1. Can you please provide an updated key contact sheet for PA DOR personnel?

**Answer**
Handout provided at meeting (Attachment A).

2. We were extremely pleased with the level of attendance at all locations of the PA Department of Revenue Fall Tax Seminars this year. We would like to request an additional seminar be held in the Gettysburg area in 2015. This addition would provide access to Pennsylvania tax information to practitioners in Adams and southern York counties who have not traditionally traveled to the Harrisburg area for the seminar. In addition, we believe that the seminar will be popular with practitioners in Maryland who practice across state borders.

**Answer**
The department would be amenable to adding a seminar to the Gettysburg area once additional information regarding potential seminar attendance numbers and facility location information is provided for further consideration.

3. As you are aware, there was much confusion and unrest among the practitioner community regarding PA Department of Revenue’s policy change as it pertained to unreimbursed employee expenses this year. In many cases, the deduction was not worth the administrative burden/cost to the taxpayer to respond and provide additional documentation to obtain the deduction.

a. Please address this issue, the background for the policy change and how the Department plans to handle these expenses in the future.

**Answer**
As part of the recently implemented Refund Fraud Project, the Department placed additional efforts on the review of all refund returns including those that included deductions for unreimbursed employee (UE) business expenses (Attachment B). Through new analytical measures that identify fraudulent and erroneous filings, the Department is making improvements in sending accurate refunds to only their rightful owners.

Department personnel, during the review of selected returns, either denied in whole or in part the expenses claimed or requested additional information to substantiate the type and the amount of the expenses being claimed. The larger effort is improving our return selection process so that tax examiners are looking at returns more likely to be fraudulently or erroneously claiming refunds and then manually or stopping those refunds. This is not a policy or procedure change, we’re simply improving our flagging capabilities, looking at more suspicious refunds and making adjustments accordingly.

In an effort to address the concerns raised from taxpayers and various professional organizations:

- The Bureau of Individual Taxes (BIT) will improve the notices that are issued to taxpayers with the goal of providing a better explanation of the exact adjustment that was made, as well as more details on how to respond to the notice.
• A review of the criteria used to select accounts for examination of UE expenses is being done to reduce the number of accounts suspended for occupations that should have allowable expenses.
• Additional education on allowable UE and areas that accountants should be cognizant of is being provided during the PIT portion of the Fall Tax Seminars.
• Review of the FAQ’s regarding UE is has been done to insure that additional details are added regarding disallowance of certain expenses and documentation that should be provided to substantiate those expenses.
• BIT is planning to only utilize seasoned tax examiners to review certain UE suspended returns this processing season instead of temporary staff which will lessen the amount of erroneous adjustments being made. Prior to the start of the upcoming processing season, additional UE focused training will be provided to those staff members who are designated to review these suspensions.

b. Does Pennsylvania have a Taxpayer Bill of Rights (similar to IRS Publication 1)?

Answer
Handout provided at the meeting is the Pennsylvania Taxpayers’ Bill of Rights.

c. Upon responding to notices with supporting documentation, in some cases it took more than 8 weeks to receive anything back from the Department. With all of the cuts etc., is this policy a good use of the Department’s limited resources based on the fact that many of the expenses were approved in prior years?

Answer
The Department did experience a backlog in reviewing correspondence this tax season as in previous years. However, steps were taken to expedite review of correspondence during the year and measures have been taken to ensure we do not have as large of a back log in the review of correspondence during the next tax season.

d. Do you have comparative annual statistics about how much revenue was generated this year vs. prior years as a result of the policy change?

Answer
As part of the new effort, the Department adjusted (either partially or wholly), 58,283 refunds totaling $11 million in in savings.

e. As an organization we like to think that we have established a good working relationship with the Department. Any communication/information that can be shared prior to such a drastic policy change benefits both the Department and the practitioner community and ultimately the taxpayer. We welcome this communication regarding issues such as this that we can in turn disseminate to our membership.

Answer
The Department understands your concerns and will communicate issues and changes so that there is appropriate time to disseminate to your membership.
f. Is it possible for the Department to provide a Pennsylvania vs. Federal comparison for UE expenses that could be made available on the website?

**Answer**
The Department has created additional FAQ’s (Attachment B) to address confusion over what are allowable UE expenses. While it is not a comparison of Pennsylvania (PA) vs. Federal, the FAQ’s do provide guidance to taxpayers on what is acceptable for PA. The Department will research the feasibility of adding comparison information to the web site.

4. Does the Department of Revenue have any new audit initiatives and/or policy changes that will go into effect this year that practitioners/taxpayers should be aware of? Once again, if there is any information that can be distributed to the practitioner community regarding such initiatives/changes please advise us. The IRS does communicate various audit initiatives to their stakeholder groups which assists collection and implementation.

**Answer**
Effective November, 2014, Pennsylvania joined the Multistate Tax Commission (MTC) joint income tax audit program for corporate net income and capital stock/foreign franchise taxes. In addition to many other functions, the MTC serves as an operating arm for 24 states which are currently participating in the Income Tax Audit program.

The MTC is an intergovernmental state tax agency working on behalf of states and taxpayers to administer tax laws that apply to multistate and multinational enterprises. The MTC was created in 1967 as a result of the Multistate Tax Compact, the Commission is charged by this law with:

- Facilitating the proper determination of State and local tax liability of multistate taxpayers, including the equitable apportionment of tax bases and settlement of apportionment disputes;
- Promoting uniformity or compatibility in significant components of tax systems;
- Facilitating taxpayer convenience and compliance in the filing of tax returns and in other phases of tax administration;
- Avoiding duplicative taxation.

Participating states pool their resources to select candidates for corporate tax audits. The Commission’s audit staff will perform the audits as if they were part of Pennsylvania’s own audit staff and forward their findings and recommendations to Pennsylvania for assessment at the completion of the audit. Participating states maintain control of the program through selection of the audit candidates, providing guidance on key issues, and independently deciding whether to act upon audit results.

An audit of a consolidated group will be completed on a separate company basis thereby broadening the Department’s ability to ensure compliance with the laws and regulation of the Commonwealth. A significant benefit of the joint audit program is that a single MTC audit takes the place of separate and duplicative audits by member states, thereby providing obvious economies of scale to the states. This program will also reveal inconsistent reporting to different states by multistate taxpayers. Taxpayers benefit from a MTC joint audit in that it relieves them of the burden of multiple ongoing audits by individual states.

The Pass Through Business Office will be starting a sales and use tax desk review program. Initially, the Office will focus on nonfilers for sales tax and potential underreporters for use tax. Eventually, the program will expand to sales tax underreporting.
5. If a divorce agreement/QUADRO allows for the spouse to receive ½ of taxpayer’s 401K and then the spouse withdraws some of the money, is her basis ½ of the taxpayer’s basis for Pennsylvania?

**Answer**
Income from a 401K is always the income of the account owner spouse even if a divorce agreement or QUADRO provides that the other spouse gets some or all of it. Any distribution from the 401K is a distribution to the 401K account owner spouse even if the money goes to the other spouse. The account owner spouse must report the income from any distribution. The account owner spouse gets to use cost recovery for any distribution.

6. Does PA have a back-up withholding requirement? If so, are we required to withhold back up withholding for a foreign resident or corporation, if so at what rate?

**Answer**
Pennsylvania has no provisions for backup withholding.

7. In August 2014, Notices of Assessment were sent to business entities that previously timely electronically filed the 2013 RCT-101 and were subject to Corporate Net Income tax. The liability indicated on the notices is exactly double the actual tax liability per return. Why is this systematic return processing error occurring?

**Answer**
The errors were primarily due to minor programming glitches and user error. Both have been addressed and corrections have been made to many accounts. If you experience this issue please contact the Bureau of Corporation Taxes Accounting Division at (717) 705-6225 or via email at: RA-RVNOTICEOFADJUSTM@pa.gov.

8. Why would PA Department of Revenue increase the PA wages to Medicare wages when the W-2 clearly shows what the amount of PA wages? This is also occurring with part-year residents (those who moved into PA from another state). Why is the Department not asking for wage reconciliation documentation before assessing extra tax for the part-year resident?

**Answer**
The department’s normal procedures for compensation verification is to use the information on the W-2 to reconcile the wages between federal and state wages using information provided on the W-2. When the information is not present on the W-2 the department’s normal procedures are to adjust the wages to the Medicare wages. Beginning with the 2012 tax year, our normal procedure was to adjust the wages without requesting the reconciliation document. For 2013 tax year, there were significantly more taxpayers (including nonresident taxpayers) where this adjustment occurred as a result of our work with Revenue Solutions Inc.

Although the Department did not send a letter requesting the information after receiving the returns, the department has provided notice that the W-2RW is needed if the Medicare wages are greater than PA wages for several years in the PA-40IN booklet and by covering the issue during discussions of the most common errors with individual returns during one or more Fall Tax Seminars.
In an effort to reduce the number of notices that may need to be sent for 2014 tax year, the department is making the W-2 RW Reconciliation Worksheet an optional part of its electronic filing specifications for 2014 electronically filed returns. It is recommended that preparers contact their software vendor to determine if that document will be supported in their software packages.

9. In a prior year a taxpayer qualified and received a PA property tax rebate. However, due to a recent IRS notice it was discovered that income from a Form 1099 was previously not included in the taxpayer’s taxable income. With the inclusion of the Form 1099 income, the taxpayer’s income for rebate purposes would now exceed the maximum $35,000 limit. Please advise as to the best way to handle this situation.

**Answer**

A letter of explanation should be submitted along with the supporting documents that reflect the additional income. A payment can be remitted along with this letter made payable to the PA Department of Revenue or if the claimant is unable to pay the balance in full, contact information should be provided so payment arrangements can be established. The letter should be mailed to:

PA Department of Revenue  
Property Tax/Rent Rebate Division  
Attention: Anita Bullock, Division Chief  
P.O. Box 280600  
Harrisburg, PA 17128-0600

10. Why is the Department of Revenue delaying refunds for clients that have had PA income tax withheld on IRA or pension distributions which were withheld in error? Practitioner reports that he has had five clients where refunds were delayed for a period of time exceeding 6 months. The practitioner received a letter from the Department of Revenue requesting copies of the 1099Rs and W-2s to verify the tax withheld. Once the requested information was submitted by the practitioner it took the Department 6 months or longer to process the refund.

**Answer**

The department requires alternative procedures and documentation whenever tax is withheld on income that is generally not taxable for PA personal income tax purposes such as retirement pay. These steps are taken to attempt to prevent fraud on the amount of tax withholding being claimed. In prior years, the department has discovered cases where the tax withheld claimed by a taxpayer was not paid to the department by the payer listed on the 1099-R. Therefore, the department requires an actual copy of the 1099-R provided to the taxpayer by the payer be included with the e-filed return via DEX-93 or attached as a pdf file. In addition, the department can request verification of the payment by the payer with the Bureau of Trust Fund Taxes. In some cases, these additional steps require more time.

If a return is received without the information, the department must make a request for that information. If the response to the request for the 1099-R is provided to the department via a letter received by U.S. Postal Service, there are multiple other factors that can further delay a refund of the taxes withheld. If a response to a notice is received via DEX-93, the department is able to provide a more timely review of the correspondence it receives.
11. Will the Department of Revenue continue to accept the federal 15% depletion expense against natural gas royalty income?

**Answer**
PA PIT law does not include a provision for the allowance of percentage depletion. Although the department does have a regulation (125.51) allowing percentage depletion, most taxpayers cannot meet all the specifications of the regulation. The department does allow cost depletion. However, the owner of the property has to be able to clearly show that the cost of the mineral rights for the property were included by separate allocation of the total purchase price of the property and that a study has been conducted to determine the amount of the reserves.

The department is focusing resources on accounts where expenses against royalty income for the 15% percentage depletion deduction. In addition, the department has noted in its examinations of the depletion expense issue that many taxpayers are also including non-deductible surface rights expenses such as interest, real estate taxes, cleaning and maintenance and travel.

12. Why does the system reject corporation extensions filed under Etides when entered on the 15th of the month?

**Answer**
E-Tides does not reject extensions on the 15th. If there are any instances where the taxpayer is unable to make an extension payment on the 15th of the month, it is most likely because of their fiscal year history in the ITS. We have over 500 extension requests in e-Tides with the date filed occurring on the 15th of a month for 2014 alone. I would suggest if a taxpayer is not able to make an extension request on the 15th of the month that they call into the Bureau of Corporation taxes and have their fiscal year history reviewed and corrected/changed as needed.

13. If you own a vacation home (original cost of $300k) and sold it for $500k, can the basis of this property be increased by mortgage interest and property taxes paid?

**Answer**
Personal income tax does not allow for adjustments to basis for mortgage interest and property taxes paid.

14. Practitioner each year files partnership returns which happen to have investments in many other partnerships; some of the partnerships issue PA RK-1s and some do not. For the last 3 years, the practitioner/taxpayer received a PA Department of Revenue *Notice of Adjustment*, but the notice offered no explanation on the adjustment that was made by the Department.

Practitioner is referred to the ‘pass through unit’ when contacting the Department of Revenue where he provides various documentation, letters, schedules in order to obtain a spreadsheet of the K-1s. Upon reviewing the information on the spreadsheet, the practitioner discovers that the changes are not from the K-1s where there was no PA RK-1, but rather, the Department of Revenue used the Federal K-1 in lieu of the filed PA RK-1, because they did not believe the PA RK-1 as filed, was accurate.
Practitioner questioned the Department of Revenue employee regarding how they can simply change figures without an audit or even making any further inquiry back to the practitioner or taxpayer and was told that “they don’t have the resources to perform those procedures”. In every case, the filed PA RK-1 had lower figures because of the Keystone Opportunity Zone, which was properly disclosed with the filed returns. Eventually the state reversed its position on the adjustment.

a. Is it really the policy of the Department of Revenue for the pass-through unit to change figures on a filed PA RK-1 without audit or question, simply because they believe it is incorrect because it doesn’t match the federal form?

**Answer**
No, this is not the policy of the Department nor of PTBO. Act 52 of 2013 states that the individual owner of a pass through entity must report income on their PA-40 consistent with the RK-1 or NRK-1.

b. Is there a way that the notices can be improved to provide meaningful information about the specific adjustments that are being made by the Department?

**Answer**
When PTBO adjusts a PA20S/PA-65, a letter is sent to the entity notifying it of the change. This letter is sent prior or at the same time the owner is assessed.

c. Is there some way to communicate with the proper level at the Department of Revenue rather than try to work with a phone operator who struggles at best to handle these complicated matters?

**Answer**
If the caller calls the TS&IC general phone line (717-787-8201) and our agent sees that case was worked by the PTBO, there standard operating procedure is to explain to the caller the situation and transfer the caller to the PTBO. If the case isn’t a PTBO item and the adjustment was made by BIT, TS&IC agents will do their best to quickly review any notes or documents with the account and do their best to assist the caller. Please understand that the phone agents are not the one who made the adjustments to the account; they are only customer service representatives that are here to help our customers.

In these situations if the preparer has reviewed the notice/adjustment and determined what has happened. I would encourage them to respond to the notice with a written explanation of the situation and copies of any documents that supports their assertions.

When an analyst in PTBO reviews an entity or individual return, the correspondence they send should have their name and phone number on it. In addition, when the phone unit in PTBO receives a call regarding an analyst case, the call is transferred to the analyst. If the above described scenario occurs, please call Suzanne Leighton at 717-346-0018.

15. On taxpayers who file a joint return, what is the maximum IRC 179 depreciation allowed?

**Answer**
The maximum Section 179 deduction for PA PIT purposes is $25,000 on a joint return. See Informational Notice 2012-05 – IRC Section 179 Expense Deductions for more information regarding the limitations and how to apply them to PA personal income tax.
16. If a taxpayer sells a business on a 5 year installment sale for a gain, and the buyer defaults on year 4, how should the taxpayer report the default in year 4 when PA required the full gain to be recognized during the year sold?

**Answer**

PA personal income tax law does not include a claim of right doctrine provision similar to the IRS’s provision that permits a loss to be reported in the year of the default. If the statute of limitations is closed on the tax year in which the sale occurred, the taxpayer is precluded from filing an amended return to adjust the sales price. However, if the sale agreement included provisions that a default on the agreement caused the property to revert back to the taxpayer, the taxpayer would be able to adjust their basis in the property for the gain less the default amount plus the tax paid on the gain.

In addition, if the taxpayer had used the cost recovery method to report the gain on the sale of the intangible property which is permitted if the purchase price paid to the seller is paid over more than one tax year, the taxpayer would not have the default issue and subsequent adjustment of sales price as a concern. However, in order to report the sale of property using the cost recovery method, the sales agreement and corresponding note would have to contain clauses that the proceeds for the sale and corresponding note are not assignable (i.e., can’t be used as collateral).

17. If an extension is filed by a tax preparer for a client, but the client subsequently has another preparer complete the return and is unable to obtain a copy of the filed extension, can PA determine if a valid extension existed upon e-filing the corporate return?

**Answer**

In cases where a client taxpayer changes tax practitioner(s) and the former possesses documentation that subsequently needs to be filed with the Department such as copy of the Federal Form 7004, 4868, Application for Automatic Extension of Time. However, due to unfortunate situations such document(s) are not made available to the taxpayer or upon request of the new successor tax practitioner, a “Statement/Affidavit” explaining such circumstances shall be included with the filing of the next ensuing tax report filing affected by the absent document(s).

This statement should be attached in lieu of the normal required FF7004 or 4868 in the proper sequence for paper submitted filings or be made an attachment in “pfd” format as accommodated for electronic filing, or MEF Fed/State e-filing.

In situations as described above, special attention should be paid to insure that the “Extension” Block is properly marked when filing the PA Corporate Annual Tax report(s) ie RCT-101. Failure to properly mark/code the tax reporting instrument, paper or electronic transmission will result in the imposition of “Late Filing Penalties” upon submission of the subject report(s).

18. How are licensing authorities (such as the PLCB) made aware when only a federal extension is granted?

**Answer**

The Department’s policy has been to not look for the 2013 corporation tax returns due to anticipated backlogs in their processing. The only way the Department would look for a current year return at this point is if it involved a special credit such as KOZ, KIZ, NIZ, R & D, REAP and Film Credits.
19. What are the new late filing penalties for business entities and who are affected by them?

**Answer**

For tax years beginning on January 1, 2014 or after, Act 52 of 2013, imposed a $500 penalty plus an additional 1% for every dollar of tax determined to be due in excess of $25,000 for the failure to file a corporate tax return.

20. If a Single Member LLC converts to an S Corporation, does the 5 year earnings history carryover?

**Answer**

61Pa. Code § 155.26 (f) reads as follows (emphasis added):

Average net income does not include net income or loss of the corporation for a period of time prior to incorporation, such as net income or loss of a partnership prior to incorporation. Net income or loss of a predecessor corporation may not be attributed to a successor corporation. In the case of a mere change in identity, form or place of organization of one corporation, net income or loss prior to the change shall be utilized in determining average net income. Net income or loss may not be adjusted in the event of a change in corporate structure, but to the extent that a change occurs as a result of a tax evasion motive, net income or loss may be adjusted to negate the effects of the change in corporate structure. The following examples demonstrate the application of this subsection with respect to mergers, consolidations and reincorporations. Where there is evidence of a tax evasion motive, average net income will be determined based on the substance of the transaction.

This is a change in form so the history of earnings will continue.

21. If ABC Inc was a PA S Corporation that owns an interest in a PA LLC taxed as a partnership, and subsequently the owner moved to another state, would ABC Inc become a foreign corporation exempt from CS/FF because the only PA activity is in owning part of a PA LLC?

**Answer**

Unless ABC, Inc. reincorporates in a different state, it is still a domestic corporation.

22. If a parent company and its subsidiary file separate PA corporation returns, and the parent company dissolves and passes its assets to its subsidiary, can the subsidiary continue to exist or must a new company be created?

**Answer**

The subsidiary is a separate company from the parent. As long as the subsidiary continues to operate under that corporate charter, it is no necessary to form a new corporation.

23. Does Pennsylvania recognize a *Foreign Earned Income Exclusion* (Similar to IRS Form 2555) for military personnel who live abroad for 330 days or more in a calendar year?

**Answer**

No. The only exemption PA has is that “compensation” does not include income derived from the US Government for active duty outside the Commonwealth as a member of the armed forces.
24. If a Pennsylvania resident owns a business incorporated and operating in Maryland, must a PA corporate return be filed?

**Answer**
As long as there is absolutely no business conducted in PA the corporation is not required to file a PA Corporate Tax Report.

25. When PA Department of Revenue leaves a message on an answering machine of a preparer, why is only a return phone number left without identifying taxpayer name, EIN/SSN, and naming individual leaving message or identification number so that a preparer can efficiently resolve issue?

**Answer**
The security of taxpayer information is always a key concern of the Department. Therefore leaving specific taxpayer information on an unknown voice mail is not something the Department will normally do. Since the scenario laid out in this question seems to be in reference to one of our automated (robo) calls. They call back to the number we left, one of our helpful agents can help them out. Also, we don’t leave the name of an individual calling, because we don’t have case ownership and the person leaving the message is most likely NOT going to be the one who answers if they do as requested and call us back.

In another scenario if a caller leaves a message on our TSIC voice mail. When our friendly and helpful Agents call back and are put into a voice mail, they will leave a message that identifies them, lets the person know we are returning their call. Similarly, if we are calling a preparer back; they will leave a message that identifies themselves and let the preparer know that they are calling back concerning X taxpayer.

26. Has there been an increase in the use of the tax practitioners email hotline from the prior year?

**Answer**
No, actually the use of the Tax Practitioner email has decreased about 34% when compared to the same time last year. 2013 – 202 emails for the year, 192 at this time, vs 127 so far in 2014.

27. Follow up from 2013. We inquired about the possibility of confirmation receipts of information that is requested by and received by the Department as well as confirmation that an issue was resolved. It was indicated on the Department’s responses that while this was not in the initial plans, that this would be considered as a suggestion. Please advise of the status.

**Answer**
Though it is acknowledged that this was taken as practical modernization suggestion, the Department is still only partially through developing the required functionality as documented in the original project plan. It is not clear when this functionality will be achieved. For PIT and PTRR individuals and prepares can use our online or automated telephone systems to check on the status of a return.
28. Follow up from 2013. Once again, we are very interested in working with the Department to identify an appropriate threshold for a standardized installment payment agreement. It was indicated on the Department’s response that “several technical issues would need to be discussed and resolved prior to the deployment of a self-service deferred payment plan (DPP). Much of it will hinge on how sales, employer, and personal income taxes are integrated into the ITS.” Can you provide an update on this issue?

**Answer**
The department remains committed to expanding self-service options for taxpayers. This includes the ability to create a DPP via the department’s website. The department has not finalized the exact parameters for a self-service DPP. However, in general the department would follow what other state revenue departments have instituted as parameters. For example, a taxpayer that owes less than $5,000 and is able to make a 20% down payment and then have six installment payments via either an automatic withdrawal from a bank account or a reoccurring credit card charge would most likely be able to set up this DPP online. Assuming timely payments are made, no follow-up collection action would be required by the department with the taxpayer regarding the delinquent account. Again, no final decisions have been made regarding the parameters.

Resource limitations at this time do not allow the department to provide an accurate estimate as to when a self-service DPP would be functional. The department is finalizing plans for the next self-service option for taxpayers from a compliance perspective, which will be online lien certificate requests. The department receives almost 20,000 lien certificate requests per year and automating this process will make the department more efficient. It is anticipated that the infrastructure used to build an online clearance request system will be available for eventual use in administration self-service DPPs.

The department developed several Q&As on deferred payment plans in late April of 2014. However, they have not yet been posted to the department’s website. (Attachment C) is a copy of the latest version of the Q&A.

29. Follow up from 2013. This question was regarding e-filed PA 41 and the fact that there were only three software vendors willing to develop a state only software product. It was indicated that once the Department becomes part of the MeF platform fed-state fiduciary e-filing program beginning with the filing of 2014 fiduciary tax returns more software vendors may offer the PA-41 e-filing product. Do you have an update on this?

**Answer**
The Department is currently in the process of testing electronic filing of the PA41 through the Fed/State e-file platform and plan to be in production in January of 2015. The Department has provided software vendors with our specifications and notified them that we are ready for testing.

**Additional question:**
30. Under an employer payment plan, an employer reimburses or pays health insurance premiums (for an employee’s substantiated premiums) directly to the insurance company for non-employer sponsored health insurance. IRC Section 106 Rev ruling 61-146 excludes the payments from the employee’s gross income. The Affordable Care Act states this a group plan and does not meet the market reform and has to be included in gross income now. Are these payments by employers for various employees considered taxable PA compensation?
**Answer**

The payment is taxable as compensation for PA PIT purposes as it considered to be made pursuant to a cash or deferred arrangement under which an employee may unilaterally elect to have the employer make payments to such third party or fund for the benefit of the employee or to the employee directly in cash and it is not part of an IRC Section 125 plan.