Rhode Island Department of Revenue
Division of Taxation

Tax Administrator's Report: Impact of Corporate Tax Changes

An analysis of the effect of reforms enacted in 2014, including corporate tax rate reduction, mandatory unitary combined reporting, single-sales-factor apportionment, and market-based sourcing

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The Honorable Marvin L. Abney
Chair, Committee on Finance
Rhode Island House of Representatives

The Honorable William J. Conley, Jr.
Chair, Committee on Finance
Rhode Island Senate

Sharon Reynolds Ferland
Fiscal Advisor
Rhode Island House of Representatives

Stephen Whitney
Fiscal Advisor
Rhode Island Senate

I am submitting this report to you in fulfillment of the requirements set forth in legislation approved by the General Assembly and signed into law by then-Governor Lincoln D. Chafee in June 2014.[1]

The terms of that legislation, codified at Rhode Island General Laws § 44-11-4.1(h), require that I report to you – on or before March 15, 2018 – on the policy and fiscal ramifications of the changes enacted to Rhode Island's business corporation tax statutes in 2014.

You directed the Division of Taxation to analyze actual tax filings for a two-year period and report on the effect of the most sweeping changes to Rhode Island's corporate tax regime since 1947. Those key changes included a 22 percent reduction in the corporate tax rate, and the establishment of mandatory unitary combined reporting, single-sales-factor apportionment, and market-based sourcing.

It is my hope that the information in this report fulfills the requirements that you set forth. Please let me know if you have any questions or concerns.

Sincerely yours,

Neena S. Savage
Rhode Island Tax Administrator

[1] Rhode Island Public Law 2014, ch. 145, art. 12, § 16

The tax administrator shall on or before March 15, 2018, based upon the actual tax filings of companies under this act for a two year period, submit a report to the chairperson of the house finance committee and the senate finance committee and the house fiscal advisor and the senate fiscal advisor analyzing the policy and fiscal ramifications of the changes enacted to business corporations tax statutes, as enacted in budget article 12 of the Fiscal Year 2015 appropriations act. The report shall include but not be limited to the impact upon categories of business, size of business and similar information as contained in Rhode Island General Laws 44-11-45, which required the original report.

-- Rhode Island General Laws § 44-11-4.1(h)

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EXECUTIVE SUMMARY: AT A GLANCE

Rhode Island's corporate income tax regime was changed as a result of legislation that was enacted in 2014 and that took effect for tax years beginning on or after January 1, 2015. For purposes of this report, there were four key changes:

- The tax rate was reduced from 9 percent to 7 percent.
- The separate-entity reporting method was changed to combined reporting.
- Three-factor apportionment was replaced by single-sales-factor apportionment.
- Cost-of-performance sourcing gave way to market-based sourcing.

✓ Overall impact

The Division of Taxation estimates that, as a result of those four key changes, unitary groups filing combined returns, in the aggregate and on net, had a $26.8 million reduction (that is, a 30 percent reduction) in their Rhode Island tax due, compared with what their tax due would have been under the old law. ("Old law" means Rhode Island corporate tax law for 2014. "New law" means Rhode Island corporate tax law for tax years beginning on or after January 1, 2015.)

✓ Overall impact by key change

Of the four key changes to the law, the switch to combined reporting and to market-based sourcing resulted, in the aggregate, in an increase in tax due. However, the reduction in the corporate tax rate, and the switch from three-factor apportionment to single-sales-factor apportionment, resulted, in the aggregate, in a decrease in tax due.

Furthermore, the increase in tax due resulting from the change to combined reporting and to market-based sourcing was more than offset by the reduction in tax due resulting from the lowering of the corporate tax rate and the switch to single-sales-factor apportionment. (To view this information in perspective, please see the "Frame of Reference" note in Section 5 of this report.)

✓ Impact on small businesses, large businesses

The Division found that most businesses, in the aggregate, saw no change in their tax due as a consequence of the new corporate tax law. That was true for small businesses and large businesses. A comparatively small portion of large businesses, and an even smaller portion of small businesses, saw either an increase or a decrease in their tax due.

✓ Impact: Out-of-state vs. Rhode Island corporations

Out-of-state corporations, in the aggregate, ended up with a 59 percent increase in tax due as a result of the new law – an increase of approximately $20.4 million. Rhode Island corporations, in the aggregate, ended up with an 87 percent decrease in tax due as a result of the new law – a decrease of approximately $47.2 million. In dollar terms, the decrease in tax due for Rhode Island corporations more than offset the increase in tax due for out-of-state corporations. (Continued on next page)

EXECUTIVE SUMMARY: AT A GLANCE (CONTINUED FROM PREVIOUS PAGE)

✓ **Shift in tax burden**

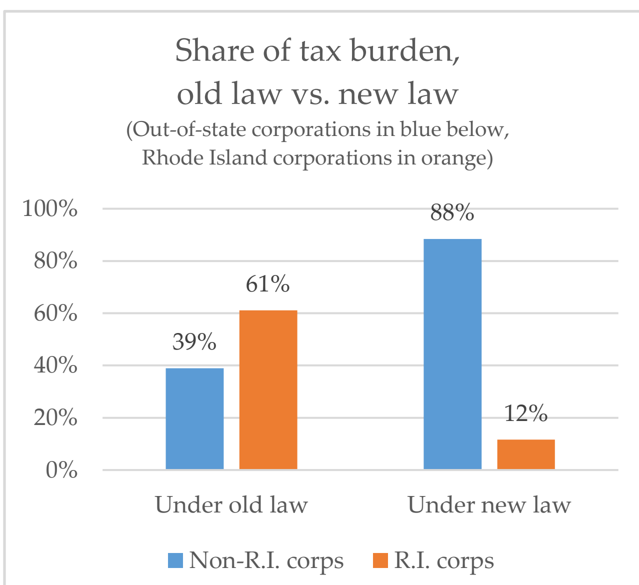
The change from the old law to the new law shifted the overall burden of tax due: Out-of-state corporations, in the aggregate, ended up with a significantly greater share of the tax burden, while Rhode Island corporations, in the aggregate, ended up with a significantly reduced share of the tax burden.

For out-of-state corporations, the tax burden more than doubled: from 38.9 percent under the old law to 88.4 percent under the new law. For Rhode Island corporations, the tax burden dropped, from 61.1 percent of the burden under the old law to 11.6 percent under the new law. (Please see chart below.)

✓ **Impact: Out-of-state vs. Rhode Island corps by key tax law change**

Rhode Island corporations, in the aggregate, saw a reduction in tax due as a result of two of the four key changes in corporate tax policy: the lowering of the tax rate, and the change in the apportionment formula. Rhode Island corporations, on average, saw a comparatively modest increase in tax due as a result of the change in the sourcing method and the switch to combined reporting.

Out-of-state corporations, in the aggregate, also saw a reduction in tax due from the lowering of the tax rate and the change in the apportionment formula. Out-of-state corporations, in the aggregate, saw an increase in their tax burden due to both the change in the sourcing method and the switch to combined reporting. (To view this information in perspective, please see the "Frame of Reference" note in Section 9 of this report.)



Executive Summary

On June 30, 2011, legislation approved by the Rhode Island General Assembly and signed into law by then-Governor Lincoln D. Chafee directed the Rhode Island Division of Taxation to study the potential impact on certain C corporations of changing from single-entity reporting to mandatory unitary combined reporting.

At the time, a C corporation taxed under Rhode Island General Laws Chapter 44-11 ("Business Corporation Tax") generally filed its annual corporate income tax return with the Rhode Island Division of Taxation as a single entity – a separate entity – taking into account only its own income.[2]

That was the case even if the corporation was part of a broader group of corporations, under common ownership, that were together engaged in a common business enterprise – a "unitary business."

Under combined reporting, a C corporation would report on its Rhode Island return not only its own income, but also the combined income of the other corporations, or affiliates, that were under common ownership and part of a unitary business.

In other words, a C corporation would treat all of its affiliates, including those in other states, as if they were one, single company, and combine all of their taxable income in a single pool. The combined group would then use a formula to apportion the amount of the combined income to Rhode Island for tax purposes.

Pro forma reporting

To determine how combined reporting might work in Rhode Island – and, in particular, what the tax impact might be on corporations and what the revenue impact might be on the State – the 2011 legislation as enacted required each C corporation that was part of a unitary business under common ownership to file a *pro forma* report for the combined group to include the combined income of the unitary group. In other words, C corporations were asked to calculate their Rhode Island corporate tax liability as if combined reporting was in effect.

As part of that effort, C corporations subject to *pro forma* combined reporting were required by statute to calculate their Rhode Island corporate income tax using two separate apportionment formulas: the standard formula under then-current law, which relied on three factors – sales, property, and payroll, and a different formula, which relied solely on sales – known as single-sales-factor apportionment, disregarding the property and payroll factors.

The 2011 legislation directed the Division of Taxation to study the impact of combined reporting over two tax years: 2011 and 2012. In summary, the Division found that, had Rhode Island adopted

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[2] Some filed consolidated returns, as described elsewhere in this report.

combined reporting for tax years 2011 and 2012, corporations subject to combined reporting, using the standard three-factor apportionment formula, would have had to pay, in the aggregate, more in Rhode Island corporate income tax, and the State would have gained more in revenue.

The Division also found that, had Rhode Island required such corporations to use the single factor of sales in their apportionment calculation under combined reporting, corporations would have had to pay, in the aggregate, still more in Rhode Island corporate income tax, and the State would have gained still more in revenue.

(It is important to note that the *pro forma* returns were required to be submitted under the assumption that the tax rate itself was unchanged (at 9 percent), and that the sourcing method for the sales factor – the cost-of-performance method – was unchanged.)

The Division of Taxation incorporated the results of its study of *pro forma* combined reporting into a report, which the Division delivered by the statutory deadline of March 15, 2014.

Changes as enacted

With the results of the Division of Taxation study on *pro forma* combined reporting in hand, the General Assembly in 2014 held a series of hearings on a proposed budget for the 2015 fiscal year.

The bill which emerged, and which was ultimately enacted, included a far-reaching package of changes to the corporate tax structure. The package included, but was not limited to, the following key features for tax years beginning on or after January 1, 2015:

- Mandatory combined reporting
- Single-sales factor apportionment
- Market-based sourcing
- A reduction in the corporate tax rate
- Repeal of the franchise tax

That legislation also required the Division of Taxation to review returns filed under the newly enacted corporate tax structure and submit a report analyzing the policy and fiscal ramifications of the corporate tax changes.

The Division was required to file the report by the statutory deadline of March 15, 2018. What follows is a summary.

Overall impact

The Division of Taxation examined the data for tax year 2015 for all combined returns. In reviewing these returns (unaudited), the Division focused on the four major changes in Rhode Island's corporate tax regime that were enacted in calendar year 2014 and that took effect for tax years beginning on or after January 1, 2015:

- The tax rate reduction (to 7 percent);
- The change in reporting method (to combined reporting);
- The change in the apportionment formula (to a single factor: sales); and
- The change in the sourcing method for the sales factor (to market-based sourcing).

In addition to reviewing the 2015 returns as filed, the Division recalculated the results from the returns to determine the tax that would have been owed under the old law (which included a 9 percent tax rate, single-entity reporting, three-factor apportionment, and cost-of-performance sourcing for the sales factor).[3]

'TAX DUE'

The term "tax due" appears numerous times throughout this report. To determine the amount of tax due, the Division used the information reported on Line 15 of the Form RI-1120C, "Business Corporation Tax Return," for the 2015 tax year. Line 15 is tax after credits, but before payments and other items.

The Division believes that this is the fairest and most accurate method – grounded, as it is, in actual return data – for providing apples-to-apples comparisons.

As a result of the aforementioned examination and calculations for tax year 2015, the Division estimated that the combined groups had approximately $62.4 million in tax due under the new law, compared with approximately $89.2 million under the old law.

Tax due overall under old law, new law

Old law	New law	Difference
$ 89,231,564	$ 62,426,195	($ 26,805,369)

In other words, the Division estimates that, under the new law compared with the old law, the combined groups saved – and the State of Rhode Island relinquished in revenue – approximately $26.8 million, a 30 percent reduction.

[3] For convenience, this report uses the term "old law" for the corporate tax regime in effect for tax year 2014, and the term "new law" for the corporate tax regime in effect for tax years beginning on or after January 1, 2015.

Impact of each key change in law

To help determine the impact of each of the four major corporate tax changes enacted in 2014 (for tax years beginning on or after January 1, 2015), the Division examined data in its new agency-wide computer system for unitary groups that filed combined reports for tax year 2015.[4] The Division then calculated what the tax due would have been under the old law compared with the new law, and determined the difference for each of the four major corporate tax changes.

(Note: To put this information in perspective, please see the "Frame of Reference" note in Section 5 of this report.)

- The effect on combined groups, in the aggregate, of the lowering of the corporate tax rate (from 9 percent to 7 percent) was a reduction in tax due of approximately $20.3 million.

Impact of lowering corporate tax rate (to 7%)
Difference
($ 20,281,836)

- The effect on combined groups, in the aggregate, of the change in the apportionment formula (from three-factor apportionment to single-sales-factor apportionment) was a reduction in tax due of approximately $47.2 million.

Impact of change in apportionment formula (to single factor: sales)
Difference
($ 47,178,994)

- The effect on combined groups, in the aggregate, of the change in the sourcing method used to determine how to treat a corporation's sales of services and/or intangible personal property (from cost-of-performance sourcing to market-based sourcing) was an increase in tax due of approximately $1.7 million.

Impact of change in sourcing method (to market-based sourcing)
Difference
$ 1,722,883

- The effect, in the aggregate, of the change from separate-entity reporting to mandatory unitary combined reporting was an increase in tax due of approximately $37.8 million.

Impact of change in reporting method (to combined reporting)
Difference
$ 37,771,117

[4] The Division determined the average marginal impact for each of the changes, as described later in this report.

Thus, of the four key changes to Rhode Island's corporate tax law, the Division estimates that two resulted in a reduction in tax due: the lowering of the corporate tax rate, and the change in the apportionment formula (to a single factor: sales).

The other two key changes to Rhode Island's corporate tax law resulted in an increase in tax due: the change in the sourcing method for sales (to market-based sourcing), and the change in the reporting method (to mandatory unitary combined reporting).

However, the impact of the two factors that resulted in a reduction in tax due more than offset the impact of the two factors that resulted in an increase in tax due.

Note

None of the four key changes listed above – involving the tax rate, the apportionment formula, the sourcing method, or the overall reporting method – stands in isolation. One is inextricably linked to the others. The dollar impact of any one of the four key changes is an estimate, resulting from averages, and should not be taken out of context. To help keep this information in perspective, please see the "Frame of Reference" note in Section 5 of this report.

Impact: Small business vs. large business

The Division examined returns, and performed calculations, to determine whether the change from the old law to the new law resulted in an increase, a decrease, or no change in tax due, for two broad categories of businesses – large businesses and small businesses.[5]

- The Division found that, for large businesses for tax year 2015, the tax due was unchanged for 76 percent, increased for 16.9 percent, and decreased for 7.1 percent, as a result of Rhode Island's moving to a new corporate tax regime.

Impact on large businesses		
No change	**Tax increase**	**Tax decrease**
76%	16.9%	7.1%

- The Division also found that, for those classified as "small businesses" for tax year 2015, the tax due was unchanged for 96.8 percent, increased for 2 percent, and decreased for 1.2 percent, as a result of the new corporate tax regime.

Impact on small businesses		
No change	**Tax increase**	**Tax decrease**
96.8%	2%	1.2%

[5] For purposes of this report, the Division used the U.S. Small Business Administration (SBA) definition of "small business", which differs depending on industry. For more information, please see Section 6 of this report.

Impact: Rhode Island vs. out-of-state corporations

The Division examined how the change from the old law to the new law affected Rhode Island combined groups versus out-of-state combined groups. (The definitions of a "Rhode Island combined group" and of an "out-of-state combined group" are contained in the body of this report.)

As a result of the aforementioned examination and calculations for tax year 2015, the Division estimated that out-of-state corporations, in the aggregate, had a tax due of approximately $55.1 million under the new law, compared with the tax due of approximately $34.7 million that they would have had under the old law.

- In other words, out-of-state corporations, in the aggregate, ended up paying more in Rhode Island tax – approximately $20.4 million, or 59 percent, more.

Impact of new law on out-of-state corporations: tax increase or decrease			
Old law	**New law**	**Difference** (in $)	**Difference** (in %)
$ 34,714,730	$ 55,086,805	$ 20,372,075	+ 58.7%

At the same time, the Division estimated that Rhode Island corporations, in the aggregate, had a tax due of approximately $7.3 million under the new law, compared to the tax due of approximately $54.4 million that they would have had under the old law.

- In other words, Rhode Island corporations, in the aggregate, ended up paying less in Rhode Island tax – approximately $47.2 million, or 87 percent, less.

Impact of new law on Rhode Island corporations: tax increase or decrease			
Old law	**New law**	**Difference** (in $)	**Difference** (in %)
$ 54,416,931	$ 7,252,893	($ 47,164,038)	- 86.7%

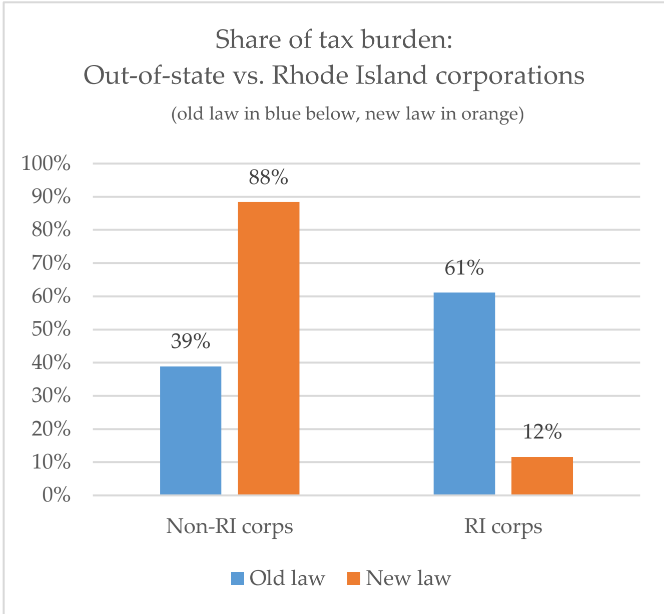
In dollar terms, the decrease in tax due for Rhode Island corporations more than offset the increase in tax due for out-of-state corporations.

Shift in tax burden overall

For tax year 2015, the change from the old law to the new law shifted the overall burden of tax due. Out-of-state corporations, in the aggregate, ended up with a greater share of the tax burden, while Rhode Island corporations, in the aggregate, ended up with a smaller share of the tax burden.

- Out-of-state corporations shouldered 38.9 percent of the burden under the old law. Under the new law, their share of the burden more than doubled, to 88.4 percent.[6]

- Rhode Island corporations shouldered 61.1 percent of the burden under the old law. Under the new law, their share of the tax burden dropped, to 11.6 percent.



In dollar terms, the decrease in tax due for Rhode Island corporations more than offset the increase in tax due for out-of-state corporations.

Fiscal impact TY 2015: Non-Rhode Island vs. Rhode Island corporations		
	Non-Rhode Island corps	**Rhode Island corps**
New law*	$ 55,086,805	$ 7,252,893
Old law**	$ 34,714,730	$ 54,416,931
Difference (in dollars)	$ 20,372,075	($ 47,164,038)
Difference (%)	58.7%	-86.7%

* New law includes 7% corporate tax rate, single-factor apportionment (sales), market-based sourcing for the sales factor, and mandatory unitary combined reporting.
** Old law includes 9% corporate tax rate, three-factor apportionment (sales, property and payroll), cost-of-performance sourcing for the sales factor, and separate-entity (single-entity) reporting.

[6] Numbers in chart are rounded.

Shift in tax burden, by specific change in law

The Division examined returns, and performed calculations, to determine the effect that each of the four key changes in corporate tax law – reduction in tax rate, change in apportionment, change in sourcing, and change in reporting method – would have had, holding all other factors constant.

(Note: To put this information in perspective, please see the "Frame of Reference" note in Section 9 of this report.)

☐ TAX RATE REDUCTION:

In the aggregate, out-of-state corporations and Rhode Island corporations benefited from the reduction in the corporate tax rate (from 9 percent for tax year 2014, to 7 percent for 2015 and later tax years). However, the tax rate reduction delivered the greatest benefit, in absolute terms, for out-of-state corporations (which, as shown earlier, shouldered a greater tax burden overall than did Rhode Island corporations). In the aggregate, out-of-state corporations saw a reduction in tax burden of approximately $12.3 million, while Rhode Island corporations saw a reduction in tax burden of approximately $7.9 million.

Fiscal impact of tax rate reduction on out-of-state, Rhode Island corporations		
	Out-of-state corporations	**Rhode Island corporations**
Increase (decrease) in tax	($ 12,312,101)	($ 7,969,735)

☐ CHANGE IN APPORTIONMENT FORMULA:

In the aggregate, out-of-state corporations and Rhode Island corporations benefited from the change in the apportionment formula (from three-factor apportionment for tax year 2014 to single-sales-factor apportionment for 2015 and later tax years). Rhode Island corporations saw most of the benefits, both in relative and in absolute terms, from the change from three-factor apportionment under the old law to single-sales-factor apportionment under the new law: They ended up with a reduction in tax due of approximately $40.4 million, while out-of-state corporations saw a reduction in tax burden of approximately $6.8 million.

Effect of change in apportionment formula on out-of-state, Rhode Island corporations		
	Out-of-state corporations	**Rhode Island corporations**
Increase (decrease) in tax	($ 6,771,568)	($ 40,407,426)

☐ CHANGE IN SOURCING METHOD:

Rhode Island corporations and out-of-state corporations, in the aggregate, did not benefit from the change in the sourcing method for sales for apportionment purposes (from cost-of-performance under the old law, to market-based sourcing under the new law). In the aggregate, out-of-state corporations had an increase in tax due of approximately $1.4 million, while Rhode Island corporations had an increase in tax due of approximately $336,000.

Fiscal impact of sourcing method change on out-of-state, Rhode Island corporations		
	Out-of-state corporations	**Rhode Island corporations**
Increase (decrease) in tax	$ 1,387,048	$ 335,835

☐ CHANGE IN REPORTING METHOD:

Rhode Island corporations and out-of-state corporations, on average, did not benefit from the change from single-entity reporting (under the old law) to combined reporting (under the new law). Out-of-state corporations ended up with a greater tax due as a result of the change: In the aggregate, out-of-state corporations had an increase in tax due of approximately $36.9 million, while Rhode Island corporations had an increase in tax due of approximately $804,000.

Fiscal impact of change in reporting method on out-of-state, Rhode Island corporations		
	Out-of-state corporations	**Rhode Island corporations**
Increase (decrease) in tax	$ 36,967,365	$ 803,752

Broader base

Rhode Island's adoption of mandatory unitary combined reporting led to a broadening of the tax base. The Division's overall analysis of the four key changes to Rhode Island's corporate tax structure shows that the move from single-entity, or separate-entity, reporting (which was in effect for the 2014 tax year) to combined reporting (for 2015 and later tax years) resulted in an increase in tax due.

Additional evidence of this can be seen in the Division's analysis of the effect of the four key corporate tax changes on Rhode Island combined groups versus out-of-state combined groups. That analysis showed that only two of the corporate tax changes – the shift to combined reporting, and the shift to market-based sourcing – led to an increase in tax due for both in-state and out-of-state combined groups. However, of those two key factors, the shift to combined reporting generated a far greater increase in tax due.

Combined reporting broadened Rhode Island's corporate tax base because, in effect, it was a recognition that a corporation doing business in Rhode Island was not a stand-alone entity if it was, in reality, part of a combined group engaged in a unitary business.

Thus, the corporation doing business in Rhode Island could no longer file its Rhode Island corporate income tax return as if it were a business in isolation; its return, under combined reporting, had to take into account the income of other corporations within the same broader business grouping, including those based in other states.

Disclaimer and notes

The following disclaimer is an integral part of this report. It is strongly recommended that the disclaimer be read in its entirety prior to any viewing of the report itself.

The Rhode Island Division of Taxation has made every effort to ensure that the data in this report is reliable. However, the Division urges that care be taken when drawing conclusions based on the data.

For example, the Division was required to compile the data based solely on the returns as filed by the corporations or their designees; there was insufficient time to audit all of those returns to ensure that they were complete and accurate.

Furthermore, the Division faced challenges in compiling this report due to limitations on the data collected and stored in its mainframe computer for tax years 2014 and before. These limitations led to a fundamental change in the agency's approach to this report, as further described later in this section.

Mainframe vs. ITS

Ideally, this report would identify all C corporations that filed Rhode Island corporate income tax returns for 2014 (which was the final year under Rhode Island's old corporate tax regime) and trace their tax results through the 2015 and 2016 tax years (the first two years under Rhode Island's new corporate tax regime).

In other words, ideally, this report would analyze C corporations to determine how those specific taxpayers fared as a result of the sweeping corporate tax changes enacted in 2014, effective for tax years beginning on or after January 1, 2015.

Such a comparison, however, could only partially be made, due chiefly to the inherent limitations of the Division of Taxation's older computerized records: Until the fall of 2016, the Division maintained its corporate tax records on a mainframe computer system, employing a programming language known as COBOL, which in the Division's case dates to the 1970s. The mainframe computer system allowed for only a limited amount of processing and data storage, and updating the old system was not an option. As a result, for purposes of the Division's analysis, there was an insufficient amount of data covering 2014 and prior tax years.

As a direct consequence of the General Assembly's foresight and funding, the Division was able in recent years to acquire, and successfully install and implement, a modernized, agency-wide computer system, known as an integrated tax system, or ITS. To minimize disruption for taxpayers and others, the Division elected to convert to the new system gradually, in phases.

It was in November 2016 that the Division transitioned its corporate tax recordkeeping system to the new ITS. As a consequence, the Division now has detailed records, all in one place, involving corporate income tax records for 2015 and later tax years.

Thus, the Division's new ITS serves as a repository for substantially all corporate income tax returns that have been filed since Rhode Island's new corporate tax structure was adopted (for tax years beginning on or after January 1, 2015).

This is important to note because – for 2015 and later tax years – the ITS repository includes, among other things, the results (for substantially all corporations) of a formula they use to determine how much of their income is taxed by Rhode Island, a formula known as apportionment – and the apportionment formula was changed by statute for tax years beginning on or after January 1, 2015.

One of the shortcomings of the old mainframe involved the amount of data it could capture. For example, the mainframe did not consistently capture information related to apportionment (apportionment schedules). Thus, if only for this reason alone, an apples-to-apples comparison for corporations between the 2014 tax year (when the old corporate tax structure was in effect) and the 2015 tax year (when the new corporate tax structure was in effect) cannot be made as it relates to the combined reporting schedule data.

There are other limitations, as well. For example, for each C corporation that filed as a single entity for tax year 2014, the Division has limited data; the mainframe stored little information about single-entity C corporations for 2014 and prior tax years.

Consolidated returns

Another factor involves consolidated returns. Federal tax law generally allows an affiliated group of corporations to make a single, consolidated return for the entire group, provided that the consolidated return clearly reflects the income tax liability of the group, as well as the various factors necessary for the determination of the affiliated group's tax liability.[7]

The filing of a consolidated return was generally allowed under the old Rhode Island corporate tax structure, and continues to be allowed under the new Rhode Island corporate tax structure (for affiliated groups that file a consolidated Rhode Island return in lieu of a Rhode Island combined return).[8]

For 2014 and prior tax years, if an affiliated group filed a consolidated return, the Division's mainframe did not identify the return as such. The impact is significant, and is perhaps best understood by example: Suppose that XYZ Corp. was, in effect, the designated agent for an

[7] See, among other things, Internal Revenue Code § 1501 *et seq*.

[8] Although Rhode Island adopted mandatory unitary combined reporting for tax years beginning on or after January 1, 2015, Rhode Island General Laws § 44-11-4.1 ("Combined reporting") generally allows an affiliated group of C corporations to treat the consolidated group as a combined group for Rhode Island purposes, under certain conditions.

affiliated group of corporations and filed a consolidated return with Rhode Island for the 2014 tax year.[9] Suppose, too, that XYZ Corp. filed a consolidated return with Rhode Island for the 2015 tax year. (In other words, XYZ Corp. checked a box on Form RI-1120C indicating that it was making the consolidated return election – filing a consolidated return in lieu of a combined return, as allowed by statute.)

For the Division to perform a proper analysis of the impact of the corporate tax changes that took effect for tax years beginning on or after January 1, 2015, the agency would have to review XYZ Corp.'s consolidated return – and each underlying member of the affiliated group included in the consolidated group – not only for the 2015 tax year (when the new corporate tax structure was in place), but also for the 2014 tax year (when the old corporate tax structure applied).

However, due to the mainframe's limitations, the Division was unable to determine the underlying members of XYZ Corp.'s affiliated group for the 2014 tax year. In other words, the Division was unable to tie all of the members of a particular affiliated group to the group's consolidated return. Thus, for example, for certain affiliated groups that each had 400 or more individual entities, the Division's mainframe did not capture data for any of the underlying members; the mainframe captured data only for the main filer (in this example, XYZ Corp.).[10]

For example, XYZ Corp. could have been the parent of the consolidated group (technically, the affiliated group) for the 2014 tax year, but the designated agent or a subsidiary for the group for the 2015 tax year. Or, XYZ Corp. could have been a subsidiary on the consolidated return for the 2014 tax year, but either the designated agent or a subsidiary on the return for the 2015 tax year.

Because of these and other limitations, the Division could not, with any degree of confidence, provide in this report the results of an apples-to-apples comparison, focusing on the tax results for C corporations when the old corporate tax structure was in place and the tax results for C corporations under the new corporate tax structure.

Revised approach

Given the limitations described above, the Division elected, after much reflection, to take a revised approach. For that approach, the Division carefully analyzed combined returns for the 2015 tax year, as contained in the agency's new ITS repository.

The Division then recomputed the tax results for those combined returns in an effort to determine how they would have fared had the old corporate tax structure remained in place for the same tax year.

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9 All names used in this publication are for illustration purposes only and are used in a fictitious manner. Any resemblance to actual persons or actual entities is coincidental.

10 Approximately 1,200 consolidated returns were filed with the Division of Taxation for the 2014 tax year.

The Division has a high degree of confidence that the results of its revised approach, as described above and more fully in the body of this report, fulfills the agency's statutory requirement to provide a report analyzing the policy and fiscal ramifications of the changes enacted to business corporations tax statutes for tax years beginning on or after January 1, 2015.[11]

For example, for the 2015 tax year, the Division was able to identify the specific members of each group – including members of combined groups and members of affiliated groups (which filed consolidated returns in lieu of combined returns).

Nevertheless, it is important to note that the revised approach described above has its own limitations, as would any detailed analysis of corporate tax data. For example:

- Substantially all of the combined returns filed for tax year 2015 are contained in the Division's new ITS repository, and their results are therefore reflected in this report. However, the Division's revised approach did not encompass combined returns for the 2016 tax year – chiefly because a number of such returns have yet to be filed. (See box nearby.)

- For purposes of its revised approach, the Division assumed that all of the corporations that had nexus in Rhode Island would have filed for the 2014 tax year – either as stand-alone corporations, or as members of an affiliated group (on a consolidated return). There can be no assurance, however, that either was the case.

- For purposes of comparing the impact of the change in the sourcing method for the sales factor under apportionment – from the cost-of-performance method under the old law to the market-based sourcing method under the new law, the Division focused on entities that had filed electronically in 2014 and were identifiably the same for their 2015 returns (based on their federal Employer Identification Numbers, or EINs). Because substantially all information from each electronically filed return was captured by the ITS, this allowed for an apples-to-apples comparison. However, the ITS did not capture all of the apportionment

FISCAL YEAR

While many returns for the 2016 tax year were filed by the fall of 2017, a number of 2016 returns are still outstanding. That is mainly because they are returns for corporations that use a fiscal year.

Some of those returns were not due until March 15, 2018 (too late for purposes of the analysis in this report) – including the returns for most of the 20 largest Rhode Island corporations (based on the size of their federal taxable income).

Therefore, this report focuses only on returns for the 2015 tax year; this report does not include the incomplete data for the 2016 tax year.

(Still, it cannot be said with any certainty that if the Division were able to include all of the combined returns for the 2016 tax year, it would make any appreciable difference in the results of the Division's fundamental analysis.)

[11] The Rhode Island corporate income tax is authorized under Rhode Island General Laws Chapter 44-11, which is titled "Business Corporation Tax."

data from paper-filed returns, so the Division could not include data from paper-filed returns in its analysis.[12]

- As noted previously, the returns analyzed for purposes of this report are unaudited. (The auditing process for a number of those returns has only just begun.) Thus, for purposes of this report, the Division relied chiefly on the results as reported by the corporations themselves.

Data cut-off date

It should also be noted that the underlying data for this report was repeatedly analyzed by the Division, and that the analysis was subject to numerous revisions. As the Division performed its work, returns continued to be filed. At some point, the Division had to halt its analysis in order to meet the deadline for this report as required by statute.

On February 16, 2018, the Division of Taxation largely ended its process of tallying and vetting the data for this report; the agency does not believe that further such efforts would result in any appreciable difference in the overall reliability of the data contained in this report.

Corporate tax volatility

It should also be stressed that the data in this report involves the corporate income tax, which historically has been a volatile source of revenue for states across the country.

A 2017 study by the Pew Charitable Trusts found that, nationwide between fiscal years 1996 and 2015, corporate income taxes and severance taxes on oil and minerals were consistently more volatile than other major state taxes, such as the personal income tax and the sales tax on goods and services.[13]

During the study period, corporate income tax revenue fluctuated more than any other tax source in 24 of the 30 states where it was a major tax, the study found.

The underlying volatility of individual tax streams is often driven by factors outside policymakers' control. These include economic factors—such as the mix of industry, natural resources, workforce, and population growth—as well as federal budget changes and unforeseen events, such as natural disasters.[14]

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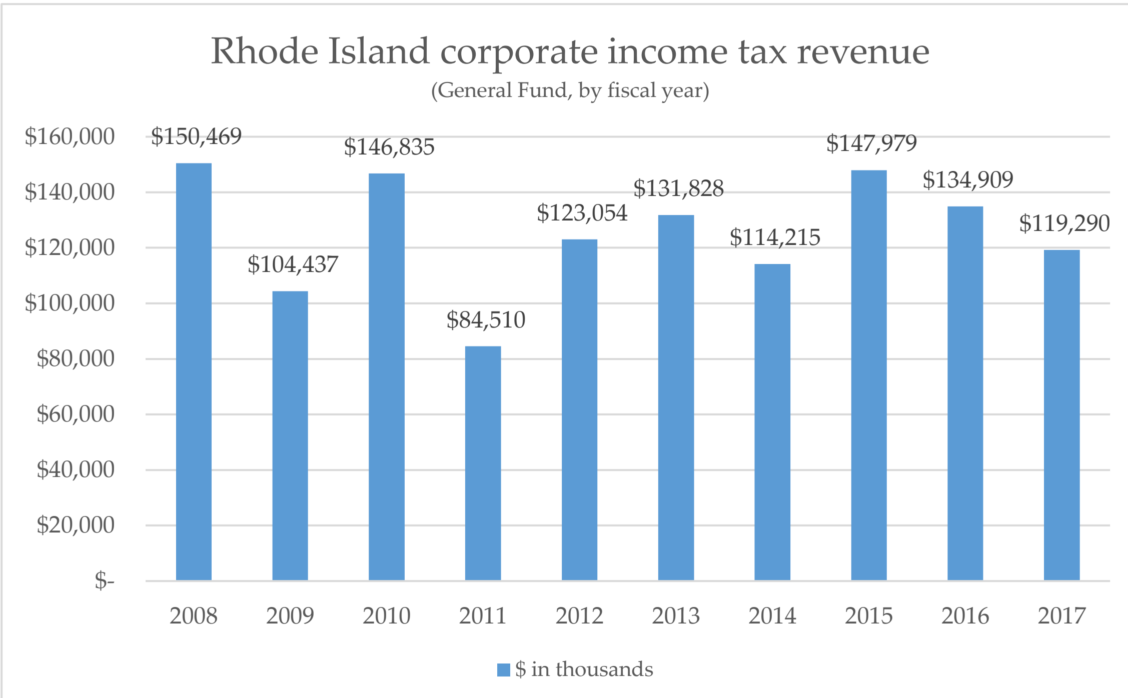
[12] For purposes of its analysis, the Division did not include data from paper-filed returns for the 2014 tax year. The Division did include data from paper-filed returns for the 2015 tax year, but only when the data from electronically filed returns for the 2014 tax year matched to a 2015 entity which had filed on paper.

[13] "Tax Revenue Volatility Poses Budget Challenges for Some States," Pew Charitable Trusts, February 2, 2017.

[14] Ibid.

Rhode Island corporate tax revenue

The following table shows corporate income tax revenue for the past 10 fiscal years, as reported in the "State of Rhode Island Comprehensive Annual Financial Report" for each fiscal year.[15]



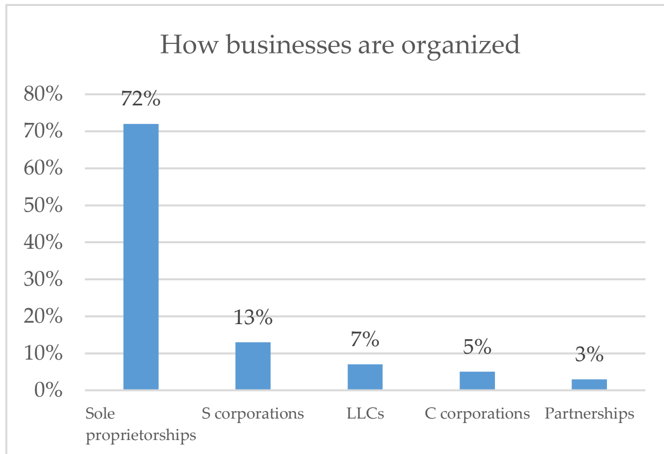
15 Actual amounts, unadjusted for inflation, from State of Rhode Island Comprehensive Annual Financial Report, "Schedule of Revenues, Expenditures and Changes in Fund Balance," General Fund, per fiscal year (actual amount).

Section 1

Background and explanation

It may be helpful, at the outset, for the Division to provide a brief overview of business entities, so that this report can be placed in some perspective.

The overwhelming majority of businesses in the United States are not corporations. As the nearby table shows, most are sole proprietorships.[16]



The next most common form of doing business is the S corporation, which is named after subchapter S of the Internal Revenue Code.

After that, the most common forms are (in order) limited liability companies (LLCs), C corporations (named after subchapter C of the Internal Revenue Code), and partnerships.[17]

Broadly speaking, entities that are treated as C corporations for federal income tax purposes are the focus of this report. However, again for perspective, it is important to note that this report focuses only on a comparatively small subset of C corporations – those that are taxed under Rhode Island General Laws Chapter 44-11 and that are part of a combined group under common ownership and engaged in a single or common business enterprise – a "unitary" business.[18]

Overall, a total of 12,764 returns were filed on Form RI-1120C for the 2015 tax year. Of those, the Division selected for analysis 2,012 returns (approximately one-half of them electronically filed).

[16] Text and table data from "A Brief Overview of Business Types and Their Tax Treatment," Congressional Research Service, August 9, 2017.

[17] Although C corporations represent a comparatively small portion of business types overall, C corporations generated more in net business income than any other business type between 1980 and 2013, according to the Congressional Research Service (see citation above).

[18] Many C corporations – and other entities – are taxed under other chapters of the Rhode Island General Laws and are not subject to Rhode Island's mandatory unitary combined reporting regime. They are therefore not the subject of this report.

That is because those 2,012 returns were filed by combined groups (each engaged in a unitary business) and contained Schedules CRS (the combined reporting schedule).[19]

Corporate tax returns on Form RI-1120C for 2015 tax year	
	Count
Total returns filed	**12,764**
Number of total returns (above) e-filed:	4,178
Number of combined returns	**2,012**
Number of combined returns (above) e-filed:	1,110
Note: Of the 12,764 returns filed on Form RI-1120C, a total of 2,012 were combined returns. Of those, 1,110 were e-filed.	

Thus, for the sake of perspective, the Division notes that approximately 16 percent of all returns filed on Form RI-1120C for the 2015 tax year were returns filed under combined reporting.

How combined reporting evolved in Rhode Island

Combined reporting was part of the sweeping changes to Rhode Island's corporate tax structure enacted in 2014, for tax years beginning on or after January 1, 2015. However, the roots of some of those changes can be traced to legislation that emerged three years earlier, in 2011. An understanding of that evolution is important for purposes of putting the current report in perspective.

On June 30, 2011, legislation approved by the Rhode Island General Assembly and signed into law by then-Governor Lincoln D. Chafee directed the Rhode Island Division of Taxation to study the potential impact on C corporations of changing from single-entity reporting to mandatory unitary combined reporting.[20]

At the time, a C corporation generally filed its annual corporate income tax returns as a single entity, a separate entity, taking into account only its own income. That was the case even if the corporation was part of a broader group of corporations, under common ownership, that were together engaged in a common business enterprise – a "unitary business."

Under combined reporting, a C corporation would report on its Rhode Island return not only its own income, but also the combined income of the other corporations, or affiliates, that were under common ownership and part of a unitary business.

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[19] Although the Division reviewed 2,012 combined returns, the Division had to perform additional filtering and fixes on some of them to ensure that they were helpful for purposes of this analysis. For example, in some cases, a parent corporation may have incorrectly structured its numerous Schedules CRS, or the parent filed the Form RI-1120C, but also filed a Schedule CRS for itself. In such cases, the Division did not filter out the entire filing. Instead, the Division manually made the required adjustments so that the return itself could be employed in the analysis. (Copies of Form RI-1120C and Schedule CRS for the 2015 tax year are appended to this report.)

[20] Rhode Island Public Law 2011, ch. 151, art. 19, § 4, subsequently codified at Rhode Island General Laws § 44-11-45 (repealed by Rhode Island Public Law 2014, ch. 145, art. 12, § 18).

In other words, a C corporation would treat all of its affiliates, including those in other states, as if they were one, single company, and combine all of their taxable income in a single pool. The combined group would then use a formula to apportion the amount of the combined income to Rhode Island for tax purposes.

Filing of *pro forma* returns

To determine how combined reporting might work in Rhode Island – and, in particular, what the tax impact might be on corporations and what the revenue impact might be on the State – the 2011 legislation as enacted required each C corporation that was part of a unitary business under common ownership to file a *pro forma* report for the combined group to include the combined income of the combined group.

In other words, C corporations were required to calculate their Rhode Island corporate tax liability as if combined reporting were in effect.

As part of that effort, C corporations subject to *pro forma* combined reporting were required by statute to calculate their Rhode Island corporate income tax using two separate apportionment formulas: the standard formula under then-current law, which relied on three factors – sales, property, and payroll, and a different formula, which relied solely on sales – known as single-sales-factor apportionment, disregarding the property and payroll factors.

FOR MORE INFORMATION

The Rhode Island Division of Taxation's website includes a page that features, all in one location, numerous documents involving combined reporting, apportionment, nexus, and related matters, including the 2014 study on *pro forma* combined reporting. To view the webpage:

http://go.usa.gov/KpyY

In addition, C corporations subject to *pro forma* combined reporting were required to calculate their combined receipts using the Joyce method versus the Finnegan method. (The methods are explained further in the body of this report.)

It is important to note that the study required under the 2011 legislation did not contemplate a change to the corporate tax rate, which at the time was 9 percent.[21]

It is also important to note that the study required under the 2011 legislation did not contemplate a change in the sourcing method for the sales factor (from cost-of-performance sourcing, which was in effect at the time, to market-based sourcing).

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[21] At the time, a corporation's Rhode Island tax was the greater of the franchise tax or the corporate income tax, and the corporate income tax rate was 9 percent. For tax years beginning on or after January 1, 2015, the franchise tax was repealed and the corporate income tax rate was reduced to 7 percent – the lowest maximum corporate income tax rate in New England at the time of enactment.

The 2011 legislation directed the Division of Taxation to study the impact of combined reporting over two tax years: 2011 and 2012.[22] The Division's report of its study, filed by the March 15, 2014, statutory deadline, is available on the Division's website: go.usa.gov/KR9F.

Overall, approximately 1,621 combined groups filed *pro forma* combined reports to Rhode Island for those years. Based on those returns, the Division found that the aggregate increase in Rhode Island corporate tax for tax year 2011 would have been $23.4 million to $25.3 million using three-factor apportionment, and $49.5 million to $54.7 million using single-sales-factor apportionment.

The Division also found that the aggregate increase in Rhode Island corporate tax for tax year 2012 would have been $21.5 million to $23.1 million using three-factor apportionment, and $38.6 million to $44.4 million using single-sales-factor apportionment.

All of the results of the study are available by viewing the 2014 report itself, so they are not reproduced in their entirety here.

In summary, however, the Division found that, had Rhode Island adopted combined reporting for tax years 2011 and 2012, corporations subject to combined reporting, using the standard three-factor apportionment formula, would have had to pay, in the aggregate, more in Rhode Island corporate income tax, and the State would have gained more in revenue.

The Division also found that, had Rhode Island required such corporations to use the single factor of sales in their apportionment calculation under combined reporting, corporations would have had to pay, in the aggregate, still more in Rhode Island corporate income, and the State would have gained still more in revenue.

Range of aggregate increase in Rhode Island corporate tax (*pro forma*)

	With three-factor apportionment	With single-sales-factor apportionment
Tax year 2011	$23.4M to $25.3M	$49.5M to $54.7M
Tax year 2012	$21.5M to $23.1M	$38.6M to $44.4M

Dollar figures are in millions. First dollar figure in each row calculated under Joyce method, second under Finnigan.
Source: Rhode Island Division of Taxation

From a broader standpoint, the Division's 2014 report showed that, under combined reporting as a whole:

- 6.6 percent of groups, on average, would have seen a decrease in tax;
- 28.8 percent, on average, would have seen an increase in tax; and
- 64.6 percent of groups, on average, would have seen no change in tax.

[22] The legislation focused on taxable years beginning after December 31, 2010, but before January 1, 2013.

There were variations by year and by apportionment formula.

Corporations with tax change, no tax change, due to combined reporting (*pro forma*)			
	% increase in tax	% decrease in tax	% no change
Tax year 2011			
Three-factor apportionment (Joyce)	29%	10%	61%
Three-factor apportionment (Finnigan)	31%	9%	60%
Single-sales-factor apportionment (Joyce)	35%	5%	60%
Single-sales-factor apportionment (Finnigan)	37%	5%	58%
Tax year 2012			
Three-factor apportionment (Joyce)	21%	8%	71%
Three-factor apportionment (Finnigan)	22%	8%	70%
Single-sales-factor apportionment (Joyce)	27%	4%	69%
Single-sales-factor apportionment (Finnigan)	**28%**	**4%**	68%
For details about the difference between the Joyce and Finnigan methods, please see following section.			

For each year of the study, the greatest percentage of corporations reporting a *pro forma* increase in Rhode Island corporate income tax – and the smallest percentage reporting a *pro forma* decrease in tax – occurred where corporations calculated tax liability using single-sales-factor apportionment.

The Division also found that, for each year of the study, the smallest percentage of corporations reporting a *pro forma* increase in Rhode Island corporate income tax – and the greatest portion reporting a *pro forma* decrease in tax – occurred when the combined groups used three-factor apportionment.

Again, it is important to note that, for purposes of the study whose results led to the Division's March 2014 report, *pro forma* returns were required to be submitted under the assumption that the tax rate itself was unchanged (at 9 percent), and that the sourcing method for the sales factor was unchanged (the cost-of-performance method).

This point warrants emphasis because the legislation that Rhode Island ultimately enacted included not only mandatory unitary combined reporting and single-sales-factor apportionment for many C corporations, but also a 22 percent reduction in the corporate tax rate (from 9 percent under former law to 7 percent under the new law), and a change in the sourcing method for the sales factor (from cost-of-performance sourcing under the old law to market-based sourcing under the new law).[23]

Thus, the results of the Division's March 2014 study were limited in their scope, and the potential impact on corporations (and on corporate tax revenue for the State) must be viewed accordingly.

[23] Rhode Island Public Law 2014, ch. 145, art. 12, § 13 *et seq*. See also, among other things, Rhode Island General Laws § 44-11-4.1.

Changes enacted

With the results of the Division of Taxation study on *pro forma* combined reporting in hand, the General Assembly in 2014 held a series of hearings on a proposed budget for the 2015 fiscal year.

The bill that emerged, and which was ultimately enacted, included a far-reaching package of changes to the corporate tax structure.

The package included the following features for tax years beginning on or after January 1, 2015:

- combined reporting;
- single-sales factor apportionment;
- market-based sourcing;
- a reduction in the corporate tax rate; and
- repeal of the franchise tax.

A brief discussion of each element is worthwhile here, given that each has a bearing on the results of the Division of Taxation's statutorily required 2018 report on analyzing the policy and fiscal ramifications of all of the changes to the business corporation tax statutes enacted in 2014 as part of the budget bill for the 2015 fiscal year.

States that have adopted combined reporting – including all states in New England				
Alaska	District of Columbia	Maine	Nebraska	Rhode Island
Arizona	Hawaii	Massachusetts	New Hampshire	Texas
California	Idaho	Michigan	New York	Utah
Colorado	Illinois	Minnesota	North Dakota	Vermont
Connecticut	Kansas	Montana	Oregon	West Virginia
				Wisconsin
Source: Institute on Taxation and Economic Policy, 2017.				

Combined Reporting

The new law mandated unitary combined reporting, including a series of related provisions which were elaborated on in a subsequent Division of Taxation regulation.

In general, combined reporting is limited to those entities that are treated as C corporations for federal income tax purposes. For Rhode Island combined reporting to apply, such a C corporation must be part of a combined group, and the combined group must be engaged in a single business enterprise -- a unitary business.

Therefore, for combined reporting purposes, corporations and their advisors face two threshold issues: the determination of the combined group, and the determination of a unitary business.

Combined group

In summary, the term "combined group" means a group of two or more C corporations in which more than 50 percent of the voting stock of each member corporation is directly or indirectly owned by a common owner or owners, either corporate or non-corporate, or by one or more of the member corporations, and that are engaged in a unitary business.

Thus, an entity treated as a C corporation for federal income tax purposes that stands alone – i.e., a C corporation with no affiliates or related companies -- is not subject to combined reporting.

However, an entity treated as a C corporation for federal income tax purposes that does business in Rhode Island and is part of a combined group – a group whose members are commonly owned and controlled and which is engaged in a unitary business – is subject to combined reporting, whether the group does business only in Rhode Island or in multiple states.

In such a situation, the C corporation must, for Rhode Island tax purposes, include the income and sales factors of all of its affiliated corporations – no matter where they are situated in the United States and no matter if the affiliates have nexus in Rhode Island.

CONSOLIDATED ELECTION

It is important to note that, prior to the enactment of mandatory unitary combined reporting, Rhode Island allowed an affiliated group of businesses to file a consolidated return.

In general, a "consolidated return" means a return filed with the Internal Revenue Service on a consolidated basis by an affiliated group of corporations under terms of IRC § 1501 *et seq*.

Even after Rhode Island's corporate tax structure was changed in 2014, implementing combined reporting for tax years beginning on or after January 1, 2015, the Division of Taxation continues to allow an affiliated group to elect to use (for Rhode Island combined reporting purposes) the same members that the affiliated group includes in filing its federal consolidated return. (Once the election is made, it must continue for five years, including the year the election is made.)

Put another way, an affiliated group of C corporations, filing a federal consolidated return, may elect to be treated as a combined group with respect to Rhode Island's combined reporting requirement.

For purposes of Rhode Island combined reporting, the consolidated election may or may not result in a lower Rhode Island tax liability for a given affiliated group.

The combined return also must include the income and apportionment factor of each foreign corporation if such corporation's sales factor in the United States is more than 20 percent.

Water's edge

In general, the term "water's edge" is a term used in tax discussions regarding to what extent a combined group should include overseas members for purposes of combined reporting.

Some states require all or substantially all of a group's members worldwide to be included in the combined group. Some states allow the combined group to adopt a "water's edge" election – which, if adopted, generally limits a combined group's membership to members within the United States – up to the "water's edge".

For purposes of Rhode Island combined reporting, water's edge treatment is mandatory. Thus, a combined group must include the entire income and apportionment factor of any member not incorporated in the United States, regardless of the place incorporated or formed, if its sales factor in the United States is more than 20 percent.

Members of a combined group must exclude as a member and disregard the income and apportionment factors of any corporation not incorporated in the United States (a "non-U.S. corporation") if its sales factor for total receipts outside the United States is 80 percent or more.[24]

EXEMPT ENTITIES

Although the 2014 legislation adopted combined reporting, the legislation and/or subsequent regulation excludes from combined reporting numerous entities – even if they are organized or operate as C corporations:

- State banks
- Mutual savings banks
- Federal savings banks
- Trust companies
- National banking associations
- Building and loan associations
- Credit unions
- Loan and investment companies
- Public service corporations
- Insurance companies
- Captive insurance companies taxed under Rhode Island General Laws Chapter 27-43
- Subchapter S corporations

Also exempt are partnerships treated as pass-through entities for federal tax purposes; limited liability companies treated as pass-through entities for federal tax purposes; sole proprietorships and similar entities that are disregarded as separate from their owners ("disregarded entities"); and any corporation incorporated in a foreign jurisdiction if its sales factor for total receipts outside the United States is 80 percent or more.

Note: Although a pass-through entity is not, in and of itself, included in a combined return, the combined group's share of the pass-through entity's income, normally reported on federal Schedule K-1, must be reported as part of the combined group's income. "Pass-through entities" for this purpose include, but are not limited to, limited liability companies that are taxed as partnerships (not as corporations) or treated as disregarded entities under federal law, single member LLCs, and S corporations that are not themselves members of the combined group.

Unitary business

A group of C corporations is not subject to combined reporting unless it is engaged in a unitary business.

The following excerpt, adapted from the Multistate Tax Commission's Model Apportionment Statute, describes in part Rhode Island's law:

[24] Division of Taxation Regulation CT 16-17 provides additional guidance on how to determine which corporations are included in, and excluded from, a combined group, including a flow chart with details involving non-U.S. corporations, tax treaty countries, and tax havens.

> A unitary business is a single economic enterprise that is made up either of separate parts of a single entity or of a commonly controlled group of entities that are sufficiently interdependent, integrated and interrelated through their activities so as to provide a synergy and mutual benefit that produces a sharing or exchange of value among them and a significant flow of value to the separate parts.
>
> This flow of value to an entity located in this state that comes from being part of a unitary business conducted both within and without Rhode Island is what provides the constitutional due process "definite link and minimum connection" necessary for Rhode Island to apportion income of the unitary business, even if that income arises in part from activities conducted outside Rhode Island. The income of the unitary business is then apportioned to Rhode Island using Rhode Island formulary apportionment.
>
> This sharing or exchange of value may also be described as requiring that the operation of one part of the business be dependent upon, or contribute to, the operation of another part of the business. Phrased in the disjunctive, the foregoing means that if the activities of one business either contributes to the activities of another business or are dependent upon the activities of another business, those businesses are part of a unitary business.[25]

For Rhode Island corporate income tax purposes, the term "unitary business" means the activities of a group of two or more C corporations under common ownership that are sufficiently interdependent, integrated, or interrelated through their activities so as to provide mutual benefit and produce a significant sharing or exchange of value among them or a significant flow of value between the separate parts.

Apportionment

The term "apportionment" refers to the formula that a combined group uses to determine the amount of a combined group's income that is to be taxed under the Rhode Island corporate income tax.

Under the old Rhode Island law, C corporations typically apportioned their income using three equally weighted factors: sales (total receipts), property, and payroll. However, under the new law, an entity that is treated as a C corporation for federal tax purposes typically must use a single factor – sales (total receipts) – for apportionment purposes (whether or not the C corporation is part of a combined group). The purpose of single-sales-factor apportionment is to determine the combined group's Rhode Island source income, which is taxable.

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25 Multistate Tax Commission Allocation and Apportionment Regulations as adopted February 21, 1973, revised through July 29, 2010, and amended February 24, 2017.

Finnigan method

For *pro forma* combined reporting, multi-state C corporations had to apportion income – for including in the combined reporting entity – using two methods that are named for seminal California court cases: the Joyce method (see *Appeal of Joyce, Inc.*, California State Board of Equalization, 66-SBE-070, November 23, 1966) and the Finnigan method (see *Appeal of Finnigan Corp.*, California State Board of Equalization, 88-SBE-022, August 25, 1988).[26]

Both the Joyce and Finnigan methods involve a concept called "nexus" – which generally refers to a corporation's presence in a state for tax purposes. ("Nexus" means a connection or link with the state sufficient to subject an entity to tax by the state. See Division of Taxation Regulation 280-RICR-20-25-8, "Nexus.")

Under the Joyce method, nexus determinations are made at the level of each individual entity; sales by an entity lacking nexus in Rhode Island are excluded from the numerator for Rhode Island tax purposes.

Under the Finnigan method, the entire unitary group as a whole is treated as the taxpayer for apportionment purposes; all sales of members of the unitary group attributable to Rhode Island are included in the sales factor numerator. The denominator must include the combined group's gross receipts from sales everywhere during the taxable year.

Overall, the Joyce method generally costs businesses less in taxes and generates less in a state's tax revenue than the Finnigan method. Ultimately, Rhode Island adopted the Finnigan method for tax years beginning on or after January 1, 2015.[27]

The following states have adopted the Finnigan approach: Alaska, Arizona, California, Connecticut, Indiana, Kansas, Massachusetts, Maine, Michigan, Minnesota, New York, Rhode Island, Utah, and Wisconsin.[28]

CORPORATE TAX REVENUE

In general, under Rhode Island's corporate income tax, also known as the business corporation tax, each corporation must annually pay to the State a tax equal to 7 percent of its net income.

For the 12 months that will end on June 30, 2018, the corporate income tax is projected to generate approximately $151.2 million in revenue, compared with $119.3 million for the 2017 fiscal year, an increase of 26.8 percent.

Overall for the 2018 fiscal year, the corporate income tax is projected to generate approximately 4 percent of Rhode Island's projected total general revenues of $3,824,400,000.

Source: Rhode Island Revenue Estimating Conference, November 2017

[26] See Division of Taxation Regulation CT 12-15, "Combined Reporting (*pro forma*)".

[27] See Division of Taxation Regulation CT 16-17, "Combined Reporting."

[28] Oregon Department of Revenue presentation to the Oregon Senate Committee on Finance and Revenue, February 6, 2017.

Sourcing

In computing the sales factor, a C corporation must determine how to treat a corporation's sale of services and intangibles for purposes of corporate income tax apportionment.

Under the old law, a C corporation assigned the sale of its services to the state in which the income-producing activity was actually performed.

If the corporation performed activity in multiple states, the sale was assigned 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.

Under the new law, a C corporation typically must use a different sourcing approach, known as market-based sourcing. Under market-based sourcing, receipts from transactions (other than sales of tangible personal property) are sourced to the market state. In other words, the sale of a corporation's services is assigned to the state in which either the services (or the benefit of the services) are received or delivered, or where the customer or marketplace is located. Thus, market-based sourcing does not levy tax based on productive in-state labor, as the cost-of-performance method did.

'MARKET' STATES

Approximately 26 states use the market-based sourcing approach for the sourcing of service receipts.

At least 10 of those jurisdictions -- Connecticut, the District of Columbia, Louisiana, Massachusetts, North Carolina, Nebraska, New York, Pennsylvania, Rhode Island, and Tennessee – have adopted the market-based sourcing approach since 2010.

-- "State Corporate Income Tax Rules for Sourcing of Revenue for Law Firms," ABA Tax Times, American Bar Association, August 2017

Tax rate, franchise tax, minimum tax

Under the old law, corporations paid either the Rhode Island corporate income tax or the Rhode Island franchise tax, whichever was higher.

The franchise tax generally applied to every corporation, joint-stock company, or association incorporated in Rhode Island or qualified to do business in Rhode Island (although certain corporations were exempt). The franchise tax had been equal to $2.50 per $10,000 of a corporation's authorized capital stock.[29] The minimum tax was $500.

However, under the new law, the corporate income tax rate was reduced by 22 percent (or 2 percentage points), to 7 percent. Also, the franchise tax was repealed. As a result, for tax years beginning on or after January 1, 2015, the maximum corporate income tax rate for a combined

[29] Due to data limitations, the Division did not analyze the impact of franchise tax repeal.

group engaged in a unitary business is 7 percent. The minimum tax for 2015 was $500. (For more about the minimum tax, and the computation of tax in general for a combined group, please see the appendices.)

Note

This report frequently uses the term “separate entity” or “single entity” to refer to the manner in which C corporations (subject to tax under Rhode Island General Laws Chapter 44-11) filed their returns for tax year 2014, before the sweeping changes to the corporate tax structure took effect. In fact, filers had a choice: file as a separate entity, or file a consolidated return (as allowed by statute).

New law vs. old law

As previously mentioned, legislation enacted in 2014 resulted in sweeping changes to Rhode Island's corporate tax regime.

The changes, which took effect for tax years beginning on or after January 1, 2015:

- reduced Rhode Island's corporate tax rate by 22 percent, to 7 percent;
- changed the reporting method, from single-entity to mandatory unitary combined reporting;
- altered the apportionment formula, from three-factor apportionment, taking into account sales, property and payroll, to a single factor: sales, and
- changed the sourcing method for sales, from cost-of-performance to market-based sourcing.

Data and tax year

For convenience, this report uses the term "old law" for the corporate tax regime in effect for tax year 2014, and the term "new law" for the corporate tax regime in effect for tax years beginning on or after January 1, 2015.

To help determine the fiscal impact of the key corporate tax changes enacted in 2014 (for tax years beginning on or after January 1, 2015), the Division examined data in its new agency-wide computer system for unitary groups that filed combined reports for tax year 2015 – including those that electronically filed returns and those that filed paper returns. The Division then calculated what the tax due would have been under the old law compared with the new law.

New law vs. old law – explanation at a glance*

	Old law	New law
Corporate tax rate:	9%	7%
Reporting method:	Separate entity	Combined reporting
Apportionment formula:	Three-factor**	Single factor**
Sourcing method for sales:	Cost of performance	Market-based sourcing

*"Old law" in effect for 2014 tax year, "new law" in effect for tax years beginning on or after January 1, 2015.
** Three-factor apportionment relied on sales, payroll, and property. Single-factor apportionment relies on one factor: sales.

Preparation of report

The analysis underlying this report began in the fall of 2017, when the Division assembled an internal team. Members of that team met repeatedly as part of a months-long effort to review thousands of corporate tax returns and painstakingly make needed adjustments to prepare the data for use.

In some cases, returns as prepared and filed contained numerous structural problems, indicating either issues with the tax-preparation software used by corporations or their tax advisors, or a lack of familiarity with the complexities involved in combined reporting and related matters. (In fairness, some corporations or their tax advisors had to assemble information from literally hundreds of affiliates or member corporations, then sort the data and perform the computations that are necessary as part of the preliminary steps involved before actually preparing and filing the return.)

Once the early results were available, the team then had to devise the most appropriate approach that would meet the General Assembly's requirements for this report while also keeping in mind the many limitations of the underlying data.

When the final approach was settled, the Division's team then had to test and re-test the data to ensure that its analysis was accurate. The team then met repeatedly to prepare the best approach for drafting a report, and reviewed the report for fairness, accuracy, and consistency. When the work was completed, the Division submitted the report by the statutory deadline of March 15, 2018.[30]

[30] Cover photo, of Rhode Island State House in Providence, Rhode Island, by Rhode Island Division of Taxation.

New law vs. old law: overall impact

As a result of the aforementioned examination and calculations for tax year 2015, the Division estimated that the combined groups had approximately $62.4 million in tax due under the new law, compared with approximately $89.2 million under the old law.

In other words, the Division estimates that the combined groups saved – and Rhode Island relinquished in revenue – approximately $26.8 million, a 30 percent reduction.

Fiscal impact: New law vs. old law	
	Tax year 2015
New law*	$ 62,426,195
Old law**	$ 89,231,564
Difference	($ 26,805,369)

* New law includes 7% corporate tax rate, combined reporting, single-factor apportionment (sales), and market-based sourcing

** Old law includes 9 percent corporate tax rate, single-entity reporting, three-factor apportionment (sales, property, payroll), and cost-of-performance sourcing.

Notes

For purposes of this analysis, the Division examined data from 2,012 returns filed by combined groups for tax year 2015. Of those, 1,917 remained for more detailed analysis. (The Division eliminated a number of the 2,012 returns for various reasons. For example, if a return included multiple Schedules CRS that were identical, the Division did not include that return in its more detailed analysis.)

Of the 1,917 returns that remained for more detailed analysis, 486 "checked the box" on the return on Form RI-1120C indicating that they made the consolidated return election. (In other words, they elected to use their federal consolidated group in lieu of a combined group for purposes of meeting Rhode Island's combined reporting requirement.)

Also, as previously noted, this report frequently uses the term "tax due." To determine the amount of tax due, the Division used the information reported on Line 15 of the Form RI-1120C, "Business Corporation Tax Return," for the 2015 tax year. Line 15 is tax after credits, but before payments and other items. The Division believes that this is the fairest and most accurate method – grounded, as it is, in actual return data – for providing apples-to-apples comparisons.

Effect of each key change in law

Section 4 of this report looked at the overall impact of the package of tax law changes enacted in 2014. This section considers the contribution of various portions of that package of changes to the overall outcome. For example, the lowering of the corporate tax rate had a negative impact on taxes owed – but how much should be attributed to that single change?

Similarly, how is the Division of Taxation to evaluate the claim that combined reporting should broaden the tax base and raise revenue, all other factors held constant, when combined reporting constituted only one portion of the package of changes in tax law?

The following analysis attempts to tease out the marginal effects of the four principal components of the change in tax law as enacted. By 'marginal effects', the Division means the effect of one portion of the corporate tax law change, with all other factors held constant.

This breakdown attempts to apportion the effects of the change, but also to examine the differential impacts of these components on in-state and out-of-state corporations. The results serve to confirm that the effects of the components are broadly consistent with both the theory and observed effects in other states. This gives the Division increased surety in the correctness of the analysis.

To help determine the impact of each of the four major corporate tax changes enacted in 2014 (for tax years beginning on or after January 1, 2015), the Division examined data in its new agency-wide computer system for combined groups that filed combined reports for tax year 2015.

The Division then calculated what the tax due would have been under the old law compared with the new law, and determined the difference for each of the four major corporate tax changes.

- The effect on combined groups, in the aggregate, of the lowering in the corporate tax rate (from 9 percent to 7 percent) was a reduction in tax due of approximately $20.3 million.

- The effect on combined groups, in the aggregate, of the change in the apportionment formula (from three-factor apportionment to single-sales-factor apportionment) was a reduction in tax due of approximately $47.2 million.

- The effect on combined groups, in the aggregate, of the change in the sourcing method used to determine how to treat a corporation's sales of services and/or intangible personal property (from cost-of-performance sourcing to market-based sourcing) was an increase in tax due of approximately $1.7 million.

- The effect, in the aggregate, of the change from separate-entity reporting to mandatory unitary combined reporting was an increase in tax due of approximately $37.8 million.

Fiscal impact: Average marginal effect of four key changes in law*	
Tax rate reduction	($ 20,281,836)
Change in apportionment formula	($ 47,178,994)
Change in sourcing method	$ 1,722,883
Change in overall reporting method	$ 37,771,117

* Table shows effect on combined groups, in the aggregate, for each of four key changes in corporate tax law that took effect for tax years beginning on or after January 1, 2015: corporate tax rate reduction (to 7% from 9%), change in apportionment formula (to single-sales-factor apportionment from three-factor apportionment), change in sourcing method for sales, or gross receipts (to market-based sourcing from cost-of-performance sourcing), and change in reporting method (to mandatory unitary combined reporting from separate-entity reporting).

Observation

Put another way, the change in the apportionment formula (to single-sales-factor apportionment), and the change in the tax rate (to 7 percent), both resulted in a decrease, in the aggregate, in tax due. Of the two elements, the change in the apportionment formula was the single largest factor in reducing the tax due. At the same time, the switch to combined reporting, and the change in the sourcing method for the sales factor in apportionment (to market-based sourcing), resulted in an increase, in the aggregate, of tax due. (The switch to combined reporting was the single largest factor in increasing the tax due.)

In the aggregate, the analysis shows that the combined effect of the change in the overall apportionment formula and the lowering of the tax rate more than offset the increase in tax due from the switch to combined reporting and the change to market-based sourcing.

Frame of reference

In Section 4 of this report, the Division of Taxation estimated that the combined groups had approximately $62.4 million in tax due under the new law, compared with approximately $89.2 million under the old law. In other words, the Division estimates that the combined groups saved – and Rhode Island relinquished in revenue – approximately $26.8 million, a 30 percent reduction.

In this section of the report, the Division shows the impact of each of the four key changes in tax law. However, a sum of the results of each of the four key changes in this section of the report totals approximately $27.97 million.

Why does the sum of each of the four key changes not equal the total of $26.8 million listed in Section 4 of this report? It is because the dollar impact for each of the four changes listed in this section of the report is, in reality, an average – of many different scenarios.

Why is it an average? It is because none of the four key changes could be analyzed on its own, in isolation. For example, in the 2014 legislation as enacted, there was a tax rate reduction -- but there was also a change in the apportionment formula, a change in the sourcing method, and a change in the reporting method.

Thus, to determine the impact of just the tax rate reduction, the Division also had to take into account the three other elements (apportionment formula, sourcing method, and reporting method) under both the old law and the new law. In other words, the Division had to examine the tax rate in concert with:

- the apportionment formula under the old law and the apportionment formula under the new law;
- the sourcing method under the old law and the sourcing method under the new law; and
- the reporting method under the old law (separate-entity reporting with the option for consolidated reporting) and the reporting method under the new law (combined reporting).

The Division then had to compute an average for each. Thus, for example, the impact listed in the table in this section of the report for the tax rate reduction is, in reality, the average aggregate impact of all of the various scenarios mentioned above. It would be misleading to present the numbers in the table as anything but average aggregate numbers. Therefore, they cannot in fairness be summed and compared with the overall impact number listed in the previous section of this report.

In other words, because these are averages, they do not sum to the whole figure in Section 4 of this report. (As it happens, however, they do come close: There is a difference of approximately 4 percent.)

Effect by size of business

The Division examined returns, and performed calculations, to determine the effect that the new tax law had on two categories of businesses – large businesses and small businesses. The goal was to determine, in the aggregate, whether the new corporate tax regime enacted in 2014 (for tax years beginning on or after January 1, 2015) resulted in an increase, decrease, or no change in tax due.

The Division found that, for each category of business, the tax due was unchanged for the overwhelming majority of businesses – although a greater percentage of small businesses than large businesses saw no change.

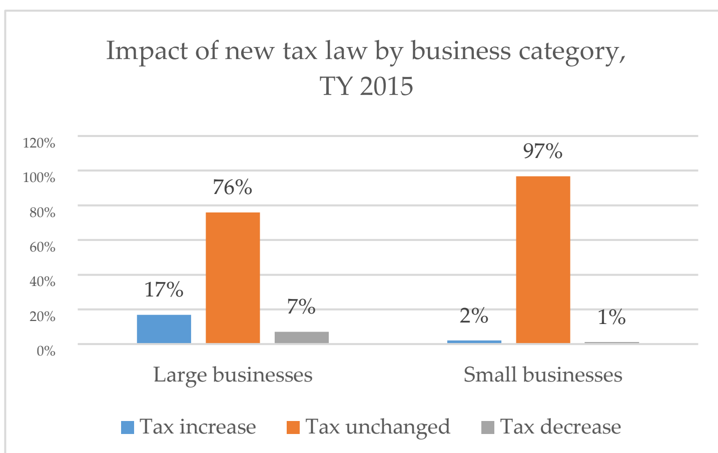
The Division also found that, for each category of business, the tax due increased for some businesses – although a greater percentage of large businesses than small businesses saw an increase.

At the other end of the spectrum, for each category of business, the Division found that the tax due decreased for a comparatively small percentage of businesses – although a greater percentage of large businesses than small businesses saw a decrease.

Results

The Division found that, for large businesses for tax year 2015, the tax due was unchanged for 76 percent, increased for 16.9 percent, and decreased for 7.1 percent, as a result of Rhode Island's moving to a new corporate tax regime.

The Division also found that, for those classified as "small businesses" for tax year 2015, the tax due was unchanged for 96.8 percent, increased for 2 percent, and decreased for 1.2 percent, as a result of the new corporate tax regime.



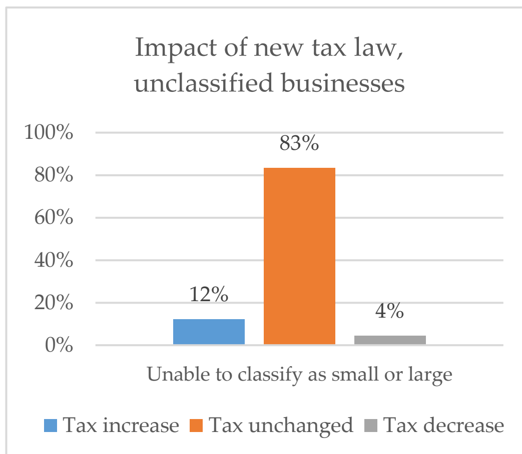
Business classification

For purposes of this report, the Division used the U.S. Small Business Administration (SBA) definition of "small business"; if an entity did not fit the SBA definition, the Division typically classified the entity as a large business (although some entities could not be classified at all, as described elsewhere in this section).

The SBA has established numerical definitions, or "size standards", for all for-profit industries. Size standards represent the largest size that a business may be to remain classified as a small-business concern. In general, the SBA definition of a small business differs depending on industry. The SBA, for most industries, defines a "small business" either in terms of the average number of employees over the past 12 months, or average annual receipts over the past three years.[31]

However, while the Division was able to classify many businesses for purposes of this analysis, approximately 49.6 percent of member organizations could not be classified. This was because of missing or inaccurate data, or because the total number of employees was not available outside of those reporting income in the State of Rhode Island.

(Thus, for example, for corporations in industries in which the definition of "small business" is based on gross receipts (sales), the Division had sufficient data and was able to apply a classification. However, for corporations in industries in which the definition of "small business" was based on the number of employees, the Division typically had insufficient data and was unable to apply a classification.)



Percentages in table do not add to 100 due to rounding

Nevertheless, for those businesses that the Division was unable to classify, the Division still determined whether the tax due increased, decreased, or was unchanged as a result of Rhode Island's new corporate tax regime.

Overall, of those businesses that the Division was unable to classify, the tax due was unchanged for approximately 83.4 percent, increased for approximately 12.2 percent, and decreased for approximately 4.4 percent.

31 The SBA has a table that includes "size standards" for hundreds of industries. For further information: https://go.usa.gov/xnSQd. To view the SBA's table of small-business size standards effective October 1, 2017: https://go.usa.gov/xnSQG.

Notes

- For purposes of this analysis, an "increase" or "decrease" in tax due refers to the effect of moving from the tax as computed under the old law (2014 tax year) to the tax as computed under the new law (for tax years beginning on or after January 1, 2015).

- As noted above, the Division was able to classify many businesses for purposes of this analysis. However, approximately 49.6 percent of member organizations could not be classified. The following table shows the number of businesses involved in the analysis (including large businesses, small businesses, and those the Division could not classify).

Number of businesses in analysis				
	Tax increase	**No change**	**Tax decrease**	**Total**
Large businesses:	706	3,176	295	**4,177**
Small businesses:	187	9,141	114	**9,442**
Could not evaluate size:	1,633	11,180	590	**13,403**
Total:	**2,526**	**23,497**	**999**	**27,022**

- It should also be noted that, for purposes of this report overall, the Division analyzed a total of 2,012 combined groups. However, for purposes of analyzing the impact of the new law on large businesses versus small businesses, the Division included a much broader universe – by taking into account the total number of member corporations within all of the combined groups. (As a practical matter, it could be argued that few of the member corporations of any given combined group are actually "small businesses" because, by definition, they are part of a combined group.)

- When considering the results in this section by industry group, it is important to note that the median corporation in each of the categories had no change in tax due.

Rhode Island vs. out-of-state corporations

The Division examined how the change from the old law to the new law affected Rhode Island corporations versus out-of-state corporations.

The Division's analysis first looked at the overall impact on out-of-state corporations in the aggregate, and on in-state (Rhode Island) corporations in the aggregate. The Division's calculations showed that both categories of corporations benefited, in the aggregate. However, the greatest benefit was to Rhode Island corporations; non-Rhode Island corporations benefited less.

The Division also analyzed the shift in overall tax burden. It showed that the portion of the overall tax burden shouldered by out-of-state corporations doubled, while the portion of the overall tax burden borne by Rhode Island corporations fell fivefold.

DEFINITION

For purposes of this report, a combined group is considered a Rhode Island group – a "Rhode Island corporation" – if the tax return for the group specified a Rhode Island address, or if the Division's ITS showed a Rhode Island address as the principal address for that group. (Otherwise, the combined group is considered an out-of-state group – an "out-of-state corporation.")

The definition is not ideal. It is possible, for example, that in some instances, an out-of-state group may have used a Rhode Island address for its return.

Nevertheless, the Division believes that this definition is the most appropriate, given the complexities involved in the analysis, and the lack of another reliable method for making the determination. For this report, the terms "Rhode Island corporations" and "Rhode Island combined groups" are sometimes used interchangeably.

Overall effect of tax changes

As a result of the aforementioned examination and calculations for tax year 2015, the Division estimated that out-of-state corporations, in the aggregate, had a tax due of approximately $55.1 million under the new law, compared with the tax due of approximately $34.7 million under the old law.

- In other words, out-of-state corporations, in the aggregate, ended up paying more in Rhode Island tax – approximately $20.4 million, or 59 percent, more.

At the same time, the Division estimated that Rhode Island corporations, in the aggregate, had a tax due of approximately $7.3 million under the new law, compared with tax due of approximately $54.4 million under the old law.

- In other words, Rhode Island corporations, in the aggregate, ended up paying less in Rhode Island tax – approximately $47.2 million, or 87 percent, less.

In dollar terms, the decrease in tax due for Rhode Island corporations more than offset the increase in tax due for out-of-state corporations.

Fiscal impact TY 2015: Out-of-state vs. Rhode Island corporations		
	Out-of-state corps	**Rhode Island corps**
New law*	$ 55,086,805	$ 7,252,893
Old law**	$ 34,714,730	$ 54,416,931
Difference (in dollars)	$ 20,372,075	($ 47,164,038)
Difference (%)	58.7%	-86.7%

* New law includes 7% corporate tax rate, single-factor apportionment (sales), market-based sourcing for the sales factor, and mandatory unitary combined reporting.
** Old law includes 9% corporate tax rate, three-factor apportionment (sales, property, and payroll), cost-of-performance sourcing for the sales factor, and separate-entity (single-entity) reporting.

Shift in tax burden

The Division also looked at the overall tax burden – and how it shifted. For purposes of this analysis, "overall tax burden" simply means the aggregate tax due for non-Rhode Island corporations and Rhode Island corporations together. (It does not take into account taxes paid by others, such as stand-alone C corporations, corporations that are taxed under other chapters of Rhode Island General Laws, partners in partnerships, or others.)

The Division determined that, under the old law (tax year 2014), Rhode Island corporations in the aggregate carried a greater share of the overall tax burden than did out-of-state corporations in the aggregate.

Under the new law (tax year 2015), the burden shifted: out-of-state corporations in the aggregate carried a greater share of the overall tax burden than did Rhode Island corporations in the aggregate.

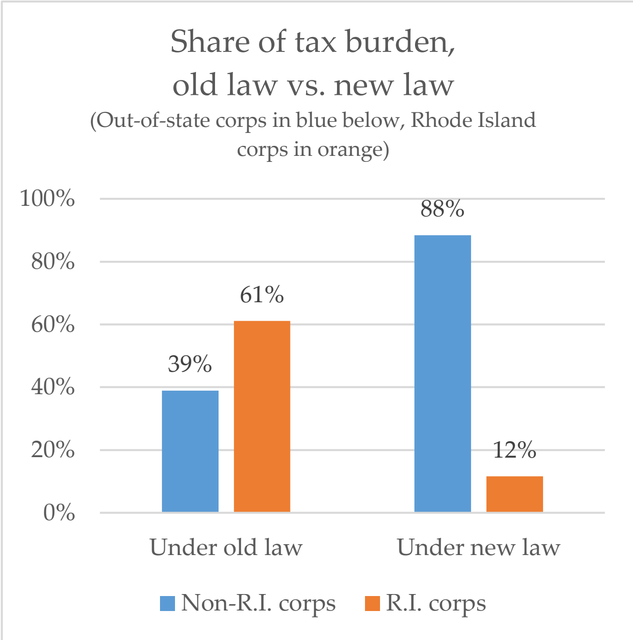
Details are described in the text below and in the table at right.[32]

OLD LAW:

Under the old law, out-of-state corporations shouldered 38.9 percent of the tax burden, while Rhode Island corporations carried 61.1 percent of the burden.

NEW LAW:

Under the new law, out-of-state corporations shouldered 88.4 percent of the tax burden, while Rhode Island corporations carried 11.6 percent of the burden.



[32] Numbers in charts in this section are rounded.

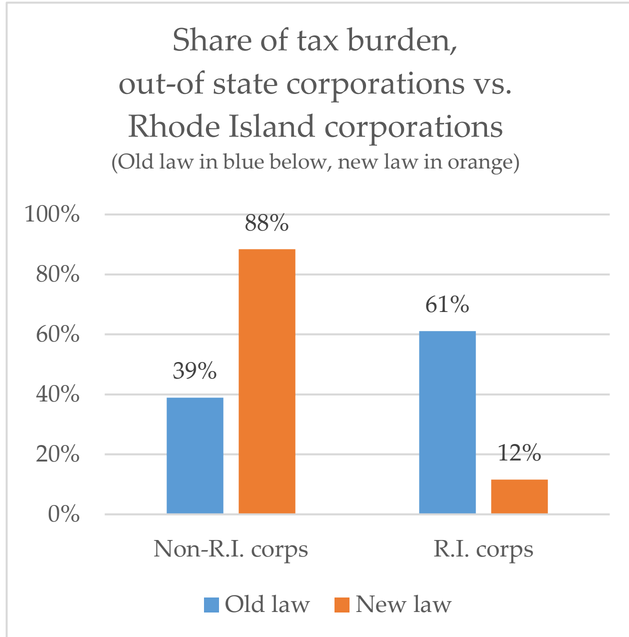
The Division also looked at the same data from a different perspective: For out-of-state corporations, how did the tax burden change from year to year? For Rhode Island corporations, how did the tax burden change from year to year? Details are described in the text and table below.

OUT-OF-STATE CORPORATIONS:

- Out-of-state corporations shouldered 38.9 percent of the burden under the old law.
- Out-of-state corporations shouldered 88.4 percent of the burden under the new law

RHODE ISLAND CORPORATIONS:

- Rhode Island corporations shouldered 61.1 percent of the burden under the old law.
- Rhode Island corporations shouldered 11.6 percent of the burden under the new law.



Reasons for shift

The Division believes that the shift in the tax burden can be explained, at least in part, by two key changes: the switch to combined reporting, and the change in the basic apportionment formula, both of which took effect for tax years beginning on or after January 1, 2015.

Under the law in effect for tax year 2014, a C corporation typically filed its Rhode Island corporate income tax return as a single entity, a separate entity, without regard to other members of its group. Under combined reporting, in effect for 2015 and later tax years, that same C corporation must file a combined report, taking into account the income of all of the members of its group (assuming that it is part of a combined group engaged in a unitary business).

Put another way, under combined reporting, all of the members of the group are treated as if they are one, single company; all of the income of all of the members is combined into a single pool of taxable income. A formula is then used to apportion the amount of the combined income for Rhode Island tax purposes. In other words, there is a larger pool of income available to tax. As the next section of this report shows, combined reporting alone had the following impact: for out-of-state groups, an increase in the aggregate of approximately $37 million in Rhode Island tax due, but for Rhode Island groups, an increase of approximately $804,000 in Rhode Island tax due.

Another key factor was the shift from three-factor apportionment to single-sales-factor apportionment. As described elsewhere in this report, three-factor apportionment in general places a greater burden on Rhode Island businesses because of the three-factor formula's reliance on payroll and property (in addition to sales); Rhode Island businesses typically have more in-state property and in-state payroll (relative to their size) than do out-of-state corporations. The shift to a single factor for apportionment purposes – sales – levels the playing field, in a sense, because the distorting factors of payroll and property are no longer taken into account.

The shift to combined reporting, and to single-sales-factor apportionment, were not the only elements that impacted out-of-state groups and in-state groups. However, they did have the biggest impacts with respect to shifting the Rhode Island tax burden.

The following table shows the shift in tax burden, in detail, for tax year 2015 compared with tax year 2014.

Fiscal impact TY 2015: Out-of-state vs. Rhode Island corporations		
Combined tax due under new law* for non-R.I. and R.I. corps: $ 62,339,698		
	Out-of-state corps	**Rhode Island corps**
Portion of combined tax due, in dollars:	$ 55,086,805	$ 7,252,893
Portion of combined tax due, in %	88.4%	11.6%
Combined tax due under old law* for non-R.I. and R.I. corps: $ 89,131,661		
	Out-of-state corps	**Rhode Island corps**
Portion of combined tax due, in dollars:	$ 34,714,730	$ 54,416,931
Portion of combined tax due, in %	38.9%	61.1%

* "New law" includes 7% corporate tax rate, single-factor apportionment (sales), market-based sourcing for the sales factor, and mandatory unitary combined reporting.
** "Old law" includes 9 percent corporate tax rate, three-factor apportionment (sales, property, and payroll), cost-of-performance sourcing for the sales factor, and single-entity (also known as separate-entity) reporting.

Observation

The Division's analysis shows that, under the old law overall, Rhode Island relied far more heavily on Rhode Island corporations than on out-of-state corporations for tax purposes. Under the new law, the tax burden was shifted so that Rhode Island corporations had far less in tax due, in the aggregate, while out-of-state corporations had far more in tax due, in the aggregate.

The Division's analysis also shows that the package of corporate tax changes under the new law resulted in a net reduction in aggregate tax due overall, but that was partly the result of the significant reduction in tax due in the aggregate for Rhode Island corporations. (These results are in the aggregate. A particular corporation's results may be different, depending on its circumstances.)

Rhode Island vs. out-of-state, by law change

The Division examined returns, and performed calculations, to determine the effect that each of the four key changes in corporate tax law – reduction in tax rate, change in apportionment formula, change in sourcing, and change in reporting method – had, holding all other factors constant.

Tax rate reduction

In the aggregate, out-of-state corporations and Rhode Island corporations benefited from the reduction in the corporate tax rate (from 9 percent for tax year 2014 to 7 percent for 2015 and later tax years).

However, the tax rate reduction delivered the greatest benefit, in absolute terms, for out-of-state corporations (which, as shown earlier, shouldered by far a greater tax burden overall than did Rhode Island corporations). In the aggregate, out-of-state corporations saw a reduction in tax due of approximately $12.3 million, while Rhode Island corporations saw a reduction in tax due of approximately $7.9 million.

Change in apportionment formula

In the aggregate, out-of-state corporations and Rhode Island corporations benefited from the change in the apportionment formula (from three-factor apportionment for tax year 2014 to single-sales-factor apportionment for 2015 and later tax years).

Rhode Island corporations saw most of the benefit, both in relative and in absolute terms, from the change from three-factor apportionment under the old law to single-sales-factor apportionment under the new law: They ended up with a reduction in tax due of approximately $40.4 million. Out-of-state corporations saw a reduction in tax due of approximately $6.7 million.

Change in sourcing method

Rhode Island corporations and out-of-state corporations, on average, did not benefit from the change in the sourcing method for sales for apportionment purposes (from cost-of-performance under the old law, to market-based sourcing under the new law).

In the aggregate, out-of-state corporations had an increase in tax due of approximately $1.4 million, while Rhode Island corporations had an increase in tax due of approximately $336,000.

Change in reporting method

Rhode Island corporations and out-of-state corporations, on average, did not benefit from the change from single-entity reporting (under the old law) to combined reporting (under the new law).

However, out-of-state corporations ended up with a greater tax due as a result of the change: In the aggregate, out-of-state corporations had an increase in tax due of approximately $36.9 million, while Rhode Island corporations had an increase in tax due of approximately $804,000.

Fiscal impact of four key changes in tax policy:* Out-of-state vs. Rhode Island corporations		
Tax increase (or decrease) due to specific changes to corporate tax regime		
	Out-of-state corps	**Rhode Island corps**
Lowering of corporate tax rate	($ 12,312,101)	($ 7,969,735)
Change in apportionment formula:	($ 6,771,568)	($ 40,407,426)
Change in sourcing method:	$ 1,387,048	$ 335,835
Change in reporting method:	$ 36,967,365	$ 803,752
* Prior law included 9 percent corporate tax rate, three-factor apportionment (sales, property, and payroll), cost-of-performance sourcing, and single-entity reporting. New law includes 7% corporate tax rate, single-factor apportionment (sales), market-based sourcing, and combined reporting.		

Broader base

In summary, Rhode Island corporations, in the aggregate, saw a reduction in tax due as a result of two of the four key changes in corporate tax policy: the lowering of the tax rate, and, especially, the change to the apportionment formula. Rhode Island corporations, in the aggregate, saw a comparatively modest increase in tax due as a result of the change in the sourcing method and the switch to combined reporting.

Out-of-state corporations, in the aggregate, also saw a reduction in tax due from the lowering of the tax rate and the change in the apportionment formula. Out-of-state corporations, in the aggregate, saw an increase in their tax burden due to the change in the sourcing method and, especially, the switch to combined reporting.

From a broader perspective, however, the Division's analysis shows that Rhode Island's adoption of mandatory unitary combined reporting led to a broadening of the tax base. The Division's overall analysis of the four key changes to Rhode Island's corporate tax structure shows that the move from single-entity, or separate-entity, reporting (which was in effect for the 2014 tax year) to combined reporting (which applies for 2015 and later tax years) resulted in an increase in tax due of approximately $37.8 million.[33]

[33] For further details, please see Section 5 of this report.

Additional evidence of this can be seen in the Division's analysis of the effect of the four key corporate tax changes on Rhode Island combined groups versus out-of-state combined groups. That analysis showed that only two of the corporate tax changes – the shift to combined reporting, and the shift to market-based sourcing – led to an increase in tax due for both in-state and out-of-state combined groups. However, of those two key factors, the shift to combined reporting generated an increase in tax due of approximately $804,000 for in-state combined groups, but an increase in tax due of nearly $37 million in tax due for out-of-state combined groups.

Combined reporting broadened Rhode Island's corporate tax base because, in effect, it was a recognition that a corporation doing business in Rhode Island was not a stand-alone entity if it was, in reality, part of a combined group engaged in a unitary business.

Thus, the corporation doing business in Rhode Island could no longer file its Rhode Island corporate income tax return as if it were a business in isolation; its return, under combined reporting, had to take into account the income of other corporations within the same broader business grouping, including those based in other states.

Viewed from a different standpoint, the net decrease in overall tax due mentioned previously was not the result of combined reporting. Rather, it was the result of the impact of other corporate tax changes, including the 22.22 percent reduction in the corporate tax rate, and the change in the basic apportionment formula.

Apportionment observation

Although the change in the fundamental apportionment formula (from three-factor apportionment to single-sales-factor apportionment) resulted in a decrease in tax due for out-of-state combined groups as well as Rhode Island combined groups, the decrease was pronounced for Rhode Island combined groups: A decrease in tax due of approximately $40.4 million, compared with a decrease of $6.8 million for out-of-state combined groups.

A chief reason is that, for Rhode Island tax purposes, the three-factor apportionment – which takes into account a corporation's property, payroll, and sales – is typically more burdensome to Rhode Island corporations. That is because a Rhode Island corporation typically has a greater portion of its property and payroll in Rhode Island than does an out-of-state corporation doing business in Rhode Island.

For example, suppose that Able Corp. has 50 percent of its payroll in Rhode Island, 50 percent of its property in Rhode Island, and 1 percent of its sales in Rhode Island. It has $10 million in taxable income. Under the old law, 34 percent of its income, or $3.4 million in this example, would be taxable to Rhode Island. Under single-sales-factor apportionment, however, only 1 percent of its income, or $100,000 in this example, would be taxable to Rhode Island (because the new law counts only sales for apportionment purposes, and in this example, only 1 percent of Able Corp.'s sales are in Rhode Island – so only 1 percent of its income is taxable to Rhode Island).

Frame of reference

In Section 7 of this report, the Division of Taxation estimated that because of the changes in tax law enacted in 2014, out-of-state corporations, in the aggregate, ended up paying approximately $20.4 million, or 59 percent, more in Rhode Island tax, while Rhode Island corporations, in the aggregate, ended up paying approximately $47.2 million, or 87 percent, less, in Rhode Island tax.

In this section of the report, the Division shows the impact of each of the four key changes in tax law. However, a sum of the results of each of the four key changes in this section of the report does not equal the aggregate totals listed in Section 7.

The reason is that the dollar impact for each of the four changes listed in this section of the report is, in reality, an average – of many different scenarios. It is an average because none of the four key changes could be analyzed on its own, in isolation. For example, in the 2014 legislation as enacted, there was a tax rate reduction -- but there was also a change in the apportionment formula, a change in the sourcing method, and a change in the reporting method.

Thus, to determine the impact of just the tax rate reduction alone, the Division also had to take into account the three other elements (apportionment formula, sourcing method, and reporting method) under both the old law and the new law. The Division then had to compute an average for each.

Thus, for example, the impact listed in the table in this section of the report for the tax rate reduction is, in reality, the average aggregate impact of all of the computations for each of the various scenarios mentioned above. It would be misleading to present the numbers in the table as anything but average aggregate numbers. Therefore, they cannot in fairness be summed and compared with the overall impact numbers listed in Section 7 of this report. In other words, because these are averages, they do not sum to the whole figures reported in Section 7 of this report.

Note

It is important to keep in mind that this report does not focus on any particular corporation or on any particular combined group. Rather, the report takes a big-picture view, analyzing the impact of corporate tax changes on combined groups in the aggregate. Similarly, this report focuses on out-of-state corporations (combined groups) in the aggregate, and on Rhode Island corporations (combined groups) in the aggregate.

Therefore, although the results of the Division's analysis show that Rhode Island corporations (combined groups) benefited in the aggregate from the corporate tax changes enacted in 2014, for tax years beginning on or after January 1, 2015, it is not necessarily the case that any particular Rhode Island corporation benefited. Whether an individual Rhode Island corporation or Rhode Island combined group saw an increase or decrease in its tax due depends on a variety of factors.

SECTION 10

Additional points

The Division believes that, for a variety of reasons, the results of this report cannot be compared to the Division's March 2014 study on combined reporting.

A key reason is that, for the 2014 study, the Division was required by statute to focus on the impact of a potential switch to combined reporting and single-sales-factor apportionment, using data from *pro forma* combined reporting returns for two prior tax years (2011 and 2012).

However, for purposes of its 2014 study, the Division was not required by statute to examine the potential impact of a 22 percent reduction in the corporate tax rate or a move to market-based sourcing for the sales factor in apportionment.

Ultimately, legislation was enacted in 2014 (for tax years beginning on or after January 1, 2015) that included all four features:

- Combined reporting (included in the 2014 study)
- Single-sales-factor apportionment (included in the 2014 study)
- Reduction in the tax rate (not included in the 2014 study)
- Market-based sourcing (not included in the 2014 study)

Furthermore, whereas the data for the 2014 study was drawn from two years' worth of tax returns, data for the current report was drawn from one year's worth of tax returns (although, as previously noted, the Division then recalculated data from tax year 2015 returns to determine the effect of the new law compared with the old law).

Unknowns

There are a number of factors – "unknowns" – that are outside the scope of this report, but which the Division nevertheless believes are worthy of consideration.

For example, a number of multi-national corporations in recent years engaged in what is known as tax inversions, or corporate inversions. In such cases, a U.S. corporation typically changes its legal domicile from the U.S. to another country – typically a lower-tax country – while maintaining at least some part of its operations in the U.S.

The effect of corporate tax inversions on Rhode Island corporate tax revenue is difficult to gauge, particularly those which took effect at approximately the same time that Rhode Island was implementing sweeping changes in its corporate tax structure. It is also difficult to determine what impact U.S. Treasury regulations, and other moves by the federal government, including the federal tax reform enacted in December 2017, have had or will have on corporate tax inversions.

Franchise tax

As previously noted, the sweeping changes to Rhode Island's corporate tax structure enacted in 2014 (for tax years beginning on or after January 1, 2015) included multiple factors, including repeal of the franchise tax. This report focused chiefly on four key changes to the corporate tax structure – including the reduction in the tax rate, and the switch to combined reporting, single-sales-factor apportionment, and market-based sourcing.

Due to data limitations, the Division was unable to determine for this report, with any degree of confidence, the fiscal or policy ramifications of the repeal of the franchise tax.

Apportionment

It should be noted that, although Rhode Island changed its apportionment formula and sourcing method for the sales factor, those two changes apply only to C corporations (and to entities treated as C corporations for federal tax purposes).

However, three-factor apportionment and the cost-of-performance sourcing method continue to apply for other entities.

Thus, readers should take note that, broadly speaking, Rhode Island continues to maintain two separate apportionment regimes. Which one applies depends upon the entity involved, as the following table shows.

Rhode Island apportionment – tax years beginning on or after January 1, 2015	
C corporations must use the following:	*Taxpayers other than C corporations must use the following:*
Single-sales-factor apportionment	Three-factor apportionment
Market-based sourcing	Cost-of-performance sourcing

"C corporations" means entities treated as C corporations for federal income tax purposes. Single-sales-factor apportionment and market-based sourcing apply to stand-alone C corporations as well as to C corporations that are part of combined groups for combined reporting purposes, or that are part of affiliated groups that file consolidated returns in lieu of combined reports. "Taxpayers other than C corporations" include, but are not limited to, businesses treated as pass-through entities for federal tax purposes. "Three-factor apportionment" typically takes into account property, payroll, and sales – each equally weighted.

In certain cases, a taxpayer may use a special apportionment formula available by statute. Also, when a dispute arises between the Tax Administrator and a taxpayer with respect to the method of apportionment applied, both the taxpayer and the Tax Administrator are authorized by statute to initiate an appeals process through an independent arbitrator.

For additional information on apportionment, see Division of Taxation Regulation 15-04, "Business Corporation Tax: Apportionment of Net Income."

Methodology

What were the principles or rules that guided the Division of Taxation in its study of the data underlying this report? What specific methods, practices, and procedures did the Division employ to in order to collect, analyze, and interpret the data? In other words, what "methodology" did the Division use?[34]

The answer can be found in nearly every section of this report, beginning with the "Disclaimer and Notes" section. In drafting this report, the Division believed that it was important to provide information on principles, practices, and procedures throughout the report, as soon as each issue arose, rather than segregate (or isolate) such information in a separate section on methodology.

[34] Information for this paragraph was adapted from the definition of "methodology" in Black's Law Dictionary.

Appendix A

How tax is computed

Following are the basic steps that a combined group takes in computing its Rhode Island corporate income tax, as prescribed under Rhode Island General Laws Chapter 44-11 ("Business Corporation Tax"):

Step 1. Combine the federal taxable income of all members of the combined group.

Step 2. Combine all deductions of all members of the combined group, including net operating losses (NOLs) in accordance with regulation.

Step 3. Combine all the additions of all members of the combined group.

Step. 4. Net the combined additions and the combined deductions against the combined federal taxable income of all members of the combined group. The result is the adjusted taxable income of the combined group for Rhode Island corporate income tax purposes.

Step 5. Combine the receipts of all members of the combined group using the Finnigan method. Calculate the apportionment ratio for the combined group. Use, as the numerator, all Rhode Island receipts – regardless of whether a group member has nexus in Rhode Island. Use, as the denominator, everywhere receipts. (Divide the numerator by the denominator to arrive at an apportionment ratio.)

Step. 6. Compute the apportioned Rhode Island taxable income of the combined group by multiplying adjusted taxable income by the combined apportionment ratio.

Step 7. Compute and combine Rhode Island adjustments, including research and development adjustments, pollution control and hazardous waste adjustment, and capital investment deduction. Subtract total of such adjustments from apportioned Rhode Island taxable income computed in Step 6 to arrive at Rhode Island adjusted taxable income.

Step 8. Multiply result from Step 7 by applicable tax rate (currently 7 percent).

Step 9. Calculate allowable credits in accordance with regulation.

Step 10. Subtract result in Step 9 (above) from the result in Step 8 (above). This is the tax due under combined reporting, before annual corporate minimum tax. (See Step 11.)

Step. 11. For purposes of the minimum tax, determine the number of members of the combined group that have Rhode Island nexus. Multiply that number by the amount of the annual corporate minimum tax under Rhode Island General Laws § 44-11-2(e). Compare that sum to the amount of net tax liability (after credits) from Step 10. Pay whichever amount is higher.

Appendix B

Minimum tax

A minimum tax continues to apply under Rhode Island General Laws § 44-11-2(e). It also applies for purposes of combined reporting. However, the minimum tax has also been reduced – by a total of 20 percent.[35]

- For tax year 2015, the minimum tax was $500.
- For tax year 2016, the minimum tax dropped to $450.
- For 2017 and later years, the minimum tax dropped again, to $400.

For combined reporting purposes, the combined group pays either the tax due based on the amount of its net income apportioned to Rhode Island, using the applicable rate, or the minimum tax, whichever amount is higher.

To compute the minimum tax, the combined group must determine the number of its members that have nexus in Rhode Island and multiply that number by the amount of the minimum tax as listed in Rhode Island General Laws § 44-11-2(e). The sum must be compared to the actual tax due for the entire combined group. The combined group must pay whichever amount is higher.

Rhode Island corporate minimum tax		
2015	**2016**	**2017**
$500	$450	$400
Note: $400 minimum tax applies for 2017 and later tax years. Rhode Island General Laws § 44-11-2(e).		

[35] The corporate tax rate was $500 for 2015. However, two separate bills were later enacted that reduced the corporate minimum tax: to $450 for 2016, and to $400 for 2017 and later tax years.

Appendix C

On estimating the effect of sourcing

As previously noted, the legislation as enacted in 2014 required that the market-based sourcing method be used for the sales factor by C corporations for tax years beginning on or after January 1, 2015.

Formerly, the cost-of-performance method had been used. Under that method, receipts from transactions (other than sales of tangible personal property) were assigned to the state in which the income-producing activity was actually performed. Under the market-based sourcing method, receipts from transactions (other than sales of tangible personal property) are sourced to the market state – that is, to the state where the recipient of the service and/or intangible personal property receives benefit from the service and/or intangible personal property.

This appendix describes how the Division went about estimating the effect on sales from the change from cost-of-performance sourcing to market-based sourcing. Because that is not something that can be directly measured within a single tax year, the Division had to provide a best-available estimate based on the change in a C corporation's Rhode Island receipts (sales) from the 2014 tax year to the 2015 tax year within the identifiably same corporate entity (based on federal EINs).

To do that, the Division had to make use of unaudited electronic filings for the 2014 tax year because they had the most complete data. (The Division's old mainframe computer system did not capture a sufficient amount of information for each entity.) Thus, the Division decided to perform its analysis using information by industry group. The Division then used the results to "back in" to its analysis of 2015 tax year data, using Schedule CRS's line 17 ("Total Rhode Island Receipts," or sales), as adjusted by the percentage change by industry.

By NAICS code

For purposes of this analysis, the Division examined the effect of the change in sourcing method for various categories of businesses based on the North American Industry Classification System, also known as NAICS.[36] The NAICS is the standard used by federal statistical agencies in classifying business establishments for the purpose of collecting, analyzing, and publishing statistical data related to the U.S. business economy. In general, corporations are required to list their principal business activities and their associated codes (based on the NAICS system) on their federal tax returns.

[36] The NAICS was developed under the auspices of the U.S. Office of Management and Budget, and adopted in 1997 to replace the Standard Industrial Classification (SIC) system. In general, the codes from both systems identify a firm's primary business activity.

To help ensure that the Division's report would be filed in as complete and timely a fashion as possible, the Division designed its corporate income tax form, Form RI-1120C, in such a way so that a code for each member of a combined group would be prominently displayed. The Division also worked with providers of computerized tax-preparation software programs to require the inclusion, in a prominent place on returns, of a code for each member of a combined group.

For purposes of this analysis, the Division computed the change in Rhode Island receipts (sales) for certain industries by NAICS code. The Division focused on changes in total Rhode Island receipts by industry for groups with a sample size of 10 or more.

Where the sample size was too small, the Division used the statewide median value across all industries. Also in cases where the sample size was too small, the Division deliberately did not report actual results out of a concern that individual taxpayers could be identified – which would have been in potential violation of Rhode Island statutes that safeguard the confidentiality of individual taxpayer information.

As a hypothetical example, if a particular category is reserved for the manufacture of Norwegian widgets, and only one combined group was engaged in that particular business, confidential taxpayer information of that particular combined group might have been inadvertently – and illegally – disclosed. Following the same principle, the Division used only the first two digits of each NAICS code for purposes of this analysis. The following table shows the overall results of the Division's analysis. It shows the change in their reported Rhode Island gross receipts (sales).

Change in sourcing method: Increase/decrease in Rhode Island receipts

Industry	NAICS code	Change in R.I. receipts
Administrative, support, and waste management	56	49.1%
Health care and social assistance	62	28.1%
Professional, scientific, and technical services	54	12.9%
Finance and insurance	52	11.9%
Transportation and warehousing	48	10.1%
Management of companies and enterprises	55	9.0%
Real estate and rental and leasing	53	8.6%
Accommodation and food services	72	7.6%
Information	51	6.8%
All others (various)	Various	5.5%
Construction	23	4.7%
Wholesale trade	42	3.7%
Manufacturing (food and clothing)	31	3.0%
Retail trade (non-store retailers)	45	1.4%
Retail trade (store retailers)	44	1.1%
Manufacturing (heavy industry, metals, etc.)	33	0.0%
Manufacturing (chemical manufacturing)	32	-10.10%

Industries are listed in order, based on change in receipts (starting with greatest percentage increase). Store retailers operate fixed point-of-sale locations, located and designed to attract a high volume of walk-in customers. Non-store retailers, like store retailers, are organized to serve the general public, but their retailing methods differ: They may reach customers and market merchandise with methods such as the broadcasting of "infomercials", the broadcasting and publishing of direct-response advertising, the publishing of paper and electronic catalogs, or other means.

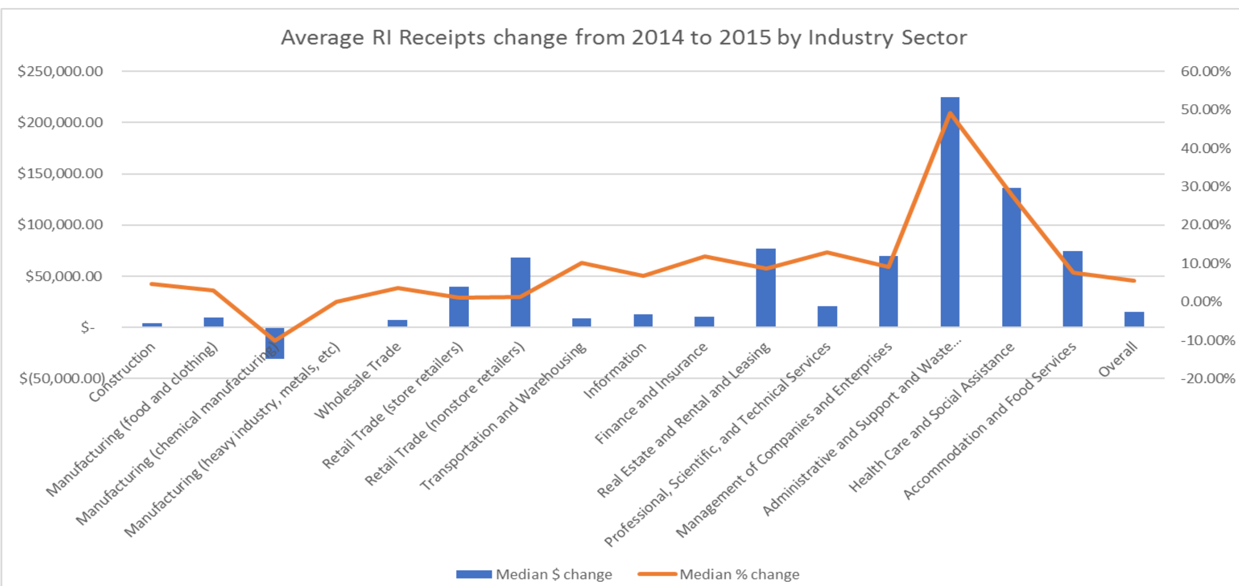
Notes

For purposes of the analysis, the results reflect the median percent change in receipts attributable to Rhode Island – so half of the individual corporations in any given industry were above the median amount of Rhode Island receipts, and half were below. (The Division did not report averages because one or more large combined groups in any given industry may have had so much in total receipts, they easily exceeded all others in the same industry, which would have led to a distorted result.)

Also for purposes of this analysis, the Division relied solely on returns filed electronically for tax year 2014, because e-filed returns provided the most complete data available for analysis. There can be no assurance that the results are representative of the population as a whole. (For example, the results do not take into account the majority of Rhode Island's largest corporations – because they typically file paper returns.)

Average change in receipts

The following table shows the average change in Rhode Island sales (gross receipts) from tax year 2014 to tax year 2015, by industry sector, for corporations that were the same in each year, based on their federal EINs, between 2014 and 2015.



Observation

As shown elsewhere in this report, the corporate tax base was broadened as a result of the change in sourcing method that took effect for tax years beginning on or after January 1, 2015: The switch to market-based sourcing resulted in an aggregate increase in tax due for Rhode Island combined groups as well as for out-of-state combined groups (although the increase for out-of-state combined groups was greatest.)

The broadening was especially the case for service industries. For example, the five industries with double-digit increases in receipts attributable to Rhode Island were:

- Administrative, support, waste management, and remediation services
- Health care and social assistance
- Professional, scientific, and technical services
- Finance and insurance
- Transportation and warehousing

Nevertheless, it should be noted that the change in taxes due between the old law (tax year 2014) and the new law (tax year 2015) for the median corporation for each NAICS industry group was zero. This implies that industry was not a major factor regarding taxes due.

It should also be noted that the increase in Rhode Island receipts from 2014 to 2015 is attributable to a variety of factors, only one of which involves the adoption of a new method for sourcing sales for apportionment purposes. Inflation and other microeconomic factors need be considered, too.[37]

[37] Rhode Island's total gross domestic product grew by 3.58 percent from 2014 to 2015. (Source: U.S. Bureau of Economic Analysis, Total Gross Domestic Product for Rhode Island [RINGSP], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/RINGSP, February 22, 2018.)

Appendix D

Form RI-1120C

State of Rhode Island and Providence Plantations

2015 RI-1120C

Business Corporation Tax Return

15110188880101

- Initial Return
- Short Year
- Final Return
- Address Change
- Amended Return
- Combined Return
- 1120F

Name			Federal employer identification number
Address 1			Gross Receipts
Address 2			Depreciable Assets
City, town or post office	State	ZIP code	Total Assets
E-mail address	NAICS code		RI Secretary of State ID number

Year end: Calendar Year: 01/01/2015 through 12/31/2015

Fiscal Year: beginning MM/DD/2015 through MM/DD/2016

Schedule A - Computation of Tax

1	Federal taxable income (see instructions)	1	
3	Total Deductions from page 3, Schedule B, line 2h	3	
5	Total Additions from page 3, Schedule C, line 4e	5	
6	Adjusted taxable income. Line 1 less line 3 plus line 5	6	
7	Rhode Island Apportionment Ratio from Schedule G, line 2. Carry to six (6) decimal places	7	
8	Apportioned Rhode Island taxable income. Multiply line 6 times line 7	8	
9	Research and development adjustments (see instructions, attach schedule	9	
10 a	Pollution control and hazardous waste adjustment (see instructions)	10a	
b	Capital investment deduction (see instructions)	10b	
11	Total adjustments. Add lines 9, 10a and 10b	11	
12	Rhode Island adjusted taxable income. Subtract line 11 from line 8	12	
13	Rhode Island income tax. Multiply line 12 times 7% (0.07)	13	
14	Rhode Island Credits from Schedule B-CR 2015 - Business Credit Schedule, line 21	14	
15	Tax. Subtract line 14 from line 13, but not less than the minimum tax of $500.00	15	
16 a	Recapture of credits	16a	
b	Jobs Growth Tax	16b	
17	Total tax due. Add lines 15, 16a and 16b	17	

Check if a Jobs Growth Tax is being reported on line 16b.

(Form RI-1120C, page 2)

State of Rhode Island and Providence Plantations
2015 RI-1120C
Business Corporation Tax Return

15110188880102

Name	Federal employer identification number

17 Total tax due from page 1, line 17		17	
18 Payments made on 2015 declaration of estimated tax	18		
19 a Other payments	19a		
b Rhode Island pass-through withholding. Attach RI-1099PT(s)	19b		
20 a TOTAL PAYMENTS. Add lines 18, 19a and 19b		20a	
b Previously issued refunds (if filing an amended return)		20b	
c NET PAYMENTS. Subtract line 20b from line 20a		20c	
21 Net tax due. Subtract line 20c from line 17		21	
22 a Late payment interest	22a		
b Late payment penalty	22b		
c Underestimating interest	22c		
d Late filing penalty	22d		
e Total interest and penalty amounts. Add lines 22a, 22b, 22c and 22d		22e	
23 Total due with return. Add lines 21 and 22e (Please use Form RI-1120V)		23	
24 Overpayment. Subtract lines 17 and 22e from line 20c		24	
25 Amount of overpayment to be credited to 2016		25	
26 Amount of overpayment to be refunded. Subtract line 25 from line 24		26	

Under penalties of perjury, I declare that I have examined this return and accompanying schedules and statements, and to the best of my knowledge and belief, it is true, accurate and complete. Declaration of preparer (other than taxpayer) is based on all information of which preparer has any knowledge.

Authorized officer signature	Print name		Date	Telephone number
Paid preparer signature	Print name		Date	Telephone number
Paid preparer address	City, town or post office	State	ZIP Code	PTIN

May the Division of Taxation contact your preparer? YES

(Form RI-1120C, page 3)

State of Rhode Island and Providence Plantations

2015 RI-1120C

Business Corporation Tax Return

15110188880103

Name	Federal employer identification number

Schedule B - Deductions to Federal Taxable Income

2 a Net operating loss deduction (see instructions - attach schedule)	2a		
b Special deductions	2b		
c Exempt dividends and interest from page 4, Schedule E, line 10	2c		
d Foreign dividend gross-up (s78) US 1120, Schedule C, line 15	2d		
e Bonus deprecation and Section 179 expense adjustment	2e		
f Discharge of business indebtedness claimed as income on Federal return and previously included as RI income under American Recovery and Reinvestment Act of 2009 under RIGL §44-66-1	2f		
g Modification for Tax Incentives for Employers under RIGL §44-55-4.1. Attach Form RI-107	2g		
h **TOTAL DEDUCTIONS**. Add lines 2a through 2g. Enter here and on RI-1120C, page 1, line 3	2h		

Schedule C - Additions to Federal Taxable Income

4 a Interest (see instructions)	4a		
b Rhode Island corporate taxes (see instructions)	4b		
c Bonus depreciation	4c		
d Domestic Production Activity addback	4d		
e **TOTAL ADDITIONS**. Add lines 4a through 4d. Enter here and on RI-1120C, page 1, line 5	4e		

Schedule D - General Information

14 a Location of principal place of business in Rhode Island	
b Location of corporation's books and records	
c List states to which you are liable for income or excise taxes for the taxable year	
d State and date of incorporation	
e President	Treasurer

f Salaries and wages paid or incurred in Rhode Island	14f		
g Salaries and wages paid or incurred everywhere	14g		

(Form RI-1120C, page 4)

State of Rhode Island and Providence Plantations
2015 RI-1120C
Business Corporation Tax Return

15110188880104

Schedule E - Exempt Dividends and Interest

1	Dividends received from shares of stock of any payer liable for RI taxes as outlined in Chapters 11, 13, & 14 (attach schedule)	1	
2	Amount of such dividends included in Special Deductions, Schedule B, line 2b	2	
3	Balance of Exempt Dividends. Line 1 less line 2	3	
	Foreign Dividends included on line 13, 14 & 17 Schedule C, US 1120		
4	More than 20% owned ______ X 80%	4	
5	Less than 20% owned ______ X 70%	5	
6	100% owned ______ X 100%	6	
7	Interest on obligations of public service corporations liable for Rhode Island Gross Earnings Tax	7	
8	Interest on certain obligations of the US (attach schedule)	8	
9	Interest on obligations of US possessions and other interest exempt under Rhode Island Law (attach schedule)	9	
10	Total. Add lines 3 through 9. Enter here and on page 3, Schedule B, line 2c	10	

Schedule F - Federal Taxable Income (US 1120, page 1, line 28)

Enter amount for year that ended:	2015	2014	2013	2012	2011

Schedule G - Apportionment

☐ Check if utilizing an alternative allocation apportionment calculation allowed under 44-11-14.1 through 44-11-14.6

			Column A Rhode Island	Column B Everywhere
1 a Gross receipts	Rhode Island Sales	1a		
	Sales Under 44-11-14(a)(2)(i)(B)			
b Dividends		1b		
c Interest		1c		
d Rents		1d		
e Royalties		1e		
f Capital gains		1f		
g Ordinary income		1g		
h Other income		1h		
i Income exempt from federal taxation		1i		
j Total. Add lines 1a, 1b, 1c, 1d, 1e, 1f, 1g, 1h and 1i		1j		

2 Ratio in Rhode Island, line 1j, Column A divided by line 1j, Column B. Calculate to six (6) decimal places. Enter here and on page 1, Schedule A, line 7 — 2

Appendix E

Schedule CRS

State of Rhode Island and Providence Plantations

2015 Schedule CRS for RI-1120C

Combined Reporting Schedule

15113088880101

Designated agent name	Federal Consolidated Election	Federal employer identification number
	☐	-
Member name	**NAICS code**	**Federal employer identification number**
		-

Combined Reporting Schedule

1	Federal taxable income	
	Deductions to Federal Taxable Income	
2	2015 NOL deduction	
3	NOL carryforward	
4	Special deductions	
5	Exempt dividends and interest	
6	Foreign dividend gross-up (s78) US 1120, Schedule C, line 15	
7	Bonus depreciation and Section 179 expense adjustment	
8	Discharge of business indebtedness claimed as income on Federal return and previously included as RI income under ARRA of 2009 under RIGL §44-66-1	
9	Modification for Tax Incentives for Employers - RIGL §44-55-4.1.	
10	**TOTAL DEDUCTIONS. ADD LINES 2 THROUGH 9**	
	Additions to Federal Taxable Income	
11	Interest	
12	Rhode Island corporate taxes	
13	Bonus depreciation	
14	Domestic Production Activity addback	
15	**TOTAL ADDITIONS. ADD LINES 11 THROUGH 14**	
	Rhode Island Adjusted Taxable Income	
16	Adjusted taxable income. Line 1 less line 10 plus line 15	
17	Total Rhode Island Receipts	
18	Total Everywhere Receipts	
19	Receipts apportionment ratio. Divide line 17 by line 18	
20	Apportioned RI taxable income. Multiply line 16 by 19	
21	R & D adjustments	
22	Pollution control/hazard waste adjustment	
23	Capital investment deduction	
24	**TOTAL ADJUSTMENTS ADD LINES 21, 22 and 23**	
25	Rhode Island adjusted taxable income Subtract line 24 from line 20	
	Tax Calculation	
26	Rhode Island tax - 7%. (Line 25 x 0.07)	
27	If nexus, check this box:	☐
28	If nexus, enter the minimum tax of $500. Otherwise, enter $0	
29	Greater of line 26 or line 28	
30	RI Credits used from carryforward of credit generated prior to 1/1/2015	
31	RI Credits being used from credit generated on or after 1/1/2015	
32	------ Reserved for 2016 ------	
33	Recapture of credits	
34	Jobs Growth Tax	
35	**TOTAL TAX**	
36	Total Rhode Island Average Net Book Value	
37	Total Everywhere Average Net Book Value	
38	Total Rhode Island Salaries/wages	
39	Total Everywhere Salaries/wages	
40	If utilizing a special apportionment calculation on line 19, check this box:	☐