



The New Tax Landscape:
Impact on Private Equity & Venture Capital Firms

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- Federal Tax Developments
 - Clawback or Giveback Financial Reporting
 - Deal Costs – FAS 141R
 - Debt-related Issues
 - Management Fee Waiver
 - Proposed Tax Rates
 - Qualified Small Business Stock
 - Proposed Carried Interest Legislation
- LLC Portfolio Company Structure: Benefit & Burdens
- State Tax
 - Multi-state Income Tax Issues
 - Sales and Use Tax Issues
 - Employment Tax and Reporting

Giveback (Clawback) Obligation

- Most Funds require the General Partner (GP) to return part or all of its prior 20% carried distributions (Giveback Obligation) if :
 - The LPs' minimum hurdle return not satisfied due to passage of time
 - Prior 20% carry allocations to GP exceed cumulative net gain because of subsequent losses
- Recent reduced valuations may create a current Giveback Obligation of the GP
 - The Fund financial statements must reflect the Giveback Obligation of the General Partner via a reduced or negative GP capital account
- In certain situations, the Giveback Obligation is typically reduced for a hypothetical income tax:
 - Highest marginal federal and state tax rate of the GP members
 - Reduce overall rate for federal benefit of state tax deductions – AMT complications?
 - *Example: \$100 gain less: 15% federal tax and 10% NY Tax = \$75* (assumes no federal benefit for the \$10 of state tax paid due to AMT)
- Tax Allocations:
 - Giveback Obligation may change how taxable income or loss is allocated
 - Consider GP cash distributions as an advance if insufficient basis to avoid gain recognition for distributions in excess of tax basis.

Deal Costs - FAS 141R

- **GAAP:** Under recently issued FAS 141R, most acquisition related costs must now be expensed rather than capitalized for financial purposes.
- **Tax:** Tax Regulations (1.263(a)) require capitalization of any costs which are “inherently facilitative” to the transaction. Examples include:
 - Most costs incurred after the LOI is executed
 - Legal fees incurred to negotiate the purchase agreement
 - Success-based fees require special level of scrutiny and documentation because presumption exists under IRS guidance that these costs are inherently facilitative
 - **Example: Investment Banking Fee is a success based fee that needs to be allocated for time spent before and after the LOI.**
 - **PLR 200830009 supports corporate deduction when shareholders sold stock and target corporation hired and paid expenses**

Tax treatment of debt purchased at discount

- Market discount on bonds is treated distinct from original issue discount (OID) under the Tax Code.
- OID is included in taxable income ratably over the life of the debt, whereas accrued market discount interest income is recognized only when principal payments are received.
 - Election can be made to include the accrued market discount in income annually
 - Market discount does not impact any pre-existing OID on note, inclusion in income still required for any OID
- Principal payments will be ordinary income to the extent they do not exceed “accrued market discount.” The remainder will reduce basis.
- Market discount is effectively amortized over the remaining debt term.
 - Amortization can be calculated using “ratable accrual” method (straight line) or under “constant interest rate” method
 - Constant interest rate method typically confers benefits on taxpayers purchasing at a discount.

Tax treatment of debt purchased at discount

- Assume a fund purchases debt originally issued for \$100 million for \$40 million.
- The debt bears a 7% coupon and provides for one principal payment of \$50 million in Year 2 and an additional principal payment of \$50 million in Year 4.
- The taxpayer elects the ratable accrual method for market discount.

	Interest Income	Market Discount Accrual	Principal Payments	Market Discount Income	Reduction in Note Basis
Year 1	7	15			
Year 2	7	15	50	30	20
Year 3	3.5	15			
Year 4	3.5	15	50	30	20
Total	21	60	100	60	40

Cancellation of Indebtedness Income

- **General Rule:** A debtor must recognize income to the extent debt has been cancelled (“COD Income”).
- **Exceptions Under Section 108:** Under this provision, no COD income is recognized in certain situations such as in Bankruptcy or to the extent the debtor is insolvent.
- **2009 Tax Act – Five Year Deferral:** If an issuer reacquires its outstanding debt in 2009 or 2010, recently modified Section 108(i):
 - Allows the issuer to defer recognition of COD income over a five year period beginning in 2014.
 - OID interest expense deductions on any replacement debt is deferred to match the recognition of the COD income.
 - Debt instrument must meet certain criteria

Section 108(i) Five Year Deferral Criteria

- Issuer must reacquire debt for
 - Cash
 - Debt for debt exchange
 - Exchange for stock of a partnership interest in the issuer
 - As a contribution to capital, or
 - As a result of a creditor's complete forgiveness.
- Issuer must be a C Corp or the issuer must have incurred the indebtedness in connection with a trade or business.

High Yield Discount Obligation – Sec. 163(e) Interest Disallowance

- Impact: HYDO OID Interest Expense (Sec. 163(e)(5))
 - Permanently Disallowed – to the extent the interest exceeds the IRS rate plus 6%.
 - Deferred – The remaining accrued OID interest expense is deductible when paid.
- Applicable HYDO Debt (Sec. 163(i))
 - The term exceeds five years
 - The interest rate equals or exceeds the IRS rate plus 5%
 - October 2009 AFR rate is 2.66 % and was as low as 1.65% in February 2009
 - The debtor is a C Corporation
 - Significant OID is unpaid after five years
- HYDO rules tested when debt issued
 - A significant debt modification treated as new debt issuance

Partial Suspension of HYDO Interest Disallowance

- The American Recovery and Reinvestment Act of 2009, PL-111-5, has suspended this disallowance of interest for debt for debt exchanges occurring between September 1, 2008 and December 21, 2009.
- This is particularly helpful for many of the refinancing transactions that have taken place in the current economic environment.
- This suspension does not apply to newly issued debt instruments.

Debt Modification

- A modification to a debt instrument can be a taxable event.
- The following are examples that would generally be considered to be significant modifications to debt. (Reg. Sec. 1.1001-3)
 - Change in yield more than the greater of 25 basis points or 5% of the annual yield on the unmodified instrument ($.05 \times$ annual yield).
 - Changes in the timing of payments would be considered a significant modification if it results in the material deferral of scheduled payments. This is a facts and circumstances analysis, however there is a safe harbor.
 - Safe Harbor – begins on the original due date of the first scheduled payment that is deferred and extends for a period equal to the lesser of 5 years, or 50% of the original term of this instrument.
 - A change in the obligor of an instrument is also a significant modification.

Proposal to Eliminate UBTI on Debt Financed Property

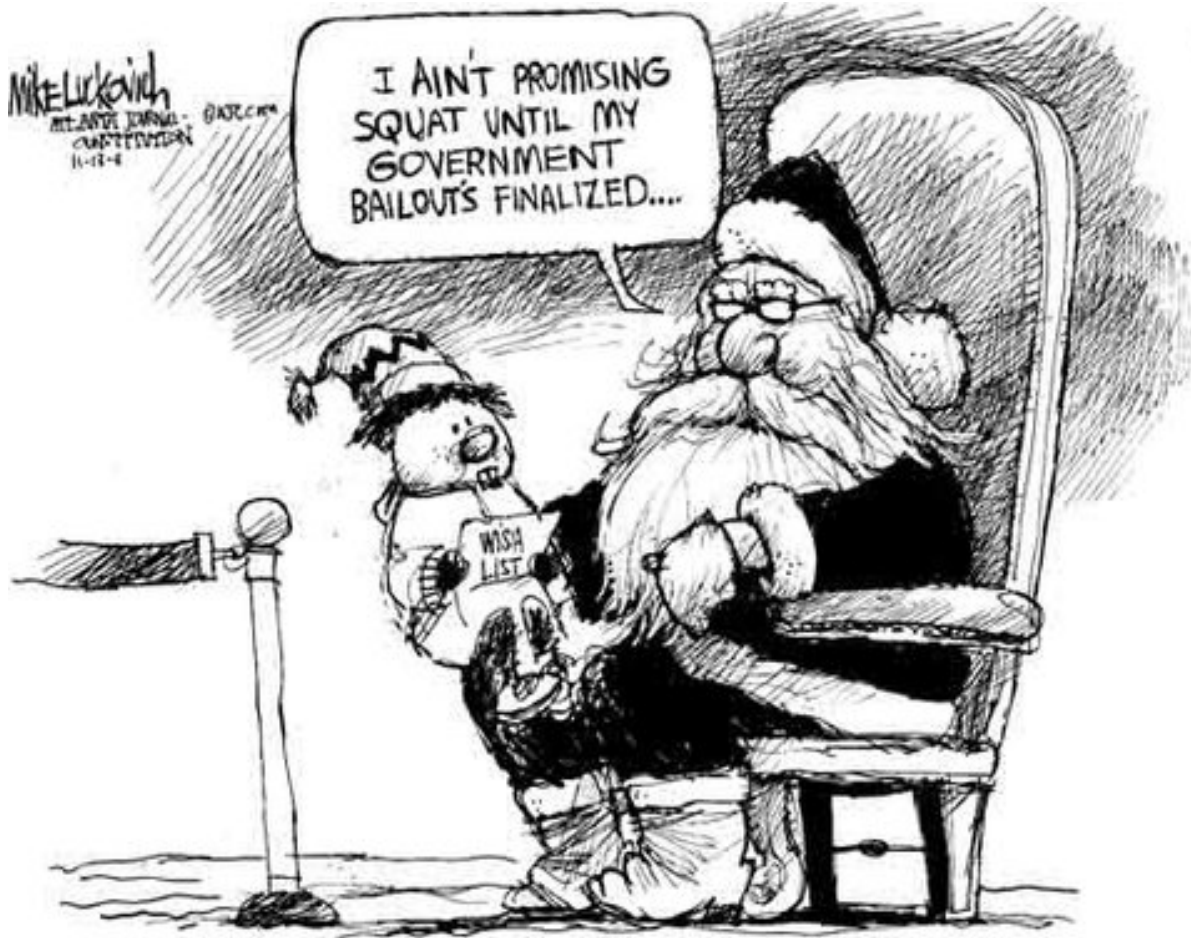
- **Current Law:** Gain from the sale of property financed directly or indirectly (e.g., through a partnership) with debt is treated as Unrelated Business Taxable Income (“UBTI”)
 - UBTI does not apply if the property is sold more than 12 months after the debt is paid off
- **Proposal:** Proposed legislation would provide that debt incurred by an entity treated as a partnership for tax purposes would not be treated as acquisition indebtedness under the UBTI rules of Section 514.
 - This should eliminate the need for non-US “blocker corporations”
 - The tax-exempt institution must be a limited liability partner directly or indirectly through a tiered partnership structure.

- **Effective date:** Non-public enterprises must comply with FIN 48 for fiscal years ending after September 15, 2009.
- **More likely than not standard:** FIN 48 provides a standard for determining when a tax contingency reserve is required; any position that is “not more likely than not” ($\leq 50\%$) will now be reserved.
- **Impact:**
 - Because most funds are structured as partnerships and have no federal income tax liability, the main disclosures will relate to state issues.
 - Portfolio companies structured as C Corps will have to consider both federal and state income tax contingencies.

FAS 109 and FIN 48 Continued

- The FASB amended disclosure rules for non-public entities. These include:
 - Elimination of requirement for an entity to provide a tabular reconciliation that reports the total balance of unrecognized tax benefits at the beginning and end of the tax period.
 - Elimination of the requirement that the entity report the potential effect of recognition of all unrecognized tax benefits on its rate.
 - The FASB will however require a non-public entity to report on the events reasonably possible to occur that could significantly increase or decrease an entity's unrecognized tax benefits within the next 12 months.
 - Non-Public entities are required to provide details related to tax years still subject to examination in major jurisdictions.

Proposed Tax Legislation



Income Tax Rate Proposals – High Income Joint Returns

Taxable Income	Pre-2002	Current	Proposed
LT Capital Gains	20%	15% Sunsets 2010	20% Effective 2011
Qualified Dividends (Debt Recaps?)	39.6%	15% Sunsets 2010	20% Effective 2011
Ordinary Income	39.6% Over \$349,700	35% Over \$372,950	*Top rate reverts to 39.6%
Healthcare Surtax	None	None	5.4%
AMT Ordinary Income	28%	28%	28%
C Corporations	35%	35%	35%



Planning for Proposed Increased Tax Rates

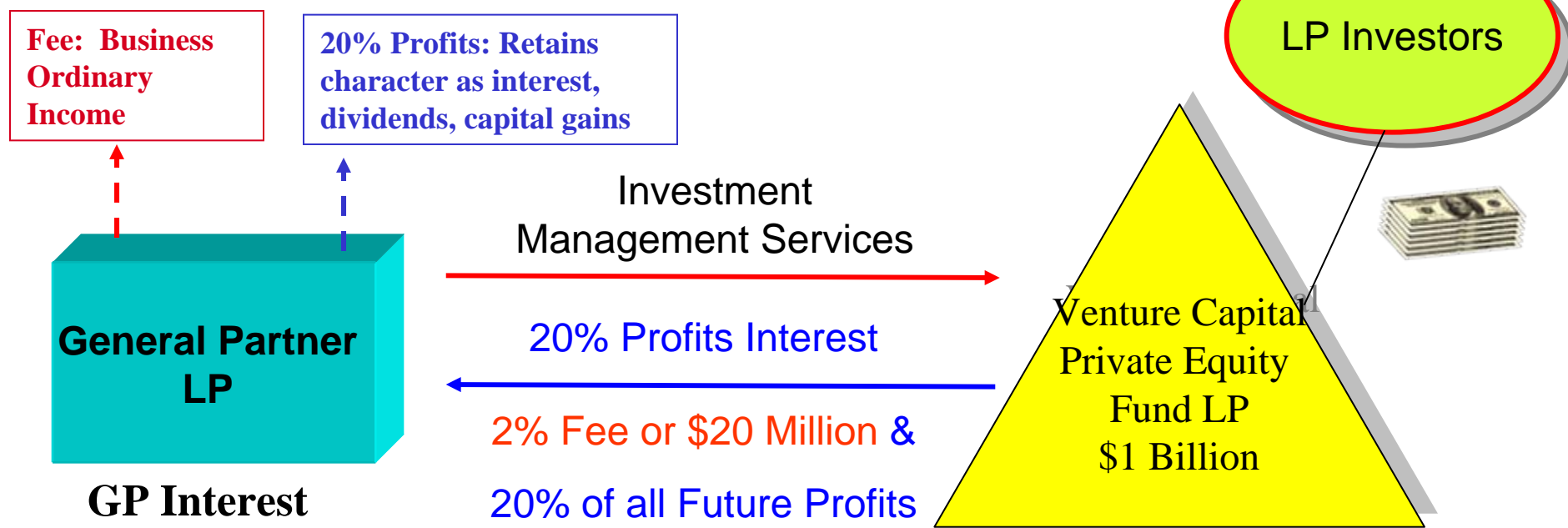
- Accelerate Ordinary Income or Defer Deductions?
 - 5% permanent savings but time value of money cost
 - Breakeven utilizing a 6% discount rate is about 2 years
 - Example: Accelerate \$100 of income payable in 2012 to 2010
 - 2012 tax at 39.6% would be \$39.60
 - The present value of this tax in year 2010 would be \$35.24 compared to \$35 tax in year 2010
- NOL: Carryback or Carryover?
 - Effective tax rate and AMT considerations
- 20% Capital Gain Rate
 - 5% permanent savings if gain recognized before effective date
 - Time value of money breakeven is about 5 years with a 6% discount rate
 - Installment sale effective date – previous changes when gain recognized.

Capital Gain Exclusion for Qualified Small Business Stock

- Current Law
 - *May exclude 50 percent of the eligible gain* of sale of certain small business stock, acquired at original issue from the corporation and held at least 5 years
 - *Exclusion increased to 75%* for stock acquired in 2009 and in 2010
 - Taxable portion is taxed at a maximum rate of 28%
 - 7% of the excluded gain is a preference item for AMT (scheduled to increase to 28% for eligible stock acquired after December 31, 2000 and 42% for stock acquired before that date)
 - Amount of eligible gain for exclusion is the greater of:
 - 10 times the taxpayer's basis in eligible stock disposed of during the year, or
 - \$10M reduced by gain excluded in prior years on disposition of the corporation's stock
 - **Small business:** Corporation's gross assets cannot exceed \$50 million when stock is issued (includes stock), cannot be an S-Corp, and must be an active business
- Proposed Change (Effective for QSBS issued after February 17, 2009)
 - *Percentage exclusion for qualified small business stock would be increased to 100%*
 - *AMT preference item for excluded gain would be eliminated*
 - Additional documentation requirements to assure compliance with statute
- Benefit Example: \$10 million eligible gain @ 20% = \$2 million plus state

Partnership Profits Interest Received For Services – “Carried Interest”

- **Profits Interest for Services:** GP Manager receives a right to a share (e.g., 20%) of the *future profits* of the Fund LP without regard to any capital investment.
- **Gen. Rule - Tax-Free:** If there is risk as to whether a profit will be earned and the interest is not disposed of within 2 years, the receipt of the profits interest is generally not currently taxable. (*See Rev. Proc. 93-27 for other requirements*).
- **Future Profit Allocations Retain Character:** Allocated partnership income to the GP Manager retains its character as interest, dividend or capital gains rather than treated as compensation for services.



Partnership Equity Compensation – Profits Interests

- Rev. Proc. 93-27, 1993-2 CB 343
 - Receipt of a profits interest for the provision of services to, or for the benefit of, a partnership in a partner capacity or in anticipation of being a partner will not be a taxable event for either the partner or the partnership
 - Three exceptions
 - Interests relating to a substantially predictable stream of income
 - Interests disposed of within two years of receipt
 - Interests in publicly traded partnerships
- Rev. Proc. 2001-43, 2001-34 IRB 191
 - Clarifies that the receipt of an unvested profits interest will not be a taxable event upon either receipt or when it vests so long as:
 - Service partner is treated as owning the interest from the date of grant
 - Partnership does not deduct the FMV of the interest either when it is granted or vests
 - The other requirements of Rev. Proc. 93-27 are satisfied.

Levin's Proposal to Tax Carried Interest Gains as Ordinary Income: HR 2834 and HR 1935

- Tax Impact: **Ordinary Income Treatment**
 - A Service Partner must recharacterize any net income allocated with respect to an Investment Services Partnership Interest (“ISPI”) as ordinary income
 - Any gain on disposition of an ISPI is ordinary income
 - Gain would be triggered on distribution of appreciated property to an ISPI and treated as ordinary income
 - Treats any net loss as ordinary loss, but defers recognition until future income allocated or ISPI disposed
- Self Employment Income - Section 1402 Applies
- Investment Services Partnership Interest (“ISPI”)
 - Interest held by a person that (directly or indirectly) provides a substantial quantity of certain services (“Covered Services”) with respect to certain assets (“Specified Assets”) of a partnership in the conduct of the trade or business of providing those services
 - May include certain related party loans and derivatives

- Covered Services
 - Advising On The Purchase And Sale Of Specified Assets
 - Managing, Acquiring Or Disposing Specified Assets
 - Arranging Financing With Respect To Specified Assets
 - Supporting Any Of The Foregoing
- Specified Assets
 - Securities (Including Stock In A Corporation And Any Evidence Of Indebtedness)
 - Real Estate (Excludes Operating Real Estate Businesses)
 - Commodities
 - Partnership Interests
 - Options Or Other Derivative Contracts On These Assets

- **Qualified Capital Interest**
 - FMV of money or other property contributed to partnership in exchange for interest
 - Any amounts included in income under Section 83 with respect to the transfer of such interest
 - Excess of income and gain items over loss and deduction
 - Reduced by distributions (and, if applicable, excess of losses and deductions over income and gain)
- **Exclusions from Qualified Capital Interest**
 - Phantom Capital
 - Does not apply to purchase price of interest acquired from third party

- Qualified Capital Interest (cont.)
 - For exception to apply, allocation to QCI must be same as allocation to unrelated, non-service partner **and** the allocation to the unrelated, non-service partner is significant compared to the service partner's allocation
 - What if there are no unrelated, non-service partners?
 - In determining whether an allocation to a service partner is the same, *amounts loaned or guaranteed by non-service partners are treated as capital*

■ Anti-Abuse Provisions

- Applies to “disqualified interests” in an entity for which a person performs (directly or indirectly) investment management services and the value of that interest (or payments related thereto) is related substantially to the amount of income or gain (realized or unrealized) from the assets with respect to which the services are being performed
- **WATCH OUT! - 40% PENALTY**



Administration's Carried Interest Proposal

- Allocated Profits Interest Income Items Treated as Ordinary Compensation Income
- Broader Scope: Applies to all Service Providers – i.e., not limited to Investment Managers
- Includes Gains from Derivatives & Other “Disqualified Interests”
 - A person who performs services for an entity and holds a “disqualified interest” in the entity is subject to ordinary income tax on any gain received with respect to the disqualified interest
 - “Disqualified Interest” – convertible or contingent debt, an option, or any derivative instrument with respect to the entity, but does not include a partnership interest or stock in certain taxable corporations
- Effective for taxable years beginning after December 31, 2010

Fund Investment Expenses & Individual Limitations

- PE/VC Fund LP: Typically treated as an investment activity
 - Management and other expenses treated as investment expenses
 - *Rev. Rul. 2008-39* treats Fund expenses related to the management of an investment in a lower tier operating partnership as an investment expense rather than a business expense.
- Investment Expense Limitations to Individual Investors
 - Investment expenses are phased-out under the 2% AGI rule of Sec. 67
 - Investment expenses are not deductible for AMT purposes
- Other Taxpayers
 - Corporations – no limits
 - Tax-exempts – not applicable

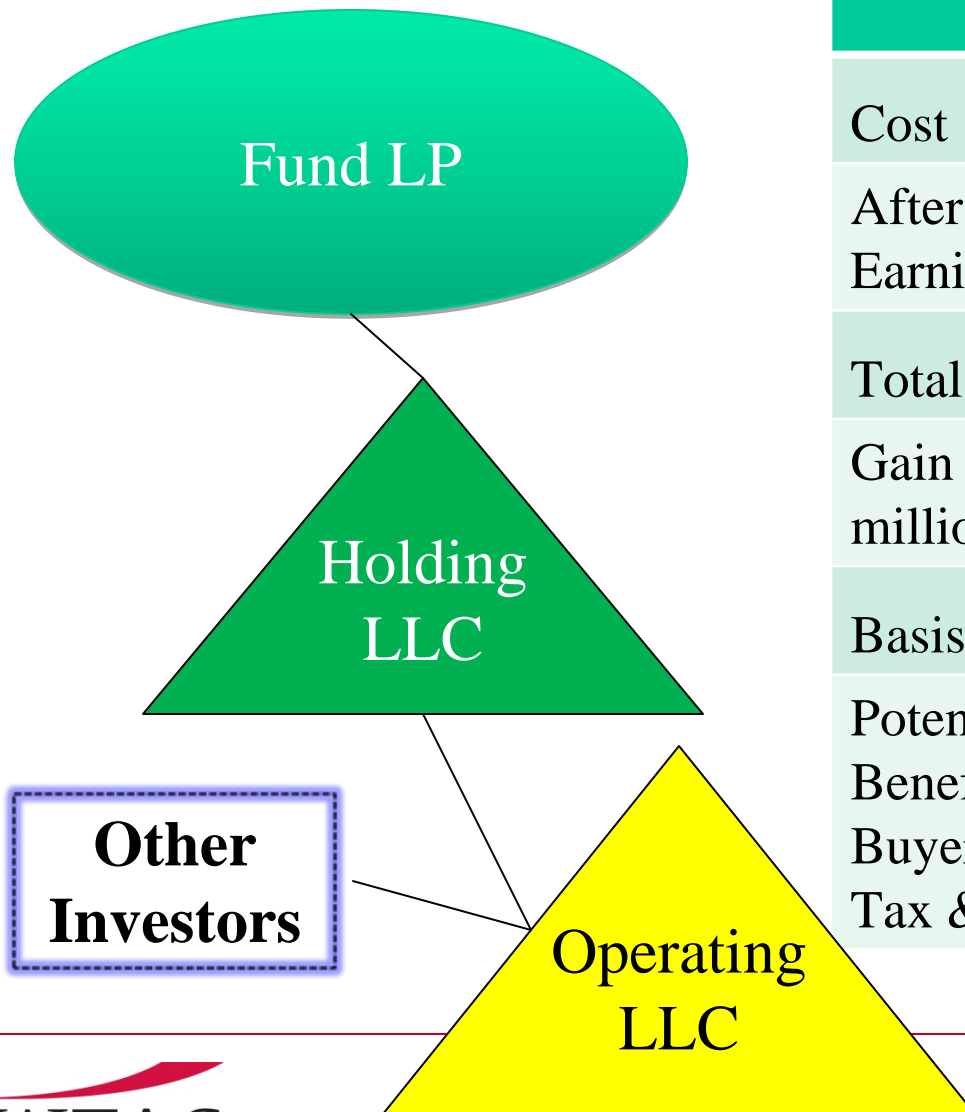
Management Fee Waiver

- Expected Tax Benefit:
 - Convert 35% ordinary income to 15% capital gain
 - Defer income until portfolio company sold at a gain
- How
 - GP waives right to a portion of its annual management fee before it is earned
 - Fund LP agreement should provide for an increased GP Profits Interest equal to the waived management fee
- Economic Risk
 - Fund must have future profits in order to receive waived management fee
- Tax Risk
 - Proposal to treat profit interest gain as ordinary income
 - Future ordinary rates may increase to 39.6% or 45%

Structuring Portfolio Company as a Flow-thru LLC

- Becoming more common to structure some portfolio investments utilizing a flow-thru entity (e.g., LLC)
 - Many Fund agreements permit a limited amount of UBTI investments
 - Investors, rather than the portfolio company, will pay tax on operating income
- Key Advantages:
 - *Less Gain On Sale:* Company's after tax earnings can be distributed tax-free or will reduce gain on sale
 - *Potential Premium Upon Sale:* Buyers typically will pay more because of their ability to deduct goodwill over a 15-year period
 - Assuming a 40% tax benefit and 7% discount rate, the present value of the tax deductions associated with the goodwill equal a potential 24% purchase premium.
 - Buyers and sellers typically split this premium, how much each party receives is subject to negotiation.

LLC Portfolio Company Structure Illustration



	C Corp	LLC
Cost	\$60	\$60
After Tax Earnings	<u>N/A</u>	<u>40</u>
Total Basis	<u>\$60</u>	<u>\$100</u>
Gain -\$200 million Sale	<u>\$140</u>	<u>\$100</u>
Basis Step-Up	<u>None</u>	<u>\$100</u>
Potential Tax Benefit to Buyer (40% Tax & 7% PV)	None	\$40 Million Payable 15 Years = \$24 Million PV

Potential Disadvantages

- Increased Tax Filings and Costs
- Generally cannot qualify for a tax-free stock for stock exchange
- Need to incorporate upon an IPO
- Tax-exempt and foreign investors receive UBIT/ECI – consider utilization of parallel fund structure with blocker corporation to mitigate impact
- IRS and State adjustments impact investors' prior returns
- Proposed individual tax rate increase would impact pass-through income allocable to individual investors

State Taxes

Multistate Income Tax Issues

- What do we mean by “sourcing?”
 - Corporations and partnerships
 - Formula approach
 - Individuals
 - Residency
 - All
 - Non-Residency
 - Formulary flow-through
 - Nature of underlying investment

Multistate Income Tax Issues

- Hot Issues for Individuals
 - Changes in residency
 - Recent Illinois Case – *Dods v. IDOR*
 - Treatment of sale of intangibles for non-residents
 - Federal legislation
 - Sales of partnership interests
 - Ohio – *Ohio Rev. Code Ann Sec. 5747.212*
 - New York – TSB-M-92(2)I
 - California – *Valentino v. Franchise Tax Board*
 - Treatment of Carried Interest

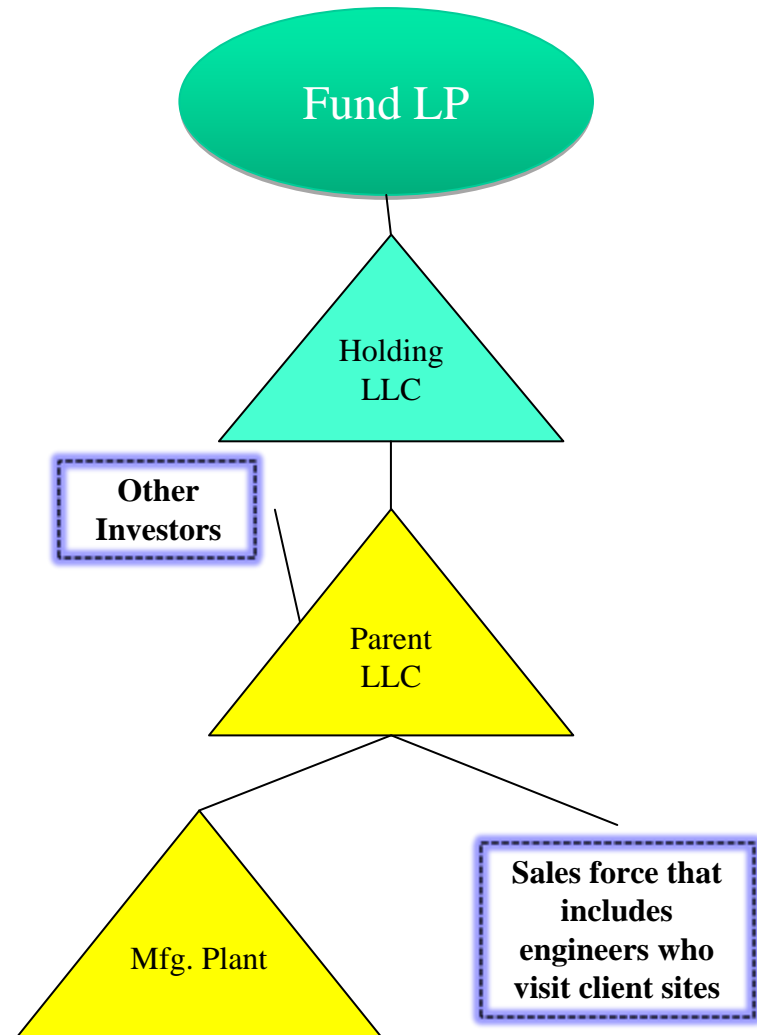
Multistate Income Tax Issues

- Hot Issues for Corporate and Partnership Entities
 - Ability of states to reach income not connected with activities in the state. *Meadwestvaco Corporation v. Illinois DOR*
 - Trend towards single factor
 - Tax policy, which exports tax liability
 - **Example:** Company's headquarters and main manufacturing locations are in Illinois. Company has no property or payroll in California, but has 50% of its sales in that state. The Company earned \$1000 of income.

Single Sales Factor Answer - \$500 subject to California tax
Three Factor (property, payroll sales) Answer - \$166 subject to California tax
 - Further trend towards “market” sourcing for services, income from intangibles, etc.

Structuring - Nexus

- Use of alternative structures may protect investors from multistate income tax liability and compliance burden
- Scenario
 - Investment in a flow-through multistate service provider creates nexus for partners
 - Resolution - Create corporation to hold nexus creating activities.



Income Tax Summary

- Structuring
 - Protection of investors
 - Limiting states connection
 - Computing the tax

Illinois Developments

- Illinois tax environment
 - Budget gap
 - Initiative to raise rate
 - Constitutional limitation on corporate taxation
 - 2009 developments
 - Reasonable compensation
 - Change in calculation of credit for taxes paid by to other states by an Illinois resident

Sales & Use Tax Opportunities

- Sales tax issues as a result of business operations
 - Uncollected Sales Taxes
 - Collected But Unremitted Sales Taxes
 - Unpaid Tax Due on Purchases

- Potential remedies/ protections
 - Voluntary Disclosure Programs
 - Bulk Sales Notification
 - Use of Successor Liability Rules
 - New Registrations

Sales & Use Tax Opportunities

- Purchase of big-ticket items
 - Aircraft
 - Artwork
 - Intangibles
 - Production related equipment

- Trends to minimize tax
 - Location of transfer of ownership / possession
 - Retail versus Casual or Occasional sale
 - Form of ownership interest
 - Establish exempt use

Employment Tax Restart Planning

In certain situations a successor employer may consider wages paid by a predecessor employer when determining whether or not an employee has reached the FICA, FUTA or SUI wage base limits.

The following illustrates a typical refund opportunity resulting from the misapplication of employment tax successor rules. Rates and wage bases vary by state.

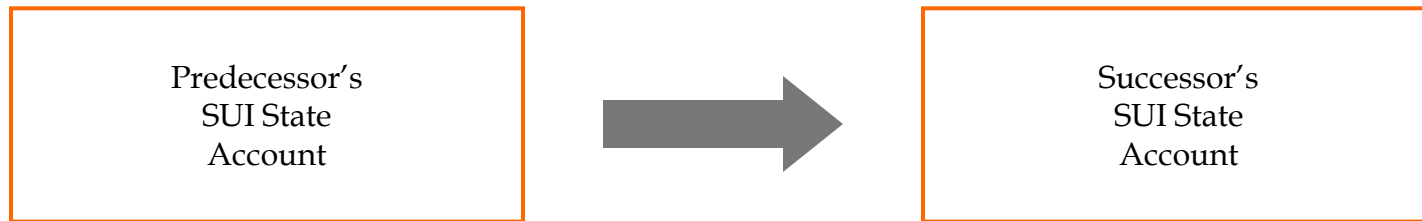
Facts: Transaction closed June 1st Number of employees transferred 860, States of operation CA, NY, MA.

Payroll breakdown 10% exceed FICA, 100% exceed SUI, and 100% exceed FUTA. Successor wage base rules we not applied at time of transfer.

FICA	$86 * 186 = \$15,996$
FUTA	$860 * 56 = \$48,160$
CA	$7,000 * 5\% = \$350 * 260 = \$91,000$
NY	$8,500 * 6.8\% = \$578 * 200 = \$115,600$
MA	$14,000 * 4.2\% = \$588 * 400 = \$235,200$

Savings \$506,000

State Unemployment Tax Due Diligence Planning



- Successor employer status required to qualify for the following:
 - SUI wage base transfers
 - Transfers of unemployment experience rates
 - Transfers of employment tax liabilities

- Research required as:
 - Transfer rules vary by state
 - Wage base transfers vary by state
 - Application for transfers vary by state
 - SUTA Dumping rules must be reviewed

State Unemployment Tax Due Diligence Planning

Transfer example:

Assumptions:

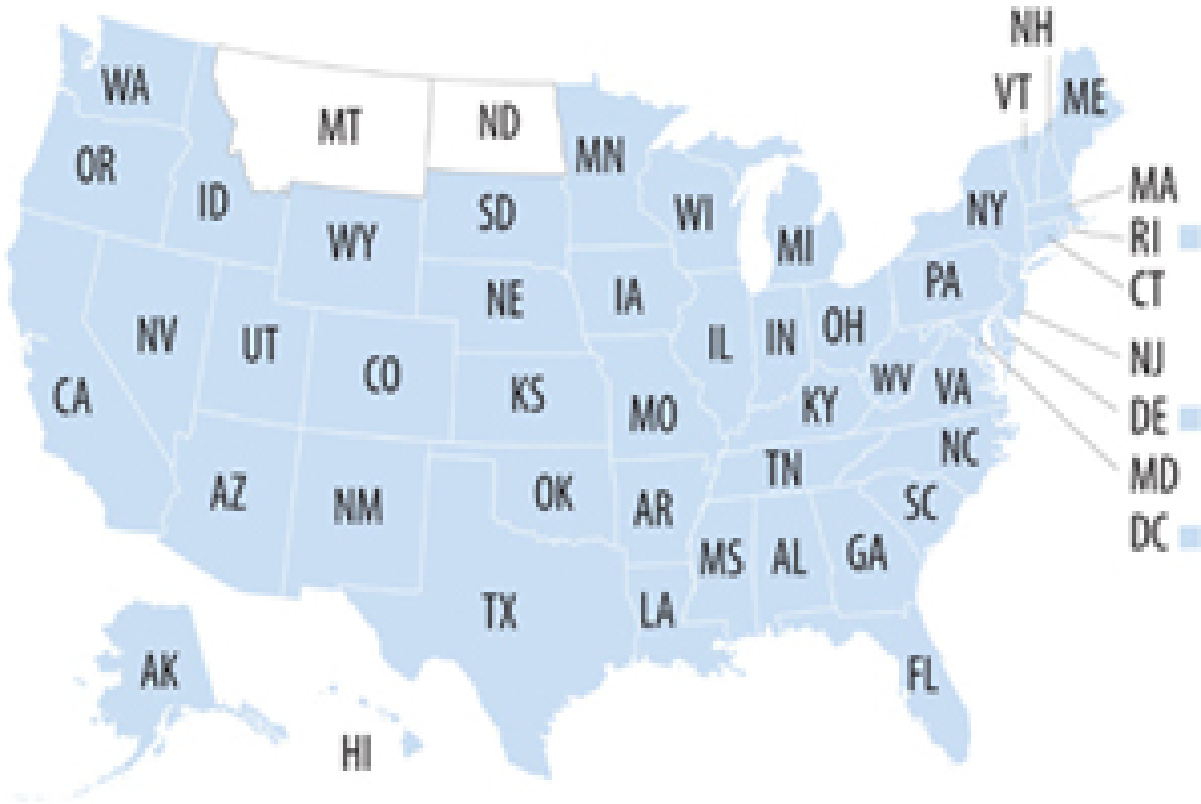
A Distinct and Severable Portion of Business, (e.g. 90%)
is Transferred to NewCo
Wage Base \$9,000

OldCo
10,000 Employees
SUI Rate 6.8%
SUI Cost \$ 6,120,000

9,000
Employees
Transferred

NewCo
9,000 Employees
SUI Rate 3.1%
SUI Cost \$2,511,000

48 States Face Budget Shortfalls



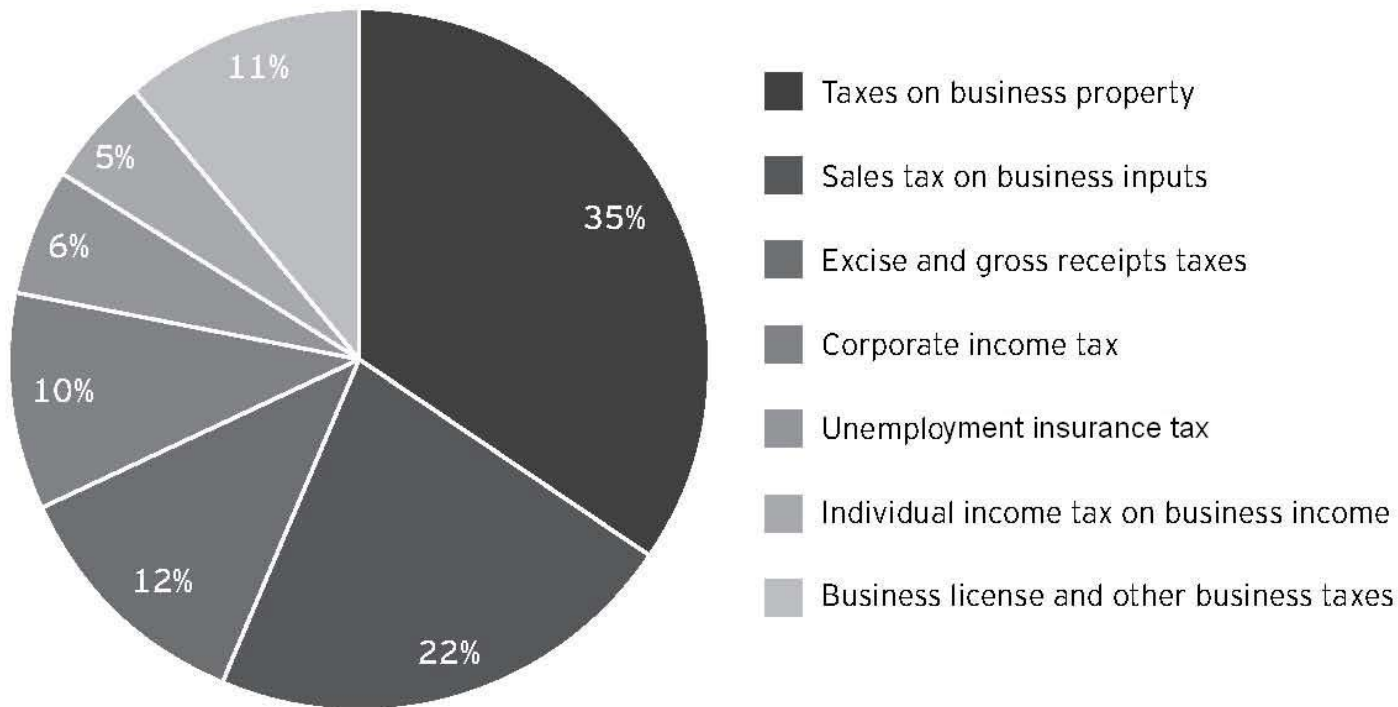
Note: Includes states with shortfalls in fiscal 2010

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- At least 48 states addressed or still face shortfalls in their budgets for the upcoming year.
 - Even before the new fiscal year starts July 1, new shortfalls of \$23 billion have opened up in the adopted 2010 budgets of at least 12 states and the District of Columbia. Shortfalls for fiscal year 2010 – those already addressed and those still open -- total \$166 billion.
 - At least 29 states have prepared estimates for the 2011 fiscal year. Initial estimates of these shortfalls total almost \$38 billion. As the full extent of 2011 deficits become known, shortfalls are likely to equal \$160 to \$180 billion.
 - Combined budget gaps for the remainder of this fiscal year and state fiscal years 2010 and 2011 are estimated to total over \$350 billion.

SELECTION OF STATES WITH PROJECTED FY2010 AND FY2011 BUDGET GAPS

State	FY2010 Gap	FY2010 - % Of Budget	FY2011 Gap	Percentage of FY2010 General Fund Budget
Arizona	\$4.0 billion	41.1%	\$2.6 billion	26.7%
California	\$53.7 billion	58.2%	\$15 billion	16.3%
Connecticut	\$4.1 billion	23.2%	\$978 million	5.6%
Florida	\$5.9 billion	22.8%	N/A	N/A
Georgia	\$3.9 billion	22.3%	Unavailable	N/A
Illinois	\$9.2 billion	33.0%	N/A	N/A
Maryland	\$1.9 billion	13.6%	\$1.2 billion	8.7%
Massachusetts	\$5.0 billion	17.9%	Unavailable	N/A
New Jersey	\$8.8 billion	29.9%	Unavailable	N/A
New York	\$17.9 billion	32.3%	\$2.2 billion	3.9%
North Carolina	\$4.6 billion	21.9%	\$4.4 billion	21.0%
Pennsylvania	\$4.8 billion	18.0%	N/A	N/A
Texas	\$3.5 billion	9.5%	N/A	N/A
Virginia	\$1.8 billion	10.9%	Unavailable	N/A
Washington	\$3.6 billion	23.3%	Unavailable	N/A

Composition of Total State and Local Business Taxes, FY2008

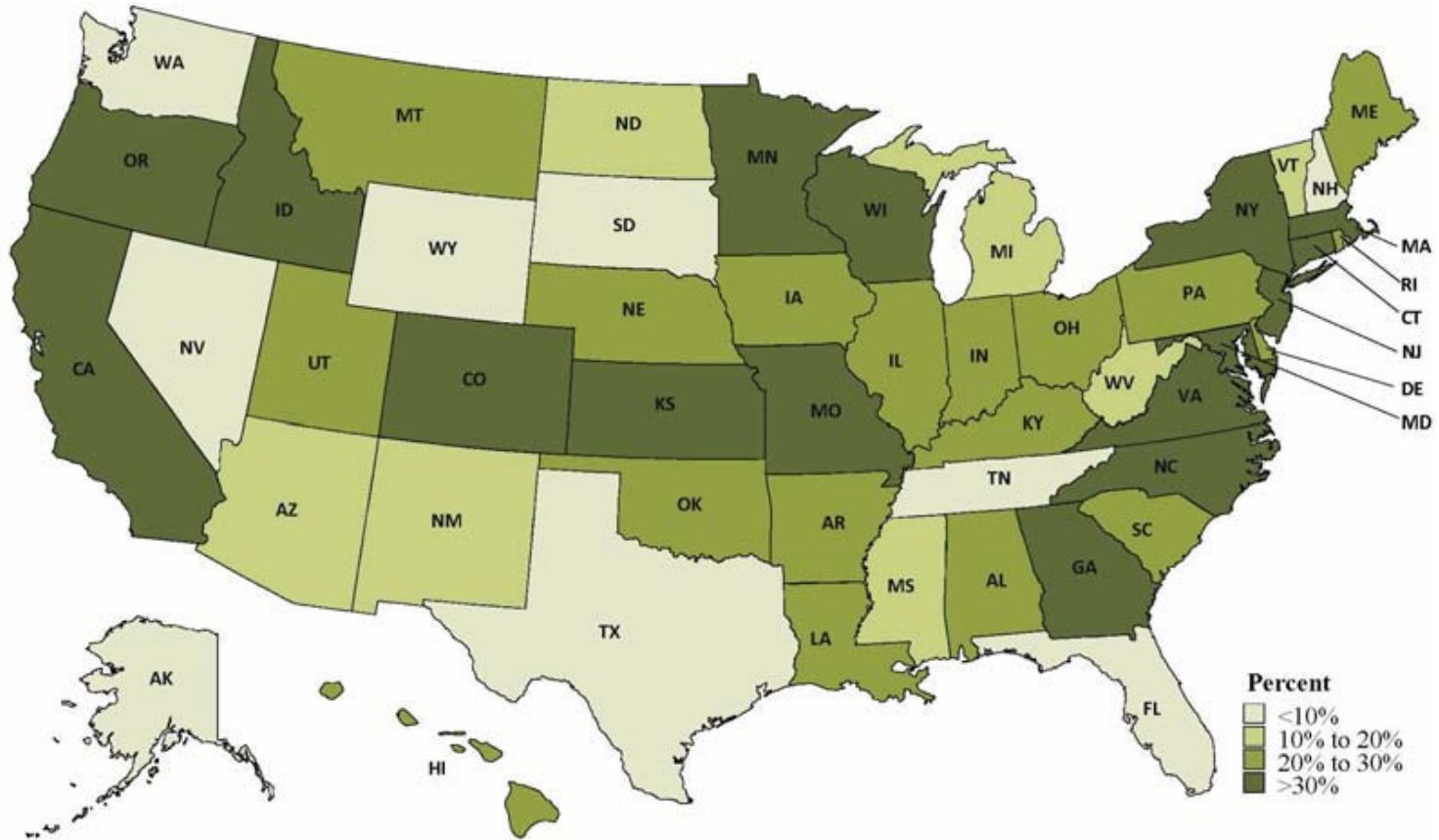


Figures do not appear to sum due to rounding

Total State and Local Business Taxes, FY2007-FY2008 (\$ billions)

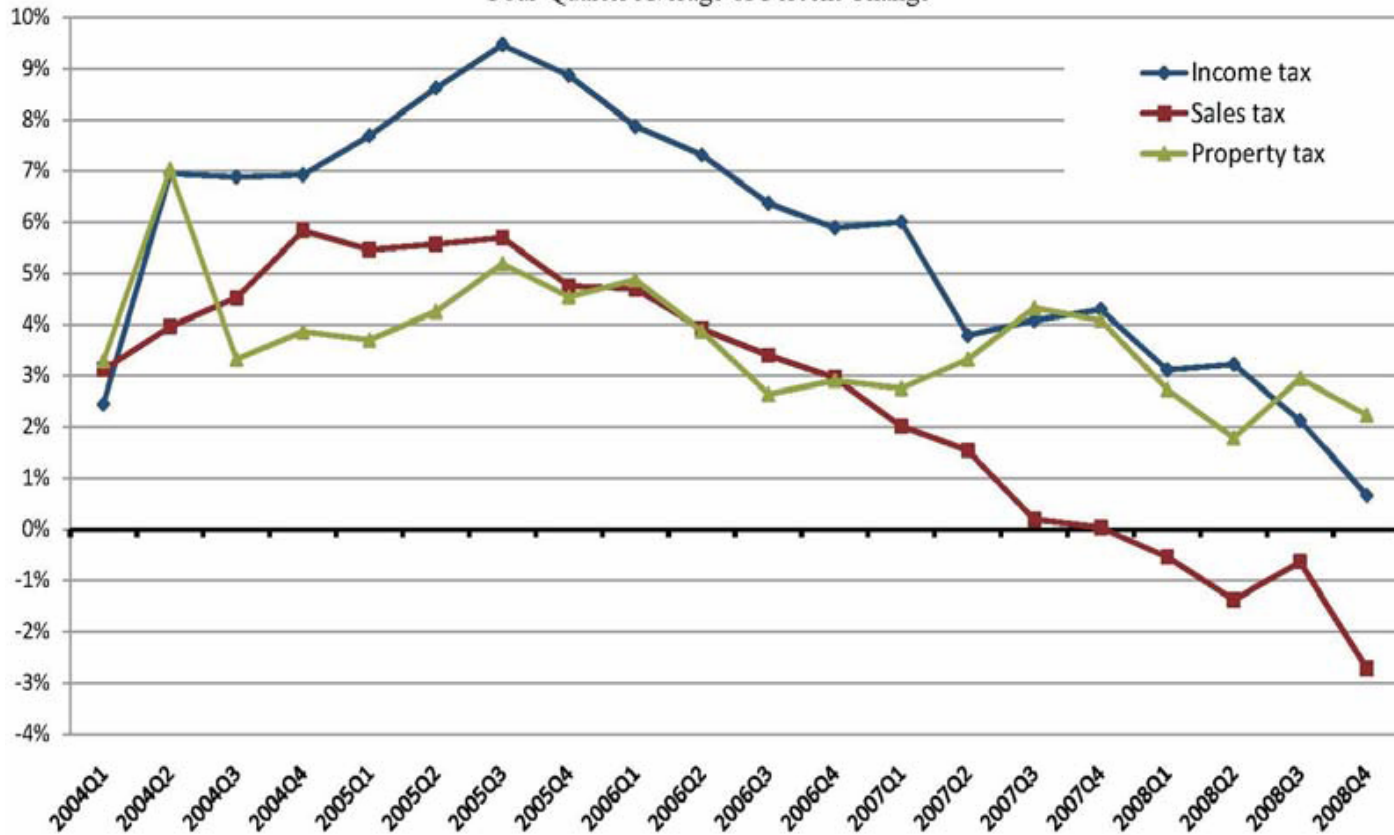
Business tax	2007	2008	% Total taxes	One-year growth
Property taxes on business property	\$199.5	\$209.3	35.5%	4.9%
General sales taxes on business inputs	\$129.0	\$130.8	22.2%	1.3%
Corporate income tax	\$61.2	\$56.9	9.6%	-7.1%
Unemployment insurance	\$35.8	\$32.5	5.5%	-9.2%
Business and corporate license	\$34.3	\$36.8	6.2%	7.1%
Public utility taxes	\$23.7	\$26.6	4.5%	12.1%
Individual income tax on business income	\$25.8	\$27.2	4.6%	5.4%
Excise taxes	\$27.7	\$26.0	4.4%	-6.0%
Insurance premiums taxes	\$15.5	\$15.6	2.6%	0.7%
Other business taxes	\$22.0	\$28.4	4.8%	28.8%
Total business taxes	\$574.6	\$590.0	100.0%	2.7%

Sales Tax as Percentage of State Government Own-Source Revenue, 2007



Source: U.S. Census Bureau.

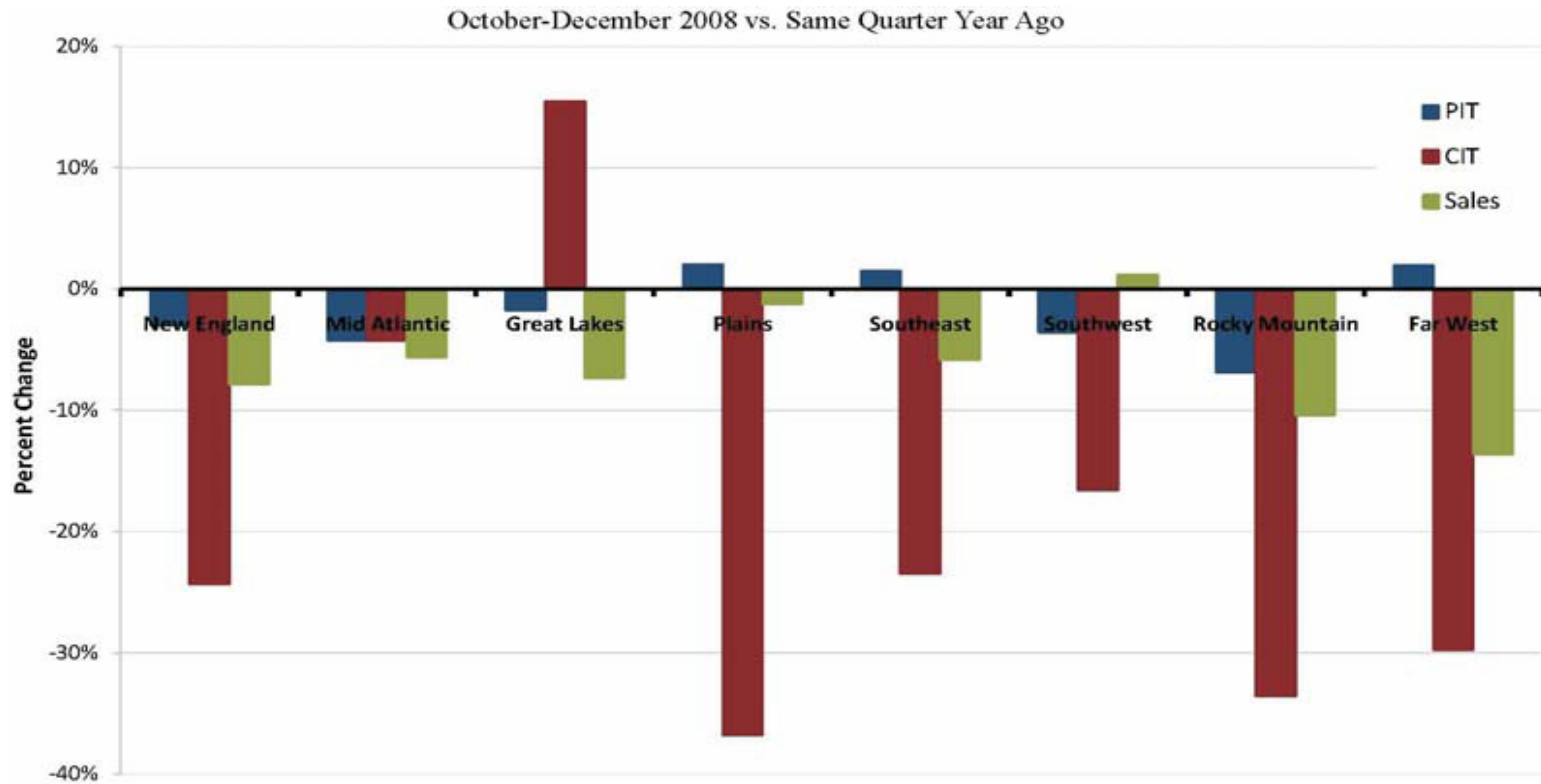
Year-Over-Year Percent Real Change in Major Taxes
Four-Quarter Average of Percent Change



Sources: U.S. Census Bureau (tax revenue) and Bureau of Economic Analysis (GDP price index).

Notes: (1) 4-quarter average of percent change in real tax revenue; (2) No adjustments for legislative changes.

State Tax Revenue Growth Adjusted for Legislative Changes



Sources: Rockefeller Institute Analysis of (1) data from U.S. Bureau of the Census (tax revenue, most states), (2) data from National Association of State Budget Officers (legislative enactments, most states), and (3) data from selected individual states (supplemental data on tax revenue and legislative enactments).

The total shortfall for fiscal year 2010 — including gaps that have been addressed through budget cuts and other measures, and newly emergent gaps — now totals \$166 billion across 48 states. Total gaps through 2011 will exceed \$350 billion

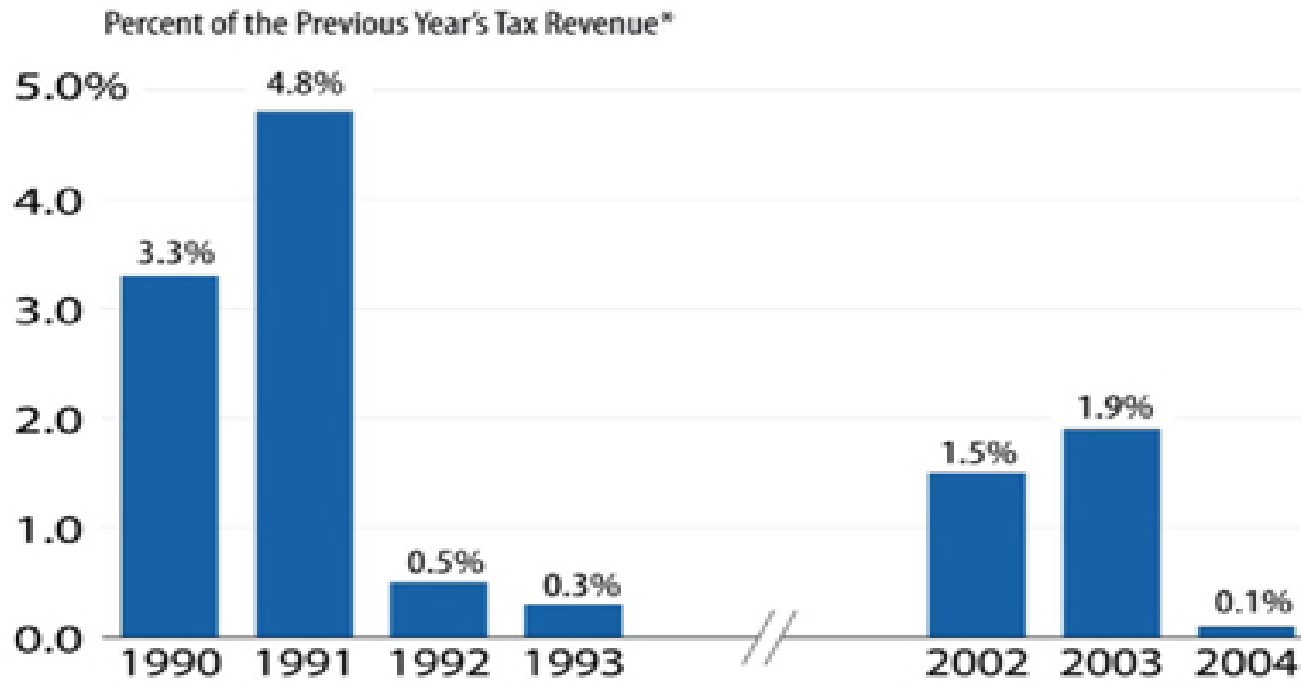
- At least 39 states have made cuts that harm vulnerable residents to help close budget gaps.
- The federal economic recovery act is providing needed relief, reducing the size and extent of cuts and closing roughly 40 percent of state budget shortfalls.
- Twenty five states have raised taxes this year and another 12 are considering doing so, as states increasingly realize that the budget holes are too big to be filled by cuts alone.



"What the ... They raised our property tax assessment 21 percent because we added a birdbath!"

FIGURE 2

Tax Increases During the Last Two Recessions: 1990-1993, 2002-2004.



* Net tax changes. Data for 2002 include tax increases enacted in late 2001.

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