

NEW JERSEY ENACTS BUDGET WITH FEW TAX CHANGES

The 2005-06 New Jersey budget was enacted on July 2nd with few tax changes (S-3000, P.L. 2005 c. 132). Some businesses are being denied a new federal deduction for state tax purposes and high income individuals are being denied the exclusion for pension and other retirement income. Although not directly related to the budget, New Jersey also enacted changes to its Sales and Use Tax Act to confirm to the requirements of the multi-state Streamlined Sales and Use Tax Agreement. Other sales and use tax proposals by Acting Governor Richard J. Codey – expanding the tax base (S-2628) and taxing electronically delivered computer software (part of S-3003) – were omitted from the final set of bills.

Decoupling Federal Tax Deduction (A-4294/S-2638, P.L. 2005 c. 127)

Newly-enacted § 199 of the U.S. Internal Revenue Code allows taxpayers to deduct a percentage of income attributable to U.S. manufacturing and other qualifying production activity. For New Jersey tax purposes, this deduction will be limited to income attributable exclusively to manufacturing or production, narrowly defined as performing an operation(s) that substantially changes the “form, composition, or character” of tangible personal property “into a different or substantially more usable product.”

Among IRC § 199 activities not meeting the New Jersey definition are growing or extracting property, software development, filmmaking, the production of electricity, natural gas and potable water, construction and engineering and architectural services. Based on a recent survey by the Federation of Tax Administrators, New Jersey will be among 19 states that are not expected to conform to IRC § 199

Pension and Retirement Exclusion Denied to High Income Individuals (A-4404/S-2637, P.L. 2005 c. 130)

Starting this year, individuals with New Jersey gross income over \$100,000 may no longer exclude any otherwise taxable payments from a pension, disability, retirement, annuity, endowment or life insurance contract or other income on account of being 62 years or older. Other taxpayers will continue to exclude up to \$20,000, \$15,000 or \$10,000, depending on filing status, for such payments.

Streamlined Sales and Use Tax Agreement Changes (A-3473/S-1958, P.L. 2005 c. 126)

Effective October 1, 2005, New Jersey has enacted definitional changes and an amnesty provision required under the Streamlined Sales and Use Tax (SST) Agreement. As a result, on July 1st New Jersey, which has been involved as a participating state since 2001, was admitted as the 18th member state of the SST’s initial Governing Board.

The SST Project was organized five years ago to simplify and modernize tax administration, to encourage remote sellers (those without a physical presence in a state) to collect sales tax voluntarily and, ultimately, to have federal legislation enacted authorizing states to compel collection by remote sellers. The SST Agreement will become effective on October 1, 2005 among the member states.

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Among the definitional changes are those affecting the taxability of food, clothing and medical equipment. Amnesty provisions will eliminate potential past liabilities of sellers who are not under audit and register with the New Jersey Division of Taxation, ostensibly by September 30, 2006. Anticipating enactment, last month the New Jersey Division of Taxation issued a draft proposed regulation to clarify and explain the state's administrative aspects of the SST Agreement, although it does not cover the amnesty provisions.

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