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Only a well-to-do few file flat-tax returns in R.I.

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PROVIDENCE — Rhode Island's flat-tax system emerged three years ago amid a summer of camaraderie at the State House.

The housing market was just about at its peak. Rhode Island's seasonally adjusted unemployment rate stood at 5.1 percent. And Democrats and Republicans joined hands to distribute a basketful of tax breaks.

What attracted the most attention was a new flat-tax option for calculating one's Rhode Island individual income tax.

House Speaker William J. Murphy and Joseph A. Montalbano, then Senate president, wrote at the time that the option would make Rhode Island more competitive with neighboring states.

And the Wall Street Journal, in a widely quoted editorial, hailed the news, saying, "The very blue state of Rhode Island adopted one of the most sweeping pro-growth tax reforms in any state in recent years."

Why the big deal? If you use the regular system to calculate your Rhode Island individual income tax, you generally may claim a variety of deductions, exemptions and credits — as well as favorable treatment of your capital gains. But you face tax rates as high as 9.9 percent.

If you use the flat-tax system, you generally cannot claim deductions, exemptions and credits, and you do not receive favorable capital-gains treatment. But you do get to use a single, flat tax rate — initially 8 percent, now 6.5 percent and scheduled to drop to 5.5 percent for 2011 and later years.

Most Rhode Island taxpayers have low or middle incomes. As a result, their Rhode Island tax rate is typically 3.75 percent.

But for higher-income taxpayers, a portion of their taxable income may be taxed at 7 percent, 7.75 percent, 9 percent, or even 9.9 percent, depending on their circumstances.

The overwhelming majority of taxpayers do not use the flat tax when figuring their Rhode Island tax; they instead use the regular system, according to figures compiled by the state Division of Taxation for 2007, the latest available.

Out of 501,531 resident returns, only 838 used the flat tax.

The flat-tax option is appealing mainly to certain higher-income taxpayers who would otherwise face higher tax rates under the regular system, said Patricia A. Thompson, former president of the Rhode Island Society of Certified Public Accountants.

For example, of the 838 returns that employed the flat-tax system for 2007, 719 — about 86 percent — showed adjusted gross income of \$200,000 or more.

But the impact will be greater when the flat-tax rate drops in future years, making it more attractive to more taxpayers and bringing Rhode Island's individual income tax system more in line with those of its neighboring states. (For 2008, for example, the flat tax rate was generally 5.3 in Massachusetts, 5 percent in Connecticut.)

Business-backed groups generally back the flat tax. Laurie White, president of the Greater Providence Chamber of Commerce, said it helps attract and retain businesses and stimulate job creation. "Private-sector job growth is the only real solution. ... You're not going to be able to tax your way out of" the current recession and Rhode Island's high unemployment rate, she said.

Opponents say that the flat-tax system should either be frozen or repealed, especially with the state facing a \$590-million budget deficit for the fiscal year that begins July 1.

Kate Brewster, executive director of The Poverty Institute, at the Rhode Island College School of Social Work, which analyzes tax and budget policies on behalf of low-income people, favors repealing the flat tax, saying it is "a very expensive tax policy that was enacted based on the fallacy that cutting income taxes for high-income taxpayers would attract and retain individuals capable of creating jobs."

Mark Higgins, dean of the University of Rhode Island's College of Business Administration, said that [Governor Carcieri](#)'s tax-reform panel earlier this year recommended elimination of the flat tax, but only as part of a proposed sweeping reform of the state's individual income-tax system that included lowering the state's top tax rate to 5.5 percent.

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