

**STATE OF NEW JERSEY
DEPARTMENT OF THE TREASURY
DIVISION OF TAXATION**

SPECIAL PROJECTS UNIT

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I. Introduction

This morning I will discuss a relatively new aspect of the New Jersey Division of Taxation's continuing efforts to address non-compliance. The Special Projects Unit of the Investigations Branch was created to focus resources and attention primarily on unregistered out-of-state transient businesses deriving economic benefit from New Jersey.

The accomplishments of this unit are the result of close cooperation and participation among several different branches of the Division of Taxation. Numerous State agencies also participated in this effort. These include the New Jersey Division of Law, the Casino Control Commission, the New Jersey Department of Labor, the New Jersey Division of Motor Vehicles and the New Jersey State Police. Trade associations and construction unions provided valuable assistance in identifying potential offenders.

Background

A discussion of any tax compliance problem and the remedy to that problem should include an examination of the economic environment and geography of the taxing jurisdiction. In particular, the underground cash economy requires attention because New Jersey is a wealthy state; second only to Connecticut in terms of per capita income, and borders two major cities, New York and Philadelphia. Delaware and Maryland are also within an easy drive.

In 1996 the State of New Jersey offered its second Tax Amnesty program. The extensive publicity made clear that there would be consequences for not coming forward during the Amnesty. Enforcement activity was going to increase. After Amnesty, the entire Investigations Branch of 200 people began extensive state-wide canvassing sweeps, including weekends, of the cash economy transient vendors at flea markets, trade shows, craft fairs, etc. An analysis of the early results made

clear we needed a new approach and procedure to gain compliance from out of State vendors who are highly mobile and quickly out of our jurisdiction.

A novel interpretation of existing statutory language provided the critical tool, that is the ability to make an immediate jeopardy assessment and enforce it with seizure powers. The Branch stepped up its attention to the transient vendor sector of the cash economy and supplemented the activity with the use of jeopardy assessments. A total of 1,547 jeopardy assessments were served against transient vendors in 1997 and 1998 and resulted in the collection of \$1.8 million in new money. Almost 5,000 new registrations were secured. In addition, almost 40,000 vendors were canvassed in person and were made aware of their tax obligations to the State of New Jersey.

The scope of the problem with transient out-of-state businesses became more widely known with the publication of a report by the State Commission of Investigation in 1997

outlining the effect that tax non-compliance had on the State's economy. The Division was also contacted with complaints from various Trade organizations and Unions conveying the impact this non-compliance had on them. They requested that the Division “level the playing field”, for the business or employer that follows the rules. The Division was determined to increase the pressure on the target groups. The decision was made to create a special unit to identify the areas of non-compliance and fashion methods that would result in voluntary; if necessary, or involuntary compliance.

II. The Concept

The Division's activities following the 1996 Amnesty program substantiated the opinion that compliance among many transient out-of-state vendors was sorely lacking. Our efforts identified many reasons for this non-compliance. The question was what was the best viable solution?

In 1998, using existing resources, a fifth region was carved out of the Investigations Branch. The new region was

named the "Special Projects Unit" and consisted of four teams spaced geographically across the state. Volunteers were encouraged. Each team was staffed with a supervisor and from five to seven investigators. Members of this unit received training in the business activities of an out of state vendor that would create nexus with New Jersey. The purpose of the Unit is to identify pockets of tax non-compliance such as the transient out-of state vendors. Both industry specific investigations and geographic point of entry surveillance techniques are utilized in the initiatives or programs developed to address the problem.

While all five regions exercise their statutory authority to make immediate, on-site jeopardy assessments of tax due, this enforcement tool would be the essential component for the activities of the Special Projects Unit. In addition to their focus on transient out-of-state vendors, the Special Projects Unit developed other projects to combat non-compliance that fell outside the expected activity of the other four regions. These

projects could be long-term initiatives or specialized short-term projects to target an immediate concern.

In addition to the creation of the new region, an extensive information campaign was undertaken. A wide spectrum of organizations were notified of the Division's intentions concerning non-compliance. "Special Notice to Vendor", as well as, "Notice to Boat Owner" flyers were widely distributed. A toll free telephone number and the Catch a Tax Cheat (CATCH) program were established to encourage anonymous leads. These programs were also highlighted in the Division of Taxation publication "State Tax News" which is widely distributed to accounting organizations.

Statutory Authority

Prior to the establishment of the Special Projects Unit in 1998 a thorough review was undertaken of the enforcement powers granted to the Division under the State Tax Uniform Procedure Law.

The following are the key elements used by the Special Projects group.

Arbitrary Assessment- If a taxpayer fails to file a report as required, the Director may estimate the tax liability from any available information and assess taxes, fees, penalties, and interest.

Jeopardy Assessment- The Director is authorized to make an arbitrary assessment, even if no tax return is due at that time, in the case of taxpayers who intend to depart quickly from New Jersey; remove from New Jersey their property or any property subject to New Jersey state tax; conceal themselves, their property or other property; or discontinue business; or do anything else to prejudice or render ineffectual attempts to assess or collect tax. Under jeopardy assessment, the Director may proceed to collect the tax or compel security for the tax and thereafter give notice of the finding to the taxpayer, together with a demand for an immediate report and immediate payment of the tax.

The Director of the Division of Taxation has the authority to make an examination of the taxpayer's place of business, tangible personal property, books, records, and documents.

The Director of the Division of Taxation may demand a bond or other security if he finds that the collection of tax, interest, or penalties may be prejudiced.

Protests

It should be noted that a taxpayer has 90 days after the Division issues a notice of assessment in which to file a written protest, setting forth the reason for the protest and requesting a hearing. Filing of the protest generally stays collection of the tax until 90 days after the Director's final determination, provided the taxpayer furnishes security where required. Security is required when an arbitrary assessment is made due to a taxpayer's failure to file a report or upon a determination that a taxpayer intends to abscond, conceal, or remove property from the state, or discontinue business.

Members of the Special Projects Unit focus on specific areas of non-compliance best addressed by mobile field staff. The essential ingredient for the Unit is the ability to utilize the jeopardy assessment provisions of the law. These tools allow Division personnel to react immediately to the problem that they are confronting. The use of both arbitrary and jeopardy assessments are subject to strict procedures to protect the Division and the vendor.

Prior to the issuance of a Warrant of Execution - Jeopardy Assessment the investigator must document the following:

- What activity was the taxpayer conducting that created nexus with New Jersey?
- What taxes administered by the Division of Taxation is the vendor subject to and why?
- What was the available information that led to the arbitrary assessment? This information must support the time period and amount assessed.

- Why was the use of the jeopardy assessment necessary?

While the use of the jeopardy assessment is a key tool, Special Projects Unit personnel regularly use all the other collection and enforcement tools available by statute. These include but are not limited to the filing of a Certificate of Debt (COD), which serves as an administrative judgement, and the enforcement of the judgment by the levy, seizure and auction sale of business and personal assets.

The following are the current projects of the Special Projects Unit:

Bankruptcy Project

This project attempts to combat the evasion of taxes through the misuse of the bankruptcy laws. It is specifically targeted to recover funds from individuals who file for Chapter 13 protection under the Federal Bankruptcy Statutes but fail to adhere to the conditions of the bankruptcy plan.

Upon the filing of a Chapter 13 bankruptcy petition, the Division of Taxation is prohibited from taking any further collection action. In many instances this prohibition delays or limits the filing of a Certificate of Debt or nullifies collection steps such as levy or seizure action.

As a condition of the protection afforded under Chapter 13, the individual must establish a plan, monitored by an appointed trustee that seeks to resolve covered liabilities. Failure to comply with or establish a plan may result in the dismissal of the Chapter 13 filing.

When the debtor files for protection under Chapter 13 it is required to begin making payments to the trustee. The trustee holds these payments until a repayment plan is established. If the bankruptcy is dismissed, the trustee returns the payments to the individual. Once the Chapter 13 is dismissed the Division of Taxation is no longer prohibited from taking collection action.

The process of the Bankruptcy Project is as follows:

- A Notice of Order Dismissing Case is received by the Division of Taxation.
- A determination is made if the trustee is holding funds to be refunded.
- Research of the individual's liability to the Division is completed.
- A levy is served on the trustee.
- All funds, up to the full amount of the liability, are paid over to the Division of Taxation.

Boat Project

The Boat Project is a year round project which seeks to identify boats that are located or used in New Jersey and the owner has avoided paying the appropriate sales or use tax. Investigators locate suspect vessels during the summer months by canvassing marinas, boat dealers, and private docks. Investigators also cruise the lagoons and other New Jersey waterways in the Division's 17 foot shallow draft Boston Whaler attempting to locate boats that are subject to tax. The New

Jersey State Police-Marine Bureau also supplies information to our investigators. Vessels that draw attention are those with an out-of-state port on their stern and/or boats without a New Jersey registration on the bow.

Experience has led the Division to conclude that many expensive vessels found in New Jersey waters are purchased by Delaware corporations specially set up by New Jersey residents. The ruling in the New Jersey Tax Court case *Coppa Bros. vs. the Director*, has been key in piercing the corporate veil used to avoid or evade taxes.

Compliance Surveillance

The Special Project Unit conducts surveillance as a means to locate out of state vendors doing business in New Jersey. Working in teams, the investigators canvass likely locations, such as shopping malls, strip malls, industrial parks and other business areas along the New Jersey border with New York, Pennsylvania and Delaware. Surveillance within city business districts has also proven to be extremely successful. Again,

through experience the investigators have determined that most commercial vehicles entering these areas will be delivering to a customer located nearby. Whenever compliance surveillance is scheduled, the investigators first notify the local police of the presence of Division personnel and the nature of their activity. If difficult enforcement action becomes necessary, the local P.D. is contacted and again their assistance is requested at the scene.

Upon identifying the business vehicle of an out of state business, the investigator does some preliminary work to determine if the company is properly registered in New Jersey. Each compliance surveillance team has a cell phone and a lap top computer with remote access software that enables them to immediately access the Division's records.

Only when a company is considered not to be compliant, which may mean either not registered, delinquent or deficient is the driver approached and the vehicle detained. The driver is interviewed to determine what activities the company is

involved in and the length of time the company has been doing business in New Jersey. The investigator also requests to view the invoices for that day's deliveries. The driver is then advised to contact the company's office so that the investigator can speak with the appropriate representative of the company to determine if the company is registered in New Jersey under some other name.

If the business is not registered, the investigator continues the interview process to determine nexus, potential liability and whether jeopardy assessment action is required. The company representative is advised of the potential consequences at the beginning of the interview. When the investigator has gathered all the available information, he is required to contact the supervisor in charge and advise the supervisor of the findings. The supervisor makes the final decision on whether a jeopardy assessment is required and the amount of the assessment. The investigator will contact the company representative again and advise them of the decision.

If immediate payment is deemed necessary, the company representative is given three methods of payment. They may wire transfer into the State's bank account, deliver a certified check to the site or the Division will levy against any funds due from the purchaser of their goods. A Warrant of Execution-Jeopardy Assessment is prepared and served. Upon confirmation or delivery of the payment, the driver is handed a sealed envelope with the Warrant, a Notice to Vendor flyer, a New Jersey Business Registration Package and the investigator's business card. The company representative is advised of their appeals rights which are also printed on the Warrant. Failure to satisfy the demand for immediate payment may result in the seizure of the company vehicle and the merchandise on board.

The Construction Project was developed because of the problem of nonpayment of use tax on construction materials. An additional issue of importance is out of state corporations

not reporting their income from construction work performed in New Jersey.

Investigators identify construction sites in many ways.

These include:

- Review of Dodge reports
- Referrals from construction unions
- Municipal construction offices
- Field observations in areas where construction activity is ongoing

When a construction site is identified, the investigator contacts the general contractor and explains the Division's program. The general contractor is asked to submit a list of all subcontractors and suppliers for that project. The list should include the corporation name, address, telephone number, contact person and federal identification number of each subcontractor. The general contractor is advised that if they prefer they can have the subcontractors and suppliers contact the investigator directly. Each subcontractor and supplier is

then mailed a nexus survey, Notice of Vendor flyer and a contact letter and requested to contact the investigator. All subcontractors and suppliers that take advantage of this initial contact are interviewed to establish their beginning date of business in New Jersey. They are advised to submit all tax returns and payments due. They are also advised of the rules governing use tax on material purchased out of state but delivered and used in New Jersey.

If a subcontractor or supplier fails to comply with the Division's request for voluntary cooperation, the investigator obtains a copy of that vendor's contract or invoice from the general contractor. The contract is reviewed to determine the nature of the work performed, the monetary value, the payment schedule and if any retainage will be held. After a thorough review of the contract, which includes a determination of the anticipated completion of work and date of final payment, the investigator and supervisor determine the best enforcement avenue to pursue.

If time permits, the investigator will obtain compliance by the normal collection process. This entails mailing Demand for Payment notices to the business and allowing ninety (90) days for payment or appeal. If necessary, a Certificate of Debt is filed against the vendor. However, if the supervisor determines that time is a critical factor, the supervisor is authorized to utilize the jeopardy assessment procedure. There are two courses the jeopardy assessment action can take. One is to demand immediate payment from the subcontractor or supplier and if necessary seize available assets such as tools or vehicles. The second action is to serve a Warrant of Execution-Jeopardy Assessment against funds payable to the vendor from the general contractor. If the taxpayer's inaction results in jeopardy assessment action, the taxpayer is required to resolve any issues by filing a protest with the Division's Conference and Appeals Branch. The general contractor is required to turn over to the State any funds that are payable up to the amount on the Warrant.

Division of Motor Vehicles (DMV) Project

The New Jersey Division of Motor Vehicles (DMV) has provided assistance and made valuable information available to the Division of Taxation.

There are two initiatives that were developed with the cooperation of DMV.

- All commercial vehicles carrying freight or products above a certain weight limit or width are required to obtain a special permit from DMV. This permit provides the following information: point of entry into New Jersey, destination, product or cargo, the name of the company delivering the merchandise and a telephone number. This permit is only valid for three days. DMV allows representatives from the Division of Taxation access to these permits. The information available enables investigators to identify vendors having potential nexus with New Jersey or if products are delivered by common carrier, of possible use tax liability. Investigators can use

this information prior to delivery, during delivery or after delivery to obtain compliance.

- DMV personnel frequently set up roadside checkpoints. Commercial vehicles and bus companies are required to stop at these checkpoints for inspection. During the course of the DMV inspection of the vehicle, Taxation personnel run a cursory check to determine if the company is registered. Vehicles of companies not registered are moved to a secure area by DMV staff to await further investigation by Taxation Investigators. Companies found to be non-compliant are subject to immediate jeopardy assessment action as previously described.

There are two initiatives included in the Nexus Review Project. The first is to assist the Division's Office Audit Branch Nexus Section to verify information they receive and to enforce the Estimated Tax Assessments issued by Audit. When Audit identifies a vendor they believe is doing business in New Jersey, they reach out to that vendor to obtain information to

determine if nexus exists and the potential liability. The source of the information is the nexus survey. Special Project Unit investigators conduct field investigations to determine the validity of the information that was supplied on the nexus survey. When Audit determines that a company has nexus and the company refuses to file returns, an Estimated Tax Assessment is issued. If compliance is not forthcoming, a Certificate of Debt (COD) is entered. Special Project Unit personnel are used to enforce collection of the COD.

The second initiative is to perform nexus investigations that consist of contacting New Jersey businesses and reviewing their purchase invoices from out of state suppliers. The business owner is interviewed concerning the activities of the out of state suppliers. Questions include means of delivery, sales method, collection practices and technical assistance provided. Out of state suppliers with potential nexus are contacted by letter and requested to submit a nexus survey. Companies with nexus are requested to voluntarily comply or

are subjected to the various enforcement actions previously discussed.

As the home of one of the nation's busiest seaports, Port Newark, and located within hours of so many other major east coast population centers, New Jersey has an abundance of warehouses and distribution centers. Since physical presence is a key component of nexus, the Special Projects Unit has canvassed warehouses and distribution centers. Many companies are unaware of the elements that create nexus and their legal and accounting representatives are often not made aware of their rental of space or storage of inventory in New Jersey.

Special Project Unit personnel canvas the warehouses and request a list of all tenants renting space. Generally, they request the names of tenants for the last three years. The warehouse manager is interviewed to establish what type of inventory or product is stored at the site. Initial contact of all non-registered tenants is made by mail. The letter asks the

business to complete a nexus survey and register their business voluntarily. They are required to file returns back to the original date of entry into New Jersey. Companies that do not respond to the written request are contacted by telephone, advised of the requirement to be registered and what New Jersey taxes they are subject to. Businesses that do not voluntarily register are subject to jeopardy assessment. In the cases where an assessment action is deemed appropriate, the warehouse manager is served a Warrant of Execution-Jeopardy Assessment and advised that any inventory in storage cannot be moved. The unregistered business is sent the Warrant by certified mail. Thus far, in every instance the vendor has come forward, paid the assessment and completed a New Jersey registration. The companies have ranged from a small North Carolina beer distributor to a national dot.com retailer.

The Weigh Station Project has had a dramatic impact in improving compliance. In 1998, the New Jersey Division of

Taxation and the New Jersey State Police signed a Memorandum of Understanding. This MOU enabled the Special Project Unit team to coordinate with the State Police who inspect commercial vehicles at weigh stations. The presence of the Division's investigators at these checkpoints has advertised the Division's intent to gain compliance.

A state of the art weigh station located on Route 295 near the Delaware Memorial Bridge has been an especially productive location. Not only have there been a significant number of unregistered businesses identified but also significant revenue has been collected. The greatest impact, however, has been from the resulting "free advertising" New Jersey gets. Truckers from across the nation have spread the word that Taxation Agents are checking commercial vehicles coming into New Jersey and if you are not just passing through, you had better be registered to do business there.

VI In Conclusion

The New Jersey Division of Taxation has sought to be progressive and innovative in tax administration. Programs are developed and implemented to address those areas where significant tax avoidance and revenue short falls exist.

Voluntary compliance is encouraged but special projects are put into place to improve compliance. When all else fails, the use of the jeopardy assessment provision of the statutes and the creation of the Special Projects Unit have proven to be extremely valuable for their deterrent effect and for the new revenue generated. The projects and initiatives implemented by the Special Project Unit since 1998 have yielded the results shown on the screen. What started as an experiment has proven itself to be a valuable component of our overall compliance efforts and is now an integral part of our collection and enforcement activity in New Jersey.

FISCAL YEAR	COLLECTIONS	NEW REGISTRATIONS
07/1998-06/1999	\$5,379,425.00	589
07/1999-06/2000	\$5,929,763.00	637
07/2000-03/2001*	\$5,756,508.00	326
TOTAL	\$17,065,696.00	1552

- DATA THROUGH 03/2001

