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Sales Tax Exemption for Sweetened Dried Fruit (General Fund Taxes -- Sales and Use Taxes)

[LFB 2021-23 Budget Summary: Page 218, #4]

CURRENT LAW

Under current law, sales of food and food ingredients, except candy, soft drinks, dietary supplements, and prepared food, are exempt from the sales tax. Fruit is included in the definition of food and food ingredients. However, sales of dried or partially dried fruits are taxed as candy if the dried fruit contains sugar or natural or artificial sweetener. Candy is defined as a preparation of sugar, honey, or other natural or artificial sweetener combined with chocolate, fruit, nuts, or other ingredients or flavorings in the form of bars, drops, or pieces. Candy does not include a preparation that contains flour or that requires refrigeration.

Effective October 1, 2009, Wisconsin entered the Streamlined Sales and Use Tax Agreement (SSUTA), which requires some uniformity in tax administration among member states. The Agreement focuses on improving sales and use tax administration systems for all sellers and all types of commerce through uniformity of major tax base definitions and simplified administration of exemptions, among other provisions.

DISCUSSION POINTS

1. In the fall of 2020, the Wisconsin State Cranberry Growers Association contacted the Department of Revenue (DOR) about creating a sales tax exemption for sweetened dried cranberries. Cranberries are a naturally tart fruit that are typically sweetened with sugar or artificial sweeteners. As a result, dried cranberries that are sweetened are treated as candy for sales tax purposes, while comparable dried fruits, such as naturally sweet raisins, are exempt from the sales tax. The administration states that providing an exemption for dried cranberries and other sweetened dried fruits would serve to treat all dried fruits similarly for tax purposes.

2. As a member of SSUTA, Wisconsin is required to utilize common definitions for certain defined terms, such as food and candy. Member states must treat all items that fall under a certain defined term the same for sales and use tax purposes. Therefore, under Wisconsin's current law definition of candy, the state could not provide an exemption for sweetened dried fruit without also providing an exemption for all other candy. To address this, DOR filed a motion to SSUTA to amend the Agreement. This motion was approved and the Agreement was amended in December, 2020.

3. The amendment gives member states the choice of excluding sweetened dried fruit from the definition of candy. Specifically, member states now have the option of specifying that candy would not include a preparation that has as its predominant ingredient dried or partially dried fruit, along with one or more sweeteners, and which may also contain other additives, including oils, natural flavorings, fiber, or preservatives. Under this specification, dried or partially dried fruits prepared with the following would not be excluded from the definition of candy: (a) chocolate; (b) nuts; (c) yogurt; or (d) a confectionary coating or glazing. Additionally, dried or partially dried fruit would not include fruit that has been ground, crushed, grated, flaked, pureed, or jellied.

4. The Governor recommends providing a sales and use tax exemption for sweetened dried fruit, which is currently defined as candy and subject to tax. To accomplish this, the state could adopt the SSUTA exclusion to the definition of candy. The administration estimates that this exemption would decrease state tax revenues by $400,000 in 2021-22 and $500,000 in 2022-23 and annually thereafter.

5. Exemptions from the general sales and use tax narrow the tax base (which puts a greater burden on the purchasers of goods remaining taxable), impede economic efficiency, create inequities between types of businesses, and complicate administration and compliance of the tax. Sales and use tax theory generally recommends imposing the tax on a broad base to keep the sales tax at a low rate. For example, in 2019-20, Wisconsin collected $5.84 billion in sales and use tax revenue. In its 2021-23 Summary of Tax Exemption Devices publication, DOR estimates that the existing sales and use tax exemption for food and food ingredients, including bottled water, resulted in $705.7 million in foregone sales tax revenue in 2019-20. If the state had eliminated the exemption for these products, the sales and use tax rate could have been reduced from 5.0% to 4.5%, while still generating a similar amount of revenue in 2019-20.

6. On the other hand, when enacted in the context of a generally broad-based sales tax, exemptions can be used selectively to lessen the regressivity of the tax. The sales tax has generally been thought to be inherently regressive because the proportion of an individual's or family's income devoted to consumption declines as income increases. Persons at lower income levels, therefore, tend to pay a larger share of their income in sales tax.

7. A strong case can be made for an expansion of the exemption for food for home consumption. Because lower-income families typically consume a larger portion of their incomes on necessities such as food than middle- and higher- income families, the burden of a sales tax on food will fall more heavily on lower-income families. According to the Bureau of Labor Statistic's 2019 Consumer Expenditures report, consumers in the lowest income quintile spent an average of 23% of their income on food for home consumption, while consumers in the highest income quintile spent only 3.3% of their income on food for home consumption. If food is exempt from an otherwise general sales tax, the tax tends to become less regressive.

8. In general, dried cranberries are a good source of fiber and antioxidants, which can benefit an individual's immune system, metabolism, and heart. However, the drying of cranberries increases its make-up of carbs and sugar, compared to raw cranberries, even before any added sweeteners. Most dried cranberries contain added sweeteners as well. The Committee could consider whether the nutritional make-up of sweetened dried fruits, such as dried cranberries, are more comparable to other unsweetened dried fruits, or if they are more comparable to candy.

9. The Committee could provide a sales tax exemption for sweetened dried fruit (Alternative 1). This would provide consistent tax treatment for all dried fruit, regardless of whether they are sweetened or not. Alternatively, the Committee could choose not to expand the sales and use tax exemption for food to include sweetened dried fruit (Alternative 2).

ALTERNATIVES

1. Provide a sales and use tax exemption for sales of sweetened dried or partially dried fruit. Specify that candy does not include a preparation that has as its predominant ingredient dried or partially dried fruit along with one or more sweeteners, and which may also contain other additives, including oils, natural flavorings, fiber, or preservatives. Specify that a preparation that includes chocolate, nuts, yogurt, or a preparation that has a confectionary coating or glazing on the dried or partially dried fruit is candy. Specify that dried or partially dried fruit does not include fruit that has been ground, crushed, grated, flaked, pureed, or jellied. Specify that the provision takes effect on the first day of the third month beginning after publication of the bill. Estimate a reduction in state tax revenues of $400,000 in 2021-22 and $500,000 in 2022-23.

ALT 1	**Change to Base**
GPR-Tax	- $900,000

2. Take no action.

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