STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS

DIVISION OF TAXATION

ADMINISTRATIVE HEARING

FINAL DECISION AND ORDER

#2016-02

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
DEPARTMENT OF REVENUE
DIVISION OF TAXATION
ONE CAPITOL HILL
PROVIDENCE, RHODE ISLAND 02908

IN THE MATTER OF:	:	**Case No.: 15-T-0113**
Taxpayer.	:	

DECISION

I. INTRODUCTION

The above-entitled matter came for hearing pursuant to a Notice of Hearing and Appointment of Hearing Officer ("Notice") issued on November 19, 2015 to the above-captioned taxpayer ("Taxpayer") by the Division of Taxation ("Division"). A hearing was held on January 5, 2016. The Division was represented by counsel. The Taxpayer was *pro se*. The parties rested on the record.

II. JURISDICTION

The Division has jurisdiction over this matter pursuant to R.I. Gen. Laws § 44-1-1 *et seq.*, R.I. Gen. Laws § 44-20-1 *et seq.*, *Division of Taxation Administrative Hearing Procedures, Regulation AHP 97-01*, and the *Division of Legal Services Regulation 1 Rules of Procedure for Administrative Hearings*.

III. ISSUE

Whether the Taxpayer owes the assessment issued by the Division in relation to other tobacco products tax and if so, what should be the sanction.

IV. MATERIAL FACTS AND TESTIMONY

, Supervisor, Special Investigations Unit ("SIU"), testified on behalf of the Division. He testified that he is familiar with the Taxpayer as he was found to be distributing other tobacco products ("OTP") to a store. He testified that to distribute OTP products, one must obtain a license from the Division. He testified that if one is selling tobacco, one must have a permit to make sales at retail and a tobacco sales license. He testified that the July 11, 2015 seizure of OTP from the Taxpayer took place in Cranston and that the Taxpayer did not have a sales permit or tobacco license for that location or hold an OTP distributor license or hold any license from the Division. He testified that there is a licensed business at that location. See Division's Exhibits A and B (said business' license application and tax records). He testified that an OTP distributer needs file OTP tax monthly with the Division. He testified that if someone who is not an OTP distributor brings in OTP to the State, then that person must file the OTP tax with the Division within five (5) days. Therefore, he testified that even if the Taxpayer was not an OTP distributer, he needed to remit the OTP tax within five (5) days of possessing the OTP within Rhode Island, but no such tax was filed. There was no cross-examination.

SIU investigator, testified on behalf of the Division. He testified that on July 11, 2015, he and another SIU investigator, went to said licensed business and saw the Taxpayer getting out of a van. He testified that when they were inside the licensed business to conduct a compliance check, he saw the Taxpayer speak to the owner of the business and heard the owner indicate that he needed more "Red Bull." He testified that he exited the store with the Taxpayer and based on his experience, he thought the Taxpayer could be making a delivery of untaxed tobacco so he looked in the van's window where he saw several boxes in the van including of little cigars, although he could not tell from the label if they were considered

cigarettes or OTP. He testified that he spoke to the Taxpayer who told him that he was delivering tobacco products and that he obtained the products for delivery from an unidentified man via telephone calls and he did not know this man's name or address. He testified that he did not see any "Red Bull" in the van. He testified that he called the Cranston police because of the Taxpayer's answers. He testified that prior to the Cranston police arriving, he searched the vehicle pursuant to his authority under R.I. Gen. Laws § 4-20-40.1.

testified that they found several boxes of OTP in the van, but also found invoices indicating tobacco deliveries that had been already made. He testified that he took photographs of the boxes and one box showed the tag of a Pennsylvania distributer where OTP is not taxed. See Division's Exhibit N (photographs). He testified that there was no evidence in the van that any OTP tax had been paid. He testified that the Cranston police took statements, seized the tobacco products, and Taxpayer was given a summons for operating without a distributer's license. He testified that he made a seizure report based on the products and from the invoices seized from the van. See Division's Exhibits C (seizure report) and D (copy of invoices). There was no cross-examination.

SIU investigator, testified on behalf of the Division. He testified that he accompanied on the investigation of licensed business and he took photographs as a result of the inspection of the van. He testified that the van was registered to the Taxpayer. See Division's Exhibit O (photographs). There was no cross-examination.

Revenue Agent, SIU, testified on behalf of the Division. She testified that she prepared an audit report of the seized products and based on that report, she calculated the tax owed for the products seized. See Division's Exhibits E (audit report) and F (tax calculation). She testified that a Notice of Deficiency was issued with a penalty imposed pursuant to R.I. Gen.

Laws § 44-20-51.1. See Division's Exhibit G. She testified that she also prepared an audit report based on the seized invoices and calculated the tax owed based on the invoices. See Division's Exhibits H and I. She testified that a Notice of Deficiency was issued with a penalty assessed pursuant to R.I. Gen. Laws § 44-20-51.1. See Division's Exhibit J. Therefore, she testified that there were two (2) separate assessments: the products seized and the invoices. There was no cross-examination.

The Taxpayer testified on his behalf. He testified that he did speak to the owner of the licensed business, but there was no transaction. He testified that Noret checked his car and asked if he had tobacco and he said "yes" and that Noret asked if he had a license and he said "no." He testified that the SIU investigators went through the van before the police came and asked him who he worked for and who he delivered to. He testified that he did not have any information to give them because he just delivers the products and does not sell the products. He testified that he was told that if he cooperated the penalty could be reduced, but because he said "no," they added the invoices to their seizure. He testified that the invoices were for candy and other non-tobacco items that he would also sell/deliver.

On cross-examination, the Taxpayer testified that he did have OTP products that day for delivery and that he had been making those types of deliveries for one (1) month. He testified that he did not know that one needed a distributer license to deliver OTP. He testified that a man would call him to make the deliveries and he would pick the deliveries up where he was told to pick them up but he did not know who the individual was. He testified that the invoices were for candy and "Red Bull" and not tobacco and that he would buy items at Walmart and resell them. He testified that he knew he needed a sales permit to sell items at retail. He testified that the owner did tell the investigators that he had not bought anything.

The Division recalled who reviewed invoice 0240901 (Division's Exhibit D) and testified that the first four (4) notations on that invoice indicated tobacco products such as blue ("game blue") and the fifth item was "CH Gum" so it could mean "chewing gum."

V. DISCUSSION

A. Legislative Intent

The Rhode Island Supreme Court has consistently held that it effectuates legislative intent by examining a statute in its entirety and giving words their plain and ordinary meaning. *In re Falstaff Brewing Corp.*, 637 A.2d 1047 (R.I. 1994). If a statute is clear and unambiguous, "the Court must interpret the statute literally and must give the words of the statute their plain and ordinary meanings." *Oliveira v. Lombardi*, 794 A.2d 453, 457 (R.I. 2002) (citation omitted). The Supreme Court has also established that it will not interpret legislative enactments in a manner that renders them nugatory or that would produce an unreasonable result. See *Defenders of Animals v. Dept. of Environmental Management,* 553 A.2d 541 (R.I. 1989) (internal citation omitted). In cases where a statute may contain ambiguous language, the Supreme Court has consistently held that the legislative intent must be considered. *Providence Journal Co. v. Rodgers*, 711 A.2d 1131 (R.I. 1998).

B. Relevant Statutes

R.I. Gen. Laws § 44-20-12 imposes a tax on cigarettes sold. R.I. Gen. Laws § 44-20-13.2 applies to "other tobacco products" and provides as follows:

> Tax imposed on smokeless tobacco, cigars, and pipe tobacco products.
> (a) A tax is imposed on all smokeless tobacco, cigars, and pipe tobacco products sold or held for sale in the state by any person, the payment of the tax to be accomplished according to a mechanism established by the administrator, division of taxation, department of administration. Any tobacco product on which the proper amount of tax provided for in this chapter has been paid, payment being evidenced by a stamp, is not subject to a further tax under this chapter. The tax imposed by this section shall be as follows:

(1) At the rate of eighty percent (80%) of the wholesale cost of cigars, pipe tobacco products and smokeless tobacco other than snuff.

(2) Notwithstanding the eighty percent (80%) rate in subsection (a) above, in the case of cigars, the tax shall not exceed fifty cents ($.50) for each cigar.

(3) At the rate of one dollar ($1.00) per ounce of snuff, and a proportionate tax at the like rate on all fractional parts of an ounce thereof. Such tax shall be computed based on the net weight as listed by the manufacturer, provided, however, that any product listed by the manufacturer as having a net weight of less than 1.2 ounces shall be taxed as if the product has a net weight of 1.2 ounces.

(b) Any dealer having in his or her possession any tobacco, cigars, and pipe tobacco products with respect to the storage or use of which a tax is imposed by this section shall, within five (5) days after coming into possession of the tobacco, cigars, and pipe tobacco in this state, file a return with the tax administrator in a form prescribed by the tax administrator. The return shall be accompanied by a payment of the amount of the tax shown on the form to be due. Records required under this section shall be preserved on the premises described in the relevant license in such a manner as to ensure permanency and accessibility for inspection at reasonable hours by authorized personnel of the administrator.

(c) The proceeds collected are paid into the general fund.

Rule 5 of the Division of Taxation's *Tax on Other Tobacco Products Regulation* – OTP 14-01 ("OTP 14-01") defines other tobacco products as follows:

(h) "Other Tobacco Product/s" (OTP) means any cigars (excluding Little Cigars which are subject to cigarette tax), cheroots, stogies, smoking tobacco (including granulated, plug cut, crimp cut, ready rubbed and any other kinds and forms of tobacco suitable for smoking in a pipe or otherwise), chewing tobacco (including Cavendish, twist, plug, scrap and any other kinds and forms of tobacco suitable for chewing), any and all forms of hookah and shisha tobacco, snuff, and shall include any other articles or products made of tobacco or any substitute therefore, except cigarettes.

R.I. Gen. Laws § 44-20-2 provides as follows:

Importer, distributor, and dealer licenses required – Licenses required. – Each person engaging in the business of selling cigarette and/or any tobacco products in this state, including any distributor or dealer, shall secure a license from the administrator before engaging in that business, or continuing to engage in it. A separate application and license is required for each place of business operated by a distributor or dealer; provided, that an operator of vending machines for cigarette products is not required to obtain a distributor's license for each machine. If the applicant for a license does not have a place of business in this state, the license shall be issued for such applicant's principal place of business, wherever located. A licensee shall notify the administrator within thirty (30) days in the event that it changes its principal place of business. A separate license is required for each class of business if the applicant is engaged in more than one of the activities required to be licensed by this section. No person shall

maintain or operate or cause to be operated a vending machine for cigarette products without procuring a dealer's license for each machine.

R.I. Gen. Laws § 44-20-40.1 provides in part as follows:

> Inspections. – (a) The administrator or his or her duly authorized agent shall have authority to enter and inspect, without a warrant during normal business hours, and with a warrant during nonbusiness hours, the facilities and records of any manufacturer, importer, distributor or dealer.
>
> (b) In any case where the administrator or his or her duly authorized agent, or any police officer of this state, has knowledge or reasonable grounds to believe that any vehicle is transporting cigarettes in violation of this chapter, the administrator, such agent, or such police officer, is authorized to stop such vehicle and to inspect the same for contraband cigarettes

R.I. Gen. Laws § 44-20-51.1 provides in part as follows:

> Civil penalties. –
>
> ***
>
> (b) Whoever fails to pay any tax imposed by this chapter at the time prescribed by law or regulations, shall, in addition to any other penalty provided in this chapter, be liable for a penalty of not more than five (5) times the tax due but unpaid.
>
> (c) When determining the amount of a penalty sought or imposed under this section, evidence of mitigating or aggravating factors, including history, severity, and intent, shall be considered.

C. Arguments

The Division argued that the Taxpayer delivered OTP in Rhode Island without the statutory required license. The Division argued that under R.I. Gen. Laws § 44-20-13.2, any person possessing OTP is required to pay the tax owed within five (5) days as either a distributer or as a consumer. The Division argued that its assessment is based on seized products and invoices for tobacco products for which there was no evidence that any OTP was paid.

The Taxpayer argued that the assessment on the invoices was not based on tobacco products and he did not know about the licensing requirement.

D. The Taxpayer Owes the Tax Assessed

It is undisputed that the Taxpayer was unable to provide evidence to demonstrate that he had paid tax on the seized other tobacco products. R.I. Gen. Laws § 44-20-13.2(b) and Rule 8 of the *Division's Tax on Other Tobacco Products Regulation* – OTP 14-01 ("OTP 14-01") require that other tobacco products' distributors[1] keep on-site complete and accurate records of all tobacco products purchased. Pursuant to R.I. Gen. Laws § 44-20-13.2, tax is to be paid on OTP. The Taxpayer had not paid tax on the seized OTP and had no records regarding the OTP. Rule 10 of the OTP 14-01 provides that any other tobacco products that are possessed, stored, retained, or otherwise brought in the State in violation of R.I. Gen. Laws § 44-20-13.2 and the OTP regulation shall be considered untaxed contraband. Pursuant to Rule 10 of OTP 14-01, the seized other tobacco products were considered contraband pursuant since they were being possessed, stored, and retained in the State in violation of the statute and the regulation. R.I. Gen. Laws § 44-20-13.2 provides for the amount of tax that is assessed on other tobacco products and Rule 11 of OTP 14-01 provides that the Division shall issue a Notice of Deficiency for the amount of tax due and that a penalty may be imposed for the failure to pay tax on other tobacco products. Therefore, the Division properly assessed the tax owed on the seized other tobacco products.

The Taxpayer argued that the assessment based on the seized invoices included non-tobacco assessments. However, he did not identify any specific item in the assessment that he believed was for non-tobacco products. The testimony indicated that one invoice included chewing gum, but a review of the computation for the assessment did not include the chewing gum. Indeed, a review of the computation for the invoice assessment indicated that it is only for tobacco products. E.g. Dutch Masters, Game Blue, Zig Zags, etc. See Division's Exhibit I. In

[1] The Taxpayer is included in the regulation's definition of distributor as a distributor of other tobacco products.

addition, the Taxpayer did not provide any evidence demonstrating that he had paid tax on the tobacco products included in the seized invoices. Therefore, the Division properly assessed the tax owed on the other tobacco products based on the seized invoices.

E. What are the Appropriate Penalties

R.I. Gen. Laws § 44-20-51.1 was amended effective June 23, 2014. The amendment changed penalties from specific amounts to be "not more than five (5) times" a certain amount. The Notice of Deficiencies assessed the Taxpayer the tax owed and the penalty pursuant to R.I. Gen. Laws § 44-20-51.1(b) which is to be not more than five (5) times the tax owed.[2] The penalty (b) assessed by the Division on the other tobacco products was the maximum allowed which is five (5) times the tax due. Since the new statute is now providing that penalties (both in (a) and (b)) be calculated as "not more than" rather than the old statute that mandated a specific penalty, the new law added subsection (c) which provides that when determining the penalty to be imposed, mitigating and aggravating factors such as history, severity, and intent shall be considered. Thus, the statute envisions some kind of progressive discipline based on the history of offenses with the penalties becoming greater based on aggravating factors.

In this situation, the Taxpayer claimed not to know that a dealer's license was required. Ignorance of the law is not a defense. See *McElroy v. Hawksley*, 196 A.2d 172 (R.I. 1963). Furthermore, the Taxpayer's testimony that he did not know the person who asked him to make deliveries should have raised questions in the Taxpayer's mind whether the delivery procedure was complying with legal requirements. It is not a stretch of imagination to believe that in this scenario delivering items for an unknown person might not be legally compliant with some law.

---

[2] The Division's position is that only the statutory penalty (b) can be applied to other tobacco products and that position is set forth in Rule 11 of OTP 14-01. R.I. Gen. Laws § 44-20-51.1 provides for a penalty in sections (a) and (b), but the only penalty applied to the deficiencies in this matter are pursuant to R.I. Gen. Laws § 44-20-51.1(b).

Nonetheless, R.I. Gen. Laws § 44-20-51.1 requires that history, severity, and intent be considered when determining which penalty to apply. This is the Taxpayer's first offense. He testified that his deliveries only started in the last month. In terms of severity, the tax owed by the Taxpayer amounts to . Since the statute requires that mitigating and aggravating factors be included in the calculation of penalties, it follows that the maximum penalty is not to be automatically applied. If the severity is to be considered,[3] it would also follow that the higher the tax owed, the higher the penalty imposed. Of course, if it was a taxpayer's second or third offense than the amount of tax owed would not be such a mitigating factor since it would be offset by the history of the taxpayer and the intent in that it would not be a first offense. If the tax owed was extremely high that might offset mitigation for a first offense as it might be that such a taxpayer was well aware of the statute and egregiously flouting the law. Nonetheless, the statute calls for a consideration of aggravating and mitigating factors. This is the Taxpayer's first offense. While the tax owed is not minimal, it is not excessively (severe) high. Therefore, the maximum penalty should not be applied. Instead, a penalty representing two (2) times the tax owed (on both deficiencies) should be applied.

VI. FINDINGS OF FACT

1. Other tobacco products and tobacco invoices were seized from the Taxpayer on July 11, 2015.

2. The Taxpayer has no previous violations.

3. A hearing was held on January 5, 2015. The Taxpayer was *pro se* and the Division were represented by counsel. The parties rested on the record.

4. The facts contained in Section IV and V are reincorporated by reference herein.

[3] The term "severe" in the statute is not defined and could apply not only to the amount of tax owed, but the method used by a taxpayer to avoid paying the statutory tax.

VII. CONCLUSIONS OF LAW

Based on the testimony and facts presented:

1. The Division has jurisdiction over this matter pursuant to R.I. Gen. Laws § 44-1-1 *et seq*. and R.I. Gen. Laws § 44-20-1 *et seq*.

2. The Taxpayer violated R.I. Gen. Laws § 44-20-1 *et seq*. on July 11, 2015.

VIII. RECOMMENDATION

Based on the above analysis, the Hearing Officer recommends as follows:

Pursuant to R.I. Gen. Laws § 44-20-1 *et seq*. and R.I. Gen. Laws § 44-20-13.2, the tax owed was properly assessed, but in light of the parameters of the R.I. Gen. Laws § 44-20-51.1(b) and (c), the penalties are reduced to twice the amount of the taxed owed on the two (2) deficiencies.

Date: February 8, 2016

Catherine R. Warren
Hearing Officer

ORDER

I have read the Hearing Officer's Decision and Recommendation in this matter, and I hereby take the following action with regard to the Decision and Recommendation:

✓ ADOPT
_____ REJECT
_____ MODIFY

Dated: 2/12/16

Neena S. Savage
Acting Tax Administrator

NOTICE OF APPELLATE RIGHTS

THIS DECISION CONSTITUTES A FINAL ORDER OF THE DIVISION. THIS ORDER MAY BE APPEALED TO THE SIXTH DIVISION DISTRICT COURT PURSUANT TO THE FOLLOWING WHICH STATES AS FOLLOWS:

R.I. Gen. Laws § 44-20-48 Appeal to district court.

Any person aggrieved by any decision of the tax administrator under the provisions of this chapter may appeal the decision within thirty (30) days thereafter to the sixth (6th) division of the district court. The appellant shall at the time of taking an appeal file with the court a bond of recognizance to the state, with surety to prosecute the appeal to effect and to comply with the orders and decrees of the court in the premises. These appeals are preferred cases, to be heard, unless cause appears to the contrary, in priority to other cases. The court may grant relief as may be equitable. If the court determines that the appeal was taken without probable cause, the court may tax double or triple costs, as the case demands; and, upon all those appeals, which may be denied, costs may be taxed against the appellant at the discretion of the court. In no case shall costs be taxed against the state, its officers, or agents. A party aggrieved by a final order of the court may seek review of the order in the supreme court by writ of certiorari in accordance with the procedures contained in § 42-35-16.

CERTIFICATION

I hereby certify that on the 10th day February, 2016 a copy of the above Decision and Notice of Appellate Rights was sent by first class mail to the Taxpayer's address on record with the Division and by hand delivery to Meaghan Kelly, Esquire, Department of Revenue, Division of Taxation, One Capitol Hill, Providence, RI 02908.

Lori Belasco