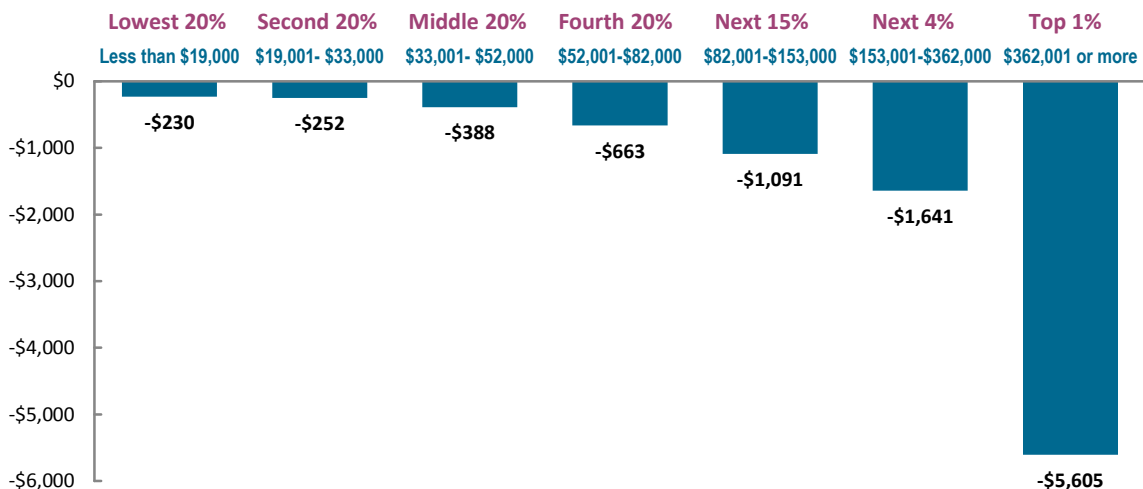
Since 2011, communities have had to raise over a billion dollars in property taxes – an average of \$180 million each year—toward education to compensate for the state underfunding its share of education costs.

Tax Giveaways to the Wealthy Are Largely to Blame

Tens of millions of dollars in recent tax breaks drive the reduction in the share of state education funding. Not only do these cuts predominately benefit wealthy Mainers, they compromise state capacity to invest in education. Since 2011, wealthy families in Maine have benefited from two decreases in their top income tax rate that gave them tax breaks much larger than the income tax breaks for low- and moderate-income Mainers. During the same period state sales tax increases, which disproportionately impact low- and moderate-income Mainers, offset some but not all of the revenue loss.

Wealthy Mainers Will Receive Largest Tax Breaks in 2017

Average household change in combined income and sales taxes since 2011 by income group



Data Source: Institute on Taxation and Economic Policy (ITEP)

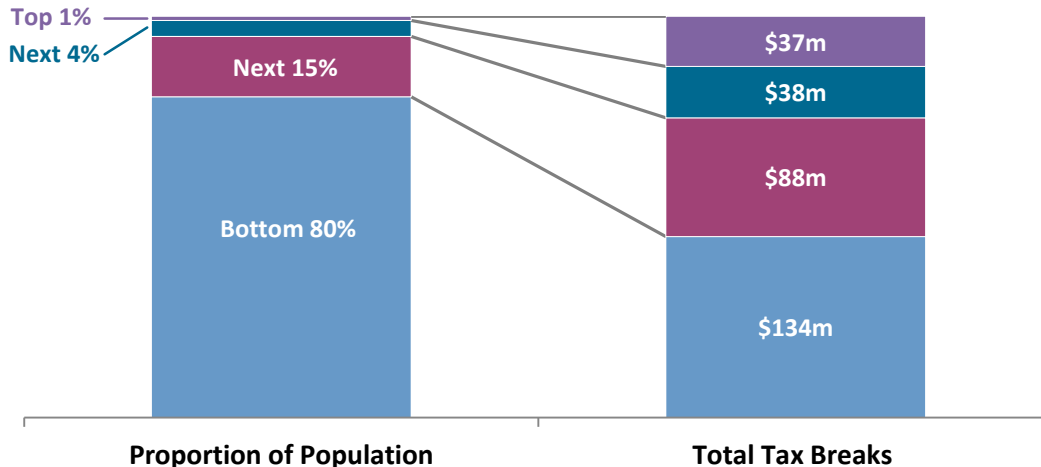
The combined effect of these tax cuts is a \$163 million dollar tax break for the top 20 percent of Maine households each year, and a \$37 million tax break for the top one percent of Maine households each year. These tax breaks have reduced state revenue compared to 2011 levels, leading to state funding cuts for

Moving Maine Students to the Head of the Class

education and revenue sharing for Maine communities.³ In 2017, as a result of these income tax cuts since 2011, Mainers will lose \$297 million in state revenue that would be available for education funding and other priorities.

Millions of Dollars in Lost Tax Revenue Will Fund Tax Breaks that Disproportionately Benefit Maine's Wealthiest Families

In 2017, income and sales tax changes from 2011 and 2015 will result in \$297 million in lost revenue, \$163 million of these tax breaks will benefit the wealthiest 20% of Maine households.



Data Source: Institute on Taxation and Economic Policy (ITEP)

State Education Funding Shortfalls Have Far-reaching Consequences

Maine's economic future hinges on providing a quality education for all students that prepares them to adapt and succeed in the modern workforce. A highly skilled and educated workforce is essential to attracting investment in Maine from new employers and meeting the needs of our existing employers. The current state education funding shortfall jeopardizes the ability of schools to meet student needs, threatens Maine's ability to fulfill employers' expectations, and undermines Maine's future economic prospects.

Widening the Opportunity Gap between Students

Low-income communities tend to have less capacity to absorb rising local costs associated with the state's reduction of its share of education funding. These communities have smaller property tax bases and many face other increasing costs for local services such as road maintenance, police, and fire protection due to state revenue sharing cuts. As the state shifts more costs to the local level, communities with less capacity to make up the difference fall further behind in the opportunities and supports they provide to their students and residents.

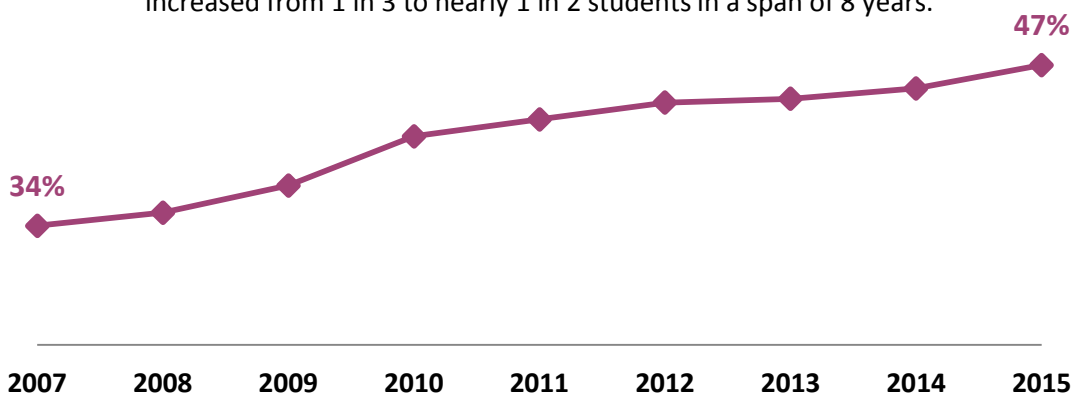
As the state shifts more costs to the local level, communities with less capacity to make up the difference fall further behind in the opportunities and supports they provide to their students and residents.

Moving Maine Students to the Head of the Class

Maine communities with higher levels of low-income students spend less per student on average than communities with fewer low-income students.⁴ Furthermore, schools with higher rates of students living in poverty have lower test scores.⁵ This is particularly troubling since the proportion of low-income students—as measured by those eligible for free or reduced lunch—has grown significantly in recent years. Since 2007, the percent of Maine’s low-income students increased 13 percentage points from 34 to 47 percent.⁶

Percent of Low-Income Students on the Rise in Maine

The proportion of Maine students receiving free or reduced price lunch increased from 1 in 3 to nearly 1 in 2 students in a span of 8 years.



Data Source: Maine Department of Education

As the proportion of Maine’s low-income students approaches one out of two students, current resources are inadequate to ensure that all students are able to meet the state’s proficiency standards. Even as the share of low-income students has increased, per student state formula funding in 2014 has decreased below 2008 levels.⁷ On its current trajectory, the state will provide an even smaller share of funding needed to meet basic education standards and will further widen existing opportunity gaps.

As the proportion of Maine’s low-income students approaches one out of two students, current resources are inadequate to ensure that all students are able to meet the state’s proficiency standards.

Federal Title I funding is available to supplement schools with high proportions of low-income students to help improve education quality. In Maine, however, Title I funds are offset in the funding formula, penalizing low-income communities instead of offering additional resources that help mitigate disparities in learning opportunity for students from low-income families.

Maine's Education Funding Formula

In 2006, Maine moved to an education funding system intended to provide adequate resources to schools to achieve learning results in a manner that promotes equity in the distribution of resources among school districts. The funding formula is based on a three-step process.

Step 1: Determine Education Costs

The state estimates the total cost of teachers, administrators, facilities, and supplies that each district will need to achieve state learning standards. This includes the costs of pre- kindergarten, vocational-technical, and career and college readiness programs. Together these costs are called 'essential programs and services' (EPS). Some students, like those with limited English proficiency, special education students, and low-income students, require more resources to achieve learning standards, and the formula apportions more funds for these students to account for their higher cost of learning. Because this formula only determines costs necessary to meet learning standards, it does not include certain costs like sports programs and school lunch in the cost estimates, which must be funded by other means.

Step 2: Calculate Local Property Tax Contribution Based on the Availability of State Funds

As part of the state budgeting process, lawmakers appropriate funds for education. The difference between what is required to fund EPS costs and what the state provides is the amount to be raised from property taxes. Passage of a 2004 ballot initiative requires the state to fund 55 percent of the cost of education, though the current state share is less than 48 percent. Based on statewide property valuation, the state then calculates a statewide property tax rate required to fund schools at the local level.

Step 3: Allocate State Funds Based on Each Town's Ability to Cover Education Costs

To determine the amount of state funding each school district receives, the state compares the amount of revenue expected to be raised locally applying the statewide property tax rate against what the local share of EPS costs are. High property value towns that are able to raise the total local EPS cost with a property tax rate lower than the one required by the state receive a smaller share of funding from the state relative to total costs. Districts that are unable to fund their EPS costs with the required property tax rate receive a greater share of funding from the state. This adjustment is an important reason why Maine is considered to have one of the more equitable funding systems for education in the country.

Putting Education Quality at Risk

Education quality is not tied to a single factor, but funding levels play a critical role, especially for low-income students. Availability of funding often heavily influences decisions to add new programs, invest in teacher professional development, and hire more staff. On average, low-income students who attend better funded schools are more likely to graduate, earn higher incomes, and are less likely to live in poverty as adults.⁸

When the state decreases its share of education costs, the amount that communities are expected to contribute—the required property tax rate—increases. Maine's current school funding formula distributes a larger share of education costs to towns with the least ability to fund their education costs through property

Moving Maine Students to the Head of the Class

taxes. However, when the formula distributes less funding, the state’s capacity to improve funding equity diminishes.

When the state decreases its share of education costs, the amount that communities are expected to contribute—the required property tax rate—increases.

In addition, communities with high property wealth, those that generally receive a smaller share of state funding, have chosen over time to allocate more funding than the state requires to their schools. Such communities spent, on average, 34 percent above the state-calculated cost of education between 2009 and 2014. This funding often supports smaller class sizes, retention of professional staff, and more generous enrichment opportunities for students. By contrast, many property-poor towns have had to implement larger property tax increases over this same time period to maintain education funding levels at just 6 percent over the state calculated costs on average.⁹

Hurting Employers who Struggle to Find Workers with the Skills their Business Needs

Statewide investment in education that enables all schools to provide quality education is not only important to promote pathways to opportunity for all students, it is essential to meet the workforce needs of employers throughout Maine. Great schools create positive “spillover” effects that are not limited to the communities in which they are located. For example, better schools produce graduates who enter the workforce at higher rates. And these graduates don’t just work in their hometowns, spreading the economic benefit of their higher incomes and family spending throughout the state.¹⁰

As Maine employers struggle to attract and retain skilled workers, high school seniors face a new economic reality—they need more skills than previous generations did to gain entry into the workforce. Demand for skilled workers with post-secondary education—defined to include anything from industrial skill certification to a graduate degree—is on the rise.¹¹ Employers rely on the K-12 system to enhance students’ ability to meet the needs of a modern workforce.

The need for modern skills combined with increasing proportions of low-income students has heightened the importance of providing adequate state resources to support the delivery of quality education and prepare all Mainers to succeed beyond high school.

Compromising the Fairness of Maine’s Tax System

To compensate for income tax cuts since 2011, Maine’s tax system is now more reliant on sales and property taxes to fund services. At the same time, targeted property tax relief for low-income homeowners and renters has diminished, making an already unfair tax system even less fair. Low- and middle-income Mainers pay a greater share of their income in state and local taxes than wealthy Mainers.

It will take more time for the effects of recent income tax cuts to ripple through Maine’s tax system, but the experience of other states suggests that deep cuts to income taxes lead to increased reliance on taxes that

Moving Maine Students to the Head of the Class

require low- and moderate-income households to pay a disproportionate share of their income in taxes. States with the least fair tax codes in the country tend to rely heavily on more regressive taxes like sales and property taxes. For example, in Washington and Florida, which do not have an income tax, state and local taxes as a share of income for the bottom 20 percent of households is seven times higher than for the top one percent of households. Middle-income families in these states pay state and local taxes as a share of income at a rate that is four times higher than the top one percent.¹² While Maine's income tax helps make our tax system relatively more fair than Washington or Florida, low- and middle-income Mainers still pay a greater share of their income in taxes than the wealthy, and income tax cuts accompanied by increased reliance on sales and property taxes are likely to increase this disparity.

Increased reliance on property taxes to fund local services will likely result in a tax system less favorable to most Maine businesses.

In 2013, property taxes made up over half of all state and local taxes collected from businesses.¹³ Increased reliance on property taxes to fund local services will likely result in a tax system less favorable to most Maine businesses. Businesses owe income taxes based on their profitability—businesses with higher profits owe more income taxes and pay income taxes at higher rates than businesses with a low or no annual profit margin. By contrast, a business owes property taxes regardless how much profit it generates. While many small business owners got an income tax cut in recent years, the reality for many is that property tax increases more than offset the value of their lower income tax. This is particularly true for small businesses with multiple locations. More research is needed to assess the full impact, but recent efforts to cut Maine's income tax under the guise of boosting business development in the state do not account for these other tax increases.

Making it Harder for Communities to Thrive

Ultimately shortchanging schools at the state level has a wide range of negative consequences for Maine students, businesses, and communities. Shifting more of the cost for education to property taxpayers—the chief revenue source for municipalities—will engender greater inequality between Maine's students and towns. Those communities that can absorb these cost shifts to maintain education quality and local services will. Communities that cannot, will not. Over time, communities with limited economic activity, declining population, or poor performing schools will find it even harder to keep pace.

Taxing the Top Two Percent to Boost State Funding for Education

The ballot question before Maine voters would establish a fund dedicated for K-12 classroom instruction paid for by a three percent tax on household income over \$200,000. For example, a household with an annual income of \$201,000 would pay the three percent only on the last \$1,000 of income for a \$30 tax increase. This initiative would increase funding for education by \$159 million in its first year and is forecast to increase thereafter.¹⁴ The state would distribute the funds raised to public schools across Maine through the state education funding formula. It would also bring the state closer to the 55 percent mandated state funding

Moving Maine Students to the Head of the Class

share, offer property tax relief to communities across the state, and help to level the playing field between the wealthy and everyone else. While an increase in education funding is not a panacea for solving all the challenges faced in Maine’s education system, it is an important step in the right direction.

Over \$150 Million Each Year to Improve Student Learning

The ballot initiative will increase state funds available for education and help local municipalities invest more in their students and in their communities. The additional tax revenue gives lawmakers more money to invest in education and must go to support direct student learning. Schools may not use the funds generated from this initiative for administrative or clerical staff.¹⁵

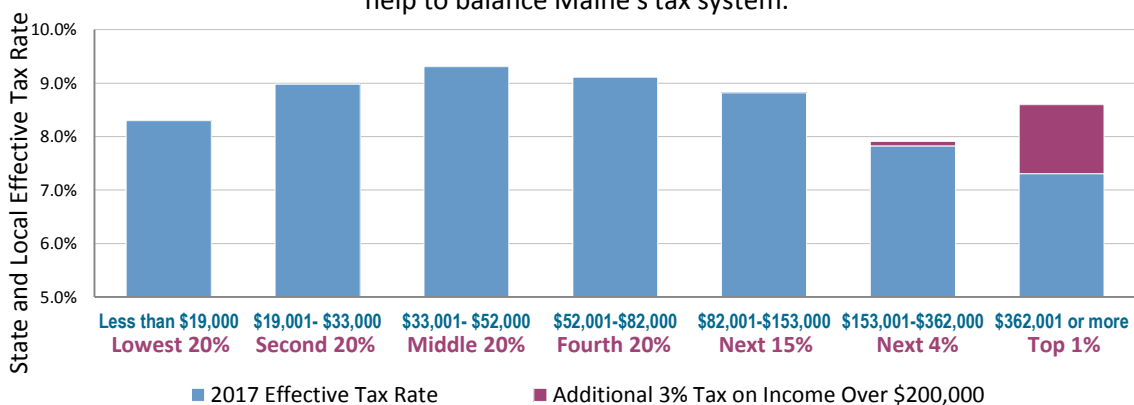
To ensure that lawmakers do not use these funds to supplant existing allocations of state funding to schools, the initiative requires lawmakers to first fund schools using available resources through the general fund. Once this is done, the Department of Education will allocate the revenues raised through the initiative according to the current school funding formula adding those dollars to the appropriation made by the legislature. Assuming the legislature maintains current levels of general fund spending on K-12 education, the additional dollars from this initiative mean the required property tax rate that towns must raise to provide a basic education will go down, freeing up town revenue to invest more in enrichment programs like foreign languages, pre-kindergarten, and career training, among others.

Improved Fairness in Maine’s Tax Code

The ballot initiative will make Maine’s tax code fairer by increasing taxes only on the wealthiest Mainers who benefited most from recent tax cuts. The 20 percent of Mainers with the lowest household incomes currently pay a higher proportion of their income in total state and local taxes than the wealthiest one percent of Mainers. Increasing taxes on the wealthiest two percent of Mainers will ensure they pay their fair share. It will not increase taxes on households with income below \$200,000.

Improved Tax Fairness for Maine Families

Under current law, wealthy families pay the lowest effective tax rate in combined state and local taxes. A 3% tax on income over \$200,000 would help to balance Maine's tax system.



Data Source: Institute on Taxation and Economic Policy (ITEP)

Greater Potential to Meet the Needs of All Maine Students

Additional state funding dedicated to K-12 education will have a more pronounced impact on lower income communities in terms of increased state share of education cost. Increased state funding for their schools will enable these towns to invest in additional learning resources for their students. More resources may also allow lawmakers to improve the state's administration of federal Title I funds so that the federal funds truly supplement rather than supplant existing state and local resources. The fact that this could not be done before without raising taxes, cutting spending elsewhere in the budget, or reducing funding to some communities is a major reason problems with Title I funding persist. Redirecting Title I funds to provide additional support to communities with high need makes sense and can be done in concert with the implementation of this ballot initiative with a win-win outcome for all communities and students.

Improved Equality among Maine's Regions

The economic value of a strong education system is greatest when all communities in Maine benefit from the improvements it brings to the workforce and business environment. Increasing state funding will increase capacity for all Maine communities to afford a high quality K-12 education that prepares students to succeed in the classroom and the workforce. It will build a stronger economy throughout Maine.

Conclusion

Mainers know that a sound, first-rate education is the gateway to good jobs, more prosperous families, and greater opportunity for successful careers. Mainers also appreciate that we all benefit when workers have the education and skills employers need to keep pace with changing technologies, to expand and open new businesses, and to remain competitive in the global marketplace. And Mainers understand that a well-funded K-12 education system is essential to robust economic growth and thriving prosperity in which we all share.

MECEP's research and analysis confirms that the proposed education funding initiative on the November ballot would raise crucial revenue for K-12 education in Maine at a time when state spending as a share of education costs and equity in public education between property-rich and property-poor communities is down. This additional revenue will expand equitable access to quality education for all students, improve the fairness of Maine's state and local tax system, and provide the resources for state and local lawmakers to invest in quality education for all Maine students.

Acknowledgments

The Maine Center for Economic Policy (MECEP) provides citizens, policy-makers, advocates, and media with credible and rigorous economic analysis that advances economic justice and prosperity for all Maine people. MECEP is an independent, nonpartisan organization founded in 1994.

About the Author

Sarah Austin is MECEP's policy lead on tax and budget issues and is a skilled policy researcher and analyst. She holds a master's of public affairs from the University of Wisconsin-Madison's La Follette School of Public Affairs and a bachelor's of science in environmental policy from Maine's Unity College.

Research Support

MECEP partnered with the Institute on Taxation and Economic Policy (ITEP) to estimate the costs and distributional effects of recent and proposed changes to Maine's tax system. ITEP has engaged in research on tax issues since 1980 and, in 1994, built a microsimulation model of the tax systems of the U.S. government and of all 50 states and the District of Columbia.

Funders

This brief is published with the support of general operating support from the Charles Stewart Mott Foundation, Ford Foundation, Elmina B. Sewall Foundation, and individual contributions.

End Notes

¹ Maine Revised Statutes, Title 20-A: Education, ch. 608, §15752. Available at: <http://www.mainelegislature.org/legis/statutes/20-A/title20-Ach608.pdf>

² Maine Department of Education. 2016. *Education Funding Graph*. Available at: <http://www.maine.gov/education/data/eps/epsmenu.htm>

³ The state distributes a share of total income and sales tax receipts to towns to ease local property taxes. This is known as municipal revenue sharing. Legislators have gradually cut municipal revenue sharing over the past ten years.

⁴ Lawrence O. Picus, et al. 2013. *An Independent Review of Maine's Essential Programs and Services Funding Act: Part 1*. Prepared for Maine Legislature's Joint Standing Committee on Education and Cultural Affairs. Available at: [http://www.maine.gov/legis/opla/EPSReviewPart1\(PicusandAssoc%20\)4-1-2013.pdf](http://www.maine.gov/legis/opla/EPSReviewPart1(PicusandAssoc%20)4-1-2013.pdf)

⁵ David L. Silvernail, et al. 2014. *The Relationship between School Poverty and Student Achievement in Maine*. Available at: http://digitalcommons.usm.maine.edu/cgi/viewcontent.cgi?article=1000&context=cepare_funding

⁶ Maine Department of Education. *Students Eligible for Free/Reduced Price Lunch*. Available from the Maine DOE Data Warehouse at: http://dw.education.maine.gov/DirectoryManager/Web/maine_report/MaineLanding.aspx

⁷ Per pupil state formula spending is down 4% when compared to inflation adjusted spending for the 2008 school year. See pre-federal funding levels and enrollment data available at: <http://www.maine.gov/education/data/eps/epsmenu.htm>; http://dw.education.maine.gov/DirectoryManager/Web/maine_report/MaineLanding.aspx

⁸ C. Kirabo Jackson, Rucker C. Johnson, and Claudia Persico, "The Effects of School Spending on Educational and Economic Outcomes: Evidence from School Finance Reforms," *Quarterly Journal of Economics*, October 1, 2015. See also Bruce Baker, "Does Money Matter in Education?" second edition, Albert Shanker Institute, 2016, <http://www.shankerinstitute.org/resource/does-money-matter-second-edition>

⁹ These estimates compare towns with property value per student ratios in the highest quartile against those in the lowest quartile by local spending over EPS and mill rate change in property tax rate. Town valuations are available from Maine Department of Education at: <http://www.maine.gov/education/data/stateevaluation/statevalmenu.htm>; Student Enrollment data is available at Maine Department of Education's Data Warehouse at: http://dw.education.maine.gov/DirectoryManager/Web/maine_report/MaineLanding.aspx; Spending as a percent of EPS data is available from Maine Department of Education at: <http://www.maine.gov/education/data/eps/epsmenu.htm>; Property tax rates are available from Maine Revenue Services at: <http://www.maine.gov/revenue/propertytax/municipalservices/fullvaluerates.pdf>

¹⁰ Thomas L. Hungerford and Robert W. Wassmer. 2004. *K-12 Education in the U.S. Economy: Its Impact on Economic Development, Earnings, and Housing Values*. National Education Association Working Paper. Available at: <http://files.eric.ed.gov/fulltext/ED490870.pdf>

¹¹ By 2020, 65% of jobs nationally are projected to require post secondary education compared to only 28% of jobs in 1973. See more at- Anthony P. Carnevale, Nicole Smith, and Jeff Strohl. 2013. *Recovery: Job Growth and Education Requirements through 2020*. Available at: https://cew.georgetown.edu/wp-content/uploads/2014/11/Recovery2020.FR_Web_.pdf

¹² The Institute on Taxation and Economic Policy. 2015. *Who Pays? A Distributional Analysis of the Tax Systems in All 50 States. Fifth Edition*. Available at: <http://www.itep.org/pdf/whopaysreport.pdf>

¹³ Andrew Philips, et al. 2014. *Total State and Local Business Taxes: State-by-state estimates for fiscal year 2013*. Available at: <http://www.cost.org/WorkArea/DownloadAsset.aspx?id=87982>

¹⁴ Maine Office of Fiscal and Program Review. 2016. Fiscal Note of LD 1622 prepared for the 127th Maine Legislature. Available at: https://legislature.maine.gov/legis/bills/bills_127th/fiscalpdfs/FN166001.pdf

¹⁵ The legislative language upon which this ballot question is based can be found at: <http://maine.gov/sos/cec/elec/citizens/k12.pdf>