NOT FOR PUBLICATION WITHOUT APPROVAL OF
THE TAX COURT COMMITTEE ON OPINIONS

MANHEIM NJ INVESTMENTS, INC.,

Plaintiff,

v.

DIRECTOR, DIVISION OF TAXATION,

Defendant.

TAX COURT OF NEW JERSEY
DOCKET NO. 015083-2014

Approved for Publication
In the New Jersey
Tax Court Reports

Decided: February 27, 2017

Marc A. Simonetti for Plaintiff (Eversheds Sutherland (US) LLP, attorneys).

Michael J. Duffy for Defendant (Christopher S. Porrino, Attorney General of New Jersey, attorney).

ANDRESINI, J.T.C.

Plaintiff, Manheim NJ Investments, Inc., filed a motion for partial summary judgment on the issues of: (1) whether N.J.A.C. 18:7-1.15(b)(9) is ultra vires and void; and (2) whether plaintiff is entitled to investment company treatment pursuant to N.J.S.A. 54:10(a)-4(f) and -5(d) for tax years 2006 through 2009. In response to plaintiff's motion, defendant, Director of the Division of Taxation (the "Division"), filed: (1) a cross-motion for partial summary judgment asserting that the Division had statutory authority to promulgate N.J.A.C. 18:7-1.15(b)(9); and (2) an opposition to plaintiff's partial summary judgment motion contending that the issue of plaintiff's qualification as an investment company is not ripe for summary judgment. With regard to the validity of N.J.A.C. 18:7-1.15(b)(9), plaintiff's motion for partial summary judgment is granted and defendant's cross-motion for partial summary judgment is denied. With respect to plaintiff's qualification as an investment company, plaintiff's motion for partial summary judgment is denied.

I. Procedural History and Findings of Fact

The court makes the following findings of fact based on the pleadings, submissions, and oral arguments of the parties pursuant to R. 1:7-4.

A. The Relevant Entities

Plaintiff was incorporated under the laws of Delaware in 2001 and, during the tax years ending December 31, 2005, through December 31, 2009, (the "Relevant Period") had its principal place of business in Atlanta, Georgia. Plaintiff was formed as part of a larger corporate restructuring to hold a limited partnership interest in National Auto Dealer's Exchange, L.P. ("NADE"). NADE, a Delaware limited partnership, was formed to operate an automobile auction business in New Jersey. On December 31, 2001, plaintiff contributed New Jersey assets worth $410,000,000 to NADE in exchange for a ninety-nine percent limited partnership interest. During the Relevant Period, plaintiff did not hold any certificate, license, or other authorization permitting it to engage in corporate activity in New Jersey. Further, plaintiff did not have any employees or own any real or personal property in New Jersey.

During the Relevant Period, plaintiff was taxed as a C corporation for federal income tax purposes and earned income solely from its investment in NADE. Plaintiff held and managed its investment in NADE for its own account and not for others. It did not engage in any other income producing business activities or own any assets other than its limited partnership interest in NADE.

On December 31, 2001, at the same time plaintiff transferred assets in exchange for a limited partnership interest in NADE, ADT Automotive, Inc. contributed assets worth $4,141,236 to NADE in exchange for a one percent general partnership interest. ADT Automotive, Inc. then transferred its interest in NADE to Georgia Auction Services, Inc. ("Georgia Auction"), a Delaware corporation. Georgia Auction was incorporated in 1987 to

carry on the business of acquiring, owning, and operating automobile auction business. After the restructure, plaintiff owned ninety-nine percent of NADE as the limited partner while Georgia Auction held one percent as the general partner. The restructure also resulted in the parent company, Manheim Investments, Inc., owning one hundred percent of Georgia Auction directly, one hundred percent of plaintiff indirectly, and one hundred percent of NADE indirectly during the Relevant Period.

Plaintiff and Georgia Auction's respective rights, obligations, and interest as partners in NADE were defined by a written agreement entitled "Agreement of Limited Partnership of National Auto Dealers Exchange, L.P., a Delaware Limited Partnership" (the "Agreement"). The Agreement prohibited plaintiff, the limited partner, from controlling, managing, directing, operating, acting for, or binding NADE. Additionally, the Agreement granted Georgia Auction the sole power to designate NADE's officers as well as the timing and amount of NADE's partnership distributions. Plaintiff relies on the Agreement as proof that Georgia Auction had full and complete responsibility for the management and control of NADE's affairs. Additionally, plaintiff asserts that it bore no personal liability for NADE's liabilities and obligations.

While defendant admits that the Agreement identifies plaintiff as a limited partner and sets clear limits on plaintiff's ability to control NADE, defendant argues that evidence discovered by the Division during an audit for tax years 2005 through 2008 shows that plaintiff exercised managerial control and, therefore, was integrally related to NADE and should be subject to corporate business tax in New Jersey. In support of its position, defendant points to the following facts: (1) the same six individuals served on the board of directors for both plaintiff and Georgia Auction; (2) the same individuals served as officers of both plaintiff and Georgia Auction; (3) the same individual served as president for both plaintiff and Georgia Auction; (4) plaintiff did not have its own bank account and, instead, participated in a cash management

system with other affiliates; and (5) during the Relevant Period, plaintiff had an intercompany payable of $10,335,973 with no interest charged or expectation of repayment at any specific point in time. Given the Division's findings, defendant contends that the matter is not ripe for summary judgment and discovery is required to determine whether plaintiff, in fact, exercised managerial control over NADE despite the limitations imposed by the Agreement.

B. Procedural History

Plaintiff filed an original CBT-100 electing to be taxed as an investment company pursuant to N.J.S.A. 54:10A-5(d) for the 2005 tax year. Plaintiff later claimed that its tax payments exceeded its reported Corporate Business Tax ("CBT") liability and requested the overpayment to be credited to its 2006 tax return. For tax years 2006 through 2009, plaintiff filed returns without electing to be taxed as an investment company. For the 2006 and 2007 tax years, plaintiff alleged overpayment of CBT and requested a refund for each year to be applied to the subsequent year. For the 2008 and 2009 tax years, plaintiff again alleged overpayment of CBT and requested a refund for each year rather than a credit for each subsequent year.

On or about June 15, 2010, the Division notified plaintiff that it was being audited for CBT purposes for tax years 2005 through 2008. By letter dated February 8, 2011, the Division denied plaintiff's refund claims for the 2008 and 2009 tax years, which plaintiff protested by a letter dated April 25, 2011.

In April 2011[1], plaintiff filed amended CBT returns for tax years 2005 through 2007 asserting that it was not was not subject to CBT based on the trial court's holding in BIS LP, Inc. v. Director, Div. of Taxation, 25 N.J. Tax 88 (Tax 2009).[2] Plaintiff asserted that it was not doing business in New Jersey and, therefore, was entitled to the refunds of CBT erroneously paid for

[1] Plaintiff did not indicate the exact filing dates of the amended CBT returns for tax years 2005 through 2007; however, defendant did not raise the issue of whether the amended returns were timely filed.
[2] The case was subsequently affirmed. 26 N.J. Tax 489 (App. Div. 2011).

the 2005, 2006, and 2007 tax years. By letter dated June 16, 2011, the Division denied refund claims for the 2005, 2006, and 2007 tax years, explaining that BIS, supra, was on appeal and until the court reaches a final determination the Division will maintain its position that a limited partnership interest in a partnership doing business in New Jersey is enough to subject a taxpayer to New Jersey CBT.

Subsequently, the Division issued an audit report dated July 16, 2011, concluding that plaintiff qualified as an investment company for 2005, but denied investment company treatment for 2006, 2007, and 2008 tax years as a result of N.J.A.C. 18:7-1.15(b)(9), which expressly prohibits investment company treatment for any company involved in "direct investment in a non-publicly-traded pass-through entity, if that entity would not satisfy the definition of investment company if it had been organized as a corporation."

The Division issued a Notice of Assessment Related to Final Audit Determination on September 13, 2011, assessing additional CBT, penalty, and interest for the 2005 tax year, and denying a CBT refund claim for the 2008 tax year. Plaintiff protested the Notice of Assessment by a letter dated October 13, 2011. Both parties participated in an administrative conference on January 30, 2014. The Division issued a Final Determination dated August 1, 2014, upholding its Notice of Assessment. In its determination, the Division opined that because plaintiff took an active part in the control of NADE it was integrally related to the New Jersey partnership. Thus, plaintiff had a nexus to New Jersey and was subject to CBT.

On October 22, 2014, plaintiff filed a complaint in the Tax Court of New Jersey challenging the Final Determination. On May 13, 2016, plaintiff filed a motion for partial summary judgment pursuant to R. 4:46-2(c) asserting that plaintiff is entitled to preferential treatment as an investment company under N.J.S.A. 54:10A-5(d) if it is subject to CBT during the tax years 2006 through 2009. Specifically, plaintiff argues that: (1) N.J.A.C. 18:7-1.15(b)(9)

is ultra vires and void because it improperly narrows the statutory definition of an investment company; and (2) plaintiff satisfies every statutory requirement for investment company treatment under N.J.S.A. 54:10A-5(d).

Defendant responded on June 28, 2016, by filing a cross-motion for partial summary judgment and an opposition to plaintiff's motion for partial summary judgment. Defendant concedes that with regard to the validity of N.J.A.C. 18:7-1.15(b)(9) there is no dispute of material fact and requests that summary judgment is granted in its favor because the same was properly enacted to end "proliferation in the use of flow through entities" and "limit tax planning through aggressive reorganization." In opposition to plaintiff's motion concerning treatment of plaintiff as an investment company, defendant argues that the issue is not ripe for summary judgment. More specifically, defendant maintains there is a genuine issue of material fact as to the degree of plaintiff's managerial control over NADE, which is fundamental to determining whether its interest as a limited partner constitutes a permissive "other security" under N.J.S.A. 54:10-4(f).

An oral argument concerning the motion was heard on Friday, July 8, 2016. During the argument, the court requested additional briefings that address whether the Acting Deputy Director was authorized to adopt the amendments to N.J.A.C. 18:7-1.15 and whether the Division relied on any studies or reports in support of its finding regarding "the proliferation in the use of flow though entities." Both parties declined to hold an additional oral argument on the said issues.

II. Standard for Summary Judgment

The New Jersey Court Rules permit either party to move for summary judgment before the case is tried if, from the pleadings, depositions, answers, admissions, and affidavits, it appears that "there is no genuine issue as to any material fact challenged and that the moving

party is entitled to judgment or order as a matter of law." R. 4:46-2(c). The moving party has the "burden to exclude any reasonable doubt as to the existence of any genuine issue of material fact" regarding the claims asserted. Judson v. Peoples Bank & Trust Co. of Westfield, 17 N.J. 67, 74 (1954) (citations omitted).

A genuine issue of material fact exists "only if, considering the burden of persuasion at trial, the evidence submitted by the parties, on the motion, together with all legitimate inferences therefrom favoring the non-moving party, would require submission of the issue to the trier of fact." R. 4:46-2(c). Disputed issues of insignificant nature cannot overcome a motion for summary judgment. Brill v. Guardian Life Ins. Co. of America, 142 N.J. 520, 529 (1995). Moreover, "[b]are conclusions in the pleadings, without factual support in tendered affidavits, will not defeat a meritorious application for summary judgment." U.S. Pipe & Foundry Co. v. Am. Arbitration Ass'n, 67 N.J. Super. 384, 399-400 (App. Div. 1961) (citation omitted).

A non-moving party must "make an affirmative demonstration, where the means are at hand to do so, that the facts are not as the movant alleges." Spiotta v. William H. Wilson, Inc., 72 N.J. Super. 572, 581 (App. Div.), certif. denied, 37 N.J. 229 (1962). Accordingly, the defendant in this case may defeat the motion by demonstrating that the evidence relied upon by the plaintiff, considered in light of the applicable burden of proof, raises sufficient credibility issues to permit a rational fact-finder to resolve the alleged disputed issue in favor of the defendant. D'Amato v. D'Amato, 305 N.J. Super. 109, 114 (App. Div. 1997).

III. Conclusions of Law

A. N.J.A.C. 18:7-1.15(b)(9) is ultra vires and void

The parties agree that there is no genuine issue as to any material fact concerning the adoption of N.J.A.C. 18:7-1.15(b)(9) and, therefore, the validity of the regulation can be decided as a matter of law. Thus, summary judgment is appropriate. Plaintiff asserts that N.J.A.C. 18:7-

1.15(b)(9) is ultra vires and void because it contravenes legislative intent behind N.J.S.A. 54:10A-5(d) and -4(f). Defendant argues that N.J.S.A. 54:10A-27 and N.J.S.A. 54:10A-10(a) grant the Division statutory authority to promulgate such restrictive regulations.

In 1945 the Legislature enacted the Corporation Business Tax Act, N.J.S.A. 54:10A-1 to -41 (the "Act"), which imposes on a taxpayer:

> [A]n annual franchise tax for each year . . . for the privilege of having or exercising its corporate franchise in this State, or for the privilege of deriving receipts from sources within this State, or for the privilege of engaging in contacts within this State, or for the privilege of doing business, employing or owning capital or property, or maintaining an office, in this State.
> . . . .
> A taxpayer's exercise of its franchise in this State is subject to taxation in this State if the taxpayer's business activity in this State is sufficient to give this State jurisdiction to impose the tax under the Constitution and statutes of the United States.
>
> [N.J.S.A. 54:10A-2.]

At its inception, the Act granted special treatment to regulated investment companies. L. 1945, c. 162, § 5. In 1947, the Act was amended to allow special treatment to all investment companies. L. 1947, c. 50, § 4(f). During the Relevant Period, the statutory provision authorizing favorable treatment for investment companies stated:

> [T]he franchise tax to be annually assessed to and paid by any investment company or real estate investment trust, which has elected to report as such and has filed its return in the form and within the time provided in this act and the rules and regulations promulgated in connection therewith, shall, in the case of an investment company, be measured by 40% of its entire net income and 40%[3] of its entire net worth . . . .[4]

[3] The investment company tax base was increased from twenty-five percent to forty percent in 2002. L. 2002, c. 40, § 3.

[4] Although N.J.S.A. 54:10A-5(d) requires that an investment company electing to report as such file its return in the "form and within the time provided" by the Act and the related rules and regulations, plaintiff's decision not to elect investment company treatment pursuant on its original CBT-100s for tax years 2006 through 2009 and the amended returns for 2006 and 2007 tax years does not bar its current claim for investment company treatment. In appealing a Division's audit determination, "the business decision rule does not operate to bind plaintiff to its original filing . . . and the taxpayer must not be precluded from advocating and proving an alternative basis of tax liability before the

[N.J.S.A. 54:10A-5(d).]

In 1947, at the recommendation of the Commission on State Tax Policy, the Legislature provided a comprehensive definition of "investment company" to aid the application of N.J.S.A. 54:10A-5(d). During the tax years in question, the Act defined an "investment company" as:

> [A]ny corporation whose business during the period covered by its report consisted, to the extent of at least 90% thereof of holding, investing and reinvesting in stocks, bonds, notes, mortgages, debentures, patents, patent rights and other securities for its own account, but this shall not include any corporation which: (1) is a merchant or a dealer of stocks, bonds and other securities, regularly engaged in buying the same and selling the same to customers; or (2) had less than 90% of its average gross assets in New Jersey, at cost, invested in stocks, bonds, debentures, mortgages, notes, patents, patent rights or other securities or consisting of cash on deposit during the period covered by its report; or (3) is a banking corporation, a savings institution, or a financial business corporation as defined in the Corporation Business Tax Act.
> [N.J.S.A. 54:10A-4(f).]

The Act also granted the Division a statutory right to "prescribe and issue such rules and regulations, not inconsistent herewith, for the interpretation and application of provisions of this act, as he may deem necessary." N.J.S.A. 54:10A-27. Prior to 1979, the Division exercised its statutory power to promulgate its own definition of "investment company," which included "qualified investment activities" and "qualified investment assets" that mirrored the list of permitted investments set forth in N.J.S.A. 54:10A-4(f). Further, in N.J.A.C. 18:7-1.15(b), the Division identified specific assets and activities that are not "qualified investment activities" or

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Tax Court on appeal." Chemical New Jersey Holdings, Inc. v. Director, New Jersey Div. of Taxation, 22 N.J.Tax 606, 612-613 (App. Div. 2004). Furthermore, plaintiff's claim is not barred by the four-year statute of limitation for refund claims set forth in N.J.A.C. 18:7-13.8. When plaintiff challenges the Division's determination of the proper filing status "[t]he issue . . . is not whether plaintiff may re-file and seek a refund, but whether the Director assessed the appropriate tax." Chemical Holdings, supra, 22 N.J. Tax at 614-116.

"qualified investment assets." In 2005, the Division defined "investment company" as any company:

> 1. Whose business for the period covered by its return consisted to the extent of at least 90 percent of "qualified investment activities" which are: investing or reinvesting in stocks, bonds, notes, mortgages, debentures, patents, patent rights, and other securities or the holding thereof after investing or reinvesting therein for its own account. As used in this rule, "qualified investment assets" are stocks, bonds, notes, mortgages, debentures, patents, patent rights, and other securities and cash on deposit;
> 2. Which had for the period covered by the return 90 percent or more of its average gross assets in New Jersey, at cost, invested in "qualified investment assets" referred to in (a)1 above;
> 3. Which meets the numerical tests in (f) below;
> 4. Which is not a banking corporation as defined by the Act;
> 5. Which is not a financial business corporation as defined by the act; and
> 6. Which is not a merchant or dealer in stocks, bonds, or other securities, and which is regularly engaged in buying and selling such securities to customers.
> [N.J.A.C. 18:7-1.15(a).]

On June 27, 2006, the Acting Deputy Director amended N.J.A.C. 18:7-1.15(a)(1) to include "publicly traded limited partnership or limited liability company interests" in the list of "qualified investment assets." 38 N.J.R. 3183(a) (August 7, 2006). Contemporaneously, the Acting Deputy Director amended N.J.A.C. 18:7-1.15(b) to exclude investments in certain pass though entities from "qualified investment activities" and "qualified investment assets," thereby narrowing the statutory definition of "investment company" under N.J.S.A. 54:10A-4(f). 38 N.J.R. 3183(a) (August 7, 2006). The amendments to N.J.A.C. 18:7-1.15(a) and (b) were a response to "proliferation in the use of flow through entities" and were intended "to limit tax planning through abusive reorganization making clear that such assets are outside the scope of qualifying assets of investment companies." 38 N.J.R. 1558 (a) (April 3, 2006).

These amendments to N.J.A.C. 18:7-1.15(a) and (b) were proposed on April 3, 2006, and were adopted on June 27, 2006, by the Acting Deputy Director, who had "full power and

authority to do and perform all and every act and thing whatsoever necessary and proper to be done by the Director, Division of Taxation…" pursuant to N.J.S.A. 54:1-11. The amendments were filed with the Office of Administrative Law on June 28, 2006 and were subsequently published in the New Jersey Register to become effective as of August 7, 2006.[5] 38 N.J.R. 3183(a) (August 7, 2006). During the Relevant Period, the amendment at issue, N.J.A.C. 18:7-1.15(b)(9), read:

> "Qualified investment activities" and "qualified investment assets" do not include the following specific assets or activities. The receipts, direct and indirect expenses and assets connected with the following will not be included in the numerator of any test:
> ….
> 9. The direct investment in a non-publicly-traded pass-through entity, if that entity would not satisfy the definition of investment company if it had been organized as a corporation.
>
> [N.J.A.C. 18:7-1.15(b).]

Plaintiff acknowledges that the Acting Deputy Director was properly deputized to perform all acts normally done by the Director of the Division and the Division has the authority to promulgate rules and regulations to interpret and apply the provisions of the Act. Nevertheless, plaintiff argues that the Division does not have statutory permission to narrow the definition of "investment company" set forth by N.J.S.A. 54:10A-4(f) by means of a regulation. Furthermore, plaintiff asserts that N.J.A.C. 18:7-1.15(b)(9) contravenes the legislative intent behind N.J.S.A. 54:10A-4(f) and -5(d) and the generally accepted meaning of "other securities" in New Jersey, which the courts have interpreted to include limited partnership interest. Plaintiff also maintains that N.J.A.C. 18:7-1.15(b)(9) arbitrarily disqualifies a class of taxpayers from being taxed as investment companies under N.J.S.A. 54:10A-5(d).

[5] The effective date of the amendment to N.J.A.C. 18:7-1.15(b) concerns the court. Because the change is effective as of August 7, 2006, rather than a particular tax year, similarly situated taxpayers are treated differently solely because of their tax return filing dates. This could result in unfair treatment of otherwise similarly situated taxpayers. However, this issue has not been raised by plaintiff in this motion and the court is not making any finding in this regard.

In opposition, defendant argues that N.J.A.C. 18:7-1.15(b)(9) cannot contravene N.J.S.A. 54:10A-5(d) because the statute does not explicitly address pass-through entities. Rather, "other securities" is the type of vague statutory language a state agency is authorized by N.J.S.A. 54:10A-27 to interpret by way of rulemaking and its interpretation should be granted substantial deference by the court. Moreover, defendant contends that N.J.A.C. 18:7-1.15(b)(9) supports the legislative purpose behind N.J.S.A. 54:10-4(f) by further clarifying which investment assets and activities should qualify for investment company treatment.

In addition to N.J.S.A. 54:10A-27, defendant points to N.J.S.A. 54:10A-10 as a source of authority to promulgate the N.J.A.C. 18:7-1.15(b)(9). N.J.S.A. 54:10A-10 grants the Division broad authority to address tax evasion. The statute provides:

> Whenever it shall appear to the director that any taxpayer fails to maintain its records in accordance with sound accounting principles or conducts its business or maintains its records in such manner as either directly or indirectly to distort its true entire net income or its true entire net worth under this act or the proportion thereof properly allocable to this State, or whenever any taxpayer maintains a place of business outside this State, or whenever any agreement, understanding or arrangement exists between a taxpayer and any other corporation or any person or firm, for the purpose of evading tax under this act, or whereby the activity, business, receipts, expenses, assets, liabilities, income or net worth of the taxpayer are improperly or inaccurately reflected, the director is authorized and empowered, in the director's discretion and in such manner as the director may determine, to adjust and redetermine such items, and to adjust items of gross receipts, tangible or intangible property and payrolls within and without the State and the allocation of entire net income or entire net worth or to make any other adjustments in any tax report or tax returns as may be necessary to make a fair and reasonable determination of the amount of tax payable under this act.
>
> [N.J.S.A. 54:10A-10 (2002).]

Defendant concedes in its supplemental brief dated August 31, 2016, that the Division cannot certify as to any particular study or report that was relied upon in adopting N.J.A.C. 18:7-

1.15(b)(9). Nevertheless, defendant asserts that the Division had a rational basis for amending N.J.A.C. 18:7-1.15 and reasonably tailored the amendment to limit tax planning and abusive reorganization. Defendant cites Statements to Assembly No. 3045 (Dec. 11, 2000) and No. 2501 (June 6, 2002) to illustrate the Division's concern that the use of pass-through entities and proliferating loopholes has allowed companies to avoid taxation of income derived from New Jersey activities. However, despite these statements, the Legislature has not amended the statutory definition of "investment company." In fact, when the Business Tax Reform Act (the "BTRA") was introduced to revise and update the CBT on June 6, 2002, the only changes made by the Legislature relevant to investment companies were: (1) an increase in the investment company tax base from twenty-five percent of entire net income to forty percent and (2) the exclusion of "saving institutions" from investment company treatment. L. 2002, c. 40, §3 and §6.

In further support of its argument, defendant presents observations from the Division's Chief of Office Audit and statements made by an attorney at a tax seminar in 2006 on the rise in businesses formed as pass through entities. Additionally, defendant cites both a Congressional Budget Office report, which alleges significant loss of government revenue due to special tax rules for S corporations and limited liability companies, and an academic journal article, which discusses the proliferation of pass-through entities and the associated tax savings. The conclusory materials offered by defendant simply point to the fact that pass-through entities have grown in popularity. Defendant fails to provide evidence that N.J.A.C. 18:7-1.15(b)(9) supports the legislative intent behind N.J.S.A. 54:10A-4(f) and 5(d).

New Jersey case law allows the Legislature to delegate to an administrative agency the authority to promulgate rules and regulations that interpret and implement statutes. T.H. v. Div. of Developmental Disabilities, 189 N.J. 478, 490 (2007). Such regulations are necessary to assist in the application of statutes to achieve the legislative purpose. Regent Corp. of Union, Inc. v.

Director, Div. of Taxation, 27 N.J. Tax 577, 598 (Tax 2014). However, an administrative agency may not undermine legislative intent by giving a statute "greater effect than its language permits" under the guise of interpretation. GE Solid State, Inc., supra, 132 N.J. at 306 (1993).

When an administrative agency is delegated the authority to enforce a statute, its interpretation receives substantial deference. Ibid. Nonetheless, an agency regulation will fail "if it is proved to be arbitrary and capricious, plainly transgresses the statute it purports to effectuate, or alters the terms of the statute and frustrates the policy embodied in it." In re Adopted Amendments to N.J.A.C. 7:7A-2.4, 365 N.J. Super. 255, 265 (App. Div. 2003). The party challenging the regulation has the burden of proving the regulation is invalid. New Jersey State League of Municipalities v. Dep't of Cmty. Affairs, 158 N.J. 211, 222 (1999).

When reviewing a claim that a regulation is arbitrary and at odds with the very statute it is designed to interpret, the court must determine the Legislature's intent with respect to the applicable provision. In re Agricultural, Aquacultural, and Horticultural Water Usage Certification Rules, N.J.A.C. 7:20A-1.1 et seq., 410 N.J. Super. 209, 224 (App. Div. 2009). The sole guidepost for courts interpreting tax statutes is the legislative intent. Public Serv. Elec.& Gas Co. v. Township of Woodbridge, 73 N.J. 474, 478 (1977). The best way to establish the Legislature's intent "is to give to the words used by the Legislature their generally accepted meaning, unless another or different meaning is expressly indicated." Ibid. (internal citation omitted).

When the Legislature enacted the CBT in 1945, it purposefully allowed preferential tax treatment of investment companies. N.J.S.A. 54:10A-5(d). At the outset, the Legislature provided a comprehensive definition of "investment company." N.J.S.A. 54:10A-4(f) expressly lists the assets in which a company may invest to qualify for investment company treatment and the types of business that are not eligible for preferential treatment. The Act has been amended

several times since 1945, yet despite any alleged concern over the proliferation of flow-through entities, the Legislature has not amended N.J.S.A. 54:10A-4(f) to exclude such entities from investment company treatment. When the Legislature enacted the BTRA in 2002, N.J.S.A. 54:10A-4(f) was amended to exclude saving institutions from investment company treatment. Clearly, the Legislature considered the type of businesses that should not receive preferential investment company treatment and elected not to exclude flow-through entities.

While N.J.S.A. 54:10A-27 provides the Division with a right to issue rules and regulations for the interpretation and application of the Act, the Division may not exceed its authority by promulgating regulations that are inconsistent with legislative intent behind N.J.S.A. 54:10A-4(f) and -5(d). Looking at the language of N.J.S.A. 54:10A-4(f), the court determines that the Legislature intended to provide an all-inclusive definition of "investment company" to be used in conjunction with N.J.S.A. 54:10A-5(d). In drafting the definition, the Legislature specified the type of entities that companies may and may not invest in to receive investment company treatment. The Legislature deliberately allowed companies to invest and reinvest in "other securities."

When the New Jersey Legislature defined "security" in the Uniform Securities Law, it unequivocally followed the definition proffered by the Federal Securities Act of 1933. Conroy v. Schultz, 80 N.J. Super. 443, 450 (Ch. Div. 1963). Consequently, when determining whether an instrument is a "security," New Jersey courts have looked to the United States Supreme Court for guidance. Id. at 451. (holding that participation units in limited partnerships were securities for purposes of the New Jersey Uniform Securities law by applying the investment contract analysis set forth in S.E.C. v. W.J. Howey Co., 328 U.S. 293, 301, 66 S. Ct. 1100, 90 L. Ed. 1244 (1946)); BIS, supra, 25 N.J. Tax at 97 (applying the Howey test to determine that a ninety-nine percent limited partnership interest is a security). The United States Supreme Court applies an

investment contract analysis to determine whether an investment contract is a security. The test is whether the company has made an "investment of money in a common enterprise with profits to come solely from the efforts of others." S.E.C. v. W.J. Howey Co., 328 U.S. 293, 301, 66 S. Ct. 1100, 90 L. Ed. 1244 (1946). Further, "[i]n applying the investment contract analysis, courts look to the degree of managerial control exercised by the limited partner." BIS, supra, 25 N.J. Tax at 96.

This court applied the investment contract analysis in BIS, supra. Similar to the plaintiff in this case, BIS was a foreign corporation and a limited partner with a ninety-nine present interest in a New Jersey limited partnership, while the general partner retained one percent interest. Id. at 92. BIS and the general partner entered into a partnership agreement that provided that the limited partner "shall not have either the obligation or the right to take part, directly or indirectly, in the active management" of the partnership, "perform any act in the name of or on [its] behalf," or "have a voice in or take part in [its] business affairs or business operations." Ibid. The limited partner elected to be taxed as an investment company, but was disallowed the election by the Division. The Tax Court reversed that determination. The court held that BIS' interest in the partnership was an investment in a common enterprise with profits to come solely from the efforts of others. Id. at 97. Thus, BIS' limited partnership interest in the partnership was an investment contract to be considered an "other security" prior to the 2006 amendment to N.J.A.C. 18:7-1.15. Ibid. [6]

Pursuant to Conroy, supra, and BIS, supra, the generally accepted meaning of security includes interest in a pass-through entity when the limited partner does not exercise control over

[6] With respect to N.J.A.C. 18:7-1.15(b)(9), the issue addressed by the Tax Court in BIS, supra, was whether the same can be applied retroactively. Since the court found that amendments to regulations must only be applied prospectively, the validity of N.J.A.C. 18:7-1.15(b)(9) was irrelevant to the matter and, thus, not addressed. BIS, supra, 25 N.J. Tax at 100.

the partnership. Consequently, such a partnership interest would qualify as an "other security" within the scope of N.J.S.A. 54:10A-4(f). The Division's exclusion of "direct investment in non-publicly traded pass-through entity, if that entity would not satisfy the definition of investment company if it had been organized as a corporation," from its definition of qualified investment activities and assets, contravenes the generally accepted meaning of "security" and the legislative intent behind N.J.S.A. 54:10A-4(f). N.J.S.A. 54:10A-27 and its interpretive case law unquestionably dictate that the Division may not issue a regulation that is inconsistent with the statute it seeks to interpret.

Furthermore, the Legislature did not vest the Division with any authority to narrow or otherwise alter the Act's comprehensive definition of an "investment company." The Division claims that it has authority to amend N.J.A.C. 18:7-1.15 pursuant to N.J.S.A. 54:10A-10(a) in addition to N.J.S.A. 54:10A-27. However, the Division's reliance on N.J.S.A. 54:10A-10(a) is misplaced. This section of the Act permits the Division to make adjustments and redeterminations to a taxpayer's tax return if the taxpayer's information is improperly or inaccurately reflected in order to prevent tax evasion. Here, there is no claim of distortion or improper information reported on plaintiff's tax returns. Rather, plaintiff is merely asserting that its tax liability should be calculated based on N.J.S.A. 54:10A-5(d) because it meets all the requirements for investment company treatment set forth by the Legislature in N.J.S.A. 54:10A-4(f).

Plaintiff is correct in noting that adjustments due to improperly reported tax information must be made on taxpayer-by-taxpayer basis. Under N.J.S.A. 54:10A-10(a), the Division would have to first determine if a particular taxpayer has distorted its tax information before making any adjustments or redeterminations. N.J.S.A. 54:10A-10(a), therefore, does not grant the Division a far-reaching authority to issue regulations that exclude an entire class of taxpayers

from receiving preferential treatment pursuant to N.J.S.A. 54:10A-4(f) and 5(d) as it has done in N.J.A.C. 18:7-1.15(b)(9).

Lastly, defendant purports that the Division had a rational basis in promulgating the Amendment and reasonably tailored it to limit abusive reorganization. However, the sole controlling factor in determining whether a regulation is valid, especially with taxation statutes, is legislative intent. The Division cannot substitute its observations and opinion for legislative intent. Plaintiff correctly states that the decision to prohibit companies with direct investments in pass-through entities from qualifying as investment companies is a policy decision to be decided exclusively by the Legislature. N.J. Coalition of Health Care Prof'ls, Inc. v. Department of Banking & Ins., Div. of Ins., 323 N.J. Super 207, 269 (App. Div. 1999) ("Under our system of government, these policy choices are made by the Legislature . . . ."); White v. N. Bergen Twp., 77 N.J. 538, 554 (1978) ("It goes without saying that the wisdom, good sense, policy, and prudence (or otherwise) of a statute are matters within the province of the Legislature."); In re Agric., Aquacultural, & Horticultural Water Usage Certification Rules, 410 N.J. Super. 209, 230 (App. Div. 2009).

Accordingly, the court finds that the Division exceeded the authority granted by N.J.S.A. 54:10A-27 when it amended N.J.A.C. 18:7-1.15 to exclude investment in certain pass-through entities. Plaintiff's motion for partial summary judgment is granted and defendant's cross-motion for partial summary judgment is denied on the issue of whether N.J.A.C. 18:7-1.15(b)(9) is ultra vires and void.

B. Investment Company Treatment

The second issue raised by plaintiff's motion for summary judgment is whether plaintiff qualifies as an investment company. The statutory definition allows investment company treatment to "any corporation whose business during the period covered by its report consisted,

to the extent of at least 90% thereof of holding, investing and reinvesting in stocks, bonds, notes, mortgages, debentures, patents, patent rights and other securities for its own account." N.J.S.A. 54:10A-4(f). The parties disagree as to whether plaintiff's ninety-nine percent interest as a limited partner in NADE qualifies as an "other security." Although the definition of "other security" is a question of law, the question of whether a partnership interest is a security rests on a factual finding that the limited partner did not exercise managerial control over the partnership. BIS, supra, 25 N.J. Tax at 96 (concluding that "[i]n applying the investment contract analysis, courts look to the degree of managerial control exercised by the limited partner").

In this case, plaintiff asserts that it was a limited partner and was, therefore, a passive investor for the purpose of N.J.S.A. 54:10A-5(d) without any control over the partnership's operation or decisions. Plaintiff relies on the Agreement and the affidavit of Mary Vickers as proof that plaintiff could not and did not exercise managerial control over NADE's business during tax years 2005 through 2009 and that Georgia Auction was the general partner solely responsible for the management and operation of NADE. In its brief, plaintiff relies heavily on BIS, supra, in support of its position, stating that the court did not have trouble concluding that the limited partner's interest in the partnership was a security for the purposes of N.J.S.A. 54: 10A-4(f).

Defendant, on the other hand, alleges that the plaintiff did, in fact, exercise managerial control of NADE, and urges the court to deny plaintiff's motion for summary judgment. Defendant alleges that the overall corporate reorganization calls into question whether plaintiff had control over NADE. During the tax years 2005 through 2009, Manheim Investments, Inc. directly owned one hundred percent of Georgia Auction and indirectly owned one hundred percent of both plaintiff and NADE. Additionally, defendant claims that the same individuals

had virtual control over all three entities. In support of its argument, defendant presents a certification of the Division's auditor, who found that:

> The officers of the limited partner and general partners [sic] are all the same with the exception of [officer] who is only an officer of the limited partner . . . the fact that there is a substantial overlapping between the officers of the general partner and the officers of [plaintiff], indicates that it is not distinguishable who the officers are acting on behalf of, the general or limited partner, when making decisions regarding the management and control of the partnership.
>
> In addition, the taxpayer was asked to name all the officers of the limited or general partner of NADE that have authority to act on behalf of NADE (make decisions, transact business, sign contracts, enter into agreement etc.) The taxpayer's list included [officers], all of whom are officers of both the general and limited partners . . . This is another indication that the limited partner participates in the making of decisions regarding the management and control of the partnership.
>
> [Neve Cert.]

Plaintiff counters that the auditor and conferee found plaintiff controlled NADE simply because the two entities shared officers and directors, and did not provide any evidence suggesting that plaintiff actually exercised control over NADE. Plaintiff also argues that the auditor and conferee focused on whether plaintiff and NADE engaged in a unitary relationship, which, though relevant to whether plaintiff had a nexus with New Jersey, is not relevant to the investment company analysis.

Based on investment contract analysis used by the courts in Conroy, supra, and BIS, supra, the court determines that it is material to ascertain whether plaintiff exercised control over NADE in order to discern if plaintiff's alleged passive partnership interest is an "other security," which would qualify plaintiff as an investment company. Plaintiff uses BIS, supra, to suggest that a partnership agreement between a limited and a general partnership is sufficient proof to show a limited partner's lack of control. The court is not convinced. While there are similarities

between BIS and the case at bar, plaintiff ignores substantial factual differences between these cases that relate to the limited partner's exercise of control over the partnership. For instance, BIS did not have a substantial overlap of directors and officers with the general partner. Here, however, plaintiff shared all officers and directors with Georgia Auction during the 2005 through 2009 tax years.

Applying the summary judgement standard discussed above, the court finds that the issue of whether plaintiff qualifies for treatment as an investment company for the purpose of the CBT is not ripe for summary judgment. Defendant has shown that the facts are not as the plaintiff alleges by presenting the results of the Divisions audit, which found that there was a substantial overlap of officers and directors of the general and limited partners. A rational fact-finder looking at this information in the light most favorable to the defendant may find that plaintiff's officers and directors did, in fact, exercise control over NADE, and resolve the disputed issue in favor of a defendant. Furthermore, an examination of the facts in this case may lead a fact-finder to find that plaintiff has a constitutional presence in New Jersey that would subject plaintiff to CBT.

Lastly, plaintiff points out that the Division allowed investment company treatment for the 2005 tax year because all of the requirements set forth in N.J.S.A. 54:10A-4(f) and N.J.A.C. 18:7-1.15 were met. Plaintiff alleges that the facts related to its investment in NADE did not change from 2005 to 2006. The only change between 2005 and 2006 was that the Division promulgated N.J.A.C. 18:7-1.15(b)(9) to restrict investment in pass-through entities. Nonetheless, defendant is not barred from taking a position opposing the auditor. New Jersey case law dictates that "the application of principles of estoppel are particularly inappropriate where the collection of taxes by a public body is involved, except in unusual

circumstances." New Jersey Tpk. Auth. v. Township of Washington, 137 N.J. Super. 543, 552 (App. Div. 1975), aff'd o.b., 73 N.J. 180 (1977).

IV. Conclusion

For the reasons stated above, plaintiff's motion for partial summary judgment with regard to the validity of N.J.A.C. 18:7-1.15(b)(9) is granted and defendant's cross-motion for partial summary judgment is denied. Plaintiff's motion for partial summary judgment with respect to plaintiff's qualification as an investment company is denied.