

DEPARTMENT OF TAXATION

2002 Fiscal Impact Statement

1. **Patron** Potts

Revised
2. **Bill Number** SB 346

3. **Committee** Senate Finance

House of Origin:

 X **Introduced**

 Substitute

 Engrossed

4. **Title** Retail Sales and Use Tax: Annual
Exemption for Clothing, Footwear, and
School Supplies

Second House:

 In Committee

 Substitute

 Enrolled

5. **Summary/Purpose:**

This bill would provide a temporary exemption from the state sales and use tax for certain items of tangible personal property. The exemption would occur on an annual basis, beginning in 2002, and would be in effect for a three-day period beginning on the third Friday in August and continuing through the third Sunday in August. The exemption would apply on a per item basis to:

- clothing and footwear costing less than \$100, and
- school supplies, including pens and pencils costing less than \$8 each, and calculators costing less than \$25 each.

This bill defines the qualifying items and requires the Department of Taxation to promulgate regulations implementing the annual exemption on or before July 15, 2002.

This bill would not affect the imposition of the local sales and use tax.

6. **Fiscal Impact Estimates are:** Tentative. (See Line 8.)

6a. **Expenditure Impact:**

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Positions</i>	<i>Fund</i>
2001-02	\$0	0	GF
2002-03	\$79,200	0	GF
2003-04	\$79,200	0	GF

6b. Revenue Impact:

<i>Fiscal Year</i>	<i>Dollars</i>	<i>Fund</i>
2002-03	(\$3.2 million)	GF
2002-03	(\$0.5 million)	TTF
2003-04	(\$3.4 million)	GF
2003-04	(\$0.6 million)	TTF

7. Budget amendment necessary: Yes.

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8. Fiscal implications:

Expenditure Impact

This bill would result in administrative costs to the department of \$79,200 in fiscal year 2003 and beyond. These costs are associated with personnel, printing, and postage charges to educate dealers about the provisions of this bill.

Revenue Impact

This bill would affect: (1) revenues dedicated to the General Fund for unrestricted use by the Commonwealth, (2) revenues returned to the localities for educational purposes, and (3) the Transportation Trust Fund revenues. This bill would not affect the 1% local option sales tax revenues.

The negative revenue impact for this bill is estimated to be \$3.7 million in fiscal year 2003 and \$4.0 million in fiscal year 2004. The revenue estimate incorporates data from the U.S. Census and taxable sales reported to the department. The Census data is organized by merchandise line sales, which takes into account sales of a given type of merchandise regardless of store type, i.e., sales in department stores are counted, as well as sales at specialty clothing and footwear stores. The data from both sources is grown into the future for the appropriate number of years using historic and forecasted growth rates for sale and use tax collections.

The cost restrictions provided in this bill are assumed to be immaterial for purposes of computing the revenue estimates.

Additionally, the estimates assume a 63% increase in sales during the exemption period attributable to the exemption itself. This percentage represents an average of the increase in sales for New York, Pennsylvania, and Iowa (which are other states with "sales tax holidays"). The experience of New York suggests that the majority of the sales

increase is attributable to taxpayers shifting their purchases into the “tax-free” time period to take advantage of the exemption. New York analyzed sales

during the temporary exemption periods and sales during the quarters when the exemption periods occurred. This analysis found that, while sales increased during a “tax-free” time period, overall sales did not increase during the quarterly period when other factors, such as growth in sales nationally, were taken into consideration.

9. Specific agency or political subdivisions affected:

Department of Taxation

10. Technical amendment necessary: None.

11. Other comments:

This bill would provide an annual exemption from the state sales and use tax for certain items of tangible personal property. Beginning in 2002, the exemption would be effective from the third Friday in August through the third Sunday in August and for the same time period each year. The time period and provisions of the exemption suggest that this bill is intended to primarily benefit purchasers of back-to-school items. The exemption would apply to the qualifying items when purchased by individuals and businesses.

The bill defines the qualifying items to include the following.

“Clothing and footwear”: Any article of apparel to be worn by human beings including fabric, thread, yarn, buttons, snaps, hooks, zippers and like items that are used to make or repair such clothing. The definition does not include watches, jewelry, handbags, handkerchiefs, umbrellas, scarves, ties, headbands, belt buckles, costumes, or rented formal wear as articles of wearing apparel. The definition also excludes items constructed from pearls, precious or semi-precious stones, jewels or metals, or imitations thereof.

“School supplies”: Pens and pencils costing less than \$8 each, ink and refills for pens and pencils, color markers, crayons, color pencils, notebook paper, typing paper, computer paper, construction paper, spiral and ring notebooks, composition notebooks, erasers, folders, book covers, rulers, compasses, pen cases and boxes, pencil cases and boxes, lunch boxes, and calculators costing less than \$25 each.*

* The Department of Taxation would assume that the \$25 cost limitation applies to calculators only in the definition of school supplies.

This bill would not affect the imposition of the local sales and use tax. Therefore, purchasers would pay a reduced sales and use tax of 1% on their purchases of clothing, footwear, and school supplies during the exemption period.

Impact on Dealers

Dealers who make sales of tangible personal property would be required to reprogram their computerized cash registers for a three-day period to account for the annual exemption period. Smaller retailers with less sophisticated systems may be unable to reprogram their registers to accommodate the exemption period.

Additionally, retailers may incur significant expenses for hiring and training staff to administer the exemption.

Other States

The other states that provide or have recently provided a “sales tax holiday” exemption from the sales and use tax are New York, Florida, Texas, Connecticut, South Carolina, Pennsylvania, Iowa, Maryland, and the District of Columbia.

New York: New York provided an exemption for clothing and footwear for seven-day periods each in January and September over a period of three years. New York now has a permanent exemption for clothing and footwear priced at \$110 or less per item.

Florida: Florida provides an annual exemption for clothing, footwear, and accessories priced at \$100 or less. Effective in 2001, school supplies costing \$10 or less per item qualify for exemption. The exemption does not apply to sales of the qualifying items at theme parks, entertainment complexes, public lodging establishments, and airports.

Texas: Beginning in 1999, Texas provides an annual exemption for clothing and footwear priced at \$100 or less per item. The exemption is effective during the first weekend in August.

Connecticut: Connecticut provides a permanent exemption for clothing and footwear priced at \$75 or less. To take advantage of the “sales tax holiday” idea, Connecticut now provides an annual, expanded exemption for seven days in August for items priced at \$300 or less.

Pennsylvania: Pennsylvania also provides a permanent exemption for clothing and footwear and chose a different approach by providing a one-time exemption for computer products for personal use. The exemption was effective for eight days each in February and August of 2000. This exemption was allowed again in 2001.

South Carolina: South Carolina provides a three-day exemption that occurs on an annual basis. The exemption is broader than the other states offering such exemptions. The exemption applies to “back-to-school” items that include clothing, clothing

accessories, footwear, school supplies, and computer equipment and software. There is no price limitation on the qualifying items.

Iowa: Effective in 2000, Iowa provided a temporary exemption for clothing and footwear priced at \$100 or less per item. The exemption was a one-time event effective for two days in August.

Maryland: The Maryland legislature approved a one-time exemption effective for seven days in August 2001. The exemption applied to clothing and footwear priced at \$100 or less.

District of Columbia: The District adopted a one-time sales tax holiday effective for ten days in August 2001 that was contingent upon certified revenue growth projections. The exemption took place from August 3 through August 12 and applied to school supplies and clothing priced at \$100 or less.

Other Legislation

The following bills would provide a similar exemption for certain qualifying items such as school supplies, clothing, footwear, and computer products: HB 31, HB 1026, and SB 529. SB 506 would provide an annual exemption for any item or article of tangible personal property.

cc: Secretary of Finance

Date: 01/16/02/GRM

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