# Rhode Island Department of Revenue
# Division of Taxation

September 21, 2020

The Honorable Representative Marvin L. Abney
Chair, House Committee on Finance
State House
82 Smith Street
Providence, Rhode Island 02903

RE: Concerns Regarding House Bill 8129 – An Act Relating to Taxation – Sales and Use Taxes

Dear Chairman Abney,

I am writing on behalf of the Department of Revenue, Division of Taxation, to express concerns regarding House Bill 8129 as currently drafted, to explain the current statutory context in order to clarify the intended and unintended consequences of this bill, and to request your consideration of these issues.

The proposed bill adds language to R.I. Gen. Laws § 44-18-30(22), which exempts from sales and use taxes, manufacturing machinery and equipment used to manufacture, convert, or process tangible personal property to be sold. The bill adds two subsections, in (v) and (vi), that, as an initial matter, include vague language that is overly broad, internally inconsistent, and susceptible to abuse. Furthermore, as written, its broad impact would have unintended consequences and the exemption would be difficult to administer. Finally, as a general matter, it is unclear what the exemption is intended to include, whether it is sales or all purchases made by the manufacturer, or any taxpayer "treated as a manufacturer[.]"

Specific concerns include, but are not limited to:

The language "[w]here a taxpayer is treated as a manufacturer" is ambiguous as it is unclear what "treated as" means. This will lead to the potential for taxpayers who do not meet the requirements for the manufacturing exemption to claim that they are "treated as" a manufacturer such that they can claim an exemption pursuant to the new language.

The proposed language imitates the language in R.I. Gen. Laws § 44-18-30(7) (purchase for manufacturing purposes) to a certain extent and it is unclear what the proposed language in R.I. Gen. Laws § 44-18-30(22) is intended to achieve. The addition appears to be for the purpose of allowing businesses to "duplicate operations" in other locations and thus automatically be entitled to exemptions from the sales and use taxes. As "operations" is not defined or limited, this could lead to potential abuse where a taxpayer may assume starting a new location or different business operation automatically allows it to claim the exemption.

The conflict between the requirement that a "factory" have a "fixed location" in R.I. Gen. Laws § 44-18-30(22)(i) and the allowance for bringing raw materials to a non-fixed location in the new section 22(v)(A) creates an internal inconsistency that essentially nullifies the earlier language.

Also in new section 22(v)(A), there is no threshold for a determination "if it would be more cost effective to bring the processing equipment to the location of the raw materials." This is ambiguous and would be impossible to administer and enforce as an exemption.

In addition to the previously mentioned undefined terms, there are no definitions or limitations on: "raw materials" or "processing operation" in new section 22(v)(B). Further, in that section, there is ambiguity as to the scope of a "contract" and what "another taxpayer" is the "title holder" of or what that term encompasses.

Section 22(v)(B)(I) is ambiguous and it is unclear what is meant by "finished goods converted under the contract." There is no manner to know what "converted" means in this context.

Section 22(v)(B)(II) essentially allows all customers to "also be considered the manufacturer/user/seller of the finished product[,]" which is all-encompassing and would have a broad impact because purportedly all such customers can claim the exemption. Further, it is unclear what the "manufacturer/user/seller" of the product would be and whether the slashes are intended to be construed as an "and" or an "or."

Section 22(vi) is ambiguous and it is not clear what is meant by a "related" company; there is no citation to the "common employer rules determined by the Internal Revenue Code" and no determination as to what these rules are can be made. Allowing "lease arrangements" to be undefined, vague, and not in writing will lead to the potential for abuse as taxpayers may claim an oral lease arrangement, or "cost sharing/reimbursement arrangement," in order to claim the exemption. Further, all businesses are statutorily required to maintain records for audit and allowing a certain class of businesses to meet this obligation with an oral informal profit-sharing arrangement totally undermines the sales and use tax and invites a potential challenge from other taxpayers.

In summary, the exemption proposed in H8129 is extraordinarily expansive and prone to abuse. The company providing the equipment need not own the raw material being processed nor need to sell the finished goods directly in order to claim the tax exemption. The customer who hired the equipment is deemed to be the tax-exempt manufacturer and seller also, and lease arrangements can be unwritten and informal. As a practical matter, a traditional manufacturer operating at a fixed location has more hurdles to meet to qualify for the manufacturing equipment exemption than a mobile equipment lessor/operator pursuant to the proposed bill. Again, the bill as drafted is impossible to administer, will cause an unintended revenue impact as it is so broad that it will encompass taxpayers clearly not meant to be included, and allow for abuse due to its vague language and lack of clear requirements.

I look forward to working with you to address any issues raised in this letter and appreciate your consideration.

Very truly yours,

Neena S. Savage,
Tax Administrator

cc: Members of the House Finance Committee
The Honorable Representative Gregg Amore
Sharon Reynolds Ferland, House Fiscal Advisor
Mark Furcolo, Director, Department of Revenue