

# NEW JERSEY ENACTS MAJOR CHANGES TO CORPORATE AND GROSS INCOME TAX

*Hodgson Russ LLP State & Local Tax Alert*  
July 6, 2023

*Updated August 7, 2023*

If you have been following the tax news in New Jersey you have probably heard a lot about significant revisions to the Corporation Business Tax signed by Governor Murphy on July 3, 2023. While not getting nearly the attention as the sunset of the CBT surtax, the most sweeping changes might be several amendments to the Gross Income Tax.

New Jersey quietly amended its partnership apportionment regime as part of Assembly Bill 5323 (A5323). In addition, on June 30, 2023, the Assembly and House passed other significant Gross Income Tax amendments as part of Assembly Bill 4694 (A4694). **Update:** Governor Murphy approved A4694 on July 21, 2023.

## **Amendments Signed into Law as Part of A5323**

**Partnership Sourcing.** A5323 provides that partnerships and sole proprietors are now required to use single sales factor sourcing. This change aligns the rules for partnership income apportionment with those applicable to corporations. The old three-factor sourcing methodology has been discarded and the Division of Taxation is already in the process of amending forms and instructions. For service providers this means sourcing is no longer based on where the work was performed. Instead, service providers apportioning income to New Jersey must use market sourcing, which looks to the location where the benefit of the service is received.

One caveat here is that we expect the Division to issue a technical bulletin and possibly regulations to reconcile some ambiguities in the new statutory provision. While we understand the Division's desire to have single sales factor sourcing apply uniformly to all businesses, the amendment borrows language from N.J.S.A. 54A:5-7 (governing the allocation of income of nonresidents) that might suggest single sales factor sourcing only applies when the partnership's income from New Jersey sources "cannot readily or accurately be ascertained."

This provision is retroactively-effective to January 1, 2023, and necessarily includes estimated tax penalty and interest relief. No penalties or interest will accrue for an underpayment of tax due with respect to any provision that creates additional tax liability, provided that for tax periods "ending on and after July 31, 2023, the additional estimated payments shall be made no later than the second next

## **Attorneys**

Open Weaver Banks  
Brandon Bourg  
Mario Caito  
Katherine Cauley  
Thomas Collura  
Paul Comeau  
William Comiskey  
Ariele Doolittle  
Christopher Doyle  
Catherine Eberl  
Joseph Endres  
Debra Herman  
Daniel Kelly  
Mark Klein  
Joshua Lawrence  
Timothy Noonan  
Elizabeth Pascal  
K. Craig Reilly  
Emma Savino  
Joseph Tantillo  
Andrew Wright

## **Practices & Industries**

State & Local Tax

## NEW JERSEY ENACTS MAJOR CHANGES TO CORPORATE AND GROSS INCOME TAX

estimated payment due following the enactment . . . or the second estimated payment due after January 1, 2024, whichever due date is later.”

**Significant CBT Amendments.** Turning now to the CBT, here are the highlights of the amendments enacted as part of A5323:

1. **Nexus Threshold Established.** Effective for tax years ending on and after July 31, 2023, a corporation is subject to the CBT if it derives receipts in excess of \$100,000 or has more than 200 separate transactions delivered to New Jersey customers. These new economic thresholds do not preclude a corporation from having nexus with New Jersey if it otherwise has sufficient activities or contacts with the state under constitutional principles or existing New Jersey statutes. Corporations protected by P.L. 86-272 are still required to pay the CBT minimum tax if they have nexus with New Jersey.
2. **New CBT Return Due Date.** For tax years ending on and after July 31, 2023, the due date for the New Jersey CBT return has changed to the 15<sup>th</sup> day of the month immediately following the month of the original due date for filing the taxpayer’s federal corporate tax return for the same tax year. In the case of a taxpayer filing on extension, the 15<sup>th</sup> day of the month immediately following the month of the extended due date for filing the taxpayer’s federal corporate tax return is the new due date.
3. **Sunset of CBT Surtax.** New Jersey will no longer have the highest corporate tax rate in the nation! The 2.5% CBT surtax was not extended and will be allowed to sunset for tax years beginning on and after January 1, 2024.
4. **Treaty-Exempt Income.** Consistent with New Jersey case law, the CBT statute now provides that for a corporation that is incorporated or formed in a foreign nation with a comprehensive tax treaty with the U.S., and that is not a member of a New Jersey world-wide group combined return, entire net income shall not include income excluded or exempted from federal taxable income under the terms of the treaty. For a non-U.S. corporation that files a federal tax return and is not a member of a group filing a New Jersey combined return on a world-wide basis, the non-U.S. corporation must calculate its New Jersey income or loss based on its effectively connected income or loss reported for federal income tax purposes, as modified by the CBT Act.
5. **GILTI.** GILTI income will now be considered a dividend, which makes the dividends received deduction available to offset 95% of this income.
6. **Finnigan Apportionment.** For tax years ending on and after July 31, 2023, all types of combined reporting groups are now required to use the “Finnigan” apportionment method and compute the numerator and denominator of the allocation factor of the combined group as one taxpayer, taking into account all unitary receipts of all members of the combined group. Previously, the “Finnigan” method only applied if a group elected to report as an “affiliated group,” instead of as either a water’s edge group or world-wide group.
7. **Change to Water’s Edge Group Definition.** The default water’s edge group definition has been modified to remove the provision that included a member merely because it had New Jersey nexus and income, and now includes “any member, wherever incorporated or formed” that is not otherwise required to be included in the group, if that member has effectively connected income or loss. Any member included under the new provision is included only to the extent of its effectively connected income or loss. This provision applies to tax years ending on and after July 31, 2023.

## NEW JERSEY ENACTS MAJOR CHANGES TO CORPORATE AND GROSS INCOME TAX

8. **New Jersey Statute of Limitations on Assessments.** A5323 amends the New Jersey statute of limitations on assessments in reaction to a 2021 decision of the New Jersey Tax Court (*R.O.P. Aviation Inc. v. New Jersey Div. of Taxation*, No. 001323-2018 (May 27, 2021)). [See our discussion of that case here.](#) That decision rejected the federal rule that allows audit adjustments to NOLs from closed years. With this legislation, adjustments to NOLs from closed years may be made by either the taxpayer or the director on assessments. But the amendment is not open-ended and incorporates a pre-existing ten-year time limit on New Jersey assessments. The amendment applies retroactively to tax years ending on or after July 31, 2022.
9. **Other Amendments.** In addition to the above highlights, other amendments enacted impact research and development credits, New Jersey's treatment of the interest deduction limitation in I.R.C. § 163(j), the New Jersey deduction for net deferred tax liabilities, as well as net operating losses, among others.

### Amendments Signed into Law as Part of A4694

**Update:** On July 21, 2023, Governor Murphy signed into law the following additional tax amendments that were part of A4694. This separate bill makes several changes that are designed to stem the flow of tax revenue from New Jersey to New York.

**New Resident Credit Limit.** Historically, New Jersey has been generous in providing credits to its residents for taxes paid to New York on income also taxed in New Jersey. [See our prior article on this topic here.](#)

The resident credit statute has always provided for a redetermination of the New Jersey tax due "regardless of any otherwise applicable statute of limitations." This meant that New Jersey residents under audit by New York did not have to worry that their New Jersey tax year would close to a refund before completion of the New York audit. A4694 creates a new deadline for claiming a refund as a result of taxes paid to another state. Effective on enactment, taxpayers are permitted to adjust the New Jersey credit within the normal statute of limitations (three years) or within one year after the date the taxpayer "received notification that the other state's income tax was due, whichever of such periods expires later."

The language regarding when the one-year clock starts ticking is unfortunate here because it is ambiguous and subject to many alternative interpretations. The right interpretation from a policy perspective would be one year from when a final determination or judgment of tax due (meaning only after a taxpayer has exhausted all appeal rights in the other state). And a "final determination" rule would be consistent with other statute of limitations starting points (*see, e.g.,* N.J.S.A. 54A:8-7 for reporting changes in federal taxable income). We will have to wait and see if the Division holds the same view.

**Retaliatory Convenience Rule.** A second way that New Jersey loses tax revenue to New York is the result of New York's "convenience rule." Under that rule, the compensation received by employees assigned to an office in New York, but who work outside of New York for their own convenience, is treated as having a New York source as long as the employee works in New York once a year. So New Jersey has enacted its own "retaliatory convenience rule" in A4694 that applies to an individual's income in the following limited circumstances:

1. the individual is a nonresident of New Jersey;

## NEW JERSEY ENACTS MAJOR CHANGES TO CORPORATE AND GROSS INCOME TAX

2. the individual has income from employee compensation from a New Jersey employer;
3. the compensation is for the performance of personal services performed outside of New Jersey that were not required by the employer to be performed outside of New Jersey; and
4. the individual's state of residence (*e.g.* New York) imposes an income or wage tax that requires employee compensation to be sourced to an employer's location if the nonresident renders the personal service from an out-of-state location for the convenience of the nonresident employee and not due to the necessity of the employer.

As the old adage goes – what's good for the goose is good for the gander.

Any employer that might be considered a "New Jersey employer" needs to think about the remote work arrangements it has with employees who are residents of New York (and other states with convenience rules) to determine if a change needs to be made to state withholding. "New Jersey employer" is not defined in the new provision, but the Division has been given authority to adopt temporary regulations immediately without going through the regular administrative review process.

**Encouraging New York Tax Challenges.** In another attempt to stand up to New York on the convenience rule, A4694 seeks to encourage New Jersey residents to challenge New York's imposition of the rule with the reward of a partial credit against New Jersey tax due as a result of the challenge.

For tax years 2020-2023, a "refund" is available to a resident taxpayer who pays any income tax or wage tax to another state (but the legislators really mean New York), who then applies for and is denied a refund from the other state "on income derived from services rendered while the resident taxpayer was within New Jersey," and then files and wins an appeal that results in a refund from the other state. If all of those stars align, then when the resident reports the other state refund to New Jersey (which may require a downward adjustment in the resident credit previously provided by New Jersey), then the resident will get a credit equal to 50% of the tax otherwise owed to New Jersey.

**Pilot Program to Encourage Re-assignment of Certain Employees to New Jersey.** Finally, A4694 establishes a pilot program to be administered by the New Jersey Economic Development Authority, through which the Authority will provide grants to businesses to re-assign their New Jersey resident-employees assigned to locations outside of the State, to New Jersey locations. To be eligible a business must have 25 or more full time employees and the business must be principally located in another state. The value of the credit will be based on the Gross Income Tax withholdings of resident employees re-assigned by the business to a New Jersey location or \$500,000, whichever is less.

Contact [Open Weaver Banks](tel:646.218.7524) (646.218.7524), if you have any questions about these tax updates.

### Disclaimer:

This Client Alert is a form of attorney advertising. Hodgson Russ LLP provides this information as a service to its clients and other readers for educational purposes only. Nothing in this Client Alert should be construed as, or relied upon, as legal advice or as creating a lawyer-client relationship.