

**NEW JERSEY DIVISION OF TAXATION
REGULATORY SERVICES BRANCH
TECHNICAL ADVISORY MEMORANDUM**

TAM - 2011- 7

ISSUED: 1-13-11

TAX: GROSS INCOME TAX

TOPIC: CLAIM OF RIGHT REPAYMENT REFUNDS (IRC 1341)

For Federal Income Tax purposes, if a taxpayer must return income paid and already included in income, a deduction for this amount in the year of repayment is allowed under the “claim of right doctrine.” This doctrine states that if a taxpayer is required to restore amounts which previously have been included in income, the taxpayer is permitted a deduction in the year of repayment. The administration of this deduction in the year of repayment is governed by section 1341 of the Internal Revenue Code. This section provides a taxpayer with two alternate methods of calculating a claim of right adjustment. Under section 1341, the taxpayer may either take the deduction in the year of repayment or treat the amount as if the repayment had been excluded in the year the claim of right income was first reported.

The New Jersey Gross Income Tax Act, however, does not contain provisions similar to IRC section 1341.

In *Wigton v. Director*, 12 N.J. Tax 373 (1992), the Tax Court stated that federal and state case law interpreting section 1341 holds that this section does not result in a reopening of the earlier taxable year. The prior year is simply used as a means of determining the least amount of tax due under the section 1341 recalculation. Therefore, for New Jersey Gross Income Tax purposes, New Jersey does not permit taxpayers to file an amended return to recover repaid amounts taxed in prior years since the income was received and used under the “claim of right” doctrine. Also, the New Jersey Legislature did not adopt the IRC section 1341 alternative calculation method allowing a taxpayer to compute tax due in the year of repayment using the original payment year as the basis for calculation instead of the repayment year.

On the Gross Income Tax return, any repayment or deduction may be applied against other income earned in the same category and in the same tax year as the repayment in accordance with N.J.S.A. 54A:5-2. For example, if wages received by the taxpayer in 2010 are repaid back to the employer in 2011, the taxpayer can adjust 2011 year wages by the repayment made during the 2011 tax year. If the offset results in a net loss or negative amount, the taxpayer must report zero income in that category.

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