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Legislative Sessions End with More Taxes and More Questions

The 2011 regular and special June 30th sessions of the Connecticut General Assembly witnessed the enactment of a dizzying array of increased tax rates and new taxes. With some provisions effective on a retroactive basis back to January 1, 2011, these changes afford both taxpayers and the Connecticut Department of Revenue Services little time, if any, to understand fully the consequences of such changes and to implement compliance measures. To its credit, the Department continues at a furious pace to publish administrative guidance and to post on its website the answers to frequently asked questions. However, due to the retroactive effective date of many of the changes, it is an almost impossible task to educate all taxpayers in a timely manner. We hope this Alert helps in the education effort, as we review the principal tax laws adopted, administrative guidance issued and court decisions rendered during the first ten months of this year.

During a special session conducted on October 26, 2011, the General Assembly enacted legislation intended to spur job growth in Connecticut. The legislation includes provisions creating a new job expansion tax credit, increasing the manufacturing reinvestment account cap, modifying the rules governing other tax credits, making the business entity tax a biennial tax commencing in 2013, and expanding the First Five Program, now called the First Five Plus Program, to promote ten development projects during the 2012 fiscal year. Time will tell whether these targeted efforts will help stimulate the Connecticut economy. In the interim, individuals and businesses will need to plan for the uncertain future by addressing the significant tax increases that are likely to impact everyone living or doing business in Connecticut regardless of their financial situation.

Please contact a member of our State and Local Tax Practice Group if you have any questions regarding the new tax law changes or how they affect you or your business.

INDIVIDUAL INCOME TAX

New and Increased Marginal Tax Rates. The prior schedule of three marginal tax rates of 3.0%, 5.0% and 6.5% is replaced, retroactively to January 1, 2011, with a schedule of six marginal tax rates, including a top rate of 6.7%. The new rates for single taxpayers (including married individuals filing separately), joint filers and heads of households, and the Connecticut taxable income levels after which each rate would apply, are as follows:

	3.0%	5.0%	5.5%	6.0%	6.5%	6.7%
Single	\$0	\$10,000	\$50,000	\$100,000	\$200,000	\$250,000
Joint	\$0	\$20,000	\$100,000	\$200,000	\$400,000	\$500,000
HOH	\$0	\$16,000	\$80,000	\$160,000	\$320,000	\$400,000

Conn. Gen. Stat. §12-700(a), as amended by Conn. Pub. Act No. 11-6, §107 (*effective May 4, 2011, and applicable to tax years commencing on or after January 1, 2011*). See DRS Special Notice 2011(12), *2011 Legislative Changes Affecting the Income Tax*.

Phase Out of Lowest Marginal Tax Rate. The amount of a taxpayer's Connecticut taxable income that will be subject to the 3.0% tax rate will begin to phase out when the Connecticut adjusted gross income of the taxpayer exceeds \$56,500 in the case of a single filer, \$100,500 in the case of a joint filer, \$78,500 in the case of a head of household filer, and \$50,250 in the case of a married individual filing separately. Income subject to the phase-out will be taxed at the 5.0% rate. Conn. Gen. Stat. §12-700(a), as amended by Conn. Pub. Act No. 11-6, §107 (*effective May 4, 2011, and applicable to tax years commencing on or after January 1, 2011*).

Recapture of Marginal Rate Benefits. The schedule of marginal tax rates includes a "recapture" provision whereby a taxpayer will lose the benefit of the lower marginal rates once the taxpayer's Connecticut adjusted gross income exceeds a certain income threshold (\$400,000 for joint filers, \$320,000 for head of household filers, and \$200,000 for single and married filing separately filers). By way of example, joint filers are required to recapture \$150 in tax benefits (i.e., pay an additional tax of \$150) for every \$10,000, or fraction thereof, in Connecticut adjusted gross income they earn over \$400,000 (up to a maximum recapture amount of \$4,500). The result is that a couple filing a joint tax return will lose any benefit of the lower marginal tax rates once their Connecticut adjusted gross income reaches \$700,000. Conn. Gen. Stat. §12-700(a), as amended by Conn. Pub. Act No. 11-6, §107 (*effective May 4, 2011, and applicable to tax years commencing on or after January 1, 2011*).

Reduction of Property Tax Credit. The tax credit for property taxes paid with respect to a primary residence or motor vehicle is reduced from a maximum of up to \$500 to a maximum of up to \$300. Prior law reduced the maximum credit by 10% for every \$10,000 (\$5,000 for married filing separately filers) in additional Connecticut adjusted gross income earned over certain thresholds. The new law provides for a steeper phase-out by increasing the percentage reduction to 15% for every \$10,000 (or \$5,000) in additional Connecticut adjusted gross income. Conn. Gen. Stat. §12-704c, as amended by Conn. Pub. Act No. 11-6, §111 (*effective May 4, 2011, and applicable to taxable years commencing on or after January 1, 2011*).

Trusts and Estates. The tax rate applicable to the Connecticut taxable income of trusts and estates is increased from 6.5% to 6.7% as of January 1, 2011. Conn. Gen. Stat. §12-700(a)(8)(E), as added by Conn. Pub. Act No. 11-6, §107 (effective May 4, 2011, and applicable to taxable years commencing on or after January 1, 2011).

Estimated Tax Payments. Any individual taxpayer required to make an estimated payment in September of 2011 is required to make a catch-up estimated tax payment in such month to account for any change in the rate of tax applicable to their 2011 Connecticut taxable income. Conn. Pub. Act No. 11-6, §109 (effective May 4, 2011). The due date for the September, 2011 estimated tax payment was later extended by the DRS to October 31, 2011, in response to Tropical Storm Irene and the Presidential Disaster Declaration for Connecticut, and then was extended again to November 15, 2011, due to ice storm Alfred.

Income Tax Withholding. The Department of Revenue Services issued new withholding tables for 2011 Connecticut income tax withholding to account for the new and increased marginal tax rates. The new withholding tables are effective August 1, 2011, and will require employers to impose “catch up” withholding for the remaining five months of the year. Nevertheless, a number of employers and payroll companies continue to experience issues implementing “catch-up” withholding if an employee receives supplemental income, such as bonus or overtime payments. In the case of payments of supplemental income after August 1st, the Department has issued Announcement 2011(6) and Form CT-W4T to help employers calculate the required withholding. For issues associated with “catch-up” withholding or supplemental income paid prior to August 1st, employers are encouraged to contact the Department to seek guidance and penalty relief. Conn. Pub. Act No. 11-6, §108 (effective May 4, 2011). See DRS Information Publication 2011(10.1), *Connecticut Income Tax Changes Affecting Withholding Requirements*, and DRS Announcement 2011(6), *Additional Guidance Regarding Withholding Calculation Rules for Supplemental Compensation and Use of Newly Issued Form CT-W4T*.

Nonresident Partner/Member/Shareholder Withholding. Since the required rate of withholding on the Connecticut source income of nonresident partners of a partnership, members of a limited liability company and shareholders of a Subchapter S corporation is the highest marginal income tax rate, the new marginal tax rate schedule increases the rate of withholding from 6.5% to 6.7%.

Withholding Tax Successor Liability. Commencing July 1, 2011, the purchaser of a business or stock of goods will become personally liable for the withholding tax liability of the seller, to the extent of the purchase price, if the purchaser fails to obtain a clearance certificate from the Commissioner of Revenue Services or to withhold a sufficient portion of the purchase price to pay all withholding taxes, interest and penalties until the seller produces a receipt from the Commissioner indicating that no such taxes are due. If the Commissioner fails to send a clearance certificate or notice of tax due within 60 days after the latest of (i) the date the Commissioner receives a written request from the purchaser for a certificate, (ii) the date of the sale or quitting of the business, or (iii) the date that the employer's records are made available to the Commissioner for audit, the purchaser is released from the obligation to withhold any portion of the purchase price. Conn. Gen. Stat. §12-707, as amended by Conn. Pub. Act No. 11-61, §58 (effective July 1, 2011, and applicable to sales of a business or stock of goods occurring on or after that date). See DRS Information Publication 2011(16), *Successor Liability for Sales and Use Taxes, Admissions and Dues Tax, and Connecticut Income Tax Withholding*.

Extended Withholding Tax Deficiency Assessment Deadline. Under new legislation, if an employer omits from Connecticut wages an amount properly includable that is in excess of 25% of the amount of Connecticut wages reported on a Connecticut withholding tax return, the period by when a proposed deficiency assessment for withholding taxes must be mailed is extended from three years to six years after the date on which the return is filed (unless the omitted amount is disclosed in the return or in a statement attached to the return). Similarly, if a pass-through entity, in filing a return, omits from the Connecticut adjusted gross income derived from Connecticut sources of a nonresident individual owner of an

interest in the pass-through entity, and the omitted income is more than 25% of the amount of Connecticut adjusted gross income derived from Connecticut sources reported on the return, the period by when a notice of proposed deficiency assessment must be mailed to the nonresident individual owner is extended from three years to six years after the date on which the return is filed (unless the omitted amount is disclosed in the return or in a statement attached to the return). Conn. Gen. Stat. §12-733(b), as amended by Conn. Pub. Act No. 11-61, §59 (*effective June 21, 2011, and applicable to taxable years commencing on or after January 1, 2011*).

Nonpayroll Payments Tax Withholding. Under existing law, the Commissioner of Revenue Services can require employers with more than \$2,000 in annual income tax withholding liability from wages to remit the withholding taxes electronically. The Commissioner can now also require electronic payments from any payers that had more than \$2,000 in income tax withholding from nonpayroll amounts (e.g., payments of gambling winnings to Connecticut residents over \$5,000; reportable Connecticut lottery winnings; pension and annuity distributions and military retirement paid to Connecticut residents requesting state income tax withholding; unemployment compensation paid to those requesting state income tax withholding; and nonwage payments to athletes and entertainers when withholding is required). Conn. Gen. Stat. § 12-686(a)(3), as amended by Conn. Pub. Act No. 11-61, § 57 (*effective July 1, 2011, and applicable to tax periods ending on or after said date*). See DRS Information Publication 2011(8), *Connecticut Tax Guide for Payers of Nonpayroll Amounts*.

Earned Income Tax Credit. Applicable to tax years commencing on or after January 1, 2011, a Connecticut resident subject to the Connecticut personal income tax generally is entitled to claim a tax credit against the taxpayer's Connecticut tax equal to 25% of the amount of the taxpayer's federal earned income credit. The credit is refundable to the extent that the credit exceeds the taxpayer's liability for Connecticut income tax, but would not earn interest in the event of a late payment of the refund. Conn. Pub. Act No. 11-6, §110 (*effective May 4, 2011, and applicable to taxable years commencing on or after January 1, 2011*), as amended by Conn. Pub. Act No. 11-1 (June Spec. Sess.), §§3-4 (*effective July 1, 2011, and applicable to taxable years commencing on or after January 1, 2011*).

Learn Here, Live Here Program. The Department of Economic and Community Development ("DECD") is directed to establish the Learn Here, Live Here Program to assist in the purchase of a first home in Connecticut by a person who graduates on or after January 1, 2014 from either (i) a regional vocational-technical school or (ii) if the person qualified as an in-state student and paid the in-state tuition rate, a Connecticut public institution of higher education. A qualifying person can apply to the DECD to have up to an annual maximum of \$2,500 of their Connecticut income tax liability segregated into a Connecticut first-time homebuyers account. (The annual total segregated amount for all participants in the program is capped at \$1 million.) For a period up to ten years after graduation, the person can apply to the DECD for a payment to be issued, up to the segregated amount, and used for a down payment on a Connecticut house if it is the first house purchased by the person. If the person ceases to live in Connecticut within five years, the person will be required to repay a percentage of the payment. Conn. Pub. Act No. 11-140, §§30-31 (*effective July 1, 2011*).

Lottery Winnings Set-Off. Effective January 1, 2012, when any person redeems a winning lottery ticket worth \$5,000 or more at the central office of the Connecticut Lottery Corporation (the "CLC"), the CLC is required to determine whether the person is a delinquent taxpayer based upon a list provided by the Commissioner of Revenue Services and, if so, deduct and withhold from the lottery prize payment the amount of the delinquent taxes, interest and penalties. Conn. Pub. Act No. 11-13, §1 (*effective October 1, 2011*).

CORPORATION BUSINESS TAX

I. Legislation

Surcharge Continued and Increased for Two Years. The 10% surcharge on the corporation business tax, that was to be applicable only to income years commencing prior to January 1, 2012, is extended for two additional years, through income years commencing prior to January 1, 2014, and is increased to 20% for each of those two additional years. As under current law, the surcharge is calculated based upon the tax liability of the Subchapter C corporation, excluding any credits, whether calculated based upon the corporation's net income or capital base, and is imposed on the corporation unless either (i) the tax liability of the corporation is equal to \$250 (i.e. the minimum tax) or (ii) the annual gross income of the corporation is less than \$100 million. The \$100 million annual gross income exemption is not available to a corporation that files a combined or unitary return. Conn. Gen. Stat. §§12-214(b)(7) and 12-219(b)(7), added by Conn. Pub. Act No. 11-6, §§76, 79 (effective May 4, 2011, and applicable to income years commencing on or after January 1, 2011).

Estimated Corporation Business Tax Overpayments. If a corporation timely files its Connecticut corporation business tax return, and the return shows an overpayment for the tax year, the corporation will be able to credit such overpayment against the corporation's estimated tax for the succeeding tax year, and the payment will be treated as paid on the due date of the first required installment of estimated tax for that succeeding tax year. Such reported overpayments shall be credited against otherwise unpaid installments in the order they would ordinarily become due. Conn. Gen. Stat. §12-242g, as amended by Conn. Pub. Act No. 11-61, §56 (effective October 1, 2011, and applicable to estimated corporation business tax payments for income years commencing on or after January 1, 2012).

Economic Nexus. The economic nexus statute is amended to provide that an out-of-state corporation will not be liable for the Connecticut corporation business tax if it otherwise is not transacting business in Connecticut and does not have a physical presence in Connecticut unless the corporation derives income from sources within the state and it has a substantial economic presence in this state. The economic nexus statute is further amended to provide that it will not apply to any corporation that is treated as a foreign corporation under the Internal Revenue Code and has no income effectively connected with a United States trade or business. If the foreign corporation does have income effectively connected with a United States trade or business, its gross income shall be such effectively connected income and, for net income tax apportionment purposes, only property used in, payroll attributable to and receipts effectively connected with the foreign corporation's United States trade or business shall be considered for purposes of calculating the corporation's apportionment fraction. Conn. Gen. Stat. §12-216a, as amended by Conn. Pub. Act No. 11-61, §55 (effective June 21, 2011, and applicable to income years commencing on or after January 1, 2011).

Manufacturing Reinvestment Account. The Department of Economic and Community Development is authorized to select not more than 100 manufacturers, each of which must have not more than 50 employees, to participate in a program where they may be able to reduce their liability for Connecticut tax. A qualifying manufacturer will be entitled to establish an interest-bearing manufacturing reinvestment account with a Connecticut bank and contribute annually to that account an amount not to exceed the lesser of (i) \$50,000 in income years commencing in 2011 (\$100,000 in income years commencing in 2012 or thereafter) or (ii) the manufacturer's gross receipts. Such contributions will be deductible for purposes of the corporation business tax. The manufacturer may use distributions from the account to purchase machinery, equipment or manufacturing facilities or for workforce training, development or expansion, and those distributions will be subject to tax at the reduced rate of 3.5% regardless of corporation business structure. Any money remaining in the account at the end of five years and any interest earned that results in the account exceeding the statutory limits are to be returned to the taxpayer and the taxpayer must pay the full tax due thereon, at the generally

applicable tax rate, within 60 days of receipt. Conn. Pub. Act No. 11-140, §4 (*effective July 1, 2011, and applicable to income years commencing on or after January 1, 2011*), as amended by Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.) §18 (*effective October 27, 2011*); Conn. Pub. Act No. 11-140, §5 (*effective July 1, 2011 and applicable to income years commencing on or after January 1, 2012*).

TAX CREDITS

I. Legislation

Credit Cap Reduction and Relief. Under prior law, the amount of tax credit or credits allowable against the corporation business tax or the insurance premium/subscriber charge tax generally could not exceed 70% of the amount of tax due. The applicable statutory provision for the insurance premium/subscriber charge tax is amended to lower the cap on credits generally to 30% of the amount of tax due for taxpayers subject to that tax for the 2011 and 2012 tax years; however, (i) the cap is lowered only to 55% for each of the film production tax credit, the entertainment industry infrastructure tax credit and the digital animation production companies tax credit provided in Conn. Gen. Stat. §§12-217jj, 12-217kk and 217ll, (ii) the 70% cap remains applicable to the Connecticut insurance reinvestment fund tax credit provided in Conn. Gen. Stat. §38a-88a, and (iii) the legislation establishes the order in which credit types must be claimed against the insurance premium/subscriber charge tax. The new legislation further permits a taxpayer to exceed the 70% cap or 30% cap, as applicable, by an amount equal to \$6,000 multiplied by the taxpayer's "average monthly net employee gain" for the year, which is determined by adding the total increase in employees for the applicable year and dividing by 12. In the case of a taxpayer subject to the corporation business tax, the relief from the 70% cap is available for an income year commencing on or after January 1, 2011, and prior to January 1, 2013, and will be based upon the average monthly net employee gain for the income year. In the case of a taxpayer subject to the insurance premium/subscriber charge tax, the new, two-year 30% cap limit would be applied on a calendar year basis, and the cap relief would be available during, and based upon the average monthly net employee gain for, the 2011 and 2012 calendar years. In both cases, the aggregate credits allowed may not exceed the total tax liability of the taxpayer. For purposes of determining whether there has been a "net employee gain," only employees who are required to work at least 35 hours per week and who were not employed in Connecticut by a related party within 12 months before the applicable calendar year will be counted. Conn. Gen. Stat. §§12-211a and 12-217zz, as amended by Conn. Pub. Act No. 11-6, §§75, 78 (*effective May 4, 2011, and applicable to income years commencing on or after January 1, 2011*), as further amended by Conn. Pub. Act No. 11-61, §48 (*effective June 21, 2011, and applicable to calendar years commencing on or after January 1, 2011*), as further amended by Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.), §54 (*effective October 27, 2011*).

First Five (Plus) Program. New legislation adopted during the regular legislative session directs the Department of Economic and Community Development (the "DECD") to establish a "First Five Program" whereby the DECD may provide "substantial financial assistance" to up to five business development projects in each of the 2012 and 2013 fiscal years. In order to be eligible, an applicant with a business development project must commit to (i) create not less than 200 new jobs within 24 months from the date its application is approved or (ii) invest not less than \$25 million and create not less than 200 new jobs within five years from the date such application is approved. If the DECD certifies the eligibility of a project, it must still be approved by the Governor. The legislation does not provide expressly what constitutes "substantial financial assistance," but implicitly suggests funding may come from Manufacturing Assistance Act funds, the Urban and Industrial Sites Reinvestment Program and other tax credit programs by waiving certain funding and credit limitation provisions for First Five Program projects (including the limitation on credits against the insurance premium/subscriber charge tax). Conn. Pub. Act No. 11-86, §1 (*effective July 1, 2011*). During the October special session, the General Assembly expanded the now-called "First Five Plus Program" to allow the DECD to provide state assistance to up to five additional business development projects (for a total of ten) during the 2012 fiscal year. The eligibility criteria for

projects remain the same, but the DECD may now give preference to projects involving the relocation of an out-of-state or international manufacturer or corporate headquarters. Conn. Pub. Act No. 11-86, §1, amended by Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.), §38 (*effective October 27, 2011*).

New Job Expansion Tax Credit. A new job expansion tax credit has been enacted for jobs created between January 1, 2012 and January 1, 2014, that can be applied against the insurance premium, corporation business, utility company or personal income tax. To be eligible to claim the credit, the taxpayer must apply to the Department of Economic and Community Development (“DECD”), be subject to one of the foregoing taxes and have been in business for at least 12 consecutive months prior to the date of the taxpayer’s application to the DECD. The credit is \$500 per month for each new employee who is a Connecticut resident, or \$900 per month if, at the time of hiring, the new employee is (i) receiving unemployment compensation benefits or has not had a full-time job since exhausting his or her unemployment benefits, (ii) a current armed forces member or one who was honorably discharged or released from active service, or (iii) receiving vocational rehabilitation services from the Bureau of Rehabilitative Services. To be eligible for the credit, the job must not have existed in Connecticut before the DECD application, and it must require the new employee to work at least (i) 35 hours per week for at least 48 weeks per calendar year or (ii) 20 hours per week for at least 48 weeks per calendar year if the employee is receiving vocational rehabilitation services or unemployment compensation or has not had a full-time job since exhausting his or her unemployment benefits. (A new employee does not count if the employee was employed in Connecticut by a related person during the prior 12 months, owns the business or is a member or partner in it, or no longer works for the business at the end of its income year.) In addition, to be eligible for the credit, the taxpayer must employ a certain minimum number of new employees based upon the number of employees of the taxpayer as of the time of the filing of the DECD application: (i) at least one new job for an employer that already then employs not more than 50 full-time employees; (ii) at least five new jobs for an employer that already employs more than 50 but not more than 100 full-time employees; and (iii) at least ten new jobs for an employer that already then employs more than 100 full-time employees. The credit must be claimed in the income year in which the job is created, but can be claimed for each of the two subsequent years if the employee held the job for the full year. Unused credits will expire and cannot be refunded. Shareholders of subchapter S corporations and partners of partnerships may claim the credit. The new job expansion credit is subject to the same aggregate \$20 million-per-year cap that currently applies to the three existing job creation credits (discussed below). Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.), §19 (*effective January 1, 2012, and applicable to income or taxable years commencing on or after January 1, 2012*).

Other Job Creation Tax Credit Programs. During the regular legislative session, the General Assembly enacted two conflicting amendments to the pre-existing job creation tax credits. First, effective July 1, 2011, the aggregate limit on tax credits granted under the jobs creation tax credit program, the qualified small business job creation tax program and the vocational rehabilitation job creation tax credit program was increased from \$11 million to \$20 million in any one fiscal year. Conn. Gen. Stat. §§12-217ii, 12-217nn and 12-217oo, as amended by Conn. Pub. Act No. 11-6, §§130-132 (*effective July 1, 2011*). The General Assembly then adopted legislation, also effective July 1, 2011, increasing the aggregate limit on tax credits granted under the jobs creation tax credit program alone to \$20 million in any one fiscal year. Conn. Gen. Stat. §12-217ii, as amended by Conn. Pub. Act No. 11-86, §3 (*effective July 1, 2011*). During the October special session, in coordination with the effective date of January 1, 2012 for the new job expansion credit program (summarized above), the General Assembly adopted legislation phasing out the three pre-existing job creation tax programs. No eligibility certificates will be issued after December 31, 2011 under the jobs creation tax credit program (and no credit can be granted more than five years after the issuance of an eligibility certificate), and the rehabilitation job creation tax credit program will not be available for employees hired in any income year commencing on or after January 1, 2012. By its original terms, the small business jobs creation tax credit is available only for employees hired during income years commencing prior to January 1, 2013. As noted above, the \$20 million aggregate cap on the three pre-existing tax credit programs was extended to include credits granted under the new job expansion tax credit program. Conn. Gen. Stat. §§12-217ii, 12-217nn and 12-217oo, as amended by Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.), §§20-22 (*effective October 27, 2011*).

Urban and Industrial Site Reinvestment Program. The limit on the sum of all tax credits allowed under the Urban and Industrial Site Reinvestment Program was increased from \$500 million to \$750 million during the regular legislative session, and then was reduced to \$650 million during the October special session. Conn. Gen. Stat. §32-9t(i)(1), as amended by Conn. Pub. Act No. 11-86, §2 (*effective July 1, 2011*), as amended further by Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.), §48 (*effective October 27, 2011*). The provisions governing the urban and industrial site reinvestment tax credits are further amended to permit a taxpayer to claim both the state credit and the federal new markets tax credit for the same investment. In general, a taxpayer can invest directly or indirectly in an eligible urban and industrial sites project through a state-registered investment fund or a qualified community development entity (a "CDE"). A CDE is a business entity created to receive new markets tax credits. The legislation creates a separate category of CDEs through which investors may claim the state credit as well as if (i) the CDE has entered into an allocation agreement with the Community Development Financial Institutions Fund for a share of new markets tax credits and (ii) the CDE's respective service areas in the allocation agreement include Connecticut. Conn. Gen. Stat. §32-94, as amended by Conn. Pub. Act No. 11-78, §1 (*effective July 1, 2011*).

Angel Investor Credit Program. The angel investor tax credit program, that is administered by the DECD, is available to taxpayers who make cash investments in qualified securities in certain Connecticut start-up, technology-based businesses. The governing statute was amended to: (i) reduce the minimum cash investment a taxpayer must make to qualify for a credit from \$100,000 to \$25,000. Conn. Gen. Stat. §12-704d(b), as amended by Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.), §29 (*effective October 27, 2011*); and (ii) provide that a business seeking to qualify as a recipient of cash investments eligible for the credit no longer needs to disclose its proprietary technology as part of its application to the State. Conn. Gen. Stat. §12-704d(d)(1), as amended by Conn. Pub. Act No. 11-254, §1 (*effective July 1, 2011, and applicable to taxable years commencing on or after January 1, 2011*).

Film Production Tax Credit. During the regular legislative session, the General Assembly acted to put constraints on the film production tax credit program. The ability of a taxpayer to transfer film production tax credits generally will now be limited if: (i) the transferring taxpayer is neither subject to the corporation business tax nor to the insurance premium/subscriber charge tax; and (ii) the transferring taxpayer does not own, directly or indirectly, at least 50% of a business entity subject to the Connecticut business entity tax. The limitation would prevent such a taxpayer from transferring more than 50% of its film production tax credits in any one year in the case of credits allowed for the 2011 income year, and more than 25% of any such credits in any one year in the case of a credit allowed for any subsequent year. The new limitation will not apply to credits issued for any qualified production that is created in whole or in significant part, as determined by the Department of Economic and Community Development ("DECD"), at a "qualified production facility." A "qualified production facility" means a facility: (i) located in Connecticut; (ii) intended for film, television or digital media production; and (iii) that has a minimum investment of \$3 million (or less if approved by the DECD). The minimum share of principal photography days that a production company must spend in Connecticut in order to qualify for the film production tax credit is increased from 25% to 50%. Conn. Gen. Stat. §12-217jj, as amended by Conn. Pub. Act No. 11-6, §77 (*effective May 4, 2011, and applicable to income years commencing on or after January 1, 2011*), as further amended by Conn. Pub. Act No. 11-61, §37 (*effective July 1, 2011*). During the October special session, the General Assembly adopted legislation to extend the film production tax credit program to a "relocated television production." A "relocated television production" is defined generally as an eligible production company's ongoing television program that: (i) has filmed all of its prior seasons outside of Connecticut; (ii) may include current event shows, other than a general news program, sporting event, or game broadcast; and (iii) is created at a Connecticut qualified production facility at which, on or after January 1, 2012, the eligible production company makes a minimum investment of \$25 million and creates at least 200 jobs. Conn. Gen. Stat. §12-217jj(a), as amended by Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.), §53 (*effective October 27, 2011*).

Entertainment Industry Infrastructure Tax Credit. The tax credit program was amended to permit a taxpayer claiming all or part of the film infrastructure tax credit to claim the credit in the income year in which the infrastructure investments are made or in any of the three immediately succeeding income years. By law, unchanged by the bill, an assignee of a film infrastructure tax credit may claim the credit only in the year in which the investment is made. Conn. Gen. Stat. §12-217kk(b)(4), as amended by Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.), §55 (*effective October 27, 2011*).

New Insurance Reinvestment Fund Tax Credit. The governing statute is amended to permit a taxpayer who is allowed a credit under the 2010 legislation creating a new insurance reinvestment fund tax credit to transfer the credit to an affiliate of the taxpayer. Conn. Gen. Stat. §38a-88a(g), as amended by Conn. Pub. Act No. 11-140, §2 (*effective July 8, 2011*).

Neighborhood Assistance Act. The Neighborhood Assistance Act, which provides business tax credits to companies that invest in certain municipally-approved community activities and programs, is amended to: (i) extend tax credit eligibility to taxpayers that are subject to the business entity tax; (ii) increase the total amount of credits a taxpayer annually may claim from \$75,000 to \$150,000; and (iii) eliminate the requirement that in order to be eligible for the credit, a taxpayer's charitable contributions for the year must at least equal its total contributions in the previous year. Conn. Gen. Stat. §§12-631 and 12-632, as amended by Conn. Pub. Act No. 11-140, §§27-28 (*effective October 1, 2011*).

Historic Preservation Tax Credits. The Connecticut Commission on Culture and Tourism has been eliminated and its powers, duties and programs have been transferred to the Department of Economic and Community Development ("DECD"). The DECD, with assistance from the State Historic Preservation Officer, will be responsible for the administration of the tax credit programs for the rehabilitation of historic homes, certified historic structures and certified historic structures for mixed-use or affordable housing. The tax credit for the rehabilitation of certified historic structures is further amended to expand the definition of "certified historic structure" to additionally encompass certified historic cultural buildings, institutional property, former municipal, state or federal government property, and residential property of more than four units. The tax credit for the rehabilitation of certified historic structures for mixed use or affordable housing also has been amended to: (i) expand the definition of "certified historic structure" to include former municipal, state or federal government property, cultural buildings, and institutional or mixed residential and nonresidential property; (ii) expand the range of eligible reuses by amending the definition of "certified rehabilitation" to include solely nonresidential use; and (iii) permit the owner to seek certification of compliance with the rehabilitation plan at the end of phases to an identifiable portion of a building rather than only upon completion. Conn. Gen. Stat. §§10-416, 10-416a and 10-416b, as amended by Conn. Pub. Act No. 11-48, §§120-122 (*effective July 1, 2011, and applicable to income years commencing on or after January 1, 2011*).

SALES AND USE TAX

I. Legislation

Rate Increases. The following base sales and use tax rates have been increased effective July 1, 2011:

- **General Sales and Use Tax Rate.** The general sales and use tax rate is increased from 6.0% to 6.35% for sales occurring on or after July 1, 2011.
- **Room Occupancy Tax Rate.** The room occupancy tax rate is increased from 12% to 15% as of July 1, 2011.
- **Motor Vehicle Rental or Lease Tax Rate.** As of July 1, 2011, the sales and use tax rate for the rental or lease of a passenger motor vehicle for a period of 30 days or less is increased from 6.0% to 9.35%.

- **Luxury Item Sales and Use Tax Rate.** Commencing July 1, 2011, the sale of the following “luxury” items are subject to a tax of 7.0% on the full purchase price: (i) a motor vehicle with a sales price exceeding \$50,000 (excluding motor vehicles purchased by nonresident members of the armed forces, motor vehicles having a gross vehicle weight rating over 12,500 pounds or having a gross vehicle weight rating of 12,500 pounds or less that is not used for private passenger purposes, but is designed or used to transport merchandise, freight or persons in connection with any business enterprise and issued a commercial registration or more specific type of registration by the Department of Motor Vehicles); (ii) a vessel with a sales price exceeding \$100,000; (iii) jewelry with a sales price exceeding \$5,000; and (iv) an article of clothing or footwear, a handbag, an article of luggage, umbrella, wallet or watch for a sales price exceeding \$1,000. See DRS Special Notice 2011 (10), *2011 Legislative Changes Affecting Motor Vehicles*, for important transition rules applicable to motor vehicle sales and leases.

- **Transition Rules.** In DRS Special Notice 2011(9), *2011 Legislative Changes Affecting Sales and Use Taxes*, the DRS published the following administrative rules governing the transition to the new sales and use tax rates, including the following:
 - The new rates will not apply to any sale of tangible personal property occurring on or after July 1, 2011, if made under a binding sales contract without an escalator clause that was entered into prior to July 1, 2011, where delivery is made within 90 days after July 1, 2011.
 - In the case of a lease of tangible personal property, the new rates will apply to lease payments due and owing on or after July 1, 2011.
 - In the case of the rental of a passenger motor vehicle for a period of 30 consecutive calendar days or less, the new 9.35% rate only applies to the portion of the rental term occurring on or after July 1, 2011.
 - Sales of gas and electricity for periods that straddle July 1, 2011, should be apportioned based upon the number of days during such period that occur prior to July 1, 2011 and the number of days during such period that occur on or after July 1, 2011, with the new rates applying only to the portion of the sale apportioned to the period on or after July 1, 2011.
 - Sales of services for periods that straddle July 1, 2011, will not be subject to the higher tax rates if payment was made on or before May 4, 2011. If payment is made after May 4, 2011, sales of services that straddle July 1, 2011, or are performed only on or after July 1, 2011, are fully taxable at the new higher tax rates. Payments after July 1, 2011, for services rendered prior to that date, are subject to the tax rate applicable when the service was rendered.

 - When a period of hotel occupancy straddles July 1, 2011, the new higher rate applies only to the portion of the occupancy occurring on or after July 1, 2011.

- **Municipal Revenue Sharing Account.** For calendar quarters ending on or after September 30, 2011, the Commissioner of Revenue Services is to deposit into a new “municipal revenue sharing account” an amount equal to the sum of (i) 1.57% of the amounts received by the State from the general 6.35% sales and use tax; and (ii) 1.43% of the amounts received by the State from the sales and use tax on luxury items. The money in the account is to be expended by the Secretary of OPM on a quarterly basis for “manufacturing transition grants” to municipalities. The grants are to equal the amount each municipality received (or estimated would have received if timely requested) in the 2011 fiscal year as a payment in lieu of taxes (PILOT) for eligible commercial vehicles and manufacturing machinery and equipment. If there are insufficient funds in the account, all grants are to be reduced proportionately. If, on the other hand, there are excess funds in the account remaining after the payment of such grants, any remaining funds are to be disbursed to municipalities according to a statutory formula.

- **Regional Performance Incentive Account.** For calendar quarters ending on or after September 30, 2011, the Commissioner of Revenue Services is to deposit into a new “regional performance incentive account” an amount equal to the sum of: (i) 6.7% of the amounts received by the State from the occupancy tax; and (ii) 10.7% of the amounts received by the State from the sales and use tax on rental or leased motor vehicles. The money in the account is to be expended by the Secretary of OPM for grants to regional entities to provide a local service on a regional basis.

Conn. Gen. Stat. §§12-408(1) and (3), 12-411(1), 12-411b and 12-414(3), as amended by Conn. Pub. Act No. 11-6, §§93-97, 103, 126-127, as further amended by Conn. Pub. Act No. 11-61, §§42-44 and 183 (*effective July 1, 2011, and applicable to sales occurring on or after that date, and to sales of services that are billed to customers for a period that includes such date*). See DRS Special Notice 2011(9), *2011 Legislative Changes Affecting Sales and Use Taxes*.

Numerous Sales Tax Exemptions Repealed. The following exemptions from the Connecticut sales and use tax are repealed, thereby rendering sales or use of these services or property subject to sales tax, effective for sales occurring on or after July 1, 2011:

- Voluntary evaluation, prevention, treatment, containment or removal of hazardous waste or other contaminants of air, water or soil when rendered to industrial, commercial or income-producing property. Conn. Gen. Stat. §12-407(a)(37)(I), as amended by Conn. Pub. Act No. 11-6, §88 (*effective July 1, 2011, and applicable to sales occurring on or after said date*).
- Valet parking provided at any airport. Conn. Gen. Stat. §12-407(a)(37)(N), as amended by Conn. Pub. Act No. 11-6, §89 (*effective July 1, 2011, and applicable to sales occurring on or after said date*).
- Yoga instruction provided at a yoga studio. Conn. Gen. Stat. §12-407(a)(37)(FF), as amended by Conn. Pub. Act No. 11-6, §91 (*effective July 1, 2011, and applicable to sales occurring on or after said date*).
- Articles of clothing or footwear costing under \$50 (thereby rendering sales of clothing and footwear generally subject to tax). Conn. Gen. Stat. §§12-412(47) as repealed by Conn. Pub. Act No. 11-6, §166 (*effective July 1, 2011, and applicable to sales occurring on or after said date*). [Note that the exemption for services of an agent selling on consignment articles of clothing or footwear, and jewelry, handbags, luggage, umbrellas, wallets, watches and similar items, exclusive of services provided by an auctioneer, was repealed and then restored. Conn. Gen. Stat. §12-407(a)(37)(S), as repealed by Conn. Pub. Act No. 11-6, §90, and restored by Conn. Pub. Act No. 11-61, §40 (*effective July 1, 2011, and applicable to sales occurring on or after said date*). *The annual one-week period when sales of certain clothing and footwear costing under \$300 is exempt from sales and use tax will run from August 21, 2011 through August 27, 2011.*]
- Nonprescription drugs and medicines. Conn. Gen. Stat. §12-412(48), as repealed by Conn. Pub. Act No. 11-6, §166 (*effective July 1, 2011, and applicable to sales occurring on or after said date*).
- Cloth or fabric purchased for noncommercial sewing. Conn. Gen. Stat. §12-412(52), as repealed by Conn. Pub. Act No. 11-6, §166 (*effective July 1, 2011, and applicable to sales occurring on or after said date*).
- Yarn for noncommercial use. Conn. Gen. Stat. §12-412(97), as repealed by Conn. Pub. Act No. 11-6, §166 (*effective July 1, 2011, and applicable to sales occurring on or after said date*).
- Products that aid in the cessation of smoking. Conn. Gen. Stat. §12-412(111), as repealed by Conn. Pub. Act No. 11-6, §166 (*effective July 1, 2011, and applicable to sales occurring on or after said date*).

Ed. note. The exemption for services or tangible personal property used or consumed in operating solid waste-to-energy facilities was repealed and then reinstated during the legislative session. Conn. Gen. Stat. §12-412(95), as repealed by Conn. Pub. Act No. 11-6, §166 (*effective July 1, 2011, and applicable to sales occurring on or after said date*), and reinstated by Conn. Pub. Act No. 11-61, §184 (*effective June 21, 2011*).

New Taxable Services. The following new services are subject to the sales and use tax effective July 1, 2011:

- Motor vehicle storage services (including motor homes, campers and camp trailers)
- Packing and crating services (to the extent not already subject to the tax in connection with the sale of tangible personal property)
- Motor vehicle towing and road services
- Intrastate transportation services provided by livery services (but not including transportation by taxicab, motorbus, ambulance or ambulette, scheduled public transportation, nonemergency medical transportation provided under the Medicaid program, paratransit services provided by agreement or arrangement with the state or any political subdivision of the state, dial-a-ride services or services provided in connection with funerals)
- Pet grooming and pet boarding services, except when such services are provided as an integral part of professional veterinary services, and pet obedience services
- Services in connection with a cosmetic medical procedure [N.B. Reconstructive surgery is statutorily excluded from the definition of “cosmetic medical procedures” and the DRS has excluded laser eye surgery, dental procedures and circumcisions.]
- Manicure and pedicure services and all other nail services
- Spa services, regardless of where performed, including body waxing and wraps, peels, scrubs and facials (but massage services by a licensed massage therapist remain nontaxable)

Conn. Gen. Stat. §§12-407(a)(37)(GG)-(NN), as added by Conn. Pub. Act No. 11-6, §92, and amended by Conn. Pub. Act No. 11-61, §41 (*effective July 1, 2011, and applicable to sales occurring on or after said date*).

Sales and Use Tax Collection by Remote Sellers (the “Amazon” Rule). A new rule has been established that will compel certain out-of-state retailers to register and collect sales tax on sales to Connecticut residents and businesses. Under the new “nexus” rule, a retailer that does not have a physical presence in Connecticut must collect and remit sales tax on its taxable sales to Connecticut if the retailer sells taxable tangible personal property or services through an agreement with another person located in Connecticut, under which such person located in Connecticut, for a commission or other consideration that is based upon the sale of tangible personal property or services by the retailer, directly or indirectly refers potential customers, whether by a link on an Internet website or otherwise, to the retailer, and the cumulative gross receipts from sales by the retailer to Connecticut customers who are referred to the retailer by all such persons with such agreements is in excess of \$2,000 during the preceding four quarterly periods. [Ed. note. Similar legislation has been enacted in other jurisdictions and is the subject of a constitutional challenge in a case brought by Amazon.com in New York.] Conn. Gen. Stat. §12-407(a)(12), as amended by Conn. Pub. Act No. 11-6, §128, as further

amended by Conn. Pub. Act No. 11-61, §§46 and 185 (effective May 4, 2011, and applicable to sales occurring on and after that date), and Conn. Gen. Stat. §12-407(a)(15)(A), as amended by Conn. Pub. Act No. 11-61, §47 (effective June 21, 2011, and applicable to sales occurring on and after May 4, 2011).

Nonresident Contractors. To secure payment of Connecticut taxes in connection with a nonresident contractor's in-state activities, Connecticut law requires a person doing business with the nonresident contractor to comply with certain security requirements or the person can become liable for taxes related to the project on which the nonresident contractor works. The governing statute has been amended to revise the security requirements and to apply them to any nonresident contractor who is not a "verified contractor" (i.e. a nonresident contractor who is registered for all applicable taxes with the DRS, has filed all required tax returns with the DRS, has no outstanding liabilities with the DRS and is treated as a verified contractor by the DRS). Under the new law, a person doing business with a prime or general contractor who is an "unverified contractor" must obtain proof that the contractor has posted with the DRS a good and valid bond with a surety company authorized to do business in Connecticut in an amount equal to 5% of the contract price. If the person fails to comply with this requirement, the person can be held personally liable for the sales and use tax and withholding tax liability of the unverified contractor arising from the activities of the contractor on the project. The DRS, upon request, is to verify whether a contractor is a resident or nonresident contractor, whether a nonresident contractor is a verified contractor and whether a valid bond has been posted with the DRS. In a similar manner, a resident or verified general or prime contractor or a resident or verified subcontractor is required to determine whether a nonresident subcontractor with which they contract is a verified contractor; however, if the nonresident subcontractor is an unverified contractor, the resident or verified general or prime contractor or subcontractor is required to: (i) hold back an amount equal to 5% of the payments due to such unverified subcontractor until the unverified subcontractor furnishes a certificate of compliance from the DRS authorizing the full or partial release of those funds; and (ii) provide notice of such hold back requirement to the unverified subcontractor no later than the time of commencement of work under the contract with such unverified subcontractor. The governing statute is also amended to clarify the protections of parties who comply with its provisions and that it is not applicable to any contract in which the contract price for the entire project is less than \$250,000. Conn. Gen. Stat. §12-430(7), as amended by Conn. Pub. Act No. 11-61, §66 (effective October 1, 2011). See DRS Special Notice 2011(17), *2011 Legislative Changes to the Procedures Governing Nonresident Contractors*.

Motor Vehicles Equipped for the Disabled. A new retroactive exemption was enacted exempting that portion of the sales price of a motor vehicle attributable to special equipment installed in the vehicle exclusively for the use of a person with physical disabilities. Conn. Gen. Stat. §§12-412(80) and 12-431, as amended by Conn. Pub. Act No. 11-61, §§60-61 (effective June 21, 2011, and applicable to all open tax periods).

II. Cases

Vehicle Registration Renewal Fees. In *HVT, Inc. v. Law*, 300 Conn. 623 (2011), the Connecticut Supreme Court held that vehicle registration renewal fees paid by lessees under motor vehicle lease agreements constitute "gross receipts" of the lessor subject to the Connecticut sales and use tax. The Court noted that the vehicle registration renewal fees were the primary obligation of the lessor, and not a shared obligation, and that the fees did not have to be paid to the lessor to be "gross receipts." The Court distinguished the *AirKaman* decision, wherein the Court held that a service provider could pass through, without sales tax, the reimbursement of payroll-related expenses paid by the service provider because the obligation to provide fixed base operation services in *AirKaman* was the primary contractual duty of the service recipient; the Court found the retention of personnel by the service provider was as an agent on behalf of the service recipient. In *HVT*, the lessee was paying an obligation of the lessor and the fees must be added to the gross receipts received under the lease.

Adequate Business Records. In Alexandre v. Commissioner, 300 Conn. 566 (2011), the Connecticut Supreme Court held that the taxpayer's failure to maintain cash register tapes showing individual transactions permitted the Department of Revenue Services to utilize the alternative industry standard mark-up method when auditing the taxpayer. The taxpayer, who owned and operated a nightclub and banquet facility, provided daily sales reconciliation reports and a copy of the cash register "Z tape" or "Z report" that contained the date, the sequence number and the total amount of cash rung through the register. The Court concluded that the failure to retain and provide detailed cash register tapes violated the express requirement to maintain those tapes under Section 12-2-12(b)(1) of the Regulations of Connecticut State Agencies, and the taxpayer could not sustain his burden by providing the Z tapes.

No Private Action for Sales Tax Overcharge. In Blass v. Rite Aid of Connecticut, Inc., 127 Conn. App 569 (2011), the Connecticut Appellate Court affirmed the decision of the Superior Court dismissing the class action lawsuit filed by the plaintiff against the defendant retailer based upon the allegation that the defendant had failed to deduct the value of coupons before calculating the sales tax due on a sale. The plaintiff asserted that Rite Aid collected \$0.24 in sales tax on the total \$3.96 gross sales price for four items, before subtracting the full face value of two \$1.00 coupons that the plaintiff submitted as partial payment. Under Connecticut law, the full face value of a coupon used by the purchaser to reduce the price paid to the retailer for an item of tangible personal property is excluded from the term "gross receipts" and the term "sales price" for purposes of the sales tax. Conn. Gen. Stat. §§12-407(b)(9)(A) and (b)(8)(A). Rite Aid moved to dismiss the lawsuit based on the fact that plaintiff had failed to exhaust her administrative remedies under Connecticut's tax procedures for obtaining a sales tax refund. The Superior Court agreed, holding that plaintiff's claim should first be against the State of Connecticut, not Rite Aid (by the filing of a refund claim with the Commissioner of Revenue Services). The Court also concluded that the Connecticut Unfair Trade Practices Act (CUTPA) does not give a taxpayer the right to avoid exhausting her administrative remedies, as the miscollection of taxes "whether negligent or intentional, does not constitute an unfair or deceptive act or practice in the conduct of any trade or commerce under CUTPA."

Action Against State Auditors. In J.P. Alexandre, LLC v. Egbuna, 2011 Conn. Super. LEXIS 1082 (May 2, 2011), the plaintiffs filed a complaint against an auditor and an audit supervisor of the Connecticut Department of Revenue Services alleging certain improprieties on the part of the Department employees in the conduct of a sales and use tax audit. See Alexandre v. Commissioner summarized above under the heading "Adequate Business Records." The trial court granted the defendants' motion for summary judgment holding that: (i) the court was deprived of subject matter jurisdiction over the plaintiffs' state law claims because they failed to exhaust their administrative remedies and because they sought relief beyond the limited scope of Conn. Gen. Stat. §12-422; (ii) the plaintiffs' federal law claims under 42 U.S.C. §§1983 and 1985 must be dismissed for lack of subject matter jurisdiction because the plaintiffs had an adequate remedy under state law pursuant to Conn. Gen. Stat. §12-422; (iii) the defendants are entitled to the qualified immunity available to state officers and employees under Conn. Gen. Stat. §4-165, and the plaintiffs did not proffer evidence that the defendants did not act in good faith, or engaged in wanton, reckless or malicious misconduct, to overcome such immunity; and (iv) the plaintiffs failed to raise a genuine issue of material fact as to whether the defendants violated any of their constitutional rights.

Confidential Tax Returns. In a Memorandum of Decision dated August 26, 2011, issued in Rainforest Café Inc. v. Commissioner, Docket No. CV 05 4004842S, the Tax Session of the Superior Court ruled that the plaintiff taxpayer could not compel the Commissioner to produce the sales and use tax returns of the taxpayer's contractor. The Court noted that the issue in dispute is whether the taxpayer had filed a tax return within the three-year statute of limitations. Accordingly, the tax returns of the taxpayer's contractor were not relevant to this inquiry and the disclosure of the returns was prohibited by the confidentiality requirements of Conn. Gen. Stat. §12-15.

ESTATE AND GIFT TAXES

Taxable Estate Threshold. Effective for the estates of decedents dying on or after January 1, 2011, the taxable estate threshold is lowered from \$3.5 million to \$2.0 million. Conn. Gen. Stat. §§12-391(g), 12-392(b)(3), 12-398(e) and 45a-107, as amended by Conn. Pub. Act No. 11-6, §§84-86, 119 (*effective May 4, 2011, and applicable to estates of decedents dying on or after January 1, 2011*). As part of the budget implementation legislation, the Connecticut General Assembly validated probate court lien release certificates that were issued and recorded before May 4, 2011, in the town records where the decedent's property is located where the decedent's Connecticut taxable estate is more than \$2 million but not more than \$3.5 million. Conn. Gen. Stat. §12-398(e), as amended by Conn. Pub. Act No. 11-61, §39 (*effective June 21, 2011, and applicable to estates of decedents dying on or after January 1, 2011*). See DRS Special Notice 2011 (2), *2011 Legislative Changes Affecting the Connecticut Estate Tax and the Connecticut Gift Tax*.

Taxable Gift Threshold. Effective for Connecticut taxable gifts made by a donor on or after January 1, 2011, including the aggregate amounts of all Connecticut taxable gifts made by the donor during all calendar years commencing on or after January 1, 2005, the taxable threshold is lowered from \$3.5 million to \$2.0 million. Conn. Gen. Stat. §12-642(a), as amended by Conn. Pub. Act No. 11-6, §87 (*effective May 4, 2011, and applicable to gifts made during calendar years commencing on or after January 1, 2011*).

PROPERTY TAX

I. Legislation

Manufacturing Machinery and Equipment/Commercial Trucks and Vehicles Used to Transport Freight for Hire.

New legislation retains the current property tax exemptions for eligible manufacturing, biotechnology and recycling machinery and equipment, and for certain commercial trucks and other vehicles used to transport freight for hire, but: (i) eliminates the state payments in lieu of taxes for such lost municipal revenues; (ii) repeals certain OPM-related requirements associated with claiming the property tax exemptions, thereby shifting to municipal assessors responsibility for prescribing the documentation required to claim the exemptions; and (iii) eliminates the requirement that machinery and equipment owners file a supplement to their personal property declaration that sets forth certain data relating to the acquisition cost and depreciated value of the machinery and equipment. The legislation retains an existing state-reimbursed property tax exemption for eligible manufacturing machinery and equipment located in targeted investment communities, enterprise zones and the Bradley Airport Development Zone. The state makes an annual grant payment to towns to reimburse them for half of the revenue loss due to this five-year, 80% property tax exemption. Conn. Gen. Stat. §§12-63, 12-81(72), 12-81(76) and 12-81(74)(D), as amended by Conn. Pub. Act No. 11-61, §§1-3, 52 (*effective July 1, 2011*). Conn. Gen. Stat. §§12-94b, 12-94c, 12-94f and 12-94g, as repealed by Conn. Pub. Act No. 11-61, §189 (*effective July 1, 2011, and applicable to assessment years commencing on or after October 1, 2011*).

Electronic Billing. Effective October 1, 2011, a municipality will be able to send to a taxpayer by electronic mail a bill for current taxes, and a statement of the year and amount of any back taxes due, so long as: (i) the taxpayer consents in writing to receive them electronically; (ii) the municipality establishes a procedure to ensure that such taxpayer receives the bill and statement and is provided the municipality's return email address; and (iii) the municipality posts its email address on its website. Conn. Gen. Stat. §12-130(a), as amended by Conn. Pub. Act No. 11-185, §1 (*effective October 1, 2011, and applicable to assessment years commencing on or after October 1, 2011*).

Electronic Personal Property Declarations. Effective October 1, 2011, a taxpayer required to file a municipal declaration of personal property may sign and file the declaration electronically on a form provided by the assessor of the municipality, provided that the municipality (i) has the technological ability to accept electronic signatures, and (ii)

agrees to accept electronic signatures for annual declarations of personal property. In addition, an assessor can send to a taxpayer the personal property declaration form electronically, rather than by mail, if the taxpayer has requested, in writing, to receive the form electronically. Conn. Gen. Stat. §§12-41 and 12-43, as amended by Conn. Pub. Act No. 11-69, §§1-2 (effective October 1, 2011, and applicable to assessment years commencing on or after October 1, 2011).

Brownfields and Designated Rehabilitation Areas. Under current law, if the legislative body of a municipality approves an authorizing resolution, the municipality can agree to fix the assessment of a property located in a designated rehabilitation area if the owner of the property agrees to rehabilitate the property or build on it new multi-family rental or cooperative housing. Effective October 1, 2011, the governing statute is amended to allow such an agreement if the property is a brownfield (as defined in Conn. Gen. Stat. §32-9cc) and the owner agrees to construct new multi-family rental housing, cooperative housing, common interest communities or mixed-use or commercial structures on the property. Conn. Gen. Stat. §12-65e, as amended by Conn. Pub. Act No. 11-96, §1 (effective October 1, 2011).

Forest Land. Under current law, a property owner may enroll in the “10 mill program”: (i) property with a minimum of 25 acres that, excluding timber, has a value of up to \$100 per acre; (ii) timber land of more than ten years’ growth; and (iii) land stocked with trees up to ten years old. Land classified under this program is taxed based upon 100% of the true valuation established at the time of the classification. That valuation is frozen for a 50-year period and the tax rate for such land is up to 10 mills. At the end of the 50-year period, the land is revalued, and is again taxed at a rate up to 10 mills for another 50 years. If the classification is cancelled before the end of a 50-year period, the land will be taxed as other land and a penalty equal to five mills per year will be assessed on the difference in valuation. The governing statutes are amended such that, if approved by a municipality’s legislative body, the owners of designated forest land can convert, without penalty, from the “10 mill program” to the state’s forest preservation program under Conn. Gen. Stat. §12-107d (which does not require revaluation every 50 years). Alternatively, if the property remains in the “10 mill program,” the woodlands cannot be assessed at a tax rate exceeding similar properties classified as forest land under the state’s forest preservation program. Conn. Gen. Stat. §§12-96, 12-97 and 12-98, as amended by Conn. Pub. Act No. 11-198, §§1-3 (effective July 13, 2011).

Mobile Telecommunications Service Provider. During the 2010 legislative session, the Connecticut General Assembly enacted legislation providing that a mobile telecommunications service provider could no longer elect to participate in the special state personal property tax regime for telecommunications providers. Instead, commencing with the October 1, 2010 assessment year, these service providers are required to pay personal property tax directly to the municipality or municipalities in which their personal property is located. Although such property taxes for the October 1, 2010 assessment year would ordinarily be billed in July 2011 and January 2012, legislation adopted during the 2011 legislative session allows a municipality, for the October 1, 2010 assessment year only, to mail the bill for the first half of the taxes due prior to July 1, 2011. The bill for the second installment of tax may be mailed on or after July 1, 2011. For subsequent assessment years, property tax bills must be sent according to the standard billing schedule. Conn. Public Act. No. 11-1, §1 (effective April 16, 2011).

Hartford Residential Property Assessments. Due to a concern that a revaluation in the City of Hartford would result in a substantial shift in the property tax burden from commercial/industrial property, personal property and motor vehicles to residential/apartment property, the General Assembly adopted legislation to temper that shift. Commencing with the October 1, 2011 assessment year, the City will be able to make annual adjustments to the assessment rate charged to apartment and residential property so long as the assessment rate for any class of property does not exceed 70%. For the October 1, 2011 assessment year, the assessor is to calculate an assessment rate that will have the effect of increasing the average property tax for residential property by 3.5% over the tax for the October 1, 2010 assessment year, but the assessment rate cannot be less than 23%. For assessment years commencing on or after October 1, 2011, the assessor is then to calculate an adjustment to the rate of assessment for residential property that is based upon a

comparison of the consumer price index and the amount by which the tax levy for the then current fiscal year exceeds the tax levy for the prior fiscal year. In the case of apartment property, the City is required to assess such property at 50% of its fair market value for the October 1, 2011 assessment year. Beginning with the following assessment year, the City must proportionately increase this assessment ratio so that it is 70% by the October 1, 2015 assessment year. Conn. Pub. Act No. 11-212, §1 (*effective July 13, 2011, and applicable to assessment years commencing on or after October 1, 2011*).

Armed Forces Property Tax Interest Abatement. The requirement that a municipality not charge or collect interest for a period of one year any property tax that is payable by a Connecticut resident who is a member of the armed forces and who has been called to active duty in Iraq and who is serving outside of the United States when the payment is due, has been extended to those taxpayers who have been called to active duty in Afghanistan. Conn. Gen. Stat. §12-146c, as amended by Conn. Pub. Act No. 11-62, §2 (*effective October 1, 2011, and applicable to assessment years commencing on or after October 1, 2011*). In addition, municipalities are now authorized, after appropriate municipal approval, to grant similar interest relief to other members of the armed forces that have been called to active duty and are serving outside of the state when the municipal property tax payment is due. Conn. Pub. Act No. 11-62, §1 (*effective October 1, 2011, and applicable to assessment years commencing on or after October 1, 2011*).

Property Tax Relief for Volunteer Fire Police Officers and Search and Rescue Team Members. The statute that permits the legislative body of a municipality to establish, by ordinance, a program to provide property tax relief for, among other positions, volunteer firefighters, emergency medical technicians and paramedics, is amended to permit such relief to be extended to a volunteer fire police officer and a volunteer active member of a volunteer underwater search and rescue team. Conn. Gen. Stat. §12-81w, as amended by Conn. Pub. Act No. 11-243, §2 (*effective July 1, 2011*).

Public-Private Partnerships. A new property tax exemption is enacted for any property developed, operated or held by a private entity pursuant to a public-private partnership agreement entered into with a state agency pursuant to legislation adopted during the October special session. Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.), §88 (*effective October 27, 2011*).

II. Cases

Open Space Land. In Goodspeed Airport, LLC v. East Haddam, 302 Conn. 70 (2011), the Connecticut Supreme Court reversed the decision of the Connecticut Appellate Court denying the taxpayer's appeal seeking open space classification and a lower valuation for the two parcels of its property not used as part of its airport operations. The town assessor had conceded that 43.04 acres of the taxpayer's land could be classified as open space but refused to lower the valuation of that parcel, and had challenged the classification of an additional 13.08 acres as open space based on the contention that those acres were used in connection with the airport. The Supreme Court disagreed, remanding the case to the Appellate Court and holding that: (i) the reclassification of the 43.04 acres as open space land required a revaluation of the parcel as the initial valuation was based upon a commercial use of the parcel; and (ii) the additional 13.08 acres, although adjoining the taxpayer's airport, could qualify as open space land if they are not used in the airport operation because the parcel was clearly designated as potential open space land on the town's land use plan.

Addresses of Public Officials. In Commissioner of Public Safety v. Freedom of Information Commission, 301 Conn. 323 (2011), the Connecticut Supreme Court held that Conn. Gen. Stat. §1-217, which prohibits public agencies from disclosing the home addresses of various federal, state and local government officials and employees pursuant to the Freedom of Information Act, is applicable to the grand lists of motor vehicles and their component data provided to town assessors by the Department of Motor Vehicles. The ruling reversed a lower court decision affirming a Freedom of Information order

requiring the town to provide to a taxpayer an exact electronic copy of the file that had been provided by the Department to the Town of North Stonington. The Supreme Court concluded that a grand list made public pursuant to Conn. Gen. Stat. §12-55(a) is still subject to the prohibition contained in section 1-217.

Failure to File Personal Property Tax Declaration. In NYNE Equipment, Inc. v. Seymour, 2011 Conn. Super. LEXIS 50 (Jan. 6, 2011), the Superior Court ruled against an appeal brought by the taxpayer business for a refund of a portion of the personal property taxes paid for the 2003, 2004 and 2005 assessment years. The taxpayer had not filed personal property declarations for those years; rather, the municipal assessor conducted an audit in 2006 and filled out a declaration and imposed an assessment against the taxpayer for each of the years. The taxpayer subsequently filed personal property declarations, based on the 2006 audit figures, for each of the 2006, 2007 and 2008 assessment years. In 2009, the municipal assessor revised the audits, significantly reducing the value of the taxpayer's personal property for 2003 and subsequent assessment years. The assessor granted a refund/credit for the taxes paid for the 2006-2008 assessment years, but not for the 2003-2005 assessment years and the taxpayer appealed. The Superior Court held that the taxpayer could not assert a refund claim based upon an assessor error for the years for which it had not filed a personal property declaration.

Reassessment in Non-Revaluation Year. In Hunt v. Andover, 2011 Conn. Super. LEXIS 12 (Jan. 6, 2011), the taxpayer appealed a change in the valuation of his home during a non-revaluation year based upon the assessor's conclusion that the property should have received a grade of B+ rather than C+. The Court noted that Conn. Gen. Stat. §12-55 accords to an assessor a "watchtower" role, whereby he or she can equalize the assessments of property in a town if necessary, and may increase or decrease the valuation of any property during the period between town-wide revaluations (except due to a sale of that property). The Court reviewed the reports of each party's expert, and entered judgment based upon the appraisal done by the taxpayer's expert.

Burden of Proof. In Dabush v. Weston, 2011 Conn. Super. LEXIS 327 (Feb. 1, 2011), the Tax Session of the Superior Court reminded all taxpayers of the distinction between bringing a property tax appeal pursuant to Conn. Gen. Stat. §12-117a and bringing a property tax appeal pursuant to Conn. Gen. Stat. §12-119. The taxpayer had appealed a real property tax assessment pursuant to section 12-117a, but it was dismissed because it was filed after the two-month period for taking an appeal from the board of assessment appeals. The taxpayer then filed an appeal pursuant to section 12-119, but based the appeal solely on a difference in valuation. The Court entered judgment in favor of the town because section 12-119 requires the taxpayer to establish that the assessor acted illegally or had a manifest and flagrant disregard for the laws of Connecticut. An appeal based only upon a valuation dispute must be brought in a timely manner pursuant to section 12-117a.

Attorney's Fees. In Zlotnick Construction, Inc. v. Stratford, 2011 Conn. Super. LEXIS 639 (Mar. 18, 2011), the taxpayer general contractor had a personal property tax assessment imposed against it based upon construction equipment located on its construction site, most of which was owned by third party subcontractors. The town's assessor requested the assistance of the taxpayer to identify the owners of the third party equipment, but the taxpayer refused to provide such assistance. The taxpayer appealed the assessment, contending that almost all of the personal property on the site was owned by independent subcontractors. Even though the assessor later conceded that most of the property was owned by third parties, the board of assessment appeals still voted to uphold the assessment. The Superior Court reduced the assessment to exclude the property owned by third parties and awarded to the taxpayer a small amount for attorney's fees. The Court noted that, in the absence of a statutory provision granting attorney's fees, the taxpayer has to prove by clear and convincing evidence that the town acted in bad faith. The Court felt that it was precluded from granting a bigger award because the taxpayer had not cooperated with the assessor's attempts to identify the true owners of the property.

Appeal from Incomplete Application. In Village Apartments, LLC v. Montville, 2011 Conn. Super. LEXIS 218 (Jan. 31, 2011), the board of assessment appeals declined to hold a hearing on the taxpayer's petitions because the petitions were

incomplete. Instead of taking no action on the petitions, however, the town sent written notices to the taxpayer denying the petitions and advising the taxpayer that it could file an appeal with the Superior Court. When the town filed a motion to dismiss the court appeal on the grounds that the taxpayer had failed to exhaust its administrative remedies by filing a proper petition with the board of assessment appeals, the Court held that it would have granted the motion to dismiss had the town not taken any action on the incomplete petitions. However, since the town had sent notices of denial and of a right of appeal, there was an "action" by the board of assessment appeals that could be reviewed by the Court.

Department Store Valuation. In The May Department Stores Co. v. Meriden, Docket No. CV 07-4007788 (Super. Ct. June 15, 2011), the trial court reviewed the valuation of each of a Macy's department store and a Sears department store at the Westfield Meriden Mall. The trial court rejected the taxpayers' attempt to enforce against the town assessor the gross building area square foot price that the Town had agreed to as part of a stipulated judgment in a separate property tax appeal filed by a J.C. Penney concerning the valuation of its department store in the same mall. The court held that a stipulated judgment did not rise to the level of a judicial finding and, therefore, could not be treated as binding on the assessor. The court also dismissed the attempt by the appraiser for each of the Town and the taxpayers to use the income approach to value the stores because they were owner-occupied properties and there were no rents. The court, instead, lowered the valuation based upon the only comparable sale found to be credible.

Tax Refund Claim. In Evergreen Associates, LLC v. Clinton, 2011 Conn. Super. LEXIS 1547 (June 22, 2011), the plaintiff owner and operator of a mobile home park paid delinquent property taxes owed by a former mobile homeowner-tenant when the town building official refused to grant a building permit because of the delinquent taxes. The plaintiff later sought a refund of the taxes on the basis that it was not lawfully obligated to pay the taxes. The Superior Court upheld the town's denial of the refund claim pursuant to Conn. Gen. Stat. §12-129, on the basis that the refund claim was filed more than three years after the last date the delinquent taxes were due.

Multiple Appeals of Valuation. In Samnard Associates, LLC v. New Britain, 2011 Conn. Super. LEXIS 908 (Apr. 8, 2011), the taxpayer land owner sought to challenge the valuation of a commercial property on the 2009 Grand List. The City moved for summary judgment on the grounds that a former tenant of the property had appealed the revaluation of the property, with the taxpayer's consent, on the 2007 Grand List and had agreed to a lower valuation of the property by the Board of Assessment Appeals without further appeal. The Superior Court granted the motion for summary judgment concluding that the taxpayer could not bring a second appeal challenging the same valuation, and must instead wait until the next city-wide revaluation.

Exempt Trade Educational Organization. In Trustees Under Restated Agreement & Declaration of Trust v. Wallingford, 2011 Conn. Super. LEXIS 1484 (2011), a trust fund exempt from federal income tax under Internal Revenue Code §501(c)(3) appealed the denial of its application for tax-exempt status as an educational institution. The sole purpose of the trust, which was created by a union, was to train, retrain and improve the education skills of apprentice and journeyman plumbers and pipefitters. The Superior Court ruled that the subject facilities, which consist primarily of classrooms and shop rooms, was exempt from property taxation because the property belonged to a tax-exempt organization for an educational purpose and does not produce income other than what is needed to provide reasonable compensation for services effectuating an educational purpose.

Exemption Defense to Foreclosure. In Weston v. Saugatuck Land Trust Co., 2011 Conn. Super. LEXIS 1968 (July 19, 2011), the defendant land trust filed an answer asserting as a special defense to a foreclosure action that the town could not foreclose on certain properties for unpaid taxes because the land trust is a charitable organization and its lands are exempt from the taxes assessed by the town. The Court granted a motion to strike the special defense because a claim that land was unlawfully assessed must be raised as part of an appeal from the assessment, and cannot be asserted in defense of a foreclosure action.

Exhaustion of Remedies. In *Baltayan v. Tito*, 2011 U.S. Dist. LEXIS 80242 (D. Conn. 2011), the United States District Court dismissed an action filed by a taxpayer against certain Hamden officials seeking, in part, the refund of certain amounts levied by Hamden because of the taxpayer's failure to pay property taxes on his motor vehicles. The Court noted that the taxpayer had failed properly to appeal the assessment and could not subsequently challenge the tax collection in an independent federal court action.

MISCELLANEOUS TAXES

I. Legislation

Business Entity Tax. Subchapter S corporations, limited liability companies, limited liability partnerships and limited partnerships currently are subject to an annual \$250 Connecticut business entity tax. Effective for taxable years commencing on or after January 1, 2013, the business entity tax will be due every other year. In practical terms, taxable entities will be required to pay: \$250 by April 15, 2012, for the 2011 tax year; \$250 by April 15, 2013 for the 2012 tax year; \$250 by April 15, 2015 for the 2013 and 2014 tax years; etc. Conn. Gen. Stat. §12-284b(b), as amended by Conn. Pub. Act No. 11-1 (October Spec. Sess.), §23 (*effective October 27, 2011*).

Hospital Provider Tax. Effective July 1, 2011, each hospital in Connecticut, other than the Connecticut Children's Medical Center and John Dempsey Hospital, will be required to pay a quarterly tax at the rate of 4.6% on its net patient revenue. "Net patient revenue" is defined as the hospital's gross revenue including the amount received by the hospital from the federal government for Medicare patients. In the case of a delinquency which has been reported by the Commissioner of Revenue Services to the Commissioner of Social Services, the Commissioner of Social Services shall deduct and withhold the delinquent amount from amounts otherwise payable by the Department of Social Services to the hospital. Returns must be filed electronically and payment made by electronic funds transfer irrespective of the general requirements pertaining to electronic filing and fund transfers set forth in Chapter 228g of the Connecticut General Statutes. Conn. Gen. Stat. §§12-263a-12-263d, as amended by Conn. Pub. Act No. 11-6, §§145-149, as further amended by Conn. Pub. Act No. 11-61, §79 (*effective July 1, 2011, and applicable to calendar quarters commencing on or after July 1, 2011*). See DRS Special Notice 2011(15), *2011 Legislation Imposing the Hospital Net Patient Revenue Tax*.

Nursing Home User Fee. The nursing home user fee cap, which is currently 5.5%, is increased to the maximum allowed under federal law, which will be 6.0% effective October 1, 2011. Conn. Gen. Stat. §17b-321, as amended by Conn. Pub. Act No. 11-6, §510 (*effective July 1, 2011*). The nursing home user fee for municipally-owned facilities and facilities with over 230 beds is \$14.78 for the third calendar quarter of 2011 and \$16.13 for the period from October 1, 2011 through June 30, 2012; and the nursing home user fee for all other nursing homes is \$19.26 for the third calendar quarter of 2011, and \$21.02 for the period from October 1, 2011 through June 30, 2012. See DRS Special Notice 2011(14), *2011 Legislation Amending the Nursing Home User Fee*.

New User Fee for Intermediate Care Facilities for Individuals with an Intellectual Disability. Effective July 1, 2011, a new user fee is imposed on residential facilities for the mentally retarded. Before October 1, 2011, the fee can be as high as 5.5%; on or after October 1, 2011, the fee is capped at the maximum amount allowed by federal law (currently 6%). Similar to the Hospital Provider Tax discussed above, the Commissioner of Social Services is to deduct and withhold any delinquent user fee amount from amounts otherwise payable by the Department of Social Services to the intermediate care facility. Conn. Pub. Act No. 11-6, §§151-153 (*effective July 1, 2011*). The intermediate care facility user fee for state-owned and operated intermediate care facilities is \$49.32 for the third calendar quarter of 2011, and \$53.81 for the period from October 1, 2011 through June 30, 2012; and the intermediate care facility user fee for all other intermediate care facilities is \$25.44 for the third calendar quarter of 2011, and \$27.76 for the period from October 1, 2011 through June 30, 2012. See DRS Special Notice 2011(16), *2011 Legislation Imposing the Intermediate Care Facility User Fee*.

Real Estate Conveyance Tax. The state conveyance tax rate currently is (i) 0.5% of (A) the first \$800,000 of the sale price of a residential property and (B) the full sale price of unimproved land and certain bank foreclosures for mortgage delinquencies; and (ii) 1% of (A) any portion of the sales price of a residential dwelling that exceeds \$800,000 and (B) sales of nonresidential property other than unimproved land. Effective July 1, 2011, both state rates are increased by 0.25% to 0.75% and 1.25%, respectively. (The tax revenue attributable to the 0.25% increase is to be deposited in the municipal revenue sharing account.) The “temporary” increase in the municipal portion of the real estate conveyance tax from 0.11% to 0.25% is made permanent as of the same date. Note that certain targeted investment communities can further increase the municipal portion of the real estate conveyance tax to 0.50%. Currently, there are 18 municipalities that have done so. Conn. Gen. Stat. §12-494, as amended by Conn. Pub. Act No. 11-6, §§102-103 (*effective July 1, 2011, and applicable to conveyances occurring on or after that date*). See DRS Special Notice 2011(3), *2011 Legislative Changes Affecting the Connecticut Real Estate Conveyance Tax*.

Cigarette and Tobacco Products Tax. The tax on each cigarette pack is increased from 150 mills to 170 mills (representing an increase from \$3.00 to \$3.40 per pack) effective July 1, 2011, and a dealer or distributor will be required to pay a floor tax of 20 mills (40 cents) per cigarette pack in the dealer’s inventory as of the close of business on June 30, 2011. Failure to file a report and pay the floor tax by August 15, 2011 may result in substantial penalties and/or revocation of such cigarette dealer’s or distributor’s license and any other Department of Revenue Services-issued license or permit the person or entity holds. Also effective July 1, 2011, the tax on snuff is increased from 55 cents to one dollar per ounce. The tax on all other tobacco products, as of the same date, is increased from 27.5% to 50% of the wholesale sales price of such products, except that the tax on cigars is capped at 50 cents per cigar. Conn. Gen. Stat. §§12-296, 12-316 and 12-330c, as amended by Conn. Pub. Act No. 11-6, §§80-83, as further amended by Conn. Pub. Act No. 11-61, §38 (*effective July 1, 2011, and applicable to sales occurring on or after said date*). The penalties for cigarette dealers who continue to sell cigarettes or taxed tobacco products after their licenses expire are reduced, if the period of operation is no more than 90 days after the expiration of the license, from a fine of up to \$500 and/or up to three months in jail to an infraction with a \$90 fine. Conn. Gen. Stat. §12-286(e), as amended by Conn. Pub. Act No. 11-61, §62 (*effective July 1, 2011*). Similarly, the penalties for certain cigarette dealers who possess cigarettes that do not have the required Connecticut tax stamps are reduced, if it is the dealer’s first violation and the dealer possesses no more than 600 unstamped cigarettes, from up to one year in jail and/or a fine of up to \$1,000 to an infraction with a \$90 fine. Conn. Gen. Stat. §12-304(a), as amended by Conn. Pub. Act No. 11-61, §63 (*effective July 1, 2011*). Finally, new legislation authorizes a franchisor of five or more retail establishments (i) to be a “chain store” for purposes of qualifying for a lower minimum mark-up on sales of cigarettes by distributors to chain stores (as opposed to sales to dealers) and (ii) to be licensed as a distributor if the franchisor buys cigarettes at wholesale exclusively for those retail stores, and shares in the gross profits generated by the stores. Conn. Gen. Stat. §§12-285(a), 12-286(a), 12-288 and 12-326a(a), as amended by Conn. Pub. Act No. 11-37, §§1-4 (*effective July 1, 2011*). See DRS Special Notice 2011(8), *2011 Legislation Affecting the Tobacco Products Tax Effective July 1, 2011*.

Alcoholic Beverages Tax. Effective for sales occurring on or after July 1, 2011, the tax on alcoholic beverages is increased generally by 20% as follows: (i) beer, and cider containing not more than 7% of absolute alcohol: from \$6.00 to \$7.20 for each barrel; \$3.00 to \$3.60 for each half barrel; \$1.50 to \$1.80 for each quarter barrel; \$0.20 to \$0.24 for each wine gallon or fraction under a quarter barrel; (ii) liquor: from \$4.50 to \$5.40 per wine gallon; (iii) still wines of not more than 21% absolute alcohol: from 60 cents to 72 cents per wine gallon; (iv) other still wines and sparkling wines: from \$1.50 to \$1.80 per wine gallon; (v) alcohol in excess of 100 proof: from \$4.50 to \$5.40 per proof gallon; (vi) liquor coolers containing not more than 7% alcohol: from \$2.05 to \$2.46 per wine gallon; and (vii) certain still wine produced by small producers: from 15 cents to 18 cents per wine gallon. A floor tax is imposed on alcohol inventories as of the effective date of the new tax rates. Failure to file a report and pay the floor tax by August 15, 2011 may result in substantial penalties and/or revocation of any Department of Revenue Services-issued license or permit the person or entity holds. Conn. Gen.

Stat. §12-435, as amended by Conn. Pub. Act No. 11-6, §§98-99 (effective May 4, 2011, and applicable to sales occurring on or after July 1, 2011). See DRS Special Notice 2011(4), *Alcoholic Beverages Tax on Alcoholic Beverages Inventory as of the Opening of Business on July 1, 2011*; DRS Special Notice 2011(7), *2011 Legislative Changes Affecting the Alcoholic Beverages Tax*.

Motor Vehicles Fuels Tax. Effective July 1, 2011, the base tax on diesel fuel is increased from 26 cents to 29 cents per gallon. A floor tax of 3 cents is imposed on inventories of diesel fuel as of the close of business on June 30, 2011. Failure to file a report and pay the floor tax by August 1, 2011 may result in substantial penalties and/or revocation of any Department of Revenue Services-issued license or permit the person or entity holds. Conn. Gen. Stat. §12-458h, as amended by Conn. Pub. Act No. 11-6, §§100-101 (effective July 1, 2011). See DRS Special Notice 2011(1), *Motor Vehicle Fuels Tax on Diesel Fuel Inventory as of June 30, 2011*.

Illegal Use of Dyed Diesel Fuel. Federal law exempts from federal fuel taxes diesel fuel used for certain non-highway purposes and requires exempt fuel to be dyed red for identification purposes. A new law imposes a fine of up to \$1,000 on anyone who uses dyed diesel fuel in a motor vehicle on a public highway, unless permitted to do so under federal law. The same fine can be assessed if a person refuses to allow inspection of the fuel supply tank of a motor vehicle by a state official. Conn. Gen. Stat. §12-487, as amended by Conn. Pub. Act No. 11-61, §64 (effective July 1, 2011).

Electric Generation Tax. Commencing July 1, 2011, and effective only through June 30, 2013, a new tax is imposed on any person providing electric generation services and uploading electricity generated at such person's electric generation facility in this state to the regional bulk power grid. The tax is the product of one-quarter of one cent multiplied by the net kilowatt hours of electricity generated by such person and uploaded to the regional bulk power grid. The tax does not apply to any net kilowatt hours of electricity generated at: (i) an electric generation facility in Connecticut exclusively through the use of fuel cells or an alternative energy system, such as a solar or wind system; (ii) a resources recovery facility; or (iii) customer-side distributed resources. The Department of Revenue Services audit, collection, and other tax administration procedures applicable to the admissions and dues taxes apply to the generator tax except where inconsistent. Conn. Pub. Act No. 11-6, §104, as amended by Conn. Pub. Act No. 11-61, §45, as amended by Conn. Pub. Act No. 11-233, §17 (effective July 1, 2011). See DRS Special Notice 2011(11), *2011 Legislation Imposing an Electric Generation Tax*.

Admissions Tax Exemptions Repealed. Effective January 1, 2012, the exemption from the admissions tax would be repealed for any event held at a number of venues, including, amongst others, the Hartford Civic Center, Connecticut Convention Center, New Britain Veterans Memorial Stadium, New Britain Beehive Stadium, Bridgeport Harbor Yard Stadium, the Arena at Harbor Yard and Lime Rock Park. Conn. Gen. Stat. §12-541(a), as amended by Conn. Pub. Act No. 11-6, §105 (effective January 1, 2012, and applicable to admission charges imposed on or after that date).

Captive Insurance Companies. During the October special session, the Connecticut General Assembly revised and expanded the laws governing captive insurance companies. The new legislation provides that a captive must pay an annual premium receipts tax on its direct-written premiums on or before March 1st, and adds a requirement that a captive must now pay an annual premium receipts tax on its assumed reinsurance premiums. The annual minimum aggregate tax by a captive (other than a sponsored captive) is \$7,500, and the annual maximum aggregate tax is \$200,000. For a branch captive, the annual aggregate tax applies only to the branch business of the captive transacted in Connecticut. For a sponsored captive, the annual minimum aggregate tax is \$7,500 and applies to the company as a whole, and not to each protected cell. A sponsored captive's annual maximum aggregate tax is the aggregate tax liability on the direct premium of each protected cell. Finally, a captive licensed on or after January 1, 2012, will receive a nonrefundable tax credit of \$7,500 for the captive's first taxable year. Conn. Gen. Stat. §38a-91nn, as amended by Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.), §66 (effective July 1, 2012, and applicable to calendar years commencing on or after January 1, 2012).

Nonadmitted Insurance. Pursuant to the federal Nonadmitted and Reinsurance Reform Act of 2010, signed into law as part of The Wall Street Reform and Consumer Protection Act (“Dodd-Frank Act”), the General Assembly adopted uniform requirements and procedures for allocating and collecting premium taxes on nonadmitted insurance policies. There currently is a 4% tax on gross premiums charged by nonadmitted (i.e. unauthorized) insurers on insurance policies procured independently or through licensed surplus lines brokers. The legislation limits the tax to any such policy where Connecticut is the insured’s “home state” (where its principal place of business or residence is located) or, if the insured risk is located entirely outside of the home state, the state to which the greatest percentage of the insured’s taxable premium is located. Individuals and brokers are required to withhold 4% of the premium due and file quarterly tax returns and remit the tax. Late payments are subject to an interest charge of 1% per month or any part thereof and a penalty of 10% of the tax due. The legislation also authorizes the DRS and the Department of Insurance to enter into cooperative or reciprocal agreements with other states. Conn. Gen. Stat. §§38a-277, 38a-743, 38a-271 and 38a-741, as amended by Conn. Pub. Act No. 11-61, §§33-36 (*effective June 21, 2011, and applicable to non-admitted insurance coverage procured, continued or renewed on or after July 1, 2011*). See DRS Special Notice 2011(18), *2011 Legislative Changes Affecting the Premiums Tax on Insureds Directly Procuring, Continuing or Renewing Insurance from a Nonadmitted Insurer*.

Major Aerospace or Defense Plant Closure. During the 2010 legislative session, the General Assembly enacted legislation whereby the Commissioner of Economic and Community Development can determine that the economy of a municipality has been severely impacted by a major aerospace or defense plant closure with not less than 800 employees. In reaching that determination, the Commissioner must find that, due to such major aerospace or defense plant closure in the municipality, (i) there is or will be a loss of employment opportunities in the municipality, and (ii) there is or will be a severe adverse impact in the municipality. If such a determination is made, the owners of any business facility located in the municipality, if a qualified “manufacturing facility,” will be eligible to seek the property tax exemptions and corporation business tax credits available to the owners of manufacturing facilities in distressed municipalities, as provided in Sections 32-9p to 32-9s, 12-217e, and 12-81(59) and (60) of the Connecticut General Statutes. To be a qualifying business facility, the facility had to be located in a building that was vacant on July 1, 1998, and was formerly used for defense manufacturing. Under 2011 legislation, the facility can now also be located in a building that was vacant on or after June 21, 2011, and was formerly a major aerospace or defense plant with not less than 800 employees. The Commissioner’s determination is effective for two years, but may be renewed by the Commissioner for an additional two years (or until the plant is reoccupied if the closure involved a military installation at which military vehicle engines were produced). Conn. Gen. Stat. §32-56, as amended by Conn. Pub. Act No. 11-61, §53 (*effective June 21, 2011*).

Reciprocal Tax Refund Agreements. Existing law permits the Commissioner of Revenue Services to withhold and remit a taxpayer’s Connecticut tax refund at the request of another state to which the taxpayer owes taxes if the other state has a similar statute that would entitle the State of Connecticut to seek such a remedy from a delinquent taxpayer owed a refund by that other state. In general, in order to claim all or a portion of a Connecticut tax refund, the other state’s tax officer must certify certain facts to the Commissioner and the Commissioner must provide notice and a copy of that certification to the affected taxpayer. The governing statute has been amended to: (i) delete the requirement that the certification of the other state’s tax officer must include a detailed statement for each taxable period showing tax, interest and penalty; (ii) require that notice be provided to the taxpayer only if the taxpayer is otherwise entitled to a refund from the State of Connecticut; and (iii) repeal the requirement that the notice include a copy of the other state tax officer’s certification. Conn. Gen. Stat. §12-35f(b), as amended by Conn. Pub. Act No. 11-61, §54 (*effective June 21, 2011*).

Electronic Tax Payment Failures. Effective January 1, 2012, the penalty for the failure to pay taxes by electronic funds transfer, when required to do so, is reduced in the case of a first or second failure. Instead of the mandatory penalty of 10% of the payment, (i) in the case of the first failure, the penalty is the lesser of 10% of the payment or \$2,500; and (ii) in the case of a second failure, the penalty is the lesser of 10% of the payment or \$10,000. Conn. Gen. Stat. §12-687,

as amended by Conn. Pub. Act No. 11-61, §65 (effective June 21, 2011, and applicable to tax periods commencing on or after January 1, 2012).

Waiver of Electronic Filing or Payment Requirement. A new process is established whereby any taxpayer required to file a tax return electronically or to make a tax payment by electronic funds transfer, may request in writing, not later than 30 days prior to when such return or payment is due, a waiver on the basis of undue hardship. The Commissioner is to respond promptly to the request and the decision of the Commissioner is final and not subject to review or appeal. The waiver, if granted, is effective for a period of 12 months from the date of grant. The process does not apply to return preparers. Conn. Gen. Stat. §12-686, as amended by Conn. Pub. Act No. 11-145, §1 (effective October 1, 2011, and applicable to payments for tax periods beginning on or after that date).

Airport Development Zones. During the 2010 legislative session, the General Assembly created a new Bradley Airport Development Zone (the "BADZ") that extends enterprise zone tax incentives, credits and exemptions to manufacturers and other specified businesses that develop or acquire property and create jobs in the BADZ. The governing provisions have been amended to provide that municipalities located in the BADZ are not distressed municipalities, Conn. Gen. Stat. §32-9p, as amended by Conn. Pub. Act No. 11-140, §17 (effective October 1, 2011), and to change the effective date of the BADZ legislation so that it is effective October 1, 2011, and applicable to income years commencing on or after January 1, 2012. Conn. Pub. Act No. 11-78, §2 (effective July 1, 2011). During the regular legislative session, new legislation that would have extended the same benefits to businesses in a new Oxford Airport Development Zone, comprised of certain census tracts in the towns of Middlebury, Oxford and Southbury, was vetoed by Governor Malloy. Conn. Gen. Stat. §§32-75d, 12-81(59)(c), 12-81(60)(c), 32-9p(d), 32-9r(a) and 32-9s, as amended by Conn. Pub. Act No. 11-142, §§1-6 (effective October 1, 2012), vetoed on July 8, 2011. After an apparent change of heart, during the October special session, the General Assembly enacted legislation that authorizes the Connecticut Airport Authority to establish additional airport development zones upon the recommendation of the DECD that the economic development benefits of creating each zone would outweigh the costs to the state and affected municipalities. The state and local tax benefits associated with the additional airport development zones are to be the same as with the BADZ, but the eligibility criteria for a qualified business applicant has been amended to require a showing that the grant of an application for an eligibility certificate would not cause an economic detriment to, or conflict with, an existing zone and that the applicant serves an airport-related function or relies substantially on airport services. Conn. Gen. Stat. §§32-75d, 12-81(59)(c), 32-9p(d), 32-9r and 32-9s, as amended by Conn. Pub. Act No. 11-1 (Oct. Spec. Sess.), §§39-45 (effective October 27, 2011).

Abatement Review Committee. The membership of the Abatement Review Committee, which is to review any abatement of interest or penalty by the Commissioner of Revenue Services, is increased to include the Commissioner of Consumer Protection or the Commissioner's designee. The legislation reflects the elimination of the Division of Special Revenue and the transfer of its responsibilities to the Department of Consumer Protection. Conn. Gen. Stat. §12-3b, as amended by Conn. Pub. Act No. 11-51, §185 (effective July 1, 2011).

Homemaker Services and Homemaker-Companion Agencies. Effective January 1, 2012, any registry in the business of supplying or referring an individual or placing an individual with a consumer to provide homemaker or companion services, and that individual is either (i) directly compensated, in whole or in part by the consumer or (ii) treated, referred to or considered by the registry as an independent contractor, must provide a written notice to the consumer within 7 days of the placement of that individual. The notice must indicate whether the registry is an employer, joint employer, leasing employer or nonemployer of the individual, and include a statement advising the consumer that he or she may be considered an employer under law and, if so, that the consumer may be held responsible for the payment of taxes, Social Security, overtime and minimum wage, unemployment, workers' compensation insurance payments and other federal and state payments. Conn. Gen. Stat. §§20-670 and 20-675, as amended and supplemented by Conn. Pub. Act No. 11-230, §§1-3 (effective January 1, 2012).

Cabaret Tax. The Connecticut General Assembly adopted, and then repealed before it became effective, a “cabaret tax” equal to 3% on all amounts charged for admissions, food and drink, service or merchandise at any cabaret or similar place furnishing music, dancing privileges or any other entertainment for profit. Conn. Pub. Act No. 11-6, §106, as repealed by Conn. Pub. Act No. 11-61, §186 (*effective June 21, 2011*).

II. Cases

Electricity Financing Fees. In Markley v. Department of Public Utility Control, 301 Conn. 56 (2011), the Connecticut Supreme Court upheld the dismissal of an action brought by an individual electric utility ratepayer challenging a fee charged to ratepayers by electric utilities, which fee was based upon a financing order issued pursuant to state statute and the proceeds of which were to be paid into the State’s general fund. The purpose of the financing order was to require electric utilities to continue to collect a fee from ratepayers that was initially established to permit the utilities to recoup “stranded costs” incurred during electricity deregulation. The fees would be continued, but the proceeds would be transmitted to the general fund to pay principal and interest on economic recovery revenue bonds issued by the State to fund the State’s deficit. The ratepayer plaintiff asserted that the financing order constituted an illegal tax on the utilities’ customers, was issued in excess of the defendants’ statutory authority and was unconstitutional. The Court held that the plaintiff’s claims were barred by sovereign immunity, and that the plaintiff had failed to demonstrate that the financing order violated his equal protection rights or to set forth a substantial allegation of illegal conduct by the defendants. [Ed. note. During the 2011 legislative session, the General Assembly rescinded future authority to issue economic recovery revenue bonds and the use of a per-kilowatt-hour surcharge (a “competitive transition assessment”) to secure and pay such bonds. Conn. Gen. Stat. §§16-245j and 16-245h; as amended by Conn. Pub. Act No. 11-61, §§49-50 (*effective June 21, 2011*).]

Petroleum Products Gross Earnings Tax Refund. In Housatonic Railroad Company, Inc. v. Commissioner, 301 Conn. 268 (2011), the plaintiff railroad corporation sought a refund of the portion of the price it paid to a fuel distributor for diesel fuel for its railroad operations attributable to the petroleum products gross earnings tax paid by the distributor on that fuel. The Connecticut Supreme Court affirmed the dismissal of the refund claim on the ground that the doctrine of sovereign immunity barred the refund claim because there was no statutory authority to bring the claim. The Court ruled that: (i) the federal Railroad Revitalization and Regulatory Reform Act, which prohibits states from taxing rail carriers in a discriminatory manner, only provides for injunctive or declaratory relief, and not for a refund of taxes already paid; (ii) Conn. Gen. Stat. §12-597 permits a taxpayer to appeal from the Commissioner’s denial of a petroleum products gross earnings tax refund, but the plaintiff was not the “taxpayer” as it related to the tax paid on the fuel because the tax was legally owed and paid by the fuel distributor; and (iii) the plaintiff could not appeal the denial of its refund claim pursuant to Conn. Gen. Stat. §12-33 because section 12-597 provides the exclusive statutory authority to appeal a decision of the Commissioner relating to the Connecticut petroleum products gross earnings tax.

Petroleum Products Gross Earnings Tax Appeal. In BYK Chemie USA, Inc. v. Commissioner, 2011 Conn. Super. LEXIS 1060 (Apr. 28, 2011), the Tax Session of the Superior Court held that Section 12-600 of the Connecticut General Statutes requires a taxpayer to pay the full amount of any assessment of petroleum products gross earnings tax, interest and penalties prior to instituting any court appeal challenging the constitutionality of the tax or its application. Accordingly, the Court dismissed the two counts of the taxpayer’s appeal challenging the constitutionality of the assessment, but denied the Commissioner’s motion to dismiss the remaining two counts alleging that the Commissioner’s application of the tax was erroneous.

ADMINISTRATIVE PRONOUNCEMENTS

Announcements

AN 2011(1), Information for Married Individuals or Civil Union Partners Who Are Both Employed and File a Joint Connecticut Income Tax Return

AN 2011(2), Assessments Refunded by Connecticut Insurance Guaranty Association

AN 2011(3), Annual List of Distributors For Motor Vehicle Fuels Tax Purposes

AN 2011(3.1), Quarterly List of Distributors for Motor Vehicle Fuels Tax Purposes

AN 2011(3.2), Quarterly List of Distributors for Motor Vehicle Fuels Tax Purposes

AN 2011(4), Annual Revision of Forms TPM-1, TPM-2 and TPM-3

AN 2011(5), Motor Vehicles Fuels Tax Rate on Diesel Fuel Increased Effective July 1, 2011

AN 2011(6), Additional Guidance Regarding Withholding Calculation Rules for Supplemental Compensation and Use of Newly Issued Form CT-W4T.

Informational Publications

IP 2011(1), Connecticut Circular CT - Employer's Tax Guide

IP 2011(2.2), Topical Index to Rulings and Administrative Pronouncements Covering Income Tax

IP 2011(3.2), Topical Index to Rulings and Administrative Pronouncements Covering Corporation Business Tax

IP 2011(4.2), Numerical Index to Rulings and Administrative Pronouncements as Affected, If at All, by Later-Issued Rulings and Pronouncements

IP 2011(5.2), Topical Index to Rulings and Administrative Pronouncements Covering Sales and Use Taxes

IP 2011(6.2), Topical Index to Rulings and Administrative Pronouncements Covering Miscellaneous Taxes and Administrative Topics

IP 2011(8), Connecticut Tax Guide for Payers of Nonpayroll Amounts

IP 2011(10.1), Connecticut Income Tax Changes Affecting Withholding Requirements

IP 2011(13), Q&A on the Cigarette Tax Increase Effective July 1, 2011, for Licensed Cigarette Dealers

IP 2011(14), Q&A on the Cigarette Tax Increase Effective July 1, 2011, for Licensed Cigarette Distributors

IP 2011(15), Q&A on the Connecticut Individual Use Tax

IP 2011(16), Successor Liability for Sales and Use Taxes, Admissions and Dues Tax, and Connecticut Income Tax Withholding

IP 2011(17), Sales and Use Taxes on Returned Goods, Even Exchanges, and Trade-Ins

IP 2011(18), Connecticut Tax Tips for Senior Citizens



Policy Statements

PS 2011(1), The Use of Commercial Cigarette-Making Machine in a Retail Establishment

PS 2011(2), Income Tax Withholding for Athletes and Entertainers

PS 2011(3), Requests for Waiver of Electronic Filing and Electronic Payment Requirements

PS 2011(4), Sales and Use Tax Exemptions for Diplomatic Personnel

Special Notices

SN 2011(1), Motor Vehicle Fuels Tax on Diesel Fuel Inventory as of June 30, 2011

SN 2011 (2), 2011 Legislative Changes Affecting the Connecticut Estate Tax and the Connecticut Gift Tax

SN 2011(3), 2011 Legislative Changes Affecting the Connecticut Real Estate Conveyance Tax

SN 2011(4), Alcoholic Beverages Tax on Alcoholic Beverages Inventory as of the Opening of Business on July 1, 2011

SN 2011(6), Summary of Tax Provisions Contained in 2011 Conn. Pub. Acts 6

SN 2011(7), 2011 Legislative Changes Affecting the Alcoholic Beverages Tax

SN 2011(8), 2011 Legislation Affecting the Tobacco Products Tax Effective July 1, 2011

SN 2011(9), 2011 Legislative Changes Affecting Sales and Use Taxes

SN 2011(10), 2011 Legislative Changes Affecting Motor Vehicles

SN 2011(11), 2011 Legislation Imposing an Electric Generation Tax

SN 2011(12), 2011 Legislative Changes Affecting the Income Tax

SN 2011(14), 2011 Legislation Amending the Nursing Home User Fee

SN 2011(15), 2011 Legislation Imposing the Hospital Net Patient Revenue Tax

SN 2011(16), 2011 Legislation Imposing the Intermediate Care Facility User Fee

SN 2011(17), 2011 Legislative Changes to the Procedures Governing Nonresident Contractors

SN 2011(18), 2011 Legislative Changes Affecting the Premiums Tax on Insureds Directly Procuring, Continuing or Renewing Insurance from a Nonadmitted Insurer