



MULTISTATE INCOME/FRANCHISE

Connecticut extends corporation business tax surcharge and makes pass-through entity tax optional Tax Alert

Overview

On June 12, 2023, Connecticut [House Bill 6941](#) (H.B. 6941) was enacted into law. This bill amends certain corporate income tax provisions, including extending the 10% surcharge for three additional years to taxable years beginning prior to January 1, 2026. The bill also revises Connecticut's pass-through entity tax ("PTET") rules, including making the PTET elective (instead of mandatory) for taxable years beginning in 2024.

This Tax Alert summarizes some of the provisions of H.B. 6941.

Corporation business tax changes

- Effective from enactment and applicable to taxable years beginning on or after January 1, 2023, H.B. 6941 extends the 10% corporation business tax surcharge for three additional years to the 2023, 2024, and 2025 taxable years.
- For taxable years beginning on or after July 1, 2025, certain Connecticut headquartered corporations providing telecommunications services and owning at least 80% of a limited liability company ("LLC") may claim a credit for 5% of the amount paid or incurred by the LLC for any new fixed capital investment during the taxable year that such fixed capital is acquired. To be eligible for the credit, the LLC making the investment must be treated as a partnership or disregarded entity for federal income tax purposes.
- H.B. 6941 also makes various other amendments to Connecticut's corporation business tax credits, including:
 - For taxable years beginning on or after January 1, 2024, the legislation increases the human capital investment tax credit

from 5% to 10% (for most eligible investments) and from 5% to 25% (for eligible childcare related expenditures).

- The legislation increases the percentage a corporation may use the 25% human capital investment tax credit for eligible childcare related expenditures to reduce its corporation business tax liability from 50.01% to 70%.
- Effective January 1, 2025, and applicable to taxable years beginning on or after January 1, 2027, the legislation creates an exemption from the corporation business tax surcharge for companies that offer a qualifying “share plan” (i.e., stock-sharing arrangement) to eligible employees.

Pass-through entity tax changes

- H.B. 6941 changes the PTET regime from mandatory to an optional elective entity level tax for taxable years beginning on or after January 1, 2024.
- For taxable years beginning on or after January 1, 2024, pass-through entities, including partnerships and S corporations, may annually elect to be subject to tax at the entity level by submitting written notice of such election no later than the due date for filing the return, including any extension granted.
- The elective PTET is imposed on the sum of the resident portion of unsourced income plus modified Connecticut source income. The tax base is consistent with the alternative tax base, which pass-through entities can elect to use to calculate the tax due for taxable years beginning prior to January 1, 2024, but the legislation changes the definition of unsourced income as described below.
- H.B. 6941 changes the definition of unsourced income to include the portion of the pass-through entity’s total income, excluding itemized deductions and adjusted for modifications under Conn. Gen. Stat. section 12-701, that is directly allocated to resident individual owners, which is not sourced to any state in which the pass-through entity has nexus, and actually imposes tax on the electing pass-through entity or its resident individual owners.
- The definition of modified Connecticut source income is consistent with the laws in effect for tax years beginning prior to January 1, 2024, and includes the portion of the pass-through entity’s total income (excluding itemized deductions and adjusted for modifications under Conn. Gen. Stat. section 12-701) to the extent connected with sources within the state that are directly or indirectly allocated to owners subject to tax under chapter 229 (i.e., individual, trust, or estates).
- The tax rate for the PTET remains unchanged and is equal to 6.99%.
- Pass-through entity income of corporate owners is not included in the tax base. As such, H.B. 6941 eliminates the credit previously available to corporate owners for their share of PTET paid. Individual, estate, and trust owners may still claim a credit equal to their direct and indirect pro rata share of the tax paid by the pass-through entity, multiplied by 87.5%.
- H.B. 6941 also eliminates the option for pass-through entities to file a combined return with one or more commonly owned pass-through entities subject to the PTET.

Composite return

- For taxable years beginning on or after January 1, 2024, H.B. 6941 reinstates the requirement for pass-through entities to file a composite income tax return and pay the tax on behalf of any nonresident owner whose only source of Connecticut income is their share of the pass-through entity's income. This requirement is similar to those applicable to taxable years beginning before January 1, 2018, and the effective date of the mandatory PTET.
- As under the pre-2018 law, H.B. 6941 requires pass-through entities to make income tax payments annually, by the regular income tax due date on behalf of non-resident owners whose share of the pass-through entity's Connecticut source income is at least \$1,000 at a rate of 6.99%. The payments will generally constitute the owners' tax payment for the year.
- The pass-through entity is required to report those payments to each owner upon whose behalf the payments were made by the 15th day of the third month. This reporting requirement is one month earlier than what was required under the pre-2018 law.
- The composite tax due shall be reduced by the nonresident owner's direct and indirect PTE tax credit that was properly reported by the pass-through entity. The payment with respect to any nonresident owner may not be less than zero.

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Have a question relating to this or any other pass-through entity tax regime? Reach out to one of our national multistate pass-through entity tax specialists.

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