

## **GeTtin' SALTy Podcast – Episode 61**

Nikki Dobay: Hello and welcome to GeTtin' SALTy, a state and local tax policy podcast hosted by Greenberg Traurig. My name is Nikki Dobay, shareholder in the Sacramento, California, and Portland, Oregon, offices. I am really excited about today's conversation. I have two wonderful guests and we are here to talk about most things Washington. We might deviate to another state for just a moment, but very pleased to have Representative April [00:00:30] Berg, who represents the 44th district in Washington with me today, as well as the esteemed Professor Richard Pomp, who many of you know and love, and teaches many, many things, SALT at UConn Law School as well as NYU. So Representative Berg and Professor Pomp, thank you so much for joining me today for this conversation.

Representative ...: Thank you for having us.

Professor Richa...: Yeah, it's a pleasure.

Nikki Dobay: Well, [00:01:00] wonderful. Well, many of the listeners of the podcast know that Washington had some things happen during the legislative session this year. I think they've gotten plenty of attention. So April, I'm going to start with you and ask you to provide an overview, some insights into the 2025 Washington legislative session, and specifically the bill that has really gotten folks talking, [00:01:30] Senate Bill 5814.

Representative ...: Yeah, well, we did get a little bit of attention this year. We had some big tax proposals and we raised quite a bit of revenue. Putting that into context, we did have a budget shortfall. We made about 8 billion in cuts, and then we raised about 8 billion through new revenue proposals. Yeah, so the biggest one I think that's gotten most attentions and most of your listeners will be interested to hear about is our sales tax on services.

Nikki Dobay: [00:02:00] Yes.

Representative ...: And so we have quite a few new classes of services that now will have sales tax applied to them. And some of these services, they range everything from temporary staffing, to security staffing, to digital ad tax. So it's quite a new world. I will put the context, folks who listen probably know that Washington is very different than other states. We don't have an income tax. We don't have all the legs of the stool of taxation. So what we're looking at is B& [00:02:30] O tax, property tax and sales tax. And as we move to more of a service-based economy from a consumption based economy, it behooved us as policymakers to look at what new revenue opportunities there were around services.

Nikki Dobay: Yeah, and so you definitely got a lot of folks' attention with that bill. There was a pretty robust effort to get the governor to veto. He did not do that, and most of those new provisions on services [00:03:00] are set to go into effect October 1st, so very soon after this podcast comes out. But Professor Pomp, I want to circle back to you now and ask you your thoughts on broadening the sales tax base to include services and really specifically advertising services as enacted. I

think Washington's bill was supposed to cover all advertising services. There were many carve outs which now really [00:03:30] have only left digital advertising in the bill. So tell the listeners from your perspective, is this good policy, bad policy? What are you thinking?

Professor Richa...: Well, services right now are taxable under every state's sales tax. Look around the room, I am looking at a microphone, a laptop, table, chairs. Services are incorporated in [00:04:00] the price of those goods, that things embody capital and labor, and that labor element, that service element, is part of the sales price of the ultimate sale to the consumer. So it's a false argument, should we tax services? We're already taxing services. We're taxing thousands of services as long as they're embodied in tangible personal property. So the question really is, when those services are provided [00:04:30] in isolation, should they be taxable? And the answer is there's no reason not to tax a service that would've been taxed had it been incorporated in a good.

Now, the problem when it comes to services is that we tax the wrong kinds of services because that's where the money is. A sales tax is not supposed to tax a business input. And we have exemptions like the purchase [00:05:00] for resale exemption, which exempts inventory. We have the ingredient and component exemption, which exempts tomatoes, and lettuce, and whatnot, that's part of a salad. And we have the manufacturer's exemption. All of this is to remove the tax on business inputs. Advertising is your quintessential business input. So as a matter of policy, it should not be taxed at all in a sales [00:05:30] tax that is supposed to conform with the underlying rationale of exempting business inputs and taxing the ultimate sale to the consumer. You tax advertising, it will cascade through the production and distribution chain, and it becomes a stealth tax because it'll be buried in the price of the good. And then when you think about it, it's antidemocratic. We should know what we are paying for government [inaudible 0:00:05:57] taxes, we don't know.

So [00:06:00] that we start off, yeah, services should be taxed if they're part of personal consumption and business input should not be taxed. So advertising is uniquely a business input. Now here's the problem. We have a federal statute, the Internet Tax Freedom Act. It says, if you want a tax advertising state, that's fine, but you got to tax all advertising. Washington [00:06:30] taxes digital advertising, and then it has all of these carve outs. And it is discriminating, at least in my opinion, it is discriminating against interstate commerce and electronic commerce, and that's the problem. And we just finished an intense one-week trial in Maryland on exactly this issue.

What does the federal [00:07:00] statute, which preempts state law, it means when it says that a discriminatory tax is when imposed on electronic commerce that's not generally imposed on similar goods or services. And now the issue becomes, what's a similar service? And there's two ways you can approach this. One is in the weeds, very granular, and say, "Oh, well a digital service [00:07:30] of advertising is not the same as a jumbotron that advertises beer. I watch an ad on my laptop for the sale of beer during halftime at a football game, and that's

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not the same as an ad that appears on a jumbotron." Or you can say, "Look, advertising is advertising. It doesn't matter what form it should take. Don't get hung up on the form. Look [00:08:00] at the substance."

It's the communication of a message to an intended and hopefully future consumer. And so you have these two approaches and that's what the Maryland trial is all about. And you're going to confront that same issue in Washington when the argument is made that a Washington's law violates the Internet Tax Freedom Act because it taxes electronic commerce and not offline, [00:08:30] similar advertising.

Representative ...: So Professor Pomp, there's a couple threads that I want to pull on just for a second because you mentioned at the beginning of your statement around services, and doing sales tax on services, and distinguishing business inputs from, let's say, personal services. So I just have to ask the question, part of our taxes we're also on, let's say, IT consulting services and website design. And so let's take website [00:09:00] design as an example, would you see that as something that's the end all or would you see that as a business input?

Professor Richa...: It's a business input. It's a means to an end. It's to have a website that people will access to buy my good or service.

Representative ...: But that's not all websites are for. I guess what I'm getting at is that when ITFA was first passed, and as we see the internet evolve, if you will, so we're in Web 2.0 world and I think we're looking at potentially [00:09:30] a Web 3.0, right? Where more consumers own more of their own data. So as things evolved, would you see an area where conversations could evolve around taxation? Because I think no one could conceive of, let's say, Facebook or maybe even... I don't know exactly that ITFA was passed, but let's say an Amazon. So as we look at the way the internet's involved and the web has evolved, websites aren't just there to sell something. They might be the [00:10:00] end to the means themselves. And without government getting too prescriptive with us saying, "Okay, your website is to do this, your website is to that," is there a way to look at updating our tax codes to actually fit the reality of what the internet has become, not what it was thought to be?

Professor Richa...: When you look at the history of the Internet Tax Freedom Act, Congress knew that we had this [00:10:30] potentially transformative internet on our hands. No one could predict what form it would take. Everyone knew that it was going to make a real difference. It's going to allow transactions to be done in a better, faster, different kind of way. And they intended to have broad protection for what they saw as a fledgling industry at that point in time.

[00:11:00] The first versions of the internet Tax Freedom Act were intended to be temporary because we were feeling our way. We just didn't know what the future was going to bring, but it was quite clear Congress wanted broad protection. Advertising's dynamic, you think about where we've come, no one knows what the future is going to bring in advertising, and technology's the

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same thing. So we have two very dynamic sectors here. And of course everything's [00:11:30] going to be different tomorrow from the way it is today, but one thing is a constant, that there are business inputs and there is personal consumption. And if you go back to fundamentals and ask the right question, well, then answers can be talked about that make sense. Websites, they're not done for personal satisfaction unless you have some kind of vanity website. They are done with a commercial purchase [00:12:00] in mind.

Representative ...: Yeah, there's a lot of vanity websites, Professor Richard Pomp.

Nikki Dobay: Yeah, [inaudible 00:12:04].

Representative ...: And I guess to just to dig in a little bit though, you said, "Dynamic sectors," right? And I understand ITFA was put in place so that we didn't tax something to death, right? So that we didn't take this fledgling technology and literally tax it to death. But if you got a dynamic sector with a stagnant tax policy, and I'm not saying that there's a right or wrong in this, but I just think that if we're looking at, through the lens of the origination of [00:12:30] ITFA, we're looking at the wrong product. The internet is not what it was when ITFA was passed, and so I think there has to be some dynamic conversations, if you will, around tax policy and the internet. It is so much bigger than just for business. And there are so many services and consumption of services, in ways that are new and novel, that it's really hard for policymakers to say our tax system has to stay stagnant to... And correct me if I'm wrong, was this passed in [00:13:00] the early 2000s or late '90s? When was ITFA passed?

Professor Richa...: First version was '98.

Representative ...: So '98. So I'm thinking, my thirty-year-old was born in '95, so it was a little bit after he was born. And I just got to say, the internet has changed. And to your point, they saw something big, and huge, and life-changing, but they had no idea what it was going to be in 2025.

Professor Richa...: Yeah, well, that's true of almost every statute. The world changes, [00:13:30] and that doesn't mean that we have our hands tied. The underlying question, what's a personal service and what's a business input, that remains the same. It may be answered differently, but if you ask the right questions, you're going to get the right answers, and you're not going to be adrift without a rudder. You're not going to say, "Oh, well the internet's different today." Everything's different today. So that doesn't really get [00:14:00] us anywhere, and I'm not saying you shouldn't do anything. I'm just saying you should do the right thing.

You should talk about personal services, not an advertising service. So I'm not saying you sit on your hands, it's just that you should go back to basics and not treat everything as fair game because, hey, these things didn't exist back when they adopted the statute. Well, of course. We're in a different world and we'll be saying the same thing about artificial intelligence. We know it's going to

[00:14:30] change and we know it's going to be transformative, but that doesn't mean because we can't anticipate change we are unable to do the right thing about dealing with the change.

Representative ...: And I think that's our crux of it, right? What is the right thing, and that definition of right and wrong, and especially as it affects the internet, because I think the business input... And I understand that argument and I don't disagree, that business inputs shouldn't be overly taxed. You end up with a pyramiding scheme, if you will, and no [00:15:00] one wants that. But I will say that the conversations around digital taxation and the internet, they're dynamic and they're evolving, and it's not one size fits all. And I feel like, as a policymaker, it's hard to sometimes thread that needle of doing good policy and not being overly paternalistic as we're looking at different, let's say, websites for instance, right? As we're looking at different websites, it's like you get this tax situation and you get that tax situation. So it's going to be some robust conversations, I think in [00:15:30] the next probably five years, around what's the right way to tax on the internet? And digital ad tax is the first in the frontier.

Professor Richa...: Yeah, I wouldn't call it any kind of legitimate frontier. And of course we're always going to have conversations. We should have ongoing conversations, but they should be conversations that are at least discussing what is right. Now you're saying, "Oh, what's right, what's not right?" We're not talking about concepts [00:16:00] like fairness where people can easily disagree, what's fair, what's not fair. We are talking, imagine if it were an income tax and the discussion is, "Oh, wow, there are all sorts of new deductions that businesses have to make a profit today." I go, "Okay, that's not anything that is going to force us into having an odd conversation about it." The question is that a legitimate cost of generating [00:16:30] profit? And yes, no one ever thought that you would make an expenditure in this manner and it would produce a profit, but at least you're asking the right question, is it personal in nature or is it business?

So the same thing when it comes to the sales tax. Ask the right question. Then you have a subset of personal services, you may not want to tax all of them. That's a perfectly legitimate decision to make. That's the decision that was really made back at the beginning [00:17:00] of the depression when sales taxes were being adopted. Services were not a big deal back then. You didn't want to tax the kid that mowed your lawn or shoveled your snow, or the high school teacher that tutored after class. Those were just small potatoes. But you create a subset today of service providers and then ask the question, which of these are business inputs? We don't want to tax them, that will cascade through the system and be basically [00:17:30] an invisible stealth tax. And which ones are legitimate because they are personal services?

So I'm not opposed to conversations, but make them legitimate conversations and give them some form and substance to them, not just throw everything up and say, "Should we tax this? Should we not tax?" We do have a guiding star here. We do have a North Star that can guide us in thinking about what is

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correct. We know what is correct. You may not want to pursue it, but [00:18:00] we know what's correct.

Representative ...: And I love listening to you, Professor Pomp. I think the biggest difference between your job and my job is that as a professor, you can operate with a certain sense of certainty, right? There's a right and there's a legitimate, and I think those are all very true and real. I think as a policymaker, we are just more nuanced in that we have to have more conversations. And even looking at sometimes our stakeholder groups around certain policy positions, there's just, sometimes there isn't the North Star that we want there to be. [00:18:30] But I think that as we have further conversations, we'll have to start establishing that in this new environment.

Professor Richa...: Let me tell you, I've drafted enough statutes in my life to not be accused of being pollyannish, or starry-eyed, or a pointy-headed academic. I understand the practicality of making tough political decisions. I'm not against that. Of course, every statute is going to be a compromise. That is not my position. [00:19:00] And I'm not naive about this whole process, but we aren't so totally different. I don't live in this dream world. I've advised many legislatures over my time and ran the New York Tax Study Commission where we did end up reforming the corporate income tax and the personal income tax. But we started off by establishing a framework. What are we trying to do here? What is the guiding principle? [00:19:30] Oh, if it's income tax, you ought to get a deduction for business deductions. Okay, well that's a good principle, let's see how we're going to implement it.

Sales tax, you shouldn't tax business inputs. You should tax personal services. Let's see how we're going to implement it. And you could sit and choose which ones that you want to tax. That's what you are paid to do is to make those decisions, but it ought to be made in a context. It ought to be made with some rational superstructure [00:20:00] that you are trying to fit these decisions into.

Representative ...: Yeah, and I think when we had our tax structure work group, we did a similar work to that. And so it wasn't probably identical to what you did in New York, but we did do a tax structure work group that was over a year. We had bipartisan, bicameral, a lot of experts, a lot of really good information. It's still online, and a great report that came out of it that really focused on B&O, moving us from a B&O to a [00:20:30] margins tax and lifting our property tax levy lid, which is artificially set at 1%. So between those two things, those were agreed upon from the study and then we were as legislators given a couple of pieces of policy. They didn't pass. We didn't actually take any of the guidance from the tax structure work group, but it was a really good exercise to hear from communities as well as stakeholders, and as well as tax policy experts.

Nikki Dobay: Oh, well, this has probably been the easiest podcast I've done [00:21:00] because you guys have just been driving all by yourself, and I hate to put a pin in this conversation, but I think we have to put a pin in this conversation, because we've got a lot more to talk about, and I know we all have places to be. But I

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think this is really, the three of us have been having this conversation on Washington for a while. And I am so grateful to both of you for coming together and talking through some of these things. But I think we should pause here and come back. There [00:21:30] has been, I'll give a few spoiler alerts. There has been a complaint filed in Washington challenging the digital ads piece of Senate Bill 5814. So we've got things happening there. I know that there are discussions about what could happen during the next legislative session on this issue. But really just thank you both for coming together and hopefully we can keep this conversation going on a future podcast. But any final thoughts [00:22:00] before I close us out? Oh, I've stunned you both. No.

Representative ...: I think [inaudible 00:22:06] I wasn't sure. No, I just wanted say thank you for having us, and I love this conversation. And Professor Pomp, thank you for taking the time. I always learn something new when I listen to you, and it's always, it's a good dialogue. And I think as we move forward with everything from the internet to AI, to all of the new things that haven't even been created yet, we're going to just keep talking about what does tax policy look like in these new spaces?

Professor Richa...: [00:22:30] And you know how we say goodbye in New York? See you in court.

Representative ...: [inaudible 00:22:35].

Nikki Dobay: Oh, dear.

Representative ...: Wow, [inaudible 00:22:39] love that.

Nikki Dobay: Got a little spicy at the end.

Representative ...: Right? It's like, all right.

Professor Richa...: I said it with a smile though. You couldn't see the smile.

Nikki Dobay: That's true. That's true. Well, thank you both for joining me. I really appreciate it and I think we'll be continuing this one. Hopefully we could have a few more conversations on the podcast. And for the listeners, [00:23:00] contact information for Professor Pomp and Representative Berg will be in the show notes. Thank you so much for listening and I will be with you soon on the next GeTtin' SALTy.