



General Assembly

February Session, 2002

Raised Bill No. 5550

LCO No. 1832

Referred to Committee on Finance, Revenue and Bonding

Introduced by:
(FIN)

AN ACT PROTECTING THE STATE'S CORPORATION BUSINESS TAX REVENUE.

Be it enacted by the Senate and House of Representatives in General Assembly convened:

1 Section 1. Section 12-226a of the general statutes is repealed and the
2 following is substituted in lieu thereof (*Effective upon passage and*
3 *applicable to income years commencing on or after January 1, 2002*):

4 (a) If it appears to the Commissioner of Revenue Services that any
5 agreement, understanding or arrangement exists between the taxpayer
6 and any other corporation or any person or firm, whereby the activity,
7 business, income or capital of the taxpayer within the state is
8 improperly or inaccurately reflected, the Commissioner of Revenue
9 Services is authorized and empowered, in his or her discretion,
10 provided such discretion is not arbitrarily, capriciously or
11 unreasonably exercised, and in such manner as he or she may
12 determine, to adjust items of income, deductions and capital, and to
13 eliminate assets in computing any apportionment percentage under
14 this chapter, provided any income directly traceable thereto shall also
15 be excluded from entire net income, so as equitably to determine the
16 tax. Where [(a)] (1) any taxpayer conducts its activity or business under

17 any agreement, arrangement or understanding in such manner as
18 either directly or indirectly to benefit its members or stockholders, or
19 any of them, or any person or persons directly or indirectly interested
20 in such activity or business, by entering into any transaction at more or
21 less than a fair price which, but for such agreement, arrangement or
22 understanding, might have been paid or received therefor, or [(b)] (2)
23 any taxpayer, a substantial portion of whose capital stock is owned
24 either directly or indirectly by another corporation, enters into any
25 transaction with such other corporation on such terms as to create an
26 improper loss or to reflect inaccurate net income, the Commissioner of
27 Revenue Services may include in the entire net income of the taxpayer
28 the fair profits, which, but for such agreement, arrangement or
29 understanding, the taxpayer might have derived from such
30 transaction. Not later than January 1, 1995, the commissioner shall
31 adopt regulations, in accordance with the provisions of chapter 54,
32 setting forth standards for taking the actions authorized under this
33 section.

34 (b) (1) There shall be a rebuttable presumption that a related loan
35 creates an improper loss, or will reflect inaccurate net income, subject
36 to adjustment under subsection (a) of this section if a loan occurred
37 within either a twelve-month period prior to the capital contributions,
38 dividends or other distributions, or a twenty-four-month period after
39 the capital contributions, dividends or other distributions, and the loan
40 is equivalent to twenty per cent or more of the aggregate value of the
41 capital contributions, dividends or other distributions made directly or
42 indirectly by the related borrower to the related lender. The taxpayer
43 may rebut the presumption set forth in this subsection by establishing
44 by clear and convincing evidence that (A) the related lender had a
45 valid business purpose and economic substance, (B) the related
46 transaction had a valid business purpose, and (C) the related
47 transaction had as its principal purpose substantial economic benefits
48 and not the avoidance of tax under chapter 208. As part of any
49 adjustment under this subsection, the commissioner shall identify, in
50 writing, the transaction giving rise to the presumption.

51 (2) As used in this subsection:

52 (A) "Interest expense" means amounts directly or indirectly allowed
 53 as deductions under Section 163 of the Internal Revenue Code for
 54 purposes of determining taxable income;

55 (B) "Related member" and "related entity" shall have the meaning
 56 set forth in section 12-218c;

57 (C) "Related loan" means any loan or advance made by a related
 58 lender to a related borrower;

59 (D) "Related lender" means any related member that makes a loan
 60 or otherwise advances funds to a related borrower for which an
 61 interest expense is claimed; and

62 (E) "Related borrower" means any related member that pays,
 63 accrues or incurs any interest expense to a related lender as a result of
 64 the direct or indirect borrowing of funds.

65 (3) Nothing in this subsection shall be construed to limit or negate
 66 the commissioner's authority to make adjustments under this section
 67 with respect to any loans whether or not described in this subsection.

68 Sec. 2. (*Effective upon passage*) The General Assembly hereby affirms
 69 that the facts, circumstances and transactions at issue in Carpenter
 70 Technology Corp. v. Commissioner, 256 Conn. 455 (2001), amply
 71 satisfy the improper or inaccurate reflection of net income standard
 72 adopted by the General Assembly in the enactment of section 12-226a
 73 of the general statutes and were properly the subject of an adjustment
 74 by the Commissioner of Revenue Services pursuant to said section 12-
 75 226a.

This act shall take effect as follows:	
Section 1	<i>upon passage and applicable to income years commencing on or after January 1, 2002</i>
Sec. 2	<i>upon passage</i>

Statement of Purpose:

To preclude a revenue loss from the decision in Carpenter Technology Corp. v. Commissioner, 256 Conn. 455 (2001).

[Proposed deletions are enclosed in brackets. Proposed additions are indicated by underline, except that when the entire text of a bill or resolution or a section of a bill or resolution is new, it is not underlined.]