Ohio Legislative Service Commission

Jean J. Botomogno

Fiscal Note & Local Impact Statement

Bill: Am. S.B. 243 of the 130th G.A. **Date**: February 26, 2014

Status: As Reported by Senate Ways & Means **Sponsor**: Sen. Bacon

Local Impact Statement Procedure Required: Yes

Contents: Creates a three-day sales tax holiday in August of each year for sales of specified clothing and computers

State Fiscal Highlights

STATE FUND	FY 2014	FY 2015	FUTURE YEARS
General Revenue Fund			
Revenues	- 0 -	Loss of up to $36 million	Loss of up to $37 million
Expenditures	- 0 -	- 0 -	- 0 -

Note: The state fiscal year is July 1 through June 30. For example, FY 2014 is July 1, 2013 – June 30, 2014.

- The bill exempts from the sales tax sales occurring on the first Friday of August and through the following Sunday of each year of the following: clothing (up to $100), school supplies (up to $20 per item), school instructional materials (up to $20), personal computers (up to $1,000), and computer supplies (up to $750).
- The bill decreases state sales tax receipts. Sales tax revenue is distributed to the state GRF, the Local Government Fund (LGF), and the Public Library Fund (PLF). Thus, the bill would reduce the amounts distributed to all three funds.

Local Fiscal Highlights

LOCAL GOVERNMENT	FY 2014	FY 2015	FUTURE YEARS
Counties, municipalities, townships, and libraries (LGF and PLF)			
Revenues	Potential Loss	Loss of up to $1 million	Loss of up to $1 million
Expenditures	- 0 -	- 0 -	- 0 -
Counties and transit authorities			
Revenues	Potential loss	Loss of up $9 million	Loss of up to $9 million
Expenditures	- 0 -	- 0 -	- 0 -

Note: For most local governments, the fiscal year is the calendar year. The school district fiscal year is July 1 through June 30.

- The temporary sales tax exemption will reduce revenue from county permissive and transit authority sales taxes. Those local permissive taxes share the state sales and use tax base.

- A share of GRF tax revenues is distributed under permanent law to the LGF and the PLF. LGF revenues are distributed to counties, municipalities, and townships, while PLF revenues are distributed to libraries. Thus, any reduction to GRF sales tax receipts would also reduce the amount distributed to the LGF and PLF.

Detailed Fiscal Analysis

S.B. 243 exempts from the sales tax sales occurring on the first Friday of August and through the following Sunday of each year of the following items: clothing (up to $100), school supplies (up to $20 per item), school instructional materials (up to $20), personal computers (up to $1,000), and computer supplies (up to $750). The bill is estimated to reduce state revenue from the sales and use tax by up to $37 million in FY 2015, the first fiscal year the bill may affect tax revenues. In FY 2016, the potential revenue reduction from the bill may be up to $38 million. Under permanent law, the GRF receives 96.68% of the revenue from the sales and use tax, while 1.66% of the receipts are transferred each to the Local Government Fund (LGF, Fund 7069) and the Public Library Fund (PLF, Fund 7065) for distribution to counties, municipalities, townships, and libraries. Thus, sales tax revenue to the GRF would decline by up to $36 million in FY 2015 and $37 million in FY 2016; and, distributions to the LGF and PLF would be reduced by a total of about $1 million in each of FY 2015 and FY 2016.

The bill will also reduce the tax base for county permissive and transit authority sales taxes. Those local permissive taxes share the state sales and use tax base. The potential revenue loss to local governments from local sales taxes, at approximately 23% of state sales tax revenues, would roughly be up to $9 million in each fiscal year. Thus, total revenue reductions for local governments, including reduced LGF and PLF distributions, may be up to $10 million each year.

The estimates are based on data primarily from surveys from the National Retail Federation (NRF) on back-to-school shopping, and also on personal consumption expenditures from the U.S. Bureau of Economic Analysis. Estimated Ohio spending was obtained by adjusting national data using an index of Midwest spending patterns (relative to national average spending) from the U.S. Bureau of Labor Statistics (Consumer Expenditure Survey for 2010). This Fiscal Note utilizes school enrollment data for 2010 by age from the U.S. Census (American Community Survey), both for K-12 and college age students.

Consumers are expected to shift their purchases by delaying or accelerating their purchases into the tax holiday period. The estimates include temporal substitution effects of up to three weeks (based on previous NRF surveys on the timing of back-to-school purchases). If the temporal substitution is less, then the revenue loss from the bill would be less than estimates. If these effects are larger than presumed, particularly for computer purchases, the revenue loss could be greater. Also, the estimates do not include the potential revenue loss from purchases of computers, computer software, and computer peripherals by businesses, though it is likely some small business spending on those items may be timed to take advantage of the holiday. If such responses to the tax holiday occur, it may increase the potential revenue loss from the bill.

The Department of Taxation will incur additional expenses associated with the implementation of this tax exemption. These expenses will be informational bulletins explaining the exemption. There may also be an increase in auditing costs, as more information will need to be verified. Costs associated with the implementation of the bill may be absorbed as part of the normal operations of the Department of Taxation. Businesses, in particular small retailers, may experience additional costs due to the need to reprogram cash registers and train staff to deal with the tax exemption.

As noted above, most additional sales during the tax holiday weekend will be delayed or accelerated purchases to take advantage of the exemption. However, other economic factors are at play. They include price and income substitution effects, cross-border sales effects and a shift of some sales from remote to store sales during the holiday weekend. The lack of precise empirical data regarding the magnitude of such factors makes this fiscal analysis more complex, and estimated revenue loss estimates may be somewhat overstated.

Price and substitution effects

The temporary sales tax exemption would effectively decrease prices of the tax-exempt items by a percentage equal to the combined state and local sales tax rates. A share of those savings will result in added purchases. Also, lower prices enhance consumer "real" income or purchasing power. This additional income from the sales tax exemption is likely to be spent on both taxable and nontaxable items, and some additional tax revenues may be collected.

Cross-border sales

Two cross-border effects are likely to take place with this bill. It is probable that some Ohioans already purchase clothing or computers in other states and most do not pay Ohio use tax on those purchases. Such cross-border sales may remain in Ohio during the sales tax holiday. Also, Ohio stores may increase sales to residents of neighboring states that do not provide a similar tax holiday. Therefore, cross-border effects are present, although impossible to quantify. However, the total cross-border effect on tax revenues is expected to be minimal.

Shift from remote sales to store sales

A number of consumers purchase clothing, footwear, and computers through mail order and the Internet, in part, as a tax avoidance strategy. Therefore, the bill would reduce the appeal of such remote purchases, and thus transfer some of the remote sales to store sales in Ohio. This effect is assumed to be small and would probably have a negligible impact on sales tax revenue.

All the factors enumerated above, although important, are difficult to quantify and may slightly reduce the fiscal cost of the bill.

SB0243SR.docx/jc