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Coronavirus (Covid-19): Payroll and employment tax considerations

To prevent the spread of contagious illnesses, such as the Coronavirus, workers may be asked to quarantine, requiring that they work remotely where telework is possible. The reassignment of work locations and/or the displacement of workers due to health safety precautions raises many employer concerns, some of them which could be addressed by upcoming federal and state policy.

President Trump calls for payroll tax cut and assistance for hourly workers who are absent from work in connection with COVID-19

On March 9, 2020, President Trump [announced](#) that he will be meeting with members of Congress to discuss a payroll tax cut and assistance for hourly workers who are displaced in connection with COVID-19. Details of the President's proposals were expected to be released on March 10, 2020.

Income tax withholding when employee lives and works in two different states

It is frequently the case that the employee's work and resident locations are in two different taxing jurisdictions. For instance, an employee may work in New York but live in New Jersey, or work in one Ohio local tax jurisdiction but live in another Ohio local tax jurisdiction. For this reason, when employees temporarily work from home, consideration must be given to

Fig. 1: States with the convenience of the employer rule

Connecticut
([Public Act 18-49, Sec. 20\(2\)\(C\)](#))

Delaware
([2017 Delaware Schedule W](#))

Nebraska
([Neb. Admin. R. & Regs. § 003.01C](#))

New York
([Technical Memorandum TSB-M-06\(5\)D](#))

Pennsylvania
([61 Pa. Code § 109.8](#))

the resident and nonresident income tax withholding rules that apply.

- *State nonresident (work location) income tax withholding.* For the nonresident state, income tax withholding is generally required only on those wages earned in the nonresident state.

An exception to this rule applies in states (see Fig. 1) that enforce the “convenience of the employer” rule. Under New York’s convenience of the employer rule, the employer is required to withhold New York state income tax from all wages paid to the employee if (1) the employee spent at least one day in the year in New York and (2) the reason the employee is working from home outside of the state is for the employee’s own convenience. If the reason the employee is working from home is for the convenience of the employer, work from home is excluded from the nonresident income tax withholding requirement. ([TSB-M-06\(5\)](#).)

The challenge is that states imposing the convenience of the employer rule generally apply a stringent definition of what constitutes work from home for the employer’s convenience. Absent specific guidance that work from home is for the employer’s convenience due to health concerns (e.g., Coronavirus), the exception from nonresident income tax withholding does not apply to these telework arrangements.

Will states that enforce the convenience of the employer rule adopt a favorable policy for COVID-19? It may take some time for states to reach a decision. However, in the past, New York state offered nonresident income tax exemptions for Hurricane Sandy, but did not concede that work outside of New York due to Hurricane Sandy was for the employer’s convenience. ([New York Department of Taxation and Finance, Hurricane Sandy, November 20, 2012.](#))

- *State resident income tax withholding.* Assuming the employer has business operations in the resident state, income tax withholding is generally required on all wages earned within and outside of the resident state. This requirement is clear if the employer has business offices, retail operations, warehouses, etc., in the employee’s resident state.

The challenge arises, however, when the only work activity within the resident state is work from an employee’s home. Arkansas recently ruled that work performed out of an employee’s home for an out-of-state contractor is subject to Arkansas income tax but not income tax withholding. ([Arkansas Revenue Legal Counsel Opinion No. 20190514, February 3, 2020.](#)) Most other 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. (New Jersey: [Telebright Corp., Inc. v. Director of Taxation](#); Virginia: [Ruling of the Virginia Tax Commissioner, Document No. 14-158](#), August 28, 2014.)

It is doubtful a state would consider an employee's home office a regular place of business if the employee worked from home for a few days; however, states can have unique definitions of what constitutes work that is primarily performed within the state. And, because the home office can trigger nexus for other employment and business taxes, it is essential that employers confirm the resident income tax rules in each state a teleworker will provide services.

- *Local payroll tax considerations.* As with state income tax, work from home may trigger local payroll taxes in the employee's resident location that would otherwise not have applied. For this reason, a careful review of the resident (and nonresident) local tax rules that apply to teleworkers is also necessary,

State unemployment insurance

Unlike state income tax, where sourcing rules can vary by state, state unemployment insurance is subject to federal uniform standards (US Department of Labor, [Unemployment Insurance Program Letter No. 20.04](#).) Under the federal "Localization of Work Provisions" unemployment insurance applies only in one state and is generally paid where the employee's work is localized. An employee's work is localized in the state if (1) the services are performed entirely within such state; or (2) the service is performed both within and outside of the state but the service performed outside of the state is incidental to the individual's service within the state; for example, is temporary or transitory in nature or consists of isolated transactions.

Accordingly, for the most part, employees temporarily working from home in connection with COVID-19, employers should continue to pay unemployment insurance to the state where the employee normally works rather than to the resident state. This can change if the telework arrangement lasts for several months, such that work for the year is primarily performed from the employee's home.

Ernst & Young LLP insights

Considering the state and local tax consequences of telework arrangements, it is vital that employers seek the assistance of qualified employment tax professionals who can confirm the applicable state and local withholding and payroll tax requirements that apply to each teleworker based on specific facts and circumstances.

It is also important that employers closely monitor federal, state and local policies as they relate to payroll tax changes in connection with COVID-19. These policies may include tax filing extensions, tax cuts, withholding exemptions, tax credits and special unemployment insurance provisions for displaced workers.

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