

# PHILADELPHIA TAX CODE & REGULATORY AMENDMENTS

## ***Ordinance Changes***

### **1. Wage and Net Profits Tax – Rates**

City Council Bill No. 010003 amended Philadelphia Code § 19 - 1502 by imposing new Wage and Net Profits Tax rates.

#### **a. Wage Tax – Effective July 1, 2001 and thereafter:**

- *Residents* 3.0385 % + 1.5% (PICA) = 4.5385%
- *Nonresidents* 3.9462%

#### **b. Net Profits Tax – Effective January 1, 2001 and thereafter:**

- *Residents* 3.0385 % + 1.5% (PICA) = 4.5385%
- *Nonresidents* 3.9462 %

### **2. Business Privilege Tax – Rates**

City Council Bill No. 010004 amended Philadelphia Code § 19-2604 by imposing new Business Privilege Tax rates for privilege years 2002 and thereafter.

#### **a. 2002 Regular Tax**

- *Gross receipts base rate* 2.4 mills
- *Net income base rate* 6.5 %

#### **b. 2002 Alternative Receipts Tax**

- *Manufacturers* 3.97 %
- *Wholesalers* 5.58 %
- *Retailers* 1.32 %

### **3. Business Privilege Tax – Active Presence Nexus Standard**

City Council Bills Nos. 980005/ 980450 amended Philadelphia Code § 19-2603 by adopting an active presence nexus standard for Business Privilege Tax effective July 1, 1998. All taxpayers will be subject to the full Business Privilege Tax (i.e. gross receipts and net income bases) if their business activity within Philadelphia constitutes an “active presence”. In effect, taxpayers engaged in the sale of tangible personal property that are protected from net income taxation by U.S. Public Law 86 –272 (15 USC § 381 et. Seq.) will be subject to the gross receipt portion of the Business Privilege Tax to the extent they maintain an “active presence” within Philadelphia.

### **4. Business Privilege Tax – Information Technology Company**

City Council Bill No. 000336 amended Philadelphia Code § 19-2601 by adding a new definition - - *Information Technology Company*. The ordinance excludes from the definition of *Receipts* any receipts or a portion of receipts from the specific business conducted by an Information Technology Company. An Information Technology Company is defined as:

*A person whose business is categorized as electronic data processing services (NAIC 5142 and 51421), computer systems design and related services (NAIC 5415, 54151, and 541512), custom computer programming services (NAIC 541513), and on-line information services (NAIC 514191), as set forth in the North American Industry Classification System, 1997 (“NAIC”) codes established by the Office of Management and Budget, Executive Office of the President.*

The exclusion is for privilege tax years 2001 through 2006. The ordinance took effect on July 1, 2000.

### **5. Wage Tax – Stock Options**

City Council Bills 000354 and 000451 amended Philadelphia Code §§ 19-1501 and 19-2802 (i.e. PICA) respectively by excluding from the definition of *Salaries, Wages, Commissions and Other Compensation* stock options which do **not** have a *readily ascertained fair market value* as defined by 26 CFR § 1.83-7(b). Any amount that would otherwise be considered as compensation arising from the exercise, exchange, sale, or disposition of stock options, whether or not they had a readily ascertained fair market value when granted will not be taxable.

Stock options that do have a readily ascertained fair market value on the date of grant will be considered compensation in the amount of such value received. If an employee is offered the choice of receiving compensation in cash or stock options and chooses the options, then the readily ascertained fair market value will be equal to the cash that was offered.

The exemption applies only to stock options that are granted after the effective date of the ordinance (i.e. September 14, 2000) and to stock options that are exercised, exchanged, sold, or otherwise disposed of, on or after that date.

## **6. Philadelphia Keystone Opportunity Zone**

City Council Bill No. 980788A added a new chapter to the Philadelphia Code (§ 19-3200) entitled *Keystone Opportunity Zone*. This ordinance provides for the exemption, abatement or credit of certain taxes (i.e. Business Privilege, Net Profits, Wage, Business Use & Occupancy, Real Estate and Philadelphia Sales & Use Taxes) within the geographical area designated as the Philadelphia Keystone Opportunity Zone. The ordinance was approved on December 30, 1998 and was effective January 1, 1999. The provisions of the ordinance will terminate on December 31, 2010.

City Council Bill No. 0100092 amends Philadelphia Code § 19-3200 to include the addition of new sub-zones collectively designated as the *Philadelphia Keystone Opportunity Expansion Zone (KOEZ)*. The tax benefits applicable to the KOEZ are effective as of January 1, 2001 and continue through December 31, 2013. The bill also amends City Council Bill No. 980788A to implement legislative technical amendments made by the Commonwealth.

## **7. Net Profits Tax & Regulated Investment Companies**

City Council Bill No. 980787 amended the Wage and Net Profits Tax Code (§ 19-1502) and the PICA Tax on Wages and Net Profits (§ 19- 2803) by providing as an exclusion from those taxes for the net profits earned by a domestic or foreign business trust, or any series thereof, that qualifies as a regulated investment company (RIC) under IRC 851 and is registered with the SEC under the *Investment Company Act of 1940*. The exclusion also applies to any related domestic or foreign business trust or any series thereof, which confines its activities in Philadelphia to the maintenance, administration and management of intangible investments and activities of regulated investment companies.

The ordinance was approved December 30, 1998 and is effective for tax years beginning on or after January 1, 1998.

## **8. Hotel Room Rental Tax – Tourism and Marketing Tax**

City Council Bill No. 990116 amended the Hotel Room Rental Tax (Philadelphia Code § 19-2400) by providing an additional excise tax on hotel room rentals and designating the tax revenues to be deposited into a special fund to be used for tourist promotion activities. The new *Tourism and Marketing Tax* is 1% on the consideration received by each operator of a hotel from each transaction of renting a room to accommodate transients.

The ordinance was approved on May 6, 1999 and was effective July 1, 1999. The ordinance was made possible by Section 10 of Pennsylvania's *Community and Economic Improvement Act* (Act 174 of 1998).

## **9. Vehicle Rental Tax**

City Council Bill No. 000083 added a new chapter to the Philadelphia Code (i.e. § 19-3200) imposing an excise tax on the rental of vehicles in the City of Philadelphia. The tax is two percent (2%) of the *Purchase Price* of the rental and is collected by the *Vehicle Rental Company*. The return and tax payments will be due from the Vehicle Rental Company on or before the 15<sup>th</sup> day of each month (for the preceding month).

The ordinance was approved on March 30, 2000 and was effective July 1, 2000.

## **10. Real Estate Non-Utilization Tax**

City Council Bill No. 000028 amended Philadelphia Code § 19-2500 by changing the definition of *Vacant and Abandoned Property*, the rate of tax and the means of collecting the tax.

*Vacant and Abandoned Property* has been divided into two (2) separate definitions - - *Abandoned Property* and *Vacant Lot*. *Abandoned Property* is any property that is not a vacant lot and which has either remained continuously unoccupied during the privilege year and for the prior four calendar years or has been licensed as vacant for the entire privilege year under Section PM-102.4 of Title 4 of the Philadelphia Code; and either:

- has been under continuous designation as a public nuisance [building(s) formerly used as a dwelling] or
- has been under continuous citation by an agency of the City for violation of Philadelphia health and safety code provisions [building(s) formerly not used as a dwelling]
- has been continuously under citation for violating PM-102.4 or PM-302.0 of title 4 of the Philadelphia Code (i.e. property maintenance code) during the privilege year [land not containing any building].

Vacant Lot is any property that is unimproved or contains no buildings and has a lien for demolition of any structures by the Department of Licenses and Inspections.

For privilege years beginning January 1, 2001 and thereafter, a tax is imposed on abandoned property at five percent (5%) of the assessed value of the real estate as most recently determined by the Board of Revision of Taxes. The tax on a vacant lot is ten percent (10%) of the assessed value of the real estate.

In any appeal from the imposition of the tax, the Tax Review Board shall find in favor of an appellant who shows the vacant lot had been completely fenced during the entire privilege year or is subject to a written agreement between the appellant and the owner of property abutting the vacant lot. An appeal will also be granted in instances where the abutting property owner also owns the vacant lot.

The provisions of the ordinance took effect January 1, 2001.

**11. Real Estate Tax – Exemption – Improvements to Deteriorated Industrial, Commercial or Other Business Properties**

City Council Bill No. 000225 amended Philadelphia Code § 19-1303(3) by extending the Real Estate Tax Exemption Schedule from three (3) years to ten (10) years for the assessable amount of improvements to deteriorated Industrial, Commercial or other Business Properties. The ordinance applies only to an exemption for which application is made to the Board of Revision of Taxes on or after the effective date. This amendment was effective October 4, 2000 (i.e. date of the Mayor's signature).

**12. Real Estate Tax – Exemption – New Construction of Residential Properties**

City Council Bill No. 000226 amended Philadelphia Code § 19-1303(4) by extending the Real Estate Tax Exemption Schedule from three (3) years to a period of ten (10) years immediately following the date on which settlement is made. This provision applies only to exemptions for which application is made to the Board of Revision of Taxes on or after the ordinance's effective date. The Mayor signed this Bill on September 12, 2000.

### **13. Real Estate Tax – Exemption – Improvements to Residential Properties**

City Council Bill No. 000227 amended Philadelphia Code § 19-1303(2) by extending the Real Estate Tax Exemption Schedule on improvements to residential properties to 100% of the assessable amount of the improvement costs for each of the ten (10) years of the exemption. The exemption shall commence for the first year for which the improvements would otherwise be taxable. After the tenth year, the exemption shall terminate. Prior law allowed a ten-year exemption, but each year successive year reduced the percentage allowed (i.e. second year 90%, third year 80%, etc.). This ordinance will apply only to exemptions for which application is made to the Board of Revision of Taxes. The Mayor signed the Bill on September 12, 2000.

### **14. Interest and Penalties – Effective July 1, 1997**

City Council Bill No. 970155 amended Philadelphia Codes §§ 19-509 and 19-1303 by increasing the rates of interest imposed for unpaid city taxes.

#### **a. Taxes and Rents – General**

- One percent (1 %) per month – 12 % annually

#### **b. Real Estate Tax**

- .75 percent (.75 %) per month – 9% annually

### **15. Personal Property Tax**

City Council Bill No. 970666 amended Philadelphia Code § 19-1102 by choosing not to impose and collect the Personal Property Tax allowed under the Act of June 17, 1913 (P. L. 507, No. 335) for tax years 1997 and thereafter. It also suspends any Personal Property Tax imposed under the authority of the Sterling Act for 1997 and thereafter.

## **16. Realty Transfer Tax – Excluded Transactions – Life Partnerships**

City Council Bill No. 970749 (effective May 19, 1998) amended the Realty Transfer Tax Ordinance at Philadelphia Code § 19-1405 *Excluded Transactions* to exclude from the Realty Transfer Tax transfers between life partners.

City Council Bill No. 970750 (effective May 19, 1998) amended the Fair Practices Ordinance at Philadelphia Code § 9-1106 by defining the term “*Life Partnerships*” as a “*long-term committed relationship between two unmarried individuals of the same gender...*”.

The legislation requires the parties to any such transfer to file a “*Life Partnership Verification Statement*” with the Commission on Human Relations. The Commission in turn will issue a “*Life Partnership Verification Statement Acceptance Letter*”; a copy of which must accompany the *Real Estate Transfer Tax Certification Affidavit* when the deed transferring title is presented for recording.

## **17. Realty Transfer Tax – Real Estate Companies**

City Council Bill No. 980303 amended the definition of a *Real Estate Company* by lowering the real estate ownership requirement from ninety percent (90%) of the tangible asset holdings (exclusive of tangible assets which are freely transferable and traded on an established market) to fifty percent (50%).

The ordinance also amended the definition of an *Acquired Real Estate Company* (at Philadelphia Code § 19-1407) by adding the following language: *A transfer shall be considered to have occurred within a period of three years of another transfer or transfers, if a legally binding commitment to execute that transfer was made within that period.*

These amendments effectively remove a tax planning technique known as an “*89/11 Transfer*”. Under the law when 90% or more of the interests of a real estate company are transferred within a three- (3) year period, transfer tax is due. Sellers and buyers willing to structure a transaction so that 89% of the interest would be transferred up front with the remaining 11% after three years could eventually transfer a 100% interest with no transfer tax consequence. Under this ordinance, if a seller now sells 89% of a real estate company and at the same time agrees to sell the remaining 11% after 3 years, the transaction will be taxed as if a 100% sale of the interest of the company occurred.

The ordinance was effective for transactions taking place on or after July 1, 2000.

**18. Refunds – Statute of Limitations**

City Council Bill No. 990220 amended Philadelphia Code § 19-1703 (Refunds) by providing that petitions for refund of taxes paid to the City and/or School District of Philadelphia must be filed within three (3) years of the date of payment or the due date of the return, whichever is later.

The law applies to refund petitions filed with the Revenue Department on or after June 11, 1999.

**19. Earnings Tax – Due Date for 4<sup>th</sup> Quarter Return**

City Council Bill No. 990219 amended Philadelphia Code § 19-1503(2) by making the fourth (4<sup>th</sup>) quarter Earning Tax return and payment due January 31. Previously, the 4<sup>th</sup> quarter Earnings Tax return was due with the Annual return on February 15. The February 15 Annual return has been pushed back (by regulation- see below) to April 15.

***Regulation Changes***

**1. Earnings Tax – Due Dates for Annual Information Returns**

Income Tax Regulation § 303(a)(2) was amended to change the due date of the annual information return for employees whose employers are not required to withhold the Wage Tax from *the last day of February to April 15*.

Starting with the fourth quarter of 1998, the fourth quarter payment will be due on January 31 of the following year (e.g. January 31, 1999). The annual information return / reconciliation will now be due on April 15 (e.g. April 15, 1999).

**2. Business Privilege/ Net Profits Taxes – Real Estate Entities – Separate Accounting**

Former Income Tax Regulation § 224 entitled *Safe Harbor Election for Real Estate Investment Trust (REITS)* was repealed in its entirety and replaced with a new Income Tax Regulation § 224 entitled *Election for Real Estate Entities*.

Any *Real Estate Entity* (for purposes of the Business Privilege Tax and Net Profits Tax) may make an irrevocable election to use separate accounting, rather

than the regular apportionment formula, to compute net income attributable to Philadelphia.

A *Real Estate Entity* includes a REIT, corporation, association, partnership (general, limited, limited liability), trust, joint venture, limited liability company or sole proprietorship which is in the business of holding, selling, or leasing owned real estate and which:

- Derives directly or indirectly 75% or more of its annual gross receipts from the ownership, leasing, or disposition of real estate and;
- Owns real estate directly or indirectly, the book value of which comprises 75% or more of the value of its assets.

“*Separate Accounting*” is the computation of net profits/income specifically attributable to each income-producing property (both rental and mortgage activity) located within Philadelphia. Gains from the sale of property are allocated to the location of the real property.

Regardless of the residency (i.e. domicile) of the person(s) subject to Net Profits Tax, the real estate entity making this election agrees to pay the tax using the resident rate. In addition, a real estate entity agrees to pay the Net Profits Tax without any exclusions otherwise applicable. For example, a Partnership composed entirely of corporate partners will be subject to the tax.

### **3. Business Privilege Tax – Tiered Partnerships – Exclusion from Receipts / Net Income**

Business Privilege Tax Regulation 302 (i.e. Exclusions from Receipts) was amended to exclude from gross receipts the dividends, interest and royalties received by a corporation or partnership where the receiving corporation or partnership owns at least 20 % of the voting power of all classes of stock and at least 20% of each class on nonvoting stock of the distributing corporation. Also excluded is the distributive share of net income received by a partner where the receiving partner’s ownership of capital at the end of the year is at least 20% of the distributing partnership.

Business Privilege Tax Regulations sections 403 (i.e. Net Income Method I) and 404 (i.e. Net Income Method II) were amended to allow the flow through of this receipts exclusion as a deduction from taxable net income.

**4. Net Profits Tax – Tiered Partnerships – Modification of Net Profits**

Income Tax Regulation 202 was amended to specify that where a partnership is required to pay the Net Profits Tax, the partners are ***not*** liable to pay the tax a second time on their distributive share of income from the partnership. This is true even if the partner is another partnership. If however, the receiving partner has other business activity (i.e. outside the partnership) in Philadelphia, a Net Profits Tax return will still be required of the partner.

**5. Business Privilege Tax – Dyers of Fabric and Yarn – Exclusion from Receipts**

Business Privilege Tax Regulation 302 was amended to exclude the receipts attributable to the bona fide delivery of fiber, yarn, fabric or materials that have been dyed by a chemical mechanical process and delivered outside Philadelphia.

This change is effective for privilege years 1996 and thereafter.

**6. General Regulations - Real Estate Tax – Application of Payments**

A new section ( i.e. § 506 ) was added to the General Regulations entitled *Application of Payments for Real Estate Taxes*.

All payments for real estate taxes shall be applied to the oldest tax year first and apportioned among tax principal, interest, penalties, costs and fees, regardless of any designation made by the taxpayer or his or her agent. However, if such allocation would result in a taxpayer being unable to take advantage of the Commonwealth’s Senior Citizen Real Estate Tax Rebate Program or being unable to enter into the Installment Payment Program (Philadelphia Code § 19-1305) the taxpayer may apply for a different allocation of the payment. The Philadelphia Department of Revenue will set the method of applying for a change in allocation of the payment forth.

**7. General Regulations – Abatement of Interest & Penalties – Real Estate Tax Lien Sale**

A new section has been added to the General Regulations (i.e. § 704) entitled ***Petitions for Abatement of Interest and Penalties in Cases Where the Real Estate Tax Claims Have Been Sold by the City or the School District.***

The Tax Review Board will no longer have jurisdiction for any petitions for the abatement of interest and penalties filed after June 30, 1997 with respect to any Real Estate tax claims which have been sold by the City or the School District to a third party. The Ombudsman for the Real Estate Tax Lien Sale will hear such petitions.

**8. General Regulations – Interest on Refunds – Rate of Interest**

Section 306 of the General Regulations was amended to specify 41 P.S. § 202 as the rate of interest to be paid on refunds. 41 P.S. § 202 specifies a “*legal rate of interest*” to be six percent (6%).

This regulation was effective 6/28/99.

**9. Use & Occupancy Tax – Repeal of Form UO4**

Section 503(b) of the Use & Occupancy Tax Regulations was amended to eliminate the landlord’s duty to file and remit delinquent payments on Form UO-4. The landlord must still report delinquent tenants on a timely filed Form UO-3. However, the tenant must now pay any subsequent payments the tenant makes on a previously reported delinquent account directly to the City in the manner prescribed by the Commissioner. The information that must be included is the tenant’s name, address, tax period, Philadelphia Business Tax Account Number and Federal Tax Identification Number.

This regulation was effective for tax periods beginning on or after January 1, 2000.