

STATE OF MAINE  
DEPARTMENT OF ADMINISTRATIVE AND FINANCIAL SERVICES  
MAINE REVENUE SERVICES  
OFFICE OF TAX POLICY

Date: May 3, 2017  
To: Joint Committee on Taxation  
From: Michael J. Allen, Associate Commissioner, Tax Policy, DAFS  
Subject: Local Option Sales Tax Bills (LDs 433, 741, 1230, 1265, & 1522)

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In recent years many bills have been submitted to the Legislature proposing to allow Maine municipalities to impose a "local option" sales tax collected and administered by the State in the same manner as the sales and use tax imposed by Title 36, Part 3. This trend has continued into the current session. Most of the bills in question share several important common elements and raise similar concerns from the perspectives of tax policy, tax administration, and statutory drafting. I am therefore taking this opportunity to highlight some of these concerns for the Taxation Committee. Many of the concerns will have been shared by the State Tax Assessor with the Committee over the years in memoranda prepared in connection with particular bills.

Maine Revenue Services (MRS) staff and I will be happy to help the Committee with any follow-up questions. In the event you move forward with a local option sales tax bill, we will be available to help in the drafting process. The major concerns we have identified are as follows:

**1. Timing and Cost of Implementation.** These bills typically require a municipality to notify the State Tax Assessor at least 90 days before a local option sales tax becomes effective and contain no limitation on how often a municipality may implement or discontinue a local option tax. Ninety days is not nearly enough time. Retailers need to update point of sale and accounting systems. Some retailers may not have the ability to easily program multiple tax rates into their current point of sale systems. MRS needs to update accounting, noticing, and billing systems; electronic filing applications; tax returns; and guidance documents. At least 6 months advance notice would be required before the initial operation of such a system; we strongly recommend 12 months or more. To ease the burden on retailers and MRS, local option tax changes should become effective at the beginning of a calendar year in order to minimize reporting confusion, complexity and administrative costs. An alternative approach would be to have the Legislature annually enact new municipal levies where standardized effective dates and any necessary appropriations could be specified. Another option for the Committee to consider is requiring that at least one year elapse between changes in a municipality's choice to implement the local option tax. ***MRS estimates a cost of at least \$750,000 with ongoing annual costs to implement a local option tax program.***

**2. Multiple Tax Rates.** Most of the bills would allow a variety of local sales tax rates to be adopted. Many allow a rate of "no more than" 1%. MRS strongly recommends that only one rate be allowed. Allowing implementation of multiple rates across municipalities greatly increases the complexity of administering a local option tax for retailers, participating municipalities, and the State. This problem would be particularly difficult if the statute were drafted so as to include a local option use tax in addition to the sales tax.

Example of the potential complexity a local option tax could create:

Assume a contractor that is also a retailer is located in a municipality with no local option tax. The contractor purchases resale inventory in a municipality that has a local option tax of .05%. Materials are removed from inventory to be installed into real property located in a municipality with a local option tax of .02%. The contractor will need to determine which local rate applies: 0% (where the item was removed from inventory), .05% (where the purchase was made), or .02% (where the item was used). This example becomes even more complex if one or more of the municipalities has enacted a seasonal local option tax.

**3. Inconsistent tax base.** Some of the bills would allow a municipality that adopts a local option sales tax to choose to not impose the tax on certain types of sales. LD 1522, introduced this session would allow municipalities to choose to exempt single transactions of up to \$100. LD 1265 would prohibit imposing tax on aircraft, furniture, machinery and equipment used in production, other items used in production, motor vehicles, watercraft, and major household appliances. Allowing municipalities to establish varying tax bases adds complexity and difficulty for retailers to comply, increases complexity in administration for MRS, and adds confusion for consumers and may only serve to shift consumption from one municipality to another. MRS recommends any local option tax be imposed on the same tax base as the State sales and use tax.

**4. Inadequate definitions.** The bills often use terms that are either not defined or not well defined for administration purposes. For example, LD 1265 introduced this session prohibits a local option tax on major household appliances purchased for more than \$500. "Major household appliance" is defined as any "piece of equipment" that is used for "a specific purpose in the home". Without a more specific definition, MRS will be in a position of developing guidance to explain whether this includes only traditional home appliances (refrigerators, washers, dryers, stoves, dishwashers, etc.) or is broader to include equipment such as an exercise machine or wide-screen television.

**5. Unclear application language.** The bills typically define the local option tax base as "those items subject to sales taxation under this Part", meaning Part 3 of Title 36 which addresses sales and use taxes. There are several services that are also subject to sales taxation. Language referencing "items" implies services are not to be part of the local option sales tax base. The bills often do not address use tax. As noted above, MRS recommends the tax base for any local option tax be the same as the State sales and use tax base.

**6. Application of revenues.** The bills require the State Tax Assessor to identify the amount of revenue attributable to each participating municipality, subtract the costs of administration, and certify the net amount to the Treasurer for distribution to each municipality. It is unclear whether "revenue attributable" to participating municipalities is the amounts reported as due or amounts actually paid over to MRS by retailers. There are also outstanding questions on how amended or adjusted tax returns are to be accounted for. Furthermore, if a retailer collects a mix of both state and local sales taxes, and becomes indebted to the state due to untimely transmission of the collected taxes, how are payments to be apportioned to the state and the municipality or municipalities where the retailer operates?

Retailers file returns by the 15th of the month following their respective reporting period. MRS needs adequate time to aggregate the data filed by retailers before reporting to the Treasurer.

Apportioning costs among electing municipalities will be administratively difficult. MRS is set up to administer taxes on an aggregated statewide basis. An appropriation of funds should be made to cover the initial cost of creating a local option tax. Otherwise, the initial cost may never be recouped from the municipalities.

**7. Confidentiality.** Reporting of revenues in smaller communities raises concerns of taxpayer confidentiality. Municipalities may be able to easily determine the gross sales of individual businesses based on the amount of local option taxes returned to that municipality.

**8. Constitutionality.** MRS' legal review to date suggests that local option tax legislation poses a genuine issue with respect to delegation of the Legislature's taxing authority under Article IX, Section 9 of the Maine Constitution ("The Legislature shall never, in any manner, suspend or surrender the power of taxation.").

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