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Tax changes take effect on Thursday, January 1

Starting January 1, 2015, Rhode Island's 9 percent corporate income tax rate will drop to 7 percent. In addition, the franchise tax will be officially repealed, mandatory combined reporting will take effect, and businesses treated as C corporations will see changes in their apportionment calculations. These and other changes are the result of legislation approved by the General Assembly and signed into law by Governor Lincoln D. Chafee on June 19, 2014.

"These are the most significant changes to Rhode Island's corporate income tax regime since 1947," said Rhode Island Tax Administrator David M. Sullivan. "The Division of Taxation has held numerous outreach sessions with taxpayers and tax practitioners throughout the state to spread the word and to help ensure that everyone is aware of these changes. But now that the new year is near, we want to take this opportunity to remind taxpayers and practitioners about the changes and their effective date," Sullivan said.

Also new for 2015 is a change in the Rhode Island estate tax. "This change will mean that fewer estates will end up being taxed. That, in turn, will make more money available to heirs and other beneficiaries," Sullivan added.

SUMMARY OF CORPORATE TAX CHANGES

■ **Tax Rate:** The corporate income tax rate under Rhode Island General Laws (RIGL) § 44-11-2 will be 7 percent for tax years beginning on or after January 1, 2015, down from the 9 percent for 2014.

■ **Franchise Tax:** For 2014, the franchise tax is generally \$2.50 per \$10,000 of a corporation's authorized capital stock. However, for tax years beginning on or after January 1, 2015, the franchise tax is repealed.

■ **Combined Reporting:** For tax year 2014, corporations subject to Rhode Island's corporate income tax file separate returns, as separate entities. However, for tax years beginning on or after January 1, 2015, Rhode Island has adopted combined reporting for corporate income tax purposes. As a result, a business which is treated as a C corporation – and which is part of a combined group engaged in a single business enterprise (a "unitary" business) – must file a

combined report with Rhode Island. Thus, a corporation will generally have to treat all of its affiliates as if they were a single company, and combine all of their taxable income in a single pool. A formula will be used to apportion combined income to Rhode Island for tax purposes.

■ **Estimated Tax:** For tax years beginning on or after January 1, 2015, Rhode Island will apply special rules regarding payments of estimated tax for any taxpayer required to file a combined report. To meet “safe harbor” provisions, such taxpayers will have to compute estimated payments for that tax year as follows:

- The installments must equal 100 percent of the tax due for the prior year plus any additional tax that is due to the combined reporting provisions; or
- The installments must equal 100 percent of the current year tax liability.

■ **Apportionment:** For tax years beginning on or after January 1, 2015, business that are treated as C corporations and that are or will be taxed under Rhode Island General Laws Chapter 44-11 will use a single factor – sales (total receipts) – for apportionment purposes, instead of the three-factor apportionment formula, which includes sales, payroll, and property. (Entities treated as pass-through entities for federal tax purposes will continue to use three-factor apportionment.)

■ **Sourcing:** For tax years beginning on or after January 1, 2015, businesses that are treated as C corporations and that are, or will be, taxed under RIGL Chapter 44-11 will use a different method regarding how to treat the sale of services for purposes of corporate income tax apportionment. For 2014, when a corporation calculates the sales factor for apportionment purposes, it assigns the sale of its services to the state in which the income-producing activity was actually performed – known as the cost-of-performance method. If the corporation performs activity in multiple states, the corporation assigns the sale to the state in which the corporation performed a greater proportion of the activity than in any other state – based on the cost of performance. However, for tax years beginning on or after January 1, 2015, Rhode Island will use a market-based sourcing approach, which says that receipts from transactions (other than sales of tangible personal property) are sourced to the market state – that is, the state where the recipient of the service receives benefit from the service.

■ **Subchapter S:** For tax years beginning on or after January 1, 2015, the franchise tax is repealed. As a consequence, subchapter S corporations will be subject to the annual minimum tax under the corporate income tax statute instead of under the franchise tax statute. (As a practical matter, most S corps will see no change: They will continue to pay the annual minimum tax of \$500. Some S corps under the old system ended up paying more than the minimum tax because of franchise tax provisions. For tax years beginning on or after January 1, 2015, those S corps will pay only the \$500 minimum.)

ESTATE TAX

For decedents dying on or after January 1, 2015, a \$64,400 Rhode Island credit will be applied to the estate tax. This will have the effect of shielding up to \$1.5 million from Rhode Island’s estate tax. Thus, in effect, Rhode Island’s estate tax “threshold” – which is \$921,655 for decedents dying in 2014 – will be \$1.5 million for decedents dying in 2015.

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