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STATE OF MAINE
ONE HUNDRED AND EIGHTH LEGISLATURE

COMMITTEE ON TAXATION

MAINE TAX STRUCTURE

Description of Areas of Possible Reform

This study, prepared by the Legislative Joint Committee on Taxation, is meant to be a constantly updated analysis of Maine taxes and policy issues. Further, it offers with each tax analysis a listing of commonly voiced areas of reform. The Committee on Taxation does not necessarily endorse any of these reform suggestions; indeed, some of them are contradictory. Rather, it offers them for public debate. If any Legislator wishes to further pursue any specific tax reform measure, please contact the Office of Legislative Assistants, Room 427, State House.

The members of the Office of Legislative Assistants who staff the Committee on Taxation in the preparation of this study are:

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Clerical assistants are:

Earl Knox
Laurette Knox
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MAINE TAX BURDENS: an analysis of Maine personal incomes and tax burdens

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STATE TAX MIX

This chapter emphasizes the importance of a relatively balanced mix of state and local taxes. The reason for achieving such balance was well stated by the 1977 Maine Select Committee on State Tax Policy:

> Of all the tools of government, taxes can be the bluntest, the most unwieldly. Often their burdens fall unfairly, without recognition of our differing situations. The sales tax cannot distinguish between the person who lives frugally and the person simply too poor to buy many goods. The property tax cannot distinguish between the family house that has been held for generations and the lot purchased for quick development. The personal income tax reflects cash flow and family size but can tell little of a person's wealth in stocks or bonds. Alone, the income, sales or property tax can be an unfair levy; but taken together in a balanced tax structure they can greatly improve the chances that each of us will be taxed according to our "ability to pay."

The materials in this chapter are:

1. The latest mix of Maine state and local taxes;
2. A valuable analyses of the Advisory Commission on Intergovernmental Relations describing the reasons behind a well balanced tax structure;
3. A description by the Legislative Finance Office of the different sources of state revenues and how they are expended;
4. The recommendation for a balanced tax mix from the 1975 Report of the Governor's Tax Policy Committee;
5. Miscellaneous materials.

STATE-MUNICIPAL TAX MIX
Fiscal Year 1976-77

	1976-77 Total revenues		Percentage of total tax revenues 1975-76%	1976-77%
Property Taxes: 1/				
Property Assessments	$ 246,060,871	2/	(33%)	(31%)
Auto Excise Taxes	26,561,258	2/		
Inventory and Livestock Taxes	13,884,914	2/		
Maine Tree Growth Tax	7,237,172			
Spruce Budworm Tax	2,055,050			
Total Property Taxes	$ 295,799,265		39 %	37.3%
Sales Tax	169,664,878		22 %	21.3%
Individual Income Tax	75,157,185		7.3%	9.4%
Corporate Income Tax	35,200,308		5 %	4.4%
Unemployment Compensation Tax	42,728,233		5 %	5.3%
Gasoline & Other Highway Taxes	55,292,831		7.3%	6.9%
Motor Vehicle Registration and Divers Licenses	23,042,851		3 %	2.9%
Cigarette Taxes	24,296,239		3.4%	3 %
Public Utilities Tax	12,027,254		1.4%	1.5%
Inheritance and Estate Taxes	8,040,815		1 %	1 %
Insurance Taxes	9,190,012		1.1%	1.1%
Inland Hunting, Fishing & Related Licenses	5,055,521		.7%	.6%
Commission on Pari-Mutuel	1,242,450		.1%	.1%
Other Taxes 3/	7,067,148			.8%
Total:	$ 792,702,406	4/		

Total Operating Fund Tax Revenue Per Controller's Financial Report	$ 482,292,337	
Unemployment Compensation Tax (above)	(42,728,233)	
Net Income transferred from the Bureau of Alcoholic Beverages	25,545,295	(3.2% of total)
Inspection and Other Services Fees	3,352,111	(.4% of total)
Total reported to U.S. Department of Commerce	$ 468,461,510	

1/ 1976 assessment year

2/ Inclues money raised for municipal expenses (e.g., Uniform Property Tax in support of education).

3/ "Other taxes" includes the following levies:
- Real Estate Transfer
- Milk Taxes
- Business Filing Taxes
- Bank Taxes
- Amusement Taxes
- Miscellaneous Business Taxes & Licenses
- Snowmobile Taxes
- Potato Tax
- Sardine Tax
- Highway Permits
- Motor Vehicle Inspections
- Dog Licenses
- Other Taxes and Licenses

4/ Total for 1975-76 was $701,448,079.73

A HIGH QUALITY STATE-LOCAL FISCAL SYSTEM

It is now clear that a high quality State-local revenue system can be achieved most effectively by shifting to the State primary responsibility for financing education and by making balanced use of the three prime tax measures – property, income, and sales.

On the basis of the Commission's recommendations drawn from its studies of intergovernmental fiscal relations, four policy characteristics stand out as the foundation on which a strong State-local sector can be built in our federal system:

1. *The State tax system should be able to generate sufficient revenue to finance most of the costs of public elementary and secondary education as well as "traditional" State programs.*[1]

For most States this would mean a State tax system that produces between 70 and 80 percent of all State-local tax revenue. At the present time, the State tax structures produce about 55 percent of total State-local taxes although there are 11 States (mostly in the South) that produce in the 70-80 percent range (Tables A and 8).

The Commission called for this policy thrust in recommendations that would have the States:

(1) establish as a basic objective of long range State-local fiscal policy the assumption by the State of substantially all responsibility for financing local schools, and

(2) equip themselves with a productive and broad-based tax system capable of underwriting a major portion of the State-local expanding expenditure requirements.

Increasingly, States have found both the general sales and personal income taxes essential to prevent excessive local property tax burdens, proliferation of local nonproperty taxes, interlocal fiscal disparities and undue dependence on Federal aid. The use of these two broadly-based taxes has become the standard by which State fiscal effort is judged because 36 States now impose both levies.

2. *The personal income tax should stand out as the single most important revenue instrument in the State tax system capable of producing close to 25 percent of total State-local tax revenue.*

At the present time, the State personal income tax accounts for only 12 percent of all State-local tax collections although there are 4 States that closely approximate this productivity (Alaska, 26.2; Delaware, 28.0; Hawaii, 23.3; and Oregon, 24.8) (Tables A and 6).

Reliance on the State personal income tax for approximately 25 percent of all tax revenue would both tone up the equity features of the system and insure an overall State-local system elasticity of between 1 and 1.2 (Tables 37, 109, and 146).

A greater reliance on the personal income tax would improve the fairness of State and local taxation by permitting a larger share of the tax burden to be adjusted to the size of the family through an exemption system -- a criterion typically disregarded by the property tax and violated by the sales tax. The unique ability of the income tax to treat individuals and households with equal income equally grows in importance as the margin between people's incomes and their consumer expenditures widens and as family homesteads become less and less indicative of taxpaying ability.

A broad-based flat-rate State income tax when combined with personal exemptions, thus, can pack both a heavy revenue punch and a substantial degree of progression. Graduated rates add progression in

TABLE A – STATE LOCAL FISCAL SYSTEMS, SIGNIFICANT FEATURES 1970-71 AND 1971-72

State	All State taxes, 1971-72 Rank	All State taxes, 1971-72 %	Percentage of State local taxes from-- State individual income tax, 1971-72	State general sales tax, 1971-72	State-local property taxes, 1971-72	Local income taxes, 1970-71	Local general sales taxes, 1970-71	Average effective property tax rates, existing single-family homes with FHA insured mortgages, 1971	State as % of State-local revenue (from own sources) for local schools, 1970-71
				State Dominant Fiscal Partner					
New Mexico	1	.80.1	9.9	30.7	20.7	*	0.5	1.70	74.5
Delaware	2	79.3	28.0	–	17.2	1.6	–	1.26	76.3
West Virginia	3	75.9	12.8	12.3[1]	20.8	–	–	.69	56.7
South Carolina	4	75.7	14.2	27.2	23.2	–	–	94	68.4
Hawaii	5	75.5	23.3	29.5[1]	19.1	–	–	.92	96.3
Mississippi	6	75.5	7.0	36.2	22.7	–	–	.96	66.3
Alabama	7	74.7	10.9	23.6	13.7	0.3	6.2	.85	74.6
North Carolina	8	74.4	18.4	16.6	25.1	–	0.7	1.58	77.9
Arkansas	9	74.3	11.4	23.4	23.9	–	–	1.14	54.2
Kentucky	10	73.6	13.4	27.2	20.9	5.5	–	1.27	64.4
Louisiana	11	70.7	6.7	17.8	18.3	–	9.7	.56	65.5
Alaska	12	68.4	26.2	–	23.3	–	6.5	1.61	86.8
Oklahoma	13	66.7	10.0	11.6	27.0	–	4.2	1.35	46.0
Median Average		(74.7)	(12.8)	(23.6)[2]	(20.9)	N.C.	N.C.	(1.14)	(68.4)
				State Strong Fiscal Partner					
Georgia	14	65.3	13.1	23.2	30.8	–	–	1.44	61.4
Idaho	15	64.8	16.3	16.7	34.8	–	–	1.72	44.6
Washington	16	64.3	–	25.9[1]	36.5	*	1.0	1.62	54.7
Utah	17	64.0	15.4	24.5	34.9	–	2.6	1.49	57.3
Florida	18	62.5	–	27.5	32.5	–	–	1.41	61.7
Tennessee	19	62.2	1.0	24.9	26.7	–	6.8	1.53	52.1
Pennsylvania	20	61.5	11.6	15.6	27.6	8.3	–	2.16	46.2
Vermont	21	61.1	17.8	8.3	38.3	–	–	2.53	35.2
Rhode Island	22	60.4	13.3	18.3	39.1	–	–	2.21	37.1
Arizona	23	60.2	9.6	22.7	38.6	–	5.4	1.65	47.5
Wisconsin	24	59.8	21.9	14.1	42.9	–	–	3.01	31.7
Virginia	25	59.6	18.3	13.0	28.2	*	4.3	1.32	37.7
Michigan	26	59.2	14.0	19.1	39.1	2.8	–	2.02	43.0
Minnesota	27	58.8	21.5	12.0	40.1	–	0.1	2.05	48.1
North Dakota	28	58.1	7.2	22.5	41.1	–	–	2.08	31.3
Texas	29	57.4	–	18.5	38.3	–	3.3	1.91	52.7
Maryland	30	57.2	20.6	13.1	31.9	9.3	–	2.24	37.4
Maine	31	57.1	5.8	21.2	43.3	–	–	2.43	34.7
Nevada	32	56.5	–	18.8	34.7	–	1.8	1.48	40.2
Wyoming	33	55.2	–	21.4	49.3	–	0.1	1.38	36.6
Iowa	34	53.1	14.2	15.3	46.2	–	–	2.63	28.9
Illinois	35	52.5	13.0	17.1	41.1	*	3.5	2.15	36.6
Missouri	36	51.9	12.6	18.2	37.2	3.1	0.8	1.79	33.8
Colorado	37	50.9	14.8	15.9	40.7	*	5.6	2.45	31.9
Connecticut	38	50.8	3.1	18.4	48.8	–	–	2.38	23.9
Kansas	39	50.7	9.2	17.3	48.7	–	–	2.17	32.1
Indiana	40	50.5	12.1	18.6	49.5	–	–	1.96	33.2
Oregon	41	50.2	24.8	–	48.0	–	–	2.33	20.8
Median Average		(58.5)	(14.0)[3]	(18.4)[2]	(38.9)	N.C.	N.C.	(2.04)	(37.3)
				State Junior Fiscal Partner					
Montana	42	49.7	18.5	–	50.4	–	–	2.19	26.1
Massachusetts	43	48.8	20.1	5.4	50.7	–	–	3.13	26.4
New York	44	48.4	17.4	10.6	36.7	3.6	6.9	2.72	50.1
Ohio	45	48.4	2.5[4]	16.5	43.0	7.4	0.4	1.47	29.8
California	46	47.9	13.1	14.3	47.6	0.1	3.9	2.48	37.1
Nebraska	47	46.2	7.8	14.5	50.3	–	1.0	3.15	20.1
South Dakota	48	42.5	–	19.4	53.8	–	0.7	2.71	16.0
New Hampshire	49	42.2	2.0	–	58.0	–	–	3.14	10.4
New Jersey	50	39.8	0.6	14.2	56.0	–	–	3.01	27.5
Median Average		(47.9)	(17.4)[5]	(14.3)[2]	(50.4)	N.C.	N.C.	(2.72)	(26.4)
Exhibit:									
District of Columbia		–	–	–	30.9	25.4	17.9	1.80	–
U.S. (excluding D.C.)		55.3	12.0	16.3	38.8	1.7	2.4	1.98	43.3
U.S. (including D.C.)		55.0	12.0	16.3	38.7	1.8	2.5	1.98	43.1

*Less than 0.05 percent. N.C. - Not computed.
[1] Excluding business gross receipts.
[2] For states with a general sales tax.
[3] For the 21 states (with a broad-based individual income tax (excludes Connecticut and Tennessee)).
[4] Based on collections for partial year. New tax effective 1/1/72.
[5] Based on the 5 states with a broad-based tax for the entire fiscal year. (excludes New Hampshire, New Jersey, and Ohio).
Source: ACIR staff calculations based on U.S. Bureau of the Census, Governments Division, U.S. Department of Housing and Urban Development, Federal Housing Administration; and National Education Association, Research Division: published and unpublished data

income tax liabilities and increase the responsiveness of income tax collections to economic growth, thereby enhancing the overall State-local revenue system elasticity (Tables 139, 141, and 142).

With a revenue system elasticity of 1.0 the State-local public sector would maintain the same growth rate as the total economy. At the elasticity of 1.2 growth in the State-local sector would be about enough to match automatic growth in National Government tax receipts, thereby creating a fiscal equilibrium within our federal system.

To maximize taxpayer convenience, the State personal income tax should be characterized by a high degree of conformity to the Federal income tax code. Alaska, Nebraska, Rhode Island, and Vermont have attained a high degree of conformity to the Federal income tax (Table 145).

3. *The general sales tax should serve as the other major State tax capable of producing between 20 and 25 percent of total State-local tax revenue without imposing an extraordinary burden on low income families -- the exemption of food and drugs or the provision of income tax credits can go a long way toward pulling most of the regressive stinger from this tax.* Five States could meet both the productivity and the anti-regressivity tests in fiscal 1971 – Florida, Hawaii, Kentucky, Maine, and North Dakota. At the present time the State sales tax accounts for about 16 percent of the total State-local tax revenue (Tables A and 6).

The number of items covered by the sales tax affects not only the amount of revenue the tax produces but also how the burden of the tax is distributed. Because low income people spend a greater fraction of their income than do high income persons, a tax on consumer purchases is inherently regressive. Excluding services from the tax base makes the sales tax even more regressive, since purchases of services become increasingly more important as one moves up the income scale (Table 134).

Exemption of food makes the sales tax nearly proportional, although only at the loss of substantial revenue. The sales tax credit accomplishes the same end at much lower cost by returning a fixed sum to each person, regardless of income (Tables 135 and 146).

4. *The local property tax should continue to serve as the principal revenue instrument for local government and should be able to pass two equity tests.*

a. *The full value test* – In order to help insure uniform assessments the State should bring local assessment levels up to the full value standard – in no case should the statewide level of assessments drop below 80 percent of current market value. At the present time, two States appear to have met the 80 percent test -- Kentucky and Oregon. Most States have a long way to go because the national assessment level is probably in the general neighborhood of 35-40 percent of current market value. Low fractional assessment will always provide a convenient graveyard in which assessors can bury their mistakes (Table 100).

b. *The anti-regressivity test* -- A State financed "circuit-breaker" system to protect low income home owners and renters from property tax overload situations – at least the elderly home owners and renters should be shielded in a way so as to insure that they are not required to turn over more than 6 or 7 percent of total household income to the local residential property tax collector. In the last few years, 22 States have adopted various applications of the "circuit-breaker" principle (Tables 106, 108 and 109).

Most States are forcing the local property tax to serve as the principal underwriter for schools. The property tax is also called on to pick up a significant share of the public welfare tab in several States. It produces almost 40 percent of all State-local tax revenue, far too much in view of the inequities caused by faulty assessment practices (Table A and Tables 73 through 84).

In order to free up the local property tax for essentially local or municipal-type functions the States should assume responsibility for the financing of most of the cost of elementary and secondary education. Such action would represent a giant step toward equalizing the amount of resources placed behind each public school pupil.

Most importantly, if the property tax were relieved of the heavy drain of welfare and educational financing it could provide comfortably for 20 to 30 percent of State-local tax revenue required for locally determined and locally financed functions.

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[1] Hopefully, the Federal Government will assume complete responsibility for the welfare function in the next few years.

TABLE [illegible]
OPERATING REVENUES AND EXPENDITURES

GENERAL FUND	HIGHWAY FUND	OTHER SPECIAL REVENUE FUNDS
Revenue Source	**Revenue Source**	**Revenue Source**
Tree Growth Tax	Gas-Use Fuel Tax	From Federal Government
Income Tax	License-Registration Fees	Hunting-Fishing Licenses
Sales and Use Tax	Federal Grants	Service Charges-Current Services
Federal Grants	Cities-Towns-Counties	Other Taxes
Liquor and Beer Tax	Other Revenues	Sardine Development Tax
Cigarette Tax	All Other Taxes	Other Revenues
Other Revenues		Gas-Use Fuel Tax
Public Utilities Tax		Taxes on Insurance Companies
Estate-Inheritance Tax		From Cities-Towns-Counties
Insurance Company Tax		Transferred From Other Operating Funds
State Property Tax		
All Other Taxes		
Pari-Mutuels Tax		
Expenditures	**Expenditures**	**Expenditures**
General Government	General Government	General Government
Economic Development	Economic Development	
Education & Culture		Education & Culture
Human Services		Human Services
Manpower		Manpower
Natural Resources		Natural Resources
Public Protection	Public Protection	Public Protection
Transportation	Transportation	Transportation

Balanced Tax Structure

Finally, the above standards - equity, competitiveness, efficiency, fiscal stability and flexibility - seem achievable only in a planned, relatively balanced tax structure. To place too great an emphasis on any single State-local tax is to inevitably cause an extraordinary tax burden on some citizens. Maine's tax structure is not balanced; its current mix of taxes is disproportionately weighted toward the property tax:

PRESENT TAX STRUCTURE (1974-75)

	Millions	Percent of Mix
Property	$208.2	39.7%
Sales	137.8	26.3
Personal Income	43.8	8.4
Corporate Income	20.9	4.0
Other (11)	113.2	21.6
	$523.9	100.0%

However, to simply impose a strictly balanced structure on Maine's unique conditions would be to ignore the facts that Maine is a state of low incomes, yet great landed wealth; a State which depends on the trade of vacationers and expends great revenues to insure that the State is worthwhile to visit. Thus, this report will recommend steps by which a balanced tax structure can be achieved while still reflecting the needs and resources characteristic to Maine.

11. "Other" taxes include all undedicated revenues (alcohol, cigarettes, aeronautical, and miscellaneous business) and the dedicated motor fuel tax.

IV

AREAS OF NEEDED REFORM IN THE MAINE TAX STRUCTURE

Does tax reform mean an increase in the total taxes raised by the State? Not at all. Rather, achievement of the standards listed in Section III can be realized in the Maine tax structure through the following general actions:

1. Designing a more balanced tax structure, one which is suitable to the characteristics of Maine and which places a greater emphasis on the personal income tax and less on the property tax.

2. Refashioning our broad based taxes - income, sales and property - so that each one taxes according to a citizen's ability to pay.

3. Implementing reforms in tax administration that assure more accurate and efficient collection of taxes.

Design of a More Balanced Tax Structure

In Maine the tax structure needs better balance: the property tax accounts for nearly 40% of all State-local revenues, while the income tax accounts for only 8.4%. The property tax levies a burden on a necessity: shelter. (See Appendix B, Who Pays the Local Property Tax?) Moreover, the Census of Governments data documents that as more and more public and business property is exempted from the property tax, it increasingly becomes a tax on housing. In 1969 in Portland, the property tax was estimated at 30.2% of the total cost of shelter.[12] Overall, this tax burden represents on the average 3.8% of a Maine citizen's income. This burden is the

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12. Federal Reserve Bank of Boston, Options for Fiscal Structure Reform in Massachusetts, 45(1975) (hereinafter cited as Options for Fiscal Structure Reform).

16th heaviest in the country.(13) These are reasons enough to explain why the property tax is popularly felt in this country to be the "least fair" tax of all, federal or state.(14)

What happens when an unbalanced tax structure such as Maine's places this burden on the necessity of housing? The following general results are, by and large, agreed upon by fiscal experts:

1. "Such high property taxes inevitably discourage investment in homes and home improvement and encourage spending on less heavily taxed items as automobiles, boats, travel, and entertainment. More importantly, in some low-income communities high property taxes discourage investments in new apartment houses, office buildings and manufacturing plants."(15)

2. A heavy property tax will magnify assessment mistakes, a deficiency common to communities.(16) High value properties are often under-assessed relative to low-cost residences. Where such variations occur the tax is made regressive.(17)

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13. Id. at 15. See also ACIR, Financing Schools and Property Tax Relief - A State Responsibility, 35-42 (1973).

14. ACIR, Changing Public Attitudes on Governments and Taxes, 9(1975)

15. Id. at 46. See also New Jersey Tax Policy Committee, the Property Tax (1972):" . . Dr. Dick Netzer found that the property tax as now constituted is a deterrent to new housing and the maintenance of existing homes and that it places a particular burden on low-income renters." at 20. (hereinafter cited as New Jersey Tax Policy Committee).

16. The Governor and the 107th Legislature recognized this deficiency by enacting into law L.D. 1917, a comprehensive reform of assessing practices. The Statement of Fact defined this need: "The purpose of this Act is to establish minimal assessing standards for Maine communities that will insure by 1979 equitable assessing practices . . . ."

17. ACIR, Property Tax Circuit Breaker: Current Status and Policy Issues, 14(1975).

3. A too heavy property tax means public services will be distributed with great inequity. The poor of Van Buren or Portland, or any of Maine's urban centers, will pay higher property taxes yet receive less services per dollar. Why? "The tax may be regressive among jurisdictions as well as among individuals. If one jurisdiction consists predominately of low-income families in low-cost housing, while a second jurisdiction is characterized by higher-income families living in higher-valued residences, property tax rates must be higher in the "poor" area in order to provide the same level of services as in the "rich" jurisdiction, other things being equal. The higher rates imposed on the low-income families contribute to the overall regressivity of the property tax."(18)

4. "Excessive property taxes have had an adverse effect upon environmental quality. This stems largely from the unending search of municipalities for tax ratables which is reflected in 'fiscal zoning'. Such zoning contributes to misuse of land resources, misdirected planning, and unnecessary pollution."(19)

5. High property taxes drive more affluent residents to suburbs with lower tax rates, leaving behind the poor and elderly in deteriorating neighborhoods.(20)

6. A high property tax is socially divisive because it encourages "snob" zoning: "Communities which are primarily inhabited by high-income people benefit by having lower tax rates because their inhabitants live in expensive homes which create a substantial tax base. Thus the tax structure provides a built-in incentive for communities to exclude medium and low income people by zoning."(21)

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18. Id.at 14. See also Connecticut Conference of Mayors and Municipalities, Property Taxpayers On the Ropes (1975): "Connecticut's property-poorest cities and towns levy an average tax rate which is more than twice the rate levied in the State's property richest. Yet, on average, the State's property poorest cities and towns can raise less than one quarter of the per capita tax yield raised in the property-rich municipalities. The property poorest town is able to raise less than one eighth of the per capita tax yield raised in the town with the richest property tax base." at 34.

19. New Jersey Tax Policy Committee 19.

20. See Massachusetts Public Finance Project, The Rich Get Richer and the Poor Pay Taxes, 27(1974).

21. Options for Fiscal Structure Reform 12.

These socially damaging effects of a too burdensome property tax clearly recommend that the property tax be made a smaller part of the State tax structure. To what tax should the burden mainly be shifted? The answer is equally clear: the personal income tax. Maine is 16th in the nation in terms of property tax burden yet we are 38th in terms of income tax burden.(22) The personal income tax can absorb most of this shifted burden.

Equitably the income tax is superior to our current property tax as a means of measuring the average person's ability to pay (the income tax reflects family size, the property tax does not) and, at only 8.4% of our current tax mix, it is an extremely underutilized tax source. Specifically, the Advisory Commission on Intergovernmental Relations (ACIR) in Washington suggests that the individual income tax assume a 20-25% share of a State's tax structure for the following reasons:

1. The personal income tax is a highly equitable tax, reflecting both horizontal equity and vertical equity.

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22. INDIVIDUAL INCOME TAX: 1973

	As a Percent of Personal Income		As a Percent of Federal Tax Liability	
	Percent	National Rank	Percent	National Rank
U.S. Average	1.5	-	13.5	-
New England States				
Massachusetts	2.8	6	25.4	9
Connecticut	.3	41	3.1	28
Maine	.8	37	9.1	38
New Hampshire	.2	42	1.9	42
Rhode Island	1.4	22	16.2	18
Vermont	2.6	8	27.6	5

Source: State Tax Collections in 1973, Table 3, p. 7, Table 6, p. 10, Preliminary Statistics of Income 1972, Individual Income Tax Returns, Table 6, p. 25. Prepared by the Federal Reserve Bank of Boston (1975).

2. The personal income tax responds well to economic growth, thereby producing revenue system elasticity. Revenues will grow as the economy grows and new services will not mean an automatic tax increase.(23)

Because Maine is a tourist state and revenue expenditures to accomodate our visitors are significant, the role of the sales tax, which taxes the consumption of both residents and visitors,(24) in the Maine tax structure should be larger than the 20-25% that is also recommended by ACIR. Currently, it is 26.3% of the tax mix and in Section V of this report the committee will recommend a slight increase in this percentage.

While the shift of burden from the property tax to the personal income tax, with slightly increased reliance on the sales tax, would produce the more balanced tax structure Maine needs, this reform is futile if the broad-based taxes that make up that structure do not reflect a person's ability to pay.

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23. Features of Fiscal Federalism 1-4.
The property tax lacks this ability to keep pace with economic growth. This is one of the roots of towns' and cities' failure to provide necessary services without increasing the property tax to an unfair level. John Menario, Portland city manager, described the failings of the property tax for the Commission on Maine's Future and made the following points:

1. Portland has been operating on the same resource base -- property -- since 1820 and it is no longer sufficient;
2. Property tax initially meant a city would be wealthier if it built tightly and as a result many cities were spoiled forever;
3. Industry and buildings, in the long run, only bring higher taxes; in 1973 Portland had its greatest development year with $15 million in new buildings. Today those buildings only produce $460,000 in added property tax revenue, not nearly enough to meet rising costs.

Menario's solution: increase State revenue sharing by returning to communities a percentage of the State income tax. See Sleeper, "City Officials Eye Tax Reform", Portland Press Herald, 1, col. 1 (July 19, 1975).

24. In Maine, 13.8% of our total taxes is generated by tourists; 10.3% is generated by out of State tourists. See Northeast Markets, Tourism in Maine: Analysis and Recommendation, 69(1975).

Refashioning Our Broad Based Taxes So That Persons Are Taxed According to Ability to Pay

The Property Tax

Is the property tax regressive in its incidence? This question in recent years has been heatedly debated. One camp of economists, the traditionalists, theorized that the burden of property taxes on structures (i.e. houses) was borne in proportion to consumption of such commodities and therefore was regressive because consumption of housing looms much larger in a poor person's budget. The other camp, the revisionists, offered a new and more persuasive argument that while the above analysis may be true for a given locality, when the property tax is viewed nationwide it is generally borne by the holders of all capital. Since capital on the average is more concentrated among high-income families than even income, the property tax is progressive.(25)

Thus, while the theorists arguing for a progressive property tax seem correct in their nationwide analysis, the practical burden in different localities might mean an extraordinary property tax for low-income homeowners and renters. Henry Aaron, the most persuasive of the new theorists, admits that despite its over-all theoretical progressivity, some poor do in fact pay more:

> ". . . even with respect to that portion of the tax levied on housing, it (economic analysis) now suggests that the property tax is probably progressive on the average, although some low income families may be exposed to heavy burdens."(26)

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25. Aaron, Henry J., Who Pays the Property Tax?, 19-20 (1975) (hereinafter cited as Who Pays the Property Tax?).

26. Id. at 2 .

Mr. Aaron further states that any progressive estimates should further be tempered by realizing the regressive effect of the Federal income tax on homeowners and renters:

> ". . . property taxes paid by a homeowner are deductible even though gross inputed income on his investment is not counted as part of his income. Such deductibility makes a proportional or even a progressive tax regressive to homeowners since the national Treasury pays a fraction of the property tax of all taxpayers who itemize their deductions."(27)

Therefore in considering whether or not our current property tax in Maine, as it is administered in each locality, with different assessment standards and different degrees of property wealth, is a superior method of measuring ability to pay, it is important to look beyond the theoretical argument of the revisionists and look at Maine's individual householders:

> "It is possible to grant virtually all the points of the revisionists and still maintain that the residential component of the property tax is very regressive indeed, provided one recognizes the pattern of tax rate differentials in metropolitan areas, the associated geographic distribution of renters and owners at various income levels and the way in which assessments are actually done." (28)

Therefore, this report will recommend in Section V that fundamental municipal property tax reform be afforded through a reduction in rates. Resident property tax payers will pay approximately for the services provided them. At reduced rates the lightened property tax burden will more directly correspond to each person's ability to pay. Regressive or progressive, this relief is needed:

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27. Id. at 47.

28. Netzer, Dick, "Is There Too Much Reliance on the Property Tax?", in Property Tax Reform, 21(1973). See also Financing Schools and Property Tax Relief - A State Responsibility, supra note 13 "If the property tax burden falls on renters and consumers, it is regressive throughout the entire income range. If it bears entirely on capital, it is regressive up to the $10,000 - $15,000 income class and becomes progressive in the upper-income ranges." at 31.

For reasons expressed above, the committee recommended expanding the sales tax share of the State tax mix. This can be accomplished while also improving the equity of the sales tax in general. How? By gradually transforming the sales tax into a tax more reflective of luxury consumption.

A major deficiency in retail sales tax is its nearly exclusive application to tangible commodities.(32) Through exemptions of specific goods and the near complete avoidance of taxation of services the sales tax base had eroded and become a levy that weighs much heavier on the poor than any other citizen class. This regressivity can be alleviated by expanding the sales tax base and instituting a credit(33) for minimal purchases. The tax then is converted to a levy on luxury consumption.

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31 Continued

$2.60 per capita.
[b] $8.60 per family.
[c] For families with income less than $1,000, the credit equals $10.80 per capita. For every additional $1,000 in family income the credit per capita is reduced by $1.80 vanishing at incomes greater than $6,000.
[d] The credit is the recently enacted New Mexico adoption adjusted to equal the cost of an over-the-counter food exemption.
[e] Vertical equity, in this analysis, is defined as the difference between the mean effective tax rate on families in the 5 highest and 5 lowest income classes under each tax, divided by the mean effective tax rate on all families.
[f] Horizontal equity requires equal treatment of equals (e.g. families equal incomes and equal sizes.

If conditions in Maine match this analysis, then Maine's current sales tax is somewhat horizontally progressive and slightly vertically regressive.

32. Morgan, David, Retail Saler Tax, An Appraisal of New Issues (1964), See also Features of Fiscal Federalism 3; Tax Foundation, State and Local Sales Taxes 21, 63 (1970); ACIR, Fiscal Balance in the American Federal System, 132 (1967); Shannon, John, "Tax Relief For the Poor", Proceedings of the National Tax Association, 1967, 557-596 (1968).

33. "Tax Relief For the Poor", supra note 32: "Recent tax credit innovations on the State sales tax have almost squared the revenue circle - that of maximizing consumer tax yields while minimizing the burden which these levies impose on low income families. Until recently, only the costly exemption approach was used to minimize regressivity of the general sales tax." at 581. See Walters, Elsie, Tax Review, 71 (1970).

The tax credit would be administered through the State personal income tax. Each citizen would be allowed to subtract from the amount of the income taxes owed a sum reflective of sales taxes paid on a minimum standard of living. Poor people who owed no income taxes would receive their credit directly from the State. The credit would be flat-rate--each citizen receiving the same amount. For example, if it were determined that $25 per month of goods and services (not including food, medicine, or medical services) represented a minimum standard of living, then, at a 5% sales tax rate, a person's credit for 12 months would be $15. Thus all other sales taxes paid -- those over $15-- could be considered a tax on "luxury consumption."

Even if the tax credit decided upon only partially reflected non-luxurious consumption, the equity of the sales tax would still be significantly enhanced because wealthier people will naturally purchase every month considerably more than a minimal amount of goods and services.

Thus, for the following reasons the committee will recommend in Section VI to expand the sales tax base to include most services:

1. Expenditures on services tend to rise as incomes rise, thus the higher incomes bear the greater weight; therefore taxation of services tends to make sales tax less regressive. Also expenditures for services rise more rapidly with income than they do for commodities, the yield of the taxes therefore adjusts more exactly in terms of rising levels of economic activity. The inclusion of services in the sales tax base will increase the responsiveness (income elasticity) of the tax to changing economic activity, particularly where the long run trend for growth is gross state income. Taxing services would postively affect progressivity of the tax.

2. Under the philosophy that sales taxes should cover as broad a base of consumer expenditures as possible, with exemption only when specifically justified, the tax should apply to services as well as commodities, since both categories satisfy personal wants. A haircut, concert, or plane ride satisfy personal desires in the same manner as does an automobile, new suit, or piano. If tangibles are taxed and services are excluded from the base, then the sales tax discriminated against individuals whose tastes run to goods as opposed to ones who prefer services. There is no economic feature of most services that warrants their exclusion from taxation. To tax goods but not services distorts the allocation of consumer dollars in favor of services.

3. A number of services (e.g. repairs) are rendered in conjunction with the sale of taxable commodities. Compliance and administration are far simpler if the entire charge is taxable than if a separation between service and commodity is necessary. Compliance costs would be reduced for businesses presently providing both goods and services. Problems in separating tangibles from services would be eliminated. Taxing services facilitates administration and lowers the costs of sales tax.

4. Increased revenues might eventually allow a reduction in sales tax (services share of the economy has increased dramatically). As we become more urbanized, we can expect the services sector to grow. From 1960-1968, spending for services rose by 69%, a rate higher than for commodities (60%). Yet services are not taxed.[34]

Further, the committee will recommend that with this base expansion, a flat rate[35] credit be instituted that will represent, in whole or in part, taxes on that portion of consumption that is not luxurious. Because this expansion of the sales tax base will produce, at a conservative estimate, approximately

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34. State and Local Sales Taxes, supra note 32 at 23.

35. An example of a flat rate credit is Massachusetts' $4 for each taxpayer, $4 for spouse and $8 for each qualified dependent. See Chap. 62 (Sec. 6b added by ch. 14, Acts 1966). Vermont has a variable rate credit, based on income and exemptions. See H.B. 125, Laws 1969; Chap. 152, Sec. 5829. New Mexico has a general low income tax credit that takes into account all state and local taxes paid by residents and is designed so that families below the U.S. poverty level have a total tax burden after credit equal to that of a family at the poverty level.

$29 million in new revenues, (36) the cost of the tax credit is easily assumed.

Appendix C details the equities involved in taxing specific services. For example, the burdens imposed by taxing services such as medical care would not seem acceptable.

The above reform of the sales tax into a levy on luxury consumption - an expanded tax base with a flat credit - produces greater revenues in a far more equitable manner.

Finally, implicit in recommending that the sales tax base be expanded to include most tangible goods and services is recognition of the fact that sales tax exemptions have proliferated in recent years and are rarely reviewed by the Legislature to insure they are still needed. Once exemptions are introduced, interest groups feel free to press for even more, thus leading to a severely eroded sales tax base. A sales tax credit, rather than ever-expanding exemptions, is a more fiscally sound approach to tax relief.

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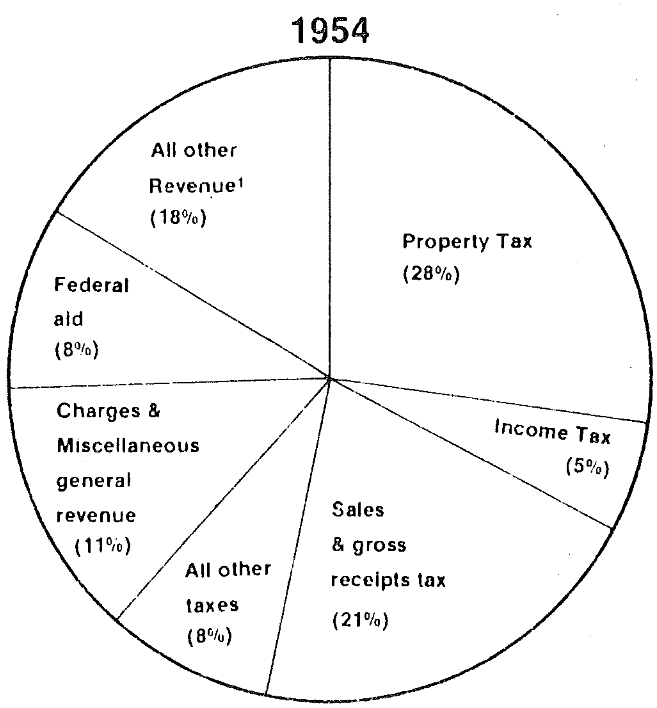
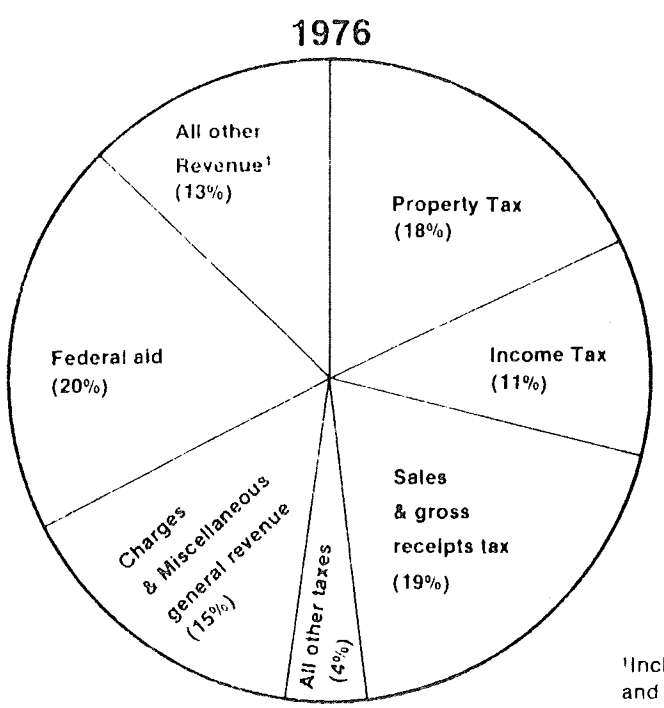
36. This estimate is based on statistics from the Maine Bureau of Taxation, the Maine State Planning Office and the ESCO 1972 report, State of Maine Government Finances Relief and Reform (1973-1975). The total does not include revenues from a sales tax base including grocery store food and fuel oil or other present sales tax exemptions.

CHART XIV

The State and Local Revenue System Becomes More Diversified with the Relative Decline in Property Taxes and Relative Increase in State Income Taxes and Federal Aid, Fiscal Years 1954 and 1976





Source: Table XIV

[1]Includes utility, liquor store, and insurance trust revenue

TABLE XIV

The State and Local Revenue System Becomes More Diversified with Relative Decline in Property Taxes and Relative Increase in State Income Taxes and Federal Aid, 1954, 1964, and 1969 Through 1976

		General Revenue							
				Tax Revenue					
Fiscal Year	Total State-Local Revenue	Total	Federal Aid	Total	Property	Sales, and Gross Receipts	Income	Charges and Miscellaneous General Revenue	Utility, Liquor Store, and Insurance Trust Revenue
				Amount (in billions)					
1954	$35.4	$29.0	$3.0	$22.1	$10.0	$7.3	$1.9	$4.0	$6.4
1964	81.5	68.4	10.0	47.8	21.2	15.8	5.5	10.7	13.0
1969	132.2	114.5	19.2	76.7	30.7	26.5	12.1	18.7	17.6
1970	150.1	130.8	21.9	86.8	34.1	30.3	14.6	22.1	19.4
1971	166.1	144.9	26.1	95.0	37.9	33.2	15.3	23.8	21.2
1972	189.7	166.4	31.3	108.8	42.1	37.5	19.7	26.3	23.4
1973	217.6	190.2	39.3	121.1	45.3	42.0	23.4	29.9	27.4
1974	237.9	207.7	41.8	130.7	47.8	46.1	25.5	35.2	30.2
1975[2]	263.0	230.0	48.0	142.0	50.8	50.0	28.7[3]	40.0	33.0
1976 est.	292.0	255.5	58.0	152.5	54.0	54.5	32.5	45.0	36.5
				Annual Percent Change					
1954	—	—	—	—	—	—	—	—	—
1964	8.7[4]	9.0[4]	12.8[4]	8.0[4]	7.8[4]	8.0[4]	11.2[4]	10.3[4]	7.3[4]
1969	10.2[5]	10.9[5]	13.9[5]	9.9[5]	7.7[5]	10.9[5]	17.1[5]	11.8[5]	6.2[5]
1970	13.5	14.2	14.1	13.2	11.1	14.3	20.7	18.2	10.2
1971	10.7	10.8	19.2	9.4	11.1	9.6	4.8	7.7	9.3
1972	14.2	14.8	19.9	14.5	11.1	13.0	28.8	10.5	10.4
1973	14.7	14.3	25.6	11.3	7.6	12.0	18.8	13.7	17.1
1974	9.3	9.2	6.4	7.9	5.5	9.8	9.0	17.7	10.2
1975[2]	10.6	10.7	14.8	8.6	6.3	8.5	12.5	13.6	9.3
1976 est.	11.0	11.1	20.8	7.4	6.3	9.0	13.2	12.5	10.6
				Percentage Distribution					
1954	100.0	81.9	8.5	62.4	28.2	20.6	5.4	11.3	18.1
1964	100.0	83.9	12.3	58.7	26.0	19.4	6.7	13.1	16.0
1974	100.0	87.3	17.6	54.9	20.1	19.4	10.7	14.8	12.7
1976 est.	100.0	87.5	19.9	52.2	18.5	18.7	11.1	15.4	12.5

[1]Including amounts for categories not shown separately.

[2]Partially estimated.

[3]Receipts from individual income taxes in 1975 were $21.7 billion (8.3 percent of total revenue.)

[4]Annual average increase 1954 to 1964.

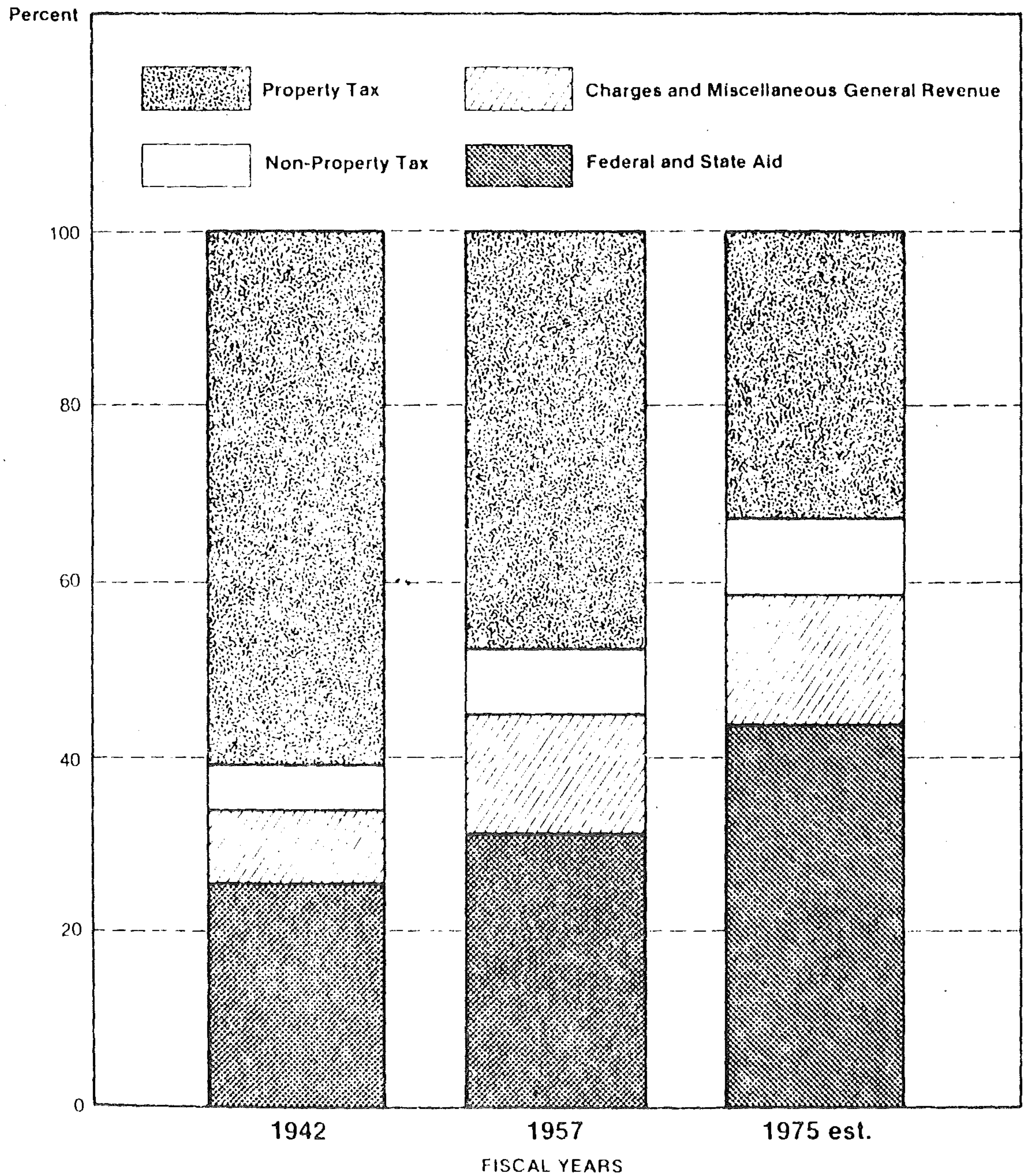
[5]Annual average increase 1964 to 1969.

Source: ACIR staff compilation based on U.S. Bureau of the Census, *Governmental Finances*, various years; and ACIR staff estimates.

CHART XV

Local Governments Are Moving Toward More Balanced Revenue Systems, Selected Years 1942-1975

(Distribution of Local General Revenue by Major Source)



Source: Table XV.

TABLE A – SUMMARY OF SIGNIFICANT FEATURES OF THE 50 STATE-LOCAL REVENUE SYSTEMS

State and Region	Incidence[1] (Family tax burdens)			Tax Effort[2]		Diversification[3] (source of state-local general revenue)						State government percentage of state-local tax revenue[4]	Equity features	
						Taxes								
	Progressive	Proportional	Regressive	state-local taxes as a % of state personal income	Per capita state-local tax revenue	Property	General Sales	Income	All other	Charges and misc. general revenue	Federal aid		Food exempt from sales tax (E) or income tax credit provided (C)[5]	State financed circuit-breaker property tax relief programs[6]
United States			X	12.3%	$664	22.6%	12.8%	12.3%	14.3%	17.4%	20.6%	56.7%	–	–
New England														
Maine			X	12.6%	671	24.4	13.7	6.4	15.8	12.7	27.0	61.0	E	E H&R
New Hampshire			X	10.8	625	36.5	0	4.9	19.4	16.0	23.1	40.1	NST	–
Vermont		X		15.5	699	24.7	4.6	11.3	17.0	14.8	27.6	56.8	E	A,H&R
Massachusetts			X	14.2	814	36.8	3.7	18.3	10.7	11.5	19.0	46.8	E	–
Rhode Island			X	11.9	645	26.0	10.8	12.1	13.3	13.8	24.0	58.5	E	–
Connecticut			X	10.8	697	34.8	13.6	4.9	15.6	12.3	18.8	49.1	E	E,H&R

STATE OF MAINE

ONE HUNDRED AND EIGHTH LEGISLATURE

COMMITTEE ON TAXATION

MAINE TAX STRUCTURE

Description of Areas of Possible Reform

This study, prepared by the Legislative Joint Committee on Taxation, is meant to be a constantly updated analysis of Maine taxes and policy issues. Further, it offers with each tax analysis a listing of commonly voiced areas of reform. The Committee on Taxation does not necessarily endorse any of these reform suggestions; indeed, some of them are contradictory. Rather, it offers them for public debate. If any Legislator wishes to further pursue any specific tax reform measure, please contact the Office of Legislative Assistants, Room 427, State House.

The members of the Office of Legislative Assistants who staff the Committee on Taxation in the preparation of this study are:

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MAINE TAX BURDENS

This chapter is devoted to materials which show the burden of Maine taxes. It contains the following materials:

1. Summary of Maine State and Local tax burdens

   Compares Maine tax burdens with the burdens in other states

2. Family tax burden differences among the States

   A study which analyzes the burden of different personal taxes on different sized families. It shows the specific degree of regressivity present in Maine family taxes

3. A short profile of Maine's poor

   Attempts to describe the specific living conditions of poor persons in Maine

4. Adjusted gross incomes of Maine taxpayers

   Shows the percentage of Maine citizens present in 32 different income brackets

5. The Advisory Commission on Intergovernmental Relations (ACIR) national poll which details which taxes are the most and least popular

6. ACIR's Measuring the Fiscal Blood Pressure" of the States: 1964-1975. Is the State of Maine spending too much?

7. Pechman and Okner study of national tax burdens.

SUMMARY OF MAINE
STATE AND LOCAL TAX BURDENS
(Source: U.S. Department of Commerce)

1. State and Local Tax Collections Per $1,000, Personal Income for Fiscal Years 1970-74

Year	1970	1971	1972	1973	1974
Maine:	$126.44	127.45	141.68	142.36	149.07

Maine's rank in the nation: 3rd heaviest (in 1970 it was 12th)

2. Percentage of Personal Income Remaining After State and Local Taxes, 1974

Maine: 86.98%: 46th heaviest in the nation

3. Per Capita Property Tax Collections, Fiscal Year 1974

Maine:$280.88, 8th heaviest in the nation

4. Property Tax Collections Per $1,000 Personal Income, Fiscal Year 1974

Maine: $70.09, 2nd heaviest in the nation

5. Per Capita Sales Tax Collections, Fiscal Year 1974

Maine: $126.72, 16th heaviest in the nation

6. Sales Tax Collections Per $1,000 of Personal Income,Fiscal Year 1974

Maine:$31.62, 10th heaviest in the nation

7. Per Capita State Individual Income Tax Revenue,Fiscal Year 1974

Maine: $37.28, 38th heaviest in the nation

8. State Individual Income Tax Revenues Per $1,000 of Personal Income, Fiscal Year 1974

Maine: $9.30, 38th heaviest in the nation

FAMILY TAX BURDENS

In 1975 Professor Stephen E. Lile of Western Kentucky University studied the regressivity of each state's personal taxes. His results for Maine were:

MAINE FAMILY TAX BURDENS, BY TYPE OF TAX

Family of four (Adjusted gross income)		Individual Income State	General Sales State	Residential Property 1/	Motor Vehicles	Cigar-ette Tax	Percentage Total Tax Burden
A.	$ 5,000	$ 0	$ 89	$ 392	$ 133	$ 60	13.6%
B.	7,500	14	118	525	133	60	11.5%
C.	10,000	39	144	574	133	60	9.7%
D.	17,500	228	211	980	199	60	9.2%
E.	25,000	674	250	1225	199	60	8.3%
F.	50,000	2788	363	2100	199	60	7.8%

This finding, that the poorest people in Maine pay the highest percentage of their income in taxes, is enforced by the State Planning Office's conclusion that over the years 1967-1973 the Maine household in the top quarter income brackets gained $600 more in constant purchasing power than did the bottom 25%. See State Planning Office, Profile of Poverty - Maine: A Data Source 5 (1975). This chart does not reflect the recent increase in the state income tax. This increase fell mainly on upper income taxpayers. However, it is important to remember that upper income persons, who frequently itemize their expenses for federal tax purposes, can deduct state taxes from their federal taxable income. Thus, such tax increases may be considerably less onerous than they appear (e.g., a taxpayer in the 50% federal tax bracket bears only 50% of any state increase). The following is a condensed version of Professor Lile's report which was published in State Government (Winter, 1975):

1/ Property tax estimates are based on these income/house value parings: $5,000/14,000; $7,500/$18,750; $10,000/$20,500; $17,500/$35,000; $25,000/$43,750; $50,000/$75,000.

State Govt.
Winter 1975

Family Tax Burden Differences among the States

by Stephen E. Lile*

THE CONSUMER PRICE INDEX is computed by the U.S. Bureau of Labor Statistics for large cities located in various States. It measures the cost of living based on prices of roughly 400 different private sector goods and services selected to represent the purchases of typical wage earners living in urban areas. This index excludes taxes which can be viewed as the price of public goods and services. This exclusion is significant because taxes account for an important part of families' total living expenses, and tax burden differences may contribute substantially to cost-of-living differences among States.

This article reports on findings of a recent study which estimated the cost of public services by computing the amount paid in major state-local taxes for hypothetical families assumed to live in 75 different cities including the largest city in each of 48 States.[1] These estimates, unlike the consumer price index, are not based on a given level and quality of services purchased in all locations. This should be remembered when interpreting differences in family tax burdens.

Estimates are based on the following major state and local taxes: state income, local income, state sales, local sales, residential property, motor vehicle, and cigarette excises. Amounts of tax are estimated on the basis of reasonable assumptions and on tax rates in effect during calendar year 1974.[2] Family income is assumed to derive solely from wages and salary.

COMPARISONS BY FAMILY TAX BURDEN

The following comparisons of family tax burden are based on the assumption that hypothetical families reside in the largest city in each of 48 States. Separate sets of comparisons are shown for each of four different family income levels.[3]

Family A: $5,000 Income

Table 1 shows that the five highest tax States for Family A are New Jersey, Connecticut, Wisconsin, Massachusetts, and Iowa, in that order. The five lowest tax States are Louisiana, Oregon, Mississippi, West Virginia, and Florida. The 48-state average is $562.

Family B: $10,000 Income

Tax burdens for Family B are shown in Table 2. The average is $889 and the range is from a low of $462 in New Orleans, Louisiana, to a high of $1,476 in Milwaukee, Wisconsin. Maryland replaces Iowa in the group of five highest tax States and Wyoming and Nevada replace Oregon and Mississippi in the low tax group.

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*Dr. Lile is Associate Professor, Economics Department, Western Kentucky University.

1. Stephen E. Lile, *Family Tax Burdens Compared among States and among Cities Located within Kentucky and Neighboring States* (Frankfort, Kentucky: Kentucky Department of Revenue, 1975).

2. The exception is the property tax which is based on 1971 effective rates reported in the 1972 Census of Governments report *Taxable Property Values and Assessment-Sales Price Ratios*, Table 12. Property tax estimates are based on these income/house value pairings: $5,000-$14,000; $7,500-$18,750; $10,000-$20,500; $17,500-$35,000; $25,000-$43,750; $50,000-$75,000. State income tax estimates are based on estimates of effective tax rates provided by the Advisory Commission on Intergovernmental Relations. Local sales, local income, and state-local cigarette excise taxes are based on rates reported in Commerce Clearing House *State Tax Reports* for 1974. In computing the cigarette excise, each family is assumed to consume 400 packs of cigarettes annually. Taxes associated with owning and operating an auto are taken from the U.S. Department of Transportation report *Road User and Property Taxes on Selected Motor Vehicles*, Table 6.

3. The full report includes estimates for families of $7,500 and $17,500 of adjusted gross income.

Family C: $25,000 Income

The five highest tax States for a typical family of $25,000 income, shown in Table 3, are Wisconsin, Massachusetts, Minnesota, Maryland, and New Jersey; the five lowest tax States are Florida, Louisiana, Nevada, Wyoming, and Texas. Tax burdens range from $863 in Jacksonville, Florida, to $3,672 in Milwaukee, Wisconsin. The 48-state average is $2,031.

Family D: $50,000 Income

Table 4 shows that the average tax burden for Family D is $3,883 and the range is from a low of $1,299 in Jacksonville, Florida, to a high of $7,492 in New York City.[4] The five highest tax States are New York, Wisconsin, Minnesota, Maryland, and Massachusetts. The five lowest are Florida, Nevada, Wyoming, Washington, and Texas. It is noteworthy that none of these has a state or local income tax.

COMPARISONS OF STATES BY DEGREE OF STATE-LOCAL TAX REGRESSION

Estimates of tax burden by family income level suggest how States compare in terms of degree of tax regression.[5] Table 5 shows family tax burdens for each residence location stated as a percent of family income. The percent of income required to pay major state-local taxes declines as income level rises in all but two States, thereby suggesting regression.

States can be compared more readily on the basis of a rough index of regression. Such an index can be computed from columns 1 and 4 of Table 5. This index has as its numerator the percent of a $5,000 family's income required to pay the seven state-local taxes studied and as its denominator the percent of a $50,000 family's income required to pay these same taxes. A number equal to 1 indicates a proportional distribution of tax burden, a number less than 1 indicates progression, and a number greater than 1 indicates regression. The index is shown in Table 6 and ranges from a low of 0.62 in Portland, Oregon, to a high of 2.97 in nearby Seattle, Washington. The 48-state average is 1.62. These results are consistent with the results of other recent studies which have shown that the typical state-local tax system is somewhat regressive.[6]

This index should be interpreted carefully and treated as only a very rough measure of state-local tax regression. One obvious reason for caution is that the index is computed for only the extremes of the income range and it therefore reveals nothing about the trend in tax burden as a percent of family income within the $5,000 to $50,000 range. Another reason is that the tax burden estimates used in computing the index are based on only one residence location from each State.

CONCLUSION

This article shows that where a family lives can have a considerable bearing on the amount it pays in major state and local taxes. Variation in tax levels as well as in the degree of tax regressivity can be traced to differences among States in emphasis placed on particular types of personal taxes, to unequal reliance on business as opposed to personal taxes, and to unequal levels of public services. First, some States rely heavily on sales and property taxes and others on income taxes. It is not surprising, therefore, that States without a broad-based income tax have tax distributions of above average regressivity. Second, unequal emphasis on business taxes helps explain how family tax burdens in some States can be substantially below the level in other States. Those States which derive unusually large amounts of revenue from business taxes or from personal taxes levied on tourists are able to finance substantial portions of program costs from taxes that are to a large extent exported to residents of other States.[7] Third, an obvious

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4. Income tax estimates for Family D are based on the assumption that all income is from wages and salary. This assumption is somewhat unrealistic for Family D because high-income families are likely to derive substantial income from property sources such as dividends, interest, and rents. Use of this assumption results in an understatement of tax burdens in States which tax only dividends and interest. It results in an overstatement in States where either a city or county levies a local income tax that applies exclusively to wage and salary income. Five of the eight cities with local income taxes apply the tax only to wages and salary.

5. A tax is said to be regressive if the percent of taxpayer income paid in tax declines as taxpayer income rises; it is proportional if the ratio tax paid to income remains constant for various levels of taxpayer income; and a tax is defined as progressive if this ratio rises as taxpayer income rises.

6. Tax Foundation, *Tax Burdens and Benefits of Government Expenditures by Income Class, 1965* (New York: Tax Foundation, Inc., 1967); Don Phares, *State-Local Tax Equity: An Empirical Analysis of the Fifty States* (Lexington, Massachusetts: Heath, 1973); J. Pechman and B. Okner, *Who Bears the Tax Burden?* (Washington, D.C.: The Brookings Institution, 1974).

7. A study based on state-local taxes in effect in 1962 estimated that over 25 percent of all state-local taxes were exported in the long run in Delaware, Louisiana, Nevada, and Texas. See Charles E. McLure, Jr., "Tax Exporting in the United States: Estimates for 1962," *National Tax Journal* (March 1967), pp. 49-78.

source of family tax burden differences is unequal levels of public services.

Additional reasons for unequal tax burdens include differences among States in the efficiency with which public services are provided, unequal costs for resources (e.g., labor) used in producing these services, and differences among States in the use made of non-tax charges.

Comparative tax loads is one of many factors that families take into account in deciding where to live. Certainly the primary consideration is place of employment although quality of life variables are likely to receive increasing attention. But tax burdens can also be important. Hopefully the results reported in this article provide information on state-local tax burdens in a form more meaningful than traditional tax comparisons.

In Tables 1 through 4 which follow, the largest cities used for comparisons, by order of the States listed, are: Birmingham, Phoenix, Little Rock, Los Angeles, Denver, Hartford, Wilmington, Jacksonville, Atlanta, Boise, Chicago, Indianapolis, Des Moines, Wichita, Louisville, New Orleans, Portland, Baltimore, Boston, Detroit, Minnepolis, Jackson, St. Louis, Billings, Omaha, Las Vegas, Manchester, Newark, Albuquerque, New York, Charlotte, Fargo, Cleveland, Oklahoma City, Portland, Philadephia, Providence, Columbia, Sioux Falls, Memphis, Houston, Salt Lake City, Burlington, Norfolk, Seattle, Huntington, Milwaukee, and Cheyenne.

Table 1
FAMILY TAX BURDENS, BY TYPE OF TAX AND BY STATE OF RESIDENCE
Family A: $5,000 income

State	Individual income: State	Individual income: Local	General sales: State	General sales: Local	Residential property	Motor vehicle (a)	Cigarette excise	Total tax burden	Rank (b)
Alabama	$15	$50	$112	$56	$112	$ 95	$48	$488	35
Arizona	25	--	107	--	210	107	46	495	32
Arkansas	--	--	83	--	154	115	71	423	42
California	--	--	96	(c)	350	105	40	591	19
Colorado	5	--	86	86	266	107	40	590	20
Connecticut	--	--	80	--	546	208	84	918	2
Delaware	40	--	--	--	308	86	56	490	34
Florida	--	--	67	--	154	87	68	376	45
Georgia	--	--	90	30	238	124	48	530	24
Idaho	10	--	83	--	266	89	36	484	36
Illinois	25	--	136	(c)	350	138	68(d)	717	6
Indiana	50	--	77	--	350	150	24	651	11
Iowa	65	--	74	--	434	102	52	727	5
Kansas	25	--	96	--	392	157	44	714	7
Kentucky	30	100(e)	93	--	126	116	12	477	37
Louisiana	--	--	53	53(f)	84	69	44	303	48
Maine	5	--	89	--	392	133	60	679	10
Maryland	30	15	69	--	462	94	24	694	9
Massachusetts	-25(g)	--	18	--	588	153	64	798	4
Michigan	-85(g)	52	121	--	336	77	44	545	23
Minnesota	135	--	50	--	294	85	72	636	12
Mississippi	--	--	148	--	14	132	44	338	46
Missouri	5	50	89	30	252	118	56(d)	600	17
Montana	50	--	--	--	280	180	48	558	22
Nebraska	-40(g)	--	74	30	350	143	52	609	16
Nevada	--	--	94	(c)	196	89	40	419	43
New Hampshire	--	--	--	--	434	129	52	615	15
New Jersey	--	--	52	--	812	84	76	1,024	1
New Mexico	5	--	135	--	224	82	48	494	33
New York	--	19	84	74(h)	238	91	76(d)	582	21
North Carolina	40	--	102	(c)	238	126	8	514	29
North Dakota	5	--	68	--	294	95	44	506	30
Ohio	15	50	57	7	266	68	60	523	26
Oklahoma	5	--	55	27	210	103	52	452	40
Oregon	-110(g)	--	--	--	336	67	36	329	47
Pennsylvania	--	156	46	--	280	72	72	626	14
Rhode Island	15	--	80	--	378	169	72	714	8
South Carolina	25	--	112	--	168	128	24	457	39
South Dakota	--	--	122	31	350	85	48	636	13
Tennessee	--	--	101	43	252	76	52	524	25
Texas	--	--	67	17	210	95	74	463	38
Utah	15	--	140	(c)	210	118	32	515	28
Vermont	-5(g)	--	41	--	406	106	48	596	18
Virginia	25	--	97	(c)	182	146	50(d)	500	31
Washington	--	--	145	1(i)	182	128	64	520	27
West Virginia	45	--	81	--	84	126	48	384	44
Wisconsin	25	--	74	--	574	76	64	813	3
Wyoming	--	--	92	--	210	104	32	438	41

(a) Includes automobile registration fees, gasoline excise, personal property tax on auto (where applicable), and in a few States special taxes in lieu of property taxes. The amounts reflect taxes that would be paid during calendar year 1973 assuming the auto is registered in each State's capital city.

(b) States are ranked from high to low, with the highest tax State assigned the number 1 and the lowest tax State the number 48.

(c) Indicates that local levy is included in estimate of state sales tax.

(d) Includes local tax on cigarettes.

(e) Includes the ¾ of 1 percent occupational tax levied by Jefferson County for school support.

(f) Includes both the 2 percent New Orleans sales tax and the additional 1 percent rate levied for the Orleans Parish School Board.

(g) Negative amounts result from credits allowed for sales tax paid on food and/or homestead credit.

(h) Reflects the fact that New York City's 4 percent tax rate became effective on July 1, 1974.

(i) Includes the 3/10 of 1 percent tax rate levied by King County in support of public transportation.

Table 2
FAMILY TAX BURDENS, BY TYPE OF TAX AND BY STATE OF RESIDENCE
Family B: $10,000 income

State	*Individual income* State	*Individual income* Local	*General sales* State	*General sales* Local	*Residential property*	*Motor vehicle (a)*	*Cigarette excise*	*Total tax burden*	*Rank (b)*
Alabama	$150	$100	$172	$ 86	$164	$ 95	$48	$ 815	28
Arizona	150	--	158	--	307	107	46	768	35
Arkansas	160	--	129	--	225	115	71	700	39
California	60	--	158	(c)	512	105	40	875	24
Colorado	160	--	127	127	389	107	40	950	16
Connecticut	--	--	143	--	799	208	84	1,234	5
Delaware	240	--	--	--	451	86	56	833	26
Florida	--	--	112	--	225	87	68	492	47
Georgia	80	--	138	46	348	124	48	784	32
Idaho	140	--	123	--	389	89	36	777	34
Illinois	150	--	202	(c)	513	138	68(d)	1,071	9
Indiana	150	--	128	--	512	150	24	964	15
Iowa	300	--	119	--	635	102	52	1,208	7
Kansas	130	--	145	--	574	157	44	1,050	11
Kentucky	240	200(e)	151	--	184	116	12	903	19
Louisiana	50	--	88	88(f)	123	69	44	462	48
Maine	60	--	144	--	574	133	60	971	14
Maryland	250	125	113	--	676	94	24	1,282	4
Massachusetts	280	--	33	--	861	153	64	1,391	3
Michigan	-60(g)	152	178	--	492	77	44	883	22
Minnesota	540	--	85	--	430	85	72	1,212	6
Mississippi	40	--	237	--	21	132	44	658	41
Missouri	110	100	133	44	369	118	56(d)	930	17
Montana	280	--	--	--	410	180	48	918	18
Nebraska	40	--	111	44	512	143	52	902	20
Nevada	--	--	135	(c)	287	89	40	551	46
New Hampshire	--	--	--	--	635	129	52	816	27
New Jersey	--	--	94	--	1,189	84	76	1,443	2
New Mexico	80	--	200	--	328	82	48	738	36
New York	210	82	134	117(h)	349	91	76(d)	1,059	10
North Carolina	260	--	156	(c)	348	126	8	898	21
North Dakota	100	--	114	--	430	95	44	783	33
Ohio	60	100	98	12	389	68	60	787	31
Oklahoma	50	--	85	43	307.	103	52	640	42
Oregon	240	--	--	--	492	67	36	835	25
Pennsylvania	200	312	86	--	410	72	72	1,152	8
Rhode Island	120	--	131	--	553	169	72	1,045	12
South Carolina	160	--	172	--	246	128	24	730	37
South Dakota	--	--	186	47	512	85	48	878	23
Tennessee	--	--	154	66	369	76	52	717	38
Texas	--	--	109	27	307	95	74	612	43
Utah	150	--	207	(c)	308	118	32	815	29
Vermont	220	--	66	--	595	106	48	1,035	13
Virginia	180	--	149	(c)	267	146	50(d)	792	30
Washington	--	--	216	2(i)	266	128	64	676	40
West Virginia	140	--	126	--	123	126	48	563	45
Wisconsin	370	--	126	--	840	76	64	1,476	1
Wyoming	--	--	136	--	308	104	32	580	44

See notes, Table 1.

Table 3
FAMILY TAX BURDENS, BY TYPE OF TAX AND BY STATE OF RESIDENCE
Family C: $25,000 income

State	*Individual income* State	*Individual income* Local	*General sales* State	*General sales* Local	*Residential property*	*Motor vehicle (a)*	*Cigarette excise*	*Total tax burden*	*Rank (b)*
Alabama	$ 600	$250	$287	$143	$ 350	$131	$48	$1,809	33
Arizona	650	--	249	--	656	171	46	1,772	34
Arkansas	775	--	216	--	481	168	71	1,711	35
California	700	--	281	(c)	1,094	159	40	2,274	15
Colorado	775	--	205	205	631	169	40	2,225	17
Connecticut	--	--	271	--	1,706	399	84	2,460	10
Delaware	1,250	--	--	--	962	97	56	2,365	11
Florida	--	--	201	--	481	113	68	863	48
Georgia	725	--	229	76	744	196	48	2,018	28
Idaho	975	--	200	--	831	101	36	2,143	21
Illinois	525	--	325	(c)	1,094	218	68(d)	2,230	16
Indiana	450	--	228	--	1,094	233	24	2,029	26
Iowa	875	--	207	--	1,356	148	52	2,638	7
Kansas	550	--	238	--	1,225	278	44	2,335	13
Kentucky	750	500(e)	266	--	394	172	12	2,094	24
Louisiana	225	--	160	160(f)	263	80	44	932	47
Maine	350	--	250	--	1,225	199	60	2,084	25
Maryland	800	400	201	--	1,444	116	24	2,985	4
Massachusetts	1,025	--	63	--	1,837	269	64	3,258	2
Michigan	225	452	286	--	1,050	94	44	2,151	20
Minnesota	1,725	--	154	--	919	136	72	3,006	3
Mississippi	475	--	395	--	44	225	44	1,183	42
Missouri	575	250	217	72	788	168	56(d)	2,126	23
Montana	950	--	--	--	875	338	48	2,211	18
Nebraska	325	--	180	72	1,094	231	52	1,954	29
Nevada	--	--	217	(c)	612	138	40	1,007	46
New Hampshire	--	--	--	--	1,356	183	52	1,591	39
New Jersey	--	--	185	--	2,537	107	76	2,905	5
New Mexico	525	--	322	--	700	104	48	1,699	36
New York	1,175	329	233	204(h)	744	117	76(d)	2,878	6
North Carolina	1,000	--	261	(c)	743	187	8	2,199	19
North Dakota	825	--	205	--	919	135	44	2,128	22
Ohio	400	250	182	23	831	78	60	1,824	32
Oklahoma	525	--	142	71	656	161	52	1,607	38
Oregon	1,175	--	--	--	1,050	77	36	2,338	12
Pennsylvania	500	781	176	--	875	81	72	2,485	9
Rhode Island	525	--	231	--	1,181	325	72	2,334	14
South Carolina	875	--	286	--	525	220	24	1,930	31
South Dakota	--	--	306	76	1,094	122	48	1,646	37
Tennessee	--	--	256	110	787	86	52	1,291	40
Texas	--	--	191	48	656	184	74	1,153	44
Utah	825	--	332	(c)	656	182	32	2,027	27
Vermont	950	--	119	--	1,268	118	48	2,503	8
Virginia	825	--	249	(c)	569	257	50(d)	1,950	30
Washington	--	--	352	3(i)	568	192	64	1,179	43
West Virginia	500	--	211	--	263	198	48	1,220	41
Wisconsin	1,500	--	229	--	1,794	85	64	3,672	1
Wyoming	--	--	220	--	656	161	32	1,069	45

See notes, Table 1.

Table 4
FAMILY TAX BURDENS, BY TYPE OF TAX AND BY STATE OF RESIDENCE
Family D: $50,000 income

State	Individual income: State	Individual income: Local	General sales: State	General sales: Local	Residential property	Motor vehicle (a)	Cigarette excise	Total tax burden	Rank (b)
Alabama	$1,300	$ 500	$418	$209	$ 600	$131	$48	$3,206	37
Arizona	1,750	--	362	--	1,125	171	46	3,454	34
Arkansas	2,300	--	314	--	825	168	71	3,678	31
California	2,900	--	408	(c)	1,875	159	40	5,382	7
Colorado	1,950	--	298	298	1,425	169	40	4,180	20
Connecticut	--	--	394	--	2,925	399	84	3,802	27
Delaware	2,500	--	--	--	1,650	97	56	4,303	17
Florida	--	--	293	--	825	113	68	1,299	48
Georgia	2,050	--	333	111	1,275	196	48	4,013	21
Idaho	2,650	--	291	--	1,425	101	36	4,503	11
Illinois	1,150	--	472	(c)	1,875	218	68(d)	3,783	28
Indiana	950	--	331	--	1,875	233	24	3,413	35
Iowa	1,900	--	301	--	2,325	148	52	4,726	10
Kansas	1,500	--	346	--	2,100	278	44	4,268	18
Kentucky	1,600	1,000(e)	387	--	675	172	12	3,846	25
Louisiana	750	--	232	232(f)	450	80	44	1,788	43
Maine	1,200	--	363	--	2,100	199	60	3,922	24
Maryland	1,900	950	293	98	2,475	116	24	5,856	4
Massachusetts	2,250	--	91	--	3,150	269	64	5,824	5
Michigan	1,050	952	416	--	1,800	94	44	4,356	16
Minnesota	3,900	--	224	--	1,575	136	72	5,907	3
Mississippi	1,350	--	574	--	75	225	44	2,268	41
Missouri	1,450	500	315	105	1,350	168	56(d)	3,944	23
Montana	2,500	--	--	--	1,500	338	48	4,386	15
Nebraska	1,150	--	262	105	1,875	231	52	3,675	32
Nevada	--	--	315	(c)	1,050	138	40	1,543	47
New Hampshire	--	--	--	--	2,325	183	52	2,560	39
New Jersey	--	--	269	--	4,350	107	76	4,802	9
New Mexico	2,000	--	469	--	1,200	104	48	3,821	26
New York	4,350	1,038	339	297(h)	1,275	117	76(d)	7,492	1
North Carolina	2,550	--	379	(c)	1,275	187	8	4,399	14
North Dakota	2,200	--	298	--	1,575	135	44	4,252	19
Ohio	1,200	500	264	33	1,425	78	60	3,560	33
Oklahoma	1,750	--	206	103	1,125	161	52	3,397	36
Oregon	3,400	--	--	--	1,800	77	36	5,313	8
Pennsylvania	1,000	1,562	256	--	1,500	81	72	4,471	12
Rhode Island	1,650	--	336	--	2,025	325	72	4,408	13
South Carolina	2,450	--	416	--	900	220	24	4,010	22
South Dakota	--	--	445	111	1,875	122	48	2,601	38
Tennessee	--	--	373	160	1,350	86	52	2,021	42
Texas	--	--	278	69	1,125	184	74	1,730	45
Utah	1,900	--	483	(c)	1,125	182	32	3,722	30
Vermont	3,000	--	173	--	2,175	118	48	5,514	6
Virginia	2,100	--	362	(c)	975	257	50(d)	3,744	29
Washington	--	--	512	4(i)	975	192	64	1,747	44
West Virginia	1,550	--	307	--	450	198	48	2,553	40
Wisconsin	3,750	--	333	--	3,075	85	64	7,307	2
Wyoming	--	--	320	--	1,125	161	32	1,638	46

See notes, Table 1.

Table 5
DISTRIBUTION OF MAJOR STATE-LOCAL TAX BURDENS RELATIVE TO FAMILY INCOME SIZE, 1974
(Tax burdens as percentages of income)

State	Income for family of four, 1974			
	$5,000	$10,000	$25,000	$50,000
All States	11.5	8.9	8.1	7.7
Alabama	9.8	8.2	7.2	6.4
Arizona	9.9	7.7	7.1	6.9
Arkansas	8.5	7.0	6.8	7.4
California	11.8	8.8	9.1	10.8
Colorado	11.8	9.5	8.9	8.4
Connecticut	18.4	12.3	9.8	7.6
Delaware	9.8	8.3	9.5	8.6
Florida	7.5	4.9	3.5	2.6
Georgia	10.6	7.8	8.1	8.0
Idaho	9.7	7.8	8.6	9.0
Illinois	14.3	10.7	8.9	7.6
Indiana	13.0	9.6	8.1	6.8
Iowa	14.5	12.1	10.6	9.5
Kansas	14.3	10.5	9.3	8.5
Kentucky	9.5	9.0	8.4	7.7
Louisiana	6.1	4.6	3.7	3.6
Maine	13.6	9.7	8.3	7.8
Maryland	13.9	12.8	11.9	11.7
Massachusetts	16.0	13.9	13.0	11.6
Michigan	10.9	8.8	8.6	8.7
Minnesota	12.7	12.1	12.0	11.8
Mississippi	6.8	6.6	4.7	4.5
Missouri	12.0	9.3	8.5	7.9
Montana	11.2	9.2	8.8	8.8
Nebraska	12.2	9.0	7.8	7.4
Nevada	8.4	5.5	4.0	3.1
New Hampshire	12.3	8.2	6.4	5.1
New Jersey	20.5	14.4	11.6	9.6
New Mexico	9.9	7.4	6.8	7.6
New York	11.6	10.6	11.5	15.0
North Carolina	10.3	9.0	8.8	8.8
North Dakota	10.1	7.8	8.5	5.5
Ohio	10.5	7.9	7.3	7.1
Oklahoma	9.0	6.4	6.4	6.8
Oregon	6.6	8.4	9.4	10.6
Pennsylvania	12.5	11.5	9.9	8.9
Rhode Island	14.3	10.5	9.3	8.8
South Carolina	9.1	7.3	7.7	8.0
South Dakota	12.7	8.8	6.6	5.2
Tennessee	10.5	7.2	5.2	4.0
Texas	9.3	6.1	4.6	3.5
Utah	10.3	8.2	8.1	7.4
Vermont	11.9	10.4	10.0	11.0
Virginia	10.0	7.9	7.8	7.5
Washington	10.4	6.8	4.7	3.5
West Virginia	7.7	5.6	4.9	5.1
Wisconsin	16.3	14.8	14.7	14.6
Wyoming	8.8	5.8	4.3	3.3

Table 6
COMPARISONS OF STATE-LOCAL TAXES, BY DEGREE OF REGRESSIVITY

State	*Index of regressivity*	*State*	*Index of regressivity*
All States	1.62		
Alabama	1.53	Nebraska	1.65
Arizona	1.43	Nevada	2.71
Arkansas	1.15	New Hampshire	2.41
California	1.09	New Jersey	2.14
Colorado	1.40	New Mexico	1.30
Connecticut	2.42	New York	0.77
Delaware	1.14	North Carolina	1.17
Florida	2.88	North Dakota	1.84
Georgia	1.33	Ohio	1.48
Idaho	1.08	Oklahoma	1.32
Illinois	1.88	Oregon	0.62
Indiana	1.91	Pennsylvania	1.40
Iowa	1.53	Rhode Island	1.63
Kansas	1.68	South Carolina	1.14
Kentucky	1.23	South Dakota	2.44
Louisiana	1.69	Tennessee	2.63
Maine	1.74	Texas	2.66
Maryland	1.19	Utah	1.39
Massachusetts	1.38	Vermont	1.08
Michigan	1.25	Virginia	1.33
Minnesota	1.08	Washington	2.97
Mississippi	1.51	West Virginia	1.51
Missouri	1.52	Wisconsin	1.12
Montana	1.27	Wyoming	2.67

A PROFILE OF MAINE'S POOR

1. Introduction

It is very difficult to prepare a condensed, easy to grasp picture of Maine's poor. Yet, some sort of understanding of their lives is essential if the question of what is or is not a fair tax burden is to be tackled.

Thus, the profile will attempt a general picture of Maine's poor and then attempt to glimpse the reality of their lives by a close examination of Maine housing conditions. Cost of housing is crucial to the question of fair tax burdens. Property taxes are one of the most onerous burden on Maine's poor. For example, in 1974 Maine had the 2nd heaviest burden in the nation as to property taxes per $1,000 of personal income ($70.09).

2. General profile of Maine's poor

The following three descriptions offer an insight into the monetary condition of Maine's poor (see also this chapter analyses of how many Mainer's are in each income bracket).

A. Income and Prices

This section provides information about household and personal incomes for Maine and its counties through Calendar Year 1973 and cost of living changes in the U.S. and the Northeast through June 1974. Income data collected in the 1970 U.S. Census and reported in earlier editions of Profile Of Poverty follow the more recent income and price information. For income data related to specific topics see also EMPLOYMENT, EDUCATION, SOCIAL PROGRAMS AND POTENTIAL CLIENTS, HOUSING and CITIZEN OPINION.

Incomes in Maine continue to lag behind those in the rest of New England and the nation. Maine's per capita income was $400 less than the U.S. and $600 less than the New England figures in 1960. These differentials had increased by 1973 to $1,000 and $1,100 respectively. Median after-tax household incomes in Maine, the U.S. and New England were $8,600, $9,600 and $10,100 in 1973. One quarter of Maine households had after-tax incomes less than $5,330 while one quarter had incomes above $13,070. This $7,700 difference between the top and bottom quarter was greater than the 1967 difference of $5,100. Even after taking inflation into account, the top quarter of households gained $600 more in constant purchasing power than did the bottom 25%. Median after-tax household incomes of counties varied from a low of $6,000 in Washington County to a high of $9,600 in Cumberland.

Inflation has become a serious problem. Consumer prices rose an average of 47% in the urban Northeast from 1967 to June 1974. Prices for food and housing, the biggest items in the budgets of the poor, rose faster than other goods and services. U.S. Consumer prices for heating fuel and gasoline, two other items for which the poor spend a proportionately greater share of their incomes, rose by 114% and 67%. After taking into account those increases, median income in Maine increased only $90 in purchasing power between 1967 and 1974.

- from Profile on Poverty In Maine (1975)

B. Poverty incomes in Maine

Size of family unit	Nonfarm family	Farm family
1	$2,970	$2,550
2	3,930	3,360
3	4,890	4,170
4	5,850	4,980
5	6,810	5,790
6	7,770	6,600

For family units with more than 6 members, add $960 for each additional member in a nonfarm family and $810 for each additional member in a farm family.

- from Department of Labor (1977

C. Maine incomes by household

In analyzing the data, estimations to the general population, and number of households have been made based on data presented to the Social Science Research Institute by the State Planning Office and the Maine State Housing Authority. These estimations are presented below:

TOTAL HOUSEHOLDS IN MAINE, 1975			321,029
Tenure:	Homeowners	69.7%	223,757
	Renters	22.7%	72,874
	Mobile Homes	7.6%	24,398
Income:	Low ($0 - $7,000)	32.2%	103,371
	Medium ($7 - $15,000)	48.4%	155,378
	High ($15,000 +)	19.4%	62,280
ESTIMATED TOTAL POPULATION, 1975			1,026,000
Income:	Low ($0 - $7,000)	32.2%	330,372
	Medium ($7 - $15,000)	48.4%	496,584
	High ($15,000 +)	19.4%	199,044

- from Maine Human Services Council (1977)

3. Maine housing conditions

By looking closely at Maine housing conditions, we can begin to understand what it is like to be poor in Maine. First, we examine a composite profile provided by the administrators of Maine's Project Fuel:

PROJECT FUEL II
COMPOSITE PROFILE OF CLIENT SERVED

The typical Project FUEL II family had a male head of household between the ages of 31 and 50 years of age with a wife and 1 or 2 children under 18. The family head was unemployed with the family income under $5,000/year, and the family was receiving food stamps. The family was living in their own home valued at less than $5,000 and paid over $50/month for utilities.

The house had 5 rooms, incomplete plumbing, a basement foundation and a central hot air furnace and/or stove which burned fuel oil. Over 1,200 gallons of fuel oil were burned during the previous heating season (fall '74-spring '75) which translates to between $400-$500 at the prevailing prices.

Project FUEL II provided approximately $75 worth of insulating materials which required fewer than 10 hours for installation.

Next, for a more comprehensive picture, we turn to the House Services Council 1977 report. Maine's Hidden Poor In Substandard Housing.

HOUSING NEEDS IN MAINE

Serious Housing Maintenance Problems:

There are an estimated 122,633 (38.2 percent) households in Maine with one or more serious home maintenance problems.[1] These problems include need for roof repair, outside painting, the presence of dry rot, cracked basement walls, defective heating systems and sagging buildings. Of those households which have two or more home maintenance problems, 27,467 (46.5 percent) are those with total family incomes of less than $7,000 compared with 25,577 (43.3 percent) whose total family incomes are between $7,000 and $15,000, and 6,025 (10.2 percent) with total family incomes of $15,000 and above.

Generally, those households which have major maintenance problems have had them for a long time. For instance, the present data show that:

* 42,954 (89.8 percent of) households needing insulation have had this condition for 4 or more years:
* 18,472 (82.2 percent of) households having structural sags have had these sags for 4 or more years;
* 12,759 (73.6 percent of) households having dry rot have had this condition for 4 or more years;
* 7,494 (66.7 percent of) households with cracked basement walls have had these conditions for 4 or more years;
* 8,411 (65.5 percent of) households with defective heating systems have had this condition 4 or more years;
* 5,834 (46.6 percent of) households needing plumbing repair have had the problem 4 or more years;
* 5,778 (40.0 percent of) households needing chimney repair have had this problem 4 or more years;
* 8,270 (27.7 percent of) households needing roof repair have had the problem for 4 or more years;
* 15,788 (26.3 percent of) households needing outside painting have had the problem 4 or more years.

In summary, for those in Maine who have serious home maintenance problems, these problems have existed for long periods of time and are not simply cosmetic or minor. In fact, the latter kinds of problems, including outside painting and cracked windows, are problems existing for less time than major structural problems.

Relationship of Income to Existence of Maintenance Problem:

The housing needs of Maine people are dramatically related to their incomes. As Table I indicates, home maintenance problems, both cosmetic and major, are more likely to be found in low income households. The reason low income people report not making necessary repairs is primarily lack of financial means.

Existing housing problems are not evenly distirbuted among homeowners, renters and apartment dwellers. The fewest number of housing concerns are presented by mobile home dwellers; the greatest number by renters. These data are affected, no doubt, by the fact that over 50 percent of mobile homes in Maine have been purchased since 1971.[2]

Housing Problems Existing Four Years or More Broken Down by Income Group by Percent of the Sample Having Problem Four or More Years and Projected Number of Households

Housing Need Identified by Income Group	% of Sample Under $7,000	Projected Number of Households	% of Sample $7,000-15,000	Projected Number of Households	% of Sample $15,000 +	Projected Number of Households
*Walls Need Insulation	87.5%	17,969	94.8%	20,415	92.7%	4,908
*Sagging Building	85.0%	8,769	88.2%	7,978	60.0%	1,795
Heating System	72.0%	4,391	55.0%	2,478	75.0%	1,682
*Dry Rot	68.4%	6,664	80.0%	5,169	50.0%	576
**Basement Cracks	60.0%	3,070	80.0%	1,733	100.0%	651
Plumbing	46.6%	3,324	49.0%	2,741	50.0%	374
*Chimney Repair	44.4%	2,248	38.5%	2,929	---	0
Outside Painting	36.6%	10,064	19.3%	5,068	18.8%	1,698
Roof Repair	32.3%	5,309	21.4%	2,893	20.0%	448
Windows Broken	22.2%	2,432	22.2%	2,001	---	0

*Mobile homes not included in tabulation.

**Mobile homes nor renters included in tabulation.

Houses Lacking Basic Facilities:

Low income people living in Maine are much more likely to lack the basic facilities that are associated with standards of adequate housing than are the general population. For instance, over 7,236 low income households (7.0 percent) do not have hot and cold running water compared with less than 2% of the remaining households in this state; another 3,825 low income households (3.7 percent) do not have flush toilets; 2,274 low income households (2.2 percent) lack complete kitchens, including a range, water, and refrigerator while no households with incomes of over $7,000 per year reported lacking these facilities.

Central heat, a housing comfort expected by nearly all Maine residents, is significantly less available in low income households where 17,056 (16.5 percent) do not have central heating.

In sum, comparing the responses of low income and the general population, low income households are significantly less likely to have basic housing facilities than the general population. These differences are presented in Table II.

Table II

Comparison of Housing Lacking Basic Facilities Between Homes Owned by Low Income People and Homes Owned by Other Income Groups

Housing Facility Lacked	% Low Income Not Having a Basic Facility	Projected Total Households Not Having Basic Facility	% General Population Not Having Basic Facilities
Complete Kitchen	2.2	2,274	0.7
Flush Toilet	3.7	3,825	1.6
Hot and Cold Water	7.0	7,236	3.2
Central Heat	16.5	17,056	8.0

That low income houses are less likely to have basic facilities is consistent with the fact that low income people live in the older houses in Maine.

Costs of Housing in Maine:

The total annual cost of housing in Maine, based upon cost of mortgage, repairs and maintenance, taxes, heating, electricity and water and sewer (not including insurance costs) amounts to $2,310 per year or $192.50 per month.

Table III

Comparison of Economic Status
and Expenditures for Total Housing Costs

	Economic Status					
	Under $7,000		$7-15,000		$15,000 and over	
Total Housing Costs	% of Sample in Each Expenditure Group	Number of Households in Each Expenditure Group	% of Sample in Each Expenditure Group	Number of Households in Each Expenditure Group	% of Sample in Each Expenditure Group	Number of Households in Each Expenditure Group
Up to $1,599	41.1	42,485	20.7	32,163	15.4	9,591
$1,600 to $2,309	30.5	31,529	22.9	35,582	20.9	13,017
$2,310 to $3,355	16.8	17,366	30.7	47,701	22.0	13,702
$3,356 and over	11.6	11,991	25.7	39,932	41.8	26,033

1975 Tax Rec

TD84

STATE OF MAINE - BUREAU OF TAXATION
INDIVIDUAL MAINE ADJ GROSS INCOME 08/31/76

		MJ	MJ TAX PAID	MS	MS TAX PAID	S	S TAX PAID	NON-RES	TAX PAID
I	NEGATIVE	0	0.00	[illegible]	0.00	0	0.00	0	0.00
N	0.00	2,241	0.01	104	0.00	1,402	0.00	1,163	0.00
C	0.01 - 1,999.99	5,691	0.00	1,379	2,[illegible]15.74	39,106	67,041.78	3,687	3,967.05
O	2,000.00 - 2,999.99	5,446	4,823.74	755	5,726.53	17,869	188,230.42	1,679	10,770.41
M	3,000.00 - 3,999.99	6,651	25,819.62	631	9,662.69	14,487	280,266.28	1,278	15,722.24
E	4,000.00 - 4,999.99	8,260	70,804.87	690	20,296.15	13,680	467,918.72	1,227	26,380.35
	5,000.00 - 5,999.99	9,643	142,827.94	661	29,570.13	12,931	649,349.81	1,306	39,835.35
	6,000.00 - 6,999.99	10,802	235,810.21	536	32,724.73	10,090	678,476.30	1,042	38,783.96
P	7,000.00 - 7,999.99	11,647	363,916.63	541	47,123.00	8,172	725,265.63	1,012	50,121.86
A	8,000.00 - 8,999.99	12,512	529,765.11	327	34,915.01	6,351	711,121.09	997	60,850.61
N	9,000.00 - 9,999.99	12,971	710,664.97	246	32,143.62	4,809	648,529.93	941	71,202.44
G	10,000.00 - 10,999.99	13,213	913,225.08	157	23,316.43	3,508	556,111.00	744	67,240.32
E	11,000.00 - 11,999.99	13,010	1,106,851.21	105	17,305.49	2,675	498,471.83	679	73,508.48
	12,000.00 - 12,999.99	12,708	1,300,197.46	70	13,882.08	2,053	438,808.15	774	100,819.30
	13,000.00 - 13,999.99	11,876	1,437,940.90	61	1[illegible]371.68	1,456	362,745.48	788	112,9[illegible].31
	14,000.00 - 14,999.99	10,923	1,552,801.90	48	13,942.60	1,123	315,985.50	542	91,176.18
	15,000.00 - 15,999.99	9,603	1,577,054.79	29	8,167.48	819	255,173.49	429	82,494.78
	16,000.00 - 16,999.99	8,497	1,594,252.83	21	5,522.81	625	212,488.17	352	70,408.39
	17,000.00 - 17,999.99	7,254	1,525,988.98	27	8,315.42	458	172,688.35	278	65,934.59
	18,000.00 - 18,999.99	5,839	1,385,103.96	15	5,841.62	343	143,234.33	232	59,329.05
	19,000.00 - 19,999.99	5,050	1,318,904.67	8	3,435.59	268	119,952.16	199	55,453.25
	20,000.00 - 22,499.99	8,776	2,666,456.46	20	8,924.12	417	210,409.45	329	104,100.69
	22,500.00 - 24,999.99	5,364	1,975,115.65	15	7,545.74	278	165,140.32	215	82,015.80
	25,000.00 - 27,499.99	3,398	1,499,584.93	8	5,480.42	192	131,734.77	121	53,833.88
	27,500.00 - 29,999.99	2,252	1,173,001.68	7	2,170.32	167	123,949.96	88	45,009.13
	30,000.00 - 34,999.99	2,466	1,589,787.67	21	16,640.33	181	158,978.96	94	63,929.17
	35,000.00 - 39,999.99	1,435	1,168,158.96	2	2,501.60	95	105,761.02	50	42,153.43
	40,000.00 - 44,999.99	926	917,530.35	4	4,624.34	72	89,464.81	32	35,871.56
	45,000.00 - 49,999.99	623	729,229.46	1	1,621.80	61	87,381.77	22	25,162.60

50,000.00 - [illegible],999.99	1,497	2,477,454.59	2	7.36	128	252,916.20	60	93,5[illegible]3
75,000.00 - 99,999.99	478	1,306,055.25	3	10,979.88	54	173,925.70	38	95,664.59
100,000.00-124,999.99	179	687,002.94	1	4,189.12	18	84,700.46	21	75,031.85
125,000.00-149,999.99	86	445,230.16	0	0.00	6	32,302.80	9	50,360.02
150,000.00-174,999.99	49	323,726.88	0	0.00	5	36,494.87	3	22,951.00
175,000.00-199,999.99	27	215,164.87	0	0.00	0	0.00	3	24,240.44
200,000.00-224,999.99	14	132,650.50	0	0.00	4	37,219.61	2	19,569.5[illegible]
225,000.00-249,999.99	11	98,488.15	0	0.00	1	10,416.41	0	0.00
250,000.00-274,999.99	2	22,405.69	0	0.00	1	15,375.58	1	13,078.48
275,000.00-299,999.99	4	49,290.22	0	0.00	0	0.00	0	0.00
300,000.00-324,999.99	4	55,189.30	0	0.00	0	0.00	1	9,215.08
325,000.00-349,999.99	1	9,709.46	0	0.00	0	0.00	0	0.00
350,000.00-374,999.99	3	55,156.25	0	0.00	0	0.00	0	0.00
375,000.00-399,999.99	2	42,692.54	0	0.00	1	13,912.01	1	17,446.42
400,000.00-424,999.99	2	40,876.96	0	0.00	1	22,794.82	1	21,644.00
425,000.00-449,999.99	0	0.00	0	0.00	0	0.00	0	0.00
450,000.00-474,999.99	1	26,121.62	0	0.00	0	0.00	1	11,479.27
475,000.00-499,999.99	1	25,257.02	0	0.00	0	0.00	0	0.00
500,000.00- UP	4	133,108.95	1	38,462.54	1	109,191.88	5	168,683.98
TOTALS	211,40[illegible]	33,659,601.39	6,491	428,096.37	143,908	9,353,929.82	20,446	2,148,060.84

TOTAL COUNT	382,247
RES ONLY COUNT	361,801
PART YEAR RES	7,724
NON-RES	12,457
RESIDENTS	362,066
NONRES EXEMPTS	35,380
PART RES EXEMPTS	18,465
RES EXEMPTS	958,956
TOTAL EXEMPTS	1,012,801

The Revenue Instrument of Choice

Table 3

Suppose Your State Government Must Raise Taxes Substantially, Which of These Do You Think Would be the Best Way to Do It?

	March 1976	March 1972
State Sales Tax	45%	46%
State Income Tax	25	25
State Property Tax	10	14
Other	6	5
Don't Know	14	10

The public clearly favors the sales tax if state taxes have to be increased. These 1976 poll results closely match our findings in 1972—the last time this question was asked.

There are significant variations, however, when the responses are examined on a regional basis (Table 3A). Northeastern respondents picked the state sales tax much less frequently than did the respondents in the other three regions and the income tax received considerably less than average support in the South.

The strongest support for the sales tax came from families residing in new suburbs or in rural areas, upper income families, and those in the 50-59 age category.

Homeowners and renters also differed sharply on this tax increase issue—49% of the homeowners favored a state sales tax increase as contrasted to only 35% of the renters. As might be expected, the property tax received considerably more support from renters (19%) than from homeowners (6%).

Table 3A

Suppose Your State Government Must Raise Taxes Substantially Which of these Do You Think Would Be the Best Way to do it -- State Income Tax, or State Sales Tax, or State Property Tax?

1. State Income Tax
2. State Sales Tax
3. State Property Tax
4. Other
5. Don't Know

	March 1976				
	1.	2.	3.	4.	5.
Total U.S. Public	25	45	10	6	14
Men	27	44	11	6	12
Women	24	45	9	6	16
18-29 Years of Age	27	43	17	5	9
30-39	23	48	9	7	13
40-49	28	45	8	8	11
50-59	18	51	7	6	18
60 Years or Over	26	40	6	5	23
Less Than High School Complete	23	38	10	5	24
High School Complete	24	49	10	6	12
Some College	30	48	10	7	5
Professional	30	49	10	5	6
Managerial	23	51	10	8	8
Clerical, Sales	24	43	16	6	11
Craftsman, Foreman	25	53	9	6	7
Other Manual, Service	24	41	12	6	17
Farmer, Farm Laborer	13	49	9	6	23
Rural	22	51	8	6	14
Old Suburb	29	44	7	4	16
New Suburb	15	60	8	11	6
City – 1 Family	27	45	11	6	11
City – Multifamily	24	37	9	9	21
City – Apartment	25	33	19	7	16
Northeast	28	37	12	6	17
North Central	26	48	9	6	12
South	20	47	11	5	17
West	30	46	8	8	9
Under $5,000 Family Income	26	32	12	4	27
$5,000-$6,999	20	45	8	6	21
$7,000-$9,999	23	44	13	7	13
$10,000-$14,999	24	50	10	7	9
$15,000 or Over	26	52	8	8	6
White	25	47	10	6	12
Non-White	24	30	9	10	27
No Children in Household	25	43	10	6	16
With Children Under 18	25	47	10	6	12
With Teenagers 12-17	27	44	9	6	14
Own Home	27	49	6	6	12
Rent Home	20	35	19	6	20

For a similar breakdown of 1972 data, see Appendix Table C.

FROM, THE ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS (1976)

Measuring the Fiscal "Blood Pressure" of the States: 1964-1975

INTRODUCTION

Disparities in economic growth rates among various regions of the nation have become sufficiently severe to attract the attention of the popular press. *Business Week*, in its May 17, 1976, issue, actually announced the coming of the "second war between the states"[1] as a result of the rapid shift of population, capital, and jobs from the Northeast and Midwest to the South and the West. Following this theme, the *National Journal* recently published a study of regional differences in federal spending patterns. The study concluded that "federal tax and spending policies are causing a massive flow of wealth from the Northeast and Midwest to the fast growing Southern and Western regions of the nation,"[2] thus exacerbating present growth patterns. It goes on to add:

> The states at the receiving end of high federal outlays (those in the South and West) also tend to be those that tax their own citizens least for state and local government services.
>
> On the other hand, the balance of payments situation generally is adverse in the Northeast and Midwest, where population is stagnant or

[1] "The Second War Between the States," *Business Week*, May 17, 1976, No. 2432, pp. 92-114.

[2] "Federal Spending: The North's Loss is the Sunbelt's Gain," *National Journal*, June 26, 1976, pp. 878-891.

declining, where unemployment is the most severe, where relative personal income is falling and where the heaviest state and local tax burdens are imposed.[3]

Similar to the discovery of city-suburb disparities in the 1960s, a number of observers feel that findings such as these indicate the need for major revisions in the federal aid system. Rather than reinforcing the fortunes of the fast growing regions of the South and West, federal policy should now provide more help to the slow growth areas of the Northeast and Midwest. However, even those suggesting revision would concede the need to develop more accurate techniques for measuring the severity of this "war between the states" and its effect on state-local fiscal systems.

This paper has a limited goal — to build a more sophisticated measure of state-local fiscal stress by comparing the variations in tax loads borne by the 50 state-local systems. Such measures — alternatively called tax burdens when viewed from the perspective of the taxpayer or tax effort when viewed from the perspective of the taxing jurisdiction — provide estimates of the relative balance between the tax revenue raised by a jurisdiction and its fiscal capacity. While there is no generally agreed upon, best measure of fiscal pressure, the traditional measure is the ratio of state-local tax collections to resident personal income for a given year.

NEED FOR BETTER MEASURES OF FISCAL PRESSURE

This traditional measure has the advantages of simplicity and ease of calculation, however, as an estimator of relative fiscal balance it also has a number of weaknesses. The two most important are: (1) it is single dimensional — a specific point in time that cannot reveal trends; and (2) resident personal income tends to ***understate*** the fiscal capacity of those states that are in a relatively good position to export a substantial portion of their tax load and *overstate* the fiscal capacity of those states that are not in such a fortunate position. As a result, the ratio of tax collections to income in any one year can be a misleading indicator of diversities in relative fiscal balance.

[3]*Ibid.*, p. 878 (parentheses added).

The Two-Dimensional Approach

Traditional estimates of fiscal pressure provi[de] interstate comparisons of relative fiscal positio[n] at a given time. There is however a second factor, time dimension, which should be considere[d] when comparing state-local fiscal systems. Re[gardless] of the fiscal pressure at a given point i[n] time, both the citizens of the state and multistat[e] corporations are more likely to perceive a heavie[r] burden in those states where tax burdens are ris[ing] than in those states where taxes as a percent[age] of income are either remaining relatively con[stant] or falling. It is that *perceived* pressure which may help to account for some of the resistance on the part of the taxpayer to increase the size of the public sector and the reluctance of corporations to locate in certain states. Therefore, tax trends should be included as a part of any estimate of comparative fiscal position.

Table 1 develops a fiscal pressure index which includes a time span dimension. *Column 1* is the ratio of own-source tax collections to resident personal income for 1975. The ratios are indexed based on the United States' median and ranked accordingly in *Columns 2 and 3*. In 1975, fiscal pressure ranged from a low of 9.1% in Arkansas to a high of 16.2% in New York.

Column 4 presents estimates of the average annual rate of change in tax effort from 1964 to 1975.[4] *Columns 5 and 6* index these rates of change based on the U.S. median and show their relative ranking. For eight states — South Dakota, Iowa, Colorado, North Dakota, Idaho, Kansas, Oklahoma, and Florida — tax pressure actually fell between 1964 and 1975. Note the degree of diversity in growth among the states. The range of growth rates was from an average increase of 3.069% per year in New York to a fall of 1.031% per year in North Dakota for a differential of 4.1% per year. In index number terms, the difference was almost 400% between these two states.

Column 7 combines these two dimensions into a single measure of "fiscal blood pressure" based on each state's index numbers. The numerator or "systolic" reading indicates the state's relative position in 1975. The denominator or "diastolic" measurement indicates the state's relative change in pressure from 1964 to 1975. Thus, the median state's fiscal pressure becomes 100 over 100.

[4]Average annual *rate* of change in the ratio of total state and local taxes to resident personal income.

Table II divides the states into quadrants: those with *relatively* high and rising increases in pressure; those with *relatively* high and falling pressure; those with *relatively* low and rising increases in pressure; and those with *relatively* low and falling pressure. With the exception of Hawaii, California, Nevada, and West Virginia, all of the states in the relatively high and rising category are in New England, the Mideast, and the Great Lakes region, while about half the sunbelt states are in the relatively low and falling group.[5]

In order to visualize these patterns and the changes involved, *Chart I* plots all of those states more than one standard deviation from the median in 1975 on either index. The most "deviant" state is New York which is actually more than two standard deviations from the median and continuing to rise. Significantly, the states in the sunbelt region do not appear so advantaged when this more rigorous test of dispersion is employed — only Alabama, Arkansas, Florida, Oklahoma, and Tennessee are more than one standard deviation from the median in the relatively low and falling category.

Table I

A Two-Dimensional Measure of Relative State-Local Fiscal Pressure Using Resident Personal Income to Estimate Fiscal Capacity: 1964–75

State	Own-Source Taxes as a Percentage of Income, 1975[1] (1)	Index (2)	Rank (3)	Average Annual Rate of Change in Tax Effort, 1964-75 (Percent Per Year)[2] (4)	Index (5)	Rank (6)	A Two-Dimensional Fiscal Pressure Index (7)
United States							
Median	11.10	100		1.033	100		
New England							
Maine	12.30	111	9	1.486	144	19	111/144
New Hampshire	10.25	92	38	1.565	152	18	92/152
Vermont	14.67	132	2	1.873	181	12	132/181
Massachusetts	13.86	125	3	2.935	284	2	125/284
Rhode Island	11.45	103	16	1.854	179	13	103/179
Connecticut	10.36	93	34	1.769	171	15	93/171

Table II

A Two-Dimensional Measure of Relative State-Local Fiscal Pressure Using Resident Personal Income to Estimate Fiscal Capacity: Dividing the States Into Quadrants: 1964–75 (Indexed on Median)

High and Falling		High and Rising	
Wisconsin	119[1]/88[2]	New York	146/297
Arizona	114/ 75	Vermont	132/181
New Mexico	110/ 77	Massachusetts	125/284
Louisiana	109/ 91	California	125/158
Wyoming	108/ 73	Hawaii	124/249
Montana	106/ 27	Minnesota	121/115
Oregon	103/ 90	Maine	111/144
Washington	103/ 88	Nevada	110/172
Mississippi	102/ 67	Maryland	105/245
		Rhode Island	103/179
		West Virginia	102/129
		Michigan	102/115
		New Jersey	101/258
		Illinois	101/233
		Delaware	101/260
		Pennsylvania	100/207

Low and Falling		Low and Rising	
South Dakota	100/–87	Kentucky	95/168
Iowa	99/ –2	Connecticut	93/171
Colorado	99/ –9	Alaska	93/279
Utah	97/ 8	Georgia	93/121
North Dakota	96/–100	New Hampshire	92/152
Indiana	95/100	District of Columbia	92/213
Idaho	94/–26	Virginia	91/213
Kansas	93/–44	Missouri	89/130
North Carolina	92/ 75	Ohio	85/104
Nebraska	91/ 74		
South Carolina	90/ 96		
Texas	87/ 44		
Oklahoma	87/–15		
Florida	86/–42		
Tennessee	86/ 37		
Alabama	84/ 46		
Arkansas	82/ 4		

[1]Tax pressure index for 1975.
[2]Index of change in tax pressure 1964–75.

Source: ACIR staff estimates based on U.S. Department of Commerce, Office of Business Economics, *Survey of Current Business*, various years; and U.S. Bureau of the Census, *Governmental Finances*, various years.

Pechman and Okner Study of the 1966 MERGE Data File

The most comprehensive, yet dated, study of tax burdens was done by Pechman and Okner in the 1974 study, Who Bears the Tax Burden (Brookings Institution). This study was unique in that it was based on a 1966 data base, the MERGE computer file. The complexity of estimating tax incidence (burden) is indicated by the fact that Pechman and Okner felt compelled to use 8 different incidence assumptions. The chart below is based on incidence (burden) assumptions Variant 1c and Variant 3b. Variant 1c produced the most progressive distribution of tax burdens; Variant 3b produced a slightly regressive distribution. What are these incidence assumptions? Peckman and Okner explain:

> The crucial factors in determining the degree of progressivity in the tax system as a whole are the assumptions made with respect to the incidence of the *corporation income tax* and the *property tax*. If it is assumed that these are taxes on corporate stockholders and owners of property (Variant 1c), they are highly progressive. The corporation income tax rises from about 2 percent of income at the bottom of the income scale to almost 26 percent at the top; the property tax rises from about 2.5 percent to 10 percent.[18] Assuming that half of the corporation income tax is a tax on consumption and that the property taxes on improvements are taxes on shelter and consumption (Variant 3b), progressivity virtually disappears. Since the ratio of total consumption and housing expenditures to annual income falls as incomes rise, the burden of the corporation income tax under Variant 3b is U shaped, while the property tax is regressive throughout the income scale. Together these two taxes amount to only 10.6 percent of income for families with incomes above $1,000,000 under Variant 3b, as compared with a total of 35.8 percent under 1c.

TABLE 4-8. Effective Rates of Federal, State, and Local Taxes, by Type of Tax, Variants 1c and 3b, by Adjusted Family Income Class, 1966

Income classes in thousands of dollars; tax rates in percent

Adjusted family income	Individual income tax	Corporation income tax	Property tax	Sales and excise taxes	Payroll taxes	Personal property and motor vehicle taxes	Total taxes
			Variant 1c				
0–3	1.4	2.1	2.5	9.4	2.9	0.4	18.7
3–5	3.1	2.2	2.7	7.4	4.6	0.4	20.4
5–10	5.8	1.8	2.0	6.5	6.1	0.4	22.6
10–15	7.6	1.6	1.7	5.8	5.8	0.3	22.8
15–20	8.7	2.0	2.0	5.2	5.0	0.3	23.2
20–25	9.2	3.0	2.6	4.6	4.3	0.2	24.0
25–30	9.3	4.6	3.7	4.0	3.3	0.2	25.1
30–50	10.4	5.8	4.5	3.4	2.2	0.1	26.4
50–100	13.4	8.8	6.2	2.4	0.7	0.1	31.5
100–500	15.3	16.5	8.2	1.5	0.3	0.1	41.8
500–1,000	14.1	23.0	9.6	1.1	0.1	0.2	48.0
1,000 and over	12.4	25.7	10.1	1.0	[a]	0.1	49.3
All classes[b]	8.5	3.9	3.0	5.1	4.4	0.3	25.2
			Variant 3b				
0–3	1.2	6.1	6.5	9.2	4.6	0.4	28.1
3–5	2.8	5.3	4.8	7.1	4.9	0.4	25.3
5–10	5.5	4.3	3.6	6.4	5.7	0.3	25.9
10–15	7.2	3.8	3.2	5.6	5.3	0.3	25.5
15–20	8.2	3.8	3.2	5.1	4.7	0.3	25.3
20–25	9.1	4.0	3.1	4.6	4.1	0.2	25.1
25–30	9.1	4.3	3.1	4.0	3.6	0.2	24.3
30–50	10.5	4.7	3.0	3.5	2.6	0.2	24.4
50–100	14.1	5.6	2.8	2.4	1.3	0.1	26.4
100–500	18.0	7.4	2.4	1.7	0.7	0.1	30.3
500–1,000	17.7	9.0	1.7	1.4	0.4	0.2	30.3
1,000 and over	16.6	9.8	0.8	1.3	0.3	0.2	29.0
All classes[b]	8.4	4.4	3.4	5.0	4.4	0.3	25.9

Source: Computed from the 1966 MERGE data file. For an explanation of the incidence variants, see Table 3-1.
Note: Variant 1c is the most progressive and 3b the least progressive set of incidence assumptions examined in this study.
a. Less than 0.05 percent.
b. Includes negative incomes not shown separately.

Pechman and Okner explain the significance of this chart:

> The *individual income tax* is distributed in the same way under both sets of incidence assumptions. (See Table 3-1.) Revenue from this source accounts for about one-third of all 1966 taxes, and this obviously has an important influence on the distribution of tax burdens. The individual income tax is progressive over virtually the entire income scale, but it becomes regressive at the very top. This pattern reflects the fact that in the highest income classes a rising portion of total income as defined in this study is not subject to income tax at either the federal or the state level.[16] The individual income tax imposes the heaviest burden—15.3 percent of adjusted family income under Variant 1c and 18.0 percent under 3b—on incomes between $100,000 and $500,000. (See Table 4-8.)
>
> The differences in the effective rates of individual income tax at the same income level are due entirely to the different definitions of income used in the two sets of assumptions. Under Variant 1c, the corporation income tax and the property tax on improvements are included in adjusted family incomes of stockholders and property income recipients; under Variant 3b, half the corporation income tax and the entire property tax on improvements are regarded as indirect taxes and are distributed among all family units in calculating adjusted family income.[17] As a consequence, stockholders and property income recipients have much higher adjusted family incomes under Variant 1c than under 3b, and the burden of the individual income tax relative to incomes at the top of the income scale (where dividends and other property incomes are large) is reduced.
>
> *Sales and excise taxes* are clearly regressive throughout the entire income scale. They begin at over 9 percent of income at the bottom and decline to about 1 percent at the top, reflecting the fact that the proportion of family income spent on goods and services subject to tax falls as income rises.
>
> *Payroll taxes* are progressive for families with incomes up to about the $10,000 level, where they reach a maximum of about 6 percent and then become regressive. The progressivity of payroll taxes at the lower end of the income scale reflects two facts: (1) a large proportion of income received by very low-income units—mainly transfer payments—is not subject to these taxes; and (2) many low-income workers are in jobs that are not covered by the employment tax system. Payroll taxes are regressive above $10,000 because they are levied at a flat rate up to a maximum amount of annual taxable earnings; above this level, the tax accounts for a declining percentage of income. In Variant 3b half of the employer payroll tax is assumed to be shifted to the consumer through higher prices. Thus the effective payroll tax rate at the two ends of the distribution is increased as compared with Variant 1c.
>
> *Personal property taxes and motor vehicle licenses* are regressive at the lower end of the income scale and proportional or slightly progressive in the higher classes. The effect of these taxes on relative tax burdens is small because they amount to no more than 0.4 percent of income throughout the income scale.

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STATE OF MAINE
ONE HUNDRED AND EIGHTH LEGISLATURE
COMMITTEE ON TAXATION

MAINE TAX STRUCTURE

Description of Areas of Possible Reform

This study, prepared by the Legislative Joint Committee on Taxation, is meant to be a constantly updated analysis of Maine taxes and policy issues. Further, it offers with each tax analysis a listing of commonly voiced areas of reform. The Committee on Taxation does not necessarily endorse any of these reform suggestions; indeed, some of them are contradictory. Rather, it offers them for public debate. If any Legislator wishes to further pursue any specific tax reform measure, please contact the Office of Legislative Assistants, Room 427, State House.

The members of the Office of Legislative Assistants who staff the Committee on Taxation in the preparation of this study are:

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A. THE SALES-USE TAX IN GENERAL

1. Sales-Use Tax Theory

a. Sales taxes

Sales taxes are imposed directly on sales or are measured by sales. Taxes imposed directly on sales are commonly known as "consumer sales taxes" since the tax is based on the consideration for each sale and is paid by the purchaser who buys at retail. Taxes measured by sales are known as "occupation" or "license" taxes.

Sales taxes are usually imposed on each article only once; sales for resale are usually not taxed. Raw materials incorporated into a finished product are not usually taxed but sales of tools, coal, etc. used or consumed in manufacturing and not incorporated into the product to be sold usually are taxed.

The different forms of sales taxes are:

(1) Consumer's taxes: paid by purchaser.
(2) Occupation or license taxes: taxes measured by the gross receipts from sales; the vendor usually passes the tax onto the consumer by adding it to the selling price.
(3) General sales tax: both wholesalers and retailers are taxed on the basis of their gross sales for the privilege of engaging in the business of selling tangible personal property.
(4) Gross proceeds taxes: taxes based not only on sales of goods but also on sales of services (e.g. car repairs, haircuts).
(5) Admissions tax: specific tax on admissions to entertainment events.

b. Use taxes

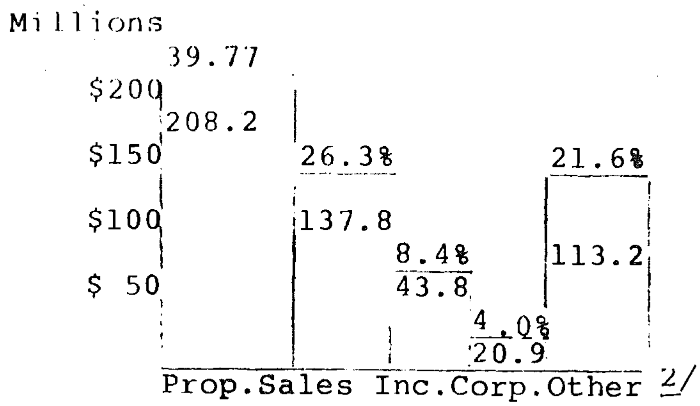
The use tax complements sales tax by taxing the storage, use or consumption in the State of personal property purchased outside the State. All States with such a tax allow a credit on sales taxes paid on the same property in another state.

2. Sales - Use Tax in Maine

Maine has a General Sales-Use Tax with a current rate of 5%; in revenue it will generate for 1975-1976 $137.6 million per year and makes up 26.3% of the State tax mix:

Present Tax Mix for 1975-76

Percent of Total



3. Sales-Use Taxes in New England

a. Comparative rates

	Rate (1975)	Revenue as a % of personal income (1973)
Connecticut	7%	2.7 1/
Maine	5%	3.2
Massachusetts	5% 3/	--
New Hampshire	--	--
Rhode Island	5%	2.2
Vermont	3%	1.5
U.S. Average	3.5%	2.1

b. Specific features

The most specific differences in surrounding states are the existance of several admission taxes, the taxation of some services, and Vermont's highly equitable income tax credit for a percentage of paid sales taxes.

(1) Connecticut. In addition to a general retail sales tax, Connecticut also taxes certain services and has a separate 10% tax on all admissions to places of amusement, entertainment or recreation.

1/ "Other" taxes include all undedicated revenues (alcohol, cigarettes, aeronautical, and miscellaneous business) and the dedicated motor fuel tax.

2/ Connecticut's sales-use tax rate in 1973 was 6.5%

3/ Massachusetts has an 8% tax on restaurant meals and restaurant alcohol.

(2) Massachusetts. The sales tax is based on the total sales price; services are not taxed, any piece of clothing up to $175 price is exempted.
(3) New Hampshire. Does not have a sales-use tax.
(4) Rhode Island. Does not tax services; has an admissions tax.
(5) Vermont. This State taxes heating oil and provides, in order to lessen the sales taxes regressivity, an apparently succesful income tax credit for sales taxes paid.

B. THE SALES TAX IN MAINE

1. A Description Of How The Tax Is Administered In Maine

The following analysis is taken from the Commerce Clearing House State Tax Guide (second edition):

¶ 60-485 **MAINE**

¶ 60-486 **Sales and Use Taxes**

Persons and Sales Subject to Tax.—A tax is imposed upon sales at retail, the rental of rooms or lodging of continuous or temporary residence (the retailer shall refund the tax for the first 28 days of continuous residence), telephone and telegraph services, including installation and equipment usage, gross proceeds from closed circuit telecasts of boxing matches and upon the storage, use or other consumption of tangible personal property purchased at retail (Tit. 36, Secs. 1811, 1816). The term "sale at retail" does not include casual sales (Tit. 36, Sec. 1752). The use tax does not apply if tax at an equal or greater rate has been paid in another jurisdiction (Tit. 36, Sec. 1862).

Exemptions.—

1. Sales which this state is prohibited from taxing under the constitution of the United States or of Maine.
2. Sales to Maine, the United States or their political subdivisions or agencies.
3. Food products for human consumption, except meals served on or off the premises of the retailer. Meals served to patients of licensed hospitals and nursing institutions are exempt.
4. Medicines for human beings sold on doctor's prescription; sales of prosthetic devices or eyeglasses, wheelchairs and crutches (Ch. 593, Laws 1973).
5. Meals served by schools.
6. Seed, feed, hormones, pesticides, insecticides, fungicides, weed killers, defoliants, litter, medicines and fertilizer used in agricultural production, and bait sold to commercial fishermen.
7. Gasoline and motor fuels now taxed by the state.
8. Coal, oil, wood and all other fuels, except gas and electricity, used for cooking or heating in buildings designed for human habitation; sales of fuel used in burning blueberry fields (Ch. 594, Laws 1973).
9. Cigarettes subject to other taxes imposed by Ch. 16.
10. Spirituous or vinous liquors sold in state liquor stores.
11. Returnable containers.
12. Bibles and other religious books and utensils of worship.
13. Regularly issued publications.
14. Sales to incorporated hospitals, incorporated, nonprofit nursing homes, schools, nonprofit corporations conducting medical research or establishing and maintaining laboratories for scientific study and investigation in biology or ecology or operating educational television or radio stations and regularly organized churches, except such sales, storage or use in activities as are mainly commercial enterprises.
15. Automobiles used in driver education programs.
16. Automobiles sold to amputee veterans.
17. Motor vehicles purchased by nonresidents to be taken out of the state immediately (Ch. 527, Laws 1975).
18. Ships' stores.
19. Rental charged for living quarters at camps entitled to exemption from property tax under chapter 91-A.
20. Rental charged for living quarters in a state-licensed hospital or nursing home; sales to incorporated, private, nonprofit, state-licensed residential child care institutions.

21. Rental charged for living quarters for a student at a school.
22. Rental charged persons residing continuously for 28 days at any one hotel.
23. Funeral services.
24. Boats sold to nonresidents.
25. Sales to incorporated volunteer fire departments and nonprofit ambulance corps.
26. Sales of gasoline and motor fuels upon which a tax is imposed by any other state or province, but not including jet or turbo jet fuels.
27. Sales of aircraft purchased by nonresidents and used outside the state.
28. Meals served by institutions and homes licensed by the Department of Health and Welfare.
29. Sales to community mental health facilities.
30. Sales of certified water and air pollution control facilities including parts or accessories.
31. Sales of new machinery and equipment used by the purchaser directly in producing tangible personal property to be sold or leased for final use by manufacturing, processing, assembling or fabricating (Ch. 794, Laws 1974, 1st Spec. Sess.; Ch. 580, Laws 1973).
32. All medical equipment and supplies used by diabetics in the treatment of diabetes (Ch. 148, Laws 1973).
33. Sales of new machinery and equipment used by the purchaser in research and development (Ch. 580, Laws 1973).
34. Vending machine sales of property costing 15¢ or less if the retailer derives more than 50% of his gross receipts from vending machine sales (Ch. 766, Laws 1974, 1st Spec. Sess.; Tit. 36, Sec. 1760).
35. Sales at retail for 10¢ or less, provided the retailer is primarily engaged in making such sales (Tit. 36, Sec. 1811).
36. Separately stated transportation charges from retailer's place of business directly to the purchaser; sales of tangible personal property which become an ingredient or component part of tangible personal property or are consumed or destroyed in manufacturing tangible personal property for later sale or lease (other than lease for use in Maine); electricity separately metered and consumed in any electrolytic process in manufacturing property for later sale (Chs. 359, 450, Laws 1975; Tit. 36, Sec. 1752).

When one or more motor vehicles, boats, aircraft or farm tractors are traded in on the sales price of another motor vehicle, boat, aircraft or farm tractor, the tax is levied only on the difference between the sales price of the purchased vehicle, boat, aircraft or tractor and the sales price of the vehicle, boat, aircraft or tractor taken in trade (Chs. 317, 528, Laws 1975; Tit. 36, Sec. 1765).

Basis.—The sales tax and the use tax are measured by the sale price (Tit. 36, Secs. 1811, 1861).

Rates.—The rate of the sales and use tax is 5% (Tit. 36, Secs. 1811, 1861). The following bracket system is provided for collection of the tax (Tit. 36, Sec. 1812):

Sales Price	Tax	Sales Price	Tax
10¢ or less	No tax	41¢ through 60¢	3¢
11¢ through 20¢	1¢	61¢ through 80¢	4¢
21¢ through 40¢	2¢	81¢ through 99¢	5¢

Over 99¢, 5¢ for each whole dollar plus the amount indicated above for each fractional part of a dollar.

Permit Requirements.—Every seller of tangible personal property, whether or not at retail, but excluding casual sellers, must secure a registration certificate, valid indefinitely, for each place of business from the State Tax Assessor. No fee is necessary. Sellers of tangible personal property who solicit orders by means of salesmen within the state for retail sales for use, storage or consumption within the state must register with the Assessor (Tit. 36, Sec. 1754). Bonds may be required (Tit. 36, Sec. 1759).

Reports.—Reports are due with the Assessor by every retailer and person subject to the use tax on or before the 15th of each month. The Assessor may permit the filing of returns other than monthly (Tit. 36, Sec. 1951).

Collection.—Tax to be added to the sale price and collected by the retailer from the purchaser (Tit. 36, Sec. 1812). Tax is due and payable at the time of the sale. The State Tax Assessor may permit postponement of payment until not later than the date when the sales or rentals so taxed are required to be reported (Tit 36, Sec. 1952). It is unlawful for a retailer to represent that the tax will be assumed by the retailer or that it will be refunded (Tit. 36, Sec. 1761).

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 60-000.

2. Analyses

a. Economic Effect

A State sales tax in the range of 4 to 6 percent will not effect businesses any more than any other tax yielding the same revenue. The first most directly affected will be retailers, for they must assume costs of collection (on the average, only a small fraction of 1 percent of the expenses of doing business). Further, since all retailers in the same line of business must incur roughly the same relative expense, they should generally be able to pass it on to their customers.

The tax presents an incentive to reduce consumption of taxed items in favor of savings, thus providing some encouragement for capital investment.

Sales taxes do not reduce incentives to work - as graduated rate income taxes possibly do.4/

A sales tax that is restricted to tangible goods alone distorts the allocation of resources (i.e. consumer purchases, capital investments) in favor of services, which are not taxed.

An oppressive level might cause consumers to make important purchases in tax-free New Hampshire.

b. Yield

1) The sales tax in Maine currently yields 137.8 million a year and represents 26.3% of the State tax mix.

2) Elasticity: the sales tax appears to be elastic - thus, it responds directly to changing economic decisions. For example, for fiscal year 1975-76 sales revenues have consistantly been behind projections.

4/ See generally Tax Foundation, State and Local Sales Taxes, 37-39, (1970).

3) Yield from increased rates:

5-1/2% - insrease of $18.5 million

c. Incidence

A general sales tax is bourne by consumers in proportion to their total expenditures, because the tax does not change relative prices and hence does not alter consumption patterns.5/ As a rule, retailers shift the general sales completely forward to the consumers.6/

d. Equity

Sales taxes are clearly regressive throughout the entire income scale. They begin at over 9% of income at the bottom income levels and decline to about 1% of the wealthiest's income. This reflects the fact that the proportion of family income spent on those goods and services subject to taxes falls as income rises.7/ Wealthier people put a larger portion of their incomes into investments and savings; poorer people do not have this option. Wealthier people also spend larger portions of their income on services, personal and professional, which are not currently taxed in Maine.8/

Because Maine exempts food, its sales tax has thus lost most of its regressiveness. Consider the following analysis of sales tax burden: (a minus equity represents regressiveness):

5/ Consumption patterns are altered, however, to the extent that various personal consumption items are exempted. By not taxing personal services, (hair cuts, repairs) for example, consumers are persuaded to spend more on services than for retail goods selected to the tax.

6/ Tax Foundation, State and Local Sales Taxes, 29 (1970) .

7/ Pechman, Okner, Who Bears the Tax Burden, 31, 58 (1974).

8/ Massachusetts Public Finance Project, The Rich Get Richer and The Rest Pay Taxes, 51 (1974).

INDICES OF VERTICAL AND HORIZONTAL EQUITY UNDER ALTERNATIVE RETAIL SALES TAXES 9/

Type of Retail Sales Tax	Indices of Vertical Equity	Indices of Horizontal Equity
Broad Based Tax		
Including Food	-0.15	2.54
Exempting Food	-0.04	1.94
Uniform Tax Credit on		
Per Capita Basis[a]	0.02	1.75
Per Family Basis[b]	0.21	1.18
Vanishing Tax Credit Variable on		
Income Per Capita[c]	0.82	0.89
Family Income & Size[d]	1.02	0.61

a. $2.60 per capita
b. $8.60 per family
c. For families with income less than $1,000, the credit equals $10.80 per capita. For every additional $1,000 in family income the credit per capita is reduced by $1.80 vanishing at incomes greater than $6,000.
d. The credit is the recently enacted New Mexico adoption adjusted to equal the cost of an over-the-counter food exemption.

If conditions in Maine match this analysis, then Maine's sales tax, which exempts food, is horizontally progressive and slightly vertically regressive. However, the chart also indicates that a broad based sales tax and income tax credit system produces both vertical and horizontal equity. Positive aspects of the sales tax are its visibility and the fact that the taxpayer makes a voluntary decision each time he or she pays.

9/ Charles Vars, "Equity Trade-Offs in Sales Taxation", National Tax Journal, 657-58 (1975). Horizontal equity requires equal treatment of equals (e.g. families of equal incomes yet different sizes). Vertical equity, in this analysis, is defined as the difference between the mean effective tax rate on families in the 5 highest and 5 lowest income classes under each tax, divided by the mean effective tax rate on all families.

e. Administration

The sales tax, as compared with most other levies, is relatively easy to administer and for taxpayers to comply with. Most problems in gaining taxpayer compliance involve relatively small, and especially new, firms. The most common problems are delinquency and failure of vendors to maintain adequate records, and these arise mainly with small sellers.

Cost of administration and compliance are relatively low. As a share of tax collected, it costs most States from .7% to 1.5% to administer the tax. The higher the rate, the lower the percentage cost of administration. 10/

f. Comments

Maine is an important tourist State; thus, the sales tax is the primary tool by which the State can assure that tourists pay their fair share for the services they enjoy. At this time, the sales tax base excludes personal and business services and is possibly too narrow considering the importance of the sales tax to a tourist state. By expanding the base to include at least some services, the regressiveness of the sales tax is lessened. This is because as a person's income increases, the portion devoted to purchases of services also increases. Further, the equities of this basically regressive 11/ tax could be greatly improved by a sales tax credit, administered through the income tax, designed to lessen the burden of sales taxes on the poor and the working poor. These comments are expanded upon in the following section, Possible Reform Areas.

10/ Tax Foundation, State and Local Sales Taxes, 40-50, (1970)
11/ As was stated in section B 2 (d) Equity, because Maine exempts take-home food, the sales tax, on the average, loses most of its regressiveness.

C. POSSIBLE AREAS OF REFORM

Presented below are a listing of some possible areas of sales tax reform, along with a brief rationale for each suggestion.

1. The sales tax base could be expanded to include specific services.

An expression of the general rationale behind expanding the sales tax base is offered by Professor John F. Due, one of this country's leading expert on sales taxation: [12]

THE CASE FOR TAXING SERVICES

The failure to tax services has long been a major defect in sales taxes. The major arguments for including them within the sales tax base are:

1. Under the philosophy that sales taxes should cover as broad a base of consumer expenditures as possible, with exemption only when specifically justified, the tax should apply to services as well as commodities, since both categories satisfy personal wants. There is no inherent feature of most services that warrants their exclusion.
2. Expenditures on services tend to rise as incomes rise; taxation of services therefore tends to make sales taxes less regressive.
3. As total personal income rises, total expenditures on services tend to rise more rapidly than expenditures on commodities. The yield of the taxes therefore adjusts more exactly in terms of rising levels of economic activity.
4. A number of services are rendered in conjunction with the sale of taxable commodities. Compliance and administration are far simpler if the entire charge is taxable than if a separation between service and commodity is necessary.

The type of service most suitable for inclusion within the tax is that rendered by business establishments, rather than by professional men or other individuals. If the tax is confined to businesses, over-all administration will be simplified; if it is extended to personal service rendered by individuals and professional men, a number of new problems are created. There are significant objections as a matter of social policy to taxing medical, dental, hospital, and related services, legal service, and the like. Other services, such as accounting, which are rendered primarily to business firms, should not be taxed for the same reasons that apply to all other producers goods.

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[12] Due, State Sales Tax Administration, 166-67 (1964)

Thus, specifically, there is particular justification for taxing the following services in addition to certain public utilities.

1. Admissions.
2. All repair of tangible personal property, refinishing, repainting, and the like.
3. Charges for installing tangible personal property in real property.
4. Charges for printing; photographic work of all types, including developing; bookbinding; and the like. The charges would not be taxable when the services were performed on an article to be sold:
5. Laundry, dry cleaning, and related activities.
6. Barber shop and beauty parlor service.
7. Hotel, motel, and other transient accommodations.
8. Charges for parking of motor vehicles (other than municipal parking meter charges).
9. All charges for work relating to motor vehicles, such as towing, battery charging, and greasing.
10. Charges for storage of all tangible personal property.

Contra to Professor Due's reasoning, the Governor's Tax Policy Committee recommended extending the sales tax base to include almost all goods and services. See A Tax Policy For Maine, 36-39 (1975).

If Professor John Due's rationale is followed - expanding the base to include only personal services rather than professional or business services - the following revenue yields might be realized in the Standard Industrial Classifications (SIC) of personal services, amusement and recreation services, and miscellaneous repair services: 13/

Personal Services Sic 72
Laundries, Cleaning, Diaper Service, Carpet Cleaning, Beauty & Barber Shops
Shoe Repair, Funeral Service

	Sales in Maine Million				
	73	74	75	76	77
Total Personal Service Sales	$54.8	60.8	63.5	69.8	76.6
State Revenue - 3%	$1.640	1.820	1.900	2.090	2.300
4%	$2.190	2.430	2.430	2.790	3.060
5%	$2.74	3.040	3.040	3.490	3.830

13/ These estimates were provided by Dr. Edgar A. Miller, the State Economist.

Amusement & Recreation Services Sic. 79

Motion Pictures, Bowling Alley, Golf Course, Membership Sport Club, Amusement Parks

Million Dollars

	73	74	75	76	77
Estimated Receipts	$21.900	24.310	25.380	27.890	30.610
State Revenue - 3%	.660	.730	.760	.840	.920
4%	.880	.970	1.020	1.120	1.220
5%	1.100	1.220	1.270	1.390	1.530

Misc. Repair Services Sic. 76

Electrical & Electronic Repair, Refirgeration, Reupholstery, Misc. Repair

The estimates here are likely to be somewhat high concerning sales tax revenue since taxes are currently collected for parts used in these services and we have no reliable way of substracting this amount.

Million Dollars

	73	74	75	76	77
Estimated Repair Service Sales	$20.700	22.970	23.980	26.350	28.930
State Revenue - 3%	.620	.690	.720	.790	.870
4%	.830	.920	.960	1.050	1.160
5%	1.035	1.150	1.200	1.320	1.450

The Governor's Tax Policy Report recommended expanding the sales tax base to include not only personal services but also business and professional services. This would mean the following increased revenues:

12/1976

Miscellaneous Business Service Sic. 73

Advertising, Window Cleaning, Computer Service, Management Consulting, Equipment Rental, Commercial Photo, Employment Agencies

Million Dollars

		73	74	75	76	77
Estimated Receipts		$47.640	52.870	55.210	60.660	66.580
State Revenue	- 3%	$1.430	1.590	1.660	1.820	2.000
	4%	1.910	2.110	2.210	2.430	2.660
	5%	2.380	2.640	2.760	3.030	3.330

Professional Services 14/

	3%	4%	5%
Medical Doctors	$2.4	$3.2	$4.0
Engineering Architects	$ .5	$ .6	$ .8
Lawyers	$1.03	$1.37	$1.72

14/ This grouping of professional services does not include accountants, dentists, artists, chemists, taxidermists, morticians, interior decorators. Dr. Miller states that the professional estimates he was able to find were "very rough"; and that "in each case the tax would be passed on to the consumer with some undesireable consequences."

If in fact the sales tax is expanded, the increased revenues could be used to lower the current rate, increase general fund revenues, finance a tax credit system (see below) or a combination of any of these.

2. Along with an expansion of the sales tax base, the Governor's Tax Policy Report recommended that the sales tax be converted to a tax on luxury consumption through the institution of a sales tax credit system.

The sales tax could be converted to a tax on luxury consumption by instituting a sales tax credit system. This credit could be easily administered through the State personal income tax system and would represent an amount equal to the tax on minimum consumption purchases.

The sales tax credit could be either a flat rate credit, which is administratively simple, or a variable graduated rate credit, which is currently successfully used in Vermont and which more accurately reflects each person's ability to pay.

The sales tax credit system, flat rate or variable, would make the tax a considerably more progressive means of raising revenues. See A Tax Policy For Maine, 36 (1975).

3. All automobile sales new, used, and trade-ins should be treated the same under the sales tax law.

The December 1974 ESCO report on the State tax structure made the following recommendation:

> "Although the Legislature in past years has considered and rejected legislation to remove the current exemption on the allowance for used cars at the time of trade-in, such legislation is still frequently advocated by many persons interviewed during the course of field studies. It is pointed out that the present exemption works a hardship on the new car purchaser who has no car or substantial value to trade in, as in the case of the person who trades cars only once in four or five years, while it gives a substantial advantage to the more affluent customer who trades cars annually. The loss in revenue to the State of Maine is very substantial. If the exemption were removed, the State would receive $8.5 million in additional revenue during the 1976-77 biennium." [15]

15/ ESCO, State of Maine Government Finances, 84 (1974).

Northeast Survey

TABLE IV-5

COMPARISON OF AGGREGATE ECONOMIC IMPACTS OF TOURISTS WITH ESTIMATED AGGREGATE ECONOMIC CONDITIONS IN MAINE--1972/73
(1972 Dollars)

	TOTAL	RESIDENT	NON-RESIDENT
A. Total Tourist Generated Wage and Salary Income	$103,407,000	$20,040,000	$83,367,000
B. Total Wage and Salary Income in Maine[1]	$2,504,000,000		
C. Proportion of Wage and Salary Income Accounted for by Tourist Activity A/B	4.1%	.8%	3.3%
D. Total Tourist Generated Tax Revenue[2]	$29,941,000	$7,518,000	$22,423,000
E. Total Taxes[2] Generated in Maine	$217,109,000		
F. Total State Revenues (Including General Fund and Special Funds)[3]	$506,241,000		
G. Tourist Generated Taxes as a Proportion of Total Taxes D/E	13.8%	3.5%	10.3%
H. Tourist Generated Taxes as a Proportion of All State Revenues D/F	5.9%	1.5%	4.4%

(Continued)

	TOTAL	RESIDENT	NON-RESIDENT
I. Employment Generated by Tourism (in Man-Months)	251,102	47,599	203,503
J. Total Maine Employment[4] (in Man-Months)	3,883,000		
K. Tourist Generated Employment as a Proportion of Total I/J	6.5%	1.2%	5.3%

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[1]Based on Third Quarter, 1972, Income Estimates in Survey of Current Business, October, 1973, Table 1.

[2]Includes Personal Income Tax, Business Income Taxes, Sales and Use Taxes, and the Gasoline Tax. Total Maine taxes are updated to 1972 from Biennial Report of the Bureau of Taxation, 1970.

[3]Includes, in addition to total taxes (E), all other General Fund and Special Fund Revenues. Fiscal 1973. Source: State of Maine, Budget Document 1974-1975. This estimates includes Federal Funds.

[4]Derived from Table 8.1, Maine Pocket Data Book, 1971.

NOTE: All dollar figures rounded to nearest thousand.

TABLE IV-6

TOTAL TOURIST EXPENDITURES IN EACH OF 23 TOURIST EXPENDITURE CATEGORIES (1972/1973)

Categories of Tourist Expenditures	($1,000)	
1. Hotels, Motels and Tourist Courts	$ 38,667	Total Accommodations $48,109
2. Rooming and Boarding Houses	1,124	
3. Camps and Trailer Parks	6,295	
4. Organization Hotels and Lodging Houses	1,124	
5. Friends and Relatives	899	
6. Eating and Drinking Places	67,892	Total Food and Beverages $93,520
7. Food Stores	21,806	
8. Liquor Stores	3,822	
9. Gasoline Service Stations	30,349	Total Transportation $42,939
10. Local Buses and Taxis	450	
11. Tolls	4,047	
12. Automotive Rental and Leasing	2,473	
13. Automobile Parking Fees	225	
14. Air Transportation	1,798	
15. Ferry Services	3,597	
16. Movie and Theater Admissions	1,124	Total Entertainment $11,015
17. Hunting and Fishing Licenses	3,147	
18. Miscellaneous Amusement and Recreation	6,744	
19. Miscellaneous Retail Stores	39,117	Total Miscellaneous $63,171
20. Apparel and Accessory Stores	14,837	
21. Personal Services	2,023	
22. Miscellaneous Repair Services and Business Services	4,496	
23. Telephone Communication	2,698	
TOTAL EXPENDITURES	$258,754	

Source: ADL Tourism Impact Model, based upon NMI expenditure surveys.

STATE SALES AND USE TAX RATES

State tax rates applicable to the retail sale of tangible personal property are tabulated below. Many states also authorize local jurisdictions to adopt sales or sales and use taxes in addition to the state tax. For details see the following state summaries.

	Sales *	Use *
Alabama [1]	4%	4%
Arizona [1]	4%	4%
Arkansas [1]	3%	3%
California [1]	4¾%	4¾%
Colorado [1]	3%	3%
Connecticut	7% [2]	7% [2]
District of Columbia	5%	5%
Florida	4%	4%
Georgia [1]	3%	3%
Hawaii	4%	4%
Idaho	3%	3%
Illinois [1]	4%	4%
Indiana	4%	4%
Iowa	3%	3%
Kansas [1]	3%	3%
Kentucky	5%	5%
Louisiana [1]	3%	3%
Maine	5%	5%
Maryland	5%	5%
Massachusetts	5%	5%
Michigan	4%	4%
Minnesota [1]	4% [3]	4% [3]
Mississippi	5%	5%
Missouri [1]	3⅛%	3⅛%
Nebraska [1]	3½%	3½%
Nevada [1]	3%	3%
New Jersey	5%	5%
New Mexico [1]	4%	4%
New York [1]	4%	4%
North Carolina [1]	3%	3%
North Dakota	3% [4]	3% [4]
Ohio [1]	4%	4%
Oklahoma [1]	2%	4%
Pennsylvania [1]	6%	6%
Rhode Island	6%	6%
South Carolina	4%	4%
South Dakota [1]	4%	4%
Tennessee [1]	4½% [5]	4½% [5]
Texas [1]	4%	4%
Utah [1]	4%	4%
Vermont	3%	3%
Virginia [1]	3%	3%
Washington [1]	4.6%	4.6%
West Virginia [1]	3%	3%
Wisconsin [1]	4%	4%
Wyoming	3%	3%

[Alabama Gross Receipts Tax begins on page 6051.]

* The list of states imposing sales and use taxes does not include Alaska and Delaware. Alaska imposes a business license (gross receipts) tax and Delaware imposes a merchants' and manufacturers' license tax and a use tax on leases. Other states impose occupation, admission, license or gross receipts taxes in addition to sales and use taxes (see Connecticut, Indiana, Maryland, Mississippi, New Mexico, Rhode Island, South Carolina, Texas, Washington and West Virginia).

[1] Local tax rates are additional.

[2] Connecticut: Manufacturing and agricultural production machinery is taxed at 2.5% and enumerated business services are taxed at 3.5%.

[3] Minnesota: Retail sales through coin-operated vending machines are taxed at 3%.

[4] North Dakota: The tax on farm machinery and agricultural irrigation equipment is 2%.

[5] Tennessee: The rate of tax is decreased to 3%, effective July 1, 1978.

STATE OF MAINE

Bureau of Taxation

Sales and Use Tax Instruction Bulletin No. 39

"SALE PRICE" UPON WHICH TAX IS BASED

(Issued February 1, 1965; Revised June 1, 1969; July 1, 1969; September 23, 1971; October 1, 1975)

Section 1811 of the Sales and Use Tax Law levies a sales tax on sales of tangible personal property and certain rentals of living quarters, "measured by the sale price".

Section 1861 of the law levies a similar use tax where sales tax is not paid at the time of purchase, the tax being determined by applying the tax rate to the "sale price" of tangible personal property purchased for use or consumption in this State.

Subsection 14 of Section 1752 of the law defines, among other terms the meaning of "sale price".

The purpose of this bulletin is to explain, on the basis of these statutory provisions, what is to be included in the sale price on which sales or use tax liability is based.

NOTE: The references given are to Title 36 of the Maine Revised Statutes (1964).

1. In General.

a. The sale price on which sales tax is based includes:

i. The full price, valued in money, whether paid in money or otherwise, including the value of traded in property (See section 2, below).

ii. The amount charged for any services (other than for installing or applying or repairing the property sold; and certain service charges in lieu of tips) that are a part of the sale, such as assembly, alteration or fabrication charges, whether separately stated or not (See section 4, below).

iii. Federal manufacturers' or importers' excise taxes with respect to automobiles, tires, cameras, firearms, tobacco, liquor, sporting goods, etc. even though this federal tax is separately stated.

b. The sale price on which sales tax is based does not include:

i. Cash discounts allowed and taken by the purchaser (See section 3, below).

ii. Charges for installing, applying or repairing the property sold, if separately stated (See section 5 a, below); and certain service charges in leiu of tips (See section 5 c, below).

iii. Charges for transportation of goods to vendee, if by common or contract carrier or by mail, and if separately stated (See section 5 b, below).

c. Partial or full credit may be taken by a retailer for transactions previously reported as taxable if:

i. A refund or credit is allowed the purchaser pursuant to warranty. (See section 6a, below).

ii. The full purchase price is refunded to the purchaser upon return of the merchandise. (See section 6b, below).

2. "Sale Price" Is to be Measured in Money. Subsection 14 of Section 1752 of the law says, in part, that " 'Sale price' means the total amount of the sale . . . price . . . of a retail sale, including any services that are a part of such sale, valued in money, whether received in money or otherwise, including all receipts, cash, credits and property of any kind or nature, and any amount for which credit is allowed by the seller to the purchaser, without any deduction therefrom on account of the cost of the property sold, the cost of the materials used, labor or service cost, interest paid, losses or any other expenses whatsoever . . ."

Thus tax applies not only to cash sales, but also to credit sales, and to transactions where the sale price is paid in part or in whole by barter, rendition of services, or any other valuable consideration.

a. Trade-ins. When property is sold, with an allowance being made for traded in property, tax applies to the entire sales price, including the allowance for trade-in. Thus if a refrigerator is sold for $350, the customer paying $300 in cash and $50 by way of allowance on a traded in refrigerator, tax is based on the full price of $350. (The only exception to this is where a motor vehicle, boat, aircraft or farm tractor, is traded in toward the purchase of a motor vehicle, boat, aircraft or farm tractor, in which case Section 1765 of the law specifically provides that the allowance for trade-in shall be deducted from the sale price in computing the tax.)

3. Cash Discounts. The definition of "sale price" states that "discounts allowed and taken on sales shall not be included" in the "sale price".

Thus if a 2% allowance is made for payment within a stated time, and this allowance or discount is actually taken by the customer, tax will apply to the stated price less the discount, or the amount actually paid.

For example, two customers purchase $100 worth of taxable goods, with 2% being allowed for prompt payment. Customer A pays promptly and thus takes the 2% discount: his tax is based upon a sale price of $98. Customer B does not pay promptly and does not take the 2% discount: his tax is based upon a sale price of $100.

On the other hand, if interest is charged on overdue accounts, tax does not apply to the interest so charged.

4. Service Charges Which Are A Part of the Sale Price. The definition of "sale price" says that it includes "any services that are a part of such sale." It also says that "sale price" shall not "include the price received for labor or services used in installing or applying or repairing the property sold, if separately charged or stated."

In other words, the sales tax normally applies to the full charge for the goods sold, including any charges for services which are a part of the sale, except for separately stated charges for installing, applying or repairing the property sold. For example, a caterer undertakes to prepare and serve food for a reception, his charge covering not only the cost of the food, but also the cost of preparation and service. Tax applies to the entire charge, since preparing and serving the food are services which are part of the sale. Even though charges for preparation and serving are separately stated, tax would still apply to these charges, since they are not charges for "installing or applying or repairing the property sold."

a. Alteration Charges. When a merchant offers goods for sale, and undertakes to alter them to the customer's requirements, the charges for such alterations are part of the sale price on which tax is based, whether separately stated or not, unless the customer can be shown to have taken title to the goods in question before the alterations are made. (See Benoit v. Johnson, 160 Me. 201). For example, a customer selects a coat the style and material of which appeal to her. However, certain alterations are necessary before the coat is satisfactory as a piece of wearing apparel for the customer. Unless it can be shown that the customer has in fact taken title to the coat - in short, that she actually owns it - before the alterations are made, the alteration charges will be considered a part of the sale price upon which tax is based, even though such charges are separately stated.

b. Fabrication Charges. Labor or fabrication charges are a part of the price of any manufactured tangible personal property. Usually the question of the taxability of such charges does not arise, since it is a generally accepted fact that tax applies to the sale price of a piece of furniture, for example, although it is also generally known that a part of that price reflects labor going into the making of the chair.

The question does sometimes arise in the case of property made to special order, where the vendor stocks the materials and also fabricates them to the customer's order. In such cases the fabrication charges are a part of the taxable "sale price" whether separately stated or not, unless the customer can be shown to have taken title to the materials before the fabrication takes place.

For example, a customer selects material for drapes and requests the merchant to make the drapes for a particular size and style. Unless it can be shown that the customer has in fact taken title to the material - in short, that he actually owns it - before the fabrication takes place, the fabrication charges will be considered a part of the sale price upon which tax is based.

c. Assembly Charges. Some types of furniture and equipment are sold either on a knocked down, or unfinished, or on an assembled, or finished, basis; the assembled or finished item being priced correspondingly higher. Charges for assembling or finishing, in such cases, are part of the taxable sale price, whether separately stated or not.

In all the above cases, the alteration, fabrication, assembly or finishing of the article sold constitute "services that are a part of (the) sale"; and since they do not fall within the categories of "installing or applying or repairing the property sold," charges for these services are part of the "sale price" and are taxable whether separately stated or not.

5. Charges Excluded from Sale Price. The definition of "sale price" not only excludes "the price received for labor or services used in installing or applying or repairing the property sold if separately stated," but also excludes "the cost of transportation from the retailer's place of business or other point from which shipment is made directly to the purchaser provided such charges are separately stated and provided such transportation occurs by means of common carrier, contract carrier or the United States mails."

a. Charges for Installing or Applying or Repairing the Property Sold, if Separately Stated. Such charges, if separately stated, are not part of the taxable "sale price".

For example, completed drapes are sold by a merchant, who also undertakes to install them at the home of the customer. Tax applies to the full charge for the drapes (See 4b, above) as well as to the charge for any hardware or other tangible personal property involved in the transaction; but the installation charges, if separately stated, are not part of the taxable "sale price".

Or, if a customer brings in a piece of furniture to be stained or painted, the merchant may charge tax on the price of the paint or stain, but will not charge tax on the charge for applying the paint, or stain, if separately stated. (Note that this differs from the situation where the customer picks out the piece of furniture from the dealer's stock, but wishes it painted or stained before taking title to it, in which case the total charge is taxable (See 4c, above).)

Transactions involving the repair of the property sold rarely, if ever, occur.

i. Separate Statement of Charges. In all the above cases, deduction of the service charges from the tax base is dependent on separate statements of such charges. While it is usually preferable that such charges be separately stated on the invoice to the customer, this is not essential. It is essential that there be a separate statement of such charges on record somewhere, either on the statement to the customer, or in the records of the vendor. (See Scott Paper Co. v. Johnson, 156 Me. 19)

b. Transportation Charges. Transportation charges are not included in the taxable "sale price" if:

i. The transportation in question is from the retailer's place of business, or some other point from which shipment is made, directly to the customer;

ii. Transportation is by means of common carrier, contract carrier or the United States mails; and

iii. The transportation charges are separately stated. (As noted above under 5, a, i, such charges need not be separately stated on the invoice, provided the separate statement is otherwise available in the records of the vendor or vendee.)

All of the above three conditions must be met if transportation charges are to be deductible. For example, charges for transportation from the point of manufacture to the vendor are not deductible; nor are charges for transportation from the vendor to the vendee, if the vendor delivers in his own equipment rather than by common or contract carrier or mail.

(Further information about transportation charges can be obtained from Instruction Bulletin No. 30.)

c. Service Charges in Lieu of Tips. The definition of "sale price" does not include an amount charged or collected in lieu of gratuity or tip, as a specifically stated service charge, when the amount so charged is to be disbursed by a hotel, motel, restaurant or other eating establishment to its employees as wages.

6. Return of Merchandise. The definition of "sale price" says that " 'Sale price' shall not include allowances in cash or by credit made upon the return of merchandise pursuant to warranty, or the price of property returned by customers when the full price thereof is refunded either in cash or by credit."

a. Returns Pursuant to Warranty. When an adjustment of price is made by a retailer on the return of defective merchandise which has been warranted, the adjustment, or allowance, is deductible on a subsequent sales tax return of the retailer if the original sales was taxable and was so reported by the retailer.

For example, a tire sold with a 30-month warranty, adjustment being based upon period of use. Assuming the tire was sold for $30.00 with an allowance of $1.00 per month for the period by which the tire fails to meet the warranty. If the tire is returned for failure after 24 months, the allowance would be $6.00. The purchaser would be entitled to $6.00 plus sales tax on this amount; and the retailer would deduct $6.00 on his next sales tax return. Usually such adjustments are made as the result of a written warranty, as in the case of an automobile tire; but it is not necessary that the warranty be in writing, since there is a general unwritten warranty that goods are not defective for the purpose for which they are intended.

While an adjustment of sales tax liability may be made for allowance by warranty, whether written or not, an adjustment cannot be made where the merchandise is returned as unsatisfactory, not because of written warranty or because it is defective and so fails to meet an unwritten warranty; but because the purchaser finds it is not suited to his purpose. In the latter case, unless the full purchase price is refunded (See below, under b), no adjustment of sales tax can be made.

For example, a customer purchases a snow blower. After using it for a short time he finds it is not powerful enough to meet his particular needs. There is neither failure to meet a written warranty nor any defect in the machine. He returns it to the dealer and is allowed 85% of the original purchase price. There is no adjustment permitted so far as sales tax is concerned.

b. Return of Merchandise and Refund of Full Purchase Price. Where merchandise is returned by the customer and the full purchase price is refunded, either in cash or by credit toward other purchases, the retailer may deduct the original purchase price of the item on a subsequent sales tax return, if the original transaction was taxable and was so reported. In such a case, applicable sales tax would also be refunded to the customer.

If, in connection with such returned merchandise, the retailer makes a standard service charge, the transaction will nevertheless be considered as a refund of the full purchase price if the service charge is separately shown and so identified on the invoice to the customer or in the records of the retailer.

For example, a retailer makes a standard service charge of $1.00 in all cases where merchandise is returned by the customer for refund. In his invoice or credit memo to the customer he shows "purchase price refunded $20.00, less service charge $1.00 - net $19.00" he may treat this as a refund of the full purchase price.

Note, however, that except for deduction of a standard service charge, the refund must be of the entire purchase price. For example, if an item has been used by the customer and the retailer therefore refunds less than the full purchase price (the transaction not involving an express or implied warranty), no adjustment of sales tax can be made.

7. Rulings on Specific Transactions. The contents of this bulletin are intended to aid in a general understanding of the particular aspects of the Sales and Use Tax Law which it covers and the bulletin is intended only as a general guide. A ruling should be obtained from the Bureau of Taxation with a regard to any transaction about which there may be question. Requests for rulings should be in writing, should contain full information as to the transaction in question, and should be directed to the:

Sales Tax Division
Bureau of Taxation
State Office Building
Augusta, Maine 04333

(Published Under Appropriation 01037-1015)

A. THE PERSONAL INCOME TAX IN GENERAL

1. Personal Income Tax Theory

The personal income tax is imposed on individual incomes of residents as well as nonresidents whose income, whole or in part, is derived in the state. The levy can tax income in the form of wages, interest, dividends from stocks and bonds, the sale of the same, etc.. Some states, following the federal formula of deductions and exemptions, procure a percentage of the individual's federal tax liability.

2. The Personal Income Tax in Maine

The new rate structure of the personal income tax in Maine, passed by the 107th Legislature and taking effect January 1, 1977,[1/] is as follows:

If the taxable income is:	The tax is:
not over $2000	1% of taxable income
$2000 but not over $4000	$20 plus 2% of excess over $2000
$4000 but not over $6000	$60 plus 4% of excess over $4000
$6000 but not over $8000	$140 plus 6% of excess over $6000
$8000 but not over $10,000	$260 plus 7% of excess over $8000
$10,000 but not over $15,000	$400 plus 8% of excess over $10,000
$15,000 but not over $25,000	$800 plus 9% of excess over $15,000
$25,000 or more	$1700 plus 10% of excess over $25,000

When this rate structure has been fully implemented, it is estimated the personal income tax will be approximately 10% of Maine total state-local tax structure.[2/]

1/ To decrease the impact of the new rate structure, an interim rate structure for 1976 was instituted which approximates the half-way point between the old and new rates.

2/ The current state-local tax structure (1975-76) is as follows:

1975-76 STATE - LOCAL TAX STRUCTURE*

Tax	Revenue		Approximate Percentage of Total Tax Revenue
Property:			
State Property (includes Uniform Property Tax - $120 million)	$ 132,139,539.15		19 %
Municipal Property	100,935,944.00	**	14 %
Municipal Auto Excise Tax	22,507,798.00	**	3 %
Municipal Inventory & Livestock	12,595,344.00	**	2 %
Spruce Budworm Tax	2,837,259.00		.2 %
Total Property Taxes	$ 271,015,884.15		39 %
State Sales	151,335,808.52		22 %
Personal Income 1/	52,266,430.03		7.3 %
Unemployment Compensation Tax	35,537,656.00		5 %
Corporate Income	32,642,106.92		5 %
Highway Fund	52,283,138.51		7.3 %
Alcoholic Beverage Operations	22,933,750.01		3 %
Motor Vehicle License & Registration	22,128,483.95		3 %
Cigarette	23,935,432.43		3.4 %
Others ***	37,369,389.26		5 %
Total:	$ 701,448,079.73		100 %

* All figures from State Bureau of Taxation - Property Tax Division and State Controller's Fiscal 1975-76 computer data.

1975 figures used as 1976 data unavailable.

*** Other taxes include:

Inheritance	$ 7,361,635.75
Milk taxes	509,528.98
Corporation Regulatory Taxes	516,532.19
Public Utility Taxes	10,282,860.86
Insurance Co. Taxes	8,369,557.92
Bank Taxes	211,470.16
Game License Taxes	91,893.01
Harness Racing Pari-Mutual	1,300,890.84
Service Oriented Licenses	2,053,916.07
Fishing & Game Licenses	4,649,401.75
Mis. License Fees	2,021,701.73
TOTAL:	$ 37,369,389.26

1/ Due to an income tax increase by the 107th Legislature, in 1977 the personal income tax will be raising approximately$18 million more than in 1975. If this increase is added to the tax mix, then the relationship of our three broad based taxes is changed accordingly:

Total property taxes	38%
Personal income tax	10%
Sales tax	21%

Table of Rates

Alabama

1st	$1,000	1½%
Next	2,000	3%
Next	2,000	4½%
Over	5,000	5%

Alaska [1]

1st	$ 4,000	3%
Next	4,000	$ 120 plus 3.5%
Next	4,000	$ 260 plus 4%
Next	4,000	$ 420 plus 5%
Next	4,000	$ 620 plus 5.5%
Next	4,000	$ 840 plus 6%
Next	4,000	$ 1,080 plus 7%
Next	4,000	$ 1,360 plus 7.5%
Next	4,000	$ 1,660 plus 8%
Next	4,000	$ 1,980 plus 8.5%
Next	4,000	$ 2,320 plus 9%
Next	8,000	$ 2,680 plus 9.5%
Next	12,000	$ 3,440 plus 10%
Next	12,000	$ 4,640 plus 10.5%
Next	12,000	$ 5,900 plus 11%
Next	12,000	$ 7,220 plus 11.5%
Next	20,000	$ 8,600 plus 12%
Next	20,000	$11,000 plus 12.5%
Next	20,000	$13,500 plus 13%
Next	20,000	$16,100 plus 13.5%
Next	20,000	$18,800 plus 14%

Alaska—Cont'd

Next	$100,000	$21,600 plus 14%
Next	100,000	$35,600 plus 14.5%
Over	400,000	$50,100 plus 14.5%

Arizona [2]

1st	$1,000	2%
2nd	1,000	3%
3rd	1,000	4%
4th	1,000	5%
5th	1,000	6%
6th	1,000	7%
Over	6,000	8%

Arkansas

1st	$ 2,999	1%
Next	3,000	2.5%
Next	3,000	3.5%
Next	6,000	4.5%
Next	10,000	6%
Over	25,000	7%

California [1a, 2]

1st	$ 2,000	1%
Next	1,500	2%
Next	1,500	3%
Next	1,500	4%
Next	1,500	5%
Next	1,500	6%
Next	1,500	7%
Next	1,500	8%
Next	1,500	9%
Next	1,500	10%
Over	15,500	11%

Colorado [3]

1st	$ 1,000	3%
2nd	1,000	3.5%
3rd	1,000	4%
4th	1,000	4.5%
5th	1,000	5%
6th	1,000	5.5%
7th	1,000	6%
8th	1,000	6.5%
9th	1,000	7%

Colorado—Cont'd

10th	$1,000	7.5%
Over	10,000	8%
Surtax on intangibles income over $5,000		2%

Delaware

1st	$ 1,000	1.6%
Next	1,000	2.2%
Next	1,000	3.3%
Next	1,000	4.4%
Next	1,000	5.5%
Next	1,000	6.6%
Next	2,000	7.7%
Next	12,000	8.8%
Next	5,000	9.3%
Next	5,000	9.9%
Next	10,000	12.1%
Next	10,000	13.2%
Next	25,000	15.4%
Next	25,000	16.5%
Over	100,000	19.8%

District of Columbia [4]

1st	$ 1,000	2%
Next	1,000	3%
Next	1,000	4%
Next	1,000	5%
Next	1,000	6%
Next	5,000	7%
Next	3,000	8%
Next	4,000	9%
Next	8,000	10%
Over	25,000	11%

Georgia [5]

1st	$ 1,000	1%
Next	2,000	2%
Next	2,000	3%
Next	2,000	4%
Next	3,000	5%
Over	10,000	6%

Hawaii [6]

1st	$ 500	2.25%
Next	500	3.25%
Next	500	4.5%
Next	500	5%
Next	1,000	6.5%

[1] Alaska: Rates shown are for married persons filing jointly and surviving spouses. Single persons and fiduciaries pay at rates ranging from 3% on taxable income not over $2,000 to $25,500 plus 14.5% on taxable income over $200,000. Heads of households pay at rates ranging from 3% on taxable income not over $2,000 to $37,910 plus 14.5% on taxable income over $300,000.

[1a] California: Rates shown are for residents and nonresidents except heads of households. Tax rates for heads of households range from 1% of taxable income not over $4,000 to 11% of taxable income over $18,000. An additional tax is imposed on taxable items of tax preference.

[2] Community property state in which, in general, one-half of the community income is taxable to each spouse.

[3] Colorado: A tax reduction credit applies to reduce the effective rate of tax ½ of 1% in each bracket up to $9,000.

[4] District of Columbia: The tax on unincorporated business is 9%. For tax years beginning on or after January 1, 1976, but before January 1, 1978, unincorporated businesses are subject to a 10% surtax. Minimum tax, $25.

[5] Georgia: Rates shown are for married persons filing jointly and heads of households. Single persons pay at rates ranging from 1% on taxable net income not over $750 to 6% on taxable net income over $7,000. Married persons filing separately pay at rates ranging from 1% on taxable net income not over $500 to 6% on taxable net income over $5,000.

[6] Hawaii: Alternative tax: deduct 50% of capital gains but pay additional tax of 4% of such gains. Special tax rates are provided for heads of households ranging from 2.25% on taxable income not over $500 to 11% on taxable income in excess of $60,000.

Hawaii—Cont'd

Next	$2,000	7.5%
Next	5,000	8.5%
Next	4,000	9.5%
Next	6,000	10%
Next	10,000	10.5%
Over	30,000	11%

Idaho [2, 7]

1st	$1,000	2%
2nd	1,000	4%
3rd	1,000	4.5%
4th	1,000	5.5%
5th	1,000	6.5%
Over	5,000	7.5%

Illinois

2½% of taxable net income.

Indiana [8]

2% of adjusted gross income.

Iowa

1st	$1,000	0.5%
2nd	$1,000	1.25%
3rd	$1,000	2.75%
4th	$1,000	3.5%
5th, 6th and 7th	$1,000	5%
8th and 9th	$1,000	6%
10th through 15th	$1,000	7%
16th through 20th	$1,000	8%
21st through 25th	$1,000	9%
26th through 30th	$1,000	10%
31st through 40th	$1,000	11%
41st through 75th	$1,000	12%
Over	$75,000	13%

Kansas

1st	$2,000	2%
Next	1,000	3½%
Next	2,000	4%
Next	2,000	5%
Over	7,000	6½%

Kentucky

1st	$3,000	2%
Next	1,000	3%
Next	1,000	4%
Next	3,000	5%
Over	8,000	6%

Louisiana [2]

1st	$10,000	2%
Next	40,000	4%
Over	50,000	6%

Maine [13]

1st	$ 2,000	1%
Next	2,000	2%
Next	1,000	3%
Next	1,000	3.5%
Next	2,000	4.5%
Next	2,000	5%
Next	5,000	6%
Next	10,000	6.5%
Next	25,000	7.5%
Over	50,000	8%

Maryland

1st	$1,000	2%
2nd	1,000	3%
3rd	1,000	4%
Over	3,000	5%

Massachusetts [11]

Interest, dividends, net capital gains	10%
Earned income, annuities	5%

Michigan [9]

4.6% of adjusted gross income.

Minnesota

1st	$ 500	1.6%
2nd	500	2.2%
2nd	1,000	3.5%
3rd	1,000	5.8%
4th	1,000	7.3%
5th	1,000	8.8%
Next	2,000	10.2%
Next	2,000	11.5%
Next	3,500	12.8%
Next	7,500	14%
Over	20,000	15%

Mississippi

1st	$5,000	3%
Over	5,000	4%

Missouri

1st	$1,000	1½%
2nd	1,000	$15 plus 2%
3rd	1,000	35 plus 2½%
4th	1,000	60 plus 3%
5th	1,000	90 plus 3½%
6th	1,000	125 plus 4%
7th	1,000	165 plus 4½%
8th	1,000	210 plus 5%
9th	1,000	260 plus 5½%
Over	9,000	315 plus 6%

Montana [14]

1st	$ 1,000	2%
2nd	1,000	3%
Next	2,000	4%
Next	2,000	5%
Next	2,000	6%
Next	2,000	7%
Next	4,000	8%
Next	6,000	9%
Next	15,000	10%
Over	35,000	11%

Nebraska

17% of adjusted federal income tax liability.

New Hampshire [15]

4¼%

New Jersey [10]

1st	$20,000	2%
Over	20,000	2.5%
N. Y. commuters' tax		
1st	$1,000	2%
Next	2,000	3%
Next	2,000	4%
Next	2,000	5%
Next	2,000	6%
Next	2,000	7%
Next	2,000	8%
Next	2,000	9%
Next	2,000	10%
Next	2,000	11%
Next	2,000	12%
Next	2,000	13%
Next	2,000	14%
Over	25,000	15%
Pa. commuters' tax		

[2] See footnote 2 on preceding page.

[7] Idaho: Each person (joint returns deemed one person) filing return pays additional $10.

[8] Indiana: Counties may impose an adjusted gross income tax on residents at ½%, ¾% or 1% and at ¼% on nonresidents.

[9] Michigan: The rate is decreased to 4.4% effective July 1, 1977. Effective January 1, 1976, persons with business activity allocated or apportioned to Michigan are also subject to a single business tax of 2.35% on an adjusted tax base. A personal income tax credit is allowed for any single business tax paid the same year.

[10] New Jersey: The personal income tax applies to tax years ending on or after July 1, 1976, and expires June 30, 1978. Taxpayers pay only the larger of the personal income tax or the N.Y.—N. J. or Pa.—N. J. commuters' tax. The commuter taxes will cease to be imposed after the assessment for any taxable year ending December 31, 1980. A 6% tax is imposed on N. Y. commuters who are subject to the federal minimum income tax on "tax preference items". For tax years beginning on or before December 31, 1976, a 2.5% surcharge is imposed on regular income taxes and on the tax on "tax preference items".

[11] Massachusetts: An additional 7.5% tax is imposed.

[13] Maine: Beginning January 1, 1977, rates range from 1% on the first $2,000 to 10% of taxable income over $25,000.

[14] Montana: A 10% surtax is imposed.

[15] New Hampshire: Limited to interest and dividends.

2% of specified classes of taxable income.

New Mexico [2, 16]

1st	$ 500	0.9%
Next	500	$ 4.50 plus 1.1%
Next	$ 500	$ 10 plus 1.3%
Next	$ 500	$16.50 plus 1.5%
Next	$ 1,000	$ 24 plus 1.6%
Next	$ 1,000	$ 40 plus 1.9%
Next	$ 1,000	$ 59 plus 2.3%
Next	$ 1,000	$ 82 plus 2.4%
Next	$ 1,000	$ 106 plus 3%
Next	$ 1,000	$ 136 plus 3.3%
Next	$ 2,000	$ 169 plus 3.6%
Next	$ 2,000	$ 241 plus 4.3%
Next	$ 8,000	$ 327 plus 6.1%
Next	$ 30,000	$ 815 plus 8%
Next	$ 50,000	$3,215 plus 8.5%
Over	$100,000	$7,465 plus 9%

New York [17]

1st	$1,000	2%
Next	2,000	3%
Next	2,000	4%
Next	2,000	5%
Next	2,000	6%
Next	2,000	7%
Next	2,000	8%
Next	2,000	9%

New York—Cont'd

Next	$ 2,000	10%
Next	2,000	11%
Next	2,000	12%
Next	2,000	13%
Next	2,000	14%
Over	25,000	15%

North Carolina

1st	$ 2,000	3%
2nd	2,000	4%
3rd	2,000	5%
Next	4,000	6%
Over	10,000	7%

North Dakota [18]

1st	$1,000	1%
Next	2,000	2%
Next	2,000	3%
Next	1,000	5%
Next	2,000	7.5%
Over	8,000	10%

Ohio

1st	$5,000	½%
2nd	5,000	1%
3rd	5,000	2%
4th	5,000	2½%
Next	20,000	3%
Over	40,000	3½%

Oklahoma [19]

1st	$2,000	½%
Next	3,000	1%
Next	2,500	2%
Next	2,500	3%
Next	2,500	4%
Next	2,500	5%
Remainder		6%

Oregon

1st	$ 500	4%
2nd	500	5%
Next	1,000	6%
Next	1,000	7%

Oregon—Cont'd

Next	$1,000	8%
Next	1,000	9%
Over	5,000	10%

Pennsylvania

2% of specified classes taxable income.

Rhode Island

17% of modified federal income tax liability.

South Carolina

1st	$ 2,000	2%
2nd	2,000	3%
3rd	2,000	4%
4th	2,000	5%
5th	2,000	6%
Over	10,000	7%

Tennessee [20]

.... 6%

Utah [21]

1st	$750	2¼%
Next	750	$ 17 plus 3¼%
Next	750	$ 41 plus 4¼%
Next	750	$ 73 plus 5¼%
Next	750	$113 plus 6¼%
Next	750	$159 plus 7¼%
Over	4,500	$214 plus 7¾%

Vermont [22]

25% of federal income tax.

Virginia

1st	$3,000	2%
Next	2,000	3%
Next	7,000	5%
Over	12,000	5¾%

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[16] New Mexico: Taxpayers filing jointly and heads of households pay at rates ranging from 0.9% on net income not over $1,000 to $15,436 plus 9% of the excess of net income over $200,000. Special rates are provided for married persons filing separately (see ¶ 15-666).

[17] New York: Unincorporated businesses have a 5½% permanent rate, but if tax is $100 or less, tax credit is the entire tax; if tax is over $100 but less than $200, tax credit is the difference between $200 and the tax; if tax is $200 or more, no credit. A 6% tax is imposed on taxpayers subject to the federal minimum income tax on "tax preference items". A 2.5% surtax is imposed on regular income taxes and on the tax on "tax preference items", effective for tax years beginning on or before March 31, 1977.

[18] North Dakota: An additional 1% tax is imposed on net incomes over $2,000 derived from a business, trade or profession other than as an employee.

[19] Oklahoma: Rates shown are for married persons filing jointly and a surviving spouse. Single persons, married persons filing separately and estates and trusts pay at rates ranging from ½% on the first $1,000 of taxable income to 6% on taxable income over $7,500. Heads of households pay at rates ranging from ½% on the first $1,500 of taxable income to 6% on taxable income over $11,250.

[20] Tennessee: Individuals are taxable only on interest and dividends: tax on dividends from corporations 75% of whose property is taxable in Tennessee is 4%.

[21] Utah: Taxpayers filing jointly pay at rates ranging from 2.75% of taxable income not over $1,500 to $356 plus 7.75% on taxable income over $7,500. Married taxpayers filing separately pay at rates ranging from 2.75% on taxable income not over $750 to $178 plus 7.75% on taxable income over $3,750.

[22] Vermont: A 9% surcharge is imposed.

West Virginia [58]

1st	$ 2,000		2.1%
2nd	2,000	$ 42	plus 2.3%
3rd	2,000	$ 88	plus 2.8%
4th	2,000	$ 144	plus 3.2%
5th	2,000	$ 208	plus 3.5%
6th	2,000	$ 278	plus 4.0%
7th	2,000	$ 358	plus 4.6%
8th	2,000	$ 450	plus 4.9%
9th	2,000	$ 548	plus 5.3%
10th	2,000	$ 654	plus 5.4%
11th	2,000	$ 762	plus 6.0%
Next	4,000	$ 882	plus 6.1%

West Virginia—Cont'd

Next	$6,000	$ 1,126	plus 6.5%
Next	6,000	$ 1,516	plus 6.8%
Next	6,000	$ 1,924	plus 7.2%
Next	6,000	$ 2,356	plus 7.5%
Next	10,000	$ 2,806	plus 7.9%
Next	10,000	$ 3,596	plus 8.2%
Next	10,000	$ 4,416	plus 8.6%
Next	10,000	$ 5,276	plus 8.8%
Next	10,000	$ 6,156	plus 9.1%
Next	50,000	$ 7,066	plus 9.3%

West Virginia—Cont'd

Next	$50,000	$11,716	plus 9.5%
Over	200,000	$16,466	plus 9.6%

Wisconsin

1st	$ 1,000	3.1%
2nd	1,000	3.4%
3rd	1,000	3.6%
4th	1,000	4.8%
5th	1,000	5.4%
6th	1,000	5.9%
7th	1,000	6.5%
8th	1,000	7.6%
9th	1,000	8.2%
10th	1,000	8.8%
11th	1,000	9.3%
12th	1,000	9.9%
13th	1,000	10.5%
14th	1,000	11.1%
Over	14,000	11.4%

Cities (Over 150,000)

Akron	1.5%
Baltimore [56]	
Birmingham	1%
Cincinnati	2%
Cleveland	1%
Columbus	1½%
Dayton	1.75%
Detroit	
residents	2%
nonresidents	½ of 1%
Flint	
residents	1%
nonresidents	½ of 1%
Grand Rapids	
residents	1%
nonresidents	½ of 1%
Kansas City, Mo.	1%
Louisville	
residents	2.2%
nonresidents	1.45%
Montgomery	1%
Newark [59]	1%
New York [60]	from 0.9% to 4.3%
Philadelphia	4 5/16%
Pittsburgh (City)	1%
Pittsburgh (School District)	1%
Portland, Ore. [61]	0.5%
St. Louis	1%
San Francisco [62]	1.1%
Toledo	1½%
Youngstown	1½%

[58] West Virginia: Rates shown are for taxpayers filing separate returns. Taxpayers filing jointly or filing a return as a surviving spouse pay at rates ranging from 2.1% of taxable income not over $4,000 to $32,932 plus 9.6% of the excess of taxable income over $400,000.

[56] Baltimore: Baltimore City must levy an income tax on residents at a rate not less than 20% nor more than 50% of the state income tax liability. The tax rate for 1976 is 50% of state income tax liability.

[59] Newark: A 1% payroll tax is imposed on certain employers for 1971 through 1976.

[60] New York City: Residents only and only for 1976 and 1977. Rates for 1971 through 1975 ranged from 0.7% to 3.5%. After 1977 residents are taxed from 0.4% to 2%. Nonresidents, ¼ of 1% (45/100 of 1% for 1971 through 1977) of wages; ⅜ of 1% (65/100 of 1% for 1971 through 1977) of net earnings from self-employment. Unincorporated business, 4%.

[61] Portland, Ore.: The tax is imposed on employers paying wages for services performed and is levied in Washington, Clackamas and Multnomah Counties. Effective July 1, 1977, and prior to 1976, the rate is 0.4%. A 2.3% business license tax on net income is also imposed in Portland.

[62] San Francisco: A 1.1% payroll expense tax is imposed on employers in the city and county of San Francisco. Prior to January 1, 1975, and after December 31, 1976, the tax rate is 1%.

4. The personal income tax yield in the New England states.

State	Yield
Connecticut	[has no income tax]
Maine (1976)	$54,266,430
Massachusetts (1974)	$971,030,000
New Hampshire	$8,344,000
Rhode Island	$73,898,000
Vermont	$52,662,000

B. THE PERSONAL INCOME TAX IN MAINE

1. Administration and rates

The following analyses is taken from the Commerce Clearing House State Tax Guide (second edition).

¶ 15-485 MAINE

[¶ 15-486] **Taxpayers and Rates.**—A tax is imposed on the entire taxable income of every resident (Ch. 805, Sec. 5121) and on the taxable income of nonresident individuals derived from Maine (Ch. 807, Sec. 5140). Estates and trusts are subject to tax on their taxable income (Ch. 809, Sec. 5160). The rate of tax is as follows (Ch. 661, Laws 1976, 1st Spec. Sess.; Ch. 803, Sec. 5111):

(Until January 1, 1976)

Taxable Income Over	Not Over	Rates
......	$ 2,000	1%
$ 2,000	5,000	$ 20 plus 2% on excess over $ 2,000
5,000	10,000	80 plus 3% on excess over 5,000
10,000	25,000	230 plus 4% on excess over 10,000
25,000	50,000	830 plus 5% on excess over 25,000
50,000	....	2,080 plus 6% on excess over 50,000

(For tax years in the period on or after January 1, 1976, to on or before December 31, 1976)

Taxable Income Over	Not Over	Rates
......	$ 2,000	1%
$ 2,000	4,000	$ 20 plus 2% of excess over $ 2,000
4,000	5,000	60 plus 3% of excess over 4,000
5,000	6,000	90 plus 3.5% of excess over 5,000
6,000	8,000	125 plus 4.5% of excess over 6,000
8,000	10,000	215 plus 5% of excess over 8,000
10,000	15,000	315 plus 6% of excess over 10,000
15,000	25,000	615 plus 6.5% of excess over 15,000
25,000	50,000	1,265 plus 7.5% of excess over 25,000
50,000	......	3,140 plus 8% of excess over 50,000

(For tax years or portions thereof on or after January 1, 1977)

Taxable Income Over	Not Over	Rates
......	$ 2,000	1%
$ 2,000	4,000	$ 20 plus 2% of excess over $ 2,000
4,000	6,000	60 plus 4% of excess over 4,000
6,000	8,000	140 plus 6% of excess over 6,000
8,000	10,000	260 plus 7% of excess over 8,000
10,000	15,000	400 plus 8% of excess over 10,000
15,000	25,000	800 plus 9% of excess over 15,000
25,000	......	1,700 plus 10% of excess over 25,000

Taxpayers may elect to compute their tax according to tables prepared by the State Tax Assessor (Ch. 765, Laws 1976, 1st Spec. Sess.; Ch. 803, Sec. 5111-A). In the case of a joint return of a husband and wife, or a return of a surviving spouse, the tax imposed is twice the tax that would be imposed if the taxable income were cut in half (Ch. 803, Sec. 5113).

[¶ 15-487] **Income, Net and Gross.**—The entire taxable income of resident individuals is federal adjusted gross income, less deductions and personal exemptions, adjusted as follows (Ch. 805, Secs. 5121, 5122):

Add (1) interest or dividends on obligations of any state or political subdivision other than Maine, and (2) interest or dividends on federal obligations exempt from federal income tax but not from state taxes.

Subtract interest or dividends on federal obligations to the extent includible in federal gross income but exempt from state taxes under federal law (the amount subtracted must be reduced by any interest on indebtedness incurred to carry the obligations and by expenses incurred in the production of interest or dividend

income to the extent such expenses, including amortizable bond premiums, are deductible in determining federal adjusted gross income).

The taxable income of nonresident individuals is that part of the taxpayer's federal adjusted gross income derived from Maine sources, less deductions and personal exemptions (Ch. 807, Sec. 5140). Adjusted gross income of a nonresident from Maine sources is the sum of (Ch. 807, Sec. 5142): (1) the net amount of items of income, gain, loss and deduction entering into the taxpayer's federal adjusted gross income derived from or connected with Maine sources, and (2) the portion of the adjustments provided above for resident individuals that relate to income from Maine sources.

The taxable income of a resident estate or trust is federal taxable income modified by its share of the fiduciary adjustment, i.e., the adjustment apportioning additions and subtractions to federal taxable income between the estate or trust and the beneficiaries (Ch. 811, Secs. 5163, 5164). Taxable income of a nonresident estate or trust is determined from income, gain, loss and deduction derived from or connected with sources in Maine. The amount of its federal exemption is deducted (Ch. 813, Sec. 5175).

References to federal laws are to the laws as they were on December 31, 1975 (Ch. 765, Laws 1976, 1st Spec. Sess.; Ch. 17, Laws 1975; Ch. 788, Laws 1974, 1st Spec. Sess.; Ch. 801, Sec. 5102).

[¶ 15-488] Deductions.—The standard deduction available to resident and nonresident individuals, husbands and wives filing jointly or married persons filing separately is as defined in Sec. 141 of the Internal Revenue Code except that the percentage standard deduction is based on adjusted gross income (from Maine sources for nonresidents) and may not be greater than 16% of Maine adjusted gross income; maximum, $2,800 for married couples filing jointly; $1,400 for married persons filing separately; or $2,400 for single persons (Ch. 660, Laws 1976, 1st Spec. Sess.; Ch. 805, Sec. 5124, Ch. 807, Sec. 5143). Residents who itemized deductions for federal purposes may elect to itemize deductions in determining Maine taxable income (Ch. 805, Sec. 5125). Nonresidents who itemized deductions for federal purposes may itemize deductions connected with income derived from Maine sources in determining Maine taxable income (Ch. 807, Sec. 5144).

[¶ 15-489] Credits and Exemptions.—Residents and nonresidents are allowed a $1,000 exemption for each exemption to which they are entitled for the taxable year for federal income tax purposes (Ch. 805, Sec. 5126, Ch. 807, Sec. 5145). Resident individuals and estates or trusts are allowed a credit against the tax for income taxes imposed in any other state or local government or by the District of Columbia (Ch. 805, Sec. 5127, Ch. 811, Sec. 5165). Resident and nonresident beneficiaries of a trust whose adjusted gross income includes all or part of a trust accumulation distribution are allowed a credit for all or a proportionate part of any tax paid by the trust that would not have been payable had the trust made distribution to its beneficiaries as provided in Sec. 666 of the Internal Revenue Code (Ch. 811, Sec. 5166, Ch. 813, Sec. 5177).

[¶ 15-490] Allocation and Apportionment.—See ¶ 10-491.

[¶ 15-491] Returns.—Individuals, estates and trusts must file returns with the State Tax Assessor on or before the due date for filing the federal income tax return (Ch. 823, Sec. 5227). Partnerships having a resident partner or having income derived from Maine sources may be required by the Assessor to file a return. Partnership returns are due on or before the 15th day of the fourth month following the close of the tax year (Ch. 825, Sec. 5241). Declarations of estimated tax are required of resident and nonresident individuals whose adjusted gross income, other than wages subject to withholding, can reasonably be expected to exceed $2,000 plus the sum of the taxpayer's personal exemptions (Ch. 823, Sec. 5228). Declarations of individuals other than farmers are due on or before April 15 or the 15th days of June, September or January depending upon when requirements for filing the declaration are first met. Farmers' declarations may be filed at any time on or before January 15 of the succeeding taxable year. If estimated tax is $40 or less for the taxable year, the declaration may be filed at any time on or before January 15 of the succeeding taxable year (Ch. 823, Sec. 5229).

[¶ 15-492] **Assessment.**—See ¶ 10-493.

[¶ 15-493] **Payment.**—The tax is paid to the Assessor with the return (Ch. 823, Sec. 5227). Estimated taxes are paid in four equal installments, the first due at the time the declaration of estimated tax is filed and the second, third and fourth due on or before the 15th days of the 6th, 9th and 13th months of the income year. Fewer installments are provided if the declaration is filed later in the year. Farmers filing declarations of estimated tax after September 15 of the tax year and on or before January 15 of the succeeding tax year pay the estimated tax in full when filing the declaration (Ch. 823, Sec. 5230).

[¶ 15-494] **Information and Withholding at the Source.**—See ¶ 10-495. The Assessor may prescribe regulations requiring information returns to be filed on or before February 28 by any person making payment or crediting, in any calendar year, $600 or more ($10 or more in the case of interest and dividends) to any person subject to the tax (Ch. 825, Sec. 5242).

Source.—References are to the Maine Revised Statutes of 1964 as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 10-000.

2. Analyses

a. Economic effects

A progressive income tax schedule, with personal deductions and exemptions, will produce an increase in revenues greater than the increase in the total income in a growing economy.

In an economy with steady average inflation, the relative increase in income tax burden caused by this elasticity will be greatest on the lower income brackets.

Income taxes reduce the rewards for work but it is uncertain, on balance, whether they increase or decrease the willingness to work.3/

3/ Goode, The Individual Income Tax 57 (1976).

Some argue that a heavy reliance by the state on personal income taxes discourages executives and small business entrepreneurs from moving to or starting up in Maine. Others argue that the quality of life a state can provide (maintained roads, clean environment, a good school system, etc.) is just as important (or more so) to businessmen. And such amentities necessitate tax revenues.

b. Yield

(1) The Maine personal income tax in 1975-76 yielded $52,266,430.03, which represented 7.3% of the total state and local tax revenues. In 1977, when the new rate schedule takes effect, revenues are expected to increase by approximately $18 million.

(2) Elasticity. The personal income tax is quite elastic - that is its revenues increase if the economy expands or inflation grows. For example, despite the fact that Maine has been in a near recession for some years, income tax revenues have increased, even when the rate of inflation is taken into account. And these increases resulted even though the rate schedules remained constant:

Calendar Year	Personal Income Tax Revenues	Percentage Rate Of Inflation[1]	Revenues Adjusted For Inflation	Percentage Increase In Personal Income Tax Revenues (Inflation Adjusted)
1970	$24,452,210	6%	$22,985,078	-----
1971	$27,075,994	4%	$25,992,283	11%
1972	$30,019,712	3%	$29,119,121	10%
1973	$34,328,707	5%	$32,612,272	10%
1974	$41,086,449	9%	$37,388,669	12%
1975	$43,787,431	8%	$40,284,437	7%

4/ Derived from seasonally unadjusted Consumer Price Index, Economic Indicators, Council of Economic Advisors, August issues-1970, 1971, 1972, 1973, 1974, 1975, page 26.

c. Incidence

The personal income tax is a direct tax, that is its burden is borne by those directly taxed and cannot be passed on. It is borne by income earners in proportion to their income.

d. Equity

Our State-local tax structure attempts, in the aggregate, to fairly tax each citizen's ability to pay. The measures of this ability are a person's wealth, consumption and income and no single tax can meet these measures alone. Property taxes, for example, do not completely reflect a person's accumulated wealth (e.g., stocks and bonds). Our present consumption taxes do not distinguish between the different buyers of necessities.

But of all the broad based taxes, the personal income tax is the most responsive to each citizen's taxpaying capacity.5/

The personal income tax is the only member of our tax mix that can accurately distinguish between the size of taxpaying families (through personal exemptions) and the different income levels of families (through the graduated rate). However, while the broad mechanism of the personal income tax is a generally equitable source, its accuracy is further enhanced by special rate tables (e.g., joint and single returns) and personal deductions designed to make it a more efficient revenue source. It is argued that Maine has lagged behind in the adoption of such means of increased accuracy and in Part C , Possible Areas of Reform, some solutions will be suggested.

5/ Good, Richard, The Individual Income Tax (1964):

"Income is an incomplete measure of the quantity of resources at the disposal of a person since it does not take account of wealth which also represents command over resources....

Nevertheless, wealth has a claim for consideration only as a supplementary index of ability to pay. It does not rival income as the primary index. The principal reason is that wealth, as usually defined, does not include the expectation of future income from personal effort...it takes no account of economic resources of persons who depend on earnings from personal services." at 21.

Thus, the personal income tax is not only vertically progressive-persons with higher incomes pay a greater percentage of their income than those with lower incomes, but it is also horizontally progressive-large families pay less than small families with a similar income.

e. Administrative costs

Compared to other state taxes the personal income tax is relatively inexpensive to administer. This is particularly true with regards to enforcement. Because Maine bases its tax on adjusted gross income, the same figure used for the federal income tax, the Internal Revenue Service provides great assistance in auditing state income tax returns. In general, the costs of administration are fairly constant. Thus, as revenues increase the costs as a percent of the revenue decreases.

Comments.

Maine's personal income tax is our most progressive levy. It reflects not only a person's income but also a person's number of dependents. Yet, it is not greatly utilized. Currently less then 10% of our state and local revenues come from the personal income tax. Whether or how these revenues should be increased (and other taxes decreased) are the subject of Section C, POSSIBLE AREAS OF REFORM.

C. POSSIBLE AREAS OF REFORM

Presented below are a listing of some possible areas of personal income tax reform, with a brief rationale for each suggestion. The committee does not endorse these proposals but offers them for debate.

1. The income tax should produce a greater percentage of our state-local tax revenues.

The state-local revenues are too heavily weighted toward property tax revenues (app. 40%) and too little toward personal income tax revenues (app. 10%). In order to tax each person according to his or her ability to pay, the state should have a relatively balanced tax structure. Specifically, the Advisory Commission on Intergovernmental Relations (ACIR) suggests the individual income tax should assume a 20-25% of the state's tax structure.

2. Municipalities should be able to raise money for local needs from a local income tax (and local sales tax).

"Local control" would be enhanced if citizens would devise the individual tax mix - property taxes, income taxes, sales taxes - most appropriate for their own local needs. Thus, by town officers vote - or by referendum - each town could decide which percentage of their total budget would be funded by the different local taxes - property, sales, income. Currently, towns can only turn to the already overburdened property tax. Yet, a town might be a merchant center or be populated by above average income residents and thus utilizing a local sales or income tax might be a fairer means of raising money.

The Advisory Committee on Intergovernmental Relations (ACIR) offers 7 safeguards if local income and sales taxes are to be established:6/

When Equipped with Proper Safeguards, Local Income and Sales Taxes Should be Viewed as One of Several Appropriate Means for Achieving a More Balanced Use of Property, Income and Sales Taxes.

The Commission concludes that our tradition of strong local government argues in favor of a state policy that grants wide latitude to local elected officials in the selection of appropriate revenue instruments to underwrite the expenditure requirements of their diverse constituencies.

The Commission reiterates its recommendation that calls on the states to assume gradually a larger share of the local school finance responsibility.

The Commission recommends that state governments permit general purpose local governments to diversify their revenue structures by levying either a local sales tax or a local income tax or both provided that the states take the necessary steps to insure the creation of a system of coordinated local income and sales taxes.

To achieve a coordinated system of local nonproperty taxes for general purpose local governments, the Commission recommends that states:

Safeguard 1: Uniform Tax Base

Provide a uniform local tax base which should conform to that of the state if the state imposes the levy.

6/ ACIR, Local Revenue Diversification 2-3 (1974).

Safeguard 2: State Administration

Collect and administer the local income or sales tax and designate or create a state agency to administer the local tax if the state does not impose such a levy.

Safeguard 3: Universal or Widespread Coverage

Encourage universal or widespread coverage by

(1) mandating a minimum local levy and permitting counties and those cities with populations of at least 25,000 to choose a rate above this subject to a specified maximum, or by

(2) giving first option to adopt the tax to the local government of widest jurisdictional reach with sharing provisions for municipal governments. The authority to adopt local sales and income taxes should also be extended to cities with populations of at least 25,000 if the larger unit of general government does not adopt the tax.

Safeguard 4: Origin Tax Situs

In general, use the point of sale rule for determining tax liability for local sales taxes and prohibit local use taxes on in-state purchases.

Safeguard 5: Constrained Rate Option

Permit local flexibility by specifying a range of tax rates that general purpose local governments may impose.

Safeguard 6: State Equalization

Minimize local fiscal disparities in those states characterized by a high degree of local fiscal responsibility and a fragmented local governmental structure by adopting an equalizing formula for the distribution of local non-property tax revenues among constituent units within the local taxing authority of widest jurisdictional reach and adopting new programs or using existing state programs of general support to offset fiscal disparities among local taxing authorities with the widest jurisdictional reach.

Safeguard 7: Income Tax Sharing

Specify arrangements for sharing taxes on earned income by non-residents between tax levying jurisdictions of residence and employment.

3. Make the Maine personal income tax schedule a percentage of the federal tax schedule.

If the Maine personal income tax schedule were based on a percentage of the federal brackets, the following benefits would accrue:

a. Maine would benefit from the extensive research that led to the formulation of the degree of progressivity in the federal brackets;

b. It would be relatively easy to either increase or decrease the amount of money raised in Maine by the personal income tax.

STATE INCOME TAXES—WHO PAYS MOST, LEAST

IF YOU'RE WONDERING how your State's income-tax bite compares with that in others—

- Biggest chunk of a family's income is taken by State income taxes in Delaware, Massachusetts, Minnesota, Oregon and Wisconsin.
- Heaviest taxer at all income levels is Minnesota.
- Lightest income taxes, among States which levy them, are taken by Louisiana, Maine, Michigan, Nebraska and Ohio.
- No income taxes at all are levied by nine States: Connecticut, Florida, Nevada, New Hampshire, South Dakota, Tennessee, Texas, Washington and Wyoming. New Jersey starts collecting an income tax this year.

These are the findings in a new study by the staff of the Advisory Commission on Intergovernmental Relations, an independent research organization created by Congress in 1959.

The Commission computed the amount that each State levies at different levels of income. Those State tax figures on three incomes for the latest available year, 1974, are given below.

To show how widely the bite varies—

With a $10,000 income, a family will pay more than $250 in seven high-tax States, ranging from $255 in Maryland to more than twice that in Minnesota. But a similar family would pay less than $65 in eight other States.

With a $17,500 income, a Minnesota resident would pay more than $1,000, while five States levy from $801 to $611, and six others are under $200.

With a $25,000 income, the family of four will pay $1,000 or more in eight States and the District of Columbia. But five other States levy less than $400.

In fact, two States—Minnesota and Wisconsin—take more tax out of a $10,000 income than some others do out of a $25,000 income—Michigan, Louisiana, Nebraska and Maine.

On the average, State income taxes figure out to about $150 or 1.5 per cent on an adjusted gross income of $10,000; $368 or 2.1 per cent on $17,500, and $750 or 3 per cent on $25,000.

The tax rate rises most steeply as income rises in California, Georgia, Idaho, New York, North Dakota and Oklahoma. Only in Pennsylvania is it the same for all incomes—a flat 2 per cent.

Keep in mind, though, that the amount of a State's income tax is not a measure of the total tax burden it imposes. You also pay sales, property, real-estate and other taxes and fees.

A New Nationwide Study Shows This . . .

States' personal income tax for a married couple with two children—

	At $10,000 of Annual Income	At $17,500 of Annual Income	At $25,000 of Annual Income
Alabama	$147	$ 339	$ 593
Alaska	$182	$ 369	$ 668
Arizona	$148	$ 314	$ 646
Arkansas	$163	$ 387	$ 771
California	$ 64	$ 293	$ 688
Colorado	$157	$ 382	$ 785
Delaware	$236	$ 652	$1,238
D.C.	$250	$ 579	$1,107
Georgia	$ 83	$ 319	$ 714
Hawaii	$212	$ 611	$1,133
Idaho	$138	$ 474	$ 973
Illinois	$150	$ 338	$ 525
Indiana	$150	$ 300	$ 450
Iowa	$295	$ 528	$ 884
Kansas	$126	$ 297	$ 560
Kentucky	$243	$ 444	$ 750
Louisiana	$ 48	$ 125	$ 227
Maine	$ 60	$ 160	$ 359
Maryland	$255	$ 479	$ 812
Massachusetts	$277	$ 641	$1,013
Michigan	-$ 59 *	$ 103	$ 221
Minnesota	$543	$1,016	$1,724
Mississippi	$ 38	$ 218	$ 473
Missouri	$109	$ 268	$ 567
Montana	$279	$ 499	$ 947
Nebraska	$ 35	$ 158	$ 330
New Mexico	$ 84	$ 238	$ 527
New York	$206	$ 550	$1,174
North Carolina	$258	$ 535	$1,000
North Dakota	$105	$ 338	$ 822
Ohio	$ 55	$ 188	$ 390
Oklahoma	$ 50	$ 196	$ 517
Oregon	$238	$ 633	$1,184
Pennsylvania	$200	$ 350	$ 500
Rhode Island	$119	$ 286	$ 521
South Carolina	$157	$ 420	$ 885
Utah	$148	$ 452	$ 821
Vermont	$216	$ 520	$ 946
Virginia	$175	$ 449	$ 829
West Virginia	$144	$ 276	$ 494
Wisconsin	$365	$ 801	$1,488

* Refund of other taxes by State.

Ten States—Connecticut, Florida, Nevada, New Hampshire, New Jersey, South Dakota, Tennessee, Texas, Washington and Wyoming—did not levy a general personal-income tax in 1974, the year for which taxes are shown. New Jersey enacted an income tax last year.

Note: Figures assume the following—all income is from wages and salaries earned by one spouse. At $10,000, the optional standard deduction is used. At $17,500, itemized deductions of $3,520 are used. At $25,000, deductions of $4,365 are assumed.

For States that allow a deduction for federal income taxes, deductions were used: $791 at $10,000; $1,908 at $17,500, and $3,470 at $25,000. Figures for Michigan are based only on taxes for Detroit home-owners.

Source: Advisory Commission on Intergovernmental Relations

TC94

1976

STATE OF MAINE - BUREAU OF TAXATION

INDIVIDUAL MAINE ~~ADJUSTED GROSS INC~~ 08/17/77

TAXABLE INCOME

	TAXABLE INCOME OF MAINE TAXPAYERS	TOTAL OF ALL TAX-PAYERS ALL COUNT	% of all tax-payers %	TOTAL MARRIED JOINT TAXPAYERS MJ COUNT	% %	TOTAL MARRIED-SINGLE TAX-PAYERS MS COUNT	% %	TOTAL SINGLE TAXPAYERS S COUNT	% %	TOTAL NON-RESIDENT TAXPAYERS NR COUNT	% %
I	NEGATIVE	0	0.000	0	0.000	0	0.000	0	0.000	0	0.000
N	0.00	97,913	24.424	30,831	7.690	1,681	0.419	56,187	14.016	9,214	2.298
C	0.01 - 1,999.99	56,309	14.046	20,278	5.058	1,421	0.354	30,987	7.729	3,623	0.903
O	2,000.00 - 2,999.99	27,153	6.773	11,203	2.794	652	0.162	13,568	3.384	1,730	0.431
M	3,000.00 - 3,999.99	26,096	6.509	11,947	2.980	678	0.169	11,985	2.989	1,486	0.370
E	4,000.00 - 4,999.99	24,150	6.024	12,632	3.151	574	0.143	9,659	2.409	1,285	0.320
	5,000.00 - 5,999.99	21,792	5.436	12,676	3.162	471	0.117	7,506	1.872	1,139	0.284
	6,000.00 - 6,999.99	19,784	4.935	12,632	3.151	325	0.081	5,818	1.451	1,009	0.251
R	7,000.00 - 7,999.99	18,396	4.588	12,637	3.152	184	0.045	4,621	1.152	954	0.237
A	8,000.00 - 8,999.99	17,189	4.287	12,360	3.083	155	0.038	3,760	0.937	913	0.227
N	9,000.00 - 9,999.99	15,287	3.813	11,677	2.912	87	0.021	2,692	0.671	831	0.207
G	10,000.00 - 10,999.99	13,276	3.311	10,546	2.630	70	0.017	1,952	0.486	708	0.176
E	11,000.00 - 11,999.99	10,813	2.697	8,933	2.228	52	0.012	1,323	0.330	505	0.125
	12,000.00 - 12,999.99	8,572	2.138	7,324	1.827	27	0.006	865	0.215	356	0.088
	13,000.00 - 13,999.99	6,835	1.705	5,982	1.472	32	0.007	614	0.153	287	0.071
	14,000.00 - 14,999.99	5,782	1.442	5,079	1.266	17	0.004	485	0.120	201	0.050
	15,000.00 - 15,999.99	4,718	1.176	4,143	1.033	13	0.003	380	0.094	182	0.045
	16,000.00 - 16,999.99	3,835	0.956	3,405	0.849	9	0.002	290	0.072	131	0.032
	17,000.00 - 17,999.99	3,120	0.778	2,775	0.692	3	0.000	229	0.057	113	0.028
	18,000.00 - 18,999.99	2,573	0.641	2,295	0.572	6	0.001	193	0.048	79	0.019
	19,000.00 - 19,999.99	2,129	0.531	1,910	0.476	9	0.002	149	0.037	61	0.015
	20,000.00 - 22,499.99	3,855	0.961	3,455	0.861	7	0.001	265	0.066	128	0.031
	22,500.00 - 24,999.99	2,528	0.630	2,251	0.561	5	0.001	191	0.047	81	0.020
	25,000.00 - 27,499.99	1,740	0.434	1,535	0.382	6	0.001	143	0.035	56	0.013
	27,500.00 - 29,999.99	1,161	0.289	1,014	0.252	6	0.001	96	0.023	45	0.011
	30,000.00 - 34,999.99	1,619	0.403	1,431	0.356	5	0.001	131	0.032	52	0.012
	35,000.00 - 39,999.99	1,011	0.252	892	0.222	2	0.000	72	0.017	45	0.011
	40,000.00 - 44,999.99	736	0.183	657	0.163	5	0.001	51	0.012	23	0.005

50,000.00 - 74,999.99	1,267	0.316	1,098	0.271	5	0.001	114	0.028	50	0.014
75,000.00 - 99,999.99	391	0.097	340	0.084	2	0.000	26	0.006	23	0.005
100,000.00-124,999.99	141	0.035	126	0.031	0	0.000	5	0.001	10	0.002
125,000.00-149,999.99	68	0.016	58	0.014	0	0.000	5	0.001	5	0.001
150,000.00-174,999.99	41	0.010	33	0.008	1	0.000	2	0.000	5	0.001
175,000.00-199,999.99	31	0.007	25	0.006	0	0.000	3	0.000	3	0.000
200,000.00-224,999.99	16	0.003	10	0.002	0	0.000	2	0.000	4	0.000
225,000.00-249,999.99	10	0.002	7	0.001	0	0.000	2	0.000	1	0.000
250,000.00-274,999.99	10	0.002	8	0.001	0	0.000	0	0.000	2	0.000
275,000.00-299,999.99	4	0.000	4	0.000	0	0.000	0	0.000	0	0.000
300,000.00-324,999.99	5	0.001	4	0.000	0	0.000	0	0.000	1	0.000
325,000.00-349,999.99	2	0.000	2	0.000	0	0.000	0	0.000	0	0.000
350,000.00-374,999.99	1	0.000	1	0.000	0	0.000	0	0.000	0	0.000
375,000.00-399,999.99	2	0.000	2	0.000	0	0.000	0	0.000	0	0.000
400,000.00-424,999.99	1	0.000	1	0.000	0	0.000	0	0.000	0	0.000
425,000.00-449,999.99	3	0.000	1	0.000	0	0.000	0	0.000	2	0.000
450,000.00-474,999.99	0	0.000	0	0.000	0	0.000	0	0.000	0	0.000
475,000.00-499,999.99	1	0.000	1	0.000	0	0.000	0	0.000	0	0.000
500,000.00- UP	9	0.002	3	0.000	1	0.000	2	0.000	3	0.000
TOTALS	400,874	100.000	214,578	53.527	6,512	1.624	154,418	38.520	25,366	6.327

TOTAL COUNT	400,874
RES ONLY COUNT	375,508
PART YEAR RES	9,440
NON-RES	15,743
RESIDENTS	375,691
NONRES EXEMPTS	45,730
PART RES EXEMPTS	22,433
RES EXEMPTS	974,534
TOTAL EXEMPTS	1,042,705

A. MAINE'S TAXES ON PROPERTY

Maine has numerous taxes on property, both personal property (e.g., antiques) and real property (land and buildings). This section will describe the following property taxes.

1. Local and state property taxes: Currently, there are three main property taxes.

   A. The Local property tax, which raises money for strictly local needs (e.g., fire protection);

   B. The State Uniform Property Tax, which raises General Fund dollars equal to approximately 50% of the cost of education; and

   C. The State Local and State Government Tax, which is a state tax designed to raise from the unorganized territory sufficient revenues to fund services this area receives. Because the state constitution requires all state property taxes to be levied on all property in the state, this tax must also be levied on property in the organized territory. The municipalities are allowed to keep the revenues from this tax, treating them in effect like local property tax revenues. This has led to two possible constitutional violations:

      (1) Some municipalities (about 180) do not collect the full amount of the Local and State Government Tax because they do not need it all for local services; and

      (2) The inhabitants of the unorganized territory may be taxed at a rate higher than is necessary to provide the services they receive.

   D. The Forestry District Tax, assessed on all property in the Maine Forestry District; and

   E. Tree Growth Tax, which is not a tax at all but rather a formula to revalue the forestry land according to its productivity.

The following descriptions of these taxes are taken from the Commerce Clearing House publication, State Tax Guide (2nd edition):

[¶ 20-486] Property Taxable.—All real and personal property (including mobile homes but not including intangibles) is taxable unless expressly exempt (Ch. 252, Laws 1975; Tit. 36, Secs. 502, 551, 601).

[¶ 20-487] Exemptions.—The following property is exempt from taxation:

(1) property of the United States (to the extent prescribed by federal law), the state and municipalities including certain municipal reservoir property, airports and structures and sewage disposal property (Tit. 36, Sec. 651).

(2) property of nonprofit religious, educational, literary, scientific, benevolent or charitable corporations (Tit. 36, Sec. 652).

(3) property owned and used by a religious society as a parsonage to the value of $20,000, and personal property to the value of $6,000 (Tit. 36, Sec. 652).

(4) vessels built, undergoing repairs or construction in Maine on April 1 owned by nonresidents; pleasure vessels and boats in Maine on April 1 owned by nonresidents and left in Maine for repair or storage unless regularly kept in Maine during the preceding year; property located and taxed in another state or country; vehicles exempt from excise tax and registered snowmobiles; farm machinery used to produce hay and field crops to the aggregate market value not exceeding $5,000, excluding motor vehicles (Tit. 36, Sec. 655); water and air pollution control facilities (Tit. 36, Secs. 655, 656); all beehives; the average amount of personal property constituting stock in trade obtained as a trade-in for property sold in the regular course of business if a separate inventory of the traded-in items is maintained (Sec. 655).

(5) mines in process of development, but only for 10 years after opening (Tit. 36, Sec. 656); property in interstate transportation or held en route to a destination named in a through bill of lading (Tit. 36, Sec. 655); pipe lines of companies supplying towns with water free of charge to put out fires (Tit. 36, Sec. 656).

(6) property owned and occupied or used solely for their own purposes by benevolent, charitable, literary and scientific institutions, the American Red Cross, veterans' organizations, chambers of commerce or boards of trade in Maine; property owned by or held in trust for fraternal organizations, except college fraternities, operating under the lodge system for use solely by such organizations; property leased by and used solely by an incorporated charitable organization exempt from federal income tax operating a licensed hospital or blood bank (Tit. 36, Sec. 652).

(7) landing areas of approved privately owned airports the free use of which is granted to the public (Tit. 36, Sec. 656); estates of blind persons up to the value of $3,500; the estates of Indians who reside on tribal reservations; residential realty to the value of $3,000 of Maine residents who are blind if its value is not over $10,000 (if over $10,000 but not over $20,000, the exemption is $2,000) and if they are not receiving the above exemption for estates of blind persons (Tit. 36, Sec. 654); radium used for medical purposes (Tit. 36, Sec. 655).

(8) property of aged or disabled veterans, their unremarried widows and mothers or minor children, to the value of $4,000 ($20,000 for paraplegic veterans or unremarried widows of such veterans) so long as the property has a taxable situs at the place of residence and estates of certain veterans when held in joint tenancy with a spouse (Ch. 550, Laws 1975; Tit. 36, Sec. 653)

(9) household furniture, including television sets and musical instruments; wearing apparel; farming utensils; mechanics' tools (Tit. 36, Sec. 655).

(10) property conveyed between husbands and wives of veterans and servicemen for the purpose of obtaining exemption from taxation (Tit. 36, Sec. 653).

(11) fallout shelters, up to $200 multiplied by the number of persons they are designed to hold (Tit. 36, Sec. 656).

(12) real estate owned by the Water Resources Board of New Hampshire used to preserve Maine recreational facilities (Tit. 36, Sec. 651).

(13) industrial inventories, including raw materials, goods in process and finished work on hand; stock in trade, including inventory held for resale by a distributor, wholesaler, retail merchant or service establishment; agricultural produce and forest products; and livestock, including farm animals, cattle and fowl* (Tit. 36, Sec. 655).

(14) deposits or accounts in financial institutions (Ch. 500, Laws 1975; Tit. 9-B, Sec. 421); shares in credit unions (Ch. 500, Laws 1975; Tit. 9-B, Sec. 833).

Maine residents who are 62 or older, who own or rent a homestead in Maine and whose household income for the calendar year for single member households is not over $4,500 or not over $5,000 for claimants of households of two or more members are entitled to tax relief limited to the amount by which property taxes accrued, or rent constituting property taxes accrued **(25% of gross rent paid), exceed 21% of household income for the tax year over $3,000 but not over $5,000. No claim less than $5 or over $400 will be granted.** Applications must be made between August 1 and October 15 (Tit. 36, Secs. 6103, 6106, 6108—6112).

[¶ 20-488] **Basis.**—All property is required to be assessed at its just value in compliance with the laws of the state (Tit. 36, Sec. 201). Vessels and barges other than steam barges are taxed on an appraised value of $20 per ton, gross tonnage, for new vessels and decreasing one dollar per year until 17 years old, at and after which time they are taxed at $3 per ton (Tit. 36, Sec. 609). Personal property employed in trade is taxed on the average amount kept on hand for sale during the preceding year (Tit. 36, Sec. 502). The value of land classified as farmland or open space land is based on its current use (productivity value, beginning in 1978) (Ch. 726, Laws 1976, 1st Spec. Sess.; Tit. 36, Secs. 590, 1105, 1108).

[Local and State Government Tax]

[Municipal Tax]

[Uniform Property Tax]

[¶ 20-489] **Rates.**—All property is taxed at a rate equal to the aggregate of all lawful levies. For local and state government expenses, a tax is assessed in each municipality and the unorganized territory at 9¼ mills for the fiscal year ending June 30, 1976; 10¾ mills for the fiscal year ending June 30, 1977, 12¼ mills for the fiscal year ending June 30, 1978; and 13¾ mills for the fiscal year ending June 30, 1979, and thereafter. Municipal taxes are paid to the city treasurer, taxes assessed in unorganized territories are paid to the state. In addition, a state uniform school property tax is assessed with the rate to be enacted by April 1 by the legislature. The rate for the period beginning July 1, 1976, and ending June 30, 1977, is 13 mills. Thereafter, the rate is 12.5 mills. The rate is applied to state valuations of each municipality and property in the unorganized territory (Ch. 660, Laws 1976, 1st Spec. Sess.; Ch. 272, Laws 1975; Tit. 36, Sec. 451).

* Industrial inventories, stock in trade, livestock and agricultural produce and forest products, otherwise tax exempt, are subject to tax beginning April 1, 1974, and continuing through April 1, 1976, for the tax year ending March 31, 1977, at the same rate as provided in Title 36, Sec. 451 (see ¶ 20-489) applied to a 100% valuation (Tit. 36, Sec. 455).

[¶ 20-490] **Period Covered—Accrual.**—Taxes are for the current fiscal year in which collected.

[¶ 20-491] **Assessment Date.**—The state tax (see ¶ 20-489) is assessed July 1 for the fiscal year ending June 30 of the following year (Ch. 272, Laws 1975; Tit. 36, Sec. 452). All property, real and personal, is assessed for city and town taxes as of April 1 (Tit. 36, Sec. 502).

[¶ 20-492] **Situs.**—Real estate shall be assessed in the place where it is situated (Tit. 36, Sec. 553). Personal property with certain exceptions (see below) shall be taxed to the owner in the place where he resides (Tit. 36, Sec. 602). Exceptions to the general rule for assessing personal property: (1) personal property employed in trade, in the erection of buildings or vessels, or in the mechanic arts is taxed in the place where employed; (2) portable mills, store and office fixtures, professional libraries and apparatus, coin-operated vending or amusement devices, boats not used in tidal waters, camp trailers and television and radio transmitting equipment are taxed where situated; (3) personal property owned by nonresidents is taxed to the owner or occupier where situated (Tit. 36, Sec. 603).

[¶ 20-493] **Assessing Official.**—The assessors shall assess all municipal taxes and their due proportion of any state or county tax (Tit. 36, Sec. 709).

[¶ 20-494] **Returns.**—Upon notice by the assessor, taxpayers are required to make returns of property, real and personal, of which they were possessed on April 1 to the assessor. Failure to make returns bars the right to make application for abatement (Tit. 36, Sec. 706).

[¶ 20-495] **Assessment, Revision and Appeal.**—The assessors and the chief assessor of a primary assessing area assess all property, real and personal, recording separately the land value, exclusive of buildings (Tit. 36, Sec. 708). The assessors, within one year from the assessment, may make abatements (Tit. 36, Sec. 841). Decisions of assessors and local boards of assessment review may be appealed to the State Board of Assessment Review (Tit. 36, Sec. 844-D). Appeals from the decisions of the assessors are made to the superior court (Tit. 36, Sec. 845). The Bureau of Taxation equalizes state and county taxes among the towns (Tit. 36, Sec. 292).

[¶ 20-496] Collection of Tax.—A lien to secure the payment of taxes shall continue in force until the taxes are paid (Tit. 36, Sec. 552). Tax is payable on a date fixed by the town to the town collector. Interest not to exceed 8% may be collected after dates fixed by the town and discounts not to exceed 10% may be allowed before specified dates (Tit. 36, Sec. 505).

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 20-000.

¶ 20-497 Public Utilities

Special Provisions.—Land and buildings thereon owned by telegraph and telephone companies are taxed in the municipalities where situated. The excise tax on gross receipts, together with the sales and use tax, is in lieu of all taxes on such companies (Tit. 36, Sec. 2689). An excise tax, together with the tax on buildings and lands, is in place of all taxes on railroads and their realty (Tit. 36, Secs. 561, 2623). The gross receipts tax on parlor car companies is in lieu of all local taxation upon the cars and equipment of such companies (Tit. 36, Sec. 2572). Other utilities are subject to local assessment in the same manner as other property.

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 80-000.

¶ 20-498 Forestry District

Special Provisions.—A tax of 4¼ mills on a 100% valuation is assessed on all property in the Maine Forestry District, including rights in public reserved lots, except that in organized municipalities the rate is 4¼ mills on a 100% valuation multiplied by a fraction whose numerator is the previous year's assessed value and whose denominator is the total previous year's assessed value of all property taxable by the municipality. The tax must be paid by October 1. The State Director of Property Taxation notifies the owners of lands assessed by July 1 (Tit. 12, Sec. 1601).

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 20-000.

¶ 20-499 Tree Growth Tax

Special Provisions.—The tree growth tax applies to any parcel containing more than 500 acres of forest land and, upon application by the owner, to smaller parcels (Tit. 36, Sec. 574). The State Director of Property Taxation values each acre of land at 100% determined by wood production rate, applicable stumpage value and type of trees (Tit. 36, Sec. 576). Areas other than forest land within any parcel of forest land are valued on the basis of fair market value (Tit. 36, Sec. 576-A). The valuations are adjusted according to the currently applicable assessment ratio in the organized area or unorganized territory (Tit. 36, Sec. 578). Reduced valuation applies to land of low productivity or on which trees have been destroyed by fire, disease or insects (Tit. 36, Sec. 577).

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 20-000.

Description and analysis of the Maine Tree Growth Tax Law

The Tree Growth Tax Law (TGTL) is designed to give incentives to forest land owners to maintain their holdings as forest land and to increase the volume of wood grown. These goals are encouraged by preferential tax treatment. The TGTL is applied to all parcels of forest land of 500 acres or more. Those parcels of 10-500 acres which qualify may be included voluntarily.

The TGTL values land classified as forest land for tax assessment. These lands are valued according to their productivity. The value of forest lands under the TGTL is determined by a formula applied to the particular valuation of mixed growth, hardwood, or softwood. The valuations are determined by applying current market stumpage prices to forest growth for three forest types by county, i.e., softwood, hardwood and mixed timber types.

The State levies a tax on lands in the Unorganized Territory directly, whereas lands in organized towns are taxed locally according to the municipal tax formula.

The TGTL should act as an incentive to improve forest management since the most productive land enjoys the assessment applied to the value of the average level of productivity in a county for the particular forest type. Therefore, intensive management is not penalized on quality stands as it was under market value property taxation. Furthermore, the tax paid is generally less than the owner would pay if his land were assessed on an ad valorem basis at its market value, as is most other real estate in the State. This should encourage landowners to maintain their land as forest land.

This law is widely appreciated and supported in the Unorganized Territory, where the vast holdings of individuals and corporations are consolidated, a greater degree of management is economically feasible, and development pressures do not exist to the same degree as in other areas of Maine. Among owners of smaller parcels in the southern and western part of the State the law is more controversial. The tax savings may be an insufficient incentive to encourage management, especially on immature stands where no income from the land is available to finance improvement costs. Pressures for other uses may force economic decisions regardless of State tax policy.

A recent study and report on the current valuation of forest land under the TGTL suggests that there may be a better method of calculating current use value, and that the basic elements of the taxation formula need periodic review.* Factors to be considered are the 30% reduction factor, stumpage prices, and the capitalization rate.

* John Joseph, Tree Growth Tax, Implications for Forest Policy and Tax Equity. Maine Department of Conservation, November, 1976.

B. That the Division of Entomology within the Bureau of Forestry in cooperation with forest owners evaluate the present ability of the State to combat tree disease and insect problems. The Division should report its findings and recommendations to the Legislature.

C. That the Bureau of Forestry in the Department of Conservation be encouraged to conduct an intensive review of its present priorities for forest insects and diseases threatening Maine forests (e.g., White Pine Blister Rust).

REGULATION

The Land Use Regulation Commission, the Department of Environmental Protection, the Department of Inland Fisheries and Wildlife, and other State agencies administer State laws and regulations governing activities on forest land in Maine. The Select Committee heard testimony from forest industry representatives that some State and Federal regulation of forests in Maine produces an adverse effect upon the forest industry and, thereby, the Maine economy.

Although it is inevitable that some costs, in terms of productivity and growth, result from regulations, it is also true that social and economic benefits result from these regulations. The important question, of course, is whether the benefits exceed the costs. Further, there is the question of how much cost the State can impose on the forest industry and have it remain a viable economic force for the good of the State and its people. The Committee did not have the resources to answer these questions.

While there was some general criticism of State regulations and administration of these regulations, there were few, if any, specific provisions cited for reform, with the exception of the deer yard provisions and their potential conflict with the silvicultural provisions of the Spruce Budworm Control Act, Maine's only comprehensive insect control program. The Committee supports recently enacted legislation which will review state agency programs and state agency rules; P.L. 1977, c. 566 and P.L. 1977, c.554.

Recommendation for Regulation

A. That the Maine Legislature undertake a comprehensive study of the impact of regulation upon forest land owners and forest products manufacturers.

FINANCIAL INCENTIVES

Maine Tree Growth Tax Law

The State makes available financial incentives for improved forest management through the Maine Tree Growth Tax Law and by means of direct federal subsidy programs.

The substance of the report's findings and recommendations may be summarized in the following points:

A. The Maine Tree Growth Tax Law as a productivity tax encourages good forest management.

B. The Maine TGTL results in differential assessments for forest land from all other forms of real property; and this produces a tax shift from forest land owners classified under the Tree Growth Tax to other property owners and the State's General Fund.

C. This shift is not completely the result of a difference between fair market value and current use value, but is largely the result of the present method of calculating "current use value" for forest land.

D. If the correct productivity value of forest land is to be assessed, the discount factor and the capitalization rate must be reviewed periodically.

While the TGTL is designed to preserve Maine's forest resources by providing preferential tax treatment of forest land, the objective of the law, in some cases, is not being achieved. One of the major reasons for the limitations of the TGTL is ignorance of the provisions of the law on the part of many small land owners. Many small land owners are simply unaware of the benefits and penalties of the law.

Another difficulty contributing to the limitations of the TGTL is that which confronts a number of small land owners in their attempt to classify their forest land under the law. Some local tax assessors have not cooperated with small land owners and have refused to classify parcels of forest land of less than 500 acres under the tax law. In addition, land owners often do not understand the procedure by which decisions of local tax assors can be appealed to the Forestry Appeals Board.

While some of the provisions of the TGTL discourage a number of small land owners from utilizing the law, the law also produces some adverse effects. For example, municipalities which experience a loss of revenues as the result of forest land classified under the TGTL are reimbursed for the loss. The level of reimbursement, however, is based upon the revenues and land valuation of municipalities in 1972, prior to the upgrading of assessment and valuation practices that have occurred throughout the State subsequent to 1972. As a result, the level of reimbursement has been very limited.

In addition to a few disincentives and adverse results of the law, there are some inconsistencies in the law. For example, the Maine TGTL does not require the land owner with less than 500 acres to file a survey of the land that will be classified under the law, but it does require the land owner to submit a survey to remove land from the TGTL.

Another inconsistency concerns the penalties of the Maine TGTL, which are significantly greater than the penalties of the Farm Productivity and Open Space Land Law, a law which is designed with the same objective for agriculture as the objective of the TGTL for forestry. Another problem with the law is the phrase "fair market value" in § 583, paragraphs (a) and (b) which is interpreted differently by different people.

P.L. 1977, c.549, "AN ACT to Improve the Administration of the Maine Tree Growth Tax Law" authorized the State Tax Assessor to review the reduction factor in 1978 and every fourth year thereafter. In addition, he shall biennally review the capitalization rate. The Act provided for establishment of a Land Classification Appeals Board and procedures for appeal from its decision to Superior Court. The Committee supports these changes in Maine law and refrains from making further recommendations at this time since the law responds to several problems discussed above.

Recommendations for the Maine Tree Growth Tax Law

The Select Committee supports the concept of taxation of taxation of forest land on the basis of productivity and the retention of the Maine Tree Growth Tax Law. The Committee recommends the following changes:

A. That the Maine Forest Service in conjunction with the Bureau of Taxation prepare a booklet on the Maine Tree Growth Tax Law to be made available to all landowners to provide information on this law.

B. That the phrase "fair market value" in 36 MRSA § 581, 3rd paragraph, (a) and (b) be substituted with the phrase "100% full tax value as determined by the tax assessor".

Direct Financial Incentives

Two programs that provide monetary incentives for intensive forest management are the Agricultural Conservation Program (A.C.P.) and the Forest Incentive Program (F.I.P.). Under A.C.P.,the Maine Forest Service provides technical assistance to woodland owners for site preparation, planting, thinning and pruning. Incentive payments, to share in the cost of the practices, are provided by the Agricultural Stabilization and Conservation Service, a Federal agency. The maximum payment for one recipient is $2,500. Most individual A.C.P. projects range between 5 and 10 acres, and the maximum ranges between 20 and 30 acres. Inspection and tree marking are necessary for approval of a program by the Service Forester and he must certify that the work is done for payment to be made. The payment is 75% of costs, or according to a schedule provided by the Agriculture Stabilization and Conservation Service. In

Prepared by
MAINE COAST HERITAGE TRUST

Farm and Open Space Tax Law

This law allows the owners of farm land and open space to apply for assessment at current use values if their land meets the definitions set forth in the law.

Under the Farm and Open Space Tax Law "farmland" is defined as land of 10 or more contiguous acres on which farming or agricultural activities have produced a gross income per year in 1 of the 2 or 3 of the 5 preceding years of $100 per acre (maximum required income = $2,000).

Owners of farmland may apply for classification under this law for calendar year 1978 by applying by April 1, 1978. An owner of farmland applies by submitting to the municipal assessors schedules identifying 1) the land to be taxed under the law, 2) the acreage of each farmland classification: cropland, orchard land and pastureland, and 3) the location of each farmland classification. The owner must indicate that the land is farmland within the Farm and Open Space Tax Law definition. On the basis of this schedule (plus any other pertinent information) the municipal assessor determines first whether the land is suitable for classification under the law and second, the acreage of each farmland classification.

The owners of land which meets all the requirements of farmland classification, except for the minimum gross income requirement, may receive a 2-year provisional classification by the submission of a schedule of the lands to be so classified. If at the end of the 2-year period the land does not qualify as farmland, the owner shall be liable for the back taxes that would be due if the land had been assessed at fair market value for the preceding 2 years plus interest.

Land designated as open space land on a finally adopted comprehensive plan or zoning map will, on application of the owner, be classified under the Farm and Open Space Tax Law. If the land is not so designated as open space, it will still qualify for classification if the municipal assessor determines that its preservation would 1) conserve scenic resources, 2) enhance public recreation opportunities, 3) promote game management, or 4) preserve wildlife.

To apply for the open space classification, the owner must submit to the local assessor a schedule containing a description of the land and its current uses plus any other pertinent information that the assessor may require to make the determination. The deadline for application is <u>April 1</u> of the year in which the owner wishes the land to be classified.

The municipal assessor shall determine the 100% current use valuation per acre for <u>good</u> cropland, orchard land, and pastureland. These valuations will be adjusted using 80% of that valuation for <u>poor</u> farmland and using 120% for <u>very good</u> farmland. The municipal assessor shall also determine the 100% current use valuation per acre for open space land. All valuations shall reflect neither the potential for development nor the value attributable to road or shore frontage. Then to determine the assessed value for farmland and open space, the municipal assessor must adjust the valuations by the ratio to full value which is applied to other properties in the municipality.

CONSTITUTION OF MAINE

Article IX

GENERAL PROVISIONS

8. Taxation; Intangible property

Section 8. All taxes upon real and personal estate, assessed by authority of this State, shall be apportioned and assessed equally, according to the just value thereof; but the Legislature shall have power to levy a tax upon intangible personal property at such rate as it deems wise and equitable without regard to the rate applied to other classes of property. Nothing shall prevent the Legislature from providing for the assessment of the following types of real estate wherever situated in accordance with a valuation based upon the current use thereof and in accordance with such conditions as the Legislature may enact:

1. Farms and agricultural lands, timberland and woodlands;
2. Open space lands which are used for recreation or the enjoyment of scenic or natural beauty;
3. Lands used for game management or wildlife sanctuaries.

In implementing the foregoing, the Legislature shall provide that any change of use higher than those set forth above, except when the change is occasioned by transfer resulting from the exercise or threatened exercise of the power of eminent domain, shall result in the imposition of a minimum penalty equal to the tax which would have been imposed over the 5 years preceding such change of use had such real estate been assessed at its highest and best use, less all taxes paid on said real estate over the preceding 5 years, and interest, upon such reasonable and equitable basis as the Legislature shall determine.

FROM: THE REPORT OF THE GOVERNOR'S TAX POLICY COMMITTEE (1975)

What happens when an unbalanced tax structure such as Maine's places this burden on the necessity of housing? The following general results are, by and large, agreed upon by fiscal experts:

1. "Such high property taxes inevitably discourage investment in homes and home improvement and encourage spending on less heavily taxed items as automobiles, boats, travel, and entertainment. More importantly, in some low-income communities high property taxes discourage investments in new apartment houses, office buildings and manufacturing plants."(15)

2. A heavy property tax will magnify assessment mistakes, a deficiency common to communities.(16) High value properties are often under-assessed relative to low-cost residences. Where such variations occur the tax is made regressive.(17)

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13. Id. at 15. See also ACIR, Financing Schools and Property Tax Relief - A State Responsibility, 35-42 (1973).

14. ACIR, Changing Public Attitudes on Governments and Taxes, 9(1975)

15. Id. at 46. See also New Jersey Tax Policy Committee, the Property Tax (1972):" . . Dr. Dick Netzer found that the property tax as now constituted is a deterrent to new housing and the maintenance of existing homes and that it places a particular burden on low-income renters." at 20. (hereinafter cited as New Jersey Tax Policy Committee).

16. The Governor and the 107th Legislature recognized this deficiency by enacting into law L.D. 1917, a comprehensive reform of assessing practices. The Statement of Fact defined this need: "The purpose of this Act is to establish minimal assessing standards for Maine communities that will insure by 1979 equitable assessing practices . . . ."

17. ACIR, Property Tax Circuit Breaker: Current Status and Policy Issues, 14(1975).

3. A too heavy property tax means public services will be distributed with great inequity. The poor of Van Buren or Portland, or any of Maine's urban centers, will pay higher property taxes yet receive less services per dollar. Why? "The tax may be regressive among jurisdictions as well as among individuals. If one jurisdiction consists predominately of low-income families in low-cost housing, while a second jurisdiction is characterized by higher-income families living in higher-valued residences, property tax rates must be higher in the "poor" area in order to provide the same level of services as in the "rich" jurisdiction, other things being equal. The higher rates imposed on the low-income families contribute to the overall regressivity of the property tax."(18)

4. "Excessive property taxes have had an adverse effect upon environmental quality. This stems largely from the unending search of municipalities for tax ratables which is reflected in 'fiscal zoning'. Such zoning contributes to misuse of land resources, misdirected planning, and unnecessary pollution."(19)

5. High property taxes drive more affluent residents to suburbs with lower tax rates, leaving behind the poor and elderly in deteriorating neighborhoods.(20)

6. A high property tax is socially divisive because it encourages "snob" zoning: "Communities which are primarily inhabited by high-income people benefit by having lower tax rates because their inhabitants live in expensive homes which create a substantial tax base. Thus the tax structure provides a built-in incentive for communities to exclude medium and low income people by zoning."(21)

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18. Id.at 14. See also Connecticut Conference of Mayors and Municipalities, Property Taxpayers On the Ropes (1975): "Connecticut's property-poorest cities and towns levy an average tax rate which is more than twice the rate levied in the State's property richest. Yet, on average, the State's property poorest cities and towns can raise less than one quarter of the per capita tax yield raised in the property-rich municipalities. The property poorest town is able to raise less than one eighth of the per capita tax yield raised in the town with the richest property tax base." at 34.

19. New Jersey Tax Policy Committee 19.

20. See Massachusetts Public Finance Project, The Rich Get Richer and the Poor Pay Taxes, 27(1974).

21. Options for Fiscal Structure Reform 12.

These socially damaging effects of a too burdensome property tax clearly recommend that the property tax be made a smaller part of the State tax structure. To what tax should the burden mainly be shifted? The answer is equally clear: the personal income tax. Maine is 16th in the nation in terms of property tax burden yet we are 38th in terms of income tax burden.(22) The personal income tax can absorb most of this shifted burden.

Equitably the income tax is superior to our current property tax as a means of measuring the average person's ability to pay (the income tax reflects family size, the property tax does not) and, at only 8.4% of our current tax mix, it is an extremely underutilized tax source. Specifically, the Advisory Commission on Intergovernmental Relations (ACIR) in Washington suggests that the individual income tax assume a 20-25% share of a State's tax structure for the following reasons:

1. The personal income tax is a highly equitable tax, reflecting both horizontal equity and vertical equity.

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22. INDIVIDUAL INCOME TAX: 1973

	As a Percent of Personal Income		As a Percent of Federal Tax Liability	
	Percent	National Rank	Percent	National Rank
U.S. Average	1.5	-	13.5	-
New England States				
Massachusetts	2.8	6	25.4	9
Connecticut	.3	41	3.1	28
Maine	.8	37	9.1	38
New Hampshire	.2	42	1.9	42
Rhode Island	1.4	22	16.2	18
Vermont	2.6	8	27.6	5

Source: State Tax Collections in 1973, Table 3, p. 7, Table 6, p. 10, Preliminary Statistics of Income 1972, Individual Income Tax Returns, Table 6, p. 25. Prepared by the Federal Reserve Bank of Boston (1975).

2. The personal income tax responds well to economic growth, thereby producing revenue system elasticity. Revenues will grow as the economy grows and new services will not mean an automatic tax increase.[23]

Because Maine is a tourist state and revenue expenditures to accomodate our visitors are significant, the role of the sales tax, which taxes the consumption of both residents and visitors,[24] in the Maine tax structure should be larger than the 20-25% that is also recommended by ACIR. Currently, it is 26.3% of the tax mix and in Section V of this report the committee will recommend a slight increase in this percentage.

While the shift of burden from the property tax to the personal income tax, with slightly increased reliance on the sales tax, would produce the more balanced tax structure Maine needs, this reform is futile if the broad-based taxes that make up that structure do not reflect a person's ability to pay.

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23. Features of Fiscal Federalism 1-4.
The property tax lacks this ability to keep pace with economic growth. This is one of the roots of towns' and cities' failure to provide necessary services without increasing the property tax to an unfair level. John Menario, Portland city manager, described the failings of the property tax for the Commission on Maine's Future and made the following points:

1. Portland has been operating on the same resource base -- property -- since 1820 and it is no longer sufficient;
2. Property tax initially meant a city would be wealthier if it built tightly and as a result many cities were spoiled forever;
3. Industry and buildings, in the long run, only bring higher taxes; in 1973 Portland had its greatest development year with $15 million in new buildings. Today those buildings only produce $460,000 in added property tax revenue, not nearly enough to meet rising costs.

Menario's solution: increase State revenue sharing by returning to communities a percentage of the State income tax. See Sleeper, "City Officials Eye Tax Reform", Portland Press Herald, 1, col. 1 (July 19, 1975).

24. In Maine, 13.8% of our total taxes is generated by tourists; 10.3% is generated by out of State tourists. See Northeast Markets, Tourism in Maine: Analysis and Recommendation, 69(1975).

The Worst Tax

Table 1

Which do you think is the worst tax - that is, the least fair?

	Percent of Total U.S. Public				
	May 1977	May 1975	April 1974	May 1973	March 1972
Federal Income Tax	28	28	30	30	19
State Income Tax	11	11	10	10	13
State Sales Tax	17	23	20	20	13
Local Property Tax	33	29	28	31	45
Don't Know	11	10	14	11	11

The American public now clearly identifies the property tax as the least fair among major Federal, state, and local tax sources.

Table 1A

Responses to "Worst Tax" Question by Region

	Percent of Total U.S. Public	Percent of Respondents by Region			
		North-east	North Central	South	West
Federal Income Tax	28	20	32	33	25
State Income Tax	11	17	9	10	7
State Sales Tax	17	23	15	17	15
Local Property Tax	33	28	37	25	45
Don't Know	11	13	8	14	7

State income and sales taxes drew heaviest fire in the Northeast. Property taxes drew heaviest fire in the West.

Source: ACIR, <u>Changing Public Attitudes on Governments and Taxes</u>, 1977.

of an infrequent mass reappraisal has no parallel in the administration of the income or sales tax. As inflation pushes property values up, the assessment hikes become more pronounced and the taxpayer shocks become more severe.

- The property tax is more painful to pay than the "pay as you go" income and sales taxes. This is especially true for those property taxpayers who are not in a position to pay the tax on a monthly installment basis.

- The property tax has the worst public image. For more than fifty years, this tax has been cited by both political leaders and tax scholars as the most wretchedly administered tax.

III. If the property tax is so widely disliked, why don't we get rid of it?

Despite its obvious defects and poor public image, the property tax has significant political and fiscal virtues. First, it is the one major revenue sources directly available to local government and therefore serves as the sheet armor against the forces of centralization. Second, it is the one tax in general use that can recapture for the community the property values the community has created. Third, its high visibility forces local officials to be concerned about public accountability.

Beyond these three considerations there is the inescapable element of fiscal realism--the nation's local governments will not quickly come up with an acceptable substitute for this powerful $65 billion revenue producer. Prudent public policy, therefore, would dictate the adoption of measures designed to reduce the irritant content of this levy.

IV. Is it possible to reconcile a state interest in checking the growth of local property tax levies with the local government concern for retaining a fairly high degree of fiscal latitude?

The answer--no, unless the state is willing to make adequate compensation--the fiscal equivalent in the form of either a new non-property tax source or a substantial state revenue sharing program.

V. <u>When is the state justified in imposing a "temporary" lid on local property levies?</u>

Lids on local government levies may be justified on a temporary basis so as to enable property tax rates to stabilize at a lower level. This temporary stabilization action can be justified, for example, to insure that a state decision to finance a substantially larger share of school costs is not immediately wiped out by the decision of local officials to recapture for themselves (during a period of taxpayer confusion) that part of the property tax that has just been "freed up" by the state. Without this protection, state officials can be expected to be very reluctant to assume the political risks involved in underwriting this form of local property tax relief.

Second, a temporary local tax rate rollback or levy limitation may also be justified in those cases where the state tax department or the courts order a massive increase in local property tax assessment levels. Understandably, state officials do not want to be placed in a position of becoming the "fall guys" if local ratemakers (again during a period of taxpayer confusion) fail to cut back their tax rates commensurate with an unusually large increase in the assessment base.

The emphasis, however, must be on the temporary character of state tax lids or rollback action. Once the stabilization action has taken place, local decisionmakers should be allowed full access to the property tax on the assumption that they--not state policymakers--will then be held politically responsible for any subsequent increase in local property tax levels.1/

1/ ACIR, <u>State Limitations on Local Taxes and Expenditures</u>.

VI. What are the major intergovernmental fiscal consequences for states that impose tight lids on local property taxes?

A. Local property tax levels tend to be somewhat lower in the "lid" states than in non-tax lid states, all other major factors held constant.

B. Total state-local expenditures from own sources however, are about the same as in the states without tax lids, all other major factors held constant.

C. The above findings support the general inference that the property tax lids tend to reenforce other factors causing fiscal centralization at the state level.

D. The tighter the tax or expenditure lid the more persuasive becomes the local case for:

1. Fiscal notes in all proposed state legislation that would have an adverse fiscal effect on local governments and

2. State reimbursement for state expenditure mandates.

For a state-by-state breakdown of state mandates and fiscal notes, see Table 2.

VII. What is the most dubious policy that states can adopt when confronted with the demand to "do something" about rapidly rising property tax assessments caused by inflation?

The answer--freeze the residential property tax assessments. While the short-run effects may appear advantageous, a freeze policy will introduce all types of additional valuation inequities into the assessment process.

THE CONDITION OF STATE-LOCAL FISCAL RELATIONS: FIVE IMPORTANT INDICATORS

State and Region	Number of State Mandates (77 Possibilities Surveyed)	Fiscal Note on Legislation Affecting Local Government	Type of State Limit Placed on Municipal Tax or Spending Powers	Type of Compensation to Local Government 1/ for Tax Exempt State Property: In Lieu Payment	Local Tax Permitted	State Share of State and Local Expenditures From Own Sources (Fiscal 1975)
UNITED STATES TOTALS	35*	17	2/	33	16	55.0*
New England	35*					60.3
Maine	39 3/	No	None	None		68.0
New Hampshire	40	No	None	X		51.0
Vermont	31	No	None	X	X	68.9
Massachusetts	46	No	None	X		56.8
Rhode Island	11 3/	No	None	None		62.4
Connecticut	45	No	None	X		54.5
Mideast	37*					58.4
New York	60	No	Tax Rate	X	X	47.4
New Jersey	45	4/	Expenditures	X	X	46.6
Pennsylvania	41	Yes	Tax Rate	X		63.3
Delaware	21	4/	None	None		75.7
Maryland	20	Yes	Full Disclosure 5/	X		59.0
District of Columbia	--	--	Full Disclosure 5/	--		--
Great Lakes	37*					56.6
Michigan	25 3/	No	Tax Rate	X	X	54.3
Ohio	49	4/	Tax Rate	X	X	51.8
Indiana	26	Yes	Tax Rate and Levy	X		58.1
Illinois	37	No	Tax Rate	X		55.7
Wisconsin	50	Yes	Tax Levy	X	X	63.3
Plains	38					
Minnesota	51	4/	Tax Rate and Levy	X	X	56.5
Iowa	33	Yes	Tax Rate and Levy	None		56.8
Missouri	32	No	Tax Rate	X		50.6
North Dakota	38	Yes	Tax Rate	X		64.0
South Dakota	39	4/	Tax Rate	X		52.1
Nebraska	36	Yes	Tax Rate	None		44.0
Kansas	35	Yes	Tax Rate and Levy	X	X	51.7
Southeast	27*					64.4
Virginia	46	No	Full Disclosure 5/		X	58.8
West Virginia	8	No	Tax Rate	None		71.0
Kentucky	28	4/	Tax Rate	None		67.9
Tennessee	23	Yes	None	None		55.6

THE CONDITION OF STATE-LOCAL FISCAL ATIONS: FIVE IMPORTANT INDICATORS
(Continued)

State and Region	Number of State Mandates (77 Possibilities Surveyed)	Fiscal Note on Legislation Affecting Local Government	Type of State Limit Placed on Municipal Tax or Spending Powers	Type of Compensation to Local Government 1/ for Tax Exempt State Property: In Lieu Payment	Local Tax Permitted	State Share of State and Local Expenditures From Own Sources (Fiscal 1975)
UNITED STATES	35*	17	2/	33	16	55.0*
Southeast (Continued)	27*					64.4
North Carolina	32	No	Tax Rate	X	X	67.9
South Carolina	27	No	None	X		72.8
Georgia	25	4/	Tax Rate	X		54.6
Florida	43	4/	Tax Rate Plus 6/	X		53.5
Alabama	11 3/	Yes	Tax Rate	None		62.5
Mississippi	29	No	Tax Rate	X		69.3
Louisiana	20	No	Tax Rate	X		69.2
Arkansas	33	No	Tax Rate	X	X	69.9
Southwest	33*					60.7
Oklahoma	25	No	Tax Rate	None		58.7
Texas	33	Yes	Tax Rate	X	X	50.1
New Mexico	36	No	Tax Rate	None		72.5
Arizona	39	No	Tax Rate and Levy	None		61.6
Rocky Mountains	37*					54.0
Montana	48	Yes	Tax Rate Plus 6/	X		49.2
Idaho	41	Yes	Tax Rate	X		60.4
Wyoming	37	No	Tax Rate		X	45.9
Colorado	23	Yes	Tax Levy	X		50.9
Utah	35	Yes	Tax Rate	X		63.8
Far West	46*					50.9
Washington	46	4/	Tax Rate and Levy	X	X	57.8
Oregon	45	No	Tax Levy	X	X	49.5
Nevada	44	Yes	Tax Rate		X	47.6
California	52	Yes	Tax Rate and Levy	X		48.7
Alaska	39	4/	Tax Rate and Levy	None		76.5
Hawaii	49	No	--	None		78.5

*Averages.

1/ In most cases, these state payments are for a small select category of property, and seldom provide for full coverage of state property.

2/ U.S. Totals: No limitations--9; Tax rate limits--24; Expenditure limits--1; Tax rate & levy limits--8; Tax levy limits--3; Full disclosure--3; and Tax rate plus--2.

Source: Recent ACIR state surveys conducted in late 1976 and early 1977.

3/ Based on partial response.

4/ Fiscal note information provided at request or on a permissive basis but not necessarily for all state government actions.

5/ Full disclosure of effect of assessment increases on property tax rate.

6/ Tax rate limit plus full disclosure policy.

VIII. In many areas, the combination of inflation and market value appraisals has caused single family assessments to rise at a faster clip than other classes of urban property. What state policy would do the least violence to the principle of uniformity while preventing a gradual shift of property tax burdens from nonresidential to residential property owners?

In my judgment, the instrument of choice is a state financed circuit-breaker designed to shield low income home owners--elderly and nonelderly--from property tax overload situations.1/

It must be admitted, however, that while it does more violence to the concept of uniformity, the "split tax roll" proposal now being considered by the California legislature is more efficient than the circuit-breaker if the primary objective is to prevent a gradual shift in tax burden among the major classes of property owners. Under a split roll arrangement, the total amount of revenue contributed by single family home owners, for example, is pegged at a certain designated percentage. This causes the tax roll to be split with one rate applied to single family assessments and a different tax rate to be applied to all other assessments.

IX. Of the various forms of constraints states are now placing on local property tax rate authorities, which approach is most compatible with the objective of preserving wide tax latitude for local legislative bodies?

The new "truth in taxation" plan, pioneered by Florida, may prove to be far superior than state mandated rollbacks in reconciling local legislative de-

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1/ ACIR, Property Tax Circuit-Breakers: Current Status and Policy Issues, February 1975.

mands for fiscal flexibility and state legislative desire to fix political responsibility for higher property taxes. Under this approach, local legislative bodies are free to set tax rates as high as they desire, provided they follow a rigorous full disclosure procedure that reveals, for example, that it was the city council's decision to increase expenditures--not the assessor's action in raising assessments--that caused the general hike in property taxes.

Under this full disclosure approach, local bodies would be required to advertise prominently that a tax increase hearing will be held because the proposed amount of property taxes to be collected in the next year will exceed (by a designated percentage) the amount of the current levy.

X. Is it possible to maintain the integrity of the assessment process (frequent full market-value appraisal) while minimizing tensions caused by inflation induced induced increases in residential assessments?

The answer--a state should be able to hold tensions at tolerable levels, provided it incorporates five major elements into its general property tax reform and relief strategy. For an outline of these elements, see page 8.

The Five Elements	Required State Action
1. Legitimacy: Adopt an enforceable State valuation policy dedicated to ending the conflict between assessment law and practice. No matter which of the options on the right is selected, an essential or "given" first step is insistence on full market-value appraisal.	First Option: Adopt and enforce a statewide full-value assessment standard for all property. Second Option: Adopt and enforce a statewide fractional assessment standard that is uniform for all types of real property. Third Option: Allow each local assessment district to set its own assessment level (subject to State-required uniformity among types of real property and a minimum level). Fourth Option: Codify existing de facto classification by establishing and enforcing different statewide assessment levels for various types of real property.
2. Openness: Provide each taxpayer valuation information to enable him to judge the fairness of his assessment, and establish a simple taxpayer appeal system as a remedy for improper assessment.	a. Annual State assessment ratio studies. b. Full disclosure of the findings of assessment ratio studies--with the local results printed on assessment notices. c. Accessible and inexpensive taxpayer appeal system, separate from the assessing function.
3. Technical Proficiency: Require that appraisers have the ability to establish and maintain accurate estimates of the market value for every class of taxable property and that the administrative structure facilitate this objective.	a. Centralize primary appraisal at the State level or, failing this, consolidate appraisal districts into units at least countywide to permit efficient use of specialized personnel and equipment. b. Strong State supervision and coordination of appraisal, incluing technical assistance to local districts, where appraisal remains a State-local function. c. State training programs and certification for appraisers.
4. Compassion: Extend relief to those taxpayers carrying extraordinary burdens in relation to income.	State-financed relief targeted to those whose property tax burdens are greatest relative to income, and phasing out as income rises (circuit-breaker).
5. Political Accountability: Local legislative bodies--not the assessor-should be held politically accountable for any general increase in property taxes.	Require local bodies to advertise prominently that a tax increase hearing will be held because the proposed amount of property taxes to be collected in the next year will exceed (by a designated percentage) the amount of the current levy.

TABLE 86 – SUMMARY PROPERTY TAX DATA, BY STATE (Cont'd)

State	Locally assessed taxable real properties, 1966								
	Number (000)	Percent distribution of number of properties and of gross assessed value, by type of property							
		Residential (nonfarm)		Acreage and farms		Vacant lots		Commercial and industrial	
		Number	Value	Number	Value	Number	Value	Number	Value
United States	74,832	57	60	19	11	19	2.6	3.3	25
Alabama	1,199	54	57	30	17	11	1.7	3.8	24
Alaska	77	42	59	11	6	44	6.0	3.7	29
Arizona	643	53	68	10	7	36	3.6	1.1	21
Arkansas	1,441	23	43	40	35	30	3.2	2.1	17
California	5,985	69	61	8	10	17	3.7	4.2	23
Colorado	779	60	59	13	13	18	1.6	3.4	25
Connecticut	838	77	73	4	3	15	1.8	4.1	22
Delaware	175	68	66	10	8	17	2.0	3.7	24
Dist. of Columbia	146	82	60	–	–	14	5.3	3.8	31
Florida	2,913	52	62	10	13	35	6.3	2.6	18
Georgia	1,318	62	61	20	16	14	2.2	4.0	21
Hawaii	218	47	60	3	4	47	9.5	3.6	27
Idaho	295	45	29	37	35	13	1.4	4.3	33
Illinois	3,806	57	56	19	18	19	2.1	2.9	24
Indiana	2,287	53	57	21	20	24	2.1	2.4	20
Iowa	1,727	37	39	49	47	11	0.8	3.0	14
Kansas	1,389	43	41	37	45	17	1.0	1.9	12
Kentucky	1,030	65	55	22	27	10	1.2	3.6	17
Louisiana	1,073	63	64	14	9	19	2.8	3.3	25
Maine	453	61	64	17	2	17	1.6	4.3	31
Maryland	1,066	72	71	7	7	17	1.6	4.1	20
Massachusetts	1,900	70	70	4	1	21	2.3	4.9	27
Michigan	3,386	62	61	16	7	18	3.3	3.8	27
Minnesota	1,354	52	44	31	27	13	1.2	4.8	28
Mississippi	812	43	46	40	36	14	2.3	2.1	16
Missouri	1,826	54	58	28	17	15	1.6	2.6	24
Montana	351	41	42	43	34	11	1.2	4.0	23
Nebraska	707	46	38	38	50	13	1.0	2.3	11
Nevada	180	50	55	17	9	28	4.9	3.7	31
New Hampshire	432	60	70	19	3	16	1.6	3.3	25
New Jersey	1,999	72	71	3	3	20	2.5	6.0	24
New Mexico	376	54	61	12	17	31	6.1	2.2	15
New York	4,076	70	58	8	2	15	1.9	5.9	38
North Carolina	1,899	58	52	19	19	19	2.6	3.9	27
North Dakota	459	21	25	58	63	18	1.2	2.7	11
Ohio	3,940	60	65	12	10	25	2.5	2.4	22
Oklahoma	1,565	45	56	22	26	32	1.7	1.2	15
Oregon	835	58	53	22	22	17	1.7	3.1	23
Pennsylvania	3,822	73	66	7	4	14	1.5	4.4	28
Rhode Island	307	65	70	3	1	26	2.6	4.6	25
South Carolina	774	62	43	18	16	18	1.7	2.0	39
South Dakota	525	27	27	59	61	11	1.1	2.7	10
Tennessee	1,313	57	60	26	12	15	2.3	2.1	25
Texas	5,987	42	39	21	13	17	1.9	1.9	21
Utah	384	58	63	21	10	17	2.3	2.8	19
Vermont	188	56	53	16	9	22	3.0	6.0	34
Virginia	1,682	51	65	20	9	26	2.6	2.2	22
Washington	1,760	50	57	21	17	28	3.6	1.7	22
West Virginia	902	46	57	26	15	15	2.0	2.2	24
Wisconsin	2,146	43	61	38	11	15	1.7	4.1	26
Wyoming	108	71	55	17	26	9	1.4	3.2	18

See footnotes at end of table.

THE CHANGING PROPERTY TAX BURDEN
SINCE THE 1973 SCHOOL FINANCE ACT AND
THE UNIFORM PROPERTY TAX

TABLE 75 – PROPERTY TAX AS A PERCENTAGE OF TOTAL STATE-LOCAL TAXES, BY STATE, AND REGION, SELECTED YEARS, 1942-1975

State and Region	1996	1975	1971	1967	1962	1957	1942
United States		36.4	39.9	42.7	45.9	44.6[1]	53.2[1]
New England		(48.1)	(47.3)	(50.2)	(53.9)	(52.7)	(60.2)
Maine	36.5%	40.4	45.2	48.5	52.8	50.0	62.7
New Hampshire		60.0	59.1	63.4	63.6	62.8	60.5
Vermont		42.8	37.3	40.1	45.2	45.0	50.4
Massachusetts		52.9	52.2	51.8	60.6	58.0	67.2
Rhode Island		41.9	38.7	45.6	47.8	50.4	62.6
Connecticut		50.5	51.2	52.0	53.6	50.0	57.5

TABLE 71 – AVERAGE EFFECTIVE PROPERTY TAX RATES, EXISTING SINGLE-FAMILY HOMES WITH FHA INSURED MORTGAGES, BY STATE AND REGION, SELECTED YEARS, 1958-1975[1]

State and Region	1975	1971	1966	1962	1958
United States	1.89	1.98	1.70	1.53	1.34
New England					
Maine	1.86	2.43	2.17	1.81	1.58
New Hampshire	N.A.	3.14	2.38	2.03	1.81
Vermont	N.A.	2.53	2.27	2.10	1.63
Massachusetts	3.26	3.13	2.76	2.47	2.21
Rhode Island	N.A.	2.21	1.96	1.93	1.67
Connecticut	1.94	2.38	2.01	1.76	1.44

TABLE 19 – PERCENTAGE OF STATE-LOCAL GENERAL REVENUE FROM PROPERTY TAXES BY STATE, SELECTED YEARS, 1942 THROUGH 1975

State	1975	1971	1967	1962	1957	1953	1942
Maine	24.4	30.1	32.9	39.0	38.5	41.3	52.8

WHAT IS THE STATE VALUATION AND HOW IS IT ARRIVED AT?
-Taken from, Is the State Valuation Accurate, the Report of the Select Committee on State Property Tax Valuation (1977)

1. INTRODUCTION

Of all the issues that swarm about the Uniform Property Tax (UPT), the state levied property tax in Maine - Does the state property tax erode the local control of schools? Is the tax too burdensome? Are property taxes generally regressive? - perhaps the most basic is whether or not the UPT is based on an accurate valuation of property? Does the state's Bureau of Taxation correctly judge the full value of each locality's property in arriving at its state valuation?

The purpose of this committee is to determine just how accurate is the state's valuation of property and to suggest what improvements are needed.[1/]

Our general conclusions are that while the state valuation is conservative and reasonably accurate and will improve with each year, there are still significant changes needed. Some of these changes are administrative, some demand legislation and a few need modest increased funding.

But before we describe exactly what must be done, it is important to understand clearly the role of the state valuation and the current standards followed by the state and each locality.

2. WHAT IS THE STATE VALUATION?

The state valuation is the Bureau of Taxation's total estimate of the market value of all property in the state. The state has been making this estimate for many, many years and it is used primarily today:

1/ See Appendix A, Study Order S.P. 610.

A. As the valuation against which the mill rate of the Uniform Property Tax (UPT)[2/] is levied; and

B. As a factor in the equations used to equalize the distribution of financial assistance to local governments for purposes such as health and welfare, road maintenance, state-municipal revenue sharing.

The Maine Constitution requires that any property tax must be assessed at its market value ("just value")[3/]. Why does the state feel it has to make its own estimates rather than simply adding up the results of each local assessor?[4/] There are two main reasons:

A. Many towns do not frequently update the valuations of their property; and

B. Most towns do not assess at full market value but rather fix the value of each house at a percentage of its true value. This "assessment ratio" is often quite low[5/] and the lower it is the less likely it is to be correct.[6/] The crucial importance

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2/ There are currently two state property taxes: The Uniform Property Tax (UPT), which has been used to fund approximately 50% of the cost of education, and the Local and State Government Tax, which is used to tax the Unorganized Territory to pay for their municipal services.

3/ Maine Constitution, Article 14, section 8.

4/ There are no local assessors in the Unorganized Territory and the state would assess the property there whether or not there was an UPT or equalizing financial assistance formulas.

5/ This is one reason why one town may have a tax rate higher than a town with similar property and similar expenses. If one local assessor values his town's property at 40% of its market value and the other town assessor uses a 80% ratio, then the former town's mill rate will be double the latter town's rate.

6/ In Massachusetts a study has shown that towns and cities which assess residential properties near their full value have a five times better chance of avoiding inaccuracies (e.g., undervaluing expensive properties and overvaluing poor properties) than those localities assessing at the lowest assessment ratios. See Lincoln Institute of Land Policy, A Study of the Interrelationship of Massachusetts Assessment Level and Assessment Quality (July 20,1976).

of at least beginning with a full value estimate is explained at length in Appendix B.

So the State makes its own assessments of the market value of Maine property. How is it done?

3. HOW THE BUREAU OF TAXATION ARRIVES AT THE STATE VALUATION.

The state valuation is now updated every year. It consists of:

A. The Bureau's individual valuation of each piece of property in the Unorganized Territory; and

B. The Bureau's gross valuation of each of 497 municipalities in Organized Territory.

In the Unorganized Territory the Bureau is the "local" assessor and has achieved fair accuracy.[7/] The other question before this committee was whether the Bureau's "gross" valuation techniques in the Organized Territory were accurate. The basis of the Bureau's estimate is the sales-ratio study. This is how the Bureau did the state valuation for April 1, 1977:[8/]

A. The state valuation of the municipalities is determined basically by comparing sales information with valuations used by the local assessor. It takes approximately one year for the field personnel to cover all 497 municipalities. The Bureau's personnel compiled from the local Registry of Deeds information on recent sales transaction.

7/ The Bureau's assessment ratio for the Unorganized Territory is 71%, which is above that currently required to be achieved by all localities by 1979. For a further explanation of this rating, see Section 4, TO WHAT STATUTORY STANDARDS ARE THE LOCAL ASSESSORS HELD?

8/ This description is based upon a more complete version contained in the Bureau of Taxation's 1976 memo to the committee, "The Maine State Valuation".

B. The field personnel took the sales information to eacn municipality for discusssion with the local assessors. The assessors then advised the Bureau as to those sales which were not representative of fair market sales, such as family sales, and sales containing good will or personal property or sales with abnormally inflated prices. These sales were eliminated.

C. A sales ratio study was performed on the remaining sales:

(1) A sales ratio study lists the sales in ascending order according to the percentage of valuation of the sales price to the assessed value. From this study an average was determined.

(2) Where sufficient sales were available and where sales representated the various categories of property located within the municipality, this average ratio was then applied to the total municipal valuation of the municipality as reflected in the municipal valuation book. For example, if it was found that the average ratio in the sales ratio study was 50%, the total valuation arrived at by the municipal assessor would be doubled to obtain the 100% market value state valuation.

(3) The sales study was broken down into the various categories of property in the municipality, such as seasonal property, residential property, commercial property and farmland. An average ratio for each of these groups was obtained where necessary because of the different ratios used by assessors for various categories of property. In other cases it was necessary for the fieldman

to apply a judgment factor as to the ratio which was being applied to such areas as commercial properties, woodland properties, etc., where there was inadequate sales information.

(4) In those municipalities affected by the Tree Growth Tax Law, the values used for land classified under that Law are the productivity values established through the statutory formula. In many woodland towns and plantations this makes up a very large share of the State Valuation.

(5) Each of these studies, upon completion, were forwarded to the central office of the Bureau where they were reviewed for consistency and uniformity to ensure that the work of the various field personnel reflected an equalized valuation in each case. Adjustments were made by the office in those areas where sales information was lacking and it was sometimes necessary to use information on values from surrounding areas. All municipalities in a geographical or economic area were reviewed together to determine that increases reflected in the sales study were uniform for the area and reflected the general inflationary pattern.

(6) The Bureau then met with each local assessor to discuss that municipality's proposed state valuation and to find any possible errors. A final proposed state valuation was arrived at and each municipality had 45 days to appeal to the Municipal Valuation Appeals Board.

This appeals process completed the 1977 state valuation. It was filed with the Secretary of State in January 1977. It was accomplished by 7-9 fieldmen and a field supervisor. Of the 497 municipalities, only 36 appealed their valuation to the Appeals Board.

From this description it is clear that no matter how accurate the Bureau's sales information, if the local assessor's valuations are poor, the state valuation will be directly influenced. Before listing our findings and recommendations, it is necessary to explain exactly what standards, by statute, the local assessor is held to.

4. TO WHAT STATUTORY STANDARDS ARE THE LOCAL ASSESSORS HELD?

It is very important to affirm the relationship of accurate valuations by the local assessor to the general accuracy of the state valuation. Indeed, many of our conclusions and recommendations speak directly to this relationship. By statute the local assessor must meet the following standards:[9/]

A. Minimum assessment ratios. By 1979 each local assessor must value property at no less than 70% of its full market value.

B. Maximum assessment quality rating. By 1979 the local assessor must achieve an assessment quality rating of no less than 20. What is a quality rating? How is it arrived at? This is important to understand because it reveals exactly how the property tax can be an inequitable levy. The assessment quality rating is another name for coefficient of dispersion. This is how it is determined:

9/ See 36 MRSA §§ 327,328.

HOW TO FIND THE TYPICAL ASSESSMENT ERROR: AN ILLUSTRATION 10/

Suppose we have four houses, each of which sold for $30,000. The assessment rolls show the homes assessed at $10,000, $16,000, $22,000, and $28,000. (Remember, they should have been assessed the same.) The assessment-sales price ratios for the three would be:

1) $\frac{\$10,000}{\$30,000} = 33\%$ 2) $\frac{\$16,000}{\$30,000} = 53\%$

3) $\frac{\$22,000}{\$30,000} = 73\%$ 4) $\frac{\$28,000}{\$30,000} = 93\%$

To find the median, we rank the four in order, from highest to lowest:

93
73
53
33

Since there are an even number of ratios, we take the middle two and find the halfway point between them:

$$\begin{array}{r} 73 \\ +\ 53 \\ \hline 126 \end{array} \qquad 126 \div 2 = 63$$

Thus the median assessment-sales price ratio, or common assessment level, is 63 percent.

Now we want to find the average deviation from this common level — that is, how much, on the average, each individual assessment was off the mark.

First we find the difference between the common level -- the average assessment-sales price ratio -- and the ratio for each individual assessment.

$$\begin{array}{r} 63 \\ -\ 33 \\ \hline 30 \end{array} \quad \begin{array}{r} 63 \\ -\ 53 \\ \hline 10 \end{array} \quad \begin{array}{r} 63 \\ -\ 73 \\ \hline -\ 10 \end{array} \quad \begin{array}{r} 63 \\ -\ 93 \\ \hline -\ 30 \end{array}$$

(We can disregard plus or minus signs.)

Next we find the average of these differences.

$$\begin{array}{r} 30 \\ 10 \\ 10 \\ 30 \\ \hline 80 \end{array} \qquad 80 \div 4 = 20$$

Thus the average assessment error is 20 percent.

Finally we express this average difference as a percent of the common level:

$$20 \div 63 = .32$$

10/ Brandon, Rowe, Stanton, Tax Politics 216 (1976). This analysis uses the median ratio to reflect the assessment quality rating. This practice parallels the Committee's Recommendation No. 4. See Sections 6, THE COMMITTEE'S RECOMMENDATIONS.

Thus, the assessment quality rating is 32. In other words, the typical assessment was 32 percent higher or lower than it should have been. This means there could be a 64 percent gap between the assessments of two homeowners who should have been assessed exactly the same.

C. Annual sales ratio studies. Local assessors must perform annual sales ratio studies and must inspect each piece of property at least every four years.

Each of these local assessment standards are immensely important to the accuracy of the state valuation. Is the mandated quality assessment rating of 20 unduly rigorous? Here is what the authors of Tax Politics, a citizen's guide to taxation say:[11]

> The lower [the quality assessment rating] is, the more uniform assessments are generally. How low should it be? If it is 10 or less, the assessor is doing a respectable job. If it is more than 15%, he is doing poorly. Experts consider a typical assessment error of between 10 percent and 15 percent, plus or minus, to be acceptable. Some go as high as 20 percent, mainly in compromise to what they perceive as the situation today. If it is over 20 percent, the sooner you get a new assessor, the better. [An assessment quality rating] of over 20 means that every taxpayer, on the average, is assessed 20 percent too high or too low, and there are taxpayers who are paying twice as much tax as others even though they should be paying exactly the same.
>
> Assessors who get their typical error down to 5 percent to 10 percent deserve applause. Since market values change constantly, there are genuine problems in cutting the error much below that.

11/ Brandon, Rowe, Stanton, Tax Politics 216-217 (1976).

The statutory requirement of an assessment quality rating of 20 is not effective until 1979. Here are recent average quality ratings, based on the 1975 state valuation, for Maine's counties:[12/]

Androscoggin	39.6
Aroostook	49.9
Cumberland	25.2
Franklin	31.3
Hancock	38.8
Kennebec	32.0
Knox	41.0
Lincoln	39.2
Oxford	26.9
Penobscot	38.2
Piscataquis	36.8
Sagadahoc	37.2
Somerset	38.6
Waldo	42.0
Washington	44.0
York	22.1
Average of Counties	36.4

12/ Prepared by the Bureau of Taxation; 70 municipalities had insufficient sales for assessment quality rating purposes.

Other statutory local assessing standings - such as required tax maps, uniform accounting systems, or mandatory use of electronic processing - are non-existant. At one time such standards were required by the Bureau of Taxation but local reluctance to have their affairs directed from Augusta results in their repeal.[13]

With this introduction to the procedures of the state valuation and the local assessing standards which directly affect the accuracy of the state valuation, we can now turn to the committee's main conclusions and recommendations.

5. THE COMMITTEE'S MAIN CONCLUSIONS

The committee's conclusions result from our lengthy schooling in the procedures used by the Bureau of Taxation to reach the state valuation, from our consultations with many of the country's leading property tax experts and from our close working relationship with Thomas L. Jacobs and Associates, the consultants employed by the committee.

Appendix C is the report of Jacobs and Associates to the committee. [Hereafter referred to as the Jacobs Report.] We endorse its analyses, conclusions and recommendations. All interested persons are urged to read it in its entirety.

For this report the committee will summarize the main conclusions and recommendations of the Jacobs Report but will also include other conclusions and recommendations that grew out of the committee's many months of study.

13/ See Public Laws, Chapter 545.

A. THE MAINE CIGARETTE TAX

The following description is taken from the Commerce Clearing House, State Tax Guide (second edition)

¶ 55-486 Cigarette Tax

Cigarettes Subject to Tax.—A tax is imposed on all cigarettes held in the state for sale. Transactions which may not be taxed under the federal constitution are exempt (Tit. 36, Sec. 4365).

Rates.—The tax is 8* mills for each cigarette (Ch. 768, Laws 1974, 1st Spec. Sess.; Tit. 36, Sec. 4365). Distributors may purchase cigarette stamps at a discount of 2½% * of their face value; dealers purchase at face value (Ch. 768, Laws 1974, 1st Spec. Sess.; Tit. 36, Sec. 4366).

Reports and Records.—Unclassified importers must notify the Tax Assessor within 24 hours after receipt of unstamped cigarettes (Tit. 36, Sec. 4365).

Distributors and dealers must preserve for 2 years records of all cigarettes manufactured, produced, purchased and sold. The books, papers and records of distributors and dealers are subject to examination by the State Tax Assessor at all times (Tit. 36, Sec. 4375).

Payments.—Stamps are purchased from the State Tax Assessor (Tit. 36, Sec. 4366). The stamps are affixed by distributors before transfer from their possession or by dealers within 72 hours after coming into possession of unstamped cigarettes (Tit. 36, Secs. 4368, 4369). Unclassified importers must pay the tax within 10 days after receipt of unstamped cigarettes (Tit. 36, Sec. 4365).

Licenses and Permits.—The following license fees are required: for a wholesale outlet, $25; for a retail outlet, $1 (including vending machines); for a wholesale dealer's license, $10; for an unclassified importer's license, no fee (Tit. 36, Sec. 4363).

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 55-000.

B. ANALYSIS

1. Economic effect.

The economic impact of cigarette smoking should not be underestimated. Illnesses caused by cigarettes result in many millions of dollars being lost to the Maine economy (medical bills, days lost on the job, etc.). Thus, it might be argued that higher taxes that cut consumption might be justified.

Two other factors should also be considered. High cigarette taxes may increase the number of "bootleg" cigarettes coming into the state and may also increasingly encourage Maine citizen's to buy their cigarettes in New Hampshire. However, at the current rates, cigarette tax revenues continue to increase ($22.9 million in 1975, $23.9 million in 1976) so it is debatable whether the current tax rate is or is not too high.

2. Yield.

a. The cigarette tax in Maine currently yields $23 million. This is approximately 3.4% of the state tax mix.

b. Elasticity: The cigarette tax is relatively inelastic.

Even when the tax is increased, the demand for cigarettes remains constant. It thus resembles the inelastic demand for alcoholic beverage.

c. Yield from increased rates

1) For every penny you add to the sales tax you can expect a $1.8 million yearly increase in revenues

2) If you removed the exemption from the sales tax of cigarette purchases you would increase revenues each year by $3.5 million.

d. Equity.

1) Cigarette taxes are clearly regressive throughout the entire income scale; that is, as your income increases, you pay a smaller percentage of it in cigarette taxes than a poor person does. On the other hand, cigarettes are also a "luxury" purchase and the tax is only paid by people who desire the luxury.

e. Administration.

1) The cigarette tax is administratively efficient, but if black market sales become a great problem, then it might become more expensive to enforce it.

C. POSSIBLE AREAS OF REFORM

1. Increase taxes so as to cut consumption. This would aid not only the individual smoker but also the Maine economy which would be less dragged down by workers with smoking related illnesses. Of course, such a "reform" might cut revenues, increase New Hampshire purchases and increase "black market" sales. It might also unfairly burden the low-income smoker.

2. Build into the taxes on personal consumption (e.g., sales taxes, cigarette taxes) a general tax rebate, to alleviate any regressiveness of such taxes. It could be administered cheaply and efficiently as a credit on personal income taxes owed by each citizen.

A. MAINE ALCOHOLIC BEVERAGES TAXES

The following description is taken from the Commerce Clearing House publication, State Tax Guide (second edition)

¶ 35-485

Persons and Beverages Subject to Tax.—An excise tax is imposed on the manufacture and sale of all malt beverages and table wines, except those sold by licensed wholesalers, manufacturers, bottlers or rectifiers to any instrumentality of the United States, ships of foreign registry or any industry for use as an ingredient in a non-beverage commodity (Tit. 28, Sec. 452). If, in the production of wines, agricultural products of other states or countries are used in part, an excise tax on raw materials is added (Tit. 28, Sec. 501). Sales of malt beverages by a wholesaler to a foreign vessel are exempt from excise taxes. Sales of malt beverages to any Maine Army National Guard training site are exempt (Tit. 28, Sec. 452). Liquor is defined as any beverage containing more than ½ of 1% alcohol. Table wine is any wine containing not more than 14% alcohol by volume, including sparkling wine (Tit. 28, Sec. 2).

The sale and distribution of intoxicating liquors are by or under the direction of the State Liquor Commission (Tit. 28, Sec. 55).

Rates.—The rate of tax on malt beverages is: wholesale licensees importing malt liquors, 25¢ per gallon; and manufacturers, 5⅓¢ per gallon on malt liquors manufactured in the state. An excise tax of 30¢ per gallon is imposed on all table wine imported into Maine, except that the tax is 20¢ per gallon on all still wine containing 14% or less alcohol by volume manufactured or bottled in Maine. An excise tax of $1 per gallon is imposed on all sparkling wines manufactured in or imported into Maine. The taxes are paid by the Maine manufacturer or the importing wholesaler (Tit. 28, Sec. 452). Excise tax on wines if produced from agricultural products of foreign states is 4¢ per gallon on liquid raw materials, and 2¢ per pound on solid or semi-solid raw materials (Tit. 28, Sec. 501). All spirits and wine, except table wine, must be sold by the Commission at a price which will produce a state liquor tax of not less than 75%* based on the less carload cost FOB the Commission's warehouse. An additional tax of 75¢ per gallon is imposed on wines containing more than 14% alcohol by volume (Tit. 28, Sec. 451).

License Requirements.—All full-year licenses are issued for one year from the date of issuance and the prescribed fee must accompany the license application. However, apple cider processing plant licenses expire August 31. License fees are imposed on manufacturers, distillers, brewers, rectifiers, bottlers and wineries, and for the sale and consumption of liquor at the following rates (Ch. 741, Laws 1976, 1st Spec. Sess.; Tit. 28, Secs. 501, 604, 651, 701):

Classification	Annual Rate
Manufacturers or foreign wholesalers of malt liquor only	$ 600
Manufacturers or foreign wholesalers of table wine only	600
Wholesalers of malt liquor and table wine (for each distributing center or warehouse)	600
Class I, spirituous, vinous and malt beverage for on-premises consumption	$ 750
Class I-A, on-premises consumption of spirituous, vinous and malt beverages in hotels that do not serve food	1,000

Classification	Annual Rate
Class II, on-premises consumption of spirituous liquor only	$ 500
Class III, on-premises consumption of vinous liquors only	200
Class IV, on-premises consumption of malt liquor only	200
Class V, on-premises consumption of spirituous, vinous and malt beverages in clubs without catering privileges	450
Class VI, off-premises consumption of malt liquor only	125
Class VI-A, optional license for off-premises consumption of malt liquor only in retail stores and service organizations without a stock of groceries worth $1,000 in wholesale value	225
Class VII, off-premises consumption of table wine only	125
Class VII-A, optional license for off-premises consumption of table wine only in retail stores and service organizations without a stock of groceries worth $1,000 in wholesale value	225

Part Time Licenses

Classification	Fee
Part time license to sell alcoholic beverages for on-premises consumption	one-half the annual fee

Two-Month Extension of Part Time License

Class I license	$140
Class I-A license	180
Class II license	40
Class III license	40
Class IV license	40
Class V license	40
Manufacturers' licenses	
Distillers and brewers	
using domestic raw materials	$ 100
using foreign raw materials	3,000
using agricultural products not available in Maine, minimum fee	1,500
base fee (to accompany license application; final fee to be determined at end of year)	100
Rectifiers and bottlers	500
Wineries using domestic raw materials	50

Reports.—All manufacturers and wholesalers must file a report with the State Liquor Commission on or before the 10th of each month (Tit. 28, Secs. 603, 652). Persons holding manufacturers' licenses must file monthly reports with Commission of raw materials used (Tit. 28, Sec. 501).

Payment.—The tax is paid to the State Liquor Commission at the time the malt beverages are purchased, or, for bonded wholesalers, the tax on malt liquor and table wine is due on or before the 10th of each month (Tit. 28, Sec. 652). Manufacturers' license fees, as finally computed, are due December 31 each year (Tit. 28, Sec. 501). The consumer's tax is paid at the time of purchase from state liquor stores (Tit. 28, Sec. 451).

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 35-000.

B. ANALYSIS

1. Economic effect

The economic effect of taxes on alcoholic beverage is similar to cigarette taxes. Both are examples of "luxury" consumption. Yet both create in some persons psychological dependencies and for these people become akin to "necessities". Both cause diseases which cost the Maine economy dearly (through absences from work, hospital costs, ect.)

Like cigarettes, our taxes encourage some citizens to make their purchases in New Hampshire. However, black market sales do not seem a problem in Maine.

2. Yield

a. Alcoholic beverage raised approximately $24 million in 1976 and $21 million in 1975. The rates did not change between those two years.

b. Elasticity

Clearly, demand for alcoholic beverages is very inelastic. Raise the taxes a moderate amount and consumption would probably not decrease.

c. Yield from increased rates:

1. $.02 increase in tax on beer: $1.8 million

2. $.03 increase in tax on wine: $.2 million

3. $.15 increase in tax on hard liquor: $1 million

d. Equity:

Alcoholic beverage taxes are regressive, that is the poorer person pays a greater percentage of his income on liquor taxes than does the wealthier person. On the other hand, alcoholic beverages are not necessities.

e. Administration

The administration of alcoholic beverage taxes is moderately efficient.

C. POSSIBLE AREAS OF REFORM

1. Increase alcoholic beverage taxes to cut consumption

2. Dedicate percent of revenues to alcoholic treatment

3. Institute income tax credit for taxes paid to remove regressiveness of the tax.

Maine currently taxes property left by a deceased person in two ways:

1. By an inheritance tax (a tax levied against a person who receives, under the deceased's will, a part of the deceased's estate, and

2. By an estate tax (a tax levied against the value of the deceased's estate.

The following description of the inheritance tax is taken from the Commerce Clearing House's publication, State Tax Guide (2nd edition):

Inheritance Tax

The inheritance tax is levied at different rates according to whether the property is Class A, B or C property. The chart below gives the different rates for the different classes and below the chart explains which persons fall in what class (e.g., a wife receiving money from her husband's will is in Class "A") and what monetary exemptions are built into the law (e.g., a wife would receive a $50,000 before the husband's bequest would begin to be taxed).

¶ 89-486 **Inheritance Tax**

Applicable to estates of decedents dying on or after October 1, 1975

Table 1

Value of Share From	To	Class A Tax on Column 1	Class A Rate on Excess	Class B Tax on Column 1	Class B Rate on Excess
(1)	(2)	(3)	(4)	(5)	(6)
$ 0	$ 25,000	$ 0	5%	$ 0	8%
25,000	50,000	1,250	5%	2,000	10%
50,000	100,000	2,500	6%	4,500	10%
100,000	250,000	5,500	8%	9,500	12%
250,000	....	17,500	10%	27,500	14%

Table 2 (Class C)

Value of Share From	To	Tax on Column 1	Rate on Excess
(1)	(2)	(3)	(4)
$ 0	$ 75,000	$ 0	14%
75,000	150,000	10,500	16%
150,000	....	22,500	18%

Personal Exemptions.—*Class A.*—Husband, wife, lineal ancestor, lineal descendant, adopted child, stepchild, adoptive parent, wife or widow of a natural or adopted son or husband or widower of a natural or adopted daughter of a decedent, grandchild who is the natural or adopted child of a natural or adopted child of a decedent. For rates see Cols. (3) and (4) in table above.

Exemption: (1) Husband, wife, $50,000, (2) Father, mother, child, adopted child, stepchild or adoptive parent or grandchild who is the natural or adopted child of a natural or adopted deceased child of decedent, $25,000, except that if there is more than one grandchild, their total exemption shall, *per stirpes*, be $25,000. The exemption is applied before computing the tax.

(3) Grandparent and other lineal ancestors of remoter degrees, wife or widow of a natural or adopted son, husband or widower of a natural or adopted daughter of a decedent, grandchild who is the natural or adopted child of a natural or adopted living child of a decedent and other lineal descendants of remoter degrees, $2,000. The exemption is applied before computing the tax.

Class B.—Brother, half-brother, sister, half-sister, uncle, aunt, nephew, niece, grand nephew, grand niece, cousin. For rates see Cols. (5) and (6) in table above.

Exemption: $1,000. The exemption is applied before computing the tax.

Class C.—All others. For rates see table 2 above.

Exemption: $1,000. The exemption is applied before computing the tax.

Charitable Exemptions.—Transfers to Maine charitable, etc., organizations, transfers for charitable, etc., use in Maine, and transfers to charitable, etc., organizations of other states or countries, when such states or countries exempt transfers to Maine organizations, are exempt from tax.

Administration.—The inheritance tax is administered by the State Tax Assessor, at Augusta, 04326.

Source.—Maine Revised Statutes, 1964, Tit. 36, Secs. 3401 and following. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 93-701 to 93-792.

Estate Tax

This description is taken from the Legislative Finance Office's, Compendium of State Fiscal Information (1976):

> There is, in addition to the inheritance tax, an estate tax upon all estates which are subject to taxation under the Federal Revenue Act of 1926. The tax is imposed upon the transfer of the estate of every person who at the time of his death was a resident of this State. The amount of the tax is the equivalent of the amount by which 80% of the federal estate tax payable under the 1926 Act exceeds the amount of the inheritance tax to be paid. Tax imposed upon the transfer of all real property or tangible personal property, etc. See 36 MRSA §§ 3741-45

B. ANALYSIS

1. Economic effect

Maine's estate and inheritance taxes produce relatively little revenues (e.g., 1975-76: $7,361,635.75) and therefore have little economic impact. Critics of change in the current law say that to make the rates more progressive might cause "tax flight" - wealthy people adopting other states as their domiciles.

2. Equity

The tax tables are slightly progressive, that is the rate increases as income increases.

C. POSSIBLE AREAS OF REFORM

The 1975 Report of the Governor's Tax Policy Committee made the following analyses of the state inheritance and estate taxes:

> Inheritance and Estate Taxes
>
> 1. "Death" taxes should be based on the federal system.
>
> It is recommended that the current inheritance and estate taxes be repealed and replaced by a single estate tax based upon a percentage of the Federal taxable estate. The rates of such a tax would be graduated upward to insure no loss in revenue.
>
> 2. The name of the "Inheritance Tax Division" should be changed to "Estate Tax Division".

The committee has found that a single estate tax, based on a percentag of the Federal taxable estate, would be a more efficient alternative for the collection of so-called "death taxes". This single estate tax would replace the current State inheritance tax and current State estate tax. If such a "piggyback" estate tax were adopted, less than 40% of the returns now processed would have to be handled, thus reducing administrative costs. A tax of this kind is "self assessing" (payment is submitted with the return).

This tax would be imposed upon the entire estate, which then would be liable for its payment. The relationship of the beneficiaries to the deceased is not considered (except in the case of a surviving spouse, who under Federal law is entitled to receive tax free one half of the adjusted gross estate). This means that the computation of the tax is greatly simplified. Similarly, since the tax is levied along Federal estate guidelines, it can be calculated as soon as the net taxable estate is determined. Further, this tax reflects each estate's "ability to pay" because smaller estates are exempted.

In the 107th Legislature, L.D. 2142 was introduced embodying this recommendation. It failed to pass.

Another possible reform is to follow the 1977 lead of N.Y. state and enact legislation that would lessen the estate taxes on family owned farms and small businesses. The reason for such legislation was a N.Y. study that showed that nearly seven out of every thousand farms in the state had to be sold in 1975 to pay estate taxes.

A. MAINE VEHICLE, ROAD AND GAS TAXES

Maine currently has the following taxes on transportation:

1. Motor fuel taxes
2. Use fuel taxes
3. Road taxes
4. Motor vehicle registration fees
5. Common carrier fees.

Not included in this analyses is the motor vehicle excise tax which is considered a miscellaneous personal tax and described in that section. The following description of these taxes is taken from the Commerce Clearing House publication, State Tax Guide (2nd edition):

Motor Fuels Tax

¶ 40-486

Persons and Motor Fuels Subject to Tax.—Distributors, including importers, pay tax on all motor fuel used, sold or distributed in Maine, including sales to the state or any political subdivision (Tit. 36, Secs. 2902, 2903).

Fuel (1) exported, (2) which may not be taxed under the federal constitution, (3) brought into the state in the fuel tank of a motor vehicle, and (4) sold by one distributor to another is exempt (Tit. 36, Sec. 2903).

Eight cents of the tax paid on fuel used in commercial motor boats, in tractors used for agricultural purposes and not operating on the public highways, in vehicles which run only on rails or tracks, in stationary engines, or in the mechanical or industrial arts is refunded (Tit. 36, Sec. 2908). Five-ninths of the tax paid on fuel used in piston-driven aircraft is refunded (Tit. 36, Sec. 2910). The entire amount of the gasoline or use fuel tax is refunded to common carriers of passengers on tax-exempt passenger-fare revenue (Tit. 36, Sec. 2909). Allowance is made for actual loss (Tit. 36, Sec. 2906).

Rates.—9¢ per gallon except that the tax on fuel for use in jet or turbo jet aircraft engines is 1¢ per gallon (Tit. 36, Sec. 2903). Distributors are allowed a deduction of 2% of the tax paid for shrinkage or loss in handling. Retail dealers are allowed a refund of ½ of 1% of the tax paid on gross purchases for losses due to shrinkage or evaporation (Tit. 36, Sec. 2906). No fee is required for distributor's certificate (Tit. 36, Sec. 2904).

Reports.—Distributors, importers or exporters report on or before the last day of each month to the State Tax Assessor (Tit. 36, Sec. 2906).

Payment.—Tax payment accompanies report (Tit. 36, Sec. 2906).

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 40-000.

Use Fuel Tax

¶ 40-490

Persons and Fuel Subject to Tax.—A tax is imposed on users of fuel when such fuel is used for the generation of power to propel motor vehicles on the public highways or turnpikes operated and maintained by the Maine Turnpike Authority. No tax is imposed on fuel exempt from taxation by the constitution of the U. S. or Maine or on fuels subject to the gasoline tax (Tit. 36, Sec. 3025). Fuel used in noncommercial vehicles having tank capacity of 20 gallons or less, owned by nonresidents, is exempt (Tit. 36, Sec. 3022). Every person selling at retail and delivering fuels directly into fuel tanks of motor vehicles must obtain a use fuel dealer's license and collect the use fuel tax (Tit. 36, Sec. 3035).

Rates.—9¢ per gallon (Tit. 36, Sec. 3025). There is no statutory provision for a dealer's license fee.

Reports.—Users of fuel file reports with the State Tax Assessor not later than April 30, July 31, October 31 and January 31 (Tit. 36, Sec. 3028). Use fuel dealers file reports with the State Tax Assessor on or before the last day of each month (Tit. 36, Sec. 3035).

Payment.—The user's tax is paid to the State Tax Assessor quarterly with the report (Tit. 36, Sec. 3028). The use fuel dealer's tax payment accompanies the reports (Tit. 36, Sec. 3035).

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 40-000.

Road Tax

¶ 40-495

Persons and Fuel Subject to Tax.—Every motor carrier and every person operating a vehicle licensed for a load in excess of 10,000 lbs. or a gross weight in excess of 20,000 lbs. shall pay a tax on the amount of fuel used in its operations in the state (Tit. 36, Secs. 2963, 2971). Credit is allowed for taxes paid on motor fuel purchased in the state (Tit. 36, Sec. 2963).

Rates.—Rate is equivalent to tax rate per gallon of motor fuel (Tit. 36, Sec. 2963).

Reports.—Reports are filed with the Tax Assessor on or before the last day of April, July, October and January (Tit. 36, Sec. 2965).

Payment.—Payment is made when the report is filed (Tit. 36, Sec. 2964).

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 40-000.

Motor Vehicle Registration Fees

¶ 50-486

Registration Fees.—The following are the principal registration fees payable to the Secretary of State. The registration year for all vehicles except automobiles is from March 1 to the last day of February following. For 1975, automobiles having a plate number with a last letter or digit as follows shall be registered to expire as follows (Ch. 56, Laws 1975; Tit. 29, Secs. 55, 106):

Last Letter	Last Digit	Registration Fee for 1975	Expiration Date
.....	0	$12.50	October 31, 1975
A, J	1	13.75	November 30, 1975
B, K, S	2	15.00	December 31, 1975
C, L, T	3	16.25	January 31, 1976
D, M, U	4	17.50	February 28, 1976
E, N, V, F, O, W	5 or 6	18.75	March 31, 1976
G, P, X	7	20.00	April 30, 1976
H, Q, Y	8	21.25	May 31, 1976
I, R, Z	9	22.50	June 30, 1976

Thereafter, automobile registrations expire annually on the last day of the same month. New registrations expire at the end of the month one year from the month of issuance (Tit. 29, Sec. 106).

PASSENGER VEHICLES

A flat fee of $15 is imposed for the registration of a motor vehicle used for the conveyance of passengers. Motor vehicles used for livery or hire and interstate motor buses pay double the registration fee provided for passenger motor vehicles; except school buses and hearses. Interstate motor buses transporting passengers for hire and operating a fleet of 2 or more buses, shall register and pay the above fees, based on the proportion which the mileage of such buses operated in Maine bears to the total mileage of all such buses operated within and without Maine. Convertibles shall pay $15. Pickup trucks not used commercially may be registered in the same manner as automobiles if they weigh less than 6,000 lbs. and if they are privately owned (Ch. 219, Laws 1975; Tit. 29, Sec. 242). House trailers, $5, and special mobile equipment which is permanently mounted on a motor chassis, $10 (Tit. 29, Sec. 244).

MOTOR TRUCKS, TRAILERS AND BUSES

Trucks Equipped with Pneumatic Tires

Gross Weight	Fee	Gross Weight	Fee
6,000 lbs. or less	$ 15.00	32,001 lbs. to 35,000 lbs.	$268.00
6,001 lbs. to 9,000 lbs.	20.00	35,001 lbs. to 38,000 lbs.	294.00
9,001 lbs. to 11,000 lbs.	35.00	38,001 lbs. to 42,000 lbs.	321.00
11,001 lbs. to 14,000 lbs.	60.00	42,001 lbs. to 46,000 lbs.	348.00
14,001 lbs. to 16,000 lbs.	80.00	46,001 lbs. to 50,000 lbs.	375.00
16,001 lbs. to 18,000 lbs.	100.00	50,001 lbs. to 55,000 lbs.	415.00
18,001 lbs. to 20,000 lbs.	125.00	55,001 lbs. to 60,000 lbs.	455.00
20,001 lbs. to 23,000 lbs.	150.00	60,001 lbs. to 65,000 lbs.	495.00
23,001 lbs. to 26,000 lbs.	175.00	65,001 lbs. to 70,550 lbs.	545.00
26,001 lbs. to 29,000 lbs.	214.00	70,551 lbs. to 73,280* lbs.	600.00
29,001 lbs. to 32,000 lbs.	241.00		

Vehicles having 2 or more solid tires pay an additional fee of 33⅓% of the registration fee (Tit. 29, Sec. 246).

Farm Trucks (2 or 3 Axles)

Gross Weight	Fee	Gross Weight	Fee
9,001 lbs. to 11,000 lbs.	$ 21.00	29,001 lbs. to 32,000 lbs.	$140.00
11,001 lbs. to 14,000 lbs.	32.00	32,001 lbs. to 35,000 lbs.	200.00
14,001 lbs. to 16,000 lbs.	43.00	35,001 lbs. to 38,000 lbs.	220.00
16,001 lbs. to 18,000 lbs.	64.00	38,001 lbs. to 42,000 lbs.	240.00
18,001 lbs. to 20,000 lbs.	75.00	42,001 lbs. to 46,000 lbs.	260.00
20,001 lbs. to 23,000 lbs.	90.00	46,001 lbs. to 50,000 lbs.	280.00
23,001 lbs. to 26,000 lbs.	105.00	(Tit. 29, Sec. 246).	
26,001 lbs. to 29,000 lbs.	125.00		

Trailers

The fee is $5 for a gross weight not over 2,000 lbs. Trailers with a gross weight of 2,000 lbs. or more shall be rated as trucks. Boat trailers registered for between 2,000 and 4,000 lbs. gross weight pay $5 and camp trailers over 2,000 lbs. gross weight pay $10 (Ch. 589, Laws 1975; Tit, 29, Sec. 244).

Tractors

Equipped with:	Per H. P.	Per 100 lbs. Weight
Pneumatic tires	$0.25	$0.25
Solid rubber tires	.25	.50
Iron, steel or other hard tires	.25	.80

Minimum fee, $2. Tractors used for agricultural purposes or not customarily used on public ways pay a fee of $2. Caterpillar tractors, except as above provided, pay a fee of $15. Tractors used to transport loads are rated as trucks (Tit. 29, Sec. 243).

MISCELLANEOUS

School Bus Safety Inspection Fee.—$2 (Tit. 29, Sec. 2011).

Semi-Trailers.—$10 per plate; replacement, $5 (Ch. 589, Laws 1975; Tit. 29, Secs. 241, 245).

Six-Year Semi-Permanent Registration Plates for Semi-Trailers.—$10 per year to the end of the six year term (Ch. 589, Laws 1975; Tit. 29, Sec. 245-A).

Farm Tractor Trailers.—Maximum fee of $2 when operated under certain conditions by farmers (Tit. 29, Sec. 244).

Motorcycles.—$10 (Ch. 589, Laws 1975; Tit. 29, Sec. 249).

Antique Vehicles.—$7.50 (Tit. 29, Sec. 247).

Specially Initialed Plates.—$10 (Ch. 589, Laws 1975; Tit. 29, Sec. 192).

Operator's License.—Application, $5; first examination (Class 1 or 2 license), $[illegible], thereafter, $5; first examination (Class 3 license), $5, thereafter, $3 (Ch. 589, Laws 1975; Tit. 29, Secs. 539, 582).

Transfer of Registration.—$5 (Ch. 589, Laws 1975; Tit. 29, Sec. 152).

Stock Race Cars.—$5 for plates (Tit. 29, Sec. 248).

Application for First Certificate of Title Including Security Interest.—$4 (Ch. 166, Laws 1975; Tit. 29, Sec. 2352).

Each Subsequent Security Interest Noted on a Certificate of Title.—$1 (Ch. 166, Laws 1975; Tit. 29, Sec. 2352).

Each Certificate of Title After a Transfer.—$3 (Tit. 29, Sec. 2352).

Dealers

Any person engaging in the business of buying, selling or offering for sale any vehicle must be licensed. Licenses expire December 31 following issuance (Tit. 29, Sec. 342). The initial application fee is $20 (Tit. 29, Sec. 344). An annual license fee of $30 is provided for every license, except as provided below, and an annual plate fee of $15 each is set with a half-rate reduction in effect between September 1 and December 31 (Tit. 29, Sec. 347). The annual registration fee for motorcycle, boat or snowmobile trailer dealers is $10 plus $5 per plate and $1 ($2 for boat and snowmobile trailer dealers) for replacement of lost or mutilated plates (Tit. 29, Secs. 357, 358). The fee for transporter's and loaner's registration certificates is $25 plus $10 per plate (Tit. 29, Secs. 360, 361).

Common Carrier Fees

¶ 50-495

Property Carriers Subject to Tax.—Every common carrier of property, including special or chartered carriers of passengers, must obtain a certificate, and every contract carrier of property must obtain a permit from the Public Utilities Commission. Certificates and permits must be renewed annually on or before March 1. Application fees for certificates and permits are $25. The fee for application for amendment or transfer of a certificate or permit or the reopening of a hearing is $10. The Commission will furnish an identification device at a fee of $5 for each straight truck and a fee of $10 for each truck tractor. A $2 fee is fixed for transfer of identification (Tit. 35, Secs. 1552, 1557).

Carriers of Passengers.—Application for an original certificate shall be accompanied by a fee of $25; yearly renewals and amendments requiring a public hearing, by a fee of $15; and transfer of a certificate, by a fee of $15 (Tit. 35, Sec. 1501).

B. ANALYSIS

1. Economic effect

The economic importance of such taxes cannot be underestimated. Time and time again a prime factor in Maine's business climate has been identified as the cost of transportation of goods to and from the market place. The revenues of these taxes are dedicated to the Transportation Fund.

2. Yield

a. The yield of these taxes - which is entirely dedicated to the Highway Fund - is approximately $52 million per year or 7.3% (in 1976) of the total state and local tax structure

b. Elasticity. Demand for motor vehicle fuel is not greatly influenced by increased taxes. Thus, demand is inelastic.

3. Equity

Because rich and poor usually pay the same, most of these taxes are regressive. This is the major stumbling block to any conservation policy through increased taxation. How can you raise taxes sufficiently to cut demand without being unfair to the poor person who must drive to his job?

C. POSSIBLE AREAS OF REFORM

1. In order to improve the business climate, a tax rebate, administered through the income tax system, for Maine businesses which transport goods long distances.

2. A tax rebate, administered through the income tax system, for low income commuters.

3. Make the proceeds from these taxes into General Fund dollars and thus more carefully scrutinize their appropriation.

A. MAINE VEHICLE EXCISE TAX

The following description is taken from the Commerce Clearing House publication, State Tax Guide (2nd edition):

¶ 50-490

Privilege of Operating on the Highways.—All vehicles operating on the highways must pay an excise tax based on maker's list price as a condition precedent to registration. If the person seeking to pay the tax owned the vehicle (other than an automobile) on or before April 1, the tax is due before property taxes for the year are committed to the collector. If the vehicle (other than an automobile) is acquired or brought into Maine after April 1, the tax may be paid at any time. Excise tax payments for 1975 for automobiles are as follows (Tit. 36, Secs. 1482, 1486):

Last Letter	Last Digit	Months of Excise Tax Payment	Expiration of Excise Tax Payment
	0	10	October 31, 1975
A, J	1	11	November 30, 1975
B, K, S	2	12	December 31, 1975
C, L, T	3	13	January 31, 1976
D, M, U	4	14	February 28, 1976
E, N, V, F, O, W	5 or 6	15	March 31, 1976
G, P, X	7	16	April 30, 1976
H, Q, Y	8	17	May 31, 1976
I, R, Z	9	18	June 30, 1976

Thereafter, the tax is due annually prior to registration. On new registrations beginning in 1975, the tax is due prior to registration and is for a one year period from the registration date. Beginning in 1975, when the tax is for 12 months or less it is prorated by dividing the number of months the tax is to be paid by 12 and multiplying the result by the mill rate provided for the appropriate model year. The tax is one-half from November 1 to the last day of February following, except that on two or three axle farm trucks it is one-half the full fee during the last six months of the registration year, and on automobiles it is one-half the full fee during the last four months of a registration year (Ch. 765, Laws 1976, 1st Spec. Sess.; Tit. 36, Sec. 1482). Payment of this tax exempts owner from further taxation on the vehicle (Tit. 36, Sec. 1485). Motor trucks or trailers engaging in interstate commerce are exempt, as are nonresident vehicles which are permited to operate under reciprocity provisions and vehicles owned and used by religious houses or societies (Tit. 36, Sec. 1483). A like tax applies to aircraft. The tax is as follows (Tit. 36, Sec. 1482).

Year	Mills per $1 of List Price: Motor Vehicles	Aircraft	Year	Mills per $1 of List Price: Motor Vehicles	Aircraft
First or current year	24	13	Fourth	10	7
Second	17½	11	Fifth	6½	5
Third	13½	9	Sixth and succeeding years	4	3

Minimum tax, $5; on aircraft, $10; maximum, for automobiles but not a bus or motor home, after 7th year, $15.

Transfer of credit to another vehicle.—$1.

Bicycles, motor attached.—$2.50.

Stock race cars.—Plates, $5; excise, $5 (Tit. 36, Sec. 1482).

Mobile Homes.—Mobile homes operated on public roads are subject to an excise tax (minimum tax, $15) at the following rates, before commitment of property taxes to the collector, as a condition of registration. Otherwise, the owner must pay a personal property tax. Camp trailers, same fees except minimum $5 (Ch. 252, Laws 1975; Tit. 36, Sec. 1482):

Year	Mills per $1 of Maker's List Price	Year	Mills per $1 of Maker's List Price
First or current year	25	Third	16
Second	20	Fourth and succeeding years	12

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 52-000.

The revenues of this tax are kept at the municipal level for local expenses.

MISCELLANEOUS PERSONAL TAXES

The following taxes are briefly described:

1. The real estate transfer tax
2. Oil terminal facility fee
3. Pari-mutual taxes
4. Hunting and fishing licenses
5. Spruce budworm excise tax

A. REAL ESTATE TRANSFER TAX

The following description is from the Commerce Clearing House publication, State Tax Guide (2nd edition).

¶ 56-486 **Realty Transfer Tax**

Transfers Subject to Tax.—A tax is imposed on the privilege of transferring title to real property. The grantor is liable for the tax (Ch. 572, Laws 1975; Tit. 36, Sec. 4641-A).

Exemptions.—The following deeds are exempt (Tit. 36, Sec. 4641-C):

1. deeds to property acquired by the U. S., Maine or any of their instrumentalities, agencies or subdivisions.
2. mortgage deeds, discharges of mortgage deeds and partial releases of mortgage deeds (Ch. 655, Laws 1976, 1st Spec. Sess.).
3. deeds of partition.
4. deeds made pursuant to mergers of corporations.
5. deeds by a subsidiary corporation to its parent corporation for no consideration other than cancellation or surrender of the subsidiary's stock.
6. deeds which, without additional consideration, confirm, correct, modify or supplement previously recorded deeds (Ch. 572, Laws 1975).
7. tax deeds; deeds between a husband and wife or parent and child without consideration (Ch. 572, Laws 1975).

Rate.—The tax rate is 55¢ per $500 or fractional part (Ch. 572, Laws 1975; Tit. 36, Sec. 4641-A).

Reports.—No reports are required but a declaration of consideration must accompany each deed, mortgage or mortgage discharge when offered for recording (Ch. 655, Laws 1976, 1st Spec. Sess.; Ch. 572, Laws 1975; Tit. 36, Sec. 4641-D).

Collection.—Tax payment is evidenced by affixing indicia, prepared by the State Tax Assessor, to the declaration of value (Ch. 572, Laws 1975; Tit. 36, Sec. 4641-B).

Source.—References are to the Maine Revised Statutes of 1964, Ch. 711-A, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 34-001.

Each register of deeds shall, on or before the 10th day of each month, pay over to the State Tax Assessor 85% of the tax collected during the previous month. The remaining 15% shall be retained for the county by the register of deeds and accounted for to the county treasurer as reimbursement for services rendered by the county in collecting the tax.

B. ANALYSIS

C. POSSIBLE AREAS OF REFORM

1. A land tax to discourage speculation in real estate. The 108th Legislature defeated LD 942, which imposed a tax on the gains from the exchange of land in Maine. Such a tax, which lessened in rate the longer a person held the land, was designed to discourage investors and developers from buying land and then quickly selling it again.

A. OIL TERMINAL FACILITY FEE

The following description is from the Commerce Clearing House publication: State Tax Guide (2nd edition):

¶ 30-486

Persons Subject to Tax.—Persons operating an oil terminal facility must secure a license from the Environmental Improvement Commission. Licenses are issued annually, expiring December 31. Licenses are not required of marinas servicing pleasure craft, fishing boats and other commercial vessels when the purchaser and consumer are the same and the serviced vessel is 75 feet or less in overall length (Sec. 545). "Oil terminal facility" does not include any facility handling no more than 500 barrels of oil nor any facility not engaged in transferring petroleum products (Sec. 542).

Rates.—The annual license fee is ½¢ per barrel transferred (Sec. 551). However, the fee is ¾¢ per barrel whenever bonds issued to cover contingencies in an oil pollution disaster are outstanding and funds available for interest and retirement are inadequate (Ch. 379, Laws 1975). The fee may be reduced below ½¢ per barrel when the Maine Coastal Protection Fund reaches $4,000,000 and funds for the bonds are adequate (Sec. 551).

Collection.—License fees are paid to the Commission monthly (Sec. 551).

Source.—References are to the Maine Revised Statutes Annotated, Title 38. Complete details are reported in CCH Maine Tax Reporter at ¶ 31-095.

A. PARI-MUTUAL TAX

The following description is taken from the Legislative Finance Office publication, Compendium of State Fiscal Information:

PARI-MUTUEL REVENUE

Harness Racing (Adopted 1935) - M.R.S.A. Title 8

Each person, association or corporation licensed to conduct a race or race meet under the provisions of this Chapter shall pay to the Treasurer of the State, to be credited to the General Fund of the State, a sum equal to 5% of the total contributions to all pari-mutuel pools conducted at any race meet.

A sum equal to 1/5 of the tax on all pari-mutuel pools shall be returned to the licensees for supplementary purse money.

A sum equal to 1% of total contributions shall go to the "Stipend Fund" for Agricultural Fair Association purposes.

Note: Thus the State receives actually 4% of the total contributions to pari-mutuel pools for general fund revenue.

Amended in 1957 increasing tax from 5-1/2% to 6% in total and 1/2% to 1% - amended in 1961 providing an amount equal to 1/6 of the tax to be returned to licensee.

Amended 1973 from 6% to 5% with 1/5 of the tax collected to be returned to licensees.

A. HUNTING AND FISHING FEES

The following description is taken from the Legislative Finance Office publication, Compendium of State Fiscal Information:

HUNTING AND FISHING LICENSES (Adopted 1917 - 1920) - M.R.S.A. Title 12

Resident fishing license	$ 7.50
Resident hunting license	7.50
Resident combination license	12.50
Jr. Resident hunting license (10-16 years)	1.50
Nonresident big game (bear or deer)	60.50
Nonresident small game	30.50
Jr. Nonresident small game (10-16 years)	15.50
Pheasant stamp	3.25
Resident or nonresident fishing (3 days)	7.50
Nonresident fishing (7 days)	12.50
Nonresident fishing (15 days)	15.50
Nonresident fishing (season)	25.50
Jr. nonresident fishing (12-16 years)	4.00
Trapping state-wide	13.00
Nonresident trapping license	250.00
Camp license (boys & girls), Blanket fee	$38, $63, $94
Guides license - resident	32.00
Guides license - nonresident	125.00
Archery deer hunting - resident	7.50
Archery deer hunting - nonresident	60.50
Snowmobile license (resident and nonresident)	11.25
Snowmobile dealers fees (2 dealer plates)	25.00 plus $10 for each additional plate
Watercraft registration	5.00
Watercraft registration - dealer	10.00

Note:

Above fees for licenses include 50 cents agents fee charged by the municipalities for issuing these licenses.

First record indicates 1899 - special license permitting second deer in September - $4.00
Adopted 1917 - nonresident fishing license - $2.00
Adopted 1919 - first resident hunting & fishing license - 25 cents (lifetime license)
Adopted 1920 - nonresident hunting license - $15.00
(Since then laws have been revised to present status as shown by above schedule.)

Of the resident snowmobile license fee, $4.75 goes to Fish and Game for administration, a safety program and enforcement, 50 cents to the Park Commission for marking or clearing trails and providing educational and informational material, and $6.00 goes to the municipality of the owner's residence. Of the nonresident snowmobile license fee, $4.75 goes to Fish and Game, 50 cents to Parks and Recreation Snowmobile Trail Fund and balance to the Department.

A. SPRUCE BUDWORM TAX

The following description is taken from the Legislative Finance Office publication, Compendium of State Fiscal Information:

SPRUCE BUDWORM EXCISE TAX - Enacted by Chapter 764, P.L. 1975

There is established a Spruce Fir Forest Protection District consisting of each of the municipalities and townships within the State in which the softwood forest cover is to a substantial extent composed of species of spruce and fir trees and wherein such spruce and fir is now, or may reasonably be expected to become, subject to infestation and destruction by spruce budworm insects.

Persons owning parcels of forest land, including those claiming timber and grass rights on public reserved lands, which are classified as forest land pursuant to Title 36, chapter 105, subchapter II-A, of more than 500 acres within the Spruce Fir Forest Protection District, shall be subject to an excise tax for the privilege of owning and operating such forest land in 1976 and the 5 years thereafter, unless the Legislature establishes an alternative method of taxation after 1976.

The excise tax rate shall be calculated so as to provide revenue sufficient to pay the percentage of the total costs of spruce budworm suppression activities and spray projects for each year in which the Legislature has determined that a portion of the costs shall accrue from excise taxes on softwood and mixed wood within the Spruce Fir Forest Protection District. Each acre of forest land shall be subject to such tax, provided that each acre classified as mixed wood shall be taxed at half the rate for acres of softwood and that no acre classified as hardwood shall be subject to taxation under this subchapter.

The excise tax on parcels of softwood forest land shall be 56 cents per acre for the year 1976. The excise tax on parcels of mixed wood forest land shall be 28 cents per acre for the year 1976.

STATE OF MAINE

ONE HUNDRED AND EIGHTH LEGISLATURE

COMMITTEE ON TAXATION

MAINE TAX STRUCTURE

Description of Areas of Possible Reform

This study, prepared by the Legislative Joint Committee on Taxation, is meant to be a constantly updated analysis of Maine taxes and policy issues. Further, it offers with each tax analysis a listing of commonly voiced areas of reform. The Committee on Taxation does not necessarily endorse any of these reform suggestions; indeed, some of them are contradictory. Rather, it offers them for public debate. If any Legislator wishes to further pursue any specific tax reform measure, please contact the Office of Legislative Assistants, Room 427, State House.

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PART II
INTRODUCTION TO BUSINESS TAXATION

There are a number of taxes levied on business in every state in the county. These taxes include property taxes, sales taxes on machinery and equipment purchased, inventory taxes, unemployment compensation taxes, social security taxes, and corporate income taxes. Most business taxes are not levied according to the principle of the "ability to pay". Most states rely on property taxes for the greatest portion of tax revenues. In Maine, nearly 40 percent of tax revenues in the State is derived from the property tax.

The corporate income tax, which is the only tax levied on the net income of firms, provided 20 percent of federal tax revenues and 3 percent of the tax revenues of the several states in 1972.[1/] In Maine, the corporate income tax is expected to provide 4 percent of State tax revenues in 1975-76, but the percentage of corporate tax revenues in Maine may drop for the 1976-77 fiscal year. The 1975-76 corporate tax revenues will represent a "one-time" increase which is the result of the recently instituted quarterly payment system.

The federal corporate income tax and many state corporate income taxes, including Maine's, are only slightly progressive. Both the federal and state corporate income taxes, in a majority of cases, are nearly proportionate taxes which levy one, two, or three flat rates on business net income. For the most part, federal and state corporate income taxes levy a much heavier tax burden on low income firms than high profit enterprise.

While most states and municipalities rely more on property taxes levied on business for revenues than business income taxes, many states exempt business enterprise from various types of property taxes. Maine, for example, is gradually phasing out the inventory tax. Some states exempt machinery and equipment as well as certain types of raw materials from property taxes. Despite the property exemptions, however, the property tax is the most onerous burden levied on corporations as well as individuals.

Maine has one of the lowest corporate income taxes East of the Mississippi River. Nevertheless, the Pine Tree State relies more heavily on property tax revenues from business firms than most states in the East. As a result, the tax climate index rating in Maine for business is one of the highest ratings in the East. The Pine Tree State therefore, ranks behind most other Eastern states in terms of a business tax structure that reflects the firms' ability to pay.[2/]

1/ United States Department of Commerce, Bureau of the Census, <u>Statistical Abstract of the United States; 1974</u>, (95th Edition), Table No. 4-12, "General Revenue of State and Local Governments, 1972", Washington, D.C. P. 254. Hereafter referred to as Statistical Abstract of the United States, 1974.

2/ <u>See</u> Table B on Page 10

Despite the controversy and problems over business taxation, evidence indicates that business taxes do not have an impact on or are of only secondary significance in regard to locational decisions of business firms. Most business enterprise is more concerned about the distance from the market, availability and cost of investment capital, transportation facilities, environmental laws, etc., than with business taxes.[3/]

A state which levies a small number of taxes with low rates may inhibit many firms from locating in such a state. A limited tax base and limited tax revenues may connote inadequate public service facilities to industry such as roads, schools, housing etc.. Firms emphasize the need for public service facilities in order to attract top level management and a productive labor force.

A. THE CORPORATE INCOME TAX IN GENERAL

1. Background

The income tax became a part of the U.S. revenue system in 1914. It was promoted initially by the Populists and the Progressives between 1890 and 1916 as a "progressive" measure to raise revenues for public use. Prior to the federal income tax, the U.S. tariff, levied on foreign imports, provided most of the federal government's revenues.

The adoption of the federal income tax in 1914 was the result, in part, of the efforts of big business. Facing strong public criticism and fearful of the outcome of the progressive movement, big business leaders became involved in the movement and soon controlled parts of it. The corporate income tax therefore, was devised by the leading corporation officials and not by the public.4/

Initially the corporate and personal income taxes produced limited revenues. In 1916, for example, the corporate income tax was levied on 340,000 corporations and produced $57,000,000 or 11.1 percent of total tax revenues. In 1970 1,700,000 corporations paid $33,294,000,000 in corporate income taxes or 16.4 percent of the total tax revenues collected by the federal government.5/ Thus federal tax revenues have increased 38,222 percent between 1916 and 1970, and corporate tax revenues collected by the federal government have increased 61,403 percent between 1916 and 1970. The federal corpor-

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3/ Tax Institute of American, State and Local Taxes on Business
4/ Gabriel Kolko, The Trumph of Conservation, (New York: The Macmillan Co.) and Robert H. Wiabe, The Search For Order, 1877-1920, (New York: Hill and Wang), 1967
5/ United States Department of Commerce, Bureau of the Census, Historical Statistics of the United States; Colonial Times to 1956, "Series Y 280-291, Corporation Income Tax Returns: 1909-1957", Washington, D.C., 1960, p.713, 714. Hereafter referred to as Historical Statistics of the United States; Colonial Times To 1957.
Statistical Abstract of the United States, 1974, Table No. 368, "Internal Revenue Collections, By Selected Sources: 1965-1973", P. 226

ate income tax is levied on the net income of corporations at rates of 22 percent on the initial $25,000 and 48 percent on the excess. Congressional tax relief has temporarily raised the net income taxed at 22 percent from $25,000 to $50,000.

While the federal government instituted the personal and corporate income taxes early in the 20th Century, the states did not levy income taxes on individuals and corporations to any significant degree until the 1960's. The states have relied primarily on property taxes, as the basis of state and local taxation. In 1972, 46 states levied a corporate income tax which produced $4,416,000,000 in revenues compared to $15,237,000,000 from personal income taxes, $42,133,000,000 from property taxes, and $37,488,000,000 from sales taxes. Corporate income taxes accounted for 2.9 percent of total state revenues in 1972 compared to 1.2 percent in 1922. Property taxes, on the other hand, accounted for nearly 40 percent of all state and local tax revenues in 1972.[6/]

Most states impose income taxes upon corporations at flat rates ranging from 3 percent to 12 percent. Several states, however, have adopted the graduated basis of rates for corporations including Arizona, Arkansas, North Dakota, and Wisconsin.

2. Corporate Income Tax Theory

There are several income tax alternatives that can be levied on corporations. The alternatives include a tax levied on net profits, corporate dividends, net profits and dividends, or undistributed profits. The most equitable tax and one that would best reflect the ability to pay is the net profits tax. The net profits tax, however, in many cases cannot be apportioned among the several states in which the profits were derived. The other alternatives either fail to tax a substantial portion of corporate revenues or they discriminate against certain types of income compared to other types of income.

As a result, the federal government and the states which levy a corporate income tax utilize net income as the basis of the tax. Net income many be defined as the difference between gross income and authorized deductions.

6/ Statistical Abstract of the United States, 1974, Table No. 408, "Summary of State and Local Government Finances: 1950-1972", P. 251, Historical Statistics of the United States: Colonial Times to 1957, Series Y517-535, "State and Local Government Revenues by Source: 1902-1957", P. 726.

3. Taxation of Corporations By The Several States

Approximately 25 states have adopted the Uniform Division of Income Tax Purposes Act (UDIPTA). The UDIPTA establishes a model apportionment formula for apportioning corporate income derived from several states. The UDIPTA standard utilizes a three factor equation which includes property, payroll, and sales factors to measure and tax the income of a corporation in each state. The UDIPTA model does not include, interest, dividends, capital gains, rentals, etc. in the apportionment of income. Some states allocate this income specifically by statute. 7/

One variation of the UDIPTA model is the Michigan approach which weighs the sales factor 50 percent and the property and payroll factors are each weighed 25 percent. The Michigan adoption of the UDIPTA formula works very well in states in which sales of goods are extensive, and corporations have little property and a small payroll compared to sales. States which may be described as producing states, such as Maine, in which sales do not comprise a much greater percentage of income compared to property and payroll, the Michigan Model does not work well.

Although the UDIPTA model has been adopted by 25 states and used as a general guide in a number of others, there are several differences between the corporate income tax structures of the several states. The basic difference between the corporate income tax policies of the various states lies primarily in the definition of total receipts of gross income. Some states exclude certain types of receipts from gross income and some states prohibit exclusions. 8/

7/ New Jersey Tax Policy Committee, Report of the New Jersey Tax Policy Committee, Part V., "Non-Property Taxes In A Fair And Equitable Tax System", Trenton, N.J., 1972, P. Hereafter referred to as The New Jersey Tax Policy Committee Report.

8/ Ibid, P.
The most common types of exclusions of receipts allowed by the various states include: (1) capital gains or a percentage thereof, (2) proceeds from life insurance policies, (3) gifts, devises, or bequests, (4) interest on state obligations, (5) some dividends, (6) income exempt under federal provisions, (7) insurance benefits for personal injuries or sickness.

In addition to exclusions, many states permit deductions from gross income to determine net taxable income. The following items, with numerous variations among the states, comprise the most common types of deductions: (1) interest paid or accrued (2) taxes, (3) uninsured losses, (4) bad debts, (5) depreciation on plant and equipment, (6) ordinary and necessary expenses incurred in the conduct of business, (7) charitable, educational, and religious gifts, (8) net loss carryovers, (9) dividends from income already taxed, and (10) contributions to employees' trusts.

Corporate income tax law in the several states differentiates between types of corporations, income, and exclusions which has encouraged a number of firms and 18 states, including Alabama, Florida, Idaho and Missouri to standardize state tax laws in regard to corporations. These states have formed the Multi-State Compact which is designed to establish complete uniformity in regard to state corporation law and regulations, the measurement of corporate income, and the apportment of corporate net income to each state.[9/] The strongest advocates of the Multi-State Compact are the Multistate corporations which are critical of the complexity and diversity of state corporate income tax laws. Multistate corporations have discovered that uniform corporate income tax laws and standards greatly simplify the tax process for each firm.[10/]

None of the New England States have joined the Multi-State Tax Compact (MTC), which is basically composed of Western states and a few Southern states. One major drawback to the MTC is the inability of the states to conduct audits of corporations. A joint auditing team conducts the audit which is used by each state.

The Multi-State Tax Compact definition of business income limits the revenues that can be derived from taxing corporations without raising tax rates. Many states define revenue that is categorized as non-business revenues by the MTC as business income which creates a higher taxable income figure for tax purposes.[11/]

4. <u>The Corporate Income Tax In New England</u>

The following Table A compares Maine with the other New England States and the United States in regard to corporate income tax rates and revenues.[12/]

Compared to the other New England States, Maine's corporate income taxes are the lowest in the region. The five other New England States not only require greater tax revenues than Maine, they also require corporations to contribute via the income tax a much larger percentage of the tax revenues than is demanded in the Pine Tree State. Maine's percentage of revenues collected from the corporate income tax is also lower than the national average of 8 percent.

9/ Commercial Clearing House, <u>State Tax Guide</u>
10/ Maine Bureau of Taxation, Corporate Income Tax Division
11/ <u>Ibid</u>.
12/ Commercial Clearing House, <u>State Tax Guide</u>

A Minnesota tax study commission in 1973 analyzed corporate income taxes of the 50 states and applied state taxes to different types of firms. The differences between the firms were limited to differences in property, payroll and sales factors which comprise the UDIPTA equation for apportioning corporate net income to the several states. According to the Minnesota study, Maine ranked consistently in the lowest third (1/3) of all the states in regard to the burden of the income tax on corporations. Maine ranked below all the New England and Northeastern states which indicates that Maine corporations bear the lightest income tax burden compared to a substantial majority of states in the nation.[13/]

There are a number of special features to the corporate income taxes of the other five New England States which are listed as follows:

Connecticut: The Connecticut corporate income tax law taxes corporations at 10 percent of net income. The Connecticut corporate income tax formula follows the federal tax form, for the most part, in regard to deductions except federal taxes on income or profits.

Massachusetts: The Bay State imposes a 14 percent surcharge in addition to the income tax. A net worth tax is applied in conjunction with the income tax. A capital investment excise tax of 8 percent is also imposed on Bay State firms.

New Hampshire: A flat rate Business Profits Tax levied on all firms including proprietorships, partnerships, and corporations.

Rhode Island: Rhode Island provides a minimum alternative net worth tax in its tax law. Corporations pay either a net worth or a net income tax, whichever is higher.

Vermont: Vermont corporate income tax rates are very slightly graduated and range from 5 percent of net income not over $10,000 to 7.5 percent of net income over $250,000. Vermont's corporate income tax rates apply to financial institutions which are taxed differently by most other New England States. Vermont follows the federal form in regard to deductions.

13/ Minnesota Tax Study Commission, Business Tax Comparisons, January 1973, pp.13-33.

6 /1976

TABLE A
A COMPARISON OF INCOME TAX RATES AND REVENUES
BETWEEN MAINE, THE NEW ENGLAND STATES, AND THE U.S. AVERAGE

NAME OF STATE	CORPORATE INCOME TAX RATES	PERCENTAGE OF STATE TAX REVENUES DEPRIVED FROM THE CORPORATE INCOME TAX	CORPORATION INCOME TAX COLLECTIONS AS A PERCENTAGE OF INCOME ORIGINATING IN THE BUSINESS SECTOR
CONNECTICUT	10% OF NET INCOME + 31/100 OF 1 MIL PER 01 OF ASSET VALUE	11.3%	1.2%
MAINE	01-$25,000=5% (federal net taxable income) $25,001 =7%	4.1%	.5%
MASSACHUSETTS	7-1/2% of net income +14% surcharge	13.7%	1.3%
NEW HAMPSHIRE	7% of federal gross business profits	12.1%	.9%
RHODE ISLAND	8% of net income or 40¢ per $100 of net worth (whichever is higher)	9.7%	1.1%
VERMONT	$1-10,000 =5% 10,001-25,000 =6% 25,001-250,000=7% 250,000+=7.5%	4.5%	.7%
UNITED STATES AVERAGF		8%	.9

B. THE CORPORATE INCOME TAX IN MAINE

1. Administration of the Corporate Income Tax

The Maine corporate income tax is very similar to the federal corporate income tax in principle and in its provisions. The Maine corporate income tax is levied on corporate net income derived in Maine at a rate of 5 percent on the initial $25,000 and at a rate of 7 percent on net income in excess of $25,000. The federal income tax levied on corporations is also based on a two flat rate system. Federal corporate income tax rates are 24 percent on the initial 25,000 of net income (temporarily raised to $50,000) and 48 percent on the excess. Both the Maine and the federal corporate income tax laws provide that firms may spread out their losses over a eight year period and extend the losses over the previous three years and the following five years. Thus, a firm which has earned profits for 1972, 1973, and 1974, and realizes a net loss in 1975 can obtain tax rebates for the years 1972-1974 to offset the loss.

Maine's corporate income tax rates have been increased, in part, to compensate communities for their loss of revenue from the phasing out of the inventory tax. Prior to July 1, 1973, the Maine corporate income tax was levied at rates of 3 percent on the initial $25,000 of net income and 5 percent on the excess. Between July 1, 1973 and December 31, 1973, the rates were increased to 4 and 6 percent respectively, and on January 1, 1974, the rates were raised to 5 and 7 percent respectively. In 1974, the Department of Finance and Administration predicted that the increased corporate income tax rates would raise a total of $14,850,000 for the fiscal year July, 1974-June, 1975. The actual revenues collected during that fiscal year were $21,051,684 or roughly $8,000,000 more than 1973 corporate income tax revenues. The expected $30,000,000 in corporate tax revenues for the 1975-76 fiscal year will be the result, in part, of the quarterly payment system which will produce a "one time" gain of nearly $7,000,000.[14]

In general a very small number of firms provide most of the corporate income tax revenues to the State of Maine. Statistics from the Maine Bureau of Taxation reveal that 1.3 percent of all the corporations paying a corporate income tax to the State provide 60 percent (4500 tax paying corporations) of all the corporate tax revenues collected by the State. Eightly percent of all the revenues derived by the State from the corporate income tax are collected from 4.5 percent of all corporations that pay corporate income taxes. Roughly 55 percent of Maine's corporations did not pay a corporate income tax in 1973. Most corporations which do not pay a corporate income tax are very small businesses which incorporate to obtain limited liability protection and other corporation benefits for the owners. The greatest expense of 5,000 non tax paying corporation is salaries which are taxed under the State's personal income tax.[15] See Table B.

14/ Maine Bureau of Taxation, Corporate Income Tax Division.
15/ Ibid

The schedule of tax paying corporations in Maine is not dissimilar to that of tax paying corporations in the United States. Statistics from Statistics of Income, 1970; Corporation Income Tax Returns indicate that 55 percent of income tax paying corporations in the United States provide 1.5 percent of the total corporate income taxes collected by the federal government. Eight percent of income tax paying corporations in the United States provided 50 percent of the corporate income tax revenues of the federal government in 1970.16/

16/ Statistical Abstract of the United States, 1974, Table 791, "Active Corporations by Asset Size: 1950-1971", p. 483. Ibid, Table 793, "Active Corporations-Income Tax Returns by Asset Size and Industry: 1971", p.484.

TABLE B
CORPORATE TAX RETURNS

9/1976

NUMBER OF RETURNS	MAINE TAXABLE INCOME 1973	TAX PAID
4,255	0 - 0	0
1,394	0 - 2,499	52,074
583	2.500 - 4,999	85,412
751	5,000 - 9,999	220,055
475	10,000 - 14,999	233,446
323	15,000 - 19,999	225,152
307	20,000 - 24,999	277,678
222	25,000 - 29,999	245,419
246	30,000 - 39,999	351,474
161	40,000 - 49,999	306,009
116	50,000 - 59,999	277,384
65	60,000 - 69,999	184,954
68	70,000 - 79,999	229,878
55	80,000 - 89,999	213,073
38	90,000 - 99,999	163,425
73	100,000 - 124,999	365,521
50	125,000 - 149,999	307,462
71	150,000 - 199,999	570,250
50	200,000 - 249,999	515,219
31	250,000 - 299,999	386,301
25	300,000 - 349,999	376,602
13	350,000 - 399,999	219,244
18	400,000 - 449,999	356,610
6	450,000 - 499,999	127,433
49	500,000 - 999,999	1,610,634
10	1,000,000 - 1,499,999	543,185
10	1,500.000 - 1,999,999	822,261
7	2,000,000 - 4,499,999	1,047,988
7	4,500,000 - and up	2,669,003
9,479		12,983,146

2. Analysis:

a. Economic Effect

The Advisory Council on Intergovernmental Relations recommends a tax mix in which general income tax (personal and corporate) revenues comprise 20-25 percent of total state tax revenues.[17/] Maine's general income tax revenues comprised 12.4 percent of total state tax revenues in 1974 which was one of the lowest percentages of the 50 states.[18/]

While the corporate income tax rates of Maine are relatively low compared to the nation as a whole, the State's "tax climate index" which measures the burden of taxes on the business sector is higher than any Southern state or any Northeastern state with the exceptions of New York and Massachusetts.[19/] The basic reason for the burdensome tax climate on business in Maine lies with the low corporate and personal income tax rates which are superficially viewed by some people as incentives for industrial development. By levying income taxes at very modest rates, Maine must rely on other taxes, namely, the property tax which is the most onerous of all taxes on business enterprise which creates an favorable tax climate. See Table C.

b. Yield

The Maine corporate income tax yielded $13,000,000 in 1973 compared to $10,000,000 in 1972 and $9,000,000 in 1971. The Income Tax Division of the Bureau of Taxation estimates that corporate income tax revenues for 1974 will have exceeded $21,000,000 and that tax revenues for 1975-76 will be roughly $30,000,000.

17/ Advisory Council on Intergovernmental Relations, Features of Fiscal Federalism, 1974.

18/ Commercial Clearing House, State Tax Guide

19/ Federal Reserve Bank of Boston, Options For Fiscal Structure Reform in Massachusetts, 1975, P. 19

Table C

A COMPARISON OF THE LEVELS OF BUSINESS TAXES IN SELECTED STATES, 1973

Collections as a Percent of Income Originating in the Business Sector

	Corporation Net Income Taxes	Property[1] Taxes	Other Business[2] Taxes	Unemployment Compensation	Total "Tax Climate Index"
U.S. Average	.9	1.9	.8	.8	4.4
Massachusetts	1.3	2.9	.5	1.3	6.0
Other New England States					
Connecticut	1.2	2.1	1.1	1.0	5.5
Maine	.5	3.2	1.0	1.3	6.0
New Hampshire	.9	2.4	.6	.6	4.5
Rhode Island	1.1	2.0	1.1	1.3	5.5
Vermont	.7	3.4	.9	.9	5.9
Industrial States					
California	1.4	2.6	.5	1.2	5.7
Illinois	.6	1.7	.7	.8	3.8
Indiana	.1	1.6	.3	.5	2.5
Michigan	1.1	1.7	.7	1.0	4.5
New Jersey	.7	2.4	.8	1.3	5.2
New York	1.3	3.3	.7	1.0	6.3
Ohio	.5	1.2	1.0	.6	3.3
Pennsylvania	1.3	1.3	1.4	.8	4.8
Wisconsin	1.1	2.6	.5	.7	4.9
Southern States					
Florida	.7	1.0	.6	.3	2.6
Georgia	.9	1.1	.4	.5	2.9
North Carolina	1.1	1.1	1.4	.5	4.1
South Carolina	1.0	1.5	.7	.7	3.9
Texas	–	1.4	1.0	.3	2.7

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[1] Only the business portion of the property tax is included. The apportioning of property was based upon the data in Census of Governments, U.S. Bureau of the Census, 1967.

[2] Other business taxes include sales and gross receipts tax revenue on insurance and public utilities as well as certain license tax revenues.

Sources: Survey of Current Business, No. 8, 1974.
State Tax Collections in 1973 Department of Commerce, Table 3, p. 7; Table 4, p. 8; and Table 5, p. 9.
Governmental Finances in 1972-1973, Bureau of the Census, Table 17,

c. Elasticity

The corporate income tax in Maine is relatively inelastic and therefore, is not significantly affected by economic downturns or upturns. The inelasticity of corporate tax revenues is basically the result of the nature of the Maine economy. Unlike the manufacturing/industrial economies of many other Northeastern states, the Maine economy is more diversified. Agriculture, retail and wholesale trade, and the service industry are subject to a lesser extent to the fluctuations in the national economy than manufacturing firms. Food and kindred products, paper, lumber, and the fishing industry are subject to cutbacks in consumption, but those products are more basic to consumers than other types of manufactured goods. In the same token, Maine products are subject to increased consumption to a lesser extent than the production, in general, of manufactured goods.

Increased revenues from the corporate income tax in Maine for the past two years are the result of increased tax rates, double digit inflation, and increased production for some firms. Thus, while the Maine economy experiences less fluctuations than other Northeastern economics, an accelerated rate of inflation will have an impact on the Pine Tree State. The effect of rapid inflation, however, is greater on industrialized economies than on non-industrialized economies.

Another factor responsible for the relative stability of corporate tax revenues in the State concerns the type of firms that are paying most of the corporate taxes in Maine. Since 1.3 percent of the corporations in Maine provide 60 percent of the corporate tax revenues, these few firms determine the effect of the tax on the State. The utilities, excluding railroad corporations, and the paper companies comprise the largest corporate tax payers in Maine.

The utilities are guaranteeed a minimum rate of return to the stockholders. Thus, a decline in demand or increased operating costs will increase rates, if justified, and thereby raise corporate income for tax purposes. The fuel adjustment clause allows power generating utilities to pass increased fuel costs on to consumers.

While Maine utilities have experienced increased costs and have obtained rate increases, demand for utility services has not declined. During double digit inflation and recession in Maine, 1973-74 for example, residential demand for electricity increased 7 percent and commercial demand for electricity increased 6 percent. Thus, increased rates and increased demand maintained or increased utility tax payments in Maine at a time that industry across the nation suffered significant cut backs in demand and profits.

The pulp and paper companies which are also leading corporate income tax contributors in Maine have a decisive effect on the stability of Maine corporate income tax revenues. According to a U.S. Forest Service Publication entitled The Outlook For Timber in the United States FRR-20,Oct.1973), demand for paper and paperboard has increased over time as a result of the displacement of other materials such as lumber, veneer, metal and glass. The demand for paper has evolved into an inelastic demand which is relatively unaffected by economic upturns and downturns because there are very few substitutes for paper. As petroleum becomes dearer in price and supply, paper may displace plastic which would increase sales of paper firms.

The nature of the leading corporate income taxpayers in Maine therefore, creates relatively inelastic corporate income tax revenues. Maine corporate income tax revenues are affected to a lesser extent by economic upturns and downturns compared to other states because the firms that provide most of the income tax revenues are not subject to the economic fluctuations that other types of enterprise experience.

d. Incidence

Historical statistical studies indicate that the ratio of after-tax profits to assets has remained consistent under significantly different levels and rates of the corporate income tax. These studies suggest the hypothesis that the corporate income tax burden, in the long run, is passed on to consumers and wage earners and not on to stockholders or owners of capital.

In Maine, the premise could be particularly true in respect to utility corporate taxes. Since the utilities are guaranteed a specific minimum rate of return to stockholders, corporate income taxes can be passed on to consumers in the form of higher product costs in order to maintain the minimum rate of return.

The hypothesis discussed above indicates that "firms may treat the corporation income tax as an element of cost and increase prices sufficiently to cover the cost." The hypothesis also assumes that the national and Maine markets are "neither perfectly competitive nor perfectly monopolistic and that firms do not necessarily seek to maximize profits."[20]

20/ Benjamin A. Okner and Joseph A. Peckman, Who Bears the Tax Burden, The Brookings Institution, 1974, pp. 34-35

On the other hand, the classical economists' view that either in a purely competitive or monopolistic economy, firms will seek to maximize profits and that income taxes will not have an effect on pricing decisions, does not appear to be applicable to Maine or the United States. In this case, the income tax would be borne by the owners of capital. The classical economists model may be more valid on the local level or in specific market areas, but the model does not fit the national or state market systems. According to C.E. Ferguson (Microeconomic Theory, Chapter 11, Theories of Price In Oligopoly Markets) the market structure in the United States is basically oligopolistic (a small number of firms dominate the market).[21]

In general, larger corporations can more easily pass the corporate income tax and other taxes paid by corporations on to consumers than small firms. Larger firms which have a dominant role in a market area do not have to worry about price competition as much as small firms.

21/ C.E. Ferguson, Microeconomic Theory, (Homewood: Richard D. Irwin, Inc. 1969), P. 302

e. Equity

The flat rate corporate income tax schedule, such as the Maine corporate income tax and the federal corporate income tax are very mildly progressive, and, in the case of Maine, almost proportionate. In Maine, 3,833 (73.3 percent) corporations of a total number of 5,224 tax paying corporations pay an income tax rate of 5 percent ($25,000 taxable income or less) and 1,391 corporations (26.7 percent) pay an income tax rate of 7 percent for the initial $25,000 of taxable income and 7 percent on the excess. The 73.3 percent of the tax paying corporations with $25,000 or less of taxable income pay 8.9 percent of the total corporate income tax revenues collected in Maine.

While the Maine corporate income tax is mildly progressive and nearly proportionate, the tax is not vertically or horizontally equitable. A firm with a taxable income of $50,000 pays the same rate of tax as a firm with $5,000,000 of taxable income. A firm with several subsidiaries and/or plants of operation with a taxable income of $100,000 pays the same rate of tax as a firm with no subsidiaries or other operating plants and realizing a taxable income of $100,000.

The burden of the Maine corporate income tax on small firms is not unlike the burden of the federal corportate income tax on small or low net income corporate enterprise. Roughly 55 percent of all corporations in the country have assets of less than $100,000 and possess 1.2 percent of the total assets and 0.5 percent of the total net income of all U.S. corporations. Approximately 0.8 percent of all corporations in the nation possess assets of $250,000,000 or more and possess 60 percent of the total net income of all U.S. corporations. A corporation with assets of less than $100,000 which has an annual net income of $35,000, pays the same tax rate as a firm with assets of more than $250,000,000 which has an annual net income of $25,000,000.[22/]

The corporate income tax rates of Maine may encourage some small businesses not to incorporate. Proprietorships and partnerships do not pay a business tax because there is no business tax in Maine. Non-incorporated businesses pay personal or individual income taxes. Maine's personal income tax structure is graduated from 2 percent to 6 percent ($50,000+). A small business therefore, will pay a lower tax on taxable income of $25,000 or less under the personal income tax than under the corporate income tax.

22/ Statistical Abstract of the United Stats, 1974, Table 791, "Active Corporations by Asset Size: 1950-1971",P.483, and Table 793, "Active Corporations - Income Tax Returns by Asset Size and Industry: 1971, P. 484

The federal and state corporate income taxes not only discriminate in favor of high profit firms, these taxes also discriminate in favor of manufacturing firms as opposed to wholesale, retail, and service corporations. According to statistics provided by the First National City Bank study of manufacturing and non-manufacturing corporations in the United States, net income and after-tax profits of manufacturing corporations comparatively exceeded net income and after-tax profits of non-manufacturing firms by roughly 30 percent in 1972 and 1973. Furthermore, total after-tax profits of manufacturing firms increased 53 percent more than total after-tax profits of non-manufacturing corporations between the last quarter of 1972 and the 4th quarter of 1973.[23]

The discriminatory character of the federal and state two flat rate corporate income tax schedules is often justified by the capital investment incentive that the taxes offer high profit firms which tend to be more capital intensive than low profit firms. High profit firms tend to have larger capital investments in machinery, plant, and equipment than low profit firms.

f. Comments

Compared to the corporate income tax schedules of most Northeastern States, including New England, Maine's corporate income tax burden is one of the lightest burdens East of the Mississippi. Unlike a number of other states, however, Maine depends upon the property tax to an extraordinary extent for state and local revenues. As a result, of the magnitude of property taxes levied on Maine business, the business climate index rating of the Pine Tree State is one of the highest in the Northeast. Maine, New York, and Massachusettts are rated roughly equal by the Federal Reserve Bank in regard to the total burden of taxes levied on business.

Since Maine is phasing out the business inventory tax, and because there is no sales tax levied on machinery and equipment, the greatest tax burden must be the property tax levied by local communities on Maine businesses. Maine communities, unlike many communities outside the State, do not levy income taxes which places nearly 100 percent of the local tax burden on the property tax.

While corporate income tax rates are low and property taxes are high, state and local taxes play only a minor consideration in the decisions made by corporations in regard to the location of corporate plants. Firms are more interested in environmental laws, distance to the market, industrial park facilities (sewerage, water,etc.),

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23/ United States Senate, Committee on Finance, Oil Company Profitability, February 12, 1974, pp. 3-4.

transportation facilities, and energy costs in taxes. Furthermore, many firms are interested in the quality of life for their executives and middle management. Taxes are deductible, and most states have special exemptions and deductions to reduce the tax burden.

C. POSSIBLE REFORM AREAS

There are a number of alternatives in regard to the taxation of business in Maine. Tax reform, particularly with respect to small businesses and low profit firms strengthen some small businesses and encourage others to develop. Reformation of the property tax levied on business in Maine could significantly reduce the State high "business tax climate index" rating of the Federal Reserve System.

1. The corporate income tax schedule could be made more progressive and better based on ability to pay by creating more brackets.

A schedule of taxes levied on corporations with rates ranging for example, from 3 percent to 10 percent, is one alternative to the present two flat rate corporate income tax. Low profit firms would be the major beneficiaries of a graduated corporate income tax schedule, and larger firms such as the paper companies, and power generating utilities, would pay higher taxes.

2. The burden of property taxes could be lifted from small corporations and other small businesses by a business property tax circuit breaker.

The most burdensome tax to all firms is the property tax. Property tax relief in the form of a circuit breaker and an increase in corporate income tax rates (which are presently the lowest in the Northeast) would provide tax relief to Maine businesses. At the same time, business firms would be subject to taxation based more on income which is a more accurate indicator of a firm's "ability to pay". A property tax circuit breaker for example, could take effect at the time that the total property taxes of a firm exceed 10 percent of its net revenue. By increasing corporate income tax rates or by creating a graduated tax rate schedule, the revenues lost by Maine communities from the property tax circuit breakers could be offset by increased revenues from the income tax.

3. A general tax cirucit breaker could help the small business overburdened by taxes.

Another alternative to help small businesses and low profit enterprise is the general tax circuit breaker. The general tax circuit breaker would establish a limit beyond which the firm would not be responsible for tax payments. For example, a schedule could be devised that "forgives" or repeals all taxes due that exceed 65 percent of a firm's net income. Another possibility is to establish a graduated schedule of tax relief. For example, 85 percent of a firm's tax burden could be forgiven when tax levies exceed 60 percent of a firm's net income, etc..

4. <u>A business franchise tax could more equitably replace the currently repealed inventory tax.</u>

A business franchise tax levied on all businesses and in place of, or in conjunction with the corporate income tax, would subject all firms to a tax based on net income. Presently proprietorships and partnerships are not taxed under the corporate income tax.

A graduated schedule of tax rates is more desirable than the flat rate system of New Hampshire. The business franchise tax could be levied in lieu of other taxes as well, such as the inventory tax, unemployment compensation tax, and local property tax.

5. <u>Repeal the unemployment compensation tax.</u>

The Unemployment Compensation Tax, levied on businesses according to their history of employment is particularly burdensome to small businesses. By levying a graduated business franchise tax in lieu of the unemployment compensation tax and/or corporate income tax, a more progressive business tax policy would be created. The tax revenues would go to an unemployment compensation fund.

6. <u>Lower the property tax and increase the income tax.</u>

The Governor's Tax Policy's major recommendation (<u>see A Tax Policy For Maine</u>, 24) was that the property tax reflected basically the cost of land-related services and that the cost of education and welfare be shifted to the personal and corporate income tax.

7. <u>Lower the property tax and institute a business franchise tax.</u>

The most regressive tax is the property tax. It is also the major cause for Maine's high business tax climate index rating of the Federal Reserve System. By levying a graduated business franchise tax levied on net income and lowering the Uniform Property Tax an equal amount, the rating would decline, and Maine businesses would obtain significant tax relief. Since property has no direct relationship with a firm's profitability, the property tax is not a "fair" measure of a firm's "ability-to-pay".

TT02 STATE OF MAINE - BUREAU OF TAXATION

CORPORATE MAINE TAXABLE INCOME 08/18/77

	TAXABLE INCOME OF MAINE CORPORATIONS		NUMBER OF CORPORATIONS PAYING COUNT	PERCENTAGE OF THE TOTAL %
I		NEGATIVE	416	4.082
N	0.00 -	0.00	4,737	46.491
C	0.01 -	4,999.99	1,846	18.117
O	5,000.00 -	9,999.99	703	6.899
M	10,000.00 -	14,999.99	447	4.387
E	15,000.00 -	19,999.99	285	2.797
	20,000.00 -	24,999.99	258	2.532
	25,000.00 -	29,999.99	211	2.070
R	30,000.00 -	34,999.99	161	1.580
A	35,000.00 -	39,999.99	115	1.128
N	40,000.00 -	44,999.99	96	0.942
G	45,000.00 -	49,999.99	106	1.040
E	50,000.00 -	59,999.99	152	1.491
	60,000.00 -	69,999.99	89	0.873
	70,000.00 -	79,999.99	62	0.608
	80,000.00 -	89,999.99	53	0.520
	90,000.00 -	99,999.99	47	0.461
	100,000.00 -	149,999.99	121	1.187
	150,000.00 -	199,999.99	75	0.736
	200,000.00 -	249,999.99	36	0.353
	250,000.00 -	299,999.99	37	0.363
	300,000.00 -	349,999.99	18	0.176
	350,000.00 -	399,999.99	21	0.206
	400,000.00 -	449,999.99	11	0.107
	450,000.00 -	499,999.99	11	0.107
	500,000.00 -	599,999.99	15	0.147
	600,000.00 -	699,999.99	8	0.078
	700,000.00 -	799,999.99	6	0.058
	[illegible]	[illegible]	[illegible]	[illegible]

900,000.00 - 999,999.99	4	0.039
1,000,000.00 - 1,999,999.99	21	0.206
2,000,000.00 - 2,999,999.99	6	0.058
3,000,000.00 - 3,999,999.99	5	0.049
4,000,000.00 - 4,999,999.99	1	0.009
5,000,000.00 - 9,999,999.99	4	0.039
10,000,000.00-14,999,999.99	0	0.000
15,000,000.00-19,999,999.99	0	0.000
20,000,000.00- UP	0	0.000
TOTALS	10,189	100.000

1/1976

A. THE UNEMPLOYMENT COMPENSATION TAX IN GENERAL

1. The History of the Tax

The Unemployment Compensation tax was one of several provisions of the 1935 Social Security Act which created several social welfare programs to alleviate social distress during economic downturns and to give working people security following retirement from active employment. The Unemployment Compensation program, in particular, was designed to reduce economic insecurity due to unemployment.

The Social Security Act did not mandate unemployment compensation programs in every state. The federal law, however encouraged the several states to adopt unemployment compensation programs by means of federal taxing power. Employers, according to the Act, were allowed to deduct contributions they pay as a credit against nine-tenths of the tax on the employee's payroll under an approved unemployment compensation insurance law of their state. Within two years, every state had unemployment compensation tax laws.

2. General theory of the Unemployment Compensation Tax

The Unemployment Compensation Tax in Maine is a tax levied on most employers with one or more employees. The tax, for the most part, is levied on the initial $4200 of each employee's salary or wages. Individuals performing agricultural labor, household domestic services, and services for the state or political subdivisions of the state, with some exceptions, are excluded from the provisions of the tax law. Railroad employees are covered with unemployment insurance benefits by the Railroad Retirement Act.

There are two types of unemployment taxes levied on business firms. One tax is determined by each state, and the proceeds are deposited in an unemployment compensation trust fund to be expended exclusively for compensation to unemployed persons. The second tax is a federal tax of 3.2 percent that is levied on the payroll of each firm which, for the most part, is based upon the taxable wage base. If a firm makes timely payments, it will receive a credit of 2.7 percent which establishes an effective rate of 0.5 percent. The revenues from the federal tax are used exclusively to administer the manpower programs of the federal government.

The tax rate that is levied on a particular business is determined by the unemployment compensation funds needed by the state, and by the employment history of the firm. A new business pays the minimum rate for at least 24 months. On December 31st of each year, every new business which has paid the tax for at least 24 months is evaluated, and a new tax rate is assigned to the firm.

The unemployment compensation tax is, in part, a rating of each business in the state. A firm that has a history of growth and/or has a stable employment record will be taxed at a lower rate than a firm that is in a marginal financial position and has an unstable employment record. A well established and stable firm that has been operating for several years will pay a lesser unemployment compensation tax than a relatively new business or one that has had employment problems.

The greater the capital reserve that a firm has built up in the unemployment compensation fund, the lower the tax rate that will be levied on the firm. Thus, a state which has a business base characterized by well-established, stable, and financially secure firms has a lower range of unemployment compensation tax rates than a state with marginal enterprise and unstable employment.

The unemployment compensation tax is also dependent upon the revenue needs of the state to fulfill the unemployment compensation obligations of the state. A state that has a high rate of unemployment as well as a wide range of unemployment benefits and high individual payments must levy a higher unemployment compensation tax rate than a state that does not provide as liberal benefits.

3. Purpose of the Tax In Maine

According to the Maine Law (26 MRSA Chapter 13), the purpose of the unemployment compensation program is to prevent the spread of unemployment "and to lighten its burden which may fall upon the unemployed worker, his family, and the entire community." In order to achieve the objective of the program, the law states:

> This objective can be furthered by operating free public employment offices in affiliation with a nationwide system of public employment services; by devising appropriate methods for reducing the volume of unemployment; and by the systematic accumulation of funds during periods of employment from which benefits may be paid for periods of unemployment, thus maintaining purchasing power, promoting the use of the highest skills of unemployed workers and limiting the serious social consequences of unemployment.

4. The Unemployment Compensation Tax In New England

New England, as a region, tends to have the highest unemployment compensation tax rates in the nation. In 1974-1975, Connecticut, Massachusetts, Rhode Island, Vermont, and Maine were part of the top nine states with the highest unemployment compensation tax rates in the nation. The unemployment compensation tax rates of the six New England states for 1976 are as follows:

STATE	RATE	TAXABLE BASE	YIELD	1974-1975 CORPORATE INCOME TAX REVENUES
Connecticut -	1.5%-6%	$6,000	$126,069,000	140,365,000 13.25%-State Tax Revenues
Maine -	2.4%-5%	$4200	$29,259,000	$30,000,000 65% of State Tax Revenues
Massachusetts-	3.9%-5.1% Plus 0.1%-1% if Reserve less than 0.5%	$4200	$260,593,000	$288,702,000 13.01% of State Tax Revenues
New Hampshire-	2.7%-4%	$4200	$13,081,000	$26,320,000 15.2% of State Tax Revenues
Rhode Island -	3.2%-5% Employees Taxed 1.5% of	$4800 $4800	$39,532,000	36,652,000 10.48% of State Tax Revenues
Vermont -	1.%-5.0%	$4200	$12,033,000	Personal/Corporate Income 65,061,000 34.7% of State Tax Revenues

One reason for the relatively high unemployment compensation tax levied in the New England states in 1974 and 1975 was the effect of the recession upon the New England region. Unemployment in 1975, for example, reached 9.9% in Connecticut, 9.4% in Maine, 12.2% in Rhode Island, and 10.1% in Vermont. Since, the unemployment compensation tax rate is, to a large extent, a function of the degree of unemployment, the tax rate was relatively high in New England in 1975.

Rising unemployment in 1974 and 1975 in New England was due, in part, to the type of enterprise comprising the regional economy. Traditional industries including food processing, textile manufacturing and leather and shoe manufacturing which have experienced economic decline in New England have contributed to higher unemployment compensation taxes in the region. Economic decline of industry in New England can be measured by several standards. Business failures, for example, rose 41 percent in 1975 compared to 1970. Business liabilities rose 736 percent in 1975 compared to 1970. Construction contracts dropped in value 25 percent in 1975 compared to 1970. The migration of firms from New England to other regions has also contributed to rising unemployment and unemployment compensation taxes.

Another variable contributing to the determination of unemployment compensation tax rates is the type of coverage provided. In Rhode Island, for example, individuals on strike receive unemployment compensation benefits.

B. THE UNEMPLOYMENT COMPENSATION TAX IN MAINE

1. Description of how the tax is administered in Maine

The unemployment compensation tax in Maine, as previously described, is levied on employers with one or more employees. The tax is levied on the initial $4200 of each employee's wages. The tax ranges between 2.4 percent and 5 percent of the taxable wage base, and the rate is determined by the employment experience record of the employer.

In 1970, 224,026 employees or 59 percent of the labor force in Maine was covered by the unemployment compensation law. By 1975, nearly 260,000 employees or 66 percent of the state's labor force was protected by unemployment compensation. The increase between 1970 and 1975 was primarily the result of a change in the tax law in 1972 that extended unemployment compensation benefits to employers with one or more employees. Previously, employers with 4 or more employees were the only types of enterprise that were protected by unemployment compensation. Another reason for the increase in the number of individuals covered by the tax law is the extension of coverage to employees in state institutions and State institutions of higher education.

While two-thirds of the labor force is protected by unemployment compensation benefits under the unemployment compensation law, state and local government employees, except employees in state institutions and institutions of higher education, are covered under the Supplementary Unemployment Assistance Program (SUA). The SUA Program operates on the direct reimbursable principle. State and local governments are not taxed for revenues. Instead, state and local governments are charged directly for the amount expended to compensate employees who have become unemployed. The SUA program therefore, increases the percentage from 66 percent to more than 75 percent of the labor force covered by some form of unemployment compensation insurance.

Since the inception of the unemployment compensation tax, both the rates and the taxable wage base have increased. In addition, the number of individuals covered under the law have been increased. The following table describes the change over time.

YEAR	EXTENT OF COVERAGE	TAXABLE WAGE BASE	RATE
1936	Employers with 8 or more employees	100% of earnings	0.9%
1937	Same as above	Same as above	1.8%
1938-1939	Same as above	Same as above	2.7%
1940-1942	Same as above	Tax levied on the initial $3000 of each persons wages	2.7%
1943-1944	Same as above	Initial $3,000 of wages	1.5-2.7%-Experience Rating Created
1945-1946	Same as above	Initial $3,000 of wages	1.2-2.7%
1946-1956	Same as above	Initial $3,000 of wages	0.9-2.7%
1957-1959	Same as above	Initial $3,000 of wages	0.5-2.7%
1960-1964	Employers with 4 or more employees	Initial $3,000 of wages	0.5-2.7%
1965-1971	Same as above	Initial $3,000 of wages	0.5-3.7%
1972	Employers with 1 or more employees	Initial $4200 of wages	0.5-4.5%
1974	Same as above	Initial $4200 of wages	1.9-4.5%
1975	Same as above	Initial $4200 of wages	2.4-5.0%

2. Analysis

a. Economic Effect

The unemployment compensation tax rates of Maine are relatively high compared to the nation, generally. In 1975, Maine ranked in the upper 14 percent of states with the highest range of tax rates. The minimum tax rate of 2.4 percent in Maine was exceeded by only 6 other states (Hawaii, Massachusetts, Nevada, Puerto Rico, Rhode Island, and Washington). The maximum tax rate of 5.0 percent in Maine was exceeded only by 8 other states including Connecticut, Delaware, Florida, Massachusetts, Michigan, Minnesota, Rhode Island and Vermont.

The unemployment compensation tax tends to injure the business climate of Maine for small business. According to the State Development Office, a significant portion of Maine business is small enterprise which does not provide the amount of revenues that large scale firms produce. As a result, tax rates must be higher in Maine compared to many other states to obtain the revenues required to pay the benefits demanded. Small businesses, therefore, tend to feel the effect of the tax more in Maine than in many other states which results in a poorer business climate for these firms.

b. Yield

The Unemployment Compensation Tax produced $30,589,000 in revenues in 1975 or 200 percent more revenues than were derived in 1970 and 1971. In 1975, the Department of Manpower Affairs paid $53,029,000 in benefits to unemployed persons which represented a 200 percent increase compared to benefits paid in 1970 and 1971. As a result of increased demand for benefits in 1975, the Department of Manpower Affairs was forced to borrow $2,400,000 in federal funds.

c. Elasticity

There is a high correlation between the taxable wage base and tax revenues collected from the Unemployment Compensation Tax. According to the Department of Manpower Affiars, there is also a high correlation between Unemployment Compensation tax revenues, the rate of unemployment, and the business cycle. A lag effect and an inflation factor must be incorporated into the variables to make the correlation.

As a result of the scarcity of data it is very difficult to establish a correlation between unemployment compensation tax revenues, the business cycle of Maine, and the rate of unemployment. It is also very difficult to forecast future revenues based on the data available.

A cursory study of unemployment cycles and tax revenues shows a steady growth in revenues between 1938 and 1971 in Maine. On several occasions, however, the tax base was increased, rates were raised, and the law was changed to incorporate more employers which produced additional revenues.

The Maine business cycle, in general, has experienced less severe troughs and peaks compared to the national business cycle. The type of enterprise comprising the Maine economy, in part, is responsible for the more stable performance of the State economy. Despite the performance of the Maine economy, however, there have been significant variations in the insured unemployment rate which has varied between 2.6 and 10.3 percent between the years 1947-1975.

If there is a high correlation between unemployment and unemployment compensation tax revenues, tax revenues and the unemployment compensation reserve fund may not be adversely affected for a number of years. According to the State Development Office, employment opportunities are expected to be limited through 1979 after which the number of high school graduates will decrease along with the unemployment rate. Employment in manufacturing will increase, but not fast enough to absorb the number of high school graduates through 1979. Employment in education and in eating and drinking establishments which previously have been the fastest growing non-manufacturing employers in Maine has plateaued. Employment in the medical health field which has also been one of the fastest growing non-manufacturing sectors of the Maine economy has also slowed down.

While unemployment is predicted to be high for the next 2 to 3 years in Maine, the State Development Office estimates that the number of job opportunities will increase after 1979. As the birth rate and the number of high school graduates falls and as the number of people leaving the work force increases, job opportunities will increase and exceed the number of job applicants. As a result the reserve fund and unemployment compensation tax revenues are expected to be stable and secure in the future.

During the years 1976-1979, the State Development Office predicts that the high unemployment rate will not adversely affect unemployment compensation tax revenues. The unemployed during these years will be uninsured members of the work force and will consist primarily of recent high school graduates who will not qualify for unemployment compensation.

The unemployment compensation reserve fund and tax revenues therefore, appear to be secure in the future. This assumption is based on a number of variables, however, that are subject to change. For example, a serious energy crisis, national economic recession, industrial migration, etc., could have very serious repercussions on the Maine economy and upon the unemployment compensation reserve fund.

ECONOMIC SECTOR	PERCENT OF TOTAL COVERED EMPLOYEES IN THE STATE	PERCENT OF TOTAL UNEMPLOYMENT COMPENSATION TAXES PAID IN THE STATE	PERCENT OF TOTAL U.C. TAX BENEFITS RECEIVED IN THE STATE
1) Manufacturing	35%	40.2%	54%
2) Wholesale and Retail Trade	18.4%	24.3%	13.9%
3) Services	26.5%	14.0%	8.5%
4) Finance Insurance and Real Estate	5.0%	4.8%	1.7%
5) Transportation Communication, Electric, Gas, Sanitation	5.3%	5.0%	3.50%
6) Construction	6.5%	11.0%	17.0%

A further breakdown of the manufacturing sector shows the industries that received the major portion of the tax benefits in 1975 as follows:

MANUFACTURING INDUSTRY	PERCENT OF TOTAL COVERED EMPLOYEES IN THE STATE	PERCENT OF TOTAL TAXES PAID IN THE STATE	PERCENT OF TOTAL TAX BENEFITS RECEIVED IN THE STATE
1) Food and Kindred Products	3.7%	4.9%	5.2%
2) Textile Mill Products	2.8%	3.4%	5.8%
3) Lumber & Wood Products	4.6%	5.6%	10.9%
4) Paper & Allied Products	6.1%	5.6%	4.5%
5) Leather & Leather Products	6.2%	7.6%	12.3%
6) Electrician Machinery	1.9%	2.2%	5.0%

d. Incidence

According to statistics from the Department of Manpower Affairs, the manufacturing sector provided the largest percentage of unemployment compensation tax funds (40%) collected in Maine in 1975 (See table on page 8.) Four industries in the manufacturing sector provided nearly 51 percent of the revenue collected from manufacturing enterprise as described below:

INDUSTRY	% OF TOTAL TAXES PAID BY MANUFACTURING ENTERPRISE	% OF TOTAL TAX BENEFITS PAID TO MANUFACTURING FIRMS
Food	12.1%	9.6%
Leather	18.8%	22.8%
Lumber & Wood	13.0%	20.3%
Paper	14.0%	8.4%

While manufacturing enterprise contributed 40 percent of the revenues, and four industries in the manufacturing sector provided the major proportion of these contributions, some industries paid more than others because of their employment experience record. In addition, some industries contribute more to the unemployment compensation reserve fund than the number of benefits they receive. The leather and lumber and wood industries, however, contributed less in 1975 to the reserve fund compared to the benefits they received. As a result the tax levied upon the paper and food industries should decline in 1976 while the tax levied on the leather and lumber and wood industries should increase.

e. Equity

The Unemployment Compensation Tax is not based on the principle of "the ability to pay." It is based on the theory that a business pays in taxes in proportion to the liabilities that it incurs. The tax operates as a tax with progressive rates that climb upward for firms with the most unstable employment records.

Thus, according to the principle of the "ability to pay",the Unemployment Compensation tax is very regressive. However, if the theory of equity is based on the business principle that a firm is responsible for its own liabilities, the unemployment compensation tax is very equitable.

Evidence tends to support the theory that more stable, financially secure, and well established firms pay lower tax rates than firms with an unstable employment record and with marginal operations. Furthermore, new businesses following their first evaluation by the Department pay a higher rate than many of Maine's largest, well established, and financially secure firms. A new business which obtains its first rating will pay a minimum tax of 3.9 percent compared to a large paper company which most probably pays a tax rate of 2.2 percent or less.

According to Department Manpower statistics, 77 percent of the agricultural service enterprise, 67 percent of the lodging establishments, 64 percent of the construction firms, 63 percent of the real estate firms, 52 percent of the food stores, 52 percent of the automobile dealers and service stations, and 45 percent of the eating and drinking establishments paid an average unemployment compensation tax rate of 3.5 percent or more during the 1974-75 fiscal years. These types of firms tend to experience cyclical demand and cyclical employment which increases tax rates.

On the other hand, 42 percent of paper and allied product firms, 40 percent of the utilities, 56 percent of the security and commodity brokerage firms, 56 percent of the insurance carriers, and 38 percent of the printing and publishing firms pay unemployment compensation tax rates of 2 percent or less. These firms tend to be more stable and more profitable than the firms paying high unemployment compensation tax rates.

f. Possible Areas of Reform

The following measures could be applied to the unemployment compensation tax. Each measure has advantages and disadvantages associated with it.

1. Extend unemployment compensation tax benefits to all workers.

2. Provide benefits to workers on strike.

3. Levy an excise tax in addition to the unemployment tax upon all businesses for a specified period of time. As soon as an adequate reserve fund is created to meet the most severe economic downturns for a year or 2 year period, the excise tax would be rescinded.

4. Levy a portion of the unemployment tax on workers.

TABLE A
Unemployment Compensation Tax Revenues in Maine, 1938-1975

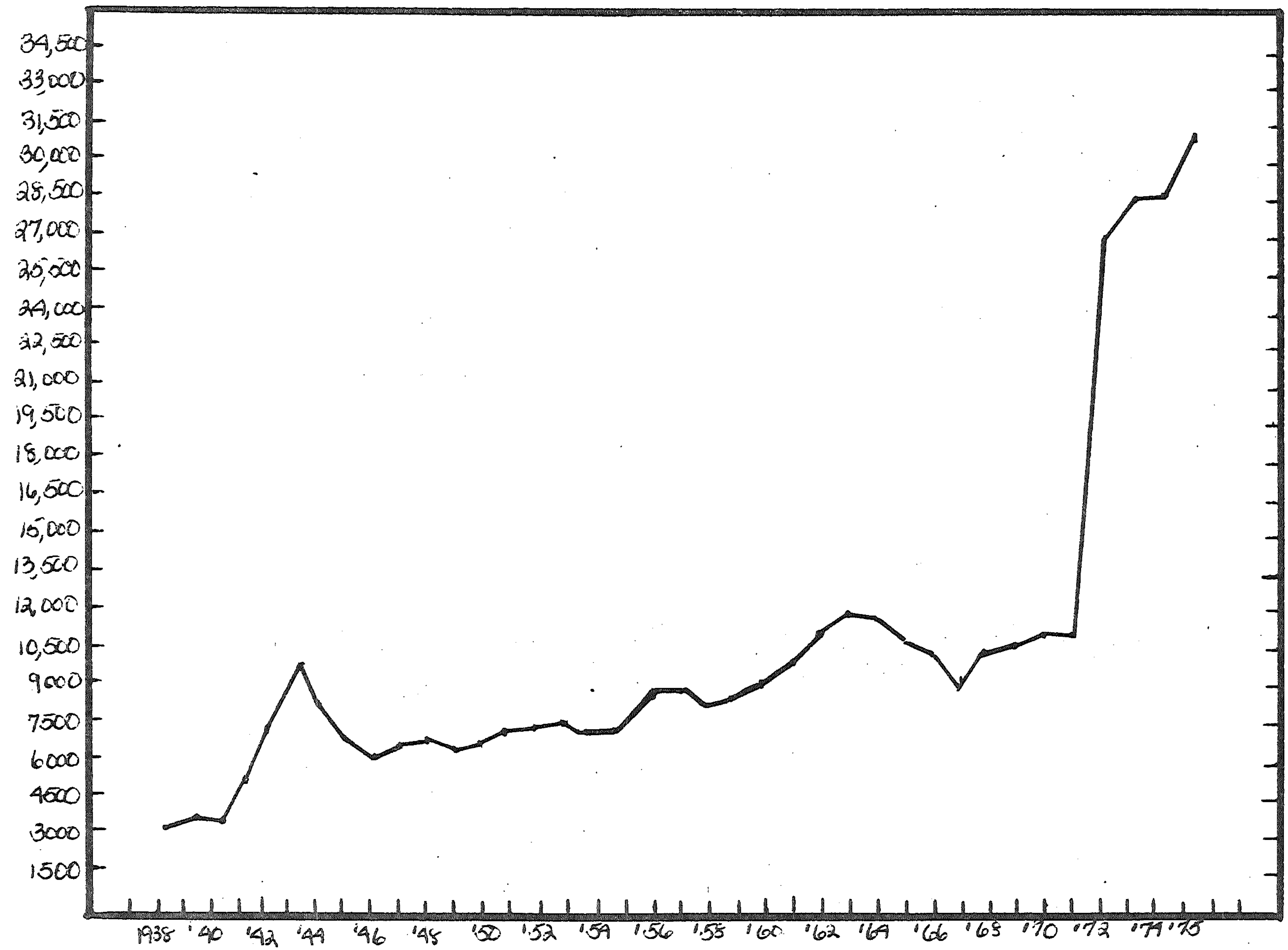
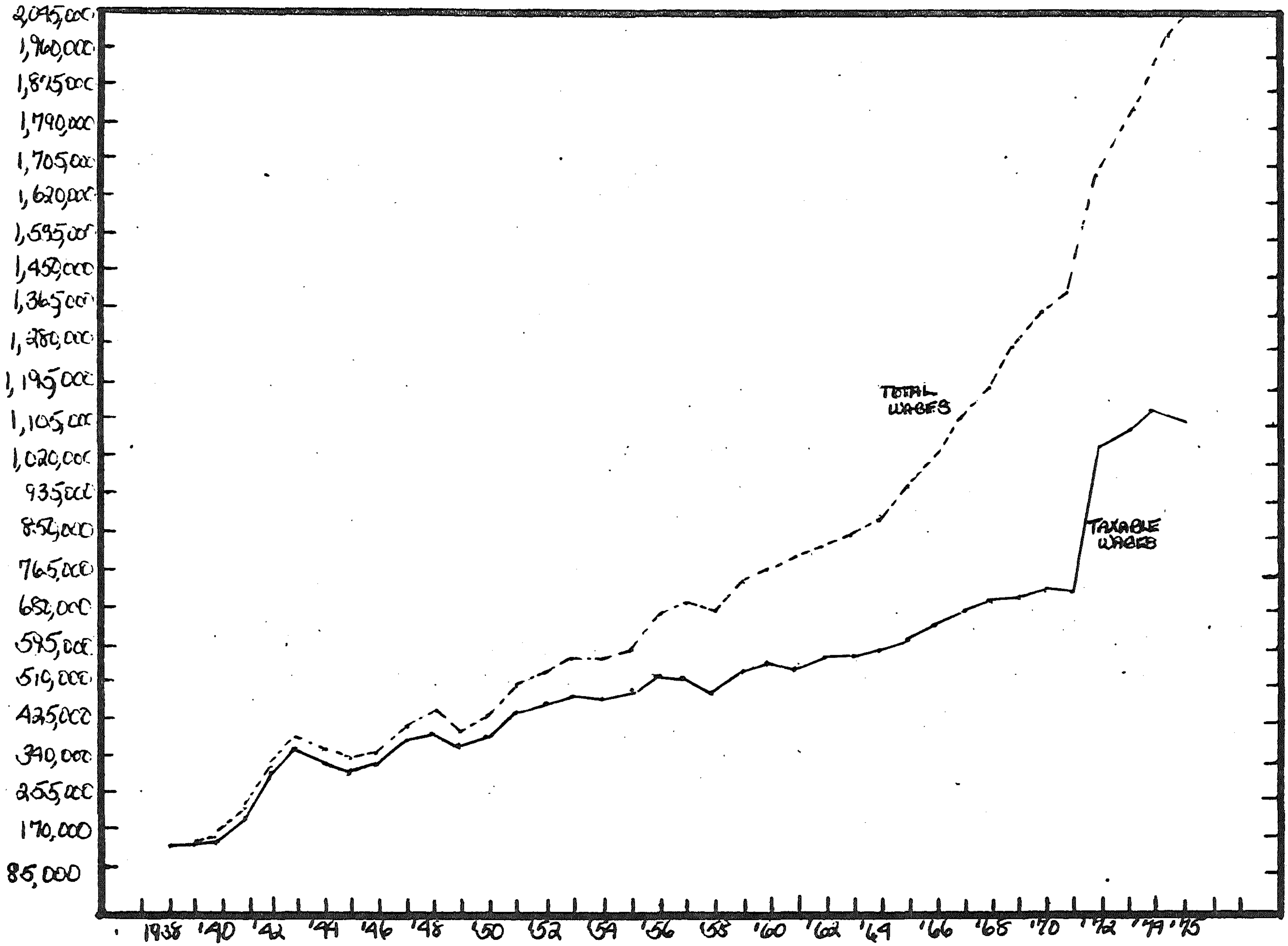


TABLE B

Total Wages and Taxable Wages Under The Unemployment Compensation Tax Law in Maine, 1938-1975



A. PUBLIC UTILITY TAXES

This description is taken from the Commerce Clearing House publication, State Tax Guide (2nd edition):

¶ 80-485

Utilities Subject to Tax.—Telephone, telegraph and railroad corporations are subject to tax (Tit. 36, Secs. 2623, 2683). This railroad tax and the municipal taxes on railroad realty and buildings are in place of all taxes on the railroad and its realty (Tit. 36, Secs. 561, 2623).

All utilities herein listed, except companies operating motor buses for transportation of persons for hire, are exempt from the motor vehicle excise tax (Tit. 36, Sec. 1483).

Basis.—Telephone and telegraph companies pay a tax based on annual gross operating revenues (Tit. 36, Sec. 2684).

The annual excise tax on railroads is computed on the basis of gross transportation receipts within the state as returned to the Public Utilities Commission for year preceding the tax levy as compared with the net railway operating income within the state for that year, except on railroads of not over 50 miles where the tax is based on annual gross transportation receipts (Tit. 36, Sec. 2624).

(SEE ALSO TAX REFORM ISSUES, K-7, in this manual which describes a model public utilities excise tax)

Rates.—(Tit. 36, Secs. 2624, 2684):

Corporations	Annual Rate
Telephone	
Annual gross operating revenues $ 1,000 to $ 5,000	1¼%
Annual gross operating revenues 5,000 to 10,000	1½%
Annual gross operating revenues 10,000 to 20,000	1¾%
Annual gross operating revenues 20,000 to 40,000	2%
For each additional $20,000 or fraction	increase of ¼%
Maximum rate	7%
Telegraph	6%
Railroad	
When annual net railway income exceeds annual transportation receipts by 10% or less	3¼%
When annual net railway income exceeds annual transportation receipts by 10% to 15%	3¾%
When annual net railway income exceeds annual transportation receipts by 15% to 20%	4¼%
When annual net railway income exceeds annual transportation receipts by 20% to 25%	4¾%
When annual net railway income exceeds annual transportation receipts by more than 25%	5¼%
When net railway operating income for the preceding year is less than 5¾% of investment in railway property used in transportation service, less depreciation and plus cash, the tax is decreased by the sum which added to net railway operating income would equal 5¾% of the investment; the tax shall not be decreased below a minimum amount of ¼ of 1% of gross transportation receipts.	
Narrow gauge railroad wholly in state	
When the annual net railway income exceeds the annual gross transportation receipts by 5% or less	No tax
When the annual net railway income exceeds the annual gross transportation receipts by 5% to 10%	¼%
When the annual net railway income exceeds the annual gross transportation receipts by more than 10%	¾%
Railroads operating not over 50 miles	1¾%

Reports.—Telephone and telegraph companies file returns with the State Tax Assessor on or before the last day of January. A final reconciliation return must be filed on or before March 31 covering the prior calendar year (Ch. 717, Laws 1974, 1st Spec. Sess.; Tit. 36, Sec. 2686). Railroads file statements of gross transportation receipts, net operating income and average miles operated with the State Tax Assessor each year between April 1 and April 15 (Tit. 36, Sec. 2621).

Collection.—Payment of tax is made to the State Tax Assessor annually by telephone and telegraph companies on or before January 31 and by railroads ⅓ on June 15, ⅓ on September 15, and ⅓ on December 15 (Ch. 717, Laws 1974, 1st Spec. Sess.; Tit. 36, Secs. 2626, 2686).

Source.—References are to Maine Revised Statutes, 1964, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER at ¶ 80-000.

SUMMARY

December, 1977

The Report of the Minority
of the Joint Committee on Taxation

Phantom Taxes Are Not Justified:
How Consumers Are Charged For Taxes
That Utilities Have Not Paid

1. Introduction (pages 1-3)

Phantom taxes are taxes which utilities have not paid yet which consumers are charged for. Consumers must pay $2 for every $1 of phantom taxes. The Minority of the Committee finds that:

A. It is in the present and future benfit of consumers if the PUC is able to deny phantom taxes as actual costs of service; and

B. Phantom taxes are in effect a regressive tax which places an unfair and unnecessary burden on Maine persons with poverty level incomes.

Complicating this issue is the fact that the Internal Revenue Code may preempt Maine's right to protect its consumers from unjust utility rates.

2. How great are phantom taxes (pages 8-9)

The nation's 150 largest electric utilities (including 2 two Maine utilities) in 1975 charged their customers $1.5 billion for federal taxes which they had not paid. This was a $.5 billion increase over the total 1974 phantom taxes.

3. How utilities require Maine consumers to pay for phantom taxes (pages 10-11).

Since 1969 when utilities have requested from the PUC increased rates, utilities have sought to have phantom taxes included as an actual cost of service. These phantom taxes were primarily tax expenses which, because of federal income tax breaks, utilities did not actually pay. The major tax breaks involved were:

1. Accelerated depreciation
2. Investment tax credit
3. Right of parent and subsidiary corporations to consolidate income tax returns.

4. Current status of the Maine PUC's regulation of phantom taxes (pages 12-14)

In over 14 cases, the PUC has "flowed through" to consumers the benefits of phantom taxes. Each of these denials of phantom taxes as actual cost of services is on appeal to the Maine Supreme Judicial Court and should be decided by July, 1978. In the 1977 NET decree alone, the PUC denied phantom taxes and reduced consumer rates by over $10 million.

5. Why phantom taxes impose an unfair and unnecessary burden on Maine consumers. (pages 15-23)

In general, the minority of the committee is convinced that allowing the PUC discretion to deny phantom taxes will result in consumer savings both in the present and future; further, the minority finds that phantom taxes are in effect a very regressive tax on Maine consumers.

Specifically, the minority of the committee feels phantom taxes represent poor social and economic policies for the following reasons:

A. If a utility is expanding or even stable, phantom taxes are a permanent tax savings (page 15).

B. If economic conditions change and phantom taxes become a necessity, utilities can apply to the PUC for a rate change (page 10).

C. In the case of regulated utilities, the corporate income tax is, in effect, a very regressive excise tax on consumers. Further, phantom income taxes are an interest-free loan that customers - poor or wealthy - are forced to contribute (page 18).

D. Regulated utilities, unlike free market industries, do not have to lower consumer prices due to federal and state tax breaks (page 20).

E. Even if utilities should be able to force interest free capital contributions from consumers, phantom taxes are a inefficient means of raising such money. Because of utility's 55% tax rate, in order to keep $1 of usable capital, a utility charges over $2. (page 20).

F. Phantom taxes, because they result in forced, interest free capital contributions from consumers, may provide utilities an incentive to construct unnecessary plant (page 21).

6. <u>Minority of the Committee findings and recommendations (pages 24-26)</u>.

A. The PUC must have discretion to deny phantom taxes as an actual cost of service.

B. If the Maine Supreme Judicial Court decides that the Internal Revenue Code does in fact prevent the Maine PUC from "flowing through" to consumers the benefits of phantom tax breaks, the Maine Legislature should consider a constitutional challenge to the federal preemption of our state rights.

C. Finally, if the Maine Supreme Judicial Court rules that the current <u>Maine</u> income tax law automatically includes any Internal Revenue Code regulation the federal government sees fit to enact, then the Maine Legislature should immediately adopt legislation that will give the PUC discretion to deny phantom <u>state</u> taxes as an actual cost of service.

A. TAXATION OF INSURANCE COMPANIES IN GENERAL

1. Introduction

In the past 5 years, state taxation of insurance companies has become a topic of comprehensive review by several states and by a number of economists. Rising costs, inflation, and the reluctance of the states to continuously raise property and income tax rates have influenced some states to broaden the tax base and to search for new sources of tax revenues. The method of state taxation of insurance companies has not changed in 125 years, and states such as Massachusetts and New York are studying alternatives to the existing system of taxation of insurance firms.[1]

While several states have been studying state taxation of insurance companies, the federal government has been considering the imposition of a uniform tax system on insurance companies to replace state insurance income taxes. A federal tax law would not only remove a number of deficiencies in state standards, it would also change the formula by which revenues of insurance firms are taxed by the states.

In order to understand the changes proposed by the several states and the alternative contemplated by the federal government with respect to state taxation of insurance firms, it is necessary to study existing methods of taxing insurance firms on the state and national levels.

2. Federal Taxation of Insurance Firms

Federal taxation of insurance firms is based upon the Income Tax Act of 1959 which subjects net income of insurance firms to federal corporate income tax rates. Although insurance firms are subject to the same tax rates as any other corporation under federal law, the method of deriving the taxable income of insurance firms is very different from that of most corporations. The following formula is used to determine taxable income of insurance firms:

Phase I is called investment income.
Phase II is underwriting income.
Phase III is the amount distributed to stockholders from the policyholder surplus account.

The taxable options are applied as follows:

If Phase II is less than Phase I then Phase II + Phase III = taxable income
If Phase II is greater than Phase I then Phase I + 50 percent of the excess of Phase II over Phase I ± Phase III = taxable income.

The formula that determines the taxable income of insurance firms subjected 76 percent of the net income of the industry to federal income taxation in 1970. In contrast, 87 percent of the net income of all industry in the United States was subject to federal income taxation in 1970.[2]

According to the Internal Revenue Service publication, "Statistics of Income, 1970 Corporation Income Tax Returns". The insurance industry, for the most part, is more concentrated than any other industry in the nation and is taxed less than any other industry. In 1970 federal income taxes comprised 40 percent of the net income of all insurance agencies, whereas federal income taxes comprised more than 50 percent of the total net income of all industries in the nation.[3]

The degree of concentration and the income tax burden imposed upon the largest firms with the greatest income in the insurance industry compared to all industries in the nation is illustrated below:

TABLE 1
THE DEGREE OF CONCENTRATION AND THE TAX BURDEN IMPOSED UPON THE INSURANCE INDUSTRY AND ALL OTHER INDUSTRIES, 1970

	INSURANCE INDUSTRY		ALL INDUSTRIES	
	Firms with Business Receipts of less than $1,000,000	Business Firms with Receipts of $100,000,000+	Firms with Business Receipts of less than $1,000,000	Firms with Business Receipts of $100,000,000+
% of Firms in the Industry	62.8%	2.57%	90%	.049%
% of Assets of the Industry	0.612%	83.4%	9.4%	51.1%
% of Receipts of the Industry	0.64%	76.6%	14.4%	46.2%
% of Net Income of the Industry		83.5%	7.42%	53.0%
% of Income Tax Paid by the Industry	0.74%	81.9%	7.75%	60.0%

Table 1 shows that the number of firms in the insurance industry with annual business receipts in excess of $100,000,000 exceeds by 500 percent the number of firms with annual receipts of more than $100,000,000 in all industries combined in the nation. In addition, the share of the income tax of the largest firms in the insurance industry is 1 percent less than the share of the net income of these firms. On the other hand, the share of the income tax of the largest firms in all industries combined is 7 percent more than the share of the net income of these firms.

Federal taxation of insurance firms creates preferential tax treatment of insurance firms which is the result, in part, of the source of insurance company income. Capital gains, which comprise more than 40 percent of insurance companies' revenues can be taxed separately at a rate of 30 percent and not be included in total taxable income which is taxed at 48 percent in excess of $24,000. In addition, dividends, which is the other principal source of income of insurance firms, are taxed at a much lower rate because of the 85 percent inter-corporate dividend deduction.[4]

3. State Taxation of Insurance Firms

For the most part, the method adopted by the several states to tax the income of insurance firms has not changed since the mid 19th century. In the mid 1800's, led by Massachusetts and New York, a number of states levied a tax on insurance premiums received by the firms. In addition to the premiums tax, a retaliatory clause was included in many state insurance tax laws. Most states have enacted retaliatory clauses similar to the one adopted by the Commonwealth of Massachusetts in 1856 which is presented below to explain how the clause operates.[5]

> "Whenever by the laws of any other state any taxes..., are or shall be imposed upon insurance companies organized in the Commonwealth doing business in such other state, then the same taxes shall be imposed on all insurance companies doing business in the Commonwealth which are organized in such other state."

The purpose of the retaliatory clause is to protect the domestic insurance firms organized in the one state and doing business in foreign states from injurious taxation by foreign states. The effect of the tax has been to fix state tax rates levied on insurance premiums at very low levels. For example, in 1873 the tax rate levied on insurance premiums by the Commonwealth of Massachusetts was 2 percent which was the same rate in effect in Massachusetts in 1973.[6]

Some attempts have been made to change the rates or provisions of state insurance tax laws, but, in many cases, the attempts have been frustrated. In 1942, the Massachusetts General Court (state legislature) considered imposing a 2 percent tax on insurance company annuities to produce additional revenues of $1,000,000 of which $400,000 would be derived from firms organized in the State, and the remainder would be derived from "foreign" firms. The Massachusetts based insurance companies convinced the General Court not to alter the existing law by pointing out that the retaliation clauses of all the other states would increase taxes levied on Massachusetts firms doing business in "foreign" states by $2,000,000. In addition, the annuities tax would reduce the ability of Massachusetts firms to compete for business in other states which did not impose an annuities tax on domestic firms. As a result, no changes were made in the Massachusetts law for 27 years when a surtax was imposed in 1969 on domestic firms.[7]

While all states impose a tax on insurance premiums, some states have additional tax provisions which clearly differentiate these states from the rest of the nation in terms of taxing insurance companies. Alabama, for example, permits municipalities to tax fire and marine insurance companies, but the local tax cannot exceed 4 percent of every $100 of gross premiums paid on policies on property located in the municipality. New York State levies a gross premium tax and a corporate income tax on insurance firms. Louisiana imposes a graduated tax schedule on insurance company premiums.[8]

In addition to different tax structures imposed upon insurance companies by some states, a number of states are more inclusive than others with respect to the types of insurance firms that are taxed. Alaska, Arizona, and Connecticut, for example, tax hospital and medical service insurance corporations and self-insured employee benefit plans. Arizona levies a higher rate on automobile insurance companies than on other types of insurance firms. New Hampshire, Rhode Island, Minnesota, and a few other states levy higher tax rates on marine insurance firms than on other types of insurance firms.[9]

4. Taxation of Insurance Firms in New England

The New England states, with the exception of Massachusetts, have similar tax laws pertaining to the taxation of insurance firms. Massachusetts tax rates are the highest of the six state region, and Maine's rates are among the lowest.[10] The following table describes the system of taxing insurance firms in each state.

TABLE 2
TAXATION OF INSURANCE FIRMS
IN NEW ENGLAND

STATE	INSURANCE FIRMS SUBJECT TO TAX	RATES OF TAXATION	YIELD IN MILLIONS OF $	% OF STATE TAX REVENUES
CONNECTICUT	Domestic Insurance Firms- Foreign Insurance Firms- Hospital & Medical Service Corporations- Unauthorized Insurers- Self-Insured Employee Benefit Plans-	2%-Net Direct Ins.Premiums 2%-Net Direct Ins.Premiums 2%-Net Direct Subscriber Charges Received 4%-Gross Premiums 2 3/4%-Benefits Paid Except 2 1/2% of Death Benefits Paid	$35.4	3.345%
[illegible]	Domestic Insurance Firms Foreign Insurance Firms Fire Companies	-1%-Gross Direct Premiums -2%-Gross Direct Premiums -Additional 6/10 of 1% Tax	$8.8	2.5%

MA‹ .CHUSETTS	Life,Savings,Insurance Banks (Domestic & Foreign)	1/4 of 1% of Net Value of Policies or 2% of Premiums whichever smaller +14% Surtax + 46% Surtax on Domestic Insurers(Life) 1% on Gorss Investment Income	$78.1	3.5%
	Marine,Fire&Marine Other Domestic Isurers	-5% of Underwriting Profit +14% Surtax 2% + 14% Surtax		
NEW HAMPSHIRE	Authorized Insurers-	2% of Gross Premiums Less Dividends Returned		
	Ocean Marine Companies-	5% of Taxable Underwriting Profit		
	Unauthorized Ins.&Independently Procured Insurance-	4%-Gross Premiums	$6.2	3.6%
	Unauthorized Marine-	2%-Gross Premiums		
RHODE ISLAND	Marine-	5%-Average Underwriting Profit		
	Domestic,Foreign Ins. Firms-	2%-Gross Premiums Less Return Premiums & Reinsurance Premiums	$7.5	2.1%
VERMONT	Domestic & Foreign	-2%-Gross Premiums Less Returns Premiums		
	Foreign Mutual Fire Ins.	-2%-Gross Premiums	$3.6	1.9%
	Domestic	-2%-Premiums Covering Risks in Other States in which no tax is collected		

B. TAXATION OF INSURANCE COMPANIES IN MAINE

1. Description of how the tax is administered in Maine

In Maine, a tax is levied on the gross direct premiums, paid to or written by insurance firms doing business in Maine. Return premiums and dividends paid to policy holders are not subject to the tax, but annuities of life insurance companies are taxed. Insurance firms organized in Maine are subject to a tax of 1 percent levied on insurance premiums, and foreign insurance firms are taxed at a rate of 2 percent. Fire insurance companies are taxed an additional 6/10 of 1 percent to cover expenses of the Fire Marshal's Office. "Foreign" insurance firms are subject to the retaliatory clause in the insurance tax law.

Unlike a number of states, Maine does not levy a tax upon hospital and medical service corporations, self-insured employee benefit (insurance) plans, or upon workmen's compensation and occupational disease compensation insurance premiums. In addition, Maine does not levy special tax rates on marine or automobile insurance premiums as do several other states.

The insurance tax is levied on roughly 600 insurance firms which do business in Maine. According to Bureau of Taxation records, 31 firms or 5.1 percent of the total number of insurance firms are organized in Maine, and 95 percent of the firms are classified as "foreign" firms which are subject to the retaliation clause.[11]

2. Analysis

a. Economic Effect

The insurance premium tax rates of Maine are among the lowest in the nation. In addition, Maine's insurance tax provisions tend to be far less inclusive than most states and exempt hospital and medical service corporations, self insured employee benefit programs, and workmen's compensation programs from the the insurance tax.

Although Maine's insurance tax rates are comparitively low, increasing the rates by 2 percent or more may significantly increase tax revenues but produce an adverse effect on Maine's firms. Maine's retaliation clause applies to foreign firms which comprise 95 percent of the insurance firms doing business in Maine. If out-of-state insurance rates are higher for Maine firms doing business out-of-state, Maine's "foreign" insurance rates are raised to match the out-of-state rates. Since most states levy a 2 percent tax on out-of-state firms' insurance premiums, 5 percent of Maine's firms pay the domestic tax rate of 1 percent, and a large proportion of the 95 percent of the "foreign firms" pay the foreign tax rate of 2 percent. New York, Massachusetts, Alabama, and Alaska, are examples of states which levy taxes in excess of 2 percent on out-of-state firms' premiums. Firms organized in these 4 states (and other states with higher foreign rates) but doing business in Maine are taxed by Maine at the same rates charged out-of-state firms by these states.[12]

Maine's flat rate insurance taxes are regressive and place a much heavier burden upon low income firms than on high income firms. Every firm pays the same proportion of its income in taxes regardless of the firms' level of income.

b. Yield

The Maine insurance tax produced roughly $8,800,000 in revenues compared to $6,500,000 of tax revenues collected from insurance firms in 1974. In 1974 and 1975, insurance tax revenues comprised 2.5 percent of Maine's total state tax revenues.

c. Elasticity

Insurance tax revenues tend to be elastic upward and relatively inelastic downward. The stability of income tax revenues is the result, in part, of the nature of the insurance business. Since 1955, insurance tax revenues in Maine have increased 400 percent compared to a 500 percent increase in state corporate income tax revenues between 1955 and 1975.

Since 1955, economic development and growth in Maine has occurred at a rate that the State had not experienced since the 19th century. As a result, the insurance industry has also prospered. Nevertheless, economic slowdowns in the late 1950's, the early and late 1960's, and in the years 1972-1974 were felt in Maine. Despite the economic slowdowns, insurance company tax revenues did not show a decline. In fact, insurance tax revenues have continuously increased in Maine over the last 20 years without any changes in tax rates.

Insurance is often considered to be a necessity. As a result, the demand for insurance remains very steady during economic upturns and downturns. The rapid rate of inflation since the mid 1960's and the strong upward trend in real and personal property values are probably the most influential factors that have been responsible for increased insurance premiums and tax revenues in Maine during the last 15 years.

d. Equity

The insurance premium tax is not based on the "ability to pay". It is a flat rate proportionate tax levied on the income of insurance firms and is a regressive tax. The greater a firm's net income the lighter the tax burden. As the net income of an insurance firm decreases, the tax burden increases.

One Maine firm, for example, with total premiums in excess of $22,500,000 paid the same tax rate (1%) as another firm with total premiums of roughly $20,000 in 1975. The Travellers and Prudential Life Insurance Companies, each with total premiums in excess of $45,000,000 in Maine, paid the same tax rate (2%) in 1975 as the Bankers Life Insurance Company with total premiums of roughly 120,000 in Maine.

While the insurance premiums tax is inequitable to comparatively low income firms, it is also inequitable, in the opinion of some economists, in comparison with the corporate income tax. While Maine based insurance firms pay an income (premiums) tax of 1 percent, and foreign based insurance firms pay a 2 percent tax rate, all other corporations (except real estate) doing business in Maine pay a corporate income of 5 percent levied on the initial $25,000 of net income and 7 percent on income in excess of $25,000.

e. Incidence

Maine insurance firms, which comprised 5.1 percent of the total number of insurance firms taxed under the Maine insurance tax law, produced 9 percent of the total insurance tax revenues in 1974 and 7 percent of the total in 1975. Approximately 570 insurance firms domiciled out-of-state provided more than 90 percent of the insurance tax revenues collected in 1974 and 1975.

In general, a small percentage of domestic and foreign firms provided a large proportion of the insurance tax revenues. Ten "foreign" insurance companies, which are among the largest companies in the nation and comprised 16.6 percent of the insurance firms operating in Maine, provided 33 percent of the total state insurance tax revenues collected in 1974. These same 10 firms provided 26 percent of the insurance tax revenues collected in 1975. Two Maine based firms which comprised 6.4 percent of the total number of Maine insurance firms, provided 95 percent of the insurance tax revenues collected from Maine insurance companies in 1974 and 1975.[13]

C. POSSIBLE AREAS OF REFORM

There are a number of alternatives to the present insurance tax law which can be implemented by the Legislature as follows:

1. Apply state corporate income tax rates to taxable income of all insurance firms doing business in Maine.

2. Subject hospital and medical service insurance corporations to the insurance tax law.

3. Subject workmens' insurance benefit programs to the insurance tax law.

4. Base the State insurance tax on the taxable income of insurance firms as reported to the federal government, and apply Maine's corporate income tax rates to the taxable income.

5. Raise the Insurance Tax levied upon foreign insurance firms from 2 percent to 4 percent. Revenues would be increased by more than $5,000,000.

1. Owen L. Clarke, "Effective Taxation of Insurance Companies," Insurance Law Journal, July 1972, P. 390.

2. Internal Revenue Service, Statistics of Income, 1970 Corporation Income Tax Returns, Computed from Table 7, pp. 65 & 92.

3. Ibid. pp. 65 and 92.

4. James Baylor and Russell J. Gallian, University of San Francisco Law Review Federal Taxation Aspects of Variable Life Insurance, September, 1974, pp. 523-555.

5. Owen L. Clarke, "Effective Taxation of Insurance Companies," Insurance Law Journal, July, 1972 pp. 391-392.

6. Ibid, p. 392

7. Ibid, pp. 392-393.

8. Commercial Clearing House, State Tax Guide, Insurance Gross Premium Taxes, pp.

9. Ibid.

10. Ibid.

11. Bureau of Taxation, Excise Tax Division, Reports of Insurance Premium Taxes.

12. Computed from the Bureau of Taxation, Excise Tax Division Reports.

13. Ibid.

From: State Retaliatory Taxation of the Insurance Industry, by The Council of State Governments (1977).

3. Possible Courses of Action

Several approaches are available for dealing with the state retaliatory tax situation in the insurance industry. Some of these options are:

(1) Make no change in current retaliatory statutes,

(2) Eliminate retaliatory legislation,

(3) Impose income taxes on insurance companies in lieu of the gross premium tax,

(4) Extend the practice of applying the gross premium tax plus an income tax, or

(5) Enact reciprocal nonretaliatory legislation.

MAKE NO CHANGE

Several spokesmen from the insurance industry feel that this would be the best option for the industry. The most likely outcome of the continuation of the present retaliatory statute provisions would be an increase in the tax burden of domestic companies in states with large insurance industries (i.e., Massachusetts) or a significant increase in the gross premium taxes of foreign corporations in those states where the foreign business of the domestic insurance companies is relatively minor (i.e., the 4 percent premium tax on foreign insurance companies in Alabama and Oklahoma). This assumes that there is little doubt that requirements for increased revenues in the states will cause some adjustment upward in the tax revenues produced by insurance companies.

ELIMINATE RETALIATORY LEGISLATION

While there are many who would be in favor of this (74 percent of the insurance and tax administrators surveyed by the State of New York in a 1973 study disagreed with the principle of retaliation),[19] the political realities are such that states are reluctant to take the plunge because they (1) fear that in so doing power may be lost to keep other states from raising the rate on their companies, and (2) believe that non-retaliation cannot be really effective until it is adopted by a large number of states.

IMPOSE INCOME TAXES IN LIEU OF GROSS PREMIUM TAX

William Craven noted the possibility of this in his statement:

One of the ways of modernizing insurance industry taxes is to adopt a net income approach.

Mr. Craven went on to note the problem of this when he said:

But, like any tax change, a shift in burden invariably results, with some companies incurring higher liabilities and others lower liabilities.[20]

James Papke conducted a study of the tax burden of 15 life insurance companies domiciled in the State of New York. The study, which was conducted in 1973, indicated that a state income tax rate of between 8.5 to 11.5 percent[21] would have provided the same revenues for the State of New York as were provided by the premium tax for years 1966-71.[22] While not advocating an income tax, Professor Papke expressed the opinion that life insurance companies are currently taxed at a greater rate than other corporations.

A different situation exists in West Virginia. There the gross receipts tax is applied to all business conducted in the state. West Virginia applies a 3 percent gross premium tax on insurance companies operating in the state (this may be reduced to 2 percent by investing 25 percent of admitted assets in West Virginia securities) while an occupational gross income tax ranging from 0.27 percent for wholesalers to over 8 percent for natural gas producers is imposed on other business in the state. In addition, insurance companies are exempt from paying state income tax while other businesses must pay the state income tax (credit is given for gross occupational tax paid). Obviously, the relative position of the insurance industry to other industries varies from state to state.

APPLY THE GROSS PREMIUM TAX PLUS AN INCOME TAX

Another course of action is to extend the practice of applying the gross premium tax plus an income tax. Nineteen states currently have provisions for applying the state income tax to domestic or foreign insurance companies. In nine of these states, the income tax applies to both foreign and domestic insurance companies. Those states are Florida, Illinois, Louisiana, Minnesota, Mississippi, Nebraska, New Hampshire, New York, and Tennessee. No credit for premium taxes paid is allowed against the income tax in Mississippi and New York. The other states do allow premium taxes paid as a credit against income tax due.

ENACT RECIPROCAL NONRETALIATORY LEGISLATION

Possibly the most promising course of action for the long-run is the enactment of reciprocal nonretaliatory legislation. New York and Massachusetts have attempted to deal with the problem of retaliatory statutes by enacting "reciprocal nonretaliatory" statutes. These statutes basically allow that any insurance company doing business in New York or Massachusetts which is domiciled in a state that does not retaliate against New York or Massachusetts companies will not be retaliated against by New York or Massachusetts. In other words, "if you won't retaliate against my companies, I won't retaliate against yours." At the present time, New York and Massachusetts are the only states with retaliatory provisions, which also have reciprocal nonretaliatory statutes. The reciprocal nonretaliatory provision would also be effective between the jurisdiction with no retaliatory statutes (Hawaii, New Mexico, North Carolina, and the District of Columbia). Bills to enact such legislation have been introduced in several other state legislatures recently. In 1974, the National Association of Tax Administrators passed a resolution calling for all of their members to encourage the enactment of reciprocal nonretaliatory legislation.

TASK FORCE RECOMMENDATIONS AND SUGGESTED LEGISLATION

After a great deal of study, the task force of the Council of State Governments came to the conclusion that the best way of dealing with the problems of retaliatory insurance taxation was to enact reciprocal nonretaliatory legislation. The recommendations of this task force and a draft of a suggested bill are found in *1977 Suggested State Legislation* published by the Council of State Governments. The draft legislation follows.

Suggested Legislation

The provision of this section shall not apply to insurance companies organized or domiciled without this state under laws which do not impose retaliatory taxes or other charges or which grant, on a reciprocal basis, exemptions therefrom to insurance companies organized or domiciled in this state.

Comment: The word "section" refers to that portion of existing state legislation dealing with insurance taxation and the present retaliatory tax.

MISCELLANEOUS BUSINESS TAXES

The following business taxes are described in this section:

A. Maine Industry taxes

   1. Sardine Development Tax

   2. Blueberry Tax

   3. Potato Tax

   4. Milk Tax

   5. Dairy and Nutrition Council Tax

B. Corporate filing fee

A. Maine Industry taxes

The following taxes are used to promote their respective industries. The descriptions are taken from the Legislative Finance Office publication, Compendium of State Fiscal Information:

SARDINE DEVELOPMENT TAX (Adopted 1951) - M.R.S.A. Title 36

An excise tax is levied and imposed upon the privilege of packing sardines. An excise tax of 25 cents per case on the type of canned sardines packed as provided.

Note: Purpose to advertise, research, study and conserve the industry along with promoting the prosperity and welfare of the State.
Amended 1963 striking provision for $500,000 limit on collections.
Amended 1965 to exempt exported sardines.
Amended 1969 to include financing of inspections of sardines.

BLUEBERRY TAX (Adopted 1945) - M.R.S.A. Title 36

There is levied and imposed a tax at the rate of 2-1/4 mills per pound of fresh fruit on all blueberries grown, purchased, sold or processed in this State.

Note: Purpose to promote the prosperity and welfare of the State and blueberry industry. Additional tax of 1 mill per pound added in 1971.

POTATO TAX (Adopted 1937) - M.R.S.A. Title 36

A tax is levied and imposed at the rate of $.025 per hundredweight on all potatoes raised in this State except those retained by the grower for seed or consumption.

Note: Amended 1955 increasing tax from 1 cent to 2 cents per barrel. Amended 1972 to $.012 per hundredweight. Amended 1975 to $.025 per hundredweight, effective 10/1/75 and to revert to $.012 per hundredweight 7/1/78. Purpose to conserve and promote the prosperity and welfare of the State and potato industry.

MILK TAX (Adopted 1953) - M.R.S.A. Title 36

A tax is levied and imposed at the rate of 5 cents per hundred weight on all milk produced in this State except that milk used on the farm where produced.

Note: Amended 1967 increasing tax from 2 cents to 3 cents per hundredweight. Amended 1969 increasing tax from 3 cents to 5 cents per hundredweight. Purpose to promote the prosperity and welfare of the State and dairy industry.

DAIRY AND NUTRITION COUNCIL TAX (Adopted 1975) - M.R.S.A. Title 36

There is levied and imposed on dealers a tax of 3 cents per hundredweight on all milk produced, purchased or imported for sale within this State. Milk exported is not subject to tax.

Note: Purpose to promote the welfare of the State and preserve the dairy industry.

B. MAINE CORPORATE FILING FEES

The following description is taken from the Commerce Clearing House publication, <u>State Tax Guide</u> (2nd edition):

¶ 5-490 **Annual Report**

Report and Fee.—Each domestic corporation and each foreign corporation authorized to do business in Maine, except those doing business without qualification as authorized by Maine law; must file an annual report with the Secretary of State between January 1 and June 1 of the year next succeeding the calendar year for which the report is made. The report is not required of religious, charitable, educational or benevolent corporations, corporations without capital stock or incorporated county law libraries (Tit. 13-A, Sec. 1301). The filing fee is $30 (Tit. 13-A, Sec. 1401).

Source.—References are to Maine Revised Statutes Annotated, as amended to date. Complete details are reported in CCH MAINE TAX REPORTER.

C. ANALYSIS

1. Economic effect

This filing fee is a significant levy in view of the fact that fully 1/2 of the corporations in Maine pay no corporate income taxes.

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FRANK M. CARTER, BANGOR

STATE OF MAINE

ONE HUNDRED AND EIGHTH LEGISLATURE

COMMITTEE ON TAXATION

MAINE TAX STRUCTURE

Description of Areas of Possible Reform

This study, prepared by the Legislative Joint Committee on Taxation, is meant to be a constantly updated analysis of Maine taxes and policy issues. Further, it offers with each tax analysis a listing of commonly voiced areas of reform. The Committee on Taxation does not necessarily endorse any of these reform suggestions; indeed, some of them are contradictory. Rather, it offers them for public debate. If any Legislator wishes to further pursue any specific tax reform measure, please contact the Office of Legislative Assistants, Room 427, State House.

The members of the Office of Legislative Assistants who staff the Committee on Taxation in the preparation of this study are:

Helen T. Ginder

James A. McKenna

Edward W. Potter

Clerical assistants are:

Earl Knox
Laurette Knox
Sandy Mathieson

TAX REFORM ISSUES

The following articles represent the latest contribution to the continuing debate of state tax reform. When significant new ideas are published they will be placed at the end of this section.

A. Tax Structure Reform — Section

Two studies and at least one legislative bill have approached tax reform as a structural problem: it is not enough to simply tinker with one or two taxes, the entire mix of taxes must be looked at and reformed. (See also the entire chapter in this manual devoted to the state tax mix.) Included in this section on structural reform are:

1. A summary of the 1975 report of the Governor's Tax Policy Committee. This report, among many other things, recommended a 2 stage shift in the tax strucure from property taxes to income taxes. The first stage was enactment of a property tax circuit breaker; the second stage was an approximately $100 million increase in income taxes and a corresponding lowering of the property tax. — A-1

2. Summary of the 1976 Joint Select Committee on State Tax Policy. This committee also recommended a tax structure shift from the property tax to income taxes. The method it endorsed was a property tax circuit breaker. — A-2

3. L.D. 1613, which adopted the New Mexico income tax credit system as a way of accurately removing the entire tax structure's unfair regressivity. (See also Professor Lile's analysis of the current regressivity in Maine tax structure, in this manual's chapter on Maine Tax Burdens). — A-3

4. Advisory Commission on Intergovernmental Relations (ACIR) listing of income tax credits used to shift the burden within state tax structure. — A-4

5. How to overcome the inequities of a flat credit — A-5

B. Property Tax Reform: How Regressive Is The Property Tax?

The following articles present contrasting views on how regressive the property tax really is and the best way to reform it.

1. "Is the Property Tax Progressive?" by Allan Odden. The author suggests that, despite arguments of the "revisionist" economics, the property tax is clearly regressive on lower income persons. — B-1

2. "Property Taxes Aren't All That Bad" by David Hagman. The author summarizes the "revisionist" economists' arguments. For a more detailed analysis by perhaps the leading "revisionist" economist, see Henry Aaron's Who — B-2

Pays the Property Tax? (1975). Section

C. Property tax reform: options for elderly tax relief

1. In 1976 HUD released a 3 volumn report, Property Tax Relief Programs for the Elderly. Reproduced here are a short summary of the report's research and a description of the many elderly tax relief programs currently existant. C-1

2. "The Elderly Face Special Problems" a July 1977 New York Times article. Reveals some "low-income" elderly do not need property tax relief. C-2

D. Renters: their need for property tax relief

1. High rent burden called new form of housing deprevation; tax help programs for renters. D-1

2. Congressional record: tax policy discriminates against tenants. D-2

3. A new tax deal for renters: proposes a way renters can realize the same federal tax deductions currently enjoyed by real estate owners. D-3

E. Property tax reform: the state valuation and the Uniform Property Tax.

1. "Is the State Valuation Accurate?",the 1977 report of the Select Committee on State Property Tax Valuation. The state valuation is the total property value of the state and is both the base against which the Uniform Property Tax is levied and a factor in many state revenue sharing formulas. E-1

2. L.D. 1607, 1608, legislation based on the State Valuation report, both defeated by the 108th Legislature. E-2

F. Income tax reform: a permanent schedule and surtax mechanism.

1. This article suggests adopting a new income tax schedule that would feature: F-1

a. Greatly increased number of tax brackets, so that "ability to pay" is more accurately determined;

b. A permanent, progressive tax rate that increases evenly and consistently as income rises; and

c. A surtax that would be increased (or decreased) whenever the Legislature wished to change the amount of income tax revenues.

Such a system would allow the income tax to become a flexible partner of the state tax mix. Currently, to change income tax revenues, all the rates must be changed. This, of course, causes great political problems. Under this system only the surtax would change. A surtax does not in way change the rate of progressivity of the permanent schedule.

2. The case for highly graduated rates in state income taxes. This case suggests that states take advantage of the fact that moderate and high income taxpayers are able to deduct state taxes from their federal taxable income. For example,a person in the 50% federal tax bracket only actually pays 1/2 of his state tax bill. The conclusion: increase the state income taxes paid by the wealthy and the federal government will pay a good portion of the tax. F-2

3. The adjusted gross income of Maine taxpayers. This analysis shows how many taxpayers are in each income bracket. F-3

4. Income taxes and inflation. How to protect the taxpayer from hidden income tax increases? F-4

G. Business tax credits

1. The Great State Robbery by Harrison and Kanter. This article argues that state tax incentives have virtually no effect on job creation or economic development; but that they do increase the income of the already wealthy. G-1

2. Staff memo to the Committee on Taxation describing the findings of the 1977 Casco Bank study of business location decisions: present state and local tax burdens are reasonable. A summary from the Casco study is also included. G-2

3. Selections from the Fauntus Co. study of Maine's business tax climate. G-3

4. June, 1977 New York Times article, Business Tax Reform In New York State A Costly, Complicated Goal, Study Finds. G-4

H. Taxing intangibles: how to expand the property tax base.

For years the property tax base has been shrinking yet one area of property has long escaped taxation: intangibles such as stocks and bonds. Since this type of property is often held by the weathier persons in our society, including it in the tax base would probably make property taxes more progressive. H-1

Section

I. <u>Limits on taxation</u>

1. <u>Local Spending and Tax Limits Across the County</u>. I-1

2. <u>Caution in state-local expenditures.</u> Prudence should be exercised in further increasing the public sector's percentage of the Gross State Product. I-2

3. <u>Staff memo argues the opposite side</u>: social services must be increased or Maine will always be the home of the poor, poorly educated and marginally employed. I-3

J. <u>Expansion of the local tax base.</u>

If the <u>local</u> (not state) tax base is expanded, "local control" will be fostered. Communities, rather than relying only on the already overstrained property tax, could pick the most efficient and fair tax service: property, sales or income taxes or user charges.

1. <u>Local income tax model legislation.</u> J-1

2. <u>Local sales tax model legislation,</u> J-2

3. <u>Local services charges on tax-exempt property</u>, passed in a limited fashion in the 108th Legislature. J-3

K. <u>Taxation of public utilities</u>

Public utilities are currently taxed in an inconsistent, inaccurate and possibly unfair manner.

1. <u>Bureau of Taxation's memo</u> outlining possible reforms to public utility taxation. K-1

2. <u>A model public utility excise tax.</u> K-2

L. <u>Taxing Consumption</u>

1. In a world of limited resources, the tax structure should perhaps be geared to conservation and penalize luxury consumption. L-1

M. <u>Tax Base Sharing</u>

1. A proposal whereby all communities share partially the fruits of new Maine industrial development. Why is this needed? Because almost all development in Maine is taking place in Southern Maine while the hinterlands continually lose persons and jobs. M-1

STATE OF MAINE
GOVERNOR'S TAX POLICY COMMITTEE
STATE HOUSE
AUGUSTA, MAINE 04333

November 17, 1975

The Honorable James B. Longley
Office of the Governor
State House
Augusta, Maine 04333

Dear Governor Longley:

The Tax Policy Committee has completed its deliberations and is pleased to submit for your consideration some important interim and fundamental tax policy directions for the State of Maine. The recommendations of the report represent a majority view of the Tax Policy Committee.

The Committee urges you to give careful study to all of the recommendations and welcomes the opportunity to give you the benefit of the differing perspectives which the Committee shared in arriving at its recommendations. We fully realize that the report must stand the test of your scrutiny, public review and ultimate action by the Legislature.

The Committee recognizes the great difficulties in securing favorable action on tax reform issues. We hope this report will stimulate the public support and leadership essential to the tax reform needed in Maine.

Sincerely yours,

John L. Salisbury

John L. Salisbury
Chairman

JLS:saw

A-1

AN IDEA WHOSE TIME HAS COME:
A TAX POLICY FOR THE STATE OF MAINE

Summary of Recommendations

Presented below is a summary of the Governor's Tax Policy Committee's recommendations. These reforms cover five basic areas:

A. *Fundamental Reforms.* These changes are the long-range goals of this report's Maine tax policy.

B. *Financing Fundamental Reforms.* The Committee does not recommend an increase in total State taxes but rather a shifting of burdens within the present tax structures.

C. *Interim Reforms.* These changes are necessary only if the fundamental reforms are not attainable in the near future. They are incremental reforms, "steps" that lead logically to the long-range fundamental goals.

D. *Financing Interim Reforms.* Again, the Committee does not recommend an increase in the total State taxes but rather a shifting of burdens within the present tax structures.

E. *Reforms in Administration.* These reforms will result in greater administrative efficiency and will aid in the elimination of unfair tax breaks.

Each of the committee's recommendations represents a majority but not necessarily unanimous opinion of the members. Where views differed substantially, members have filed minority opinions included in the appendix.

A-1

B. FINANCING FUNDAMENTAL REFORMS

The Personal Income Tax

The personal income tax should be increased to assume approximately 61% of the $98.3 million shifted burden. The present vertical progressivity of the tax should be maintained or slightly improved in the upper income brackets. Such an increase would place the income tax's share of State revenues at a reasonable 20-21%. *See* page 34.

Corporate Income Tax

The dramatic reduction in property taxes will result in a significant drop in business tax levels. The corporate income tax should assume approximately 5% of the shifted burden. *See* page 35.

The Sales Tax

The sales tax base should be expanded to include most tangible goods and services with a credit instituted, thereby converting the sales tax into a tax reflecting to a greater degree luxury consumption. This expanded sales tax should assume approximately 14% of the shifted burden. *See* page 36.

Current State Property Related Services

It is recommended that the State transfer to the municipalities the cost of some property related services currently provided by the State. *See* page 38.

Taxation of Inventories

With the conversion of the municipal property tax to a tax more closely reflective of the services provided property, business inventories should again be taxed. This reform will eliminate the $11.5 million still to be raised under 30 M.R.S.A., § 5056 to reimburse municipalities for revenues lost when business inventories were phased out from property taxes in 1973. (*See* page 38.) This cost avoidance will represent approximately 15% of the shifted burden.

Real Estate Transfer Tax

Because the fundamental reform plan will lower property taxes, on the average, by 50%, it is reasonable to increase the current real estate transfer tax formula. Property owners gain from such relief. *See* page 38.

Domestic Insurance Premium Tax

The tax on domestic insurance companies should be raised to 2% of premiums and fund approximately .5% of the shifted burden. *See* page 39.

C. RECOMMENDATIONS FOR INTERIM STRUCTURAL REFORMS

If fundamental reform is not at this time possible, the following "steps" or interim reforms should be accomplished.

The Property Tax

Institute a General Property Tax "Circuit Breaker"

Until the fundamental reform of removing the cost of education and welfare from the property tax burden is attainable, the committee recommends the interim step of adoption of a general property tax circuit breaker with a $10 million expenditure limit. *See* page 40.

Reimburse Loss of Inventory Taxes Through Revenue Sharing Formula

In 1977 when business inventories are completely exempt from the property tax, reimbursement for lost tax revenues will continue indefinitely in an inconsistent and unjust manner. It is recommended that the reimbursement method be repealed and an equivalent amount be distributed through the State revenue sharing formula to all communities in Maine. *See* page 42.

Personal Income Tax

Income Tax Equity Should be Improved

Until the fundamental reform plan - the shift from property taxes to other broad based taxes - is attainable, the Federal IRS provisions listed above should still be enacted as soon as possible. *See* page 45:

a. Head of Household schedule;

b. Standard (includes low income allowance) deductions;

c. Retirement income credit.

Sales Tax

The Sales Tax Rate Should be Lowered

Until the fundamental reform to sales taxes described above is attainable, the sales tax base should still be expanded to include services and the rate reduced to a level that will generate equivalent revenues. *See* page 45.

A-1

D. FINANCING INTERIM REFORMS

Preferred Plan

A majority of the committee recommends that the total amount be funded from an increase in the income tax. *See* page 46. If this proposal is not acceptable, the following options are suggested.

First Alternative

It is a possibility that the income tax could fund a portion of the reform with the remainder (approximately $14 million) being taken from an expansion of the sales tax base with a corresponding reduction of the sales tax rate to 4-1/2%. *See* page 46.

Second Alternative

It is also a possibility that interim reforms could be funded by $15 million income tax increase and imposition of a service levy on inventories. This would eliminate the need for $11.5 million more in inventory reimbursements to the municipalities. *See* page 47.

At the same time, it would be recommended that the current $3.5 million inventory property tax reimbursement method be shifted to the present State-local revenue sharing fund. This would minimize the slight increase in property taxes.

E. REFORMS IN ADMINISTRATION

Property Tax

Tree Growth, Open Space and Farm Land Provisions

As a Fundamental Change, Farm Land, Open Space, and "Tree Growth" Classifications Should be Repealed

Because the committee advocated the substantial reduction of property tax, and thus reducing pressure on farm land, open space and "tree growth" owners to pay high taxes, and because effective land use planning should be done through local zoning regulations and not taxation, our recommendation is that the farm land, open space, and "tree growth" classifications based upon current use valuation be eliminated in the future. *See* page 48.

Until Current Use Classifications of Farm Land, Open Space, and "Tree Growth" Are Repealed, an Investigation and Adjustment in the "Tree Growth" Formula Appear to be Necessary

Due to time constraints, the committee was only able to conclude that the tree growth formula did not adequately reflect the property's value. It is recommended that the Executive or Legislative branch carry out further research into the tree growth formula, specifically as it relates to land values, stumpage and growth rate factors. *See* page 49.

Until They are Repealed, Eliminate Unfair Tax Breaks From Farm Land, Open Space and "Tree Growth" Classifications

a. Because the seller of any of the above properties realizes a tax break during his ownership of land under current use classification, it is recommended that the seller, not the buyer, pay the recapture fee at the time of sale of the property-that fee being equal to the taxes which would have been assessed if the land had been assessed at its fair market value on the date of classification withdrawal or sale less the amount of taxes actually paid plus interest, for the previous ten years (fifteen years for open space).

b. In the case of tree growth land, the above provision would go into effect when the Property Tax Division has a necessary record of fair market valuations.

c. Recapture should be instituted at either the time of ownership change or change in use. Sale of property does not end a classification; only change in use would alter that.

d. To avoide mass transferrals rather than sales of property, a recapture tax should be levied on transfer of property rights.

e. In order to eliminate the so called "gentleman farmer" from undeserved preferential treatment, the committee recommends that farm land classification be defined on the basis of minimum production of $100 gross income per acre for one year on a tract containing at least ten contiguous acres. The present provision that requires farm production for 3 of 5 calendar years would be eliminated. *See* page 50.

Institutional Property Tax Exemptions

It Should be Locally Optional Whether Exempt Properties Pay in Lieu Service Charges

Because of inequities involved in the exemption from taxation of institutional properties, it is recommended that the legislative body in each municipality be given the option of levying an in lieu assessment that would reflect the cost of services, excluding welfare and education, rendered by the community to various classifications of property tax exempt non-profit institutions. *See* page 52.

The classification of property upon which communities would vote to permit in lieu service charges would be:

a. Church property (excluding houses of worship);

b. Hospital properties;

c. Private colleges, universities, elementary and secondary schools;

d. All other non-profit tax exempt organizations.

State Should Pay Municipalities For Services Provided to State Owned Property

State owned property makes up a great percentage of tax exempt property in many municipalities, thus denying them of substantial revenues. It is recommended that there be consistency in State in lieu assessments for service costs as recommended for other exempt institutions. An appropriation level should be determined in order to reimburse municipalities for service provided to State owned tax exempt property. *See* page 56.

Inheritance and Estate Taxes

"Death" Taxes Should Be Based on the Federal System

a. It is recommended that the current inheritance and estate taxes be repealed and replaced by a single estate tax based upon a percentage of the Federal taxable estate. The rates of such a tax would be graduated upward to insure no loss in revenue.

b. The name of the "Inheritance Tax Division" should be changed to "Estate Tax Division."

c. An estate tax rate should be adopted similar to the schedule attached in Appendix F. *See* page 57.

Income Tax

Nonresident Capital Gains Should be More Efficiently Collected

In order to facilitate better collection (and thus avoid evasion) of the tax on income made on the sale of real estate by nonresidents, the committee recommends that the Bureau of Taxation collect that tax at the point of sale. Sufficient resources should be provided the Bureau to accomplish this task. *See* page 58.

Not Presently Advisable to Have Federal Collection of State Income Taxes

Because Federal collection of State income taxes would cause a lack of flexibility and stability on the part of the State in determining its tax base, it is recommended that the so-called "piggyback" method of tax collection not be adopted as a more administratively efficient manner of collecting State income tax. *See* page 58.

Tax Shelters

No Tax Shelter Adjustments At This Time

The committee recommends that no current action be taken with respect to revision of Maine income taxation affecting so-called tax sheltered investments. *See* page 60.

Unorganized Territory

The Unorganized Territory Should Pay the Uniform Tax For Education, And Be Taxed at a Rate That Pays For the Other Services It Receives

A fairly detailed review of tax expenditures for services to the unorganized territory and the uniform property tax for educational purposes shows that property owners of this part of the State are not paying their fair share of taxes. The unorganized territory pays $6,262,145 in property taxes, yet receives $2,037,430 more than that for services and education from the State. The committee recommends that the Legislature adjust the State tax rate and tree growth formula so that the taxes in the unorganized territory properly reflect services provided it and reflect revenues comparable to what the uniform education tax would yield. *See* page 61.

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STATE OF MAINE

JOINT SELECT COMMITTEE ON STATE TAX POLICY

1. Introduction

Of all the tools of government, taxes can be the bluntest, the most unwieldly. Often their burdens fall unfairly, without recognition of our differing situations. The sales tax cannot distinguish between the person who lives frugally and the person simply too poor to buy many goods. The property tax cannot distinguish between the family house that has been held for generations and the lot purchased for quick development. The personal income tax reflects cash flow and family size but can tell little of a person's wealth in stocks or bonds. Alone, the income, sales or property tax can be an unfair levy; but taken together in a balanced tax structure they can greatly improve the chances that each of us will be taxed according to our "ability to pay."

The recommendations of this report . . .

continued, page 1-1

A PROGRESS REPORT ON MAINE'S STATE AND LOCAL TAX STRUCTURE

DECEMBER 1976

REPORT SUMMARY

1. INTRODUCTION

Alone, the income, sales or property tax can be an unfair levy; but taken together in a balanced tax structure they can greatly improve the chances that each of us will be taxed according to our "ability to pay". The recommendations of this report do not seek to raise the total tax burden of the state. Rather they shift the burdens within the state-local tax structure. See pages 1-1 to 1-2.

2. A PROGRESS REPORT ON THE CURRENT TAX STRUCTURE

Because Maine is a land rich, income poor state, the current mix of broad based state taxes - sales, income, property - is acceptable at this time. *See* pages 2-1 to 2-3. However, because the general tax structure remains regressive, changes are still needed. *See* pages 2-4 to 2-5.

The Uniform Property Tax (UPT) should not be repealed for the following reasons:

A. The UPT is a state, broad-based tax that, when combined with the income and sales taxes, more accurately reflects each person's "ability to pay".

B. The UPT only *raises* funds for education, it does not determine how much money each town *receives* from the state.

C. The UPT is a state tax but one that is collected by each town, with the revenues belonging to the state's general fund. Its mill rate is determined by the state's valuation of all property in the state. The yearly state valuation process encourages accurate local assessing practices.

D. The UPT is a more equitable way of taxing. It is not an education tool and has little relation to "local control".

See pages 2-5 to 2-15.

3. REFORMS TO
STATE-LOCAL PROPERTY TAXES

1. The property tax on inventories is hard to administer and harmful to the business climate. Its repeal should be continued and reimbursement made through the state revenue sharing formula. See pages 5-1 to 5-2.

2. A general property tax circuit breaker would ease any unfair burdens caused by the Uniform Property Tax (UPT) and local property tax. It would generally enhance the "ability to pay" accuracy of property taxes. If the Legislature fails to enact a general circuit breaker, then the elderly tax relief formula must be revised. See pages 3-3 to 3-6.

3. The accuracy of the state valuation is essential to the fairness of the UPT and the local property tax. Their accuracy is threatened by assessor error - either state or local. The committee supports improvements to the state valuation procedures and recommends state assessors assist the local assessor where necessary. See pages 3-6 to 3-7.

4. The UPT is a broad-base state tax. If increased revenues from the UPT are possible due to an increase in the value of Maine property, then some additional revenues should be returned in such a way that they benefit the most in need. See page 3-8.

4. REFORMS TO THE PERSONAL INCOME TAX

1. While the personal income tax is the most accurate of our broad based taxes in terms of taxing according to "ability to pay", the rate schedule can impose on some an unfair burden. Last session's personal income tax increase in some cases resulted in such burdens. Thus:

A. a Head of Household schedule should be adopted;

B. a state retirement credit should be adopted;

C. an income averaging formula should be adopted.

See pages 4-1 to 4-3.

2. A personal income tax should be progressive but not confiscatory, and have a sufficient number of brackets and gradations in the percentage rate to correctly identify each person's "ability to pay". The current income tax schedule should be investigated in order to achieve these qualities. See

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pages 4-3 to 4-4.

5. REFORMS TO THE SALES TAX

The sales tax can lose much of its regressivity by exempting necessities. The sales tax should not be imposed on residential water, gas or electricity. See pages 5-1 to 5-2.

2. The progressivity of the sales tax can also be improved by the selective taxation of services. See page 5-2.

3. Ideally, the sales tax should be a levy only on personal consumption. This would allow more accurate taxation of luxury consumption and improve Maine's business climate. The sales tax exemption for new manufacturing machinery and equipment should be expanded to fishing and, eventually, agriculture. See page 5-3.

6. FINANCING THE OMNIBUS TAX REFORM BILL

The recommendations of this report do not seek to increase the total tax burden of the state. Rather, they shift burdens within the state-local tax structure. The financing recommendations stand on their own as worthwhile changes to our tax laws:

A. Increase the real property transfer tax. See page 6-1.

B. The sales tax base should be expanded to include amusements. See page 6-2.

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D. Include life insurance proceeds of over $50,000 in the taxable estate.

See page 6-2.

E. Apply the 5% tax to cigarettes. See page 6-3.

F. Collect a percent of the federal minimum tax on "loophole" or "tax shelter" income.

See page 6-3.

G. Utilize federal revenue sharing funds.

See page 6-3.

H. Impose a minimum tax on all corporations.

See page 6-3.

I. Part of the new revenues due to be realized from the Uniform Property Tax (UPT) should be returned through a property tax circuit breaker and reimbursement to the towns for loss of inventory tax revenues.

See page 6-4.

7. AREAS DESERVING FUTURE STUDY

1. The Tree Growth Tax and Farm and Open Space Tax should be evaluated as to whether the burdens they impose are equitable in relation to the burdens of other property taxes. Such tax breaks are justified only if that land is seriously threatened by changes harmful to the public's interest.

See page 7-1.

2. The current state-revenue sharing formula might be improved so as to make it more accurate in its determination of need. See page 7-2.

3. Fundamental reform of the state sales tax should be pursued.

See page 7-2.

4. The administrative difficulty of taxing the unorganized territory at the same property tax rate as the organized areas should be resolved. See page 7-3.

Sec. 3. Appropriation. There is appropriated from the General Fund to the Department of Transportation, Bureau of Taxation, the sum of $60,000 to carry out the purposes of this Act. The breakdown shall be as follows:

	1977-78
FINANCE AND ADMINISTRATION, DEPARTMENT OF	
Bureau of Taxation	
All Other	$60,000

STATEMENT OF FACT

A $60,000 appropriation for 1977-78 will be necessary to fund the economic research needed to estimate relative tax burdens and to construct the rebate schedule of this bill which ensures that low paid workers, the elderly and the poor of Maine are not taxed at a higher rate than all other citizens. For fiscal year 1978-79, a $4 million appropriation will be necessary to fund the comprehensive tax rebate program.

1. Introduction

The comprehensive tax rebate program established by this bill is intended to lessen for lower and middle income persons the overall regressivity of the total state-local tax structure. It does this by calculating the regressive burden, if any, of each state-local tax and then establishing a single rebate formula that insures that no Maine family or person below the poverty level, worker, elderly or poor, will pay a greater share of taxes than a similar family or person whose income equals the poverty level. Although it is a partial reimbursement for taxes of all types, property taxes, sales taxes, etc., for efficiency and convenience, it is administered through the state income tax system.

A very important by-product of this bill will be the economic research, to be updated every 2 years, that will calculate:

A. Poverty level income for different types of Maine families;

B. Distribution of income received by family size for residents of the State;

C. A distribution of consumer expenditures made by residents of the State; and

D. Shifting and incidence assumptions with respect to each state tax.

Such information will provide the Legislature with a continuing and an up-to-date picture of the impact of our taxes.

2. Regressivity of the Maine tax structure

While the precise regressivity of each state or local tax will be calculated under the provisions of this bill, it is possible to see the general regressivity of Maine taxes. In 1975 the Kentucky Department of Revenue[1] analyzed the total family tax burdens in each state. The results for Maine in 1974 were:

[1] This analysis was completed before the recent $18 million (progressive) income tax increase. It was based on the following taxes: income, sales, property (residential), motor vehicle, cigarette.

Family of Four (Adjusted Gross Income)	Percent of Income Paid in Taxes
A. $5,000	13.6%
B. $7,000	11.5%
C. $10,000	9.7%
D. $17,000	9.2%
E. $25,000	8.3%
F. $50,000	7.8%

3. The New Mexico experience

The comprehensive tax rebate approach to solving the overall regressivity of a state's tax structure was pioneered by New Mexico. Since Maine and New Mexico are quite similar in terms of population, tax burden and per capita income,[2] it is instructive to look briefly at New Mexico's experience with this program.

Since it was first implemented in 1972, New Mexico's comprehensive tax rebate has grown from a $1.2 million program to, in fiscal year '75-76, a $5.37 million program. Several times the New Mexico Legislature has expanded the eligibility and adjusted the formula due to increased costs of living. A comparison of the 1972 program and the 1976 program shows:

New Mexico Comprehensive Tax Rebate 1972 and 1976

	1972	1976
A. Total rebates	$ 1.55 million	$ 5.37 million
B. Acreage rebate	$41.38	$86.74
C. No. of returns	37,000	61,865
D. Percentage of Personal Income Tax returns receiving the rebate	10.01%	14.9%

Further, it is instructive to see what types of New Mexico citizens (workers, elderly, poor) took advantage of the rebate:

1974 New Mexico Comprehensive Tax Rebate Returns by Sources of Income

Major source of Income	Returns processed (%)
A. Wages and salaries	30.5%
B. Social security	34.4%
C. Public assistance	25.8%
D. Other	9.3%

Finally, 2 federal studies have commented on the New Mexico credit. A 1975 report, sponsored by the U.S. Department of Housing and Urban Development states:

[2] Per capita income in New Mexico in 1973 was even lower than Maine's — $3,853 (N.M.) to $4,082 (Me.). In 1974 in state taxes per $1,000 of income, Me. had the 3rd heaviest burden in the country, New Mexico had the 13th heaviest.

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[The New Mexico mechanism] is a flexible one and offers attractive administrative advantages. . . . Because the comprehensive credit condenses many of the other tax credits currently being used by the states to reduce regressivity (property tax, renters, food tax and sales tax credits) into a single, efficient, easily administered formula, it has great promise for both New Mexico and other governments that select this approach.

Another 1975 report, by the U.S. Advisory Commission on Intergovernmental Relations states:

Programs like the New Mexico [comprehensive tax rebate], if properly funded and administered, are potentially the most powerful tools yet tried for providing broad-based relief to low- and moderate-income families. . . .

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Table 10—State Use of a Personal Income Tax Credit-Rebate to Minimize or Offset the Regressivity of Sales and Property Taxes[1]

State	Type of Credit	Year Adopted	Amount of Credit	Law	Administrative Procedure
Colorado	For sales tax paid on food	1965	$7 per personal exemption (exclusive of age and blindness)	Chap. 138, Art. 1 (Secs. 138-1-18 & 138-1-19 added by H.B. 1119, Laws 1965, effective 6/1/65)	Credit to be claimed on income tax returns. For resident individuals without taxable income a refund will be granted on such forms or returns for refund as prescribed by the Director of Revenue.
	For senior citizen property tax relief (homeowners and renters)	1971	Varies with income up to $3700; limited to 50 percent of property tax or $200	Chap. 138, Art. 1 (Secs. 138-1-20 & 138-1-21 added by H.B. 1040, Laws 1971, effective 7/1/71)	Credit claimed on income tax returns or, for those having no taxable income, on forms prescribed by the Department of Revenue.
Hawaii	For consumer-type taxes	1965	Varies based on income[2]	Chap. 121 (Secs. 121-12-1 & 121-12-2 added by Act 155, Laws 1965)	The Director of Taxation shall prepare and prescribe the appropriate form or forms to be used by taxpayers in filing claims for tax credits. The form shall be made an integral part of the individual net income tax return. In the event the tax credits exceed the amount of the income tax payments due, the excess of credits over payments due shall be refunded to the taxpayer.
	For drug or medical expenses	1970	do	Act 180, Laws 1970; sec. 235-56	
	For household rent	1970	do	Act 180, Laws 1970	
Idaho	For sales taxes paid	1965 and 1969	$10 credit per personal exemption (rebate applicable to taxpayers 65 and over only)	Chap. 195, Laws 1965. Chap 456, Laws 1969, Sec. 63-3024(d)	Credit (or rebate if credit exceeds tax liability) to be claimed on income tax returns. For resident individuals (65 and over) without taxable income a refund will be granted on such forms or returns for refund as prescribed by the State Tax Commission.
Indiana	For sales tax paid on food	1963	$8 per personal exemption (exclusive of age and blindness)	Chap. 50 (Chap. 30, Sec. 6d added by H.B. 1226, Laws 1963, 1st sp. sess., effective 4/20/63)	Credit to be claimed on income tax returns. If an individual is not otherwise required to file a return, he may obtain a refund by filing a return, completing such return insofar as may be applicable, and claiming such refund.
Kansas	For senior citizen homestead relief	1970	Varies, based on income and amount of property tax	Chap. 403 (H.B. 1253, Laws 1970)	Tax credit (or rebate if credit exceeds tax liability). The Department of Revenue shall make available suitable forms with instructions for claimants, including a form which may be included with or a part of the individual income tax blank.

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Table 10—State Use of a Personal Income Tax Credit-Rebate to Minimize or Offset the Regressivity of Sales and Property Taxes[1]

State	Type of Credit	Year Adopted	Amount of Credit	Law	Administrative Procedure
Massachusetts . . .	For consumer-type taxes	1966	$4 for taxpayer, $4 for spouse, if any, and $8 for each qualified dependent[4]	Chap. 62 (Sec. 6b added by ch. 14, Acts 1966)	Same as Indiana.
Minnesota	For senior citizen homestead relief[5]	1967	Varies with income from 75% to 10% of net property tax or equivalent rent not to exceed $800 (Max. credit $450)	Chap. 290 (Secs. 290.0601 to 290.0617 added by Ch. 32, Art. VI, Laws 1967, effective 1/1/68)	Tax credit or refund to be claimed on income tax return. Department of Taxation shall make available a separate schedule for information necessary to administration of this section and the schedule shall be attached and filed with the income tax return. Cash refund granted if property tax credit exceeds State personal income tax liability.
	Tax relief for renters	1967	7.5% of the total amount paid by claimant as rent, not to exceed $90[6]	Chap. 290 (Secs. 290.981 to 290.992 added by Ch. 32, Art. XVII, Laws 1967, effective 1/1/68)	Same as above.
Nebraska	For sales tax paid on food	1967	$7 per personal exemption (exclusive of age and blindness)	H.B. 377, Laws 1967	Credit to be claimed on income tax returns. Refund will be allowed to the extent that credit exceeds income tax payable but no refund will be made for less than $2.
Vermont	For sales tax paid	1969	Varies, based on income and number of personal exemptions (other than age and blindness)[7]	H.B. 125, Laws 1969; Chap. 152, Sec. 5829	Credit to be claimed on income tax returns. Credits properly claimed by resident individuals who have no income or no income subject to Vermont tax will be allowed the full amount of the credit as a refund.
	For senior citizen property tax relief	1969	Equal to the amount by which property taxes or rent constituting property taxes on their households exceeds 7% of the individuals total household income multiplied by the local rate factor[8]	H.B. 222, Laws 1969; Chap. 139, Sec. 5901	The credit may not exceed the property tax, but if income tax liability is less than the credit the difference between the liability and the credit will be refunded.

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Table 10—State Use of a Personal Income Tax Credit-Rebate to Minimize or Offset the Regressivity of Sales and Property Taxes[1]

State	Type of Credit	Year Adopted	Amount of Credit	Law	Administrative Procedure
Wisconsin	For senior citizen homestead tax relief	1963	Varies, based on income and amount of property tax or rental payment	Chap. 71 (Sec. 71.09 (7) added by Ch. 566 (A.B. 301) eff. 6/10/64. Ch. 580 (A.B. 907) repealed & recreated Sec. 71.09(7) effective Dec. 19, 1964.)	Tax credit or refund to be claimed on income tax return. The Department of Taxation shall make available a separate schedule which shall call for the information necessary to administering this section and such schedule shall be attached to and filed with the Wisconsin income tax form. Cash refund granted if property tax credit exceeds State personal income tax due.
Washington, D.C. ..	For sales tax paid on food	1969	Varied, based on income[9] (credit applicable to low income taxpayers only)	P.L. 91-106 (H.R. 12982)	Tax credit or refund to be claimed on income tax return.

[1]If a taxpayer has no State personal income tax liability or a tax liability insufficient to absorb the entire credit (a negative tax credit situation) he is entitled to the appropriate cash refund. If the taxpayer's State personal liability is equal to or greater than the tax credit, his personal income tax liability is reduced by the amount of the credit (a positive tax credit situation).

[2]The credits for consumer-type taxes are based on "modified adjusted gross income" (regular taxable income plus exempt income such as social security benefits, life insurance proceeds, etc. and range from $21 per qualified exemption for taxpayers having a modified adjusted income of less than $1,000 to $1 per exemption where such income is between $8,000 and $9,999.

[3]Ranges from $12 per qualified exemption for taxpayers having taxable income under $1,000 to $0 where such income is over $7,000.

[4]Credits are only allowed if total taxable income of taxpayer and spouse, if any, does not exceed $5,000 for the taxable year.

[5]All homeowners residing in their own homes are allowed a direct reduction of their property taxes due by means of the Homestead Property Tax Credit. This credit amounts to 35 percent of the tax levy, excluding the amount levied for bonded indebtedness, to a maximum credit of $250. Senior citizen homeowners also receive this credit. Local governments are reimbursed for their tax loss from the state property tax relief fund.

[6]Elderly may choose this relief or senior citizen relief but not both.

[7]Ranges from $12 to $81 for taxpayers having less than $1,000 total household income to $0 to $36 for those having between $6,000 and $6,999 income, based on number of personal exemptions.

[8]The commissioner shall annually prepare and make available the local rate factors by arraying all municipalities according to their effective tax rate and dividing the population of the State into quintiles from such array with those having the lowest effective tax rates being in the first quintile. The local rate factors shall be as follows: first quintile, 0.6; second quintile, 0.8; third quintile, 1.0; fourth quintile, 1.2; fifth quintile, 1.4. The amount of property taxes or rent constituting property taxes used in computing the credit are limited to $300 per taxable year.

[9]Low income taxpayers (AGI not over $6,000) are allowed a credit ranging from $2 to $6 per personal exemption, depending upon the taxpayer's income bracket.

Source: ACIR, *State and Local Finances: Significant Features and Suggested Legislation, 1972 Edition* (M-74, 1972).

APPENDIX IX

How to overcome the inequalities of flat credit

The best way to avoid the difficulty of inequitable credits, say Leong and Rhyne, is to apply a rate to the difference between the claimants income and lower limit of his income bracket and deduct the product from the amount of tax credit suggested at each income bracket.[22]

eg: Let's say that the maximum credit per exemption for the group with income of less than $1000 is $20, according to sales taxes paid. For a person with income of $1000-1999, the credit of $20 is reduced by - (the product of his income in excess of $1000) x a rate (ex .005). If the income is $1100 or $100 in excess of $1000, he is entitled to $19.50 per exemption. With $2000 income, he is allowed $15 credit, which is $20 (the maximum credit allowable) - ($1000, amount over base, x .005, arbitrary percentage). Thus the amount of credit is reduced from each income bracket in inverse order until it reaches a point where income level does not have regressivity of taxes. This scheme, admits the authors, may complicate filing and cause administrative problems.

[22] Leong, Y.S. and Rhyne, Iola, "Hawaii's Inversely Graduated Tax Credits", National Tax Journal, Vol 22, 1969, p 455.

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Is the Property Tax Progressive?

A Potential Threat to School-Finance Reform

By ALLAN ODDEN

Legislators and other state officials should be on the alert for a relatively new view in tax analysis that, if it prevails, could undermine current efforts to reform property-tax policies related to school finance.

In essence, the revisionist view, now being debated primarily in academic hallways, maintains that property taxes are progressive rather than regressive—and that, therefore, reform may be unnecessary.

Supporters of the reform movement can take heart, however, because fresh research is clearly contradicting the claims of the revisionists. Thus, when the debate finally reaches the legislative level, the reformers should be well prepared to refute those claims.

Local property taxes, of course, constitute the single largest source of revenue for public elementary and secondary schools in the United States. Recent reform activities in school finance have focused on the fact that this heavy reliance on property taxes has produced inequalities in the ability of local school districts to raise money for school purposes.

This, in turn, has refocused attention on the tax, itself, with particular emphasis on property tax incidence—a reference to the percent of income a household pays for the tax.

The conventional wisdom of the past two decades has been that the property tax is regressive in incidence, taking proportionately more from low-income households than from high-income households.

Within the past few years, however, some academicians and public-finance scholars have begun to claim that the property tax is progressive, taking proportionately more from high-income households.

These two different views create a dilemma for state legislators. If, indeed, the property tax is progressive, as the revisionists claim, basic reform might not be necessary.

However, if the property tax is regressive, then the need for fundamental reform continues. In particular, we would still need the popular state-financed "circuit-breaker" programs of property-tax relief, which are specifically designed to reduce regressiv-

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Allan Odden is director of the ECS Education Finance Center.

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Under the revisionist view, it's irrelevant whether businesses or landlords shift property taxes to others.

ity by limiting tax payments to a percent of income.

Under the conventional view, the property tax is viewed as a nonuniform local tax, used and levied by thousands of local governments. As such it is considered an excise tax; its effect is to increase the costs of owning or renting a home and to increase the price of consumer goods that were produced by firms paying the tax.

The conventional analysis assumes that homeowners pay for the property taxes on their homes but that property taxes on business and rental properties are passed on to consumers and renters in the form of higher prices. When these assumptions are used to determine property-tax incidence, the results usually reveal a strong pattern of regressivity, especially for just that portion falling on homeowners.

The revisionist view of property-tax incidence takes an entirely different perspective. It maintains that since the property tax is used by nearly all local governments, it is, at heart, a uniform national tax on all real capital. As such, the property tax is considered a capital tax.

A capital tax and an excise tax have different effects. A capital tax may raise the price of some consumer goods, but it lowers the price of others. A uniform tax on all real capital, however, lowers investment earnings for all types of capital.

Thus, when the property tax is viewed as a capital tax, its major effect is to lower the investment returns to those who possess capital. Since capital is owned predominantly by persons with high incomes, the implication of the revisionist view is that the property tax has a progressive, rather than a regressive, pattern of incidence.

Under the revisionist view, the issue of whether businesses or landlords shift their property taxes to consumers and renters becomes irrelevant. The major effect of the property tax is to lower the investment returns to all those who own capital, thus producing a progressive pattern of incidence.

There are two major problems with the revisionist view. First, it holds that the property tax is a tax on *all* capital. In fact, the best estimates are that it reaches only 60 percent of the nation's capital. Although half of the remaining capital belongs to the government or to nonprofit corporations, the other half—20 percent of the nation's capital—is privately held and not subject to property taxation.

The second problem is that the re-

The research finds that property-tax incidence is regressive, no matter which perspective is used.

visionists see the property tax as a *uniform* tax. This is questionable. To begin with, more than 65,000 local governments have different property-tax rates. If special property-tax districts are included, the number of actual tax rates probably reaches into the hundreds of thousands. Furthermore, because assessment practices are not uniform, there are actually millions of effective tax rates across the country.

At the same time, the conventional view overstates the degree to which landlords can shift their property taxes to tenants in the form of higher rents, as well as the degree to which the business community can shift its property taxes to consumers in the form of higher prices. According to recent research, the shift in both cases is probably no more than 50 percent. That analysis represents a "middle view" of property-tax incidence and the one that is most realistic.

Although it is useful to know what the different theoretical perspectives are, the important thing is what the research shows about property-tax incidence.

We have a slight handicap here, since it is almost impossible—or at least prohibitively expensive—to determine precisely which groups ultimately pay what property taxes. The only practical research alternative is to impute tax payments to various household groups (according to income level) on the basis of certain assumptions drawn from a given theoretical perspective.

Working within that framework, however, the research finds that property-tax incidence is regressive no matter which perspective is used—the conventional, the revisionist or the middle view. This becomes clear in the accompanying graphs.

(Because the bulk of the population—about 85 percent—has income below $15,000 a year, the incidence pattern below that level is of most interest for the purposes of public policy.)

FIGURE 1 shows nationwide estimates of property-tax incidence based on the three perspectives. Significantly, the incidence pattern is regressive for incomes below $17,500 regardless of theoretical perspective.

For example, according to the revisionist view, the property tax takes 4.4 percent of household incomes between $4,000 and $5,700, but only 3.3 percent of incomes between $12,000 and $17,500.

According to the middle view, the tax takes 5.7 percent of incomes between $4,000 and $5,700 and just 3.7 percent of incomes between $12,000 and $17,500.

Even according to the revisionist view, the tax imposes a regressive burden on the bulk of the population.

A second important feature of these results is that the incidence for middle-income households ($12,000 to $17,500) does not vary greatly from one theoretical perspective to another, taking 3 to 4 percent from that group.

For those with high incomes, however, the incidence pattern is strongly related to the theoretical view used. The incidence varies from 0.8 percent according to the conventional view to 7.1 percent according to the revisionist view.

While the middle view, which best approximates the real behavior of the tax, yields an incidence of 3.3 percent for those with high incomes, the wide variation for the upper-income levels suggests the need for more research.

But the incidence pattern for the lower-income ranges is clear: Irrespective of theoretical orientation, the property tax is regressive.

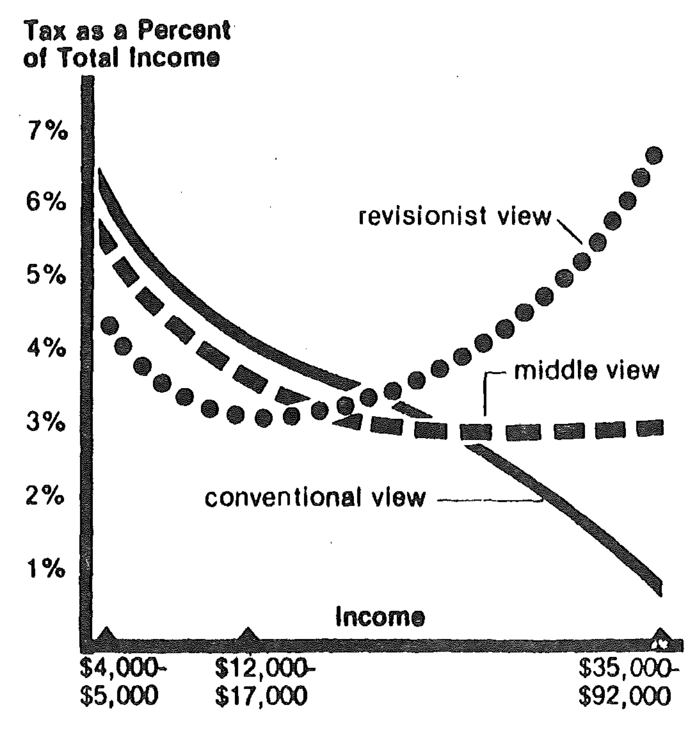
FIGURE 2 shows the incidence of the property tax within a single state—Minnesota (in 1971)—and gives a more accurate picture. This is because, although nationwide estimates may give rough approximations of incidence, the property tax is not national. Administered at the local level, it is usually regulated by a state agency.

The use and administration of Minnesota's property tax is similar to those in many Midwestern and Eastern states, so we can also expect their incidence patterns to be similar.

Note again that the incidence pat-

FIGURE 1

Nationwide Estimates of Property-Tax Incidence



SOURCE: RICHARD AND PEGGY MUSGRAVE, PUBLIC FINANCE IN THEORY AND PRACTICE (McGRAW HILL)

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School-finance structures cannot be equitable if their fiscal base—property taxation—is unfair.

tern is regressive for incomes below $15,000 according to all three perspectives, although it is less regressive under revisionist assumptions than under the middle view.

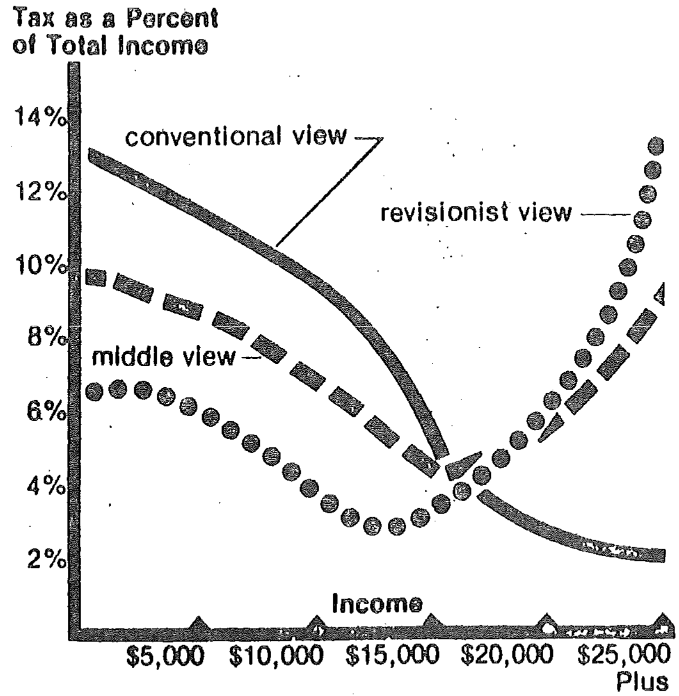
According to the middle view, Minnesota's property tax takes more than twice as much from those with low incomes as it does from those with middle incomes—10.2 percent of incomes less than $1,000 and only 4.3 percent of incomes between $10,000 and $15,000—a markedly regressive pattern. Even under the revisionist view, the pattern is still regressive.

(The incidence for those with higher incomes varies widely and definite conclusions cannot be drawn.)

FIGURE 3 shows the incidence of only the residential portion of Minnesota's property tax. It is highly regressive over all income ranges, taking 13.4 percent of household incomes less than $1,000, 4.9 percent of household incomes between $3,000 and $4,000, 2.7 percent of household incomes between $10,000 and $15,000 and only 1.4 percent of household incomes greater than $25,000.

FIGURE 2

Total Property-Tax Incidence in Minnesota, 1971



There can be only one conclusion. In spite of revisionist suggestions that there is "new hope for the property tax" [see COMPACT, February 1975], the new view is not supported by research. Even under the assumptions of the revisionist perspective, research shows the incidence to be regressive—extremely so for the residential portion of the tax.

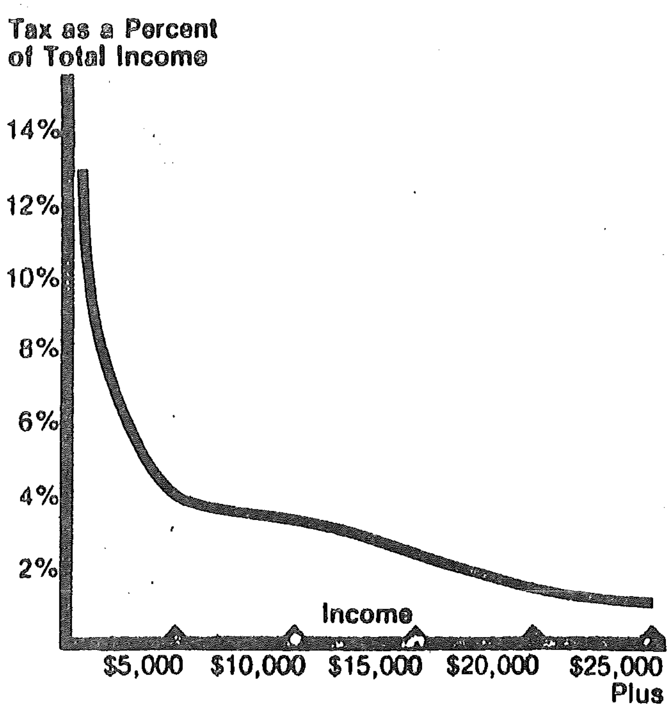
In short, the property tax still takes proportionately more from the low-income taxpayer than it does from the middle- or high-income taxpayer.

State legislators can thus be assured that their efforts over the last two decades to reform the property tax have not been in vain. There is still a great need to reduce the inequitable incidence of the tax. In particular, there is still a need for fully implemented state circuit-breaker programs of property tax relief.

School-finance reforms must continue to include tax reform on its agenda for change. School-finance structures cannot be equitable if their fiscal basis—property taxation—is unfair. No longer can school finance be concerned only with the details of state-aid formulas. Today school finance must begin and end with issues of state and local tax policy.

FIGURE 3

Residential Property-Tax Incidence in Minnesota, 1971



Property Taxes Aren't All That Bad

Los Angeles Times
SUNDAY, NOVEMBER 28, 1976

They Can Be a Fair Levy (1 Wealth

BY DONALD G. HAGMAN

This year's sharp property-tax increases have revived charges that the tax is oppressive—so high that it forces some persons to give up their homes—and is unfair. To defend the property tax is almost political suicide for a public official. But there is much to be said for its fairness and usefulness. Here, in the form of a discussion between me and hypothetical tax specialists, is an attempt to give the maligned property tax equal time.

Hagman: Is the property tax "too high?"

Specialists: All taxes are "too high" if you think government is too big. But the property tax probably is not "too high" in a relative sense: Only 18.5% of total state and local government revenues came from the property tax in 1976, down from 20.6% in 1954.

But federal aid to state and local governments increased considerably during that period, so the percentage of total state and local government revenues from the property tax should be down.

True. But even excluding federal aid, the property tax of states and localities in 1976 produced about the same percentage of revenues as in 1954—29% then, 30% now. Meanwhile, the percentage of state and local revenues raised by their own income taxes more than doubled.

So, if by "too high" one means that taxes are increasing rapidly, the income tax is the one that's "too high."

Yes.

But income taxes should increase because they are progressive and the property tax is regressive.

By progressive, you mean the richer a person is, the greater the percentage of his riches he pays in taxes.

Yes, and by regressive I mean that a poor person pays a greater percent for taxes than does a rich person.

The income tax is not all that progressive; indeed, a property tax may be more progressive than an income tax. The progressivity of the income tax is often judged by the ratio of taxes to adjusted gross income—the income left after loopholes.

Well, of course, the income tax could be reformed to make it more progressive.

Of course. Congress just passed and the President signed the Tax Reform Act of 1976, conceded to be the major revision since 1954. Yet the changes are so complex that no one can say whether it is more or less progressive than before. In any event, I wouldn't count on major revisions again in the near future.

Well, maybe the income tax isn't so progressive, but that doesn't make the property tax progressive.

Right, but wealth is more concentrated than income.

Please explain.

If you take the top layer of wealthy people, you will find that they own a greater percentage of total wealth than if you took the same top percentage of income earners and compared their income with total income.

Do you have any proof?

Yes. Prof. Mason Gaffney, UC Riverside, noted that most studies show that the top 10% of income receivers get about 30% of all income. He then cited 12 studies of various kinds of wealth—land, estates, corporate shares. One study showed that 1% of the wealthiest persons in America own 24% of the wealth. The other study showed that the 1% owned 28%.

Then, generally speaking, cuts in taxes on property make the rich richer and the poor poorer.

Yes.

So if I'm rich, I should demand a cut in the property tax.

Yes, but that wouldn't be very good public relations. Since cutting taxes for the rich is not an appealing argument, the rich like to hide behind a few poor old widows. For instance, here is this little old widow homeowner with a house worth say, $41,000, and an income of $4,000 ($1,200 over the poverty level). She is, it is alleged, being forced out of her house by property taxes, which in a high tax rate area in California would run about $1,300 per year.

Well, she really doesn't pay $1,300 in taxes. Under the California Senior Citizens Property

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Tax Assistance Law she would pay $182 of property taxes. The state pays the rest.

Well, I have forgotten for the moment; do the taxes paid by the state become a lien on the property and become due on transfer or death as in most states?

No, taxes paid by the state are a gift and are not collected later. The Legislature has upcoming hearings to implement Proposition 13 passed last June authorizing postponement of the rest of the tax.

That's a good deal compared with a little old lady tenant.

Do tenants pay property taxes?

Of course, as part of their rent.

But California has a tenant property tax relief act, too.

I know. The same little old widow tenant renting a $41,000 dwelling would get $46 of property tax relief, while the little old widow homeowner would get $1,118 of relief, plus deferral of the rest, if the Legislature implements Proposition 13.

That doesn't seem fair.

It isn't, particularly when the homeowner can deduct property taxes on his federal income tax return, but the tenant cannot.

Maybe property taxes should not be deductible from income taxes.

Deductions make the income tax less progressive. And since most homeowners are richer than most tenants, the rich get richer and the poor get poorer if you allow property tax deductions.

It does seem kind of harsh, however, to force little old widows out of their homes.

It also seems kind of harsh to deny young marrieds homes because little old widows are rattling around in homes too large for them, keeping them off the market by conspicuous consumption of housing and thus increasing their price. Just because a little old widow drove a Cadillac when she was a married matron shouldn't give her the right to do so when her income falls off and she can no longer afford it.

I see what you mean. Why should society keep the widow in her big house if she can't afford it, particularly if tenants indirectly end up paying a much larger share of taxes?

Of course, there is the argument that the little old widow really doesn't have a $41,000 house, because when she and her husband bought it 30 years ago they paid only $4,000.

That sounds like a pretty good argument.

It isn't. Property taxes are primarily based on wealth—that is, one's share of the property tax depends on one's share of the wealth. Say there are two property taxpayers in town. One just bought a house for $41,000 and another bought 30 years ago for $4,000 but the house is now worth $41,000. Both have equal ability to pay the property tax, since it is based on wealth, and both should pay equally.

But that makes it sound like people buy houses for investment rather than for shelter.

They do. How many people have you heard say, "I can't afford not to buy a house." They are looking for the capital appreciation and for the mortgage-interest and property-tax deductions on their homes, which they would not get if they rented.

There's also the exemption of imputed income.

What do you mean?

Suppose you had $50,000 to invest and you put it in a savings and loan acc[illegible] 7% interest. You would pay income tax on the $3,500 earned.

Right.

Of course, since you did so invest, you had to rent housing.

Right.

Assume the housing cost you the same as it would if you owned and lived in the house in which you invested the $50,000. How much income tax on the $50,000 would you pay if you had invested it in a house

None.

Of course, even though some income must have been imputed to it or you would be crazy to forego the $3,500 interest on the savings account. So the exemption of imputed income is another large rip-off by the homeowner of the other taxpayers.

You seem to take less than kindly to home owners. Shouldn't homeownership be encouraged?

Maybe, but there are a lot of worthy causes if we are looking for causes to subsidize. Should we subsidize home ownership, particularly in the Los Angeles basin where every additional single-family house decreases our opportunity to attain clean air in the basin? Clean air and single-family housing probably are incompatible.

Well, let's get back to the little old widow. She did not cause the increase in value, why should she be taxed out of her house?

The fact that she didn't cause the increase is precisely why she should be taxed. She just sat there, doing nothing, and because of the efforts of others in the community—the building of streets and supermarkets and new industrial plants and the like—her property increased in value. It is fair that the increase be recaptured by the community that created it.

But a lot of that increase was inflation. That's not a real increase.

Of course not, but the increase was not entirely due to inflation. You own a home don't you?

Of course, I couldn't afford not to.

How much has it increased in value?

About $12,000 a year for the last 10 years since I bought it.

And how much are your property taxes?

About $2,200.

And how much of the $12,000 per year is inflation?

Probably about half.

Have you added improvements to your house to cause the increase?

No.

Then you surely don't mean to say that while the community caused an increase of $6,000 per year in your house while you sat there doing nothing, that you couldn't afford to pay one-third of that back to the community? *I guess I could. On the other hand, I may not have the income.*

Didn't you borrow money to buy the house?

Yes.

Why can't you borrow again to pay the taxes; that is, use the annual increase in your borrowing power to pay the taxes?

I could. I guess people do, although it is hard, particularly for little old widows who don't have much income.

Perhaps the state should pass a law overcoming the barriers to refinancing housing so that increases in property values could easily be turned into income to pay taxes.

That would take care of the little old widow. She might even, in effect, convert her house into *an annuity sufficient to pay taxes, have a higher, secure income, yet continue to live in her house.*

There is another important aspect of property taxes: Lower taxes capitalize into higher home prices. Suppose you could buy a house for $10,000 which had property taxes of $500, or a house for $10,000 which had property taxes of $1,000. Which would you buy, everything else being equal?

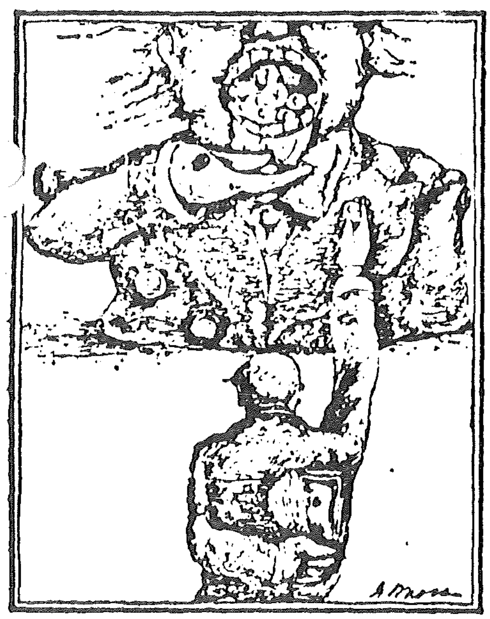
I'd buy the one with the lower taxes, of course.

So would everyone. In fact, you'd probably be willing to spend $12,000 or maybe even more for the lower-taxed house: Lower taxes make investment in certain property more attractive. If houses are undertaxed, that increases demand for them and hence increases price. The opposite is also true. Increase taxes on houses and prices would be lowered.

So if property taxes were increased, that would lower the initial price of housing, and more have-nots would be able to afford houses.

Yes, assuming they can pay the annual taxes, and most renters are already paying the equivalent in their rent. Acquiring enough wealth for the downpayment is the major problem for many tenants who would like to become owners.

But, as distinguished from years ago when property was truly an indication of ability to pay, we think of income or consumption as measuring ability to pay these days.



We do nowadays tax consumption by the sales tax and income by the income tax to reflect the changing assumptions about ability to pay. But wealth is still some indication of ability to pay.

There is, of course, the argument that property taxes should be paid only for property-related services. What about that?

You weren't paying attention before. Relative wealth is the principle behind the share of property taxes each person has the ability to pay. It has only some to do with how much service one gets.

But to some extent property taxes are for services, and surely things like welfare and education are not property-related—they are person-related.

Are they? Stop paying welfare in a community and what do you think would happen to property values? Welfare payments increase your home where you did without the neighborhood school?

No. But shouldn't some of the costs of these things be shifted to the state or the federal government?

Perhaps. Whichever collects the taxes, of course, may call the tune. Besides, a shift has little to do with who should pay the property tax. There is no assurance other than custom that the shift would lower property taxes. And since occupants are voters, they have some control over the amount of local expenditures by their control of how much property taxes are increased.

If all of these things you say are true, why is there such opposition to the property tax?

First, it is the tax hardest to pay—especially for homeowners who have paid off their mortgage and do not pay impoundments to the bank.

Second, taxpayers resent the assessment lag. Because the assessor doesn't get around to reassessing every year, you may have a 10% increase in market value every year which doesn't show up for, say, three years. That results in a 30% increase in taxes for one year even if rates do not change.

Don't people realize they were underassessed in the two previous years?

No, and most taxpayers do not save to pay for their increase in taxes when the assessor catches up.

Why doesn't the assessor assess every year?

It's too expensive, although many assessors are trying to do so and to use computers so that the costs of assessment can be kept low.

But aren't homeowners assessed at a higher ratio to fair market value than other property owners?

That is far from clear. State law requires assessments of most property at a 25% ratio. The assessor in Los Angeles County admits to assessing residential property at 22% and the latest U.S. Census survey shows the assessor assessing most property at 20% of value on average. While far from what it could be, assessment in Los Angeles County and in most urban California counties is probably as high in quality as anywhere in the world. The legal ripoffs are a far greater problem.

What do you mean by legal ripoffs?

I mean the loopholes that the state Legislature and the people by initiative keep putting in the law. At one time in most states, including California, all property was defined to be within the property tax base. With loopholes, the rates on everyone else's property goes up if the property tax is to produce the same amount of revenue.

Can you give me some examples of property tax loopholes?

Sure. Initially all property was in the tax base, and assessed at the same ratio. The Constitution gives the Legislature the right to tax or not tax or partially tax any personal property. As a result, only about $12 billion of personal property is in the tax base in California; about half of that is in business inventories and those inventories are assessed at half the normal 25% ratio. Land in California has an assessed value of $29 billion, but much of that is not assessed at market value. Over 20,000 square miles of California land is in agricultural or open-space preserves, assessed at 25% of use value rather than 25% of market value.

The homeowner's exemption in California reduces the assessed value of improvements on land from $43 billion to $37 billion. the Constitution by vote of the people. So the people have only themselves to blame for loopholes in the tax on real estate.

How much property is left within the property tax base?

We don't exactly know. I did a study a few years ago based on some research of the National Bureau of Economic Research and U.S. Census data and concluded that 59% of the total value of property in the United States as of 1962 was intangible property—stocks and bonds and the like. None of that property is subject to property taxes in California. The Bureau's study also estimated that national assets in the United States in 1968 were $7 trillion dollars. In about the same year the total assessed value of the United States was $0.5 trillion, meaning that assessed values were only about 7% of market values, down from estimates of 24% in 1900. These figures mean that if all property in the United States was assessed at market value, property tax rates could be 7% of what they are now.

Wouldn't it be a good idea to shift property taxes to commercial and industrial property?

Same result, the rich may become richer.

How so?

If taxes are increased on business, they are passed to labor or consumers, or absorbed by the the capitalist. If passed on, all consumers pay more, and the effect is regressive because the poor consume a greater proportion of their income than do the rich. If the capitalist is forced to absorb the tax, that may mean less investment causing more unemployment or lower wages, to which the poor are especially vulnerable.

Do all economists agree to all those statements?

No, they don't all agree. But many recent property tax studies give the property tax much better marks than it used to receive on the regressivity issue. Property tax reformers ought to be aware of some of these kinds of issues, assuming that the poor rather than the rich are the ones to be given tax relief.

Let's see if I have this right: You would recommend assessing all property at a uniform ratio of assessed value to market value and taxing all at the same rate; having more accurate, annual assessments and making the property tax easier to pay—similar to the ease with which income or sales taxes are paid. You would also have the state facilitate the conversion of capital invested in homes to income, particularly for the elderly. Further, you do not think the property tax should be increased on business property.

Your first statements are correct. The final one is not necessarily correct. It may be that California business is underburdened by taxes. There are many property tax exemptions that currently favor business and would be eliminated if all property were fully assessed for property taxes. Increasing taxes on business might be appropriate. The matter would take further study. Just keep in mind the consequences.

Will your recommendations be followed?

No.

Why not?

Mostly because facts don't count. Homeowners, for example, are a powerful voting group, and no politician can afford to offend them, whether the homeowners are right or wrong about their property taxes. There are

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PART 1: A SUMMARY OF THE CONCLUSIONS OF HUD'S NOVEMBER 1975 REPORT, PROPERTY TAX RELIEF PROGRAMS FOR THE ELDERLY

In brief, the highlights of the research conducted in the course of this Study can be summarized as follows:

(1) Existing state and local property tax relief efforts have achieved the magnitude of a major social program.

At the close of 1974, 48 states and the District of Columbia had authorized 83 different programs. The circuit breaker program type disbursed nearly $500 million in benefits to 3.2 million claimants of all ages in 1974, with an average relief payment of $143. Homestead exemptions, the other major program type, distributed in 1973 more than $1 billion in benefits to at least 6.3 million claimants of all ages, the average benefit standing at $173. The elderly received preferential treatment in all but three of the programs surveyed.

(2) Existing property tax relief programs appear to have at least five objectives in common:

- Reducing the regressivity of the property tax;
- Shielding low income households from large tax liabilities;
- Enabling the elderly to retain their homes;
- Slowing neighborhood deterioration; and
- Influencing voting behavior.

(3) Evidence on the attainment of the majority of program objectives is either mixed, scanty, or not presently available.

The regressivity of the property tax is itself subject to increasing question, and there is some evidence--not yet conclusive--that the tax may, on balance, prove to be mildly progressive. Programs do, however, offset large tax liabilities through rebates or tax credits that supplement the income of needy households, although vertical and horizontal "fairness" outcomes are uneven.

Evidence was found that the elderly rarely move for <u>any</u> reason; the role of property tax relief in influencing the decisions of those who do is presently unknown. No evidence suggesting that programs slow neighborhood decay was encountered; the relatively modest average program benefit makes this outcome appear implausible. There may be some impact of property tax relief programs on the voting behavior of the general population on public finance questions, but the effects on elderly voters appear to be minimal.

(4) In view of the uncertainty surrounding the degree to which existing state programs attain their objectives, a similarly-motivated federal program of property tax relief does not appear to be warranted.

The costs and distributional effects of a federal property tax relief program, based on existing program types could be considerable. Cost estimates made for this Study range as high as $5.7 billion annually for a federal program similar to that now used in Michigan to distribute benefits to eligible applicants of all ages. The distributional effects by region, income, age and tenure status of such a generous plan appear to fall short of an acceptable policy option. Again, if the Michigan plan were implemented nationally, the program cost could average as much as 19.4% of existing federal grants to the states, ranging from 30% in seven states to 5% in nine states.

(5) States and localities are likely to continue to employ current forms of property tax relief, even as they evaluate more effective and equitable options.

While modest programs of property tax relief will probably be continued, states and localities are less likely to initiate "super" circuit breaker programs.

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These programs, which offer benefits regardless of age and tenure and whose origins can, in part, be traced to the state budget surpluses that characterized the early 1970s, are in today's more restrictive economic climate considerably less attractive.

(6) Many states would welcome technical assistance in designing more effective property tax relief programs and in receiving information on new program concepts. Moreover, the need uncovered in the course of this Study for additional data collection and research in the property tax relief field is substantial, particularly as it affects the elderly, housing policy and community development.

(7) A new entity is proposed to meet these needs for technical assistance and ongoing research.

Provisionally called the National Property Tax Research and Assistance Center (NAPTRAC), the proposed new entity could focus the staff and resources of several federal and state agencies and the research community on meeting these needs for technical assistance and ongoing research over an initial five-year term. Additionally, it could conduct demonstration projects of promising alternatives to existing property tax relief programs and, where appropriate, make policy and legislative recommendations for consideration by both federal and state authorities.

In conclusion, it is clear that the property tax, for generations both an object of intense criticism and a vital source of revenue for the public good, is entering a new period of development. On the one hand, over the past five years, both state and local authorities have monitored with increasing care the resources available to support vital public services. On the other, further analysis of the economic and political effects of relief from this levy has challenged some of the traditional assumptions about the effectiveness and equity of property tax relief for low-income households, whether for the elderly or the general population.

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The confluence of these developments has already touched off sharp controversy over the most appropriate policy for alleviating the harsh financial circumstances of many Americans. In its simplest form, the question can be framed as follows: Is it more effective and equitable for government to intervene to ease some of these circumstances indirectly through relief of property tax liabilities, or should it rather adopt programs of direct income supplementation?

The debate continues. This Study has attempted to make a contribution toward its resolution by presenting an accurate picture of what is actually happening in property tax relief at the state and local level, by analyzing the effects of these programs on economic behavior, by identifying the options available to policymakers at the state level to fashion more equitable and efficient programs, and by concluding that, at the present time, no federal program of property tax relief appears warranted.

In an economy that is constantly changing, however, the public decisions that finally ensue can only temporarily reorder priorities and redress inequities. As Kenneth Wheare noted earlier in his book, Federal Government:

> There...can be no final solution to the allocation of financial resources in a federal system. There can only be adjustments and reallocations in the light of changing conditions.

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PART 2: A DESCRIPTION OF VARIOUS PROPERTY TAX RELIEF PROGRAMS CURRENTLY EXISTANT, FROM HUD'S PROPERTY TAX RELIEF PROGRAMS FOR THE ELDERLY.

2.2 Evolution and Current Status of Programs[2]

Some of the state programs giving residential property tax relief were implemented in the late nineteenth century. Their objectives were seldom made explicit in enabling legislation; in general, they reflected the notion that the state should help homesteaders who could not pay taxes on their property by allowing or requiring local governments to reduce the assessed value of their property by an arbitrary fixed-dollar amount. This relief mechanism, called a homestead exemption, was usually financed by the local tax jurisdiction either by reducing expenditures by the total amount of revenues foregone via the exemption or by increasing taxes on remaining fully-assessed properties to make up the difference.

During the 1930s and 1940s, variations of homestead exemption programs were instituted by many states throughout the country, often with the stated objective of "encouraging home ownership." Over the years the focus of tax relief shifted to elderly homeowners who were, as a class, believed to be more harshly affected by the property tax than the non-aged.

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[1] Advisory Commission on Intergovernmental Relations, Property Tax Circuit Breakers: Current Status and Policy Issues (Washington, D.C.: U.S. Government Printing Office, February 1975); Financing Schools and Property Tax Relief - A State Responsibility; The Property Tax in a Changing Environment (Washington, D.C.: U.S. Government Printing Office, March 1974).

[2] A detailed account of information presented here can be found in Bain, Compendium.

An additional refinement was also added to the previously open-ended eligibility criteria in general use: income ceilings were introduced by some states to restrict tax relief benefits to those households with incomes below specified levels. No homestead exemption program, however, used a family's income to determine the amount of exemption from property value which was to be permitted for taxing purposes. Rather, income--like age, place of residence, or proof of ownership--became one of several eligibility requirements which qualified all who met them for the same amount of exemption.

In 1964, Wisconsin implemented a new kind of property tax relief program, initially called a homestead tax credit by Wisconsin and later a circuit breaker by ACIR, which dramatically changed the direction of property tax relief throughout the country. Unlike earlier forms of property tax relief, the circuit breaker determines relief on the basis of a household's ability to pay its tax and thus incorporates household income into its relief formula. Generally, upper limits are placed on the amount of tax relief allowed or on the amount of property tax or assessed value which can be used to compute the rebate amount, both of which limit the value of property which is subject to property tax relief. In many cases, states require homeowners to pay a minimum amount in taxes so that the circuit breaker covers only a portion of the total liability. As income increases, so may the minimum, so that the relief of the more affluent is a smaller portion of the total tax liability.

Circuit breakers as a tax relief mechanism have not replaced the earlier homestead exemption programs; in fact, both types of relief measures are found in some states. But their growth in popularity (24 states and the District of Columbia have now passed circuit breaker legislation) has been rapid and far flung.

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All 50 states have enacted some form of property tax relief at some time, and 48 states currently operate--or permit localities to operate--a total of 83 different programs. The emphasis in most programs is on providing property tax relief benefits to elderly homeowners and other selected groups, such as the disabled and the blind. As is shown in Table 2-1, the range among states with regard to numbers of program participants, total benefits, and average benefits is large. Average benefits provided by circuit breakers, for example, range from $19 in West Virginia to $224 in Connecticut. Nevada's program serves only 643 households while Michigan's provides benefits to more than one million (elderly and non-elderly combined). Altogether, nearly half a billion dollars was distributed in circuit breaker benefits to 3.5 million households in 1974; the average payment was $143.

Data presented in Table 2-2 indicate that, despite the rise in popularity of circuit breakers, homestead exemption programs disburse substantially greater sums of property tax relief benefits to more recipients.[1] The homestead programs included in Table 2-2 provided over a billion dollars in benefits to six million recipients with an average benefit of $173.

The account of current program activity is complicated by the fact that seven states have both circuit breaker and homestead exemption programs in effect and seven other states have more than one homestead exemption program operating. This mixture of programs provides different levels of property tax relief to different taxpaying groups.

The perception of need which led each state to arrive at the program or programs it offers varies widely. Economic circumstances and the role played by the property tax in each state's overall revenue structure prevent one from concluding, for example, that Connecticut, with an average circuit breaker benefit of $224, is more generous than California

[1] The data in Table 2-2 represent only 17 of the 40 homestead programs known to exist. Figures for the circuit breaker programs, on the other hand, are for all known programs.

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Table 2-1

CIRCUIT BREAKER PROGRAMS

NUMBER OF PARTICIPANTS AND AVERAGE BENEFITS, CALENDAR YEAR 1974[1]

Program	Number of Participants	Total Benefits ($000)	Average Benefits
Elderly			
Arkansas	3,900	233	60
California	309,000	49,900	162
Connecticut	41,525	9,290	224
Kansas	59,000	8,600	146
Maine	15,000	3,100	210
Missouri	59,121	5,255	89
Nevada	643	71	110
Ohio	264,300	31,000	120
West Virginia	8,566	166	19
Subtotal[2]	761,000	108,000	142
Elderly & Selected Others (Disabled, Blind, etc.)[3]			
Colorado	28,000	2,500	89
Idaho	15,974	1,881	117
Illinois	105,783	16,737	158
Indiana	35,318	1,500	42
Iowa	42,940	3,156	74
Michigan[4]	289,000	59,509	206
Minnesota	113,000	10,300	91
Pennsylvania	391,481	53,274	136
Subtotal[2]	1,021,000	148,900	145
No Age Limitation			
Michigan[5]	723,000	90,806	126
Oregon	519,000	71,900	138
Vermont	26,204	4,997	191
Wisconsin	202,000	39,400	195
Subtotal[2]	1,470,000	207,100	141
Total[2]	3,253,000	464,000	143

Source: Survey of State Property Tax Relief Programs

[1] Arizona, the District of Columbia, Oklahoma, and North Dakota had not processed claims at the time of Survey.

[2] Columns may not add due to rounding.

[3] See description of eligible population in Section 7.1, The Compendium, for information on groups which each state include.

[4] Michigan also provides homestead exemptions to elderly claimants who received such relief in 1973 and who choose not to use the circuit breaker relief formula.

[5] Does not include any elderly or disabled claimants.

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Table 2-2

HOMESTEAD EXEMPTION PROGRAMS*

NUMBER OF PARTICIPANTS AND AVERAGE BENEFITS, CALENDAR YEAR 1973

Program Type	Number of Participants	Total Benefits ($000)	Average Benefits
Elderly			
Alaska	1,884	632	334
Florida[1]	303,723	12,900	42
Hawaii[1,2]	23,300	3,360	144
Illinois	381,745	42,947	113
Kentucky	152,000	10,000	70
Massachusetts	69,766	32,533	466
New Jersey	166,018	26,833	162
North Carolina	125,000	6,500	52
Washington	87,240	8,116	93
Subtotal[3]	1,311,000	140,000	108
Elderly & Disabled			
Mississippi[4]	104,500	6,785	65
Nebraska	43,065	9,447	219
South Carolina[1]	61,920	3,400	55
Tennessee[1]	61,000	2,830	46
Subtotal[3]	270,000	22,500	83
No Age Limitation			
California	3,473,000	700,000	200
Minnesota	899,000	186,100	207
Mississippi	418,000	25,000	60
Subtotal[3]	4,790,000	900,000	188
Total[3]	6,371,000	1,100,000	173

Source: Survey of State Property Tax Relief Programs

[1]Data are for calendar year 1972.

[2]Includes both the exemption for persons aged 60-69 and persons aged 70 and over.

[3]Columns may not add due to rounding.

[4]Based on estimates for calendar year 1975.

*Table 2-2 lists only those programs for which participants and benefit data were available at the time of the survey. A full listing of characteristics of all known programs is given in Section 9.3.

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with an average benefit of $162. It would be necessary to have data on individual tax liabilities before and after the application of tax relief in order to assess the value of each state's program to its recipients. Such data are, for the most part, not available. Compiling it is another area in which further analysis at both the federal and state level appears warranted.

In addition to homestead exemption and circuit breaker programs, five other kinds of property tax relief programs were identified in the Study. They are discussed in more detail in Section 4.0 of this Final Report and in the earlier Compendium. Briefly they are as follows:

(1) Local option programs exist in at least six states. In each case, the state government has enacted legislation permitting but not requiring localities to offer programs of property tax relief. Both homestead exemption and circuit breaker local option programs exist.

(2) Deferral programs are found in five states. Simply put, the deferral mechanism functions as a loan program, allowing eligible applicants to defer all or part of their property taxes until the property is transferred to a new owner. When the property title is transferred to an heir or buyer, the loan--consisting of cumulative deferred taxes (plus interest in some states)--is repaid to the taxing jurisdiction providing this form of relief.

(3) Tax freezes are used in two states. These programs hold property taxes at a set level--usually that paid by participants when they reached the age of 65.

(4) A low income comprehensive tax credit program has been used for two years in New Mexico. Unlike other programs described, New Mexico's program provides relief based on the average incidence of all taxes paid within the state and is adjusted for both family size and income. To receive benefits under this program, applicants need neither own nor rent property.

(5) Renter credit programs are found in four states and allow renters to deduct a specified amount from their annual state income tax liability (three states) or to reduce the amount of income they report for state income tax purposes by a specified amount (one state).

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Before leaving this summary description of the current status of state and local property tax relief programs, it will be useful to recapitulate some of the important distinctions between the two major program types as they commonly exist today:

Homestead exemption programs

- May use income as a relief eligibility criterion but not as a factor determining the amount of relief to be provided;
- Reduce the assessed value of the home and result in a lower tax bill. (Since renters do not receive property tax bills, they are not included in coverage under these programs);
- Have differential revenue impacts on communities within a given state if they are locally financed since effective tax rates differ greatly among taxing jurisdictions within each state, and
- Function much like a direct grant, offering the same amount of relief to those who are eligible, regardless of income.

Circuit breaker programs

- Use income as part of the formula determining the amount of relief a claimant is to receive; most set maximum income levels for eligibility,
- Pay benefits in the form of credit applied against state income tax liability or through a direct rebate (in nearly all cases, the property owner must first pay his tax and then receive a rebate from the state);
- Can include renters in coverage by establishing a percentage of rent paid (typically between 15% and 20%) as a proxy for property taxes paid;
- Counteract intrastate variations in the effective tax rate because they use actual tax liability, not an assessment reduction, to determine the amount of relief to be provided; and
- Function much like a negative income tax mechanism applied to property tax liability.

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2.3 Summary

Property tax relief has been a feature of local and state government in this country for 75 years. Homestead exemptions dominated the field until 1964 and, in fact, still provide more total tax relief to more homeowners than do circuit breakers. The latter have gained popularity in recent years, however, and presently extend nearly $500 million in property tax relief to 3.5 million households nationwide. Average relief per participating household is $143 under circuit breaker programs and $173 under homestead exemptions. The tax freeze and tax deferral approaches to property tax relief are used much less extensively across the country.

The recent rapid growth in the number of programs, the numbers of households covered, and the level of benefits provided can be explained in large part by three significant social and economic factors at work in the society during the past five years. The movement toward state-level fiscal reform coincided in many ways with the effects of property tax relief programs. State budget surpluses arising from the availability of federal revenue-sharing funds and generally increased state revenues caused by the rapidly expanding national economy of 1972-73 provided the resources to fund expanded or new property tax relief programs. Finally, the increasing awareness of the problems encountered by the elderly in achieving a dignified and independent way of life focused more attention on providing tax relief to this group than to any other.

With this review of the background and current status of property tax relief programs, it is important next to examine the objectives of these programs, a task to which Section 3.0 of this Report is devoted.

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The Elderly Face Special Problems

The proportion of income that the elderly pay for housing is a subject of especially sharp dispute among housing specialists and those who deal with the problems of older people.

According to a United State Census Bureau survey in 1975, elderly apartment renters in New York City generally pay a significantly higher part of income for their housing than do the city's apartment renters as a whole.

ratio for all the city's rental households to be 25 percent—that is, half the city's rental households were paying less than 25 percent of gross income for rent and utilities, and half were paying more.

But in apartments with male heads of household 65 years of age or older, the median rent-to-income ratio was 30 percent, and in apartments with female heads of household 65 or older the median rent-to-income ratio was more than 40 percent.

To many looking at these figures, it would seem that many of New York City's elderly, especially widows living alone, are in dire straits because so much of their often limited incomes are going for rent, leaving little to be spent on other items.

But some housing analysts insist that the Census Bureau figures make the overall situation appear more alarming than it is.

"By and large, people in older age brackets have made their major investments, are living off inventory and their needs outside food and rent are very minimal," says Frank S. Kristof of the Urban Development Corporation.

He and others note that elderly people do not have growing children to support, usually have reduced clothing and travel requirements and have Medicare to pay for a major part of their medical expenses.

Still others say that the elderly often live partly off savings and other assets, which are not reflected in Census Bureau surveys that measure income but

Elderly Face Special Problems

Continued from Page 1

which supplement income from such sources as Social Security and pensions.

While the proportion of income spent for housing tends to be higher for elderly renters, it tends to be lower for elderly homeowners because they frequently have paid off their mortgages, one housing researcher said.

Roberta Spohn, deputy commissioner of New York City's Department for the Aging, disagrees sharply.

"We're dealing with people with very low family incomes" for whom assets "are not a significant factor," she says of most elderly. In considering their rent payments, she says, "you have to think of it against what's left to live on."

Mrs. Spohn cites "tremendous increases in their cost of living not covered by increases in Social Security" and says that a sizable part of their usually larger medical costs are not covered by Medicare because of deductible and insurance requirements.

New York City's elderly population in particular, she says, was generally not able in its younger years to accumulate major assets. "Think of the nature of the city, what supported the economy and where these people came from—they worked in things like the needle trades and stores," she says.

She takes issue with one recent study that defines "excessive financial burden" for the low-income elderly as paying more than 35 percent of gross income for rent, rather than the 25 percent the study cites for the nonelderly poor.

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Tax Help For Renters

A number of states are taking steps to lower taxes for people who rent. At present in most states, renters can not deduct the money they pay for housing as property taxes, while homeowners can.

Indiana, for instance, allows renters to deduct from their state income taxes the total amount of rent paid, or $1000, whichever is less. Arizona permits renters to deduct 10% of their rent or $50, whichever is less.

Bills proposed in California and Colorado would benefit rent-payers by transferring liability for paying property taxes from landlord to tenant. As a result tenants could deduct property taxes from their state and federal taxes. A problem with the Arizona, Indiana, Colorado and California legislation is that it does not provide the benefits of "circuit breaker" legislation since most low-income people do not itemize their deductions.

"Circuit breaker" legislation gives tax rebates to homeowners and renters who pay more than a certain percentage of their income on rent or in property taxes. Michigan, Oregon, Vermont, and Wisconsin offer some type of rebate to homeowners and renters, while 11 states and the District of Columbia restrict such assistance only to homeowners and elderly renters.

Families' High Rent 'Burden' Called New Form of Housing Deprivation

By JOSEPH P. FRIED

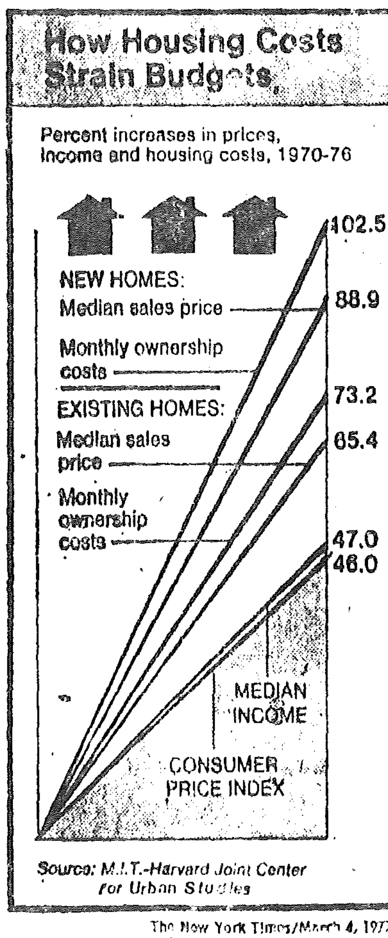
The rising portion of income needed to acquire adequate housing represents a significant new form of "housing deprivation" in the United States, according to a major study made public yesterday.

While physically inadequate housing remains a major problem, the study found that the excessive portions of income needed to acquire acceptable quarters had become a serious housing concern.

The report was compiled by the Joint Center for Urban Studies of Harvard University and the Massachusetts Institute of Technology. Those heading the research team concluded that, with poor and middle-income families increasingly unable to afford decent homes, and with housing production far below what was needed, "the United States has seriously fallen behind in meeting the housing needs of the American people."

The study also predicted that the kind of housing needed in coming years would generally be much different from what was needed in the 1950's and 1960's. Then, the housing industry focused on building large, single-family houses to accommodate the parents and children of the "baby-boom" years.

By the early 1980's, according to the researchers, the main demand will be for "moderate-sized houses" to accommodate the smaller families of the "grownups baby-boom children," who are expected to have fewer children.



Source: M.I.T.-Harvard Joint Center for Urban Studies

The New York Times/March 4, 1977

The principal authors of the 141-page study, who discussed their findings at a news conference at the Essex House in New York City, were Arthur P. Solomon, director of the M.I.T.-Harvard Joint Center for Urban Studies, and Bernard J. Frieden, former director and now a member of the center's faculty executive committee.

The center was founded in 1959.

In discussing what they consider the changing nature of housing deprivation, Mr. Solomon and Mr. Frieden gave the following figues, based on an analysis of Census Bureau data:

In 1960, they said, 15.3 million households in the country suffered from housing deprivation. Seventy-one percent of the total were families in physically inadequate houses or apartments, 5 percent were in physically adequate but overcrowded quarters and 24 percent were in physically adequate units that were not overcrowded but paid a "high rent burden."

A Contrast in Figures

By contrast, of the 12.8 million housing deprived families in 1973, 47 percent, or twice the proportion in 1960, were in the high-rent-burden category. Only 49 percent of the housing-deprived families in 1973 were in the physically inadequate group, with 4 percent in the overcrowded group.

A household with a high rent burden was defined as one having an annual income under $7,500 in 1960 or under $11,400 in 1973 and also falling in one of the following categories:

Having two or more people, with the head less than 65 years old, and paying more than 25 percent of income for rent, or having two or more people with the head 65 or over and paying more than 35 percent of income for rent.

The report said that its definition of a high-rent burden, and the definitions involving the other items of housing deprivation, led to conservative estimates of families having housing deprivation. The 12.8 million housing-deprived families reported for 1973 made up 18 percent of the nearly 70 million households in the country that year.

A Broader Picture

Nonetheless, the inclusion of rent burden as a form of housing deprivation provides a broader picture of housing deficiencies than does a concentration on physical inadequacy alone. In the 1960's, ing deprivation involved from 6 million government-commissioned reports that emphasized the physical aspects of slum- to 11 million families.

In discussing housing costs yesterday, Mr. Solomon said that "escalating costs are becoming the main housing problem not only for the poor, but are spreading upward to affect middle-income people as well."

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January 17, 1977

TAX POLICY DISCRIMINATES AGAINST TENANTS

The SPEAKER. Under a previous order of the House, the gentleman from Virginia (Mr. HARRIS) is recognized for 5 minutes.

Mr. HARRIS. Mr. Speaker, approximately 36 percent of all housing units in the United States are renter occupied. Tenants rent single family homes, townhouses, garden apartments, and high rises; and, they pay property taxes on these dwelling units. However, unlike other taxpayers, tenants—who pay their property taxes through their rent—are not currently allowed to claim their property tax payments for Federal income tax purposes.

There can be no question that a portion of a tenant's rent is a property tax payment: the local government sets the tax rate, the landlord adjusts his rent to collect the tax, the tenant pays the property tax through his rent, and the landlord passes it on to the local government. The property tax collected by the landlord is not and should not be considered as taxable income for the landlord. But certainly the tenants should have the same right as other taxpayers to claim the property tax payment for Federal income tax purposes; there is no reason why our tax laws should discriminate against the taxpayer who rents.

Along with 64 of my colleagues, I have introduced H.R. 81, the tenants' tax justice bill which allows tenants to claim their share of State and local property tax payments for Federal income tax purposes. This bill in no way reduces the advantages of homeownership, nor increases the tax burden on landlords. Simply, the bill extends property tax relief to tenants.

The text of the tenants' tax justice bill and my explanation appear on page H49-51 of the January 4, 1977, CONGRESSIONAL RECORD. I urge my colleagues who desire additional information about the bill to contact me. The list below indicates by State the percentage of dwelling units which are renter occupied:

PERCENTAGE OF DWELLING UNITS WHICH ARE RENTER OCCUPIED, BY STATE

(The occupants of these dwelling units, unlike other taxpayers, are currently denied the opportunity to claim their property tax payment for federal income tax purposes. Because of this discrimination, the federal income tax liability for these taxpayers is greater.)

[In percent]

Alabama	33.3
Alaska	49.7
Arizona	34.7
Arkansas	33.3
California	45.0
Colorado	36.6
Connecticut	37.5
Delaware	32.0
Dist. of Columbia	71.8
Florida	31.4
Georgia	38.9
Hawaii	53.1
Idaho	29.9
Illinois	40.6
Indiana	28.3
Iowa	28.3
Kansas	30.9
Kentucky	33.1
Louisiana	36.9
Maine	30.0
Maryland	41.2
Massachusetts	42.5
Michigan	25.6
Minnesota	28.5
Mississippi	33.7
Missouri	32.8
Montana	34.3
Nebraska	33.6
Nevada	61.5
New Hampshire	31.8
New Jersey	39.1
New Mexico	33.6
New York	52.7
North Carolina	34.6
North Dakota	31.6
Ohio	32.3
Oklahoma	30.8
Oregon	33.9
Pennsylvania	31.2
Rhode Island	42.1
South Carolina	33.9
South Dakota	30.4
Tennessee	33.3
Texas	35.3
Utah	30.6
Vermont	30.9
Virginia	37.0
Washington	33.2
West Virginia	31.1
Wisconsin	30.9
Wyoming	33.6

NOTE.—Percentages vary within States. For information regarding particular Congressional districts, please call Congressman Harris' office. This information was obtained from Congressional Districts in the 1970's.

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THE McKINSEY REPORT: TOWARD A NEW DEAL FOR RENTERS

By Peter Marcuse

New York City residents now pay at least $250 million more to Uncle Sam each year than the average national taxpayer, simply because the Federal tax system punishes people who rent homes and apartments and subsidizes people who own them. Nationally, the amount of the tax break given to home owners has been estimated at $9.7 *billion* dollars a year—a tax inequity that, despite its scale, is so widespread in its application that even Senator McGovern flinched from challenging it in his tax reform proposals. This inequity comes about because of the deductibility of real estate taxes and mortgage interest to home-owners, and the exclusion from their taxable income of the proceeds of their investment in their homes. (How this works is explained in a minute.) The existence of the inequity is generally conceded by experts in the field of taxation, but its full magnitude is little appreciated by the average citizen-taxpayer.

With a large majority of its residents rent-paying tenants, New York City is the chief victim. If it simply had the same proportion of tenants as the national average, the reduction in New Yorkers' tax payments to the Federal Government would be over $250 million (see footnote, next page). If *all* renters got the same tax break as owners now get, the total tax savings to New York's tenants would then rise to $350 million.

And even this understates the inequity. Tenants are in general in a lower tax bracket than home-owners. In New York, for instance, their median income in 1970 was $7,200, compared with $11,200 for owners. Instead of equalizing treatment of tenants and owners by giving them both tax deductions (which helps the higher-income owners even more), tenants would benefit if *neither* were given the deduction. The increased Federal revenue thus generated would be enough to increase everyone's personal exemption on the order of some $240. This would be a much more progressive solution, for even if tenants got a tax break comparable to that of owners, it would be of considerably less value to them because of their lower income.

What is it in the Federal tax system that produces these staggering inequities? Simply this:

The Federal tax system permits a home-owner to deduct local real estate taxes and even the interest on his mortgage payment from his gross income when he prepares his Federal income tax return. The effect is to *lower* the net income on which he is taxed. Such a deduction is not inherently required by logic or justice; it simply arises out of a Congressional policy implicitly favoring home-ownership. From the taxpayer's point of view, real estate taxes and interest are simply personal expenses, much like clothing or fuel. The fact that a tax deduction happens to attach to a real estate tax payment or a mortgage interest payment is, for the individual, simply a gratuitous blessing. For the homeowner, it is as if 50 per cent (or whatever proportion his real estate taxes and interest come to) of his annual housing expense were automatically allowed as a deduction to him. A tenant is permitted no such deduction, although he indirectly pays the same items as part of his rent. The landlord, who does get the deduction, has it as a business expense, which is what it really is, to *him*.

To add insult to injury, not only is the home-owner allowed to deduct something that *is not* a business expense to him, he is also *not* taxed on what *is*, in effect, business income. If a businessman buys a house as an investment and makes a monthly profit of $100 on it, after deducting all expenses, taxes, and interest, he must pay an income tax on the $100. But if he himself moves into the house, he escapes tax on the $100. This is called his "imputed net rent," and most calculations place the loss to the Federal treasury from non-taxation of imputed net rent as even larger than the loss from the deductibility of real estate taxes or mortgage interest.

These inequities have not gone entirely unchallenged. There are, in fact, several proposals afoot at least to ameliorate their results. One, in New York, is a bill introduced in the State Senate by Roy Goodman and William Conklin (SS 9795) that would shift the real estate tax from landlord to tenants, requiring (with some technical problems) a corresponding reduction in rent for the tenant. In the Congress, Representative Ed Koch has introduced a bill to amend the Federal Internal Revenue Code to permit the deduction by tenants of an amount equal to the tax their landlord pays. A third is the possibility, perhaps not even requiring supporting legislation, of drawing a legal instrument between landlord and tenant that shifts the legal liability for both interest and tax payment from landlord to tenant. It would, in effect, make the tenant the legal "owner" of his unit for the period of his occupancy, with the landlord repurchasing it at the termination of occupancy at such a price that the economic consequences of the real tenancy arrangement would be carried forward. (The Internal Revenue Service might look dubiously at such a document.)

One of the more elegant of the recent proposals dealing with the problem is one put forward by McKinsey and Com-

Most figures in this article are estimates from the limited data available, and rounded off on the conservative side. The McKinsey and Company figures cited here are based on their own calculations, based in some cases on original data and on calculations developed by them.

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pany, the well-known consulting firm, in a short report prepared for the city's Bureau of the Budget. It is a plan that would benefit the tenant slightly but achieve a major bonus for the treasury of the City of New York—a not surprising objective, since McKinsey was hired by the City to examine its tax situation.

The plan starts with a variation on the Goodman-Conklin-Koch approach: drop the real-estate tax on landlords, assess the same tax instead against tenants, and then provide that the landlord shall collect it from the tenant and pay it to the city. The beauty of the idea is that the landlord and the city are in the same position as before, but the tenants have picked up a deduction for income tax purposes worth, McKinsey calculates, about $107 per year for a family of four with a $7,000 annual income in New York City; $231 a year for a $17,500 family; $480 to a $27,500 family—these are all *after-tax cash savings*, not before-tax. The larger the family—thus, generally, the higher its rent—the greater the in-pocket cash savings. For example, for a tenant earning $12,500 the savings are $108 for a one-person household, but $174 for a six-person household, if each pays a typical rent for an uncontrolled unit.

Now add one more wrinkle, since McKinsey is working for the City of New York, not the National Tenants Organization. Impose a city tax (McKinsey calls it a "recoupment" tax) on the savings that each tenant would realize on his Federal income tax. The simplest plan, of course, is to make the city recoupment tax directly proportional to the Federal tax savings; McKinsey estimates that if the city taxes 80 per cent of the savings, it would make $131.2 million a year on the plan!

A more beautiful way of increasing city tax revenues could not be imagined by the most beleaguered Mayor. The city passes a simple ordinance, which provides a direct and tangible benefit to a large group of its citizens, and it recoups part of that benefit by a new tax that is simple, reliable, and incontrovertibly fair. And it leaves everyone better off than he was before—with the (locally irrelevant) exception of the Federal Government.

There are, of course, some inelegant flies in this inspired ointment for sick cities, but they might be pulled out without too much difficulty. The idea of directly taxing the actual amount of the Federal income tax savings received by each tenant was originally rejected by McKinsey as administratively unworkable and excessively slow in producing such tax revenue. As a realistic alternative, they suggested a recoupment tax fixed at a flat 6 per cent of all rental payments, exempting non-welfare families (why tax *them*, since the state and Federal government pay most of welfare families' rents?) with an annual gross income of under $6,000. This tax is administratively much easier to collect and results in nearly as much tax revenue for the city, estimated at $107 million for New York in 1971-1972. But such a flat tax could actually increase the total payments being made by some middle-income families in the $6,000-$15,000 income range. After some hesitation, McKinsey is finally recommending that the recoupment tax be directly on Federal income tax savings, thus ensuring the fairness of the tax, perhaps at 80 per cent. The city could overcome the delay—at a modest price—by selling tax anticipation notes, and McKinsey believes it has, or can, work out satisfactorily the administrative problems.

Some allocation formula has to be worked out for determining how much of the landlord's former real property taxes each tenant would pay in a multifamily building. McKinsey suggests making it proportional to the gross rent paid, certainly a simple method of handling the problem, if not necessarily the fairest. The city should not assume any increased burden of collection, or risk of noncollectibility, by shifting the tax from the landlord to the tenant; McKinsey suggests leaving the landlord secondarily liable for taxes. As a matter of fact, they whisper the suggestion that the landlord could be considered an agent or trustee for the state in collecting real property taxes from tenants, and be made criminally liable if he breached his trust by not remitting to the city taxes he had collected from tenants, thus strengthening rather than weakening existing enforcement procedures! The possible effect of such a procedure in slowing down the abandonment process is also hinted at.

The right to contest taxes would be given theoretically to a much larger number of people under the plan, and this could cause administrative problems. The report suggests that a 50 per cent consensus of tenants in a building might be required before a real property tax appeal for that building could be initiated, but that once initiated, the costs and benefits would be shared equally among all tenants.

Some problems are not spelled out in McKinsey's report. There is some danger that landlords might take advantage of the imposition of the new tax to raise rents. The plan itself neither justifies nor impedes such a rent increase. As long as rent control in some form exists, increases presumably could not be justified, since there is no real additional cost to the landlord. Apart from rent control, whatever forces produce the existing rent structure would have to be relied upon to avoid any additional burden on tenants.

Other effects of the plan are not dealt with in the McKinsey report. Clearly, as among tenants, its immediate impact is regressive. The deduction made available to high-income taxpayers is greater than that to lower-income ones. Since the recoupment tax only takes a percentage of the savings, it too will be regressive.

On the other hand, the plan is progressive in three ways. First, it makes available to rent-payers some of the deduction benefits already available to home owners. It thus reduces the heavily regressive features of the existing tax preferences for home-owners. Equally important, the plan really constitutes a form of unilateral revenue sharing between cities, now heavily dependent on regressive real property taxes, and the Federal Government, the major beneficiary of the more progressive income taxes. If we assume the Federal Government will raise tax rates enough to compensate for its loss, and the cities in turn will not raise real estate taxes, the net result would be a shift from a less to a more progressive tax. Finally, the distribution of the benefit will, for a change, favor those cities with a high level of multi-family occupancy—New York's is 87 per cent, compared with a national average of 27 per cent. The overwhelming odds are that cities with the largest numbers of poor will be the ones most benefited by the plan.

There is one final wrinkle to the McKinsey plan. If the recoupment tax is itself deductible on his income tax return, the benefit to the tenant and the possible level of recoupment might be even higher. In other words, taking the

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New York City example, the city could, by the simple shift in the incidence of the real property tax, do the Federal Government out of $164 million saved by those benefiting from the plan. These beneficiaries would deduct $131.2 million of that total from their Federal tax, even further increasing the loss to the national treasury, and even further increasing the amount that the city could justifiably corral.

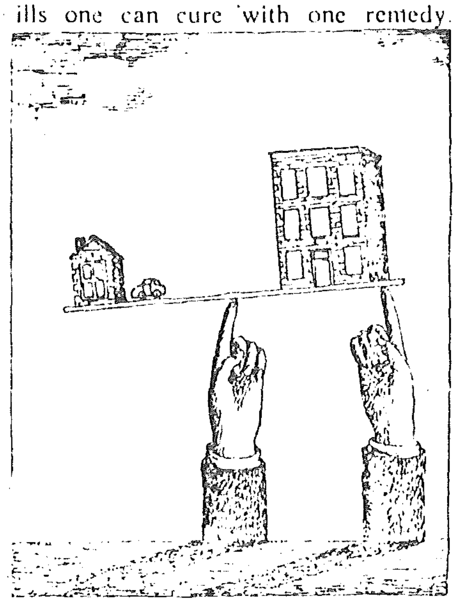
The plan might require a change in the Internal Revenue Code; the McKinsey report suggests that it would, although if the tax were properly formulated it should be held deductible under the Code's Section 164. Payments under California and Hawaii laws imposing real property taxes on lessees rather than owners of real property have been ruled deductible by the Service. The situations may be distinguished, and perhaps an advanced ruling should be required. Senators Goodman and Conklin were insecure enough on the point to make their bill contingent on a favorable ruling by the Internal Revenue Service.

Even if the Internal Revenue Code now permits the plan to become effective, the outrage of Congress at being so neatly hung by the logic of its own favoritism for home-owners might find expression: McKinsey's unilateral revenue-sharing scheme, then, would not be countenanced for long. A political battle might well be the result.

As far as the New York State income tax goes, the authors of the plan simply take it for granted that the Legislature would prohibit any cavalier deductions for state income tax purposes at the same time that it passed the enabling legislation needed to get the Federal deductions.

Other tax advantages of ownership over tenancy are not touched in the McKinsey plan. The owner-occupant can still deduct the interest paid on his mortgage, while the tenant receives no benefit from the interest his landlord pays. Even more, the exemption from tax of the imputed income on the homeowner's investment in his home remains untouched. And perhaps there should be a local recoupment tax on the homeowner's real estate tax deduction, too?

But there is a limit to the number of ills one can cure with one remedy.



The report does argue that the inner city may be assisted as a whole compared with the suburbs, although the relative attractiveness of co-operative and condominium ownership might also be diminished somewhat. The deductibility of real estate taxes has always been one of their advantages.

So, the McKinsey plan essentially has two quite separate components. The first is the simple extension to tenants, as well as to owners, of the deduction from income taxes for local real property taxes by having them pay real property taxes directly rather than as part of their rent. It is hard to argue with the logic of that suggestion. The second component, in the short run, appears equally logical. Having given a tremendous new benefit to a select group of taxpayers, the city should have the right to share in the benefits it has itself created for them. The McKinsey plan is one of the most aesthetically pleasing tax schemes that have come down the pipeline in a long time! It isn't often these days that city governments are able to beat the Feds financially and logically at their own game.

But all this still assumes that the deductibility of taxes and mortgage interest (and non-taxation of imputed rent) is here to stay for home-owners. If it is, New York City should certainly do what it can to equalize the situations for its tenants, and it can hardly be blamed for planning to share in their new benefit. But the argument for broader reform is compelling. The regressive nature of the home-owners' deduction has already been pointed out. The implicit subsidy the deductions confer upon higher-income taxpayers is in striking contrast to the sums paid out to subsidize lower-income families who cannot afford decent housing at market prices: $8.7 billion to the indirectly subsidized higher-income each year . . . as compared to a *total* Federal expenditure on *all* lower-income housing programs put together (including public housing; Sections 235 and 236 lower-income housing; rent supplements; rehabilitation, etc.) of substantially less than $3 billion. If Congress wants to put $11.7 billion into housing, there must be a more equitable, efficient, and accountable way to distribute the equivalent of 6 per cent of the Federal budget.

Finally, the long-term but less tangible costs of a tax system that grossly favors home-ownership may exceed even its short-term unfairness. Some 73 per cent of our housing is today single-family housing. It is this form of construction that has created the mushrooming suburbs of megalopolis, that has eaten up open space, accelerated inner city deterioration, forced miles upon miles of highway construction, rendered mass transit outdated, and accentuated segregation by race and by income. Yet single-family home-ownership is precisely what the tax laws foster, since 93 per cent of all owner-occupied units are one-family houses. As the distinguished Douglas Commission pointed out, it would be almost financial madness for an upper-income taxpayer to give up the home-owner benefits of the Internal Revenue Code in order to rent. The entire system of tax favoritism for home-ownership ought to be done away with.

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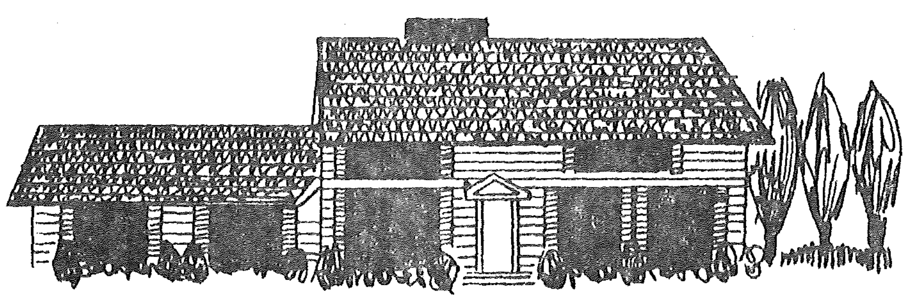
The Report
Of The Select Committee
On State Property Tax Valuation

Is The State Valuation Accurate?



February 1977

1. INTRODUCTION

Of all the issues that swarm about the Uniform Property Tax (UPT), the state levied property tax in Maine - Does the state property tax erode the local control of schools? Is the tax too burdensome? Are property taxes generally regressive? - perhaps the most basic is whether or not the UPT is based on an accurate valuation of property? Does the state's Bureau of Taxation correctly judge the full value of each locality's property in arriving at its state valuation?

The purpose of this committee is to determine just how accurate is the state's valuation of property and to suggest what improvements are needed.[1/]

Our general conclusions are that while the state valuation is conservative and reasonably accurate and will improve with each year, there are still significant changes needed. Some of these changes are administrative, some demand legislation and a few need modest increased funding.

But before we describe exactly what must be done, it is important to understand clearly the role of the state valuation and the current standards followed by the state and each locality.

2. WHAT IS THE STATE VALUATION?

The state valuation is the Bureau of Taxation's total estimate of the market value of all property in the state. The state has been making this estimate for many, many years and it is used primarily today:

1/ See Appendix A, Study Order S.P. 610.

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A. As the valuation against which the mill rate of the Uniform Property Tax (UPT)[2/] is levied; and

B. As a factor in the equations used to equalize the distribution of financial assistance to local governments for purposes such as health and welfare, road maintenance, state-municipal revenue sharing.

The Maine Constitution requires that any property tax must be assessed at its market value ("just value")[3/]. Why does the state feel it has to make its own estimates rather than simply adding up the results of each local assessor?[4/] There are two main reasons:

A. Many towns do not frequently update the valuations of their property; and

B. Most towns do not assess at full market value but rather fix the value of each house at a percentage of its true value. This "assessment ratio" is often quite low[5/] and the lower it is the less likely it is to be correct.[6/] The crucial importance

---

2/ There are currently two state property taxes: The Uniform Property Tax (UPT), which has been used to fund approximately 50% of the cost of education, and the Local and State Government Tax, which is used to tax the Unorganized Territory to pay for their municipal services.

3/ Maine Constitution, Article 14, section 8.

4/ There are no local assessors in the Unorganized Territory and the state would assess the property there whether or not there was an UPT or equalizing financial assistance formulas.

5/ This is one reason why one town may have a tax rate higher than a town with similar property and similar expenses. If one local assessor values his town's property at 40% of its market value and the other town assessor uses a 80% ratio, then the former town's mill rate will be double the latter town's rate.

6/ In Massachusetts a study has shown that towns and cities which assess residential properties near their full value have a five times better chance of avoiding inaccuracies (e.g., undervaluing expensive properties and overvaluing poor properties) than those localities assessing at the lowest assessment ratios. See Lincoln Institute of Land Policy, A Study of the Interrelationship of Massachusetts Assessment Level and Assessment Quality (July 20,1976).

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of at least beginning with a full value estimate is explained at length in Appendix B.

So the State makes its own assessments of the market value of Maine property. How is it done?

3. HOW THE BUREAU OF TAXATION ARRIVES AT THE STATE VALUATION.

The state valuation is now updated every year. It consists of:

A. The Bureau's individual valuation of each piece of property in the Unorganized Territory; and

B. The Bureau's gross valuation of each of 497 municipalities in Organized Territory.

In the Unorganized Territory the Bureau is the "local" assessor and has achieved fair accuracy.[7/] The other question before this committee was whether the Bureau's "gross" valuation techniques in the Organized Territory were accurate. The basis of the Bureau's estimate is the sales-ratio study. This is how the Bureau did the state valuation for April 1, 1977:[8/]

A. The state valuation of the municipalities is determined basically by comparing sales information with valuations used by the local assessor. It takes approximately one year for the field personnel to cover all 497 municipalities. The Bureau's personnel compiled from the local Registry of Deeds information on recent sales transaction.

7/ The Bureau's assessment ratio for the Unorganized Territory is 71%, which is above that currently required to be achieved by all localities by 1979. For a further explanation of this rating, see Section 4, TO WHAT STATUTORY STANDARDS ARE THE LOCAL ASSESSORS HELD?

8/ This description is based upon a more complete version contained in the Bureau of Taxation's 1976 memo to the committee, "The Maine State Valuation".

B. The field personnel took the sales information to each municipality for discusssion with the local assessors. The assessors then advised the Bureau as to those sales which were not representative of fair market sales, such as family sales, and sales containing good will or personal property or sales with abnormally inflated prices. These sales were eliminated.

C. A sales ratio study was performed on the remaining sales:

(1) A sales ratio study lists the sales in ascending order according to the percentage of valuation of the sales price to the assessed value. From this study an average was determined.

(2) Where sufficient sales were available and where sales representated the various categories of property located within the municipality, this average ratio was then applied to the total municipal valuation of the municipality as reflected in the municipal valuation book. For example, if it was found that the average ratio in the sales ratio study was 50%, the total valuation arrived at by the municipal assessor would be doubled to obtain the 100% market value state valuation.

(3) The sales study was broken down into the various categories of property in the municipality, such as seasonal property, residential property, commercial property and farmland. An average ratio for each of these groups was obtained where necessary because of the different ratios used by assessors for various categories of property. In other cases it was necessary for the fieldman

to apply a judgment factor as to the ratio which was being applied to such areas as commercial properties, woodland properties, etc., where there was inadequate sales information.

(4) In those municipalities affected by the Tree Growth Tax Law, the values used for land classified under that Law are the productivity values established through the statutory formula. In many woodland towns and plantations this makes up a very large share of the State Valuation.

(5) Each of these studies, upon completion, were forwarded to the central office of the Bureau where they were reviewed for consistency and uniformity to ensure that the work of the various field personnel reflected an equalized valuation in each case. Adjustments were made by the office in those areas where sales information was lacking and it was sometimes necessary to use information on values from surrounding areas. All municipalities in a geographical or economic area were reviewed together to determine that increases reflected in the sales study were uniform for the area and reflected the general inflationary pattern.

(6) The Bureau then met with each local assessor to discuss that municipality's proposed state valuation and to find any possible errors. A final proposed state valuation was arrived at and each municipality had 45 days to appeal to the Municipal Valuation Appeals Board.

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This appeals process completed the 1977 state valuation. It was filed with the Secretary of State in January 1977. It was accomplished by 7-9 fieldmen and a field supervisor. Of the 497 municipalities, only 36 appealed their valuation to the Appeals Board.

From this description it is clear that no matter how accurate the Bureau's sales information, if the local assessor's valuations are poor, the state valuation will be directly influenced. Before listing our findings and recommendations, it is necessary to explain exactly what standards, by statute, the local assessor is held to.

4. TO WHAT STATUTORY STANDARDS ARE THE LOCAL ASSESSORS HELD?

It is very important to affirm the relationship of accurate valuations by the local assessor to the general accuracy of the state valuation. Indeed, many of our conclusions and recommendations speak directly to this relationship. By statute the local assessor must meet the following standards:[9]

A. Minimum assessment ratios. By 1979 each local assessor must value property at no less than 70% of its full market value.

B. Maximum assessment quality rating. By 1979 the local assessor must achieve an assessment quality rating of no less than 20. What is a quality rating? How is it arrived at? This is important to understand because it reveals exactly how the property tax can be an inequitable levy. The assessment quality rating is another name for coefficient of dispersion. This is how it is determined:

9/ See 36 MRSA §§ 327,328.

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HOW TO FIND THE TYPICAL ASSESSMENT ERROR: AN ILLUSTRATION 10/

Suppose we have four houses, each of which sold for $30,000. The assessment rolls show the homes assessed at $10,000, $16,000, $22,000, and $28,000. (Remember, they should have been assessed the same.) The assessment-sales price ratios for the three would be

1) $\frac{\$10,000}{\$30,000} = 33\%$ 2) $\frac{\$16,000}{\$30,000} = 53\%$

3) $\frac{\$22,000}{\$30,000} = 73\%$ 4) $\frac{\$28,000}{\$30,000} = 93\%$

To find the median, we rank the four in order, from highest to lowest:

93
73
53
33

Since there are an even number of ratios, we take the middle two and find the halfway point between them:

$$\begin{array}{r} 73 \\ +\ 53 \\ \hline 126 \end{array} \qquad 126 \div 2 = 63$$

Thus the median assessment-sales price ratio, or common assessment level, is 63 percent.

Now we want to find the average deviation from this common level — that is, how much, on the average, each individual assessment was off the mark.

First we find the difference between the common level — the average assessment-sales price ratio — and the ratio for each individual assessment.

$$\begin{array}{r} 63 \\ -\ 33 \\ \hline 30 \end{array} \quad \begin{array}{r} 63 \\ -\ 53 \\ \hline 10 \end{array} \quad \begin{array}{r} 63 \\ -\ 73 \\ \hline -\ 10 \end{array} \quad \begin{array}{r} 63 \\ -\ 93 \\ \hline -\ 30 \end{array}$$

(We can disregard plus or minus signs.)

Next we find the average of these differences.

$$\begin{array}{r} 30 \\ 10 \\ 10 \\ 30 \\ \hline 80 \end{array} \qquad 80 \div 4 = 20$$

Thus the average assessment error is 20 percent.

Finally we express this average difference as a percent of the common level:

$$20 \div 63 = .32$$

10/ Brandon, Rowe, Stanton, Tax Politics 216 (1976). This analysis uses the mediam ratio to reflect the assessment quality rating. This practice parallels the Committee's Recommendation No. 4. See Sections 6, THE COMMITTEE'S RECOMMENDATIONS.

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Thus, the assessment quality rating is 32. In other words, the typical assessment was 32 percent higher or lower than it should have been. This means there could be a 64 percent gap between the assessments of two homeowners who should have been assessed exactly the same.

C. Annual sales ratio studies. Local assessors must perform annual sales ratio studies and must inspect each piece of property at least every four years.

Each of these local assessment standards are immensely important to the accuracy of the state valuation. Is the mandated quality assessment rating of 20 unduly rigorous? Here is what the authors of Tax Politics, a citizen's guide to taxation say:[11]

> The lower [the quality assessment rating] is, the more uniform assessments are generally. How low should it be? If it is 10 or less, the assessor is doing a respectable job. If it is more than 15%, he is doing poorly. Experts consider a typical assessment error of between 10 percent and 15 percent, plus or minus, to be acceptable. Some go as high as 20 percent, mainly in compromise to what they perceive as the situation today. If it is over 20 percent, the sooner you get a new assessor, the better. [An assessment quality rating] of over 20 means that every taxpayer, on the average, is assessed 20 percent too high or too low, and there are taxpayers who are paying twice as much tax as others even though they should be paying exactly the same.
>
> Assessors who get their typical error down to 5 percent to 10 percent deserve applause. Since market values change constantly, there are genuine problems in cutting the error much below that.

11/ Brandon, Rowe, Stanton, Tax Politics 216-217 (1976).

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The statutory requirement of an assessment quality rating of 20 is not effective until 1979. Here are recent average quality ratings, based on the 1975 state valuation, for Maine's counties:[12]

Androscoggin	39.6
Aroostook	49.9
Cumberland	25.2
Franklin	31.3
Hancock	38.8
Kennebec	32.0
Knox	41.0
Lincoln	39.2
Oxford	26.9
Penobscot	38.2
Piscataquis	36.8
Sagadahoc	37.2
Somerset	38.6
Waldo	42.0
Washington	44.0
York	22.1
Average of Counties	36.4

12/ Prepared by the Bureau of Taxation; 70 municipalities had insufficient sales for assessment quality rating purposes.

Other statutory local assessing standings - such as required tax maps, uniform accounting systems, or mandatory use of electronic processing - are non-existant. At one time such standards were required by the Bureau of Taxation but local reluctance to have their affairs directed from Augusta results in their repeal.[13]

With this introduction to the procedures of the state valuation and the local assessing standards which directly affect the accuracy of the state valuation, we can now turn to the committee's main conclusions and recommendations.

5. THE COMMITTEE'S MAIN CONCLUSIONS

The committee's conclusions result from our lengthy schooling in the procedures used by the Bureau of Taxation to reach the state valuation, from our consultations with many of the country's leading property tax experts and from our close working relationship with Thomas L. Jacobs and Associates, the consultants employed by the committee.

Appendix C is the report of Jacobs and Associates to the committee. [Hereafter referred to as the Jacobs Report.] We endorse its analyses, conclusions and recommendations. All interested persons are urged to read it in its entirety.

For this report the committee will summarize the main conclusions and recommendations of the Jacobs Report but will also include other conclusions and recommendations that grew out of the committee's many months of study.

13/ See Public Laws, Chapter 545.

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A. <u>Conclusion No. 1.</u> The state valuation produced by the Bureau of Taxation seems reasonably accurate. Greater accuracy, however, is needed and is possible with minimum expenditure of money. <u>See Jacobs Report</u> pages 21-22.

B. <u>Conclusion No. 2.</u> The Bureau's method of arriving at the full market value of each locality's property by adjusting the local assessor's valuations according to recent sales information (<u>see</u> Section 3 of this Report) is sound and proper. However, even greater accuracy could be achieved by:

(1) more accurate classifications of property according to their use (residential, seasonal, etc.);

(2) a series of on-location appraisals by state personal to supplement inadequate sales information.

<u>See Jacobs Report</u>, pages 22-29.

C. <u>Conclusion No. 3.</u> There are two questions concerning the accuracy of state valuation: Is it inflated? Is it uniform?

(1) The state valuation seems <u>conservative</u> in representing the full value of taxable property in the respective municipalities. Such conservatism promotes stability in the property tax base.

(2) The state valuation seems reasonably <u>uniform</u> among most of Maine's communities.

<u>See Jacobs Report</u>, pages 29-38.

D. <u>Conclusion No. 4.</u> In the perceptions of local assessors there is little dissatisfaction about the state valuation and the job the Bureau of Taxation is doing. However,

(1) The local assessor, whose accuracy is very important to the accuracy of the state valuation, is desireous for

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state assistance in meeting the statutorily prescribed local assessing standards (see Section 5 of this report); and (2) The Bureau needs additional staff if the accuracy of the state valuation is to be improved.

See Jacobs Report, pages 38-40.

E. Conclusion No. 5. The Bureau of Taxation's assessment of all property in the Unorganized Territory is considerably below full market value (an assessment ratio of 71%). While this is slightly better than the standard the local assessor will be held to by 1979, there is still need for improvement. See Jacobs Report, page 40.

F. Conclusion No. 6. If property taxes are to be accepted by the Maine public, not only is general accuracy necessary but also needed is an improved means of appeal of questionable assessments and more informative tax bills.

6. THE COMMITTEE'S RECOMMENDATIONS

A. Recommendation No. 1 -- Complete support should be extended by the State and local government officials to a commitment and practice of firm enforcement of the legislation assessment standards (see Section 5 of this report). Concurrently, the Property Tax Division should design and carry out a more extensive program of technical assistance to the local assessors. See Jacobs Report, pages 57-58. This recommendation will necessitate expenditures totaling this biennium $260,000 and the creation of 10 new positions. Of all our recommendations, the Committee places the highest priority on this one and will introduce emergency legislation for the necessary appropriation.

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B. Recommendation No.2 -- The Property Tax Division should establish procedures and instructions to require that sales prices are compared with the assessments of the properties just preceding the date of the sale. See Jacobs Report, page 46.

C. Recommendation No.3 -- Statutory requirement should be established for the Property Tax Division to conduct annual assessment-sales ratio studies applicable to each municipality or assessing jurisdiction, and to publish the results of these studies. See Jacobs Report, pages 46-47.

D. Recommendation No. 4 -- The Property Tax Division should incorporate the results and analyses of the sales ratio studies in an information system and exchange with the respective municipalities. See Jacobs Report, pages 46-47.

E. Recommendation No. 5 -- The Property Tax Division in reporting the results of sales ratio studies should use the median ratio to reflect the over-all level of assessments, and the assessment quality rating (coefficient of dispersion: one-half the interquartile range divided by the median) to reflect the quality of assessments. See Jacobs Report, pages 47-48.

F. Recommendation No. 6 -- The statutory assessment standards for rating of assessments should be adjusted to provide for a maximum assessment quality rating of 18 by 1979 and thereafter, measured by the coefficient of dispersion. See Jacobs Report, pages 47-48.

G. Recommendation No. 7 -- The Select Committee on State Property Tax Valuation reaffirms the abosolute necessity for a certified statement of the consideration in all real estate transfer transactions, to be provided in an appropriate form. See Jacobs Report, pa 48-49.

H. Recommendation No. 8 -- Legislation should be adopted to require that all municipalities classify all parcels of property on their assessment roll according to the standard property classification system and any additional special categories that are significant in their municipality, and that the municipalities report to the State Bureau of Taxation the totals of assessed values for these classes on their municipal valuation returns. The standard classification system should include but not be limited to the following classes:

- Residential improved
- Residential vacant
- Commercial improved
- Commercial vacant
- Industrial improved
- Industrial vacant
- Agricultural improved
- Agricultural vacant

See Jacobs Report, pages 50-51.

I. Recommendation No. 9 -- The Property Tax Division should make full value appraisals of a sample of properties, where required in municipalities where there are an inadequate number of sales to produce a valid assessment-sales analysis. The goal, as in cases where there are sufficient sales, should be a sample of about 4% of the number of parcels in the municipality, which in the municipalities concerned would be a combination of sales and appraisals. See Jacobs Report, page 52.

J. Recommendation No.10 -- Legislation should be adopted to assign responsibility to the Property Tax Division to appraise at full value all industrial property in the state with a value

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over $1,000,000 and all operating utility property subject to taxation, to require the Property Tax Division to certify such individual full value appraisals to the municipalities where the properties are located, to require the municipalities to use these appraisals as the basis for their assessed value of the individual properties, and to provide for the financing of this appraisal service from State funds. See Jacobs Report, pages 54-55. This recommendation will necessitate a total expenditure for the next two years of $300,000 and the creation of 10 new positions. (An alternative approach deserving further consideration would be to tax public utilities through a state excise tax with revenues returned to the appropriate communities. The Committe did not have time to properly consider this approach.)

K. Recommendation No. 11 -- The Property Tax Division, in assessing property in the Unorganized Territory, should update its appraisal standards to more nearly approximate current values, and should institute systems to maintain the values at a more current level. See Jacobs Report, pages 55-56. This recommendation will necessitate a total expenditure for the next two years of $60,500 and the creation of two new positions.

L. Recommendation No. 12 -- The Property Tax Division should be provided with sufficient manpower and other resources to effectively carry out its on-going and expanded duties -- at a level to fulfill its increased workload and to accomplish the necessary improvements in property tax administration. See Jacobs Report, pages 57-58.

M. Recommendation No. 13 -- A review should be made of the classification and compensation of appraiser type positions in the Property Tax Division, to assure that they are identified and compensated on a basis that will attract and keep personnel with the required capabilities. See Jacobs Report, pages 57-58.

N. Recommendation No. 14 -- An improved citizen appeals process should be instituted, whereby if the assessor refuses to make the abatement (adjustment in a citizen's tax bill) asked for, the citizen may appeal directly to the State Board of Assessment Review and, if still not satisfied, to the Superior Court. To further increase taxpayer awareness each locality's tax bill should include the assessed valuation of the taxpayer's property, the tax rate, the amount of tax due and a statement indicating the ratio or percentage of full (100%) value certified to the Bureau of Taxation and used in determining the assessed value.

O. Recommendation No. 15 -- When time and personnel permit the Bureau of Taxation should provide Maine's smaller communities with a revaluation service. See Jacobs Report, page 57.

7. IMPLEMENTATION OF RECOMMENDATIONS

Many of these 15 recommendations will require legislation. The total appropriations necessary to fund them for the next two years are estimated at $620,500. When one considers that the property tax produces approximately $271 million per year and that the Property Tax Division's administrative costs (even with cost of this report's recommendations) would represent about $\frac{4}{10}$ of 1% of that amount, therefore, the cost to improve the state and local valuations is completely justified.

Some recommendations can be implemented administratively by the Bureau of Taxation and we have been assured that their adoption is currently under way or will be in the immediate future.

The Committee is preparing two bills to carry its recommendations to fruition:

1. An emergency appropriation for personnel to immediately assist the local assessor (see Recommendation No.1); and

2. An omnibus property tax assessment reform.

We would caution against expectations of immediate and dramatic improvements in assessments. Change will take time. If adopted, the recommendations will begin to have an impact with the 1979 state valuation. It is important to note that the sequence of events for the 1978 valuation have commenced as illustrated below:

1978 State Valuation 14/

1. The sales information used by state assessors 15/ is from October 1975 to September 1976 sales;

2. This information is applied against the municipal assessment records of April 1, 1976;

3. The state valuation is then filed with the state, January 1978;

4. Thus, the taxes based on the state valuation are affected in the following ways:

(a) Municipalities: the Local and State Government Tax from July 1, 1978 - June 1, 1979;

(b) County taxes: January 1978 - December 1978;

(c) Uniform Property Tax (UPT): July 1,1978 - June 30,1979.

14/ For a detailed description of how the Property Tax Division compiles each state valuation, see above, Section 2, WHAT IS THE STATE VALUATION?

15/ For a description of how the Property Tax Division discards deceptive property sales, see Appendix B.

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8. CONCLUSION

As the recommendations of this report become fully implemented, the state valuation (and local assessing practices) will continue to improve in accuracy. Such accuracy will bring a greater degree of equity to the tax burden each of us must bear.

If property taxes are to be debated as a means of raising revenue, let that debate begin not with whether or not the tax is properly administered but with whether an accurate property tax is a proper source of state or local funds.

This LD, and the following LD 1608, were the result of the 1977 report, Is The State Valuation Accurate(both were defeated by the 108th Legislature.

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(EMERGENCY)

ONE HUNDRED AND EIGHTH LEGISLATURE

Legislative Document **No. 1607**

S. P. 464 In Senate, April 14, 1977

Reported by Select Committee on State Property Tax Valuation, pursuant to S. P. 610 of the 107th Legislature and printed under Joint Rules No. 17.

MAY M. ROSS, Secretary

Filed by the Select Committee on State Property Tax Valuation, under Joint Rule 17, pursuant to Senate Paper 610.

STATE OF MAINE

IN THE YEAR OF OUR LORD NINETEEN HUNDRED SEVENTY-SEVEN

AN ACT to Make Possible Property Tax Valuation Assistance to Local Officials.

Emergency preamble. Whereas, Acts of the Legislature do not become effective until 90 days after adjournment unless enacted as emergencies; and

Whereas, the property tax is the main source of state and local revenues; and

Whereas, the accuracy of the property tax depends directly on the accuracy of the local tax assessor; and

Whereas, the Select Committee on State Property Tax Valuation found that the most urgent need was for the State to offer immediate technical assistance to the local assessor; and

Whereas, in the judgment of the Legislature, these facts create an emergency within the meaning of the Constitution of Maine and require the following legislation as immediately necessary for the preservation of the public peace, health and safety; now, therefore,

Be it enacted by the People of the State of Maine, as follows:

Sec. 1. 36 MRSA § 330 is enacted to read:

§ 330. State assistance to local officials

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At the request of appropriate officials of either primary assessing areas of a municipality, the Bureau of Taxation shall provide technical assistance in the following areas:

1. **Appraisal.** Appraisal of property values; and

2. **Assessment standards.** Administration and achievement of the assessment standards established in this subchapter.

Sec. 2. Appropriation. There is appropriated from the General Fund to the Department of Finance and Administration, Bureau of Taxation, the sum of $260,000 for fiscal years 1977-78 and 1978-79. The breakdown shall be as follows:

	1977-78	1978-79
FINANCE AND ADMINISTATION, DEPARTMENT OF		
Bureau of Taxation		
Personal Services	(10) $70,000	(10) $145,000
All Other	10,000	30,000
Capital Expenditures	5,000	
Total	$85,000	$175,000

Emergency clause. In view of the emergency cited in the preamble, this Act shall take effect when approved.

STATEMENT OF FACT

The purpose of this bill is to improve the assistance provided by the State to local tax assessors. It is one of the recommendations of the 1977 Select Committee on State Property Tax Valuation. The committee made 14 detailed recommendations as to how the state valuation procedures could be improved. Their recommendation that the local assessors be able to request technical assistance from the State was the committee's most urgent request and the committee specifically requested that it be an emergency measure (see page 12 of the report). The committee's experience was that the local assessor desired such assistance. Copies of the committee's report can be obtained from the Office of the Legislative Assistants, Room 427, State House.

In general, the committee's report can be summarized as follows:

A. What is the state valuation?

The state valuation is the yearly estimate by the Bureau of Taxation of the market value of all property in the State.

B. How is the state valuation used?

(1) It is the valuation against which the uniform property tax is levied.

(2) It is a factor in state-local revenue sharing formulas.

(3) It is a standard against which to judge the accuracy of the local assessor.

C. Why can't the State simply add up each municipality's valuations?

(1) Many towns do not frequently update their valuations.

(2) Many towns have low assessment ratios (a percentage of full value) and the lower the ratio, the less likely it is to be correct.

(3) Thus, it is necessary for the Bureau of Taxation personnel to go into the field and analyze recent real estate sales and meet with the local tax assessors.

D. Is the state valuation accurate?

The committee finds the state valuation is:

(1) Conservative;

(2) Reasonably accurate; and

(3) Will improve with each year:

(a) Sales data will improve; and

(b) Statutory local assessing standards will become stiffer each year.

E. Do errors in the state valuation discriminate against certain types of localities?

Apparently not. There was not discovered a pattern to the types of towns in which the state valuation was inconsistent. Two trends did emerge however:

(1) In towns in which there was inconsistency, the state valuation erred by being too conservative; and

(2) These towns had low local assessment ratios and lack of valuation documentation.

F. How many new personnel will be needed?

In addition to adjustments in their statistical methods, the Property Tax Division will also need additional field personnel.

These persons will assist the local assessor and, for the state valuation, perform on-the-spot assessments where local sales are scanty.

G. Why is field assistance to the local assessor necessary?

No matter how accurate the sales information used by the State is, if the local assessor's valuations are inaccurate, the state valuation will be directly influenced. The committee emphasized that its experience revealed that the local assessor desires such assistance.

H. Does the value of the state valuation go beyond insuring an accurate state property tax?

Most definitely, the state valuation provides essential help in making sure the local property tax is accurately assessed, and further, it provides a basis for distribution of different kinds of state aid.

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ONE HUNDRED AND EIGHTH LEGISLATURE

Legislative Document **No. 1608**

S. P. 465 In Senate, April 14, 1977

Reported by Select Committee on State Property Tax Valuation, pursuant to S. P. 610 of the 107th Legislature and printed under Joint Rules No. 17.

MAY M. ROSS, Secretary

Filed by the Select Committee on State Property Tax Valuation under Joint Rule 17, pursuant to Senate Paper 610.

STATE OF MAINE

IN THE YEAR OF OUR LORD NINETEEN HUNDRED SEVENTY-SEVEN

AN ACT to Establish the 1977 State Valuation Omnibus Reform Act.

Be it enacted by the People of the State of Maine, as follows:

Sec. 1. 30 MRSA § 2060, sub-§ 6, as reenacted by PL 1973, c. 695, § 1, is repealed.

Sec. 2. 30 MRSA § 5351, sub-§ 2, as reenacted by PL 1973, c. 695, § 2, is repealed.

Sec. 3. 36 MRSA § 208, sub-§ 1, is enacted to read:

1. Annual studies. The State Tax Assessor shall conduct annual assessment sales ratio studies applicable to each municipality and primary assessing area and publish the results of such studies.

Sec. 4. 36 MRSA § 209 is enacted to read:

§ 209. Valuation of certain property

1. Valuation. The State Tax Assessor, beginning in the year 1978, shall determine the taxable just value of each industrial property with taxable just value exceeding $1,000,000. The State Tax Assessor shall on or before June 1st of each year certify such value to the assessors of the municipalities and chief assessors of the primary assessing districts where such properties are subject to assessment. Assessors of municipalities and chief assessors of primary assessing districts shall use such values, at their certified ratios, for local assessment purposes. When he deems it necessary, the State Tax Assessor shall cause a valuation to be made to determine whether certain property meets the dollar value criterion of this section. The taxable just

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value as herein determined shall be included in the equalized just value of all real and personal property in each municipality and unorganized place which is subject to taxation under the laws of this State as provided for in section 305.

2. Industrial property. As used in this section, "industrial property" shall mean all real and personal property located on contiguous parcels and used in the processing of natural resources, in the production of electrical energy, or in the assembly, fabrication, processing, manufacture and warehousing of tangible personal property.

3. Mandatory information. The State Tax Assessor may require the owner of industrial property to provide, within 90 days of his written request, any information which he deems necessary to the determination of the taxable just value of such industrial property. Any owner of industrial property who does not provide such information, in such format as the State Tax Assessor may reasonably request, shall be foreclosed from reconsideration and appeal, under subsections 4 and 5, of determinations made under this section by the State Tax Assessor.

4. Reconsideration. A municipality, primary assessing district or any property owner aggrieved by a determination of the State Tax Assessor under this section may petition in writing to the State Tax Assessor for reconsideration of the determination within 15 days after notice of the determination. If a petition for reconsideration is not filed within the 15-day period, the determination of the State Tax Assessor shall become final at the expiration thereof as to law and fact. If a petition for reconsideration is timely filed, the State Tax Assessor shall reconsider his determination and, if the petitioner has so requested in his petition, shall grant the petitioner an oral hearing with 10 days' notice. If appeal is not taken under subsection 5, the decision upon reconsideration shall become final as to law and fact at the expiration of the 30-day period therein allowed.

5. Appeals. A municipality, primary assessing district or any property owner aggrieved by the decision upon reconsideration under subsection 4 may, within 30 days after notice thereof, apply in writing to the State Board of Assessment Review for review of such decision. Either party may appeal from the decision of the State Board of Assessment Review to the Superior Court in accordance with the Maine Rules of Civil Procedure, Rule 80B. Pending the result of any appeal, the valuation established by the State Tax Assessor shall be used for valuation purposes. In the event that an appeal results in the amendment of a valuation, the board or court shall order such supplemental assessments and reimbursements and such other relief as are necessary to offset inequities caused by the erroneous valuation.

Sec. 5. 36 MRSA § 327, sub-§ 2, as enacted by PL 1975, c. 545, § 13, is amended to read:

2. Maximum rating of assessment. A maximum rating of assessment quality of 30 by 1977; a maximum rating of assessment quality of 25 by 1978; a maximum rating of assessment quality of ~~20~~ 18 by 1979 and thereafter;

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Sec. 6. 36 MRSA § 486, sub-§ 2, ¶ C is enacted to read:

C. Valuation appeals. To hear and determine appeals by municipalities, primary assessing districts or property owners from determinations by the State Tax Assessor under section 209.

Sec. 7. 36 MRSA § 708, as amended by PL 1973, c. 620, § 17, is amended by adding at the end a new paragraph to read:

They shall classify each parcel of real estate in accordance with the property classification system required by the State Tax Assessor and report the totals of assessed values for such classes on their annual municipal valuation returns.

Sec. 8. 36 MRSA § 708-A, 1st sentence, as enacted by PL 1973, c. 620, § 18, is amended to read:

The chief assessor of each primary assessing area shall on or before the 30th day of each June make perfect lists of the real estate and personal property values referred to in ~~section~~ sections 209 and 708 and commit the same to the municipal officers of each municipality comprising the primary assessing area.

Sec. 9. 36 MRSA § 754-A is enacted to read:

§ 754-A. Tax bills

Tax collectors shall annually, within 30 days after the commitment of taxes, prepare and mail a tax bill to each taxpayer who is named on the list provided by the assessors or municipal officers pursuant to sections 709 and 709-A. The tax bill shall include the assessed valuation of the taxpayer's property, the tax rate, the amount of tax due and a statement indicating the ratio or percentage of full 100% value used in determining the assessed valuation.

Sec. 10. 36 MRSA § 843, as last amended by PL 1973, c. 625, § 246, is repealed.

Sec. 11. 36 MRSA § 844, as last repealed and replaced by PL 1973, c. 645, § 6, is repealed and the following enacted in its place:

§ 844. Appeals

If the assessor refuses to make the abatement asked for, the applicant may apply in writing to the State Board of Assessment Review within 30 days after notice of decision from which such appeal is being taken or after the application shall be deemed to have been denied, and if the board thinks he is overassessed he shall be granted such reasonable abatement as the board thinks proper. Either party may appeal from the decision of the State Board of Assessment Review directly to the Superior Court, under the conditions provided for in section 845. Appeals to the State Board of Assessment Review shall be directed to the Chairman of the State Board of Assessment Review, who shall convene the board to hear the appeal and shall notify all parties of the time and place thereof.

Sec. 12. 36 MRSA § 845 is repealed and the following enacted in its place:

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§ 845. **Appeal to Superior Court**

Any person entitled to appeal to the State Board of Assessment Review for an abatement of his taxes may, if he so elects, appeal under the same terms and conditions from the decision of the assessors to the Superior Court in and for that county.

Sec. 13. **Appropriation.** There is appropriated from the General Fund to the Department of Finance and Administration, Bureau of Taxation, the sum of $300,000 for the biennium to be used to carry out the purposes of this Act. The breakdown shall be as follows:

	1977-78	1978-79
FINANCE AND ADMINISTRATION, DEPARTMENT OF		
Bureau of Taxation		
Personal Services	(7) $ 50,000	(7) $122,000
All Other	95,000	25,000
Capital Expenditures	5,000	3,000
	$150,000	$150,000

STATEMENT OF FACT

1. **Introduction.**

This bill is an omnibus reform bill, embodying the recommendations of the 1977 Select Committee on State Property Tax Valuation. Copies of the committee's report, "Is the State Valuation Accurate?" can be obtained from the Office of Legislative Assistants, Room 427, State House, Augusta, Maine.

2. **Specific recommendations.**

The recommendations upon which this bill is based are as follows:

1. An improved citizen appeals process should be instituted whereby, if the assessor refuses to make the abatement (adjustment in a citizen's tax bill) asked for, the citizen may appeal directly to the State Board of Assessment Review and, if still not satisfied, to the Superior Court. No appropriation is needed. See bill sections 1, 2, 10, 11 and 12.

2. Statutory requirement should be established for the Property Tax Division to conduct annual assessment-sales ratio studies applicable to each municipality or assessing jurisdiction, and to publish the results of such studies. No appropriation is needed. See bill section 3.

3. Legislation should be adopted to assign responsibility to the Property Tax Division to appraise at full value all industrial property in the State with a value over $1,000,000 and all operating utility property subject to taxation, to require the Property Tax Division to certify such individual full value

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appraisals to the municipalities to use these appraisals as the basis for their assessed value of the individual properties, and to provide for the financing of this appraisal service from state funds. This recommendation requires an appropriation of $300,000. See bill sections 4, 6 and 8.

4. The statutory assessment standards for rating of assessments should be adjusted to provide for a maximum quality rating of 18 by 1979 and thereafter, measured by the coefficient of dispersion. No appropriation is needed. See bill section 5.

5. Legislation should be adopted to require that all municipalities classify all parcels of property on their assessment roll according to the standard property classification system and any additional special categories that are significant in their municipality, and that the municipalities report to the State Bureau of Taxation the totals of assessed values for such classes on their municipal valuation returns. No appropriation is needed. See bill section 7.

6. To further increase taxpayer awareness, each locality's tax bill should include the assessed valuation of the taxpayer's property, the tax rate, the amount of tax due and a statement indicating the ratio or percentage of full 100% value certified to the Bureau of Taxation and used in determining the assessed value. No appropriation is needed. See bill section 9.

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INCOME TAX REFORM

1. Introduction

An often voiced area of reform is the revision of the current personal income tax rates. The argument most commonly voiced is that the 1975 rate change too greatly burdened the upper income brackets and the single taxpayer. In order to help you judge the validity of the argument, the following analysis of the tax change is presented:

STATE OF MAINE
BUREAU OF TAXATION

March 8, 1976

EFFECT OF THE MAINE INDIVIDUAL INCOME TAX INCREASE ENACTED IN THE 1976 SPECIAL LEGISLATIVE SESSION

The following examples are based on use of the Standard Deduction

	(a)	(b)	(b)	(a)	(c)	(c)	(a)	(c)	(c)
	SINGLE 1 EXEMPTION			MARRIED 2 EXEMPTIONS			MARRIED 4 EXEMPTIONS		
Adjusted Gross Income	1975	1976	1977	1975	1976	1977	1975	1976	1977
$ 5,000	$ 50	$ 26	$ 26	$ 25	$ 9	$ 9	$ 5	$ -0-	$ -0-
7,500	103	72	92	55	34	34	28	14	14
10,000	170	184	218	100	78	78	60	39	39
15,000	350	411	528	220	201	224	160	138	144
17,500	450	561	728	295	282	322	235	205	228
20,000	550	719	944	370	394	472	310	304	352
25,000	750	1,044	1,394	540	642	816	460	540	674
30,000	980	1,385	1,860	740	942	1,216	660	822	1,056
40,000	1,480	2,135	2,860	1,140	1,568	2,068	1,060	1,438	1,888
50,000	1,980	2,885	3,860	1,540	2,218	2,968	1,460	2,088	2,788
75,000	3,460	4,868	6,360	2,760	4,045	5,420	2,660	3,895	5,220
100,000	4,960	6,868	8,860	4,010	5,920	7,920	3,910	5,770	7,720

(a) 1975 Standard deduction was 10% of adjusted gross income, to a maximum of $1,000.

(b) 1976 and 1977 Standard deduction computed at 16% of adjusted gross income, with a maximum of $2,400 and a minimum of $1,700.

(c) 1976 and 1977 Standard deduction computed at 16% of adjusted gross income, with a maximum of $2,800 and a minimum of $2,100.

NOTE: For 1976 and 1977, those persons filing Married-Separate should estimate a standard deduction of 16%, not to exceed $1,400, with a $1,050 minimum (one-half the Married-Joint rate).

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An important point to note when looking at these various burdens is that even though the lower percentage rates of the 1975 law were mainly steeper than the present law, the latter schedules resulted in great tax savings for lower income levels. Why? Largely because the present law adopted the federal low income deductions and this allowed many families to reach a much lower taxable income than they could under the old law.

2. Suggested changes

There are several variables in designing a income tax schedule:

A. Exemptions. In Maine each person can subtract from their adjusted gross income (AGI) $1,000 for each exemption they claim. Under federal law only $750 is allowed for each exemption.

B. Deductions. Under the 1975 law, the standard deduction was only 10% of adjusted gross income (AGI) up to $1,000 but under present law it is 16% of Adjusted Gross Income, but for single persons never less than $1,700 nor more than $2,400 and for married couples never less than $2,100 nor more than $2,800.

C. The number and size of income brackets in the schedule. The 1975 law had a few, large brackets; thus a person earning $25,000 was taxed at the same rate as a person earning $10,000. This poorly reflects a person's ability to pay. The 1976 change increased the number of brackets while decreasing their size.

D. The percentage rate assigned each bracket. This is the most confusing factor because a few small income brackets at the lower income levels with 1% or 2% or 3% rate has a very profound effect on later higher income brackets. The result is that the percentage rate of upper income brackets often does not clearly reflect the true burden (the effective tax rate). This paradox

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is clearly evident when we compose the burdens of the 1975 income tax schedule, the burdens of the present law and the burdens of Rep. Ingegneri's defeated bill, L.D. 2211. The present law goes up to only 10% yet Rep. Ingegneri's bill, which would have brought in approximately the same revenues and which goes up to 12% actually taxes many higher incomes at a lower rate.

The most commonly voiced changes are:

A. To adopt the federal income brackets. There are 25 brackets and adopting them would breatly increase the accuracy of the tax as it would better targer each person's "ability to pay". Currently, there are only 8 brackets and, as an example, a person earning $15,000 will pay at the same rate as a person earning $25,000; and

B. To adopt either a percentage of federal rates or to adopt an equally progressive rate, beginning at .5% or 1% and increasing at every income bracket by an equal amount.

Then, with the adoption of such a "permanent" income tax schedule, if in future years the Legislature had to increase the income tax revenues it would not have to change the entire schedule but simply add a surtax. A surtax does not change the degree of progressivity of the original schedule. An example of how such a permanent schedule would look is:

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If the taxable income is:					The tax is:						
Not over $500					1% of taxable income						
$ 500	but	not	over $	1,000	$ 5	plus	1.5%	of	excess	over	$ 500
1,000	"	"	"	1,500	12.5	"	2.0%	"	"	"	$
1,500	"	"	"	2,000	22.5	"	2.5%	"	"	"	
2,000	"	"	"	4,000	35.0	"	3.0%	"	"	"	
4,000	"	"	"	6,000	95.0	"	3.5%	"	"	"	
6,000	"	"	"	8,000	165.0	"	4.0%	"	"	"	
8,000	"	"	"	10,000	245.0	"	4.5%	"	"	"	
10,000	"	"	"	12,000	335.0	"	5.0%	"	"	"	
12,000	"	"	"	14,000	435.0	"	5.5	"	"	"	
14,000	"	"	"	16,000	545.0	"	6.0%	"	"	"	
16,000	"	"	"	18,000	665.0	"	6.5%	"	"	"	
18,000	"	"	"	20,000	795.0	"	7.0%	"	"	"	
20,000	"	"	"	22,000	935.0	"	7.5%	"	"	"	
22,000	"	"	"	26,000	1,085.0	"	8.0%	"	"	"	
26,000	"	"	"	32,000	1,405.0	"	8.5%	"	"	"	
32,000	"	"	"	38,000	1,745.0	"	9.0%	"	"	"	
38,000	"	"	"	44,000	2,105.0	"	9.5%	"	"	"	
44,000	"	"	"	50,000	2,675.0	"	10.0%	"	"	"	
50,000	"	"	"	60,000	3,275.0	"	10.5%	"	"	"	
60,000	"	"	"	70,000	4,325.0	"	11.0%	"	"	"	
70,000	"	"	"	80,000	5,425.0	"	11.5%	"	"	"	
80,000	"	"	"	90,000	6,575.0	"	12.0%	"	"	"	
90,000	"	"	"	100,000	7,675.0	"	12.5%	"	"	"	
100,000	or more				8,925.0	"	13.0%	"	"	"	

This so called "permanent" schedule does not reflect decisions on the exemptions and deductions to be provided. Adoption of a permanent schedule and surtax arrangement would allow the income tax to become a flexible partner in the state tax mix.

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THE CASE FOR HIGHLY GRADUATED RATES IN STATE INCOME TAXES

ROBERT I. KELLER*

INTRODUCTION

There exists today in the United States a major but rarely mentioned indirect program of general revenue sharing[1] between the federal government and the state and local governments. This program, which should not be confused with the program of direct general revenue sharing enacted by the State and Local Fiscal Assistance Act of 1972,[2] is administered by the United States Treasury Department. The amount of federal tax receipts disbursed under the program to any given state or local government is, however, entirely within the control of the state or local government itself. This is because the amount distributed is determined solely by two factors: (1) the total amount of tax revenue that the state or local government can collect; and, (2) the federal marginal tax brackets of the taxpayers from whom such revenue is collected.[3]

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1. The concept of revenue sharing has been described as:

> [a strategy under which] . . . a portion of federal tax receipts are disbursed by means of a predetermined formula to state and local governments, with few strings attached. Washington's role is that of collecting taxes and distributing the receipts to lower levels of government; it is not involved in designing, administering, or regulating the specific public services on which the money is spent. . . .
>
> Two types of revenue sharing may be encompassed by this strategy: *general revenue sharing*, under which the recipient units of government are free to use their grants as they see fit, and *special revenue sharing*, or block grants, under which the recipients must spend their grants on programs in a broad functional area, such as education or urban development.

E. FRIED, A. RIVLIN, C. SCHULTZE & N. TEETERS, SETTING NATIONAL PRIORITIES THE 1974 BUDGET 266 (1973).

2. 31 U.S.C. §§ 1221-64 (Supp. II, 1972).

3. The funds allocated to state and local governments under the State and Local Fiscal Assistance Act of 1972 are disbursed using a multiple factor approach:

> The money is first allocated among the states. Each state as an area is allotted the amount available to it under either the original Senate version or the original House version of the general revenue sharing plan, whichever is greater. *Under the Senate's distribution formula the revenue is divided among the states according to their total populations, relative incomes, and tax efforts (that is, the ratio of total taxes collected to personal income); the House version of the formula includes, in addition, urbanized population and state income tax collections.* One-

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The program is identified in the Tax Expenditure Budget of the United States[4] as the "deductibility of nonbusiness State and local taxes (other than on owner-occupied homes and gasoline),"[5] and is listed in that budget under the appropriate heading: "[r]evenue sharing and general purpose fiscal assistance."[6] The estimated cost to the federal

> third of each state's allotment is given to the state government to use as it sees fit. The remaining two-thirds is divided among the county areas of the state on the basis of each county's population, tax effort, and relative income.

E. FRIED, A. RIVLIN, C. SCHULTZE & N. TEETERS, *supra* note 1, at 279-80 (emphasis added).

For purposes of this article, it is important to note that the House formula relies in part on "state income tax collections." If, as suggested herein, a state moves to an increased reliance on the income tax as a source of revenue, that state will effectively be increasing its share of both the indirect revenue sharing grants under the federal tax system and the direct revenue sharing grants under the State and Local Fiscal Assistance Act of 1972.

4. OFFICE OF MANAGEMENT AND BUDGET, SPECIAL ANALYSES, BUDGET OF THE UNITED STATES GOVERNMENT FISCAL YEAR 1976, at 101-17 (1975) [hereinafter cited as SPECIAL ANALYSES].

The phrase "tax expenditures" was first used in a 1967 speech by Professor Stanley S. Surrey, then Assistant Secretary for Tax Policy in the Treasury Department.

> The speech pointed out that those provisions of the federal income tax containing special exemptions, exclusions, deductions, and other tax benefits were really methods of providing governmental financial assistance. These special provisions were not part of the structure required for the income tax itself, but were instead Government expenditures made through the tax system. They were similar in purpose, therefore, to the direct expenditures listed in the regular budget. But since they provided their assistance through the route of tax reduction rather than direct aid, . . . [they were called] "tax expenditures."

S. SURREY, PATHWAYS TO TAX REFORM vii (1973). The "Tax Expenditure Budget" identifies and quantifies the existing tax expenditures. The Congressional Budget and Impoundment Control Act of 1974, 31 U.S.C. §§ 1301-53 (Supp. IV, 1974), requires that a listing of tax expenditures be included in the regular budget document of the United States. Section 3(a)(3) of the act defines "tax expenditures" as "those revenue losses attributable to provisions of the Federal tax laws which allow a special exclusion, exemption, or deduction from gross income or which provides a special credit, a preferential rate of tax, or a deferral of tax liability." 1 S. SURREY, W. WARREN, P. MCDANIEL & H. AULT, FEDERAL INCOME TAXATION CASES AND MATERIALS 113 n.6d (Supp. 1975).

5. SPECIAL ANALYSES, *supra* note 4, at 109. The SPECIAL ANALYSES further explains this item as follows:

> The deductibility of nonbusiness State and local taxes provides indirect assistance to these governments. The deductibility of property taxes on owner-occupied homes and excise taxes on gasoline are classified elsewhere. The estimates . . . are primarily for the deductibility of State and local income and sales taxes.

Id. at 114.

6. *Id.* at 109. The Tax Expenditure Budget also lists under this heading: "Exclusion of interest on State and local debt," and "Exclusion of income earned in U.S. possessions." *Id.*

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government of this revenue sharing program for the fiscal year 1976 is \$9.95 billion.[7]

The nature of the general revenue sharing program brought about by the deductibility of nonbusiness state and local taxes is easily observed. When, for example, a state imposes a \$100 tax on a person in the 50 percent federal income tax bracket, only \$50 of the \$100 tax is actually borne by the taxpayer; the remainder is borne by the federal government. Mechanically, of course, the taxpayer remits the full \$100 to the state, but in so doing he is, to the extent of \$50, acting as a mere conduit to pay federal dollars into the state treasury. By deducting the \$100 state tax on his federal income tax return, the state taxpayer reduces his federal income taxes by \$50, and is thus reimbursed to that extent by the federal government. *In effect, then, the state has imposed a "net tax burden"[8] of \$50 on the 50 percent bracket taxpayer, and has received a federal matching grant of \$50.*

In direct expenditure terms,[9] the assistance furnished by the federal government to state and local governments through the itemized de-

7. *Id.* The equivalent figures for the years 1968, 1971, and 1974 were \$2.8 billion, \$5.6 billion, and \$6.96 billion, respectively. 1 S. SURREY, W. WARREN, P. MCDANIEL & H. AULT, FEDERAL INCOME TAXATION CASES AND MATERIALS 244 (1972); SPECIAL ANALYSES, *supra* note 4, at 109. By comparison, the direct program of general revenue sharing established by the State and Local Fiscal Assistance Act of 1972 will have distributed about \$30.2 billion to state and local governments between January, 1972, and December, 1976, when the program is scheduled for termination. This amounts to annual disbursements of slightly over \$6 billion. 2 NATIONAL SCIENCE FOUNDATION RESEARCH APPLIED TO NATIONAL NEEDS, GENERAL REVENUE SHARING: RESEARCH UTILIZATION PROJECT 1 (1975).

8. The term "net tax burden" or "net state tax burden" will be used throughout this article to mean that figure arrived at by deducting from the amount of taxes actually remitted by a taxpayer to a state or local government, the amount of federal tax savings achieved by deducting such state and local tax payments at the taxpayer's marginal federal income tax bracket.

9. Every tax expenditure program can be translated into direct expenditure terms and analyzed as if it were a direct expenditure program. *See generally* S. SURREY, PATHWAYS TO TAX REFORM (1973). The analysis in the text views the deductibility of nonbusiness state and local taxes as a system of indirect revenue sharing grants from the federal government to state and local governments. However, the direct expenditure program brought about by the federal deductibility of state and local taxes can also be analyzed from the vantage point of the aid it gives to individual taxpayers. Viewed in this manner, the direct assistance program to state and local taxpayers would appear as follows:

1. If a married couple had more than \$200,000 of taxable income, the federal government would, for each \$100 of state and local taxes imposed on the couple, pay \$70 to the state or local government, leaving the couple to pay \$30;

2. If a married couple had \$10,000 of taxable income, the federal government would, for each \$100 of state and local taxes imposed on the couple, pay \$22 to the state or local government, leaving the couple to pay \$78; or,

3. If a married couple were too poor to pay any income tax, the federal government would pay no part of any tax imposed on the couple by the state and local government.

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duction for nonbusiness state and local taxes can be seen as a program of matching grants from the federal government to the state and local governments distributed on the following terms:

1. If a state or local government imposes a $30 net tax burden on a person in the 70 percent federal tax bracket, the federal government pays the state or local government a matching sum of $70;[10]
2. If a state or local government imposes a $30 net tax burden on a person in the 50 percent federal tax bracket, the federal government pays the state or local government a matching sum of $30;[11]
3. If a state or local government imposes a $30 net tax burden on a person in the 14 percent federal tax bracket, the federal government pays the state or local government a matching sum of approximately $5;[12]
4. If a state or local government imposes a $30 net tax burden on a person who is either a nontaxpayer for federal income tax purposes, or who, although a taxpayer, elects the federal optional standard deduction, the federal government pays nothing to the state or local government.[13]

No attempt will be made here to discuss the propriety, from a federal viewpoint, of using the deduction mechanism to provide aid to state and local governments.[14] Rather, the purpose of this article is

10. To achieve the same result indirectly through the tax system, a state imposes a $100 tax on the 70 percent bracket taxpayer. The taxpayer initially remits the full $100 to the state, but is reimbursed for $70 of his cost by a $70 reduction in his federal income taxes.

11. To achieve the same result indirectly through the tax system, a state imposes a $60 tax on the 50 percent bracket taxpayer. The taxpayer initially remits the full $60 to the state, but is reimbursed for $30 of his cost by a $30 reduction in his federal income taxes.

12. To achieve the same result indirectly through the tax system, a state imposes a tax of approximately $35 on the 14 percent bracket taxpayer. The taxpayer initially remits the full $35 to the state, but is reimbursed for approximately $5 of his cost by a $5 reduction in his federal income taxes.

13. The standard deduction is itself a tax expenditure item. *See* note 4 *supra*. The imposition of an additional state tax burden on the user of a standard deduction, however, neither increases federal tax expenditures nor decreases the taxpayer's federal income tax liability (unless the additional state or local tax paid gives the taxpayer itemized deductions in excess of the maximum standard deduction). Therefore, the additional $30 tax imposed by a state or local government on a taxpayer electing the optional standard deduction is paid entirely out of the pocket of that taxpayer, and the federal government makes no additional contribution to the state or local government.

14. There have been numerous proposals offered either to substitute a federal credit for the current deduction for state and local income taxes, or to buttress the deduction with such a credit. *E.g.*, W. HELLER, DEDUCTIONS AND CREDITS FOR STATE

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to show how a state, through the use of an income tax with highly graduated rates, can best take advantage of the open-ended revenue sharing possibilities inherent in the federal deductibility of state and local taxes,[15] while at the same time creating for itself a tax system

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INCOME TAXES, TAX REVISION COMPENDIUM 1 HOUSE COMM. ON WAYS & MEANS, 86TH CONG., 1ST SESS., 419 (Comm. Print 1959); ADVISORY COMMISSION ON INTERGOVERNMENTAL RELATIONS, II JOINT ECONOMIC COMM. 90TH CONG., 1ST SESS., REVENUE SHARING AND ITS ALTERNATIVES: WHAT FUTURE FOR FISCAL FEDERALISM 1137–40 (Comm. Print 1967) [hereinafter referred to as 1965 ACIR]; G. BREAK, INTERGOVERNMENTAL FISCAL RELATIONS IN THE UNITED STATES 39–45 (1967); H.R. 8193, 92ND CONG., 1ST SESS. (1971) and accompanying explanation at 117 CONG. REC. 14197 (1971) (remarks of Representative Byrnes). A federal tax credit for state and local income taxes (whether enacted as a substitute for, or in addition to the current deduction) would provide a reduction in federal taxes to taxpayers who now use the federal optional standard deduction or low-income allowance and who, therefore, obtain no advantage from the existing personal deduction.

However, if a fixed percentage credit (*e.g.*, 30 percent of the state and local taxes paid) were substituted for the current deduction for state and local income taxes, high bracket taxpayers would find their net state tax burden increased. It would, therefore, be politically more difficult for a state to move to highly graduated rates. *See* text accompanying notes 52–54 *infra*. Moreover, because a fixed credit would not have the same regressive effct on net state tax burdens as does the present deduction system (*i.e.*, all taxpayers would have their nominal tax burdens reduced by the same percentage credit), there would be less need for a highly graduated state income tax to insure an equitable distribution of the state tax burden. *See* notes 33–46 and accompanying text *infra*. Finally, under a fixed credit system, the imposition of a given amount of state tax on a high bracket taxpayer would bring forth no greater federal revenue sharing to the state than would the imposition of the same tax on a lower bracket taxpayer. This effect would also undermine a major argument in favor of highly graduated state income taxes. *See* notes 27–32 and accompanying text *infra*.

Other commentators have favored eliminating the deduction for all state taxes, including the income tax, and substituting direct federal subsidies. *See, e.g.*, H. BRAZER, THE DEDUCTIBILITY OF STATE AND LOCAL TAXES UNDER THE INDIVIDUAL INCOME TAX, 1 HOUSE COMM. ON WAYS AND MEANS, 86TH CONG., 1ST SESS., TAX REVISION COMPENDIUM 407 (Comm. Print 1959). Professor Brazer criticizes the federal deductibility of nonbusiness state and local taxes as being inequitable to individual taxpayers, and irrational and inefficient as a mechanism for providing aid to state and local governments. "If Federal subsidies are desirable they should be direct, subject to the scrutiny provided by the operation of the budgetary process, and specifically tailored to meet the objectives being sought." *Id.* at 418.

15. Note that the reference in the text is to a state's use of an income tax with highly graduated rates. This article does not advocate the proliferation of independent income taxes at local levels. Rather the proposal contained herein for the use of highly graduated rates is intended to fall within the broader recommendations of the Advisory Commission on Intergovernmental Relations that the taxation of personal income be either by the state or, if also by local governments, *"in the form of a supplement ('piggyback') to be administered with the State tax."* 1965 ACIR, *supra* note 14, at 1153 (emphasis in original). For an excellent work fully analyzing both the positive and the negative aspects of local income taxes, see R. SMITH, LOCAL INCOME TAXES: ECONOMIC EFFECTS AND EQUITY (1972). As of 1972 Maryland was the only state in which local income taxes were levied as supplements to the state tax. *Id.* at 14–15.

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which more equitably distributes the tax burden among its citizens and which is more responsive to economic growth and inflation. The State of Maryland, whose existing personal income tax structure is very mildly graduated, will be used as a model.[16] The discussion, however, is equally relevant to any state that does not raise a major portion of its revenue through an income tax with highly graduated rates.[17]

THE CURRENT MARYLAND PERSONAL INCOME TAX STRUCTURE

The current Maryland personal income tax structure taxes the first $1,000 of taxable income at a rate of 2 percent, the second $1,000 at 3 percent, the third $1,000 at 4 percent and all taxable income in excess of $3,000 at 5 percent.[18] In addition, Baltimore City and nearly all of the counties of Maryland impose a local income tax (normally referred to as the local piggyback tax) at a rate of 50 percent of that of the state.[19] Therefore, the combined state and local rates in Mary-

16. For a similar analysis using Massachusetts as a model, see Moscovitch, *State Graduated Income Taxes — A State-Initiated Form of Federal Revenue Sharing*, 25 NAT'L TAX J. 53 (1972) [hereinafter cited as MOSCOVITCH]. Minnesota was used as a model in W. HELLER, *supra* note 14.

17. The only states today that have income taxes with highly graduated rate structures (defined somewhat arbitrarily here as those with maximum marginal rates of 10 percent or more and with marginal brackets that graduate up to at least $30,000 of taxable income) are: Alaska (14.5 percent, on taxable income over $400,000); Delaware (19.8 percent on taxable income over $100,000); Hawaii (11 percent on taxable income over $30,000); Iowa (13 percent on taxable income over $75,000); Montana (11 percent on taxable income over $35,000); Rhode Island (17 percent of federal income tax liability which is equivalent to 11.9 percent on taxable income over $200,000); Vermont (25 percent of federal income tax liability which is equivalent to 17.5 percent of taxable income over $200,000). Jurisdictions whose highest marginal rate of tax is ten percent or more but whose highest bracket is under $30,000 include California (11 percent on taxable income over $15,500); Minnesota (15 percent on taxable income over $20,000); New York (15 percent on taxable income over $25,000); North Dakota (10 percent on taxable income over $8,000); Oregon (10 percent on taxable income over $5,000); Wisconsin (11.4 percent on taxable income over $14,000); and the District of Columbia (10 percent on taxable income over $25,000). Colorado's tax is only 8 percent of taxable income over $10,000, but there is a 2 percent surtax on intangible income over $5,000. New Jersey has no broad-based income tax of its own, but imposes a tax on New York commuters equal to the New York income tax. 1 CCH STATE TAX GUIDE 1531–34 (1975). A bill has recently been introduced in California (S.B. No. 540) (1975) to increase the marginal rates in its personal income tax to 23 percent on taxable income over $127,500.

18. MD. ANN. CODE art. 81, § 288(a) (1975).

19. MD. ANN. CODE art. 81, § 283(a) (1975) authorizes each county and Baltimore City to impose a local income tax upon its residents equal to a percentage (to a maximum of 50 percent) of such residents' state income tax liability *See* note 15 *supra*.

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Summary

The case for highly graduated rates in state income taxes may be summarized as follows: (1) The highly graduated state income tax most effectively takes advantage of the indirect program of federal revenue sharing resulting from the deductibility of state and local taxes for federal income tax purposes; (2) It is only the highly graduated state income tax which imposes a greater net state tax burden on high-income taxpayers than on low-income taxpayers; and, (3) It is only the highly graduated state income tax which, because of its greater responsiveness to changes in personal income, is capable of financing the rapidly increasing cost of state and local governmental operations. Just as the states' needs for additional revenue overcame the historical opposition to the very use by states of income taxes,[72] their current needs for expanding revenue sources are beginning to erode opposition to highly graduated state income tax rates. As more states move toward the adoption of highly graduated state income tax rates, fears of interstate tax competition (already greatly mitigated by the effects of federal deductibility) will be effectively laid to rest.

68. Del. Code Ann. tit. 30, § 1102 (1974).

69. Va. Code Ann. § 58-151.011 (1974).

70. D.C. Code Ann. § 47-1567b(a) (1973).

71. According to a recent editorial in the Washington Post:

> [T]he fiscal news emanating from Richmond is not good. In fact, each time Gov. Mills E. Godwin discusses the state's financial shape, it is worse. . . .
>
> Certainly it has been difficult for all governments to anticipate the pressures of the economy on their budgets and programs. . . . [This pressure] will require a recognition by Gov. Godwin and the General Assembly that the answer cannot be merely to reduce services. . . . *New sources of revenue must be proposed, lobbied for and approved.*

Washington Post, Dec. 4, 1975, § A, at 18, col. 1 (emphasis added). There are also indications that the District of Columbia is considering a 4 to 5 percent increase in its personal income tax (which now has a maximum marginal rate of 10 percent). Washington Post, Jan. 7, 1976, § D, at 1, col 1.

72. J. Pechman, *supra* note 55, at 221.

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ADJUSTED GROSS INCOME OF MAINE TAXPAYERS (INCL. BEFORE DEDUCTIONS AND EXEMPTIONS)

% of all Maine taxpayers in income brackets

MARRIED-JOINT | MARRIED-SINGLE | TAX-PAYERS | TAXPAYERS

STATE OF MAINE - BUREAU OF TAXATION

1976 INDIVIDUAL MAINE ADJUSTED GROSS INC 08/16/77

		ALL COUNT	%	MJ COUNT	%	MS COUNT	%	S COUNT	%	NR COUNT	%
I	NEGATIVE	0	0.000	0	0.000	0	0.000	0	0.000	0	0.000
N	0.00	4,504	1.123	2,038	0.508	96	0.023	1,339	0.334	1,031	0.257
C	0.01 - 1,999.99	45,868	11.441	4,675	1.166	1,079	0.269	36,178	9.024	3,936	0.981
O	2,000.00 - 2,999.99	26,382	6.581	4,663	1.163	747	0.186	18,873	4.707	2,099	0.523
M	3,000.00 - 3,999.99	24,022	5.992	5,933	1.480	660	0.164	15,737	3.925	1,692	0.422
E	4,000.00 - 4,999.99	22,780	5.682	6,880	1.716	629	0.156	13,659	3.407	1,612	0.402
	5,000.00 - 5,999.99	24,621	6.141	8,476	2.114	664	0.165	13,895	3.466	1,586	0.395
	6,000.00 - 6,999.99	23,520	5.867	9,482	2.365	586	0.146	12,039	3.003	1,413	0.352
R	7,000.00 - 7,999.99	21,626	5.394	10,310	2.571	534	0.133	9,462	2.360	1,320	0.329
A	8,000.00 - 8,999.99	20,047	5.000	10,948	2.731	428	0.106	7,425	1.852	1,246	0.310
N	9,000.00 - 9,999.99	18,500	4.614	11,464	2.859	261	0.065	5,672	1.414	1,103	0.275
G	10,000.00 - 10,999.99	17,978	4.484	12,168	3.035	228	0.056	4,530	1.130	1,052	0.262
E	11,000.00 - 11,999.99	16,311	4.068	11,903	2.969	139	0.034	3,402	0.848	867	0.216
	12,000.00 - 12,999.99	15,627	3.898	12,025	2.999	105	0.026	2,657	0.662	840	0.209
	13,000.00 - 13,999.99	14,370	3.584	11,429	2.851	84	0.020	2,039	0.508	818	0.204
	14,000.00 - 14,999.99	14,010	3.494	11,389	2.841	59	0.014	1,644	0.410	918	0.228
	15,000.00 - 15,999.99	12,677	3.162	10,741	2.679	35	0.008	1,204	0.300	697	0.173
	16,000.00 - 16,999.99	11,073	2.762	9,684	2.415	39	0.009	818	0.204	532	0.132
	17,000.00 - 17,999.99	9,794	2.443	8,688	2.167	19	0.004	671	0.167	416	0.103
	18,000.00 - 18,999.99	8,473	2.113	7,570	1.888	15	0.003	515	0.128	373	0.093
	19,000.00 - 19,999.99	7,297	1.820	6,582	1.641	12	0.002	400	0.099	303	0.075
	20,000.00 - 22,499.99	13,136	3.276	11,994	2.991	26	0.006	651	0.162	465	0.115
	22,500.00 - 24,999.99	8,272	2.063	7,572	1.888	19	0.004	392	0.097	289	0.072
	25,000.00 - 27,499.99	5,331	1.329	4,898	1.221	5	0.001	251	0.062	177	0.044
	27,500.00 - 29,999.99	3,360	0.838	3,046	0.759	4	0.000	184	0.045	126	0.031
	30,000.00 - 34,999.99	3,859	0.962	3,468	0.865	12	0.002	256	0.063	123	0.030
	35,000.00 - 39,999.99	1,992	0.496	1,776	0.443	8	0.001	133	0.033	75	0.018
	40,000.00 - 44,999.99	1,298	0.323	1,166	0.290	3	0.000	81	0.020	48	0.011
	[illegible]	[illegible]	[illegible]	[illegible]	[illegible]	3	0.000	55	0.013	[illegible]	0.009

75,000.[illegible] - 99,999.99	674	0.160	575	0.1[illegible]	4	0.000	63	0.015	32	0.007
100,000.00-124,999.99	239	0.059	207	0.051	1	0.000	11	0.002	28	0.006
125,000.00-149,999.99	112	0.027	95	0.023	0	0.000	9	0.002	8	0.001
150,000.00-174,999.99	64	0.015	52	0.012	0	0.000	4	0.000	8	0.001
175,000.00-199,999.99	37	0.009	31	0.007	0	0.000	1	0.000	5	0.001
200,000.00-224,999.99	24	0.005	17	0.004	1	0.000	2	0.000	4	0.000
225,000.00-249,999.99	12	0.002	9	0.002	0	0.000	2	0.000	1	0.000
250,000.00-274,999.99	15	0.003	13	0.003	0	0.000	1	0.000	1	0.000
275,000.00-299,999.99	6	0.001	6	0.001	0	0.000	0	0.000	0	0.000
300,000.00-324,999.99	4	0.000	3	0.000	0	0.000	1	0.000	0	0.000
325,000.00-349,999.99	6	0.001	3	0.000	0	0.000	1	0.000	2	0.000
350,000.00-374,999.99	4	0.000	4	0.000	0	0.000	0	0.000	0	0.000
375,000.00-399,999.99	2	0.000	2	0.000	0	0.000	0	0.000	0	0.000
400,000.00-424,999.99	1	0.000	1	0.000	0	0.000	0	0.000	0	0.000
425,000.00-449,999.99	1	0.000	1	0.000	0	0.000	0	0.000	0	0.000
450,000.00-474,999.99	0	0.000	0	0.000	0	0.000	0	0.000	0	0.000
475,000.00-499,999.99	1	0.000	1	0.000	0	0.000	0	0.000	0	0.000
500,000.00- UP	14	0.003	4	0.000	1	0.000	2	0.000	7	0.001
TOTALS	400,874	100.000	214,570	53.527	6,512	1.624	154,418	38.520	25,366	6.327

TOTAL COUNT	400,874
RES ONLY COUNT	375,500
PART YEAR RES	9,448
NON-RES	15,743
RESIDENTS	375,691
NONRES EXEMPTS	45,738
PART RES EXEMPTS	22,433
RES EXEMPTS	974,534
TOTAL EXEMPTS	1,042,705

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Income Taxes and Inflation

(Excerpts from) Inflation and Federal and State Income Taxes
by Advisory Commission on Intergovernmental Relations

A SUMMARY OF FINDINGS OF THE REPORT

The major findings of this report are as follows:

FISCAL ACCOUNTABILITY

- *Inflation interacts with any progressive individual income tax to generate increases in tax revenue more than proportionate to the rate of inflation. These increases occur with practically no public debate or disclosure of the fact.* Although progressive income taxes also exhibit elasticity with respect to real income growth that property is inherent in a progressive tax and can be considered intended. Since recent inflation rates and those projected for the immediate future are well above the historical average, the automatic increase in aggregate, effective, personal income tax rates due to inflation is a significantly new and different issue.

TAX EQUITY

- *Among the different taxpayers, the inflation induced increases in personal income taxes without legislated tax cuts are arbitrary.* They depend on differences among taxpayers as to family size, level of gross income, type of income received, and the degree to which the various dollar limitations in the tax code affect tax liabilities.

- *Inflation is especially hard on low-income families and all families with many dependents because it erodes the value of personal exemptions, the low-income allowance, the maximum limit of the standard deduction and per capita credits.* After one year of 7 percent inflation, the value (in constant dollars) of a \$750 personal exemption falls to \$701, the \$1,600 low income allowance falls to \$1,495, the \$2,600 maximum standard deduction for married persons falls to \$2,430. The income tax impact of the decline in the real value of personal exemptions increases with family size. The relative increase in tax liability because of the effect of inflation on all these variables will be greater for lower income taxpayers (with the exception that those with very low income may still owe no tax even after inflation erodes the value of these tax features).

- *On the average, increases in tax liabilities due to the inflation erosion of income tax brackets will be greater for taxpayers in the upper income range where brackets are narrow and the rise in tax rates between brackets is fastest.* For the Federal personal income tax, this occurs in the \$28,000 to \$200,000 income range.

- *The middle-income taxpayers those with income between \$10,000 and \$15,000, incur the smallest decline in real, after-tax purchasing power due to the inflation-income tax interplay.* This occurs because the exemption-credit-deduction effect diminishes in importance faster than the bracket effect grows in importance.

- *On balance, the four major tax cuts enacted since 1960 have introduced a greater element of progressivity into the income tax structure than would have been the case under an indexed system.* This inference can be drawn from the fact that classes of taxpayers below \$25,000 generally have lower 1975 effective tax rates than they would have had if the 1960 law had been indexed and no other changes had been made. Taxpayers with incomes above \$200,000 also had lower 1975 effective tax rates than they would have had under an indexed system.

- *Both the magnitude and the differential impacts of the inflation-induced individual tax increases, in the absence of indexation and enacted tax cuts, can be substantial.* For example, after five years of 7 percent inflation, the inflation-induced tax increase in the fifth year is \$352 for an average family with constant real income of \$6,000, \$602 for a real income of \$15,000, and \$1,743 for a real income of \$30,000. From another viewpoint, the decreases in real disposable income over this five-year period for families with these real incomes are: \$6,000 income—a \$449 or 7.4 percent decrease in disposal income, \$15,000 income—a \$420 or a 3.1 percent decrease, and \$30,000 income—a \$1,235 or 4.9 percent decline.

PUBLIC SECTOR GROWTH

- Assuming annual 6 percent inflation, annual 6 percent real income growth, and no discretionary tax code changes from 1976 on:

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- ●● *The inflation-induced real increase in personal income tax revenue for a hypothetical "average state" (under the above assumptions and assuming a state personal income tax elasticity equalling 1.65) would be about $15 million or 3 percent of income tax after one year and about $140 million or 14 percent of income tax after five years.* Again, these are the amounts of the automatic increase in income tax that would be eliminated by tax indexation. Any given state's situation will vary from this projection depending on its income tax elasticity, the nominal amount of income tax revenue, and the state's reliance on the income tax in its total revenue picture.

- *Since few local governments utilize progressive personal income taxes, the inflation impact is not significant at the local level.* Important exceptions to this generality are: local jurisdictions in Maryland where the local individual income tax is a percent of the state income tax; New York City which has a progressive individual income tax and allows personal exemptions specified in fixed dollars; and the District of Columbia which has a progressive individual income tax.

- *Most states have not cut their income tax rates so as to reduce the inflation impact on their revenues.* From 1966 to 1973, state discretionary action in the aggregate served to increase income taxes beyond the impact of income growth and inflation. Since 1973, most states have not raised their rates but have relied on inflation's impact on their revenue to maintain their public service levels.

- *Using the economic projection of the Congressional Budget Office—average annual total income growth of 10 percent including about a 6 percent average annual inflation rate—the average annual increases in aggregate state income tax revenue will be about 13 percent from 1977 to 1980 with indexation; and about 16.5 percent without indexation.* In contrast, actual aggregate state individual income tax revenue increased at an average annual rate of about 15.5 percent from 1971 to 1975.

INTERGOVERNMENTAL FISCAL EFFECTS

Without Indexation

In the absence of indexation, the interaction of substantial inflation with progressive income taxes is likely to produce the following intergovernmental fiscal effects:

- *Of the revenue systems of the three levels of government, the Federal sector has the greatest capacity to automatically realize the revenues which accrue as inflation generates nominal increases on various tax bases.* The Federal government makes relatively intensive use of the progressive personal income tax. Federal collections account for about 85 percent of all individual income taxes.

- *State governments have the second greatest ability to realize inflation-generated tax revenues.* States rely more heavily on progressive personal income taxation than do local jurisdictions.

- *On the expenditure side, local governments tend to be more "inflation prone" than the other sectors (Federal, state, private) of the economy.* Local government services are relatively most labor intensive (e.g., teaching, health).

- *The 16 states which permit their residents to deduct their Federal income tax liability in computing the state income tax will experience, during an inflation, a lower growth of revenues than would otherwise occur.* As inflation induces Federal personal income tax increases that are proportionately greater than inflation, these higher liabilities will erode these states' income tax base.

- *States which "piggyback" their state income tax on the Federal income tax (state tax liability is computed as a set percentage of Federal liability) are likely to find a roller-coaster effect on their income tax revenues.* Their tax collec-

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tions will automatically rise with inflation due to the inflation responsiveness of the Federal income tax. If Congress follows past practice, however, (as is plausible) and enacts tax cuts to offset the inflation-generated, real income tax increases, the piggyback states will experience declines in their tax revenues (for a given tax rate). At the very least, the "piggyback" states will experience uncertainty of revenues with inflation.

- *Most state and local governments will be in too weak a fiscal position to enact tax reductions during the next few years.* State and local governments do not, in general, have highly inflation-responsive tax structures. Some state governments and many local governments have been forced to restrict or even reduce the quality and scope of their services in the last few years. Unlike the Federal government, they cannot engage in extended deficit financing to bridge their current expenditure-revenue gap. Accordingly, in the next two-three years, new state and local expenditures may be needed just to maintain past (e.g., 1972) program service levels.

- *The inflation-personal income tax interaction will slightly reduce the net resident burden of state and local taxes.* This interesting and beneficial twist for state-local jurisdictions results from the fact that the major state and local taxes are deductible when a taxpayer itemizes deductions on his or her Federal income tax. The reduced "cost" of state-local taxes thus occurs as inflation pushes taxpayers into higher Federal tax rate brackets and, as a result, increases the dollar value of the state-local tax deduction.

With Federal Indexation

With the indexation of the Federal individual income tax, the following intergovernmental effects are likely to occur:

- *State and local governments would find that their residents experience a rise in the net burden of state-local taxes relative to what otherwise would occur because of the reduction in the dollar value of the state-local tax deduction on the Federal income tax return.* Federal tax indexation would permit taxpayers with constant real incomes to avoid being moved into higher tax rate brackets where the dollar value of the state-local tax deduction on the Federal tax return is slightly increased.

- *States which permit the deductibility of Federal tax liability against their state income taxes would experience a slight increase in the revenue productivity of their taxes as Federal tax liabilities have the automatic "inflation tax" component eliminated.*

- *Piggyback income tax states would, just as the Federal government, lose the revenues once generated by the "inflation tax."* Federal indexation might reduce to some extent, the fiscal uncertainty these states now experience as a consequence of the possible periodic Congressional reductions in the Federal personal income tax.

State Indexation (In Addition to the Federal)

If the states as well as the Federal government index the individual income tax, the following fiscal effects are likely to occur:

- *In general, state income tax indexation could be expected to increase state-local fiscal tensions.* Because state governments have limited ability to incur deficits to finance current expenditure-revenue gaps and because their long-run budget situation *is at best one of balance or slight surplus,* indexation at the state level would mean either reduction in the rate of expenditure growth and/or the likelihood of

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more tax increases than would be the case in the absence of indexation.

- *The degree of fiscal stress due to indexation would vary among states depending on the extent to which they rely on progressive personal income taxation. In general, jurisdictions which have a high reliance on the personal income tax would experience the most fiscal strain due to indexation.* But some states which have rapidly growing economic bases (e.g., the "energy rich" states) may well be able to afford indexation and still be able to increase the scope and quality of their public services or cut taxes.

- *To the extent that indexation would reduce the fiscal flexibility of certain states, local governments in these states would also experience financial strain if the states become more reluctant to increase state to local aid (e.g., for property tax relief) and/or take over certain local fiscal responsibilities (e.g., school financing).* Over the last 20 years, state aid as a percent of local general revenue has risen from 42 to 60 percent.

OTHER INDEXATION ISSUES

- *Indexation is not likely to alter the built-in, economic stabilizing influence of the Federal individual income tax.* The response of income taxes to changes in real national income would remain under indexation. Any indexation impact on the built-in stabilizer would depend somewhat on how the index is determined.

- *If unions or individuals bargain for wage levels high enough to maintain real after-tax purchasing power, then indexation would reduce pressure for wage increases.* Indeed, the severe inflation (about 15% per year) in Australia has prompted the labor unions in that country to "bargain" for real wage increases by urging income tax indexation as a means to protect automatically at least part of wage gains negotiated at the bargaining table.

STATE RECOMMENDATIONS

The policy implications of state income tax indexation differ from the Federal in two important respects. First, state governments face budgetary constraints and economic pressures which are fundamentally different from the national government (e.g., limits on deficit financing, special vulnerability of expenditures to inflation).

Second, statements about the effects of indexation on state income taxes are less subject to generalization due to the fact that there are 30 different broad-based, state income taxes with varying degrees of progressivity and relative quantitative importance.

FULL DISCLOSURE AND ANNUAL INDEXATION OF STATE INDIVIDUAL INCOME TAX

The Commission recognizes that inflation induces increases in real income tax revenue and introduces distortions in interpersonal tax equity. The Commission is persuaded that taxpayers may not readily perceive the automatic, real tax increase that occurs from the inflation-personal income tax interplay. **Therefore, the Commission recommends, in the interest of complete public information, that governors have an estimate made of the amount of the inflation-induced state personal income tax increase and publicize the estimate for each tax year.**

While a full disclosure policy is a desirable first step, the Commission also believes that effective personal income tax rates should be increased only by overt state legislative action and should not be an automatic consequence of inflation. **The Commission recommends, therefore, that all states give early and favorable consideration to annual indexation of exemptions, deductions, per capita tax credits, and tax rate brackets. The Commission believes that the need for this remedial action is especially apparent for those states that combine a highly progressive, income tax rate structure with heavy reliance on the tax.**

The same major considerations—fiscal accountability, tax equity, public sector growth—that prompted the Advisory Commission to recommend the indexation of the Federal income tax also support indexation of the state personal income tax.

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Over the last 15 or 20 years, many states have moved strongly to make balanced use of various revenue sources including particularly the personal income tax. Thirty-nine states now use progressive individual income taxes that provide, on average, a substantial portion of own-source state revenue. As a result, state revenue systems now generally enjoy higher elasticity—that is stronger growth responsiveness—than ever before. There is little doubt that the inflation-induced real increases in income tax revenue encouraged the states to make greater use of income taxes. Now that these progressive, state personal income taxes are established, however, further automatic real increases *due to inflation* should not be tolerated.

With indexation, the distortions in interpersonal tax equity that are introduced by inflation interacting with progressive state income taxes would be largely eliminated. Furthermore, states would still enjoy substantial, income tax elasticity from the income tax response to real economic growth. Indeed, the evidence suggests that, with indexation, aggregate state personal income tax collections can increase over the next four years at about 13 percent annually. This is only 2.5 percentage points less than the actual annual revenue growth between 1971 and 1975—a period of significant legislative action to raise taxes.

Although state individual income tax collections approximate only 20 percent of Federal collections from this source, this average obscures the heavy reliance certain states make of this tax instrument. While Ohio and Louisiana income tax yields are only about 7 percent of the Federal, Minnesota and Wisconsin income tax yields are 41 and 38 percent, respectively, of Federal collections. In states where a highly progressive rate structure is combined with heavy reliance on the income tax, the impact of inflation on the state's income tax collections can be substantial.

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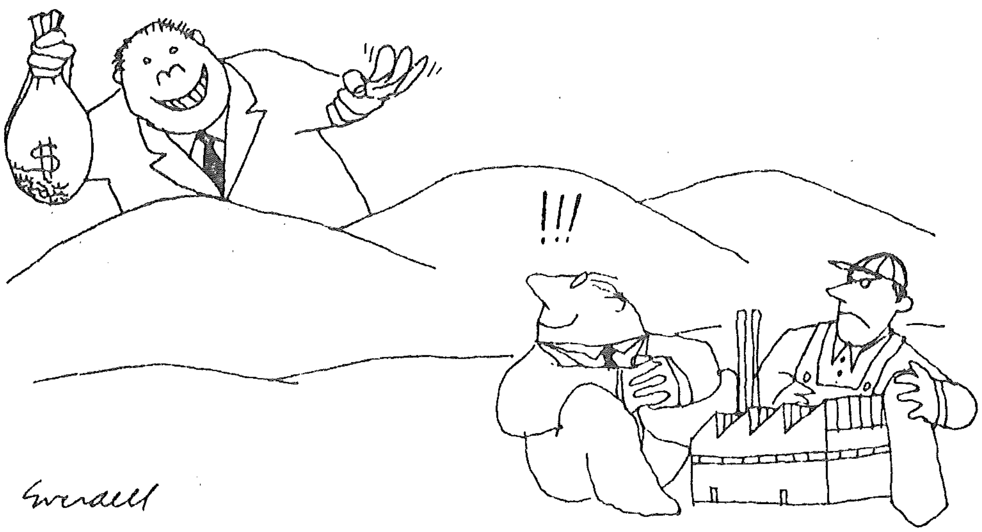
The Great State Robbery

by BENNETT HARRISON and SANDRA KANTER

State tax incentives for business have virtually no effect on job creation or economic development. But they do redistribute income—upwards.



Contenders for the office of governor in Mississippi last November agreed on at least one thing, according to a *New York Times* account: "economic colonialism." They were both against it.

Responding to an interviewer's question as to how he felt about "manufacturers building plants in the state to take advantage of cheap labor," Democrat Charles C. Finch (who won the election) said "with a show of passion": "I don't want them to come here just because they may be able to get nickel or dime savings on their labor. We've been holding our head in the sand by offering cheap wages. The blue chip industries are not looking for cheap wages." His Republican opponent proposed putting less emphasis on tax incentives for industry. "The state needs to think instead about incentives for agriculture to get idle land back into production," he said.

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"The Mississippi race," the *Times* story went on, "is the latest indication that Southern leaders are changing their traditional stance toward industrialization. For generations Southern politicians and businessmen lured Northern industry with every device they could find, from cheap labor to tax write-offs."

Cheap labor and favorable political conditions almost surely had more to do with enticing low-wage industry from the North to the South than tax write-offs. Indeed, the latter may not have made any difference at all. Effective or not, however, "devices" like tax write-offs to businesses are still advocated in practically every state legislature as a way to stimulate production and thus to create jobs within a state's boundaries.

Such incentives are opposed by some observers on the grounds that competition among states for jobs does nothing to increase the country's overall employment; it just changes its location. Other opponents see the incentives as one more example of how public money is used to benefit private corporations. However valid these objections, we are going to make a

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different argument against the incentives: They don't work. What's more, they cost states a lot of money in uncollected taxes.

Special-interest lobbyists have succeeded in selling states the idea that incentives are effective and even necessary both to attract and to keep business. Surprisingly little work has been done to find out how firms actually do respond to the incentives. Perhaps that is because the policies sound perfectly plausible. If a state reduces the costs of doing business relative to other states, surely firms will be attracted to it.

That argument may sound right. But there are a host of reasons, some of them even from standard economic theory, why the incentives that most states use will not significantly affect production or employment. And empirical studies, spotty though they may be, provide little or no evidence that business decisions are influenced by these incentives.

The Theory

State subsidies to business are almost as old as the Constitution. In the late 1700s, for example, the government of the Commonwealth of Massachusetts authorized bounties or outright gifts of money to producers of hemp, flax, and glass to encourage production of these goods. The Commonwealth also offered to reduce the taxes of brewers who produced over 100 barrels of beer annually.

Today the rationale for business incentive policies is less to encourage the production of particular goods than it is to encourage the creation of jobs within a state. These policies include tax credits and "forgiveness"; the provision of capital raised through tax-exempt bonds; low-interest loans; and state guarantees of loans or mortgages written by private sector lenders. Nearly every state in the union provides some mix of these business incentives (see box, p.62).

Popular—and legislative—discussions about business incentives are invariably couched in very general terms: "Cut taxes and get businesses to create new jobs." Economic theory cannot tell us with any precision whether or not cutting taxes in a state creates jobs. It can, however, shed light on a number of issues about business incentives that are not covered in the existing empirical studies—and that should be of concern to policymakers. For example, if incentives do work, which sorts of businesses are likely to respond to them? What kinds of jobs are apt to be created? How important to firms are reductions in costs of the magnitude the states can offer, compared to other market conditions?

There is, in elementary economics, a model of "perfect competition" in which firms compete with one another on equal terms for markets, labor, and capital. No one firm is so powerful that it can directly influence the price of its product or the prices it must pay for labor or capital. And so on. According to this theory, under conditions of perfect competition, *any* reduction in a firm's costs will induce some change in its output and employment decisions. In its search to maximize profits, the firm will tend to increase production and, therefore, employment.

Though many of these assumptions never hold in the real world, firms do behave differently according to the degree of their competitiveness. Oligopolies, for example, are firms in industries that are characterized by a relatively small number of larger producers. To some extent, oligopolies like Ford or General Motors can set their own prices and output levels without fear of losing out to a competitor. Tee-shirt factories, by comparison, have to produce as many shirts as they can and sell them at a price low enough to be competitive or else they'll go out of business. Though even they do not exactly fit the model of perfect competition, they will respond more nearly to the textbook model than the oligopolies, which are less affected by external market conditions. It follows, then, that if they have any effect at all, incentives that lower the costs of taxes and interest on bonds and loans will have a relatively larger impact on competitive firms than on oligopolies. In theory, at least, the competitive firms are more apt to respond by increasing production and employment.

In recent years, a huge literature has developed on the "rules of thumb" by which oligopolists (and even small firms facing less than perfectly competitive conditions) make output and employment decisions in response to changes or uncertainties in market conditions. This literature stresses the importance of "threshold effects": unless price, cost, and other external conditions change by more than some minimum amount in a given time period, the firm will probably ignore the changes since the very act of adjusting to them would have real costs. For example, if business taxes fall by a small amount, the firm may not react at all. The revenue a firm gains from tax incentives that are granted whether it increases its hiring or not—such as reduced excise taxes on existing machinery—is simply a windfall profit.

Firms of all types are more likely to increase output and therefore employment if there is an increased demand for their goods and services. But at the state level, business tax incentives do virtually nothing to stimulate the demand for goods and services (although consumer income tax deductions and credits may do so).

In principle, of course, there must be some level of

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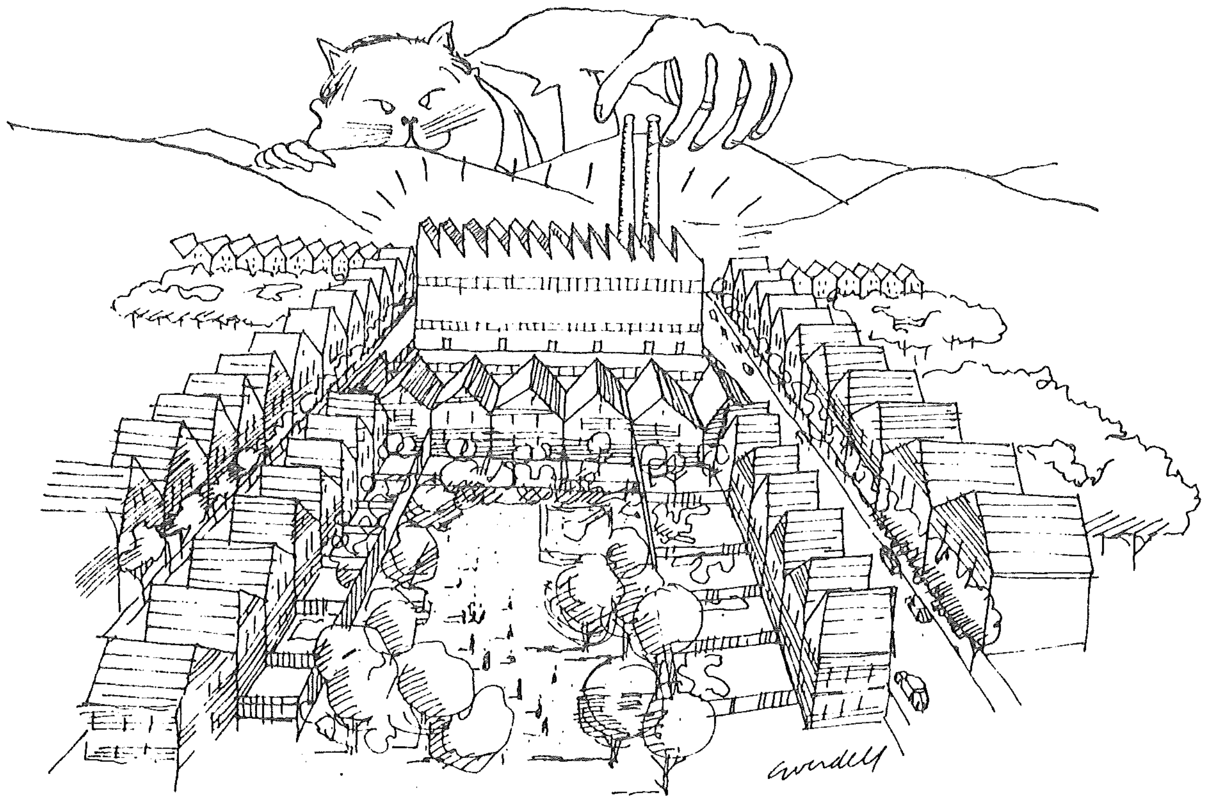

business incentive so great that the resulting cost reduction would, over time, induce at least some firms to increase their output and employment significantly. But the larger the incentives, the greater the tax revenue the state foregoes that might have been used to finance other things, such as state social services, repayment of interest on the state's bonded debt, and so on. There are, therefore, political limits to how much a state can offer in business incentives.

If and when some firms do respond to tax incentives by increasing output and employment, theoretically at least, they are most likely to be firms in the competitive sector, rather than oligopolies. Yet, according to the "dual labor market" literature, these are the industries that in general pay lower wages, offer worse working conditions, provide les stable (full year and/or full week) employment, and make it more difficult for labor to organize. Thus, incentives that lower costs of doing business appear to be policy instruments—if they work at all—that are most likely to "goose" the sector of the economy with the least desirable jobs, while providing windfall profits to the segment of the business community that least needs them.

Some business incentives, for example investment tax credits, are intended to lower the price of capital, and thus encourage firms to invest in new plants, expand existing plants, and relocate from other states. Though economic theory has not had great success in predicting investment decisions, one thing is clear: the decision to invest depends not only, or even primarily, on the cost of capital, but also on expectations about the likely "returns" to that investment through sales. Almost anything that a government can do to reduce the uncertainty about sales is more likely to induce businesspeople to go ahead and build or expand a plant than any other kind of public action—including the granting of incentives.

Orthodox theory ignores the question of who has access to capital for investment in the first place. Most treatments assume that capital is always available for a price. If it pays an investor to borrow the capital in order to build or expand his or her facilities (because the expected rate of return is higher than that available from other applications of the funds), the borrowing and investing will in fact take place.

But capital allocation depends only partly on "supply and demand." Blacks, women, entrepreneurs working in low-income communities, and nonprofit developers have trouble getting capital at *any* price. (Since the New York City debacle, state and local governments may be in the same category.) A particu-

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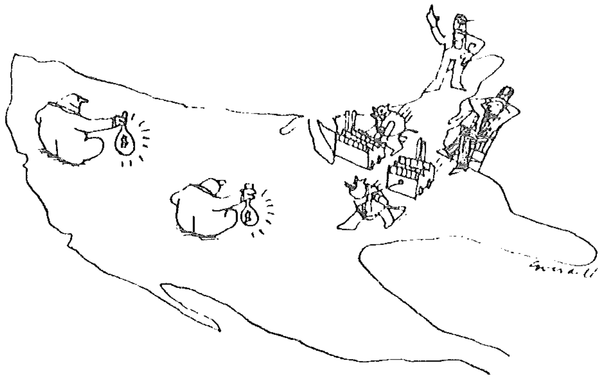
lar problem for these investors is the "debt-to-equity capital mix." Equity capital is usually obtained by selling stock in an enterprise. The lender (stockholder) is paid a share of the profits—if and when there are any profits. When capital is obtained through loans, however, the borrower usually has to begin paying back interest on the loan immediately, whatever shape the business is in. Thus, businesspeople who must rely mainly on loans for capital investments face high probabilities of failure because of their indebtedness. And equity capital is particularly scarce for the traditionally excluded groups mentioned above.

The smallest firms, with the poorest "track records," and the least powerful investors or groups, perhaps with no "track record" at all, find it most difficult to borrow or to attract new equity investments. Large firms with good credit ratings have less trouble raising their own capital, whether externally or through their own retained earnings. But if the investing and lending of private banks, or of state economic development authorities, is based on the creditworthiness of the borrower, then the normal operation of the capital markets will work to channel ever more financial resources to the oligopolists at the expense of the more competitive segment of the market. On the one hand, then, competitive industries are more likely to need tax and interest rate incentives and so they are more likely to take advantage of them. On the other hand, competitive firms face greater uncertainty about business success so they may be less likely to invest at all and thus they may not take advantage of state investment incentives.

Aside from some speculation about the different behavior of firms in oligopolistic industries compared to competitive industries, economic theory is ambiguous in predicting the impact of state incentives on job creation. This even extends to the national level, at least in terms of tax credits or tax cuts. The Brookings Institution conducted a series of econometric evaluations of the impact of the 1962 federal investment tax credit, which was designed to stimulate the business sector's demand for capital goods and therefore, indirectly, the demand for labor. Half of the studies concluded that the credit worked. But half concluded that it did not affect output and employment at all.

The Evidence

Judging from the speeches of elected and appointed officials and the editorials of newspaper writers, most people seem to expect new jobs to be created in a state's economy over time through the relocation into the state of plants that are closed down elsewhere, or through the decision of multiplant firms to build their



next new plant in the state. To this end, states use an additional policy instrument, industrial recruiting. They hire advertising agencies or management consultants to place ads and hustle up new business. Visiting company representatives are wined and dined, and shown around the state.

Most urban and regional economists believe that companies select regions by broad, qualitative criteria such as the availability of basic resources, adequate transportation access, and, though it is seldom put so bluntly, a politically passive labor force. The sort of cost differences that incentives try to create are considered less important.

For example, Peter Bearse, formerly the executive director of the council of economic advisers to the governor of New Jersey, discusses the role of these marginal cost differences in the corporate decision-making process:

Decisions can be arrayed in a hierarchy—from minor allocation decisions of the type described by textbook economic theory to major "all or nothing" decisions like the decision to move or build a plant. Major decisions are subject to thresholds and long gestation periods. Marginal adjustments in the cost of debt finance or in certain tax rates do not stand a chance of affecting a major decision unless a firm is at or near a threshold; and even then, several other factors are operative . . . . It is a question of probabilities—the odds that a given policy can have an intended effect. I claim that the concept of an adaptive, sequential decision making process subject to thresholds makes the efficacy of current policies look very dubious.

Bearse's doubts appear to be validated by the empirical data, sketchy though they are, that have been collected about corporate responses to the business incentives offered by various states.

Since the 1950s, government agencies and independent researchers have tried to measure the relative impact of business incentives on industrial location or expansion. Unfortunately, the quality of the empirical

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material is uneven. Nonetheless, with a very few exceptions, the literature does not reveal significant plant relocation or expansion resulting from interstate differentials in state business incentives.

Surveys have asked employers to name the factors that mattered in their decision either to expand their facilities in a particular location or region, or to move into that area. The firms seldom mentioned such things as state and local taxes or the availability of subsidized credit. When taxes or credits were specified by the questionnaire, the proportion of respondents checking them off usually rose to between 5 percent and 15 percent. When these surveys then asked the respondents to indicate whether these factors were "critical" or not, few considered them as such. The findings were similar for the relative importance of other types of business incentives. A wide range of "mentions" were recorded, state bonding programs for example, but no such factor was considered to be "critical" by more than a small proportion of the sample. The results of these surveys are remarkably consistent even though they were made at different times, under different circumstances, and in different areas of the country.

One of the earliest surveys was conducted in 1950 by the Survey Research Center of the University of Michigan. The managers of only 9 percent of 188 plants moving into Michigan felt that the state's tax benefits were an "important consideration" in their moves. A Regional Plan Association study of firms moving plants out of New York City between 1947 and 1955 concluded that 14 percent of the moves were related to interregional tax differentials. (A more recent study of firms moving facilities out of New York State, however, shows a much greater sensitivity to taxes as a cost of doing business, with half of the respondents indicating taxes as one factor in their relocation decision.) A questionnaire was mailed to firms expanding or relocating into seven southern states in the late 1950s; 11 percent of the respondents checked local taxes as a factor, but only 2 percent called that factor "critical." In a 1963 study of the movement of industrial plants into Ohio since before World War II, only 2 percent of the companies interviewed voluntarily cited tax differentials as a factor.

One particularly careful study was conducted at the Stanford Research Institute in 1964 by economist Robert Spiegelman. He analyzed the locational behavior of one of the more footloose industries, precision instrument manufacturing. More than one-half of the 45 firms in the study considered interregional tax differences relevant, but only one called them "the most important factor." In a mid-1960s survey of industrial migration into Texas, only 13 percent of the firms considered taxes to be one determinant of their decision.

A national mail survey conducted by the U.S. Department of Commerce in 1972, covering 2,900 companies in high-growth industries across the country, revealed that 78 percent considered tax incentives or "holidays" to be relevant to their locational decisions. But only 8 percent rated such incentives as "critical."

There is no way of knowing whether the person who answers these mail questionnaires is a public relations staffer, a lower-level executive, or the person directly in charge. In 1974, to get more precise responses, personal interviews were conducted in Massachusetts and Connecticut. Two legislative staffers interviewed executives of 15 Massachusetts companies from the pool of companies that had applied for state "job-creation tax credits." Credits were claimed by 14 of the companies for alleged expansion in excess of "normal" growth, and one was for relocation into Massachusetts. Every single interview yielded the same result: the company took actions according to its own plans, then learned about the existence of the tax credits and applied for them. An independent set of interviews with Connecticut businesspeople participating in that state's business incentive programs produced identical results. In these two states, at least, the availability of the incentives did not produce business behavior that would not have occurred otherwise. Instead, the incentives functioned as a windfall for the companies at the expense of the taxpayers.

One way to estimate the effects of the incentives while avoiding the inherently subjective nature of the survey approach is to compare the rate of job growth in states with high and low business taxes. C.C. Bloom correlated growth in manufacturing employment with per-capita state and local tax collections among all the states, for two periods, 1939 to 1953 and 1947 to 1953. In neither case was there a statistically significant relationship. An econometric model describing the growth of the Michigan economy between 1947 and 1955 showed no significant relationship between state and local taxes and employment growth over time. A nonprofit citizens organization, the Pennsylvania Economy League, rank-ordered 11 states in 1971 according to the burden of state and local taxation on ten specific industries. We find no systematic correlation between this rank ordering and the state unemployment rates; in fact, the lowest unemployment state, Indiana, was consistently found to be among the very highest tax-burden states for most of the industries. Finally, for 15 of 16 major industries studied in an econometric model of the Massachusetts economy describing the period 1950 to 1972, there was no statistically significant

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INCENTIVES GALORE!

Tax credits and forgivenesses. Property tax concessions are the oldest and most important of the business incentives offered by states. Twelve states and Puerto Rico permit cities and towns, counties, or the state itself to exempt part or all of business property from property taxation for a specified time period. Puerto Rico's tax incentive law is probably the most liberal: manufacturers of goods first produced in Puerto Rico after 1946 pay neither property nor income taxes for a period of up to 25 years. Three states provide similar, though smaller, tax concessions to new industry. Nine states give local counties or municipalities permission to give abatements to businesses on some or all of their local property taxes.

Alabama, Mississippi, Georgia, and North Dakota exempt new and/or expanding industries from local ad valorem taxes on all tangible property for a stipulated time period. (Ad valorem taxes are taxes levied on the value of property. Sales taxes, on the other hand, are based on the sale of goods and services.) New York, Massachusetts, and North Dakota give tax credits to businesses that expand employment. In North Dakota, new firms may receive a tax credit of up to 1 percent of their annual gross wage and salary expenditures for three years. In New York, firms that expand in low-income areas qualify for an income tax credit. Massachusetts gives income tax credits to businesses that employ people who were on welfare or drawing unemployment compensation.

Four states permit some form of investment tax credit. Firms may take a certain percentage of the cost of acquiring buildings, structures, machinery, and equipment as a tax credit and reduce their total state tax bill by the amount of the credit, which varies from state to state. New York and Rhode Island allow manufacturing firms a tax credit equal to 2 percent of the cost of new buildings, equipment, and facilities; Massachusetts allows 3 percent. Manufacturers in West Virginia may receive a credit equal to 10 percent of the cost of new production facilities for a period of ten years.

Loan guarantees. Thirteen states guarantee commercial loans. Ten of these states have organized industrial finance authorities specifically authorized to guarantee, on behalf of the state, the repayment of some or all of a mortgage or loan made by a conventional market source on an industrial facility. New Hampshire, the originator of the program, has a relatively modest policy: the state insures the portion of a loan that is in excess of 50 percent of a property's appraised value or in excess of 65 percent of the value of machinery and equipment. At the other end of the spectrum, Rhode Island guarantees up to 90 percent of the cost of plant construction. Most states charge firms a fee for administrative costs that ranges from 1 percent to 3 percent of the outstanding loan.

Industrial development bonds. There are two kinds of industrial development bonds: general (or "moral") obligation bonds, and revenue bonds. Thirteen states permit localities to float general obligation bonds, whose payments are guaranteed by the full faith and credit of the state or municipality. Forty-three states allow local governments to issue revenue bonds that are paid solely from the proceeds of the project and do not become the obligation of any government. Both types can be used to finance the construction of industrial development projects or sports facilities, convention or trade show buildings, docks, wharves, airports, parking lots and garages, sewage or solid waste disposal plants, and air or water pollution equipment. Income from general obligation and revenue bonds is usually exempt from federal taxation.

Low interest loans. Thirty states have state-chartered credit corporations that make loans to businesses unable to obtain long and short-term financing in the conventional capital markets. The corporations issue stock to banks, insurance companies, and other private parties which are often exempt from paying state taxes on their income.

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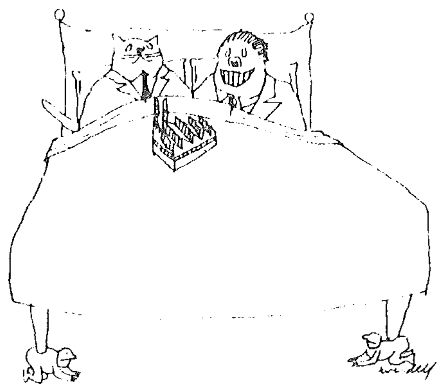
relationship between quarter-to-quarter changes in Massachusetts' share of national employment and changes in the ratio of Massachusetts' business taxes to the average for all states. Ephron Catlin, dean of Boston's financial wizards, banker extraordinaire, was recently quoted in a local paper: " . . . Our taxes aren't bad. I don't think many firms have moved out because of business taxes."

If, as seems to be the case, tax incentives are not very effective in luring businesses from one state to another, why not? We suspect that the main reason is that state and local taxes are such a small proportion of a firm's total costs of doing business. Incentives, in effect, reduce the cost of something that's not that important a consideration to begin with.

Interestingly enough, none of the empirical studies measure taxes in relation to business costs per se. We can get a good idea of their relative insignificance, however, from studies that estimate state and local taxes as a percentage of sales or of value added. (Value added is the actual contribution of a specific firm to the final market value of a good. If we take an auto factory, for example, the value of "intermediate products" made elsewhere—like steel bars or business forms—would not be included in the value added by the auto factory itself to the market value of autos.)

State and local taxes are consistently estimated at from a half to 3 percent of value added and from 2 percent to at most 5 percent of sales. A 1954 study in New York showed state and local taxes to be 1 percent of value added. In a 1958 calculation for Michigan, the ratio of state taxes to value added was under 1 percent. A study of five western states in 1963 found that taxes as a percent of value added ranged from a low of .93 percent in the food industry to a high of 2.73 percent in fabricated metals. Recently, the Federal Reserve Bank of Boston estimated that the average U.S. business paid 4.4 percent of its income to state and local governments. (This estimate, for 1973, breaks down into .9 percent going to pay corporate income taxes, 1.9 percent for property taxes, .8 percent for unemployment compensation contributions and .8 percent for "other business taxes.") Since corporate and unincorporated business income averages about one-eighth of the value added, this translates into an average ratio of state and local taxes to value added of about .6 percent.

Using another measure, J.A. Stockfish of the California Economic Development Agency found that state and local taxes as a percentage of stockholders' equity varied among selected industries over 17 states within a very narrow range: 3.9 percent (fabricated metals) to 6.4 percent (apparel).



Businesses, of course, must consider not only the cost of state taxes, but federal taxes as well. In Massachusetts, for example, a manufacturing or research-and-development firm is allowed to credit, against its annual state excise tax liability, 3 percent of the cost of new investment in buildings, machinery, or other equipment. The legislature intended this to be quite a large tax incentive to expand or relocate in Massachusetts. But the amount deducted from the state taxes, as a credit, is an addition to the firm's income, which is subject to the 48 percent federal corporate income tax. The saving is, therefore, cut almost in half. Suppose a middle-sized manufacturing firm, with total annual operating costs of $6.7 million, undertakes a new investment of $800,000 in Massachusetts. The state credit for the investment would be $24,000 ($800,000 x .03). But of the $24,000 "saved," the federal tax takes $11,520 ($24,000 x .48). The real saving to the firm is $24,000 less $11,520. or $12,480. And that amounts to a mere .19 percent of its total costs.

Since expansion or relocation decisions are assumed, even by the advocates of these policies, to depend on relative total costs in different places, it is no wonder that these, and similar, state business incentives don't have any great influence over corporate decision making. And since nearly all of the states follow one another in legislating these incentives, the savings differentials from one state to another are by and large meaningless.

Finally, the incidence of physcial plant relocations—the objective of the incentives—is actually very small in the United States, *whatever* causes it. Between December 1969 and December 1972, according to an MIT-Harvard Joint Center for Urban Studies report using Dun and Bradstreet credit-rating data on all manufacturing and most nonmanufacturing firms in the country, plants moving into a state added an average of only .3 percent to that state's 1969 employment base; plants moving out took an average of only .2

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percent of the jobs with them. In no single state was the gain or loss of jobs due to moving plants ever greater than .5 percent. This was, of course, a recessionary period, and data through 1973 may show increased movement of plants. Nevertheless, this first empirical estimate makes the competition among the states for new plants seem even more futile. There are few winners, yet all states incur costs.

In fact, the winners may not even benefit from relocated industry, however it is attracted. If the company brings part or all of its labor force with it, the new families will place an increasing burden on the social services, housing, and labor markets of the receiving state, and there will be at best only a small net effect on the local unemployment rate. If only the skilled labor force is relocated, the local job creation will occur in the unskilled, low-wage segment of the labor market. Only recently have state and local planners begun to look carefully at the expected impact of new plants on environmental quality and maintenance costs; under many circumstances, these, too, could more than offset the job-creation and tax benefits accruing to the state from successful industrial recruiting.

The Costs

Tax incentives force a state to forego tax revenue—the revenue that would have been collected in the absence of the incentives. The goods and services these foregone revenues could have purchased are called the "opportunity costs" of tax incentives. According to estimates made by the Massachusetts commissioner of taxation, his state lost about $65 to $70 million from six of the ten tax incentives the state offered to businesses in 1974. Calculations were not done for the other four incentives, but they probably would have brought the cost to over $100 million a year.

Mortgage guarantees, loans, and industrial development bonds do not reduce the amount of taxes that accrue to state governments, but there are also opportunity costs associated with these types of incentives.* These costs have to do with the availability and price of capital. Who will be affected by this "capital crowding" depends on the reaction of financial institutions to the overall economic conditions at the time. Though we know of no empirical estimates of these costs at the state and local level, a look at the financing process itself illustrates the problems.

Banks have a finite amount of savings at any one time, and they have to allocate their investments among different kinds of bonds and loans. Assuming everything else is equal, financial institutions prefer mortgages that have their payments guaranteed by government over unsecured loans, and tax-exempt bonds over taxable investments. To compete for these limited bank funds, others who seek capital for investment must pay higher rates of interest to the banks. Private investment is therefore more expensive for the borrower than it might have been in the absence of government-backed and tax-exempt financial instruments.

In recent years, banks have come to hold almost two-thirds of all state and local industrial development bonds. Banks are very "unstable" customers; they tend to purchase tax-exempt bonds when money is easy, when they have met their obligation of a legally required reserve, and when they have satisfied the loan needs of their customers. When money becomes tight, banks raise cash by selling their state and local securities. States and localities wishing to finance capital projects in periods when banks are reducing their portfolios of state and local bonds have two choices: they can either pay high interest rates on the bonds to attract other investors; or, where possible, finance their projects with short-term notes. Short-term notes, however, have their own disadvantages. First, they usually carry a higher effective rate of interest (including underwriting charges) than long-term obligations and thus cost the public more. Second, they are only a temporary solution to a serious economic situation and are not themselves marketable when money is scarce.

If incentives are as ineffective and costly as they appear to be, why are they so widely used? Perhaps the explanation is that state governments have so little power to affect their local economies, officials feel compelled to do *something*; and local taxes and bonding are something they can manipulate. Perhaps these officials are simply serving the class interests of the business sector for whom such incentives are a source of profit.

However uncertain the motivation of state officials, we believe the motivation of private corporations is clear-cut: to increase their own income at the expense of workers, consumers, and the public sector. Governments, of course, must tax the business sector to help finance the production and delivery of public goods and services. Not surprisingly, businesses resist

*They do, however, affect federal tax revenues. Harvard's Stanley Surrey estimates that in fiscal year 1968, the federal income tax deduction of the interest on state and municipal bonds cost the U.S. Treasury about $1.8 billion. According to the U.S. Office of Management and Budget, in fiscal year 1976 the foregone federal revenues will amount to nearly $4.8 billion, with three-fourths of that accruing to corporations and only one-fourth to private individuals. A recent study has concluded that the loss to the U.S. Treasury from the flotation of industrial development bonds alone was about $90 million in 1973.

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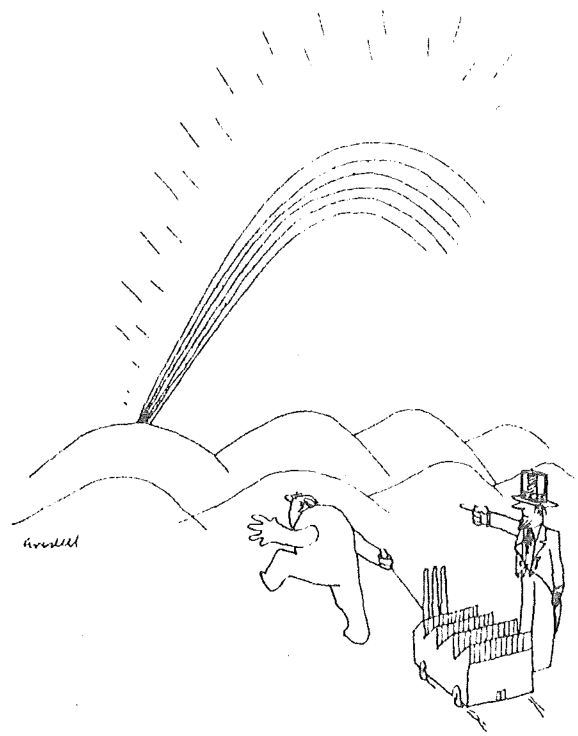

this redistribution and try to reverse it through lobbying efforts if they can. Peter Bearse notes that some are more successful than others:

It should be no surprise to anyone that development programs are biased towards the established industry, larger firms, low-risk debt finance and manufacturing. Any stroll through state legislative chambers will show that these are the better organized, articulate political interests.

One representative of "Jobs for Massachusetts," a prominent business lobbying group, told Harvard researcher James Dumont that he would prefer an outright cut in the state's corporate income tax rate, but since the former was hard to obtain, "tax incentives will have to do." Another lobbyist, who led the successful struggle for passage of the Massachusetts $500 "job creation tax credit," admitted that his organization fully intended the credit to be a "gift" to companies, to "compensate" for the state's high tax rates.

Some officials think that their probusiness stance will create a "positive climate for investment" in their particular states. If history is any guide, however, that is a losing strategy, particularly when applied to the older industrial areas. Ever since the beginning of the industrial revolution, capitalist economic growth has been marked by "uneven development," a description first used by Friedrich Engels. When capital can be invested more profitably someplace else, those who control the processes of production abandon one area for another—even if it means leaving behind whole systems of physical capital, like neighborhoods and even entire regions. And those who remain become increasingly dependent on the public sector.

Bearse argues that uneven development explains much of the decline in the economic fortunes of the older industrial belt of the United States. As markets, capital, and even new research and development shift from the older region (with New York City at its political center) to the newer South and Southwest (with Texas the potential new "capital"), the older places undergo secular deterioration.

There is some evidence that the business incentives are in fact most readily available in these older areas. But, in the context of the larger historical movement of capital, the idea of restoring the older area's comparative advantage seems ludicrous. As the public costs in the South and the Southwest increase over time, taxes and other costs of doing business there will rise too. But there is no reason to think that firms will then turn around and repopulate, say, New England. Clothing firms, in fact, are now moving out of South Carolina to Colombia and other parts of South America.

This shifting of the center of economic activity away from the northeastern and north-central parts of the country (a shift that goes a long way toward explaining the current fiscal crisis of the older cities and states) has been supported and consciously promoted by the federal government since the end of World War II. Public investments in infrastructure, military production contracts, and new bank charters have all been awarded increasingly to southern and southwestern firms, often at the expense of those in the older regions (especially New York). In this context, state incentives to businesses in lagging areas are equivalent to welfare grants, serving at best to ease their pain.

Even if the incentive approach were successful, however, we believe it would be misplaced. The conventional theory of local economic development centers on the concept of industry producing for export. The industry employs local workers and purchases locally produced goods and (especially) services. According to this conventional wisdom, who owns and controls that exporting activity, and whether that ownership/control is "absentee," is of little consequence. Because the payoff for capturing such export-base activity is believed to be so high, states and local governments engage in an expensive competition for the thousand or so new plants built in this country each year.

"Economic colonialism," as the gubernatorial contenders in Mississippi seem to have discovered, is not

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the answer to economic development needs within states. That kind of development produces the same sort of dependency and unbalanced economic growth in the rich United States as it has always done in the poor Third World. New plants that are controlled by corporations headquartered elsewhere impose enormous infrastructure costs on a community. They import much of their labor (especially the "good" jobs), and they often house their highest-paid workers outside the taxing jurisdiction where the plant is situated. Then—after all the effort expended to get them in the first place—they often move to some other place when the local inducements run out.

It is the planning and financing of community-based enterprises that should be getting the lion's share of the resources generated by state and local taxes (and federal, for that matter). The present economic development applications of such resources are, we are convinced, going largely to windfall profits for the business sector. Surely that is at best a waste of scarce resources, and at worst a politically inequitable approach to the pursuit of economic development.

WP

NOTES AND SOURCES

There are a number of empirical and theoretical studies in the field of industrial location, some of which are cited in this article. A good, but dated, summary of the literature can be found in John Due, "Studies of State-Local Tax Influences in Location of Industry," *National Tax Journal*, Vol. XIV, June 1961.

Additional readings for those interested in the subject include the following:

Peter Bearse, "Government as Innovator: A New Paradigm for State Economic Development Policy," New Jersey Economic Policy Council, 1975. Available from the Center for New Jersey Affairs, Princeton University, Princeton, New Jersey.

Alfred Eichner, *State Economic Development Agencies*, University of Michigan, 1970.

Gary Fromm (ed.), *Tax Incentives and Capital Spending*, Brookings Institution, 1969.

David M. Gordon, *Theories of Poverty and Underemployment*, D.C. Heath, 1971.

Bennett Harrison, *Economic Development of Massachusetts*, Joint Committee on Commerce and Labor, Massachusetts Legislature, November 1974.

Charles Henning, William Pigott, and Robert Scott, *Financial Markets and the Economy*, Prentice-Hall, 1975.

Kirkpatrick Sale, *Power Shift*, Random House, 1975.

N.M. Singer, *Public Microeconomics*, Little, Brown and Company, 1972.

Stanley Surrey, "Tax Incentives as a Device for Implementing Government Policy," *Harvard Law Review*, February 1970.

The Use of Public Funds or Credit in Industrial Location, New York State Department of Commerce, Research Bulletin No. 6, January 1974.

Leonard Wilson and L.V. Watkins, "How States Plan," *Challenge*, January/February 1976.

Business Incentives, By States, 1974

1. *State, county, or local property tax exemptions:* Hawaii, Kentucky, Louisiana, Maryland, Michigan, Montana, New York, Oklahoma, Puerto Rico, Rhode Island, South Carolina, South Dakota, Vermont.

2. *Ad valorem or sales tax exemption for plant, machinery, or equipment:* Alabama, Georgia, Mississippi, North Dakota.

3. *Tax credits to expand employment:* Massachusetts, New York, North Dakota.

4. *Investment tax credits:* Massachusetts, New York, Rhode Island, West Virginia.

5. *Mortgage or loan guarantees:* California, Connecticut, Delaware, Hawaii, Indiana, Maine, Maryland, Mississippi, New Hampshire, North Dakota, Ohio, Rhode Island, Vermont.

6. *Local industrial development bonds (general obligation):* Alabama, Arkansas, Hawaii, Kentucky, Louisiana, Maryland, Massachusetts, Mississippi, Missouri, North Dakota, Oklahoma, Tennessee, Washington.

7. *Local industrial development bonds (revenue):* Alabama, Arizona, Arkansas, Colorado, Florida, Georgia, Hawaii, Illinois, Indiana, Iowa, Kansas, Kentucky, Louisiana, Maine, Maryland, Massachusetts, Michigan, Minnesota, Mississippi, Missouri, Montana, Nebraska, Nevada, New Mexico, New York, North Carolina, North Dakota, Ohio, Oklahoma, Oregon, Pennsylvania, Rhode Island, South Carolina, South Dakota, Tennessee, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wisconsin, Wyoming.

8. *State-chartered credit corporations:* Alaska, Arkansas, Connecticut, Florida, Iowa, Kansas, Kentucky, Maine, Maryland, Massachusetts, Mississippi, Missouri, Montana, Nebraska, New Hampshire, New Jersey, New York, North Carolina, North Dakota, Pennsylvania, Rhode Island, South Carolina, South Dakota, Texas, Utah, Vermont, Virginia, Washington, West Virginia, Wyoming.

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STATE OF MAINE
OFFICE OF LEGISLATIVE ASSISTANTS
STATE HOUSE
AUGUSTA, MAINE 04333

May 18, 1977

To: Committee on Taxation

From: James A. McKenna

Subject: Business tax incentives

Please find enclosed a short memo on the various choices to be made when considering business tax incentives and a summary of the Feb. 1977 study commissioned by Casco Bank and Trust Company, Why Firms Decide For or Against a Maine Location. Three major findings of this study (based on a 40% return on their questionnaire) are:

-- Nearly half the firms that have recently located or relocated in Maine identified labor supply characteristics, suitable land or existing buildings, and our reasonable tax structure as among the most important factors in their final decision. (emphasis added)

-- Heat and energy costs, labor productivity and cost, as well as the cost of living were all identified as important in varying degrees to those who located in or seriously considered Maine.

-- Firms that have decided against or ruled out a Maine location identified distance to their markets or suppliers as a primary factor in their decision.

JAMK/lk
Enc.

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STATE OF MAINE
OFFICE OF LEGISLATIVE ASSISTANTS
STATE HOUSE
AUGUSTA, MAINE 04333

May 19, 1977

To: Committee on Taxation

From: James A. McKenna

Subject: Tax breaks for businesses

My research indicates that the major factors to be considered when discussing business tax breaks are:

1. A business tax break is received whether or not the business was going to expand without such tax incentives. Thus, tax breaks seem inefficient compared to more direct Government aid to business (e.g., assistance in raising capital if the business cannot obtain it through normal commercial channels).

2. In Maine the business tax climate seems currently to be considered "reasonable" and, in fact, a reason why companies move here or expand here (<u>see</u> Appendix A, summary of the 1977 Casco bank report).

3. The two major factors considered in business location or expansion in Maine are:

   A. Will the company make a profit in Maine; and

   B. Is the "quality of life" the business owners and employees will have in Maine acceptable.

Thus, it seems to me when considering how Maine can most efficiently spend money to attract business in Maine, the crucial questions to be asked are:

1. Is the current tax climate so poor that the best remedy is a tax incentive available to all businesses, whether or not they need it?

2. Or, if money is to be spent improving the attractiveness of Maine to businesses should it be spent on

   A. Direct aid for specific business problems (e.g. cost of capital or cost of transportation to markets or cost of energy).

B. Direct aid for the business infrastructure (e.g., sewage, improved vocational training, development of local and state economic plans, inventory of labor characteristics of each community).

3. Or, should the decision be made that the business profit climate is reasonably sound and that the quality of life in Maine -- the other major factor in business location or expansion decisions -- should be improved.

Clearly, in a time of limited resources, the benefits of each of these courses of action must be balanced against the others.

Please find attached a summary of the Feb. 1977 Casco Bank study, Why Firms Decide For or Against A Maine Location.

JAMK:lk
Attachment

From, Why Firms Decide For Or Against A Maine Location, a Feb. 1977 study commissioned by Casco Bank and Trust Company

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Section III. Summary, Conclusions and Recommendations

As stated earlier, the purpose of our research was to answer the following three questions:

1. For what reasons have firms recently located or relocated in Maine?

2. Why have some firms seriously considered but decided against a Maine site?

3. Why did a number of northeastern-based firms never consider a Maine site in their most recent locational decision?

In answer to these questions:

. Firms that have recently located or relocated in Maine identified the quality of Maine's work force, present state and local tax burdens, realized and anticipated energy and heating costs, and existing plant structures or suitable land as among the most important factors in their final decision.

. Firms that have decided against or ruled out a Maine location identified distance to their markets or suppliers as a primary factor in their decision.

As indicated in earlier pages, between 1975 and 1976 Maine's ability to attract new manufacturing activity improved measurably (by 43%) compared to the average for all New England states. Nevertheless, Maine continues to rank third, behind Vermont and New Hampshire, in its present ability to attract new manufacturing firms.

Maine can improve this situation by magnifying the state's perceived strengths regarding labor, land, and existing structures while at the same time minimizing weakness with respect to distance from major markets and suppliers.

Magnify Strengths:

. All Maine communities should develop, alone or in conjunction with other areas, both short and long range plans which articulate resident economic objectives. The state and regional plans might then be a synthesis of this thinking.

. Maine communities, with both public and private assistance, might begin by determining their labor market boundaries. That is, over what distance might people be expected to commute to a new employment opportunity? Labor supply characteristics within these areas then should be evaluated, inventoried, and summarized. For a number of larger communities, these tasks have already been partially accomplished.

. Existing buildings should be inventoried with an eye to the cost of rehabilitation and reuse. A determination should be made as to what type of activity the renovated structure might house.

. Depending upon the community economic plan, a number of questions might be asked such as: what financial alternatives are available to the community for the construction of a speculative building? Has suitable land been zoned and set aside for economic development?

. Community and industrial development people in Maine are highly rated, but they don't have the level of visibility attributed to those outside the state, particularly agents involved in industrial real estate. Through an intensiv marketing research effort, the visibility of Maine's economic development people could be increased.

. Good informal lines of communication between summer and winter residents should be established in each community (if they are not already) in order to explore the various background connections of individuals who might be instrumental in influencing a firm to seek a Maine location. This might begin with informal "town meetings" held during the summer season.

Minimize Weakness:

. Distance to markets or suppliers and related costs may be minimized by examining various rate structures. Rail rates with respect to certain types of commodities--grain, etc. are presently being considered. Although the Maine Turnpike will, according to various acts of Congress, become a toll-free road in 1980, the rate structure should be examined to minimize impediments to economic development efforts. What might be the response of certain types of traffic to rate reductions by vehicle classification?

. Economic development efforts should focus upon those industries where transportation costs represent a small percentage of the total cost of either producing or marketing the product. Certain activities involving the printing, photography, and manufacture of specialized electronics may fall into this category. Present attempts at increasing the value added to products in Maine would in effect reduce transportation costs. Increased service industries that use the mail as a means of transporting their product--insurance industries, consulting activities, etc.--would also help to reduce transportation costs.

. Increasing costs of transportation due to energy constraints and long-range weather cycles will increase the economic viability of locally made products for nearby markets. This is especially true for food and other products where relative transportation costs represent a large percentage of total costs.

Strategically-placed advertising and publicity can dispel Maine's stereotype as an isolated, snowbound, culturally barren outpost. Documented data can show that:

1. Excellent highway systems, combined with minimum urban traffic congestion, minimize travel time

a. between major Maine cities
b. between cities and residential "suburbs"
c. between residential and recreational areas: lakes, ocean, ski areas, etc.
d. between Maine points and other major cities: Boston, Montreal, New York.

Information on air travel time also should be included, to prove that in Maine, "you CAN get there from here"--faster--than if you lived in other areas.

2. Because Maine's highway departments are accustomed to winter weather, roads are cleared rapidly, even after major snowstorms. This applies to most Maine roads--not just major arteries.

3. In addition to its natural resources, Maine offers a wealth of cultural and recreational activities: theatre, concerts, art galleries, sports and entertainment arenas in Augusta and Portland, and fine restaurants throughout the state. An arts calendar page torn from any Maine city newspaper will flatly

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contradict the statement that there is "nothing to do" in Maine.

Finally, it should be recognized that there is no one factor that might be altered which would significantly influence the number of firms seeking a Maine location. On the other hand, personal contact appears to be extremely important in any successful economic development effort.

In sum, our study identifies factors important to firms recently locating in Maine and the northeastern part of the United States. At the same time, recent site choices indicate the importance of relative population centers, organized labor markets, developed transportation systems, utilities, and sewerage. Firms locate or relocate into areas that exhibit some level of economic development. As stated earlier, this likely means that many Maine communities and counties may have to develop to a certain economic level from within their borders before they can expect to attract firms from outside the state. Therefore, encouragement of local initiative and entrepreneurship may be a necessary first step in attracting new firms to many communities in the state of Maine.

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STATE RANKING OF BUSINESS CLIMATE
BY FANTUS COMPANY
NET MANUFACTURING JOBS WON/LOST, % INCREASE/DECREASE, (1967-1974)
U. S. Department of Labor - Manpower Report to the President

Fantus Ranking	State	Net Mfg. Jobs Won/ Lost - 1967-1974		% Increase/ Decrease	% Ranking	Jobs Won Ranking
1	Texas	150,000	Won	22.6% Increase	14	1
2	Alabama	50,000	Won	16.8% Increase	19	9
3	Virginia	55,000	Won	15.9% Increase	20	6/7
4	South Dakota	6,000	Won	40 % Increase	5	27/28
5	South Carolina	54,000	Won	16.9% Increase	18	8
6	North Carolina	122,000	Won	18.4% Increase	16	2
7	Florida	81,000	Won	27.6% Increase	12	4
8	Arkansas	49,000	Won	32.2% Increase	8	10
9	Indiana	20,000	Won	2.8% Increase	31	21
10	Utah	19,000	Won	38 % Increase	6	22
11	North Dakota	5,000	Won	55.6% Increase	3	29/30
12	Mississippi	47,000	Won	28.1% Increase	11	11
13	Georgia	44,000	Won	10 % Increase	27	12
14	Iowa	28,000	Won	12.8% Increase	25	18/19
15	Tennessee	77,000	Won	17.7% Increase	17	5
16	Arizona	33,000	Won	41.8% Increase	4	15/16
17	Nebraska	10,000	Won	12.5% Increase	26	25
18	Colorado	33,000	Won	32 % Increase	9	15/16
19	Missouri	4,000	Lost	.9% Decrease	34	37
20	Kansas	21,000	Won	14.4% Increase	21	20
[illegible]	Oklahoma	37,000	Won	31.9% Increase	10	14
22	Kentucky	55,000	Won	23.8% Increase	13	6/7
23.5	Nex Mexico	11,000	Won	61.1% Increase	2	24
23.5	Wyoming	1,000	Won	14.4% Increase	22	32
25	Idaho	13,000	Won	37.1% Increase	7	23
26.5	Louisiana	8,000	Won	4.6% Increase	30	26
26.5	Ohio	6,000	Won	.4% Increase	32	27/28
28	New Hampshire	3,000	Lost	3.1% Decrease	37	36
29	West Virginia	6,000	Lost	4.5% Decrease	40	38
30	Maine	12,000	Lost	10.3% Decrease	45	39
31	Montana	3,000	Won	13.6% Increase	23	31
32	Nevada	5,000	Won	71.4% Increase	1	29/30
33	Rhode Island	1.000	Lost	.8% Decrease	33	33/34
34	Wisconsin	28,000	Won	5.5% Increase	29	18/19
35	Illinois	60,000	Lost	4.3% Decrease	39	44
36	Maryland	30,000	Lost	10.6% Decrease	46	41
37	New Jersey	71,000	Lost	8 % Decrease	42	45
38	Vermont	1,000	Lost	2.3% Decrease	35	33/34
39	Washington	24,000	Lost	8.7% Decrease	43	39
40	Oregon	32,000	Won	19.4% Increase	15	17
41	Minnesota	41,000	Won	13.5% Increase	24	13
42	Pennsylvania	88,000	Lost	5.7% Decrease	41	47
43	Connecticut	48,000	Lost	10 % Decrease	44	43
44	Delaware	2,000	Lost	2.8% Decrease	36	35
45	Michigan	35,000	Lost	3.1% Decrease	38	42
[illegible]	Massachusetts	82,000	Lost	11.7% Decrease	47	46
47	California	94,000	Won	5.9% Increase	28	3
48	New York	286,000	Lost	15.2% Decrease	48	48

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MAINE
STATE LEGISLATIVE CLIMATE
RANKINGS

		Rank Out of 50 States	Rating
1.	Corporate income tax as a source of state financing.	9	Excellent
2.	Per capita property taxes paid.	31	Fair
2a.	Public assistance outlays per capita.	39	Fair
3.	Per capita personal income taxes paid.	12	Excellent
4.	Per capita taxes paid.	23	Good
5.	Per capita state and local taxes.	26	Fair
6.	Labor laws favorable to industry.	27.5	Fair
7.	Existence of laws regulating strikes, picketing, and boycotts.	25	Good
7a.	Regulation of labor unions.	30	Fair
8.	Average unemployment compensation rate.	45	Poor
9.	Workmen's compensation benefits per employed worker.	17	Good
10.	Number of governmental units per capita.	41	Poor
11.	State and local government payrolls for functions other than education.	15	Good
12.	Per capita debt.	36	Fair
13.	Per capita state and local debt.	17	Good

STATE SUMMARY:	Number	% of Total
Excellent Rating	2	
Good Rating	5	
Total Excellent & Good	7	47%
Fair Rating	6	
Poor Rating	2	
Total Fair & Poor	8	53%

MAINE
CHARACTERISTICS OF THE POPULATION
RANKINGS

		Rank Out of 50 States	Rating
14.	Selective service rejection rate.	27	Fair
15.	Average school years completed.	28	Fair
16.	School attendance as a percent of enrollment.	19	Good
17.	Percent of those eligible who voted.	10	Excellent
18.	Proportion of owner-occupied homes.	5.5	Excellent
19.	Percent of families earning under $3,000.	19.5	Good
20.	Percent of workers belonging to a union.	23	Good
21.	Lost time due to work stoppages.	13	Good

STATE SUMMARY:	Number	% of Total
Excellent Rating	2	
Good Rating	4	
Total Excellent & Good	6	75%
Fair Rating	2	
Poor Rating	0	
Total Fair & Poor	2	25%

MAINE
FACILITIES FOR LIVING
RANKINGS

		Rank Out of 50 States	Rating
22.	Educational expenditures per pupil.	40	Poor
23.	Average student-teacher ratio.	27.5	Fair
24.	Availability of institutions of higher education.	15	Good
25.	Vocational education expenditures per capita.	20	Good
26.	Recreational expenditures per capita.	13	Good
27.	Park acreage per 1,000 persons.	44	Poor
	Hotel and motel availability.	5	Excellent
29.	Fishing and hunting license holders.	35	Fair
30.	Number of physicians per 1,000 persons.	34	Fair
31.	Hospital beds per 1,000 persons.	21.5	Good

STATE SUMMARY:	Number	% of Total
Excellent Rating	1	
Good Rating	4	
Total Excellent & Good	5	50%
Fair Rating	3	
Poor Rating	2	
Total Fair & Poor	5	50%

Business Tax Reform in New York State A Costly, Complicated Goal, Study Finds

New York Times
June, 1977

By MICHAEL STERNE

Reforming the New York State tax system to make the state more attractive to business and businessmen will be more costly, complicated and politically difficult than has been assumed by many public and private sector leaders, according to a new study made for Governor Carey.

The study, by the state's little-known Economic Development Board and still unpublished, examined the full effects of the tax structure on personal and business income in detail for the first time. It found that:

¶The personal income tax, despite steeply progressive rates of 1 percent to 15 percent that are designed to hit the rich harder than the poor, actually imposes roughly equal rates of 9 to 11 percent on all income classes.

¶Any reduction in the top rates, which has been proposed to keep businessmen from moving out of the state, would make the system regressive—that is, more burdensome on the poor than on the rich.

¶The factor that evens out New York State's progressive tax rates and makes them less burdensome on high-income families than they seem is the deduction of state and local tax payments from Federal tax liabilities. But this factor, the study says, is "a double-edged sword," making it very costly for the state to offer tax relief to a prosperous businessman. To give such a man $100 worth of relief would re quire the state to give up $200 in revenues.

¶Despite the Federal tax offset, the study says, "at every income level New York State personal tax burdens are greater than those imposed by other states," and in New York City "the burden is even higher." An upstate New Yorker can cut his tax bill 20 to 33 percent by moving to California and 40 to 70 percent by moving to Texas. New York City residents could save 5 to 10 percent more by making the same moves.

¶Until the 20 percent surcharge on the business income tax was reduced by the Legislature this year, the tax burden on manufacturers was higher in New York than in other states.

¶The business tax rebates authorized in 1977, which wiped out the surcharge for most companies, now make New York competitive with other states. But the rebates are effective only for this year and would have to be extended by the Legislature to continue.

¶The burden of business taxation falls unevenly and favors multinational and multistate companies that make most of the sales out of the state. Companies that sell all or most of their output in the state pay the most and have a real incentive to invest in plants outside New York.

¶The additional tax burdens New York City imposes on business makes the city uncompetitive with the rest of the state and with other states. The study's calculations, however, were made before Mayor Beame advanced a group of proposals to reduce the city's business taxes. These measures, if they are approved by the Legislature, are expected to reduce, but not eliminate, the tax gap between the city and other jurisdictions.

The study was completed late last month and has been circulating quietly for the last few weeks among Mr. Carey's cabinet aides and among members of the Economic Development Board, a group of business and labor leaders that advises the Governor.

Business Tax Reform Urged

Donald A. Gaudion, a Rochester businessman who is chairman of the board, said yesterday that there were no plans to make the study findings public until he and his colleagues had an opportunity to assess them and to frame recommendations.

A copy obtained by The New York Times showed that the study makes only one firm recommendation — that the method for computing business tax liability be amended promptly to make it more equitable for companies that sell most of their output within the state. Without that adjustment, such companies pay such high taxes that they have an incentive to move or to establish plants outside the state. The estimated cost of such a measure would be $14 million a year.

The board's small professional staff, headed until last month by Dr. Richard W. Richardson, an economist, did the study with the help of outside consultants. It is believed to be the most thorough assessment ever made of what it costs in taxes to live in New York State and to operate a manufacturing business here.

Unlike previous studies, which looked primarily at published tax rates, the board study set out to find what accountants call the "bottom line" what is left after the totality of tax costs is deducted.

For individuals, this approach meant not just comparing income-tax rates from state to state, but property and sales taxes as well. Using patterns of expenditures at different income levels derived from Federal tax data, the study examined the taxes that would be paid in 30 locations in 12 states by families earning $9,000, $12,000, $20,000, $30,000 and $50,000 a year.

For manufacturers, the study looked at the full range of tax costs at the same 39 locations for three types of companies —pharmaceuticals, food and apparel. The basic question for business was: What locations would allow the largest after-tax returns on a new plant investment of $1 million?

After-Tax Returns Compared

The results varied considerably, but showed, generally, that New York State was competitive in business taxes. The study found, for example, that for a drug company that sold 10 percent of its output in its home state, the after-tax return would be higher in Texas than in New York, but lower in New Jersey, North Carolina, Tennessee, Arkansas, Ohio, Indiana, Pennsylvania, Connecticut, Kansas, California and Washington.

If, however, such a company sold 50 percent of its output in its home state, then four other states would provide a higher after-tax return—Washington, Arkansas, New Jersey and Tennessee.

Because of the complexity of such computations and the variety of factors that can affect after-tax results, the study said that drafting proposals to lower business taxes equitably would be extremely difficult. A broad-stroke measure, like a percentage reduction for all, might give too much relief to some kinds of companies and not enough to others.

"The characteristics of the individual firm are at least as important in determining the tax ranking of New York State as the actual tax schedules in the state tax structure," the study said.

The study also points out that though it is widely assumed that companies locate new plants on the basis of tax costs, there is no hard evidence to support this. Other factors—among them labor, energy, transportation, land and business costs, and the regulatory climat—are also important, with different companies giving different weights to each factor.

Attractive Alternatives Noted

For individuals, job opportunities, family ties and the level and adequacy of personal services and amenities may weigh more heavily than taxes. Nevertheless the study showed that a businessman who decided where to live principally on the basis of how much of his income was left after taxes would not chose New York State.

A businessman earning $20,000 a year would keep $836 more of it if he lived in Yolo, Calif., $878 more if he lived in Elkhart, Ind., and $1,361 more if he lived in Denton, Tex. If his income was $30,000 a year, the differentials would be $1,356 in Yolo, $1,684 in Elkhart and $2,404 in Denton. At earnings of $50,000 a year, the differences grow to $2,206 in Yolo, $3,256 in Elkhart and $4,253 in Denton.

Earlier studies have cited New York State's higher personal taxes as a reason for the movement of businessmen out of the state and have recommended reducing the tax rates on high earners. A 1976 study made for the Municipal Assistance Corporation, for example, proposed bringing down the income tax rates from 15 to 10 percent in steps over a five-year period.

Revenue Problem Stressed

The Economic Development Board study warns against such a step. Based on its finding that the Federal tax offset makes the state's system proportional (equal rates applied to all) rather than progressive (higher rates on higher incomes), it says that a reduction in the top rates would make the system regressive (higher rates on lower incomes).

"This would require a broad change in New York's tax philosophy, which has traditionally favored progressive taxation," the study said. It also said that an alternative way of attacking the problem—giving tax relief to the rich while extending it to the poor as well—would be took expensive in terms of lost government revenue.

The study made no estimate of the costs of lowering income tax rates for all, but it pointed out that half the state's tax revenues now came from taxpayers with incomes under $20,000. This means that even a small cut for those with lower incomes would make a deep cut in state tax receipts.

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PEOPLE & TAXES
OCTOBER, 1976

SPECIAL REPORT

Intangibles: States Ignore Rich Vein

by DONALD FIRKE and SUSAN KNIPPS

Across the nation state and local governments confronted by fiscal crises are being forced to raise taxes while they cut services. Since the property tax is a major source of revenue for these jurisdictions, citizens in all areas find their greatest lifetime investments --their homes --assessed at higher values and taxed at higher rates, yet protected by fewer police and fire fighters.

Even while legislators and home owners both struggle to balance their respective budgets, over $2 trillion worth of property goes untaxed by property tax systems in the U.S. This figure represents the value of intangible property in the U.S. --stocks, bonds, savings accounts and the like.

Intangible property currently amounts to four-sevenths of all wealth in the United States. Quite naturally, it is principally the property of the rich. (In fact, the richest 1% of the population owned over 50% of all corporate stock and over 60% of all bonds in 1975.) Intangible property escapes taxation in most states through exemption, exclusion, and loopholes devised early in the twentieth century. Inclusion of this important form of wealth in the property tax base could add almost $8 billion in revenues to state and local governments.

The theory originally justifying the property tax was that an individual's amassed possessions were a suitable and sufficient indication of his or her ability to pay for services rendered by the government. Wealth at that time consisted mainly of real estate and livestock -- but there were also some types of intangible property, such as loans or licenses. Under the laws adopted in the early 19th century, all property, including intangible property, was assessed and taxed uniformly. Given the simple composition of wealth at this time, the property tax was particularly easy to administer and accept. With the growth of the corporate form of business and modern credit structures, however, the nature of private wealth changed greatly. Stocks, bonds and saving accounts grew in importance until they became worth far more than physical assets. But property tax administration changed little in response to the new economic realities. Tax administrators tended to rely on physical property rather than on intangible property.

ASSESSORS IGNORE PROBLEMS

Rather than grapple with the administrative problems associated with this new increasingly important form of wealth, assessors in many state capitals and city halls have simply ignored its existence. By the 1920's, most state and local governments either exempted paper wealth from the tax base, or made no effort to collect revenues due. Today, the property tax serves primarily as a levy on real estate, and thus in form it still closely resembles the institution developed in rural America. But the resemblance is in form only. The motivating spirit of the tax -- in terms of the ability-to-pay principle -- has been subverted by the exclusion of intangible types of wealth.

The taxation of intangible wealth along with real property would reduce inequities in the current property tax system and provide local governments with a new source of revenue. The most feasible method of implementing a tax on intangible wealth would be to have each state collect a tax on the income which individuals and fiduciaries (persons who manage the property of others) gain from passive investments in intangible property. By taxing the dividends, profits, or interest produced by intangible property -- with generous exemptions for

Possible Effects in Each State of Intangible Property Tax Proposal on Other Property Taxes (Millions of Dollars)

	Total General State & Local Revenues	Total Property Taxes (and % of Total Revenues)	Total Current Intangible Property Taxes (and % of Total Property Taxes)	Total Int. Prop. Tax Under Proposal (and % of Total Property Taxes, if tot. stays same)	Possible % Decrease in Other Property Taxes due to Proposal
Alabama	3,617	231 (6.4%)	12 (5.2%)	81 (35.1%)	29.9%
Alaska	975	92 (9.4%)	5 (5.4%)	10.5 (11.4%)	6.0%
Arizona	2,754	628 (22.8%)	36 (5.7%)	107 (17.0%)	11.3%
Arkansas	1,944	230 (11.8%)	14 (6.1%)	63 (27.4%)	21.3%
Calif.	33,723	9,570 (28.4%)	0 (0%)	1,103 (11.5%)	11.5%
Colorado	3,405	656 (18.7%)	39 (5.9%)	124 (18.9%)	13.0%
Conn.	3,787	1,316 (34.8%)	14 (1.1%)	220 (16.7%)	15.6%
Delaware	841	90 (10.7%)	1.5 (1.7%)	78 (86.7%)	85.0%
Florida	8,891	1,644 (18.5%)	166 (10.1%)	576 (35.1%)	24.9%
Georgia	5,587	968 (17.3%)	63 (6.5%)	149 (15.0%)	8.9%
Hawaii	1,503	157 (10.4%)	0 (0%)	39 (24.8%)	24.8%
Idaho	929	159 (17.1%)	9.5 (6.0%)	35 (22.3%)	16.3%
Illinois	14,522	3,789 (26.1%)	228 (6.0%)	587 (15.5%)	9.5%
Indiana	5,846	1,487 (25.4%)	29 (2.0%)	208 (14.0%)	12.0%
Iowa	3,559	912 (25.6%)	0 (0%)	151 (16.6%)	16.6%
Kansas	2,663	695 (26.1%)	10.5 (1.5%)	107 (15.4%)	13.9%
Kentucky	3,674	390 (10.6%)	17.5 (4.5%)	110 (18.8%)	11.3%
Louisiana	4,556	391 (8.6%)	23 (5.9%)	108 (27.6%)	21.7%
Maine	1,215	296 (24.4%)	0 (0%)	41 (13.9%)	13.9%
Maryland	5,680	1,054 (18.6%)	52 (4.9%)	167 (15.8%)	10.9%
Mass.	8,259	2,491 (30.2%)	125 (5.0%)	268 (10.8%)	5.8%
Michigan	12,510	3,232 (25.8%)	47 (1.5%)	290 (9.0%)	7.5%
Minnesota	5,693	1,099 (18.6%)	66 (6.0%)	181 (16.5%)	10.5%
Miss.	2,431	278 (11.6%)	16 (5.8%)	50 (18.1%)	12.3%
Missouri	4,835	1,060 (11.9%)	0 (0%)	229 (21.6%)	21.6%
Montana	1,019	275 (27.0%)	16 (5.8%)	[illegible] (14.9%)	[illegible]
Nebraska	1,842	525 ([illegible])	0 (0%)	76 (14.6%)	[illegible]
Nevada	923	182 (19.7%)	0 (0%)	37 (20.3%)	20.3%
New Hamp.	854	312 (36.5%)	6 (1.9%)	38 (11.5%)	[illegible]
New Jersey	9,576	*	11.5 (*)	[illegible]476 (*)	[illegible]
New Mexico	1,529	133 (8.7%)	0 (0%)	38 (28.6%)	[illegible]
New York	33,748	8,084 (24.0%)	0 (0%)	1,178 (13.8%)	[illegible]
N. Carolina	5,51[illegible]	777 (14.1%)	28 (3.6%)	159 (20.5%)	16.[illegible]
N. Dakota	909	148 (16.3%)	9 (6.1%)	28.5 (19.3%)	[illegible]
Ohio	11,327	2,633 (23.2%)	168 (6.4%)	403 (15.3%)	[illegible]
Oklahoma	2,973	384 (12.9%)	23 (6.0%)	140 (36.5%)	30.5%
Oregon	3,294	767 (23.3%)	0 (0%)	116 (15.1%)	15.1%
Penn.	13,949	2,337 (16.8%)	42 (1.8%)	354 (15.1%)	13.3%
Rhode Is.	1,163	302 (26.0%)	4.5 (1.5%)	34.5 (11.4%)	9.9%
S. Carolina	2,808	344 (12.3%)	0 (0%)	63 (18.3%)	[illegible]
S. Dakota	834	220 (26.4%)	13 (5.9%)	38 (17.3%)	11.4%
Tennessee	4,[illegible]25	592 (14.4%)	18.5 (3.1%)	109 (18.4%)	15.3%
Texas	12,838	2,835 (22.1%)	169 (6.0%)	510 (18.3%)	12.3%
Utah	1,385	221 (16.0%)	0 (0%)	33 (14.9%)	14.9%
Vermont	692	171 (24.7%)	0 (0%)	17 (9.9%)	9.9%
Virginia	5,584	946 (16.9%)	11 (1.2%)	134 (14.2%)	12.0%
Washington	5,007	986 (19.7%)	0 (0%)	146 (14.8%)	14.8%
W. Virginia	2,046	220 (10.8%)	13 (5.9%)	41.5 (18.9%)	13.0%
Wisconsin	6,137	1,511 (24.6%)	0 (0%)	211 (14.0%)	14.0%
Wyoming	628	128 (20.4%)	7.5 (5.9%)	26 (20.3%)	14.4%
U.S. Total	339,940	62,304 (18.3%)	1533 (2.5%)	9,473 (15.2%)	12.7%

* New Jersey has just instituted an income tax and reduced its property tax.

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"...the richest 1% of the population owned over 50% of all corporate stock..."

small amounts of income -- the difficulties once encountered in ad valorem taxation of intangible wealth would be avoided.

Institution of a low tax rate on the income from intangible property -- say 8% -- would yield about $8 billion in new revenues for state and local governments, which is almost $2 billion more than the amount given to state and local governments in fiscal year 1975 under the entire Federal revenue sharing program. This 8% tax on income would produce a lower tax burden upon intangible property than taxing the property itself under typical property tax schemes. By assessing the property at 50% of its actual value, and imposing a rate of 40 mills (.4%), the property tax on $50,000 worth of stocks would be $1,000. Assuming a 5% yield on the stocks, an 8% tax on the income received would produce a tax liability of only $200.

(Proponents of the intangible property tax use an 8% rate in positing their argument on the grounds it is an equitable one, despite its apparent steepness. They point out that lower bracket taxpayers, for lack of possession of intangible property, would not be subject to the tax at all. On the other hand, taxpayers in very high brackets would be able to deduct such a state tax from their Federal returns so that in all probability the actual levy against them could be as low as 4%.)

This tax on income from intangible property should not be confused with a general state income tax, nor should an income tax be viewed as an adequate substitute. The issue at stake here is the distinction currently made between tangible and intangible property, and the unreasonable preferantial treatment afforded intangible property by its exclusion from the property tax base. The implementation of a state income tax in addition to a conventional property tax would not eradicate this inequity in the treatment of these two classes of property. Rather, under an income tax real estate would be taxed twice -- once for its own value, and once for the income which it produces -- while intangible property is taxed only once. In fact, it would be no different from the present system where landlords are subject to both property taxes on their apartments, etc., and income taxes on the rental income received from these apartments.

A handful of states, including Colorado and Massachusetts, have attempted to eliminate this preferential treatment of intangible property by instituting a dual rate general income tax, which imposes a surtax upon gross income from some forms of intangible property.

DOUBLE TAXATION ARGUMENT

Critics of a tax on intangible property frequently allege that such a tax entails "double taxation." This argument states that since a share of stock stands for the physical assets of a corporation, these assets are already subject to property taxes, thus, to tax the stock is to tax the same property twice. The facts, however, hardly support this contention. Corporate stock stands for much more than just physical assets. Patents, good will, and other intangible assets also contribute to its value. Not all the physical assets of a corporation are subject to property taxation either. A study by Lester Snyder, Professor of Law at the University of Connecticut, shows that at most, only one-fifth of intangible property would be subject to "double taxation." Moreover, double taxation is so common in the American tax system, the charge itself should cause little concern.

Other charges against the intangible property tax prove similarly specious. Some object to such a tax because of administrative difficulties, claiming that intangible property is easily concealed from the tax collector. Although valid at one time, this argument has little merit in today's world of computers. State access to Federal income tax data on individual dividend and

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interest income should discourage major attempts at evasion. Another argument points to the potential plight of "widows and orphans," asserting that the tax would unfairly burden low income persons who depend upon small investments for subsistence. This argument is patently fallacious: the bulk of intangible property is held by the very wealthy, and an exemption to protect small taxpayers could be given. The only "widows and orphans" who would be affected by an intangible property tax would be wealthy ones.

PROJECTED YIELDS

The accompanying table presents estimates of current intangible property incomes by state, taken from statistics obtained from the Internal Revenue Service and the Congressional Joint Committee on Taxation. The tax base in the proposal which we suggest is composed of dividends, interest, capital gains, and royalty income received by individuals and fiduciaries. The total investment income subject to the suggested tax would be about $132 billion. Allowing a 10% reduction in this amount for low income exemptions that might be grant ed, and applying an 8% tax rate yields a total of $9.5 billion that states could hope to collect and distribute to local governments by taxing income from intangible property.

The point made by tax reformers is that the adoption of an intangible property tax would not be so much the imposition of another tax as it would be a new distribution of the burden. By easing the financial woes of local and state governments, the intangible tax, applied in the ideal sense, would impose restraints on raising rates on other types of taxes, chiefly those on real property.

(Rick Bauman contributed research to this report.)

(from NTA NEWS)

KENTUCKY COURT RULES ON SITUS OF PERSONAL BANK ACCOUNTS

The Kentucky Board of Tax Appeals has ruled that non-domestic bank accounts of a personal investment nature have situs within Kentucky for purposes of the property tax on intangibles.

The taxpayer lived in Kentucky but maintained a bank account in New York City. The bank there held and managed her securities. All of the taxpayer's personal expenses were paid out of a domestic account. The taxpayer was not engaged in a business of any kind. She argued that the non-domestic bank account had no situs within Kentucky, and was therefore exempt from the intangibles tax.

The board disagreed, saying that unless an out of state account of a Kentucky resident was maintained for purposes of a business, calling, or profession, its situs for the property tax was in Kentucky. (MADISON NATIONAL BANK OF RICHMOND v. DEPARTMENT OF REVENUE, decided September 17, 1976)

FROM: LOCAL SPENDING AND TAX LIMITS ACROSS THE COUNTRY (1976), by Public Expenditure Research Foundation, Inc.

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THE LIMITATION CONCEPT

Wisconsin local governments have completed their first budgeting season under the permanent tax and spending increase limitations incorporated in the state budget bill passed in July, 1975. Attention now is focused on the effect of the limits and what ceilings on spending and tax increases are in use in other states.

Limit Concept Not New

Information from various sources in other states indicates the policy of placing limits on local government property tax increases or spending is widespread. Forty-one states are indicated as having such a policy. The nine states without it are Connecticut, Hawaii, Maryland, Massachusetts, New Hampshire, Rhode Island, Tennessee, Vermont and Virginia.

States with limits have a variety of approaches, many affecting property tax amounts or spending. Some have constitutional limitations, some statutory, some both. Some limit only school expenditures. Generally, a state policy will cover most local government types. In some states the limits can be exceeded by local referendum, as in Wisconsin. In other cases it may be necessary to get approval from a state administrative agency, generally one which has a direct relationship to the revenue or expenditure picture. In some instances a state official may approve exceeding the limits, a state legislative body may authorize it, or the local governing body by a greater than simple majority vote may exceed the limitations.

A paper, entitled "Property Tax Reform", published by the International Association of Assessing Officers and The Fund for Public Policy Research for a July, 1973 seminar in Washington D.C. says that property tax limitations have been in use in this country for over a century with early limitations enacted "to place a cap on rising governmental expenditures."

"Fear of confiscatory property taxes during depression years caused the public to bring pressure to bear upon state legislators to put brakes on property tax rates. The depressions of 1873 and the 1930's had their impact on the use of limitations. Some of the present constitutional and statutory limitations were originally adopted at the time of the Panic of 1873. However, most of them were precipitated by the great depression of the 1930's." the Fund says.

Rhode Island and Nevada were reported by the Advisory Commission on Intergovernmental Relations as among the first states to adopt limitations, Rhode Island in 1870 and Nevada in 1895. Alabama and New York are reported to be the first to place specific limitations in their constitutions, in 1875 and 1884 respectively. The first state to adopt an overall limitation in its constitution was Oklahoma in 1907, followed by Ohio in 1911. No constitutional property tax limitations are reported in any of the states prior to the Civil War, but by the end of the 19th century 18 states had constitutional property tax limitations and six more states were added to the list between 1900 and 1925. At least 14 states adopted property tax limits in 1932 and 1933. Seven of these states placed the limitations in their constitutions. Nine provided for overall limits.

A majority of the limitations on property taxes are described as restricting rates, although some limit the amount of revenue to be collected. Chart I reviews common local government revenue and expenditure limitation concepts.

In this review, "levy" is used in the sense of property tax amount to be raised rather than as a rate which is applied to valuations to produce the tax amount. In some states "levy" takes on the meaning of a tax rate.

Trends in Recent Years

The oldest limit on property taxes has been a maximum tax rate either on overall taxes on property or applied to each of several local governments or even to several specific purposes for which a given local government may levy taxes. In more recent years there have been freezes on tax rates with revenue growth dependent on growth in valuation; increases in levies limited to fixed percentages or to growth as measured by specific indexes; and limits on increases in expenditures, such as for schools on a per pupil basis in fixed dollar amount or percentage.

The generally higher rate of increase in taxable valuations in recent years has tended to make property tax rate limitations less restrictive, especially if they were unrealistically high in the first place or if assessed valuation ratios were pushed up closer to full value with resulting increased leeway under the rate limits. Many jurisdictions do not assess at full value.

Some of the more recent developments in property tax limitations came with efforts to relieve property taxes -- extra money appropriated by state legislatures in aids or credits -- and a will to guarantee the moves actually resulted in property tax relief rather than more money spent. The impetus for the limitations came from the legislature in some states and from the executive department in others and no particular political party policy dominates the varied proposals and enactments.

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EXHIBIT I

AN OVERVIEW OF COMMON LIMITATION CONCEPTS IN LOCAL GOVERNMENT FINANCE

Property Valuation	Increases in valuation bring potential increases in tax collections, limited by maximums on tax rates or on levy increases in most states. Unless valuations taxed are assessed uniformly or are on full value they may be increased by reassessment and thus weaken the effect of the tax rate maximums.
times	
Tax Rate	Maximum tax rates may be set by constitution or statutes, for aggregate totals for several overlapping units of government, for individual units, or for individual purposes of governmental units. They may be at an arbitrary rate or a rate frozen from a prior year or years.
equals	
Property Tax Levy	In addition to being constrained by rate maximums, some tax levies have limitations on their percentage increase, set as a flat percent figure or related to an index or other trend measure. The limitation sometimes applies only to valuation of property previously assessed, with new construction and improvements bringing added increments.
plus	
Other Taxes and Revenues	At times a tax levy may be allowed to increase enough so that with other basic specified revenues a certain percentage aggregate increase potential may be reached.
equals	
Expenditure Budget	Limitations on increases in expenditures such as for school districts, perhaps on the basis of percentage or amount per pupil, are becoming more common, especially when aid or other money has been provided expressly for property tax relief.
Limitations conditioned by:	
Adjustments	The most common exclusion from limitation is principal and interest obligations of long-term debt. Others may cover losses of aid and other revenue declines. Increased leeway may be provided for new programs, more population, and numerous other factors.
Referendums	Referendums may be authorized whereby governing bodies present proposals to exceed limitations to the electorate, for one or more years, with a simple majority approval usually required.
Appeals	Sometimes appeals to state agencies or courts are provided for and may bring adjustments for specified factors or for relief in unusual circumstances concerning the limitations.

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II

CAUTION IN STATE - LOCAL EXPENDITURES

The assignment of this committee concerns only sources of revenue, not how these revenues are expended. However, an important word of caution is in order if all the benefits of tax reform suggested in this report are to be retained for more than a few short years.

From 1963 to 1973 total state and local expenditures increased more than threefold. During the same period the Gross State Product (GSP), a measure of total income generated in Maine, only a little more than doubled. Simultaneously, that part of total Gross State Product going to the State-local public sector has increased from slightly less than 11 percent of GSP to in excess of 16 percent. See Table 11-1, page 4.

A continued imbalance in the growth of the Gross State Product and State-local expenditures would result in a deterioration of our tax base as a source of sufficient revenues. Such an event could lead to a fiscal crisis with both our State and municipal governments being even further hampered in providing services.

The percentage of Maine personal income that is paid in State-local taxes was the seventh highest in the nation.(3) Although the benefits of the services provided by such an expansion are not to be underestimated, it is important to note that five years ago Maine's rank was only 27th.

Great prudence, then, should be exercised in further increasing the public sector's percentage of the Gross State Product. Rather, the primary focus should be on effectively allocating the limited tax resources Maine has and assuring the efficient expenditure of those tax dollars.

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3. Id.

TABLE II-1

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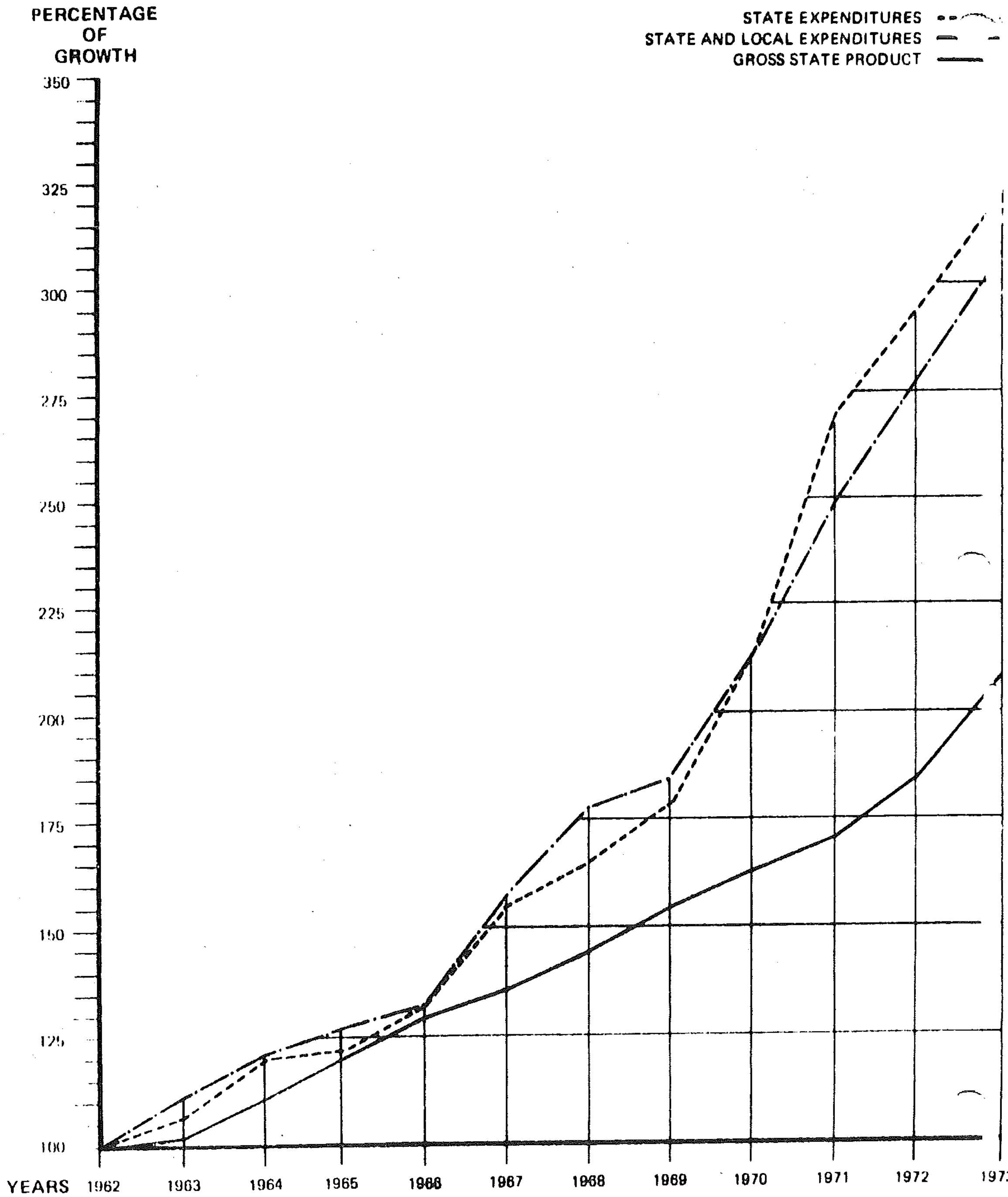
GROWTH OF EXPENDITURES FOR THE STATE OF MAINE AND THE STATE AND LOCAL GOVERNMENTS COMBINED COMPARED TO GROSS STATE PRODUCT [4]

Expenditure Caution /4



SOURCE: UNITED STATES DEPARTMENT OF COMMERCE, CENSUS OF GOVERNMENTS.

4. Federal Reserve Bank of Boston (1975).

Figures compiled by
Office of Legislative Assistants
at the request of
Rep. Roosevelt Susi (1975)

Maine's national ranking of 7th in terms of State and local taxes' percentage share of personal income might be explained not by saying that Maine's governmental expenditures are irresponsibly high but rather by realizing that Maine possesses approximately the 7th lowest per capita income in the nation (1) and that if the State is to provide even minimum public services, the per capita tax burden, in relation to income, must be comparatively high. High per capita tax burden does not always mean irresponsible State expenditures. Indeed, let us examine Maine educational spending. The current School Finance Act is often pointed to as an example of excessive State spending. Yet is it? Compared to the rest of the country, Maine is an example of educational frugality. Only six states spend less per pupil than we do. While the 1974-75 average per-pupil expenditures was $1,245, Maine spent only $936. (2) The School Finance Act may in the past have been inaccurate in its funding estimates; but this does not mean that its funding level is unreasonably high. Indeed, if anything, the counter-argument would be that Maine spends comparatively little for the education of its young.

This analysis is suitable in other areas of State services. Maine ranks approximately 13th from the bottom in unemployment benefit weekly payments. The average weekly payment is $65.19. Maine pays only $54.44.(3) Similarly, Maine is approximately 18th from the bottom in total AFDC payments per recipient. The average per recipient payment is $65.50. Maine pays only $50.75.(4)

In terms of all per capita government spending - education, highways, public welfare, health and hospitals, all other - it has been estimated that Maine in 1972 was 18th from the bottom when compared to all other states. The average per capita expenditure was $801 yet Maine spent only $684.(5)

Thus, the conclusion that is often drawn from our high per capita tax level - that taxes should be reduced - might be turned on its head. The counter argument would be as follows:

> Our per capita tax burden is high not because of "irresponsible" government expenditures but rather because we are a State of low per capita income and to attempt to supply even the necessities for school children, individuals unable to work, and unemployed, we must tax at least at the current level.

Footnotes

(1) Maine's per capita was estimated for 1973 to be $3,944. Maine consistently has the lowest per capita income in the New England area. _See_ U.S. Department of Commerce, _Statistical Abstract of the U.S., 1974_, 380 (1975).

(2) National Education Association, _A Statistical Profile: Education in the States, 1974-75_ (1975).

(3) U.S. Department of Labor, _Unemployment Insurance Statistics_, 3 (January, 1975).

(4) U.S. Department of Health, Education and Welfare, _Public Assistance Statistics, February, 1975_, 9 (1975).

(5) U.S. Department of Commerce, _Statistical Abstract of the U.S._, 1974, 225 (1975).

3.203 AUTHORIZATION FOR A LOCAL INCOME TAX[1]

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In the aggregate, local governments of all sizes and types raised $2.5-billion from local income taxes, or approximately 4.5 percent of total tax revenues in 1974. Most of the local income tax revenue was generated by cities ($2-billion), with county governments accounting for an additional $200-million. Among the nation's 48 largest cities (excluding Washington, D.C.), 13 utilize the local income tax and raised $1.4-billion in 1974 from this revenue source. Relative reliance on this tax source ranged from a low of 14.2 percent of total taxes in Baltimore to 78.2 percent in Columbus, Ohio.

Although local income taxes are imposed by 4,200 local jurisdiction in ten states, widespread coverage of the population by the local income tax is restricted to three states — Maryland, Ohio, and Pennsylvania. Moreover, the great bulk of the 4,000 plus jurisdictions are located in Ohio (335 municipalities) and Pennsylvania (3,765 municipalities, townships, and school systems). As the large number of local jurisdictions in both Ohio and Pennsylvania indicates, the local income tax is used by some of the very smallest jurisdictions as well as some of the largest cities. Despite the fact that most of the local governments using the income tax are "small," there is a "big city" dimension to this tax. Following Philadelphia (1939), Toledo was the next big city (over 50,000 population) to levy a local income tax (1946), one of 11 such cities to adopt the tax between 1946 and 1959. An additional 11 large cities imposed local income taxes during the decade of the 1950s. The local income tax movement picked up additional momentum during the 1960s with 26 "big city" adoptions. In the 1970s, only Birmingham, Alabama, among cities of 50,000 or more population, has adopted a local income tax though 34 Indiana counties adopted the tax in 1973.

In its 1974 report, *Local Revenue Diversification,* the Advisory Commission on Intergovernmental Relations recommended that state governments permit counties and larger cities (25,000 and over) to levy local income and sales taxes provided certain safeguards are met: (a) collection by a state agency — as a supplement to the state income tax in those states (40) using that tax; (b) restriction to counties and larger cities or use by counties with sharing among its constituent municipalities; (c) utilization in such a way as not to widen interlocal fiscal disparities; and (d) arrangements for sharing taxes on earned income by non-residents where both jurisdiction of residence and of employment levy the tax.

The suggested legislation that follows includes the foregoing safeguards. *Section 1* specifies the purpose of the act, and *Section 2* sets forth definitions used. *Section 3* authorizes all counties and all cities of 25,000 or over to impose a local income tax of a specified percent of state income tax liability. To avoid layering, if the county desires to use the tax it must do so on a countywide basis and share the revenue with all its municipalities. If the county does not levy the tax, cities of 25,000 or more are empowered to enact it subject to subsequent preemption by the county.

Section 4 provides for 120 day advance notice to the state administering agency for imposition or repeal of the tax. *Section 5* provides for state administration for deducting administrative costs from the proceeds, and determination of tax liability as between resident and non-resident local jurisdictions.

Section 6 deals with reciprocal credits for taxes paid another local government on income subject to the tax authorized by the act.

Section 7 sets forth the procedure for distribution of the proceeds to the appropriate local governments.

The suggested legislation is based in part on Maryland statutes and on Indiana, P.L. 50, *Laws of 1973.*

[1]Derived from: Advisory Commission on Intergovernmental Relations, *Local Revenue Diversification: Income, Sales Taxes and User Charges,* Report A-47 (Washington, D.C.: U.S. Government Printing Office, October, 1974).

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[UNIFORM LOCAL INCOME TAX LAW]

(Be it enacted, etc.)

SECTION 1. *Purpose.* It is the purpose of this act to authorize counties and certain cities of the state to levy a local income tax under certain conditions.

SECTION 2. *Definitions.*

(a) An "eligible city" is a city of at least 25,000 population as of the effective date of the tax.

(b) A "non-resident" is anyone who is not a resident.

(c) "Persons." [*To be defined in conformity with the state income tax code.*]

(d) A "resident" of a county or eligible city is an individual who is domiciled in that jurisdiction unless he maintains no permanent place of abode in the county or city and does maintain a permanent place of abode elsewhere and spends in the aggregate not more than [30] days of the taxable year in the city or county; or who is not domiciled in the county or city but maintains a permanent place of abode in the county or city and spends in the aggregate more than [183] days of the taxable year in the county or city.

(e) "Taxable year." [*To be defined in conformity with the state income tax code.*]

SECTION 3. *Authorization.*

(a) Any county is authorized to impose a local income tax on its residents and on all other persons earning or receiving income from economic activities carried out in the county or eligible city at a rate not less than [ ] percent of the state income tax liability nor more than [ ] percent of the state income tax liability, provided that the rate adopted is evenly divisible by five. The county shall have the right to preempt a city income tax by adopting a countywide income tax provided that the revenues so raised by the county are shared with all cities [of at least [ ] population in the county].[1]

(b) The share for all cities shall be equal to the fraction which total tax revenue raised by all cities within the county represents of the total tax revenue raised by the county and its cities. The share for each city shall be determined by the ratio of the city population multiplied by the fraction represented by the ratio of the county equalized, full value assessment to the city equalized, full value assessment.[2] If the county does not adopt the tax, the authority to enact local income taxes is extended to all eligible cities within the county subject to the conditions set forth in subsection (a) above and to subsequent

[1] If the state does not impose an income tax, counties and cities could be authorized to apply the local tax rates to the Federal income tax base, thereby maximizing taxpayer convenience. Also, for those states not imposing an income tax, a section requiring employer withholding of local income taxes may need to be added to the legislation. Withholding provisions are contained in the ACIR suggested legislation, *State Personal Income Tax Bill.*

[2] If equalized property tax assessment data are not readily available some other measure of fiscal ability such as income, tax effort, or fiscal capacity might be used.

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preemption by the county.[1]

SECTION 4. *Certification and Withdrawal of the Local Income Tax.*

(a) Any county or eligible city enacting an income tax pursuant to this act, shall certify at least [120] days in advance to the [*state tax commissioner*] the effective date of the ordinance imposing an income tax, the rate of the tax for the entire tax year, and the date when the enactment becomes effective.

(b) A county or eligible city imposing an income tax within the provisions of this act may repeal its income tax only after first giving at least [120] days notice of the contemplated repeal of its income tax to the [*state tax commissioner*]. The withdrawal shall be effective from and after the first day of the next calendar year.

SECTION 5. *State Administration of the Local Income Tax.* The income tax authorized under the provisions of this act in any county or eligible city shall be administered by the [*state tax commissioner*].[2]

(a) Revenues collected under local income taxes shall be accounted for separately and shall be paid into a separate fund to be distributed to the county and eligible cities imposing such taxes after deducting an amount to cover expenditures incurred by the [*state tax commissioner*] in administering the local income taxes. The rules and regulations promulgated in accordance with the state income tax shall apply to the local income taxes except when, in the judgment of the [*state tax commissioner*], such rules would be inconsistent or not feasible of proper administration. The [*state tax commissioner*] is authorized to make any refunds to taxpayers pursuant to this act.

(b) In the case of the withholding of local income taxes from wages of a non-resident, the local income tax shall be credited solely to the place of employment provided such jurisdiction imposes a local income tax and the place of residence in this state does not impose a local income tax. If both the jurisdiction of employment and of residence impose local income taxes, an amount equal to one-half of the tax a non-resident would owe if such person worked in his jurisdiction of residence in this state shall be credited by the [*state tax commissioner*] to the non-resident's place of residence in this state.

SECTION 6. *Credit for Income Tax Paid to a Political Subdivision of Another State.* A resident individual shall be allowed a credit against the tax otherwise due under this act for the amount of any income tax required to be paid by him during the taxable year to a political subdivision of another state of the United States on income derived from sources therein and which is also subject to tax

[1]Intercounty equalization of revenues can be dealt with by state grant programs designed to bring all below average county income tax yields *per capita* (adjusted for differences in rates) up to the average for the state.

[2]If the state does not impose an income tax, the state (central finance agency, comptroller, or department of local affairs) might be selected to administer the tax.

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under this act.

SECTION 7. *Distribution of Collection Among Local Governments.* All sums collected pursuant to this act shall be credited to a special local income tax fund which is hereby established in the [*state treasury*]. After deducting the amount of refunds made, a reserve for expected or anticipated refunds, and the costs of administering the tax, the remaining sums shall be returned by [*appropriate state official*] to the county or eligible city of origin by the [15th day of the month following the month during which such sums were collected].

SECTION 8. *Separability.* [*Insert separability clause.*]

SECTION 9. *Effective Date.* [*Insert effective date.*]

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ONE HUNDRED AND EIGHTH LEGISLATURE

Legislative Document **No. 1657**

H. P. 1403 House of Representatives, April 13, 1977

On motion of Mr. Carey of Waterville, referred to the Committee on Taxation. Sent up for concurrence and ordered printed.

EDWIN H. PERT, Clerk

Presented by Mr. Greenlaw of Stonington.

STATE OF MAINE

IN THE YEAR OF OUR LORD NINETEEN HUNDRED SEVENTY-SEVEN

AN ACT to Permit Municipalities to Levy and Collect Service Charges for Certain Municipal Services from Tax Exempt Residential Property Used to Provide Rental Income.

Be it enacted by the People of the State of Maine, as follows:

36 MRSA § 652, sub-§ 1, ¶ L is enacted to read:

L. Service charges.

(1) The owners of certain institutional and organizational real property, which is otherwise exempt from state or municipal taxation, may be subject to service charges when these charges are calculated according to the actual cost of providing municipal services to that real property and to the persons who use that property. These services shall include, without limitation:

(a) Fire protection;

(b) Police protection;

(c) Road maintenance and construction, traffic control, snow and ice removal;

(d) Water and sewer service;

(e) Sanitation services; and

(f) Any services other than education and welfare.

(2) The establishment of service charges is not mandatory, but rather is at the discretion of the municipality in which the exempt property is

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located. The municipal legislative body shall determine those institutions and organizations on which service charges are to be levied by charging for services on any or all of the following classifications of tax exempt real property:

(a) Residential properties currently exempt from property taxation, yet used to provide rental income.

If a municipality levies service charges in any of the classifications of this subparagraph, that municipality shall levy these service charges to all institutions and organizations owning property in that classification.

(3) With respect to the determination of service charges, appeals shall be made in accordance with an appeals process to be provided for by municipal ordinance.

(4) The collection of unpaid service charges shall be carried out in the same manner as provided in Title 38, section 1208.

(5) Municipalities shall use the revenues accrued from service charges to fund, as much as possible, the costs of those services.

(6) The total service charges levied by a municipality on any institution and organization under this section shall not exceed 2% of the gross annual revenues of the organization. To qualify for this limitation the institution or organization shall file with the municipality an audit of the revenues of the organization for the year immediately prior to the year which the service charge is levied. The municipal officers shall abate the service charge amount that is in excess of 2% of the gross annual revenues.

(7) Municipalities shall adopt any necessary ordinances to carry out the provisions of this paragraph regarding service charges.

STATEMENT OF FACT

The purpose of this bill is to give municipalities the option of establishing service charges for tax exempt residential property used to provide rental income.

APPENDIX B

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STATE OF MAINE

Inter-Departmental Memorandum

Date July 16, 1975

To R. L. Halperin, State Tax Assessor — Dept. Bureau of Taxation

From Norman P. Ledew, Director — Dept. Property Tax Division

Subject Taxation Committee - Subject for discussion - Public Utilities

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The Taxation of Public Utilities in Maine is inconsistent. Telephone and Telegraph companies are taxed by the State on an excise tax basis except for land and buildings which are subject to the property tax by the municipality where they are located. Railroad companies are subject to an excise tax by the State except for buildings and land and fixtures located outside the right of way which are subject to the property tax by the municipality within which they are located. Electric power companies on the other hand are totally subject to the local property tax system.

As each of these systems service the entire State and have their rate structure and therefor revenue controlled by the Public Utilities Commission, it would seem that the taxation of all such companies should be uniform insofar as property taxation is concerned.

The present method of taxation by individual municipalities leaves much to be desired in the way of equity. Although the Bureau has made several attempts to obtain current values from the major companies during the past five years, there has been a reluctance on their part to furnish current data needed by the Bureau for valuation in the unorganized territory as well as in assisting municipal assessors. Some of this reluctance is engendered by the fear on the part of the companies as to the use of such information at the local level.

The use of antiquated values for State valuation purposes may well reflect equity as compared to company property in one municipality to another, but certainly does not when comparing company property with other property in a municipality.

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As company property values are an important ingredient of State valuation in many municipalities, the lack of current data is a detriment to obtaining an equalized valuation. The valuations of telephone or railroad companies, except for land and building, are not now part of the State valuation or municipal valuations. There appears to be three options available.

1. Continue the present situation in regards to electric companies and develop current values for municipal assessment and the State valuation.

2. Adopt State assessment of the electric companies, removing such valuations from the State valuation computation. Revenue to be distributed to municipalities through a formula such as State-Municipal Revenue Sharing.

3. Impose an excise tax on electric companies such as is now in effect with railroad and telephone companies with revenue distributed to the municipalities.

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Public Utility Excise Tax

§ 1. Definitions

(a) Taxpayer means any corporation, association or person subject to taxation under this chapter.

(b) Electric Generating Facilities means all facilities located in Maine which generate electricity for use in Maine, and are certified by the Public Utilities Commission, except those facilities owned by a public municipal corporation of this State and located within the corporate limits and confines of such public municipal corporation.

(c) Gross Receipts means all receipts of a taxpayer from the sale of electricity produced by an electric generating facility in the preceding calendar year except (a) receipts from sales to facilities owned by a public municipal corporation of this State and located within the corporate limits and confines of the public municipal corporation, and (b) receipts from sales in interstate commerce which under the Constitution and statutes of the United States may not be the subject of taxation by this State.

§ 2. Exemption from property tax. The excise tax collected under this chapter shall be in lieu of all property taxes upon the real and personal property of electric generating facilities.

§ 3. A. 36 MRSA § 656(1)(H) is enacted to read:

The following real estate is exempt from taxation: All electric generating facilities which are subject to taxation pursuant to the Public Utilities Excise Tax.

B. 36 MRSA § 655(1)P is enacted to read:

The following personal property is exempt from taxation: All machinery and equipment of electric generating facilities which are subject to taxation pursuant to the Public Utilities Excise Tax.

§ 4. Imposition and rate of tax. An annual excise tax computed at the rate of ____% shall be imposed upon the gross receipts of electric generating facilities for the preceding calendar year.

§ 5. Taxpayer's returns.

A. All taxpayers shall return to the State Tax Assessor, prior to ___________ 1st, (a) a statement, signed by its treasurer or its chief accounting officer, of the gross receipts of all its electric generating facilities itemized by municipality, and (b) the payment of its tax computed in accordance with sec. 4.

B. The State Tax Assessor or his duly authorized agent shall have access to the books of any taxpayer, to ascertain if the required returns are correctly made. Any taxpayer refusing or neglecting to make the returns required by law or to exhibit to the said Tax Assessor or to his duly authorized agent, its or his books for the purpose aforesaid, or making returns which the president, clerk, treasurer or other person certifying such returns knows to be false shall forfeit not less than $1,000 nor more than $10,000, to be recovered by indictment or by a civil action.

C. Any taxpayer who understates its reported gross receipts by more than 20% shall be liable to a penalty of 25% of such understated liability. The State Tax Assessor may enforce this penalty by a civil action.

D. If the State Tax Assessor determines that a taxpayer's returns are incorrect, he may either assess an additional tax or refund the amount of any overpayment.

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E. If any taxpayer fails to make the returns required by section 5A, the State Tax Assessor shall make an assessment of tax upon such taxpayer.

F. Any taxpayer may apply for an abatement of its tax within 30 days after the tax is due or within 30 days after the State Tax Assessor has taken action pursuant to subsection D anJ E.

§ 6. Lien

The excise tax shall constitute a lien on the property of the taxpayer. The lien shall take precedence over all other liens.

§ 7. Penalty and Interest

Taxes shall become delinquent if unpaid after the date on which payment is due. Interest of ____% per year shall be charged on delinquent payments beginning on the date on which the payment becomes delinquent. A penalty of ____% per year shall be charged on delinquent installments beginning 30 days after the payment becomes delinquent.

§ 8. Apportionment between State and Municipalities

The municipalities in which electric generating facilities subject to taxation under this act are located shall be allocated ________ percent of the revenues collected by the excise tax. The balance of revenues shall be allocated to the state and deposited in the general fund.

§ 9. Distribution to Particular Municipalities

Each municipality in which an electric generating facility subject to taxation under this act is located shall receive a portion of the revenues allocated to all municipalities pursuant to § 8 of this act. A municipality's portion shall be arrived at by multiplying the total municipal allocation by a fraction computed as follows:

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Denominator: Sum of kilowatt generating capacity of all electric generating facilities subject to taxation under this act.

Numerator: Sum of kilowatt generating capacity of all electric generating facilities subject to taxation under this act located within a particular municipality.

beings have ever created." But they also show the candidate speaking for himself, and Carter's radio and television advertising is the most explicit, direct and issue oriented of any candidate's in either party. As an example, here is Carter explaining his ideas on money management in a 60-second spot: "With a new budgeting technique called zero based budgeting, we eliminated [in the state government in Georgia] all the old obsolescent programs, put into effect long range goals and planning and cut administrative costs more than 50 percent, and shifted that money and that service toward giving better government services to our people. Zero based budgeting is the best management tool I have ever seen. You require every program that spends the taxpayer's money to rejustify itself annually and you have an automatic reassessment of priorities so you phase out the old programs automatically and you just have the new programs financed every time."

Some have taken issue with the claims made by Jimmy Carter about the gains made during his administration in Georgia and the feasibility of his management concepts. But it has been a long time since a presidential candidate attempted to advance ideas of this complexity in such specific terms on advertising time purchased with his own campaign dollars.

That's what the candidates look and sound like after they've been packaged by the ad agencies. The media campaign sets the tone of the contest, and its content. I'll leave it to you to decide (to paraphrase former FCC Commissioner Nicholas Johnson) whether they are molesting the minds of America's voters.

Ken Bode

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A New Route to Reform

Taxing Consumption

by Martin S. Feldstein

Despite the continual efforts of tax reformers for more than two decades, our income tax law still permits some of those who enjoy the most affluent consumption to pay little or no tax. Through capital gains, tax exempt municipal bond interest and "paper" losses on tax shelter activities, the rich are able to reduce their taxable income and increase their personal consumption. And the inequities of our current tax system will continue until the goal of tax reform is redefined.

A growing number of economists now favor substituting a progressive tax on personal consumption for the current income tax. Although such a change would have little effect on taxes paid by most families, it would force all of those who enjoy a high standard of consumption to pay their fair share of taxes. It would also eliminate many anomalies in the current tax law while encouraging certain forms of saving. Moreover, administering a progressive consumption tax such as the one described below would be easier than operating our current income tax. While the switch to tax consumption would not be without problems, it is time to refocus the energies of tax reform on this new goal.

When the basic structure of our current income tax law was designed more than 60 years ago, it was intended to raise a very limited amount of revenue. The maximum rate of tax was seven percent and was applicable only to very high incomes. With such low rates there was little incentive to rearrange income in order to reduce taxes and little scope for serious inequities. Even during the decade before World War II only about four percent of families paid any income tax at all and the median ~~tax rate for these~~ high income families was less than five percent! Today nearly 500,000 taxpayers pay marginal tax rates of 50 percent or more. These high rates are incentive enough for people to manipulate economic activities in order to substitute untaxed income for taxed income and thus give rise to inequities.

The basic problems with the current tax system arise in the taxation of capital income and in the treatment of accumulation. The special treatment of capital gains is the most important way in which tax law reduces the obligation of the wealthy. When stocks or other assets are sold, the gain is taxed at half of the usual tax rate or

Martin S. Feldstein is professor of economics at Harvard.

less. Anyone who finances his consumption primarily by selling assets, as many of the rich do, will pay much lower taxes than someone who finances that same standard of living out of ordinary income. The low rate of tax on capital gains is only part of the favorable treatment of capital gains. Because no tax is due on an appreciating stock or other asset until it is sold, the wealthy pay no tax on this form of saving. In contrast, those whose income consists only of wages or salary save out of after-tax dollars (except for limited employer pension contributions) and pay tax on each year's interest. The deferral of the tax on capital gains until the asset is sold substantially raises the net rate of return that asset holders can earn. It has been estimated that deferral reduces the effective tax rate on capital gains to less than 10 percent.

The tax wise investor can do even better by borrowing to finance his consumption while holding appreciating assets with which ultimately to repay the debt. The interest that he pays is a tax deduction that immediately reduces the tax that he must pay on his other income. In contrast, the taxes on his capital gains are due only when the assets are sold. Moreover, no tax is due on any gain if the individual dies before selling the asset. If his estate sells the asset and pays his debt, the individual and his estate completely escape all tax on the consumption that he enjoyed.

An example will show how the powerful subsidy of leveraged investment works in practice. Consider a man with a $50,000 salary, common stock worth $500,000 and a bank loan of $200,000 secured by the stock. The stock will produce dividends of about $20,000, approximately equal to the interest on the loan; as a result, there is no tax on the dividends. Although the change in share prices varies from year to year, the average experience of the past 25 years suggests a gain of 5 percent or $25,000 on his $500,000 of stock. No tax is due on this gain unless the shares are sold. By borrowing an additional $25,000 from the bank, the individual can consume his gains without any increase in tax.

Real estate investments are another important device for financing consumption without paying tax. In a typical real estate investment, the accounting depreciation allows the investor to receive his net rental income untaxed and to offset some of the tax liability on his other income. This accounting depreciation is allowed as a tax deduction even if the property is actually increasing in value. When and if the property is sold, the capital gain is taxed at a favorable low rate. And the investor can avoid even this tax by refinancing his mortgage instead of selling his property.

This combination of borrowing, artificial accounting losses and untaxed capital appreciation is the common feature of tax shelters in such diverse activities as oil drilling, cattle feeding and low-income housing. In every case, the investor seeks to reduce his total tax bill and increase his own consumption.

Why have obviously unfair features of our tax system been allowed to persist? Certainly not because tax reformers have failed to make Congress aware of them. Inequities survive in part because it is difficult, if not impossible, to eliminate them within the framework of our current income tax without at the same time creating new and equally serious problems. For example, the low rate of tax on capital gains is retained because it provides an incentive to socially productive portfolio investment, because it is at least a crude adjustment for inflation, and because the proceeds of such sales are generally reinvested. The deferred taxation on capital gains until assets are sold is required by the practical difficulty of revaluing all capital assets each year. The abuses that result from borrowing are difficult to stop in our tax system because borrowing does not give rise to income even when it finances consumption. Although piecemeal solutions for some of the current problems could be developed within the existing tax system, doing so would only complicate tax laws even further and might introduce new sources of inequity.

The proper remedy lies in a more general reform of the tax system to base tax liabilities directly on consumption so that the intractable problems of measuring income are effectively avoided. Under a consumption tax there would also be no rationale for special tax rates for capital gains, for the exemption of consumption financed by municipal bond interest, or for any of the myriad of other provisions that currently favor wealthy taxpayers.

The idea that everyone's tax should depend on how much he consumes, regardless of how that consumption is financed, appeals strongly to our sense of fairness. Although this principle has not been fully incorporated into our tax law, it is honored in part by the special ~~treatment of pensions: current~~ income that is contributed to a pension plan by an employer is specifically excluded from taxable income. By exempting pension saving, ~~and what is saved~~ when the value of assets increases, our tax law goes part way toward the goal of taxing only consumption. But the system exempts only part of the savings from wage and salary income and fails to tax the consumption financed by borrowing and capital appreciation.

A progressive consumption tax would be surprisingly easy to implement. To calculate "taxable consumption," the taxpayer would add all of his receipts and subtract his additions to saving and investment. In addition, his business expenses and certain personal deductions that are not regarded as ordinary consumption (like the current deductions for casualty losses and medical expenses) would be subtracted. For households that currently use the standard deduction and the simplified "short form," no change would be required. Wealthy households would however be forced to pay tax on the receipts from borrowing and from the sale of assets if they are used to finance consumption. Only when such finds are reinvested would they be subtracted in calculating taxable consumption. Moreover, the accounting losses like accelerated depreciation and depletion that currently reduce taxable income but not the cash flow available for consumption would not be deductible.

The switch to such a cash-flow consumption tax would thus eliminate the fundamental inequity in our current tax system. By basing taxes on consumption, everyone who enjoys a high standard of living would pay a correspondingly high tax. Any two taxpayers with the same spending on personal consumption would pay the same tax, regardless of the way in which that income was financed.

Economists have long favored the consumption tax for another reason as well. Our current income tax lowers the rate of return on savings and thus distorts everyone's choice between consuming today and saving for a higher level of consumption in the future. Because the income tax takes away some of the potential reward for saving, everyone is made worse off. The consumption tax would eliminate this wasteful distortion.

A switch to a consumption tax is likely to increase the nation's rate of saving. With more saving available, our rate of investment would rise and our capital stock would grow larger. This increase in the amount of capital per worker would increase productivity and therefore raise real wage rates. Workers as a whole would therefore gain indirectly as well as directly from this tax reform.

Inflation increases the attractiveness of the consumption tax. Inflation is the source of a great many problems and inequities in our current income tax because inflation makes it difficult to measure the real income earned on savings and investments. Consider for example what happens to the interest on savings deposits. Interest rates have risen substantially in the past decade as a result of the accelerating rate of inflation. The higher interest rate compensates depositors for the loss in purchasing power of the money they have on deposit. However, the compensation is not complete because part of this inflation premium is taxed away. Even the lucky saver who has been able to earn an interest rate equal to the seven percent average inflation during the past five years will have seen the real value of his savings decline because he has paid a tax even though he has had no real income. The effect of inflation on the taxation of capital gains and business profits is even more complex. The relation between taxes and real income (*i.e.*, income after adjusting for the effects of inflation on money assets and liabilities) differs greatly from what Congress intended when it wrote the tax law. Individuals with the same real income can pay vastly different income taxes in an inflationary economy. None of the ambiguity of evaluating income carries over to measuring consumption. The consumption tax thus eliminates the problems and inequities that inflation brings to our current income tax.

A consumption tax would also be a more effective instrument of macro-economic policy than our current income tax. A temporary cut in the consumption tax would stimulate demand in two ways. A fall in tax collections increases disposable income and thus increases consumption. (This is the mechanism by which our current income tax cuts are intended to operate.) In addition, a temporary cut in the rate of consumption tax would lower the net cost of current purchases relative to future purchases. This would tend to speed up the purchase of consumer durables, thus helping the consumption goods industries that are usually hardest hit in a recession and that income tax cuts are least effective in helping.

The consumption tax has been rapidly gaining supporters among economists and tax experts. But there are still some who fear a consumption tax would be insufficiently progressive or would fail to provide an adequate check on the accumulation and enjoyment of wealth. I think these fears are not justified. Consider first the concern that the consumption tax will not be adequately progressive. This view reflects in part a confusion between a progressive consumption tax collected from individuals and a proportional excise tax on consumer goods. Historically, the only consumption taxes in the United States have been proportional excise taxes; the value added tax now used as a major source of revenue by most European countries is also an excise tax. But the individual consumption tax can be every bit as progressive as the current income tax and even more progressive.

Changing the tax base from the current taxable income to cash flow net of savings without changing tax rates would affect individual tax liabilities in two countervailing ways. By closing many of the current loopholes, the switch to a consumption tax would increase tax liabilities. The deduction for saving would however lower taxes. Both effects would be relatively larger at high incomes than at low incomes. The current progressivity could probably be maintained with relatively small changes in the current tax rates at each income level.

The consumption tax can do more than match the *average* rate of progressivity of the current income tax. As I emphasized above, our current tax law allows some of those with the highest standard of living to pay little or no tax. In contrast, a progressive consumption tax would eliminate these opportunities and force those with high levels of personal consumption to pay a correspondingly high personal tax.

The consumption tax would also be an implicit tax on current wealth. Nicholas Kaldor, a distinguished British economist and a leading economic adviser of the Labour party, has urged Britain to adopt a consumption tax as an effective way of taxing those who support a high lifestyle on the basis of inherited wealth. Wealthy taxpayers in America who finance extravagant spending by capital gains on accumulated wealth, by investing in tax exempt municipal bonds, by borrowing against their wealth, or by investments that yield tax-sheltered income would find that these tax privileges now conferred by wealth would be eliminated by a consumption tax.

Some critics of the consumption tax dislike the deduction of savings because it allows individuals to accumulate wealth more easily. But why is this a problem? The accumulated wealth will be taxed whenever it is used to finance personal consumption. Moreover, if it is given or bequeathed to others, it will also be subject to the gift and estate taxes and then, when it is spent, to a further tax on consumption. I find it difficult to understand why the critics are worried more about the accumulation of new wealth within individual lifetimes under a consumption tax than about the untaxed consumption supported by inherited wealth under the current income tax.

The concern about the accumulation of substantial wealth reflects the fact that money confers power in our society. This concern with the accumulation of power is no doubt the primary reason why many supporters of the consumption tax also favor introducing a progressive tax on wealth above a very high exclusion like $500,000 or one million dollars. The current income tax attempts to tax wealth indirectly by taxing the income from wealth, but it is clearly a very poor substitute for a tax aimed at the power conveyed by wealth: the tax rate on capital income depends on the amount of wage and salary income, there is no exclusion to focus the tax on the power conveyed by large fortunes, and there are ample opportunities to avoid the tax. Indeed, many of the devices for reducing income tax liabilities are available only to those with sufficient wealth! By contrast, the consumption tax effectively reduces the real value of wealth by requiring that a tax be paid whenever the wealth is spent. If a more direct limit on the accumulation and transmission of large fortunes is desired, the solution lies not in the income tax but in the reform of the estate and gift taxes and in the introduction of a tax on wealth.

The switch to a consumption tax would not eliminate all of the problems of our current law. An ambiguous line between personal consumption and business expense—entertainment, travel, the company car, etc.—will be the same source of abuse under the consumption tax as it is under the income tax. A subsidy to homeowners is also likely to continue under a consumption tax. The process of transition from the income tax to the consumption tax would involve additional difficulties. But it would be worth grappling with them to achieve the advantages of a consumption tax. The redirection of tax reform will require widespread public and political debate and careful legal analysis. The universal discontent with our current tax law should provide the necessary impetus. An election year is a good time to begin.

Ford's Failure to Follow Through on Nixon's Initiative

Who Lost Our China Policy?

by Thomas L. Hughes

In a recent issue of the *Ladies Home Journal*, ex-President Nixon complained "we have very little leadership in our country today." The groundswell is still imperceptible for his return to Washington, but he will undoubtedly bask in the fervor of his return to Peking. Indeed Mao's invitation and Nixon's acceptance both stand as not-so-subtle accusations of faulty follow-through on the high drama of the first visit of four years ago. With Mao and Nixon practicing togetherness again in the Forbidden City, the man who for a generation curdled American politics with his cries of "Who lost China?" now has a more legitimate question to ask. This time he can address it to his own two appointees, President Ford and Secretary Kissinger, and the question is: "Who lost our China policy?"

Four years ago in February, 1972, Peking was the scene of Nixon's and Kissinger's greatest triumph. It

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Thomas L. Hughes is president of the Carnegie Endowment for International Peace and a former Assistant Secretary of State. His views here do not necessarily represent those of the Carnegie Endowment.

Produced by John Joseph, State Planning
Office, as a staff memo for the 1976
Governor's Tax Task Force

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Tax Base Sharing

The Concept

The tax base sharing concept is essentially a simple one capable of being understood by people who are not versed in the intracacies of fiscal policy but yet pay taxes. The first principle of the tax base sharing plan is that tax base and not tax revenue is shared. One form of tax base sharing might provide every municipality in the state, based on some agreed upon distribution formula, 40% of the net growth of the non-residential tax base in the entire state.

This 40% of new growth in non-residential valuation would be taxed at the average municipal tax rate, put into a "growth pool", and distributed to other localities according to the acceptable formula. The 60% new growth in valuation remaining would be taxed at the local tax rate which will be determined by the community in which the property is located.

The growth pool does not accumulate; all monies paid in a given fiscal year are redistributed exhaustively to participating jurisdictions. The redistribution formula, as mentioned above, can take any agreed upon form. One alternative in Maine is to adopt the present general state revenue sharing formula with a factor to phase out the pay in.

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Tax Base Sharing
A.I.P. Journal
March 75
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$$\text{Towns Allocation} = \overbrace{\left[pL_i \cdot C - .013\, V_i \right]}^{A} + \overbrace{\frac{\frac{Pi \times Ti}{Vi}}{\frac{P \times T}{V}} \cdot \left[\begin{array}{c} \text{Growth} \\ \text{Pool} \end{array} \right] \cdot .0247}^{B}$$

Growth Pool = 40% of New Growth in Commercial, Industrial, Nonresident valuation in all communities

PL_i = Number of Pupils in Town i

V_i = Valuation in Town i

C = Education cost per pupil

P_i = Town Population

T_i = Total Property Taxes in the Town

P = State Population

T = State Property Taxes

V = State Property Valuation

A is the present allocation formula - towns pay in if the formula yields a negative number, i.e., if they collect more than their education costs with 13 mills assessed on their state valuation.

B is each town's allocation based upon applying the present state revenue sharing formula to the "growth pool" and assessing that "growth pool" and the average municipal tax rate which is presently .0247 mills.

BENIFITS OF THE TAX BASE SHARING CONCEPT

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1. LOCAL CONTROL

The tax base rather than the level of tax collections is shared. Local Communities are left to determine their own tax rate. The revenue from the tax base sharing scheme is distributed directly to the communities which leaves the communities the option of choosing the programs in which to invest their own local tax base if that is their pleasure.

2. STATEWIDE ASSESMENT STANDARD

All increments to the statewide non-residential tax base are assessed on the same standard by a statewide board of assessors. This issue's uniformity and equity in property assesment in industrial and commercial property which is difficult to assess at the local level.

3. CONSERVATION OF NATURAL RESOURCES

The tax base sharing concept would aid in environmental preservation and conservation by partially"compensating" localities that provide open space and recreational resources for themselves and the state as a whole. This is accomplished by reducing the pressures to develop areas in order to relive residential property tax burdens.

4. NEW GOVERNMENT

No new taxes or additional taxing authorities would be created, the concept merely divides the future base among the existing municipalities.

5. STABLIZATION

Provides for stability in the level of revenue localities have available over the the fiscal cycle of the municipalities. Mature communities with high levels of services, and little industrial development would not be inclined to increase tax rates on existing property because they will share in the tax base of expanding communities with little need for high rates.

6. IMPROVE TAX EQUITY

Much economic development locates in areas with developed infrastructures. These infrastructures are often constructed with federal and state funds and not exclusively the funds of the localities in which industrial and Commercial facilities are located. Equity considerations suggest that a portion of the fiscal income derived from these facilities be shared statewide in partial compensation for the public investment in the infrastructure of the area.

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7. Phase out the Pay in Communities

The pay in towns will be eliminated as the growth pool grows in size. As the B component grows all towns will share this growth - but the pay in towns will simply pay in less and at some point not pay in at all and begin to share in the fiscal benefits of commercial and industrial expansion.

8. Economic Development

Predicting interstate industrial investment decisions is difficult and imprecise but there is no obvious reason to expect a states attractiveness to industry to deteriorate simply because part of the local tax bill would be pooled. Indeed, it is likely that investors will regard this favorably as a means of reducing somewhat the autonomy of local governments over their tax liability. It is also likely that more sensible long-run development planning in public infrastructure that would result from the tax base sharing concept would attract those industries most advantageous to the state.

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A GUIDE TO INCREASED REVENUES

"To tax and to please, no more than to love and be wise, is not given to man."
-Edmund Burke

INTRODUCTION

In general, there are two reasons for increasing the revenues of a specific tax:

A. To finance new or present programs; or

B. To shift tax burdens within the tax structure to try to more accurately tax according to "ability to pay" (e.g., increase the sales or income tax and lower the property tax).

This paper attempts to list the many possible sources of increased revenues for one fiscal year. The revenue estimates are approximate and in some cases taken from dated studies. Still, they offer a guide to where a legislator might look for increased state revenues.

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SOURCES OF INCREASED REVENUES

A. PROPERTY TAXES

1. Increase the Uniform Property Tax (UPT). Delete the restriction in the School Finance Act which limits the UPT to no more than 50% of the cost of education and the UPT would become a completely unrestricted general fund revenue source. Each mill in fiscal year 1977-78 produces 11.6 million.[1/]

2. Remove current property tax exemptions.

a. Remove the exemption of business inventories and the UPT would generate $7 million more at the current mill rate. Further, the base of the local property tax would be expanded, thereby providing greater local revenues.[2/]

b. Remove the current veteran's residential property tax exemption and UPT revenues would be increased by $ .9 million.[3/]

1/ Bureau of Taxation estimate.

2/ Id.

3/ Id.

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B. SALES TAXES

1. Increase the sales tax rate by 1/2%: $18.5 million. 4/

2. Expand the sales tax base to include:

a. Personal services (e.g., laundries, barber shops, carpet cleaning, etc.): $3.8 million. 5/

b. Miscellaneous repair services (e.g., electrical repairs, reupholstering, etc.): $1.40 million. 6/

c. Amusements (motion picture admissions, golf courses, etc.): $1.6 million. 7/

d. Miscellaneous business services (e.g., advertising, window cleaning, etc.): $3.3 million. 8/

e. Drug stores: $2.6 million. 9/

f. Professional services (e.g., lawyers, doctors, etc.): more than $7 million. 10/

g. Food, with an income tax rebate to protect the low income person: $12.7 million. 11/

h. Gambling. 12/

(i) Lottery sales: $ .4 million;

(ii) All other gambling: $1.3 million.

3. Remove sales tax exemptions. The sales tax has a multitude of exemptions, together they add up to a state expenditure equal to more than 60 million.

4/ Bureau of Taxation estimate.
5/ State Planning Office estimate.
6/ Id.
7/ Bureau of Taxation estimate.
8/ State Planning Office estimate.
9/ Id.
10/ Id.
11/ ESCO Research, Inc. estimate.
12/ Bureau of Taxation estimate.

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C. LIQUOR EXCISE TAX

1. $ .02 increase a six pack of malt liquor: $1.8 million.

2. $ .03 increase per bottle of table wine: $ .2 million.

3. Small increase in the sparkling wine tax: $11,000.00.

4. Increase the mark up on hard liquor (a $5.95 bottle would now costs $6.10): $ 1 million.

D. CIGARETTE AND TOBACCO EXCISE TAXES 14/

1. Increase the cigarette excise tax by $ .01: $ 1.5 million. A perhaps more favorable method is to simply expand the sales tax to cover cigarettes: $3.5 million.

2. Apply an excise tax to the previously exempted tobacco products (e.g., cigars, pipe tobacco): $ .75 million.

E. DEDICATED FUNDS

1. Release surplus funds in small dedicated accounts so they can be used for general fund expenditures: $3-5 million 15/ (each biennium); or

2. An increase in the gasoline tax of $ .01 per gallon would increase revenues by $5.75 million. 16/

F. PERSONAL INCOME TAXES 17/

1. A 1% surcharge for each of the present income brackets would increase revenues by $ .8 million.

13/ Bureau of Alcoholic Beverages estimate.
14/ Bureau of Taxation estimate.
15/ State Budget Office estimate does not include gas taxes or monies from hunting or fishing licenses.
16/ Bureau of Taxation estimate.
17/ Id.

2. Increase revenues by expanding the number of brackets and increasing the rates. This not only could increase the revenues but also make for a more gradual progressivity. For example, a schedule which is based on 16% of the federal personal income tax schedule (see Appendix A) would bring in $6.1 million more than is currently projected for 1977-78.[18/]

G. BUSINESS INCOME TAXES

1. Increase revenues by expanding the number of income brackets and increasing the rate. For example, the following schedule was recommended by the 1976 Committee on State Tax Policy and would increase revenues by $2.1 million:[19/]

Taxable income	Tax owed
$0-$25,000	5%
$ 25,000-$100,000	7%
$100,000+OVER	8%

2. a 1% increase in each of the two current corporate income brackets would increase revenues by $3.6 million.[20/]

3. A general business excise tax, levied on gross proceeds or income. One example of such a tax is West Virginia's Occupational Gross Income Tax, which is used in conjunction with a state corporate income tax but is clearly the dominant state business tax (27% of state revenues as opposed to 2% for the corporate income tax). This tax may be of special interest to the legislators as it provides for different tax rates for different industries (i.e., utilities, paper companies) and also provides a vehicle for business credits. It appears to give the state great leverage in creating a favorable business tax climate fashioned to the state's

18/ Bureau of Taxation estimate.
19/ Id.
20/ Id.

particular resources (see Appendix B).

4. A general business excise tax levied on net income. One example of such a tax is Michigan's Single Business Tax, which replaced all their other business taxes, applies to individuals, corporations, financial institutions, estates, trusts and partnerships, and which is levied at a rate of 2.35% of the taxpayer's federal taxable income.

H. INHERITANCE TAX

1. 1% rate increase in all inheritance classes would increase revenues by $1 million.[21/]

I. INSURANCE COMPANY TAXATION[22/]

1. Increase to 2% premium receipts tax on domestic insurance companies: $ .5 million.

2. Increase to 3% premium receipts tax on out of state insurance companies: $1.25 million.

3. Institute a gross receipts tax on the investment income of domestic insurance companies: $1.5 million.

J. MISCELLANEOUS SOURCES OF INCREASED REVENUES[23/]

1. Impose the sales tax on the automobile trade-in allowance: $ 4.5 million.

2. Impose a 1% meals and lodging tax: $2.5 million.

3. Increase the real estate transfer tax to 1%: $3.5 million.

4. Increase automobile registration fees by $5: $2.2 million (dedicated).

5. Consider the principle of increasing charges to users of specialized state services (no estimates).

6. Consider saving revenue by limiting bonding as a source of state funds (no estimate).

21/ Bureau of Taxation estimate.
22/ ESCO Research, Inc. estimates.
23/ Id.

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APPENDIX A

A personal income tax schedule based on 15% of the new federal schedule and yielding $ 6.1 million in new revenue.

TAXABLE INCOME		TAX OWED
$0 - 500		2.2%
500	1,000	$ 11 + 2.4%
1,000	1,500	23 + 2.6%
1,500	2,000	36 + 2.7
2,000	4,000	50 + 3
4,000	6,000	110 + 3.4
6,000	8,000	178 + 3.8
8,000	10,000	254 + 4
10,000	12,000	334 + 4.3
12,000	14,000	421 + 4.6
14,000	16,000	514 + 5
16,000	18,000	613 + 5.4
18,000	20,000	722 + 5.8
20,000	22,000	837 + 6.1
22,000	26,000	958 + 6.4
26,000	32,000	1,214 + 7.2
32,000	38,000	1,646 + 8
38,000	44,000	2,126 + 8.8
44,000	50,000	2,654 + 9.6
50,000	60,000	3,230 + 9.9
60,000	70,000	4,222 + 10.2
70,000	80,000	5,246 + 10.6
80,000	90,000	6,302 + 10.9
90,000	100,000	7,390 + 11
100,000 and over		8,494 + 11.2

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Occupational Gross Income Tax

Persons and Sales Subject to Tax.—A tax is levied on all persons and corporations, for the privilege of engaging in business, based on values or gross income (Sec. 2).

Exemptions.—The first $50 of annual tax is exempt. The following persons and corporations are also exempt (Sec. 3):

1. Insurance companies paying a premium tax; the exemption does not apply to that part of the gross income of insurance companies received as rentals or royalties for the use of realty.
2. Non-profit cemetery companies.
3. Non-profit societies, organizations, etc., organized for the benefit of their members, except as to gross income from sales of liquor, food and related services by licensed private clubs.
4. Religious or charitable corporations, associations and societies.
5. Production credit associations.
6. Credit unions.
7. Gross income from radio and television advertising (S. B. 316, Laws 1975).
8. Any demonstration, pilot or research project, at least partially funded by public money, for the gasification or liquification of coal, but only until June 30, 1981 (S. B. 316, Laws 1975).
9. West Virginia business development corporations (Ch. 31, Art. 14, Sec. 13).

A tax credit for industrial expansion is allowed industrial taxpayers equal to 10% of the cost of qualified investments made for such expansion. The credit is applied over a ten-year period to reduce the tax at the rate of 1/10th of the amount of the credit per taxable year, beginning with the taxable year that the qualified investment is first placed in service or use. The credit may not reduce the tax imposed below 50% of the tax that would be imposed for the taxable year without the credit computed before application of the annual credit (Ch. 11, Art. 13C, Sec. 3).

Basis.—The tax is measured, in the case of producers, by the gross proceeds of production; in the case of manufacturers of commodities, by the gross proceeds of sales; in other businesses, by the gross income (Secs. 2—2-(j)). Losses and expenses are not deductible but cash discounts and refunds are excludable (Sec. 1).

Rates.—Rates are as follows:

Product or Business	Rate
Coal	3.5 %
Additional tax on coal, effective July 1, 1975 (S. B. 285, Laws 1975; Sec. 2(1))	0.35%
Limestone or sandstone, quarried or mined	2.2 %
Oil	4.34%
Natural gas (over $5,000)	8.63%
Blast furnace slag	4.34%
Mineral products not quarried or mined	4.34%
Timber	2.2 %
Other natural resources (Sec. 2-(a))	2.86%
Manufacturing, compounding, preparing of products, including newspaper publishing (Ch. 133, Laws 1974; Sec. 2-(b))	0.88%
Wholesale selling of tangible property	0.27%
Other selling of tangible property (Sec. 2-(c))	0.55%
Street, interurban and electric railways	1.4 %
Water companies	4.4 %
Electric light and power companies, sales for domestic purposes and commercial lighting	5.72%
Sales for other purposes	4.29%
Natural gas companies	4.29%
Toll bridge companies	4.29%

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Product or Business	Rate
Other public utilities, except railroad, car, express, pipe line, telephone, telegraph, steamship and motor carriers ... (Sec. 2-(d))	2.86%
Contracting ... (Sec. 2-(e))	2.2 %
Operating amusements ... (Sec. 2-(g))	0.71%
Service businesses or callings not otherwise taxed, including professions ... (Sec. 2-(i))	1.15%
Leasing or furnishing real or tangible personal property, other than money or public securities ... (Sec. 2-(j))	1.15%
Banking or financial businesses ... (Sec. 2-(k))	1.15%

Permit Requirements.—No statutory provisions.

Reports.—All taxpayers report to the State Tax Department within one month after the expiration of each quarterly and annual period (Secs. 4, 5).

Collection.—Tax payment to accompany quarterly and yearly reports. If the total tax does not exceed $100 in any year the taxpayer may pay the tax quarterly or, with permission, at the end of the month following the close of the tax year (Secs. 4, 5).

Source.—References are to West Virginia Code of 1931, Chapter 11, Art. 13, as enacted by Ch. 33, Laws of 1933, and amended to date. Complete details are reported in CCH WEST VIRGINIA TAX REPORTER at ¶ 65-000.

FULL DISCLOSURE OF THE EFFECT OF RATE AND BASE CHANGES ON LOCAL REVENUES[1]

Under our democratic system, justice and fair play demand that citizens have an opportunity to be informed about the fiscal affairs of their government and to express their views on major fiscal decisions.

The Commission believes that one of the specific elements that should be disclosed to the public is the effect changes in the rate and base of local taxes, fees, and charges have on local revenue; for example, the impact changes in assessments have on the local property tax levy.

One way to assure such disclosure is enactment of state legislation designed to encourage public discussion of local tax decisions before proposed tax and spending plans become final. Such legislation, popularly termed "truth in taxation," relies not on explicit tax or spending limits but on strengthening the control inherent in public awareness of the political process.

Under a full disclosure procedure, applicable, for example, to the property tax, the local assessor each year must announce a certified tax rate which, when applied to the assessment base, will provide the same amount of property tax revenue as is obtained in the current year. This certified rate then becomes the highest tax rate which the taxing jurisdiction is authorized to impose unless it advertises its in-

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1/ Derived from Advisory Commission on Intergovernmental Relations <u>State Limitations on Local Taxes and Expenditures</u> (Washington, D.C., U.S. Government Printing Office, March 1977) tention to raise the level of property taxation and holds a hearing to obtain public reaction.

To illustrate the procedure, let us assume that the taxable assessed value for a certain taxing district is $10 million currently and the tax levy is $100,000 based on a rate of 10 mills, or $1 per $100 of assessed value. The assessor adds $1 million to the assessment roll for the upcoming year ($500,000 in revaluation; $500,000 in new construction). Thus, the total taxable value of the jurisdiction for the upcoming year will be $11 million, a 10 percent increase in the tax base.

Without changing its tax rate, the jurisdiction would net a 10 percent increase in property tax revenues. Under a full disclosure procedure, the assessor would be required to calculate a tax rate (9.1 mills) which, when applied to the new assessed value ($11 million) would produce $100,000, the same revenue as is currently obtained.

To allow for some growth in the local budget, however, the law might allow subtraction of new construction from the full amount of the new assessment roll. Thus, the assessor would determine the certified rate by dividing $100,000 (the current levy) by the total assessed value less new construction or $10,500,000. The certified rate would be 9.5 mills, a half mill lower than the current rate.

If the local taxing district chose to accept the new, lower rate of 9.5 mills, the total levy would be $104,500, a 4.5 percent increase. Any taxpayer whose assessed value increased by 5 percent or less would experience no tax increase whatever because the new rate is 5 percent lower than the current rate.

If the 5 percent increase in the total tax levy appeared to be inadequate to the needs of the taxing jurisdiction, its officials could increase the revenue by exceeding the certified rate as long as the higher rate had been advertised, a public hearing held, and the local governing body had then voted to approve the higher rate.

The full disclosure approach, as described here, serves two purposes. It provides citizens with the information and opportunity they need to express themselves on proposed expenditure and tax increases. It fixes political responsibility for any property tax increase on the local governing body, whose task is to determine the spending level and required tax rate, and not on the local assessor or any state officials charged with responsibility for determining the assessed value.

The distinction between property tax levy limits and full disclosure laws is the method provided for exceeding the limit. In the case of levy limits, laws usually provide that the voters must approve at a referendum any property tax levy greater than that allowed by the limit. With the full disclosure procedure, the final judgment to exceed the established millage rate rests with the local governing body. Under full disclosure, when assessments rise, property tax rates are automatically reduced pending tax rate action by elected officials.

Jurisdictions which have adopted the full disclosure procedure applicable to the property tax are Florida (1971), Montana (1974), the District of Columbia (1975), Hawaii (1976), and Virginia (1976). The accompanying suggested legislation is based on the full disclosure laws of Florida and Montana (Chapter 70-368 and "Property Taxpayers Information Act" Chapter 386, Laws of 1974, respectively).

Section 1 covers the purpose of the act. Section 2 calls for the certification of taxable values and the tax rate applicable to the property tax which, when applied to the previous year's assessed value, will produce the same revenue. More fiscal leeway can be granted local taxing jurisdictions by specifying that the assessor use a percentage (less than 100 percent) of the assessed value of property on the roll in the previous year in calculating the certified rate. Section 3 requires local governing bodies intending (a) to increase the property tax rate above the certified rate or (b) to increase any other fee, charge, or rate, or to redefine the objects or activities subject to such fees, charges, or rates to advertise their intention. The requirement in Section 4 that the advertisement of proposed increase over the certified property tax rate be prominent and not be in the classified ads has caused these announcements in Florida newspapers to be termed "Doomsday Notices." Section 4 also calls for a public hearing and passage of a resolution or ordinance establishing the property tax rate. Section 5 deals with administration and application of the property tax rate by the treasurer, assessor, and state tax agency. Section 6 permits local officials to automatically take into account in the certified property tax rate any change required as a result of reduced assessments on appeals. Section 7 specifies instances in which readvertising shall occur. Section 8 affirms the authority of local jurisdictions to reduce the property tax levy.

Suggested Legislation

[AN ACT PROVIDING FOR FULL DISCLOSURE OF THE EFFECT OF RATE AND BASE CHANGES ON LOCAL REVENUES]

(Be it enacted, etc.)

SECTION 1. Purpose. It is the purpose of this act to provide for full disclosure of the effect of rate and base changes on local revenues.

SECTION 2. Certification of taxable values and tax rates applicable to the property tax. At the time that the assessment roll is prepared and published, the (State Tax Agency or Assessor) shall certify to each taxing authority the taxable value within the jurisdiction of the taxing authority. The (State Tax Agency or Assessor) shall also send to each taxing authority an estimate of the total assessed value of all new construction and improvements not included on the previous assessment roll, and the value of deletions from the previous assessment roll. Exclusive of such new construction, improvements, and deletions the (State Tax Agency or Assessor) shall certify to each taxing authority a tax rate which will provide the same ad valorem revenue for each taxing authority as was levied during the prior year. For the purpose of calculating the certified rate, the (State Tax Agency or Assessor) shall use the taxable value appearing on the roll exclusive of taxable value of properties appearing for the first time on the assessment roll.

SECTION 3. Increase of revenue--Advertising of intention required.

(1) No taxing authority shall budget an increased amount of ad valorem tax revenue exclusive of revenue from ad valorem

taxation on properties appearing for the first time on the assessment roll, unless it advertises its intention to do so at the same time that it advertises its intention to fix its budget for the forthcoming fiscal year.

(2) No taxing authority shall budget an increased amount of revenue from revenue sources (other than the property tax) over which it has control when such revenue will result from (i) an increased fee, charge, or rate or (ii) a change in the definition of the object or activity to which the fee, charge, or rate is applied, unless it announces its intention to do so at the same time it advertises its intention to fix its budget for the forthcoming fiscal year.

SECTION 4. Resolution or ordinance for increase over certified tax rate applicable to property taxes. No tax rate in excess of the certified tax rate shall be levied until a resolution or ordinance has been approved by the governing board of the taxing authority, which resolution or ordinance must be approved by said taxing authority according to the following procedure:

(1) The taxing authority shall advertise its intent to exceed the certified tax rate in a newspaper of general circulation in the county, as provided in Section 3 of this act. The advertisement shall be no less than one quarter (1/4) page in size and the smallest type used shall be eighteen (18) point. The advertisement shall not be placed in that portion of the newspaper where legal notices and classified advertisements appear. The advertisement shall state that the taxing authority will meet on a day, at a time and place fixed in the advertisement, which shall be not less than seven (7) days after

the day that the advertisement is published, for the purpose of hearing comments regarding the proposed increase and to explain the reasons for the proposed increase. The meeting on the proposed tax rate increase may coincide with the hearing on the proposed budget of the taxing authority.

(2) The taxing authority, after the public hearing has been held in accordance with the above procedures, may adopt a resolution or ordinance levying a tax rate in excess of the certified tax rate. If the resolution or ordinance adopting said tax rate is not approved on the day of the public hearing, the day, time and place at which the resolution or ordinance will be scheduled for consideration and approval by the taxing authority must be announced at the public hearing. If the resolution or ordinance is to be considered at a day and time that is more than two (2) weeks after the public hearing, the taxing authority must again advertise in the same manner as provided in section 3 and 4(1) of this act.

SECTION 5. Approval and copies of resolution or ordinance. The resolution or ordinance approved in the manner provided for in this act shall be forwarded to the (assessor, treasurer, and State Tax Agency). No tax rate in excess of the certified tax rate can be levied until the resolution or ordinance to levy required in section 4(1) and (2) of this act is approved by the governing board of the taxing authority and submitted to the assessor and the State Tax Agency.

SECTION 6. Exceptions for decisions of tax appeal boards. The (State Tax Agency) shall notify each taxing authority of any change in the assessment roll which results from actions by the State or county tax appeal boards. An increase in the taxing authority's tax rate above that certified by the (department or assessor) or adopted by resolution or ordinance of the governing body of the taxing authority, which is required solely by a reduction of the assessment roll by the State or county board of tax appeals, may be adopted without further notice.

SECTION 7. Additional tax rate increase - Readvertising and revoting. If, after the initial tax rate vote provided for in section 3 of this act, the taxing authority determines that it requires a greater tax rate or fails to act in the specified period, it shall readvertise and revote as required in sections 3 and 4 of this act.

SECTION 8. Increase over legal maximum not authorized - Reductions permitted. Nothing contained in in this section shall serve to extend or authorize any tax rate in excess of the maximum permitted by law nor prevent the reduction of the tax rate.