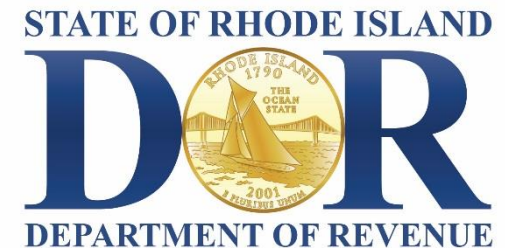


Senate Finance Committee: State Revenue Briefing

Rhode Island Department of Revenue

January 28, 2021

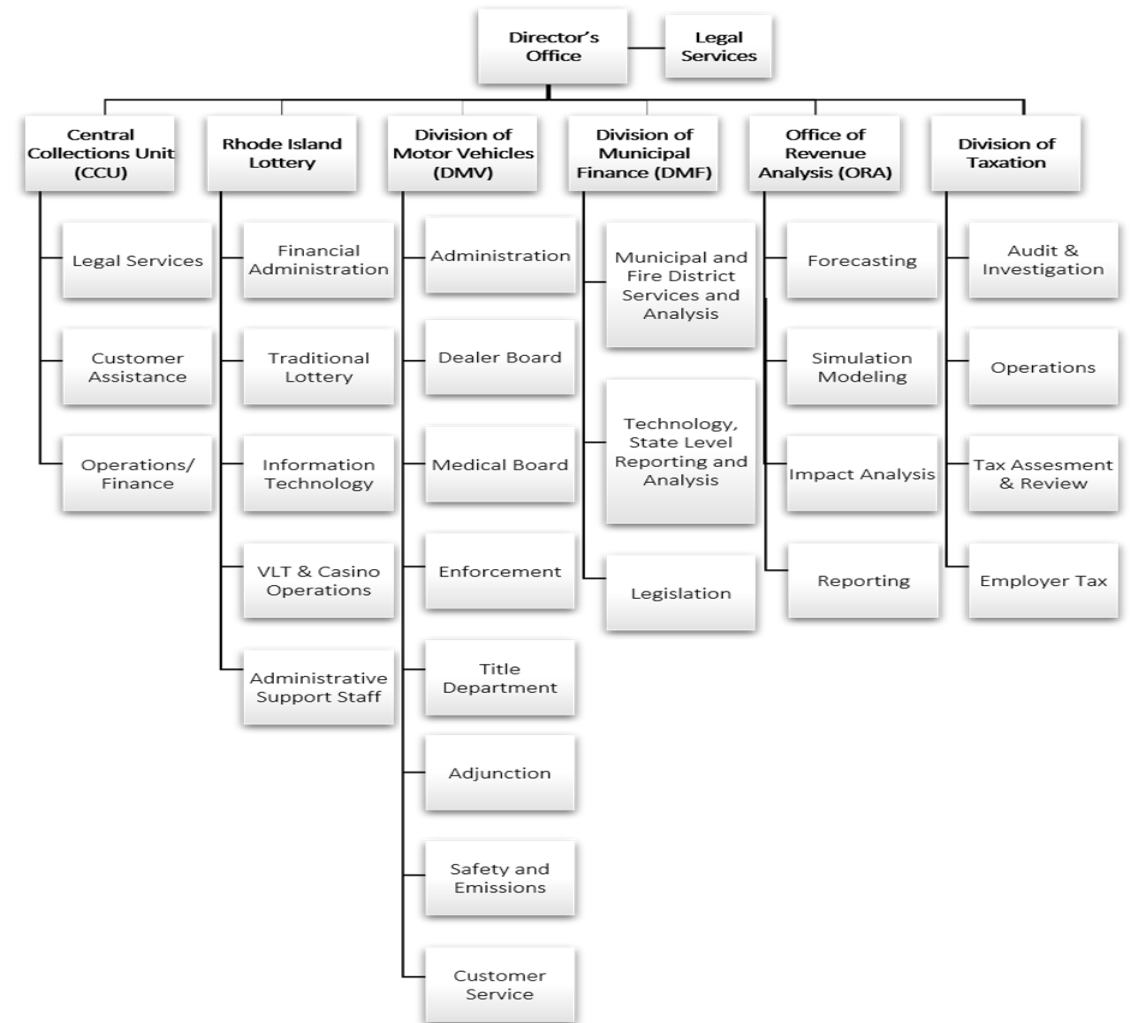


Presentation Outline

- Introduction to the Department of Revenue
- Current Revenues as of December 2020
- A Comparison of Rhode Island Revenues to Other States
- Revenue Impacts of the COVID-19 Pandemic
- Federal Tax Law Changes Included in the Coronavirus Relief Package
- Revenue Trends and Projections

The Department of Revenue

- 600 authorized employees (FTEs)
- 6 divisions, excluding the Director's Office and Legal Services
- 1.6+ million driver's licenses, IDs, and vehicle registrations managed by the DMV
- 2.4+ million tax filings annually processed within Taxation
- \$3.4+ billion in revenue in Fiscal Year 2020- approximately one-third of the state's annual budget



Department of Revenue Reports

- The Department of Revenue issues five reports a month on state revenues
 - The Monthly and Fiscal Year-to-Date (YTD) Revenue Assessment Report
 - Compares adjusted general revenues by source to expected general revenues by source based on official revenue estimates on a monthly and fiscal YTD basis
 - ❖ July through October reports use enacted revenue estimates
 - ❖ November through April reports use November Revenue Estimating Conference (REC) revised estimates
 - ❖ May report uses the May REC revised estimates
 - ❖ In lieu of a June report, a special report on fiscal year preliminary revenues is released in September
 - The Monthly and Fiscal YTD Cash Collections Report
 - Compares actual cash receipts to prior period cash receipts on a year-over-year (YoY) and fiscal YTD-over-fiscal YTD basis

Department of Revenue Reports

- The Local 1% Meal and Beverage Tax Collections Report
 - Reports the amount of local 1% meal and beverage tax collections by municipality on a month-to-month (MtM), YoY, and fiscal YTD-over-fiscal YTD basis for the period of activity

- The Local 1% Hotel Tax Collections Report
 - Reports the amount of local 1% hotel tax collections by municipality on a MtM, YoY, and fiscal YTD-over-fiscal YTD basis for the period of activity
 - ❖ Report breaks out the local 1% hotel tax collections by source for each municipality
 - ✓ Traditional hotels, motels, and bed and breakfasts
 - ✓ Room resellers and hosting platforms
 - ✓ Realtors and homeowners

Department of Revenue Reports

- The State 5% Hotel Tax Collections Report
 - Reports the distribution of the state hotel tax to tourism districts, municipalities, Rhode Island Commerce Corporation (CommerceRI) and the Providence Warwick Convention & Visitors Bureau (PWCVB) on a Y-o-Y and fiscal YTD-over-fiscal YTD basis for the period of activity
 - ❖ Report breaks out state 5% hotel tax collections by source for each tourism district, municipality, CommerceRI, and PWCVB
 - ✓ Traditional hotels, motels, and bed and breakfasts
 - ✓ Room resellers and hosting platforms
- All of these reports are posted on the Department of Revenue's website: www.dor.ri.gov and can be found under the Revenue Analysis link and the State Reports tab or the Local Reports tab depending on the report.

Rhode Island December Revenues

- The FY 2021 Monthly and YTD Revenue Assessment Report for December 2020 was released on Friday, January 22, 2021. The major fiscal YTD findings of the report were:

Revenue Item	Adjusted Revenues	Expected Revenues	Difference	Variance
Total General Revenues	\$1,936,242,184	\$1,878,236,121	\$58,006,063	3.1%
Personal Income Tax	\$735,452,743	\$704,268,543	\$31,184,220	4.4%
<i>Final Payments</i>	<i>\$76,429,326</i>	<i>\$49,287,624</i>	<i>\$27,141,702</i>	<i>55.1%</i>
<i>Withholding Payments</i>	<i>\$631,831,764</i>	<i>\$620,973,833</i>	<i>\$10,857,931</i>	<i>1.7%</i>
Sales and Use Tax	\$656,353,394	\$642,714,892	\$13,638,502	2.1%
Business Corporation Tax	\$70,922,750	\$64,748,736	\$6,174,015	9.5%
Departmental Receipts	\$95,110,187	\$90,833,333	\$4,276,855	4.7%
Lottery Transfer	\$108,739,299	\$109,561,033	\$(821,734)	-0.8%

Rhode Island December Revenues

- The major monthly findings of the report were:

Revenue Item	Adjusted Revenues	Expected Revenues	Difference	Variance
Total General Revenues	\$404,267,056	\$370,803,294	\$33,463,763	9.0%
Personal Income Tax	\$155,133,152	\$146,307,235	\$8,825,917	6.0%
<i>Estimated Payments</i>	\$15,546,530	\$24,924,409	\$(9,377,879)	-37.6%
<i>Final Payments</i>	\$30,990,361	\$5,983,835	\$25,006,526	417.9%
<i>Withholding Payments</i>	\$117,363,787	\$121,218,720	\$(3,854,933)	-3.2%
<i>Refunds and Adjustments</i>	\$(8,767,526)	\$(5,819,729)	\$(2,947,797)	50.7%
Sales and Use Tax	\$100,625,774	\$93,263,823	\$7,361,951	7.9%
Business Corporation Tax	\$32,609,619	\$26,327,721	\$6,281,898	23.9%
Departmental Receipts	\$17,355,849	\$14,290,827	\$3,065,022	21.4%
Lottery Transfer	\$19,681,290	\$20,503,024	\$(821,734)	-4.0%

RI Revenues vs Other States: December 2020

- The December 2020 YoY cash receipts for other Northeastern states with available data for selected revenue sources is below:

Revenue Item	CT	MA	MD	NH	NJ	NY	PA	RI	VT
Personal Income Tax	15.3%	3.1%	19.4%	n/a	18.3%	12.7%	12.8%	6.3%	15.2%
<i>Estimated Payments</i>	15.6%	-2.6%	No data	n/a	No data	-11.6%	-1.2%	2.7%	22.0%
<i>Final Payments</i>		16.6%	No data	n/a	No data	43.2%		24.0%	-20.4%
<i>Withholding Payments</i>	15.2%	3.4%	No data	n/a	No data	14.6%	14.6%	1.2%	13.7%
<i>Refunds and Adjustments</i>	No data	-19.6%	No data	n/a	No data	-13.9%	-45.6%	-34.8%	-26.9%
Sales and Use Tax	-12.4%	-1.5%	-7.3%	n/a	2.7%	-4.7%	4.2%	10.0%	16.0%
Business Corporation Tax	11.1%	51.7%	83.0%	6.8%	34.3%	6.1%	42.3%	44.7%	92.9%

* Data is from the research section of the Federation of Tax Administrators.

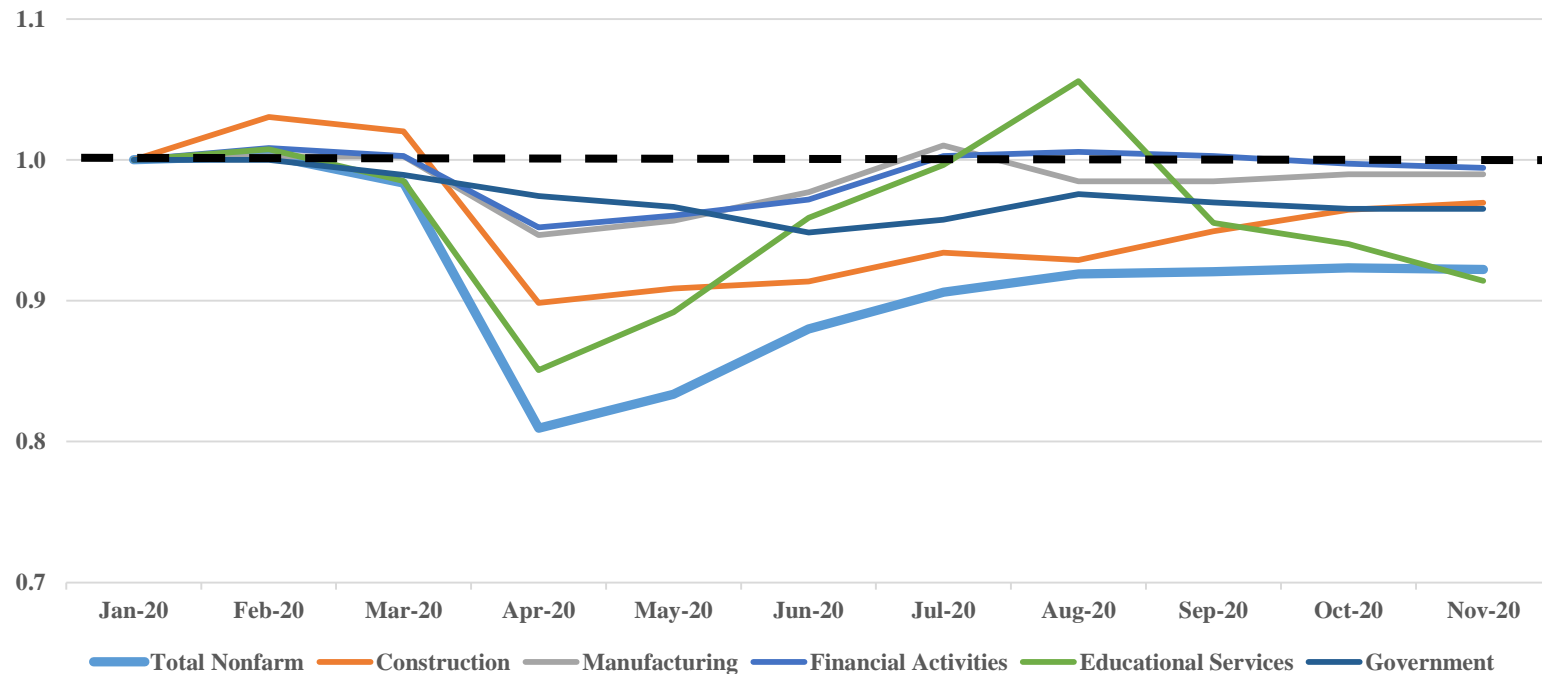
- Different tax rates, tax bases, and categorizations of receipts by each state makes interpretation of these results a challenge.



Revenue Impacts of the COVID-19 Pandemic

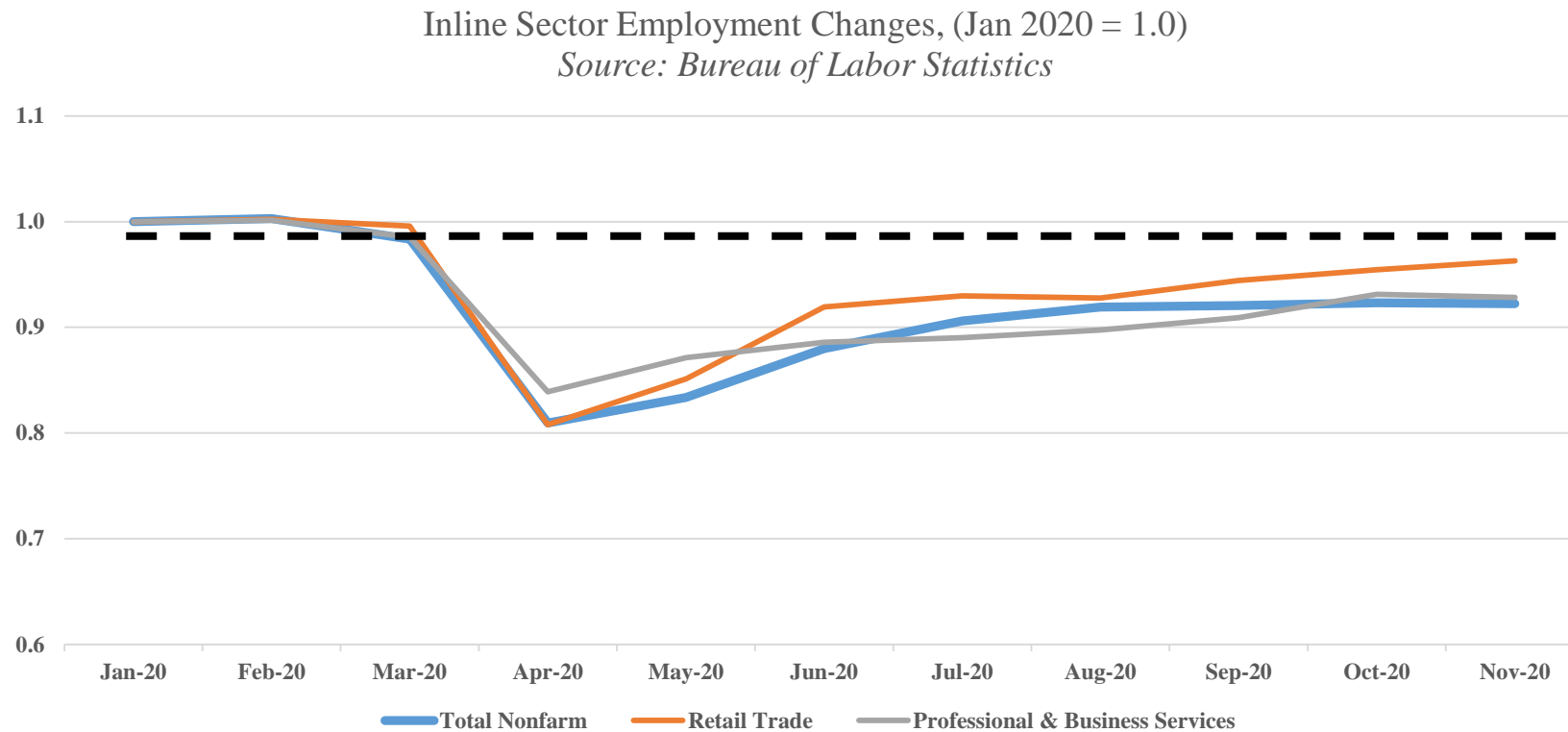
- Economically, the impact of the COVID-19 pandemic has been uneven across Rhode Island's economy:

Overperforming Sector Employment Changes, (Jan 2020 = 1.0)
Source: Bureau of Labor Statistics



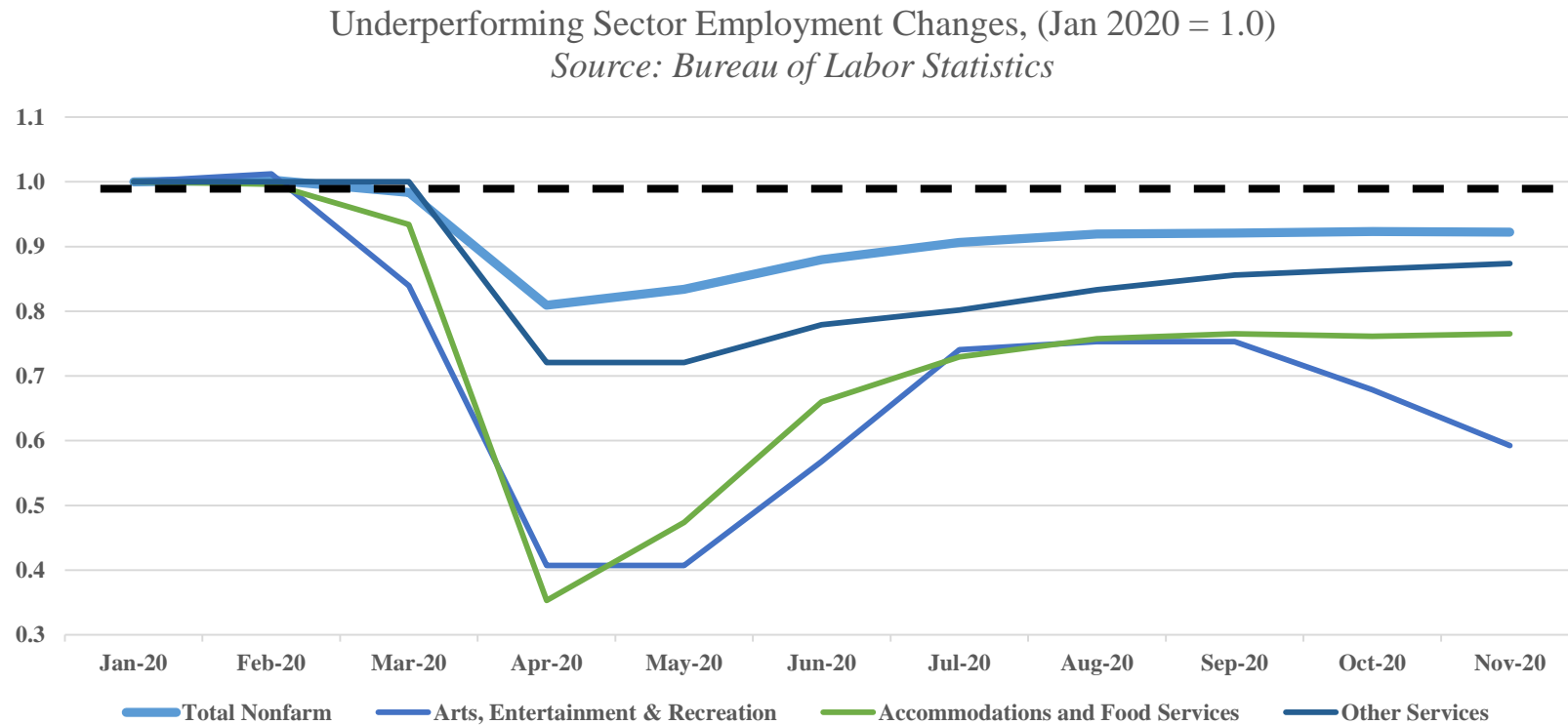
Revenue Impacts of the COVID-19 Pandemic

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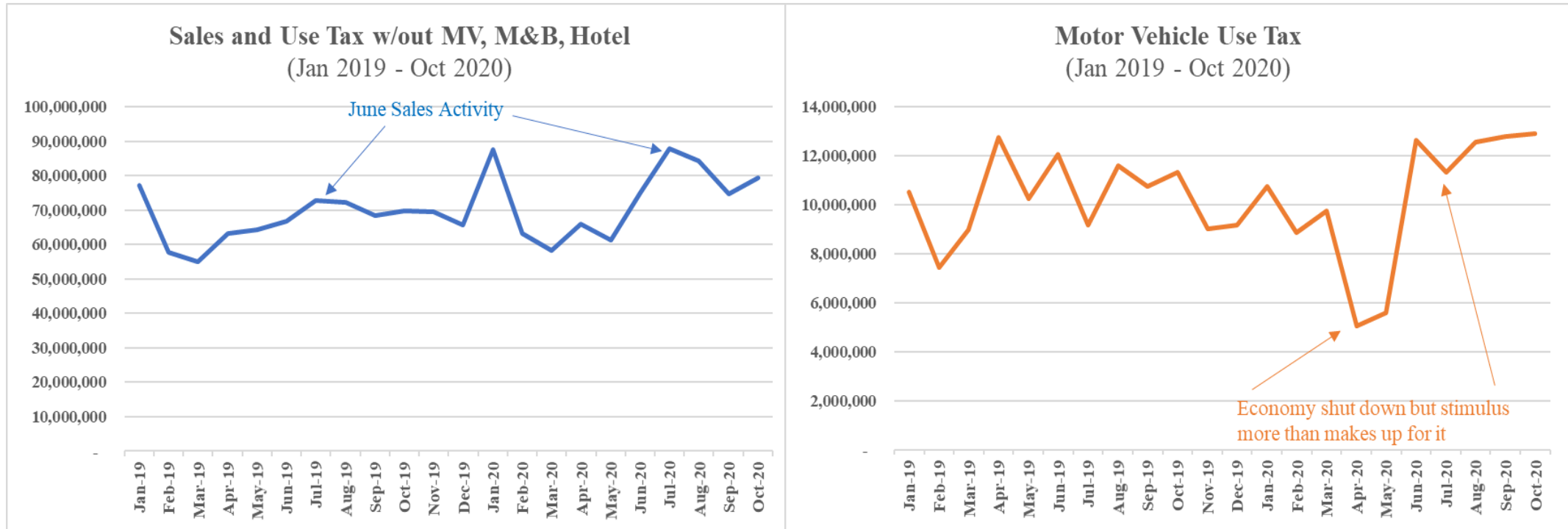
Revenue Impacts of the COVID-19 Pandemic

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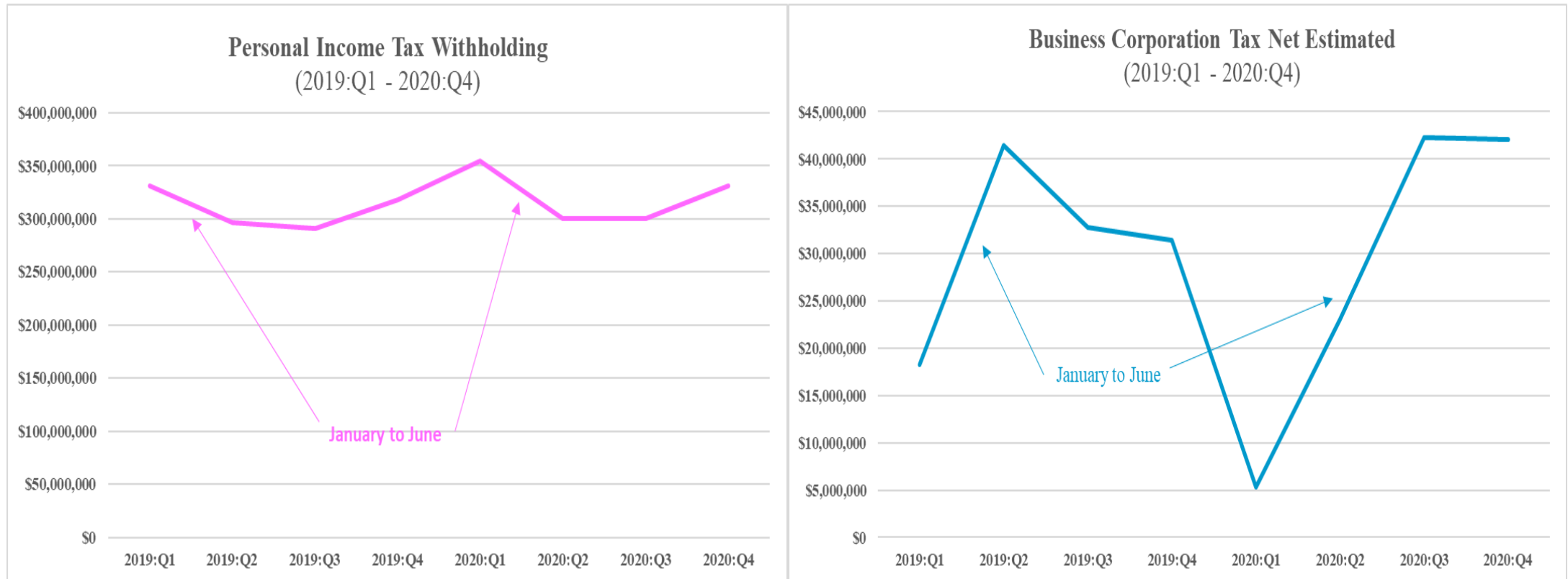
Revenue Impacts of the COVID-19 Pandemic

- Some revenues have done well even with the impact of COVID-19:



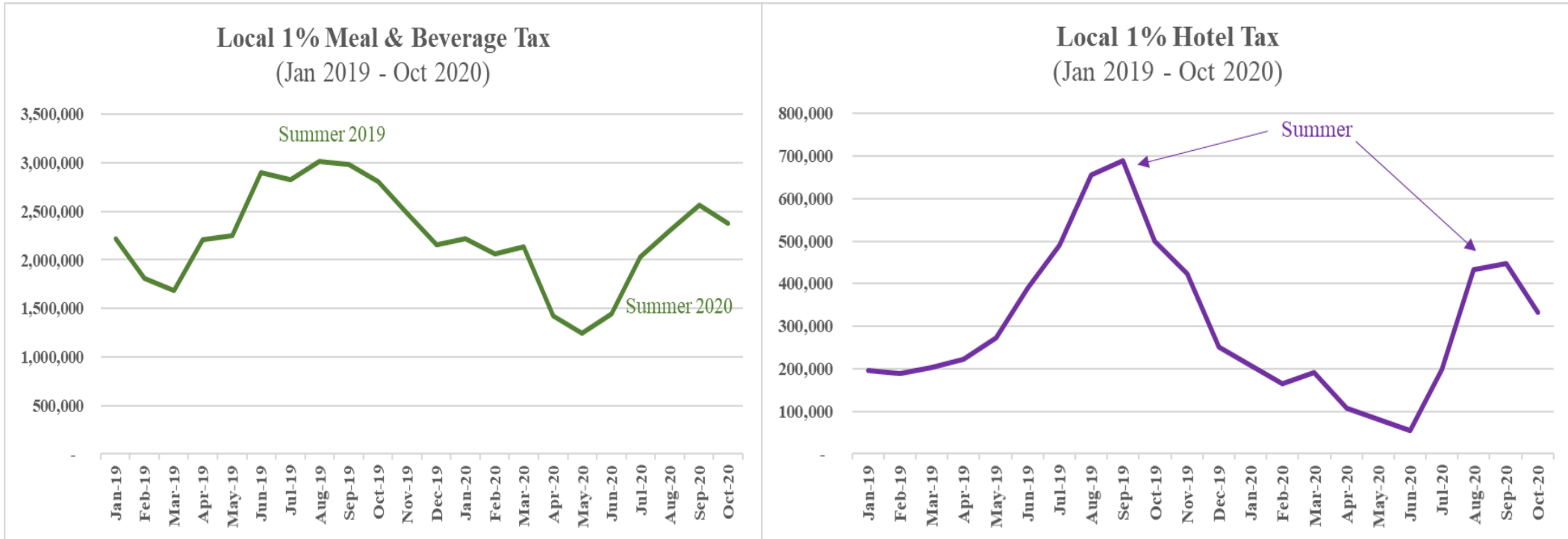
Revenue Impacts of the COVID-19 Pandemic

- Other revenues appear to have recovered from initial COVID-19 impacts:



Revenue Impacts of the COVID-19 Pandemic

- But other revenues continue to negatively impacted by COVID-19:



Coronavirus Relief Package: Tax Law Changes

- Tax treatment of Paycheck Protection Program (PPP) Loans
 - The CARES Act made PPP loans available to small businesses in TY 2020 to allow them to continue to pay payroll and other expenses in the face of the COVID-19 pandemic
 - Small business is a non-public company with no more than 500 employees
 - If the proceeds from a PPP loan are spent according to federal requirements, then the PPP loan would be forgiven
 - These requirements are that 60% of the PPP loan proceeds be spent on payroll costs and 40% on other eligible expenses such as rent, utilities, etc.
 - IRS regulations stipulate that a forgiven loan, technically referred to as cancellation of debt, has to be recognized as income in the tax year in which the loan is forgiven
 - The CARES Act deemed PPP loan forgiveness as tax exempt income

Coronavirus Relief Package: Tax Law Changes

- IRS regulations have also held that expenses paid for with tax exempt income cannot be deducted against other taxable income sources
 - In August 2020, the IRS issued guidance saying that the qualified expenses paid with forgiven PPP loan proceeds could not be deducted from other taxable income
- The Coronavirus Relief Package (CRP) signed into law on December 27, 2020 changed the law, nullifying the IRS guidance that would not allow for expenses paid with forgiven PPP loan proceeds to be deducted against other taxable income sources
 - One effect of this change in the tax treatment of the deductibility of expenses paid with tax exempt income (PPP loan) is to provide a “double” benefit to taxpayers

Coronavirus Relief Package: Tax Law Changes

- A simplified example:

No PPP Loan	Normal TY 2020	Pandemic TY 2020	Explanation
Gross Sales	\$100.00	\$50.00	COVID-19 pandemic impact reduces sales by 50%
Total Expenses	90.00	45.00	Business reduces expenses proportional to revenue decline
Net Income	\$10.00	\$5.00	Business net income decreases

- Without a PPP loan, the business reduces variable expenses, such as labor costs, by laying off workers and increasing unemployment
- PPP loan is made available so business can retain workforce and not add to unemployment

Coronavirus Relief Package: Tax Law Changes

- A PPP loan is now made available to the business under CARES Act and IRS August 2020 guidance:

With PPP Loan & IRS Aug 2020 Guidance	Pandemic TY 2020	Pandemic TY 2020	Explanation
Gross Sales	\$50.00	\$50.00	COVID-19 pandemic impact reduces sales by 50%
Total Expenses	45.00	[90.00]	Business pays expenses with PPP loan that is forgiven so cannot deduct expenses
Net Income	\$5.00	\$50.00	Business net income increases

- Under the August 2020 IRS guidance, business realizes an increase in net income above what would have been realized without the PPP loan

Coronavirus Relief Package: Tax Law Changes

- CRP passes and nullifies IRS regulations regarding the deductibility of expenses paid with forgiven PPP loan (tax exempt income):

With PPP Loan & CRP Expense Deductibility	Pandemic TY 2020	Pandemic TY 2020	Explanation
Gross Sales	\$50.00	\$50.00	COVID-19 pandemic impact reduces sales by 50%
Total Expenses	[90.00]	90.00	Business can deduct expenses paid with PPP loan against other taxable income
Net Income	\$50.00	\$(40.00)	Business net income decreases

- Under CRP nullification, business that took out a PPP loan that is forgiven has reduced net income (a loss in this example) that may be less than the net income realized without the PPP loan

Coronavirus Relief Package: Tax Law Changes

- How does this change in federal tax law impact Rhode Island taxes?
 - Rhode Island's personal income tax (PIT) and business corporation tax (BCT) systems automatically conform to federal tax law changes that affect federal Adjusted Gross Income (PIT) and federal taxable income (BCT)
 - The change to the deductibility of expenses paid with PPP loans impacts business net income which is a component of federal AGI and federal taxable income
 - Federal AGI is the starting point for Rhode Island's personal income tax
 - Federal taxable income is the starting point for Rhode Island's business corporation tax
 - Decreases in federal AGI and/or federal taxable income will reduce personal income tax and/or business corporation tax revenues

Coronavirus Relief Package: Tax Law Changes

Tax Form Linkage: Personal Income Tax

Tax Form Linkage: Business Corporation Tax

Income	7	Wages, salaries, tips, etc. Attach Form(s) W-2	7	
	8a	Taxable interest. Attach Schedule B if required	8a	
	b	Tax-exempt interest. Do not include on line 8a	8b	
	9a	Ordinary dividends. Attach Schedule B if required	9a	
	b	Qualified dividends	9b	
	10	Taxable refunds, credits, or offsets of state and local income taxes	10	
	11	Alimony received	11	
	12	Business income or (loss). Attach Schedule C or C-EZ	12	
	13	Capital gain or (loss). Attach Schedule D if required. If not required, check here <input type="checkbox"/>	13	
	14	Other gains or (losses). Attach Form 4797	14	
	15a	IRA distributions	15a	
	b	Taxable amount	15b	
	16a	Pensions and annuities	16a	
	b	Taxable amount	16b	
	17	Rental real estate, royalties, partnerships, S corporations, trusts, etc. Attach Schedule E	17	
	18	Farm income or (loss). Attach Schedule F	18	
	19	Unemployment compensation	19	
	20a	Social security benefits	20a	
	b	Taxable amount	20b	
	21	Other income. List type and amount	21	
	22	Combine the amounts in the far right column for lines 7 through 21. This is your total income	22	
Adjusted Gross Income	23	Educator expenses	23	
	24	Certain business expenses of reservists, performing artists, and fee-basis government officials. Attach Form 2106 or 2106-EZ	24	
	25	Health savings account deduction. Attach Form 8889	25	
	26	Moving expenses. Attach Form 3903	26	
	27	Deductible part of self-employment tax. Attach Schedule SE	27	
	28	Self-employed SEP, SIMPLE, and qualified plans	28	
	29	Self-employed health insurance deduction	29	
	30	Penalty on early withdrawal of savings	30	
	31a	Alimony paid. b Recipient's SSN	31a	
	32	IRA deduction	32	
	33	Student loan interest deduction	33	
	34	Tuition and fees. Attach Form 8917	34	
	35	Domestic production activities deduction. Attach Form 8803	35	
	36	Add lines 23 through 35	36	
	37	Subtract line 36 from line 22. This is your adjusted gross income	37	

RI Business Corporation Tax Starts Here

RI Personal Income Tax Starts Here

1120		U.S. Corporation Income Tax Return		OMB No. 1545-0123
Department of the Treasury Internal Revenue Service		For calendar year 2020 or tax year beginning _____, 2020, ending _____, 20		2020
Go to www.irs.gov/Form1120 for instructions and the latest information.				
A Check if:	B Name	C Employer identification number		D Date incorporated
1a Consolidated return (attach Form 991)	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>
2 Life/health consolidated return	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>
3 Personal holding co. (attach Sch. PHS)	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>
4 Schedule M-3 attached	<input type="checkbox"/>	<input type="checkbox"/>		<input type="checkbox"/>
E Check if:	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>	<input type="checkbox"/>
(1) Initial return	(2) Final return	(3) Name change	(4) Address change	
1a Gross receipts or sales	1a	1b	1c	
b Returns and allowances				
c Balance. Subtract line 1b from line 1a				
2 Cost of goods sold (attach Form 1125-A)				
3 Gross profit. Subtract line 2 from line 1c				
4 Dividends and inclusions (Schedule C, line 23)				
5 Interest				
6 Gross rents				
7 Gross royalties				
8 Capital gain net income (attach Schedule D (Form 1120))				
9 Net gain or (loss) from Form 4797, Part II, line 17 (attach Form 4797)				
10 Other income (see instructions—attach statement)				
11 Total income. Add lines 3 through 10				
12 Compensation of officers (see instructions—attach Form 1125-E)				
13 Salaries and wages (less employment credits)				
14 Repairs and maintenance				
15 Bad debts				
16 Rents				
17 Taxes and licenses				
18 Interest (see instructions)				
19 Charitable contributions				
20 Depreciation from Form 4562 not claimed on Form 1125-A or elsewhere on return (attach Form 4562)				
21 Depletion				
22 Advertising				
23 Pension, profit-sharing, etc., plans				
24 Employee benefit programs				
25 Reserved for future use				
26 Other deductions (attach statement)				
27 Total deductions. Add lines 12 through 26				
28 Taxable income before net operating loss deduction and special deductions. Subtract line 27 from line 11.				
29a Net operating loss deduction (see instructions)		29a		
b Special deductions (Schedule C, line 24)		29b		
c Add lines 29a and 29b		29c		
30 Taxable income. Subtract line 29c from line 28. See instructions				
31 Total tax (Schedule J, Part I, line 11)				

Coronavirus Relief Package: Tax Law Changes

- The timing of the change in the deductibility of expenses paid with forgiven PPP loans is such that the potential revenue impacts were not included in the November 2020 REC estimates
- The CARES Act resulted in a total of \$521.5 billion of PPP loans being issued in TY 2020
 - A total of \$1.904 *billion* of PPP loans were made to 17,875 Rhode Island businesses and non-profits
 - \$192.9 million in PPP loans were made to tax exempt non-profit entities
 - \$1.711 *billion* in PPP loans were made to for-profit taxable entities
- If all \$1.711 billion of PPP loans are forgiven and \$1.711 billion of expenses paid with these loans are deducted against other taxable income, the impact on state revenues for TY 2020 (FY 2021) would be in the tens of millions of dollars

Coronavirus Relief Package: Tax Law Changes

- The CRP also authorized a second round of PPP loans in TY 2021
 - Non-public companies with no more than 300 employees
 - Used or will use all of the proceeds of a first round PPP loan as allowed
 - Can show at least a 25% drop in gross receipts in either the first, second, or third quarter of 2020 versus the same quarter in 2019
- The total amount of second round PPP loans authorized was \$284 billion
- Based on first round PPP loans data for RI businesses, ORA projected the potential impact of second round PPP loans in TY 2021 (FY 2022)
 - ORA estimates \$1.037 billion of PPP loans will be made to Rhode Island businesses and non-profits in TY 2021
 - \$105.1 million in PPP loans will be made to tax exempt non-profits
 - \$932 million in PPP loans will be made to for-profit taxable entities

Coronavirus Relief Package: Tax Law Changes

- If all \$932 million of second round PPP loans are forgiven and \$932 million of expenses paid with these loans are deducted against other taxable income, the impact on state revenues in TY 2021 (FY 2022) would also be in the tens of millions of dollars, but < in TY 2020 (FY 2021)
- There are other federal tax law changes included in the CRP that will affect Rhode Island tax revenues. For example:
 - Increase in the “above-the-line” charitable contribution deduction for TY 2021 to \$600 for joint filers who use the federal standard deduction
 - In TY 2020, a \$300 “above the line” deduction was allowed per return
 - Reduces federal AGI which will reduce Rhode Island personal income tax revenues for TY 2021 (FY 2022)
 - Amount of revenue loss likely significantly less than for PPP loans

Revenue Trends and Projections

- The late passage of the CRP may have caused PPP loan recipients to make estimated/final payments to the state on or before December 15, 2020 that reflected current law in place at the time, thus overpaying the actual tax liability to be incurred
 - These overpayments could result in higher refunds or lower estimated/final payments than expected being realized in March to June 2021
- The 11 week extension of PEUC, including both PUA and FPUA, and the restoring of the \$300 supplemental payments should provide additional support to personal income tax withholding payments
 - Rhode Island subjects unemployment insurance payments to the income tax and requires recipients to opt out from withholding on these payments

Revenue Trends and Projections

- The direct payments to individuals of \$600 per person (stimulus checks) are structured as advanced federal income tax credits just like the CARES Act Recovery Rebates
 - These stimulus checks are not included in federal AGI and thus have no impact on Rhode Island personal income tax revenues
 - The second round of recovery rebates should continue to support sales and use tax revenues provided they are spent on taxable items
- The enacted budget reduced the lottery transfer by \$18 million, concentrated in gaming revenues. Provided no future closures of Twin River or Tiverton, this revenue reduction may be larger than the actual decline in gaming revenues providing potential upside in this source

Revenue Trends and Projections

- Grants made to businesses as part of the Restore RI program, the Hotels, Arts & Tourism (HArT) program, the RI On Pause program, and the Relief Fund for Restaurants and Bars are considered taxable income for federal and state income tax purposes
 - This tax treatment is different from that for PPP loan forgiveness and may give rise to an equity issue for those businesses that received grants from the state vs. those businesses that received PPP loans
- The CRP has numerous other tax law changes that may or may not flow through to Rhode Island
 - ORA and the Division of Taxation are currently reviewing these provisions to determine which ones impact state revenues

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Thank You