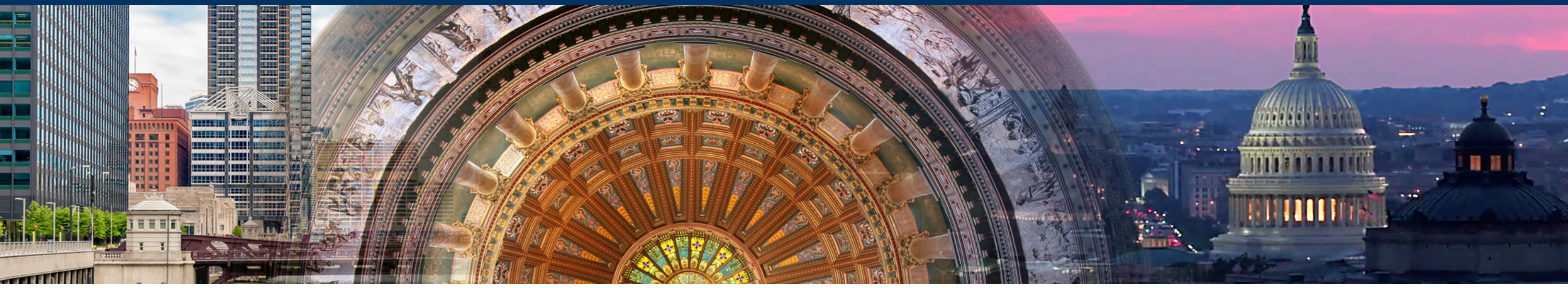

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Should Illinois Eliminate the State Grocery Tax?

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The state of Illinois imposes a "Retailer's Occupation Tax" (ROT), or sales tax, of 6.25% on general merchandise and 1% on qualifying food, drugs, and medical appliances.[1] The 1% tax is charged on most food items for home consumption, or "food at home" (FAH) and is often referred to as a "grocery tax." The state grocery tax plays a role in local government finance because a portion of state receipts are passed through to municipalities. Illinois is among 13 states that impose a grocery tax (Figueroa & Legendre, 2020).[2]

Grocery taxes are a controversial way to raise revenue. Because low-income households spend a much higher share of their income on food than better-off households, the concern is that the grocery tax may be regressive, so that low-income households end up paying more than their "fair share" of taxes. A tax on FAH may also encourage consumer substitution into less nutritious food away from home (FAFH). Because of this, the grocery tax could have an adverse impact on lower-income households' health.

Under current law, one percentage point of the state's 6.25% ROT (or 16% of state ROT collections) is passed through to municipal governments.[3] Elimination of the grocery tax would lower ROT revenue by reducing the taxable base of retail sales.[4] In 2022 Gov. Pritzker and the General Assembly agreed to suspend the grocery tax for state fiscal year (SFY) 2023 (P.A. 102-0700). From July 1, 2022 through June 30, 2023, items formerly subject to the 1% tax rate (with the exception of medicines and drugs) were not subject to the state tax.[5] It is important to note that the elimination of the grocery tax only eliminates the portion of ROT revenue that is generated by grocery sales. The state still passes through a 1% ROT collected on non-grocery items. This means that the elimination of the grocery tax has a fairly small revenue impact relative to all ROT that is passed through to local governments.

[1] A detailed description of Illinois sales taxes can be found at https://perma.cc/X3J8-MG4D.
[2] The other states with grocery taxes are Arkansas (0.125%), Missouri (1.23%), Virginia (2.5%), Utah (3.0%), Alabama (4.0%), Hawaii (4.0%), Tennessee (4.0%), Oklahoma (4.5%), South Dakota (4.5%), Idaho (6.1%), Kansas (6.5%) and Mississippi (7.0%). Hawaii, Oklahoma, Idaho, and Kansas have a state tax credit to partly offset the cost of the tax for low-income households (Figuero & Legendre, 2020).
[3] For more details on how the state ROT is distributed, see https://perma.cc/6QG6-7QMG.
[4] Items such as alcoholic beverages, soft drinks, and prepared food for immediate consumption would continue to be taxed at the 6.25% rate (see https://perma.cc/Y7MH-L2F7).
[5] Further details on the SFY 2023 suspension are available at https://perma.cc/U8JV-B8AT.

The state estimated a revenue reduction of $360 million due to the elimination of the grocery tax in SFY 2023 (Gourdie, 2024), and local governments were reimbursed for their losses.[6]

The state grocery tax went back into effect on July 1, 2023. In his 2025 budget, Gov. Pritzker seeks to permanently eliminate the tax on July 1, 2024, without offering local governments any compensating revenue stream.

> **In announcing his proposal, Governor Pritzker argued that**
>
> **"It's one more regressive tax we just don't need. If it reduces inflation for families from 4% to 3%, even if it only puts a few hundred bucks back in families' pockets, it's the right thing to do (Inklebarger, 2024)."**

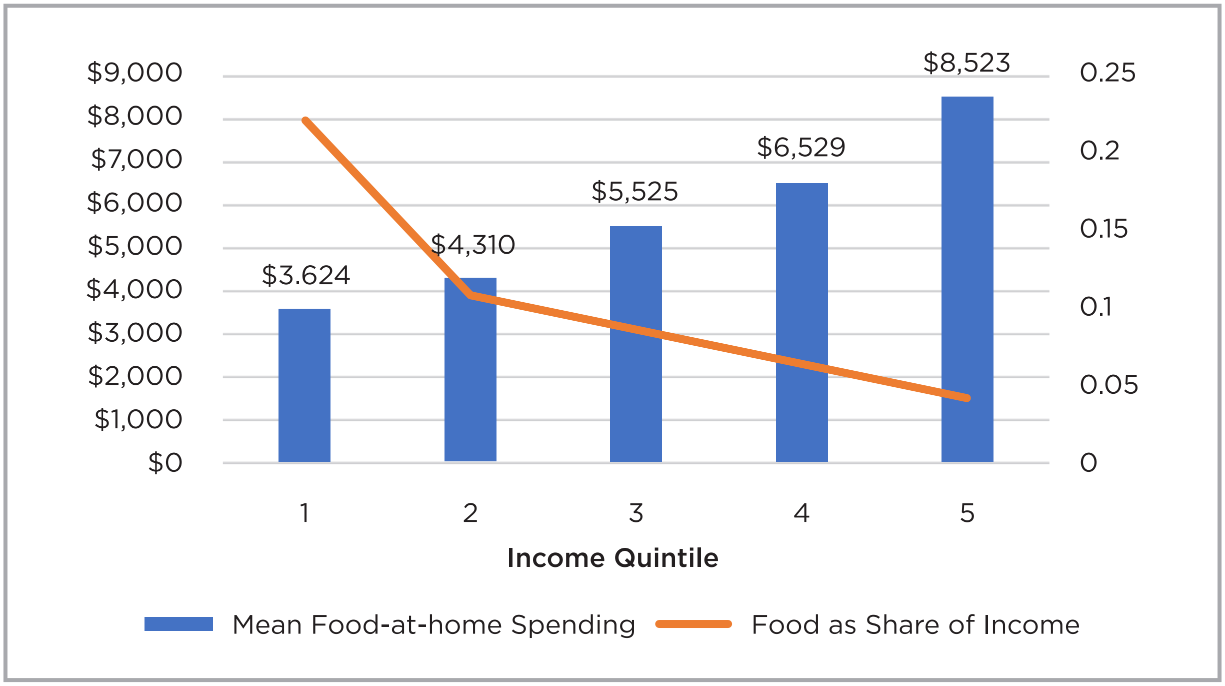
This brief argues that the implications of eliminating the grocery tax are not so clear-cut. I consider the extent to which eliminating the grocery tax would reduce household expenses, reduce tax regressivity, and encourage healthy diets. That analysis is followed by a discussion of the impact on municipal revenue and possible responses.

OVERVIEW OF FISCAL BALANCE

Because the state grocery tax is just 1%, a family would have to spend at least $30,000 on FAH grocery items to obtain the "few hundred bucks" in savings mentioned by the Governor in the course of one year. **Figure 1** shows that average annual expenditures on FAH for 2022 (the latest available year) in the U.S. ranged from $3,624 for the lowest-income households to $8,523 for the highest-income households.[7] It would take a low-income family over 8 years to accumulate several hundred dollars in tax savings from the elimination of the grocery tax. The state grocery tax liability of higher-income households would go down the most due to their higher FAH spending, but even the highest quintile households would need more than 3 years to accrue several hundred dollars in savings.

Figure 1. Food at Home Expenditures and Food at Home Expenditures as a Share of Household Income

Notes: Data from Bureau of Labor Statistics Table 1101 available at https://www.bls.gov/cex/tables/calendar-year/mean-item-share-average-standard-error/cu-income-quintiles-before-taxes-2022.pdf.



[6] It is notable that in FY 2023, SNAP benefits were still enhanced due to COVID. Because SNAP purchases are not subject to tax, the revenue losses from foregoing the tax at that time were lower than they would be now that COVID provisions have expired.
[7] Arraying households from lowest to highest income, the first quintile selects the 20% of households with the lowest income, the second quintile the next 20% of households by income, and so on. The blue bars correspond to the axis on the left, while the line corresponds to the axis on the right.

IS THE GROCERY TAX REGRESSIVE?

A tax is regressive when the amount paid is higher relative to income for lower than higher income families. **Figure 1** shows that the share of FAH expenditures in income are declining as income rises. Families in the lowest 20% of the income distribution spent 22.2% of their income on FAH in 2022. This share is cut in half at the second quintile (to 11.0%) and is below 5% of after-tax income for the wealthiest families.

Table 1: Mean Income and Food Expenditures by Income Quintile, 2022

Income Quintile Lower Limit	Mean Income	FAH Expenditures[8]	FAH expenditures as a Share of Income
$0	$14,191	$3,624	0.22
$25,807	$37,441	$4,310	0.11
$50,092	$65,659	$5,525	0.09
$83,696	$108,730	$6,529	0.07
$140,363	$244,025	$8,523	0.04

Note: Data from Bureau of Labor Statistics Table 1101 available at https://www.bls.gov/cex/tables/calendar-year/mean-item-share-average-standard-error/cu-income-quintiles-before-taxes-2022.pdf.

Viewed in isolation, the spending patterns shown in **Figure 1** and **Table 1** suggest that Illinois' grocery tax is inherently regressive. But the important issue is not whether FAH expenditures are regressive but whether grocery tax payments are. The major means-tested federal nutrition program, the Supplemental Nutrition Assistance Program (SNAP), supports low income households' FAH purchases. Because SNAP-funded purchases are not subject to tax, SNAP is a key determinant of who bears the grocery tax. As a means-tested program, SNAP benefits are distributed disproportionately to lower income households, relieving many of them of the grocery tax burden. Therefore, to assess regressivity of the grocery tax, we must consider how much of FAH is financed by SNAP.

Table 2 presents details of the calculations to determine after-SNAP regressivity of the grocery tax. Information on the distribution of SNAP benefits (the amount of FAH not subject to grocery tax) by income quintile is available for the entire U.S. for 2014 and is shown in column 2 of **Table 2**.[9] Column 3 repeats average FAH spending from Table 1 for convenience. The SNAP benefit shares to each quintile in column 2 are multiplied by total SNAP spending in Illinois for 2022 and divided by one-quarter of the number of households in Illinois to arrive at average SNAP-funded FAH purchases by quintile (column 4). Average taxable FAH spending is equal to average FAH spending less average SNAP-funded FAH purchases (column 5). Applying the grocery tax rate of 1% to taxable FAH spending yields the average amount of grocery tax paid in a year (column 6). The final column presents the average grocery tax divided by average income in each quintile.

Accounting for SNAP payments reduces the incidence of the grocery tax on the bottom quintile to 0.01%. The incidences are higher for the other quintiles, so the tax is not regressive with respect to the bottom of the income distribution (lowest quintile). However, the tax is regressive from the point of view of quintiles 2 and 3, because the income share declines from

[8] *Consumer Expenditures in 2022*. BLS Report 1107. Shane Meyers, Geoffrey D. Paulin, & Kristen Thiel. December 2023. https://perma.cc/3DFF-Q6WJ.
[9] This information from the Congressional Budget Office is reported in Reeves & Pulliam (2018). I assume that the U.S. and Illinois distributions of SNAP benefits over quintiles are similar, and that these distributions have not changed much in the past decade.

quintiles 2 and 3 through quintile 5. Therefore, accounting for SNAP considerably reduces, but does not eliminate, grocery tax regressivity.[10,11]

Table 2: Incidence of the Grocery Tax After SNAP Benefits

Quintile of Income	Share of SNAP Payments	Average FAH Expenditures	Average FAH Purchased with SNAP	Taxable FAH Spending	Average Grocery Tax	Tax as Share of Income
1	63.2	$3,624	$3,459.92	$164.08	$1.64	0.01%
2	24.6	$4,310	$1,346.74	$2,963.26	$29.63	0.08%
3	7.4	$5,525	$405.12	$5,119.88	$51.20	0.08%
4	1.1	$6,529	$60.22	$6,468.78	$64.69	0.06%
5	0	$8,523	$ -	$8,523.00	$85.23	0.04%

Notes: Data from Bureau of Labor Statistics Table 1101 available at https://www.bls.gov/cex/tables/calendar-year/mean-item-share-average-standard-error/cu-income-quintiles-before-taxes-2022.pdf. The distribution of SNAP benefits is from the Congressional Budget Office as reported in Reeves and Pulliam (2018).

WOULD ELIMINATING THE GROCERY TAX IMPROVE NUTRITION?

Foods subject to the 1% grocery tax are generally more nutritious than other items in grocery stores (like soft drinks and candy) subject to the 6.25% rate as well as FAFH. By lowering the relative cost of healthy foods, eliminating the grocery tax may tilt consumption away from restaurant and junk food.

A USDA study provides evidence on this point (Dong & Stewart, 2021). The findings confirm that, consistent with the exemption of SNAP purchases from taxation, grocery taxes do not seem to impact the balance between FAH and FAFH consumption of SNAP-receiving households. Households with similar but somewhat higher incomes than SNAP recipients were found to increase their FAH spending very modestly when grocery taxes were lower. These findings reinforce the conclusion that benefits of eliminating the grocery tax are concentrated on households that are low, but not lowest, income.

IMPLICATIONS OF REMOVING THE GROCERY TAX FOR MUNICIPAL BUDGETS

> **"If [municipalities] want to impose a grocery tax on their local residents, they should be able to go do that," [Governor Pritzker] said. "I don't think it's the right thing to do, I wouldn't do it locally. Having said that, I understand the need for the dollar, and if they feel like they need them they should think about imposing that tax on their own (Vinicky, 2024)."**

In FY 2022, the state collected $14.7B in total from the ROT applied to all taxable products (Mendoza, 2022). Of this amount, $2.35B (16%), passed through to municipal governments. As noted, the state reported that the grocery tax suspension of 2022 reduced state payments to municipalities by $360 million (Gourdie, 2024).[12]

[10] The regressivity analysis relies on quintile averages. Within each quintile, there is a range of grocery tax payments, so not every household pays the same average grocery tax. For example, there are individual households in the first quintile who do not receive SNAP, and so pay a higher-than-quintile-average grocery tax.
[11] Illinois has extremely high SNAP participation eligible households. Between 95% and 100% of eligible individuals participated in SNAP in Illinois in 2018, including 92% of eligible workers (see https://perma.cc/3DFF-Q6WJ). This implies that the incidence of the grocery tax could not be changed much through further efforts to recruit households to SNAP.
[10] The base of the state grocery tax would be larger in SFY 2025 under the grocery tax because SNAP enhancements expired in March 2023. Therefore the loss from suspending the tax in SFY 2025 is likely higher than $360 million.

For municipalities, passing their own grocery tax is not a light lift. For one, politics may be a hindrance. Will the typical taxpayer understand that the 1% restoration of the grocery tax by a municipality is not a "new" tax? Many municipalities already impose sales taxes; an existing municipality grocery sales tax could be perceived as high to begin with, and taxpayers may frame an additional 1% tax increment as excessive in that context, even though it simply replaces the lost state tax.

The goal of ending the state grocery tax on July 1, 2024 does not appear to leave municipalities time to pass a "replacement" local sales tax until some of the next fiscal year has passed. Home-rule municipalities can levy a new sales tax rate as an ordinance, but this had to be accomplished by April 1, 2024 if a local grocery tax was to take effect on July 1, 2024. Non-home rule municipalities would need to mount a voter referendum by May 1, 2024 for a July 1, 2024 start (Illinois Municipal League, 2021). An ordinance or referendum result by October 1, 2024 would put the new municipal sales tax into effect mid-fiscal year. That means that if the state did repeal the grocery tax by July 1, 2024, even local governments moving expeditiously to institute a local grocery tax would lose half of SFY 2025's potential revenue. Exactly how this plays out will depend on when (and whether) the state passes a law to repeal the grocery tax.

If the state chooses to eliminate the grocery tax without providing any compensating funds, and if municipalities are reluctant to impose an additional 1% grocery tax locally, they will need to turn to other sources of revenue or reduce expenditures. One possibility is to further raise the sales taxes on regular retail items to make up for the elimination of groceries from the sales tax base. However, because lower-income households buy other retail goods that cannot be purchased with SNAP benefits, and expenditures on these goods are comparatively high, this option is more regressive than the grocery tax. Property taxes–municipal governments' other major option for raising revenue—are widely regarded as regressive (Institute on Taxation and Economic Policy, 2024). The state argues that by increasing pass-throughs from state income taxes to municipalities, it has already begun to ameliorate the impact of the grocery tax elimination. Since the Illinois income tax is modestly progressive, this may be a good solution. However, the SFY 2025 budget does not include an increase in state allocations of the income tax to municipalities to make up for the loss of state grocery tax revenue.

CONCLUSION

Grocery taxes are controversial. While not as regressive as is often portrayed because SNAP receipt exempts most of the FAH purchases of the lowest-income households from the tax, the grocery tax is regressive from the point of view of households in the lower-middle and middle of the income distribution. There is also some evidence that lower-income households not on SNAP shift their food consumption a little from FAFH into FAH when grocery taxes fall. Overall, this suggests that there are some benefits to eliminating the grocery tax for low and middle income households. However, given realistic levels of FAH expenditures, Illinois' low grocery tax rate, and very small effects of taxing groceries on food consumption, the impact of Illinois' grocery tax on any group of households is likely to be quite small.

While the savings to an individual household of lifting the grocery tax is very modest, the loss of tax revenue to municipalities is consequential, and the timetable caused by eliminating the tax on July 1, 2024 may lead to delays in implementing a local replacement. If municipalities do not cut spending, state increases in the amount of income tax that is passed on to municipalities may make up for lost revenue without increasing reliance on regressive taxes.

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