

SENATE, No. 3246

STATE OF NEW JERSEY 218th LEGISLATURE

INTRODUCED DECEMBER 3, 2018

Sponsored by:

Senator PAUL A. SARLO

District 36 (Bergen and Passaic)

Senator TROY SINGLETON

District 7 (Burlington)

Senator STEVEN V. OROHO

District 24 (Morris, Sussex and Warren)

Senator ANTHONY R. BUCCO

District 25 (Morris and Somerset)

SYNOPSIS

Establishes elective pass-through business alternative income tax and allows refundable gross income tax credit for taxpayers earning income from pass-through businesses in taxable year.

CURRENT VERSION OF TEXT

As introduced.



1 AN ACT establishing an elective pass-through business alternative
2 income tax and allowing a refundable gross income tax credit for
3 taxpayers earning income from pass-through businesses,
4 supplementing Title 54A of the New Jersey Statutes and
5 amending N.J.S.54A:4-1 and P.L.1993, c.173.

6
7 **BE IT ENACTED** by the Senate and General Assembly of the State
8 of New Jersey:

9
10 1. (New section) This act shall be known and may be cited as
11 the “Pass-Through Business Alternative Income Tax Act.”

12
13 2. (New section) As used in P.L. , c. (C.) (pending
14 before the Legislature as this bill):

15 “Distributive proceeds” means the income, dividends, and gain
16 of a pass-through entity, derived from or connected with sources
17 within the State, and upon which tax is imposed and due on a
18 member of the pass-through entity pursuant to the “New Jersey
19 Gross Income Tax Act,” N.J.S.54A:1-1 et seq., in a taxable year.

20 “Member” means a natural person who is a shareholder of a New
21 Jersey S corporation; a partner in a general, limited, or limited
22 liability partnership; or a member of a New Jersey limited liability
23 company.

24 “New Jersey limited liability company” means an entity
25 organized pursuant to the “Revised Uniform Limited Liability
26 Company Act,” P.L.2012, c.50 (C.42:2C-1 et seq.), or prior law
27 providing for the formation of a limited liability company in this
28 State that, pursuant to section 92 of P.L.2012, c.50 (C.42:2C-92), is
29 classified as a partnership.

30 “New Jersey S corporation” means the same as that term is used
31 in subsection (p) of section 4 of P.L.1945, c.162 (C.54:10A-4).

32 “Partnership” means a syndicate, group, pool, joint venture, or
33 other unincorporated organization, through or by means of which
34 any business, financial operation, or venture is carried on in this
35 State, and which is not, within the meaning of P.L. , c. (C.)
36 (pending before the Legislature as this bill), a trust or estate or a
37 corporation.

38 “Pass-through entity” means a partnership, a New Jersey S
39 corporation, or a New Jersey limited liability company, with at least
40 one member who is liable for tax on distributive proceeds pursuant
41 to the “New Jersey Gross Income Tax Act,” N.J.S.54A:1-1 et seq.,
42 in a taxable year.

43 “Pro rata share of distributive proceeds” means the portion of
44 distributive proceeds attributable to a member of a pass-through
45 entity in a taxable year.

EXPLANATION – Matter enclosed in bold-faced brackets [thus] in the above bill is not enacted and is intended to be omitted in the law.

Matter underlined thus is new matter.

1 “Taxable year” means the same as that term is used in section 12
2 of P.L.1993, c.173 (C.54A:5-10).

3
4 3. (New section) a. A pass-through entity with at least one
5 member who is liable pursuant to the “New Jersey Gross Income
6 Tax Act,” N.J.S.54A:1-1 et seq., for tax on that member’s pro rata
7 share of distributive proceeds of the pass-through entity in a taxable
8 year may elect to be liable for, and pay, a pass-through business
9 alternative income tax in the taxable year.

10 b. (1) Each pass-through entity that makes an election for a
11 taxable year pursuant to this section shall report to each of its
12 members, for the taxable year, the member’s pro rata share of
13 distributive proceeds.

14 (2) The tax imposed on a pass-through entity pursuant to this
15 section shall be equal to the sum of: each member’s pro rata share
16 of distributive proceeds attributable to the pass-through entity for
17 the taxable year, multiplied by 10.75%.

18 (3) If a member’s proportionate share of New Jersey gross
19 income tax liability for the taxable year, after the application of any
20 credits, deductions, or exemptions, is an amount equal to or less
21 than \$1, then that member’s pro rata share of distributive proceeds
22 shall be disregarded for purposes of determining the tax pursuant to
23 this section; provided, however, that the member shall not be
24 eligible to claim a credit pursuant to section 5 of P.L. ,
25 c. (C.) (pending before the Legislature as this bill) for the
26 taxable year.

27 c. The amount of pass-through business alternative income tax
28 due from a pass-through entity in a taxable year shall be exclusive
29 of any amount of tax due and paid by the pass-through entity
30 pursuant to the "Corporation Business Tax Act (1945)," P.L.1945,
31 c.162 (C.54:10A-1 et seq.), during any privilege period, except as
32 otherwise provided in P.L. , c. (C.) (pending before the
33 Legislature as this bill).

34 d. The director shall set the schedule and procedures for the
35 payment of pass-through business alternative income tax.

36
37 4. (New section) a. For the purpose of administration of
38 P.L. , c. (C.) (pending before the Legislature as this bill),
39 the director shall have those powers as the director deems necessary
40 to apply to a pass-through entity subject to P.L. , c. (C.)
41 (pending before the Legislature as this bill), for the reporting,
42 payment, collection, administration, and enforcement of the tax
43 imposed pursuant to P.L. , c. (C.) (pending before the
44 Legislature as this bill), as may be applicable to the collection,
45 administration, and enforcement of the New Jersey gross income
46 tax provided in the “New Jersey Gross Income Tax Act,”
47 N.J.S.54A:1-1 et seq., except as otherwise provided by subsection
48 b. of this section.

1 b. Taxes collected under the provisions of P.L. , c. (C.)
2 (pending before the Legislature as this bill) shall be deposited by
3 the State Treasurer in the General Fund.

4
5 5. (New section) a. Except as otherwise provided in paragraph
6 (3) of subsection b. of section 3 of P.L. , c. (C.) (pending
7 before the Legislature as this bill), a taxpayer shall be allowed a
8 refundable gross income tax credit, pursuant to the "New Jersey
9 Gross Income Tax Act," N.J.S.54A:1-1 et seq., if the taxpayer is a
10 member of a pass-through entity that elects to owe and pay the
11 pass-through business alternative income tax determined pursuant
12 to section 3 of P.L. , c. (C.) (pending before the Legislature
13 as this bill) for the taxable year.

14 For each pass-through entity of which the taxpayer is a member,
15 the amount of the credit shall equal the member's pro rata share of
16 the tax paid pursuant to section 3 of P.L. , c. (C.) (pending
17 before the Legislature as this bill) multiplied by 89.25%, which
18 credit shall be applied against the gross income tax liability of the
19 member in the taxable year.

20 b. The order of priority in which the credit allowed by this
21 section and any other credits allowed by law may be taken shall be
22 as prescribed by the director.

23 c. For a taxpayer that applies the credit available pursuant to this
24 section to the tax due pursuant to N.J.S.54A:1-1, if the credit
25 exceeds the amount of tax otherwise due, that amount of excess
26 shall be an overpayment for the purposes of N.J.S.54A:9-7;
27 provided however, that subsection (f) of N.J.S.54A:9-7 shall not
28 apply.

29
30 6. Section 3 of P.L.1993, c.173 (C.54:10A-5.22) is amended to
31 read as follows:

32 3. a. A corporation may elect, in accordance with the provisions
33 of this section, to be a New Jersey S corporation. In order for an
34 election to be valid, the corporation and each of its shareholders on
35 the day on which the election is made (hereinafter "initial
36 shareholders") must consent to such election and the jurisdictional
37 requirements of becoming a New Jersey S corporation. The form of
38 the election and consent to jurisdictional requirements and the place
39 for filing shall be as prescribed by the Director of the Division of
40 Taxation.

41 b. Each initial shareholder and the corporation shall consent to
42 the following jurisdictional requirements:

43 (1) That this State shall have the right and jurisdiction to tax and
44 collect the tax on each shareholder's S corporation income as
45 defined pursuant to section 12 of P.L.1993, c.173 (C.54A:5-10) and,
46 if applicable, the pass-through business alternative income tax
47 pursuant to P.L. , c. (C.) (pending before the Legislature as
48 this bill);

1 (2) That New Jersey's right and jurisdiction to tax the income as
2 set forth in paragraph (1) of this subsection shall not be affected by
3 a change of a shareholder's residency, except as provided by the
4 "New Jersey Gross Income Tax Act," N.J.S.54A:1-1 et seq.; and

5 (3) If shareholders that are not initial shareholders of the
6 corporation, while the corporation is a New Jersey S corporation,
7 fail to consent to New Jersey's jurisdiction to tax S corporation
8 income to such shareholders, this State shall have the right and
9 jurisdiction to collect a payment of tax each year directly from the
10 corporation equal to the S corporation income allocated to this
11 State, as defined pursuant to section 12 of P.L.1993, c.173
12 (C.54A:5-10), of the nonconsenting shareholders for the accounting
13 or privilege period multiplied by the maximum tax bracket rate
14 provided under N.J.S.54A:2-1 for the accounting or privilege
15 period. In such case, the corporation shall have the right, but not
16 the obligation, to recover payments made by the corporation
17 pursuant to this paragraph from each nonconsenting shareholder.

18 c. A corporation may make an election to become a New Jersey
19 S corporation with respect to an accounting or privilege period for
20 which the corporation is or will be an S corporation. The election
21 for an accounting or privilege period, along with the consents to
22 jurisdictional requirements, shall be filed within one calendar
23 month of the time at which a federal S corporation election would
24 be required if such accounting or privilege period were a "taxable
25 year" for which a federal S corporation election were to be made
26 pursuant to section 1362 of the federal Internal Revenue Code of
27 1986, 26 U.S.C. s.1362. Such elections may only be revoked
28 pursuant to subsection d. of this section. Such election shall
29 terminate immediately upon the corporation's failure to satisfy the
30 definition of a New Jersey S corporation pursuant to paragraph (p)
31 of section 4 of P.L.1945, c.162 (C.54:10A-4).

32 d. A corporation may revoke an election pursuant to this section
33 on or before the last day of the first accounting or privilege period
34 to which the election would otherwise apply.

35 (cf: P.L.1993, c.173, s.3)

36

37 7. Section 4 of P.L.1993, c.173 (C.54:10A-5.23) is amended to
38 read as follows:

39 4. a. With respect to each of its shareholders that is not an
40 initial shareholder, a New Jersey S corporation shall satisfy the
41 requirements of either paragraph b. or c. of this section.

42 b. Deliver a consent to the jurisdictional requirements as set
43 forth in subsection b. of section 3 of P.L.1993, c.173 (C.54:10A-
44 5.22).

45 c. Make payments to the Director of the Division of Taxation on
46 behalf of each nonconsenting shareholder in an amount equal to the
47 shareholder's pro rata share of S corporation income allocated to
48 this State, as defined pursuant to section 12 of P.L.1993, c.173

1 (C.54A:5-10), reflected on the corporation's return for the
2 accounting or privilege period, multiplied by the maximum tax
3 bracket rate provided under N.J.S.54A:2-1 in effect at the end of the
4 accounting or privilege period. The payments shall be made no
5 later than the time for filing of the return for the accounting or
6 privilege period. The director may, by regulation, require that
7 amounts estimated to be equal to the liability expected to be due
8 pursuant to this subsection be withheld from any distribution made
9 to a nonconsenting shareholder.

10 d. If a shareholder that is not an initial shareholder of a New
11 Jersey S corporation fails to deliver a consent to the jurisdictional
12 requirements set forth in subsection b. of section 3 of P.L.1993,
13 c.173 (C.54:10A-5.22), and objects to New Jersey's jurisdiction to
14 withhold payments pursuant to subsection c. of this section, then
15 this State shall have the right and jurisdiction to collect a tax each
16 year directly from the corporation equal to the pro rata share of the
17 S corporation income allocated to this State, as defined pursuant to
18 section 12 of P.L.1993, c.173 (C.54A:5-10), of the nonconsenting
19 shareholder times the maximum tax bracket rate provided under
20 N.J.S.54A:2-1 for the appropriate accounting or privilege period.
21 In such case, the corporation shall have the right, but not the
22 obligation, to recover payments made by the corporation pursuant to
23 this subsection from each nonconsenting shareholder. The
24 corporation shall not be liable for the pass-through business
25 alternative income tax pursuant to P.L. , c. (C.) (pending
26 before the Legislature as this bill) relative to collections made in a
27 taxable year for such nonconsenting members.

28 (cf: P.L.1993, c.173, s.4)

29

30 8. N.J.S.54A:4-1 is amended to read as follows:

31 54A:4-1. Resident credit for tax of another state. (a) A resident
32 taxpayer shall be allowed a credit against the tax otherwise due
33 under this act for the amount of any income tax or wage tax
34 imposed for the taxable year by another state of the United States or
35 political subdivision of such state, or by the District of Columbia,
36 with respect to income which is also subject to tax under this act,
37 except as provided by subsections (c) and (d) of this section.

38 (b) The credit provided under this section shall not exceed the
39 proportion of the tax otherwise due under this act that the amount of
40 the taxpayer's income subject to tax by the other jurisdiction bears
41 to his entire New Jersey income.

42 (c) No credit shall be allowed against the tax otherwise due
43 under this act for the amount of any income tax or wage tax
44 imposed for the taxable year on S corporation income allocated to
45 this State.

46 (d) No credit shall be allowed for the amount of any taxes paid
47 or accrued for the taxable year on or measured by profits or income

1 imposed on or paid on behalf of a person other than the taxpayer,
2 whether or not the taxpayer may be held liable for the tax.

3 (e) Readjustment of the tax of another state or political
4 subdivision thereof--if the taxpayer is allowed credit under this
5 section for more or less of the tax of another state or political
6 subdivision thereof than he is finally required to pay, the taxpayer
7 shall send notice of the difference to the director who shall
8 redetermine the tax for any years affected regardless of any
9 otherwise applicable statute of limitations.

10 (f) A resident taxpayer shall be allowed a credit against the tax
11 otherwise due under this act for the amount of any tax that the
12 director determines is substantially similar to the tax imposed
13 pursuant to section 2 of P.L. , c. (C.) (pending before the
14 Legislature as this bill), for the taxable year, by another state of the
15 United States or political subdivision of such state, or by the
16 District of Columbia, with respect to the direct and indirect
17 distributive proceeds from a pass-through entity, which distributive
18 proceeds are also subject to tax under this act.

19 For purposes of this subsection, "distributive proceeds" and
20 "pass-through entity" mean the same as those terms are used in
21 section 2 of P.L. , c. (C.) (pending before the Legislature
22 as this bill).

23 (cf: P.L.1993, c.173, s.7)

24

25 9. Section 11 of P.L.1993, c.173 (C.54A:5-9) is amended to read
26 as follows:

27 11. **[An]** Except as otherwise provided by P.L. , c. (C.)
28 (pending before the Legislature as this bill), an S corporation as
29 such shall not be subject to the tax imposed by the "New Jersey
30 Gross Income Tax Act," N.J.S.54A:1-1 et seq., but the S
31 corporation income, dividends, and gain of a shareholder of an S
32 corporation shall be subject to the tax, and the tax shall be imposed
33 on the shareholder's pro rata share, whether or not distributed, of the
34 S corporation income for its taxable year ending within or with the
35 shareholder's taxable year.

36 (cf: P.L.1993, c.173, s.11)

37

38 10. Section 15 of P.L.1993, c.173 (C.54A:5-13) is amended to
39 read as follows:

40 15. For purposes of **[this act]** the "New Jersey Gross Income
41 Tax Act," N.J.S.54A:1-1 et seq., if a shareholder of an S
42 corporation is both a resident and a nonresident of this State during
43 any taxable year, the shareholder's pro rata share of the S
44 corporation income allocated to this State and S corporation income
45 not allocated to this State for the taxable period shall be further
46 prorated between the shareholder's periods of residence and
47 nonresidence during the taxable period, in accordance with the
48 number of days in each period. Any prorated amount of S

1 corporation income determined pursuant to this section shall also
2 apply to determinations of income for purposes of the assessment of
3 the pass-through business alternative income tax, pursuant to
4 P.L. , c. (C.) (pending before the Legislature as this bill).
5 (cf: P.L.1993, c.173 s.15)

6
7 11. (New section) The director shall adopt, pursuant to the
8 “Administrative Procedure Act,” P.L.1968, c.410 (C.52:14B-1 et
9 seq.), and immediately upon filing with the Office of
10 Administrative Law, rules and regulations necessary to effectuate
11 the purposes of P.L. , c. (C.) (pending before the
12 Legislature as this bill), which shall be effective for a period not to
13 exceed 360 days following enactment of P.L. , c. (C.)
14 (pending before the Legislature as this bill) and may thereafter be
15 amended, adopted, or readopted by the director in accordance with
16 the requirements of P.L.1968, c.410.

17
18 12. This act shall take effect immediately and shall apply to
19 taxable years of pass-through entities beginning on or after January
20 1, 2019.

21 22 23 STATEMENT

24
25 This bill, the “Pass-Through Business Alternative Income Tax
26 Act,” establishes an elective entity-level tax to be paid by pass-
27 through businesses and provides an offsetting credit to taxpayers
28 who receive income from a pass-through business.

29 Pass-through businesses are partnerships, New Jersey limited
30 liability companies that are not taxed as incorporated entities by the
31 State, and New Jersey S corporations. These entities are called
32 pass-through businesses because, generally, the profits are passed
33 directly through the business to the owners, and tax is assessed and
34 levied on the owners' individual tax returns.

35 The bill creates an optional entity-level tax on pass-through
36 businesses. Specifically, and at the election of the business, the tax
37 is levied on a pass-through business that has at least one partner,
38 shareholder, or member (collectively, “member”) that is a natural
39 person and owes New Jersey gross income tax on income,
40 dividends, and gain received from the pass-through business, and
41 sourced to the State, in the tax year (the “distributive proceeds”).
42 To calculate the amount of tax due, the pass-through business is
43 first required to determine the amount of distributive proceeds that
44 each member receives from the business in the tax year. Then, each
45 member’s pro rata share of the distributive proceeds is multiplied
46 by the highest marginal rate under the New Jersey gross income tax,
47 which is 10.75% (the “taxed share”). Finally, the pass-through
48 business adds together each member’s taxed share to determine the

1 business's pass-through business alternative income tax liability for
2 the tax year. However, if a member does not owe gross income tax
3 in a tax year, or the liability is less than \$1, then that member's
4 amount of distributive proceeds is disregarded for purposes of
5 calculating the pass-through tax liability for the tax year.

6 For a business that chooses to pay the pass-through tax in a tax
7 year, the bill provides a refundable gross income tax credit that is
8 available to taxpayers who are members of the pass-through
9 business. Specifically, the amount of this credit is equal to that
10 member's taxed share, multiplied by 89.25%. However, if a
11 member does not owe gross income tax in a tax year, or the liability
12 is less than \$1, then that member is prohibited from claiming the tax
13 credit that is available under this bill for the tax year, since that
14 member's pro rata share of distributive proceeds was disregarded
15 for purposes of determine the tax liability.

16 The Director of the Division of Taxation in the Department of
17 the Treasury is authorized to develop and promulgate rules,
18 regulations, procedures, and forms for the administration and
19 collection of the tax, including but not limited to the payment
20 schedule, and the tax credit provided by this bill.

21 Pass-through businesses may be small and medium-sized,
22 privately owned entities that operate for federal and state personal
23 income tax purposes as pass-through entities and not actual income
24 tax paying entities. For each of these entities, the taxable income is
25 reported on the member's personal tax return, and taxes are paid by
26 the individual. The ability of these individuals to deduct these
27 personal state income tax payments are now restricted as federal
28 personal itemized deductions to no more than \$10,000 per year, but
29 are not capped for businesses to use as unlimited business expenses
30 that can reduce the income passed on to their individual members.
31 This bill establishes a new tax and individual tax credit that will
32 preserve, at the business level, an uncapped offset against taxable
33 income, and that business income offset will credit the individual
34 taxpayer for their individual liability attributable to that income
35 derived from the pass-through business.

36 The bill takes effect immediately and applies to taxable years of
37 pass-through entities beginning on or after January 1, 2019.