

CHAPTER 35

NEW JERSEY GROSS INCOME TAX

Authority

N.J.S.A. 54:50-1, 54A:9-8.2 and 54A:9-17(a).

Source and Effective Date

R.2008 d.282, effective August 21, 2008.
See: 40 N.J.R. 2222(a), 40 N.J.R. 5245(b).

Chapter Expiration Date

In accordance with N.J.S.A. 52:14B-5.1b, Chapter 35, New Jersey Gross Income Tax, expires on August 21, 2015. See: 43 N.J.R. 1203(a).

Chapter Historical Note

Chapter 35, New Jersey Gross Income Tax, was adopted prior to September 1, 1969.

Subchapter 2, Setoff of Individual Liability, was adopted as R.1982 d.161, effective May 17, 1982. See: 13 N.J.R. 940(a), 14 N.J.R. 474(b).

Pursuant to Executive Order No. 66(1978), Chapter 35, New Jersey Gross Income Tax, was readopted as R.1983 d.353, effective August 12, 1983. See: 15 N.J.R. 1091(a), 15 N.J.R. 1488(c).

Pursuant to Executive Order No. 66(1978), Chapter 35, New Jersey Gross Income Tax, was readopted as R.1988 d.299, effective June 7, 1988. See: 20 N.J.R. 514(a), 20 N.J.R. 1571(b).

Pursuant to Executive Order No. 66(1978), Chapter 35, New Jersey Gross Income Tax, was readopted as R.1993 d.315, effective June 4, 1993. See: 25 N.J.R. 1500(a), 25 N.J.R. 2906(b).

Former Subchapter 3, Information Return for Business Employment Incentive Program/Business Relocation Assistance Grant Program of the New Jersey Economic Development Authority, was adopted as R.1997 d.533, effective December 15, 1997. See: 29 N.J.R. 4076(b), 29 N.J.R. 5313(a).

Pursuant to Executive Order No. 66(1978), Chapter 35, New Jersey Gross Income Tax, was readopted as R.1998 d.195, effective March 26, 1998. See: 30 N.J.R. 612(a), 30 N.J.R. 1428(a).

Chapter 35, New Jersey Gross Income Tax, was readopted as R.2003 d.285, effective June 20, 2003. See: 35 N.J.R. 1384(a), 35 N.J.R. 3386(a).

Subchapter 11, Filing Fee Payments by Partnerships, was adopted as Special Adopted and Concurrent Proposed New Rules by R.2003 d.135, effective February 17, 2003 (to expire August 26, 2003). See: 35 N.J.R. 1573(a). The concurrent proposal of Subchapter 11, Filing Fee Payments by Partnerships, was adopted as R.2003 d.370, effective August 22, 2003. See: 35 N.J.R. 1573(a), 35 N.J.R. 4310(a).

Subchapter 2, Excludable Income, was renamed Exclusions and Deductions by R.2007 d.55, effective February 5, 2007. See: 38 N.J.R. 4658(a), 39 N.J.R. 546(a).

Chapter 35, New Jersey Gross Income Tax, was readopted as R.2008 d.282, effective August 21, 2008. See: Source and Effective Date. See, also, section annotations.

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SUBCHAPTER 1. GROSS INCOME—CATEGORIES AND CALCULATION

18:35-1.1 Net profits from business

(a) Each taxpayer is subject to gross income tax on the taxpayer's "net profits from business" within the meaning of N.J.S.A. 54A:5-1b, which shall be determined as provided in this subchapter.

(b) For purposes of the Gross Income Tax Act, a sole proprietorship, which shall include self-employed individuals and independent contractors, is a form of business in which one taxpayer owns all the assets of a business and which is not a partnership or corporation. A single member limited liability company whose member is an individual, estate, or trust shall be treated as a sole proprietorship, unless classified otherwise for Federal tax purposes. Sole proprietors shall report their income or loss as net profits from business.

(c) A taxpayer's net profits from business shall be determined by taking into account all income of the taxpayer derived from the conduct of a business, profession or any other activity intended to produce income, provided such activity qualifies for and reports as a trade or business for Federal income tax purposes. All income attributable to the taxpayer's conduct of a trade or business, reduced by costs and expenses as provided in (d) below, shall be taken into account in determining the taxpayer's net profits from business. All other income of the taxpayer subject to gross

income tax that is not attributable to the conduct of a trade or business shall be included in one or more of the other categories of gross income specified in N.J.S.A. 54A:5-1 according to its character and shall not be includable in the category of income "net profits from business." The determination of whether income is derived from the conduct of a trade, business or profession shall be based upon an examination of facts and circumstances of the taxpayer's activities.

1. Income derived as remuneration for services rendered in the sole proprietorship's conduct of a trade or business shall be taken into account in determining a self-employed taxpayer's net profits from business. Income derived by a taxpayer in the taxpayer's capacity as an employee, as defined in N.J.A.C. 18:35-7.1, shall not be taken into account in determining the taxpayer's net profits from business, but rather shall be taxed under N.J.S.A. 54A:5-1a (salaries, wages, etc.).

2. Interest and dividend income derived by a taxpayer in the conduct of a trade or business shall be taken into account in determining a taxpayer's net profits from business. The taxpayer shall annex to the taxpayer's return a statement demonstrating that the interest or dividends were realized in the conduct of the trade or business. Interest and dividends from investment activities or other income-producing activities which do not constitute the conduct of a trade or business shall be separately stated on the taxpayer's return and taxed either as interest described in N.J.S.A. 54A:5-1e or dividends described in N.J.S.A. 54A:5-1f.

3. Rental income derived by a taxpayer in the conduct of a trade or business shall be taken into account in determining a taxpayer's net profits from business. Rental income of a taxpayer which is not received in the conduct of a trade or business shall be taken into account in determining the taxpayer's net gains or net income from rents, royalties, patents and copyrights described in N.J.S.A. 54A:5-1d.

4. Royalty, patent, or copyright income derived by a taxpayer in the conduct of a trade or business that licenses intangible property shall be taken into account in determining the taxpayer's net profits from business. Income derived from royalties, patents or copyrights of a taxpayer which is not derived from a trade or business shall be taken into account in determining the taxpayer's net gains or net income from or in the form of rents, royalties, patents and copyrights described in N.J.S.A. 54A:5-1d.

5. Gains from the sale, exchange or other disposition of trade or business property shall be taken into account in determining a taxpayer's net profits from business. The taxpayer shall annex to the taxpayer's return a statement which demonstrates that gains and losses from the sale, exchange, or other disposition of property were realized in the conduct of a trade or business. The sale, exchange or other disposition of property which is not directly related to or employed in the conduct of a trade or business must be reported as described in N.J.S.A. 54A:5-1c, net gains or

Unless the medical specialist that XY Medical Services, Inc. brings into its location on a case-by-case basis maintains a qualified practice of his own, he does not qualify for an HEZ deduction.

Example 2

Dr. Johnson has a medical practice, organized as a single member LLC with two locations. Location one is within five miles of an HEZ, and location two is neither in an HEZ nor within five miles of an HEZ.

For 2005, Dr. Johnson's practice reports the following:

- Location one's gross receipts are \$200,000. Its qualified receipts are \$125,000.

- Sixty percent of location one's qualified receipts, \$75,000, are from patients living in an HEZ.
- Location one is a qualified practice because at least 50 percent of the gross receipts were qualified receipts and at least 50 percent of the qualified receipts were from patients living in an HEZ.
- Location one's HEZ deduction percentage would be 62.5 percent calculated by dividing the location's qualified receipts, \$125,000 by the location's gross receipts, \$200,000.

- Location two's gross receipts are \$300,000. Its qualified receipts are \$130,000.
- Twenty-five percent of location two's qualified receipts, \$32,500, are from patients living in an HEZ.
- Location two is not a qualified practice because it is neither in an HEZ nor within five miles of an HEZ.
- Net profits from operations for the entire business are \$180,000. Location one's net profits from operations are \$60,000 and location two's net profits from operations are \$120,000.

For tax year 2005, Dr. Johnson, a New Jersey resident, reports \$180,000 as net profits from business on his NJ-1040 return. Dr. Johnson is entitled to an HEZ deduction for location one of \$37,500, calculated as follows:

HEZ deduction		Net profits from		
percentage	×	the qualified	=	deduction
62.5%	×	location	=	\$37,500
		\$60,000		

Dr. Johnson is not entitled to an HEZ deduction for location two because it is not a qualifying practice.

In accordance with N.J.A.C. 18:35-2.7(d), businesses and practices that have more than one location must maintain separate books and records for each location, so that the deduction percentage and net profits from the individual locations can be determined. These separate books and records must be available to the Division of Taxation for audit and verification of the HEZ deduction.

Example 3

ABC Medical, Inc. has two locations, location one is in an HEZ and location two is neither in nor within five miles of an HEZ. Dr. L. is the sole shareholder of ABC Medical, Inc.

For 2005, ABC Medical, Inc. reported the following:

- Location one's gross receipts were \$400,000. Its qualified receipts were \$325,000.
- Thirty percent of location one's qualified receipts, \$97,500, were from patients living in an HEZ.
- Location one qualifies for an HEZ deduction even though 50 percent of its qualified receipts were not from patients living in an HEZ because location one is located in an HEZ.
- Location one's net profits from operations were \$45,000.
- Location one's HEZ deduction percentage is 81.25 percent calculated by dividing the location's qualified receipts, \$325,000, by its gross receipts, \$400,000.

- Location one's HEZ deduction is \$35,563, calculated by multiplying location one's net profits, \$45,000, times its HEZ deduction percentage, 82.25 percent.
- Location two's gross receipts were \$500,000. Its qualified receipts were \$175,000 and 25 percent of location two's qualified receipts, \$43,750, were from patients living in an HEZ.
- Location two is not a qualified practice because it is neither in nor within five miles of an HEZ.
- Location two's net profits from operations were \$180,000.
- ABC Medical, Inc., an S corporation, for 2005, reports an HEZ deduction of \$35,563 for location one. This amount is reflected on the CBT-100S K1 issued to Dr. L. for 2005.
- Net profits from operations for the entire corporation were \$225,500.

For tax year 2005 Dr. L., a nonresident, reports \$225,500 as net pro rata share of S corporation income on his NJ-1040NR return. Dr. L. will also claim an HEZ deduction of \$35,563, as reflected on his NJ-K1 from ABC Medical, Inc.

In accordance with N.J.A.C. 18:35-2.7(d), businesses and practices that have more than one location must maintain separate books and records for each location, so that the deduction percentage and net profits from the individual locations can be determined. These separate books and records must be available to the Division of Taxation for audit and verification of the HEZ deduction.

Example 4

Dr. E is associated with three separate qualified dental practices. He is a member (partner) in HIJ Associates, LLC and KLM Associates, LLC. He is also a shareholder of NOP Orthodontics, Inc., a New Jersey S corporation.

For tax year 2005, Dr. E received the following information on his K-1s from the three dental practices:

HIJ Associates, LLC		
Distributive Share of Partnership Income		\$225,000
HEZ Deduction		\$73,253
KLM Associates, LLC		
Distributive Share of Partnership Income/loss		(\$23,500)
HEZ Deduction		00
NOP Orthodontics, Inc.		
Net Pro Rata Share of S Corporation Income		\$86,000
HEZ Deduction		\$22,747

For tax year 2005, Dr. E, a New Jersey resident, reports the following items of income on his NJ-1040 return:

Distributive Share of Partnership Income	Supporting Detail	Total
HIJ Associates	\$225,000	
KLM Associates	(\$23,500)	\$201,500
Net Pro Rata Share of S Corporation Income		
NOP Orthodontics, Inc.	\$86,000	\$86,000
HEZ Deduction		
HIJ Associates	\$73,253	
KLM Associates	\$0	
NOP Orthodontics, Inc.	\$22,747	\$96,000

Dr. E is not entitled to an HEZ deduction for KLM Associates because he had no net taxable income from the practice. He had a loss.

Example 5

Dr. J has a practice with two locations. Location one is located within an HEZ and location two is located within five miles of an HEZ. For 2005, Dr J's practice reports the following:

- Location one's gross receipts were \$300,000. Its qualified receipts were \$110,000.
- Location one qualifies for an HEZ deduction because it is located within an HEZ.
- Location one's HEZ deduction percentage is 36.667 percent, calculated by dividing its qualified receipts, \$110,000, by its gross receipts, \$300,000.
- Location one's net profits from operations were \$85,000.
- Location one's HEZ deduction is \$31,167, calculated by multiplying location one's net profits, \$85,000, times its HEZ deduction percentage, 36.667 percent.
- Location two's gross receipts were \$400,000, its qualified receipts were \$300,000 and 60 percent of location two's qualified receipts, \$180,000 were from patients living in an HEZ.
- Location two also qualifies for an HEZ deduction because it meets all the criteria to be a qualified practice.
- Location two's HEZ deduction percentage is 75 percent calculated by dividing its qualified receipts, \$300,000, by its gross receipts, \$400,000.
- Location two's net profits from operations were \$110,000.
- Location two's HEZ deduction is \$82,500, calculated by multiplying location two's net profits, \$110,000, times its HEZ deduction percentage, 75 percent.

- Net profits from operations for Dr J's entire practice were \$195,000.

For tax year 2005, Dr. J, a New Jersey resident, will report on his NJ-1040 \$195,000 as net profits from business, \$85,000 from location one and \$110,000 from location two. Dr. J can claim an \$113,667 HEZ deduction, \$31,167 from location one and \$82,500 from location two. Dr. J must attach a schedule to his return showing how he arrived at his HEZ deduction.

In accordance with N.J.A.C. 18:35-2.7(d), businesses or practices that have more than one location must maintain separate books and records for each location, so that the deduction percentage and net profits from the individual locations can be determined. These separate books and records must be available to the Division of Taxation for audit and verification of the HEZ deduction.

New Rule, R.2007 d.55, effective February 5, 2007.
See: 38 N.J.R. 4658(a), 39 N.J.R. 546(a).

SUBCHAPTER 3. ESTIMATED TAX

18:35-3.1 Estimated tax

(a) Every resident and nonresident individual shall make a declaration of the individual's estimated New Jersey personal income tax for each taxable year beginning after June 30, 1976, if the individual's estimated New Jersey personal income tax can reasonably be expected to be more than \$400.00 in excess of any credits allowable against the individual's tax, whether or not the individual is required to file a Federal declaration of estimated tax for such year. Estates and trusts are required to file declarations of estimated tax, other than estates and trusts that meet the two year limitation and other criteria of Internal Revenue Code section 6654(l).

(b) The term "estimated tax" means the amount which an individual estimates to be the individual's income tax under the Gross Income Tax Act for the taxable year, less the amount which the individual estimates to be the sum of any credits allowable against the tax.

(c) N.J.S.A. 54A:8-4(d) requires individuals, other than farmers, who can reasonably expect their New Jersey personal income tax to be more than \$400.00 in excess of any credits allowable against the individual's tax, to file a declaration of estimated tax on or before April 15 of the taxable year. N.J.S.A. 54A:8-4(d) also divides the remainder of the taxable year into three periods. If during the period the individual becomes subject to the Gross Income Tax, for example as a part-year resident, or it becomes apparent that the individual's (other than farmer's) personal income tax for the taxable year can reasonably be expected to be more than \$400.00 in excess of any credits allowable against the individual's tax, a declaration of estimated tax must be filed

on or before the due date for the period. The periods and due dates are as follows:

1. After April 1 and before June 2 of the taxable year: June 15;
2. After June 1 and before September 2: September 15;
3. After September 1 of the taxable year; January 15 of the succeeding year.

Fiscal year taxpayers shall estimate their tax for the period covered by their fiscal year, and file a declaration of estimated tax on the 15th day of the fourth, sixth or ninth month of their fiscal year or the first month after the end of their fiscal year.

(d) A declaration of estimated tax of an individual having an estimated New Jersey income from farming (including oyster farming) for the taxable year which is at least two-thirds of the individual's New Jersey estimated income for the taxable year may be filed at any time on or before January 15 of the succeeding year.

(e) A declaration of estimated tax of an individual having a total estimated tax for the taxable year of \$400.00 or less may be filed at any time on or before January 15 of the succeeding year.

(f) N.J.S.A. 54A:8-5(a) requires payment of estimated tax in equal installments on due dates related to when the individual filed the declaration of estimated tax pursuant to (c) above. The due dates are as follows:

1. If the declaration is filed on or before April 15, installments are due on or before April 15 (with the filing of the declaration), June 15, September 15, January 15.
2. If the declaration is filed after April 15 and not after June 15: the first installment is due with filing of declaration, and the second and third installments are due on or before the following September 15 and January 15.
3. If the declaration is filed after June 15 and not after September 15, and is not required to be filed on or before June 15, the first equal installment is due with the filing of the declaration and the second equal installment is due on or before the following January 15.
4. If the declaration is filed after September 15, and is not required to be filed on or before September 15, the estimated tax is due in full at the time of the filing of the declaration.
5. If the declaration is filed late, all the installments that would have been due if the declaration was filed on time shall be paid with the filing of the declaration, and the remaining installments are due on the dates they would have been due if the declaration had been filed on time.

(g) An individual may amend a declaration of estimated tax if the individual experiences an unanticipated increase or decrease in income, credits, exemptions or deductions. If an amendment of a declaration is filed, any remaining installments shall be ratably increased or decreased to reflect any increase or decrease in the estimated tax. If any amendment is made after September 15 of the taxable year, any increase in the estimated tax shall be paid at the time of making such amendment. To amend a declaration, the individual should indicate any necessary changes when filing the next quarterly return. Form 2210 must be filed with the Gross Income Tax return showing that declarations and payments properly reflect the receipt of income.

Example 1: A taxpayer (wage earner) sells an investment in the third quarter. The proper amount of tax has been withheld from taxpayer's wages. The taxpayer pays the tax related to the sale of the investment with the third quarter declaration of estimated tax and files Form NJ-2210 with his or her final return. No estimated interest is due.

(h) If on or before February 15 of the succeeding taxable year an individual files his or her return for the taxable year for which the declaration is required, and pays the full amount of the tax shown to be due on the return:

1. Such return shall be considered as his or her declaration if no declaration was required to be filed during the taxable year, but is otherwise required to be filed on or before January 15;
2. Such return shall be considered as the amendment permitted by N.J.S.A. 54A:8-4(g) to be filed on or before January 15 if the tax shown on the return is greater than the estimated tax shown in a declaration previously made.

i. Any amount overpaid and appearing on the face of the return NJ-1040 for the immediate preceding year may be applied in lieu of any payment of estimated tax otherwise due under this section where the taxpayer indicates on the face of such return that he or she elects to have such overpayment so applied. Such amount will be considered to be a payment of the first installment of the estimated tax for the next succeeding year unless the taxpayer designates otherwise on the face of the return for the year in which the overpayment was made. The taxpayer may apply the credit partially or fully to any installment. The taxpayer may divide the credit evenly so that the installment payments are also equal. When applying the credit, the taxpayer should subtract the amount of the credit being applied from the installment amount due for the period, then remit the balance. When completing the estimated tax voucher, Form NJ-1040ES, the taxpayer should indicate only the amount actually remitted.

New Rule, R.2003 d.285, effective July 21, 2003.
See: 35 N.J.R. 1384(a), 35 N.J.R. 3386(a).

18:35-3.2 Failure to file declaration or underpayment of estimated tax

(a) If any taxpayer fails to file a declaration of estimated tax or fails to pay all or any part of an installment of estimated tax, the taxpayer shall be deemed to have made an underpayment of estimated tax.

(b) N.J.S.A. 54A:9-6(c) imposes an addition to tax on an underpayment of any installment of estimated tax by an individual. The amount of the underpayment for any installment is the excess of the lesser of:

1. The amount of the installment which would be required to be paid if all installment payments were equal to 80 percent of the tax (two-thirds of the tax for farmers) shown on the return for the taxable year; or

2. One hundred percent of the tax shown on the return for the previous taxable year, over the amount, if any, of

the installment paid on or before the last day prescribed for such installment.

(c) N.J.S.A. 54A:9-6(c) requires that each underpayment shall bear interest at the rate imposed under the State Tax Uniform Procedure Law, N.J.S.A. 54:48-1 et seq. (for tax first due or deficiencies first assessed on or after July 3, 1993, three percent above the prime rate assessed for each month or fraction thereof, compounded annually from the date the tax was originally due and payable until the date of payment). Interest is determined at the annual rate referred to above based on the amount of the underpayment of any installment of estimated tax for the period from the date such installment was required to be paid until the 15th day of the fourth month following the close of the taxable year, or the date such underpayment was received by the Director, whichever is earlier.