

THE STERLING ACT OF 1932

Establishment of the Sterling Act

In 1932, the PA General Assembly authorized the city of Philadelphia to levy, assess and collect...such taxes on persons, transactions, occupations, privileges, subjects and personal property...as it shall determine...” The Philadelphia income tax was one of three first levied in the nation. Under this broad authority, Philadelphia has enacted taxes on wages, earnings and net profits, admissions to amusements, real estate transfers, parking lot receipts, mechanical devices, bowling alleys and sound reproduction. The income tax imposed by the city applies not only to residents of the city wherever they may work, but also to nonresidents earning income within the city. A 1977 law limited increases in the rate levied on nonresidents. Since the city’s tax was imposed before any other local government income taxes, the non-resident income tax was retained by the city and a credit provision allowed non-residents to reduce their income taxes in their school district and municipality by the amount paid to the city of Philadelphia. The Sterling Act is only state law that authorized non-resident income taxation.

A resident of a school district who commutes to Philadelphia for work is able to deduct the city commuter wage taxes from any local EIT that the school district of residence levies. As a result, many suburban communities lose EIT revenue – and some find that it is not even worthwhile to levy the tax. As jobs have become suburbanized (a long term trend over 30 to 50 years), the crediting provisions of the Sterling Act have become less significant across all of the suburbs and some of the suburbs have instituted earned income taxes. Philadelphia Wage Tax rates have been reduced for taxable compensation as of January 1, 2006. The Philadelphia resident rate is 4.301% and the non-resident rate is 3.7716%.

Act 1 and the Sterling Tax

Act 1, in section 324, specifies that each school district will receive, from the Property Tax Relief Fund, an amount equal to the aggregate Sterling Act amount paid by their resident taxpayers. These funds will then be used to provide a portion of the homestead/farmstead exclusion in the district.

Impact on the Taxpayer

A district’s resident taxpayer who pays the Sterling tax or the Philadelphia wage tax will continue to pay the Sterling tax and claim a credit for income taxes levied by the school district of residence. Under Act 1, it becomes more likely that a district of residence will levy an EIT. If they are a homeowner, the taxpayer will benefit from lower property taxes resulting from the district tax shift. They will also benefit from lower property taxes resulting from gaming funds allocated to the district and a credit against taxes paid to the city of Philadelphia.

Impact on the School District Budget

This reimbursement is revenue neutral for a school district. However, it gives them a more diverse revenue base which can now include property tax shifts, gaming funds and a state credit for the Sterling tax. This could potentially allow a school district to provide a larger dollar exclusion per property in part relying on gaming funds, rather than on property tax shift. The statute, in section 324, specifies that school districts will receive a full payment when the amount available for distribution through the Property Tax Relief Fund is greater than \$750 million and

that the payments will be pro rata reduced among all eligible districts when the amount in the Fund is less than \$750 million. Full payment is calculated as the aggregate of each resident taxpayers' Sterling tax on salaries, wages, commissions or other compensation.

Sources

Governor's Center for Local Government Services "Taxation Manual"

Act 1 of 2006

Philadelphia Revenue Department website <http://www.phila.gov/revenue/Home/home.html>