Sec. 12-715(c)-1. Connecticut income tax avoidance or evasion

(a) If a partnership agreement provides for a special allocation among the partners of any item of partnership income, gain, loss or deduction, federal income tax law requires that such a provision be disregarded for federal income tax purposes, where its principal purpose is the avoidance or evasion of federal income tax. In such a case, each partner's distributive share of such item is determined by such partner's distributive share for federal income tax purposes of the taxable income or loss of the partnership as described in section 702(a)(8) of the Internal Revenue Code. This treatment and distribution of the item is reflected in each partner's federal adjusted gross income and, therefore, in each partner's Connecticut adjusted gross income, even though in a particular case no Connecticut income tax avoidance or evasion may be involved.

(b) In certain cases, however, a provision for special allocation does not have as its principal purpose the avoidance or evasion of federal income tax, but has as its principal purpose the avoidance or evasion of Connecticut income tax. In such an instance, any such provision shall be disregarded and each partner's share of the pertinent item of partnership income, gain, loss or deduction shall also be determined by the partner's distributive share for federal income tax purposes of the taxable income or loss of the partnership as described in section 702(a)(8) of the Internal Revenue Code.

(c) Whether the principal purpose of a special allocation of an item is the avoidance or evasion of Connecticut income tax depends on the surrounding facts and circumstances. Among the relevant facts to be considered are the following: whether the partnership or partner individually has a business purpose for the allocation; whether the allocation has substantial economic effect, as the term is used in section 704(b)(2) of the Internal Revenue Code (i.e., whether the allocation may actually affect the dollar amount of the partners' shares of the total partnership income or loss independently of Connecticut income tax consequences); whether related items of income, gain, loss or deduction from the same source are subject to the same allocation; whether the allocation was made without recognition of normal business factors and only after the amount of the specially allocated item could reasonably be estimated; the duration of the allocation; and the overall Connecticut income tax consequences of the allocation.

Example: A and B are equal partners. The partnership agreement, however, allocates to A, who has a higher effective rate of Connecticut income tax than B, all interest income on bonds of the State of Connecticut held by the partnership and allocates to B all interest income on bonds of other states. The partnership agreement also provides that any difference in the amounts of such interest income allocated to each partner is to be equalized out of other partnership income. Because the purpose and effect of this allocation is solely to reduce the Connecticut income tax of A without actually affecting the distributive shares of A and B in partnership income, such allocation is not recognized. Accordingly, in determining their respective Connecticut adjusted gross incomes, A and B each shall add to federal adjusted gross income one-half of the interest income from bonds of other states under § 12-701(a)(20)-2 of Part I.

(d) While this section pertains to Section 12-715(c) of the general statutes, for purposes of supplementary interpretation, as the phrase is used in Section 12-2 of the general statutes, the adoption of this section is authorized by Section 12-740(a) of the general statutes.

(Effective November 18, 1994)