



Credit For Taxes Paid to Other Jurisdictions- S Corporation Income

TAM 2011-10 – Issued February 10, 2011

Tax: Gross Income Tax

The New Jersey Division of Taxation continues to maintain its long-standing position that a resident S Corporation shareholder that pays tax to other jurisdictions on S Corporation income allocated to New Jersey is not eligible for a credit for taxes paid to other jurisdictions on that income on the Gross Income Tax resident return (NJ-1040).

The credit for taxes paid to other jurisdictions is provided under the Gross Income Tax Act at N.J.S.A. 54A:4-1 and allows taxpayers to take a credit against the tax otherwise due under this Act for the amount of any income tax or wage tax imposed for the taxable year by another state on their income tax return. The credit is limited in N.J.S.A. 54A:4- 1(c) with regard to taxpayers that are S Corporation shareholders by stating that: "No credit shall be allowed against the tax otherwise due under this act for the amount of any income tax or wage imposed for the taxable year on S Corporation income allocated to this State."

When an S Corporation allocates 100% of its income to New Jersey and this same S Corporation pays a tax based on or measured by income to both another state and to New Jersey, the S Corporation is eligible for a credit against its tax on the New Jersey Corporation Business Tax S Corporation return (CBT-100S). See N.J.A.C. 18:35-1.5(c)7. For New Jersey Gross Income Tax purposes, the Corporate Income taxed by both the other state and on the New Jersey CBT-100S return is deemed S Corporation income allocated outside of New Jersey.

The payment of a minimum tax to another state by an S Corporation does not fulfill the above criteria and the income is not deemed to be S Corporation income allocated outside of New Jersey under N.J.A.C. 18:35-1.5(c)6.

In addition, for all CBT-100S filers, beginning with the 2007 tax year, there is no longer a tax on income of the S Corporation that is not subject to Federal Corporate taxation. Therefore, only income of the S Corporation that is subject to Federal Corporation tax and subject to a Corporate Tax based on or measured by income in both another state and on the New Jersey CBT-100S return, and which is eligible for a credit on the New Jersey CBT-100S return, will meet the criteria for income deemed to be S Corporation income allocated outside New Jersey.

Thus, if a New Jersey S Corporation allocates 100% of its income to New Jersey but does not, or cannot, take a credit for taxes paid to other jurisdictions on the CBT-100S return then a resident shareholder is not entitled to a credit for taxes paid to other jurisdictions on the Gross Income Tax return for S Corporation income allocated to New Jersey.

S Corporation income allocated to New Jersey means income statutorily allocated pursuant to N.J.S.A. 54:10A-6. Taxpayers maintaining a regular place of business outside New Jersey use Schedule J on the CBT-100S return in accordance with N.J.S.A. 54:10A-8. The application of N.J.S.A. 54:10A-8 is through the Division's CBT regulation N.J.A.C. 18:7-8.3.

N.J.A.C. 18:7-8.3 provides that if it appears that the business allocation factor computed on the basis of all or any of the property-receipts-payroll fractions does not properly reflect the activity, business receipts, capital, entire net worth or net income of the taxpayers in New Jersey, the Director may adjust or the taxpayer may request an adjustment of the business allocation factor.

To address the issue of an adjustment of the business allocation factor, the Individual Tax Audit Branch and the Office Audit Branch are working to ensure that the allocation factor relief claimed by S Corporations is valid and that validated and approved allocations are extended accordingly to the individual shareholders in the filing of their Gross Income Tax returns with regard to any credit for taxes paid to other jurisdictions that may be warranted.

As of July 1, 2010, the Corporation Business Tax's statutory requirement that a corporation must maintain a regular place of business, other than a statutory office, outside of New Jersey in order to allocate income inside and outside of New Jersey has been eliminated. Many S Corporations that were previously precluded from allocating because they did not meet the statutory requirement are now able to do so. This relief will flow through to S Corporation resident shareholders who will be eligible for a credit for taxes paid to other jurisdictions on the S Corporation income allocated outside of New Jersey.

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