



**House
Legislative
Analysis
Section**

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**TAX HOLIDAY FOR CLOTHING:
TWO WEEKS AROUND LABOR DAY**

**House Bill 4862 (Substitute H-5)
Sponsor: Rep. Nancy Cassis**

**House Bill 5665 (Substitute H-2)
Sponsor: Rep. Sandra Caul**

**Committee: Tax Policy
First Analysis (5-11-00)**

THE APPARENT PROBLEM:

State tax collections continue to be extraordinarily robust, exceeding expectations. Personal income and consumer spending continue to rise. With a budget surplus in the offing, it makes sense to reduce the burden on Michigan taxpayers. One proposal is to provide a "sales tax holiday" on clothing and footwear each year during a specified time period. Several other states have adopted this practice (beginning with New York in 1997) and retailers say that it boosts sales. A number of proposals have been introduced on this topic, including one that would create a two-week sales tax holiday around Labor Day, during the closing days of the summer tourist season and the traditional back to school shopping season.

THE CONTENT OF THE BILLS:

House Bill 4862 would amend the General Sales Tax Act (MCL 205.54x) to exempt clothing and footwear from the sales tax during the period of seven days before Labor Day and seven days after Labor Day. The exemption would apply to an article of clothing or footwear with a purchase price of \$150 or less to be worn on an individual. It would not apply to jewelry or to accessories, other than belts, neckwear, and head scarves. House Bill 5665 would amend the Use Tax Act (MCL 205.94t) in the same way.

The state treasurer would be required on December 31 of each year to estimate the amount of sales tax and use tax that was not collected because of the exemption and transfer from the general fund to the state school aid fund the amount that would otherwise have gone to the state school aid fund. A similar provision would apply to sales tax revenues that would otherwise have gone to revenue sharing for local governments.

The Department of Treasury would be required to post information on the state Internet website regarding the exemptions.

BACKGROUND INFORMATION:

New York, Texas, and Florida conducted sales tax holidays or moratoriums on clothing during 1999, according to a recent Arthur Andersen study prepared for the National Retail Federation. New York had two one-week holidays, one during the back to school season and one in January. The exemption there applied to items under \$500. Florida's program applied to nine days (covering two weekends) during the back to school period and three days in January and had a \$100 limit. In Texas, the program covered three days in back to school season with a \$100 limit. Florida's law provides an annual sales tax moratorium for the same three days. The other two states apparently provide the sales tax moratorium for specific periods each year (e.g., September 1-7, 1999 and January 15-21, 2000, in New York). The states differ as to what items they allow to be exempt. As of March 1, 2000, New York will exempt clothing and footwear items under \$110 on a permanent basis, year-round. According to the Andersen report, seven states provide a full or limited sales tax exemption for clothing and footwear: Connecticut, Massachusetts, Minnesota, New Jersey, Pennsylvania, Rhode Island, and Vermont. Five states reportedly have no broad-based sales tax: Alaska, Delaware, Montana, New Hampshire, and Oregon.

FISCAL IMPLICATIONS:

The House Fiscal Agency reports that sales tax revenue would be reduced by somewhere between \$22 million and \$27 million annually. The agency reports that there is insufficient data to determine the impact on use

House Bills 4862 and 5665 (5-11-00)

tax revenues. (HFA fiscal notes dated 5-10-00) The bills contain provisions intending to “hold harmless” the State School Aid Fund and revenue sharing for local governments, so the loss in revenue would affect the General Fund.

ARGUMENTS:

For:

A Labor Day sales tax holiday is an excellent way to reduce the burden of the state’s taxpayers during a time when tax collections are so strong and the state’s budget is in surplus. It is a broad-based tax cut that is available to all consumers and that applies to a necessity – clothing. It is timed so as to stretch the “back to school” clothing shopping dollar, a particular benefit to families with growing children. It will boost retail sales throughout the state over a two-week period, and further encourage end of season tourism. This is a simple approach: it is not a deduction, a credit, a rebate, or a refund. There are no forms to fill out and no round trip for tax dollars; the money never leaves the taxpayer. The sales tax holiday particularly helps low- and moderate-income families since the sales tax is usually said to have the greatest impact on people with the least amount of discretionary income. Retailers say that sales tax holidays boost sales overall; they do not simply shift sales from one period to another. Apparently, tax-free shopping appeals to consumers out of proportion to the amount of the actual savings. The proposal will be good for the state’s economy and the state’s taxpayers.

Against:

Some people think that revenue reduction and tax cut proposals should be evaluated comprehensively and balanced against one another. There may be better ways to deal with surplus revenues. The state’s overall tax structure needs examination so as to safeguard the state’s long-term fiscal health. Once enacted, “permanent” tax cuts will be hard for future legislatures to undo if there is a downturn in the economy and in state revenues. Furthermore, the proposal “holds harmless” state school aid and revenue sharing for local governments. That means, all of the revenue loss is to the state’s General Fund. Is this wise over the long run? If tax cuts continue to be accompanied by hold harmless provisions for schools, the ability of the legislature to respond to the needs of the state with General Fund spending will be severely restricted.

Specifically, this proposal raises a number of questions and concerns. Does holding the holiday around Labor Day provide a geographic advantage to tourist areas in

the state (particularly in the northern regions of the state) at the expense of the ordinary retailer? Does it really focus on a “necessity” since not all clothing and footwear fits that category? Is the \$150 maximum the right figure, since few necessary clothing items reach that amount (particularly “back to school” clothing)? Will the proposal create an administrative headache for retailers and tax officials, separating out clothing and footwear from other items on sale and separating items below \$150 from those above? Will it seem fair to charge full sales tax on an item that costs \$155 and no tax on an item that costs \$150? Would it be preferable to exempt the first \$150 from tax, no matter what the cost of the item? Will the Department of Treasury (or, alternatively, retailers) need to make difficult decisions about what is included in “clothing” and “footwear”?

Response:

Three other large states, Texas, Florida, and New York, have conducted these sales tax holidays several times, so they are manageable. Other states have figured out which items are exempt and which are not. As to the cap on exempt goods, the bill as introduced applied to clothing and footwear up to \$500 per item, and some people would still prefer a maximum higher than \$150. For example, people entering or re-entering the work force might need to purchase a suit or similar clothing costing more than \$150. (Applying the exemption to a flat amount rather than the full price of an item, however, would benefit purchasers of luxury goods.) It should be noted that a recent study carried out for retailers suggests that the loss of revenue to states with sales tax moratoria in 1999 was less than had been predicted beforehand.

POSITIONS:

A representative of the Michigan Retailers Association testified in support of the legislation. (5-9-00)

The International Council of Shopping Centers has indicated its support. (5-9-00)

The Department of Treasury is opposed to the bills. (5-10-00)

Analyst: C. Couch

■ This analysis was prepared by nonpartisan House staff for use by House members in their deliberations, and does not constitute an official statement of legislative intent.