

## Changing sales tax could open 'Pandora's box'

By William Hamilton  
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Gov. Donald L. Carcieri borrowed several ideas from his tax-policy panel in drawing up the 2010 state budget proposal, but he says there was one suggested tax-structure overhaul that the state can't afford right now.

Carcieri's \$7.62 billion state budget for fiscal 2010 does not contain any recommendations to lower the state's 7 percent sales tax.

The Governor's Tax Policy Strategy Workgroup had expressed an interest in making such a move, to help the state become more competitive with Massachusetts. In the end, however, the governor decided it wasn't worth it.

An analysis showed that if Rhode Island were to match both Massachusetts' 5 percent sales tax and the goods that fall under the sales tax, the Ocean State would lose as much as \$250 million in tax revenue annually.

"The sales tax is problematic," Carcieri told Providence Business News last week. "In order to drop the rate and be 'revenue neutral,' you've got to broaden the tax incredibly."

That would mean taxing goods and services that have never been taxed in Rhode Island before. The tax work group, at one point in its months-long discussion, had developed a list of 200 items and services that could potentially be taxed, ranging from nonprescription drugs and newspapers to haircuts and car repairs.

"The thing, in my judgment, was kind of a Pandora's box," the governor said.

Instead, administration officials thought it best to focus their overhaul on the corporate income tax, personal income tax and the estate tax – in order to make the state more competitive in attracting and retaining companies, and in turn, boosting the tax base.

"If we [change the corporate, personal and estate taxes], I'm thinking we'll be in the middle of the pack between Connecticut and Massachusetts," Carcieri told PBN. "And if we bring the corporate tax down even further, as we've planned, we'll be even more attractive."

As it stands now the governor's 2010 budget proposal calls for the corporate tax to drop to 7.5 percent from 9 percent on Jan. 1, 2010, with further 2 percent decreases each year until the corporate tax is fully eliminated in 2014.

Currently, the corporate income tax rate in Massachusetts stands at 9.5 percent – it is expected to drop to 8.5 percent next year. In Connecticut, it's 7.5 percent, according to the Tax Foundation in Washington, D.C.

In addition, the proposal reduces the minimum franchise tax payment from \$500 to \$450 in 2014.

State Budget Officer Rosemary Booth Gallogly said last week that in the first phase of the corporate tax cut, the state would lose \$14.5 million in tax revenue.

That proposal drew complaints from some quarters at a time when the state has had to cut services and jobs to help deal with a projected \$347 million shortfall in fiscal 2009, and an estimated \$505 million in 2010.

The phasing out of the corporate tax and other proposals “represent a continuation of a decade of failed tax policies that cut taxes for wealthy individuals and businesses in the name of economic development,” Kate Brewster, executive director of the Poverty Institute, said last week.

In talking with PBN last week, Carcieri defended the projected loss of revenue, saying other planned measures will more than make up the difference.

“I’ve got revenues – like the cigarette tax and some other things – that are more than going to cover it,” Carcieri said, referring to the \$1-a-pack hike in the cigarette excise tax that has yet to be passed by the General Assembly.

The hike, if it takes effect by April 1, should add \$7.99 million in revenue for fiscal 2009, and another \$30.19 million in fiscal 2010.

Carcieri followed other recommendations from his tax-policy work group, including raising the threshold for the estate tax from \$675,000 – which is the lowest in the country – to \$1 million to match the exemption in Massachusetts, beginning Jan. 1.

The Carcieri administration said the higher exemption would eliminate the payment of estate taxes for 44.8 percent of Rhode Islanders subject to the estate tax. It's estimated that the estate tax savings for filers in fiscal 2010 would be \$1.49 million.

Beginning in 2011, the governor also wants to lower the state's top marginal personal income tax rate to 5.5 percent, from the current 9.9 percent, and lower the bottom rate to 3.5 percent, from the current 3.75 percent. His proposal would create four income brackets, as opposed to the current five, and would do away with itemization on state personal income tax forms.

According to the tax-policy work group's analysis, people below \$1 million in adjusted gross income (AGI) would, on average, experience a tax cut, while those above that threshold would, on average, pay more.

For instance, taxpayers with an AGI of between \$55,001 and \$75,000 would see an average tax cut of \$4.34, according to the tax panel. Someone with an AGI of more than \$10 million – and there are 36 of them in Rhode Island, according to the state – would pay, on average, \$814,346.50 more.

Laurie White, president of the Greater Providence Chamber of Commerce, praised the proposed corporate tax phaseout, particularly combined with the personal income tax changes.

While the phaseout would affect bigger companies, the personal income changes would assist S corporations where profits or taxable income are passed through to the owners, and taxes are assessed on personal income instead.

“We’re going to be more competitive [in attracting more jobs] in every sense,” said White, predicting that the state will jump in various business-related national rankings. “Right now, we’re in the cellar. ... But we have to do something that will make us stand out.”

Although Carcieri side-stepped revising the sales tax, it could be a topic of discussion as the budget process moves along. The governor said he has “heard rumors” that lawmakers might consider expanding the number of items and services that can be taxed.

He said it’s not something he would support. “Our tax burden is still too high. I’m opposed to it,” he told PBN. •