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**TESTIMONY IN OPPOSITION TO L.D. 2212, PART N**

Good morning, Senator Rotundo, Representative Gattine, Members of the Committee on Appropriations and Financial Affairs, and Senator Grohoski, Representative Sayre, Members of the Joint Standing Committee on Taxation.

My name is Olga Goldberg. I live in South Portland, and I am a state and local tax attorney with Pierce Atwood. My practice is focused on Maine taxes, and I often represent taxpayers whose businesses operate across state lines. I am here today on behalf of the Maine Society of CPAs to testify in opposition to two specific aspects of Part N of the budget, the pass-through entity tax proposal.

At the outset, I want to commend the Governor and Maine Revenue Services for including the pass-through entity tax (PTET) in the budget. The CPA Society has long-championed Maine adopting a PTET, and we have proposed an amendment to the original PTET bill, LD 191, which has been circulated to the Taxation Committee and to the Governor's office, and which adopts best practices for a state PTET. A copy of our amendment is attached. The PTET as proposed by Part N will be a significant step toward bringing Maine in line with the 36 other states and DC that have already adopted a PTET. The CPA Society supports much of the Governor's approach to a Maine PTET. However, Part N makes two significant changes to the CPA Society's proposal that we believe will put Maine residents at a disadvantage.

**Issue 1: Smaller PTET base = Smaller benefit to Maine and Maine residents**

As a general rule, pass-through entities, like partnerships and S corporations, are not subject to Maine income tax. Instead, Maine tax is imposed on the entity's owners and is based on each owners' proportional share of the entity's income. Maine resident owners are taxed on 100% of their share, regardless of whether the entity earned the income in Maine or elsewhere. Nonresident owners are taxed only on their share of the entity's income from Maine sources.

The PTET should be an analog to Maine's individual and fiduciary income taxes. That is why the CPA Society has proposed that pass-through entities pay tax on 100% of a Maine resident owner's share and on the Maine-source income of a nonresident owner's share of the pass-through entity's income. Part N, however, would limit the tax on pass-through

entities to just their Maine-source income, for resident and nonresident owners alike. There are 3 significant benefits of the CPA Society's proposal over Part N:

1. **More revenue to the State of Maine.** Both proposals would allow pass-through entity owners a 90% credit for Maine PTET paid. This means Maine keeps the remaining 10% of the tax. The CPA Society's proposal results in a larger tax base, and a larger amount of PTET paid to and retained by Maine. Part N, on the other hand, could leave significant dollars on the table—especially for pass-through entities that operate in multiple states.
2. **A larger federal tax benefit for Maine resident small business owners.** The CPA Society's proposal would allow Maine residents to pay a PTET on all of the taxable income received from their small business. On the other hand, Part N may limit the PTET to just a small portion of a Maine resident's taxable income from the business, which, in turn, may significantly limit the Maine resident's federal deduction for Maine PTET paid by the business. The CPA Society's proposal results in a larger federal tax benefit for Maine resident owners, which is then available to be invested in the State.
3. **Conformity with other PTET jurisdictions.** About half of states with a PTET follow the model set out in the CPA Society's proposal. For federal income tax purposes, residents of those states will be able to deduct PTET paid on 100% of their distributive share income, while Maine residents may only be able to deduct PTET paid on some smaller portion of their distributive share income. A Maine PTET should not put Maine residents at a disadvantage.

## **Issue 2: No Maine resident credit for New Hampshire business profits tax**

There is another significant change made in Part N: It does not allow Maine resident owners to claim a credit for New Hampshire business profits tax paid by their pass-through entity. This means that Maine residents could get a credit for PTET paid to virtually every other state—except the tax paid by the pass-through entity to Maine's closest neighbor, New Hampshire. This approach again puts Mainers at a disadvantage; our neighbors in Massachusetts are allowed the credit for New Hampshire business profits taxes.

There does not seem to be any tax policy reason for excluding New Hampshire from the credit. Consider a sole proprietorship owned by a Maine resident to a partnership owned by two Maine residents. Assuming that each business operates in New Hampshire and pays BPT, only the owner of the sole proprietorship will get a Maine credit for the BPT paid. As soon as the sole proprietor takes on a partner, the credit disappears.

Tax policy dictates that similarly situated taxpayers should be treated similarly. The CPA Society's proposal would expressly make the Maine resident tax credit available for New Hampshire BPT paid by a pass-through entity.

Thank you for your time today, and I would be happy to answer any questions.

**Amendment to LD 191**  
**An Act to Support Maine Businesses Through a Pass-Through Entity Tax and Tax Credit**

**Sec. 1.** Amend Sec. 1 of the Bill to read as follows:

**Sec. 1. 36 MRSA c. 814-A** is enacted to read:

**CHAPTER 814-A**

**PASS-THROUGH ENTITY TAX**

**§5186. Definitions**

As used in this chapter, unless the context otherwise indicates, the following terms have the following meanings.

**1. Electing pass-through entity.** "Electing pass-through entity" means an eligible partnership or an eligible S corporation that has made a timely election to pay the tax imposed pursuant to section 5187.

**2. Member.** A "member" must be an individual subject to tax under Chapter 803 or a trust or estate subject to tax under Chapter 809, and

A. A shareholder of an eligible S corporation;

B. A partner in an eligible partnership; or

C. A member of a limited liability company that is treated as a partnership or an S corporation for federal income tax purposes.

If an owner of an electing pass-through entity is a disregarded entity, such entity is disregarded for the purpose of determining whether its owner is a "member" of the electing pass-through entity.

**3. Eligible partnership.** "Eligible partnership" has the same meaning as in the Code, Section 7701(a)(2) and regulations adopted thereunder, but does not include a publicly traded partnership, as defined in the Code, Section 7704(b). "Eligible partnership" includes a limited liability company that is treated as a partnership for federal income tax purposes.

**4. Eligible S corporation.** "Eligible S corporation" has the same meaning as in the Code, Section 1361 and regulations adopted thereunder. "Eligible S Corporation" includes a limited liability company that is treated as an S corporation for federal income tax purposes.

**5. Tax year.** "Tax year" means the tax year of an electing pass-through entity for federal income tax purposes.

**6. Pass-through entity taxable income.** "Pass-through entity taxable income" means the sum of each member's distributive share of an electing pass-through entity's items of income, gain, loss, or deduction to the extent they are included in such member's Maine taxable income under this Part.

**§5187. Pass-through entity taxation election**

**1. Election.** An eligible partnership or eligible S corporation may elect to become an electing pass-through entity in a tax year. The election shall be made on an original tax return, taking into account any valid extensions. Once an election is made for a particular tax year, the election is irrevocable for that tax year. A separate election must be made for each tax year.

**2. Imposition and rate of tax.** Notwithstanding any provision of law to the contrary, a tax is imposed for each tax year on the pass-through entity taxable income of an electing pass-through entity. The rate of tax is equal the highest rate of tax applicable to individuals under section 5111.

**3. Carry-forward.** If pass-through entity taxable income results in a net loss for the electing pass-through entity, the net loss may not be carried forward to subsequent tax years.

**4. Filing of return.** A nonresident individual who is a member of an electing pass-through entity must file an income tax return to claim the credit provided by this chapter.

**5. Report of distributive share.** Each electing pass-through entity shall report to each of its members, for each tax year, the member's distributive share of the tax imposed pursuant to this chapter.

**6. Report of credit.** A subsidiary electing pass-through entity shall report to a parent electing pass-through entity the amount of the credit the subsidiary allocates to the parent electing pass-through entity.

**7. Amount of credit.** Each member of an electing pass-through entity is entitled to a credit equal to 90% of the member's distributive share of the tax paid pursuant to this chapter. If the amount of the credit authorized by this subsection exceeds the member's tax liability imposed pursuant to this Part, the excess amount is refundable to the member. A member claiming a credit pursuant to this subsection must increase federal adjusted gross income by the member's distributive share of an electing pass-through entity's federal income tax deduction of the tax imposed by this chapter.

**8 Effect of taxes paid in and credit from other jurisdictions.** Each resident individual who is a member of an electing pass-through entity that is subject to a tax imposed by another state or by the District of Columbia that is substantially similar to the tax imposed by this chapter is entitled to a credit for the direct member's or indirect member's distributive share of taxes paid to that other state or to the District of Columbia. The State Tax Assessor shall determine on an annual basis which states or District of Columbia's taxes are substantially similar to the taxes imposed by this chapter, except that the New Hampshire Business Profits Tax shall be deemed substantially similar to the taxes imposed by this chapter. If the amount of the credit authorized by this subsection exceeds the member's tax liability for the tax imposed pursuant to this chapter, the excess amount is not refundable and may not carry forward.

**9. Filing of return and payment of tax.** Each electing pass-through entity shall file a return and shall pay, on or before the 15th day of the 3rd month following the close of each tax year, to the assessor the tax as determined under this chapter. The return shall report the name, address, social security number or federal employer identification number and

Submitted by Maine Society of CPAs

such other information required by the assessor of each member whose distributive share of the pass-through entity taxable income is more than \$500.

**§5188. Effective date.** The tax imposed pursuant to section 5187 is effective for tax years beginning on or after January 1, 2025.

**§5189. Rules.** The bureau may adopt rules to implement this chapter. Rules adopted pursuant to this section are routine technical rules pursuant to Title 5, chapter 375, subchapter 2-A.