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**Pittsburgh's New Business Tax Structure: Who Pays?**

After much deliberation, the Pennsylvania Legislature agreed on a bailout plan for the City of Pittsburgh. One of the key components of the bailout plan is the implementation of a payroll tax on all for-profit firms and the for-profit operations of non-profit organizations. This new tax will be close to revenue neutral since the mercantile tax will be eliminated and the business privilege tax is reduced by two-thirds immediately and is to be phased out completely over time. It is assumed the City will adopt the Legislature's tax plan before the end of December.

Under the old system, the City collected \$50.6 million in revenue, \$43.2 million from the business privilege and \$7.4 million from the mercantile tax. The Intergovernmental Cooperation Authority (Oversight Board) estimated a payroll tax set at 0.55 percent would generate \$41.2 million in revenues. The business privilege tax at 2 mils should produce about \$14.4 million. Therefore, the new combination of payroll and a reduced business privilege tax is expected to garner \$55.6 million in tax revenues for the City—an increase of \$5 million over previous business tax revenues.

One intention of allowing the payroll tax was to create a fairer tax compared to the business privilege tax, a gross receipts tax with major exemptions, including manufacturing firms and the financial industry. According to the State Department of Labor and Industry's Center for Workforce Information Analysis (L&I), there were 14,380 manufacturing workers in the City in 2003. Using adjusted Allegheny County wage data, we estimate the average manufacturing wage in the City to be around \$70,000 per year. Thus, the manufacturing payroll would be just over \$1 billion annually. With a 0.55 percent payroll tax, the City can expect tax revenues from this sector of approximately \$5.5 million.

The financial sector will also be hit by the payroll tax. According to the State, there are 24,237 workers in the finance industry and we place the average wage for workers in the financial sector at around \$72,300. These data put the estimated financial payroll in the City at nearly \$1.8 billion, which should generate \$9.6 million in payroll taxes. Taken together, the manufacturing industry and financial industry, which are exempt from the business privilege tax, will produce \$15.1 million in revenues for the City.

How will firms who were paying business taxes under the old system fare under the new system? Those paying the mercantile tax—retailers and wholesalers—will no longer pay a tax on their gross receipts, but they will have to pay the payroll tax. According to the Department of Labor and Industry, there are more than 20,800 workers in the retail industry working in the City and another 5,900 in the wholesale industry. Countywide, workers in retail earned an average wage of \$24,250 in 2004 while workers in the wholesale industry earned \$52,470. Using these figures, we estimate the City will collect \$4.5 million in payroll taxes from these sectors. Previously they

had been paying \$7.4 million in mercantile taxes and therefore they will pay \$2.9 million less in business taxes than under the old system.

Meanwhile, companies that were required to pay the business privilege tax will still be required to pay that tax, but at a reduced rate. But they will also be required to pay the payroll tax. The Oversight Board estimates the total payroll tax revenues to be \$41.2 million. As estimated above, manufacturers and financial institutions will pay \$15.1 million and retailers and wholesalers will pay \$4.5 million for a total of \$19.6 million. Therefore, those who were paying the business privilege tax will account for the difference—\$21.6 million. Taking their payroll tax payments and what they still owe in business privilege taxes, they will have total tax payments of \$36.0 million under the new plan. Thus, these firms can expect to see a net reduction in their business taxes of roughly \$7.2 million. The table below summarizes these changes.

	Revenues from Firms Who Pay the Business Privilege Tax (in millions)	Revenues from Firms Who Pay the Mercantile Tax (in millions)	Revenues from Firms Who Paid neither BPT or Mercantile Tax (in millions)	Total Tax Revenues (in millions)
Under Old System	\$43.2	\$7.4	\$0	\$50.6
Under New System	\$14.4	\$0	\$0	
Payroll Tax Payments	\$21.6	\$4.5	\$15.1	
Total Revenues Under New System	\$36.0	\$4.5	\$15.1	\$55.6
Increase/Decrease in total business taxes	\$(7.2)	\$(2.9)	\$15.1	\$5.0

Overall, business taxes will rise by some \$5million. The increase is due to the \$15 million in payroll taxes paid by manufacturing and financial firms that more than offsets the decrease in mercantile and business privilege taxes.

For the firms who will pay both the business privilege tax and the payroll tax in 2005, there is a simple formula for determining which ones will pay more total taxes and those who will pay less total taxes than they paid under the old system. If the firm has a payroll greater than 73 percent of its gross receipts, it will pay more. The higher the ratio of payroll to gross receipts above 73 percent the more added taxes the y will pay. By the same token, those firms with payrolls less than 73 percent of gross receipts will have a smaller total business tax bill than before.

For the retail mercantile taxpayers, only those with payrolls exceeding 36 percent of sales will pay more. And for wholesalers, those having payrolls more than 18 percent of sales will pay more under the new system. Since both the business privilege taxpayers and the mercantile payers will pay less total taxes, it is reasonable to assume that most firms will enjoy some reduction in business taxes compared to the old system. However, it is important to remember that there might be some who will not be so fortunate and will actually pay more.

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