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State of Rhode Island
Budget Office
Department of Administration

State Fiscal Note for Bill Number: 2019-H-5311

Date of State Budget Office Approval: **Tuesday, March 12, 2019**

Date Requested:

Date Due:

Impact on Expenditures		*Impact on Revenues*	
FY 2019	n/a	FY 2019	n/a
FY 2020	n/a	FY 2020	$(2,042,579)
FY 2021	n/a	FY 2021	$(4,153,189)

Explanation by State Budget Office:

This bill would amend Rhode Island General Laws Chapter 44-30 entitled "Personal Income Tax" by adding an allowable modification amount taken by taxpayers reducing federal Adjusted Gross Income (AGI) under Rhode Island General Law Section 44-30-12 titled "Rhode Island income of a resident individual." The modification reducing federal AGI would be equal to the amount of taxable retirement income distributed from individual retirement accounts (IRA) or 401(k) accounts that is included in federal AGI, up to a maximum of $15,000, for tax years beginning on or after January 1, 2020. To be eligible for this modification reducing federal AGI, a taxpayer must have reached the age used for calculating full or unreduced Social Security retirement benefits and have federal AGI of $80,000 or less, in 2016 dollars (for tax year 2018 the inflation adjusted amount is $83,550), for an individual filer or federal AGI of $100,000 or less, in 2016 dollars (for tax year 2018 the inflation adjusted amount is $104,450), for joint filers.

Under current law, effective for tax years beginning on or after January 1, 2017, a modification is allowed for up to $15,000 of taxable retirement income from certain pension plans and annuities under Rhode Island General Law Section 44-30-12(c)(9) titled "Rhode Island income of a resident individual Modifications reducing federal adjusted gross income" subject to the same age minimum and federal AGI limitations as noted above.

Comments on Sources of Funds:

All personal income tax revenues are general revenues.

Summary of Facts and Assumptions:

*****************REVISED 3/20/2019*********************************

The effective date of the bill is January 1, 2020, which will impact tax years beginning on or after that date. Based upon the accrual methodology employed by the Department of Administration's Office of Accounts and Controls (OAC), tax law changes that take effect in the middle of a fiscal year have a current fiscal year revenue impact equal to one-half of the succeeding fiscal year's revenue impact. The Department of Revenue's Office of Revenue Analysis (ORA) has used this accrual-based methodology to provide the budgetary revenue impacts contained in this fiscal note.

It should be noted that the bill will have no impact on FY 2019 personal income tax revenues as the bill will be effective for tax years beginning on or after January 1, 2020. The impact of the bill on FY 2020 personal income tax revenues will be

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realized through the personal income tax net accrual rather than actual revenue flows during the fiscal year as the returns filed for TY 2020 would not be received until FY 2021. The impact of the bill on FY 2021 personal income tax revenues will be realized through actual revenue flows during that fiscal year but primarily concentrated in the month of April.

It should be noted that, although this modification reducing federal AGI is provided for in Rhode Island General Law Section 44-30-12 titled "Rhode Island income of a resident individual", said modification reducing federal AGI is extended to non-resident taxpayers via subsection (c) of Rhode Island General Law Section 44-30-32 titled "Rhode Island income of a nonresident individual".

The bill explicitly allows for the inclusion of distributions from 401(k) accounts as part of the modification decreasing federal AGI. This reference is unnecessary. As the Division of Taxation has made clear in its Rhode Island Personal Income Tax Guide: Modification for Income From Pensions, 401(K) Plans, Annuities and Other Such Sources of October 3, 2017, "taxable distributions from pensions, annuities, 401(k) plans, 403(b) plans, governmental 457(b) plans, and military retirement pay count as "pension and/or annuity income" for purposes of Rhode Island's pension/annuity income modification under Rhode Island General Laws § 44-30-12." Thus, the revenue impacts estimated in this fiscal note are only for the addition of taxable distributions from individual retirement accounts to the modification reducing federal AGI contained in Rhode Island General Law § 44-30-12(c)(9).

The revenue figures reported in this fiscal note are based on ORA's TY 2016 personal income tax simulation model adjusted to reflect current tax law as of TY 2018. Under TY 2018 law, a modification reducing federal AGI is allowed for taxable retirement income, including pensions, annuities, 401(k), 403(b), and 457(b) distributions, of up to $15,000 per eligible taxpayer. The simulation used the TY 2016 personal income tax files adjusted to reflect TY 2018 law and applied the proposed modification decreasing federal AGI for taxable retirement income to include taxable IRA distributions as reported on the federal 1040 tax form for TY 2016. It should be noted that in the case of joint filers, ORA was unable to determine whether taxable retirement income was attributable to one or both taxpayers. In the case where both taxpayers were eligible for this modification based on age or where age information for one or both taxpayers was missing, ORA assumed both taxpayers were eligible to receive up to the maximum modification amount from retirement income, $30,000 in total for the proposed bill. The results of this simulation were compared to a base simulation which used the TY 2016 personal income tax files adjusted to reflect TY 2018 law without the inclusion of taxable IRA distributions in the retirement income modification. The results of the simulation incorporating the provisions of the bill indicate that implementation of the bill would decrease personal income tax revenues by 0.3086 percent.

Using the personal income tax simulation model, ORA determined that resident and nonresident TY 2016 personal income tax collections under TY 2016 law were $1,128,925,907. This amount solely represents payments made by taxpayers for that tax year. It is important to distinguish between a tax year's revenues and total personal income taxes received in a given calendar year. Total personal income tax

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payments received in a given calendar year may include tax payments that are associated with prior tax year liabilities or estimated payments for future tax year liabilities, as well as tax payments that are related to current tax year liabilities. To account for the receipt of tax payments not associated with the current tax year, ORA compared the resident and nonresident TY 2016 personal income tax revenues to total personal income tax revenues received in calendar year 2016 of $1,244,073,186 to arrive at an estimate of the ratio of total calendar year personal income tax revenues that TY 2016 payments comprise of 90.7443 percent (i.e., $1,128,925,907 / $1,244,073,186).

The ratio of TY 2016 personal income tax revenues to CY 2016 personal income tax revenues was applied to the Department of Administration, Office of Management and Budget's (OMB) FY 2021 projection of personal income tax revenues of $1,458,830,234. This projection is consistent with the FY 2020 revenue estimates adopted at the November 2018 Revenue Estimating Conference (REC). This calculation yields estimated TY 2020 personal income tax payments of $1,323,805,756 realized in FY 2021 (i.e., $1,458,830,234 * 0.907443). Applying the 0.3086 percent estimated personal income tax revenue loss from passage of the bill to the FY 2021 estimate of TY 2020 personal income tax revenues yields estimated personal income tax revenue losses of $4,085,159 in TY 2020 attributable to adding a modification decreasing federal AGI for taxable retirement income including taxable IRA distributions (i.e., $1,323,805,756 * 0.003086). The two percentages described above were also applied to OMB's projection of FY 2022 personal income tax revenues of $1,507,417,930 to yield an estimated $4,221,219 in decreased personal income tax revenue from the addition of a modification decreasing federal AGI for taxable retirement income including taxable IRA distributions up to $15,000 (i.e., 0.907443 * $1,507,417,930 * 0.003086).

Employing the Office of Accounts and Controls accrual methodology yields budgetary revenue losses from the passage of this bill for FY 2020 of $2,042,579 (i.e., 0.5 * $4,085,159) and for FY 2021 of $4,153,189 (i.e., 0.5 * $4,085,159 + 0.5 * $4,221,219).

The Governor's FY 2020 Recommended Budget projects a closing surplus of $2,948,779 in FY 2019 and $688,004 in FY 2020. Passage of this bill would have no impact on the FY 2019 closing surplus, but it would put the Governor's FY 2020 Recommended Budget out of balance and increase the projected deficit for FY 2021.

Summary of Fiscal Impact:

*****************REVISED 3/20/2019*********************************

FY 2019: Not applicable due to the implementation date of January 1, 2020.

FY 2020: A revenue loss of $2,042,579 is forecast.

FY 2021: A revenue loss of $4,153,189 is forecast.

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