

LOCAL TAX DEVELOPMENTS

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"All Power Is Inherent in the People," BUT

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In a recent case most interesting for its discussion of political powers "inherent in the people," the Commonwealth Court has upheld an *en banc* Lebanon County Court of Common Pleas decision invalidating the tax referendum requirement in the City of Lebanon's Home Rule Charter. The City had filed an action to invalidate the Charter provisions requiring a public referendum on any real estate tax increase of more than two mills. The Commonwealth Court agreed with the court below that the provision violated 53 Pa. C.S. § 2962(b) which "states that in home rule municipalities, the 'governing body shall not be subject to any limitation on the rates of taxation imposed upon residents.'"

The court rejected a taxpayer argument that the decision below violated Article I, Section 2 of the Pennsylvania Constitution, which provides:

Political Powers Section 2

All power is inherent in the people, and all free governments are founded on their authority and instituted for their peace, safety and happiness. For the advancement of these ends they have at all times an inalienable and indefeasible right to alter, reform or abolish their government in such manner as they may think proper.

The court noted that this provision:

has never been applied to Home Rule Charters, or municipal government generally. Article I, Section 2 has been applied only in the context of statewide governmental questions, such as the procedure for amending the Pennsylvania Constitution. See, e.g., *Com. v. Tharp*, 562 Pa. 231, 754 A.2d 1251 (2000). Even more fundamentally, a constitutional provision granting rights to "the people" does not eviscerate the laws setting forth the procedures by which the citizens may exercise those rights. The people act through the laws passed by their representatives in the General Assembly as well as through local enactments, and under our existing structure of government, a local municipality simply may not override affirmative State law.

In re: City of Lebanon Home Rule Charter, Dkt. No. 364 C.D. 2010, 9/1/2010.

Following are notes of other PA local tax developments.

Distinction Between Earned & Unearned Income Constitutional

The Earned Income Tax law's classification of earned income as taxable and unearned income as not taxable does not violate the Uniformity Clause of the Pennsylvania Constitution. This distinction is based upon a reasonable classification of those taxpayers engaged in performing services, and those taxpayers merely receiving income from passive activities, such as the ownership of property, and such a classification does not violate the Uniformity Clause. *Boguslavsky v. North Pocono School District*, No. 1139 C.D. 2010 (December 16, 2010).

Other PA Tax Notes

2011 Interest Rate. For 2011, the interest rate for underpayments of PA taxes is 3%. The same rate will be paid on Personal Income Tax refunds. Refunds of other taxes will accrue interest at 1%. *Pa. Bulletin Vol. 40, December 25, 2010.*

2011 PURTA Surcharge Rate. The Public Utility Realty Tax surcharge rate for 2011 is 1.6 mills. *Pa. Bulletin Vol. 40, p. 2419.*

2011 Fuel Tax Rates. For 2011 the Pennsylvania tax rate for aviation gasoline is increased to 5.5¢ per gallon; jet fuel is increased to 1.7¢ per gallon. The 2011 rate for the Oil Company Franchise Tax remains at 19.2¢ per gallon on "liquid fuels" (gasoline) and 26.1¢ per gallon on "fuels" (diesel). Per gallon rates for alternative fuels: Ethanol (20.8¢), Methanol (15.4¢), Propane/LPG (22.8¢), E-85 (21.9¢), M-85 (17.8¢), CNG (7.9¢), LNG (18.2¢). Electricity as a fuel is taxed at 0.93¢ per kwtt. *Pa. Bulletin Vol. 40, p. 2377.*

Inheritance Tax - Annuity Not Exempt As Life Insurance

An investment product characterized as an "annuity" by the provider was not exempt from Inheritance Tax as life insurance when it allowed for regular payments to the annuitant and did not involve any element of risk on the part of the provider. The terms of the investment product provided for an initial lump sum premium deposit, and a guaranteed effective interest rate. The purchaser had an unlimited right to withdraw income after the first 30 days and to withdraw up to 15% of the total value of the annuity annually without penalty. Although the purchaser died without receiving any distributions, the policy was more akin to an annuity than to life insurance because the purchaser possessed the right to receive payments of principal and income up to the maximum amounts provided for in the agreement. *Ruling No. INH-10-002, issued July 15, 2010.*

Realty Transfer Tax - Purchase of Leasehold and Underlying Property

Tax applies to the entire purchase price where the purchaser is buying real estate subject to a short-term master lease and option to buy held by a related entity, and is simultaneously buying out the lessee. The purchaser may not exclude the purchase price allocated to the master lease and related option to buy. Because of the relationship between the lessor and lessee, the purchase is viewed as a single transaction. *Ruling No. RTT-10-003 (November 10, 2010).*

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