Crossing US borders
Managing state and local mobile workforce
income tax compliance
As US business travel and nonresident income tax enforcement both continue to increase, employers are no longer asking if they should comply, but how.
Foreword

Nonresident income tax is a substantial and increasing source of governmental revenue

Nonresident income tax withholding compliance is now a boardroom concern

15 factors increasing the chances of income tax withholding assessments

What are the risks of failing to withhold nonresident income tax?

Ten frequently misunderstood facts about income withholding for the US mobile workforce

1. Short-term assignments aren't necessarily disregarded for nonresident income tax purposes.
2. The Connecticut and New York 14-day rule doesn't extend to employees' personal income tax obligations.
3. Nonresident income tax exclusions under reciprocal agreements are not necessarily automatic.
4. Employers are responsible for knowing when a work assignment triggers a nonresident income tax withholding obligation.
5. Employee work at home can trigger nexus.
6. Teleworkers' wages may create an income tax withholding requirement in the corporate office state.
7. Federal treaty exemptions don't necessarily apply at the state and local level.
8. Resident income tax may continue to apply even after the employee moves to another state.
9. Computation of income tax varies when employees work partly in and outside of the state.
10. Federal law prohibits nonresident income tax for certain industries and payments.

Legislative trends in US mobile workforce income tax

Summary

Are you on board?

How well are you performing in the compliance continuum?

How we can help

You can read this report online at www.ey.com/us/getonboard.
In 2005, we issued a special report, *Crossing the line: myths, facts and the latest trends in nonresident withholding*, in response to how New York deployed an Technology Assist Audit (TAA) for nonresident income tax withholding capable of casting a broad enforcement net across the US.

A decade later, we now find ourselves at a pivotal point in history.

As US business travel and nonresident income tax enforcement both continue to increase, businesses are no longer asking if they should comply, but how. While many taxing authorities have fine-tuned their income tax guidance and audit guidelines, there’s been little relief from the complexity or burden faced by employers and their short-term business travelers. These circumstances fueled the start of a tax reform movement that began in 2008 with Pennsylvania’s adoption of Act 32 to streamline local taxes; and in 2009 when the proposed federal Mobile Workforce State Income Tax Simplification Act was first introduced.

In this report, we analyze the many recent developments affecting mobile workforce income tax compliance and provide insights for managing and helping to mitigate risk.

To complement this report, we joined Bloomberg BNA on June 10, 2015, in releasing our first comprehensive US mobile workforce income tax compliance survey. Survey results will assist businesses in benchmarking their policies and procedures for US income tax withholding with others in their industry. For more information please go to www.ey.com/us/getonboard.

Sincerely,

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Not only do businesses remit personal income taxes throughout the year to taxing authorities, but in meeting their Form W-2 reporting requirements, they assist taxing authorities in identifying nonresidents who have failed to file income tax returns and to pay any additional tax owed.

Employers are generally required to withhold resident and nonresident income taxes from wages, and they are vital to the tax revenue collection and enforcement process.

Nonresident income tax is a substantial and increasing source of governmental revenue
Nonresident income tax is a substantial and increasing source of governmental revenue

Despite significant advances in telecommunications, there’s been no slowdown in US business travel. According to the Global Business Travel Association (GBTA), an estimated 492.1 million US business trips are expected to take place in 2015, an increase of 1.7% over 2014. This is encouraging news for the travel industry as well as state and local jurisdictions that collect taxes from income generated by nonresident business travelers.

A US employee is potentially subject to state (and local) income tax on all wages in the resident location and on any wages sourced to a nonresident work location. A credit for nonresident income tax is often allowed against the resident income tax. Thus, when the system works to avoid double taxation, this may be a mere tax swap for employees, but it can be an important trade for nonresident jurisdictions. For instance, a state stands to profit from its nonresident income tax collections when:

1. It has a high volume of nonresident traffic (e.g., California and New York).
2. The business traveler pays no income tax in the resident location (e.g., Texas and Florida).
3. The nonresident income tax rate is higher than the resident tax, which is likely in states with the highest US personal income tax rates (e.g., California, New York, Minnesota and Oregon).

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Which states have the most to gain from nonresident income tax enforcement?

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Employers are generally required to withhold resident and nonresident income taxes from wages, and they are vital to the tax revenue collection and enforcement process. In tax year 2014, for instance, the New York Department of Taxation and Finance reported net personal income tax collections of $43 billion, of which $33 billion, or 77%, was obtained from employers through the wage withholding process.

Today’s enforcement landscape has changed dramatically by a rise in the consequences, materiality and risks of failing to meet income tax withholding requirements. Once a footnote in payroll discussions, nonresident tax compliance has made headlines and reached boardrooms.
Nonresident income tax withholding compliance is now a boardroom concern

Embroided in meeting a litany of employment-related mandates, companies once found it all too easy to ignore the meekly expressed concerns of accountants and payroll supervisors that employees working outside of their resident or primary work location jurisdictions might be subject to nonresident state and local income tax. This former attitude of complacency was primarily fueled by the simple fact that there was little consequence for overlooking nonresident withholding tax requirements. Withholding tax audits were rare, industry-specific and generally involved only athletes, entertainers and consultants. When balancing business risk with the expense of compliance, it seemed prudent to conclude that attention in this area wasn’t warranted merely because a handful of Texas employees were assisting oil crews in Louisiana or a Florida executive was taking infrequent trips to New York for stockholder meetings.

Tipping the scales – the advent of withholding tax audits

Without technology, revenue agents did not have the time or tools to identify potential non-filers and sift through the volume of data and paper files needed to support worthwhile audit findings. Put simply, tax collectors were hampered by the proverbial tail wagging the dog – insufficient revenue to devote to revenue-generating audits. Sadly for businesses, that dog has found its tail.

The New York Department of Taxation was the pioneer of the Technology Assisted Audit (TAA) withholding tax audit, followed in 2009 by the Connecticut Department of Revenue Services. Incorporating the use of technology in its payroll data analysis, New York has been able to conduct hundreds of substantial withholding tax audits each year and collect from businesses millions in underwithheld tax liabilities, penalties and interest. By requiring that businesses supply electronic files that include work state, resident state, percent of time worked in the state (or its localities, if applicable), and federal and state Form W-2 and W-4 data, jurisdictions like New York and Connecticut with electronic audit capabilities can efficiently make assertions concerning nonresidents for whom the employer has allegedly not reported wages or withheld the correct amount of state (and local) income taxes.

The proliferation and impact of their withholding tax audits in the past few years has been so sweeping that both New York and Connecticut have agreed that when auditing businesses, they will no longer impose nonresident income tax withholding assessments for the population of employees with primary work locations outside of their state and who reasonably expect to work fewer than 14 days in the state in a calendar year.3

Modifications in the Form W-2 reporting requirements over the years (Box 12, codes V, Y and Z) and the more recent IRS requirements for statutory stock option reporting (Forms 3921 and 3922) have made it far easier for state and local taxing jurisdictions to identify underwithholding errors connected to what are frequently material items of compensation.

Joining Connecticut and New York are those states that aggressively monitor long-term deferrals (also known as “trailing compensation”), such as nonqualified deferred compensation and stock options, and assert at the time of distribution that a portion of the income was earned in the state and subject to its income tax withholding requirements.4

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The results of these trends, together with an increased focus on the accurate reporting of contingent tax liabilities on financial statements (i.e., FAS 5)5, have made nonresident withholding compliance a corporate executive hot topic. More than ever before, company decision makers are inquiring about their short-term business traveler tax compliance policies and are directing their staff to begin the process of closing compliance gaps.

Today’s enforcement landscape has changed dramatically by a rise in the consequences, materiality and risks of failing to meet income tax withholding requirements. Once a footnote in payroll discussions, nonresident tax compliance has made headlines and reached boardrooms.

4. For example, see California Audit Guidelines
Top 15 income tax withholding audit flags

1. The state(s) where employees perform services is actively engaged in withholding tax audits.
2. Vehicles or equipment that prominently display the company’s name and/or logo are frequently present in the jurisdiction.
3. Officers and highly paid employees frequently perform services in a particular state, and/or their presence in the state is easily documented or otherwise well-known. For example, public records reflect an upcoming acquisition, purchase or stockholder meeting.
4. Sales and use taxes are paid to the state but not income tax withholding.
5. Wages are reported on Form W-2 to the state, but no local wages are reported.
6. Expense reports show reimbursement for travel to other states and localities.
7. Accounts payable records show travel, relocation or other “out-of-state” related costs paid on behalf of employees.
8. A parent operates a subsidiary in one or more states other than the state of the parent company.
9. The company holds a corporate lease or otherwise owns property in the jurisdiction for use by its employees.
10. Employees own or lease residential property, hold driver’s licenses or are registered to vote in a state other than the resident state shown on the Form W-2 or Form W-4.
11. Unemployment insurance is paid to the state but not income tax withholding.
12. Wage and tax adjustments were filed with one taxing jurisdiction and not another. Keep in mind that the IRS has an agreement with a number of states to share tax audit findings. (See California Information sheet DE231TA, Employment Tax Audit Process.)
13. Accounting records reflect a tax reserve for contingent liabilities connected with underreported wages and related income taxes.
14. The company is under contract with the state or municipality to provide goods or services.
15. Independent contractors are substantially used in a state, irrespective of whether the company is deemed to be doing business in that jurisdiction.
What are the risks of failing to withhold nonresident income tax?

In formulating the business case for compliance with nonresident income tax withholding and reporting requirements, businesses should consider these risks:

- **Withholding tax liability**
- **Penalties, interest and criminal charges**
- **Officer personal liability**
- **Employee audits and assessments**
- **Loss of business license**
- **Loss of reputation**

**Increasing consequences**
noncompliance risks to consider

**Withholding tax liability** | The most significant portion of cost associated with an audit is the income tax an employer fails to withhold. Without exception, taxing jurisdictions hold the employer liable for 100% of the income tax withholding shortage. Some or all of this liability may be abated where the employer is able to obtain signed affidavits from employees similar to IRS Form 4669, wherein employees state that they have reported the wages on their income tax return and paid the applicable tax. For instance, Form DE938P is used for California personal income tax withholding. (California Personal Income Tax Audit Adjustment Process)

Frequently, employers will be unable to obtain such affidavits because employees are not likely to report income that isn’t included in taxable wages on the Form W-2 in Box 16.

**Penalties, interest and criminal charges** | Penalties can be assessed for underwithholding of tax, failure to timely pay tax, failure to file correct and timely withholding tax returns, and, where applicable, failure to file a state/local Form W-2. In addition, and depending on the facts and circumstances, taxing authorities may also impose higher negligence or intentional-disregard penalties and, in certain extreme circumstances, criminal charges.

Some states may impose higher assessments for errors discovered through audit, further increasing the financial consequences of not voluntarily disclosing income tax withholding errors.

**Officer personal liability** | Personal liability may attach to the “responsible persons” of the business. For instance, Maryland holds the officer of the corporation who exercises direct control over its fiscal management personally liable for withholding, penalties and interest.

For this reason, taxing authorities frequently require the names and Social Security Numbers of persons in the business responsible for the payment of taxes. (See California here.)

**Employee audits and assessments** | In order to maintain good relations with their employees, many businesses will accept responsibility for the tax assessments that may be made against their individual employees for failure to file a nonresident state or local personal income tax return. These assessments include penalty, interest and the current taxes owed on the “gross-up.” Needless to say, an individual audit of an officer or highly paid employee might also result in additional assessments due to other source income, such as personal property, within the state.

**Loss of business license** | To add more teeth to the withholding tax requirements, other sanctions may also apply. Maryland, for instance, has the right to suspend or revoke any Maryland-issued business license of a taxpayer failing to withhold Maryland state income tax. (Md. Code Ann., Tax-Gen. § 13-707(a).)

Government contractors may be barred from doing business with the jurisdiction or existing contracts may be terminated for taxpayer noncompliance and the resulting outstanding tax debts. (Federal Acquisition Regulation (FAR) 52.209-5; Los Angeles Ordinance 173677, Article 14.)

**Loss of reputation** | The greatest risk is to the company’s brand. Negative press can travel fast if it involves a large number of employees, jurisdictions or a large amount of dollars. Reputation is so vital to a business, in fact, that Maryland uses it as leverage to discourage tax delinquency in its “Caught in the Web” policy.

In formulating the business case for compliance with nonresident income tax withholding and reporting requirements, businesses should consider these risks.
The risk of a nonresident income tax audit is on the rise, in the US and across the globe.
Nonresident income tax withholding compliance is now a boardroom concern.
US state and local income tax withholding rules can vary significantly across jurisdictions. Consequently, misunderstandings, rather than intentional disregard, account for many withholding errors.
Ten frequently misunderstood facts about income withholding for the US mobile workforce

US state and local income tax withholding rules can vary significantly across jurisdictions. Consequently, misunderstandings, rather than intentional disregard, account for many withholding errors. If your employees travel for work or work primarily from their homes, here are 10 facts to consider.

01 Short-term assignments aren’t necessarily disregarded for nonresident income tax purposes.

Some companies believe that if employees spend only a few days attending meetings or performing services in another state, their wages are exempt from nonresident income tax withholding. The fact is, states and localities differ in terms of what may constitute an exempt activity (e.g., activities incidental to the main job) and the time or wages (de minimis employment) that may be disregarded for income tax withholding purposes.

23 states with de minimis nonresident income tax exemptions

Note that Colorado requires a written request for waiver for short-term assignments.

» Exempt occasional duties. Some jurisdictions specifically exempt from nonresident income tax wages paid to employees who are present in the state to perform occasional duties that are incidental to the employee’s out-of-state job duties. Massachusetts, for instance, exempts from nonresident income tax items that are casual, isolated and inconsequential to the nonresident’s primary business or employment duties performed at a base of operations outside of Massachusetts (i.e., occasional presence for management reporting or planning, training, attendance at conferences/symposia). Philadelphia provides a similar exemption for local income tax purposes.7

» De minimis employment. Of the states that impose an income tax on wages, 23 of them exempt wages from nonresident income tax withholding if the tax liability is below a threshold or the time working in the state is de minimis

6. 830 CMR 62.5A.1(3h).

Note that Colorado requires a written request for waiver for short-term assignments.
The de minimis threshold at which nonresident income tax withholding applies may be based on income derived while working in the state during the year (e.g., for Idaho, less than $1,000 in a calendar year), or the number of days present in the state, or a combination of both. The “days threshold” ranges from 12 (e.g., Maine) to 60 (e.g., Hawaii).

Outside of these 22 states, and with limited exceptions, all covered wages derived from employment in a nonresident state are generally subject to the state’s personal income tax and withholding requirements.

**02 The Connecticut and New York 14-day rules don’t extend to employees’ personal income tax obligations**

Like Connecticut and New York, which, in audit, excuse employers from withholding nonresident income tax for employees working in the state 14 or fewer days in the year, the de minimis state exception to nonresident income tax does not necessarily apply to the individual. This is an important distinction, because where personal income tax continues to apply (i.e., Connecticut and New York), employees are required to file a nonresident individual income tax return and to pay any tax due, even though the employer did not withhold under the 14-day safe harbor.

Consequently, the 14-day rule of Connecticut and New York should be viewed as merely a withholding tax audit safety net. In fact, both states require the reporting of nonresident state wages attributable to services rendered in their states in Box 16 of Form W-2 regardless of whether state income tax is required to be withheld.

**03 Nonresident income tax exclusions under state reciprocal agreements are not necessarily automatic**

A number of states, particularly those that share borders, maintain reciprocal agreements with each other that exempt nonresidents of states covered by the agreement from their income tax and withholding requirements.

For example, all employees performing services within Ohio are subject to Ohio state income tax unless they are residents of states having a reciprocal agreement with Ohio. Those states are Michigan, Indiana, Kentucky, West Virginia and Pennsylvania.

**States with reciprocal income tax agreements**

- District of Columbia
- Montana
- Illinois
- New Jersey
- Indiana
- North Dakota
- Iowa
- Ohio
- Kentucky
- Pennsylvania
- Maryland
- Virginia
- Michigan
- West Virginia
- Minnesota
- Wisconsin

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8. [36 Me. Rev. Stat. §5142, sub-§8-B](#); Maine nonresident income tax withholding is also not required on wages earned of $3,000 or less.

9. [Haw. Admin. Rules §18-235-61-04(b)](#).

10. Note that in addition to New York’s 14-day rule, if a nonresident employee works for only a short period of time within New York and it is reasonably expected that the total wages of such nonresident will not exceed such employee’s personal exemptions, the employer need not withhold or deduct any amount of New York personal income tax from the employee’s wages until the aggregate amount paid exceeds the employee’s personal exemptions. ([20 NYCRR 171.6(b)(4)](#).

11. Connecticut, AN 2010(3); New York, TSB-M-12C5.

12. Connecticut, AN 2010(3); New York, TSB-M-12C5.
But here's the catch. An exemption under a state reciprocal agreement generally does not apply unless the nonresident employee has completed a reciprocal agreement form. For instance, residents of Michigan, Indiana, Kentucky, West Virginia and Pennsylvania are exempt from Ohio nonresident tax only if they have completed and submitted to their employer Form IT 4NR, Employee’s Statement of Residency in a Reciprocity State.

All too often employers neglect to obtain the necessary reciprocal agreement form from employees, leaving them exposed to withholding tax assessments despite the existence of the reciprocal agreement.

**04 Employers are responsible for knowing when a work assignment triggers a nonresident income tax withholding obligation**

The state usually places some, if not all, responsibility on the employer to have knowledge of an employee’s work in a nonresident state. Even in those states that require nonresidents to estimate the percentage of time they will perform nonresident services, the employer is nonetheless expected to determine the reasonableness of the employee’s assertions.

For example, nonresident employees of New York are encouraged to estimate the percentage of wages allocable to New York on Form IT-2104.1, Certificate of Nonresidence, especially if other “adequate records” are not available. The employer is responsible for determining if the assertions made on Form IT-2104.1 are reasonable based on the facts and circumstances of such employee. One example of demonstrating the reasonableness of the employee’s assertions is review and approval of the form by the employee’s immediate supervisor or, alternatively, the allocation percentage is based on actual days in New York as recorded by an employer’s time and attendance system.13

Further, New York has stated that an employer may not rely on the Form IT-2104.1 if it has actual knowledge or reason to know that the form is incorrect. An employer reimbursing an employee for travel expenses to New York is deemed to have actual knowledge or reason to know the Form IT-2104.1 is incorrect if the day count in New York based on expenses is greater than the estimate on the form.

In contrast, Mississippi regulations place all the burden for determining the percentage of time worked in the state on the employer. There is no form comparable to the Form IT-2104.1 for an employee to estimate the percentage of nonresident wages allocable to the state.14

**05 Employee work at home can trigger nexus**

Technology advances have made it possible for employees to take direction and control from business locations that are hundreds or even thousands of miles away. Due to real estate costs, concern for fuel emissions and energy conservation, and efforts to create a flexible work environment, businesses are increasingly adopting telecommuter policies. According to GlobalWorkplaceAnalytics.com, telecommuting increased 79.7% from 2005 to 2012.

Most states contend that when work is primarily performed from an employee’s home, the employee’s home is a regular place of business. Accordingly, state resident income tax withholding and other employment and business taxes (e.g., unemployment insurance and sales/use tax) apply in the state of the employee’s home.15

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Some employers are faced with a more difficult dilemma when it comes to telecommuters. A handful of states, including New York, assert that work performed in another state by a telecommuter for a New York employer is considered work performed in New York unless the work was performed outside of New York for “the necessity of the employer and not for the mere convenience of the employee.”

In November 2003, a court upheld the New York Department of Taxation and Finance’s position that a resident of Connecticut spending part of his time teaching at a New York City law school was required to pay New York state income tax on 100% of his earnings.16 In another case, a Tennessee telecommuter spending 25% of his time in New York was also required to pay New York state income tax on 100% of his earnings.17

Because of the double taxation that potentially arises from the “convenience of the employee rule,” legislation has been repeatedly proposed to prohibit it, most recently in 2014.18

If an income tax treaty applies, a US nonresident alien eligible under that treaty claims exemption from federal income tax withholding by submitting to the employer Form 8233, Exemption From Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual.

Numerous state and local taxing authorities require income tax and withholding on the portion of trailing compensation that was earned within the jurisdiction regardless of where the employee lives or works when it is paid. Apportionment rules can vary by jurisdiction and type of wage payment.

Trailing compensation rules can also vary between the state and its localities. For instance, in 2014, the Indiana Department of Revenue ruled that state income tax and withholding, but not county income tax, applies to bonuses that are earned within the state but paid to employees who no longer reside in the state.21

Compare Indiana’s county tax rules for trailing compensation paid to nonresidents to New York’s local tax requirements. Income tax withholding isn’t required by New York City but is required by Yonkers.22 (See NY Pub. NYS-50.)

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19. California Information Sheet 231TE, Types of Employment (p. 9); 20 NYCRR § 171.3.
20. Pennsylvania REV-415; Local Tax Enabling Act; Sterling Act; City of Philadelphia Income Tax Regulations, Article II, Section 209.
### US income tax treaties

- Armenia
- Australia
- Austria
- Azerbaijan
- Bangladesh
- Barbados
- Belarus
- Belgium
- Bulgaria
- Canada
- China
- Cyprus
- Czech Republic
- Denmark
- Egypt
- Estonia
- Finland
- France
- Georgia
- Germany
- Greece
- Hungary
- Iceland
- India
- Indonesia
- Ireland
- Israel
- Italy
- Jamaica
- Japan
- Kazakhstan
- Korea
- Kyrgyzstan
- Latvia
- Lithuania
- Luxembourg
- Malta
- Mexico
- Moldova
- Morocco
- Netherlands
- New Zealand
- Norway
- Pakistan
- Philippines
- Poland
- Portugal
- Romania
- Russia
- Slovak Republic
- Slovenia
- South Africa
- Spain
- Sri Lanka
- Sweden
- Switzerland
- Tajikistan
- Thailand
- Trinidad
- Tunisia
- Turkey
- Turkmenistan
- Uzbekistan
- Venezuela

US income treaties are available [here](#).
Numerous state and local taxing authorities require income tax and withholding on the portion of trailing compensation that was earned within the jurisdiction, regardless of the employee’s location at the time of payment.
As previously explained, a credit can generally be claimed against resident state income for nonresident income tax paid to other states; however, local jurisdictions frequently don’t allow for this credit.23

It is frequently assumed that employers always first withhold nonresident income tax and then the portion of resident income tax withholding, if any, that exceeds the nonresident income tax. This is not always the case. Wisconsin, for instance, requires no resident income tax withholding on wages sourced to Minnesota.24 In Alabama, resident income isn’t required for wages earned outside the state unless there is no income tax withholding in the nonresident work state (e.g., Florida and Texas).25

At various times, federal legislation has been enacted to limit a state’s ability to impose income tax on out-of-state employees under specific circumstances.

Here are some of these laws:

- **Pension plans.** In 1996, federal legislation under P.L. 104-95 (codified in 4 U.S.C. § 114) was enacted to prevent states from taxing certain pension income (e.g., qualified retirement income and certain nonqualified deferred compensation) earned while working there but paid or distributed after the employee leaves the state.

- **Interstate Income Act of 1959.** P.L. 86-272 prohibits a state from imposing income tax pursuant to activities constituting solicitation of orders for sales of tangible personal property when orders are filled or shipped outside of the state.

- **Interstate transportation.** Motor carriers (49 USC § 14503(a)), rail carriers (49 USC § 11502), water carriers (49 USC § 14503(b)(2)), air carriers (49 USC § 40116(f)(2)).

- **Military Spouse Residency Relief Act.** See more here.

Before assuming that wages are excluded from state nonresident income tax under federal law, employers should carefully review the state laws and regulations that govern how they are applied.

For instance, in 2014, the Illinois Department of Revenue held that Illinois nonresident income tax withholding is not required if the services employees perform in Illinois are merely incidental to the services they perform outside of the state, their base of operations is outside of the state, and their services within the state are protected from nonresident income tax under the federal Motor Carrier Act.

The Department held that Illinois income tax withholding is not required if the service that the employee performs qualifies for protection under federal law pursuant to Department Regulations § 100.2590(a). In the alternative, the exemption under federal law does not apply if the service the employee performs in Illinois is more than merely incidental to the services performed outside of Illinois or if the employee’s base of operations is within Illinois.26

Computation of income tax varies when employees work partly in and outside of the state

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The uptick in tax audits is certainly increasing compliance while at the same time fueling litigation and a movement for tax reform.
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At the behest of employers and mobile employees burdened by multiple and inconsistent state income tax laws, interest groups such as the Council on State Taxation (COST) and the American Institute of Certified Public Accountants (AICPA) have championed passage of a federal law restricting a state’s ability to impose nonresident income tax under the Mobile Workforce State Income Tax Simplification Act.

In 2011, the Multistate Tax Commission (MTC) also adopted Model Mobile Workforce Statute (MMWS) for adoption by compact member states to simplify nonresident income tax withholding for mobile employees.

Some states too have recently taken initiative to provide relief for short-term business travelers, in particular, for those who enter the state in support of disaster relief and recovery efforts.

Local income taxes have thus far benefited most from the push for tax relief and uniformity, a trend that is likely to continue thanks to the 2015 US Supreme Court decision involving Maryland’s county income tax scheme.27

Model Mobile Workforce Statute (MMWS). The MMWS differs from proposed federal legislation in a number of ways, most notably in the de minimis threshold. MMWS uses 20 days as the threshold at which nonresident income tax would apply, as compared to 30 days under the proposed Mobile Workforce State Income Tax Simplification Act. Other differences are highlighted in the chart on page 26.

The MMWS is the result of input provided by five states (Idaho, Colorado, Montana, New York and California) and feedback from state and taxpayer representatives, including the Council on State Taxation and the Federation of Tax Administrators (FTA).28

Since its adoption in 2011, only one state, North Dakota (effective January 1, 2013) has enacted this model law. Legislation was introduced in 2013 (HB 1143) to adopt the law in Colorado, but it failed to pass.

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Where US state and local taxes apply

Source: Tax Foundation

Figure 1

Differences in proposed Mobile Workforce State Income Tax Simplification Act and Model Mobile Workforce Statute

<table>
<thead>
<tr>
<th>Provision</th>
<th>Mobile Workforce State Income Tax Simplification Act</th>
<th>Model Mobile Workforce Statute</th>
</tr>
</thead>
<tbody>
<tr>
<td>Days constituting de minimis</td>
<td>30</td>
<td>20</td>
</tr>
<tr>
<td>Definition of “day” in nonresident state</td>
<td>Where most time is spent</td>
<td>Any part of day, regardless of multiple state assignments</td>
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<tr>
<td>Travel through the state purely for travel</td>
<td>Not counted in threshold</td>
<td>Any transit time in state not considered in determining work location</td>
</tr>
<tr>
<td>Work for more than one related employer</td>
<td>No specific provision</td>
<td>Days are aggregated in determining if threshold is reached</td>
</tr>
<tr>
<td>Income threshold</td>
<td>No provision</td>
<td>De minimis threshold doesn’t apply to key employees (50 highest-paid officers)</td>
</tr>
<tr>
<td>Workers not covered by the de minimis rule</td>
<td>Professional athletes, professional entertainers, certain public figures (persons of prominence)</td>
<td>Professional athletes, professional entertainers, persons of prominence, construction workers, top highest-paid officers</td>
</tr>
</tbody>
</table>
Nonresident income tax relief for disaster-related services.  
In a trend started by Maine in 2012,²⁹ more states are enacting legislation that excludes wages from nonresident income tax if connected with temporary disaster-related services.

From January 1, 2015 to May 1, 2015, several states enacted legislation with substantially similar provisions for this purpose (Arkansas, Kansas, Mississippi, Oklahoma and Virginia). These states, in addition to relieving qualified businesses from other fees and business taxes, exempt qualified employer and employees from nonresident income tax/withholding and related returns and information statements. This relief from nonresident income tax is generally available for 60 days and applies to disaster-related or emergency-related work that includes repairing, renovating, installing, building and rendering services or other business activities relating to critical infrastructure that has been damaged, impaired or destroyed by a declared state disaster or emergency.

Local income tax simplification. Local jurisdictions have clearly made the most significant inroads in simplifying income tax for the mobile workforce, as shown in the timeline beginning on page 28.
Leading the trend to simplify local income tax compliance was Pennsylvania, which, after four years of effort, enacted sweeping changes to its Local Tax Enabling Act under Act 32 of 2008. Effective in 2012, Act 32 transferred the administration of the Earned Income Tax (EIT) collection system from 519 municipalities and school districts to a much smaller system that as of May 1, 2015, is managed by just 69 county-level Tax Collection Districts (TCDs) supported by only 19 Tax Officers.

Under the direction of the Pennsylvania Department of Community and Economic Development (DCED), PA Act 32 has also streamlined how the local Earned Income Tax is applied to short-term business travelers. Instead of a patchwork of EIT municipal codes governing de minimis exclusions from nonresident income tax, the DCED provides uniform guidelines, including a safe harbor allowing employers with multiple work locations within the state to source the income of floating employees to a central Pennsylvania EIT work location.

On December 19, 2014, Ohio Governor John Kasich signed into law Sub. H.B. 5, which simplifies employer local income tax withholding, remittance and return filings, effective January 1, 2016. Of significance to short-term business travelers, the law increases the de minimis threshold at which nonresident income tax can be imposed from 12 to 20 days.

Starting in 2016, employers are not required to withhold income tax from compensation paid to a nonresident employee who works 20 or fewer days in another municipality, but they are required to withhold income tax for the municipality in which the employee’s principal place of work is located. Once an employee’s time in the municipality exceeds 20 days, the employer is required to withhold on compensation earned from the 21st day forward. Limiting the benefit of the law to Ohio entrants, the 20-day safe harbor generally applies only to employers that have offices or operations in Ohio.
Effective in 2017, Indiana legislation under HB 1485 (Public Law 243) consolidates local income taxes into a single income tax rate per county. Currently, there are three basic local income tax types – Country Adjusted Gross Income Tax (CAGIT), County Option Income Tax (COIT) and County Economic Development Income Tax (CEDIT) – and a country can adopt a combination of no more than two of these basic tax types.

Unfortunately, the law forces a trade of simplicity for higher nonresident income tax; namely, HB 1485 requires counties to impose the county income tax rate equally on resident and nonresident local taxpayers. As a result, most nonresident county taxpayers will be taxed at a higher rate than under the current statute, increasing statewide local income tax revenue by an estimated $22 million in its first year of implementation (2017).

In 2015, the US Supreme Court handed down a long-awaited decision that Maryland’s personal income tax scheme that denies a local income credit for taxes paid to other states is unconstitutional.32

The anticipated impact of this decision is that other local taxing jurisdictions that don’t currently allow a resident income tax credit for taxes paid in other states (e.g., New York City and Philadelphia)33 will eventually be compelled to do so, giving some relief from local taxation to the US mobile workforce.

33. See the City of Philadelphia website.
Summary

Passage of federal legislation restricting states’ rights to impose nonresident income tax isn’t impossible; there are a number of such pre-emptive laws already on the books (see page 23). However, to become reality, mobile workforce income tax simplification will need to overcome significant hurdles.

One challenge facing the proposed Mobile Workforce State Income Tax Simplification Act is disagreement among policy influencers. In June 2012, for instance, the FTA withheld its support of the House-passed bill, a move that may have contributed to stopping the legislation in its tracks in the 112th Congress. The FTA stated that the legislation “represents a substantial preemption and intrusion into state tax authority” and that a “simple days threshold will expose some jurisdictions to substantial revenue disruptions.” In summary, the FTA revoked its support of federal legislation in favor of state voluntary adoption of a model uniform statute.35

Of greater importance, the proposed federal legislation lacks political backing from states like California and New York that have high tax rates and substantial nonresident business traffic. Gathering enough support to overcome geographical opposition will require attention and negotiation.

With election year around the corner and a broader electorate base to consider, it’s uncertain if lawmakers are willing to invest the political capital needed to pass the Mobile Workforce State Income Tax Simplification Act in the 114th Congress.

In the near future, substantial benefits of the mobile workforce income tax simplification reform movement will likely reach only to local taxpayers thanks to pioneering states like Pennsylvania and the 2015 landmark decision of the US Supreme Court in Wynne (Comptroller of the Treasury of Maryland v. Wynne, Dkt. No. 13-485, May 18, 20).

Enforcement of employers’ state and local withholding and reporting obligations continues to be aggressive, with no substantial legislative relief in sight in the foreseeable future.

At least for now, businesses with employees working in more than one state need to continue to be vigilant in meeting their nonresident income tax withholding and information reporting requirements, keeping in mind that currently only 23 states waive their nonresident income tax requirements based on de minimis earnings and/or time spent in the state.

Careful monitoring of state and local income tax developments will be important in this dynamic and evolutionary period of mobile workforce income tax reform.

35. FTA Resolution 2012-2.
Are you on board?

Are you perpetually tracking employee movement and meeting the related wage tax liabilities across national, state and local borders?

When employees receive compensation for services provided in prior years, do you consider potential tax liabilities for the states/cities of employment during the period earned?

Is your mobile workforce tax policy addressing your compliance and governance requirements?

Are employees familiar with your mobile workforce tax policy, and do you provide them with resources to address their questions and concerns?

For employees routinely living and working in different jurisdictions, do you have a system for apportioning wages and timely withholding taxes?

If your tax processes are not optimal, have you quantified the risks?

See how we're helping businesses get on board.
http://www.ey.com/us/getonboard
How well are you performing in the compliance continuum?

1 - High risk
2 - Medium high risk
3 - Medium risk
4 - Low or no risk

Rank your performance overall and in each of these five phases of mobile workforce income tax compliance.
How we can help
Short-Term Business Traveler (STBT) Services

**EY Travel Risk and Compliance**
**EY TRAC**
Helps organizations monitor and assess their STBT risk in real time for tax and immigration in more than 100 countries (and their local jurisdictions).

**EY TRACER**
A smartphone application that allows employees to track their location by picking up the GPS signal on their cell phones.

**EY Calendar**
Used in conjunction with EY TRACER, assists employees and their employers in tracking work locations by day and year.

**STBT Policy and Design**
We help businesses design and implement an STBT program tailored specifically to their organizational culture and applicable governance requirements.

**Tax Compliance & Advisory**
We assist businesses in accessing their business and employer tax risks for federal, state and local taxing authorities and in meeting their compliance and controversy requirements.

**Immigration Compliance & Advisory**
We have the largest network of immigration practitioners in the world to ensure businesses and their employees receive accurate and reliable immigration services in real time.

Local focus. Global perspective
**Ernst & Young LLP Short-Term Business Traveler (STBT) Services contacts**

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