

**REPORT OF THE  
JOINT SUBCOMMITTEE  
STUDYING**

**Criteria for Evaluating  
Retail Sales and Use Tax  
Exemption Legislation**

**TO THE GOVERNOR AND  
THE GENERAL ASSEMBLY OF VIRGINIA**



**Senate Document No. 27**

**COMMONWEALTH OF VIRGINIA  
RICHMOND  
1988 -**

MEMBERS OF SUBCOMMITTEE

Senator Charles J. Colgan, Chairman  
Delegate Warren G. Stambaugh, Vice Chairman  
Senator Elmo G. Cross, Jr.  
Senator William T. Parker  
Delegate Lewis W. Parker, Jr.  
Delegate S. Wallace Stieffen  
Delegate Walter A. Stosch

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STAFF

Regina M. McNally, Staff Attorney  
John A. Garka, Economist  
Jane C. Lewis, Executive Secretary

ADMINISTRATIVE AND CLERICAL

Office of the Clerk, Senate

SENATE JOINT RESOLUTION NO. 119

*Establishing a joint subcommittee of the Senate and House to study criteria for evaluating requests for exemptions from the retail sales and use tax.*

Agreed to by the Senate, February 4, 1987

Agreed to by the House of Delegates, February 25, 1987

WHEREAS, tangible personal property sold or used in the Commonwealth is subject to the Virginia retail sales and use tax, unless the property is exempt from taxation; and

WHEREAS, each year numerous organizations petition the General Assembly to exempt certain property from the sales and use tax; and

WHEREAS, the number of sales and use tax exemptions granted by the General Assembly has substantially increased during the past four years, and currently there are sixty-seven different categories of property which are exempt from the sales and use tax; and

WHEREAS, there need to be guidelines or criteria established for evaluating requests for sales and use tax exemptions, so that the exemptions are based on equitable considerations that relieve certain taxpayers from an unfair tax burden; now, therefore, be it

RESOLVED by the Senate, the House of Delegates concurring, That a joint subcommittee be established to study factors and criteria which should be used by the General Assembly in evaluating requests from taxpayers for exemptions from the retail sales and use tax.

The joint subcommittee shall consist of seven members who shall be appointed in the following manner: three members of the Senate Finance Committee appointed by the Senate Committee on Privileges and Elections, and four members of the House Finance Committee appointed by the Speaker of the House.

The joint subcommittee shall complete its work prior to November 15, 1987.

The indirect costs of this study are estimated to be \$5,860 and the direct costs are estimated to be \$2,520.

Report of the  
Joint Subcommittee Studying  
Criteria for Evaluating Retail Sales and Use Tax  
Exemption Legislation

To

The Governor and the General Assembly of Virginia  
Richmond, Virginia  
1988

To: Honorable Gerald L. Baliles, Governor of Virginia,  
and  
The General Assembly of Virginia

## INTRODUCTION

The 1987 General Assembly established this joint subcommittee pursuant to Senate Joint Resolution No. 119 to develop and recommend criteria to evaluate retail sales and use tax exemption legislation in order to increase the efficiency and effectiveness of the General Assembly in evaluating the voluminous amount of retail sales and use tax exemption legislation. The joint subcommittee elected Senator Charles J. Colgan and Delegate Warren G. Stambaugh Chairman and Vice Chairman, respectively.

## SCOPE OF STUDY

The joint subcommittee held six meetings and examined the following retail sales and use tax exemption issues:

- (1) General facts about the administration and collection of the retail sales and use tax;
- (2) National trends in retail sales and use tax exemptions;

- (3) Standards for evaluating the purposes and goals of retail sales and use tax structures;
- (4) Arguments supporting limiting exemptions from the retail sales and use tax; and
- (5) Problems and alternatives in evaluating retail sales and use tax exemption legislation.

## FINDINGS

The joint subcommittee determined that a retail sales and use tax consists of four general purposes and goals which are widely used by tax analysts for evaluating sales and use tax structures:

1. The sales tax is designed to be a uniform tax on consumer expenditures except where there is specific justification for exemption. Its structure therefore should (a) facilitate shifting the tax to the ultimate consumer; (b) apply to all consumption expenditures at a uniform rate, unless certain circumstances justify exception; and (c) apply to the amounts actually paid by the final consumer.
2. The tax structure should be designed to minimize regressivity in the distribution of tax burdens in order to conform as closely as possible with accepted standards of equity.
3. The tax structure should not create competitive disturbances in business activity.
4. The tax structure should facilitate administration and vendor compliance.

The joint subcommittee examined the retail sales and use tax exemptions in relation to the preceding standards and made the following observations:

- (1) The retail sales and use tax exemptions have expanded from 21 categories to 68 categories since 1966 when the tax was first enacted;

- (2) The amount of retail sales and use tax exemption legislation substantially increases annually. In 1987, 63% of all retail sales and use tax legislation were exemptions bills;
- (3) Since 1966, there has been a trend away from broad categories of exemptions to specific exemptions to benefit particular interest groups; and
- (4) The expansion of exemptions in Virginia is consistent with the national trend which reflects a pattern of sales tax base erosion through an increased number of exemptions and higher statutory rates. (See Appendix for Tables)

The expansion of retail sales and use tax exemptions concerned the subcommittee for the following reasons:

1. Exemptions erode the tax base and reduce revenue.
2. Exemption requests increase as more exemptions are granted.
3. Exemptions increase the difficulty of compliance and administration.
4. Exemptions make audits more difficult and increase chances for error.

The subcommittee determined that the basic problem in Virginia's current procedure for analyzing retail sales and use tax exemption legislation is that the revenue impact of the proposed exemptions is often excluded from analysis of the legislation, because background information relating to the nature of the organization and the type of its purchases are usually unavailable or unknown. Since the purpose of the sales tax is to raise revenue for the Commonwealth, any exemption request should be examined by considering the revenue loss to determine if other taxpayers will be unduly burdened by the tax exemption. The Department of Taxation estimated that the total annual revenue loss attributable to sales tax exemptions may be as much as \$1.3 billion annually, and such amount can be broken down as follows:

General Fund	=	\$845 million
Local	=	\$290 million
Transportation	=	\$145 million

The lack of background information about nonprofit organizations requesting exemptions often makes estimating revenue loss impossible. Additionally, it makes precision in drafting more difficult, which results in additional administrative burdens for the Department of Taxation.

The joint subcommittee determined that in evaluating retail sales and use tax exemptions, existing exemptions and future exemptions may need to be treated according to different criteria. The subcommittee explored the following options in order to devise an approach that evaluates the equity, economic and fiscal impact of the different categories of exemptions. The options considered are summarized in the following chart.

# Summary of Options for Evaluating Retail Sales and Use Tax Exemptions

## Existing Exemptions

1. Sunset exemptions in 1994, authorize tax expenditure study on all sales tax exemptions during interim to establish criteria for evaluating existing and future exemptions (proposed at Nov. 16)
2. Limit tax expenditure study to nonprofit organizations. Require the Department of Taxation to evaluate the revenue loss and administrative costs on sales tax exemptions for nonprofits. Require nonprofits to report to Dept. of Taxation information relating to the types of purchases made, value of purchases, how items purchased are used by the organization, list of the cities and counties where the organization operates, and the local taxes which it pays. Sunset nonprofits only.
3. No sunseting; leave exemptions alone.

## Future Exemptions

1. Any new exemptions should have a two-year sunset, require Department of Taxation to analyze the revenue impact and administrative cost during the two-year period.
2. Enact new exemptions with a refund mechanism, so that exempt taxpayer pays the tax but files for refund. This mechanism will enable the Dept. of Taxation to obtain data about exempt taxpayers.
3. Establish a permanent advisory group to analyze any proposed sales tax exemption, and the advisory group will make a recommendation to the General Assembly concerning the exemption.
4. Require all new exempt taxpayers to obtain a sales tax exemption permit so that all purchases can be traced to the taxpayer's identification number. Authorize the Tax Commissioner to revoke the exemption permit, if it is determined that the taxpayer used the permit for nonexempt purposes.

## RECOMMENDATIONS

After evaluating the advantages and disadvantages of the numerous possible options, the joint subcommittee made the following recommendations:

1. The sunset clause on exemptions should be rejected for 1988 because the majority of exemptions appear to be based upon valid economic or equitable reasons;
2. Legislation should be introduced to authorize the Tax Commissioner to collect data from exempt taxpayers to determine the policy, economic and fiscal impact of the retail sales and use tax exemptions;
3. A study resolution should be introduced to continue the examination of the retail sales and use tax exemptions, and to request the Tax Commissioner and Secretary of Finance to provide the following information to the subcommittee:
  - (a) specific guidelines for analyzing the policy, economic and fiscal impact of existing retail sales and use tax exemptions;
  - (b) specific guidelines for determining if any existing retail sales and use tax exemptions should expire at a future date; and
  - (c) specific guidelines and information essential for evaluating the policy, economic and fiscal impact of future retail sales and use tax exemption requests.

The legislation and resolution recommended by the joint subcommittee are contained in the Appendix.

Respectfully submitted,

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The Honorable Charles J. Colgan, Chairman

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The Honorable Warren G. Stambaugh, Vice Chairman

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The Honorable Elmo G. Cross, Jr.

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The Honorable Lewis W. Parker, Jr.

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The Honorable S. Wallace Stieffen

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The Honorable Walter A. Stosch



## APPENDIX

1. Draft legislation
2. Volume of retail sales and use tax exemption legislation
3. Retail Sales and Use Tax Exemptions Passed by the General Assembly: 1980 - 1987
4. Five Types of Tangible Personal Property Exempt from the 4½% Retail Sales and Use Tax Rate and Subject to Taxation at a Lower Rate:
5. Major Features of State Sales Tax
6. Analysis of Alternatives for Evaluating Retail Sales and Use Tax Exemptions

2 SENATE BILL NO. .... HOUSE BILL NO. ....

3 A BILL to amend and reenact § 58.1-601 of the Code of Virginia,  
4 relating to administration of retail sales and use tax  
5 exemptions.

6

7 Be it enacted by the General Assembly of Virginia:

8 1. That § 58.1-601 of the Code of Virginia is amended and reenacted  
9 as follows:

10 § 58.1-601. Administration of chapter.-- A. The Tax Commissioner  
11 shall administer and enforce the assessment and collection of the  
12 taxes and penalties imposed by this chapter.

13 B. The Tax Commissioner shall investigate and evaluate the  
14 fiscal impact, economic impact and equity of existing retail sales and  
15 use tax exemptions. The Tax Commissioner may require persons exempt  
16 from the retail sales and use tax to furnish the Department with  
17 books, records or other information relating to exempt purchases or  
18 sales, and any other information relating to direct or indirect  
19 government financial assistance which the exempt person receives.

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SENATE JOINT RESOLUTION NO.....

3 Requesting the Senate and House Finance Committees to continue the  
4 joint subcommittee studying criteria for evaluating retail sales  
5 and use tax exemption legislation.

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7 WHEREAS, Senate Joint Resolution No. 119 of the 1987 Session of  
8 the General Assembly of Virginia established a joint subcommittee to  
9 develop criteria for evaluating retail sales and use tax exemption  
10 legislation; and

11 WHEREAS, the joint subcommittee determined that the categories of  
12 sales tax exemptions have expanded from twenty-one to sixty-eight  
13 since 1966 when the retail sales and use tax was first enacted; and

14 WHEREAS, the expansion of exemptions has resulted in piecemeal  
15 erosion of the retail sales and use tax base; and

16 WHEREAS, the joint subcommittee concluded that the fiscal impact,  
17 economic impact and equity of existing retail sales and use tax  
18 exemptions cannot be comprehensively analyzed without obtaining  
19 additional information from exempt taxpayers relating to their  
20 purchases, sales and any direct or indirect governmental assistance  
21 which they receive; and

22 WHEREAS, the Secretary of Finance and the Commissioner of the  
23 Department of Taxation are requested to investigate and analyze the  
24 fiscal impact, economic impact and equity of the existing retail sales  
25 and use tax exemptions, before the joint subcommittee adopts final  
3 criteria for recommendation to the General Assembly; and

1           WHEREAS, the Secretary of Finance and Commissioner of the  
2 Department of Taxation shall report to the joint subcommittee the  
3 following findings:

4           (i) Specific guidelines for analyzing the equity, economic and  
5 fiscal impact of existing retail sales and use tax exemptions;

6           (ii) Specific guidelines for determining if any existing retail  
7 sales and use tax exemptions should expire in 1994; and

8           (iii) Specific guidelines and information essential for  
9 evaluating the equity, economic and fiscal impact of future retail  
10 sales and use tax exemption requests; and

11           WHEREAS, the joint subcommittee shall make final recommendations  
12 based on the report of the tax expenditure study to the 1989 Session  
13 of the General Assembly; now, therefore, be it

14           RESOLVED by the Senate, the House of Delegates concurring, That  
15 the joint subcommittee studying criteria for evaluating retail sales  
16 and use tax exemptions is hereby continued. The members appointed  
17 pursuant to SJR 119 (1987) shall continue to serve, with vacancies  
18 filled by the same appointing authority specified in that resolution.

19           The indirect costs of this study are estimated to be \$8255; the  
20 direct costs of this study shall not exceed \$3780.

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TABLE I

VOLUME OF RETAIL SALES AND USE TAX EXEMPTION LEGISLATION  
1980 -- 1987

<u>YEAR</u>	<u>TOTAL RETAIL SALES AND USE TAX BILLS INTRODUCED</u>	<u>RETAIL SALES AND USE TAX EXEMPTION BILLS INTRODUCED</u>	<u>RETAIL SALES AND USE TAX EXEMPTIONS PASSED</u>
1980	30	20 (66%)	8
1981	24	14 (58%)	4
1982	27	18 (66%)	5
1983	21	11 (52%)	6
1984	8	6 (75%)	4
1985	20	16 (80%)	8
1986	30	16 (53%)	7
1987	24	15 (62%)	7

CONCLUSION:

- 63% of total retail sales and use tax legislation are exemption bills.
- 42% of all retail sales and use tax exemption bills introduced each session are passed.

Table II

Retail Sales and Use Tax Exemptions  
Passed by the General Assembly: 1980 - 1987

1. 1980: 8 Bills:

	<u>Page</u>	<u>Purpose</u>
SB 73	1184	◦ gift wrapping services by nonprofit organizations
HB 960	927	◦ amplification, transmission and distribution equipment used by cable TV
SB 162	1192	◦ fuels for domestic consumption
SB 260	889	◦ insulin syringes by diabetics
SB 63	880	◦ materials used in agriculture production
HB 179	914	◦ commercial leasing or renting laundered textile products
SB 62	877	◦ tangible personal property for research and development
HB 282	94	◦ textbooks used in certain institutions of learning

2. 1981: 4 Bills:

SB 559	523	◦ certain historical documents, manuscripts, paintings and art objects purchased by nonprofit historical societies
SB 579	531	◦ certain tangible personal property sold to youth organizations that sponsor certain camping assemblies
HB 1255	565	◦ tangible personal property of a noncommercial educational telecommunication entity
HB 1640	939	◦ tangible personal property used by certain institutions of learning

3. 1982: 5 Bills:

HB 161	924	◦ tangible personal property purchased by nonprofit museum of fine arts
SB 373	344	◦ vending machine operators
SB 176	1192	◦ devices used by diabetics and equipment or materials purchased to produce certain publications
SB 202	895	◦ tangible personal property purchased by HMO's providing education or training to retarded citizens

HB 177 933 ° tangible personal property sold or leased for use in nutrition programs for elderly, and tangible personal property sold or used by the Virginia Federation of Humane Societies

4. 1983: 6 Bills:

	<u>Page</u>	<u>Purpose</u>
HB 669	756	° advertising supplements to daily newspaper publications
SB 262	808	° certain tangible personal property purchased by voluntary health organizations
HB 549	109	° tangible personal property purchased by educational institution
HB 848	745	° certain tangible personal property used for church activities
HB 40	470	° tangible personal property purchased by nonprofit organizations for use by certain ill children and families
HB 417	200	° tangible personal property sold to a combination boarding and day school for physically handicapped children

5. 1984: 4 Bills:

HB 628	1470	° certain parts and tires used on taxicabs
SB 223	863	° drugs and supplies used in hemodialysis and peritoneal dialysis
HB 879	1483	° machinery, tools and equipment when used directly for processing or manufacturing
HB 106	654	° durable medical equipment and devices and related parts

6. 1985: 8 Bills:

HB 1388	736	° certain fishing boats and equipment
SB 583	709	° food banks
HB 1262	725	° certain nonprofit science technology museums
HB 1312	729	° certain paper and other material used by a printer
HB 1472	745	° certain uses in advertising
HB 1739	754	° special typewriters and computers used by certain handicapped persons
HB 1453	741	° certain tangible personal property used by certain public parks
HB 1241	122	° certain tax on gas, heating and oil used by certain churches

7. 1986: 8 Bills:

	<u>Page</u>	<u>Purpose</u>
HB 26	519	◦ donated property purchased by an organization that distributes food or clothing during Christmas to needy
HB 149	652	◦ tangible personal property purchased for sale by or donated to a school by PTA's and similar groups
SB 164	697	◦ high speed electrostatic duplicators
SB 192	1499	◦ WIC recipients
HB 765	1050	◦ WIC recipients and residential youth shelter organizations
SB 40	141	◦ certain purchases by American Heritage Indian Foundation
HB 248	560	◦ tangible personal property used by a residential youth shelter organization
HB 467	579	◦ tangible personal property used by governmental agencies

8. 1987: 7 Bills:

HB 972		◦ property purchased by licensed physicians and dentists providing free health care
HB 1256		◦ certain property purchased by church camps and conference centers
HB 1303		◦ parts, tires, meters and dispatch radios sold or leased to taxicab operators
HB 1407		◦ tangible personal property purchased by community health centers providing health care services to a medically underserved population
HB 1594		◦ medicines, drugs and prescriptions distributed by veterinarians
SB 382		◦ property purchased by licensed health maintenance organizations
SB 587		◦ property purchased by a nonprofit elementary or secondary school, including class rings and school photographs, property purchased by an organization providing education, training, services and assistance to foster care children



### Table III

## Five Types of Tangible Personal Property Exempt from the 4½% Retail Sales and Use Tax Rate and Subject to Taxation at a Lower Rate:

#### \*Aircraft

Virginia aircraft sales and use tax is levied at the rate of 2% upon the retail sale of every aircraft sold in this state.  
(§ 58.1-1500 through § 58.1-1570)

#### \*Alcoholic Beverages Sold by the Virginia Alcoholic Beverage Control Board through Government Stores

Virginia beer and beverage excise tax is levied on all beer and beverages sold in Virginia, and is paid by the manufacturer, bottler or wholesaler selling such beer or beverages to persons licensed to sell beer at retail.  
(§ 58.1-700 through § 58.1-718)

#### \*Motor Vehicles

Virginia motor vehicle sales and use tax is levied at the rate of 3% upon the retail sale or use of motor vehicles in Virginia with a minimum tax of \$35.  
(§ 58.1-2400 through § 58.1-2426)

#### \*Motor Vehicle Fuel and Special Fuel

Virginia motor fuel and special fuel tax is levied at the rate of 17½ cents per gallon on all motor fuel, except aviation fuel sold, delivered or used in the state. The rate of 16 cents per gallon is levied upon all special fuel.  
(§ 58.1-2100 through § 58.1-2147)

#### \*Watercraft Sales and Use Tax

Virginia watercraft sales and use tax is levied at the rate of 2% of the sale price of each watercraft sold in the Commonwealth, or 2% of the gross receipts from the lease, charter or other use of watercraft by a registered dealer. Maximum tax is \$1,000.  
(§ 58.1-1400 through § 58.1-1410)

TABLE IV

**MAJOR FEATURES OF STATE SALES TAX**  
(effective January 1987)

State and Region	Tax Rate	States Exempting				States Granting Income Tax Credit	Degree of Taxation of Services <sup>1</sup>
		Food	Pre-scription Drugs	Consumer Electric and Gas Utilities	Clothing		
U.S. Median Rate	4.75% <sup>2</sup>	29	44	32	6	8	
<b>New England</b>							
Connecticut	7.5	X	X	X	X*		4
Maine	5	X	X	X*			5
Massachusetts	5	X	X	X	X*		5
New Hampshire			- NO STATE SALES TAX -				
Rhode Island	6	X	X	X	X*		5
Vermont	4*	X	X	X		X	5
<b>Mideast</b>							
Delaware			- NO STATE SALES TAX -				
Washington, DC	6	X	X				3
Maryland	5	X	X	X*			3
New Jersey	6	X	X	X	X		3
+New York	4	X	X	X			3
Pennsylvania	6	X	X	X	X		3
<b>Great Lakes</b>							
+Illinois	5	X	X				5
Indiana	5	X	X				5
Michigan	4	X	X				5
+Ohio	5	X	X	X			3
+Wisconsin	5	X	X	X*			3
<b>Plains</b>							
+Iowa	4	X	X				2
+Kansas	4		X	X		X*	3
+Minnesota	6	X	X	X*	X		5
+Missouri	4.225*		X	X			5
+Nebraska	4	X	X				5
+North Dakota	5	X	X	X			5
+South Dakota	4		X			X*	1
<b>Southeast</b>							
+Alabama	4		X				5
+Arkansas	4		X	X*			3
+Florida	5	X	X	X			1
+Georgia	3		X				5
+Kentucky	5	X	X	X			5
+Louisiana	4	X	X	X			3
Mississippi	6		X				3
+North Carolina	3	*	X	X			4
South Carolina	5		X	X*	X*		4
+Tennessee	5.5		X	X			3
+Virginia	3.5		X	X			5
West Virginia	5	X	X	X			2
<b>Southwest</b>							
+Arizona	5	X	X				4
+New Mexico	4.75	*	*			X	1
+Oklahoma	3.25		X	X			5
+Texas	5.25	X	X	X			3
<b>Rocky Mountain</b>							
+Colorado	3	X	X	X			5
+Idaho	5		X	X		X	5
Montana			- NO STATE SALES TAX -				
+Utah	4.5938*		X	X*			3
+Wyoming	3		X			X*	3
<b>Far West</b>							
+California	4.75		X	X	X		5
+Nevada	5.75*	X	X	X			5
Oregon			- NO STATE SALES TAX -				
+Washington	6.5	X	X	X			2
+Alaska			- NO STATE SALES TAX -				
Hawaii	4	*	*			X	1

+ Additional local sales tax rates may be additional.

\*See notes on next page.

## MAJOR FEATURES OF STATE SALES TAX

### Notes

<b>Arkansas:</b>	Exempts the first 500 kilowatt hours of electricity per month for residential customers whose income is not more than \$12,000 per year.
<b>Connecticut:</b>	Clothing less than \$75 is exempt.
<b>Hawaii:</b>	Although Hawaii does not exempt food and prescription drugs from the general sales tax, a tax credit is granted on the state income tax to help offset the sales tax (and other excise taxes). This credit is available to taxpayers earning \$20,000 or less.
<b>Idaho:</b>	Rate is scheduled to be decreased to 4% on July 1, 1987.
<b>Kansas:</b>	Related income tax credit allowed for senior citizens depending on income level.
<b>Maine:</b>	The first 750 KWH per month is exempt.
<b>Maryland:</b>	Residential electricity bills are exempt from sales tax, but natural gas bills are not.
<b>Massachusetts:</b>	Sales tax applies if an item of clothing is over \$175.
<b>Minnesota:</b>	Residential use of natural gas or electricity for heating purposes is exempt through the months of November–April.
<b>Missouri:</b>	The sales tax will decrease 1/10 of 1% in June 1990.
<b>New Mexico:</b>	Although New Mexico does not exempt food and prescription drugs from the general sales tax, a tax credit (refundable if no tax is due) is available to taxpayers with modified gross income less than \$10,000—this to offset the sales tax on food and prescription drugs.
<b>Nevada:</b>	The state has a mandatory 3.75% county sales tax, which in practice gives the state a sales tax rate of 5.75%.
<b>North Carolina:</b>	Exempted food purchased with food stamps. Adopted non-refundable credit on personal income tax to help affect sales tax on food purchases. The credit ranges from \$15 to \$25 depending on income level. The credit is not available to taxpayers with taxable income greater than \$15,000.
<b>Rhode Island:</b>	Sales tax applies for sports clothing.
<b>South Carolina:</b>	Adopted a \$12.50 income tax credit to help offset the one percent sales tax increase passed in 1984.
<b>South Dakota:</b>	Related income tax credit allowed for senior citizens depending on income level.
<b>Texas:</b>	Rate is scheduled to be decreased to 4.125% on September 1, 1987.
<b>Utah:</b>	Rate decreases to 4.5% on January 1, 1990. Residential utility sales tax reduced from 1.625% to 1.594% from July 1, 1986 through December 31, 1989, and drops to 1.5% on January 1, 1990.
<b>Vermont:</b>	The 4.0% tax rate decreases to 3.0% on July 1, 1987.
<b>Wisconsin:</b>	Residential use of natural gas or electricity for heating purposes is exempt through the months of November–April.
<b>Wyoming:</b>	Related income tax credit allowed for senior citizens depending on income level.

<sup>1</sup>Degree of state taxation of professional and personal services other than utilities, admissions, and transient accommodations is divided into five (5) categories:

<sup>2</sup>Given the nature of the data, a “clean” median does not exist. Of the 46 states with sales taxes, 25 states have rates above 4.75%, 19 states have rates below 4.75%, with two states having a rate of 4.75%. The mode is 5% (14 states).

1. General taxation of most services (Includes most professional and personal services.);
2. Broad taxation of services (May include taxation of repairs; investment counseling; bank service charges; barber and beauty shops; carpentry; laundry and cleaning; photography; rentals; interior decorating; printing; packing; parking; and bookkeeping and collection services.);
3. Substantial taxation of services (May include taxation of repair services; bookkeeping and collection services; laundry and drycleaning; cable T.V.; parking; and landscaping);
4. Narrow taxation of services; (May include taxation of advertising selected business services, and laundry and dry cleaning.); and
5. No (or little) taxation of additional services.

**Sources:** ACIR staff compilations of rates, food and drug exemption information as of January 1, 1987, based on Commerce Clearing House, *State Tax Guide*. Remaining exemption data from John F. Due and John L. Mikesell, *Sales Taxation: State and Local Structure and Administration*, Johns Hopkins University Press, 1983, as updated in the *Washington Post*, May 3, 1987, p. H-3.

TABLE V

ANALYSIS OF ALTERNATIVES FOR EVALUATING RETAIL SALES AND USE TAX EXEMPTIONS

Presented to January 13, 1988 Meeting of SJR 119 Subcommittee

Alternative 1: Sunset exemptions on 7/1/94 with concurrent tax expenditures study; new exemptions subject to 2-year sunset with concurrent expenditure study; development of criteria for evaluation of exemptions

Advantages

1-Tax expenditure study provides first comprehensive overview and study of costs/benefits of existing exemptions

2-Sunset provision provides strong incentive for industry participation in data gathering process

3-Provides mechanism for mandatory ongoing analysis of new exemptions-process for avoiding current situation

4-Comprehensive tax expenditure study treats all currently exempt entities equally and does not single out a particular group or groups for special scrutiny

5-Information collected in tax expenditure study provides good database for subsequent evaluations of exemptions

6-Comprehensive tax expenditure study follows the national trend among states towards ongoing review of costs of expenditures

7-Establishment of permanent criteria provides rational framework for evaluation of future exemptions in a manner which will be equitable to all persons seeking exemption

Disadvantages

1-Proposal for comprehensive study of existing exemptions will generate considerable opposition from a wide range of current exemption holders

2-Sunset provision will require affirmative legislative action to avoid sunset of exemptions

3-Reevaluation of existing exemptions may result in rehashing of prior legislative arguments

4-Proposal may send a negative message on economic development. Virginia may be perceived as laying the groundwork for a base broadening initiative, and newly located or expanded businesses may perceive sunset provisions as renegeing on previous commitments

Alternative 2: Conduct tax expenditure study of nonprofit organization exemptions and sunset these exemptions; enact new exemptions with a refund, rather than direct exemption, mechanism

Advantages

1-Since nonprofit exemptions are the most numerous and varied in scope and application, may be the most logical starting point for expenditure study

2-Nonprofit organizations are also under study by HJR 303 subcommittee; this provision appears to interface well with their study

3-Limited tax expenditure study would be less costly

4-The refund process would minimize the initial revenue impact of new exemptions by delaying their cost until refund requests are filed

5-The refund process would simplify the audit trail for transactions involving persons with new exemptions

Disadvantages

1-Nonprofit organizations would object to being singled out for special scrutiny

2-A large segment of recent exemptions (since 1980) would not be evaluated under the limited study concept. Since 1980, 27 of the 56 new or expanded exemptions do not relate to nonprofit organizations

3-There is no provision for establishment of permanent evaluation criteria. While refund provisions would facilitate data collection, no mechanism is provided for an "up front" evaluation of proposed exemptions. Once enacted, it is very difficult to repeal exemptions

4-Utilization of a refund process for new exemptions only would be administratively complicated for both the Department of Taxation and sales and use tax dealers both of whom would be operating under two different exemptions systems

5-Administrative cost of refund process would be high. The administrative costs to many small nonprofit organizations may be very high in relation to the value of their sales and use tax exemption

6-While refund process would simplify audit process for new exemptions, impact would be negligible since a large number of taxpayers would continue to operate under the straight exemption mode

ANALYSIS OF ALTERNATIVES FOR EVALUATING RETAIL SALES AND USE TAX  
EXEMPTIONS

Page 3

Alternative 3: Establish advisory group to recommend actions on proposed new exemptions; no impact on existing exemptions

Advantages

1-Allows use of experts to provide an independent analysis of proposed exemptions

2-Allows flexibility in evaluating each proposed exemption

3-Elimination of sunset provision reduces opposition by current exemption holders

Disadvantages

1-Does not address a comprehensive study of any portion of existing exemptions

2-Does not address the establishment of permanent criteria for evaluating exemptions thus creating environment for ongoing debate over advisory commission's recommendations

3-Due to the short time frame between the introduction of an exemption bill and the end of the legislative session, advisory committee would have little time to analyze legislation or perform any type of comprehensive study. This approach may be more feasible if all exemption bills are required to be submitted to study at least 6 months prior to the session or if exemption bills are automatically introduced in the first year of the biennium and carried over to the second for action. This would make introduction and passage of bills in the second year very difficult.

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Alternative 4: Require all new exempt taxpayers to obtain exemption permit and provide Tax Commissioner to revoke exemption permit

Advantages

- 1-Provides good audit trail
- 2-Permit process is simple for permitted taxpayers
- 3-Revocation authority is a good compliance tool

Disadvantages

- 1-Permitting of taxpayers has very high administrative costs
- 2-Creation of a dual system of permitted and non-permitted taxpayers would be extremely confusing for sales and use tax dealers
- 3-Does not establish permanent criteria for the evaluation of exemptions. Without some criteria for initial evaluation of proposed exemptions, ineffective exemptions will continue to be enacted
- 4-Does not address the impact of existing expenditures
- 5-Procedure will enable the revocation of persons not complying with the law, but does not address overall exemptions which may prove to be problematic

