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FISCAL IMPACT REPORT

ORIGINAL DATE 2/1/18
 SPONSOR Pirtle LAST UPDATED 2/9/18 HB _____
 SHORT TITLE Tax Definition Of "Food" & SNAP Program SB 129
 ANALYST Iglesias

REVENUE (dollars in thousands)

Estimated Revenue					Recurring or Nonrecurring	Fund Affected
FY18	FY19	FY20	FY21	FY22		
\$0.0	\$82,370.0	\$82,020.0	\$81,520.0	\$81,140.0	Recurring	General Fund
\$0.0	\$7,070.0	\$7,690.0	\$8,440.0	\$9,040.0	Recurring	Counties
\$0.0	\$8,730.0	\$10,820.0	\$13,360.0	\$15,620.0	Recurring	Municipalities
\$0.0	\$98,170.0	\$100,530.0	\$103,320.0	\$105,800.0	Recurring	TOTAL

Parenthesis () indicate revenue decreases

SOURCES OF INFORMATION

LFC Files

Responses Received From

Human Services Department (HSD)
 Taxation and Revenue Department
 Department of Health (DOH)

SUMMARY

Senate Bill 129 limits the definition of food qualifying for a deduction from gross receipts tax to food items approved by the department of health for the federal special supplemental nutrition program for women, infants, and children (WIC), as well as unprocessed meat, poultry and fish, and flour tortillas. ¹ The bill also seeks to restrict purchases under the Federal Supplemental Nutrition Assistance Program (SNAP) to those foods available under WIC and meat purchases.

The effective date of this bill is July 1, 2018.

FISCAL IMPLICATIONS

By narrowing the definition of food, in effect the bill makes all food that does not meet WIC definitions taxable under the gross receipts tax. Net effects of the bill are presented in the

¹ For a list of WIC-eligible foods, see http://archive.nmwic.org/grocers/approved_grocer_list.php.

revenue table on page one. The table below shows gross effects of the changes, as well as changes to hold harmless distributions. The estimate does not assume any changes in consumption.

Estimated Revenue					R or NR **	Fund Affected
FY18	FY19	FY20	FY21	FY22		
\$0.0	\$45,200.0	\$46,300.0	\$47,600.0	\$48,700.0	Recurring	General Fund (deduction)
\$0.0	\$14,490.0	\$14,830.0	\$15,240.0	\$15,620.0	Recurring	Counties (deduction)
\$0.0	\$38,480.0	\$39,400.0	\$40,480.0	\$41,480.0	Recurring	Municipalities (deduction)
\$0.0	\$37,170.0	\$35,720.0	\$33,920.0	\$32,440.0	Recurring	General Fund (hold harmless)
\$0.0	(\$7,420.0)	(\$7,140.0)	(\$6,800.0)	(\$6,580.0)	Recurring	Counties (hold harmless)
\$0.0	(\$29,750.0)	(\$28,580.0)	(\$27,120.0)	(\$25,860.0)	Recurring	Municipalities (hold harmless)

The estimated fiscal impact uses data from a November 2016 report commissioned by the United State Department of Agriculture (USDA) titled, *Foods typically purchased by Supplemental Nutrition Assistance Program (SNAP) households*. The overall study found few significant differences between SNAP and non-SNAP households. Based on this study’s findings, about 50 percent of all foods purchased would qualify as taxable under this bill.

	SNAP Household Expenditures		Non-SNAP Household Expenditures	
	\$ millions	% of total	\$ millions	% of total
Meat, Poultry & Seafood	\$1,262.9	19.2%	\$5,016.3	15.9%
Vegetables	\$473.4	7.2%	\$2,873.9	9.1%
Cheese	\$186.4	2.8%	\$948.9	3.0%
Fruits	\$308.2	4.7%	\$2,271.2	7.2%
Milk	\$232.7	3.5%	\$1,211.0	3.8%
Baby food	\$126.8	1.9%	\$198.2	0.6%
Eggs	\$73.8	1.1%	\$388.2	1.2%
Beans	\$38.3	0.6%	\$234.5	0.7%
Juice	\$43.5	0.7%	\$269.0	0.9%
Baked breads	\$163.7	2.5%	\$874.8	2.8%
Soft Tortillas and Wraps	\$23.7	0.4%	\$113.1	0.4%
Cereal	\$186.9	2.8%	\$933.9	3.0%
Yogurt	\$59.9	0.9%	\$442.3	1.4%
Peanut Butter	\$20.4	0.3%	\$127.8	0.4%
Non-taxable food	\$ 3,200.6	48.6%	\$ 15,903.1	50.5%

Source: U.S. Department of Agriculture, *Foods Typically Purchased by Supplemental Nutrition Assistance Program (SNAP) Households*, November 2016.

Using these percentages, and applying them to NM population-weighted “food-at-home” averages from the Bureau of Labor Statistics, Consumer Expenditure Survey, LFC staff calculate that the average New Mexico household spends \$1,918 a year on taxable food items as defined by this bill, out of a total food expenditure of \$3,836. These are 2015 statistics. Estimates are

adjusted annually based on IHS Global Insight’s projections for changes in the consumer price index for food.

Estimates provided by the Taxation and Revenue Department (TRD) used a different methodology for determining the fiscal impact. TRD estimates the total revenue generated from this bill to range between \$121 million and \$138 million annually, about \$70 million to \$80 million of which would be to the general fund due to GRT on some food items and reductions in hold harmless payments to local governments.

Unlike previous similar versions of this bill (2017 SB441), this bill seeks to alter the exemption for food purchased with SNAP EBT cards by restricting SNAP-eligible foods to those foods that are WIC-eligible as well as meat purchases. As of January 2018, data from USDA show approximately 19.4 percent of households in New Mexico receive SNAP benefits. Under current law, all SNAP purchases are non-taxed, and this would not change. However, by restricting the types of foods allowed to be purchased with SNAP benefits to WIC definitions (plus meat), then SNAP recipients could not use their SNAP benefits to purchase food items that do not meet the new definition. They would have to purchase those foods using means other than a SNAP EBT card.

Notably, the revenue estimate is a conservative one. The USDA report used to gather data for the estimate does not classify some foods to a granular level such that a more accurate revenue estimate can be calculated. For example, the WIC food definition includes whole wheat and whole grain bread, but not other types of breads. The USDA report provides a food expenditure amount for baked breads, but not all variety of breads. Therefore, the estimate assumes all breads are tax deductible, wherein only a portion of those breads will actually qualify for the deduction. Therefore, the revenue estimate is smaller than it would be if only whole wheat and whole grain breads were considered. Such is also the case with estimates of cereal and juices, in which the USDA report data is broader than the WIC definitions, resulting in an underestimate of the potential revenue generated.

The total county and municipal tax rates and the hold harmless distribution rates were obtained from an RP500 based spreadsheet, which was built to calculate the impact of adjusting the hold harmless distributions.

SIGNIFICANT ISSUES

GRT Food Deduction and Hold Harmless. The original legislation for the GRT food deduction enacted provisions to hold harmless the revenues of municipal and county governments from any lost revenue resulting from the deduction. Therefore, the state effectively has two tax expenditures: the lost revenue from not taxing food products, and the payments to municipalities and counties. The GRT deduction was originally enacted in 2004 and has not been amended. The hold harmless provision was originally enacted in 2004 and was amended in 2013 to phase out the distribution to larger counties and municipalities over a 15-year period.

By reinstating GRT for select food items, this bill would have the effect of generating revenues directly from the tax and indirectly through reduced hold harmless obligations. According to the Taxation and Revenue Department’s 2016 Tax Expenditure Report, the GRT food deduction benefits consumers by reducing the costs of food; however, because of the hold harmless provision and the loss of revenue made up through other tax burdens, this reduction has

significant cost to both the general fund and the taxpayers it benefits. In FY16, the cost of the GRT food deduction was \$142 million and the cost of hold harmless payments was \$94.3 million.

SNAP Qualifying Foods. Under current law, receipts from qualifying food sales at retail food stores as defined under the federal SNAP program are deductible from gross receipts. Except for clear exclusions – such as alcoholic beverages, tobacco products, vitamins, and food to be eaten in the store – the SNAP approved food list is unrestricted.²

According to the New Mexico Department of Health (DOH), “SNAP provides benefits to people with extreme financial need and who live under or below federal poverty levels. It provides basic subsistence for elderly, homebound, handicapped, and homeless people. Unlike WIC, SNAP benefits include foods that are easy to prepare or ready-made to heat and eat and this bill removes foods that are pre-prepared. [This bill] could negatively impact elderly, battered, disabled, and homeless who may not be able to prepare their own foods either due to skill level, disability, or homelessness.”

As noted above, this bill does *not* alter the tax exemption for food purchased with SNAP benefits. SNAP purchases will remain tax-exempt. However, the bill does seek to limit the types of foods that be purchased with SNAP benefits to those that meet WIC definitions and meat purchases. The New Mexico Human Services Department (HSD) indicates that states across the country have previously submitted waivers to the USDA/FNS to restrict SNAP purchases; however, to date, such waiver applications have been denied.

According to TRD, if a waiver is received from the U.S. Secretary of Agriculture to restrict purchases under the federal SNAP program to the food items defined by New Mexico, there is a possibility of a change in federal funding levels.

Flour Tortillas. The rationale for specifying flour tortillas in Section 1 of this bill is to address the issue that only whole-wheat tortillas are included in the WIC definition of qualifying foods. Thus, flour tortillas will continue to be non-taxed. However, Section 2 of the bill does not specify flour tortillas in the new, narrowed SNAP eligibility requirements. In effect, this means SNAP recipients could *not* use their SNAP benefits to purchase flour tortillas.

Impact on Grocers and Food Vendors. If this bill were enacted, each individual New Mexico food vendor would need to re-program their current point-of-sale and grocer systems to identify the purchase of certain types and brands of food as taxable and to identify certain types and brands of foods as SNAP-eligible.

The responsibility of administering and tracking which foods are deductible from GRT will fall on the Taxation and Revenue Department (TRD) and individual retail stores. In response to similar legislation (2017 SB441), TRD stated the nature of the WIC program and the current structure of retail sales in relationship to the WIC program make this new definition of food under Section 7-9-92 NMSA 1978 administratively difficult for retailers and TRD (see below).

Differences in the SNAP and WIC Programs. There are several fundamental differences between the SNAP and WIC programs. These factors directly impact the complexity of

² List of eligible food items on the SNAP program: <https://www.fns.usda.gov/snap/eligible-food-items>

switching the GRT deduction from food as allowed under SNAP to food as allowed under WIC. Due to the current broad eligibility of food items under SNAP, this is a more manageable program for retail stores in terms of programming Universal Product Codes (UPC), which retailers uniquely assign to each trade item. However, since WIC serves a narrow population of pregnant or postpartum women, infants, and children up to age 5, the food allowed under this program focuses on the nutritional value of the food to supplement this population's diet. Retail stores have to program their systems to uniquely identify those foods that may be purchased under the WIC benefit.

Administrative Complexity of the WIC Program. WIC is a grant program and receives a finite budget each year which is then allocated to states. Because of the budget constraint, the New Mexico WIC program limits the brands and types of food under the major categories. For example, cheese that can only be purchased in block form is further limited by brand. More expensive brands are not approved by the New Mexico WIC program. This added brand restriction makes it challenging for both the WIC participant and the retailer. But for the retailer, this adds another layer of complexity in programming which UPC codes will be accepted by the WIC program. National retailers such as Kroger cannot have a nationwide WIC approved list, as each state modifies the WIC list to meet their program needs. Added to this complexity is that WIC-approved foods may change each year due to federal nutrition and program guidelines and the New Mexico program adjusting to budget constraints.

ADMINISTRATIVE IMPLICATIONS

The primary impact to TRD will be taxpayer education. Because WIC-approved food lists are complex and changing, it will be particularly difficult for food markets not already equipped for WIC purchases to re-program their systems to accommodate this bill's changes. TRD will need to establish a working relationship with the Department of Health and its WIC program to coordinate and maintain the definition of food for this deduction.

Taxpayers (food vendors) will need assistance from TRD to clearly understand what may be taken as a deduction and to update their systems and business processes to properly meet the definition by the bill's effective date. The scope of what is required for taxpayers will need further research and understanding.

TRD indicates complications in audit may be encountered when auditing a retail food store. Auditors will have to make a determination whether food or food products sold are approved by the Department of Health for the SNAP and WIC programs. The different requirements on the content of fat, sugar, etc. on food products will increase the complexity of verification of transactions.

Given the administrative complexity on the part of TRD and food markets, as well as the need for substantial taxpayer education on this change, the July 1, 2018 effective date of this bill may not be feasible. An effective date of January 1, 2019 is suggested.

TECHNICAL ISSUES

Although the bill specifies flour tortillas as a non-taxable food item, it does not separately specify flour tortillas as a SNAP-eligible food. Instead, the bill limits SNAP-eligibility to meat purchases and foods that meet WIC definitions. Only whole-wheat tortillas are included in the

WIC definition of qualifying foods, which means SNAP recipients could *not* use their SNAP benefits to purchase flour tortillas. If the intent is limit SNAP eligibility to the same foods that the bill identifies as non-taxable, then flour tortillas may need to be specified separately in Section 2-A of the bill.

OTHER SUBSTANTIVE ISSUES

According to the New Mexico Department of Health (DOH), this bill is related to DOH's strategic plan relative to improved health status for New Mexicans.

The revenue estimates for this bill assume no changes in food consumption due to the tax. However, impact of taxes on the prices consumers pay can affect what consumers eat and drink. Nevertheless, the size of this response varies. For example, consumers may find it easier to switch away from sugary drinks, which may have alternatives, than from other foods and drinks. Thus, taxes are an imprecise way to address many nutritional concerns. More research is needed to determine how taxes affect entire diets, how diets change over prolonged periods, and how responses vary across different groups of people. While taxing unhealthy food choices may narrow the price gap between healthy and unhealthy foods, in which unhealthy foods tend to be less expensive, imposing such a tax may disproportionately affect those less able to afford it.³

Does the bill meet the Legislative Finance Committee tax policy principles?

- 1. Adequacy:** Revenue should be adequate to fund needed government services.
- 2. Efficiency:** Tax base should be as broad as possible and avoid excess reliance on one tax.
- 3. Equity:** Different taxpayers should be treated fairly.
- 4. Simplicity:** Collection should be simple and easily understood.
- 5. Accountability:** Preferences should be easy to monitor and evaluate

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³ Chriqui et al., 2007, State Sales Tax Rates for Soft Drinks and Snacks Sold Through Grocery Stores and Vending Machines, *Journal of Public Health Policy*, 29(2), 226-249.