Maryland Needs an Effective, 21st Century Tax Code

Position Statement in Support of House Bill 1354

Given before the House Ways and Means 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 We should comprehensively reform our tax code to close corporate loopholes, end ineffective tax breaks, and modernize outdated policies.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 luxury services would bring our tax code more in line with today's economy. This reform would generate $338 million or more in new revenue over five years, meaningfully increasing our ability to invest in vital public services.[i] For these reasons, the Maryland Center on Economic Policy supports House Bill 1354.

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. House Bill 1354 would move our tax code in the right direction for two reasons:

- Household consumption has shifted significantly during the last half century, with consumption of generally taxable tangible goods declining and consumption of generally untaxed services increasing. Only about 30 percent of consumer sales nationwide are subject to sales taxes today, down from about 40 percent throughout the 1970s.[ii] By expanding the number of services subject to sales tax, House Bill 1354 would make our tax code more effective and could slow the long-term erosion of our tax base.
- The share of income going to the wealthiest 1 percent of Maryland households has doubled since the late 1970s.[iii] Because our tax code is upside-down—allowing the wealthiest individuals to pay a smaller share of their income in state and local taxes than the rest of us do[iv]—growing inequality can also slow revenue growth. Many of the services taxed under House Bill 1354, such as country club memberships, are likely disproportionately consumed by wealthy individuals. For this reason, this bill has potential to make our tax code both more effective and more equitable.

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. Expanding the sales tax base to include luxury services 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 House Ways and Means Committee make a favorable report on House Bill 1354.

Equity Impact Analysis: House Bill 1354

Bill summary

House Bill 1354 would expand Maryland's sales tax base to include luxury services such as travel arrangement or reservation services, gold course or country club membership, and interior design or decorating services.

Background

Maryland's sales tax is based primarily on the tangible goods that dominated our economy throughout the 20th century. As our economy has transitioned toward services, sales tax revenues increasingly lag economic growth and Marylanders' needs for public investments such as education and health care.

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.

It is possible that House Bill 1354 would improve the equity of Maryland's tax code. Many of the services the bill would tax are likely disproportionately consumed by wealthy individuals, such as country club memberships. However, detailed data would be necessary to accurately estimate who would have the most increased tax responsibilities under House Bill 1354. Generally, sales taxes are 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. The best approach to making Maryland's tax code more effective and more equitable would pair sales tax reform with more comprehensive tax reforms to ensure that the most powerful among us pay their share and would strengthen working family tax credits that help many Marylanders afford necessities.

Impact

House Bill 1354 **may improve on racial and economic equity** in Maryland.

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[i] House Bill 1354 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] Christopher Meyer, "What a $15 Minimum Wage Would Mean for Maryland: Good Jobs, Secure Families, and a Healthy Economy," Maryland Center on Economic Policy, 2018, http://www.mdeconomy.org/minimumwage/

[iv] Meg Wiehe, Aidan Davis, Carl Davis, Matt Gardner, Lisa Gee, and Dylan Grundman, "Who Pays? A Distributional Analysis of the Tax Systems in All 50 States," Institute on Taxation and Economic Policy, 2018, https://itep.org/wp-content/uploads/whopays-ITEP-2018.pdf Maryland-specific data available at https://itep.org/whopays/maryland/