Professional service taxes hurt state and local economies, impacting both businesses and consumers.

Sales taxes on professional services encourage consumers to use out-of-state professionals due to tax differentials across state lines. Because professional services are inherently mobile, many services can be performed anywhere regardless of where the provider or purchaser resides. If a state taxes professional services while other states do not, it encourages consumers to shop outside of state lines for a service provider, putting in-state businesses at a disadvantage. It also discourages multi-state businesses from expanding in the state, which further negatively impacts economic growth and development, resulting in lost jobs, wages, and tax revenues.

Compliance with a sales tax on services is extremely complicated for businesses large and small, and administration by state and local governments is costly. Due to the multi-state nature of customers and service providers, it is often difficult to determine where, when, and how the services take place and what services are actually covered.

While a tax on services would be difficult for all businesses small and large to comply with, it will be particularly burdensome on smaller service providers. What’s more, small and emerging firms often have a need to use outside service-providers that would be taxed (such as external legal counsel or tax-filing services), while larger companies with in-house expertise could avoid taxation for such services as a result of vertical integration.

Sales taxes are regressive in nature. Since sales taxes apply to all taxpayers at the same tax rate, regardless of income level, sales taxes fall harder on lower-income families with less ability to pay. The Institute on Taxation and Economic Policy (ITEP) estimates that the lowest 20 percent of households (based on income) forgo seven percent of their income to pay sales taxes, while the top one percent forgoes less than one percent.

Taxing business inputs, something that nearly all professional services are, is bad tax policy.

Economists and public finance experts agree that business inputs shouldn’t be taxed under the sales tax. When business inputs are taxed, taxes pile up on one another along the production chain, resulting in double and even triple taxation (with taxes becoming embedded in the purchase price) -- a phenomenon known as “tax pyramiding.” Tax pyramiding leads to numerous negative economic effects, such as creating arbitrary price differences between similar services, industries, and business.

A significant share of professional services are business inputs (that is, business services purchased by other business to be used in the production or provision of another good or service.). The Council on State Taxation (COST) estimates that approximated 42 percent of existing state and local sales tax revenues in the 2014 fiscal year were levied on businesses. Taxing professional services will only exacerbate this problem.

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Tax on Services: Action in Recent Years

Legislation seeking to impose sales tax on services (TOS) has been prevalent in state legislatures in recent years. The map below shows states where TOS legislation has been introduced over the last four years. Darker colors indicate higher and/or more recent activity. 2017 saw a record number of TOS bills, with 44 bills introduced in 24 states. Even two states without the tax (Montana and Oregon) had bills that would impose a sales tax. Six states have had services tax legislation every year for the last four years (California, Illinois, Missouri, North Carolina, Pennsylvania, and South Carolina). Despite this activity, no state has enacted and successfully maintained a broad based services tax in decades.

*Montana and Oregon do not currently impose state-level sales taxes, but legislation was introduced in both states that would do so.

**2017** | 44 bills in 24 states
Alabama, California, Georgia, Illinois, Indiana, Kansas, Kentucky, Louisiana, Minnesota, Missouri, Montana, North Carolina, Nebraska, New Jersey, Ohio, Oklahoma, Oregon, Pennsylvania, South Carolina, South Dakota, Utah, Virginia, West Virginia, Wyoming.

**2016** | 29 bills in 19 states

**2015** | 42 bills in 23 states

**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.

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