

Testimony neither for nor against LD 513, An Act to Eliminate the State Income Tax for Maine Public Employee Retirement System Pensions

Good afternoon Senator Dow, Representative Tipping-Spitz and honorable members of the Taxation Committee. My name's Sarah Austin, a policy analyst at the Maine Center for Economic Policy. I'm here to testify neither for nor against LD 513, An Act to Eliminate the State Income Tax for Maine Public Employees Retirement System Pensions.

State spending, which includes tax expenditures, is a reflection of state priorities. It is important to consider not only whether the spending in question is a priority, but also the priorities like education and public health and safety that lose out when other priorities are pursued. While making sure Maine seniors are able to achieve economic security in their retirement is an important priority, this bill in its current form would ultimately deliver benefits to already economically secure seniors and come at a high cost.

This bill does surface an important issue:

- 1) Social security income in Maine is not subject to the state income tax.
- 2) Most state employees have limited or no social security income and therefore do not benefit from the exemption of social security income as much as other retirees.

As a result, a retiree whose income derives solely from MainePERs will pay a higher effective income tax rate than a retiree whose income includes social security income in excess of the current \$10,000 exemption on all retirement income. To highlight this point, I have included several scenarios with my testimony. A senior with \$15,000 of social security income and \$15,000 of pension income will pay no income tax while a senior with \$30,000 in pension income alone will pay \$250.

From these scenarios, it is important to note that because of Maine's existing personal exemption, standard deduction, and \$10,000 pension exemption, the first \$25,650 of an individual's income in retirement is not subject to income tax. For married filers, the amount is \$51,100. That means that this law would only help seniors with income over those amounts.

To address the discrepancy in the treatment of income that individuals with public employee pensions face under the current retirement system, the most cost-effective solution would be to change the existing pension exemption rules so that the first \$10,000 in MainePERS income is exempted from taxable income.

While MECEP would not oppose a change in how MainePERS income is treated under the existing pension exemption, we do have concerns about the entire elimination of state income tax for MainePERS pensions. At the very least such a proposal should be means tested and include a phase out so that funding for schools and other priorities isn't being compromised. This is important for two reasons. First, for most retirees, property and sales taxes, not income tax account for the greater share of state and local taxes paid. Any proposal that reduces income tax has the potential to shift more costs onto property and sales taxes. For many seniors, this would pose a greater hardship. Second, the primary beneficiaries of complete elimination of state income tax for MainePERS pension are likely to be wealthier households. Ultimately, these outcomes would subvert rather than enhance efforts to boost the economic security of struggling retirees and come at too high a price.

Tax Impact on Individual Tax Filers with MainePERS Income

\$30,000 Total Income	Deductions and exemptions	Current Income Tax	Proposed Income Tax	Change in Income Tax	Notes
30,000 Social Security	N/A	\$0	\$0	\$0	Social Security is not taxed
15,000 Social Security/ 15,000 Pension	\$4,050 Personal Exemption + \$11,600 Standard Deduction + \$10,000 Pension Exemption	\$0	\$0	\$0	Social Security offsets the entire pension exemption, none of the pension is exempted. Taxable income after deductions = \$0
30,000 Pension		\$252	\$0	(\$252)	Taxable income after deductions = \$4,340

\$80,000 Total Income	Deductions and exemptions	Current Income Tax	Proposed Income Tax	Change in Income Tax	Notes
15,000 Social Security/ 65,000 Pension	\$4,050 Personal Exemption + \$11,600 Standard Deduction + \$10,000 Pension Exemption	\$3,178	\$0	(\$3,178)	Social Security offsets the entire pension exemption, taxable income after deductions = \$ 49,350
80,000 Pension		\$3,536	\$0	(\$3,536)	Taxable income after deductions = \$54,350