Maryland Needs an Effective, 21st Century Tax Code

Position Statement in Support of Senate Bill 1001

Given before the Senate Budget and Taxation Committee

Maryland's economy has changed in important ways during the last half century, but our revenue system has not always kept up. Operating a 20th century tax code in a 21st century economy has caused Maryland's revenue growth to stagnate, falling further behind on meeting Marylanders' needs. We should comprehensively reform our tax code to close corporate loopholes, end ineffective tax breaks, and modernize outdated policies. As one part of that effort, expanding our sales tax base to include digital products such as apps and streaming video would bring our tax code more in line with today's economy. This reform could generate as much as $117 million in fiscal year 2021 and $147 million in fiscal year 2025, meaningfully increasing our ability to invest in vital services.[i] For these reasons, the Maryland Center on Economic Policy supports Senate Bill 1001.

Maryland has been underinvesting in the foundations of our communities ever since the Great Recession. We chipped away at public school funding, allowing the number of school districts that were close to full funding under the Thornton formula to fall from 23 out of 24 in fiscal year 2008 to only six by 2017—with more than half of the state's Black students going to school in a district that was underfunded by 15 percent or more. At the same time, we have allowed our investments in other essential services to erode, from public health to reliable transit. Marylanders now face a choice: We can stay the course, skimp on the basics, and watch our economy weaken over time, or we can fix our revenue system to build a thriving future.

Building a truly effective revenue system will require multiple steps, such as closing corporate loopholes, ending ineffective business tax breaks, and fixing a system that currently allows the wealthiest 1 percent of Maryland households to pay a smaller share of their income in state and local taxes than the rest of us do. Updating our sales tax to include the modern iterations of goods that have always been part of the tax base would a step in the right direction, especially if paired with other revenue reforms to ensure our tax code is both effective and equitable.

Only about 30 percent of consumer sales nationwide are subject to sales taxes today, down from about 40 percent throughout the 1970s.[ii] In the music industry alone, worldwide sales of physical media like CDs fell by three-quarters from 2002 to 2017.[iii] Streaming and digital downloads now account for more than 80 percent of all music industry revenue.[iv] Exempting digital products from the sales tax costs Maryland millions of dollars in lost revenue every year—and we can expect to miss out on even more revenue in future years as the economy continues to digitize.

Modernizing our sales tax to include digital products will put Maryland in good company. As early as 2012, 33 states plus the District of Columbia taxed one or more types of digital product—including states as disparate as Alabama, Massachusetts, and Wyoming.[v] Tax policy experts of all ideological stripes recommend applying the same standards to similar activities, without arbitrary exemptions. Maryland's current treatment of digital products violates this principle.

Our tax code today is increasingly outdated, making it unable to raise the resources we need to support a healthy economy. As Marylanders consider the major investments we will need to strengthen the foundations of our economy in future years—from world-class schools to high-quality health care—we should assess how well each component of our revenue system reflects our values as well as today's economy. Applying the same standards to physical and digital products will bring our revenue system into the 21st century and help build thriving communities across Maryland.

For these reasons, the Maryland Center on Economic Policy respectfully requests that the Budget and Taxation Committee make a favorable report on Senate Bill 1001.

Equity Impact Analysis: Senate Bill 1001

Bill summary

Senate Bill 1001 would expand Maryland's sales tax base to include digital products including apps, streaming video, ebooks, digital editions of newspapers and magazines, and other products.

Background

Maryland's sales tax is based primarily on the tangible goods that dominated our economy throughout the 20th century. As our economy has digitized and transitioned toward services, sales tax revenues increasingly lag economic growth and Marylanders' needs for public investments such as education and health care. About 30 states currently include at least some types of digital product in their sales tax base.

Equity Implications

Our growing underinvestment in essential services like education, health care, and transportation harms all Marylanders, and at the same time has outsized impacts on people who face economic roadblocks because of low income or the ongoing legacy of racist policy. Reforming Maryland's tax code to raise adequate revenue would strengthen our ability to invest in the foundations of our economy and reduce barriers that hold back too many Marylanders.

At the same time, sales taxes are known to be among the most lopsided sources of state and local revenue, generally asking more of families who live paycheck to paycheck than of those who have the resources to invest their income. Because digital technology is so pervasive in our lives today—one of the most important reasons why taxing digital products is prudent policy—updating our sales tax would reduce many working Marylanders' purchasing power. Policymakers can mitigate this effect by pairing sales tax reform with more comprehensive tax reforms to ensure that the most powerful among us pay their share, and by strengthening working family tax credits that help many Marylanders afford necessities.

Impact

Senate Bill 1001 would likely **have mixed effects on racial and economic equity** in Maryland.

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[i] Senate Bill 1001 Fiscal and Policy Note.

[ii] Michael Leachman and Michael Mazerov, "Four Steps to Moving State Sales Taxes into the 21st Century," Center on Budget and Policy Priorities, 2013, https://www.cbpp.org/research/state-budget-and-tax/four-steps-to-moving-state-sales-taxes-into-the-21st-century

[iii] "Global Music Report 2018: Annual State of the Industry," IFPI, 2018, https://www.ifpi.org/downloads/GMR2018.pdf

[iv] Recording Industry Association of America, 2019, https://www.riaa.com/facts/

[v] Michael Mazerov, "States Should Embrace 21st Century Economy by Extending Sales Taxes to Digital Goods and Services," Center on Budget and Policy Priorities, 2012, https://www.cbpp.org/sites/default/files/atoms/files/12-13-12sfp.pdf