

Businesses disagree on cutting sales tax

By [Nicole Dionne](#), Staff Writer

Amid efforts to make Rhode Island's tax structure more competitive, some have begun to ask whether the state's sales tax, which is the highest in New England, needs to be cut. But given the size of the budget deficit and the complexity of the issue, it's not an easy task.

At 7 percent, Rhode Island's sales tax rate is one of the highest in the nation, surpassed only by the combination of state and local taxes in some parts of the country. And with Connecticut charging only 6 percent, and Massachusetts, 5 percent, some businesses report being hurt.

For Quality Jewelers in Tiverton, about three miles from the Fall River border, the higher tax rate is such a handicap that the store often has to compensate in its prices to stay afloat.

"It's very difficult to compete," said John Fossum, the general manager. "Quite often we have days where we absorb the sales tax. For a while, during the holidays, we would do it every Saturday, or we try to give them 10 percent off so that it will more than cover the tax."

"I've had people come in and refuse to pay the tax," he added, "so if we won't pay the tax, they won't do business with us. ... We're right on the state line, so if we didn't do that, we would lose half our business."

Farther away from the state line, the effect is harder to quantify.

Keith Stokes, executive director of the Newport County Chamber of Commerce, said it would be nice to lower the sales tax, but he's not sure what effect it would have.

"I think that before a decision could be made, there would have to be a thorough examination of the costs and benefits," Stokes said. "A blanket statement that it will help business is just not enough."

For stores that sell big-ticket items such as furniture, appliances and major electronics, the sales tax almost never makes a difference, because customers who buy an item outside the state and have it delivered are charged the higher Rhode Island rate. The same is true with automobiles, for which the sales tax is paid where the car is registered.

(When a Rhode Islander buys an item outside the state and isn't charged the Rhode Island sales tax, state law requires that he or she pay the difference, called a "use tax," directly to the state. That rule, however, is difficult to enforce.)

And for high-end clothing purchases, Rhode Island can actually be better. Here, all clothes are exempt, Connecticut exempts only the first \$50 of the value, and Massachusetts, the first \$175.

The tax rate has been 7 percent since the early 1990s, when it was raised from 6 percent, purportedly on a temporary basis, to help finance the state's bailout of the Rhode Island Share and Depositors Insurance Corporation. By 1993, however, the rate had become permanent.

In recent years, convinced that the 7-percent tax rate contributes to the state's image as a high-tax place, Gov. Donald L. Carcieri and others have said they'd like to reduce it – either by just cutting it, or by modifying it so the rate drops but the tax base is expanded to compensate.

Last year, the General Assembly approved a proposal by House Speaker William J. Murphy to create a study commission to review the sales tax. The group, which includes the state tax administrator, the chief of the Office of Revenue Analysis, the chairmen of the House and Senate finance committees and four other legislators, will begin its work later this year.

In the meantime, Carcieri chose not to address the sales tax in his budget for fiscal 2008. "Ultimately, [the governor] would like to bring the Rhode Island sales tax in alignment with taxes in the neighboring states, but there hasn't been a specific proposal put forward – possibly because our budget situation in the past four years has not been as positive as we would like," said Jeff Neal, spokesman for Carcieri.

Gary S. Sasse, executive director of the Rhode Island Public Expenditure Council, said the reluctance to act is not surprising.

"You have to ask yourself: Is it fiscally prudent to reduce the sales tax at a time when there's a deficit?" he said.

There are other concerns as well – most notably, the potential tradeoffs.

David R. Carlin III, vice president of government affairs for the Northern Rhode Island Chamber of Commerce and lobbyist for the Rhode Island Chamber of Commerce Coalition, expressed concern that a lower sales tax would lead to tax increases in other areas.

"We would wholeheartedly support [lowering the sales tax] if it proved to be fiscally responsible and didn't hurt our members in other ways," he said.

The sales and use taxes are expected to yield \$929.5 million for the state in fiscal 2008, a close second to Rhode Island's top tax revenue source, the personal income tax (\$1.1 billion). Given the sales tax's importance, few believe the rate would be cut without expanding the tax base.

One way to expand the tax base that has been suggested by policy experts is to tax more services. The Federation of Tax Administrators, Sasse noted, lists 160 services that can be taxed, and Rhode Island only taxes 29. Massachusetts taxes 19, and Connecticut, 80.

Ellen Frank, senior economist at the Poverty Institute at Rhode Island College, said the sales tax could be made "more progressive" if it covered a few more services, including fees at golf courses, marinas and fitness centers, personal

services (except funeral services) and repairs and maintenance.

In some cases, the lack of a tax on services now creates odd discrepancies, Frank noted. "If you buy a bag of diapers at CVS, you pay sales tax, but if you have a diaper service, you don't pay tax," she said. "If you buy nail polish at Walgreens, you pay tax, but if you get a manicure, you don't. If we could broaden the sales tax to most services, we could probably lower the rate and not lose revenue."

But Carlin is completely against taxing services. Terrance S. Martiesian, state director of the National Federation of Independent Businesses, doesn't like the idea, either.

"If you lower the sales tax rate, then you have to expand it, but we're pretty much in line with Massachusetts with what's covered," Martiesian said. "So if you have to expand it to reduce it, you're going to run into other issues."

Changing the types of goods that are covered is another idea but that became more difficult last year when Rhode Island joined the multi-state Streamlined Sales Tax Project, which standardized definitions for what can be taxed.

The project, which aims to facilitate interstate commerce and build a foundation for making online purchases subject to state sales taxes, allows states to exempt items covered by the agreement. But states can't tax items not covered in the agreement. A few items that have become tax-exempt in Rhode Island as a result include Kool-Aid (powdered drink mixes) and candy that includes flour, such as Kit-Kats and Twix bars.

Still, there are some goods, such as boats and airplanes, that Rhode Island now exempts but that could be taxed under the agreement. The latter, which were only exempted in 2004, probably should be taxed again, Frank said.

"The rationale for exempting boats is that it would spur the local boat building industry, and certainly we have a very vital and dynamic boating industry that we would not want to mess with," she said. "But there is no airplane industry in Rhode Island, so it's not like we're preserving jobs of people making and selling airplanes in the state."

The argument for exempting planes, Frank noted, was "that it would encourage CEOs to locate their planes here and therefore relocate their jobs here. There's no proof it had any economic impact at all except to lose \$1 million in revenue for the state. I think we should be looking at all sales tax exemptions to see if they have any economic benefit."

As with other tax policy issues in Rhode Island, a shortage of information makes it harder to determine how to solve the dilemma.

"We don't have much of a sales tax burden, but we know there are border impacts," Sasse said. "We need to get some data on the impact the sales tax rate has on the ... the retail sector."