

Real Estate Group

Legal Update

ESTIMATED GAINS TAX ON REAL ESTATE SALES NOW REQUIRED AT CLOSING

On August 1, 2007, the New Jersey Legislature adopted N.J.S.A. 54:50-38, which modified the reporting requirements of a sale of assets not in the ordinary course of business. Previously, N.J.S.A. 54:32B-22(c) imposed a reporting duty only on businesses required to collect sales and use tax and escrow notifications and clearance waivers were issued based solely upon any tax deficiency found to be due. This was expanded to include commercially used real estate assets of a business being sold, considering the sale of business-owned real estate as part of the bulk sale of an operating business. The direction from the Division as of August 2007 required that even single asset real estate entities file the new form C-9600, however, in a transaction in which the sale of real estate was unrelated to an organized business operation, no escrow would be required because of the lack of a sales tax or employers wage tax component. In large part, that position of the State was consistently applied and the transferee filing the C-9600 in a pure real estate transaction routinely received a no escrow letter from the State.

New Rules

Late last year, the Division changed its position, signifying a dramatic change in the method for collection of tax on gains realized from the sale of real estate. The Division now asserts that all real estate sales for real estate primarily used for business operations made not in the ordinary course of business, including single asset entities unattached to an ongoing business, will be reviewed at the time of sale, not only for tax deficiencies (which are largely aimed at operating entities), but also to the amount of any capital gain estimated on the sale of the real estate.

While in the past, New Jersey resident sellers of real estate paid taxes on gain in the normal course of filing tax returns, this is no longer the case. The State asserts it will impose on the purchaser's attorney, an escrow obligation equal to the amount of gain as estimated by the State upon review of form C-9600 and the contract of sale supplied with the form. Payment of the tax is now due at the time of closing. Purchases failing to comply with this new directive risk imposition of a payment obligation for a seller's unpaid capital gains and other taxes.

TTD Form

In order to forestall an unusually large escrow demand by the State, the State has developed form TTD which may be submitted separately by the Seller prior to closing. Form TTD (Asset Transfer Tax Declaration) is a declaration of estimated tax by the taxpayer. The form requires that each member, partner or shareholder of the selling entity complete a separate TTD. Accordingly, any entity or individual receiving a K-1 must comply. In addition, the TTD to be filed by the Seller is considered confidential and not a form that the Seller needs to share with the Purchaser.

Unanswered Questions

The practical implementation of this new regulation is producing various anomalies that require treatment on a case by case basis. For example, what is to be done when there will be no closing proceeds such as the sale of real estate for less than the mortgage amount or in the instance of a Purchaser paying nominal consideration for environmentally contaminated property? Additionally, the requirement that each member of the entity complete a TTD declaration can be cumbersome when the entity is comprised of numerous members or partners. The Division is still considering methods for streamlining the process without compromising the effectiveness.

Sellers, purchasers and their attorneys need to become familiar with the requirements involved with the new rules and the Asset Transfer Tax Declaration form in order to avoid surprises at the time of closing and liability for unpaid taxes.

This Scarinci Hollenbeck Client Alert has been prepared for the general information of clients and friends of the firm. It is not meant to provide legal advice with respect to any specific matter and should not be acted upon without professional counsel.

Individuals with questions are urged to contact the Scarinci Hollenbeck attorney with whom they work. Questions can also be directed to following attorney:

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