

ARTICLE V. PERSONAL INCOME TAX

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Authority

The provisions of this Article V issued under the Tax Reform Code of 1971 (72 P. S. §§ 7101—8203), unless otherwise noted.

Source

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CHAPTER 101. GENERAL PROVISIONS

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§ 101.1. Definitions.

The following words and terms, when used in this article, have the following meanings, unless the context clearly indicates otherwise:

Accepted accounting principles and practices—Those accounting principles, systems or practices which are acceptable by standards of the accounting pro-

fession and which are not inconsistent with the regulations of the Department setting forth those principles and practices.

Association—An unincorporated society; a body of persons united and acting together without articles of incorporation but upon the methods and forms used by incorporated bodies, for the prosecution of some common enterprise. The common enterprise shall be the conduct of a business, trade or profession or the view to ultimate enhancement in value of the property of the association which is either to be returned to the members or sold and the profits returned to the members. The term does not include associations that are purely charitable or religious organizations, recreational or social clubs, and similar agencies.

Business—An enterprise, activity, profession, vocation, trade, joint venture, commerce or other undertaking of any nature if engaged in as a commercial enterprise and conducted for profit or ordinarily conducted for profit, whether by an individual, partnership, association or other unincorporated entity.

Cafeteria plan—A plan qualifying under section 125 of the IRC (26 U.S.C.A. § 125).

Casual employe—An individual who performs, or by agreement, refrains from performing, any service of whatever nature and is not an employe.

Casual employer—A person for whom a casual employe performs, or refrains from performing, any service, provided that, if the person does not make the payment of remuneration, the term also includes the person making payment.

Charitable trust—A trust operated exclusively for religious, charitable, scientific, literary or educational purposes.

Claimant—A person who is subject to the tax imposed under this article, is not a spouse or child who derives more than one-half of their total support from another person.

Department—The Department of Revenue of the Commonwealth.

Dependent—A spouse or child who derives more than one-half of his total support during the entire taxable year from another individual. A spouse means a husband or wife. A child means and includes a natural child, an adopted child, a stepchild and a grandchild. A foster child who during the entire taxable year lives in the claimant's home shall be considered to be a child. For purposes of determining support, all sources of income are to be considered, whether taxable income or nontaxable income. Conditions of blindness or old age may not be a factor in determining the number of a claimant's dependents.

Discriminatory plan—A plan that treats highly compensated participants more favorably in coverage, contributions or benefits. In determining whether a cafeteria plan is discriminatory, the special rules of section 125(g) of the IRC apply.

Dividends—A distribution in cash or property made by a corporation, association or business trust out of accumulated earnings and profits, or out of

earnings and profits of the year in which the dividend is paid. The term does not include a return of premium.

Domicile—The place which an individual intends to be his permanent home and to which he intends to return whenever he may be absent.

Employe—An individual from whose wages an employer is required under the IRC to withhold Federal Income Tax. For the purpose of this definition, the terms “employe,” “employer” and “wages” have the same meanings as in Chapter 24 of the IRC (26 U.S.C.A. §§ 3401—3406), relating to collection of Income Tax at source on wages.

Employe welfare benefit plan—

(i) A plan established or maintained to provide to eligible employes or their beneficiaries plan benefits, such as:

(A) Medical, surgical or hospital care or benefits in the event of sickness, accident or disability.

(B) Death benefits.

(C) Scholarships.

(D) Personal expense reimbursements, advancements or allowances such as rental vehicle, dependent care, food or housing allowances.

(ii) The term does not include:

(A) Plans that offer a benefit that defers the receipt of compensation or operate in a manner that enables participants to defer the receipt of compensation.

(B) Plans established or maintained to provide fringe benefits described in § 101.6a (relating to fringe benefits in the form of use of property or services).

Employer—An individual, partnership, association, corporation, governmental body or unit or agency, or any other entity who or that is required under the IRC to withhold Federal Income Tax from wages paid to an employe. For the purpose of this definition, the terms “employe,” “employer” and “wages” have the same meanings as in Chapter 24 of the IRC.

Fiduciary—A guardian, trustee, executor, administrator, receiver, conservator or a person acting in a trust or similar capacity, whether domiciliary or ancillary. This term is intended to be all encompassing and includes any person defined as a fiduciary under any other statute of the Commonwealth. The fact that a person is defined as a fiduciary in one statute and not in another is immaterial for the purpose of this article.

Health, accident or death plan—

(i) The term means:

(A) An accident, health or term life insurance policy issued by an insurance company.

(B) A self-insured employe welfare benefit plan under which benefits are payable upon hospitalization, sickness, disability or death or for the prevention of sickness or disability.

(ii) The term does not include a program under which benefits are payable either upon hospitalization, sickness, disability, death or for the prevention of sickness or disability; or upon separation from employment or some other contingency.

Example: Under A's benefit plan, B qualifies for a lump sum payment equal to 26 weeks' pay upon proof of permanent disability or separation from employment. The plan does not constitute a health, accident or death plan because program benefits are also payable upon separation from employment. Instead, it constitutes a severance pay plan.

Highly compensated participant—

- (i) A plan participant who is one of the following:
 - (A) An officer.
 - (B) A shareholder owning more than 5% of the voting power or value of all classes of stock of the employer.
 - (C) An individual who, for the preceding taxable year:
 - (I) Received compensation from the employer in excess of the Federal limitation (after adjustment by the Secretary of the United States Treasury for inflation) set forth in section 414(q)(1)(B) of the IRC (26 U.S.C.A. § 414(q)(1)(B)).
 - (II) Is in the group consisting of the top 20% of all full-time employees of the employer with at least 3 years of service when ranked on the basis of compensation paid during the taxable year.
- (ii) A partner or other self-employed individual.
- (iii) A spouse or dependent of a highly compensated individual.

*Income—*The total of the classes enumerated under Chapter 103, Subchapter B (relating to the determination of tax) received by a taxpayer directly, or through partnerships, associations or Pennsylvania S corporations and the amount of each class derived by the taxpayer through estates or trusts determined and computed in accordance with the requirements of this article relating to the taxation of a natural individual's personal income, including the requirements that:

- (i) There is no setoff between, or among, any different classes of Personal Income Tax income. For example, an individual's net profit from manufacturing toys is \$100, his net loss from the business of selling garden supplies is \$20 and his net loss from passive ownership of investment rental properties is \$10. His total net business profits are \$80 which is his income, against which he may not set off his losses on rentals.
- (ii) A deduction is not allowed for expenses, whether paid or incurred for the production or collection of income or for the management, conservation or maintenance of property, except:
 - (A) Unreimbursed employee business expenses.
 - (B) Costs of goods sold and expense incurred in the operation of a business.

(C) Costs of acquisition, expenses of sale and collection expenses.

(D) Expenses necessary to the production or collection of rents and royalties or for the management, conservation or maintenance of rents, royalties, patents or copyrights.

(iii) The distributive income of a Pennsylvania S corporation, partnership or other association, trust or estate is classified, determined and computed in the same way and on the same basis as the taxable income of a natural individual; and, in the case of a Pennsylvania S corporation, partnership or other association, each shareholder, partner or member shall take into income the shareholder's, partner's or member's pro rata share of the income or loss in each applicable class of income received by the Pennsylvania S corporation, partnership or other association.

(iv) Married persons may not compute their tax as if they were one person; and no setoff between married persons is permitted. For example, an individual's net profit from manufacturing toys is \$100, his net loss from the business of selling garden supplies is \$20, his wife's loss from a business she operates is \$20 and his net loss from passive ownership of investment rental properties is \$10. His total net business profits are \$80 which is his income, against which he may not set off his wife's business losses.

Individual—A natural person and includes the members of a partnership or association.

Limited plan of termination—A plan that has one or more of the following attributes:

(i) The plan, when begun, is scheduled to be complete on a certain date or upon the occurrence of one or more specified events.

(ii) The number, percentage or class of employees whose services are to be terminated are specified in advance of the employees' terminations of service.

(iii) The plan is otherwise temporary or limited.

Nonresident estate or trust—An estate or trust which is not a resident estate or trust. In determining whether an estate or trust is a resident estate or trust, reference should be made to definitions of resident estates and resident trust in this section. Charitable trusts and pension or profit sharing trusts are not included within the term nonresident trusts.

Nonresident individual—An individual who is not a resident of this Commonwealth. In determining whether an individual is a resident, reference should be made to the definition of a resident in this section. References to nonresidents are equally applicable to nonresident aliens.

Partnership—An undertaking by two or more persons to place their money, property, labor, skill or all of these in commerce, business or a profession with a view to earning a profit which they shall share. The term includes limited and general partnerships and joint ventures. It shall be immaterial whether the

undertaking is limited as to subject, time or any other factor. The term does not include an organization taxed as a corporation under the laws of the Commonwealth.

Permanent place of abode—A dwelling place maintained by the taxpayer, whether or not owned by him. This term generally includes a dwelling place owned or leased by the taxpayer's spouse. However, a mere camp or cottage, which is used only for vacations, is not a permanent place of abode.

Person—An individual, employer, association, fiduciary, partnership, corporation or other entity, estate or trust, resident or nonresident, and the plural as well as the singular number. For the purpose of determining eligibility for special tax provisions, the term means a natural individual.

Plan—A cafeteria plan or other wage and salary supplemental or replacement program or arrangement established or maintained by an employer or by an employee organization, or by both, for the benefit of eligible employees or their beneficiaries. The term includes temporary or permanent programs or arrangements covering hospitalization, sickness, disability or death, supplemental unemployment benefits, strike benefits, social security or retirement, a trust that forms part of a plan, and a contract of insurance.

Poverty—An economic condition wherein the total amount of poverty income is insufficient to adequately provide the claimant, his spouse and dependent children with the necessities of life.

Poverty income—

(i) For the purpose of determining eligibility for special tax provisions, moneys or property, including interest, gains or income derived from obligations which are statutorily free from State or local taxation under any other act of the General Assembly of the Commonwealth or under the laws of the United States, received of whatever nature and from whatever source derived, but not including the following:

(A) Periodic payments for sickness and disability other than regular wages received during a period of sickness or disability.

(B) Disability, retirement or other payments arising under workmen's compensation acts, occupational disease acts and similar legislation by a government.

(C) 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.

(D) Payments commonly known as public assistance, or unemployment compensation payments by a governmental agency.

(E) Payments to reimburse actual expenses.

(F) Payments made by employers to labor unions for programs covering hospitalization, sickness, disability or death, supplemental unemployment benefits, strike benefits, social security and retirement.

(ii) Income which must be included, includes, but is not limited to: taxable income; interest received, whether taxable or nontaxable; realized capital gains, whether taxable or nontaxable; child support; alimony; life insurance proceeds; gifts of cash or property; educational stipends; military pay received for services outside of a combat zone; awards or prizes, including lottery winnings; inheritances; and other income not specified as “Income Not Included.”

(iii) The following income may not be included: Social Security and Medicare benefits; periodic payments for sickness and disability; workers’ compensation payments; public assistance and relief (welfare); unemployment compensation; reimbursed actual expenses; pensions or annuities, including railroad retirement benefits received by reason of retirement; and military pay received by servicemen for duty in a combat zone.

(iv) In cases where property is jointly owned, any income therefrom shall be divided according to the parties’ respective interest therein and be reported accordingly.

Qualified annuity—An arrangement under which the payee is entitled to equal, or substantially equal, periodic payments, paid at least annually, for any of the following periods:

(i) The life of the participant, or, if applicable, the joint lives of the recipient and recipient’s designated beneficiary.

(ii) The life expectancy of the participant, or, if applicable, the joint life expectancies of the recipient and recipient’s designated beneficiary.

(iii) A period of at least 10 years.

Resident estate—The estate of an individual who at the time of his death was a resident individual. The single controlling factor in determining if an estate is a resident estate for purposes of this article shall be whether the decedent was a resident individual at the time of his death. The residence of the fiduciary and the beneficiaries of the estate shall be immaterial.

Resident individual—An individual who is domiciled in this Commonwealth unless he maintains no permanent place of abode in this Commonwealth and does maintain a permanent place of abode elsewhere and spends in the aggregate not more than 30 days of the taxable year in this Commonwealth, or who is not domiciled in this Commonwealth but maintains a permanent place of abode in this Commonwealth and spends in the aggregate more than 183 days of the taxable year in this Commonwealth. An individual may be a resident of this Commonwealth and taxable as a resident even though he would not be deemed a resident for other purposes.

Resident trust—The single controlling factor in determining if a trust is a resident trust for purposes of this article shall be whether the decedent, the person creating the trust or the person transferring the property was a resident individual or person at the time of death, creation of the trust or the transfer of

the property. The residence of the fiduciary and the beneficiaries of the trust shall be immaterial. A resident trust shall be one of the following:

- (i) A trust created by the will of an individual who at the time of his death was a resident individual.
- (ii) A trust created by a person who at the time of the creation was a resident.
- (iii) A trust consisting in whole or in part of property transferred to the trust by a person who at the time of the transfer was a resident.

Severance pay—A payment made upon separation from employment under:

- (i) A plan which has both of the following attributes:
 - (A) Payments are not contingent solely upon an employee's retirement from service or being the same age as, or older than, the earliest retirement age under a qualifying retirement benefit plan or qualifying retirement income plan sponsored by the employer.
 - (B) Total payments cannot exceed twice the employee's annual compensation accruing during the year preceding the employee's termination.
- (ii) A plan under which all payments to any plan participant are completed within 120 months of the participant's termination.
- (iii) A plan under which no benefit is, or only reduced benefits are payable to, or can be taken, assigned, pledged or otherwise charged or dealt with by, any plan participant after the participant reaches normal retirement age or service.
- (iv) A plan, including a stock bonus or profit-sharing plan formed by a trust that meets the requirements for qualification described in section 401 of the IRC (26 U.S.C.A. § 401) or employee stock ownership plan, with one or more of the following attributes:
 - (A) The amount of earnings on contributions (or allocations of contributions or earnings) and the amount of benefits are determined with regard to the current or accumulated profits or losses of the employer.
 - (B) The employer can contribute only in those years when it has current or accumulated profits.
 - (C) The employer's contributions can fluctuate depending on the level of its profits.
 - (D) The employer's contributions are made out of current or accumulated profits.
 - (E) Distributions are paid with respect to stock of a corporation which is held by an employee stock ownership plan.
- (v) A plan under which the accrued benefit payable to each vested participant who does not die before the payment starting date is neither paid nor payable in the form of a qualified annuity.
- (vi) A limited plan of termination.

Special tax provisions—A refund or forgiveness of all or part of the claimant's liability under this article.

State—A state or commonwealth of the United States, the District of Columbia, the Commonwealth of Puerto Rico, a territory or possession of the United States, and a foreign country, but not a political subdivision of any of the foregoing.

Supplemental unemployment benefit plan—A plan established or maintained by an employer or by an employee organization, or by both, that has all of the following attributes:

(i) No benefit is payable to, or can be taken, assigned, pledged or otherwise charged or dealt with by, any plan participant except upon lay-off or involuntary separation from the employment of the employer (whether or not the separation is temporary) resulting directly from:

- (A) A reduction in force.
- (B) Plant closing.
- (C) Change in organizational structure.
- (D) Discontinuance of an operation.

(E) The participant's failure to meet or maintain standards of performance for the position due to inability to carry out the responsibilities of the position, health, obsolescence, failure to meet the changed responsibilities of the position or similar circumstance beyond the control of the participant.

(ii) No benefit is payable to, or can be taken, assigned, pledged or otherwise charged or dealt with by, any plan participant if the participant either:

- (A) Voluntarily separates from service.
- (B) Is separated or discharged from service for any of the following reasons:

(I) Refusal to accept another position with reasonably comparable compensation.

(II) The commission of illegal acts.

(III) Insubordination, failure or refusal to comply with rules or regulations or similar acts within the control of the participant.

(iii) Employer payments to provide benefits are paid to an independently controlled trust or pooled fund established or maintained for the purpose of funding or providing benefits under the plan.

Tax—Interest, penalties and additions to tax, and tax which is withheld under this article by an employer on compensation paid.

Taxable year—When the taxpayer or a claimant is required to file a Federal income tax return under the Internal Revenue Code of 1954, as amended, taxable year means the taxable period for which the return is required. Where the taxpayer is not required to or does not file a Federal income tax return, taxable year means the calendar year. Notwithstanding the foregoing for the first taxable period after the imposition of this tax, taxable year means the period beginning June 1, 1971, and ending with the last day of the taxable period for which the taxpayer files a Federal income tax return under the Internal Revenue

Code of 1954, as amended, or December 31, 1971, if he is not required to or does not file a Federal income tax return.

Taxpayer—An individual, estate or trust subject to the tax imposed by this article; a partnership having a partner who is a taxpayer under this article; and an employer required to withhold tax on compensation paid.

Wage or salary supplement—

- (i) Employer-provided coverage under a plan.
- (ii) Separation pay, vacation pay, holiday pay, guaranteed pay, reimbursement for personal expenses, an employer payment to provide benefits under a plan and any other amount paid, under an agreement, to one or more of the following:
 - (A) An independently controlled trust or pooled fund established or maintained for the purpose of funding or providing benefits under the plan.
 - (B) An insurance company for the purchase of insurance.
 - (C) A third party for the benefit of the employe.
- (iii) Any benefit under a plan to the extent attributable to plan coverage or contributions by the employer which were not includible in income of the employe.
- (iv) Any benefit under a plan which is directly paid by the employer.

Authority

The provisions of this § 101.1 amended under section 354 of the Tax Reform Code of 1971 (72 P. S. § 7354).

Source

The provisions of this § 101.1 amended through June 12, 1975, effective June 13, 1975, 5 Pa.B. 1561; amended December 10, 1999, effective December 11, 1999, 29 Pa.B. 6249; amended August 4, 2000, effective August 5, 2000, 30 Pa.B. 3938; amended January 11, 2002, effective January 12, 2002, 32 Pa.B. 250, 253. Immediately preceding text appears at serial pages (268447) to (268454).

Cross References

This section cited in 61 Pa. Code § 123.3 (relating to taxability under special provisions).

§ 101.2. Accounting methods.

No one method of accounting is prescribed for taxpayers. Each taxpayer shall adopt the methods, forms and systems that best suit his needs, so long as they clearly reflect income. A method of accounting which reflects the consistent application of generally accepted accounting principles in a particular trade or business in accordance with prevailing conditions or practices in that trade or business shall be presumed to clearly reflect income, if the method is used for Federal income tax purposes.

§ 101.3. Domicile.

(a) In the case of an individual domiciled in this Commonwealth, the maintenance of a permanent place of abode in this Commonwealth is alone sufficient to make him a resident for tax purposes. Even though he remains outside this Commonwealth for the entire year, the 183-day rule applies only to taxpayers who are not domiciled in this Commonwealth. Reference should also be made to § 101.5 (relating to rules for days within and without the Commonwealth).

(b) A domicile, once established, continues until the individual in question moves to a new location with the bona fide intention of making his fixed and permanent home there. No change of domicile results from a removal to a new location if the intention is to remain there only for a limited time; this rule applies even though the individual may have sold or disposed of his former home. The burden shall be upon the individual asserting a change of domicile to show that the necessary intention existed. In determining an individual's intention in this regard, his declarations shall be given due weight, but they may not be conclusive if they are contradicted by his conduct. The fact that an individual registers and votes in one place is important but not necessarily conclusive, especially if the facts indicate that he did this merely to escape taxation in some other place.

(c) Domicile is not dependent on citizenship; that is, an immigrant who has permanently established his home in this Commonwealth shall be domiciled here regardless of whether he has become a United States citizen or has applied for citizenship. However, a United States citizen will not ordinarily be deemed to have changed his domicile by going to a foreign country unless it is clearly shown that he intends to remain there permanently. For example, a United States citizen domiciled in this Commonwealth, who goes abroad because of an assignment by his employer or for study, research or recreation, does not lose his Commonwealth domicile unless it is clearly shown that he intends to remain abroad permanently and not to return.

(d) An individual may have only one domicile. If he has two or more homes, his domicile shall be the one which he regards and uses as his permanent home. In determining his intentions in this matter, the length of time customarily spent at each location shall be important but not necessarily conclusive. An individual who maintains a permanent place of abode in this Commonwealth is taxable as a resident even though he may be domiciled elsewhere.

(e) Ordinarily, the domicile of the wife follows that of her husband, but if they are separated in fact she may, under some circumstances, acquire her own separate domicile, even though there is no judgment or decree of separation.

(f) Domicile of a child ordinarily follows that of his father, or of his mother after the death of the father, until he reaches the age of self-support and actually establishes his own separate domicile. The domicile of a child for whom a guardian has been appointed may not be necessarily determined by the domicile of the guardian.

§ 101.4. Residents not domiciled in this Commonwealth.

(a) An individual domiciled in this Commonwealth shall be a resident for purposes of this article for a specific taxable year, unless for that year he satisfies all three of the following requirements:

- (1) Maintains no permanent place of abode in this Commonwealth during the year.
- (2) Maintains a permanent place of abode elsewhere during the entire year.
- (3) Spends in the aggregate not more than 30 days of the taxable year in this Commonwealth.

(b) For example, an individual, although retaining his Commonwealth domicile for legal reasons, such as voting purposes, may maintain his only permanent place of abode in the District of Columbia where he is employed by the Federal government. As long as he continues to meet all three of the conditions stated in subsection (a), he shall be a nonresident of this Commonwealth for income tax purposes. However, if for any taxable year he fails to meet any one of these three conditions, he shall be subject to Commonwealth income tax as a resident for that year.

(c) Where an individual claims to be a nonresident for any taxable year, the burden shall be upon him to show that during that year he satisfied all three of the requirements set forth in subsection (a).

(d) If, at the time he entered military service, the domicile of a serviceman was in this Commonwealth, assignment to duty outside the state does not change his Commonwealth domicile. Although his military pay is not "compensation" as defined by this article and, therefore, not taxable, he shall file a return and pay tax on all other income taxable under this article in the same manner as any resident individual unless he satisfies all three of the conditions set out in subsection (a).

(e) Military pay of military personnel domiciled outside of this Commonwealth but living or stationed in this Commonwealth is not subject to tax under the provisions of the Soldiers and Sailors Civil Relief Act.

Source

The provisions of this § 101.4 amended June 12, 1975, effective June 13, 1975, 5 Pa.B. 1561.

§ 101.5. Rules for days within and without this Commonwealth

(a) In counting the number of days spent within and without this Commonwealth, presence within this Commonwealth for any part of a calendar day constitutes a day spent within this Commonwealth, except that the presence within this Commonwealth may be disregarded if it is solely for the purpose of boarding a plane, ship, train or bus for travel to a destination outside of this Commonwealth, or while traveling by motor, plane, or train through the Commonwealth to a destination outside this Commonwealth.

(b) An individual domiciled outside this Commonwealth who maintains a permanent place of abode within this Commonwealth during any taxable year and claims to be a nonresident shall keep and have available for examination by the Department adequate records to substantiate the fact that he did not spend more than 183 days of the taxable year within this Commonwealth.

Cross References

This section cited in 61 Pa. Code § 101.3 (relating to domicile).

§ 101.6. Compensation.

(a) Compensation includes items of remuneration received, directly or through an agent, in cash or in property, based on payroll periods or piecework, for services rendered as an employee or casual employee, agent or officer of an individual, partnership, business or nonprofit corporation, or government agency. These items include salaries, wages, commissions, bonuses, stock options, incentive payments, fees, tips, dismissal, termination or severance payments, early retirement incentive payments and other additional compensation contingent upon retirement, including payments in excess of the scheduled or customary salaries provided for those who are not terminating service, rewards, vacation and holiday pay, paid leaves of absence, payments for unused vacation or sick leave, tax assumed by the employer, or casual employer signing bonuses, amounts received under employee benefit plans and deferred compensation arrangements, and other remuneration received for services rendered.

(b) Scholarships, stipends, grants and fellowships shall be taxable as compensation, if services are rendered in connection therewith.

(1) When used in this subsection, the following words have the following meanings, unless the context clearly indicates otherwise:

(i) *Fellowship stipend* or *fellowship award*—A fixed sum of money paid periodically for services or to defray expenses to a graduate student who is enrolled in a graduate degree program at a university.

(ii) *Grant-in-aid*—Financial support given by a public agency or private institution to an individual to further the individual's education.

(iii) *Postdoctoral research fellowship stipend* or *postdoctoral research fellowship award*—A fixed sum of money paid periodically for services or to defray expenses of an individual who has obtained a doctoral degree at a university and is conducting research at a research facility.

(iv) *Scholarship*—A grant-in-aid to a student.

(2) Scholarships, grants, awards and other types of student aid which require no past, present or future services in return for receipt of the funds are not taxable.

Examples:

(i) John has a high school diploma and is currently employed. John's employer promises to pay for John's college tuition, room and board for 4 years if John agrees to return to his employer after obtaining his degree and to work for the employer for 4 consecutive years. John's grant-in-aid is taxable compensation and is subject to Pennsylvania employer withholding and reporting.

(ii) Peter is employed by ABC Company. Peter and ABC Company agree that he will work for them for 1 year without receiving any salary. In return, after that year Peter will attend XYZ College and ABC Company will pay his tuition, room and board for the entire year. ABC's payment of Peter's tuition, room and board is taxable compensation and is subject to Pennsylvania employer withholding and reporting.

(iii) John is employed by XYZ Corporation. XYZ Corporation has established a "Scholarship Program" for the children of its employees. The program does not qualify as an employer scholarship program for Federal income tax purposes. John's child, Erin, receives a "scholarship" from the plan to attend college. The fair market value of the Federally nonqualified scholarship is taxable compensation to John and is subject to Pennsylvania employer withholding.

(3) Fellowship awards or fellowship stipends made to graduate students enrolled in a graduate degree program at a university chartered by a state or foreign country on the basis of need or academic achievement for the purpose of encouraging or allowing the recipient to further his educational development are not taxable. When the fellowship awards or fellowship stipends are made as compensation for past or present employment or in expectation of future employment services they are taxable.

Example:

Jane is enrolled in a graduate degree program in biochemistry at a university. Jane is in the first year of a 3-year graduate degree program. A pharmaceutical company enters into an agreement to pay the remaining tuition, room and board expenses necessary for Jane to obtain her graduate degree. In return, Jane promises to work for the pharmaceutical company for 4 years after graduation. Jane's receipt of these payments from her future employer constitute taxable compensation.

(4) Fellowship awards and fellowship stipends are taxable compensation for services if the recipient is required to apply his skill and training to advance research, creative work or some other project or activity, unless the recipient can show that the recipient is a candidate for a degree and the same activities are required of all candidates for that degree as a condition to receive that degree.

Example:

Steven is enrolled in a graduate degree program in education at ABC University. Degree candidates are required to teach an undergraduate education course for 5 hours a week to obtain their degree. Steven and two of the other 15 candidates in the degree program are receiving fellowship stipends. If Steven does not perform additional services for ABC University, his teaching will not make his stipend taxable compensation.

(5) For a payment received by a postdoctoral research fellow for conducting research to be excludable from the definition of compensation, the payment shall meet the following conditions. If the payment fails to meet one or more of these conditions, the payment is taxable compensation:

(i) The source of funding for the payment is a governmental agency, a private foundation as described in section 509 of the Internal Revenue Code (26 U.S.C.A. § 509), a Federally exempt organization as described in sections 501(c)(3) or (5) of the Internal Revenue Code (26 U.S.C.A. § 501(c)(3) and (5)), or a public or private university chartered by a state.

(ii) The organization which is permitting the fellow to use its facilities and which is sponsoring the fellow's research (sponsoring organization) is a governmental agency, a Federally exempt organization as described in section 501(c)(3) of the Internal Revenue Code, or a public or private university chartered by a state.

(iii) Prior to enrollment in the sponsoring organization's postdoctoral research fellowship program, the fellow has obtained a doctoral degree in a field of study which is related to the field of study being researched by the fellow.

(iv) The amount of the fellow's stipend or grant is based on the scale established by the source of funding.

(v) Each fellow formulates his own research project or advances his own research project throughout the stipend or grant period.

(vi) The sponsoring agency serves only in an advisory capacity in the selection of research projects and cannot establish or control the fellow's hours or methods of research except as control relates to legal or regulatory matters.

(vii) The fellow is not required to perform administrative work, teaching assignments or other duties for the sponsoring organization or another entity as a condition for receiving a payment and will not be penalized for not performing these duties.

(viii) The fellow is not required to enter a contractual commitment for future employment with a specified entity as a condition for obtaining or continuing to obtain the payments.

(ix) Payments to the fellow for conducting research are limited to no more than 36 months.

(x) Research results or writings made by the fellow during the program do not become the property of the sponsoring organization or another entity other than the fellow. Patent or copyright royalties or other income derived directly or indirectly from the fellow's research results or writings may become the property of the sponsoring organization. Income or gain derived from patent or copyright royalties by the postdoctoral research fellow is taxable income to the fellow.

(xi) The fellow is not required to assist employees of the sponsoring organization in conducting research being performed by employees of the sponsoring organization.

Example:

John is a postdoctoral research fellow at ABC Cancer Research Institute. His research is being funded by the National Institute of Health. The sponsoring organization, ABC Cancer Research Institute, requires John to spend half of his time assisting its own employees on their own research project as a condition for sponsoring his research. John's postdoctoral research fellowship stipend is taxable compensation.

(xii) The fellow does not receive fringe benefits to which an employee of the sponsoring organization is entitled, except to the extent that the benefits are at no additional cost to the sponsoring organization. For purposes of this subparagraph "fringe benefits" means payor provided health, life, disability income or group legal services insurance plans, payor provided automobile and payor provided dependent care assistance, educational assistance plans or retirement benefits.

(xiii) Pennsylvania unemployment compensation premiums are not required to be paid by the sponsoring organization or another entity on behalf of the fellow.

(xiv) Federal social security employment tax is not required to be paid by the sponsoring organization or another entity or the fellow with respect to the fellowship.

(xv) The fellow is not under the coverage of the sponsoring organization's worker's compensation insurance plan or policy.

(6) Fellowship stipends paid to medical interns and residents under an internship or residency program which conforms or substantially conforms to standards set by the American Medical Association are taxable compensation.

(c) Compensation does not mean or include any of the following:

(1) Periodic payments for periods of sickness or disability paid by or on behalf of an employer under a program or plan unless the payments are regular wages. Additionally, no amount of damages received (whether by suit or agreement and whether as lump sums or as periodic payments) if pain and suffering, emotional distress or other like noneconomic element was, or would have been, a significant evidentiary factor in determining the amount of the taxpayer's

damage. No payments made by third-party insurers for periods of sickness or disability would be considered payments of regular wages. A program or plan where any of the following occur would not be considered payment of regular wages:

- (i) The periodic payments have no direct relationship to the employee's usual rate of compensation.
 - (ii) The periodic payments are computed with reference to the nature of the sickness or disability and without regard to the employee's job classification.
 - (iii) Periodic payments would be reduced by payments arising under Workmen's Compensation Acts, Occupational Disease Acts, Social Security Disability or similar legislation by any government.
 - (iv) The periodic payments exceed the employee's usual compensation for the period.
- (2) Disability, retirement or other payments arising under workmen's compensation acts, occupational disease acts or similar legislation by any government.
 - (3) Federal old age insurance benefits payable under 42 U.S.C.A. § 401, Railroad Retirement Act benefits payable under 45 U.S.C.A. § 228 or § 231 or any retired or retainer pay of a member or former member of a uniformed service computed under 10 U.S.C.A. § 1401.
 - (4) Payments commonly known as public assistance or unemployment compensation by a government agency.
 - (5) Payments made by employers to employees to reimburse actual expenses allowable as an ordinary, reasonable and necessary business expense.
 - (6) Payments made by an employer or labor union or elective contributions deemed to be made by an employer under a cafeteria plan for a nondiscriminatory health, accident or death plan.

Example:

P is a partnership that is engaged in providing accounting services. On a nondiscriminatory basis, it offers the following fringe benefits to both employees and partners of the firm:

Blue Cross/Blue Shield medical coverage.

Dental and eyeglass coverage with a deductible.

Group term life insurance with coverage up to the equivalent of the employee's annual salary.

P pays the premiums on behalf of all employees and partners for all medical, dental, eyeglass and insurance coverage directly to the insurance carrier or benefit provider. P does not add the premium costs for the benefits to any employee's gross wages and it accounts for the benefit costs as nonsalary fringe benefit expenses. In other words, the value of the benefits are not shown as an addition to any employee's wages on the paystubs furnished to employees.

The plan is not a Federally qualifying cafeteria plan.

Conclusion: For the employes of P the employer-provided hospitalization (Blue Cross/Blue Shield), eyeglass, dental coverage and group life insurance benefits are excludable from compensation and are therefore not subject to withholding. The premiums paid on behalf of the partners, however, are not deductible or excludable from the income of the partnership or the partners.

(7) The value of meals and lodging furnished for the convenience of an employer or casual employer does not constitute compensation. Payments made to an Individual Retirement Account, as provided by the Employee Retirement Income Security Act of 1974 (ERISA), the act of September 2, 1974 (Pub. L. No. 93-406, 88 Stat. 829), are not excludable in computing income which is subject to tax under this article.

(8) Old Age or Retirement Benefit Plans.

(i) *Scope.* For the purpose of this section, the term plan includes Individual Retirement plans (IRA), Simplified Employee Pension Plans (SEP), Keogh plans, Federally qualified employee pension plans and similar old age or retirement benefit plans.

(ii) *Contributions.*

(A) Contributions to a plan made by employers or labor unions on behalf of an employe are excludable from the employe's income, except as otherwise provided in this chapter.

(B) Contributions to a plan made by an employe or other individual directly or indirectly, whether through payroll deduction, a salary reduction agreement or otherwise, are not excludable from his income. Contributions by, on behalf of or attributable to a self-employed person are not excludable from either compensation or net profits from a business, profession or other activity.

(iii) *Distributions.*

(A) Amounts distributed to an individual from a plan shall be included in income to the extent that contributions were not previously included in this income except for either of the following:

(I) Distributions made upon or after his retirement from service after reaching a specific age or after a stated period of employment.

(II) Distributions transferred into another plan, where the transferred amounts are not included in income for Federal income tax purposes.

(B) To determine the portion of a distribution to be included in income, an individual shall use the cost recovery method.

Example 1:

John contributed \$1,000 to his IRA. He pays tax on the \$1,000 contribution. Three years later the account has earned \$750 in income. The total balance of the account at that time is (\$1,000 + \$750 =)

\$1,750. John receives a distribution of \$750 from his IRA. Since the amount of the distribution does not exceed \$1,000, the distribution is not includable in income.

Example 2:

Same facts as Example 1, except that John receives a distribution of \$1,500. Since the amount of the distribution exceeds \$1,000, the excess of the distribution, \$500, is includable in his income, as compensation.

(iv) *Income on plan assets.* Income on assets held in a plan is not includable in income.

(9) Payments made by an employer or labor union for a nondiscriminatory supplemental unemployment benefit or strike benefit plan.

(10) Federally excludable benefits provided for the convenience of the employer.

(11) Fringe benefits described in § 101.6a (relating to fringe benefits in the form of personal use of property or services).

(12) Program benefits payable on condition of hospitalization, sickness, disability or death under a health, accident or death plan.

(13) Guaranteed payments to a partner for services rendered to the partnership.

(14) Benefits payable by an employer or labor union under a supplemental unemployment benefit plan, whether payable on a periodic basis or in the form of cash, services or property.

(d) The Department may require the submission of a statement from an employer or casual employer with respect to its employes or casual employes regarding the verification or substantiation of unreimbursed and reimbursed business expenses. The statement of the employer or casual employer should verify that the expenses were required by the employer or casual employer. The statement shall set forth the types of expenses such as travel, meals, hotel and so forth that the employer or casual employer specifically requires the employe or casual employe to incur and to what extent, if any, the expenses are reimbursed. If the employer or casual employer requires the employe or casual employe to maintain an office, or office-in-home, a statement by the employer or casual employer to this effect should also be included. The Department does not require the employer or casual employer to specifically list the amount expended or to verify each expense incurred by the employe or casual employe.

(e) Compensation paid in a medium other than cash shall be valued at its current market value. Compensation paid in the form of employer-provided coverage under an employe welfare benefit plan shall be valued at cost. The cost shall be the total amount of payment made during the year by the employer on account of the plan and plan participant, except in the following situations:

(1) In the case of self-insured insurance plans, the cost shall be the annual cost for financial accounting purposes.

- (2) The amount of compensation paid in the form of Federally taxable noncash fringe benefits shall be determined in the same manner as is prescribed by the Internal Revenue Service under Federal statutes and regulations.
- (3) In the case of cafeteria plans, amounts specified in the plan document as being available to the participant for the purpose of selecting or purchasing benefits, when so used, shall be included in the total amount of payment made during the year by the employer on account of the plan and plan participant.
- (f) Compensation in the form of incentive, qualified, restricted or nonqualified stock options shall be considered to be received:
- (1) When the option is exercised if the stock subject to the option is free from any restrictions having a significant effect on its market value.
 - (2) When the restrictions lapse if the stock subject to the option is subject to restrictions having a significant effect on its market value.
 - (3) When exchanged, sold or otherwise converted into cash or other property.
- (g) The following rules apply if, under a cafeteria plan, plan participants may choose between benefits consisting of cash, additional paid vacation days, and other benefits; or if, outside a cafeteria plan, plan participants can purchase additional paid vacation days:
- (1) If additional paid vacation days are elected or purchased and they are used before the next calendar year, the following apply:
 - (i) The amount of cash foregone in exchange for the paid vacation day is excluded from income.
 - (ii) The vacation pay is includable in income when paid.
 - (2) If additional paid vacation days are purchased outside a cafeteria plan and they are not used before the next calendar year, the amount of cash foregone in exchange for the paid vacation days is excludable for Pennsylvania Personal Income Tax purposes only if both of the following apply:
 - (i) The value of the vacation day cannot be cashed out or used for any other purpose.
 - (ii) The vacation day cannot be carried over to the next taxable year.
- (h) Employer payments to reimburse employees for uninsured medical or dental expenses are taxable as compensation if the employee is assured of receiving (in cash or any other benefit) amounts available but unused for covered reimbursement during the year without regard to whether the employee incurred covered expenses or not. If the amounts available for covered reimbursement cannot be cashed out or used for any other purpose during the taxable year or be carried over to any other taxable year, normal cash compensation that is forgone by an employee under a spending account or otherwise, and credited to a self-insured medical reimbursement account and drawn upon to reimburse the employee for uninsured medical or dental expenses to which section 105(b) of the IRC (26 U.S.C.A. § 105(b)) applies is excludable from tax.
- (i) After December 31, 1996:

(1) Payments made after December 31, 1996, for employe welfare benefit plans under a cafeteria plan will be deemed to be an “employer contribution” for Pennsylvania Personal Income Tax purposes if the following apply:

(i) The payments were not actually or constructively received, after taking section 125 of the IRC (26 U.S.C.A. § 125) into account.

(ii) The payments were specified in a written cafeteria plan document as being available to the participant:

(A) For the purpose of selecting or purchasing benefits under a plan.

(B) As additional cash remuneration received in lieu of coverage under a plan.

(iii) The benefits selected or purchased are nontaxable under the IRC when offered under a cafeteria plan.

(iv) The payments made for the plan would be nontaxable under the Pennsylvania Personal Income Tax if made by the employer outside a cafeteria plan.

(2) If the requirements of paragraph (1) are satisfied, cafeteria plan contributions are taxed under such rules as they apply to employer payments for employe welfare benefit plans. However, if the benefits are taxable for Federal Income Tax purposes when offered under a cafeteria plan, the payments will also constitute compensation for Pennsylvania Personal Income Tax purposes. Payments also will constitute compensation if they would be taxable under the Pennsylvania Personal Income Tax if made by the employer outside a cafeteria plan. For example, although not taxable under the IRC, coverage under a dependent care plan providing for the reimbursement of expenses for household or dependent care services would constitute compensation under the Pennsylvania Personal Income Tax because it would be taxable if made by an employer outside a cafeteria plan.

(j) Compensation includes the entire cost of employer-provided coverage provided to a highly compensated participant under any discriminatory employe welfare benefit plan.

(k) Contributions made by an employer for IRC 401(k) plans under a cafeteria plan under which the employe unilaterally may elect to have the employer either make the payments as contributions to a 401(k) plan or other plan on behalf of the employe or to the employe directly in cash are not excludable from the employe’s compensation.

(l) Except as provided in § 101.6a (relating to fringe benefits in the form of use of property or services), compensation is taxable regardless of the form of the payment. Examples of taxable forms of payment include:

(1) Cash.

(2) Foreign currency.

(3) A check or other negotiable instrument.

(4) Freely transferable, readily marketable obligations or other cash equivalent.

- (5) Tangible property interests, intangible personal property or other rights, claims or things that either:
- (i) Can be enforced in courts of equity and transferred and have an ascertainable fair market value.
 - (ii) Can be reduced to cash or eliminate an expenditure.
- (6) A monetary payment in reimbursement of a personal expenditure or to eliminate a personal expenditure.
- (7) Below-market rate loans.
- (8) A cancellation of indebtedness constituting a quid pro quo or incentive that would be taxable had the amount by which the debt had been forgiven or discharged instead been paid to the debtor in cash or property.
- (m) For purposes of this section:
- (1) A person who separated from service before satisfying superannuation requirements shall be deemed to be retired from service upon reaching retirement age, regardless of whether he has permanently and wholly withdrawn from active working life or not.
 - (2) The voluntary discontinuance of a plan within 3 years after it has taken effect, for any reason other than business necessity, will be evidence that the plan was temporary and limited.

Authority

The provisions of this § 101.6 amended under section 354 of the Tax Reform Code of 1971 (72 P. S. § 7354).

Source

The provisions of this § 101.6 adopted February 19, 1972, effective February 20, 1972, 2 Pa.B. 259; amended March 13, 1976, effective March 14, 1976, 6 Pa.B. 454; amended April 8, 1978, effective April 9, 1978, 8 Pa.B. 1055; amended through April 13, 1984, effective April 14, 1984, 14 Pa.B. 1308; amended May 15, 1992, effective May 16, 1992, 22 Pa.B. 2541; amended December 10, 1999, effective December 11, 1999, 29 Pa.B. 6249; amended August 4, 2000, effective August 5, 2000, 30 Pa.B. 3938; amended January 11, 2002, effective January 12, 2002, 32 Pa.B. 250, 253. Immediately preceding text appears at serial pages (268457) to (268467).

Notes of Decisions

Actual Expenses

Transferred employees reimbursement for expenses incurred in purchasing new residence are compensation and reportable as taxable income. *Williamson v. Commonwealth*, 525 A.2d 475 (Pa. Cmwlth. 1987).

Court rejected taxpayers request to interpret term "actual expenses" to mean "any" expenses including living expenses; rather, Department's interpretation of term as limited to business expenses is consistent with legislative intent and previous rulings of Pa. Supreme Court. *Williamson v. Commonwealth*, 525 A.2d 475 (Pa. Cmwlth. 1987).

Constitutional

Retirement contributions made on behalf of partners is money that the partners would otherwise receive in their share of the net profits of the partnership, and the contributions are made, at least theoretically, at the election of the partners. On the other hand, when an employer makes contributions to an employee's retirement plan, the contributions are not made by reducing the employee's

salary, and the employee is given no control over whether the contributions are to be made. Furthermore, the employee does not actually or constructively receive the contributions because the receipt of benefits under the retirement plan could be subject to substantial limitations and restrictions. There is, therefore, a legitimate and nonarbitrary reason for distinguishing between partners and employees, thus rendering the Department of Revenue's regulations constitutional. *Smith v. Commonwealth*, 684 A.2d 647 (Pa. Cmwlth. 1996).

Contributions

The provisions of subsection (c)(8)(ii) violate the Uniformity Clause of the Pennsylvania Constitution (Article VIII, section 1) insofar as they permit employees who are similar to independent contractors to exclude unreimbursed business expenses from taxable income while denying an exclusion for such expenses to employees who are not similar to independent contractors. *Ritz v. Commonwealth*, 432 A.2d 169 (Pa. 1981).

Federal Treatment

Just because the Internal Revenue Code and certain Pennsylvania statutes treat rollover contributions differently from other contributions, did not mean that Pennsylvania courts would also treat them differently when interpreting 42 Pa.C.S. § 8124. Thus, debtor's claimed exemption for an IRA is denied to the extent of \$56,134.75, such amount representing the difference between the \$71,134.75 debtor contributed to the IRA in 1992 and the \$15,000 yearly exemption limitation under Pennsylvania law. *In re Barshak*, 185 Bankr. 210 (Bankr. E. D. Pa. 1995); reversed 106 F.3d 501 (3rd Cir. 1997).

An employer must withhold personal income tax from contributions to an employee's savings plan under a salary reduction plan and Federal law is inapplicable. *AMP Products Corp. v. Commonwealth*, 593 A.2d 1 (Pa. Cmwlth. 1991); affirmed 608 A.2d 25 (Pa. Cmwlth. 1990).

Partnerships

Co-owners of a law firm, organized as a partnership, assume the status of self-employed individuals. *Smith v. Commonwealth*, 684 A.2d 647 (Pa. Cmwlth. 1996).

Post Termination Income

A post-termination "Special Incentive Compensation Plan," involving payment of dividend units was compensation and not old-age or retirement payments. *Bickford v. Commonwealth*, 533 A.2d 822 (Pa. Cmwlth. 1987).

If a distribution to a taxpayer from an employer-sponsored profit sharing trust constitutes payment for services rendered and is a severance rather than a retirement benefit, it is compensation. *Goswisch v. Department of Revenue*, 397 A.2d 1288 (Pa. Cmwlth. 1979).

Rollover Contributions

The Legislature's failure to specifically address the rollover problem does not demonstrate an intent to exclude rolled-over funds from the protection of 42 Pa.C.S.A. § 8124, particularly since such an intent would be in conflict with the Legislature's other purposes in enacting the statute. *In re Barshak*, 195 Bankr. 321 (E. D. Pa. 1996).

Self Employed

The provision that states that contributions to an IRA by a self-employed individual for the individual's own benefit are not ordinary business expenses and cannot be excluded from net profits is reasonable. *Kalodner v. Commonwealth*, 615 A.2d 900 (Pa. Cmwlth. 1992); adhered to on reconsideration 636 A.2d 1230 (Pa. Cmwlth. 1994); affirmed by 675 A.2d 710 (Pa. 1995).

Union Dues

Union dues should be permitted to be excluded from income if union membership is mandated by the contract between the union and the employer. *Ritz v. Commonwealth*, 432 A.2d 169 (Pa. Cmwlth. 1981).

Cross References

This section cited in 61 Pa. Code § 103.11 (relating to compensation).

§ 101.6a. Fringe benefits in the form of use of property or services.

(a) Remuneration for services received in the form of personal or business use of property is not taxable as compensation if the following requirements are met:

- (1) The property belongs to, or is held under a lease by, the employer at the time of use.
- (2) No title, interest or estate therein is conferred upon, or vested in, another person.

(b) Examples of property that are excludible from tax if the requirements of subsection (a) are met include:

- (1) Educational or training facilities.
- (2) Housing or clothing.
- (3) Day care facilities.
- (4) Passenger cars and commuter highway vehicles.
- (5) Aircraft or water craft.
- (6) Construction or recreation vehicles.
- (7) Athletic facilities or equipment.
- (8) Recreational facilities or equipment.
- (9) Entertainment facilities or equipment.
- (10) Parking facilities.
- (11) Eating facilities.
- (12) Office facilities or equipment.
- (13) Tools, equipment or supplies.

(c) Remuneration for services received in the form of personal or business use of services is not taxable as compensation if either:

- (1) The service is provided or supplied directly by the employer or a co-employee.
- (2) Rights to the service were procured beforehand by the employer.

(d) Examples of services that are excludible from tax if the requirements of subsection (c) are met include:

- (1) The operation of an eating facility.
- (2) Transportation in a commuter highway vehicle.
- (3) Air or rail transportation of passengers or cargo.
- (4) Parking.
- (5) Education or training.

- (6) Legal, medical, accounting or other professional or technical services or assistance, including adoption assistance.
- (7) Day care services or assistance.
- (8) Dependent care assistance.
- (9) A tuition reduction provided to an employee or his dependents or to a teaching and research assistant.
- (e) Remuneration for services received in the form of consumption of a consumable, such as food and supplies, is not taxable as compensation.
- (f) This section applies even if:
 - (1) The use or service is offered on a discriminatory basis.
 - (2) The employer incurs substantial additional cost, including forgone revenue, in providing the use or service.

Authority

The provisions of this § 101.6a issued under section 354 of the Tax Reform Code of 1971 (72 P. S. § 7254).

Source

The provisions of this § 101.6a adopted August 4, 2000, effective August 5, 2000, 30 Pa.B. 3938.

Cross References

This section cited in 61 Pa. Code § 101.1 (relating to definitions); and 61 Pa. Code § 101.6 (relating to compensation).

§ 101.7. Receipt of income.

(a) *General rule.* An amount, the privilege of receiving which is taxable, shall be considered as received in the year in which it is actually or constructively received unless includable for a different year in accordance with the method of accounting of the taxpayer. Under an accrual method of accounting, income shall be includable in gross income when all the events have occurred which fix the right to receive the income and the amount thereof may be determined with reasonable accuracy. Therefore, under such a method of accounting if, in the case of compensation for services, no determination may be made as to the right to the compensation or the amount thereof until the services are completed, the amount of compensation is ordinarily income for the taxable year in which the determination can be made. Under the cash receipts and disbursements method of accounting, such an amount shall be includable in gross income when actually or constructively received. Where an amount of income is properly accrued on the basis of a reasonable estimate and the exact amount is subsequently determined, the difference, if any, shall be taken into account for the taxable year in which the determination is made. To the extent that income is attributable to the recovery of bad debts for accounts charged off in prior years, it shall be includable in the year of recovery in accordance with the method of accounting of the taxpayer regardless of the date when the amounts were charged off. If a taxpayer ascer-

tains that an item should have been included in gross income in a prior taxable year, he should file an amended return and pay an additional tax due. Similarly, if a taxpayer ascertains that an item was improperly included in gross income in a prior taxable year, he should, if within the period of limitation, file a claim for credit or refund of an overpayment of tax arising therefrom.

(b) *Special rule in case of death.* The taxable year of a taxpayer ends on the date of his death. See § 117.3 (relating to deceased individuals). In computing taxable income for the year, there shall be included only amounts properly includable under the method of accounting used by the taxpayer. However, if the taxpayer used an accrual method of accounting, amounts accrued only by reason of his death may not be included in computing taxable income for the year. If the taxpayer uses no regular accounting method, only amounts actually or constructively received during the year shall be included.

(c) *Constructive receipt of income.* Income although not actually reduced to possession shall be constructively received by him in the taxable year during which it is credited to his account, set apart for him, or otherwise made available so that he may draw upon it at any time. However, income may not be constructively received if the control by the taxpayer of its receipt is subject to substantial limitations or restrictions. Therefore, if a corporation credits its employees with bonus stock, but the stock is not available to the employees until some future date, the mere crediting on the books of the corporation does not constitute receipt. In the case of interest, dividends or other earnings credited in respect of a deposit or account in a bank, building and loan association, savings and loan association, or similar institution, the following are not substantial limitations or restrictions on the control by the taxpayer over the receipt of the earnings:

- (1) A requirement that the deposit or account and the earnings thereon shall be withdrawn in multiples of even amounts.
- (2) A requirement that a notice of intention to withdraw shall be given in advance of the withdrawal.

(d) *Examples of constructive receipt.* Interest coupons which have matured and are payable but which have not been cashed are constructively received in the taxable year during which the coupons mature, unless it is shown that there are no funds available for payment of the interest during the year. Dividends on corporate stock shall be constructively received when unqualifiedly made subject to the demand of the shareholder. However, if a dividend is declared payable on December 31 and the corporation followed its usual practice of paying the dividends by checks mailed so that the shareholders would not receive them until January of the following year, the dividends are not be considered to have been constructively received in December. Generally, the amount of dividends or interest credited on savings bank deposits or to shareholders of organizations such as building and loan associations or cooperative banks is income to the depositors or shareholders for the taxable year when credited. However, if a portion of the dividends or interest is not subject to withdrawal at the time credited, the portion

may not be constructively received and does not constitute income to the depositor or shareholder until the taxable year in which the portion first may be withdrawn. Accordingly, if under a bonus or forfeiture plan a portion of the dividends or interest is accumulated and may not be withdrawn until the maturity of the plan, the crediting of the portion to the account of the shareholder or depositor may not constitute constructive receipt. However, in this case the credited portion shall be income to the depositor or shareholder in the year in which the plan matures. Accrued interest on unwithdrawn insurance policy dividends is gross income to the taxpayer for the first taxable year during which the interest may be withdrawn by him.

(e) *Present economic benefit.* An amount paid as a contribution shall be considered as received if an employee receives rights, such as coverage under a plan that are the following:

- (1) Of a value which can in no event fall materially below the amount of the contribution.
- (2) Presently belonging to the employee.
- (3) Unequivocally provided for the ultimate benefit of the employee under whatever contingency and whatever circumstance the occasion for the benefit should arise.

(f) *Wage and salary deductions; taxability.*

(1) Except as provided in paragraph (2), any amount lawfully deducted and withheld by an employer from the remuneration of an employee and accounted for as a part of the employee's total remuneration shall be considered to have been paid to the employee as compensation at the time the deduction is made.

(2) An amount will not be considered to have been paid to the employee because the amount is specified in a written cafeteria plan document as being available to the participant for the purpose of selecting or purchasing benefits under a plan or as additional cash remuneration received in lieu of coverage under a plan. Whether an amount is specified in a cafeteria plan document as being available to a participant shall be determined using Federal rules.

Example.

Employer M is a manufacturing company situated in this Commonwealth and under its collective bargaining agreement with a union, all nonmanagement personnel must contribute \$15 per week from their gross salary toward the purchase of Blue Cross/Blue Shield coverage and \$3 per week toward the purchase of group life insurance.

The plan is not a Federally qualifying cafeteria plan.

Conclusion: M shall withhold Pennsylvania Personal Income Tax from the \$18 contributed by each nonmanagement employee toward benefits.

Authority

The provisions of this § 101.7 amended under section 354 of the Tax Reform Code of 1971 (72 P. S. § 7254).

Source

The provisions of this § 101.7 amended August 4, 2000, effective August 5, 2000, 30 Pa.B. 3938. Immediately preceding text appears at serial pages (261967) to (261969) and (205345).

Notes of Decisions

If a cash basis taxpayer actually receives a lump sum distribution from a profit sharing trust, the entire amount is taxable unless the taxpayer can demonstrate that a portion of the distribution was constructively received prior to June 1, 1971. *Gosewisch v. Department of Revenue*, 397 A.2d 1288 (Pa. Cmwlth. 1979).

If a taxpayer does not have a legal right to money in an employer-sponsored profit sharing trust until termination of employment, disability or death, payments to the trust are not considered to be constructively received by the taxpayer. *Gosewisch v. Department of Revenue*, 397 A.2d 1288 (Pa. Cmwlth. 1979).

§ 101.8. Income from sources within this Commonwealth.

(a) For a nonresident individual, estate or trust income from sources within this Commonwealth includes all income enumerated and classified under Chapter 103, Subchapter B (relating to determination of tax) to the extent it is earned, received or acquired from sources within this Commonwealth as follows:

(1) By reason of ownership or disposition of an interest in real or tangible personal property in this Commonwealth.

(2) In connection with a trade, profession or occupation carried on in this Commonwealth or for the rendition of personal services performed in this Commonwealth.

(3) As a distributive share of the income of an unincorporated business, profession, enterprise, undertaking or other activity as the result of work done, services rendered or other business activities conducted in this Commonwealth, except as allocated to another state under regulations promulgated by the Department.

(4) From intangible personal property employed in a trade, profession, occupation or business carried on in this Commonwealth.

(b) Income from intangible personal property such as interest or dividends even though paid by a Commonwealth bank or corporation may not be income from sources within this Commonwealth, except as provided in subsection (a)(4).

(c) Income derived from ownership of an interest in real or tangible personal property includes rental income from real or tangible personal property in this Commonwealth or an interest therein. Rental income does not include income attributable to the ownership of an interest in real or tangible personal property located outside of this Commonwealth, even though rental payments in respect of the property may be made from or received at a point within this Commonwealth.

(d) A trade, profession or occupation shall be carried on in this Commonwealth by a nonresident when he or a partnership or association of which he is a member occupies, has, maintains or operates an office, shop, store, warehouse, factory, agency or other place where his or its affairs are systematically and regu-

larly carried on. This definition is not exclusive. A business shall be carried on within this Commonwealth if activities within this Commonwealth in connection with the business are conducted in this Commonwealth with a fair measure of permanency and continuity.

(e) Personal services by a nonresident shall be deemed to have been performed within this Commonwealth if, and to the extent that, his services were rendered within this Commonwealth. Compensation for personal services rendered by a nonresident individual wholly without this Commonwealth is not taxable regardless of the fact that payment may be made from a point within this Commonwealth or that the employer is a resident individual, partnership or corporation. If the personal services are performed within and without this Commonwealth, the portion of the compensation attributable to the services performed within this Commonwealth shall be determined in accordance with § 109.3 (relating to business carried on wholly within this Commonwealth). If personal services are performed within this Commonwealth, whether or not as an employee, the compensation for the services constitutes income from Commonwealth sources regardless of the following:

- (1) That the compensation is received in a taxable year after the year in which the services were performed.
- (2) That the compensation is received by someone other than the person who performed the services.

Cross References

This section cited in 61 Pa. Code § 109.1 (relating to taxable income of nonresident individuals); 61 Pa. Code § 109.3 (relating to business carried on wholly within this Commonwealth); and 61 Pa. Code § 109.4 (relating to business carried on partly within and partly without this Commonwealth).

§ 101.9. Trusts.

(a) *Charitable trust.* A charitable trust shall be exempt from the personal income tax. This exemption has been granted because the trusts serve a public rather than a private interest. Accordingly, no trust may be deemed to be a charitable trust unless it is operated exclusively during the taxable year in question for religious, charitable, scientific, literary or educational purposes and serves a public interest as compared with a private interest. Additional requirements are as follows:

- (1) A trust created by the will of an individual who at the time of his death was a resident individual, one created by a person who at the time of the creation was a resident, or one consisting in whole or in part of property transferred to it by a person who at the time of the transfer was a resident and which is a charitable trust may not be within the term resident trust as used in this article.

(2) A trust shall be regarded as operated exclusively for one or more exempt purposes only if it engages primarily in activities which accomplish one or more of the exempt purposes set forth in subsection (a)(1).

(3) A trust is not regarded as charitable if more than an insubstantial part of its activities is not in furtherance of an exempt purpose. A trust is not deemed to be operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals. For example, a trust is created by a resident individual and under its governing instrument income is payable to the spouse of the individual for life. Upon the death of the spouse all income of the trust is payable, at the discretion of the trustees, to charitable organizations. The trust may not be a charitable trust for a year in which the income of the trust is payable to the spouse of the individual.

(b) *Influencing of legislation as purpose of trust.* A trust is not deemed to be operated exclusively for one or more of the exempt purposes if a substantial part of its activities is attempting to influence legislation by propaganda or otherwise. An organization shall be regarded as attempting to influence legislation if the organization does any of the following:

(1) Contacts, or urges the public to contact, members of a legislative body for the purpose of proposing, supporting or opposing legislation.

(2) Advocates the adopting or rejection of legislation. The term legislation includes action by Congress, a State legislature, a local council or similar governing body, or the public in a referendum, initiative, constitutional amendment or similar procedure. An organization may not fail to meet the test as a charitable trust merely because it advocates, as an insubstantial part of its activities, the adoption or rejection of legislation. An organization is not deemed to be operated exclusively for one or more of the exempt purposes if it participates or intervenes directly or indirectly in a political campaign on behalf of or in opposition to a candidate for public office. Activities which constitute participation or intervention in a political campaign on behalf of or in opposition to the candidate shall include, but are not limited to, the publication or distribution of written or printed statements or the making of oral statements on behalf of or in opposition to a candidate.

(c) *Special rule.* With respect to a trust consisting in whole or in part of property transferred to it by a person who at the time of the transfer was a resident, the tax imposed by § 103.1 (relating to tax imposed on residents) applies only to the income realized from the property transferred to the trust by the resident person, from dealings with respect to the property, and to an income realized from the reinvestment of the proceeds realized from a sale or exchange of the property.

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