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TAX POLICY

State Tax Officials Have Concerns About a Federal Consumption Tax

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The Honorable Dan Rostenkowski
Chairman, Joint Committee on Taxation

The Honorable Lloyd Bentsen
Vice Chairman, Joint Committee on Taxation
Congress of the United States

This report provides an overview of state tax officials' concerns related to the enactment of a broad-based federal consumption tax, as determined by a survey of state tax policymakers and administrators. The report was prepared, not at your request, but pursuant to GAO's basic statutory authority. We undertook the effort to assist Congress in its consideration of options for reducing the federal budget deficit.

We are sending copies of this report to the Secretary of the Treasury and the Director of the Office of Management and Budget as well as to appropriate congressional committees and members of Congress.

If you have any questions, please call me on 275-6407. Major contributors to this report are listed in appendix VI.

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Executive Summary

Purpose

The objective of this report is to provide Congress with an overview of state tax officials' concerns related to the enactment of a broad-based federal consumption tax—in the form of a federal retail sales tax or a value-added tax. It presents the responses of state tax policymakers—Governors and their staff and chairs and staff of major tax policy committees of state legislatures—to a GAO questionnaire on their preferred revenue options for dealing with the deficit and their concerns regarding a broad-based federal consumption tax. In addition, it discusses tax design alternatives that may address these concerns. It also presents the responses of state tax administrators to a separate GAO questionnaire on the effects of a federal consumption tax on state tax program administration.

Background

GAO has previously issued several reports discussing consumption taxes. These reports discussed the various types of consumption taxes, the principal methods for calculating a value-added tax, and key tax policy issues U.S. tax policymakers would face if they consider a value-added tax based on insights from the international experience.

A value-added tax is a consumption tax collected on the difference between a business' purchases and its sales, otherwise known as the business' "value added." For example, if a business buys \$150 worth of materials and equipment and produces a product that sells for \$200, its value added is \$50. A 5-percent tax on the value added to this product would yield \$2.50 in tax revenue. The United States has very limited experience with value-added taxes, but they are widely used in other countries.

A retail sales tax is collected on the total price of a good or service at the time it is sold to the final consumer. Forty-five states have a retail sales tax, and in 1987 state revenue from general sales and gross receipts taxes amounted to 32 percent of overall state tax revenue.

Retail sales taxes and value-added taxes are collected at different stages of the production and distribution process. A retail sales tax is collected only once, when a good or service is sold to a consumer. A value-added tax is collected at various stages of production and distribution. Both taxes could raise about the same amount of revenue given the same tax rate and tax base.

Results in Brief

When asked what potential revenue sources the federal government should use to reduce the deficit, 54 percent of the policymakers selected existing federal taxes exclusively; 8 percent selected a broad-based federal consumption tax exclusively; and 18 percent selected both existing taxes and a new consumption tax. Only 20 percent did not select a revenue option, indicating the federal government should not raise taxes to reduce the deficit.

A broad-based federal consumption tax was opposed by over two-thirds of all state tax policymakers responding. Both a federal retail sales tax and a value-added tax were viewed as an intrusion into state tax programs. Policymakers were especially concerned about the impact of a broad-based consumption tax on their ability to increase the future revenue generated by their own state retail sales taxes. Other concerns included the possibility of increased federal spending and inflation, and the impact of a broad-based consumption tax on the poor, i.e., regressivity.

Designing a consumption tax to address state tax officials' concerns would involve trade-offs. For example, design features incorporated to reduce state regressivity concerns, such as exemptions or multiple rates, would add to administrative complexity and limit revenue. According to responding tax administrators from states with retail sales taxes, the impact of a federal consumption tax on the administration of their state tax programs would depend on the type of tax and its visibility to the final consumer.

GAO's Analysis

Forty-five percent of the policymakers indicated that additional revenue for deficit reduction should come from corporate income taxes. Thirty-seven percent would use individual income taxes. (More than one source could be selected by respondents.) Policymakers supported raising tax rates and broadening the base of both corporate and individual income taxes. (See pp. 14-16.)

Intrusion on State Revenue Source

Intrusion into a major state revenue source was cited as a concern by 80 percent of the policymakers opposed to a federal sales tax and 70 percent of the policymakers opposed to a federal value-added tax. This concern stems from the states' dependence on consumption taxes as well as the desire to maintain the independence of their state tax systems. (See pp. 16-18.)

Policymakers are concerned that a federal consumption tax could (1) limit the states' ability to raise additional revenue from state sales taxes, (2) pressure the states to alter their tax bases to conform with the federal tax base, and (3) confuse taxpayers about the distinction between state and federal consumption taxes. Offering to share federal consumption tax revenue with the states received little support. Less than a fifth of the respondents indicated they would reduce their opposition to a federal tax if states received a share of revenue. (See pp. 16-23.)

Effect on the Poor

Over half of the state tax policymakers responding were concerned about the regressivity of a federal consumption tax. A tax is regressive if low-income families pay a larger proportion of their income in taxes than high-income families. Several alternatives can be used for reducing the regressivity of a consumption tax, including (1) exempting basic necessities from the tax base or adopting multiple rates which would tax necessities at a lower rate than other goods, (2) providing a tax credit for low income taxpayers on their income tax return, or (3) raising entitlement payments and ceilings to compensate for the increased cost of the consumption tax. (See pp. 24-26.)

These alternatives have potential drawbacks, including increased administrative costs and reduced federal revenue for reducing or eliminating the deficit. (See pp. 27-29.)

State Tax Program Administration

Tax administrators from states with retail sales taxes varied in their opinions on how much a federal consumption tax would complicate the administration of their state sales tax programs. A federal sales tax was expected to have more impact than a value-added tax, and a visible tax more than an invisible tax. For a federal sales tax, 31 percent of the administrators expected the impact to be great, 26 percent placed it in the moderate category, and 43 percent predicted some to no impact. For a federal value-added tax, 59 percent expected no impact. (See p. 33.)

Recommendations

GAO is not making any recommendations.

Comments

Survey results were discussed with officials from the Advisory Commission on Intergovernmental Relations, the National Governors' Association, the National Conference of State Legislators, the National Association of State Budget Officers, and the Federation of Tax Administrators. The results generally confirmed what they perceived to be the concerns of their constituents.

Contents

Figures

Abbreviations

ACIR	Advisory Commission on Intergovernmental Relations
CBO	Congressional Budget Office
IRS	Internal Revenue Service

Introduction

Income taxes are the present principal source of federal revenue. Congress responded to concerns about the perceived unfairness of the income tax system by enacting the Tax Reform Act of 1986. The Act was designed to be revenue neutral, i.e., it provided no additional revenue to reduce the budget deficit or national debt. Because many members of Congress believe they made a tacit agreement with taxpayers to lower income tax rates in return for broadening the base, it may be difficult to reach congressional consensus on efforts to raise revenue by increasing income tax rates.

Explanation of Consumption Taxes

If changes to the income tax system are ruled out, a broad-based consumption tax represents one of the few single revenue alternatives for raising large amounts of revenue. A consumption tax is levied on taxpayers' expenditures for goods and services rather than on their total income. The part of the taxpayer's income that is saved is not subject to current taxation from a consumption tax. Some economists believe that this would induce people to save more and consume less. However, the evidence on the strength of this belief is inconclusive. Consumption taxes also differ from income taxes in respect to who is responsible for collecting and remitting tax payments—businesses rather then households. Another basic difference is that a consumption tax is levied on individual transactions without regard for the taxpayers' personal circumstances, and income taxes generally attempt to take these circumstances into account.

The two most commonly used broad-based consumption taxes are the retail sales tax and the value-added tax. A retail sales tax is imposed at the point of final sale and is generally collected by the retailer directly from the consumer. Currently, 45 states have retail sales taxes. In addition, many states' sales taxes are combined with local sales taxes, such as counties, cities, special districts, and transit authorities. For example, California has a 6 percent statewide sales tax rate. Of the 6 percent, 4.75 goes to the state, and the remaining 1.25 percent goes to the counties and cities. However, in several California counties the rate is 6.5 or 7 percent; the additional .5 to 1 percent is used to finance local transportation and other local government services.

A value-added tax is a multistage tax on goods and services. In principle, it is equivalent to a retail sales tax on goods sold to consumers, but it is calculated differently and collected at each stage of the production and distribution process. For each stage the tax is calculated as a proportion of the difference between the value of goods and services purchased and the value of goods and services sold. In effect, this difference is the measure of the value firms add to the goods and services they buy from suppliers. While the United States has very limited experience with value-added taxes, they are widely used in other countries. A comparison of some of the operational differences between a federal value-added and a federal retail sales tax is in appendix I.

A federal consumption tax could raise large amounts of revenue. The Congressional Budget Office (CBO) estimates that a comprehensive value-added tax imposed at a rate of 5 percent could raise $125 billion in 1992. Even if food, housing, and medical care were exempt, the tax could still yield $72 billion annually. A retail sales tax with the same tax base and rate could raise similar amounts. Table 1.1 compares selected federal revenue sources.

Table 1.1: Selected Federal Revenue Options for 1992

Dollars in billions

	Estimated added 1992 revenue from each option
Individual income taxes	
Raise marginal tax to 16 and 30 percent	$35.7
Add a 5 percent surtax	26.0
Eliminate deductibility of state and local income and property taxes	29.6
Consumption taxes	
Impose a 5 percent value-added or federal retail sales tax with comprehensive base	125.4
— with exemptions for food, housing, and medical care	72.0
— with low-income relief by increasing funds for social programs[a]	103.5

[a]Includes increased outlays for Food Stamps, Supplemental Security Income, and Aid to Families with Dependent Children.

Source: Revenue estimates from "Reducing the Deficit: Spending and Revenue Options - Part II," Congressional Budget Office, February 1989.

Objective, Scope, and Methodology

We have previously issued reports discussing consumption taxes. These reports focused on the various types of consumption taxes, the principal methods for calculating a value-added tax, and key value-added tax policy issues based on international experience.

Unlike the United States, most countries that have a national consumption tax do not have independent federal-state tax systems. Therefore, their tax systems do not have the complexities of overlapping governments. If the federal government were to adopt a broad-based consumption tax, the federal tax and a state retail sales tax would be in force in 45 states. In 1987, general sales taxes provided 32 percent of total state tax revenue. It is unclear what impact a federal consumption tax would have on state retail sales tax systems, but many people, including state policymakers, believe the states would resist a federal consumption tax because of its perceived potential impact on state tax systems and state tax prerogatives.

The objective of this report is to provide Congress with an overview of state officials' concerns related to the enactment of a broad-based federal consumption tax and of possible ways to mitigate these concerns. To address these issues this report

- identifies state tax policymakers' views about how to reduce the deficit, including their preferred revenue options;
- identifies the nature and extent of state tax policymakers' concerns related to a broad-based federal sales tax or value-added tax;
- discusses how to address policymakers' concerns through the design of the tax or other methods; and
- identifies state tax administrators' opinions on the effects of a federal consumption tax on state administration, revenue, and tax evasion.

To obtain state officials' views of a federal consumption tax and its potential impact, we sent 261 questionnaires to state policymakers (governors, state budget officers, state fiscal officers, and chairs of state legislatures' major tax policy committees) in all 50 states. We received 153 responses; 42 declined to answer; and 66 did not respond. We received at least one response from tax policymakers in 49 states. We also surveyed the 50 state tax administrators (using a different questionnaire) to assess their concerns about the impact of a value-added tax on state tax

[1] Choosing Among Consumption Taxes (GAO/GGD-86-91, Aug. 20, 1986). Tax Policy: Tax-Credit and Subtraction Methods of Calculating a Value-Added Tax (GAO/GGD-89-87, June 20, 1989). Tax Policy: Value-Added Tax Issues for U. S. Tax Policymakers (GAO/GGD-89-125BR, Sept. 15, 1989).

administration. We received 44 responses and 3 declinations. Three administrators did not respond. We entered the answers into a computerized database and analyzed them. Responses from policymakers are discussed in chapter 2, and responses from tax administrators are discussed in chapter 3. (See app. II for a detailed explanation of the questionnaire methodology.)

Part of our questionnaire analysis included, where appropriate, comparison of responses based on specific respondent characteristics. These included the following:

- the type of respondent—legislators (state senators, state representatives, state fiscal officers) versus executives (governors and state budget officers);
- the degree to which a state is dependent on individual income taxes for revenue;
- the degree to which a state is dependent on retail sales taxes for revenue.

The results are discussed in appendix III.

To identify ways of addressing policymakers' concerns, we reviewed published sources, including economic textbooks, government reports, professional journals, and accounting firm and trade association publications (see bibliography). To get a wide range of opinions on consumption tax issues, we met with academic experts and knowledgeable officials of several states.

Our work was done between January 1988 and August 1989 and in accordance with generally accepted government auditing standards.

Survey results were discussed with officials from the Advisory Commission on Intergovernmental Relations, the National Governors' Association, the National Conference of State Legislators, the National Association of State Budget Officers, and the Federation of Tax Administrators. The results generally confirmed what they perceived to be the concerns of their constituents.

State Tax Policymakers' Views on a Broad-Based Federal Consumption Tax

The majority of state tax policymakers responding to our questionnaire believed the federal government should use existing federal revenue sources to reduce the deficit.[1] Increasing existing income and excise taxes was preferred over a new broad-based consumption tax. Some policymakers also suggested such revenue sources as increasing user fees, having a national lottery, or charging the National Atlantic Treaty Organization for troops stationed in Europe. Only 20 percent selected no revenue option, indicating the federal government should not raise taxes for deficit reduction.[2] Several of these policymakers indicated that spending should be cut instead.

Both a federal retail sales tax and a value-added tax were perceived as intrusions into state tax programs. Policymakers were especially concerned about the impact of a broad-based consumption tax on their ability to increase revenue generated by their own state retail sales taxes. Other concerns included the possibility of increased federal spending and inflation, and the impact of a broad-based consumption tax on the poor.

A federal consumption tax could be designed to mitigate some state tax policymaker concerns. However, some mitigating features may produce other undesirable effects, such as increased administration costs and reduced revenue for federal deficit reduction.

Existing Federal Taxes Preferred Over Other Revenue Options

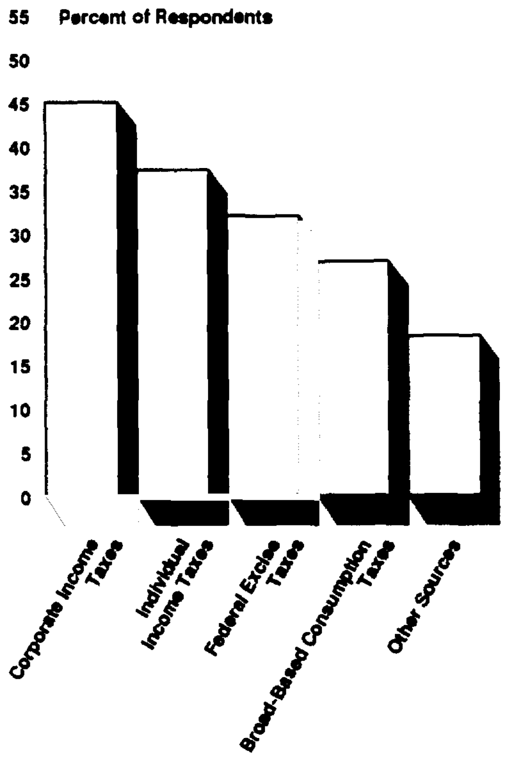
When asked which potential sources of additional federal revenue they preferred to be used to reduce the deficit, 72 percent of state tax policymakers responding selected existing federal taxes. Fifty-four percent selected existing taxes exclusively; 18 percent selected existing taxes and a broad-based federal consumption tax; and 8 percent selected only a consumption tax.

As illustrated in figure 2.1, corporate and individual income taxes were the revenue options chosen most frequently by state policymakers to raise revenue, followed by federal excise taxes and broad-based federal consumption taxes. Of the policymakers who chose a federal consumption tax, two out of three preferred a value-added tax over a federal retail sales tax.

[1] Includes governors, state budget officers, chairs of state legislatures' major tax policy committees, and state fiscal officers.

[2] An additional 10 percent of respondents indicated federal taxes should not be raised but also selected one or more revenue options for reducing the deficit.

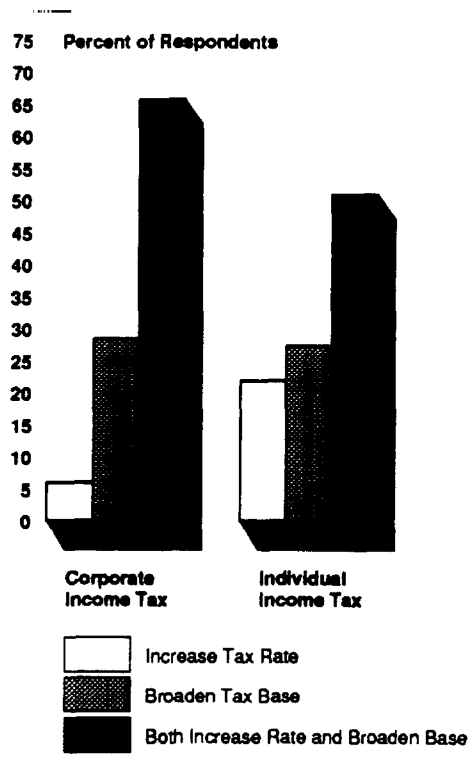
Figure 2.1: Policymakers' Preferences for Federal Government Deficit Reduction



Note: More than one revenue source could be selected by respondents.

Forty-five percent of the policymakers indicated that additional revenue for deficit reduction should come from corporate income taxes. Thirty-seven percent would use individual income taxes. As shown in figure 2.2, these policymakers supported raising tax rates and broadening the base of both corporate and individual income taxes.

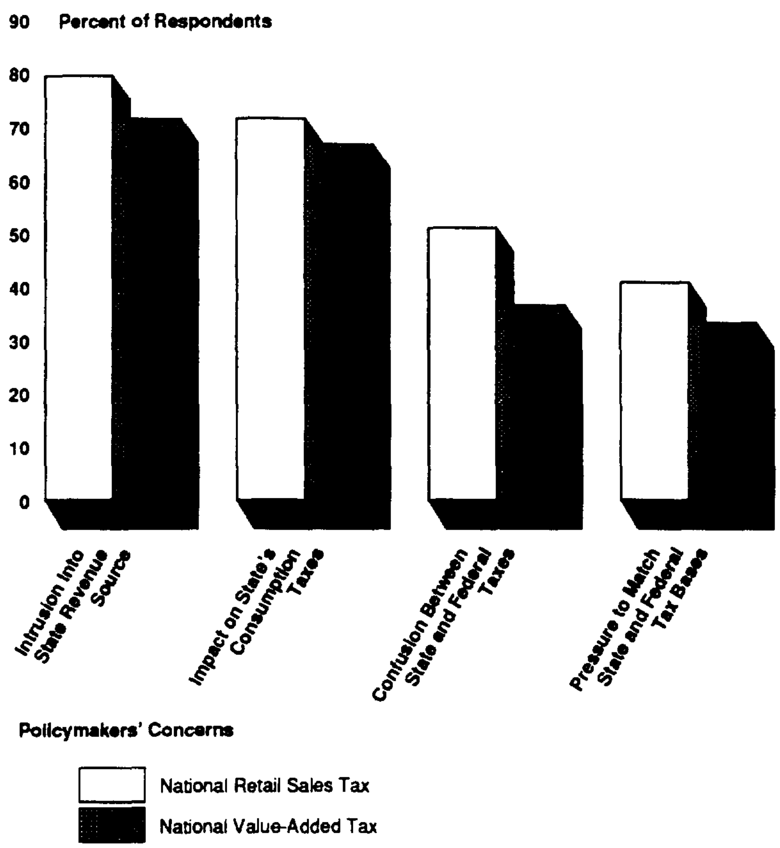
Figure 2.2: Policymakers' Preferences for Changing Corporate and Individual Income Taxes Expressed by Those Policymakers Favoring the Use of Those Taxes for Federal Deficit Reduction



Concerns Focus on Potential State Tax Program Impacts

Overall, state policymakers responding opposed a broad-based federal consumption tax. Eighty-one percent of the policymakers were opposed to a federal sales tax, and 68 percent were opposed to a federal value-added tax. Policymakers' most frequently cited concerns (as shown in figure 2.3) focused on the impact of a federal consumption tax on state tax programs. Specifically, 80 percent of the policymakers opposed to a federal sales tax and 71 percent of the policymakers opposed to a federal value-added tax cited intrusion into their traditional source of revenue.

Figure 2.3: Policymakers' Most Frequently Cited Concerns, Very Great or Great, About the Impact of a Federal Consumption Tax on State Tax Programs



State tax policymakers are very concerned about the federal government's budget policies that lead to higher national debt and annual deficits and their impact on state finances. Over the last few years, as the national debt increased, state and local governments have lost federal revenue sharing and have seen reductions in federal grant funds. In addition, the Tax Reform Act of 1986 reduced federal tax rates and broadened the tax base, in part by repealing a provision that allowed individual deduction of state sales taxes, thus creating the potential of increased resistance to state and local sales taxes. Finally, growing public opposition to increases in property taxes has left the state officials feeling they have few, if any, ways to increase revenue.

Therefore, the prospect of a federal consumption tax intruding into state revenue sources concerned state officials. A majority of the respondents were greatly concerned that a federal consumption tax could affect their ability to increase state retail sales taxes. Specifically, 80 percent of the policymakers from states with a retail sales tax indicated that a federal consumption tax could discourage their state from increasing their sales tax rate. Sixty-four percent of these policymakers indicated that a federal consumption tax could discourage their state from broadening their tax base. However, five out of nine policymakers responding from states with no retail sales tax indicated that a federal consumption tax would have little, if any, effect on their decision to adopt a state retail sales or value-added tax.

States' concern about federal intrusion is understandable given their reliance on retail sales taxes for revenue. States have used the consumption tax base extensively as a major source of state general revenue. In states with a retail sales tax, sales tax revenue represents approximately 31 percent of the total state tax revenue collected for fiscal 1987. This percentage has remained relatively stable around 30 percent since 1970. As shown below, 31 of the 45 retail sales tax states generated 30 percent or more of their tax revenue from retail sales taxes.

- Four states obtained over 50 percent of state tax revenue from state retail sales tax.
- Ten states obtained between 40 and 50 percent of state tax revenue from state retail sales tax.
- Seventeen states obtained between 30 and 40 percent of state tax revenue from state retail sales tax.

States May Be Pressured to Match Federal Tax Base

Policymakers felt the federal government would be encroaching upon state taxing autonomy by enacting a federal consumption tax. They were concerned that a federal consumption tax would put pressure on their state to match their state tax base with the federal tax base. One policymaker commented that a federal consumption tax would trespass on the states' tax base and would affect the states' independence and control over their revenue source. Another believed the federal consumption tax may have an "evening" effect: over time the bases of the federal and state retail sales taxes may move closer together—if the federal tax were a federal retail sales tax.

Interviews with other state officials and our literature review suggest that the tax base concern may also stem from some states' use of retail sales taxes to implement state social or economic policies or gain an economic advantage over other states competing for businesses to locate in their state. For example, Virginia exempted basic research, fish farming, and computer software from state retail sales tax in order to encourage certain industries to locate there. Nebraska exempted farm machinery from its sales tax base, so farm equipment dealers would not lose sales to a neighboring state that had exempted the same items.

Another viewpoint, expressed by ACIR,[3] suggests that a federal consumption tax may not be competitive with the state retail sales tax, particularly if the tax is an invisible value-added tax not separately identified in the final price.

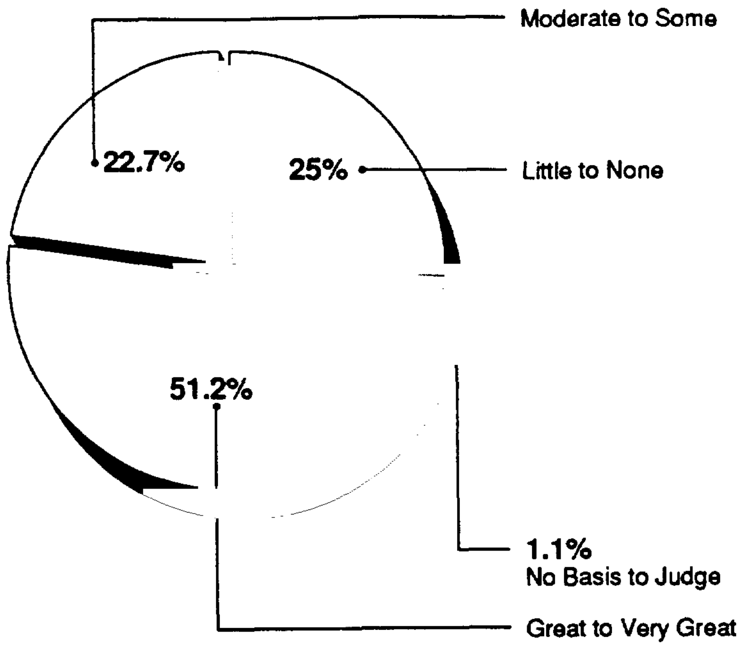
It can be argued that some states could realize revenue gains by replacing their current sales taxes with their own add-on to a federal consumption tax. States doing this could capitalize on the potentially broader base of the federal tax. If similar to federal consumption taxes in other countries, the federal consumption tax base would cover items not presently included in most state retail sales tax bases, such as professional and personal services.

Taxpayers May Confuse State and Federal Taxes

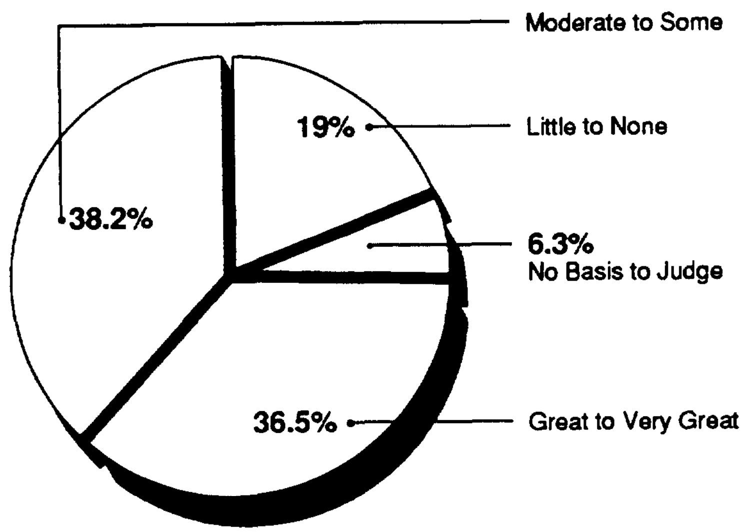
Another issue was potential taxpayer confusion between state and federal consumption taxes, especially for a federal retail sales tax. This concern focuses on difficulties that retailers and consumers may have distinguishing between the potentially different tax rates and tax bases. Figure 2.4 shows the degree of state policymakers' concern about taxpayer confusion of state and federal taxes.

[3]3Advisory Commission on Intergovernmental Relations, "Strengthening the Federal Revenue System: Implications for State and Local Taxing and Borrowing," pp. 89-96, Washington, D.C., October 1984.

Figure 2.4: Degree of Concern About Potential Confusion Between State and Federal Taxes If a Federal Consumption Tax Is Enacted



Federal Retail Sales Tax



Federal Value-Added Tax

Concern about taxpayer confusion may be well-founded. Eighty percent of the tax administrators responding to our questionnaire indicated that retailers are currently having some difficulty in determining which items are subject to the state retail sales tax. This is generally the result of the exemption of certain items from state retail sales taxes, and the taxation of similar products. This is discussed in more detail in the regressivity section of this chapter.

Interviews with some tax administrators indicated that, since state retail tax bases differ among the states, a federal consumption tax with a different base could cause confusion among consumers and among retailers collecting the tax. Confusion regarding which items are taxable under which tax system coupled with potentially different reporting requirements and the higher combined state-federal tax burden may create an opportunity for underreporting and tax evasion.

Mitigating Concerns Over Federal Intrusion Could Be Difficult

Because states have used the consumption tax base extensively as a major source of general revenue, mitigating state policymakers' concerns about intrusion could be difficult. Some experts believe this concern might be alleviated if any federal consumption tax proposal were coupled with provisions attractive to state governments. Such provisions might include sharing consumption tax revenue directly with the states, letting states piggyback onto the federal tax, or enacting legislation that would require out-of-state vendors to collect and remit state taxes on mail-order sales.

Sharing Consumption Tax Revenue

Of the large majority of state tax policymakers who opposed a federal consumption tax for deficit reduction, very few would reduce their opposition if offered an opportunity to share in the revenue generated. Less than 20 percent of the policymakers indicated their opposition would be reduced if the consumption tax revenue were shared without conditions or if the federal government agreed to pay a larger share of federally mandated social programs.

Piggybacking

Piggybacking was also rejected by most state officials. Piggybacking would allow states to add on a percentage to the federal consumption tax rate while the federal government administers and collects the entire tax and remits to the states their portion. Piggybacking would give the states added revenue without decreasing the federal revenue available for deficit reduction. As shown in table 2.1, only about 20 percent of the state tax policymakers expressed interest in piggybacking on either a federal sales or a value-added tax.

Table 2.1: State Officials' Interest in Piggybacking

Figures in percent

	Federal retail sales tax	Federal value-added tax
Definitely or probably yes	19.0	20.3
Uncertain	24.8	25.5
Definitely or probably no	45.8	43.1
No basis to judge	10.5	11.1
Total	**100.1[a]**	**100.0**

[a]Total does not add to 100 percent due to rounding.

Mail Order Sales

While not directly tied to the passage of a federal consumption tax, one option for increasing state sales tax revenue would be to include in the consumption tax legislation provisions which would allow states to require out-of-state vendors to collect and remit state retail sales taxes on mail order sales. This would provide states with additional sales tax revenue from their existing tax systems. States estimate that over $2 billion of sales tax dollars are lost because sales tax is not collected on these purchases. The state of Texas estimates that it loses about $130 million annually on mail-order sales and that local governments in Texas lose another $30 million.

State sales tax is a destination-based tax—it applies to imports (into the state) but not to exports. Goods shipped to out-of-state purchasers are commonly exempt from state sales taxes, and consumer purchases are commonly subject to the tax of the state of residence of consumers, with one exception. In National Bellas Hess,[4] a case decided in 1967, the Supreme Court decided that mail-order houses cannot be required to collect and remit sales taxes to the state of residence of a customer unless they have a business presence in the state.

Since the Supreme Court decision, a variety of bills have been introduced in Congress to resolve this issue. For several reasons, including a strong mail-order industry and a lack of consensus on whether local sales taxes should be included, none have been enacted. However, within the past few years, 21 states have passed statutes to extend their reach to out-of-state mail-order catalog firms. Further, 23 states have entered into regional compacts to cooperate on sales tax compliance. The purpose of many of these efforts is to test various aspects of the original

[4]National Bellas Hess, Inc. v. Department of Revenue of the State of Illinois, 386 U.S. 753, 1967

Bellas Hess decision before the Supreme Court. To date this has not taken place.

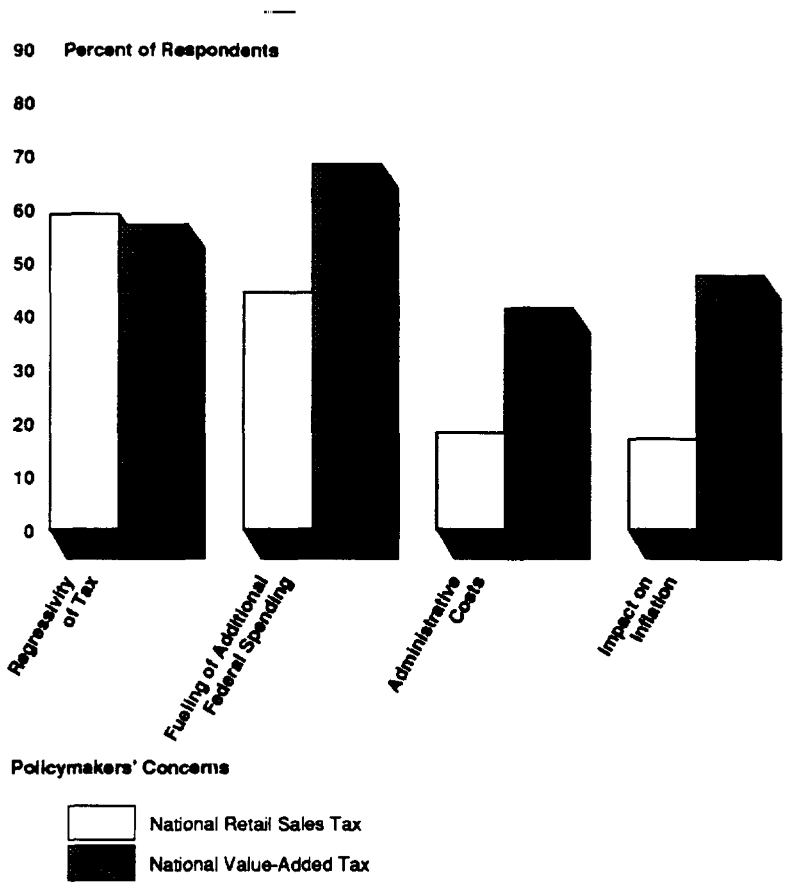
A federal consumption tax could be designed that would allow the states to make out-of-state vendors responsible for collecting and remitting state sales tax, whether or not the firm has a physical presence in a state. However, it is likely that these provisions would face the same obstacles as past proposals.

Other Frequently Cited Concerns of Policymakers

State policymakers' concerns went beyond the direct impacts a federal consumption tax could have on state tax programs (see fig. 2.5). Many policymakers were concerned

- about the potential economic impacts of a federal consumption tax on low income taxpayers;
- about the federal government's use of the revenue from a federal consumption tax for something other than to reduce the deficit;
- about the prospect of increased inflation; and
- about the cost of enforcing a new federal consumption tax, especially a federal value-added tax.

Figure 2.5: Policymakers' Other Frequently Cited Concerns, Very Great or Great, About the Impact of a Federal Consumption Tax



Regressivity

Almost 60 percent of policymakers indicated that they were greatly concerned about the regressivity of a federal consumption tax. A broad-based consumption tax on basic necessities would likely be regressive because lower income households spend a greater portion of their income on food, clothing, medical care, and shelter than higher-income households. Therefore, a broad-based consumption tax would fall most heavily on those taxpayers who are least able to afford it.

While there is little doubt that a single-rate, broad-based consumption tax is regressive, the degree of regressivity can vary depending on the time period over which the regressivity is measured. In general, the tax appears to be more regressive when taxes on annual consumption are compared with annual income. However, if taxes on lifetime consumption are compared with lifetime income, the degree of regressivity is generally reduced.

Mitigating Regressivity Concerns

Several methods could be used to offset the regressivity of a consumption tax. These methods include taxing necessities at a lower rate (a multiple-rate tax), refundable tax credits, and increased transfer payments.[5] However, each method has drawbacks either in terms of reduced revenue generation, more complicated administration, or the degree to which they address the regressivity concerns. For example, compensating low income individuals would reduce consumption tax revenue and using multiple rates would complicate tax administration.

Tax Necessities at a Lower Rate. In most European Economic Community countries, the value-added tax is made less regressive through the use of multiple rates which tax necessities at a lower or zero rate. Most state tax policymakers favored exempting from the tax base such basic necessities as prescription drugs, medical and dental services, food, household fuels, and housing.

CBO estimates that a broad-based federal consumption tax imposed at a rate of 5 percent could raise $125 billion in 1992. However, if food, housing, and medical care were removed from the tax base, it would yield $72 billion annually. Thus, if the government needs to raise $125 billion annually the tax rate would have to be almost doubled in order to raise the same amount of revenue. Also, because high income households spend a significant portion of their budgets on the low tax rate goods, one of the drawbacks of using multiple rates is that the offset to regressivity is not well targeted to low income households. The tax break is provided to anyone, regardless of income level, who consumes a good taxed at a low rate.

Multiple rates can also interfere with the neutrality of a broad-based consumption tax system. Goods with tax rates below the standard can become more attractive to consumers, and goods with above-standard rates can become less attractive. For example, a medicated shampoo that is considered a non-taxable medicine may be less expensive and have competitive advantage over a non-medicated shampoo that is taxable.

[5]Issues concerning and methods for mitigating the regressivity of the tax are discussed in more detail in our reports titled Tax Policy: Tax Credit and Subtraction Methods of Calculating a Value-Added Tax, (GAO/GGD-89-87, June 20, 1989) and Tax Policy: Value-Added Tax Issues for U.S. Tax Policymakers (GAO/GGD-89-125BR, Sept. 15, 1989).

Another drawback of multiple rates is the effort and costs of administration associated with this type of system. The federal agency administering the tax would be faced with the same administration problems facing the 28 states that exempt some foods from their retail sales tax bases. For example, New York does not tax food and medicine. As a result

- small marshmallows are not taxable because they are considered cooking ingredients (food), but large marshmallows are considered candy and taxed;
- a wafer covered with chocolate is taxable when put on the store shelves with candy, but it is considered a cookie and not taxable when shelved with cookies; and
- some items, such as soft drinks and plant seeds, are not taxable if purchased with food stamps, but they are taxable otherwise.

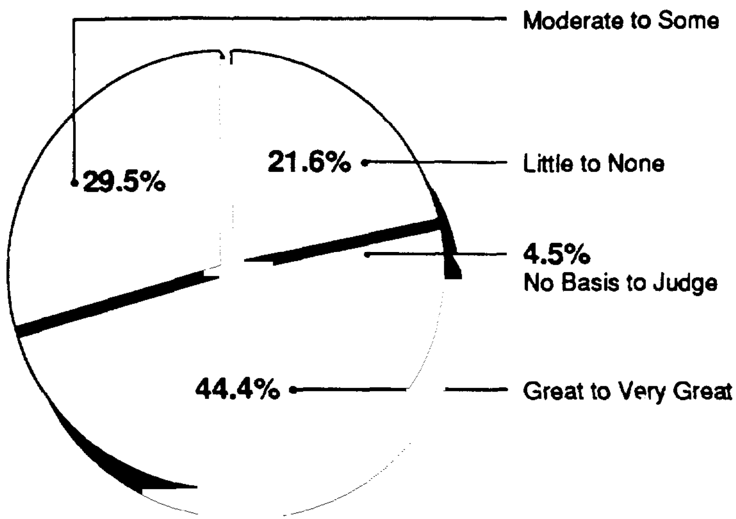
Increase Social Transfer Payments. Increasing transfer payments to low income individuals could also provide relief from the regressivity of the tax. Programs such as Aid to Families with Dependent Children and other social welfare transfer payments could be increased to compensate for the tax. Which programs are indexed would affect how well targeted to the poor this approach would be and the amount of additional revenue that would be needed to finance these programs. If limited to needs-tested programs, this method would better target the poor than if extended to all social transfer payments. This is because some payments, for example social security, go to eligible recipients, regardless of economic status.

Establish Refundable Income Tax Credits. A third alternative to reduce regressivity would be to establish a refundable income tax credit for consumption taxes paid. Taxpayers could use this credit to offset their income tax liability. Those who pay less income tax than the amount of the credit would receive a refund from the government. To reduce the amount of revenue lost, the credit could decline as income increases and disappear at a designated level of taxable income. A disadvantage of this alternative would be the increased number of taxpayers who would have to file returns, many of whom are not currently required to do so. Currently, eight states use some form of tax credit to offset the regressivity of their state sales tax.

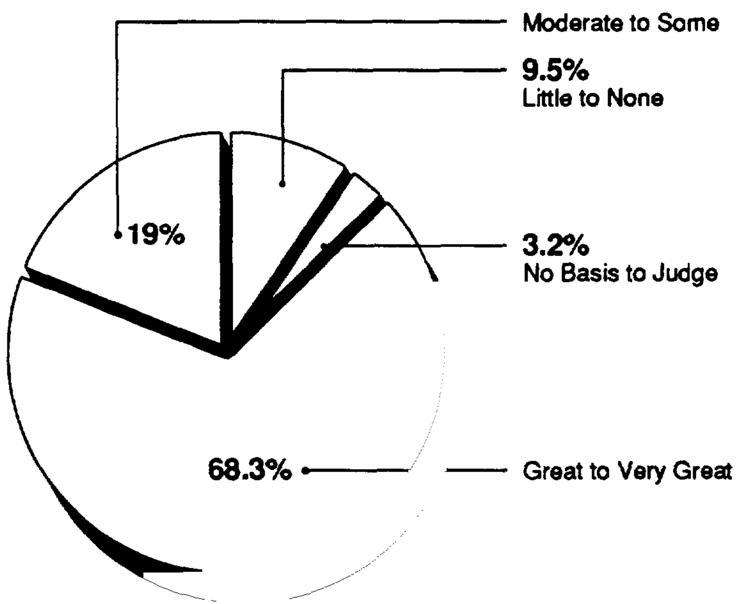
Revenue Might Not Be Used to Reduce the Deficit

As shown in figure 2.6, state policymakers were greatly concerned that revenue from a federal retail sales tax or a value-added tax might be used to finance additional federal spending, rather than to reduce the deficit. Most noticeably, a higher proportion of those opposed to raising federal taxes was greatly concerned that federal retail sales tax or value-added tax revenue might not be used to reduce the deficit. Several policymakers indicated that they did not "trust" Congress to earmark new funds for deficit reduction and that a federal consumption tax would only provide Congress with a new source of revenue for spending. Figure 2.6 illustrates that this perception of unchecked government spending seems to be more closely associated with a federal value-added tax than a federal retail sales tax. This viewpoint may stem partially from the influence of consumption tax opponents who oppose a federal value-added tax as a money machine that will fuel more spending rather than help to reduce the deficit, according to an interest group representative.

Figure 2.6: Degree of Concern About a Federal Consumption Tax Financing Additional Federal Spending Rather Than Deficit Reduction



Federal Retail Sales Tax



Federal Value-Added Tax

Mitigating Concerns That Revenue Might Not Be Used to Reduce the Deficit

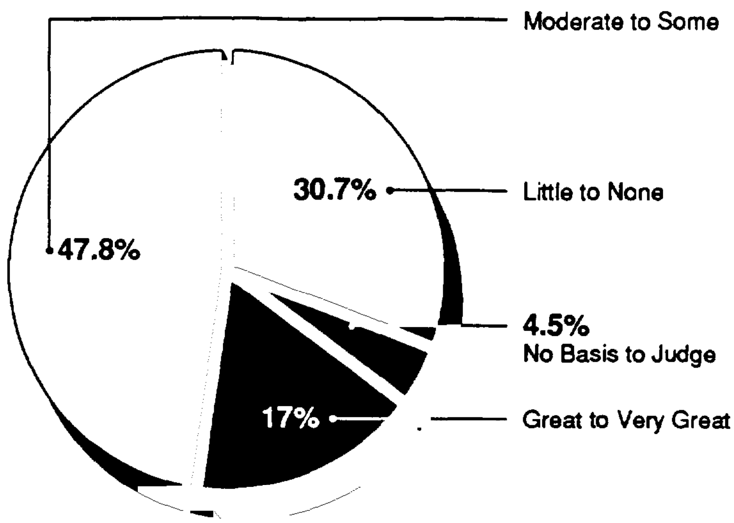
Several solutions may address the concern that a federal consumption tax might be used to finance additional federal spending rather than federal budget deficit reduction. These include (1) requiring the Gramm-Rudman-Hollings deficit reduction target of zero in 1993 to remain in effect with no changes; (2) reducing the debt ceiling each year by all or part of the revenue generated by the tax; and (3) making changes to the rate or base of the tax allowable only by a two-thirds vote of both houses of Congress. For example, in 1989 legislation was introduced to enact a value-added tax for deficit reduction. That legislation contained provisions requiring that revenue derived from the imposition of the value-added tax be deposited in a deficit and debt reduction trust fund. Money from this trust fund would be available only for payments on the principal and interest of the federal debt.

Adding these or other provisions to consumption tax legislation would provide some immediate assurance that the funds, for the most part, would be used to reduce the deficit. However, future Congresses could choose to change any such provisions. For example, the 99th Congress enacted legislation requiring the elimination of the deficit by fiscal year 1991. The 100th Congress extended the deadline for the elimination of the deficit to 1993.

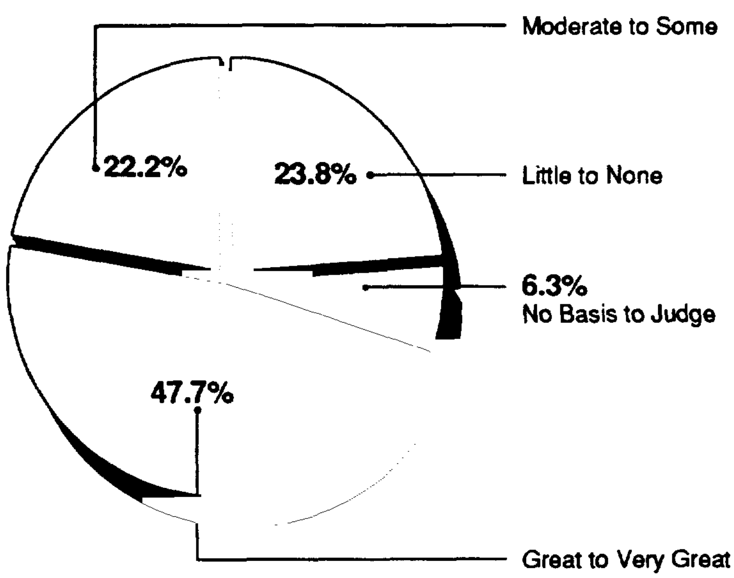
Possible Inflationary Impact

As shown in figure 2.7, inflationary impact was also an issue with state policymakers. As a consumption tax can be passed forward to consumers in the form of higher prices, the introduction of a broad-based consumption tax would probably cause a one-time increase in prices by the amount of the tax. This is not the same as an increase in the ongoing rate of inflation. This will increase the rate of inflation for about one year, but the rate of inflation should not be any higher in subsequent years than in the absence of a consumption tax.

Figure 2.7: Degree of Concern About the Impact of a Federal Consumption Tax on Inflation



Federal Retail Sales Tax



Federal Value-Added tax

Administration Costs

Many policymakers were concerned about the administration costs of enforcing a federal consumption tax, particularly with a federal value-added tax. In 1984, the Internal Revenue Service (IRS) estimated that a federal value-added tax would require 20,000 additional IRS employees, would cost about $700 million per year to administer, and would take about 18 months to implement. However, these estimates were made over 5 years ago, and according to IRS, assumptions about economic conditions and other variables are subject to change. In addition, Customs Service costs to administer border-tax adjustments[6] with a value-added tax would also have to be considered.

While there is no available estimate of the administration costs of a federal retail sales tax, some current literature suggests that a federal value-added tax would be slightly more expensive to administer than a federal retail sales tax. A federal value-added tax would require more information to be reported and processed than a federal retail sales tax. In addition to differences in staffing and equipment, cost differences would also depend on factors such as filing requirements.

Mitigating Concerns About Administration Costs

Administration costs would vary depending on the tax imposed, the breadth of the tax base, and methods that could be included to offset regressivity. International experience shows that the simpler the tax the easier and less costly to administer. This is consistent with the responses to our questionnaire. Almost all of the state tax policymakers and administrators agreed that a single-rate federal consumption tax with few or no exemptions would be easier to administer.

Conclusion

Most state policymakers responding to our questionnaire favored using additional revenue from existing federal tax sources to reduce the federal budget deficit. Eighty-one percent of them were opposed to a federal retail sales tax, and 68 percent were opposed to a value-added tax. Their major concern about a broad-based federal consumption tax is their perception that it would intrude on state tax systems and limit their ability to raise additional revenue from state retail sales taxes.

The effect of a federal consumption tax on state revenue is somewhat speculative and may ultimately depend on the type and design of the tax adopted. For instance, a relatively low rate, invisible value-added tax may not affect state sales tax revenue. Also, states could be given

[6] Border tax adjustments are attempts by countries using a consumption based value-added tax to remove the tax from goods that are exported and apply it to goods that are imported.

opportunities to realize added revenue by adding on to a federal tax. but the independence of their own tax systems could be reduced—a concern that could be difficult to mitigate.

State officials also were troubled by the potential regressivity, the potential impact on inflation and increased federal spending, and the administration costs of a broad-based consumption tax. These concerns could be addressed but would involve trade-offs between competing concerns in the design of the tax.

Tax Administrators' Views on a Broad-Based Federal Consumption Tax

According to responding state tax administrators from states with retail sales taxes, the impact of a federal consumption tax on the administration of their state tax programs would depend on the type of tax and its visibility to the final consumer.[1] An invisible tax was expected to have less impact than a visible tax, while a federal retail sales tax was expected to have more impact than a value-added tax.

While there was no clear consensus on whether a federal consumption tax would complicate state tax administration, in general tax administrators indicated that a federal consumption tax would have some impact on their state's existing tax program's revenue, evasion rate, and administration costs. The tax administrators overwhelmingly responded that each level of government should collect its own tax.

Impact on State Tax Administration

Tax administrators from retail sales tax states varied in their opinions about how much a federal consumption tax would complicate the administration of their sales tax programs. A federal sales tax was expected to have more impact than a value-added tax. For a federal sales tax, 31 percent of the administrators who had a basis to judge expected the impact to be great; 26 percent placed it in the moderate category; while 43 percent predicted some to no impact. For a federal value-added tax, 59 percent expected no impact and 22 and 19 percent expected moderate or great impact, respectively.[2]

Impact on State Tax Revenue

State tax administrators believe that the visibility of the federal consumption tax will determine whether state sales tax revenue will be affected. As shown in figure 3.1, when asked what impact a federal consumption tax would have on state retail sales tax revenue, almost half of the tax administrators indicated that a visible retail sales tax[3] would probably decrease state revenue, and 13 percent believed revenue would increase. If the retail sales tax were invisible to the final consumer, 25 percent thought revenue would decrease, but 28 percent believed

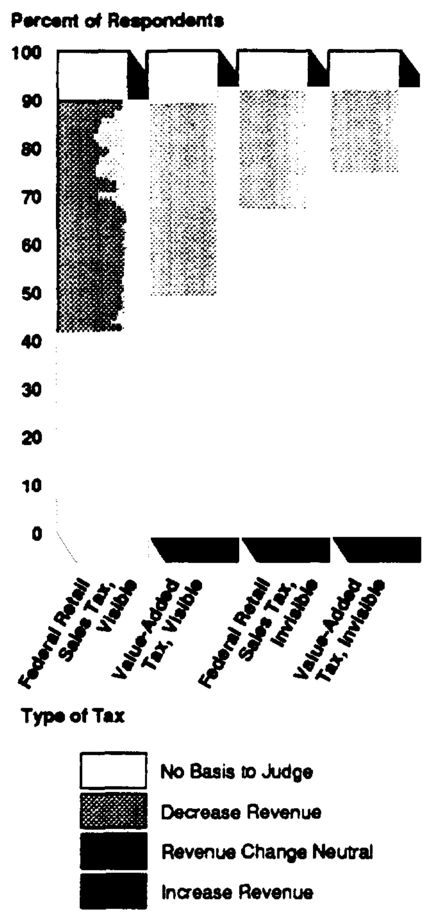
[1] Responses from tax administrators in the five states without a sales tax were from such a small population and so diverse that they could not be effectively analyzed.

[2] Percentages do not include respondents who indicated they had no basis to judge how much a federal consumption tax would complicate the administration of their state sales tax.

[3] An "invisible" tax would be included in the price of goods and services before the sale and would therefore be less noticeable to a consumer than a "visible" tax which would be added to the price of goods and services during the sale. For discussion of visibility and value-added taxes see Tax Policy: Tax-Credit and Subtraction Methods of Calculating a Value-Added Tax (GAO/GGD-89-87, June 20, 1989).

revenue would increase. Eighteen percent indicated that they believed an invisible value-added tax would decrease state sales tax revenue, and 31 percent thought they would increase.

Figure 3.1: State Tax Administrators' Concerns About the Impact of a Federal Consumption Tax on State Sales Tax Revenue

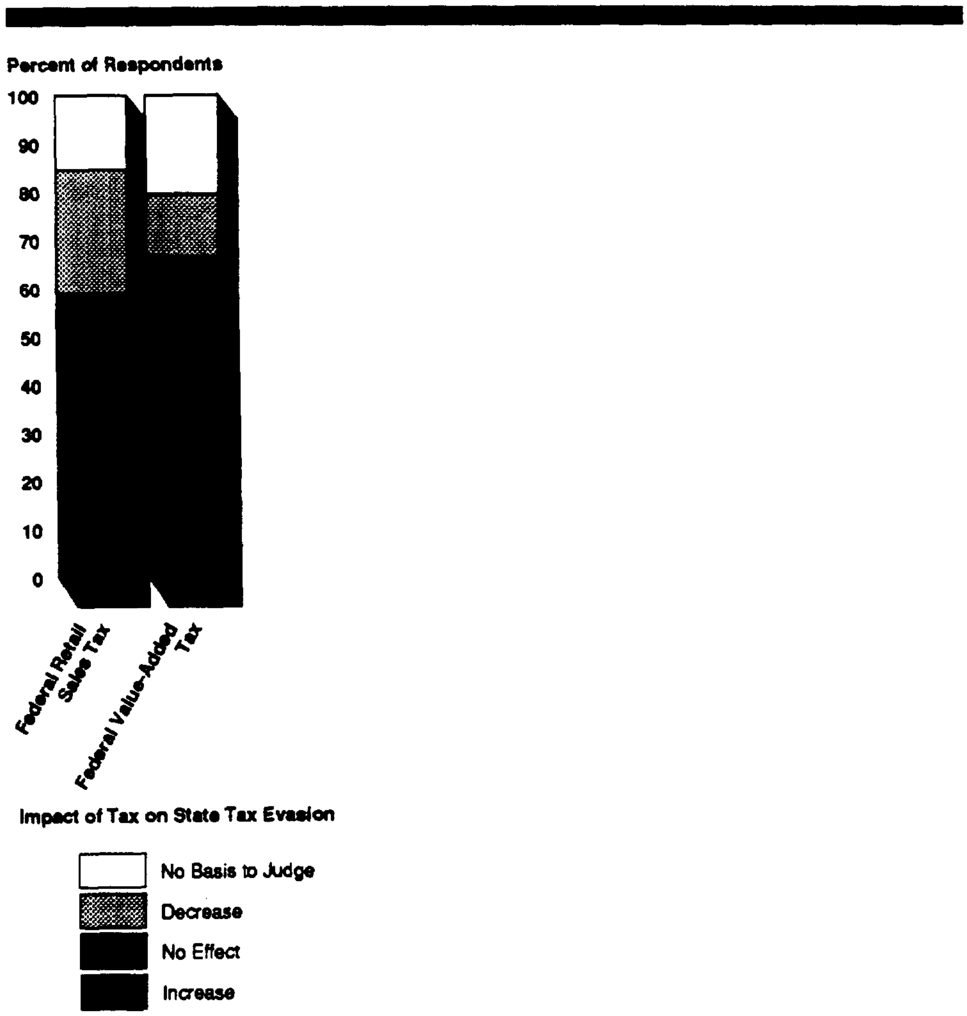


State tax revenue may be expected to decrease with a visible tax because the higher combined federal-state tax rate would make tax evasion more financially attractive, according to our discussions with some state tax administrators and officials. Other tax administrators may have thought that revenue would increase because of the federal audit presence in the consumption tax area, and for an invisible tax, because the federal tax may be included in the state tax base, according to an interest group representative.

Impact on Sales Tax Evasion

There was also no clear consensus among the state tax administrators about the impact of a federal consumption tax on state sales tax evasion rates. About 40 percent of the tax administrators from retail sales tax states indicated that a federal retail sales tax would decrease or not affect their state retail sales tax evasion rate. An equal number believed that tax evasion would increase. With a value-added tax, 51 percent of the administrators thought state sales tax evasion rates would either decrease or not be affected, and 28 percent believed evasion would increase (see fig. 3.2).

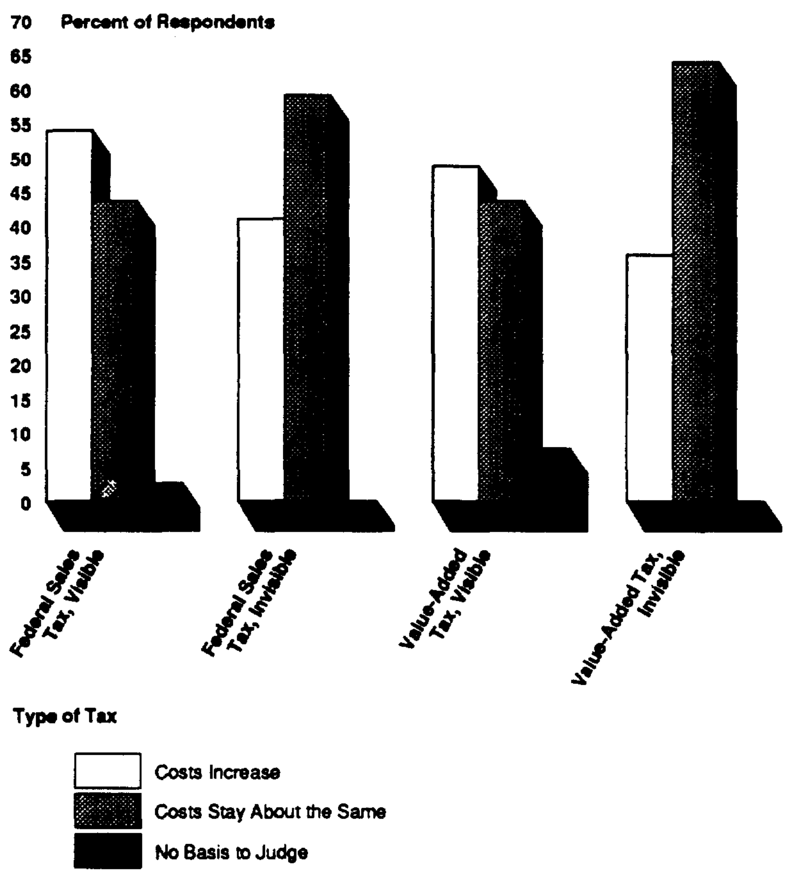
Figure 3.2: State Tax Administrators' Concerns About the Impact of a Federal Consumption Tax on State Tax Evasion



Concerns About Administration Costs

Although no tax administrators thought administration costs would decrease, about 60 percent of them believed that administration costs of the state retail sales tax would stay about the same with an invisible federal consumption tax. For a visible federal consumption tax, the respondents were nearly split between the opinions that state administration costs would increase or remain the same (see fig. 3.3).

Figure 3.3: State Tax Administrators' Concerns About the Impact of a Federal Consumption Tax on States' Costs to Administer State Sales Taxes



Joint Collection Not Recommended

According to most tax administrators, the most efficient manner of collecting consumption taxes is for the states to collect state taxes and the federal government to collect federal taxes. For a federal sales tax, 69 percent of them said the federal and state governments should each collect their own tax; for a value-added tax the percentage increased to 90 percent.

Ten administrators indicated that it would be most efficient for their state to collect both state and federal sales taxes. Only two administrators indicated that the federal government should collect both the state and federal taxes if a federal value-added tax were enacted. Lack of interest in federal collection of state taxes is not surprising, since none of the states have applied for federal collection of state individual income taxes, an option provided in section 6361(a) of the federal tax code as of October 1972.

Conclusion

According to responding tax administrators from states with retail sales taxes, the impact of a federal consumption tax would depend on whether the tax was visible or invisible and whether it was a sales tax or a value-added tax. An invisible value-added tax was expected to have less negative impact on state tax programs, and a visible retail sales tax was expected to have greater negative impact on state tax programs.

In general, tax administrators indicated that a federal consumption tax would have some impact on their state's existing tax revenue, evasion rate, and administration costs. The tax administrators responded that each level of government should collect its own tax.

Operational Differences Between a Federal Retail Sales Tax and a Value-Added Tax

The federal retail sales tax and the value-added tax are taxes on the consumption of goods and services and have similarities and differences. Both could raise about the same amount of revenue, assuming the same tax rate and the same tax base. The operating assumption of policymakers and economists is that either tax would be fully shifted forward onto the consumer in some form or another. The final after-tax price of the product to the consumer may be the same for both taxes, but the operating procedures of the two taxes differ.

These operating differences may have important policy implications and include such factors as administration costs, tax collection, enforcement, broadness of tax base, implementation time, evasion, and flexibility. In addition, as the total taxes (federal, state, local) on consumption increase (whether value-added tax or federal retail sales tax), the more attractive tax evasion becomes. This may result in lower voluntary compliance and higher administration costs.

Following is our discussion about how each type of federal consumption tax (retail sales or value-added) may have some comparative advantage over the other, given the following assumptions: (1) the federal consumption tax will be a tax in addition to existing federal taxes and will not replace any current taxes; (2) compliance cost is defined as the cost incurred by businesses to comply with the new tax; and (3) the tax base is broad and includes all goods and services, except those related to financial institutions, education, religion, and housing rentals.

Administration Costs

A federal sales tax is assumed to be less costly to the business community as a whole because only those businesses selling at retail would have to collect the tax. Under a value-added tax almost all businesses would have to collect. Administration costs are also believed to be lower for a sales tax, primarily because fewer businesses would be collecting the tax.

Compliance Costs

For the business community as a whole, a value-added tax would probably have higher compliance costs than a federal retail sales tax because almost all businesses, not just retail businesses, would collect taxes. If a credit value-added tax is implemented,[1] most businesses would have to keep invoices for all sales to and all purchases from other firms. These invoices would be subject to audit by tax authorities. The subtraction method value-added tax would require less documentation. If certain items (such as food, clothing, and shelter) were taxed at a lower rate or not at all, compliance would be more complex, and costs would potentially increase for businesses that sold both taxable and non-taxable items. If multiple rates were used to offset regressiveness, complexity would again increase and affect compliance costs.

Ease of Collection

The federal retail sales tax might have an advantage over the value-added tax if federal and state sales taxes could be collected jointly—either by the state or the federal government. Realistically, however, states impose sales taxes on different items (some tax almost all goods and services; others tax only certain items) and at different rates (3 to 7.5 percent). To have an efficient collection process, all 45 states with a retail sales tax would have to conform their sales tax bases to the federal government's base.

Start-Up Time

The biggest advantage a federal retail sales tax may have is the estimated time it would take to implement it. A sales tax should not have a long implementation period because it would fall mainly on retail outlets in 45 states that currently charge state and local sales taxes. States and retail businesses are familiar with the sales tax concept. Value-added tax is a new concept to the United States, and many businesses are not familiar with this form of taxation. The IRS estimates it could take 18 months from time of enactment to implement a value-added tax.

Enforcement

With a credit value-added tax, firms have a financial interest in ensuring that the amounts of value-added tax paid on purchases made in producing a good or service are accurately reported on their invoices, since they receive credit against their value-added tax liabilities for previously paid value-added tax. This self-enforcing feature not only

[1] Credit and subtraction are two ways of calculating a value-added tax. Under the subtraction method a firm calculates its value added by subtracting its total purchases from its total sales. Then it calculates the tax liability by multiplying its value added by the tax rate. The credit method calculates the tax for each transaction. A firm's tax liability is determined by adding up the taxes paid on all purchases and the taxes collected on all sales, and subtracting the total tax paid from the total tax collected. For a more complete discussion of these methods of calculating a value-added tax see Tax Policy: Tax-Credit and Subtraction Methods of Calculating a Value-Added Tax (GAO/GGD-89-87, June 20, 1989).

enhances compliance but also provides tax authorities with documentation for cross-checking the amount of value-added tax collected. A federal retail sales tax and a subtraction method value-added tax both lack this self-enforcing feature.

Size of Base

Because of the better enforcement properties, it may be possible to levy a federal value-added tax on more goods and services than a federal retail sales tax. In fact, European nations, on the average, levy value-added taxes on more goods and services than most state sales taxes in the United States.

Exemptions From the Base

Goods and services may be exempted from the tax base under either a federal retail sales tax or a value-added tax. Under a retail sales tax exemption the entire tax is removed, but under a value-added tax exemption only the tax at the final point of distribution or production is removed.

If the intention is to remove the tax completely under a value-added tax, "zero-rating" can be used. A zero-rating under a value-added tax applies a tax rate of zero on the sale of a good and allows a full deduction, or credit, for any tax paid on items purchased to produce the good. Zero-rating differs from exemption because zero rating keeps the firms producing zero-rated goods "in the system," that is, they are registered with the tax authority and must file a tax return.

Evasion

Most taxpayers are reluctant to attempt to evade their tax obligations—until the tax rate becomes so high that the potential financial gain from evasion exceeds the cost of the potential punishment if caught. A credit value-added tax with the self-enforcing feature increases the probability of exposing tax evaders. A federal retail sales tax has no such feature. Therefore, up to some given tax rate, a value-added tax would be expected to have better voluntary compliance than a federal retail sales tax. Thus, the federal value-added tax rate that would trigger significant levels of evasion would probably be higher than the federal retail sales tax rate that would trigger significant levels of evasion.

Methodology for GAO Consumption Tax Questionnaire

These GAO questionnaires were developed on the basis of information collected from published sources, including economics and accounting textbooks, government reports, professional journals, and accounting firm and trade association publications. We spoke with academic experts and with knowledgeable officials of the Canadian government and the states of Maryland, Michigan, Nebraska, New York, Oregon, Virginia, and Washington. We also spoke with representatives of several business associations, including the Michigan State Chamber of Commerce and Tax Executives Institute.

Four separate questionnaires were developed to send to (1) policymakers in states with a retail sales tax, (2) policymakers in states without a retail sales tax, (3) tax administrators in states with a retail sales tax, and (4) tax administrators in states without a retail sales tax. Preliminary drafts of the questionnaires were reviewed by officials of the ACIR, the National Governors' Association, the National Conference of State Legislators, the National Association of State Budget Officers, and the Federation of Tax Administrators. Based on their suggestions, changes were made where appropriate. These officials did not in any way endorse or sponsor the questionnaires but did supply GAO with the names and addresses of the appropriate state officials to receive questionnaires. State senators and representatives who received the questionnaires were chairpersons of the tax policy committees in their respective states.

A draft of the questionnaires was pretested with the appropriate state officials in New York, Oregon, and Washington. These states were selected for the following reasons:

- New York because it has both a retail sales tax and a state income tax;
- Oregon because it has an income tax but no retail sales tax; and
- Washington because it has a state retail sales tax but no state income tax.

The first mailing was done on August 17, 1988. Follow-up letters and questionnaires were mailed on September 30 and November 17, 1988. Telephone follow-up was done in December 1988 and January 1989. Our analysis includes all responses received by March 15, 1989. The answers received by respondent type are shown in table II.1.

Table II.1: Summary of Questionnaire Respondents by Type of Official

Policymaker/Administrator	Total mailed	No response	Declined to answer	Answered questions	Percent response rate
Governors	50	18	7	25	50
Budget officers	50	13	6	31	62
Senators	54	19	9	26	48
Representatives	49	10	6	33	67
Fiscal officers	58	6	14	38	66
Tax administrators	50	3	3	44	88
Total	**311**	**69**	**45**	**197**	**63**

We analyzed and quantified responses for all policymakers and administrators in states with a sales tax. Responses from tax administrators in the five states without a sales tax were such a small population and so diverse that they could not be effectively analyzed. The level of respondents in each state is shown in table II.2.

Table II.2: Level of Questionnaire Respondents by State

	Executive Branch		Legislative Branch			
State	Governors	Budget officers	Senators	Representatives	Fiscal officers	Tax administrators
Alabama	N	C	N	C	C	N
Alaska	D	D	N,N	C	N	N
Arizona	C	C	C	C	C	C
Arkansas	N	C	C	C	C	C
California	D	D	N,C	D	D	C
Colorado	N	C	N	C	D	C
Connecticut	N	C	D	C	D	C
Delaware	C	C	N	C	D	C
Florida	C	C	C,C	•	C,C	C
Georgia	N	C	•	C	C	C
Hawaii	C	C	C	C	D	C
Idaho	C	C	C	C	C	C
Illinois	N	C	C	C	C	C
Indiana	C	N	C	C	C	C
Iowa	N	N	C	C	D	C
Kansas	N	D	C	N	D	C
Kentucky	C	C	N	C	N	C
Louisiana	N	C	C	N	N	C
Maine	C	C	N	N	C	C
Maryland	C	C	C	N	D	C
Massachusetts	N	N	N,N	N	C	N
Michigan	C	C	C	C	C,C	C
Minnesota	C	C	D	C	N	N
Mississippi	N	N	C	C	C	C
Missouri	C	C	N	N	C	N
Montana	D	N	D	D	C	C
Nebraska	C	C	C	•	C	C
Nevada	D	N	N	N	C	N
New Hampshire	C	C	D	D	D	C
New Jersey	C	C	N	D	N	C
New Mexico	C	C	C	C	C	C
New York	N	N	C	N	C,N	C
North Carolina	C	C	C	N	C	C
North Dakota	D	N	C	C	C	C
Ohio	C	C	D	C	D	C
Oklahoma	C	N	D	D	D	C
Oregon	D	D	C	C	C	C

(continued)

State	Executive Branch		Legislative Branch			
	Governors	Budget officers	Senators	Representatives	Fiscal officers	Tax administrators
Pennsylvania	N	N	N	C	C,C	C
Rhode Island	C	C	C	C	C,C	C
South Carolina	C	C	N	C	C	C
South Dakota	N	C	C	C	C	C
Tennessee	N	C	C	C	C	C
Texas	N	N	D	C	D	C
Utah	N	N	C	C	C	C
Vermont	C	N	N	C	C	C
Virginia	D	D	D	C	C,D	N
Washington	C	C	N	C	C,C	C
West Virginia	N	D	N	C	C	C
Wisconsin	C	C	D,N	N,C	D	C
Wyoming	C	C	C	C	C,C	C

Note: C-Completed Questionnaire, D-Declined to Respond, and N-No Response. Two letters indicate two persons in a policymaking position in that state were sent questionnaires.

Sales tax dependence was calculated with data from the Department of Commerce report Government Finances in 1986-87 (Bureau of the Census, Series GF-87-5). High and low retail sales tax dependence was determined by calculating the revenue from retail sales tax as a percent of general revenues for each state. If a state's percentage was above (or below) the national average of 24.578 percent, it was considered to have a high (or low) dependence on its state retail sales tax. States without a sales tax were included in the low retail sales tax dependency group. State data is shown in table II.3. Where there was a significant difference in the answers given by these various groups, it was noted in our report.

Table II.3: State Characteristics

State	States having a retail sales tax	States having a individual income tax	Dependence on retail sales tax: Above average	Dependence on retail sales tax: Below average
Alabama	X	X		X
Alaska				X
Arizona	X	X	X	
Arkansas	X	X	X	
California	X	X	X	
Colorado	X	X		X
Connecticut	X	[a]	X	
Delaware		X		X
Florida	X		X	
Georgia	X	X	X	
Hawaii	X	X	X	
Idaho	X	X	X	
Illinois	X	X	X	
Indiana	X	X	X	
Iowa	X	X		X
Kansas	X	X	X	
Kentucky	X	X		X
Louisiana	X	X		X
Maine	X	X	X	
Maryland	X	X		X
Massachusetts	X	X		X
Michigan	X	X		X
Minnesota	X	X		X
Mississippi	X	X	X	
Missouri	X	X	X	
Montana		X		X
Nebraska	X	X		X
Nevada	X		X	
New Hampshire		[b]		X
New Jersey	X	X		X
New Mexico	X	X	X	
New York	X	X		X
North Carolina	X	X		X
North Dakota	X	X		X
Ohio	X	X	X	
Oklahoma	X	X		X
Oregon		X		X

(continued)

State	States having a retail sales tax	States having a individual income tax	Dependence on retail sales tax: Above average	Dependence on retail sales tax: Below average
Pennsylvania	X	X	X	
Rhode Island	X	X		X
South Carolina	X	X	X	
South Dakota	X		X	
Tennessee	X	[b]	X	
Texas	X		X	
Utah	X	X	X	
Vermont	X	X		X
Virginia	X	X		X
Washington	X		X	
West Virginia	X	X	X	
Wisconsin	X	X		X
Wyoming	X			X

[a]Connecticut taxes only interest, dividends and capital gains and was counted as a state not having an individual income tax.

[b]New Hampshire and Tennessee tax only interest and dividends and were counted as states not having an individual income tax.

Level of Concern by Respondent Characteristics

Our questionnaire analysis included, where appropriate, comparison of responses based on specific respondent characteristics. These included analyses based on

- type of respondent—legislators (state senators, state representatives, state fiscal officers) versus executives (governors and state budget officers);
- degree to which a state taxes personal income as determined by the dependence of that state on individual income taxes for revenue—40 states with a broad-based individual income tax versus 10 states with a low or no individual income tax;
- degree to which a state is dependent on a retail sales tax—states above the national average were determined to have high dependency versus states below the national average (low dependency)—25 states with above average dependence versus 25 states below average.

Limited comparisons of policymakers' responses were made between states with and without a retail sales tax because of the low level of response from policymakers in states without a retail sales tax.

Policymakers indicated their level of concern regarding either a federal value-added tax or a retail sales tax based on their preference for some type of federal consumption tax. Those not favoring a federal retail sales tax indicated their concerns about a federal retail sales tax. Those not favoring a federal value-added tax indicated their concerns about a value-added tax.

Questionnaire responses indicated that the level of concern for many issues varied depending on whether the respondent was a legislative or executive branch policymaker and whether the policymaker opposed raising taxes. Concerns about issues also varied depending on the proportion of state revenue derived from retail sales tax in the respondent's state.

Executive branch policymakers were more concerned than legislative branch policymakers about the regressivity of a consumption tax. Policymakers opposed to raising taxes were more concerned about the impact of a consumption tax on inflation or that the tax might not be used to reduce the deficit. Policymakers from states with a relatively lower retail sales tax were more concerned about the regressivity of a federal consumption tax.

A higher proportion of executive branch policymakers than legislative policymakers indicated concern about the regressivity of a federal sales or value-added tax. These executive branch policymakers indicated greater concern about the regressivity of both a federal sales and a value-added tax. For a value-added tax, they were especially concerned about the invisibility of the tax, its potential impact on inflation, and the administrative costs associated with enforcing the new tax.

As shown in tables III.1, III.2, and III.3, a higher proportion of those opposed to raising federal taxes indicated great concern about potential drawbacks of a consumption tax than those not opposed to raising federal taxes. Most noticeably, a higher proportion of those opposed to raising federal taxes was greatly concerned that

- federal retail sales tax or value-added tax revenue might not be used to reduce the deficit;
- a federal retail sales tax or value-added tax would increase inflation; and
- a federal value-added tax would create pressure on the state to match its tax base with the federal tax base.

A higher proportion of those who did not oppose raising federal taxes was greatly concerned about the regressivity of a federal retail sales tax.

Levels of concern also varied depending on whether the respondent's state's retail sales tax revenue as a percentage of total state revenue was below or above the average level for all states. A larger proportion of policymakers responding from states below the average was greatly concerned about regressivity and inflation. A slightly higher proportion of policymakers from states with sales tax revenue exceeding the average was greatly concerned about the impact of a federal consumption tax on their state's ability to increase its sales tax.

Table III.1: Percentage of Responding Executives and Legislators Who Were Greatly or Very Greatly Concerned With Federal Consumption Tax Issues

	Federal retail sales tax		Federal value-added tax	
	Exec.	**Leg.**	**Exec.**	**Leg.**
Revenue may not be used to reduce the deficit	43%	45%	68%	68%
Regressive nature of the tax	71	53	72	47
Impact of the tax on inflation	21	15	60	40
Administrative cost to enforce the tax	14	20	52	34
Intrusion of the federal government into state revenue source	82	78	64	76
Impact of the tax on state's ability to increase a state consumption tax	71	72	64	68
Confusion between state and federal tax	54	50	36	37
Confusion between state and federal tax base	54	53	32	45
Pressure to match state tax base with federal tax base	39	42	32	34
Visibility of the tax to the consumer	21	18	16	16
Invisibility of the tax to the consumer	4	10	60	24

Table III.2: Percentage of Responding Policymakers Who Were Opposed or Not Opposed to Raising Taxes and Who Were Greatly or Very Greatly Concerned With Federal Consumption Tax Issues

	Federal retail sales tax		Federal value-added tax	
	Opposed to raising taxes	Not opposed	Opposed to raising taxes	Not opposed
Revenue may not be used to reduce the deficit	71%	38%	79%	62%
Regressive nature of the tax	29	66	63	54
Impact of the tax on inflation	29	14	67	36
Administrative cost to enforce the tax	29	16	50	36
Intrusion of the federal government into state revenue source	82	79	75	69
Impact of the tax on state's ability to increase a state consumption tax	65	73	75	62
Confusion between state and federal tax	53	51	38	36
Confusion between state and federal tax base	53	54	42	39
Pressure to match state tax base with federal tax base	41	41	46	26
Visibility of the tax to the consumer	12	21	17	15
Invisibility of the tax to the consumer	13	7	46	34

Table III.3: Percentage of Responding Policymakers From States With a Level of Retail Sales Tax Dependence Below and Above the Average Who Were Greatly or Very Greatly Concerned With Federal Consumption Tax Issues

	Federal retail sales tax		Federal value-added tax	
	Below	Above	Below	Above
Revenue may not be used to reduce the deficit	42%	46%	72%	65%
Regressive nature of the tax	73	51	72	42
Impact of the tax on inflation	21	15	63	32
Administrative cost to enforce the tax	24	15	41	42
Intrusion of the federal government into state revenue source	79	80	66	77
Impact of the tax on state's ability to increase a state consumption tax	67	75	59	74
Confusion between state and federal tax	55	49	31	42
Confusion between state and federal tax base	49	56	38	42
Pressure to match state tax base with federal tax base	33	46	31	36
Visibility of the tax to the consumer	21	18	25	7
Invisibility of the tax to the consumer	9	7	44	33

Questionnaire and Responses From State Tax Policymakers

This appendix includes the questionnaire and responses of state tax policymakers. Responses to questions 3 through 9 and 11 through 18 reflect the number of policymakers from states with and without a state retail sales tax. Responses to questions 10, 19, and 20 could not be combined for policymakers in states with and without a sales tax because the questions are not identical. Responses from policymakers in states with a retail sales tax are shown in sequence. Responses from policymakers in states without a sales tax are on the last page of this appendix.

United States General Accounting Office

Survey of State Tax Policymakers Concerning a Possible Federal Consumption Tax

INTRODUCTION

The U.S. General Accounting Office (GAO), an agency of the Congress responsible for evaluating federal policies and programs, is conducting a survey of state tax policymakers and administrators. The questionnaire asks you as a state tax policymaker to provide your perspective on the possibility/feasibility of federal consumption taxes as a means to increase federal revenues. To clarify what is meant by the terms in the questionnaire, a glossary is included.

This questionnaire is being sent to state tax policymakers in each state. The questionnaire should be completed by the addressee or someone he/she designates. A similar questionnaire is being sent to state tax administrators. Your participation is voluntary. However, our report to the Congress will be less than complete without your input. We encourage you to reply.

This is not an anonymous survey. Your individual responses may be provided to the Congress. After receiving the replies, GAO will judgmentally select a number of states and follow-up in person to obtain more detailed information on the questionnaire responses. Therefore, it is important that we receive the name of a contact person in question 1.

The questionnaire should take 20 to 30 minutes to complete. Most of the questions can be quickly answered by checking boxes. Please return the questionnaire in the enclosed postage-paid envelope within 10 days of receipt. If you have any questions, please call, collect, Mr. George Zika on (415) 556-6200 or Ms. Lynda Willis on (202) 272-7904. In the event the envelope is misplaced, the address is:

U.S. General Accounting Office
Mr. George Zika
San Francisco Regional Office
Suite 900
1275 Market Street
San Francisco, CA 94103

Thank you for your help.

* * * *

Glossary

Value-added tax (VAT): A multistage tax that is imposed on the value added to goods and services at every stage in the production and distribution process. Value-added is the difference between a business firm's sales and its purchases from other firms.

Retail sales tax (RST): A tax that is calculated and added to the price of goods or services sold to consumers.

Consumption tax: Retail sales tax or value-added tax.

Invisible tax: A retail sales tax or value-added tax that is included in the price of goods or services sold to consumers instead of being calculated and added to the before-tax price at the time of sale.

Visible tax: A retail sales tax or value-added tax that is calculated and added to the price of goods or services sold to consumers instead of being included in the price before the sale.

Piggyback tax: A state retail sales tax or value-added tax that is added on to a federal retail sales tax or value-added tax and that applies to the same transactions as the federal tax. Administration and collection of both taxes are performed by a federal agency, which periodically remits to the state the amounts collected for it.

Broad-based tax: A tax base that includes almost all goods and services. Exclusions would include rental value of owner and tenant occupied housing, medical care, insurance and finance, education, religious, and welfare activities.

I. BACKGROUND

1. Please indicate the name, title, and telephone number of the person we should contact if additional information is required about your responses.

NAME: ______________________

TITLE: ______________________

TELEPHONE NUMBER: (____) ______________
area code

2. For which state are you a tax policymaker?

____

II. POTENTIAL SOURCES OF ADDITIONAL FEDERAL REVENUE

3. In your opinion, which of the following sources, if any, would you prefer the federal government use to reduce the deficit? *(Check all that apply.)*

1. ☐ Corporate income taxes (69)
2. ☐ Individual income taxes (57)
3. ☐ Broad-based consumption taxes (RST or VAT) (41)
4. ☐ Federal excise taxes (alcohol, tobacco, motor fuels, etc) (49)
5. ☐ Other *(Please specify)* (28)

____

____

6. ☐ The federal government should NOT raise taxes to reduce the deficit. (46)

If you checked **only** 4, 5, or 6 in question 3, please skip to question 6.

If you checked either 1 or 2 (corporate or individual income taxes) in question 3, please answer question 4. If you did **not** check 1 or 2 in question 3, please skip to question 5.

4. For corporate or individual taxes, would you favor broadening the tax base, increasing the tax rate, or both? *(Check one box in each row. If you checked only one source in question 3, check "N/A" for the other.)*

	Broaden tax base	Increase tax rate	Both	N/A
	(1)	(2)	(3)	(4)
1. Corporate tax	19	4	44	
2. Individual tax	15	12	28	

If you checked 3 (consumption taxes) in question 3, please answer question 5.

5. Would you favor a federal retail sales tax, a value-added tax, or both? *(Check one.)*

1. ☐ Retail sales tax (10)
2. ☐ Value-added tax (24)
3. ☐ Both (4)
4. ☐ Other *(Please specify)* (2)

____

III. STATE CONCERNS ABOUT A BROAD BASED FEDERAL CONSUMPTION TAX.

6. Would you favor or oppose a broad-based federal consumption tax to decrease the national deficit? *(Check one box in each row.)*

	Strongly favor	Favor	Neither favor nor oppose	Oppose	Strongly oppose	No basis to judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. Retail sales tax	8	6	12	51	73	3
2. Value-added tax	10	18	17	46	58	4

If you checked 4 (oppose) or 5 (strongly oppose) for either retail sales or value-added taxes in question 6, please answer questions 7-9. If you did not check those answers, skip to question 10.

7. Would your opposition to a broad-based federal consumption tax (either retail sales or value-added) be reduced if the states were offered a share in the revenue **without** conditions (no strings attached)? *(Check one box in each row.)*

	Definitely yes	Probably yes	Uncertain	Probably no	Definitely no	No basis to judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. Retail sales tax	1	23	7	40	51	2
2. Value-added tax	1	11	6	43	40	2

8. Would your opposition to a broad-based federal consumption tax (either retail sales or value-added) be reduced if the federal government agreed to pay a larger share of your state's federally-mandated social program costs? *(Check one box in each row.)*

	Definitely yes	Probably yes	Uncertain	Probably no	Definitely no	No basis to judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. Retail sales tax	3	17	17	39	47	1
2. Value-added tax	0	13	16	36	37	1

9. **Would your opposition to a broad-based federal consumption tax be reduced if the tax was invisible to the consumer?** *(Check one box in each row.)*

	Definitely yes	Probably yes	Uncertain	Probably no	Definitely no	No basis to judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. **Retail sales tax**	1	6	2	43	71	1
2. **Value-added tax**	0	0	4	34	64	1

10. **In your opinion, would the existence of a broad-based federal consumption tax encourage or discourage your state from increasing its sales tax rate or broadening its sales tax base?** *(Check one box in each row.)*

	Greatly encourage	Encourage	Neither encourage nor discourage	Discourage	Greatly discourage	No basis to judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. **Increase sales tax rate**	0	1	20	59	56	7
2. **Broaden sales tax base**	1	11	27	58	34	12

11. **Assuming there was going to be a broad-based federal consumption tax, would you prefer a federal consumption tax that was a retail sales tax or a value-added tax?** *(Check one.)*

1. ☐ **Prefer retail sales tax** *(Skip to question 13.)* (53)
2. ☐ **Prefer value-added tax** *(Continue to question 12.)* (78)
3. ☐ **Other (please specify)** *(Please answer question 12 and question 13.)* (10)

____

4. ☐ **No basis to judge** *(Skip to question 14.)* (12)

12. To what extent, if any, do you believe the following issues are reasons why the federal government should not implement a broad-based **retail sales tax**? *(Check one box in each row.)*

	Very great extent (1)	Great extent (2)	Moderate extent (3)	Some extent (4)	Little or no extent (5)	No basis to judge (6)
A. The revenue may be used to finance additional federal spending rather than for deficit reduction	24	15	10	16	19	4
B. Regressive nature of a retail sales tax — a federal retail sales tax may take proportionally more from a low-income household than from a high-income household	15	37	18	9	8	1
C. Impact a federal retail sales tax may have on inflation	2	13	22	20	27	4
D. Administrative cost to enforce a federal retail sales tax	8	8	16	14	40	2
E. Federal government's intrusion into what has been exclusively a state source of revenue	46	24	6	5	7	0
F. Impact a federal retail sales tax may have on state's ability to increase state retail sales tax	38	25	7	7	9	2
G. Confusion between state and federal retail sales taxes	19	26	15	5	22	1
H. Confusion between state and federal tax bases	20	27	10	13	17	1
I. Pressure to match state tax base with federal tax base	16	20	20	11	20	1
J. Visibility of a federal retail sales tax to the consumer	5	12	12	16	37	6
K. Invisibility of a federal retail sales tax to the consumer	2	5	11	17	42	9
L. Other *(Please specify)* (3)						

SKIP TO QUESTION 14

13. To what extent, if any, do you believe the following issues are reasons why the federal government should not implement a broad-based value-added tax? *(Check one box in each row.)*

	Very great extent (1)	Great extent (2)	Moderate extent (3)	Some extent (4)	Little or no extent (5)	No basis to judge (6)
A. The revenue may be used to finance additional federal spending rather than for deficit reduction	24	19	7	5	6	2
B. Regressive nature of a value-added tax — a federal value-added tax may take proportionally more from a low-income household than from a high-income household	21	15	9	9	6	3
C. Impact a federal value-added tax may have on inflation	12	18	8	6	15	4
D. Administrative cost to enforce a federal value-added tax	14	12	10	9	12	6
E. Federal government's intrusion into what has been exclusively a state source of revenue	30	15	5	4	9	0
F. Impact a federal value-added tax may have on state's ability to increase state consumption taxes	24	18	6	8	3	4
G. Confusion between state and federal consumption taxes	10	13	13	11	12	4
H. Confusion between state and federal tax bases	14	11	12	9	13	4
I. Pressure to match state tax base with federal tax base	13	8	11	10	19	2
J. Visibility of a federal value-added tax to the consumer	4	6	6	10	33	4
K. Invisibility of a federal value-added tax to the consumer	16	8	6	9	17	6
L. Other *(Please specify)* (7)						

IV. DESIGN OF A FEDERAL CONSUMPTION TAX

14. In your opinion, which of the following items, if any, should be **exempt** from a broad-based federal retail sales tax (RST) or value-added tax (VAT)? *(Check one box for "RST" and one box for "VAT" in each row.)*

ITEMS	RST should exempt?			VAT should exempt?		
	Yes (1)	No (2)	No basis to judge (3)	Yes (1)	No (2)	No basis to judge (3)
1. Food consumed on premises	29	108	15	36	94	22
2. Food for take out	36	101	15	43	87	22
3. Food unprepared	103	38	12	92	42	19
4. New automobiles	13	117	21	14	110	28
5. Used automobiles	25	105	22	31	91	30
6. New trucks	15	115	22	13	110	29
7. Used trucks	25	104	23	28	94	30
8. Truck motor fuel	56	78	18	48	78	26
9. Other motor fuel	59	76	17	53	74	25
10. General merchandise	13	119	19	13	111	27
11. New houses	91	42	19	69	56	27
12. Used houses	93	38	21	75	48	29
13. Building materials	43	91	18	34	92	26
14. Furniture	13	120	19	14	111	27
15. Public utilities						
a. Household fuel	89	51	13	78	55	20
b. Electricity	85	55	13	74	58	21
c. Telephone	60	77	16	55	74	23
16. Manufacturing (not part of the final product)	53	76	24	39	85	29
17. Manufacturing (part of the final product)	64	62	26	37	85	30

QUESTION 14 CONTINUED ON THE NEXT PAGE

QUESTION 14 CONTINUED

ITEMS	RST should exempt? Yes (1)	RST should exempt? No (2)	RST should exempt? No basis to judge (3)	VAT should exempt? Yes (1)	VAT should exempt? No (2)	VAT should exempt? No basis to judge (3)
18. Over the counter drugs	54	86	12	53	80	19
19. Prescription drugs and medicines	116	26	11	95	40	18
20. Services						
a. Medical and Dental	103	36	13	86	45	21
b. Other professional services	45	84	23	39	80	33
c. Repair services	35	101	16	36	92	24
d. Personal services	36	94	22	35	86	31
e. All other services	33	95	23	32	87	31
21. Other *(Please specify)* (10)				10		

15. To what extent, if any, would you favor or oppose a broad-based federal retail sales or value-added tax that was invisible to the consumer? *(Check one box in each row.)*

	Strongly favor (1)	Favor (2)	Neither favor nor oppose (3)	Oppose (4)	Strongly oppose (5)	No basis to judge (6)
1. Retail sales tax	4	8	15	37	83	6
2. Value-added tax	7	10	20	33	76	7

16. To what extent, if any, would you favor or oppose a broad-based federal retail sales or value-added tax that was visible to the consumer? *(Check one box in each row.)*

	Strongly favor	Favor	Neither favor nor oppose	Oppose	Strongly oppose	No basis to judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. Retail sales tax	4	12	16	55	59	7
2. Value-added tax	3	17	17	49	55	12

V. ADMINISTRATION OF A FEDERAL TAX

17. In your opinion, which of the following features, if any, would facilitate the administration of a broad-based federal consumption tax? *(Check all that apply.)*

1. ☐ Low rate (61)
2. ☐ Single rate (118)
3. ☐ Multiple rates (10)
4. ☐ Few or no exemptions (111)
5. ☐ Invisible at the retail level (31)
6. ☐ Visible at the retail level (46)
7. ☐ Small business exemption (12)
8. ☐ Other *(Please specify)* (25)

VI. SHARING CONSUMPTION TAX REVENUES WITH STATES

18. Suppose the federal government enacted a broad-based retail sales or value-added tax. In your opinion, would your state be interested in piggybacking upon the federal tax if the opportunity to do so were available? *(Check one box in each row.)*

	Definitely yes	Probably yes	Uncertain	Probably no	Definitely no	No basis to judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. Retail sales tax	4	25	38	38	32	16
2. Value-added tax	5	26	39	42	24	17

19. In your opinion, would your state agree to piggyback on a broad-based federal **retail sales** tax if the federal government required your state to repeal its retail sales tax as a condition of participation? *(Check one.)*

1. ☐ Definitely yes (12)
2. ☐ Probably yes (20)
3. ☐ Uncertain (28)
4. ☐ Probably no (47)
5. ☐ Definitely no (25)
6. ☐ No basis to judge (12)

20. In your opinion, would your state agree to piggyback on a broad-based federal **value-added** tax if the federal government required your state to repeal its retail sales tax as a condition of participation? *(Check one.)*

1. ☐ Definitely yes (15)
2. ☐ Probably yes (14)
3. ☐ Uncertain (26)
4. ☐ Probably no (44)
5. ☐ Definitely no (28)
6. ☐ No basis to judge (17)

VII. COMMENTS

21. Please use the space below to provide any comments you may have about this questionnaire, a federal retail sales tax, or a federal value-added tax. Attach additional sheets, if necessary.

Thank you for your help.

10. In your opinion, to what extent, if any, would the existence of a federal consumption tax make your state reluctant to adopt a retail sales or value-added tax? *(Check one box in each row.)*

	Very great extent	Great extent	Moderate extent	Some extent	Little or no extent	No basis to judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. Reluctant to adopt a retail sales tax	2	1	0	1	5	0
2. Reluctant to adopt a value-added tax	1	2	0	1	5	0

19. In your opinion, would your state agree to piggyback on a broad-based federal **value-added** tax if the federal government required your state not enact a state retail sales tax as a condition of participation? *(Check one.)*

1. ☐ Definitely yes (1)
2. ☐ Probably yes (1)
3. ☐ Uncertain (1)
4. ☐ Probably no (4)
5. ☐ Definitely no (2)
6. ☐ No basis to judge (0)

20. In your opinion, would your state agree to piggyback on a broad-based federal **retail sales** tax if the federal government required your state not enact a state retail sales tax as a condition of participation? *(Check one.)*

1. ☐ Definitely yes (1)
2. ☐ Probably yes (2)
3. ☐ Uncertain (1)
4. ☐ Probably no (3)
5. ☐ Definitely no (2)
6. ☐ No basis to judge (0)

Questionnaire and Responses From State Tax Administrators

This appendix includes the questionnaire and responses of state tax administrators from states with a retail sales tax. Because only five states do not have a retail sales tax, a limited number of responses was received, and these showed no patterns sufficient for data analysis.

United States General Accounting Office

Survey of State Tax Administrators Concerning a Possible Federal Consumption Tax

INTRODUCTION

The U.S. General Accounting Office (GAO), an agency of the Congress responsible for evaluating federal policies and programs, is conducting a survey of state tax policymakers and administrators. The questionnaire asks you as a state tax administrator to provide your perspective on the possibility/feasibility of federal consumption taxes as a means to increase federal revenues. To clarify what is meant by the terms in the questionnaire, a glossary is included.

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This is not an anonymous survey. Your individual responses may be provided to the Congress. After receiving the replies, GAO will judgmentally select a number of states and follow-up in person to obtain more detailed information on the questionnaire responses. Therefore, it is important that we receive the name of a contact person in question 1.

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U.S. General Accounting Office
Mr. George Zika
San Francisco Regional Office
Suite 900
1275 Market Street
San Francisco, CA 94103

Thank you for your help.

GLOSSARY

Value-added tax (VAT): A multistage tax that is imposed on the value added to goods and services at every stage in the production and distribution process. Value-added is the difference between a business firm's sales and its purchases from other firms.

Retail sales tax (RST): A tax that is calculated and added to the price of goods or services sold to consumers.

Consumption tax: Retail sales tax or value-added tax.

Invisible tax: A retail sales tax or value-added tax that is included in the price of goods or services sold to consumers instead of being calculated and added to the before-tax price at the time of sale.

Visible tax: A retail sales tax or value-added tax that is calculated and added to the price of goods or services sold to consumers instead of being included in the price before the sale.

Broad-based tax: A tax base that includes almost all goods and services. Exclusions would include rental value of owner and tenant occupied housing, medical care, insurance and finance, education, religious, and welfare activities.

I. BACKGROUND

1. Please indicate the name, title, and telephone number of the person we should contact if additional information is required about your responses.

   Name: ____________________

   Title: ____________________

   Telephone Number: (   ) ____________________
   area code

2. For which state are you a tax administrator?

   ____

II. ADMINISTRATION OF STATE TAXES

3. In your opinion, to what extent, if at all, do you believe your state's retailers have difficulty determining which items are subject to the state sales tax? (Check one.)
   1. ☐ Very great extent (0)
   2. ☐ Great extent (3)
   3. ☐ Moderate extent (13)
   4. ☐ Some extent (15)
   5. ☐ Little or no extent (7)

   - - - - - - - - - - - - - -

   6. ☐ No basis to judge (1)

4. Does your state provide some type of credit or rebate to low-income taxpayers to lessen the burden of the sales tax? (Check one.)
   1. ☐ Yes (8)
   2. ☐ No (30)

III. EFFECT OF FEDERAL TAX ON STATE SALES TAX ADMINISTRATION

5. In your opinion, if the federal government enacted a broad-based retail sales tax or value-added tax, would the resources that the federal government applied to tax administration have spill-over benefits for the administration of your state sales tax program? (Check one box in each row.)

	Definitely No	Probably No	Uncertain	Probably Yes	Definitely Yes	No Basis to Judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. Retail sales tax	1	9	4	20	3	2
2. Value-added tax	1	11	11	9	2	5

6. If the federal government enacted and administered its own broad-based consumption tax (retail sales or value-added), do you believe that your state would be interested in signing an information-sharing agreement with the federal government to enhance the administration of your state's sales tax program? (Check one box in each row.)

	Definitely Yes	Probably Yes	Uncertain	Probably No	Definitely No	No Basis to Judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. Retail sales tax	21	15	1	1	0	1
2. Value-added tax	18	16	2	1	0	2

7. To what extent, if at all, would a broad-based federal retail sales tax or value-added tax complicate the administration of your state sales tax? (**Check one box in each row.**)

	Very Great Extent	Great Extent	Moderate Extent	Some Extent	Little or No Extent	No Basis to Judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. Retail sales tax	3	8	9	9	6	4
2. Value-added tax	3	3	7	10	9	7

8. In your opinion, would the administrative costs of your state sales tax program increase, decrease, or stay about the same if the federal government imposed either a broad-based federal sales tax or a value-added tax that was **visible** to the consumer? (**Check one box in each row.**)

	Greatly Increase	Somewhat Increase	Stay About the Same	Somewhat Decrease	Greatly Decrease	No Basis to Judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. Retail sales tax	4	17	17	0	0	1
2. Value-added tax	4	15	17	0	0	3

9. In your opinion, would the administrative costs of your state sales tax program increase, decrease, or stay about the same if the federal government imposed either a broad-based federal sales tax or a value-added tax that was **invisible** to the consumer? (**Check one box in each row.**)

	Greatly Increase	Somewhat Increase	Stay About the Same	Somewhat Decrease	Greatly Decrease	No Basis to Judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. Retail sales tax	2	14	23	0	0	0
2. Value-added tax	2	12	25	0	0	0

10. In your opinion, would the revenue from your state's sales tax increase, decrease, or stay about the same if the federal government imposed either a broad-based federal sales tax or a value-added tax that was **visible** to the consumer? **(Check one box in each row.)**

	Greatly Increase	Somewhat Increase	Stay About the Same	Somewhat Decrease	Greatly Decrease	No Basis to Judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. **Retail sales tax**	1	4	11	18	1	4
2. **Value-added tax**	1	5	13	16	0	4

11. In your opinion, would the revenue from your state's sales tax increase, decrease, or stay about the same if the federal government imposed either a broad-based federal sales tax or a value-added tax that was **invisible** to the consumer? **(Check one box in each row.)**

	Greatly Increase	Somewhat Increase	Stay About the Same	Somewhat Decrease	Greatly Decrease	No Basis to Judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. **Retail sales tax**	2	9	15	10	0	3
2. **Value-added tax**	2	10	17	7	0	3

12. **In your opinion, would a federal broad-based retail sales tax or a value-added tax increase, decrease, or have no effect on evasion of your state sales tax by taxpayers? (Check one box in each row.)**

	Greatly Increase	Somewhat Increase	No Effect	Somewhat Decrease	Greatly Decrease	No Basis to Judge
	(1)	(2)	(3)	(4)	(5)	(6)
1. **Retail sales tax**	4	13	6	9	1	6
2. **Value-added tax**	1	10	15	4	1	8

IV. ADMINISTRATION OF A FEDERAL TAX

13. In your opinion, which of the following features, if any, would facilitate the administration of a broad-based federal consumption tax? **(Check all that apply.)**

    1. ☐ Low rate (22)
    2. ☐ Single rate (38)
    3. ☐ Multiple rates (0)
    4. ☐ Few or no exemptions (39)
    5. ☐ Invisible at the retail level (18)
    6. ☐ Visible at the retail level (4)
    7. ☐ Small business exemption (3)
    8. ☐ Other (please specify) (2)

14. If the federal government enacted a broad-based retail sales tax, in your opinion, which of the following methods, if any, would be the most **efficient** in collecting this tax? **(Check one.)**

    1. ☐ Federal government should collect both federal and state taxes. (0)
    2. ☐ States should collect the tax for both federal and state governments. (10)
    3. ☐ Federal government should collect it's own taxes and states should collect their own taxes. (27)
    4. ☐ Other (please specify) (2)

15. If the federal government enacted a broad-based, value-added tax, in your opinion, which of the following methods, if any, would be the most **efficient** in collecting this tax? **(Check one.)**

    1. ☐ Federal government should collect both federal and state taxes. (2)
    2. ☐ States should collect the tax for both federal and state governments. (1)
    3. ☐ Federal government should collect it's own taxes and states should collect their own taxes. (35)
    4. ☐ Other (please specify) (1)

V. COMMENTS

16. If you have additional comments about this questionnaire, a federal retail sales tax or a federal value-added tax, please provide them in the space below. Attach additional sheets, if necessary.

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