

To: Members of The House Ways and Means Committee

From: DeAndre Morrow, Legislative Committee, Tax Council

Subject: HB1515 – Sales and Use Tax -Rate Reduction and Services

Date: March 11, 2024

Position: **Oppose**

The Maryland State Bar Association (MSBA)’s Taxation Section’s Tax Council **opposes House Bill 1515 - Sales and Use Tax – Rate Reduction and Services.**

House Bill 1515 proposes an unprecedented expansion of Maryland’s sales tax to a broad array of services, a move that merits a thorough examination beyond its fiscal impact to consider its long-lasting implications on societal equity, the administration of taxes, and Maryland’s economic landscape.

Overview of House Bill 1515 (“HB 1515”)

The current tax regime taxes the purchase of tangible personal property and a handful of very specific services. By revising the definition of “taxable price” HB 1515 systematically removes exclusions for various services that were previously not subject to tax. Notably, it proposes that professional services, which are explicitly excluded under the current statutory regime, fall within the ambit of taxable services. This fundamental change means that professional services, such as legal services, financial services, and taxation services, will become taxable to businesses and individuals alike, altering consumer behavior in the business landscape in our state significantly.

Moreover, HB 1515 also expands the scope of “taxable services” dramatically. Where the existing law confines taxable services to 13 enumerated services, HB 1515 proposes to broaden this to encompass “any activity engaged in for a buyer for consideration,” with only a few exceptions. This sweeping change not only increases the tax base but introduces a level of ambiguity around what precisely constitutes a taxable service, potentially complicating compliance, and enforcement efforts. Expanding however, the simplicity can lead to complexity and practical application. This broad definition requires businesses to assess a vast array of services for taxability, including potentially ambiguous and novel services not traditionally viewed as taxable. Determining whether a specific service falls within this expanded definition can become challenging, especially for innovative or

evolving service offerings, leading to uncertainty and inconsistency in tax compliance and enforcement.

Tax Pyramiding 101

HB 1515 introduces a framework for business inputs — services essential to the production of other goods and services — are subject to sales tax, laying the groundwork for tax pyramiding. Tax pyramiding occurs when a tax is applied multiple times throughout the production and distribution stages of a service, leading to a situation where the same value was taxed repeatedly. The effect is often an increase in the final costs of the service for consumers, as businesses often pass these accumulated taxes down the supply chain until they reach the end buyer. This layering of taxes not only disrupts market equilibrium but disproportionately affects our most vulnerable populations, exacerbating income inequality. The regressive nature of such a tax structure warrants a critical examination.

Dissuading the Use of Essential Professional Services

The expansion of the sales tax to encompass professional services stands to significantly alter the landscape for tax and legal professionals and their clientele. By removing the exemption for professional services, the bill not only increases the operational costs for these practitioners but also makes accessing vital tax preparation and tax legal advisory services more financially burdensome for Maryland residents and businesses. This shift could disproportionately affect those of modest means, complicating their ability to comply with tax laws and potentially discouraging engagement with vital professional services. Many Maryland constituents are members of low-income households but are not eligible to benefit from pro bono legal services because the threshold for eligibility is too low, or, there simply isn't a sufficient supply of lawyers to meet their pro bono needs. A tax on tax and legal services could be the dispositive factor that determines whether someone goes into court with adequate representation. Such an outcome not only undermines the fiscal well-being of individual taxpayers but also potentially complicates tax compliance which will have invariable effects on tax administration and efficiency.

Increasing Barriers to Entrepreneurship and Economic Innovation

HB 1515 broadening of the tax base presents a substantial barrier to entrepreneurship and innovation. By including essential business services in that taxable category, this bill raises financial barriers for startups and small businesses potentially stifling innovation and economic diversity in Maryland. The additional financial burden could deter entrepreneurs from establishing or growing their businesses in the state, affecting Maryland's economic landscape and long-term competitiveness.

Administrative Quagmire

HB 1515's broad overhaul of the sales tax regime across the service spectrum fails to account for the Herculean lift required to administer such a substantial shift overnight. In 2007, the Maryland legislature imposed a sales tax on computer services, effective on July 1, 2008. The tax applied to web design, facilities management, custom computer programming, data center support, systems integration, installation, and maintenance, but not internet access, computer training, and data entry. Prior to the imposition of this tax, other states, such as Pennsylvania and Florida had already repealed their version of this tax due to difficulties in implementation. Not only were there issues such as situs, but questions as to whether a service was one of the services identified as taxable, and when it morphed into or ceased being that taxable service. More obvious issues included the identification of where the service was rendered, the situs of the sale or its delivery, and the handling of transactions between affiliates. A tremendous backlash ensued from the tech community and many businesses expressed an intent to move over state lines to remain competitive. In light of these occurrences, the tax was repealed before it became effective.

In conclusion, while the motivations behind HB 1515 are understood, the proposed method of expanding the sales tax base is fraught with significant socioeconomic and practical challenges. Our testimony, built on technical analysis, case studies, and legal considerations, calls for thoughtful attention of the path in favor of one that not only safeguards Maryland's economic viability but also champions the principles of equity, justice, and a transparent path to tax compliance.

For the reason(s) stated above, the MSBA's Taxation Section **opposes HB 1515 and urges an unfavorable Committee report.**

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