

BUSINESS PRIVILEGE TAX / NET PROFITS TAX: Owner Occupied Rental Property

Q: A taxpayer owns a boarding home. The taxpayer lives upstairs and the boarding home occupies the downstairs of the home. The boarding home is incorporated and the taxpayer is the only shareholder. The boarding home is paying rent to the taxpayer. Based on the aforementioned facts, what is the Department of Revenue's position regarding the taxability of owner occupied rental property?

A: *Excluded from the definition of "Business" under Business Privilege Tax Regulation 101(D.)(8.) is "... rental income generated from real property which is the principal residence of the owner and consists of three or less residential units." Additionally, Income Tax Regulation 220(b)(1)(a) excludes from the NPT rental activity which meets **each** of the following criteria: 1) it is the principal residence of the owner; 2) is totally residential; and consists of three (3) rental units or less.*

*BPT Regulation 103(D.)(4.) lists as an example the "(h)olding, acquiring, leasing, or disposing of any property located in Philadelphia" as an activity which constitutes doing business in Philadelphia and subjecting a taxpayer to the full measure of the tax (i.e. gross receipts and net income bases). In the scenario presented, the individual sole shareholder receives rental income from a business lessee (in this particular case, a corporation) that in effect changes the character of the rental income to the individual as "commercial" rent. The "residential rental" protection from BPT/NPT taxation of the regulations noted above would **not** apply. This rental activity is fully taxable for BPT/NPT purposes.*