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INSIGHT: Connecticut Issues Guidance on Tax Implications of Pandemic Relief



BY MARC T. FINER

On July 6, 2020, the Connecticut Department of Revenue Services (DRS) issued two pieces of official guidance regarding the Connecticut tax implications of the CARES Act tax relief provisions. Highlights of this guidance include:

Office of the Commissioner Guidance (OCG-10)

■ **Economic Stimulus Payments:** The federal economic stimulus payments of up to \$1,200 (\$2,400 if married filing jointly) are not subject to Connecticut personal income tax because the payments are not subject to federal personal income tax and Connecticut does not require that these payments be added back when computing Connecticut adjusted gross income (AGI).

■ **Qualified Retirement Account Distributions.** The Connecticut taxation of Coronavirus-related distributions from qualified retirement accounts for a particular year will be dictated by whether the distributions are included or excluded from the individual participant's federal AGI for a particular year. However, these distributions will be subject to Connecticut income tax withholding at 6.99% unless the recipient requests that no or a lesser amount of Connecticut income tax be withheld.

■ **Paycheck Protection Program Loans:** Loans that are forgiven under the Paycheck Protection Program are not subject to Connecticut personal or corporation business income tax because the payments are excluded from federal AGI and Connecticut does not require these payments be added back when computing Connecticut AGI.

■ **Net Operating Loss 5-Year Carryback:**

■ The 5-year net operating loss (NOL) carryback provision of the CARES Act has no impact on the calculation of the Connecticut corporation business tax because Connecticut has its own specific rules for corporate NOLs.

■ Connecticut conforms to the federal NOL carryforward and carryback rules for Connecticut personal income tax purposes. However, the DRS guidance points out that the carryback of federal NOLs that affect an individual's income tax liability are applied consistent with the Connecticut Tax Court's decision in *Adams v. Sullivan*. This means that NOLs can only be used to offset an individual's Connecticut AGI for a prior year to the extent that the NOL was used by the taxpayer to offset federal taxable income for that year.

■ **Excess Business Loss Limitations:** The CARES Act provides that for the years 2018-2020, losses related to a trade or business of a non-corporate taxpayer are not limited to \$250,000 (\$500,000 for joint filers) in excess of trade or business income and gain. Because there is no Connecticut statutory modification specific to excess business loss limitations for purposes of calculating Connecticut AGI, the extent to which the excess business loss limitation increases or decreases federal AGI in a particular year will dictate the Connecticut tax treatment of the limitation for that year.

Office of the Commissioner Guidance (OCG-11)

■ **Qualified Improvement Property:** The CARES Act changed the depreciable life of qualified improvement property (QIP) from 39 years to 15 years under the general depreciation system and 20 years under the alter-

native depreciation system. This change allows taxpayers to apply 100% bonus depreciation to eligible QIP placed in service after Dec. 31, 2017. Taxpayer that wish to claim the additional bonus depreciation in one or more of the years 2018-2020 have the choice of either (i) filing an amended federal return for the placed in service year of the QIP on or before Oct. 15, 2021, or (ii) filing IRS Form 3115 (Application for Change in Accounting Method) with a timely filed federal income tax return for the year of the change.

Corporation Business Tax

The DRS guidance states that Connecticut tax law conforms to the federal treatment of QIP as 15- and 20-year property for corporation business tax purposes but does not conform to the ability to claim bonus depreciation on QIP. The DRS guidance therefore, instructs corporations that file an amended federal return to reflect the QIP depreciation change to file a corresponding amended corporation business tax, except that the depreciation deduction for Connecticut purposes should be calculated without regard to bonus depreciation. Taxpayers that claim the additional QIP depreciation on IRS Form 3115 should report the adjustment on the corresponding corporation business tax return calculated without regard to bonus depreciation.

Individual Income Tax and Pass-Through Entity Tax

For Connecticut personal income tax and pass-through entity taxable years beginning on or after January 1, 2017, Connecticut does not conform to the federal treatment of bonus depreciation with respect to property placed in service after Sept. 27, 2017 and requires an addition to federal taxable income for any bonus de-

preciation taken at the federal level. However, for bonus depreciation that has been added to federal taxable income, a Connecticut subtraction modification is allowed for 25% of added bonus depreciation which may be taken each year for four succeeding years.

Consistent with Connecticut tax law, the DRS guidance states that a taxpayer that files an amended federal tax return to reflect the QIP depreciation change must file a corresponding Connecticut amended return but must add back any bonus depreciation deducted on the amended federal return. The taxpayer may deduct 25% of the disallowed deduction over each of the four succeeding tax years. Similarly, the guidance states that if the taxpayer files IRS Form 3115, the amount of the adjustment that relates to bonus depreciation must be added back to calculate Connecticut taxable income. The taxpayer may claim a subtraction equal to 25% of the amount added back in each of the four years following the taxable year for which the add back was reported.

The CARES Act provides significant current Federal tax relief for many individuals and businesses financially impacted by the Coronavirus. The guidance issued by the DRS provides extremely helpful assistance to taxpayers with questions related to the impact of the CARES Act on Connecticut tax law.

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Author Information Marc T. Finer is a tax partner at Murtha Cullina LLP in Hartford, Conn. He can be reached at 860-240-6096 or mfiner@murthalaw.com. More information on the Connecticut tax implications of the CARES Act tax relief provisions is available [here](#).