

A Guide to Pennsylvania Business Privilege and Mercantile Taxes



When an entrepreneur decides to start a new business, there are many state and local tax considerations that should go into the planning process. Here is a brief update on the business privilege and mercantile tax, just one local tax applicable to some businesses operating in Pennsylvania.

2014 Changes

Act 42 of 2014 set guidelines that establish a compliance requirement for businesses to register and file local business privilege and mercantile tax returns. Traditionally this had been based on physical presence with a base of operations in the jurisdiction, but recent court cases (see "Making Cases" section) created uncertainty by establishing potential tax liability by virtue of a "privilege," a "transaction," or both. Act 42, effective Jan. 1, 2014, attempts to establish a new "bright line" for imposition of the taxes, but businesses in Pennsylvania may still have to register and file business privilege taxes in multiple Pennsylvania taxing jurisdictions.

Act 42 expands and clarifies the factors that permit a Pennsylvania jurisdiction to tax business activities. The tax is permissible in two instances:

- a. When a business exercises or conducts business transactions for all or part of 15 or more days within the calendar year.

- b. When a business exercises or conducts business through a base of operations in the jurisdiction.

To ensure a taxpayer is not subject to double taxation, the taxable receipts determined in (b) shall not include those receipts in (a). The act redefines the term "base of operations" as an actual, physical, and permanent place of business from which the taxpayer manages, directs, and controls its business activities (relative to that location). Act 42 amends all Pennsylvania Act 511 jurisdictions (which are separate from Philadelphia).

Act 511

Act 511, known as the Local Tax Enabling Act, was adopted in 1965. It established the authority to assess business and mercantile taxes, along with additional local earned income taxes and occupational taxes, which is now the local services tax.

Nearly all Pennsylvania business privilege and mercantile taxes are measured and assessed based upon taxable gross receipts/revenues. However, due to legislation known as the Local Tax Reform, no new receipts-based tax legislation can be implemented by local jurisdictions after 1988. As a result, only about 10 percent of local Pennsylvania jurisdictions (less than 300 total) have a business privilege tax (BPT). Those jurisdictions with a BPT,

however, provide challenges to businesses navigating local taxes. While the provisions of Act 42 establish a de minimis basis for nexus (the basis for a compliance obligation), there is no limit to the number of BPT taxpayer responsibilities.

Sterling Act

The Sterling Act of 1932 established an entirely separate local taxing guideline. Philadelphia's BPT, reconstituted as the Business Income and Receipts Tax, is a two-part tax, taxing both gross receipts/revenues and net income. Tax nexus in Philadelphia is more stringently defined:

- Any person/business who engages in a taxable activity in or attributable to Philadelphia is subject to the tax, whether or not the person/business is a resident, or whether or not there is a permanent place of business in Philadelphia.
- In general, taxable activity includes any trade, business, profession, vocation, or any manufacturing, commercial, service, financial, or utility business or activity that originates from, is carried on through, is directed from, or is otherwise attributable to Philadelphia.

Act 42 ensures no double taxation by Act 511 jurisdictions of receipts that are taxed by Philadelphia.



Making Cases

The first bright line case of significance, *Gilberti v. City of Pittsburgh* (and reaffirmed by *Township of Lower Merion v. QED Inc.*), cemented the “base of operations” standard for establishing a taxable nexus that was consistent guidance, without deviation, for 21 years.

These cases helped to define the practices of allocating gross receipts (determining share of receipts at one base of operation when more than one base of operations exists), apportioning gross receipts (calculating share of receipts includable in the tax base when there is performance of services outside of Pennsylvania), and attributing gross receipts (used to specifically identify receipts directly or indirectly to a particular base of operations).

Cases such as 2002’s *Northwood Construction Co. v. Township of Upper Moreland* permitted the carve-out basis for apportionment, while still holding true the base of operations standard affirmed in *Gilberti*. But in the 2007 Pennsylvania Supreme Court case *Rendina Inc. v. City of Harrisburg*, there was an emphasis on the privilege of doing business in a jurisdiction, without regard to a base of operations. Shortly thereafter, *A&L Inc. v. Township of Rostraver* presented the privilege of doing business, exclusive of a base of operations, in attributing taxable gross receipts activities.

Despite all the cumulative guidance of Act 511 and the related court cases, it may come down to the specifics of a locality’s regulations and ordinances. In the Commonwealth case of *J&K Trash Removal Inc. v. City of Chester*, for instance, poorly crafted language backfired against the local tax jurisdiction in the area of apportionment.

The New BPT Reality

While each local jurisdiction may regulate differently, the changes resulting from the passage of Act 42 are automatic across the state. As a result, businesses not previously registered and filing with a local jurisdiction who reach or exceed 15 days of sales/service performed in the jurisdiction in 2015 will create a 2015 filing responsibility. Businesses that go into many jurisdictions as a part of their business purpose – such as contractors, lawn/snow removal services, or even tax and accounting firms – could find themselves subject to many different jurisdictions’ business privilege and mercantile taxes.

An extensive business review, and perhaps even an overhaul of the business’s accounting system to better track where sales or services are provided, may be necessary.

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