Testimony Regarding Governor's Budget Amendment 14, Relating to Taxes (Article 8)
House Finance Committee
September 23, 2020

The Economic Progress Institute supports saving the state approximately $29 million in much needed revenue by approving Budget Amendment 14 to decouple from a misguided tax provision of the Coronavirus Aid, Relief, and Economic Security (CARES) Act.

Section 2304 of the CARES Act essentially eliminates any limit on pass-through businesses using operating losses as deductions to reduce tax liability. Under the Tax Cut and Jobs Act (TCJA) of 2017, such deductions were limited to $500,000 per year. This meant, for example, that an investor or business owner who had $5 million in taxable income and a business loss on paper of $5 million would still need to pay taxes on $4.5 million in that tax year; such a person would still be able to carry forward the losses as excess business losses to claim against tax liability in future years. With the change provided by the CARES Act, the individual can zero out tax liability and avoid paying approximately $1.7 million in taxes.¹

Ostensibly, this provision was intended to keep cash in the hands of business owners struggling against the current economic downturn. However, the provision appears mostly to benefit those who need the relief least. Some tax losses do not correspond to economic losses; businesses can deduct for rent payments and depreciating property having nothing to do with loss of income due to COVID-19. It even allows applying the deduction retroactively to tax years 2018 and 2019, before COVID-19 made any impact on businesses.

The Joint Committee on Taxation of the U.S. Congress concluded that this one provision will result in a federal revenue loss of $86 billion and that $70.3 billion (more than 80%) of these tax benefits will accrue to 43,000 filers with income of $1 million or more each.² The federal law is already in place, but the state can avoid increasing the benefit by $29 million more in Rhode Island, at a loss to the General Revenue account, just when we need such funds to prevent cutting valuable jobs and services.

Unless there is a proactive decision to do otherwise, Rhode Island’s tax code automatically conforms to the federal tax code and any changes to it. It would therefore be wise for Rhode Island to decouple from this particular provision, as have a number of other states, including North Carolina, New York, Georgia, and Colorado. Facing the economic crisis and revenue shortfall created by the coronavirus pandemic, now is the time for Rhode Island’s government to preserve its vital sources of revenue.

² Congress of the United States, Joint Committee on Taxation, Letter to the Honorable Sheldon Whitehouse and the Honorable Lloyd Doggett on “the distributional effects of the temporary suspension of the limitation on excess business losses,” April 9, 2020.