

Testimony to the
South Carolina Tax Realignment Commission on
Sales Tax Exemptions, Exclusions, and Caps

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I am Holley Ulbrich, an economist at the Strom Thurmond Institute of Government and Public Affairs at Clemson University. I commend your efforts to broaden the base of our state sales tax, which has not kept up with changes in what consumers buy. As a result, growth of retail sales tax revenue continues to lag behind the growth of gross retail sales.

As we rely more heavily on the sales tax not only for the General Fund but also for property tax relief and local governments in 29 counties, this gap will make it increasingly difficult to generate the resources we need to fund even our most basic public services. Most economists strongly recommend that the major taxes have a broad base with few exemptions. Such a tax provides a more dependable source of revenue and distributes the burden more fairly among households and firms.

I strongly recommend extending the sales tax to more services, but I will address that issue on the appropriate future date. I also strongly recommend that we index excise taxes for inflation, but again, today is probably not the appropriate occasion, although you could consider combining an excise tax on gasoline with a sales tax, as Georgia does. I'm sure your staff has called that option to your attention.

For today, I have three specific recommendations to offer. The first recommendation is to revise the current \$300 sales tax cap on personal vehicles, commercial vehicles, aircraft, boats, and motorcycles. This exemption was first adopted in response to a similar cap in North Carolina. North Carolina has since changed its law and assesses a three percent tax each time a title is transferred, with a \$1,000 cap only on commercial vehicles.

In addition to the revenue loss, the cap is also regressive. The tax on a used vehicle costing \$6,000 is the same as on a luxury vehicle costing \$60,000 or a yacht costing \$600,000. Ten years ago, we realized that the property tax burden on personal vehicles was excessive relative to other forms of property and relative to other states in the region, and a reduced assessment rate was phased in. That would have been the right time to address the sales tax cap, but better late than never.

We realize that the auto industry has fallen on hard times, and we do not wish to see them suffer any further erosion of sales. However, the cap can be modified gradually in two ways. First, the cap could be completely removed on boats and airplanes. It serves no discernable public purpose. Second, the cap on cars could be raised to \$1,000, which is equivalent to a six percent tax on a vehicle costing \$16,667—about the average price of a new basic vehicle. Or third, the cap could be converted to a percentage equivalent such as three percent, which would raise more revenue and also distribute the burden more fairly. At three percent, the tax on that vehicle costing \$16,667 would be \$500. That step would put us back in line with our neighbors in North Carolina.

Second, the admissions tax remained at five percent when the sales tax was raised to six percent. There is no reason to favor admissions over other taxable purchases. Raising the rate to six percent will also make the sales tax less regressive, because spending on admissions rises with income.

Finally, I have always been ambivalent about the food tax exemption. Those at the bottom of the income scale who use food stamps pay no sales tax on those purchases. The working and unemployed poor who may not receive food stamps probably need some relief, but that leaves at least two-thirds of the state's population who could well afford to pay sales tax on food. Other states have found ways to relieve the sales tax burden on food for low income households, either with income tax rebates or a lower rate on food than other purchases. Including food in the tax base also makes the revenue stream more stable.

There are many more changes that could be considered, but I think that in my limited time these are the most urgent. Thank you for your hard work and your patient attention, and for giving interested citizens and tax professionals the opportunity to provide input.



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