Maine Center for Economic Policy

POLICY BRIEF

The LePage Tax Bill

On March 1, Gov. Paul LePage's Administration presented a tax bill to the Legislature designed to mirror at the state level some of the reforms enacted by passage of the Tax Cuts and Jobs Act at the federal level. The proposal is framed as simple conformity with federal law but goes much further than routine and technical updates to Maine's own tax code.

The LePage Tax Bill costs $88 million over the remainder of the current two-year budget cycle, and $115 million over the next biennium. Much like the federal law, the governor's proposal focuses on tax breaks for profitable businesses and wealthier families and offers little to low and moderate-income Mainers. For example, the bottom one-fifth of Maine households would receive a one-dollar tax cut on average under the governor's proposal.

The proposed changes, a significant rewrite of Maine's tax code, would deliver tax cuts to filers who don't need them and who are already reaping significant benefits from recent federal tax changes. Perhaps more importantly, the governor's proposal would significantly deplete available public resources, jeopardizing the state's ability to meet critical needs in education, health care, infrastructure, and other priorities identified by legislators and Maine voters.

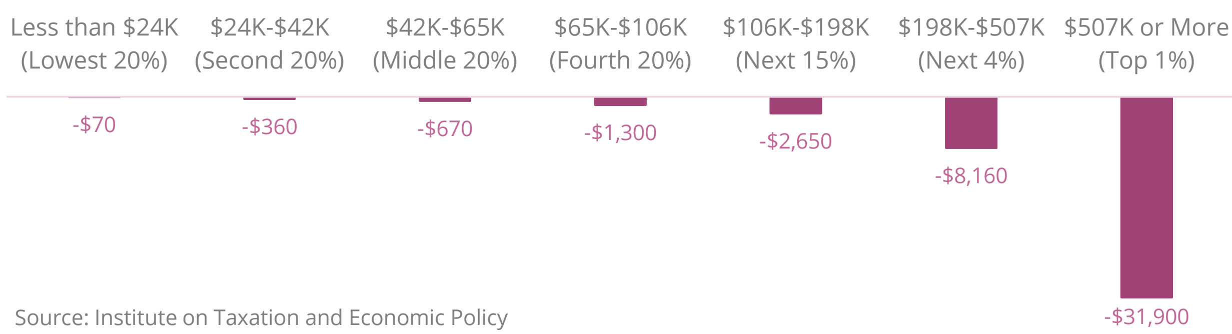
FEDERAL TAX CODE REVISIONS SET THE STAGE FOR LEPAGE TAX BILL

The federal Tax Cuts and Jobs Act, or TCJA, enacted into law and signed by President Donald Trump in December 2017, made dramatic changes to the federal tax code. The law shifts the tax base in favor of wealthier households, corporations, and pass-through entities while ultimately raising taxes on low- and moderate-income households across the country. According to a Center on Budget and Policy Priorities report based on an analysis by the Congressional Joint Committee on Taxation, households with taxable incomes under $75,000 will see a tax increase in 2027, when short-term individual tax cuts expire, while higher-income earners and profitable businesses will continue to see tax breaks because of permanent changes to tax laws affecting corporations and pass-through businesses.

Passage of the federal tax law triggered a debate in Maine about whether to update our own tax code to mirror the federal changes. The LePage Tax Bill offers one vision of how to respond to the federal law, doubling down on some provisions of the federal tax law while rejecting others.

It's important to note that no matter how Maine lawmakers dispose of the LePage Tax Bill, Maine tax filers can already expect to receive a $1 billion federal tax cut in 2019 because of the federal tax law. Just under half of these tax breaks will accrue to profitable corporations and pass-through businesses. For households, these tax breaks provide the greatest benefit to the wealthiest Mainers, according to analysis by the Institute on Taxation and Economic Policy.

Wealthiest Maine households gain tens of thousands from federal tax breaks
Federal tax change by Maine household income group, 2019



Source: Institute on Taxation and Economic Policy

THE LEPAGE TAX BILL DOUBLES DOWN ON TAX BREAKS, ALLOWING SOME PROFITABLE BUSINESSES TO AVOID PAYING INCOME TAXES ALTOGETHER

The governor's proposal mirrors the federal repeal of the corporate alternative minimum tax, or corporate AMT, which ensures profitable corporations pay some income tax even if they're able to assemble a collection of deductions, credits and other loopholes that would negate their income tax liability. Eliminating this backstop in Maine's tax code would cost the state $1.5 million next year.

The proposal also copies federal changes to a class of business tax breaks known as "accelerated depreciation," which allow businesses to more quickly write off investments in long-term assets such as vehicles, equipment, or software.

A normal depreciation schedule allows businesses to account for the way their long-term assets lose value, or depreciate, over time. Accelerated depreciation allows businesses to deduct a portion of their assets' current value faster than the asset loses value, resulting in lower taxes for that business. The federal tax law supercharged accelerated depreciation programs, including Bonus Depreciation and the Section 179 Deduction, allowing businesses to write off the entire cost of new assets in their first year. Gov. LePage proposes adopting the same reform in Maine, at a cost of $55 million this budget cycle.

Finally, the LePage Tax Bill would eliminate the state's top corporate tax rate of 8.93 percent on taxable income over $250,000 in 2020. This move would make the state's corporate tax code less progressive by moving from four brackets to three and would cost the state $14 million in the next budget cycle.

DOUBLING ESTATE TAX GIVES TAX BREAKS TO ROUGHLY 20 OF THE WEALTHIEST FAMILIES IN MAINE

The estate tax exemption shields a portion of inherited wealth from taxation. The federal tax law doubles the maximum exemption, from $11.2 million per family to $22.4 million.

Gov. LePage proposes adopting the same revision in Maine's tax code. If this change is adopted, it would make Maine's estate tax exemption more than 11 times larger than it was in 2012, when the maximum exemption for families was $2 million.

More Info: Accelerated Depreciation

The governor proposes the following changes to state-level accelerated depreciation programs:

Section 179 Deduction:

Double the limit, from $500,000 to $1 million, which would allow businesses with less than $2.5 million in depreciable assets to write-off $1 million in the first year.

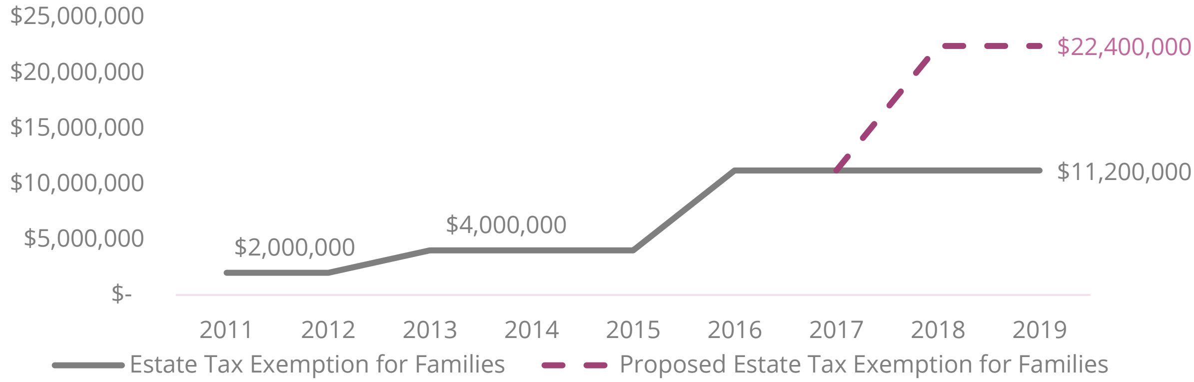
Bonus Depreciation:

Maine and Connecticut are the only New England states with any bonus depreciation program, and Gov. LePage proposes full conformity with the federal program for the first time. Full conformity will allow businesses to write-off 100 percent of any depreciable assets until 2022.

While Maine's program has historically only been available for assets located in Maine, full conformity would open the program up to out-of-state assets, **creating an $18 million tax break this budget cycle for out-of-state corporate investments.**

Growing tax breaks for multimillionaire heirs

New estate tax exemption would be more than 11 times larger than it was in 2011.



Under current law at the $11.2 million family exemption, only 20 estates each year (about one-tenth of one percent of all Maine estates) pass on enough wealth to owe any Maine estate tax, according to the Center on Budget and Policy Priorities analysis of federal tax data. Doubling the exemption amount means family estates can pass on an additional $11.2 million untaxed. This provision would cost Maine $4.5 million next year.

LEPAGE TAX BILL REPLACES PERSONAL EXEMPTION WITH PROPOSAL THAT PROVIDES GREATER BENEFITS TO WEALTHIER HOUSHOLDS

The Maine personal exemption is a deduction nearly all families use to reduce the amount of a household's income subject to tax. Households can use the exemption to lower their taxable income by $4,150 per household members, e.g. a four-person household pays no income tax on the first $16,600 of income.

The federal tax law eliminated the federal personal exemption. If the state were to repeal the personal exemption, thereby conforming to the federal tax code, Maine households would face a $233 million tax increase in 2018. The LePage Tax Bill would conform to the repeal of personal exemption and replace it with several changes to the tax code designed to shield Mainers from the ensuing tax increase.

However, the governor's approach goes beyond holding Mainers harmless by delivering larger tax cuts to more well-off households.

The governor proposes a new zero percent tax bracket that is equivalent to the value of the personal exemption – $4,150 for single filers and $8,300 for married filers. Because this bracket wouldn't phase out for high income households, as the personal exemption does, the governor’s approach delivers a new tax break to wealthier households who will benefit from the new zero percent bracket but were phased out of the personal exemption.

The zero percent bracket, though, is not enough to hold harmless those families with children and/or dependents. To address this issue, the governor proposes a $500 nonrefundable credit tied to the federal child and dependent tax credit. The credit would phase out for the same incomes that the personal exemption previously did, at roughly $400,000 for married filers.

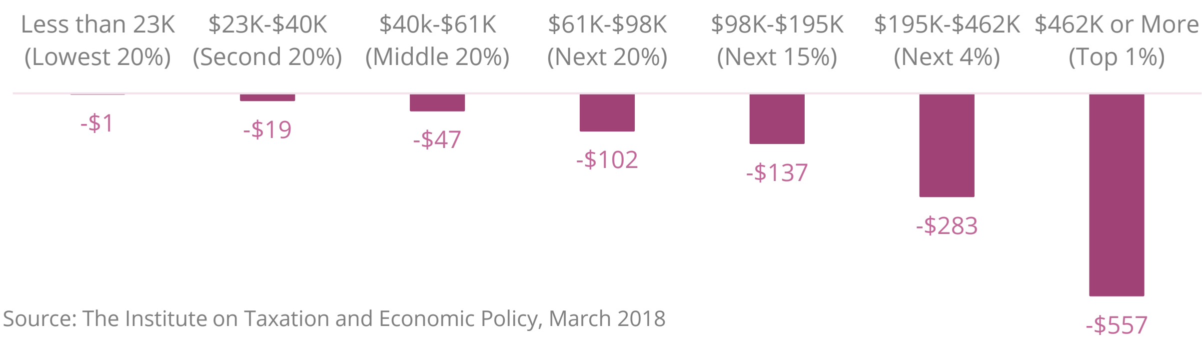
However, the nature of nonrefundable tax credits means filers with income too low to owe income tax get no benefit from this credit. So, this larger, nonrefundable credit also shifts the bulk of the benefits toward more well-off households.

The LePage Tax Bill goes one step further by proposing increased standard and itemized deductions for higher-income households. Under current law, standard and itemized deductions start to phase out for married couples with income over roughly $140,000 and single filers with income over roughly $70,000. The governor's proposal would start this phase out at $160,000 for married couples and $80,000 for single filers.

The cumulative effect of the governor’s proposal to replace the personal exemption, skews tax breaks to the wealthiest Maine households, as demonstrated by the Institute on Taxation and Economic Policy’s analysis below.

Governor LePage's tax bill favors households at the top

Tax break for the top 1 percent eleven times larger than those for middle-income households



Source: The Institute on Taxation and Economic Policy, March 2018

Note: This analysis only includes the governor's proposed replacement for the personal exemption and leaves out other provisions of conformity impacting estate and business tax law. Included here is the proposed 0% bracket, increased standard deduction, new phase outs for standard and itemized deductions, and the $500 non-refundable child and dependent tax credit

CONCLUSION

The recent revision to Maine's revenue forecast indicates the state will have a roughly $128 million surplus this budget cycle. That surplus revenue gives policymakers much-needed flexibility not only to meet the state's current fiscal needs, but to put the state on more solid footing for the next budget cycle, when persistent shortfalls in education funding, municipal revenue sharing, and transportation infrastructure will need to be addressed.

Additionally, while the Legislature has the resources necessary to begin implementation of the voter-approved Medicaid expansion law this year, further funding is necessary for the future. According to Manatt Health, the state must appropriate roughly $30.5 million in the next fiscal year to cover its share of the biennial cost of expanded health care access for roughly 70,000 Mainers.

The governor's tax bill proposes to deplete more than two-thirds of the $128 million surplus forecast for this budget cycle to deliver tax breaks skewed to the wealthiest households. The governor's tax bill siphons resources that could be used to benefit all Maine residents through investments in schools, health care, and infrastructure. Tax breaks that disproportionately benefit high-income earners and profitable businesses are only one side of the coin. The other is an erasure of future revenue that makes it harder to meet the needs of all Maine's residents.