Maine Issue Brief

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Raising Taxes for DHHS Budget Would Cost Private Sector Jobs

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The Maine Department of Health and Human Services is running a serious budget deficit of an estimated $121 million for this year alone. As lawmakers work to decide how to fix the structural problems that have led to this massive shortfall, ultimately they will have to decide whether to decrease spending or increase taxes to cover the shortfall.

Raising taxes on Maine's beleaguered private sector would be a critical mistake. According to the latest data from the U.S. Department of Commerce's Bureau of Economic Analysis, Maine's private sector share of personal income is a dismal 64.1 percent—ranking Maine at 39th in the country. Clearly Maine's private sector is in a precarious situation.

Increasing taxes on the private sector will have two consequences. First, higher taxes will mean less money in the pockets of individuals and businesses which will reduce their ability to invest for the future. Second, using that money for further DHHS spending will crowd-out the private sector in competition for scarce labor and capital—which is already compounded by Maine's falling labor force participation rate.[1]

As a consequence of these tax hikes, Maine taxpayers will pay a steep price with higher tax bills, lower incomes and fewer jobs. Table 1 shows the impact of these tax proposals on the average Maine household. The most immediate impact is that the average household will face an increase in their tax bill of $215—money better spent putting groceries on the table or fuel oil in the tank.

However, more troubling, is that in the longer-run there will be a much higher economic cost to pay in either lower incomes or fewer jobs. Overall, the Maine economy will suffer a drop in personal income of $351 million, or nearly 3 times greater than the tax increase itself. The drop in personal income can manifest itself in one of two ways—lower household income for everyone or fewer jobs, though reality will lie somewhere in-between.

Table 1 shows the economic cost of a $121 million increase in taxes ranges from: $631 less personal income for all households with no private sector job loss; or, no change in personal income but the loss of 6,463 private sector jobs. The better option is to shelve tax increases and reduce government spending which would, in turn, expand the private sector. The private sector could then get back to work increasing personal incomes and creating new jobs.

Table 1
Economic Cost of Raising Taxes by $121 Million to Cover DHHS Budget Shortfall

	Tax Increase Per Household	Personal Income Lost per Household	or	Job Loss Equivalent
Maine	$215	$631	or	6,463

Source: U.S. Department of Commerce: Bureau of Economic Analysis and Census Bureau and The Maine Heritage Policy Center

Methodology

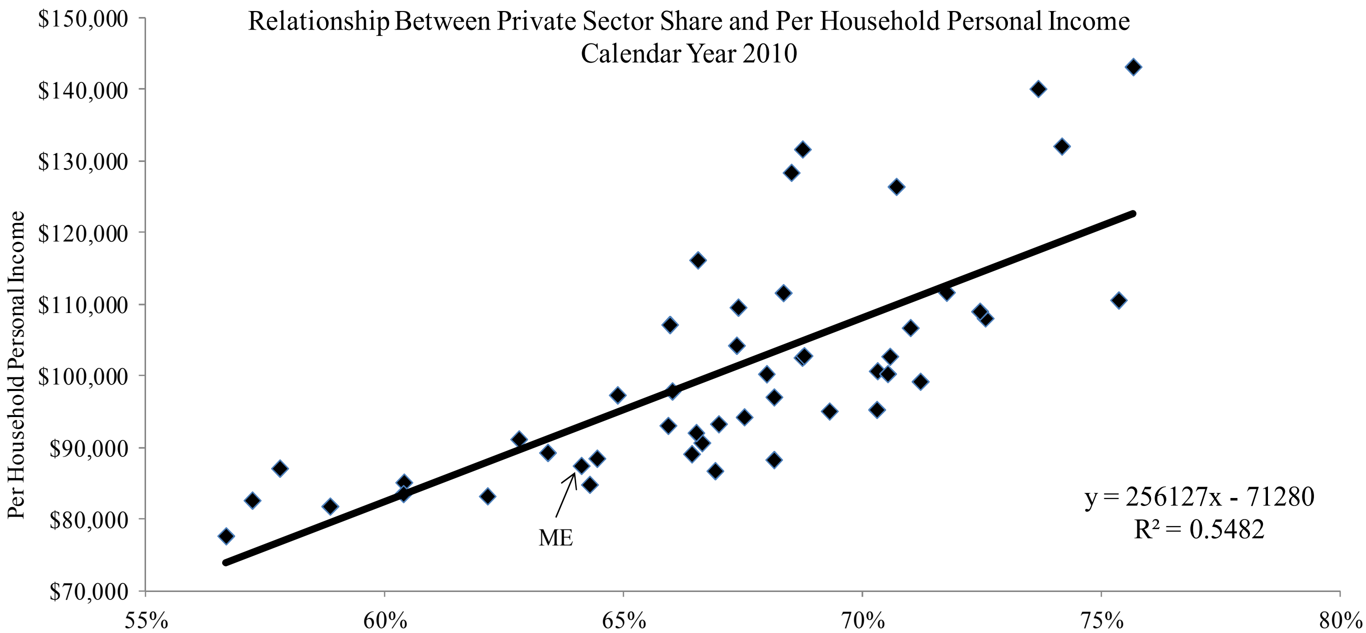
States with larger private sectors will grow faster over time than states with smaller private sectors. When examining all the 48 lower states, the analysis finds that, on average, a 1 percentage point decrease in the size of the private sector yields a decrease in per household income of approximately $2,561. Increasing Maine's taxes by $121 million would shrink the private sector by up to 0.25 percentage points. That means, in the near future, the average household in Maine would see their income drop by up to $631 ($2,561 times 0.25 percentage points). The overall loss in personal income would be up to $351 million ($631 times 557,219 households).

The drop in personal income will hit Maine taxpayers by 1) reducing income for everyone or 2) destroying jobs for a few. To represent this range of possibilities, the lost personal income is shown on a *per household basis* (lost personal income divided by households) and on a *per job basis* (lost personal income divided by the average private sector compensation)—reality will lie somewhere in-between. This analysis estimates a reduction in the long-term growth in the economy and does not necessarily mean an elimination of existing household income or jobs. It does mean that future pay increases and job creation will be lower than they would be in the absence of higher taxes and spending.

Notes and Source:

[1] Maine's labor force participation rate peaked in 2000 at 68 percent and has since fallen back to 65.1 percent in 2011. See: http://www.maine.gov/labor/cwri/data/laus/Excel/SeasonallyAdjustedLAUSEstimates.xls

Chart 1
Relationship Between Private Sector Share and Per Household Personal Income
Calendar Year 2010



Source: U.S. Department of Commerce: Bureau of Economic Analysis, Census Bureau and The Maine Heritage Policy Center. Excludes AK and HI.

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