

**FISCAL NOTE**  
**SENATE, No. 2466**  
**STATE OF NEW JERSEY**  
**209th LEGISLATURE**

DATED: JULY 18, 2001

**SUMMARY**

**Synopsis:** Concerns payment obligations of certain partnerships and limited liability companies and certain of their partners and members under the corporation business tax.

**Type of Impact:** Limits potential decreases in corporation business tax revenue.

**Agencies Affected:** Department of the Treasury, Division of Taxation.

**Executive Estimate**

<b>Fiscal Impact</b>	<b><u>Year 1</u></b>	<b><u>Year 2</u></b>	<b><u>Year 3</u></b>
<b>State Revenue</b>	\$420 million	Not specified	Not specified

**Office of Legislative Services Estimate**

<b>Fiscal Impact</b>	<b><u>Year 1</u></b>	<b><u>Year 2</u></b>	<b><u>Year 3</u></b>
<b>State Revenue</b>	Indeterminate	Indeterminate	Indeterminate

- ! The bill requires limited liability companies and limited partnerships that are classified as partnerships for federal tax purposes to obtain the consent of each of its non-individual (e.g., incorporated) members or partners to New Jersey taxation. A business that does not have the consent for one of its "non-individual" (usually incorporated) owners must pay corporation business tax on behalf of that nonconsenting owner's share of the business' New Jersey income.
- ! The bill forecloses an avenue of corporation business tax avoidance.

**BILL DESCRIPTION**

Senate Bill No. 2466 of 2001 provides a mechanism for taxing the owners of limited liability companies and limited partnerships. The bill allows a limited liability company, foreign limited liability company, limited partnership or foreign limited partnership that is classified as a partnership for federal tax purposes to obtain the consent of each of its owners that are not individuals, trusts or estates subject to the "New Jersey Gross Income Tax Act", N.J.S.54A:1-1 et seq. (for example, each owner that is itself a corporation) that this State has the right and

jurisdiction to tax the owner's income derived from the activities of the limited liability company or limited partnership in New Jersey. A business that does not have the consent of all of its owners must pay a corporation business tax liability, on behalf of its nonconsenting owners, on each of the nonconsenting owner's shares of the business' New Jersey income. A number of organizations, because of their distinctive characteristics, are exempted from certain provisions of the substitute.

For each privilege period of a limited liability company or limited partnership, the company or partnership must make a payment on the 15th day of the fourth month following the close of the period (in most cases, April 15) equal to the corporation business tax imposed at its highest rate on the income shares of the organization's owners that have not themselves consented to New Jersey taxation (no amount is paid on behalf of owners that have consented to taxation).

These payment amounts are credited to accounts for the nonconsenting owners, who may let them stand in payment of their liabilities or who may consent to taxation and, as part of that process, apply for refunds of any amounts in excess of their actual liability paid on their behalf.

The limited liability companies and limited partnerships will also make estimated payments of their nonconsenting members' current years' taxes on 15th day of the fourth month of the privilege period (again, usually April 15th). These payments will be based, where appropriate, on the prior year's income of the company or partnership.

The substitute is effective, retroactively, for privilege periods beginning on or after January 1, 2001. Transition provisions exempt the companies and partnerships from making estimated payments for tax year 2001 (those payments would have been due April 15, 2001) and reduce the final payment of tax on behalf of the nonconsenting members for 2001, due in 2002, to 45 percent of the amount otherwise due to account for the enactment of the new provisions in the middle of a tax period.

## **FISCAL ANALYSIS**

### ***EXECUTIVE BRANCH***

The Department of the Treasury notes that there are approximately 70,000 limited liability companies and 15,000 limited partnerships doing business in New Jersey. The department notes that the detailed information concerning percentage of ownership and allocations of net income of limited liability companies and limited partnerships is unavailable, and that therefore only a rough order-of-magnitude estimate is possible.

The department notes further that if 25 percent of the entire corporation business tax base for 1998 were subject to the tax avoidance mechanism being foreclosed by the bill, then corporation business tax revenues for that period would have been reduced by over \$350 million. The department notes further that, in cooperation with corporation tax experts, it has identified several New Jersey limited liability companies where the combined revenue impact of the bill could exceed \$200 million.

Apparently using this information, after noting that taxation for the 2001 privilege period will be 45 percent of the amount otherwise due, the department projects that the 2001 liability period final payments due in FY2002 will be \$120 million and that the estimated payments (based on 100 percent of the 2001 liability) due in FY2002 will be \$300 million, for a total FY2002 revenue impact of \$420 million.

***OFFICE OF LEGISLATIVE SERVICES***

The Office of Legislative Services (OLS) concurs with the Department of the Treasury that only a rough order-of-magnitude estimate is possible.

The department states that its revenue estimate is based on specialized anecdotal data, which is unavailable to the OLS. There is no information available to the OLS which would allow it to agree or disagree with the departmental estimate, although the OLS does note that 45 percent of 300 is 135, not 120, and, if the departmental estimate is on target, it is not unlikely that businesses that were able to direct 25 percent of the entire corporate tax base through a tax avoidance vehicle in a few years will be able to adjust their behavior to the changes under the bill.

Section: *Revenue, Finance and Appropriations*

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This fiscal note has been prepared pursuant to P.L.1980, c.67.