HB 614

Department of Legislative Services

Maryland General Assembly
2008 Session

FISCAL AND POLICY NOTE

House Bill 614 (Delegate Ali)
Ways and Means

Sales and Use Tax - Elective Cosmetic Procedures

This bill expands the definition of taxable service so that the State sales and use tax is imposed on specified elective cosmetic procedures, except in cases where the cosmetic medical procedure is considered medically necessary, including orthodontics.

The bill takes effect July 1, 2008.

Fiscal Summary

State Effect: General fund revenues could increase by $34.8 million and Transportation Trust Fund (TTF) revenues could increase by $2.4 million in FY 2009. Future year revenue increases are based on projected sales tax revenue growth. Expenditures would not be affected.

($ in millions)	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
GF Revenue	$34.8	$36.6	$38.4	$40.3	$42.3
SF Revenue	2.4	2.5	2.7	2.8	2.9
Expenditure	$0	$0	$0	$0	$0
Net Effect	$37.2	$39.1	$41.1	$43.1	$45.3

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

Local Effect: None.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: Elective cosmetic procedures include, teeth whitening, laser eye surgery, breast reduction or augmentation, rhinoplasty, face lift, liposuction, gastric bypass surgery, laser hair removal, tattooing, or body piercing.

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).

In addition, Chapter 3 of the 2007 special session expanded the definition of taxable service to include computer services beginning in fiscal 2009 – the provision terminates on June 30, 2013.

Background: 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 Fiscal Effect: Total sales and use tax revenues could increase by $37.2 million in fiscal 2009 from taxing the specified elective cosmetic procedures. In addition to increasing the sales and use tax rate from 5% to 6%, Chapter 6 of the 2007 special session also altered the distribution of sales and use tax revenues by requiring that 6.5% of revenues, after specified distributions, be diverted to TTF beginning in fiscal 2009. As a result, imposing the sales tax on elective cosmetic procedures could increase general fund revenues by $34.8 million and TTF revenues by $2.4 million in fiscal 2009. The estimate is based on the following facts and assumptions:

- the American Society of Aesthetic Plastic Surgery estimates that there were 11.5 million cosmetic surgeries performed nationally in 2006; the average cost of each procedure is $2,500;
- the American Academy of Cosmetic Dentistry indicates that teeth whitening generated approximately $300 million in revenues in 2005;
- TLC Vision estimates that there were 1.3 million laser eye surgeries performed in 2007; the average cost for each procedure is estimated to be $2,500;
- Maryland represents 1.86% of the total U.S. population; and
- sales of these procedures will increase 5% annually.

To the extent that any of these procedures is determined to be medically necessary, the total amount of sales and use taxes collected would decline accordingly.

The estimate reflects an estimated 6.0% decline in the taxable base resulting from the imposition of the sales tax on these services. Future year revenues are assumed to increase by approximately 5% annually. The 6% decline in taxable sales reflects sales that no longer are subject to Maryland sales tax for two reasons: • the sale does not take place at all because the cost dissuades the purchaser; or • the sale is diverted to a neighboring state where the service is not subject to a sales tax or the 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.

Small Business Effect: To the extent that the additional sales tax rate encourages consumers to shift purchases to out-of-state and away from Maryland service providers that are small businesses, these small businesses could experience a meaningful negative impact. Based on estimated annual taxable sales of approximately $660 million, a 6.0% decline in sales would result in a decline of about $40 million in gross taxable sales.

Additional Information

Prior Introductions: None.

Cross File: None.

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

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