State of Rhode Island
Budget
Office
Department of Administration

# State Fiscal Note for Bill Number: 2013-H-5751

***Date of State Budget Office Approval:***

***Date Requested:*** **Friday, March 29, 2013**

***Date Due:*** **Monday, April 08, 2013**

| ***Impact on Expenditures*** | | ***Impact on Revenues*** | |
|---|---|---|---|
| FY 2013 | n/a | FY 2013 | n/a |
| FY 2014 | n/a | FY 2014 | $59,498,300 |
| FY 2015 | n/a | FY 2015 | $62,655,030 |

*Explanation by State Budget Office:*

This act would add a fourth tax bracket to the tax imposed under Rhode Island General Law Chapter 44-30 entitled "Personal Income Tax". For tax year 2012, a marginal tax rate of 3.75 percent is applied to the first $57,150 of taxable income. The next $72,750 of taxable income is taxed at a rate of 4.75 percent and taxable income amounts that exceed $129,900 are taxed at a rate of 5.99 percent.

The fourth bracket envisioned in the act would apply a marginal tax rate of 7.99 percent to the amount of taxable income that exceeds $250,000. The $250,000 threshold amount corresponds to the tax brackets that were in place for tax year 2011. Rhode Island General Law subsection 44-30-2.6(c)(3)(E) indexes the tax year 2011 tax bracket amounts for inflation.. If the $250,000 taxable income amount at which the higher tax rate takes effect in the act were indexed for inflation, the tax year 2012 taxable income amount would be $259,800. Under the act, the 5.99 percent rate would apply to taxable income amounts which have been indexed for tax year 2012, greater than $129,900 but not more than $259,800 with the 7.99 percent tax rate applying to taxable income amounts of $259,800 or more.

*Comments on Sources of Funds:*

All personal income taxes are considered to be general revenues.

*Summary of Facts and Assumptions:*

The effective date of the act is upon passage and applies to tax years beginning January 1, 2013 and thereafter.

The revenue gain figures reported in the fiscal note are based on the TY 2011 personal income tax simulation executed by the Office of Revenue Analysis (ORA). In tax year 2011, a marginal tax rate of 3.75 percent was applied to the first $55,000 of taxable income, the next $70,000 of taxable income was taxed at a rate of 4.75 percent and taxable income amounts that exceed $125,000 were taxed at a rate of 5.99 percent. The simulation applied the proposed 7.99 percent marginal tax rate to all taxable income in excess of $250,000 for resident and non resident tax returns that were filed for tax year 2011 and compared the result of this simulation to actual TY 2011 personal income tax revenues generated by the state's TY 2011 personal income tax system with a top marginal tax rate of 5.99 percent for all taxable income greater than $125,000. The result of the simulation with taxable income greater than $250,000 taxed at a marginal rate of 7.99 percent indicates that implementation of the act would increase personal income tax revenues by 5.27 percent.

Given that the provisions of the act are for tax years beginning on or after January 1,

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2013, ORA assumed that the increased revenues from the act will be realized in the fiscal year following the tax year to which the proposed change in the personal income tax applies. Thus, TY 2013 revenues are assumed to be received in FY 2014 and TY 2014 revenues are assumed to be received in FY 2015.

Applying the 5.27 percent estimated personal income tax revenue gain to the FY 2014 estimate for personal income tax revenues of $1,129,000,000 adopted at the November 2012 Revenue Estimating Conference yields an estimated personal income tax gain of $59,498,300 for FY 2014. Similarly, for FY 2015, the 5.27 percent estimated full year impact of the act's proposed personal income tax change was applied to the Budget Office's estimate for FY 2015 personal income tax collections of $1,188,900,000 to yield a projected revenue gain of $62,655,030.

The revenue estimates provided above are static estimates and do not include any behavioral responses that might be engendered from the act. As a result, these estimates should be interpreted as being the maximum revenue impacts from the passage of the act.

The Governor's FY 2014 Recommended Budget projects an ending balance of $1.4 million in FY 2014 and a deficit of $170.5 million in FY 2015. Passage of the act would increase the Governor's FY 2014 recommended ending balance and decrease the FY 2015 projected deficit.

*Summary of Fiscal Impact:*

FY 2013: Not applicable given the assumption that revenues that result from the change in the personal income tax for a given tax year are realized in the following fiscal year.

FY 2014: A maximum revenue increase of $59,498,300 is forecast based on applying the results of the Office of Revenue Analysis' TY 2011 personal income tax simulation.

FY 2015: A maximum revenue gain of $62,655,030 is forecast based on applying the results of the Office of Revenue Analysis' TY 2011 personal income tax simulation.

*Budget Office Signature:* Thomas A Mullaney

*Fiscal Advisor Signature:* Sharon Reynolds Ferland — see attached ~~ADD~~ Fiscal Advisor Comments

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**House Fiscal Advisor Comments H 5751:**

As presented, the Fiscal Note does not identify potential issues with change in tax rate after the tax year has begun including taxes owed on transactions that have already occurred. Previous years' fiscal notes have included the information quoted below:

*"It is important to note that as written, the act increases the marginal tax rate on taxpayers with taxable income amounts over $250,000 on a retroactive basis (i.e., it applies the new higher marginal tax rates to income earned in periods prior to the passage of the act). This will cause problems with the administration of the personal income tax system and likely result in legal action against the state. The act's retroactivity should be eliminated".*