

**SENATE APPROPRIATIONS COMMITTEE
FISCAL NOTE**

BILL NO. House Bill 17

PRINTER NO. 2900

AMOUNT

See Fiscal Impact

FUND

General Fund

DATE INTRODUCED

January 28, 2019

PRIME SPONSOR

Representative Ryan

DESCRIPTION AND PURPOSE OF BILL

House Bill 17, as amended, amends the act of March 4, 1971 (P.L.6, No.2), known as the Tax Reform Code of 1971, by providing for a Sales and Use Tax exclusion for canned computer software directly used by a financial institution conducting the business of banking. The legislation also amends section 3003.22 to authorize a financial institution data match mechanism and adds new sections 3003.23 and 3003.24 to Article XXX (relating to general provisions) with regard to the period of time for the collection of assessed taxes and for criminal tax prosecutions.

Sales and Use Tax Exclusion

House Bill 17, as amended, amends section 204 of the Tax Reform Code of 1971 (relating to exclusions from tax) by adding a Sales and Use Tax exclusion for the sale at retail or use by a financial institution of canned computer software directly utilized in conducting the business of banking. The term "financial institution" means an institution doing business in the Commonwealth subject to the Bank and Trust Company Shares Tax or the Mutual Thrift Institutions Tax.

Under current law, Sales and Use Tax is imposed on canned computer software (i.e. software available for purchase "off-the-shelf"), but it is not imposed on custom computer software, which is categorized as non-taxable computer services. In recent years there has been confusion and disagreement between the Department of Revenue (department) and taxpayers with regard to the taxability of core computer processing and information services purchased by financial institutions to be used in transactions with customers and service providers. The Sales and Use Tax exclusion specified in House Bill 17 clarifies the taxability of computer software and services used in the business of banking.

Financial Institution Data Match Program

House Bill 17, as amended, amends section 3003.22 of the Tax Reform Code of 1971 (TRC) to authorize the department to enter into agreements with financial institutions, and for financial institutions to share with the department, certain bank account information for purposes of delinquent tax collections through a mechanism generally known as a Financial Institution Data Match (FIDM). The legislation is designed to increase the effectiveness of the existing bank attachment mechanism which allows debtors to collect delinquent liabilities directly from an individual's or

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business' bank account on a case-by-case basis. The FIDM legislation provides a well-tested structure for obtaining account information from multiple financial institutions on a regular basis. FIDM has been part of Pennsylvania's Department of Human Services' bank attachment process to collect delinquent child support payments for many years.

House Bill 17, as amended, requires the department, within five days after notifying a financial institution to attach an account, to send a notice to the obligor (i.e. delinquent taxpayer) by first class mail informing the obligor that the department has ordered a financial institution to attach the amount of the tax lien owed from one or more of the accounts of the obligor. An obligor, a financial institution, or an account holder of interest may challenge the actions of the department by filing a petition with the court of common pleas within ten days of the notice. The legislation provides legal immunity such that a person, government agency or financial institution operating in good faith shall not be subject to any civil or criminal liability for providing, reporting and matching information and data or encumbering or surrendering assets as required by law.

An "obligor" is defined as an entity engaged in a business, a sole proprietor, a shareholder, member or partner of a pass-through entity, or a corporate officer whose corporate employer has been assessed for trust fund taxes, which are subject to a Commonwealth tax lien totaling at least \$1,000.

The legislation specifies that accounts, funds, and property subject to attachment under the FIDM program shall not include the following:

1. An account subject to a security interest, control agreement or pledged security for a loan or other obligation;
2. Funds or property deposited to an account after the time that a financial institution initially attaches the account;
3. An account that a financial institution has a present right to exercise a right of setoff either under an agreement between the financial institution and the obligor or otherwise under applicable law;
4. An account that has an account holder of interest named as an owner on the account;
5. An account that an obligor does not have an unconditional right of access; or
6. An account that may not be attached under federal law.

Time Period for Collection of Assessed Taxes

The legislation adds new section 3003.23 to the TRC, which provides that for all taxes administered by the Pennsylvania Department of Revenue, except for the Inheritance Tax, the department may collect the tax owed if collection commences within ten years of the date the settlement, determination or assessment of the tax becomes final. The term "tax" is defined as a tax, interest, addition to tax, penalty, fee and other cost, including the cost of collection.

For non-filed returns, the department is required to induce the filing of a return, or to settle, determine or assess the tax liability of a non-filed tax period within ten

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years of the tax return due date. The filing of a tax lien shall not extend the ten-year period to collect a tax.

The changes implemented by House Bill 17 to establish a ten-year collection period do not affect the department's ability to collect taxes at any time under the following circumstances:

1. For trust fund tax liabilities a taxpayer either collected or withheld (e.g. sales and use tax and employer withholding tax), as an agent of or in trust for the Commonwealth, but willfully failed, grossly neglected or refused to remit;
2. Where a taxpayer files a false and fraudulent tax return or report;
3. Where a taxpayer willfully fails to file a tax return or report as required by law;
4. Where a taxpayer attempts to evade or defeat a tax;
5. For a tax offense for which a taxpayer has been criminally charged and convicted in which tax liabilities remain unpaid; or
6. For liabilities of eligible taxes unknown to the department that have not been extinguished within a ten-year period prior to the commencement of the tax amnesty period of a subsequently enacted or approved tax amnesty program.

The legislation requires that the collection expiration date be tolled for the time when any of the following events are pending, plus one year:

1. During a bankruptcy or proceeding during which the taxpayer's assets are in the control or custody of an administrative body, court or duly appointed guardian, receiver or trustee;
2. The period during which a taxpayer's offer-in-compromise is under consideration by the department;
3. The duration of an installment agreement or deferred payment plan between the taxpayer and the department;
4. The duration, from commencement through final determination, of a proceeding which constitutes a tax appeal or which opposes a collection action before an administrative tribunal or court of law or in which the taxpayer has filed a lawsuit or brought a cause of action against the department;
5. The duration of a taxpayer's military service for which the taxpayer is eligible for and has received a federal extension; or
6. For a period of time as the taxpayer and the department may agree, in writing, to extend the collection expiration date.

Time Period for Criminal Tax Prosecutions

House Bill 17 adds new section 3003.24 to the TRC to establish a time limit on criminal tax prosecutions such that a person shall not be prosecuted, tried or punished for an offense under a tax statute administered by the department except if prosecution is instituted within three years after the commission of the offense. Regardless of the three-year time period, a prosecution may be instituted under the following circumstances:

1. An offense a material element of which is either fraud or a breach of fiduciary obligation within one year after the discovery of the offense. However, this provision does not extend the time period otherwise applicable by more than two years.

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2. The offense of willfully attempting to evade or defeat a tax or the payment of a tax within one year after the discovery of the offense. However, this provision does not extend the time period otherwise applicable by more than two years.

In addition to a criminal offense identified in the tax statutes administered by the department, a person may be prosecuted for an offense provided for under 18 Pa.C.S. (relating to crimes and offenses), regarding misconduct under the tax statutes, if the prosecution is instituted within five years after commission of the offense. A taxpayer convicted of a tax-related offense is required to pay the department restitution of each tax liability for which a conviction has been entered.

The addition of sections 3003.23 and 3003.24 shall not relieve a person of a tax, interest, addition to a tax, penalty fee and other cost payable by the person on the effective date of the act. If a court determines that a tax cannot be settled, assessed or collected under the procedure provided for in the legislation, the matters shall be settled under the laws in force prior to the effective date of this act.

With regard to the addition of section 3003.23 relating to the time period for collection of assessed taxes, the ten-year collection period shall begin on the effective date or when the settlement, determination or assessment becomes final, whichever is later.

House Bill 17 provides that a tax lien created prior to January 1, 2021, shall not be impaired, shall remain in full force and effect and shall retain the priority under the provision imposing the tax lien, without the necessity of refileing or revival, until January 1, 2031.

The addition of section 204(73) regarding the Sales and Use Tax exclusion on computer software applies immediately to the sale at retail or use of canned software by financial institutions. The legislation requires the department to develop guidelines prior to requesting information or attaching an account under the FIDM program; therefore, implementation of the FIDM program will be temporarily delayed until the guidelines are issued. Section 3003.23 of the act shall take January 1, 2021, and the addition of section 3003.24 relating to criminal tax prosecutions shall take effect immediately.

FISCAL IMPACT:

The Department of Revenue indicates that the Sales and Use Tax exclusion for canned computer software directly used by financial institutions in the business of banking will reduce General Fund revenues by approximately \$5 million per fiscal year once fully implemented. Because the provision is effective immediately, House Bill 17, as amended, may result in a revenue loss of approximately \$2.5 million for the remainder of fiscal year 2019-20.

Implementation of the FIDM program is expected to generate additional General Fund revenues of approximately \$2 million per fiscal year by increasing the department's ability to effectively and efficiently collect delinquent taxes that are subject to a tax

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lien. Because account attachments cannot occur until guidelines are issued, the FIDM program is likely to generate little revenue during the current fiscal year. The legislation specifies that financial institutions are entitled to payment from the department in the amount of \$250 per quarter (\$1,000 per year) to reimburse the financial institutions for the cost of conducting data matches. This cost will be offset by the increased delinquent tax collections resulting from FIDM.

The addition of section 3003.23 will have no fiscal impact on Commonwealth funds in near-term fiscal years because implementation of the ten-year period to collect assessed taxes begins January 1, 2021. Beginning with assessments issued on January 1, 2021 and thereafter, the Department of Revenue will have ten years to collect the amounts due from assessments, so the legislation’s fiscal impact in this regard will be delayed for some time. The legislation provides that changes to the time period for collections shall not relieve a person of tax liabilities owed on or prior to the effective date of the act. Therefore, pre-existing tax liabilities and delinquencies can continue to be collected in the same manner as under current law.

Based upon historical collections data, the department estimates that House Bill 17 will decrease General Fund revenue by \$15 million per fiscal year ten years after the January 1, 2021 effective date.

Under current law, there is no expiration as to when the department can collect delinquent taxes. According to the department, the following amounts were collected from payments that were more than ten years past due:

Fiscal Year	Revenue Collected from Payments More Than 10 Years Past Due
2017-18	\$9.7 million
2016-17	\$14.0 million
2015-16	\$15.0 million

The primary purpose of extending the time for criminal tax offenses by adding section 3003.24 to the TRC is to protect collected trust fund taxes totaling \$20 billion per year, and the indirect effect of the threat of prosecution for stealing such taxes encourages greater compliance by taxpayers. For a similar proposal supported by the department in 2017, it estimated that additional revenues attributed to augmenting the time period for criminal tax offenses would generate \$1 million to \$3 million annually depending upon staffing levels committed to this purpose.