STATE OF NEW JERSEY

DEPARTMENT OF THE TREASURY

DIVISION OF TAXATION

A FEASIBILITY STUDY

(Pursuant to Senate Concurrent Resolution 3024)

The Optional Double Weighting of the Sales Factor in the Corporation Business Tax Allocation Formula

Prepared by the Research and Statistics Section

Division of Taxation

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LETTER OF TRANSMITTAL

TO THE LEGISLATURE OF THE STATE OF NEW JERSEY:

A feasibility study of the optional double weighting for the sales factor in the Corporation Tax Allocation Formula is herewith submitted, pursuant to Senate Concurrent Resolution (SCR3024), filed January 19, 1978.

Double weighting of the sales factor would result in a substantial reduction in corporation tax for a small number of corporations. A major portion of all corporation taxpayers would not be affected. However, if use of double weighting is optional, the revenue effect would be substantial resulting in an estimated net loss of $19.3 million based on the 1975 income year before adjustment for prepayment losses the first year. If use is mandatory, the estimated loss would be $12.7 million. Although it has been claimed that the change would generate increased corporate activity and increased corporation taxes, there is no evidence to that effect.

New York and Massachusetts are presently implementing such a change in corporation business allocation. Tax officials in both states advise that sufficient time has not elapsed to adequately appraise its effect.

Respectfully submitted,

Sidney Glaser

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Director
Division of Taxation

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SUMMARY OF FINDINGS

AS AN INDUCEMENT TO INDUSTRY

1. The probability is slight that location decisions will be favorably influenced by a double weighting of sales in the allocation factor.

2. Some location decisions will be adversely influenced by a change in allocation factors.

3. The lighter weight given to property and payroll in the proposed allocation factor are insufficient to counterbalance the relatively high costs of labor and property in this State.

4. There is no evidence to indicate that the proposed formula will expand the Corporate Tax Base.

5. Our research indicates that industry prefers uniformity of allocation among states, and views a change from standard allocation formula as an annoyance.

IMPACT UPON STATE REVENUE

1. Increased administrative costs would be expected to result from increased audit activity.

2. The revenue effect is substantial. Calculations for all allocating corporations for the 1975 income year (1976 collections) indicate a reduction of $16.1 million in net income tax for 3,937 corporations. Application of the same optional allocation formula to net worth would reduce the corporation tax by another $3.2 million--bringing the total tax reduction to $19.3 million before adjustment for prepayment losses during the first year.

   Approximately 81% of the calculated corporation tax reduction would apply to 200 large multi-state corporations. Some examples are included.

   Growth in corporation income, net worth and tax since 1975 suggests tax reductions higher than the $19.3 million calculated for that year.

I. PURPOSE OF THIS REPORT

On January 19, 1978 Senate Concurrent Resolution No. 3024, requesting the Division of Taxation "to investigate the feasibility of the optional double weighting of the sales tax factor in the Corporate Income Tax apportionment formula and to report to the Legislature its findings and recommendations as to the implications such an allowance would have on State tax revenues, and the inducements it might create for increased industrial investment in the State of New Jersey" was filed with the Secretary of State. This represents compliance with that resolution.

II. WHY ALLOCATION?

For the same reason states can tax all income of individuals, wherever earned, they can also tax all income of domestic corporations, wherever earned. Similarly, for the same reason states can tax non-resident income only to the extent that it is earned in that state, they can tax foreign corporations net income only to the extent that it can be brought into their taxing jurisdiction.

There are three usual means of arriving at a state's proportionate share: (1) separate accounting, (2) assignment of particular types of income that can be said to be earned in a particular state to that state, and (3) apportionment by a mathematical formula.

The larger part of business income for a multistate corporation which might consist of a wide assortment of various activities which cross state lines in a manner not measurable within an integrated operation cannot be satisfactorily assigned by methods (1) or (2) above. In order

to devise an equitable system of dividing this income for taxation purposes, all states that have corporation income taxes have apportionment formulas. It is usually the case that states allow domestic corporations to allocate in order not to place such corporations at a competitive disadvantage.

III. DIVISION OF CORPORATE INCOME - HISTORY

As early as 1921, the National Tax Association set forth model taxation acts. In 1922 the income division sections of the model business tax act were revised to bring their provisions more closely into accord with State practice. It was concluded that if uniformity was to be attained, the proposals would have to be tailored to fit the views of the States.

This conclusion has colored all subsequent efforts to achieve uniformity of income division. The major concern by the mid-thirties was the creation of an acceptable apportionment factor. The equally weighted property-receipts-payroll factor formula had the widest support from the states. (A four-factor formula, property + payroll + receipts + receipts /4 was seriously considered by the National Tax Association in 1938. It was eventually decided against because its adoption would require too many changes in state laws.)

In 1957, hopes were raised that the states could solve the problem of equitable income distribution without Federal assistance, when the National Conference of Commissioners on Uniform State Laws adopted the Uniform Division of Income for Tax Purposes Act. Between 1956 and 1963 only 3 states adopted this Act.

In 1961, the Subcommittee on State Taxation of Interstate Commerce, House Judiciary Committee, began a four year study of Corporate Sales Taxes

and Income Taxes. Their report described the Corporation Tax system in effect in 1965 as follows:

> Although it cannot be said that interstate business is today incurring burdensome compliance costs, the reasons for the absence of these costs raise serious issues in themselves. What has happened is that the ...multistate tax system...has resulted in non-compliance and in the inequities which come with a tax system in which formal requirements have been abandoned.(1)

As a result of this study the Interstate Taxation Bill of 1966 (HR 11798) was introduced (but not enacted). Since 1966, several versions of the Interstate Tax Bill (incorporating the property, payroll and receipts allocation formula as an optional maximum) have been introduced. None has passed.

Of the 45 states (and the District of Columbia) which tax corporate net income, 35 states (and the District of Columbia) use the property-payroll-receipts factor. These are Alabama*, Alaska*, Arizona, Arkansas*, California*, Connecticut, Delaware, the District of Columbia*, Georgia, Hawaii*, Idaho*, Illinois*, Indiana*, Kansas*, Kentucky*, Louisiana, Maine*, Maryland, Michigan*, Montana*, Nebraska, New Hampshire, New Jersey, New Mexico*, North Carolina*, North Dakota*, Ohio*, Oklahoma*, Oregon*, Pennsylvania*, Rhode Island, South Carolina*, Tennessee*, Utah*, Vermont and Virginia*. Five states, Florida, Massachusetts, Minnesota, New York and Wisconsin, have weighted property-payroll receipts factors. Five states, Colorado, Iowa, Mississippi, Missouri and West Virginia do not use one of property, receipts or payroll in their allocation factor.

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(1) Report of the Special Subcommittee on State Taxation of Interstate Commerce House Judiciary Committee, 1965. p.384.

*Have adopted the UDITPA - Uniform Division of Income for Tax Purposes Act.

IV. THE PROPOSED OPTIONAL CORPORATION NET INCOME TAX ALLOCATION FACTOR

A. The Corporation Business Tax Allocation Factor

The New Jersey Corporation Business Tax Act imposes a tax of 2 mills per dollar of Allocated Net Worth and 7.5 cents per dollar of Allocated Net Income on most corporations doing business or having assets in New Jersey. The Allocation Factor, or Allocation Percentage, is the percentage of Net Worth (or Net Income) apportioned to New Jersey by corporations doing an interstate business. In the case of an Investment Company the Allocation Factor is 25%. In the case of a Regulated Investment Company or Real Estate Investment Trust the Net Worth Allocation Factor is 15% and the Net Income Allocation Factor is 4%. In the case of a regular corporation maintaining no regular place of business outside New Jersey or waiving allocation, the allocation percentage is 100%. For all other corporations liable for this tax the Allocation Factor is defined as follows:

$$\text{NJ Allocation Factor} = \frac{\%\ \text{Property} + \%\ \text{Receipts} + \%\ \text{Payroll}}{3}$$

where:

$$\%\ \text{Property} = \frac{(\$)\ \text{Tangible Property in New Jersey}}{(\$)\ \text{Tangible Property Everywhere}}$$

$$\%\ \text{Receipts} = \frac{(\$)\ \text{Receipts with New Jersey situs}}{(\$)\ \text{Receipts Everywhere}}$$

$$\%\ \text{Payroll} = \frac{(\$)\ \text{Wages, salaries and other personal compensation--New Jersey}}{(\$)\ \text{Wages, salaries and other personal compensation--Everywhere}}$$

If the denominator of one of these fractions is zero, the other two are added and the sum divided by 2 and if the denominators of two of the fractions are zero, the remaining percentage may be used as the allocation factor.

An additional apportionment is built into the Corporation Franchise (Net Worth) Tax. This tax is paid on the greater of Allocated Net Worth (as defined above) and one-fourth of New Jersey tangible assets.

If it appears that the allocation factor as computed above does not reflect the New Jersey activity of the corporation, the Director of Taxation may adjust, or the taxpayer may request an adjustment, of the allocation factor. (NJSA 54:10A-8)

B. The Proposed Corporation Net Income Tax Allocation Factor (Optional)

The Net Income Tax Allocation Factor with receipts double weighted is defined as follows:

$$\text{DW Allocation Factor} = \frac{\%\ \text{Receipts} + \%\ \text{Receipts} + \%\ \text{Property} + \%\ \text{Payroll}}{4}$$

or, alternatively, the average (among the receipts, property and payroll percentages) of those fractions with non-zero denominators (where the receipts percentage is counted as two fractions).

This change will not affect those corporations with no regular place of business outside New Jersey, nor will it affect Investment Companies, Regulated Investment Companies or Real Estate Investment Trusts. It will affect only allocating corporations.

The option to use either the old or the new allocation factor means that, presumably only those corporations which stand to gain from using the Double Weighted Allocation Factor will use it. This change, therefore, according to 1976 figures, would affect 3,937 out of 150,400 corporations (or 2.62% of all corporations.)

V. CONCLUSIONS ABOUT THE DOUBLE WEIGHTED FORMULA AS AN INDUCEMENT TO INCREASE INDUSTRIAL INVESTMENT IN NEW JERSEY

A. It is not the case that large location decisions will be favorably influenced by a change in the Business Allocation Factor. The Fantus Corporation, in a Consultants' Report to the New Jersey Manufacturers Insurance Company, says

> In the news lately has been a trend to double weight the sales factor in the corporate income tax apportionment formula. Massachusetts and New York recently followed Florida and Wisconsin in the adoption of this practice. The possibility of New Jersey following suit has been suggested in some quarters.
>
> It is Fantus' understanding that such a move by New Jersey would be undertaken primarily as a defensive measure, since some of the competitive states have adopted such a posture. Proponents also argue that double weighting will encourage job-creating investment in the state and discourage the out-migration of plants and employees (i.e., in effect it would be very favorable to companies with a relatively large capital and payroll presence in the state, as compared to their in-state sales).
>
> Viewed strictly as a facet of New Jersey's business climate, double weighting of sales will also have negative effects. For instance, there will be those companies with "capital-payroll-sales" configurations requiring highest corporate income tax payments under the proposed apportionment formula.
>
> If, after sufficient study of the subject has been made, and double weighting of sales is deemed necessary, Fantus would recommend making it optional for the individual taxpayer. In this way, the choice of single or double weighting sales can be promoted to potential investors as a true incentive, without suffering the backlash of negative investment decisions (i.e., against locating or expanding in New Jersey), which would accompany a switch to the double weight system alone.[2]

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[2] Fantus Company, A Research Program To Strengthen New Jersey's Competitive Position For Business And Industry, pp. 41-42.

> Typically, corporate income taxes are not the critical screening factor in location decisions. This is especially true of multiplant companies (with facilities in a number of states) where allocation of income often involves complex computations based on total corporate accounts. At any rate, New Jersey's corporate income taxes by themselves have not been viewed as particularly onerous by the business community. (3)

B. It is the case that some location decisions will be adversely influenced by a change in allocation formula. That is to say, there will be some corporations that will choose out of state locations in order to gain from allocation. As Ralph Vecchio, Deputy Director of the New York State Corporation Tax Bureau says of this state's experience with the mandatory DW Factor,

> A side effect which I expect to see is the establishment (of out-of-state offices by non-allocators). Like many states, New York does not allow allocation unless the taxpayer establishes a bona fide regular place of business outside New York. If I were advising a company, I would certainly examine the...savings possible from allocation.(4)

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(3) Ibid, p.38.

(4) Vecchio, Ralph, "Use Of a Weighted Sales Factor in Apportioning Corporate Income," Revenue Administration, 1976, p.79.

C. The Relatively Lighter Weight Given to Property and Payroll in the Proposed Allocation Factor Are Insufficient to Counterbalance the Relaively High Costs of Labor and Property in New Jersey.

On realty taxes, New Jersey manufacturers have long suspected that they have not received fair treatment at the hands of the tax assessor. A statistical study of true tax rates recently completed by the Center for Local Tax Research tends to agree. According to the study the average true property tax rates in New Jersey are: residential 2.84%; vacant land 2.79%; industry 3.51%. Early rectification of this situation should do much to improve the state's tax image in the eyes of industry.[5]

* * * *

In New Jersey the costs of unemployment insurance have tended to be higher than other states by reason of more liberal benefits..(These replace) such a high proportion of take home pay (as to provide) scant incentive to seek or accept employment until all benefits have been exhausted.[6]

* * * *

The image of worker's compensation has paralled that of unemployment insurance.[7]

* * * *

Labor management relations and labor laws have not been accorded sufficient importance in studies of New Jersey's industrial development. Fantus' experience with out-of-state firms indicates that this facet of business climate has had a tremendous effect on numerous investment decisions. In many cases New Jersey has been knocked from contention very early in the location decision making process, because...high wages and fringes can be expected due to the degree of organization in the state.[8]

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(5) Fantus, op.cit. p.32. The 1977 average true value tax rates for these property classes were: Vacant:$2.42, Residential: $2.65, Business: $3.50.

(6) Ibid. p.35.

(7) Ibid. p.36.

(8) Ibid. pp.25-26.

> A very interesting thought process has been identified for some New Jersey firms with a need to expand. Many executives realize that union organization of their new facilities may be inevitable; however, if they move to certain southern states...union representation can be delayed for a couple of years. This can make or break an expansion, since many extraordinary costs are encountered only during the first few years of operation. In the same vein, some companies have contractually agreed with their unions that any new plants in New Jersey will be automatically organized, and existing wage and fringe benefits will apply. This again makes for unattractive investment in New Jersey.(9)

D. There is no evidence to indicate that this allocation factor will expand the corporate tax base. There is a body of opinion holding that nothing short of an overhaul will do this.

According to the Fantus Corporation,

> Uncertainty concerning the tax outlook in the state has also hindered development in the past. Therein lies the importance of the recently passed income tax, which can form the basis for solid tax reform. The repeal of such "budget balancing add-ons" as the retail gross receipts tax, the capital gains and unearned income tax, and the unincorporated business tax, can also contribute to a more stable situation (i.e., psychological, since these taxes don't affect most manufacturers).
>
> In summary, New Jersey's tax climate is now in a state of flux. A number of recent changes seem to be heading the state in the right direction, but more remains to be done. The key must be a concurrent effort to improve the various aspects of business climate. For example, witness New York and Massachusetts which can boast many of the tax incentives discussed above, yet by focusing primarily on taxes, significant positive change in how industry perceives their business climate has yet to take place.(10)

E. Industry, which has been asking for uniformity of allocation among states in order to reduce the cost of corporation tax return preparation, may view a change from the relatively standard allocation formula

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(9) Ibid. p.26.

(10) Ibid. p. 42-43.

that New Jersey now uses as an annoyance. Moreover, the mandatory double weighted factor is open to constitutional challenge on the grounds of unfairness.

The following is excerpted from the Statement of Leonard E. Kust, Member, U.S. Chamber of Commerce, before the Senate Finance Committee, Subcommittee on State Taxation of Interstate Commerce:

> The National Chamber favors the enactment by Congress of legislation which will:
>
> 1. Establish a uniform jurisdictional standard for the imposition of taxes by the States on interstate business.
>
> 2. Promote uniformity in the division among the states of interstate business income and in the tax base for income tax purposes, and
>
> 3. Promote uniformity in definitions of common terms and common standards used by the states in the imposition of the obligation on interstate sellers to collect sales and use taxes.
>
> It is clear that Congressional action is needed to solve a problem that cannot be solved in the foreseeable future by a compact of the states. In spite of efforts...to form such a compact, only two-fifths of the states are members and the compact itself is of questionable legality.
>
> The apportionment formula for the division of income should include the three factors of sales, property and payroll. This formula, used by most of the states, is contained in the Uniform Division of Income for Tax Purposes Act. As may be seen from the 1966 House hearings, most of the business representatives preferred the three-factor formula.
>
> The sales factor should be on a destination basis. The numerator should consist, without exception of sales of products delivered in or shipped into the taxing jurisdiction. The denominator should consist of total sales.[11]

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(11) Subcommittee on State Taxation of Interstate Commerce, Senate Committee on Finance; Hearings on Proposals Regarding State Taxation of Interstate Commerce, 1973, p.90.

The American Textile Manufacturers Institute, in the same hearings, said:

> ATMI favors the optional three factor formula to define the maximum income or capital that can be attributed to a particular taxing jurisdiction. There is a pressing need for a uniform formula for the division of income and capital among the states, both to provide more equitable treatment of businesses operating in interstate commerce and to lighten their compliance burdens.(12)

Ralph Vecchio says:

> I, as tax administrator, must assume that double weighting is constitutional. The issue has not been clearly settled, however, and an honest evaluation of precedent does not lead inevitably to a conclusion that double weighting will withstand a constitutional challenge. Consequently, such a challenge is to be expected.(13)

VI. IMPLICATIONS OF THE DOUBLE WEIGHT FACTOR ON STATE REVENUE

A. Administrative

The New York State Department of Taxation and Finance has been unable to provide New Jersey with a meaningful estimate of increased administrative costs resulting from adoption of this allocation factor, because they have insufficient data at present. They do know that there will be increased enforcement cost. As Ralph Vecchio writes in the article mentioned previously:

> I foresee taxpayers coupling very limited activity with taxability in another state to claim a regular place of business there...We will have to look to the bona fides of a regular place of business...
>
> These cases will no doubt present very difficult fact questions, but they are not insurmountable. One case already decided in New York concerned a taxpayer who rented space in a public warehouse in another state and put a few thousand dollars worth

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(12) Ibid. p.446.

(13) Vecchio, Op. cit. p.89.

of merchandise there...The goods never moved - the same few thousand dollars stayed and never changed. Obviously, this was not a bona fide regular place of business.

I believe it will be incumbent on us... to examine whether there is a real business purpose in establishing a location outside New York.[14]

B. State Tax Revenues

A corporation's New Jersey Net Income as well as its percentages of property, receipts and payroll can change from year to year. Therefore it is difficult to estimate future tax revenue implications of such a change with certainty. We have been able to compute the tax revenue effects of this change for Return Year 1975 (the latest available data). This means that estimates of the change in current tax collections must be assumed to be like those calculated for the tax year 1975 subject to adjustment upward for income growth and other factors. It is estimated that this proposal will reduce Corporation Net Income Tax liability of 3,937 corporations by $16.1 million. Approximately 81% of this money would go to 200 multi-state corporations.

Realistically any change in allocation factor should apply to net worth as well as net income. Calculations for 1975 tax year returns indicate that optional application of the double weighted formula to net worth would reduce the tax for these same 3,937 corporations by an additional $3.2 million. This would mean a total reduction of $19.3 million in Corporation Tax revenues before any adjustment to reflect prepayment losses during the first year of

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(14) Ibid. p.89.

losses during the first year of application.

Computations have been made under two mutually exclusive assumptions. First, it is assumed that the tax paying corporation may elect to continue the present allocation or move to the new one. Second, that all corporations would be required to use the new formula based upon double weighting of receipts. As previously stated it is assumed that no corporation would have its taxes increased under the first assumption whereas those that do not benefit from double weighting of receipts would have their taxes increased under the second.

All computations are summarized in the following table and descriptive text.

Effect of Proposed Change In Business Allocation Formula on Corporation Taxes
($ Amounts in millions)

	Optional			Mandatory		
	Gaining	No Chng.	Total	Gaining	Losing	Total
Number	3,937	6,209	10,146	3,937	6,209	10,146
Net Worth Tax						
Present	$ 21.2	$ 8.8	$ 30.0	$ 21.2	$ 8.8	$ 30.0
Proposed	18.0	8.8	26.8	18.0	10.0	28.0
Difference	$ 3.2	$ -0-	$ 3.2	$ 3.2	- $ 1.2	$ 2.0
Net Income Tax						
Present	$ 99.6	$ 37.9	$137.5	$ 99.6	$37.9	$137.5
Proposed	83.5	37.9	121.4	83.5	43.3	126.8
Difference	$ 16.1	$ -0-	$ 16.1	$ 16.1	- $ 5.4	$ 10.7
Total						
Present	$120.8	$ 46.7	$167.5	$120.8	$46.7	$167.5
Proposed	101.5	46.7	148.2	101.5	53.3	154.8
Difference	$ 19.3	$ -0-	$ 19.3	$ 19.3	$ 6.6	$ 12.7
% Change	- 15.9%	-0-	- 11.5%	- 15.9%	+ 13.9%	- 7.6%

10,147 (6.75%) of 150,400 corporations filing New Jersey Corporation Business Tax Returns in 1976 were "allocating corporations" (less than 100% in New Jersey).

3,937 corporations (38.80% of all allocating corporations) would reduce their tax $19.2 million with double weighting of the receipts factor in the allocation formula.

This 15.9% reduction for 3,937 corporations would be distributed between net worth and net income taxes as follows:

Net worth reduced $3.2 million from $21.2 million to $18.0 million.

Net income reduced $16.1 million from $99.6 million to $83.5 million.

6,209 corporations (61.20% of all allocating corporations) would increase their tax $6.5 million with double weighting of the receipts factor in the allocation formula.

This 13.9% increase for 6,209 corporations would be distributed between net worth and net income taxes as follows:

Net worth increased $1.2 million from $8.8 million to $10.0 million.

Net income increased $5.4 million from $37.9 million to $43.3 million.

If the double weighting formula was applied to all "allocating corporations" the net reduction would thus be $12.7 million (7.6%) of tax liability of allocators.

If the double weighting sales formula were optional at the choice of the taxpayer corporation, the reduction would total $19.2 million (11.5%).

Only the 3,937 benefiting corporations would elect to use the alternative formula. These benefits would average $4,886 per benefiting corporation.

All computations assume no change in operations as they existed when 1976 corporation tax returns were filed. There is no estimate of possible changes in operations of the 6,209 corporations for which no benefits are anticipated.

No assumptions are made concerning possible changes in operating procedures for corporations not allocating in 1976. New York State tax administrators report that double weighting of the sales factor in that state has led some non-allocating corporations to open sales offices outside the state to gain some advantage in allocation.

VII. SOME EXAMPLES OF BENEFICIARIES AND NON-BENEFICIARIES

Example 1 is a large exporter with a number of facets especially suited to New Jersey location. It has the following percentages: 6.8364% Property, 3.3634% Receipts and 10.7615% Payroll. It presently allocates 6.9871% of Net Income (after adjustment) to New Jersey. It would allocate 6.0812% of Net Income under this proposal. Its 1976 Net Income Tax liability was $7.3 million. It would have been $6.3 million. This corporation would have had its Net Income Tax liability reduced by $1 million because of its New Jersey allocation and its first year tax payment reduced by $1.6 million. To increase its property percentage by one per cent, this corporation would have to locate an additional $400 million in land, buildings and/or equipment in New Jersey.

Example 2 is a large importer because a disproportionate share of its market is in New Jersey. It has the following New Jersey percentages: Property: 2.3427%, Receipts: 3.925%, Payroll: 3.2850%.

To increase its property percentage sufficiently to receive a small tax advantage would require minimal investment of $400 million. This proposal of itself provides insufficient incentive for that kind of investment.

Example 3 is large importer which will soon become an exporter. It has the following New Jersey percentages: Property: .6366%, Receipts: 2.6026% Payroll: .6294%. It would require a capital investment of $200 million to bring this corporation to the point at which it benefits from the proposal under consideration. This corporation will make that investment only in order to increase its profits, as indicated by decisions already made.

Example 4 is a large department store chain in the United States. It has been chosen as an example because it is typical of allocating retail stores. Its New Jersey percentages are: Property: 3.2179%, Receipts: 3.0775%, Payroll: 2.9095%. Double weighting receipts in its allocation formula would not change very much the Corporation Business Tax this corporation pays. Retail stores have in common the fact that increase in any one of the New Jersey percentages usually requires increase in all three.

Example 5 is a large exporter located almost entirely in New Jersey. Its New Jersey percentages are: Property: 90.7012%, Receipts: 6.475%, Payroll: 85.3587%. Its 1975 allocation factor was 60.845%. Had this proposal been law its allocation factor would have been 47.2525%. This would have reduced its Net Income Tax liability by $1.5 million. Include reduction in prepayment liability and the total first year reduction in Corporation Business Tax becomes $2.5 million. This corporation located in New Jersey because of the advantages New Jersey offers to research oriented firms.

Computation of the Present Allocation Factor:

A) New Jersey Corporation Tax Return - Schedules J and K
B) Instructions for filling in Schedules J and K

SCHEDULE J (See Instruction 26)

(a) This schedule showing average values of real and tangible personal property must be completed by every taxpayer entitled to and electing to allocate.
(b) The average values of real and tangible personal property are to be computed on the basis of the average book values thereof and not on original cost.
(c) The basis upon which the amounts in Cols. A and B below have been averaged is ..... (See Instruction 26).

Item No.	ASSETS	AVERAGE VALUES (See Instruction 26) (Omit Cents) Column A Everywhere	Column B New Jersey	BUREAU USE ONLY
13.	Land			
14.	Buildings and other Improvements			
15.	Machinery and Equipment			
16.	Inventories			
17.	All other Tangible Personalty (Itemize on Rider)			
18.	*Total Real and Tangible Personal Property* (Total Items 13 to 17) (Carry Item 18, Column B to Item 8, Sec. II, Page 1)	$	$	

SCHEDULE K **COMPUTATION OF ALLOCATION FACTOR (See Instruction 27)**

IMPORTANT – THIS SCHEDULE MAY BE OMITTED: (a) if this taxpayer does not maintain a regular place of business outside this state other than a statutory office, in which case the tax law requires the allocation factor to be 100%; or (b) if this taxpayer, for practical convenience, wishes to waive the allocation provisions of the act and allocate 100% of the adjusted net worth and adjusted net income to the State of New Jersey.

	COLUMN A (OMIT CENTS)	COLUMN B
1. Average value of the taxpayer's real and tangible personal property *OWNED:*		
(a) In New Jersey (Schedule J, Column B, Item 18)	$	
(b) Everywhere (Schedule J, Column A, Item 18)	$	
(c) Percentage in New Jersey [Item 1(a) divided by Item 1(b)]. Enter in Col. B		%
2. Receipts:		
(a) From sales, in the regular course of business, of tangible personal property *LOCATED* in New Jersey at time of receipt of or appropriation to the orders, where shipments are made to points within New Jersey, *IRRESPECTIVE OF WHERE THE ORDERS WERE RECEIVED OR ACCEPTED.* [See Instruction 27(b)]	$	
(b) From sales, in the regular course of business, of tangible personal property *LOCATED* outside New Jersey at time of the receipt of or appropriation to the orders, where shipment is made to points within New Jersey, *IRRESPECTIVE OF WHERE THE ORDERS WERE RECEIVED OR ACCEPTED.* [See Instruction 27(b)]	$	
(c) From services performed in New Jersey	$	
(d) From rentals of property situated in New Jersey	$	
(e) From royalties for the use in New Jersey of patents and copyrights	$	
(f) All other business receipts earned in New Jersey. – [See Instruction 27(c)]	$	
(g) Total New Jersey receipts [Total of Items 2(a) to 2(f), inclusive, in Col. A]	$	
(h) Total receipts from all sales, services, rentals, royalties and other business transactions within and without New Jersey. – [See Inst. 27(c)]	$	
(i) Percentage in New Jersey [Item 2(g) divided by Item 2(h)]. Enter in Col. B		%
3. Wages, salaries and other personal service compensation [See Instruction 27(d)]		
(a) In New Jersey	$	
(b) Everywhere	$	
(c) Percentage in New Jersey [Item 3(a) divided by Item 3(b)]. Enter in Col. B		%
4. Sum of New Jersey percentages shown at Items 1(c), 2(i) and 3(c). Enter in Col. B		%
5. *Allocation Factor* [Item 4 divided by three, or by the number of percentages included in Item 4 – See Instruction 27(e)]. Enter in Col. B and carry to Page 1, Item 4 and Page 2, Item 38.		%

26. **SCHEDULE J – AVERAGE VALUES:** Average value is generally computed on a quarterly basis where the taxpayer's usual accounting practice permit such computation. At the option of the taxpayer or the State, a more frequent basis (monthly, weekly or daily) may be used. Where the taxpayer's usual accounting practice does not permit computation of average value on a quarterly or more frequent basis, a semi-annual or annual basis may be used where no distortion of average value results. If any basis other than quarterly is used, state the basis and reasons for use thereof on rider.

27. **SCHEDULE K – ALLOCATION FACTOR:**

(a) **ITEM 1 – PROPERTY FRACTION:** For general information regarding method of valuation in arriving at average values, see Instruction 26. Tangible personal property is within New Jersey if and so long as it is physically situated or located here. Only property **OWNED BY THE TAXPAYER** is to be included in either the numerator or denominator. Property of the taxpayer held in New Jersey by an agent, consignee or factor is (and property held outside New Jersey by an agent, consignee or factor is not) situated or located within New Jersey.

(b) **ITEMS 2(a) and 2(b) – ALLOCATION OF RECEIPTS:** 100% Allocation to New Jersey of receipts from sales of tangible personal property is required where New Jersey, or another State or place is the place of origin and New Jersey is the destination.

(c) **ITEMS 2(f) and 2(h)**

(1) **RECEIPTS FROM SALES OF CAPITAL ASSETS:** Receipts from sales of capital assets (property not held by the taxpayer for sale to customers in the regular course of business), either within or without New Jersey, should not be included. **Note:** Where the taxpayer's business is the buying and selling of real estate or the buying, holding or selling of securities for investment purposes, receipts from the sale of such assets should be included.

(2) **DIVIDEND INCOME:** The amount of dividends excluded from adjusted entire net income at Item 33, Schedule A, should not be included.

(d) **ITEM 3 – PAYROLL FRACTION:** See N.J.S.A. 54:10A-7 for a detailed definition of wages, salaries and other personal services compensation allocable to New Jersey. All executive salaries are includible in both the numerator and denominator as applicable. In general, a taxpayer reporting to the Division of Employment Security in the New Jersey Department of Labor and Industry will allocate to New Jersey all wages, salaries and other personal service compensation, etc., reportable to that Commission, including the portions thereof, in individual cases, over $4,200.

(e) **ALLOCATION FRACTIONS – GENERAL:** If the corporation owned no real estate or tangible personal property during the taxable year **WITHIN OR WITHOUT** New Jersey, leave Item 1 (c) blank, and divide Item 4 by two to obtain Item 5. If the corporation owned no real estate or tangible personal property during the taxable year **WITHIN** New Jersey, but did own such property **OUTSIDE** the State enter zero at Item 1 (c). If the corporation had no New Jersey receipts, enter zero at Item 2 (i). If the corporation had no employees in New Jersey, enter zero at Item 3 (c).

APPENDIX II

The Uniform Division of Income For Tax Purposes Act

Section 1. As used in this Act, unless the context otherwise requires:

(a) "Business income" means income arising from transactions and activity in the regular course of the taxpayer's trade or business and includes income from tangible and intangible property if the acquisition, management and disposition of the property constitute integral parts of the taxpayer's regular trade or business operations.

(b) "Commercial domicile" means the principal place from which the trade or business of the taxpayer is directed or managed.

(c) "Compensation" means wages, salaries, commissions and any other form of remuneration paid to employees for personal services.

Section 2. Any taxpayer having income from business activity which is taxable both within and without this state, other than activity as a financial organization or public utility or the rendering of purely personal services by an individual, shall allocate and apportion his net income as provided in this Act.

Section 3. For purposes of allocation and apportionment of income under this Act, a taxpayer is taxable in another state if (1) in that state he is subject to a net income tax, a franchise tax measured by net income, a franchise tax for the privilege of doing business, or a corporate stock tax, or (2) that state has jurisdiction to subject the taxpayer to a net income tax regardless of whether, in fact, the state does or does not.

Section 4. Rents and royalties from real or tangible personal property, capital gains, interest, dividends, or patent or copyright royalties, to the extent that they constitute nonbusiness income, shall be allocated as provided in sections 5 through 8 of this Act.

Section 5. (a) Net rents and royalties from real property located in this state are allocable to this state.

(b) Net rents and royalties from tangible personal property are allocable to this state:

(1) if and to the extent that the property is utilized in this state, or

(2) in their entirety if the taxpayer's commercial domicile is in this state and the taxpayer is not organized under the laws of or taxable in the state in which the property is utilized.

(c) The extent of utilization of tangible personal property in a state is determined by multiplying the rents and royalties by a fraction, the numerator of which is the number of days of physical location of the property in the the state during the rental or royalty period in the taxable year and the denominator of which is the number of days of physical location of the property everywhere during all rental or royalty periods in the taxable year. If the physical location of the property during the rental or royalty period is unknown or unascertainable by the taxpayer tangible personal property is utilized in the state in which the property was located at the time the rental or royalty payer obtained possession.

Section 6. (a) Capital gains and losses from sales of real property located in this state are allocable to this state.

(b) Capital gains and losses from sales of tangible personal property are allocable to this state if:

(1) The property had a situs in this state at the time of the sale, or

(2) The taxpayer's commercial domicile is in this state and the taxpayer is not taxable in the state in which the property had a situs.

(c) Capital gains and losses from sales of intangible personal property are allocable to this state if the taxpayer's commercial domicile is in this state.

Section 7. Interest and dividends are allocable to this state if the taxpayer's commercial domicile is in this state.

Section 8. (a) Patent and copyright royalties are allocable to this state:

(1) if and to the extent that the patent or copyright is utilized by the payer in this state, or

(2) if and to the extent that the patent or copyright is utilized by the payer in a state in which the taxpayer is not taxable and the taxpayer's commercial domicile is in this state.

(b) A patent is utilized in a state to the extent that it is employed in production, fabrication, manufacturing or other processing in the state or to the extent that a patented product is produced in the state. If the basis of receipts from patent royalties does not permit allocation to states or if the accounting procedures do not reflect states of utilization, the patent is utilized in the state in which the taxpayer's commercial domicile is located.

(c) A copyright is utilized in a state to the extent that printing or other publication originates in the state. If the basis of receipts from copyright royalties does not permit allocation to states or if the accounting procedures do not reflect states of utilization, the copyright is utilized in the state in which the taxpayer's commercial domicile is located.

Section 9. All business income shall be apportioned to this state by multiplying the income by a fraction, the numerator of which is the property factor plus the payroll factor plus the sales factor, and the demominator of which is three.

Section 10. The property factor is a fraction, the numerator of which is the average value of the taxpayer's real and tangible personal property owned or rented and used in this state during the tax period and the denominator of which is the average value of all the taxpayer's real and tangible personal property owned or rented and used during the tax period.

Section 11. Property owned by the taxpayer is valued at its original cost. Property rented by the taxpayer is valued at eight times the net annual rental rate. Net annual rental rate is the annual rental rate paid by the taxpyer less any annual rental rate received by the taxpayer from sub-rentals.

Section 12. The average value of property shall be determined by averaging the values at the beginning and ending of the tax period but the tax administrator may require the averaging of monthly values during the tax period if reasonably required to reflect properly the average value of the taxpayer's property.

Section 13. The payroll factor is a fraction, the numerator of which is the total amount paid in this state during the tax period by the taxpayer for compensation, and the denominator of which is the total compensation paid everywhere during the tax period.

Section 14. Compensation is paid in this state if:

(a) the individual's service is performed entirely within the state; or

(b) the individual's service is performed both within and without the state, but the service performed without the state is incidental to the individual's service within the state; or

(c) some of the service is performed in the state and (1) the base of operations or, if there is no base of operations, the place from which the service is directed or controlled is in the state, or (2) the base of operations or the place from which the service is directed or controlled is not in any state in which some part of the service is performed, but the individual's residence is in this state.

Section 15. The sales factor is a fraction, the numerator of which is the total sales of the taxpayer in this state during the tax period, and the denominator of which is the total sales of the taxpayer everywhere during the tax period.

Section 16. Sales of tangible personal property are in this state if:

(a) the property is delivered or shipped to a purchaser, other than the United States government, within this state regardless of the f. o. b. point or other conditions of the sale; or

(b) the property is shipped from an office, store, warehouse, factory, or other place of storage in this state and (1) the purchaser is the United States government or (2) the taxpayer is not taxable in the state of the purchaser.

Section 17. Sales, other than sales of tangible personal property, are in this state if:

(a) the income-producing activity is performed in this state; or

(b) the income-producing activity is performed both in and outside this state and a greater proportion of the income-producing activity is performed in this state than in any other state, based on costs of performance.

Section 18. If the allocation and apportionment provisions of this Act do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for, or the tax administrator may require, in respect to all or any part of the taxpayer's business activity, if reasonable:

(a) separate accounting;

(b) the exclusion of any one or more of the factors;

(c) the inclusion of one or more additional factors which will fairly represent the taxpayer's business activity in this state; or

(d) the employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's income.

Section 19. This Act shall be so construed as to effectuate its general purpose to make uniform the law of those states which enact it.

Section 20. This Act may be cited as the Uniform Division of Income for Tax Purposes Act.

The Act has been substantially adopted in the following jurisdictions:

SENATE CONCURRENT RESOLUTION No. 3024

STATE OF NEW JERSEY

INTRODUCED SEPTEMBER 29, 1977

By Senators FELDMAN, GARRAMONE and SCARDINO

(Without Reference)

A CONCURRENT RESOLUTION requesting the Division of Taxation to study the feasibility of the optional double weighting of the sales tax factor in the Corporate Income Tax apportionment formula.

WHEREAS, A fair and realistic Corporation Income Tax is a central concern for New Jersey industry; and

WHEREAS, An expanding industrial sector is of vital importance to the creation of new employment opportunities and the economic health of the State of New Jersey as a whole; and

WHEREAS, The willingness of industry presently in New Jersey to expand their operations in the State, and of new industries to locate within the State, is to a large extent dependent on industry viewing the New Jersey Corporation Tax system in a favorable light; and

WHEREAS, Providing for the optional double weighting of the sales tax factor in the Corporation Income Tax apportionment formula would add a measure of flexibility to the New Jersey Corporation Tax structure and thus might provide an incentive for industrial expansion in the State; now, therefore,

BE IT RESOLVED *by the Senate of the State of New Jersey (the General Assembly concurring):*

That the Legislature does hereby request the Division of Taxation to investigate the feasibility of the optional double weighting of the sales tax factor in the Corporate Income Tax apportionment formula, and to report to the Legislature its findings and recommendations as to the implications such an allowance would have on State tax revenues, and the inducements it might create for increased industrial investment in the State of New Jersey.

STATEMENT

The purpose of this resolution is to request the Division of Taxation to study the feasibility of the optional double weighting of the sales tax factor in the Corporate Income Tax apportionment formula, and to report to the Legislature its findings and recommendations. The willingness of industry presently in New Jersey to expand their operations in the State, and of new industries to locate within the State, is to a great extent dependent on industry viewing the New Jersey Corporation Income Tax in a favorable light. The optional double weighting of the sales tax factor in the Corporate Income Tax apportionment formula would introduce a measure of flexibility into the New Jersey Corporation Tax structure. The optional double weighting of the sales tax factor would provide some tax relief to firms which have a large net worth presence in the State but small in-State sales, or to firms with a large net worth but which in any particular year might have a poor sales record. By allowing firms the option of emphasizing their sales (as opposed to their net worth) in the computation of their taxes, this resolution would provide an incentive to industrial expansion in New Jersey.

Letter from the Commonwealth of Massachusetts - Executive Office for Administration & Finance, dated May 26, 1978.

ROBERT H. McCLAIN, Jr.
Undersecretary of
Administration

The Commonwealth of Massachusetts

Executive Office for

Administration and Finance

State House, Boston 02133

May 26, 1978

Mr. James Arnold
Chief of Tax Research
State of New Jersey
Tax Building - 9th Floor
State and Willow Sts.
Trenton, N. J. 08625

Dear Mr. Arnold:

In response to your recent telephone request, the following information is submitted.

At the time the change in our allocation formula was proposed by the Associated Industries of Massachusetts, it was done primarily to try to attract the home offices of many national firms then moving out of New York City to Massachusetts. There is no indication that any considerable number of such offices did, in fact, move to Massachusetts. No actual analysis has been made of the corporation tax returns which would give us the specific revenue loss due to this change in our allocation formula. However, at the request of what was then known as the Capital Formation Task Force, the state tax department did estimate that approximately 1,400 corporations out of approximately 70,000 were benefited by the change in the law and that such change probably resulted in a revenue loss of at least four and a half million dollars. It is not contemplated that the tax department would analyze the returns for a more accurate figure in the near future.

However, if you would like us to try to get more specific information, we will attempt to do so.

Very truly yours,

Robert H. McClain, Jr.

Robert H. McClain, Jr.
Undersecretary

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