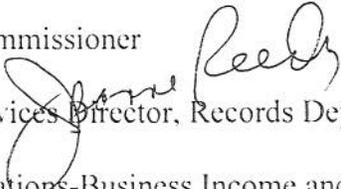


Memorandum

City of Philadelphia

Date: 12/17/15

To: Clarena I.W. Tolson, Revenue Commissioner

From:  Jeanne Reedy, Administrative Services Director, Records Dept.

Subject: Advertisement of Proposed Regulations-Business Income and Receipts
Tax-New Section 510-Distressed Business Tax Credit

The above Regulations promulgated by the Department of Revenue were received in the Department of Records on 12/16/15 for filing and advertising.

If there are no requests for hearings these Regulations will become effective 1/15/16.

Cc: Joseph F. Procopio Jr., CPA Manager – Technical Staff

Article V of the Business Income and Receipts Tax Regulations is being amended to add a new Section 510 entitled *Distressed Business Tax Credit*. Section 501 is being added as a result of City Council Bill No. 140209 (enacted on January 15, 2015) that provides a Distressed Business Tax Credit for eligible taxpayers for Tax Year 2015 and thereafter.

CITY OF PHILADELPHIA
BUSINESS INCOME AND RECEIPTS TAX REGULATIONS

ARTICLE V

CREDITS

Section 510. Distressed Business Tax Credit.

(a) Definitions – For purposes of this section, the following terms are defined as follows:

1. Distressed Business. A business that meets the eligibility criteria set forth in this section. The Distressed Business location must be within the physical limits of the City of Philadelphia.
2. Lost Net Income and Sales/Receipts. The reduction between the net income and sales/receipts of a distressed business at the location where and in the tax year in which the business obstruction occurred, and the average net income and sales/receipts of the distressed business in the two preceding tax years.
3. Public Works Project. A publicly-funded construction project undertaken by the United States, the Commonwealth of Pennsylvania, the City, or other governmental or quasi-governmental agency, for the benefit or use of the general public. For purposes of this definition, "other governmental or quasi-governmental agency" shall include the Delaware River Port Authority and the Southeastern Pennsylvania Transportation Authority. Public Works shall not include privately-owned utilities.

(b) Eligibility – The credit as provided by this section shall only apply to businesses that meet all of the following criteria:

1. Proximity. The business must be within 100 feet of the site of a public works project.
2. Business obstruction. For at least thirty (30) days, the public works project must substantially obstruct customer access to the place of business, or substantially obscure the place of business such that the existence of the place of business or the fact that the business is open may not be ascertained from the street.
3. Lost net income and sales/receipts. A business must suffer loss of net income in an amount that is at least 10% of the business's total net income and loss of sales/receipts in the amount that is at least 10% of the business's total sales/receipts in the tax year in which the business obstruction occurred.

(c) Application – A taxpayer wishing to apply for the credit under this section must complete an application on a form as provided by the Department and must include documentation that the business meets all eligibility criteria for this credit. Such documentation includes photographs depicting the business obstruction, evidence of the proximity of the Public Works Project to the Distressed Business Location, Lost net income and sales/receipts, the time duration of the business obstruction and such other proof as the Department may require. The application must be received on or before the due date of the Business and Income Tax return for the Tax Year in which the obstruction occurred.

(d) Tax Credit - Starting in Tax Year 2015, for any tax year in which a distressed business experiences a business obstruction caused by a Public Works Project, such business shall be eligible for a credit against its Business Income and Receipts Tax liability, in the amount of 20% of the business's Lost sales/receipts amount, up to \$20,000 but no more than the after tax loss in net income. Unused Distressed Business Tax Credits may not be carried forward and the credit is non-refundable.

(e) Calculation of Net Income attributable to the Distressed Business Location – The net income attributable to the Distressed Business location is the business entity's current year BIRT net income after the allocation of nonbusiness income (pursuant to Section 406) and apportionment (pursuant to Section 408), but before the Statutory Net income deduction (pursuant to Section 403) and any available loss carry forwards (pursuant to Section 411), multiplied by the ratio of sales/receipts attributable to the Distressed Business location to sales/receipts attributable to all Philadelphia locations.

Example 1

A corporation (with a total of 20 retail stores in 5 states) is seeking the Distressed Business Tax Credit attributable to one (1) of their three (3) Philadelphia locations. The corporation has an overall Federal Net Income (before the dividends received deduction and net operating loss) of \$100,000. The corporation in apportioning net income to Philadelphia for purposes of calculating the BIRT Net Income tax base (using Single Sales/Receipts Factor Apportionment) has calculated a Philadelphia Apportionment percentage of fifteen percent (15%). There is no nonbusiness income subject to allocation. Therefore the current year net income reported on line 9 of Schedule B of the 2015 BIRT is \$15,000 (i.e. \$100,000 * 15%). The calendar year 2015 sales/receipts for the three (3) Philadelphia retail stores is as follows:

<u>Store 1 (Distressed Business location)</u>	<u>\$ 15,000</u>
<u>Store 2</u>	<u>\$ 60,000</u>
<u>Store 3</u>	<u>\$ 75,000</u>
<u>Total Sales</u>	<u>\$150,000</u>

The net income attributed to the Distressed Business location is the BIRT current year net income of \$15,000 multiplied by the ratio of the sales of the Distressed Business location to sales of all Philadelphia locations (i.e. \$15,000/\$150,000 = 10%). Therefore, the net income attributed to the Distressed Business location is \$1,500 (i.e. \$15,000 *10%). This methodology (applied to the 2015 BIRT) will also be applied to the calculation of the net income attributed to the Distressed Business location for the 2013 and 2014 tax years and be used to determine the average net income for the Distressed Business location.

- (f) Calculation of Lost Sales/Receipts– In order to determine the Lost Sales/Receipts it will be necessary to determine the sales /receipts attributable to the Distressed Business location for the Tax Year in which the obstruction occurred and for the immediate two (2) prior Tax Years. The average sales /receipts for the Distressed Business Location for the immediate two (2) prior Tax Years will be compared to the sales /receipts in the Tax Year of the obstruction to determine the Lost Sales for the Distressed Business location and in turn the Lost Sales Percentage. The business must suffer in the obstruction Tax Year at the Distressed Business location a loss of sales/receipts that is at least ten percent ($\geq 10\%$) of the average Sales /Receipts for the location for the immediate two (2) prior Tax Years.

Example 2

Continuing with Example 1 above, Store 1 (the Distressed Business location) had \$15,000 in sales for Tax Year 2015- the year of the obstruction. For Tax Years 2013 and 2014, Store 1 had sales of \$85,000 and \$90,000 respectively. The average sales for Tax Years 2013 and 2014 is \$87,500 (i.e. $\$85,000 + \$90,000 = \$175,000/2 = \$87,500$).

The Lost Sales/Receipts for Tax Year for the Distressed Business location is \$72,500 (i.e. \$87,500 - \$15,000). The Lost Sales/Receipts percentage is 82% (i.e. \$72,500/\$87,500 = 82%). Since this loss percentage is >= to 10%, the corporation can continue to calculate the tax credit.

(g) Calculation of Lost Net Income - In order to determine the Lost Net Income it will be necessary to determine the net income attributed to the Distressed Business location as calculated pursuant to subsection (e) of this section for the Distressed Business location for the Tax Year in which the obstruction occurred and the immediate two (2) prior Tax Years. The average net income attributed to the Distressed Business Location for the immediate two (2) prior Tax Years will be compared to the net income in the Tax Year of the obstruction to determine the Lost Net Income and in turn the Lost Net Income Percentage. The business must suffer in the obstruction Tax Year a loss of Net Income at the Distressed Business location that is at least ten percent (>=10%) of the average Net Income for the location for the immediate two (2) prior Tax Years.

Example 3

Continuing with the same facts as Examples 1 and 2 above, but adding the additional data for Tax Years 2013 and 2014 for Philadelphia Stores 2 and 3

	<u>2013</u>	<u>2014</u>	<u>2015</u>
<u>Current Year Net Income - All Philadelphia Locations</u>	<u>\$40,000</u>	<u>\$50,000</u>	<u>\$15,000</u>
<u>Store 1 Sales/Receipts (Distressed Business location)</u>	<u>\$95,000</u>	<u>\$80,000</u>	<u>\$ 15,000</u>
<u>Store 2 Sales/Receipts</u>	<u>\$70,000</u>	<u>\$65,000</u>	<u>\$ 60,000</u>
<u>Store 3 Sales/Receipts</u>	<u>\$85,000</u>	<u>\$90,000</u>	<u>\$ 75,000</u>
<u>Total Sales/Receipts</u>	<u>\$250,000</u>	<u>\$235,000</u>	<u>\$150,000</u>
<u>Net Income for Distressed Business location</u>	<u>\$15,200</u>	<u>\$17,021</u>	<u>\$1,500</u>

In accordance with the methodology of subsection (e), the Net Income for the Distressed Business location is calculated by multiplying the Current Year BIRT Net Income by the ratio of the sales at the Distressed Business location to all Philadelphia sales. Therefore, the Net Income for the Distressed Business location for Tax Years 2013 and 2014 is calculated as follows:

Tax Year 2013 \$40,000 * \$95,000/\$250,000 = \$15,200

Tax Year 2014 \$50,000 * \$80,000/\$235,000 = \$17,021.

Average of 2013/2014 = \$15,200 + \$17,021 = \$32,221/2 = \$16,110

Tax Year 2015 \$15,000 * \$15,000/\$150,000 = \$1,500

Lost Net Income = \$16,110 - \$1,500 = \$14,610

Lost Net Income % = \$14,610/\$16,110 = 90%

Since this loss percentage is >= to 10%, the corporation can continue to calculate the tax credit.

- (h) Calculation of the Effective Income Tax Rate – The effective income tax rate is the average rate at which the business entity is taxed on its pre-tax net income. The rate is calculated by dividing the total of all net income taxes paid (Federal, state and local) by the total Federal pre-tax net income of the entity. The net income base of the Business Income and Receipts Tax is to be included in the calculation.

Example 4 - Continuing from Example 3

As noted in Example 1, the corporation's overall pre-tax Federal net income is \$100,000. The corporation has paid \$40,000 in total Federal, state, and local net income taxes in the five (5) states in which it is doing business. The corporation has an overall effective net income tax rate of 40%. This tax rate is determined by dividing the total Federal, state and local income tax paid for the tax year by the overall corporate pre-tax net income (i.e. \$40,000/\$100,000). This effective net income tax rate can then be used to calculate the Lost Net Income (net of taxes). The Lost Net Income (net of taxes) is \$14,610 * 60% = \$8,766.

- (i) Calculation of the Distressed Business Tax Credit – The credit is 20% of the business's Lost sales/receipts amount, up to \$20,000 but no more than the after tax loss in net income.

Example 5 – continuing with the same facts as Examples 1 through 4

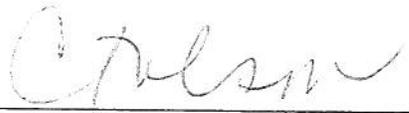
Lost Sales/Receipts \$72,500 * 20% = \$14,500 (not to exceed \$20,000)

Lost Net Income (net of tax) = \$8,766

The credit in our fact pattern is \$8,766 since 20% of the Lost Sales/Receipts cannot (i.e. \$14,500) cannot exceed the Lost Net Income (net of tax).

- (j) Tax Credit Cap – In the event that the aggregate amount of the Distressed Business Tax Credits to which businesses are entitled to in any tax year would exceed \$1,000,000, the amount of tax credit awarded to any single Distressed Business shall instead be computed as follows: (1) obtaining a reduction factor by dividing \$1,000,000 by the aggregate amount of all Distressed Business Tax Credits provisionally approved in that tax year; and (2) multiplying the amount of the tax credit to which a Distressed Business would be entitled by the reduction factor.
- (k) Unused Distressed Business Tax Credits may not be carried forward.
- (l) Tax Compliance – In order for a Distressed Business to receive the credit as provided by this section, the business must be in compliance with all applicable City and School District of Philadelphia taxes.

_____ Underline and bold denotes new matter


_____ Date: 12/9/15

Commissioner Clarena I.W. Tolson, Chief Revenue Collections Officer