

Cancellation of Indebtedness Is Income in Pennsylvania, Part IV.

The final part of the majority opinion in *Wirth v. Commonwealth*, No. 82 MAP 2012 (Pa. June 17, 2014) deals with the question whether non-resident taxpayers were the subject of constitutionally improper disparate treatment.

The majority opinion rejected that contention. While acknowledging that the question was “close,” the majority concluded that there was no violation of the Privileges and Immunities Clause or of the Equal Protection or Commerce Clauses. *Wirth*, majority slip op. at 55. The result rested on two distinct rationales. First, the court noted that the non-resident taxpayers could offset the foreclosure gain against other Pennsylvania sourced income. *Id.* at 55-56. Second, in the court’s view, since any gain on the partnership interest would have been taxed in the taxpayer’s home state, it was appropriate that any loss be applied to income in that state. *Id.* at 56. For similar reasons, the court also rejected the taxpayers’ assertion that the outcome violated the uniformity clause of the Pennsylvania Constitution.

There were two separate opinions, a concurrence and a dissent. The dissent is the more interesting of the two. In it, Justice Saylor comments that “I have much difficulty with the majority’s assertion that, upon foreclosure, the outstanding balance on nonrecourse debt associated with a mortgage unambiguously results in either an ‘amount realized’ or ‘[n]et gains or income from the disposition of property,’ under Section 303 of the Tax Reform Code of 1971.” *Wirth v. Commonwealth*, No. 82 MAP 2012, dissenting slip op. at 1. As Justice Saylor explains, the federal case law that the majority relied upon was not based upon the plain meaning of the Internal Revenue Code. *Id.* at 1-2 & n.2.

In Justice Saylor’s view, a narrow, text-based approach to statutory construction was appropriate for two reasons: first, to respect separation of powers; second, to assure that taxpayers have fair notice of the nature and extent of potential tax liabilities so that they can structure their business matters accordingly. *Id.* at 5.

For my part, I find the second of these reasons to be particularly resonant, as I have a hard time believing that any of these investors were not surprised by this outcome.

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