

*City of Alexandria, Virginia*

MEMORANDUM

DATE: FEBRUARY 29, 2008

TO: THE HONORABLE MAYOR AND MEMBERS OF CITY COUNCIL

FROM: JAMES K. HARTMANN, CITY MANAGER *J*

SUBJECT: BUDGET MEMO # 16 : RESTAURANT MEALS TAX

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**I. Background**

This memo provides additional detail regarding the City’s tax on restaurant meals. The restaurant meals tax rate in Alexandria is currently 3% and is expected to generate \$11.1 million in revenue. An increase in the meals tax by 0.5% to 3.5% would be expected to generate an additional \$1.85 million. An increase in the meals tax by 1.0% to 4.0% would be expected to generate an additional \$3.7 million in revenues.

Restaurant meals are defined generally in State Code (58.1-3833) and more specifically in City Code (Article N Section 3-2-341) as “any prepared food or beverage offered or held out for sale by a restaurant for the purpose of being consumed by any person to satisfy the appetite and which is ready for immediate consumption.” For detailed information regarding the City’s definition of prepared food, see Appendix I. Exemptions include meals served by public or nonprofit day care centers, elementary or secondary schools, or colleges and universities to their students or employees.

**II. Comparative Information**

**Table I** breaks out the tax rate by neighboring jurisdictions. It includes the sales tax which is assessed on restaurant food and beverages in all the jurisdictions. Due to state law restrictions, the counties of Fairfax, Loudoun, and Prince William are unable to levy the tax without a favorable referendum. Arlington County does have a meals tax and State law had a special exception that allowed it to levy a meals tax without a referendum. The State of Maryland does not allow local jurisdictions to levy a meals tax, with the exception of Ocean City. Virginia law allows cities and some select counties to adopt local meals tax by ordinance and 39 Virginia cities and 39 Virginia counties have a restaurant meals tax.

**Table I. Comparative Meals Tax Rates Among Jurisdictions**

Jurisdiction	Local Meals Tax	Total Sales Tax	Total Tax
Alexandria City	3%	5%	8%
Arlington County	4%	5%	9%
Fairfax City	4%	5%	9%
Fairfax County	NA	5%	5%
Falls Church City	4%	5%	9%
Loudoun County	NA	5%	5%
Manassas City	4%	5%	9%
Manassas Park	4%	5%	9%
Prince William County	NA	5%	5%
Washington, DC	10%	NA	10%
Montgomery County	NA	5%	5%
Prince George's County	NA	5%	5%

**Policy Implications**

Typically, restaurants will oppose increases to restaurant meals taxes. This is evidenced in Fairfax County's failed meals tax referendum in 1992. The National Restaurant Association's (NRA) website ([www.restaurant.org](http://www.restaurant.org)) details some of the reasons why. The NRA believes it unfairly shifts the tax burden to restaurants instead of having the burden shared equally among all sellers of goods and services, including grocery stores. In addition, the NRA believes that meals tax increases will significantly impact restaurants on the border with other local jurisdictions by driving customers to other jurisdictions with lower rates. Also, they suggest that most patrons who utilize restaurants are not tourists and that such taxes have a disproportionate impact on the residents of the affected City.

Staff has been unable to find any on point research detailing the effect of meals tax increases on restaurant business, even after contacting the National Restaurant Association directly. Staff believes that restaurant demand is relatively inelastic and that an additional tax of 0.5% or 1.0% in Alexandria will make little difference to customers deciding where to eat. When consumers choose which restaurant to dine at, the choice is usually based on a number of factors such as distance from one's home, perceived quality of the food, and atmosphere of the restaurant, food type or genre, and the general price range of the restaurant. The differential in the total tax applied to restaurant meals is almost never a factor in choosing a restaurant. When one chooses to dine out, one is making an uneconomic decision in that eating out is nearly always more expensive than eating a similar meal at home. When Arlington County adopted its meal tax in 1991, meals tax revenues increased in the following fiscal year.

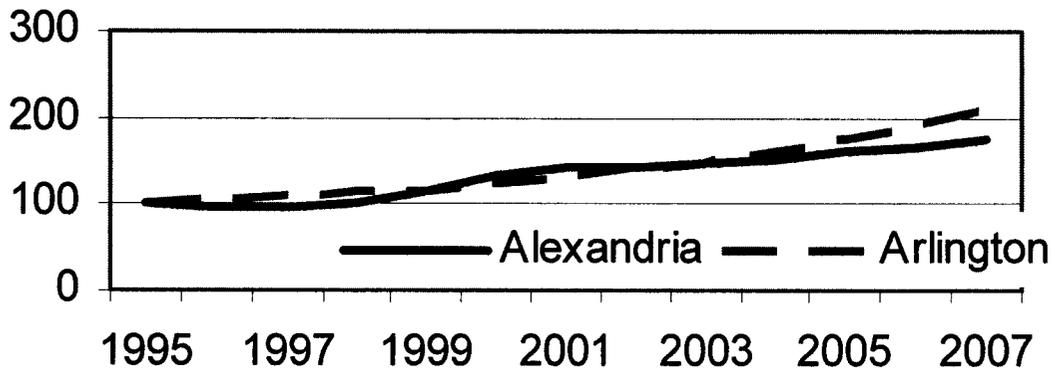
In response to the NRA point on the "border" issue, it does not appear that is a significant issue as many cities in Virginia (such as Fairfax City) that have long had a restaurant meals tax are surrounded by counties that do not have such a tax. Staff notes that the City's neighboring jurisdictions of Arlington and Washington, D.C. have higher tax rates on restaurant food of 9%

and 10%, respectively, including sales tax. The rates in Fairfax and Prince George County are lower, at 5%.

The NRA articulated issue of the restaurant meals tax impacting residents more than tourists and business travelers is true for many jurisdictions. Insofar as Alexandria is a magnet for tourists and business travelers, a substantial percentage of the City's meals tax is likely to come from non-residents.

The indexed graph below shows that meals tax revenues from Arlington have risen at a slightly faster pace than Alexandria's since 1995 so the higher tax rate has not prevented Arlington's restaurant industry from thriving.

### A Cross-Jurisdictional Comparison Transient Lodging (1995=100)



Revenues from the meals tax have risen consistently over the last fifteen years. Table I from the budget text 7-34 shows the average annual real and nominal increases to meals tax revenues from 1992-2007.

**Table II. Average annual increases to Restaurant Meals tax revenues**

	5 years	10 years	15 years
Nominal Increase	4.5%	6.1%	6.5%
Inflation adjusted increase	1.5%	3.4%	3.7%

### Appendix I. Exemptions from the City's Restaurant Meals Tax

Sec. 3-2-246 Exemptions; limitations on application.

The tax imposed under this article shall not be levied on the following:

- (1) Meals furnished by restaurants to employees of the restaurant in the course of or in connection with their employment when no charge is made to the employees.
- (2) Meals purchased with food coupons issued by the United States Department of Agriculture under the Food Stamp Program or drafts issued through the Virginia Special Supplemental Food Program for Women, Infants, and Children.
- (3) Meals sold by public or nonprofit (a) day care centers, (b) elementary or secondary schools, or (c) colleges or universities, to their students or employees.
- (4) Meals for use or consumption and which are paid for directly by the Commonwealth, any political subdivision of the Commonwealth or the United States.
- (5) The following items, as more particularly described in the Food Stamp Act of 1977, 7 U.S.C. § 2012, as amended, and federal regulations adopted pursuant to that act:
  - (a) except as provided in subsection 3-2-241(2), any food or food product for home consumption;
  - (b) in the case of persons who are 60 years of age or over, persons who receive supplemental security income benefits, disabled persons, or blind persons, and their spouses, meals prepared by and served in senior citizens' centers and other facilities which serve such persons;
  - (c) in the case of persons who are 60 years of age or over, persons who are physically or mentally handicapped or disabled, or persons who are otherwise so disabled they are unable adequately to prepare all of their meals, and their spouses, meals prepared for and delivered to such persons at their home by a public or private nonprofit organization or by a private establishment under contract with the appropriate government agency to perform such services;
  - (d) in the case of narcotics addicts or alcoholics, and their children, served by drug addiction or alcoholic treatment and rehabilitation programs, meals prepared and served under such programs;
  - (e) in the case of persons who are residents in certain public or private nonprofit group living arrangements, meals prepared and served under such arrangements;
  - (f) in the case of women and children temporarily residing in public or private nonprofit shelters for battered women and children, meals prepared and served by such shelters; and
  - (g) in the case of homeless persons, meals prepared for and served by a public or private nonprofit establishment (approved by an appropriate government agency) that feeds such persons or by a private establishment under contract with an appropriate government agency to offer meals for such persons.
- (6) Alcoholic beverages sold in factory sealed containers and purchased for off-premises consumption.
- (7) Food and beverages sold through vending machines. (Code 1963, Sec. 36-102; Ord. No. 4133, 5/13/00, Sec. 4)