October 31, 2021

Remote Work Arrangements

There has always been a small remote workforce, but, for the past year, the COVID-19 pandemic and the government ordered shutdowns that followed made remote work very common. According to a recent survey by FlexJobs, 65% of remote workers do not want to return to their offices, and many employers are continuing to use a remote work arrangement.

Having an employee working from home in a state where the employer is not headquartered creates several issues: where to withhold state and local income tax, and whether the remote workforce creates nexus such that the employer owes income or franchise tax to the remote state. It may also create tax complexity for remote workers.

Late last year, New Hampshire brought a case against Massachusetts. Massachusetts created a temporary rule in 2020 to tax the income of New Hampshire residents who used to commute but now work from home. In effect, Massachusetts wants to tax income for services performed in another state. Whether the Supreme Court will hear the case remains to be seen. A May 2021 amicus curiae brief filed by the U.S. Solicitor General, which reflects the Biden Administration's position, urged the U.S. Supreme Court not to hear the case. But, a number of states, including Connecticut and New Jersey, filed amicus curiae briefs urging the court to hear the case.

For most federal payroll tax purposes, the location of the employer and employee is irrelevant. Federal income tax withholding applies regardless of their location.

Similarly, the Federal Unemployment Tax Act (FUTA) tax applied regardless of the location of the employer. However, the amount of FUTA tax paid can vary, based upon location; this is because some states are considered "credit reduction states" for FUTA tax purposes, which increases the amount of federal unemployment tax paid by the employer. Although there were no credit reduction states for 2020, there may be several in 2021. Therefore, determining to which states wages are allocated can impact the amount of FUTA taxes due.

Each state has its own rules for income tax withholding (other than Alaska, Florida, Nevada, New Hampshire, South Dakota, Tennessee, Texas, Washington, and Wyoming, where there is no income tax).

Some states such as Massachusetts, Connecticut, and New York, made special income tax withholding rules to address this temporary situation during the COVID-19 pandemic.

Some employees, such as professional athletes, work for short periods in other states and potentially face multiple state and local income taxes. Not only may they have to pay income tax on earnings within the state in which they provide services; they must also pay an allocable portion of all other income. For example, for someone who is not a resident of or domiciled in New York but has New York source income, state income tax is first calculated as if the employee were a full-time resident. Then an allocation is made based on the percentage of New York source income versus federal income.

Payroll tax matters aside, having a remote workforce may subject employers to state and local taxes on a portion of their profits. For example, when and to what extent does New York City ‘s unincorporated business tax (UBT) apply? Having employees in a location creates nexus to a state or locality, which may trigger state income or franchise tax in that location.

If you need advice in this area, please call Melissa Rosenfeld in our office for specific advice tailored to your situation. *The CPA Journal June/July 2021 p.14, 15.*

Temporary NJ COVID-19 Policy on Teleworking Ends

The NJ Division of Taxation temporarily waived the Corporation Business Tax nexus standard that is generally met if an out-of-state corporation has an employee working from home in New Jersey. As long as the out-of-state employer did not otherwise have a physical presence in or economic nexus with New Jersey, the Division did not consider the employer to have nexus for CBT purposes during the waiver period.

This policy ends on September 30, 2021 and unless employees located in NJ are sales employees engaged solely in permitted solicitation activities, those employees could cause a business to be subject to NJ taxation.

Even employers with no receipts apportionable to NJ will be responsible for the CBT minimum tax if they have nexus as the result of a teleworking employee.

An employee working from home in New Jersey will therefore create physical presence and Sales Tax nexus for an out-of-state employer because working at a location in NJ is considered physical presence by the state.

As always, if you have any questions about these or any other matters, do not hesitate to call us.