

## New Jersey Tax Court Approves Alternative Path for Seeking Tax Clarity

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Labor Ready's recent case reminds taxpayers that there is no need to wait for a lengthy audit or assessment before heading to court.

The New Jersey Tax Court recently affirmed a vendor's right and ability to seek court resolution of a tax dispute even before an audit occurs or an assessment is issued. The taxpayer, Labor Ready Northeast, Inc., (represented by McDermott) was informally notified that the New Jersey Division of Taxation considered its temporary staff services to be subject to sales tax under some circumstances. The taxpayer considered the statutory list of taxable services to be exclusive and, because that list does not include temporary staff services, it believed that its services were not taxable. Instead of waiting for the Division to audit (which could have started at any time or never), and instead of potentially over-collecting from customers, Labor Ready filed a complaint in the Tax Court under the Uniform Declaratory Judgments Act (UDJA). N.J.S.A. § 2A:16-50 et. seq. The UDJA allows a taxpayer to go to court "to settle and afford relief from uncertainty and insecurity with respect to rights, status and other legal relations" even in the absence of an assessment or final determination. See N.J.S.A. § 2A:16-51. A taxpayer may bring a declaratory action under the statute if there is a justiciable controversy (i.e., a real dispute between the parties) and there are no adequate or appropriate alternative administrative remedies.

### Justiciable Controversy

As proof that a justiciable controversy existed, Labor Ready submitted a letter it had received from the Division in August 2009 that explained the Division's position regarding Labor Ready's services. The letter explicitly stated that Labor Ready performed taxable enumerated services under certain circumstances and must collect and remit sales tax or procure resale certificates on some of its sales. Labor Ready disagreed with the Division's position and maintained that its sales were of non-taxable services. Clearly, the parties were at odds regarding the taxability of the services provided. Labor Ready argued that it should not be required to wait until the Division begins and completes an audit and then issues a final determination (meanwhile accruing substantial potential tax liability, interest and penalty liabilities if it does not collect in the interim) or alternatively harm its client relations by collecting sales tax that is not actually owed. Accordingly, Labor Ready argued that a justiciable controversy existed for which declaratory relief was proper and necessary.

The Division argued that no controversy or dispute existed because there was no ensuing final determination, and that the August 2009 letter was only advisory in nature. The Division argued that there was no justiciable controversy because it had no “intent” to assess and might never audit Labor Ready.

The Tax Court agreed with the taxpayer that a justiciable controversy existed for purposes of a declaratory judgment. The August 2009 letter evidenced a bona fide dispute regarding whether Labor Ready’s services were taxable. The Tax Court relied on a series of cases holding that a declaratory judgment action was proper where the Division issued “taxpayer specific” notices that acted as “forewarning[s]” and specifically addressed a taxpayer’s facts. The Tax Court explicitly rejected the Division’s argument that the August 2009 letter was merely advisory, distinguishing it from a “policy announcement” or “merely an advisory opinion.” The Tax Court specifically noted that the August 2009 letter was sent only to Labor Ready and that it detailed its business, and only its business, not taxpayers generally.

The Tax Court went so far as to say that the “clear intent of the letter was that Labor Ready be on notice” as to the Division’s position, which suggested that an audit was more than “purely hypothetical.” The Tax Court gave little credence to the Division’s argument that a justiciable controversy did not exist because the Division might ultimately not audit Labor Ready, noting that the Division stated that Labor Ready should not be concerned about an audit if it changed its business practice; this language created more than a speculative threat.

The Division also argued Labor Ready’s complaint was untimely and the Tax Court lacked jurisdiction because Labor Ready failed to file its complaint within 90 days (the statutory period for filing an appeal from a determination) from the date of the August 2009 letter. The Tax Court dismissed the Division’s argument, concluding, as it had in other cases, that it had jurisdiction over complaints seeking declaratory relief and also noting that there is no statute of limitations under the UDJA.

## **Alternative Remedies**

The Tax Court also agreed with Labor Ready that no alternative remedies would better address Labor Ready’s complaint. The Tax Court held that, in the absence of a final determination or assessment that triggers administrative review, declaratory relief is appropriate and because there had been no final determination that would entitle Labor Ready to administrative review as to the taxability of its services, declaratory judgment was proper.

## **Conclusion**

Although the final resolution of this case on the merits (whether Labor Ready must collect sales tax on its sales of temporary help services) is pending, the case is an important taxpayer victory. Taxpayers are generally hesitant (or decline) to bring an action in Tax Court before the issuance of an assessment for a variety of reasons. However, this

case serves as a welcome reminder to taxpayers that the opportunity may exist to get a court hearing without waiting for an audit and assessment. A declaratory judgment action can be advantageous for several reasons. Where a justiciable controversy exists, taxpayers need not adopt a “wait-and-see approach,” possibly racking up a significant liability in the process. The administrative appeals process can often be a long and expensive undertaking. By filing a declaratory action, taxpayers can accelerate their case to a potentially more desirable independent judicial forum, rather than proceeding through the state’s administrative forums. A speedy resolution of disputes brings certainty and can avoid financial statement disclosure.

It remains to be seen what this case law means for taxpayers seeking to file declaratory actions more broadly. Based on this holding, a taxpayer that receives a specific letter that states explicitly that the Division disagrees with a taxpayer position should consider filing a declaratory judgment action in the Tax Court. The same result might not occur if the Division had publicly stated its position in a manner not aimed at one specific taxpayer, but rather to a larger class of taxpayers (e.g., a regulation), or where the Division simply advises of its position through more generally applicable correspondence. The answer will likely hinge on the taxpayer’s ability to prove that a justiciable controversy truly exists. Taxpayers should assess their particular facts and consider whether seek to declaratory judgment in light of this case.

Labor Ready is represented by McDermott lawyers Peter L. Faber and Leah Robinson.

For more information regarding this subject, please contact your regular McDermott Will & Emery lawyer, or:

Peter L. Faber  
+1 212 547 5585  
[pfaber@mwe.com](mailto:pfaber@mwe.com)

Leah Robinson  
+1 212 547 5342  
[lmrobinson@mwe.com](mailto:lmrobinson@mwe.com)

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