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The Changing Face of Employer State Tax Reporting and Payment Obligations in the Coronavirus Telework "New Normal"

By Larry Brant and Peter Evalds on 10.2.20 | Posted in Legislation, State and Local Tax, Tax Planning

In the wake of the coronavirus pandemic, companies in wide-ranging industries across the country have unprecedented numbers of employees working from remote locations. In a [prior post](#), we discussed numerous issues that may arise from this new normal of teleworking, including tax, labor and employment, liability, and business registration implications.

In this post, we drill down a bit further with respect to employers' state tax reporting and payment obligations that may result from having employees working remotely in states other than where the employers maintain physical offices. This is especially relevant in metropolitan areas that straddle multiple states, like here in Portland, Oregon.

Nexus

One issue that arises for employers is whether the presence of teleworkers in a state constitutes "nexus" sufficient to trigger the application of corporate income tax or gross receipts tax in that state (as well as local jurisdictions within that state). If an employer becomes subject to one or more new state or local tax jurisdictions as a result of satisfying the requisite nexus requirements, it may have new tax reporting and payment obligations (e.g., income taxes, payroll taxes and/or sales and use taxes).

Nexus is a federal constitutional requirement—a state or local government must have a "minimum connection" with a taxpayer in order to impose tax on it.

States typically subject companies that have physical presence (e.g., employees or property located within their borders) to income tax. Many states also impose an "economic nexus" standard whereby companies that derive sufficient income from a state will be subject to tax there. Many states tie economic nexus to a specific threshold (e.g., \$500,000 in annual sales).

One limitation on state taxation is Public Law 86-272—a federal law that prevents states from imposing income tax on businesses located out of state if their business activities are limited to "mere solicitation of orders" for sales of tangible personal property in a state. There is fear, for good reason, that the presence of teleworkers may limit the protection offered by Public Law

86-272 where teleworkers are now present in a state other than merely to solicit sales.

Oregon

Oregon maintains a “substantial nexus” standard whereby a corporation has nexus in Oregon where it regularly takes advantage of Oregon’s economy to produce income, which may be established by the corporation engaging in any of the following enumerated nonexclusive activities:

- Maintaining continuous and systematic contacts with Oregon’s economy or market;
- Conducting deliberate marketing to or solicitation of Oregon customers;
- Filing or being required to file reports or returns with Oregon regulatory bodies;
- Receiving significant gross receipts attributable to customers in Oregon;
- Receiving significant gross receipts attributable to the use of the corporation’s intangible property in Oregon; or
- Receiving benefits provided by the state, such as:
 - Laws providing protection of business interests or regulating consumer credit;
 - Access to courts and judicial process to enforce business rights, including debt collection and intellectual property rights;
 - Highway or transportation system access for transport of the corporation’s goods or services;
 - Access to educated workforce in Oregon; or
 - Police and fire protection for property in Oregon that displays the corporation’s intellectual or intangible property.

Example: If a Washington corporation located in Vancouver, WA, has no offices or telecommuting employees in Oregon and makes no sales in Oregon, it probably is not subject to the Oregon corporate income or excise tax. However, if some of its employees started to work from home in Oregon due to the pandemic, absent guidance to the contrary, the company could potentially be subject to the Oregon corporation excise or income tax.

The good news for the Washington corporation in the above illustration is that the Oregon Department of Revenue (“ODOR”), through informal guidance set forth on [its website](#), has provided temporary relief for this situation. In this guidance, the ODOR stated that for Oregon corporate excise tax and corporate income tax purposes, the presence of a corporation’s teleworking employees in Oregon between March 8, 2020 and November 1, 2020 will not be treated by the ODOR as a “relevant factor” when making a nexus determination if the employees at issue are regularly based outside Oregon.

Practice Alert: As noted above, this guidance is informal, and as such, an employer’s reliance on such guidance may be limited. Additionally, this guidance, by its express terms, ends on November 1, 2020. If that date is not extended, employers may want to rethink their telework policies.

Washington

Nexus for purposes of Washington’s Business & Occupations (“B&O”) tax includes both physical presence and economic presence. According to the Washington Department of Revenue (“WDOR”), the presence of one employee is sufficient to create physical nexus. The economic presence standard for B&O tax purposes is \$100,000 in gross receipts sourced or attributed to Washington.

Oregon companies with no physical presence in Washington before the pandemic and less than the applicable economic presence standard (e.g., \$90,000 in gross receipts attributable to Washington) may become subject to B&O tax by virtue of a pandemic-related telework arrangement in Washington.

While WDOR has provided some [coronavirus-specific guidance](#), we are not aware of any such guidance with respect to nexus for purposes of the Washington B&O tax.

Practice Alert: Oregon companies might also have issues related to other tax regimes in Washington, such as sales and use tax. The presence of a single employee is likely sufficient to create sales tax nexus in Washington.

Apportionment

In some states, the sudden presence of one or more employees may also affect apportionment.

Some states still use three-factor apportionment (property, payroll and sales). Each of these factors may be implicated by temporary telework.

- Payroll. Generally, the numerator of the payroll factor includes compensation paid to employees for the state where the employee performs services. Absent guidance to the contrary, this may include payroll paid to employees working in the state from which they telework.
- Property. Generally, the numerator of the property factor includes the value of property the taxpayer owns or uses in a state. If employees use employer property at their home offices, the value of that property may need to be included in the property factor.

- Sales. Some states use a cost-of-performance method for apportioning receipts from the sale of services, whereby companies include receipts in the numerator if receipts are from income-producing activity in a state. If employees are performing those services in a state from which they now telework, that activity may need to be included in the numerator. The same would generally not apply to market-based sourcing states where receipts are sourced to the state where customers receive the benefits of the services.

The good news for Oregon and Washington employers with temporary teleworkers is that the potential impact to them of the apportionment issues discussed above is relatively low, because both Oregon's corporate income/excise tax and Washington's B&O tax (at the state level) employ single-sales-factor apportionment and each uses a market-based apportionment method for sourcing receipts from sales of services. However, local jurisdictions in Washington use two-factor apportionment that includes payroll. (RCW 35.102.130).

Federal Preemption

One proffered solution is the Remote and Mobile Worker Relief Act (S.3995), introduced in the U.S. Senate by Senator John Thune in June of this year. This Act would provide temporary coronavirus telework relief by way of limited federal preemption.

Among other things, the Act would:

- provide that the temporary presence of teleworkers in a state as a result of the coronavirus pandemic would not in and of itself create tax nexus; and
- require receipts or income for state and local income and gross receipts tax purposes to be apportioned and sourced to the tax jurisdiction that relates to the employee's "primary work location" (the address of the employer where the employee is regularly assigned to work when such employee is not working remotely) during the "covered period" (the period that began when the employee began to telework and that ends on the earlier of the date when the employer allows the employee and not less than 90 percent of the employer's workforce to return to such primary work location, or December 31, 2020).

The Act would not cover professional athletes, professional entertainers, certain film and television production employees, or certain public figures.

While the bill has reportedly received support from the business community and the American Institute of CPAs, it has not yet advanced in the legislative process. So, at least for now, it is not law.

Conclusion

The coronavirus pandemic has upended the way companies do business across the country. With that upheaval has come state and local tax issues related to the locations from where employees work. While we only specifically mentioned the tax laws of Oregon and Washington for illustrative purposes, the same issues permeate across the entire country at the state and local levels. The tax consequences of having remote workers so far depends in large part on the tax regimes of each state and local government. Federal legislation has been introduced that could provide some certainty in this area, but its passage is far from certain at this time. Tax advisors need to stay abreast of the ever-changing state and local tax landscape, and carefully advise their clients about these issues and the potential exposure to jurisdictions where they hadn't contemplated any tax reporting or payment obligations.

Tags: apportionment, Business, Coronavirus, corporate income tax, COVID-19, employees, employers, gross receipts tax, Oregon, Oregon Department of Revenue, Oregon Taxpayers, remote workforce, substantial nexus, Taxpayer, teleworking, U.S. Senate, Washington Business & Occupations Tax, Washington Department of Revenue, Washington state