More states consider imposing a sales tax on ride-sharing services

David M. Kall | Wednesday, August 10, 2016

In *Why Sales Taxes Should Apply to Services*, the Institute on Taxation and Economic Policy (ITEP) made its case for the sensibility of taxing haircuts, car repairs and the like, which has become more common of late. The historical omission is "largely a historical accident" because in the olden days, officials lacked the means by which to monitor the sales of services. But now, states are more adept at capturing this activity, and so have the means for collection and enforcement. In 2015, sales of services accounted for 67 percent of household spending, so states that have not modernized their policies are leaving much revenue on the table.

Doing so would remove the disadvantage imposed on taxpayers who consume more goods than services, enable states to broaden the tax base to collect more revenues without raising taxes, and could help stabilize budgets.

Broadly speaking, this is consistent with what economists are suggesting for managing the new economy. Last week, we wrote a piece about the challenges that face some state governors as they grapple with 21st century ways of living and doing business. For example, lawmakers in Massachusetts have proposed a new "Airbnb" tax that would regulate the young online home rental/hospitality industry and help level the playing field. At this time, Gov. Charlie Baker is reluctant to pass any new taxes, even if they would eliminate the competitive advantage that short-term room rental concerns currently enjoy.

The ride-sharing business, which includes upstarts like Uber and Lyft, is under similar scrutiny. Last week, a Bloomberg article pointed out that while only two states, Rhode Island and Nevada, now require transportation network companies (TNCs) to collect and remit sales taxes, others are considering it. Among the policy questions being debated are how taxes on TNCs would compare to those imposed on the traditional livery industry, at what level of income individual drivers should be taxed, and the extent to which the TNCs themselves should have responsibility for compliance.

Existing ride-sharing tax laws

In Rhode Island, the Department of Revenue's Division of Taxation published a notice alerting taxpayers that a 7 percent sales and use tax on TNCs was to go into effect on July 1, 2016. There, a TNC is defined as an entity that uses a digital network to connect transportation network company riders to transportation network operators who provide prearranged rides. In addition to requiring any TNC to charge, collect, and remit sales and use tax to the Division of Taxation, the law also requires any TNC to 1) file a business application and registration form with the Division of Taxation; and 2) obtain a permit from the Division of Taxation to make sales at retail.

In Nevada, Assembly Bill 175 created a structure under which the Public Utilities Commission of Nevada would regulate transportation network companies, including establishing insurance, permit, fee and annual assessment protocols. The Nevada law defines a transportation network company as "an entity that uses a digital network or software application service to connect passengers to drivers who can provide transportation services to passengers," and imposes a 3 percent excise tax.

What is notable about Nevada's law is that traditional taxi companies are not subject to the new 3 percent tax.

States that do not want to tax TNCs

Bloomberg also highlighted certain states that take the opposite approach. In Arizona, for example, Gov. Doug Ducey signed legislation in May that imposes stricter restrictions on when cities and counties can subject sharing economy businesses to new regulatory burdens. It essentially prohibits local government entities from regulating those companies in the same way they would regulate businesses that provide goods and services directly to customers.

In New Jersey, lawmakers proposed legislation in May 2016 that prohibits the state, as well as counties and municipalities, from imposing a tax or fee that applies only to TNCs.

In Iowa, Gov. Terry Branstad signed House File 2414 into law on May 9, 2016. It provides for the regulation of TNCs and taxicabs, but as Bloomberg notes, the Iowa Department of Revenue has determined that TNCs aren't providing a taxable service.

In total, 34 states have passed laws that regulate TNCs with requirements related to safety, insurance and, in some cases, restrictions on where drivers can pick up passengers.

Unresolved issues

As touched on above, Massachusetts Gov. Charlie Baker wants to level the playing field between traditional and new economy ride-share providers, but does not want to pass new taxes. Beyond this sort of reluctance to raise taxes, Bloomberg highlighted other considerations, one of which is whether traditional transportation companies, like livery services, are already subject to state sales and use tax rules. Another is the difficulty of enforcement and compliance associated with the sharing economy in general.

Bloomberg cited two economists who thought several tactics could help: industry-specific Internal Revenue Service guidance; clarification of how existing tax rules apply to ride sharing; and guidance on interpretation of the 1099-K, the income reporting document for receipts of electronic payments. Beyond this, educating drivers could also make a difference, as many of them in TNCs are unaware of their obligations, and may not even understand their status as small business owners, even when they receive their 1099 statements.

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Team member bio