

The Beacon Hill Institute



The Economic Effects of a Meals Tax on Virginia Localities

**THE BEACON HILL INSTITUTE FOR PUBLIC
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Introduction

State and local level of governments increasingly turn to the taxation of prepared foods as a source of revenue. Twenty states and the District of Columbia authorize a tax on prepared food, commonly known as a “meals tax.” Maine and New Hampshire levy only a state meals tax, while both state and local governments in Vermont levy meals taxes.¹

Local governments use meals taxes to raise additional revenue outside traditional sources of revenue, particularly property taxes. Like taxes on hotel rooms and rental cars, the burden of a meals tax falls partly on visitors from other states, and thus non-voters. This makes meals taxes particularly attractive in tourist destinations, and other localities where a substantial portion of the tax burden can be offloaded to out-of-town visitors.

The state of Virginia allows local governments to levy a meals tax on prepared food for immediate consumption. State law authorizes counties to levy a meals tax at a rate of up to 4 percent with the approval of the voters by referendum. However, the counties of Roanoke, Rockbridge, Frederick, Arlington, and Montgomery and individual cities and towns can levy a meals tax without holding a referendum.² Voters in Virginia’s counties have rejected the imposition of a meals tax over the course of 47 of the last 60 referendums, with 57.4 percent of all votes cast against a meals tax.³

¹ Jared Walczak, “Punching the Meal Ticket: Local Option Meals Taxes in the States,” The Tax Foundation: Fiscal Fact, No. 538, (January 2017), <https://files.taxfoundation.org/20170126102319/TaxFoundation-FF538.pdf>.

² VA Code Ann. § 58.1-3833.

³ See Virginia Department of Elections, Elections Database, County/City Questions, 2000-2016, http://historical.elections.virginia.gov/ballot_questions/search/year_from:2000/year_to:2016/text:food.

In Fiscal Year (FY) 2016, over 70 of Virginia’s cities and towns and 45 counties imposed a meals tax. Cities and towns levy meals tax rates ranging from 2.5 percent in Herndon to 8 percent in Orange. The rate averages 5.08 percent across all municipalities when weighted by meals tax revenue collections. In total, counties, cities and towns collected \$539 million in meals tax in FY 2016.⁴

In this report, The Beacon Hill Institute analyses the fiscal and economic impact on selected local economies of a new or increased meals tax.

Analysis of a Virginia Meals Tax on Select Local Economies

The Beacon Hill Institute (BHI) applied its VA-STAMP® (Virginia State Tax Analysis Modeling Program) to estimate the effects of new or increased meals tax on selected local economies.⁵ We assume the tax changes would take place in 2017 and report the results for the first year and five years out, or 2021. The estimates are “dynamic,” in the sense that they capture the effects of the new tax on work, investment and disposable income. Insofar as the tax exerts negative effects on these measures of economic activity, they reduce the amount of revenue gained by levying the tax.

BHI distributed the VA-STAMP simulation to selected counties, cities and towns based on their meals tax base and whether the local government imposes a meals tax. We report the results for the year 2021. Table 1 displays the results for a 4 percent meals tax for selected localities. (For counties that already have a meals tax in place, this simulation captures the impact of an additional 4 percent tax.)

⁴ Auditor of Public Accounts Commonwealth of Virginia, Local Government, Local Government Comparative Report Fiscal Year 2016,

http://www.apa.virginia.gov/APA_Reports/LG_ComparativeReports.aspx.

⁵ Full methodological details are available upon request in a technical appendix.

Table 1: The Economic Effects of a 4% Meals Tax on Local Economies

County	Private Employment (jobs)	Investment (\$)	Real Disposable Income (\$)
Arlington	-1,070	-16,170,488	-77,329,294
Loudoun	-649	-12,516,331	-63,276,819
Fairfax	-2,057	-39,665,581	-200,530,953
York	-174	-2,621,415	-12,535,936
Prince William	-577	-11,133,390	-56,285,307
Floyd	-6	-118,739	-600,291
Town or City			
Alexandria	-535	-8,080,496	-38,641,940
Bristol	-107	-1,624,092	-7,766,610
Newport News	-391	-5,902,671	-28,227,309
Hampton	-307	-4,636,974	-22,174,589
Staunton	-61	-925,097	-4,423,929
Danville	-141	-2,131,556	-10,193,367
Williamsburg	-161	-2,433,590	-11,637,730
Harrisonburg	-211	-3,181,912	-15,216,300

The cities and counties with larger economies would experience the largest impacts. In Fairfax and Arlington counties, employment would drop by 2,057 jobs and 1,070 jobs respectively; investment would fall by \$40 million and \$16 million, and real disposable income would fall by over \$201 million and \$77 million. Floyd and York counties would experience only a fraction of the economic impacts due to their smaller economies. The cities of Alexandria, Newport News and Hampton would see the largest job, investment and real disposable income losses under a 4 percent meals tax.

Conclusion

When elected officials discuss tax increases, they tend to highlight the revenue effects thinking that the increases will result in a needed flow of new revenue. However, any honest discussion must include an estimate of how the economy will respond to tax increases. Tax increases do not exist in a vacuum; consumers, investors and taxpayers often change their behavior in response to higher taxes.

Like all governments, Virginia localities rely on a healthy underlying economy for income. When local governments suffer budget shortfalls, leaders can be tempted to seek additional revenue to fill the gap. However, higher taxes can cause negative economic impacts such as lower employment, investment and incomes. Due to these consequences, most economists recommend against raising taxes during times of budget strain.

The Beacon Hill Institute for Public Policy Research focuses on federal, state and local economic policies as they affect citizens and businesses. The Institute conducts research and educational programs to provide timely, concise and readable analyses that help voters, policymakers and opinion leaders understand today's leading public policy issues.

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