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NJ Governor Christie Signs Legislation Phasing in Single Sales Fraction and Establishing Revenue Miles Fraction for Airlines

Publication Date: April 29, 2011

Yesterday, New Jersey Gov. Chris Christie signed into law apportionment legislation, P.L. 2011, c.59, that phases in a single sales factor for the corporation business tax beginning next year. The current apportionment formula, by contrast, is comprised of a property fraction, payroll fraction, and double-weighted sales fraction.

The new formula is projected to save New Jersey-based manufacturers at least $75 million annually. Accordingly, it was broadly supported by both the governor and the legislature, which unanimously passed the underlying bill (S-2753) in early March. Of course, out-of-state taxpayers whose New Jersey sales are proportionately higher than their New Jersey property and payroll will face a significant tax increase. A taxpayer with low property and payroll fractions could see its tax nearly double.

The phase-in would occur under the following schedule:

	Sales Fraction	Property Fraction	Payroll Fraction
Existing law	50%	25%	25%
Privilege periods beginning on or after January 1, 2012	70%	15%	15%
Privilege periods beginning on or after January 1, 2013	90%	5%	5%
Privilege periods beginning on or after January 1, 2014	100%	0%	0%

Given that the sales fraction will soon take on additional importance, now may be a good time for taxpayers to re-evaluate their New Jersey sales fraction. New Jersey does not conform to the Uniform Division of Income for Tax Purposes Act, and its sales-fraction rules often differ from other states' rules. Merely following the same sourcing methods used in other states could lead to missed opportunities (or potential exposures). Taxpayers should also pay close attention to pending controversies involving the sourcing of dock sales and patent royalties, and whether sales of goods should be sourced to the immediate or ultimate destination.

The legislation also establishes a new apportionment formula for airlines based on the ratio of revenue miles in New Jersey divided by total revenue miles. This new formula goes into effect for privilege periods beginning on or after January 1, 2012. Since the current airline fraction is based on the ratio of New Jersey departures to total departures, the new formula should benefit carriers with a disproportionate number of take-offs and landings in New Jersey. The legislation does not specifically address "overflight" miles involving flights that merely pass over New Jersey without a take-off or landing in the state. But consistent with other states' treatment of the issue, taxpayers should consider excluding these miles from the numerator of their fraction.

Interestingly, the legislation does not provide any definition of "revenue miles." Taxpayers should take advantage of this ambiguity. For example, the term could be interpreted as simply excluding "dead head" miles. Alternatively, it may require some sort of calibration (such as using revenue-ton miles) to account for aircraft size or payload capacity. The potential for savings is illustrated by our Pennsylvania case, *FedEx Ground Package System, Inc. v. Commonwealth*, 939 A.2d 323 (Pa. 2007), in which we convinced the court to adopt the taxpayer's interpretation of "revenue miles" and reject the Department of Revenue's calculation.

For more information on the changes to New Jersey's apportionment formula, contact the authors of this Alert or another member of the Reed Smith State Tax Group. For more information on Reed Smith's New Jersey tax practice, visit www.reedsmith.com/njtax.

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