

Department of Legislative Services
 Maryland General Assembly
 2002 Session

FISCAL NOTE

Senate Bill 520 (Senator Kasemeyer, *et al.*)
 Budget and Taxation

Sales and Use Tax - Back-to-School Tax-Free Week

This bill provides that during the week of August 16, 2002 through August 22, 2002, the sales and use tax will not apply to the sale of school supplies or clothing or footwear (excluding accessories) if the taxable price of the individual items is less than \$101.

The bill takes effect July 1, 2002.

Fiscal Summary

State Effect: Sales tax revenues (general funds) could decline by \$9.4 million in FY 2003. General fund expenditures by the Comptroller's Office to administer the program would increase by approximately \$88,500 in FY 2003.

(in dollars)	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
GF Revenue	(\$9,400,000)	\$0	\$0	\$0	\$0
GF Expenditure	88,500	0	0	0	0
Net Effect	(\$9,488,500)	\$0	\$0	\$0	\$0

Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: None.

Small Business Effect: Potential meaningful impact from increased sales (offset by administrative costs) for small businesses selling apparel and/or school supplies.

Analysis

Bill Summary: School supplies are defined to include pens, pencils, erasers, crayons, notebooks, notebook filler paper, legal pads, composition books, poster paper, scissors, cellophane tape, glue, paste, rulers, protractors, compasses, backpacks, bookbags, and calculators.

Current Law: Current law does not provide for any sales tax holiday or tax-free week. Chapter 576 of 2000, which created a tax-free week for clothing and footwear, applied only to a specified week in 2001.

Background: Chapter 576 of 2000 exempted from the sales and use tax the sale of clothing or footwear (except accessories) for the week of August 10 through August 16, 2001, if the taxable price of the item of clothing or footwear was less than \$100. The Comptroller's Office estimates that the tax-free week resulted in lost sales tax revenue of \$5.1 million. This estimate is based on regression analysis of historical sales tax collection trends in the categories of vendors (apparel stores, department stores, etc.) that sell a large share of the exempted clothing and footwear. The Comptroller's Office cannot provide a more precise estimate because the agency does not collect sales tax data by the type of good sold, nor does it collect the total value of taxable transactions for those vendors who file returns electronically.

In its *Assessment of Maryland's Tax-free Week*, the Comptroller's Office reports that sales tax collections from the categories of vendors most likely to sell exempted items declined by 5.2% for the month including the tax-free week, versus the same month in 2000. The agency estimates that the majority of this decline is associated with the exemption rather than nationwide or other economic factors. The agency estimates that total apparel sales likely increased by 2.6% during the period. The agency estimates that most of any increase in sales of non-exempted goods would have occurred in any event, and hence that fiscal impact is minimal. Finally, any impact on income tax revenues from the tax-free week is difficult to estimate but expected to be minimal.

Several other states have recently initiated one-time or ongoing sales tax holidays.

<u>State</u>	<u>Days</u>	<u>Items Included</u>	<u>Maximum Cost</u>
New York (1)	See ⁽¹⁾	clothing	\$500 / \$110
Florida	9	clothing/accessories	\$100
Texas	3	clothing/footwear	\$100
Connecticut	7	clothing/footwear	\$300
South Carolina	3	clothing, computers, supplies	N/A
Pennsylvania	14	computers	N/A
Iowa	2	clothing/footwear	\$100
District of Columbia	10	clothing/footwear, school supplies	\$101

⁽¹⁾ New York had two sales tax holidays; one was for clothing only, while the other was for both clothing and footwear. New York's holiday has since become a permanent exemption for items priced under \$110.

State Revenues: It is estimated that sales tax revenues would decline by approximately \$5.3 million in fiscal 2003 due to the exemption for clothing and footwear. This estimate is based on the \$5.1 million estimate of sales tax losses from the prior tax-free week, adjusted for 2.6% growth in the consumer portion of sales tax projections and a minimal revenue loss increase due to the change in the tax-free limit from \$100 to \$101. It is estimated that sales tax revenues would decline by approximately \$4.1 million in fiscal 2003 due to the exemption for school supplies based on: (1) an examination of the sales of the categories of Maryland vendors that sell items that could be exempt under the "school supply" exemption; (2) assumptions regarding the amount of sales that is diverted from taxable weeks to the tax-free week; and (3) the percentage of vendors' sales that would be subject to the exemption. In total, it is assumed that State sales tax revenues would decline by \$9.4 million as a result of the exemption.

State Expenditures: The Comptroller's Office would incur approximately \$88,500 in administrative expenses to implement the tax-free week. This estimate is based on the approximately \$100,000 that the agency incurred implementing the prior tax-free week, less certain computer programming that can be reused from the prior initiative. Future year expenditures are forecasted to grow at approximately 1% per year. In addition, the agency advises that the substantial amount of work involved in the first tax-free week diverted some staff from audit activities. For this bill the agency advises that staff diversion may result in up to \$100,000 in lost tax revenues from the loss of one-half of an auditor's time. The Comptroller's Office also notes that there may be additional

administrative expenditures to educate vendors that the exemption applies to items priced less than \$101 this year, versus \$100 last year.

Small Business Effect: According to the 1998 Survey of U.S. Business by the U.S. Census Department, 91.7% of the retail firms in Maryland had less than 50 employees. This bill could cause a net increase in sales for small businesses to the extent that sales would be made in Maryland during the period that would otherwise have been made out-of-state, through the Internet, or by mail order. Small businesses located in shopping malls or other areas with a number of stores in close proximity may experience increased sales for nonapparel and/or non-school supply items because of increased foot traffic due to the tax-free week. On the other hand, compliance costs for small businesses could increase, if changes to cash register programming and accounting systems are required. The net effect would vary from business to business, but it is likely to be positive.

Additional Information

Prior Introductions: None. See discussion of Chapter 576 of 2000 above.

Cross File: None.

Information Source(s): Comptroller's Office, Department of Legislative Services

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lc/jr

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