



TESTIMONY AGAINST EXPANDING THE SALES TAX TO COVER LEGAL AND OTHER PROFESSIONAL SERVICES

Good morning, Chairman Brubaker, Minority Chairman Wozniak, members of the Committee, and staff. I am Thomas G. Wilkinson, President of the Pennsylvania Bar Association, representing the 28,000 lawyers of the Association. Thank you for inviting us to testify today. The PBA opposes expanding the imposition of the sales and use tax to professional services, specifically to legal services.

The PBA is well aware of the fiscal issues facing some homeowners in Pennsylvania. We are sympathetic to those homeowners that have difficulty paying their real property taxes, and those taxes seem to increase even when property values are stagnant. Pennsylvania lawyers are on the front lines every day helping financially stressed homeowners maintain their residences and in providing pro bono legal services through mortgage foreclosure diversion programs. That being said, the Commonwealth must not solve this issue by expanding the imposition of the sales tax to professional, including legal, services. Such an expansion policy would counter longstanding Commonwealth tax policy, exacerbate inequality, create legal fairness issues, and also hurt small businesses.

Professional services, including legal services, are necessities. People hire an attorney because they have to, not because it is an optional luxury service. When people need an attorney, they *really need* an attorney. Individuals hire an attorney, for example, to probate a will, to defend against a tort action, to fight an assessment made by their township, to deal with a hostile

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landlord or tenant, to avoid foreclosure, or to deal with a civil rights issue. Stated plainly, the very nature of the justice system is unique and should be treated as such. Access to justice is a basic constitutional right, and justice is not a commodity for sale like an automobile or furniture, but rather a key basis for a functioning civil society. Effective legal representation routinely requires legal counsel. A sales tax on legal services places an undue and unjust burden on the legal system, a burden particularly felt by those of lesser means, and therefore on the equal access to justice.

The need for legal services is not dependent upon income, as lower-income people need legal services every bit as much as do higher-income people, often even more so. The Commonwealth recognizes this very need by allocating funding in the state budget for civil legal services to the indigent. Imposing an additional sales tax on legal services would make it that much more difficult for lower-income people to hire an attorney when they really need to do so. The inability to hire an attorney, or to hire an attorney for sufficient amount of time, in turn, hurts law firms, which are valuable small businesses and job providers across Pennsylvania.

For example, suppose a family suffers a job loss and is unable to pay its mortgage. Taxing legal services would mean that the family would have to pay an additional seven percent under Senate Bill 1400 to retain an attorney to negotiate a fair resolution with the mortgage bank, while the bank would not have to pay the seven percent tax because it is a business.

Precisely because the sales tax is regressive, it has not been imposed on necessities such as legal services. Therefore, replacing real property taxes with regressive sales taxes turns Pennsylvania tax policy on its head. Were Senate Bill 1400 to become law, every family living in a \$400,000 home would benefit, as would every family living in a \$1,000,000 home, while

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lower-income people in need of legal services would effectively pay more in sales taxes. Such a situation can hardly be viewed as fair or just.

Moreover, charging a sales tax on professional services would burden not just the redress of fundamental rights in the courts, but also the redress of rights in front of almost every government body. Virtually *any time* a professional is needed to address *any* issue—tax, legal, engineering, etc.—with local or state government, individual Pennsylvanians would have to pay an additional sales tax to the Commonwealth to use that professional. However, the government in question can obtain the same services without paying that tax. In other words, one would have to pay the government to challenge the government.

By taxing some legal services and not others, Senate Bill 1400 presents serious questions under the Pennsylvania Constitution's uniformity of taxation provision. One plaintiff would pay counsel on an hourly basis and have to pay sales tax, while another plaintiff in the exact same legal situation would pay counsel on a contingency fee basis and pay no sales tax. As there is no rational basis here for separating the two plaintiffs into different classes for imposition of the sales tax, this tax dichotomy is likely unconstitutional. We are frankly skeptical of any argument that the General Assembly is expressing a public policy encouraging payment of legal fees on a contingency fee basis, as any such policy is within the purview of the Pennsylvania Supreme Court. We also question the constitutionality of taxing individuals for legal services but not businesses that frequently fund legal services for individual officers or employees.

Nor should these infirmities in the bill be addressed by further expanding the scope of the proposed sales tax to legal services regardless of method of payment. When a judge or jury renders a verdict in the form of a money judgment representing recoverable damages, that judgment should not be diminished by imposing a sales tax on the component representing legal

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fees, nor should it be increased to cover the sales tax. Worse yet, this tax expansion would upset the carefully crafted and politically delicate workers' compensation system. It would force injured employees to pay from their benefits an additional seven percent tax on the services rendered by their workers' compensation attorney. This additional tax could add up to hundreds of dollars every year for an injured worker.

Finally, Senate Bill 1400 leaves numerous significant questions unanswered about whether a legal service is taxable, some revolving around exemption (83) which provides that "The sale at retail or use of services performed by any person to the extent that the recipient or user of such services receives those services free of charge." For example:

- What if a business paid for the personal legal services of an officer, say for estate planning, and simply had the bills delivered to its treasurer?
- What if a tenant sues a landlord individually and the landlord has the LLC or other business entity that owns the building pay for the legal services?
- What if a lawyer provides in the fee agreement that the fee will be contingent on a recovery but that fee will be determined based on the lawyer's usual hourly rate?
- What are "domestic relations" matters? Is a collection case to pursue unpaid child support included? How about a protection from spousal abuse action?
- What if parents pay for their child's attorney for his or her delinquency proceedings? If this legal service is taxable, how do we justify exempting criminal defendants from sales tax, but not juveniles facing delinquency proceedings?
- What if a daughter pays the legal fees for her father to deal with abuse in his nursing home?

The Pennsylvania Bar Association understands that there are serious property tax issues facing some homeowners in the Commonwealth, but the proper "fix" or reform should not be to impose an unfair and likely unconstitutional tax on our citizens' access to justice.

Thank you.