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N.J. Bulk Sales Notification Requirements: Recent Changes and Guidance

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For nearly five years now, New Jersey transactional attorneys have been working under a broad application of the New Jersey bulk sales tax law, N.J.S.A. 54:50-38 (Bulk Sales Act). In most cases, compliance is simple. But there are some unusual transactions — including short sales and deeds in lieu of foreclosure, sign-and-close deals, contributions of property to joint ventures and auction sales — where complying with the Bulk Sales Act is not so straightforward.

Originally, the bulk sales tax law dealt only with persons required to collect and

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remit sales tax. N.J.S.A. 54:32B-22(c). In 2007, the Bulk Sales Act was adopted, which expanded the original bulk sales tax law to apply to transactions in which any seller makes a bulk sale. Failure to comply results in the buyer's becoming liable for all state tax obligations of the seller, not just sales tax.

As a result of the 2007 changes in the law, a much broader class of transactions became covered by the notice provisions, and because buyers potentially became liable for all state taxes, the stakes were raised significantly.

The law was scaled back somewhat this past fall, with the enactment of P.L. 2011, Ch. 124, effective Sept. 14, 2011, to exempt a transfer of "a simple dwelling house" or "certain seasonal rental units" if the transferor is an individual, estate or trust under the N.J. Gross Income Tax Act. This exemption is not available to a transferor that is a business entity, such as a corporation, LLC, partnership or sole proprietorship. A "simple dwelling house" may include an attached or

detached dwelling unit, but not more than a two-family building or structure.

Thus far, no regulations have been issued, but we understand the Division of Taxation plans to propose regulations in the near future. For now, guidance on the law can be gleaned from "frequently asked questions" (FAQs) and answers on the division's website, as well as in N.J. Technical Bulletin TB-60R. The FAQs were updated on Jan. 25, 2012, to address the September 2011 amendment and to simplify the guidance.

The Notification and Escrow Process

To satisfy the notice requirement of the Bulk Sales Act:

- The purchaser must submit a fully completed and signed Form C-9600, including valid tax I.D. numbers for the seller and the purchaser, and including a specific date of closing and a copy of the executed contract of sale, clearly showing the sales price and all terms and conditions of the transfer;
- Form C-9600 should be submitted via registered, certified mail or by overnight mail, FedEx or UPS; and
- Form C-9600 and the contract must be received by the Division of Taxation 10 business days prior to the date of closing.

There is no filing fee for the Form C-9600, and the seller need not countersign it. Within 10 business days of receiving the Form C-9600, the division should notify

the purchaser of the amount of the state's tax claim, if any. If an escrow is required, the division will issue an escrow letter (stating the escrow amount) to the purchaser with a copy to the seller. If returns are delinquent, the division will issue a "returns required letter," outlining which returns need to be filed and tax paid to obtain clearance regarding the bulk transfer.

The purchaser or its escrow agent must hold back the escrow amount from the purchase price. If not, the purchaser is liable for the seller's N.J. state tax liabilities.

Form TTD

To assist it in calculating the final amount of the escrow, the Division of Taxation will issue Form TTD to be completed by the seller to disclose information on the income-tax liability of the seller as a result of the bulk sale.

The information submitted on Form TTD is used by the division to adjust the amount of the escrow. Because of this, sellers are incentivized to file quickly a Form TTD to reduce the division's escrow requirement. For example, a seller will obviously want to disclose its high tax basis in the property, the fact that the seller is tax-exempt or possesses substantial net operating losses, or that the transaction is tax-deferred under Internal Revenue Code Section 1031. In fact, the seller may want to include a fully completed and signed Form TTD with the Form C-9600.

Critically, especially with respect to many commercial real estate transactions, in the case of an S corporation, partnership or LLC, all of the shareholders, partners or members must each separately complete Form TTD.

Special Cases

Parties can face some very difficult situations under the Bulk Sales Act. The breadth of the statute alone surprises practitioners. Although in most cases compliance is uncomplicated, some more difficult situations follow.

• *Deed in lieu of foreclosure.* A borrower conveying mortgaged property to its lender

by deed in lieu of foreclosure typically has few or no assets to meet any escrow requirement imposed by the Division of Taxation, and the lender is not paying the borrower anything for the conveyance, except for the release of indebtedness. Nevertheless, the division takes the view that compliance with the Bulk Sales Act is required if the lender wants to be insulated from liability. The division's position is supported by *N.J. Hotel Holdings v. Director, Div. of Taxation*, 15 N.J. Tax 428 (1996). Because a lender that fails to comply can become liable for all of the borrower's state tax liabilities, taking a deed in lieu is highly problematic.

• *Short sales.* Similar to a deed in lieu, a short sale typically yields no or few proceeds to the seller. The recently updated FAQs simply state that "it will be between the purchaser and seller to decide who will provide the additional funds at the time of closing to satisfy the escrow."

• *Sign-and-close deals or quick closings.* The Bulk Sales Act requires a purchaser to submit a signed contract of sale with its C-9600, 10 business days in advance of closing. What if the parties are signing the contract and closing simultaneously, or closing in less than 10 business days? The act has no exception for these deals. The Division of Taxation may be willing to expedite its review, in the case of a quick closing, but the parties cannot rely on it, and there is no room for expedited review in the case of a sign-and-close. Here, the division may be willing to act on a draft contract with a separate signed authorization from seller to release information to the buyer or its counsel. However, if the final contract materially deviates from the draft submitted, the buyer will not be protected.

• *Material amendments.* What happens when a contract is materially amended after it has been submitted to the Division of Taxation with the purchaser's C-9600, and the division has issued its reply? There is no clear guidance, but experience suggests that the division will try to work with the parties and the case worker should be notified as

soon as possible.

• *Flow-through entities.* If the seller is a flow-through entity with a significant number of Schedule K-1 recipients, merely gathering the completed and signed Forms TTD from those parties can be daunting. If income tax is owed by those Schedule K-1 recipients, the division takes that into account in determining the escrow, even though the selling entity otherwise may well not have a direct obligation to pay that tax. Form TTD does not distinguish between partnerships with resident partners and those with nonresident partners (under N.J. law, a partnership with nonresident partners would have likely needed to pay the income tax with respect to those nonresident partners when the partnership filed its return).

• *Contributions of property to joint ventures.* In real estate joint ventures, it is common for one party to contribute real estate to the venture by deeding it to the entity. Is such a contribution of property subject to the Bulk Sales Act, and if so, how can the entity be protected from liability? There is no clear guidance and the safe route is to file a C-9600, treating a contribution agreement (if there is one) as the contract, or (if there is no contribution agreement) treating the signing of the venture agreement and simultaneous deeding of the real estate in the same manner discussed above regarding sign-and-close transactions.

• *Auction sales.* The FAQs suggest that a sheriff's sale free and clear of liens is not subject to the Bulk Sales Act, and it would seem to follow that other court-ordered sales free and clear of liens, such as a sale under section 363 of the Bankruptcy Code, do not require Bulk Sales Act compliance. However, in other cases when a seller's property is auctioned for sale, the Bulk Sales Act applies. To comply, the auction would need to be structured so that the winning bidder enters into a contract and files a C-9600, with the right to escrow proceeds.

The Bulk Sales Act is very broad. Logic may suggest it is not applicable in certain cases, but do not trust your instincts. As stated in the FAQs: when in doubt, file. ■