Responding to the Pandemic: A Case Study

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Responding to the Pandemic: A Case Study

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Connecticut could have been a poster child in the recession and financial meltdown starting in 2007. It was one of the first states to be affected and one of the last to rebound. This time the state has caught a break. The stock market’s resiliency, now at pre-pandemic levels, has meant increased dividends and capital gains generating robust income taxes, unsurprising for a state that has one of the highest per capita incomes in the country.

Ironically, the hollowing out of New York City has also been a windfall, as those who left — often the wealthy — flocked to Connecticut. They realized that the view of Central Park from their penthouses along Fifth Avenue could be replicated, albeit on a smaller scale, from the backyards of their new spacious Connecticut homes. They traded in their views of the Hudson or East rivers with that of the Atlantic or Long Island Sound. They brought their income tax bases with them, and generated sales taxes as the purchase of new homes often does, through secondary and tertiary purchases of furniture and appliances, snowblowers and lawnmowers, trees and shrubs, windows and shades, and the like.

Connecticut has benefited from higher-than-anticipated tax revenues, both income and sales, which have gone a long way to eliminating its short-term budget deficit. And quite amazingly, Connecticut generated a $3 billion rainy-day fund.

Three tugs of war now exist between Gov. Ned Lamont (D) and his Democratic legislature. First, the rainy-day fund. Some within his party wants to devote the fund to pandemic tax relief — the governor does not. His view is that things may get worse, and then we will really need it. His worst case: another shutdown, another surge of the virus or its mutations, more unemployment, a loss of health care and child care, and a breakdown in the will to do what is needed to break the back of the pandemic. He may be aided by the provision in the stimulus plan that precludes states from using the revenue to finance tax cuts.

The cynical view is that the governor wants the rainy-day fund intact in case he runs for a second term, which he once hinted that he would not do. But he is riding high on his handling of the pandemic with strong approval ratings, and the fund would be useful to cushion cuts in spending, or even a source of tax cuts during an election.

Second, who will control the billions Connecticut will receive from the federal stimulus plan? The legislature wants a seat at the table.

Third, the governor is a true believer that increasing taxes on the wealthy would be bad for the state and even force people to leave Connecticut, contrary to the evidence. But that evidence is built around macro data; if only a few of the ultra-wealthy in Connecticut were to leave, they would dent the income tax. The governor can be expected to resist existing calls for a special surcharge on capital gains, proposals to raise the top individual and corporate tax rates, a state surcharge on residences above a certain value, and an increase in the estate tax.

For now, no one is willing to talk seriously about the 900-pound elephant in the room — $90 billion in debt, including unfunded pension

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22 Id.

23 Id.


liabilities. About 25 percent of the fixed-cost budget services this — one of the highest percentages in the country. The debt is lamented by all, but the hand wringing is more posturing without any serious attempt at reform. The debt continues to grow like a cancerous tumor, and if left unaddressed, will have the same inevitable deadly effects.

So, what is the land of steady habits doing to cope? Of all the threadbare ideas for dealing with the pandemic, the governor has proposed yet another tax amnesty. This will be the state’s seventh since 1990. This latest amnesty would wave penalties and cap interest at 3 percent over the next two fiscal years. The estimates are for no more than $40 million per year.

Amnesties are becoming a joke to the point that accountants are advising their clients to just wait for the next one. But this time may be different. For amnesties to work well, taxpayers must fear that a tax department will be coming at them if they don’t grab this one, last safety line. Taxpayers must be convinced “that the times, they are a-changin.” The state claims it is in the midst of overhauling its analytics division to use enhanced technology for better auditing. The question is whether taxpayers will assess this as a credible threat.

Next up is gambling. In a deal negotiated in the 1990s by then-Gov. Lowell Weicker (ACP), the Mashantucket Pequots and the Mohegan tribal nations have exclusive gaming rights in Connecticut in exchange for the state taking a 25 percent cut of the slots revenue. That deal has generated more than $8 billion to the state since its inception.

Lamont now wants to expand gambling. He reached an agreement with the Mohegan tribe, owner of Mohegan Sun casino, to allow it to offer sports betting and online gambling. The state wants a 13.75 percent tax on sports bets placed with the casino, whether online or in person, and a 20 percent tax on the rest of the tribe’s newly expanded powers. The Mohegans are said to have agreed to this — nothing in writing — and the Mashantucket Pequots, the other major tribe, is in separate negotiations. Unclear if either tribe has a most favored nations clause.

Another wild card is possible litigation by Sportech, a licensed vendor of off-track betting, arguing that sports betting is not a casino game. Both tribes have always argued that only they could operate sports betting. And just to complicate things a bit more, the Connecticut Lottery would now have the right to offer sports betting at new facilities in Bridgeport and Hartford, as well as online.

The fairness of further picking the pockets of those who are bad at math, as the saying goes, is questionable, if not immoral, especially when the governor will not increase taxes on the wealthy.

Visiting a casino illustrates that smoking and gambling go together. So why not legalize recreational marijuana? What faster way to get gamblers to lose more money, more quickly? Under a Senate bill cannabis possession of up to 1.5 ounces will be permitted for those age 21 and older. Right now, this potential tax base drives to neighboring states that have legalized it; we might as well keep these purchases at home where they can be taxed. As long as marijuana is illegal federally, however, financing for local

29 Id.
30 Id.
31 Id.
35 Id.
36 Id.
39 Id.
40 Id.
41 Ambrose Bierce quotes, Goodreads: “Lottery: A tax on people who are bad at math.”
entrepreneurs who want to enter the business remains a problem.

The dismal history of useless tax incentives is being repeated. The state waived sales taxes for 20 years for any data center that invests $200 million in the state. Or just $50 million if the facility is within a state-designated enterprise zone. It will be extended to 30 years if a $400 million investment is made, or if a $200 million investment is made in an enterprise zone. The exemption is needed, so its supporters claim, because the industry must continually update its equipment to remain competitive, a statement that would describe many others. And there is no study showing these incentives will pay for themselves — almost all do not.

As part of the deal, Connecticut would also waive its right to impose a financial transactions tax, like what was proposed by New York and New Jersey. Given the weaknesses in those taxes, it would be foolish for Connecticut to even think of adopting something similar.

These data centers are looked at as the industry of the future, rather than the fad du jour. The deal should be viewed as another misguided waste of money. The bill authorizes the municipalities where these data centers would be located to negotiate “host municipality fee agreements.” The state is not content to engage in “beggar thy neighbor” policies with neighboring states; now the municipalities are invited to do so with each other.

The governor said, “Connecticut needs to get in the game and bring this industry to our state.” But 11 data centers in Connecticut came without any incentives. Apparently, it is a game not worth playing. The delicious irony is that a bill that would have the state join an interstate compact to phase out corporate giveaways will also be coming up for hearings.

Rolling along. The governor could not get the Legislature to buy into his proposal on tolls, and so he is back with an unconstitutional alternative. He wants a highway usage fee on large trucks that pass through the state. Has no one heard of the commerce clause’s nondiscrimination requirement?

Finally, the governor just signed a bill to protect workers from double taxation by giving a credit for income taxes paid to states like Massachusetts, which is being sued by New Hampshire, for asserting nexus over nonresidents who used to work in Massachusetts but cannot do so because of the pandemic. Also covered would be New York under its convenience of the employer doctrine.

Exactly what the Connecticut bill does is unclear. The existing credit is administered by the Connecticut taxpayer attaching a copy of the tax return from the other state showing the amount of income tax paid there. Whether that state has acted unconstitutionally is not apparent from its tax return so that a credit is typically forthcoming. This new law is “full of sound and fury, signifying nothing.”

In that same vein is a tax on digital advertising based on Maryland’s defective law, which should be tied up in the courts for years. Maryland knew all about the defects in its tax when it was just a proposal, and yet chose to ignore them. A big splash to be sure, but Maryland’s tax will drown under years of litigation and eventually be struck down. Connecticut picked a lousy role model, although

45 Id.
46 Id.
49 Id.
54 Macheth, Act 5, Scene 5.
it has time to cure the defects in the Maryland legislation.

And so, Connecticut muddles along for now, letting a crisis go to waste when it could have been a catalyst for real reform. The billions Connecticut will shortly receive from Congress under the stimulus plan will certainly take pressure off the parties to act nobly. And the cancer that is the debt will continue growing.