MEMORANDUM

DATE: June 1, 2022

TO: Assembly Finance Committee

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SUBJECT: **Sales Tax on Food – Continued Consideration**

The Assembly has now considered exempting sales tax on food for several meetings. To-date, the Assembly has confirmed a decision to consider exempting only SNAP-eligible foods. At the last meeting of the Committee of the Whole, the Committee voted to advance a proposal to replace a portion of the revenue lost from exempting food by increasing the summer sales tax rate to 6% and retaining the current 5% in the winter. This would require the public to endorse the tax rate increase via ballot question.

Feedback from Businesses

Business owners and the Juneau Chamber of Commerce have urged caution about the application of a seasonal sales tax rate. Their concerns are three-fold.

First, many business owners have expressed concern about the perceived fairness of a seasonal sales tax aimed at non-residents. To those business owners, a seasonal sales tax feels unfairly targeted at summer visitors, who they see as drivers of Juneau's summer tourism economy.

Second, several businesses have expressed concern about the administrative burden and cost of changing their Point-of-Sale (POS) systems twice per year to accommodate the seasonal sales tax. Some commenters have suggested that certain businesses simply may not be able to comply at all. It would appear that this issue is more significant for larger businesses and national franchises with more complex POS systems than it is for small and micro businesses with less complex POS systems.

Third, several business owners have expressed a concern about the increased sales tax cost for the inputs to their business, with some noting that the additional tax burden on the business would simply be passed along to the consumer, and others arguing that they could not pass that burden along and it would simply make their businesses less sustainable.

Overall, it would appear that business owners are significantly concerned with a seasonal sales tax, but they appear mixed/neutral/undecided on the merits of a higher year-round rate to offset the revenue lost by exempting food.

Impact on Local Seniors

Under CBJ 69.05.045, qualifying seniors are already exempt from sales tax on SNAP-eligible foods. Hence, seniors who enjoy that exemption already would almost certainly pay *more* in total CBJ sales tax because of the higher summer tax rate. With the current proposal, there is no simple fix to this challenge. Juneau's seniors vary from lower-income to higher-income, just like the rest of Juneau's resident population. CBJ issues sales tax exemption cards to approximately 3,300 senior households each year, but it only issues about 330 hardship rebates to those cardholders. Hence, only about 10% of Juneau's senior households appear to be in the lowest income category. On the other hand, Juneau's senior population includes many local, state, and federal government retirees receiving ample pension benefits; and many of those higher-income senior households also enjoy the financial stability of owning their homes debt-free. The only likely fix to the challenge of seniors paying more in sales tax under the current proposal would be to be extend some kind of new or enhanced tax benefit to all qualifying seniors to offset the increase in tax. Increasing the amount of the existing hardship rebate could solve this problem for the low-income seniors who qualify for that rebate.

Impact on SNAP Beneficiaries

Under current law, recipients of SNAP benefits do not pay sales tax on the portion of the grocery/food bill that is paid for with their SNAP benefits. About 1,600 families or 2,800 individuals per month receive SNAP benefits in Juneau, with an average benefit per family of about $4,800 per year. That level of benefit would cover a substantial portion, though not likely the entirety, of a family's food bill. Hence, as with seniors, those beneficiaries may pay more in total CBJ sales tax with implementation of the current proposal because the increased summer tax would be greater than the benefit of tax-free food paid for with their SNAP benefits. There is no easy fix to this challenge. The only way to correct for this unintended impact would be to extend a new or enhanced benefit to SNAP recipients to offset the higher sales taxes paid annually.

Seasonal vs. Year-Round

With business owners having voiced concern about the operational challenges of a seasonal rate, some assembly members have expressed openness to consideration of a higher year-round rate. Notably, the differential impact on residents and non-residents is very different under a seasonal versus a year-round rate. A higher rate in the summer has the effect of shifting a greater portion of the sales tax burden to non-residents (visitors). A higher year-round rate raises somewhat more revenue from summer visitors, but it does not shift the tax burden from residents to visitors in the same way. The table below describes the projected impact of a seasonal rate versus a year-round rate.

		Resident Tax Savings		Vistor Tax Increase		Net Increase/(Loss)
Winter Rate	Summer Rate	Total Annual	Per Household	Total Annual	Per Visitor	of CBJ Revenue
5.00%	6.00%	$ 1,760,853.52	$ 143.47	$ 1,260,000.00	$ 0.97	$ (500,853.52)
5.50%	5.50%	$ 2,050,130.12	$ 167.04	$ 405,000.00	$ 0.31	$ (1,645,130.12)
5.60%	5.60%	$ 1,341,950.67	$ 109.34	$ 576,000.00	$ 0.44	$ (765,950.67)
5.70%	5.70%	$ 633,771.22	$ 51.64	$ 747,000.00	$ 0.57	$ 113,228.78

Without the impact of a seasonal rate shifting the tax burden from residents to visitors, either resident savings will be lower or the loss of CBJ revenue will be greater. There is no easy win here. Shifting the tax burden from residents to non-residents is likely popular with local taxpayers, but it appears unpopular with the business community. Some observers have noted that there are easier ways to get more revenue from visitors—namely by increasing the passenger fee. But, in keeping with the CLIAA settlement, passenger fees can only be spent on services and improvements that benefit the "marine enterprise" (basically the infrastructure and services used by passengers when they disembark). Sales tax revenues paid by visitors, however, can be used for any general government purpose.

Replacement of Lost Sales Tax Revenue with Property Tax

While recent deliberations have focused on replacing foregone sales tax revenue with new sales tax revenue from higher rates or reduced exemptions, the Assembly could choose to replace the foregone revenue with any other municipal revenue source. Assembly member Alicia Hughes-Skandijs has advanced the concept to replace lost revenue with increased property tax collections. A 1.0 mill increase would replace approximately $5.7 million of the revenue lost by exempting food, and a 1.1 mill increase would replace approximately $6.3 million. These options could resolve all three of the above concerns: the unintended tax increase on seniors, the unintended tax increase on SNAP beneficiaries, and the business community's concerns about implementing a seasonal rate.

As discussed previously, economists consider property tax a progressive tax because the level of taxation is proportional to one's income or accumulated wealth. Those who own more expensive properties pay more property tax, and those who own (or rent) less expensive properties pay less property tax. In most cases, there is a strong correlation between income, property ownership, and property taxes paid (i.e. individuals with higher income generally own more property and pay more property taxes).

The following table illustrates the impact of a 1.0 mill increase to property tax while exempting food from sales tax. It demonstrates that for most lower-income households, there would be a reduction in total taxation if food were exempt and the Assembly replaced the lost revenue with a 1.0 mill increase to property tax. Middle-income would see a more modest benefit. Higher-income households would break even or see a minor tax reduction. Only households with significant accumulated wealth (i.e. real property holdings) would likely see a net tax increase.

Household Scenarios	Annual income	Property value (or rental value)	Cost of 1.0 mill Property Tax	Annual Food Spend	Benefit of Tax-Free Food	Benefit (cost) difference
Higher accumulated wealth	$ 500,000	$ 5,000,000	$ 5,000	$ 12,000	$ 600	($4,400)
Median accumulated wealth	$ 350,000	$ 2,500,000	$ 2,500	$ 12,000	$ 600	($1,900)
Lower accumulated wealth	$ 250,000	$ 1,500,000	$ 1,500	$ 12,000	$ 600	($900)
One High Earner - No Children	$ 120,000	$ 500,000	$ 500	$ 10,000	$ 500	$0
Two High Earners - Some Children	$ 200,000	$ 600,000	$ 600	$ 12,000	$ 600	$0
Two High Earners - Large Family	$ 200,000	$ 600,000	$ 600	$ 14,000	$ 700	$100
One Median Earner - No Children	$ 70,000	$ 350,000	$ 350	$ 8,000	$ 400	$50
Two Median Earners - Some Children	$ 120,000	$ 400,000	$ 400	$ 10,000	$ 500	$100
Two Median Earners - Large Family	$ 120,000	$ 400,000	$ 400	$ 12,000	$ 600	$200
One Low Earner - No Children	$ 30,000	$ 100,000	$ 100	$ 6,000	$ 300	$200
Two Low Earners - Some Children	$ 50,000	$ 150,000	$ 150	$ 8,000	$ 400	$250
Two Low Earners - Large Family	$ 50,000	$ 150,000	$ 150	$ 10,000	$ 500	$350

Alternative Concept – Tax Rebate for Low Income Households

Mayor Weldon has advanced an alternative concept to issue a cash rebate to low income individuals in the amount of $150, upon successful application annually. The concept has been modeled after the qualifying criteria for the Senior Hardship Rebate that is already codified under CBJ 69.05.046. Hence, any resident would qualify for the rebate if their income were not greater than 250% of the federal poverty guideline. The Finance Department assumes that the Assembly's intention is that such a rebate would be mutually exclusive from the rebate currently extended to low income seniors. Using data from the US Census Bureau, the Finance Department estimates that approximately 2,000 non-senior households may meet qualifying income criteria. Assuming that half of households are two qualifying adults and half are one qualifying adult, CBJ would lose approximately $450,000 of sales tax revenue. Such a rebate process would require an application review and approval process in the Sales Tax Office. That office lost a clerical position in 2020 due to budget cuts, and it would not be possible for them to operate another such application review program without additional staff.

Caution on Precision

The Finance Department can model the impact of different sales tax rates on CBJ revenue with relatively high confidence. However, estimates and calculations of impacts on individual taxpayers are low confidence. We have encountered many challenges with calculating these impacts. Of greatest significance is the lack of available data. There is limited good Alaska-specific or Juneau-specific data on consumer spending. Relatedly, the CBJ Sales Tax Office has exhaustive data about how businesses collect sales taxes, but it has no data about who pays those sales taxes. Importantly, Juneau businesses *pay* an unknown portion of all sales taxes collected, so a change to sales tax policy has a fiscal impact (positive or negative) on those businesses that will be different than the impact on residents and visitors—a difference that cannot easily be calculated. Lastly, the available data on these subjects is often bifurcated between individuals and households, and there is not a highly reliable way to extrapolate data between those two measures. In summary, I believe our estimates of impact on CBJ revenue are reasonably accurate, but we would need to contract with an economist to better model the impact on individual taxpayers.