Pennsylvania Enacts Record Tax Reform

Pennsylvania's 2022-2023 budget, Act of Jul. 8, 2022, P.L. __. No. 53 (Act 2022-53) (HB 1342) implements sweeping tax reform and revises some of Pennsylvania's most business-unfriendly tax provisions. The bill will:

Personal Income Tax

Permit Like-Kind Exchanges for All Taxpayers – Pennsylvania was one of the only states in the country that did not generally conform to I.R.C. § 1031, which permits taxpayers to defer gain on the exchange of investment properties. The bill allows individuals to defer Pennsylvania income tax on such exchanges in alignment with federal law. It is effective for transactions occurring after December 31, 2022.

Broaden the Section 179 Expense Deduction – Pennsylvania was one of a minority of states that did not conform to I.R.C § 179, which allows individual owners of pass-through entities to take a full deduction for the purchase price of qualifying equipment used by their business in Pennsylvania. The bill amends Pennsylvania's personal income tax to permit individual owners who are Pennsylvania residents or non-residents to take the same deduction for state income tax as for federal income tax, based upon when the property was placed in service. It is effective for property placed in service in tax years beginning after December 31, 2022.

Corporate Income Tax

Reduce the Corporate Net Income Tax Rate – Pennsylvania's 9.99% corporate net income tax is one of the highest in the country. The bill will reduce the rate gradually to 4.99% by 2031. The rate will drop to 8.99% for the 2023 tax year, 8.49% for the 2024 tax year, and will continue to drop at that annual rate until it reaches 4.99% in 2031, assuming there are no freezes or slow-downs of the rate reduction implemented via future tax bills.

Amend Corporate Income Tax Sourcing Rules for Sales of Intangible Property – Under the old rule, sales of intangible property were sourced to Pennsylvania if the income-producing activity occurred in Pennsylvania or based on the costs of performing such activity if it was performed inside and outside Pennsylvania. The amended statute generally sources sales of intangibles to Pennsylvania if the property is used in Pennsylvania. Receipts from the sale, redemption, maturity, or exchange of bonds are sourced to Pennsylvania if the customers are located in Pennsylvania. The statute also adds sourcing rules for interest, fees, and penalties from loans made by corporations that are secured by real property, generally sourcing such income to Pennsylvania if the property is located in Pennsylvania. Where the corporate loans relate to the sale of tangible personal property, the income is generally sourced to Pennsylvania if the property is delivered or shipped to a purchaser in Pennsylvania. Special rules apply for transportation property and vehicles, including aircraft used in Pennsylvania, and for interest from credit card receivables. For loans not secured by real property or relating to tangible property not covered by the aforementioned rules, the income from such loans is sourced to Pennsylvania if the borrower is located in Pennsylvania. Other types of loans not covered by the specific rules are sourced to Pennsylvania if the lender's commercial domicile is in Pennsylvania. Intangible property that does not fall into any of the designated categories in the statute is not included in the sales factor. Thus, for example, receipts from the sale of goodwill are excluded from the sales factor under the statute.

Corporate Nexus – The bill amends the nexus provisions for corporations under Section 402 to expand what business activities outside of physical presence in the Commonwealth create nexus with Pennsylvania and codifies the Department of Revenue's economic nexus policy that

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corporations with $500,000 or more sales sourced to the Commonwealth are presumed to have nexus with Pennsylvania. In combination with the expanded sourcing rules discussed above for sales from intangibles, it is likely that many additional corporations will be subject to Pennsylvania corporate net income tax under this economic nexus standard. This rule applies to taxable years beginning after December 31, 2022.

Other Notable Provisions

Effective immediately, where a qualified business was granted an extension of the term of a Keystone Opportunity Zone as the result of new job creation or new capital investment within the Zone by such qualified business, an affiliate of the qualified business may receive the same tax exemptions and benefits as the qualified business, so long as the affiliate is also a qualified business. Further, the deadline for filing an application for additional Keystone Opportunity Zones in specific, smaller counties within the Commonwealth has been extended to allow a political subdivision to file such an application with the Department of Community and Economic Affairs no later than October 1, 2023, which must then act on the application by December 31, 2023.

The bill adds a new Article XIX-H applicable to airport land development zones, which establishes a program to encourage airports to create new jobs on properties that they own, and new Article XIX-I, which creates a Pennsylvania Child and Dependent Care Enhancement tax credit program. These provisions take effect in fiscal years beginning after June 30, 2022.

The bill also imposes sales and use tax on peer-to-peer car sharing programs at the rate of $2 per day. Peer-to-peer car sharing programs allow personal vehicles to be rented to the public. Peer-to-peer car sharing is a business distinct from Uber and similar transportation services. Shared vehicle owners cannot utilize the resale exemption if they purchase or repair shared-use vehicles.

The text of the bill is available here.