June 26, 2017

Re: Email to Senate Finance Committee - Please Support HB 866

Dear Senator,

On behalf of the 22,000 members of the Pennsylvania Institute of Certified Public Accountants (PICPA), I am writing to respectfully request your support for House Bill 866 (Printer’s No. 972) sponsored by Rep. George Dunbar, which passed the House on June 13 by a vote of 189-0. The bill is on the Senate Finance Committee agenda for consideration today.

The Bill

HB 866 amends the Local Tax Enabling Act (LTEA) to provide greater uniformity and clarity in the collection of local income taxes. Opposition is specifically targeted at the provision in HB 866 for out-of-state tax credits to be allowed against a jurisdiction’s entire earned income tax (EIT) rate, instead of the first 1 percent (which is being referred to as the “base rate,” but which is neither defined or even stated in the LTEA). HB 866 is nearly identical to House Bill 245 from last session that Gov. Tom Wolf unexpectedly vetoed on Nov. 4, 2016. That bill was overwhelmingly passed by the House (148-42) and Senate (36-12).

House Bill 866 Prevents Double Taxation

Prior to Act 32 of 2008, all jurisdictions in the state allowed taxpayers to offset out-of-state credits (primarily for work in New York and Delaware) against the entire EIT rate. There was no stipulation that add-ons to a “base rate” were to be treated differently or exempted from credit. Most of the additions to the EIT rate came from four sources: 1) Act 47 distressed communities, 2) Act 205 distressed pension plans, 3) open space referenda, and 4) Act 24 replacement of occupation assessment tax (OAT). The intention of Act 32 was to streamline the collection and distribution of EIT funds without increasing or decreasing any one taxpayer’s liability. Therefore, the intent was that if a credit was allowed prior to Act 32, it would still be allowed after Act 32. Unfortunately, due to a wording change in the Act, some jurisdictions found an interpretation loophole and chose to limit credits, disallowing them for the open space and OAT add-ons. Needless to say, this created an increase in tax for some taxpayers, directly against the intent of Act 32. It also created double taxation for those taxpayers, as they were paying tax to the other state as well as their locality. Consequently, the provision in HB 866 attempts to correct this misinterpretation by clarifying the law to retain the pre-Act 32 crediting.

House Bill 866 Does Not Violate Revenue Neutrality

Some groups claim that the Act 24 add-on was meant to be revenue neutral at the time of its passing, and allowing credits against this would violate the neutrality. When a jurisdiction opts to replace a flat tax (OAT) with a tax based upon a percentage of revenue (EIT), it can only be revenue neutral at the specific time of the change. As taxpayers’ earnings increase, the revenue generated from EIT also increases, whereas under the OAT an increase in taxpayers’ earnings would not affect the revenue generated. Therefore, to say that the provision in HB 866 would violate the revenue neutrality of Act 24 is simply not true or relevant.
Impact to Schools is Minor
For HB 866 to adversely affect a school district, two conditions would need to be met. The school district would need to have an add-on for Act 24, and it would have to currently not allow out-of-state taxes to be credited against that add-on. Of the 500 school districts in Pennsylvania, only two match those criteria: Solanco and Warwick school districts in Lancaster County. In addition, the impact would only be on the revenue generated by the add-on tax and only for those taxpayers working in New York or Delaware. Obviously, that impact is extremely small compared to school district revenue from EIT throughout the commonwealth.

Other important taxpayer protections in HB 866 include a safe harbor provision that is consistent with federal language in the Internal Revenue Code, limited oversight of the system by the Department of Community and Economic Development, a prohibition against charging taxpayers with no income a penalty when they do not file a return, clarification of the withholding tax rates for employees who are on a temporary assignment, prohibition of the collection of delinquent taxes through contingent fee audits, prohibition of an assessment of any earned income tax to be imposed more than five years after the date on which the tax should have been filed (except in cases of fraud), and authorization for the local tax collector to abate any penalty imposed under the LTEA. The Sterling Act, and therefore the City of Philadelphia, is not affected by these amendments.

Please view our issue brief which further explains the PICPA’s position. Thank you in advance for your support.

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