



# **Understanding the Impact of Adopting Local Option Sales Taxes**

**David L. Sjoquist**

**Financing Municipalities in New England:  
Revisiting the State-Local Relationship**

**Federal Reserve Bank of Boston**

**December 5, 2007**



# **I. Some Background**

# **States with Local Sales Taxes**

**NYC was the first – 1934**

**12 states in 1963**

**25 states in 1975**

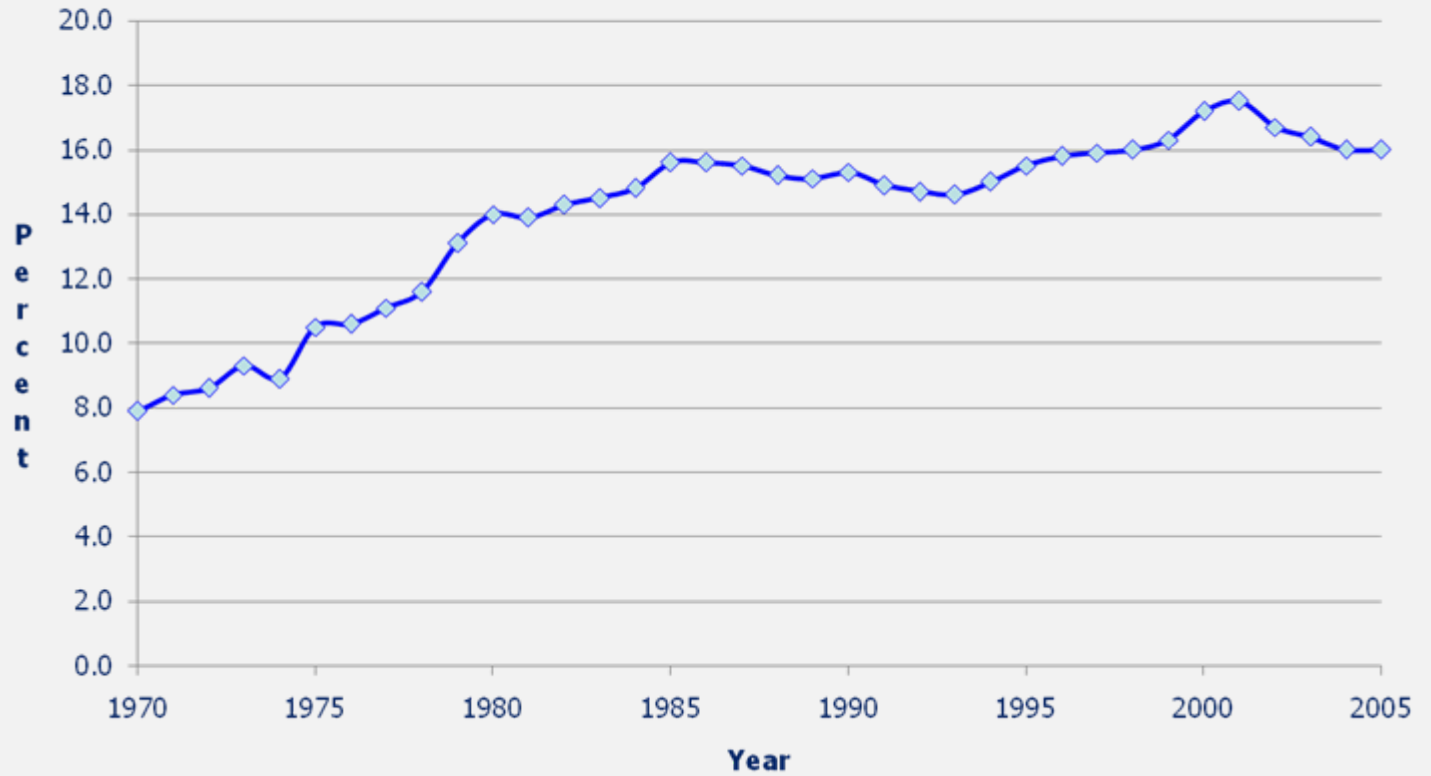
**30 states in 1980**

**33 states in 1994**

**34 states currently**

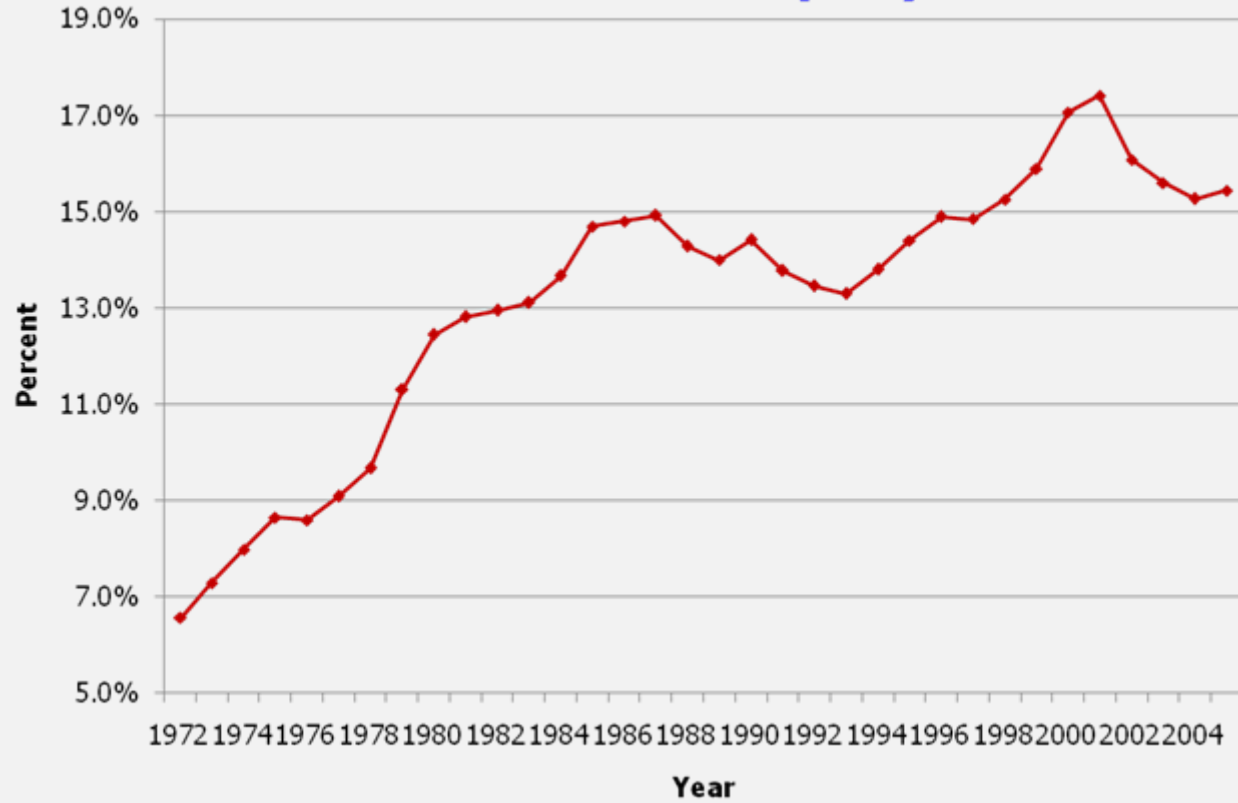
**[5 states without state sales tax]**

## Sales and Gross Receipts Taxes Percent of Taxes



Source: Tax Foundation and Census Bureau

## Sales Tax as % of Property Tax



Source: U.S. Census Bureau, State and Local Government Finances

# Local Sales Tax as a Percent of Local Taxes (2005)

|                |       |
|----------------|-------|
| Arkansas       | 50.2% |
| Louisiana      | 49.7% |
| Oklahoma       | 39.5% |
| Alabama        | 38.6% |
| New Mexico     | 37.5% |
| Colorado       | 29.7% |
| Arizona        | 24.8% |
| Tennessee      | 24.3% |
| Missouri       | 23.3% |
| South Dakota   | 21.3% |
| Georgia        | 19.9% |
| North Carolina | 18.9% |
| Washington     | 18.4% |
| Utah           | 18.0% |
| Wyoming        | 17.2% |
| New York       | 16.6% |
| California     | 15.8% |
| Alaska         | 14.5% |
| Kansas         | 14.0% |
| Iowa           | 11.1% |

Source: Census Bureau, State and Local Government Finances

# Examples

## Georgia

All are 1% and countywide.  
Referendum is required

- **MARTA**
  - Transit system
- **LOST**
  - Property tax relief
  - General expenditures
- **SPLOST**
  - Infrastructure
- **ESPLOST**
  - Education Infrastructure
- **HOST**
  - Homestead exemption
- **MOST**
  - Water/sewer – city of Atlanta

## **California**

### **1.00% (Bradley-Burns Sales Tax)**

- **0.25%** - to county of sale; dedicated to transportation
- **0.75%** - to city or county depending on location of sale

### **Local option – up to 1.5%**

- **rates range from 0.125% to 1.5%**
- **Majority are earmarked – transportation, libraries, etc.**

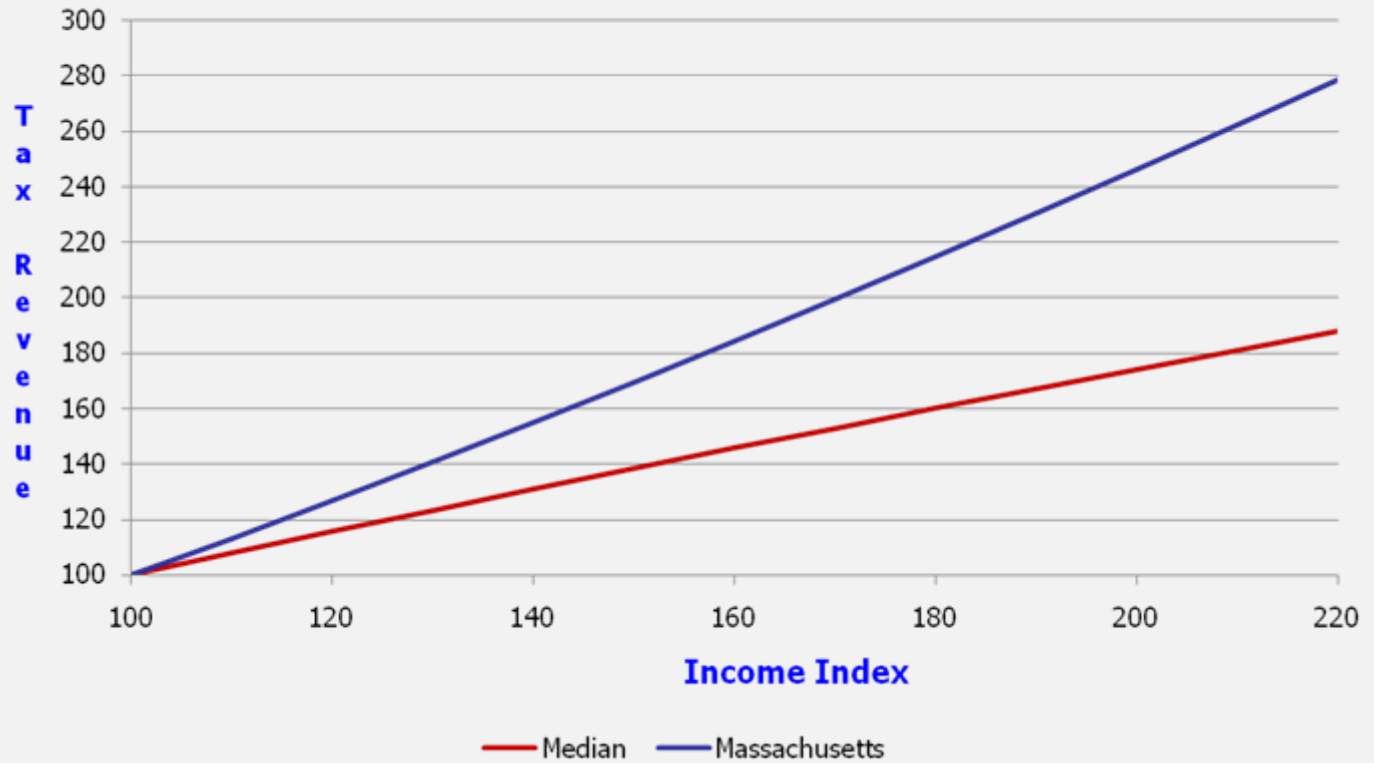




## **II. Some Implications**

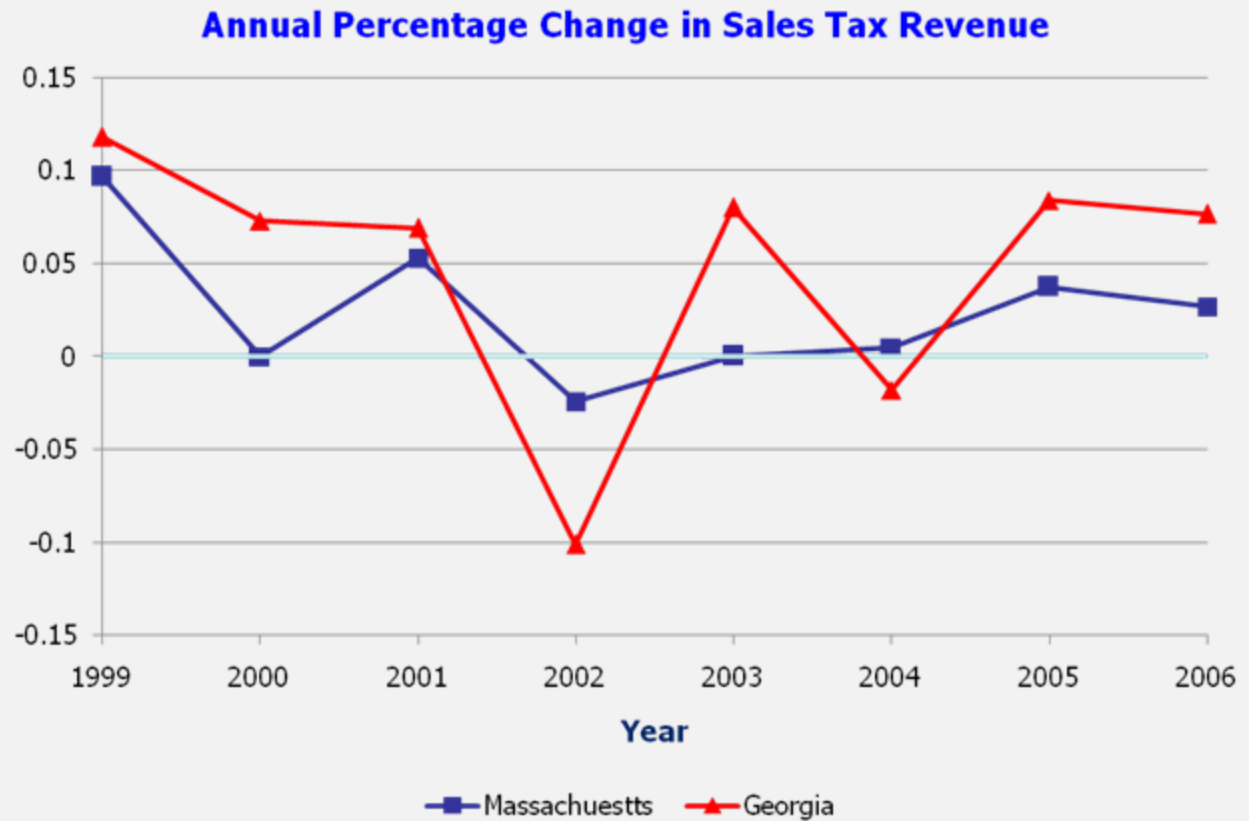
# A. Growth

## Predicted Growth

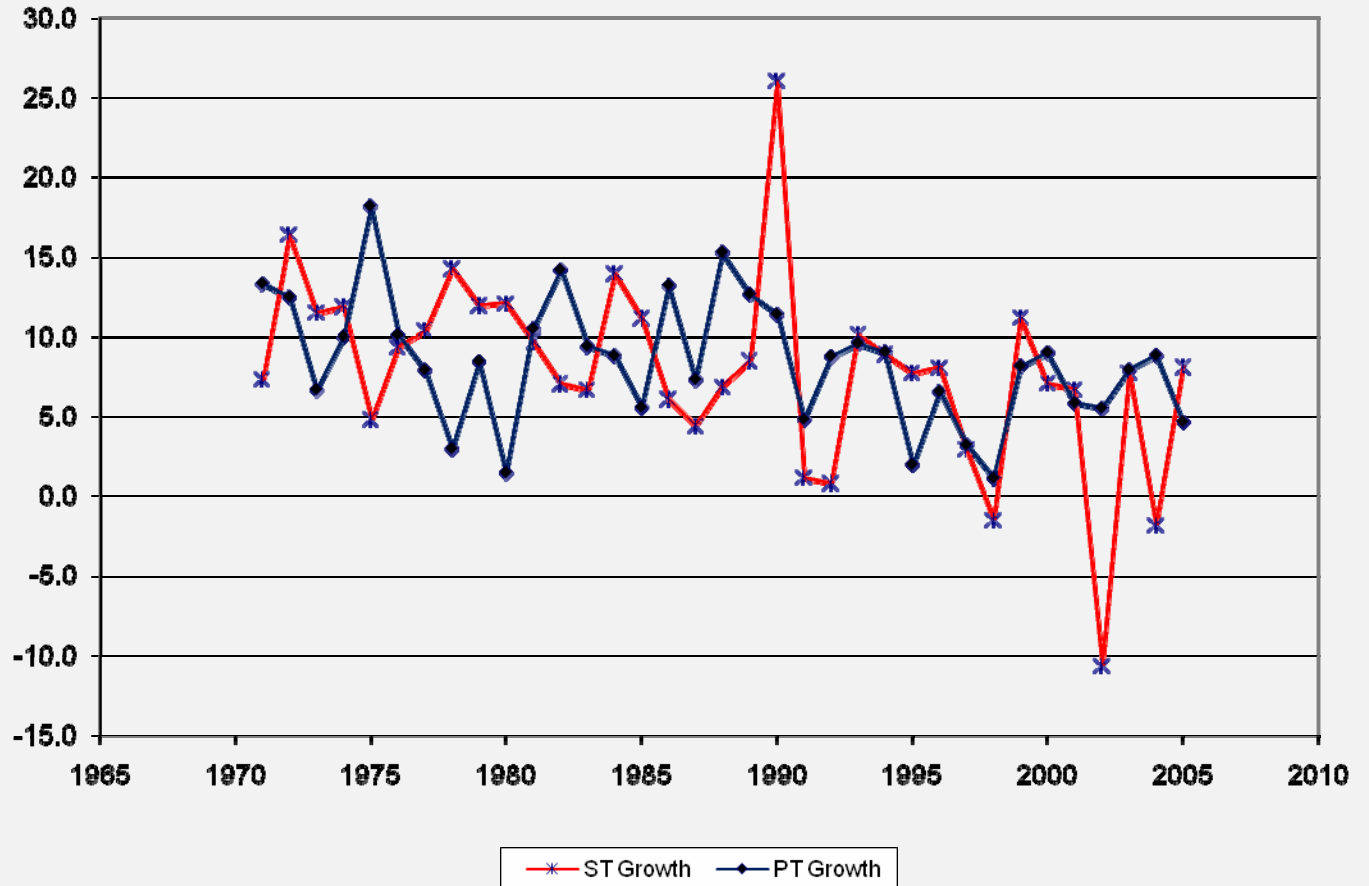


Source: Dye and Merriman (2005); Bruce, Fox, and Tuttle (2006)

## B. Stability



# Annual Growth Rates Sales Tax and Property Tax (Georgia)



## **C. “Fiscalization”**

**Increased inter-jurisdictional competition for retail, especially large shopping centers.**

**Wassmer (2002) found that in the West**

- **10% increase in state reliance on local sales tax led to a 2.4% increase in retail sales in non-central areas**

**Lewis (2001) surveyed California city managers**

- **Retail was the most desirable land use**
- **Retail increased the likelihood of providing incentives**
- **Sales tax revenue was the most important factor influencing development decisions.**

# **D. Effects on Expenditures and Property Taxes**

## **Two Contrasting Views:**

- Elected officials respond to the demands of voters, who are rational and informed.**
- Elected officials are able to manipulate voters, who are not informed.**

# General Evidence

- **more diversified/complex tax structure is associated with more expenditures**
- **adoption of new tax does not lead to increases in expenditures**

# More Specific Evidence

- **Sjoquist, Wallace and Edwards (2004): Existence of a local sales tax is associated with lower property taxes.**
- **Sjoquist, Walker, and Wallace (2005): Cities differ in how much property tax is reduced.**
- **Jung (2001): in Georgia 28% of local sales tax revenue went to property tax relief.**
- **Sjoquist, Walker, and Wallace (2005): some cities do not increase expenditures, but others do.**

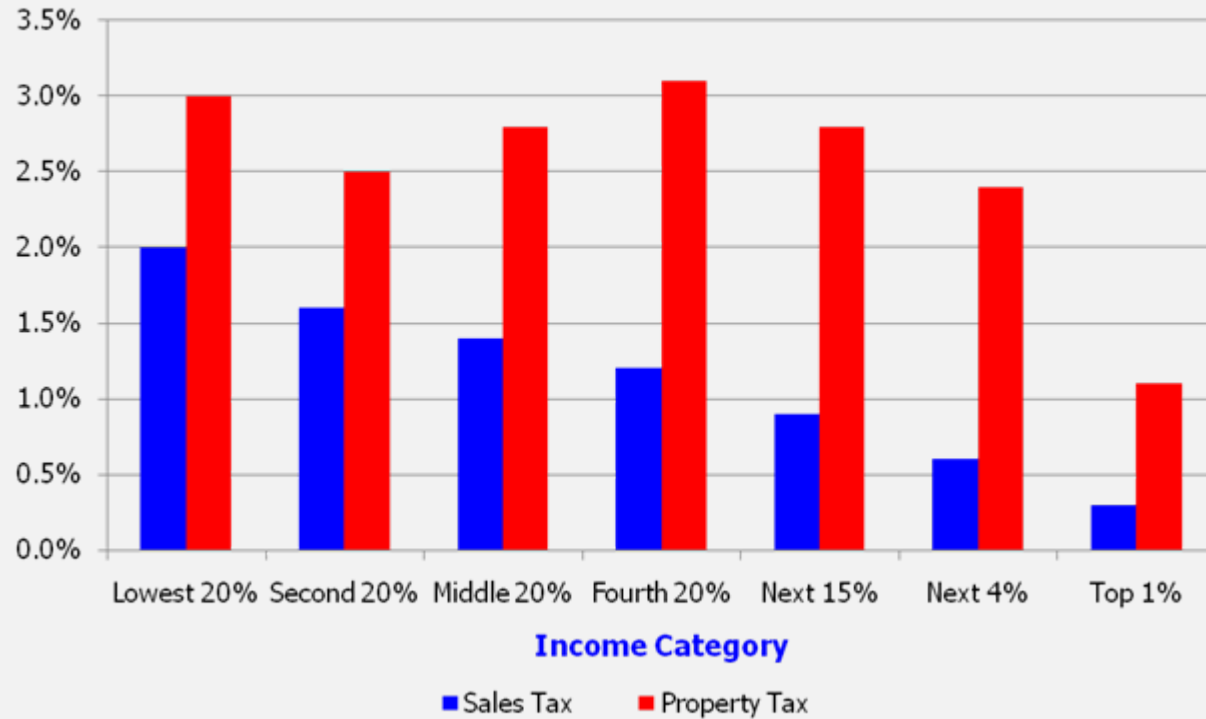


# **E. Equity By Income**

- **Retail sales component is regressive**
- **Sales tax on business purchases is also regressive**
- **Distribution of burden depends on tax base**

**Source: Derrick and Scott (1998)**

## Tax Burden (Massachusetts, 2002)

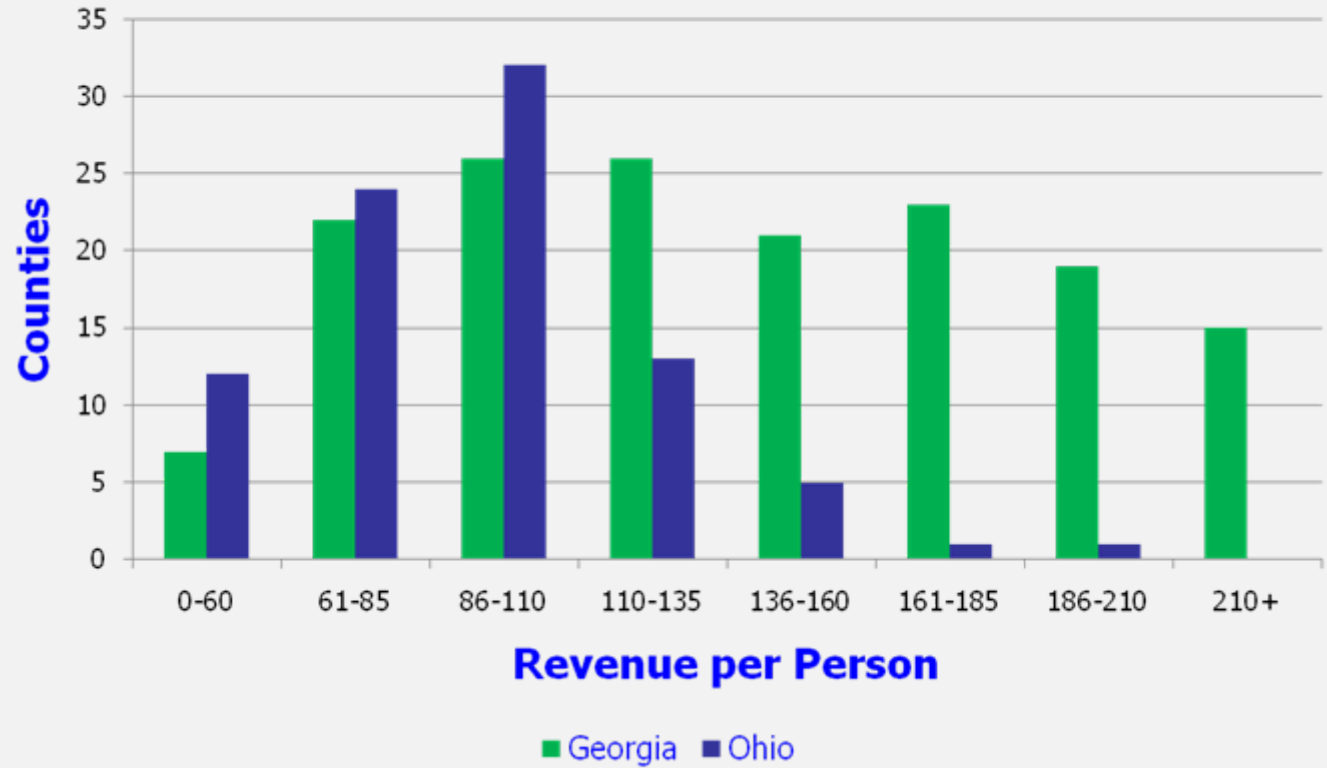


Source: *Who Pays? A Distributional Analysis of the Tax Systems in All 50 States*,  
Institute on Taxation & Economic Policy



## **F. Equity by Geography**

## 1% Sales Tax Revenue Per Capita (2006)



# Ohio



**County Tax Base Per Capita/  
State Tax Base Per Capita**

## **G. Effect on Tax Base**

**Increasing the total tax rate from 5% to 6% would reduce sales tax base by 11 percent.**

**Bruce, Deskins, and Fox (2006)**



## **III. Policy Issues**

# **A. Choosing Among Alternatives**

## **Alternatives:**

- **Local income or payroll tax**
- **Gross receipts tax**
- **Hotel/motel tax**



# Factors to Consider

- **Diversifies tax structure**
- **Relationship to benefits of public services**
- **Equity**
  - **By income class**
  - **Across jurisdictions**
- **Mobility of tax base**
- **Stability of revenue**
- **Economic distortions**
- **Ability to export burden to nonresidents**
- **Visibility of tax**

## **B. Policy Choices: Local Sales Tax**

- **Conformity with state base**
- **Universal versus local option**
- **Situs**
- **Coordination**
- **State v. local administration**



**Thank you**

**Questions?**

## References

- Bruce, Donald, John Deskins, and William Fox. 2006. "On the Relative Distortions of State Sales, Corporate Income and Personal Income Taxes." Working Paper, College of Business Administration, Creighton University.
- Bruce, Donald, William Fox, and M.H. Tuttle. 2006. "Tax Base Elasticities: A Multi-state Analysis of Long-run and Short-run Dynamics", *Southern Economic Journal* . 73(2): 315-341.
- Derrick, Frederick W. and Charles E. Scott. 1998. "Sales Tax Equity: Who Bears the Burden?", *Quarterly Review of Economics and Finance*. 38(2): 227-237.
- Dye, Richard F. and David F. Merriman. 2005. "State Revenue Stability: Alternative Conceptualizations", *Proceedings, 97<sup>th</sup> Annual Conference on Taxation*. Washington, DC: National Tax Association: 258-268.
- Jung, Changhoon. 2001. "Does the Local-Option Sale Tax Provide Property Tax Relief? The Georgia Case", *Public Budgeting & Finance*. Spring: 73-86.
- Lewis, Paul G. 2001 "Retail Politics: Local Sales Taxes and the Fiscalization of Land Use", *Economic Development Quarterly*. 15(1): 21-35.
- Sjoquist, David L., Mary Beth Walker, and Sally Wallace. 2005. "Estimating Differential Responses to Local Fiscal Conditions: A Mixture Model Analysis", *Public Finance Review*. 33(1): 36-61.
- Sjoquist, David L., Sally Wallace, and Barbara Edwards. 2004. "What a Tangled Web: Local Property, Income and Sales Taxes", in Amy Ellen Schwartz (ed), *City Taxes, City Spending: Essays in Honor of Dick Netzer*. Northampton, MA: Edward Elgar: 42-70.
- Wassmer, Robert W. 2002. "Fiscalisation of Land Use, Urban Growth Boundaries and Non-Central Retail Sprawl in the Western United States", *Urban Studies*. 39(8): 1307-1327.