

Monday, October 12, 2009

## Study: Taxing services could yield state \$6.8B

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The non-partisan Indiana Fiscal Policy Institute this morning released a new study exploring the ramifications of expanding the state's sales tax to include services.

In its last fiscal year, Indiana raised \$5.7 billion from its 7-percent sales tax, which applies to the sales of most tangible goods, with exemptions for items such as prescription drugs, groceries and newspapers.

According to the IFPI study, Indiana could raise as much as another \$6.76 billion annually if it extended its sales tax to include all service transactions. Even if Indiana exempted medical and legal services, Indiana could raise almost \$4.5 billion from an expanded sales tax, according to IFPI.

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Such figures are sure to appeal to legislators in Indiana's General Assembly, who struggled mightily over recession-driven spending cuts this spring. A special session of the Legislature was ultimately necessary to craft a two-year state budget.

Indiana government's economic picture hasn't improved much since then. On Oct. 8, Gov. Mitch Daniels revealed Indiana's revenue for the quarter ended Sept. 30 was \$254 million less than previously predicted, despite the fact that Indiana's revenue forecast has been repeatedly revised downward.

New revenue could help fill such gaps. But an expansion of Indiana's sales tax has many potential drawbacks, which the IFPI study details.

For starters, Indiana's 7-percent state sales tax is already the highest in the Great Lakes region. Extending it might prompt Indiana residents to seek services elsewhere. Indiana is currently tied with Mississippi, New Jersey, Rhode Island and Tennessee for the second-highest sales tax in the nation. Only California's 7.25 percent tax is higher.

The IFPI study points out that the effective sales tax rate is actually higher in some regions because of local sales taxes tacked onto state sales taxes. Alabama, for example, has a 4-percent sales-tax rate, but certain localities there have their own 6-percent sales taxes, creating a 10-percent total tax.

Most states, including Indiana, already tax a few services, such as public utilities, hotel-room rentals and stadium admissions, according to IFPI. But only a handful, such as South Dakota, West Virginia, Hawaii, New Mexico, Delaware and Washington, tax more than a handful of services.

Indiana currently ranks 39th among states for the number of services it taxes, taxing 24 of 168 services surveyed by the Federation of Tax Administrators.

The logistics of expanding the sales tax to additional services would be challenging for some businesses. IFPI points out it could be difficult for many businesses to levy such a tax. Businesses that already sell some goods would have an easier time than pure-service providers. For example, a cosmetologist that now collects taxes on the shampoos and conditioners its sells while exempting styling services, would simply have to stop segregating taxable and nontaxable sales.

But other businesses that sell no tangible goods would find they suddenly must establish a relationship with the Indiana Department of Revenue and maintain a whole new type of record. The cost could be significant, IFPI points out, particularly for small businesses.

"Of the major sources of revenue available to the state, broad-based taxation of services is the only one yet to be tapped by the State of Indiana," wrote the IFPI report's author, Earl Ryan. "The revenue possibilities are great, and it would bring a degree of equity to the tax system. At the same time, defining the base would be difficult, both conceptually and politically, and the cost of collecting the tax on the part of both the state and the taxpayers would be significant."

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