

NO. CV 04 0525585S : SUPERIOR COURT
ROBERT BLASKO, MARY ELIZABETH
BLASKO : TAX SESSION
v. : JUDICIAL DISTRICT OF
: NEW BRITAIN
COMMISSIONER
OF REVENUE SERVICES : MARCH 10, 2005

MEMORANDUM OF DECISION

The plaintiffs, Robert Blasko and Mary Elizabeth Blasko (collectively, the Blaskos), husband and wife, filed this appeal pursuant to General Statutes § 12-730 contesting an additional income tax assessment levied by the commissioner of revenue services (commissioner) for the taxable year of 1998.

The Blaskos take issue with the commissioner's assessment because they believe that their claim for a Connecticut alternative minimum tax credit on their 1998 return was incorrectly disallowed.

The sole issue presented in this appeal is whether the Blaskos were in fact eligible to claim a Connecticut alternative minimum tax credit on their 1998 Connecticut income tax return.

In February 1997, Robert Blasko (Blasko) retired as a managing director of J.P. Morgan Chase & Company (J.P. Morgan). During Blasko's period of employment with

J.P Morgan he received incentive stock options to purchase 9,474 shares of J.P. Morgan common stock. Upon his retirement, Blasko exercised the stock options on February 26, 1997, which netted him stock valued at \$450,939. (See Defendant's Exhibit 2; Plaintiff's Brief, dated August 26, 2004, p. 3.) This amount was treated as tax deferred income pursuant to section 422 of the Internal Revenue Code and, therefore, it was not recognized as income for regular federal income tax purposes. See 26 U.S.C. § 422. The gain was recognized as ordinary income in 1998 when Blasko sold the stock.

In 1997, the Blaskos filed a joint federal individual income tax return form 1040 reporting a taxable income of \$325,688, excluding the deferred income that came from the exercise of the stock options, resulting in a tax of \$103,283. (See Defendant's Exhibit 2.) The Blaskos also filed a 1997 federal alternative minimum tax form 6251 in order to calculate their alternative minimum tax liability for that year, which totaled \$115,219. This amount was reported on line 48 of their 1997 federal form 1040, along with an employment tax of \$396 reported on line 47, so that the total federal tax paid by the Blaskos for 1997 was \$218,898. (See Defendant's Exhibit 2.)¹

Conceptually, when a taxpayer has deferred income, that income, although not taxable as ordinary income, is subject to tax under the alternative minimum tax statute.

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The Blaskos reported on their 1997 federal form 6251 (Part II) a total income of \$792,863, which is a combination of their regular income of \$325,688 and the deferred gain from the exercise of the stock option of \$450,939, plus other adjustments, resulting in the tentative minimum tax of \$115,219. (See Defendant's Exhibit 2.) The tentative minimum tax of \$115,219, added to the tax on ordinary income of \$103,283 and the employment tax of \$396, equaled the total tax of \$218,898 paid by the Blaskos for 1997.

For tax purposes, when the value of the stock, as exercised in 1997, was added to the plaintiffs' ordinary income, it was subject to the alternative minimum tax because this amount exceeded the amount of their ordinary income.²

The alternative minimum tax, on the federal level, originates from section 55 of the Internal Revenue Code and in effect creates a tax independent of the regular income tax when the alternative tax exceeds the regular tax liability. K. Bucklin, "The Alternative Minimum Tax for Individuals: Present Problems and Future Possibilities," 63 Wash. L. Review. 103 (1988). The objective of the alternative minimum tax is to prevent taxpayers from avoiding the payment of income taxes by using exclusions, deductions and credits. Urbanek v. United States, 866 F. Sup. 1414, 1419 (S.D. Fla. 1994), aff'd, 71 F.3d 855 (11th Cir. 1996).

On the state level, the alternative minimum tax originates from General Statutes § 12-700a (a), Alternative Minimum Tax, which recites: "Every resident individual, as defined in section 12-701, subject to and required to pay the federal alternative minimum tax under Section 55 of the Internal Revenue Code shall pay, in addition to the tax imposed under section 12-700, the net Connecticut minimum tax. The tax shall be the difference computed by subtracting the tax imposed under subsection (a) of section 12-700 from the Connecticut minimum tax, as provided in subdivision (26) of subsection (a)

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Internal Revenue Code, 26 U.S.C. § 55 provides: "(a) General rule.- There is hereby imposed (in addition to any other tax imposed by this subtitle) a tax equal to the excess (if any) of-

“(1) the tentative minimum tax for the taxable year, over

“(2) the regular tax for the taxable year.”

of section 12-701." Connecticut alternative minimum tax liability is based upon two preconditions: (1) the taxpayer was a Connecticut resident and (2) the taxpayer had a federal alternative minimum tax liability. (See Defendant's Exhibit 12, Informational Publication 94 (2.4) issued January 29, 1998, by the Connecticut Department of Revenue Services.)

Following the payment of the Connecticut alternative minimum tax, a "minimum tax credit is available and calculated in the year that the taxpayer pays regular income tax. It is limited to the amount by which the regular income tax exceeds the minimum tax for the taxable year (the excess is carried forward)." (Defendant's Exhibit 18, May 1, 1997 memorandum from Stacey K. Pavano, tax attorney, to Susan B. Sherman, legislative program manager, regarding HB 6891- Summary of the Alternative Minimum Tax Changes.) Attorney Pavano notes in her memorandum that "[a] taxpayer who pays the Connecticut minimum tax is eligible for a credit in succeeding years in which the taxpayer is subject to the regular income tax. The credit is limited to the minimum tax paid on *deferral items* only. In addition, the credit is further limited to the amount by which the regular income tax exceeds the minimum tax in a taxable year." (Emphasis in original.) Id.

When Blasko exercised his option to purchase the J.P. Morgan stock in 1997, pursuant to the stock option plan, the difference between the exercise price and the fair market value of the stock at the time the stock option was exercised was included in the Blaskos' alternative taxable income for 1997. This amount, however, was excluded from

the Blaskos' regular taxable income until the stock was sold in 1998. As an example, if a taxpayer was given a stock option for 10,000 shares of stock with an option price of \$50 per share, and he exercised this option, he would pay \$50 per share, or \$500,000, for the 10,000 shares. If, at the time the taxpayer exercised the option by paying \$500,000 for the stock, the stock had a then market value of \$100 per share, the taxpayer would own an asset of 10,000 shares of stock worth \$1,000,000. The federal minimum tax requires the taxpayer to declare and pay a tax on the \$500,000 paper profit made at the time of the exercise of the stock option as deferred income. When the taxpayer subsequently sells the 10,000 shares of stock for \$100 per share in the following year for \$1,000,000, he or she would pay a tax on the \$500,000 profit realized at that time as ordinary income, even though he or she would have already paid a tax on the \$500,000 profit in the prior year under the federal minimum tax concept. For this reason, the taxpayer is allowed to take a tax credit for the payment of the minimum tax and apply this credit to the tax generated from the sale of the stock that had been previously treated as deferred income. Otherwise, the taxpayer will have paid a tax twice: once when the stock was considered deferred income, and once when the sale of the stock becomes ordinary income.³

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The commissioner of the department of revenue services, Gene Gavin, at a legislative finance hearing on March 24, 1997, in response to Senator Rich Nickerson's concern about tax credits for the alternative minimum tax, replied: "Our proposal here will eliminate any question of a possible double tax on income from AMT [alternative minimum tax] and tax on the regular tax." (Defendant's Exhibit 11, Finance Committee Hearing Transcript for March 24, 1997.)

In 1998, the Blaskos, having sold the J.P. Morgan stock, filed a joint federal individual income tax return form 1040 reporting an adjusted gross ordinary income of \$5,355,120 and a tax of \$1,992,790. (See Defendant's Exhibit 1, Form 1040, lines 33 and 40.) The Blaskos further filed a 1998 federal alternative minimum tax form 6251 and reported an alternative minimum taxable income of \$5,351,997 with a tentative minimum tax of \$1,495,059. (See Defendant's Exhibit 1, Form 6251, lines 21 and 26.) Since the Blaskos' 1998 ordinary income tax of \$1,992,790 (line 27 of federal form 6251) exceeded the tentative minimum tax of \$1,495,059 (as reported on line 26), no alternative minimum tax was due the federal government for the taxable year of 1998. (See Defendant's Exhibit 1, Form 6251, line 28.) Similarly, on the state level, no minimum tax was due the state since the Connecticut alternative minimum tax is prefaced on there being a federal alternative minimum tax. See General Statutes § 12-700a ("Every resident individual, as defined in section 12-701, subject to and required to pay the federal alternative minimum tax under Section 55 of the Internal Revenue Code shall pay, in addition to the tax imposed under section 12-700, the net Connecticut minimum tax."). See also Plaintiffs' Exhibit A; Defendant's Exhibit 12 (Informational Publication 94 (2.4), explaining that the two requirements for the Connecticut minimum tax are (1) residency in Connecticut and (2) a liability for the payment of a federal alternative minimum tax).

The Blaskos prepared and filed a 1997 federal form 8801, Credit For Prior Year Minimum Tax, with their filing of the 1998 form 1040, showing a minimum tax credit of

\$115,219, to be reported as a credit on their 1998 federal tax return. (See Defendant's Exhibit 1.) The \$115,219 credit was then reported on line 48 of the Blaskos' 1998 federal form 1040 and applied to reduce their total tax for 1998 from \$1,992,790 to \$1,877,571. (See Defendant's Exhibit 1, Form 1040, line 49.)

The Blaskos' central complaint is that because of the sale of the J.P. Morgan stock, they were allowed to use a \$115,219 tax credit from the payment of the 1997 alternative minimum tax on their 1998 federal form 1040 tax return, and yet, on the state level, they were precluded from taking the 1997 state alternative minimum tax credit of \$25,471 on their 1998 income taxes.⁴ (See Defendant's Exhibit 3, Form 1040, Line 13.)

The Blaskos had assumed that if they were entitled to use the 1997 credit of \$115,219 against their federal income earned in 1998, Connecticut tax law would also permit a similar treatment as to their 1998 state taxable income. In order for the Blaskos to obtain the 1997 credit for the alternative minimum tax, they were required by Connecticut form 8801 (CT-8801) (Credit for Prior Year's Connecticut Minimum Tax for

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It is undisputed that the Blaskos paid a Connecticut alternative minimum tax credit of \$25,471 in 1997. (See Defendant's Post-Trial Memorandum of Law, dated November 12, 2004, p. 19; Defendant's Exhibit 4, Form 1040, line 9.) There is, however, a discrepancy as to the amount of the Blaskos' Connecticut alternative minimum tax credit. It should be noted that the Blaskos originally claimed a credit of \$25,471, the full amount of the tax paid. (See Defendant's Exhibit 3, Form 1040, line 13.) The Blaskos then filed a revised 1998 Connecticut form 8801 claiming a credit of \$22,294, \$14,527 of which they believed they were eligible to claim in 1998 with \$7,767 being carried forward. (See Defendant's Exhibit 10.) The commissioner, on the other hand, claims that the Blaskos' credit equals \$22,908, all of which must be carried forward. (See Defendant's Exhibit 6; Defendant's Post-Trial Memorandum of Law, dated November 12, 2004, n. 21.)

Individuals, Trust and Estates) to fill out a 1998 Connecticut form 6251 (CT-6251)⁵ as well as the 1998 form CT-8801. Line 8 of form CT-8801 contained the 1998 Connecticut individual income tax, minus allowable credits, of \$41,759.28.⁶ (Defendant's Exhibit 6.) Line 9 of form CT-8801 contained the 1998 Connecticut alternative minimum tax, minus allowable credits, of \$270,812. (Defendant's Exhibit 6.) The 1998 form CT-6251 required the Blaskos to deduct their Connecticut income tax of \$243,579.11 from the Connecticut minimum tax of \$270,812, to arrive at the net Connecticut minimum tax of \$27,232.89. (Defendant's Exhibit 5, lines 22-24.) Line 10 of form CT-8801 required the taxpayer to subtract line 9 from line 8, which in this case, resulted in 0. (Defendant's Exhibit 6.) The net result of this computation was that the Blaskos could not use the alternative minimum tax credit created in 1997 to reduce their income taxes due the state

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As previously noted, since the Blaskos had no federal minimum tax obligation in 1998, they were not required to complete and file Connecticut form 6251. However, in order to complete and file Connecticut form 8801, claiming a tax credit from 1997, this form required them to complete the 1998 Connecticut form 6251. (See Defendant's Exhibit 13, Form CT-8801, instructions for line 9: "To claim a credit for prior year's alternative minimum tax, complete Form CT-6251 or Form CT-1041, Schedule I, even if you do not have a federal alternative minimum tax and are not required to file the Connecticut Form CT-6251 or Form CT-1041, Schedule I.")

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There are four CT-8801 forms in evidence. Defendant's exhibit 6 is a reconstructed form prepared by the defendant; defendant's exhibit 10 is a revised form prepared by the plaintiffs; defendant's exhibit 13 is a blank form with instructions attached; and there is a form CT-8801 attached to exhibit 3, the plaintiffs' 1998 state income tax return.

for 1998.⁷ On the Blaskos' 1998 Connecticut form 1040, they show an adjusted gross income of \$5,353,636 and a tax due of \$240,689. (Defendant's Exhibit 3.) On this same Connecticut form 1040, the Blaskos took an adjusted net Connecticut minimum tax credit, from the attached form CT-8801, of \$25,471.

Contrary to the state tax treatment, on the federal level, because the Blaskos' regular tax liability was greater than their tentative minimum tax, they were allowed to deduct their minimum tax credit of \$115,219 from their 1998 federal income tax liability of \$1,992,790. (See Defendant's Exhibit 1, Form 1040, lines 40 and 48) These computations show the difference in the use of the minimum tax credit on the federal level and the state level. On the federal level, the Blaskos were able to apply their minimum tax credit earned in 1997 to their federal taxes in 1998, whereas on the state level they could not apply their minimum tax credit earned in 1997 since their 1998 Connecticut minimum tax of \$270,812, as computed by the commissioner, exceeded their 1998 ordinary income tax of \$243,579.11. (See Defendant's Exhibit 5, line 23.)

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Defendant's exhibit 3, a photocopy of the Blaskos' 1998 Connecticut 1040 tax return shows on line 13 that the Blaskos took a \$25,471 adjusted net Connecticut minimum tax credit, which was obtained from their attached form CT-8801, line 11. However, the commissioner's audit unit prepared a reconstruction of the Blaskos' 1998 form CT-6251 and the Blaskos' 1998 form CT-8801. Line 11 of form CT-8801 indicates that no 1998 Connecticut minimum tax credit is available to the Blaskos. (See Defendant's Exhibit 6.) The primary reason for this discrepancy is that the commissioner, in preparing form CT-6251, showed on line 20 a 1998 Connecticut minimum tax of \$270,812, whereas the Blaskos, not having prepared a form CT-6251, left line 9 of their form CT-8801 blank. (Compare Defendant's Exhibit 5 with Defendant's Exhibit 3.)

The Blaskos' primary argument is with the language of General Statutes § 12-700a (d) (2), which provides as follows: "The credit allowable for a taxable year under this subsection is limited to the amount, if any, by which (A) (i) the tax imposed under section 12-700, (ii) less the credit, if any, allowed under section 12-704 exceeds (B) (i) the Connecticut minimum tax, determined without regard to whether the individual or the trust or estate is subject to and required to pay for that taxable year the federal alternative minimum tax under Section 55 of the Internal Revenue Code, (ii) less the credit, if any, allowed under subsection (e) of this section." In other words, a tax credit for the previous payment of the Connecticut minimum tax is only allowed when the tax on ordinary income for any subsequent year exceeds the Connecticut minimum tax for that year.

Applying § 12-700a (d) (2) to the Blaskos' case, the commissioner, in reconstructing the 1998 form CT-6251 of the taxpayer, listed on line 17 of that form an adjusted federal tentative minimum tax of \$1,513,044. The commissioner then concluded that taking the lesser of 19 percent of the federal tentative minimum tax or 5 percent⁸ of the adjusted federal alternative minimum taxable income, the Blaskos had a Connecticut minimum tax of \$270,812. Because the Connecticut minimum tax of \$270,812 exceeded the Blaskos' Connecticut regular income tax of \$243,579.11, they were disqualified from using their minimum tax credit derived from the payment of the Connecticut minimum tax in 1997.

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This rate has since been increased to 5.5 percent. See Public Acts, Spec. Sess., June, 2003, No. 03-6, § 72.

The problem the court has with the commissioner's preparation of the Blaskos' reconstructed form CT-6251 (Defendant's Exhibit 5), is that according to Informational Publication 94 (2.4) (Defendant's Exhibit 12), a Connecticut resident must have a "federal alternative minimum tax liability" in order to be subject to the Connecticut alternative minimum tax. Since the Blaskos had no federal alternative minimum tax liability for 1998, they therefore had no minimum tax due the state in 1998. (See Defendant's Exhibit 1, Form 6251, line 28, showing "0" for the federal alternative minimum tax.)

The court notes that the commissioner's determination that the Blaskos' 1998 Connecticut minimum tax was \$270,812, comes from the commissioner's preparation of the reconstructed 1998 form CT-6251. (See Defendant's Exhibit 5.) That form lists, on line 1, the federal alternative minimum taxable income of \$5,351,997. This last figure, in turn, comes from line 21 of the federal 1998 form 6251, which is attached to the Blaskos' 1998 federal form 1040. (Defendant's Exhibit 1.) Clearly, the amount of \$5,351,997 was ordinary income, coming, for the most part, from the sale of the J.P. Morgan stock in 1998 and had no relationship to the Connecticut minimum tax. As previously noted, the Blaskos had no 1998 federal minimum tax liability and, therefore, they were not required to complete the 1998 form CT-6251. However, in order for the Blaskos to claim the 1997 minimum tax credit in 1998, they were required by the 1998 form CT-8801 to fill out, as a preliminary requirement, the 1998 form CT-6251. The confusion caused by this requirement becomes evident because the instructions contained on form CT-6251

require the taxpayer to list a federal minimum tax when in fact no federal minimum tax existed for 1998. The culprit here is the instruction in the 1998 form CT-8801 that states: "Line 9 - 1998 Connecticut alternative minimum tax minus allowable credits. To claim a credit for prior year's alternative minimum tax, complete Form CT-6251 or Form CT-1041, Schedule I, even if you do not have a federal alternative minimum tax and are not required to file the Connecticut Form CT-6251 or Form CT-1041, Schedule I.

"Resident Individuals and Part-year Resident Individuals: Subtract the amount on your 1998 Form CT-6251, Line 25 from the amount on your 1998 Form CT-6251, Line 22, and enter the difference on Line 9."

Line 22 on the reconstructed 1998 form CT-6251 prepared by the commissioner lists the apportioned Connecticut minimum tax of \$270,812. This is a fallacy because the Blaskos had no Connecticut minimum tax to pay in 1998. Yet, defendant's exhibit 5, the reconstructed 1998 form CT-6251, shows a Connecticut alternative minimum tax due of \$27,232.89. (Defendant's Exhibit 5, lines 24 and 26.) The Connecticut minimum tax on line 24 of the reconstructed 1998 form CT-6251 was arrived at by deducting line 23, \$243,579.11 (plaintiffs' Connecticut income tax), from line 22, \$270,812 (plaintiffs' Connecticut minimum tax). In effect, the Blaskos would be paying a tax of \$243,579.11 on their ordinary income in addition to paying a Connecticut minimum tax of \$27,232.89, for a total payment of taxes to the state of Connecticut of \$270,812.

The Connecticut minimum tax of \$270,812 shown on line 20 of the 1998 form CT-6251 constructed by the commissioner was arrived at by the commissioner making a

choice for the Blaskos of the "five percent rate" rather than the "nineteen percent rate." (See Defendant's Exhibit 5.) If the commissioner had chosen the "nineteen percent rate," the Connecticut minimum tax would have been "0" since nineteen percent of zero (there being no federal minimum tax) is zero. Using the nineteen percent rate would mean that the Blaskos tax of \$243,579.11 exceeds the Connecticut minimum tax of zero since the Blaskos had the option to take the lesser of \$270,812 (the five percent rate) or zero (the nineteen percent rate). (See Defendant's Exhibit 5, lines 18, 19 and 20.)

If the purpose of the alternative minimum tax is to tax "*deferral items and exclusion items*" this tax fails in this instance because the Blaskos income in 1998 came from the sale of stock as ordinary income, not deferred income. (Emphasis in original.) (Defendant's Exhibit 18, May 1, 1997 memorandum from Stacey K. Pavano, tax attorney, to Susan B. Sherman, legislative program manager, regarding HB 6891- Summary of the Alternative Minimum Tax Changes.)

Contrary to the Commissioner's position that the federal minimum tax and the state minimum tax come from separate taxing authorities, and therefore cannot be considered jointly in the interpretation of these statutes, the Connecticut minimum tax is in fact based upon a percentage of the federal minimum tax or the federal tentative minimum taxable income. See General Statutes § 12-701 (a) (26); 26 U.S.C. § 55. Simply put, if there is no alternative minimum federal tax, there is no alternative minimum state tax.⁹

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The Blaskos' federal form 6251, attached to their federal form 1040 income tax return, recites on line 6 of part II that a taxable income of \$5,098,956, which results in an alternative

Although this court has previously held that the federal government and the state of Connecticut are separate and distinct taxing powers, and therefore are not inextricably tied together; See Deyo v. Commissioner of Revenue Services, Superior Court, judicial district of New Britain, Docket No. CV 03 0524331 (September 27, 2004, Aronson, J.T.R.) (38 Conn. L. Rptr. 28); in this situation, our legislature has chosen to tie the state's minimum tax to the federal minimum tax. See General Statutes § 12-701 (a) (24) and (29) (defining "Adjusted federal tentative minimum tax" and "Federal alternative minimum taxable income.")

General Statutes § 12-730, Appeals, provides, in pertinent part that "[s]aid court may grant such relief as may be equitable" The exercise of the J.P. Morgan stock in 1997 and the tax incurred on the deferred income was calculated as the difference between the option price and the market value of the stock at the time that the option was exercised. The tax on the Blaskos' sale of this same stock in 1998 was calculated on the difference between the option price as exercised and the market value of the stock at the time of sale in 1998. Obviously, the tax in 1998 based upon the income derived from the sale of the J.P. Morgan stock overlapped the Blaskos' payment of the tax on the deferred income when they exercised the stock option in 1997. Unless the Blaskos obtain a credit for paying a tax on the deferred income in 1997 against the income derived in 1998 from

minimum taxable income of \$5,351,997 as shown on line 21. Part III of form 6251, line 28, shows "0" alternative minimum tax because the ordinary tax of \$1,992,790, as shown on line 27, exceeds the tentative minimum tax of \$1,495,059, as shown on line 26. (See Defendant's Exhibit 1.)

the sale of the J.P. Morgan stock, they will have been taxed twice on the same income. This is essentially what the Blaskos are claiming. The Blaskos also argue that whereas the Connecticut income tax is based on 4.5 percent of Connecticut source income, and the Connecticut minimum tax is based on the lesser of 19 percent of the adjusted federal tentative minimum tax, which includes income sources outside of the state of Connecticut, or 5 percent of the adjusted federal alternative minimum taxable income, also including income sources outside of Connecticut, in his retirement stage of life, he will at no point in the future have his Connecticut tax on ordinary income exceed the Connecticut alternative minimum tax. On this basis, the Blaskos claim that he will never have the opportunity to recoup the credit earned in 1997. (See Plaintiff's Post-Trial Brief, dated November 15, 2004, p. 8.)

The fact that the Blaskos will not, in all likelihood, recoup the credit earned in 1997, is neither fair nor equitable. It is no argument for the Commissioner to say that she is not denying the Blaskos of the use of the tax credit earned in 1997 because, as she claims, the Blaskos can use this tax credit at any time in the future when their ordinary Connecticut income tax exceeds their Connecticut alternative minimum tax. As Blasko points out, the chance of this happening is nil.

In this case, the commissioner has recognized that the Blaskos are entitled to the use of a tax credit from the payment of the 1997 alternative minimum tax so that they will not have overpaid their state income taxes. However, the commissioner, in denying the Blaskos use of the 1997 tax credit, made an election on their behalf, on their 1998 income

tax return, that was adverse to their interest because it resulted in their paying a tax twice on the same income. Such a result is not consistent with the intent of the legislature that individuals not be taxed twice on the same income. Under these circumstances, it is only fair and equitable that this court allow the Blaskos to use the 1997 tax credit of \$25,471 against their taxes in 1998, the year that the stock responsible for the tax on deferred income was sold. See Allen Mfg. Co. v. Administrator, 139 Conn. 402, 409, 94 A.2d 608 (1953).

Accordingly, judgment may enter in favor of the plaintiffs sustaining their appeal.

Arnold W. Aronson
Judge Trial Referee