

Department of Legislative Services
Maryland General Assembly
2005 Session

FISCAL AND POLICY NOTE
Revised

Senate Bill 599

(Senator Gladden, *et al.*)

Budget and Taxation

Ways and Means

Sales and Use Tax - Tax-Free Period for Back-to-School Shopping

This bill exempts from the State sales and use tax the sale of clothing or footwear (except accessories) for the period of August 23 through August 27, 2006, if the taxable price of the item of clothing or footwear is \$100 or less.

The bill takes effect July 1, 2005.

Fiscal Summary

State Effect: General fund revenues could decrease by \$5.5 million in FY 2007. General fund expenditures for the Comptroller's Office to administer the program would increase by approximately \$95,600 in FY 2007.

(\$ in millions)	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
GF Revenue	\$0	(\$5.5)	\$0	\$0	\$0
GF Expenditure	0	.1	0	0	0
Net Effect	\$0	(\$5.6)	\$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 clothing and footwear.

Analysis

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

Background: The sales and use tax is the State's second largest source of general fund revenues accounting for approximately \$3.2 billion in fiscal 2006. The Maryland sales and use tax rate is currently set at 5.0%.

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 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 believes 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 and that most of the increase would have occurred in any event, and hence any offsetting revenue increase was minimal. The agency reports that any impact on income tax revenues is difficult to estimate but expected to be minimal.

State Revenues: The bill exempts purchases of eligible clothing and footwear from the State sales and use tax for a five-day period from August 23, 2006 through August 27, 2006. It is estimated that sales tax revenues would decrease by approximately \$5.5 million in fiscal 2007 due to the five-day tax-free period, based on the following assumptions:

- the \$5.1 million impact from the 2001 tax-free week;
- an assumption that the equivalent of six days of sales would occur during the five-day tax-free period; and
- the consumer portion of sales tax revenue is projected to increase by 26.4% from fiscal 2002 to fiscal 2007, as estimated by the Bureau of Revenue Estimates.

State Expenditures: The Comptroller's Office would incur approximately \$95,600 in administrative expenses to implement the tax-free period in fiscal 2007. This estimate is

based on the \$102,400 that the agency incurred implementing the prior tax-free week, less certain computer programming that can be reused from the prior initiative. In addition, the agency advises that the substantial amount of work involved in the first tax-free week diverted some staff from audit activities. There could be a decline in audit revenues from such a diversion.

Small Business Effect: According to the 1998 *Survey of U.S. Business* by the U.S. Census Bureau, 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 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: This bill was introduced as HB 900 in the 2004 session. No action was taken by the House Ways and Means Committee. HB 37 of 2003 would have exempted statewide specified clothing and footwear from the sales tax for a set period of time. No action was taken by the House Ways and Means Committee.

Cross File: HB 37 (Delegate Cryor, *et al.*) – Ways and Means.

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

Fiscal Note History: First Reader - February 10, 2005
ncs/hlb Revised - Senate Third Reader - April 7, 2005

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