Committee Meeting

of

ASSEMBLY REGULATORY OVERSIGHT COMMITTEE

“Simplifying tax compliance and collection”

LOCATION: Committee Room 11
State House Annex
Trenton, New Jersey

DATE: March 1, 2000
10:00 a.m.

MEMBERS OF COMMITTEE PRESENT:

Assemblyman Guy R. Gregg, Chairman
Assemblyman Kevin J. O’Toole, Vice-Chairman
Assemblyman Michael Patrick Carroll
Assemblyman Gary L. Guear Sr.
Assemblyman Reed Gusciora

ALSO PRESENT:

David L. Sallach
Office of Legislative Services
Committee Aide

Laura A. Neumann
Assembly Majority
Committee Aide

Mary Alice Messenger-Gault
Assembly Democratic
Committee Aide

Meeting Recorded and Transcribed by
The Office of Legislative Services, Public Information Office,
Hearing Unit, State House Annex, PO 068, Trenton, New Jersey
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APPENDIX:

Summary of testimony plus attachments submitted by
E. Martin Davidoff, CPA, Esq. 1x

Comments submitted by
James B. Evans Jr., CPA, Esq. 13x

rs: 1-123
ASSEMBLYMAN GUY R. GREGG (Chairman): Good morning, everybody. If we can take our seats, we'll get this Committee hearing started.

I’d like to welcome you to the first public hearing for the Regulatory Oversight Committee. I’d like to thank all the staff that have put some time into this, David Sallach, OLS people, who put the time together, and our recorders that are here today.

I’d like to remind everyone that this hearing is being recorded, so when you do come up to testify, please give your name first and the business or group that you represent prior to your testimony.

This hearing today is dedicated to Treasury. Your testimony, we hope, will deal with issues that go from the way Treasury communicates with you -- fees in relation to taxes, audits, basically how government, through the Taxation Department and Treasury, deals with you.

This hearing is meant to be informative. We welcome members of the Treasury, Bob Thompson and his people, who are to my left and over by the window. We thank him for coming here to listen to your remarks.

I think it’s important to begin this hearing to remember that-- We tend to remember and think of the way government interacts with us with our last, worst experience. And sometimes we forget the difficulty that the bureaucracy has when they have to deal with us. We are a large state, eight million people, many businesses, many entities, and, quite frankly, the people who work for Treasury and all of our other departments are hardworking citizens that normally live right next door to us.
So I would hope that we think about that when we come up and testify today. We do want to find areas that we can improve upon. That is our goal, and I’m sure it is also Treasury’s goal, to walk away from these hearings with better ideas, with a better view of, perhaps, the actual interaction at the level of the individual, the business, or the public entity.

So with that beginning, I would like to give an opportunity for my members to introduce them to you and the areas of the state that they represent, if you would as well, so some of you folks who are testifying will know the geography of the members of the Committee.

I’d like to begin with my Vice-Chair, to my left, Kevin O’Toole.

ASSEMBLYMAN O’TOOLE: Good morning. I’m Kevin O’Toole. I’m the Vice-Chair. I’m happy to be here. I want to thank Guy for arranging this meeting. I’m sure we’re going to see many meetings like this throughout the next couple of years dealing with the individual departments and finding out how we can best serve our constituents. I represent Essex County and Union County. I also serve as the Assistant Majority Leader.

ASSEMBLYMAN CARROLL: Michael Patrick Carroll, 25th District, Morris County.

ASSEMBLYMAN GUEAR: Good morning. Gary Guear, 14th District, parts of Mercer, parts of Middlesex.

ASSEMBLYMAN GUSCIORA: Good morning. Reed Gusciora, 15th district. I represent communities along the Route 1 Corridor, from Trenton to Princeton. And I welcome you to the 15th District.

ASSEMBLYMAN GREGG: Thank you very much, members.
At this point, I will give just a little more information on how we're going to be working today, and then we'll begin the testimony. Treasury has reminded me that you may be testifying on issues that have certain privacy issues. If, at the end of your testimony, you wish to confer with the Treasury, again, they are over to my left and your right. And you can do that in a private manner. If, at the end of your testimony, you would like to have your issues specifically be able to come to this Committee for this review, we have a waiver form that Treasury will have that you can go over and will help you fill out, so the Committee can have access to your complete record through Treasury and to us. So you'll have a couple of options there.

With that said, we will begin the hearing. And the first individual is Dan Murphy. And I will also remind everyone else, while Dan is coming up, we have a space-age microphone system here. So if there are too many red lights on the board down there, ours will not work up here. So the red light must be on for you to be able to be heard. And the microphone -- the tape recorder's -- for the recording individuals will continue.

So at this point, Dan, I'm going to turn my light out so yours will come on.

**D A N   M U R P H Y:** I'm on.

Mr. Chairman and members, thank you very much for the opportunity to address you and basically tell you what a lot of us within the industry have gone through.

To qualify myself, my name is Dan Murphy. I have been in food service since 12 years old. I'm now 56.
ASSEMBLYMAN GREGG: Dan, you can sit down and relax. We’re not that formal here.

MR. MURPHY: I’m trying to relax.

I’ve had Danny’s Italian Restaurant, now Danny’s Steak House, for some 30 years. I was a board of director with the New Jersey Restaurant Association, and I sit on just about every board going in my town and my community and have been a player in developing my industry for years. I was on the Drunk Driving Task Force for 12 years.

Approximately three years ago -- if I can prefix it with the fact that I went from being an Italian restaurant--

ASSEMBLYMAN GREGG: Dan, is your red light on? (referring to PA microphone)

MR. MURPHY: Now it is, sir.

I went from being an Italian restaurant for 25 years to a steak house some five or six years ago. Red Bank became very popular. We went from 17 restaurants to 73 restaurants within one square mile. And in order to compete, you must be very competitive and change. And I turned Danny’s into a steak house at that time.

It was a general conception within the industry that we had heard horror stories that we were going to be -- that a sales tax audit was going on, and that it was the-- And once again, this is what we heard within the industry, that it was the job of the sales tax department to come in to find out -- find as much money as they possibly could that we were stealing or taking or not reporting.
As in any industry, I know there are people that are not honest. Any industry, I don’t care what it is. But the majority of my people out there, especially private sector restaurants, such as myself -- we follow the rules. And you have no choice but to do that in today’s economy. What we were told was basically that we’d get a sales tax audit at some point and that, regardless of what your numbers would be or what you showed, they would come back and say, “Listen, you owe $40,000 or $50,000,” and you would settle for a certain amount of money. And it was the perception that this was a tactic to raise money for the State of New Jersey. That’s what we were led to believe. I have always felt that if I followed the rules and do everything just so, that unless I made some stupid mistake and it’s my fault, that I’m going to follow the rules and do everything properly.

I received a notice that I was going to be -- have a sales tax audit in June, two years ago. And one of the things I had to do was everything that was on this list. All the records for approximately three to four years, they wanted. And that goes-- Well, I can pass it around to you because it’s pretty extensive. And what I did was I eventually got in touch with a Mr. Remi Inekuna who was going to do my sales tax audit. And I called him ahead of time and asked him what did he need. And he gave me a list over the phone of what I needed.

I asked him how long the audit would last for because I have a restaurant that seats 77 people and 30 at the bar. That’s it. That’s my total seating. And I live over the restaurant. I have an apartment upstairs. And if he needed a space to work, I couldn’t have him in the middle of my dining room, nor did I necessarily want someone “in my living space” for a week, two
weeks, three weeks, or a month. He told me it would be anywhere from two
weeks to two months.

I worked out a thing with the local Count Basie Theatre where I
had a space for this gentleman. And my accountant, Steve Sorgente, I made
available because I wanted to make sure that nothing came back at me that I
didn’t know about or didn’t expect.

So my accountant, Mr. Steve Sorgente, and myself met Remi in
June, and I brought him to this big room, and we had there, literally, 15 boxes
of checks, records, accounts, everything we could possibly do. And for the next
two weeks, my accountant was sitting there with him.

Whatever he needed, whether it was a bill, a (indiscernible) checks.
I also prefixed it. I said, “Listen, I want to show you a little about my industry
so you know what I do.” I showed him pictures of the meat market in New
York where I go and buy meats. And being a dry-aged steak house, or if you’re
selling any fine foods-- There’s a difference between a fast food chain, where
everything comes in, every single thing is accounted for, everything is
prefrozen, prewrapped, to a restaurant that serves good food, to a restaurant
that serves a dry-aged product or seafood, where you have a tremendous
amount of waste.

I explained to him right off the bat. I said, “Remi, I want you to
understand with the meats, as you’re looking at these bills, that when you dry
age a steak, you lose 15 percent of the gross when it dries. You also cut away
all the fat and bone that is around this product. And what you’re left with is
about 50 percent of the original product.” Okay. I said, “That is cut into
steaks, and that is what we sell.” And I went through that. I went through
every glass in the bar. There was also three different pricings, from happy hour to times when we have entertainment. And I gave him absolutely every possible detail I could.

So for two weeks, he ran through the audit. At the end of two weeks, I received -- actually, it was about a month or so later, because the total audit lasted six months. And he handed us this sheet, and on it all these pages -- I don’t know if you can just see the fine print. I had it blown up at a photographer’s studio so we could work with it. But it was 50 invoices of every -- 10 for master purveyors, 20 from this. And there’s approximately 46 on each page. And he wanted us to calculate out all six columns of this -- of all these pages. It comes out to 4500 functions -- is what we had to do.

In other words, I sat down with my cooks, my accountant, and bartender and made him go through every -- all of these. And they literally had to factor out what the cost of each item would be, right down to the last ounce.

At this point, I probably should have called a supervisor or asked for help, but I was determined to go through this audit. By this time I was committed.

We filled in all the information. We gave him absolutely everything he wanted. Six months later, he walked in the door and sat down and said to me, “You owe $125,000.” If he had said $20,000, I’d have been upset. He said $125,000. I was incensed. One hundred and twenty-five thousand dollars. I looked at him. I said, “Do you understand what you’re saying? One hundred and twenty-five thousand dollars, in sales tax, comes out to $2 million a year that you’re saying in the last three years I have not reported. Where’s my yacht, where’s my car, where’s my plane, where’s my
girlfriend dripping with furs? This doesn’t make sense.” I said, “You’ve got--” I said, “You’re also saying that I stole this money, that I didn’t pay withholding tax or income tax on over $2 million. My business seats 77 people, and you’re saying that I stole $7000 a week out of this place every week for three years.” I mean, I was no longer upset. I was no longer nervous. I was no longer worried. Now I was just angry.

I called a sales tax attorney and my accountant. I met with them. I spent about a month-- Remi, at that time said, “You must sign this.” I said, “I’m not signing anything.” He said, “If you don’t sign this, it automatically-- you are guilty and must pay the fine.” So I signed the document, which was the right, I guess, to go before a supervisor.

At this point, I want to thank the other side of the Division of Taxation, which is the senior members that have been in this industry for years and know about it. There are three key figures that played a part: Mr. David Levine, who is in the Sales Tax Division; James Bandura, who later on helped me with advice, showing us what to look at; and then the supervisor, who came in the door some seven months after this started, and it was Thomas Coughlin.

And he walked in the door, and on the bar I had set up an entire short loin, which weighed 28 pounds. I had it-- Next to that-- I had it laying on the table with all the beef and fat cut off it and then cut into steaks. I had every dish that I serve in the restaurant -- was wrapped in cellophane and on the table so he could see the weights and measures. And I said to him, “Mr. Coughlin, this man does not understand food waste. He doesn’t understand. I don’t know what his numbers are based on.”
Mr. Coughlin looked at the restaurant. He went to the point of sale machine, which I had for five years. The point of sale machine records every single drink and every food item that we sell or record. It is much easier to keep track of it that way than to have it lost or stolen or to have people not write it down. Your employees will lose a ton of money on you if you don’t have that.

And he looked at the point of sale machine. He asked me what our procedures were. All the records were right there. It was taken off onto a daily sheet. The sales tax was computed at the end of every night. And we were up-to-date and current on our sales tax.

At that point, he said to me -- he said to Remi, “You go back to Newark. I’ll finish up with this.” And he sat down and said to me, “At this point—” He said, “Truthfully, I’m sorry. Had myself or some of the people who have been in the industry for a long time walked in and looked through this, this would have lasted two to three days, maybe a week.” He said, “At this point, from all of your records,” he said, “you don’t owe us anything. There’s no point in pursuing this.” And I said, “What was—” And he said, “I have to tell you,” he said, “when I asked my tax man what he based his figures on, he just kept saying, ‘His number’s too high.’ What did you base the final $125,000 on? ‘His number’s too high.’ What formula did you base it on? ‘His number’s too high.’”

My industry, like your industry — the Taxation, has great employees and people that really know their stuff and are there and willing to help you. And then you have people, unfortunately, that you hire. I have bad people in my industry — when I say bad people, they’re not well learned in the
industry -- that are given a set of guidelines to follow. And if you’re dealing with a liquor store that buys $100,000 worth of -- cases of beer and can’t show where it is, that’s a definite. But if you can explain to someone that we have food costs, spillage, weight that’s thrown away-- I mean, my industry -- private sector restaurants are basically at the mercy of an auditor who feels we’re hiding something, that feels -- that doesn’t understand what we do with food, that if you buy a salmon that weighs 10 pounds, you only wind up with maybe 5 pounds of product that you sell.

At the end of it, I spent $5000 to $6000 in legal fees and accounting fees. You must realize that in my industry today, in order to come up with $5000 or $10,000 in profit, you’ve got to do $30,000, $40,000, $50,000, $60,000 — I don’t know the numbers -- $60,000 or $70,000 in sales to generate $4000 or $5000 “in profit,” or money that we use to pay our bills with. So if we lose $5000, $10,000, or $20,000 in a sales tax audit, we’ve got to generate $80,000 to $100,000 in sales to make up for that. If we’re guilty of it, we deserve to pay it. And there’s a lot of people in the industry -- a lot of times where people haven’t done the right thing, either by mistake or on purpose. But when everything’s in front of you and all the paperwork is there and everything is there and we’re cooperating 100 percent, I, or anybody in my industry, should not have to go through that six months.

I have to tell you, from the time he hit me with that number until the time I finally talked to Mr. Coughlin, I’d wake up in the middle of the night because my whole-- My life, as far as I was concerned, was in jeopardy. My business-- I mean, what happens if I wind up in court for two years? How do I pay those legal fees? I mean, it just goes on. So you’d wake up in the
middle of the night in a cold sweat, thinking how in the world did I get into this position, and will I get out. And once again, when--

I just have to call attention to the good guys. There was Mr. Gold with the ABC years ago, who we used to call for any question within the industry, and he knew it. He was one of those guys who just knew his industry backwards. And Mr. Gold eventually retired and/or passed away, and years later, the same agent -- some of the agents we talked to reminisce on how much he knew in his industry. We need more Mr. Golds in all avenues of the State Department. You need to hire people that really know their industry and are well-trained.

That’s it. Thank you.
Any questions?
ASSEMBLYMAN GREGG: Press your button again, please, Dan.
(referring to PA microphone)
MR. MURPHY: Nope.
ASSEMBLYMAN GREGG: Press your button again.
MR. MURPHY: Are there any questions?
ASSEMBLYMAN O’TOOLE: It’s a sobering account to sit here and listen to what you’ve gone through. And this is precisely why we want to have the regulatory oversight. And I want to, again, commend the Chairman for not only being the Chair of this new Committee, so to speak, but also to have the insight to put together a meeting like this where you can have a forum, and we can hear from you, be educated from you, and hear the concerns that are not only in the industry, but that are affecting residents day to day who are – whether-- You’re in Red Bank. I’m up in North Jersey. I’m
just as concerned about your plight as I am at somebody that resides in my home county.

And it’s frightening to think that this happens in America and it happens in New Jersey, where, apparently, an uneducated individual, outside of the expertise needed to do the audit, has come into your restaurant, kind of like a gestapo, and basically said, after doing what was supposed to be a two-week audit to a six-month audit, and at the end of it says you have a $125,000 tax bill. I mean, think about that. He’s calling you a thief, really.

Here’s my take on it. I think that -- and audits are part of our lives, whether it’s our personal income tax, Federal income tax, whether it’s restaurants or businesses. And we’re all going to, at some point, come under that scrutiny by a random check or whatnot. I have no problem with that. And I think those people who engage in what I perceive to be sloppy bookkeeping should be reprimanded and fined accordingly. But for those individuals who are deceptive and deliberately misleading and steal the sales tax, those people should be prosecuted and put into jail.

And the flip side of that, for those people who are doing the audit, they should be trained, they should be competent. But for this Mr. Coughlin coming into your life -- you’d be looking at a real, real problem. And where are you going to come up with this -- small business owner come up with $125,000. They’re saying you stole $2 million over the last three years, $7000 a week. I mean, it’s outrageous. So I’m happy to hear that there was a result that was favorable at the end. I’m unhappy to hear that you had to go through the hell that you went through and had to pay $5000 or $6000 or $7000.
So maybe part of the problem, and maybe we can hear from Treasury some other time-- First of all, if this individual -- if he has another side, I’d like to hear it. And number one and number two, is there a way that, if we’re talking about a specific industry where there is an expertise, whether it’s the salmon waste or the aged steak -- 15 percent or 50 percent runoff.

Maybe when we’re doing these audits, Mr. Chairman, we should have somebody that’s trained, perhaps, in the industry, or has some knowledge and some specialized training so they can appreciate what you’re going through and what your losses are and just some cold accountant coming out and saying you owe $125,000 because your numbers are too high. I just don’t think there’s a natural fit there.

And if you don’t mind-- If you could just pass that binder up, I’d like to take a look to educate myself through some of the process of what you’ve gone through.

But having said all that, I’d like to hear from Treasury at a later time, either today or another hearing, as to how a case like this actually occurs. And maybe we should have the Coughlins of the world come in at an earlier time, when they see the audits reaching beyond the projected two weeks to two months to six months. At some point, maybe, a supervisor has to step in and say, “Well, what’s going on right here?” But I’d like to hear from Treasury.

MR. MURPHY: May I-- If I may state, there’s a part of this, too, that if we have someone who is new to our country, his culture is different from ours, and we must understand his culture and let him understand ours.

ASSEMBLYMAN O’TOOLE: No, I wasn’t aware he was from a different country, and frankly, I don’t care if he’s from another country or
from our country. If he’s an employee of the State, he’s held to the same standard as the rest of us. He has to be educated and fair. And if there’s a problem, in terms of communication, that’s incumbent upon the supervisors and Treasury to make sure that that communication gap has been bridged.

MR. MURPHY: May I say something?

I have found that anyone in the upper levels of the Taxation Department are always very accessible, are more than willing to explain what we need and what we need to do. And if I were going to make a recommendation -- how it works -- I would have the Mr. Coughlins and Banduras and Levines-- Let them go out and do a quick spot-check. And if there’s a glaring error -- if it’s obvious that something’s wrong after a couple of days -- then send in someone to do the mechanics. I don’t know if that’s possible, given the sheer number of restaurants and the size of the Division. But I do know the upper echelon of this industry has always been incredibly accessible to us. And I don’t feel harmful -- it’s when someone walks in that’s relatively new, has been trained on what to do and cannot bend or understand a different concept within this industry.

That’s it. Thank you.

ASSEMBLYMAN GREGG: Thank you, Mr. Murphy.

I share my Vice-Chairman’s thoughts on this issue. And your testimony has been very valuable. If you would like to sign a waiver form for Treasury, your documents, then, could be forwarded to the Committee, if you would like to do that.

MR. MURPHY: Sure. These are just notes that I took, but I’ll be happy to let you go through them.
ASSEMBLYMAN GREGG: Thank you, Mr. Murphy.

I have noted provisionally that former Congressman Michael Pappas has entered the room. And I will give him the privilege to step up at this period of time. I understand he has testimony.

So, Congressman, come on up.

MICHAEL PAPPAS: Which button do I press? (referring to PA microphone)

ASSEMBLYMAN GREGG: The red button.

MR. PAPPAS: Thank you, Assemblyman and members of the Committee.

I did not come prepared to speak, but I would just like to offer my best wishes to you folks embarking on a very important mission. Government is there and here to serve, and you folks are public servants and, I know, take your responsibilities very, very seriously. Too often, there are unintended consequences to some regulations that are compiled, sometimes, over a period of time. And well-intentioned people, even public officials and staff, can end up putting small businesspeople in situations that I don’t think anyone would ever intentionally want to see take place. For those that may intentionally want to see some terrible things take place, well they need to be held accountable, as well.

And I wish you all the best in this important effort that you’re engaged in and beginning today. And I wanted to be here today, just to tell you that someone like myself and literally thousands and thousands of other people throughout our state are very pleased that the leadership established
such a Committee. And I certainly would hope that at some point, maybe in the future, I might be able to come and participate in a more meaningful way. Thank you for the opportunity.

ASSEMBLYMAN GREGG: Thank you, Congressman. And I would certainly like to note Congressman Pappas’s fine work on working on estate taxes and his time in Congress.

One of the real egregious issues we have in our country and our state is the issue of estate taxes, where small businesses are forced to sell through their families, after inheritances, because they don’t have enough money to pay the taxes to maintain a family business.

And Congressman, I know your efforts were well appreciated, and we thank you for that. Thank you for being here today.

MR. PAPPAS: Thank you very much.

ASSEMBLYMAN GREGG: Martin Davidoff, CPA.

Welcome.

E. MARTIN DAVIDOFF, CPA, ESQ.: Would anybody like some wine?

ASSEMBLYMAN GREGG: Mr. Murphy, did you leave a wine list up here?

MR. MURPHY: Yes, in case you’re ever in Red Bank.

ASSEMBLYMAN GREGG: If that was meant to be a bribe, it’s not quite noon yet, but when it gets to be noon, perhaps, we can start.

Mr. Davidoff.

MR. DAVIDOFF: My button doesn’t seem to be working here. (referring to PA microphone)
ASSEMBLYMAN GREGG: I’m out of control here.

MR. DAVIDOFF: Good morning. My name is E. Martin Davidoff. I’m a CPA and a tax attorney on my own account. I am a member of the National Federation of Independent Business, NFIB. And on a couple of the items I’m talking to today, I will be talking as their tax chairman.

First of all, I’d just like to make a comment. Dan’s observation as a professional -- works with the Division of Taxation -- Dan’s observation about the upper level being excellent is absolutely true. We have some very fine people there. And his problems with the lower level are also -- from time to time, also true. As a professional, we know -- we have a quick trigger. If we see a problem, we immediately ask for the supervisor. The Tom Coughlins of the world are really excellent people, and they’re very reasonable. And they do justice to us, in terms of dealing fairly with taxpayers and being effective in collecting revenue for the State.

I have six items I’d like to speak on. You all have a summary of my testimony, I hope -- Is that correct? (affirmative response) -- along with detailed backup. I’d ask the Chair, if I could, please make sure that all of the items are included in the record.

ASSEMBLYMAN GREGG: They will be.

MR. DAVIDOFF: Thank you very much.

The first item, and this is an item -- if you pull out your hot pink sheet, it’s basically about my button here -- (indicating) Tax Equity Now. And this is tax equity for small businesses.

Many small businesses, such as myself, provide fringe benefits to their employees, such as pension plans, medical. We also pay Social Security
tax on our employees. And for this, the government, both the Federal and the State, say that we can take a tax deduction for that in arriving at our taxable income.

However, when it comes to paying for Social Security on ourselves and paying for pension plans for ourselves, the State of New Jersey, because it’s a gross income tax state and because of the way that the Federal government allows the deduction on another part of their form and not on the proverbial Schedule C-- In New Jersey, you do not get a deduction for a contribution to your Keogh Plan. You do not get a deduction for paying the one-half of your FICA taxes, your self-employment taxes. Each individual pays 15.3 percent. So I urge this Committee and the Assemblymen and the members of the Legislature and the Assemblywomen to please introduce legislation that will eliminate this equity.

And I have enclosed, as part of this, a -- under the pink sheet, “Small Business Needs Tax Help”; a comprehensive article that describes all of that. You will also notice, on the back of the pink sheet, computations that basically say that a sole proprietor, in the exact same economic situation as an employee or as an owner of a C Corporation, pays 63.7 percent more in New Jersey gross income taxes. This is based on 1997 tax rates, but it hasn’t changed significantly. And it’s something that is really important.

So that’s the first topic.

Mr. Chair, do you want to take questions after each topic, or would you like me to go on through all the topics?
ASSEMBLYMAN GREGG: The members are free to ask questions at any time, so at this point, I think, they will wait until you complete your testimony.

MR. DAVIDOFF: Okay. Thank you very much.

The second topic – if you turn, there’s an editorial in the October 21 Metuchen-Edison Review, followed by three pages of materials that talk about, basically, New Jersey’s tax rates. They’re not indexed.

As you know, the Federal tax rates-- Each year, the brackets are indexed. As inflation eats away at our pay, the bracket for the 15 percent in the Federal is increased to be wider, based upon inflation. New Jersey does not do that. As a result, the State of New Jersey is putting forth a tax increase on all of its citizens that amounts to about several hundred million dollars every year.

If you take a look at some of the materials, you’ll see that basically from -- in a two-year period, the gross income tax went from $5.6 billion in revenue to $6.8 billion. Now, part of that was due to capital gains and a strong economy. Good for you. You guys have been doing a good job. However, part of it was because what’s happening here was bracket creep. That is, people going from-- And I’ve given you actual detailed examples. And in one example, during a 10 percent increase in taxes, somebody with gross income of $85,000 -- a family of four -- had a tax increase of 28 percent. Well, if my income goes up 10 percent, my taxes should go up 10 percent, not 28 percent. Similarly, a single individual goes through -- making $42,500, their taxes go up 32.7 percent when inflation eats away 10 percent.
These are incredible numbers. And it’s a tax increase not just for small business. It’s for every individual in this state. And if you need to raise more taxes, do it affirmatively, not through a hidden tax increase.

I ask you to do now -- to do this year, for this budget -- is to index the brackets, index the exemptions, index deduction for real estate, and to implement that as a change in tax law going forward. That’s the end of my second topic.

The third thing is, and this gets a little bit technical, but there’s -- towards the bottom, the next to last page in the package -- allow for unrestricted claims for income tax refunds.

If I have an assessment by the Internal Revenue Service and I pay that tax, I have two years to file a claim for refund, under any circumstances. There are no loopholes, no problems, nothing I have to jump over other than, within two years of the payment, I file a claim for refund. And the claim would be based upon some theory that I paid it erroneously. In New Jersey, that’s not the case. Now, although there’s been a significant liberalization with allowing some refunds, it’s still not all the way. I’m asking you to make the New Jersey law parallel to the Federal.

I’ll give you an example. In the State of New Jersey, if I’m hit with an assessment of $25,000, for example, and I give it to my accountant, and he says, “Oh yeah, I’ll get to it,” and then he doesn’t file, within 90 days, a protest, I have lost my right to go to the New Jersey Tax Court, plain and simple. And that’s similar to the Federal, and that’s fair. But in the Federal rule, if I pay my $25,000, whether I pay it today, tomorrow, three years from
now, whenever I pay it, with interest and penalty, normally, I would then have two years to have an appeal on the merits and claim a refund.

In New Jersey, if you don’t make that payment within 450 days, one year and 90 days from the date of the assessment— If you don’t file that claim— If you don’t make the payment of tax because you don’t have the money, let’s say, all right, and then three years later the IRS finally says, “Okay—” not the IRS, the Division of Taxation finally, as it should, collects the tax, you then have no recourse, you cannot file a claim for a refund. And this is very unfair.

First of all, people have to learn two sets of rules. You have the New Jersey rule and the Federal rule. Second of all, people may not have the money to pay the tax. And often, it’s not their fault that that 90 days slip by. Sometimes, it’s even the Division of Taxation’s fault. And I’ve had some cases overturned strictly because the Division of Taxation mailed it to the wrong place, mailed it to the wrong person, didn’t provide their rights. So it’s not really a Division of Taxation problem, it’s a law problem. And you, as the Legislature, can eliminate this administrative problem by saying, “We’re going to follow the Federal rule. We’re going to give you two years to file your income tax refund claim and get a hearing on the merits.”

The other thing this does, in reality, and this is really the important part— During that period between when you’re assessed a tax and when you pay it, if they know that you always have the right to claim a refund, the State of New Jersey will develop some sort of administrative procedure to informally hear your case. That’s what the Internal Revenue Service has done. They know that if eventually you pay the tax and then you sue them for a
refund, well, they might as well listen to you now. And if there's any way to resolve the case at a lower level, let's do it. And this is a way, even for somebody who has missed the 90 days, at least, to get an informal internal review of their case by the higher-ups in the Division of Taxation, who we already said are very reasonable people.

The next item, Offers in Comprise. A lot of you have heard of the offer to compromise program in the Federal government. They are now doing, within the State of New Jersey, over 300 cases a month. New Jersey, based upon the information I have, is doing from 25 to 30 cases -- 25 to 50 cases a month, far fewer than the IRS.

And the reason is fairly simple, and it's outlined on the last page of your program for your reading. It's really very simple. The IRS says, "We're going to collect as much money as we can." Their process says, "Let me look at your gross assets, not your net of liabilities, your gross assets. We're going to take them -- not take them, but we're going to count them as a minimum number you have to give us for the offer. We're also going to say, 'How much can you make in the next four or five years. And we're going to take the excess number you have, we're going to add it up, and we're going to come up with a number. We want you to give us more than that number.'" That number that they come up with is what they call collection potential. And if you give them more than that number, why should they chase after you? If you're going to voluntarily come forward and say, "They determined--" Let's say you owe $20,000. They determined you can pay $10,000. If you offer $11,000, they will accept it. And they determined it strictly on collection potential.
Now, they investigate your veracity. They make sure that you’re doing all that you’re supposed to do. But let’s say you owe them $100,000 and your collection potential is $10,000. The IRS will still take $11,000. Let’s say you owe them $1 million. Will they still take $11,000? Probably, but, of course, you’ve got to be very careful that that really is your collection potential. They may be more careful in making the determination, but the philosophy is the same.

When you go to the Division of Taxation, they have adopted, to their credit, an informal offer and compromise program through their closing agreements. And they do it a little bit differently. They do look at collection potential, but then they look at the amount of tax. So if I have a taxpayer who owes $100,000, and their collection potential is $20,000, and maybe they owe another $50,000 in penalties, so they owe $150,000 in total, the State of New Jersey says, “Give us $100,000. We’ll do the deal.” All right?

And as you know, Offers in Compromise are nothing short of means tested amnesty. They’re amnesty for people who got in trouble, are trying to straighten their lives out, and are trying to go forward. And it’s means tested because you’re looking at what their means are and what they have to pay. Unlike the amnesty you gave before, which if the guy had $1 million in the bank, and he owed $150,000, you were going to let him pay off $75,000 or $80,000 at some point. This means test-- And it makes sense because you’re going to maximize your collection, and at the same time you’re going to give people some freedom.

However, back to my case. The person owes $100,000. They have collection potential of $20,000. New Jersey, 99 out of 100 times, is going to
say no to a $21,000 offer. All right? And they’re going to say, “Give us the tax.” And you’ll say $30,000. And they’ll say, “Give us the tax.” And they won’t -- they usually will not relent until you give them $100,000.

So what’s the choice to the person who can only, realistically, come up with $20,000 or $21,000 or $22,000? The choice is that person lives for 20 years, he pays them nothing or he makes himself judgement proof. And for 20 years, he lives under the cover of having a New Jersey tax judgement against him and can never get free. And New Jersey, in most cases -- in those kinds of cases, if you’re dealing with people who are basically honest, they’re not going to collect the revenue.

Now, understand-- The rationale I’ve heard for the New Jersey policy is, “Well, most people lie the first time they give us their financial information.” And as Assemblyman O’Toole indicated before, “Hey, if you’re lying to us, let us give the full wrath of the State.” All right? That’s not what-- We’re not looking to help those people. We’re looking to help people who got in trouble, ran a business, got over their heads, couldn’t pay the payroll, so they said, “I’ll pay the payroll instead of the sales tax.” Wrong to do, but nevertheless it’s behind them now, they’re going forward, and they’re trying to get right.

You need to provide legislation or work administratively with the Division of Taxation, give them encouragement to change their focus of the Offers in Compromise program.

The next item, and I’m almost done. First of all, I want to tell you that when I heard about the State of New Jersey pulling trucks over on the side of the road from people out of state who are, on a frequent basis, coming to
this state, making sales, and not paying sales tax, I, as a taxpayer, said, “This is terrific. They’re protecting the revenue so that I get to pay less in taxes.”

And I think when you have a New Jersey Division of Taxation that has tried creative ways of collecting the tax through even the amnesty program, although I hope you don’t have another amnesty program — I don’t think that would be good for us — but through out-of-state vendors, through enforcing the tax laws against people who are not reporting income, through having programs where they can match what people buy and their cost of goods sold. These are good programs. Yes, they have to be applied with some reasonableness, but when you have people who are clearly not obeying the law, it’s good to know. It gives a taxpayer a good feeling and says, “Hey, you know what? The tax cheats aren’t winning because you all know you go to the cocktail party and they say, ‘Well, I beat the IRS on this, or I beat the IRS on that.’” And if you find people who are being more straightforward and there is a change in attitude, maybe we can lower taxes further because we’re going to collect taxes. We’ll get more compliance, and everything will be better.

Finally, partnership returns were included in 1993 legislation with the S Corporation for New Jersey, legislation that I wrote in conjunction with Phil Laloya, who just walked out of here before, and Harriet Durman. In any event, part of that was to require partnership tax filings in New Jersey. Although, and I don’t have any statistics in front of me, the sense that I have is there is more cross matching that can be done with those partnership returns to make sure that out-of-state residents are indeed paying their fair share of taxes here in New Jersey.
In addition, I think more can be done to make sure that out-of-state partnerships -- maybe cross-referencing with Secretary of State files, maybe cross-referencing with property ownership files -- more can be done to make sure that all the partnerships are indeed filing tax returns. Every time there is a sale of property, for sure, we should be having some cross matching with the owners, and if they’re out-of-state, we should make sure that we’re collecting the revenue. Pennsylvania does an excellent job of that. We should emulate that.

And I’d like to thank you all for allowing me to appear today. I certainly-- I just wanted-- Just going back to my first topic about the tax equity for small business, that is a topic that has been approved by our leadership council for the NFIB. And I’m very happy -- pleased to be here, and I’ll be glad to answer any questions that you have.

ASSEMBLYMAN GREGG: Members? (no response)

You were very thorough, Martin. I don’t think anybody on the Committee has a stronger opinion about subchapter S than I do, for those of you who followed that issue and the pocket veto of that bill. But I suspect it will come up again. Your points of view are in writing and well done. And we will take them under advisement.

Thank you very much for time today, Martin.

MR. DAVIDOFF: Thank you very much, Mr. Chairman.

ASSEMBLYMAN GREGG: Next is Tim Howes, NFIB.

TIM HOWES: (Speaks from audience)

ASSEMBLYMAN GREGG: Would you like me to go the next, Tim?
You’re up. And let me remind you to please introduce yourselves when you come to the microphone and the company or entity that you’re representing.

M R. HOWES: Does the light need to be-- (referring to PA microphone)

ASSEMBLYMAN GREGG: Red light should be on.

M R. HOWES: My name is Tim Howes, and I’m the Chairman of the National Federation of Independent Business State Trust. My other hat is as Borough Councilman in the Borough of Peapack and Gladstone, which is in Somerset County -- northern Somerset County. Almost in Mr. Carroll’s district, but not quite. And I’m here as the Borough Councilman to address one item that, in my investigation -- in my time, has come up.

My auditor advises me that there may be a bit of a move to change the way that municipalities keep their books. And they currently are under one system, which is essentially a cash-based system. There has been a move, from time to time, to move to Generally Accepted Accounting Principles. And the municipality -- our municipality, which is a small municipality of 2100 people with suburban and rural areas with one major ratable, it would have-- It would not have a positive effect to make that move, so we’d really oppose -- if that were to come up in this session, we’d oppose that.

The current method -- the acronym is even too long for me to remember. I mean, it’s like a 19 letter acronym, so I can’t remember it. It’s a more conservative system. It allows for a projection for the coming year in your budget, based on receipts from the prior year. GAAP, Generally Accepted Accounting Principles, would allow for projections based on other things --
more projected revenue, which would come into play if there were a new assessment.

Now, this was particularly important in our own case. We have a major ratable, which takes up about 35 percent of our tax rolls. Beneficial finance, which is now Pharmacia and Upjohn’s headquarters, for instance, was assessed at one value. It’s most recent assessment-- And to say we had our heads handed to us in tax court and lost about half of that in tax court would be to use a euphemism.

Had we been using Generally Accepted Accounting Principles, the projection for the following budget year may have been way overstated, I mean, way overstated. And if spending had gone along those lines, as even local government tends to be tempted to do, to say well, “We won’t be raising taxes, let’s go ahead and spend this money,” -- it’s not my personal preference, but it’s what tends to happen. That would have caused, in a town of 2100 people, a major tax increase the following year.

The current method tends to be a little bit of a check on that tendency and would prevent such situations. So that was, after my little investigation -- after receiving, Mr. Chairman, your letter inviting various testimony -- that was the main issue with the municipality and the Department that came up. Otherwise, I’m advised, things seem to go fairly smoothly with the Department, and I’m happy to hear that.

So other than that, I’d just like to wish the Committee well. I think it’s a great new addition to the State government. And good luck to you. If there’s any questions--

ASSEMBLYMAN GREGG: Thank you, Tim.
Any members have questions on this issue? (no response)
Thanks a lot for taking the time.
MR. HOWES: Thank you very much, Mr. Chairman.
ASSEMBLYMAN GREGG: Kevin Monaco, Bill Foelsch, and Jim Marturano. And again, if you could introduce yourselves and who you’re representing.

KEVIN MONACO: Thank you, Mr. Chairman.

My name is Kevin Monaco. I’m the Director of Legislative Affairs for the Utility and Transportation Contractors Association of New Jersey. The Utility and Transportation Contractors Association represents approximately 1200 member firms, primarily small businesses around the state involved in heavy highway utility construction, environmental remediation construction, as well as park development and park construction.

With your indulgence, Mr. Chairman, we’d like to have Mr. Marturano, who is a member of our Association, begin our comments.

ASSEMBLYMAN GREGG: Fine.
Welcome, Jim.

JAMES P. MARTURANO: Thank you.

My name is Jim Marturano. I’m the President of Marturano Recreation Company, which is actually a small business located in Bricktown, New Jersey. The business was started in 1974 with two employees, and we currently have 30 people full-time. We’re also affiliated with a construction company, World Construction, which is located in Atlantic Highlands, New Jersey, and they employ 20 people.
We design, sell, and install all types of playground equipment, site amenities, shelters and gazebos, and sports lighting. To give you an example of the type of work we do, we just completed the new playground at Liberty State Park. It’s actually the biggest project we’ve ever done, and one of the largest playgrounds installed in the whole United States. And that was done for the New Jersey State parks department. We provide services to hundreds of municipalities, school boards, state agencies, and county governments.

I appreciate the opportunity to speak to you this morning, because I feel that this meeting -- this hearing is the proper forum to discuss a major policy change that is taking place in Treasury that could severely damage many small businesses in New Jersey.

I currently am the Chairperson of an industry coalition. It’s the Park and Playground Suppliers Equipment Coalition. This coalition was formed because of this policy change by the Treasury. It’s comprised of 12 vendors, all small businessmen like myself, throughout the state. Together, we collectively do over 90 percent of the playground business in the state. We’re all extremely concerned about this policy change. We have met with the Treasury Department. We have met twice, and our next meeting is scheduled for March 15. However, we’re not sure if we’re going to be able to solve this -- have a solution. And it might have to come before the legislators. And that’s why I felt it was important to speak to you this morning.

Just to briefly outline the issue, due to some recent court cases, the purchasing department has started a process of potentially eliminating multivendor contracts. We feel that, in response to these court cases, the
purchasing department is taking a narrow view when permitting multivendor contracts to continue.

The current contract -- State contract for park and playground equipment is due to expire in April. We have been informed that it will be extended until July 31, and at that time it will end. In our industry, playground and park equipment, July 31 is in the middle of the season. We will be either left without any contract or, even a worse scenario, we will be given a contract with one vendor.

There are numerous reasons why we need multivendor contracts. And just to list a few-- When the towns or the schools or the counties go to purchase the equipment, they should have a freedom of choice. The State contracts now provide vendors that the State has approved. They’ve approved the brands of equipment, and they’ve certified that the prices are the best prices possible. This allows the towns and the people the freedom of choice to pick the ones that best meet the needs of their situation. It also provides for direct property tax relief, because without these contracts it means that every time these people want to buy playground and park equipment it will have to go out for bid. They will have to develop specifications, go out for a bid, review them, and then award them. This also will open them up to legal cases when bids are challenged.

It’s important that they have a choice of variety of items. If there is only one playground that can be purchased under the State contract, that means if you want to buy a playground in High Point, New Jersey, Princeton, Asbury Park, or Cape May, you will be forced to buy that one type of equipment, that one playground. We believe that everyone could be best
served if the State would provide a list of approved vendors who can supply a variety of equipment.

Our industry, we feel, would be devastated if this type of contract went to a single vendor. My own company does about 85 percent of our business under State contracts. And the Coalition, as a whole, when surveyed, does over 80 percent of their business.

We don’t feel that any of us could survive with a single vendor, and we don’t feel that any single vendor could adequately supply the equipment and services as needed in the state. And of course, the worst case scenario would be that an out-of-state firm, let’s say somebody in Missouri, would win the overall State contract without any New Jersey employees, and we, the local people, would be forced out of our business in the state.

Thank you.

ASSEMBLYMAN GREGG: Thank you, Jim.

ASSEMBLYMAN CARROLL: Mr. Chairman, if I may.

ASSEMBLYMAN GREGG: Is that a question?

ASSEMBLYMAN CARROLL: If I may--

So the statement is that the proposal under consideration is for the State, as a whole, to deal with only one firm for the playground installation statewide?

MR. MARTURANO: That’s one possibility, yes.

ASSEMBLYMAN CARROLL: Okay, thank you.

ASSEMBLYMAN GREGG: Assemblyman.
ASSEMBLYMAN GUSCIORA: Jim, given the example of Liberty State Park playground, can you give us the benefit of what multivendors were involved in that project?

MR. MARTURANO: Well, what happened on that project was the State parks department set out a request for a quotation under the State contract. I think they solicited quotes and proposals from four or five firms. And then what they did was take all those firms and evaluate them on not only price, but quality and the type of design. And fortunately, we were the State contract vendor that was chosen.

ASSEMBLYMAN GREGG: Just to clarify this. There seems to be a couple of questions coming from the Committee.

What your concern is, Jim, is that the Treasury, through an action of changing purchasing, would then have the capacity to offer all of the contracts for the State for all of the equipment for playgrounds, potentially, to one contractor. That is what you’re stating.

MR. MARTURANO: Yes, sir, doing away with the multivendor contract.

ASSEMBLYMAN GREGG: At this point, is it your understanding that that is being done through regulation or will be done under--

And feel free, Kevin, to answer.

MR. MONACO: Mr. Chairman, we’ve been meeting with the Division of Purchase and Property. They are making this move. And I don’t know that they’re going to actually write regulations to do this. The way they’ve explained it to us is that there have been at least three recent court cases, which we can provide to the Committee, that they are responding to,
wherein the courts essentially said there are very narrow rules currently in the statute, which allow for multiple vendors, and the courts have questioned whether or not Treasury has met that criteria to allow for multiple vendors.

Our position, and which is why we’re eventually talking to the Legislature, is perhaps it should be the other way around. Perhaps, rather than having single vendors as the starting point and the State have to explain and meet a criteria why there should be multiple vendors—perhaps we should start with the idea that multiple vendors are better for the State, and Treasury is providing a service to local government entities by giving them that choice of products to meet the individual needs of their community. And perhaps Treasury should have to meet a criteria and explain why they’re only doing one vendor.

ASSEMBLYMAN GREGG: Assemblyman.

ASSEMBLYMAN CARROLL: Let’s go through this a little bit just now, because I’m not 100 percent certain that I’m on -- firing all cylinders on this one.

There is a list, presumably, somewhere along the lines, prepared by somebody, of State-approved contractors for playground services. Is that correct?

MR. MARTURANO: Yes, sir.

ASSEMBLYMAN CARROLL: And the argument is -- apparently is in response to several court cases that there should only be one State-approved contractor, and that any municipality or entity that wished to install, upgrade, maintain, or otherwise deal with playground equipment would have to go to one source? That’s the argument?
MR. MONACO: Assemblyman--

If I could answer that question, Mr. Chairman.

Yes, that is the basic argument. I’d just like to clarify, though, that this is not only playground equipment. That’s what Mr. Marturano’s business is. The change at Treasury would apply to all categories. I have some of them listed here: microcomputer workstations, copiers, stationary office supplies, motor vehicles for law enforcement, highway and construction, parts and repair services, dormitory residential furniture, office furniture, computer electronic supplies.

ASSEMBLYMAN CARROLL: Hold it, you’ve made your point. (laughter) But I mean-- So basically, if I understand what you’re saying, is there is some movement afoot, in any one of those categories, to have -- presumably have some statewide competition in RFP to handle all the work for the entire State, and what you’re concerned about is that these municipalities would be proscribed from using any one company because they’d have only one choice.

MR. MONACO: Assemblyman, that’s correct. There would be one vendor for each category of the services.

ASSEMBLYMAN CARROLL: So if a municipality, say for example, wished to buy a police car, no longer would it do an individual RFP, instead it would go to whomever had won the State contract?

MR. MONACO: That’s correct. Instead of having a choice of a Ford, Chevy, or Dodge, they would have a Ford, or whatever the State had already chosen for that.
ASSEMBLYMAN CARROLL: I’d be appreciative if you would be so kind as to cite me some specific court cases that have been reported on that. Not now, but when you get a moment.

MR. MONACO: Mr. Chairman, I have copies of them; not enough for the Committee, but I can supply one copy today to the Committee, if you’d like.

ASSEMBLYMAN GREGG: Kevin, if you would leave that with staff, we would appreciate that.

Assemblyman Guear, questions?

ASSEMBLYMAN GUEAR: Yes, I guess my question would be directed at Treasury. Why only a single vendor? If we have a prequalification process, and we have a half-dozen or more outfits that are qualified, why would Treasury want to support a single-vendor process?

ASSEMBLYMAN GREGG: Well, we will get that answer. I’m not going to put Treasury on the spot today for that, but I think it’s a valid question.

Kevin, do you have any other testimony today?

MR. MONACO: Mr. Chairman, yes. We have with us, also, Mr. Bill Foelsch, who is the Executive Director of the New Jersey Recreation and Parks Association, and I believe he has a statement as well.

WILLIAM FOELSCH: Thank you, Mr. Chairman and members of the Committee.

My Association represents -- it’s a voluntary association representing 700 members who predominantly work in the municipal, county, and State government sectors. They are the professional personnel who
administer the Department of Parks and Recreation, including the State Park Service and citizens who serve on commissions and advisory boards statewide.

We do support the continuation of the multiple vendor contract for park and playground equipment beyond this pending July 31, 2000 date. We do agree with Mr. Marturano and the Coalition that the real -- the prime use of the multivendor contracts has been the ability to have local choice, both in the quality of equipment that is purchased for park sites, as well as the aesthetics that go along with that choice.

Parks are more than just putting hard equipment out there. They're an integrated environment. We try to blend equipment and amenities into that environment to create either a passive environment, something pleasing to the soul, if you will. But it goes beyond just providing an athletic field for someone to run on. There are a number of different designs and needs for local parks. We believe that the multivendor contracts allow us to go out to a variety of vendors to do so.

We currently have selection, under State contract, from some 20 vendors, providing institutional quality equipment. That's not backyard equipment that you can go out to a local home center and get. These are specifically designed for the public setting, the institutional setting. Nearly all of our local governments have been using the State contract for the selection of park and recreation equipment for well on 35 or 40 years -- has been in existence. It certainly was in existence when I started in the profession in 1971. And it’s been there, and serving us well, since that time.

It does allow us to go to the respective needs of the community to find out what those needs are and match that up to the choice that may be
available through a particular vendor or multiple vendors for a particular site. Very often, these playgrounds are now chosen not only by the professional personnel, but citizens and committees which form, look at the site, look at the design, the aesthetics, and the needs of that community, and make selections over the wide vendor opportunities.

Certainly, with a single vendor under State contract, it will make things much more difficult to look at that variety. And certainly, the avoidance of the public bidding process has been a benefit to this state and to those municipalities and counties who have used the State contract. We do believe that the State has provided the most appropriate pricing on these equipment -- from these equipment vendors, and that should continue with the certainty that they’ve done a good job -- been able to avoid all that expense for bidding.

We have supported the State Division of Purchase and Property survey of our municipalities over the last couple of months. However, we have not seen the results of a survey specifically designed to pull out from the municipalities the types and variety of vendors they’re working with. But we know, through the discussions within our industry, that there’s been strong support from the recreation and park departments in responding to that survey and noting the different levels of purchasing that they’ve had from the multiple vendors under the contract.

Last year, the Legislature showed great wisdom in enacting legislation that provides for all public playgrounds to comply with the Consumer Product Safety Commission’s Guidelines for Public Playgrounds. I must tell you, this is having a far-reaching effect. As we go out to
municipalities, counties, and other public settings, we're looking over the next eight years for much of the equipment on site in playgrounds to be either replaced or improved. And of course, this is going directly back to the industry saying we need to be able to move the volume, to move safer equipment into our playgrounds.

There are some very strong concerns about what would happen under a single contract approach, where we would need to be assured of the quality in the variety, in order to fulfill these new mandates that we're going forward with for playground safety. So we do think it has a somewhat far-reaching effect there.

We're going to need multiple vendors to supply the demand. We're going to need multiple vendors to ensure that the quality of the equipment is put out there -- that we're looking for the safest possible equipment at the lowest possible cost, and again having local choice for that. We believe that high quality equals direct benefit to public safety.

We think that the accountability of local New Jersey-based companies is going to be a very significant issue in this. We do not want to see representation or vendors selected from out of state. We would like to keep the current process, where we have companies which serve New Jersey, going forward and continuing to be able to serve New Jersey with this type of equipment.

And we share the concerns noted before about the multiple vendor contract availability in some other areas. In the park and recreation environment, we're talking about State contracts for sporting goods, State contracts for craft supplies, State contracts for sand and clay products for the
parks and ballfields, and turf maintenance equipment being high on our list, wanting to retain a multiple contract approach to the State contracts.

Thank you. We appreciate your attention and concern.

ASSEMBLYMAN GREGG: Thank you very much.

I just have one quick question. Today, are the contracts by the State permissive or required? Can you--

MR. FOELSCH: They’re permissive.

ASSEMBLYMAN GREGG: So, at this point, your choice is to go to the State contract, which most of the time, of course, has a better price or go to a private person or another individual that didn’t have that contract. So, as I would understand it, if we went to a one-size-fits-all scenario, you would still have that choice, as a municipality, but it could end up costing you more money because in order to get what you need or desire, you would not have access to multiple vendors. Am I correct in that assumption?

MR. FOELSCH: Under the State contract approach now--

ASSEMBLYMAN GREGG: You have choice.

MR. FOELSCH: Well, they’re looking for it. We have the opportunity to go to a variety of vendors and select the best for our needs. Single contract approach -- we would either take it from the single contract State vendor or go to the public bidding process, as per any other purchasing municipalities or local governments would do.

ASSEMBLYMAN GREGG: Which could end up costing you more money.

MR. FOELSCH: Yes.

ASSEMBLYMAN GREGG: Any other questions by the members?
Assemblyman Gusciora.

ASSEMBLYMAN GUSCIORA: Yes, I just have a comment. Not only does this have implications for recreation, but in the State’s move to provide sprinklers to college dormitories, we could imagine the nightmare with just one vendor, given the short time that -- there’s probably going to be a lot of problems generated with that, as well.

ASSEMBLYMAN GREGG: Thank you, Assemblyman.

Assemblyman Carroll.

ASSEMBLYMAN CARROLL: I don’t know. Just look how well we’ve done with one vendor for the DMV. (laughter)

ASSEMBLYMAN GREGG: I was truly hoping that that wasn’t going to come up. (laughter) And I probably should have brought it up myself to handle it right from the beginning.

But thank you, Assemblyman Carroll, for that -- for not making us wait in line for that.

ASSEMBLYMAN CARROLL: You’re going to be the straight man today, Mr. Chairman.

ASSEMBLYMAN GREGG: I understand.

ASSEMBLYMAN CARROLL: It’s part of the job description.

ASSEMBLYMAN GREGG: Kevin, thank you. I think your testimony was excellent. I think you brought some points to the Committee that we will definitely review. So if you would get any documentation you can, through the Chair, to the Committee, I will disseminate it to the members and move forward with your issue.

MR. MONACO: Thank you very much, Mr. Chairman.
If I could just also emphasize the fact that we are working cooperatively with Treasury at this time. They’ve been very helpful. We’re having meetings in an ongoing manner. However, as we’ve heard, the deadline for this particular contract is July 31, so we may be looking to your Committee and the Legislature for your help.

Thank you very much.

ASSEMBLYMAN GREGG: And in a perfect world, we would hope that everything gets resolved after our hearings, as opposed to having to go to legislation. (laughter) So have a good day, Kevin.

MR. MONACO: Thank you.

ASSEMBLYMAN GREGG: Jack O’Connor, representing New Jersey Restaurant Association.

JACK O’CONNOR: Do I have a red light, Mr. Chairman? (referring to PA microphone)

ASSEMBLYMAN GREGG: Red light.

MR. O’CONNOR: I’m Jack O’Connor. I’m a small businessperson. I operate a restaurant in Bridgewater, New Jersey, Somerset County. I’m a Director of the New Jersey Restaurant Association. I belong to a number of trade associations because I’m interested in the issues of small business and survival in New Jersey and in the country.

My particular concern, regarding the subject you brought up today, is the Treasury Department of the State of New Jersey. About a year ago, a normal process that was started in New Jersey, where holders of liquor licenses would receive a clearance from the department of Taxation of the Treasurer’s Office saying all their taxes were paid, and the municipalities may
then reissue them their liquor license, which, you know, sounds fine-- I received a letter from the Treasury, Division of Taxation, saying I owed three years back taxes that I hadn’t paid, and they would not give me a clearance to renew my liquor license in Bridgewater.

The letter had a phone number at the bottom of the page. It was a 609 number. We file an electronic transfer filing. Our moneys are transferred from our bank account directly to the Treasury. We have records of that. None of those so-called three years of delinquencies of nonpayment were true. It was inaccurate. I called the number at the bottom of the letter. There was no answer. It was constantly busy. I called for two weeks. It was constantly busy for two weeks. I finally called the secretary of the Treasurer of New Jersey Office, got hold of a person, and that person got hold of another person who was, supposedly, in charge of this getting the clearance for your liquor license every year.

And they said they sent out 3000 letters on the same day. They had one telephone. By the way, it was not a toll-free phone, it was a toll-paying phone. And no one was assigned to answer the phone. That really bothered me a little bit. Finally, after about three or four days of talking to different people, I finally had someone from the Division of Taxation call me. I supplied the information -- the proof that I had paid. And I received a letter of clearance.

I was worried about the other 2999 people who weren’t as persistent as I was. And I was concerned at how it happened. And I was told that there are two departments in the Secretary of the Treasury (sic). One is the Revenue department, they get the money -- either your Federal -- electronic
transfer money or the check you mail in, and the Taxation department. And those are the people that come running after you and try and penalize you and charge you interest and tell you that you haven’t paid.

Unfortunately, in the Secretary of the Treasury Department, they don’t talk to each other, or one’s records are not available to the other. So they sort of operate independently. And that caused the problem.

So, as a member of the Restaurant Association, we set up a meeting with the Treasurer. And Mr. Thompson attended because he’s in charge of that Taxation department. And I brought up this issue, and some of our other members brought up the issue of the audits and the criteria used, which we thought were really unfair and unreasonable. And the Treasurer sat there, and after about an hour and one-half -- Mr. Thompson said absolutely nothing— And the Treasurer, after an hour and one-half, said, “We’ve got to get more telephones in the Treasury Department.” I said to myself, “What about accountability? Who is accountable in the Treasury Department for doing things right the first time, for correcting things when they’re wrong, and for standing up and saying, ‘We made a mistake,’” because that’s what’s expected of a small businessperson when we step out of line?

And now that Treasurer has gone, and we have a new Treasurer, although Mr. Thompson is still there. And about two months ago, I started a process of a bulk transfer. A lot of small businesspeople like myself are under pressure, and I think we’ll probably end up, eventually, selling our business. And I wanted to bulk transfer my liquor license and change my liquor license. Well, guess who I have to go back to. I have to go to that Department, under the Treasurer, and Taxation, and get a clearance letter so that the municipality
may transfer my liquor license, and they will charge the person, or the company buying the liquor license -- they will charge them a sales tax on the liquor inventory.

So the fellow calls me up, and he says, “I want to know what your food sales are.” I said, “I thought we were transferring liquor.” And he said, “Well, I have to do it this way. And if you give me the right answers, we won’t audit you.” I said, “Why are you going to audit me? I take inventory every single week. I know to the penny how many dollars and how many ounces I have in inventory. Would you like me to give you the number? Would you like to come down here and see it?” He said, “No, we get the amount of liquor purchases that you buy from the liquor wholesalers. And you tell us how much food sales you buy. And we have these criteria that we use -- these so-called percentages, that we get from God knows where, and then we determine that you’re accurately carrying this amount of inventory to support these kind of sales.” I said, “All right, I’ll give you what you want, and I’ll even give you the liquor inventory.”

And then I got a letter saying that I hadn’t paid the penalties on my taxes and, therefore, I was not cleared to transfer my liquor license. Now, remember -- small businessperson. We’ve had 50 employees, but probably myself and a 20-hour person do the books. So look through and see what they’re talking about. And yes, we had paid late on some of the electronic transfers, and yes, we had paid the penalties, and no, we didn’t owe any penalties, and by God we had paid one penalty twice because they sent us two bills with two amounts for exactly the same period of time, and they owe me money. And so I tried to convey to this man from the Treasury Department --
the Taxation department, that they owe me money, that these were paid, and I got to provide proof that I paid it.

And I guess my real question is accountability. I think the Treasury-- I think Mr. Thompson and the Secretary to the Treasurer-- I think they should be accountable for what they do. I think they should do it well. And when they do it wrong, I think they should apologize. I think they should, in some way, go to the small businessperson and say, “We goofed. We made a mistake.”

And I would offer to this Committee a possible model solution. I got very involved at the Federal level with Federal agencies like the IRS, like the Division of Taxation in New Jersey. And from a small business standpoint, they passed a law that was called the Small Business Regulatory Enforcement Fairness Act of 1996. It was a very good model. And if I would take that Act, which has been used by small businesses throughout the country, and apply it to New Jersey, I’d pick some agency in New Jersey, probably Economic Development, and I’d appoint an ombudsman, or taxpayers advocate. And then I would have maybe two or three volunteer committees throughout the state where they would sort of ask people what kind of problems they were having.

And then this ombudsman would then go to the agency, Division of Taxation or someplace else-- make it involve other agencies -- and say, “You know you got a problem? How are you going to solve this problem? We’re here to ask you for a solution.” And then they can say, “You’re right. We really didn’t know about that. We really haven’t addressed that. We didn’t have enough manpower. And we’re going to solve this problem.” And that’s
the last you hear of it. But if they stonewall, like they have in this instance I’m giving you, for two years, and they are not doing their job and they’re not doing it well, then this ombudsman, this advocate, would report to the Legislature at the end of the year and say, “Well, we had these things, and they did that. And we had these, and they didn’t do anything. And I guess you’re going to have to do something with these people. They don’t seem to want to be accountable or responsible.”

So that’s my suggestion for a model. That’s my particular issue. I can talk about the other issues that were brought up by other restaurants or other retail people, but I want to stick to the one that I had personal experience on. And I -- if you have any questions or any further information, I’d be happy to answer them.

ASSEMBLYMAN GREGG: Thank you, Jack.

Members, any questions? (no response)

Thank you for your time.

The next group is from the New Jersey Licensed Beverage Association. We have a number of folks. We have enough seats up here, I believe.

Bill Cleary, Morris Compton, Umberto Rescinio, Georgette O’Toole--

Any relation, Kevin?

ASSEMBLYMAN O’TOOLE: Not that I know of.

ASSEMBLYMAN GREGG: --Jim Daly, Mike Marsh, and Joe Ardire are the names I have listed.

ASSEMBLYMAN O’TOOLE: Do we look that similar, Guy?
ASSEMBLYMAN GREGG: No.

Bill, I’ll allow you to take control of your group there.

WILLIAM J. CLEARY: I don’t know that that’s possible, sir. I yield the control to the Chair.

ASSEMBLYMAN GREGG: I’ll request -- try to keep only one red light on at a time. (referring to PA microphone)

MR. CLEARY: Okay. We’re probably going to go in the order that we submitted to you just recently.

My part in this is just to thank you very much for holding the hearing. It was very interesting listening to some of the other groups from the NFIB and some others with the problems that all small businesses have.

I think the group here today has a very specific concern, one that I know hits home for you. And I ask to move forward on this, allowing us to speak, because we have not one, but two CPAs in the heart of tax time that were very kind enough to join us here today.

So right off the bat, I’ll introduce Morris Compton, who’ll address the group.

MORRIS A. COMPTON, CPA.: My experience with taxes--

Which mike is it?

ASSEMBLYMAN GREGG: There’s one mike for recording, one mike for volume.

MR. COMPTON: Oh, I see.

ASSEMBLYMAN GREGG: Your hand is on the volume mike.

MR. COMPTON: I have over 40 years experience dealing with taxes. Thirty-two of those years were with the New Jersey Division of
Taxation, which I retired from in 1991. For the last eight and one-half years, I’ve been a tax consultant, specializing in Federal and tax matters, mostly audits, some offers in compromises, and other enforcement actions.

Going back to the first speaker, Mr. Murphy, and what he experienced in his audit—Unfortunately, that is the rule rather than the exception. I’ve dealt with, directly or indirectly, probably over 100 of these cases, and that’s what I have experienced, also. It’s the new, inexperienced, maybe overzealous auditor who is trying to maximize an assessment. It’s bad enough the numbers that come out as a result of that, but the anxiety it creates to the taxpayer, to the family is enormous because it lasts for quite some time. These problems are not resolved within six months or a year. Many times it takes two or three years, especially if it’s not resolved at the immediate level or with the supervisor.

Not everyone is fortunate enough to get a Tom Coughlin. You get other supervisors who are very hard in their stance and just stick with, maybe, what the original was or make a small adjustment, which is really not reflective of that business activity. Therefore, you take it to conference and appeals, and the process now just to get a hearing—You have 90 days to -- after you’re billed, to request a -- protest the assessment and request a hearing. You do that within the 90 days, and then you have anywhere from a year to a year and one-half to wait for a hearing.

The reason for that is, I think you have 200 people out there doing these assessments, and maybe a dozen conferees, so it’s not the conferees’ fault. So either they have to do less audits, or hire more conferees, or have—My suggestion would be, have better quality audits.
Their initial approach is to have a preaudit questionnaire. Usually, the taxpayer’s not familiar with the terms of the questions that are in this questionnaire, and many times even the accountant isn’t. So when they come in with that preaudit questionnaire, there’s a lot of things that are nebulous, to say the least.

I know it’s only a civil proceeding, but taxpayers should be Mirandized. They do not have the knowledge or the skills, and a lot of times their accountants don’t, to understand exactly what’s going on. For instance, the initial document is a consent order. This is not explained. In every situation I was involved in, they never explained to the taxpayer the consequences of the consent order, which establishes the period which you’re going to audit and then the time they have from which to do that.

Now, when they initially have it— There are some mistakes, but let’s say it’s accurate, and it incorporates the taxes and the tax period which is going to be audited. All are within the statute at that time. However, the top paragraph -- the last sentence -- they put a termination date on the consent form, and the auditor has just allowed himself a year and one-half to two years to complete this audit.

I think that’s really unfair because if there is an assessment -- and by the time the bill gets out, a lot of the periods would have expired by the statute of limitations; however, they’re incorporated because the taxpayer signed the consent form, not understanding what it was about. And the early years of the assessment would have interest equal to the tax that’s due. So that really gets out of hand.
There’s a lot of other intangibles or variables that have to be considered, also, which are not explained to the taxpayer properly. The Division initially looks at the corporation tax returns, or the Federal 1120s, takes the gross receipts, divides it by the cost of goods, and comes up with the report of mark on ratio.

They say, “All right, this is what you’re reporting. Here’s your ratio. And then we’re going to go ahead with the audit.” What they fail to overlook is on line two, which is the cost of goods, there may be many items in there that are not saleable items. It could be supply expense, rental expense, I’ve even seen salaries in there. So it’s not fair to the taxpayer without advising him and say, “Go through your cost of goods, eliminate these items that you may be reporting at a 2.5, but if you extract those items at a cost of goods you’re at 3.5, and then you wouldn’t even come up for audit.” If that’s a percentage they’re reporting, or however they went about their audit or how they go about their audit will coincide with that markup. But that’s not explained to the taxpayer. So their markup is going to be a certain percentage, which will come in standards which I believe are predetermined before they start the audit, which— That shouldn’t happen either.

One thing I’ve experienced in my 40-plus years is that every business is different, just as different as every individual here is different. And they should have a more open mind as to how that business is run, as Mr. Murphy explained, “Here’s how I cut up the meat,” and go through all that detail. And you go down to another operation, it could be entirely different. And percentages are what it’s all about.
There are other variables as far as packaged goods are concerned. I’ve seen these auditors keep asking what the price of a six-pack is and incorporate that in their audit. And then they may ask about how much a case costs for the same product. The difference between the markups is considerable. If you sell a six-pack for $5, four of them would be $20. Usually a case of beer costs $12, so you have a 1.67 markup. However, if you sell a case of the same product for $16, then your markup is 1.33. So you have a 33 percent variance there. But if you look at these audits, everything is six-packs, six-packs, six-packs, which is going to boost up the overall markup when incorporated with the other markups.

Again I could go on and on for quite a bit, but there has to be better quality control right up front, as to the methodology you’re using. There has to be more explanation given to the tax (indiscernible) up front. He really should be advised that if he doesn’t have an accountant that really understands how these audits are conducted, he should get someone to do that and give him time to do-- The ones I’ve been involved in from the beginning came out right because I was on top of everything. But I got involved with some very late, which were very difficult to resolve at that point -- when they’ve already exhausted their administrative remedies at the audit level, also at the conference and appeal level, and the next appeal is tax court. And that’s going to take quite a bit of time.

So we go right back to the beginning of doing the job properly, with quality, when it initially starts.

That’s all I have.

UMBERTO N. RESCINIO, CPA: My name is--
ASSEMBLYMAN GREGG: Excuse me, we have a question from one of the members.

ASSEMBLYMAN O’TOOLE: All right.

Mr. Compton, thank you very much for your testimony. It’s refreshing to hear someone with your four decades of experience, without the emotion of being involved in a specific case, just talk this passionately about what’s right and what’s wrong with the current system. And you speak with not only experience, but apparently with a great deal of creditability.

And what troubles me with what you said is that we heard from Mr. Murphy earlier today, and you indicated that’s more the norm than the exception.

MR. COMPTON: Exactly.

ASSEMBLYMAN O’TOOLE: And that’s very disturbing to hear that, given your experience.

And is it the norm because there is such a level of inexperience or there’s not enough auditors or there’s just too much pressure, perhaps, on the lower rung -- the first-tier investigators?

MR. COMPTON: That’s some of it. I also think there’s some aggressive supervisors that are looking to maximize an assessment.

ASSEMBLYMAN O’TOOLE: And you’re saying, potentially, the answer is either less auditors, more conferees, or more experienced auditors. Is there some way you can tie in the supervisors having responsibility, frankly, for their little -- their group that they oversee? Is there some mechanism? I mean, if you’re going to have individual investigators, either renegade investigators or those that aren’t being watched very well or those who are
operating outside the rules of the game, perhaps we can tie in their performance with the performance of the supervisors and ultimately account -- have both groups accountable for this, supervisors and the lower-tier investigators.

MR. COMPTON: Yes, exactly.

ASSEMBLYMAN O’TOOLE: In terms of the Mirandizing, I’m just a little concerned about that issue. Does there ever come a time where an individual resident, because of the audit or the consent form that he signs, is subject to criminal proceedings?

MR. COMPTON: Not that I’m aware of, although, with my experience back at Taxation, the sale taxes are trust funds-- So if they’re not remitting that and they’re doing that deliberately, it could proceed with criminal--

ASSEMBLYMAN O’TOOLE: I mean--

MR. COMPTON: But most of these are civil, and they’re looking for the assessment.

ASSEMBLYMAN O’TOOLE: Well, having heard that testimony, I think that we would be hard pressed to ask for a Miranda warning at that level for--

MR. COMPTON: I said that sort of facetiously, but some kind of explanation. By no means should the taxpayer be told, after they advise the auditor that they had me as a consultant, and the auditor came back-- “Oh, you don’t need a consultant.”

ASSEMBLYMAN O’TOOLE: Yes.
MR. COMPTON: “Let us just come here and do that. You don’t need him at all. Save the money.”

ASSEMBLYMAN O’TOOLE: Yes, there should be a full explanation -- full disclosure as to the consequences of his release of information. I believe that. But beyond that-- Like I say, if, at the end of the day, there’s criminal activity, let’s prosecute the bad apples.

But thank you very much for your testimony.

MR. COMPTON: Okay. You’re welcome.

ASSEMBLYMAN GREGG: Thank you, Mr. Vice-Chair.

Next.

MR. RESCINIO: My name is Umberto Rescinio. I’m a CPA. I’ve had 45 years of auditing and accounting experience. I was on -- employed by the big eight firms, a few of them, in fact. I went in business on my own, as a CPA. And I’m here on my own behalf. I just want to make that perfectly clear because I am on the New Jersey State CPA Society State Taxation Committee. And I have met with Commissioner Thompson and his staff a couple of times.

I first want to make a comment about that. I think Mr. Thompson and his staff-- When I talk about his staff, I’m talking about his Assistant Directors, like Mr. Gavin and Mr. Fox. They’re very good people and very competent. And I think they got a tiger by the tail. And sometimes you can’t let it go.

And to try to explain-- I mean, you have to turn your hat around now to when Mr. Murphy was here. We’re going back to the Taxation -- and not only for restaurants, but we’re talking about any industry that was in the liquor business, whether it’s a wholesaler, a bar, a restaurant, a liquor store,
whatever it may be. These audits, I think, started about five years ago. And when they started, I was on the Taxation Committee, and I was a member of the -- what we call the Department of Labor Subcommittee. And I was instrumental with the Department of Labor in coming up with an audit manual for the Department of Labor. So when it comes to auditing, I think I know a little bit about auditing. And it’s an art. And to me, to try and explain to you simply what went on -- what’s going on, it would be easier for me to explain how I got here from the Jersey Shore, going through Route 29 North. I got lost. And you’ll get lost with this.

There isn’t that much time to go over this. But about five years ago -- and the gentleman is here from the State Taxation Committee -- asked me to give him, in simple terms, a one-sheet write-up, and I did. And at that time -- given it to him-- Subsequent to that, about a year ago, I think, in one of the journals, I see -- I read where Senator Littell was trying to sponsor something in the budget about doing audits based on audit standards and records and not on estimations, computations. Really, I guess the word is outrageous way of doing it. And I have that sheet here, and I’m going to give it to the board (sic). And basically what it says is that an audit -- and I don’t want to call these audits, let’s call them reviews -- these reviews are -- should be based on -- if you have records, use the records. And you have to have some tolerance in these kind of audits.

This is not what’s happening. They’re not auditing. They have a modus operandi of going in and doing something on these reviews of these restaurants and bars and whatever. And they follow this.
Now, Mr. Murphy, who I’m very familiar with, mentioned that after six months he got a no change from Mr. Coughlin. But you have to understand, I think that’s the minority percentage and not the majority. I think, and Mr. Thompson probably could refresh my memory, or yours, in the year and one-half period, what they call these liquor audits -- cash audits, generated like $200 million in assessments, not collections, assessments -- maybe a little less or a little more, I don’t remember.

But the majorities -- and the supervising auditors are fully aware of this because they are the ones that review these audits that are being performed or reviewed. It’s difficult to explain how these audits should be done, but I’m going to try to give you a couple of explanations.

No. 1, Mo mentioned about the -- going through the appeals procedure. It took me four years even to get my Society to realize that the letter they received from the New Jersey Division of Taxation stating that you should go through appeals before you go to the tax court is incorrect. The State statutes, and fully aware of State statutes-- The State says this, that you do not have to do that. And there is a case, and the case is Harris v. The New Jersey Division of Taxation, 1995. It says that you can go straight to the tax court. That’s one of the major errors that they have in finalizing their reports.

Now, do you want to go through appeals? I think you do, before you go to the tax court. But I feel that the appeals office should not be part of the Division, but separate from the Division in the Treasury Department because you’re putting the fox in with the chickens. You should do that. The IRS does the same thing.
Now, as to the audit itself, and this one sheet will explain it. And I’m going to try, in a short period of time -- five minutes. I’ll give you a few examples.

ASSEMBLYMAN GREGG: I’m just stopping you for a second so I can talk to Bill for a second.

How much more testimony-- Will everybody be speaking?
MR. CLEARY: We’ll probably have Georgette speak, and then--
ASSEMBLYMAN GREGG: I just want to keep the time within a normal realm. I want to hear what you want to say.

Is that document in front of you, Umberto, from the budget? Is that the language--

MR. RESCINIO: No, this was written about four or five years ago to a gentleman that’s sitting right in back of me.

ASSEMBLYMAN GREGG: Great. I just wanted to make sure it wasn’t the budget language because I’m pretty familiar with the budget language that was vetoed.

Go forward and try to be as quick as you can.
MR. RESCINIO: Okay.
My light is off. (referring to PA microphone)
ASSEMBLYMAN GREGG: Put it back on.
MR. RESCINIO: Okay, it’s on.
No, this was written five years ago when they started these type of reviews by the Division of Taxation. Subsequent, I read, almost identical to what I wrote here, that Senator Littell, I think, had in his line item to the Governor, which she vetoed. She just scratched it out, from what I’m told.
In talking about the audits-- I’m going to just give a couple of examples, and then I’ll get off.

Mo talked about the cost of sales. You have to know-- You have to be technically sound in auditing to know what he’s saying. Actually, what’s happening here, and Dan Murphy, this morning, mentioned it-- He had a couple hundred items that were line items, liquor sales and such and so, to get ratios. You have a possibility of maybe five or six errors in that, where the auditor is looking at some stuff. He takes-- Sometimes they take these invoices -- they say two years prior to the year that he’s looking at -- the prices that they sell items for. In other words, the menu or liquor sales may be ’98 and he’s doing a ’96 -- looking at vendors’ invoices, so you have a difference of cost as to compare to pricing in the same year. That happens.

You also have problems in that you can get errors in quantity, cost, and sales price. And I don’t want to go into detail, but you got about maybe, in some cases, up to 400 items that you got to look at to determine if the ratio is right. Then what they do-- They apply the ratio to a cost of sales based on, usually, what your income tax is. That’s an error because they’re not auditing cost of sales, they’re auditing an item of cost of sales, which is purchases.

So therefore, used in the cost of sales they raised -- the basis -- what a person -- applying that percentage to-- So that’s another error. Then, when you look at their voluminous report, they’ll say third party. Well, sometimes you’re thinking that it says third party -- you assume it’s correct. Sometimes they’re not. There’s a difference. They’re not really third-party verifications -- couple items that I had.
So we’re running into these kinds of errors. But basically what needs to be done -- and the gentleman asked it -- I think you need to have the thinking, at that State level -- You have to have maybe an outside firm come in and go over what an auditor should be doing, how an audit should be performed, and setting up an actual audit program, not what they have now. I don’t consider that an audit program. I consider that more like a -- “Oh here, go out and do this, here’s your modus operandi.”

So it’s standard. And that’s the biggest problem, right there -- in addition to having -- the auditors not being trained. They’re not. They come out there -- And the supervisors -- You don’t get $200 and some million in a year and one-half assessment by the supervisors always saying no change or the audit -- there’s no findings. That’s not the case.

So there are so many other things to know about this. I just can’t go into-- The State does say, “Oh we’ll give you a percentage. We’ll give you 10 percent for your spillage, your waste, your this, and your that, or your theft, whatever.” And it’s not true. When I say not true, meaning that the 10 percent -- I mean, it could be 50 percent. It could be 10 percent, 5 percent. I mean, we’re playing games. Do the audit based on records available. If the records are not available, then do what the IRS says, reconstruct them. And the statute of limitations -- yes, we do have a problem in the statute of limitations. But we need to have someone at the State level. Either hire an outside firm or someone go in there and say, “Here’s how an audit should be preformed,” and then train those auditors to do that.

Basically that’s it.
By the way, there is a probable criminal area. When you sign that report off, and if you got the GIT in there-- In other words, you got a sales, you got a corporate tax, you got different types of taxes, and you have one that says GIT, you’re actually committed, in my opinion -- and I’m not a lawyer-- That’s not civil. It could be criminal. You sign it, you’re saying you committed fraud. You didn’t pay your tax.

ASSEMBLYMAN GREGG: Thank you, Umberto.

I’d just like to share, for the Committee’s edification, that language you speak of, the Littell-Gregg language, drafted by me for the budget, was vetoed. I think it comes to the crux of the issue. And I would like to ask the question before you continue to testify.

I’ve spent a lot of time in the retail business. And it is my sense that the overriding problem here is that the government is not determining whether or not you collected sales tax on what you sold. They have become much more interested in what you might have made as a product and then as a sale. And I often use the example of the IRS or Treasury going to General Motors and saying, “You have bought 50 million pounds of steel. You’re short 3000 cars.” And I think that that’s the methodology that has been used because it’s all we have. And our industry has gotten much more complex in all manners, whether it be retail in car shops, or retail in restaurants and taverns. The capacity for computerized registers, in controlling your costs, is far and above the cigar box that some people may have remembered 30 or 40 years ago.

So I come to the table here, and I’ll be happy to listen to more testimony on this issue. Somehow we’re going to have to find a way to go back
to the original theme that you, as a retailer, are responsible for collecting sales tax for the State of New Jersey on behalf of them and remitting it to them. You are not responsible for producing a perfect beer, 252 per keg. You’re not responsible for producing 27 scotch and waters. You’re not responsible for producing eight hamburgers from $X$ amount of pounds of beef. You are responsible, however, once you transact the sale in the State of New Jersey to collect the appropriate tax on it.

How we get from there to an appropriate method for the government to determine when you have been wrong in not collecting taxes or collecting taxes and keeping it for yourself, which, of course, is wrong, and I don’t think anybody supports, but finding that fine line is important, and I think that line falls on whether we are guilty until proven innocent, or innocent until proven guilty. And I think that that is going to be a hard balance to find. And I think that I come from that.

And I’m going to look at the two CPAs because, quite often, when I get phone calls from constituents, members of your association, on how to progress in an audit, my first questions usually deal with, “What does your accountant say?” My first question is, “Do you have tapes and records? Do you have a register?” Too often I hear no. And too often I hear, “I don’t have those records.” So I think it’s very important, and that’s why that language was crafted that way.

You have to have evidence because once you don’t have a record to say this is what I’ve done, you lose credibility. And those people fall off, and ultimately should be subject to whatever the fines and penalties are appropriate at that point.
So I would-- At that point, I would like to--

MR. RESCINIO: May I add to what you’re saying?

Yes, there are certain businesses out there that are doing wrong. They’re taking money out that they’re not supposed to. And I think you should go after them wholeheartedly. But most of these that we’re talking about are honest people that are being assessed these humongous amounts, and then you go into, what I call, a negotiating bid. Sometimes these things last over two years, and the reports are going back and forth. It’s not the one report -- like maybe four or five reports. They give you a report, you find something wrong, you give it back to them, they correct it, it comes back and forth. And that’s the problem you have in this thing. And this is something that should be addressed when the State does have someone come in.

And I think they ought to have some sort of accounting firm come in there and help them out. Now, I’m talking about the higher level because I think that’s where it should start, with Mr. Thompson. I think he’s well aware of that. And I think Mr. Thompson, at one time, said something about -- and I’m not sure, and if I’m wrong, I hope he corrects me--

ASSEMBLYMAN GREGG: He’s right behind you.

MR. RESCINIO: Maybe we ought to take this liquor and bring it back to the wholesaler and let them pay the tax rather than retailers.

Now, that’s a possibility for this industry. But remember, this auditing -- and the Division of Taxation doesn’t end with this type of audits in this business. And they’ll go on to another type of business, another classification. And you may have the same problems go on to another business. It could be anything. It could be pizzerias, it could be doctors,
dentists, it could be auto washes, garages. This thing could go on and on and on. If you don’t get the right auditors and train them and have them know really what auditing means, then you got a problem. Not now, but you will have it going on forward.

ASSEMBLYMAN GREGG: It will never change. And regardless of your methodology of taxation--

MR. RESCINIO: You’re right.

ASSEMBLYMAN GREGG: --there will still be tax audits because if you had a wholesale tax on liquor, they’re still coming after your food. So you have to solve the problem. Moving it around is still going to have the people who don’t want to pay taxes not paying them because they won’t be collecting the money at the register, and they may be paying the wholesale tax.

So the ultimate solution is finding a fair way for the State to interact with its citizens and businesses. And I think some of CPA Davidoff’s points of view of having a Federal scenario where there is an actual decision of what your capacity to pay -- would also have some meaning because to put small businesses out of business because of a tax problem doesn’t make sense for the employees, the families, or anybody else. And I know that’s occurring.

So I’ll defer, Bill, now, to your other individuals, unless I have any questions.

MR. CLEARY: We’d like Georgette to very briefly go over her situation. You have, in your packets, or was handed to you, her testimony. And then, rather than four horror stories, we’ll just yield to the other three to just make comments -- what was unique about their cases, different than Georgette.
So, Georgette--

ASSEMBLYMAN GREGG: Thank you, Bill.

Georgette, welcome.

GEORGETTE O’TOOLE: Hi. Good morning.

ASSEMBLYMAN GREGG: Georgette, could you move down to where we have a public microphone there? You have to get to one of the shorter mikes so your testimony will be recorded. Do you see the small mike? There you go.

M.S. O’TOOLE: Good morning, and thank you.

My name is Georgette O’Toole. My husband Henry and I run a small local bar in Milford, New Jersey, which is along the Delaware River in the rural county of Hunterdon. Milford is a small town. Population is less than 2000 people. We have a small neighborhood bar. At this point of time, for about the last 10 years, we have not dealt in food, other than private parties, birthday parties, so forth, and I give out, from time to time, food, in the form of buffets, on holidays and various situations.

My first correspondence from the Division of Taxation was on October 11, 1996. It outlined what information we would need for our sales tax audit, which was scheduled for October 24. We were audited for full five fiscal years, fiscal years starting 3-1-99 ending 2-29-92 through fiscal year ending 2-28-96 plus the first quarter of the 1997 fiscal year.

After this first audit, the Division of Taxation stated we owed sales tax of $13,020 and corporate business tax of $23,967, for a total of $36,987 plus interest. The auditor returned, per our request, on November 26, after I discovered errors on the first audit. There were errors in addition, calculating
figures and costs. The other vending figures the auditor used were not the figures we showed in our records. He had much higher figures. The same was true with the cigarette purchase figures.

Another item we questioned was the fact that the auditor used 33 drinks from every liter bottle of liquor purchased – in his audit – for the retail sales figures. Less than 33 drinks are sold from one liter bottle of liquor. Complementary drinks have to be considered. Also, more than one ounce may be used in a mixed drink. Also, we questioned certain purchases of liquor are sold strictly as package items. An example – we purchased Appleton Rum as a special order for one customer and is sold only as packaged goods. None is sold over the bar. Also, not all our barrels of beer are sold at the bar. We sell a barrel to our customers at a modest markup price as a service to them for parties, weddings, other occasions, or we use barrels of beer for our pool teams or our baseball teams.

The auditor used a sample three-month period from 1994 for his purchases and calculating costs in his audit, but used the current, 1996, retail prices in order to get a markup percentage formula, which he then used for all five years that he audited.

We questioned his using the current, 1996, retail prices, when the retail prices were lower in the years he audited. He did another audit on that day, November 26. After this audit, we owed the State sales tax of $7512 and corporate business tax of $13,173, for a total of $20,685. This was a reduction of $16,301.
We received a bill dated December 13, 1996, for the figure of $20,685 plus interest, calculated to January 20, 1997, of $5665, for a total amount due of $26,350.

Also, during this time, I was receiving correspondence stating we owed individual gross income tax to the State of $2204 plus interest of $458, for a total of $2662. This made a grand total that we owed, at this time, of $29,013.

A letter dated December 16, 1996, informed us we could file a protest with the Division of Taxation requesting an informal, administrative hearing within 90 days or pay the amount due within 90 days.

We met again on March 5, 1997, with the auditor. He informed us he could not do any more with our audit and advised to file for the hearing. I requested this audit -- this hearing on March 6. I had already been preparing for this hearing before the last meeting with the auditor. I spent countless hours preparing my own audit for the same sample period the auditor used, but used the retail prices that were in effect at the time. I filled out papers, answered questions, supplied much documentation in support of our protest. A power of attorney, form M-5008, had to be filled out. I also answered much correspondence pertaining to our individual income tax and asked to have the two protests combined. The outcome of our corporation protest would affect the individual income tax due.

I must state, at this point in time, I was becoming very frustrated with this whole affair. I was at the point of tears. This whole ordeal was extremely time consuming and stressful. We are a small business collecting the State sales tax. The State is telling us how much sales tax we are expected to
collect. If we did not collect as much as the State audit showed was to be collected, we were billed for the difference plus interest.

We have been in the liquor business—My husband and I have been in the liquor business for 26 years, and we have always filed all our sales tax forms on time and paid all our sales tax on time.

Our first hearing was scheduled for June 12, 1997, but was changed to July 9 by the State. It was held in Trenton. Our accountant had to attend this meeting. He had also attended all three meetings with the auditor. This extra accounting time cost us $1200. Again I had to present documentation pertaining to our protest. We felt the tax people at the hearing did not have enough knowledge of the liquor business. Each business is different. The State cannot use an across-the-board formula for all licensees. We operate in a small, rural town and cannot charge the same prices as in a larger city. Our customers buy a large amount of packaged goods. We are allowed to sell packaged goods, as well as operate as a bar.

They did not cover all documentation we presented when we filed our protest. After the hearing, I had to send in more documentation concerning items discussed. Again, it was time consuming and stressful. We were notified a determination would be made on all this additional information. A final determination letter was sent to us October 3, 1997, and was for zero. The whole process took one year, countless hours of work, a lot of stress, a lot of tears, and expense. I’m just glad it’s over.

ASSEMBLYMAN GREGG: Assemblyman O’Toole.

ASSEMBLYMAN O’TOOLE: Thank you.

We are, obviously, of no relation.
M.S. O’TOOLE: No, not that I know of.

ASSEMBLYMAN GREGG: Now that you have no tax liability, he might wish to be. (laughter)

ASSEMBLYMAN O’TOOLE: Let me thank you for coming here today. I know it has taken much out of your life, and I imagine you had to summon some courage to come and try to deal with this nightmare over again. But I’m glad you and people like Mr. Murphy and others have come to testify. And, as I indicated from the beginning of this meeting, that’s precisely why we’re here. And that’s why this Regulatory Oversight Committee has been reconvened and brought to being in the year 2000. We’ve heard so many horror stories of State government out of control, bureaucracies that are accountable to no one. At the end of the day they have to be accountable to the eight million residents. If not, then there’s no reason for the State government to exist.

And whether it’s DEP or DCA or how we hire and fire people or whether it’s racial biases that go on in our State government, we have to know what’s going on, person to person. We can look at you, eyeball to eyeball, and say, “How can we make your life a little easier?” And that’s what my job is. That’s what the Chairman’s job is, whether we’re Democrat or Republican. We have to make life easier for all of us. And that sometimes means reining in big government.

And I think there’s a purpose. Obviously, Treasury has a purpose. Obviously, there’s some restaurants and bars and some taverns that are underreporting their income because we’ve had some individuals come out and were fined and whatnot.
One size doesn’t fit all. Whether you’re talking about school costs per pupil, insurance costs, or whether you’re tax-- If they’re going to exact per ounce, per glass of beer, per-- It doesn’t fit. You know a mom and pop and a retail, main street New York City bar or restaurant -- they’re just two totally different dynamics.

And as the other accountant indicated, every face, every individual has a different story. And I’m hopeful that, first of all, I can hear from Treasury, at some other time, as to how do we deal with one size doesn’t fit all; how do we individualize these audits to make sure that we’re not penalizing you for the success of others or if you’re charitable. There’s one case I just read about that -- someone gave away six cases of wine to a parish, and now they’re being taxed, per ounce, on that case of wine. I think that’s ridiculous.

And if we have-- A charity has to be recognized. If you’re giving, as a house courtesy, a free drink or a free meal or whatever the case may be-- You’re giving a catering event for your softball team, and you’re going to be taxed on that. I think that’s very unfair. And it certainly doesn’t strike me as being very equitable.

I want to thank you for coming here. I’m glad, at the end of the day, that the result that you received was a just one, that you owed nothing. But I apologize for you having to endure the heartache and the nightmare and certainly the fees and the headache that associate with that. And by your testimony here today, ma’am, I think it’s going to make it easier to, hopefully, avoid some of these problems with other people that are in your circumstance throughout the state.

M S. O’TOOLE: I’m glad I could help. Thank you.
ASSEMBLYMAN GREGG: Thank you, Mr. Vice-Chair.

Any other questions, specifically?

MIKE MARSH: My name is Mike Marsh. I own the Coles Mill Tavern in Franklinville. I would-- Just to limit my comments-- I don’t want to go into my case because I’m still being audited. I got my first letter 3-11-98, and I’m still under audit. It hasn’t been-- We haven’t heard anything in, probably, over a year.

But my comments would go to the attitude of auditors, in general. And I believe this comes from the top. I don’t think these guys were hired -- four or five years ago, they couldn’t come in with these attitudes. Somebody had to give them the attitude. And their attitude is that we stole money, they’re going to prove it, and we’re going to pay. And that’s the attitude they have when they walk in the door.

My auditor called me a thief twice, once in front of his friends -- once in front of his supervisor, and once -- I’m sorry, twice to my face, once to my accountant. And he told me-- When he first came, he told my accountant that he had 40 to 60 hours undercover investigation in my bar. My gross for the four years that they were auditing was never over $300,000.

They told my accountant that they were in the woods at night -- I have a trailer on the property next to the bar, a house trailer -- looking in the windows to see if anyone lived there. When they came to my place, the auditor told me that I had three mortgages on my house, which I don’t. So apparently they did a personal background check before they ever got to my bar. They went outside and told-- I’m sorry, before that, they told my accountant that they went through my trash. And when the auditor was at my
bar, he wanted to go out and see where my trash was. And I asked him why. And he said, “because you don’t claim that you sell cans over the bar.” And I said, “We don’t.” And he said he wanted to look in my trash to see if I had cans in my trash, because if I had cans in my trash can, apparently I would sell cans over the bar. So that was his reason for that.

And it upsets me that I talked to over 60 people to come to this hearing today, and they won’t come. They are deathly afraid that the gentlemen sitting back there will be on them again. They settled. Some guys have settled. This one guy sold his bar and could not collect his money until he settled with the Division of Taxation. And after about five or six months, he went and said, “Look, we got to make a deal. We have to sit down and make a deal. What is it?” And he gave them $5000 or $6000, whatever it was, just so he could collect his money.

And I think it’s wrong when my accountant writes a letter to the auditors, and they tell you that -- this is my audit papers that they give you. I’ve never seen it, but-- I went to parochial school. Maybe the public schools teach a different system. But they have three decimal points in their monetary system. And he explains it that, in their internal system, this all works out. And when I told him that the numbers don’t add up-- I’m not talking about rounding off. The first page of this audit, and I have a copy, I’ll give it to you-- If there’s 90 numbers -- 90 rows on there that they multiplied, 86 of them don’t multiply across. They don’t add up.

So for this guy to tell me that I have to assume that somewhere in his internal calculating system these numbers balance out, I’m not-- I’m sorry,
I can’t take it. For one, he calls me a thief to my face, and then he tells me to accept his numbers when he can’t even add.

That’s basically all I want to say. The attitude of the auditors--I thought we lived in America, and I thought that--I have records. I have detailed records. I’ll show you what I turned into the Division of Taxation. I have--I thought I was doing good. In 1990, I went to a computer system. Every day I have a cash in sheet. And it tells you, in detail, package liquor, bar liquor, bar beer, bar liquor, food, cigarettes, vending, total cash in, total cash out, total deposits, for every year that I’ve been in business, for every day, and they don’t accept that. The first thing he did was he came in there and he said my purchases added up to $148,201. Their outside source added up to $148,205. I was $4 off. And I believe they made a mistake, not me.

But they would accept those numbers, but they don’t accept these numbers. They came in, and they made up their own set of numbers. And that’s what they--They told me that I stole or underreported my income by $82,000 a year for four years, based on--I have no idea--on a false science. This is not an audit.

If someone came into me and said, “We want to audit your books--” If you were a bank, they’re going to say, “How much money did you take in? Where did you spend it? There’s a difference here. Let’s find it.” These guys come in and they say, “You should have taken in this much money.” I couldn’t see it in the book. Maybe I’m a bad businessman. I’ve been in business 22 years. I bought my bar in 1977. I live in a rural area that’s--We had less than 15,000 people when I bought my bar, and 15 licenses in the town. You can’t walk to my bar. The nearest transportation is five miles away.
If you don’t drive to my bar, you don’t come there. I also live right next to Cumberland County. I’m in Gloucester County. But Cumberland County is the next town next to me. And it’s the poorest county in the state. So for them to come in and say I’m supposed to get this much money, it’s just not feasible.

It’s just a faulty system. I don’t care if anybody wants to come in and audit my books. If I made a mistake adding or subtracting, fine. I’ll pay the difference. If I made a mistake, fine.

And the thing about signing this form that they’re talking about—I didn’t—You don’t think it’s—And they’ll sign the form because if you don’t sign the form, they lose the first three months, which started like mine—fiscal year ending in 1994. Then they would pick up the next three months. And that would continue on until the audit was over. But I didn’t know that when I signed the papers. So I’m stuck now. My audit goes from 1994 to 1997. The whole time that—I’ve been waiting two years to finish my audit. I’m going to owe penalty and interest on this money. That’s what happens when you sign that form. Maybe someone should explain it a little better to us.

Thank you. I don’t want to take up too much time.

ASSEMBLYMAN CARROLL: Mr. Chairman, just a couple of comments and a couple of questions.

ASSEMBLYMAN GREGG: Go ahead.

ASSEMBLYMAN CARROLL: I think we have to recognize that small businesses, for a long time, have served as the backbone of our economy here in New Jersey. And in our quest for more revenues and our quest for the $100 million revenues that the State government believes is out there, we’re
trampling on the rights of the men and women who are pumping this local economy of ours. And I think we have to take a step back and say, “What are we really looking to accomplish here?” If it’s to drive the small businessmen and -women out of our state, then we’re doing a heck of a job.

And I really want to hear from Treasury at some point, because there’s two sides to every story. Sometimes there’s three. But this is the second time.

And I know, Guy, you’ve received some comments and some phone calls from individuals that are afraid to come here.

Now think about that concept. Here in New Jersey, here in America, where we enjoy this wonderful democracy, people are afraid to testify for fear of retribution. Whether it’s a real fear or an imagined fear, it’s a fear. And we’ve had the same thing at the Federal level. We had the IRS agents who were just like warlords, beating up the local businessmen and -women with audits. And we’ve seen that, kind of, come around in the last two years. And perhaps it’s time to really look at the overall structure of Treasury and find out what we’re doing right. We’ll keep it and improve upon it. What we’re not doing right, let’s just junk. And let’s make sure that the honest men and women of New Jersey are not being penalized.

But I’m going to say it again, and I’m going to be repetitious about it. If we find that there are men and women who are not being honest, let’s come down on them very hard. Let them go to jail. Let them forfeit their businesses. Let them pay the proper tax and penalties and whatever liability that’s out there.
But I got to tell you. I just read an article about an individual who was presented -- a small business owner from Union City, who was presented a tax bill for $200,000. He was so overwhelmed with it, he killed himself. I mean, think about that. Isn’t that troubling? Isn’t that horrifying? There’s got to be something that we could do to bridge the gap about the reality and perhaps the fantasy that’s out there -- what’s owed and what is not owed. And if there are the cheats, let’s track them down.

The concern that I have is that the average businessman or businesswoman isn’t aware of any recourse they may have coming to the State Legislature, maybe the appeals process. We’ve got to find a way, Chairman, to outline, for an individual who is about to be engaged in an audit -- to let them know, full disclosure, full information, as to what this audit entails, how long it’s going to entail, what the costs are, what the parameters are. And frankly, if there’s an appeals process, let’s engage in that appeals process as soon as necessary.

But again, if there’s wrongdoing, let’s curtail it, but if there’s not--

And we’ve heard three or four horror stories here today. I’m sure there’s more that are out there. I’d like to hear from Treasury as to the counterpoints to the horror stories we’ve heard so far.

But thank you very much for your courage for coming out. You’ve taught us an awful lot.

MR. MARSH: I just want to make one comment.

I’m sorry I forgot to mention that I hadn’t finished my audit yet, but I paid one accountant, a woman who had experience with the Division of
Taxation, already, $2500. She went through every receipt for my -- they call it an--

This isn’t my regular accountant. This is another accountant, another CPA, that I paid just to do this. And my other accountant -- I’m probably up to $5000 in fees already. To prove that I don’t owe any money could cost me over $10,000. If I have to go to court, I know it’s going to cost me over $10,000. But that’s where you have to go if you feel you’re right, which I do. I feel I’m right. I pay my taxes. I didn’t cheat anybody.

So this is what’s wrong. Where do I recoup my money from? Is the Division of Taxation accountable for my fees? Can I sue them? Can I sue the State of New Jersey to give back my $15,000 that I wouldn’t have had to pay? That’s what’s wrong about this.

ASSEMBLYMAN O’TOOLE: It’s something we should look at.

ASSEMBLYMAN GREGG: Thank you, Mike.

Thank you, Vice-Chair. It’s about the third time we’ve heard the question of whether or not the Treasury will have an opportunity. The methodology that I’m prescribing for this Committee, and this is the first step, is to hear public comment. I think it is important that we get the public input on issues that affect them. After that public comment can be assimilated, certainly we would request that Treasury does come in front of this Committee in response to that. They will have a fair and open opportunity to do that. And I think that’s important.

Some of these issues may be able to be dealt with quickly. Others may have to require legislative changes. I would hope the first method happens faster, but there’s no question that I share the concern of the Vice-
Chair, and I’m sure all the members of the Committee, that it is very easy for us, as elected officials at a statewide level and at a Federal level, to somewhat forget what Main Street looks like, and sometimes forget what the individuals go through every day to make a living. I happen to be a small businessperson, so I hope I don’t forget, ever.

And I am sensitive to the fact that when you have no liability for that $1200 bill, you don’t have a no liability, Georgette, and you’re not going to have a no liability. How we answer those questions is difficult. We have to have responsible citizens that pay their taxes appropriately and on time. But we also have to have a government that is flexible enough to know that it isn’t a one-size-fits-all situation -- the tie you buy in Macy’s isn’t the same price today as it’s going to be next week or Columbus weekend -- and, ultimately, the tax liability on whatever that may be. And a tie is not sales tax liability, but certainly it’s an income tax issue to a retail store.

That all has to be in the system. I think this Committee is going to look hard at how we can come up with a fair way to do that because there’s just been too much of this in the newspapers.

Small businesses are struggling. I believe, today, they don’t have the big accounting companies to back them up. They don’t have environmental agencies behind them to help them. They don’t have all the consultants that some large companies do. And, quite frankly, they don’t have the ability to just write off losses. Their losses are their future retirement.

So I share your concerns and commitment, Vice-Chair, and the rest of the members.

Bill, do you have any other testimony on this issue?
M R. C L E A R Y: Just our Chairman, the President of the New
Jersey Licensed Beverage Association.

Mr. Ardire is going to take two minutes to wrap up.

J O S E P H   A R D I R E: Less than two minutes.

A S S E M B L Y M A N   G R E G G: I'll use the appropriation two minute
bell then for that, and we'll monitor you. (laughter)

M R. A R D I R E: Mr. Chairman, as you're aware, being in the
business, we have third-party information. The liquor wholesalers and the beer
wholesalers report our purchases. And I believe that if your purchases are
confirmed as being accurate, then the Division of Taxation should walk away.
That should be the end of it. As long as your purchases jibe with the third-
party information, the Division of Taxation shouldn't have any right to tell you
that you should have a 300 percent markup on beer or a 250 percent markup
on food and a 500 percent markup on wines. That is absolutely ridiculous,
and I don't think that they should be conducting-- Like Mr. Rescinio says,
they don't conduct audits, they do a review.

That's all I have to say.

A S S E M B L Y M A N   G R E G G: Thank you, Joe.

Thank you, Bill, for bringing all these folks here today.

Thank you to all the CPAs in the audience, who are here, for
taking time away from their busy tax season.

M R. C L E A R Y: Thank you, Mr. Chairman.

M R. A R D I R E: Thank you, Mr. Chairman.


Welcome, Wade.
Wade Avondoglio: Thank you, Mr. Chairman.

Mr. Chairman and members of the Committee, my name is Wade Avondoglio, and my family and I have a restaurant in northwest New Jersey called Perona Farms. We've been in business for 83 years. My great-grandparents started it. And we consider ourselves one of the pillars of the community in Sussex County.

I'm here to testify about a witch-hunt which occurred back at Perona Farms back in 1996. We had the-- We got a letter, first of all, addressed to Perona Realty, which is our real estate company, stating that we made lots of purchases of alcoholic beverages, but we didn't report any sales. My accountant immediately called up the Division of Taxation and said, "The number that the wholesalers have been reporting to you is Perona Realty, and the sales company is Perona Enterprises. That's who operates the business. So all those sales that were mistakenly put on the wrong taxpayer ID number should have been on Enterprises." They said, "Well, that explains why you didn't have any sales for realty." And they said, "But we're going to audit Enterprises anyway."

So they came up. They sent us a letter. It's in your packet of the documents that they wanted to see. They wanted copies of the corporate business tax from 1991 through 1995; copies of the Federal returns, '91 through '95; copies of the office returns for '93 through '95; W-2s and W-3s for '93 through '95; litter tax returns; bank statements with canceled checks, '93 to '95. I mean, it took an enormous amount of time to get all this stuff ready for when the auditors were coming to my place of business.
When the auditors did show up, there were two of them that came. They spent two days in my building. My accountant was there with them the whole two days. Then they said they wanted to spend-- After two days they found absolutely nothing that they could charge me for. We have records of everything. They couldn’t find a penny that was owed to the State.

After two days, they decided to go down in my accountant’s office. Down there they found two bills that he had copies of, which -- I had purchased some china, in 1995, I believe, from a company in New York out of the Bowery. I paid the bill to the china company. I did not pay sales tax. Sales tax was not on the bill. I, I guess negligently, did not pay the sales tax on it. It was out of state, so I just paid the bill. They came, they found those two bills, they ended up charging me about $600 in fees. My accountant’s bill for the three days that he spent with them was well over $1800.

Now, I call it a witch-hunt because after two days, they couldn’t find anything. After three days, they found a small bill that they charged me $600 for. I mean $600 is not the issue here. It’s the time, aggravation. They should go after the people who carry a cigarette box, or whatever, as their cash register.

For people like me-- They also told me that in all the years that they’ve been doing the reviews, I had the best records that they have ever seen. We pride ourselves. We’ve been in business 83 years. We plan on being in business another 83 years. And for them to come up and just annoy us is ridiculous.

I’m also on the Board of Directors of the New Jersey Restaurant Association. We have had numerous meetings with the Department of
Taxation -- the Restaurant Association has. And they've listened to us, but you hear the horror stories. So apparently, what they're listening to isn't helping.

In closing, I just want to say that why they did the audit on Perona Enterprises, I don't understand. They wanted to come to do the audit on Perona Realty. We explained the situation to them, and they still did the audit, which is beyond me.

That's all I have to say.

Thank you, Mr. Chairman.

Any questions?

ASSEMBLYMAN GREGG: Members? (no response)

That was very succinct. I think your point, the way it is -- that your liability to the State was only one-third of your liability to your accountant, which is a very valid point. It may be quick and simple, but I think it's an excellent point.

I thank you for taking the time to come here.

MR. AVONDOGLIO: Thank you.

ASSEMBLYMAN GREGG: Earl Hall, Chairman of the Leadership Council, National Federation of Independent Business.

EARL HALL: Thank you, ladies and gentlemen, for having me here today.

For those of you who may not be familiar with NFIB, which we've been throwing the initials around, is the National Federation of Independent Business. We have approximately 12,000 in the State of New Jersey. All of these are independent business owners who employ lots and lots of your constituents.
We've had quite a long session here this morning, and I'd like to just be very brief in a comment of personal experience, but it represents stories that I hear from members that I associate with through the Chamber of Commerce, through the Rotary Club, and through NFIB and my general business association.

I had a business card left in the door of a business that I closed because it wasn't doing properly -- from Taxation. It said, “Please call.” I called, and the investigator, whose name was on the card, said, “We want to get together with you because we think you’re not paying your sales tax.” I said, “Okay. Let’s set a time.” He said, “Okay. Give me your Social Security number and your home address.” So I said, “You know, we’re trying to set an appointment here. What does it have to do with my personal Social Security number and my personal address?”

He immediately went off on me. “You’re withholding information. You’re--” I can’t remember his exact words but, “we’re going to close you down. We’re going to seize your bank accounts. We’re going to file a list pendent in the courts to tie you up because you won’t give us your personal information.” I said, “What does that have to do with the corporation? The corporation has obligations. The corporation has a number. You already know what that number is.” He said, “Oh, well you never even obtained a sales tax number.” I said, “Well, how come I have a sales tax number in my files that I obtained from the State of New Jersey?” He said, “Well, that can’t be.”

Well, the point that I really want to make here is that I think their tactics are less than professional. I’m sure Mr. Thompson, and he’s here today, shudders when he hears stories like this and the stories that preceded my
appearance here. But the way things go here-- The process is really a triumph of hope over reason. That’s what we have today. I believe, according to the comments that were made here today, this has to be changed.

I have only a couple of other requests to make here today. And that is that you continue to have broader hearings not just on taxation, but on other overregulation issues. Small business can testify to this from one end of the spectrum to the other. It can include overzealous zoning officials. There are unfair taxes on small businesses in the way of you pay more for your telephone; you pay more for your insurance; you pay more for banking; you are not allowed, by State edict, to get interest on your checking account -- on your business checking account, and some of the business checking accounts carry large balances.

We suffer a lot as small businesses. And I’m glad that you’re focusing your attention on it.

Thank you. And I hope much success in your future.

ASSEMBLYMAN GREGG: Thank you, Earl.

Questions? (no response)

Thank you.

James Evans.

I want to make sure I get my accountants out of here. I want you to save money for New Jersey taxpayers.

JAMES B. EVANS JR. CPA, ESQ.: Good afternoon.

My name is Jim Evans. I’m a trustee of the New Jersey Society of Certified Public Accounts. The Society represents over 14,000 New Jersey
accountants in the business industry, public practice, education, and government service.

I’d like to thank, on behalf of the Society, the Committee and Chairman Gregg for the opportunity to talk about simplifying tax compliance and collection.

First of all, I want to stress that the Division of Taxation, the department of Revenue -- the Division of Revenue, the Department of Labor all have, I think, extended their hand and made a concerted effort to have a good working relationship with the CPAs, the tax professionals with whom they deal.

We’ve had ongoing conversations with the Division about the cash audit programs. I think, in the early phases, there was a learning program that both taxpayers and the Division of Taxation were required to go through. I think there are probably still some lessons to be learned, but I think there is a true effort, certainly, from Director Thompson’s office on down, to make a concerted effort to improve that audit program. I think it’s a difficult task, policing the cash audit business. And I think the efforts early on may have yielded some unusual, unfair results. I think they have been addressed. I think there’s an ongoing training program that the Division of Taxation has undertaken for both supervisors and at the field level. I hope that that bears fruit and that the stories that you’ve heard become the exception rather than, perhaps, the earlier rule.

Having said that, I think the Division of Taxation, and all the tax administrators, should be commended for some other administrative programs. The Gateway Program, or the one-stop shopping business initiative that was
begun several years ago, is beginning to bear fruit, making it easier for New Jersey businesses, particularly small businesses, to register, with the Division of Taxation and other State agencies, their efforts to consolidate tax reporting forms, making tax compliance by taxpayers less burdensome. Electronic filing and electronic payment of taxes, I think, are coming on-line to make a more effective and more efficient tax administration.

I think there are problems -- we heard them discussed briefly earlier this morning -- with a transition to the Division of Revenue in handling the overwhelming amount of paper tax filings that are still required. The division of responsibilities between the department of Revenue and the Division of Taxation and the Division of Revenue is posing challenges. Hopefully, those challenges will be addressed.

Processing of returns is -- hopefully becomes more efficient with a single stop. However, it also poses the risk of a bottleneck. That bottleneck can result in delays of refund claims. Small businessmen in particular have a hardship if some refunds are delayed. And the State can incur substantial interest expenses if these returns are not properly and efficiently processed.

I think the Division of Revenue’s efforts should be redoubled, as far as efforts in getting additional personnel technology and funding.

What I’d like to do is suggest, perhaps, some broader concepts that the Committee might consider.

April 17 is the tax filing deadline this year. It’s a Monday. And I think that it’s appropriate to consider that approach as the Gross Income Tax Act. It started out in 1976 as a simple low rate gross income tax, but over the past 25 years, with statutory amendments, regulations, judicial interpretations,
and administrative guidance, it’s become, in itself, a complex tax law. And I think that the opportunity—One of the primary purposes for the Gross Income Tax Act, initially, was to uncouple it from the complex, unfair, and abuse-laden Federal Income Tax Act of the time.

Federal tax reform, I think, has advanced, and we should now be considering whether it makes sense for New Jersey to piggyback the Federal tax bill. Simplification, by having a single income tax in New Jersey rather than a separate, independent system, may be the ultimate in regulatory reform. We can do away with a number of the duplicate regulations that are required to administer the gross income tax and allow taxpayers a better understanding by understanding a single tax system.

Albert Einstein had noted that there was nothing more difficult to understand than the income tax. He was a New Jersey resident before there were two income taxes to deal with. You could only wonder what he would think now.

Three other brief comments. One has to deal with the residential real estate property tax relief programs. Real estate property relief has been an issue—a goal of the Legislature. New Jersey has three separate programs, three separate returns or applications to be filed. One is due with your income tax return. Many taxpayers are not going to be required to file income tax returns because of the recent reforms and filing threshold increases that were passed last year. In addition, we have the NJ SAVER Program, which now has a June 15 application date. And we have the homestead property tax reimbursement application for December.
Each of these applications, if late, can mean a loss of benefits to those who, perhaps, are an (indiscernible) taxpayers. And some consolidation or consideration has to be given to the burden of taxpayers and on tax administrators of these compound programs.

In addition to taxes that are administered by the Division of Taxation, there are also payroll taxes administered by the Department of Labor. Consideration should be given to extending the Taxpayer Bill of Rights that was enacted in 1993, which assures taxpayers fair and equitable administrative treatment, and which establishes rights and obligations of the Division of Taxation regarding procedures for refunds, collections, and audits. These should be extended to the payroll tax examinations that the Division of Unemployment and Disability Benefits Insurance conduct. Many of these audits—Again, it's very similar to tax audits. The procedural and administrative safeguards that were appropriate for the Division of Taxation seem to be equally appropriate for the labor audits.

And finally, with respect to Labor—Another set of rules, the worker classification rules for Federal income and employment tax and for New Jersey income tax. There is a single set of rules for worker classification. However, for employment taxes, there is a second set. An individual can be an employee for employment tax and income tax purposes, but for New Jersey labor employment tax purposes, can be classified as a worker, while an independent contractor for all other purposes. This causes employers, workers, a tremendous amount of hardship in determining their classification and the tax obligations that they have. And consideration should be given to coordinating those rules with the Federal and other State rules as well.
With that, I would like to again extend the thanks of the Society for the interest of this Committee in tax and regulation oversight. If there are any questions, otherwise, I’d be happy to--

ASSEMBLYMAN GREGG: Members?

MR. EVANS: If not, I thank you.

ASSEMBLYMAN GREGG: I have a question.

MR. EVANS: Oh, yes, sir.

ASSEMBLYMAN GREGG: Well, sir, we had appropriations for five years. It became more and more apparent that our income tax, due to its progressive nature, was collecting more and more of its funds from the higher income individuals. There, of course, is the philosophical point of view of maybe that’s a good thing because they have a greater capacity to pay, but then there’s also the concerning side, which is that you’re placing your income at a higher -- smaller group, which is a higher risk.

Your comments earlier were reflective of the complexity of the State income tax where it was supposed to be a very simple tax, and now it is very complex because of that nature. Do you advocate a flatter, simpler, tax again, which--

MR. EVANS: The State Society undertook a white paper evaluation of the State tax system. And it looked at simplifying the tax system, primarily by piggybacking onto the Federal system, taking, for instance, a Federal tax benchmark like adjusted gross income and using that as the base with which to compute the New Jersey tax. Some of the virtues of that is the adjusted gross income is a fairly stable tax base at the Federal level and would
not, to a large -- to advocate to any great degree, some of the revenue prerogatives that the State should retain.

On the other hand, in looking at adjusted gross income, it was possible, at least based on 1993 numbers, for the State to have a reform that was revenue neutral, with rates between 2 and 4 percent. Who would be the winners? Who would be the losers of reform? A change in a tax base are things that I think require greater study. But I think that there is the potential, certainly, for a much simpler administrative tax system. Whether the burden should be shifted among taxpayers is obviously a decision that I think this society would rather leave to you all.

ASSEMBLYMAN GREGG: Jim, if you would get a copy of that white paper--

MR. EVANS: I’d be happy to provide that to the Committee.

ASSEMBLYMAN GREGG: --and forward that to the Committee, I would appreciate that.

ASSEMBLYMAN CARROLL: Jim, if I may.

ASSEMBLYMAN GREGG: Assemblyman Carroll.

ASSEMBLYMAN CARROLL: I’m looking over your concept of a piggyback tax, and I’m enthralled. Back, of course, when the New Jersey gross income tax was imposed, the Federal income tax was a -- what was the line, I think, George Will used to say, rococo tax? It went all over the place and -- deductions and exceptions and such.

With the reform of 1986, which is still substantially in place, the code is, at least in theory, a lot fairer.
Would you propose a New Jersey adjunct, whereby we just simply took a percentage of whatever your Federal tax liability or your Federal AGI is and substituted that for our present existing code?

MR. EVANS: There are a-- This is one of the alternatives, again, that the white paper explores. I’d be happy to share it with the Committee -- what is the appropriate place to tie into the Federal tax system. Is it tax liability? Is it adjusted gross? Are there, for policy reasons, items that should be adjusted from tax -- from the Federal tax, either-- Are they required under constitutional law or some other to make some adjustments, or are there policy adjustments that the State would feel appropriate?

But certainly, as a starting point, much like the corporate business tax, it starts out with Federal taxable income and then makes State appropriate adjustments. I think that would be, certainly, an avenue to explore for taxpayer simplification.

ASSEMBLYMAN CARROLL: Certainly, when Mr. Davidoff was here beforehand, he was talking about how New Jersey small businesses are treated differently than their employee cousins would be because of the fact that they can’t deduct their share of the employer self-employment tax, deductions which apply to the Federal government. This would solve that problem, at least in theory, because your AGI already takes in those deductions and those considerations into account.

Now, if we did that-- I know I’m putting you on the spot here, but is there-- Assuming we went to a Federal AGI as the basis for our New Jersey taxes, do you have any idea what kind of adjustments would have to be made, in rates, in order to keep in revenue neutral, assuming that was our goal?
M. R. EVANS: Again, the white paper, which is based on some older numbers, quite frankly -- and I'd be remised on thanking, again, the Division of Taxation and technical people for the assistance they gave the Society in getting those numbers together-- We're looking at rates from approximately 2 to 4 percent, based on an AGI -- using AGI as a base.

I think your comments are worth noting, and we see New Jersey's tax and some of the complexities of the tax coming from an attempt to adopt some of the Federal relief programs, for instance, the ability to deduct self-employed medical expenses that the Legislature passed recently, the inclusion of the real estate tax deduction. These types of items that we see adding complexity, but argue with fairness to the New Jersey system, are things that may be already addressed to the Federal program.

ASSEMBLYMAN CARROLL: Thank you, Mr. Chairman.

ASSEMBLYMAN GREGG: Thank you, Assemblyman.

Thank you, Jim.

Paul Bontempo.

I know we have one more CPA out there, which is very enlightening. And you will be next. We just don't want to have you follow another CPA. We wanted to have a little break in the middle.

Paul, welcome.

PAUL BONTEMPO: Good afternoon, Mr. Chairman.

I'm Paul Bontempo, representing the American Forest and Paper Association. I'm here today with Bob Stegemann, who is Vice President of International Paper; and attorney Stacy Cohen, representing International Paper.
First of all, Mr. Chairman, we’d like to commend you and the Committee for conducting this hearing, and we suspect that we’ll see bigger and better things as you move forward, so our hats are off to you. Thank you very much. And thank you for giving us the opportunity to cast some light on what we think is an inequitable imposition of a particular tax, that being the tax on litter-generating products.

Quickly, I’d like to tell you about the American Forest and Paper Association. It’s the trade association, based in Washington, which represents the paper and forest products industry, as its name suggests. To put it-- To relate it to names close to home-- The Association consists of large international corporations like International Paper, Procter and Gamble, Georgia-Pacific. New Jersey-based companies include Marcal Paper and Garden State Paper, folks that you know. And our organization also includes a significant number of small, family-run businesses as well.

Why we are here is-- In 1996, as result of audits to a number of paper companies conducted by the Division of Taxation -- companies, by the way, who have been paying the tax on litter-generating products since 1986, when the tax was enacted, and compiling to the fullest extent in their opinion--

By the way, as you know, this tax is intended to fund the Clean Communities Program, which the industry, International Paper, and the member companies fully support.

However, as a result of audits, it was to our surprise and dismay a number of companies in the industry were told that they had not been paying the tax on certain products that we were befuddled to learn were subject to the tax. And hopefully, we will, as we have your attention now-- When you
hear the logic or the rationale used by the Division to include these other products into this tax, you may agree that it, indeed, is inappropriate and at a significant stretch.

And I would like, before you hear more substantive testimony from Mr. Stegemann and Ms. Cohen, I would like to mention that, on this subject, Senators Bucco and Robertson and, just as recently as this week, Assemblyman Merkt, have introduced legislation which attempts to address this inequity.

With that, I’d like to--

Bob Stegemann.

ROBERT STEGEMANN: Hello, and thanks for the opportunity to talk to you about this issue.

And I thank you for the promotion. I’m not a Vice President. I’m a Regional Manager.

International Paper has been in New Jersey for quite a while, but our presence has grown considerably with the acquisition, recently, of Union Camp, and several years before that, Federal Paper Board. So we have about 1200 employees and six converting facilities in the state, and our presence has grown. We have about nearly half a billion dollars in sales. And I think that number will also grow with this acquisition. So our presence is here.

And this litter tax, like we’ve said, is not something that we are opposed to, but we want to see it fairly applied. So I think it’s a fairly minded tax but a poorly applied tax. In the-- And we’re going to get into some real detail on that in just a moment. But, just in a general sense, we do a lot of converting with bringing large rolls of paper to bring in -- to make products like
packaging for cosmetics and that sort of thing. When these rolls come in -- big eight-foot rolls to be converted -- that roll is considered a litter tax subject item. And in our view, it should not be, at that point in time, later on in the process, perhaps, but not at that point in time. And we'll get into some of these.

But these things-- The application of the tax has been made so broad and so far up the pipeline that it dissuades businesses from wanting to do distribution in the State. For example, International Paper -- this is not the only reason, but International Paper is locating a distribution center -- a large distribution center -- half a million square feet -- million square feet, somewhere in there -- outside of the state because of the -- partly because there was a difference in cost, but a large part of that difference was due to the litter tax that will be applied to roll stock simply coming in to be distributed somewhere else, not even necessarily in New Jersey.

So I think that the tax is well intentioned and fair minded and certainly has good program objectives, but the policy objectives are not being really met -- followed in this. And we'd like to clear up and clarify just what is subject to the tax with the Department. We're in the middle of doing that with both the Department and--

Stacy.

**STACY COHEN, ESQ.**: Let me just make a comment to follow up on Bob's statement.

International Paper has no problem with its finished products, anything from point of purchase displays, fine papers, paper garments. And those are the type of items for which the tax would be appropriately levied, in its opinion. What they have the problem with are the intermediate type goods
or the unfinished type products that then go out for further manufacturing, potentially out of state for further manufacturing. They might never come back into the state.

A little bit about the tax—How tax liability is triggered, under this scheme, is you have to be what’s deemed a litter-generating product. And a litter-generating product, through the statute, is one of 15 enumerated items, paper products and household paper being one of them, along with all the others, are generally finished consumer type items. And then, in order to meet the definition, you have to meet one of a three-part test, being either a product produced, distributed, or purchased in disposable containers, wrapping, or packages. They have to be either commonly discarded in public places or of a highly unsanitary or unsightly nature, capable of being thrown in a public place. And again, I think that comports with the legislative intent to resolve what was a litter problem in this state. Then, in order for the sale to be a sale that’s subject to the tax liability, it would be a sale within the state, as defined by another section of the statute.

What has happened in the interpretation of the scope of this statute has been basically on the definition of litter-generating product— that all paper comes in, no matter at what stage, be it the corrugated roll that comes in—more so because not only as paper is included in the item, but we have had the Department obviate the entire three-part test by saying if it’s in any way strapped, banded and typically these—They’re sold by the ton, and they’re handled through machinery. If there’s a metal band surrounding these roll stocks— if that’s cut, clipped, then you meet the packaging criteria of the three-part test. And virtually everything is going to meet that test, unless it has
a reusable band or strapping. And as I’ve explained, these are typically brought in with a metal strapping. And the metal strapping, which brings the product into the litter-generating definition, is recycled -- never goes into the waste stream. It’s not something that really -- it’s our belief the legislation was ever intending to address.

Then the Department has also taken the position that an intermediate item coming in -- again, once that metal band is clipped or the product is in any way repackaged for further distribution, there's been a sale for use and consumption in the state. That’s not to say that ultimately this product may go out of state and come back as a cereal box or some other type of finished consumer product within the state, but there’s the great likelihood it never comes back into the state. And again, this is where the product, being in almost a pulp state, is still taxed.

What International Paper does have is a high proportion of its sales being roll stock and other unfinished goods. In 1998, that was roughly one-third of its sales. That will change with the new acquisitions. And again, these types of sales are for products that, by and large, are recycled at a very high rate. The industry, as a whole, recycles its products. Corrugated is, I believe, up to 70 percent industry-wide. It’s even higher within different companies.

We also would like to point out that the paper industry and International Paper -- its corrugated products are comprised of recyclable materials. So, in a way, this has been an industry that’s responsive to the litter problems, yet is being taxed at 100 percent.
Also, with regard to the locational decision that Bob had discussed earlier, one of the use -- the use and consumption issue, which we have discussed today, was something that was at issue with that facility, which was going to be merely a distribution facility, again, because the roll stock being distributed through the state would be subject to the tax. That facility has approximately 200 employees. It’s a half-million-plus square feet, so as far as the incentive to have facilities like that located in New Jersey-- I’m sure that there would be an interest on part -- discussing this problem.

Are there any questions?

ASSEMBLYMAN GREGG: Any questions, members? (no response)

So simply stated, you have two pieces of legislation that are now in process, plus you’re in negotiations with Treasury. Would that be correct?

MR. BONTEMPO: Well, there’s two pieces of legislation, and International Paper is in discussions with Treasury, and we're seeking to have a dialogue with Treasury. We have, just for the record, as all this surfaced-- Coincidentally, the regulations were on the litter tax we’re about to sunset. And so we provided comments, which were really, quite frankly, pretty much dismissed. We then went for some informal help from the Legislature. Assemblyman Bagger wrote a real good letter to then Treasurer DiEleuterio, who wrote back, pretty much dismissing our point of view. And so we hope to continue the dialogue with Treasury, but we also, fortunately, have some interested ears in the Legislature, and we hope even more after today.

ASSEMBLYMAN GREGG: Well, the litter tax has always been an issue. It comes back every five years after sun setting. I remember when
the litter tax occurred. You were around. It was really a trade-off for a bottle bill. That was prior to the recycling efforts that have happened in society, quite frankly. We didn’t recycle bottles. We didn’t recycle paper. We didn’t recycle tin cans and the types of things we recycle today. New Jersey has done a much better job in its garbage.

Unfortunately, because of the allocation of the tax off to municipalities, the Legislature has not always had the courage just to end the tax at the five year time, when it should be done. That’s the way I voted last time. So I’ll be happy to look at this. I hope the members will be, as well. If you could get us some specific information on it--

Your issue seems to be much more targeted to an expansion of the base of the tax, as opposed to the tax itself. And I think I understand it. I think the members do, too. Please give us some written information or more, if you have it, and the Committee will take it under advisement.

M R. B O N T E M P O: Thank you, Mr. Chairman.

A S S E M B L Y M A N G R E G G: Thank you.

M r. W o o d f o r d. A n d t h e n o n e m o r e.

S o m e o n e a l w a y s h a s t o b e l a s t. A n d I’ m s o r r y s o m e o n e a l w a y s h a s t o b e l a s t. B u t y o u w i l l g e t t h e m o s t t i m e b e c a u s e n o o n e w i l l b e b e h i n d y o u.

R O B E R T A. W O O D F O R D: Good morning -- or I guess, good afternoon.

B o b W o o d f o r d, N e w J e r s e y B u s i n e s s a n d I n d u s t r y A s s o c i a t i o n. I h a v e w i t h m e a C P A, w h o i s a m e m b e r o f o u r t a x a t i o n c o m m i t t e e, R a l p h E v a n g e l i s t a.
I would tell you in advance that what I am going to say today is a collection of things drawn from different members of our taxation committee. It does not represent a consensus from discussion of the committee. As it happens, we have a meeting of the committee with the Director and two Assistant Directs of the Division Friday that might have led to--

We've had a very good relationship with the officials of the Department. They've been very helpful to us over the years. And for me, that goes back almost 37 years of working with the officials of the Department. I continue to have the highest respect for the capability and helpfulness of those officials.

I will get into what will be a collection of input from the rest of our committee. And I’d like Ralph to be able to present items of interest to him as a member of our committee, first.

R A L P H   E V A N G E L I S T A,   CPA: Mr. Chairman, Mr. Vice-Chairman, and members of the Committee, not only am I a CPA, I also have a speciality in taxation. I have a master’s in taxation. And I take pride in my tax work. So what I am going to bring today would be, hopefully, solutions to issues that you and the taxpayers are trying to resolve. So I’m going to bring ideas to you. I’m not going to consider any gripes. They’re going to be strictly ideas that I think may be helpful to the Committee.

ASSEMBLYMAN GREGG: Perhaps we should have saved you for last.

MR. EVANGELISTA: What was that?

ASSEMBLYMAN GREGG: Perhaps we should have saved you for last. We always like the optimistic approach.
MR. EVANGELISTA: I suggest that we have a tax amnesty period with installment payments permitted, which is different than prior tax amnesty periods where if a person could not come up with a lump sum payment within the 90-day time frame, they cannot qualify for an amnesty -- tax amnesty. And I suggest that not only would it be for installment payments, say over 36 months, that -- and as well no penalties be assessed -- that the interest rate be primary.

The second idea would be for practitioners, as well as a CEO of a company who is preparing a corporate income tax return, to be able to access the New Jersey Annual Report via the Internet. What I have found is that -- I don’t know if you’re aware of it, but this year--

Let me take a step back here from the idea. This year, we have to send in the New Jersey Corporate Business Tax Return to the same address as the New Jersey Annual Report, which has the payment along with the New Jersey Annual Report. That goes to the same address as the New Jersey Corporate Business Tax Return. However, they have two separate envelopes. Why we cannot consolidate into one envelope, I don’t understand.

But anyway, taking a step forward with the New Jersey Annual Report form-- I know that the State of New Jersey likes this annual report form to have completed information. So us, as tax practitioners, if we don’t have the booklet that is mailed to the taxpayer, then we have to actually prepare a form, and we have to put information down that may be partially complete, which may slow down the process here in Trenton.

The third idea would be to actually -- for the State of New Jersey to come up with a standardized form to request a copy of a previous tax form.
Presently, if I want a copy of the tax return, I actually have to contact the State of New Jersey, ask them where I can actually mail in my request, and they tell me to mail in X number of dollars. That doesn’t happen too often, where I need to request a copy of a tax form. However, when it does come up, I always have to recall it in my memory files and say, “Okay, what did we do last time?” And unlike the Federal, there is no form. So if we do have a standardized form, we would always know the dollar amount and where to mail it. And I think it would actually speed up the process.

One of the problems I did have with the Department of Treasury, I guess, had to do, maybe, with the merger of the two Departments, the Department of Revenue and the Department of Treasury. I had a case -- I was dealing with some attorneys where we were trying to pay back tax liabilities. And we E-mailed in, let’s say, five years of income tax returns, and I waited eight months for those returns to be filed and processed through the Department of Revenue -- Department of Treasury.

So I had to write a letter to Mr. DiEleuterio, who actually handed it down, and thank God he processed it quickly because I had money in escrow that I had to respond to, and I needed to know how much I needed to pay off this tax liability. So he had put a gentleman on the case to resolve the problem. But it took eight months for it to be processed through the system. I was really surprised it would take that long for a prior year’s income tax return to actually get through, be processed, and the taxpayer could find out what their actual, true liability would be -- to be billed by the State of New Jersey.
So I actually had to take a step above and beyond the call of duty to get the process completed. But I think, maybe, now that the merger is complete, maybe the process -- the processing of returns may be a little bit faster.

One of the things with the New Jersey Sales Tax Division-- I don’t know if anybody has really brought it to your attention today. I really didn’t hear it, but-- We receive a tremendous amount of notices saying that tax payments have not been made. And I receive it-- I would say, within about 10 percent of my client base sends me a notice, and I look at it and say we’ve already paid it. So then I have to write a letter responding, along with the canceled checks, saying, “Okay, well we did make that payment.”

Then I get another letter from the tax clearance section that says that we still have that outstanding tax liability -- sales tax liability. As you know, each year the sales tax-- Actually, I should say that the liquor industry has this tax clearance process that they have to go through before they renew their license.

So it seems that the tax clearance section in the sales tax section may be -- not have the same computer and the same information because each time I have to contact tax clearance and say, “Hey, I’ve sent a letter.” Then they look in the computer and say, “Oh, yes. Don’t worry about it.” But in the meantime, it took a lot of time and effort on the taxpayer’s part and on my part to piece it all together to get to the proper people to let them know the payment has been made. This way we can get the tax clearance certificate so the client can have their license renewed.
Another idea here would be to allow tax payments to be made by credit card. As you know, some credit card companies do allow reduced rates, say 9 percent or 5 percent. It’s a short time frame, but a person can actually move that balance around to keep below what the State interest rate is, as well as the penalties that are assessed. So the penalties for not paying the tax and also the interest on that amount could be somewhere in the 20 percentile. Whereas, if a person was to charge in on a credit card, if they were to properly -- used the proper card, they may pay, maybe, half that rate. And the State would be guaranteed to get their money.

Another point I’d like to bring up is allowing the deductibility on the simple IRA or standard IRA, thereby promoting savings for taxpayers out there. I think the State of New Jersey really has not come up with a plan to promote individuals to save money. I know with 401K plans they do allow deductibility of that money. So this was so they could put away money -- pretax dollars. But that hasn’t come through yet for a simple IRA or a standard IRA.

When working with the New Jersey Package X -- I received it on a CD-ROM. It’s interesting. They do have a lot of tax forms there. It’s well put together, but I would just like to take it to the next step. And that is maybe you can make it so whoever processes or puts together the CD-ROM disc can actually make it so when you access the disc, you can actually put information on it, and then everything would come out typed. So maybe you don’t have to -- the people in Trenton, who are actually processing these forms, do not have to look at somebody’s handwriting that they cannot read and slow down the process, or maybe input the information incorrectly since they
cannot interpret the numbers properly, whether it be Social Security numbers or amounts on the tax returns.

Another thing I’d like to promote, and suggest we promote, would be a child care deduction because now you have both spouses working. And I think it would be a good approach to amenity here in New Jersey to help them out because child care is so expensive. It’s exorbitant, especially if you want good child care for your child. I know that-- I certainly-- I have two daughters, and I certainly would not want to risk their care by scrimping on making decent payments to a facility that is well qualified to take care of my child -- my children. So what I suggest is that if you have a child care deduction in place, maybe it would enhance the quality of child care in this state.

I would also like to suggest direct telephone numbers for practitioners and corporations of people to contact who are knowledgeable in specific areas. What I’ve found is that you can call the 609 hot line number, and you can kind of jump some hoops for a while. You could be on hold for a long time, jump hoops. And what I find is that State taxation, like Federal taxation, is absorbent with information. There is a tremendous wealth of information out there. I don’t know it. I have a speciality in taxation. I have a decent size client base, and I’ve been practicing for over 15 years now in public accounting.

So the point I’m trying to make is that I don’t know how a person on a hot line can answer all my questions. I’ve called. A lot of times they don’t have the answer. They try to refer me to somebody who knows the answer, but it just doesn’t work.
What I’d like to suggest here would be a person or persons, it would take multiple individuals, that would handle specialities with, you know, individual taxation, as well as corporate taxation, as well as partnership taxation -- maybe help out the attorneys, the CPAs, who are practitioners, who are involved with compliance, as well as the CEOs and CFOs who are trying to make sure that they comply within the letter of the law. And we are out there dealing with a gray area, and we’re sitting here saying, “Which way do we sway here?” And it would be nice that we have somebody that we could contact and that can answer the questions or maybe set up a department that could help us out.

I have found that I have to somehow get to somebody that could help me out. I might have to get to, and distract, maybe five or six individuals before I get to the proper person. So it could actually save the taxpayer some dollars by paying me less and actually save the State some money by not interrupting the people here who are working in the Division of Taxation by directing the call to that person that can handle the calls. We do have telephone numbers that are published, but they do change. I haven’t received updated telephone numbers. I got them through other people I’d have to call, but I did not receive any mailing from the State of New Jersey or whatever. But I think it would help streamline the process here.

One final point here, and that is the homestead rebate. I feel that seniors who have no income and are not required to file the New Jersey 1040 form-- I shouldn’t say no income at all, but income that would not put them into a taxable situation where they are required to file, then they would have
to file the New Jersey HR-1040 form in order to receive their homestead rebate.

Once again, to help you streamline the process here is to either give a direct credit, or how about mailing them a postcard. And then this way, a senior citizen -- let’s assume they really need the money -- doesn’t lose out since they did not file a tax form or they don’t go through this voluminous process of trying to fill out the New Jersey HR-1040 form. We can simplify it, and they can just send a postcard.

I do know that, if it’s missed, what they do is -- we have to call down in Trenton -- down here -- make numerous phone calls to try to get them their rebate. And we have to go through all types of generations. And I do it because -- and I know other practitioners do it as well, because if the senior could really use the money, and they missed out on it because they didn’t know any better--

So you can give them a direct credit or a post card. I think it would save a tremendous amount of time and effort on everybody’s part.

So I would like to thank you and also say that I would like to wish you much success in your endeavor in trying to put together -- simplifying compliance and collection.

ASSEMBLYMAN GREGG: Thank you for your time.

Any questions, members?

ASSEMBLYMAN CARROLL: If I may, Mr. Chairman, real quick.

ASSEMBLYMAN GREGG: Assemblyman Carroll.

ASSEMBLYMAN CARROLL: Don’t we run the serious risk, if we keep extending these amnesty programs every year, two or three, that people
will catch on and just simply say, “I’m not going to pay my taxes until such time as they adopt another one of these amnesty programs, and then I’ll pay it, and I can have my money and use it for the course of the two or three or four years between programs?

MR. EVANGELISTA: Absolutely. That’s one of the downside risks, but that’s why-- I wouldn’t say that every year we’re going to do it, but you just surprise -- come up with it and maybe have a window of 90 days or six months.

I think I’m more concerned with the people who are underground that you don’t know about their dollars. They haven’t surfaced. And they don’t want to surface because they’re afraid of what may happen to them, so to speak. Maybe they’ll be put in jail or fined and penalized severely.

ASSEMBLYMAN CARROLL: But my thought--

MR. EVANGELISTA: I know, it’s a double-edged sword here.

ASSEMBLYMAN CARROLL: My thought is if they’re underground is it’s probably not for want of amnesty that they’re there. That may very well be.

MR. EVANGELISTA: But you know what I’m saying. If they’re not reporting, it would be nice to bring them forward so we can put them on the rolls so at least they could start reporting.

ASSEMBLYMAN CARROLL: Oh, so it’s a sneak attack. You’ll find them next year, then. Well, that’s interesting.

Now, the IRA deductibility -- child care deductibility. That would all be solved, in a sense, if we did go to the piggyback tax that was discussed previously -- if you’re using your Federal AGIs, would that not? We already
have the child care credit on the Federal level. And we have IRA deductibility on the Federal level. So if we went to a State program of using the Federal AGI as the basis for our income taxation, that would no longer be necessary. Is that correct?

MR. EVANGELISTA: That’s correct, if you adopt the Federal Tax Code as law.

ASSEMBLYMAN CARROLL: Now, let me ask you one last question. I don’t know if this is something that New Jersey does or can do. I know the Federal used to do--

MR. EVANGELISTA: Excuse me one second, Assemblyman.

ASSEMBLYMAN CARROLL: No. Go ahead.

MR. EVANGELISTA: I just want to go back to the child care issue. That’s not part of the adjusted gross income. It’s a direct reduction against the tax.

ASSEMBLYMAN CARROLL: It’s a credit. I know that.

MR. EVANGELISTA: Yes.

ASSEMBLYMAN CARROLL: Where do they apply that? Is that on the second page of the--

MR. EVANGELISTA: It’s on the second page, correct. It’s a direct reduction against tax.

ASSEMBLYMAN CARROLL: So no matter what you do-- Let’s assume, again in the same stage, that you do have a credit for child care. Far be it from me to oppose any tax cut. But it seems to me that that’s already been taken care of--

MR. EVANGELISTA: Absolutely.
ASSEMBLYMAN CARROLL: --which would be-- My understanding-- We talked a little while ago about income bracket creep and how some people want to index our rates to inflation. That’s one of the things I have proposed in the past. I have not yet gotten the bill in this year, but I will.

Would it be an effective policy here in New Jersey to split income between married couples so as to ensure that, for example, if you make $100,000, and your wife stays home, that each one of you pays taxes on $50,000-- Would that be a way of reducing the tax burden on married couples while at the same time not imposing what, I guess, the Federal government is talking about as a marriage penalty?

MR. EVANGELISTA: It’s a good thought. I never really thought that one through, but it’s a good idea.

ASSEMBLYMAN GREGG: That’s why we have Michael here.

MR. EVANGELISTA: Keep him busy.

ASSEMBLYMAN GREGG: Assemblyman, are you done?

ASSEMBLYMAN CARROLL: Yes, sir. Thank you, Mr. Chairman.

MR. WOODFORD: I have some additional input.

The matter of linking the gross income tax to a Federal figure, particularly Federal adjusted gross income, has come up before our full taxation committee for discussion and was favored -- linking and then adjusting a percentage of Federal tax.
There are some major items like treatment of social security, the retirement income exclusion in New Jersey, and other features that, I think, most people would like to preserve.

Other members of our committee have called me to raise a number of issues that I’d like to raise with you very briefly. One, notices of delinquency-- I’ve heard the complaint that they’re often untimely, that you can have a notice of delinquency that reaches you nine months after the delinquency has occurred, if it occurred, in fact. And that, of course-- During this period of time you’ve had no ability to satisfy that delinquency, if you are not aware of it, and penalties are building on it. There really ought to be a process to notify the people, fairly, promptly, that the Division has not received something or has not received something in time so that the individual business can react to that and satisfy any claim.

On the corporation business tax, several members of our committee commented that New Jersey’s corporation business tax form is far more complex, and therefore more burdensome on small businesses than that of many other states. Other states, often, will have a shorter form, and you will file a copy of the Federal return to back that up. Much of the bulk in the New Jersey return is apparently centered in the fact that we decoupled from the Federal accelerated cost recovery system depreciation in the period of ’82 through ’93, and therefore there are adjustments that have to be listed.

New Jersey has complex tables. Many states simply have a line that indicates what your depreciation adjustment is and leaves the determination to your own paperwork. It’s been suggested that we could
greatly simplify that tax form, particularly for the sake of the small businesses that file them.

I want to add just one story, and I don’t mean that it’s representative of what is going on in the Division. It may be the squeaky wheel, but there really is a need. We would emphasize that from the other stories you’ve heard today -- to not go into a business on an audit with the presumption that whatever they have in records, they have, somehow, violated the law.

I had a call about two years ago from a small business. It was a father and daughter with a small sale of groceries. They made sandwiches, but they also sold items as wholesalers to fraternities at a neighboring college. The father first called me, then his daughter, who handled their books, called and told me all the kinds of records she had had available and made available to the auditor. The auditor ignored these.

I’d like to tell you up front that the -- that I reached a high official of the Division of Taxation, and it was straightened out. But before it was straightened out, the auditor had indicated to this very small business, in a declining area of a community, that they owed a $250,000 in sales tax and $7500 in corporation business tax.

When we reached the end of that process, the dollar amount in sales tax was zero. And they reached an agreement on the corporate tax to mostly get it out of the way as quickly as they could. This was extremely burdensome on the owner, who was elderly.

And it seems that when there are good records available, as in this case, that an auditor ought to be instructed not to try to reconstruct the
finances of the business. For example, those large salamis and chuck cheeses sold to a fraternity turned out to be reformulated, in this case, by the auditor -- figuring how many slices go into a sandwich, how much profit for a sandwich. If you had sold all the sandwiches in this small business-- And the calculation of sales tax was based upon the sale price of sandwiches, where there were clearer records and invoices available to indicate that the wholesale business had covered a large quantity of the items that were sold. This may be an aberration. It certainly says that something needs to be done, in terms of auditors moving into the field where a business, in fact, has good records, not to try to reconstruct where those records are available.

Just to add one thing to what Ralph Evangelista has said, in terms of numbers to reach in the Department-- The organization -- the phone numbers that are published for the Division of Taxation are by function, but they are not by tax. And businesses and other taxpayers, on occasion, really need to reach someone who specializes in the particular tax. So I think that is something that-- And I realize that the specialists in taxes are often in high levels in the Department -- Division, and don’t want to have to spend all of their time dealing with mundane issues on the phone. But we could have people, I think, who are trained in these specific areas of taxation who are listed by phone numbers so that when you have a problem that doesn’t necessarily go through a general list -- through the 800 number that every taxpayer in the state is trying to reach-- If you are a business and you’re dealing with corporate tax, you need someone with more specialized expertise.
I’m certainly available for questions, but those are the items that were— And I’ve eliminated others that were really covered by others who appeared earlier.

ASSEMBLYMAN GREGG: Thank you, Bob. We appreciate your time.

Mr. Evangelista, thank you for coming.

MR. EVANGELISTA: You’re welcome.

ASSEMBLYMAN GREGG: If you have any documentation you’d like to provide the Committee, we’d be happy to have that.

MR. WOODFORD: Good luck.

ASSEMBLYMAN GREGG: Joel Rosenfeld, come on up. You’ve been patient. Thank you for waiting. It’s been somewhat of a long day. All the members are getting a taste of what appropriations is like.

JOEL ROSENFELD, CPA: Thank you, Mr. Chairman. I hope you saved the best for last. I’ll go on.

I’m Joel Rosenfeld. I’m a CPA -- I’m a practicing CPA. I’ve been practicing for 42 years. I’m with the accounting firm of Mintz Rosenfeld. I limit my end of the practice to real estate and real estate taxation. I’m here as -- on the behalf of NAIOP, which is the National Association of Industrial and Office Properties. I am a trustee of the New Jersey Chapter, and I am the Chairman of the National Tax Committee for NAIOP, which is represented in all 50 states throughout our country.

And before I get into our issues, I must say that when I took the trip down here -- two hours -- I just thought about my issues because it’s been a very long time since I ever did a sales tax audit, although many of my
partners in the firm continue to handle it. And I heard all the passionate pleas of some of the restaurant owners and some of my colleagues from the CPA Society. And I do appreciate what they say. What an absolute nightmare it was when I was doing it 20 years ago. And I could write my own stories of thrown out -- basically throwing out sales tax auditors that decided to set camp in my office for two to three weeks. I could tell stories of some of these auditors that demanded doughnuts with their coffees. And I could tell stories, when I asked an auditor what they were doing the month before they became an auditor, and it turned out to be a musician. So my intent was not to come in and say this, but I certainly support them.

Let me go on with our issues. We represent the real estate industry. And NAIOP supported a very important recent case in the Supreme Court called the Koch case. And Koch prevailed in the Supreme Court.

The three issues that I'd like to talk about, and some are not necessarily Koch, are— When we get into the complexity of tax law, specifically real estate, and we are in the trenches preparing these tax returns, and my firm prepares tax returns -- probably all 50 states -- the State of New Jersey is a total nightmare. I would prefer, any day of the week, doing a New York state tax return because it’s a piggyback type of return. I’ll do a California return faster than I would like to do a New Jersey return.

We know, historically, New Jersey put in a gross income tax many years ago. I remember doing the very first one. I did it for myself. I paid $127, and we all went home. Who cared what the tax law was at that time? Now, we face a 6.37 percent rate. This is getting expensive. And because we have a gross income tax law, it becomes chaotic in preparing these tax returns.
Once again, when you’re getting into the more complicated issues-- And the complicated issues tend, very often, to fall into real estate.

So what happened here was, maybe a year and one-half ago-- I am one of the few CPAs in NAIOP. They asked me to review a case called the Koch case and asked whether NAIOP should financially support the litigation in the Supreme Court. And in reviewing the Koch case, I found out, and I’ll get into the case, that Mr. Koch did not prevail in the lower courts. Mr. Koch took it to the appellate division, and he did not prevail in the appellate division. Lo and behold, he was supported by NAIOP and a number of other real estate organizations. And Mr. Koch prevailed, handily, in the Supreme Court decision that had come down in his favor.

We in the real estate industry looked at that case and said the basis and the theory and the motif of that case absolutely applies into the real estate industry. And so we all got very excited by this case.

And basically, if I may, Mr. Chairman, I would like to take you through the issues. Before I get into the Koch case, one of the other issues-- And then I’m going to take you through. I’m going to make you, if I may, a developer -- owner of some of these office complexes -- industrial office complexes that are all over our state. Real estate is a major industry here in New Jersey.

Okay. You’re a real estate developer and you buy an office complex and you operate that complex. And let’s presume it’s your only complex. And you get losses. You get losses as you do on the Federal basis. Federally, you can’t deduct that loss unless you set it off income. That’s fine. That was the ’86 Tax Reform Act. In New Jersey, you get a loss, forget it. It’s
gone. Lost forever. Federally, I can carry it forward. I can use it when I sell my property, or I terminate the ownership of the property in other shapes and forms. That’s pretty fair. In New Jersey, forget the loss.

The next thing is, suppose, Mr. Chairman, that you happen to get into trouble with your piece of real estate. And you go to the bank, and you do a workout. And the bank says, “You know, you used to owe us $4 million. You can’t operate the property this way, so what we’re going to do is what is known as a cram down. We’re going to lop off some of the principal of that debt. And from $4 million, we’re going to take it down to $3 million.” Well, federally that was a taxable event but with tax relief provisions, because in 1993, President Clinton knew when the real estate industry had gone down into the ’80s and early ’90s that if we taxed these taxpayers on the cancellation of their debt not only were they down and out and bankrupt, but we’d be kicking them in the head further. Mr. Clinton proposed a bill to give tax relief to these people that have cancellations of debt. For example, if you’re insolvent, you will not pay tax. If you are bankrupt, you will not pay tax. However, if you are solvent, you may take that income and reduce the basis of your property. And what that effectively does is, down the line, when you sell that property, you’re going to pay the gain then.

The State of New Jersey has been totally unclear on these issues. I have read the cases. We, as practitioners, scratch our heads on how to handle this. There are taxpayers that are taking positions that are not right. There are taxpayers taking no positions. And yet, the State stands back and says, “We follow Federal in almost all cases.” However, I have found that they have taken very inconsistent positions in Federal. That’s cancellation of debt.
Now, let’s move on. You own a property. You’ve taken the losses. You’ve taken depreciation, federally, and now you sell your property. The State didn’t allow the losses. Effectively, they didn’t allow you depreciation because when you take Federal property and you take your cost, less your depreciation, you have what’s called an adjusted basis. And you match your selling price to that net book value or adjusted basis, and the Federal taxes you on that gain. It’s equitable. New Jersey’s says, “We take the same position, and therefore we want the same gain.” But wait a minute folks. We didn’t get the losses. We didn’t get the depreciation. It is unfair. So along comes Koch.

Now, Mr. Koch’s case was that he was a partner in a cable TV deal. Mr. Koch invested $75,000 to buy his partnership interest. He ultimately sold it for $125,000. Mr. Koch, on his $75,000, took $218,000 of losses, while he held his partnership interest. When Mr. Koch sold his interest, Mr. Koch not only recaptured all his losses, but he also -- the $75,000 that he received, and he paid the government a handsome sum of money. That’s equitable.

State of New Jersey came along and said, “You know, Mr. Koch, you got to pay on the same basis as the Federal.” Koch objected. He said, “I never had the benefit of these losses. I should only pay the difference between $125,000 and $75,000, which is $50,000, not on $200-and-some-odd thousand dollars.

Mr. Koch, once again, took it to the lower court, lost, went to appellate and lost, went to the State. The opinion came down on Koch, which I thought was an excellent opinion. The judges had, basically, three issues. The first issue was whether the State of New Jersey adopts the Federal method
of tax accounting, which incorporates the Federal tax benefit rule. And for some of you that don’t know what the Federal tax benefit rule is, I’ll take a second and explain it.

It’s very simple. “I don’t give back what I don’t get. If I take losses and I make gains, then I’m going to pay on my gains.” It’s the Federal tax benefit rule. But heck, don’t tax me on something that I never had a benefit of, because if I bought the building for $100 and sold it for $100 I had no economic benefit. Therefore, I should pay zero tax. However, if I depreciate the building from $100 down to $50 and sell it for $100, I have a $50 gain. And that’s fine, federally, and that would be fine if New Jersey allowed us all the losses, but they don’t. So the learned judges came up with the Federal tax benefit. They said Koch did not have Federal tax benefit.

The second issue was recognizing the Federal principal of allowing tax-free return of your capital. That’s the example I just gave you. “I spent $100. I got back $100.” That’s return of capital. That’s not a gain. The next dollar is a gain.

Thirdly, in whether -- computing gain or loss on disposition of property, does the taxpayer use the Federal adjusted basis, that’s cost less depreciation, or does he use cost when depreciation is not allowed.

The Court reached a decision to the fact that Koch was entitled to Federal tax benefit. The fact is that he had a return of capital, which was tax free. And the fact of the matter is, in reading the court case, he was certainly entitled to have his return capital, or if he didn’t use his losses, not certainly to pay tax on it.
Now, it’s my experience that certain taxpayers were very excited by this. They said, “Well, we’re going to file amended tax returns. We reported it wrong, based on the Koch case.” And nobody knew what to do with this thing. Practitioners stood for quite a while until Treasury came out-- And as practitioners, we all get this -- I’m sure you’re familiar with it -- State Tax News. And if I may read it to you, it says, “On January 14, 1999, New Jersey’s Supreme Court, in Sidney Koch v. Director, reversed a long-standing judicial doctrine, that when a New Jersey resident disposes or sells their partnership interest, they may use their Federal adjusted basis in the partnership in determining gain or loss New Jersey purposes.

In its finding, the Supreme Court stated, “that the intent of the gross income tax statute was to,” and I emphasize, “tax economic gain, not return of capital.” The Court further stated that, “a taxpayer must use their Federal method of accounting in determining gain or loss as directed.” As reflected in the facts in the Koch case, applying one’s Federal method does not always result in the use of a Federal adjusted basis, but may require the use of a New Jersey adjusted basis to reflect the economic gain. So far, it sounds good.

“Although the Supreme Court’s decision in Koch dealt solely with the sale of a partnership interest, the Division of Taxation is not taking such a narrow view. The Division is of the opinion that this decision may also be applied to the sale or liquidation of a sole proprietorship or to the sale of rental property not held by a business entity” -- almost all real estate is held in a partnership form, a businesses entity -- “whose income or loss was reported as net gains or income from rents, royalties, and etc.” And here’s the key. It’s the
last line. “The Division does not believe that this opinion extends to transactions by a partnership or sole proprietorship in the day-to-day operation of its business.”

Now, what this says to me is one thing. I think the Supreme Court decision had come down and said, basically, if I may use the analogy, “Hey, folks, you can run a Chevrolet down the New Jersey Turnpike, and that’s fine.” And Treasury turned around and said, “You can run that Chevy down the New Jersey Turnpike, but it better be a blue one and no other color.”

And I think that this is a gross injustice in this particular case because what Treasury said -- sell the partnership interest. Well heck, if -- Mr. Chairman, yourself and myself are partners in a piece of real estate, we normally would sell that real estate, but we’re going to get creamed by the State of New Jersey. Well, let’s sell our partnership interest. We can defeat that. But it is not real that we’re going to sell a partnership interest in real estate because that’s not the way the real estate industry works. They buy bricks. They buy dirt. They don’t buy partnership interests.

Therefore, in summary, I think it behooves this Committee to look long and hard at this issue. And NAIOP is prepared to move ahead to further see that there’s equity -- that somehow we can get the Koch decision, which, in substance, applies to the real estate industry, and not solely in a narrow view of the sale of a partnership interest.

I thank you very much for your attention.

Any questions?

ASSEMBLYMAN GREGG: Thank you.

Assemblyman Carroll.
ASSEMBLYMAN CARROLL: Just one.
Would you prefer it if New Jersey were to permit loss carryovers?
MR. ROSENFELD: Well, I heard a lot of testimony here today about piggyback tax-- Start with the Federal AGI. I think if we had that form of taxation, we would not have these problems. I would not be sitting here testifying today. I’ve had calls from New Jersey -- from New York taxpayers, who sold property here in the state -- who just happened to question me. They said, “Heck with New Jersey, I’m not paying that. That’s unfair.” I’ve had people call me that won’t do business in the State of New Jersey because they know they’re going to get creamed with a New Jersey tax.

And in answer to your question, if we had piggyback taxes -- solve a lot of problems.

ASSEMBLYMAN GREGG: Joel, I thank you.
ASSEMBLYMAN GUSCIORA: We have a question over here.
ASSEMBLYMAN GREGG: Oh, I’m sorry.
ASSEMBLYMAN GUSCIORA: It’s not a question, just a comment.

I just wanted to thank the Chair and commend him on these excellent hearings. It’s been very informative for me. And I really appreciate the testimony that all the witnesses have given us today. And it certainly gives us food for thought so that we can work. But again, I want to commend the Chair for hosting these hearings.

MR. ROSENFELD: Thank you very much -- excellent job.

ASSEMBLYMAN GREGG: I’d just like to thank the Committee for doing a marathon today. I expected it to be a little long, but four hours is
a little bit longer than I expected. I’d like to again thank them for their time and diligence.

I’d like to thank the members of Treasury for spending time with us as well and to remind them that they will certainly have an opportunity to come back in front of this Committee and make comments as soon as we have all of the comments put into readable form.

So I’d like to thank them and all the people who participated today. I’m sure all the members share my amazement on how many issues we touched today. I have to admit, my head is somewhat spinning with the diversity of the issues, but that’s what the purpose of this Committee is. This is step one, and we look forward to step two.

Thank you for your time.

Committee ended.

(MEETING CONCLUDED)