



STATE OF IDAHO  
OFFICE OF THE ATTORNEY GENERAL  
LAWRENCE G. WASDEN

December 12, 2011

The Honorable Ben Ysursa  
Secretary of State  
**HAND DELIVERED**

RE: Certificate of Review  
Proposed Initiative to Broaden the Sales Tax Base and Lower the Sales Tax Rate

Dear Secretary of State Ysursa:

An initiative petition was filed with your office on December 6, 2011. Pursuant to Idaho Code § 34-1809, this office has reviewed the petition and prepared the following advisory comments. Given the strict statutory timeframe in which this office must review the petition, our review can only isolate areas of concern and cannot provide in-depth analysis of each issue that may present problems. Further, under the review statute, the Attorney General's recommendations are "advisory only." The petitioners are free to "accept or reject them in whole or in part." The opinions expressed in this review are only those which may affect the legality of the initiative. This office offers no opinion with regard to the policy issues raised by the proposed initiative, nor the potential revenue impact to the state budget.

**BALLOT TITLE**

Following the filing of the proposed initiative, our office will prepare short and long ballot titles. The ballot titles must impartially and succinctly state the purpose of the measure without being argumentative and without creating prejudice for or against the measure. While our office prepares titles for the initiative, petitioners may submit proposed titles for consideration. Any proposed titles should be consistent with the standard set forth above.

**MATTERS OF SUBSTANTIVE IMPORT**

The purpose of the proposed initiative is to broaden the sales tax base to include services and lower the rate from six percent (6%) to five percent (5%). Included within the definition of sales are contracts for applying, installing, cleaning, altering, improving, decorating, treating, storing, or repairing real property. See proposed Idaho Code § 63-3612(k). This provision has the effect of making many contracts for the improvement of real property retail sales subject to

sales tax. Idaho Code §§ 63-3622A and 63-3622O prohibit or exempt the imposition of taxes on sales to governmental entities, which means the proposed initiative will completely exempt materials and labor used on government contracts. Under present law, materials used on government contracts by contractors are taxed. Contractors working at the Idaho National Laboratory (INL), Mountain Home Air Force Base, and contractors building or repairing highways and other roads are just examples of contracts that would completely escape taxation under the petitioners' proposal.

Alternatively, the petitioners could consider amendments similar to states like Washington, which treat most contracts as retail sales, but for government contracts, the contractor is taxed on the materials used or consumed.

The proposed initiative may, in certain instances, tax the sale of new homes. If a builder builds a home that he intends to sell upon completion, he may be able to purchase the materials and the subcontract services for resale. Once the house is complete and he sells it, this may be a retail sale. Sales of existing homes are not considered to be retail sales pursuant to the initiative.

The proposed statute does not exempt any services except for those services consumed in a production process. Idaho Code § 63-3622D. There are many other statutes that provide exemptions of tangible personal property but would not exempt related services. For example, the occasional sale exemption exempts the transfer of tangible personal property between related entities. The proposed initiative would impose tax on service transactions between related entities. There are other exemptions that similarly exempt transactions involving tangible personal property, but related-service transactions would be taxed under the initiative. Some obvious examples include the pollution control exemption, the research and development exemption, and the logging exemption. The drafters of the initiative have the prerogative to either provide for or not provide for exemptions. However, since the proposed initiative does not remove any of the exemptions for sales of tangible personal property, the petitioners may wish to consider some consistency for service-related transactions.

Though not classified as an exemption, the initiative does not impose tax on services provided by “. . . licensed medical doctors, dentists, osteopaths, physical therapists, optometrists, physician assistants, midwives, podiatrists, hospitals, nursing homes, chiropractors, nurse practitioners, naturopaths, or psychologists.” See proposed Idaho Code § 63-3614A.<sup>1</sup> In a broad sense, the drafters are not taxing medically-related services. The method they have chosen to reach that result is to exclude services provided by certain medically-related professionals. The services provided by these professionals are not subject to sales tax regardless of whether the services are medically related. For example, if a physical therapist opened a day care at her business location that she operated in conjunction with her physical therapy business, the child care may be exempt from sales tax even though child care provided by a licensed day care would be taxable under the proposed statute.

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<sup>1</sup> The drafters inserted “midwives” twice in the sentence identifying the professionals who are providing services for purposes of the tax on services.

The drafters of the initiative have included several sections to source the sale of tangible personal property and services to certain locations.<sup>2</sup> These sourcing rules seem unduly complex for the state sales tax and may or may not be consistent with other provisions of the Idaho sales tax law. Sourcing is defined as the point at which a retail sale occurs. The statute then provides a series of rules to determine the location of the sale. However, if the sale occurs in Idaho, then the transaction is subject to sales tax. Under present law, if delivery of tangible personal property occurs in Idaho, then the sale takes place in Idaho. If the sale takes place in another state, and if no sales tax is charged, then use tax is due if the property is used in Idaho.

The sourcing rules for services are inconsistent. For example, proposed Idaho Code § 63-3642(1)(a) provides that if the service is received by the purchaser at a business location of the seller, the sale is sourced to that location. Paragraph (1)(b) provides that if the service is not received at the business location of the seller, it is sourced to the location where received. In short, pursuant to subsection (1), the sale is sourced to the location where the service is received.

Subsection (5) of proposed Idaho Code § 63-3642 introduces some new terms for sourcing of services. Pursuant to this provision, the sale is sourced to Idaho if the consumption of the service occurs in Idaho, even if the service is performed outside Idaho. These provisions are confusing. Under one provision, the service is sourced to Idaho if the service is received in Idaho, whereas under a second provision, the service is sourced to Idaho if it is consumed in Idaho. The provision creates a conflict between the terms “receipt” and “consume.” If an Idaho mechanic repairs a car belonging to an Oregon resident at the mechanic’s business location in Idaho, the service is performed in Idaho and, presumably, the receipt of the service occurs in Idaho. However, if the Oregon resident drives his car back to Oregon where he keeps it and uses it, the services may be said to be consumed in Oregon. The petitioners may want to clarify the sourcing rules for services.

The proposed statutes appear to raise revenue for the State of Idaho. The initiative does not address revenue impact, but since it only lowers the rate to five percent (5%) and substantially broadens the tax base, there is a likelihood that the initiative will raise revenue. This raises the question of whether an initiative that raises revenue may not be allowed because it is contrary to art. III, sec. 14 of the Idaho Constitution, which provides that all revenue-raising bills originate in the House. At a minimum, there is an argument that an initiative to raise revenue is prohibited by art. III, sec. 14, which provides that “[b]ills may originate in either house, but may be amended or rejected in the other, except that bills for raising revenue shall originate in the house of representatives.”<sup>3</sup>

By using the term “bill,” the drafters of the Constitution implied that the provision only applies to legislative enactments. An initiative, as allowed for in art. III, sec. 1, is a process for the people through signatures and voting to enact legislation. The history of the federal Origination Clause is all about balance between the two legislative houses. Idaho seems to have

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<sup>2</sup> See proposed Idaho Code §§ 63-3642 and 63-3643.

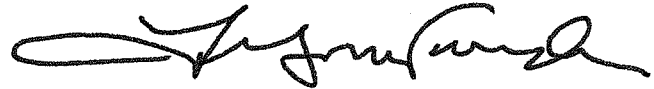
<sup>3</sup> We are unaware of any case authority, and we are unsure whether a court has ever addressed the issue, but we believe we are compelled to raise the issue for the petitioners to consider.

just copied the federal practice. The Idaho Constitutional Convention in 1889 adopted this section without debate or amendment. At the federal level, the clause had two motives. First, it put the fiscal authority in the House of Representatives, which was seen as being the house closest to the people. Second, it acted as a counterbalance to the special powers granted only the Senate – the power to advise and consent to Presidential appointments and to ratify treaties.<sup>4</sup> Thus, the rationale for requiring revenue-raising measures in the House seems inapplicable to initiatives. If in fact one of the motives is to give the power to the body closest to the people, then it seems logical that the initiative process could be used to raise revenue.

### **CERTIFICATION**

I HEREBY CERTIFY that the enclosed measure has been reviewed for form, style, and matters of substantive import. The recommendations set forth above have been communicated to the Petitioner via a copy of this Certificate of Review, deposited in the U.S. Mail to Robert C. Huntley, The Huntley Law Firm, PLLC, P. O. Box 2188, Boise, Idaho 83701.

Sincerely,

A handwritten signature in black ink, appearing to read 'L. Wasden', with a stylized flourish at the end.

LAWRENCE G. WASDEN  
Attorney General

**Analysis by:**

WILLIAM A. VON TAGEN  
Deputy Attorney General

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<sup>4</sup> The Federalist No. 66 (Alexander Hamilton).