

MAINE STATE LEGISLATURE

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STATE of MAINE

JOINT INTERIM LEGISLATIVE COMMITTEE

TO STUDY THE TAX STRUCTURE OF THE STATE

REPORT

to the

106TH MAINE LEGISLATURE

JANUARY, 1973

SPECIAL JOINT INTERIM COMMITTEE TO STUDY THE TAX STRUCTURE
OF THE STATE OF MAINE

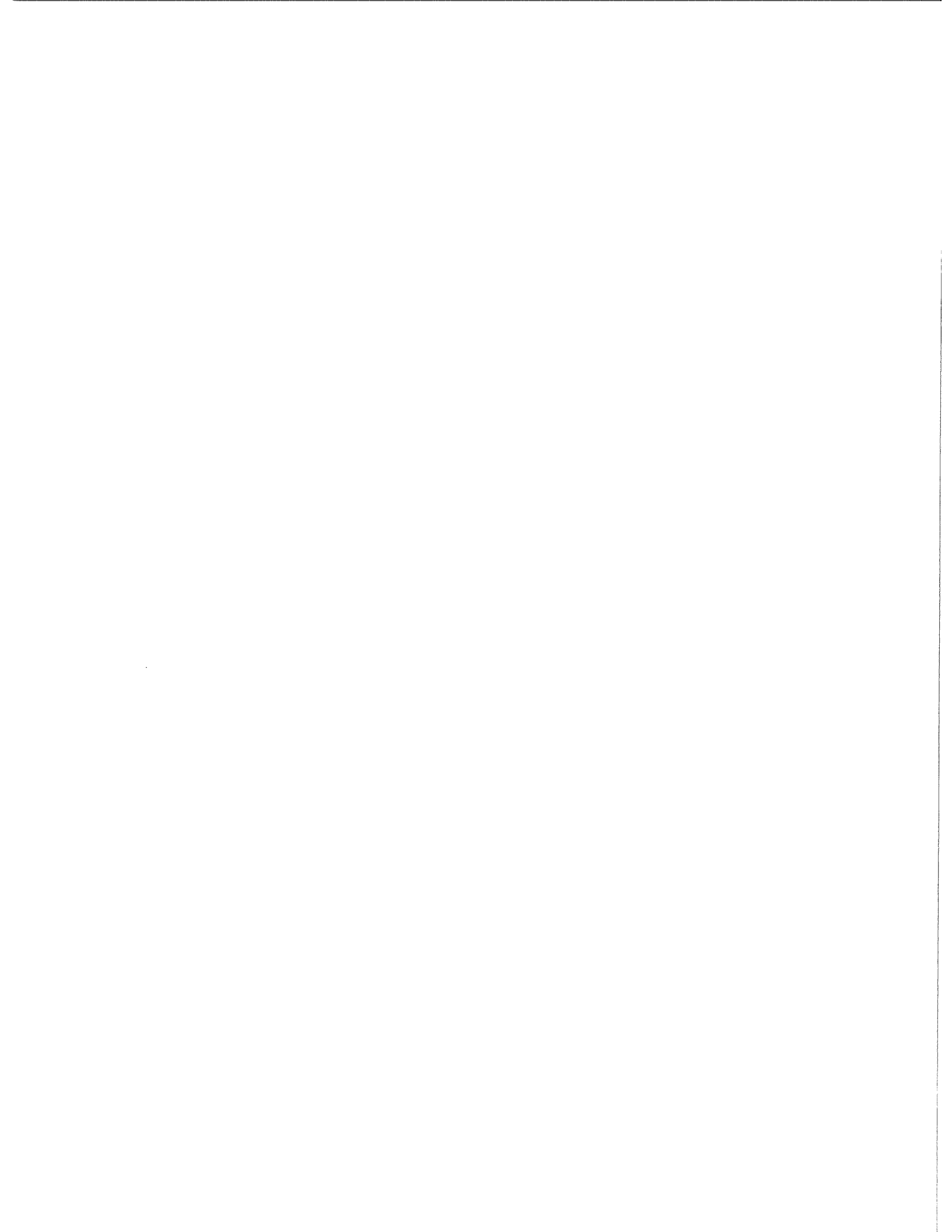
Senator George H. Chick, <u>Chairman</u>	Monmouth
Senator J. Hollis Wyman	Milbridge
Senator Armand J. Fortier	Rumford
Rep. Rodney Ross, Jr.	Bath
Rep. Louis Finemore	Bridgewater
Rep. David Emery	Rockland
Rep. John Cottrell, Jr.	Portland
Rep. Jay McCloskey	Bangor
Mr. Edwin A. Heisler (Public) <u>Vice Chairman</u>	Portland
Mrs. Joan Bush (Banking)	Farmingdale
Dr. Lincoln T. Fish (Education)	Gorham
Mr. Scott Fox, Jr. (Business)	Cumberland
Mr. John Hanson (Labor)	Bangor
Mr. John Salisbury (Municipal)	Hallowell
Mr. Arthur Stedman (Industry)	Waterville

Research Assistants:

Earl K. Ireland
Robert Briggs

Secretary:

Mrs. Rosa Prime



STATE OF MAINE
HOUSE OF REPRESENTATIVES
105th LEGISLATURE
FIRST SPECIAL SESSION

Whereas, the tax structure of the State of Maine must adequately meet the ever-increasing demands for financing future public services; and

Whereas, the additional demands for welfare, educational subsidy and change in method of school financing pose grave challenge to the existing structure; and

Whereas, all major sources of taxation are presently being utilized by the State with no consideration being given to alternative means of meeting probable increases; and

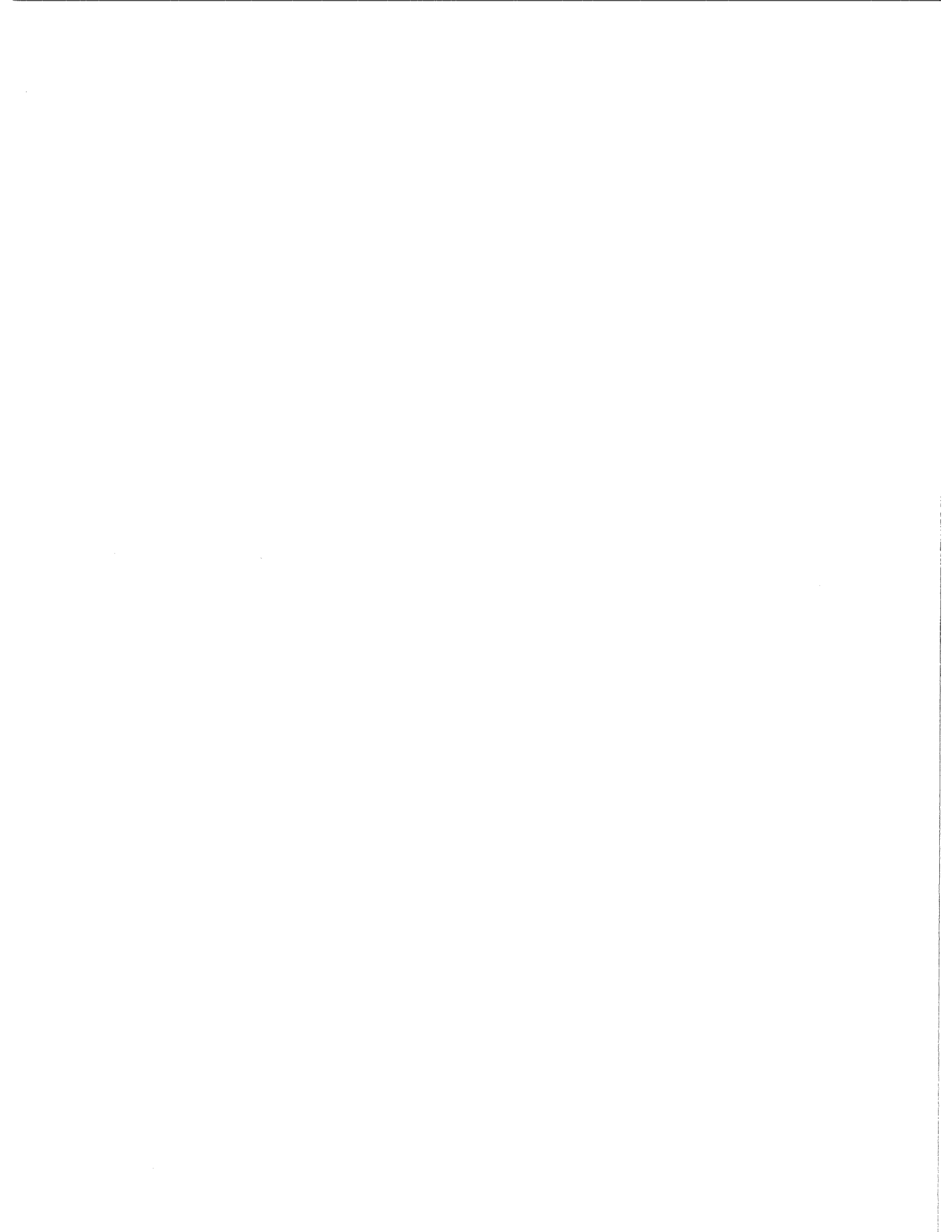
Whereas, there is an urgent need to determine if the present tax structure is fair, equitable and adequate as presently constituted to meet the needs of the future; now, therefore, be it

ORDERED, the Senate concurring, that there is created a Special Joint Interim Committee to consist of 3 Senators to be appointed by the President of the Senate and 4 Representatives to be appointed by the Speaker of the House to study the tax structure of this State and for the purpose of this study any subject or matter adjudged by the committee to be relevant or germane to the subjects of its study or helpful to it in the consummation of its work hereunder shall be deemed within the scope of the committee's inquiry hereunder; and be it further

ORDERED, that the committee shall report the results of its study to the next regular session of the Legislature; and be it further

ORDERED, that all state departments and agencies provide the committee to the extent possible, with information and assistance in the fields of tax and economic research, and make available to the committee, as needed, the services of persons knowledgeable in the field of taxation, public finance and economics; and be it further

ORDERED, that the members of the committee be compensated for time spent in attendance at meetings of the committee and when engaged in performance of duties



STATE OF MAINE

In House _____

Ordered,

under instructions of the committee and authorization by its chairman at the rate of \$25 per day and actual expenses incurred in the performance of their duties under this Order; such sums to be paid out of the Legislative Account; and be it further

ORDERED, that the committee shall have the authority to employ professional and clerical assistance within the limits of funds provided; and be it further

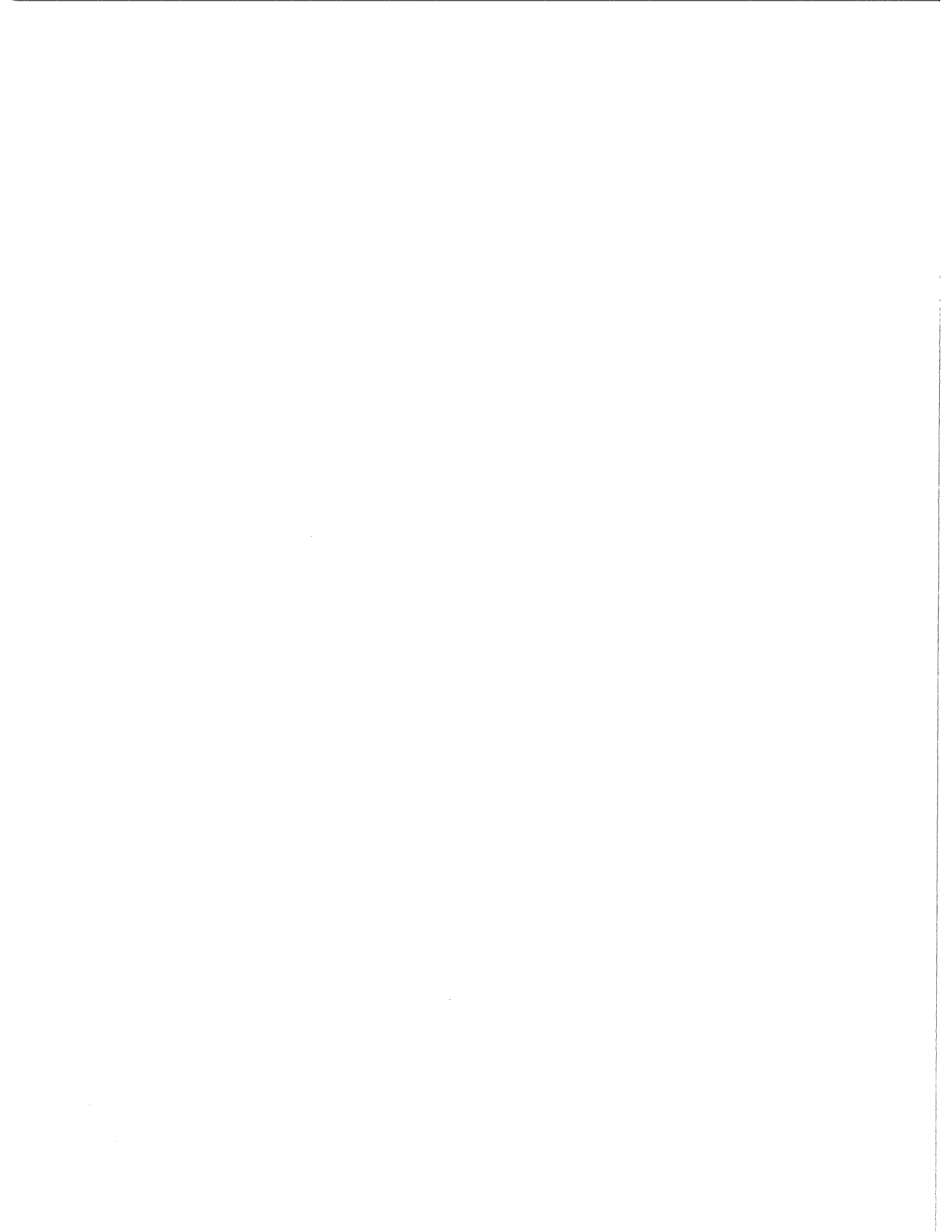
ORDERED, that there is allocated to the committee from the Legislative Account the sum of \$10,000 to carry out the purposes of this Order.

Name: Susi

Town: Pittsfield

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1/28/72



STATE OF MAINE
HOUSE OF REPRESENTATIVES
105TH LEGISLATURE
FIRST SPECIAL SESSION

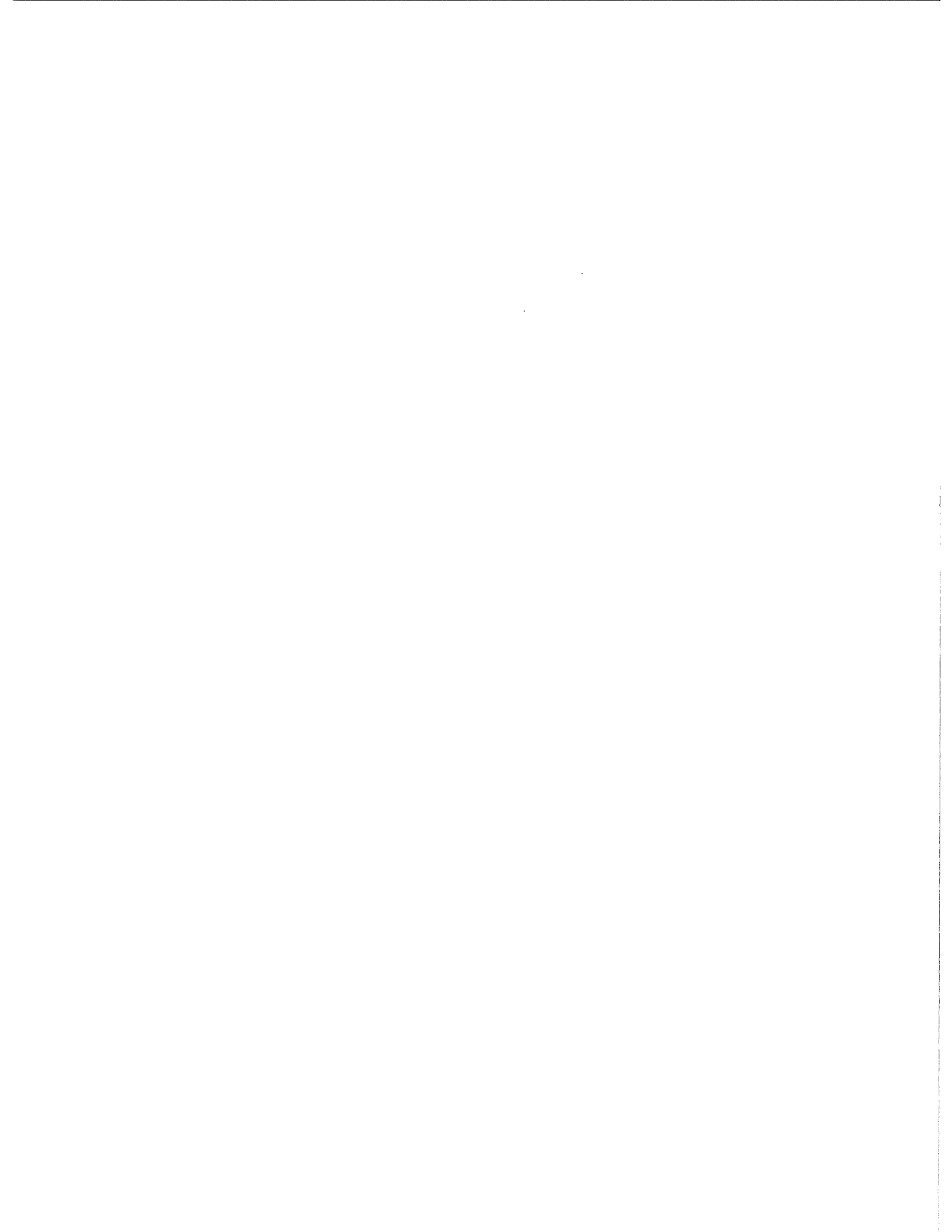
HOUSE AMENDMENT "A" to House Joint Order to Study the Tax Structure of the State.

Amend said Order by striking out all of the 5th paragraph and inserting in place thereof the following:

'ORDERED, the Senate concurring, that there is created a Special Joint Interim Committee to consist of 15 persons to be appointed as follows: 3 Senators to be appointed by the President of the Senate, 5 Representatives to be appointed by the Speaker of the House and 7 to be appointed by the Governor to represent the public, industrial, business, labor, banking, municipal and educational interests of the State to study the tax structure of this State and for the purpose of this study any subject or matter adjudged by the committee to be relevant or germane to the subjects of its study or helpful to it in the consummation of its work hereunder shall be deemed within the scope of the committee's inquiry hereunder; and be it further'

Further amend said Order by striking out all of the 8th paragraph and inserting in place thereof the following:

'ORDERED, that the legislative members of the committee be compensated for time spent in attendance at meetings of the committee and when engaged in performance of duties under instructions of the committee and authorization by its chairman at the rate of \$20 per day and all members of the committee shall receive actual expenses incurred in the performance of their duties under this Order; such sums to be paid out of the Legislative Account; and be it further'



INTRODUCTION

The work of the Special Interim Committee on Tax Structure focused on answering two fundamental questions:

- (1) What are the characteristics of a high quality, balanced state-local tax structure?
- (2) What steps can be taken in Maine state and local government to develop a better balanced tax structure?

A comprehensive overview of Maine's present state-local revenue structure indicates that approximately 44% of the total tax dollars come from property taxes, 22% from the sales tax, 7.5% from the income tax, and 26.5% from other taxes. After a thorough examination of what constitutes our existing tax structure, the Committee started a process of developing guidelines for what in its collective judgment was a "balanced state-local tax structure".

In the course of its examination, the Committee has heard from, and consulted in return, representatives from education, industry, business and insurance; has reviewed other reports such as the Sly Report, the Advisory Committee on Business Taxation Report, the report of the Advisory Committee on Intergovernmental Relations, and drafts of the Governor's ESCO Report; has had expert advice and invaluable aid from the State Bureau of Taxation, and has collected voluminous amounts of data and figures.

The Committee has adopted as a high quality state-local tax structure one that will provide 30% of revenues from property taxes, 21.8% from the sales tax, 25% from the income tax, and 23.2% from other taxes. The Committee recommends that this structure be implemented in a series of steps over the next three bienniums.

The tax structure at present relies for about two-thirds of its revenue upon the property and sales taxes. Both of these taxes are regressive. The present burden of property taxes in almost every area of the state is oppressive and is continuing to increase. In addition, ownership of property today no longer necessarily represents monetary wealth; thus taxes drive all but the more wealthy off their lands.

It is an economically accepted theory that higher personal incomes create demands for more public services, which in turn means more taxes to support these services. If the structure were to continue as is, periodic financial crises would arise, alleviated only by tax rate increases. Under the proposed structure, with more dependence on the income tax, revenue intake would be more responsive to income increases -- tax dollar increases would be rather automatic. In other words, as personal income increased, so would demands on public treasuries, but so would public revenues.

The first step in, and a prime motivating factor for, restructuring the tax system is refinancing public education. Court decisions will inevitably force Maine to abandon its present inequitable system of relying on local property taxes, thus steps should be taken now to avoid emergency action later. The Committee recommends, by a vote of ten in favor, none opposed, three abstentions, that the state assume 60% of the total cost of public education, grades K through 12, subsidizing communities on a per pupil basis. It should be noted that this 60% is distinct from and exclusive of the statewide property tax revenues discussed later.

In addition, a mechanism for a tax credit, not to exceed a set sum, for tuition paid by parents to send their public school age children to private schools, should be established; private schools absorb what would be a significant burden upon public schools, were these private schools forced to close. It is felt that Federal constitutional problems are avoided if the tax credit is available for all private schools, not just certain ones.

Another factor making the "new" structure desirable is that combined with Federal Revenue Sharing, it offers an opportunity to effectuate significant tax reforms. In addition, as part of the restructuring process, several existing taxes could be modernized or eliminated, as appropriate.

Finally, it must be emphasized that this report does not favor and is not recommending increases in taxes for the purpose of adding to revenue generally. Rather, the Committee is concerned with restructuring the revenue system and re-allocating tax burdens within the existing or projected budgets, for the purpose of creating a more responsive, equitable, and evenly balanced system of taxation. Of course, the Legislature may finally decide that more money is

needed for new programs. If so, then it should be clear that the Committee would direct revenue-raising proposals to sources other than the property or sales taxes.

As additional steps in the restructuring process, the Committee offers the following:

PROPERTY TAXES

As most of the inequities in the existing property taxes result from the multitude of assessing districts and practices, the Committee recommends, by an eight to four, one abstention, vote of its members, that a uniform state-wide property tax be established, some of the money therefrom to be used to finance not more than 40% of the costs of education. This 40% is unrelated to the 60% state assumption referred to earlier. It should be noted that the objections to the use of the property tax to finance education stem from the existing local character of the tax; a broader based one, as proposed, would be acceptable. In addition, some property tax is necessary and desirable; property creates demands that must be paid for, and much property is owned by non-residents who do not otherwise pay taxes here. This recommendation does not include the elimination of local property taxes; they are obviously necessary to pay for local services.

To administer this tax, an adequately funded Property Tax Bureau should be established under the Commissioner of Finance. This Bureau should be empowered to develop, adopt and implement assessment standards and qualifications of professional assessors, to be in effect by April 1, 1975. These standards should include matters such as elimination of fractional valuation. The Bureau should also have authority to delineate assessment districts, so that those communities that cannot meet the standards on their own can join with other similar communities within boundaries set by the Bureau. The Committee feels that this plan for administration meets both the need of a broader based property tax and the necessity of local involvement in property assessment.

A State Board of Property Tax Appeals should also be instituted, to provide a speedy, more economical means of appeal for the average aggrieved taxpayer.

Real property tax exemptions are especially troublesome. These exemptions put the burden of paying for services to the exempted properties on other property taxpayers, and otherwise serve to narrow the tax base. Therefore, the Committee, by a vote of eight to four, recommends that as to the state property tax the whole spectrum of exemption for real property be reevaluated, and that as to local property taxes, the committee recommends, by a seven to six vote, that all real property tax exemptions be eliminated, except for property used exclusively for charitable, educational, religious, or scientific purposes by an organization which qualifies as an exempt organization under section 501 (c) (3) of the Internal Revenue Code of 1954, and property used exclusively for public purposes by federal, state and local governments. The reason for the more liberal view toward the state property tax is that its primary purpose is to be used in education financing, and certain institutions can rightfully claim to be exempt from these costs.

The Committee, by a vote of ten to two, recommends the reduction or elimination of the personal property tax on business inventories and stock in trade. This tax is highly regressive and detrimental to Maine's competitive position in attracting business. Some businesses go out of their way to a considerable extent to warehouse their products out of state in order to escape this tax. The loss to local taxing units (which should be reimbursed by the state on a declining balance over a period of years) would over the long haul be regained in the form of increased business activity.

The Committee, voting eleven to one, recommends the elimination of the Bank Stock Tax, and the removal of the exemption of the applicable banks from the personal property tax. This tax is returned either to the place where the main office of the bank is located or to where the stock is owned, and is in lieu of a personal property tax. A personal property tax, payable to where the property is located, is more realistic.

The Committee also voted, nine to two, to recommend that all insurance companies, including Blue Cross/Blue Shield, be subject to the tangible personal property tax. The gross premiums tax, traditionally the only tax on insurance companies except real estate, sales, and payroll taxes, was instituted long before many present taxes, and thus can no longer be said to be in lieu of all these taxes.

INCOME TAXES

Under the "high quality structure", more emphasis would be on the income tax, in conjunction with tax reductions in other areas, specifically the property tax, as part of a program to align our tax system with a concept of ability to pay taxes.

In recognition of the high tax burden upon Maine residents and property owners, and of the fact that much real property is owned by nonresidents, the Committee recommends a formula for an individual income tax credit for residential property taxes paid within the state.

In the area of corporate taxes, the Committee voted eleven to none in favor of a progressive corporate income tax instead of the present flat rate of 4%. The rate should be fixed up to \$25,000, with a higher rate for amounts over \$25,000. This system represents a more efficient use of the corporate income tax and one method of replacing revenue lost through other recommendations in this report.

The Committee recommends, by a vote of ten to two, that the Legislature remove the premiums tax on all health insurance companies and impose an income tax on the investment income of all insurance companies, including Blue Cross/Blue Shield.

INSURANCE PREMIUMS TAXES

The Committee recommends, by a vote of ten to two, that the premiums tax on domestic and foreign insurance companies be maintained at the present 1% and 2% level because of the above decision to impose an income tax on the investment income of all insurance companies.

SALES AND USE TAX

The Committee, voting eleven in favor, recommends the elimination of the sales and use tax on machinery used in manufacturing. (Consumables are already "exempt" in that they are not included in the definition of "retail sales".) This step is necessary in making Maine more attractive to industry, and encouraging existing industries to expand. A 5% sales tax represents a large amount of cash when purchasing expensive equipment; industries indicate that either this step, or an investment credit on corporate income taxes, are most important measures. The sales tax route is more desirable, as it represents less money spent "now" rather than a return of money next year. Increased industry activity, and a higher corporate income tax, should make up for the lost revenue here.

POLL TAX

The Committee voted eight to none to recommend the elimination of the poll tax. As presently applied, to adult males only, court challenge and disapproval is inevitable. It is also a regressive tax, and a local administrative headache. For these reasons, the Committee recommends its elimination rather than broadening it to include women.

INHERITANCE TAX

The Committee, voting eight to one with two abstentions, recommends that the existing exemption for widows and for close relatives (\$15,000 and \$10,000 respectively) be increased, and that insurance proceeds to named beneficiaries, which are currently exempt, be taxed as are inheritances. Insurance death benefits are designed to protect surviving dependents; this is better accomplished through inheritance tax exemptions, rather than purchasing insurance to avoid inheritance taxes. The argument that insurance is purchased with after-tax dollars overlooks the fact that bequests and devises, subject to inheritance taxation, also represent after-tax dollars, or property purchased with after-tax dollars.

LEGISLATIVE TAXATION COMMITTEE

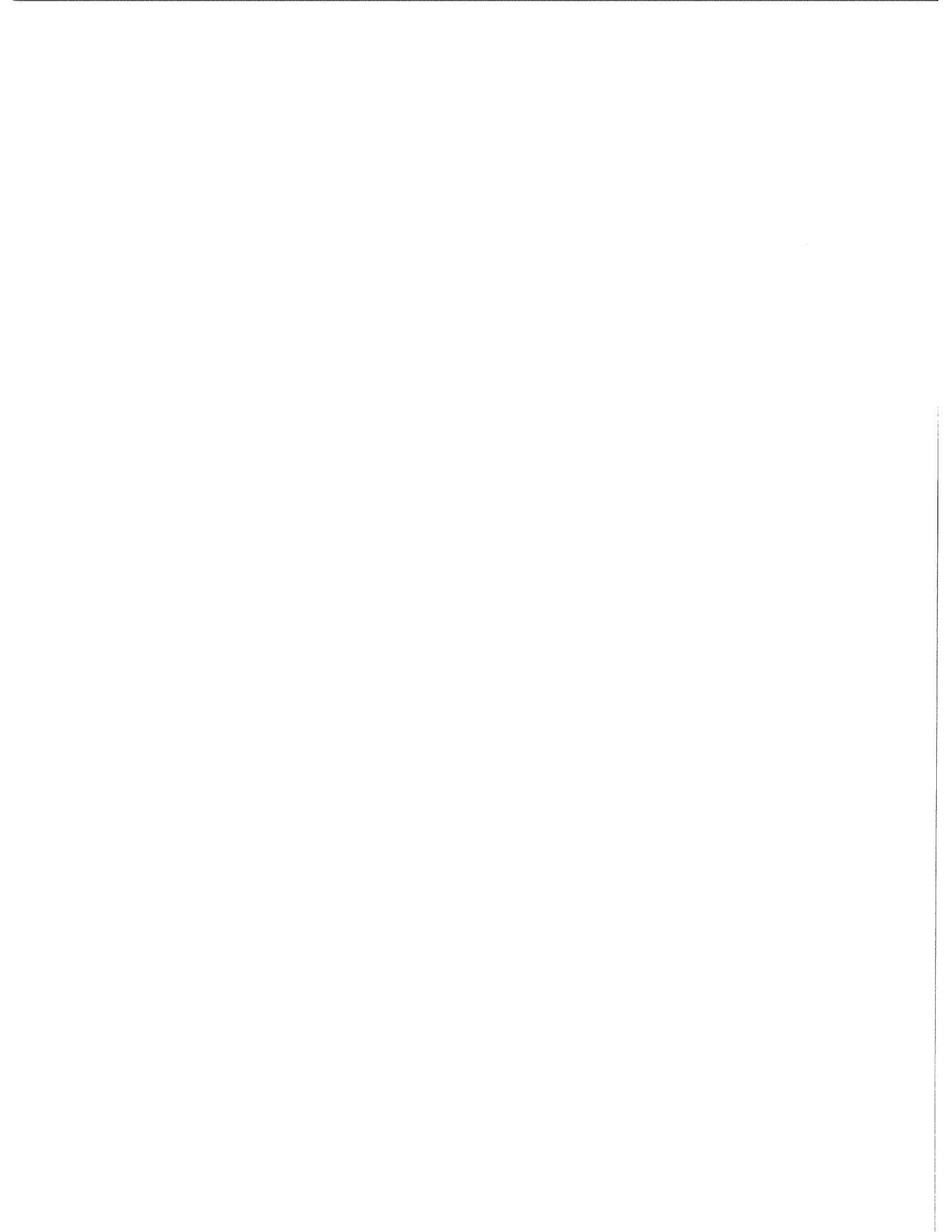
The Committee voted unanimously to recommend that the Joint Standing Legislative Committee on Taxation be authorized to meet regularly during the biennium. It was also recommended that they meet periodically with the Appropriations Committee, and that they have funds for professional staff on a permanent basis.

CONCLUSION

Obviously, many of the above recommendations could be instituted alone; just as obviously some depend on or are corollaries to others. The Committee requests that the members of the Legislature take the latter view. Observe the state-local tax system as a whole, keeping in mind the present inequities. Then consider all the recommendations from the point of view of formulating a new structure, with related items combined in bills:

- A. The ideal percentages for a "high quality structure" (Page 1 above).
- B. The refinancing of public education (Page 2).
- C. The state-wide property tax (Page 3).
- D. A Property Tax Bureau (Page 3).
- E. A State Board of Property Tax Appeals (Page 3).
- F. Review and elimination of real property tax exemptions (Page 4).

- G. Tax relief for business inventories (Page 4).
- H. The elimination of the Bank Stock Tax (Page 4).
- I. A restructuring of taxes on insurance companies (Pages 4 and 5).
- J. Income tax credit for residential property taxes paid (Page 5).
- K. Revised corporate income taxes (Page 5).
- L. Exemption of machinery used in manufacturing from the sales tax (Page 5).
- M. Elimination of the poll tax (Page 6).
- N. The readjustment of the inheritance tax (Page 6).



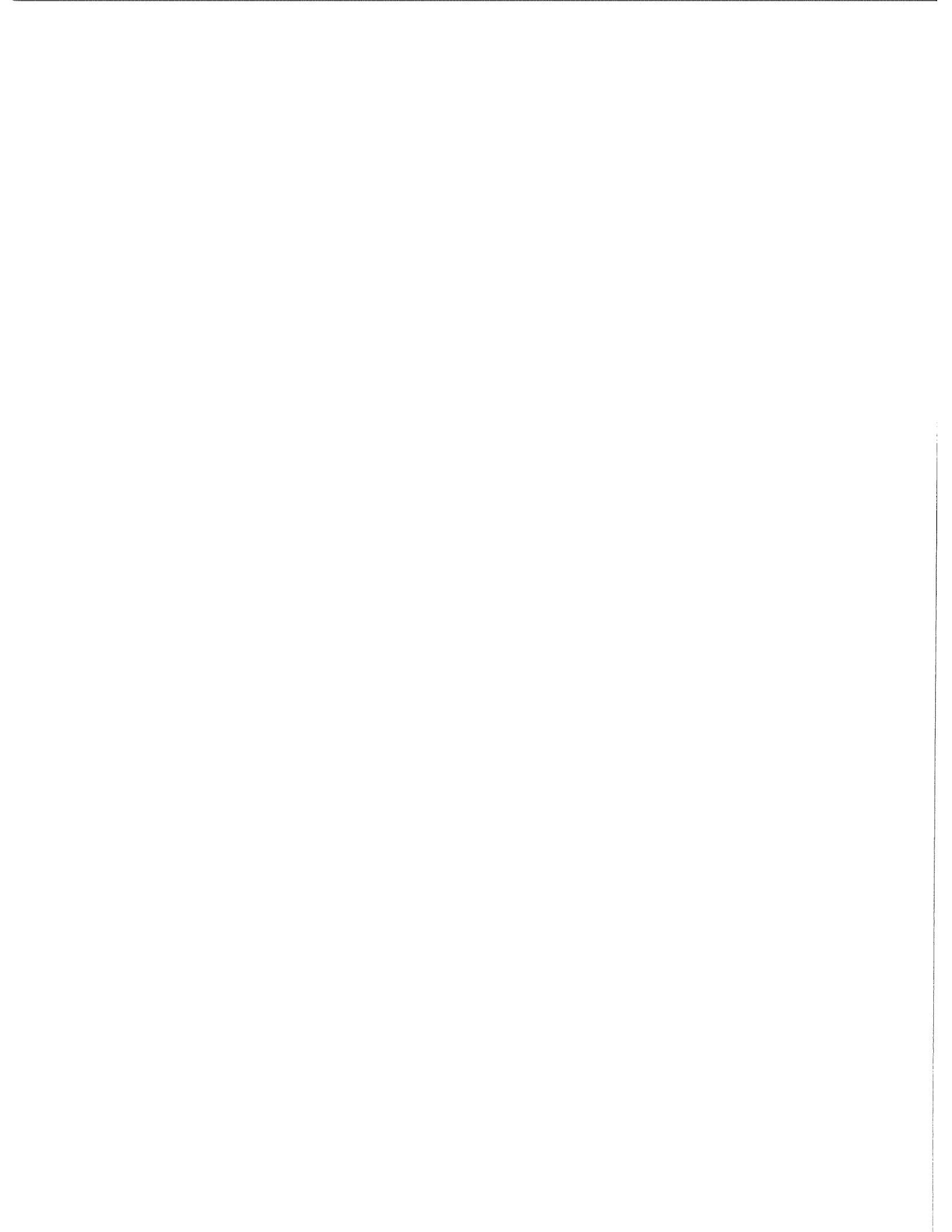
MINORITY REPORT

Although I agree with the greatest part of the Committee Report, I feel constrained to file this Minority Report with respect to the recommendation relating to the taxation of insurance companies and the Inheritance Tax revision.

I agree with the report of the Governor's Advisory Committee on Business Taxation that the Legislature should study further the complex issue of insurance taxation.

Our Inheritance Tax laws have not been revised in decades. I agree that the present exemptions for surviving spouses and children are too low. I believe that a thorough study should be made to determine Maine's revenue needs from this source and correlate these results with an equitable system to fairly tax the transfer of property upon death.

Representative John B. Cottrell



MINORITY REPORT

We respectfully decline to join in the report of the Committee and request that this "minority report" be attached to the Committee's final report. Many of the recommendations contained therein appear to be unwise, unrealistic, regressive, and punitive in their effect.

Property Taxes

The Committee recommends that "a uniform statewide property tax be established." It is difficult to see how such uniformity can be accomplished merely by establishing new state bureaucracies which will create additional costs to the taxpayers of Maine. Valuation of property varies with the locale and individuals closest to the property in question will continue to have the greatest knowledge concerning these matters. If the Committee feels that a statewide system is necessary in order to overcome possible constitutional infirmities in the manner in which educational operations are financed, we would recommend the institution of a statewide tax predicated upon state valuations wherein each municipality is assessed by the same rate.

We do agree with the Committee that the system of review and appeal concerning property taxes should be restructured. We do not, however, agree that the only answer is the establishment of an additional board. The entire system should be reviewed to ascertain what procedural steps are not necessary.

Real Estate Tax Exemption

The Committee has recommended that the exemption from local real property taxation be eliminated except for property used exclusively for "charitable, educational, religious, or scientific purposes by an organization which qualifies as an exempt organization under section 501 (c) (3) of the Internal Revenue Code of 1954 and property used exclusively for public purposes by federal, state, and local governments. Initially, the Committee fails to recommend any standard to be utilized in determining when property is being used "exclusively" for charitable purposes, etc. We would recommend that property be deemed to be exclusively utilized for charitable purposes unless the income derived from the use of such property would constitute income from an "unrelated trade or business" as that term is defined in section 513 of the Internal Revenue Code of 1954.

We do not concur with the Committee's recommendation that the exemption be limited to so-called 501 (c) (3) organizations. Historically, real estate exemptions have been granted so as to

allow organizations providing services for the common betterment to operate as inexpensively as possible. By limiting the exemption to those organizations qualifying under 501 (c) (3) we would impose real estate taxes upon the following types of entities:

1. Corporations organized under an Act of Congress, which are exempt from Federal income taxes. [501 (c)(1)]
2. Corporations organized for the exclusive purpose of holding title to property, collecting income therefrom, and turning over the entire amount thereof, less expenses, to an organization which itself is exempted under section 501 of the Internal Revenue Code. [501 (c) (2)]
3. Civic leagues or organizations not organized for profit but operated exclusively for the promotion of social welfare, or local associations of employees, the membership of which is limited to the employees of a designated person or persons in a particular municipality, and the net earnings of which are devoted exclusively to charitable, educational, or recreational purposes. [501 (c) (4)]
4. Labor, agricultural, or horticultural organizations. [501 (c) (5)]
5. Business leagues, chambers of commerce, etc. [501 (c) (6)]

This is not the entire list of the types of organizations which would be subjected to real estate taxes if the committee's recommendations were to be implemented. Why should an organization operated exclusively for the promotion of social welfare which devotes its earnings exclusively to charitable purposes be faced with taxation while a charitable organization would not? Such is exactly what would occur since the former is considered a 501 (c) (3) organization while the latter is a 501 (c) (4).

Throughout the course of the Committee's deliberations it was apparent that a great deal of concern was expressed over the tax exempt status of non-profit clubs operated for pleasure and fraternal beneficiary societies, order, or associations. If it is the Committee's latent intent to remove the tax exemptions from such entities, we would submit that they are recommending the use of a cannon where a pistol would do.

Many worthwhile non-profit organizations are in operation throughout the State of Maine. They provide necessary services to the citizens of Maine and have been able to continue such programs in the face of rising costs. Their operating funds

are derived from contributions of interested citizens and fees charged to recipients of the services they provide. To impose additional burdens upon these organizations is, in essence, to tell them to go out of business. We respectfully submit that such organizations pay their own way by the services they provide and should not have additional financial burdens placed upon them unless the State of Maine is willing to carry on such programs in the absence of these organizations. Therefore, we would recommend that all organizations exempt from taxation under section 501 and all subsections thereof of the Internal Revenue Code remain exempt from real property taxes.

Taxes on Business

The Committee report indicates that certain of its recommendations must be read together so that tax increases in some areas are balanced by decreases in other areas so that the system is more equitable while not placing additional burdens on taxpayers. We do not endorse the recommendation to eliminate the personal property tax on business inventories and stock in trade. We do, however, endorse the elimination of the sales and use tax on machinery used in manufacturing. We also endorse the recommendation to tax corporations on the basis of a progressive rate rather than the current flat rate of 4%. However, we wish to make it clear that such endorsement is made only so long as corporate taxes, even under a progressive system, are not increased more than is necessary to compensate for the elimination of the sales and use tax on machinery.

Bank Stock Tax

We would propose, as an alternative to the Bank Stock Tax, that the State Department of Taxation administer a program of personal property taxation whereby the State taxes the personal property of applicable banking institutions and then returns prorated amounts to each community on the basis of the value of the personal property owned by the bank which is located in that particular community.

Such a system would alleviate the problem of banking institutions having branches in many communities having to deal with many assessors, etc. Such dealings would be time consuming and would constitute an additional burden.

Personal Property Taxation of Insurance Companies and Blue Cross

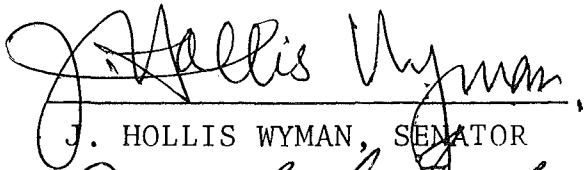
The Committee has, in our opinion, committed a serious error by placing Blue Cross in the same category with insurance companies for the purpose of taxing personal property. Unlike insurance companies, Maine Blue Cross and Blue Shield is a non-profit organization. The Act of Incorporation under which Associated Hospital Service of Maine was organized, and under which it operates, provides that the organization must have contracts with its providers of service (hospitals and physicians). The provider must guarantee to furnish benefits to members, as provided in subscribers contracts, in return for which the organization agrees to reimburse the provider under terms of the participation agreement. If Blue Cross has insufficient funds to meet the full payment agreed upon, providers agree to accept pro-rata amounts, according to the ability of Associated Hospital Service to pay.

It should be remembered that Associated Hospital Service is also different from the commercial carriers in other ways. Of their 440,000 members, 66,000 are Maine's elderly who look to them to provide benefit plans needed to pay the deductibles and co-insurance not covered under Medicare. Blue Cross has just announced that it will increase Companion Plan benefits on January 1, 1973 to compensate for Medicare benefit reductions caused by increased deductibles and co-insurance. This will be done without premium increase. Taxing elderly persons with limited income who are making an effort to stay off the Medicaid and welfare roles through purchase of Blue Cross Companion Plan to supplement Medicare benefits does not make good economic sense.

Secondly, we feel that a personal property tax on Maine's domestic insurance companies is discriminatory since it would not be imposed upon foreign carriers doing business in the state. The only vehicle available to tax foreign companies is the premiums tax. We must keep in mind that domestic companies employ many Maine citizens and should not be forced to pay additional taxes, including an increase in the premiums tax rate.

Committee on Taxation

We would also recommend that the Joint Standing Committee on Taxation of the Legislature be authorized and enabled by the Legislature to meet at times when the Legislature is not in session for the purposes of continuing review and analysis of the tax laws of the State. This Committee should be authorized to employ staff on a permanent basis. This Committee could seek such advisory assistance as it felt necessary and would be able to utilize more effectively the current departments of state government. The Legislature has evidenced that it has the ability to handle such duties while out of session. For example, the Joint Committee on Government Reorganization met with regularity when the Legislature was not in session and succeeded in accomplishing its goal because the Legislative Committee was involved at all stages of fact finding, drafting and implementation of Governmental reorganization.


J. HOLLIS WYMAN, SENATOR


ARMAND J. FORTIER, SENATOR


LOUIS F. FINEMORE, REPRESENTATIVE


ARTHUR F. STEDMAN