Dealing With A Mobile Workforce

State Tax Considerations, Including Nexus, Individual Income Taxation and Withholding

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Dealing With A Mobile Workforce

Topics:
- Nexus Considerations
- Individual Income Taxation
- Withholding for Multi-State Businesses
- Federal Law: Proposed Solutions
- Other Issues
  - Federal Tax Travel Issues
  - Unemployment Insurance
  - International Tax
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- Nexus Considerations:
  - Non-Resident Workers and Nexus
  - Nexus: Minimum Connection With State
  - Business (Income/Franchise) Tax
  - Sales and Use Tax
  - Unemployment Insurance
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- Nexus – Constitutionally Limited Tax Jurisdiction
  - Transporter moved GM vehicles from Jackson MS rail station to MS dealers, but vehicles were shipped in Interstate Commerce
  - Test Applicable to taxing Interstate Commerce
    - Substantial Nexus between state and taxpayer
    - No discrimination against Interstate Commerce
    - Fair Apportionment to reflect activity in state
    - Related to services provided by State (e.g., police and roads)

- Statutory Limitation: PL-86-272
  - Sales of tangible personal property and
  - mere solicitation
  - n/a to services or activities beyond mere solicitation
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- Nexus – Employee/Independent Contractor:
  - Test: Whether activities of employee “performed in this state on behalf of the taxpayer are significantly associated with the taxpayer’s ability to establish or maintain a market in this state for its sales.”
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- Nexus – Employee/Independent Contractor:
  - Operational employees versus administrative employees
    - Florida technical Assistance Advisement No. 09A-058 (consulting independent contractor working on non-Florida company processes from her Florida home did not create sales and use tax nexus – general consulting)
  - Tennessee Letter Ruling No. 97-04 (one officer of a non-TN company worked from his TN home – for personal reasons – no income/franchise tax nexus)
  - *NJ Telebright Corp v Director, Division of Taxation*, 25 NJ Tax – Maryland software developer had nexus in NJ based on one NJ resident employee who worked in his NJ home performing daily software code writing for products sold by the employer – operational work)
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- **Nexus – Non-Resident Employees**
  - Employer nexus: income/franchise taxes, sales and use taxes, employer taxes (withholding)
  - Employee – individual income tax at workplace location
  - Employee nexus/jurisdiction
    - **Resident** subject to individual income tax on ALL income in residence state
    - **Non-resident** subject to individual income tax on income derived from sources within the non-resident state (workplace)
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- Individual Income Tax
  - No State Individual Income Tax
    - Washington
    - Nevada
    - Wyoming
    - South Dakota
    - Texas
    - Florida
    - Tennessee
    - New Hampshire
    - DC – no tax on non-residents working in DC
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- Individual Income Tax
  - Non-residents subject to tax in state in which services are provided
  - Focus on state sovereignty – Federalism
  - Lack of uniformity in taxation and credits
  - *De minimus* rules normally not broad protection – working in a state 1 day or earning $1
  - Reciprocity is limited AND specific
  - Reciprocal states are summarized in the following table:
## State Reciprocity Agreement Summary

<table>
<thead>
<tr>
<th>STATE</th>
<th>RECIPROCITY WITH STATE(S)</th>
<th>NON–RESIDENT FORM</th>
<th>NOTES</th>
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<tbody>
<tr>
<td>Arkansas</td>
<td>Texas</td>
<td>Arkansas Form AR4EC(TX) – Texarkana Employee’s Withholding Exemption Certificate</td>
<td>Employees claiming exemption from Arkansas withholding must be residents of either Texarkana, TX and Texarkana, AR. Texas has no individual income tax.</td>
</tr>
<tr>
<td>District of Columbia</td>
<td>Maryland and Virginia</td>
<td>D.C. Form D–4A – Certificate of Nonresident in the District of Columbia</td>
<td>Form D–4A must be filed by &quot;non–resident&quot; to be exempt from D.C. withholding. To qualify as a non–resident an employee must have a permanent residence outside DC during the entire tax year and not &quot;reside&quot; in DC for 183 days or more during the tax year.</td>
</tr>
<tr>
<td>Illinois</td>
<td>Iowa, Kentucky, Michigan, Wisconsin</td>
<td>Illinois Form IL–W–5–NR – Employee’s Statement of Nonresidence in Illinois</td>
<td></td>
</tr>
<tr>
<td>Indiana</td>
<td>Kentucky, Michigan, Ohio, Pennsylvania, Wisconsin</td>
<td>Indiana – Certificate of Residence WH–47</td>
<td></td>
</tr>
<tr>
<td>Iowa</td>
<td>Illinois</td>
<td>Iowa Form 44–016 – Employee’s Statement of Nonresidence in Iowa</td>
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<td>Kentucky</td>
<td>Illinois, Indiana, Michigan, Ohio, West Virginia, Wisconsin, Virginia</td>
<td>Kentucky Form 42A809 – Certificate of Nonresidence</td>
<td></td>
</tr>
<tr>
<td>Maryland</td>
<td>District of Columbia, Pennsylvania, Virginia, West Virginia</td>
<td>Maryland Form MW 507 – Employee’s Maryland Withholding Exemption Certificate</td>
<td></td>
</tr>
<tr>
<td>Michigan</td>
<td>Illinois, Indiana, Kentucky, Minnesota, Ohio, Wisconsin</td>
<td>Statement of Non–residence in Michigan</td>
<td>Michigan does not have a specific form. An employer generally must develop a form or obtain a signed and dated letter from the employee. Form or letter must contain employee’s name, legal address, and SSN. The employer must retain this document in his files. A sample form is attached.</td>
</tr>
<tr>
<td>Minnesota</td>
<td>Michigan, North Dakota</td>
<td>Minnesota Form MWR – Reciprocity Exemption/Affidavit of Residency for Tax Year 2014</td>
<td></td>
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<td>Montana</td>
<td>North Dakota</td>
<td>Montana Form NR–2 – Employee Certificate of North Dakota Residence</td>
<td></td>
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<tr>
<td>New Jersey</td>
<td>Pennsylvania</td>
<td>New Jersey Form NJ–165 – Employee's Certificate of Nonresidence in New Jersey</td>
<td></td>
</tr>
<tr>
<td>North Dakota</td>
<td>Minnesota, Montana</td>
<td>North Dakota Form NDW–R – Reciprocity exemption from withholding for qualifying Minnesota and Montana residents working in North Dakota</td>
<td></td>
</tr>
<tr>
<td>Ohio</td>
<td>Indiana, Kentucky, Michigan, Pennsylvania, West Virginia</td>
<td>Ohio Form IT 4NR – Employee’s Statement of Residency in a Reciprocity State</td>
<td></td>
</tr>
<tr>
<td>Pennsylvania</td>
<td>Indiana, Maryland, New Jersey, Ohio, Virginia, West Virginia</td>
<td>Pennsylvania Rev–419 – Employee's Nonwithholding Application Certificate</td>
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<td>Texas</td>
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<td>See Arkansas summary above</td>
<td>Texas does not impose an individual income tax. Reciprocity with Arkansas applies to residents of Texarkana, AR and Texarkana, TX – Arkansas withholding.</td>
</tr>
<tr>
<td>Virginia</td>
<td>District of Columbia, Kentucky, Maryland, Pennsylvania, West Virginia</td>
<td>Virginia Form VA-4 – Personal Exemption Worksheet</td>
<td></td>
</tr>
<tr>
<td>West Virginia</td>
<td>Kentucky, Maryland, Ohio, Pennsylvania, Virginia</td>
<td>West Virginia Form WV/IT-104 – Employee's Withholding Exemption Certificate</td>
<td></td>
</tr>
<tr>
<td>Wisconsin</td>
<td>Illinois, Indiana, Kentucky, Michigan</td>
<td>Form W-220 – Nonresident Employee's Withholding Reciprocity Declaration (residents of Illinois, Indiana, Kentucky)</td>
<td>Reciprocity between WI and MN existed prior to 2010, but was not renewed.</td>
</tr>
</tbody>
</table>
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- Reciprocity Agreements
  - 27 states do not have reciprocity agreements
  - Alabama, Arkansas (except Texarkana), California, Colorado, Connecticut, Delaware, Georgia, Hawaii, Idaho, Kansas, Louisiana, Maine, Massachusetts, Missouri, Nebraska, New Hampshire, New Mexico, New York, North Carolina, Oklahoma, Oregon, Rhode Island, South Carolina, Tennessee, Utah and Vermont
Arizona – Hybrid Reciprocal Arrangement

Arizona does not have reciprocity agreements with any other state. But Arizona has special provisions for residents of the following states: California, Washington, DC, Indiana, Oregon and Virginia.

“The Department is authorized to relieve employers from withholding if the non-residents are allowed a tax credit for income taxes paid to their state of residence sufficient to offset the Arizona tax to be withheld.” An Arizona non-resident may claim an exemption from Arizona non-resident (workplace) withholding:

- (1) – the employee is a resident of California, Washington, DC, Indiana, Oregon or Virginia and
- (2) – the employee is allowed a tax credit for income taxes paid to his state of residency.

See A.R.S. Sec. 43–403; A.R.S. Sec. 43–1096; A.R.S. Sec. 43–434
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- Withholding For A Mobile Workforce
  - Non-uniformity among states
  - Employer burden – penalty exposure
  - Again, reciprocity limited and specific
  - Predisposition towards over-withholding
  - Even if withholding is not required, employees could owe tax (e.g., *de minimus* withholding exception)
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- Withholding Types
  - Resident withholding
    - Only required if employer has nexus in resident state
    - e.g., NY resident working in CT. NY resident owed NY income tax on all earnings, Employer not required to withhold CT tax. Employee owes NY tax on income and takes credit for CT taxes paid.
  - Workplace (non-resident) withholding
    - Required in state in which work is performed
    - e.g., Employer withholding CT tax (CT workplace)
  - Confusion within tax, payroll, HR, management departments
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- Non-Resident Withholding
  - No uniformity among states
  - Residency tests
    - Domicile
    - Present intent
    - Number of days
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- *De Minimus* Exceptions:
  - New York “*de minimus*” threshold: withholding not required on wages of non-resident employee who works in NY 14 days or less during the calendar year. Prior example CT resident in NY – NO W/H
  - NY memorandum provides guidance re: employer’s withholding responsibilities under the “14-day” rule. (TSB–M–12(5)I, N.Y.S. Dept. of Taxation and Finance, July 5, 2012)
  - Other states vary widely
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- *De Minimus* Exceptions:
  - Other examples of “*de minimus*” threshold states: California, Hawaii, New Jersey, Oklahoma.
  - No uniformity – *De minimus* threshold an be based on different standards/measures.
  - Withholding failures – employers can be assessed for uncollected tax plus penalties and interest (similar to federal Sec. 6672 trust fund penalty).
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- General rule – state income tax withholding is required on the wages of a non-resident employee performing services in a workplace state.
- Exception: State Reciprocity Agreements between or among reciprocal states provide for individual income tax and withholding reciprocity – employer not required to withhold state income tax for the workplace state if the employee is a non-resident of that state AND employee is a resident of the reciprocal state).
- Example: Employee is a resident of Constantine, Michigan, but works at all times in Bristol, Indiana. Employer is not required to withhold Indiana income tax on the employee’s wages (only withhold Michigan income tax) IF the employer has the appropriate form completed and signed by the employee in its records.
Remedial Actions: Voluntary Disclosure Agreement ("VDA")

- Options available to employers that should have been withholding on non-residents wages.
- States generally have VDA programs for non-resident payroll withholding delinquencies.
  - Similar to business tax or sales and use tax VDA programs
  - Benefits typically include limited look-back period and penalty abatement. (However, because payroll is a “trust fund tax”, benefits may be limited if payroll tax was withheld and not remitted)
  - Whenever a VDA is being signed, it is good practice to consider potential payroll withholding exposure.
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- Federal Law Proposed Solutions
  - Mobile Workforce Act
- Supported by AICPA, COST, State CPA societies, State Bar Associations and Others
  - Uniformity
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- Remedial Actions: Federal Mobile Workforce Legislation

  Stated Purpose: “To limit the authority of states to tax certain income of employees for employment duties performed in other states” (Congressional Commerce Clause Action)

  - H.R. 1129: Mobile Workforce Income Tax Simplification Act of 2013 (S. 1645 [Identical Senate Bill]).
  - Would prohibit “the wages or other remuneration earned by an employee who performed employment duties in more than one state from being subject to income tax in any state other than:
    1. the state of the employee’s residence, and
    2. the state within which the employee is present and performing employment duties for more than 30 days during the calendar year.”
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- H.R. 1129 also would provide that employers are exempt from the tax withholding requirements and information reporting requirements for employees who are not subject to income tax.
- Would address both income taxation AND withholding
- Similar legislation introduced previously (H.R. 3359 introduced in 2007, H.R. 2110 introduced in 2009, and H.R. 1864 introduced in 2012.)
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- Proposed Best Practices
  I. Identify states at issue:
     I. Workplace state(s); and
     II. employee locations/resident state(s)
  II. Reciprocity states:
     A. If yes, have all employees complete appropriate forms
     B. If no, consider *de minimus* exceptions
     C. For other states, implement HR policy to track employees
  III. Vote in support of federal legislation
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- Additional Tax Issues
- Unemployment Insurance
  - Nexus threshold
  - Lower than business taxes can be
  - State law “employer”
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- Additional Issues
- Federal Tax: Mobile Workforce Travel Issues
  - Internal Revenue Code Section 162: Travel Expenses “away from home”
  - Tax home
  - Deductibility of travel expenses/income to employee
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- Additional Issues
- International Travel
  - Visa considerations
    - Work location
    - Address
    - Duration
    - Type
    - Does Visa holder have a United States “tax home”?
      - Under State law?