

MST Journal Podcast #1 (July 2022)

Welcome to the San Jose State University MST Journal Podcast!

This is Annette Nellen. I'm a professor at San Jose State University and director of the graduate tax program where students earn an MS Taxation degree. These podcasts feature excerpts of select articles from our MST program journal titled - The Contemporary Tax Journal. This is a student-run, online journal that is published twice per year at scholarworks.sjsu.edu/sjsumstjournal/. It features works of tax practitioners and faculty as well as MST students. We also have CPA exam review questions on tax topics and an interview of a "tax maven," a well-known person in the tax field with a connection to San Jose State. We also feature tax policy analysis of legislative proposals written by our MST students.

For this first podcast, I'm reading excerpts from a tax policy article published in the Winter 2022 Volume 11 issue of *The Contemporary Tax Journal*.

The proposal analyzed by the students is California AB 1121, Sales Tax Exemption Emergency Preparation Items

This was written by MST students Pooja Karelia, CPA and Sheetal Partani, Enrolled Agent.

Introduction

On February 18, 2021, California Assembly Member Rodriguez introduced AB-1121, Sales and Use taxes: exemptions: emergency preparation items. This bill would provide an exemption from sales taxes for emergency preparation items, purchased during the 3-day period beginning at 12:01 a.m. on the Saturday before the last Monday in June and ending at midnight on the last Monday in June. Thus, this bill would create a "sales tax holiday" which would be the first one in California. This bill was proposed as a temporary provision for two years.

There is no limit on the number of items that could be purchased during this sales tax holiday, however there is a limit on the dollar amount of the items. The proposal specifies 12 items which

would be exempt - a portable generator up to \$1,500 and 11 other types of products which have a sales price under \$75 each.

Next, the article analyzes California AB 1121, Sales Tax Exemption Emergency Preparation Items, using the twelve principles set out in the AICPA’s Guiding Principles of Good Tax Policy: A Framework for Evaluating Tax Proposals. The full article applies all 12 principles to AB 1121, this podcast covers four of the principles.

Criteria	Does the proposal satisfy the criteria?
<p><i>Equity and Fairness –</i> Are similarly situated taxpayers taxed similarly? Also consider any different effects based on an individual’s income level and where they live.</p>	<p><i>Horizontal equity:</i> Horizontal equity requires similarly situated taxpayers to be taxed similarly. California AB 1121 exempts certain items from sales tax during a three-day window in June for years 2022 and 2023. This practice is quite common and many states like Florida, Texas, Louisiana have almost similar provisions for emergency/disaster preparedness items. However, this proposal favors selected products relative to other products. One can argue that various items like axes, pocketknives, handwarmers, ladders, blankets, tents, bug repellants, etc., are also useful in emergencies. There is no exemption for these items. The sales tax exemption is available only during the three-day period and not during other days, encouraging people to stock up during such time or wait until the sales tax holiday occurs in the next year.</p> <p><i>Vertical equity:</i> The vertical equity principle is satisfied when taxpayers with higher income pay more tax than taxpayers with lower income. Taxpayers with higher income would get the same amount of exemption as taxpayers with a lower income, or likely more as they can afford to purchase more of the tax exempt items. There is some debate whether higher income individuals really need a sales tax exemption and whether it is fair to distribute the burden of this tax</p>

	<p>expenditure on all taxpayers. Generally, because high-income taxpayers have more resources available to purchase emergency preparedness items, they will get a greater benefit of the sales tax exemption assuming they spend more money on such items. Since the exemption treats all consumers equally regardless of their income levels, it violates the principle of vertical equity.</p>
<p><i>Information Security</i> – Will taxpayer information be protected from both unintended and improper disclosure?</p>	<p>The exemption of sales tax on the emergency preparation items does not require any taxpayer to have an exemption certificate or additional information reporting by the seller in tax forms. So, there is no additional risk of unintended or improper disclosure of taxpayer information.</p>
<p><i>Neutrality</i> - The effect of the tax law on a taxpayer’s decisions as to how to carry out a particular transaction or whether to engage in a transaction should be kept to a minimum.</p>	<p>The proposal may result in government influencing consumers to change when they purchase certain goods. It might not be a wise idea for the consumers to wait until the 3-day period mentioned in the bill. This kind of proposal might affect consumer timing decisions. This bill does not support principle of neutrality because it favors consumers in picking products and industries to favor with sales and use tax exemptions. This bill discriminates among the products and across the time and alters consumer decisions.</p>
<p><i>Economic growth and efficiency</i> – will the tax unduly impede or reduce the</p>	<p>This bill would be beneficial to the consumers and provide relief to those who are adversely impacted and who need these emergency supplies. This exemption provides some relief to low-income individuals, yet gives unexpected and unneeded benefits to high income earners. This bill does not promote economic growth or</p>

<p>productive capacity of the economy?</p>	<p>significantly increase consumer purchases. A 2017 study by the Federal Reserve found that this kind of exemption simply shifts the timing of purchases without necessarily increasing spending. It is possible that some retailers will increase prices of the products during the 3-day holiday period, thereby reducing consumer savings. This bill provides an exemption for certain items, but not for others which might also be required for emergency situations. This proposal favors particular products, thereby causing capital to flow to particular products mentioned in the bill. This can harm other industries.</p> <p>Similar bills in other states have faced difficulties and some states and localities had to cancel or opt out of their sales tax holidays. North Carolina officials found that repealing their sales tax holiday in 2013 would save the state \$16.3 million the next year, and allow those dollars to be applied to individual and corporate income tax cuts.</p>
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Conclusion

AB 1121 should be reevaluated. Rather than providing a tax cut or boost to the economy, this bill is likely to impose costs on consumers and businesses without providing sufficient benefits. To achieve the goal of this bill the sales tax exemption should be neutral towards the products and timing decisions; all the products required during emergencies should consistently be subject to the same sales tax rate. The sales tax exemption will benefit buyers of the proper products during the three-day period but also provide benefit to people who would have purchased these products anyway. Also, if these products are so important to all individuals, why is the cost only lower for three days of the year?

The tax revenues lost during the holiday could instead be spent on publicity and buying supplies for low-income households. This bill in general does not provide expected tax relief to the low-income individuals, but provides greater tax savings to high-income individuals.

Suggested Improvements

1. If a purchase is made during the holiday period and is exchanged for another item after the holiday period, the exemption would not apply to the new item, thereby causing potential confusion and reporting errors. The bill should include a provision regarding return or exchange of items.
2. Also such exemptions set precedents for future exemptions, there should be a proper study conducted to understand whether such tax holidays change the consumer behavior or simply subsidize existing behavior.
3. Non-tax solutions should be pursued to meet the intended goal of ensuring more people have emergency supplies such as providing them to low-income households.

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