



# Issue Brief

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## Don't Let COVID Remote Work Become a Tax Trap

As the coronavirus pandemic continues to rage across the country, many Americans are moving from working in their normal offices to makeshift home offices, whether it be at their own houses or those of friends and family. But the complications this invites go beyond just coping with the quirks of teleconferencing or stir-crazy children — absent state action or federal pre-emption, it could mean tax complications that individuals and their employers may not even understand.

An individual whose office is located in a different state than the home in which they are waiting out the pandemic (or businesses whose employees fall under this category) may be unwittingly creating the “nexus,” or sufficient connection to justify tax authority, that states need to pursue additional revenue. Should states pursue these taxes, it could create tax filing headaches for individuals and for businesses at a time when taxpayers need relief.

Doing so would run directly counter to the goal of easing tax obligations during this time of crisis. Every [state](#) and the [federal government](#) has acted to delay the deadlines for tax filing and payment in recognition of the fact that most taxpayers have greater worries at the moment than filing taxes.<sup>1</sup> Rigidly enforcing new tax obligations as a result of remote work makes little sense in this context.

<sup>1</sup> “Which States Have Delayed Tax Payments or Filings?,” National Taxpayers Union Foundation, April 15, 2020. Retrieved from: <https://www.ntu.org/foundation/detail/which-states-have-delayed-tax-payments-or-filings>; and Kaeding, Nicole. “Congress Needs To Step In To Delay Tax Filing, Not Just Tax Payments.” National Taxpayers Union, March 18, 2020. Retrieved from: <https://www.ntu.org/foundation/detail/congress-needs-to-step-in-to-delay-tax-filing-not-just-tax-payments>.

### Key Facts:



The number of Americans working remotely has increased drastically over the past few weeks as a result of the COVID-19 pandemic.



Many of these workers and the businesses that employ them may be unaware of, or unprepared to deal with, the exposure to new tax jurisdictions this can create.



To ensure that Americans are not saddled with new tax obligations from remote work arising out of state-mandated business closures, Congress and state governments should act to treat all remote work performed during the COVID-19 crisis as in-office work for tax purposes.

As of this writing, just six states (Mississippi, New Jersey, Minnesota, North Dakota, Indiana and Pennsylvania) and the District of Columbia have confirmed that they will treat coronavirus-related remote work as normal in-office work for tax filing purposes. It's a positive sign that some states are cognizant of the challenges remote work nexus poses in this context, but the need for broader federal action or, failing that, additional state forbearance is clear.

After all, the scale of remote work has exploded since the beginning of the pandemic. A recent MIT study conducted from April 1-5 found that [34.1 percent](#) of the American workforce, or roughly 56 million Americans, have shifted from commuting to remote work since the pandemic began.<sup>2</sup> As data from the last census estimates that [3.8 percent](#) of Americans regularly commute across state lines, this would mean more than 2.1 million Americans potentially being exposed to new tax filing and payment obligations absent action to protect them.<sup>3</sup>

Even this is likely a conservative estimate, as it does not include Americans doing partial remote work, or those that will switch to remote work by the time the pandemic runs its course.

## **Individual Filers**

In general, taxpayers are required to pay income taxes to the state in which they work or earn their income, not their home state, though they then must submit a tax return to their home state too. Individuals who travel frequently and for extended periods for work also must deal with the complicated rules for cross-border income taxes, as some states begin imposing taxes on individuals who work there for just a single day.

There are some exceptions to these broad rules. Some states, such as Maryland, Virginia, and the District of Columbia, have reciprocity agreements, where individuals pay taxes in their home state, not their working location state. Other areas with frequent cross-border activity don't, such as New York, Connecticut, and New Jersey. Some states are more aggressive in their thresholds for cross-border activity, seeking to enforce income tax obligations for even one day of work performed in the state.

New York, for example, is famous for its persistent auditing of business travelers. It also imposes onerous rules on remote workers through its "convenience of the employer rule." According to [New York's Department of Revenue](#), remote workers whose job could have been completed in New York must still pay New York income taxes, even if they live in Connecticut or another state.<sup>4</sup> Arkansas, among other states, has adopted a similar rule to try and capture more out-of-state revenue.

With the dramatic expansion of teleworking due to the COVID-19 crisis, many more Americans could be caught in this tangled web of tax compliance. Determining the allocation of income taxes could create tax headaches. Absent some action to protect them, taxpayers working from home for the first time would be responsible for tracking days worked in their traditional office and days worked in their home when filing their 2020 taxes. Even for taxpayers who are aware of this obligation, this is likely low on the list of priorities in such a fluid environment. Taxpayers unaware of this could find themselves caught between two tax departments each trying to claim as much revenue as possible, which places a high premium on accurate record-keeping in the face of a tumultuous social situation.

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<sup>2</sup> Brynjolfsson, Erik et al. "COVID-19 and Remote Work: An Early Look at US Data." April 8, 2020. Retrieved from: [https://john-joseph-horton.com/papers/remote\\_work.pdf](https://john-joseph-horton.com/papers/remote_work.pdf).

<sup>3</sup> McKenzie, Brian. "Out-of-State and Long Commutes: 2011." The U.S. Census Bureau, February 2013. Retrieved from: <https://www2.census.gov/library/publications/2013/acs/acs-20.pdf>.

<sup>4</sup> Comeau, Paul et al. "New York's Revised Convenience Rule Provides Some Clarity and Continued Controversy." Journal of Multistate Taxation and Incentives, August 2006. Retrieved from: <https://www.hodgsonruss.com/newsroom-publications-NewYork-revisedconvenience-ruleprovidessomeclarity.html>.

And many taxpayers may end up working in more than just two states by the time the 2020 tax year is complete. For example, an individual may work from their office's state in the beginning of the year, then from their home state in the early weeks of the pandemic, before shifting to another state to take care of family members later on. Demanding that this individual file three separate income tax returns, let alone track how much work was done in each state, defies reason in the middle of a national health crisis.

Further complicating matters is the existence of states that allow for local income taxes. Pennsylvania's local income tax structure is notoriously complex, with [more than 2,500](#) local income tax jurisdictions in the state.<sup>5</sup> Pennsylvania residents pay income taxes based on where they live and where they work. If the rates are different between the two localities, residents pay taxes at the higher rate.

Nowhere is this more pronounced than for workers in Philadelphia, who must pay a wage tax of 3.4481 percent, compared to 1 or 1.5 percent in most of the surrounding municipalities. Because of this, workers in the city of Philadelphia have a much larger tax burden just because their offices are located in the city center. Philadelphia is [giving nonresident remote workers](#) a pass on this tax, but many other jurisdictions aren't being as flexible.<sup>6</sup> Pittsburgh, which charges a 3 percent wage tax on workers in the city limits, hasn't provided the same regulatory lenience that Philadelphia has. Taxpayers residing in areas such as these could be incurring the obligation to file and pay income taxes to multiple jurisdictions without ever having left their home state.

Workers in other states with local income taxes, such as Ohio and Maryland, are also dealing with similar complications.

Even the rare taxpayer who is aware of all these complications and manages to meticulously track hours worked in each state and locality may still not be off the hook. After all, this taxpayer would still need to coordinate with their employer to update their tax withholding in each tax jurisdiction — something businesses struggling to stay afloat may not have the time or capacity to handle. And if their tax withholdings aren't adjusted the employee would then need to remit tax payments directly to the new taxing state, while waiting for the other state to refund their taxes paid, creating quite a paperwork mess.

## **Business Filers**

Businesses would likewise be greatly affected by aggressive enforcement of remote work nexus rules. Smaller businesses that normally do not incur income tax liability in all 50 states would be particularly affected by coronavirus-related remote work.

In order for a state to claim some portion of a business's income taxes, the company must have a connection to the state, often employees or a physical location. Some states view customers as being sufficient to establish nexus and taxing rights.

Should states decline to waive remote work nexus rules, businesses that pay income taxes to just one or two states could discover that many more states are claiming a share of their income for the 2020 tax year. After all, just a single employee switching to remote work in a state that a business does not otherwise have physical presence in is technically enough for certain states to claim some of that business's income taxes.

<sup>5</sup> "Municipal Statistics," Tax Registers, Pennsylvania Department of Community and Economic Development, December 2019. Retrieved from: [http://munstats.pa.gov/Reports/ReportInformation2.aspx?report=EitWithCollector\\_Dyn&type=O](http://munstats.pa.gov/Reports/ReportInformation2.aspx?report=EitWithCollector_Dyn&type=O).

<sup>6</sup> McCrystal, Laura. "Do You Still Have to Pay the Philly Wage Tax If You're Working from Home in Suburbs Due to Coronavirus?" The Philadelphia Inquirer, April 8, 2020. Retrieved from: <https://www.inquirer.com/news/wage-tax-work-from-home-philadelphia-remote-resident-20200408.html>.

Under normal circumstances, businesses tend to carefully control employee telework for exactly this reason. Of course, nonessential businesses whose offices are required to close their doors have little choice but to let their employees work from home — an action which should not incur additional tax liability during this time.

And even businesses that do not incur income tax liability in new states could find that their income tax situation still changes significantly. Because states use an apportionment formula which takes into account some combination of three factors (a business's sales, payroll, and property within that state), any shift in the ordinary mix of factors could lead to changes in tax liability.

How this apportionment formula would change is most obvious in cases where a business's employees do remote work in three-factor states, as that state would be able to claim a greater share of a business's income tax liability due to a jump in payroll to employees within its borders. But employees remote working in single-factor states can cause the apportionment formula to change drastically as well. For example, a business which normally has large amounts of sales to a state but normally lacks physical presence to a single-factor state could have its income tax apportionment shift significantly with the introduction of just a single employee remote working there.

Drastic changes in apportionment can cause a business's total income tax liability to fluctuate wildly. Once it is determined what proportion of a business's profits are subject to taxes in each state, each jurisdiction then imposes its own tax business income tax rate on its slice of the pie. Should higher-tax states be able to claim a greater proportion of a business's income taxes, the business's total tax rate would go up.

## Potential Responses

As previously noted, a few states have already acted to waive remote work nexus and clarified that they will treat remote work as normal office work. An optimistic view would hold that these states are just the earliest to act, and each state will eventually confirm that they will not go after remote work income tax revenue. And certainly, in the meantime, every state that has not done so already should work to treat coronavirus remote work as in-office work.

The cleanest way to achieve that on a state-by-state basis is for legislators to pass statutes clarifying that remote work performed during a specified crisis period will be treated as ordinary in-office work both for individual and business income tax purposes. In states where revenue officials already have sufficient authority to define enforcement standards on nexus questions without the need for new legislation, they should issue clear guidance with dates and specifics of application.

But there's reason to fear that not all states will be so discerning. A [previous NTUF paper](#) noted the budget pressures that states may soon find themselves under as revenue falls off a cliff and balanced budget requirements force states to make the budget math work.<sup>7</sup> That paper focused on the potential for a specific type of bad policy action — retroactive taxation — but states in desperate fiscal situations may also feel that they must act to aggressively collect on any revenue they technically can claim the right to, even if it comes as a result of telework driven by public health recommendations.

In all likelihood, action to ameliorate nexus issues associated with telework will be spotty, with some states failing to enact protections for taxpayers. The resultant blizzard of paperwork and filing

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<sup>7</sup> Wilford, Andrew. "Taxpayers Beware: Economic Contractions Often Lead to State Budget Shenanigans." National Taxpayers Union Foundation, April 6, 2020. Retrieved from: <https://www.ntuf.org/foundation/detail/taxpayers-beware-economic-contractions-of-ten-lead-to-state-budget-shenanigans>.

complications could have serious implications for interstate commerce. The prospect of aggressive state enforcement of new tax obligations could force businesses to disallow remote work entirely during the period of crisis in order to avoid subjecting themselves to new tax codes. It might also cause them to be more cautious about allowing remote work in the future, should this virus re-emerge or should some other threat disrupt the ordinary course of in-office work.

Left unchecked, this could do serious damage to an economy that is already in free-fall and could harm the much-needed recovery after the pandemic subsides. It would also undermine the advancements in technology that have allowed many Americans to keep their jobs, purchase supplies, and stay connected socially — all while barely leaving the home. An explosion of new tax requirements would do significant damage, making interstate commerce less vibrant and further harming the economy.

That is why Congress would be well within its rights to pass a federal law protecting taxpayers from new tax obligations that might arise from telework during this crisis. When scrapping the failed Articles of Confederation to draft the Constitution, America’s founders had the wisdom to empower Congress to ensure the free flow of interstate commerce. Acting to prohibit aggressive states from pouncing on individuals and businesses simply because they complied with public health directives to work from home would be a clear instance of defending interstate commerce from state tax burdens that could undermine it.

More specifically, Congress should consider a statute that ensures remote work performed during the presidentially-declared crisis period is treated as in-office work for state tax purposes. This would effectively “freeze” nexus during the pandemic nationwide, allowing individuals to work from home in accordance with public health guidelines without fear of triggering new tax obligations. Any individual working remotely due to the COVID-19 crisis should not be responsible for new income tax liabilities or requirements, nor should telework during this period expand a business’s corporate income or sales tax nexus.

Such a bill should be thought of as a first step toward more comprehensive reform of tax treatment of remote workers. Legislation like the [Mobile Workforce Tax Simplification Act](#) would address state overreach in cross-border tax enforcement issues that existed prior to the pandemic and will persist after it subsides, but the short-term priority must be a response targeted to the unique challenges that the COVID-19 crisis presents.

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After all, waiting for states to act presents its own downsides, even if every state eventually fell in line. Taxpaying individuals and businesses would be forced to guess in the meantime if their states and localities would eventually freeze remote work nexus during the pandemic. Updating withholding documents, tracking hours worked in each locality, and determining how apportionment would change budgets all represent a significant amount of effort at a hectic time — and yet businesses would essentially need to guess whether doing all this would be worthwhile, or if they should risk hoping for a nexus freeze.

citizens.

## Conclusion

A few states have taken the positive step of declaring that they will not imprudently enforce damaging new tax requirements triggered by remote work while a pandemic sweeps across the country. Rather

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8 Thune, John (R-S.D.). “S.604 - 116th Congress (2019-2020): Mobile Workforce State Income Tax Simplification Act of 2019.” Accessed April 27, 2020, <https://www.congress.gov/bill/116th-congress/senate-bill/604>.

than waiting for other states to follow suit, the federal government should act to protect taxpayers and eliminate a threat to interstate commerce by enacting a nationwide “freeze” on nexus triggered by remote work during the crisis period. The last thing Americans struggling to pay rent, put food on the table, and take care of loved ones need is for state tax bureaucrats to harass them over a technicality.

## **About the Authors**

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