# High-level feedback from Joint Fiscal Office and Legislative Counsel staff on Chapter 4 (formerly 3) – Consumption Tax -received by 12/10/2020

**Broadening the tax base – how much, how fast, and how it positions VT relative to other states**

- This chapter should emphasize that this is now the second time a commission has gotten together to evaluate the tax system and it's the second time, with completely different people, that a commission recommends the sales tax base be expanded. This is not a unique idea for the TSC. Two separate commissions with six different people from a variety of backgrounds all agreed that it doesn't make sense that the base isn't wider.
- As Janet Holtzblatt pointed out in the Zoom meeting earlier this fall, one initial step for Vermont would be to broaden the variety of goods in the consumption tax base to bring Vermont's narrow breadth closer to the middle-of-the-pack of states. She echoed the views of much of the economic and tax profession when she said she was not so enthusiastic about taxing necessary goods and services, including health care and education, given experience in other states.
- This chapter really glosses over the potential hurdles to such a sweeping proposal. In a sense, it is being too rational. For instance, it makes the point that businesses should be in favor of this because it treats everyone the same. If only it were so simple. When businesses who are not used to collecting taxes are subjected to new administrative duties, they get very angry. Massachusetts and Florida tried doing a rougher version of what this chapter is proposing and the laws were repealed within a couple years.
    - Relatedly, if this idea were adopted, Vermont would be the only state in the country with such a broad sales tax base, outside of maybe Hawaii and New Mexico. There are arguments why the broadest possible base is good tax policy, but accountants and businesses really hate when there are significantly different rules across states. Also, key legislators hate sticking out like a sore thumb when it comes to tax policy.

**Emphasizing the role of taxes in impacting consumer behavior and advancing the public good**

- In general, tax policy is a powerful tool that can encourage the consumption of public goods and discourage the purchase of public bads. That concept often gets lost in the discussion of raising revenue and not distorting consumer behavior throughout the chapter. In some cases, it's very much in the public interest to distort consumer behavior. Witness the cigarette taxes (both the sales tax and the excise tax) that played a big role in reducing smoking and thereby raising life expectancy and the quality of life.

**Taking care with citations and analysis**

- The piece makes references like "if we did this, we would raise $X number of dollars." It needs to cite something there, or at least include some analysis in the report. Either that, or say that the Commission estimates that it will be this much, showing it is the author's own analysis. Otherwise, it seems like it is being pulled out of thin air.
- The Kellogg study is more nuanced than indicated in the draft chapter. From the Kellogg study: "The researchers saw no impact on household spending habits four months to a

year after a sales-tax increase. But when they focused their "microscope" down to the month immediately before the change, as well as the month immediately after, they found that "all this anticipatory action occurs," Baker says. "It's only when you're able to zoom in on an actual month that you can actually see a very clear, very stark pattern of change in the way individual households spend their money."

- Price elasticity is discussed in the chapter as if it is one value that applies to all households. In fact, price elasticity for a consumption item can vary greatly across the income distribution. For example, the decision to visit the doctor when out-of-pocket costs are $300 could be much more problematic for a middle-income family not covered by Medicaid than for a high-income family. From the public health perspective, it's not desirable for any family to cut back on necessary health care.
  - It may be useful to apply the single price elasticity value when one is looking at the likely revenue to be raised from imposing a new tax on a particular item, but it is less useful when thinking about the equity implications.

**Considering general structure, flow, and content**

- The chapter meanders. The Introduction is really not an introduction- it's a discussion about the VAT and tax pyramiding. It gains structure in the sections where it asks questions about the sales tax, and then it goes on a long section about healthcare taxation, then quickly wraps up with M&R, and excises taxes (with a big recommendation in that section, despite the fact that it's only about a quarter page long).
  - The report could benefit from a small section on what exactly is the sales tax. It's a tax on tangible personal property (TPP), which necessarily does not include services. The chapter talks about healthcare, education, groceries, clothing being "exempt." That doesn't seem like correct wording. Clothing and groceries are exempt because they are TPP but specifically excluded from the base in statute, but healthcare and education are not "exempt," they are just not TPP and therefore not taxed, in the same way that a bike is not considered a motor vehicle and therefore not subject to the purchase and use tax.

**Checking for consistency with rest of report**

- Other sections of the report emphasize the value of conformity with other states and the risks inherent with being the only state to follow a particular approach. Should this chapter have a deeper discussion of how Vermont currently has one of the narrowest sales tax bases in the nation, but the commission's proposal would make its base far broader than any other state in the region (if not the nation)? If there is a reason that conformity is crucial in other areas but less important in this one, that would be good to address directly.

**On health care**

- Health care is a particularly complex subject and an issue which needs a deeper, more nuanced analysis than a broad-focused commission can be expected to deliver along with its high-level analysis of the State's entire tax system. The chapter proposes getting rid of the current provider tax, which is a tax paid by providers ~~(if they don't pass it fully onto consumers)~~, and replacing it with a 3.5% sales tax on the final purchase of healthcare goods and services, which would be more directly paid by the consumer? Could that kind of tax be fully passed through the chain of payers?

  - In order to be used as matching state funds that draw down federal Medicaid dollars, provider taxes are subject to CMS requirements (broadly based, uniformly applied, under 6%, clearly not holding anyone harmless, etc.) and have been carefully negotiated to maximize revenue while keeping Vermont in good standing with the federal government.
  - Medicaid-participating providers get some portion of the provider tax back through Medicaid rates, though we can't guarantee that they will be held harmless, while a sales tax that was not used for Medicaid match would not serve to enhance Medicaid reimbursement rates.
  - If provider taxes were pegged to a lower rate in order to match a reduced sales tax rate, it could potentially run into multiple problems simultaneously, including a) resistance from categories of providers currently taxed at a lower rate, b) administrative burden on categories not currently taxed, and c) lower revenue overall – a hole that would effectively have to be backfilled by other General Fund sources or through cuts in reimbursement rates and/or covered services.

- One thing missing from the analysis of what's involved in expanding the scope of the provider tax is the difficulty in determining net patient revenues (or a similar measure) for providers whose finances are not regulated by the State – i.e., the issue Nolan described with the dentists, which would also apply to independent physician practices, chiropractors, etc. Someone will need to track and collect that information, which will require resources and potentially new regulatory authority for some State entity.
- The report conducted by PHPG for DVHA back in 2011 (released 2012) is a useful reference document on all things provider taxes. The report also dedicates two chapters to the mechanics, considerations, and potential revenues for expanding the tax to the other classes of providers not taxed at the time. Keep in mind that the rates and estimates are a bit outdated.
  - Since the report was published there have been at least three instances when the legislature has addressed proposals for taxing new provider classes and/or changing an existing provider tax. These instances highlighted both the complexities and lessons learned regarding provider tax legislation and might be useful to address.

**Acknowledging the impacts of Covid-19**

- The Covid-19 recession may change many of our perceptions about the stability of the pieces of the tax base. We used to think that consumption of services was more stable than consumption of goods. Given the shutdown of the tourism industry, however, that perception may be on the chopping block. Similarly, we used to think of non-residential real estate as relatively stable but residential real estate as subject to housing booms and busts. Again, the Covid-19 recession has had the opposite effect in many markets. Such basic questions may be the starting point for the next Tax Structure Commission, but the questions need to be raised here.

**Considering sustainability**

- The "sustainability" goal deserves more discussion somewhere in the report. As used strictly in this report on tax structure, it refers to the long-term stability of tax revenues and the ability of the state to raise revenues sufficient to fund public goods and services. But sustainability also refers to the long-term viability of our economy and our environment. Hence one must be careful when raising taxes or fees on those households who choose to switch to electric cars. The "externalities" (effects on everyone in the state) should be considered in all cases, whether the choice is gasoline-burning or electric-powered vehicles. Of course, that full discussion is a complex one that deserves more than a sentence or two.
    - On a related note, NCSL recently released an interesting piece on how different states are choosing to raise revenue from owners of plug-in vehicles. Some are choosing a fee at the time of registration, and others are choosing Road User Charges or Vehicle Miles Traveled tax.