



Senate Finance Committee

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BILL SUMMARY

SENATE BILL 1063, PN 1366 (SENATOR EARLL)

This legislation amends the Local Tax Enabling Act to consolidate the collection of earned income taxes at the county-wide level.

Specifically, the purpose of this legislation is to effectuate a reformed local income tax collection system by further providing for the recapture of tax, for register for earned income and occupational privilege taxes, for the collection of taxes, for audits of earned income taxes, providing for the consolidated collection and uniform distribution of local income taxes, for penalties and for costs of delinquent tax collection, making editorial changes, and making repeals.

This legislation would establish various reforms in relation to the collection of earned income tax (EIT) that would consolidate, modernize and introduce uniformity to the collection process. This legislation would consolidate local income tax collection systems on a countywide bases, thereby reducing the number of collectors from 560 to 66 (one for each county) with regard to the collection of taxes on behalf of nearly 2,900 municipalities and school districts. The term "local income tax" is utilized so that these provisions will apply to EIT collection systems and any local personal income tax collection systems that might be established in the future.

Background:

The Center for Local Government Services within the Department of Community and Economic Development (DCED) formed a work group back in 2001 to study EIT collection and released a report in September 2004 (*Pennsylvania Earned Income Tax Collection System, An Analysis with Recommendations – August 2004 Report*) that documented a fragmented and inefficient collection system of 560 tax collectors. While tax collectors processed about \$2 billion dollar annually in local taxes, the 2004 report estimated approximately \$100 million in school district and municipal EIT revenues went uncollected on an annual basis (based on FY 2000-01 data). The Pennsylvania Economy League of Southwestern PA (PELSW) has since developed its own updated estimate based on DCED's methodology, using FY 2004-05 data, and its analysis shows that \$237 goes uncollected annually.

Prior Legislation:

Senate Bill 1063 is a result of a cooperative effort that began in the 2005-06 legislative session with DCED and various stakeholders, which produced the version of House Bill 1427 of the 2005-06 legislative session (Denlinger), PN 4641, which was reported out of the Senate Finance Committee on September 26, 2006.

Similar legislation, House Bill 1550, has also been introduced in 2007-08 session in the House of Representatives by Representative Levdansky, Representative Nickol and Representative Denlinger.

Summary:

Uniformity:

The omissions, ambiguities, and inconsistencies in Act 511 have resulted in different withholding, remittance distribution and reporting or nonresident taxes by tax collectors. These different practices complicate withholding for employers and are largely responsible for the loss of over \$237 in local tax revenues annually. The purpose of uniform withholding, remittance and distribution is to capture the loss of local income tax revenues and to ease the burden of local withholding on employers in Pennsylvania. This is accomplished by creating clarity and uniformity in the statutory process for tax collection and by aligning the flow of tax monies. These changes, in conjunction with better recordkeeping, will simplify withholding for employers and allow taxing authorities and collectors to track every local tax dollar from the time it is withheld to the time it is reported on an employee's W-2 at the end of the year.

Withholding:

Employers will be required to withhold the entire local tax owned by each employee, and to remit those taxes to the tax collector for the tax collection district where the employer's facility is located. The "entire tax owed by an employee" includes the tax levied by the school district and municipality where and employee lives and the nonresident tax levied by the municipality where an employee works.

Uniform withholding will capture virtually all taxes imposed on employees in Pennsylvania, reducing the need to collectors to find and bill taxpayers quarterly or at the end of the year. Uniform withholding will achieve the goal of a zero-local-income tax balance for employees at the end of the year and improve cash-flow for local governments during the year.

Distribution:

Senate Bill 1063 requires uniform distribution, based on quarterly detail, rather than allocations from the prior year. Additionally, the bill requires that collectors distribute taxes within 60 days of receipt or the quarterly employer remittance deadline, whichever is later. In addition to any other information required by DCED, tax collectors must keep records of the amount, date and destination of all taxes distributed. These records must be provided to the collector or taxing jurisdiction to which the taxes are distributed. The requirement that collectors distribute taxes that belong to another district without demand is retained in the legislation.

Remittance:

Employers will be subject to the same basic quarterly remittance requirement, 30 days after the end of each quarter and the frequency of revenue distribution will be 60 days, the same frequency as under current law. The legislation allows a Tax Collection Committee (TCC) to require its collector to distribute more frequently or negotiate with other districts for more frequent distribution. For instance, a committee could require that taxes belonging to

municipalities and school districts within the district be deposited daily in its accounts. Because all taxes will be tracked and a process is established for tax claims, there is much less chance that taxes will be lost in the distribution process. In addition, tax monies that remain unidentified for two years must be paid to the municipality where the tax was collected.

Optional Remittance:

Senate Bill 1063 permits employers with workplaces in more than one county to remit local taxes for all their employees to one district's collector. If they elect this option, they must do so monthly and electronically. If these taxes are collected from outside the taxing jurisdiction of residence or workplace, the tax collector must distribute the taxes within 30 days instead of the standard 60 days under current law.

Tax Collection Districts and Committees:

Under Senate Bill 1063, 66 tax collection districts are created for the purpose of local income tax collection. School districts are included in the county where the majority of the school district population is located. Municipalities are included in the county where their school districts are located. The TCC is created to appoint a tax collector and oversee tax collection in each district. The committee is composed of a delegate and an alternate delegate from each taxing jurisdiction located in the district that imposed a local income tax. The governing body of each taxing jurisdiction appoints delegates and alternates, who must be residents of the taxing jurisdiction they represent. Only delegates appointed by a taxing jurisdiction or their alternate are entitled to vote on actions taken by a TCC.

TCCs are provided flexibility in appointing a tax collector. An existing collector such as a municipality, school district, private company, or non-profit bureau could be chosen to collect the tax. Alternatively, a new non-profit bureau, similar to the bureaus in the 13 counties that are already consolidated, could be created by merging the existing offices of the jurisdictions in a district.

Voting Rights:

Voting rights for each delegate will be weighted based on the proportional population of each political subdivision in proportion to the population of each tax collection district as determined by the most recent official Decennial Census data. Initially, a majority of the delegates is needed for the tax collection committee to establish a quorum and a majority vote of delegates present is needed to take action. Tax collection committees may change voting rights, quorum and action requirements in their bylaws.

Accountability:

There will be an increase in the scrutiny of all taxes that are distributed. Tracking, auditing and oversight of taxes will provide accountability and the financial safeguards needed to restore integrity and transparency to the system.

Tax collector must keep records of every dollar received and distributed and respond to claims for undistributed taxes from other tax collectors or face daily fines. In addition, collectors must submit monthly reports accounting for each dollar or face additional fines. The annual audit

includes a reconciliation of monthly reports and the receipt and disbursement of all tax monies by an independent certified public accountant. Auditors must file and findings if noncompliance with the TCC, the Office of Attorney General, the Office of the Auditor General and DCED. In addition, tax collectors will be required to use standard forms, reports and procedures so that taxes can be tracked from the time they are withheld from an employee's paycheck to the W-2 at the end of the year.

At the same time, TCCs will be required to oversee collectors and improve the dispute resolution process. Each TCC is required to create an appeals board of at least three delegates to hear appeals of determinations by its tax collector concerning the assessment, collection, refund, withholding, remittance or distribution of the income tax. Appeals could be brought by taxing jurisdictions, taxpayers, employers and tax collectors affected by the determinations of the tax collector. This will create an opportunity for all parties, including local governments that are part of a tax collection district, to resolve disputes and differences with a tax collector without going to court, which will speed up the resolution process.

The larger tax collection areas required by this legislation mean that less tax monies need to be transferred among collectors, which reduces the probability that revenue will be lost. In addition, with larger TCCs, there is a much greater chance that an employer will be remitting directly to the tax collector for a municipality of school district, and the municipality of school district will not have to wait the additional 60 days for another district's tax collector to distribute the tax. The larger tax districts will enable the Department of Revenue to coordinate and cooperate more with local tax collectors. The Department of Revenue is required to enter into an agreement with each tax collection district for the exchange of information as necessary for the collection of income taxes.

Enforcement:

Under Senate Bill 1063, tax collectors will continue to utilize existing enforcement tools, and be provided with new tools to prosecute non-filers. Penalties and fines are increased for employers and taxpayers who do not file required reports of who underpay or fail to pay the tax. The penalty on unpaid taxes is increased from 0.5% per month to 1% per month to match the state rate. Maximum fines for violation of the law are increased from \$500 to \$2,500 for each offense, except that employers who do not remit or cannot account for withheld taxes could be fined up to \$25,000. Tax collectors are given specific authority to request and examine a taxpayer's state or federal returns and schedules, but such examination is limited to information pertaining to the local income tax. Employers who do not keep or supply required quarterly and annual records and returns cannot be penalized. Maximum imprisonment time for violations is increased from 30 days to six months. In addition, the Department of Revenue will be required to enter into an agreement with each tax collection district for the exchange of tax information.

Transition:

DCED will calculate the weighted vote for each political subdivision by September 1, 2009. By September 15, 2009, each political subdivision that imposed an EIT prior to July 1, 2009 will appoint one voting delegate and one alternate delegate to the TCC. The first meeting of the TCC will be convened by the chair of the County Commissioners on November 15, 2009. Each TCC shall adopt bylaws no later than April 15, 2010, and by September 15, 2010, each TCC will appoint a tax officer to collect the tax. Senate Bill 1063 also requires that DCED promulgate

temporary regulations establishing uniform forms, reports and returns for taxes levied prior to January 1, 2010. The bill provides full implementation of the new collection system on January 1, 2012. At that point, tax collectors would be required to follow the new distribution and recordkeeping requirements. The legislation also establishes fines and penalties for tax collectors who collect taxes prior to January 1, 2012, and violate the act during the transition.