

AN ALERT FROM THE BDO STATE AND LOCAL TAX PRACTICE

BDO KNOWS:

SALT

► SUBJECT

NEW JERSEY ENACTS SIGNIFICANT TAX CHANGES

► SUMMARY

On June 30, 2014, New Jersey Governor Chris Christie signed into law A. 3486, 216th Leg. (N.J. 2014) (“A. 3486”), which results in several significant tax changes, including changes to the Corporation Business Tax (“CBT”) laws as follows: (1) broaden the definition of operational income; (2) require a nonresident partner (corporate or noncorporate) to file a tax return in order to obtain a credit/refund of income tax paid on its behalf; and (3) reduce a net operating loss (“NOL”) for debt discharged and excluded from income on account of bankruptcy or insolvency. In addition, for sales and use tax purposes, the state has adopted a “click-through nexus” standard with respect to Internet sales activity. The CBT changes are effective for privilege periods ending after June 30, 2014, and the “click-through nexus” standard applies to sales made, services rendered, and uses occurring after June 30, 2014.

► DETAILS

Operational income definition

A. 3486 changes the CBT definition of “operational income” (*i.e.*, New Jersey’s equivalent of business income) so that it includes “income from tangible and intangible property if the acquisition, management, *or* disposition of the property constitute an integral part of the taxpayer’s regular trade or business operations[.]” (Emphasis supplied). Under the old law, the definition of “operational income” included income from tangible and intangible property only if the acquisition, management, *and* disposition of the underlying property constituted an integral part of the taxpayer’s regular trade or business operations.

Nonresident partner return and subject to tax requirement

A. 3486 mandates that only a nonresident partner (corporate or noncorporate) that files a New Jersey tax return and reports income that is subject to New Jersey tax may take a credit for income tax a partnership paid on its behalf. Moreover, A. 3486 prohibits a partnership from claiming a refund of tax paid on behalf a nonresident partner.

Reduction of CBT NOLs for debt discharged

A. 3486 requires a reduction of a CBT NOL arising from or carried over to a privilege period ending after June 30, 2014, for an amount excluded from federal taxable



CONTACT:

WEST:

ROCKY CUMMINGS, Tax Partner
415-490-3130 / rcummings@bdo.com

PAUL MCGOVERN, Tax Senior Director
714-913-2592 / pmcgovern@bdo.com

NORTHEAST:

JANET BERNIER, Tax Principal
212-515-5405 / jbernier@bdo.com

MATTHEW DYMENT, Tax Senior Director
617-239-4130 / mdyment@bdo.com

MARK SEIDEN, Senior Director
212-885-8004 / mseiden@bdo.com

SOUTHEAST:

ASHLEY MORRIS, Tax Senior Director
919-278-1963 / amorris@bdo.com

ATLANTIC:

JONATHAN LISS, Tax Senior Director
215-636-5502 / jliss@bdo.com

JEREMY MIGLIARA, Tax Senior Director
703-770-0596 / jmigliara@bdo.com

CENTRAL:

ANGELA ACOSTA, Tax Senior Director
248-688-3313 / aacosta@bdo.com

NICK BOEGEL, Tax Senior Director
414-615-6773 / nboegel@bdo.com

JOE CARR, Tax Principal
312-616-3946 / jcarr@bdo.com

GENE HEATLY, Tax Senior Director
214-665-0716 / gheatly@bdo.com

MARIANO SORI, Tax Partner
312-616-4654 / msori@bdo.com

RICHARD SPENGLER, Tax Senior Director
616-776-3687 / rspengler@bdo.com

SOUTHWEST:

TOM SMITH, Tax Partner
918-281-4080 / tasmith@bdo.com

income under Internal Revenue Code (“IRC”) section 108(a)(1)(A) through (C) for the privilege period of the discharge of indebtedness.

“Click-through nexus” standard for sales and use taxes

A. 3486 creates a rebuttable presumption of nexus with respect to a person that enters into an agreement with an independent contractor or other representative that has a New Jersey physical presence, for a commission or other consideration, if: (1) the independent contractor or representative directly or indirectly refers potential customers (e.g., by a link on an Internet Web site); and (2) the cumulative gross receipts from sales to New Jersey customers who were referred by all independent contractors or representatives that have this type of an agreement with the person were in excess of \$10,000 during the preceding four quarterly periods.

► BDO INSIGHTS

A. 3486 effectively overturns the decision of the New Jersey Superior Court, Appellate Division, in *McKesson Water Products Co. v. Director, Division of Taxation*, 408 N.J. Super. 213, 974 A.2d 443 (2009). In *McKesson*, the court held that the taxpayer’s gain arising from an IRC section 338(h)(10) election did not meet the definition of “operational income” under the old law because the Division was required to adhere to all of the fictional consequences of a taxpayer making such an election, including the deemed liquidation distribution to the parent, which the court found to be a disposition of property that generally does not constitute an integral part of a taxpayer’s regular trade or business operations. Thus, with the change from an “and” to an “or” immediately preceding the word “disposition” in the definition of “operational income,” New Jersey could presumably tax gain arising from an IRC section 338(h)(10) election if the acquisition or management of the property in question constituted an integral part of the taxpayer’s regular trade or business operations without having to even consider the “disposition” aspect of the definition.

The requirement that only a nonresident partner that files a New Jersey tax return and reports income that is subject to New Jersey tax may take a credit for income tax a partnership paid on its behalf and the prohibition against a partnership claiming a refund of tax paid on behalf of a nonresident partner are, no doubt, each a reaction to the decision of the New Jersey Superior Court, Appellate Division, in *BIS LP, Inc. v. Director, Division of Taxation*, No. A-1647-12T3 (unpublished opinion, Apr. 11, 2014). In *BIS LP*, the court held that a corporation that limited its connection with New Jersey to a limited partnership interest in a partnership doing business in the state was entitled to claim a refund notwithstanding the fact that it did not pay the tax or consent to New Jersey tax and was found to not have nexus with New Jersey. The requirement under A. 3486 is troublesome considering that a partnership is required to withhold on a nonresident corporate partner on the basis of its share of entire net income without exception for a corporate partner that may not have nexus with New Jersey.¹ Thus, if strictly read, New Jersey statutes and regulations would require the partnership to pay tax on behalf of a nonresident corporate partner that lacks nexus with New Jersey and A. 3486 would leave the partner and the partnership with no mechanism to seek a credit or refund of the tax.

With the adoption of a “click-through nexus” standard for purposes of subjecting a seller to its sales tax collection, reporting, and payment requirements, New Jersey joins the likes of several other states that have adopted “click-through nexus” laws, including, among others, Arkansas, California, Connecticut, Georgia, Illinois, Kansas, Maine, Missouri, New York, Pennsylvania, Rhode Island, and Vermont.

¹ N.J.S.A. § 54:10A-15.11(a)(1); N.J.A.C. § 18:7-17.5(a)(2).

The Tax Practice at BDO is among the largest tax advisory practices in the United States. With 49 offices and more than 400 independent alliance firm locations in the United States, BDO has the bench strength and coverage to serve you.

BDO is the brand name for BDO USA, LLP, a U.S. professional services firm providing assurance, tax, financial advisory and consulting services to a wide range of publicly traded and privately held companies. For more than 100 years, BDO has provided quality service through the active involvement of experienced and committed professionals. The firm serves clients through 49 offices and over 400 independent alliance firm locations nationwide. As an independent Member Firm of BDO International Limited, BDO serves multinational clients through a global network of 1,264 offices in 144 countries.

BDO USA, LLP, a Delaware limited liability partnership, is the U.S. member of BDO International Limited, a UK company limited by guarantee, and forms part of the international BDO network of independent member firms. BDO is the brand name for the BDO network and for each of the BDO Member Firms. For more information, please visit www.bdo.com.

To ensure compliance with Treasury Department regulations, we wish to inform you that any tax advice that may be contained in this communication (including any attachments) is not intended or written to be used, and cannot be used, for the purpose of (i) avoiding tax-related penalties under the Internal Revenue Code or applicable state or local tax law provisions or (ii) promoting, marketing or recommending to another party any tax-related matters addressed herein.

Material discussed in this tax alert is meant to provide general information and should not be acted on without professional advice tailored to your firm’s individual needs.