

A Fair Tax Swap

By Kimble Forrister

Not all tax breaks are created equal. Bad tax breaks give unfair advantage to one group of taxpayers. Good tax breaks protect the essential money people need to survive.

* That's why all but two states give some kind of sales taxes break for groceries.

* That's why Alabama offers a homestead exemption: We don't pay property tax on the first \$40,000 of value of our homes. (And we need to update that amount for inflation.)

* That's why most states have income tax deductions to exempt from taxes at least the first \$20,000 of income for a family of four.

Rep. John Knight's House Bill 555 would update our income tax deductions and cut the grocery tax as well. When Arkansas cut its grocery tax in half this year, it left Alabama and Mississippi as the only states that still charge a sales tax on groceries without any rebate or reduced rate.

Alabama's regressive tax looks most unfair as you cross the Florida line. When you buy \$100 worth of groceries in Montgomery or Mobile, you pay \$110. When you buy \$100 worth of groceries in Pensacola, you pay \$100.

This tax on groceries is "only" 10 cents on the dollar, but it adds up, week after week, month after month. Of all the elements of tax reform, reducing the grocery tax is probably the most popular. People don't think we should tax the essentials of life. We exempt prescription drugs, so why do we still tax groceries?

One reason is that we've disagreed on how to fill the budget gap if we didn't. To replace the four-percent state portion of the tax, we need to find about \$300 million for public education. For the local remainder, it's more complicated. In some counties, the supermarket is a major source of revenue for public safety and education.

Our neighboring states have each taken a different approach. Florida has no grocery tax; Tennessee reduced the sales tax on groceries by one percent, which doesn't give much relief; and Georgia exempted groceries from the state portion of the sales taxes, but left them subject to local sales taxes. That means that in a given county you might pay two percent on groceries and six percent on detergent or toothpaste.

Of all these ideas, the most viable for Alabama is Georgia's approach, removing the state tax and leaving the local portion alone. Under Knight's bill, the 4-percent state sales tax would no longer apply to groceries, but the local portion of the sales tax (ranging from 7 percent in Arab to zero in Leroy) would still apply to these items.

What does this mean for consumers? According to the USDA website, a family of four with a

“moderate” grocery bill pays \$181 a week. That family would save \$376 a year if we remove the state portion of the grocery tax. The USDA says that two adults with a “moderate” grocery bill pay \$113 a week. They would save \$235 a year.

Removing the 4-percent state grocery tax would be good for family budgets, but what about replacing the revenue it raises for schools? Where else can we find \$300 million?

The answer proposed by John Knight is to close an income tax loophole that has outgrown its usefulness: the income tax deduction for federal income tax. It sounds good, but in fact it’s an unfair deduction. This deduction will cost Alabama nearly \$600 million next year, and about 80 percent of that amount will go to the top one-fifth of earners.

Consider how this deduction differs in its effects on high- and middle-income earners. For those with incomes over \$300,000 a year, the deduction reduces state income taxes by thousands of dollars. For the average filer in the middle three-fifths of earners, it reduces taxes by less than \$100.

If we swap the deduction for federal income tax for a four-percent reduction in the grocery tax, most middle-income families will trade in that tax cut worth less than \$100 for a grocery tax cut worth two or three times that much. It’s going to be important for voters to understand the swap, because they will have to approve it next February in a constitutional amendment.

If Alabama ends the \$600 million deduction for federal income tax and fills the \$300 million hole left by the grocery tax, we will have about \$300 million left over. Knight would use this balance to expand the standard deduction to \$11,100 per couple and the personal exemptions to \$2,000 for every child and adult. This is partly a matter of equity, granting children the same “value” as adults, and partly a matter of economics, catching up with 70 years of inflation. The plan would also expand deductions for small businesses that provide health insurance to their employees. And we can do all this without diverting tax dollars from our schools.

It’s a simple concept. To make our tax system family-friendly, we need to expand the good tax breaks and end a very bad one. If the Legislature approves House Bill 555, Alabama voters will have a chance to close a \$600 million tax loophole, reduce the tax on groceries by 4 percent, and expand income tax deductions that should have been updated decades ago.

It’s a swap worth making.

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