



TAXATION AND BUDGET REFORM COMMISSION

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Staff Analysis and Economic Impact Statement

Measure: CP 7

REFERENCE:

ACTION:

Sponsor: Finance and Taxation
Committee

1. FTC
2. GPSC
- 3.

Pre-meeting

Subject: Legislative review and vote to
repeal sales tax exemptions

Date: February 6, 2008

I. Summary:

Constitutional Proposal 7 requires the Legislature to take a roll-call vote on whether to repeal each sales tax exemption as part of a review of sales tax exemptions. Revenue gained as the result of this measure must be used to lower the sales tax rate or reduce the required local effort component of property taxes.

II. Present Situation:

The *2007 Florida Tax Handbook* estimates that Florida's sales tax will raise \$23,581,500,000 for fiscal year 2007-2008. The value of a 1 percent levy on the sales tax base was estimated to be \$3.9303 billion.¹

Sales Tax

Florida law provides that each sale, admission charge, storage, or rental is taxable unless the transaction is specifically exempt. Florida's general sales tax rate is 6 percent. However, there is an established "bracket system" for collecting sales tax on any part of each total taxable sale that is less than a whole dollar amount. Additionally, a discretionary sales surtax is imposed by many Florida counties. To compute the Florida sales tax rate for each county, the county imposed discretionary sales surtax rate is added to the general sales and use tax rate.²

Discretionary Sales Surtax

Under specific conditions, Florida counties are authorized to levy a discretionary sales surtax on most transactions that are subject to sales and use tax. A dealer who sells and delivers taxable merchandise or taxable services is required to collect the surtax at the

¹ The Florida Senate, *2007 Florida Tax Handbook: Including the Fiscal Impact of Potential Changes*, p. 114 (2007).

² Department of Revenue, Florida Sales and Use Tax, http://dor.myflorida.com/dor/taxes/sales_tax.html (last visited Jan. 15, 2008).

rate imposed in the county where the merchandise or service is delivered. For motor vehicle and mobile home sales, the surtax rate of the county where the vehicle or mobile home will be registered is used to calculate the appropriate tax.³

Only the first \$5,000 of a single sale of tangible personal property is subject to a discretionary sales surtax if the property is sold as a single item, in bulk, as a working unit, or as part of a working unit. The \$5,000 limit does not apply to commercial rentals, transient rentals, or services.⁴

Use Tax and Consumption

Use tax complements, and is applied in the same manner as, sales tax. The use tax rate and sales tax rate are the same, including discretionary sales surtax, if applicable. Use tax is due on purchases made out of state and brought into Florida within 6 months of the purchase date. Also, if you purchase a product tax-exempt that you plan to sell at retail, but end up using it at your place of business, the “use” of the product is subject to tax. If you purchase materials that are “consumed” in a manufacturing process to create your end product, but are not part of the end product, those materials are subject to tax.⁵

The “use” component of the sales and use tax provides uniform taxation on items that are purchased outside Florida, but are used or stored in the state. If the item brought into Florida is subject to tax, a credit for lawfully imposed taxes paid to another state, a U.S. territory, or the District of Columbia is permitted. Credit is not given for taxes paid to another country.⁶

Sales Tax Exemptions

The *2007 Florida Tax Handbook* lists 246 exemptions from the sales tax.⁷ The *Tax Handbook* states that several of the exemptions are fundamental to the structure of the tax. These structural exemptions include:

- Items purchased for subsequent resale;
- Intangible personal property;
- Tangible personal property imported or produced for export; and
- Purchases of agricultural products used in further processing for resale.

The revenue impact of the remaining exemptions is estimated to be \$12.3403 billion. However, the *Tax Handbook* notes that some of the exemptions overlap such that the repeal of all of the exemptions, excepting the structural exemptions, would yield less than \$12.3403 billion. Of non-structural exemptions:

- \$8.15 billion relate to household items;
- \$0.67 billion relate to organizations;

³ *Id.*

⁴ *Id.*

⁵ *Id.*

⁶ *Id.*

⁷ The Florida Senate, 2007 Florida Tax Handbook: Including Fiscal Impact of Potential Changes

- \$2.16 billion relate to business items; and
- \$1.35 billion relate to miscellaneous items.⁸

Sales Tax on Services

In 1986, the Legislature repealed the sales tax exemptions on services, effective July 1, 1987. In 1987, the Legislature integrated the tax on services with the sales tax on tangible personal property. In a 1987 special session, the Legislature repealed the sales tax on services, effective January 1, 1988. Accordingly, the state's experience with a broad-based sales tax on services lasted six months.

Most services are not [currently] subject to Florida's sales tax. This lack of tax on most services is not due to an exemption from the tax, but from the fact that services are not specified as taxable. There are basically two exceptions to this. First, s. 212.05(1)(k), F.S., specifically states that detective, burglar protection, and other protective services and nonresidential cleaning and pest control services are subject to the sales tax.⁹

Second, the definition of "sales price" in s. 212.02, F.S., states that the amount paid for tangible personal property includes any services which are part of the sale "without any deduction therefrom on account of the cost of property sold, the cost of materials used, labor or service cost, interest charged, losses, or any other expense whatsoever." The definition also states that sales price includes "the consideration for a transaction which requires both labor and material to alter, remodel, maintain, adjust, or repair tangible personal property."¹⁰

The third component important in the discussion of sales tax on services is the exemption in s. 212.08(7)(v), F.S., relating to a professional, insurance, or personal service transaction that involves sales of tangible personal property as "inconsequential," and elements for which no separate charges are made. Thus, even though a lawyer might issue a written opinion in the performance of his or her duties, the written report is considered inconsequential to the main service of rendering the opinion.¹¹

The *Tax Handbook* estimates that the annualized receipts from the application of the state sales and use tax on service transactions for fiscal year 2007-2008 would yield \$23.4144 billion.

III. Effect of Proposed Changes:

Constitutional Proposal 7 requires the Legislature to take a roll-call vote on whether to repeal each sales tax exemption as part of a review of sales tax exemptions. Revenue gained as the result of this measure must be used to lower the sales tax rate or reduce the required local effort component of property taxes.

⁸ *Id.* at 118.

⁹ The Florida Senate, Fiscal Resource Committee, *Sales Tax Exemptions: A Tool for Lowering the Sales Tax Rate in Florida* 13 (Aug. 2000).

¹⁰ *Id.*

¹¹ *Id.* at 13-14.

Review Procedure and Components

The measure requires the Legislature to establish a procedure to review exemptions prior to January 1, 2009. This procedure likely would be promulgated through a joint legislative rule. This rule may develop a process to identify the measures on which votes will be taken as part of the review. However, this measure, by operation of Article XI, s. 5(e) of the Florida Constitution, will not take effect until January 6, 2009. Thus, the Commission may wish to amend the measure to delay the date by which the Legislature must establish procedures until at least the end of the 2009 regular session.

The first component of the review required by this measure is a review of exemptions for conformance with the principles of equity, compliance, pro-competitiveness, neutrality, stability, and public purpose. These principles may have had their genesis in a report of the State Tax Reform Task Force.¹² These principles were also components of HB 195 (2006) and HB 2027 (2002). The result of this review will likely be a report produced by Legislative staff at the direction of the Legislature.

The second component of the review is a roll-call vote on whether to repeal each exemption from the sales tax. The measure provides for the vote to occur during the 2010 regular session. The procedure for the vote requires the Legislature to vote on a series of questions, rather than a bill or resolution. The questions are structured as follows:

“Shall the exemption from the tax on sales, use, and other transactions for (the subject of exemption) authorized under (the specific section, subsection, paragraph, etc.), Florida Statutes, be repealed?”

Upon an affirmative vote of both houses of the Legislature the exemption is repealed. The measure does not permit the Governor to veto the repeal of an exemption by the Legislature. For ease of administration and notice to sales tax dealers, the Commission may wish to specify an October 1, or January 1, date as the effective date of the repeal of an exemption.

Upon repeal of an exemption, the Office of Legislative Services, Division of Statutory Revision likely will conform the statutes accordingly.¹³ However, the Commission may wish to consider the use of a bill to repeal exemptions to avoid creating confusion as to the duties of the Division of Statutory Revision and to include the Governor in the process.

The measure defines exemption as a “single transaction or an exemption set forth in a section, subsection, or paragraph of chapter 212, Florida Statutes, whichever describes the fewest number of transactions.” Multiple exemptions and subcategories of exemptions can be contained in a single paragraph of a section of chapter 212, Florida Statutes. The Commission may wish to consider whether the measure should be amended to ensure that both houses of the Legislature will vote on the same issues. Perhaps, the

¹² The State Tax Reform Task Force was created by ch. 2000-222, L.O.F.

¹³ See s. 11.242(5), F.S., for the authority of the Division of Statutory Revision.

measure should expressly require the creation of a joint committee to identify the issues presented to a vote of both houses of the Legislature.

Exempt Exemptions

This measure expressly excludes from the review the exemptions for:

- Groceries;
- prescription drugs;
- health services;
- residential rent;
- electricity and heating fuel;
- items purchased for subsequent resale;
- intangible personal property;
- tangible personal property imported or produced for export; and
- purchases of agricultural products for further processing for resale.

These items refer to the important structural exemptions and to broad categories of exemptions, as opposed to specific exemptions identified by statute. These exemptions likely correspond to nearly the full revenue impact of the exemptions categorized as “household items” in the *Tax Handbook*. Viewed broadly, the categories of exemptions may refer to the items described as excerpted from the *Tax Handbook* below.

Line No.	Exemption	Revenue Impact (in \$ m)	Type
17	Rent charges paid by certain long term occupants.	4.0	Household
18	Rent charges paid by certain full-time students.	33.1	Household
19	Rent charges paid by active military personnel.	32.0	Household
20	Rent charges paid by permanent residents.	1,259.2	Household
21	Charges for rent in certain mobile home parks.	3.3	Household
22	Rent charges for living accommodations in migrant labor camps	13.1	Household
99	Groceries purchased for human consumption.	2,651.5	Household
100	Food purchased with food stamps.	1.2	Household
101	Prescription drugs.	896.0	Household
102	Non-prescription drugs.	199.0	Household
103	Eyeglasses and other corrective lenses.	44.3	Household
104	Medical supplies and products such as syringes and prosthetics.	114.8	Household
160	Charges for hospital meals and rooms.	603.2	Household
161	In-facility meals purchased by residents of homes for the aged.	22.2	Household
162	Purchases of power & heating fuels by residential households.	2,178.9	Household
200	Nonprofit cooperative hospital laundries.	0.1	Business
207	Complimentary food items.	0.8	Business
208	Food or beverages donated to nonprofit organizations.	<u>0.3</u>	Organization
		8,057.0	

The maximum amount of revenue that may be gained by the repeal of all non-structural sales tax exemptions is estimated to be \$12.3403 billion.¹⁴ The most that the Legislature will be able to recover from the non-exempt exemptions is slightly more than \$4 billion.

Revenue Neutrality

The measure requires revenue neutrality. Additional revenues must lower the sales tax or reduce the required local effort component of property taxes. However, the required local effort requirement changes from year to year. As a result, it may be impossible to determine whether the Legislature acts in good faith if it chooses to reduce property taxes, rather than reduce the sales tax rate.

Expiration Date

This measure provides for a one-time review of sales tax exemptions and expires on January 1, 2011.

Effective Date

By operation of Article XI, s. 5(e) of the Florida Constitution, this measure will take effect on January 6, 2009.

IV. Constitutional Issues:**A. Constitutional or Legislative Matter:**

Previously, HB 195 (2006) and HB 2027 (2002) proposed a statutory mechanism to provide for a review of sales tax exemptions. However, a statute requiring a Legislature to review sales tax exemptions can be amended or repealed by a future Legislature.¹⁵

B. Other Constitutional Issues:

None.

V. Economic Impact and Fiscal Note:**A. Tax/Fee Issues:**

This measure may facilitate the repeal of sales tax exemptions by the Legislature. However, revenues gained must be offset by a lower sales tax rate or a reduction in the required local effort component of property taxes.

B. Private Sector Impact:

¹⁴ The *Tax Handbook* states that some exemptions overlap. As a result the repeal of all exemptions would generate less than \$12.3403 billion.

¹⁵ *Neu v. Miami Herald Pub. Co.*, 462 So. 2d 821, 824 (Fla. 1985) (stating that “a legislature may not bind the hands of future legislatures by prohibiting amendments to statutory law”).

This measure may facilitate the repeal of sales tax exemptions by the Legislature. However, revenues gained must be offset by a lower sales tax rate or a reduction in the required local effort component of property taxes.

C. Government Sector Impact:

The Department of Revenue will have to notify sales tax dealers of the repeal of sales tax exemptions.

VI. Technical Deficiencies:

The date of “January 1, 2009” on line 19 by which the Legislature must establish review procedures occurs before the January 6, 2009 effective date of the measure. The Legislature should be given at least one session, if not two, to develop review procedures. As such, should be replaced with a date that occurs after the 2009 or 2010 regular sessions.

The word “residential” should be inserted before the word “electricity” on line 55.

The parenthetical statement on line 69, “(the subject of exemption)” should add the word the after the word “of.”

VII. Related Issues:

For ease of compliance by the Legislature, the Commission may wish to identify the specific sales tax exemptions, rather than categories of exemptions that are excluded from the review required by this measure.

The measure defines exemption as a “single transaction or an exemption set forth in a section, subsection, or paragraph of chapter 212, Florida Statutes, whichever describes the fewest number of transactions.” Multiple exemptions and subcategories of exemptions can be contained in a single paragraph of a section of chapter 212, Florida Statutes. The Commission may wish to consider whether the measure should be amended to ensure that both houses of the Legislature will vote on the same issues. Perhaps, the measure should expressly require the creation of a joint committee to identify the issues presented to a vote of both houses of the Legislature.