

# Special Report

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## Florida Sales Tax Exemptions Overstated

Cass D. Vickers, Vickers Madsen & Goldman, LLP, Tallahassee, FL

The assertion has been made, and much repeated, that Florida's sales tax exempts far more than it taxes. Specifically, it has been said in connection with the debate over SJR 938, a proposed constitutional amendment being considered by the 2002 Florida Legislature, that the tax brings in some \$17 billion, but that it affords exemptions having a value of \$23 billion.

The "exemption" figures derive from the 2001 Florida Tax Handbook prepared under the auspices of the Florida Legislature by the Office of Economic and Demographic Research and the Florida Department of Revenue, Office of Research & Analysis. There is a listing of "exemptions" at pages 109-114 of that Handbook, and on page 114 there is a Grand Total for the so-called "exemptions" for FY 2001-02 of \$22,671,900,000. The truth is that there is nothing like \$23 billion in exemptions. The "exemptions" label is being misused to describe billions upon billions of dollars in transactions that are either not within the purview of Florida's sales tax at all or which the State is barred by the U.S. Constitution or other controlling law from taxing.

An "exemption" is a matter of legislative grace, a favor granted by which, in the case of sales tax, a transaction that would otherwise be subject to tax, is carved out from the tax. Florida's sales tax is imposed pursuant to Chapter 212, Florida Statutes. The tax reaches sales of tangible personal property (with a corresponding use tax on purchases of such property outside the State), the sale of a very few, specifically-enumerated services, the sale of admissions, transient rentals, leases of real property for commercial purposes, the sale of service warranties covering tangible personal property, and certain other listed transactions.

**Avoiding pyramiding and duplicative taxation.** The Florida sales tax is a one-level<sup>1</sup> tax on retail sales to final consumers. In order to assure the character of the tax as a retail sales tax (as opposed to a gross receipts tax, for example), items purchased for resale are not subject to tax. While the Handbook list does not include the value of most purchases for resale in the \$23 billion total as such, it does include variants of such transactions. Thus, materials used for packaging other items being sold are not taxable-their cost is included in the price of the item being packaged and sold and is subject to tax at that time. The Handbook depicts this as a \$27 million "exemption," when in fact, the statutory provision in question simply preserves the tax as one on the final retail transaction.

Another example of over counting "exemptions" is separately billed utility charges to a tenant on which the landlord has already paid sales tax; the Handbook identifies this as a \$13.2 million "exemption." Without that treatment, the tax would be collected twice,

from both the landlord and the tenant even though the electricity is only used once, by the tenant.

The list includes a \$30 million "exemption" for materials and supplies used in fulfillment of a service warranty. The Legislature decided to tax the full amount paid to the issuer of a service warranty, an extended warranty sold in connection with a washing machine, for example, rather than to tax such parts, if any, as might later be used to maintain or repair the washing machine. State revenue collections certainly benefitted from this approach, realizing not only more sales tax but collecting it sooner than under the prior regime. The so-called "exemption" merely guards against the duplicative taxation of both the service warranty premium and the parts and supplies used to meet the issuer's contract obligations.

There are numerous other provisions which effectively assure the character of the tax as a retail-level tax on consumers rather than as a pyramiding tax levied at each stage of production, distribution and sale.<sup>2</sup> A prominent example is the \$150.5 million "exemption" for the purchase of fuel by public and private utilities. Consuming businesses pay tax on the final cost of the electricity, defined by the statute as tangible personal property. To tax the fuels used to generate electric power would be to tax both the component cost and the final sale of that electricity. Again the putative exemption is not really a matter of the Legislature affording some favored treatment, but the structural preservation of the tax as a one-level tax on retail sales.

Guarding against the imposition of tax on tax is also the object of a number of other provisions such as the "exemption" that avoids imposing Florida sales tax on federal taxes on admissions (\$.4 million), on the federal excise tax on retailers (\$.8 million), and on federal, state and local consumer taxes on utilities (\$35.9 million). Yet these and other similar treatments run under the rubric of "exemptions" and are demeaned as if they represent some favor to a special interest group rather than being acknowledged for what they are--accommodations to the Legislature's anti-pyramiding intent.

**Services not exempt.** The Handbook presents a long list of services as "exempt" from Florida sales tax. They are not exempt but are simply beyond the reach of the tax as enacted by the Florida Legislature in 1949 and amended through the years. That fact is acknowledged by the Senate Staff Analysis and Economic Impact Statement for recently-released CS/SJR 938:

Aside from the services mentioned above [detective, burglar protection and other protective services, and nonresidential cleaning and pest control], services are not directly subject to Florida's sales and use tax. This lack of tax on most services is not due solely to exemptions from the tax, but from the fact that the services are not specified as taxable.

Despite the couched language, the point is clear: the Legislature has not exempted medical, dental, engineering, legal, banking, insurance, securities, construction and other services from tax. They are simply beyond the pale of a tax which has historically been a

tax on the retail sale of tangible personal property (along with admissions, transient rentals and other non-service transactions).

Only during Florida's brief experiment with the taxation of services in 1987 were services generally subjected to Florida sales and use tax and that was accomplished not by the mere repeal of some "exemption" from tax, but by the affirmative imposition of tax on specified service transactions. The new "implementing bill" offered in support of SJR 938, namely CS/SB 1106 also effectively concedes this point, taking the 1987 tack and affirmatively listing those services to be taxed. While there is nothing which in principle forbids the Legislature from adding services to Florida's sales tax base, the statement that they are currently "exempt" from tax is not an accurate statement of the law. Yet the value of the services "exemptions" in the Handbook amounts to more than \$13 billion of the so-called \$23 billion in "exemptions." Taking that correction alone, the claim that Florida exempts more than it taxes fails since the tax collects over \$16 billion and could then be said to exempt no more than \$10 billion at the outside.<sup>3</sup>

**Limiting the tax to those engaged in business.** The Florida sales tax, although collected from consumers by the selling dealer, is an excise or privilege tax imposed upon the privilege of engaging in the "business" of making taxable sales. Accordingly, occasional and isolated sales (garage and yard sales and transfers of title occurring in connection with business reorganizations, by way of illustration) are not subject to tax. The statutory treatment of occasional and isolated sales is not fairly denominated "exemptions" but is designed to limit the reach of the tax to those engaged in making sales as a business. Yet the Handbook includes a \$25.5 "exemption" for occasional and isolated sales by businesses.

**Taxation prohibited by federal or other controlling law.** The Handbook identifies \$97 million worth of "exemptions" on Internet access fees. The fact is that taxation of such fees is prohibited by federal legislation, the Internet Tax Freedom Act and Florida could not at present tax such fees even if there were no "exemption" in former Florida Statutes § 212.05(1)(e)1.a. (now in Florida Statutes § 212.11(3)(h) of the Communications Services Tax).

The Handbook reflects a supposed "exemption" of \$23.1 million for the credit allowed against Florida use tax for sales tax paid in other states. The fact is that such a credit is required by the Commerce Clause of the United States Constitution. Without the credit, both the sale of an item in, for example, North Carolina and its use in Florida would be subject to tax whereas the same purchase in Florida would yield only one tax, a scheme which burdens transactions in interstate commerce and so runs afoul of the Commerce Clause. Florida cannot lawfully fail to extend the credit in question, yet the number is lumped with exemptions which could be lawfully repealed for the purpose of raising additional revenue.

A similarly misleading line item is the Handbook "exemption" for sales directly to the federal government. The United States Government is immune from taxation by the states under the Supremacy Clause of the United States Constitution, Art. VI, cl. 2. The

State (including political subdivisions of the State such as counties) is immune from its own taxes and could not, in any event, raise any revenue by taxing itself. Municipalities could be subjected to State sales tax but are exempted by statute law. While the number in the Handbook is an aggregate figure, it is fair to say that some very substantial portion of the state \$269.6 million "exemption" is no exemption at all, but a number that merely represents the multiplication of the 6% State sales tax rate by a dollar value for sales to the United States Government and its agencies, the State of Florida and its agencies and political subdivisions, transactions which are constitutionally immune from tax.

**Conclusion.** There are other "exemptions" in the Handbook list which cannot fairly be called "exemptions" from Florida's sales and use tax. A complete analysis is beyond the scope of this short paper. The tax scheme embodied in Chapter 212, Florida Statutes is a very complicated one, and it is not made complicated by exemptions alone. A more complete review of the transactions identified as "exempt" from Florida tax is, nonetheless, patently in order if the Legislature and the public are to have an informed discussion of tax reform. In the meantime, neither the assertion that Florida's sales tax exempts more than it reaches or that there is anything approaching \$23 billion in "exemptions" withstands scrutiny and the repetition of those myths does no service to those who would make decisions on this important front.

## ENDNOTES

1. The Legislature has expressly declared its intention that the tax be one on the final consumer and so no pyramid, i.e., that it not operate to impose tax on tax or duplicatively on successive transactions. Fla. Stat. § 212.12(12).
2. The latter is the kind of tax imposed under gross receipts and value-added tax schemes.
3. It should be said that even the characterization of the listed transactions as "services" is, in many instances, arguable. Franchise fees, patent and royalty payments (described as a \$711.6 million "exemption") and insurance carrier payments (shown as an "exemption" valued at over \$1.8 billion), for example, may be regarded as payments for intangible contractual rights and most would regard the charges for "money lending" (a supposed \$689 million "exemption") as interest rather than as a purchase of banking services. The author is not aware of any state sales tax codes which tax interest, insurance premiums, franchise fees and the like. Such sums may be subject to tax in jurisdictions imposing a gross receipts tax and, in the case of insurance may, as in Florida, be subject to premiums taxation, but those are fundamentally different levies from the sales tax on consumers imposed under Florida law.

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## ABOUT THE AUTHOR

Cass Vickers was admitted to the practice of law in Florida in 1973. He has concentrated his practice in state and local tax matters since receiving an LL.M. in Taxation from Georgetown University in 1982. Mr. Vickers is the current chair of the Florida Chamber of Commerce Taxation Committee, a member of the Florida TaxWatch Board of Trustees, was appointed by the House Speaker to the Sales Tax Study Commission in 1986, and was Director of Tax Policy and Dispute Resolution at the Florida Department of Revenue (1995-1996).

Mr. Vickers has taught at the Florida State University College of Law, the Georgetown University State and Local Tax Institute, the Institute for Professionals in Taxation (IPT)

Advanced Sales and Use Tax School, COST Sales and Use Tax and Income Tax Conferences, and regularly speaks at tax seminars and conferences for such groups, as IPT, the Tax Executives Institute, and the Florida Bar.

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Keith G. Baker, Ph.D., Senior Vice President  
and Chief Operating Officer.

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