

## State Tax Observations

### New Jersey Overhauls Its Taxes

By Sandy Weinberg, JD, Principal

After a flurry of activity in the New Jersey legislature, Governor Phil Murphy signed a series of tax bills that will have an immediate and significant impact on taxpayers in New Jersey. The new tax laws are intended to increase revenue, make sweeping changes to the Corporate Business Tax (CBT), and increase the highest rate for individual gross income tax purposes. A bill which will impose sales tax on remote sellers has been passed and is awaiting the Governor's signature. Also, a new Tax Amnesty Program, which has been signed into law, will be offered this year.

Below is a brief review of New Jersey's tax law overhaul.

#### Corporate Business Tax

**Market Based Sourcing** – Beginning January 1, 2019, sales of services will be sourced to New Jersey if the benefit of the service is received in New Jersey. If the benefit is received within and outside of New Jersey, the sales should be sourced proportionally to each state using reasonable approximation. The sourcing rules could be different for individuals and businesses depending on billing address, location of operation and origin of order.

**Combined Returns** – Also beginning January 1, 2019, New Jersey will require combined reporting for unitary businesses under common control where at least one member of the group is subject to tax in New Jersey. Common control means greater than 50% voting control under standard federal definitions.

**Temporary Corporate Surtax** – A surtax will be applied to any taxpayer, excluding public utilities, with an allocated net income of over \$1 million. The rates and periods are:

- 2.5% between January 1, 2018 and December 31, 2019
- 1.5% between January 1, 2020 and December 31, 2021

No tax credits can be applied against the surtax other than overpayments from previous estimated tax payments.

**Prior Net Operating Loss (PNOL) Carryover** – Prior year pre-apportioned NOLs will be converted to current year post-apportioned NOLs. This will be accomplished by multiplying the prior year NOLs by the "base year" apportionment. The carryforward period remains to be 20 years from the date the NOL was incurred. Additionally, PNOLs and NOLs may only be used to offset the specific group member's income that sustained the loss.

**Note:** An NOL existing before July 1, 2018 can be carried forward for 20 years, but it must be converted to an "unabsorbed portion of net operating loss."

**Dividends Exclusion** – For periods beginning after December 31, 2016, taxpayers that own 80% or more of a subsidiary will be allowed a dividend received deduction (DRD) of 95%, which has been reduced from 100%. For 2017, taxpayers must apportion the non-deductible portion using the lower of:

- a three-year average allocation factor from 2015 to 2017, or
- 3.5%.

After 2017, taxpayers will utilize normal apportionment rules.

**Interest Expense Addback** – New Jersey also amended one of the exceptions to its interest addback requirements. A taxpayer is not required to add back interest if the following criteria are met:

- the taxpayer can demonstrate that the interest was paid to a related member in a foreign country;
- the related member was subject to tax in that country on a tax base that included the interest payment; and
- the effective rate of the tax was equal to or greater than New Jersey's rate, minus three percentage points.

**Federal Decoupling** – New Jersey will decouple from the federal IRC § 199A qualified business income (QBI) deduction which acts to minimize income from flow-through entities. The deduction, permitted federally, will not be allowed for New Jersey.

Additionally, the federal deduction allowed under IRC § 965, relating to the repatriation tax on deferred foreign income, will again not be allowed in calculating the CBT.

In New Jersey, the interest deduction limitation in IRC § 163(j) is applied on a pro rata basis to interest paid to both related and unrelated parties, regardless of whether the related parties are subject to New Jersey's related party interest addback rules.

## Sales Tax

After the Supreme Court's holding in *South Dakota v. Wayfair*, New Jersey passed "remote seller" legislation. The new law states that sales tax nexus is created if a seller has sales exceeding \$100,000 into New Jersey or at least 200 separate transactions.

## Income Tax

**Millionaire Tax Bracket** – A new tax rate of 10.75% (up from 8.97%) will be effective for taxpayers with income exceeding \$5 million. Employers will be required to withhold 15.6% on salaries and wages exceeding \$5 million for tax year 2018.

**Nonresident Exclusion** – The exclusion for nonresidents relating to carried interest and income from investment management services has been eliminated. For corporate business tax and gross income tax purposes, a 17% surtax will also be applied to investment management services.

**Property Tax Deduction** – Starting in 2018, individual taxpayers will be allowed a deduction for property taxes paid up to \$15,000. The allowance was \$10,000 before 2018.

## Tax Amnesty

New Jersey will be offering a 90-day amnesty period ending no later than January 15, 2019. The period available for relief is for returns due February 1, 2009 to September 1, 2017. A taxpayer that pays the outstanding tax liability and one-half of the interest due by November 1, 2018 will not be subject to the following:

- The remaining one-half of the interest balance due,
- Late payment and filing penalties,
- Delinquency penalties, and
- Recovery fees and cost of collection.

## Contact Us

For questions concerning New Jersey's tax legislation or amnesty, or if you have state tax questions generally, please contact:

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