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November 30, 2011

Ms. Mary R. Sprunk
Office of Chief Counsel
PA Department of Revenue
P. O. Box 281061
Harrisburg, PA 17128-1061

Re: Proposed Regulations relating to 61 Pa. Code, Chapter 91, Realty Transfer Tax

Dear Ms. Sprunk:

When I read the proposed regulations regarding Realty Transfer Tax in the November 19, 2011 issue of the Pennsylvania Bulletin, I felt an overwhelming sense of *déjà vu*; but then I realized that these were the proposed regulations that were circulated in draft form for comment among the members of the Pennsylvania Bar Association's Tax Law Section almost one year ago and that the actual proposed regulations had never appeared in print before.

I remember writing to you at that time with comments; and, sure enough, I was able to retrieve a copy of the December 23, 2010 letter I wrote to you at the time about several of the draft changes. Since the now officially-proposed regulations vary only slightly from their draft counterparts of over a year ago, I shall not try your patience with a repeat (except in one situation) of what I said a year ago. I am enclosing a copy of that letter and reiterate my comments and objections contained in that letter.

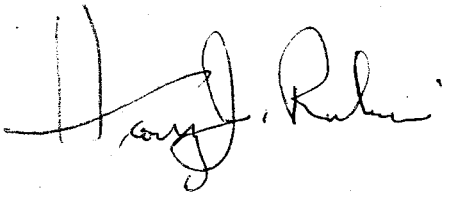
The one situation that bears repeated objection --- now, even more so --- is the change of the words "exclusion" and "excluded" to "exemption" and "exempt." Since the circulation a year ago of the draft proposal, the Commonwealth Court has handed down (on March 29, 2011) its decision and opinion in *Charles O. Miller, Jr. and Dorothy M. Miller v. Commonwealth of Pennsylvania,* 757 F.R. 2007, in which the Court, in a 6 to 1 decision emphatically rejected this argument made by the Commonwealth regarding the characterization of the non-taxable transactions that the Department of Revenue now wants to adopt. Even the one dissenting judge did not exhibit any dissent from this position but rather dissented on the substantive merits of the case.

Standing alone, if no more were at hand, this would require the Department to withdraw all references to this change in the proposed regulations. However, I understand that the

Commonwealth has appealed this decision to the Pennsylvania Supreme Court; and it ill behooves the Department to proceed with this proposed regulatory change while the case is yet undecided by Pennsylvania's highest Court. I am not a betting person; but I would be willing to wager a small sum that on this issue the Supreme Court affirms the Commonwealth Court regardless of what the former may do with respect to the merits of the case (on which the Commonwealth may have a perfectly good position).

I suggest that either this part of the proposed regulatory change (which the Department has characterized as "generic change (2)") be withdrawn or that adoption of the entire set of proposed regulations be postponed pending the decision by the Supreme Court in the *Miller* case. If my guess is correct regarding the Supreme Court's holding on the "exclusion versus exemption" issue, the Department will have considerable egg on its face if it now proceeds to adopt the proposed regulation in final form.

Sincerely,



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December 23, 2010

Ms. Mary R. Sprunk
Office of Chief Counsel
PA Department of Revenue
P. O. Box 281061
Harrisburg, PA 17128-1061

Re: Draft Proposed Regulation relating to 61 Pa. Code, Chapter 91, Realty Transfer Tax

Dear Ms. Sprunk:

I'm sending these comments to you as a result of my recent receipt of the draft proposal from the Pennsylvania Bar Association. I apologize for the delay in responding --- too much to read and too many diversions. Nevertheless, I hope they are helpful.

1. I have one general comment in response to the two generic changes mentioned at the beginning of the Explanation as changes being proposed throughout the regulation. One of these changes is described as follows: " 'Excluded' has been changed to 'exempt.' "

There is no justification for this change. There has been no amendment to the statute of which I am aware that requires it. The word "exempt" is used in the statute only in connection with a description of parties who or which are not subject to realty transfer tax (e.g., the United States). The word "excluded" remains the only word used to describe a particular transaction (e.g., a testamentary transfer) that is not included among the transactions subject to the tax.

An exclusion is not an exemption. An exclusion is used generally in tax matters to describe a transaction that is inherently free from tax --- i.e., it is not included in the taxable transactons base at all. An exemption is used to describe a transaction that may otherwise be taxable but that, because of the particular situation being described, is free from tax. The traditional consequence of this distinction is that an exclusion is interpreted strictly against the government that is trying to impose the tax while an exemption is interpreted strictly against a taxpayer who is claiming that the otherwise applicable tax does not apply to the particular taxpayer in the situation presented.

There is no justification for this change.

2. The statute provides that no tax is to be imposed upon transactions between a principal and the principal's agent --- i.e., a transfer of real estate between them is excluded from tax. This exclusion has long been a part of the statute (section 1102-C.3 (11)) and has long been reflected in a regulatory counterpart (61 Pa. Code section 91.153). I think it is reasonable to conclude that the boundaries of this particular exclusion have long been understood by everyone (with the one exception of Internal Revenue Code section 1031 transactions, about which I shall comment further below).

In this light I question the necessity of amending this regulatory provision at this late date to add new words --- "straw party" and "real party in interest" --- which essentially add nothing to the regulatory provision beyond use of the traditional words of "principal" and "agent." The change is redundant, only provides confusion and is unnecessary.

3. The one area in which application of the normal principal and agent exclusion has not been satisfactorily addressed is in the context of like-kind exchanges pursuant to Federal Internal Code section 1031; and the addition of proposed subsection (e) to 61 Pa. Code section 91.153 does not help the situation. It reflects the Department of Revenue's total lack of understanding of the Federal regulations under section 1031 of the IRC, particularly its failure to understand the particular (and peculiar) meaning of the term "agent" as used in those Federal regulations.

These changes should all be withdrawn. In addition, the Department of Revenue should convene a task force of persons knowledgeable in the area of section 1031 transactions in an effort to focus its attention more accurately and clearly on this matter. Once that is done, the need for a change in the regulations may disappear.

4. *Baehr Bros. v .Commonwealth,* Regulation Section 91.170. In 2007 --- 28 years after the decision was written --- The Department of Revenue latched on to one sentence of *dictum* in a 1979 Pennsylvania Supreme Court decision **that it lost** and erected an entire superstructure of regulatory language essentially designed to capture additional realty transfer tax in situations where multiple unrelated parties may collapse proposed transfers (e.g., X to Y to Z) of real estate into an single transfer (e.g., X to Z) and attempt to pay only one tax where two taxes would have been due if each transfer had been made separately (e.g., X to Y and Y to Z). I tend to agree with the Department in this matter although I do not think that this "wretched excess" of regulatory matter is necessary.

But, that comment is just an aside. The major change to the existing regulation is a revision to Example 1 of subsection (b). Present example 1 is quite simple. It says that if X agrees to sell a parcel of real estate to Y for $100,000, if Y then assigns his rights under the sales agreement to Z for $1,000,000, if X gives a deed directly to Z and receives $100,000 from Z, and if Z then pays $1,000,000 to Y, realty transfer tax is due on $1,100,000 (as if X transferred the real estate by deed to Y for $100,000 and then Y transferred the same real estate to Z for $1,000,000).

Revised example 1 is both substantively different and a quite confusing. It says that X agrees to sell a parcel of real estate to Y for $100,000 and Y subsequently assigns his rights to Z for

$900,000 with Z assuming Y's $100,000 obligation to X. It goes on: "Therefore, the total amount that Z must pay as a result of the assignment is $1,000,000." X then conveys the real estate to Z who pays X $100,000 and Y $900,000. It correctly notes that there are two taxable transaction in this one deed, X to Y and Y to Z, and, I believe incorrectly, asserts that "The taxable value of the deed from X to Z is $1,100,000 [sic] based upon the original sale price of $100,000 and the total amount of $1 million that Z had to pay as a result of the assignment.

Truly, the Department has found a way to covert lead into gold. The actual consideration that changed hands here was $1,000,000, not $1,100,000. If X had conveyed the property by deed to Y for $100,000, there would have been tax on $100,000. If Y had then conveyed the property to Z for $900,000, there would have been tax on $900,000 The Commonwealth would have received tax on a total of $1,000,000. In a two-transaction situation, Z would not also have had to pay an additional $100,000 to X because Y would have already paid it; in a one-transaction situation, Y would not have had to pay $100,000 to X because Z will pay it. The example is patently incorrect even under the logic of the *Baehr Bros* dictum. The present example 1 is correct and should be retained.

Sincerely,

Harry J. Rubin

bcc: Caroline Hoffer, Jeff Lobach

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