PENNSYLVANIA STATE AND LOCAL TAX UPDATE

ALLEGHENY TAX SOCIETY
MAY 16, 2022

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Supreme Court IRS Ruling Elevates Fight Over Key Tax Deadline

By Aysha Bagchi and Jeffery Leon
April 22, 2022, 2:07 PM

Bloomberg Law News 2022-04-25T11:18:17307-04:00

Supreme Court IRS Ruling Elevates Fight Over Key Tax Deadline

By Aysha Bagchi and Jeffery Leon 2022-04-22T14:07:29000-04:00

A Thursday Supreme Court ruling on a taxpayer-lawsuit deadline affects only a small subset of litigation against the IRS, but opens the door to a broader fight over a different deadline that applies to most U.S. Tax Court cases: challenges to tax bills.

In its opinion in *Boechler, P.C. v. Commissioner* , the high court agreed with a North Dakota law firm that the deadline to challenge IRS property seizure decisions isn't "jurisdictional"—a label that deprives a court of authority to hear any case that misses the filing deadline. The court further held that the Tax Court may apply what's known as "equitable tolling" to pause the property seizure filing deadline at issue in special circumstances.

While the court didn't discuss what those special circumstances might look like, In past cases it has provided parameters around equitable tolling. For example, a 2016 ruling in *Menominee Indian Tribe of Wisconsin v. United States* said litigants may secure equitable tolling if they have been pursuing their rights diligently and "some extraordinary circumstances" got in the way of filing on time.

The Thursday ruling only affected the 30-day time limit under tax code Section 6330(d)(1) to challenge the IRS's seizure decisions. Tax law specialists, however, said the ruling could lead to more lawsuits testing the contours of other taxpayer lawsuit deadlines.

"You're going to have taxpayers lodge a full-frontal assault on any deadline, and then try at least to make the argument and shoehorn in this decision to say that the statutory deadline is not jurisdictional in nature," said Joseph DiRuzzo, a tax controversy attorney at DiRuzzo & Company.

DiRuzzo represented the petitioner in *Myers v. Commissioner* , a 2019 decision from the U.S. Court of Appeals for the D.C. Circuit reversing the Tax Court's dismissal of a whistleblower challenge for lack of jurisdiction.

The biggest Tax Court jurisdictional question will likely center on the deadlines for challenging IRS deficiency notices, or tax bills, under tax code Section 6213(a)—90 days for domestic taxpayers, 150 days for those overseas.

Deficiency lawsuits alone take up the vast majority of the Tax Court's docket. In fiscal year 2020, for example, they accounted for 95% of the nearly 17,000 cases filed at the court, according to a report providing the court's justification for its 2022 fiscal year budget.

"That's going to be where the next big fight is," said T. Keith Fogg, who heads the Harvard Law School tax clinic. Fogg co-authored a friend-of-the-court brief on behalf of the Center for Taxpayer Rights that supported Boechler's position.

Pro-Taxpayer Language

While the high court's ruling only focused on the property seizure lawsuit deadline, multiple aspects of the opinion could provide fodder for broader deadline challenges, according to tax specialists.

The IRS had argued, for example, that lower-court rulings that had deemed the deficiency deadline to be jurisdictional before Congress created the property seizure deadline were evidence that Congress expected the new time limit also to be jurisdictional.

But Justice Amy Coney Barrett wrote for the unanimous court that nearly all of those deficiency deadline decisions also pre-dated the Supreme Court's "effort to 'bring some discipline' to the use of the term 'jurisdictional'" through its decisions in recent decades.

Barrett's language would support taxpayer arguments that the longstanding decisions deeming the deficiency deadline to be jurisdictional are now on uncertain footing, according to Monte Jackel, an attorney at Leo Berwick who has worked in various roles at the U.S. Treasury's Office of Tax Policy and the IRS Office of Chief Counsel.

"The court didn't have to say that those decisions predating" the Supreme Court's recent precedent on jurisdictional deadlines "are now suspect—and that's what they said," Jackel said.

Fogg also pointed to a portion of the decision stating that other Tax Court deadlines for lawsuits seeking innocent spouse relief or interest abatement were enacted around the same time as the property seizure court deadline but, by contrast, "much more clearly link" their time limits to the court's jurisdictional authority.

The Supreme Court cited those "as examples of Congress seeming to make it clear," but "they notably did not cite to deficiency jurisdiction," Fogg said.

Pro-IRS Language

The court's narrow focus in the decision on the property seizure deadline, however, could support potential IRS arguments that the ruling doesn't have implications for other deadlines, according to Elizabeth Maresca, a clinical professor at Fordham University's law school.

"I'm not sure that this Supreme Court opinion on this statute—which is worded very differently, I think—is going to affect" the law around whether the deficiency deadline is jurisdictional, she said.

Maresca is representing a taxpayer in a case, *Castillo v. Commissioner* , that was put on hold at the U.S. Court of Appeals for the Second Circuit to await the Supreme Court's *Boechler* decision. That case involves the same property seizure deadline at issue in *Boechler*.

The Supreme Court also contrasted its Thursday ruling with its 1997 *United States v. Brockamp* decision. There, the court held that equitable tolling wasn't available for a deadline to file tax refund claims.

That case was different from *Boechler*, the court said Thursday, because of how the tax refund deadline was written, including its list of explicit deadline exceptions. The writing reflected the "administrative problem" that would flow from allowing equitable tolling of the refund deadline given that the IRS was processing more than 200 million tax returns and issuing more than 90 million refunds each year, Barrett wrote.

"I think the government would argue that a case under [the deficiency lawsuit deadline] would be more like *Brockamp*," said Gil Rothenberg, who previously headed the Justice Department Tax Division's Appellate Section and now holds roles in the law schools at American University and the University of Pennsylvania. Rothenberg noted the large number of legal challenges dealing with IRS deficiency determinations.

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From: Kaschak, John
Sent: Friday, December 17, 2021
Subject: PA DOR Comments on Remote Help Supply & Taxation of Equipment Rentals Bulletins

Remote Help Supply

- A multinational company is headquartered in PA that enters into a help supply agreement for multiple locations whereby the purchaser's managers are located in various states, but not PA, but the invoices are addressed to a payment center in PA, would the vendor be able to accept an exemption certificate from the purchaser stating the services are not sourced to PA? The vendor would be able to accept a properly completed exemption certificate that provides delivery of the service occurs outside Pennsylvania. The certificate would have to comply with the general rules regarding exemption certificates, e.g., shall contain no statement or entry which the vendor knows, or has reason to know, is false or misleading.

  On the purchaser end would the purchaser be able to substantiate the exemption with documentation of where the managers are located? The purchaser would need to substantiate that delivery and use occurs outside Pennsylvania. Where the managers are located is not necessarily dispositive—see the fourth example of Bulleting 2021-03.

- Same scenario as above but one of the manager's overseeing the help supply is located in PA. Can the purchaser render a multiple points of use exemption certificate?

  See the answer above. Under most scenarios, hours billed should be able to be allocated to a specific location.

- Multistate corporation headquartered in Pennsylvania uses computer programmers located overseas for a project that would benefit the corporation across all their locations. Would the Department allocate the portion of taxable help supply based upon the benefit received or would tax be due on the entire project cost since the headquarters are located in Pennsylvania? Would depend on the facts of the actual situation/project. If the programmers are configuring tangible personal property that is located in Pennsylvania, the services would be allocated to Pennsylvania.

- Same facts except the corporation is headquartered outside of Pennsylvania and has operations in Pennsylvania. Would a portion of the help supply service be taxable in Pennsylvania or would none as the headquarters are located outside of the state? See answer above.

- How would the Department apply nexus standards to the overseas computer programming company? If the services are deemed to be performed in Pennsylvania, would the company have to begin collecting tax on the first dollar of taxable help supply services (traditional nexus), or would the economic nexus standards apply? Economic nexus standards apply.

Taxation of Equipment Rental

- A vendor leases equipment and has a separate division that performs exempt services. The company purchases a piece of equipment for the leasing division and charged tax in accordance with the bulletin. The company has a single use of the equipment with their services division; is the use tax calculated on the fair rental value for the time the company uses the equipment for their own use? Yes.

- If the vendor primarily rents equipment and collects sales tax from customers, the vendor would likely have issued a resale certificate upon purchase of the equipment. In certain isolated instances, the vendor will perform a service with the same equipment using their own operator and meeting the standards for a non-taxable service as specified in the Bulletin. How would the vendor calculate the use tax due on the isolated instance where the equipment was used to perform a non-taxable service? The vendor must calculate use tax on the fair rental value of the equipment. Presumably, if the vendor is in the business of primarily renting equipment (as stated in the question) it should know the fair rental value of the equipment. For example, if an excavator is hired to clear a field for development, uses their own equipment with their own operator, is that going to be considered an equipment rental with an operator? If the vendor provides equipment with the services of their operator to complete a specific task or tasks without direction from the customer, then vendor is providing a nontaxable service and does not charge tax to its customer on the price of its services.

MULTISTATE TAX COMMISSION

Statement of Information Concerning Practices of
Multistate Tax Commission and Supporting States Under Public Law 86-272

Originally adopted by the Multistate Tax Commission on July 11, 1986
Revised version adopted by the MTC Executive Committee on January 22, 1993
Second revision adopted by the Multistate Tax Commission on July 29, 1994
Third revision adopted by the Multistate Tax Commission on July 27, 2001
Fourth revision adopted by the Multistate Tax Commission _____

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INTRODUCTION

In this Statement, "Supporting State" means a State that adopts or otherwise expressly indicates support for this Statement by legislation, regulation or other administrative action. Other states may adopt or otherwise indicate support for individual sections of this Statement.

This Statement addresses the application of Public Law 86-272, 15 U.S.C. §§381-384 (which is set forth in Addendum I). P.L. 86-272, which Congress adopted in 1959, prohibits a state from imposing a net income tax on the income of a person derived within the state from interstate commerce if the only business activities within the state conducted by or on behalf of the person consist of the solicitation of orders for sales of tangible personal property, provided that the orders are sent outside the state for acceptance or rejection, and, if accepted, are filled by shipment or delivery from a point outside the state.

In the decades since P.L. 86-272 was enacted, the way in which interstate business is conducted has changed significantly. Congress, however, has neither created a federal mechanism to provide administrative guidance to taxpayers nor has it updated the statute to indicate how it applies to new business activities. *See Wisconsin Department of Revenue v. William Wrigley, Jr.*, Co., 505 U.S. 214, 223 (1992) (finding the statute's minimum standard "to be somewhat less than entirely clear"). The contents of this Statement are intended to serve as general guidance to taxpayers and to provide notice as to how Supporting States will apply the statute.

This Statement is guided by the principle that sovereign authority of states to impose tax will not be preempted unless it is the "clear and manifest purpose of Congress" to do so. *Department of Revenue of Oregon v. ACF Industries, Inc.*, 510 U.S. 332, 345 (1994). *See also Heublein, Inc. v. South Carolina Tax Comm'n*, 409 U.S. 275, 281-82 (1972) (noting that Congress must convey "its purpose clearly" or "it will not be deemed to have significantly changed the Federal-State balance").

The Supreme Court recently opined, in *South Dakota v. Wayfair, Inc.*, construing the Commerce Clause, that an Internet seller "may be present in a State in a meaningful way without that presence being physical in the traditional sense of the term." 138 S. Ct. 2080, 2095 (2018). Although the *Wayfair* Court was not interpreting P.L. 86-272, the Supporting States consider the Court's analysis as to virtual contacts to be relevant to the question of whether a seller is engaged in business activities in states where its customers are located for purposes of the statute.

This Statement does not attempt to take into account limitations on the application of business income taxes other than P.L. 86-272, including those limitations that may be provided under state law. For example, the Multistate Tax Commission has adopted a model factor presence nexus statute and recommends that states adopt that statute to shield from taxation small businesses or businesses that have minimal contacts with the state. *See* Factor Presence Nexus Standard for Business Activity Taxes, adopted by the Multistate Tax Commission on October 12, 2002 (which is set forth in Addendum II).

Finally, P.L. 86-272 not only affects the determination of whether a state into which tangible personal property is delivered (the "destination state") may tax the income of the seller, but it also affects the determination of whether the state from which tangible personal property is shipped (the "origin state") may subject the related receipts to that state's throwback rule. The Supporting

States intend to apply this Statement uniformly, irrespective of whether the destination state is determining whether it can tax the income of the seller, or whether the origin state, is determining whether the related receipts are subject to that state's throwback rule.

I. NATURE OF PROPERTY BEING SOLD

Only the solicitation to sell tangible personal property is afforded immunity under P.L. 86-272; therefore, the leasing, renting, licensing or other disposition of tangible personal property, or transactions involving intangible property, such as franchises, patents, copyrights, trademarks, service marks and the like, or any other type of property are not protected activities under P.L. 86-272.

The sale or delivery, and the solicitation for the sale or delivery, of any type of service that is not either (1) entirely ancillary to solicitation of orders for sales of tangible personal property or (2) otherwise set forth as a protected activity under Section IV.B of this Statement is also not protected under P. L. 86-272.

II. SOLICITATION OF ORDERS AND ACTIVITIES ANCILLARY TO SOLICITATION

For in-state activity to be a protected activity under P.L. 86-272, it must be limited solely to *solicitation* (except for *de minimis* activities described in Article III and those activities conducted by independent contractors described in Article V). Solicitation means (1) speech or conduct that explicitly or implicitly invites an order; and (2) activities that neither explicitly nor implicitly invite an order but are entirely ancillary to requests for an order. *See Wisconsin Department of Revenue v. William Wrigley, Jr., Co.,* 505 U.S. 214 (1992).

Ancillary activities are those activities that serve no independent business function for the seller apart from their connection to the solicitation of orders. Activities that a seller would engage in apart from soliciting orders are not ancillary to the solicitation of orders. The assignment of activities to sales personnel does not, merely by such assignment, make those activities ancillary to the solicitation of orders. Additionally, activities that seek to promote *sales* are not ancillary, because P.L. 86-272 does not protect activity that facilitates sales; it only protects ancillary activities that facilitate the request for an order.

Activities that are neither solicitation of orders for sales of tangible personal property nor entirely ancillary to solicitation, and that are not *de minimis*, are not protected.

III. DE MINIMIS ACTIVITIES

De minimis activities are those activities that, when taken together, establish only a trivial connection with the taxing state. An activity conducted within a taxing state on a regular or systematic basis or pursuant to a company policy (whether the policy is in writing or not) normally will not be considered trivial. Whether or not an activity consists of a trivial or non-trivial connection with-a state is measured on both a qualitative and quantitative basis. If an

activity either qualitatively or quantitatively creates a non-trivial connection with the taxing state, and is otherwise not protected, then the activity exceeds the protection of P.L. 86-272. Establishing that unprotected activities only account for a relatively small part of the business conducted within the taxing state is not determinative of whether the activities are *de minimis*. The relative economic importance of unprotected in-state activities, as compared to protected activities, does not determine whether the conduct of the unprotected activities within the taxing state is inconsistent with the limited protection afforded by P.L. 86-272.

IV. SPECIFIC LISTING OF UNPROTECTED AND PROTECTED ACTIVITIES

The following two listings -- Section IV.A and Section IV.B -- set forth in-state activities that are presently treated by the Supporting States as "Unprotected Activities" or "Protected Activities." These listings, as well as the contents of Section IV.C, which addresses activities conducted via the Internet, may be amended by each Supporting State.

Each Supporting State may choose, in its discretion, to treat any in-state activity as protected, even if P.L. 86-272 does not require protection, provided that the state treats such activity consistently for purposes of imposing tax and applying the state's throwback rule. The mere inclusion of an activity on the listing of "Protected Activities" by a state, therefore, is not a statement or admission by that state that P.L. 86-272 protects that activity.

A. UNPROTECTED ACTIVITIES:

The following in-state activities are not considered solicitation of orders for sales of tangible personal property, entirely ancillary thereto, or otherwise protected under P.L. 86-272:

1. Making repairs or providing maintenance or service to the property sold or to be sold.

2. Collecting current or delinquent accounts, whether directly or by third parties, through assignment or otherwise.

3. Investigating credit worthiness.

4. Installation or supervision of installation at or after shipment or delivery.

5. Conducting training courses, seminars or lectures for personnel other than personnel involved only in solicitation.

6. Providing any kind of technical assistance or service including, but not limited to, engineering assistance or design service, when one of the purposes thereof is other than the facilitation of the solicitation of orders.

7. Investigating, handling, or otherwise assisting in resolving customer complaints, other than mediating direct customer complaints when the sole purpose of such mediation is to ingratiate the sales personnel with the customer.

8. Approving or accepting orders.

9. Repossessing property.

10. Securing deposits on sales.

11. Picking up or replacing damaged or returned property.

12. Hiring, training, or supervising personnel, other than personnel involved only in solicitation.

13. Using agency stock checks or any other instrument or process by which sales are made by sales personnel.

14. Maintaining a sample or display room in excess of two weeks (14 days) at any one location within the state during the tax year.

15. Carrying samples for sale, exchange or distribution in any manner for consideration or other value.

16. Owning, leasing, using or maintaining any of the following facilities or property in-state:

    a. Repair shop.
    b. Parts department.
    c. Any kind of office other than an in-home office as described as permitted under IV.A.18 and IV.B.2.
    d. Warehouse.
    e. Meeting place for directors, officers, or employees.
    f. Stock of goods other than samples for sales personnel or that are used entirely ancillary to solicitation.
    g. Telephone answering service that is publicly attributed to the business or to employees or agent(s) of the business in their representative status.
    h. Mobile stores, *i.e.*, vehicles with drivers who are sales personnel making sales from the vehicles.
    i. Real property or fixtures to real property of any kind.

17. Consigning stock of goods or other tangible personal property to any person, including an independent contractor, for sale.

18. Maintaining, by an employee or other representative, an office or place of business of any kind (other than an in-home office located within the residence of the employee or representative that (i) is not publicly attributed to the business or to the employee or representative of the company in an employee or representative capacity, (ii) so long as the use of the office is limited to soliciting and receiving orders from customers; for transmitting such orders outside the state for acceptance or rejection by the business; or for such other activities that are protected under P.L. 86-272).

    A telephone listing or other public listing within the state for the business or for an employee or representative of the business in such capacity or other indications through advertising or business literature that the business or its employee or representative can be contacted at a specific address within the state normally will be determined as the business maintaining within this state an office or place of business attributable to the business or to its employee or representative in a representative capacity. However, the normal distribution and use of business cards and stationery identifying the employee's or representative's name, street address, email address, telephone and fax numbers and affiliation with the business shall not, by itself, be considered as advertising or otherwise publicly attributing an office to the business or its employee or representative.

    The maintenance of any office or other place of business in the state that does not strictly qualify as an "in-home" office as described above will, by itself, cause the loss of protection.

    For the purpose of this subsection it is not relevant whether the business pays directly, indirectly, or not at all for the cost of maintaining an in-home office.

19. Entering into franchising or licensing agreements; selling or otherwise disposing of franchises and licenses; or selling or otherwise transferring tangible personal property pursuant to such franchise or license by the franchisor or licensor to its franchisee or licensee within the state.

20. Activities performed by an employee who telecommutes on a regular basis from within the state unless the activities constitute the solicitation of orders for sales of tangible personal property or are entirely ancillary to such solicitation.

21. Conducting an activity not listed in Section IV.B below which is not entirely ancillary to requests for orders, even if-the activity helps to increase purchases.

B. PROTECTED ACTIVITIES:

The following in-state activities are protected:

1. Soliciting orders for sales of tangible personal property by any type of advertising.

2. Soliciting of orders for sales of tangible personal property by an in-state resident employee or representative of the business, so long as the employee or representative does not maintain or use ~~any~~ office or other place of business in the state other than an "in-home" office as described in IV.A.18.

3. Carrying samples and promotional materials only for display or distribution without charge or other consideration.

4. Furnishing and setting up display racks and advising customers on the display of the business's products without charge or other consideration.

5. Providing automobiles to sales personnel for their use in conducting protected activities.

6. Passing orders, inquiries and complaints on to the home office.

7. Missionary sales activities; *i.e.*, the solicitation of indirect customers for the business's goods. For example, a manufacturer's solicitation of retailers to buy the manufacturer's goods from the manufacturer's wholesale customers is protected if these solicitation activities are otherwise immune.

8. Coordinating shipment or delivery without payment or other consideration and providing information relating thereto either prior or subsequent to the placement of an order.

9. Checking of customers' inventories without a charge therefor (for re-order, but not for other purposes such as quality control).

10. Maintaining a sample or display room for two weeks (14 days) or less at any one location within the state during the tax year.

11. Recruiting, training or evaluating sales personnel, including occasionally using homes, hotels or similar places for meetings with sales personnel.

12. Mediating direct customer complaints when the purpose thereof is solely for ingratiating the sales personnel with the customer and facilitating requests for orders.

13. Owning, leasing, using or maintaining personal property for use in the employee or representative's "in-home" office or automobile that is limited to the conducting of protected activities. Therefore, the use of personal property such as a cellular telephone, facsimile machine, duplicating equipment, personal computer and computer software that is limited to the carrying on of protected solicitation and activity entirely ancillary to such solicitation will not, by itself, remove the protection.

C. Activities Conducted Via the Internet:

To determine whether a person that sells tangible personal property via the Internet is shielded from taxation by P.L. 86-272 requires the same general analysis as with respect to persons that sell tangible personal property by other means. Thus, an Internet seller is shielded from taxation in the customer's state if the only business activity it engages in within that state is the solicitation of orders for sales of tangible personal property, which orders are sent outside that state for approval or rejection, and if approved, are shipped from a point outside of that state.

If the activities of such a seller within a state extend beyond solicitation of orders for sales of tangible personal property and are neither entirely ancillary to solicitation nor de minimis, P.L. 86-272 does not shield the seller from taxation by the customer's state.

As a general rule, when a business interacts with a customer via the business's website or app, the business engages in a business activity within the customer's state. However, for purposes of this Statement, when a business presents static text or photos on its website, that presentation does not in itself constitute a business activity within those states where the business's customers are located.

Following are examples of activities conducted by a business that operates a website offering for sale only items of tangible personal property, unless otherwise indicated. In each case, customer orders are approved or rejected, and the products are shipped from a location outside of the customer's state. The business has no contacts with the customer's state other than what is indicated.

1. The business provides post-sale assistance to in-state customers by posting a list of static FAQs with answers on the business's website. This posting of the static FAQs does not defeat the business's P.L. 86-272 immunity because it does not constitute a business activity within the customers' state.

2. The business regularly provides post-sale assistance to in-state customers via either electronic chat or email that customers initiate by clicking on an icon on the business's website. For example, the business regularly advises customers on how to use products after they have been delivered. This in-state business activity defeats the business's P.L. 86-272 immunity in states where the customers are located because it does not constitute, and is not entirely ancillary to, the in-state solicitation of orders for sales of tangible personal property.

3. The business solicits and receives on-line applications for its branded credit card via the business's website. The issued cards will generate interest income and fees for the business. This in-state business activity defeats the business's P.L. 86-272 immunity in states where the on-line application for cards is available to customers because it does not constitute, and is not entirely ancillary to, the in-state solicitation of orders for sales of tangible personal property.

4. The business's website invites viewers in a customer's state to apply for non-sales positions with the business. The website enables viewers to fill out and submit an electronic application, as well as to upload a cover letter and resume. This in-state business activity defeats

the business's P.L. 86-272 immunity in the customer's state because it does not constitute, and is not entirely ancillary to, the in-state solicitation of orders for sales of tangible personal property.

5. The business places Internet "cookies" onto the computers or other electronic devices of in-state customers. These cookies gather customer search information that will be used to adjust production schedules and inventory amounts, develop new products, or identify new items to offer for sale. This in-state business activity defeats the business's P.L. 86-272 immunity because it does not constitute, and is not entirely ancillary to, the in-state solicitation of orders for sales of tangible personal property.

6. The business places Internet "cookies" onto the computers or other devices of in-state customers. These cookies gather customer information that is only used for purposes entirely ancillary to the solicitation of orders for tangible personal property, such as: to remember items that customers have placed in their shopping cart during a current web session, to store personal information customers have provided to avoid the need for the customers to re-input the information when they return to the seller's website, and to remind customers what products they have considered during previous sessions. The cookies perform no other function, and these are the only types of cookies delivered by the business to its customers' computers or other devices. This in-state business activity does not defeat the business's P.L. 86-272 immunity because it is entirely ancillary to the in-state solicitation of orders for sales of tangible personal property.

7. The business remotely fixes or upgrades products previously purchased by its in-state customers by transmitting code or other electronic instructions to those products via the Internet. This in-state business activity defeats the business's P.L. 86-272 immunity because it does not constitute, and is not entirely ancillary to, the in-state solicitation of orders for sales of tangible personal property.

8. The business offers and sells extended warranty plans via its website to in-state customers who purchase the business's products. Selling, or offering to sell, a service that is not entirely ancillary to the solicitation of orders for sales of tangible personal property, such as an extended warranty plan, defeats the business's P.L. 86-272 immunity—*see* Article I.

9. The business contracts with a marketplace facilitator that facilitates the sale of the business's products on the facilitator's on-line marketplace. The marketplace facilitator maintains inventory, including some of the business's products, at fulfillment centers in various states where the business's customers are located. This maintenance of the business's products defeats the business's P.L. 86-272 immunity in those states where the fulfillment centers are located—*see* Article V.

10. The business contracts with in-state customers to stream videos and music to electronic devices for a charge. This in-state business activity defeats the business's P.L. 86-272 immunity because streaming does not constitute the sale of tangible personal property for purposes of P.L. 86-272—*see* Article I.

11. The business offers for sale only items of tangible personal property on its website. The website enables customers to search for items, read product descriptions, select items for purchase, choose among delivery options, and pay for the items. The business does not engage in

any in-state business activities that are not described in this example, such as the activities described in examples 2-5 and 7-10 above. This business activity does not defeat the business's P.L. 86-272 immunity because the business engages exclusively in in-state activities that either constitute solicitation of orders for sales of tangible personal property or are entirely ancillary to solicitation.

V. INDEPENDENT CONTRACTORS

P.L. 86-272 provides protection to certain in-state activities if conducted by an independent contractor that would not be afforded if performed by the business or its employees or other representatives. Independent contractors may engage in the following limited activities in the state without the business's loss of immunity:

1. Soliciting sales.

2. Making sales.

3. Maintaining an office.

Sales representatives and others who represent a single principal are not considered to be independent contractors.

Maintenance of a stock of goods in the state by the independent contractor under consignment or any other type of arrangement with the business, except for purposes of display and solicitation, removes the protection.

Performance of unprotected activities by an independent contractor on behalf of a seller, such as performing warranty work or accepting returns of products, also removes the statutory protection.

VI. APPLICATION OF DESTINATION STATE LAW IN CASE OF CONFLICT

When it appears that two or more Supporting States have included or will include the same receipts from a sale in their respective receipts factor numerators, at the written request of the business, these states will confer with one another in good faith to determine which state should be assigned the receipts. Such conference will identify what law, regulation or written guideline, if any, has been adopted in the destination state with respect to the issue. The destination state is the state in which the purchaser or its designee actually receives the property, regardless of f.o.b. point or other conditions of sale.

In determining which state is to receive the assignment of the receipts at issue, preference is given to any clearly applicable law, regulation or written guideline that has been adopted by the destination state. However, except in the case of the definition of what constitutes "tangible personal property," a Supporting State is not required by this Statement to follow any other state's

(including the destination state's) law, regulation or written guideline if it determines that to do so (i) would conflict with its own laws, regulations, or written guidelines and (ii) would not clearly reflect the income-producing activity of the business within its borders.

Notwithstanding any provision set forth in this Statement to the contrary, each Supporting State will apply the destination state's definition of "tangible personal property" to determine the application of P.L. 86-272 as it relates to the origin state's throwback rule, if any. If the destination state lacks a definition that would enable a determination of whether the sale in question is a sale of "tangible personal property," then each state may treat the sale in any manner that would clearly reflect the income-producing activity of the business within its borders.

VII. MISCELLANEOUS PRACTICES

A. Application of Statement to Foreign Commerce.

Congress explicitly applied P.L. 86-272 only to "interstate commerce." Therefore, by its terms, the statute does not apply to foreign commerce. *See Border Pipe Line Co. v. Fed. Power Comm'n*, 171 F.2d 149 (D.C. Cir. 1948) (explaining that Congress may choose to protect or regulate interstate but not foreign commerce). States, however, may elect to apply P.L. 86-272 in the context of foreign commerce. If a Supporting State applies P.L. 86-272 in the context of foreign commerce, it will do so consistently whether it is determining if activities of a foreign seller are protected or whether it is determining if sales into the foreign jurisdiction will be thrown back.

B. Application to Corporation Incorporated in State or to Person Resident or Domiciled in State.

The protection afforded by P.L. 86-272 does not apply to a corporation incorporated under the laws of the taxing state or to a person who is a resident of or domiciled in the taxing state.

C. Registration or Qualification to do Business.

Merely registering or qualifying to do business within a state, without more, will not forfeit the protection that may otherwise apply under P.L. 86-272 in that state. Seeking to use or protect any additional benefit under state law through engaging in other activity not protected under P.L. 86-272 (such as protecting a trade secret or corporate name) will forfeit the protection.

D. Loss of Protection for Conducting Unprotected Activity During Part of Tax Year.

The protection afforded by P.L. 86-272 is determined on a tax year by tax year basis. Therefore, if at any time during a tax year a business conducts activities that are not protected under P.L 86-272, the business will not be considered protected under P.L. 86-272 for the entirety of that year.

Addendum I - Public Law 86-272

••• §381. Imposition of net income tax.

(a) Minimum Standards.

No state or political subdivision thereof, shall have power to impose, for any taxable year ending after September 14, 1959, a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either, or both, of the following:

(1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection and, if approved, are filled by shipment or delivery from a point outside the State; and

(2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1).

(b) Domestic corporations; persons domiciled in or residents of a State.

The provisions of subsection (a) of this section shall not apply to the imposition of a net income tax by any State, or political subdivision thereof, with respect to ----

(1) any corporation which is incorporated under the laws of such State; or

(2) any individual who, under the laws of such State, is domiciled in, or a resident, of such State.

(c) Sales or solicitation of orders for sales by independent contractors .

For purposes of subsection (a) of this section, a person shall not be considered to have engaged in business activities within a State during any taxable year merely by reason of sales in such State, or the solicitation of orders for sales in such State, of tangible personal property on behalf of such person by one or more independent contractors, or by reason of the maintenance of an office in such State by one or more independent contractors whose activities on behalf of such person in such State consist solely of making sales, or soliciting orders for sales, of tangible personal property.

(d) Definitions.

For purposes of this section ----

(1) the term "independent contractor" means a commission agent, broker, or other independent contractor who is engaged in selling, or soliciting orders for the sale of, tangible personal property for more than one principle and who holds himself out as such in the regular course of his business activities; and

(2) the term "representative" does not include an independent contractor.

••• §382. Assessment of net income taxes; limitations; collection.

(a) No State, or political subdivision thereof, shall have power to assess, after September 14, 1959, any net income tax which was imposed by such State or political subdivision, as the case may be, for any taxable year ending on or before such date, on the income derived within such State by any person from interstate commerce, if the imposition of such tax for a taxable year ending after such date is prohibited by section 381 of this title.

(b) the provisions of subsection (a) of this section shall not be construed ----

(1) to invalidate the collection, on or before September 14, 1959, of any net income tax imposed for a taxable year ending on or before such date, or

(2) to prohibit the collection, after September 14, 1959, of any net income tax which was assessed on or before such date for a taxable year ending on or before such date.

••• §383. Definition.

For purpose of this chapter, the term "net income tax" means any tax imposed on, or measured by, net income.

••• §384. Separability of provisions.

If any provision of this chapter or the application of such provision to any person or circumstance is held invalid, the remainder of this chapter or the application of such provision to persons or circumstances other than those to which it is held invalid, shall not be affected thereby.

Addendum II – MTC Factor Presence Nexus Standard for Business Activity Taxes

Approved by the Multistate Tax Commission October 17, 2002

A. (1) Individuals who are residents or domiciliaries of this State and business entities that are organized or commercially domiciled in this State have substantial nexus with this State.

(2) Nonresident individuals and business entities organized outside the State that are doing business in this State have substantial nexus and are subject to [list appropriate business activity taxes for the state, with statutory citations] when in any tax period the property, payroll or sales of the individual or business in the State, as they are defined below in Subsection C, exceeds the thresholds set forth in Subsection B.

B. (1) Substantial nexus is established if any of the following thresholds is exceeded during the tax period:

(a) a dollar amount of $50,000 of property; or

(b) a dollar amount of $50,000 of payroll; or

(c) a dollar amount of $500,000 of sales; or

(d) twenty-five percent of total property, total payroll or total sales.

(2) At the end of each year, the [tax administrator] shall review the cumulative percentage change in the consumer price index. The [tax administrator] shall adjust the thresholds set forth in paragraph (1) if the consumer price index has changed by 5% or more since January 1, 2003, or since the date that the thresholds were last adjusted under this subsection. The thresholds shall be adjusted to reflect that cumulative percentage change in the consumer price index. The adjusted thresholds shall be rounded to the nearest $1,000. As used in this subsection, "consumer price index" means the Consumer Price Index for All Urban Consumers (CPI-U) available from the Bureau of Labor Statistics of the United States Department of Labor. Any adjustment shall apply to tax periods that begin after the adjustment is made.

C. Property, payroll and sales are defined as follows:

(1) Property counting toward the threshold is the average value of the taxpayer's real property and tangible personal property owned or rented and used in this State during the tax period. Property owned by the taxpayer is valued at its original cost basis. Property rented by the taxpayer is valued at eight times the net annual rental rate. Net annual rental rate is the annual rental rate paid by the taxpayer less any annual rental rate received by the taxpayer from sub-rentals. The

average value of property shall be determined by averaging the values at the beginning and ending of the tax period; but the tax administrator may require the averaging of monthly values during the tax period if reasonably required to reflect properly the average value of the taxpayer's property.

(2) Payroll counting toward the threshold is the total amount paid by the taxpayer for compensation in this State during the tax period. Compensation means wages, salaries, commissions and any other form of remuneration paid to employees and defined as gross income under Internal Revenue Code § 61. Compensation is paid in this State if (a) the individual's service is performed entirely within the State; (b) the individual's service is performed both within and without the State, but the service performed without the State is incidental to the individual's service within the State; or (c) some of the service is performed in the State and (1) the base of operations or, if there is no base of operations, the place from which the service is directed or controlled is in the State, or (2) the base of operations or the place from which the service is directed or controlled is not in any State in which some part of the service is performed, but the individual's residence is in this State.

(3) Sales counting toward the threshold include the total dollar value of the taxpayer's gross receipts, including receipts from entities that are part of a commonly owned enterprise as defined in D(2) of which the taxpayer is a member, from

(a) the sale, lease or license of real property located in this State;

(b) the lease or license of tangible personal property located in this State;

(c) the sale of tangible personal property received in this State as indicated by receipt at a business location of the seller in this State or by instructions, known to the seller, for delivery or shipment to a purchaser (or to another at the direction of the purchaser) in this State; and

(d) The sale, lease or license of services, intangibles, and digital products for primary use by a purchaser known to the seller to be in this State. If the seller knows that a service, intangible, or digital product will be used in multiple States because of separate charges levied for, or measured by, the use at different locations, because of other contractual provisions measuring use, or because of other information provided to the seller, the seller shall apportion the receipts according to usage in each State.

(e) If the seller does not know where a service, intangible, or digital product will be used or where a tangible will be received, the receipts shall count toward the threshold of the State indicated by an address for the purchaser that is available from the business records of the seller maintained in the ordinary course of business when such use does not constitute bad faith. If that is not known, then the receipts shall count toward the threshold of the State indicated by an address for the purchaser that is obtained during the consummation of the sale, including the address of the purchaser's payment instrument, if no other address is available, when the use of this address does not constitute bad faith.

(4) Notwithstanding the other provisions of this Subsection C, for a taxpayer subject to the special apportionment methods under [Multistate Tax Commission Regulations IV.18.(d) through (j)], the property, payroll and sales for measuring against the nexus thresholds shall be defined as they are for apportionment purposes under those regulations. Financial institutions subject to an apportioned income or franchise tax shall determine property, payroll and sales for nexus threshold purposes the same as for apportionment purposes under the [MTC Recommended Formula for the Apportionment and Allocation of Net Income of Financial Institutions]. Pass-through entities, including, but not limited to, partnerships, limited liability companies, S corporations, and trusts, shall determine threshold amounts at the entity level. If property, payroll or sales of an entity in this State exceeds the nexus threshold, members, partners, owners, shareholders or beneficiaries of that pass-through entity are subject to tax on the portion of income earned in this State and passed through to them.

D. (1) Entities that are part of a commonly owned enterprise shall determine whether they meet the threshold for nexus as follows:

(a) Commonly owned enterprises shall first aggregate the property, payroll and sales of their entities that have a minimum presence in this State of $5000 of combined property, payroll and sales, including those entities that independently exceed a threshold and separately have nexus. The aggregate number shall be reduced based on detailed disclosure of any intercompany transactions where inclusion would result in one State's double counting assets or revenue. If that aggregation of property, payroll and sales meets any threshold in Subsection B,
the enterprise shall file a joint information return as specified by the [tax agency] separately listing the property, payroll and sales in this State of each entity.

(b) Those entities of the commonly owned enterprise that are listed in the joint information return and that are also part of a unitary business grouping conducting business in this State shall then aggregate the property, payroll and sales of each such unitary business grouping on the joint information return. The aggregate number shall be reduced based on detailed disclosure of any intercompany transactions where inclusion would result in one State's double counting assets or revenue. The entities shall base the unitary business groupings on the unitary combined report filed in this State. If no unitary combined report is required in this State, then the taxpayer shall use the unitary business groupings the taxpayer most commonly reports in States that require combined returns.

(c) If the aggregate property, payroll or sales in this State of the entities of any unitary business of the enterprise meets a threshold in Subsection B, then each entity that is part of that unitary business is deemed to have nexus and shall file and pay income or franchise tax as required by law.

(2) "Commonly owned enterprise" means a group of entities under common control either through a common parent that owns, or constructively owns, more than 50 percent of the voting power of the outstanding stock or ownership interests or through five or fewer individuals (individuals, estates or trusts) that own, or constructively own, more than 50 percent of the voting

power of the outstanding stock or ownership interests taking into account the ownership interest of each such person only to the extent such ownership is identical with respect to each such entity.

E. A State without jurisdiction to impose tax on or measured by net income on a particular taxpayer because that taxpayer comes within the protection of Public Law 86-272 (15 U.S.C. § 381) does not gain jurisdiction to impose such a tax even if the taxpayer's property, payroll or sales in the State exceeds a threshold in Subsection B. Public Law 86-272 preempts the state's authority to tax and will therefore cause sales of each protected taxpayer to customers in the State to be thrown back to those sending States that require throwback. If Congress repeals the application of Public Law 86-272 to this State, an out-of-state business shall not have substantial nexus in this State unless its property, payroll or sales exceeds a threshold in this provision.

Prepared for: Charles Potter

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California's E-Commerce Tax Expansion Vexes Small Online Sellers

By Laura Mahoney and Michael J. Bologna
March 7, 2022, 4:45 AM

- State has expanded income tax to internet-based activities
- Legal challenges likely, including on retroactive application

Bloomberg Law News 2022-05-10T15:45:23166-04:00
California's E-Commerce Tax Expansion Vexes Small Online Sellers

By Laura Mahoney and Michael J. Bologna 2022-03-07T04:45:55000-05:00

1. State has expanded income tax to internet-based activities
2. Legal challenges likely, including on retroactive application

California's recent decision to scoop tens of thousands of out-of-state online businesses onto its income tax rolls will likely spur other states to do the same, but not without courtroom battles over the state's legal rationale.

Guidance from the state's Franchise Tax Board mirrors an August 2021 statement from the Multistate Tax Commission reinterpreting a federal law that has largely shielded out-of-state retailers from state income taxes for more than 60 years.

The new interpretation, which applies retroactively, removes some of the protections for sellers that weave online support services into their e-commerce models. The guidance is expected to impact legions of sellers that previously had no income tax obligations in California. Compliance could prove challenging for the estimated 2.5 million online merchants operating in the U.S., particularly small- and medium-sized sellers.

"I just wish California and the MTC had thought about what they were doing and how destructive this could be," said Paul Rafelson, executive director and general counsel for the Online Merchants Guild, which represents small internet-based sellers. "It's like they don't understand the difference between Google and a kitchen table sales enterprise. If every other state starts doing this, we're done, we're toast."

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California's guidance is so expansive, it probably captures almost any e-commerce business with "a functional website," said Nikki Dobay, a California tax partner with Eversheds Sutherland LLP.

And while California is the first state to adopt the MTC's legal interpretation, Dobay said it won't be the last. Colorado, Illinois, Oregon, and Utah have previously said they were considering implementing some or all of the MTC statement.

"California's being out front on this will provide cover or make other states feel more comfortable about issuing similar guidance," she said.

To businesses, the change is a drastic expansion of corporate-tax authority. State tax administrators, however, say the MTC's interpretation and California's guidance are simply clarifications of existing law.

"This is not a change but an effort to apply a 60-year-old statute to modern facts," said Brian Hamer, MTC counsel and lead author of the commission's interpretation. "It is incumbent upon the states themselves to interpret that statute until the courts say otherwise."

Websites and Apps

The California guidance updates the state's approach to Public Law 86-272, a 1959 federal law that prohibits states and localities from imposing income taxes on out-of-state businesses if their only activity within the state is soliciting sales of tangible personal property.

California and the commission broadened the definition of "business activity" in a state, endorsing a general rule holding that businesses interacting with customers through a website or an app engage in a business activity within the customer's state. For instance, businesses would likely lose the protection of P.L. 86-272 if they offer remote repairs and product updates, provide electronic customer service chat functions, and monitor customer preferences through "cookies" placed on their computers.

Possible Triggers for E-Seller State Income Tax

The MTC describes 11 scenarios in which a seller's customer engagement would either preserve or defeat the protections in P.L. 86-272. Here are six.

Protected **Protection Lost**

Sells products from a static website and offers no ancillary services	Offers remote repair and product upgrades
Offers post-sale assistance through a list of frequently asked questions	Offers post-sale assistance through electronic chat
Places cookies on customers' computers for solicitation of sales	Places cookies on customers' computers to gather customer search data

Bloomberg Tax & Accounting

Source: Multistate Tax Commission

"In the decades since PL 86-272 was enacted, the way in which interstate business is conducted has changed significantly," the California tax board said in its guidance memo. "Congress, however, has neither created a federal mechanism to provide administrative guidance to taxpayers nor has it updated the statute to indicate how it applies to new business activities."

California relies on the U.S. Supreme Court's 2018 ruling in *South Dakota v. Wayfair, Inc.* as a vehicle for bringing remote businesses into the income tax code. The high court ruling, which permitted states to impose sales tax collection obligations on remote retailers based on economic activity instead of physical presence, has resulted in bonanzas for state coffers, especially in the pandemic years.

"Although the United States Supreme Court was not interpreting P.L. 86-272 in Wayfair, California considers the court's analysis as to virtual contacts to be relevant to the question of whether a seller is engaged in business activities in states where its customers are located for purposes of P.L. 86-272," the tax board says in the memo.

Depending on their structure, e-commerce businesses pulled into California's code could be subject to the 8.84% corporate income tax, the 6.65% alternative minimum tax, or the 1.5% franchise tax, which applies to pass-through businesses.

Cost and Complexity

The cost and complexity of compliance could multiply quickly for small businesses if California's posture extends to a bevy of new states, said Brad Scott, director of finance for Halstead Bead Inc., an online seller of jewelry supplies.

"With filing income and franchise taxes in other states—I'm not equipped to do that at all," said Scott, a frequent critic of tax compliance burdens on small businesses. "It becomes a financially difficult thing because we will have to pay our CPA to do it for us and then we'll have to pay the tax bill itself."

With customers in all 50 states, Halstead's duties could jump from four states to dozens, Scott said. The company already pays income tax in its home state of Arizona, but also pays California's franchise tax and Washington's Business & Occupation Tax. In addition, Halstead pays tax to Hawaii, which limited the scope of P.L. 86-272 protections in the Aloha State two years before the MTC's statement.

Ongoing Audits

California intends to apply the guidance retroactively to all open tax years, tax board spokesperson Angela Jones said. The California statute of limitations for income tax matters is four years, but that is often extended when a taxpayer is being audited.

The board's position could find its way into ongoing audits for past years, applying rules that are different from what taxpayers followed at the time they filed their tax returns, said Carl Joseph, principal in indirect state and local tax services at Ernst & Young LLP. Taxpayers have relied for many years on FTB Publication 1050, which still reflects the board's previous interpretation of what activities are protected under PL 86-272.

Jones said the tax board is in the process of updating Publication 1050.

"The question of retroactivity here really comes down to fair play," Joseph said. "If I'm a taxpayer and I've done everything I can to make sure that I am consistent with California's view of 86-272 and I read the Pub 1050 every year, I still have a problem because they've pulled the rug out from under me."

Jamie Yesnowitz, state and local tax practice and national tax office leader at Grant Thornton LLP, agreed.

"Companies won't really know what the policy is until they get audited for past periods and California might try to apply this position," Yesnowitz said.

Legal Challenges Likely

California's new posture and its commitment to retroactive application will likely be challenged as soon as the state starts issuing assessments. The American Catalog Mailers Association and the Direct Marketing Association have been critical of the commission's interpretation and are poised to challenge aggressive audits.

DMA counsel George S. Isaacson called California's posture a disingenuous interpretation of P.L. 86-272 designed to rob taxpayers of important protections guaranteed by Congress. Isaacson, who represented e-commerce sellers before the Supreme Court in *Wayfair*, also objected to California's creation of a legal rationale that he believes was never envisioned under the *Wayfair* precedent.

"California's reliance on the *Wayfair* decision is ill-placed," said Isaacson, a partner with Brann & Isaacson in Lewiston, Maine. "That decision neither referenced nor applied to P.L. 86-272. Indeed, to the contrary, the majority decision acknowledged the supremacy of congressional authority, when affirmatively exercised, to regulate commerce."

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Prepared for: Charles Potter

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New York Opens the Door for Income Tax on Internet Sales (1)

By Donna Borak and Michael J. Bologna
May 2, 2022, 11:01 AM; Updated: May 2, 2022, 3:02 PM

Bloomberg Law News 2022-05-10T15:46:18267-04:00
New York Opens the Door for Income Tax on Internet Sales (1)

By Donna Borak and Michael J. Bologna 2022-05-02T11:01:30000-04:00

New York is expanding the reach of its corporate income tax to thousands of additional online businesses, issuing a draft rule that peels back protections previously allowed under a federal law designed to shield out-of-state retailers from state taxes.

The state Department of Taxation said Friday that it planned to conform with August guidance from the Multistate Tax Commission that updated how states should rethink the federal law at a time when so much commerce happens online. The commission specified that orders for tangible personal property are the same whether the transaction occurs on the internet or in person.

The deadline to comment on the state's proposed changes under the Interstate Income Act, PB-86-272 is June 30.

New York would be the second state to conform to the MTC's legal interpretation of the federal law. In February, the California Franchise Tax Board, which oversees income and franchise tax for the state, released a technical memorandum revising how internet activities were taxed.

New York's effort to expand the scope of its corporate tax code is nearly identical to the approach described by the California tax board with one important difference, said Joe Huddleston, managing director of indirect tax at EY LLP and a former executive director of the MTC.

California issued its guidance as a technical advice memorandum, permitting the tax board to apply it retroactively. By issuing a regulation subject to the administrative review process and a public hearing, Huddleston said New York will avoid some legal controversies by acknowledging its program will be applied prospectively.

"I like the regulation process because it establishes a point in time where the issue of retroactivity is not a problem and it carries a little more weight," he said.

Dozens of other state revenue agencies are considering adopting the commission's new interpretation, which has protected out-of-state sellers for 60 years. Revenue officials in Colorado, Illinois, Oregon, and Utah have all weighed how to implement some or all of a 2020 MTC statement on the federal law to reflect the impact of e-commerce on the broader economy.

Other states could take similar action based on their having previously adopted the commission's principles through guidance and tax positions taken during audits.

The shift in state policies could have a major impact on the income tax obligations of more than 2 million online merchants operating in the U.S., according to tax practitioners.

(First paragraph modified, paragraphs 5, 6 and 7 added reflecting the views of Joe Huddleston.)

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Documents

Proposed Rule
New York guidance

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SALES TAX IN THE RESTAURANT INDUSTRY

RECORDKEEPING REQUIREMENTS

One of the most important jobs of an eating establishment is to keep good records. These businesses must maintain records for review by the Department of Revenue in accordance with Regulation 34.2 Keeping of Records. This regulation spells out that records must show the amount of tax separate from the total sales and that records must be maintained for each store or other outlet. It is required that these records (hardcopy or electronic format) be kept for the current year and the three previous calendar years.

Keeping detailed records of your business operation will help you prepare accurate and complete sales tax returns. Detailed records will also serve as documentation of the accuracy of your returns if you are audited. Such records should include:

TRANSACTIONAL SALES RECEIPTS

Transactional sales receipts simply record the details of a transaction at the point of sale. This includes items such as cash register tapes, guest checks, invoices, point of sale receipts, sales slips, written receipts, or any other original sales document. These receipts should include at minimum, the following information:

- Date
- Sequential receipt number
- Description of food and beverage sale
- Sales amount of each item sold
- Discounts and/or coupon amounts (if applicable)
- Total sale amount
- Separately stated sales tax
- Method of Payment

CREDIT CARD SLIPS

Credit card slips are generally not as detailed as a formal sales receipt, but they must still be maintained to help validate any credit sales accepted by the business.

VOIDED OR CANCELLED SALES

Any time a sale is voided or cancelled the transaction must be recorded.

EXEMPTION CERTIFICATES

Any time a sale is made to a registered charitable organization who is providing an exemption certificate, the exemption certificate must be kept on file for at least 4 years. This will validate why no tax was collected on a specific transaction.

BANK STATEMENTS

Bank statements should show any deposits from the eating establishment.

DAILY SALES REPORTS

Daily sales reports should summarize the total taxable sales, total nontaxable sales, total gross sales, and total sales tax collected. Total sales should also be divided as to cash sales and credit sales. These reports must reconcile to the transactional sales receipts for the day.

MONTHLY SALES REPORTS

Monthly sales reports should summarize the total taxable sales, total nontaxable sales, total gross sales, and total sales tax collected. Total sales should also be divided as to cash sales and credit sales. These reports must reconcile to the transactional sales receipts for the month.

MONTHLY MERCHANT STATEMENTS & 1099-K FORMS

Monthly merchant statements should show a detailed list of all electronic transactions that occurred during the month along with any processing fees that may be associated as well as the annual 1099-K forms.

MONTHLY STATEMENT FROM 3RD PARTY DELIVERY COMPANIES

If the eating establishment or caterer has a relationship with an online company such as Grub Hub, Door Dash, UberEATS, etc. they must maintain monthly statements from all third parties as well.

FEDERAL & STATE INCOME TAX RETURNS

Income tax returns are used for gross sales comparison and must be made available upon request.

pennsylvania
DEPARTMENT OF REVENUE
www.revenue.pa.gov

SALES TAX IN THE RESTAURANT INDUSTRY

WHAT IS TAXABLE?

The sale of food and non-alcoholic beverages by a caterer or eating establishment in Pennsylvania is subject to tax regardless of whether the customer is dining in or taking out. The Pennsylvania sales tax rate is 6 percent. By law, sales from eating establishments located in Allegheny County and Philadelphia County are subject to an additional sales tax rate of 1% and 2%, respectively.

An eating establishment is defined as a business, or an identifiable location within a business, which advertises or holds itself out to the public as being engaged in the sale of prepared or ready-to-eat food or beverages, to customers for their immediate consumption on or off the premises. An eating establishment may be mobile or immobile and may or may not provide seating accommodations for its customers.

An eating establishment includes, but is not limited to the following:

- Arenas
- Amusement parks
- Automats
- Bars (serving food)
- Cafes
- Cafeterias
- Carnivals
- Carry out shops
- Coffee Shops
- Dining Cars
- Employee cafeterias
- Fast food operations
- Fairs
- Food trucks
- Honor boxes
- Hotels
- Juice stands
- Lunch carts
- Lunch counters
- Night clubs
- Pizzerias
- Popcorn stands
- Private/social clubs
- Restaurants
- Stadiums
- Taverns
- Theaters

The following items are outlined in the law as tax exempt and therefore would not be subject to sales tax:

- **Alcoholic Beverages-** with the exception of PLCB licenses that include a Wine Expanded Permit. Wine Expanded Permit holders must charge sales tax on the sale of wine for off-premises consumption such as to-go orders.
- **Bottled Water-** as long as it contains no flavoring
- **Candy & Gum-** including hard candy, caramel, chocolate candy, licorice, fudge, cotton candy, caramel coated popcorn, chocolate coated granola bars and similar items.
- **Gift Cards-** gift cards are not subject to sales tax but tax is due on the ready to eat food or beverages purchased with a gift card.
- **Gratuities (tips)-** not taxable when separately stated on the customer's receipt, guest check, or sales invoice
- **Wearing apparel** such as t-shirts, hats, jackets, etc.

NOTE: Food and beverages billed to and paid for by a registered charitable organization which have a valid sales tax exemption number are also exempt from tax. These entities must provide an exemption certificate upon purchase that includes their "75" number. Food and beverages billed to and paid for by individuals on behalf of exempt organization are not entitled to the exemption.

DISCOUNTED FOOD ITEMS

Any on-spot discount such as store discount, employee discount, or coupon establishes a new purchase price as long as both the item being sold, and coupon are described on the invoice or register tape.

Example: A customer purchases two hamburgers with a "buy one, get one free" coupon and a bottle of unflavored water. The price of one hamburger is $2 and the bottled water is $1.00. The restaurant should ring up $5 on the cash register and enter a credit for the amount of $2 which would result in an adjusted price of $3. The acceptance of the BOGO Burger coupon by the restaurant along with the description of the item and coupon on the register receipt establishes a new taxable purchase price of $3 which is subject to 12 cents in tax.

RECEIPT	
Burger – T	$2.00
Burger – T	$2.00
Bottled Water - NT	$1.00
Subtotal	$5.00
Coupon	-$2.00
Total	$3.00
Sales Tax (6%)	$0.24
Amount Due	$3.24

RECEIPT	
Burger - T	$2.00
Burger - T	$2.00
Bottled Water – NT	$1.00
Subtotal	$5.00
BOGO Burger Coupon	-$2.00
Total	$3.00
Sales Tax (6%)	$0.12
Amount Due	$3.12

NOTE: If the restaurant does not describe the coupon on the register tape, but simply reduces the amount due then sales tax is due on the total amount of $4.

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PSCRIPT Page Separator

Letter Date 3/02/2022
Contact by phone 717-425-2495, ext 72251

SPORTS GRILLE AT CRANBERRY
1294 FREEDOM RD
CRANBERRY TWP PA 16066-4950

Dear Taxpayer,

The Department of Revenue is implementing a new approach to help businesses in the restaurant industry as they continue to work through the hardships caused by the COVID-19 pandemic. This two-fold approach is designed to first provide additional resources and guidance for the industry and secondly, to better utilize department resources and ease the burden on compliant businesses. Below is an overview.

1. Education and Outreach: The department has created industry specific guidance tailored for the restaurant industry, including tips that explain how to handle sales tax, recordkeeping, and other tax obligations. These resources are accessible at **revenue.pa.gov/restaurants**. They highlight common issues along with best practices to ensure you are in good standing at all times. Additionally, Revenue employees will be traveling to some Pennsylvania restaurants to go over these available resources and review any compliance issues that may exist. This approach is designed to provide assistance to all restaurants and additional outreach to those that may have outstanding issues with their tax accounts.

2. New Process for Audit: When a restaurant is selected for audit in 2022, the department will conduct a limited scope audit of a current month instead of the traditional three-year lookback if a restaurant meets certain requirements. To meet the requirements, a restaurant must have no missing tax returns or tax liabilities due, show proof of proper recordkeeping, filing of accurate tax returns, and proper remittance of taxes collected and withheld.

The Department of Revenue is implementing this new approach to provide as much customer service as possible to Pennsylvania restaurants. This also is a way to ensure that restaurant owners are operating on a level playing field.

In addition to the web page mentioned above, you can contact a department representative by calling (717) 425-2495, Ext. 72251 to receive help and answer any questions that you may have related to this outreach initiative.

Sincerely,

PA Department of Revenue

PICPA Annual Meeting

October 2021: Questions and Answers

We provide here a summary of answers provided by the Department of Revenue (DOR) from October 21, 2021. This presentation is classified as revenue information issued for informational purposes only for the convenience of PICPA's members. Pursuant to 61 PA. Code Section 3.4, this presentation should not be relied upon for any purpose or used in tax appeals. Taxpayers requiring a binding opinion on a specific situation may request a written letter ruling under 61 PA. Code Section 3.3.

1. **Is there a number to call at the department to ask for the status of a refund check from either BOA or BF&R? Using the online system can take nearly a month to receive an answer with back-and-forth correspondence as staff does not always understand how to reference docket numbers, and they get confused between BOA and BF&R (example question reference number 210820-000069). Pre-Covid, there used to be a number practitioners could call at the DOR, and the department could give a status of whether it was processed or not. We've been waiting on BOA and BF&R to refund checks at upwards of six months after decision this past year. If we could have the ability to check status with the DOR on a particular docket, that would be very helpful to our clients. Is this capability once again possible?**

If you have a question about a Board of Appeals decision or appeal rights to the Board of Finance and Revenue, you should call the direct dial of the examiner that is listed in the header of the decision of the Board of Appeals. Most refunds are processed with a turnaround time of 10 days. Please be advised that most refund checks will be mailed directly to the taxpayer or petitioner.

2. **The department plans to require taxpayers to sign an agreement to enter into a deferred payment plan that waives their right to appeal the assessment generating the amount due. When does the department envision using the form and does it plan to offer deferred payment plans and waivers in all collection cases?**

The appeal waiver letter is only required for taxpayers wishing to establish a Deferred Payment Plan (DPP) on balances that have not yet reached collections. To protect taxpayers from moving into a collections workflow, prior to their appellate rights expiring, the system will not allow dunning activity to occur, which includes the establishment of a DPP. The Appeal Waiver Letter allows us to bring the case into our workflow and set up the plan, and serves as record that the taxpayer acknowledged, the cessation of their appellate rights. As for when they envision using it, this is a form that we have used for many years. It is not required for cases that are already in collections (or outside of their appeal period).

3. **We've received a large volume of Schedule G/L and Schedule OC credit denials in the past nine months. Some go back to the 2017 tax year and others are blatantly incorrect. One example is the attached notice received denying an EITC. (See the copy of the submitted Rev-1123 submission.) The notice states that the Rev-1123 was filed late and the tax liability is not large enough to use the credit.**

The Bureau of Individual Taxes has been working remotely since the start of the pandemic in March of 2020, which posed some challenges with the review of the REV-1123 forms since these forms were mailed directly into our bureau, so they could be reviewed manually. They were not previously scanned like other correspondence our bureau reviews. Since the department didn't have staff working in the building, we were unable to review these forms until the department was authorized to return to the office. In October of 2020, all REV-1123 forms that were received in the Bureau of Individual Taxes were scanned so they could be processed. Although the REV-1123 form that was referenced in this example was stamped received by the department's Harrisburg District Office; the Bureau of Individual Taxes did not receive this form. The Tax Examiner that reviewed this taxpayer's return even referenced in the notes that he searched in multiple locations to see if the REV-1123 form could be located, in case it was

scanned in as general correspondence in error. The example in question was adjusted in September, after the bureau received a copy of the REV-1123.

Since we continue to work remotely the REV-1123 forms are now scanned upon receipt and the department now offers an email resource account where the REV-1123 forms can be emailed in lieu of mailing them. That email address is REV1123@pa.gov. This question also referenced that a large volume of Schedule G/L credits were denied in the past nine months. The bureau would appreciate examples so we can research them further.

4. **For other notices, the department is not following the Office of Chief Counsel's policy (see PICPA/DOR Q&A 10-19-2016 question #5) regarding use of resident credits that are from distributed income of an irrevocable trust that is grantor in the other state. We've attempted to resolve notices via DOR's online customer service, but during 2021, the help desk response is often, "you must file with Board of Appeals," and no administrative attention is given (example question reference number 210826-000022). Filing at the Board of Appeals can be costly for taxpayers. Most of the notices are relatively small dollars and don't warrant hiring a professional to take on the appeal process for them. For Schedule G/L and Schedule OC notices that are sent in error or that can be easily resolved, what is the best approach to garner administrative attention to a practitioner's response to a notice?**

The department is administering this accurately; however, in this particular instance an employee incorrectly adjusted the return. The Bureau of Individual Taxes does review correspondence in response to adjustments that were made. The only time we will not is if an assessment notice was issued. Once an assessment is issued, the taxpayer must file a petition with the Board of Appeals. The example in question did not result in an assessment; so, a manager has reviewed the return again and made the appropriate adjustments.

As discussed during the meeting, if a taxpayer disagrees with a notice, we encourage them to submit the correspondence via myPaTH so the information will post quickly and accurately to our system. Below is the list where they can send the info if they choose not to use myPaTH. Once an assessment is issued, the taxpayer must file an appeal through BOA.

Processed Return Notices: Adjustment Summary, Application of Credit Notice, Billing Notice
PA Department of Revenue
Bureau of Individual Taxes
PO BOX 280431
Harrisburg, PA 17128-0431
Fax (717) 705-6236

ID Validation Notices
PA Department of Revenue
Bureau of Individual Taxes
Fraud Detection and Analysis Unit
PO Box 280607
Harrisburg, PA 17128
Fax (717) 705-4614

Request for Information Notices
PA Department of Revenue
Bureau of Individual Taxes
PO BOX 280501
Harrisburg, PA 17128-0501
Email: RA-BITPITHOLDCORFAXE@pa.gov

5. **Refund checks issued by the department typically do not include information concerning the reason for the payment. Would it be possible to include a statement that discloses the tax type, tax period, and breakdown of tax versus interest components? If it is not feasible to include this with the physical checks, could it be posted to the taxpayer's account for online access?**

PICPA Annual Meeting

October 2021: Questions and Answers

Currently, the only information provided on the refund checks will be the tax type. A statement cannot be included with the refund checks, so a separate letter would need to be created and mailed to the taxpayer to provide the requested information; however, it would not be guaranteed that the letter would arrive prior to the refund check.

6. **Please provide an update on regulatory projects, including the status of CNIT apportionment of services, nonbusiness income and realty transfer tax. What other topics are on the department's agenda for policy bulletin or regulatory updates?**

- The Governor's Semi-Annual Regulatory Agenda appeared in the Saturday, August 14th edition of the Pennsylvania Bulletin.
- The promulgation date for the RTT amendment in that bulletin was September 2021, as proposed. We are looking at a new date.
- The promulgation date for the CNIT apportionment regulation was September 2021, as proposed. We are looking at a new date.
- The promulgation date for the CNIT NBI regulation is October 2021.

So far in 2021, the department has published 4 sales and use tax (non-medical masks and face coverings, energy drinks, remote help supply services, and waste transportation and the public utility exclusion). The department has also published an OTP bulletin (RYO clubs), Corporation Tax Bulletin (Telecommunications GRT Remote Entities), Medical Marijuana (clinical registrants), and several restricted tax credit bulletins (application and sale, limited carryforward)

7. **In response to prior Q&A, the department has previously indicated that cancellation of debt income that is excluded from income federally under IRC Sec. 108 does not require the reduction of Pennsylvania NOLs. Sec. 108 may also require the reduction of the tax basis of assets for federal purposes. Is there any difference in the basis reduction for Pennsylvania purposes?**

There is no statutory authority to adjust Federal taxable income for this item in computing Pennsylvania taxable income.

8. **If a corporation believes it does not have nexus pursuant to PL 86-272, is it required to file Form RCT-101? If the form is required, what information must be included in support of the "no nexus" claim? If a corporation does file the RCT-101 and discloses its position as to PL 86-272 (or other situation involving a "no nexus" position), does the return start the running of the statute of limitations for audits and assessments?**

A taxpayer who believes it does not have nexus pursuant to P.L. 86-272 should file a RCT-101 with a completed REV-986 included along with any additional statements the taxpayer feels are necessary to appropriately explain its position. Regardless of whether Form REV-986 is completed or a statement claiming protection under PL 86-272 is attached to the RCT-101, it is the longstanding position of the Department that no statute of limitations is commenced unless an RCT-101 is filed reporting all required information necessary for the calculation of CNIT, even if no CNIT is actually due based on the protections afforded under P.L. 86-272.

9. **Our understanding is that the online PA-100 does not include an option to designate corporation tax subjectivity and that the Department generally creates corporate accounts based on Secretary of State registrations by corporations. Please describe the process for a taxpayer to receive a PA ID and open a corporate tax account when the entity is not required to be registered with the PA**

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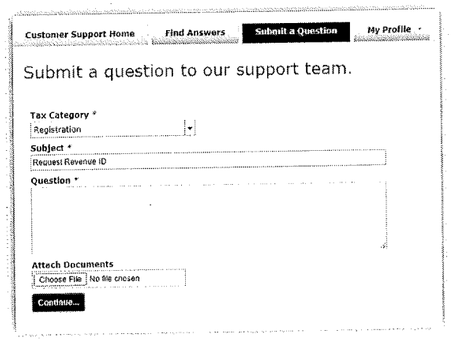
October 2021: Questions and Answers

Secretary of State's office or the entity is a Limited Liability Company or other non-corporate entity that elects to be classified as a corporation for federal (and thus PA CNIT) purposes.

For a taxpayer who has registered with the Department of State and has not received their expected Revenue ID or to receive a Revenue ID and open a corporate tax account when the entity is not required to be registered with the Department of State or the entity is a Limited Liability Company or other non-corporate entity that elects to be classified as a corporation for federal (and thus PA CNIT) purposes a Revenue ID may be requested. To request a Revenue ID for corporate tax account(s), visit our website at https://revenue-pa.custhelp.com and use the "Submit a Question" button. Once a user account is created or an existing user is logged in, use the Tax Category "Registration" to make your request for a Revenue ID. Taxpayer's making a request will receive a short request form asking a few basic questions to assist us with finding the DOS records for the requesting entity or the reason for the request and the corporation tax type(s) needed.



10. Is the following an accurate representation by the Department for withholding treatment under the "convenience of employer" rules for PA? Is a "cyber employee" different than a "remote employee"? A client reached out to the Department and received the following responses:

Initial question:
Per employer withholding for nonresidents who do not live in reciprocal states: Individuals will continue to be employees of Company A, located in PA, and for internal purposes, be assigned to one of Company A's PA offices. EX: Employee moving to Texas, will be working from home. While Texas does not have a state income tax, is any of their compensation subject to PA state tax withholding when all their work will be done in Texas? Does PA actually have what is called a "convenience rule" when it comes to employer withholding?

Initial DOR answer:
The employee would be considered a cyber employee. Cyber employees are considered to be working from the location of their computer ONLY when they have an agreement or letter from the employer that says the work is to be performed at the employee's location and not the employer's location. If there is no letter or employment agreement that states where the work is performed, the compensation is considered to be PA compensation, and PA state tax should be withheld by the employer. The employee should file a PA-40 personal income tax return as a nonresident to report the compensation as taxable to PA.

Follow-up question:
Does the Department's response apply to any state where PA does not have a reciprocal agreement? Does the employer need to submit the letter or agreement somewhere, other than to the employee? Does the employee who receives the letter or agreement need to submit it somewhere?

DOR follow-up response:
The response applies to any state that does not have a reciprocal agreement with Pennsylvania. It is not necessary as the employer to submit the letter to the Department. If PA state tax is taken out in error, the employee would need to submit a copy of the letter with the PA-40 tax return to obtain a refund of the withholding.

The department is working on additional guidance for the convenience of employer effect on PIT.

PICPA Annual Meeting

October 2021: Questions and Answers

11. If an s corporation does not report the composite taxes it paid on behalf of the PA shareholders on the "resident credit" line of the PA 20S, are there any issues with the resident shareholders claiming the taxes paid as long as they submit copies of the state returns?

Ideally, the shareholder should have an RK-1 reporting the shareholder's amount of resident credit along with a statement providing the information necessary to complete Schedule G/L. If the shareholder cannot get the S corporation to provide the RK-1 with the resident credit and the supporting statement, the shareholder can report the resident credit and attach copies of the state composite returns. Note the department has the right to request any additional documentation at a later date to support the amount of the credit.

12. The department is not recognizing the assignment of credit forms from pass through entities. The department and taxpayers are both wasting their time responding to the notices that the entities have not completed the paperwork when we know it has in fact been submitted. How can this situation be rectified?

Please provide specific examples where the department did not recognize the assignment of credit forms so that we can further research to determine what happened.

13. We've had the Department adjust overpayment amounts on several 2020 PA-40's. Rather than following the amounts entered on lines 30 (refund) and 31 (credit to 2021), DOR arbitrarily changed the refund amount, altering the expected amount to be credited to tax year 2021. What is the reason this would have been carried out?

Please provided specific examples of accounts where this scenario occurred, so that we may further research to provide a response as to what may have occurred. In general, any time an adjustment to an overpayment is made, a notice providing a reason for the adjustment as well as the amount of the adjustment, should be issued by the department.

14. 72 Pa. Stat. § 8102-C.5(a)(1) applies a limitation stating that a real estate company becomes acquired upon a change in the ownership of the company only if the change in the ownership interest "does not affect the continuity of the company." Neither the statute nor its regulations define this phrase. Could the Department provide some general guidance or examples where this limitation would apply?

Continuity means "continuity of life." Unlike an individual that can die, many entities (corporations, LLCs, etc.) can continue to exist beyond the death of an owner or can survive a change of ownership.

The statutory language means that if the entity continues to exist after a change of ownership, the entity can become acquired. However, if a change of ownership would cause an entity to disappear or end, then the continuity of the entity would be affected.

Because the tax is imposed upon the entity when it becomes acquired, it stands to reason that the entity still has to be there after the acquisition for it to be able to pay the tax. The most common situation may be when a change of ownership may affect the continuity of a company is if the change of ownership happens in combination with a merger and the merger causes the real estate company to end.

15. What is the timing of the release of proposed regulations on: market-based sourcing, realty transfer tax, nonbusiness income, and any other topics?

PICPA Annual Meeting

October 2021: Questions and Answers

- The Governor's Semi-Annual Regulatory Agenda appeared in the Saturday, August 14th edition of the Pennsylvania Bulletin.
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- The promulgation date for the CNIT apportionment regulation was September 2021, as proposed. We are looking at a new date.
- The promulgation date for the CNIT NBI regulation is October 2021.

16. Can the department provide current developments on a pilot program mentioned by Amy Gill, Policy Director in a 2020 meeting. The concept was that certain selected taxpayers would work with the department to self-audit transactions and ascertain that proper PA sales and use tax was remitted. The program may have been directed at larger taxpayers (those that remit over $XX per month to the DOR). Pursuant to such a program a taxpayer could make sure it is meeting its PA sales tax obligations for sales and use tax. While there is no promise of a reduction in future audits, the hope is that a taxpayer's voluntary participation in this program could be taken into consideration.

Could the department comment on whether PA would ever consider something similar to a "managed audit" program like one operational in Texas. Texas' managed audit program allows for the waiver of penalty and interest for successful participants. The purpose of the program is to save the state audit manpower hours and bring in tax dollars. Details of the TX program are at https://comptroller.texas.gov/taxes/audit/managed.php.

I believe you are referencing our Business Activity Review Pilot Program which is initially focused on construction contractors due to the complex nature of their compliance obligations. The department launched this customer service outreach program to help businesses in December 2020. The program involves experienced sales tax personnel from the Department of Revenue meeting with Pennsylvania business owners to help them understand how their business is impacted by the sales and use tax laws and regulations in Pennsylvania. We initially mailed letters to contractors throughout the state and are planning follow-up through e-tides email correspondence to remind them of the opportunity. Fourteen businesses have participated with each review taking about 15 hours. While participation rates are low, the feedback from those participating has been very good. We are considering what other industry or business segments may benefit and what the next steps are for this program.

As you point out, participation does not result in any increased chance of a future audit. The program is currently available to taxpayers that have not been contacted by the Department for an audit. Additional information about the program is available at www.revenue.pa.gov/COVID19/ReliefForTaxpayers/SUTHelp/.

Regarding managed audits, the department has worked with taxpayers and practitioners through the years at their request to do managed audits. This has been limited to circumstances where we anticipated some efficiency gains over a traditional audit. Taxpayers that participate in a managed audit and meet the mutually established timelines may be granted penalty abatement. The department does not however have the authority to abate interest. We continue to evaluate how a more formal program would benefit taxpayers and the department as this has produced mixed results in terms of whether it saves time or is more efficient for the department or the taxpayer. Of particular concern has been those situations when an entity has a business exemption where the complexity and challenges of making the appropriate determinations has not led to any measurable time savings or efficiency gains. Taxpayers interested in pursuing a managed audit may discuss that approach with the auditor assigned to complete the audit when the audit begins.

PICPA Annual Meeting

October 2021: Questions and Answers

17. Tax Credits - The KOZ Act sources payroll to the KOZ for credit apportionment purposes if some of the services are performed in the KOZ and the base of operations is in the KOZ. With the spread of hybrid work arrangements, how does the Department determine the base of operations for these purposes, and consequently the sourcing of payroll for KOZ apportionment purposes?

After the "End Date," specific costs (e.g., employee wages, research and development expenses) must be sourced to the commonwealth or a defined location within the commonwealth. For example, if a taxpayer participates in the Research and Development Tax Credit program and pays an employee working remotely from a location outside the commonwealth to conduct research, the employee's wages will no longer qualify as a qualified research and development expense as of the "End Date." Similarly, as an example for the zone programs, if a qualified business is located in a Keystone Opportunity Zone and pays an employee working 51% or more of the time remotely from a location outside the Zone, the employee's wages will no longer be sourced to the zone as of the "End Date."

18. Historically, the Pa. R&D credit was awarded in Dec. Therefore, the credit was taken in that tax year (12/15/20 award toward the 2020 tax return). Now the award letter will arrive in May. For the award letter coming in May 2022, which year should it be used in? The 2021- or 2022-income tax return?

The effective date of the credit will be 12/1/2021. To directly answer your question, it will be awarded toward the 2021 tax return.

19. Can the department clarify the appropriate reporting for Shuttered Venue Operations Grants (SVOG) for PA income tax purposes? This would be for S Corps, C Corps and Partnerships.

Grants are generally not taxable unless they would fall withing one of the taxable classes of income, but that has to be determined on a case-by-case basis. In reviewing the SVOG particulars, the department has decided it is not taxable.

I. PENNSYLVANIA PERSONAL INCOME TAX

A. Structure of Tax

1. Decoupled from the federal income tax system

2. Separate Classes of income worth no offsets between classes

3. It is possible to argue that many items of income taxable for federal purposes are not taxable for Pennsylvania purposes

(a) alimony

(b) arbitration awards

(c) annuities

B. Sources of Authority

1. Statute

2. Regulations

3. Rulings

4. PIT Guide

C. Dispute Resolution

1. Correspondence

2. Rulings

3. Appeals Process - New Policy at the Board of Appeals (Tax Bulletin 2011-02)

4. Voluntary Disclosure

5. Amended Returns (New Rules)

6. New Amnesty Program

7. New Policies at Board of Finance & Revenue

II. TOPICS OF CURRENT INTEREST

A. Deduction of Intangible Drilling Costs. See Section 7303 (a.2) of the tax reform code, Chapter 23, PIT Guide, Staley 344 A2d 748 (1975) Act 52 Changes, and Bulletin 2013-04 and (Schedule I)

B. Deb Forgiveness Income. Wirth 82 MAP 2012 (6-17-14)

C. Section 1031 Exchanges (Pearlstein 741-743 FR 2017)

pennsylvania
DEPARTMENT OF REVENUE

CORPORATION TAX BULLETIN 2022-01

Issued: February 17, 2022

Split-Factor Apportionment

The purpose of this bulletin is to provide guidance on the proper apportionment of income by a taxpayer involved in both an activity subject to one or more of the special apportionment formulas under 72 P.S. § 7401(3)2.(b)-(e), as well as separate activities subject to standard single sales factor apportionment under 72 P.S. § 7401(3)2.(a)(15)-(17).

This issue was previously addressed by the Commonwealth Court in the matter of *Buckeye Pipeline Co. v. Commonwealth.*[1] In that case the taxpayer requested the use of pipeline apportionment to apportion all of its income. The Commonwealth countered that the taxpayer was a management company because 98.6% of its gross receipts were derived from management activities and only 1.4% of its gross receipts were derived from pipeline activities. In the alternative, the Commonwealth argued that the taxpayer was entitled to an apportionment methodology whereby the taxpayer's taxable income was subject to "split apportionment" according to the proportion of gross receipts derived from the transportation of liquid property compared to the proportion of gross receipts derived from management activities.

The Commonwealth Court ultimately adopted the Commonwealth's split apportionment methodology wherein it stated:

> The Commonwealth concedes in its brief that applying the three-factor method of apportionment to all of Buckeye's receipts would not fairly represent Buckeye's business activity in Pennsylvania. Based on this provision, the revenue barrel mile method of apportionment should apply to the 1.4% of Buckeye's receipts that derive from transporting petroleum products through pipelines to "effectuate an equitable allocation and apportionment of Buckeye's income.

[1] *Buckeye Pipeline v. Commonwealth*, 689 A.2d at 366 (Pa. Cmwlth. 1997).

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Example 2 - Taxpayer Operating a Pipeline, a Trucking Operation and Performing Other Business Activities subject to Standard Apportionment

Split Apportionment Calculation	
1 Total Gross Receipts (excluding receipts related to income allocable pursuant to 72 P.S. § 7401(3)2.(a)(4)-(8))	425,000,000
2 Gross Receipts from Trucking activity subject to special apportionment pursuant to 72 P.S. § 7401(3)2.(b)	125,000,000
3 Gross Receipts from Pipeline activity subject to special apportionment pursuant to 72 P.S. § 7401(3)2.(c)	100,000,000
4 Gross Receipts subject to standard apportionment pursuant to 72 P.S. § 7401(3)2.(a)(15)-(17) (Line 1 - Line 2 - Line 3)	200,000,000
Standard Apportionment Portion	
5 Gross Receipts Fraction - standard apportionment activity (Line 4/Line 1)	0.470588
6 Income or Loss to be apportioned (Line 6, Section B of Form RCT-101)	50,000,000
7 Income or Loss subject to Standard Apportionment (Line 5 * Line 6)	23,529,412
8 Apportionment (from Schedule C-1 line 1C - standard apportionment)	0.18
9 PA Taxable Income - Standard Apportionment (Line 7 * Line 8)	4,235,294
plus	
Special Apportionment Portion - Trucking	
10 Gross Receipts Fraction - Trucking Activity (Line 2/Line 1)	0.294118
11 Income or Loss to be apportioned (Line 6, Section B of Form RCT-101)	50,000,000
12 Income or Loss subject to Special Apportionment for Trucking Companies (Line 10 * Line 11)	14,705,882
13 Apportionment (from Schedule C-1 line 2C - special apportionment - Trucking Activity Only)	0.65
14 PA Taxable Income - Special Apportionment - Trucking (Line 12 * Line 13)	9,558,824
plus	
Special Apportionment Portion - Pipeline	
15 Gross Receipts Fraction - Pipeline Activity (Line 3/Line 1)	0.235294
16 Income or Loss to be apportioned (Line 6, Section B of Form RCT-101)	50,000,000
17 Income or Loss subject to Special Apportionment for Pipeline Companies (Line 15 * Line 16)	11,764,706
18 Apportionment (from Schedule C-1 line 2C - special apportionment - Pipeline Activity Only)	0.07
19 PA Taxable Income - Special Apportionment - Pipeline (Line 17 * Line 18)	823,529
equals	
Combination of All Portions	
20 Pennsylvania Taxable Income - Standard Apportionment Portion (Line 9)	4,235,294
21 Pennsylvania Taxable Income - Special Apportionment Portion - Trucking (Line 14)	9,558,824
22 Pennsylvania Taxable Income - Special Apportionment Portion - Pipeline (Line 19)	823,529
23 Nonbusiness income or loss allocated to PA	-
24 PA Taxable Income or Loss After Apportionment (Line 20 + Line 21 + Line 22 + Line 23)	14,617,647
25 Total Net Operating Loss Deduction (RCT-103, Part A, Line 4)	1,800,000
26 PA Taxable Income or Loss (Line 24 - Line 25)	12,817,647
27 PA Corporate Net Income Tax (Line 26 * 0.0999)	1,280,483

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Finally, see below for an example where the taxpayer is in a loss position for the year.

Example 3 - Taxpayer Operating a Pipeline and Performing Other Business Activities subject to Standard Apportionment

Split Apportionment Calculation	
1 Total Gross Receipts (excluding receipts related to income allocable pursuant to 72 P.S. § 7401(3)2.(a)(4)-(8))	575,000,000
2 Gross Receipts from Pipeline activity subject to special apportionment pursuant to 72 P.S. § 7401(3)2.(c)	100,000,000
3 Gross Receipts subject to standard apportionment pursuant to 72 P.S. § 7401(3)2.(a)(15)-(17). (Line 1 - Line 2)	475,000,000
Standard Apportionment Portion	
4 Gross Receipts Fraction - standard apportionment activity (Line 3/Line 1)	0.826087
5 Income or Loss to be apportioned (Line 6, Section B of Form RCT-101)	(100,000,000)
6 Income or Loss subject to Standard Apportionment (Line 4 * Line 5)	(82,608,696)
7 Apportionment (from Schedule C-1 line 1C - standard apportionment)	0.18
8 PA Taxable Income - Standard Apportionment (Line 6 * Line 7)	(14,869,565)
plus	
Special Apportionment Portion	
9 Gross Receipts Fraction - Pipeline Activity (Line 2/Line 1)	0.173913
10 Income or Loss to be apportioned (Line 6, Section B of Form RCT-101)	(100,000,000)
11 Income or Loss subject to Special Apportionment for Pipeline Companies (Line 9 * Line 10)	(17,391,304)
12 Apportionment (from Schedule C-1 line 2C - special apportionment)	0.65
13 PA Taxable Income - Special Apportionment (Line 11 * Line 12)	(11,304,348)
equals	
Combination of Both Portions	
14 Pennsylvania Taxable Income - Standard Apportionment Portion (Line 8)	(14,869,565)
15 Pennsylvania Taxable Income - Special Apportionment Portion (Line 13)	(11,304,348)
16 Nonbusiness income or loss allocated to PA	-
17 PA Taxable Income or Loss After Apportionment (Line 14 + Line 15 + Line 16)	(26,173,913)
18 Total Net Operating Loss Deduction (RCT-103, Part A, Line 4)	-
19 PA Taxable Income or Loss (Line 17 - Line 18)	(26,173,913)
20 PA Corporate Net Income Tax (Line 19 * 0.0999)	-

We, therefore, hold that Buckeye is a pipeline company for 1.4% of its gross receipts, which are derived from transporting petroleum, and is entitled to have that amount apportioned according to the revenue barrel mile method. Buckeye is not a pipeline company for the remaining 98.6% of its gross receipts and must, therefore, apportion that amount according to the three-factor method.[2]

Since the issuance of the above opinion the Department has consistently applied the split factor methodology adopted by the court in *Buckeye Pipeline* to similarly situated taxpayers which engage in activities subject to both the standard apportionment formula as well as one or more of the special apportionment formulas found at 72 P.S. § 7401(3)2.(b)-(e). Application of this approach involves the following steps:

1. Calculate the income or loss to be apportioned (currently reported as line 6 of Section B of the Form RCT-101). In accordance with the unitary business concept, this is one amount encompassing all of the activities engaged in by the taxpayer.
2. Determine the entity's total gross receipts from all activities.
3. Determine the gross receipts from special apportionment activities.
4. Subtract the amount from Step 3 from the amount in Step 2 in order to determine the gross receipts from standard apportionment activities.
5. Calculate the percentage of gross receipts applicable to each activity by separately dividing the amounts from Step 3 and Step 4 by the amount determined in Step 2.
6. Multiply each of the percentages from Step 5 by the income or loss to be apportioned from Step 1.
7. Apply the standard apportionment formula to the amount of income or loss determined in Step 6 to be subject to standard apportionment.
8. Apply the applicable special apportionment formula to the amount of income or loss determined in Step 6 to be subject to special apportionment.
9. Add the results of Steps 7 and 8 together.
10. Add any nonbusiness income or loss allocated to Pennsylvania to the amount determined in Step 9.
11. If the taxpayer has positive income in Step 10, deduct available Pennsylvania net losses (subject to applicable limitations).
12. Apply the CNIT rate to the amount determined in Step 11.

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[2] *Buckeye Pipeline*, 689 A.2d at 372. Note that for the period at issue in the case standard apportionment consisted of a three-factor method based on property, payroll and sales. For tax years beginning after December 31, 2012 the standard apportionment formula requires all income to be apportioned to Pennsylvania based on the sales factor alone.

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See below for an example of these calculations relating to a taxpayer involved in one activity subject to special apportionment and one or more other activities subject to standard apportionment.

Example 1 - Taxpayer Operating a Pipeline and Performing Other Business Activities subject to Standard Apportionment

Split Apportionment Calculation	
1 Total Gross Receipts (excluding receipts related to income allocable pursuant to 72 P.S. § 7401(3)2.(a)(4)-(8))	300,000,000
2 Gross Receipts from Pipeline activity subject to special apportionment pursuant to 72 P.S. § 7401(3)2.(c)	200,000,000
3 Gross Receipts subject to standard apportionment pursuant to 72 P.S. § 7401(3)2.(a)(15)-(17). (Line 1 - Line 2)	100,000,000
Standard Apportionment Portion	
4 Gross Receipts Fraction - standard apportionment activity (Line 3/Line 1)	0.333333
5 Income or Loss to be apportioned (Line 6, Section B of Form RCT-101)	50,000,000
6 Income or Loss subject to Standard Apportionment (Line 4 * Line 5)	16,666,667
7 Apportionment (from Schedule C-1 line 1C - standard apportionment)	0.18
8 PA Taxable Income - Standard Apportionment (Line 6 * Line 7)	3,000,000
plus	
Special Apportionment Portion	
9 Gross Receipts Fraction - Pipeline Activity (Line 2/Line 1)	0.666667
10 Income or Loss to be apportioned (Line 6, Section B of Form RCT-101)	50,000,000
11 Income or Loss subject to Special Apportionment for Pipeline Companies (Line 9 * Line 10)	33,333,333
12 Apportionment (from Schedule C-1 line 2C - special apportionment)	0.65
13 PA Taxable Income - Special Apportionment (Line 11 * Line 12)	21,666,667
equals	
Combination of Both Portions	
14 Pennsylvania Taxable Income - Standard Apportionment Portion (Line 8)	3,000,000
15 Pennsylvania Taxable Income - Special Apportionment Portion (Line 13)	21,666,667
16 Nonbusiness income or loss allocated to PA	-
17 PA Taxable Income or Loss After Apportionment (Line 14 + Line 15 + Line 16)	24,666,667
18 Total Net Operating Loss Deduction (RCT-103, Part A, Line 4)	1,800,000
19 PA Taxable Income or Loss (Line 17 - Line 18)	22,866,667
20 PA Corporate Net Income Tax (Line 19 * 0.0999)	2,284,380

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See below for an example of these calculations relating to a taxpayer involved in two different activities subject to special apportionment and one or more other activities subject to standard apportionment.

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Netflix, Hulu Franchise Fee Case Draws Skeptical Judges in Ohio

By Perry Cooper
April 13, 2022, 12:41 PM

- Class could include over 2,000 municipalities in the state
- Companies face up to 5% gross revenue fee on subscriptions

Bloomberg Law News 2022-04-14T08:22:2256-04:00
Netflix, Hulu Franchise Fee Case Draws Skeptical Judges in Ohio

By Perry Cooper 2022-04-13T12:41:26000-04:00

1. Class could include over 2,000 municipalities in the state
2. Companies face up to 5% gross revenue fee on subscriptions

The Ohio Supreme Court appeared skeptical of a Cleveland suburb's arguments that Netflix Inc. and Hulu LLC are subject to local franchise fees paid by cable TV and internet service companies.

The city of Maple Heights seeks to represent a class of potentially over 2,000 Ohio local governments that argue streaming services should pay them up to 5% of their subscription revenue because they are "video service providers" under the state's Fair Competition in Cable Operations Act.

Several justices pressed Justin J. Hawal of DiCello Levitt Gutzler, who represented Maple Heights, on whether the city's broad reading of the statute would cover anyone posting videos online.

"Doesn't that mean everybody—teenagers with TicToc postings, Instagram?" Justice Melody J. Stewart asked at oral argument Wednesday.

"Would you recommend Columbus tax us" for streaming arguments online? Justice Patrick F. Fischer asked. "I mean, these are pretty good broadcasts!"

Hawal answered that such online videos aren't comparable to television in the way Netflix and Hulu are with respect to content, quality, and entertainment value.

Hulu attorney Victor Jih of Wilson Sonsini Goodrich & Rosati called those "very questionable determinations" to serve as the fulcrum for whether a company is subject to the law. "The fulcrum should actually be who is actually physically putting things in the rights of way," Jih said.

'Absurd Result'

The suit is one of more than a dozen class actions going after streaming services playing out across the country with mixed results.

When Netflix and Hulu asked the U.S. District Court for the Northern District of Ohio to dismiss Maple Height's suit, the court instead asked the Ohio high court to weigh in on whether the law applies.

Netflix and Hulu argue the law only applies to companies such as cable television and internet providers that install wire, lines, and other equipment along public rights-of-way to deliver service.

Netflix attorney Gregory G. Garre of Latham & Watkins LLP told the justices that Maple Heights' reading of the statute would lead to an "absurd result, or at least an extreme conclusion" that anyone who streams content over the internet—a high school streaming games, a church streaming services, or this court streaming arguments—would be subject to franchising fees.

The state sided with the companies. Deputy Solicitor General Mathura J. Sridharan called streaming companies like Netflix and Hulu "wholly agnostic to how the video content they provide is actually delivered to their users." The statute is focused on who digs in the cities' rights-of-way, she said. "If they don't dig, then they don't pay."

The justices had no questions for Sridharan, and very few for Jih and Garre. They focused most of their attention on Hawal, signaling they may be more skeptical of his arguments.

Question for Legislature?

Some of the justices questioned whether the state legislature was better suited to consider these policy questions.

"I agree with you on the service costs—the broadband, the wires, the fiber optics are a big deal," Fischer said to Hawal. "But shouldn't you be up at the state house a block and a half away instead of the courthouse trying to get the law changed?"

Justice Jennifer Brunner also asked Hawal whether his argument would require a change in the statute to redefine what a video service provider is.

Hawal answered the cities don't seek to change the law. The statute defines the term as someone who provides video programming over cables and wires, and it was meant to be flexible as technology evolved, he argued.

"As more and more people move away from traditional cable television and move towards services like Netflix and Hulu, the fees that go to the municipalities and townships to invest in this infrastructure are being pulled away from the cities," Hawal said. Netflix and Hulu put a physical burden on the infrastructure by requiring more bandwidth to stream high-quality video, he said.

The case is City of Maple Heights, Ohio v. Netflix, Inc., Ohio, No. 2021-864, argued 4/13/22 .

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Pa. Resident Says Wayfair Doesn't Permit Cleveland Tax

By Asha Glover · Mar 24, 2022, 8:40 PM EDT · Listen to article

The U.S. Supreme Court's Wayfair decision that allowed states to collect tax on sales from out-of-state businesses did not empower Cleveland to tax a Pennsylvania resident who worked remotely for a Cleveland business, she told an Ohio court.

The Cuyahoga County Court of Common Pleas should reject Cleveland's argument that the South Dakota v. Wayfair decision showed that physical presence is no longer required under the U.S. Constitution's due process clause and commerce clause for tax purposes, Pennsylvania resident Manal Morsy told the court Wednesday.

Wayfair does not apply here, according to her brief, because the statute central to that case did not impose a tax on the selling corporation and instead required Wayfair to collect and remit sales tax from South Dakota customers who were ultimately responsible for the tax. Additionally, Wayfair dealt with sales taxes, while Morsy's case is related to municipal income taxation and the taxpayer's physical presence.

"The city's focus on inapposite federal cases relating to businesses selling into another state — where there are recent Ohio Supreme Court cases directly on point speaking to the due process limits on municipalities vis-à-vis employees — is telling," according to the brief.

At issue is a 2020 law that deems remote work performed during the coronavirus pandemic to occur at an employee's principal place of work until 30 days after Ohio lifts its pandemic-related state of emergency. The law was partially reversed in a budget signed by Republican Gov. Mike DeWine in July. The budget specifies that provision offers withholding relief for 2021, allowing remote workers to claim refunds of taxes paid to cities on days when they

worked elsewhere during the year.

However, the budget doesn't disturb the sourcing change for 2020. Local governments had cautioned lawmakers that compelling them to issue refunds for the closed tax year could have calamitous effects on their coffers. Whether refunds will need to be paid for 2020 is being left for the courts to decide.

The case is one of several challenging the law around the state, saying that the cities where their employer's offices are located have no authority to impose income taxes on them for days in which they worked from home.

Morsy, in Wednesday's brief, argued that she is not required to exhaust any administrative remedies before the challenge can be heard because the court has original jurisdiction over constitutional challenges to illegal taxes.

If the Pennsylvania resident were required to appeal to the Cleveland Board of Tax Review, her efforts would be futile because the board lacks the authority to declare the law unconstitutional, she said.

"This is not a remedy that the city's Board of Tax Review can provide," according to the brief. "Further, even if the board had the power to grant Dr. Morsy the relief she seeks, it lacks jurisdiction to hear her complaint."

The Board of Tax Review's jurisdiction is limited to appeals by taxpayers of assessments regarding a municipal income tax obligation and Cleveland has not issued any assessment to Morsy in the present case, according to the brief.

"Indeed, because her employer has already withheld all of the disputed taxes and they have been transferred to the city, there is no reason the city would issue an assessment," Morsy said, adding that without an assessment the board lacks jurisdiction to hear any appeal from the dispute.

Morsy also argued that the Ohio General Assembly cannot authorize cities to engage in extraterritorial taxation. She urged the court to reject Cleveland's argument that the Legislature can expand a city's taxing power to reach non-Ohio residents working outside the state.

"Morsy is willing to pay municipal income tax for those days that she actually worked in the

city — indeed she has already paid them," according to the brief. "But that is not what [the 2020 law] and the city demand."

Cleveland's argument also ignores the fundamental principle that any state statute must conform to the due process clause, according to the brief.

"The city's suggestion that a state can statutorily authorize what the due process clause forbids is hard to take seriously," Morsy said. "A tax imposed without jurisdiction, whether authorized by state statute or not, violates due process."

The court should additionally reject the city's argument that the due process clause is not offended because Morsy is plainly subject to the Ohio General Assembly's authority because she had worked several days a week in Ohio before the pandemic, according to the brief.

"No court has ever held that an employee can be subject to the income tax of a foreign city or state simply because her employer is located there," Morsy said.

Representatives for Cleveland did not immediately respond to a request for comment.

Representatives for Morsy were not immediately available for comment.

Morsy is represented by Robert Alt and Jay Carson of the Buckeye Institute.

Cleveland and James Gentile, its interim finance director, are represented by Diane Menashe and Daniel Anderson of Ice Miller LLP.

The case is Manal Morsy v. James E. Gentile et al., case number CV-21-946057, in the Cuyahoga County Court of Common Pleas.

--Additional reporting by Paul Williams. Editing by Neil Cohen.

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EBay Backing Online Sellers Coalition to Address Tax Threshold

By Erin Slowey
March 24, 2022, 4:11 PM

- Burden of transaction threshold falls on sellers
- EBay does not have a threshold number in mind

Bloomberg Law News 2022-03-25T07:51:07824-04:00
EBay Backing Online Sellers Coalition to Address Tax Threshold

By Erin Slowey 2022-03-24T16:11:57000-04:00
1. Burden of transaction threshold falls on sellers
2. EBay does not have a threshold number in mind

EBay is launching a coalition to lobby for 1099-K fairness in response to the decrease in the business transaction threshold established by the American Rescue Plan Act last year, the company announced in a media briefing Thursday.

"The coalition aims to promote the interests of millions of Americans casually selling goods online and advocate for common sense tax regulations to govern the online goods resale market," said Jordan Sweetnam, eBay senior vice president and general manager of the Americas market.

The ARPA provision required third-party networks to send 1099-K forms to taxpayers who have business transactions of more than $600 without a minimum threshold for number of transactions, beginning in 2022. The previous threshold was $20,000 with a minimum of 200 transactions.

The new requirement will impact small, casual sellers; discourage individuals from buying and selling online; hinder potential opportunities; and encourage waste instead of reuse, according to Sweetnam.

The provision was created to require companies such as Uber and Lyft to tell contract workers how much money they have made on those platforms. Previously, gig workers were at risk of getting audited and owing back taxes for which they weren't prepared.

"The forum is intended to reward sales made through third-party platforms; nearly all U.S. goods are sold at a loss," Sweetnam said. "And the sellers must now be prepared to prove this loss in the event of an audit, which may be impossible whether it's a long-owned family heirloom or simply a vintage rock concert T-shirt from 20 years ago."

Reps. Cindy Axne (D-Iowa) and Chris Pappas (D-N.H.) introduced legislation earlier this month to raise the threshold for when third-party settlement organizations have to issue 1099-K tax forms to taxpayers to $5,000 from $600.

For legislative options, eBay does not have a set threshold number in mind, Sweetnam said, adding that he would be supportive of anything that reduced the filing burden on small businesses.

EBay surveyed 757 U.S. sellers who made less than $20,000 in online sales of goods from Feb. 8 to 14, 2021 and found:

- 86% of casual sellers made less than $5,000 in gross revenue, with 95% saying they sold 100 or fewer items.
- 47% said they were unaware of new IRS reporting requirements.
- Nearly 40% said the change posed an economic hardship, and of those, 74% said they sell online to help pay for necessary personal expenses.
- 67% said the new reporting requirements would cause confusion as to what income from online sales should be reported to the IRS.

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Mich. Justices Pass On Bed Bath & Beyond's Win On Mail Tax

By Sanjay Talwani · Mar 24, 2022, 3:43 PM EDT · Listen to article

The Michigan Supreme Court will let stand a lower court decision that Bed Bath & Beyond does not owe use taxes on marketing materials mailed to state residents because it ceded control of the activity to an out-of-state firm.

The state's highest court, in a one-sentence order Wednesday, said it was not persuaded by the Michigan Department of Treasury that the question presented should be reviewed by the court. A state appeals court ruled in July that the New Jersey-based company isn't liable for the use tax because it gave control of the materials, including advertising and coupons, to an out-of-state marketing agency.

"The court's order was appropriate, given the facts of the case and Michigan's prior precedence that has determined that the mere distribution of advertising, without more, does not constitute a taxable use," Lynn A. Gandhi, representing Bed Bath & Beyond, told Law360 on Thursday.

The appeals court said in its 2-1 decision in July that the home furnishings retailer isn't liable for the tax because its contract with the marketing agency, Harte Hanks Mailing House, ceded control over the materials and discretion over their transfers to the U.S. Postal Service. That ruling affirmed a state Court of Claims summary disposition negating a $317,000 Michigan Department of Treasury assessment from Aug. 1, 2008, through July 31, 2012.

The appeals court ruling relied on its 1996 decision in Sharper Image Corp. v. Department of Treasury, which held that mail-order catalogs mailed from a postal facility in Nebraska weren't subject to tax. The court in that case said that the company's exercise of power over the catalogs ended when they were delivered to the postal service and that the company didn't

use the items in Michigan.

The appeals panel acknowledged in its 2021 ruling that Bed Bath & Beyond provided Harte Hanks with numerous materials including a list of customers and their mailing addresses inside and outside Michigan, and required Harte Hanks report on the dates of distribution. But that panel said the agreement didn't give Bed Bath & Beyond the level of power or control over the materials to hold it responsible for the tax.

In a partial concurrence and dissent of the appeals court ruling, Judge Jane E. Markey had said that Bed Bath & Beyond should be liable for tax on materials delivered to postal service facilities inside of Michigan but not for materials delivered to mail facilities outside of Michigan.

The department had argued that all the mailed materials were taxable under the state appellate court's 2008 holding in Ameritech Publishing Inc. v. Department of Treasury, which held that a company owed use tax on telephone directories printed in Illinois and distributed from centers located in Michigan. The panel rejected that argument, saying Ameritech retained more control over the directories under a distribution contract with a company than Bed Bath & Beyond held over the materials in its contract with Harte Hanks.

A representative of the Michigan Department of Treasury declined to comment.

A representative of the state attorney general's office, which represents the department, declined to comment.

Bed Bath & Beyond is represented by Lynn A. Gandhi of Foley & Lardner LLP.

The Michigan Department of Treasury is represented by Randi Merchant of the Michigan Department of the Attorney General.

The case is Bed Bath & Beyond Inc. v. Department of Treasury, case number 163443-4, in the Michigan Supreme Court.

--Additional reporting by Paul Williams. Editing by Neil Cohen.

Update: This article has been updated with a response from the Michigan Department of Treasury.

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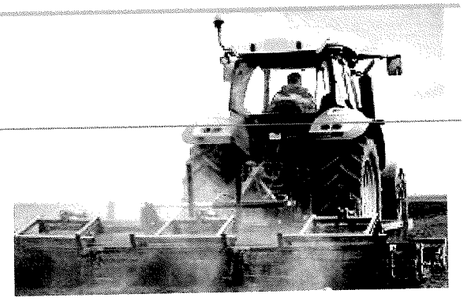
By Mark A. Balistrieri, CPA

The Pennsylvania Department of Revenue (DOR) issued Sales and Use Tax Bulletin 2021-05 on Nov. 2, 2021, regarding the taxation of equipment rental and equipment rental with operators. The bulletin restates the presumption that when a vendor provides the use of equipment with an operator the transaction is a rental of equipment.[1] As such, the charge for the rental of the equipment is subject to Pennsylvania sales and use tax, and the charge for the operator is subject to tax as a help supply service.[2] The presumption can be rebutted if the transaction can be supported by facts that demonstrate that the work being performed is exclusively under control of the vendor. If those facts can be established, the transaction is treated as a nontaxable service. Additionally, providing equipment without an operator is also considered to be taxable rental of the equipment.[3]

Regarding the operator charges, if that portion is separately stated the employee cost can be excluded from the taxable base and the tax would be applied to the markup of the operator charge consistent with the taxation of other help supply services.[4] If the charge is not separated from the equipment, the full charge is subject to tax.

The bulletin also addresses taxation of the purchase of the equipment by the vendor. If the predominant purpose of the equipment is for rental activities, the vendor is entitled to claim the resale exemption at the time of purchasing the equipment.[5] Conversely, if the predominant purpose of the equipment is to be used in providing a nontaxable service, the vendor owes tax on the original purchase price of the equipment.[6] If

the resale exemption was claimed on the exempt equipment, and the equipment is then used to provide a nontaxable service, the vendor would be required to accrue and remit use tax on the fair rental value during the usage to provide the nontaxable service.



The bulletin also addresses the assessment of tax against vendor refunds of tax paid by the purchaser of nontaxable services. Regarding refunds of tax, the purchaser may obtain refunds where they are able to document through invoices and/or contracts that the transaction is a nontaxable service. The DOR has also added an additional documentation requirement before a refund will be approved. Form REV-1890 will now be required to be completed by the vendor stating that the vendor incorrectly charged sales tax on the transactions and that the vendor will remit the use on the fair rental value of the equipment. The bulletin also states that it is the DOR's position that if a vendor charged tax on the original transaction, then provided REV-1890 in support of the purchaser's refund claim, the DOR can assess tax against the vendor on the fair rental value of the equipment, even if the equipment was purchased outside the three-year statutory assessment period – seemingly based on 72 P.S. Section 7260 regarding the filing of false and fraudulent returns.

Vendors of equipment rentals and nontaxable services involving the use of equipment should review their invoicing and contracts to verify that the sales and use tax treatment is consistent with Pennsylvania sales and use tax regulations and that the tax decisions can be supported under a DOR audit or review.

[1] *Pa. Code Section 31.4(a)(1))*

[2] *72 P.S. Sections 7201(g)(6) and (k)(15)*

[3] *61 Pa. Code Section 31.4(a)*

[4] *72 P.S. Section 7201(g)(6)*

[5] *61 Pa. Code Section 31.4(b)*

[6] *61 Pa. Code Section 31.4(b)(1)*

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)6/10/2019

lew Services Help Online Sellers with Pennsylvania Sales Tax

Harrisburg, PA — The Department of Revenue is making it easier for people and businesses elling products online to collect and remit Pennsylvania sales tax.

he department is working with Certified Service Providers (CSPs) — companies that allow out-of tate online sellers to outsource most of their sales tax collection responsibilities. CSPs will file tax eturns and also collect and forward tax payments to the Department of Revenue on behalf of heir clients.

he software that CSPs offer can also help an online seller determine which items they are selling re subject to Pennsylvania sales tax. Under the CSPs' arrangement with the Department of Revenue, CSPs will offer their services for free or at a reduced cost to online sellers with no physic presence in Pennsylvania.

There have been significant changes to federal and state laws in recent years that have drasticall changed the sales tax obligations for those who are selling products over the Internet," Revenue Secretary Dan Hassell said. "Because of these changes in the law, we have developed a solution hat will make it easier for out-of-state sellers and Pennsylvania purchasers to meet their sales tax obligations. We want to do everything that we can to provide taxpayers with the tools they need o follow the law."

he department has launched a new web page (https://www.revenue.pa.gov/GeneralTaxInformation/Tax%20Types%20and%20Information/SUT/Economic-Presence/Pages/Certified-Service-Providers.aspx) hat provides an overview of the services offered by CSPs. The four CSPs the department is vorking with are:

- AccurateTax (https://www.accuratetax.com/) https://www.accuratetax.com
- Avalara (https://www.avalara.com/) https://www.avalara.com
- https://sovos.com

axCloud (https://taxcloud.com/))

he department started working on this initiative after the U.S. Supreme Court in June 2018 issue
in opinion in *South Dakota v. Wayfair.* The opinion overturned the court's previous ruling in *Quill*
Corp. v. North Dakota, which required a business to have a physical presence in a state in order fo
he business to be required to collect that state's sales tax.

Read in conjunction with Pennsylvania's Tax Reform Code, the Supreme Court's decision in the
Wayfair case requires out-of-state sellers making $100,000 or more in annual gross sales to
Pennsylvania customers to collect and remit Pennsylvania sales tax. This was the threshold
suggested in the Wayfair case. This requirement will take effect in Pennsylvania on July 1, 2019.

The Supreme Court made it clear in its decision that tax administrators should not make it overly
difficult for out-of-state sellers to comply with the law," Hassell said. "The work the department is
doing with Certified Service Providers will remove many of the obstacles for Internet sellers who
will soon be required to collect Pennsylvania sales tax."

For more information, visit the Department of Revenue's website (https://www.revenue.pa.gov/) or visit the
department's pages on Facebook (https://www.facebook.com/padepartmentofrevenue) Twitter (https://twitter.com/parevenue) and LinkedIn (https://www.linkedin.com/company/parevenue)

MEDIA CONTACT: Jeffrey Johnson, Department of Revenue,
717-787-6960

###

Department of Revenue > Tax Information > Tax Types and Information > Sales Use and Hotel Occupancy Tax > Marketplace Sales > Remote Sellers

REMOTE SELLERS

A remote seller is a seller that does not maintain a place of business in Pennsylvania and makes sales directly to individual and business customers in Pennsylvania.

Mandatory Election

A remote seller that makes taxable sales totaling $10,000 or more to Pennsylvania customers in the previous calendar year must elect one of two options by March 1, 2018:

Option 1 - Register to collect and remit Pennsylvania sales tax.

Option 2 - Comply with Pennsylvania's notice and reporting requirements.

An election made on or before March 1, 2018 will be in effect through June 30, 2019.

The remote seller must complete REV-1830 (Annual Marketplace Sales Election Form) to make the election.

An election to comply with the notice and reporting requirement may be changed at any time to an election to collect and remit sales tax.

Failure to file an election will be treated by the Department of Revenue as an election to comply with the notice and reporting requirements.

Option 1 - Sales Tax Registration

If a remote seller elects to collect and remit sales tax, then it is required to register for a sales tax license. A sales tax license can be obtained at this web address: https://www.pa100.state.pa.us/Registration.htm.

Collections are to begin April 1, 2018 for the current election cycle.

Option 2 - Notice and Reporting Requirements

If a remote seller elects to comply with the notice and reporting requirements, it must

take the following actions starting April 1, 2018:

1. **Post a notice on the sales forum that states:**

Pennsylvania sales or use tax may be due in connection with the purchase and delivery of tangible personal property to Pennsylvania individuals and businesses.

The purchaser is required to file a use tax return if tax is due in connection with the purchase and delivery in the Commonwealth.

This notice is required pursuant to the provisions of the Tax Reform Code of 1971. 72 P.S. § 7213.2.

2. **Provide a written notice on all invoices, order forms, sales receipts or similar documents, whether in paper or electronic form, to each purchaser at the time of each sale that states:**

Pennsylvania sales tax was not collected on this sale. Therefore, you may be required to remit use tax directly to the Commonwealth on your purchase if the items are subject to Pennsylvania sales tax. Please visit this link to learn more about your use tax obligations under Pennsylvania law.

No statement that sales or use tax is not imposed on a transaction may be made by a remote seller, unless the transaction is exempt from sales and use tax, pursuant to Article II of the Tax Reform Code or other applicable Commonwealth law.

3. **Provide an annual report to the purchaser that states:**

A remote seller making an election to comply with the notice and reporting requirements must submit an annual report by January 31 of each year to the purchaser that includes the following.

[Name of remote seller] did not collect sales tax in connection with your transactions. You may be required to remit use tax to the Pennsylvania Department of Revenue. Following is a list by date, type and purchase price of each product, purchased or leased by the purchaser from this remoter seller, and delivered to a location within this Commonwealth.

[Insert list]

Remote Sellers

Please visit this link to learn more about your use tax obligations under Pennsylvania law.

[Name of remote seller] is required to submit an annual report to the Department of Revenue that includes the name of the purchaser and total dollar amount of the purchases from this remote seller.

This report shall be mailed by first class mail, in an envelope prominently marked with words indicating that important tax information is enclosed, to the purchaser's billing address, if known, or if unknown, to the purchaser's shipping address. If the purchaser's billing and shipping address are unknown, the report shall be sent electronically to the purchaser's last known email address with a subject heading indicating that important tax information is being provided.

4. Provide an annual report to the Pennsylvania Department of Revenue

A remote seller making an election to comply with the notice and reporting requirements must submit an annual report by January 31 of each year to the Department of Revenue that includes the following:

- *The purchaser's name, billing address, delivery address and, if different, the purchaser's last known mailing address.*
- *The total dollar amount of purchases from this remote seller.*

A report required under this section shall be submitted by an officer of the remote seller and shall include a statement made under penalty of perjury by the officer that the remote seller made reasonable efforts to comply with the notice and reporting requirements of this part.

Each failure to comply with the notice and reporting requirements can result in a penalty of $20,000 per violation, per year, or 20 percent of total Pennsylvania sales during the previous 12 months, whichever is less.

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Enforcement Date: August 3, 2017

May 17, 2017
Pennsylvania Sales and Use Tax
No. SUT-17-002
Tangible Personal Property/
Information Retrieval Products

ISSUE:

Are the information retrieval products, as described below, subject to Pennsylvania Sales and Use Tax as tangible personal property?

CONCLUSION:

The information retrieval products, as described below, are subject to Pennsylvania Sales and Use Tax as tangible personal property.

FACTS:

Taxpayer develops and sells information retrieval products in the form of subscriptions to specialized internet-based research services. These information retrieval products are used by professionals in a variety of industries including accounting, tax, finance, and law. The information retrieval products are accessed electronically over the internet using an ID and password. The information retrieval products are provided on a subscription-fee basis for monthly, quarterly or annual periods, with the subscription fees generally being based upon the number of users and/or resources to which a subscriber requests access. Subscribers are subject to certain terms and conditions of an agreement such as "a non-exclusive, non-transferrable, limited license…to use" the ordered information retrieval product. Further, in addition to the agreement, certain general terms and conditions are also applicable to provide certain limitations on the use of the information accessed within the information retrieval products.

Each information retrieval product provides access to resources from primary and secondary sources. Primary sources are sources including Federal, state and local statutes, court opinions, regulatory filings with or from governmental bodies, regulatory guidance from non-governmental bodies, and full-text patents. Secondary sources are sources including information from various non-governmental entities such as businesses, industry associations, and similar organizations.

The information retrieval products are maintained on servers which are located outside of Pennsylvania and accessed by a web browser previously existing on a subscriber's computer or device. As an alternative means of access, the information retrieval products are also available via a mobile phone application available for download free of charge. Such mobile phone application is available to the general public whether or not the person accessing and downloading the application has a subscription to the information retrieval product. The mobile phone application permits access with limited functionality on mobile devices, however no research content or related resources are included within the free mobile application download.

Subscribers typically interact with the information retrieval products through an advanced search function whereby search commands are transmitted by the subscriber's web browser to Taxpayer's servers. Application software on these servers processes the queries and returns the results to the subscriber. Results may be presented, according to the user's preference, in chart or spreadsheet format to make comparisons and facilitate further research. In addition to the above-described access to basic functionality, occasionally, a server hosting an information retrieval product returns information including "executable code" in a programming language designed to be executed by the subscriber's web browser. This executable code is used to provide a more graphically sophisticated user interface.

DISCUSSION:

Article II of the Tax Reform Code (TRC) imposes a six percent tax on "each separate sale at retail of tangible personal property or services, as defined herein, within this Commonwealth." 72 P.S. § 7202(a). The term sale at retail is defined, as "any transfer, for a consideration, of the ownership, custody or possession of tangible personal property, including the grant of any license to use or consume whether such transfer be absolute or conditional and by whatsoever means the same shall have been effected." 72 P.S. § 7201(k)(1). This statutory language demonstrates that not all sales in Pennsylvania are subject to Pennsylvania Sales and Use Tax. Rather, such tax is only imposed upon transactions for tangible personal property unless specifically exempted, services constituting a sale at retail, and services made taxable because of the broad definition of purchase price. 72 P.S § 7201(g) and (k).

The Pennsylvania sales tax law was recently updated by expanding the statutory definition of "tangible personal property" to expressly include certain specified items including video, books, applications, games, music, audio, canned software, and other specified items. *See* Act 84 of 2016 (pertinent section at 72 P.S. § 7201(m)(2) *effective* August 1, 2016). Act 84 of 2016 provides that such items constitute tangible personal property whether "electronically or digitally delivered, streamed or accessed" and "whether purchased singly, by subscription or in any other manner." *Id.* The statement of policy on computer software, hardware and related transactions which the Department adopted on January 7, 2000, does not address all aspects of tangible personal property as that term is now defined under Act 84 of 2016. *See* 61 Pa. Code § 60.19. For example, tangible personal property now expressly includes "maintenance, updates and support." 72 P.S. § 7201(m)(2). To the extent the statute and the statement of policy at 61 Pa. Code § 60.19 are inconsistent, the provisions of the statute apply. Where consistent however, the statement of policy provides additional guidance including, as relevant to the instant request, the definitions of "canned" and "custom" software. *See* 61 Pa. Code § 60.19(b).

In applying the above statutory and regulatory provisions to the information retrieval products, both the functionality and the resource content are relevant. When a subscriber interacts with the information retrieval products through an advanced search function, search commands are transmitted by the subscriber's web browser to Taxpayer's servers then application software processes the queries and returns the results to the subscriber. In utilizing the search function of the information retrieval product, the subscriber is exercising a license to access canned computer software. Furthermore, by entering inputs to obtain a certain desired output, the subscriber is exercising power and control over the software. See 72 P.S.

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CORPORATION TAX BULLETIN 2019-04[1]

ISSUED: SEPTEMBER 30, 2019

NEXUS FOR CORPORATE NET INCOME TAX PURPOSES

The federal underpinnings of a state's jurisdiction to tax is based on both the Due Process and the Commerce Clauses of the U.S. Constitution. Per applicable precedent, a state's jurisdiction to tax under the Due Process Clause "'requires some definite link, some minimum connection, between a state and the person, property or transaction it seeks to tax.'" *Quill Corp. v. North Dakota*, 504 U.S. 298, 306, 112 S.Ct. 1904 (1974) (quoting *Miller Bros. Co. v. Maryland*, 347 U.S. 340, 344-45, 74 S.Ct. 535, 98 L.Ed. 744 (1954). This threshold has traditionally been deemed to have been met by a showing that the entity has purposefully directed its activity into a jurisdiction. In *Quill* the Supreme Court noted that the Commerce Clause of the United States Constitution imposes a similar but more rigorous standard than that of Due Process; thus, "a tax may be consistent with due process and yet unduly burden interstate commerce." *Quill Corp. v. North Dakota*, 504 U.S. 298 at 313-14 n.7 (1992).

Historically, the U.S. Supreme Court has held that in order for a state tax to be constitutionally valid under the Commerce Clause it must:

(1) Apply to an activity with a substantial nexus with the taxing State;
(2) Be fairly apportioned;
(3) Not discriminate against interstate commerce; and,
(4) Be fairly related to the services the State provides.

Complete Auto Transit v. Brady, 430 U.S. 274, 97 S.Ct. 1076, 51 L.Ed.2d 326 (1977).

In June 2018 the U.S. Supreme Court issued its decision in the matter of *Wayfair v. South Dakota,* 138 S. Ct. 2080, 201 L. Ed. 2d 403 (2018). As part of that decision the Court found that:

> First, the physical presence rule is not a necessary interpretation of the requirement that a state tax must be "applied to an activity with a substantial nexus with the taxing state." *Complete Auto,* 430 U.S. at 279. Second, *Quill* creates rather than resolves market distortions. And third, *Quill* imposes the sort of arbitrary,

[1] To the extent this bulletin conflicts with Pennsylvania Corporation Tax Bulletin No. 2004-01 (05/19/2004), that bulletin is superseded.

formalistic distinction that the Court's modern Commerce Clause precedents disavow.

The Court went on to conclude "that the physical presence rule of *Quill* is unsound and incorrect."

As a result, the Commerce Clause analysis set forth in *Complete Auto Transit* remains valid, but the physical presence rule, which was previously held in *Quill* to be a necessary part of the substantial nexus prong is incorrect. While taxpayers contested for years whether the physical presence nexus standard in *Quill* was limited to sales taxes or also applied to corporate net income taxes, the decision in *Wayfair* has made certain that, at least prospectively, no physical presence standard exists for purposes of limiting the ability of a state to impose a net income tax on an out of state taxpayer so long as the constitutional requirements under the Due Process and Commerce Clauses of the United States Constitution are satisfied.

The corporate net income tax is imposed under Article IV of the Tax Reform Code (TRC). 72 P.S. §§7401 et seq. upon corporations:

> [E]xercising, whether in its own name or through any person, association, business trust, corporation, joint venture, limited liability company, limited partnership, partnership or other entity, any of the following privileges:
>
> (1) Doing business in this Commonwealth.
> (2) Carrying on activities in this Commonwealth, including solicitation which is not protected activity under the act of September 14, 1959 (Public Law 86-272, 15 U.S.C. Section 381 et seq.).
> (3) Having capital or property employed or used in this Commonwealth.
> (4) Owning property in this Commonwealth.

For Pennsylvania Corporate Net Income Tax purposes the decision in *Wayfair* has confirmed that out of state corporations are considered to be doing business in this Commonwealth and/or carrying on activities in this Commonwealth to the extent they are taking advantage of the economic marketplace of the Commonwealth regardless of whether they are physically present in Pennsylvania. As a result, the Department will require such taxpayers to begin filing Corporate Tax Reports so long as they meet the minimum thresholds for nexus under the Constitution of the United States. While the Court in *Wayfair* did not express a bright line threshold of economic activity which would satisfy the nexus requirements existing under the Due Process and Commerce Clauses, it did approve the approach of South Dakota whereby an out of state taxpayer was subjected to a sales tax collection requirement where it had in excess of either 200 sales or

$100,000 worth of sales of goods or services to South Dakota customers during the course of a tax year. While all taxpayers with nexus under the Constitution of the United States should file a Corporate Tax Report with Pennsylvania, the Department will deem there to be a rebuttable presumption that corporations without physical presence in the state, but having $500,000 or more of direct or indirect gross receipts from any combination of the following, sourced to Pennsylvania per year pursuant to the sales factor rules contained in 72 P.S. § 7401, have a filing requirement with the Commonwealth for purposes of the Corporate Net Income Tax:[2]

(1) Gross receipts from the sale, rental, lease, or licensing of tangible personal property;
(2) Gross receipts from the sale of services; and/or,
(3) Gross receipts from the sale or licensing of intangibles, including franchise agreements.

In interpreting this standard the Department recognizes that taxpayers with or without physical presence in the Commonwealth can still potentially claim exemption from the imposition of the Corporate Net Income Tax under the provisions of P.L. 86-272.[3] To the extent protection under this federal law is claimed, taxpayers should continue to file a Pennsylvania Corporate Tax Report (Form RCT-101) and complete the necessary schedules to claim this exemption from tax.

Consistent with the standards in this bulletin, the Department will require taxpayers without physical presence in the Commonwealth, but having nexus with Pennsylvania under the Constitution of the United States, to file Corporate Tax Reports for tax periods starting on or after January 1, 2020.

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[2] Note that in keeping with existing law and practice this standard will apply to taxpayers regardless of whether or not the entity is subject to federal income tax.

[3] *See* Pennsylvania Corporation Tax Bulletin No. 2004-01 (05/19/2004).

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SALES AND USE TAX BULLETIN 2019-01
Issued: January 8, 2019
Revised: January 11, 2019
Effective July 1, 2019
Maintaining a Place of Business in the Commonwealth

The relevant information contained in this bulletin was codified with the passage of Act 13-2019, which also suspended the Marketplace Sales laws. Please refer to Act 13 and the Department of Revenue's website for information on calculation, compliance and CSP guidance.

The Department of Revenue issues this bulletin to clarify when marketplace and remote sellers, marketplace facilitators, and all other vendors maintain a place of business in the Commonwealth, after the June 21, 2018, Supreme Court of the United States opinion in South Dakota v. Wayfair, Inc., 585 U.S. ___ (2018). The decision upheld South Dakota's economic nexus statute, and overturned its previous decision in Quill Corp. v. North Dakota, 504 U.S. 298 (1992), which required a business to have a physical presence in a state in order for it to be required to collect that state's sales tax. The decision in Wayfair, read in conjunction with the Tax Reform Code, creates an economic nexus for certain sellers of products in the Commonwealth, where previously, nexus existed only for those with a physical presence. The Department will enforce the Tax Reform Code consistent with the analysis set forth below and in accordance with applicable state and federal law.

Factual and Legal Background

South Dakota's statute, enacted in 2016, required out-of-state vendors who sold more than $100,000 worth of property to South Dakota's residents in the past year, or in more than 200 separate transactions, to begin to collect South Dakota's sales tax on future sales into the state. The statute applied prospectively only, and South Dakota previously had adopted the Streamlined Sales and Use Tax Agreement. The Agreement system standardizes taxes, including a single, state level tax, uniform definitions, simplified tax rates, and the availability of free tax administration software. Users of the state supplied software are immune from select audit liability.

In its decision, the Supreme Court concluded that its earlier decision in Quill was incorrect; a physical presence nexus rule is not required by the Constitution's Commerce Clause. As long as a vendor has a substantial nexus with a taxing state and the tax does not create an undue burden to that vendor, a virtual presence is sufficient to require the vendor to collect sales tax.

Although choosing not to resolve the undue burden issue in its decision, the Court

did address those specific portions of South Dakota's Act that it found to satisfactorily prevent discrimination. These included the safe harbor for those vendors who have limited business within South Dakota (less than $100,000 of sales or 200 transactions per year); no retroactive application; and the uniform rules and administration of the tax afforded by the Streamlined Agreement and corresponding software.

Current Pennsylvania Law

The Tax Reform Code requires every person maintaining a place of business in the Commonwealth to sell tangible personal property, or perform taxable services, to be licensed to, and collect, sales tax from its customers. 72 P.S. §§ 7202, 7208. The Code defines "maintaining a place of business in this Commonwealth" to include "[h]aving any contact within this Commonwealth which would allow the Commonwealth to require a person to collect and remit tax under the Constitution of the United States."

Upon careful review of the Supreme Court's decision in Wayfair that a physical presence was not required by the United States Constitution, and that an economic nexus, such as that prescribed by the South Dakota Act, is sufficient, the Department provides this guidance that a substantial economic nexus satisfies the Tax Reform Code's definition of maintaining a place of business, requiring a person to collect and remit Pennsylvania's sales tax.

Vendor Safeguards

Pennsylvania currently has only one state sales tax rate that applies across the Commonwealth. 72 P.S. § 7202(a).

To prevent any discrimination or undue burden on taxpayers whose virtual presence with the Commonwealth is limited:

1. Pennsylvania's economic nexus applies only to those persons who, in the previous twelve months, made more than $100,000 of gross sales into the Commonwealth.
    a. A marketplace facilitator with no physical presence in Pennsylvania should use both facilitated and direct sales to determine whether it has exceeded the economic nexus threshold.
    b. A marketplace seller with no physical presence in Pennsylvania should use only its direct sales and those sales made through a marketplace facilitator that does not collect sales tax on its behalf, to determine whether it has exceeded the economic nexus threshold.
2. The Department will certify service providers that will offer software and perform services that when relied upon by a vendor to determine whether or not the sale of a particular product or provision of a particular service is subject to sales tax, will relieve the vendor of liability upon audit.
3. The certified service provider also will aid in the registration, collection, reporting, and remittance of sales tax.

Coordination with the Marketplace Sales Act

The economic nexus rules do not replace or provide an alternative to the provisions of Act 43. The provisions of Act 43 remain valid law applicable to those vendors who have neither a physical presence nexus nor an economic nexus in Pennsylvania. However, for those marketplace facilitators and remote sellers who were required by Act 43 to elect to either collect and remit sales tax or give notice to customers and report to the Department, but now have an economic nexus in Pennsylvania, the Act 43 election no longer is available. Marketplace facilitators and sellers who made over $100,000 in Pennsylvania sales now will be required to register for a license and collect, report, and remit sales tax on sales into the Commonwealth. Additionally, if a marketplace facilitator has economic nexus in Pennsylvania, it now will be required to collect the sales tax on all sales into the Commonwealth, even if the sale is on behalf of a marketplace seller that does not individually have any nexus.

The provisions of this Bulletin shall apply to transactions that occur on or after July 1, 2019 and do not affect marketplace sellers for whom marketplace facilitators collect and remit on their behalf.

Additional procedural and technical guidance, as well as the available certified service providers, will be available on the Department's website.

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SALES AND USE TAX BULLETIN 2018-01

Issued: January 26, 2018

Marketplace Sales

Act 43 of 2017 ("Act") amended the Tax Reform Code of 1971 ("TRC") to level the retail playing field by establishing marketplace sales tax collection, notice, and reporting requirements. The TRC will be enforced by the Department consistent with the analysis set forth below, and in accordance with applicable state and federal law.

Legal Background

Vendors are required to collect sales tax from purchasers and remit the collected tax to the Commonwealth. 72 P.S. §7202(a). If a taxable sale at retail is made without collection of sales tax, and the purchaser uses the purchased item within the Commonwealth, the purchaser is required to pay use tax directly to the Commonwealth. 72 P.S. §7202(b). Thus, when anyone takes delivery in Pennsylvania of items purchased from a person who maintains no place of business in Pennsylvania, and the items would be taxable if purchased at a store in Pennsylvania, but sales tax is not collected, the purchaser is legally required to accrue and remit use tax directly to the Department. However, it is more efficient and less burdensome for the sales tax to be collected at the time of purchase, and then remitted directly to the Department.

Act 43

Act 43 of 2017 adds Part V-A to Article II, giving certain marketplace facilitators, remote sellers, and referrers the option to either collect and remit the sales tax that is due on taxable sales within the Commonwealth, or elect to notify their customers that use tax may be due, and report to the Department the customers names, addresses, and aggregate dollar amounts of each customer's purchases. 72 P.S. § 7213 et seq.

"Marketplace facilitators" are defined as persons, including vendors, who list or advertise tangible personal property for sale in any forum, directly or indirectly, collect the payment from the purchaser, and transmit the payment to the marketplace seller. 72 P.S. § 7213(c).

A "marketplace seller" is one who uses a marketplace facilitator to facilitate a sale. 72 P.S. § 7213(d).

A "referrer" receives consideration to advertise a seller's products, and transfers a buyer to the seller, facilitator, or other party to complete a sale, without collecting a receipt from the purchaser. 72 P.S. § 7213(g).

A "remote seller" is anyone other than a marketplace facilitator, marketplace seller, or referrer, who does not maintain a place of business in Pennsylvania, but who sells tangible personal property that would be subject to sales tax here. 72 P.S. § 7213(h).

On or before March 1, 2018, a remote seller, a marketplace facilitator, or a referrer who is not maintaining a place of business within the Commonwealth, but who had aggregate taxable sales in Pennsylvania worth at least $10,000 in the prior twelve months, must either file an election with the Department to collect and remit sales tax going forward, or comply with the notice and reporting requirements. 72 P.S. § 7213.1(a).

Only those marketplace facilitators who do not maintain a place of business within the Commonwealth are allowed to elect to collect, or give notice and report. 72 P.S. § 7213.1(c). If the marketplace facilitator maintains a place of business within the Commonwealth, the facilitator already is mandated by the TRC to collect sales tax on sales made on its own behalf, and on behalf of any marketplace seller for whom a sale within Pennsylvania is facilitated. 72 P.S. §§ 7201(b), (p) and 7202. If the marketplace facilitator does not maintain a place of business within the Commonwealth but facilitates for a marketplace seller who does, the burden has been and remains on the marketplace seller to collect sales tax on sales made within the Commonwealth. *Id.* Although not covered by this Act, a Pennsylvania marketplace seller also may contract with an out of state facilitator to collect sales tax on his behalf.

For referrers, the option to elect to collect or report applies only to sales at retail from referrals to marketplace sellers who do not maintain places of business in Pennsylvania, sales directly resulting from referrals to remote sellers, and sales of the referrer's own products if the referrer does not maintain a place of business here. 72 P.S. § 7213.1(d). A referrer can make differing elections for sales resulting from referrals, and sales of its own products. However, a referrer continues to be required to collect sales tax on sales of its own products if the referrer maintains a place of business in the Commonwealth. 72 P.S. §§ 7201(b), (p) and 7202.

Finally, for remote sellers meeting the threshold level of sales in Pennsylvania, there are no circumstances where an election is not required. If a remote seller makes more than $10,000 of taxable sales within the Commonwealth, he must collect sales tax from his Pennsylvania customers, or notify the customers that they may owe use tax and report all of the Pennsylvania sales to the Department.

Failure to make the required election is deemed an election to comply with the notice and reporting requirements. 72 P.S. § 7213.1(f). An election to provide notice and report can be switched to an election to collect by filing a new election at any time during the fiscal year the notice and report election is valid. 72 P.S. § 7213.1(e).

Additional procedural and technical guidance, as well as forms, will be published on the Department's website www.revenue.pa.gov.

pennsylvania
DEPARTMENT OF REVENUE

Sales & Use Tax Bulletin 2017-01

Issued April 10, 2017

Revised: March 5, 2021

Review of Large and Complex Refund Requests

To improve overall tax compliance and to improve the efficiency of reviewing these requests, large refund requests may be addressed through the field audit process.

There are several advantages for both taxpayers and the Department in addressing refund requests through a field audit:

- Overpayments established would offset any audit liability, potentially reducing the amount of interest and penalty due if a follow-up audit were conducted after a refund was granted.
- Furthermore, when an audit finds a net credit, interest will be calculated from the date of overpayment to the date of the audit report. In contrast, interest on a refund granted on appeal can only be granted starting 60 days after the petition is filed.
- A field audit can involve a stratified random sample of liabilities and overpayments, including overpayments to third parties, to limit the number of transactions required to be reviewed at all appellate levels.
- Through a field audit, areas of liabilities and overpayments would be specifically identified and discussed with the taxpayer, so that the taxpayer can take corrective action to improve compliance.
- A taxpayer can provide on-site evidence to the auditor, allowing an informed decision regarding the proper application of sales and use tax.
- Consolidating the liability and overpayment issues into a field audit would allow the appellate process to handle both issues simultaneously.

If a large refund request results in an audit being issued, the taxpayer will have the option to continue pursuing the refund through the appeal process or withdrawing the petition for refund and allowing the overpayments to be addressed in the audit. The audit will generally encompass the periods statutorily open to audit which is the three prior years plus the current year. An audit may extend to additional periods if the taxpayer agrees to a waiver of the statute of limitations on assessments. The taxpayer's due process rights for that period are fully preserved through the field audit process. Any refunds not granted in the audit for the audit period may be raised in a refund petition within six months of the mailing date of the notice of assessment, or within three years of actual payment of the tax, whichever is later, under 72 P.S. § 10003.1(b).

The decision to conduct a field audit will be at the discretion of the Department, but in general, refund petitions requesting in excess of $100,000, or multiple petitions in one year exceeding that threshold in the aggregate, are more likely to be referred for a field audit.

REV-1220 (TR) 03-22

START

pennsylvania
DEPARTMENT OF REVENUE

PENNSYLVANIA EXEMPTION CERTIFICATE

STATE AND LOCAL SALES AND USE TAX
STATE 6% AND LOCAL 1% HOTEL OCCUPANCY TAX
PUBLIC TRANSPORTATION ASSISTANCE TAXES AND FEES (PTA)
VEHICLE RENTAL TAX (VRT)
ADDITIONAL LOCAL, CITY, COUNTY HOTEL TAX *

This form cannot be used to obtain a Sales Tax Account ID, PTA Account ID or Exempt Status.

(Please Print or Type)
Read Instructions On Reverse Carefully

THIS FORM MAY BE PHOTOCOPIED – VOID UNLESS COMPLETE INFORMATION IS SUPPLIED

CHECK ONE: **PENNSYLVANIA TAX UNIT EXEMPTION CERTIFICATE** (USE FOR ONE TRANSACTION)
PENNSYLVANIA TAX BLANKET EXEMPTION CERTIFICATE (USE FOR MULTIPLE TRANSACTIONS)

Name of Seller, Vendor or Lessor

Street	City	State	ZIP Code

NOTE: Do not use this form for claiming an exemption on the registration of a vehicle. To claim an exemption from tax for a motor vehicle, trailer, semi-trailer or tractor with the PA Department of Transportation, Bureau of Motor Vehicles, use one of the following forms:

FORM MV-1, Application for Certificate of Title (first-time registrations)

FORM MV-4ST, Vehicle Sales and Use Tax Return/Application for Registration (other registrations)

Property and services purchased or leased using this certificate **are exempt** from tax because: (Select the appropriate paragraph from the back of this form, check the corresponding block below and insert information requested).

1. Property or services will be used directly and predominately by purchaser in performing purchaser's operation of: _____
2. Purchaser is a/an: _____ holding Sales Tax Exemption Number _____
3. Property will be resold under Account ID _____ (If purchaser does not have a PA Sales Tax Account ID, include a statement under Number 8 explaining why a number is not required).
4. Property or services will be used directly and predominately by purchaser performing a public utility service.
   PA Public Utility Commission PUC Number _____ and/or U.S. Department of Transportation MC/MX _____
5. Exempt wrapping supplies, Account ID _____ (If purchaser does not have a PA Sales Tax Account ID, include a statement under Number 8 explaining why a number is not required).
6. Canned computer software purchased by a financial institution subject to the Bank and Trust Company Shares Tax (Article VII) or the Mutual Thrift Institutions Tax (Article XV).
7. Canned computer software licenses that are billed to a PA address but used outside of PA. The total number of software licenses purchased for invoice # _____ is _____. The total number of users accessing and using the software outside PA is _____.
8. Other _____
   (Explain in detail. Additional space on reverse side).

I am authorized to execute this certificate and claim this exemption. Misuse of this certificate by seller, lessor, buyer, lessee or their representative is punishable by fine and imprisonment.

Name of Purchaser or Lessee	Signature **Please sign after printing.**	EIN	Date

Street	City	State	ZIP Code

1. **ACCEPTANCE AND VALIDITY:**
   For this certificate to be valid, the seller/lessor shall exercise good faith in accepting this certificate, which includes: (1) the certificate shall be completed properly; (2) the certificate shall be in the seller/lessor's possession within 60 days from the date of sale/lease; (3) the certificate does not contain information which is knowingly false; and (4) the property or service is consistent with the exemption to which the customer is entitled. For more information, refer to Exemption Certificates, Title 61 PA Code §32.2. An invalid certificate may subject the seller/lessor to the tax.
2. **REPRODUCTION OF FORM:**
   This form may be reproduced but shall contain the same information as appears on this form.
3. **RETENTION:**
   The seller or lessor must retain this certificate for at least four years from the date of the exempt sale to which the certificate applies.
   ⚠ **IMPORTANT: DO NOT RETURN THIS FORM TO THE PA DEPARTMENT OF REVENUE.**
4. **NONPROFIT EXEMPT ORGANIZATIONS:**
   This form may be used in conjunction with form REV-1715, Exempt Organization Declaration of Sales Tax Exemption, when a purchase of $200 or more is made by an organization which is registered with the PA Department of Revenue as an exempt organization. These organizations are assigned an exemption number, beginning with the two digits 75 (example: 75000000).

Reset Entire Form TOP OF PAGE NEXT PAGE PRINT

GENERAL INSTRUCTIONS

Those purchasers set forth below may use this form in connection with the claim for exemption for the following taxes:

a. State and local sales and use tax;
b. PTA rental fee or tax on leases of motor vehicles;
c. Hotel occupancy tax (state 6%, Philadelphia 1%, Allegheny 1%) if referenced with the symbol (●);
d. PTA fee on the purchase of tires if referenced with the symbol (+);
e. Vehicle rental tax (VRT).

EXEMPTION REASONS

1.) Property and/or services will be used directly and predominately by purchaser in performing purchaser's operation of:

A. Manufacturing
B. Mining
C. Dairying
D. Processing
E. Farming
F. Shipbuilding
G. Timbering

This exemption is not valid for property or services used in: (a) constructing, repairing or remodeling of real property, other than real property used directly in exempt operations; or (b) maintenance, managerial, administrative, supervisory, sales, delivery, warehousing or other nonoperational activities. This exemption is not valid for vehicles that are required to be registered under the Vehicle Code, as well as supplies and repair parts for such vehicles, the PTA tire fee, and certain taxable services.

2.) Purchaser is a/an:

\+ A. Instrumentality of the commonwealth (to include public schools and state universities).
\+ B. Political subdivision of the commonwealth (includes townships and boroughs).
\+ ● C. Municipal authority created under the Municipality Authorities Acts.
\+ ● D. Electric cooperative corporations created under the Electric Cooperative Law of 1990.
● E. Cooperative agricultural associations required to pay corporate net income tax under the Cooperative Agricultural Association Corporate Net Income Tax Act (exemption not valid for registered vehicles).
\+ ● F. Credit unions organized under Federal Credit Union Act or Commonwealth Credit Union Act.
\+ ● G. U.S. government, its agencies and instrumentalities.
● H. Federal employee on official business (exemption limited to hotel occupancy tax only. A copy of orders or statement from supervisor must be attached to this certificate).
I. School bus operator (This exemption certificate is limited to the purchase of parts, repairs or maintenance services upon vehicles licensed as school buses by the PA Department of Transportation).
J. Charter Schools and Community Colleges.

Renewable Entities beginning with "75":

K. Religious Organization
L. Nonprofit Educational Institution
M. Charitable Organization

Permanent Exemptions beginning with the two numbers "75":

N. Volunteer Fire Company
O. Relief Association

Special Exemptions

P. Direct Pay Permit Holder
Q. Individual Holding Diplomatic ID
R. Keystone Opportunity Zone (beginning with two digit 72 account number)
S. Tourist Promotion Agency

Exemptions for exempt organizations K through S are limited to purchases of tangible personal property or services for use and not for sale. Exempt organizations K - O above, shall have an sales tax exemption certificate number assigned by the PA Department of Revenue. Exempt organizations K-O above, are not exempt for purchases used for the following: (1) constructions, improvement, repair or maintenance or any real property, except supplies and materials used for routine repair or maintenance of the real property; (2) any unrelated activities or operation of a public trade or business; or (3) equipment used to maintain real property.

3.) Property and/or services will be resold or rented in the ordinary course of purchaser's business. If purchaser does not have a PA Sales Tax Account ID (8 digit number assigned by the department), complete Number 8 explaining why such number is not required. This exemption is valid for property or services to be resold: (1) in original form; or (2) as an ingredient or component of other property.

4.) Property or services will be used directly and predominately by purchaser in the production, delivery or rendition of public utility services as defined by the PA Utility Code.

This exemption is not valid for property or services used for the following: (1) construction, improvement, repair or maintenance of real property, other than real property used directly in rendering the public utility services; or (2) managerial, administrative, supervisor, sales or other nonoperational activities; or (3) vehicles, as well as supplies and repair parts for such vehicles, unless the predominant use is for providing a common carrier service; or (4) tools and equipment used but not installed in maintenance of facilities or direct use equipment. Tools and equipment used to repair "direct use" property are exempt from tax.

5.) Vendor/seller purchasing wrapping supplies and nonreturnable containers used to wrap property which is sold to others.

6.) Canned computer software or services to canned computer software directly utilized in conducting the business of banking purchased by a financial institution subject to the Bank and Trust Company Shares Tax (Article VII) or the Mutual Thrift Institutions Tax (Article XV).

7.) Seller is required to collect tax on canned software accessed remotely when the user is located in PA. If the billing address is a PA address, the presumption is that all users are located in PA. Purchaser is responsible for apportioning and remitting the tax due to each taxing jurisdiction and must provide the total number of licenses purchased and the number of those licenses used outside PA on Line 8. Please note that any unused licenses will be considered to be allocated to PA.

8.) Other (Attach a separate sheet of paper if more space is required).

* *Employees or representatives of the Commonwealth traveling on Commonwealth duty are exempt from any taxes on hotel stays or room rentals imposed by local governments that are in addition to the 6% state tax and the 1% Philadelphia and Allegheny County hotel occupancy tax.*

e total	State Sales Tax	Local Sales Tax	Invoice Description	(i) Usage based licensing or (ii) server/network operating system?	What is the Software? (Please be specific)	Who uses the software? (e.g. attorneys, IT)	Are users employees of taxpayer, employees of taxpayer's subsidiary, taxpayer's customer, etc.	Per License Fee	# of users Listed on Invoice	# of users in taxpayer's user count/study	Please provide an explanation for variations in software licenses from the users, e.g. simultaneous licenses	Exhibits (e.g. contracts, hyperlinks to website)

locuments for all purchases listed.

:d.

rmation from question 1.

age information.

ts may be requested to support employee locations or positions.

rganizing the type of information that is helpful in reviewing transactions that may involve out-of-state software users.

Vendor	Invoice #	Invoice total	State Sales Tax	Local Sales Tax	Invoice Description	(i) Usage based licensing or (ii) server/network operating system?	What is the Software? (Please be specific)	Who uses the software? (e.g. attorneys, IT)	Are users employees of taxpayer, employees of taxpayer's subsidiary, taxpayer's customer, etc.	Per License Fee	# of users Listed on Invoice	# of users in taxpayer's user count/study	Please provide an explanation for variations in software licenses from the users, e.g. simultaneous licenses	Exhibits (e.g. contracts, hyperlinks to website)

1. Provide copies of all listed invoices, contracts, Statements of Work, or other relevant documents for all purchases listed.
2. Provide proof of payment for all invoices where refund of Pennsylvania tax is requested.
3. Please provide the names, locations, and roles of all software users
4. For all software requiring user ids, please provide all user ids in conjunction with information from question 1.
5. For all software purchased other than on a per user basis, please provide additional usage information.
6. To what extent are the licenses used exclusively in Pennsylvania
7. Additional information such as payroll, unemployment records, or organizational charts may be requested to support employee locations or positions.

** Completing this schedule does not entitle a Petitioner to relief, but the schedule is a way of organizing the type of information that is helpful in reviewing transactions that may involve out-of-state software users.

Potter, Charles

From: Richard Schmidt <rschmidt@gmgconsulting.com>
Sent: Friday, March 18, 2022 2:26 PM
To: Annette Knapp; mbalistrieri@kpmg.com; timothy.billow@highmarkhealth.org; troy.cannode@gmail.com; mjeby@rklcpa.com; meckman@mpbcpa.com; eernest@tollbrothers.com; Jerry.Glynn@us.gt.com; Potter, Charles; jason@pivotsalt.com; kstoops@deloitte.com; mszitas@mpbcpa.com; danwestovercpa@aol.com; jwilliams@kkbcpas.com; Adam Batchelor; James V. DeLuccia; Katie Nale; Peter N. Calcara; Alexandra Fabian; Thompson, Steven; Matthews, Louisa B.
Subject: RE: Updated: 3-23-22 PICPA SUT TLC Mtg. Agenda

External Email: Use Caution When Opening Attachments or Links.

Hi Annette,

Do you have a copy of the "template" attachment Ben referenced below?

Thanks, and have a great weekend!

Rich

From: Annette Knapp <aknapp@picpa.org>
Sent: Friday, March 18, 2022 1:58 PM
To: mbalistrieri@kpmg.com; timothy.billow@highmarkhealth.org; troy.cannode@gmail.com; mjeby@rklcpa.com; meckman@mpbcpa.com; eernest@tollbrothers.com; Jerry.Glynn@us.gt.com; cpotter@tuckerlaw.com; Richard Schmidt <rschmidt@gmgconsulting.com>; jason@pivotsalt.com; kstoops@deloitte.com; mszitas@mpbcpa.com; danwestovercpa@aol.com; jwilliams@kkbcpas.com; Adam Batchelor <abatchelor@picpa.org>; James V. DeLuccia <JDeLUCCIA@picpa.org>; Katie Nale <knale@picpa.org>; Peter N. Calcara <PCalcara@picpa.org>; Alexandra Fabian <afabian@picpa.org>; Thompson, Steven <stethompson@deloitte.com>; Matthews, Louisa B. <lmatthews@deloitte.com>
Subject: RE: Updated: 3-23-22 PICPA SUT TLC Mtg. Agenda

CAUTION: This email originated from outside of the organization. Do not click links or buttons in the body of the email or open attachments unless you recognize the sender email address and confirmed verbally with the sender that the content is safe.

Hi folks,

Here is some more background information regarding the PA DOR Software Sourcing Rules discussion for next week's meeting:

March 17, 2022

Feedback from the PA DOR-Revenue Tax Audit Program Administrator, Ben Turek:

Good morning everyone,

I wanted to pass along some updates concerning documenting out-of-state software use.

The first update is concerning the Pennsylvania Exemption Certificate (REV-1220). The REV-1220 has been updated to specifically include a line relating to out-of-state software

use. The presumption remains that software billed to an address in PA is 100% subject to PA sales tax unless the vendor receives a properly completed exemption certificate that includes the total number of licenses purchased and the total number of licenses used outside of PA. The taxable percentage would calculated by: $\frac{(Total\ Number\ of\ Licenses - Total\ Licenses\ used\ Outside\ of\ PA}{Total\ Number\ of\ Licenses}$. Software will not always be sold with what are often called "seated" license, which is where an individual is named for each license sold. In those cases the form should list all of the potential users of the software and all of the potential out-of-state users. When reviewing the sales of vendor, if the form is complete it should be considered as accepted in good faith unless the invoice or contract would give you a reason to believe that the exemption certificate is incorrect.

The other document that is attached is a template that is to be used when a taxpayer is requesting a refund of taxes paid for software used in other states. The taxpayer will need to complete the attached template and provide all of the information contained in the instructions. When agreeing to allow a refund, it is important that we verify the accuracy of the users, for location as well as actual use of the software. An example would be a taxpayer claiming a refund for their accounting software. It is unlikely that all of the taxpayers are actually using this type of software, it is probably a smaller group. It is important to understand how the software is being used and who is actually using it. When completing the template, they will need to provide a user study/breakdown of employees by state and selected employee information should be verified to payroll records or wage/unemployment tax forms. Please remember that in any audit where we are granting refunds for software used in another state, the records supporting the out-of-state use and invoices for the purchases should be sent to the division on an Additional Headquarters Processing Request. This template should also be used as a customer exemption statement when assessing sales tax on the taxpayers nontaxed sales of software to their customers when they indicate that the software is used in multiple states. This template is also going to be used by the Board of Appeals when granting similar refunds, so our approach should now be consistent.

Thanks,
Annette

From: Annette Knapp
Sent: Wednesday, March 16, 2022 12:40 PM
Subject: Updated: 3-23-22 PICPA SUT TLC Mtg. Agenda

Good afternoon,

Attached you'll find the updated Wed., March 23 Sales and Use Tax Thought Leadership Committee meeting agenda and a handout on the *Quality Driven Copack, Inc. vs. Commonwealth of PA* decision. We've added a PA DOR Software Sourcing Rules discussion.

This Microsoft Teams meeting will begin at 2:30 p.m.

Log in details:

Microsoft Teams meeting

Join on your computer or mobile app
Click here to join the meeting
Or call in (audio only)
+1 267-857-3799,,453227425# United States, Philadelphia
Phone Conference ID: 453 227 425#

Find a local number | Reset PIN

Learn More | Meeting options

Please let me know if you need anything else.

Thanks,
Annette

Annette Knapp | Government Relations Coordinator
Pennsylvania Institute of CPAs | 500 North 3rd Street, Suite 600A | Harrisburg, PA 17101
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The opinions expressed herein are my own, and do not reflect those of the Pennsylvania Institute of Certified Public Accountants, or the Institute/Foundation's officers, members or employees.

Potter, Charles

From: Dan Westover <danwestovercpa@aol.com>
Sent: Wednesday, April 27, 2022 2:33 PM
To: stethompson@deloitte.com; mbalistrieri@KPMG.com; afabian@picpa.org; aknapp@picpa.org; timothy.billow@highmarkhealth.org; troy.cannode@gmail.com; mjeby@rklcpa.com; meckman@mpbcpa.com; eernest@tollbrothers.com; Jerry.Glynn@us.gt.com; Potter, Charles; rschmidt@gmgconsulting.com; jason@pivotsalt.com; kstoops@deloitte.com; mszitas@mpbcpa.com; jwilliams@kkbcpas.com; abatchelor@picpa.org; JDeLUCCIA@picpa.org; knale@picpa.org; PCalcara@picpa.org; lmatthews@deloitte.com
Subject: Re: Following up 3-23-22 PICPA SUT TLC Call

External Email: Use Caution When Opening Attachments or Links.

While I'm thinking about it... I think Steve brought up issues regarding the information required for the software exemption on the new exemption certificate (Line 7).

Because this document acts legally to alter the sales tax responsibility from the seller to the purchaser, I believe a more valid statement should read "Invoice or other reference to software purchased" and "Exempt percentage." The exemption certificate shouldn't convey any methodology.. that's the purchaser's domain. It's strictly used by the seller to alter taxability and deflect responsibility. It's really not the responsibility of the seller to determine the appropriate reasoning.

Sorry if that's already been discussed.

Dan

Daniel L Westover CPA
449 Willow Drive
Pittsburgh, PA 15243

Cellular: 412-427-6331
danwestovercpa@aol.com

-----Original Message-----
From: Thompson, Steven <stethompson@deloitte.com>
To: Balistrieri, Mark A <mbalistrieri@KPMG.com>; Alexandra Fabian <afabian@picpa.org>; Annette Knapp <aknapp@picpa.org>; Tim Billow (EXTERNAL) <timothy.billow@highmarkhealth.org>; troy.cannode@gmail.com <troy.cannode@gmail.com>; mjeby@rklcpa.com <mjeby@rklcpa.com>; meckman@mpbcpa.com <meckman@mpbcpa.com>; eernest@tollbrothers.com <eernest@tollbrothers.com>; Jerry.Glynn@us.gt.com <Jerry.Glynn@us.gt.com>; cpotter@tuckerlaw.com <cpotter@tuckerlaw.com>; rschmidt@gmgconsulting.com <rschmidt@gmgconsulting.com>; jason@pivotsalt.com <jason@pivotsalt.com>; Stoops, Kenneth <kstoops@deloitte.com>; mszitas@mpbcpa.com <mszitas@mpbcpa.com>; danwestovercpa@aol.com <danwestovercpa@aol.com>; jwilliams@kkbcpas.com <jwilliams@kkbcpas.com>; Adam Batchelor <abatchelor@picpa.org>; James V. DeLuccia <JDeLUCCIA@picpa.org>; Katie Nale <knale@picpa.org>; Peter N. Calcara <PCalcara@picpa.org>; Matthews, Louisa B. <lmatthews@deloitte.com>
Sent: Tue, Apr 26, 2022 11:18 am
Subject: RE: Following up 3-23-22 PICPA SUT TLC Call

All -While there are many examples that we could cite to illustrate the problems that taxpayers have had with the taxation of software, it may be helpful to frame the discussion with the PA DOR using some version of the categories below. We are hopeful that working within a framework like this will create space to highlight the many specific issues while engaging in a solutions-oriented discussion. In trying to make this issue accessible to the executive office of the PA DOR, this may be a case of "less is more".

1. **Updated REV 1220**

The following language from the recently updated Form REV 1220 language (below) is problematic.

> *7. Canned computer software licenses that are billed to a PA address but used outside of PA. The total number of software licenses purchased for invoice # is ___. The total number of users accessing and using the software outside PA is ___.*

It is not clear what action a software vendor should take if it receives a certificate that identifies (for example)

- 1 license (server based) and 504 users accessing and using the software outside of PA
- 1000-3000 licenses (tiered pricing) and 504 users accessing and using the software outside of PA

The information requested with the revised exemption certificate is insufficient for vendors to calculate the correct amount of tax. Note that Letter Ruling 12-001 simply advised purchasers that *"[o]n Line No. 7 of the exemption certificate, the purchaser must state the percentage of users of the software who are located in Pennsylvania"*. If the Department's policy continues to be that software is taxed where it is used, then there seems little reason to do anything other than to follow the guidance in Letter Ruling 12-001.

2. **"Unused licenses"**

Pursuant to the instructions to REV 1220, line 7 *"any unused licenses will be considered to be allocated to PA"*. This contradicts the Department's policy to source software to the location of the users. *"Unused licenses"* are, by definition, not associated with any users. Sourcing unused licenses to any particular state is not consistent with a policy that sources software to user location.

Double taxation -Many states source software to the location of the user. If the value of *"unused licenses"* is taxed by Pennsylvania, that same value will also be taxed by states in which the users are located. All states that source software to the location of the user will allocate the entire value of the software among the user base. The PA DOR policy for sourcing unallocated licenses is out of step with every other state.

3. **Documentation of user location**

The introduction of the attached spreadsheet may be an attempt to standardize information requests to determine software location. We note that failure to provide <u>all</u> information requested is often cited by the PA DOR as grounds to source all software to Pennsylvania. While an attempt to increase efficiency by removing judgment is understandable, it is ill-advised. There are too many scenarios and variables in the sale and use of software for a rules-based approach to succeed. Some of them are listed below. What is needed is an agreement on fundamental principles that will guide the PA DOR and taxpayers as they strive for compliance in an ever-evolving area.

- User location is dynamic and is affected by any number of factors including employee relocation and reassignment.
- Number of users is dynamic and is affected by factors including layoffs, M&A activity, expansions, etc.
- Because the number and location of users is dynamic, a PA software allocation percentage is inherently an estimate. It should be expected that the percentage of PA software users will vary from year to year if not month to month.
- Software licenses rarely have a direct correlation with the number of users.
    - One license may authorize use by an undefined (or range) of users
    - Licenses may be location-based, rather than user-based
    - Licenses may be device-based, rather than user-based

Steven C. Thompson
Deloitte Tax LLP
Tel/Direct: +1 215 246 2463
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From: Balistrieri, Mark A <mbalistrieri@KPMG.com>
Sent: Friday, April 22, 2022 11:48 AM
To: Alexandra Fabian <afabian@picpa.org>; Annette Knapp <aknapp@picpa.org>; Tim Billow (EXTERNAL) <timothy.billow@highmarkhealth.org>; troy.cannode@gmail.com; mjeby@rklcpa.com; meckman@mpbcpa.com; eernest@tollbrothers.com; Jerry.Glynn@us.gt.com; cpotter@tuckerlaw.com; rschmidt@gmgconsulting.com; jason@pivotsalt.com; Stoops, Kenneth <kstoops@deloitte.com>; mszitas@mpbcpa.com; danwestovercpa@aol.com; jwilliams@kkbcpas.com; Adam Batchelor <abatchelor@picpa.org>; James V. DeLuccia <JDeLUCCIA@picpa.org>; Katie Nale <knale@picpa.org>; Peter N. Calcara <PCalcara@picpa.org>; Thompson, Steven <stethompson@deloitte.com>; Matthews, Louisa B. <lmatthews@deloitte.com>
Subject: [EXT] RE: Following up RE: 3-23-22 PICPA SUT TLC Call

All,

Here are some of the data/thoughts I have gathered since our prior call:

1. There are some IT departments that do have access to reports that can identify the number of total users at a given time. There is also the ability to identify if the user is in PA or another state. The basis for that can vary. For example, some IT departments the can identify the user by a login/userid. As that login is assigned to the employee IT/HR can identify what office/location that person is assigned to. Some devices my have location/GPS services turned on to identify where the device is.
    a. This seems to be more readily available for enterprise wide software
2. Software that are specific to a group within the company can be limited for access to that group. For example, R&D, design software, etc. is intended for certain groups and can access can be limited by user. This most likely is known at the time of the purchase.
3. Software used in production or other facilities: Software that could be used in areas such as manufacturing. shipping, etc. may be purchased by IT or someone in operations may be responsible for purchasing the software. Therefore there is a possibility that the users may not be in the same jurisdiction as the billing address.

A lot of the discussion I've had was around how easy/difficult it would be to pull and maintain the type of information the DOR is requesting.

Some things it seems maybe we should give more thought to:

1. Would the DOR be willing to establish a safe harbor position that software that should be allocated can be done so on using an employee headcount allocation? Should that headcount be US or global? Given the potential for a hybrid environment, should the basis be the business location the individual is assigned to? As it's a safe harbor, should it be recalculated each year and apply to purchases made in that particular? Would everyone be willing to agree that any safe harbor percentage change not be retroactively applied for either refund or assessment?
2. If any taxpayer would like to use a percentage other than the safe harbor they would have to be able to document that percentage to the DOR and the DOR would have the ability to review that calculation.
3. The DOR is stating some software, such as accounting software, may not be apportionable. We should have some discussion around how to determine if software should not be apportioned. I personally think that should be determined on a case by case basis. While SAP and Oracle may be viewed as "accounting" software, they are not solely for accounting purposes and are intended for other uses within the enterprise. Maybe software such as Vertex or OneSource would be viewed differently. And if a software is cloud based as opposed to on premise, should it automatically default to be subject to allocation?
4. Will the DOR agree that if a vendor is presented an exemption certificate claiming a MPU percentage the DOR will not challenge the vendor for having an properly executed form.
5. The above should apply to both refunds requests and audit assessments

Please feel free to comment and "beat up" the above.

If you all can let Alex know your responses before in the next day or two that would be appreciated.

Thanks

Mark

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Sent: Wednesday, April 20, 2022 10:28 AM
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Subject: [EXTERNAL] RE: Following up RE: 3-23-22 PICPA SUT TLC Call

Good afternoon,

Following up to see if anyone has feedback they'd like to share on the Pa. DOR Software Sourcing Rules issue. We have a call scheduled on Wednesday, April 27th at 1:00pm. Please share any feedback prior to next week's call so we can discuss.

Best,
Alex

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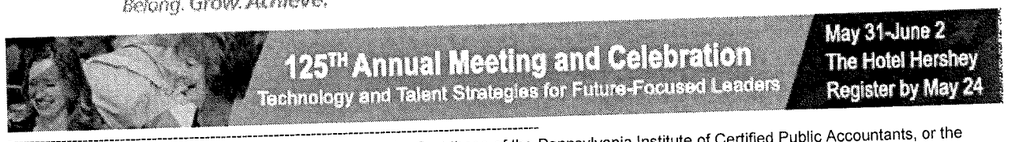

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From: Alexandra Fabian
Sent: Thursday, March 24, 2022 3:01 PM
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Subject: Following up RE: 3-23-22 PICPA SUT TLC Call

Good afternoon,

As a follow up to our call yesterday – please share any feedback on the PA DOR Software Sourcing Rules issue with Peter or I. We are planning to discuss comments we'd like to share with the DOR on our next call. We are aiming to schedule one end of next month (Annette reached out to collect availability).

Best,
Alex

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Subject: RE: Updated: 3-23-22 PICPA SUT TLC Mtg. Agenda

Hi folks,

Here is some more background information regarding the PA DOR Software Sourcing Rules discussion for next week's meeting:

March 17, 2022

Feedback from the PA DOR-Revenue Tax Audit Program Administrator, Ben Turek:

Good morning everyone,

I wanted to pass along some updates concerning documenting out-of-state software use.

The first update is concerning the Pennsylvania Exemption Certificate (REV-1220). The REV-1220 has been updated to specifically include a line relating to out-of-state software use. The presumption remains that software billed to an address in PA is 100% subject to PA sales tax unless the vendor receives a properly completed exemption certificate that includes the total number of licenses purchased and the total number of licenses used outside of PA. The taxable percentage would calculated by: $\frac{(\text{Total Number of Licenses} - \text{Total Licenses used Outside of PA})}{\text{Total Number of Licenses}}$

. Software will not always be sold with what are often called "seated" license, which is where an individual is named for each license sold. In those cases the form should list all of the potential users of the software and all of the potential out-of-state users. When reviewing the sales of vendor, if the form is complete it should be considered as accepted in good faith unless the invoice or contract would give you a reason to believe that the exemption certificate is incorrect.

The other document that is attached is a template that is to be used when a taxpayer is requesting a refund of taxes paid for software used in other states. The taxpayer will need to complete the attached template and provide all of the information contained in the instructions. When agreeing to allow a refund, it is important that we verify the accuracy of the users, for location as well as actual use of the software. An example would be a taxpayer claiming a refund for their accounting software. It is unlikely that all of the taxpayers are actually using this type of software, it is probably a smaller group. It is important to understand how the software is being used and who is actually using it. When completing the template, they will need to provide a user study/breakdown of employees by state and selected employee information should be verified to payroll records or wage/unemployment tax forms. Please remember that in any audit where we are granting refunds for software used in another state, the records supporting the out-of-state use and invoices for the purchases should be sent to the division on an Additional Headquarters Processing Request. This template should also be used as a customer exemption statement when assessing sales tax on the taxpayers nontaxed sales of software to their customers when they indicate that the software is used in multiple states. This template is also going to be used by the Board of Appeals when granting similar refunds, so our approach should now be consistent.

Thanks,
Annette

From: Annette Knapp
Sent: Wednesday, March 16, 2022 12:40 PM
Subject: Updated: 3-23-22 PICPA SUT TLC Mtg. Agenda

Good afternoon,

Attached you'll find the updated Wed., March 23 Sales and Use Tax Thought Leadership Committee meeting agenda and a handout on the *Quality Driven Copack, Inc. vs. Commonwealth of PA* decision. We've added a PA DOR Software Sourcing Rules discussion.

This Microsoft Teams meeting will begin at 2:30 p.m.

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Please let me know if you need anything else.

Thanks,
Annette

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