

American Economics Group, Inc.

Study of Visitor-Related Local Tax Options: A Menu for Durham, NC

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City of Durham

County of Durham

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I. Executive Summary

American Economics Group, Inc. (AEG) was asked to investigate the suitability of various visitor-related taxes as a means to fund local government services including the extent to which any revenues should be earmarked for visitor promotion and marketing to protect and fuel these revenue sources.. The quandary of imposing greater taxes is that higher prices of lodging, meals, car rentals, admissions or gasoline, etc. will reduce sales of those goods and services. However, if the tax proceeds are put to good use, they may actually increase demand and more than offset their economic burden.

One example of a sound tax policy that increases economic activity is an earmarked lodging tax used to promote visitors, conventions, business meetings and overall tourism. If applied at reasonable rates and used effectively to augment visitor traffic, the natural tendency of higher prices (including taxes) to reduce sales may be overcome by shifting demand for a local area to a higher position among its competitors.

This study addresses the following questions: 1) Which new or higher visitor-related taxes are suitable to help fund local government services and lessen over reliance on property taxes? 2) How much will these new taxes generate in revenue? 3) What is their effect on the existing travel to Durham? 4) How much will they affect business and jobs in the community? 4) To what degree will their burden fall on lower income resident households?

It is often difficult to imagine that a small change in a tax will affect behavior in a significant way. However, it is seen over and over again that people adjust their behavior in response to tax changes. Even small changes will affect some economic decisions, and it is important to gauge their impact before imposing them. This analysis does that, and focuses on the incremental effect of each tax.

AEG has examined a wide range of taxes for their suitability as a visitor-related local option tax menu in Durham County.

- There are many possible visitor-related taxes and fees that might be considered to help fund local government services and fund CVB promotional activities that protect and fuel the revenue streams and offset the impact on the businesses shouldering these taxes. Some are already levied by North Carolina, by Durham County, by The City of Durham, or by other jurisdictions in the area. Other taxes would be new to the area or feature new components.
- Based upon our review, we selected taxes that have a logical connection with travel and visitors, have a sufficiently large base to raise several million dollars at reasonable tax rates, and have a collection history in other places across the country.

We examined each of the following taxes under the assumption that one or more of them would be increased from their current levels and/or redesigned to alter the impacts:

- A tax on purchase of prepared food and beverages by-the-drink (restaurant meals tax)
- An occupancy tax on hotels, motels and other transient lodging
- An airport/airline tax based on passenger enplanements
- A gasoline tax on purchases for on-road vehicles
- A motor vehicle rental tax
- An admissions tax on amusements, entertainment and sports events

Increased taxes can cause a noticeable reduction in economic activity in general, reduce revenue for specific businesses, and even lower the collection of other taxes.

- Even taxes imposed at reasonable and competitive rates will tend to reduce future growth. At excessive rates they may cause an absolute decline in economic activity.
- Durham can overcome the effect of the tax by increasing its spending on visitor promotional and marketing activities. Earmarking a portion of visitor-related taxes to CVB promotional activities can offset the decline by increasing the demand for Durham as a destination for visitors, conventions, meetings, and tourism.
- Promotions can target both overnight visitors and regional traffic that includes a large component of day trip visitors. It will also be productive to broadening the burden for promotion from just the occupancy tax (now paid by 20% of all travelers) to include businesses serving day trip visitors.

The recent increase in the combined tax on lodging from 11% to 13% is causing a decline in room night sales, which can be overcome by greater CVB promotional activity

- Overnight visitors to Durham now face a tax of 13% for lodging, 7% for meals, 7% for retail and entertainment and 25.6% for vehicle rentals.
- Currently, Durham's 13% lodging tax is reducing taxable lodging revenue from overnight visitors by about \$7.0 million and room nights by 95,033. This includes the impact of the recent tax increase of 1%, which reduced lodging revenue by \$540,000 and room night sales by 7,310.
- By 2008, this loss will grow unless additional CVB promotion increases the demand for Durham rooms. In that year, the 13% hotel tax is expected to reduce room revenues by almost \$10.7 million and to reduce room nights sold by 127,249.

Increased taxes on visitors are only partly borne by the visitors and exported out of the county. Contrary to popular belief, much of the burden of these taxes falls upon Durham businesses, workers and their families.

- Although out-of-town visitors purchase most of the lodging and much of the vehicle rental services in Durham County, it is wrong to assume that the tax burden falls exclusively on them.
- Actually, much of the tax burden falls on the County's lodging, restaurants and vehicle rental industries, their workers and their suppliers, as well as other businesses that benefit from the spending by those same workers and suppliers.

This study does not examine the legal authority to impose these additional taxes

- This analysis is done solely from an economics perspective. Taxes are examined without consideration of the legal authority to impose them, the political will to do so, or the arrangements with neighboring jurisdictions that may be needed.
- Some new taxes or increases may be undertaken locally without additional authority. However, many will require state-level legislation to impose them directly or to authorize local statutes levying them.
- In the case of the airport passenger enplanement tax and perhaps the motor vehicle rental tax, the location of the airport in neighboring Wake County may require a joint undertaking and an appropriate agreement on how to advance the authority and split the tax proceeds.

The following variations in each tax were considered

- The tax on restaurant meals is calculated at alternative tax rates of 1%, 2% and 3% on a tax base that alternatively includes all sales at eating and drinking places, and then limits the tax to sales greater than \$10, \$15 and \$30 per customer.

- As a proxy for many possible approaches to taxing airlines and/or air passengers we used a head tax on persons enplaning at Raleigh-Durham International Airport (RDU). This includes those beginning their travel at RDU and those embarking on their return trip from RDU. The revenue estimates are based upon a split between Wake County and Durham County according to relative population. Other formulas to divide the tax proceeds are possible.
- We measured the potential revenue from increased gasoline taxes, but ultimately dropped that tax from consideration because it would unduly weigh on lower income commuters and presents a high political liability.
- Admission and amusement taxes offer a large number of variations. We calculated the potential revenue from sports events, movies, other entertainment and amusements.
- We deemed an increased motor vehicle rental tax as unreasonable because the existing rate is already among the highest in the nation. A further increase would attract national attention and likely have a negative impact on visitors and meeting planners. However, redirecting a portion of the car tax to CVB promotions and marketing would help protect that revenue source and increase visitors and visitor spending in general.
- We estimated the revenue from an increased occupancy tax taking into account recovery from the current period of slow economic growth and tying together our projections of RDU air traffic and hotel stays.

Using a scale of 1 (best) to 4 (worse), as shown in figure 1, we compared the six taxes, accounting for their impact on: general Durham business, specific types of business, lower income households, nearby and distant day-trip visitors, overnight visitors and conventions

- From an economics perspective, we recommend four of the six taxes in the following order (most to least favorable): Airport tax, occupancy tax, restaurant tax, admissions tax.
- We recognize that an airport tax may be difficult to impose because of the multiple jurisdictions involved and possible covenants that exist. However, that tax would raise significant revenue at low rates and have the least unfavorable economic impacts.
- The restaurant tax could be imposed on meals above \$10 and have a minimal impact on low income families, a particular concern raised in Durham politically. However, this would miss the majority of drinking and eating establishments and the substantial number of higher income households who frequent lower priced quick service restaurants.
- We recommend that any of these taxes that are imposed have a significant portion earmarked to CVB promotional activities to offset the negative economic effects of higher taxes, and also to overcome the already negative impact of the current 13% bed tax.

Often taxes are seen as fixed budget amounts to be divided among programs like slices of a pie. Investing in CVB promotions and marketing can increase the pie, thereby enhancing revenue for all purposes. To do that, funds must be allocated initially to CVB activities from what seems to be fixed revenue, but is actually dynamic revenue that will increase as marketing takes effect.

Figure 1

Impact Comparison of Tax Alternatives

Durham County 2003 est.*

Tax to add or increase	Highest reasonable additional rate	Approximate annual revenue yield	Initial impact	Ultimate Impact (scale 1 to 4, where 4 is worse)				
				Impact on Durham business/jobs in general	Impact on specific Durham business and jobs	Impact on lower income households	Impact on overnight visitors	Impact on conventions
Tax on eating & drinking out	3.00%	\$8.1 million	Residents, non-resident workers, daytrippers, overnight visitors	2	3	2	1	1
Occupancy tax**	2.00%	\$1.9 million	Overnight visitors	1	3	2	2	2
Car rental tax	0.00%	No added revenue	Overnight visitors	1	4	1	2	2
Airport/Airline taxes	\$2 / outbound	\$2.3 million	Overnight visitors, local residents who travel	1	2	1	2	2
Gasoline tax	2 cent / gal.	\$2.0 million	Residents, non-resident workers, daytrippers, overnight visitors	1	2	3	1	1
Admissions tax	\$195,000 per 1% amusement tax; \$60,000 per 1% movie tax		Residents, daytrippers, overnight visitors	1	2	2	1	1

*As if tax had been in effect the entire year and stabilized. NOTE, many of these levies require state legislation and agreements.

**Use of the funds for visitor promotions can more than offset the negative impact.

II. Background

A. Introduction

American Economics Group, Inc. (AEG) was asked to investigate the suitability of various visitor-related taxes as a means to fund local government services including the extent to which any revenues should be earmarked for visitor promotion and marketing to protect and fuel these revenue sources.. The quandary of imposing greater taxes is that higher prices of lodging, meals, car rentals, admissions or gasoline, etc. will reduce sales of those goods and services. However, if the tax proceeds are put to good use, they may actually increase demand and more than offset their economic burden.

One example of a sound tax policy that increases economic activity is an earmarked lodging tax used to promote visitors, conventions, business meetings and overall tourism. If applied at reasonable rates and used effectively to augment visitor traffic, the natural tendency of higher prices (including taxes) to reduce sales may be overcome by shifting demand for a local area to a higher position among its competitors.

This study addresses the following questions: 1) Which new or higher visitor-related taxes are suitable to help fund local government services and lessen over reliance on property taxes? 2) How much will these new taxes generate in revenue? 3) What is their effect on the existing travel to Durham? 4) How much will they affect business and jobs in the community? 4) To what degree will their burden fall on lower income resident households?

It is often difficult to imagine that a small change in a tax will affect behavior in a significant way. However, it is seen over and over again that people adjust their behavior in response to tax changes. Even small changes will affect some economic decisions, and it is important to gauge their impact before imposing them. This analysis does that, and focuses on the incremental effect of each tax.

Methodology Overview

AEG uses a two-step approach to estimate the impact of higher taxes. The first step employs a simulation model that calculates collections from the tax in question. For example, the restaurant meals tax employs a database of annual sales by price calibrated to the Durham area. The simulation calculator applies historical price elasticities¹ to the data in order to adjust sales in response to a meals tax. Another model feature restricts changes to the portion of the food and beverage market affected by the tax.

The second step estimates the full economic impact under pre- and post-tax scenarios, including the effect on all sales, jobs and wages in the county. This uses AEG's input-output model based upon the well-known "Implan" economic impact system.

The economic impacts include the following concepts:

- (1) **Direct Impact:** Economic activity directly providing visitors with lodging, food and beverages, amusements, shopping, transportation and other goods and services. The size and number of meetings and trips and average visitor spending per trip affects this.
- (2) **Indirect Impact:** Economic activity from Inter-industry purchases among businesses directly serving visitors and their suppliers and, subsequently, suppliers purchasing from their suppliers.

¹ Elasticity refers to the effect on sales of a change in price. It is commonly calculated as the percentage change in the quantity sold following a given percentage change in price. Price means total price including all taxes.

- (3) **Induced Impact:** Economic activity created by the household spending of employees, owners and others affiliated with the direct and indirect industries.

B. Selected Visitor-Related Local Option Tax Menu

There are more than two dozen possible visitor-related taxes and fees that might be considered in a local option menu to both fund local government and to support CVB promotional activities. Some are already levied by North Carolina, by Durham County, by The City of Durham, or by other jurisdictions in the area. Other taxes would be new to the area or feature new components.

Based upon our review and the tax principles discussed below, we have focused our work upon a list of six taxes. We selected ones that have a logical connection with travel and visitors, have a sufficiently large base to raise several million dollars at reasonable tax rates, and have a collection history in other places across the country. These are:

- A tax on purchase of prepared food and beverages by-the-drink (restaurant meals tax)
- An occupancy tax on hotels, motels and other transient lodging
- An airport/airline tax based on passenger enplanements
- A gasoline tax on purchases for on-road vehicles
- A motor vehicle rental tax
- An admissions tax on amusements and sports events

Judging a tax by its characteristics

Each tax has its own characteristics that affect its suitability to support CVB activities. These include impacts on:

- Revenue collected
- Business and jobs in Durham, generally
- Specific local industries and businesses
- Lower income households
- Overnight visitors
- Daytrip visitors
- Conventions and meetings

Taxes considered will raise between \$1 million and \$8 million at reasonable rates. Each can be fine-tuned to target a specific revenue level, and some can be established to avoid untoward effects on low income households or other identified groups. After presenting each tax in sequence, figure 1 in the Executive Summary is a table that compares them on the important features listed above.

When is a tax excessive?

Aside from the political reality of elections that may define tax “reasonableness,” there are the twin issues of competition and economic impact. Durham must compete with other visitor, convention and meeting

destinations. New York City found itself blackballed by meetings planners when its combined bed taxes stood at 22%. With a label of “New York: stay four nights, pay five,” convention planners moved the city off their charts, and convention bookings plummeted. Clearly, the New York tax was “unreasonable.”

Each area has its own threshold of “tax excessiveness.” Two areas can have equal prices and taxes, but if one has a vastly greater visitor attraction quotient, it may be able to raise its tax rates, while the other cannot. We have used our experience and judgment in suggesting top tax rates in Durham County for each of the taxes studied.

An important caveat: legal authority to impose these taxes is not examined in this analysis

This analysis is done solely from an economics perspective. Taxes are examined without consideration of the legal authority to impose them, the political will to do so, or the arrangements with neighboring jurisdictions that may be needed. Some new taxes or increases may be undertaken locally without additional authority. However, many will require state-level legislation to impose them directly or to authorize local statutes levying them. Also, in the case of the airport passenger enplanement tax and perhaps the motor vehicle rental tax, the location and joint ownership of the airport with neighboring Wake County may require a joint undertaking and an appropriate agreement on how to advance the authority and split the tax proceeds.

Consider the tax burden

First, there is the tax burden, meaning who pays the tax? Of course, in the first instance the person who hands over cash or a credit card to pay for a meal or room or a tank of gas pays the tax. However, the burden may shift, and be borne by businesses affected by reduced spending in response to the tax. Or businesses may reduce prices to offset the tax and push wages downward, thus transferring the burden to their employees. How this all works out is determined by how extensively consumers alter their purchases and how aggressively businesses react to recapture profits.²

One important consideration is the degree to which a tax burden is exported out of the county. A popular misconception on taxes that affect visitors is that because they pay the tax initially they carry its burden home with them. However, to the extent Durham business is reduced, jobs are cut, and less income is generated, the tax burden remains in Durham. This split between the impact on initial taxpayers and the businesses and workers in Durham who may bear a significant part of the burden must be examined carefully.

The impact of a tax begins with the initial response of consumers to increases in the prices they pay including taxes. Then, to avoid common misconceptions about who bears the tax burden and where the ultimate impacts of a tax fall, the path of the tax burden must be traced. The party initially paying the tax may not end up bearing its full cost. An example using the occupancy tax illustrates the tax “shifting” mechanism:

Both economic theory and sound research validate the well known inverse relationship between the price of a good or service and the amount of it sold, meaning that as prices rise, sales fall, and vice versa. Hotel room sales are no different in this regard from most other goods and services. At higher room rates, fewer room nights are sold, other things equal. Consider a new occupancy tax of 13% in an area with no bed tax. Overnight visitors notice up to a 13% increase in the final cost of their rooms, and over time some visitors would reduce the nights they stay, shift to lower priced rooms or even avoid the area entirely.

As word spreads to other travelers and to meeting planners, there is a decided drop in revenue per available room (REVPAR) at hotels in the area. In response, hoteliers reduce their rates, give larger discounts to attract groups, increase promotions and other business-building steps. The question arises, “Who is paying the tax?” Obviously, visitors pay the tax in the first instance. But, the hotels are “taxed” implicitly by losing revenue. The final resting place of the tax burden is partly with visitors and partly with hotels, their relative proportions depending upon many factors including the unique attractiveness or pull of the area, the other destination options available, the cost to hotels of discounts, advertising, promotion and other factors. The answer turns out to be quite complex.

² Economists examine the elasticity of demand (the consumers’ response) in contrast to the elasticity of supply (the business response) to determine how the tax burden splits between these two groups.

Skillful use of tax proceeds can actually increase visitors to Durham

The normal effect of increasing taxes on visitors is to reduce their number of trips, length of stay and amounts spent on lodging, food and beverages, amusements, purchases of merchandise, etc. However, that need not be the case. If at least part of the tax proceeds is earmarked to the CVB's promotional activity, the negative effect may be more than overcome.

This requires CVB "leveraging" of funds to shift demand and attract more additional meetings and visitors than are reduced by the tax. The effectiveness of promotional spending can be tracked and measured following a tax increase, if a statistical process is established in advance or perhaps already exists.

Issues in earmarking tax revenues

"Earmarking" is a term used to denote that a tax or portion of it may be used only for a certain purpose. As the revenue flows in, the earmarked portion automatically flows to the proper account to be used for the purpose intended. This differs from the usual budget process in which revenue flows into a general fund and is dispersed for the full array of budgeted expenditures. Advocates for roads, schools, the environment and travel promotion have been the most successful in getting taxes earmarked for their programs.

A new earmarked tax, say for education, may get public support when a general increase will not. That is one reason behind earmarking. Another is to carve out a portion of revenue by statute, to have the money flow automatically and avoid an annual debate that might result in a lower appropriation for the earmarked item. A program may be more secure if it depends upon earmarked funds rather than general funds. Even though either can be changed by legislation, removing earmarking is a specific identifiable act that can more easily raise opposition.

In some situations, earmarking may act like a "fee for service," as in the case of road taxes that pay for construction and maintenance of roadways for the use of those paying a gasoline tax. Earmarking may even act like "dues." For example, a special business district may be established within which an additional property tax levy is charged to pay for litter removal or added police or transportation or parking, etc. Earmarking can even be used to offset the burden on low income households, e.g. job training.

An important use of earmarking is to protect and enhance the tax, itself. Bed taxes illustrate the case where a tax is imposed to raise general revenue, but by earmarking a portion of receipts to a CVB to promote the area as a destination, added revenue is raised without jeopardizing hotels, restaurants, sports events, theaters, retail stores and other travel-supported businesses. In fact, if properly leveraged, the amount dedicated to promotion may more than offset the burden of the tax, and actually enhance the travel sector in the Durham area.

One caution concerning earmarked taxes is needed in the situation where the dedicated funds are in addition to a much larger flow from general funds into a program area. A dedicated lottery for education is an example of this, in which earmarking may be no more than an expedient way to get voter approval for the lottery. Once established and funds are flowing, the general funds are back down to less than they would otherwise have been. Thus, the lottery did not really add money to education, but rather added it to general revenue.

This strong criticism of earmarking does not apply when earmarked taxes dominate the government payments for a given program. All of the taxes we are examining in this analysis avoid this worry because there is no large general fund appropriation to the CVB to use in the offset game just described. Earmarking funds for CVB promotions makes good sense because they can help protect the revenue source itself and mitigate or eliminate any negative impact from a higher tax.

Visitors and conventions including meetings create significant sales, jobs, local tax revenues and income; new or increased taxes should be designed to not harm this relationship

Earlier, in the methodology section, we discussed the three levels of economic impact a tax may have. These are: the direct impact (visitor and meeting spending), indirect impact (spending on suppliers), and induced impact (employee spending).

The full economic impact of visitors and meetings on Durham area business is best understood in the context of the sales, jobs, and wages they support. Visitor spending in 2000 supported an estimated \$573 million in taxable sales for businesses throughout the City and County. Workers held 10,682 jobs to produce these goods and services and were paid \$216 million in wages and other compensation.³

The full economic impact of visitors begins with direct spending of \$559 million in 2000 on lodging, food and beverages, retail purchases, sports events, amusements and other goods and services. Of this amount, about \$177 million was spent on rooms and about \$382 million on the long list of other items purchased in other types of non-lodging businesses.. Even in hotels, sponsors of conventions and meetings and those attending the meetings or conventions also purchase food; rent equipment, exhibit space, and meeting rooms; host hospitality suites; and acquire a variety of business services.

Here is a benchmark to consider with the specific taxes discussed in the next section:

If high taxes reduce Durham's overnight visitor spending by just 5%, total taxable sales of local business will fall by \$28.6 million, 535 jobs will be lost, and the collection of all other state and local other taxes will fall.

³ "The Economic Impact of Visitors to Durham, N.C.," prepared for the Durham Convention and Visitors Bureau by D.K. Shifflet & Associates and American Economics Group, Inc., October 29, 2001.

III. Alternative Tax Possibilities:

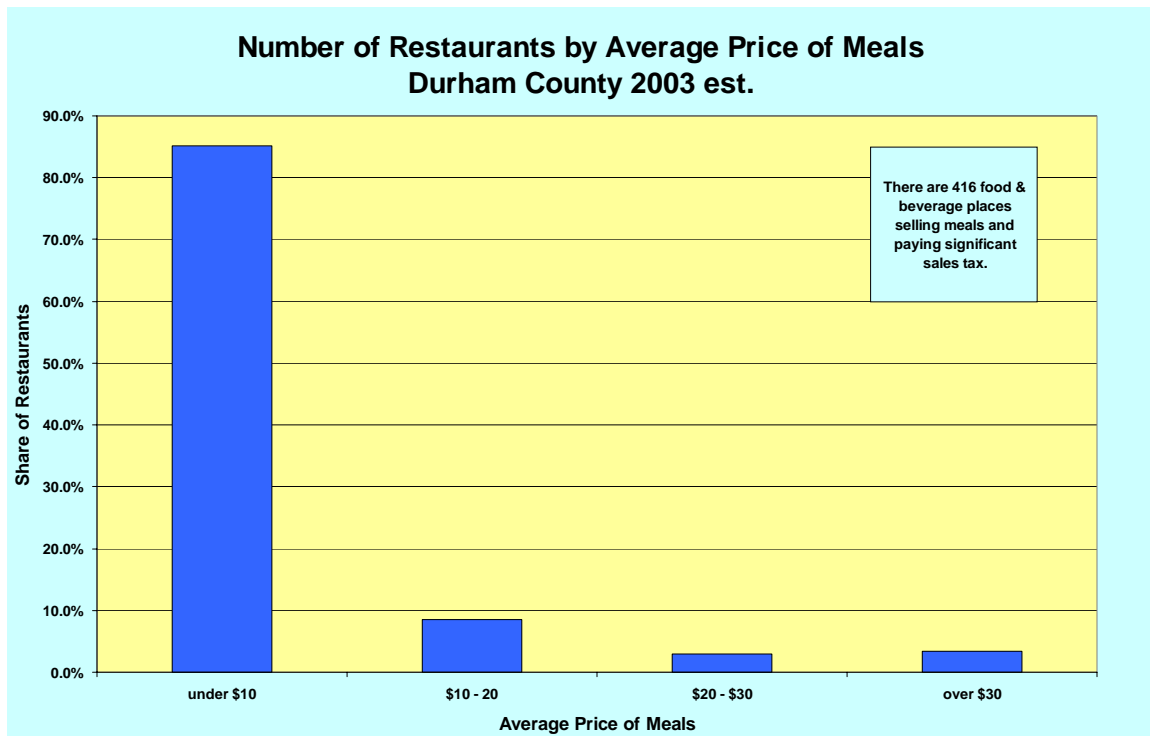
A. Restaurant Meals Tax (Prepared Food)

The variations of a restaurant meals tax considered here would levy an additional tax of 1%, 2% or 3% upon restaurant meals in excess of some fixed amount per person. We have made calculations for a tax limited to meals over \$10, over \$15 and over \$30.⁴ The tax would be added to the current sales tax rate of 7%.

“Restaurant meals tax” is a bit of a misnomer because it applies to most sales of prepared food and sales of beverages by the drink and in single serving containers. Thus, restaurants, taverns and bars, fast food vendors, delicatessens, sandwich shops, coffee stands, donut shops and all similar establishments would be included. Alternatively, the tax would be applied to all sales or to sales of more than a \$10, \$15 or \$30 threshold set in law.⁵ As the threshold increased, the tax becomes closer to a pure restaurant tax because many other eating and drinking places would be excluded because of their lower average checks.

Figure III-1 shows the large number of eating and drinking places with average checks under \$10, about 85% of establishments fall into this category. About 9% have average sales between \$10 and \$20, while only a few percent average higher amounts per patron.

Figure III-1



⁴ Of course, the threshold could be set to any level as could the tax rate. The calculations here are simply a guide to what various combinations of tax rates and thresholds would yield in revenue.

⁵ These calculations are based upon the tax applied to a purchase by individuals. Parties of two or more would pay the tax if the amount of their combined check was greater than the threshold when divided among them. As with any tax there is the potential for taxpayers to try to game the system, but in general the tax could be applied fairly and controlled by the computerized registers now found in most businesses.

Figure III-2 takes a slightly different view and reveals the full distribution of meals by price regardless of the restaurant or other merchant selling them. The average meal before tax is just under \$8, while most sales (the mode) are under \$6. This accounts for the larger number of fast food restaurants, coffee sellers, sandwich makers and other small ticket vendors.

Figure III-2

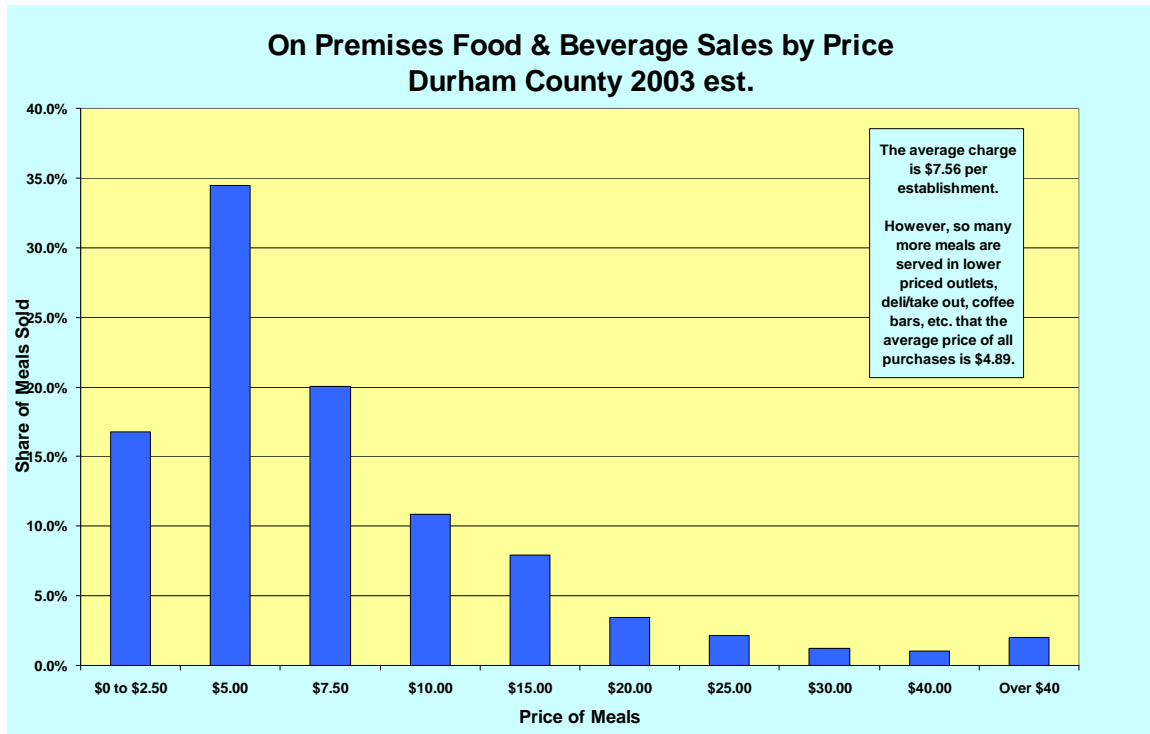


Figure III-3 summarizes the collections from each combination of additional tax rate and threshold price of meals. It covers all sales in Durham County falling under the tax during calendar year 2003. We estimate \$303.8 million in total sales. Adding a 1% tax would decrease sales slightly to \$301.3 million and yield \$2.743 million in tax, if applied to all sales. That would increase to \$5.436 million at 2% and \$8.080 million at 3% above the existing sales tax.

Applying the 1% tax would yield \$1.402 million if limited to meals over \$10, \$1.041 million if over \$15, and \$0.625 million if over \$30. Increasing the rate to 2% would result in revenue increasing slightly less than proportional. For meals over \$10 the yield would be \$2.778 million, \$2.063 million for meals over \$15, and \$1.239 million for meals over \$30. Finally, a 3% additional tax would return \$4.129 million applied to all meals over \$10, \$3.066 million raising the meal threshold to \$15, and \$1.842 million for meals \$30 and over.

How much of the tax would fall on Durham County residents is answered in Figure III-4. The table is similar to Figure III-3, except it shows the results only for county residents. The amounts in the table decline by roughly 36%, although they vary from category to category. A 2% tax applied to meals over \$10 would draw from within the county \$1.8 million of the total tax collection of \$2.8 million. At the high end, a 3% tax on meals over \$30 would draw \$1.2 million from county residents of the total of \$1.8 million.

Figure III-3

Total Additional Tax if Higher Sales Tax on Restaurant Meals*								
Durham County (as if in effect for all of 2003)								
Additional sales tax	All meals		Meals \$10 & over		Meals \$15 & over		Meals \$30 & over	
	Sales	Added tax	Sales**	Added Tax	Sales**	Added tax	Sales**	Added tax
No change	\$303,807,841	\$0	\$155,234,699	\$0	\$115,277,860	\$0	\$69,241,064	\$0
1% tax	\$301,252,448	\$2,742,970	\$153,928,987	\$1,401,558	\$114,308,233	\$1,040,802	\$68,658,663	\$625,152
2% tax	\$298,697,055	\$5,436,468	\$152,623,274	\$2,777,836	\$113,338,606	\$2,062,832	\$68,076,261	\$1,239,029
3% tax	\$296,141,662	\$8,080,494	\$151,317,562	\$4,128,837	\$112,368,979	\$3,066,089	\$67,493,860	\$1,841,631

*All figures account for reduced sales at higher prices when tax is raised.

**Sales of meals at and above the price indicated

Figure III-4

Additional Tax from Durham Residents if Higher Sales Tax on Restaurant Meals*								
Durham County (as if in effect for all of 2003)								
Additional sales tax	All meals		Meals \$10 & over		Meals \$15 & over		Meals \$30 & over	
	Sales	Added tax	Sales**	Added Tax	Sales**	Added tax	Sales**	Added tax
No change	\$192,337,218	\$0	\$98,277,286	\$0	\$72,981,075	\$0	\$43,835,714	\$0
1% tax	\$190,989,060	\$1,757,423	\$97,588,427	\$897,979	\$72,469,526	\$666,842	\$43,528,454	\$400,536
2% tax	\$189,640,902	\$3,488,745	\$96,899,567	\$1,782,621	\$71,957,976	\$1,323,781	\$43,221,195	\$795,122
3% tax	\$188,292,744	\$5,193,968	\$96,210,708	\$2,653,928	\$71,446,426	\$1,970,816	\$42,913,935	\$1,183,761

*All figures account for reduced sales at higher prices when tax is raised.

**Sales of meals at and above the price indicated

The breakdown of taxpayers between residents and non-residents appears in figure III-5. Of the \$303.8 million in total sales of prepared food and single beverages, \$192.3 million, 63.3%, is spending by residents. Of the remaining amount, \$42.2 million comes from nearby non-residents, 13.9% of total, and \$69.3 million is spending by overnight visitors and day travelers from outside the three county area.

Figure III-5

Who Purchases Restaurant Meals in Durham County?		
All Food & Beverage Purchases in Durham County 2003 est.		
	Purchase of food and beverages at eating & drinking places	
Durham County residents	\$192,337,024	63.3%
Out-of-county commuters & daytrip visitors (under 50 miles)	\$42,235,223	13.9%
Overnight visitors & daytrip visitors (over 50 miles)	\$69,235,593	22.8%
Total	\$303,807,841	100.0%

An additional perspective on the impact of the tax is given in figure III-6. It reveals the expected impact of the tax by household income class. The table shows only the 1% tax, but it presents it for each price threshold. (An approximate estimate of the 2% and 3% tax is slightly less than doubling or tripling the 1% tax.)

The 95,602 households residing in Durham County are distributed by total household income. Their numbers are in column two. Next to that is the average amount they spend of food and drink away from home followed by the total amount for that income class.⁶ The remaining sections list the total added tax paid by each category and the average dollar amount of that tax per household.

For example, households in the \$10,000 to \$14,999 income class would spend an average \$10.75 more in tax over the course of a year, if the 1% tax was applied to all items without a threshold. At a %10 threshold, the average amount would fall to \$2.65 per year, to \$1.17 at a \$15 threshold, and 46 cents if the threshold for the tax was \$30. Obviously few families with incomes under \$15,000 will be buying meals priced above \$30.

One important consideration that relates to the income distribution is that higher income households purchase many low priced meals, beverages, sandwiches and snacks. Thus, the lower the threshold is set, the more of their spending is taxed. Setting the threshold higher does concentrate the tax more at higher incomes, but limits the amount of spending that is taxed in those same households.

⁶ Note that the lowest income class has a slightly higher average spending on food and drink away from home. That is because of the large number of single individuals and students that are included.

Figure III-6

Burden of Additional Sales Tax on Restaurant Meal Purchases

Durham County Residents Purchase in Durham County 2003 est.

Household Income	Number of Households*	Average annual spending on food & drink away from home	Total annual spending on food & drink away from home	Additional sales tax of 1% on all restaurant meals		Additional sales tax of 1% on meals over \$10/person		Additional sales tax of 1% on meals over \$15/person		Additional sales tax of 1% on meals over \$30/person	
				Additional sales tax paid	Additional tax per household per year	Additional sales tax paid	Additional tax per household per year	Additional sales tax paid	Additional tax per household per year	Additional sales tax paid	Additional tax per household per year
\$0 to \$4,999	2,218	\$1,142	\$2,532,548	\$19,364	\$8.73	\$557	\$0	Minimal	Minimal	Minimal	Minimal
\$5,000 to \$9,999	6,635	\$712	\$4,725,555	\$54,213	\$8.17	\$3,966	\$0.60	\$760	\$0.11	Minimal	Minimal
\$10,000 to \$14,999	6,788	\$896	\$6,081,294	\$72,994	\$10.75	\$17,974	\$2.65	\$7,925	\$1.17	\$3,107	\$0.46
\$15,000 to \$19,999	7,572	\$928	\$7,027,738	\$84,429	\$11.15	\$17,891	\$2.36	\$8,746	\$1.16	\$6,474	\$0.85
\$20,000 to \$29,999	12,734	\$1,196	\$15,227,712	\$170,475	\$13.39	\$42,137	\$3.31	\$22,908	\$1.80	\$10,185	\$0.80
\$30,000 to \$39,999	10,000	\$1,451	\$14,507,160	\$155,843	\$15.58	\$59,986	\$6.00	\$42,640	\$4.26	\$25,109	\$2.51
\$40,000 to \$49,999	8,757	\$1,811	\$15,855,588	\$138,555	\$15.82	\$60,246	\$6.88	\$35,094	\$4.01	\$19,620	\$2.24
\$50,000 to \$69,999	11,147	\$2,331	\$25,982,983	\$209,564	\$18.80	\$106,240	\$9.53	\$79,413	\$7.12	\$44,699	\$4.01
Over \$70,000	29,751	\$3,375	\$100,396,447	\$851,986	\$28.64	\$588,982	\$19.80	\$469,356	\$15.78	\$291,341	\$9.79
Total	95,602	\$2,012	\$192,337,024	\$1,757,423	\$18.38	\$897,979	\$9.39	\$666,842	\$6.98	\$400,536	\$4.19

*Not all of these households eat out, and others vary from nearly every day to infrequently.

The initial impact of the restaurant meals tax is, of course, upon those purchasing food and beverages. The effect is moderate for the Durham economy as a whole when limited to a 3% rate and particularly as the threshold price where the tax applies rises to over \$10 or \$15. There is a stronger impact on the specific industry of eating and drinking places that can only be offset by additional traffic, such as developed by CVB promotions that build visitor traffic.

The impact on lower income households is moderate, but less so than several other taxes examined, including the bed tax. The impact of a higher food and beverage tax would have minimal impact on visitors and minimal impact on attracting conventions and meetings to Durham. Those travelers have experience with meals taxes and, in any event, Durham meal prices are below what is expected in many cities. Visitors will not get sticker shock because of a 1% to 3% additional tax. Raising the tax above that level will also heighten an adverse comparison with nearby areas.

Higher taxes affect both business and consumers. Increasing the sales tax on restaurant meals will inevitably reduce restaurant sales, other things equal.⁷ Figure III-7 reveals the sales restaurants will lose at alternative tax rates and meal price thresholds.

Taxing all meals an added 3%, for example, will cost restaurants about \$2.5 million in sales of food and beverages, as shown in the third column of the table. The same 3% applied to meals of \$30 and over will reduce restaurant sales by about \$1.3 million (last column). The loss in sales includes some patrons moving to lower priced menu items, some switching to lower priced establishments, some dividing a fixed budget between tax and food, some eating more at home, and others dining outside Durham County.

⁷ Using tax revenue for CVB promotions and marketing will protect the revenue stream by adding more visitors and visitor spending to Durham. Other things would not be the same, if the funds were spent to enhance business.

Figure III-7

Change in Restaurant Sales under Alternative Taxes on Restaurant Meals*								
Durham County (as if in effect for all of 2003)								
Additional sales tax	Tax on all meals		Tax on meals \$10 & over		Tax on meals \$15 & over		Tax on meals \$30 & over	
	Total Sales	Lost Sales	Total Sales*	Lost Sales	Total Sales*	Lost Sales	Total Sales*	Lost Sales
No change	\$303,807,841	\$0	\$303,807,841	\$0	\$303,807,841	\$0	\$303,807,841	\$0
1% tax	\$301,252,448	\$2,555,393	\$303,285,556	\$522,285	\$303,274,546	\$533,295	\$303,371,040	\$436,801
2% tax	\$298,697,055	\$2,555,393	\$302,763,271	\$1,044,570	\$302,741,251	\$1,066,590	\$302,934,239	\$873,602
3% tax	\$296,141,662	\$2,555,393	\$302,240,986	\$1,566,855	\$302,207,957	\$1,599,884	\$302,497,438	\$1,310,403

*Accounts for lower sales of meals in each price range and shift of some patrons to lower priced food.

Occupancy Tax on Hotels, Motels and other Overnight Lodging

The typical occupancy or bed tax is what economists call “ad valorem” taxes, that is calculated as a percent of the price of the room. Infrequently, they are applied as “unit” taxes, a fixed dollar tax per night. In another wrinkle, occupancy taxes may be unique taxes on overnight visitors or combined in some way with a general sales tax. In many jurisdictions there is both an occupancy tax and a local sales tax. In some localities the total bed tax consists of an occupancy tax plus a sales tax on overnight lodging, plus even an additional assessment for some specific purpose like a convention center.

Across the country, bed tax rates (including sales taxes and all combinations) vary widely. They average about 12% and extend to just below 20%.⁸ Most locations tax between 10% and 13%. Currently, the tax in Durham County is 13% after several recent increases in both the occupancy and sales tax, This leaves some leeway to raise it without becoming part of the highest taxed group.

Occupancy taxes are often used by local politicians as a way of exporting the tax burden out of the state or local area. This misguided thinking stems from a low awareness of the link between overnight visitors and local sales, jobs, and taxes. Many bed taxes cost government more in lost revenue from sales taxes, income taxes, and other levies than they bring in themselves. In Durham, for example, a 5% reduction in overnight visitors caused by an excessive tax would reduce state and local tax collections by about \$5 million. High bed taxes can be harmful not only to the lodging industry but to many other businesses in the city, county, and state imposing them.

One serious problem is that bed tax collections often flow to general revenue in state and local governments, and are not used for travel-related purposes. When spent on travel promotion for convention and visitors bureaus, and for other travel-expanding purposes, that portion of the tax levy is less destructive to the lodging industry because it builds travel business and protects the revenue source, itself.

Because virtually all business in Durham benefit to some degree from spending by overnight lodging guests and visitors more generally, it is a concern that the higher taxes may reduce visitor stays and spending. To the extent there is a potential negative impact on the local economy from the increased taxes, the CVB may initiate other measures to promote and otherwise augment visitor activity in Durham to reclaim any loss and even expand beyond that. Durham business would benefit as would the county and city from even greater tax collections.

Both economic theory and empirical studies suggest an inverse relationship between the price of a good or service and the amount of it sold. That is as prices rise, sales fall, and vice versa. Hotel room sales are no different in this regard from most other goods and services. At higher room rates, fewer room nights are sold, other things equal. The room rate is the price for the entire bundle of goods and services the hotel provides to overnight guests. The bed tax is the payment for a different bundle of goods and services provided by government (known as “complementary goods”). These include a wide range of items from police protection and ease of public transportation to cleanliness and various amenities.

Occupancy tax impact in Durham

Figure III-8 summarizes the tax revenue and resulting change in room nights sold if an additional occupancy tax of 1% was applied to all Durham County overnight stays on top of the 1% that was added in 2002. We have projected an average room rate of \$74 for 2003, increasing by about 2.5% annually. Room night sales for 2003 are projected at 1,462,053 room nights under the current tax and under current conditions. These would increase by 7.2% in 2004 reflecting a pickup in the economy and in travel generally. Growth continues but falls into the 5% to 6% range for the remaining years through 2008.

Taking account of Durham’s competition with other areas for conventions and meeting, an additional 1% room tax, bringing the overall rate to 14%, will reduce room sales unless offset by CVB promotional activities. The

⁸ We are in the process of conducting a detailed state and local bed tax survey for the American Hotel and Lodging Foundation. It will be completed in the fall of 2003.

worse case scenario is depicted in the remaining columns of figure III-8, which does not allow any portion of the tax to flow to the CVB.

The result is a 0.5% reduction in room night sales assuming no change in hotel pricing. The added tax would have brought in just over \$1 million annually, if it had been applied for the entire 2003 calendar year. This increases to about \$1.6 million by 2008 under the assumptions noted above. The adjusted room nights columns account for the suppression of sales by virtue of the higher total room price after the increased tax is applied.⁹

The final two columns in the table show the tax needed to reach a target level of \$8 million in collections in the initial year. The rate would have to be set at 7.79% in addition to the current tax, a total rate of 19.79%, a national tax high. Notice the reduction in room sales by about 3.5%.¹⁰

Figure III-8

Additional Occupancy Tax on Overnight Visitors						
Durham County (estimated as if in effect for entire year)						
Year	Average room rate	Room nights sold with current 13% tax	Adjusted room nights	Added tax at 1.0%	Adjusted room nights	Added tax at 7.79% (to reach \$8 million target revenue)
2003	\$74.00	1,462,053	1,455,584	\$1,059,133	1,411,669	\$8,000,000
2004	\$75.85	1,567,882	1,560,945	\$1,164,192	1,513,851	\$8,793,546
2005	\$77.75	1,657,372	1,650,039	\$1,261,407	1,600,256	\$9,527,841
2006	\$79.69	1,751,970	1,744,218	\$1,366,739	1,691,594	\$10,323,451
2007	\$81.68	1,851,967	1,843,772	\$1,480,867	1,788,145	\$11,185,498
2008	\$83.72	1,957,671	1,949,009	\$1,604,525	1,890,206	\$12,119,530

⁹Currently, Durham’s 13% lodging tax is reducing taxable lodging revenue from overnight visitors by about \$7.0 million and room nights by 95,033. This includes the impact of the recent tax increase of 1%, which reduced lodging revenue by \$540,000 and room night sales by 7,310. By 2008, this loss will grow unless additional CVB promotion increases the demand for Durham rooms. In that year, the 13% hotel tax is expected to reduce room revenues by almost \$10.7 million and to reduce room nights sold by 127,249.

¹⁰ Of course, pushing the rate to the highest level would have its own signal effect and a potentially greater impact should convention planners conspire to avoid Durham.

Need to offset tax increase with additional CVB promotional activity

Instituting higher bed taxes without offsetting their impact would be a risky policy for Durham to follow. The reduction in overnight visitors by about 3.5% would mean a serious loss of sales to local business, of jobs to local residents. It would also mean a reduction in the collection of other state and local taxes by over \$3 million, offsetting the \$8 million the added occupancy tax would yield. It would make sense to dedicate a substantial portion of any new levy to be used in advertising and promotional work to attract conventions, meetings and tourists to Durham.

There is a time lag between the implementation of a new or increased tax and its full effect. In part, this reflects the difficulty visitors and organizations have in immediately adjusting their plans in response to the tax. In part, the "learning curve" reflects the time it takes for the tax changes to become generally known and taken into account. There will also be a lag between the promotional expenditures CVB may make and the resulting increased visitor activity. Once implemented, several years should be allowed before a full assessment of the tax impact can be validated.

C. Airport/Airline taxes

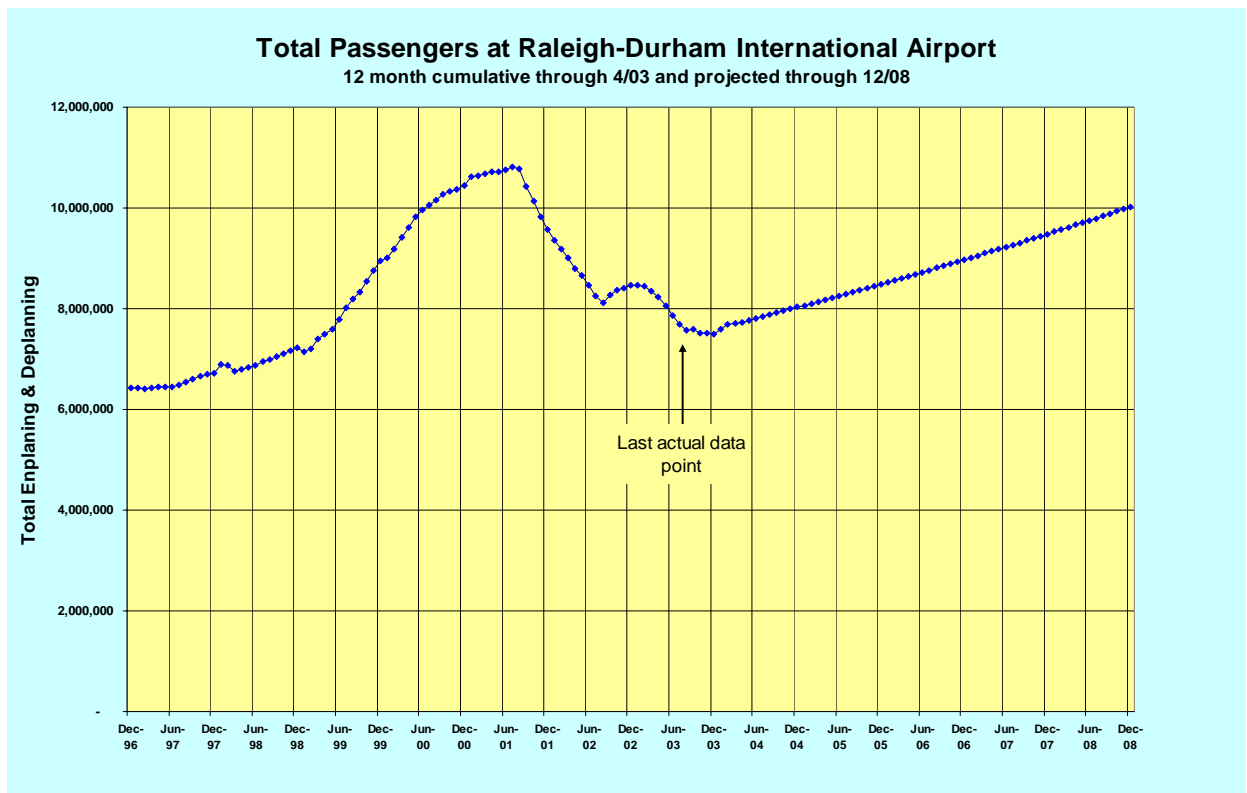
For Durham County to establish a new tax on airlines or air passengers would require legislative and regulatory action as well as some agreement between Durham County and Wake County, in which the Raleigh-Durham International Airport (RDU) is located. The design of such a levy would require significant additional research as well. There would be many hurdles to overcome before Durham would see any added revenue from new airport taxes or fees.

Consequently, the purpose of this portion of the analysis is only to examine the possible dimensions of an airport/airline tax. Given that the tax would support visitor and meetings promotions, we selected as the tax base for this analysis the total number of passengers moving through RDU annually. There are, of course, air freight and tangential activities that might be taxed; however air travelers represent the closest link to travel promotions.

Consider this a gauge of the dimension of an airport/airlines tax, however levied, as measured by the number of air travelers through RDU.

Figure III-9 graphs the total number of passengers enplaning and deplaning at RDU. Each point is an annual total of the previous 12 months. This 12 month moving average removes the seasonality from the data, making the trends more easily visible.

Figure III-9



Before September 11, 2001, RDU experienced rapid growth in passenger traffic. In the 12 months ending in August 2001, traffic grew by 6.0%. Overall growth from 1996 to the fateful 9/11 date was over 10% annually. The sharp and immediate drop that month started the roll-off from a peak 11 million passengers to an expected

2003 level of about 7.5 million, a decline of nearly one-third. The national economic recession combined with the 9/11 aftermath continues to debilitate passenger air traffic.

However, brighter skies are ahead. We forecast sustained growth in annual RDU passengers from the 2003 low point forward at about an 7.2% annual rate. This takes account of the climb out of the recession, the completion of overseas wars of a major scale and a declining effect from the 9/11 attacks. (Renewed terror and or war activity could quickly alter that forecast.) Under these assumptions, RDU could expect to return to more than 10 million total enplanements and deplanements by 2008.

Figure III-10 tabulates the revenue from applying alternative tax rates to persons enplaning at RDU. Because most travel is in round trips, it makes little difference in the revenue applying the tax to passengers who are out-bound or in-bound or both. Meeting a specific revenue target, would mean adjusting the rate accordingly. (Conceptually, we favored taxing those who would leave versus those who would arrive.)

Figure III-10

Airline Passenger Head Tax on Enplanements				
Raleigh Durham International Airport (estimated as if in effect for entire year)				
Durham County's share based upon population (22.7% share of Triangle) adjusted for impact on enplanements				
Calendar Year	Total persons enplaning w/o tax	\$1.00 per person	\$5.00 per person	\$9.54 per person (to reach \$8 million target revenue)
2003	3,743,592	\$848,581	\$4,218,627	\$8,000,000
2004	4,014,567	\$910,043	\$4,524,935	\$8,582,524
2005	4,243,706	\$962,024	\$4,784,176	\$9,075,932
2006	4,485,923	\$1,016,973	\$5,058,241	\$9,597,595
2007	4,741,965	\$1,075,060	\$5,347,974	\$10,149,130
2008	5,012,622	\$1,136,463	\$5,654,271	\$10,732,242

*This amount per passenger speaks to alternative types of tax as well.

Because the airport is co owned by and located adjacent to Durham, but in Wake County, there must be a way to share collections between the two counties and other local jurisdictions. We have assumed a pro-rata distribution according to population. There are other possible allocators or even the potential of a home address allocator, but the population ration gives a reasonable sharing of the total levy.

A tax of \$1.00 per person would yield \$848,581 in 2003, assuming it had been fully in effect the entire year. By 2008, the tax yield would increase to over \$1.1 million. At \$5.00 per person, the results are just slightly less than proportional, yielding \$4.3 million in 2003 and increasing to \$5.7 million by 2008. Notice that there is an

elasticity effect that accounts for less travel at higher prices. It is not huge in this case, but it is apparent. To reach a revenue target of \$8.0 million would require a tax of \$9.54 per out-bound traveler.

If the split to Durham County were based upon its share of visitors to the Triangle rather than on population, the county would receive significantly more revenue. Figure III-11 calculates the result of a 45% allocation to Durham County. At \$1 per head enplanements, the revenue for 2003 would have been \$1,682,210 not \$848,581. The values in the table for alternative tax rates and years would rise proportionately.

Figure III-11

Airline Passenger Head Tax on Enplanements				
Raleigh Durham International Airport (estimated as if in effect for entire year)				
		Durham County's share based upon relative visitors (45% of Triangle) adjusted for impact on enplanements		
Calendar Year	Total persons enplaning w/o tax	\$1.00 per person	\$5.00 per person	\$9.54 per person
2003	3,743,592	\$1,682,210	\$8,362,916	\$15,859,031
2004	4,014,567	\$1,804,049	\$8,970,135	\$17,013,814
2005	4,243,706	\$1,907,096	\$9,484,050	\$17,991,936
2006	4,485,923	\$2,016,026	\$10,027,349	\$19,026,070
2007	4,741,965	\$2,131,176	\$10,601,710	\$20,119,420
2008	5,012,622	\$2,252,900	\$11,208,907	\$21,275,369

*This amount per passenger speaks to alternative types of tax as well.

The initial impact of the tax, of course, would be on travelers, visitors to Durham plus local Durham and less so on residents who travel by air. The impact on Durham business would be minimal, and the impact on travel-related business in the county would be small. Lower income households would be little affected by the tax.

While it would get notice by some visitors and by meeting planners, a low rate of tax at one or two dollars would not significantly hamper business. If it were dedicated at least in part to travel promotion, It could be a sound approach for the CVB to recommend. However, there is a difficult road to enact such a tax and it could be a long time before any revenue was distributed in the best of circumstances.

In our judgment, an airline passenger tax of \$2.00 per out-bound passenger should be considered a practical maximum. That would yield of \$2.3 million annually (not shown in table). If Durham is seriously interested in moving forward with an enplanement tax, we recommend additional study of the tax and its use and experience in other localities.

D. Gasoline tax

Because it is travel-related, an increase in the gasoline tax applied to all motor fuel sales in the county may seem at first glance to be a viable option to generate additional revenue for local government. However, the tax is so broadly applied to households of every income that it loses its link to visitors. Low income households in the area would be heavily impacted because transportation costs are an increasing burden on the working poor.

Moreover, the gasoline tax is highly unpopular with the electorate, and despite its value to the environment in reducing pollution, it has a troubled history at the state and local level. At least one governor has lost his position by calling for higher gasoline taxes. Local politicians suffer the same strong response from the electorate because gasoline costs, particularly at current high prices, have become a significant outlay for today's commuters¹¹.

If a two cent per gallon additional gasoline tax were applied throughout Durham County for all of calendar year 2003, revenue would be approximately \$2.1 million. A rule of thumb for this county is about a \$1 million yield for every one cent tax increase. At a several cents or more there would be a strong sales effect as even resident commuters began to fill their tanks in other counties.

Considering the broad impact of this tax, particularly on low income commuters, and its political liability, we do not recommend it and have limited our study of this revenue source.

¹¹ Commuters include both residents and non-residents who drive to work. Between the two groups, the impact would fall more heavily on resident commuters. Non-residents could more easily fill up at gas stations outside Durham County, a practice that would impact Durham station operators.

E. Vehicle rental tax

The vehicle rental tax or rental car tax as it is commonly known around the country is one of many fees and charges applied to rental customers. The current tax rate on rental vehicles at Raleigh-Durham International Airport (RDU) is quite high. It includes an 8% state alternative highway use tax, a 1.5% county vehicle rental tax, and a 5% tax for the benefit of the regional transit authority. In addition, there is an 11.11% airport concession “recoupment” fee, which pays for the rental facilities use of airport property. This fee is not uncommon at airports in the United States, most of which charge 10-11% for this service.

All considered, the combined total taxes and fees on automobiles rented at RDU is 25.61%. Notably absent from the taxes and fees charged at the airport is a city vehicle rental tax. North Carolina law permits cities to levy up to a 1.5% vehicle rental tax in addition to the 1.5% tax levy permitted for counties. While vehicles rented in the city of Durham are subject to this tax, vehicles rented at the airport are not.

In order to compare this rental rate against rates in other similar cities and metropolitan areas, we performed a total tax and fee calculation for a sample car, rented for four days at a rate of \$50 per day. This approach accommodates RDU taxes and fees, which are all calculated as a percentage of the rental rate while many other places assess them per day or per rental. In addition, all taxes and fees are calculated on a car rented from an airport location to ensure uniformity in the comparisons. Rentals elsewhere in an area will be somewhat different.

Based on the standard sample car used in this comparison, the total tax and fee rate at RDU of 25.61% is among the highest rates in the United States. It exceeds the median of total rates for taxes and fees on rental cars in other similarly sized jurisdictions by 4.66%.

Most of the other jurisdictions that have a higher rate than Durham include some fixed-dollar rate taxes or fees. Should the vehicle rental rate on the sample car be increased with inflation or price adjustments, Durham, which is on a percentage basis, would appear even higher relative to others, unless they specifically raised their fixed fees. Three cities—Little Rock, Austin, and Reno—have a total percentage rate of taxes and fees that is greater than the total percentage at RDU, so RDU is not destined to become the most expensive place to rent a car unless it specifically raises its tax.

How much room does RDU have to raise the rental car tax? Not much, we are afraid unless it wishes to have the tag as the highest tax in the country. The highest total percentage rate for taxes and fees on a rental car is in Little Rock, which charges a total of 28.13%. This is only 2.52% greater than the total rate at RDU, leaving little room to increase taxes and fees at RDU without pushing it to the highest rate among these similar cities.

We do not recommend further exploration of the vehicle rental tax as a source of additional revenue. In fact, the current combined tax already has a negative effect on car rentals at RDU, and no portion of the tax is “re-invested” to build demand and protect the tax revenue stream. Measuring the exact amount of business now lost is beyond the scope of this study. However, at the high tax level currently imposed, it is certainly a relatively large share of potential vehicle rental business.

F. Admissions/amusement tax

Admission and amusement taxes are difficult to estimate. We have prepared some approximate revenue estimates for alternative designs of admissions and amusement tax levy in Durham County. They are based on industries represented by industrial codes (NAICS) 512131 (movie theaters) and 71 (other amusements) from the 1997 Economics Census, the latest available for the area. Code 71 does not exactly match all businesses that would be taxed under a general amusements tax, but is reasonably close. These estimates have not been adjusted for inflation or local population or economic growth since the census was taken. They are included to give a sense of the revenue level from such a tax and should be calculated with more precision if such taxes were actively considered.

Admissions and amusement taxes in North Carolina are grouped with other business privilege license taxes imposed by the state. The state imposes a tax rate of 3% on gross receipts for amusement admissions, except for movie theaters, where the tax rate is 1%. The State greatly restricts the authority of local governments to levy additional taxes on amusement activities. North Carolina General Assembly Statutes §105-37.1(d) currently limits the tax imposed by local governments to a maximum of \$25.

Tax on athletic events

If Durham were to apply an admission tax on college sports, the bulk of the revenue would come from events related to Duke. That makes the home cities of other Atlantic Coast Conference (ACC) schools a good comparison base.

Nearly half the ACC is in NC, and so is subject to basically the same tax laws as Duke in Durham. The University of Virginia has a very low tax rate; and Florida State technically has to collect sales tax, but the revenues are kept by the University, so the tax is basically moot.

Duke financial information on athletics is not available; they're a private institution and they closely guard their detailed financials. Some analysis on ticket prices and attendance at football and basketball, the two major revenue producing sports, suggest what an additional admissions tax might yield. This could be a relatively painless way for Duke to compensate the community to offset part property tax savings as an exempt institution.

Assuming ticket sales for these two events at about \$5.5 million annually, a 1% added admissions tax would yield about \$55,000 in tax revenues. Since there is already a 3% state levy, and the highest taxes nationally on amusements and admissions are about 10%, it would not be entirely unreasonable for local governments to levy an additional 7%, resulting in approximately \$385,000 in annual revenue. If student ticket sales were exempt from the tax, collections would fall to approximately \$288,000.

The effect of higher prices including the tax would vary. Basketball tickets should still sell-out; however, football tickets sales might fall somewhat with an increase in price, but the drop would be dwarfed by the normal variation in attendance due to the weather, opponents, and how well the team is doing.

Tax on movies

We estimate a tax yield of about \$60,000 per 1% additional tax on movie tickets. The current state tax is 1%, plus a local tax of nominal value. If a "maximum reasonable" tax rate is considered to be 10% (some jurisdictions in neighboring Virginia have this rate) then Durham County could raise an additional \$540,000 by increasing the tax with their own levy of 9%.

Tax on other amusements

For all amusements in this NAICS category, we estimate about \$195,000 yield per 1% additional tax. The current state tax is 3%, plus a minimal local tax. Again, if a "maximum reasonable" tax rate is considered to be 10% (some jurisdictions in neighboring Virginia have this rate) then Durham County could possibly raise an additional \$1,365,000 by increasing the tax with their own levy of 7%.

Other jurisdictions

In comparison to other jurisdictions, the tax rate on amusement admissions in North Carolina is low, although several states do not levy a tax on amusement admissions and some also prohibit local governments from imposing a tax. Many jurisdictions that tax amusement admissions do so by imposing their regular sales tax on amusement admissions, while some states establish an admissions or amusement tax equal to their sales tax. Among similar cities surveyed, the tax rate in Durham is the lowest rate where a tax is collected.

Figure III-12

Taxes on Amusement Admissions, Selected Jurisdictions

Jurisdiction	Tax on Amusements
Akron, OH	None
Austin, TX	State Sales Tax 6.25% + Local Sales Tax 2% = 8.25%
Birmingham, AL	State Sales Tax 4% + Local Sales Tax 1% = 5%
Boise, ID	State Sales Tax 6% only
Columbia, SC	5%
Des Moines, IA	State Sales Tax 4% + Local Sales Tax 1% = 5%
Durham, NC	1% on Movie Theatres, 3% on other amusements, small local fixed fees
Ft. Lauderdale, FL	6% Sales Tax only, College Sports exempt
Grand Rapids, MI	None
Jackson, MS	7% Sales Tax only
Lansing, MI	None
Little Rock, AR	6.625% Sales Tax + 2% Tourism Tax (tourist activities, does not including movies or sports)
Madison, WI	State Sales Tax 5% + Local Sales Tax .5% = 5.5%
Mobile, AL	State Sales Tax 4% + Local Sales Tax 4% = 8%
Montgomery, AL	State Sales Tax 4% + Local Sales Tax 3.5% = 7.5%
Newport News, VA	7.50%
Ontario, CA	None
Orlando, FL	6.5% Sales Tax only, College Sports exempt
Providence, RI	None
Reno, NV	None
Richmond, VA	6%
Rochester, NY	4.25% State Sales Tax + 4% Local Sales Tax = 8.25%
Savannah, GA	State Sales Tax 4% + Local sales Tax 2% = 6%
Spokane, WA	5%, except 2% on Golf, 4% on driving ranges, 3% on swimming pools and skating rinks
Tampa, FL	7% Sales Tax only, College Sports, NFL Playoffs exempt

Most taxes inflict some damage on their tax base, and amusement and admissions taxes are no exception. At a minimum, imposing a tax is akin to raising prices, and will create a burden both on the businesses/activities, which will experience lower sales, and on the ticket purchasers, who will reduce their purchases to some extent. A reasonable rule of thumb is that a tax which raises the price of admissions by 5% will cause about a 3% reduction in sales. There really is no free lunch, and policymakers would do well to understand that if a tax is imposed, it makes sense to spend some of it on promotions to protect and enhance the tax activity.