

Apportionment

Philadelphia Suddenly Shifts to Single Sales; Advisers Say Take Advantage of Ambiguity

Tax advisers in Philadelphia are advising clients that the city's sudden switch to sales-factor-only apportionment may not hold up under scrutiny, and some say they are taking advantage of the ambiguity to benefit clients when filing their 2015 returns.

"We're being expedient," Mark Zinman, a CPA and managing partner of Zinman & Co. P.C. in Southampton, Pa., told Bloomberg BNA March 3. "For those clients where it would be beneficial, we're doing single; for those where it wouldn't, we're doing it the old way."

The new method of calculating Philadelphia business income and receipts tax (BIRT) took effect Jan. 19 for tax years beginning in 2015. The new rule, which could make some tax bills soar, requires all taxpayers doing business in the city to calculate the apportionment of net income using a single sales factor instead of a three-factor method including property and payroll—a method the city had used for decades.

Unlawful Fiat. The city's outgoing revenue commissioner, Clarena I. W. Tolson, filed the proposed regulatory change with the Department of Records in December during the final days of Mayor Michael Nutter's (D) administration, and by law it automatically became effective 30 days later because no one requested a hearing. The new Philadelphia mayor, Jim Kenney (D), was inaugurated Jan. 4.

In a client alert March 3, ReedSmith LLP argues that the change to single-factor apportionment is "an unlawful exercise of lawmaking power by the Revenue Commissioner" and advises taxpayers to consider continuing to use the three-factor formula using property, payroll and sales.

"We argue that the city's switch to a single sales factor was unlawfully done by administrative fiat," wrote Kyle O. Sollie and Stephen J. Blazick, partners in the state tax group in the firm's Philadelphia office.

Word of Caution. Not all tax advisers agree.

"The taxpayer should realize that filing using the three-factor [method] will open them up to an assessment by Philadelphia, since I am sure the City will want to keep the additional revenues associated with the change to single factor apportionment," said Jason C.

Skrinak, a CPA and SALT practice leader in the Tax Services Group for Reinsel Kuntz Leshner LLP in Harrisburg. "From a state perspective, I have never seen a taxpayer successfully argue that changing to a single or more heavily weighted sales factor was improper."

30 Years. ReedSmith argues that under Pennsylvania law, apportionment is a policy choice that must be decided by the Legislature—either the state's General Assembly or Philadelphia's City Council. Without any change of state or city law, the outgoing mayor and revenue commissioner changed 30 years of tax policy, they wrote. "After 30 years of giving 'due regard' to property and payroll, they have decided to give it no regard whatsoever."

"A change on this scale is rare," Sollie told Bloomberg BNA March 3. The regulation, if valid, would most adversely affect out-of-city taxpayers with payroll and property outside the city, according to ReedSmith. Under the new rules, out-of-city taxpayers could see their tax bills triple.

Philadelphia imposes a 6.41 percent BIRT on top of the state's 9.99 percent corporate net income tax, ReedSmith notes.

Best of Ambiguity. Zinman told Bloomberg BNA that he agreed with ReedSmith, and expected the regulation would eventually be challenged. The three-factor method, he said, "is used for everything," and he doubted that Philadelphia could unilaterally change the formula without help from the state. "I don't think it's going to hold up," he said.

Until confusion is resolved, he plans to use the new rule to his clients' advantage, he told Bloomberg BNA. "If the law is ambiguous, you can take the best position for the client—as long as you tell the client," he said.

By LESLIE A. PAPPAS

To contact the reporter on this story: Leslie A. Pappas in Philadelphia at lpappas@bna.com

To contact the editor responsible for this story: Ryan Tuck at rtuck@bna.com

□ The ReedSmith alert is at <http://src.bna.com/c2U>.

The Philadelphia regulation is at <http://src.bna.com/c2V>.

For additional discussion of apportionment in Pennsylvania, see *Corporate Income Tax Navigator*, at Pennsylvania 6.

To request permission to reuse or share this document, please contact permissions@bna.com. In your request, be sure to include the following information: (1) your name, company, mailing address, e-mail and telephone number; (2) name of the document and/or a link to the document PDF; (3) reason for request (what you want to do with the document); and (4) the approximate number of copies to be made or URL address (if posting to a website).
