# Rhode Island State Tax – 2018 Budget Highlights

## Description

### Current Status

**After being delayed for approximately a month, Rhode Island's budget through June 30, 2018 was finally signed into law by the governor on August 3, 2017. An analysis of the relevant tax sections in the budget is provided below. For reference, the enacted Public Laws version of House Bill 5175 Substitute A As Amended is available here (ch. 302, Articles 8 & 11).**

Sales and Use Tax

*Taxation of online retailers*

Joining a large number of other states in recent years, the budget contains several statutory provisions collectively referred to as the "Non-Collecting Retailers, Referrers, and Retail Sale Facilitators Act" that altogether impose obligations on out-of-state remote sellers to either begin collecting sales tax on shipments to Rhode Island-based customers, or send coercive reminders to customers that use tax is due.

Currently, due to the U.S. Supreme Court's holding in the case of *Quill Corp. v. North Dakota*, the imposition of a sales tax collection obligation on an out-of-state seller is only permitted to the extent the seller has a greater than *de minimis* physical presence in the state of destination. The *Quill Corp*. case, which was decided before the explosive growth of the internet in the two decades following, has long been criticized by states as effectively walling off ecommerce from the reach of state sales and use tax laws. The result has been a steady and consistent erosion of the sales tax base of most states. Consequently, the *Quill Corp*. decision has recently been criticized in dicta by the U.S. Supreme Court as an anachronism.

Reasoning that the traditional definition of physical presence used in *Quill Corp*. is outdated, the budget expands the sales tax definition of physical presence to cover situations where a party's software is present on the devices of an in-state customer for the purposes of generating sales. The new definition works to apply a regulatory burden on out-of-state retailers, entities that receive commissions or exchange customer data with retailers ("referrers"), and software companies that facilitate retail transactions ("retail sale facilitators"). By including this legislation in the budget, the State of Rhode Island is laying the foundation to challenge the conventional thinking that *Quill Corp* requires a remote seller to have an agent or personal property in the state of destination in order to be subjected to a compliance burden.

The budget imposes on out-of-state retailers, referrers, and retail sale facilitators the responsibility to either register and begin collecting tax on sales to in-state customers, or provide to customers several different notices of liability. Specifically, the budget requires non-collecting retailers to do the following:

- **Conspicuously post on their websites that tax is due on certain purchases;**
- **Notify in-state customers that tax is due at the time of purchase and that Rhode Island law requires in-state customers to file use tax returns;**
- **Notify customers a second time in writing within 48 hours following checkout that use tax is due; and**
- **Provide to in-state customers with at least $100 in annual purchases an annual summary of all taxable and nontaxable purchases made by January 31st of the following tax year.**
- **Attest by February 15th of each year that they are in compliance with Rhode Island law.**

**Referrers and sales facilitators are subject to similar notice and attestation requirements. Critically, failure to comply with any of the new mandates can result in the assessment of a penalty of the greater of either $10,000 per year or $10 per failure.**

These reforms are actually the second major effort by the Rhode Island legislature to curb sales tax avoidance by remote sellers. In 2013, the legislature amended R.I. Gen. Laws §44-18-18 to provide that if a federal law was enacted to enable states to require remote sellers to collect and remit sales tax, Rhode Island’s sales tax rate would be automatically reduced from 7% to 6.5%. Since 2013 though, efforts in Congress to repeal *Quill Corp*. have completely stalled and relief under this section appears unlikely for Rhode Islanders. Presumably the enactment of the budget will not spur the legislature to consider reducing the sales tax rate.

*Exempt organizations, exemption certificates*
Starting July 1, 2017, sales and use tax exemption certificates issued to exempt organizations will only remain valid for four years from the date of issuance. Taxpayers with existing exemption certificates will be required to apply for reissuance in four years.

Seeds and Plants
Seeds and plants used to grow food and food ingredients are now exempt from sales and use tax. The budget clarifies the exclusion does not apply to marijuana seeds or plants, however.

*Enhanced penalties for willful violations*
Penalties for the willful violation of several sales and use tax provisions have been increased in the budget. Taxpayers that willfully fail to collect sales tax from customers or willfully fail to remit collected tax to the state may now be subjected to a maximum $25,000 penalty. The previous maximum penalty was $10,000. The maximum jail time for such actions was also increased from one year to five.

**Car Tax**
For Rhode Island residents, the most significant development in the budget is probably the phase-out of the Excise Tax on Motor Vehicles and Trailers (“the car tax”).

The budget phases-out the car tax gradually through 2023 before it is fully repealed in 2024. The phase-out reduces the maximum percentage of retail value an assessor may include in the tax base, provides for increased valuation exemptions, and reduces the maximum rate a locality may assess on vehicle values. Vehicles older than fifteen years old will be 100% exempt from the car tax from fiscal year 2018 and onwards.

**Corporate Income Tax and Pass-Through Entity Withholding**
*Payment of estimated taxes*
The budget changes the due date for estimated Rhode Island corporate income tax payments for tax years beginning on or after January 1, 2018. The revised due dates for quarterly estimated payments, notwithstanding holidays and weekends, will now be the 15th days of the 4th, 6th, 9th, and 12th months of each tax year. The changes were needed to coordinate with revised federal-level deadlines for corporate income tax returns and estimated tax payments. The payment due dates on other estimated tax filings have also been changed.

*Pass-through entity withholding rate*
The budget changes the rate of pass-through entity withholding for nonresident corporate members from 9% to 7%. The change was made to reconcile the withholding tax rate applicable to corporations with the corporate income tax rate which was already reduced to 7% in 2015. Despite the prior language of the statute, the Division of Taxation’s pass-through entity withholding forms already reflected the 7% rate for corporate taxpayers for the 2016 tax year.

**Other Miscellaneous Items**
*Amnesty*
The budget provides for the creation of a one-time tax amnesty program which will be available on December 1, 2017 and last through February 15, 2018. Taxpayers filing for amnesty during this period will be given an opportunity to report and pay back taxes without being subjected to any civil prosecution, criminal prosecution, or penalties. Interest is not waived. Based on the generous terms of the amnesty provisions, the amnesty program might be an ideal time for taxpayers to come forward and resolve lingering tax compliance problems.

Amnesty is available for delinquent taxes of all types that are collected by the Division of Taxation and are due for any period ending on or prior to December 31, 2016. Amnesty is not available for taxpayers who are under criminal investigation or who are parties to a criminal or civil fraud proceeding. Unlike many state amnesty programs, however, relief appears to be at least partially available for periods where the taxpayer has already received a notice of deficiency determination.

In order to qualify for amnesty, the taxpayer must pay all taxes and interest due upon the filing of an amnesty return, or alternatively enter into an installment agreement if he or she can demonstrate financial hardship. Financial hardship will eventually be defined by the Division of Taxation. Interest computed on taxes paid under amnesty is discounted by 25%. Considering that Rhode Island imposes an exceptionally high 18% rate of interest on back taxes, the 25% discount alone is potentially a boon for qualifying taxpayers.

*Hospital licensing fees*
The budget increases the hospital licensing fee rate, which is essentially a tax on net patient-services revenue, from 5.652% to 5.856%. The new rate is effective for fiscal years ending on or after January 1, 2016. Hospitals subject to the increased licensing fee are required to pay the Division of Taxation on or before July 10, 2018.

*Cigarette tax*
The stamp tax rate imposed on cigarettes was increased from 18.75% to 21.25% effective July 1, 2017. This represents an increase from $3.75 of tax per pack to $4.25. A separate 2.5% “floor stock” tax on cigarettes was also enacted. The floor stock tax is based on the number of cigarettes held by any person in inventory on August 1, 2017 and is a one-time charge designed to bring the stamp tax applied to existing cigarette inventories up to the new rate. Various other changes have been made to the definitions section of the cigarette tax laws to clarify that tax applies to other tobacco products such as pipe tobacco and chewing tobacco.

*Business transfers – notice*
The budget makes several changes to the requirements that notice must be given to the Division of Taxation when a business sells or transfer a majority of its assets. Upon such a transfer, corporate income tax, sales and use tax, and employment taxes are generally due at the time of the transfer. Unless the taxpayer gives the Division of Taxation notice of the transfer, Rhode Island reserves the right to avoid the legal effect of the transfer and impose tax liability on successors.

The budget expands the language of several such notice provisions to require that taxpayers give notice to the Division of Taxation by filing a request for a letter of good standing. The amendments also require notice be provided when there is a transfer of the assets made by a limited liability companies, limited partnerships, and other foreign and domestic entities.

*Tax procedure*
The budget gives the Division of Taxation several expanded enforcement tools. In particular, the Division of Taxation is given the power to punish generic violations of title 44 of the Rhode Island General Laws by permitting it to take various actions against violators including revoking or suspending tax licenses and permits, levying administrative penalties of up to $50,000, and enjoining prohibited activities. The Division of Taxation was also granted a general power to make jeopardy determinations for all types of taxes where the circumstances indicate a delay would endanger the state’s ability to collect.

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