

ASSEMBLY APPROPRIATIONS COMMITTEE

STATEMENT TO

ASSEMBLY, No. 4295

with committee amendments

STATE OF NEW JERSEY

DATED: JUNE 23, 2022

The Assembly Appropriations Committee reports favorably and with committee amendments Assembly Bill No. 4295.

This bill, as amended, makes various changes to administration of the gross income tax and the corporation business tax by adapting new federal partnership audit regime, ending COVID-related extensions concerning certain State taxes and eliminating requirement to affirmatively elect New Jersey S Corporation status.

Partnership Audit Regime

New Jersey imposes income tax on partners in accordance with N.J.S.A. 54A:2-2 and N.J.S.A. 54A:5-4. The United States Internal Revenue Service has changed its partnership audit regime so that partnerships are the focus of an audit instead of partners due to legislative changes made by the enactment of Title XI of the Bipartisan Budget Act of 2015 (PL 114-74) and I.R.C. Section 6221(a). Federal audit determinations will be made at the partnership level for post-2017 partnership returns. The provisions of this bill adapt the New Jersey Gross Income Tax to this new federal partnership audit regime that audits the partnership for greater efficiency instead of auditing individual partners. This bill adopts the Multistate Tax Commission's Model Uniform Statute for Reporting Adjustments to Federal Taxable Income and Federal Partnership Audit Adjustments for purposes of the New Jersey Gross Income Tax Act and Corporation Business Tax Act.

Ends COVID-related Extension

This bill ends the extension of time for the statute of limitations on tax due that was enacted in response to the COVID-19 pandemic. The bill also ends the extension for the provisions regarding the State's payment of interest on a taxpayer's overpayment of tax.

Both of these extension's end dates are currently tied by statute to the end of the state of emergency declared by the Governor in Executive Order No. 103. Separately, in Executive Order No. 170, the Governor extended the time for taxpayers to file a claim for a refund

on taxes paid. The end date for that extension is tied to the end of the public health emergency.

On June 4, 2021, the Governor terminated the public health emergency with Executive Order No. 244, but did not terminate the state of emergency. As a result, the extension of time for the statute of limitations on tax due, and payment of interest on tax overpayments, still do not have an end date, while the extension of time for the filing of refund claims does have an end date.

This bill changes the end dates for the extension of time for the statute of limitations on tax due, and payment of interest on overpayments of tax, so that the extensions are tied to the end of the public health emergency, as is the case with the extension for the filing of refund claims.

Separate S Corporation Election

This bill eliminates the requirement that a taxpayer which qualifies as a Subchapter S Corporation for federal tax purposes affirmatively elect New Jersey S Corporation status for purposes of the State's Corporation Business Tax and Gross Income Tax. S Corporations retain certain benefits of the corporate form, such as limited liability, without the "double" taxation of corporate income and dividends distributed that applies to C Corporations. When S Corporation status is elected for federal purposes, the income and losses incurred by the entity pass-through to the shareholders of the S Corporation.

A "small business corporation" as defined in the federal Internal Revenue Code may elect to be an S Corporation for purposes of federal income taxation. The corporation must affirmatively elect to be an S Corporation for a particular taxable year, and all shareholders must give their consent to the election.

New Jersey currently requires that entities which have elected to be S Corporations for federal tax purposes, and that want to be treated as S Corporations for State tax purposes, must affirmatively elect to be treated as a New Jersey S Corporation by annually submitting a form to the Director of the Division of Taxation. Failure to make such an election for State purposes results in the taxation by the State of the entity's corporate income and of dividends received by shareholders, as occurs for corporations generally.

This bill removes the requirement that a taxpayer which elects treatment as an S Corporation for federal tax purposes must also elect to be a "New Jersey S Corporation." This bill links New Jersey S Corporation status to the S Corporation election for federal income tax purposes and eliminates the confusion and administrative snafus that have prevented some eligible taxpayers from receiving the benefits of "pass-through" taxation.

An S corporation may also elect not to be taxed as a New Jersey S corporation. This election must have the consent of 100 percent of the

shareholders of the S corporation. The election may be made for any taxable year at any time during the preceding taxable year or at any time on or before the due date or extended due date of the S corporation's tax return. An election to not be taxed as a New Jersey S corporation may be revoked if shareholders holding more than 50 percent of the shares of stock of the S corporation on the day on which the revocation is made consent to the revocation.

Upon enactment of this bill, New Jersey would join the majority of states that accept a federal S Corporation election for state tax purposes without requiring any additional action on the part of the corporation. The bill streamlines the process by which eligible corporations may avail themselves of "pass-through" tax treatment on the State level.

The bill retains the requirement that the S Corporation and each shareholder affirmatively consent to existing jurisdictional requirements, in a form and manner to be determined by the director.

COMMITTEE AMENDMENTS

The committee amendments clarify that an S corporation may elect not to be taxed as an S corporation with the consent of 100 percent of the shareholders of the S corporation.

FISCAL IMPACT:

The Executive has not published a formal fiscal note, but does anticipate this bill will be revenue neutral.

The Office of Legislative Services (OLS) can neither confirm nor refute the Executive's determination that this bill will likely be revenue neutral. The OLS notes that these provisions are largely meant to ease the administrative burden of the Division of Taxation while also simplifying certain processes for taxpayers. However, there could be underlying effects that reduce costs for the State or capture more revenue.