

# The Maine View

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## LD 1495: Frankenstein Tax Reform

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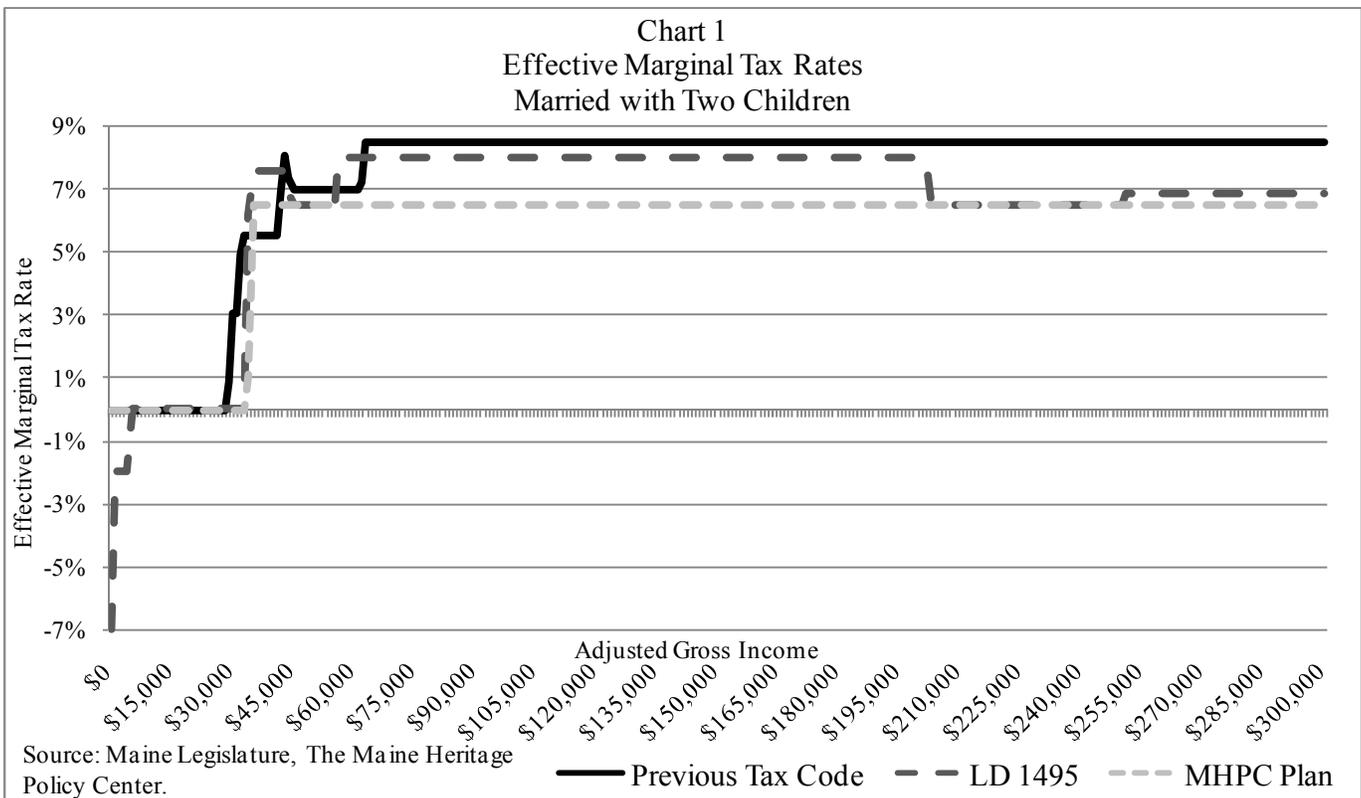
By J. Scott Moody

Since LD 1495, which replaced LD 1088, became the law of the land, everyone from the Governor on down has been crowing about the economic benefits of the lower, flat 6.5 percent marginal tax rate for most Mainers. Unfortunately, standard tax analysis demonstrates that other provisions in the controversial bill will result in most Mainers facing tax rates that are significantly lower in some cases and in other cases are far higher than the statutory 6.5 percent tax rate.

This analysis calculates the *effective marginal tax rate* (EMTR) under LD 1495. The EMTR is measured by taking the change in tax liability divided by the change in income. For example, a change in tax liability of \$80 per \$1,000 in income yields an EMTR of 8 percent. EMTR is important because work effort and entrepreneurship are determined on the margin. Put simply, people work less if the EMTR becomes punitively high.

Chart 1 and Table 1 plot the changes in the EMTR for income ranges, as measured by adjusted gross income (AGI), between \$0 and \$300,000 for a married couple with two children under prior law, LD 1495 and “The MHPC Plan” for calendar year 2010 (when LD 1495 takes effect). The analysis shows that this family will only have an EMTR of 6.5 percent if they earned income between \$46,000 and \$54,000 or between \$204,000 and \$250,000. If they earned income between \$56,000 and \$201,000 they will face an EMTR of 8 percent - only 0.5 percentage points less than previous law! Furthermore, if their earned income is less than \$33,000 they will face an EMTR that is zero or, more disturbingly, even negative.

In summary, LD 1495 is not a 6.5 percent flat rate as advertised. Maine taxpayers would be far better served if the state adopted a handful of meaningful changes to the tax code, as detailed in this report, in place of LD 1495.



*We the people of Maine...*

THE MAINE HERITAGE POLICY CENTER

Table 1  
Effective Marginal Tax Rates for a Married Couple with Two Children (Standard Deduction)  
Calendar Year 2010

Adjusted Gross Income	Effective Marginal Tax Rates			Tax Liability			Adjusted Gross Income	Effective Marginal Tax Rates			Tax Liability		
	Previous Law	Current Law (LD 1495)	Difference	Previous Law	Current Law (LD 1495)	Difference		Previous Law	Current Law (LD 1495)	Difference	Previous Law	Current Law (LD 1495)	Difference
\$0	0.00%	-7.00%	-7.00%	\$0	-\$70	-\$70	\$76,000	8.50%	8.00%	-0.50%	\$3,295	\$3,055	-\$240
\$2,000	0.00%	-2.00%	-2.00%	\$0	-\$110	-\$110	\$78,000	8.50%	8.00%	-0.50%	\$3,465	\$3,215	-\$250
\$4,000	0.00%	-2.00%	-2.00%	\$0	-\$150	-\$150	\$80,000	8.50%	8.00%	-0.50%	\$3,635	\$3,375	-\$260
\$6,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$82,000	8.50%	8.00%	-0.50%	\$3,805	\$3,535	-\$270
\$8,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$84,000	8.50%	8.00%	-0.50%	\$3,975	\$3,695	-\$280
\$10,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$86,000	8.50%	8.00%	-0.50%	\$4,145	\$3,855	-\$290
\$12,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$88,000	8.50%	8.00%	-0.50%	\$4,315	\$4,015	-\$300
\$14,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$90,000	8.50%	8.00%	-0.50%	\$4,485	\$4,175	-\$310
\$16,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$92,000	8.50%	8.00%	-0.50%	\$4,655	\$4,335	-\$320
\$18,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$94,000	8.50%	8.00%	-0.50%	\$4,825	\$4,495	-\$330
\$20,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$96,000	8.50%	8.00%	-0.50%	\$4,995	\$4,655	-\$340
\$22,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$98,000	8.50%	8.00%	-0.50%	\$5,165	\$4,815	-\$350
\$24,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$100,000	8.50%	8.00%	-0.50%	\$5,335	\$4,975	-\$360
\$26,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$102,000	8.50%	8.00%	-0.50%	\$5,505	\$5,135	-\$370
\$28,000	0.00%	0.00%	0.00%	\$0	-\$150	-\$150	\$104,000	8.50%	8.00%	-0.50%	\$5,675	\$5,295	-\$380
\$30,000	3.05%	0.00%	-3.05%	\$40	-\$150	-\$190	\$106,000	8.50%	8.00%	-0.50%	\$5,845	\$5,455	-\$390
\$32,000	4.93%	0.00%	-4.93%	\$119	-\$150	-\$269	\$108,000	8.50%	8.00%	-0.50%	\$6,015	\$5,615	-\$400
\$34,000	5.55%	6.18%	0.63%	\$231	-\$88	-\$319	\$110,000	8.50%	8.00%	-0.50%	\$6,185	\$5,775	-\$410
\$36,000	5.55%	7.55%	2.00%	\$342	\$63	-\$279	\$112,000	8.50%	8.00%	-0.50%	\$6,355	\$5,935	-\$420
\$38,000	5.55%	7.55%	2.00%	\$453	\$214	-\$239	\$114,000	8.50%	8.00%	-0.50%	\$6,525	\$6,095	-\$430
\$40,000	5.55%	7.55%	2.00%	\$564	\$365	-\$199	\$116,000	8.50%	8.00%	-0.50%	\$6,695	\$6,255	-\$440
\$42,000	6.93%	7.55%	0.63%	\$689	\$516	-\$173	\$118,000	8.50%	8.00%	-0.50%	\$6,865	\$6,415	-\$450
\$44,000	7.34%	6.84%	-0.50%	\$843	\$660	-\$183	\$120,000	8.50%	8.00%	-0.50%	\$7,035	\$6,575	-\$460
\$46,000	7.00%	6.50%	-0.50%	\$983	\$790	-\$193	\$122,000	8.50%	8.00%	-0.50%	\$7,205	\$6,735	-\$470
\$48,000	7.00%	6.50%	-0.50%	\$1,123	\$920	-\$203	\$124,000	8.50%	8.00%	-0.50%	\$7,375	\$6,895	-\$480
\$50,000	7.00%	6.50%	-0.50%	\$1,263	\$1,050	-\$213	\$126,000	8.50%	8.00%	-0.50%	\$7,545	\$7,055	-\$490
\$52,000	7.00%	6.50%	-0.50%	\$1,403	\$1,180	-\$223	\$128,000	8.50%	8.00%	-0.50%	\$7,715	\$7,215	-\$500
\$54,000	7.00%	6.50%	-0.50%	\$1,543	\$1,310	-\$233	\$130,000	8.50%	8.00%	-0.50%	\$7,885	\$7,375	-\$510
\$56,000	7.00%	8.00%	1.00%	\$1,683	\$1,455	-\$228	\$132,000	8.50%	8.00%	-0.50%	\$8,055	\$7,535	-\$520
\$58,000	7.00%	8.00%	1.00%	\$1,823	\$1,615	-\$208	\$134,000	8.50%	8.00%	-0.50%	\$8,225	\$7,695	-\$530
\$60,000	7.00%	8.00%	1.00%	\$1,963	\$1,775	-\$188	\$136,000	8.50%	8.00%	-0.50%	\$8,395	\$7,855	-\$540
\$62,000	7.22%	8.00%	0.78%	\$2,105	\$1,935	-\$170	\$138,000	8.50%	8.00%	-0.50%	\$8,565	\$8,015	-\$550
\$64,000	8.50%	8.00%	-0.50%	\$2,275	\$2,095	-\$180	\$140,000	8.50%	8.00%	-0.50%	\$8,735	\$8,175	-\$560
\$66,000	8.50%	8.00%	-0.50%	\$2,445	\$2,255	-\$190	\$142,000	8.50%	8.00%	-0.50%	\$8,905	\$8,335	-\$570
\$68,000	8.50%	8.00%	-0.50%	\$2,615	\$2,415	-\$200	\$144,000	8.50%	8.00%	-0.50%	\$9,075	\$8,495	-\$580
\$70,000	8.50%	8.00%	-0.50%	\$2,785	\$2,575	-\$210	\$146,000	8.50%	8.00%	-0.50%	\$9,245	\$8,655	-\$590
\$72,000	8.50%	8.00%	-0.50%	\$2,955	\$2,735	-\$220	\$148,000	8.50%	8.00%	-0.50%	\$9,415	\$8,815	-\$600
\$74,000	8.50%	8.00%	-0.50%	\$3,125	\$2,895	-\$230	\$150,000	8.50%	8.00%	-0.50%	\$9,585	\$8,975	-\$610

Source: Maine Legislature, The Maine Heritage Policy Center.

Table 1 Continued  
 Effective Marginal Tax Rates for a Married Couple with Two Children (Standard Deduction)  
 Calendar Year 2010

Adjusted Gross Income	Effective Marginal Tax Rates			Tax Liability			Adjusted Gross Income	Effective Marginal Tax Rates			Tax Liability		
	Previous Law	Current Law (LD 1495)	Difference	Previous Law	Current Law (LD 1495)	Difference		Previous Law	Current Law (LD 1495)	Difference	Previous Law	Current Law (LD 1495)	Difference
<b>\$152,000</b>	8.50%	8.00%	-0.50%	\$9,755	\$9,135	-\$620	<b>\$226,000</b>	8.50%	6.50%	-2.00%	\$16,045	\$14,690	-\$1,355
<b>\$154,000</b>	8.50%	8.00%	-0.50%	\$9,925	\$9,295	-\$630	<b>\$228,000</b>	8.50%	6.50%	-2.00%	\$16,215	\$14,820	-\$1,395
<b>\$156,000</b>	8.50%	8.00%	-0.50%	\$10,095	\$9,455	-\$640	<b>\$230,000</b>	8.50%	6.50%	-2.00%	\$16,385	\$14,950	-\$1,435
<b>\$158,000</b>	8.50%	8.00%	-0.50%	\$10,265	\$9,615	-\$650	<b>\$232,000</b>	8.50%	6.50%	-2.00%	\$16,555	\$15,080	-\$1,475
<b>\$160,000</b>	8.50%	8.00%	-0.50%	\$10,435	\$9,775	-\$660	<b>\$234,000</b>	8.50%	6.50%	-2.00%	\$16,725	\$15,210	-\$1,515
<b>\$162,000</b>	8.50%	8.00%	-0.50%	\$10,605	\$9,935	-\$670	<b>\$236,000</b>	8.50%	6.50%	-2.00%	\$16,895	\$15,340	-\$1,555
<b>\$164,000</b>	8.50%	8.00%	-0.50%	\$10,775	\$10,095	-\$680	<b>\$238,000</b>	8.50%	6.50%	-2.00%	\$17,065	\$15,470	-\$1,595
<b>\$166,000</b>	8.50%	8.00%	-0.50%	\$10,945	\$10,255	-\$690	<b>\$240,000</b>	8.50%	6.50%	-2.00%	\$17,235	\$15,600	-\$1,635
<b>\$168,000</b>	8.50%	8.00%	-0.50%	\$11,115	\$10,415	-\$700	<b>\$242,000</b>	8.50%	6.50%	-2.00%	\$17,405	\$15,730	-\$1,675
<b>\$170,000</b>	8.50%	8.00%	-0.50%	\$11,285	\$10,575	-\$710	<b>\$244,000</b>	8.50%	6.50%	-2.00%	\$17,575	\$15,860	-\$1,715
<b>\$172,000</b>	8.50%	8.00%	-0.50%	\$11,455	\$10,735	-\$720	<b>\$246,000</b>	8.50%	6.50%	-2.00%	\$17,745	\$15,990	-\$1,755
<b>\$174,000</b>	8.50%	8.00%	-0.50%	\$11,625	\$10,895	-\$730	<b>\$248,000</b>	8.50%	6.50%	-2.00%	\$17,915	\$16,120	-\$1,795
<b>\$176,000</b>	8.50%	8.00%	-0.50%	\$11,795	\$11,055	-\$740	<b>\$250,000</b>	8.50%	6.50%	-2.00%	\$18,085	\$16,250	-\$1,835
<b>\$178,000</b>	8.50%	8.00%	-0.50%	\$11,965	\$11,215	-\$750	<b>\$252,000</b>	8.50%	6.85%	-1.65%	\$18,255	\$16,387	-\$1,868
<b>\$180,000</b>	8.50%	8.00%	-0.50%	\$12,135	\$11,375	-\$760	<b>\$254,000</b>	8.50%	6.85%	-1.65%	\$18,425	\$16,524	-\$1,901
<b>\$182,000</b>	8.50%	8.00%	-0.50%	\$12,305	\$11,535	-\$770	<b>\$256,000</b>	8.50%	6.85%	-1.65%	\$18,595	\$16,661	-\$1,934
<b>\$184,000</b>	8.50%	8.00%	-0.50%	\$12,475	\$11,695	-\$780	<b>\$258,000</b>	8.50%	6.85%	-1.65%	\$18,765	\$16,798	-\$1,967
<b>\$186,000</b>	8.50%	8.00%	-0.50%	\$12,645	\$11,855	-\$790	<b>\$260,000</b>	8.50%	6.85%	-1.65%	\$18,935	\$16,935	-\$2,000
<b>\$188,000</b>	8.50%	8.00%	-0.50%	\$12,815	\$12,015	-\$800	<b>\$262,000</b>	8.50%	6.85%	-1.65%	\$19,105	\$17,072	-\$2,033
<b>\$190,000</b>	8.50%	8.00%	-0.50%	\$12,985	\$12,175	-\$810	<b>\$264,000</b>	8.50%	6.85%	-1.65%	\$19,275	\$17,209	-\$2,066
<b>\$192,000</b>	8.50%	8.00%	-0.50%	\$13,155	\$12,335	-\$820	<b>\$266,000</b>	8.50%	6.85%	-1.65%	\$19,445	\$17,346	-\$2,099
<b>\$194,000</b>	8.50%	8.00%	-0.50%	\$13,325	\$12,495	-\$830	<b>\$268,000</b>	8.50%	6.85%	-1.65%	\$19,615	\$17,483	-\$2,132
<b>\$196,000</b>	8.50%	8.00%	-0.50%	\$13,495	\$12,655	-\$840	<b>\$270,000</b>	8.50%	6.85%	-1.65%	\$19,785	\$17,620	-\$2,165
<b>\$198,000</b>	8.50%	8.00%	-0.50%	\$13,665	\$12,815	-\$850	<b>\$272,000</b>	8.50%	6.85%	-1.65%	\$19,955	\$17,757	-\$2,198
<b>\$200,000</b>	8.50%	8.00%	-0.50%	\$13,835	\$12,975	-\$860	<b>\$274,000</b>	8.50%	6.85%	-1.65%	\$20,125	\$17,894	-\$2,231
<b>\$202,000</b>	8.50%	7.50%	-1.00%	\$14,005	\$13,130	-\$875	<b>\$276,000</b>	8.50%	6.85%	-1.65%	\$20,295	\$18,031	-\$2,264
<b>\$204,000</b>	8.50%	6.50%	-2.00%	\$14,175	\$13,260	-\$915	<b>\$278,000</b>	8.50%	6.85%	-1.65%	\$20,465	\$18,168	-\$2,297
<b>\$206,000</b>	8.50%	6.50%	-2.00%	\$14,345	\$13,390	-\$955	<b>\$280,000</b>	8.50%	6.85%	-1.65%	\$20,635	\$18,305	-\$2,330
<b>\$208,000</b>	8.50%	6.50%	-2.00%	\$14,515	\$13,520	-\$995	<b>\$282,000</b>	8.50%	6.85%	-1.65%	\$20,805	\$18,442	-\$2,363
<b>\$210,000</b>	8.50%	6.50%	-2.00%	\$14,685	\$13,650	-\$1,035	<b>\$284,000</b>	8.50%	6.85%	-1.65%	\$20,975	\$18,579	-\$2,396
<b>\$212,000</b>	8.50%	6.50%	-2.00%	\$14,855	\$13,780	-\$1,075	<b>\$286,000</b>	8.50%	6.85%	-1.65%	\$21,145	\$18,716	-\$2,429
<b>\$214,000</b>	8.50%	6.50%	-2.00%	\$15,025	\$13,910	-\$1,115	<b>\$288,000</b>	8.50%	6.85%	-1.65%	\$21,315	\$18,853	-\$2,462
<b>\$216,000</b>	8.50%	6.50%	-2.00%	\$15,195	\$14,040	-\$1,155	<b>\$290,000</b>	8.50%	6.85%	-1.65%	\$21,485	\$18,990	-\$2,495
<b>\$218,000</b>	8.50%	6.50%	-2.00%	\$15,365	\$14,170	-\$1,195	<b>\$292,000</b>	8.50%	6.85%	-1.65%	\$21,655	\$19,127	-\$2,528
<b>\$220,000</b>	8.50%	6.50%	-2.00%	\$15,535	\$14,300	-\$1,235	<b>\$294,000</b>	8.50%	6.85%	-1.65%	\$21,825	\$19,264	-\$2,561
<b>\$222,000</b>	8.50%	6.50%	-2.00%	\$15,705	\$14,430	-\$1,275	<b>\$296,000</b>	8.50%	6.85%	-1.65%	\$21,995	\$19,401	-\$2,594
<b>\$224,000</b>	8.50%	6.50%	-2.00%	\$15,875	\$14,560	-\$1,315	<b>\$298,000</b>	8.50%	6.85%	-1.65%	\$22,165	\$19,538	-\$2,627
							<b>\$300,000</b>	8.50%	6.85%	-1.65%	\$22,335	\$19,675	-\$2,660

Source: Maine Legislature, The Maine Heritage Policy Center.

**How to Fix LD 1495**

There are five simple steps to making LD 1495 into a true 6.5 percent flat rate tax:

1. **Eliminate the 0.35 percent tax surcharge on income earned over \$250,000.** The tax surcharge was put into place by Governor Baldacci as a precondition for his support. This blatant “punish success” ideology simply has no place in a well-designed income tax that Maine needs and deserves.
2. **Eliminate the phase-out of the household tax credit.** The household tax credit takes the place of current deductions and exemptions. For the family of four illustrated in this study, the total household credit is worth \$2,200 (\$1,200 as a married, filing jointly taxpayer and another \$250 per person). This means that this household will pay no income taxes until their tax liability exceeds the \$2,200 household credit - which occurs at approximately \$34,000 of income.

Unfortunately, the household tax credit phase-out reduces the credit by \$15 for every additional \$1,000 earned (a 1.5 percent rate) over \$55,000 (for a married, filing jointly

taxpayer). As a result, if the household earns another \$1,000 (to \$56,000), they will pay an additional \$65 in taxes (6.5 percent of \$1,000) and lose \$15 of their \$2,200 household tax credit (now worth \$2,185). Combined, this amounts to an increase in their tax liability of \$80 equally an EMTR of 8 percent (\$80 divided by \$1,000). The 8 percent EMTR nearly wipes out the benefits of LD 1495 for many Mainers.

3. **Eliminate the refundability of the household tax credit.** The household tax credit is refundable if the credit exceeds a taxpayer’s tax liability by up to \$70 (for a married, filing jointly taxpayer). For example, this means that if their household’s tax liability was \$1,000 but their household tax credit was worth \$2,200 then they would owe -\$1,200. The state will send a check for \$70 (called a “refund”) of the -\$1,200 tax liability. This refundability creates a -7 percent EMTR and, perhaps more disturbing, also transforms the income tax code into a welfare program.
4. **Eliminate the Earned Income Tax Credit (EITC), especially its refundability.** Governor Baldacci also insisted the EITC be refundable up to \$150 (for a married, filing jointly taxpayer). Unfortunately, the refundability only

**Table 1 Continued**  
**Effective Marginal Tax Rate for a Married Couple with Two Children (Standard Deduction)**  
**Calendar Year 2010**

Adjusted Gross Income	Effective Marginal Tax Rate			Tax Liability			Adjusted Gross Income	Effective Marginal Tax Rate			Tax Liability		
	Previous Law	Current Law (LD 1495)	Difference	Previous Law	Current Law (LD 1495)	Difference		Previous Law	Current Law (LD 1495)	Difference	Previous Law	Current Law (LD 1495)	Difference
\$305,000	8.50%	6.85%	-1.65%	\$22,760	\$20,018	-\$2,742	\$405,000	8.50%	6.85%	-1.65%	\$31,260	\$26,868	-\$4,392
\$310,000	8.50%	6.85%	-1.65%	\$23,185	\$20,360	-\$2,825	\$410,000	8.50%	6.85%	-1.65%	\$31,685	\$27,210	-\$4,475
\$315,000	8.50%	6.85%	-1.65%	\$23,610	\$20,703	-\$2,907	\$415,000	8.50%	6.85%	-1.65%	\$32,110	\$27,553	-\$4,557
\$320,000	8.50%	6.85%	-1.65%	\$24,035	\$21,045	-\$2,990	\$420,000	8.50%	6.85%	-1.65%	\$32,535	\$27,895	-\$4,640
\$325,000	8.50%	6.85%	-1.65%	\$24,460	\$21,388	-\$3,072	\$425,000	8.50%	6.85%	-1.65%	\$32,960	\$28,238	-\$4,722
\$330,000	8.50%	6.85%	-1.65%	\$24,885	\$21,730	-\$3,155	\$430,000	8.50%	6.85%	-1.65%	\$33,385	\$28,580	-\$4,805
\$335,000	8.50%	6.85%	-1.65%	\$25,310	\$22,073	-\$3,237	\$435,000	8.50%	6.85%	-1.65%	\$33,810	\$28,923	-\$4,887
\$340,000	8.50%	6.85%	-1.65%	\$25,735	\$22,415	-\$3,320	\$440,000	8.50%	6.85%	-1.65%	\$34,235	\$29,265	-\$4,970
\$345,000	8.50%	6.85%	-1.65%	\$26,160	\$22,758	-\$3,402	\$445,000	8.50%	6.85%	-1.65%	\$34,660	\$29,608	-\$5,052
\$350,000	8.50%	6.85%	-1.65%	\$26,585	\$23,100	-\$3,485	\$450,000	8.50%	6.85%	-1.65%	\$35,085	\$29,950	-\$5,135
\$355,000	8.50%	6.85%	-1.65%	\$27,010	\$23,443	-\$3,567	\$455,000	8.50%	6.85%	-1.65%	\$35,510	\$30,293	-\$5,217
\$360,000	8.50%	6.85%	-1.65%	\$27,435	\$23,785	-\$3,650	\$460,000	8.50%	6.85%	-1.65%	\$35,935	\$30,635	-\$5,300
\$365,000	8.50%	6.85%	-1.65%	\$27,860	\$24,128	-\$3,732	\$465,000	8.50%	6.85%	-1.65%	\$36,360	\$30,978	-\$5,382
\$370,000	8.50%	6.85%	-1.65%	\$28,285	\$24,470	-\$3,815	\$470,000	8.50%	6.85%	-1.65%	\$36,785	\$31,320	-\$5,465
\$375,000	8.50%	6.85%	-1.65%	\$28,710	\$24,813	-\$3,897	\$475,000	8.50%	6.85%	-1.65%	\$37,210	\$31,663	-\$5,547
\$380,000	8.50%	6.85%	-1.65%	\$29,135	\$25,155	-\$3,980	\$480,000	8.50%	6.85%	-1.65%	\$37,635	\$32,005	-\$5,630
\$385,000	8.50%	6.85%	-1.65%	\$29,560	\$25,498	-\$4,062	\$485,000	8.50%	6.85%	-1.65%	\$38,060	\$32,348	-\$5,712
\$390,000	8.50%	6.85%	-1.65%	\$29,985	\$25,840	-\$4,145	\$490,000	8.50%	6.85%	-1.65%	\$38,485	\$32,690	-\$5,795
\$395,000	8.50%	6.85%	-1.65%	\$30,410	\$26,183	-\$4,227	\$495,000	8.50%	6.85%	-1.65%	\$38,910	\$33,033	-\$5,877
\$400,000	8.50%	6.85%	-1.65%	\$30,835	\$26,525	-\$4,310	\$500,000	8.50%	6.85%	-1.65%	\$39,335	\$33,375	-\$5,960

Source: Maine Legislature, The Maine Heritage Policy Center.

makes a bad part of the tax code even worse.  
<sup>[1]</sup>

Maine’s EITC piggy-backs on the federal EITC by allowing 5 percent of the federal EITC to be used by Maine taxpayers. This has the effect of bringing the negative baggage of the federal EITC to Maine.

The fatal flaw in the design of the federal EITC is that it has a 40 percent phase-in rate for income earned less than \$12,060 and a 21.06 percent phase-out rate for income earned between \$18,750 and \$41,656.<sup>[2]</sup> In the phase-in range, this means that a taxpayer’s EITC increases by 40 cents for every extra \$1 earned—which creates a negative EMTR because it is refundable. On the other hand, in the phase-out range, this means that a taxpayer’s EITC decreases by 21.06 cents for every extra \$1 earned—which creates a positive EMTR since the taxpayer is receiving a smaller benefit. As shown in Chart 1 and Table 2, the added negative EMTR and positive EMTR for income earned below \$41,656 is due to the “importation” of this roller-coaster effect from the federal tax code.

The simplest way to fix the EITC and Governor Baldacci’s new refundability is to just eliminate it altogether.

5. **Eliminate the phase-out of the elderly credit.** While not shown in this analysis, a married elderly couple earning between \$52,000 and \$58,000 face another 2 percentage points added to their EMTR due to the phase-out of the \$120 elderly tax credit which is meant to provide tax relief to those on a fixed income. However, the phase-out creates an EMTR of up to 10 percent which is higher than that faced by younger Mainers! Is this anyway to treat one of Maine’s fastest growing age cohorts?

**One Other Fix:**

- **Immediately allow for inflation indexing of the household tax credit amount.** LD 1495 currently calls for the indexing of the household tax credit to begin in CY 2014. This waiting period amounts to a hidden “inflation tax” that will raise taxes on Mainers. If revenue-neutrality only applies to the first year of the LD 1495, it makes you wonder what other hidden tax increases lie in wait?

Adjusted Gross Income	“The MHPC Plan”		Difference with Previous Law		Difference with Current Law (LD 1495)	
	Tax Liability	Effective Marginal Tax Rate	Difference	Previous Law	Current Law (LD 1495)	Difference
\$0	\$0	0.00%	\$0	0.00%	(\$70)	-7.00%
\$10,000	\$0	0.00%	\$0	0.00%	(\$150)	0.00%
\$20,000	\$0	0.00%	\$0	0.00%	(\$150)	0.00%
\$30,000	\$0	0.00%	\$40	3.05%	(\$150)	0.00%
\$40,000	\$400	6.50%	\$164	-0.95%	(\$35)	1.05%
\$50,000	\$1,050	6.50%	\$213	0.50%	\$0	0.00%
\$60,000	\$1,700	6.50%	\$263	0.50%	\$75	1.50%
\$70,000	\$2,350	6.50%	\$435	2.00%	\$225	1.50%
\$80,000	\$3,000	6.50%	\$635	2.00%	\$375	1.50%
\$90,000	\$3,650	6.50%	\$835	2.00%	\$525	1.50%
\$100,000	\$4,300	6.50%	\$1,035	2.00%	\$675	1.50%
\$110,000	\$4,950	6.50%	\$1,235	2.00%	\$825	1.50%
\$120,000	\$5,600	6.50%	\$1,435	2.00%	\$975	1.50%
\$130,000	\$6,250	6.50%	\$1,635	2.00%	\$1,125	1.50%
\$140,000	\$6,900	6.50%	\$1,835	2.00%	\$1,275	1.50%
\$150,000	\$7,550	6.50%	\$2,035	2.00%	\$1,425	1.50%
\$160,000	\$8,200	6.50%	\$2,235	2.00%	\$1,575	1.50%
\$170,000	\$8,850	6.50%	\$2,435	2.00%	\$1,725	1.50%
\$180,000	\$9,500	6.50%	\$2,635	2.00%	\$1,875	1.50%
\$190,000	\$10,150	6.50%	\$2,835	2.00%	\$2,025	1.50%
\$200,000	\$10,800	6.50%	\$3,035	2.00%	\$2,175	1.50%
\$210,000	\$11,450	6.50%	\$3,235	2.00%	\$2,200	0.00%
\$220,000	\$12,100	6.50%	\$3,435	2.00%	\$2,200	0.00%
\$230,000	\$12,750	6.50%	\$3,635	2.00%	\$2,200	0.00%
\$240,000	\$13,400	6.50%	\$3,835	2.00%	\$2,200	0.00%
\$250,000	\$14,050	6.50%	\$4,035	2.00%	\$2,200	0.00%
\$260,000	\$14,700	6.50%	\$4,235	2.00%	\$2,235	0.35%
\$270,000	\$15,350	6.50%	\$4,435	2.00%	\$2,270	0.35%
\$280,000	\$16,000	6.50%	\$4,635	2.00%	\$2,305	0.35%
\$290,000	\$16,650	6.50%	\$4,835	2.00%	\$2,340	0.35%
\$300,000	\$17,300	6.50%	\$5,035	2.00%	\$2,375	0.35%
\$310,000	\$17,950	6.50%	\$5,235	2.00%	\$2,410	0.35%
\$320,000	\$18,600	6.50%	\$5,435	2.00%	\$2,445	0.35%
\$330,000	\$19,250	6.50%	\$5,635	2.00%	\$2,480	0.35%
\$340,000	\$19,900	6.50%	\$5,835	2.00%	\$2,515	0.35%
\$350,000	\$20,550	6.50%	\$6,035	2.00%	\$2,550	0.35%
\$360,000	\$21,200	6.50%	\$6,235	2.00%	\$2,585	0.35%
\$370,000	\$21,850	6.50%	\$6,435	2.00%	\$2,620	0.35%
\$380,000	\$22,500	6.50%	\$6,635	2.00%	\$2,655	0.35%
\$390,000	\$23,150	6.50%	\$6,835	2.00%	\$2,690	0.35%
\$400,000	\$23,800	6.50%	\$7,035	2.00%	\$2,725	0.35%
\$410,000	\$24,450	6.50%	\$7,235	2.00%	\$2,760	0.35%
\$420,000	\$25,100	6.50%	\$7,435	2.00%	\$2,795	0.35%
\$430,000	\$25,750	6.50%	\$7,635	2.00%	\$2,830	0.35%
\$440,000	\$26,400	6.50%	\$7,835	2.00%	\$2,865	0.35%
\$450,000	\$27,050	6.50%	\$8,035	2.00%	\$2,900	0.35%
\$460,000	\$27,700	6.50%	\$8,235	2.00%	\$2,935	0.35%
\$470,000	\$28,350	6.50%	\$8,435	2.00%	\$2,970	0.35%
\$480,000	\$29,000	6.50%	\$8,635	2.00%	\$3,005	0.35%
\$490,000	\$29,650	6.50%	\$8,835	2.00%	\$3,040	0.35%
\$500,000	\$30,300	6.50%	\$9,035	2.00%	\$3,075	0.35%

Note: In the "Difference" column, a negative value means the MHPC plan is higher while a positive value means the MHPC plan is lower.  
 Source: Maine Legislature, The Maine Heritage Policy Center.

### The MHPC plan

Table 2 compares the previous tax law, LD 1495 with “The MHPC Plan” which incorporates the fixes stated previously. These fixes will create a true flat rate whereby the statutory marginal tax rate of 6.5 percent exactly equals the effective marginal tax rate of 6.5 percent, thereby eliminating gimmicks like tax surcharges, refundability and phase-ins and phase-outs.

Keep in mind, however, The MHPC Plan is meant only to fix the income tax rate portion of LD 1495. There are other problems within the income and sales tax portions of LD 1495 that are not included in this study.

### Conclusion

This analysis shows that the so-called 6.5 percent flat rate in LD 1495 is illusory. It would have been much easier and simpler to have just lowered the top marginal rate of 8.5 percent to 6.5 percent. Instead, the Legislature and Governor created this Frankenstein monster filled with gimmicks such as the tax surcharge, refundability of the household tax credit and EITC and phase-out of the household tax credit.<sup>[3]</sup>

Of course, some of these elements were necessary to insure that LD 1495 was “revenue neutral.” The result, however, is that the overall effectiveness of LD 1495 in boosting Maine’s economy must be called into question, especially in light of the higher sales tax rate on a multitude of goods and services and compliance costs.<sup>[4]</sup>

Much of this uncertainty might have been avoided if the tax plan was a genuine tax cut as well as tax reform. A first step toward this goal would be to enact “The MHPC Plan” with these five suggested fixes and without current or future offsetting tax increases.

### Notes and Sources:

- [1] And oddly, the EITC and household credit are both capped at -\$150 which essentially negates the household credit.
- [2] Thanks to Patrick Fleenor at the Tax Foundation for providing estimates for the federal EITC values in CY 2010.
- [3] Thanks to the Maine Revenue Service, taxpayers can calculate their own EMTR by using their on-line tax calculator. <http://www.maine.gov/revenue/incomeestate/1040/taxreformindividual.htm>
- [4] For more on sales tax compliance burdens, especially on Maine’s small businesses, see: <http://www.maineconomy.org/library/resources/152.pdf>

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