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2014 Connecticut Tax Forecast: DRS Legislative Proposals, Transparency and Regulations

The recent release of the 2014 legislative proposals of the Connecticut Department of Revenue Services (the “Department” or “DRS”) and the issuance of two executive orders by Governor Dannel P. Malloy suggest that 2014 will be a busy year for the Department and a year during which Connecticut taxpayers may see substantive tax law changes. This Alert summarizes the highlights of the 2014 DRS legislative proposals and the two executive orders. Readers can access our year-end review of 2013 Connecticut tax developments at <http://shipmangoodwin.com/webfiles/CT%20Tax%20Developments%20October%202013.pdf>.

- 1. DRS Legislative Package.** Last week, the Office of Policy and Management published on its website the 2014 legislative proposals of the DRS. Among those legislative proposals are the following:
 - Sales and Use Tax Collection Overhaul. A proposal would change the manner in which sales and use tax is remitted to the state by requiring: (i) each taxpayer who files sales and use tax returns and remits taxes on a monthly or quarterly basis to file its returns and remit the tax due on or before the twentieth (20th) day, and not the last day, of the month following the reporting period; and (ii) a delinquent taxpayer, after notification by the Commissioner, to remit tax collected for a weekly period on a weekly basis for a period of one year (regardless of whether the taxpayer would otherwise be a monthly, quarterly or annual filer). In addition, a taxpayer whose tax liability for the preceding twelve-month period ending June 30th was \$500,000 or more will be required to make monthly estimated payments equal to 75% of the tax reported on the taxpayer’s return for the corresponding month of the preceding year. Such taxpayer will then pay the difference between the estimated payment due for a month and the actual amount due for the month with its return by the 20th day of the succeeding month.
 - Apportionment of Pass-Through Income for Partnerships, LLCs and S Corporations. A proposal would establish a new apportionment formula for the income of pass-through entities (i.e. a partnership, S corporation or limited liability company taxed as a partnership) doing business in and outside of Connecticut. The three-factor apportionment formula will be based upon the averages of the percentages of property, payroll and gross income. Gross receipts from sales of property will be considered earned within Connecticut when the property is delivered or shipped

to a purchaser in Connecticut, whereas gross receipts from sales of services are considered to be earned in Connecticut when the services are performed by an employee, agent, agency or independent contractor chiefly situated at, connected by contract or otherwise with, or sent out from, offices or other locations situated within Connecticut.

- Nonresident Real Property Income. A nonresident individual's Connecticut source income is proposed to now include items of income, gain, loss and deduction derived from ownership of an interest in a partnership, limited liability company or S corporation that owns Connecticut real property if that real property has a fair market value that equals or exceeds 50% of all of the assets of that entity on the date of the sale or exchange of the taxpayer's interest in the entity (excluding assets owned by the entity for less than two years). Gains or losses from the sale or exchange of an interest in such an entity would be apportioned to Connecticut based upon the percentage of all assets held by the entity.
- Nonresident Deferred Compensation. A proposal would add to a nonresident individual's Connecticut source income his compensation from nonqualified deferred compensation plans attributable to services performed in Connecticut, including compensation required to be included in federal gross income under Internal Revenue Code Section 457A.
- Financial Institution Data Match. The Commissioner is seeking authorization to develop and operate a data match system that will permit the DRS to contact a financial institution to determine whether a delinquent taxpayer has an account at that institution prior to issuing a notice of levy.
- Public Inspection. The Commissioner is seeking authorization to make available publicly a list of each person whose application to the Commissioner for a license, permit or certificate has been denied or whose license, permit or certificate has not been renewed, or has been revoked or suspended.
- Trusts and Estates. The proposal would add a further modification to the Connecticut fiduciary adjustment to the Connecticut taxable income of a trust or estate for lump-sum distributions from qualified plans.
- Mattress Fee. A proposal would exclude from the calculation of sales or use tax on the sale of a mattress the new state mattress stewardship fee that is to be collected upon the sale of a mattress in Connecticut.

It remains to be seen which, if any, of the foregoing proposals will be adopted by the General Assembly.

2. **Governor's Executive Order No. 38.** On December 3, 2013, Governor Malloy issued Executive Order No. 38 to require the disclosure of certain information regarding the use of state economic assistance and tax credits in Connecticut. On or before March

31, 2014, the Department of Economic and Community Development (“DECD”) is to establish a searchable electronic database or databases that will contain the following information with regard to economic assistance (i.e. state-authorized grants, loans and loan guarantees) and state tax credits:

- The name and principal location of the recipient of the economic assistance
- The nature and type of economic assistance
- The amount or value of the economic assistance or tax credits approved or authorized by DECD
- The statutory authority for the economic assistance
- Any job-creation or job-retention agreements upon which the economic assistance depends, as well as the number of persons employed by the recipient at the time of the award and then later created or retained, and a statement as to whether the job-creation or job-retention commitments were met

In addition to the foregoing, the DRS is to provide to the DECD, on or before February 28, 2014 and annually thereafter, a report indicating the aggregate amount of each state tax credit that was claimed and, to the extent permissible, additional information concerning the size, type, and location of the businesses claiming the tax credit. The DECD, in turn, is then to post its analysis of the economic and employment impacts of each state tax credit program.

3. Governor’s Executive Order No. 37. On October 16, 2013, Governor Malloy signed Executive Order No. 37 mandating a review of all state regulations and purporting to implement a more transparent and efficient state regulatory process. The Executive Order solicited public comment, that was to be submitted by December 16, 2013, on regulations that have been in effect for greater than four years and whether any of those regulations are outdated, unnecessarily burdensome, insufficient or ineffective. Each state agency now is required to (i) review the public comments on regulations under its jurisdiction, (ii) conduct an independent review of all regulations under its jurisdiction and (iii) submit, on or before February 3, 2014, a report summarizing the comments received and review conducted and offering a plan to implement any recommendations the agency deems appropriate for eliminating or modifying any regulations. Effective immediately, the Executive Order additionally establishes new principles and procedures that a state agency is to follow in connection with the promulgation, repeal or modification of a regulation, including taking the following steps prior to any regulatory action:

- Identify its policy goals and whether the regulatory action is needed and the least burdensome means to achieve those goals
- Endeavor to encourage economic progress and the development of jobs in Connecticut



- Identify best practices for regulation, including using innovative and the least burdensome tools for achieving regulatory ends
- Develop, consider and make public a rigorous impact analysis that includes an analysis of both qualitative and quantitative costs and benefits and, where practicable, includes input from external experts and academic institutions
- Where appropriate, seek public input prior to issuing a formal notice of rulemaking
- Where an agency anticipates proposing a regulation of significant impact, give notice to the public no fewer than 60 days prior to submitting the proposed regulation to the Attorney General for review. “Significant impact” is defined, in part, as a regulation that has an adverse impact on small businesses or a significant financial impact on medium or large businesses.

Questions or Assistance?

Please do not hesitate to contact any member of our State and Local Tax Practice Group (listed on page 1) if you have any questions regarding the DRS legislative proposals or executive orders or their potential impact on you and your business.

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