Pennsylvania Institute of Certified Public Accountants
(PICPA)

Testimony
to

House Finance Subcommittee on Tax Modernization & Reform

Pennsylvania House of Representatives

Feb. 20, 2018
On behalf of the Pennsylvania Institute of Certified Public Accountants (PICPA), thank you for the opportunity to discuss Pennsylvania’s personal income tax law and its impact on taxpayers.

My name is Jason Skrinak, and I am the practice leader for RKL’s state and local tax group. I am also past chair and current member of the PICPA State Taxation Committee.

RKL is a leading financially oriented professional services firm with 400 team members in offices located in Lancaster, Reading, York, Harrisburg, and Mechanicsburg. RKL primarily serves privately held businesses, including many family-owned and closely held entities, throughout the Mid-Atlantic and beyond. The PICPA, founded in 1897, is the second-oldest and the fourth-largest CPA organization in the United States. Membership includes more than 22,000 practitioners in public accounting, industry, government, and education. The PICPA preserves the legacy and propels the integrity of the CPA profession by working with state and federal legislative and regulatory bodies and the public to develop sound public policy in the areas of accounting, auditing, and taxation.

The Pennsylvania personal income tax (PIT) is levied against the taxable income of resident and nonresident individuals, estates and trusts, partnerships, S corporations, business trusts, and limited liability companies that are not taxed as corporations for federal purposes. It is difficult to directly compare Pennsylvania’s personal income tax rate with other states because Pennsylvania computes taxable income on gross earnings, while other states compute taxable income on net earnings, like federal taxation.

Additionally, because of the uniformity clause of the Pennsylvania Constitution, an item is taxable only if it falls into an enumerated category. In states modeled on the federal system, income is considered taxable unless specifically excluded. Also, Pennsylvania does not tax pension income, unlike most other states. Taking all this into consideration, Pennsylvania has an effective personal income tax rate that is one of the lowest in the country.

Pennsylvania has had a personal income tax rate of 3.07 percent since 2004. Below are the eight income types that are taxed by the Commonwealth:

- Compensation
- Interest
- Dividends
- Net profits from business, profession, or farm, including interest income from business working capital
- Net gain from the sale or disposition of property
- Net income from rents, royalties, patents, and copyrights
- Income from estates and trusts
- Gambling and lottery winnings, except Pennsylvania state lottery prizes
Lastly, to help you in your endeavor of evaluating changes in tax rules, we encourage you to review a framework of 10 guiding principles of good tax policy developed by the American Institute of Certified Public Accountants (AICPA).

In brief, the 10 principles are as follows:

- **Equity and fairness.** Similarly situated taxpayers should be taxed similarly. This includes horizontal equity (taxpayers with equal ability to pay should pay the same amount of taxes) and vertical equity (taxpayers with a greater ability to pay should pay more taxes).
  Note: Equity is best measured by considering a range of taxes paid, not by looking just at a single tax.

- **Certainty.** Tax rules should clearly specify when and how a tax is to be paid, as well as how the amount will be determined. Certainty may be viewed as the level of confidence a person has that a tax is being calculated correctly.

- **Convenience of payment.** A tax should be due at a time or in a manner most likely to be convenient to the taxpayer. Convenience helps ensure compliance. The appropriate payment mechanism depends on the amount of the liability, and how easy (or difficult) it is to collect. Those applying this principle should focus on whether to collect the tax from a manufacturer, wholesaler, retailer, or customer.

- **Economy of calculation.** The costs to collect a tax should be kept to a minimum for both the government and the taxpayer.

- **Simplicity.** Taxpayers should be able to understand the rules and comply with them correctly and in a cost-efficient manner. A simple tax system better enables taxpayers to understand the tax consequences of their actual and planned transactions, reduces errors, and increases respect for that system.

- **Neutrality.** The tax law’s effect on a taxpayer’s decision whether or how to carry out a particular transaction should be kept to a minimum. A tax system’s primary purpose is to raise revenue, not change behavior.

- **Economic growth and efficiency.** A tax system should not impede productivity but should be aligned with the taxing jurisdiction’s economic goals. The system should not favor one industry or type of investment at the expense of others.

- **Transparency and visibility.** Taxpayers should know that a tax exists, and how and when it is imposed on them and others. Taxpayers should be able to easily determine the true cost of transactions and when a tax is being assessed or paid, and on whom.

- **Minimum tax gap.** A tax should be structured to minimize noncompliance. The tax gap is the amount of tax owed less the amount collected. To gain an acceptable level of compliance, rules are needed. However, a balance must be struck between the desired level of compliance and the tax system’s costs of enforcement and level of intrusiveness.
• **Appropriate government revenues.** A tax system should enable the government to determine how much tax revenue it likely will collect and when. Thus, the system should have some level of predictability and reliability.

Thank you and I will be happy to answer questions.