



SEN. JUSTIN CHENETTE, SENATE CHAIR
REP. ANNE-MARIE MASTRACCIO, HOUSE CHAIR

MEMBERS:

SEN. JAMES HAMPER
SEN. LISA KEIM
SEN. NATHAN LIBBY
SEN. LINDA SANBORN
SEN. JEFFREY TIMBERLAKE
REP. KATHLEEN R.J. DILLINGHAM
REP. AMY ARATA
REP. THOM HARNETT
REP. H. SAWIN MILLETT, JR.
REP. TERESA PIERCE

MAINE STATE LEGISLATURE
GOVERNMENT OVERSIGHT COMMITTEE

MEETING SUMMARY
February 21, 2020

Call to Order

The Chair, Sen. Chenette, called the Government Oversight Committee to order at 9:08 a.m. in the Cross Office Building.

Attendance

Senators: Sen. Chenette, Sen. Hamper, Sen. Timberlake and Sen. Sanborn
Absent: Sen. Libby and Sen. Keim

Representatives: Rep. Mastraccio, Rep. Harnett, Rep. Millett, and Rep. Pierce
Absent: Rep. Arata, Rep. Dillingham

Legislative Officers and Staff: Danielle Fox, Director of OPEGA
Kari Hojara, Analyst, OPEGA
Jennifer Henderson, Senior Analyst, OPEGA
Scott Farwell, Senior Analyst, OPEGA

Introduction of Committee Members

The members of the Government Oversight Committee introduced themselves.

New Business

• Presentation of OPEGA Report on Maine Capital Investment Credit (MCIC)

Director Fox introduced Ms. Hojara, lead, and Ms. Henderson the OPEGA analysts on the MCIC review.

Director Fox introduced the presentation and stated that the subject matter is quite complex so the presentation will describe the material at a fairly high level. Director Fox and Analyst Kari Hojara presented the report on MCIC. (The report can be found at <http://legislature.maine.gov/opega/opega-reports/9149> .) The GOC members' comments and questions included:

Rep. Pierce asked if Maine can be decoupled from the Federal program, but still provide the benefits of being in conformity. Ms. Hojara replied that Maine is decoupled, but chooses to offer MCIC to approximate a portion of the Federal benefits provided by bonus depreciation, and that this would be addressed in more detail later in the presentation.

Sen. Hamper asked how many businesses in Maine claim MCIC. Ms. Hojara answered that understanding how many businesses claim MCIC is a bit complicated. Maine Revenue Services (MRS) estimate that approximately 4,000 taxpayers per year claim MCIC, but about 90% of these claims are on individual's tax returns in a pass-through manner. Sen Hamper asked if there is a way to determine if it is mostly small or large businesses that are claiming MCIC. Director Fox said that this credit is claimed primarily by those who do their business' taxes through their individual's tax returns, so there is no way for OPEGA to know the business size.

Commenting on the Federal depreciation graphic, Sen. Chenette observed that if a business takes the total depreciation in the first year they cannot claim depreciation in subsequent years for that asset. Director Fox clarified that that is true, at the federal level. Rep. Pierce asked if the business may make that decision themselves and Ms. Hojara confirmed that they may.

Rep. Mastraccio asked if there was a way for Maine to conform and continue to apply the credit only to assets located in Maine. She commented that the current process seems complicated and asked if there is a less complicated way to only provide the credit for assets in Maine, such as conforming without decoupling. Director Fox answered that would be a different response to non-conformity.

Rep. Harnett asked if other states that decouple do so for the same reasons as Maine, or is there a variety of reasons. Ms. Hojara answered that OPEGA cannot speak to the reasons other states decouple, but there are ways other state decouple that are easier on businesses.

Sen. Chenette asked if there was normal depreciation somewhere else in statute that better reflects Maine decoupling that can be modeled in MCIC. Director Fox said that the underlying reason this is done is because Maine taxable income is based on Federal taxable income as the foundation. Maine accepts regular Federal depreciation, but not bonus Federal depreciation, as a factor in Maine taxable income.

Rep. Pierce asked if the 1.2% add-back is in statute. Ms. Hojara said yes, with the 1.2% being set during the 129th Legislature.

Sen. Chenette clarified that the discussion still refers to Maine specific assets being subject to MCIC even when discussing multi-state businesses and equalizing their opportunity, not out of state assets. Rep. Pierce asked if there has been any noticeable decrease in people claiming MCIC due to the effects of the equitability changes. Ms. Hojara answered that the changes will take effect with the 2020 tax year so is too soon to tell

Rep. Harnett asked if it was more valuable to businesses to claim the depreciation all in the first year verses spreading it out. Director Fox said this largely depends on the lifespan of the asset and perhaps other factors unrelated to investment.

Rep. Pierce asked if Maine offers any tax offset to compensate for the extra effort it takes to claim MCIC. Rep. Mastraccio said it is an extra form, or forms, that have to be completed and taxpayers either have to complete them themselves or provide the information to their accountant to handle. She also said based on her understanding, the decision to take the entire depreciation of an asset in the first year or spread it out was dependent in part on other business factors.

Rep. Mastraccio clarified that the low take-up rate referred to Federal bonus depreciation and asked what the reasons might be for the low take-up rate. Director Fox said that the taxpayer's business factors for a particular year might impact whether they claim bonus depreciation, or other factors, such as the lifespan of an asset, may impact that decision.

Sen. Hamper asked if OPEGA interviewed different companies to ask if they were taking advantage of bonus depreciation. Director Fox said the literature is robust at the Federal level and it is OPEGA's understanding that MCIC is designed to approximate the value that a taxpayer would get at the Federal level so, we believe the findings of this literature, is applicable to the MCIC credit in Maine.

Rep. Timberlake asked if Maine did not have MCIC would businesses just write Maine off. Director Fox responded that there isn't really a scenario where Maine wouldn't have anything at all because Maine has to respond to what is offered at the Federal level. Because bonus depreciation is offered at the Federal level, and Maine taxable income is based on Federal taxable income, there has to be something available. There are other methods than what Maine uses, as most states are decoupled from bonus depreciation.

Rep. Pierce asked what percentage of states that decouple provide some sort of compensation to approximate the value of bonus depreciation. Director Fox said that OPEGA does not have that breakdown, but could get that for the Committee. Ms. Hojara responded that Maine is the only state that does this approximation of the value through a credit in combination with decoupling.

Sen. Sanborn asked how much revenue Maine is forgoing through this program. Director Fox provided the MRS estimates of the cost of the credit as \$11.8 million in FY18, \$23.3 million in FY19, \$19.9 million in FY20 and about \$18 million in FY21.

Rep. Mastraccio asked if the same equipment may be subject to both MCIC and BETR & BETE. Director Fox answered that it could be.

Sen. Timberlake commented that he is familiar with BETR & BETE and, based on his experience, it is very hard for a small business to qualify for BETR & BETE. He said it is easier for a small business to qualify for bonus depreciation. Director Fox reiterated that the credit is available based on whether the taxpayer claimed depreciation at the Federal level.

Sen. Chenette asked about the necessity of the taxpayer keeping "two sets of books", and if that was an adjustment an accountant could do with software. Director Fox said she could not speak to what types of software is available to handle this situation, but can say that the tax procedures for depreciation at the Federal and State level are different and separate. OPEGA did not assess the difficulties involved in doing tax preparation.

Rep. Harnett commented that his understanding, at a high level, is there is a Federal program that only about 50% of eligible claimants take advantage of. Of those, only 10% say it has a significant impact on their investment decisions, and Maine has made that even more complicated.

Sen. Chenette commented that since no other states offer a credit like what Maine does, members of the GOC would be interested in what other models look like, or how other New England states handle this situation. Director Fox noted that there are some examples of what other states do on page 10 of the report. Some other states incorporate their response in how they decouple, rather than add on a credit like Maine does. This is what makes Maine's response unique.

Rep. Pierce asked about comparisons to other states, particularly the 80% referenced in relation to North Carolina and Minnesota. Ms. Hojara answered that rather than doing something like MCIC, those two states simply allow a percentage of the Federal bonus as the add back. In Maine, the add back is the difference between what is claimed as Federal bonus depreciation and what the normal depreciation would have been, which is what necessitates keeping two sets of records.

Rep. Pierce asked if there was some advantage to the way Maine designed MCIC. Ms. Hojara answered that Maine is trying to limit depreciation to in-state assets, which results in it being more complicated.

Rep. Mastraccio asked if Maine could just decouple and not offer anything beyond the Federal credit. Ms. Hojara said that the decision about conformity and offering a credit could be separated.

Rep. Pierce commented that OPEGA does a great job of explaining the tax programs.

Unfinished Business

None

Planning for upcoming meetings

The Chair, Sen. Chenette, said that the GOC would be hearing public comment on both the BETE & BETR report and the MCIC report at the next GOC meeting on Friday, February 28, 2020. Also, at that meeting there will be a follow-up with the Chairs and Leads of the Health and Human Services and Judiciary Committees regarding the DHHS Child Protective Services efforts. The purpose of this follow-up is to check in with them regarding the information they have been provided by the GOC, discuss any potential related legislation the Committees are considering and to discuss recent reports from the Maine Children's Ombudsman and DHHS. The discussion with the Chairs and Leads will be the first item on the agenda and the public comment periods on the two tax reports will follow, and will be conducted separately. Director Fox said OPEGA has been compiling questions that have come up related to the tax reports so far, but will wait until after the public comment meeting to add any questions that may arise and compile and provide answers to all the questions at once for the work session. Chair Chenette said that there would be an opportunity for the GOC to lightly discuss BETR & BETE and MCIC at the end of the public comment meeting, but an in-depth discussion would likely take place during a work session at the following GOC meeting.

Report from Director

• Status of projects in process

Director Fox stated that policy committees are doing their review of Quasi-independent agency reports and those reports should soon be coming to the GOC.

The Director indicated that there will be information upcoming regarding the next tax reviews, including next steps and proposed parameters.

The Director gave an update on the upcoming OPEGA office move to a new location on the first floor of the Cross Building that will provide increased space and a conference room. Rep. Pierce asked if the office had moved yet and if the Committee could get a tour. The Director said that the move would hopefully take place sometime in March.

Next GOC meeting date

The next GOC meeting is scheduled for February 28, 2020 at 9:00 a.m.

Adjourn

The Chair, Sen. Chenette, adjourned the GOC meeting at 10:20 a.m. on the motion of Rep. Pierce, second by Sen. Harnett, unanimous.

Maine Capital Investment Credit (MCIC) –

A Complicated Response to Federal Bonus Depreciation that Is Unlikely to Significantly Encourage Capital Investment in Maine

Finding

MCIC is a complicated response to bonus depreciation, and is unlikely to affect capital investment in Maine

- **MCIC is complex for businesses**
- **MCIC is unlikely to encourage businesses to expedite their capital investments to any significant degree**
- **MCIC is unlikely to encourage businesses to choose Maine over other states when making capital investments.**

Presentation Map

PART I: Program Explainer

PART II: Evaluation

Evaluation Criteria

- **Intent — To stimulate the Maine economy by encouraging businesses to expedite capital investments in Maine.**
- **Goal — To encourage businesses to expedite purchases of qualifying business property in Maine.**
- **Part of Maine's response to federal bonus depreciation (Conformity)**

PART I: MCIC Explainer

- (1) Internal Revenue Code (IRC) Conformity
- (2) The Credit
- (3) Federal Bonus Depreciation
- (4) Related Tax Modifications
- (5) Changes Over Time

(1) IRC Conformity

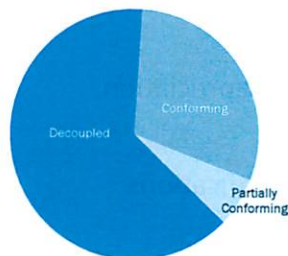
Maine lawmakers decide whether the state will conform with all federal income tax provisions or “decouple” from some, excluding them from the calculation of state income taxes.

| |
|---|
| <p>Conforming— when state tax policy follows the Internal Revenue Code</p> <p>Decoupling— when state tax policy diverges from the Internal Revenue Code</p> |
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IRC Conformity and Federal Bonus Depreciation

MCIC is part of Maine's response to federal bonus depreciation, from which Maine is decoupled.

The Majority of States Decouple from Federal Bonus Depreciation



Conformity Benefits for Businesses

(1) Financial Value

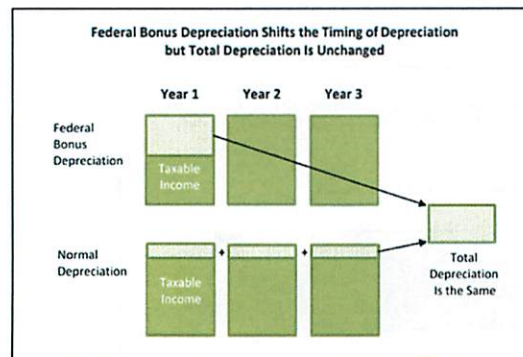
(2) Simplification of Tax Compliance

(2) MCIC Credit

- MCIC is a personal and corporate income tax credit for depreciable property placed in service in Maine.
- Available to Maine taxpayers who claimed bonus depreciation on their federal income tax returns.
- The credit works with an add-back and modifications to decouple from bonus depreciation but also attempt to provide the value of bonus depreciation.
- Presentation and report are focused on the most recent version of the credit (Title 36 §5219-NN(1-A)).

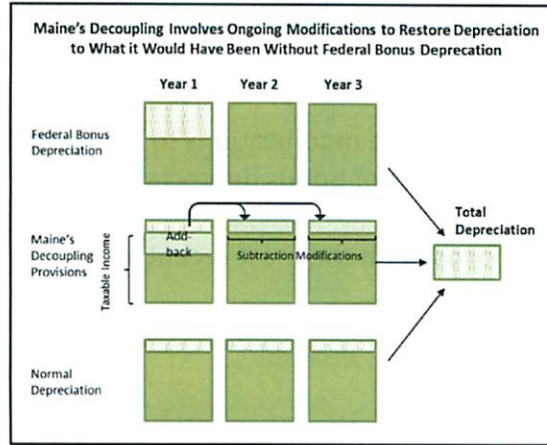
(3) Federal Bonus Depreciation

Federal Bonus Depreciation affects the amount of income tax a business owes



(4) Maine Tax Modifications

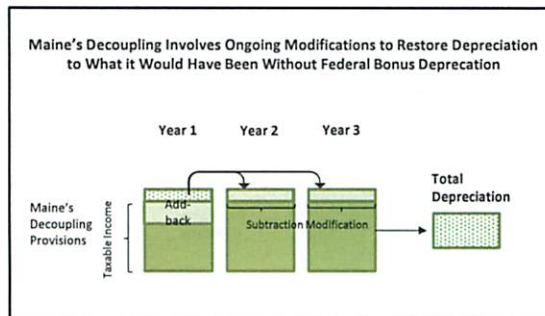
Maine does not conform but takes a different approach, requires modifications to taxable income over multiple years



Add-back – removes the effect of federal bonus depreciation from Maine taxable income for the year in which federal bonus depreciation was claimed

MCIC Credit Calculation

$$\text{MCIC credit} = \left[1.2\% \right] \times \left[\text{bonus depreciation add-back for Maine equipment} \right]$$



Add-back – removes the effect of federal bonus depreciation from Maine taxable income for the year in which federal bonus depreciation was claimed

(5) MCIC Changes

- Recent changes have increased equity between types of taxpayers (see Appendix C)
- However, the changes have also increased complexity

PART I: Summary

- Maine does not conform to federal bonus depreciation
- However, it is also uniquely complicated in its approach to providing a similar value to taxpayers.
 - See pg. 10 for examples of how other states decrease complexity.

PART II: Evaluation

MCIC's Intent

To stimulate the Maine economy by encouraging businesses to expedite capital investments in Maine.

MCIC's Goal

To encourage businesses to expedite purchases of qualifying business property in Maine.

As established in the Evaluation Parameters for this review

Is MCIC likely to encourage businesses to expedite capital investments?

- In general, business investment decisions are more likely to be driven by economic conditions and short-term sales and earnings than by tax considerations.
- Low “take-up”
- When used, not found to impact capital investment significantly
- Other positive effects (GDP, cash flow)
- MCIC less likely to have an impact

Is MCIC likely to encourage businesses to choose Maine over other locations when making capital investments?

- MCIC provides some of the limited financial value of conformity
- MCIC provides none of the tax simplicity that makes conformity desirable for businesses

Finding

MCIC is a complicated response to bonus depreciation, and is unlikely to affect capital investment in Maine

- MCIC is complex for businesses
- MCIC is unlikely to encourage businesses to expedite their capital investments to any significant degree
- MCIC is unlikely to encourage businesses to choose Maine over other states when making capital investments.