F I S C A L   I M P A C T   R E P O R T

SPONSOR Ortiz y Pino **ORIGINAL DATE** 02/26/11 **LAST UPDATED** **HB**

SHORT TITLE Sweetened Beverage Excise Tax **SB** 288

ANALYST Golebiewski

REVENUE (dollars in thousands)

Estimated Revenue			Recurring or Non-Rec	Fund Affected
FY11	**FY12**	**FY13**		
	$1,200.0	$2,500.0	Recurring	Child Obesity Prevention Fund
	$23,600.0	$47,700.0	Recurring	County-Supported Medicaid Fund
	$24,800.0	$50,200.0	Recurring	Total Excise Tax Revenue
	($430.0)	($860.0)	Recurring	Local Governments
	($95.0)	($190.0)	Recurring	General Fund

(Parenthesis ( ) Indicate Revenue Decreases)

ESTIMATED ADDITIONAL OPERATING BUDGET IMPACT (dollars in thousands)

	FY11	FY12	FY13	3 Year Total Cost	Recurring or Non-Rec	Fund Affected
Total		$145.0	$135.0	$280.0	Recurring	Taxation and Revenue Department

(Parenthesis ( ) Indicate Expenditure Decreases)

SOURCES OF INFORMATION
LFC Files

Responses Received From
Taxation and Revenue Department (TRD)
Department of Health (DOH)

SUMMARY

Synopsis of Bill

Senate Bill 288 would create a new excise tax on distributors of sweetened beverages at a rate of ½ cent per ounce. The County-Supported Medicaid Fund would receive 95 percent of the receipts and a new fund, the Child Obesity Prevention Fund, will receive 5 percent of the receipts.

FISCAL IMPLICATIONS

TRD:

> This estimate is based on work by Yale University's Rudd Center for Food Policy and Obesity with adjustments to account for the slight difference in this bill's definition of sweetened beverages.
>
> Although there are significant differences in sweetened beverage consumption patterns depending on age, income, and race, the overall consumption patterns in New Mexico are not expected to differ significantly from nationwide patterns. The age distribution in New Mexico does not indicate any difference from the national consumption patterns. Income levels in New Mexico indicate slightly above average sweetened beverage consumption in New Mexico; however, the race differences between New Mexico and the US average indicate a slightly lower consumption.
>
> Because the elasticity of demand is assumed to be -1.2 the overall expenditures on sweetened beverages will be reduced by this tax. The reduced expenditures will impact both gross receipts tax revenue of counties, municipalities, and the General Fund, and also hold harmless distributions from the General Fund to local governments because of lower gross receipts tax food deductions. The negative figures shown in the estimated revenue impact represent the initial revenue loss due to reduced consumer expenditures on sweetened beverages. To the extent that this expenditure reduction is merely shifted to other expenditures taxable under the gross receipts tax the effect shown will be reduced; however, to the extent that this reduction shifts expenditures towards, saving, housing (including rent), fuels, certain health care expenditures, and some other categories the ultimate revenue outcome will be more complex. This estimate does not attempt to apportion the expenditure shift into new categories or show possible revenue effects such as increased fuel tax revenue.

<u>Continuing Appropriations language</u>

This bill creates a new fund and provides for continuing appropriations. The LFC has concerns with including continuing appropriation language in the statutory provisions for newly created funds, as earmarking reduces the ability of the legislature to establish spending priorities.

SIGNIFICANT ISSUES

SB 288 would impose a new excise tax on sweetened beverages. The distribution to County-Supported Medicaid and the Child Obesity Prevention Fund serves to link the beneficiaries of the additional tax to those who pay the tax on sweetened beverages, which is consistent with the benefit principle of taxation. However, it also sets up a tax earmark which removes legislative control of funds.

With respect to the taxation of sweetened beverages by the ounce, it can be considered a regressive tax. Beverages such as sweetened iced tea priced around $1 are approximately 20 ounces, which translates to a tax of 10 cents, or a tax rate of 10 percent. A 2-liter bottle of Pepsi priced around $1 is 64 ounces, which translates to a tax of 32 cents, or a tax rate of 32 percent. The different consumption patterns of individuals at different income levels may also magnify the regressivity.

SB 288 also introduces economic distortions into the New Mexico tax system. Taxpayers are incentivized to change their consumption patterns to avoid the additional excise tax on bottled sweetened beverages. There are a number of options open to taxpayers. For example, if a taxpayer was considering the purchase of Kool-aid in a bottle, they could instead purchase the Kool-aid powder mix and make the beverage at home to avoid the excise tax.

In addition, they could change their beverage consumption on the margin. Consider for example, the purchase of a large beverage (assume 32 ounces) at a fast food restaurant, which on average, is 50 cents more than a small beverage (assume 16 ounces); this would increase the difference in price between the two choices by 8 cents, or by 16 percent of the difference. This may cause consumers to choose the small beverage with greater frequency than they would in the absence of the excise tax.

The policy proposed in SB 288 increases the complexity of the tax system and in response, the taxpayers will have to pay a substantial amount of compliance costs. In addition, TRD will incur additional administrative costs.

DOH:

SB288 would result in an increase in the price of soft drinks relative to other beverages. Pricing strategies have proven effective in decreasing the consumption of tobacco products in the United States (http://www.cdc.gov/tobacco/sgr/sgr_2000/sgr_tobacco_aag.htm). However, in a recent USDA pricing study, results showed it took a 20 percent price increase to decrease soft drink consumption (http://www.ers.usda.gov/Publications/err100/).

Studies among adults and children have found an association between high consumption of sugar-sweetened beverages and overweight status (*Lancet, 2001; NHANES III, 2000; Journal of the American Dietetic Association, 1997*). The Centers for Disease Control and Prevention (CDC) has identified the decrease of soft drinks and sweetened beverages in diets as a promising strategy for weight management (*CDC Division of Nutrition and Physical Activity Progress Monitoring Report, January 2006*). Key nutrition recommendations from the *2005 Dietary Guidelines for Americans* state that Americans should avoid excessive amounts of calories from added sugars.

Obesity is a growing problem in the nation and in New Mexico. In 2009, 28.0% of youth (New Mexico Youth Risk and Resiliency Survey data, 2010: http://www.youthrisk.org/) and 61.8% of adults (New Mexico Behavioral Risk Factor Surveillance System data, 2010: http://ibis.health.state.nm.us/query/builder/brfss/BRFSSAgeAdj/BMIAgeAdj.html) living in New Mexico were either overweight or obese. Further, the prevalence of obesity continues to grow and occur at younger ages. In 2010, 30.3% of kindergarteners and 38.3% of third graders living in New Mexico were either overweight or obese (New Mexico Department of Health BMI Surveillance Report, 2010: http://www.health.state.nm.us/plans/BMISurveillance.pdf). The percentage of obese children participating in the Women, Infants and Children (WIC) Program increased from 10.6% in 2000 to 13.4% in 2008 (New Mexico Department of Health, WIC data, 2009).

ADMINISTRATIVE IMPLICATIONS

TRD:

This bill creates a new fairly complex tax program and will have a moderate impact on the Department.

Estimated Additional Operating Budget Impact*				R or NR**	Fund(s) or Agency Affected
FY2011	FY2012	FY2013	FY 11-13		
0	145	135	0	R	Taxation and Revenue Department

The bill imposes a rate of tax on each ounce of sweetened beverage, including those produced from powders and syrups. Pursuant to Section 4, the volume of beverage produced from these products is based on the volumes produced by or typically produced by retailers. It might be necessary for the Department to promulgate regulations to facilitate communication between retailers and distributors of the volumes produced.

This bill will create a new tax program that will require an additional option on the current registration form or development of a new registration form. Filing instructions and forms will need to be developed with taxpayer education required. The Revenue Processing Division anticipates an additional 3 FTE (at $45,000 per FTE) will be required to process/administer returns and for bond administration. Mandated electronic filing of returns does minimize the number of FTE that would otherwise be required. Due to the complexity of the record keeping required, this tax would be very difficult for taxpayers to track and for the Department to audit.

Implementing the new tax will also have a moderate IT impact in the first year. Approximately 750 hours will be devoted to implementation at a cost of $67,500 broken down as follows:

1) Changes to the pipeline for Wausau capture for the new tax program – 190 hours (Note: No change necessary to E-DCR because the bill states that all returns must be filed electronically.)
2) Changes to configuration for the new tax program – 190 hours
3) Changes to revenue accounting – 100 hours
4) Changes to TAP and NMWebFile – 190 hours

Testing – 80 hours

Once programming changes are made to GenTax by IT, Financial Distributions Bureau (FDB) staff will need to verify the changes by performing selected tests of data and functionality, prior to authorizing IT to move changes into production. Programming changes and testing would need to be completed by January 31, 2012. Within the state's central accounting system (SHARE) new subaccounts would need to be created by FDB staff to account for the receipts from the sweetened beverage tax and the distribution to the County Supported Medicaid Fund and Childhood Obesity Prevention Fund.

Appropriation ($thousands)*			R or NR**	Fund(s) or Agency(ies) Affected
FY2011	FY2012	FY 11-12		
0	(23,600)	(23,600)	R	County-Supported Medicaid Fund
0	23,600	23,600	R	Medicaid Services
0	(1,200)	(1,200)	R	Child Obesity Prevention Fund
0	1,200	1,200	R	Department of Health

* Parentheses ( ) indicate an appropriation out of the fund. ** Recurring (R) or Nonrecurring (NR).

Money in the County-Supported Medicaid Fund from the sweetened beverage excise tax shall be expended for Medicaid services. Money in the Child Obesity Fund is appropriated to the Department of Health to support child obesity prevention.

TECHNICAL ISSUES

TRD:

Since the excise tax would be administered pursuant to the Tax Administration Act, Section 7-1-2 NMSA 1978 should be amended to include the Sweetened Beverage Excise Tax Act. Also it is suggested that Section 4, Subsection A be amended to clarify that the excise tax is imposed on each ounce of sweetened beverage "sold by the distributor," in order to avoid any interpretation that the tax is imposed on retail sales.

JAG/svb

The Legislative Finance Committee has adopted the following principles to guide responsible and effective tax policy decisions:

1. ***Adequacy:*** *revenue should be adequate to fund government services.*
2. ***Efficiency:*** *tax base should be as broad as possible to minimize rates and the structure should minimize economic distortion and avoid excessive reliance on any single tax.*
3. ***Equity****: taxes should be fairly applied across similarly situated taxpayers and across taxpayers with different income levels.*
4. ***Simplicity***: *taxes should be as simple as possible to encourage compliance and minimize administrative and audit costs.*
5. ***Accountability/Transparency:*** *Deductions, credits and exemptions should be easy to monitor and evaluate and be subject to periodic review.*

More information about the LFC tax policy principles will soon be available on the LFC website at www.nmlegis.gov/lcs/lfc