

Few Winners and Many Losers in Rhode Island Tax Reform

The budget passed by the House Finance committee made three significant tax policy changes that will impact the income of tens of thousands of Rhode Islanders.

The estate tax, earned income tax credit, and property tax relief program were all dramatically altered in the budget.

The clear winners are a small number of wealthy taxpayers whose estates will pay less in taxes and in many cases, nothing at all starting next year. The clear losers are tens of thousands of low- and modest-income Rhode Islanders who will pay more in taxes next year. Unemployed homeowners and renters are among the biggest losers, because they will no longer qualify for property tax assistance and are not eligible for the earned income tax credit. Many of the lowest-wage workers will also be negatively impacted by the loss of the property tax refund, even with an eventual boost in the EITC.

The shift in state resources from low- and modest-income taxpayers to high-income taxpayers is significant. The state will give up \$9.4 million to provide large tax breaks to just over 200 estates that owe taxes. Estates worth less than \$1.5 million will pay no estate tax; estates above that amount will get a tax credit worth \$64,400, reducing their estate tax bill by that amount. The cost of the tax break doubles to \$18 million by 2016.

At the same time, in the coming year, the state will save a net of \$3.9 million by modifying the EITC and eliminating the property tax relief circuit breaker program for low- and modest-income Rhode Islanders who are not elderly or disabled. By Fiscal Year 2016, the state will spend more on the reformed EITC, but total state spending on tax assistance for low- and modest-income taxpayers will just get back to what it is today.

For some low-income taxpayers who receive both the state earned income tax credit and property tax refund, an increase in the EITC may offset the loss of the property tax refund. But others will lose out completely. For example, someone who is unemployed and qualifies for the property tax refund to help offset their property taxes will no longer receive any tax benefit. Modest-income taxpayers who qualify for the EITC will also be likely to pay more income tax as the credit is lowered from 25 percent to 10 percent.

Estate tax changes

The state currently taxes the full value of estates worth more than \$921,655. The estate tax generates between 28 million and 46 million a year.¹ The budget establishes a new \$64,400 estate tax credit that basically exempts estates worth \$1.5 million or less from the estate tax, while providing a tax cut equal to the credit for all other estates. Just over 200 estates paid taxes in 2013, one-third of which belonged to out-of-state residents.

Budget impact FY15: \$9.4 million revenue loss
 Budget impact FY16: \$18 million revenue loss

VALUE OF ESTATE	ESTATE TAX OWED TODAY	TAXES WITH NEW CREDIT	PERCENT BREAK	EFFECTIVE TAX RATE
\$1 million	\$30,555	\$0	100%	0%
\$1.5 million	\$64,400	\$0	100%	0%
\$2 million	\$99,600	\$35,200	65%	1.8%
\$5 million	\$391,600	\$327,200	16%	6.5%

Earned Income Tax Credit

Today, the state’s earned income tax credit is equal to 25 percent of the federal credit, but it is only partially refundable. Just 15 percent of the 25 percent credit is refundable – meaning the credit is worth 3.75 percent of the federal credit for working families and individuals with very low income tax liability. Just over 83,000 taxpayers claimed the EITC in 2012, totaling close to \$16 million. For those who received a refund, the average was about \$82 in tax year 2012.²

Lawmakers are reforming the credit by reducing it to equal 10 percent of the federal EITC and making it fully refundable. This change is likely to result in larger refunds for some of the lowest-wage workers in our state, and some workers who did not receive a refund will now get to keep more of what they earn come tax time. Still, many modest-income EITC filers with relatively higher income tax liability will pay more in taxes as the credit is reduced.

¹ May 2014 Revenue Estimating Conference

² 2012 Statistics of Income. RI Division of Taxation, 2014.

Budget impact FY15: \$4.3 million revenue loss

Budget impact FY16: \$8.8 million revenue loss

Property Tax Relief Circuit Breaker

Rhode Island provides a refund for a portion of property taxes paid by low-income homeowners and renters who have income of less than \$30,000. The refund is available if property taxes exceed between 3 and 6 percent of household income. Close to 42,000 homeowners and renters received a refund in 2012, totaling \$11.3 million.³ The average refund was \$271 in tax year 2012.⁴

The budget passed by the House Finance Committee eliminates this assistance to anyone who is not elderly or disabled.

Budget impact FY15: \$8.2 million revenue gain

Budget impact FY16: \$8.2 million revenue gain ⁵

³ 2012 *Statistics of Income*. RI Division of Taxation, 2014.

⁴ 2012 *Statistics of Income*. RI Division of Taxation, 2014.

⁵ No estimate was available for FY16 so the same estimated state savings was assumed as that for FY15.