



# Initial Guidance on New Jersey's Conformity to I.R.C. §1502 for Combined Returns

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**Tax: Corporation Business Tax**

Beginning with tax year 2019, New Jersey mandated combined reporting. Subsequently, P.L. 2020, c. 118, which was signed into law on November 4, 2020, made a series of technical corrections, clarifications, and changes to the Corporation Business Tax Act. Among other things, the technical changes clarified that several aspects of the federal consolidated return rules apply to combined returns.

The purpose of this Technical Bulletin is to provide general guidance on the federal Internal Revenue Code sections or rules as they relate to, or differ from, the New Jersey Corporation Business Tax Act. However, it may not encompass all of the various issues. Therefore, the Division of Taxation reserves the right to add additional topics or cover specific issues involving the federal consolidated return rules and the Corporation Business Tax Act in updates to this publication or in additional Technical Bulletins.

Combined returns are not necessarily the same as consolidated returns, although they are similar. A consolidated return is filed with the IRS by a parent company or a corporation that owns a group of affiliated companies. Whereas, a combined return is filed by members of a commonly controlled group of businesses that are required to combine the profits/losses they earned in a state. A New Jersey combined group can be composed of:

- The same group of taxpayers filing a federal consolidated return,
- A group of taxpayers filing various separate federal returns,
- Multiple federal consolidated return groups,
- Taxpayers that are partially from the same federal consolidated group, or
- Taxpayers that do not file any federal returns.

For purposes of the New Jersey Corporation Business Tax Act, the starting point for taxable income is entire net income before net operating losses and special deductions with several modifications for additions and deductions (see N.J.S.A. 54:10A-4 and N.J.A.C. 18:7-3.12). Thus, a taxpayer's entire net income as reported on a federal consolidated return must match the taxpayer's entire net income on line 28 on Schedule A of the CBT-100, CBT-100U, or BFC-1, before the respective New Jersey modifications. This principle was successfully litigated by the Division in *MCI Communication Services, Inc. v. Director Division of Taxation*, Docket No. 013905-2010, (Tax Court of New Jersey 2015); affirmed 2018 N.J. Super. Unpub. LEXIS 1401; cert. denied 195 A.3d 528 (October 18, 2018).

**For privilege periods ending on and after July 31, 2019, N.J.S.A. 54:10A-4.6 in relevant part states:**

- e. Except as otherwise provided by regulation, business income from an intercompany transaction among members of the same combined group shall be deferred in a manner similar to the deferral under 26 C.F.R. s.1.1502-13, as determined by the director. Upon the occurrence of either of the events set forth in paragraphs (1) and (2) of this subsection, deferred income resulting from an intercompany transaction among members of a combined group shall be restored to the income of the seller and shall be included in the net income of the combined group as if the seller had earned the income immediately before the event:
  - (1) The object of a deferred intercompany transaction is: (a) resold by the buyer to an entity that is not a member of the combined group, (b) resold by the buyer to an entity that is a member of the combined group for use outside the unitary business in which the buyer and seller are

engaged, or (c) converted by the buyer to a use outside the unitary business in which the buyer and seller are engaged; or

- (2) The buyer and seller cease to be members of the same combined group, regardless of whether the buyer and seller remain sufficiently interdependent, integrated, and interrelated through their activities so as to provide a synergy and mutual benefit that produces a sharing or exchange of value between them.

In the case of an event set forth in paragraph (2) of this subsection, no portion of the income or loss shall be included in entire net income of the combined group, but shall be included in the entire net income of the respective member.

- f. A charitable expense incurred by a member of a combined group shall, to the extent allowable as a deduction pursuant to section 170 of the federal Internal Revenue Code, 26 U.S.C. s.170, be subtracted first from the combined group's entire net income, subject to the income limitations of that section applied to the entire net income of the group. A charitable deduction disallowed under section 170 of the federal Internal Revenue Code, 26 U.S.C. s.170, but allowed as a carryover deduction in a subsequent privilege period, shall be treated as originally incurred in the subsequent year by the same member and the provisions of this section shall apply in the subsequent privilege period in determining the allowable deduction for that privilege period.
- ...
- j. An expense of a member of the combined group that is directly or indirectly attributable to the income of any member of the combined group, which income this State is prohibited from taxing pursuant to the laws or Constitution of the United States, shall be disallowed as a deduction for purposes of determining the combined group's entire net income.
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- m. To the extent consistent with the Corporation Business Tax Act (1945), P.L.1945, c.162 (C.54:10A-1 et seq.), the federal rules and regulations governing consolidated return net operating losses and net operating loss carryovers shall apply to the New Jersey net operating loss carryover provisions under subsection h. of this section as though the combined group filed a federal consolidated return, regardless of how the members of the combined group filed for federal purposes.
- n. The principles and provisions set forth in federal regulations promulgated pursuant to section 1502 of the Internal Revenue Code (26 U.S.C. s.1502), shall apply to the extent consistent with the Corporation Business Tax Act (1945), New Jersey combined group membership principles, New Jersey combined unitary return principles, and regulations set forth by the director.
- ...
- p. This section shall apply to world-wide group elective combined returns and affiliated group elective combined returns in accordance with section 23 of P.L.2018, c.48 (C.54:10A-4.11). An election to file an affiliated group combined return shall be an election to treat all of the member's attributes and income as though they were from one unitary business.

Thus, in general, the principles set forth in the Treasury regulations promulgated under Section 1502 of the Internal Revenue Code (including the principles relating to deferrals, eliminations, intercompany offsets, etc.) apply to the extent they are consistent with the New Jersey Corporation Business Tax Act and the unitary business principles to a combined group filing a New Jersey combined return as though the combined group filed a consolidated return. Additionally, the limitations governing federal net operating losses and net operating loss carryovers apply. Federal carrybacks do not apply because New Jersey net operating losses can only be carried *forward* for 20 privilege periods.

**Tax Rates, Payments, and Due Dates.** For New Jersey Corporation Business Tax purposes, tax rates, tax computations, estimated payment provisions, and due dates are different than for federal purposes.

**Definitions, Inclusions, Exclusions, Modifications, Tax Base, and Return Matters.** The New Jersey Corporation Business Tax Act ("Act") has its own definitions for combined group, affiliated group (for the purposes of the affiliated group election), member, taxable member, nontaxable member, group privilege period, common ownership, commonly owned, managerial member, etc. It also has its own included and excluded entity provisions, which differ from the federal consolidated return entity inclusions and exclusions. The Act has its own additions, deductions, exclusions, and other modifications to entire net income. New Jersey combined returns are filed using a default mandatory water's-edge filing method or the elective world-wide or affiliated group filing method. To be included on a water's-edge return or world-wide return, an entity needs to be part of a unitary business of the combined group as defined in the Act. Water's-edge and world-wide returns are state tax concepts not federal consolidated return concepts. The composition of the New Jersey affiliated group combined return for New Jersey purposes may be larger than the federal affiliated group because there are specific New Jersey inclusions and exclusions. For combined groups, New Jersey has its own payment, accounting period, and liability provisions (N.J.S.A. 54:10A-4.8 and N.J.S.A. 54:10A-4.10). The managerial member of the New Jersey combined group (which may be a different corporation than the corporation filing the federal consolidated return on behalf of a federal consolidated group) files the combined return on behalf of the combined group.

**Ownership Requirements and Attribution Rules.** For New Jersey combined reporting purposes, the requisite ownership threshold is more than 50%. Although the federal rules otherwise apply, New Jersey does not conform to the 80% ownership required for federal consolidated returns. If a New Jersey combined group composition is different than the federal consolidated return, the group must compute the combined group entire net income as though the entire group filed a federal consolidated return and then make the New Jersey additions, deductions, exclusions, and other modifications.

**Intercompany Transactions.** Generally, the provisions of 26 C.F.R. 1.1502-13 apply, except as otherwise noted in N.J.S.A. 54:10A-4.6(e) and except where 26 C.F.R. 1.1502-13 deals with specific provisions of the federal Internal Revenue Code to which New Jersey does not conform.

**Depreciation and Certain Expensing Provisions.** The federal consolidated return rules in relation to depreciation and expensing apply, except that New Jersey has decoupled from I.R.C. §168(k) bonus depreciation and I.R.C. §179 expensing provisions and certain other depreciation and expensing provisions. See N.J.S.A. 54:10A-4(k)(1), N.J.S.A. 54:10A-4(k)(2)(F), N.J.S.A. 54:10A-4(k)(12), and N.J.S.A. 54:10A-4(k)(13). Adjustments must be made accordingly.

**Dividends, Dividend Exclusion, GILTI, FDII, Net Operating Losses (NOLs), and Special Deductions.** The federal dividend received deductions (DRD) are special deductions for federal purposes, which are adjustments below line 28. As such, these provisions in the federal consolidated rules **do not** apply for New Jersey purposes. New Jersey has its own dividend exclusion (see N.J.S.A. 54:10A-4(k)(5)). The rules and limitations governing the federal dividend received deductions were not incorporated into N.J.S.A. 54:10A-4(k)(5). Pursuant to N.J.S.A. 54:10A-4.6(d), dividends paid by one member to another member of the combined group are eliminated from the income of the recipient.

**Note:** The rules and limitations of the NOLs will be discussed in separate Technical Bulletins.

The NOL-DRD ordering rules found in N.J.S.A. 54:10A-4(u), N.J.S.A. 54:10A-4(v), and N.J.S.A. 54:10A-4.6(h)(1) (by operation of N.J.S.A. 54:10A-4(v)) still apply because they are provisions of the Corporation Business Tax Act. The federal limitations that govern the interaction of the federal net operating losses/net operating loss carry overs and the federal dividend received deductions **do not** apply because the federal dividend received deductions are special deductions under the Internal Revenue Code. Likewise, the federal dividend deduction rules do not apply to N.J.S.A. 54:10A-4(k)(5) since the federal dividend received deductions are special deductions for federal purposes.

The only federal rules with regard to a federal special deduction that apply are the rules in relation to IRC section 250 (see [N.J.S.A. 54:10A-4.15](#), which specifically coupled the Act to IRC section 250). None of the other federal rules governing federal special deductions apply. If a combined group has GILTI and FDII, and the members are eligible for the IRC section 250 deductions, the federal consolidated return rules and federal rules governing the interaction of net operating losses and the IRC section 250 deductions apply.

**Tax Credits.** New Jersey has its own tax credits and its own rules for tax credits, except with regard to the New Jersey Research and Development Tax Credit. Although the New Jersey Research and Development Tax Credit has its own specific limitations, the federal rules governing IRC section 41 apply.

**Discharge of Indebtedness.** In general, New Jersey follows the guidelines set forth under federal consolidated return regulations regarding IRC section 108. Although there may be some caveats, see [N.J.S.A. 54:10A-4\(k\)\(6\)](#), [N.J.S.A. 54:10A-4\(k\)\(14\)](#), [N.J.S.A. 54:10A-4\(u\)](#), and [N.J.S.A. 54:10A-4\(v\)](#). Additionally, IRC section 108 and the interaction with NOLs will be discussed in separate Technical Bulletins.

The Division of Taxation is in the process of drafting regulations addressing the topics covered by this Technical Bulletin.

**Note:** A Technical Bulletin is an informational document that provides guidance on a topic of interest to taxpayers and may describe recent changes to the relevant laws, regulations, and/or Division policies. It is accurate as of the date issued. However, taxpayers should be aware that subsequent changes to the applicable laws, regulations, and/or the Division's interpretation thereof may affect the accuracy of a Technical Bulletin. The information provided in this document does not cover every situation and is not intended to replace the law or change its meaning.