

Where Does MA Rank After Sales Tax Increase?

In 2009, Massachusetts revised its sales tax laws. Among the more important changes, the general sales tax rate was raised from 5 percent to 6.25 percent and alcoholic beverages were made newly subject to the general sales tax (separate from the longstanding *selective* sales tax already applied to alcoholic beverages).¹ These 2009 sales tax law changes will increase revenues in FY 2011 by approximately \$1 billion.² The specific components of this estimated \$1 billion increase include:

Regular Sales	\$633 million
Meals Sales	\$159 million
Motor Vehicle Sales	\$118 million
<u>Alcoholic Beverage Sales</u>	<u>\$110 million</u>
Total:	\$1.02 billion

State Rankings

As noted, Massachusetts' state sales tax rate is now 6.25 percent. This rate is similar to other southern New England states but higher than rates in northern New England. There is a range in state-level general sales tax rates across the rest of the US as well. California, for example, has a rate of 8.25 percent, while some other states have rates of 4 percent or lower.³

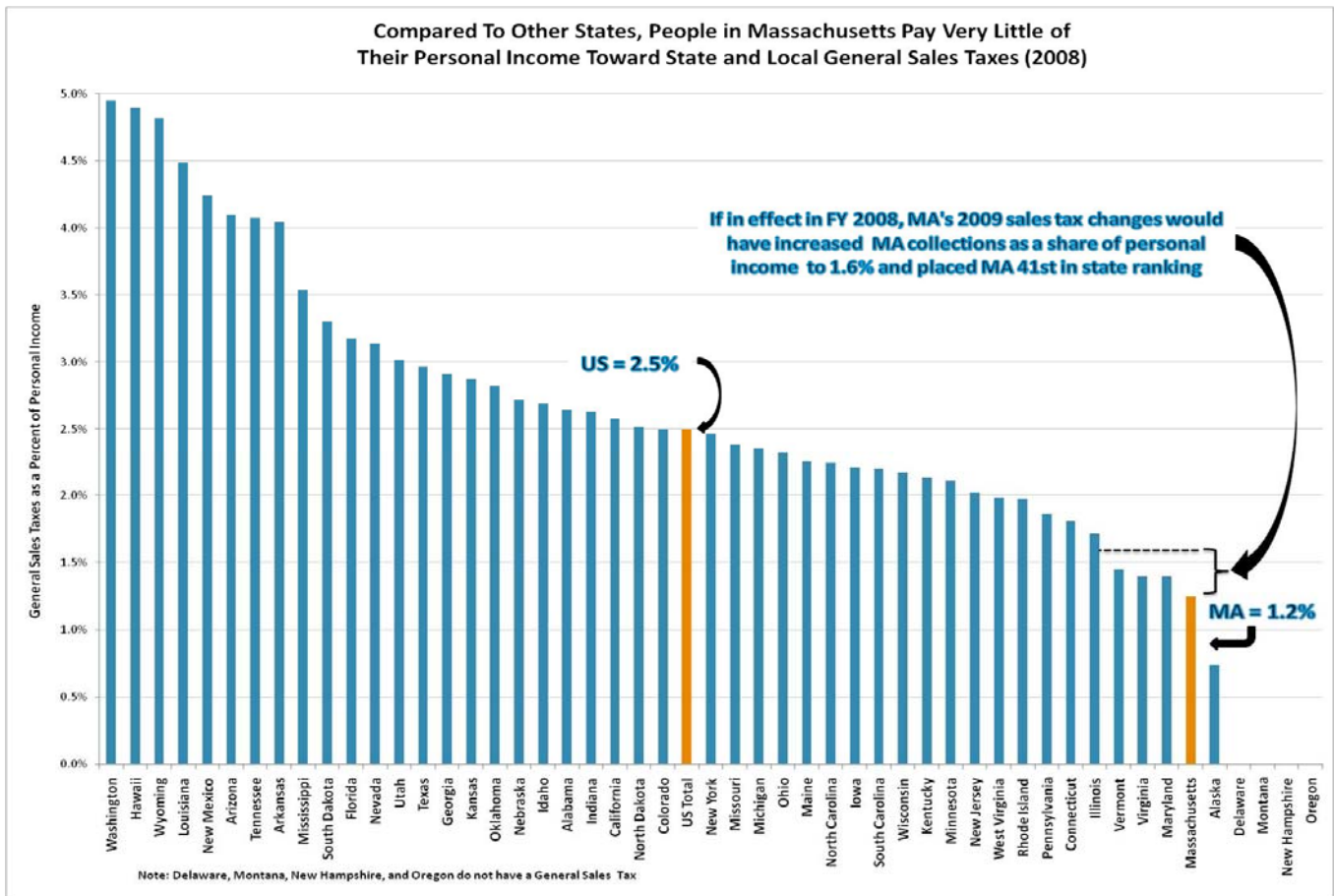
Tax rates themselves, however, are not an especially useful measure by which to compare the actual impact of taxes in different states. While only 12 states have state-level general sales tax rates equal to or higher than Massachusetts,⁴ a number of factors make the actual *impact* of the Massachusetts general sales tax smaller than in almost every other state:

- Massachusetts exempts many necessities from the general sales tax (including most food, clothing, prescription medicine, and home energy purchases).
- Massachusetts applies the general sales tax to far fewer services (as opposed to "tangible goods") than do many other states.⁵
- Massachusetts allows very little "add on" sales tax revenue to be collected at the local level through local option sales taxes. ⁶ (Unlike New York, for example, which has a 4 percent state sales tax with local option sales taxes of 3 percent to 5 percent added on top of the state tax, for a combined average rate of 8.3 percent.)⁷

The result of these features is that in Massachusetts a much smaller percentage of personal income is spent on general sales taxes than in most other states. General sales tax revenue in Massachusetts was equal to 1.2 percent of personal income in FY 2008,

placing the Commonwealth at a rank of 45th out of 46 states that levy a general sales tax (see Figure 1).⁸

Figure 1



These 2008 data, however, do not take into account the sales tax increases enacted in 2009. Had the 2009 general sales tax rate of 6.25 percent been in effect in FY 2008 (along with the other changes, noted above, that accompanied the rate increase), general sales tax revenue in Massachusetts as a percent of personal income would have been slightly higher, equaling 1.6 percent of personal income.⁹ This increase would have shifted the Commonwealth’s ranking from 45th to 41st among all states. Collectively, in all 50 states, general sales taxes accounted for 2.5 percent of personal income in FY 2008. Four states have no general sales tax.

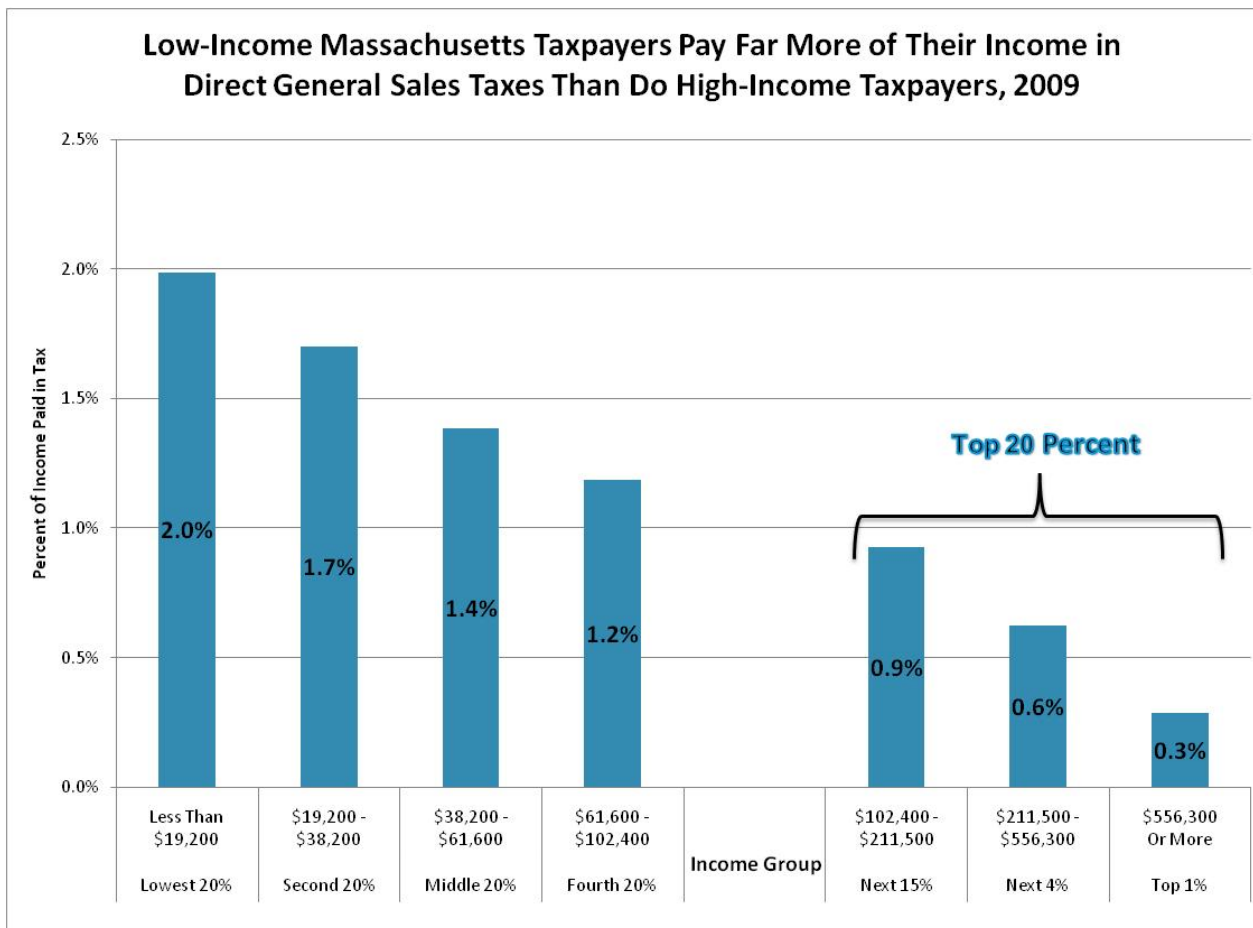
Who Pays The General Sales Tax?

Analysis performed by the Institute on Taxation and Economic Policy (ITEP) finds that, on average, in 2009 Massachusetts taxpayers in the lowest 20 percent of incomes paid 2.0 percent of their incomes in direct general sales taxes.¹⁰ The share of income going to direct general sales taxes drops off steadily as income rises, with the top 1 percent paying only 0.3 percent of their total income toward these taxes (see Figure 2, next page).

This can be explained by the difference between the consumption requirements of low vs. high-income taxpayers. People with low incomes usually must spend all of their income in order to make ends meet (or even more than their total income in some years, if borrowing and use of savings is taken into account). This means that much of their income becomes subject to the sales tax through the purchases they make. People with high incomes, by contrast, typically spend only a portion of their income, saving or investing the remainder.

The overall effect of the general sales tax therefore is regressive, with poorer people paying more of their income toward this tax than do richer people. At the same time, reducing the sales tax rate would reduce state revenues. Unless these sales tax revenue losses were offset with revenue increases (most likely from other tax sources), the state would have to reduce spending on programs and services, many of which directly benefit low and moderate income people.

Figure 2



¹ As part of the package of changes made to the sales tax in 2009, Massachusetts raised its “meals tax” rate from 5 percent to 6.25 percent as well. Though technically a separate tax, the meals tax - with a rate that matches that of the general sales tax -- effectively functions as one of several

components of the general sales tax. In addition to this change, the 2009 package also permitted local governments to adopt a “local option” meals tax of 0.75 percent. Revenues from this change will fund local government functions and are not included in the \$1 billion FY 2011 estimate of increased state-level revenues.

² From DOR revenue estimates as of July, 2010.

³ Ibid.

Four states (including New Hampshire) have no state-level general sales tax.

⁴ Ibid.

⁵ Federation of Tax Administrators, July 2008 Bulletin:

<http://www.taxadmin.org/fta/pub/services/btn/0708.pdf>

The Center on Budget and Policy Priorities estimates that Massachusetts forgoes hundreds of millions - if not billions - of dollars annually in potential sales tax revenue as a result of excluding so many commonly taxed services from its general sales tax (July 2009):

<http://www.cbpp.org/files/8-10-09sfp.pdf>

⁶ Along with the change in Massachusetts law that increased the state sales tax from 5 percent to 6.25 percent, localities were permitted to adopt both a “local option” tax of 0.75 percent on meals and raise their hotel room tax from 4 percent to 6 percent. As of November 2009, less than 20 percent of communities had adopted the increases. Massachusetts DOR Website:

http://www.mass.gov/Ador/docs/dls/publ/bull/2009/2009_15B.pdf

http://www.mass.gov/?pageID=dorterminal&L=4&L0=Home&L1=Businesses&L2=Current+Tax+Year+Information&L3=Recent+Tax+Changes%3a+Sales%2c+Meals+%26+More&sid=Ador&b=terminalcontent&f=dor_budget_updateFY2010&csid=Ador

⁷ Tax Foundation, *Updated State and Local Option Sales Tax*, October 2009:

<http://www.taxfoundation.org/files/ff196.pdf>

In another Tax Foundation report (“*Major Metropolitan Area Sales Tax Rates*”, August 19, 2010) Boston is found to be among the cities with the lowest overall sales tax rates (see Tables 2 and 3):

<http://www.taxfoundation.org/publications/show/26622.html>

⁸ In addition to the design features of the Massachusetts general sales tax that tend to reduce its impact on households (including exempting many necessities from the tax, excluding many services from the tax, and limiting local option taxes), Massachusetts also has high levels of personal income relative to other states which means that sales taxes as a share of income tends to be lower in Massachusetts than in other states.

U.S. Census Bureau, *State and Local Government Finances by Level of Government and by State: 2007-08*. The 2007-08 Census data is the most recent available:

<http://www.census.gov/govs/estimate/>

State personal income data is drawn from US Bureau of Economic Analysis data:

<http://www.bea.gov/regional/sqpi/>

⁹ This *MassBudget* estimate assumes no change in the collection totals of other states and no effect on consumer spending due to the tax increase in MA. We increase the Census’ 2008 MA sales tax revenue figure (\$4.098 billion) by 25 percent (to \$5.123 billion), add in an inflation adjusted \$190 million for the combined sales taxes derived from a) alcoholic beverage sales (\$99 million in 2008 dollars) and b) the local option meals tax (\$89 million in 2008 dollars), and divide by BEA 2008 MA personal income (\$329.8 billion).

¹⁰ ITEP analysis performed upon request by MassBudget, March 2010 (see *MassBudget’s Tax Primer*, Appendix B, at

http://www.massbudget.org/documentsearch/findDocument?doc_id=748&dse_id=1336