Governor’s FY 2018 Budget: Articles

Staff Presentation to the House Finance Committee
March 22, 2017
Introduction

- Article 8 – Taxes and Revenues
  - Section 1 Gas Tax
  - Section 2 & 3 Cigarette Tax
  - Section 8 Other Tobacco Products
  - Sections 4 & 7 Taxation Enforcement
  - Section 5 Corporate Tax Withholding
  - Section 6 Sales Tax Exemption
- Article 9 – Remote Sellers
Current law – DHS receives 1 cent of the gas tax for paratransit services - $4.4 million
- Elderly/disabled transportation
- Contracts with RIPTA for some services

Current contract:
- DHS keeps 21% - $0.9 million
  - Non Medicaid paratransit services
- RIPTA receives 79% - $3.5 million
RIPTA $3.5 million:
- $2.5 million to subsidize elderly/disabled bus services
- $1.0 million for match on paratransit vehicles purchases plus, maintenance, inspection, wheelchair lifts
  - Billed monthly
    - May not get first payment until January
  - EOHHS has administrative oversight
    - Legislative solution for administrative problem?
Article 8, Sections 2-3 - Cigarette Tax

- Current law – Tax on all cigarettes sold or held for sale in the state
  - Tax evidenced by stamps
  - Current state tax is $3.75 per pack of 20 (effective August 1, 2015)

- FY 2018 Proposal - Increase cigarette tax by $0.50 to $4.25 per pack of 20
  - Effective 12:01am, August 1, 2017
FY 2018 Budget includes $8.7 million
- Cigarette tax - $6.5 million
- Sales tax - $1.1 million
- Floor Tax - $1.0 million
  - Tax on existing inventory – difference between the two tax rate
Estimate includes 5.3% demand drop
- FY 2017 estimate for $0.25 increase included 0.7% demand drop
### Article 8, Sections 2-3 - Cigarette Tax

- **2015 Assembly increased tax from $3.50 to $3.75**

<table>
<thead>
<tr>
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</tr>
</thead>
<tbody>
<tr>
<td>Per pack Tax</td>
<td>$3.50</td>
<td>$3.50</td>
<td>$3.75</td>
<td>$3.75</td>
<td>$3.75</td>
<td>$4.25</td>
</tr>
<tr>
<td>Total (millions)</td>
<td>$134.6</td>
<td>$132.7</td>
<td>$136.6</td>
<td>$130.4</td>
<td>$126.1</td>
<td>$133.7</td>
</tr>
</tbody>
</table>
Article 8, Sections 2-3 - Cigarette Tax

- Each state/territory has own tax
  - Highest – New York, $4.35/pack
  - CT is 2nd highest at $3.90/pack
  - RI is 3rd highest at $3.75/pack
  - Lowest – Missouri, $0.17/pack
- 36 states & DC have tax of >$1.00
- 18 states & DC have tax of ≥ $2.00
- 8 states have tax of $3.00 or more
## Article 8, Sections 2-3 - Cigarette Tax

<table>
<thead>
<tr>
<th>New England States</th>
<th>Tax</th>
<th>U.S. Rank</th>
</tr>
</thead>
<tbody>
<tr>
<td>Connecticut</td>
<td>$ 3.90</td>
<td>2</td>
</tr>
<tr>
<td>Maine</td>
<td>$ 2.00</td>
<td>14</td>
</tr>
<tr>
<td>Massachusetts</td>
<td>$ 3.51</td>
<td>4</td>
</tr>
<tr>
<td>New Hampshire</td>
<td>$ 1.78</td>
<td>21</td>
</tr>
<tr>
<td><strong>Rhode Island</strong></td>
<td>$ 3.75</td>
<td>3</td>
</tr>
<tr>
<td>Vermont</td>
<td>$ 3.08</td>
<td>6</td>
</tr>
</tbody>
</table>

*Source: Campaign for Tobacco-Free Kids, Jan. 3, 2017*
State cigarette tax not only factor in final price

Federal tax - $1.01 since 2009

State sales tax

Some states allow local cigarette tax options in addition to state tax

- New York City - $1.50 local tax
- Chicago - $1.18 local tax, $3.00 county tax
Article 8, Sections 2-3 - Cigarette Tax

- Base price of product
  - Product use/popularity
- Minimum markup – Retail and Wholesale
  - Lowest price at which product can be sold
  - To prevent sales below cost or unfair pricing
  - 1939 Assembly enacted initial minimum markup laws
Cigarette Tax

**Article 8, Sections 2-3**

**Consumer** - Pays retail price plus sales tax

**Dealers (Retailers)**
- Must include retail minimum markup in price to consumers

**Distributors (Wholesalers)**
- Must include wholesale minimum markup in price to dealers
- Pay cigarette tax

**Manufacturer**
- Sets the product base price
# Article 8, Sections 2-3 - Cigarette Tax

<table>
<thead>
<tr>
<th>Current Prices</th>
<th>RI</th>
<th>CT</th>
<th>MA</th>
</tr>
</thead>
<tbody>
<tr>
<td>Base price/pack of 20 (incl. fed. excise tax)</td>
<td>$4.39</td>
<td>$4.39</td>
<td>$4.03</td>
</tr>
<tr>
<td>State Cigarette Tax</td>
<td>3.75</td>
<td>3.90</td>
<td>3.51</td>
</tr>
<tr>
<td><strong>Total Base Price/pack of 20</strong></td>
<td>$8.14</td>
<td>$8.29</td>
<td>$7.54</td>
</tr>
<tr>
<td>Minimum Markup – Wholesaler</td>
<td>2.75%</td>
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<td>6.00%</td>
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<td><strong>Total Markup/pack of 20</strong></td>
<td>8.93%</td>
<td>15.02%</td>
<td>28.44%</td>
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<td>Post Markup Price/pack of 20</td>
<td>$8.87</td>
<td>$9.54</td>
<td>$9.69</td>
</tr>
<tr>
<td>Sales Tax Rate</td>
<td>7.0%</td>
<td>6.35%</td>
<td>6.25%</td>
</tr>
<tr>
<td><strong>Final Retail Price</strong></td>
<td>$9.49</td>
<td>$10.14</td>
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Article 8, Sections 2-3 - Cigarette Tax
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Article 8, Section 8 – Other Tobacco Products

- Other Tobacco Products – Tax on products sold or held for sale, except cigarettes
  - Tax evidenced by stamps
  - Current tax is 80% of wholesale
- Technical changes to be consistent with enacted law
- No revenue assumed from changes
Article 8, Sections 4 & 7 – Tax Enforcement

- Authorizes Tax Administrator
  - Certain punitive powers
  - Designed to improve collections
    - Jeopardy determination
    - Letter of good standing request prior to transfer or sale of a business
  - Recovery of legal fees
- Increased penalties for failure to remit taxes collected
2013 Assembly criminalized use of software or other technology that allows the modification of point-of-sale records or transaction data.

Article 8 adds remote manipulation to prohibition:
- Persons may not knowingly send or receive data for purposes of manipulation.
2016 Assembly lowered minimum C corporation withholding from 9.0% to 7.0%

Established a $400 Minimum withholding

Corrects withholding rate for pass-through entities to 7.0 percent
- Includes S corporations, Partnerships, LLCs, LLPs, Trusts
Article 8, Section 6 – Sales Tax Exemption

- Limits tax exemption certificates for charitable organizations to be valid for 4 years
  - Retroactive for all certificates effective July 1, 2017

- Maintains current fee of $25
Purchases made out of state or from remote sellers who do not collect RI sales tax are subject to use tax

- If no sales tax was charged, 7% is owed
- If sales tax less than 7% is charged, difference is owed
  - Auto purchased in Massachusetts
Article 9, Remote Sellers Tax Collection

- Compelling collection from out of state sellers has been seen as an impediment to interstate commerce
- Two Supreme Court rulings set standard for nexus as “physical presence”
  - National Bella v. Hess (1967)
Rhode Island has taken several measures over the years to facilitate collection of use taxes owed on remote transactions:

- Streamlined Sales and Use Tax Agreement and Membership - 2007
- “Amazon” Law - 2009
- Use Tax Look-Up Table - 2014
Streamlined Sales and Use Agreement

- Collective effort by states to simplify and modernize sales and use tax administration
  - Substantially reduce burden of tax compliance
- Participating retailers volunteer to collect taxes for member states
  - Rhode Island became a full member in 2007
  - Recent annual collections $2.7 million
“Amazon Law” – 2009

- Added companies that contract with RI companies and sell over the internet to the definition “retailer”
  - Certain sites dropped RI affiliates rather than comply/challenge
- In January 2017, Amazon announced it had agreed to begin collecting sales tax from its RI customers
  - Doing so for 41 states and DC now
Use Tax Tool - 2014

- Assembly authorized Tax Administrator to develop tool for personal income tax forms to simplify use tax collection
  - 0.08% of federal adjusted gross income
  - Additional itemized tax owed on purchases of $1,000 or more

- Proper use of tool is “safe harbor” for all use tax owed
  - Budget assumed $2.2 million in additional revenues, about half has been realized
Recent Colorado case ruling opened door to additional option

  - Physical presence still standard for collection but notification & reporting acceptable

Remote Sellers likely opt for collection rather than reporting requirements
Article 9, Remote Sellers Tax Collection

- Article 9 establishes requirements for certain entities engaged in transaction activities within RI
  - Collect and remit taxes, or
  - Provide notice to buyers of their tax liability
- Applies to those with revenues of $100,000 or 200 transactions
  - Marketplace providers, remote sellers or referrers
Article 9, Remote Sellers Tax Collection

- Notices
  - To buyers: tax liability notice on website, at purchase, and via email within 48 hours of purchase
    - Annual tax document mailing by Jan. 31
  - To retailers from referrers with $10,000 in referral fees that transaction may be subject to tax
- Penalties
  - $5 per notice not sent; minimum $20,000
Article 9, Remote Sellers Tax Collection

- Budget assumes $34.7 million in revenues
  - Uses national sales data scaled to RI
  - Assumes a full year of collections and full compliance
    - Out of sync with drafting on compliance date
      - Amendment submitted to change dates
    - Does not account for current use tax collections
      - SSUTA voluntary collections - $2.7 million
      - Lookup table - possible revision needed?
### Revenue Estimation Methodology

<table>
<thead>
<tr>
<th>Description</th>
<th>Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>U.S. E-Commerce Sales 2010</td>
<td>$1,790.0</td>
</tr>
<tr>
<td>Avg. Annual Growth 2010-2014</td>
<td>15.0%</td>
</tr>
<tr>
<td><strong>Total Est. Sales 2018</strong></td>
<td>$3,122.0</td>
</tr>
<tr>
<td>Est. Rhode Island Share</td>
<td>0.27%</td>
</tr>
<tr>
<td><strong>Est. RI E-Commerce Sales</strong></td>
<td>$835.0</td>
</tr>
<tr>
<td>Est. Non-Nexus Sales</td>
<td>59.4%</td>
</tr>
<tr>
<td><strong>Est. Sales Subject to Collection</strong></td>
<td>$495.9</td>
</tr>
<tr>
<td>RI State Sales Tax</td>
<td>7.0%</td>
</tr>
<tr>
<td><strong>Est. FY 2018 Revenue</strong></td>
<td>$34.7</td>
</tr>
</tbody>
</table>

*$ in millions*
Article 9, Remote Sellers Tax Collection

- Requested amendments on compliance
  - Directs compliance w/in 2 weeks of passage
    - Consistent with revenue estimate
  - Non-collectors must file reporting compliance notification by Feb. 15 annually
  - Alters language on referrers’ notice to 90 days consistent with streamlined tax agreement
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