The Economic Impact of Repealing Mississippi's Grocery Tax

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Introduction

Mississippi is one of 45 states and the District of Columbia that levy sales taxes. The majority of states have reduced, eliminated, or developed mechanisms to offset sales taxes on food for consumption at home. According to the Center for Budget and Policy Priorities, 30 states and the District of Columbia exempt food purchased for consumption at home; five states tax groceries at lower rates than other goods; and five states tax groceries but offer tax credits or rebates to provide eligible households with relief on grocery sales taxes. Only three states, Mississippi, Alabama, and Arkansas, apply full sales taxes to groceries with no offsetting relief for lower income families. Generally, local governments follow the state policy on exempting groceries from sales tax, with the exception of Colorado, Georgia, Arizona, Louisiana, and North Carolina. In those states, groceries are still taxed by localities (Campbell, 2007).

During the 2007 session of the Mississippi Legislature, there was considerable discussion about repealing the statewide tax on grocery sales and raising the tax on tobacco products sold in the state. The proposal generated further discussions on the economics of this tax policy. Arguments for and against the proposal centered on the benefits and costs of repealing the grocery tax, but no significant empirical evidence was introduced to support these positions.

Proponents of repealing the grocery tax argued that this tax burden falls unduly on the poor. They said a grocery tax raises food prices and forces lower-income families to buy less food, which can lead to malnourishment. Since many economic and social indicators rank Mississippi at the bottom, repealing or reducing the grocery tax would create an "income effect" by raising the purchasing power of all Mississippi residents. For many, especially the poor, this relief would mean more household income to spend on other goods and services in the state.

Proponents desiring to repeal the grocery tax also argue that lower and middle income individuals and households are more likely to face fixed, inflexible budget constraints. Many families in these households cannot increase their spending when prices rise substantially because they tend to have saving rates that are either closer to zero or negative in some cases[1]. They tend to have little or no accumulated (liquid) wealth, and many have also "tapped out" any line of available credit. These households are not likely to have access to inter-family transfers of credit or cash, or intergenerational transfers of any significance. When gasoline or food prices rise significantly, these households are the most likely to face the difficult economic choices of either spending more of their income on gasoline for necessary travel and less on other taxable and nontaxable goods and services, or spending less on gasoline and more on goods and services (Casey and Stevens, 2005).

In an article published in April of 2007 by the Denver Post, David Migova expressed an opinion that these households don't pay taxes and the elimination of grocery sales taxes is nothing more than giving free money to people who don't pay the taxes. This statement is flawed to a certain extent. According to current data in the Consumer Expenditure Survey, low-income households in the United States spend about 64.98 percent of their food budget ($5,931) per year on food at home [1]. Approximately $3,854 is annually spent on food away from home.

1/ This study assumed that all increases in household income would be spent. This is consistent with the low savings rate (between 3 and 4 percent) among most Americans today.

Most low-income households qualify for food stamps in Mississippi ($2,484 for each recipient), which leaves a $1,370 food gap of taxable expenditures. Mississippi had 178,775 households that qualify to receive food stamps, according to the 2007 U.S. Department of Agriculture Food Stamp Report. This number multiplied by the food gap of $1,370 produced taxable grocery sales of approximately $245 million ($244.93 million) in 2006. Applying the statewide average grocery tax of 7 percent suggests these households paid more than $17.14 million in taxes during this period.

The continual climb of interest rates and fuel costs increases the price of new goods and services throughout the supply chain to the end-consumer. This circumstance also reduces the disposable income of consumers who have existing needs to heat their homes and fuel their automobiles (Patterson, 2004).

If the law requiring Mississippi to collect 7 percent sales tax on groceries was repealed without a means to off-set the loss of the grocery tax, the state would lose almost $237 million [2] in tax revenues in 2006. Totally eliminating the sales tax on groceries significantly reduces the amount of revenue the state collects. This scenario would not be good for Mississippi. An alternative to eliminating the grocery tax would be to implement the change over a period of several years.

This research paper was undertaken to quantify the impacts of this proposed tax policy after several editorials published in the Jackson Clarion Ledger and Hattiesburg American newspapers in Mississippi.

2/ Calculated from the 2006 Mississippi State tax Commission Service Bulletin and assume no other changes in tax policy.

Objectives

The primary objective of this paper is to evaluate the fiscal and economic impacts of repealing the statewide average food tax of 7 percent in Mississippi. The specific objectives are to:

1) Determine the impact of eliminating Mississippi's 7 percent grocery sales tax on the purchase of groceries.
2) Determine retail employment responsiveness to changes in grocery sales.
3) Determine how much state revenues would decline if the 7 percent grocery tax was repealed.

Data

Data used in the study consisted of secondary-time series data taken from multiple sources. Employment in grocery stores and other retail establishments were obtained from the Mississippi Employment Security Commission Covered Wages and Employment Report selected years. Information on grocery, total retail sales, and grocery sales taxes were obtained from the Mississippi State Tax Commission Service Bulletin for selected years. Population data was obtained from Woods and Poole Population Profiles for Mississippi, grocery expenditures from the 2005 Consumer Expenditure Survey, and household disposable income from the Iowa State Data Center and the South Carolina Statistical Abstract. The study was based upon statewide data since these statistics are readily available and more complete.

Methods

Analysis of the most recent Consumer Expenditure Survey data suggests that the propensity to purchase food for consumption at home from increased income is 5 to 10 percent (dependent upon income level and age group). This would leave 90 to 95 percent of the savings from not paying taxes on non-prepared foods available for other purchases

(Campbell, 2007). In 2005 and 2006, grocery taxes on groceries were $222.44 and $236.3 million respectively. If we use the upper end of the range spent from increased income due to the tax repeal, this would increase new purchases of groceries by $22.24 million in 2005 and $23.63 million in 2006. If the amount spent on additional groceries were accurate, then this suggests that $200.2 and $212.67 million would be available to spend on other goods and services during these periods in Mississippi.

A state-level, economic model of Mississippi (developed by the Minnesota IMPLAN Group, MIG) was used to estimate the impact of changes in grocery sales on the state's economy to capture the multiplier effects of repealing the tax policy in Mississippi. Specific impacts from this analysis include employment, sales, labor income, and government revenues.

Results

Concerns over the economic impact of declines in sales revenues have been a primary argument against repealing the grocery sales tax. The important role that grocery sales play in the state's revenue streams indicated a need for an empirical study of the effect of the tax policy on Mississippi's economy.

With the IMPLAN model, the study examined the overall economic impact using data on increased grocery sales and household disposable income resulting from the grocery tax elimination. This modeling system also indicate gains in employment associated with repealing the 7 percent grocery tax in the state. The authors formulated the overall economic impact using increases in grocery sales ($22.24 million in 2005 and $23.63 [3] in 2006) and increases in household disposable income ($200.2 and

3/ Figures obtained by multiplying 0.1 times $222.44million and $236.3 million, respectively.

$212.67 [4], respectively) resulting from the tax repeal. Since it should be pointed out that the proposed tax policy would only exempt grocery items and not other retail purchases expenditures households might make. These impacts were modeled in a stepwise fashion as listed above.

The first scenario model employed increased grocery expenditures to reflect the gain in sales of $22.63 million absent any taxes in 2006. Results suggest an increase of 607 total jobs (retail and other) because of these purchases in Mississippi (Table 1). These purchases represented the income effect associated with the tax policy. The study used the same procedure in the second approach and then increased household disposable income by $212.67 million during this same period in Mississippi [5]. The results show employment rose by 7,671, sales by $308.6 million, and labor income by $136.95 million in 2006 (Table 2). Although sales taxes associated with these purchases rose by $34.72 million, net state revenues from this policy declined almost $201.6 million during this period (Table 3).

Table 1. Economic Impact On Grocery Expenditures of Repealing Mississippi's 7% Percent Food Tax, 2006

Impact	Direct	Indirect	Total	Total Multipliers
Output	$23,630,000	$12,234,207	$35,864,207	1.52
Labor Income	8,013,601	3,822,194	11,835,795	1.48
Employment	480	128	607	1.26

Note: Indirect effects are the sum of indirect and induced effects in the model.

Table 2. Economic Impact On Other Retail Expenditures of Repealing Mississippi's 7% Percent Food Tax, 2006

Impact	Direct	Indirect	Total	Total Multipliers
Output	$213,630,000	$95,961,218	$308,591,218	1.44
labor Income	107,240,600	29,705,617	136,949,217	1.28
Employment	6,697	944	7,641	1.14

Note: Indirect effects are the sum of indirect and induced effects in the model.

Table 3. Economic Impact On State Revenues of Repealing Mississippi's 7% Percent Food Tax, 2006	
Tax revenues (loss)	-$236,300,000
Tax gain (from spending)	34,720,000
Net gain (loss)	(201,580,000)

Results from each of these analyses suggest there could be significant economic impacts associated with changes in grocery sales. The model indicated that Mississippi employment would increase by almost 8,248 percent because of the increase in grocery sales and other goods and services associated with removing the grocery tax.

The impact on employment is consistent with the opinion of the authors that increases in grocery sales and other goods and services would cause total retail employment to increase along with some off-setting declines in sales and employment in other areas of the state's economy. With grocery sales comprising a large share of retail sales in Mississippi, changes in the amount of groceries purchased in the state would have a major impact (either positively or negatively) on employment and taxes in the state. With the state loosing almost $202 million in tax revenues, it is not clear if the gains in employment would be enough to offset the revenue losses.

4/ Total income effect in each year subtracted from the additional amount spent on groceries in 2005 and 2006. Expenditures made with this income would be taxable.

5/ The study assumed all household groups would response similarly to price increases.

Conclusions

This study introduces empirical evidence to the debate on the effect of grocery sales taxes by employing analytical methods derived from extensive research on the economics of taxes.

The study quantified the degree to which grocery sales are affected by taxes and demonstrates how grocery tax revenues respond to changing levels of taxation. Most importantly, the study clarifies the impact of grocery sales on employment in Mississippi.

Results from the analyses indicate that repealing the 7 percent grocery tax would produce modest gains in grocery sales but major increases in the purchases of other goods and services. Revenues from the sale of additional groceries would be exempt from taxes, thus producing only employment and labor income. Because low-income households spend a larger portion of their food budget on groceries, the bulk of the tax savings probably would be allocated to this group. However, research suggests that these households spend between 10 and 12 percent of additional income on food. The rest is spent on other taxable goods and services. Finally, the authors conclude that increases in grocery sales would generate small employment gains, while sales of other goods and services would generate significant gains in employment, income, and other sales in Mississippi.

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