SENATE APPROPRIATIONS COMMITTEE FISCAL NOTE

BILL NO. Senate Bill 671

PRINTER NO. 671

AMOUNT

No Fiscal Impact
See Fiscal Impact
See Fiscal Impact

FUND

General Fund
Property Tax Relief Fund
Local Funds

DATE INTRODUCED

April 28, 2023

PRIME SPONSOR

Senator Farry

DESCRIPTION

Senate Bill 671 amends the act of December 31, 1965 (P.L.1257, No.511), known as the Local Tax Enabling Act (LTEA), as follows:

1. Amends the title of the Local Tax Enabling Act to include cities of the first class;
2. Adds a new Chapter 6 entitled Local Taxes in Cities of the First Class;
3. Prohibits Philadelphia from imposing its tax on salaries, wages, commissions or other compensation on certain nonresidents of the city whose duties or services are performed outside the city;
4. Requires a city of the first class to reimburse school districts and municipalities for credits against local wage taxes claimed by their residents who are subject to Philadelphia's tax on salaries, wages, commissions or other compensation;
5. Repeals the act of August 5, 1932 (Sp.Sess., P.L.45, No.45), referred to as the Sterling Act, and recodifies it into the LTEA; and
6. Repeals section 324 of the Taxpayer Relief Act and places the Sterling Act credit reimbursement to school districts in Chapter 6 of the LTEA.

Prohibition of Tax on Certain Nonresidents of a City of the First Class

Under current law, the Sterling Act authorizes the City of Philadelphia to tax any person, transaction, occupation, privilege, subject and personal property within its city limits so long as such subjects of taxation are not subject to a state tax or license fee. The Sterling Act is the primary source of Philadelphia's authority to levy the wage and net profits tax, mercantile license tax, realty transfer tax, amusement tax and public parking facility tax.

The Local Tax Enabling Act is the enabling statute for most taxing authority of the Commonwealth's political subdivisions. Senate Bill 671 repeals the Sterling Act and recodifies it into the LTEA by adding a new Chapter 6 relating to local taxes in cities of the first class. In addition, Chapter 6 includes a new subsection 601(b), which prohibits Philadelphia from imposing its tax on salaries, wages, commissions or other compensation on a nonresident individual who is employed by an employer whose place of business is located in a city of the first class and who performs all employment duties or services outside of Philadelphia. Furthermore, if a nonresident individual performs a portion of his or her employment duties or services outside of Philadelphia, the city may impose a wage tax only on that portion of wages attributable to duties performed within the city.

Senate Bill 671 stipulates that for purposes of new subsection 601(b) relating to the prohibition of wage tax on nonresidents of Philadelphia, an employment duty or service is deemed to be performed where the employee is physically located, notwithstanding any electronic device, computer network or other technology that connects the employee to a person or premises located in a city of the first class.

Reimbursement to School Districts and Municipalities

The legislation adds section 604 with regard to reimbursements, which applies only to a taxpayer who is a resident of this Commonwealth and not a resident of a city of the first class but who is subject to the wage tax imposed by a city of the first class under Chapter 6.

Senate Bill 671 requires that payment of Philadelphia's wage tax by a nonresident of the city shall be credited by a school district and municipality of the taxpayer's residence at an amount no greater than the tax imposed on wages by the school district and municipality in which the taxpayer resides. Additionally, the legislation requires affected employers to make quarterly reports to Philadelphia conveying the amount of wage tax imposed by the school district and municipality where a taxpayer resides. Utilizing this information, the Department of Education and the Department of Community and Economic Development shall promulgate temporary regulations delineating procedures necessary to calculate the aggregate amount of tax credited by each school district and municipality, respectively.

The Department of Education and the Department of Community and Economic Development shall certify the amount of credits calculated to the city of the first class, and the amount certified shall be paid by the city to the school district and municipality of residence of each taxpayer within 30 days of receipt of certification.

Repeals and Applicability

The legislation repeals the act of August 5, 1932 (Sp.Sess., P.L.45, No.45) and provides that all activities initiated under the Sterling Act shall continue and remain in full force and effect and may be completed under Chapter 6 of this act, with the exception of changes made regarding prohibition of tax and reimbursements.

Senate Bill 671 also repeals section 324 of the Taxpayer Relief Act in order to effectuate school district Sterling Act credit reimbursements pursuant to this legislation. Under current law, Sterling Act reimbursements are paid annually to school districts from money deposited into the Property Tax Relief Fund.

Reimbursement for school district and municipal credits shall apply for tax years beginning after December 31, 2023. The remainder of the act shall take effect in 180 days or January 1, 2024, whichever is later.

SENATE APPROPRIATIONS COMMITTEE FISCAL NOTE

FISCAL IMPACT:

General Fund

Senate Bill 671 will have no fiscal impact on Commonwealth funds. The requirements placed on the Department of Community and Economic Development (DCED) and the Department of Education (PDE) can be accomplished within each department's existing resources. Under the Taxpayer Relief Act, PDE currently facilitates Sterling Act credit reimbursements to school districts, and the department's duties would be similar under Senate Bill 671. DCED will work in consultation with PDE and will be able to use a similar framework for municipal credit reimbursements.

Property Tax Relief Fund

Beginning in Fiscal Year 2024-25, the Property Tax Relief Fund will no longer be required to fund Sterling Act credit reimbursements to school districts under the Taxpayer Relief Act. The fund will realize a savings of approximately $28 million per fiscal year.

School District and Municipal Funds

Senate Bill 671 will have a positive fiscal impact on municipalities that are currently required to provide their residents with a credit against a municipality's local earned income tax for wage tax paid to Philadelphia. The City of Philadelphia estimates that prohibiting the city from taxing certain nonresident wages and/or requiring the city to reimburse school districts and municipalities for credits claimed against their local income taxes could result in up to a $190 million revenue loss to the city. Any revenue loss to the city under this legislation will be realized as a revenue gain to municipalities that are required to forego local income tax revenue from their residents who pay Philadelphia's nonresident wage tax in lieu of taxes to the municipalities in which they reside.

Under current law, section 317 of the Local Tax Enabling Act requires political subdivisions to allow a credit for payment of the Philadelphia wage tax by residents of a municipality as a deduction from the liability of taxpayers for an earned income tax imposed under authority of the LTEA. Therefore, a political subdivision that provides a credit to its residents who pay the Philadelphia wage tax does not receive earned income tax revenue on these wages. To the extent Philadelphia is prohibited from imposing its wage tax on certain nonresident individuals, those individuals residing in other municipalities located in the Commonwealth will pay local earned income tax to their respective municipalities of residence and will have no credit, or in some instances a lesser credit, for taxes paid to Philadelphia.

In addition, Senate Bill 671 requires a city of the first class to reimburse school districts and municipalities for residents of the Commonwealth who are nonresidents of the city, subject to the Philadelphia wage tax and receive a credit to offset their school district and municipal wage tax liabilities. Presently, the Taxpayer Relief Act funds Sterling Act credit reimbursements to school districts totaling just over $28 million annually. Under this legislation, Philadelphia will now reimburse school districts, and the city will also be required to reimburse municipalities for Sterling Act credits claimed by taxpayers to offset municipal wage tax liabilities. As such, school districts should expect to receive a similar amount of reimbursements as they do currently, but municipalities will begin receiving credit reimbursements not received currently. School districts may potentially realize a reduction in Sterling Act credit reimbursements due to fewer nonresidents of Philadelphia being subjected to the city wage tax. However, increased tax revenue may be received from school district residents who are no longer paying the Philadelphia wage tax and receiving a credit, likely offsetting any reduction.

Typically, most municipalities and school districts each receive half of the revenue generated from local wage taxes. Therefore, if school districts currently receive approximately $28 million for Sterling Act credit reimbursements, municipalities can be expected to receive a similar amount of additional revenue.

City of the First Class Funds

The prohibition of wage tax on certain nonresidents of Philadelphia will have a negative fiscal impact on the City of Philadelphia by prohibiting the city from taxing nonresident employees who perform all employment duties or services outside the city or by allowing the city to tax only that portion of wages related to duties performed in the city by employees who work both inside and outside Philadelphia. Presently, Philadelphia may not be imposing its wage tax on nonresident taxpayers working outside the city, depending upon the circumstances.

The City of Philadelphia provided written testimony to the Senate Republican Policy Committee with regard to a committee hearing held on March 2, 2023, examining the impact of the Philadelphia wage tax on municipalities surrounding Philadelphia. The city indicates that prohibiting Philadelphia from taxing certain nonresident wages would result in a $190 million annual revenue loss to the city. However, this estimate contemplates that all school districts and municipalities that presently do not impose a local wage tax will now authorize a new one percent wage tax in response to this legislation. To the extent that not all school districts and municipalities without a wage tax will impose a new tax on their residents, the $190 million estimate may be overstated.

With regard to reimbursements made to school districts and municipalities, the City of Philadelphia will be required to reimburse these political subdivisions for the amount of credit allowed by a school district or municipality of a taxpayer’s residence. According to the city, the anticipated cost of these reimbursements is captured within the estimate methodology used to arrive at the $190 million revenue loss noted above.