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The Government Affairs Group at Murtha Cullina LLP is pleased to provide information about current topics of interest.

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BUDGET WARS - CONNECTICUT PART III

In the spirit of compromise, and in an effort to jump-start stalled budget negotiations, Governor M. Jodi Rell let it be known last week that she would entertain possible tax hikes if the legislature supported additional, legitimate budget cuts. After months of holding the high ground on tax increases, Rell announced she would propose some new revenue enhancements to plug the \$8.5 billion hole in the state's two-year budget for FY10 and FY11. Democrats seized this opportunity to report out their own tax and spending package which is radically different from Rell's budget proposal, but does concede some new reductions in a number of state programs.

Budget Negotiations

As Connecticut's economy continues to sputter, the state has seen its core revenues fall off a cliff. According to the economists at the State Labor Department, the state's personal income tax is down more than 20% from the prior year and corporate and sales and use taxes are down 17.9% and 8.5%, respectively, for the same period. Responding to this revenue loss, Governor Rell called for \$391 million in new taxes and additional budget cuts that are \$1.6 billion below the budget she vetoed on July 1. The largest of these tax increases would raise the state's cigarette tax from \$2.00 to \$3.00, generating \$227.4 million over two years. The Governor's other tax proposals are as follows:

Other Tobacco Products		\$4.2 million (two-year revenues)
- Cigars & chewing tobacco	20% to 27.5%	
-Snuff	40¢ to 44¢ / oz	
Alcohol Beverage Tax	10% increase	\$8.4 million (two-year revenues)
Out-of-State Corporate Tax (based on economic nexus)	New	\$10 million (FY 11)

Democrat Budget Proposal

The same day Governor Rell released her new budget, majority Democrats reported out their own modified tax and spending proposals. Democrats proposed a \$35.4 billion General Fund, two-year budget that is \$1.3 billion below the appropriations level of their previ-

ously passed and vetoed budget. To meet revenue shortfalls, Democrats called for new taxes totaling \$1.8 billion, the vast majority of which would come from new state income taxes on couples earning over \$500,000 annually. The current 5% tax rates on these couples would move up to 6% at an income level of \$500,000 a year, 6.5% for income levels above \$600,000 annually and 7% for couples earning \$750,000 or more a year. Total revenues expected to be raised by this change, and a delay in the planned increase in the singles exemption, would bring in approximately \$1.3 billion over a two-year period.

Other tax and fee increases proposed by the Democrats breakdown as follows, with individual revenue estimates included:

	FY10	FY11
Sales Tax		
Establish Use Tax Look-Up Table on Personal Income Tax Form	0.5	0.5
Corporation Tax		
Temp. Rate increase from 7.5% to 8.635% IY 2009, 2010, 2011	80.0	53.0
Decouple from Federal Domestic Production Deduction	27.5	27.5
Repeal the exemption for Income earned by DISCs	25.0	25.0
Repeal the exemption for Dividends from DISCs	25.0	25.0
Increase Preference Tax from \$250k to \$900k	5.5	5.5
Insurance Companies Tax		
Modification to Film Tax Credit	—	10.0
Estate & Gift		
30% Surcharge IY 2009, 2010, 2011	42.7	51.2
Cigarette & Tobacco Taxes		
Cigarettes (75¢), effective 1/1/10	51.7	90.2
Increase Other Tobacco Products Tax:	1.1	2.0
Snuff: from 40¢ to 55¢ / ounce		
Other Tobacco: from 20% to 27,5% of wholesale price		
Licenses, Permits & Fees		
Increase Various Fees (including Marshalls, excludes Nurses	58.2	51.2
Sale of Assets	10.0	10.0

What's Next?

Following release of last week's dueling budget documents, legislative leaders and the Governor's budget negotiators will again adjourn to the back rooms of the Capitol to attempt to work out their differences and break the budget stalemate. Connecticut, Michigan and North Carolina are the only remaining states which have not enacted budgets for their new fiscal years. Governor Rell is now running the state on a month-to-month basis through executive

order. Waiting on the sidelines are the state's municipalities, the bond rating agencies and numerous social service organizations that are tuned into and reliant on state cash flow for their existence. And let's not forget the chain-smoking millionaire who occasionally enjoys a spirit or two. That individual is clearly at risk as these negotiations move forward.

If you have any questions about the issues addressed here, please feel free to contact David McQuade, Senior Government Affairs Consultant, at 860-240-6141 / dmcquade@murthalaw.com, or your attorney.



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