

Rhode Island's FY 2022 Budget Outlook

**Budget Situation
Stabilized with Federal
Funding, Jump in
Estimated State Revenues**

*The Fifth in a Series on the
Fiscal Impact of COVID-19*

June 2021



RIPEC

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I. Introduction

Governor Daniel J. McKee's submitted his first budget for fiscal year (FY) 2022 only nine days after being sworn in as governor, on March 11, 2021, following Governor Gina M. Raimondo's confirmation as U.S. Secretary of Commerce. Governor McKee's budget does not take account of the enormous federal assistance to state and local governments provided by the American Rescue Plan Act (ARPA), signed into law by President Joe Biden on the same day that Governor McKee's budget was introduced. Governor McKee's budget also did not have the benefit of the very large increase in available state revenues projected by the Revenue Estimating Conference in May 2021.

The state's budget for FY 2022, which begins on July 1, 2021, represents the third annual state budget complicated by the COVID-19 pandemic and its economic fallout. Faced with plummeting revenues, the General Assembly enacted a revised budget for FY 2020 last June that was balanced largely on a \$120 million transfer from the state's rainy day fund and the use of \$97.3 million in federal COVID relief funds.¹ Facing a massive shortfall in revenues and anticipating an additional federal relief package, the Assembly deferred action on a budget for FY 2021, which commenced on July 1, 2020.² While a federal relief package stalled, the budget picture brightened considerably, with a large upward projection of revenues and lower expenditures than expected.³ With the fiscal year nearly half over, on December 18, the General Assembly passed a pared-down, or "skinny," budget for FY 2021, which included a large appropriation for federally-funded COVID response costs, but otherwise contained no significant policy or programmatic changes to current law.⁴

This report analyzes Governor McKee's proposed budget as the latest in this continuum of annual state spending plans reconciling revenue shortfalls resulting from the pandemic and incorporating expenditures of substantial federal resources. In particular, the report focuses on the extent to which the budget utilizes one-time federal funding to pay for ongoing state expenditures, thereby implicating potential structural deficits for future budgets. The report next analyzes the projected increases in available state resources, as determined by the most recent Revenue and Caseload Estimating Conferences, held in May, as well as the expenditures projected in the Office of Management and Budget's (OMB) Third Quarter Report for FY 2021, issued later in May. The report also summarizes the federal resources available to the state under ARPA in the context of the state budget. Finally, the report includes RIPEC observations and recommended policy considerations.

¹ RIPEC, "[Rhode Island's FY 2020 Supplemental Budget: The General Assembly Takes the First Step in Responding to Pandemic Fallout](#)," July 2020.

² By law, when the Assembly does not approve a budget before the beginning of a fiscal year, the state operates under spending allotments to agencies in the same amounts as appropriated in the previous fiscal year. R.I. Gen. Laws [§ 35-3-19](#).

³ RIPEC, "[Rhode Island's FY 2021 Enacted Budget and the Fiscal Challenges Ahead](#)," January 2021.

⁴ R.I. General Assembly, [2020—House Bill 7171 Substitute A](#). The budget was signed by Governor Raimondo on December 21, 2020.

II. Governor McKee's Proposed FY 2022 Budget

In his first budget, Governor McKee proposed a status quo spending plan, largely a continuation of taxing policies and programs of the Raimondo Administration. The FY 2022 budget proposal includes no broad-based tax increases, major new programs, or large program expansions. However, the budget does include some important policy proposals, including new initiatives as well as some of Governor Raimondo's FY 2021 budget proposals, which were almost universally deferred by the General Assembly in enacting the skinny budget in December. While Governor McKee did not have the benefit of utilizing federal assistance under ARPA, his budget takes advantage of previously authorized federal funding to pay for ongoing state expenditures in the current year, mostly through his proposed revised, or supplemental, FY 2021 budget, introduced as separate legislation in conjunction with the FY 2022 appropriations act.

The FY 2021 Supplemental Budget

In his supplemental budget for FY 2021, Governor McKee proposes \$13.75 billion in total spending—over \$1 billion more than the \$12.73 billion authorized in the budget enacted by the Assembly less than three months earlier. However, state general revenue expenditures in the revised budget, at \$3.88 billion, are lower than the \$4.15 billion authorized in the enacted budget.⁵ As a result, the projected surplus for FY 2021 increased by \$253.2 million, from \$12.2 million in the enacted budget to \$265.4 million in the proposed revised budget.⁶

This large reduction in state general revenue expenditures is driven not by reduced spending but by shifting state expenditures to federal funding. The largest shift—totaling \$118 million—results from federal guidance authorizing the Federal Emergency Management Agency (FEMA) to increase federal reimbursement to 100 percent from 75 percent for eligible COVID response expenses, retroactive to January 2020.⁷ The supplemental budget also uses federal funding to pay for COVID response costs in the Department of Health (\$77.6 million), as well as additional ongoing expenses for correctional officers in the Department of Corrections (\$45.4 million), and for personnel in the Department of Public Safety (\$22.1 million).⁸ In addition, the supplemental budget incorporates additional enhanced Federal Medical Assistance Percentage (FMAP) savings (\$34.5 million).⁹

⁵ R.I. OMB, [FY 2022 Budget Proposal, Executive Summary](#).

⁶ R.I. OMB, [FY 2022 Budget Proposal, Executive Summary, Schedule A](#).

⁷ R.I. Senate Fiscal Office, "[Governor's FY 2022 and FY 2021 Supplemental Budget](#)," May 18, 2021. FEMA funding reimburses for costs of eligible emergency protective measures, as defined by FEMA guidance. R.I. OMB, [FY 2022 Budget Proposal, Executive Summary](#).

⁸ Ibid.

⁹ R.I. OMB, [FY 2022 Budget Proposal, Executive Summary, Schedule A](#); R.I. Senate Fiscal Office, "[Governor's FY 2022 and FY 2021 Supplemental Budget](#)," May 18, 2021. The federal Families First Coronavirus Response Act enhanced the federal matching rate for eligible Medicaid expenses by an additional 6.2 percentage points. On January 22, 2021, the U.S. Secretary of Health and Human Services issued a letter indicating that the enhanced rate would likely remain in place for the entirety of calendar year 2021. Ibid. The FMAP increase does not apply to administrative expenditures or to programs already at a higher FMAP rate, except for the Children's Health Insurance Program. Medicaid.gov, "[Families First Coronavirus Response Act – Increased FMAP FAQs](#)," April 13, 2020.

As shown in Figure 1, the proposed supplemental budget also includes savings of \$82.5 million by deferring \$70 million of the \$90 million appropriated in the enacted budget to repay the Rhode Island Capital Plan Fund in connection with the \$120 million transfer from the rainy day fund used to balance the FY 2020 budget.¹⁰ The FY 2021 enacted budget included a \$90 million repayment, with the remaining \$30 million left to be repaid in FY 2022. The governor’s proposed budget reduces the amount of repayment in FY 2021 to \$7.5 million for a savings of \$82.5 million, and includes repayment of \$42.5 million in FY 2022, thereby deferring \$70 million to be repaid in FY 2023.¹¹

The supplemental budget also includes an increase in the hospital licensing fee, projected to increase revenues by \$32.3 million. The FY 2021 enacted budget had reduced the hospital license fee from 6.0 percent to 5.0 percent. The supplemental budget restores the fee to 6.0 percent, the fee level assessed in FY 2019 and FY 2020.¹²

The FY 2022 Budget

Governor McKee’s FY 2022 budget proposes total expenditures of \$11.17 billion, considerably less than the \$12.73 billion authorized in the FY 2021 enacted budget and the \$13.75 billion proposed in the revised FY 2021 budget. The reduction in total expenditures in FY 2022 are largely the result of less federal funding connected with COVID response activities. The governor’s budget, however, proposes state general revenue spending of \$4.37 billion—an increase of \$218.0 million, or 5.2 percent, over the enacted FY 2021 budget.¹³

Figure 1		
Governor's Proposed Repayment of Capital Plan Fund (\$ Millions)		
FY 2020 Rainy Day Fund Transfer		\$ 120.0
FY 2021 Enacted	Repayment Schedule	
	FY 2021	\$ 90.0
	FY 2022	\$ 30.0
		\$ 120.0
Governor's Proposed FY 2021 Supplemental Budget	Repayment Schedule	
	FY 2021	\$ 7.5
	FY 2022	\$ 42.5
	FY 2023	\$ 70.0
		\$ 120.0
Proposed FY 2021 Savings		\$ 82.5
Source: R.I. Senate Fiscal Office, “Governor’s FY 2022 and FY 2021 Supplemental Budget”		

¹⁰ Better known as the rainy day fund, Rhode Island’s Budget Reserve Account was established under the Rhode Island Constitution and is funded by three percent of revenues annually. The Reserve Account is capped at five percent of estimated general revenues and any excess funds are transferred each year to the Rhode Island Capital Plan Fund to be used solely for capital projects. For more on the relationship between the budget, rainy day fund, and Capital Plan Fund, see: RIPEC, “[Rhode Island’s FY 2020 Supplemental Budget: The General Assembly Takes the First Step in Responding to Pandemic Fallout](#),” July 2020.

¹¹ R.I. Senate Fiscal Office, “[Governor’s FY 2022 and FY 2021 Supplemental Budget](#),” May 18, 2021.

¹² R.I. OMB, [FY 2022 Budget Proposal, Executive Summary, Schedule A](#). The governor proposes continuing the hospital license fee increase in FY 2022 for a revenue increase of \$31 million in that fiscal year. R.I. Senate Fiscal Office, “[Governor’s FY 2022 and FY 2021 Supplemental Budget](#),” May 18, 2021.

¹³ R.I. OMB, [FY 2022 Budget Proposal, Executive Summary](#).

In contrast to the FY 2021 supplemental budget, the FY 2022 proposed budget makes only limited use of federal funding to pay for state general revenue expenditures. The proposed budget includes savings of \$58.3 million based on two quarters of federal enhanced FMAP based on the most recent federal guidance.¹⁴

The most significant revenue item in the governor's proposed FY 2022 budget relates to state income taxes resulting from loan forgiveness under the federal Paycheck Protection Program (PPP). State general revenues projected in November assumed that, because expenses connected with PPP loans could not be deducted for federal tax purposes, such expenses therefore would not be deductible for state tax purposes since Rhode Island's tax treatment is legally coupled with the federal treatment in this instance. In December 2020, however, Congress permitted expenses connected with PPP loans to be deducted. Since Rhode Island law follows federal treatment, the federal tax change resulted in no state taxation of PPP loans, leaving a combined revenue shortfall of \$133.3 million in FY 2021 and FY 2022, given that these revenues were assumed in the November revenue estimate. Faced with this shortfall, the governor's budget proposes to treat PPP loan amounts above \$150,000 as taxable income, thereby recouping \$67.7 million over both fiscal years.¹⁵ If adopted, taxation of PPP loans would be inconsistent with federal policy and with the practices of the great majority of states.¹⁶

Governor McKee's FY 2022 budget contains several key expenditure initiatives. The most ambitious expenditure savings proposal involves the transformation of the Eleanor Slater Hospital (ESH) by closing the state's long-term acute care hospital facilities, creating a new Institute of Mental Disease at the existing Benton facility, and \$64.9 million in new debt financing to construct a newly licensed long-term care facility on the Zambarano campus—thereby saving \$38.7 million in state general revenues in FY 2022.¹⁷ This reorganization plan follows the loss of federal reimbursement for hospital operations and questions as to compliance with federal requirements that patients are treated in the most appropriate and least restrictive setting. Governor McKee has recently announced that these transformation plans are on hold pending input from stakeholders and the General Assembly.¹⁸

The budget also proposes a major investment in, and changes to, the developmental disability system: \$15 million in all funds financing—of which \$10 million is from general revenues—to

¹⁴ R.I. House Fiscal Advisory Staff, "[FY 2022 Budget Analysis](#)."

¹⁵ R.I. Senate Fiscal Office, "[Governor's FY 2022 and FY 2021 Supplemental Budget](#)," May 18, 2021. The FY 2022 appropriations act would provide the Tax Administrator with authority to reverse the taxation of PPP loans in the event the federal government provides funds to the state for revenue replacement. R.I. House Fiscal Advisory Staff, "[FY 2022 Budget Analysis](#)." In his budget transmittal letter, Governor McKee indicates that reversal of the taxation of PPP loan amounts over \$150,000 should be considered if more federal stimulus funding is forthcoming. R.I. OMB, [FY 2022 Budget Proposal, Executive Summary](#).

¹⁶ K. Loughhead, "[Which States Are Taxing Forgiven PPP Loans?](#)," Tax Foundation, updated May 5, 2021.

¹⁷ R.I. OMB, [FY 2022 Budget Proposal, Executive Summary](#).

¹⁸ R.I. Senate Fiscal Office, "[Governor's FY 2022 and FY 2021 Supplemental Budget](#)," May 18, 2021. The governor has proposed a budget amendment to restore the savings in full. R.I. OMB, "[Amendments to FY 2022 Appropriations](#)," June 6, 2021.

support improving the quality of, and access to, integrated community day and employment support programs for individuals with developmental disabilities. In addition, the governor's budget includes all funds savings of \$19.2 million, of which \$8.1 million is from general revenues, by shifting the operations of the current state-run developmental disabilities group home system—Rhode Island Community Living and Supports—to private organizations.¹⁹

In his budget, the governor also proposes \$9.2 million in total funding, including \$4.5 million in general revenues, on initiatives to encourage home and community-based services as an alternative to residential long-term care settings.²⁰

The governor's budget includes a permanent funding stream of \$2.6 million in FY 2022 and \$5.7 million on an annualized basis for affordable and workforce housing through an increase in the real estate conveyance tax on the value of residential property exceeding \$700,000 and the shifting of existing conveyance tax revenues from state general revenue to a restricted receipt account.²¹

The FY 2022 budget proposes legalizing adult-use marijuana through a program of retail licenses, with 25 retail licenses granted each year. The proposal includes the creation of a Governor's Cannabis Reinvestment Task Force to recommend long-term investment of marijuana revenues in specific areas of job training, access to capital for small businesses, affordable housing, health equity, and community development.²² The budget includes \$1.7 million in tax and license fee revenues in FY 2022 attributable to implementation of the adult-use marijuana market under this program, based on anticipated retail sales beginning in April 2022.²³

The budget proposal also includes funding for the continuation of the motor vehicle excise tax phaseout in accordance with the schedule in current law. For FY 2022, the budget includes \$139.7 million in total general revenue reimbursement funding for cities and towns in connection with the phaseout, including \$29.1 million in funding added in FY 2022.²⁴

Governor McKee's FY 2022 budget proposes to fully fund K-12 education at the funding formula level by increasing state aid by \$34.9 million. The budget also includes \$6 million in federal funding to raise reimbursement rates for childcare providers and incentivize providers to deliver the highest quality care. In addition, the governor's budget proposes to remove the sunset on the Promise Scholarship program, which offers two years of free tuition at the Community College of Rhode Island to recent high school graduates. The program would be funded at a total of \$7.7 million.²⁵

¹⁹ R.I. OMB, [FY 2022 Budget Proposal, Executive Summary](#).

²⁰ Ibid.

²¹ Ibid.

²² Ibid.

²³ R.I. Senate Fiscal Office, "[Governor's FY 2022 and FY 2021 Supplemental Budget](#)," May 18, 2021.

²⁴ R.I. House Fiscal Advisory Staff, "[FY 2022 Budget Analysis](#)."

²⁵ R.I. OMB, [FY 2022 Budget Proposal, Executive Summary](#). The governor's proposal to make permanent the Promise Scholarship program has already been enacted by the General Assembly. R.I. General Assembly Press Releases, "[Rhode Island Promise program permanently enacted](#)," May 28, 2021.

The governor’s budget includes \$42.0 million in total general revenue funding in support of economic development and housing programming within the Executive Office of Commerce, including \$22.5 million for Rebuild RI program incentives, equivalent to the FY 2021 enacted level, and raising the program cap from \$210.0 million to \$240.0 million. Additional general revenue funding of \$3.0 million is proposed for the Real Jobs Rhode Island job training program, increasing total general revenue funding for the program to \$8.5 million.²⁶

Reliance On One-Time Funding

Governor McKee’s FY 2022 budget relies on \$281.2 million in one-time federal pandemic relief funding to pay for ongoing state general revenue expenditures. The budget also relies on the deferral of \$70 million of the \$120 million appropriated to repay the Rhode Island Capital Plan, as well as \$67.7 million in revenues connected with taxation of PPP loans, a one-time event. The extent to which federal sources and one-time sources are used to fund state general revenue expenses is important since additional state revenues will need to be generated to continue to pay for these expenditures in the future. Any gap in continuing state expenditures and available state revenues would likely result in a structural deficit in future budgets. Figure 2 details the items of one-time federal and other funding used to pay for ongoing state expenditures, in total amounting to \$418.9 million.

The governor’s budget recognizes the impact of these one-time sources of revenue in projecting a large structural budget deficit in its five-year forecast. Based on the assumption that one-time strategies to balance the FY 2022 budget would no longer be available, the budget deficit is projected to range from \$374.4 million in FY 2023 to \$318.9 million in FY 2026. The five-year forecast notes that new federal stimulus funding would change these assumptions. Figure 3 illustrates the structural budget deficit as forecasted in FY 2021 and FY 2022 and shows that projected budget deficits have increased dramatically between forecasts in these two fiscal years.²⁷

Figure 2
FY 2022 Proposed Budget
One-Time Funding (\$ Millions)

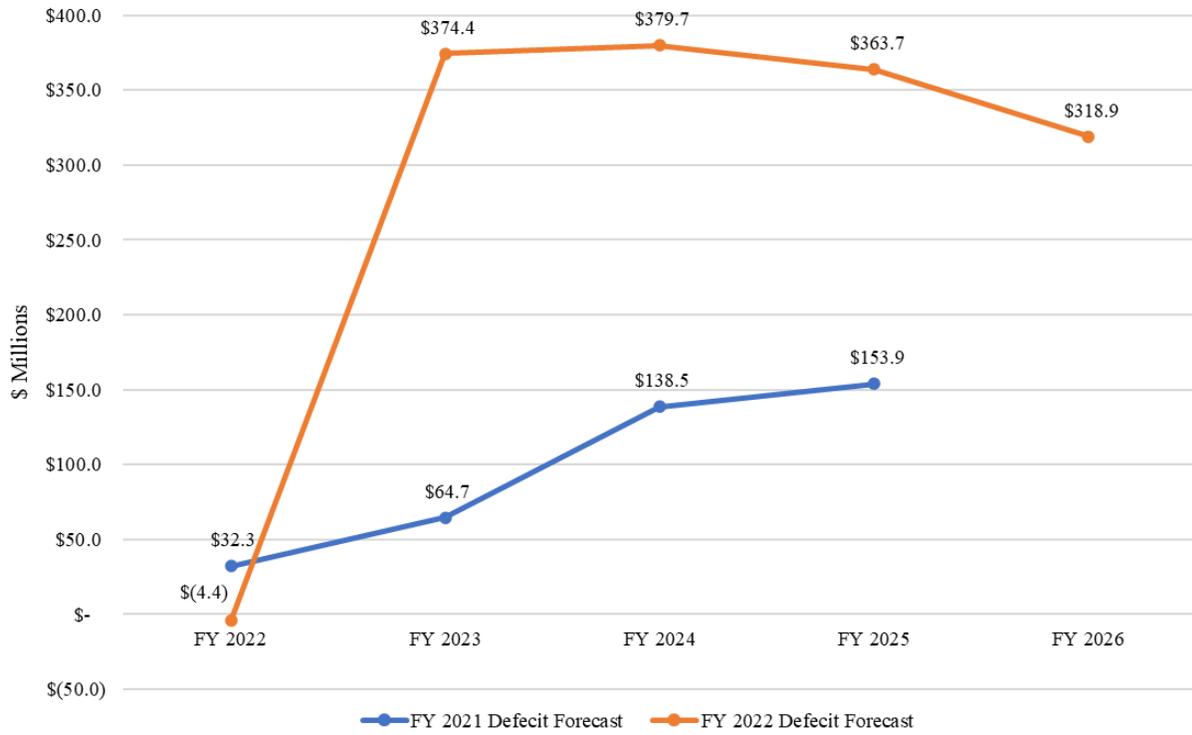
Action	Fiscal Years	Amount
FEMA Reimbursement to 100 percent	2021	\$ 118.0
Federal Funding of Public Safety Personnel	2021	\$ 67.5
Enhanced FMAP	2021/2022	\$ 95.7
Deferral of repayment to RICAP	2021/2022	\$ 70.0
Taxation of PPP Loans	2021/2022	\$ 67.7
Total		\$ 418.9

Source: R.I. OMB FY 2022 Budget Proposal, Executive Summary; R.I. House Fiscal Advisory Staff, "FY 2022 Budget Analysis"

²⁶ R.I. OMB, [FY 2022 Budget Proposal, Executive Summary](#).

²⁷ Ibid.

Figure 3
Structural Budget Defecit, FY 2021 & FY 2022 Forecasts (\$ Millions)



Source: R.I. OMB, FY 2022 Budget Proposal, Executive Summary

III. Revised Budget Outlook

In Rhode Island, the annual state budget is based on projections of general revenues determined through a Consensus Revenue Estimating Conference, which occurs in May and November of each year.²⁸ Revenue estimates reflect the consensus reached by the three Conference principals: the State Budget Officer, the House Fiscal Advisor, and the Senate Fiscal Advisor.²⁹ The Conference typically relies on testimony from executive branch officials as well as economic forecasting by an independent forecasting firm to produce estimates for both the current and subsequent fiscal year. Contemporaneously, the Conference principals convene a Caseload Estimating Conference for the purpose of estimating anticipated expenditures relating to medical and public assistance.³⁰

The determination of estimated revenues by the Revenue Estimating Conference is central to the integrity of the budget process and to meeting the state’s constitutional requirement of a balanced budget.³¹ The governor typically presents to the legislature a proposed budget for the upcoming fiscal year in January which relies on the estimates produced in the preceding November Revenue Estimating Conference. As such, the November Conference presents the first projection of estimates for the next fiscal year. When the General Assembly enacts a budget—typically before the fiscal year begins on July 1—it relies on the Conference’s May estimates.³²

While the Revenue Estimating Conference is perennially important to the state’s fiscal position, the last three Conferences have taken on outsized importance and have been uncharacteristically volatile due to the economic upheavals accompanying the COVID-19 pandemic. The May 2020 Conference, held less than two months after the first cases of COVID-19 were detected in Rhode Island, determined that estimated revenues for FY 2020 and FY 2021 would be dramatically lower than estimated at the November 2019 Conference: \$280.9 million (6.7 percent) lower for FY 2020 and \$515.8 million (12.2 percent) lower for FY 2021.³³ In contrast, in November 2020, estimated revenues for FY 2021 were sharply increased by \$330.6 million (8.9 percent) over revenues estimated in May 2020.³⁴

²⁸ R.I. Gen. Laws [§ 35-16-2](#). General revenues are one of four primary revenue types collected by the State of Rhode Island and, unlike the state’s three other funding streams—federal grants, other funds, and restricted receipts—general revenues are typically used for any type of budgeted expenditure.

²⁹ Ibid.

³⁰ R.I. Gen. Laws [§ 35-17-1](#).

³¹ In fact, under the Rhode Island Constitution, aggregate state general revenue appropriations in any given fiscal year may not exceed 97 percent of estimated state general revenues for such fiscal year. R.I. Constitution, [Article IX](#), § 16(a).

³² R.I. Gen. Laws, [§ 35-16-1\(a\)](#).

³³ R.I. OMB, [May 2020 Revenue Estimating Conference Report](#).

³⁴ R.I. OMB, [November 2020 Revenue Estimating Conference Report](#).

The May 2021 Revenue Estimating Conference

Economic Forecasting Testimony

Given the rapidly changing economic recovery from the pandemic, economic forecasting testimony was a critical input to the May 2021 Revenue Estimating Conference. IHS Markit, a state-contracted and nationally based firm which has provided testimony at prior conferences, painted a mixed picture, testifying that while Rhode Island has recouped two-thirds of the jobs lost during the pandemic, recovering the last third of the lost jobs will take much longer. IHS Markit’s forecast assumes that Rhode Island’s unemployment rate will remain above 5 percent until mid-FY 2022 and nonfarm employment will not surpass its pre-COVID peak until FY 2024. A return to peak employment in Rhode Island is forecasted to take longer than the nation on average.³⁵

As depicted in Figure 4, the May 2021 forecast was also somewhat mixed when compared to IHS Markit’s November Forecast. IHS Markit’s May forecast for Rhode Island employment was down slightly for FY 2021 (11,700 jobs) and FY 2022 (4,800 jobs) when compared to the November 2020 forecast, in large part due to the infection surge at the end of calendar year 2020. However, personal income growth was forecast to be much greater in FY 2021 as compared to the November forecast (7.1 percent in May, as compared to 2.6 percent forecast in November), while growth was forecast to decline slightly more in FY 2022 than was forecast in November (1.8 percent decline in May, as compared to 0.9 percent decline forecast in November). Consumer spending was forecast to grow in both fiscal years at rates greater than was forecast in November (by 2.6 percent in FY 2021 and 7.9 percent in FY 2022 forecasted in May, as compared to 2.2 percent in FY 2021 and 5.3 percent in FY 2022 forecasted in November).³⁶

Figure 4
Consensus Economic Forecast
November 2020 - May 2021 Difference

		Nov-20	May-21	Nov-May Difference
Non-Farm Employment (Thousands)	FY 2021	475.6	463.9	-11.7
	FY 2022	492.1	487.4	-4.8
Personal Income Growth	FY 2021	2.6%	7.1%	4.5%
	FY 2022	-0.9%	-1.8%	-0.9%
Personal Consumption Growth	FY 2021	2.2%	2.6%	0.4%
	FY 2022	5.3%	7.9%	2.6%

Source: R.I. OMB November 2020 and May 2021 Revenue Estimating Conference Reports

³⁵ R.I. OMB, [May 2021 Revenue Estimating Conference](#).

³⁶ IHS Markit, [“Rhode Island Outlook,”](#) April 30, 2021.

Revenue Estimates

Depicted in Figure 5, total general revenues for FY 2021 were estimated at \$4.22 billion at the May 2021 Revenue Estimating Conference, an increase of \$177.1 million, or 4.4 percent, over the FY 2021 enacted budget. Consistent with the economic forecast, this large increase in estimated revenues for FY 2021 was driven by strong increased projections for personal income taxes (up \$89.6 million, or 6.2 percent, over the enacted level), sales and use taxes (up \$79.5 million, or 6.6 percent), and lottery revenues (up \$34.4 million, or 13.5 percent).³⁷

Figure 5
FY 2021 Revenues, Enacted Budget vs. May 2021 Estimate
(\$ Millions)

	Enacted	May-21	Difference	
Personal Income Tax	\$ 1,450.4	\$ 1,540.0	\$ 89.6	6.2%
General Business Taxes	\$ 458.2	\$ 422.9	\$ (35.3)	-7.7%
Sales and Use Tax	\$ 1,212.8	\$ 1,292.3	\$ 79.5	6.6%
Other Taxes*	\$ 251.9	\$ 244.0	\$ (7.9)	-3.1%
<i>Total Taxes</i>	<i>\$ 3,373.3</i>	<i>\$ 3,499.2</i>	<i>\$ 125.9</i>	<i>3.7%</i>
Department Receipts	\$ 390.0	\$ 398.0	\$ 8.0	2.1%
Lottery	\$ 254.5	\$ 288.9	\$ 34.4	13.5%
Miscellaneous	\$ 10.3	\$ 13.8	\$ 3.5	33.7%
Unclaimed Property	\$ 10.3	\$ 15.6	\$ 5.3	51.5%
Total General Revenues	\$ 4,038.4	\$ 4,215.5	\$ 177.1	4.4%

* Includes motor vehicle, cigarettes, alcohol, estate and transfer, racing and athletics, and realty transfer taxes

Source: R.I. OMB, May and November Revenue Estimating Conference Reports

Total general revenues for FY 2022 were forecast to be \$4.19 billion, an increase of \$146.8 million, or 3.6 percent, over FY 2022 revenues estimated in November. As outlined in Figure 6, this increase is driven largely by a jump of \$95.9 million (6.7 percent) in projected personal income tax revenues, as well as by an increase of \$41.7 million (3.3 percent) in estimated sales and use tax revenues.

³⁷ R.I. OMB, [May 2021 Revenue Estimating Conference](#).

Figure 6
FY 2022 Revenues, November 2020 Estimate vs. May 2021 Estimate
(\$ Millions)

	Nov-20	May-21	Difference	
Personal Income Tax	\$ 1,439.1	\$ 1,535.0	\$ 95.9	6.7%
General Business Taxes	\$ 470.3	\$ 455.4	\$ (14.9)	-3.2%
Sales and Use Tax	\$ 1,263.5	\$ 1,305.2	\$ 41.7	3.3%
Other Taxes*	\$ 243.3	\$ 244.2	\$ 0.9	0.4%
Total Taxes	\$ 3,416.2	\$ 3,539.8	\$ 123.6	3.6%
Department Receipts	\$ 249.0	\$ 251.0	\$ 2.0	0.8%
Lottery	\$ 356.3	\$ 375.7	\$ 19.4	5.4%
Miscellaneous	\$ 12.2	\$ 11.0	\$ (1.2)	-9.5%
Unclaimed Property	\$ 11.3	\$ 14.2	\$ 2.9	25.7%
Total General Revenues	\$ 4,045.0	\$ 4,191.7	\$ 146.8	3.6%

* Includes motor vehicle, cigarettes, alcohol, estate and transfer, racing and athletics, and realty transfer taxes

Source: R.I. OMB, May and November Revenue Estimating Conference Reports

The higher May estimates for FY 2022 are \$23.8 million less than enacted revenues for FY 2021, with the decline primarily due to the exclusion of the hospital license fee, which is typically renewed each year but is not included in current law. Assuming revenues from a renewed hospital license fee at the same level as FY 2021 (\$161.5 million), total projected revenues for FY 2022 would be \$4.35 billion, an increase of \$137.7 million (3.3 percent) over the FY 2021 enacted level. The revenue estimate for FY 2022 reflects the relatively slow growth projected by the economic forecast despite the full reopening of the economy.³⁸

As discussed above, the May 2021 estimates do not include revenues connected with taxation of PPP loans, thereby reversing projected revenues of \$133.3 million included in revenue estimates at the November 2020 Conference.

Caseload Estimates

Depicted in Figure 7, the May Caseload Estimating Conference also contributed to an improved budget outlook for both FY 2021 and FY 2022. Compared to the FY 2021 enacted budget, the May Conference estimated cash assistance and medical assistance expenditures would decrease by \$26.9 million in total, with reduced general revenue expenditures of \$45.0 million. For FY 2022, the May Conference estimated expenditures would increase by a total of \$196.1 million over

³⁸ Ibid.

the November Conference estimates, mostly due to delay of anticipated federal reduction in disproportionate share payments to hospitals. Despite this large increase in total expenditures, general revenue expenditures for FY 2022 were reduced by \$8.6 million as compared to November Conference estimates. Over the two fiscal years, the May Conference estimated total general revenue savings of \$53.6 million.³⁹

Figure 7
May 2021 Caseload Estimating Conference (\$ Millions)

		FY 2021			
		Enacted	May-21	Change	
All Funds	Cash Assistance	\$ 103.8	\$ 90.5	\$ (13.3)	-14.7%
	Medical Assistance	\$ 2,703.9	\$ 2,690.3	\$ (13.6)	-0.5%
	Total	\$ 2,807.7	\$ 2,780.8	\$ (26.9)	-1.0%
General Revenues	Cash Assistance	\$ 28.4	\$ 27.6	\$ (0.8)	-2.7%
	Medical Assistance	\$ 940.0	\$ 895.7	\$ (44.2)	-4.7%
	Total	\$ 968.3	\$ 923.3	\$ (45.0)	-4.6%
		FY 2022			
		Nov-20	May-21	Change	
All Funds	Cash Assistance	\$ 104.4	\$ 102.9	\$ (1.5)	-1.4%
	Medical Assistance	\$ 2,689.3	\$ 2,886.9	\$ 197.6	7.3%
	Total	\$ 2,793.7	\$ 2,989.8	\$ 196.1	7.0%
General Revenues	Cash Assistance	\$ 28.7	\$ 28.0	\$ (0.7)	-2.6%
	Medical Assistance	\$ 1,009.3	\$ 1,001.4	\$ (7.9)	-0.8%
	Total	\$ 1,038.0	\$ 1,029.4	\$ (8.6)	-0.8%

Source: R.I. OMB, May 2021 Caseload Estimating Conference Report

FY 2021 Third Quarter Report

On May 14, 2021, the OMB issued the FY 2021 Third Quarter Report, which projected anticipated expenditures at year end in the current year, as required by law.⁴⁰ The Third Quarter Report incorporates the expenditure adjustments connected with the use of federal funding to pay for state general revenue expenditures contained in the governor’s FY 2021 supplemental budget

³⁹ R.I. OMB, [May 2021 Caseload Estimating Conference](#). The caseload savings incorporate savings connected with the enhanced FMAP. Ibid.

⁴⁰ The state budget officer is required to prepare a quarterly report projecting the anticipated year end balances. R.I. Gen. Laws [§ 35-1-5](#).

submission, as well as the increased revenues and reduced expenditures for FY 2021 as estimated at the May Revenue and Caseload Estimating Conferences. The Third Quarter Report also includes \$6.9 million in savings for additional reallocations of state-financed personnel expenses at the Department of Corrections. Based on these inputs, the Third Quarter Report estimates a general revenue surplus of \$416.8 million, amounting to 10.0 percent above the enacted FY 2021 budget.⁴¹

Importantly, the Third Quarter Report includes risks associated with federal participation under Medicare and Medicaid with respect to operations at ESH that could affect the projected general revenue surplus of \$1.5 million for the Department of Behavioral Healthcare, Developmental Disabilities, and Hospitals over the FY 2021 enacted budget. While the federal Centers of Medicare and Medicaid Services has approved the latest Rhode Island State Plan Amendment for reimbursement retroactive to April 2020, billing for services in FY 2021 has not yet taken place. Additionally, if the proportion of psychiatric patients at ESH—a two-campus state hospital with facilities in Cranston and Burrillville—exceed federal standards, there is a risk that it would be reclassified as an Institute of Mental Disease and thereby no longer qualify for federal reimbursement. In total, \$16.5 million in federal reimbursement is at risk.⁴²

⁴¹ R.I. OMB, [FY 2021 Third Quarter Report](#), May 14, 2021.

⁴² Ibid.

IV. The American Rescue Plan Act

On March 11, 2021—the same day Governor McKee submitted his budget—President Biden signed ARPA into law, the latest in a series of legislation enacted by Congress to provide economic relief during the COVID-19 pandemic. While the governor’s proposed FY 2022 budget did not take account of ARPA, the enormous federal funding to be provided under ARPA to state and local government will have a major impact on the Rhode Island state budget going forward.

ARPA provides \$1.9 trillion in total federal assistance in the form of direct economic impact payments to individuals and families, expanded child tax credits, homeowner assistance, rental assistance, expanded credit for small businesses, and expanded unemployment benefits. ARPA also included \$350 billion in direct funding to state and local governments, along with hundreds of billions of dollars in additional funding for COVID-19 response, education, rental assistance, childcare, transportation, and other programs.⁴³

Under ARPA State and Local Fiscal Recovery Funds, Rhode Island state government will receive an allocation of \$1.1 billion and local governments will receive a total of \$536.9 million.⁴⁴ ARPA also includes a Capital Projects Fund totaling \$10 billion for states, territories, and tribes to cover the costs of capital projects “directly enabling work, education, and health monitoring, including remote options, in response to the public health emergency.”⁴⁵ Rhode Island will receive an allocation of \$112.7 million from the Capital Projects Fund.⁴⁶

ARPA’s State Fiscal Recovery Funds can be spent only for eligible purposes. States can use these funds to respond to the COVID-19 public health emergency “or its negative economic impacts, including assistance to households, small businesses, and nonprofits, or aid impacted industries such as tourism, travel, and hospitality.” States also can use the funds to provide premium pay to state employees performing essential work, or to employers that have employees performing essential work. Fiscal Recovery Funds can be used to cover shortfalls in state revenues resulting from the pandemic. States can also employ this funding for “necessary investments in water, sewer, or broadband infrastructure.” States have until December 31, 2024, to spend these funds. States cannot use Fiscal Recovery Funds to reduce taxes or to make contributions to a pension fund.⁴⁷

In addition to over \$1.2 billion in State Recovery Funds and Capital Projects Funds, Rhode Island will receive large allocations of additional funding for a range of programs, including \$415.0

⁴³ U.S. Treasury, “[Fact Sheet: The American Rescue Plan Will Deliver Immediate Economic Relief to Families](#),” March 18, 2021; National Conference of State Legislatures, “[American Rescue Plan Act of 2021](#),” March 9, 2021.

⁴⁴ U.S. Treasury, “[Coronavirus State and Local Fiscal Recovery Funds](#).” Funding for Rhode Island’s cities and towns is somewhat complicated: Cranston, East Providence, Pawtucket, Providence, Warwick, and Woonsocket will receive direct allocations totaling \$273.1 million. The remaining Rhode Island municipalities will receive a total of \$58.1 million distributed by population. Rhode Island also receives \$205.7 million in allocations to counties which is distributed to municipalities in each county by population. Ibid.

⁴⁵ [P.L. 117-2, § 9901](#).

⁴⁶ R.I. Department of Administration, “[COVID-19 Stimulus Update](#),” June 1, 2021.

⁴⁷ [P.L. 117-2, § 9901](#).

million for K-12 education, \$90.8 million for public higher education, \$245.3 million for rental and homeowner assistance, \$94.4 million for childcare, \$78.9 million for public health, and funding for several other programs.⁴⁸

⁴⁸ R.I. Department of Administration, "[COVID-19 Stimulus Update](#)," June 1, 2021.

V. RIPEC Comments

The COVID-19 pandemic wreaked havoc on Rhode Island's economy and upended the state budgeting cycle. Governor Daniel J. McKee's first budget for FY 2022, submitted in March, is the third annual budget complicated by the pandemic, and follows enactment of a pared-down, or "skinny," budget for FY 2021, enacted only a few months before, in December, with the fiscal year nearly half over.

Governor McKee's proposed FY 2022 budget represents a status quo spending plan, largely a continuation of taxing policies and programs of the prior Raimondo Administration. The budget makes very little use of federal funding to pay for state expenditures in FY 2022 but relies heavily on the use of federal funds to pay for state expenditures in the current fiscal year, FY 2021. The budget also relies on the deferral of \$70 million appropriated to repay the Rhode Island Capital Plan Fund in connection with the rainy day fund transfer in FY 2020, as well as \$67.7 million in revenues from taxation of PPP loans, a one-time event. In total, the FY 2022 budget depends on \$418.9 million in one-time items. Not surprisingly, the governor's proposed budget projects future deficits ranging from \$374.4 million in FY 2023 to \$318.9 million in FY 2026.

The budget picture, however, brightened considerably as a result of the May 2021 Revenue Estimating Conference and, to a lesser extent, the May 2021 Caseload Estimating Conference. The May Conference projected that estimated revenues for the current FY 2021 budget would be \$177.1 million higher than the enacted FY 2021 level. For FY 2022, the May Conference projected that revenues would be \$146.8 million greater than revenues projected at the November 2021 Conference. Over the two fiscal years, the May Caseload Estimating Conference estimated total general revenue savings of \$53.6 million.

Incorporating the federal funding savings and the revenue and caseload changes, the FY 2021 Third Quarter report projected a general revenue surplus of \$416.8 million. Compared to revenues and caseloads estimated at the November Conference, revenues and caseload adjustments for FY 2022 yield a positive variance of \$155.4 million. Over the two fiscal years, projected FY 2021 surplus revenues and additional FY 2022 revenues as compared to November 2020 estimates total a remarkable \$572.2 million. Importantly, the May 2021 estimates do not include revenues connected with taxation of PPP loans, thereby reversing projected revenues of \$133.3 million included in revenue estimates at the November 2020 Conference. Nor do these surplus revenues include any funding from ARPA.

Based on this analysis, RIPEC offers the following considerations for policymakers:

The state should avoid spending beyond available revenues and minimize the structural deficit going forward. As a result of a substantial increase in state revenues projected at the May 2021 Revenue Estimating Conference, the state finds itself in the fortuitous position of having little to no structural deficit for the first time in many years. In fact, the positive variance of the May 2021 Revenue and Caseload Conferences is \$377.5 million, almost exactly the amount as the

budget deficit forecast for the next fiscal year, FY 2023. It is critical that this stable budget situation be preserved by avoiding spending commitments in the FY 2022 budget beyond available revenues. If additional federal funding is used, such funding should pay for one-time, rather than continuous, state expenditures.

The state should fully repay the Rhode Island Capital Plan Fund in connection with the \$120 million rainy day fund transfer used to balance the FY 2020 budget. While the state’s rainy day fund balance has been restored to five percent of estimated general revenues, as required by the Rhode Island Constitution, the Rhode Island Capital Plan Fund—which is financed through excess rainy day funds each year and represents the state’s primary vehicle for capital improvements—has not been fully repaid. Governor McKee’s budget proposes to defer repayment of \$70 million to FY 2023. Given the greater state revenues now available, and the state’s considerable capital needs, this repayment should be completed in FY 2022.

Policymakers should not raise state personal income taxes. Despite abundant state revenues and over \$1 billion in federal funding for state government under the American Rescue Plan Act, there remain serious efforts in the General Assembly to raise state personal income taxes on high income earners. Since the great majority of businesses, and nearly all small businesses, in Rhode Island are organized as pass-through entities and report their profits through the personal income tax, these proposals would impose a higher tax burden on business, and particularly on small business, at a time when many businesses are struggling to survive and recover from the pandemic’s economic fallout. The proposed legislation also would undercut and reverse important work done in the last decade to improve Rhode Island’s income tax structure and business tax climate.⁴⁹

The state should avoid imposing state income taxes on PPP loans. Since the November 2020 Revenue Estimating Conference assumed that PPP loans would be subject to state income taxes in projecting available revenues, Governor McKee faced a large revenue loss if such loans were not taxed and proposed to tax PPP loans in part by exempting from taxation loans up to \$150,000. The situation has changed dramatically as a result of the May 2021 Revenue Estimating Conference, which assumed that PPP loans would not be taxed and also projected a large increase in available revenues. Imposing a state income tax on a federal grant primarily spent by businesses to keep their employees on the payroll is at odds with the position taken by the federal government and by the great majority of states.

Policymakers should resolve the spending issues connected with the Eleanor Slater Hospital. The ESH has been the subject of considerable recent controversy relating to issues of patient safety, appropriate levels of care, and the proposed transformation of the hospital system. Besides these

⁴⁹ In 2011, Rhode Island’s overall business tax climate was ranked 47th in the nation, according to the Tax Foundation, a national tax policy research organization. As a result of the state’s 2011 income tax reform, and other tax reforms affecting businesses and individuals, Rhode Island’s business tax climate ranking has climbed steadily—now at 37th in the Tax Foundation rankings. However, the Ocean State remains in the bottom third of states. RIPEC, “[Rhode Island Ranks 37th in 2021 Business Tax Climate Index](#),” December 2020.

important concerns, ESH represents arguably the most troubling spending issue in the state budget given the sizable loss and uncertainty relating to federal reimbursement, extremely high per patient costs, and the recent reversal of proposed budget savings.⁵⁰ It is important that ESH operations be placed on a financially responsible and sustainable path.

The state should follow a deliberate process to plan expenditures of ARPA funds. Under ARPA, Rhode Island state government will be receiving over \$1 billion in discretionary funds, along with over \$1 billion more in funding for K-12 education, higher education, rental and homeowner assistance, childcare, public health, and other programs. This funding represents a once-in-a-generation opportunity to pursue transformative investments that could potentially change the trajectory of our state’s economy and quality of life. With nearly four years to commit this funding, state policymakers should follow a deliberate and inclusive process to decide how these dollars should be spent. At the same time, it is imperative policymakers resist using these one-time funds to create new programs, or expand existing programs, that the state would be unable to sustain once the federal funding is exhausted.

⁵⁰ R.I. House Fiscal Advisory Staff, “[Health & Human Services EOHHS & BHDDH Article 4—Sections 4 and 5,](#)” Staff Presentation to House Finance Committee, June 2, 2021.