



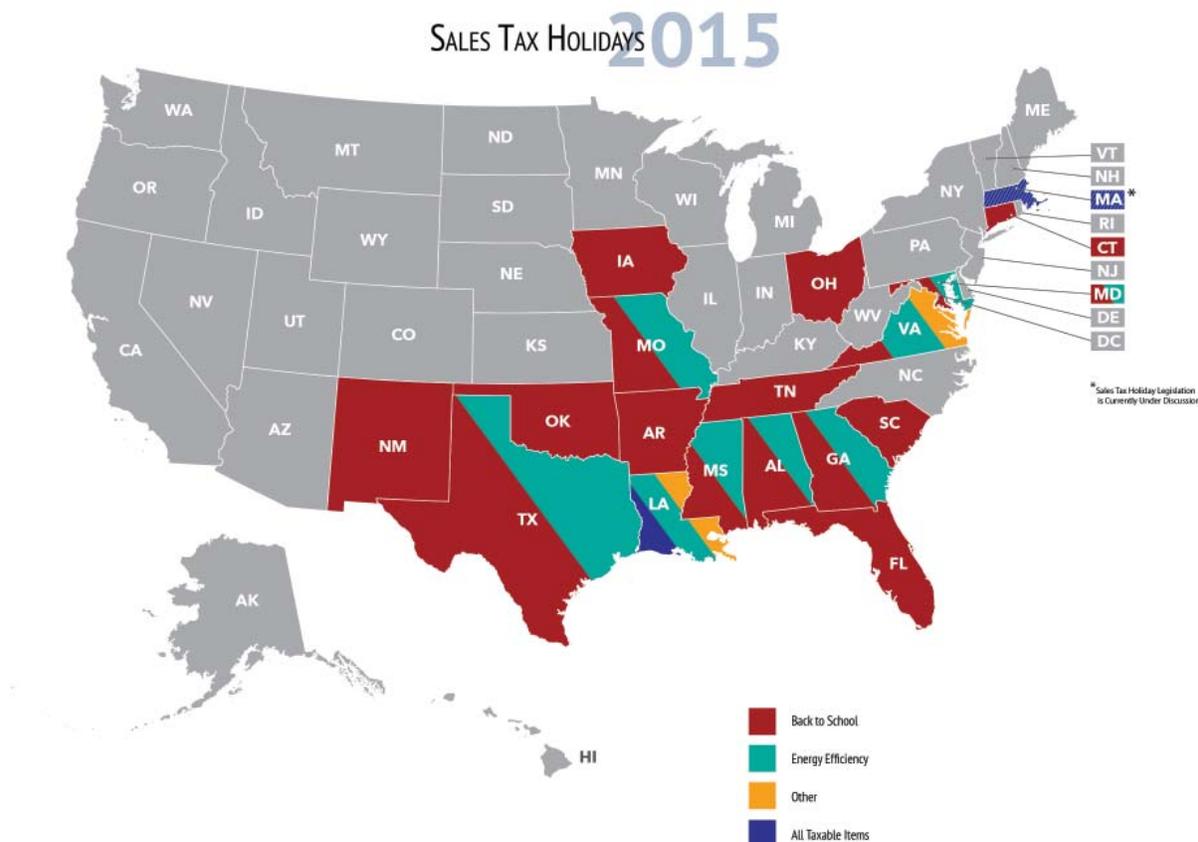
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Sales Tax Holidays: An Ineffective Alternative to Real Sales Tax Reform

Sales taxes are an important revenue source, comprising close to half of all state revenues in 2015. But sales taxes are also inherently regressive because the lower a family's income, the more the family must spend on goods and services subject to the tax. Lawmakers in many states have enacted "sales tax holidays" (at least 17 states will hold them in 2015), to provide a temporary break on paying the tax on purchases of clothing, computers and other items. While these holidays may seem to lessen the regressive impacts of the sales tax, their benefits are minimal. This policy brief examines the many problems associated with sales tax holidays and concludes that they have more political than policy benefits.

How Sales Tax Holidays Work

Sales tax holidays are temporary sales tax exemptions, usually applying to a small number of taxable items for a very limited period. These holidays are typically timed to take place in August, during the traditional "back to school" shopping season, and offer breaks on school-related items such as clothing, school supplies, and computers. Yet, a few states exempt all taxable goods during the holiday. Separate holidays for energy efficient appliances and storm preparation materials are becoming increasingly common as well. Most sales tax holidays last only two or three days, and almost all holidays apply only to items below some specified price (e.g. clothing items worth over \$100 are generally not exempted).



History of Sales Tax Holidays

The notion of a holiday was first introduced in 1980 when Ohio and Michigan didn't tax sales of automobiles for a period of time.¹ New York experimented with the current concept of sales tax holidays in 1996, and since then more than a dozen other states have passed similar legislation (New York no longer offers a holiday). Ohio lawmakers enacted a new back to school holiday this session and Florida lawmakers extended the state's back to school holiday from 3 to 10 days (though they also eliminated holidays for hurricane preparedness and energy efficient appliances). In Virginia instead of offering three separate holidays for school supplies, hurricane preparedness and energy efficient appliances the holidays were combined into a single weekend.

Many states either repealed or temporarily suspended sales tax holidays during the recession. For example, lawmakers in Florida, Georgia, Maryland, Massachusetts and Washington D.C. all canceled holidays during the height of the recent economic recession (though all but D.C. have reinstated them in recent years).

Holidays in Illinois, New York, North Carolina, West Virginia and Vermont were either short-lived or repealed.

Problems with Sales Tax Holidays

Policy makers tout sales tax holidays as a way for families to save money. On the surface, this sounds good. However, a two- to three- day sales tax holiday for selected items does nothing to reduce taxes for low- and moderate-income taxpayers during the other 362 days of the year. Sales taxes are inherently regressive. In the long run, sales tax holidays leave a regressive tax system unchanged, and the benefits of sales tax holidays for working families are minimal. Here are some other problems with these holidays:

Sales Tax Holidays are Poorly Targeted

- Because wealthier taxpayers also benefit from sales tax holidays, they offer less “bang for the buck” from a fairness perspective than more targeted tax breaks such as low-income sales tax credits (described in ITEP Policy Brief, “Options for Progressive Sales Tax Relief”) or Earned Income Tax Credits (described in ITEP Policy Brief, “Rewarding Work Through Earned Income Tax Credits”).
- Wealthier taxpayers are often best positioned to benefit from the holidays since they have more flexibility to shift the timing of their purchases to take advantage of the tax break –an option that isn't available to families living paycheck to paycheck. Many low-income taxpayers spend most or all of their income just getting by, which means that they have less disposable income than wealthier taxpayers to spend when the holiday arrives.
- One recent study found that while households that earn more than \$30,000 were likely to shift the timing of their clothing purchases to coincide with a sales tax holiday, but households earning less than \$30,000 were not.²
- The benefits of sales tax holidays are not limited to state residents, but instead extend to anybody who happens to be within the state's borders at the time of the holidays, including tourists and individuals who live close to the border.

¹Janssen, C. B. (2012), (Un) Happy Holidays: The True Meaning of Sales Tax “Holiday” Policy, *Loyola Consumer Law Review*, 24: 411–440.

²Marwell, Nathan and Leslie McGranahan (2010), The Effect of Sales Tax Holidays on Household Consumption Patterns. Federal Reserve Bank of Chicago

³Harper, R. K., Hawkins, R. R., Martin, G. S. and Sjolander, R. (2003), Price Effects around a Sales Tax Holiday: An Exploratory Study. *Public Budgeting & Finance*, 23: 108–113.

Sales Tax Holidays Offer No Significant Retail Boost

- One popular rationale for sales tax holidays is that they increase local consumer spending and boost local retail, but this has not been demonstrated. Rather, increased sales during sales tax holidays have been shown to be primarily the result of consumers' shifting the timing of their planned purchases.

Some Retailers Exploit Sales Tax Holidays

- Unscrupulous retailers can take advantage of the shift in the timing of consumer purchases by increasing their prices or watering-down their sales promotions during the tax holiday. One study of retailers' behavior during a sales tax holiday in Florida found evidence of precisely that: up to 20 percent of the price cut consumers thought they were receiving from the state's sales tax holiday was actually reclaimed by retailers.³

Sales Tax Holidays Create Administrative Difficulties

- Sales tax exemptions create administrative difficulties for state and local governments and for retailers who must collect the tax. For example, exempting groceries requires a sheaf of government regulations to police the border between non-taxable groceries and taxable snack food. A temporary exemption for clothing (or for any other back-to-school item) requires retailers and tax administrators to wade through a similar quantity of red tape for an exemption that lasts only a few days. Further complexity can arise in states with local sales taxes when some localities opt not to participate in the holiday and consumers unexpectedly end up paying local sales taxes on their purchases.

Sales Tax Holidays Cost Revenue

- In 2015, these holidays will cost states more than \$300 million. Revenue lost through sales tax holidays will ultimately have to be made up somewhere else, either through painful spending cuts or increasing other taxes.

Conclusion

Sales tax holidays are poorly targeted and too temporary to meaningfully change the regressive nature of a state's tax system. Lawmakers must understand that they can not resolve the unfairness of sales taxes simply by offering a short break from paying these taxes. If the long-term consequence of sales tax holidays is a higher sales tax rate, low income taxpayers may ultimately be worse off as a result of these policies. Policy makers seeking to achieve greater tax fairness would do better to provide a permanent refundable low-income sales tax credit or Earned Income Tax Credit (EITC) to offset the impact of the sales tax on low- and moderate-income taxpayers. 📌

Appendix: Sales Tax Holidays 2015

2015 Sales Tax Holidays			
State	Description	Dates	Detailed Information
Alabama	Clothing, Computers, School Supplies	August 7-9	https://www.revenue.alabama.gov/salestax/salestaxhol.cfm
Alabama	Severe Weather Preparedness	February 20-22	http://www.revenue.alabama.gov/salestax/WPSalesTaxHol.cfm
Arkansas	Clothing, School Supplies	August 1-2	http://www.dfa.arkansas.gov/offices/exciseTax/salesanduse/Pages/taxHoliday.aspx
Connecticut	Clothing, Shoes	August 16-22	http://www.ct.gov/drs/cwp/view.asp?a=1510&q=507134
Florida	Clothing, School Supplies	August 7-16	http://dor.myflorida.com/dor/tips/pdf/tip15a01-05_2015final06192015.pdf
Georgia	Clothing, School Supplies	July 31-August 1	https://dor.georgia.gov/sites/dor.georgia.gov/files/related_files/document/Sales%20Tax%20Holiday%20IB%202014_1.pdf
Georgia	Energy Star Products	October 2-4	http://gefa.georgia.gov/energy-star-and-watersense-sales-tax-holiday
Iowa	Clothing	August 7-8	https://tax.iowa.gov/iowas-annual-sales-tax-holiday
Louisiana	All Taxable Items Under \$2,500	August 7-8	http://www.revenue.louisiana.gov/NewsAndPublications/salestaxholiday
Louisiana	Firearms, Ammunition	September 4-6	http://www.revenue.louisiana.gov/NewsAndPublications/secondamendmentsalestaxholiday
Louisiana	Hurricane Preparedness	May 30-31	http://www.revenue.louisiana.gov/NewsAndPublications/hurricanepreparednessalestaxholiday
Maryland	Clothing, Shoes	August 9-15	http://comptroller.marylandtaxes.com/Public_Services/Agency_Information/Office_of_the_Comptroller/Comptroller_Initiatives/Shop_Maryland_Tax-free_Week/
Maryland	Energy Star Products	February 14-16	http://comptroller.marylandtaxes.com/Public_Services/Agency_Information/Office_of_the_Comptroller/Comptroller_Initiatives/Shop_Maryland_Energy/
Massachusetts	All Taxable Items	TBD	
Mississippi	Clothing, Shoes	July 31-August 1	https://www.dor.ms.gov/secondsalestaxholiday.html
Mississippi	Firearms, Ammunition	September 4-6	https://www.dor.ms.gov/docs/2014SecondAmendmenttotheSalesTaxHoliday_3.pdf
Missouri	Clothing, Computers, School Supplies	August 7-9	http://dor.mo.gov/business/sales/taxholiday/school/
Missouri	Energy Star Products	April 19-25	http://dor.mo.gov/business/sales/taxholiday/green/consumers.php
New Mexico	Clothing, Computers, School Supplies	August 7-9	http://www.tax.newmexico.gov/tax-holiday.aspx
Ohio	Clothing, School Supplies	August 7-9	http://www.tax.ohio.gov/sales_and_use/SalesTaxHoliday.aspx
Oklahoma	Clothing	August 7-9	http://www.ok.gov/tax/faqs.html#c412
South Carolina	Clothing, Computers, School Supplies	August 7-9	https://dor.sc.gov/resources-site/media-site/Pages/SOUTH-CAROLINA'S-ANNUAL-SALES-TAX-HOLIDAY-IS-AUGUST-7-9.aspx
Tennessee	Clothing, Computers, School Supplies	August 7-9	http://www.tn.gov/revenue/article/sales-tax-holiday
Texas	Backpacks, Clothing, School Supplies	August 7-9	http://comptroller.texas.gov/taxinfo/taxpubs/taxholiday/d/
Texas	Energy Star Products	May 23-25	http://comptroller.texas.gov/taxinfo/taxpubs/tx96_1331/
Virginia	Clothing, School Supplies	August 7-9	http://www.tax.virginia.gov/content/sales-tax-holiday
Virginia	Energy Star Products	August 7-9	http://www.tax.virginia.gov/content/sales-tax-holiday
Virginia	Hurricane Preparedness	August 7-9	http://www.tax.virginia.gov/content/sales-tax-holiday