

Department of Legislative Services  
 Maryland General Assembly  
 2007 Special Session

**FISCAL AND POLICY NOTE**

House Bill 11 (Delegates Gilchrist and Rice)  
 Ways and Means

**Sales and Use Tax - Services**

This bill imposes the State sales and use tax on specified services by expanding the definition of a taxable service.

The bill takes effect January 1, 2008.

**Fiscal Summary**

**State Effect:** General fund revenues could increase by \$262.3 million in FY 2008 and \$590.5 million by FY 2012. Future year revenues represent tax collections on an annualized basis and projected sales tax growth that incorporates a 5.0% decline in taxable sales. General fund expenditures could increase by \$92,300 in FY 2008 and \$189,700 by FY 2012. Future years reflect annualization and inflation.

(\$ in millions)	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
GF Revenue	\$262.3	\$540.4	\$556.6	\$573.3	\$590.5
GF Expenditure	.1	.2	.2	.2	.2
Net Effect	\$262.2	\$540.2	\$556.4	\$573.1	\$590.3

*Note:() = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect*

**Local Effect:** None.

**Small Business Effect:** Meaningful.

**Analysis**

**Bill Summary:** The bill imposes the State sales and use tax on a variety of services listed in **Exhibit 1**.

---

**Exhibit 1**  
**Potential Revenue Resulting from the Taxation of Specified Services**  
**(\$ in Millions)**

<u>Service Category</u>	<u>FY 2008</u>	<u>FY 2009</u>
Cable TV <sup>1</sup>	\$23.5	\$48.4
Vehicle Services	24.1	49.6
Parking	3.7	7.6
Barber/Beauty	7.8	16.1
Physical Fitness Facility or Service	8.1	16.7
Docking/Landing	3.3	6.8
Engineering	67.6	139.2
Storage Service	4.4	9.1
Shoe Repair	0.1	0.2
Tax Preparation	4.3	8.8
Tanning/Massage/Sauna/Steam bath <sup>2</sup>	0.6	1.2
Weighing Machine	*	*
Public Locker	*	*
Dating/Escort	0.1	0.2
Dieting	0.7	1.4
Direct Mail	7.3	15.0
Commercial Photo/Art	1.0	2.1
Stenographic	0.8	1.7
Exterminating	3.4	7.0
Personnel/Temporary Help	56.0	115.3
Management/Consulting/Public Relations	25.2	51.9
Real Property Management	15.2	31.3
Testing Laboratory	2.7	5.6
Sign Painting	0.4	0.9
Interior Decorating	1.5	3.1
Auctioneering	0.2	0.3
Business Brokerage	*	*
Drafting	0.4	0.8
Independent Lecture Bureau	*	*
Printing Brokerage	*	*
Notary Public <sup>3</sup>	*	*
Shop Window Decorating	*	*
<b>Total</b>	<b>\$262.3</b>	<b>\$540.4</b>

\*Estimate unavailable or revenue assumed to be minimal.

<sup>1</sup> May include some already taxable items.

<sup>2</sup> Excludes any health club facility membership.

<sup>3</sup> Many notaries do not charge for services. Revenues are assumed to be minimal.

Source: *U.S. Economic Survey*, 1997 and 2002; *Consumer Expenditure Survey*, 2005 Bureau of Labor Statistics

**Current Law:** The following services are subject to the State sales and use tax:

- fabrication, printing, or production of tangible personal property by special order;
- commercial cleaning or laundering of textiles for a buyer who is engaged in a business that requires the recurring service of commercial cleaning or laundering of the textiles;
- cleaning of a commercial or industrial building;
- cellular telephone or other mobile telecommunications services;
- “900,” “976,” “915,” and other “900”-type telecommunications services;
- custom calling services provided in connection with basic telephone service;
- telephone answering services;
- pay-per-view television services;
- credit reporting;
- security services, including detective, guard, or armored car services;
- security systems services;
- transportation services for transmission, distribution, or delivery of electricity or natural gas, if the sale or use of the electricity or natural gas is subject to the sales and use tax; and
- prepaid telephone calling arrangements.

Although they are not considered services under the State sales and use tax, the tax also applies generally to such items as rentals of tangible personal property, restaurant meals, hotel rooms, and utilities (although specific exemptions are allowed for residential purchases of electricity and gas).

**Background:** The sales and use tax is the State’s second largest source of general fund revenue accounting for \$3.5 billion in fiscal 2008 and \$3.7 billion in fiscal 2009. Historically, the State sales and use tax has been imposed broadly on the sale or use of tangible personal property, but only narrowly on a few specifically enumerated taxable services. Over the past few decades, the growth in sales and use tax revenues has not kept pace with the growth in personal income, as the tax base has eroded due to several factors. One major contributing factor cited for the erosion of the sales tax base is a major shift that has occurred in the national economy from the consumption of goods, the traditional base of the tax, to the consumption of services.

About half the states that impose sales taxes limit taxation of services to utilities, rentals of property, restaurant meals, hotel rooms, and admissions and amusements. Only six states have taxes that generally apply to all services (including two that impose gross receipts taxes on businesses that are not technically sales taxes). About 10 states impose the sales tax broadly on services related to tangible personal property, such as fabrication, installation, and repair services. Several states also tax at least a few other personal services, and a few states also tax some business services.

Among surrounding jurisdictions, New Jersey, Pennsylvania, West Virginia, and the District of Columbia tax a broad range of repair services, including automotive repairs. Pennsylvania and West Virginia tax some business services, and West Virginia also taxes some personal services. Delaware, which does not have a retail sales tax, is considered to

have a broad taxation of services under its gross receipts tax, which applies to most businesses.

**State Revenues:** General fund revenues could increase by \$262.3 million in fiscal 2008 and by \$540.4 million in fiscal 2009 from taxing the additional services listed in the bill. This estimate is based on data from the two most recent (1997 and 2002) *Economic Census* reported from the U.S. Census Bureau, recent *Consumer Expenditures Surveys* conducted by the Bureau of Labor Statistics, and the *Personal Consumption Expenditure Report* prepared by the Bureau of Economic Analysis. Exhibit 1 outlines the potential revenue resulting from each of the services subject to the sales tax under the bill in fiscal 2008 and 2009 assuming a 5.0% reduction in taxable sales. The estimate is based only on those services where there was either consumption or expenditure data available upon which to base an estimate.

Future year revenues are expected to increase by approximately 3% annually. The 5.0% decline in taxable sales reflects sales that no longer are subject to Maryland sales tax for two reasons: (1) the sale does not take place at all because the cost dissuades the purchaser; or (2) the sale is diverted to a neighboring state where the service is not subject to a sales tax or the sales tax rate is lower. To the extent that the impact on sales volume varies from what is projected, sales tax revenues would rise or decline correspondingly.

It is important to note that several of the services that are estimated to generate significant revenue under the bill, including engineering, personnel, and management/consulting are “business-to-business services,” or services that are largely consumed by businesses. To the extent that businesses decrease their purchases of these services, by performing them in-house, for example, the revenue estimate would be lower.

**State Expenditures:** The Comptroller’s Office advises that the bill imposes the State sales tax on some services that are provided by businesses that already collect sales tax. However, those businesses that do not currently collect the sales tax could require more auditing, which would result in the need for additional personnel. As a result, general fund expenditures for the Comptroller’s Office could increase by \$92,337 in fiscal 2008, which accounts for the bill’s January 1, 2008 effective date. This estimate reflects the cost of one revenue specialist, one revenue examiner, and one office clerk to collect and audit the additional sales tax collections. It includes salaries, fringe benefits, one-time start-up costs, and ongoing operating expenses.

Salaries and Fringe Benefits	\$77,977
Operating Expenses	<u>14,360</u>
<b>Total FY 2008 State Expenditures</b>	<b>\$92,337</b>

Future year expenditures reflect • full salaries with 4.5% annual increases and 3% employee turnover; and • 1% annual increases in ongoing operating expenses.

**Small Business Effect:** As discussed above, increasing the number of services subject to the sales tax in Maryland may result in a decline in consumer purchases of these services from State providers. To the extent possible, residents may purchase more services in neighboring states where these services are not taxed (or are taxed at a lower tax rate) or may choose not to purchase these services at all. The extent to which this may happen cannot be reliably estimated, but the majority of Maryland residents live within a short distance to a neighboring state and therefore could have access to service providers located in other states. While the percentage will vary from service to service, it is likely that many of the service providers in each of the service categories in Exhibit 1 are small businesses.

### **Additional Information**

**Prior Introductions:** This bill was introduced as HB 448 in the 2007 regular session. The House Ways and Means Committee took no action on the bill. In addition, similar bills were introduced as HB 1364 in 2004 and HB 1337 in 2001. The House Ways and Means Committee took no action on HB 1364 and reported HB 1337 as unfavorable.

**Cross File:** None.

**Information Source(s):** Comptroller's Office, Department of Legislative Services

**Fiscal Note History:** First Reader - November 1, 2007  
mll/hlb

Analysis by: Michael Sanelli

Direct Inquiries to:  
(410) 946-5510  
(301) 970-5510