

ISSUE BRIEF

SENATE POLICY DEVELOPMENT AND RESEARCH OFFICE

PREPARED IN CONJUNCTION WITH THE SENATE REPUBLICAN POLICY COMMITTEE

State Tax Changes - 2008

Introduction

In February of 2008, Governor Rendell proposed approximately \$230 million in new taxes and fees as part of his 2008-09 budget proposal. The proposed tax changes included the following:

- Capital Stock and Franchise Tax Rate Increase — modify the CSFT rate reduction schedule by increasing the 2009 rate from 1.89 mills to 2.49 mills and the 2010 rate from 0.89 mills to 1.02 mills. FY 2008-09 tax increase on business would be approximately \$40 million.
- Cigarette Tax Rate Increase — increase the tax rate by 10 cents per pack. FY 2008-09 approximate cost to taxpayers of \$66.1 million.
- Tobacco Products Tax — impose a new tax at 36 cents per ounce for smokeless and loose tobacco and the equivalent of 36 cents per 10 cigars and cigarillos. FY 2008-09 approximate cost to taxpayers of \$48 million.
- Flood Tax — impose an assessment of 7 cents per \$100 on property insurance premiums paid by individuals purchasing flood insurance for structures located in flood plains. FY 2008-09 approximate cost to taxpayers of \$3.2 million.
- Electricity Tax — impose a Systems Benefit Charge of 1/20th cent per kilowatt-hour of electricity consumption — a cost of 45 cents per month for the average household. FY 2008-09 approximate cost to taxpayers of \$75 million.

Following up on last year's successful 7-for-7 stand against the Governor's proposed tax increases, the Senate Republicans were again successful in ensuring that the 2008-09 budget did not include any new taxes. However, a number of bills affecting taxation at the state or local level were passed by the General Assembly during 2008. A description of these measures follows.

State Level Tax Changes

[House Bill 377](#) (Evans) — signed into law as Act 66 of 2008 — amended the Tax Reform Code of 1971 with three provisions.

Personal Income Tax

- **Breast and Cervical Cancer Research check-off** — This check-off will remain on the Personal Income Tax form; however, the contributions deducted from refunds by the Department of Revenue will be transferred to the Pennsylvania Breast Cancer Coalition instead of the Pennsylvania Cancer Control, Prevention and Research Advisory Board within the Department of Health. (Effective immediately)
- **Alternative Special Tax Provisions for Poverty Study** — The Joint State Government Commission was directed to conduct or provide for a comprehensive study to determine whether alternative forms of personal income tax forgiveness would be more beneficial to low-income Pennsylvanians. The study will include a comparison between Pennsylvania's existing special tax provisions for poverty and the federal earned income tax credit concept. The study will consider any effects of linking the alternative special tax provisions for poverty to federal law, including any misuse in the federal program and any difference in fiscal costs to the Commonwealth. The Commission will present a report after August 1, 2009 and before September 1, 2009. (Effective immediately)

Tax Credits

- **Volunteer Responder Retention and Recruitment Tax Credit** — Provides for a \$100 tax credit against the personal income tax for active volunteer firefighters and active volunteer emergency medical services workers. For the 2008 tax year, an active volunteer is entitled to a maximum credit of \$100. If the taxpayer is not an active volunteer for the entire year, the amount of the credit will be prorated. A taxpayer who claims a credit but fails to meet the requirements would be required to repay the full amount of the credit. The total amount of tax credits authorized could not exceed \$4.5 million. The State Fire Commissioner and the Director of the Emergency Medical Services Office in the Department of Health are responsible for developing a system to establish requirements designating firefighters and emergency medical services providers as active volunteers. No later than June 1, 2009, the Department of Revenue is required to report to the General Assembly on the tax credits granted and the applicability of the tax credit to the retention of active volunteers. (Effective immediately)

[House Bill 1067](#) (Mann) — signed into law as Act 61 of 2008 — amended numerous sections of the Public School Code of 1949. Three of these changes dealt with the Educational Improvement Tax Credit. (Effective immediately)

Educational Improvement Tax Credit

- **Section 2002-B. Definitions** was amended to add a “pass-through entity” to the definition of a “business firm” for the purposes of applying for a tax credit under the Educational Improvement Tax Credit program. The program allows business firms to receive tax credits for certain contributions made to non-profit, scholarship and educational improvement organizations. A pass through entity is either a partnership, which means a domestic or foreign general partnership, joint venture, limited partnership, limited liability company, business trust or other unincorporated entity that for Federal income tax purposes is classified as a partnership, or a Pennsylvania S corporation, which means any small corporation, which has not had a valid election to not be taxed as a Pennsylvania S corporation.

If unused tax credits are not used, the pass-through entity may transfer, with approval, all or a portion of the credit to shareholders, members or partners in proportion to the share of the entity’s distributive income to which the shareholder, member or partner is entitled.

- **Section 2005-B. Tax Credit** was amended to increase the amount of the tax credit under the program for contributions made to a scholarship or educational improvement organization for a single business firm from \$200,000 to \$300,000 annually. Also, the amount of the tax credit for contributions made to pre-kindergarten scholarship organizations was increased from \$100,000 to \$150,000 annually.
- **Section 2006-B Limitations: Tax Liability** was amended to clarify that a tax credit granted to a pass-through entity for any taxable year may not exceed the tax liability of the pass-through entity and its shareholders, members or partners. For additional information on the school funding legislation, please see the *FY 2008-09 Education Funding Issue Brief*.

Keystone Opportunity Zones

[Senate Bill 1412](#) (Pippy) — signed into law as Act 79 of 2008 — amends the Keystone Opportunity Zone (KOZ), Keystone Opportunity Expansion Zone (KOEZ) and Keystone Opportunity Improvement Zone (KOIZ) Act (Act 92 of 1998). (Effective immediately)

Among other modifications, the bill provides for the extension of the tax exemptions, deductions, abatements or credits for certain unoccupied parcels in existing zones. If a political subdivision applies by June 30, 2009, the Department of Community and Economic Development would be authorized to extend all tax exemptions, deductions, abatements or credits for any parcel that is unoccupied on the effective date of the amendment, as follows:

- in a KOZ, KOEZ, or KOIZ for a period of seven years from the expiration date of the zone; or
- in a KOZ or KOEZ for a period of ten years from the date of occupancy, provided that the parcel is occupied on or before December 31, 2015.

The extensions, except authorized exemptions for the sales and use tax, take effect only upon occupancy. The legislation further permits a political subdivision to apply for and the Department to grant a request to add up to 15 acres of deteriorating property to an existing KOEZ, KOIZ, or a subzone of a KOZ for parcels that are contiguous to the existing zone or subzone.

The legislation also permits the Department to designate up to 15 additional Keystone Opportunity Expansion Zones provided that a political subdivision makes application for designation as a new KOEZ no later than May 1, 2009 and meets the criteria outlined in the legislation. Persons and businesses within an additional KOEZ would be entitled to all tax benefits, for a period of ten years beginning January 1, 2010 and ending December 31, 2020.

Additional provisions would prohibit a person or a business that receives a tax exemption, deduction, abatement or credit under the Act from knowingly permitting the labor services of an illegal alien under a contract to which the person or business is a party in the applicable KOZ, KOEZ, or KOIZ. Full repayment of the value or amount of the tax exemption, deduction, abatement or credit would be required if:

- the person or business is sentenced under federal law for an offense involving knowing use of labor by an illegal alien; or
- if a contractor to a person or business that received the tax exemption, deduction, abatement or credit is sentenced under federal law for an offense involving use of labor by an illegal alien and the person knew or had reason to know of the contractor's knowing use of such labor.

The legislation also provides an exemption from the sales and use tax for construction materials used within a zone, prohibits certain payments by businesses to municipalities for zone designation, and further clarifies apportionment of income for the purposes of the Corporate Net Income Tax and the Business Gross Receipts Tax. For additional information on the Keystone Opportunity Zones legislation, please see the *Keystone Opportunity Zones Issue Brief*.

Alternative Energy Production Tax Credit

[2007-08 Special Session #1, House Bill 1](#) (DePasquale) — signed into law as Act 1 of 2007-08 Special Session #1 — creates the Alternative Energy Investment Act. One of the provisions of the Act establishes the Alternative Energy Production Tax Credit Program.

- As a general rule, a taxpayer who develops or constructs an alternative energy production project located in the Commonwealth with a useful life of at least four years may apply for a tax credit.
- An eligible taxpayer will receive a tax credit for the taxable year in an amount equal to 15 percent of the total amount of all development, equipment and construction costs paid for the project (minus any grant or other subsidy received from a federal, state or local government entity), not to exceed \$1 million for each taxpayer in the taxable year.
- Taxpayer credits that are not used for the taxable year can be carried over to the next taxable year with certain established requirements. With approval by the Department of Environmental Protection, a taxpayer may sell or assign an alternative energy production tax credit.
- Tax credits are limited and may exceed: 1) \$5 million in fiscal years 2008-09 through 2011-12;
- 2) \$8 million in fiscal year 2012-13; 3) \$10 million in fiscal years 2013-14 through 2014-15; and 4) \$2 million in fiscal year 2015-16. A total of \$50 million is authorized over the eight year period..
- No later than September 1 of each year, the Department of Environmental Protection is required, in conjunction with the Department of Revenue, to submit a report to the General Assembly summarizing the effectiveness of the tax credit. The report must include the name of each taxpayer utilizing the credit, the amount of credits approved or utilized by each taxpayer and other specified information.