SB 17

Department of Legislative Services
Maryland General Assembly
2002 Session

FISCAL NOTE

Senate Bill 17 (Senator Hafer)
Budget and Taxation

Sales and Use Tax - Higher Education Supplies

This bill designates one week annually during which the sales and use tax would not apply to the sale of any textbook or "class supply," if the taxable price of the textbook does not exceed $150, or the taxable price of the class supply does not exceed $100.

The bill takes effect July 1, 2002.

Fiscal Summary

State Effect: State sales tax revenues (general funds) could decline by $5.2 million in FY 2003 based on current student spending patterns. Revenue losses could be significantly higher if average exempted spending per student increases by displacing taxable sales. Future year revenue losses reflect projected increases in higher education expenses. General fund expenditures by the Comptroller's Office to administer the program would increase by approximately $88,500 in FY 2003 increasing by approximately 1% per year thereafter.

(in dollars)	FY 2003	FY 2004	FY 2005	FY 2006	FY 2007
GF Revenue	($5,200,000)	($5,460,000)	($5,733,000)	($6,019,700)	($6,320,600)
GF Expenditure	88,500	89,400	90,300	91,200	92,100
Net Effect	($5,288,500)	($5,549,400)	($5,823,300)	($6,110,900)	($6,412,700)

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 textbooks or class supplies.

Analysis

Bill Summary: The exemption period applies beginning on the last Thursday in August and ending on the first Wednesday in September each year. Class supplies are defined to include items other than textbooks used to complete work for a class offered at an institution of higher education, an institution of postsecondary education, or a private career school. Electronic equipment would not qualify as class supplies.

Current Law: The above items are currently subject to the 5% sales and use tax. Current law does not provide for any sales tax holiday or tax-free week.

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.

State	Days	Items Included	Maximum Cost
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 $5.2 million in fiscal 2003 due to the exemption.

While it is not explicitly specified in the bill, the Comptroller's Office contemplates adoption of regulations limiting the exemption to sales to enrolled higher education students by requiring the purchaser to show a valid school-issued ID card. Even so, the exemption is drafted broadly and could include virtually every type of office supply and items as varied as test tubes, video tapes, lab coats, software, and paint brushes as well as textbooks.

Most universities in the State advise students to budget about $750 per year for books and course supplies, although the amounts can vary widely depending on the course level, institution, and course type. Although the tax exemption provided in the bill is only applicable for the fall term, it is assumed that each student will spend about $400 during the exemption period each year as some books and supplies (e.g. notebooks) can be purchased in advance. According to the Maryland Higher Education Commission, there are approximately 260,000 students enrolled in Maryland institutions, including students in private career schools, who could take advantage of this exemption.

Under these assumptions, the estimated annual reduction in State revenues would be approximately $5.2 million. This amount could be substantially higher in the event that persons with student ID cards do not properly segregate items used for classes from those used for other purposes (preventing retailers from properly collecting the sales and use taxes) or otherwise increase their purchases of exempt goods. Future year revenue losses are forecasted to grow at 5% based on historical growth in higher educational expenses.

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.

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 non-exempt 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. Under this bill, retailers would be required to determine both whether the good itself is exempt, and whether the purchaser is exempt. The net effect would vary from business to business, but it is likely to be positive.

Additional Information

Prior Introductions: None.

Cross File: None.

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

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