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SALES TAX & COMPLIANCE

More Taxation on Services Expected this Year

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Gail Cole • Jan. 25, 2022



Though the United States economy is “dominated by services-oriented companies,” most states currently tax only select services, if any. That could change in 2022:

Legislation seeking to tax services has been introduced in Indiana and Nebraska, and other states could follow their lead.

[From the [Avalara blog](#).]

Indiana sales tax would apply to most services starting in 2023

A bill seeking to tax sales of services and phase out the corporate income tax has been introduced in Indiana. Should [Senate Bill 372](#) become law, Indiana sales tax would apply to most services in the state starting January 1, 2023. The bill also seeks to reduce individual income tax rates and gradually eliminate the Indiana corporate adjusted gross income (AGI) tax.

SB 372 proposes to extend [Indiana state sales and use tax](#) (currently 7%) to “any activity engaged in for another person, if the person purchases the service as the end user of the service for consideration.” However, the following services would be exempt:

- B2B transactions (i.e., “the wholesale sale of services that are performed by a business and rendered to another business for the use or consumption in the production of tangible personal property or the delivery of other services that are for sale”)
- Government services
- Services rendered by an employee

According to the [bill’s fiscal analysis](#), extending the state’s 7% sales and use tax to services starting January 1, 2023, “would have an estimated net impact of \$1,936.2 M to \$2,204.2 M in FY 2023 and \$4,902.9 M to \$5,581.4 M in FY 2024.”

The bill would also implement a social media provider surcharge tax on social media providers that derive “economic benefit from the data individuals in Indiana share with the company” and have a public social media platform, more than 1 million active Indiana account holders, and annual gross revenue (from social media advertising services in Indiana) of at least \$1 million.

Nebraska sales tax would apply to services starting October 1, 2022

A 2021 bill that was carried over to 2022 would broaden sales tax to services and gradually lower the state sales tax rate. [LB 422](#) presumes services are taxable “unless a specific sales tax exemption applies.”

The measure defines “service” as “all activities that are engaged in for other persons for a consideration and that involve predominantly the performance of a service as distinguished from selling or leasing tangible personal property.” Services “rendered by an employee to his or her employer” would not be subject to tax.

If LB 422 succeeds this go-round, the tax on services would take effect October 1, 2022.

Other states could propose taxing services in 2022 or beyond

Proposals to tax certain services could surface in other states as well — especially states that have recently tried to expand their sales tax. There’s a lot of opportunity for movement on this front, given that Hawaii, New Mexico, and South Dakota are the only states that tax all but specified services.

[Texas sought to tax many services](#) in 2021, including specified professional services. West Virginia Governor Jim Justice proposed taxing professional services during his [2021 State of the State address](#), when he also floated a plan to increase the sales tax rate and levy an additional tax on cigarettes and soda, to make West Virginians “healthier and better.” We’ll see what he says in 2022. (Governor Justice was scheduled to deliver the 2022 State of the State address on January 11, but [postponed it after coming down with COVID-19](#).) Many services are already subject to West Virginia sales tax, though [personal services](#), [professional services](#), and [public services](#) are not.

[West Virginia also looked at taxing digital advertising services in 2021](#), as did Connecticut, Indiana, Massachusetts, Montana, New York, Texas, Washington, and Washington, D.C. (Maryland currently has the nation’s only digital advertising tax). [Wyoming considered a digital streaming tax](#) in 2021, and the West Virginia State Tax Department let it be known that [streaming services were subject to sales tax](#) after all.

Why taxing services can be tricky

Despite obvious potential for revenue gains, attempts to tax services typically face pushback. Approximately 23 states proposed taxing at least some services in 2017, and [most measures failed](#). [Nebraska tried to broaden sales tax to services](#) — unsuccessfully — in both 2020 and 2021. Where such proposals have succeeded, like [Washington, D.C.](#), they typically targeted services not backed by powerful lobbyists.

Scott Peterson, vice president of government relations at Avalara, offers some insight. He says the complicated part of tax policy changes like the one being considered in Indiana isn't estimating the amount of tax a different tax will produce versus the current tax; it's balancing who bears the tax burdens. "This idea will be opposed by many businesses, including those that will become new tax collectors and those who purchase lots of services. This will also be opposed by those who believe income taxes are a more equitable method of apportioning the state's tax burden among the people and corporations doing business in the state."

He also notes that attorneys and accountants, who would become tax collectors under SB 372, "have very good lobbyists."

Learn more about issues affecting sales tax compliance this year in [Avalara tax changes 2022](#).

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Gail Cole is a Senior Writer at [Avalara](#). She's on a mission to uncover unusual tax facts and make complex laws and legislation more digestible for accounting and business professionals.

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