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Merchants may pine for a sales tax holiday, but consumers are better off with a plain old sale

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(Illustration / Kim Rosen)

By Tom Keane | August 6, 2006

It's like Christmas in August. I've been waiting all year - holding off on buying that sofa, deferring the purchase of a mattress, eyeing a new plasma screen - all in anticipation of a sales tax holiday next weekend. Massachusetts had its first tax holiday, a suspension of the 5 percent sales tax on most items under \$2,500, on August 14, 2004. Last year, in deference to the sensibilities of Jews observing Saturday Sabbath and vacationgoers who missed out on the fun as they traveled to and from summer rentals, the holiday was for an entire weekend in August. This year, it appeared for a while to be a sure thing. The Senate easily passed it in May as part of the state budget; the House also seemed ready, and then - poof - in one of those complicated bits of legislative legerdemain that defy mortal understanding, earlier last month it was gone. Yet traditions - even those of only two years' life - die hard. As I write this, some legislators are scrambling to revive the holiday. It would be better if they failed.

Why? Well, it turns out it's a bad idea.

Not because it's a hit to the state budget (although that's what worries some). The Department of Revenue figures the holiday cost the state \$10.1 million in 2004 and \$15.4 million in 2005. In the context of a

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\$25.7 billion annual budget, that's not a big deal. Instead, the real problem with tax holidays is that they are little more than meaningless anti-tax showpieces that offer taxpayers few real benefits.

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New York had the first tax holiday in 1997. This year, at least 13 states will have one; almost all will be in August, with some lasting as long as 12 days. Retailers have been the biggest proponents of the idea, arguing that by pumping up retail sales while saving shoppers money, the holidays are a boon to the economy as well as to consumers. Both arguments, if not false, are unproven.

There's little question that, when the holidays occur, sales jump. But the measure of an economy is not retail sales for a day or two. The real issue is, do the holidays somehow spur sales for the year to higher-than-normal levels? Curtis Dubay, an economist with the nonpartisan Tax Foundation in Washington, D.C., argues no. "These are sales that would have occurred otherwise," he says. Most people are on a budget, with a relatively fixed amount of discretionary income. The opportunity to save 5 percent, for example, will persuade few to buy an item they otherwise would not have purchased. At most, a tax holiday will merely change their timing.

There's nothing wrong with that, of course, if it saves shoppers money. If I need a new \$1,000 computer and can wait until a tax holiday comes along, I'll save \$50. Even if the tax holidays have no effect on overall retail sales, they do seem to have the virtue of putting extra cash into consumers' pockets.

Except that it's not consumers who are pocketing the difference. Most of the time, according to David Brunori, a professor of public policy at The George Washington University in Washington, D.C., any potential tax savings is off set by price increases. His own studies show that retailers may charge up to 10 percent more than normal on those taxfree days (sometimes cleverly - instead of discounting by 25 percent, they may only discount by 15 percent). "Prices end up as high as or even higher than they were before," he says. In other words, the \$15.4 million that Massachusetts lost in taxes during last year's holiday probably ended up in the hands of merchants, not consumers, as store profit. No wonder retailers love them so much.

Yet, even though consumers actually benefit little from the holidays, they love them. "There's something about not giving money to the government," acknowledges Michael Widmer, president of the Massachusetts Taxpayers Foundation, a business-backed government watchdog group. In truth, though, a one- or two-day respite is no reform at all. That's particularly relevant this year, when both income- and property tax cuts are on the agenda of those who are running for governor. The sales tax is arguably the most regressive tax of all, since, rich or poor, we all pay the same tax on a roll of toilet paper. Rather than trying to salve its sting through tax holidays - what Brunori calls "the ultimate political gimmick" - it, too, deserves to be on that agenda.

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