

**CHAPTER 153. CORPORATE NET INCOME TAX****SUBJECTABILITY TO TAX REPORTING**

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**SUBJECTABILITY TO TAX REPORTING****§ 153.1. Taxpayers.**

(a) *Inclusions.* The following entities organized and incorporated under the statutes of this Commonwealth, the United States or another state, territory, foreign country or dependency, and doing business in this Commonwealth, or carrying on activities in this Commonwealth, or owning property in this Commonwealth, or having capital or property employed or used in this Commonwealth by or in the name of itself, or a person, partnership, association, limited partnership, joint-stock association or corporation are taxpayers for purposes of this article. See section 401(1) of the TRC (72 P. S. § 7401(1)).

- (1) Corporations having capital stock.
- (2) Joint-stock associations.
- (3) Limited partnerships, including:

- (i) Registered partnerships formed and existing under the act of May 9, 1899 (P. L. 261, No. 153) (59 P. S. §§ 241—311) prior to January 1, 1971, the effective date of its repeal by section 1203(e)(2) of the Business Corporation Law (15 P. S. § 2203(e)(2)).

- (ii) Partnership associations formed and existing under the act of June 2, 1874 (P. L. 271, No. 153) (15 P. S. §§ 12701—12710) prior to its repeal, effective August 9, 1970, by section 14(a)(1) of the Professional Corporation Law (15 P. S. § 2914(a)(1)).

- (4) Professional corporations formed under the Professional Corporation Law (15 P. S. §§ 2901—2914) and professional associations formed under the

Professional Association Act (15 P. S. §§ 12601—12619) which elect, under section 4 of the Professional Corporation Law (15 P. S. § 2904), to accept the provisions thereof.

(5) Corporations having authority to issue capital stock and organized or created by or under the nonprofit corporation law of a state.

(6) S corporations, as provided for under section 1361 of the IRC (26 U.S.C.A. § 1361).

(7) Domestic International Sales Corporations, commonly known as DISCs, as provided for under section 991 of the IRC (26 U.S.C.A. § 991).

(8) Foreign Sales Corporations, commonly known as FSCs, as provided for under section 921 of the IRC (26 U.S.C.A. § 921).

(9) General or limited partnerships formed under the statutes of the Commonwealth which elect to be governed by 15 Pa.C.S. Ch. 87 (relating to electing partnerships).

(b) *Exclusions.* The following entities are not taxpayers for purposes of this article. See section 401 of the TRC (72 P. S. § 7401).

(1) Massachusetts Trust or business trust, or common law trusts or Real Estate Investment Trusts (commonly referred to as REITs, as provided for under section 856 of the IRC (26 U.S.C.A. § 856)) which are not organized or created by or under the statutory law of a state.

(2) Nonprofit corporations without authority to issue capital stock.

(3) Limited partnerships formed under or governed by 15 Pa.C.S. Ch. 85 (relating to Pennsylvania Revised Uniform Limited Partnership Act) or the Uniform Limited Partnership Act of another state.

(4) Corporations having a valid Pennsylvania S Corporation election in effect for the taxable year.

#### Authority

The provisions of this § 153.1 issued under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408); amended under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

#### Source

The provisions of this § 153.1 amended October 5, 1984, effective October 6, 1984, 14 Pa.B. 3624; amended January 16, 1987, effective January 17, 1987, 17 Pa.B. 273. Immediately preceding text appears at serial pages (94411) to (94412).

### § 153.2. [Reserved].

## TAX BASE

### § 153.11. Definition of “taxable income.”

As used in this chapter, the term “taxable income” means “Federal taxable income before net operating loss deduction and special deductions” (presently Line 28 of Page 1 of Federal IRS Form 1120 or Line 24 of Page 1 of Federal

IRS Form 1120-A) as returned to and ascertained by the Federal government and as modified or adjusted under section 401(3)1. of the TRC (72 P. S. § 7401(3)1.) and under this chapter, unless the context clearly indicates otherwise.

**Authority**

The provisions of this § 153.11 amended under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

**Source**

The provisions of this § 153.11 amended November 3, 1978, effective November 4, 1978, 8 Pa.B. 3035; amended January 1, 1987, effective January 17, 1987, 17 Pa.B. 273; amended March 19, 1993, effective March 20, 1993, 23 Pa.B. 1322. Immediately preceding text appears at serial pages (115309) to (115310).

**§ 153.12. Altering Federal taxable income.**

*Foreign taxes paid.* Foreign taxes taken by the taxpayer as a credit against Federal taxes are not allowed to reduce taxable income. Reference should be made to § 153.13 (relating to Federal tax credits). Foreign taxes taken by the taxpayer as a deduction in arriving at Federal taxable income are a proper deduction (reflected presently on Line 17 of Page 1 of Federal IRS Forms 1120 and 1120-A). See § 153.13.

**Authority**

The provisions of this § 153.12 issued under section 270 of the Tax Reform Code of 1971 (72 P. S. § 7270); amended under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

**Source**

The provisions of this § 153.12 amended October 5, 1984, effective October 6, 1984, 14 Pa.B. 3624; amended January 16, 1987, effective January 17, 1987, 17 Pa.B. 273. Immediately preceding text appears at serial pages (94413) and (36116).

**Cross References**

This section cited in 61 Pa. Code § 153.13 (relating to Federal tax credits); and 61 Pa. Code § 153.25 (relating to payroll factor).

**§ 153.13. Federal tax credits.**

In the determination of taxable income, Federal tax credits, for example the Federal tax credit for taxes paid to a foreign country, is not allowed to reduce the "Federal taxable income before net operating loss deduction and special deductions" (presently Line 28 of Page 1 of Federal IRS Form 1120 or Line 24 of Page 1 of Federal IRS Form 1120-A). Reference should also be made to § 153.12 (relating to altering Federal taxable income).

**Authority**

The provisions of this § 153.13 amended under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

**Source**

The provisions of this § 153.13 amended January 16, 1987, effective January 17, 1987, 17 Pa.B. 273. Immediately preceding text appears at serial page (36116).

**Cross References**

This section cited in 61 Pa. Code § 153.12 (relating to altering Federal taxable income).

**§ 153.14. Other adjustments.**

The following items will be allowed as special deductions in determining Commonwealth taxable income if supported by a detailed schedule:

(1) *Special deduction for western hemisphere trade corporations.* A deduction will be allowed in the amount of the deduction permitted under sections 921 and 922 of the IRC (26 U.S.C.A. §§ 921 and 922).

(2) *Contribution adjustments to State taxable income.* A taxpayer filing with the Federal government as a member of a consolidated group may be entitled, on a separate company reporting basis, to a larger contribution deduction in arriving at Commonwealth taxable income. Because consolidated reporting is not permitted for Commonwealth purposes, the taxpayer may reflect on a separate company reporting basis the contribution deduction to which it would have been entitled had it filed a separate return with the Federal government.

(3) *Special deduction for section 1250 of the IRC (26 U.S.C.A. § 1250) property depreciated on an accelerated depreciation basis when the accelerated depreciation falls below straight line depreciation.* This adjustment may be taken in accordance with the following:

(i) A taxpayer depreciating section 1250 of the IRC (26 U.S.C.A. § 1250) property on an accelerated depreciation basis is permitted a special deduction to taxable income to be apportioned when the accelerated depreciation falls below straight line depreciation. The amount of the deduction for a tax year is limited to the amount of depreciation below straight line. The aggregate adjustment to taxable income to be apportioned for amounts below straight line may not exceed the aggregate of the amount added to taxable income to be apportioned in previous tax years.

*Example:* Taxpayer, a calendar year company, purchases a plant, which is a section 1250 of the IRC property, on January 1, 1976, having a depreciable value of \$900,000 and a 20-year useful life. Taxpayer depreciates the property on a double-declining (accelerated) basis. Straight-line depreciation would be \$45,000 per year. Taxpayer's depreciation on its Federal return for 1984 would be \$43,047. Taxpayer's 1984 taxable income to be apportioned on its Commonwealth report would be adjusted by permitting a deduction for the amount of depreciation below straight-line or \$1,953 (\$45,000 minus \$43,047).

(ii) A taxpayer depreciating section 1250 of the IRC property on an accelerated depreciation basis is permitted a special deduction to taxable income to be apportioned when a section 1250 of the IRC property is sold. The Department will permit the taxpayer a special deduction for accelerated depreciation previously included in income to be apportioned in prior years.

*Example:* Taxpayer purchases a building in 1971 and elects to depreciate the building on an accelerated depreciation basis. The following amounts were included as tax preference items for the years listed:

<i>Year</i>	<i>Tax Preference Amount</i>
1971	\$10,000
1972	7,500
1973	5,000
1974	2,500
Total	\$25,000

The building was sold on January 1, 1975. Each of the years listed in this example produced taxable income and the tax preference amounts listed in this example were included in income to be apportioned. The Department will permit the taxpayer a special deduction of \$25,000.

(iii) The special deductions described in subparagraphs (i) and (ii) will not be permitted for a tax year when the taxpayer did not have income to be apportioned.

(4) *Special deduction for certified pollution control facilities amortized under section 169 of the IRC (26 U.S.C.A. § 169).* This adjustment may be taken in accordance with the following:

(i) A taxpayer depreciating a certified pollution control facility under section 169 of the IRC (26 U.S.C.A. § 169) is permitted a special deduction to taxable income to be apportioned when the rapid amortization period expires. The amount of the deduction for a given tax year is limited to the amount of depreciation which the taxpayer would have been allowed under the depreciation method elected under section 167 of the IRC (26 U.S.C.A. § 167) minus a depreciation which the taxpayer has taken for a given tax year. The total special deductions may not exceed the total amount added to taxable income to be apportioned in prior years.

*Example:* Taxpayer's, a calendar year company, rapid amortization period of a certified pollution control facility constructed in late December 1971, begins January 1972 and expires December 1976. No other depreciation has been taken and the depreciable value is \$1 million and the useful life is 20 years. Straight-line depreciation

would be \$50,000 per year. Since the useful life is greater than 15 years, taxpayer's Federal rapid amortization deduction is available only for the portion of the property's depreciable value attributable to the first 15 years of its useful life or 75% (15/20) of its depreciable value (75% of \$1 million or \$750,000) over the 60 months rapid amortization period. The remaining 25% of its depreciable value (25% of \$1 million or \$250,000) is depreciated by the straight-line method over the 20-year useful life period. Taxpayer's depreciation on its Federal return for 1977 would be \$12,500. Taxpayer's 1977 taxable income to be apportioned on its Commonwealth report would be adjusted by permitting a deduction for the amount of depreciation below straight-line or \$37,500 (\$50,000 minus \$12,500).

(ii) The special deduction described in subparagraph (i) will not be permitted for a tax year when the taxpayer did not have income to be apportioned.

#### Source

The provisions of this § 153.14 amended December 2, 1977, effective December 3, 1977, 7 Pa.B. 3451; amended March 19, 1993, effective March 20, 1993, 23 Pa.B. 1322. Immediately preceding text appears at serial pages (115311) to (115312) and (174431).

#### Notes of Decisions

##### *Depreciation*

The taxpayer was not denied the right to use straight line depreciation on its State return since it chose to use accelerated depreciation on its Federal tax return. *Roosevelt Arms, Inc. v. Commonwealth*, 608 A.2d 648 (Pa. Cmwlth. 1992).

##### *Special Deduction*

The taxpayer did not prove that it or its predecessor added back any depreciation in prior years; therefore, having failed to meet its burden, the taxpayer was not entitled to special deductions for its "Section 1250 property." *Eat 'n Park Restaurants Business Trust v. Commonwealth*, 803 A.2d 845 (Pa. Cmwlth. 2002); exceptions sustained in part, overruled in part 821 A.2d 160 (Pa. Cmwlth. 2003).

### § 153.15. Net loss deduction.

(a) *Definitions.* The following words and terms, when used in this section, have the following meanings, unless the context clearly indicates otherwise:

(1) *Net loss*—For a corporation ineligible to allocate or apportion its income, the negative amount for a taxable year arrived at under section 401(3)1. of the TRC (72 P. S. § 7401(3)1.). For a corporation eligible to allocate or apportion its income, the negative amount for a taxable year arrived at under section 401(3)2. of the TRC. Negative amounts shall be allocated and apportioned in the same manner as positive amounts.

(2) *Net loss deduction*—The net loss deduction for a taxable year is the lesser of the amount of the net loss which may be carried over to the taxable year or taxable income for the taxable year.

(3) *Taxable year*—The taxable year of a corporation is the taxable year which the corporation, or a consolidated group with which the corporation participates in the filing of consolidated returns, actually used in reporting taxable income to the Federal government.

(b) *General rule.* For taxable years beginning in 1982 and thereafter, a net loss deduction will be allowed from taxable income as arrived at under section 401(3)1. of the TRC for corporations which do not qualify to allocate or apportion their income for the taxable year or from taxable income as arrived at under section 401(3)2. of the TRC for corporations which qualify to allocate or apportion their income for the taxable year.

*Example 1.* Corporation “A” has a loss of \$100,000 before allocation and apportionment. Corporation “A” is entitled to allocate and apportion its income. Corporation “A” has a three factor apportionment formula percentage of 25%. Corporation “A” has a nonbusiness loss of \$30,000 allocable to state “X” and nonbusiness income of \$10,000 allocable to Pennsylvania. Corporation “A” has a net loss of \$10,000, determined as follows:

Taxable Income or (Loss)	(\$100,000)
Less: Nonbusiness Loss Allocable to State “X”	(\$30,000)
Less: Nonbusiness Income Allocable to Pennsylvania	10,000
Apportionable Business Income	(\$80,000)
Pennsylvania Apportionment Percentage	25%
Business Income or (Loss) Apportioned to Pennsylvania	(\$20,000)
Nonbusiness Income Allocable to Pennsylvania	10,000
Net Loss	(\$10,000)

*Example 2.* For the 12-month taxable year ended December 31, 1986, Corporation “A” has taxable income, after allocation and apportionment, of \$100,000. For the taxable year ended December 31, 1985, Corporation “A” had a net loss of \$90,000. Corporation “A” has no other net losses.

Corporation “A” has a net loss deduction of \$90,000 for its taxable year ended December 31, 1986.

(c) *Carryover.* A net loss for a taxable year may only be carried forward under the following schedule:

<i>Taxable Year</i>	<i>Carryover Period</i>
1981	1 taxable year
1982	2 taxable years
1983 and thereafter	3 taxable years



The earliest net loss shall be carried over to the earliest taxable year to which it may be carried under this schedule.

*Example.* For its taxable year ended December 31, 1986, Corporation A has taxable income, after allocation and apportionment of \$50,000. Corporation A has the following net losses available:



For taxable year ended	
December 31, 1983	\$15,000
For taxable year ended	
December 31, 1984	30,000
For taxable year ended	
December 31, 1985	20,000

All the taxable years are full 12 month years.

For its taxable year ended December 31, 1986, Corporation A has a net loss deduction of \$50,000. The deduction consists of the \$15,000 net loss from taxable year 1983, the \$30,000 net loss from taxable year 1984 and \$5,000 of the net loss from taxable year 1985.

The remaining \$15,000 of net loss from taxable year 1985 is available for carryover to Corporation A's next 2 taxable years.

(d) *Pennsylvania S Corporations.*

(1) While a corporation is in Pennsylvania S status, no loss may be carried over from a taxable year when the corporation was subject to the Corporate Net Income Tax to a taxable year when the corporation is treated as a Pennsylvania S corporation. If a corporation's Pennsylvania S election is either terminated or revoked, no loss may be carried over from a taxable year when the corporation is treated as a Pennsylvania S corporation to a taxable year during which the corporation is subject to the Corporate Net Income Tax.

(2) A taxable year during which a corporation is a Pennsylvania S corporation is considered a taxable year for determining the number of years to which a net loss may be carried. The short taxable year of a corporation after revocation or termination of Pennsylvania S status is treated as a taxable year.

(e) *Change in ownership.* Under section 401(3)4.(g) of the TRC, in the case of a change in the ownership of a corporation effected in a manner described in sections 381 or 382 of the IRC (26 U.S.C.A. §§ 381 or 382), certain limitations provided the IRC with respect to the use of net operating losses after a change in ownership shall apply for the purpose of computing the portion of the net loss available for carry-over as a deduction against income subject to the Corporate Net Income Tax, whether the change is effected by purchase, liquidation, acquisition of stock or reorganization. The applicable limitations include limitations imposed by the IRC solely on account of a change in ownership, including but not limited to, sections 269, 318 (insofar as it defines the scope of section 382 of the IRC (26 U.S.C.A. § 382)), 381 and 382 of the IRC (26 U.S.C.A. §§ 269, 318, 381 and 382). The carryover of net losses is not limited by the Federal consolidated return regulations.

**Authority**

The provisions of this § 153.15 issued under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

**Source**

The provisions of this § 153.15 adopted January 16, 1987, effective January 17, 1987, 17 Pa.B. 273.

**ALLOCATIONS AND APPORTIONMENTS****§ 153.21. Transacting business outside.**

(a) A taxpayer may allocate and apportion if in addition to transacting business outside this Commonwealth as established in subsection (b) it is either “subject to” a tax in another state as provided in § 153.22 (relating to subject to) or another state has “jurisdiction to subject” as provided in § 153.23 (relating to jurisdiction to subject) the taxpayer to a Corporate Net Income Tax.

(b) What constitutes transacting business outside cannot be precisely defined. It may be generally stated that a taxpayer is “transacting business outside” when its presence outside this Commonwealth is related to its actual business activity. The presence may be through, but not limited to, administrative functioning, property ownership, or sales activity.

*Example 1.* Taxpayer actively engaged in manufacturing farm equipment in this Commonwealth. In State W taxpayer owned a manufacturing plant. Taxpayer leased the plant to another company to be used for the manufacturing farm equipment. Taxpayer acquired the lessee’s products and subsidized its operations by advancing money to it. Upon the expiration of the lease, the manufacturing operations in State W ceased completely. Up to the expiration of the lease, taxpayer was transacting business outside this Commonwealth. After the expiration of the lease, taxpayer’s ownership of the property in State W was not related to its actual business activity, and, therefore, taxpayer was not transacting business outside this Commonwealth.

*Example 2.* Taxpayer manufactures sparkplugs in this Commonwealth and all activities are carried on in this Commonwealth except that administrative function and executive policies are performed and established by taxpayer’s officers located in the State O. The activities in State O are related to the manufacturing activity in this Commonwealth and are part of the taxpayer’s business. Thus, taxpayer is transacting business outside of this Commonwealth.

**Source**

The provisions of this § 153.21 adopted January 27, 1978, effective January 28, 1978, 8 Pa.B. 257.

**§ 153.22. Subject to.**

(a) A taxpayer is “subject to” one of the four taxes specified in section 401(3)2.(a)(3) of the TRC (72 P. S. § 7401(3)2.(a)(3)) in a particular state if it carries on business activity in the state and the state in fact requires it to file, and, in fact, does file one of the four enumerated tax reports based on the business activity. A taxpayer claiming it is “subject to” one of the four specified taxes may be required by the Bureau to furnish proof that the taxpayer has filed the required tax report in the other state and the other necessary information.

*Example:* State A has a corporation franchise tax measured by net income for the privilege of doing business in that state. Taxpayer files a return based upon its business activity in the state but the amount of computed liability is less than the minimum tax. Taxpayer pays the minimum tax. Taxpayer is subject to State A’s corporation franchise tax.

(b) A taxpayer is not “subject to” one of the specified taxes within the meaning of section 401(3)2.(a)(3) (72 P. S. § 7401(3)2.(a)(3)) if the taxpayer voluntarily files one or more of the tax reports when not required to do so by the laws of that state or pays a minimum fee for qualification, organization or the privilege of doing business in that state, but:

- (1) Does not engage in business activity in that state.
- (2) Does actually engage in some business activity, but not sufficient for nexus.

*Example:* State A has a corporation franchise tax measured by net income, for the privilege of doing business in that state. Taxpayer files a return and pays the \$50 minimum tax, although it carries on no business activity in State A. Taxpayer is not “taxable” in State A.

(c) Only those taxes enumerated in section 401(3)2.(a)(3) of the TRC (72 P. S. § 7401(3)2.(a)(3)) which may be considered as basically revenue raising rather than regulatory measures shall be considered in determining whether the taxpayer is “subject to” one of the taxes specified in section 401(3)2.(a)(3) of the TRC (72 P. S. § 7401(3)2.(a)(3)).

*Example:* State A requires nonresident corporations which qualify or register in State A to pay to the Secretary of State an annual license fee or tax for the privilege of doing business in the state regardless of whether the privilege is in fact exercised. The amount paid is determined according to the total authorized capital stock of the corporation; the rates are progressively higher by bracketed amounts. The statute sets a minimum fee of \$50 and a maximum fee of \$500. Failure to pay the tax bars a corporation from utilizing the State courts for enforcement of its rights. State A also imposes a corporation income tax. Nonresident Taxpayer is qualified in State A and pays the required fee to the Secretary of State but does not carry on any activities in State A other than utilizing its courts. Taxpayer is not “taxable” in State A.

**Source**

The provisions of this § 153.22 adopted February 13, 1976, effective February 14, 1976, 6 Pa.B. 327.

**Cross References**

This section cited in 61 Pa. Code § 153.21 (relating to transacting business outside).

**§ 153.23. Jurisdiction to subject.**

(a) A particular state has “jurisdiction to subject” the taxpayer to a net income tax, if the taxpayer’s business activity in the state is sufficient to give the State jurisdiction to impose at least a net income tax under the constitution and statutes of the United States. See section 401(3)2.(a)(1)(F) of the TRC (72 P. S. § 7401(3)2.(a)(1)(F)). Whether the state does in fact impose a tax is not relevant. Jurisdiction to tax is not present where the state is prohibited from imposing the tax by reason of the provisions of 15 U.S.C.A. §§ 381—385.

(b) The determination of whether the state has “jurisdiction to subject” the taxpayer to a net income tax shall be made upon the same rules that are applied in determining whether a taxpayer has sufficient activity in this Commonwealth to subject the taxpayer at least to the Pennsylvania Corporate Net Income Tax. See section 401 of the TRC (72 P. S. § 7401).

*Example 1.* Taxpayer manufactures pin ball machines in this Commonwealth. Taxpayer has salesmen in State N who have the right to, and do in fact, accept orders there. State N has no corporate tax statutes. State N has “jurisdiction to subject” taxpayer to a net income tax because 15 U.S.C.A. §§ 381—385 does not apply.

*Example 2.* Taxpayer manufactures farm equipment in this Commonwealth and in foreign country B. Both the Commonwealth and foreign country B impose a net income tax, but foreign country B exempts corporations engaged in manufacturing farm equipment. Foreign country B has jurisdiction to subject taxpayer to a net income tax.

**Authority**

The provisions of this § 153.23 amended under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

**Source**

The provisions of this § 153.23 adopted January 27, 1978, effective January 28, 1978, 8 Pa.B. 257; amended January 16, 1987, effective January 17, 1987, 17 Pa.B. 273. Immediately preceding text appears at serial page (36121).

**Cross References**

This section cited in 61 Pa. Code § 153.21 (relating to transacting business outside).

**§ 153.24. [Reserved].****Source**

The provisions of this § 153.24 adopted September 17, 1976, effective September 18, 1976, 6 Pa.B. 2286; amended January 16, 1987, effective January 17, 1987, 17 Pa.B. 273; amended April 24, 1992, effective April 25, 1992, 22 Pa.B. 2243. Immediately preceding text appears at serial pages (115319) to (115323).

**§ 153.25. Payroll factor.**

(a) *General.* The payroll factor is a fraction, the numerator of which is the total amount of compensation paid in this Commonwealth during the tax period by the taxpayer to its employees and the denominator of which is the total amount of compensation paid everywhere during the tax period by the taxpayer to its employees.

(b) *Effect of method of accounting.* If the taxpayer uses either the cash or accrual method of accounting in reporting its taxable income to the IRS, the total amount paid to individuals for a tax period is determined upon the basis of the accounting method of the taxpayer.

(c) *Effect of denial of deduction for wages and salaries.* The payroll factor shall include compensation whether or not included as part of the deduction for wages and salaries of the taxpayer. Reference should also be made to § 153.12 (relating to altering Federal taxable income).

**Source**

The provisions of this § 153.25 adopted June 9, 1978, 8 Pa.B. 1579, amended February 20, 1981, effective June 23, 1979, 11 Pa.B. 726. Immediately preceding text appears at serial page (36125).

**Cross References**

This section cited in 61 Pa. Code § 153.29 (relating to corporation tax: interest in partnership/joint venture).

**§ 153.26. Sales factor.**

(a) *Interest on United States securities and dividends received.* Gross receipts in the form of interest on United States securities and dividends received shall be excluded from sales. Reference should be made to section 401(3)2.(a)(1)(E), (15) and (17) of the TRC (72 P. S. § 7401(3)2.(a)(1)(E), (15) and (17)).

(b) *Sales of tangible personal property.* The following sales factors shall apply to the sale of tangible personal property.

(1) *When sales of tangible personal property are in this Commonwealth.* Sales of tangible personal property are in this Commonwealth if the property is delivered or shipped to a purchaser within this Commonwealth regardless of the f.o.b. point or other conditions of the sale. Reference should be made to section 401(3)2.(a)(16) of the TRC (72 P. S. § 7401(3)2.(a)(16)).

(2) *General rule.* Sales of tangible personal property are in the state in which delivery to the purchaser occurs.

*Example:* A taxpayer produces beer in New York. Taxpayer sells the beer to a distributor located in this Commonwealth. Distributor sends its truck into New York to taxpayer's plant to pick up the beer and brings the beer back to its Commonwealth business location. Delivery has occurred in New York and these taxpayer's sales are in New York.

(3) *Definitions.* The following words and terms, when used in this chapter, have the following meanings, unless the context clearly indicates otherwise:

(i) *Delivered*—The physical transfer of possession of tangible personal property to the purchaser.

(ii) *Purchaser*—The term includes the following:

(A) The ultimate recipient of the property if the taxpayer, at the designation of the purchaser, delivers property in this Commonwealth to the ultimate recipient.

*Example:* A taxpayer in this Commonwealth sold merchandise to a purchaser in New York. Taxpayer directed the manufacturer of the merchandise in Ohio to ship the merchandise to the purchaser's customer in this Commonwealth under purchaser's instructions. The sale by the taxpayer is in this Commonwealth.

(B) A consignee if the taxpayer (consignor) delivers or ships property in this Commonwealth to a consignee which the consignee subsequently sells.

*Example:* The taxpayer (consignor) located in Ohio ships property to this Commonwealth to a consignee. Consignee, also a taxpayer, sells and ships such property to New York to its purchaser. The consignor's sale is in this Commonwealth and the consignee's sale is in New York.

(iii) *Shipped*—The transportation of tangible personal property, including delivery, to the purchaser.

(4) *Application of general rule.* The general rule shall be applied as follows:

(i) Property shall be deemed to be delivered to a purchaser within this Commonwealth if the shipment terminates in this Commonwealth, even though the property is subsequently transferred by the purchaser to another state.

*Example:* A taxpayer makes a sale of desks to a purchaser who maintains a central warehouse in this Commonwealth at which merchandise purchases are received. The purchaser reships sale. The taxpayer's desks shipped to the purchaser's warehouse in this Commonwealth are sales in this Commonwealth.



(ii) When property is being shipped by a taxpayer (consignor) from the state of origin to a consignee in another state and is diverted while enroute and shipped in this Commonwealth to a purchaser, the sale is in this Commonwealth.

*Example:* The taxpayer begins shipment of property from Ohio to the purchaser's place of business in New York. While enroute the property is diverted to and shipped to the purchaser's place of business in this Commonwealth. The sale by the taxpayer is in this Commonwealth.

#### Source

The provisions of this § 153.26 amended through November 16, 1984, effective November 17, 1984, 14 Pa.B. 4163. Immediately preceding text appears at serial pages (81525) to (81526) and (89263).

#### Notes of Decisions

##### *Construction*

This section is contrary to the clear wording of § 401(3)2(a)(16) of The Tax Reform Code. *Commonwealth v. Gilmour Manufacturing Co.*, 822 A.2d 676 (Pa. 2003).

##### *Interest on United States Securities and Dividends Received*

In determining that the regulation excluding gross receipts in the form of interest on U.S. securities and dividends received from "sales" for sales factor purposes applies to computation of the Capital Stock Tax as well as the Corporate Net Income Tax, the court held that the Revenue Department's interpretation of the tax code as expressed in the regulation is reasonable and not clearly inconsistent with the statute. *SmithKline Beckman Corp. v. Commonwealth*, 482 A.2d 1344 (Pa. Cmwlth. 1984); order affirmed 498 A.2d 374 (Pa. 1985).

#### Cross References

This section cited in 61 Pa. Code § 153.29 (relating to corporation tax: interest in partnership/joint venture); and 61 Pa. Code § 170.11 (relating to documentation requirements to establish out-of-State sales after *Gilmour Manufacturing* decision).

### § 153.27. Railroad, truck, bus and airline companies.

(a) The taxpayer shall be transacting business outside this Commonwealth in order to be entitled to the use of the appropriate special statutory apportionment fraction. See section 401(3)2. of the TRC (72 P. S. § 7401(3)2.).

(b) The taxpayer is not required to have income from business activity which is taxable both within and without this Commonwealth as a further condition precedent to its use of the revenue miles apportionment fraction but is entitled to the use of the revenue miles apportionment fraction without regard to whether or not

the taxpayer has income from business activity which is taxable outside this Commonwealth. See section 401(3)2.(a)(2) and (3) of the TRC (72 P. S. § 7401(3)2.(a)(2) and (3)).

**§ 153.28. Property factor.**

(a) *Definitions.* The following words and terms, when used in this section, have the following meanings, unless the context clearly indicates otherwise:

(1) *Net annual rental rate*—The annual rental rate paid by the taxpayer for an item of real or tangible personal property less annual rental income received by the taxpayer from subrentals, but not less than zero.

(2) *Original cost*—The basis of the real or tangible personal property for Federal income tax purposes at the time of acquisition by the taxpayer and adjusted by subsequent capital additions or improvements thereto and partial disposition thereof, by reason of sale, exchange, abandonment and the like.

(3) *Owned*—Property to which the taxpayer has both legal and equitable title, property to which the taxpayer has legal title subject to the security interest of another and property which the taxpayer is purchasing under an installment sales agreement or similar agreement under the terms of which legal title remains in the seller for security purposes until the purchase price is paid.

(4) *Owned or rented and used*—Property owned by the taxpayer and used by the taxpayer. Property rented to the taxpayer and used by the taxpayer.

(5) *Real and tangible personal property*—Land, buildings, machinery, equipment, furniture, fixtures, automobiles, trucks, inventory and other similar property. The term does not include coin, currency, shares of stock or evidence of indebtedness.

(6) *Used*—Actually used or available for or capable of being used during the taxable year by the taxpayer.

(b) *General.* The property factor is a fraction, the numerator of which is the average value of the taxpayer's real and tangible personal property owned or rented and used in this Commonwealth during the taxable year and the denominator of which is the average value of all of the taxpayer's real and tangible personal property owned or rented and used during the taxable year.

(c) *Inclusions.*

(1) *Mineral interests.* A leasehold interest in minerals in place, however the interest may be designated, described or characterized by the law of the situs state, is included in the property factor as owned property.

(2) *Minerals.* Minerals which have been severed or extracted are included in the property factor.

(3) *Partially used construction in progress.* The average value of the real and tangible personal property owned by the taxpayer and partially used by the taxpayer while construction is being completed shall, to the extent used, be included in the property factor. A schedule detailing the basis of the value of partially used construction in progress shall be submitted to the Department.

(4) *Mobile and movable property.* The value of mobile and movable property, such as construction equipment, trucks, automobiles or leased electronic equipment, which are located and used within and without this Commonwealth during the taxable year is determined for the purposes of the numerator of the factor on an equitable and reasonable basis, such as on a time used or mileage basis. Property in transit between locations of the taxpayer to which it belongs shall be considered to be at the destination for purposes of the property factor. Property in transit between a seller and buyer which is included by a taxpayer in the denominator of its property factor in accordance with its regular accounting practices shall be included in the numerator according to the state of destination.

(d) *Exclusions.*

(1) *Construction in progress.* Real and tangible personal property owned but not used by the taxpayer because the property is in the process of construction is excluded from the property factor.

(2) *Security interests.* The security interest of a taxpayer as seller or lessor in personal property sold or leased under a conditional sale, bailment lease, chattel mortgage or other contract providing for the retention of a lien or title as security for the sale price of the property is excluded from the property factor.

(3) *Idle property.* Property which is not actually used or available for or capable of being used during the taxable year by the taxpayer is excluded from the property factor.

*Example 1.* The taxpayer closes one of its facilities with the intention that the closing will be permanent. The facility remains closed for several years, until it can be disposed of. The property would be included in the property factor the year the facility is closed, but would thereafter be excluded.

*Example 2.* The taxpayer closes its manufacturing facility for a 3-month period during which the facility is refurbished. The property would remain in the property factor.

*Example 3.* The taxpayer owns certain mineral interests which have been depleted of reasonably recoverable minerals. The mineral interests should be excluded from the property factor thereafter.

(e) *Valuation of owned property.*

(1) *General rule.* Real and tangible personal property owned by the taxpayer, other than inventories, shall be valued at original costs.

(2) *Mineral interests.* Mineral interests shall be included in the property factor at original cost. Delay rentals, to the extent not treated as a part of original cost, shall be included in the property factor as rents. Payments, however designated, which are based on the level or rate of production are not considered rent for property factor purposes.

- (3) *Inventories.* Inventories shall be included in the property factor in accordance with the valuation method used for Federal Income Tax purposes.
- (f) *Valuation of rented property.* Real and tangible personal property rented to the taxpayer shall be valued at eight times the net annual rental rate.
- (g) *Averaging property values.*
- (1) *Owned property.*
- (i) *Annual averaging.* The average value of real and tangible personal property owned by the taxpayer is determined by averaging the values at the beginning and ending of the taxable year.
- (ii) *Monthly averaging.* The Department may require the averaging of monthly values during the taxable year of real and tangible personal property owned by the taxpayer if the method is reasonably required to reflect properly the average value of the taxpayer's property. Monthly averaging will be necessary if substantial fluctuations in the value of the real and tangible personal property exist during the taxable year or if property is acquired after the beginning of the taxable year or disposed of before the end of the taxable year or if property is acquired after the beginning of the taxable year and disposed of before the end of the taxable year or for a similar circumstance.
- (2) *Rented property.* The value of property rented for only a portion of the taxable year shall be eight times the net rent paid.

#### Authority

The provisions of this § 153.28 issued and amended under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

#### Source

The provisions of this § 153.28 adopted March 9, 1984, effective March 10, 1984, 14 Pa.B. 853; amended January 16, 1987, effective January 17, 1987, 17 Pa.B. 273. Immediately preceding text appears at serial pages (96403) to (96404).

### § 153.29. Corporation tax: interest in partnership/joint venture.

#### (a) General.

(1) When a taxpayer has an interest in a partnership, joint venture, association or other unincorporated enterprise (hereinafter referred to in this section as partnership), the amount of its distributive share of partnership income shall be determined in accordance with the IRC. The taxpayer's interest in the partnership shall, for purposes of Commonwealth corporate taxation, be considered a direct interest in the assets of the partnership rather than an intangible interest. Accordingly, the taxpayer's share of the partnership's payroll, property and sales—as hereafter determined—shall be included in the apportionment factors of the taxpayer unless otherwise excluded by this section.

(2) A taxpayer's partnership interest for the purpose of computing the portion of the partnership's property, payroll and sales to be included in the tax-

payer's property, payroll and sales factors shall be determined under the partnership agreement and in accordance with the IRC

(b) *Nexus.*

(1) If the separate activities of the taxpayer or the activities of the partnership are sufficient to meet the conditions of section 401(1) of the TRC (72 P. S. § 7401(1)) relating to doing business, carrying on activities, having capital or property employed or used or owning property within this Commonwealth, then the taxpayer will be subject to corporate taxation by the Commonwealth.

(2) If the separate activities of the taxpayer or the activities of the partnership are sufficient to constitute transacting business outside this Commonwealth and render the taxpayer taxable to another state under section 401(3)2.(a)(2) and (3) of the TRC (72 P. S. § 7401(3)2.(a)(2) and (3)), then the taxpayer will be allowed to apportion and allocate its income.

(c) *Business income.*

(1) Income arising from transactions and activity in the regular course of the taxpayer's trade or business constitutes business income. The determination of whether a corporate partner's distributive share of partnership income is business income depends upon whether the income arose in the regular course of the taxpayer's trade or business, determined in accordance with § 153.24 (reserved). The taxpayer's trade or business shall include activities performed in partnership.

*Example 1:* Corporation A's distributive share of Partnership P's income is 20%. Corporation A manufactures toys which are sold in seven other states by Partnership P.

Corporation A's business income for the year, disregarding its distributive share of Partnership P's income, was \$1,000,000. Partnership P's business income for the same year was \$800,000. The business income of Corporation A is \$1,160,000 (\$1,000,000 plus 20% of \$800,000).

(2) The classification of income by the labels customarily given such as interest, rents, royalties and capital gains, is of no aid in determining whether distributive partnership income is business or nonbusiness income. The income is determined to be either business or nonbusiness income depending upon the relationship to the trade or business of the corporate partner, not of the partnership, as determined by paragraph (1).

(d) *Apportionment of business income.* A corporate partner entitled to apportionment under subsection (b)(2) shall determine the business income attributable to this Commonwealth by use of a three-factor formula consisting of property, payroll and sales of the taxpayer including its share of the partnership's property, payroll and sales for a partnership year ending within or with the taxpayer's tax year as follows:

(1) *Property factor.*

(i) *General rule.* The numerator and denominator of the property factor shall be determined as set forth in section 401(3)2.a(10)—(12) of the TRC (72 P. S. § 7401(3)2.(a)(10)—(12)) and this chapter; however, the special rules in subparagraph (ii) will apply.

(ii) *Special rules.* A portion of the partnership's real and personal property, both owned and used and rented and used during the tax year to the extent of the taxpayer's interest in the partnership shall be included in the numerator and denominator of the taxpayer's property factor. However, the value of the property which is rented or leased by the taxpayer to the partnership or *vice versa* shall, with respect to the taxpayer, be adjusted in the numerator and denominator of the taxpayer's property fraction in order to avoid duplication in the following manner:

(A) If the property is owned by the taxpayer and rented to the partnership, no portion of the rental value of the rented or leased property will be in the taxpayer's property factor.

(B) If the property is owned by the partnership and rented to the corporate partner, the property factor of the taxpayer will include the sum of:

(I) The value of the property multiplied by the percentage of taxpayer's interest in the partnership.

(II) The rental value of the property multiplied by the percentage of the interests in the partnership not held by the taxpayer.

*Example 1:* Corporation A's interest in Partnership P is 20%. Corporation A's distributive share of Partnership P's income is included in business income of Corporation A to be apportioned by formula. Corporation A owns a building (original cost of \$100,000) which is rented to Partnership P for \$12,000 per year. Corporation A must include the original cost of \$100,000 for the building in its Property Factor. Therefore, no portion of the rental value of the rented property will be reflected in the Property Factor of Corporation A.

*Example 2:* Same facts as in Example 1 except Partnership P owns the building and rents it to Corporation A. Corporation A will include \$20,000 (20% of \$100,000) in its Property Factor because of its interest in Partnership P, and in addition, Corporation A will include \$76,800 (( $\$12,000 \times 8$ ) 80%) of rental value in its Property Factor in order to give weight in the property factor to the rented building used in Corporation A's operation. Thus, the value of the building to be used in the Property Factor of Corporation A is \$96,800 (\$20,000, plus \$76,800).

(2) *Payroll factor.*

(i) *General rule.* The numerator and denominator of the payroll factor shall be determined as set forth in § 153.25 (relating to payroll factor); however, the special rules in subparagraph (ii) will also apply.

(ii) *Special rules.* The partnership's payroll shall be included in the denominator of the taxpayer's payroll factor to the extent of the taxpayer's interest in the partnership. The amount of a payroll applicable to this Commonwealth shall also be included in the numerator of the taxpayer's payroll factor.

*Example 1:* Corporation A's interest in Partnership P is 20%, and its distributive share of Partnership P's income is included in business income of Corporation A to be apportioned by formula. Corporation A's own payroll is \$1,000,000 and the payroll of Partnership P is \$800,000. Corporation A's total payroll for purposes of the Payroll Factor is \$1,160,000 (1,000,000, plus 20% of \$800,000).

(3) *Sales factor.*

(i) *General rule.* The numerator and denominator of the sales factor shall be determined as set forth in § 153.26 (relating to sales factor); however, the special rules set forth in subparagraph (i) will also apply.

(ii) *Special rules.*

(A) The partnership's sales which give rise to business income shall be included in the denominator of the taxpayer's sales factor to the extent of the taxpayer's interest in the partnership. The amount of the sales attributable to this Commonwealth shall also be included in the numerator of the taxpayer's sales factor. Intercompany sales between the partnership and the taxpayer shall be eliminated from the denominator and numerator of the taxpayer's sales factor as follows: sales by the taxpayer to the partnership to the extent of the interest in the partnership; sales by the partnership to the taxpayer not to exceed the taxpayer's interest in partnership sales.

(B) Notwithstanding an intercompany eliminations described in clause (A), sales made by the taxpayer or the partnership to nonpartners shall be included in the taxpayer's sales factor in an amount equal to the taxpayer's interest in the partnership.

(C) Application of clauses (A) and (B) is illustrated by the following examples:

*Example 1:* Corporation A's interest in Partnership P is 20%, and its distributive share of Partnership P's income is included in business income of Corporation A to be apportioned by formula. Corporation A's sales were \$20,000,000 for the year, \$5,000,000 of which were made to Partnership P. Partnership P made sales of \$10,000,000 during the same year, none of which were to Corporation A or the other partners.

The denominator of Corporation A's Sales Factor is \$21,000,000 determined as follows:

Sales by Corporation A		\$20,000,000
Add: Corporation A's interest (20%) in Partnership P's sales	2,000,000	
Less: Corporation A's interest (20%) in Corporation A's sales to Partnership P	1,000,000	1,000,000
	<u>1,000,000</u>	<u>1,000,000</u>
Denominator of Sales Factor		\$21,000,000

*Example 2:* The following facts are applicable to Examples 2(a) through (c) below. Corporation A's interest in Partnership P is 20%, and Corporation B's interest is 80%. The distributive share of partnership income is included in business income of Corporation A and Corporation B, respectively.

(a) The sales made by Corporation A, Corporation B, and Partnership P are as follows:

Corporation A		\$20,000,000
Corporation B		60,000,000
Partnership P:		
To Corporation A	\$2,000,000	
To Corporation B	8,000,000	\$10,000,000
	<u>8,000,000</u>	

The denominator of Corporation A's Sales Factor is \$20,000,000 determined as follows:

Sales by Corporation A		\$20,000,000
Add: Corporation A's interest (20%) in Partnership P's sales	\$ 2,000,000	
Less: Partnership P's Sales to Corporation A	2,000,000	-0-
	<u>2,000,000</u>	<u>-0-</u>
		\$20,000,000

The denominator of Corporation B's Sales Factor is \$60,000,000 determined as follows:

Sales by Corporation B		\$60,000,000
Add: Corporation B's interest (80%) in Partnership P's sales	\$ 8,000,000	



Less: Partnership P's sales to Corporation B	8,000,000	-0-
	<u>8,000,000</u>	<u>\$60,000,000</u>

(b) The sales made by Corporation A, Corporation B, and Partnership P are as follows:

Corporation A		\$20,000,000
Corporation B		\$60,000,000
Partnership P:		
To Corporation A	\$ 1,000,000	
To Corporation B	9,000,000	\$10,000,000
	<u>10,000,000</u>	

The denominator of Corporation A's Sales Factor is \$21,000,000 determined as follows:

Sales by Corporation A		\$20,000,000
Add: Corporation A's interest (20%) in Partnership P's sales	\$ 2,000,000	
Less: Partnership P's Sales to Corporation A	1,000,000	1,000,000
	<u>1,000,000</u>	<u>1,000,000</u>
Denominator of Corporation A's Sales Factor		<u>\$21,000,000</u>

The denominator of Corporation B's Sales Factor is \$60,000,000 determined as follows:

Sales by Corporation B		\$60,000,000
Add: Corporation B's interest (80%) in Partnership P's sales	\$ 8,000,000	
Less: Intercompany sales between Partnership P and Corporation B	8,000,000*	-0-
	<u>8,000,000*</u>	<u>-0-</u>
Denominator of Corporation B's Sales Factor		<u>\$60,000,000</u>

\*Not to exceed taxpayer's interest in Partnership P's sales.

(c) The sales made by Corporation A, Corporation B, and Partnership P are as follows:

Corporation A		\$20,000,000
Corporation B		80,000,000
Partnership P:		
To Corporation A	\$ 3,000,000	
To Corporation B	6,000,000	\$10,000,000
To Corporation X	1,000,000	

The denominator of Corporation A's Sales Factor is \$20,200,000 determined as follows:

Sales by Corporation A		\$20,000,000
Add: Corporation A's interest in Partnership P's sales to nonpartner X Corporation (20% × \$1,000,000)		200,000
Corporation A's interest in Partnership P's sales to Partners (20% × \$9,000,000)	\$ 1,800,000	
Less: Intercompany sales from Partnership P to Corporation A	\$ 1,800,000*	-0-
Denominator of Corporation A's Sales Factor		\$20,200,000

\*Not to exceed taxpayer's interest in Partnership P's sales.

The denominator of Corporation B's Sales Factor is \$82,000,000 determined as follows:

Sales by Corporation B		\$80,000,000
Add: Corporation B's interest in Partnership P's sales to nonpartner X Corporation (80% × \$1,000,000)		800,000

Corporation B's interest in Partnership P's sales to Partners (80% × \$9,000,000)	\$ 7,200,000	
Less: Intercompany Sales from Partnership P to Corporation B	\$ 6,000,000	1,200,000
Denominator of Corporation B's Sales Factor		<u>\$82,000,000</u>

(e) *Nonbusiness income.*

(1) The determination of whether a taxpayer's distributive share of partnership income is business or nonbusiness income shall be made in accordance with this subsection if the conditions of subsection (b) are met.

(i) The first step is to determine which portion of the taxpayer's income and its distributive share of the partnership items constitute "business income" and "nonbusiness income" under section 401(3)2.(a)(1)—(17) of the TRC (72 P. S. § 7401(3)2.(a)(1)—(17)) and this chapter. The various items of nonbusiness income are then directly allocated to specific states under section 401(3)2.(a)(4)—(8) of the TRC (72 P. S. § 7401(3)2.(a)(4)—(8)) and this chapter. The taxpayer's distributive share of the nonbusiness income shall be reported in the same manner as other nonbusiness income derived from other activities of the taxpayer. See § 153.24 (relating to business income and nonbusiness income).

(f) *Accounting period.*

(1) The corporate taxpayer and the partnership are required to maintain their accounting periods as prescribed under section 706 of the IRC (26 U.S.C.A. § 706).

(2) Where the partnership keeps its books on a fiscal or calendar year which is different from the tax year of the taxpayer, the taxpayer shall report its share of the partnership income and apportionment factors in its tax year in which or with which the partnership year ended.

(g) *Accounting method.*

(1) In determining the corporate partner's distributive share, the same method of accounting shall be used that the partnership uses in keeping its books. This is true even though the partnership method of accounting is not the same as that which the corporate partner used in preparing its corporate return. Thus, a cash basis partner would have to include items which are accrued but unpaid by an accrual basis partnership.

(h) *Filing requirements.*

(1) A corporation filing under this section shall file a copy of the partnerships' Federal Form 1065 and a detailed description of partnership activity. The description shall include a detailed explanation of all business and nonbusiness income.

(i) *Effective date.* This section will take effect for the tax years beginning January 1, 1982.

#### Authority

The provisions of this § 153.29 issued under section 408(a) of the Tax Reform Code of 1971 (72 P. S. § 7408(a)).

#### Source

The provisions of this § 153.29 adopted March 11, 1983, effective March 12, 1983, 13 Pa.B. 991.

### § 153.30. Safe harbor leases.

(a) *Definitions.* The following words and terms, when used in this section, have the following meanings, unless the context clearly indicates otherwise:

- (1) *Lessee*—The lessee under a safe harbor lease.
- (2) *Lessor*—The lessor under a safe harbor lease.
- (3) *Safe harbor lease*—An agreement which is characterized as a lease under section 168(f)(8) of the IRC (26 U.S.C.A. § 168(f)(8)) and the Treasury regulations thereunder.

(b) *Determination of taxable income.*

- (1) To the extent otherwise permitted:
  - (i) The Federal cost recovery and interest expense deductions and the Federal rental income of a lessor attributable to safe harbor leases will be reflected in the lessor's Pennsylvania taxable income.
  - (ii) The Federal deduction for rent paid and the Federal interest income of a lessee will be reflected in the lessee's Pennsylvania taxable income.
- (2) Income and deductions associated with safe harbor leases are considered part of a corporation's regular trade or business and consequently are included in computing the business income of the corporation.

(c) *Ownership of property.*

(1) Under section 168(f)(8) of the IRC and the Treasury regulations thereunder, a transaction may qualify as a safe harbor lease if it is treated by the parties as a lease for Federal tax purposes only. The regulations expressly provide that the lessee may be the owner of the property under state or local law. In terms of subjectability to taxation within this Commonwealth and apportionment, safe harbor leases will have different consequences depending upon whether title to the property covered by the lease has passed to the lessor. The determination of whether title to the property covered by the safe harbor lease passes to the lessor will be determined under general principles of Pennsylvania law.

(2) The parties to the safe harbor lease are required to demonstrate whether the lessor has required and retained title to the property covered by the safe harbor lease.

(d) *Subjectability of lessor to Pennsylvania corporate taxation.*

(1) If the sole contact of a corporation with this Commonwealth is the lease of property located in this Commonwealth under a safe harbor lease where title to the property does not pass to the corporation, the corporation will not be subject to Pennsylvania corporate taxation.

(2) If the lessor under a safe harbor lease actually takes title to the property located in this Commonwealth covered by the lease, the lessor will be treated as the owner of the property and, during the time that the title is retained by the lessor, the lessor will be subject to Pennsylvania corporate taxation.

(e) *Three factor apportionment formula.*

(1) If title to property covered by a safe harbor lease does not pass to the lessor, the lessee will be considered to be the owner of the property. The lessee of the property shall include the value of the property in the denominator of the property fraction, and the numerator of the fraction if the property is located in this Commonwealth. The lessor may not include the property in its property fraction. The lessee may not include a down payment or installment payment relating to the safe harbor lease in either the numerator or denominator of its sales fraction. The lessor may not include rental income attributable to the safe harbor lease in either the numerator or denominator of its sales fraction.

(2) When title to property covered by a safe harbor lease does pass to the lessor, the lessor shall report the property in the denominator of its property fraction, and in the numerator of the fraction if the property is located within this Commonwealth. The lessee shall include the value of the property in the denominator of its property fraction, and in the numerator if the property is located within this Commonwealth, at eight times its net rental value. The lessor shall include in the denominator of its sales fraction, and in the numerator if the property is located in this Commonwealth, rental income attributable to the property covered under the safe harbor lease during the time that the purchaser retains title. The lessee shall include in the denominator of its sales fraction, and in the numerator if the property is located within this Commonwealth, a down payment and installment payment attributable to the safe harbor lease.

(f) *Single taxable assets fraction.*

(1) If title to property covered by a safe harbor lease does not pass to the lessor, the lessee will be considered to be the owner of the property. The lessee shall include the value of the property in the denominator of its single taxable assets fraction, and the numerators of the fraction if the property is located within this Commonwealth. The lessor may not include the property in its single taxable assets fraction.

(2) When title to property covered by a safe harbor lease does pass to the lessor, the lessor shall include the property in the denominator of its single taxable assets fraction, and in the numerator of the fraction if the property is located within this Commonwealth. The lessee may not include the property in its single taxable assets fraction.

**Authority**

The provisions of this § 153.30 issued under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

**Source**

The provisions of this § 153.30 adopted January 16, 1987, effective January 17, 1987, 17 Pa.B. 273.

### EQUITABLE REMEDIES

§ 153.41. [Reserved].

§ 153.42. [Reserved].

**Source**

The provisions of this § 153.42 reserved February 6, 1976, effective December 12, 1975, 6 Pa.B. 230.

§ 153.43. **Sales factor.**

If the apportionment provisions do not fairly represent the extent of the taxpayer's business activity in this Commonwealth, section 401(3)2.(a)(18) of the TRC (72 P. S. § 7401(3)2.(a)(18)) may be utilized on a case-to-case basis to effectuate an equitable apportionment by any of the methods provided therein.

**Source**

The provisions of this § 153.43 amended through November 16, 1984, effective November 17, 1984, 14 Pa.B. 4163. Immediately preceding text appears at serial pages (81535) to (81536).

### REPORTS AND PAYMENT OF TAX

§ 153.51. [Reserved].

§ 153.52. [Reserved].

§ 153.53. [Reserved].

§ 153.54. **Changes made by Federal government.**

(a) *General.* If the amount of taxable income, as returned by a taxpayer to the Federal government, is finally changed or corrected by the Commissioner of the

Internal Revenue or by another agency or court of the United States, the taxpayer, within 30 days after the receipt of the final change or correction, shall make a report of change, under oath or affirmation, to the Department showing the finally changed or corrected taxable income, upon which tax is required to be paid to the United States. See section 406 of the TRC (72 P. S. § 7406). A change or correction of taxable income includes an increase or decrease in Federal taxable income before net operating loss deduction and special deductions.

(b) *What is required to be filed with the Department.* The following are required to be filed with the Department:

- (1) A Report of Change as prescribed by the Department.
- (2) Where a Federal audit has been conducted a copy of the summary of the Federal agent's report, commonly referred to as an "RAR."
- (3) The Department may require the taxpayer to submit additional information or proof as it deems necessary.

(c) *When a Report of Change is required to be filed.* A Report of Change is required to be filed with the Department within 30 days of receipt of the final change or correction in taxable income as returned to the Federal Government. A Report of Change is required to be filed whether the Federal taxable income has been increased or decreased. See section 406(a) of the TRC.

(d) *When a change or correction in Federal taxable income is final and received.* A change or correction will be final and received as follows:

- (1) A change or correction which increases the taxable income as returned to the Federal Government is final when a Federal Notice and Demand for Payment is issued to the taxpayer. Such a change or correction is received by the taxpayer on the date the taxpayer receives the Federal Notice and Demand for Payment.

*Example 1.* Taxpayer files a 2003 Report with the Department in conformity with its Federal Return as filed in 2003. In 2004 the Internal Revenue Service audits the taxpayer's Return which results in an increase of the taxpayer's Federal taxable income. Taxpayer does not contest this change. Thirty days after receipt of a Federal Notice and Demand for Payment, the taxpayer is required to file a Report of Change with the Department.

*Example 2.* Taxpayer files a 2003 Report with the Department in conformity with its Federal Return as filed in 2003. In 2004 the Internal Revenue Service audits the taxpayer's Return which results in an increase of taxpayer's Federal taxable income. Taxpayer contests this change and files a petition in the United States Tax Court. The United States Tax Court upholds the Internal Revenue Service's action. Taxpayer does not appeal the United States Tax Court's decision. Thirty days after receipt of a Federal Notice and Demand for Payment, the taxpayer is required to file a Report of Change with the Department.

*Example 3.* Taxpayer files a 2003 report with the Department in conformity with its Federal return as filed in 2003. In 2004 the Internal Revenue Service audits the taxpayer's return which results in an increase of the taxpayer's Federal

taxable income. Taxpayer contests this change and pursues all administrative and judicial remedies available without paying the contested amount of tax. The United States Supreme Court upholds the Internal Revenue Service's action. Thirty days after receipt of a Federal Notice and Demand for Payment, the taxpayer is required to file a Report of Change with the Department.

(2) A change or correction which decreases the taxable income as returned to the Federal Government is "final" when the taxpayer receives a refund or credit. The change or correction is received by the taxpayer on the date the taxpayer receives the refund or credit.

(3) A change or correction which does not increase or decrease the taxpayer's Federal tax is final when the taxpayer receives a notice from the IRS that its return will be adjusted in accordance with the examination report. The change or correction is "received" by the taxpayer on the date the taxpayer receives notice from the IRS that its return will be adjusted in accordance with the examination report.

*Example.* Taxpayer files a 2003 report with the Department in conformity with its Federal return as filed in 2003. In 2005 the Internal Revenue Service audits taxpayer's Federal return. The audit does not result in an increase in the Federal tax, but a change in the Commonwealth taxable income does occur due to the Federal action. Taxpayer is required to file a Report of Change within 30 days of notification by the Internal Revenue Service of its action.

(e) *More than one change or correction in Federal taxable income for a particular tax year.* A taxpayer is required to file a Report of Change for each change or correction by the Commissioner of Internal Revenue or by any other agency or court of the United States in the taxpayer's taxable income as reported to the Federal Government.

*Example.* As a result of a Federal audit of its 2003 Federal return, the taxpayer's Federal taxable income has been increased and the taxpayer has paid the Federal government additional tax. Since the taxpayer's Commonwealth taxable income also increased for 2003, taxpayer has filed a Report of Change with the Department. Thereafter, in a separate and subsequent court action the taxpayer contests the change in its Federal taxable income for 2003 and receives a refund from the Federal Government. Since its Commonwealth taxable income for 2003 has been decreased by this separate and subsequent action, the taxpayer is required to file a second Report of Change with the Department.

(f) *Penalties for failure to file a Report of Change.* Where there has been a final change or correction in the amount of taxable income, as returned by the taxpayer to the Federal government, which results in an increase in the taxable income, the taxpayer is required to file a Report of Change with the Department within 30 days after receipt of the final change or correction. If the taxpayer fails to file a Report of Change within the 30-day period, there shall be added to the



tax a penalty of \$5.00 for every day during which the taxpayer is in default, but the Department may abate a penalty in whole or in part. See section 406(a) of the TRC.

(g) *Report of Change required to report Federal change or correction.*

(1) *Corporate Net Income Tax settled prior to January 1, 2008.* When a Federal change or correction in taxable income as reported to the Federal government occurs within 1 year of the date of settlement and, therefore, a Commonwealth amended report could be timely filed as provided in § 153.64 (relating to amended report), the taxpayer nevertheless is required to file a Report of Change. Filing an amended report will not satisfy the requirement of filing a Report of Change.

*Example.* Taxpayer files a Federal Return on March 15, 2003. Based upon that return, the taxpayer files its Commonwealth Report on April 15, 2003. In August of 2003, the IRS discovers an error in the taxpayer's return. Taxpayer shall file a Report of Change even though the final change or correction was received within the period in which the taxpayer could file an amended report. An amended report will not satisfy the requirement of filing a Report of Change.

(2) *Corporate Net Income Tax not settled prior to January 1, 2008.* When a change or correction in taxable income as reported to the Federal government occurs, the taxpayer is required to file a Report of Change regardless of whether or not an amended report could have been timely filed as provided in § 151.14 (relating to amended report). This requirement applies to changes or corrections initiated by either the taxpayer or the Federal government. Filing an amended report will not satisfy the requirement of filing a Report of Change.

*Example.* Taxpayer files a Federal Return on March 15, 2007. Based upon that return, the taxpayer files its Commonwealth Report on April 15, 2007. In August of 2008, the IRS conducts an audit and notifies taxpayer that its Federal taxable income is different than the reported figure. Taxpayer shall file a Report of Change even though the final change or correction was received within the period in which the taxpayer could file an amended report. An amended report will not satisfy the requirement of a Report of Change.

(h) *Changes initiated by the taxpayer.*

(1) A Report of Change shall be filed, and additional tax due paid, within 30 days of the date the amended Federal return is filed, or would have been filed in the case of a corporation participating in the filing of a consolidated Federal return.

(2) The taxpayer shall provide a copy of the amended Federal Income Tax return if the Report of Change is filed due to a change in Federal taxable income based on the filing of an amended Federal Income Tax return. In addition, the Department may also require proof of acceptance of the amended Federal Income Tax return. Examples of proof of acceptance by the Federal government include the following:

(i) Copy of the IRS refund check.

- (ii) IRS statement of adjustment to your account.
- (iii) IRS account transcript.
- (iv) Other documentation at the discretion of the Department.

(3) Amended Federal Income Tax returns include any document allowed or authorized by the IRS for a taxpayer to adjust the taxpayer's Federal taxable income.

*Example 1.* Taxpayer files a Federal Return on March 15, 2007. Based upon that return, the taxpayer files its Commonwealth Report on April 15, 2007. In August of 2008, the taxpayer discovers taxable income was underreported and files an amended Federal Income Tax return. Taxpayer shall file a Report of Change even though the final change or correction was received within the period in which the taxpayer could file an amended report. An amended report will not satisfy the requirement of a Report of Change.

*Example 2.* Taxpayer files a Federal Return on March 15, 2007. Based upon that return, the taxpayer files its Commonwealth Report on April 15, 2007. In March 2009, when filing the Federal Income Tax return for 2008, the taxpayer files Federal Form 1139, Corporation Application for Tentative Refund, adjusting 2006 Federal taxable income for a capital loss carryback for 2008. Taxpayer shall file a Report of Change even though the final change or correction was received within the period in which the taxpayer could file an amended report. An amended report will not satisfy the requirement of a Report of Change.

#### Source

The provisions of this § 153.54 adopted December 30, 1977, effective December 31, 1977, 7 Pa.B. 3980; amended June 18, 2010, effective June 19, 2010, 40 Pa.B. 3356. Immediately preceding text appears at serial pages (249896) to (249899).

## SETTLEMENT AND RESETTLEMENT

### § 153.61. Settlement.

(a) *General rule.* Settlement of taxes due shall be made, so far as possible, so that notice thereof may be mailed to the taxpayer within 18 months after the tax report was required to be made. See section 407(a) of the TRC (72 P. S. § 7407(a)).

(b) *Extensions of time to file reports.* If a taxpayer requests an extension of time in which to file its Federal return, settlement will be made, so far as possible, so that notice thereof may reach the taxpayer within 18 months after the taxpayer files its Pennsylvania return. In the case of a taxpayer requesting a Pennsylvania extension which did not request a Federal extension, settlement will be made, so far as possible, so that notice may be mailed to the taxpayer within 18 months after the taxpayer files the return. See section 405 of the TRC (72 P. S. § 7405).

(c) *Delinquent reports.* In the case of a tax report which is filed after the original due date, or if an extension has been requested, after the extended due date, settlement will be made, so far as possible, so that notice may be mailed to the taxpayer within 18 months after the tax report was filed with the Department.

**Authority**

The provisions of this § 153.61 amended under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

**Source**

The provisions of this § 153.61 amended January 13, 1978, effective January 14, 1978, 8 Pa.B. 141; amended January 16, 1987, effective January 17, 1987, 17 Pa.B. 273. Immediately preceding text appears at serial pages (94421) to (94422).

**Cross References**

This section cited in 61 Pa. Code § 153.66 (relating to applicability).

**§ 153.62. Copy of the settlement will be sent to the taxpayer.**

(a) *General.* Promptly after the date of settlement, the Bureau is required to send a copy of the settlement of corporate taxes to the taxpayer. See section 407(c) of the TRC (72 P. S. § 7407(c)).

(b) *Where the tax settlement computations differ from the tax computations as submitted by the taxpayer.* Where the tax settlement computations differ from the tax computations as submitted by the taxpayer, the Bureau will send a copy of the tax settlement in the form of a photocopy of the settlement sheet, which is located on the back of the submitted report, as settled by the Bureau and audited and approved by the Department of the Auditor General.

(c) *Where the tax settlement computations show no change from the tax computations as submitted by the taxpayer.* Where the tax settlement computations show no change from the tax computations as submitted by the taxpayer, the Bureau will send a copy of the settlement.

**Authority**

The provisions of this § 153.62 issued under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

**Source**

The provisions of this § 153.62 adopted January 13, 1978, effective January 14, 1978, 8 Pa.B. 141; amended October 5, 1984, effective October 6, 1984, 14 Pa.B. 3624. Immediately preceding text appears at serial page (36133).

**Cross References**

This section cited in 61 Pa. Code § 153.66 (relating to applicability).

**§ 153.63. Resettlement by the Department.**

(a) *Resettlement of settlements.* If, within a period of 1 year after the date of a settlement, the Department is not satisfied with the settlement, the Department

may resettle the tax due based upon the facts contained in the report, or upon information within its possession. See section 407(b) of the TRC (72 P. S. § 7407(b)).

(b) *Appealed settlements.* In the case of a settlement of tax which has been appealed to the Board of Finance and Revenue, the Department is authorized to resettle under section 407(b) of the TRC if the Board of Finance and Revenue has not acted upon taxpayer's petition, or, if the Board of Finance and Revenue has acted upon taxpayer's petition, the Department will have authority to make a resettlement, if the resettlement is consistent with the action of the Board of Finance and Revenue on any issue raised before the Board.

(c) *Petitions for refund.* The filing of a Petition for Refund with the Board of Finance and Revenue does not affect the jurisdiction of the Department to make a resettlement of tax due. Action taken on a Petition for Refund by the Board of Finance and Revenue does not affect the jurisdiction of the Department to make a resettlement of tax due, if the resettlement is consistent with the action of the Board of Finance and Revenue on any issue raised before the Board.

#### Authority

The provisions of this § 153.63 issued under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

#### Source

The provisions of this § 153.63 adopted January 13, 1978, effective January 14, 1978, 8 Pa.B. 141; amended January 16, 1987, effective January 17, 1987, 17 Pa.B. 273. Immediately preceding text appears at serial pages (94422) and (36134).

#### Cross References

This section cited in 61 Pa. Code § 153.54 (relating to changes made by Federal government); and 61 Pa. Code § 153.66 (relating to applicability).

### § 153.64. Amended report.

(a) *General.* An amended report may be filed by a taxpayer within 1 year after settlement of the original report. An amended report may be filed for the purpose of bringing to the attention of the Department a correction to the original report the taxpayer requests the Department to consider. If an amended Federal return is filed or would have been filed with the Federal government, a corrected report shall be filed with the Department under § 153.65 (relating to corrected reports).

(b) *Amended report filed before settlement.* When an amended report is filed in the Department before settlement of the original report, settlement will be based upon consideration of the information contained in the amended report, subject to verification by the Department.

(c) *Amended report filed after settlement but within 90 days of settlement mailing date.* After settlement of the original report but within 90 days after the date upon which the copy of the original settlement notice was mailed to the tax-

payer, the taxpayer, if it seeks to have the settlement changed, shall file in the Department a Petition for Resettlement to which may be attached an amended report, subject to verification by the Department, in support of its petition. See section 1102 of the FC (72 P. S. § 1102).

(d) *Amended report filed after 90 days of settlement mailing date but within 1 year of settlement.* An amended report may be filed in the Department beyond 90 days after the date upon which the copy of the original settlement notice was mailed to the taxpayer but within 1 year after the date of settlement of the original report. The Department may resettle the original report based upon consideration of the information contained and verified in the amended report, subject to verification by the Department. See section 407(b) of the TRC (72 P. S. § 7407(b)).

(e) *Amended report received after 1 year after settlement.* After an amended report is received after 1 year of the date of settlement of the original report, the Department is without jurisdiction to make a resettlement, but the taxpayer may pursue its normal statutory remedy by timely filing a Petition for Refund. See section 503 of the FC (72 P. S. § 503).

#### Authority

The provisions of this § 153.64 amended under section 6 of The Fiscal Code (72 P. S. § 6).

#### Source

The provisions of this § 153.64 amended January 13, 1978, effective January 14, 1978, 8 Pa.B. 141; amended September 9, 1988, effective September 10, 1988, 18 Pa.B. 4100. Immediately preceding text appears at serial pages (115345) to (115346).

#### Cross References

This section cited in 61 Pa. Code § 153.66 (relating to applicability).

### § 153.65. Corrected report.

(a) *General.* A corrected report shall be filed by a taxpayer who files an amended return with the Federal government if the amended Federal return may result in a change in Pennsylvania taxable income or loss. In the case of a taxpayer participating in the filing of a consolidated Federal return, a corrected report shall be filed by the taxpayer if, had the taxpayer reported to the Federal government on a separate company basis, the taxpayer would have filed an amended return with the Federal government and the amended return may result in a change in Pennsylvania taxable income or loss. If the amended Federal return constitutes a claim for a credit or refund, it shall have been filed within the applicable Federal period of limitation for making the claim. Other amended Federal returns shall have been filed within the applicable Federal period of limitation on assessment. In the case of a taxpayer participating in the filing of a consolidated Federal return, the return which would have been filed shall be deemed timely if

the corrected Pennsylvania report is filed within 30 days of the time the amended Federal return would have been required to be filed.

(b) *Time for filing and payment.* A corrected report shall be filed, and additional tax due paid, within 30 days of the date the amended Federal return is filed, or would have been filed in the case of a corporation participating in the filing of a consolidated Federal return.

(c) *Effect of filing.* A corrected report amends the original report as of the original due date, and tax due shall be resettled, in so far as possible, so that notice thereof reaches the taxpayer within 18 months after the corrected report was made.

(d) *Limitations on resettlement.* If, as a result of the filing of a corrected report, there is a change in the amount of the taxable income of a corporation, the Department has the power and duty to resettle the tax. Changes to the tax due made as a result of the filing of the corrected report are limited to those which result directly from the filing of the amended Federal return.

(e) *Required documents.* The taxpayer shall file the following:

(1) A corrected report which reflects a change in Pennsylvania taxable income or loss.

(2) A copy of the Federal 1120X Return or other amended Federal return filed with the Federal government. In the case of a corporation participating in the filing of a consolidated Federal return, the amended Federal return that would have been filed had the corporation filed on a separate company basis.

(3) If no Federal 1120X return or other amended Federal return has been filed with the Federal government, a complete and detailed statement sworn to by an authorized officer of the taxpayer indicating why the amended return was not filed.

(4) A complete and detailed statement sworn to by an authorized officer of the taxpayer indicating why the correction was not included in the original Pennsylvania Corporate Net Income Tax report.

(f) *Proof of acceptance.* The Department may, on a case-by-case basis, require the taxpayer to submit evidence that the amended Federal return has been accepted by the Federal government or was prepared in accordance with the Internal Revenue Code.

(g) *Interest on underpayments and overpayments of tax.* An underpayment of tax resulting from the filing of a corrected report shall bear interest from the original due date of the tax until paid. In the case of an overpayment, the corrected report will be deemed a final return or report under section 806.1(a)(5) of the FC (72 P. S. § 806.1(a)(5)).

#### Authority

The provisions of this § 153.65 issued under section 6 of The Fiscal Code (72 P. S. § 6).

**Source**

The provisions of this § 153.65 adopted September 9, 1988, effective September 10, 1988, 18 Pa.B. 4100.

**Cross References**

This section cited in 61 Pa. Code § 153.64 (relating to amended report); and 61 Pa. Code § 153.66 (relating to applicability).

**§ 153.66. Applicability.**

Sections 153.61—153.65, regarding settlement and resettlement, apply to taxes settled prior to January 1, 2008.

**Authority**

The provisions of this § 153.66 issued under section 6 of The Fiscal Code (72 P. S. § 6).

**Source**

The provisions of this § 153.66 adopted June 18, 2010, effective June 19, 2010, 40 Pa.B. 3356.

**ENFORCEMENT****§ 153.71. Inquisitorial powers of the Department.**

- (a) [Reserved].
- (b) [Reserved].
- (c) *Duties of the taxpayer.* Taxpayers shall have the following duties:
  - (1) *General.* Every taxpayer shall maintain and keep for a period of 3 years after a report is filed under the TRC records of its business within this Commonwealth for the period covered by the report and other pertinent papers required by the Department. See section 409 of the TRC (72 P. S. § 7409).
  - (2) *What constitutes records and papers.* [Reserved].
  - (3) *Microfilm (including microfiche) reproduction.* A taxpayer may utilize microfilm (including microfiche) reproduction of general books of account and supporting records of detail which are records of its business within this Commonwealth and other pertinent papers as a method of maintaining and keeping the records and papers if the IRS approves of the taxpayer's system of microfilm (including microfiche) reproduction and the general books of account and supporting records of detail produced by the reproduction. A taxpayer utilizing this system of record retention will make available upon request by the Department a reader-printer for the reading, location and reproduction of records and papers being maintained on microfilm.

**Source**

The provisions of this § 153.71 adopted December 19, 1975, effective December 20, 1975, 5 Pa.B. 3276.

**ELECTIONS****§ 153.81. Elections under 26 U.S.C.A. § 338.**

- (a) *General.* Under section 338 of the IRC (26 U.S.C.A. § 338), a corporation which acquires at least 80% of the stock of another corporation—the target—within a 12 month period may elect, or, under certain circumstances, may be

treated as having elected to treat the stock purchase as a purchase of assets. Where the target corporation is not includable in a consolidated Federal return for a period that includes the acquisition date, the tax liability, if any, resulting from a deemed sale of assets by a target corporation shall be reported in the Federal return filed for the target corporation's taxable year that ends at the close of the acquisition date. If the target corporation is a member of an affiliated group for the taxable year that includes the acquisition date and the target corporation would be includable in a consolidated Federal return by the selling group for this period, the deemed sale of assets is treated as the target corporation's last transaction occurring at the close of the acquisition date in a separate taxable year. The tax liability resulting from the deemed sale shall be reported by the target corporation in a final, separate deemed sale Federal return. This section sets forth special rules which shall be followed by a target corporation subject to Pennsylvania corporate taxation.

(b) *Reports required.* Target corporations shall file Corporate Net Income and Capital Stock or Foreign Franchise Tax reports for periods for which a Federal return is required to be filed, including a Federal 1-day deemed sale return. An election made with the Federal government is binding for Commonwealth purposes, as is a failure to elect.

(c) *Due date for reports.* Reports are due 30 days after the return to the Federal government is due, or would be due in the case of a corporation participating in the filing of a consolidated Federal return.

(d) *Effect of election on tax liability.*

(1) *Corporate Net Income Tax.* Taxable income generated as a result of a section 338 election is subject to Pennsylvania Corporate Net Income Tax and treated as business income subject to apportionment, if the taxpayer was entitled to apportionment for the taxable year ending immediately prior to the acquisition date. The income consequences of a Section 338 election shall be reflected on a separate company basis and not as part of a combined or consolidated report.

(2) *Capital Stock or Foreign Franchise Tax.* In computing the capital stock value of a target corporation on a deemed sale report, actual net worth as of the close of that day shall be used. In computing average net income on a 1-day deemed sale report, the average net income for the period ending immediately prior to the acquisition date shall be used.

(e) *Apportionment.* Where the effects of a Section 338 election are shown on a 1-day deemed sale Federal return, the apportionment factors or the taxable assets fraction, as the case may be, for the period ending immediately prior to the acquisition date shall be used.

(f) *Bulk sales requirements.* If only shares of stock are transferred a deemed sale of assets does not constitute a sale or transfer within the meaning of section 1403 of the FC (72 P. S. § 1403). If there is also a sale or transfer of assets in addition to the stock transfer, a bulk sale or transfer will have occurred if 51% of



a stock of goods, wares or merchandise of any kind, fixtures, machinery, equipment, building or real estate is sold or transferred.

**Authority**

The provisions of this § 153.81 issued under section 408 of the Tax Reform Code of 1971 (72 P. S. § 7408).

**Source**

The provisions of this § 153.81 adopted January 16, 1987, effective January 17, 1987, 17 Pa.B. 273.

**Notes of Decisions**

*Treatment*

Taxpayer's gain from the financial liquidation of assets deemed to occur under a Federal tax election under 26 U.S.C.A. § 338(h)(10) is taxable as nonbusiness income. *Canteen Corp. v. Commonwealth*, 818 A.2d 594 (Pa. Cmwlth. 2003); affirmed 854 A.2d 440 (Pa. 2004).

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