



Testimony Relating to H-7127 Budget Article 5, Section 2
Pass-Through Entity Election to Pay Taxes at the Entity Level
Senate Committee on Finance
April 30, 2026
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The Economic Progress Institute **opposes** the proposal in Budget Article 5, Section 2 to **increase from 5.99% to 8.99% the taxation rate for Pass-Through Entities (PTEs)** electing to pay taxes at the entity level.

Presumably, the Governor's recommended budget increases this rate to match the new top Personal Income Tax rate for the proposed 4th tax bracket for income above \$1 million. However, this parallel move is not required, as evidenced by the fact that Massachusetts did not increase its PTE rate to match their Fair Share Amendment millionaires tax.

Briefly, this is how PTE taxation works:

- Most Rhode Island businesses – including S-Corps, Partnerships, and LLCs – are organized as PTEs.
- This means that they do not pay the higher Corporate Tax rate, because instead the taxable profits of the business are passed through to the owners, who pay taxes at the lower Personal Income Tax rates.
- Businesses have the *option* to pay these taxes at the entity level, in order to gain certain federal tax advantages without harming state tax revenue. Many, if not most, business owners do not actually do this, because overall there is not a greater additional benefit.
- When a business does this, the owners must still file taxes on their Personal Income Tax returns, but because the taxes have been paid already, the business passes through not only the income like usual, but also a 90% credit for the taxes paid by the entity.
- If an owner ends up having a larger credit than their overall tax liability, they *lose* the extra value of the credit.

Therefore, although having a PTE rate of 8.99% might be fine for business owners with over a million dollars of profits after all non-taxable business expenses, this rate would be disadvantageous for owners who are not millionaires and have a top marginal rate of 5.99%, let alone those with such low profits that their top rate is lower. It would become more likely that such small business owners would end up with unused credit. For this reason, the Economic Progress Institute urges you to **keep the PTE tax rate at 5.99%, or consider adopting a tiered structure much like the Personal Income Tax bracket system.**