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- Both of These Broad-Scale Expansions were Repealed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 . . .

Number of State Taxing

- Software - package/canned: 47
- Software - modifications to canned: 29
- Software - custom programs: 21
- Software - custom programs - informational services: 15
- Data processing services: 12
- Mainframe computer access and data processing services: 11
- Online data processing services: 11
- Software - downloaded: 12
- Books - downloaded: 28
- Music - downloaded: 28
- Movies/Digital Video - downloaded: 28
- Other electronic goods - downloaded: 23
- Streaming music/audio services new: 16
- Streaming video services new: 17
- Rental of DVD/tapes for home: 45
Few States Tax Cloud Computing Services

Number of State Taxing

- **Software as a Services, Generally (Remote Access to Hosted Software)**
  - Remote Access to Hosted Software - Personal Use: 14
  - Remote Access to Hosted Software - Business Use: 15
  - Remote Access to Hosted Business Custom Applications: 14

- **Infrastructure as Service, Generally**
  - Personal Cloud Storage/Backup: 8
  - Business Cloud Storage/Backup: 9
  - Business Data Warehouses: 8
  - Ecommerce Site/Webserver Hosting: 9
  - Provision of Virtual Computing Capacity: 9
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 successful 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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