CUMMINGS & LOCKWOOD LLC

CLIENT ALERT - A SUMMARY OF THE TAX LAW PROVISIONS OF THE 2024-2025 CONNECTICUT BIANNUAL BUDGET

June 20, 2023

On June 12, 2023, Governor Ned Lamont signed Connecticut's two-year, $51 billion budget into law. The budget is said to include the largest income tax cut in Connecticut history and includes approximately $500 million in tax relief to Connecticut taxpayers, primarily by lowering certain income tax rates, modifying the pass-through entity tax, and expanding or increasing certain tax credits. The historic tax cuts will benefit approximately 1 million (or almost 60% of all) tax filers. The most significant tax law changes include:

- **Reduction in Personal Income Tax Rates**. For tax years beginning on or after January 1, 2024, the Connecticut income tax rate on the first $10,000 and $20,000 of Connecticut income earned by single filers and joint filers, respectively, is reduced from 3% to 2%. The income tax rate on income greater than $10,000 but not more than $50,000 for single filers and on income greater than $20,000 but not more than $100,000 for joint filers is reduced from 5% to 4.5%. The reduced tax rates begin to phase out for single filers earning more than $105,000 and joint filers earning more than $210,000, and are capped at $150,000 for single filers and $300,000 for joint filers.
- **Revisions to Pass-Through Entity Tax.** Starting with the 2024 tax year:
    1. the pass-through entity ("PTE") tax becomes elective. PTEs electing to pay the tax must do so by giving the Department of Revenue Services written notice (1) for each tax year they make the election, and (2) no later than the due date for filing the return (taking any tax return filing extension into account).
    2. the standard base method for calculating the PTE tax is eliminated and all electing PTEs are required to use the alternative based method to calculate their PTE tax liability. Under this latter method, the PTE is subject to tax on (1) the portion of its Connecticut source income that flows through to owners who are resident or nonresident individuals, trusts or estates, plus (2) the portion of its total income not sourced to any state with which the PTE has nexus and that directly flows through to owners who are resident individuals.
    3. PTEs are required to file an income tax return on behalf of any nonresident member for whom the business is the only source of Connecticut income and are also required to make Connecticut income tax payments at the highest marginal tax rate for the year on behalf of nonresident members where the member's share of PTE income from Connecticut sources is at least $1,000.
    4. companies that are members of PTEs that pay the PTE tax or a substantially similar tax in another state are no longer permitted to claim an offsetting credit against their Connecticut

- corporation business tax liability for these tax payments.
5. the option for PTEs to file a combined return with one or more commonly controlled PTEs is eliminated. For this purpose, a PTE is commonly controlled if more than 80% of its voting control is directly or indirectly owned by a common owner or owners.

- **Expansion of Existing Exemption for Certain Pension and Annuity Earning.** Current Connecticut law allows taxpayers to deduct 100% of their qualifying pension, annuity and IRA income from their Connecticut taxable income if their federal adjusted gross income ("AGI") is less than (1) $75,000 for single filers or (2) $100,000 for married people filing jointly. Beginning with the 2024 tax year, the budget eliminates the retirement income tax "cliff" by extending eligibility for pension, annuity and IRA (other than Roth IRAs) income tax exemptions to taxpayers with AGI of (1) at least $75,000 but less than $100,000 for single filers, and (2) at least $100,000 but less than $150,000 for joint filers. However, the budget gradually reduces the deductions for these taxpayers until they fully phase out at $100,000 or $150,000, as applicable. The IRA deduction phases in over four (4) years - 25% of IRA income for 2023, 50% for 2024, 75% for 2025 and 100% for 2026 and future years.
- **Extension of Corporation Business Tax Surcharge.** The 10% corporation business tax surcharge is extended for three additional years to the 2023-2025 income years. The surcharge applies to companies that have more than $250 in corporation tax liability and either (1) have at least $100 million in annual gross income in those years, or (2) are taxable members of a combined group that files a combined unitary return, regardless of their annual gross income amount.
- **Cannabis Business Expense Deduction.** Starting with the 2023 tax year, Connecticut will decouple from the Internal Revenue Code with respect to the treatment of ordinary and necessary business expenses of a cannabis business. Under the budget, personal income and corporation business taxpayers holding medical or adult-use cannabis licenses are permitted to deduct, for Connecticut tax purposes, the amount of ordinary and necessary business expenses of the business. These expenses remain nondeductible for federal income tax purposes because marijuana is considered a controlled substance under federal law.
- **Repeal of Angel Investor Tax Credit for Cannabis Businesses.** Beginning July 1, 2023, the 40% angel investor tax credit for eligible investments in approved cannabis businesses is eliminated.
- **Increase of the Human Capital Investment Tax Credit.** Starting with the 2024 tax year, the budget increases the human capital investment tax credit that corporations may use to offset their corporation business tax liability from 5% of the amount paid or incurred for eligible investments to (1) 10% for most eligible investments, and (2) 25% for childcare-related investments. The budget also expands eligibility for the 25% credit and authorizes corporations to use the 25% human capital investment tax credits (i.e., credits for the child care-related investments) to reduce up to 70% of their corporation business tax liability each year (up from a 50.01% credit cap).

The 10% credit will apply to investments in:

1. in-state job training for in-state employees;
2. work education programs;
3. worker training and education for in-state employees provided by in-state higher education institutions;
4. donations or capital contributions to higher education institutions for improvements or technology advancements, including physical plant improvements; and
5. contributions made to the Individual Development Account Reserve Fund.

The following expenses are eligible for the 25% credit (up from 5%):

1. expenses paid for site preparation and planning, constructing, renovating, or acquiring facilities to establish a child care center for use primarily by in-state employees' children, and
2. subsidies to in-state employees for in-state child care.
3. donations or capital contributions to 501(c)(3) nonprofit organizations for site preparation and planning, constructing, renovating, or acquiring facilities to establish a child care center for use by children living in the community, including in-state employees' children.

- **Increase in Earned Income Credit.** Starting with the 2023 tax year, the earned income credit, which is a refundable state income tax credit for low and moderate income working individuals and families, is increased from 30.5% to 40% of the federal credit.

If you have any questions regarding this alert, please contact your Cummings & Lockwood private clients attorney.