

Department of Legislative Services  
 Maryland General Assembly  
 2008 Session

**FISCAL AND POLICY NOTE**

House Bill 65 (Delegate Smigiel)  
 Ways and Means

**Sales and Use Tax - Exemption - Clothing**

This bill exempts the sale of any item of clothing from the sales and use tax.

The bill takes effect June 1, 2008.

**Fiscal Summary**

**State Effect:** General fund revenues would decrease by \$29.4 million in FY 2008, reflecting the bill's June 1 effective date. General fund revenues would decrease by \$344.2 million and Transportation Trust Fund (TTF) revenues would decrease by \$23.9 million in FY 2009. Future year revenue losses are based on projected sales tax revenue growth.

(\$ in millions)	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
GF Revenue	(\$29.4)	(\$344.2)	(\$361.4)	(\$379.5)	(\$398.5)
SF Revenue	0	(23.9)	(25.1)	(26.4)	(27.7)
Expenditure	\$0	\$0	\$0	\$0	\$0
Net Effect	(\$29.4)	(\$368.1)	(\$386.6)	(\$405.9)	(\$426.2)

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

**Local Effect:** None.

**Small Business Effect:** Potential meaningful.

## Analysis

**Current Law:** With enactment of Chapter 6 (HB 5) of the 2007 special session, clothing and footwear are taxable at the rate of 6% (effective January 3, 2008). In addition, Chapter 6 provides for an annual sales tax-free period for clothing and footwear costing less than \$100 beginning in fiscal 2011.

**Background:** The sales and use tax is the State's second largest source of general fund revenue accounting for \$3.7 billion in fiscal 2008 and \$4.3 billion in fiscal 2009, according to the most recent revenue forecast. **Exhibit 1** shows the sales and use tax rates in surrounding states. As noted in the exhibit, Delaware and Pennsylvania do not impose a sales tax on clothing.

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### Exhibit 1 Sales and Use Tax Rates in Maryland and Surrounding States

Delaware	0%
District of Columbia	5.75%
Maryland	6%
Pennsylvania	6% plus 1% in certain local jurisdictions 0% sales tax on clothing
Virginia	5%, includes 1% for local jurisdictions
West Virginia	6%

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**State Revenues:** Total sales tax revenues would decrease by \$29.4 million in fiscal 2008 accounting for the bill's June 1, 2008 effective date and by \$368.1 million in fiscal 2009. In addition to increasing the sales and use tax rate from 5% to 6%, Chapter 6 of the 2007 special session also altered the distribution of sales and use tax revenues by requiring that 6.5% of revenues, after specified distributions, be diverted to the TTF beginning July 1, 2008. As a result, the clothing exemption proposed by the bill would reduce general fund revenues by \$29.4 million in fiscal 2008 and \$344.2 million in fiscal 2009 while reducing TTF revenues by \$23.9 million in fiscal 2009. The estimate is based on the following facts and assumptions:

- \$168.2 million in sales tax collections in fiscal 2007 were classified as apparel by the Comptroller's Office; it is estimated that 85% of this amount would qualify for the exemption.

- \$613.3 million in sales tax collections in fiscal 2007 were classified as general merchandise by the Comptroller's Office; it is estimated that 23% of this amount would qualify for the exemption.
- Sales tax revenues are projected to increase by approximately 5% annually, per the current revenue forecast.

To the extent that taxable sales, as part of the same transaction as tax-free sales, would be made in Maryland that would otherwise have been made out-of-state, through the Internet, or by mail order, total sales tax revenues would increase, mitigating the revenue loss described above. Also, businesses would become more profitable and income tax revenues could increase. The amount of either such increase cannot be reliably estimated at this time.

**Small Business Effect:** This bill could cause a net increase in sales for small businesses, to the extent that sales would be made in Maryland that would otherwise have been made out-of-state, through the Internet, or by mail order. Small businesses located near Delaware and Pennsylvania (which do not tax clothing and footwear) may experience increased sales that are currently displaced to those states.

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### **Additional Information**

**Prior Introductions:** This bill was introduced as HB 40 in the 2007 special session. No action was taken by the House Ways and Means Committee.

**Cross File:** None.

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

**Fiscal Note History:** First Reader - January 24, 2008  
mcp/hlb

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