Principles of Sales Taxation

Deciding what to tax, or not to tax, under the sales tax requires balancing considerations of sound tax policy, administrative capability, equity, economic realities and revenue needs. Policy considerations of things to avoid or encourage relevant to the evaluation of sales tax exemptions and exclusions include:

- Avoid economic distortions created by taxing intermediate sales. The sales tax is designed to be a tax on final sales – the acquisition of goods and services for personal consumption. Taxing intermediate sales:
    - Causes tax policy to overly impact economic decision-making.
    - Creates an artificial incentive for vertical integration of business.
    - Causes tax pyramiding, in which the multiple layers of taxation inflate the price of goods or services.
    - Makes taxes less transparent to the ultimate purchasers of the item.

- Avoid adverse economic consequences.
    - To the extent Texas tax policy is more aggressive, Texas businesses and consumers are at a disadvantage to those in other states.
    - Taxing business inputs and expenses increases the cost of doing business in Texas and discourages capital investment.

- Avoid adverse economic consequences for individuals.
    - Sales taxes tend to be regressive because those of lower income spend a larger portion of total income on consumption.
    - Regressivity is lessened by excluding purchases of essential items (such as food and drugs) from the tax base.

- Facilitate efficient administration and vendor compliance.
    - Avoid undue administrative difficulty for the state and unreasonable compliance costs for vendors who collect the tax.
    - Provide uniform taxation of a particular good or service.

- Create a stable revenue stream, but not at the expense of good tax policy.
    - An existing exemption should not be eliminated simply because doing so would produce a certain amount of additional revenue. Making tax policy by spreadsheet may create unforeseen consequences.

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