



# This Week in State Tax (TWIST)

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## New Jersey: Appeals Court Rejects Challenge to Sales Tax Refund Claim Regulations

In two recent decisions, the New Jersey Superior Court addressed challenges to the regulations governing the requirements needed to substantiate sales and use tax refund claims. For instance, the taxpayers objected to the requirement that a taxpayer provide bank statements if payments were made electronically and asserted that the regulatory requirement that refund claims with 25 or more transactions be submitted with a spreadsheet did not conform to modern business practices. The taxpayers were affiliates that filed refund claims with the Division of Taxation for certain sales and use taxes paid on manufacturing equipment, repair parts, and supplies used in the production of chemicals. The Division denied most of the requested refunds because it could not determine that sales tax was actually paid to vendors, or that use tax was accrued and remitted. Part of the issue was that the taxpayer accrued use tax on certain items and then took credits against the accrued tax before it was remitted. The Division could not reconcile the transactions in the refund claim against those for which a “self-help” credit may have been taken. Ultimately, the Division denied most of the refunds. The taxpayer protested, and the matter went to the tax court. The tax court concluded the Division properly denied the refunds, and the taxpayers appealed.

On appeal, the taxpayers challenged the regulations on the basis that they limited the types of proof that could be presented to support a refund claim and were arbitrary and capricious because they unreasonably “restricted taxpayers’ ability to prove that tax was erroneously collected or paid. For example, N.J.A.C. 18:2-5.8(d)(3)(i), states that a sales tax refund claim form “must be” filed with certain “documents, such as invoices, receipts, proof of payment of tax, and exemption certificates. The taxpayers argued that the regulation’s use of the word “must” was unduly restrictive. Similarly, the regulation stated that the Division “will” accept cancelled checks as proof of payment, and the taxpayer argued this limited them to providing cancelled checks. The court rejected the taxpayer’s arguments, noting that the statute was silent as to the documentation requirements for refund claims; therefore, the regulations did not exceed the scope of the statute. Further, the statute empowered the Director of the Division of Taxation to adopt regulations addressing the evidence required. The court further rejected the taxpayers’ arguments that the regulations should be invalidated because they do not comport with modern business practices or promote uniform remedies and procedures for refunds. The regulations, the court found, were flexible and expressly permitted a taxpayer to submit “alternative proof.” A review of the record showed that the refunds at issue were denied because of the insufficiency of the proof provided and the fact that the taxpayers failed to reconcile their use tax accruals to their use tax remittances. Please contact Steve Carozzi with questions on *Solvay Specialty Polymers, LLC v. Director, Division of Taxation*; *Solvay Solexis, Inc. v. Director, Division of Taxation*.

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