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The Retailer's Discount Costs Over $100 Million a Year

A Higher Road for a Better Tomorrow

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A CORPORATE WELFARE PROGRAM THAT ILLINOIS CANNOT AFFORD: THE RETAILER'S DISCOUNT COSTS OVER $100 MILLION A YEAR

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Executive Summary

The retailer's discount is a generous corporate welfare program that Illinois can no longer afford. At a time when Illinois' financial condition has required cutbacks to essential services, Illinois must find new ways to save funding or generate new revenue to protect taxpayers. Illinois should lower its retailer's discount to the 0.50 percent rate used in Wisconsin.

Illinois currently dishes out $142 million per year in subsides to retailers through its 1.75 percent retailer's discount rate. Illinois is also one of only 12 states that does not cap the amount of revenue a retailer can make per filing period. Illinois loses substantially more in revenue to retailers than its neighboring states, and the biggest beneficiary is the corporate giant, Walmart.

If Illinois lowered the retailer's discount to 0.50 percent of all sales taxes collected:

- the Illinois General Fund would add $102 million to help fix the budget deficit and fund essential public services;
- the Illinois economy would grow by an additional $25 million; and
- good, middle-class jobs would be saved or created in Illinois.

Opponents of this policy change claim that a high retailer's discount encourages retailers to open up stores in a state. However, economic data finds no evidence that more retail companies are located in the states with higher subsidies to retailers. There is also not a significant correlation between a higher retailer's tax discount and a larger retail sector in the economy. In fact, retailers are doing just as well in the 22 states that do not have a retailer's discount as they are in the states with high subsidies. Factors other than a tax discount provided to retailers are far more important in supporting a strong retail sector.

Illinois needs to fix the budget over the long term. Illinois simply cannot afford to continue providing a 1.75 percent subsidy to retailers on the sales taxes they collect. Lowering the retailer's discount to the 0.50 percent rate of neighboring Wisconsin would improve the budget by over $100 million per year, provide funding for essential public services, boost economic output by $25 million annually in the state, and have a negligible impact on retailers. Reducing the retailer's discount is a common sense way to help fix the budget in Illinois.

Introduction

In January 2017, Illinois may experience another budget impasse. Illinois now faces a potential operating deficit of $9 billion (Dye et al., 2015). According to estimates, Illinois' deficit could grow up to $12.8 billion by the end of Fiscal Year 2017 due to the backlog of unpaid bills. Meanwhile, revenue in Illinois' General Fund has declined substantially as the corporate income tax has fallen from 7.00 percent to 5.25 percent and as the individual income tax has declined from 5.00 percent to 3.75 percent.

Illinois needs to fix its long-term budget outlook. Given Illinois' current financial condition, the state cannot afford to willingly surrender tax revenue. In a time of cutbacks to essential services and likely tax increases, the state has continued a "generous reimbursement to retailers" through a program called the "retailer's discount" (The Civic Federation, 2016).

Over half of all U.S. states allow retailers to keep a portion of the sales taxes they collect from shoppers through a retailer's discount, also known as a vendor discount. Shoppers do not submit sales tax payments to the state or a local government when they purchase a taxed good. Instead, sales taxes are collected by retailers at the time of the transaction and are later submitted to state and local revenue departments. Illinois is one of 28 states that compensate companies for the cost of collecting sales taxes and reporting their payments in a timely manner (The Civic Federation, 2016).

Reducing the retailer's discount is one possible way to raise needed revenue for Illinois. Illinois has a 1.75 percent retailer's tax discount – meaning that retailers get to keep 1.75 percent of all sales taxes they collect from consumers. Currently, the 1.75 percent discount costs Illinois taxpayers approximately $142 million every year.

Retailer's Discounts across the United States

Retail companies in 28 states are able to keep a portion of the sales taxes they collect on behalf of state and local governments through a retailer's discount. In these states, sales tax revenues that would otherwise go to the government to pay for services (or balance the budget) are given to retailers. The policy is effectively a redistribution of tax revenues from the government to retail businesses. Cumulatively, over $1 billion is state tax revenue is lost every year through retailer's discounts across the nation. Walmart alone is provided $70 million in corporate subsidies every year through retailer's tax discounts (Mattera & McIlvaine, 2008).

Retailers argue that these discounts encourage businesses to open up stores in a particular state. Retailers also claim that they should be compensated for collecting sales taxes for the government because of the administrative costs and transaction costs from credit and debit cards. These were practical arguments decades ago when most retailers maintained handwritten records, a labor-intensive process that was costly. Today, however, the process is automated for nearly all retailers. While retail companies should still receive compensation for their service, the tax discount should be limited.

Some states limit the amount that a company can keep by passing laws to "cap" the service fee. A total of 16 states place a cap or ceiling on how much a retailer can receive each filing period. A total of 12 state do not have a cap on how much revenue an individual store or chain can be compensated every filing period (Figure 1). Depending on the state, the filing period can be monthly, quarterly, or per year.

Retailer's discount rates range from as low as 0.25 percent to as high as 5.00 percent in the states that provide compensation (Figure 1). New York has the highest tax subsidy, with a rate of 5.00 percent. However, New York also has a ceiling of $200 per quarter when filing sales tax collections. This limits the amount of revenue a large corporation can make off of the retailer's discount, but still provides the retail companies with appropriate compensation. On the other hand, Colorado provides a 3.33 percent discount rate and does not cap the amount that retailers can receive per filing period. It is worth noting that Texas, a state with the same state sales tax rate as Illinois, has a lower retailer's discount rate (0.50 percent) than Illinois (1.75 percent).

Figure 1: Retailer's Discount Rates by State, Ceiling vs. No Ceiling, 2016

With a Subsidy Ceiling	
State	**Rate**
NY	5.00%
AL	2.0%-5.0%
SC	2.0%-3.0%
FL	2.50%
NE	2.50%
AR	2.00%
MS	2.00%
WY	1.0%-1.95%
KY	1.5%-1.75%
ND	1.50%
SD	1.50%
MD	0.9%-1.2%
AZ	1.00%
OK	1.00%
MI	0.50%
WI	**0.50%**

Without a Subsidy Ceiling	
State	**Rate**
CO	3.33%
GA	0.5%-3.0%
MO	2.00%
IL	**1.75%**
VA	0.8%-1.6%
UT	1.31%
PA	1.00%
LA	0.94%
OH	0.75%
IN	0.73%
TX	**0.50%**
NV	0.25%

Source: "State Sales Tax Rates and Vendor Discounts" by Federation of Tax Administrators

The Retailer's Discount in Illinois

Illinois has an uncapped retailer's discount rate of 1.75 percent, the 3rd-highest subsidy to retails of the 12 states without a ceiling (Civic Federation, 2016). This means that retailers get to keep 1.75 percent of all state sales taxes they collect. For example, consider an Illinois family that purchases a used car for $10,000. The family pays an additional 6.25 percent in state sales taxes, or $625. The car dealership gets to keep 1.75 percent of that $625 as a subsidy from the state government, or about

$11. This government subsidy adds up for large dealerships with thousands of these transactions in a year.

The corporation receiving the largest retailer's discount subsidy from Illinois taxpayers is Walmart. Walmart accounts for 7 percent of all retailer's discount subsidies in Illinois. In 2008, Walmart collected $476.1 million in sales taxes for Illinois and received about $8.5 million in additional compensation through the program (Mattera & McIlvaine, 2008). Redistributing taxpayer dollars from the General Fund to the largest corporation in the world is essentially the definition of corporate welfare.

Illinois can no longer afford its high retailer's discount rate. Illinois forfeits the most revenue to retailers of any state. In 2008, Good Jobs First estimated that Illinois had an annual revenue loss of $126.1 million due to the 1.75 percent retailer's tax discount. Texas was the second highest state in annual revenue loss to the compensation fee with $89.6 million, approximately $36.5 million less than Illinois. Among the states with a ceiling on the amount a retailer can collect, Florida lost the most revenue, at $65.2 million annually from a 2.50 percent subsidy. Thus, Florida only lost half the amount of Illinois (Mattera & McIlvaine, 2008).

Illinois' retailer's discount rate is higher than most of its neighboring states. Indiana (0.73 percent), Kentucky (1.50-1.75 percent), and Wisconsin (0.50 percent) all have lower rates than Illinois. Iowa and Minnesota have no retailer's tax discount. Only Missouri is higher than Illinois, at 2.00 percent. Even though Missouri's retailer's tax discount rate is higher than Illinois, Illinois still loses more revenue annually to retailers than Missouri (Mattera & McIlvaine, 2008).

Compared to the rest of the country, Illinois' retailer's discount rate is excessive. To boost revenue and eliminate corporate welfare, Illinois should adopt a 0.50 percent retailer's tax discount as in Wisconsin. Wisconsin has provided a retailer's discount of 0.50 percent of the amount of tax liability if taxes are paid in a timely manner since 1993. Wisconsin has a minimum filing rate per time of $10 and a maximum ceiling rate of $1,000 per filing period, meaning retailers can only receive compensation of $10 to $1,000 per filing period. Illinois could save tens of millions of dollars by adopting Wisconsin's rates.

The State of Illinois needs to cut unnecessary spending and compensation programs to save revenue for the growing deficit. Figure 2 shows the current retailer's tax discount rate and other possible discount rates for retailers. The Illinois Economic Policy Institute estimates that Illinois now loses approximately $142 million due to the current rate of the retailer's discount. This estimate is based on 1.75 percent of total sales tax revenue in Illinois (IDOR, 2016).

If Illinois lowered its retailer's discount to Wisconsin's rate of 0.50 percent, revenue in the state's General Fund would increase by an additional $102 million per year (Figure 2). This estimate assumes that Illinois' retailer's discount would remain uncapped. In addition, Texas, a state with the same state sales tax rate as Illinois, and the neighboring state of Michigan both have a retailer's subsidy of 0.50 percent.

Figure 2 also includes alternative savings estimates from adjusting the retailer's discount. If Illinois reduced the rate to 1.00 percent– closer to Indiana's 0.73 percent rate and equivalent to the 1.00

percent rate in Pennsylvania– the state would hand out $61 million less in corporate subsidies every year. Of course, joining the 22 states that have eliminated the retailer's discount altogether would improve the state's budget deficit by $142.2 million per year.

Figure 2: Cost of Retailer's Discount in Illinois, Current Rate vs. Proposed Rates

Retailer's Tax Discount		
Rate	**Subsidy Cost**	**Tax Savings**
1.75%	$142,157,225	$0.00
1.00%	$81,232,700	$60,924,525
0.50%	**$40,616,350**	**$101,540,875**
0.00%	$0.00	$142,157,225

Source: Authors' analysis of IDOR (2016) using methods from Mattera & McIlvaine (2008).

The Economic Impact Retailer's Discount in Illinois

This section utilizes the IMPLAN (IMpact analysis for PLANning) software to measure the impact of an additional $100 million in Illinois' General Fund from reducing the retailer's discount from 1.75 percent to 0.50 percent. IMPLAN is an input-output software that estimates the ripple effect, or multiplier, of changes in industry spending or household expenditures. The input-output model investigates inter-industry relationships in an economy based on Census data, specifically measuring market transactions between industries and consumers. IMPLAN is considered the "gold standard" for economic impact modeling (Vowels, 2012).

The economic impact analysis finds that economic activity in Illinois would increase by $25 million if the state decreased the retailer's discount rate to 0.50 percent (Figure 3). The additional revenue in the General Fund due to reducing the retailer's discount to Wisconsin's rate would allow Illinois to maintain $100 million in public services, rather than cutting programs. The $100 million subsidy to retailers currently results in a $122.7 million impact on the state economy. However, reducing the subsidy and ensuring taxpayer dollars fund public programs rather than private businesses, would boost Illinois' GDP by $148.0 million, a net gain of over $25 million. In addition, the jobs that are created or saved by the limiting this form of corporate welfare all pay over twice as much on average ($55,035 per year) as the jobs that are created or saved by subsidizing retailers ($25,210 per year). Reducing the retailer's discount would help fix the budget, provide essential services to those in need, and grow Illinois' economy.

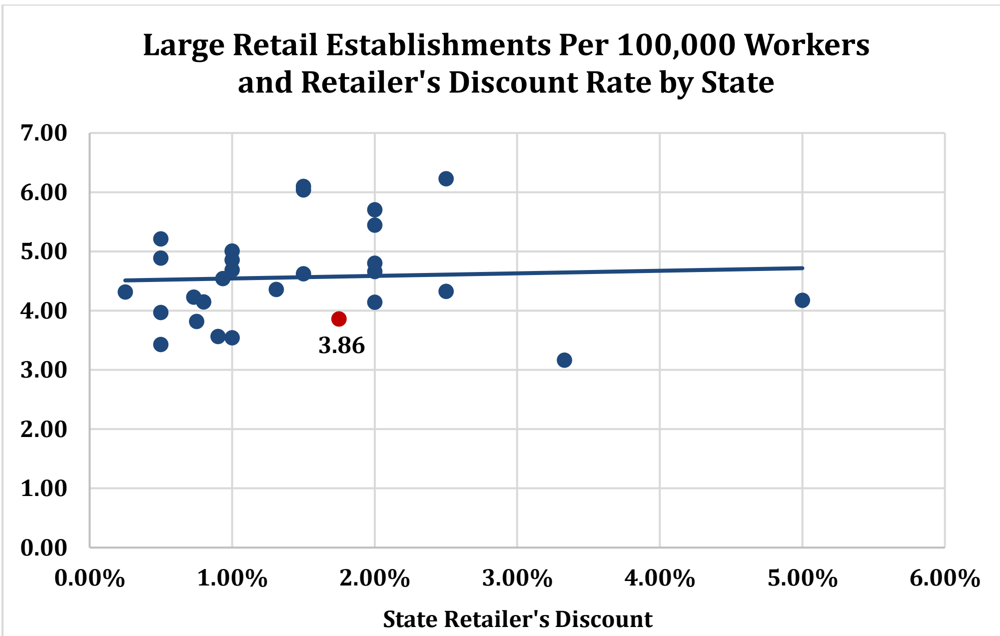
Figure 3: The Economic Impact of Reducing the Retailer's Discount in Illinois to 0.50 Percent

Economic Impact Analysis (IMPLAN Data)	Impact on Illinois' GDP (Value Added)	Annual Compensation (Per Employee)
Retail Sector	$122,667,342	$25,210
Government Sector	$148,039,371	$55,035
Net Impact	**+$25,372,031**	**+$29,825**

Source: IMPLAN (2015)

Opponents of reducing the retailer's tax may argue that this policy change would result in retailers leaving the state. However, actual economic data reveals that large retail establishments are no more likely to be located in states that have high retailer's tax discounts. Figure 4 shows an insignificant correlation between the retailer's discount rate in a state and the number of large retail stores per 100,000 workers (whose earnings translate into consumer spending at retail stores) in the state. Claims that retailers would suffer and not locate in Illinois if the state were to lower its retailer's discount rate to 0.50 percent are not supported by Figure 4.

Figure 4: Large Retail Establishments per 100,000 Workers in States with Subsidies

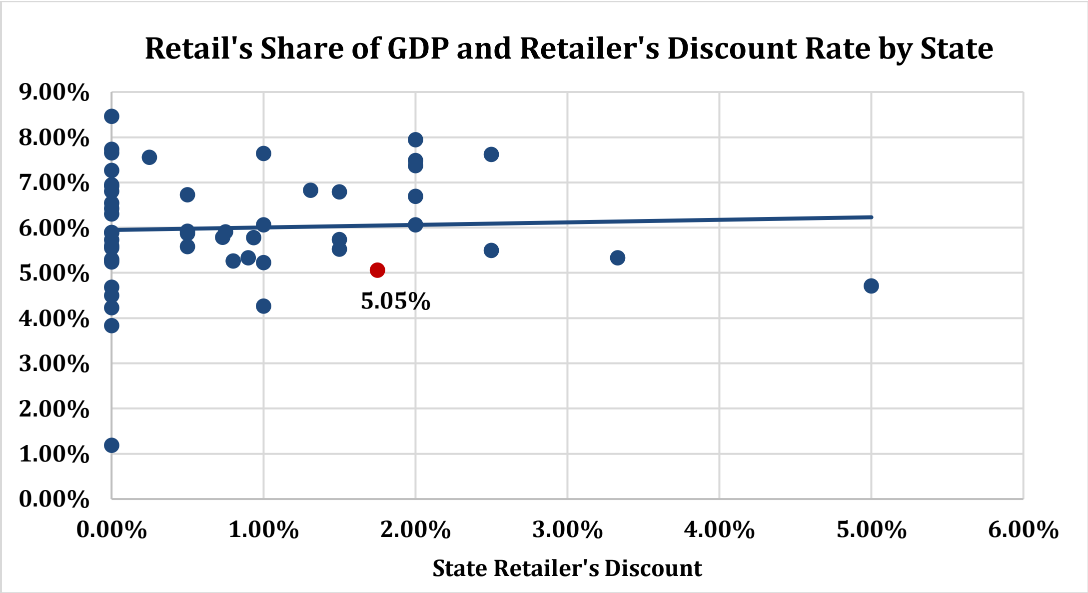


Source: "2014 Business Patterns" by the U.S. Census Bureau (2016) and "State Sales Tax Rates and Vendor Discounts" by Federation of Tax Administrators (2016)

Similarly, Figure 5 shows that there is no significant correlation between the retailer's discount rate in a state and retail's share of a state economy. The retail industry currently accounts for 5.05 percent of the Illinois economy. Figure 5 finds that states with higher retailer's subsidies do not have larger retail sectors. Figure 5 also includes states without a retailer's discount; there is wide variation in the size of the retail sector even in these states with an effective retailer's discount of 0.00 percent.

Ultimately, there is no significant correlation between the retailer's tax discount rate and the success of retailers in a state. A state's retail sector is not impacted by the tax discount provided to retailers. Others factors are far more important, such as high average wages that result in strong consumer demand. Ultimately, Illinois could reduce its discount rate to 0.50 percent to help fix the budget and limit a form of corporate welfare.

Figure 5: Retail's Share of the Economy and Retailer's Discount Rate, All States



Source(s): "Regional Data - GDP & Personal Income" by Bureau of Economic Analysis (2015) and "State Sales Tax Rates and Vendor Discounts" by Federation of Tax Administrators (2016)

Conclusion

The retailer's discount is a generous corporate welfare program that Illinois can no longer afford. At a time when Illinois' financial condition has required cutbacks to essential services, Illinois must find new ways to save funding or generate new revenue to protect taxpayers. Illinois should lower its retailer's discount to the 0.50 percent rate used in Wisconsin.

Illinois currently dishes out $142 million per year in subsides to retailers through its 1.75 percent retailer's discount rate. Illinois is also one of only 12 states that does not cap the amount of revenue a retailer can make per filing period. Illinois loses substantially more in revenue to retailers than its neighboring states, and the biggest beneficiary is the corporate giant, Walmart.

Illinois would improve the budget by $102 million if the retailer's discount was lowered to 0.50 percent. This additional revenue in the General Fund would help fix the budget deficit and fund essential public services. Furthermore, Illinois' economy would grow by an additional $25 million by reducing the retailer's tax to 0.50 percent.

Opponents of this policy change claim that a high retailer's discount encourages retailers to open up stores in a state. However, economic data finds no evidence that more retail companies are located in the states with higher subsidies to retailers. There is also not a significant correlation between a higher retailer's tax discount and a larger retail sector in the economy. In fact, retailers are doing just as well in the 22 states that do not have a retailer's discount as they are in the states with high subsidies. Factors other than a tax discount provided to retailers are far more important in supporting a strong retail sector.

Illinois simply cannot afford to continue providing a 1.75 percent subsidy to retailers on the sales taxes they collect. Lowering the retailer's discount to the 0.50 percent rate of neighboring Wisconsin would improve the budget by over $100 million per year, provide funding for essential public services, boost economic output by $25 million annually in the state, and have a negligible impact on retailers. Reducing the retailer's discount is a common sense way to help fix the budget in Illinois.

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