

# Broadening the Sales Tax Base

**Joe Crosby**  
Multistate Associates

June 16, 2017

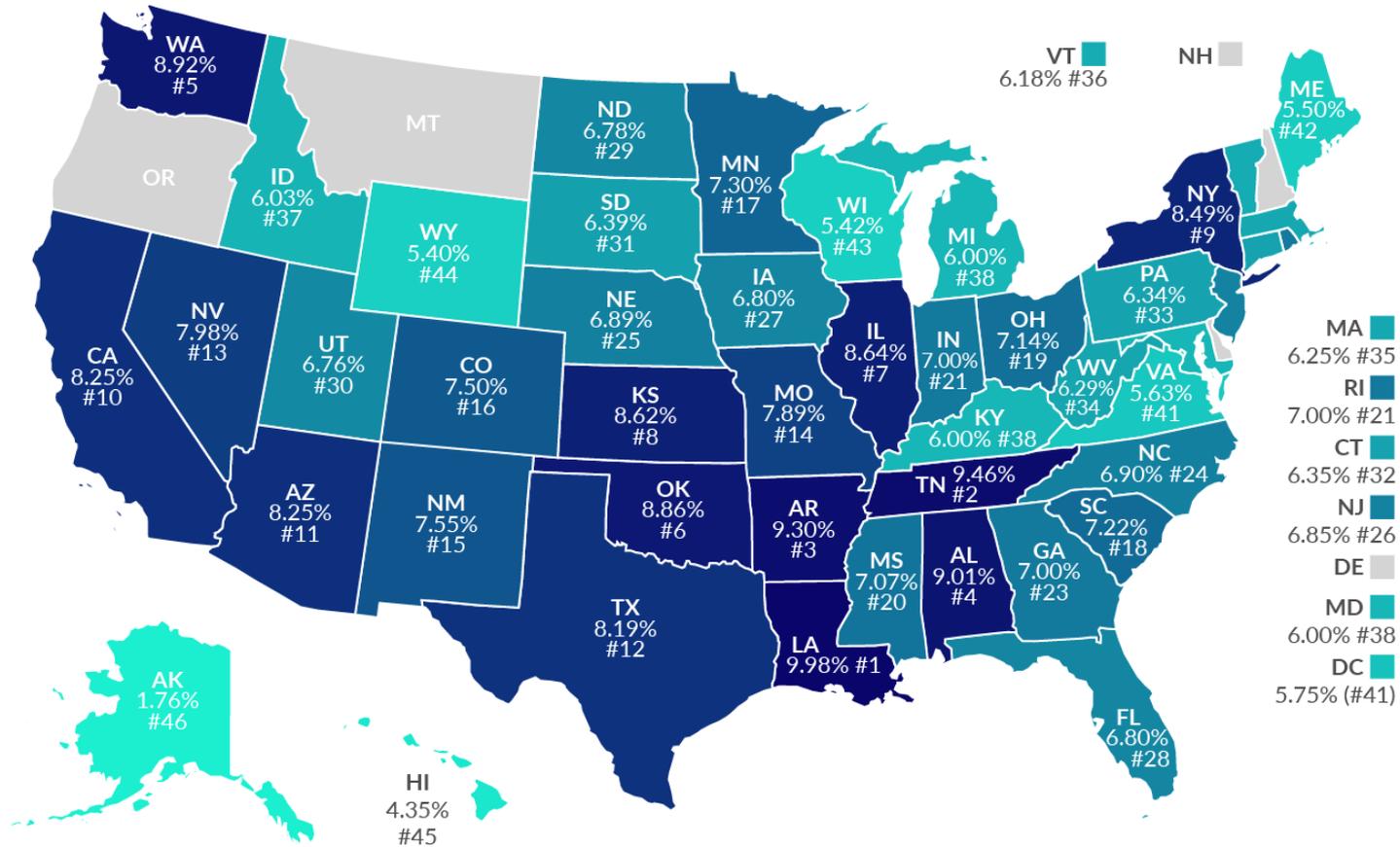
**Joseph Henchman**  
Tax Foundation

**Fred Nicely**  
Council on State Taxation



# How High Are Sales Taxes in Your State?

Combined State & Average Local Sales Tax Rates, Jan. 1 2017

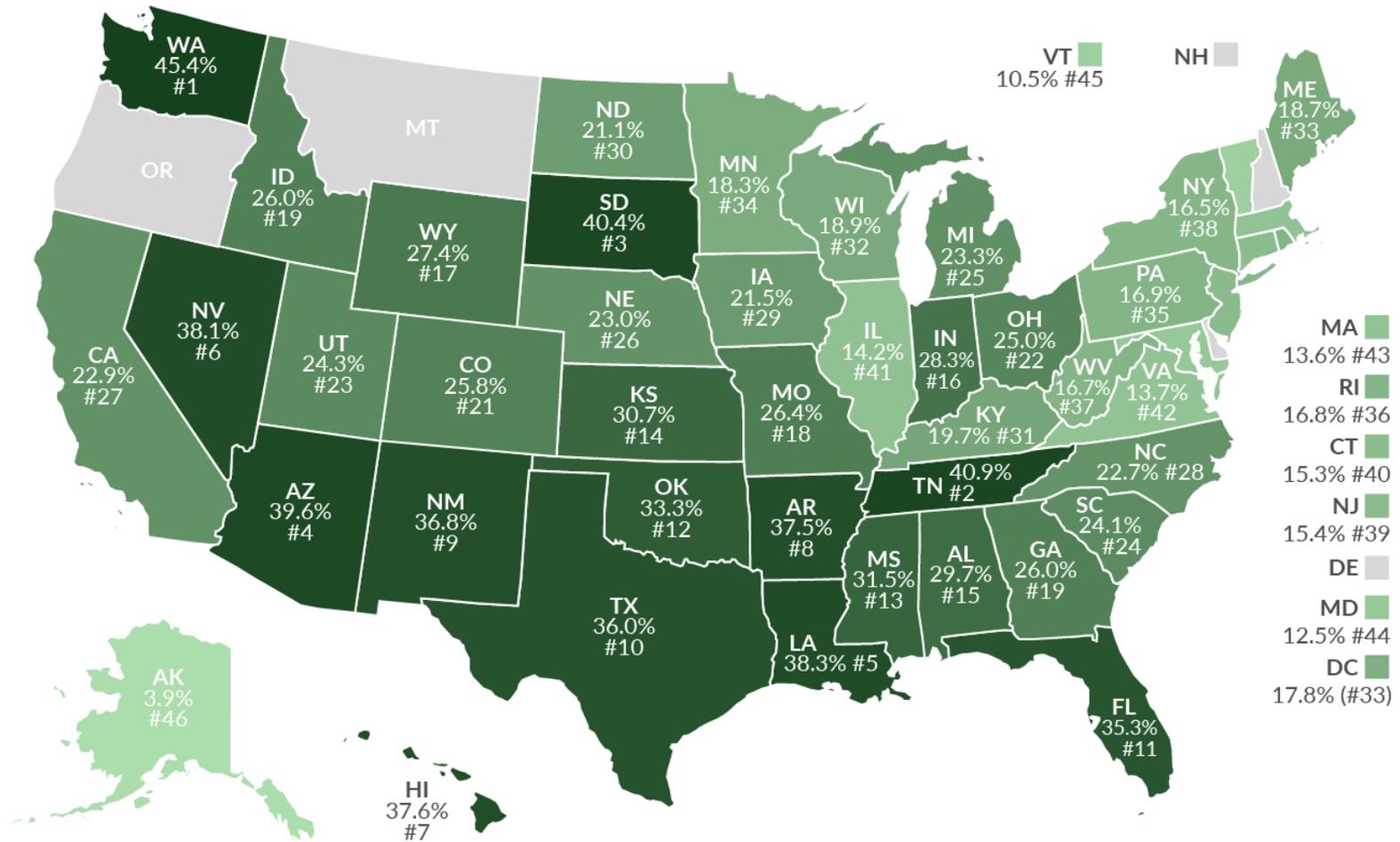


Note: City, county and municipal rates vary. These rates are weighted by population to compute an average local tax rate. Three states levy mandatory, statewide, local add-on sales taxes at the state level: California (1%), Utah (1.25%), Virginia (1%), we include these in their state sales tax. The sales taxes in Hawaii, New Mexico and South Dakota have broad bases that include many services. Due to data limitations, table does not include sales taxes in local resort areas in Montana. Salem County is not subject to the statewide sales tax rate and collects a local rate of 3.4375%. New Jersey's average local score is represented as a negative.

Source: Sales Tax Clearinghouse, Tax Foundation calculations, State Revenue Department Websites

# To What Extent Does Your State Rely on Sales Taxes?

Sales Tax Collections As a Percent of Total State and Local Tax Collections, FY 2014



Note: Percentages may not add to 100 due to rounding.  
Source: Census Bureau; Tax Foundation calculations.

Percent of Total State & Local Collections from Sales Taxes



# A PROPERLY STRUCTURED RETAIL SALES TAX

- Apply to all final consumption so that you can have a broad base and a low rate
- Most states don't:
  - They do not tax services
  - They exempt many final consumer goods, instead of taxing them
  - They tax business-to-business transactions, instead of exempting them
- And states are limited in their ability to tax Internet sales.

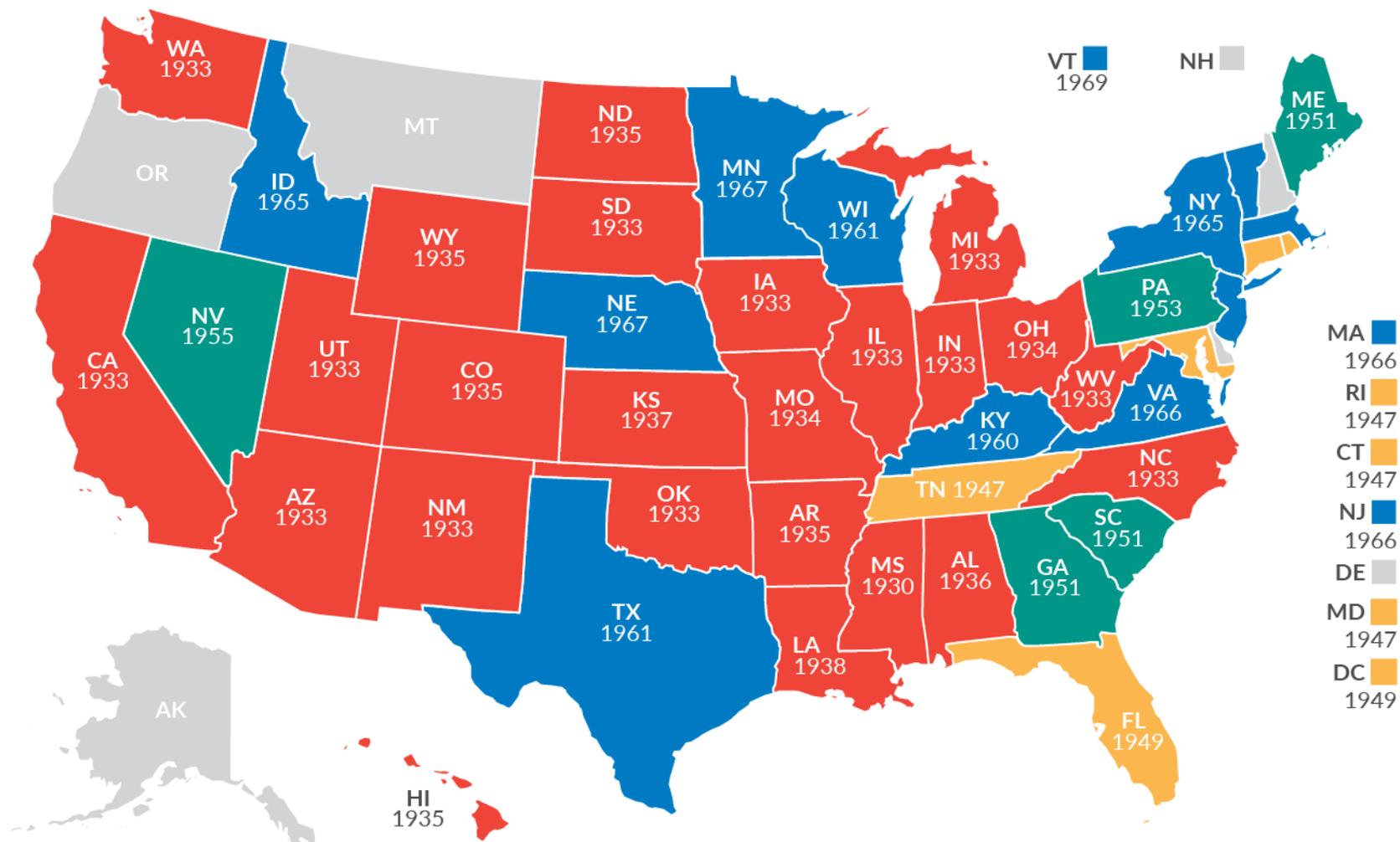
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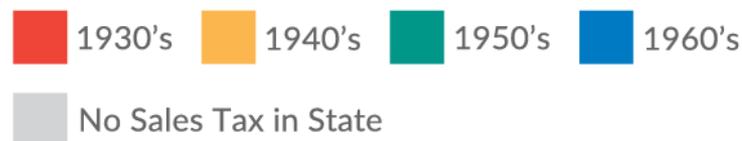
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# When Was a Sales Tax Adopted in Your State?



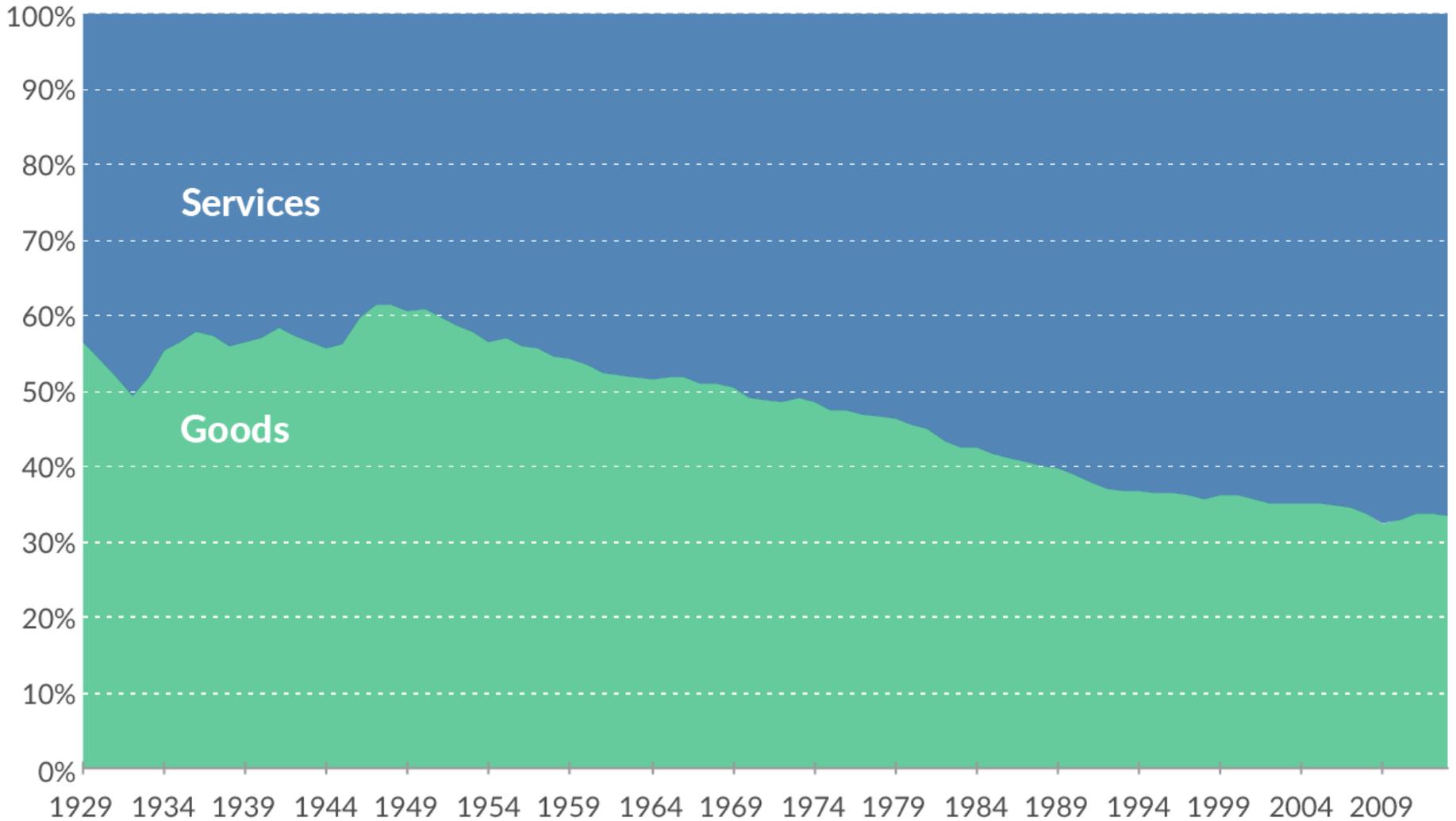
Note: Indiana adopted a gross income tax in 1933, but in 1963 it enacted a 2% retail sales and use tax. Gross receipts taxes are not strictly comparable to the retail sales taxes.

Source: *Significant Features of Fiscal Federalism: Budget Processes and Tax System*, Vol. 1, 1994.



# Percent of Total Personal Consumption Expenditures

Goods vs. Services, U.S. (1929-2013)

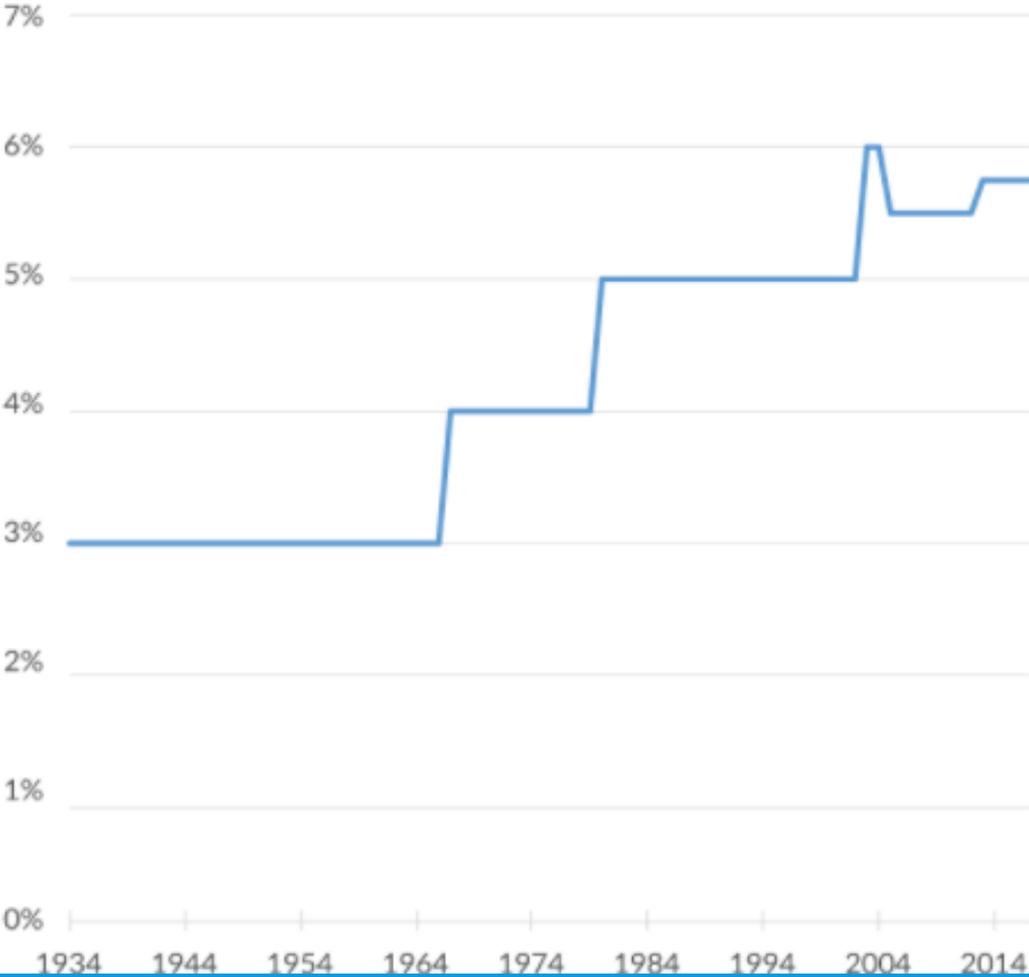


Source: Bureau of Economic Analysis, *National Income and Product Accounts*, "Personal Income and Outlays."

# Ohio's Sales Tax Rate Has Risen over Time

Ohio's State General Sales Tax Rate (1934-2017)

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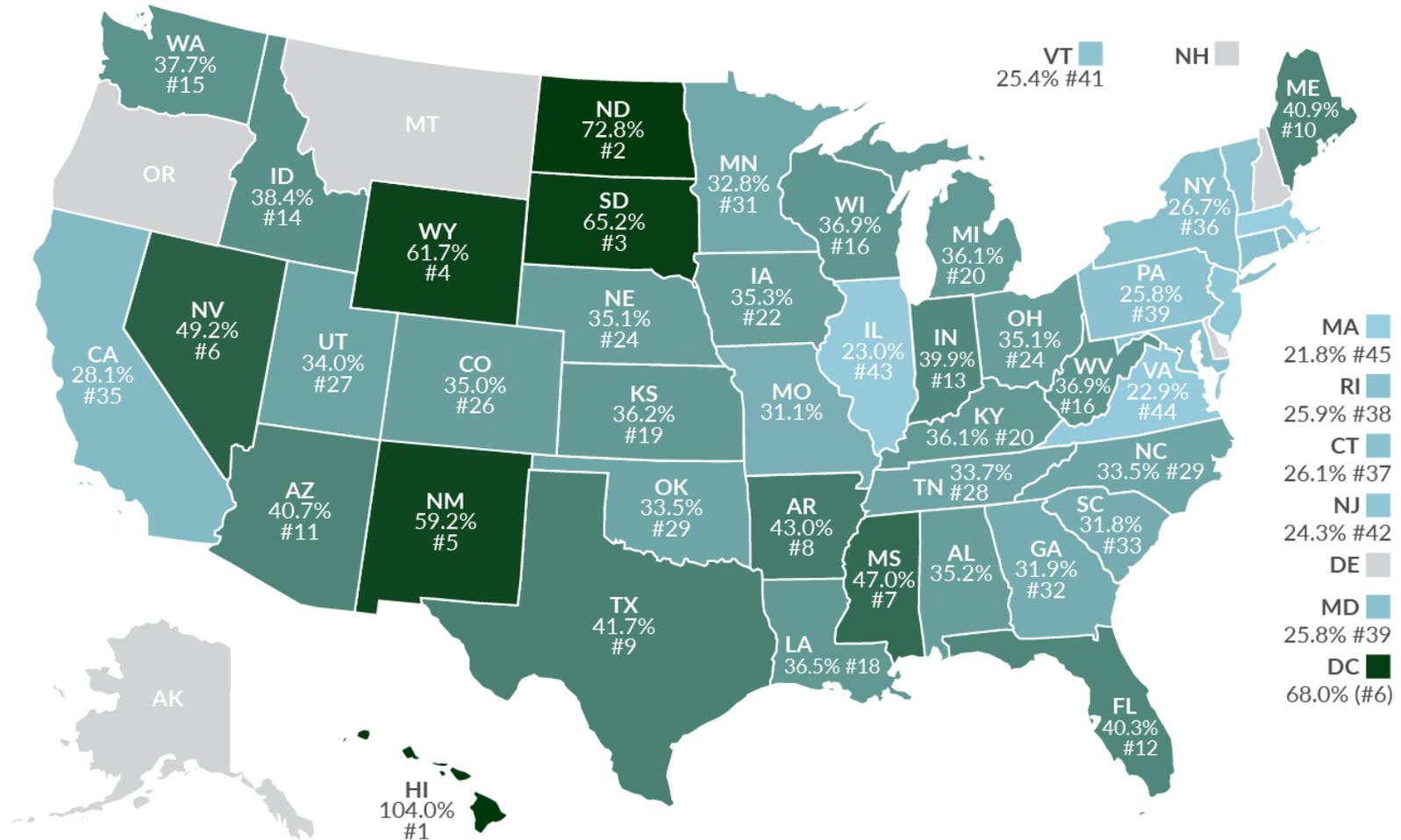
Since its creation in 1934, Ohio's state sales tax rate has nearly doubled to 5.75 percent today. Except for one rate decrease in 2005, the sales tax rate has increased over time, with four rate hikes. The current state-level rate of 5.75 percent is the 27th highest in the country.

Note: These rates do not include local sales tax rates.

Source: Ohio Department of Taxation, "Sales & Use Tax: History of Major Changes."

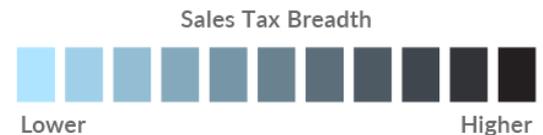
# How Broad Is Your State's Sales Tax Base?

Sales Tax Breadth by State, 2017



Note: Sales tax breadth is defined as the ratio of the implicit sales tax base to state personal income. (\*) The sales taxes in Hawaii, New Mexico, and South Dakota have broad bases that include many business-to-business services.

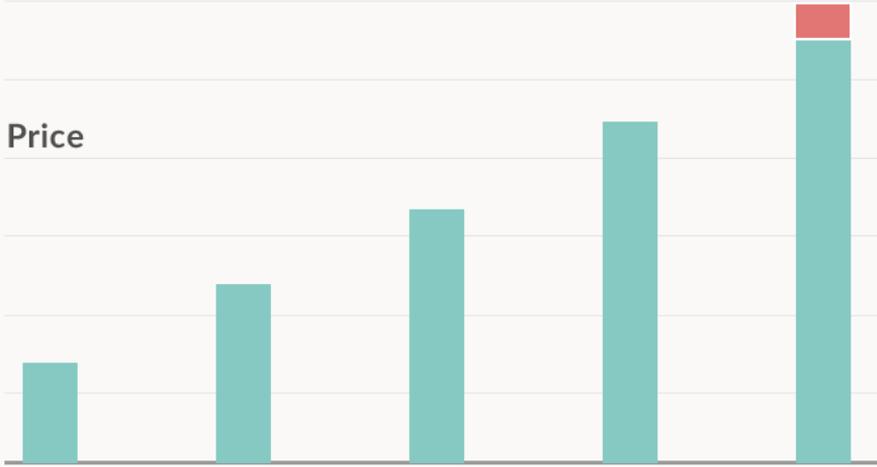
Source: Professor John Mikesell (Indiana University).



## Ideal Sales Tax on Final Consumption

Taxes  
Price of Product

Price

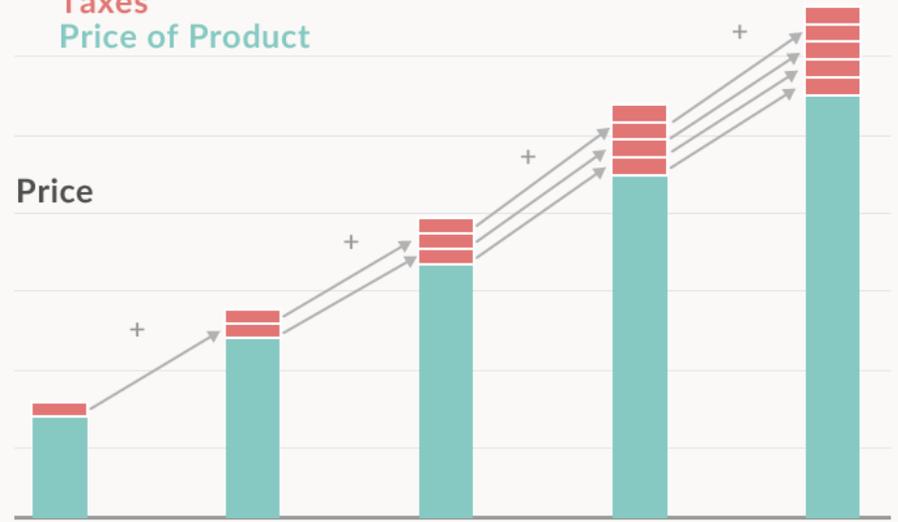


Stages of Production

## Gross Receipts Tax

Taxes  
Price of Product

Price



Stages of Production

# SALES TAXATION OF GOODS, SERVICES, AND BUSINESS INPUTS

Category	Tax	Tax at Lower Rate	Exempt
Farm Equipment	8	2	36
Office Equipment	46	0	0
Manufacturing Machinery	7	3	36
Manufacturing Raw Materials	2	1	43
Business Fuel & Utilities	13	1	33
Business Leases & Rentals	44	0	1

# SALES TAXATION OF GOODS, SERVICES, AND BUSINESS INPUTS

Category	Tax	Tax at Lower Rate	Exempt
Groceries	7	6	33
Gasoline*	3	0	42
Clothing	39	0	7
Prescription Drugs	0	1	45
Non-Prescription Drugs	35	1	10
Periodicals	22	0	24

# SALES TAXATION OF GOODS, SERVICES, AND BUSINESS INPUTS

Category	Tax	Tax at Lower Rate	Exempt
Legal	3	0	43
Financial	3	0	43
Accounting	3	0	43
Medical	2	0	44
Dry Cleaning	19	0	27
Fitness Club Memberships	13	0	33
Barber & Hair Salon	4	0	42
Landscaping	17	0	29
Repair	22	0	24
Real Estate	3	0	43

## Tax Repeal on Services In Florida Widely Felt

By JON NORDHEIMER, Special to the New York Times

Published: December 25, 1987

**MIAMI, Dec. 24**— Florida's repeal of its tax on personal and professional services is having an impact on states that monitored the progress of the tax, from enactment with broad bipartisan support last spring to crushing defeat earlier this month.

Repeal and the political bloodletting that accompanied it have caused leaders in a half-dozen or so states that were contemplating similar legislation to back away from a fight with powerful national advertising and media forces. The outcry from those forces led to the defeat of the Florida tax.

The print and electronic media contended that the tax was an infringement on the right of free speech, would harm commerce and would establish a precedent for other states. Florida applied the tax to all advertising distributed in Florida, including national broadcasters and magazines whose headquarters are not in Florida, and also to some services of out-of-state architects, lawyers and accountants.

"What happened to Florida on the services tax is having a lot of influence with other states," said William T. Pound, executive director of the National Conference of State

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### March 12, 2008 Rally: Maryland Computer Services Sales Tax h



Mitch Arnowitz

EDITORIAL

# 'Tech tax' causes confusion, and best fix would be repealing it



| AUGUST 08, 2013

BUSINESSES SHOULDN'T be required to guess what they must pay taxes on. Yet that's exactly where Massachusetts' software-services industry finds itself several weeks after state legislators passed a bill to put a 6.25 percent sales tax on "computer system design services" to fund transportation projects. But implementation of the so-called "tech tax" isn't the problem. It's the irresponsible policymaking that underlies it that is now jeopardizing one of the state's fastest-growing sectors. Opponents are filing a 2014 ballot initiative to repeal the levy. Legislators, however, should step in to provide a faster fix.

Tax officials, for their part, have made a valiant effort to inform businesses about the new tax

## Top 10 Trending Articles

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Tall Ships event assigned top security risk

Here are the changes legislators want to make to voter-approved Mass. marijuana law

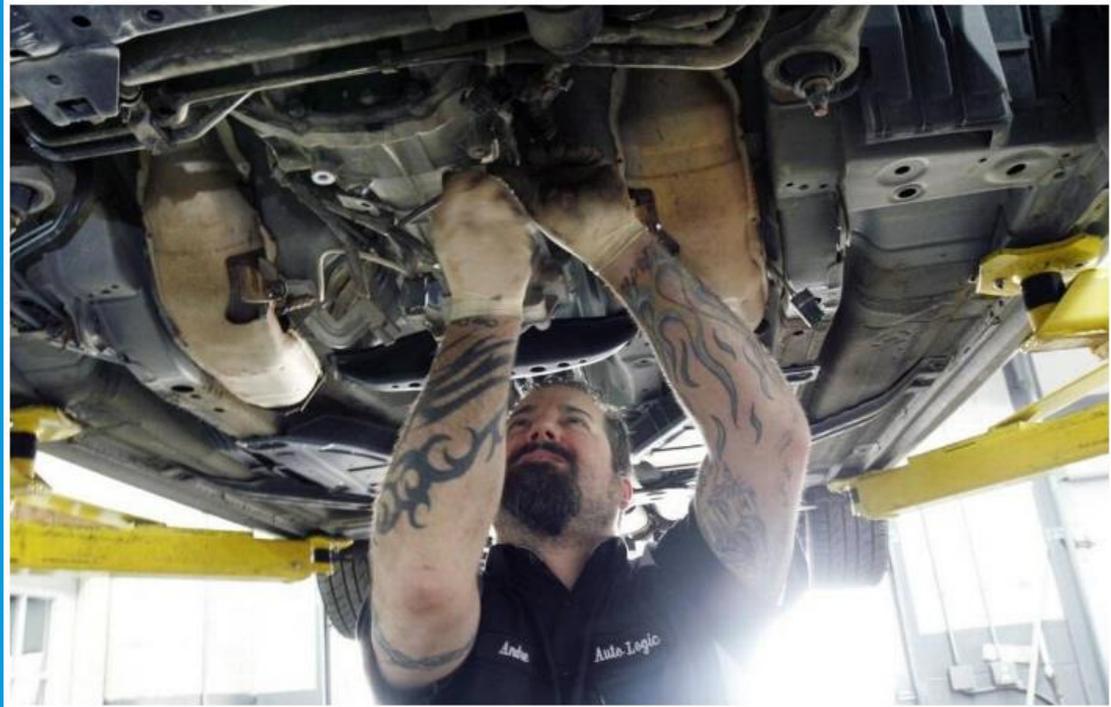
Stephen Kinzer: Saudi Arabia is destabilizing world

Read the Facebook messages between Michele Carter and Conrad Roy

That \$9.99 find at T.J. Maxx? It might raise questions about labor practices

AG Jeff Sessions stonewalls the Senate

Stephen King has been blocked by Trump on



Tech mechanic Andre Dalrymple does transmission inspection and repairs to a customer's car at Auto Logic of Carrboro in 2013. Car repairs will be subject to sales taxes starting on Tuesday. **HARRY LYNCH** - News & Observer File Photo

STATE POLITICS

FEBRUARY 27, 2016 4:28 PM

## Sales tax on auto repairs, dozens of other services starts Tuesday



BY COLIN CAMPBELL  
[ccampbell@newsobserver.com](mailto:ccampbell@newsobserver.com)



New sales taxes will take effect across North Carolina on Tuesday, adding to the cost of services ranging from car repairs to appliance installations.



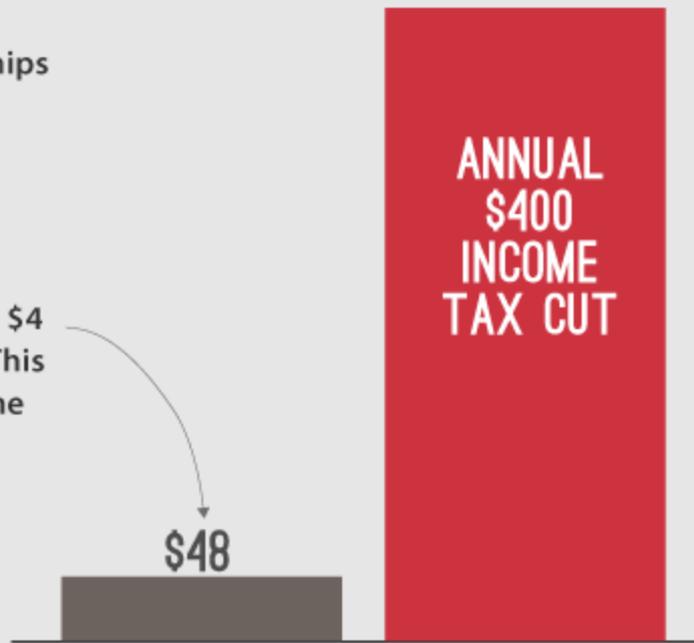
The legislature approved the additional sales taxes last year - part of a Republican-led shift to lower income taxes by expanding the number of services subject to sales taxes.



# DC TAX REFORM SAVES MIDDLE CLASS RESIDENTS **\$400 PER YEAR**

How does expanding DC's sales tax to gym memberships compare to the income tax cuts that everyone will receive?

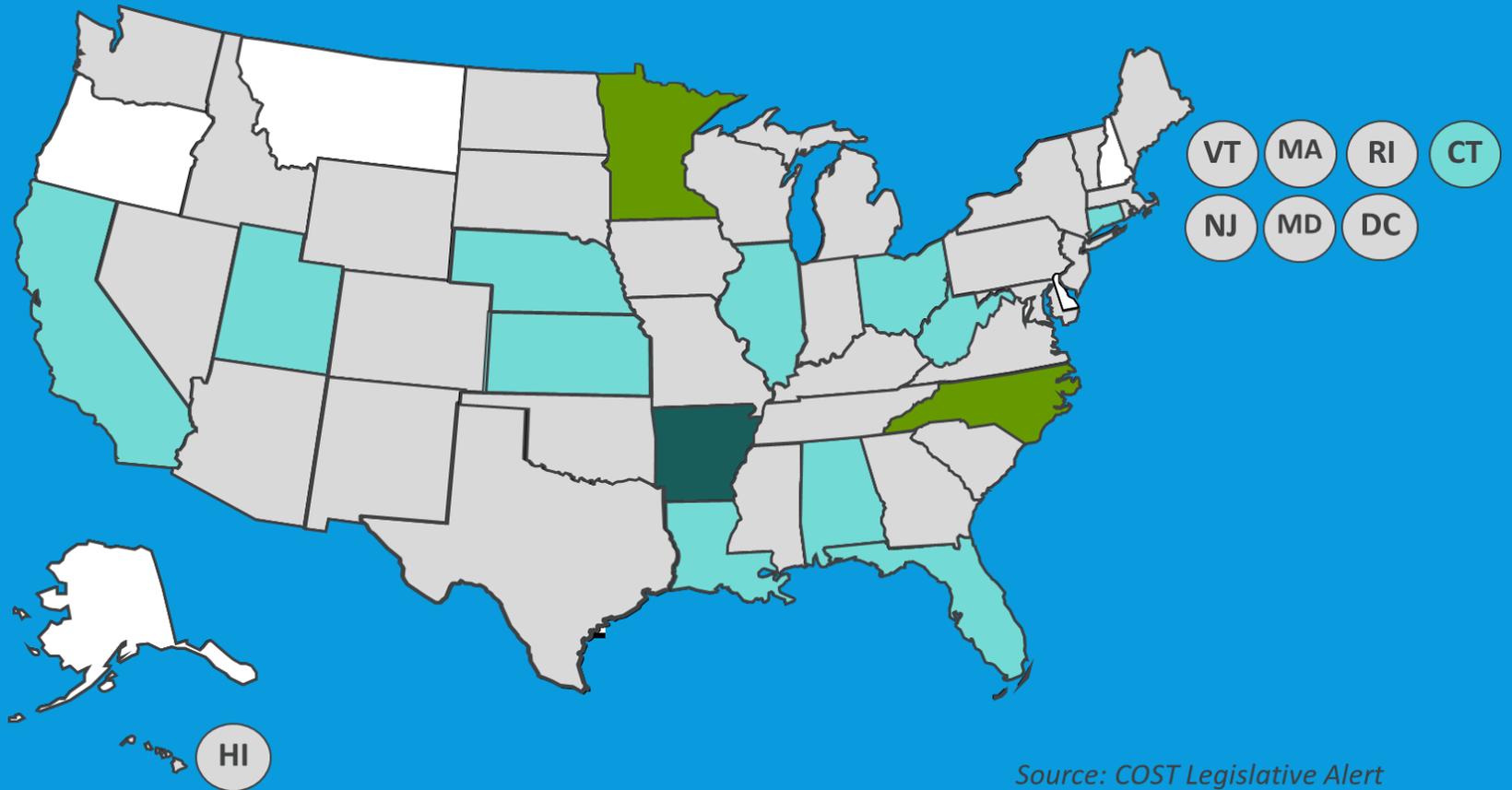
The sales tax on a \$70 per month gym membership is \$4 per month (\$48 per year). This is greatly outweighed by the income tax cuts.



Note: Income tax cut is average cut for incomes between \$50,000-\$75,000  
Source: Wes Rivers, Sales Tax on Services Helps Provide Tax Reductions for Most DC Residents, DC Fiscal Policy Institute

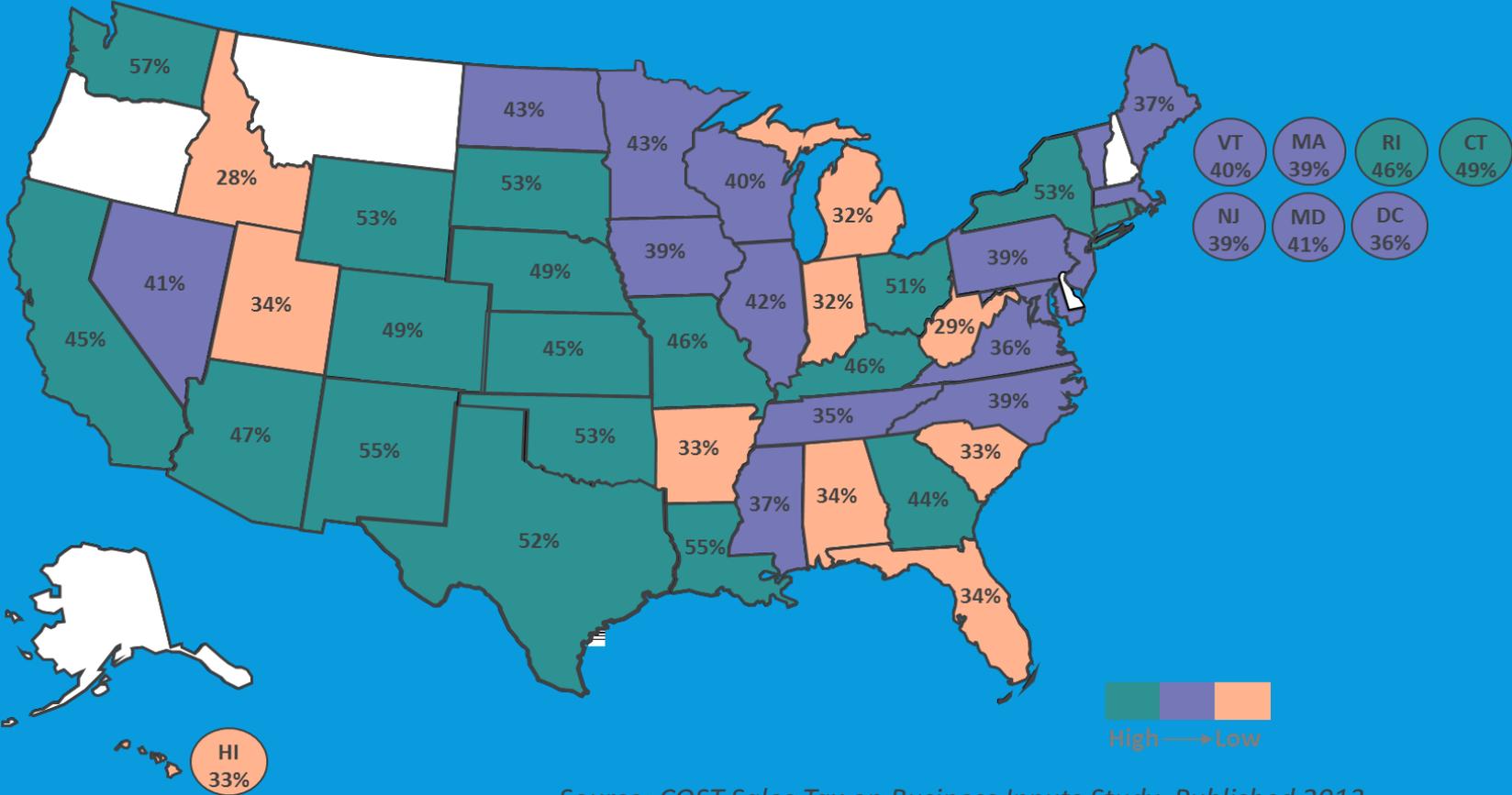
## 2017 Legislative Efforts to Expand Sales Tax Base

proposed enacted proposed or enacted legislation for contraction of base



Source: COST Legislative Alert

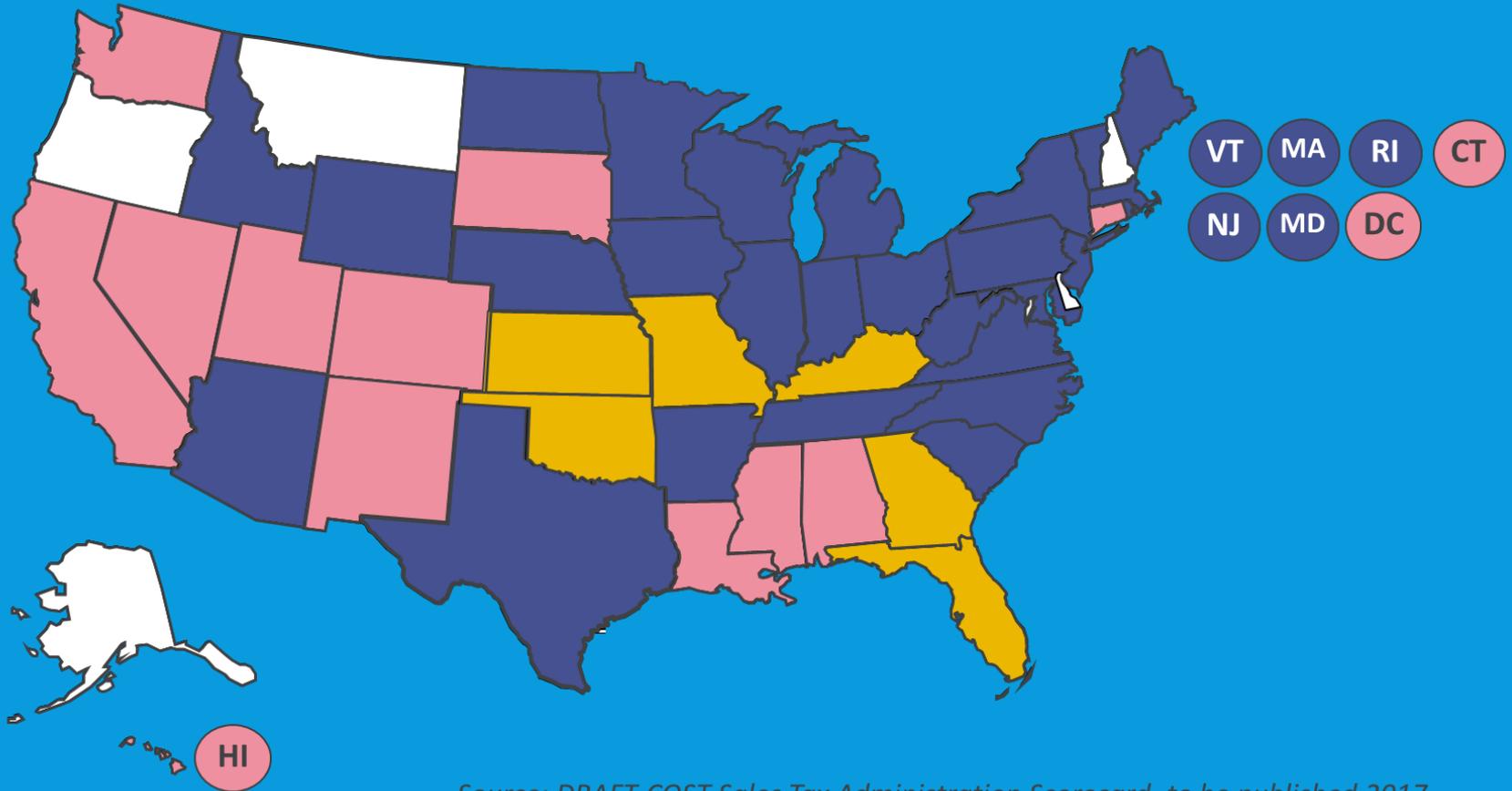
# State and Local Sales Taxes Imposed on Business Inputs



Source: COST Sales Tax on Business Inputs Study, Published 2013  
 (Note, certain gross receipts taxes included; e.g., Ohio & Washington)

## Breadth of the States' Manufacturing Exemptions

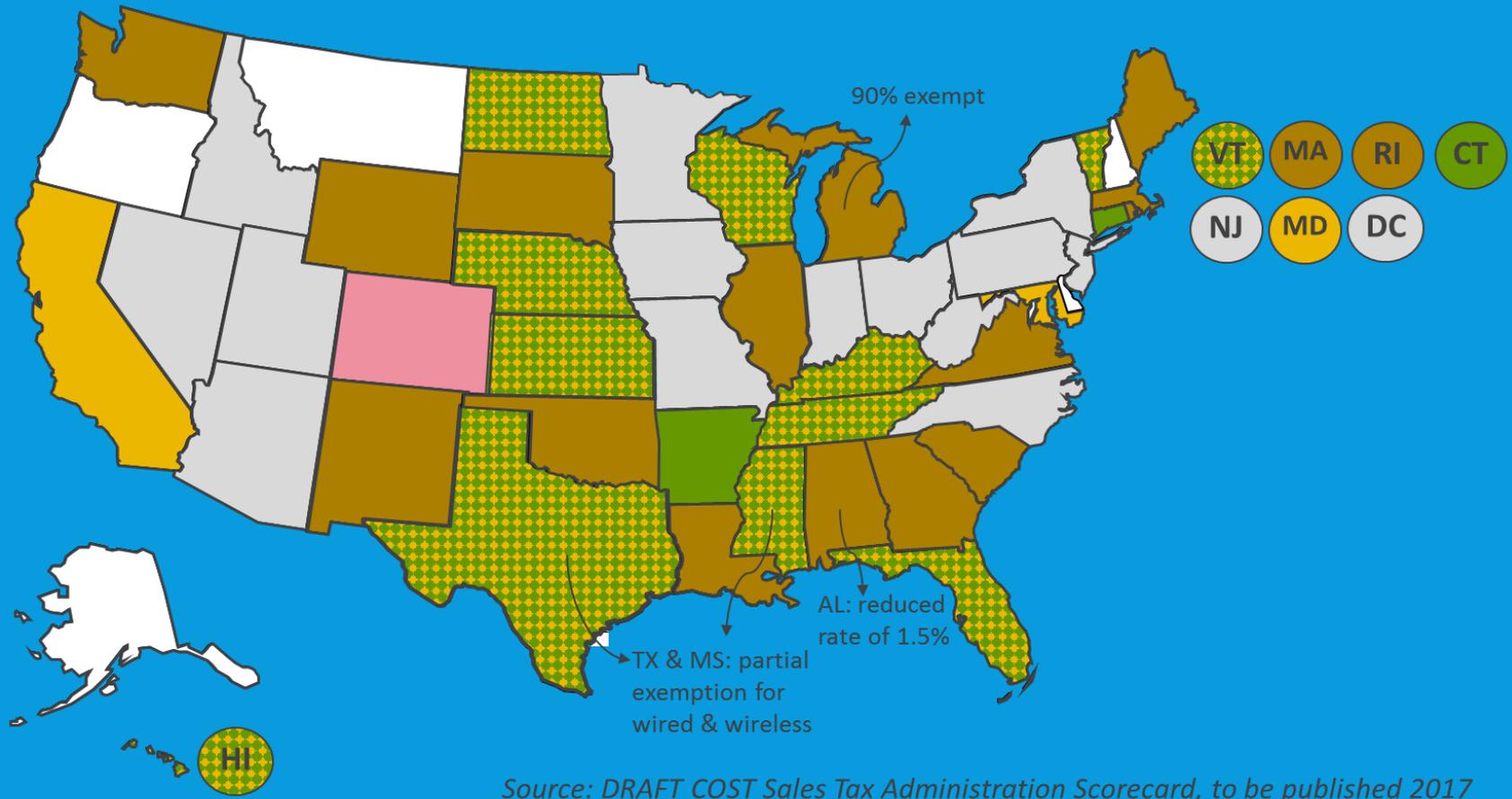
● none or restricted exemption    ● direct or primary use exemption    ● integrated plant exemption



Source: DRAFT COST Sales Tax Administration Scorecard, to be published 2017

# Double Taxation on Wired, Wireless and/or Cable Services

- wired & wireless
- wireless
- cable
- wired & cable
- wired, wireless & cable



Source: DRAFT COST Sales Tax Administration Scorecard, to be published 2017

ABOUT  
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# PROFESSIONAL SERVICES ALLIANCE



## About Us

The Professional Services Alliance protects and promotes the interests of professional services in the state and local tax arena, supporting policies that grow state and local economies.

[LEARN MORE](#)

## Our Position

The Alliance opposes any effort to enact a state service or use tax on accounting, advertising, legal, real estate, or other professional services, even if the new tax were to be in exchange for lower existing taxes. Application of a services tax penalizes individuals and businesses seeking to comply with state law, generates an administrative burden for the business community, and creates an economic disadvantage for businesses to move to the state or supply services within. It also leads to detrimental effects for state and local economies due to the cascading nature of taxes on business services, arbitrarily and unfairly increasing costs across businesses and raising prices for consumers.





## Downloadable Materials

Below are several downloadable PDF documents. Click the thumbnail images below and the document will download and open in a new window.

### Historical Examples: Past Failed Attempts to Tax Services

Several states have attempted to tax professional services, and each time the law has been repealed shortly after it went into effect.



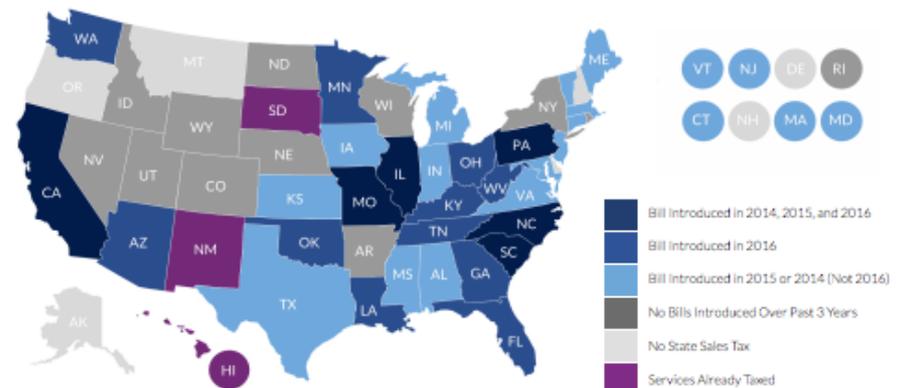
### The Economic Case Against Taxes on Professional Services

Professional service taxes hurt state and local economies, and basic economic policy teaches that they shouldn't be taxed.



## Tax on Services: Legislative State of Play

Legislation seeking to impose sales tax on services has been prevalent in state legislatures in recent years. The map shows states in which legislation has been introduced over the last three years. Darker colors indicate higher and/or more recent activity. Six states have had tax on services legislation every year over the last three years: California, Illinois, Missouri, North Carolina, Pennsylvania, and South Carolina. Despite this activity, no state has enacted and successfully maintained a broad based tax on services in decades.



### 2016 | 29 bills in 18 states

Arizona, California, Florida, Georgia, Hawaii, Illinois, Indiana, Kentucky, Louisiana, Minnesota, Missouri, North Carolina, Ohio, Oklahoma, Pennsylvania, South Carolina, Tennessee, Washington, West Virginia.

### 2015 | 42 bills in 23 states

Alabama, California, Connecticut, Florida, Hawaii, Illinois, Indiana, Kentucky, Louisiana, Maine, Maryland, Mississippi, Missouri, New Jersey, North Carolina, Ohio, Pennsylvania, South Carolina, Tennessee, Texas, Vermont, Virginia, Washington.

### 2014 | 35 bills in 16 states

California, Illinois, Iowa, Kansas, Maine, Massachusetts, Minnesota, Missouri, New Jersey, Oklahoma, North Carolina, Pennsylvania, South Carolina, South Dakota, Texas, Virginia.



## Past attempts to expand sales tax to services have failed.

Although many states tax a few select services, there is no trend of states successfully and broadly expanding their sales tax base to include professional services. Even at the height of the recession, most states looking at a sales tax on professional service rejected the idea as inherently unworkable. In 2016, 18 states saw 29 bills containing tax on service language introduced in their respective legislatures but none of the bills were successfully enacted. There have been multiple failed attempts in recent memory of states enacting a tax on services and repealing it shortly thereafter.



Minnesota

Minnesota enacted a tax on warehouse and storage services in 2014. Following the tax's passage, there was a large outcry that the tax would negatively impact the state economy and harm jobs and investment within Minnesota. It was repealed prior to its effective date.



Massachusetts

In 2013, Massachusetts approved an expansion of the definition of services to include computer software and design services, which faced immediate backlash. Two months later, the Governor signed legislation repealing it. Back in 1990, the state passed a tax on services provided to businesses. It was repealed two days after it took effect.



Michigan

Michigan enacted a broad tax on services in 2007 and a taxpayer coalition was quickly formed to repeal it. The group was worried that it would negatively affect jobs. The tax was repealed 17 hours after it became effective.



Florida

In 1987, Florida passed a broad sales tax on services. Six months later, lawmakers repealed it because it put in-state businesses at a competitive disadvantage to out-of-state counterparts.

No major industrial state levies a sales tax on professional services. Only three states tax services broadly (Hawaii, New Mexico, and South Dakota), but all three of these are low population states with unique tax systems and state economies. Each of them has a population of two million or less, and each has different revenue resources driving their tax systems. For example, South Dakota does without income taxes, depending much more heavily on sales tax, and Hawaii is geographically isolated, leading to less interstate competition.

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