

PENNSYLVANIA TAX: AUDITS/APPEALS/UPDATES
ALLEGHENY TAX SOCIETY – JANUARY 13, 2025

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I. AUDIT

A. Audit Notification

1. Broad request for documentation
 - a. Invoices or register tapes
 - b. Ledgers and Journals
 - c. Request for Computer Files Requirement Form
2. REV-554 – Taxpayer’s Rights and Obligations

B. Preparing for the Audit

1. Confirm audit period
2. Identify statute of limitations
3. Gather documentation
 - a. Review prior audit workpapers
 - b. Accumulate & review tax accrual information
 - c. Review purchases and sales information
 - d. Accumulate & review income tax return information
4. Analyze current compliance position - McNeil-PPC, Inc. v. Commonwealth, 834 A.2d 515 (Pa. 2003) - The Pennsylvania (“PA”) Supreme Court reversed a Commonwealth Court (“CCt”) ruling requiring the Department of Revenue (“DoR”) to correct both underpayments and overpayments of tax during audits; may have an effect on timing of refund interest, as well.
5. Develop audit strategy

C. Contact by the auditor

1. Obtain auditor information
2. Confirm taxes to be audited, audit periods
3. Ask about audit focus – request for records
4. Establish audit start date

D. Pre-Audit Conference

1. Allow auditor to provide request list
 - a. Establish timing requirements
2. Provide business background information
 - a. Tax accrual records
 - b. Plant tour
3. Set guidelines for auditor
 - a. Contact with other personnel
 - b. Communication of audit results

E. Audit Examination - Provide requested documentation

1. Sampling v. Complete audits
 - a. Random Sampling
 - b. Statistical Sampling
 - c. Block Sampling

2. Sales Tax
 - a. Tax accrual reconciliation
 - b. General ledger and return backup
 - c. Invoices
 - d. Exemption certificates
3. Use Tax
 - a. Tax accrual reconciliation
 - b. General ledger and return backup
 - c. Depreciation schedules
 - d. Purchase invoices
4. Error Resolution
 - a. Adequate time to obtain support
 - b. The law
 - c. Information sources

F. Reverse Audits

1. Identify where tax has been paid
2. Understand the law
3. Trusted sources for information
4. Evidence of exemption

G. Post-Audit Conference

1. Obtain all final workpapers
 - a. Compare to drafts for accuracy
 - b. Ensure credits/overpayments are applied
2. Discuss recommendations for improvement
3. Discuss any disagreements in detail
 - a. Supervisory or other informal meetings
 - b. Legal avenues for dispute

H. Notice of Assessment

1. Reconcile to audit workpapers
2. Determine if appeal is necessary

II. APPEALS

A. Reassessment

1. Board of Appeals (“BoA”) - Any taxpayer who is not satisfied with the DoR’s assessment can petition for reassessment to the BoA, which is a Bureau of the DoR, within **60 days** of the mailing date of the notice of assessment, effective for all assessments **post-12.29.2017**. However, under **Act 123 of 2024**, the statute of limitations to file appeals for Article III taxes (Personal Income Tax/PIT) has been increased back to **90 days**, effective immediately (10/29/2024, see more below).
 - a. Miscellaneous Tax Bulletin 2011-02 (November 16, 2011) Offers in Compromise
2. Board of Finance and Revenue (“BFR”) - Within **60 days** (non-Art. III taxes), after the mailing date of the BoA’s Decision & Order (“D&O”) – post 12.29.2017 – the petitioner may petition for review to the BFR, which is part of the Department of

Treasury (“Treasury”); under Act 123 of 2024, this has been increased to **90 days** for PIT/Art. III taxes.

The BFR was restructured in 2014 under Act 52 of 2013, to wit:

- a. Three (3) appointed members: the Chair is appointed by the Sec. of Treasury; the remaining 2 members are appointed by the Governor and confirmed by the Senate (6-year terms, though one of the 1st at-large members is still there until next year); stay until removed.
- b. *Ex parte* communications are prohibited, other than procedural issues.
- c. Both attorneys and accountants permitted to practice before it.
- d. Ability to compromise – very restrictive.
- e. Published decisions in a searchable database.
- f. The DoR is a full party to the appeal & will be at the hearing to counter-argue.
- g. BFR hearings are now being taped & recorded & may be placed on the website.

The BFR may uphold the action of the BoA, or it may redetermine, according to law, either the amount due PA or the petitioner. The BFR must notify both the DoR and the petitioner of its action. If the BFR does not act within six months, the action taken by the BoA is upheld. One can petition the BFR for Reconsideration of a D&O within 15 days of the mailing date thereof; this usually works well for math errors.

Act 123 of 2024: the PICPA, Biz Chamber, and the PA Dept. of Treasury really pushed for this legislation, signed into law by Gov. Shapiro on 10/29/2024, effective 1/27/2024; the biggest difference – aside from the PIT appeal deadline changes noted above (back to 90 days) – relates to the establishment of a formal Settlement Conference Process, providing for paid Settlement Officers (“SO”); SOs will act as mediators to assist the Parties (taxpayer & DoR) to come to a settlement before the BFR hears the case and issues a D&O. *If* (?) the DoR’s Office of Chief Counsel (“OCC”) chooses to cooperate, this could greatly reduce the number of cases – particularly large sales/use tax refund cases which traditionally made-up half of the CCt docket (though, see below).

Oddly enough, the old Offer-in-Compromise system will still be in-place – i.e., can make a settlement offer & the DoR’s settlement committee will either accept, deny, or counteroffer with no back-and-forth negotiation (take-it-or-leave-it).

3. PA Commonwealth Court - Any party aggrieved by a decision or a failure to act within six months may appeal to CCt. Either the taxpayer or the DoR (via the Office of Attorney General (“OAG”) may appeal to CCt within **30 days** of the mailing date of the BFR’s D&O; CCt panel (3 member) decisions may be petitioned on Exceptions to the entire CCt *en banc*; it is not unheard-of for the entire CCt to reverse the panel (see Green Acres case). Because the OAG is crushed and has too few deputies to handle the massive docket, all sales/use tax refund appeals (and some reassessments) are to be transferred to the DoR/OCC for resolution; as of last Thanksgiving, only about 400 have been pushed to the OCC, who has started hiring more attorneys.
4. PA Supreme Court - CCt decisions (post-Exceptions) may be appealed to the PA SupCt as a **matter of right** for state tax cases, not under a writ of *allocator*, as in other cases that start in local Courts, since CCt is considered a trial *de novo*, or “anew,” being the first time a **state** tax case is heard in the Courts with a formal

record; **local** tax cases – e.g., property/earned income/business privilege taxes – are different & go to the Court of Common Pleas first; thus, the CCt acts as an appellate court and appeals are NOT guaranteed to be heard by the SupCt; it is not unheard-of – and, is quite common, actually – for the PA SupCt to reverse the PA CCt (see NexTel Communications, Mission Funding Alpha) or even themselves (see Alcatel-Lucent USA/General Motors cases). Recently, a writ of *allocator* was granted for the PGH Jock Tax case (ask Chuck P.); also, petition for reargument was denied in Pearlstein and has been requested in Alcatel-Lucent USA, but not yet decided.

5. U.S. Supreme Court - Taxpayers may petition to the U.S. Supreme Court (“The Supremes”) for a writ of *certiorari*, which it may issue or deny said writ; most state tax cases are denied, though one of the more recent cases (see Wayfair) altered the national sales tax landscape. Most recently, Zilka v. City of Philadelphia was petitioned to The Supremes, and petitioner’s counsel expects to hear whether or not a writ of *certiorari* is granted by the week of 1/13.

B. Refund – A taxpayer may file a Petition for Refund:

1. Requesting the review of the denial of any credit in the audit within 6 months after the date of the assessment or within three years of actual payment of the tax, whichever is later, or,
2. Requesting a refund of monies paid as a result of an assessment within 6 months after the actual payment of the assessment.
3. Petitions for Refund begin with the BoA and proceed through the appeals process as described for Petitions for Reassessment; however, as of May of 2017, the DoR has instituted a policy in which all “complex” refunds (e.g., > \$100k) will be pushed-down to the Bureau of Audits for review, along with a review of potential underpayments; the BoA will technically issue a denial *without prejudice*, so that the Audit results can be appealed, as per above; the DoR also issued a revised appeal schedule (REV-39) for use in all refunds during this same time period.

III. PA/Local Tax UPDATES

- A. Recent PA tax changes per last budget bill: continued CNI reduction, NOL expansion, etc.
- B. Sales/use tax collection, reporting, & audits – Act 84 of 2016 (digital items), etc., and the recent Canned Computer Software/Digital Goods guidance from the DoR looms large over audits & appeals.
- C. Recent PA Courts’ case decisions of note: NHLPA, et al, v. City of Pittsburgh (“PGH Jock Tax”); Quality Driven Copack v. PA; Synthes USA v. PA; Pearlstein/Slogoff v. PA; Alcatel-Lucent USA v. PA; Zilka v. Philly.
- D. Cases currently in the litigation pipeline @ OAG.
- E. Allegheny County property tax reform/countywide reassessment?
- F. Issues/emerging issues in which to be cognizant.