

PA TAX LAW NEWS

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PA Adopts Business Friendly Budget & Tax Changes

by *James L. Fritz*

The General Assembly and Governor Corbett have approved a state budget for 2012-13 which restrains state spending while preserving the scheduled phase-out of the Capital Stock and Franchise Taxes, moving to Single Sales Factor apportionment of the Corporate Net Income Tax, preserving the vendors' allowance for Sales Tax collection, adopting a \$1.65 billion credit to promote development of businesses in the Marcellus Shale Gas area and making a significant number of other substantive and procedural changes.

Capital Stock & Franchise Phase-out

Notwithstanding many interested parties - including local schools, county commissioners and social service groups - seeking to avoid cuts or obtain increases, the General Assembly and Governor preserved the scheduled phase-out of Pennsylvania's onerous Capital Stock and Franchise Taxes. The tax rate was reduced to 1.89 mills on January 1, 2012, and will be reduced to 0.89 mills on January 1, 2013, with full elimination on January 1, 2014. The benefit to the business community for FY 2012-13 is just under \$300 million.

Single Sales Factor

For taxable years beginning after December 31, 2012, business income will be apportioned using a single sales factor. Currently, the sales factor is weighted 90% while the property and payroll factors are weighted 5% each. The change will save businesses \$12 million in FY 2012-13.

Sales Tax Vendor Discount

The Corbett administration and certain elements in the Legislature attempted to cap the 1% vendor's discount at \$250 per month. Strong lobbying by the Pennsylvania Retailers Association and other business organizations demonstrated that this would saddle vendors with tens of millions of dollars of costs for collecting Pennsylvania's tax. Support from certain leaders and many rank-and-file legislators successfully preserved the vendors' compensation at 1% of tax collected, with no cap. Even this is not sufficient to cover the costs of administering the collection of the complicated tax.

Marcellus Shale Manufacturing Credit

To help entice the location of an ethane cracking plant in Pennsylvania, the Legislature has approved Governor Corbett's proposed "Resource Manufacturing Tax Credit" equal to \$0.05 per gallon of ethane purchased from January 2, 2017 to December 31, 2042, for use in manufacturing ethylene. To qualify, a taxpayer must make a capital investment of at least \$1 billion and create at least 2,500 construction-phase jobs. Credits may offset up to 20% of a qualified taxpayer's tax liabilities in the year for which credit is claimed. Credit may not be carried back or forward and may not be used to obtain a refund.

Unused credits may be transferred to the owner of a pass-through entity. Unused credits also may be sold or assigned. Sales to upstream or downstream companies are favored. A purchaser or assignee must use the credit in the calendar year in which purchased or assigned; up to 50% of a qualified tax liability may be offset by purchased or assigned credits.

Other Substantive and Procedural Changes

Sales Tax - Prepayment Alternative. Last year the General Assembly enacted a requirement for larger monthly filers to "prepay" an estimated half of their monthly sales tax liabilities (Act 26 of 2011). The prepayment has been due on the 20th of the month and has been equal to 50% of the tax remitted for the same month in the prior year. This has caused cash flow issues for companies which have experienced significant declines in tax collections compared to the prior year. To help alleviate this problem, the General Assembly has enacted an alternative for use by certain vendors in calculating the prepayment amount - 50% of the tax ultimately due for the current month. For returns due after September 30, 2012, this will apply to companies whose tax liability in the third quarter of the prior year was at least \$25,000 and less than \$100,000. Companies whose third quarter tax was \$100,000 or more must continue to pay based on the same month in the prior year.

Sales Tax – Wrapping and Packaging Services. The wrapping supply exemption provision has been amended to clarify that wrapping and packaging services will not be taxable if the property wrapped or packaged will be resold by the purchaser of the services.

Sales Tax – Processing of Eggs. The "collection, sorting, inspecting and packaging of eggs" has been added to the definition of "Processing." Effective immediately, machinery, equipment and other tangible personal property used directly and predominantly in such activities will be excluded from PA sales and use tax.

Sales Tax – Volunteer Firefighters' Organizations. Volunteer Firefighters' Relief Associations are now specifically recognized under the exemption for charitable organizations. Once issued to a Volunteer Firefighters' Relief Association or to a Volunteer Firefighters' Organization, exempt status will not expire unless and until the activities of the Organization or Association change so that the requirements for an "institution of purely public charity" are no longer met.

Corporate Tax Report Extensions. For taxable years beginning on or after January 1, 2013, Pennsylvania will automatically extend the PA due date where a federal extension is granted.

Corporate Net Income Tax – Reports of Federal Changes. For taxable years beginning on or after January 1, 2013, the deadline for submitting reports of federal changes will be six months after the change becomes final. The deadline is currently 30 days from finality.

Personal Income Tax – 1099 Misc. Requirements. Effective immediately, persons who make payments of PA-source nonemployee compensation or payments under an oil and gas lease to a resident or nonresident individual, an entity treated as a partnership for tax purposes or a single-member limited liability company, and are required to submit a 1099-Misc. to the IRS, shall file a copy with the PA Dept. of Revenue and provide a copy to the payee by the federal filing deadline. Willful failure to comply will be subject to a \$50 penalty for each violation.

Personal Income Tax - Returns of Deceased. Effective for tax years beginning on or after January 1, 2013, the final return of a deceased individual may be filed by a "personal representative" other than an executor or administrator. A

surviving spouse may file jointly with the deceased spouse for the year of death or may file a separate return for the deceased spouse; however, an after-appointed fiduciary for the deceased may file a superseding return. A joint return may be filed where both spouses die during the same year.

Personal Income Tax – Estimated Tax Penalty. The special tax provisions for poverty must now be taken into account in determining penalties for underpayment of estimated taxes.

Realty Transfer Tax – Family Exemption. Transfers between a stepparent and his or her stepchild or the spouse of the stepchild are now covered by the exemption.

Realty Transfer Tax - Acquired Real Estate Companies. For transactions occurring after December 31, 2012, a transfer for purposes of determining whether a “Real Estate Company” has been “acquired” (triggering tax) will be deemed to include the provision of a legally-binding commitment to make the transfer, enforceable at a later date.

Realty Transfer Tax – Family Farm Exemption. Retroactive to July 1, 2010, the exemptions for transfers to family-owned corporations and partnerships have been combined into a “Family Farm Business” exemption. The statute has been clarified to indicate that the business may be conducted as a general partnership or limited liability partnership as well as a corporation or limited partnership. Transfers may be made by family members or another family farm business. The current 75% asset and ownership tests, as well as other conditions, continue to apply. Transfers of ownership interests within the family also are exempted, as are transfers of assets between family farm businesses under at least 50% common ownership.

Cigarette Tax - Wholesaler Definition. Owners of 3 or more retail outlets (formerly 5) will be considered "wholesalers."

Inheritance Tax - Family Farm Exemption. Exemption now applies to transfers of agricultural real estate between members of the same family, provided the property continues to be used for agricultural business for seven years.

Inheritance Tax - Other Agricultural Transfers. Exemption also applies to the transfer of an agricultural commodity, agricultural conservation easement, agricultural reserve, agricultural use property or a forest reserve to lineal descendants or siblings.

R & D Tax Credit. The Research and Development Tax Credit annual limitation has been increased from \$40 million to \$55 million, with \$11 million designated for small business.

Job Creation Tax Credit. Credit for hiring an unemployed individual will be \$2,500 instead of \$1,000. The small business job creation requirement is reduced to '10% within three years.' The term for creation of new jobs will be 1, 2 or 3 years - as determined by DCED.

Educational Improvement Tax Credit. The annual cap on EITC credits is increased from \$75 million to \$100 million. Surplus lines insurance companies are now eligible for credit. The per-business annual credit cap is increased from \$300,000 to \$400,000 for FY 2012-13, and to \$750,000 for subsequent years. The cap on credits for contributions to pre-kindergarten scholarship organizations is increased from \$150,000 to \$200,000. The delayed application date for pass-through entities is removed.

Educational Opportunity Scholarship Tax Credit. In addition to expanding the EITC, a new credit has been established for businesses contributing to organizations awarding scholarships to students residing in some of the Commonwealth's most poorly performing public schools, to allow the student to attend participating public or non-public schools. The limitations on business contribution and business application procedures are similar to those under the EITC. A total of \$50 million in credits may be granted annually.

Film Production Tax Credit. The annual cap on credit awards is set at \$60,000,000. A purchaser or assignee of credits may carry forward unused credits purchased in 2010, to taxable years 2011 and 2012. Credits may now be used against the Bank Shares and Insurance Premiums Taxes. Awards of credits may include parts of the award amounts available in subsequent fiscal years. An additional 5% credit (above the current 25% cap) may be awarded if certain "qualified production facility" requirements are met. Under certain circumstances, the Department may waive the 60% requirement for PA production expenses.

Neighborhood Assistance Tax Credits. Preference will be given to applications by businesses contributing food or money to charitable food programs.

Historic Preservation Incentive Tax Credit. Effective July 1, 2013, taxpayers may apply for credits of up to 25% of the costs of restoring a qualified historic commercial building. Aggregate credit awards will be limited to \$3 million per year and the maximum per taxpayer will be \$500,000. Credits may be carried forward for up to 7 years. There will be no carry back or refund of credits, but unused credits may be transferred to the owners by a pass-through entity or may be sold or assigned for use in the year of sale or assignment.

Community-Based Services Tax Credit. Effective July 1, 2013, businesses contributing to providers of community-based services to individuals with intellectual disabilities or mental illness may apply for credit up to 50% of their contributions (75% if 2-year commitment). The maximum credit per business per year will be \$100,000. Total credit awards will not exceed \$3 million per year.

Changes to Tax Appeals Process

Assessments No Longer Mailed Certified. Effective immediately, the Department of Revenue is no longer required to use certified mail when issuing assessments. This appears to be driven by cost considerations as the use of certified mail originally was the Department's idea. The business community opposed this change.

Adjustments Not Immediately Impacting Tax. There has been no immediate opportunity to contest a Revenue Department adjustment that does not change the current tax. The tax code now authorizes the inclusion of such an issue in a petition for reassessment. The statute specifically recognizes that such issues may include:

- Recalculation of corporate net income tax net loss as adjusted by the Department.
- Recalculation of "average net income" for capital stock or franchise tax purposes as adjusted by the Department.
- Recalculation of personal income tax basis as adjusted by the Department.

A taxpayer still retains the option of challenging such adjustments in a subsequent year when the Department's adjustment has a tax impact.

Authority for Compromise. Although the Department implemented a compromise process several months ago for cases before the Department's Board of Appeals, there has been some question about the legal authority for such compromises. The statute now clarifies that the Secretary of Revenue may compromise any civil matter before the Department in an administrative appeal. The compromise may be based on doubt as to liability and the "promotion of effective tax administration."

Refund Limitations Extended. Two refund statutes of limitations which have caused much confusion in the tax community over the past several years have been extended. First, if an audit does not grant credit for tax paid within the audit period, the taxpayer may now file a refund petition by the later of 3-years from the date of payment or six months from the mailing date of the audit assessment, determination or settlement. Second, as to tax paid as a result of an assessment, determination or settlement, a refund petition may now be filed within six months of the date of payment (formerly six months from assessment date).

Administrative Bank Attachment

The Department of Revenue has been authorized to attach accounts subject to tax liens totaling at least \$1,000. This includes accounts of business entities, individuals operating as sole proprietors, shareholders, members and partners of pass-through entities and corporate officers or other responsible individuals who have been individually assessed and liened. Accounts may not be attached if access is restricted due to pledge as security, the financial institution has a present right to exercise a right of setoff, another party is an owner on the account or the obligor otherwise lacks an unconditional right of access. Attachment also does not apply to funds or property deposited after attachment. The financial institution may assess a reasonable administrative fee in connection with the attachment. After the financial institution confirms the amount attached, the Department must give notice to the account holder. The attachment may then be challenged within ten days by filing a motion with the county court of common pleas. Among the reasons for challenge is a request for spousal relief from joint liability.

Pennsylvania Changes Position on Taxation of "Cloud Computing"

by [Sharon R. Paxton](#)

On May 31, 2012, the Pennsylvania Department of Revenue issued a private letter ruling (Ruling No. SUT-12-001), in which it concluded that "[a]ccessing taxable canned software is taxable when the user is located in Pennsylvania." This ruling, which ties the taxability of software access to the location of the end users, represents a reversal of the Department's long-standing position that the taxability of access to software located on a remote server depended solely on the location of the server.

In earlier letter rulings, the Department had uniformly taken the position that the sale of access to software solely through the Internet was not a taxable transfer of software unless the server was located in Pennsylvania. See, e.g., Ruling Nos. SUT-10-005 and SUT-08-005, both of which have been removed from the Department's website. The Department had also applied this rule in situations where a multistate business purchased software for use by its employees. That is, if a business loaded software on a Pennsylvania server for use by employees located both inside and outside of Pennsylvania,

the Department sought to tax the entire purchase price of the software, even if a majority of the employees using the software were located outside the state. Conversely, if the software was located on a server outside Pennsylvania and accessed by employees in Pennsylvania, no portion of the software charges were subject to sales and use tax in Pennsylvania.

In Ruling No. SUT-12-001, the Department addressed two scenarios in which the taxpayer uses "cloud computing." First, the taxpayer purchases and installs software on servers for use by its employees to enable them to access their office computers and perform work-related tasks from remote locations, both within and outside of Pennsylvania. Second, the taxpayer installs software on its servers for access by its customers, who either pay a subscription fee or pay the taxpayer on a per-use basis. The Department concluded that "in light of recent case law and technological advances," a charge for electronically accessing taxable software in Pennsylvania is subject to sales and use tax because the end user "is exercising a license to use the software, as well as control or power over the software, at the user's location." Both the taxpayer's employees and its customers were characterized as "end users" of the software licenses under these scenarios. The same rationale would apply to other types of software purchased by a business and then loaded on a server for use by employee "end users" both within and outside of Pennsylvania at their office computers.

We understand that the Department plans to apply the new policy, which did not result from any change in applicable law, on a prospective basis. If the billing address for canned software which is accessed remotely is in Pennsylvania, the Department will presume that all users of the software are located in Pennsylvania. In order to rebut this presumption, a purchaser should provide an exemption certificate to the software vendor, stating the percentage of software users who are located in Pennsylvania on Line 7 of the certificate. The Department's position that the taxable use of software occurs where the software user is located, rather than where the server hosting the software is located, seems more logical than making taxability determinations based solely on the location of the server. A purchaser of the right to access software over the Internet may not know where the vendor's server(s) are located and has no control over the location of those servers. Also, the vendor could change the location of the servers from time-to-time without the subscriber's knowledge.

Further guidance from the Department may, however, be needed to clarify the difference between the purchase of a nontaxable service that is provided over the Internet and the purchase of a right to use or "access" canned software. In Ruling No. SUT-10-005, for example, the Department had addressed the taxability of various "web-based services," but seemed to base its determination that the "services" were not taxable, at least in part, on the fact that "access to software solely through the Internet is not a taxable transfer of software unless the server or data center resides in Pennsylvania." In the scenario addressed in Ruling No. SUT-10-005, the taxpayer's customers accessed its web-based services (which enabled subscribers to have remote computer access, to attend and participate in meetings online, and to provide technical computer support to employees and external customers) by downloading an applet, for which there was no charge, that allowed them to connect to the taxpayer's system. No other software was transferred to the taxpayer's customers, and the services did not allow subscribers to access the taxpayer's computer code or manipulate the software in any way. The taxpayer's proprietary software was maintained in a hosted site, on its equipment, and the equipment and software were at all times under the control of the taxpayer. While it appears that the web-based services offered by the taxpayer in Ruling No. SUT-10-005 involved "access" by subscribers to the taxpayer's proprietary software in some manner, it is not clear whether the subscribers' access to the taxpayer's system was evidenced by a "license to use" the taxpayer's software. Ruling No. SUT-12-001 does not directly address the standards that will be applied by the Department to distinguish between nontaxable services and taxable software "access" in these types of situations.

If your company requires assistance in analyzing the impact of Ruling No. SUT-12-001, please contact any member of our State and Local Tax group.

Computation of Interest on IFTA Audit Deficiencies

by Sharon R. Paxton

On May 2, 2012, a three-judge panel of the Commonwealth Court ruled in *Southern Pines Trucking v. Commonwealth*, 352 F.R. 2008, that an interstate trucking company was not entitled to credit in an IFTA audit for interest on tax overpayments made to various jurisdictions.

After an IFTA audit, the Pennsylvania Department of Revenue issued a Notice of Determination to Southern Pines identifying overpayments and underpayments by jurisdiction. The Notice imposed a net tax deficiency of \$17,840.25 (\$83,918.19 less \$66,077.94 of credits for net tax overpayments made to other jurisdictions), plus interest of \$18,615.24 (computed on the pre-credit deficiency of \$83,918.19). Southern Pines contended that the Department had improperly charged interest on amounts owed to jurisdictions where tax was underpaid, without giving any credit for interest on the company's tax overpayments to other jurisdictions.

Under IFTA, when a motor carrier's base jurisdiction conducts an audit, it is required to determine the carrier's tax reporting compliance for every member jurisdiction in which the carrier travels. IFTA Article R1230 specifically mandates that the amount of interest due be calculated separately for each jurisdiction. The IFTA agreement also provides that "[a]n overpayment for one jurisdiction shall have no effect on the interest calculation for any other jurisdiction." As a general rule, a taxpayer is entitled to interest on an IFTA overpayment only when the taxpayer files a refund claim (and the state's obligation to pay interest on a tax overpayment does not generally begin until after the refund claim is filed). Since the disputed credits were established through an IFTA audit, and not by a taxpayer's refund request, the court ruled that the Department of Revenue lacked authority under IFTA to calculate interest on the tax credits it found during the audit.

The court also determined that Southern Pines had waived its right to challenge the auditor's method of computing credits for fuel taxes allegedly paid when its owner-operators purchased fuel used in unreported operations because it did not adequately plead the issue. Nevertheless, the court examined the merits of Southern Pines' arguments regarding double taxation and indicated that those arguments lacked merit under the court's recent decision in *R & R Express v. Commonwealth*.

Recent PA Sales Tax Guidance Concerning Natural Gas and Other Mining Activities

by James L. Fritz

With the rush to develop the Marcellus Shale natural gas fields, the Pennsylvania Department of Revenue has been issuing guidance right and left to address the treatment of gas development activities under the sales and use tax and other state taxes. We have summarized below sales and use tax guidance from a recently-published bulletin, various Q&A's published on the Department's website, and several unpublished letter rulings and informal advisories. These supplement the Department's formal regulations which pre-date the Marcellus Shale "fracking" activity. Companies should keep in mind that while regulations have the force of law, published letter rulings are not binding as to anyone other than the company to which the letter was issued and other forms of published and unpublished advice are not binding at all. We can assist companies to obtain formal letter rulings on which the company may rely.

Gas recovery activities qualify as mining

Starting with basics, the Department has made clear that extracting natural gas is an excluded mining activity:

The law defines mining to include exploring for, drilling, extracting and refining of natural resources such as natural gas. The Department considers the actual mining process to begin with the drilling of the wellbore and ends with the last physical change of the gas prior to being sold and transferred by the miner to another.

PA Rev. Dept. Q & A (4/17/2012).

The Department has cited the following examples of gas recovery activities considered to be mining activities:

- Drilling
- Cementing (pumping cement slurry to bond casing or piping to the wall of the bore hole)

- Fracking (the use of a fluid, a mixture of water and chemicals, to crack the rock formation and the injection of proppants such as sand and ceramic materials into cracks in the formation to open channels through which the gas flows)
- Acidizing (the injection of acid below rock fractures to create flow channels within the rock formation)
- Extraction of gas from underground
- Removal of water and hydrocarbons from gas prior to its transfer from a miner to its customers

Id.

Taxable Pre-Mining, Post-Mining, Materials Storage and Other Non-Exempt Activities

Pennsylvania's mining exclusion applies only to tangible personal property and certain services directly used in excluded activities. Pre-production, post-production and other remote activities do not qualify.

Site Preparation. Machinery, equipment and other tangible personal property or services used to remove trees and clear ground in preparation for extraction activities is not considered to be directly used in mining. 61 Pa. Code § 32.35(a)(3)(i). Property used to build access roads also is taxable. *Sales and Use Tax Bulletin 2012-01 (4/16/2012).*

Examples of taxable site preparation equipment and materials include:

- Bull dozer
- Backhoe-front loader
- Stone, except stone directly under exempt equipment
- Road fabric
- Sluice pipe
- Security fencing
- Bridges and bridge construction materials

PA Rev. Dept. Q&A (4/17/2012).

Water and Other Materials Storage. The construction of water holding ponds and other facilities for storage of materials is not considered part of the mining process. Equipment used in fabricating such facilities, and materials consumed in the fabrication or incorporated into such facilities are not considered to be directly used in mining. *Sales and Use Tax Bulletin 2012-01 (4/16/2012).*

Examples of taxable storage facilities:

- Pipe racks/pipe boats for pipe storage
- Fuel storage units
- Sand or gravel storage units
- Oil storage tank connected to the wellhead through a pipe. Both the storage tank and the connecting pipe from the wellhead to the tank are taxable.
- Water storage ponds used to store water prior to being used in the drilling operations, including construction materials and rubber liner.
- Water transportation system pumping water from the river or creek to the water storage pond.

PA Rev. Dept. Q&A (4/17/2012).

Production Recording. Equipment and supplies used to record the volume and pressure of gas flowing from the wellhead is not directly used in mining because there is no "active causal relationship" to the production of the gas. Taxable items would include the chart recorder, batteries powering the chart recorder, charts, chart labels, pens, pen tips, pen arms and ink for the chart recorder. House and farm tap meters used to measure gas used by the property owner also would be taxable if used by the mining company (but would be exempt under the Public Utility Exclusion if used by a public utility). *Unpublished Revenue Dept. Letter Ruling.*

Exempt Mining Equipment.

Natural Gas Drilling Equipment qualifies for exclusion.

- Extracting natural gas qualifies as mining for sales and use tax purposes. Property such as drilling equipment is considered directly used in a natural gas extraction operation.
- The mining exclusion, like all business exclusions (manufacturing, processing, public utility operations, etc.), is a limited exclusion. Section 201(k)(8)(A) of the Tax Reform Code of 1971 provides that the exclusion may only be claimed by a purchaser who uses or consumes the property directly in a mining operation.

PA Rev. Dept. Q & A (4/2/2012).

Examples of exempt mining equipment and supplies in gas recovery activities.

- Drilling rig unit and all repair parts

- Drilling head
- Cutting bits
- Drilling extensions
- Fuel used to run the drilling unit
- Casing
- Cement to encase the casing
- A frack unit (affixed to the back of a truck chassis) and all repair parts and fuel used in running the frack unit
- Pump (placed at the bottom of the well)
- Pump rod (connected to the pump)
- Sucker pipe (pipe that allows oil to flow to the surface)
- Cap (affixed to the top of wellhead)
- Pump jack (provides upward and downward movement to the pump rod directly resulting in the operation of the pump)
- Electricity and off-road fuel used to run the pump jack
- Fishing or extraction tools used exclusively to retrieve and remove objects from drilled hole
- Gathering lines connecting wellhead to the last fluids and hydrocarbons removal system prior to miner selling and transferring gas
- Pit liner used in the sludge holding pond
- Silt fence and stakes

PA Rev. Dept. Q&A (4/17/2012).

Gyroscope Services. A contractor qualified for the mining exclusion for his wireline equipment used to lower a gyroscope into an oil well to determine that the well was being drilled in the proper direction. However the contractor's truck, as a registered vehicle, was not eligible for exemption. Since the operator of the equipment was under the direction of the customer, the charge for the operator was for a taxable "help supply" service. *Unpublished Revenue Dept. Letter Ruling.*

Foundations for Mining Equipment. As a general rule, property and services used in the "construction, reconstruction, alteration, remodeling, servicing, repairing, maintenance or improvement of real estate" are not covered by the mining exclusion. However, materials incorporated into a foundation for exempt drilling equipment are excluded from tax. Dozers, backhoes and other equipment used to construct the foundation would not be excluded. Sand, stone and other materials incorporated into a rigging pad are examples of excluded materials. *See, Sales and Use Tax Bulletin 2012-1 (4/16/2012).*

Compression Equipment. Equipment and supplies are excluded from tax where used to compress natural gas at or near the gas mining site. The compression qualifies as a continuation of the manufacturing/mining process. This activity would be exempt whether performed by the mine operator or by a contractor working for the operator. *Unpublished Revenue Dept. Advisory Letter.*

Electricity to Pump Oil or Natural Gas. Electricity used to pump oil out of the earth is excluded from tax because it is directly used in manufacture/mining. Electricity used to pump oil or natural gas from the well to a second location where the same company refines the oil or gas would also be directly used because the tax statute treats both extraction and refining as parts of manufacture/mining. However, if the purchaser of the electricity does not perform a second excluded operation

after extraction, tax would apply to electricity used in the transportation or storage of oil or gas after extraction. *Unpublished Revenue Dept. Letter Ruling.*

Pollution Control and Abatement. Property "used for waste handling and disposal of pollutants other than in the course of production operations is taxable unless the equipment, machinery and supplies are designed and used to control, abate or prevent air, water or noise pollution generated in the mining operation." *Sales and Use Tax Bulletin 2012-01 (4/16/2012).*

"Ponds used to control or abate pollution generated in the mining operation ... are excluded from tax. Therefore, although equipment used to build such ponds is taxable, any materials used in that construction, such as liners, sand and gravel, would be excluded from tax."

Sales and Use Tax Bulletin 2012-1 (4/16/2012).

Containment. Geotechnical products used to contain contaminated fracking water, erosion control products such as silt fences and stakes, and backup containment systems are exempt when used as pollution abatement systems. Products used to hold clean water for use in drilling are considered to be taxable pre-production products. *Unpublished Revenue Dept. Letter ruling.*

Gas Gathering Pipelines. Company which limited its activities to construction and operation of underground pipelines linking natural gas producer's wells to producer's processing plant was entitled to claim mining exclusion on dehydrators (remove water and vapors to stabilize gas), pipes and materials used as foundations under the pipes. Construction equipment used to build pipelines was taxable since not directly used in mining. *Unpublished Revenue Dept. Letter Ruling.*

Distribution Storage Facility - Mining & Public Utility Exclusions

The Department of Revenue has issued an unpublished, informal advisory letter addressing the taxability of machinery, equipment and supplies to be used in operating an underground natural gas storage facility (a converted natural gas reservoir which had been depleted). Although the facility's rates and service will be regulated by the Federal Energy Regulatory Commission, the Department did not characterize the facility, itself, as a public utility. The facility's customers, however, included local gas distribution companies and pipeline companies (which are recognized utilities) as well as non-utilities such as natural gas marketers.

The Department indicated that machinery, equipment and supplies used to withdraw natural gas from the underground storage facility would qualify for the manufacture/mining exclusion because the statutory exclusion includes "extracting from the earth or from waste or stock piles ... any natural resources" 72 P.S. § 7201(c)(3).

Machinery, equipment and supplies used to compress and inject gas into the underground storage facility would not qualify for the manufacturing/mining exclusion, but could qualify for the Public Utility Exclusion if the majority of the storage was for companies constituting recognized public utilities. *Unpublished Revenue Dept. Advisory Letter.* (NOTE: If less than a majority of the storage was used by companies otherwise recognized as public utilities, we could suggest that such a storage facility further explore whether the facility itself should be characterized as a public utility.)

Miscellaneous.

Equipment Rental. Provision of an operator with the rental of non-excluded equipment may be treated as two transactions:

Generally, when charges are billed separately for the equipment rental and the operator's time, the charges are taxable as taxable rental of equipment and taxable help supply service respectively.

PA Rev. Dept. Q & A (4/17/2012).

Compression Services. Contractor provided a nontaxable service where compressor operator installed and operated compressor "based on conditions and specifications outlined in the service agreement," the operator was not on-site at all times and compensation was on a monthly lump-sum basis. The contractor's compressor, lubricants, parts and supplies were considered exempt as directly used in mining. *Unpublished Revenue Department Letter Ruling.*

Truck Chassis. Tax applies to a "truck chassis to which drilling unit, frack unit, or service rig is affixed and repair parts." *Pa. Rev. Dept. Q&A (4/17/2012).*

Compression Services and Stripper Plant. Tax applies to a "stripper plant that strips various hydrocarbons contained within the natural gas into byproducts for sale" and to "compression services alone without removal of fluids and hydrocarbons." *Pa. Rev. Dept. Q&A (4/17/2012).*

Real Estate Assessment Appeals

Lebanon, Lehigh, Bedford, Allegheny and some other Pennsylvania counties are undergoing countywide reassessments. The deadlines for annual appeals in other counties are fast-approaching (generally August 1 or September 1). We recently published a separate newsletter discussing these appeals. The newsletter is available on the McNees Wallace & Nurick website or by clicking [here](#). If you have any questions concerning real estate assessment appeals, please contact Bert Goodman, Randy Varner or Tim Horstmann - or another member of the McNees SALT Group.

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