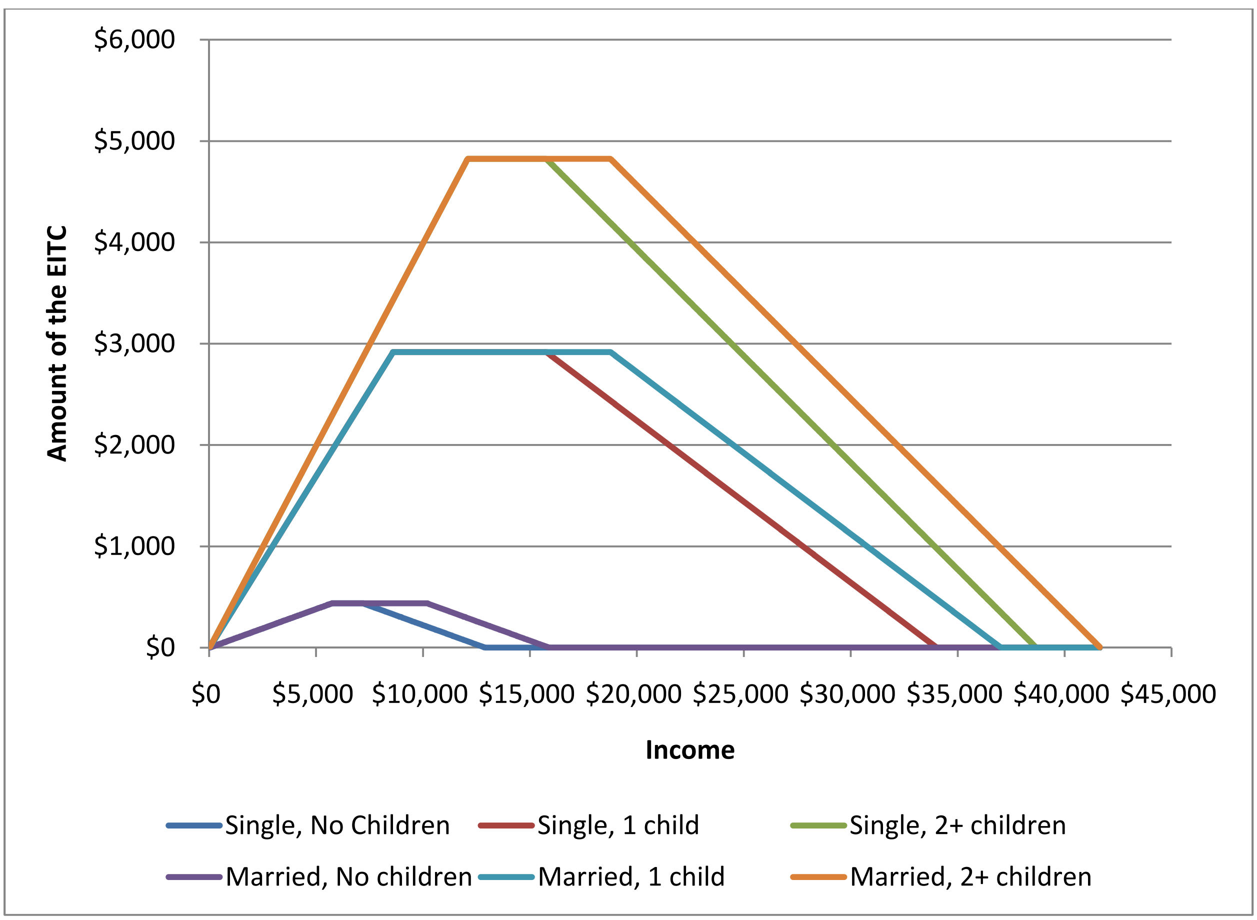
To: Mark Buchi
From: Larry Walters

Re: Mitigating the regressive effects of restoring the sales tax on groceries.

First, let me comment on what I see as problematic about linking any tax credit to the EITC. The following chart shows the amount of the EITC for different income levels, filing status and family size. You will note that there are three distinct phases: ramp up, plateau and phase out. If a tax credit intended to offset the regressive effects of the sales tax on food is tied to the EITC, the majority of the benefits will go to households with income in the $10,000 to $25,000 range. Thus, those most in need (families making less than $10,000) will receive a relatively small share of the benefits. Based on the 2007 state income tax data, that represents somewhere in excess of 167,000 Utah households, plus those who do not file returns. The other problem is that many low income households do not qualify for or do not claim the EITC. Based on 2007 Federal data for Utah, only 25% of those with reported AGI of less than $10,000 received any EITC. The percentage does increase for higher incomes to around 55%.



If we are to have a system which is easy to administer and easy to understand, I suggest that for most people the credit needs to show up on the state income tax return. I would suggest we consider a much flatter credit. I have reviewed Phil Dean's analysis and done a bit more on my own and would offer the following observations.

1) We need to be a bit careful about using the Consumer Expenditure Survey estimates for expenditures for food consumed at home. The CES reports that in the west region, expenditures in this category are about 10.6% higher than the national average.
2) Making the adjustment for regional differences, if the sales tax rate were 4%, households with incomes below $20,000 would be spending between $96 and $110 per year. Households with incomes between $20,000 and $40,000 would spend between $122 and $145 per year.
3) Nearly 55% of the households filing 2007 Utah state income tax returns reported AGIs of $40,000 or less.

Based on these observations and a few other calculations, I would propose that we consider a two-tiered tax credit tied simply to AGI. For those with AGI of $20,000 or less, there should be a refundable credit of $100. For those with AGIs between $20,000 and $40,000, the refundable credit should be $50.

If all filing households took advantage of this credit, the cost to the state would be about $45 million annually, based on the distribution of 2007 returns. Based on participation levels in the EITC, the actual number is likely to be much smaller.

For those who do not file a state tax return, we will need to have a simple (but auditable) alternative form that is widely distributed and easily accessible.

Cc: Keith Prescott