Tax Restructuring Policy Proposal

Sponsor(s): *Sen. Lincoln Fillmore*

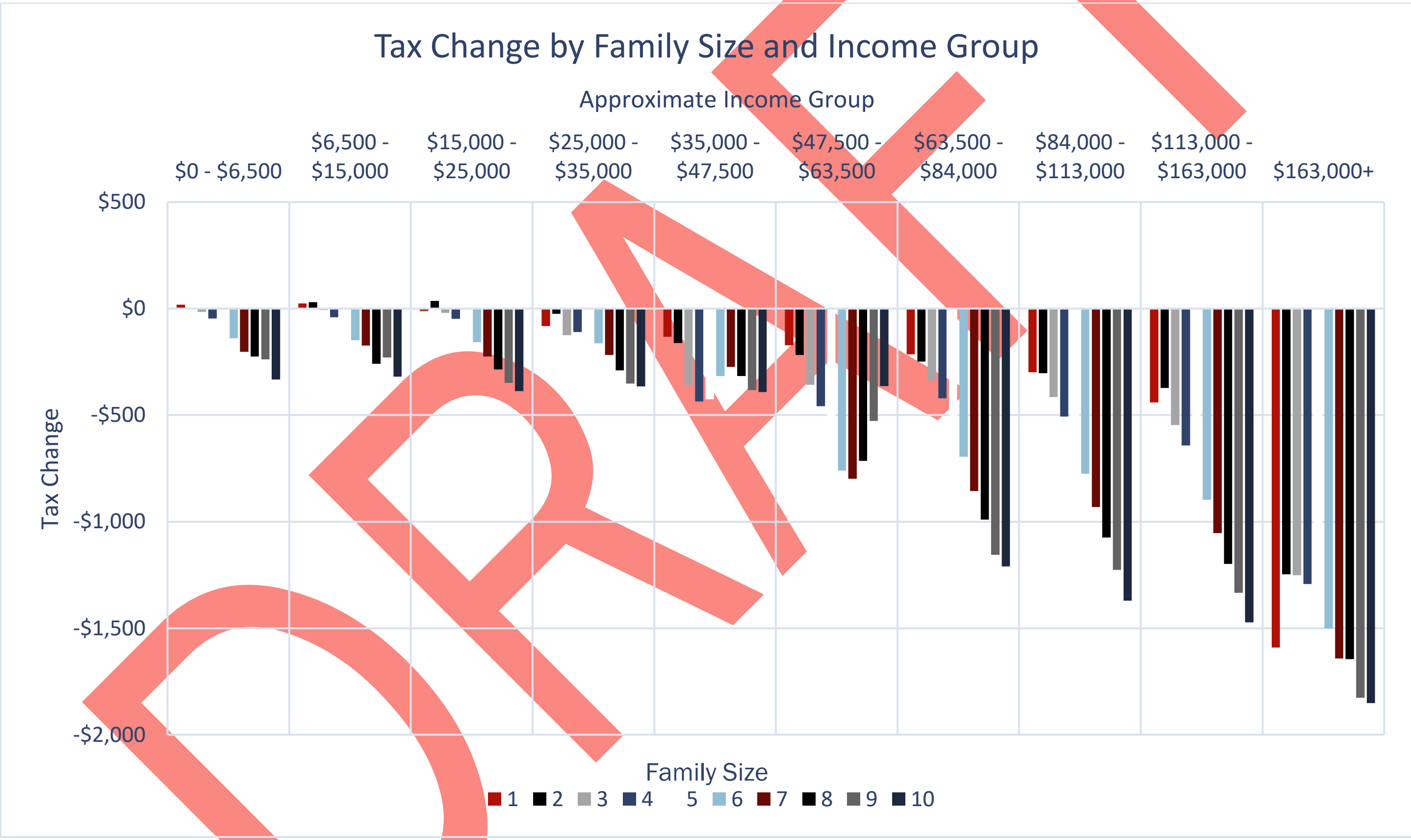
Executive Summary:

This proposal would take steps to address the state's structural revenue imbalance. The result of these policy changes would be a tax structure with increased flexibility for the Legislature in choosing how to fund state programs and a substantial net tax cut.

Budgetary Impact

- Results in an overall net tax reduction of approximately $420 million.
  - A family of four making $60,000 per year would see an estimated average total tax reduction of more than $450 per year

Incidence of Tax



Policy Impact:

- The sales tax base would be moderately increased and would better track ongoing changes in consumer expenditures.
- Impacts to lower-income and/or fixed-income residents from a higher sales tax rate on food would be mitigated by a Grocery Tax Credit, as well as an increased Utah Dependent Exemption and a new income tax credit for certain Social Security retirement income.
- Income tax rates would be reduced and revenue would no longer be constitutionally earmarked for education programs. Legislators would have increased flexibility in funding all government programs.

Policy Summary:

This proposal includes the following policy modifications:

Reductions

Income Tax

- Reducing individual and corporate income tax rates
- Expanding the "Utah Dependent Exemption" provision of the taxpayer tax credit
- Creating an income tax credit for certain Social Security retirement income
- Creating a "Grocery Tax Credit" for low-to-middle-income residents

Expansions

Sales Tax

- Restoring the full sales tax rate on unprepared food
- Expanding the sales tax base by charging sales tax on certain services
- Utilizing anticipated increases in sales tax revenue collected from online remote sales, as a result of recent changes in law, to help address the state's funding needs

Budgetary Flexibility

- Removing the constitutional restriction on income tax

Policy Description:

Reduce Individual and Corporate Income Tax Rates

- Reduce the state income tax rate to 4.50%

Expand the Utah Dependent Exemption

- Increase the exemption amount per dependent from $565 to $3,113
- Credit remains 6% of exemption amount
- Phaseout rate of credit remains $0.013 per dollar over:
  - $14,256 for single filers
  - $21,384 for head of household filers
  - $28,512 for joint filers
- Phaseout thresholds adjust for inflation

Create an Income Tax Credit for Social Security Income

- Non-refundable tax credit equal to total Social Security income included in Adjusted Gross Income (AGI) x State Income Tax Rate
- Amount of credit reduced by $0.025 per dollar that modified AGI (including Social Security and all other income) exceeds:
  - $24,000 for married filers filing separately
  - $30,000 for single filers
  - $48,000 for head of household or joint filers

Create a "Grocery Tax Credit" for Low-to-Middle-Income Residents

- $50 refundable income tax credit per household member
- Available to all filers with annual household income of less than $45,000
- In addition to the income parameters, to qualify, a claimant must:
    - Be considered a resident for income tax purposes
    - Not have been a convicted felon in state prison for any portion of the year
    - File a completed form with the Tax Commission
- A separate form will be created for claimants who do not have to file income taxes

Restore Full State Sales Tax Rate on Food

- The sales tax rate on unprepared food and food ingredients (e.g. groceries) would return to the full state sales tax rate of 4.85% from the currently reduced rate of 1.75%

Broaden the Sales Tax Base by Charging Sales Tax on Certain Additional Services

- Include certain services in the tax base to make the sales tax a broader consumption tax and providing more similar treatment to goods and services
- Newly taxed services would be those primarily consumed by the end user to minimizing tax pyramiding
- The following services would be included in the tax base:
    - Taxi and limousine service
    - Peer to peer ride sharing
    - Streaming media
- Sales or use tax would be due from the end user of these services if the end user is in Utah
- Businesses (whether in-state or out-of-state) providing the services would collect and remit the tax
- Businesses collecting and remitting the tax would be eligible to retain a portion of the sales tax collected as a vendor discount to minimize the compliance burden

Collect Additional Sales Tax Collected from Remote Sellers

- As compliance with recent changes in law increases, sales tax revenue from remote sales is likely to continue to increase

Remove the Constitutional Restriction on Income Tax

- Amend the Utah Constitution to allow for needed flexibility for funding all of state government

Fiscal Assumptions:

Estimated revenue impacts for FY2021 are based on the most direct data accessible assuming a certain set of assumptions. Data sources include the Utah State Tax Commission, the U.S. Economic Census, the Bureau of Labor Statistics' Consumer Expenditure Survey, and information collected and analyzed by the Office of the Legislative Fiscal Analyst.

Assumptions include the following:

- Estimates for the revenue from services are based on the 2012 U.S. Economic Census, grown forward to FY2021 using 4.6% assumed growth.
- Tax incidence modeling assumes percent of individual income spent on certain goods and services based on data from the Consumer Expenditure Survey.
- Tax incidence modeling does not account for effect on businesses. Businesses will benefit by approximately $25 million of the tax change. Businesses will be affected by the lower income tax rate, expansion of sales tax to services, and the sales tax on food. We do not have reliable data on the percentage of food or certain services purchased by businesses. Change in business tax incidence may affect consumers if businesses raise or lower their prices due to tax changes.
- The average decrease in total tax incidence may be slightly inflated due to the exclusion of non-resident filers in the average calculations of the food credit.
- The average decrease in household tax incidence is a sum of each individual component, independent of the other components of the proposal. A simultaneous model, including interaction between the components, may slightly change household tax incidence.