

**To: New Jersey Law Revision Commission**  
**From: James Finnegan, Legislative Law Clerk**  
**Re: Definition of “Misrepresentation” as used in N.J.S. 54A:9-4 (*Malhotra v. Dir., Div. of Tax’n*, 32 N.J. Tax 443 (N.J. Tax 2021))**  
**Date: July 11, 2022**

## MEMORANDUM

### Project Summary

When a New Jersey taxpayer receives an erroneous refund, the refund is considered an underpayment of the tax due.<sup>1</sup> The Division of Taxation (the “Division”) is entitled to issue an assessment for the deficiency arising out of the erroneous refund.<sup>2</sup> The Division, pursuant to N.J.S. 54A:9-4, must make such a deficiency assessment within three years from the issuance of the erroneous refund.<sup>3</sup> The statute, however, extends this time period to five years from the issuance of a refund where “it appears that any part of the refund was induced by fraud or misrepresentation of a material fact.”<sup>4</sup>

In *Malhotra v. Dir., Div. of Tax’n*, the Tax Court considered the meaning of the term “misrepresentation” as used in N.J.S. 54A:9-4.<sup>5</sup> The plaintiffs in that case were taxpayers who had immigrated to the United States and made a mistake in filing their first tax return in America.<sup>6</sup> Although both sides agreed on the innocence of the mistake, the Division argued that even innocent mistakes constitute misrepresentation and therefore trigger the five-year statute of limitations.<sup>7</sup>

N.J.S. 54A:9-4 does not define the term misrepresentation.<sup>8</sup> Additionally, neither the statute nor its legislative history provides guidance about the level of intent needed to satisfy the misrepresentation standard.<sup>9</sup> Relying on extrinsic evidence, the *Malhotra* Court determined that to invoke the five-year statute of limitations, “a misrepresentation of material fact must be more than an innocent mistake.”<sup>10</sup>

### Statute Considered

N.J.S. 54A:9-4, entitled “Limitations on assessment” states, in relevant part:

(c) Exceptions.

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<sup>1</sup> N.J. STAT. ANN. § 54A:9-4 (West 2022).

<sup>2</sup> *Id.*

<sup>3</sup> *Id.*

<sup>4</sup> *Id.*

<sup>5</sup> *Malhotra v. Dir., Div. of Tax’n*, 32 N.J. Tax 443 (N.J. Tax 2021).

<sup>6</sup> *Id.* at 454.

<sup>7</sup> *Id.*

<sup>8</sup> *Id.*

<sup>9</sup> *Id.*

<sup>10</sup> *Id.* at 459.

(4) Recovery of erroneous refund. An erroneous refund shall be considered an underpayment of tax on the date made, and an assessment of a deficiency arising out of an erroneous refund may be made at any time within 3 years from the making of the refund, except that the assessment may be made within 5 years from the making of the refund if it appears that any part of the refund was induced by fraud or misrepresentation of a material fact.<sup>11</sup>

### **Background**

When Punish and Indu Malhotra (“Taxpayers”) filed their New Jersey state income tax return for the 2013 tax year, they erroneously reported \$5,522 of New Jersey income tax withholding, the amount of their New York State income tax withholding.<sup>12</sup> The 2013 tax year was the first year that the Taxpayers were required to file a return following their 2012 immigration to the United States.<sup>13</sup> Taxpayers also claimed a credit of \$3,751 for taxes paid to New York.<sup>14</sup> These credits resulted in the New Jersey Division of Taxation issuing a refund of \$5,203 on March 11, 2014.<sup>15</sup> The Director of Taxation (the “Director”) later reviewed the return, corrected the erroneous withholding listed and, on May 9, 2018, issued a billing notice in the amount of \$5,706.28, covering the underpayment resulting from the erroneous refund along with penalty and interest charges.<sup>16</sup> The May 9, 2018, deficiency notice was sent more than four years after the issuance of the erroneous refund, thus falling outside the standard three-year statute of limitations.

On June 3, 2018, Taxpayers filed a complaint disputing the set-off of their 2017 tax year refund on grounds that the assessed interest and penalty amounts were exorbitant.<sup>17</sup> The Director filed a motion for summary judgment on September 10, 2020, and the Taxpayers filed an opposition and cross-motion for summary judgment.<sup>18</sup> The Director argued, in part, that the five-year statute of limitations applied, thus making the deficiency assessment timely.<sup>19</sup>

The Director did not argue, and the record did not suggest, that the refund was induced by fraud or any intentional act to evade tax.<sup>20</sup> The only way that the five-year statute of limitations could have applied under N.J.S. 54A:9-4 is if Taxpayers misrepresented a material fact.<sup>21</sup> Both parties agreed that Taxpayers did not act intentionally, and instead simply made a mistake.<sup>22</sup>

The Director argued that any false statement of a material fact, regardless of intent, constitutes a misrepresentation under N.J.S. 54A:9-4(c)(4) and triggers the five-year statute of

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<sup>11</sup> N.J. STAT. ANN. § 54A:9-4 (West 2022).

<sup>12</sup> *Malhotra*, 32 N.J. Tax at 445.

<sup>13</sup> *Id.* at 446.

<sup>14</sup> *Id.* at 445.

<sup>15</sup> *Id.* at 445–446.

<sup>16</sup> *Id.* at 446.

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> *Id.* at 447.

<sup>20</sup> *Id.* at 453.

<sup>21</sup> *Id.*

<sup>22</sup> *Id.* at 450.

limitations.<sup>23</sup> Taxpayers argued that an innocent mistake does not qualify as a misrepresentation, which requires intent.<sup>24</sup>

### Analysis

The issue before the Court was whether the term misrepresentation, as used in N.J.S. 54A:9-4, may be satisfied by any mistake or omission or whether the term requires a deliberate intent.<sup>25</sup> The statute does not define “misrepresentation,” nor does the statute’s plain language support a determination by the Court of the requisite level of intent.<sup>26</sup> The legislative history of the statute also did not provide guidance regarding the definition of misrepresentation.<sup>27</sup>

In the absence of other guidance, the Court turned to alternative legal contexts that employ the term “misrepresentation” frequently: contract law and insurance contracts.<sup>28</sup> Both contemplate a misrepresentation as including an element of intent.

In contract law, misrepresentation involves a false statement of fact “made with knowledge of its falsity” and “with the intention that the other party rely” on the false statement.<sup>29</sup> In the insurance context, coverage under an insurance policy may be voided by the insurer because of a post-loss misrepresentation made by the insured only if the misrepresentation is “knowing and material.”<sup>30</sup> Only a “willful” lie constitutes a misrepresentation in this context, “[a] mere oversight or honest mistake” cannot justify an insurer voiding an insured’s policy.<sup>31</sup> The deceit need not be rooted in “an intent to recover proceeds to which he or she was not entitled” to qualify as a misrepresentation.<sup>32</sup>

The Court also considered the definitions of “misrepresentation” and “material misrepresentation” found in Black’s Law Dictionary, which says that misrepresentation may be “understood to mean a statement *made to deceive or mislead*.”<sup>33</sup> A material misrepresentation is defined as a “*deliberate* hiding or falsification of a material fact” which directly affects the viability or terms of a contract, deal, or transaction between two parties.<sup>34</sup>

Each of the extrinsic sources consulted by the Court required “a level of intent that does not rise to the level of fraud but cannot be done accidentally.”<sup>35</sup> The Court noted that each context

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<sup>23</sup> *Id.* at 453–454.

<sup>24</sup> *Id.* at 448.

<sup>25</sup> *Id.* at 454.

<sup>26</sup> *Id.* at 455.

<sup>27</sup> *Id.*

<sup>28</sup> *Id.* at 456.

<sup>29</sup> *Id.* at 456 (citing *Berman v. Gurwicz*, 189 N.J. Super. 89, 92, 458 A.2d 1311 (Ch. Div. 1981) (quoting *Foont-Freedensfeld v. Electro-Protective*, 126 N.J. Super. 254, 257, 314 A.2d 69 (App. Div. 1973), *aff’d*, 64 N.J. 197, 314 A.2d 68 (1974))).

<sup>30</sup> *Id.* at 455 (quoting *Longobardi v. Chubb Ins. Co.*, 121 N.J. 530, 540, 582 A.2d 1257 (1990) (citing N.J. STAT. ANN. § 17:33A-4a(1))).

<sup>31</sup> *Id.*

<sup>32</sup> *Id.*

<sup>33</sup> *Id.* at 456 (quoting *Black’s Law Dictionary*, 903 (5th ed. 1979)) (emphasis added).

<sup>34</sup> *Id.* at 456 (quoting *Black’s Law Dictionary*, 881 (5th ed. 1979)) (emphasis added).

<sup>35</sup> *Id.* at 457.

employed words and phrases of intent in defining misrepresentation, including “knowing,” “intent that others rely,” “lying,” “deliberate,” and “concealment” and that “misrepresentation must include some level of intent that is above a mistake.”<sup>36</sup>

The Court further reasoned that the statute’s differentiation between a three-year statute of limitations for acting on some errors, and a five-year statute of limitations for errors involving fraud or misrepresentation is justifiable only if there are “assessable errors that are not misrepresentations of material facts.”<sup>37</sup> Therefore, the statute’s two-tiered construction “implies that not every error rises to the level of a misrepresentation of material fact.”<sup>38</sup> While any mistake prompting action by the Director must be material in nature, “that does not mean that all material mistakes are misrepresentations.”<sup>39</sup> A finding that “every mistake is a misrepresentation would render the distinction between the five-year and three-year statutes of limitations meaningless.”<sup>40</sup>

Ultimately, the Court determined that a misrepresentation of material fact under N.J.S. 54A:9-4 requires “more than an innocent mistake.”<sup>41</sup>

### **Pending Bills**

Currently, there is one bill pending that concerns N.J.S. 54A:9-4, but it does not address the definition of the term “misrepresentation” as raised in *Malhotra v. Dir., Div. of Tax’n*.<sup>42</sup>

### **Conclusion**

Staff seeks authorization to conduct additional research and outreach to determine whether it would be appropriate to modify N.J.S. 54A:9-4 to clarify the term “misrepresentation” as discussed by the Court in *Malhotra v. Dir., Div. of Tax’n*.

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<sup>36</sup> *Id.*

<sup>37</sup> *Id.*

<sup>38</sup> *Id.* at 458.

<sup>39</sup> *Id.*

<sup>40</sup> *Id.*

<sup>41</sup> *Id.* at 459.

<sup>42</sup> A.B. 4295, 220th Leg., 2022 Sess. (N.J. 2022) and S.B. 2876, 220th Leg., 2022 Sess. (N.J. 2022) (“Adapts new federal partnership audit regime under gross income tax, ends COVID-related State tax extensions, and eliminates requirement to affirmatively elect New Jersey S Corporation status”).