



Policy Brief:

Why Maine lawmakers should reject the Local Option Sales Tax

by Sarah Austin, Policy Analyst | March 29, 2019



A Local Option Sales Tax would tilt our tax code even further in favor of the wealthiest — while leaving many Maine communities, particularly rural towns, behind.

Communities in every corner of the state have suffered from underfunding of education and local services. The symptoms of cuts to communities are greater pressure on town budgets, cuts to local services and schools, and property tax increases.

Some communities have responded by pushing the state Legislature to authorize “Local Option Sales Taxes,” which would allow municipalities to increase sales taxes within their boundaries. In most proposals, the revenue created by the increase would flow directly to that municipality, rather than to the state.

A Local Option Sales Tax could raise significant revenue for some service centers and for communities heavily reliant on the tourism industry.

However, its implementation in those communities would disproportionately affect lower-income Mainers. It would deepen economic inequality by tipping our already lopsided tax code even further out of balance.

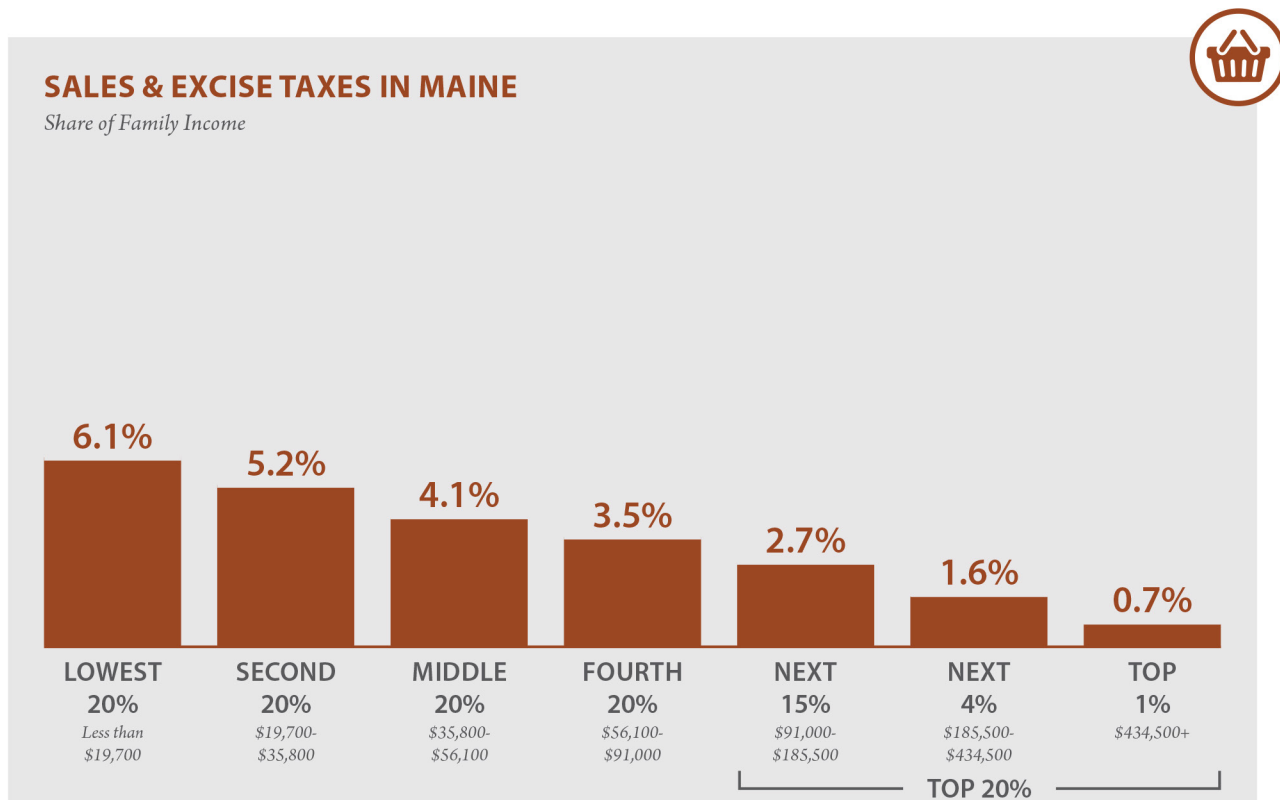
Insufficient funding for communities is a statewide problem. It deserves a statewide solution. The Local Option Sales Tax is not the answer.

A comprehensive plan to raise revenue at the state level so we can fund local schools and services is a fairer and more comprehensive solution to the challenges faced by Maine communities.

Local Option Sales Tax creates haves and have-nots

Local option sales taxes are a tool that would empower some communities while doing little — or even nothing — for others. That’s because such taxes are feasible for those municipalities with enough commerce to raise meaningful revenue but not for those communities, often rural ones, without such a sales base.

Figure 1: Sales tax is the most regressive tax in Maine



SOURCE: Institute on Taxation and Economic Policy, *Who Pays 6th Edition* analysis for Maine.
Available at: <https://itep.org/>

To illustrate this point: The ten municipalities with the highest meals and lodging sales in the state generate 45 percent of the state's meals and lodging tax revenues.

But those same ten municipalities are home to just 16 percent of the population. Similarly, the ten municipalities with the highest total taxable sales in our state generate 42 percent of all sales tax revenue but represent only 19 percent of the state's population.¹

By creating a new system of haves and have-nots, the Local Option Sales Tax would create even greater division between communities with means and those without. It would also be inadequate to meet our municipalities' needs.

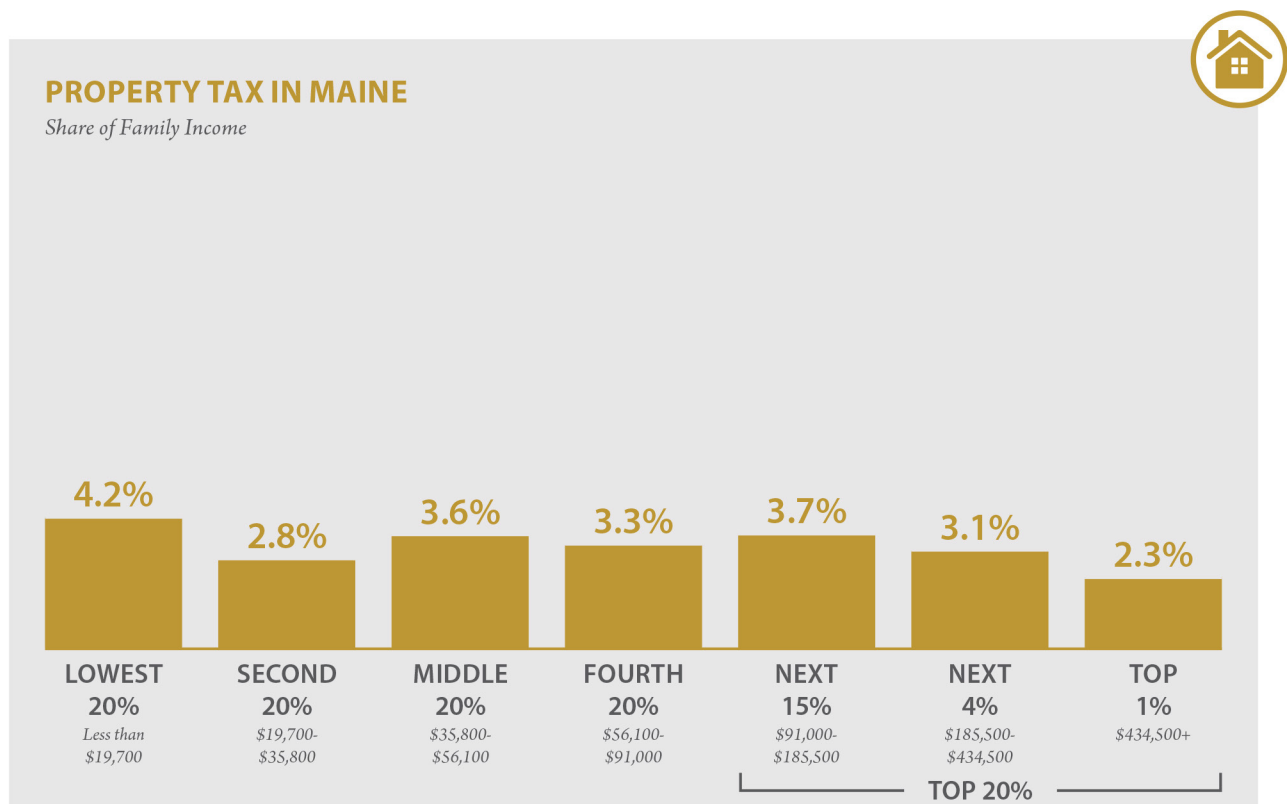
Even in the unlikely scenario where every town voted to approve a 1 percent general sales tax, they would only create \$435 million in revenue for communities during the coming two-year budget cycle.² Fully funding schools and communities on the other hand would send an additional \$520 to municipalities over the same timeframe.³

The poor pay more for sales taxes

Three of the bills before the Legislature this year would allow communities to create a general Local Option Sales Tax. For towns looking for an alternative to property tax increases, a general sales tax is a poor choice.

Both property and sales taxes hit those who earn the least more than those who earn the most. But in real terms, the sales tax affects poorer Mainers far more than the property tax. The poorest 20 percent of

Figure 2: Property tax still regressive, but pales in comparison to sales tax



SOURCE: Institute on Taxation and Economic Policy, *Who Pays 6th Edition* analysis for Maine. Available at: <https://itep.org/>

Mainers pay an effective sales tax rate that is 8.7 times higher than the top 1 percent of Mainers. Those same low-income families pay an effective property tax rate that is 1.8 times higher than the richest 1 percent (see Figure 1, opposite page, and Figure 2, above).⁴

Although a portion of a Local Option Sales Tax would be paid by tourists and residents of nearby communities, residents of the implementing municipalities would pay the tax most often and those residents with the lowest incomes would be hit the hardest.

Maine needs a statewide revenue solution

All sales taxes are regressive, but statewide increases to less regressive ones — such as the meals and lodging taxes — can be part of a solution to raising necessary revenue for our communities. But that only works if those increases are paired with progressive tax reforms, such as rate increases for the wealthiest and profitable corporations and expanded income tax credits for low- and middle-income earners.

That balancing act is only feasible and prudent at the state level. The state already has some programs to offset high property taxes for low-income residents, but the burden of local sales taxes would be much harder to offset because they are more difficult to track.

Rather than have different tax mixes across the state, lawmakers should consider meals and lodging sales tax increases as part of a larger, comprehensive revenue strategy. In doing so, they could fully fund the state's key priorities, alleviate pressure on property taxes, and create a fairer state and local tax system overall.

Fully funding education, Municipal Revenue Sharing is a good start

The state is required to disburse 5 percent of all broad-based tax revenues, such as those from the income and sales taxes, to municipalities. This disbursement, known as “Municipal Revenue Sharing,” is designed to help fund services that make our communities great places to live and to reduce the pressure on property taxes.

Fully funding the state’s existing commitments to municipalities would better support small towns while addressing the unique pressures facing Maine’s service centers.

The state is also required to fund a portion of the cost of public schools. Maine voters have used the referendum three times since 2004 to demand that the state cover 55 percent of the cost of essential programs and services in the state’s public K-12 schools.

The Legislature has never delivered a budget that met the 55 percent threshold, and Municipal Revenue Sharing has been underfunded every year since 2009. These funding cuts forced towns to reduce services, increase property taxes, or both.

The Great Recession had the state in a dire financial situation when Municipal Revenue Sharing was first cut a decade ago. However, now the state is in the peak of recovery. Legislators should find a way to return to full funding for Maine’s communities.

Fully funding Municipal Revenue Sharing and our public schools is a better solution for towns that would receive little through implementation of a Local Option Sales Tax. It also would address the unique pressures faced by service-center communities.

While most of the funds distributed through Municipal Revenue Sharing are distributed proportionately to all communities, a portion of the funds are targeted to service centers and those with higher property taxes. The formula ensures that communities receive greater aid for the greater level of services they offer to their own residents and to surrounding communities, while also making sure rural communities aren’t left behind

Conclusion

There’s no question that communities across the state are struggling to provide services and keep property taxes low. However, a Local Option Sales Tax would worsen inequality within and between communities.

A comprehensive statewide solution to our revenue challenges, one that fully funds revenue sharing and schools, is the best way to ensure residents across the state have access to high-quality services.

Endnotes

- 1 Maine Revenue Services, Annual Taxable Sales by Town 2018. Some data suppressed to maintain confidentiality.
- 2 MECEP analysis of Maine Revenue Services, Annual Taxable Sales by Town 2018. Total taxable sales adjusted for fiscal year and for inflation using the revenue forecast estimates for sales tax revenues for the 2020-2021 biennium.
- 3 This is the difference of full revenue sharing funding at 5% and school funding at 55% compared to the 2019 baseline.
- 4 Institute on Taxation and Economic Policy, Who Pays 6th Edition analysis for Maine. Available at: <https://itep.org/whopays/maine/>