Governor's FY 2021 Budget: Articles

Staff Presentation to the House Finance Committee
September 23, 2020

Introduction

- Article 8
  - Governor requested an amendment on August 18
  - Temporarily decouples Rhode Island income tax from federal excess business loss rules
    - To address potential revenue loss from provision of the CARES Act
    - Excess losses refer to “active” participants in the day to day of a business entity
      - Not passive participants like shareholders

COVID-19 Relief Background

- There have been 4 federal acts to address the public health emergency
  - Coronavirus Preparedness & Response Supplemental Appropriations Act – March 6
  - Families First Coronavirus Response Act – March 18
  - CARES Act – March 27
  - Paycheck Protection Program & Health Care Enhancement Act – April 24

COVID-19 Relief Background

- Federal acts include funding for
  - State and local budgets
    - Strings and limitations
  - Individuals
    - Direct stimulus payments
    - Optional tax changes
  - Businesses
    - Loans
    - Optional tax changes

COVID-19 Relief Background

- Some tax changes in the CARES Act affect state tax revenues
  - Depends on link to state tax structure
- May 2020 Revenue Conference
  - Department of Revenue provided estimated value of these changes, if available
    - Reported that some impacts indeterminable
  - Revenue estimates included impacts as reported for FY 2020 and FY 2021

COVID-19 Relief Background

- Prior to 2017, individual taxpayer's excess business losses could offset the nonbusiness income without limitation
- The Tax Cut and Jobs Act (TCJA) adopted in December 2017 contained dozens of changes to multiple tax types
  - Limited amount of excess business losses a taxpayer can claim each year to $250k/$500k joint
    - Excess business losses are deferred into future years

COVID-19 Relief Background

- The CARES Act suspends the cap on excess business losses for pass-through entities imposed in the TCJA
  - Effective for tax years 2018, 2019 and 2020
  - This was one provision for which DOR was unable to provide a fiscal impact for REC
- Further review in the following months resulted in revised analysis suggesting a 2-year, $29.1 million impact
  - Same estimate as used for TCJA impacts

Article 8 – Requested Amendment

- The Governor's requested amendment does two things
  - Disallows excess loss deduction in tax years 2018 through 2020 by adding that amount to Rhode Island taxable income
  - Allows for 20% of the disallowed deduction to be taken each year for tax years 2021 through 2025

Article 8 – Requested Amendment

- Most states use federal tax law as starting point for their own tax codes
  - Some use fixed point in time, but many automatically conform to changes as they occur
  - Some of the CARES Act temporary changes will flow through to state taxes
    - States may chose to decouple from certain changes to avoid negative revenue impacts

Article 8 – Requested Amendment

- Examples from other states
  - Nebraska & North Carolina decoupled from business loss provision as proposed in amendment
  - Colorado decoupled from several provisions
    - For both corporate & personal income tax
  - Massachusetts is not coupled to federal law on this issue
  - Connecticut remains coupled to this CARES Act provision

Article 8 – Requested Amendment

Fiscal Year	2020	2021	2022	2023	2024	2025	2026
Current Law	$(18.8)	(10.3)	-	-	-	-	-
GBA	$ -	-	(5.8)	(5.8)	(5.8)	(5.8)	(5.8)

- FY 2020 preliminary closing assumed $18.8 million in potential refunds
  - Would be reversed if Assembly enacts provision before Controller issues final closing report
- FY 2021 estimate would need to reflect revenue loss absent state law change

Article 8 – Requested Amendment

- FY 2021 Impact
  - 692 returns
    - 70% of those with federal adjusted gross income over $1.0 million
    - 64% of returns from non-residents
  - Average tax change ~ $15,000
  - 80% of revenue to be paid by Rhode Island residents

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