

## DEPARTMENT OF TAXATION 2002 Fiscal Impact Statement

1. Patron: Deeds

3. Committee: Senate Finance

4. Title: Retail Sales and Use Tax:  
Food Tax Reduction Program

2. Bill No: SB 189

House of Origin:

X Introduced

       Substitute

       Engrossed

Second House:

       In Committee

       Substitute

       Enrolled

### 5. Summary/Purpose:

This bill would replace the current Food Tax Reduction Program and provide an exemption from the state sales and use tax on food purchased for human consumption.

The bill would not affect the imposition of the local sales and use tax.

The effective date of this bill is not specified.

Under this bill, "food purchased for human consumption" means food as defined in the Food Stamp Act of 1977, 7 U.S.C. § 2012, except for seeds and plants which produce food for human consumption. This is the same definition used in the current Food Tax Reduction Program.

6. Fiscal Impact Estimates are: Tentative. (See Line 8).

#### 6a. Expenditure Impact:

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Fund</i>
2001-02	\$343,300	GF
2002-03	\$176,000	GF

#### 6b. Revenue Impact:

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Fund</i>
2002-03	(\$210.7 million)	GF
2002-03	(\$43.5 million)	TTF
2003-04	(\$237.9 million)	GF

2003-04 (\$49.2 million)

TTF

**7. Budget amendment necessary:** Yes.

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**8. Fiscal implications:**

Administrative

There are costs associated with modifying the system to implement this legislation. TAX is currently in the process of replacing its automated systems as part of a partnership with AMS. As a result, TAX will be maintaining two systems – the current STARS system and the new IRMS system – for a period of time as a contingency. The contract with AMS generally provides for the costs of implementing routine legislation. However, changes attributable to major legislation are not within the scope of the contract.

TAX would incur \$151,700 in fiscal year 2002 in costs for changes to its existing system and other administrative costs of \$191,600 for processing and postage. Changes to the new IRMS system will be covered under the AMS contract. In addition, TAX would incur administrative costs of \$176,000 in fiscal year 2003 for personnel costs and forms development.

Revenue

This bill would eliminate the state portion of the retail sales and use tax on food purchased for human consumption. This would affect: (1) revenues dedicated to the GF for unrestricted use by the Commonwealth, (2) revenues returned to the localities for educational purposes, and (3) TTF revenues. It is estimated that this bill would have a negative impact on GF and TTF revenues of \$254.2 million in fiscal year 2003 and \$287.1 million in fiscal year 2004.

**9. Specific agency or political subdivisions affected:**

Department of Taxation

**10. Technical amendment necessary:** No.

**11. Other comments:**

**Reduced Sales Tax Rate**

This bill does not affect the imposition of the local sales and use tax. Therefore, consumers would pay a reduced sales and use tax rate of 1% on purchases of food for human consumption.

### **Food Stamp Definition**

Under this bill, “food purchased for human consumption” means food as defined under the federal Food Stamp Program. This is the same definition utilized under the current Food Tax Reduction Program. The definition is broad and includes any food or food product for home consumption, except alcoholic beverages, tobacco, and hot foods or hot food products ready for immediate consumption. Hot meals for immediate consumption are generally excluded from the food stamp definition.

In utilizing the food stamp definition, the reduced sales and use tax rate would apply to purchases of a wide variety of grocery and staple items such as meats, fruits and vegetables, cereals, beverages, snack and bakery foods, and dietary and health foods. In addition, cold prepared foods and beverages packaged for home consumption qualify as “food purchased for human consumption” under the federal definition.

### **Allocation of Revenues from Sales of Food**

Under the current Food Tax Reduction Program, the revenue generated from the 4.0% sales and use tax is allocated to the GF, the TTF, and the localities. The GF currently retains tax revenues generated by the 1.5% tax rate for unrestricted use by the Commonwealth. The tax revenue from the 1% tax rate goes into the GF for educational purposes and is returned to the localities based on school-age population. The TTF receives sales tax revenues from the 0.5% tax rate, and the remaining 1% represents the local option sales tax revenues.

This bill would eliminate the GF 1.5% tax rate share of the revenues for unrestricted use, revenues dedicated to the GF for educational purposes, and revenues dedicated to the TTF. Revenues generated from the local option sales and use tax would not be affected by this bill.

### **Other States’ Food Exemptions**

#### Generally

Of the 45 states that impose sales and use taxes, 30 currently provide an exemption of some type for food for human consumption. These exemptions range from full exemptions, some with phase-out provisions, to partial exemptions applying reduced rates on food. Some states fully tax food sales and allow an income tax credit or grant a refund for sales and use tax paid on food. The most recent additions are Louisiana, North Carolina and Virginia. Louisiana, however, has temporarily suspended its

exemption. North Carolina and Virginia currently provide a reduced sales and use tax rate on food for human consumption. (Source: Survey by Federation of Tax Administrators.)

#### Border States

The border states that provide an exemption of some type for food are the District of Columbia, Kentucky, Maryland, and North Carolina.

- The District of Columbia provides an exemption for all food and drink with the exception of food or drink sold through vending machines or prepared for immediate consumption, and snack food. The District of Columbia does not follow the food stamp definition of “food.”
- Kentucky does not follow the food stamp definition of “food,” but instead provides an exemption for food products deemed to be a “nutritional necessity.” Taxable items include candy, confectionery, chewing gum, soft drinks, sodas and similar beverages, water, meals served on or off the premises, and food sold through vending machines.
- Maryland provides an exemption and follows the food stamp definition of “food” with exceptions for soft drinks or carbonated beverages, candy and confectionery. These items, however, are exempt when sold by grocers and markets and through vending machines. Maryland also exempts milk, fresh fruit, fresh vegetables and yogurt sold through vending machines.
- North Carolina provides a reduced sales and use tax rate (local tax applies) on food for human consumption and follows the food stamp definition of “food” with no exceptions. The reduced rate does not apply to sales of food for immediate consumption and food sold through vending machines.

Tennessee and West Virginia currently impose the sales and use tax on food and food products.

#### Other Legislation

House Bill 86 would amend the definition of food to exclude certain establishments from imposing the reduced sales and use tax on food for human consumption.

House Bill 1052 would repeal the current Food Tax Reduction Program and provide a total exemption from the state and local sales and use taxes for food purchased for human consumption, effective July 1, 2002.

Senate Bill 104 would delete the safeguards in the current Food Tax Reduction Program and reduce the state sales and use tax on food purchased for human consumption to 1½%, effective April 1, 2003.

cc: Secretary of Finance

Date: 1/28/02/VHM

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