AN ACT

Amending the act of March 4, 1971 (P.L.6, No.2), entitled "An act relating to tax reform and State taxation by codifying and enumerating certain subjects of taxation and imposing taxes thereon; providing procedures for the payment, collection, administration and enforcement thereof; providing for tax credits in certain cases; conferring powers and imposing duties upon the Department of Revenue, certain employers, fiduciaries, individuals, persons, corporations and other entities; prescribing crimes, offenses and penalties," in personal income tax, further providing for definitions and for classes of income.

The General Assembly of the Commonwealth of Pennsylvania hereby enacts as follows:

Section 1. The General Assembly finds and declares as follows:

(1) Pennsylvania instituted the Personal Income Tax (PIT) in 1971 after a constitutional amendment in the late 1960s.

(2) Pennsylvania's PIT is levied against the taxable income of resident and nonresident individuals, estates and trusts, partnerships, S corporations, business trusts and limited liability companies that are not taxed as
corporations for Federal income tax purposes.

(3) Pennsylvania, at the time of the adoption of the constitutional amendment, adopted a "necessary, ordinary and reasonable" rule for the deduction of "all expenses" whether they were for business, farming or unreimbursed employee business expenses.

(4) At the time of the adoption of the constitutional amendment, the Federal Government applied the same "necessary, ordinary and reasonable" rule but currently permits the use of "per diems" to allow business to streamline recordkeeping and to eliminate wasted time during Internal Revenue Service (IRS) audits on businesses and taxpayers.

(5) IRS regulations allow businesses to reimburse their employees for work-related expenses by providing businesses with the option to account for each expenditure or use a per diem rate plan that is based on IRS-established per diem rates for lodging and meals plus incidental expenses.

(6) The Department of Revenue has concluded that "per diems" as adopted by the United States Treasury for the IRS and other branches of the Federal Government are excessive in nature and do not constitute necessary, ordinary and reasonable deductions, which create a financial hardship on Pennsylvania businesses and Commonwealth employees.

(7) It is the intent of the General Assembly to rectify the Department of Revenue's interpretation of the necessary, ordinary and reasonable rule by requiring that the Department of Revenue allow the constitutionally mandated deduction for all ordinary, reasonable and necessary business expenses, including the use of per diems established by the Federal
Government and to promulgate regulations accordingly.

Section 2. Sections 301(d) and 303(a)(1)(i) of the act of March 4, 1971 (P.L.6, No.2), known as the Tax Reform Code of 1971, are amended to read:

Section 301. Definitions.--Any reference in this article to the Internal Revenue Code of 1986 shall mean the Internal Revenue Code of 1986 (Public Law 99-514, 26 U.S.C. § 1 et seq.), as amended to January 1, 1997, unless the reference contains the phrase "as amended" and refers to no other date, in which case the reference shall be to the Internal Revenue Code of 1986 as it exists as of the time of application of this article. The following words, terms and phrases when used in this article shall have the meaning ascribed to them in this section except where the context clearly indicates a different meaning:

* * *

(d) "Compensation" means and shall include salaries, wages, commissions, bonuses and incentive payments whether based on profits or otherwise, fees, tips and similar remuneration received for services rendered, whether directly or through an agent, and whether in cash or in property. The term "compensation" shall include any part of a distribution under a plan described in section 409A(d)(1) of the Internal Revenue Code of 1986 (Public Law 99-514, 26 U.S.C. § 409A(d)(1)), as amended, attributable to an elective deferral of income or the income on any elective deferral of income, whether paid or payable during employment or to a retired person upon or after retirement from service.

The term "compensation" shall not mean or include: (i) periodic payments for sickness and disability other than regular wages received during a period of sickness or disability; or
(ii) disability, retirement or other payments arising under workmen's compensation acts, occupational disease acts and similar legislation by any government; or (iii) payments commonly recognized as old age or retirement benefits paid to persons retired from service after reaching a specific age or after a stated period of employment; or (iv) payments commonly known as public assistance, or unemployment compensation payments by any governmental agency; or (v) payments to reimburse actual expenses, including per diem reimbursements made pursuant to an accountable plan operated in accordance with Federal law; or (vi) payments made by employers or labor unions, including payments made pursuant to a cafeteria plan qualifying under section 125 of the Internal Revenue Code of 1986 (Public Law 99-514, 26 U.S.C. § 125), for employee benefit programs covering hospitalization, sickness, disability or death, supplemental unemployment benefits or strike benefits: Provided, That the program does not discriminate in favor of highly compensated individuals as to eligibility to participate, payments or program benefits; or (vii) any compensation received by United States servicemen serving in a combat zone; or (viii) payments received by a foster parent for in-home care of foster children from an agency of the Commonwealth or a political subdivision thereof or an organization exempt from Federal tax under section 501(c)(3) of the Internal Revenue Code of 1954 which is licensed by the Commonwealth or a political subdivision thereof as a placement agency; or (ix) payments made by employers or labor unions for employee benefit programs covering social security or retirement; or (x) personal use of an employer's owned or leased property or of employer-provided services; or (xi) amounts that are ordinary, reasonable or
necessary business expenses incurred by the taxpayer to the extent the expenses are not reimbursed or are not eligible to be reimbursed by the employer.

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Section 303. Classes of Income.--(a) The classes of income referred to above are as follows:

(1) Compensation.

(i) All salaries, wages, commissions, bonuses and incentive payments whether based on profits or otherwise, fees, tips and similar remuneration received for services rendered whether directly or through an agent and whether in cash or in property except income derived from the United States Government for active duty outside the Commonwealth of Pennsylvania as a member of its armed forces and income from the United States Government or the Commonwealth of Pennsylvania for active State duty for emergency within or outside the Commonwealth of Pennsylvania, including duty ordered pursuant to 35 Pa.C.S. Ch. 76 (relating to Emergency Management Assistance Compact). For the purposes of this subparagraph, the term "compensation" shall not include costs and expenses lawfully deducted.

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Section 3. The following shall apply:

(1) The Department of Revenue shall, within 90 days of the effective date of this section, promulgate temporary regulations that effectively incorporate the regulations at 5 U.S.C. § 5702 and sections 162 and 274(d) of the Internal Revenue Code of 1986 (Public Law 99-514, 26 U.S.C. §§ 162 and 274(d)) to effectuate the amendment of sections 301(d) and 303(a)(1)(i) of the act. The temporary regulations shall not be subject to the following:
(i) Sections 201, 202, 203, 204 and 205 of the act of July 31, 1968 (P.L.769, No.240), referred to as the Commonwealth Documents Law.

(ii) Sections 204(b) and 301(10) of the act of October 15, 1980 (P.L.950, No.164), known as the Commonwealth Attorneys Act.


(2) The temporary regulations shall expire upon the promulgation of final-form regulations or two years following the effective date of this section, whichever is later.

Section 4. This act shall take effect immediately.