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State Tax Observations

New Jersey Legislation Results in Substantial Tax Changes

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New Jersey's fiscal year 2023-2024 State Budget was signed by Governor Murphy late last month. The legislation enacts significant business and personal income tax changes, several of which are detailed below. Many of these changes are effective now so it's important that you are familiar with them.

Partnership Sourcing

- **Partnership Sourcing** – Effective January 1, 2023, similar to corporations, partnerships (and sole proprietors) will be required to use a single sales factor to allocate its income, rather than the current three-factor formula. In addition, service providers must now use a market-based sourcing approach to allocate income vs the current cost of performance.

- **Partnership Filing Requirement** – The current NJ-1065 instructions state "every partnership that has income or loss derived from sources in the State of New Jersey must file Form NJ-1065." Under the new single sales factor market-based sourcing rules, a partnership having a client or customer in NJ will now have income or loss derived from NJ sources, resulting in a partnership filing requirement.

- **Unitary Partnerships and the Nonresident Partner Partnership Withholding** – Effective for tax years ending on or after July 31, 2023, unitary partnerships are exempt from paying the portion of the partnership withholding tax that is directly or indirectly (in the case of a tiered partnership) attributable to the member of the combined group that is a corporate partner in the unitary partnership.

Corporation Business Tax (CBT)

Effective for tax years ending on or after July 31, 2022, NJ will implement the following changes:

- **Net Operating Loss (NOL) Adjustments** – Adjustments to NOLs from closed years may now be made by either the taxpayer or the director on assessments for a period up to 10 years after the return is filed.

- **Timing of Deduction of New Jersey Qualified Research Expenditures** – The entire amount of NJ qualified research expenditures may be deducted in the same year as the NJ Research and Development Tax Credit.

Effective for tax years ending on or after July 31, 2023, NJ will implement the following changes:

- **"Wayfair"-type economic nexus threshold for corporate income tax** – For corporate income tax purposes, NJ will extend the same bright-line economic nexus thresholds to remote sellers that it already has in place for sales tax purposes (i.e., 200 or more transactions or receipts of more than $100,000).

- **Change in due date** – The due date for the NJ CBT return has changed to the 15th day of the month immediately following the month of the original due date for filing the taxpayer's federal corporate tax return for the same tax year (i.e., April 15th).

- **GILTI deduction increase** – New Jersey's Global Intangible Low-Taxed Income (GILTI) deduction will increase from 50% to 95%, a change that NJ industries have been seeking for years.

- **NJ's conformity to IRC Section 172 limitations** — The Legislation conforms to IRC Section 172's 80% limitation on utilization of NOLs. It also allows sharing of NOL and prior NOL (PNOL) carryforwards among combined group members, regardless of whether such NOL or PNOL carryforwards were created within a combined filing with the sharing members.

- **Shift from "Joyce" to "Finnigan" combined filing method** – All combined reporting groups are now required to use the "Finnigan" apportionment method and compute the numerator and denominator of the allocation factor of the combined group as one taxpayer, taking into account all unitary receipts of all members of the combined group.

- **Definition of Unitary Business Amended** – The definition of a unitary business will include business entities under common ownership that are: "sufficiently interdependent, integrated, or interrelated through their activities so as to provide a synergy and mutual benefit that produces a sharing or exchange of value among them and a significant flow of value among the separate parts."

- **Changes to the Water's-Edge Group** – The default water's edge group has been revised to eliminate the provision that included a member merely because it had NJ nexus and income.

- **Changes to Calculating Taxable Net Income** – Net operating losses will now be allowed before utilizing the dividends received deduction.

In addition to the above, other legislation awaiting the Governor's signature targets New York State's convenience of the employer rule by creating its own reciprocal convenience rule starting in 2023 (to be detailed in a later Thought Leadership Article).

Contact Us

If you have any questions regarding these matters, please contact your PKF O'Connor Davies client engagement partner or:

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