



State of Rhode Island Department of Revenue

House Bill 09-H-5983

FY 2010 BUDGET

Articles 36, 37 & 38



Governor's Tax Policy Strategy Workgroup

- ❑ Created on May 21, 2008
- ❑ Mission: "Develop a tax strategy so that Rhode Island's tax structure is a competitive advantage in retaining jobs and recruiting businesses"
- ❑ Twenty-one member group consisting of accountants and attorneys who specialize in tax matters, economists, and business and labor leaders.



Why Does Rhode Island Need Tax Reform?

- According to a 2008 CNBC ranking of all 50 states on 40 different measures of competitiveness, Rhode Island finished 48th out of 50
- Rhode Island fared relatively well on the Education and Workforce metrics, ranking 17th and 18th respectively
- Rhode Island was below average at 29th, 30th, and 39th on the Quality of Life, Technology and Innovation, and Access to Capital Markets



Why Does Rhode Island Need Tax Reform?

- ❑ Where Rhode Island really came up short was on the Cost of Living, 43rd, Cost of Doing Business, 46th, Business Friendliness, 47th, and Transportation, 48th
- ❑ But Rhode Island's worst performance was on the Economy metric, where Rhode Island ranked 49th

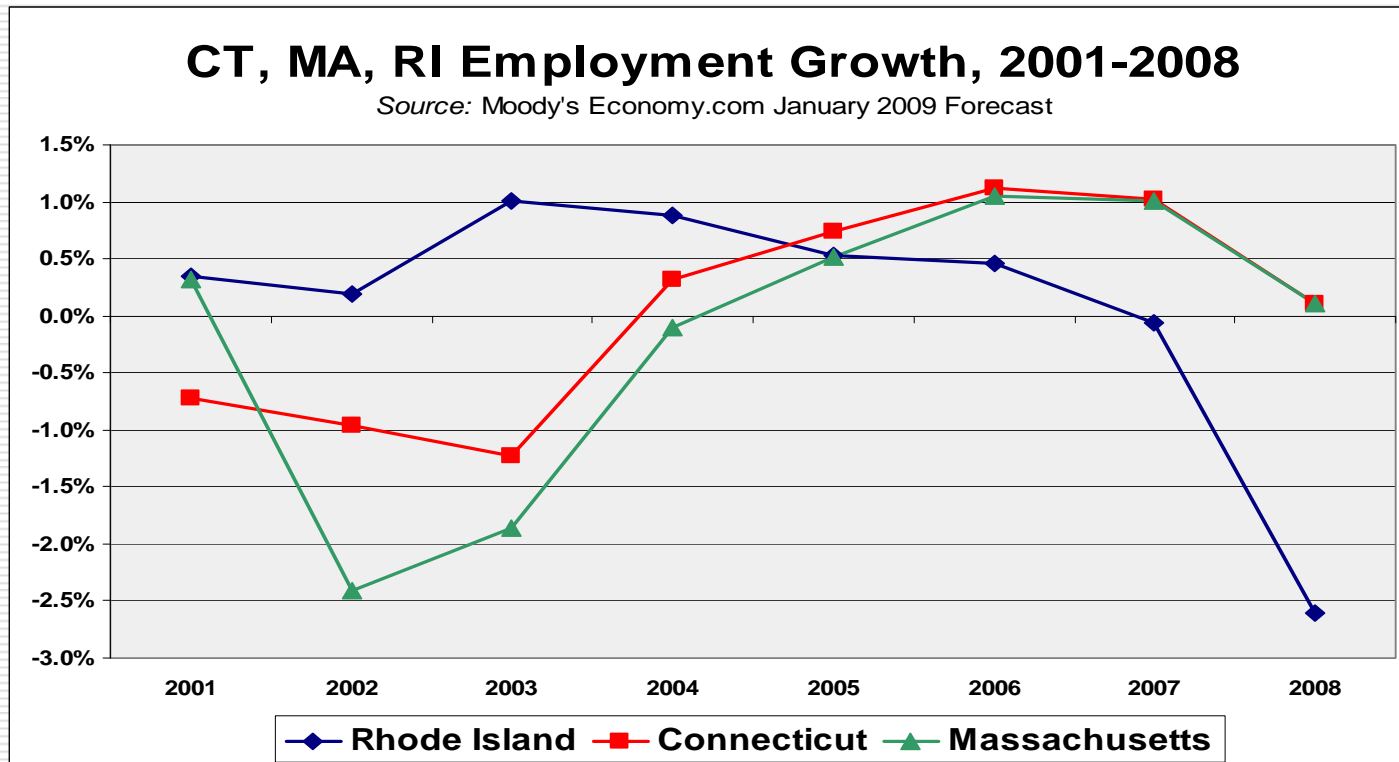


Why Does Rhode Island Need Tax Reform?

- The Economy metric considered “the basic indicators of economic health and growth.” What are these basic indicators of growth?
- At the state level, two of the most common indicators used are employment growth and personal income growth
- How does RI compare to its neighbors on these indicators?

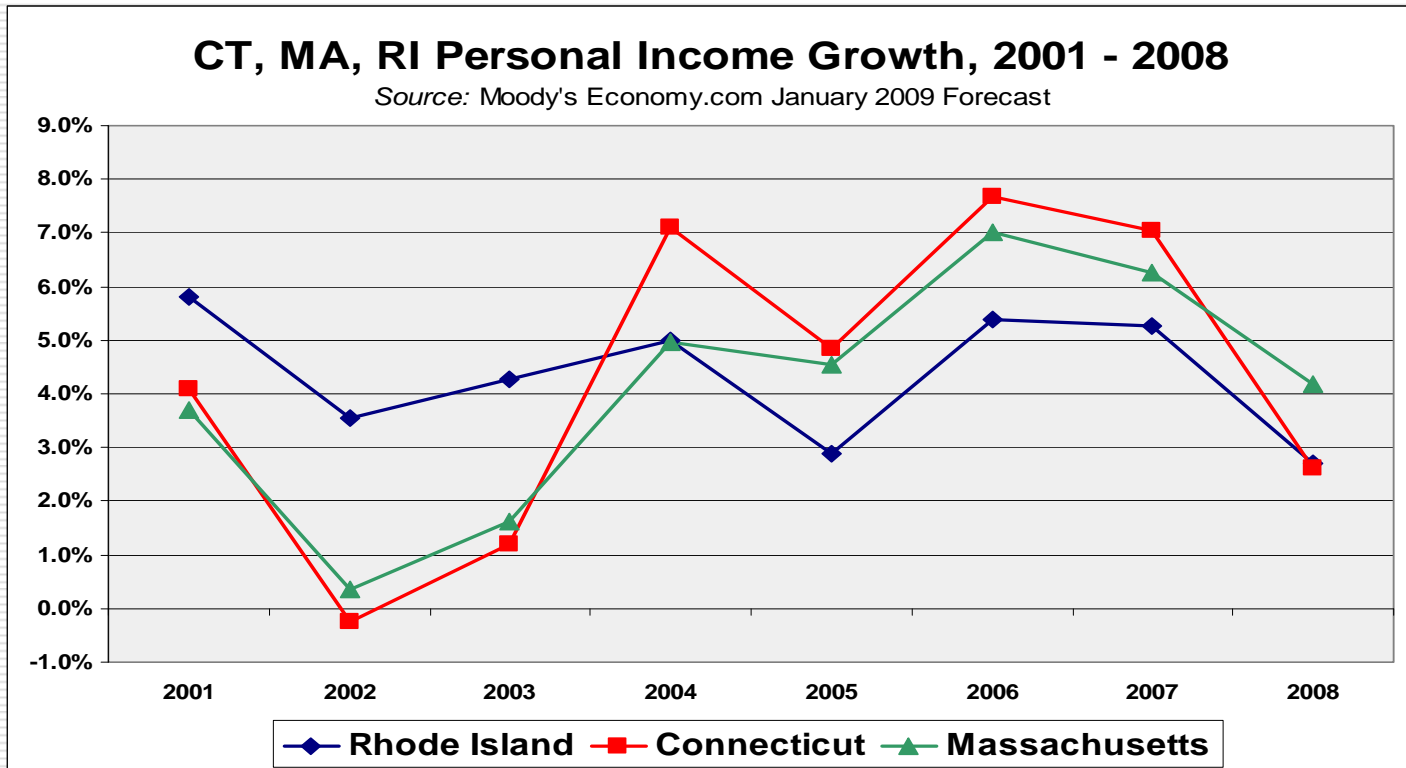


Why Does Rhode Island Need Tax Reform?





Why Does Rhode Island Need Tax Reform?





Why Does Rhode Island Need Tax Reform?

- ❑ The Governor's tax policy proposals are designed to address these basic indicators of economic health and growth
- ❑ The Governor's tax policy proposals target job creators by reducing taxes on those taxpayers that start, expand and locate businesses and jobs in the state



Why Does Rhode Island Need Business Tax Reform?

- Rhode Island ranked 46 out of 50 on the Tax Foundation's 2009 State Business Tax Climate Index

State	Score	Rank
New Jersey	3.92	50
Rhode Island	4.20	46
North Carolina	4.76	39
Connecticut	4.84	37
Massachusetts	5.03	32
Virginia	5.73	15
Delaware	6.02	10
New Hampshire	6.17	8
U.S. Average	5.00	n/a



Why Does Rhode Island Need Business Tax Reform?

- In Tax Year 2010, Rhode Island will have the highest Corporate Income Tax rate in New England

State	Corporate Income Tax Rate	
	TY 2009	TY 2010
Connecticut	7.50%	7.50%
Maine	3.50% to 8.93%	3.50% to 8.93%
Massachusetts	9.50%	8.75%
New Hampshire	8.50%	8.50%
Rhode Island	9.00%	9.00%
Vermont	6.00% to 8.50%	6.00% to 8.50%



Why Does Rhode Island Need Business Tax Reform?

- Businesses pay 45.8 percent of all state and local taxes in Rhode Island

State	Business Share of State and Local Taxes
New Hampshire	55.4%
Delaware	52.8%
Rhode Island	45.8%
Massachusetts	37.9%
New Jersey	37.2%
Virginia	36.7%
North Carolina	36.2%
Connecticut	32.3%
U.S. Average	44.1%



Why Does Rhode Island Need Business Tax Reform?

- Rhode Island's business taxes paid as a share of State GDP is 16.0 percent above the national average:

State	Percent of State GDP
Rhode Island	5.7%
New Hampshire	5.4%
New Jersey	5.0%
Massachusetts	4.2%
Virginia	3.9%
Delaware	3.8%
Connecticut	3.7%
North Carolina	3.6%
U.S. Average	4.9%



Why Does Rhode Island Need Income Tax Reform?

- At 9.9 percent, Rhode Island has one of the highest top marginal tax rates for personal income

State	Highest Marginal Tax Rate	Applicable Taxable Income
Hawaii	11.00%	> \$200,000
California	10.55%	> \$1,000,000
Rhode Island	9.90%	> \$357,700
Oregon	9.00%	> \$7,600
Iowa	8.98%	> \$63,315
New Jersey	8.97%	> \$500,000
Maine	8.50%	> \$19,450
Vermont	8.50%	> \$78,850
Massachusetts	5.30%	> \$0
Connecticut	5.00%	> \$10,000



Why Does Rhode Island Need Income Tax Reform?

- ❑ Rhode Island's personal income tax system allows 8 modifications increasing Federal AGI and 18 modifications decreasing Federal AGI
- ❑ Modifications decreasing Federal AGI include, but are not limited to, the profit or gain for writers, composers and artists, income from qualifying options, securities or investments
- ❑ These modifications result in a tax system in which similarly situated taxpayers are not treated similarly



Why Does Rhode Island Need Income Tax Reform?

- ❑ For example, consider two taxpayers who reside in Pawtucket, where one works as an artist and the other as a machinist
- ❑ Each taxpayer has Federal AGI of \$40,000 but the artist has \$10,000 of income that is eligible for exclusion from Federal AGI for Rhode Island income tax purposes
- ❑ How does this exclusion affect the relative tax burdens of each taxpayer?



Why Does Rhode Island Need Income Tax Reform?

Tax Year 2008	Machinist	Artist
Filing Status	Single	Single
Federal AGI	\$ 40,000	\$ 40,000
Modification	-	(10,000)
RI AGI	\$ 40,000	\$ 30,000
Standard Deduction	5,450	5,450
Exemption Amount	3,500	3,500
RI Taxable Income	31,050	21,050
RI Tax Liability	\$ 1,163	\$ 788
Effective Tax Rate	2.9%	2.0%

Impact of Modification Decreasing Federal AGI	
Nominal Tax Savings due to Modification	\$ (375)
Percentage Tax Savings due to Modification	-32.2%



Why Does Rhode Island Need Income Tax Reform?

- ❑ Rhode Island's personal income tax system permits the use of more than 45 credits against personal income tax owed
- ❑ Tax credits reduce income tax liability on a dollar for dollar basis
- ❑ These credits result in a tax system in which not only are similarly situated taxpayers not treated similarly but progressivity of the income tax is compromised



Why Does Rhode Island Need Income Tax Reform?

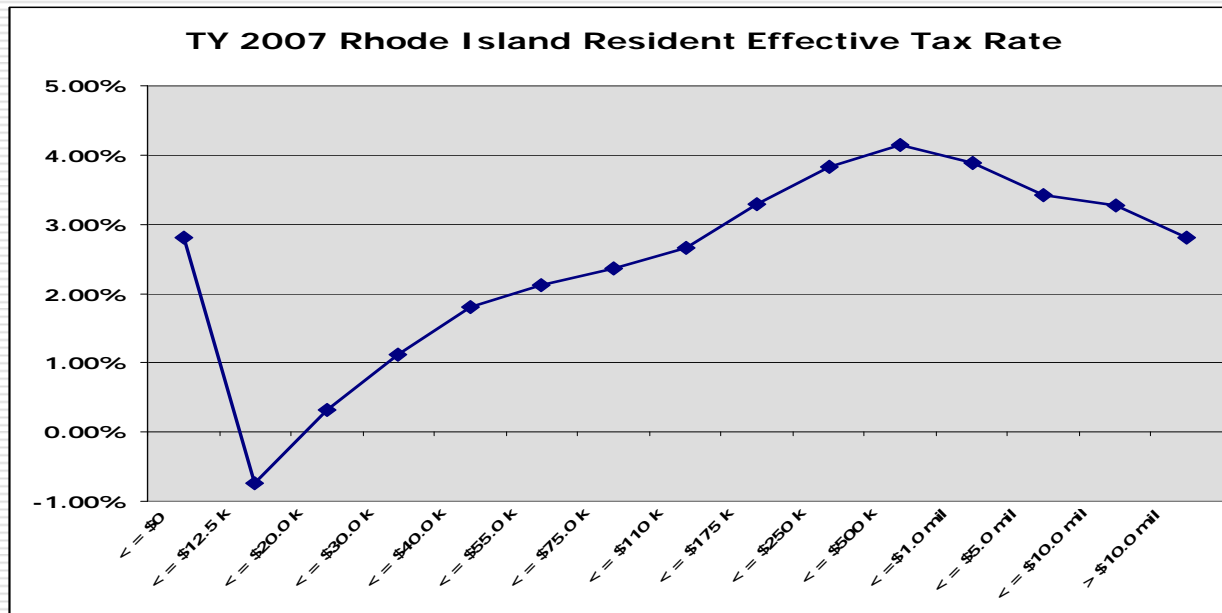
- ❑ Consider the use of Historic Preservation Investment Tax Credits

Tax Year 2008	Small Business Owner	Lawyer
Filing Status	Married Joint	Married Joint
Number of Exemptions	4	4
RI AGI	\$ 300,000	\$ 300,000
Itemized Deduction	53,045	53,045
Exemption Amount	14,000	14,000
RI Taxable Income	232,955	232,955
RI Tax Before Credits	\$ 15,708	\$ 15,708
Historic Tax Credit	\$ -	\$ 16,000
RI Tax Liability	\$ 15,708	\$ (292)
Effective Tax Rate	5.2%	-0.1%



Why Does Rhode Island Need Income Tax Reform?

- The use of tax credits has eroded the progressivity of Rhode Island's current personal income tax





Why Does Rhode Island Need Income Tax Reform?

- ❑ Rhode Island is one of only six states that gives preferential tax treatment for capital gains income

State	Highest Marginal Tax Rate	Preferential Tax Rate for Capital Gains
Hawaii	11.00%	7.25%
Rhode Island	9.90%	1.67%
Vermont	9.50%	5.70%
Arkansas	7.00%	4.90%
South Carolina	7.00%	3.92%
Wisconsin	6.75%	2.70%



Why Does Rhode Island Need Estate Tax Reform?

- ❑ Rhode Island has the lowest Estate Tax exemption amount in the country

State	Exemption Amount
Connecticut	\$2,000,000
Delaware	No Estate Tax
Massachusetts	\$1,000,000
New Hampshire	No Estate Tax
New Jersey	\$675,000
North Carolina	\$3,500,000
Rhode Island	\$675,000
Virginia	No Estate Tax



Article 36 – Estate Tax

- Article increases the Estate and Transfer Tax exemption amount from \$675,000 to \$1,000,000.
- Effective for decedents whose death occurs after December 31, 2009.



Why Increase the Estate Tax Exemption Amount?

- If Rhode Island had indexed its estate tax exemption amount for inflation in 2001 the current exemption amount would be \$150,000 higher

Tax Year	CPI-U Inflation	Rhode Island Estate Tax Exemption Amount if Indexed for Inflation
2001		\$675,000
2002	1.6%	685,800
2003	2.3%	701,573
2004	2.7%	720,516
2005	3.4%	745,013
2006	3.2%	768,854
2007	2.9%	791,151
2008	3.8%	821,214
2009	-1.1%	812,181
2010	1.7%	825,988



Article 37 – Corporate Income Tax

- Article eliminates the Corporate Income Tax over a five year period
- Replaces the corporate minimum tax with a tiered system according to corporations' net income in Tax Year 2014
- Article reduces the maximum jobs development rate reduction for eligible companies as corporate income tax rate declines



Article 37 – Corporate Income Tax

Proposed Corporate Income Tax Rate Reductions

Tax Year	Corporate Income Tax Rate	Job Development Act Maximum Rate Reduction
2009	9.00%	6.00%
2010	7.50%	4.50%
2011	6.00%	3.00%
2012	4.00%	2.00%
2013	2.00%	1.00%
2014	0.00%	n/a



Why Eliminate the Corporate Income Tax?

- In Rhode Island, firms with > 500 employees, typical C Corporations, employ 42.9 percent of the working population but comprise only 3.5 percent of businesses

Employment Size of Enterprise	Firms	Percentage of Total	Paid Employees	Percentage of Total	Annual Payroll (1,000)	Average Annual Salary
Firms with 0 to 19 employees	22,774	85.3%	91,857	20.8%	3,037,226	\$33,065
Firms with 20 to 99 employees	2,390	9.0%	88,393	20.1%	3,123,227	\$35,333
Firms with 100 to 499 employees	599	2.2%	71,416	16.2%	2,571,864	\$36,012
Firms with 500 employees or more	928	3.5%	189,131	42.9%	8,340,505	\$44,099
All firms	26,691		440,797		17,072,822	



Article 38 – Personal Income Tax

- Article reduces the number of income tax brackets from five to four with lower marginal rates

Taxable Income Bracket	Tax Rate
\$0 to \$54,999	3.50%
\$55,000 to \$109,999	4.00%
\$110,000 to \$174,999	4.50%
\$175,000 and more	5.50%



Article 38 – Personal Income Tax

- ❑ Article eliminates itemized deductions in favor of large combined standard deduction and exemption amount

Filing Status	Standard Deduction Amount
Married Joint / Widow(er)	\$15,000
Single / Married Separate	\$7,500
Head of Household	\$11,250

Exemption Type	Exemption Amount
Personal	\$2,500
Dependent	\$2,500



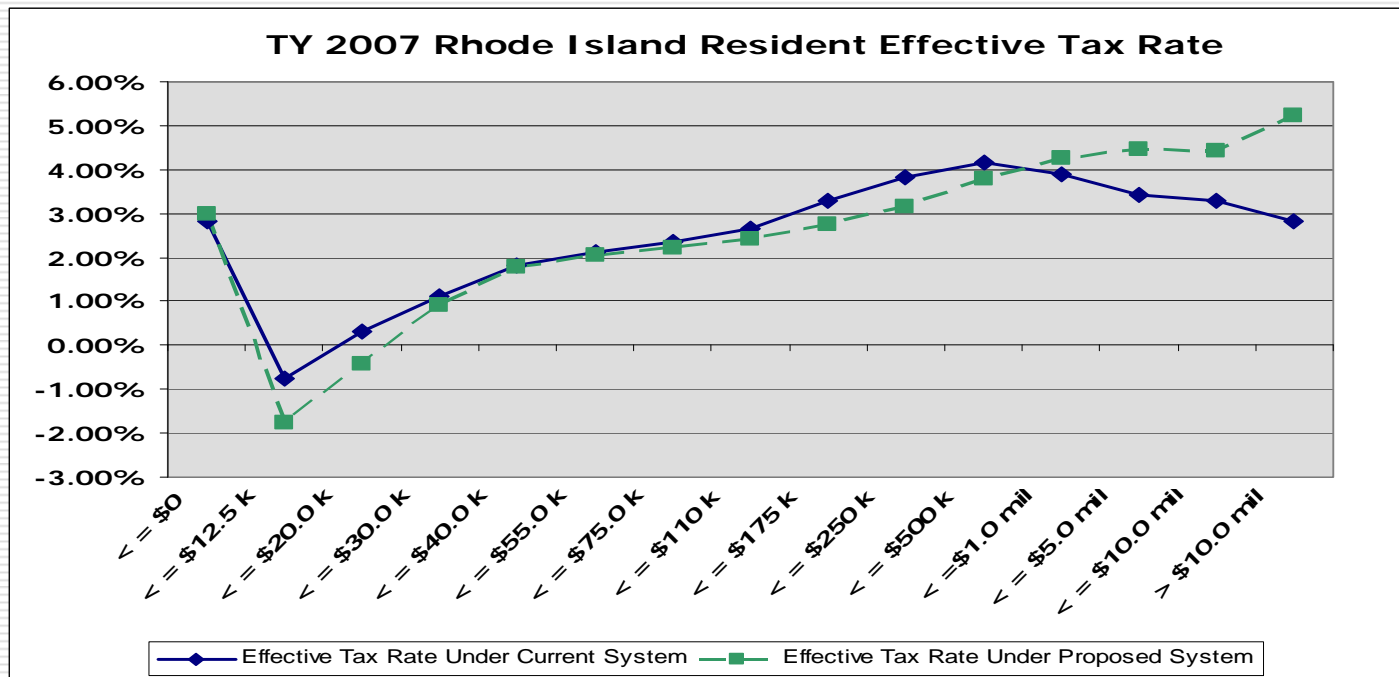
Article 38 – Personal Income Tax

- Article 38 allows for five credits against tax: a fully refundable Earned Income Tax Credit, a Property Tax Relief Credit, a Lead Paint Abatement Credit, a Credit for Contributions to Scholarship Organizations, and a Credit for Income Taxes Paid to Other States.
- Article 38 also eliminates the preferential tax treatment of capital gains. The proposed system taxes capital gains at ordinary income tax rates



Why Reform Rhode Island's Personal Income Tax?

- Proposed income tax system maintains progressivity across AGI classes





The Impact of Personal Income Tax Reform

AGI Ranges	TY 2007 Resident Filers Only, Assumed Flat Tax Rate of 5.5 Percent					
	All Taxpayers		Taxpayers w/ Itemized Deductions		Taxpayers w/ Capital Gains Income	
	Returns with a Tax Decrease	Returns with a Tax Increase	Returns with a Tax Decrease	Returns with a Tax Increase	Returns with a Tax Decrease	Returns with a Tax Increase
\$12,500 and Under	55,592	1,939	3,961	1,839	2,000	209
\$12,501 to \$20,000	45,572	4,467	6,959	4,034	849	782
\$20,001 to \$30,000	46,418	12,601	8,766	8,063	1,234	1,110
\$30,001 to \$40,000	33,019	13,794	6,857	11,131	1,239	1,237
\$40,001 to \$55,000	33,418	18,059	11,275	17,307	2,174	2,091
\$55,001 to \$75,000	31,811	19,441	18,554	19,149	3,315	2,586
\$75,001 to \$110,000	35,076	19,148	28,840	19,051	5,506	3,358
\$110,001 to \$175,000	28,340	5,281	27,420	5,236	6,712	1,900
\$175,001 to \$250,000	8,114	1,174	8,053	1,148	2,978	784
\$250,001 to \$500,000	5,036	1,058	5,015	1,039	2,482	766
\$500,001 to \$1,000,000	1,242	464	1,237	453	725	382
\$1,000,001 to \$5,000,000	504	332	501	328	329	293
\$5,000,000 and up	49	55	49	55	39	52
Totals	324,191	97,813	127,487	88,833	29,582	15,550
Ratio of Decrease to Increase		3.31		1.44		1.90



The Impact of Personal Income Tax Reform

AGI Ranges	TY 2007 Resident Filers Only, Assumed Flat Tax Rate of 5.5 Percent					
	All Taxpayers		Taxpayers No Itemized Deductions		Taxpayers No Capital Gains Income	
	Returns with a Tax	Returns with a Tax	Returns with a Tax	Returns with a Tax	Returns with a Tax	Returns with a Tax
	Decrease	Increase	Decrease	Increase	Decrease	Increase
\$12,500 and Under	55,592	1,939	51,631	100	53,592	1,730
\$12,501 to \$20,000	45,572	4,467	38,613	433	44,723	3,685
\$20,001 to \$30,000	46,418	12,601	37,652	4,538	45,184	11,491
\$30,001 to \$40,000	33,019	13,794	26,162	2,663	31,780	12,557
\$40,001 to \$55,000	33,418	18,059	22,143	752	31,244	15,968
\$55,001 to \$75,000	31,811	19,441	13,257	292	28,496	16,855
\$75,001 to \$110,000	35,076	19,148	6,236	97	29,570	15,790
\$110,001 to \$175,000	28,340	5,281	920	45	21,628	3,381
\$175,001 to \$250,000	8,114	1,174	61	26	5,136	390
\$250,000 and up	6,831	1,909	29	34	3,256	416
Totals	324,191	97,813	196,704	8,980	294,609	82,263
Ratio of Decrease to Increase		3.31		21.90		3.58



State of Rhode Island Department of Revenue

Thank You