

MSDA

Michigan Soft Drink Association

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William E. Lobenherz, President
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9 June 2010

The Honorable Kate Ebli, Chair
Committee on Tax Policy
Michigan House of Representatives
P.O. Box 30014
Lansing, MI 48909

**RE: HB6219, HB6220
Impose Sales Tax on Vended Foods**

Dear Chairperson Ebli:

For the last several years, legislation has been introduced to levy the state sales tax on soft drinks sold from a vending machine. Even though the legislation has never received sufficient support for passage by the legislature, we have thoroughly researched the issue, and would like to share our conclusions with you.

The Michigan Soft Drink Association strongly opposes the imposition of a sales tax levy on our vended beverages. Such a tax increase would be highly regressive, costs Michigan jobs, offends the Michigan Constitution, and jeopardizes our state's certification for compliance with the Streamlined Sales Tax Project (SSTP).

HIGHLY REGRESSIVE

Both young and low income consumers must use a much greater portion of their after tax income when purchasing soft drinks than consumers with higher incomes. To then impose a tax on top of those purchases would hit the very low income consumer about 10 times harder than the upper middle income family. A basic tenet of good public policy with respect to tax structure is to avoid regressive taxes. To impose this sales tax on vended soft drinks would be considered highly regressive.

COSTS MICHIGAN JOBS

In economic terms, soft drinks have a relatively high negative elasticity of demand, meaning even a very small increase in price has a significant negative impact on sales. It is estimated that soft drinks have an economic elasticity of

demand in the range of -0.4 to -2.37. This means that the imposition of a 6% increase in price would cause sales to drop anywhere from 2.4% to 14%. This would translate to a loss of jobs and income not only for those employed in the soft drink industry, but also in the retail sector.

OFFENDS THE MICHIGAN CONSTITUTION

The Michigan Constitution of 1963 was amended by initiative petition in 1974 to prohibit the levy of a sales tax on prescription drugs and food for human consumption. The only exceptions to this prohibition were “prepared food intended for immediate consumption” and “alcoholic beverages.”

Soft drinks are a food. Their manufacture and sale are regulated as a food under both federal and Michigan law. The courts have unanimously concurred that soft drinks are a food. The scientific community also defines soft drinks as a food, since it contains two (or three, when counting carbohydrates) of the seven basic nutrients considered essential to sustaining life.

The Michigan Constitution is very specific. In order for any food to be subject to the sales tax, the food sold must either be an alcoholic beverage, or it must meet **both** of two criteria:

1. First, it must be “**prepared food.**”
2. Second, it must also be “**intended for immediate consumption.**”

These are two separate and distinct concepts and criteria that must be met. For Michigan, a review of this issue then must address not only SSTP considerations, but also Michigan’s relatively unique position among the states, because this restriction on legislative authority to levy a sales tax on food and beverages is a constitutional prohibition.

JEOPARDIZES SSTP COMPLIANCE

The Streamlined Sales Tax Project (SSTP) was developed to facilitate a state’s ability to significantly increase its sales and use tax collections, especially from operations in other states selling products to Michigan residents and businesses. (You might recall the benefit to the state when Dell Computer’s catalogue operations began collecting and remitting sales and use tax to Michigan once we became SSTP compliant.)

Under SSTP, those states which have changed their sales and use tax statutes to conform to the SSTP provisions may petition SSTP for membership by certifying they are SSTP compliant. Annually thereafter, a state must certify to SSTP that it is compliant.

To be SSTP compliant, the state must stipulate on the SSTP Certificate of Compliance form whether the requirements of the SSTP are met by the state’s

sales and use tax laws. Among the items on the compliance form are a listing of the different food and food products definitions set forth in the SSTP, and a place to certify, if the state statute contains a particular definition, whether it conforms to the SSTP definition. The definitions listed are for:

- Alcoholic Beverages
- Candy
- Dietary supplement
- Food and food ingredients
- Food sold through vending machines
- Prepared food
- Soft drinks
- Tobacco

Michigan has adopted the SSTP definition for “prepared food” and we have certified to the SSTP that we are compliant for that definition.

Under SSTP, and our current sales tax act, “prepared food” means:

- A. Food sold in a heated state or heated by the seller; or
- B. Two or more food ingredients mixed or combined by the seller for sale as a single item; or
- C. Food sold with eating utensils provided by the seller, including plates, knives, forks, spoons, glasses, cups, napkins, or straws. A plate does not include a container or packaging used to transport the food.

It is clear that our product sold from a vending machine does not meet the SSTP definition of being a “prepared” food. This SSTP definition would permit food sold in a heated state from a vending machine to be subject to the sales tax. For the state to levy a sales tax on food sold from a cooled or unheated vending machine, however, it would first have to revise its adopted SSTP definition of “prepared food” as it applies to vending machine sales to add that circumstance (which is what HB6219 tries to do). But then the state’s sales tax law falls out of compliance with the SSTP definitions and potentially jeopardizes many more tax revenues from the SSTP program.

DOUBLE JEOPARDY

While the SSTP specifically states that it makes no attempt to regulate vending machine sales, the SSTP does not contain a similar forgiveness clause with respect to changing the SSTP definition of prepared food.

The state could possibly claim that even if it transgressed the SSTP definition of “prepared food,” as noted above, this should be considered just a minor sin, and the state should therefore retain its overall certification because it is still in

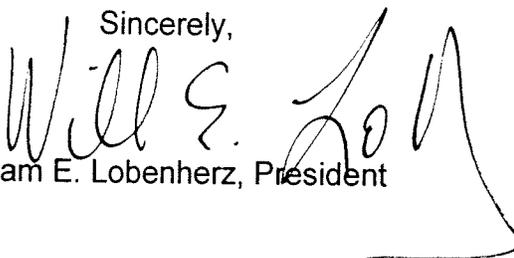
“substantial” compliance. While the state could take a chance on the SSTP’s leniency, this does not cure the legislation’s violation of our state constitution’s prohibition on taxing vended foods and beverages, “except in the case of prepared food intended for immediate consumption as defined by law.”

A court would see the obvious attempt to end run the constitutional prohibition by blurring the distinction between “prepared food” and food “intended for immediate consumption.” These are two separate and distinct concepts and criteria that must be met for a food to be subject to the sales tax, and this legislation seeks to disguise or confuse those two preconditions by combining them into one definition. It would be obvious to the court (and probably the SSTP) that the legislature had a choice to write it’s legislation in a way to be compliant with both, instead of offensive to both, but chose not to in an attempt to expand the reach of it’s taxing authority.

To be consistent with both our state constitution and the SSTP, the legislation need only state that all vending machine sales, be they food or nonfood, shall be subject to the sales tax... but if a food, it can be taxed only if it meets the SSTP definition of being a “prepared” food.

Thank you in advance for your careful consideration.

Sincerely,


William E. Lobenherz, President

Cc: The Honorable Mark Meadows
Members, House Committee on Tax Policy
Brendan Ringlever, Tim Ward, Fritz Bensen
Michigan Legislative Consultants