FTA Services Taxation Survey – 2017 Update [preliminary results]

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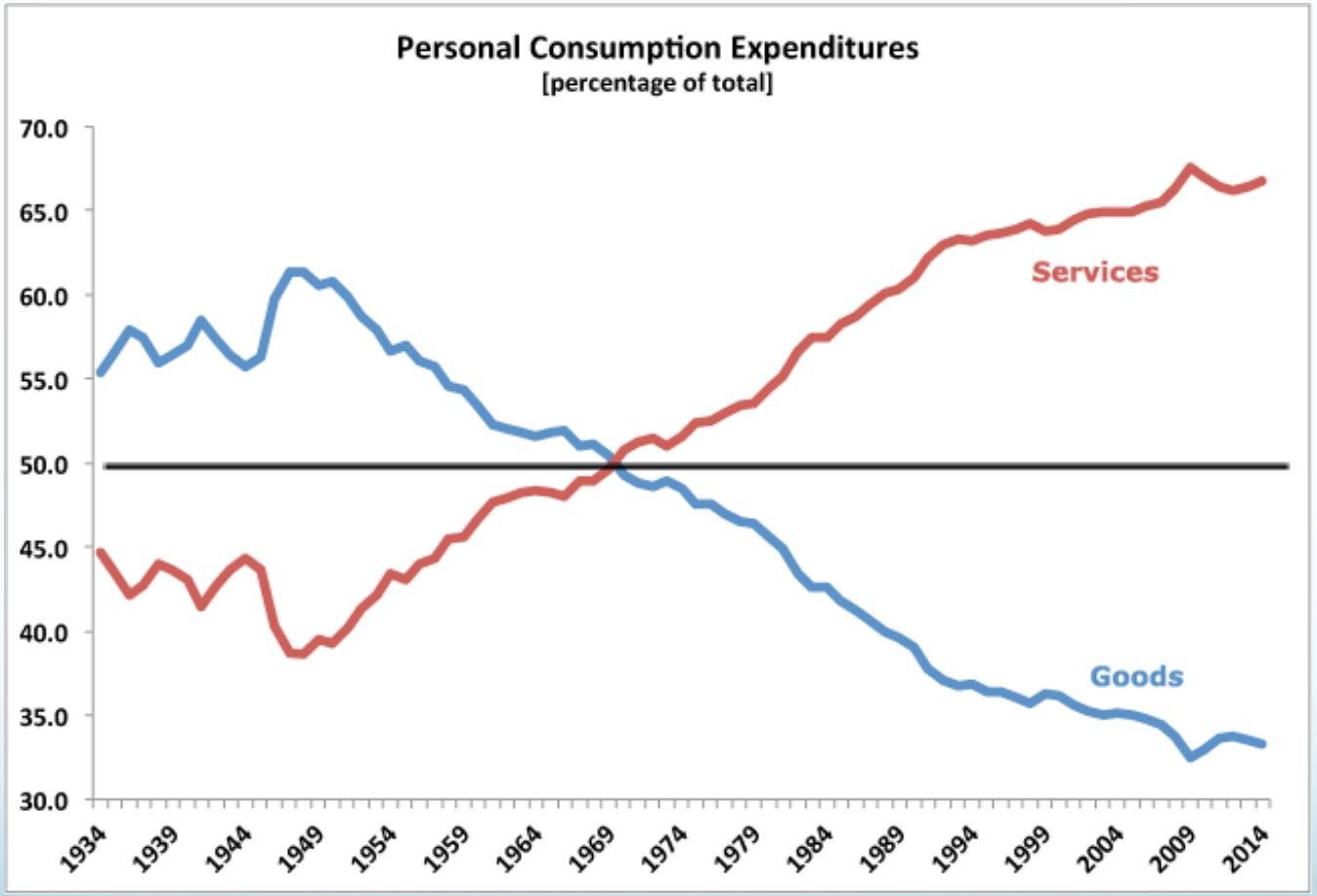
Overview

- Background
- Review Issues
- Summary of the Survey Results
- Where Do We Go From Here?
  - How Do States Move Forward?
  - Improvements in the Survey

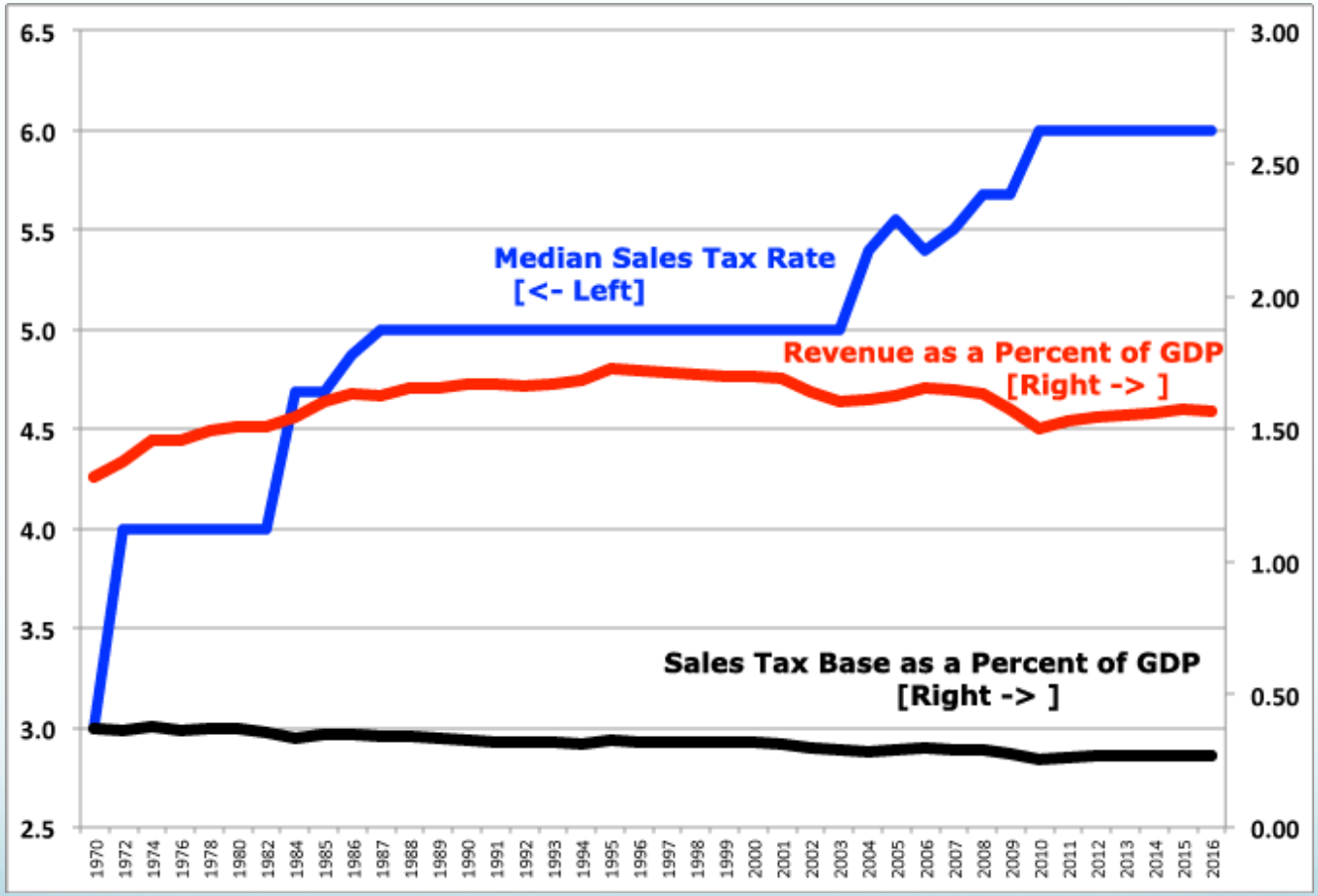
Background

- Survey First Compiled in 1990
  - 167 Services
- Updated Periodically, the Last Update was 2007
- The 2017 Survey Added Cloud Computing and Other Online Services
  - 176 Services, plus 10 Cloud Computing Services
- Purpose: **To Develop a System to Help Understand the Extend that States Tax Services**!

Why Should We Be Concerned About Services?



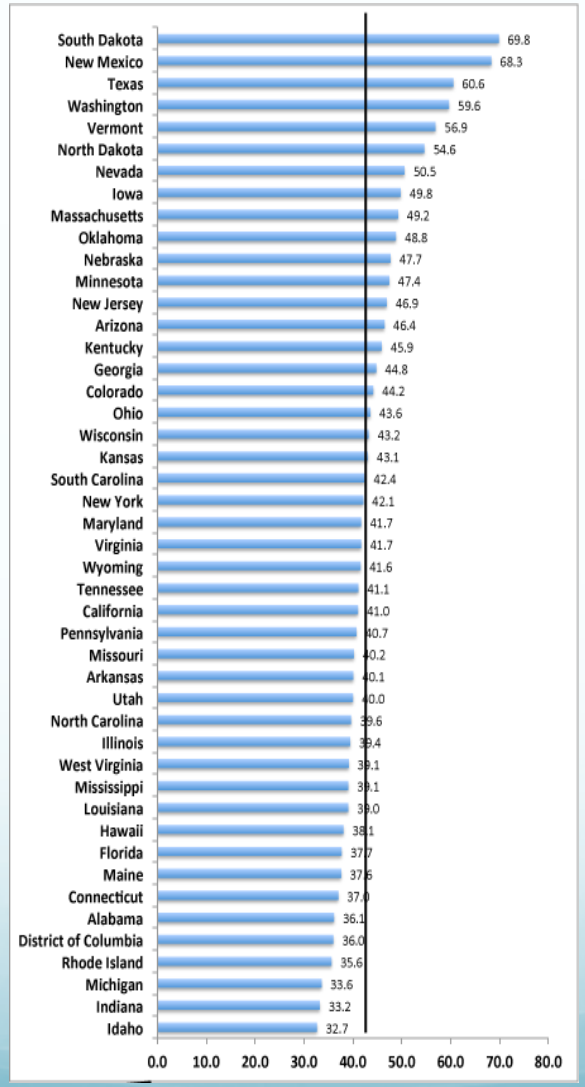
Sales Tax Rates Have Increases and Revenues . . .



What About Business Services?

- Economists Generally Frown on Taxing Business Purchases
  - Incentive for Businesses to Become More Centralized
  - Can Lead to Pyramiding
    - A Washington State Study Found Its GRT Tax Increased Taxes Paid by 150%
    - A 2005 Study Found a 27% Increase in Taxes Paid from the New Mexico GRT
    - See Barbe 2012 Revenue Estimating Conference Paper
  - Does This Mean We Should Not Tax Business Purchases?

We Already Tax Business Purchases . . .



Source: Ernst & Young LLP

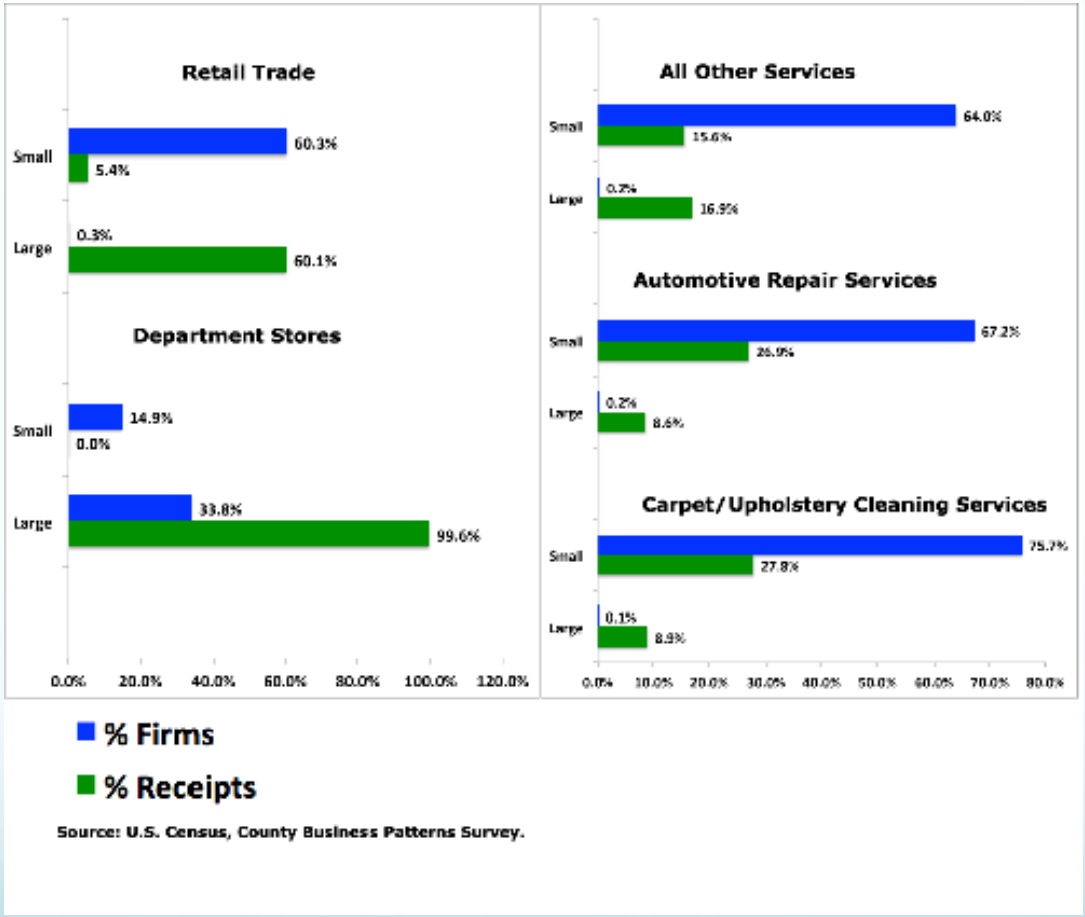
Why Can't Business Services Fit into the Current Sales Tax System?

- Exempting a Business Service from Taxation While Taxing a Comparable/Competing Product Introduces Another Distortion.
- The Current System in Most States Allow Resale or Production Exemptions to Limit Pyramiding
- States Should Examine Any Service on a Case-by-Case Basis, with an Eye Toward Minimizing Distortions.

Including Services Would Expand the Number of Taxpayers

- States Would Add Many New Sellers Who May Be Unfamiliar and Do Not have Software to Collect and Remit Sales Taxes
  - A California BOE Study Found that Broadly Taxing Services Could Add 2.5 Million New Sale Tax Registrants

Many of These New Taxpayers Would Be Small Businesses



Most Difficult Issue . . . What Is a Taxable Service?

- Two Way of Defining the Tax Base
  - Tax All Purchases Unless Explicitly Exempt [Florida 1986]
  - Itemize or List Services to be Taxed [Massachusetts 1990]
  - Both of These Broad-Scale Expansions were Repealed
- Any Political Expansion to Services Would Need to be an Incremental Approach . . .

How Do We Define Services?

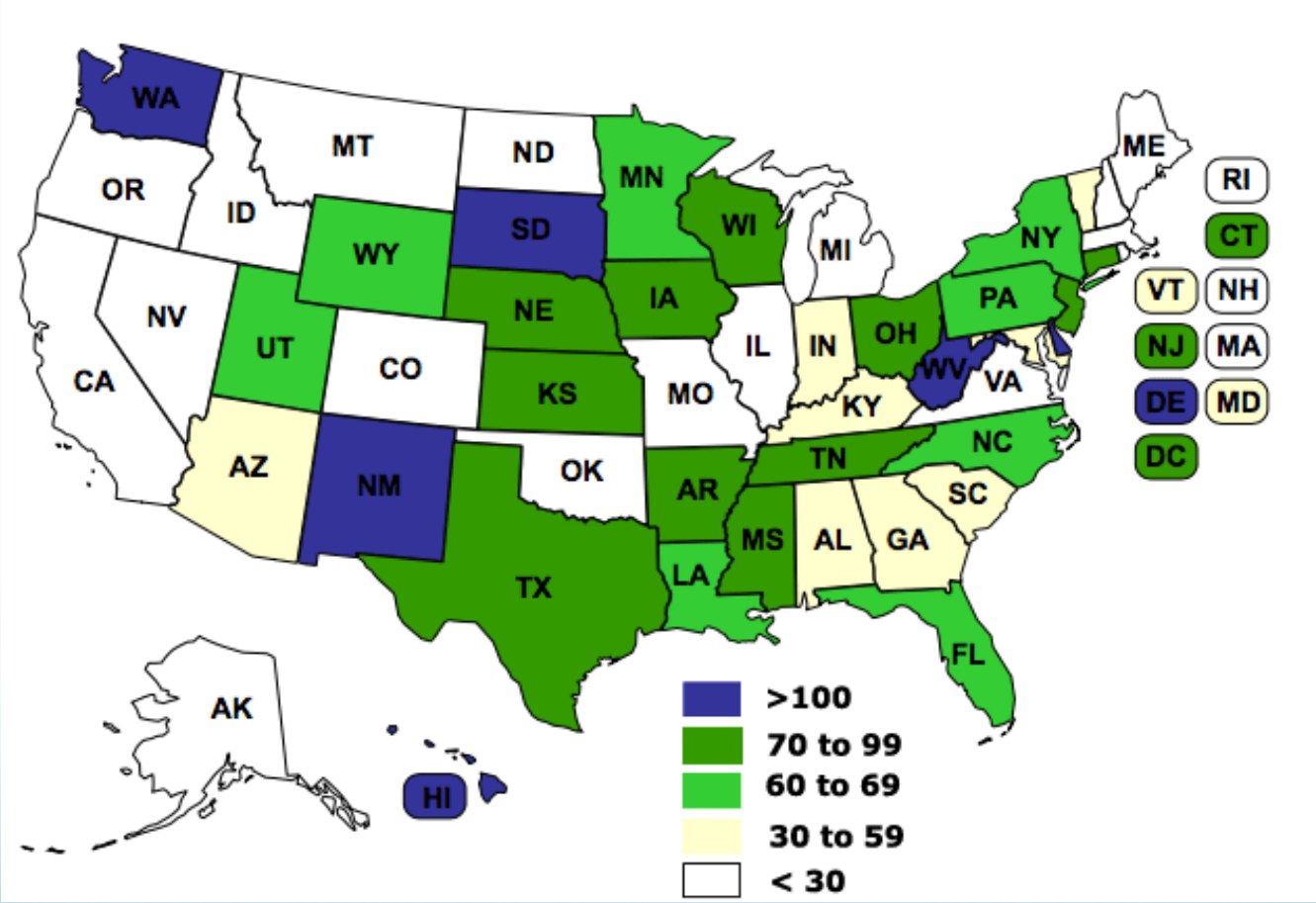
- Massachusetts Used NAICS
- SSTP – They Have Not Tackled Service Industries
- The New NAPCS Shows Promise, But is Still Under Development
  [www.census.gov/napcs]
- Note: **The FTA Survey is NOT a Comprehensive List of Services that Should/Could be Taxed!**

Recent Legislation Since 2007 . . .

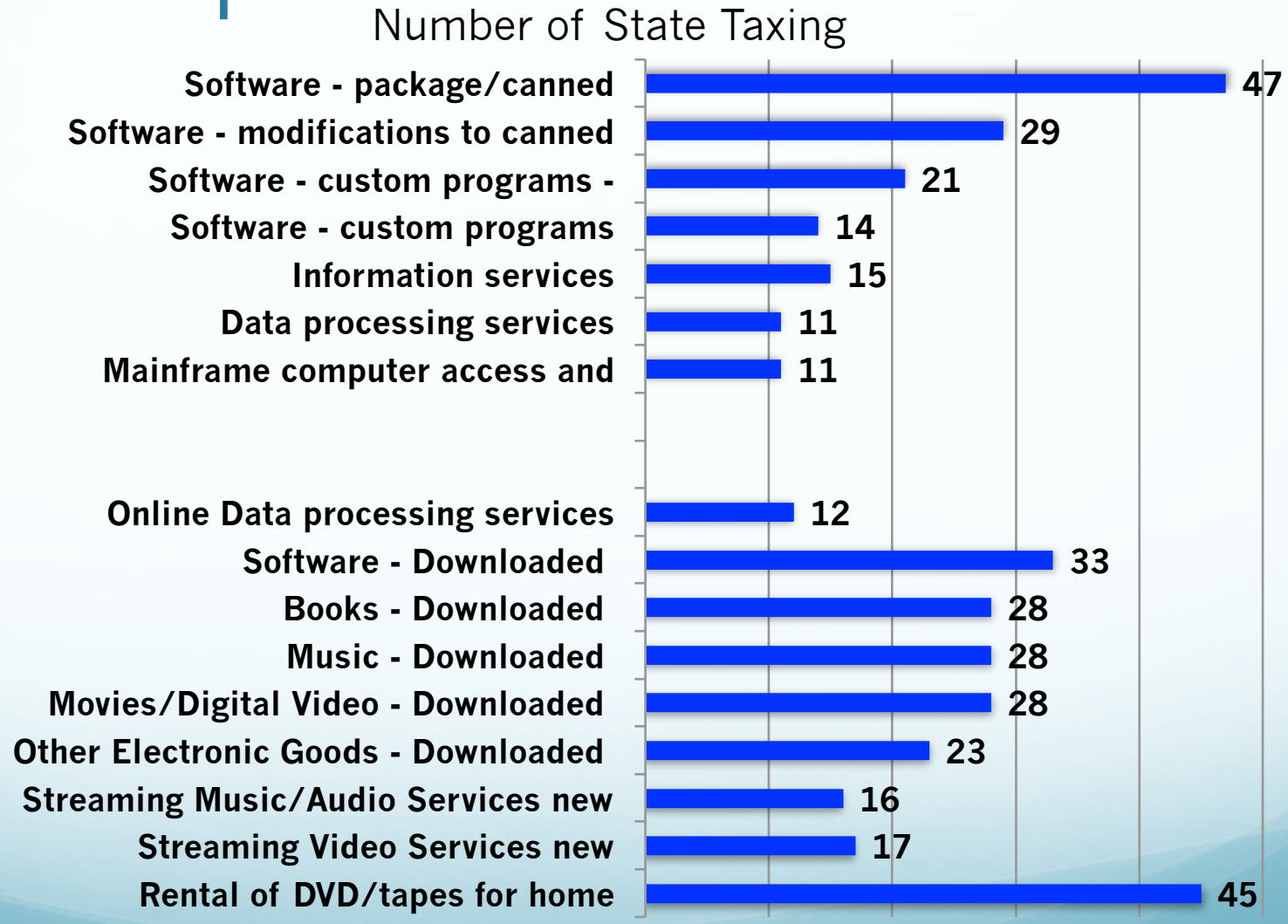
- Connecticut in 2012 and 2015
  - Added Selected Business & Personal Services
  - Increased the Number of Services from 88 to 99
- The District of Columbia in 2012 and 2015
  - Added a Number of Personal Services
  - Increased the Number of Services from 75 to 91
- North Carolina Added Repair Services in 2016
  - Increased the Number of Services from 36 to 62

Number of Services Taxed-2017

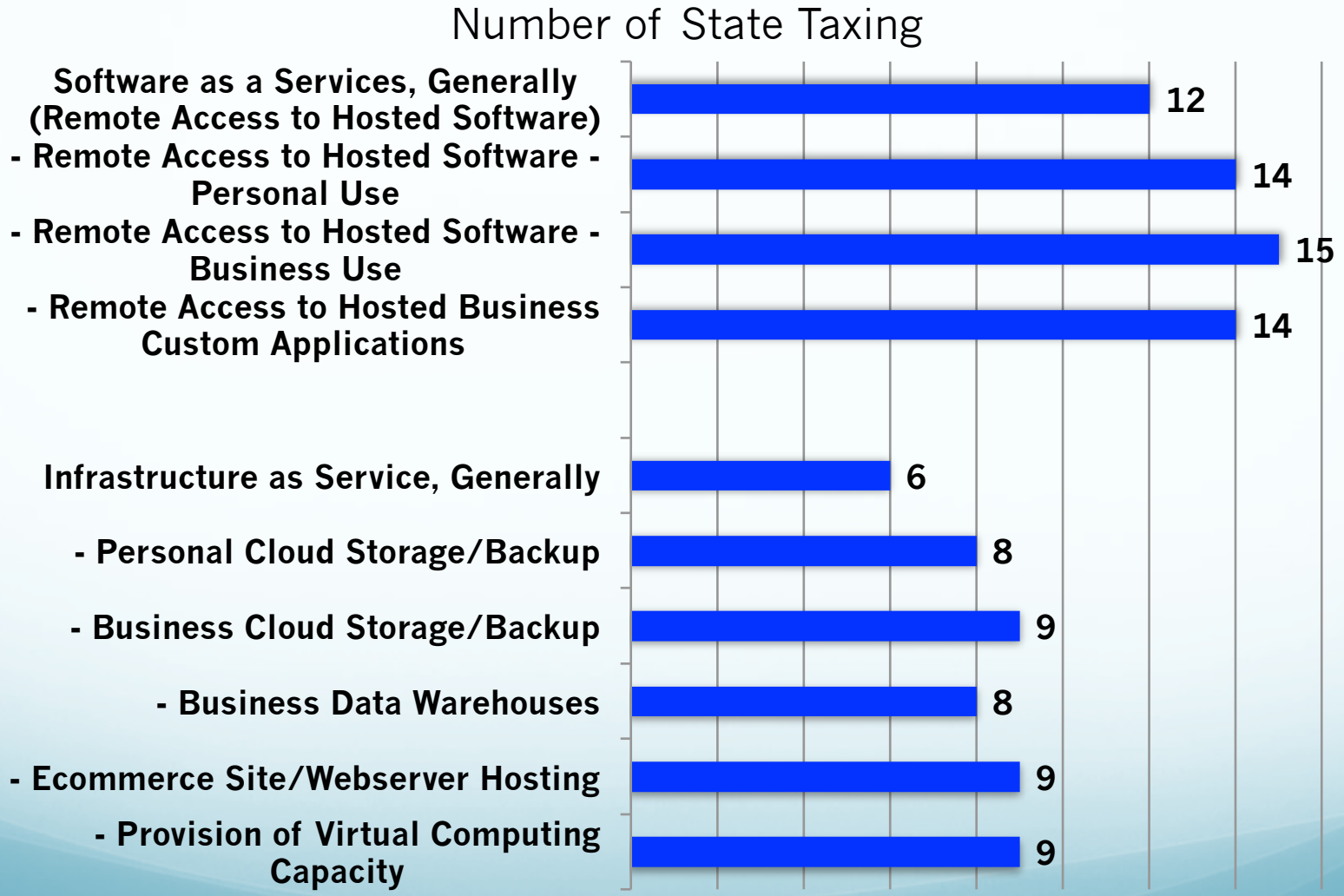
[Preliminary Results]



Software is Taxed . . . But, Computer Services . . .



Few States Tax Cloud Computing Services



Where Do States Go From Here? [Lessons Learned]

- Massachusetts and Florida teach us that only an incremental approach will work.
- A few states have been sucessful in broadening the sales tax to selected services
- Still, State have a long way to go.

Survey, Next Step?

- Spreadsheet with the Preliminary Results are Available on our Private Website [members only]
- The Spreadsheet and Results will be Available on Our Public Website [by the end of the year]
- Improvements to the Survey?
  - Add More Services?
  - Revenue Potential?
  - Weighting Services by Size/Potential?

Questions

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