My name is Michael Semes. I have been a partner at Blank Rome LLP, PricewaterhouseCoopers LLP and Ernst & Young LLP. I have also been honored to serve as Chief Counsel in the Pennsylvania Department of Revenue under Governor Tom Ridge and on the transition teams for Governor Ed Rendell and Governor Josh Shapiro. For the last four years I have been a full-time Professor of Practice at the Villanova University Charles Widger School of Law where, among other courses, I teach State and Local Tax Foundations, and Of Counsel BakerHostetler LLP.

You have asked me to respond to the following questions:

*What is the uniformity clause? And why did PA incorporate it into our constitution?*

*How does this constitutional mandate currently impact PA's tax policy and its ability to generate revenue equitably?*

*How could HB 1773 pass constitutional muster to move PA toward a far more equitable tax system?*

My written testimony, upon which I am happy to elaborate in person at the March 1, 2024 House Finance Committee Hearing, will answer the questions above by first providing an abridged history of - and policy background on - the Uniformity Clause. The testimony will then provide a sampling of several relevant Supreme Court of Pennsylvania (SCOPA) cases to illustrate how SCOPA might analyze whether HB 1773 – which "establishes different classes of subjects and imposes different tax rates [of 1.9% and 12%] on each class"[1] - passes Uniformity Clause muster.

### *1. The Uniformity Clause of the Pennsylvania Constitution*

Article VIII of the Pennsylvania Constitution, in relevant part, states:

> § 1. Uniformity of taxation.
>
> All taxes shall be uniform, upon the same class of subjects, within the territorial limits of the authority levying the tax, and shall be levied and collected under general laws.
>
> § 2. Exemptions and special provisions.
>
> (b) The General Assembly may, by law:
>
> . . .
>
> (ii) Establish as a class or classes of subjects of taxation the property or privileges of persons who, because of age, disability, infirmity or poverty are determined to be in need of tax exemption or of special tax provisions, and for any such class or classes, uniform standards and qualifications. The Commonwealth, or any other taxing authority, may adopt or employ such

[1] HB 1773, PN 2178 at page 2, lines 1 -2.

> class or classes and standards and qualifications, and except as herein provided may impose taxes, grant exemptions, or make special tax provisions in accordance therewith. No exemption or special provision shall be made under this clause with respect to taxes upon the sale or use of personal property, and no exemption from any tax upon real property shall be granted by the General Assembly under this clause unless the General Assembly shall provide for the reimbursement of local taxing authorities by or through the Commonwealth for revenue losses occasioned by such exemption[.][2]

### 2. *Why do we have a Uniformity Clause?*

Now, let's turn to a quick history of the Uniformity Clause. This clause was part of a larger package of constitutional provisions in adopting the "Reform Constitution" of 1874, which addressed certain legislative practices Pennsylvanians perceived to provide benefits to "particular individuals, corporations, or groups"[3], that "were not afforded the general public."[4] It has been speculated that Pennsylvania voters enacted the Uniformity Clause as a reaction – at least in part - against the legislature's exempting railroads from tax entirely.[5] For purposes of analyzing the constitutionality of HB 1773, it is also important to note that since in 1874 Pennsylvania voters have twice rejected amendments to allow for graduated tax rates: once in 1913 and again in 1928.[6]

### 3. *Two Personal Income Tax (PIT) cases, which invalidated PIT statutes as violating the Uniformity Clause, are instructive.*

#### a. *Kelley v. Kalodner*, 181 A. 598 (1935).

In *Kalodner*, the Pennsylvania Supreme Court was asked whether the PIT statute enacted in 1935 violated the Uniformity Clause. The 1935 PIT statute: (a)(i) allowed deductions for living expenses of $1,000 for a single person $1,500 for married person; and (ii) $400 for each dependent under eighteen years of age; and (b) imposed PIT at rates ranging from 2.0% to 8% of taxable income violated the Uniformity Clause.[7] The Court quoted *In re Estate of Cope*, 1, 43 A. 79 (1899), a decision in which the Court plainly held: ""A pretended classification that is based solely on the difference in quantity of precisely the same kind of property is necessarily unjust, arbitrary and illegal."[8] Because the 1935 PIT statute "clearly falls within this language . . . it is

---

[2] Pennsylvania Constitution, Article VIII.
[3] *Nextel Communications Mid-Atlantic, Inc. v. Commonwealth*, 729, 171 A.3d 682, 694 n.14 (Pa. 2017), *quoting Pennsylvania State Association of Jury Commissioners v. Commonwealth*, 64 A.3d 611 , 616 n.9 (Pa. 2013).
[4] *Nextel*, 171 A. 3d at 694.
[5] *Nextel*, 171 A. 3d at 694 - 695.
[6] *Nextel*, 171 A. 3d at 694, n. 16.
[7] *Kalodner*, 181 A. 599 – 600
[8] *Kalodner*, 181 A. 602.

unnecessary to elaborate the matter further to show that the proposed [graduated PIT rates] plainly and palpably violates the rule of uniformity." *Id.*[9]

*b. Amidon v. Kane*, 279 A.2d 53 (1971).

Unlike the 1935 statute at issue in *Kalodner*, the Statute at issue in *Amidon* – the PIT provisions in the Tax Reform Code of 1971 – provided for a single rate of tax: 3%. The *Amidon* statute, however, imposed the PIT "[f]or the privilege of receiving, earning or otherwise acquiring income from any source whatsoever" at the flat rate of 3% on "'taxable income' as defined in the Internal Revenue Code[.]"[10]

Therefore, Pennsylvania "taxable income" is a function of the various adjustments, deductions, and exemptions in the Internal Revenue Code (IRC), which cause "taxable income" to not reflect all income from whatever source. For example, a PIT taxpayer who has a mortgage on her principal residence may deduct her mortgage interest to arrive at her "taxable income" under the IRC. However, a PIT taxpayer who rented would – and otherwise earned the same amount of income – would have more "taxable income" and, therefore, be taxed at a higher effective rate than the one who benefitted from a mortgage interest deduction.

As a result, SCOPA held that tying the definition of 'taxable income' to the IRC definition caused similarly situated PIT taxpayers – i.e., citizens taxed on "the privilege of receiving, earning or otherwise acquiring income from any source whatsoever" – to be taxed at different effective tax rates.[11] Therefore, while the Tax Reform Code of 1971 imposed tax at a flat 3% rate on its face, defining the tax base in a way that granted some taxpayers deductions to which not all were entitled, violated the Uniformity Clause. [12]

***4. A recent SCOPA case reinforced Uniformity Clause precedent and sheds light on the appropriate remedy for a violation.***

The statute at issue in *Nextel Communications Mid-Atlantic, Inc. v. Commonwealth*, 171 A.3d 682 (2017) limited the amount of NLC a CNIT taxpayer was permitted to deduct to the greater of 12.5% of the corporation's taxable income or $3 million. Citing *Cope's Estate*, SCOPA recognized its lengthy Uniformity Clause precedent invalidating arbitrary and unreasonable classifications:

---

[9] The Court went on to quote *Fox's Appeal*, 112 Pa. 337 , 4 A. 149 , 153 , 17 Week. Notes Cas. 449, 43 Legal Int. 214 (Pa. 1886)

> [The Uniformity Clause] was intended to and does sweep away forever the power of the legislature to impose unequal burdens upon the people under the form of taxation. The evils which led up to its incorporation into the organic law are well known. The burden of maintaining the state had been, in repeated instances, lifted from the shoulders of favored classes, and thrown upon the remainder of the community.").

[10] Section 302(q) as originally enacted in the Tax Reform Code of 1971.
[11] 279 A.2d at 55.
[12] 279 A.2d at 57 - 63.

> For over a century, our Court has steadfastly adhered to an interpretation of the Uniformity Clause that classifications based solely upon the quantity or value of the property being taxed are arbitrary and unreasonable, and, hence, forbidden.[13]

SCOPA also confirmed that its uniformity analysis does not stop with the statutory language but examines the effect of that language. SCOPA expressly acknowledged that a statute that "does not explicitly exempt income below a certain threshold from taxation [but] operates in a manner that creates . . . exemption from taxation solely on the basis of income [is] violative of the Uniformity Clause."

Based on this rationale, SCOPA concluded that the CNIT NLC provision violates the Uniformity Clause because it creates two classes of taxpayers: those with more than $3 million of NLC and those with less than $3 million of NLC:

> the NLC, by allowing corporations to take a flat $3 million net loss carryover deduction against their taxable income, has effectively created two classes of taxpayers among corporations which have net loss carryover deductions equal to or exceeding their taxable income. The first and larger class, comprising 98.8% of all corporate taxpayers for tax year 2007, was exempted from paying any corporate net income tax simply because their income was $3 million or less, and a much smaller class of corporate taxpayers, 1.2%, was required to shoulder the entire corporate net income tax burden for that tax year due only to the fact that each of those class members had income in excess of $3 million. Because the NLC has created disparate tax obligations between these two classes of similarly situated taxpayers based *solely* on . . . the amount of each class member's taxable income — it is, as the Commonwealth Court determined, an arbitrary and unreasonable classification which is prohibited by the Uniformity Clause.[14]

Once having invalidated the NLC provision, SCOPA next addressed remedy and noted that it had three options:

> (1) sever the flat $3 million deduction from the remainder of the NLC;
>
> (2) sever both the $3 million and 12.5% deduction caps and allow corporations to claim an unlimited net loss — the remedy chosen by the Commonwealth Court majority; or

---

[13] 181 A. 3d at 696. (emphasis added).
[14] 171 A.3d at 699 (emphasis added).

(3) strike down the entire NLC and, thus, disallow any net loss carryover.[15]

SCOPA analyzed the legislative history of the NLC and the General Assembly's policy goals. After doing so, concluded that severing the flat $3 million NLC cap and leaving the 12.5% cap furthered the legislature's goals of allowing some losses to be deducted while protecting the state fiscal health:

> Thus, the overall structure of the NLC reflects the legislature's intent to balance the twin policy objectives of encouraging investment (by allowing corporations to deduct some of the losses they sustain when making such investments against their future revenues), and ensuring that the Commonwealth's financial health is maintained (through the capping of the amount of this deduction).[16]

5. ***Conclusion.***

The text above summarizes the history and purpose of the Uniformity Clause. It also provides a sampling of more than century of SCOPA's Uniformity Clause precedent.

This summary and sample make clear that SCOPA has not addressed whether the Uniformity Clause permits the General Assembly to create multiple classes of PIT taxpayers as HB 1773 proposes.

It should be observed that subclause 2(b)(ii) of Article VIII expressly limits the Generally Assembly's authority to establish PIT classes for individuals "who, because of age, disability, infirmity or poverty [of the individual] are determined to be in need of tax exemption or of special tax provisions."[17] SCOPA has not interpreted the how much authority this subclause grants to the General Assembly to establish classes of PIT taxpayers. SCOPA could apply well-established rules of statutory construction to conclude that the General Assembly may only establish classes of PIT taxpayers that meet the express parameters of subclause 2(b)(ii). The classes HB 1773 proposes to establish exceed the boundaries subclause 2(b)(ii). Therefore, SCOPA could find that the rules of statutory construction dictate that HB 1773 violates the Uniformity Clause.

Therefore, it reasonable to conclude:

1. SCOPA may find that "personal income is personal income" and, therefore, HB 1773 violates the Uniformity Clause by impermissibly "establish[ing] different classes of subjects and impos[ing] different tax rates on each class"[18]; those who receive income:

---

[15] 171 A.3d at 703
[16] 181 A.3d at 704.
[17] Pennsylvania Constitution, Article VIII, Section 2(b)(ii).
[18] HB 1773, PN 2178 at page 2, lines 1 -2.

a. in the form of compensation and certain types of interest and who are taxed at 1.9%;[19] and
b. from other sources and who are taxed at 12.%.[20]

2. If SCOPA were to find that HB 1773 violated the Uniformity Clause it may choose to:
   a. replace the 12% rate (the provision that violates the Uniformity Clause) with a 1.9% rate so that all types of income would be taxed uniformly;
   b. replace the 1.9% rate with the 12% rate so that all types of income would be taxed uniformly;
   c. strike down both the 1.9% rate and 12% rate and, as it did in *Kalodner* and *Amidon*, strike down the entire PIT statute.

[19] HB 1773, PN 2178 at page 3, lines 3 – 19 and page 4 at lines 8 – 24.
[20] HB 1773, PN 2178 at page 3, lines 3 – 19 and page 4 at lines 8 – 24.

**Pennsylvania Constitution**
**Article VIII**[21]

**Section 1. Uniformity of taxation.**

All taxes shall be uniform, upon the same class of subjects, within the territorial limits of the authority levying the tax, and shall be levied and collected under general laws.[22]

**Section 2. Exemptions and special provisions.**

(a) The General Assembly may by law exempt from taxation:

(i) Actual places of regularly stated religious worship;

(ii) Actual places of burial, when used or held by a person or organization deriving no private or corporate profit therefrom and no substantial part of whose activity consists of selling personal property in connection therewith;

(iii) That portion of public property which is actually and regularly used for public purposes;

(iv) That portion of the property owned and occupied by any branch, post or camp of honorably discharged servicemen or servicewomen which is actually and regularly used for benevolent, charitable or patriotic purposes; and

(v) Institutions of purely public charity, but in the case of any real property tax exemptions only that portion of real property of such institution which is actually and regularly used for the purposes of the institution.

---

[21] Reproduced from:

https://www.legis.state.pa.us/cfdocs/legis/LI/consCheck.cfm?txtType=HTM&ttl=00&div=0&chpt=8

**Adoption.** Unless otherwise noted, the provisions of present Article VIII (formerly Article IX) were adopted December 16, 1873, 1874 P.L.3, effective January 1, 1874. The article number was changed from IX to VIII by proclamation of the Governor of July 7, 1967, P.L.1063.

**Prior Provisions.** Former Article VIII (Suffrage and Elections) was renumbered to Article VII by proclamation of the Governor of July 7, 1967, P.L.1063.

[22] (Nov. 6, 1923, P.L.1117, J.R.1; Nov. 4, 1958, 1957 P.L.1021, J.R.3; Nov. 7, 1961, P.L.1785, J.R.6; Nov. 2, 1965, P.L.1908, J.R.2; Apr. 23, 1968, P.L.App.9, Prop. No.5).

**1968 Amendment.** Section 4 of Proposal No.5 provided that the amendment to section 1 shall take effect as soon as possible but no later than July 1, 1970.

(b) The General Assembly may, by law:

(i) Establish standards and qualifications for private forest reserves, agricultural reserves, and land actively devoted to agricultural use, and make special provision for the taxation thereof;

(ii) Establish as a class or classes of subjects of taxation the property or privileges of persons who, because of age, disability, infirmity or poverty are determined to be in need of tax exemption or of special tax provisions, and for any such class or classes, uniform standards and qualifications. The Commonwealth, or any other taxing authority, may adopt or employ such class or classes and standards and qualifications, and except as herein provided may impose taxes, grant exemptions, or make special tax provisions in accordance therewith. No exemption or special provision shall be made under this clause with respect to taxes upon the sale or use of personal property, and no exemption from any tax upon real property shall be granted by the General Assembly under this clause unless the General Assembly shall provide for the reimbursement of local taxing authorities by or through the Commonwealth for revenue losses occasioned by such exemption;

(iii) Establish standards and qualifications by which local taxing authorities may make uniform special tax provisions applicable to a taxpayer for a limited period of time to encourage improvement of deteriorating property or areas by an individual, association or corporation, or to encourage industrial development by a non-profit corporation; and

(iv) Make special tax provisions on any increase in value of real estate resulting from residential construction. Such special tax provisions shall be applicable for a period not to exceed two years.

(v) Establish standards and qualifications by which local taxing authorities in counties of the first and second class may make uniform special real property tax provisions applicable to taxpayers who are longtime owner-occupants as shall be defined by the General Assembly of residences in areas where real property values have risen markedly as a consequence of the refurbishing or renovating of other deteriorating residences or the construction of new residences.

(vi) Authorize local taxing authorities to exclude from taxation an amount based on the assessed value of homestead property. The exclusions authorized by this clause shall not exceed 100% of the assessed value of each homestead property within a local taxing jurisdiction. A local taxing authority may not increase the millage rate of its tax on real property to pay for these e exclusions.

(c) Citizens and residents of this Commonwealth, who served in any war or armed conflict in which the United States was engaged and were honorably discharged or released under honorable circumstances from active service, shall be exempt from the payment of all real property taxes upon the residence occupied by the said citizens and residents of this Commonwealth imposed by the Commonwealth of Pennsylvania or any of its political subdivisions if, as a result of military service, they are blind, paraplegic or double or quadruple amputees or have a service-connected disability declared by the United States Veterans Administration or its successor to be a total or 100% permanent disability, and if the State Veterans' Commission determines that such persons are in need of the tax exemptions granted herein. This exemption shall be extended to the unmarried surviving spouse upon the death of an eligible veteran provided that the State Veterans' Commission determines that such person is in need of the exemption.[23]

---

[23] (Apr. 23, 1968, P.L.App.9, Prop. No.5; May 15, 1973, P.L.451, J.R.1; Nov. 8, 1977, P.L.361, J.R.1; Nov. 6, 1984, 1982 P.L.1478, J.R.2; Nov. 5, 1985, P.L.556, J.R.2; Nov. 4, 1997, P.L.633, J.R.1; Nov. 7, 2017, 2018 P.L.1197, J.R.1)

**2018 Amendment.** Joint Resolution No.1 of 2017 amended subsec. (b)(vi).
Rejection of Proposed 1989 Amendment. The question of amending subsection (b) to permit local taxing authorities to reduce tax rates on residential real property to the extent of additional revenues obtained from personal income taxes, as more fully set forth in Joint Resolution No.1 of 1989, was submitted to the electors at the municipal election on May 16, 1989, and was rejected. Section 1 of Article XI prohibits the submission of an amendment more often than once in five years.

**1985 Amendment.** Joint Resolution No.2 amended subsec. (c).

**1984 Amendment.** Joint Resolution No.2 of 1982 added subsec. (b)(v).

**1973 Amendment.** Joint Resolution No.1 amended subsec. (b)(i).

**1968 Amendment.** Proposal No.5 renumbered former section 2 to present section 5 and added present section 2. Section 4 of Proposal No.5 provided that section 2 shall take effect as soon as possible but no later than July 1, 1970.