

D.C. Tax Revision Commission Policy Options
Policy Option #1: Expand the Sales Tax to Additional Services

MEMORANDUM

Proposal: Extend the sales tax to additional services

Tax Type: Sales

Origin: William Fox

Commission Goal: Broaden the tax base

Current Law

Many services are exempt from the general sales tax (5.75%) in D.C. These exemptions exist because the sales tax started as a levy on goods but not all consumption.

Proposed Change

Levy the sales tax on select services. William Fox suggested the following additions:

- Construction contractors
- Carpentry and other construction related services
- Storage of household goods
- Mini-storage
- Water for consumption at home
- Barber and beautician services
- Carpet and upholstery cleaning
- Health clubs and tanning studios
- Carwashes
- Bowling alleys and billiard parlors

Reason for Change

The sales tax base has declined both nationally and in D.C. as consumers shift their spending to services. In 1979, services accounted for 47.4% of total personal consumption expenditures. In 2011, services accounted for 66% of personal consumption. To maintain revenue with a diminished sales tax base, many states and localities have increased the sales tax rate. Extending the sales tax to certain services is an alternative to future rate hikes (or a means for lowering the current rate).

Pros

- Taxing additional services broadens the D.C. sales tax base and may generate new tax revenue and/or allow for a lower sales tax rate.
- Expanding the base to more services addresses both horizontal equity (treating transactions equally) and vertical equity (services are disproportionately consumed by wealthy consumers while low-income consumers are more reliant on goods).

- The services presented for consideration in this memo are linked to tangible goods and/or real property located in D.C. This prevents consumers from avoiding the tax by making purchases in other jurisdictions and limits any negative effects of the tax on the D.C. economy/businesses.

Cons

- Consumers might still travel to neighboring jurisdictions to consume a service that is now taxed in D.C., but untaxed in Maryland or Virginia.
- Policymakers in numerous states have resisted similar efforts to expand the sales tax to services for political reasons.
- The list of proposed services excludes most of the major services in D.C. (lawyers, accountants, consultants, etc.) and therefore revenue gains and/or opportunities for rate reduction are limited.

Revenue Impact

The Office of Revenue Analysis estimates the following revenue increases in the first year of implantation:

Apply the Sales Tax to Specific Services	
Water consumption for home ¹	\$2 million
Storage of household goods/mini storage	\$0.5 million
Barber and beautician services	\$7 million
Carpet and upholstery cleaning	Less than \$0.5 million
Health clubs and tanning studios	\$5 million
Car washes	Less than \$0.5 million
Bowling alleys and billiard parlors	\$0.7 million
Construction contracts	\$12 million
TOTAL if all services listed are taxed	\$28.2 million

¹ This estimate is based on NAICS Code 454390 and is broader than water consumption at home. This industry comprises establishments primarily engaged in retailing merchandise (except food for immediate consumption and fuel) via direct selling, such as in-house sales (i.e., party plan merchandising), truck or wagon sales and portable stalls (i.e., street vendors).