MOBILE WORKFORCE STATE INCOME TAX FAIRNESS AND SIMPLIFICATION ACT OF 2007

HEARING

BEFORE THE

SUBCOMMITTEE ON
COMMERCIAL AND ADMINISTRATIVE LAW

OF THE

COMMITTEE ON THE JUDICIARY
HOUSE OF REPRESENTATIVES

ONE HUNDRED TENTH CONGRESS

FIRST SESSION

ON

H.R. 3359

NOVEMBER 1, 2007

Serial No. 110–143

Printed for the use of the Committee on the Judiciary

Available via the World Wide Web: http://judiciary.house.gov

U.S. GOVERNMENT PRINTING OFFICE

38–642 PDF WASHINGTON : 2008

For sale by the Superintendent of Documents, U.S. Government Printing Office
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NOVEMBER 1, 2007

MOBILE WORKFORCE STATE INCOME TAX FAIRNESS AND SIMPLIFICATION ACT OF 2007

THURSDAY, NOVEMBER 1, 2007

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW,
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Subcommittee met, pursuant to notice, at 12:12 p.m., in room 2237, Rayburn House Office Building, the Honorable Linda Sánchez (Chairwoman of the Subcommittee) presiding.

Present: Representatives Sánchez, Johnson, Watt, Cannon and Jordan.

Staff present: Michone Johnson, Majority Chief Counsel; Norberto Salinas, Majority Counsel; Stewart Jefferies, Minority Counsel; and Adam Russell, Majority Professional Staff Member.

Ms. SÁNCHEZ. I would bang the gavel, but I don't have one with me this morning, or this afternoon, I should say. But I am going to call the hearing of the Committee on the Judiciary, Subcommittee on Commercial and Administrative Law to order. And I am going to recognize myself for a short statement.

Our workforce has increasingly become mobile. Some employees travel and work in several States throughout the year, while others live in one State but work in another. When it comes time to complete their income tax returns, many employees must file several returns because each State has the authority to tax all the income earned within its borders and all the income of the residents wherever the income is earned.

While employees are responsible for filing State income tax returns, their employers are duty bound to withhold State income taxes for their employees. Therefore, both employees and employers must know the different thresholds for each State in which the company operates.

These varying thresholds have raised concerns of employee tax liability and employer State income tax withholding compliance during this period of improved corporate transparency. To remedy this confusing system, my colleagues, Congressman Johnson and Ranking Member Cannon introduced H.R. 3359, which aims to establish a uniform national threshold of 60 work days within a calendar year before a State may tax certain nonresidents.

Today's hearing serves a dual purpose. First, this hearing will provide us with an opportunity to learn more about State taxation of nonresidents, specifically the differing thresholds States maintain and how they affect employees, employers and State and local revenues. And second, the testimony provided today will help us determine what role Congress has in this matter, and whether H.R. 3359 addresses the concerns of employee liability and employer withholding requirements for nonresidents, while protecting the interests of State and local governments to tax the income earned within their boundaries.

Accordingly, I very much look forward to today's hearing and the testimony of our witnesses. And at this time I would like to recognize my colleague, Mr. Cannon, the distinguished Ranking Member of the Subcommittee and co-author of the bill that we are examining today for his opening remarks.

[The bill, H.R. 3359, follows]:

I

110TH CONGRESS
1ST SESSION

H. R. 3359

To limit the authority of States and localities to tax certain income of employees for employment duties performed in other States and localities.

IN THE HOUSE OF REPRESENTATIVES

AUGUST 3, 2007

Mr. JOHNSON of Georgia (for himself and Mr. CANNON) introduced the following bill; which was referred to the Committee on the Judiciary

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A BILL

To limit the authority of States and localities to tax certain income of employees for employment duties performed in other States and localities.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

SECTION 1. SHORT TITLE.

This Act may be cited as the "Mobile Workforce State Income Tax Fairness and Simplification Act of 2007".

SEC. 2. LIMITATIONS ON STATE AND LOCALITY WITHHOLDING AND TAXATION OF EMPLOYEE INCOME.

(a) IN GENERAL.—No part of the wages or other remuneration paid to an employee who performs duties in more than one State or locality shall be subject to the income tax laws of any State or locality other than—

(1) the State or locality of the employee's residence; and

(2) the State or locality in which the employee is physically present performing duties for more than 60 days during the calendar year in which the income is taxed.

(b) WAGES OR OTHER REMUNERATION.—Wages or other remuneration paid in any calendar year are not subject to State or locality income tax withholding and reporting unless the employee is subject to income tax under subsection (a). Income tax withholding and reporting under subsection (a)(2) shall apply to wages or other remuneration paid as of the commencement date of duties in the State or locality during the calendar year.

(c) OPERATING RULES.—For purposes of determining an employer's State income tax withholding and information return obligations—

(1) an employer may rely on an employee's determination of the time expected to be spent by such

employee in the States or localities in which the employee will perform duties absent—

(A) actual knowledge of fraud by the employee in making the estimate; or

(B) collusion between the employer and the employee to evade tax;

(2) if records are maintained by an employer recording the location of an employee for other business purposes, such records shall not preclude an employer's ability to rely on an employee's determination as set forth in paragraph (1); and

(3) notwithstanding paragraph (2), if an employer, at its sole discretion, maintains a time and attendance system which tracks where the employee performs duties on a daily basis, data from the time and attendance system shall be used instead of the employee's determination as set forth in paragraph (1).

(d) DEFINITIONS AND SPECIAL RULES.—For purposes of this Act:

(1) DAY.—An employee will be considered physically present and performing duties in a State or locality for a day if the employee performs more than 50 percent of the employee's employment duties in such State or locality for such day.

(2) EMPLOYEE.—The term ''employee'' shall be defined by the State or locality in which the duties are performed, except that the term ''employee'' shall not include a professional athlete, professional entertainer, or certain public figures.

(3) PROFESSIONAL ATHLETE.—The term ''professional athlete'' means a person who performs services in a professional athletic event, provided that the wages or other remuneration are paid to such person for performing services in his or her capacity as a professional athlete.

(4) PROFESSIONAL ENTERTAINER.—The term ''professional entertainer'' means a person who performs services in the professional performing arts, provided that the wages or other remuneration are paid to such person for performing services in his or her capacity as a professional entertainer.

(5) CERTAIN PUBLIC FIGURES.—The term ''certain public figures'' means persons of national prominence who perform services for wages or other remuneration on a per-event basis, provided that the wages or other remuneration are paid to such person for services provided at a discrete event in the form of a speech, similar presentation or personal appearance.

(6) EMPLOYER.—The term "employer" has the meaning given such term in section 3401(d) of the Internal Revenue Code of 1986 (26 U.S.C. 3401(d)) or shall be defined by the State or locality in which the duties are performed.

(7) LOCALITY.—The term "locality" means any political subdivision, agency, or instrumentality of a State.

(8) STATE.—The term "State" means each of the several States (or any subdivision thereof), or any territory or possession of the United States.

(9) TIME AND ATTENDANCE SYSTEM.—The term "time and attendance system" means a system where the employee on a contemporaneous basis records his work location for every day worked and the employer uses this data to allocate the employee's wages between all taxing jurisdictions in which the employee performs duties.

(10) WAGES OR OTHER REMUNERATION.—The term "wages or other remuneration" shall be defined by the State or locality in which the employment duties are performed.

○

Mr. CANNON. Thank you, Madam Chair. And I apologize. I am going to have to be leaving the hearing virtually immediately. We have a bill on the floor that would save us from a 19th century piece of legislation. I worry that somebody will want to save us from an 18th century Constitution at some point in time. So I need to go over and do an amendment there.

And I apologize in advance to our distinguished panel and appreciate them being here. This, of course, is legislation that I introduced last year. And I wanted to thank Mr. Johnson for introducing it on behalf of the majority this time.

This is good legislation. It creates some bright lines and significantly facilitates the nature of what we are doing, what is actually happening in America, that some States just can't keep their hands off.

And so, with that, Madam Chair, I would actually like to submit my statement for the record.

Ms. SÁNCHEZ. Without objection, so ordered.

[The prepared statement of Mr. Cannon follows:]

PREPARED STATEMENT OF THE HONORABLE CHRIS CANNON, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF UTAH, AND RANKING MEMBER, SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW

In today's increasingly mobile workplace, employers and employees face numerous challenges in determining tax liability, particularly in instances when employers send their employees into another state to work for a short period of time.

Of the 41 states that have a personal income tax, 24 have no minimum threshold for employer withholding requirements. That is, employers and employees are liable for that state's taxes the moment an employee sets foot in the state to do work. Six states have exemptions for employer filing requirements that are determined by the number of days that an employee works in the state. Those thresholds range from a minimum of 10 days in Maine to 60 days in Arizona and Hawaii.

Another 11 states have exemptions based on the amount of income that an employee earns in a particular state. Those income thresholds range from a minimum of $300 in any calendar quarter in Ohio to $7,000 in Virginia. According to the Council on State Taxation (COST), represented here by Mr. Doug Lindholm, the point at which tax liability attaches to an individual is usually, but not always, the same as when a company's withholding requirement kicks in.

This patchwork of state laws creates significant administrative headaches for both companies and their employees. Under Sarbanes-Oxley, a company must certify that it is compliance with all state and local laws, including tax laws. With so many variations on the state withholding laws, employers argue that it is impossible to be fully in compliance with Sarbanes-Oxley.

All four of the witnesses today recognize that there is a problem here. That is a good start. Obviously the state taxing authorities, as represented by Mr. Harley Duncan, have their concerns about this legislation, which is to be expected. But I am heartened to see that they are willing to talk about ways to fix the problem.

We are all concerned about federalism on this committee and on the ability of states to control activities within the state's borders. That said, this Subcommittee, this Committee, and this Congress have also recognized that there are times when the country's needs outweigh the needs of any individual state. Such was the case with the recently enacted Internet Tax Freedom Act Amendments Act, which was signed by the President yesterday.

In addition to Mr. Duncan and Mr. Lindholm, I want to thank our other witnesses here today, particularly Ms. Nelson, who flew in from Alaska to give us her perspective on the burdens that the current situation places on employers and employees. I also want to thank Professor Hellerstein for being here; he has testified before this Subcommittee in previous Congresses and his knowledge of the Commerce Clause as it relates to state taxation is invaluable.

Finally, I am thankful that Representative Johnson has introduced H.R. 3359, the "Mobile Workforce State Income Tax Fairness and Simplification Act of 2007." I am a co-sponsor of that legislation and was a sponsor of a similar bill, H.R. 6167, in the last Congress. H.R. 3359 is beginning to garner more co-sponsors, and I am hopeful that this hearing will raise awareness of this issue and begin to get the ball rolling towards a legislative solution.

American companies and American workers deserve no less.

I look forward to hearing from our witnesses.

Mr. CANNON. And in addition to that, I have a document, a statement by the AICPA, the American Institute of Certified Public Accountants. I would ask unanimous consent that we can submit that to the record.

Ms. SÁNCHEZ. Without objection, so ordered.

[The information referred to is available in the Appendix.]

Mr. CANNON. Thank you, Madam Chair. And I yield back.

Ms. SÁNCHEZ. I thank the gentleman for his statement. I also would like to enter into the record a statement from Mr. Conyers who could not join us today. Without objection, it will be entered into the record.

[The prepared statement of Mr. Conyers follows:]

PREPARED STATEMENT OF THE HONORABLE JOHN CONYERS, JR., A REPRESENTATIVE IN CONGRESS FROM THE STATE OF MICHIGAN, CHAIRMAN, COMMITTEE ON THE JUDICIARY, AND MEMBER, SUBCOMMITTEE ON COMMERCIAL AND ADMINISTRATIVE LAW

Today we hold a legislative hearing on H.R. 3359, a bill introduced by two distinguished members of this Subcommittee, Congressman Hank Johnson and Ranking Member Chris Cannon. This legislation attempts to impose a uniform national standard for when employees are required to pay state income taxes to those states in which they work but do not reside. Some concerns have been raised that some employees who work in several states throughout the year have difficulty knowing in which states they must file an income tax return and that some employers also experience the same challenges when withholding deductions for their employees. These concerns apparently exist because the states have different standards by which they begin to tax non-resident employees.

Although this legislation seems to address those concerns, I worry about Congress treading upon state sovereignty. My state of Michigan has already addressed some of the concerns some of you will discuss this afternoon by entering into reciprocity agreements with surrounding states. I would hope that the states can resolve these concerns first, and if they cannot, we can determine whether Congress should step in and strike a balanced piece of legislation.

I have concerns about how H.R. 3359 may impact Michigan and other states. According to an attachment to Mr. Lindholm's testimony, this legislation will result in an estimated revenue loss for Michigan, a state which is experiencing severe budgetary problems. Other states, especially California, Illinois, and New York, will stand to lose tens of millions of dollars in revenues if H.R. 3359 passes without any changes. We should be careful not to cause more revenue losses for states. Remember that the power to tax is the power to govern, and if states cannot tax the income earned within their states, how will they afford to provide needed services to those within their states. I understand that the Federation of Tax Administrators opposes H.R. 3359 as written, and I look forward to hearing their testimony this afternoon on how this bill can be improved so that we can pass a balanced bill.

Ms. SÁNCHEZ. And at this time, I would like to recognize Mr. Johnson for his opening statement.

Mr. JOHNSON. Thank you, Madam Chairwoman, for holding this important hearing that affects businesses large and small. Today if an Atlanta-based employee of a Chicago company travels to headquarters on business once a year, that employee would be subject to Illinois tax, even if his annual visit only lasts 1 day.

But if he travels to Maine, his trip would be subject to tax only if his trip lasts for 10 days. And if he traveled to a weekend conference in Virginia, withholding would occur if his wages were above his personal exemptions and standard deduction, unless the employee elected his filing threshold.

These varying thresholds within the 41 States that have a personal income tax have their own different set of standards for liability and enforcement. This inconsistency between statute and practice has the effect of placing tremendous compliance burdens on businesses and employees.

With the passage of the Sarbanes-Oxley Act employers are spending a tremendous amount of time and resources to fully comply with tax laws and withholding regulations. Under section 404 of the act, auditors of public companies must attest under penalty of perjury that they have reviewed the corporation's systems and that the company is in full compliance with all of its tax obligations.

With 41 different tax laws, however, and with various de minimis rules, companies are facing difficulties complying with these rules and are expending a significant amount of resources to comply. That is why I, along with my colleague, Congressman Chris Cannon, introduced H.R. 3359, the "Mobile Workforce State Income Tax Fairness and Simplification Act of 2007." This is an act that Congressman Cannon has been working on even prior to the 110th Congress, which is my first session of Congress, of course.

So I appreciate your work and effort in this regard in the 109th, Mr. Cannon.

H.R. 3359 would establish uniform and administratable rules, including appropriate de minimis rules, which would ensure that the appropriate amount of income tax is paid to jurisdictions without placing undue burdens on employees and their employers. This legislation was not designed to usurp State rights to tax. Rather, this bill was introduced in order to aid companies to fully comply with applicable laws and regulations, including State tax laws.

We are all aware of the problem. It is my hope that this bill can serve as the impetus to a solution that will minimally impact State revenues while assisting businesses as they comply with complex tax laws.

Thank you. And I yield back my time.

Ms. SÁNCHEZ. I thank the gentleman for his opening statement.

And without objection, other Members' opening statements will be included in the record. Without objection, the Chair will be authorized to declare a recess of the hearing at any time.

I am now pleased to introduce the witnesses for today's hearing. Our first witness is Douglas Lindholm. Mr. Lindholm is president and executive director of the Council on State Taxation, an organization dedicated to preserving and promoting equitable and nondiscriminatory State taxation of multi-jurisdictional entities.

He also served for 3 years as legislative director for COST. Prior to taking the helm at COST, Mr. Lindholm served as counsel for State tax policy for the General Electric Company in Washington, D.C., where he managed and coordinated State tax policy initiatives before State legislators and State administrative agencies.

We want to welcome you here.

He has written numerous articles on Federal, State, and local tax issues in a wide variety of publications, testified frequently before State legislatures and Congress on State tax issues and is a frequent speaker at State tax and State government affairs conferences and seminars.

Our second witness is Dee Nelson. Ms. Nelson has over 17 years of experience as a payroll professional, an active member of the American Payroll Association since 1998. She chairs the automated clearinghouse committee nominations and election committee and the global affairs task force as well as the hotline referral service. She also teaches courses for APA's fundamental payroll certification and certified payroll professional designations.

She received a meritorious service award in 2003 and the special recognition award in 2007. At the State level, she has served as president of both the northern life and, I know this is going to be a tough one, Matanuska-Susitna Valley—is that pretty close—chapters. Ms. Nelson currently works as payroll manager for Alutiiq LLC, a company that provides government contracting service.

Welcome to you.

Our third witness is Harley Duncan. Mr. Duncan is the executive director of the Federation of Tax Administrators and the chief executive officer of the National Association of State Tax Administration Agencies. FTA represents the revenue departments of each of the 50 States plus D.C. and New York City and carries out a program of research, information sharing, training, inter-governmental coordination, and Federal representation.

Prior to joining the FTA, Mr. Duncan served as secretary of the Kansas Department of Revenue and was responsible for administration of major State taxes as well as motor vehicle registration, drivers licensing, alcoholic beverage control, and property tax oversight. He is a frequent lecturer and speaker at national and regional tax conferences and meetings and has written several tax articles. Mr. Duncan regularly testifies before congressional Committees on matters affecting State and local taxation.

We want to welcome you this afternoon as well.

Our final witness is Walter Hellerstein. Professor Hellerstein joined the University of Georgia's School of Law faculty in 1978 and was named Francis Shackelford distinguished professor of taxation law in 1999. He teaches in the area of State and local taxation, international taxation, and Federal income taxation.

Professor Hellerstein is co-author with his late father of both the leading treaties on State taxation, State Taxation Volumes I and II, which probably gave me nightmares as a law student, and the leading casebook on State and local taxation, State and Local Taxation. In 1992 Hellerstein received the multi-state tax commission's 25th anniversary award for outstanding contributions to multistate taxation.

I want to thank all of you for your willingness to participate in today's hearing. Without objection, your written statements will be placed into the record. And we are going to ask that you limit your oral testimony to 5 minutes.

You will note that we have a lighting system that we try to keep on top of, let us be honest, but don't always. When you begin your testimony, you will get a green light. After 4 minutes, the light will turn yellow.

It serves as a warning that you have one minute left to give your testimony. When it turns red, that means your time has expired, and we would appreciate it if you could just conclude your final thoughts so that we can move on to the next witness.

After each witness has presented his or her testimony, Subcommittee Members will be permitted to ask questions subject to the 5-minute limit.

And so, at this time, I would invite Mr. Lindholm to please proceed with his testimony.

TESTIMONY OF DOUGLAS L. LINDHOLM, PRESIDENT AND EXECUTIVE DIRECTOR, COUNCIL ON STATE TAXATION, WASHINGTON, DC

Mr. LINDHOLM. Thank you, Madam Chairwoman and Ranking Member Cannon and Congressman Johnson. I very much appreciate the opportunity to be here and the fact that you are holding this hearing. As indicated, my name is Doug Lindholm. I am president and executive director of the Council on State Taxation. Our membership consists of almost 600 multi-state businesses engaged in both interstate and international commerce.

I realize that time is somewhat short today, so let me just make three points regarding the bill before us today, House bill 3359. First of all, as opening statements attest, this is indeed a widespread problem that we feel Congress is best suited to resolve. Secondly, the bill contains a simple and practical solution to that problem. Third, we feel that solution very effectively balances State sovereignty issues with Congress' interest in resolving burdens on interstate commerce.

Now, let me elaborate briefly on some of those. First of all, with regard to how widespread the problem is, one of the greatest strengths of our economy is that we have an increasingly nimble and mobile workforce, national workforce. Those of you that have spent any time in an airport recently realize that thousands of employees are sent by their employers on an almost daily basis to nonresident States to work in those States. Most of those trips are temporary in nature.

Typically they will travel out, conduct some business, and then fly back to their State of residence. Unfortunately, the 41 States that impose a personal income tax have widely diverging rules for determining two things: one, when the liability for that employee attaches and two, when the withholding obligation for that employee's employer attaches.

Some States attach a liability the moment you set foot in the State. Some States have a days threshold. Arizona and Hawaii, to name two, have a 60-day threshold similar to what we are proposing. Others have a dollar threshold, an earnings threshold. And still others have a combination of a days and a dollar threshold. And there is an attachment to my testimony that does a pretty good job of laying this out in a map.

A key point I would like to make is that this is not just an issue for large corporations. It impacts small businesses, nonprofits, State and local governments, hospitals, churches, universities, anyone who has employees that travel regularly for work.

Point two, we think this is a simple and practical solution. And essentially what it does is it creates a Federal threshold of 60 days for temporary work assignments in nonresident States. And another point is that for anything up to 60 days the employee would remain taxable in their State of residence.

Now, I am sure we will get the question, why 60 days? We conducted a fairly extensive survey of our membership, our member companies. And 60 days came back as the figure that our employers felt resolved most of the problems.

First of all, that time period covers the vast majority of employee travel. Secondly, if you start shortening that time period, there is a—it becomes more and more likely that employees will inadvertently or unwittingly back into the State rules.

Secondly, if you start to shorten that time period, it increases the possibility that there will be arguments over what constitutes a day or what are the duties that they are performing for employment in a day. The 60 days allows that company to focus on that small set of employees that actually travel for long-term work assignments.

The second question I would like to address is that why no dollar threshold. I would like to point out that we have been working with the State administrators on this issue for 2 years, or discussing it with them for 2 years. And we know that this is a concern for States. But after considering this dollar threshold, we ultimately rejected it because it would actually make the compliance burden greater in many cases than it is now.

Employers would be forced to track every employee on a daily basis, compare that with sensitive payroll data, and then make allocations to the States where they travel. And all this before the employee has filed a single tax return. So although we are sympathetic to State concerns, we feel that that really would create a greater compliance burden.

A third point, we really do think that this solution strikes the proper balance between individual State concerns over sovereignty and revenue and national concerns of Congress over reducing burdens on interstate commerce. We have got a fiscal note attached, and we feel that the impact on States is negligible. For all 50 States, the net reduction in personal income tax revenues is estimated to be 100 of 1 percent, .01 percent.

And again, I want to point out that we had been working on this issue with tax administrators for several years. We very much appreciate their constructive engagement. But this is an issue that if left unresolved will only grow in scope and complexity. Accordingly, we very much urge your support, thank you for your support. And I would be happy to answer any questions.

[The prepared statement of Mr. Lindholm follows:]

PREPARED STATEMENT OF DOUGLAS L. LINDHOLM

Statement of

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President & Executive Director
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Before the

U.S. House of Representatives
Committee on the Judiciary
Subcommittee on Commercial and Administrative Law

Hearing on H.R. 3359
The Mobile Workforce State Income Tax Fairness and Simplification Act of 2007

The Honorable Linda T. Sanchez, Chair

November 1, 2007

Chairwoman Sanchez, Ranking Member Cannon, Congressman Johnson and other Members of the Subcommittee, I am Doug Lindholm, President and Executive Director for the Council On State Taxation, which is more commonly known as COST.

COST is a non-profit trade association consisting of nearly 600 multistate corporations engaged in interstate and international business. COST's objective is to preserve and promote equitable and non-discriminatory state and local taxation of multi-jurisdictional business enterprises.

I very much appreciate the opportunity to share with you COST's views on the important issue of nonresident state and local personal income taxes imposed on employees who travel away from their resident states for temporary work periods and the withholding obligations of their employers.

I would like to thank Congressman Johnson and Ranking Member Cannon for being the initial cosponsors of HR 3359, The Mobile Workforce and State Income Tax Fairness Act of 2007, to allow Congressional, public sector and private sector dialogue to continue on this very important and widespread issue.

Widespread Problem—Simple Solution

The problem addressed by H.R. 3359 can be simply stated: every business day thousands of employees across the country are sent by their employers to work in nonresident states. The vast majority of these trips are temporary in nature, whereby the employee conducts business in the nonresident state for a short period of time and then returns to his/her resident state. Unfortunately, states that impose a personal income tax have diverse rules relating to the obligation of the nonresident employee to file a personal income tax return and to the commensurate employer withholding deductions. Some states impose a personal income tax filing requirement based upon a "first dollar" earned approach with respect to the nonresident employee. Other states set a minimum threshold period of a specific number of days under which the employee is not subject to the nonresident state personal income tax. For example, Arizona and Hawaii have sixty day threshold periods. Some states utilize an earnings threshold, and yet other states utilize a combination of day and earnings threshold periods. In most cases, the commensurate withholding obligations on employers match the rules for determining the employee's liability, but in at least one state the burdens are disparate, with the employee responsible for paying nonresident tax on the first dollar earned, but the employer's responsibility for withholding triggered only after a fourteen day in-state period. The patchwork of inconsistent state laws and rules is shown by the map and chart attached as Exhibit A to my testimony. The challenges imposed upon employees to understand these widely divergent rules, track down the appropriate nonresident state forms and actually comply with this multiplicity of state tax rules is nearly insurmountable.

So too, employers are extremely hard pressed to comply with these varying and disparate rules and provide the appropriate nonresident state withholding. It is important to note that this is not only an issue affecting large corporations with thousands of employees travelling for work each year; small business, churches and other charitable entities, and even state and local governments severely struggle to attempt compliance with this regime. I must emphasize that there is no readily available technological solution to this problem. Very few large corporations have the capability to integrate payroll with business operating systems to allow tracking of employees' whereabouts on a daily basis in order to comply with the patchwork of nonresident state withholding obligations. The costs of creating such systems would be exorbitant in relation to any compliance gains to the various states. Small business would experience similar issues of undue expense for limited increases in compliance.

Simple Solution

The simple answer to this widespread problem is to legislate a federal threshold period of sixty days for temporary employee work assignments to nonresident states. Employees working in nonresident states for sixty or fewer days would remain fully taxable in their resident state for all earnings, to the extent the resident state chooses to have a state personal income tax system. The vast majority of employees who travel outside their resident state for employment purposes would fit within this threshold period. To the extent the employee has duties in the nonresident state for an extended period exceeding the sixty day annual threshold, then the employer would have adequate information to provide accurate withholding of wages to the nonresident state, and the employee would be on notice that the state filing rules must be complied with. This uniform rule would greatly enhance compliance for all businesses under the state withholding rules, and would provide much greater certainty for employees in fulfilling their personal nonresident state filing obligations.

Why is the Sixty Day Period Important? What about a Dollar Threshold?

I would like to respond to a concern raised by some state policymakers that the sixty day period is too long and that a dollar threshold period should be considered.

With respect to a day threshold, COST members carefully analyzed various threshold periods and determined that the sixty day period enhanced and simplified compliance to the greatest extent. With a uniform sixty day threshold, the vast majority of employees who travel for business duties would not be subject to nonresident state taxation but would remain fully taxable in their resident states, with the employer fulfilling the normal withholding obligations on those resident state earnings. This time period further allows employers to focus compliance and education efforts on a small pool of employees who have easily identifiable extended duties at particular nonresident state locations. Shorter time periods would enhance the probabilities that employees would "back into" the nonresident state rules unknowingly through intermittent trips of short duration, and would provide commensurately greater burdens on employers to identify those employees subject to nonresident state withholding and educate those employees on their filing obligations.

The sixty day threshold compares favorably with existing state reciprocity agreements. Under these agreements, some states provide for a full exemption for nonresidents traveling between neighboring states for work. In essence, these states have provided a "365 day threshold" for nonresidents from neighboring states. H.R. 3359 is conceptually similar to these existing agreements, albeit with a sixty day threshold rather than a full 365 day exemption, and it reflects the realities of our modern economy in which employees are as likely to travel across the country for temporary work assignments as they are to the state next door.

With respect to a dollar threshold, either as a substitute or in conjunction with a day period threshold, any such threshold nullifies the potential compliance gains and simplification from a uniform federal rule. Dollar limit thresholds would require even more onerous burdens than exist in most cases under the current patchwork of state laws: each employee would have to be tracked on a daily basis as to his or her whereabouts, and such information would have to be compared with personal and highly sensitive payroll data about salaries, and then allocations of salary and other remuneration would have to be made. Dollar thresholds would render the current state-by-state system even more complicated, and should not be considered a viable solution to the need for uniform rules to enhance compliance.

As a final point on the issues presented by state policymakers, I note that HR 3359 contains several provisions that are designed specifically to protect the legitimate prerogatives of the states, such as exceptions from the uniform rule for professional athletes, entertainers and other public figures.

Why Uniform Rules are Needed Now

While states' laws addressing nonresident withholding and personal income tax liability have been on the books for many years, resolution of this issue has reached a critical stage for corporations for a number of reasons, most notably the enactment of the Sarbanes Oxley Act of 2002. Under Section 404 of the Act, company management is required to certify that processes and procedures are in place to comply with applicable laws and regulations, including state tax rules. This rule, along with a commensurate desire by corporations to be fully compliant with all rules and requirements as part of corporate governance responsibilities, has increased the interest of business in desiring uniformity and simplicity in matters of nonresident state income and withholding laws.

Furthermore, businesses have a significant interest in ensuring that employees comply with all state law taxation requirements. COST members are acutely aware of the burdens placed on their employees who travel outside their resident states for business. They have expressed a strong desire to meet their responsibilities as employers by assuring their employees comply with these burdens. Unfortunately, the current patchwork of state rules renders employees' abilities to comply with nonresident state law requirements extremely challenging.

Can the States Resolve These Issues Without a Federal Rule?

In a limited manner, some states have resolved the issue on a regional basis, typically with adjoining states through the bilateral reciprocal agreements noted previously. A list of existing reciprocal agreements is set forth in Exhibit B to my testimony. These existing agreements are helpful in discrete regional situations, but fall well short of solving a problem that is nationwide in scope. We believe that it would be extremely difficult and take many years for each of the states that impose a personal income tax to pass a uniform set of laws governing both the income tax liability of the nonresident employee and the employer's commensurate withholding obligations. Although the states might as an administrative matter be in a better position to promulgate uniform withholding rules, such collaborative administrative relief on behalf of the states without creating companion symmetrical rules for employees' personal income tax liability through extremely time consuming state-by-state legislation would, in reality, provide no real benefit to either employees or employers. As a result, we believe the only way to secure a nationwide resolution of the issues is to provide a uniform and simple set of rules established under federal guidelines.

HR 3359 – Explanation of Provisions

First and foremost, HR 3359 provides that all wages and other remuneration paid to an employee would be subject to the income tax laws in the state or locality of the employee's residence. In addition, under the legislation wages and other remuneration are also subject to tax in the state or locality in which the employee is physically present performing duties for more than sixty days in a calendar year, and employers would be subject to commensurate withholding requirements of that nonresident state. The sixty day threshold does not apply to professional athletes, professional entertainers, or certain public figures who, because of their national prominence, are paid on a per-event basis to give speeches or similar-type presentations. For example, a professional football player would be subject to nonresident state personal income taxes for performance in an athletic event. As another example, a well-known author who is an employee of a speakers' organization would be subject to nonresident state income taxes for making a presentation in a state and receiving compensation based on that event. In both of these cases, their respective employers would be subject to the nonresident state withholding requirements.

An employer may rely on an employee's determination of the time spent in a nonresident state absent knowledge of employee fraud or collusion between the employer and employee. If an employer, however, at its discretion, maintains a time and attendance system tracking where employees perform their services, such system must be used instead of the employee's determination.

An employee is considered to be in a state or locality for a "day" if the employee performs more than fifty percent (50%) of his or her duties in such state or locality for such day.

The terms "employee" and "wages or other remuneration" are defined by the state or locality in which the employment duties are performed. These references to state law protect the prerogatives of the state, and we believe it is the overall intention of the legislation to make the least incursion practicable in current state withholding and personal income tax rules and regulations.

Impact on State Taxes

With respect to the impact of HR 3359 on state revenues, in some states, the nonresident taxes currently collected exceed the tax credits provided to residents. In other states, the converse is true. In the majority of states, the net impact is not significant as a percentage of the state's overall tax receipts. I have included a detailed explanation of the impact on state tax receipts and a state-by-state analysis as prepared by Ernst & Young, LLP as Exhibit C to my testimony. As noted in the fiscal impact analysis, twenty-nine states either gain revenue or have net reductions of less than two hundredths of one percent (0.02%). The impact of the legislation results in a redistribution of income taxes between resident and nonresident states with only a very slight reduction in total income taxes collected by the states. For all fifty states and the District of Columbia combined, the net change is only a reduction of one hundredth of one percent (.01%), which accrues as a net reduction in overall personal income taxes.

Why is there a net reduction in overall personal income taxes? Under H.R. 3359, employees whose work responsibilities in nonresident states are under the sixty day threshold period would experience a reduction in personal income taxes under the following two circumstances: (1) to the extent the employee's resident state imposes tax at a lower rate than the nonresident state or (2) when a nonresident state tax is imposed on an employee whose resident state does not also impose a personal income tax.

Conclusion

The sixty day threshold period and other operating rules provided in H.R. 3359 respond to an immediate need for uniformity in the nonresident state taxation of employees. The uniform rules will greatly enhance compliance and provide simplicity in administration for employers and employees alike. The legislation is further structured to protect state taxation prerogatives to the greatest extent possible. Chairwoman Sanchez, I thank you again for the opportunity to present this testimony before the Subcommittee today. I welcome any questions that you or other Subcommittee Members would like to discuss.

Exhibit A – Nonresident Personal Income Taxes

Key

Non-Resident Withholding Required — NO *de minimis* rule

Non-Resident Withholding Required — *de minimis* rules / safe harbors

Non-Resident Withholding NOT Required (only Washington, D.C.)

No personal Income Tax (thus, no withholding and no credits for taxes paid to other states)

States currently have widely inconsistent standards regarding state income tax withholding requirements. In general terms, listed below are the various exemption threshold levels utilized by the states when determining whether an employer must withhold on a nonresident's wages. Exemption thresholds generally fall into two categories: a set number of days or a dollar threshold (a few states use both).

State Exemption for Nonresident Personal Income Tax Withholding Measured by Days:

Arizona:	Withholding is not required if the nonresident is physically present in the state for less than 60 days in a calendar year.
Georgia:	Withholding is not required if the nonresident has been employed in the state for 23 days or less in a calendar quarter and the remuneration for services performed in the state do not exceed the lesser of 5% of total income received by the nonresident in the taxable year or $5,000.
Hawaii:	Withholding is not required if the nonresident employee is performing services in the state for no more than 60 days.
Maine:	Withholding is not required if personal services are performed in the state for 10 days or less.
New Mexico:	Withholding is not required if the employee is to perform services in state for 15 days or less.
New York:	Withholding is not required for wages paid for services performed in state for 14 or fewer days or for wages that will not exceed the employee's personal exemption.

State Exemption for Nonresident Personal Income Tax Withholding Measured by Dollars:

California:	Withholding is not required for wages below "Low Income Exemption Table" amounts (i.e., semi-monthly wage amount of $470 or less for 2007).
Idaho:	Withholding is not required if the nonresident will be paid below $1,000 in a calendar year for services performed in Idaho.
Maryland:	Withholding is not required for wages paid below $5,000.
Nebraska:	Withholding is not required for payments for personal services below $5,000.
New Jersey:	Withholding is not required for wages paid below an employee's personal exemption.
Ohio:	Withholding not required for wages paid below $300 in any calendar quarter.
Oklahoma:	Withholding not required for wages paid below $300 in any calendar quarter.
South Carolina:	Withholding not required for wages paid below $1,000 for the year or for wages paid below the employee's Federal personal exemption.
Virginia:	Withholding not required for wages paid below the employee's personal exemptions ($900 each) and standard deduction ($3,000 individual) or, if elected by the employee, the employee's filing threshold (single $7,000; married $14,000).
West Virginia:	Withholding not required for wages paid below employee's personal exemption amount (one exemption equals $2,000).
Wisconsin:	Withholding not required for wages paid below $1,500.

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EXHIBIT B

STATE RECIPROCITY AGREEMENTS
UPDATED as of 10/10/07

The table below summarizes the state "reciprocity agreements" that exist for non-resident withholding tax purposes. Generally, under such agreements, each signatory state agrees not to require withholding from the wages of residents of the other signatory state, regardless of the amount of work performed in the state of non-residence.

State	Agreements	Citations
Alabama	None	N/A
Arizona[1]	California, Indiana, Oregon, Virginia	Arizona Withholding Tax Ruling No. 92-3 (10/1/02); Form WEC "Withholding Exemption Certificate"
Arkansas	None	N/A
California	None	N/A
Colorado	None	N/A
Connecticut	None	N/A
Delaware	None	N/A
District of Columbia[2]	N/A -- Taxation of nonresidents prohibited by Federal law	Pub. L. No. 93-198
Florida	No Personal Income Tax	N/A
Georgia	None	N/A
Hawaii	None	N/A
Idaho	None	N/A
Illinois	Iowa, Kentucky, Michigan, Wisconsin	Form IL-1040 Instructions; Form IL-W-5-NR
Indiana[3]	Kentucky, Michigan, Ohio, Pennsylvania, Wisconsin	Ind. Admin. Code tit. 45, r. 3.1-1-115; Form WH-47; Publication WH-13
Iowa	Illinois	Iowa Admin. Code r. 701-38.13(422)
Kansas	None	N/A
Kentucky[4]	Illinois, Indiana, Michigan, Ohio, Virginia, West Virginia, Wisconsin	103 Ky. Admin. Regs. Sec. 17:010
Louisiana	None	N/A
Maine	None	N/A
Maryland	District of Columbia, Pennsylvania, Virginia, West Virginia	Form MW507 "Employee Exemption Certificate"
Massachusetts	None	N/A
Michigan	Illinois, Indiana, Kentucky, Minnesota, Ohio, Wisconsin	Michigan Form 1040 Instructions
Minnesota	Michigan, North Dakota, Wisconsin	Minnesota Form M-1 Instructions; Income Tax Fact Sheet 4 (Revised December 2006)
Mississippi	None	N/A
Missouri	None	N/A
Montana	North Dakota	Mont. Admin. R. 42.17.134; Montana Form NR-2 "Employee Certificate of

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		North Dakota Residence"
Nebraska	None	N/A
Nevada	No Personal Income Tax	N/A
New Hampshire	None	N/A
New Jersey	Pennsylvania	Form NJ-165 "Employee's Certificate of Non-Residence in New Jersey"
New Mexico	None	N/A
New York	None	N/A
North Carolina	None	N/A
North Dakota	Minnesota, Montana	Form ND-1 Instructions
Ohio	Indiana, Kentucky, Michigan, Pennsylvania, West Virginia	Form IT-4 NR "Employee's Statement of Residency in a Reciprocity State"
Oklahoma	None	N/A
Oregon	None	N/A
Pennsylvania	Indiana, Maryland, New Jersey, Ohio, Virginia, West Virginia	Form REV-420
Rhode Island	None	N/A
South Carolina	None	N/A
South Dakota	No Personal Income Tax	N/A
Tennessee	None	N/A
Texas	No Personal Income Tax	N/A
Utah	None	N/A
Vermont	None	N/A
Virginia[5]	District of Columbia, Kentucky, Maryland, Pennsylvania, West Virginia	Va. Admin. Code 10-110-250; Form 763 Instructions
Washington	No Personal Income Tax	N/A
West Virginia	Kentucky, Maryland, Ohio, Pennsylvania, Virginia	Form WV/IT-104
Wisconsin	Illinois, Indiana, Kentucky, Michigan, Minnesota	Wis. Admin. Code Sec. Tax 2.02
Wyoming	No Personal Income Tax	N/A

[1]Arizona: Arizona has no reciprocal agreements. However, due to credits it grants to nonresidents for income tax paid to certain states of residence or domicile, Arizona does not require withholding for such nonresidents.

[2]District of Columbia: Pursuant to Federal law, the District of Columbia is barred from taxing the income of nonresidents. Nonresidents who work in D.C. must file Form D-4A with their employers to confirm their exempt status. Note that Maryland and Virginia each treat D.C. as a reciprocating state.

[3]Indiana: While Indiana regulations (Ind. Admin. Code tit. 45, r. 3.1-1-115) list Illinois as a reciprocal state, this agreement was halted effective January 1, 1998.

[4]Kentucky: The agreement with Virginia only applies to taxpayers who commute daily to their employment in the nonresident state.

[5]Virginia: Pursuant to Virginia Form 763 Instructions, Virginia's agreements with D.C. and Kentucky only apply to taxpayers who commute daily to their employment in Virginia. 23 Va. Admin. Code 10-110-250 indicates that this restriction applies more broadly to other reciprocal states (the regulation was last updated in 1985).

Exhibit C

October 11, 2007

Preliminary Estimates of State-by-State Impacts of H.R. 3359

Table 1 presents state-by-state estimates of the net change in personal income taxes projected from the impact of H.R. 3359 at fiscal year 2007 levels. The estimates for each state include two components: 1) the reduction in tax collections due to the increase in the number of in-state days required before a nonresident employee is subject to taxation, and 2) the increase in tax collections due to reduced credits on resident tax returns for taxes paid in other states. Table 1 provides the change in personal income taxes in dollar terms and in terms of the net change in state personal income taxes divided by total estimated state taxes in fiscal year 2006.[1]

Thirty of the forty-four states (including the District of Columbia) with a personal income tax either gain revenue, have no change, or have net reductions less than 0.02% (two-hundreds of a percent or two-tenths of a mill) as a result of H.R. 3359. As the table illustrates, the bill redistributes income taxes between resident and nonresident states with only a very slight reduction in total income taxes collected by the states. For all fifty states and the District of Columbia combined, the net change in total state taxes is only a reduction of -.01% which accrues as a reduction in overall personal income taxes.

[1] The estimates were prepared by Ernst & Young LLP based on survey data provided by seventeen states through the Federation of Tax Administrators, as well as state tax collection data for other states from the U.S. Census *Governmental Finances* and journey-to-work data from the U.S. Census. More detailed estimates, as well as a description of the estimating methodology, are available upon request. The bill will also have a small net impact on local personal income taxes in several states. The local tax impact is not included in Table 1. FY 2006 is the latest available year for state-by-state total state tax collections.

Table 1: Preliminary Estimates of Impact of H.R. 3359		
State	Net Change as a Percent of Total State Taxes	Net Change in Millions of Dollars
Alabama	0.01%	$1
Alaska	0.00%	0
Arizona	0.02%	3
Arkansas	-0.01%	-1
California	-0.01%	-15
Colorado	-0.03%	-3
Connecticut	0.07%	9
Delaware	0.11%	3
District of Columbia	0.01%	1
Florida	0.00%	0
Georgia	-0.02%	-4
Hawaii	0.01%	0
Idaho	0.01%	0
Illinois	-0.05%	-14
Indiana	0.05%	7
Iowa	0.04%	2
Kansas	0.02%	1
Kentucky	-0.03%	-3
Louisiana	-0.04%	-4
Maine	0.00%	0
Maryland	-0.02%	-3
Massachusetts	-0.07%	-13
Michigan	-0.01%	-3
Minnesota	-0.03%	-6
Mississippi	0.03%	2
Missouri	0.03%	3
Montana	-0.01%	0
Nebraska	-0.01%	0
Nevada	0.00%	0
New Hampshire	0.00%	0
New Jersey	0.23%	57
New Mexico	0.00%	0
New York	-0.19%	-104
North Carolina	-0.01%	-3
North Dakota	-0.01%	0
Ohio	-0.02%	-5
Oklahoma	-0.02%	-1
Oregon	-0.08%	-6
Pennsylvania	0.00%	0
Rhode Island	0.24%	6
South Carolina	0.06%	5
South Dakota	0.00%	0
Tennessee	0.00%	0
Texas	0.00%	0
Utah	-0.02%	-1
Vermont	0.03%	1
Virginia	-0.01%	-3
Washington	0.00%	0
West Virginia	-0.02%	-1
Wisconsin	-0.01%	-1
Wyoming	0.00%	0
Total for All States	**-0.01%**	**-$93**

Ms. SÁNCHEZ. Thank you. We appreciate your testimony.

Ms. Nelson, you may begin your testimony.

TESTIMONY OF DEE NELSON, PAYROLL MANAGER, ALUTIIQ, LLC AND SUBSIDIARIES, ANCHORAGE, AK, ON BEHALF OF THE AMERICAN PAYROLL ASSOCIATION

Ms. NELSON. My name is Dee Nelson. And I am speaking today on behalf of the American Payroll Association in favor of H.R. 3359. The American Payroll Association is a nonprofit payroll association with more than 23,000 members. Most of our members are the payroll managers for their employers. And some of our members work for payroll service providers who in turn process the payrolls of another 1.5 million employers.

I have been a payroll professional for 17 years, of which 10 of the last have been with a multi-state company. I have been in this environment, so I know firsthand the problems that employers and employees face in trying to manage their way through multi-state tax requirements.

Even in the case of an employee who resides in one State and works throughout the year in another State, State and local tax withholding and reporting can be very complicated. The employer has to verify the employee's State of residence, check whether the two States have a reciprocity agreement, analyze the tax laws of both States, and likely withhold tax for both States and prepare a form W-2 for both States.

Of the 41 States with income tax withhold, most tax all wages earned within their borders by residents of other States. States have widely varying de minimis amounts, but need to be exceeded before withholding is required.

Just as the United States taxes its citizens and residents on their worldwide income, so do the States impose a tax on their residents who earn income outside their borders. If the employer has a business connection within the employee's State of residence, it generally must withhold tax for the State of residence in addition to the State in which the services are performed. Besides the withholding requirement, each State also has its own wage reporting requirement.

I offer this as background on how much more complicated it becomes when an employee has a temporary assignment to another State. Whenever an employer sends an employee to a worksite outside of the State in which the employee normally performs services, the requirements that are then imposed on the employer, such as to register for the withholding account and to withhold tax, creates a very burdensome process.

As a payroll professional it is my duty to ensure that taxation is happening properly for the State in which the employee is working, as well as the State in which the employee claims residency. What I do for an employee who is a California resident who temporarily goes to work in New York is completely different from what I do for the same employee if he or she goes to work in New Jersey or Georgia.

If I send an employee who is an Oregon resident to temporarily work in New York, New Jersey, or Georgia, I will be required to handle it entirely differently than I did for the California resident.

The current process is not only burdensome, but it is costly to both employees and employers.

As a multi-state employer for the company I work for, not only are we required to withhold taxes for each of the States in which our employees may temporarily work, but we also have the responsibility to register our business in each of the States in which we are required to pay the tax. The registration process for businesses can be just as burdensome as trying to manage the tax itself.

This process is very time consuming and utilizes many of my payroll department staff resources for a small group of our employees. Our employees are also burdened. Each employee has to file a State personal income tax return for each State for which tax was taken from their pay. For some of our employees, this can mean up to eight State tax returns in addition to the one for their home State.

Most of the States have thresholds of income below which no income tax is due. Payroll systems have no way of detecting the length in which an employee will be in any State, so State withholding is taken even for someone who spends only 1 week in that State out of the entire year. In such a situation, the employee, of course, has to file a State personal income tax return and will likely get a refund on all of that withholding.

So, because there is no standard time period before withholding is required, employers have to withhold tax, report wages, employees must file income tax returns, and in cases like these, States have to process wage reports and income tax returns of individuals for whom they will refund all the taxes withheld. That is a lot of time, effort, and burden with no positive return for the employer, the employee, or the State.

At my company, to assist our employees and to ensure we can keep their positions filled, we pay for preparation of their additional tax returns. This costs our company approximately $50,000 annually.

I have told you about the processes and burdens at my company. However, it certainly can be said that due to the extreme complexity of the varying current State tax regulations, there are many companies that are not withholding properly due to ignorance or due to lack of systems, personnel, time, money, or other resources to uphold the complex rules.

More employers will comply with a law that is uniform across all States and localities and that is federally supported, versus the current patchwork of laws of which an employer might not even be aware. The American Payroll Association and its 23,000 members strongly recommend that this legislation be considered and enacted.

And I thank you for your time you have allowed me today. And I hope to see this legislation passed.

[The prepared statement of Ms. Nelson follows:]

PREPARED STATEMENT OF DEE NELSON

Statement of
Dee Nelson, CPP

Payroll Manager
Alutiiq, LLC, and Subsidiaries

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Before the
U.S. House of Representatives
Committee on the Judiciary
Subcommittee on Commercial and Administrative Law

Hearing on H.R. 3359
The Mobile Workforce State Income Tax Fairness and Simplification Act of 2007
The Honorable Linda T. Sanchez, Chair
November 1, 2007

Statement of Dee Nelson, Certified Payroll Professional

Good afternoon. My name is Dee Nelson, CPP, and I am speaking today on behalf of the American Payroll Association in favor of HR 3359, the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007.

The American Payroll Association is a non-profit professional association of over 23,000 members. Most of our members are the payroll managers for their employers, and some of our members work for payroll service providers, who in turn process the payrolls of another 1.5 million employers.

I have been a payroll professional for 17 years, and for the last 10 of those years, I have worked for multi-state employers. Having worked in this environment, I know first hand the problems that employees and employers face in trying to manage their way through the multi-state requirements to withhold proper state and local income taxes.

Even in the case of an employee who resides in one state and works throughout the year in another state, state and local tax withholding and reporting can be very complicated. The employer has to verify the employee's state of residence, check whether the two states have a reciprocity agreement, analyze the tax laws of both states, and likely withhold tax for both states and prepare a Form W-2 for both states.

Of the 41 states with income tax withholding, most tax all wages earned within their borders by residents of other states. Some have varying de minimis amounts, or thresholds, that need to be exceeded before withholding is required. The thresholds differ widely, including various numbers of days worked within the state and various wage amounts earned. (The District of Columbia has an income tax but does not impose it on nonresidents who earn wages within the District.)

Just as the United States taxes its citizens and residents on their worldwide income, so do the states impose a tax on their residents who earn income outside their borders. If the employer has nexus – that is, a business connection – within the employee's state of residence, it generally must withhold tax for the state of residence in addition to the state in which the services are performed. Again, the states vary on their requirement to withhold tax from their residents who work elsewhere. Some want full withholding, some want withholding only if there is no withholding being taken for the state in which the services are performed, and some want withholding less a credit for whatever withholding is taken for the state in which the services are performed. Besides the withholding requirement, each state also has its own wage reporting requirement.

I offer this as background to how much more complicated it becomes when an employee has a temporary assignment to another state.

Whenever an employer sends an employee to a worksite outside of the state in which the employee normally performs services, the requirements that are then imposed on the employer, such as to register for a withholding account and to withhold tax, create a very burdensome process. As a payroll professional it is my duty to ensure that taxation is happening properly for the state in which the employee is working as well as the state in which the employee claims residency. As I mentioned, there is no consistent guidance on what to do in each particular case of an employee temporarily working in a new state due to the fact that each state has its own set of tax laws and regulations applicable to non-resident workers. In addition not all states impose these regulations in the same manner, and each pairing of states (state of residence and state of service) creates a new requirement.

What I do for an employee who is a California resident who temporarily goes to work in New York is completely different from what I do for the same employee if he or she goes to work in New Jersey or Georgia. If I send an employee who is an Oregon resident to temporarily work in New York, New Jersey, or Georgia, I will be required to handle it entirely differently than I did for the California resident.

The current process is not only burdensome but costly to both employees and employers.

As a multi-state employer, not only are we required to withhold taxes for each of the states in which our employees may temporarily work, but we also have the responsibility to register our business in each of the states in which we are required to pay a tax. The registration process for businesses can be just as burdensome as trying to manage the tax itself. In the case of my company's employees, we move them from state to state numerous times a year. This work is temporary in nature and is constantly changing in terms of where, when, and for how long we send employees.

Often, we have to send our employees to a new state or locality at a moment's notice, and we will begin withholding and accumulating tax for a new jurisdiction before we have even registered our business there. Sometimes the tax has to be deposited with the jurisdiction under a status of "account applied for," and a reconciliation has to be performed once the withholding account is established.

This process is very time consuming and utilizes many of my payroll department staff resources for a small group of our employees. In order to ensure timely deposits and filings for all these states due to the temporary work situations, we have outsourced our tax filing to an outside payroll service provider. We still have the burden of tracking the employees' work locations and the time spent in each one, and that is often a manual process. Of course, the outsourcing of the tax filing has increased the cost of compliance.

Our employees are also burdened. Each employee has to file a state personal income tax return for each state for which tax was taken from their pay. For some of our employees, this can mean up to eight state tax returns in addition to the one for their home state.

Most of the states have thresholds of income – not to be confused with wages – such as a standard deduction based on filing status, below which no income tax is due. Payroll systems, of course, have no way of detecting whether an employee will be in a state for one week or three months. Rather, payroll systems generally apply withholding calculations based on an expectation that, whatever the employee earned in that jurisdiction in the current pay period, the employee will earn that much in that jurisdiction in every other pay period of the year. So, state withholding is taken, even from someone who spends only one week in that state out of the entire year. In such a situation, the employee, of course, has to file a state personal income tax return and will likely get a refund of all of that withholding.

So, because there is no standard threshold of wages as a minimum amount before withholding is required, employers have to withhold tax and report wages, employees must file income tax returns, and in cases like these, states have to process wage reports and income tax returns of individuals for whom they will refund all taxes withheld. That's a lot of time, effort, and burden with no positive return for the employer, the employee, and the state.

At my company, to assist our employees and to ensure we can keep their positions filled, we pay for the preparation of their additional tax returns. Of course, tax preparation assistance is a taxable benefit, so we have to add the value of it to our employees' wages, and, to save the employee from an additional tax burden, we pay the taxes on it on their behalf (and paying those taxes is another taxable benefit). This results in a cost of approximately $50,000 annually for our company.

I've told you about the processes and burdens at my company. However, it certainly can be said that, due to the extreme complexity of the varying current state tax regulations, there are many companies that are not withholding properly due to ignorance or due to lack of systems, personnel, time, money, or other resources to uphold the complex rules. More employers will comply with a law that is uniform across all states and localities and that is federally supported, versus the current patchwork of laws of which an employer might not even be aware.

The American Payroll Association and its 23,000 members strongly recommend that this legislation be considered and enacted so that the burden and cost of administering multi-state taxes by American workers and American businesses can be reduced and so that we can ensure fair and consistent handling of this employment issue and the related taxes across the nation.

I thank you for the time you have allowed me to speak to you and look forward to watching this important legislation pass.

Multi-State Income Taxation: For Which State Must You Withhold?

If your company has operations in more than one state, you may be faced with income tax withholding for more than one state. Sometimes, you may even have to withhold income tax for more than one state from the same employee. Withholding can get even more complicated when you have employees who live in a different state than the one they work in or who perform services in more than one state.

Deciding which state's income tax to withhold can be a confusing process. How do you determine who is a resident and whether you should follow the laws of the state of residence or the laws of the state in which services are performed? Not all states answer these basic questions in the same way and, sometimes, state laws conflict. Even the simple word "operations," as used in the paragraph above, is more complex than you might think.

From a basic rule of thumb to three rules

The default rule of state income tax withholding that can be used as a starting point is to withhold income tax for the state in which services are performed. It can be applied in most situations in which the employee lives and works in the same state (assuming it is not one of the nine states without income tax withholding: Alaska, Florida, Nevada, New Hampshire, South Dakota, Tennessee, Texas, Washington, and Wyoming).

However, up to three other withholding rules may have to be considered when the situation is not as straightforward. For example, an employee who lives and works in one state may still be a resident of some other state; that's where withholding Rule No. 1 comes into play. In this scenario, the employee may have income tax liability for the state of residency, and, if you have operations in that state and meet certain other criteria, you may be required to withhold for that other state. On the next level, if an employee lives in one state and works in another, each state's laws of reciprocity (withholding Rule No. 2) and resident/non-resident taxation policies (withholding Rule No. 3) must be examined.

Withholding Rule No. 1: Resident defined

The very first determination that must be made is the state of residence of the employee. This is primary because a resident of a state is subject to the laws of that state, including its income tax laws. Furthermore, states have varying policies on withholding from residents who perform services in another state and from nonresidents who perform services within the state. To locate and apply the policies correctly, you'll need to know which state(s) can claim the employee as a resident.

Employees commonly claim that they are a resident of their "home" state. If the employee has relocated to work for you, he/she may assert that the former state is his/her state of residence because he/she still has a home and family there (and doesn't want to complete personal income tax returns for two states). An employee who works for you only during the nine months of the school year, for example, might try to claim that she is a resident of the state she grew up in but in which she now spends only three months of the year. This may be especially likely if her home state doesn't have an income tax.

It's up to you to locate and follow the rules of the appropriate state. Most states have a two-pronged definition of residency, outlining that someone will be a resident by either:

- being domiciled in the state, or
- spending more than a certain number of days in the state.

The term "domicile" usually means the place where an individual has a true, fixed, permanent home and principal establishment, and it usually means the place to which the individual intends to return. Common indicators that an individual is domiciled in a particular location include:

- property ownership,
- bank accounts,
- driver's license and vehicle registration,
- voting registration,
- presence of family, and
- club and church memberships.

Who is a Resident?

STATE DEFINITIONS OF A RESIDENT FOR INCOME TAX WITHHOLDING	
State	**Definition**
Alabama	A person having a permanent place of abode or who is domiciled in the state and spends more than 7 months a year in the state.
Alaska	Not applicable.
Arizona	A person domiciled or who spends more than 9 months a year in the state, unless there for a temporary or transitory purpose.
Arkansas	A person domiciled or who maintains a residence and spends 6 months a year in the state.
California	A person domiciled in the state or in the state for other than a temporary or transitory purpose (Franchise Tax Board Publication 1031 explains "temporary or transitory"). A person working on a contractual foreign assignment and in California for no more than 45 days in any consecutive 18-month period is not a resident.
Colorado	A person who maintains a permanent place of abode or who is domiciled in the state and spends at least 6 months of the year in the state.
Connecticut	A person who is domiciled or has a permanent place of abode and spends more than 183 days of the year in the state. Excludes certain individuals domiciled in the state but present in a foreign country for at least 450 days during any period of 548 consecutive days.
Delaware	A person who is domiciled, maintains a permanent place of abode, and spends more than 183 days of the year in the state. A person who is in a foreign country for at least 495 full days in any consecutive 18-month period, is not present in Delaware for more than 45 days during that period, and does not have a permanent place of abode in Delaware where a spouse, children or parents are present for more than 45 days during that period, is not a resident.
Dist. of Col.	A person who is domiciled in D.C., or who has a place of abode in D.C.

STATE DEFINITIONS OF A RESIDENT FOR INCOME TAX WITHHOLDING	
State	**Definition**
Florida	Not applicable.
Georgia	Anyone who is a legal resident on income tax day, resides in the state on a regular basis (not temporary or transitory), or resided in the state for 183 days of the immediately preceding 365 days.
Hawaii	Any person domiciled or residing in the state; to "reside" in the state means to be in the state for other than a temporary or transitory purpose and for more than 200 days of the year.
Idaho	A person who is domiciled or maintains a place of abode in Idaho for the entire year and spends more than 270 days of the year in Idaho.
Illinois	Any person who is domiciled in the state or in the state for other than a tempo-rary or transitory purpose during the year.
Indiana	Anyone who resides in Indiana for the entire year, or has a permanent place of abode in Indiana and spends more than 183 days of the year in the state.
Iowa	A person domiciled in or maintaining a permanent place of abode in the state.
Kansas	A person domiciled in or spending more than 6 months of the year in the state.
Kentucky	A person who is domiciled, maintains a permanent place of abode, and spends more than 183 days of the year in the state.
Louisiana	Anyone domiciled, maintaining a permanent place of abode, or spending more than 6 months of the year in the state.
Maine	A person who is domiciled, maintaining a permanent place of abode, and spending more than 183 days of the year in the state.
Maryland	A person who is domiciled in Maryland on the last day of the year, or has a place of abode in Maryland for more than 6 months of the year regardless of domicile.
Massachusetts	A person who is domiciled in the state, or who maintains a permanent place of abode and spends more than 183 days of the year in the state.
Michigan	A person who lives in the state at least 183 days of the tax year (or more than half the days for a tax year of less than 12 months).
Minnesota	A person domiciled in or who maintains a place of abode in the state and spends more than one-half of the year in the state.
Mississippi	A person domiciled or who has a residence in the state.
Missouri	A person domiciled or who has a permanent place of abode in Missouri and spends more than 183 days of the year in the state.
Montana	A person who has a domicile or who maintains a permanent place of abode within the state and is temporarily absent but has not established a permanent residence elsewhere.
Nebraska	A person who is domiciled in or who has a permanent home in Nebraska and spends more than 6 months of the year in the state.
Nevada	Not applicable.
New Hampshire	Not applicable.

STATE DEFINITIONS OF A RESIDENT FOR INCOME TAX WITHHOLDING	
State	**Definition**
New Jersey	Any person domiciled in the state for the full year or who has a permanent home in the state and spends more than 183 days of the year in the state.
New Mexico	An individual domiciled in New Mexico during all of the tax year, or an individual who is physically present in New Mexico for a total of 185 days or more in the aggregate during the tax year, regardless of domicile (i.e., the place where an individual has a true, fixed, permanent home); an individual domiciled in New Mexico who is physically present in New Mexico for fewer than 185 days and moves out-of-state with the intention of living there permanently is not a resident for the period after the change of domicile.
New York	A person who is domiciled in the state, unless: (1) the person does not have a permanent place of abode in New York, has a permanent abode elsewhere, and spends no more than 30 days of the year in the state; or (2) is in a foreign country or countries for at least 450 out of 548 consecutive days (approximately 15 out of 18 months), is not in New York for more than 90 days during the 548-day period, and does not have a permanent residence in the state where a spouse or children live for more than 90 days during the 548 day period.
North Carolina	A person domiciled in the state during any part of the year or who resides in the state for other than a temporary or transitory purpose. A person living in the state for more than 183 days of the tax year is presumed to be a resident.
North Dakota	A person domiciled, or who maintains a permanent place of abode within the state and spends more than 7 months of the year in the state.
Ohio	A person domiciled in or who maintains a permanent place of abode in the state.
Oklahoma	A person who maintains a permanent place of abode, or is domiciled in the state and spends more than 7 months of the year in the state.
Oregon	A person domiciled in Oregon or who maintains a permanent place of abode in Oregon and spends more than 200 days of the year in the state.
Pennsylvania	A person who is domiciled in the state (unless a permanent place of abode is maintained elsewhere and no more than 30 of the year days are spent in the state) or who has a permanent place of abode in the state and spends more than 183 days of the year in the state.
Rhode Island	A person who is domiciled in or who maintains a permanent place of abode in the state and spends more than 183 days of the year in the state.
South Carolina	A person domiciled in the state.
South Dakota	Not applicable.
Tennessee	Not applicable.
Texas	Not applicable.
Utah	A person who is domiciled in or who maintains a permanent place of abode in Utah and spends more than 183 days of the year in the state.
Vermont	A person who is domiciled or who maintains a permanent place of abode in Vermont and spends more than 183 days of the year in the state.
Virginia	A person who is domiciled or who maintains a permanent place of abode in Virginia and spends more than 183 days of the year in the state.

STATE DEFINITIONS OF A RESIDENT FOR INCOME TAX WITHHOLDING	
State	**Definition**
Washington	Not applicable.
West Virginia	A person who is domiciled (unless he/she has a permanent place of abode elsewhere and spends no more than 30 days of the year in the state) or who maintains a permanent place of abode and spends more than 183 days of the year in the state.
Wisconsin	A person who is domiciled in the state or in the state for other than a temporary or transitory purpose.
Wyoming	Not applicable.

Withholding Rule No. 2: Reciprocity

If an employee performs services in a state other than the state of residence, you must find out whether the two states have a reciprocal agreement. A reciprocal agreement allows you to withhold only for the state of residence, as opposed to the state in which services are performed. (This is an example of why the rule of thumb is only a starting point.) Accordingly, you would report wages only to the state of residence when completing Boxes 16-17 (state wages) of federal Form W-2, *Wage and Tax Statement*. In most cases, the employee will be required to submit a certificate of non-residence for the state in which he/she works before you can honor the reciprocal agreement.

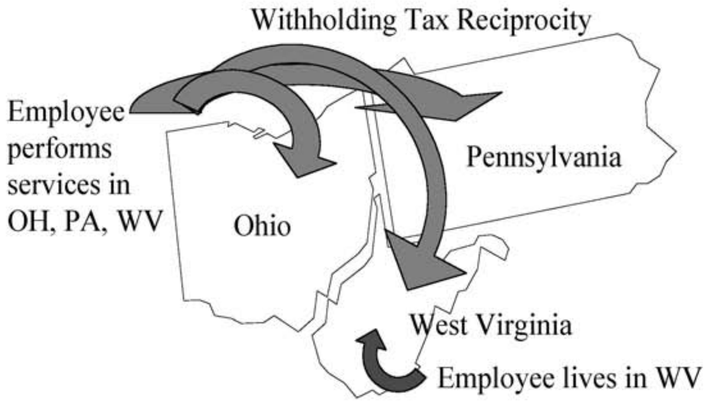
The general purpose of reciprocity is to make things administratively easier for the employee and employer. The employee will have to file only one state personal income tax return, and the employer will withhold only for the state in which the employee lives. This is especially helpful if you have an employee who performs services in two or more states that have reciprocity with the state of residence. For example, for an employee who lives in Kentucky, works in Kentucky, Illinois, and Indiana, and submits certificates of non-residence for Illinois and Indiana, the employer will need to withhold only Kentucky income taxes because the three jurisdictions have reciprocal agreements with each other. Without reciprocity, the employer would have to withhold for all three jurisdictions based on the time worked in each one. On the other hand, the presence of a reciprocal agreement requires you to change the state of withholding and reporting if the employee moves his/her residence from one state to another, even though there has been no change in the state in which the services are performed.

Reciprocal Coverage

RECIPROCAL WITHHOLDING AGREEMENTS BETWEEN STATES	
State	**Reciprocal Agreements**
Alabama	None
Alaska	Not applicable.
Arizona	None
Arkansas	Border city exemption for residents of Texarkana, which is located on the border of Texas and Arkansas. Residents of Texarkana, Arkansas are exempt from Arkansas state income tax and withholding. Residents of Texarkana, Texas are exempt from Arkansas income tax for wages earned in Texarkana, Arkansas. Agreement does not apply to residents of other cities or other Texas residents working in other parts of Arkansas. Employer must supply Form AR-4EC (TX), *Texarkana Employee's Withholding Exemption Certificate.* Employer copy filed with Form AR-3Q-TEX.
California	None
Colorado	None
Connecticut	None
Delaware	None
District of Columbia	A reciprocal agreement is in effect with Maryland and Virginia. Non-resident employees of DC are not subject to DC withholding and must file Form D-4A, *Certificate of Non-Residence in the District of Columbia.*
Florida	Not applicable.
Georgia	None
Hawaii	None
Idaho	None
Illinois	Residents of Iowa, Kentucky, Michigan and Wisconsin are not subject to Illinois income tax withholding for wages earned in Illinois if Form IL-W-5NR, *Employee's Statement of Non-Residence in Illinois,* is filed with the employer. The reciprocal agreement with Indiana expired at the end of 1997.
Indiana	Residents of Kentucky, Michigan, Ohio, Pennsylvania, and Wisconsin are exempt from Indiana income tax withholding. They should complete Form WH-47, *Certificate of Residence.* The reciprocity is not applicable to county income taxes. The reciprocal agreement with Illinois expired at the end of 1997.
Iowa	Residents of Illinois have Illinois state tax withheld only if Form 44-016, *Employee's Statement of Nonresidence in Iowa*, is filed with the employer.
Kansas	None
Kentucky	Residents of Illinois, Indiana, Michigan, Ohio, West Virginia, and Wisconsin have only their resident state tax withheld if Form 42A809, *Certificate of Nonresidence*, is filed with the employer. Daily commuters between Kentucky and Virginia are provided reciprocal benefits.
Louisiana	None
Maine	None

RECIPROCAL WITHHOLDING AGREEMENTS BETWEEN STATES	
State	**Reciprocal Agreements**
Maryland	No Maryland tax is withheld from employees who commute daily to Maryland and reside in the District of Columbia, Pennsylvania, Virginia and West Virginia. A certificate of nonresidence (Form MW 507, *Employee Exemption Certificate*) must be filed with the employer.
Massachusetts	None
Michigan	Michigan employers do not withhold Michigan state income tax from residents of Illinois, Indiana, Kentucky, Minnesota, Ohio, and Wisconsin. Michigan employees must file certificates of nonresidence to be exempt from withholding. A form is not provided.
Minnesota	Residents of Michigan, North Dakota, and Wisconsin are exempted from Minnesota withholding. Form MW-R, *Reciprocity Exemption from Minnesota Withholding, Affidavit of Residency*, is required to certify residency.
Mississippi	None
Missouri	None
Montana	Montana employers are not required to withhold Montana income tax from residents of North Dakota. A certificate of North Dakota residency is required (Form NR-2, *Employee Certificate of North Dakota Residence*).
Nebraska	None
Nevada	Not applicable.
New Hampshire	Not applicable.
New Jersey	Pennsylvania residents filling out a certificate of nonresidence (Form NJ-165, *Employee's Certificate of Non-Residence in New Jersey*) are not subject to New Jersey withholding.
New Mexico	None
New York	None
North Carolina	None
North Dakota	Residents of Minnesota and Montana working in North Dakota are not required to have North Dakota tax withheld. Form NDW-R, *Affidavit of Residency*, should be filed with their employer annually.
Ohio	Ohio has reciprocal agreements with Indiana, Kentucky, Michigan, Pennsylvania, and West Virginia. Form IT-4 NR, *Employee's Statement of Residency in a Reciprocity State*, must be filed with the employer to claim the exemption.
Oklahoma	None
Oregon	None
Pennsylvania	Pennsylvania has reciprocal agreements with Indiana, Maryland, New Jersey, Ohio, Virginia, and West Virginia. Form REV-420, *Employee's Statement of Nonresidence in Pennsylvania and Authorization to Withhold Other State's Income Tax*, must be filed with the employer. For New Jersey residents who work in Pennsylvania, the amount of any Pennsylvania local income tax withholding reduces the amount of New Jersey income tax to be withheld from those same wages.

RECIPROCAL WITHHOLDING AGREEMENTS BETWEEN STATES	
State	**Reciprocal Agreements**
Rhode Island	None
South Carolina	None
South Dakota	Not applicable.
Tennessee	Not applicable.
Texas	Not applicable.
Utah	None
Vermont	None
Virginia	Full reciprocal agreement with West Virginia but a certificate of nonresidence in Virginia must be filed. Daily commuters from District of Columbia, Kentucky, and Maryland filing a certificate of nonresidence are exempt from Virginia tax. Pennsylvania and West Virginia residents can file the certificate only if subject to the state income of the resident state.
Washington	Not applicable.
West Virginia	Reciprocal agreements are in place with Kentucky, Maryland, Ohio, Pennsylvania, and Virginia. A *West Virginia Certificate of Nonresidence* (found on the back of Form WV/IT-104) must be filed with the employer.
Wisconsin	Illinois, Indiana, Kentucky, Michigan and Minnesota residents working within Wisconsin must provide a written statement to their employer certifying the place of residence in order for the employer to not withhold Wisconsin income tax. Minnesota residents are required to fill out Form W-222, *Statement of Minnesota Residency*, annually. Others must fill out Form W-220, *Nonresident Employee's Withholding Reciprocity Declaration.*
Wyoming	Not applicable.



Report all wages on W-2 for West Virginia and withhold West Virginia tax from all wages, as West Virginia has reciprocal agreements with each of Ohio and Pennsylvania. Employee will have had to have submitted to employer the Ohio and Pennsylvania forms that declare non-residence in those states.

Nexus: business connection

The word "nexus" literally means "connection." Nexus is established by having a business presence in a state. An office, store, or factory will create nexus, as will the mere entry of an employee into a state to make a sale or perform a service call.

In the withholding context, the employer's concern is whether it has a business connection, or any operations, within a state. If it does, it is subject to the withholding laws of that state. This will make the difference in whether an employer has to withhold income tax for an employee's state of residence even though he or she performs no services there.

If an employer does not have nexus with an employee's state of residence, but there is a reciprocal agreement between the two states, then the employer must honor the reciprocity agreement and not withhold income tax for the state where the employee works. However, the employer is not obligated to withhold income tax for the state where the employee lives because the employer does not have nexus with the resident state (the employee will have to make estimated payments).

If an employer does not have nexus in a state for which one of its employees will have a personal income tax liability, it can choose to establish a withholding account in that state and begin withholding as a courtesy to its employees. However, the payroll department should check with the corporate tax and legal departments of the company first because once you voluntarily register for one tax, you may receive inquiries from the state about other taxes for which you are not liable, such as sales tax or corporate income tax. Also, in some states, withholding and paying over taxes may thereby establish nexus, making your company open to being sued in the courts of that state.

Withholding Rule No. 3: Resident/non-resident taxation policies

If an employee is a resident of one state but performs services in another, and there is no reciprocal agreement, you must consider the laws of both states. The correct determination of the state of residency (Rule No. 1) is very important in these situations because it tells you which state's laws you may need to consider in addition to those of the state in which the employee works.

The state in which the services are performed will almost always require withholding from non-residents who come into the state to work (withholding only from the wages for services performed in that state). A few states have exceptions to this, usually based on whether the employee works in the state for less than a certain length of time or earns less than a certain amount of money. For example, if a California resident works in Arizona, Arizona withholding is required if the employee is physically present in the state for 60 days or more. In general, an employer is always subject to the laws of any state in which it has an employee performing services, whether or not the employer has a facility (such as an office, factory, or store) in the state.

The employee's state of residence may also need to be considered even if the employee doesn't work there. If the employer has a business connection, also referred to as "nexus," with the state in which the employee resides, then the employer is subject to the laws of that state even if the employee doesn't work there. For example, if the California resident works exclusively in Arizona for six months, and if the employer has nexus with California:

- Arizona withholding is required (the 60-day threshold is exceeded), and
- California withholding is required, with a credit for income tax withheld for the work-state (in this case, Arizona).

In this situation, the employer must first calculate and withhold Arizona income tax. Then the employer must calculate California income tax on the same wages and, if the California tax is greater, withhold an amount equal to the difference between the California income tax and the Arizona income tax. If the California tax is less than the Arizona tax, no California tax need be withheld.

If, however, the employer does not have nexus with California, then the employer is not subject to the laws of that state and is not required to withhold that state's income tax. However, the employee may have personal income tax liability on these and all other earned wages by virtue of being a resident of that state.

Employees working in multiple states without reciprocity

If an employee works in multiple states that do not have reciprocity with the employee's state of residence, then the amount of wages earned in each state must be separately examined under withholding Rule No. 3. The first step is to split the wages by state, which may be done by the number of hours worked for an hourly employee or days worked for a salaried employee, or by the sales volume for a commissioned salesperson. The employer will definitely have nexus in the state in which services are performed and will most likely (depending on the state's law) need to withhold the work-state's tax from the wages earned within the state. In addition, if the employer has nexus in the employee's resident-state, it may need to consider withholding for that state from these wages as well.

There are exceptions to this process under the Amtrak Reauthorization and Improvement Act of 1990 (Pub. L. 101-322). Railroad and motor carrier employees (i.e., operators of a commercial motor vehicle, like a tractor, trailer, or semitrailer) who work in more than one state are subject only to the state and local income tax laws of their state of residence, regardless of where they work. Employees in air transportation are subject to withholding for their state of residence and any other state in which they earn more than half of their wages.

Under Pub. L. 106-89, merchant mariners employed in interstate commerce are subject to the state and local income taxes of their state of residence.

WITHHOLDING ON RESIDENTS WORKING OUT-OF-STATE AND NONRESIDENTS		
State	**Residents: Withholding Required on Services Performed Out-of-State (and Wage Reporting Requirement), If Nexus**	**Nonresidents: Withholding Required on Services Performed In-State**
Alabama	Yes (report on Form W-2), unless withhold for the state where services are performed (then don't report on Form W-2); AL tax must be withheld if no tax is withheld for the other state.	Yes; if the nonresident works partly within and partly outside AL withhold only on the portion of wages earned in AL.
Alaska	Not applicable.	Not applicable.
Arizona	No, but employer may withhold where services are performed if requested by employee on Form A-4V (withholding for either state should be separately reported on Form W-2).	Yes, if physically present in the state for 60 days or more in the calendar year, but see reciprocity. If a nonresident works partly within and partly outside AZ, only the wages earned in AZ are subject to AZ withholding.
Arkansas	No, provided the other state imposes an income tax (don't report on Form W-2); if the other state has no income tax, AR tax must be withheld on the out-of-state wages (and must be reported on Form W-2).	Yes, but see reciprocity. If a nonresident works partly within and partly outside AR only the wages earned in AR are subject to AR withholding.

WITHHOLDING ON RESIDENTS WORKING OUT-OF-STATE AND NONRESIDENTS		
State	**Residents: Withholding Required on Services Performed Out-of-State (and Wage Reporting Requirement), If Nexus**	**Nonresidents: Withholding Required on Services Performed In-State**
California	Yes. If a resident's services are taxable in both CA and another state, first withhold as required by the other state, and then for CA withhold only the amount by which the CA withholding exceeds the withholding amount for the other state; or, do not withhold any CA PIT if the withholding amount for the other state equals or exceeds the withholding amount for CA. Report wages on Form W-2 and on quarterly Form DE 6.	Yes. If a nonresident performs services partly within and partly outside of CA, only the wages earned in CA are subject to CA PIT withholding; the amount of wages subject to PIT withholding is that portion of the total number of working days employed in CA compared to the total number of working days employed in both CA and the other state. Report all PIT wages and PIT withheld on Form DE 6.
Colorado	No, provided income tax is withheld for the state where services are performed (don't report on Form W-2); CO withholding is required if no state income tax is withheld for the work state (and CO wages must be reported on Form W-2).	Yes.
Connecticut	Yes, but only to the extent the CT withholding exceeds the withholding amount for the state where services are performed (report all wages on Form W-2). The CT resident will receive credit from CT for income tax paid to the other state for work performed in the other state (amounting to the lesser of the tax paid to the other state or the tax CT imposes on the out-of-state wages).	Yes, but only on that portion of the employee's wages that relate to services performed in CT.
Delaware	No, but the employee may elect to have DE tax withheld (if so, withhold first for the work state and then for DE, reducing DE withholding by the amount withheld and paid to the other state; report all wages on Form W-2).	Yes.
District of Columbia	Yes; an employee may claim a personal income tax credit for any income tax paid to another state for services performed there (report all wages on Form W-2).	No; non-resident employees working in DC are not subject to DC withholding and must file Form D-4-A, *Certificate of Non-Residence in the District of Columbia.*
Florida	Not applicable.	Not applicable.

WITHHOLDING ON RESIDENTS WORKING OUT-OF-STATE AND NONRESIDENTS		
State	**Residents: Withholding Required on Services Performed Out-of-State (and Wage Reporting Requirement), If Nexus**	**Nonresidents: Withholding Required on Services Performed In-State**
Georgia	Yes, unless income tax is required to be withheld for the work state (report all wages on Form W-2).	Yes, if the nonresident works more than 23 days in a calendar quarter in GA, or if 5% of total earned income is attributable to GA or the remuneration is more than $5,000.
Hawaii	Yes, even if tax is withheld by the work state on the same wages, but only if the regular place of employment is in HI or wages are paid from an office within HI (don't report the wages on Form W-2). A HI resident may receive credit on his/her personal income tax return for taxes paid to another state.	Yes, unless (1) the employee will perform services in HI for not more than 60 days in the calendar year, (2) he/she is paid from an office outside HI, (3) his/her regular place of employment is outside HI, and (4) the employer does not reasonably expect the employee to perform services in HI for more than 60 days during the calendar year; if all conditions are met except the 60-day requirement and the Director of Taxation finds that withholding would be burdensome or enforcement impractical, an exception from the withholding requirement may be allowed.
Idaho	Yes, withhold for the work state; but if the work state has no income tax then withhold for ID (report all wages earned in either state on Form W-2 even if no tax is withheld for the particular state).	Yes, unless employee earns less than $1,000 in the year in ID or is exempt from federal income tax withholding (report all ID wages on Form W-2 even if no ID tax is withheld).
Illinois	Yes, if the employee's services are localized in IL (e.g., the out-of-state services are incidental to primary services the employee performs in IL), or, the services are not localized in any state but some services are performed in IL, and either the base of operations is in IL or the place from which the services are directed or controlled is in IL (report all wages on Form W-2). Withholding is also required if the employee's service is not localized in any state but some of the service is performed in IL, the base of operations or direction or control is not in any state in which some part of the service is performed, and the employee is an IL resident.	Yes, but see reciprocity. If the employee is a resident of a non-reciprocity state, IL income tax must be withheld on all income that is paid in IL if the services are performed entirely within IL. If the services are performed both inside and outside of Illinois, but the services performed outside IL are "incidental" to those performed in IL, all wages are subject to IL withholding. If the services performed outside IL are not "incidental" to those performed in IL, then the wages will only be subject to IL withholding if the employer has its base of operations in IL or the employee's services are controlled or directed from the employer's IL location.

WITHHOLDING ON RESIDENTS WORKING OUT-OF-STATE AND NONRESIDENTS		
State	**Residents: Withholding Required on Services Performed Out-of-State (and Wage Reporting Requirement), If Nexus**	**Nonresidents: Withholding Required on Services Performed In-State**
Indiana	Yes (report all wages on Form W-2).	Yes, but see reciprocity. Nonresidents working in IN must submit a completed Form WH-47 to the employer identifying the state of residence.
Iowa	Yes, withhold for the state in which the wages were earned, except Illinois which has a reciprocal agreement with Iowa (report all wages on Form W-2 for the work state(s)).	Yes, but see reciprocity.
Kansas	Yes, withhold from total wages the amount of KS tax due less the amount required to be withheld for the other state; if the other state's withholding amount is more, then no KS withholding tax is due (don't report on Form W-2).	Yes. If the nonresident performs services both within and outside of KS, withhold only on the wages earned in KS (determine withholding using the apportionment formula found on Form K-4C, *Kansas Nonresident Employee Certificate for Allocation of Withholding Tax,* submitted by the nonresident employee).
Kentucky	Yes (report all wages on Form W-2).	Yes, but see reciprocity.
Louisiana	Yes (report the wages on Form W-2), unless withholding is required in the state where the services are performed (then don't report the wages on Form W-2).	Yes. If a nonresident works partly within and partly outside LA, only the wages paid for services performed in LA are subject to LA withholding provided the employee files Form R-1300 (L-4), Employee's Withholding Exemption Certificate with the employer (if no certificate is filed then all of the wages paid to the employee are subject to LA withholding).
Maine	Yes (report all wages on Form W-2).	Yes, provided the nonresident works in ME for at least 10 days during the year. If the nonresident works partly within and partly outside of ME, withhold only on the ME source income.
Maryland	Not required if the employee is subject to withholding in the work state (and can receive personal income tax credit against the MD tax liability for taxes paid to the work state).	Yes, but see reciprocity.
Massachusetts	Yes, less any amount required to be withheld by the other state (report all wages on Form W-2 but do not send it to the state; also report all wages on quarterly Form WR-1).	Yes. For nonresidents who work partly within and partly outside of MA, withhold only on wages earned in MA.

WITHHOLDING ON RESIDENTS WORKING OUT-OF-STATE AND NONRESIDENTS		
State	**Residents: Withholding Required on Services Performed Out-of-State (and Wage Reporting Requirement), If Nexus**	**Nonresidents: Withholding Required on Services Performed In-State**
Michigan	Yes, with personal income tax credit for any taxes paid to the other state (report all wages on Form W-2).	Yes, but see reciprocity.
Minnesota	Yes, if federal income tax withholding from the employee's wages is required (report all wages earned on Form W-2), but see reciprocity.	Yes, but see reciprocity.
Mississippi	Yes (report separately the wages earned in each state and the amount withheld for each state on Form W-2), unless withholding is required by the work state (then don't report on Form W-2).	Yes. If the nonresident's principal place of employment is outside MS but he/she works partly within and partly outside of MS, only wages for work performed in MS are subject to withholding. If the nonresident's principal place of employment is within MS but he/she occasionally works outside of MS, withhold MS tax on total wages unless withholding is required by the other state.
Missouri	Yes, if the work state does not have a state income tax (report the wages on Form W-2); if work is performed partly within and partly outside MO only wages paid for work performed in MO is subject to MO withholding provided the work performed in the other state is subject to the other state's income tax.	Yes if all work is performed in MO. If work is performed partly within and partly without MO, only wages paid for work done in MO is subject to MO withholding provided the employee files Form MO W-4A, *Certificate of Nonresidence/ Allocation of Withholding Tax.*
Montana	Yes, even if the employee is subject to withholding in the work state (report all wages on Form W-2).	Yes, but see reciprocity.

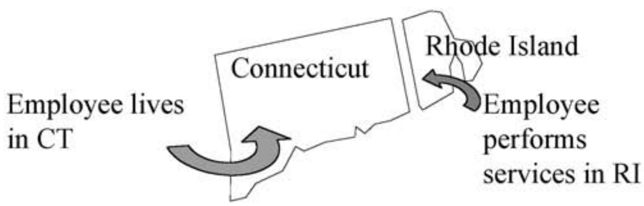
WITHHOLDING ON RESIDENTS WORKING OUT-OF-STATE AND NONRESIDENTS		
State	**Residents: Withholding Required on Services Performed Out-of-State (and Wage Reporting Requirement), If Nexus**	**Nonresidents: Withholding Required on Services Performed In-State**
Nebraska	Yes; withhold from total wages the amount of NE income tax less the amount required to be withheld for the other state(s) (report all wages on Form W-2).	Yes, a nonresident who works in NE and whose wages are subject to federal withholding is subject to the same withholding on their entire wages as that used for NE residents. Form 9N, *Employee Certificate for Allocation of Withholding Tax,* may be filed with the employer by a nonresident employee who works for an employer in both NE and other states to designate the approximate percentage of the wages subject to NE withholding (but this does not determine the wage amount that must be included on the Form W-2 as NE wages). A nonresident who performs personal services in NE but is not subject to federal withholding may still be subject to NE income tax withholding.
Nevada	Not applicable.	Not applicable.
New Hampshire	Not applicable.	Not applicable.
New Jersey	Yes. If all services are performed out of state, first withhold as required by the other state, then withhold for NJ only the amount by which the NJ withholding exceeds the withholding amount for the other state. Report on Form W-2 all wages paid for work performed both inside and outside NJ and indicate to which state(s) tax was remitted.	Yes, but see reciprocity. If a nonresident performs all services in NJ, the tax must be withheld from all wages paid to the employee. If a nonresident works partly within and partly outside NJ, only the wages paid for services performed in NJ are subject to withholding.
New Mexico	Yes (report all wages on Form W-2).	Yes, unless the nonresident works in NM for 15 or fewer days in the calendar year.
New York	Yes, with personal income tax credit for any taxes paid to the other state or locality on income earned in that jurisdiction while a NY resident. Unemployment insurance rules of coverage are followed to determine withholding and what wages to report and the state they should be reported to. Report all wages on Form W-2 but do not send them to the state; report on 4th quarter Form NYS-45.	Yes, unless the nonresident works in NY for 14 or fewer days in the calendar year (any part of a day spent performing services in NY counts as a full day). The 14-day rule does not apply to payments made to nonresident athletes and entertainers performing services in NY, or to payments of deferred compensation or nonstatutory stock options.

WITHHOLDING ON RESIDENTS WORKING OUT-OF-STATE AND NONRESIDENTS		
State	**Residents: Withholding Required on Services Performed Out-of-State (and Wage Reporting Requirement), If Nexus**	**Nonresidents: Withholding Required on Services Performed In-State**
North Carolina	Yes (report all wages, no matter where earned, and the NC tax withheld on Form W-2), unless state income tax is required to be withheld for the work state (then don't report on Form W-2).	Yes (report all NC wages and NC tax withheld on Form W-2; or, if show the total wages for the year and the total state tax withheld, provide a breakdown showing the wages paid and tax withheld for each state); any relief from double withholding must be granted by the employee's state of residence.
North Dakota	Yes, if the employer's main place of business is located in ND and if the wages are subject to federal income tax withholding (report wages on Form W-2); ND withholding is not required if the employer is required by the other state to withhold that state's income tax from the employee's wages.	Yes, but see reciprocity.
Ohio	Yes (report on Form W-2).	Yes, but see reciprocity.
Oklahoma	Yes, even if withholding is required by the work state. Report the out-of-state wages on Form W-2 as OK wages in addition to reporting them as wages for the work state.	Yes, unless earnings are less than $300 in a calendar quarter.
Oregon	Yes, unless tax is withheld for the work state (report all OR wages on Form W-2); if the resident paid tax to OR and another state he/she may claim a credit on their OR return for income taxes paid to the other state. Withholding is not required for Oregon resident employees if the employer has no employees working in Oregon, but the state prefers withholding on wages paid to Oregon residents as a convenience to the employees.	Yes, unless employee's Oregon earnings for the year will be less than his/her standard deduction amount for his/her filing status. Non-resident employees with wages greater than their standard deduction amount must file an Oregon non-resident tax return.

WITHHOLDING ON RESIDENTS WORKING OUT-OF-STATE AND NONRESIDENTS		
State	**Residents: Withholding Required on Services Performed Out-of-State (and Wage Reporting Requirement), If Nexus**	**Nonresidents: Withholding Required on Services Performed In-State**
Pennsylvania	Withhold PA tax on all wages paid if all services are performed in the other state and the other state has no income tax (report all PA taxable compensation paid to the employee on Form W-2). Do not withhold PA tax if the other state has an income tax which the employer is withholding (but report on Form W-2 the wages earned in PA even though no PA tax was withheld). If PA resident's services are performed partly within PA and partly in another state and the employer withholds the other state's income tax, employer must also withhold PA tax on the services rendered in PA (report all PA taxable compensation on Form W-2); if the other state has no income tax, employer must withhold PA income tax on the employee's total compensation.	Yes, withhold PA tax on all wages if all services are performed in PA, unless a reciprocal agreement applies; if services are performed only partly within PA, withhold PA tax only on wages paid for the services performed within PA provided adequate current records are maintained to determine accurately the amount of compensation earned in PA (if such records are not maintained, the employer must withhold on all compensation paid to a nonresident who works partly within and partly outside PA).
Rhode Island	Not required.	Yes
South Carolina	Yes (if employee is paid $800 or more per year), unless withhold state income tax for the work state (report all wages earned on Form W-2).	Yes (if employee is paid $800 or more per year); if enter a contract exceeding $10,000 with a nonresident contractor for temporary services to be performed in SC withhold SC tax from the payments.
South Dakota	Not applicable.	Not applicable.
Tennessee	Not applicable.	Not applicable.
Texas	Not applicable.	Not applicable.
Utah	Yes; personal income tax credit is allowed if income tax is withheld for the work state (don't report the wages on Form W-2).	Yes, unless the employer does business in the state for 60 days or less in the year and has received an exemption certificate from the state.

WITHHOLDING ON RESIDENTS WORKING OUT-OF-STATE AND NONRESIDENTS		
State	**Residents: Withholding Required on Services Performed Out-of-State (and Wage Reporting Requirement), If Nexus**	**Nonresidents: Withholding Required on Services Performed In-State**
Vermont	Yes. Withholding is calculated on the employee's entire earnings and is then reduced by the amount of tax withheld for the work state (don't report the out-of-state wages on Form W-2). If the employee works partly within and partly outside of VT for the VT employer and the other state has no income tax, withhold on all the wages paid; if the other state does have an income tax, withhold both VT tax and the tax for the work state on the services performed there.	Yes. If a nonresident works partly within and partly outside of VT, only compensation for services performed in VT is subject to withholding.
Virginia	No, unless the other state has no income tax or there is a reciprocal agreement with the other state which requires withholding. Employees subject to tax in the other state are entitled to credit for those taxes against the amount of tax owed to VA (the employee should file Form VA-4B, *Employee's Withholding Income Tax Credit for Income Taxes Paid to Another State).*	Yes, but see reciprocity.
Washington	Not applicable.	Not applicable.
West Virginia	Yes (report all wages on Form W-2).	Yes, but see reciprocity. If the nonresident works entirely within WV, withhold from all wages paid to the employee.
Wisconsin	Yes (report all wages on Form W-2).	Yes, unless the annual WI earnings are expected to be less than $1,500 a year or the employee is covered by a reciprocal agreement.
Wyoming	Not applicable.	Not applicable.

Resident and Non-Resident Withholding



Neither Connecticut nor Rhode Island have reciprocal agreements with any other state. RI requires withholding from non-residents that work within its borders. CT requires withholding from wages of its residents for services performed in another state (assuming the employer has nexus), allowing credit for the other state's withholding. Withholding should be taken first for RI. If employer has nexus in CT, and CT withholding on the same wages would be a higher amount, withhold the difference for CT. Report wages on W-2 for RI and CT.

Ms. SÁNCHEZ. Thank you, Ms. Nelson. We appreciate your testimony.

At this time, I would invite Mr. Duncan to give his testimony.

TESTIMONY OF HARLEY T. DUNCAN, EXECUTIVE DIRECTOR, FEDERATION OF TAX ADMINISTRATORS, WASHINGTON, DC

Mr. DUNCAN. Madam Chairwoman, Members of the Committee, my name is Harley Duncan. I am the executive director of the Federation of Tax Administrators. I appreciate the opportunity to appear before you on H.R. 3359 to present the views of State tax administrators.

The federation is an association of the principal tax administration agencies in each of the 50 States, D.C., New York City, and Puerto Rico. Our policy on this matter is attached to my testimony. It was adopted by our membership in Chicago, and amplified last week by our board of trustees.

As a preliminary matter, while I will be speaking to States because that is who I represent is States, the issues involved in this bill and I think the comments I make also apply to a fair number of local governments that apply and impose income taxes, particularly cities of St. Louis, Kansas City, Philadelphia, and a number in Ohio and Kentucky as well.

The federation is opposed to H.R. 3359 as that bill has been introduced. We have three major policy objections to the issue.

The first is that it represents a substantial intrusion into State tax sovereignty and authority, the authority of States to design a tax system that meets their needs within the contours of the Constitution and to impose tax on economic activity that occurs within its borders. If enacted as introduced, it would leave States exposed to a situation in which an individuals could make extensive use of the marketplace in the State without making a contribution in terms of income tax paid.

Second, it represents a very substantial and radical departure from current State tax policy with respect to income taxes. Namely, States employ the source tax principle as does the Federal Government. And income is generally taxed where the services giving rise to the income are performed. This bill with the 60-day threshold will substantially turn that on its head for any number of employees and individual and convert the country to essentially a residency-based system.

There are States that use the residency-based. There are States that have reciprocal agreements with one another. But they have chosen to do so voluntarily, generally, where the economies of those States match up and the tax systems of those match up. This would be a mandated reciprocal arrangement by the Congress.

And finally, we believe that H.R. 3359 goes well beyond where the Congress has been in the area of regulating individual income taxation in the past. If you look across the various enactments, they are generally of two types. The first is where there is a substantial Federal interest involving either Federal employees, members of the military service, employees on Federal installations.

The second is where the workers are regularly engaged in interstate commerce: the railway workers, the airline workers, the motor carriers where it is their job to travel from State to State.

Those are really the only two areas where the Congress has enacted bills in the individual income tax area. To step in to the extent that this one does, we think, is a radical departure.

This is not to say that we have our head in the sand or are unmindful of the burdens that are imposed by the current system. Complying with the current system where there is no de minimis threshold on either liability or withholding is indeed difficult and probably impractical. That is why a number of States, several States have moved to address the issue on their own. That is why we have worked with the Council on State Taxation to try to fashion legislation that could be workable.

If you desire to move forward in this, we have raised a number of issues in my written remarks that we would ask that you address and we would be willing to work with you. Two most important ones are first, the 60-day rule.

The 60-day rule, we believe, goes well beyond what is necessary to deal with the burden issue. If in 60 days you can't figure out where you are going to be, then I think we have some more issues than just withholding.

You can deal with it in far less than 60. Sixty days gives a person a quarter of a year of operating within a State without owing a tax liability. And we think it goes well beyond what is necessary.

The second issue that we have raised for you is that our policy provides that if a threshold in a bill such as this is enacted that it should have a dollar component as well. And we would suggest that the withholding can be triggered off of days, but there needs to be a backstop on if the employee's income exceeds some threshold in a State, he or she has a liability to that State.

Otherwise, State revenue systems are exposed. And we believe that the days only threshold leaves the systems too exposed. We believe a days and a dollar can be done in a fashion that substantially alleviates the burden and doesn't expose State systems to the risk that they would under the bill that is introduced.

Thanks very much. We look forward to working with you in the future.

[The prepared statement of Mr. Duncan follows:]

PREPARED STATEMENT OF HARLEY T. DUNCAN

Statement of
Harley T. Duncan
Executive Director
Federation of Tax Administrators

Before the

Subcommittee on Commercial and Administrative Law
House Committee on the Judiciary
U.S. House of Representatives

H.R. 3359
Mobile Workforce State Income Tax Fairness and Simplification Act of 2007
November 1, 2007

Chairwoman Sanchez, Ranking Member Cannon and Members of the Subcommittee:

The Federation of Tax Administrators appreciates this opportunity to appear before you on H.R. 3359, a bill that would limit state and local income taxation of individuals that work in a state for limited periods of time as well as limiting the obligations of the employers of such persons to withhold state and local income tax on the income earned by such persons. The Federation opposes this measure as it has been introduced.

Introduction

The Federation of Tax Administrators (FTA) is an association of the principal tax and revenue collecting agencies in each of the fifty states, the District of Columbia, New York City and Puerto Rico. Our purpose is to improve the techniques and standards of tax administration through a program of research, information exchange, training, and representing the interests of state tax administrators before the Congress and federal executive branch. The Federation is governed by an 18-member Board of Trustees elected by the member agencies.

The policy of the Federation with respect to this issue was embodied in Resolution Six adopted by the membership at its June 2007 Annual Meeting in Chicago, Illinois. A copy of the resolution is attached.

FTA opposes enactment of H.R. 3359 as introduced because it represents a substantial intrusion into state tax authority and sovereignty and will cause significant disruption to state tax policies and the revenue systems of some states. It runs directly counter to the fundamental, underlying principle of state income taxation -- namely that income should be taxed where it is earned or where the services giving rise to the income are performed. H.R. 3359 goes well beyond previous measures that Congress has enacted concerning individual income taxation and what is necessary to resolve issues of burden and compliance that the bill is purportedly designed to address.

This should not be interpreted to suggest that state tax administrators are unmindful of the issues that individuals and employers face in complying with current state and local tax regimes. As noted in our Policy Resolution, we recognize there are issues in the current system that should be addressed. If Congress moves into this area, it should balance several interests. Congress should minimize the intrusion into state authority and the disruption of state revenue systems. It should also insure that any legislation is directed squarely at the burden and issues presented and is not overreaching. In particular, we believe the 60-day threshold in the bill is excessive and administratively inadequate. Any threshold that determines when an individual has a tax liability to a state should have an income level and a time component to it. (See below for explanation.)

State Tax Sovereignty

There can be no doubt that H.R. 3359 represents a substantial intrusion into state tax sovereignty. If enacted, the bill would allow a wide range of individuals to conduct substantial amounts of economic activity within a state without owing a tax liability to the state. It would constitute one of the most far-reaching measures the Congress has ever enacted in the area of state individual income taxation. While some might consider the concept of tax sovereignty to be esoteric, it is fundamental to our system of federalism and to the operation of states. Within their sphere of responsibility, states are able to define the level of government services they desire. Further, they are, within the bounds of the U.S. Constitution, free to tax the activities occurring within the state to finance those services. The two responsibilities go hand in hand. H.R. 3359 intrudes substantially on the authority to design one's tax system.

The U.S. Court of Appeals for the 11th Circuit said it well when it wrote:

> Perhaps the most fundamental power of a sovereign is the power to tax. This power was originally considered so integral a power of the states as to admit of no abridgement by the federal government, *see* The Federalist No. 32 (Alexander Hamilton), and its singular importance to the states has been repeatedly acknowledged. [Citations omitted.] This understanding of the relationship of sovereignty and taxation is implicit: "It is upon taxation that the several States chiefly rely to obtain the means to carry on their respective governments." [Citation omitted.] *CSX Transportation, Inc. v. Georgia State Board of Equalization, et al.*, 472 F.3d 1281, 1288, (11th Cir. 2006), *cert. granted*, 127 S.Ct. 2879 (U.S. 2007) (No. 06-1287).

The importance of state tax authority to state sovereignty and our federal system argues that Congress should tread lightly in limiting the authority of the states and do so only on a showing of compelling need and only after balancing an array of appropriate interests.

Source Tax Principle

The basis of current state income tax systems is that a state may tax income that is derived from "sources" within the state. In-state sources are defined generally to include the performance of services in the state, the conduct of a trade or business in the state, or the receipt of income from property owned within the state. Further, income from in-state sources are subject to tax regardless of whether it is earned by a resident or a nonresident who otherwise enters the state for a period of time to carry on the income-producing activity. This is not unique to states; it is, in fact, the same tax principle underlying the federal income tax.[1]

State authority to tax nonresident income from in-state sources was validated by the U.S. Supreme Court over 70 years ago in *Shaffer v. Carter* 252 U.S. 37 (1920) when it wrote:

> ...we deem it clear, upon principle as well as authority, that just as a State may impose general income taxes upon its own citizens and residents..., it may, as a necessary consequence, levy a duty of like character, and not more onerous in its effect, upon

[1] As evidence of the importance of the "source principle," note that the IRS has just announced a compliance initiative aimed at insuring that foreign athletes who earn income in the U.S. are properly paying the tax due. See, Dustin Stamper, "IRS Targeting Foreign Athletes and Entertainers, IRS Official Says," Tax Notes Today, October 29, 2007.

> incomes accruing to non-residents from their property or business within the State, or their occupations carried on therein....

As the *Shaffer* court noted, and as has been developed in subsequent cases, the essential constraint on the states in the taxation of nonresident income is that the nonresident not be taxed to a greater degree than a similarly situated resident of the state and not be discriminated against by virtue of the nonresident status. Beyond this, the Court has essentially left it to state legislatures to control nonresident taxation.[2]

Abrogation or abandonment of the source principle (and replacing it with what is largely a residency based system as proposed in H.R. 3359) would create a situation in which persons could avail themselves of the marketplace in a state and many of the services provided by that state without compensation to the state. It could well lead to a series of "tax havens" in certain interstate metropolitan areas and unhealthy interstate tax competition.

The source tax principle should not be, and historically has not been, lightly discarded by Congress. To a considerable extent, Congress has refrained from dictating the circumstances in which a state may tax economic activity occurring within its borders. The primary instances in which Congress has intervened in state individual income taxation include:

- A Member of Congress is subject to tax only in the state of his/her residence;
- Income of federal employees may not be taxed differently from that of state employees, and employees on certain federal installations that straddle two states are taxable only in their state of residence;
- The Servicemember's Civil Relief Act establishes special rules for taxation of members of the active military service;
- Special rules have been enacted for employees in selected interstate commerce industries (railway workers, airline workers and motor carrier employees); and
- Retirement income of most individuals is taxable only by the state of residence.

In each case, Congress determined that there was a substantial federal interest or an overwhelming compliance burden that required overriding the source principle of taxation. In

[2] There are legal requirements and state mechanisms to avoid double taxation of income earned by an individual. Generally speaking, if income is taxed by a state in which an individual is a nonresident, the state in which the individual is a resident provides a credit for taxes paid to the nonresident state.

evaluating, H.R. 3359, FTA believes Congress should exercise similar restraint and diligence. As introduced, H.R. 3359 goes well beyond these earlier measures and establishes a substantial "safe harbor" that would allow any employee to work in a state for an extended period of time and not be subject to the tax laws of the state.

H.R. 3359 as introduced will, to a considerable degree, undo the traditional system of state income taxation in which income is taxed where the services giving rise to the income are performed and convert it to a residency-based tax system. Some states have chosen voluntarily (through reciprocity agreements) to tax primarily on a residency basis, but most have not. The U.S. Supreme Court has consistently upheld the authority of states to tax on a source basis. That authority should not be overturned lightly.

FTA Policy

The FTA Policy on this issue says in pertinent part:

> The ability to tax income where it is earned is fundamental to state tax sovereignty and state income tax systems. Moreover, this ability is absolutely necessary in our federal system, where a state may choose to not employ an income tax. States do, however, recognize the administrative and compliance burdens imposed on individuals and employers under current arrangements and are willing to explore options for addressing those burdens for persons who are in the state for limited periods of time.
>
> FTA will assess any federal legislative measures in this area against the following criteria: (1) Recognizing that the benefits of federalism will impose administrative burdens on commerce, is there disinterested evidence that the administrative burden and complexity posed by current state and local practices is impeding the growth of commerce? (2) Does the proposed preemption address issues of simplification and complexity? (3) Can meaningful simplifications and uniformity be achieved through state action? (4) Would preemption disrupt state and local revenue flows and tax systems? (5) Would preemption cause similarly situated taxpayers to be taxed differently; specifically, does the proposal create advantages for multistate and multinational businesses over local business? (6) Does the preemption support sound tax policy? (7) Does the preemption create unknown or potential unintended consequences? (8) Have state tax authorities and taxpayer representatives together agreed to a beneficial change in federal law?

As FTA evaluates H.R. 3359 as introduced, we believe it comes up short in two ways with respect to these criteria. First, while the bill supports certain aspects of sound tax policy –

simplification, certainty and uniformity – it goes beyond what is necessary to achieve these ends and is overly intrusive into state tax authority and policy. By allowing an individual to be present in a state for 60 days before a tax liability would attach effectively eviscerates the source principle of taxation and allows individuals to reap substantial benefits from a state without contributing to the financing of the services provided by that state. In short, the proposal tips the balance too far in favor of simplification and is disruptive of sound, established tax policy and state tax authority.

Second, as evidence of the degree to which the proposal deviates from current tax policies, the proposal as introduced is disruptive of revenue flows in certain states. According to preliminary work commissioned by the proponents of the bill, it would reduce revenues in New York State by over $100 million per year.[3] This is to be expected given the nature of the economy of the state and its principal metropolitan area as well as its role as an international center of business and finance. Any proposal that has an impact of this nature needs to be carefully evaluated.

Concerns with H.R. 3359

If Congress intends to pursue legislation in this area, FTA recommends that the following issues be addressed.

60-Day Rule. Beyond the policy concern of intruding into state authority, the dominant concern of states is the 60-day rule contained in H.R. 3359. It will effectively convert state income tax systems to residency-based tax systems and goes well beyond what is necessary to deal with the burden and compliance issues present in the current system. It will allow an individual to work in a jurisdiction for over 25 percent of a work year and be absolved of any liability to the state in which he/she worked. This is certainly more than is required to deal with the compliance and burden issues that the bill was intended to address. It will effectively limit nonresident taxation to those that work permanently in another state or are assigned to a state on a continuing basis; it is certainly well beyond any level that is necessary to deal with individuals

[3] The data discussed here have not been verified or evaluated fully by the states. There is some concern that the estimated impact could be underestimated – not purposely but because of the difficulty of the task and the availability of the data to measure changes among states. Several states are in the process of conducting their own estimates. These will be made available to the Committee when produced.

who travel regularly as part of their jobs e.g., attorneys with litigation, training personnel, meeting organizers, as well as government affairs and sales personnel.

It is the excessive nature of the 60-day rule that contributes to the substantial revenue impact that the bill has on certain states, particularly New York State because of the nature of its economy and its role as an international center of finance and business. While we would not argue that accounting for minimal amounts of time in a jurisdiction is always practical, the proposed 60-day rule is over-reaching. It is certainly more than is necessary to deal with the burdens employers might face.

Dollar-denominated Threshold. As noted in our Policy Resolution, FTA believes that if legislation is enacted in this area, the de minimis threshold should also have an income component in addition to a time component. That is, state tax obligations would be triggered if the total of wages and remuneration paid to an employee for services in a state exceeded a specified amount of income or if the employee exceeded a certain number of days in the state. This is similar to the approach used in the U.S. income tax system to determine the taxability of income paid to a nonresident alien.[4] As noted, H.R. 3359 exposes some states to significant revenue shifts and disruptions based on the preliminary estimating work that has been done. The addition of a dollar-denominated threshold will reduce the exposure of states to revenue disruptions. In our estimation, it can be done in a manner that does not impose undue burdens on employers or employees.

FTA recommends that the de minimis formula should be "bifurcated" and formulated as follows: (a) An employer would have a withholding obligation only if the employee is a resident of the state or is present in the state in excess of some specified number of days; and (b) an employee should be subject to a state's income tax if she/he: (1) is a resident of the state; (2)

[4]Section 861(a)(3) of the Internal Revenue Code provides that compensation for labor or personal services performed in the U.S. is not be deemed to be income from sources within the U.S. if (A) the labor or services are performed by a nonresident alien individual temporarily present in the U.S. for a period or periods not exceeding a total of 90 days during the taxable year; (B) such compensation does not exceed $3,000 in the aggregate; and (C) the compensation is for labor or services performed as an employee of or under a contract with a nonresident alien, foreign corporation or other enumerated entity. See IRS Publication 513, "Tax Information for Visitors to the United States." Income of a resident alien is generally taxable in the same manner as that of a U.S. citizen. (See IRS Publication 519, "U.S. Tax Guide for Aliens.")

exceeds the withholding threshold denominated in terms of time; or (3) has income in excess of some dollar threshold in a state.

Such a construct would provide employers with the certainty and simplification they require to efficiently handle their withholding obligations. At the same time, it provides states with protection against substantial disruptions to their revenue flows. Concern has been expressed that this approach could leave employees in a situation where they would have a tax liability without any withholding having occurred. This, of course, is no different than the current system, and we believe that if the threshold is properly constructed, it is a situation that would affect relatively few employees that should, in conjunction with their employers, be in a position to manage their affairs to avoid the situation.[5] In our estimation, the reduction in the exposure of state revenue systems requires adoption of this approach if Congress intends to pursue legislation in this area.

Definition of "Day." Section 2(d)(1) of H.R. 3359 defines "day" as any day when the employee is physically present in the state or locality and performs "more than 50 percent of the employee's employment duties in such State or locality for such day." We would recommend that this be changed to substitute "all or any part of a day in which the employee is present and performs services in the state."

As now written, this provision will do anything but bring clarity and simplification to the determination of when an employee may be subject to tax and when an employer may be subject to withholding. Instead of providing a bright line, it asks employers and employees to make a determination about the proportion of their duties (an undefined term) that were performed in the state. "Duties" could be interpreted to mean specifically assigned obligations or something mandated by an employer, rather than perhaps all the services performed by an employee. Further, how is the "50 percent" to be determined – by time, value of the duty to the employer or

[5] For example purposes only, consider if the bill imposed a threshold of 20 days in a state or $20,000 in income allocable to a state. In such a case, an employee would have to earn in excess of $260,000 per year in order to exceed the $20,000 threshold (gross income before any deductions, exemptions, etc.) without exceeding the 20 days threshold (based on 260 working days per year.) Employees in this income range should reasonably be able to assess the states in which they are likely to exceed such a threshold in a given year and make arrangements with their employer for withholding if he/she so desires.

some other measure. If it is difficult to determine where an employee is on any given day (as proponents of the bill have argued), it is immeasurably harder to have consistent documentation on where an employee performed a majority of his/her duties for the day. We believe this provision, besides being unclear, could lead to manipulation and gaming the system.

Converting the standard to "all or any part of a day in which the employee is present and performs services in the state" will provide clarity in determining when the withholding and liability thresholds have been met. These are easily understood and commonly used terms. The Committee should also note that for purposes of determining when a nonresident alien being paid by a foreign corporation is subject to U.S. income tax, one of the determinations is how many days the individual is present in the U.S., and "day" is defined as "any part of a day" for federal income tax purposes. Finally, in evaluating this recommendation, the Committee should keep in mind that the definition of "day" affects only whether the withholding/liability threshold is met and not the amount of any liability.

Compensation Paid Over Multiple Years/Stock Options. H.R. 3359 provides no guidance and will likely disrupt established state policies on an increasingly frequent form of compensation – stock options or other compensation paid in one year for services performed in an earlier year. Most states have developed rules for this compensation that would be affected by the bill. It is not uncommon for states to allocate option income earned by a nonresident to a state based on the proportion of time worked in the state from the time the option is granted to the time it is exercised (i.e., the stock is purchased at the price offered in the grant).[6] (For federal tax purposes, income earned during this period is treated as taxable compensation and not capital gains income.) Under H.R. 3359, it could be argued that if the individual does not exceed the 60-day threshold in the year the option is exercised, a state may not be able to tax the portion of the income earned during that period even though it is normally treated as taxable compensation and the individual may have exceeded the threshold during the years from grant to exercise. In other words, by imposing an arbitrary (and excessive) days-based threshold on when a taxpayer is subject to tax in a state, H.R. 3359 will disrupt established state tax policies that are based on

[6] See Jack Trachtenberg and Paul R. Comeau, "State Taxation of Stock Options," Presentation to FTA Annual Meeting, Chicago, Illinois, June 2007.

the accepted source tax principle and are designed to deal with a relatively complex, but increasingly common, form of compensation. Disrupting practices in this area has the potential to exacerbate the revenue loss considerably. Including a dollar-denominated threshold for when a tax liability is incurred by an employee within a state would also help address this problem and reduce the disruption to state revenues.

Records Used in Determining Withholding Obligation. H.R. 3359 provides that for purposes of determining an employer's withholding obligations, an employer may rely on an employee's determination of time in a state unless the employer has "actual knowledge of fraud by the employee..." It further provides that an employer is not required to use records regarding the location of an employee that it may have unless it maintains a "time and attendance system" that "contemporaneous[ly] records the work location of the employee for every day worked and the employer uses this data to allocate the employee's wages between all taxing jurisdictions in which the employee performs duties." These provisions, taken together, appear to be designed to absolve employers of virtually any obligation to use information that they have at their disposal in determining whether an employee is subject to a withholding requirement (and consequently a tax liability) in a state. Instead, they let the employer rely solely on an employee's estimate of the time he/she may have performed services in a state.

FTA would make two recommendations in this area. First, the fraud standard in Section 2(c)(1)(A) should be eliminated, and the employer should be allowed to rely on an employee's estimate of time in a state unless the employer has "actual knowledge" that the employee's estimate is in error. Fraud is an exceedingly high standard to prove, and the purpose here is to determine if an employer has a withholding obligation, not whether there is some intent to evade taxes. Second, as to the "time and attendance system," we find the language to be overly narrow and protective of the employer. We would recommend that Sections 2(c)(2) and 2(c)(3) be replaced by a requirement that if an employer in the normal course of the business maintains records that record the location of an employee, such records should be used to determine whether an employer has a state income tax withholding and information return obligation. If the records are maintained and considered sufficiently accurate for other business purposes, we would argue that they should also be used for purposes of determining the applicability of state tax withholding obligations.

Certain Public Figures. The bill is drafted so as not to apply to certain types of individuals that are paid on a "per event" basis because such individuals know where they are and how much was earned for the event. We believe, however, that the term "certain public figures" and "persons of national prominence" are rather imprecise and could lead to litigation, etc. We recommend instead that the bill be amended simply to provide that "persons paid on a per event basis" are not to be subject to the terms of the bill.

"Cliff" Effect. H.R. 3359 (Section 2(b)) provides that if an employee crosses the 60-day threshold, withholding shall commence from the first day the employee performed services in the state. That is, if an employee crosses the 60-day threshold in November, the December wage payments to the individual would have to reflect withholding for all 60-plus days. This seems to us impractical and could work a hardship on the employee. Importantly, this is really a reflection of the excessive nature of the 60-day requirement. A significant reduction in the 60-day threshold will minimize this problem for employees and reduce the fiscal impact on states.

Conclusion

As introduced, H.R. 3359 represents a radical departure from the norm in terms the degree of change that it would work in traditional state tax policies and in the degree of Congressional intervention into state individual income taxation. The bill will substantially eviscerate the source principle of taxation and prevent a state from taxing substantial amounts of economic activity that occur within its borders. As such, it runs counter to traditional norms of federalism and exposes states to substantial and unwarranted disruption of their revenue streams.

Maintenance of a federal system in which states have the authority to design their own tax systems will necessarily impose higher compliance burdens on individuals and their employers than a unitary system with a single tax regime. State tax administrators are not unmindful of the need to consider these compliance burdens and to balance them against the objectives of maintaining state tax sovereignty and not disrupting revenue flows. As noted in the FTA Policy

Statement, tax administrators are committed to exploring options to address the burden of the current withholding and tax liability rules for persons temporarily employed in a state.

FTA believes that H.R. 3359 as introduced does not appropriately balance the interests in this debate. It goes well beyond what is necessary to address legitimate issues of certainty, simplification and compliance and does real harm to state tax systems. To a considerable degree, the harm and exposure to state tax systems is caused by the excessive 60-day threshold contained in the bill and the lack of an income-denominated component to the threshold for determining when individuals are liable for taxes in a state in which they have worked temporarily. We look forward to working with the Committee to address these and the other issues we have outlined should you so desire.

Resolution Six
Taxation and Withholding of Earnings in Multiple States

Background

The fundamental principle of state individual income taxation is that income is taxable where it is earned or where the services giving rise to the income are performed. In addition, the state of a taxpayer's residence may tax all income regardless of where earned, but is generally required to offer a credit for taxes paid to other states to assure that income is not subject to multiple taxation. This is the same tax policy embraced by the U.S. government and by all other income-taxing governments.

As U.S. work patterns shift to increasingly include telecommuting and multistate travel, more workers find themselves with tax obligations to more than one state. Likewise, employers are faced with an increased responsibility for withholding income taxes for multiple states. State laws and practices vary widely with respect to de minimis thresholds for withholding. There also is wide variance in enforcement programs aimed at compliance among persons (and their employers) who are temporarily in the state.

In the 109th Congress, H.R. 6167, the Mobile Workforce State Income Tax Fairness and Simplification Act, would have authorized a state to impose an income tax liability and a withholding requirement only when a nonresident had been in the state for at least 60 days in a calendar year. The bill contained an exception for professional athletes and entertainers.

In correspondence with proponents of H.R. 6167, FTA made several points. A 60-day threshold is excessive. While states recognized concerns regarding the administrative burdens imposed by current practices, the 60-day threshold is well beyond a level necessary to deal with the vast majority of individuals who would be temporarily in a state. Further, H.R. 6167 would substantially disrupt the current tax system in favor of a system based on taxation by the resident state. Moreover, a simple "days threshold" may expose some states to substantial revenue disruptions; a "dollar threshold" should also be applied. Finally, independent state action is a viable and preferred substitute for federal legislation.

Policy

The ability to tax income where it is earned is fundamental to state tax sovereignty and state income tax systems. Moreover, this ability is absolutely necessary in our federal system, where a state may choose to not employ an income tax. States do, however, recognize the administrative and compliance burdens imposed on individuals and employers under current arrangements and are willing to explore options for addressing those burdens for persons who are in the state for limited periods of time.

FTA will assess any federal legislative measures in this area against the following criteria: (1) Recognizing that the benefits of federalism will impose administrative burdens on commerce, is there disinterested evidence that the administrative burden and complexity posed by current state and local practices is impeding the growth of commerce? (2) Does the proposed preemption address issues of simplification and complexity? (3) Can meaningful simplifications and uniformity be achieved through state action? (4) Would preemption disrupt state and local revenue flows and tax systems? (5) Would preemption cause similarly situated taxpayers to be taxed differently; specifically, does the proposal create advantages for multistate and multinational businesses over local business ? (6) Does the preemption support sound tax policy? (7) Does the preemption create unknown or potential unintended consequences? (8) Have state tax authorities and taxpayer representatives together agreed to a beneficial change in federal law?

Moreover, any federal legislation in this area should meet the following additional criteria: (1) It should contain a de minimis threshold that minimizes the disruption of state revenues and reduces the exposure of states to such disruptions; and (2) It should not apply to persons paid on a "per event" basis for services performed in the state.

This resolution shall automatically terminate three years after the Annual Business Meeting at which it is adopted, unless reaffirmed in the normal policy process.

Adopted, June 13, 2007

Ms. SÁNCHEZ. Thank you, Mr. Duncan. I appreciate your testimony.

And finally, I would invite our final witness, Mr. Hellerstein, to please begin his testimony.

TESTIMONY OF WALTER HELLERSTEIN, FRANCIS SHACKELFORD DISTINGUISHED PROFESSOR OF TAXATION LAW, UNIVERSITY OF GEORGIA SCHOOL OF LAW, ATHENS, GA

Mr. HELLERSTEIN. Thank you very much, Madam Chairwoman. I am very grateful for the opportunity to testify before this Subcommittee and to have the special privilege of testifying before a fellow Georgian, Congressman Johnson.

My testimony addresses three specific questions, the first two of which I think should not be controversial at all. First, does Congress have the constitutional authority to enact H.R. 3359? Second, is there historical precedent for Congress enacting legislation analogous to H.R. 3359? And finally, the more controversial question, is this an appropriate exercise of congressional power?

Question one, I think it is clear the Congress has the authority under the commerce clause to enact H.R. 3359. The case law in this area is clear that Congress has extremely broad powers to enact legislation that affects interstate commerce. Indeed, when the court has dealt with or addressed issues involving State taxation in particular, it has stated in very broad terms that Congress essentially can do what it wants in this area.

Just to read you one quote, "It is clear that the legislative power granted by Congress—to Congress by the commerce clause would amply justify the enactment of legislation requiring all States to adhere to uniform rules for the division of income." So presumably they can also create uniform rules for the withholding of income or when tax liability occurs. I think that really should be a noncontroversial issue.

The second question is whether there is precedent for this kind of legislation. Congress has never enacted really broad-based legislation regulating State taxation. There is no uniform apportionment formula. There are no broad-based rules that limit the States in what they can do.

But there is a lot of precedent, really, I think, quite analogous to H.R. 3359, for Congress enacting specific legislation targeted at specific problems. Indeed, Harley Duncan just referred to one type of legislation, taxes on employees engaged in interstate transportation. They are quite analogous, I think, although certainly a narrower target, to dealing with the problems of income taxation of employees engaged in water transportation, air transportation, motor carrier transportation.

Congress has also acted to restrict the power of States to tax nonresidents, retirement income. And I have this whole litany in my testimony, and I don't want to use all my time up on this list. But just to go through some of the areas, Congress has limited States in their power to tax interstate businesses when they sell tangible property and do no more than solicit in the State. Congress has limited power, limited the States' power to tax—to impose discriminatory taxes on railroads, on motor carriers, and on air carriers.

Congress has limited the States' power to impose taxes that affect a pension plan under the Employees Retirement Income Security Act. So it seems to me this is something for which there is really quite substantial precedent. Just 2 days ago by voice vote, Congress unanimously re-extended the Internet Tax Freedom Act, another example of targeted legislation.

Finally, and this is a more—probably the only controversial question here is—is this an appropriate exercise of congressional power. And in my opinion, I think it is.

First, I really do wish to make it clear that I believe the States have a legitimate interest in assuring that workers who earn income in the State pay their fair share of the State tax burdens for the benefits and protections that the State provides to them. But this legitimate interest has to be balanced against the burdens that are imposed on multi-state enterprises and on the conduct of interstate commerce by uncertain, inconsistent, and unreasonable withholding obligations imposed by the State.

Yes, I think it is telling that the States themselves recognizing this problem have to some extent tried to alleviate it through their own voluntary reciprocal exemption agreements. As Bill Gates would say, a known problem.

In the end, although there may well be room for additional fine tuning of the statutory language to assure that the right balance is struck between the States' legitimate interest in revenue raising and the Nation's interest in preserving our national common market, I believe that a targeted response to the specific problem reflected in H.R. 3359 is an appropriate exercise of congressional commerce power. Thank you.

[The prepared statement of Mr. Hellerstein follows:]

PREPARED STATEMENT OF WALTER HELLERSTEIN

Testimony of Walter Hellerstein

on the

Mobile Workforce State Income Tax
Fairness and Simplification Act of 2007
(H.R. 3359)

Before the
Subcommittee on Commercial and Administrative Law
of the
Committee on the Judiciary
United States House of Representatives

November 1, 2007

I am Walter Hellerstein, the Francis Shackelford Professor of Taxation at the University of Georgia School of Law. I have devoted most of my professional life to the study and practice of state taxation and, in particular, to state taxation of interstate commerce and the federal constitutional restraints on such taxation. A copy of my vita is attached to this testimony.

I am honored by the Chairman's invitation to testify today. I welcome the opportunity to share with the Subcommittee my views on the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007. I do not appear here on behalf of any client, public or private, and the views I am expressing here today reflect my independent professional judgment.[1]

My testimony addresses three questions. First, does Congress have the constitutional authority to enact the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007? Second, is there historical precedent analogous to the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007 for congressional legislation restricting state taxing power? Third, would enactment of the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007 constitute an appropriate exercise of congressional power? As explained in more detail below, I believe the answer to all three questions is "yes."

I. CONGRESS HAS CLEAR AUTHORITY UNDER THE COMMERCE CLAUSE TO ENACT THE MOBILE WORKFORCE STATE INCOME TAX FAIRNESS AND SIMPLIFICATION ACT OF 2007

There should be no serious controversy over Congress's broad authority to adopt virtually any rule that it believes is appropriate with respect to matters that substantially affect interstate commerce, as state taxation of workers that cross state lines in furtherance of such commerce plainly does. The Constitution grants Congress the power "[t]o regulate commerce . . . among the several States . . . ."[2] The U.S. Supreme Court has interpreted that power in sweeping terms. Thus in the *Shreveport Rate Case*,[3] which sustained Congress's power to regulate local rates because they affected interstate rates, the Court declared:

> It is unnecessary to repeat what has frequently been said by this court with respect to the complete and paramount character of the power confided to Congress to regulate

[1] In the interest of full disclosure, it should be noted that I am of counsel to Sutherland Asbill & Brennan LLP, which is counsel to the Council on State Taxation (COST), an active supporter of H.R. 3359. As stated in the text, however, the following testimony represents my independent professional judgment, and it does not necessarily represent the views of any institution or organization with which I am affiliated.

[2] U.S. Const. art. I, § 8, cl. 3.

[3] *Houston E&W Tex. Ry. v. United States*, 234 U.S. 342 (1914).

> commerce among the several States. It is of the essence of this power that, where it exists, it dominates. . . . By virtue of the comprehensive terms of the grant, the authority of Congress is at all times adequate to meet the varying exigencies that arise and to protect the national interest by securing the freedom of interstate commercial intercourse from local control.[4]

In construing Congress's "plenary"[5] power to promote interstate commerce under the Commerce Clause, the Court has routinely sustained as legitimate exercises of this power far-reaching congressional legislation, including legislation that (1) regulates the amount of wheat a farmer can grow for his own consumption,[6] (2) bars discriminatory practices in local hotels and restaurants,[7] and (3) proscribes local criminal activity.[8]

The Court has also indicated that Congress has ample power to prescribe rules regarding state taxation in particular. For example, in *Moorman Manufacturing Co. v. Bair*,[9] the Court sustained Iowa's single-factor gross receipts formula for apportioning net income, despite substantial claims that it would lead to multiple taxation. After recognizing that prevention of multiple taxation would require national uniform rules for the division of income, the Court declared:

> While the freedom of the States to formulate independent policy in this area may have to yield to an overriding national interest in uniformity, the content of any uniform rules to which they must subscribe should be determined only after due consideration is given to the interests of all affected States. *It is clear that the legislative power granted to Congress by the Commerce Clause of the Constitution would amply justify the enactment of legislation requiring all States to adhere to uniform rules for the division of income.* It is to that body, and not this Court, that the Constitution has committed such policy decisions.[10]

Similarly, in *Quill Corp. v. North Dakota*,[11] which reaffirmed the judicial doctrine that the "negative" or "dormant" Commerce Clause[12] prohibits a state from requiring a

[4] *Id.* at 350-51.

[5] *Prudential Insurance Co. v. Benjamin*, 328 U.S. 408, 434 (1946).

[6] *Wickard v. Filburn*, 317 U.S. 111 (1942).

[7] *Katzenbach v. McClung*, 379 U.S. 294 (1964); *Heart of Atlanta Motel v. United States*, 379 U.S. 241 (1964).

[8] *Perez v. United States*, 402 U.S. 146 (1971).

[9] 437 U.S. 267 (1978).

[10] *Id.* at 279-80 (emphasis supplied).

[11] 504 U.S. 296 (1992).

vendor without physical presence in the state to collect a sales or use tax on sales to in-state customers, the Court declared that "Congress is . . . free to decide whether, when, and to what extent the States may burden interstate mail-order sales with a duty to collect use taxes."[13]

In *Arizona Public Service Co. v. Snead*,[14] Congress had enacted a statute prohibiting discriminatory state taxation of the generation or transmission of electricity. In a challenge to a New Mexico tax that allegedly violated the statute, the state contended that "if the federal statute is construed to invalidate the New Mexico tax, it exceeds the permissible bounds of congressional action under the Commerce Clause."[15] The Court summarily dismissed the argument, observing:

> In view of the broad power of Congress to regulate interstate commerce, this argument must be rejected. Here, the Congress had a rational basis for finding that the New Mexico tax interfered with interstate commerce, and selected a reasonable method to eliminate that interference. The legislation thus was within the constitutional power of Congress to enact.[16]

It is true that a few of the Court's recent decisions construing Congress's affirmative power under the Commerce Clause have taken a narrower view of that power than that reflected in some of the Court's more sweeping earlier pronouncements. Thus, in *United States v. Morrison*,[17] the Court held that Congress lacks the power under the Commerce Clause to provide a civil remedy for victims of gender-motivated violence because gender-motivated crimes do not substantially affect interstate commerce. Likewise, in *United States v. Lopez*,[18] the Court held that Congress lacks the power under the Commerce Clause to prohibit possession of firearms in school zones because possession of a gun in a local school zone does not substantially affect interstate commerce. But these decisions do not seriously

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[12] As noted above, the Commerce Clause by its terms is simply an affirmative grant to Congress "[t]o regulate commerce . . . among the several States . . . ." U.S. Const. art. I, § 8. However, since the early nineteenth century, the U.S. Supreme Court has read this affirmative grant to carry with it certain implied limitations on state authority, even in the absence of affirmative congressional action. These implied, judicially developed Commerce Clause restraints are frequently referred to as the "negative" or "dormant" Commerce Clause.

[13] *Quill*, 504 U.S. at 318.

[14] 441 U.S. 141 (1979).

[15] *Id.* at 150.

[16] *Id.* (citations to *Wickard v. Filburn*, *Katzenbach v. McClung*, *and Heart of Atlanta Motel v. United States* omitted).

[17] 529 U.S. 598 (2000).

[18] 514 U.S. 549 (1995).

inhibit the extensive power that Congress clearly possesses to deal with the problems raised by state taxation of interstate commerce, and, in particular, state taxation of employees who temporarily work in a state in pursuit of interstate commerce.[19]

II. THERE IS SUBSTANTIAL HISTORICAL PRECEDENT FOR THE ENACTMENT OF FEDERAL LEGISLATION ANALOGOUS TO THE MOBILE WORKFORCE STATE INCOME TAX FAIRNESS AND SIMPLIFICATION ACT OF 2007

Although Congress has never enacted comprehensive legislation limiting state taxation of interstate commerce, there is a considerable body of federal legislation directed at specific problems raised by such taxation. These targeted federal statutory restraints on the exercise of state tax power are in many respects analogous to the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007, because they constitute a particularized federal response to an identifiable problem that, in Congress's view, threatened to burden interstate commerce. I describe these targeted federal statutory restraints below.

A. Taxes on Employees Engaged in Interstate Transportation

Perhaps the most pertinent historical precedent for the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007 is federal legislation that currently restricts the power of states to tax the compensation of nonresident employees engaged in interstate transportation within the state. Federal statutes prohibit a state, other than the state of the employee's residence, from taxing the employee's compensation from an interstate rail carrier, motor carrier, or merchant mariner.[20] Federal law limits the states'

[19] *See generally* Walter Hellerstein, "Federal Constitutional Limitations on Congressional Power to Legislate Regarding State Taxation of Electronic Commerce," 53 *National Tax Journal* 1307 (2000). Indeed, even though the Court in *Lopez* made it plain that Congress's power to legislate under the Commerce Clause is not unlimited, it did so in an opinion that reaffirmed, rather than discredited, the essential contours of the Court's affirmative Commerce Clause doctrine. Thus, after summarizing the "era of Commerce Clause jurisprudence that greatly expanded the previous defined authority of Congress under that Clause," *Lopez*, 514 U.S. at 556, the Court identified "three broad categories of activity that Congress may regulate under its commerce power" (*id*):

> First, Congress may regulate the use of the channels of interstate commerce. . . . Second, Congress is empowered to regulate and protect the instrumentalities of interstate commerce, or persons or things in interstate commerce, even though the threat may come only from intrastate activities. . . . Finally, Congress' commerce authority includes the power to regulate those activities having a substantial relation to interstate commerce, . . . *i.e.*, those activities that substantially affect interstate commerce.

Id. at 567. As noted above, the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007 falls comfortably within the third category of those activities over which Congress may exercise its Commerce Clause authority.

[20] See 49 U.S.C. § 11502 (railroad employees); 49 U.S.C. § 14503 (motor carrier employees); 46 U.S.C. § 11108(b) (merchant mariner employees).

power to tax the compensation of employees who perform regularly assigned duties on interstate air carriers in more than one state to the state of the employee's residence and to the state in which the employee earns more than 50 percent of the compensation paid by the carrier to such employee.[21] Federal law also imposes limits on the states' authority to require withholding of income taxes from certain employees of water carriers.[22]

B. Taxes on Nonresidents' Retirement Income

In 1996, Congress enacted legislation prohibiting a state from imposing "an income tax on any retirement income of an individual who is not a resident or domiciliary of such State (as determined under the laws of such state)."[23] The legislation defines "retirement income" as distributions from qualified plans under the Internal Revenue Code as well as distributions from certain nonqualified plans that mirror qualified plans. As a consequence, the states are now substantially restrained in their ability to tax nonresidents on their retirement income on a "source" basis.

C. Net Income Taxes on Sellers of Tangible Personal Property Whose Activities in the State Do Not Exceed "Solicitation of Orders"

The most important piece of legislation that Congress has enacted limiting the states' power to tax interstate business is Public Law 86–272.[24] The legislation was enacted in 1959 as a specific response to the U.S. Supreme Court's decision in *Northwestern States Portland Cement Co. v. Minnesota*,[25] which explicitly held for the first time that the states possessed power to impose a fairly apportioned corporate net income tax on taxpayers engaged exclusively in interstate commerce. Congress feared that expanded state taxing authority over interstate business would burden interstate commerce. Public Law 86-272 prohibited the states from imposing a net income tax upon persons whose activities within a state do not exceed "solicitation of orders" for sales of tangible personal property fulfilled from outside the state – precisely the type of activity that was at issue in *Northwestern*.

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[21] 49 U.S.C. § 40116(f)(2).

[22] 46 U.S.C. § 11108(a) provides that wages due or accruing to a master or seaman on a vessel in the foreign, coastwise, intercoastal, interstate, or noncontiguous trade or an individual employed on a fishing vessel or any fish processing vessel may not be withheld under the tax laws of a state or a political subdivision of a state. However, the statute does not prohibit withholding wages of a seaman on a vessel in the coastwise trade between ports in the same state if the withholding is under a voluntary agreement between the seaman and employer of the seaman. Moreover, the law does not affect the liability of these employees for state income taxes.

[23] Pub. L. No. 104-95, 109 Stat. 979 (1996), codified at 4 U.S.C. § 114.

[24] 73 Stat. 55 (1959), codified at 15 U.S.C. § 381 *et seq.*

[25] 358 U.S. 450 (1958).

D. Taxes on Air Travel and Transportation

In 1970, Congress enacted legislation designed to assist states and localities in improving the nation's air transportation system (including the imposition of several federal aviation taxes to fund local airport expansion and improvement).[26] In 1972, the U.S. Supreme Court held that neither this legislation nor the Commerce Clause prevented states or localities from imposing charges designed to recoup the costs of airport construction and maintenance.[27] Congress responded to this decision by enacting a statute providing that "[n]o State...shall levy or collect a tax, fee, head charge, or other charge, directly or indirectly, on persons traveling in air commerce or on the carriage of persons in air commerce or on the sale of air transportation or the gross receipts derived therefrom."[28]

E. Discriminatory Taxes on Rail Carrier, Motor Carrier, and Air Carrier Transportation Property

1. Rail Carrier Property

In response to widespread complaints of state and local tax discrimination against railroads, Congress in 1976 adopted a special statute prohibiting the states from taxing rail transportation property at a higher ratio to its true market value than the ratio that the assessed value of other commercial and industrial property in the same assessment jurisdiction bore to the true market value of such other commercial and industrial property.[29] The statute also prohibits ad valorem property taxation of rail transportation property at a higher rate than that applicable to other commercial and industrial property.

2. Motor Carrier Property

In 1980, Congress extended to motor carriers protection against discriminatory state property taxes that is similar to protection it had previously enacted for railroads.[30] The principal difference between the statutes is that the motor carrier statute does not contain any provision prohibiting the states from imposing nonproperty taxes that discriminate against motor carriers.

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[26] See *Aloha Airlines, Inc. v. Director of Taxation*, 464 U.S. 7, 8-9 (1983).

[27] *Evansville-Vanderburgh Airport Authority District v. Delta Airlines*, 405 U.S. 707 (1972).

[28] Pub. L. No. 93-44, § 7(a), 87 Stat. 88, 90 (1973), codified in slightly different language at 49 U.S.C. § 40116(b).

[29] Pub. L. No. 94-210, § 306, 90 Stat. 31, 54 (1976), codified at 49 U.S.C. § 11501(b).

[30] See 49 U.S.C. § 14502.

3. Air Carrier Property

In 1982, Congress extended to air carriers protection similar to that which it had provided for motor carriers, except for federal court jurisdiction.[31]

F. Taxes Affecting Employee Benefit Plans Protected by the Employee Retirement Income Security Act (ERISA)

In enacting the Employee Retirement Income Security Act (ERISA),[32] Congress preempted state taxes affecting employee benefit plans, by providing that the Act "supersede[s] any and all State laws insofar as they may now or hereafter relate to any employee benefit plan."[33]

G. Energy Taxes Discriminating Against Interstate Commerce

In 1976, Congress enacted legislation prohibiting the states from imposing taxes on or with respect to the generation or transmission of electricity that discriminate against out-of-state manufacturers, producers, wholesalers, retailers, or consumers of electricity.[34] The history of the legislation indicated that it was directed specifically at a New Mexico tax, which the U.S. Supreme Court ultimately invalidated under the legislation.[35]

H. Taxes Interfering With Federal "Superfund" Legislation

The Federal Comprehensive Environmental Response, Compensation, and Liability Act,[36] the so-called Superfund legislation, preempts state taxes whose "purpose" is to provide "compensation for claims for any costs of response or damages or claims which may be compensated under this [Act]."[37]

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[31] See 49 U.S.C. § 40116.

[32] 29 U.S.C. § 1001 *et seq.*

[33] 29 U.S.C. § 1144(a).

[34] Tax Reform Act of 1976, § 2121(a), 90 Stat. 1914 (1976), codified at 15 U.S.C. § 391.

[35] *Arizona Public Service Co. v. Snead*, 441 U.S. 141 (1979).

[36] 42 U.S.C. § 9614(c).

[37] *Id.*

I. Taxes on Internet-Related Activities

In 1998, Congress enacted the Internet Tax Freedom Act (ITFA).[38] The Act imposed a three-year moratorium on three types of taxes: (1) taxes on Internet access; (2) discriminatory taxes on electronic commerce; and (3) multiple taxes on electronic commerce. In 2001, Congress extended the moratorium without change for two more years. Although the moratorium technically expired in 2003, Congress retroactively reextended the moratorium in 2004 for another four years through November 1, 2007. A further proposed extension is currently pending before Congress.

J. Taxes on Interstate Passenger Transportation by Motor Carrier

In response to the U.S. Supreme Court's decision in *Oklahoma Tax Commission v. Jefferson Lines, Inc.*,[39] which sustained a state tax on the purchase of interstate transportation services, Congress passed legislation in 1995 effectively overruling the decision.[40] The legislation bars a state or political subdivision thereof from imposing a tax or other charge on (1) a passenger traveling in interstate commerce by motor carrier; (2) the transportation of a passenger traveling in interstate commerce by motor carrier; (3) the sale of passenger transportation in interstate commerce by motor carrier; or (4) the gross receipts derived from such transportation.[41] After an Illinois court held that this statute did not bar a tax on commercial vehicle operators who transported passengers within Illinois when the passengers had prearranged such transportation in connection with an interstate journey by air,[42] Congress once again legislated and overruled the decision by providing that "[n]o State or political subdivision thereof…shall enact…any law…requiring a license or fee on account of the fact that a motor vehicle is providing pre-arranged ground transportation service"[43] when the service involves transportation from one state to another or transportation within a state with intermediate stops in another state.

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[38] Pub. L. No. 105–277, §§ 1101–04, 112 Stat. 2681–719 to 2681–726 (1998).

[39] 414 U.S. 175 (1995).

[40] Pub. L. No. 104–88, 109 Stat. 803 (1995), codified at 49 U.S.C. § 14505.

[41] *Id.*

[42] *Tri-State Coach Lines, Inc. v. Metropolitan Pier and Exposition Authority*, 732 N.E.2d 1137 (Ill. App. 2000), *appeal denied*, 738 N.E.2d 936 (2000), *cert. denied*, 532 U.S. 994 (2001).

[43] Pub. L. No. 107-298, 116 Stat. 2342 (2002), codified at 49 U.S.C. § 14501(d).

K. Local Taxes on Direct-to-Home Satellite Service Providers

Congress has prohibited localities from imposing taxes on providers of direct-to-home satellite services.[44]

L. Stock Transfer Taxes

Congress prohibits states from imposing stock transfer taxes based solely on the in-state physical location of facilities of registered clearing agencies or registered transfer agents.[45]

* * *

In sum, there is substantial historical precedent for the type of targeted congressional legislation limiting state taxing authority under the Commerce Clause that is reflected in the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007.

III. ENACTMENT OF THE MOBILE WORKFORCE STATE INCOME TAX FAIRNESS AND SIMPLIFICATION ACT OF 2007 WOULD CONSTITUTE AN APPROPRIATE EXERCISE OF CONGRESSIONAL POWER

In my opinion, enactment of the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007 would constitute an appropriate exercise of congressional power. In expressing this opinion, I wish to make it clear that I believe the states have a legitimate interest in assuring that workers who earn income in the state pay their fair share of the state tax burden for the benefits and protections that the state provides to them. The states' legitimate interest, however, must be balanced against the burdens that are imposed on multistate enterprises, and on the conduct of interstate commerce, by uncertain, inconsistent, and unreasonable withholding obligations imposed by the states. Indeed, it is telling that a number of states themselves have implicitly recognized these burdens by adopting reciprocal provisions exempting income, or certain classes of income, earned by nonresidents in their state if the nonresident's home state grants a similar exemption to residents of the exemption-granting state.[46]

[44] Pub. L. No. 104-104, tit. VI, § 602(a), 110 Stat. 144(a) (1996) (reprinted at 47 U.S.C. § 152, historical and statutory notes).

[45] 15 U.S.C. § 78bb(d).

[46] The following states have entered into reciprocal agreements exempting compensation paid in their states to residents of other states:

STATE	AGREEMENT WITH
Illinois	IA, KY, MI, WI
Indiana	KY, MI, OH, PA, WI

In the end, although there may well be room for additional fine-tuning of the statutory language to assure that the right balance is struck between the states' legitimate interests in revenue raising and the nation's interest in preserving our national common market, I believe that a targeted response to the specific problem reflected in the proposed Mobile Workforce State Income Tax Fairness and Simplification Act of 2007 is an appropriate exercise of the congressional commerce power.

(note 46, continued)

STATE	AGREEMENT WITH
Iowa	IL
Kentucky	IL, IN, MI, OH, VA, WV, WI
Maryland	DC, PA, VA, WV
Michigan	IL, IN, KY, MN, OH, WI
Minnesota	MI, ND, WI
Montana	ND
New Jersey	PA
North Dakota	MN, MT
Ohio	IN, KY, MI, PA, WV
Pennsylvania	IN, MD, NJ, OH, VA, WV
Virginia	DC, KY, MD, PA, WV
West Virginia	KY, MD, OH, PA, VA
Wisconsin	IL, IN, KY, MI, MN

See RIA State and Local Tax Services for individual states, available at www.checkpoint.riag.com (¶¶ 55,205, 55,325, and 55,875 for individual states).

Ms. SÁNCHEZ. Thank you very much for your testimony.

We are now going to begin our questioning. And I will begin by recognizing myself for 5 minutes.

Mr. Lindholm, in your written testimony for today's hearing you argue that a dollar amount threshold as opposed to a days worked threshold like the one in H.R. 3359 would be more burdensome because each employee would have to be tracked on a daily basis. And it seems that in either a days worked or a dollar amount threshold the employer is going to need to be tracking the employee anyway. So I am interested in knowing why you think that one is a superior method than the other.

Mr. LINDHOLM. Well, two points, Madam Chairwoman. Let me address first with respect to the 60 days. Most travel is temporary in nature. And most employees don't travel anywhere close to the 60 days. So they automatically would not be within that pool of employees that an employer would track.

Secondly, with respect to the dollar threshold itself, it really does require not just a tracking of their whereabouts, but a tracking of very sensitive payroll data within the company. And it increases the exposure of that payroll data among employees of the company, which obviously is a very sensitive thing.

And, you know, I think the FTA has proposed a combination dollar-day with a dollar backstop. The other issue there is that it would, in effect, separate the liability question, could make that rule distinct from the withholding obligation. And when you have got those two operating under separate rules, it increases the complexity greatly.

Ms. SÁNCHEZ. But how would you respond to Mr. Duncan's concern that 60 days is quite a long time before triggering the liability?

Mr. LINDHOLM. You know, Congress has enacted several, as Professor Hellerstein pointed out, several protective or analogous pieces of legislation. Airline employees—it is their resident State or the State where they earn 50 percent or more of their pay. For motor carrier employees, rail carrier employees, Members of Congress, they, in effect—Congress has, in effect, enacted a 365-day threshold.

And, you know, the—from our standpoint, a number of States also have enacted reciprocal agreements, which are, in effect, a 365-day threshold. So in our sense, the 60-day pretty much draws a very effective line in the sand for those traveling employees.

Ms. SÁNCHEZ. Mr. Duncan, I want to give you an opportunity to respond to some of these complexities. Now, you are advocating a clarification of the definition of what a day worked is. Can you talk about that?

Mr. DUNCAN. Yes, that is right. In our testimony, we have suggested that the definition of day needs to be changed. As it is contained in the bill—and I apologize I don't have a copy in front of me. But it says a day is defined as a day in which the employee performs more than 50 percent of the work duties in a State.

To me, I don't know what that means. I don't know what performing more than 50 percent of the work duties are. Is it by time? Is it by value? Is it—I don't want to be flip, but how hard it was?

So we have suggested that it should be—a day should be a day or any part of a day.

And remember we say that because that is the easiest thing to count. That is the least controversial thing. And we are only using it to determine whether the threshold is met. And for that reason, we think the day or any part of a day is workable.

That is the way a number of States are now. That is the way Federal law with respect to the taxation of nonresident aliens that are working in the State operates as well.

Ms. SÁNCHEZ. Thank you, Mr. Duncan.

Ms. Nelson, I am interested, since you are the expert on payroll, under the 60-day threshold, if an employee hits the 60-day threshold late in the year, the employee's paycheck would reflect withholding for the 60 days. For some employees that could be a huge dent in their paycheck.

Although a lower threshold is a possibility and would seem like less of a hardship on an employee once they hit that, what are some of the things that a payroll department or company could do to perhaps lessen the hardship of a 60-day trigger? You know, could they spread those out, those withholdings out over several paychecks? Do you have any thoughts on that?

Ms. NELSON. Well, I think just addressing some kind of threshold across all States would first just ease my burden as a payroll professional.

Ms. SÁNCHEZ. I understand.

Ms. NELSON. Yes, and so——

Ms. SÁNCHEZ. Maybe you could look at it from the perspective it also keeps you employed.

Ms. NELSON. Yes, there is that. But because of DOL I have plenty of those job securities.

So to answer your question, yes, we could find a way to, you know, pass those payments off during, you know, each check retrospectively for however many pay periods. I mean, there would be ways to manage it.

Ms. SÁNCHEZ. You mean there are ways to help minimize that? Okay.

Ms. NELSON. Yes.

Ms. SÁNCHEZ. My time has expired.

And at this time, I would invite Mr. Johnson for his 5 minutes of questions.

Mr. JOHNSON. Madam Chair, my friend from North Carolina has an important engagement that he needs to attend to, so I would yield my position and allow him to move in front of me, if that is okay with the Chair.

Ms. SÁNCHEZ. Excellent. I think that is fine.

Mr. Watt, you are recognized for 5 minutes.

Mr. WATT. I thank the wonderful Chairperson of this Subcommittee. And I thank my colleague from Georgia for allowing me to go in front of him.

I think maybe before I ask a question I will confess that our Chairperson who Chairs this Subcommittee may be now understanding why I opted not to become the Chair of the Subcommittee. It was the combination of Internet taxation. This individual issue that we are having the hearing about today, remote sales taxation, and collection of those remote sales, and physical presence—those are about the four most difficult taxation issues that are really out there. And so, I decided that Chairing a Subcommittee on financial services and dealing with predatory lending was actually easier than dealing with this.

But I am delighted that the Chair is taking on these issues because there needs to be more discussion about it. And she has done a masterful job of passing the Internet taxation moratorium. And I saw the Senate and everybody is now onboard with that. So if she can pull that rabbit out of that hat for Internet taxation, maybe she has got three more rabbits in the hat. And if anybody can do it, I have confidence that my Chair——

Ms. SÁNCHEZ. But no pressure, right, Mr. Watt?

Mr. WATT. No pressure, no pressure. But I am confident that she can do it.

These are difficult issues. And as Ranking Member of the Subcommittee for two or three or however many—it seemed like forever, I got an appreciation of how difficult the issues are.

Let me ask Mr. Duncan first. One of the things that always was told to me in the context of both this issue and the remote sales issue was that there was a series of negotiations going on and there might be some possibility that all the stakeholders would find common ground and make this easier for us. I think in the remote sales area, we even passed some kind of threshold that said if a certain number of States passed a model statute then the Federal Government would act.

Talk to me, Mr. Lindholm and Mr. Duncan, about the impediments to you all getting together and working something out that is mutually satisfactory. Because the States obviously have a very serious interest in this issue, as do businesses and employees. What is the status of those discussions? And are you all just deluding us when you say these discussions are going on and we are going to work this out at some point?

Mr. DUNCAN. I don't think we are trying to fool you. I don't know anything about financial services, but maybe I could learn so I could leave these issues sometime, too.

Mr. WATT. If you want to go over and tackle the massive foreclosures that are going on, we will welcome you over there.

Mr. DUNCAN. No, thank you. As I indicated in our testimony, we have been in conversations and discussions with the business community about this. We have had a working group of State people to make sure that we understand the bill and that we try to get some real world experience from them.

In addition, I can guarantee you that our people understand the burden issues and the difficulties of compliance. We have not at this point had a board action from our organization that says we are prepared to begin negotiating or at least, you know, enter into something to resolve this issue with the Council of State Taxation. I am to report back based on this hearing and we will, I am certain, have further conversations because our people do understand the burden issue and that it needs to be addressed.

Mr. WATT. I know you want to respond. But let me just say I applaud the Chair for taking on the issue. It seems to me that the ramping up of this as an issue and the movement of employees as much as they move kind of ramped up at the same time that technology was ramping up. And one would hope that there would be some technological answer to this that would allow the movement.

I don't know that technology or the system—as you say in one place in your testimony, Ms. Nelson, there is no system to take care of this, the way it is being done now. But I don't see any system, any payroll system to take care of it under the 60-day threshold, either. And that is not a knock on the 60-day threshold.

I just think there are some real technical problems. And I hope technology will make some advances at the same time that movement makes advances to make this easier. I mean, it is just a very, very difficult issue.

I don't envy you, Madam Chair. But I am going to yield back my time to you and rely on you to pull those other three rabbits out of the hat.

Ms. SÁNCHEZ. Thank you, Mr. Watt. And we appreciate your participation in today's hearing.

Now I think it is appropriate that we hear from one of the bill's authors and allow him to ask questions that he may have.

So, Mr. Johnson, you are recognized.

Mr. JOHNSON. Thank you, Madam Chair.

Mr. Duncan, you have indicated in your testimony or you stated that complying with the current system is burdensome and impractical for businesses. Is that a fair assessment?

Mr. DUNCAN. I think the way I framed it was that where there is no de minimis standard in a State, where there isn't a 15-day or 20-day de minimis threshold and where liability and withholding presumably would trigger on day one, I think we would all say that is impractical.

Mr. JOHNSON. And we just have a multiplicity of rules now among the States that make the entire effort to collect income taxes from nonresidents, temporary workers impractical and burdensome at this point, even for the tax administrators. Is it not?

Mr. DUNCAN. There are certainly issues in terms of collecting tax from nonresidents. First of all, you have to have the information flows and reports so that you know who has performed services, the income earned from the State. Then there is the collection issues as well.

Mr. JOHNSON. Pretty much voluntary information and collections that have to be forwarded to you by the businesses. And it definitely can impact the amount of money that States collect for income taxes due. Is that correct?

Mr. DUNCAN. Yes. I mean, there is—you know, what we would like to have is the withholding, the voluntary remittances withholding following up with the information reports. I think it is not——

Mr. JOHNSON. It is difficult for businesses to comply, say a small business, a number of small businesses. It is difficult for them to understand what the rules are and then perhaps they will not forward those payments in, if you will.

Mr. DUNCAN. Just two quick points. I think you are right, that if we can make the rules clear and administerable, compliance can improve, particularly in the small business community. Second, there are a number of States with significant enforcement programs in the nonresident area. But I wouldn't argue your central point that if it is simpler and clearer, compliance will improve. The question, of course, is one of balance as to how to construct the threshold and where that threshold ought to be.

Mr. JOHNSON. Let me ask this question. Has there been a collective effort by the States to come up with uniform and simple method for the collection for nonresidents?

Mr. DUNCAN. There has not been an effort that has gathered the 41 States together to do it. We have areas where the States share borders, share economies, have similar tax systems where they have had reciprocity agreements. I think what——

Mr. JOHNSON. It would be ideal, would it not, that there would be some national uniform standard that everyone could stand easily and comply with?

Mr. DUNCAN. That would certainly make the task of withholding knowing when one has an obligation simpler.

Mr. JOHNSON. But you have no objection to a Federal solution to this problem? You just have a problem with the substance of the solution that has been proposed. Is that a fair assessment?

Mr. DUNCAN. The position of our group is that the bill as introduced goes too far and that we are in a position to have to oppose the bill as it has been introduced. We have tried to lay out the issues as clearly as we can.

Mr. JOHNSON. Okay. I understand. So you really would like to see a dollar threshold along with a threshold as far as number of days?

Mr. DUNCAN. We believe that that can bring all the benefits of the burden reduction and at the same time, minimize the risk and exposure of States, yes, sir.

Mr. JOHNSON. Do you have any specifics on both of those points? How many days would be suitable to tax administrators and what dollar amount would be suitable?

Mr. DUNCAN. I am not in a position to be able to give those to you today. We don't have those at this point. In part there is a couple of moving parts here. There is a seesaw function to it that if the days threshold is relatively high, then perhaps the dollar threshold needs to be relatively lower or vice versa because we are trying to achieve a balance and reduce risk and exposure. And so, I think—I don't have a ready-made solution to provide you today on that.

Mr. JOHNSON. Mr. Lindholm, would you care to weigh in on that?

Mr. LINDHOLM. Yes, thank you, Congressman Johnson. First of all to address the issue of our efforts to resolve some of our differences, I very much appreciate the—you know, we have met with Harley and his group several times to talk about this issue. And I think we have a fundamental difference in perspective in that I think the States' viewpoint is a collective viewpoint of how this issue affects each administrator of a specific State.

And that is rightly so. That is the job that they are hired to do. That is the job that they are appointed to do in some cases.

But I would submit that we should view this from the perspective of how many more people would be in compliance. I think there is a tendency to say from a State administrator's perspective to look at this bill and say how many people are paying now that would not be paying in our State because of this change in the law. But if you look at this from a national perspective, then you can point a finger to how many more people would be able to comply with this law.

Secondly, if I could address Mr. Watt's question about the technology, can we come up with technology to do this. Yes, it is possible, but at great expense. And I think the question that this Committee ought to address is although it is possible whether it is sensible to force companies to do so when a simple and practical solution is at hand that would prevent that.

Ms. SÁNCHEZ. Mr. Johnson, your time has expired. But if you have further questions, I don't think there would be objection to some additional time.

Mr. JOHNSON. Thank you, Madam Chair.

Ms. SÁNCHEZ. I will recognize you for an additional 3 minutes of questions.

Mr. JOHNSON. Mr. Lindholm, would the Council on State Taxation be opposed to the threshold requirement that—a dollars feature as well as days? Is that something that you oppose in principle, and why?

Mr. LINDHOLM. I think we would, Congressman. And I think the difficulty there is that any time you have a dollar threshold, you are forced to track, as I said, every employee that conceivably could spend time there and not just for those—for the day period, but for the—you know, everybody's dollar amount if they exceed that threshold.

The second issue is that under their proposed solution, there is a tendency to look at—it bifurcates the tax liability with the—from the withholding obligation. And anytime you do that, you have got employees that are potentially under-withheld or over-withheld. And it complicates things tremendously for employers trying to withhold for the proper allocation of proper States.

Mr. JOHNSON. Isn't it a fact, by the way, that most employees who have been—whose wages have been withheld to do their work in other States—isn't it a fact that most of them end up getting credits from that State because the amount of tax and the amount of wages earned is below the amount necessary for taxation?

Mr. LINDHOLM. That is precisely correct. And let us say I, for example, travel to 10 States and happen to trigger whatever the—either the wage threshold or the day threshold in those States, I am then required to file a return in each of those States and then file a credit against my return in the state of Virginia. And again, all those 10 returns where I entered that threshold would not be necessary, since I am getting a lot of credit for that anyway.

It ends up being a wash between State-to-State, unless, of course, there is a differentiation between the rates. But effectively the 60-day threshold would allow the resident State to continue withholding regardless of where they traveled, unless it was clear that that employee was on a long-term assignment and expected to be on a long-term assignment within that State, within the nonresident State.

Mr. JOHNSON. Thank you.

Ms. SÁNCHEZ. Thank you, Mr. Johnson. And I think this has been a very enlightening hearing trying to figure out how we can balance the interests of State and local governments' concerns about loss of revenue while eliminating some of the complexities and not having a uniform national standard.

And it is an ongoing battle. While obviously there is not a complete agreement among everyone, my hope is that they will be able to incorporate some of the information that you have shared with us today and try to bring about a solution that is acceptable.

I want to thank all of the witnesses for their testimony today. Without objection, Members will have 5 legislative days to submit any additional written questions which we will forward to the witnesses and ask that you answer as promptly as you can so that they can be made a part of the record. And without objection, the record will remain open for 5 legislative days for the submission of any additional materials.

Again, I thank everybody for their time and their patience. And this hearing on the Subcommittee of Commercial and Administrative Law is adjourned.

[Whereupon, at 1:09 p.m., the Subcommittee was adjourned.]

A P P E N D I X

Material Submitted for the Hearing Record

ANSWERS TO POST-HEARING QUESTIONS FROM DOUGLAS LINDHOLM, PRESIDENT AND EXECUTIVE DIRECTOR, COUNCIL ON STATE TAXATION, WASHINGTON, DC

COST
COUNCIL ON STATE TAXATION

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December 20, 2007

Via email

Mr. Adam Russell
Subcommittee on Commercial and Administrative Law
Committee on the Judiciary
2138 Rayburn House Office Building
Washington, DC 20515-3951

Re: Questions for the Record - Hearing on H.R. 3359, The Mobile Workforce State Income Tax Fairness and Simplification Act of 2007, November 1, 2007

Dear Mr. Russell,

Please find below responses to the additional questions for the hearing record posed by the Subcommittee on Commercial and Administrative Law and Chairwoman Sanchez regarding the Subcommittee hearing on H.R. 3359, the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007.

1. Mr. Lindholm, in your testimony you state that the uniform rules, such as those set forth in H.R. 3359 are needed now. Could you elaborate on the reasons you believe that Congress should take action on this issue at this time?

There are a number of reasons why resolution of this issue has reached a critical stage. First, Section 404 of the Sarbanes Oxley Act of 2002 requires company management to certify that processes and procedures are in place to comply with applicable laws and regulations, including state tax laws. This provision, along with a commensurate desire by corporations to be fully compliant with all rules and requirements as part of corporate governance responsibilities, has increased the interest by employers in desiring uniformity and simplicity in matters of nonresident state income and withholding laws.

Second, employers have a significant interest in ensuring that employees comply with all state law taxation requirements. COST members are acutely aware of the burdens placed on their employees who travel outside their resident states for business. They have expressed a strong desire to meet their responsibilities as employers by assuring their employees comply with these burdens. Unfortunately, the current patchwork of state rules renders employees' abilities to comply with nonresident state law requirements extremely challenging.

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Third, COST members have noticed an increasing amount of state audit activity focusing on nonresident withholding requirements. While these audits appear to be limited to a few states, this development highlights the need for Congress to take action now on this issue.

2. Could you elaborate on your testimony on why the sixty day threshold is important, and why a dollar amount threshold is less desirable?

A sixty-day threshold is important because it would significantly enhance and simplify compliance while at the same time not unduly interfere with state revenues. With a uniform sixty-day threshold, the majority of employees who travel for business would not be subject to nonresident state taxation. They would remain fully taxable in their resident states, with the employer fulfilling the normal withholding obligations on those resident state earnings.

A sixty-day threshold also allows employers to focus their compliance and education efforts on a small pool of employees who are more likely to have extended duties at nonresident state locations. Shorter time periods would increase the likelihood that employees would "back into" the nonresident state rules unknowingly through intermittent trips of short duration and would impose greater burdens on employers to identify and educate those "at-risk" employees.

A dollar threshold is significantly less desirable because it completely nullifies the potential compliance gains and simplification from a uniform federal rule. In fact, COST believes that a dollar threshold would create even more onerous burdens than exist in many cases under the current patchwork of state laws.

From a practical perspective, a dollar threshold would force employees to guess: 1) their annual compensation for the coming year; and 2) the number of days they will work that year. From those figures, each employee would estimate his or her income on a per day basis.

Although that calculation may seem simple, it is not. While a "day" is the same everywhere, the concept of "income" is defined differently in every state. A dollar threshold would thus require either a federal definition of "income" – a concept that would significantly intrude on state tax statutes – or employees would be required to research each specific state statute where they expect to travel in order to calculate their earnings on a per day basis. In addition, compensation plans have changed dramatically over the decades, and few employees, especially those who travel frequently, earn income today at a consistent and flat rate over the course of a year. For example, it is common practice for many employers to award year-end bonuses to employees based on their performance throughout the year as well as the overall company results. Thus, in most cases, it is impossible for either the employee or the employer to know until year-end exactly how much an employee has earned for that year. The number of days an employee will work in any given year is similarly uncertain. (For example, would paid vacation, holiday and sick leave be included in determining the "per day" income? What about paid or unpaid leave?)

Furthermore, when employees travel they do not think in terms of the "dollars" earned while they are away from home, but the "days" they are on business travel. In other words, a dollar threshold would be converted by employees and employers into a day threshold, except that this day threshold would vary widely by employee and would merely be a guess. Such a rule is not simple, would not ease compliance for employees or employers (or state auditors), and it would not be a meaningful or positive change from the current patchwork system.

In their testimony, the Federation of Tax Administrators recommended a bifurcated rule under which employer withholding rules would be different than personal income tax liability rules. Under their proposal, employer withholding would be required only in the employee's state of residence and a nonresident state in which the employee has performed duties in excess of a certain number of days. The personal income tax filing requirement, on the other hand, would be triggered if the nonresident employee either performed duties in the nonresident state over the threshold number of days or had income in excess of some dollar threshold in the state. We respectfully submit that decoupling the withholding requirements from the personal income tax liability would provide no benefit to employees struggling to properly comply on their own, with necessary allocations and calculations, without the benefit of companion employer rules. It is a fair statement that employee-only compliance under any bifurcated system would be nearly impossible. A bifurcated approach also would not benefit employers because of the great importance employers place on facilitating full compliance by their employees with all applicable state tax laws.

3. The FTA is concerned about how compensation paid over multiple years and/or stock options would be affected by this legislation. What is your take on that?

COST recognizes that there are a multitude of issues and complexities inherent in the state personal income tax arena. COST understands that the purpose of HR 3359 is to set a uniform, national threshold for nonresident personal income taxes and not to address all issues associated with state taxation of employee compensation or to provide a series of uniform federal rules that would supersede state rules on many compensation issues. Under H.R. 3359, residents and nonresidents who exceed the sixty day threshold would continue to have compensation that was paid over multiple years and/or via stock options taxed as provided under current state laws.

4. How did COST come up with the estimates on state tax revenue that you included with your testimony?

COST retained the Quantitative Economics and Statistics Group at Ernst & Young LLP to estimate the state tax revenue impact of H.R. 3359.

The revenue impact estimates are based on information collected from a survey of state tax agencies, publicly reported state and local income tax collection information from state tax agencies and the U.S. Census *Governmental Finances*, U.S. Census data on state-by-state journey-to-work patterns, and Bureau of Economic Analysis estimates of the components of state personal income.

COST and Ernst & Young worked with staff at the Federation of Tax Administrators and the Multistate Tax Commission to survey state tax agencies for personal income tax information to be used in the estimating process.[1] Detailed information was received from seventeen states, including California, Connecticut, New Jersey and New York.

The methodology used by Ernst & Young is described below.

<u>Revenue Reductions from Nonresidents</u>

The first step in the estimation process was to develop state-by-state estimates of the amount of wages attributable to nonresident tax filers. This wage component was either reported by the states responding

[1] At the time of the survey, the bill implementing the nonresident income and withholding tax provisions was H.R. 6167.

to the survey or imputed using federal tax return ratios of wages to adjusted gross income (AGI) and adjusted gross income for nonresidents reported by the states.[2] A share of the estimated nonresident wages was removed from the state's taxable income to account for the impact of H.R. 3359.

The adjustment share was based on information reported on the state surveys and the relationship between a state's current *de minimis* rules and the 60-day provision in the bill. In addition, the reduction in taxable wages included adjustments for 1) any nonresident reciprocity agreements that currently exclude nonresident wages from the income tax base in work states covered by the agreements, 2) the impact of convenience of employer rules, and 3) the fact the bill's provisions would not apply to professional athletes and entertainers. The adjustment shares calculated for the survey states were then used to impute estimates to the rest of the states depending upon individual state economic characteristics and current tax law features.

The loss in taxable wages was then multiplied by the state (and local, if applicable) top marginal tax rate to generate the estimated state-by-state direct revenue reductions due to H.R. 3359.

<u>Estimating Offsets Due to Reductions in Resident Credits</u>

In most states, the direct individual income tax reductions from H.R. 3359 are offset in part by reduced credits on resident tax returns for taxes paid in the work state. The key component in determining reductions in resident income tax credits is the mapping of worker flows from resident states to work states. This mapping of worker flows is derived from the U.S. Census *Journey-to-Work* (JTW) survey conducted in 2000, the latest available year. The survey captured the work location of each survey respondent in the week prior to the survey. Though intended to record full-time commuting patterns between counties and municipalities in the U.S., the JTW survey also captured commuting patterns for part-time commuters such as those affected by H.R. 3359.

The JTW's county-to-county commuting data was converted into a state-to-state mapping of nonresident worker flows. As the first step in assessing how tax reductions in work states are reflected as credit reductions in resident states, the distribution of resident states from which a given work state draws its employees was determined. For example, the two largest states providing Texas nonresident workers are New Mexico (17%) and Oklahoma (14%). This information was used to estimate a resident state's credit offsets due to the decrease in nonresident taxes due to H.R. 3359.

States generally limit the amount of credit allowed for taxes paid to nonresident states to the taxes that would have been paid in the resident state. To compensate for this ceiling on the size of allowed credits in resident states, the credit offsets between states were capped based on the ratio of the top marginal tax rate in the resident state to that in the work state. These caps on credits help explain why there is a small net revenue decrease for all states combined due to H.R. 3359.

<u>Net State-by-State Impacts</u>

The final step was to estimate the net impact of the bill on each state and the District of Columbia. The net impact is the difference between the reduction in taxes on nonresident workers and the higher taxes paid by residents through lower credits for taxes paid to other states.[3]

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[2] In some cases, non-resident wages were estimated from the combined amount of wages or income reported for non-resident and part-year residents. An additional data source, the U.S. Bureau of Economic Analysis estimates of state wages earned by non-residents, was used as a check on the state-by-state estimates of non-resident wages.
[3] All state estimates were inflated to fiscal year 2007 levels.

5. The legislation as written kicks in when the bright line 60-day threshold is met. What would the reporting, withholding and overall compliance burden be if the 60-day threshold straddles a filing quarter or occurs at the end of a taxable year? Do you believe a prospective instead of retroactive application is more practical and less burdensome?

As noted above, the 60-day threshold was chosen because it is a sufficiently long period such that most employees who travel for business duties would not be subject to nonresident state taxation. Employers, therefore, will be better able to focus their compliance and education efforts on a small pool of employees who have easily identified extended duties at nonresident state locations. Thus, in most circumstances, employees who may exceed the 60-day threshold during a calendar year will likely have notified their employer of that possibility and the employer would have initiated withholding as of the first day of work in the nonresident state.

If the employee failed to anticipate exceeding the 60-day threshold but nevertheless did so at the end of the taxable year, then the employee would be under-withheld in the nonresident state and over-withheld in the resident state. When filing the nonresident return, the employee would owe taxes but would receive an equivalent (or nearly equivalent) reduction in taxes in his or her resident state. The employee may also owe interest and penalties in the nonresident state, but that would likely occur only if the employee had been a taxpayer in the nonresident state in prior years (and thus should have been able to anticipate that taxes would also be owed in the current year). Of course, this same situation can occur under current law. H.R. 3359 would dramatically reduce the number of employees who would ever be in this position.

COST believes that with a 60-day threshold, the reporting issues and compliance burdens for both employees and employers are minimized. As a result, we believe either a retroactive or prospective application of the withholding requirements would be equally beneficial for employees and employers.

<u>Questions for Doug Lindholm from Chairwoman Sanchez</u>

1. When considering a day threshold, we must define what constitutes a day. H.R. 3359 seems to provide a vague definition of a day. What is your response to substituting "all or any part of a day in which the employee is present and performs services in the state" as Mr. Harley Duncan recommended in his prepared testimony and discussed in response to a question from the Chair?

COST notes that the goal of H.R. 3359 is to promote a simple and easily administered rule. Although the definition of a "day" in H.R. 3359 may seem vague to some, in practice it would ensure that each work day is assigned only to one state.

The definition of a "day" suggested by Mr. Duncan would require tracking multiple locations on a daily basis. More importantly, such a rule would, by design, ensure that many days are assigned to more than one state, which may expose employees to taxation of the same income by more than one state. Finally, substituting the language to include "any part of a day" would require complicated exceptions for certain types of temporary presence in a state, such as air travel, airport layovers, driving through a state en route to a work destination, or travel via interstate rail or motor carriers.

2. H.R. 3359 would set a uniform threshold across the nation. What are the benefits of a uniform threshold? Would not a 10-workday threshold or even a combination of a dollar-denominated and days-worked threshold benefit employers and employees?

There are many benefits to a uniform threshold, including the creation of a simple, easily administered rule that will lead to greatly increased compliance along with a concomitant reduction in administrative burdens on employers, compliance burdens on employees, and audit burdens on the states.

The purpose of a 60-day threshold is to significantly reduce the number of employees potentially subject to nonresident state withholding in a clear and certain manner. A 10-day threshold, comparatively, would substantially increase the number of employees subject to tax in nonresident states and enhance the possibility that employees would "back into" the nonresident state rules unknowingly through intermittent trips of short duration, and would provide commensurately greater burdens on employers to identify those employees, provide proper withholding and education on personal filing obligations.

A combination of a dollar-denominated and days-worked threshold would nullify the potential compliance gains and simplification from a uniform 60-day rule. In fact, as noted in greater detail in response to a previous question set forth above, COST believes that a dollar threshold would create even more onerous burdens than exist in many cases under the current patchwork of state laws. These burdens would include making inherently unworkable calculations of annual wages during the year and total days worked in a year.

3. How do you respond to Mr. Harley Duncan's concerns that a 60-workday threshold is about a quarter of the work year and thus effectively converting state income tax systems from source-based to residency-based?

COST members carefully analyzed various threshold periods and determined the 60-day threshold enhanced and simplified compliance to the greatest extent without any practical overall negative effect on the states. COST believes a 60-day threshold represents a clear balance between legitimate state interest in assuring that employees who earn income in their state pay their fair share and the burdens imposed on employers and employees operating in interstate commerce.

COST further notes that Congress has previously adopted restraints on state taxing authority when it believed that particular state practices were impeding interstate commerce. For example, Congress has enacted legislation limiting state withholding and personal income taxation of nonresident air, rail and motor carrier employees, merchant seamen, water carriers and Members of Congress, all with thresholds greater than 60 days.

Finally, COST is confused by the assertion that the existing state income tax systems are "source-based" rather than "residency-based." In reality, state income tax systems are based on both concepts. Individuals are subject to tax in their resident state on all of their income, regardless of source, barring a federal restraint as discussed above or a voluntary restraint adopted by the resident state. Individuals are also subject to tax by the state in which their income is sourced.

H.R. 3359 does not change these existing systems. Many states with a personal income tax already have a threshold of some kind for nonresidents or a reciprocity agreement with a neighboring state to forego taxes on nonresidents. Consistent with these concepts, H.R. 3359 simply provides for a reasonable, national threshold to facilitate compliance for both employees and employers.

Once again, I sincerely appreciate the opportunity to comment on this pressing issue of national importance. I hope that these responses address the additional questions posed by the Subcommittee on Commercial and Administrative Law regarding H.R. 3359. I would be pleased to submit any further information or analysis the Subcommittee would find helpful on these important issues. If you have any additional questions, please feel free to contact me at (202) 484-5212.

Sincerely,

Douglas L. Lindholm, Esq.

ANSWERS TO POST-HEARING QUESTIONS FROM DEE NELSON, PAYROLL MANAGER, ALUTIIQ, LLC AND SUBSIDIARIES, ANCHORAGE, AK, ON BEHALF OF THE AMERICAN PAYROLL ASSOCIATION

American Payroll Association

Government Relations • Washington, DC

December 31, 2007

Via email

Mr. Adam Russell
Subcommittee on Commercial and Administrative Law
Committee on the Judiciary
U.S. House of Representatives
2138 Rayburn House Office Building
Washington, DC 20515

Re: Questions from Chairwoman Sanchez and Questions for the Record
- **Following Hearing on H.R. 3359, The Mobile Workforce State Income Tax Fairness and Simplification Act of 2007, November 1, 2007**

Dear Mr. Russell,

Please find below my responses to the questions posed to me by Chairwoman Sanchez and the additional questions for the hearing record posed by the Subcommittee on Commercial and Administrative Law, following the November 1, 2007, hearing on H.R. 3359, the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007.

On behalf of the American Payroll Association, I greatly appreciate the opportunity to comment and to provide further information on this pressing issue of national importance. I hope that my responses answer the questions to the satisfaction of Chairwoman Sanchez and her Subcommittee. If you need any further information, please contact Scott Mezistrano, CPP, Senior Manager of Government Relations, American Payroll Association, at 202-232-6888 or smezistrano@americanpayroll.org.

Sincerely,

Dee Nelson, CPP
Payroll Manager
Afognak Native Corp, Alutiiq LLC, and Subsidiaries

Questions from Chairwoman Sanchez and Responses from Dee Nelson, CPP

1. *As someone who sees daily the challenges discussed during the hearing, how will a uniform threshold benefit businesses with employees who perform duties in more than one state? How would a uniform threshold benefit consumers?*

Businesses would benefit a great deal and in many ways by the establishment of a uniform threshold of time to be exceeded before nonresident income tax withholding is required. It will allow businesses to remove many employees from the costly nonresident withholding process and to focus compliance efforts and education on the remaining few. In addition, it will be much easier to comply with a single standard across all the states and localities compared with the patchwork of laws in the 41 states and thousands of localities with income tax withholding.

Employers will be able to avoid the expensive process of withholding taxes and filing Forms W-2 for multiple states in which an employee will spend only a short amount of time. To the extent that a business's employees perform services in a particular state, but no single employee spends enough time in that state to exceed the threshold, the business will never be faced with the costs of registering for a withholding tax account in that state, setting up that state's withholding tables in its payroll system, learning that state's withholding tax laws and regulations (e.g., Which benefits are taxable wages? What are the depositing and filing due dates?), withholding that state's tax, depositing those taxes, filing employment tax returns, or filing Forms W-2 with that state.

Currently, an employer has to perform all the above tasks – many on very short order – the moment any employee begins to perform services in a new state (unless it is one of the few states that has a threshold to be exceeded, a state that has a reciprocal agreement with the employee's state of residence, or a state without an income tax).

In addition, the employer has to learn and apply the rules of the resident state for wages earned by its residents who are earning wages in another state. Some states require simultaneous full withholding of their tax, some require withholding but allow a credit for withholding taken for the worked-in state, and some require withholding only if no withholding is being taken for the worked-in state. These rules would still exist even if a uniform threshold for nonresident withholding were enacted, but for the employee who does not exceed the threshold and is not subjected to the nonresident tax, these rules would all point to withholding the tax of the resident state, so they wouldn't pose a burden to the employer.

After the systemic hurdles are surpassed, the payroll department deals with many questions (and sometimes suffers protestations) from employees who are seeing a new state's tax withheld from their paychecks, sometimes in addition to taxes still being withheld for the state of residence, and has to explain to the employees that they will have to file a personal income tax return for that state.

These tasks add great expense to a business's payroll department budget. A lot of time and resources can be spent on the relative few employees who are doing this sort of business travel compared with the broader employee base. Sometimes, to appease or compensate employees who travel throughout many states for which withholding is taken, an employer will pay for the preparation of all those nonresident income tax returns. Since tax preparation assistance is a taxable benefit, the employer must add the value of it to the employees' wages, and, to save the employees from an additional tax burden, many employers will pay the taxes on that benefit. Some employers will go so far as to reimburse the employee for any extra taxes he or she is paying as a result of working in multiple states (compared with the tax he or she would have paid had the employer not required services to be performed outside the resident state). Such a reimbursement is also a taxable benefit.

In my testimony and in these answers, I tend to focus on the burden of multi-state withholding, but the burden of withholding for local jurisdictions should not be ignored. For example, an employee in Pennsylvania might never leave the state, but if he or she performs on-site consulting work for the employer's clients in different cities throughout the state, the employer must withhold taxes for each of those cities.

The establishment of the uniform threshold will save an employer from the above burden, cost, and drain on human resources for all but the employees that spend significant amounts of time in another state or local jurisdiction.

The consumer, or employee, who does not spend enough time in another jurisdiction to exceed the proposed uniform threshold would also benefit, in terms of expense, cash flow, and filing burden.

Currently, if an employee performs temporary service in another state without a threshold but with a higher tax rate than that of the state of residence, he or she suffers an irretrievable increase in tax expense. Naturally, this is especially true if the employee's home state doesn't have an income tax.

However, even if the two states have a very similar tax structure, the employee can suffer a significant cash flow problem if the resident state requires simultaneous full withholding of its tax (that is, no credit is allowed for the withholding for the worked-in state). When the employee files a personal income tax return with the resident state, a credit will be allowed for the tax liability to the worked-in state, and the employee can get a refund, but that can be well over a year after the tax was originally withheld.

In addition, the employee will have to file a personal income tax return in the nonresident state(s). Each state has its own tax rules, forms, and filing processes. Many employees in these situations hire a tax professional and bear the expense of paying someone to do this for them.

What is especially wasteful in the case of an employee who spends a short amount of time in another state is that he or she will very possibly have earned less than the threshold of income that is even subject to that state's tax. Payroll systems generally apply withholding calculations based on an expectation that, whatever the employee earned in that jurisdiction in the current pay period, the employee will earn that much in that jurisdiction in every other pay period of the year. So, state withholding is taken, even from someone who spends only one week in that state out of the entire year. In such a situation, the employee, of course, has to file a state personal income tax return and will likely get a refund of all of that withholding.

So, because there is no uniform threshold of time to be exceeded before nonresident income tax withholding is required, employers have to withhold tax and report wages, employees must file income tax returns, and, in cases like these, states have to process wage reports and income tax returns of individuals for whom they will refund all taxes withheld. That's a lot of time, effort, and burden with no positive return for the employer, the employee, or the state.

2. *H.R. 3359 allows an employer to rely on an employee's determination of time in a state to determine whether an employee is subject to a withholding requirement and tax liability. H.R. 3359 seems to place the onus on employees and not employers. What is the difficulty in employers keeping track of where their employees work? Do not technology or payroll systems do this already, and if not, why not?*

A number of employers use "time and attendance" systems to track when and where their employees work. These systems are constantly improving, adding more features and ways for employees to "sign in," such as via the Internet or via a phone call from a cell phone. In certain situations, H.R. 3559 establishes an employer's "time and attendance" system (for those employers that have one) as the source of data concerning an employee's whereabouts.

Nevertheless, not all employers utilize such systems and some employers don't use them for all employees, as they can be costly and/or they can be impractical for tracking certain employees. For example, if an employer has a system on which an employee can "sign in" via the Internet, it may not be practical for an employee who travels from state to state repairing equipment at client sites and doesn't always have access to the Internet. The time and location of such an employee's work will probably be determined via the employer's record of the employee's assignments, a summary the employee will periodically submit, or both.

However, no matter how the employer tracks the employee's time and location, without a uniform threshold of time to be exceeded before nonresident income tax withholding is required, the employer is burdened with "getting it exactly right" for a great deal many more employees. A uniform threshold would ease that burden as it relates to the many employees who enter nonresident jurisdictions for short periods of time.

Moreover, the much larger issues for "technology and payroll systems" are system modifications and compliance with another state's rules and deadlines when a new state's withholding is required, as discussed in the answer to question #1. And these issues would be greatly mitigated with the proposed uniform threshold.

Interestingly, there exists a precedent for relying on an employee's declaration of physical presence in a particular jurisdiction. When an employee works outside the U.S., he or she may tell the employer the amount of time that will be spent in another country. The correct amount of time creates eligibility for exemption from federal tax withholding on the wages earned there. This declaration is made by the employee providing the employer with Internal Revenue Service Form 673, *Statement for Claiming Exemption From Withholding on Foreign Earned Income Eligible for the Exclusion(s) Provided by Section 911.*

<u>Questions for the Record and Responses from Dee Nelson, CPP</u>

1. Not only are we living with a more mobile workforce, we are living in with a more technologically savvy workforce. Are there ways for employers to monitor electronically when and where an employee works for the purposes of establishing state tax liability?

When and where an employee works can be tracked with the right software and the right tools. However, these may not be practical for all employers or all employees. For example, we have an online "time and attendance" system, and our employees can sign on via the Internet from wherever they are. However, most of our mobile workforce report to U.S. military installations, and the government, for security purposes, does not always allow our employees to use their Internet connection. These employees record their time and location after regular work hours using their laptops in their hotel rooms, which may be in a different city than the one in which they worked earlier that day. So, it's not exactly the way our system was intended to be used, but we compare their input with our record of their assignments.

As I mentioned in my answer to question #2 from Chairwoman Sanchez, such systems are improving and more employers are using them, but not all employers utilize such systems and some employers don't use them for all employees, as they can be costly and/or they can be impractical for tracking certain employees, such as those who travel without access to the Internet.

Moreover, the much larger issues for nonresident withholding are system modifications, compliance with another state's rules and deadlines, and employee relations, as explained in my answer to question #1 from Chairwoman Sanchez.

2. As a payroll manager, do you get involved in an employee's filing of income tax returns? That is, if an employee has questions about where he owes taxes, do you assist him with that?

I certainly don't offer tax advice or tax preparation services. That would be well beyond my role as my company's payroll manager. Nonetheless, when our employees have questions about their paychecks, including the taxes withheld from those checks and the ramifications of those taxes, they come to me!

My staff and I spend a great deal of time explaining to employees, sometimes over their protests, why we are required to withhold the tax of the state in which they were on temporary assignment, why we are sometimes required to also withhold the tax of their resident state from those same wages, and that they will have personal income tax filing responsibilities in multiple states. We provide them the withholding allowance certificates and tax tables of whichever states they go to, and we point them to the websites of state revenue agencies so they can find forms and instructions for filing those nonresident personal income tax returns.

The time spent on this adds a great deal to my payroll department budget. A lot of time and resources are spent on the relative few employees who are doing this sort of business travel compared with the broader employee base.

So that we can keep these mobile workforce positions filled and complete our company mission, we pay for the professional preparation of all those nonresident income tax returns. Since tax preparation assistance is a taxable benefit, we add the value of it to the employees' wages, and, to save the employees from an additional tax burden, we pay the taxes on that benefit. Some employers will go so far as to reimburse the employee for any extra taxes he or she is paying as a result of working in multiple states (compared with the tax he or she would have paid had the employer not required services to be performed outside the resident state). Such a reimbursement is also a taxable benefit.

3. The FTA advocates a bifurcated approach to this bill. That is, they want to apply a time threshold for the withholding liability of the employers and a time and dollar threshold for the employee liability. Do you think such an approach will simplify the employer's task of ensuring that the proper taxes are paid?

No, I do not. Employers generally place a great value on helping their employees comply with their tax liabilities. If an employee has an income tax liability to a state, he or she will request that the employer withhold that state's tax, and many employers will do that as a courtesy to the employee, even if the employer is not required to do so. And then we'd be back where we started, withholding for more states than would be required under H.R. 3559.

I base the above statement on the fact that many employers already open withholding accounts for states to which they are not responsible but to which they know their employees will owe tax. For example, if an employee lives in California, but works for a company that operates in Oregon and nowhere else, the employee will owe tax to Oregon and California. The employer will be required to withhold only for Oregon. It has no presence in California and is not subject to California's laws. However, knowing that the employee will owe tax to California, may not be likely to make estimated payments, and will be a more productive employee next year if not subject to a state tax levy for unpaid taxes, the employer will set up a California withholding account, withhold and deposit tax, and file the necessary employment tax returns.

H.R. 3559 would limit, on an equal basis, the states to which an employee owes tax and the states for which the employer must withhold tax.

While the following may not have an impact on an employer's tasks, I submit that decoupling the employee and employer responsibilities would, at best, add burden to individuals who must deposit tax on their own because it is not required to be withheld by the employer and their employer won't establish courtesy withholding, and it would, at worst, result in individuals who owe tax and fail to file returns that would only confirm that in the eyes of the state.

4. Can you quantify the dollar cost to your company to comply with the myriad taxing regimes that you encounter?

The cost to our company can vary from year to year, depending on the number of employees we have in our mobile workforce. For tax year 2006, it cost our company approximately $50,000 for tax preparation assistance provided to employees and approximately $60,000 in salary for time spent by payroll and human resource staff for the special handling of our mobile workforce. This totaled $110,000 for the management of only 250 of our 5,000 employees. I foresee the cost for 2007 to be the same.

We're by no means the largest company out there. Many of my colleagues in the American Payroll Association work for larger companies with greater numbers of traveling employees and have told me that they spend much more than my company does.

5. The legislation as written kicks in when the bright line 60-day threshold is met. What would the reporting, withholding and overall compliance burden be if the 60-day threshold straddles a filing quarter or occurs at the end of a taxable year? Do you believe a prospective instead of a retroactive application is more practical and less burdensome?

A prospective application would certainly be less burdensome for employers, but, of course, that's not what H.R. 3559 proposes, and that may not be appropriate in certain circumstances in terms of its impact on states' revenues.

Any threshold carries with it some issue of "predicting" whether an employee is going to exceed it, so as to know whether or not to withhold the nonresident-state tax from the first day of work. It is true that if one predicts incorrectly, and then the 60-day threshold is hit with just a few days remaining in the year, it will be difficult to withhold the necessary amount of tax in the remaining time. However, that issue exists already in the states that have thresholds.

However, a standardized 60-day threshold across all 41 states and the thousands of localities with income tax withholding would greatly reduce the number of employees for whom any prediction would need to be considered and would greatly reduce the number of employees who would ever trigger nonresident withholding. Employers would be able to concentrate their compliance and education efforts on the fewer, and much more obvious, employees who have extended assignments in nonresident states. With the proposed 60-work-days threshold (which is longer than the existing threshold in the relatively few states that apply one), there will be many fewer employees whose sporadic trips to a state surprisingly exceed the threshold toward the end of the year.

A single standard across all the states and localities that is federally established and well publicized would be significantly easier to apply for employers and employees across the nation, and employers' systems (payroll and time/attendance) are more likely to be able to support it, thereby increasing compliance.

ANSWERS TO POST-HEARING QUESTIONS FROM HARLEY DUNCAN, EXECUTIVE DIRECTOR, FEDERATION OF TAX ADMINISTRATORS, WASHINGTON, DC

Questions for the Record
H.R. 3359 – Mobile Workforce State Income Tax Fairness and Simplification Act
Submitted by Harley Duncan, Federation of Tax Adminitrators
December 21, 2007

Questions from Chairwoman Sanchez for Harley Duncan

1. Please explain what effect a 60-day uniform threshold would have on state and local revenues. What effect would a 20-day uniform threshold have? Where is the balance of interests of states and local governments' concern about loss of revenues and the elimination of some of the complexities in not having a national uniform standard?

The effects of any particular threshold are difficult to quantify because all of the information necessary to the analysis is not readily available for each state. Ernst and Young (E&Y), however, did a preliminary analysis of the impact of a 60-day threshold for each of the states based on information from several states as well as some national information. That review showed that in the aggregate, state revenues would be reduced by about $100 million nationally. It also showed that some states are more heavily affected than others because of the nature of their economies and their current laws. In particular, the E&Y work projects a net reduction of over $100 million for New York State alone. Work by the New York State Tax Department believes this figure could be underestimated by as much as 50 percent. Work on a 20-day threshold has not been done on a national basis, but preliminary work in New York suggests that the loss under a 20-day rule would be one-fourth as much as the 60-day rule.

The question of balance is both critical and difficult. The appropriate answer may, in fact, vary from state-to-state. That is, in part, why we suggested in our testimony that there be a dollar component to the threshold as well as a days component. The dollar component reduces the exposure of state revenue systems by providing a back-stop to the days threshold. With a dollar threshold structured as outlined in our testimony, we believe the days threshold for determining when a withholding liability exists could be relatively higher (than in a system in which there is no dollar component), thus insuring significant reductions in the burden facing employers.

2. Are the exemptions of professional athlete, professional entertainer and certain public figures as defined in H.R. 3359 sufficiently narrow? If not, why not?

We believe the definitions of professional athlete and entertainer are sufficient. As to the public figures, we believe consideration should be given to simply providing that individuals paid on a "per event" basis are not subject to the act instead of trying to discern who may be a public figure and who is not.

3. Which states and local governments would be most affected, both positively and negatively by H.R. 3359?

As noted, the E&Y analysis indicates that New York State is the most negatively affected state. New Jersey ($57 million) and Connecticut ($9 million) are the most positively affected states. While an analysis at the local level has not been done, I would expect that Philadelphia would be among the most affected. The city levies a wage tax of 3 percent on all persons (resident and nonresident) working in the city.

4. In his prepared testimony, Mr. Douglas Lindholm asks the question: "Can the states resolve these issues without a federal rule?" and answers that it is unlikely. Can the states address these concerns effectively and promptly?

Our policy statement that was submitted with my written testimony outlines a number of questions that we use to evaluate whether a federal preemption of state authority should be considered as appropriate. Among those is whether states can address the question being considered on their own through cooperative action or otherwise. While it is conceivable that all income tax states could agree to and enact a uniform threshold for withholding and liability of nonresidents, we would agree that such a process would take considerable time and probably still result in some differences among states. We are prepared to agree that this is one area that a federal rule probably makes the most sense and is certainly the most expeditious manner of addressing the issue.

Other Questions

1. Two states, Arizona and Hawaii, have a 60-day threshold for withholding income from an employee's paycheck if that employee is a resident of another state. Why, then, do you insist that 60 days is too long for the purposes of H.R. 3359?

Two points are important here. First, the threshold in Hawaii and Arizona applies only to a withholding obligation and not the ultimate obligation of the employee for a tax liability because of work performed in the state. If H.R. 3359 dealt only with withholding, we would likely consider a higher threshold than we are inclined to do when the actual liability of the individual is at issue. Second, the nature of the economy and geography in these states may be such that they do not have significant amounts of workers in the state temporarily and thus may not be greatly affected by a 60-day rule. The beauty of our federal system is that they are free to set the threshold where they believe it makes sense for them.

2. In your written testimony, you advocate for the addition of a dollar threshold in determining an employee's personal tax liability, but not for an employer's withholding liability. Why the difference? Why should the employee have to track the dollar amount he or she earns in a particular jurisdiction, when the employer does not?

In formulating our proposal, we were trying, in part, to respond to concerns from the employer community that they do not have the ability to track dollars on a contemporaneous basis. Thus, we used only a days threshold to remove significant parts of the employer burden. We used the dollar threshold to reduce the exposure of state tax systems to substantial revenue shifts. In our view, the employer would essentially be making an end-of-the-year calculation based on total income attributable to a state, rather than tracking on a regular basis. Depending on where the thresholds are set, the dollar threshold could be set so that it affected relatively few employees, but it would still provide protection to the states. The situation facing an employee would not be dissimilar from that facing them at the present time when they have income from sources that are not subject to withholding or an employer does not withhold properly.

3. As part of his testimony, Mr. Lindholm included a preliminary estimate of the impact of the bill on state treasuries. In all but two cases, the impact on a state's budget was less than $15 million, which sounds like a lot of money to me, but is, in reality, an almost vanishingly small amount of a state's total tax revenue. In fact, according to Mr. Lindholm's figures, the most impact that this bill will have on any state's revenue – either positively or negatively – is less than a quarter of one percent. Do you context these numbers?

States are currently evaluating the estimates presented by Mr. Lindholm. Some have found the estimates to be reasonable for their state. New York, however, believes the impact in that state could be understated by as much as 50 percent because the analysis did not have access to a file that contained audit adjustments and taxpayers may alter their behavior to avoid New York tax under the bill.

4. If a 60-day threshold is too long for FTA, what would you consider to be a reasonable threshold? What dollar threshold would you say is reasonable under FTA's preferred approach to this bill?

We are currently working with the states to develop the appropriate response to these issues.

Harley Duncan
Federation of Tax Administrators
December 21, 2007

ANSWERS TO POST-HEARING QUESTIONS FROM WALTER HELLERSTEIN, FRANCIS SHACKELFORD DISTINGUISHED PROFESSOR OF TAXATION LAW, UNIVERSITY OF GEORGIA SCHOOL OF LAW, ATHENS, GA

1785
The University of Georgia
School of Law

November 29, 2007

By email to Adam.Russell@mail.house.gov

Mr. Adam Russell
Subcommittee on Commercial and Administrative Law
Committee on the Judiciary
U.S. House of Representatives
2138 Rayburn House Office Building
Washington, DC 20515-6216

Re: Hearing on H.R. 3359, the "Mobile Workforce State Income Tax Fairness and Simplification Act of 2007"

Dear Mr. Russell:

In response to Chairwoman Sanchez's letter of November 20, 2007, I have attached hereto my transcript edits correcting errors in transcription. In addition, I have set forth below my responses to the additional questions that Chairwoman Sanchez forwarded to me to supplement the testimony I provided at the hearing on November 1, 2007.

Questions from Chairwoman Sanchez and Responses

1. Is there any evidence that the administrative burden and complexity posed by the current state and local practices and as described by Mr. Douglas Lindholm and Ms. Dee Nelson do impede commerce?

   The question you raise is an empirical one, namely, whether the costs of complying with current state and local income tax laws, and corresponding employer withholding obligations, impede commerce. I have not conducted such empirical research nor am I aware of empirical studies that provide evidence as to whether such costs impede commerce. Nevertheless, as a matter of elementary economic analysis, increasing the cost of carrying on an activity will normally lead to less of that activity being carried on, all other things being equal. Accordingly, the compliance costs that current state and local government practices (as described by Mr. Douglas Lindholm and Ms. Dee Nelson) impose on businesses whose employees cross state lines to engage in interstate commerce almost certainly impede the amount of commerce being carried on as compared to the amount of commerce that would be carried on if such costs were materially reduced.

2. Concerns have been stated about the federal intrusion on state taxing authority by this bill, H.R. 3359. With your expertise in federal constitutional restraints on state taxation of interstate commerce, what is the likelihood that all of the states which impose individual income taxes can address the concerns discussed during the hearing through their own actions? Or is this when the federal government should step in?

   In my judgment, the likelihood that all of the states that impose individual income taxes can address the concerns discussed during the hearing through their own actions is extremely remote, at least when viewed in light of the historical record of states with income taxes voluntarily agreeing to uniform state income tax laws, *and, more importantly, maintaining that uniformity over time*. As I indicated in my testimony, I believe that a targeted response to the problem addressed by H.R. 3359 is an appropriate exercise of congressional power, although, as I also indicated, there may well be room for additional fine-tuning of the statute to assure that the right balance is struck between the states' legitimate interest in raising revenue and the nation's interest in preserving our national common market.

3. You state in your prepared testimony that you believe that the states have a legitimate interest in assuring that workers who earn income in the state pay their fair share. Would this legislation approach the slippery slope of further federal intrusion into states' interests?

   As my testimony indicates, Congress for many years has adopted targeted restraints on state taxing authority when it believed that particular state practices were contrary to the national interest. In my view, H.R. 3359 falls comfortably within this limited type of restraint and would not "approach the slippery slope of further federal intrusion into states' interests." Moreover, the slope is not inherently slippery; it is only as slippery as Congress, in its wisdom, allows it to be.

Questions for the Record

1. You give three examples of laws that are analogous to H.R. 3359. Have any of the statutes that you mentioned, those dealing with railroad employees, motor carrier employees, or merchant mariner employees, ever been challenged as violations of the Commerce Clause? Based on your other testimony, I take it that you think that those laws – and this one – could stand up to such a challenge, correct?

To the best of my knowledge (based on a Westlaw search), none of the three statutes identified in the question has ever been challenged as a violation of the Commerce Clause. It is an accurate characterization of my testimony and my opinion "that those laws – and this one – could stand up to such a challenge."

2. One of the concerns that the FTA has raised is the length of the 60 day threshold in determining the employer's withholding liability. How do the other statutes that you cited as somewhat analogous to this situation deal with this problem. Are they absolute bars on the non-resident state's imposition of taxes on railroad employees, etc.?

   The statutes I cited do not rely on a days-in-state threshold after which the prohibition on income tax withholding or tax liability ceases to apply. Instead, they generally provide for an absolute bar on withholding or taxation of the specified nonresident employees' compensation. Specifically, the bar on state withholding and taxation of specified nonresident rail and motor carrier employees' compensation is absolute. 49 U.S.C. §§ 11502, 14503. The bar on state taxation of specified nonresident merchant seamen's wages is absolute. 46 U.S.C. § 11108 (b). The bar on state withholding of specified merchant seamen's wages is absolute (with a limited exception for a voluntary agreement between the seamen and the employer to withhold). 46 U.S.C. § 11108 (a). In addition, certain water carriers must file income tax information and other reports with the water carrier employee's state of residence and the state in which the employee earned more than 50 percent of his or her pay from the water carrier during the preceding year. 49 U.S.C. § 14503(b)(2).

3. How do the myriad of reciprocal agreements that exist between neighboring states regarding the withholding of income from residents of those states affect your analysis about (a) the constitutionality of H.R. 3359 and (b) the need for legislation to address the problems identified by the bill.

   (a) The existence of reciprocal agreements between neighboring states regarding the withholding of income from residents of those states has no effect on my analysis of the constitutionality of H.R. 3359. What the states do voluntarily does not affect Congress's Commerce Clause power to restrain state taxation.

   (b) The existence of reciprocal agreements between neighboring states regarding the withholding of income from residents of those states – at least in their present form – reinforces my view that congressional legislation is appropriate. In a sense, it is a recognition by the states – an "admission against interest," if you will – that the problem of withholding for cross-border employment is a real one that needs to be addressed. The problem is that the states have addressed it in only a piecemeal fashion, thus underscoring the need for a uniform national solution that

Congress alone can provide. My answer to this question would have been different if all states with personal income taxes had entered into a uniform, nationwide reciprocity arrangement that in essence accomplished through voluntary action what HR. 3359 is seeking to achieve through congressional action.

I hope this responds to the Chairwoman's and Subcommittee's questions. Please let me know if you have any additional questions or if I can be of any further assistance.

Sincerely,

Walter Hellerstein

Walter Hellerstein
Shackelford Professor of Taxation

PREPARED STATEMENT OF THE AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

The American Institute of Certified Public Accountants (AICPA) appreciates the opportunity to submit this statement for the record to the Committee on the Judiciary, Subcommittee on Commercial and Administrative Law for the hearing on H.R. 3359, the "Mobile Workforce State Income Tax Fairness and Simplification Act of 2007."

The AICPA is the national, professional association of CPAs, with more than 350,000 members, including CPAs in business and industry, public practice, government, and education; student affiliates; and international associates. It sets ethical standards for the profession and U.S. auditing standards for audits of private companies; federal, state and local governments; and non-profit organizations. It also develops and grades the Uniform CPA Examination.

Approximately 42% of our membership is made up of members in public practice. Of our members in public practice, approximately 75% are in firms of 10 people or less. This numbers 46,500 firms.

The AICPA supports H.R. 3359, the Mobile Workforce State Income Tax Fairness Act of 2007. Businesses, including small businesses and family businesses that operate interstate, are subject to a significant regulatory burden with regard to compliance with nonresident state income tax withholding laws. These burdens translate into an administrative burden on these entities that takes resources from operating their business. Also, the cost must be passed on to the entity's customers and clients. Having a uniform national standard for state nonresident income tax withholding would significantly ameliorate these burdens. And concomitant with this is the need for a de minimis exemption from the multi-state assessment of state nonresident income tax.

Accounting firms, including small firms, do a great deal of business across state lines. Many clients have facilities in nearby states that require an on-site inspection during the conduct of an audit. Additionally, consulting, tax or other non audit services that CPAs deliver may be provided to clients in other states, or to facilities of local clients that are located in other states. Many small business clients of CPAs also have multi-state activities. All of these small businesses, accounting firms and their clients are affected by nonresident income tax withholding laws.

There are 41 states that impose a personal income tax on wages and partnership income, and there are many differing tax requirements regarding the withholding for income tax of nonresidents among those 41 states. A number of states have a de minimis threshold, or exemption for nonresidents working in the state before taxes must be withheld and paid. Others have a de minimis exemption based on the amount of the wages earned, either in dollars or as a percent of total income, while in the state. The rest of the states that impose personal income taxes on nonresident income earned in the state require only a work appearance in the state. Further complicating the issue is that a number of these states have reciprocity agreements with other, usually adjoining, states that specify that they will not require state income tax withholding for residents of the other states that have signed the reciprocity pact.

It is not difficult to understand that the recordkeeping, especially if business travel to multiple states occurs, can be voluminous. And the recordkeeping and withholding a state requires can be for as little as one day's work in another state. Additionally, the amount of research that goes into determining what each state law requires is expensive and time consuming, especially for a small firm or small business that does not have a great amount of resources. A small firm or business will often be required to engage outside counsel to research the laws of the other states. And this research needs to be updated yearly to make sure that the state law has not changed. Having a uniform national standard would eliminate the burden of having to research state law for each state where work is performed.

In addition to uniformity, there needs to be a de minimis exemption. AICPA believes that the 60 day limit contained in H.R. 3359 is fair and workable. The economic changes that have occurred as our country has gone from local economies to a national economy are huge. Where businesses once tended to be local, they now have a national reach. This has caused the operations of even small businesses to move to an interstate basis. Because of the interstate operations of these companies, many providers of services to these companies, such as CPAs, find that they are also operating, to some extent, on an interstate basis. And with the ease of communication through the internet, and the ease of travel, the ability to provide some services far from home is not an issue, as it once was. What once were local taxation issues have now become national in scope, and burdens must be eased in order to promote this interstate commerce and insure it runs efficiently.

Many smaller firms and businesses use third party payroll services instead of performing that function in house. A number of third party payroll service providers are unable to handle multi-state reporting. They often limit, for example, reporting to two states, the state of residence and the state of employment. Additionally, third party payroll service providers generally report on a pay period basis (e.g., twice per month, bi-weekly, etc.) as opposed to daily, which can be a necessity when interstate work is performed. These reporting issues require employers to track and manually adjust the reporting and withholding to comply with various state requirements. The alternative is to pay for a much more expensive payroll service. H.R. 3359 would provide significant relief from these burdens.

The 60 day limit in the bill ensures that the interstate work for which an exemption from withholding is granted does not become a means of avoiding being taxed or shifting income tax liability to a state with a lower rate. Instead, it insures that the primary place(s) of business for an employee are where that employee pays state income taxes.

There is one amendment to the bill that the AICPA would recommend. Once the 60 day threshold is reached, the employee should pay withholding and state income taxes in the host state for all wages earned going forward. The withholding should not be made retroactive for the first 60 days. To do so would be unfair to the employee. If the reach is retroactive, then on the 61st day of working in the other state, the employee would owe withholding to that state for the 60 day period. This could be a substantial amount, which could even cause the employee to immediately be in an underpayment penalty situation. It would be unfair to require the employee to pay this much money, especially where the employee is a resident of one of the other 40 states that imposes a state income tax. In that situation, the employee would have double paid withholding and would not receive a refund from the home state until tax returns are filed and refunds paid. Even should a state allow for current withholding and filing in the open payroll period, this could cause cash flow challenges for employees should they find themselves in a high tax rate jurisdiction.

The AICPA appreciates the opportunity to submit this statement in support of H.R. 3359.

PREPARED STATEMENT OF EDWARD A. ZELINSKY, MORRIS AND ANNIE TRACHMAN PROFESSOR OF LAW,[1] BENJAMIN N. CARDOZO SCHOOL OF LAW, YESHIVA UNIVERSITY

I strongly support H.R. 3359, the Mobile Workforce State Income Tax Fairness and Simplification Act of 2007. H.R. 3359 is a useful, indeed a long overdue, effort by Congress, using its authority under the Commerce Clause, to begin to rationalize the states' income taxation of nonresidents. The core concept of H.R. 3359 is compelling: In any calendar year, a state may tax the income of a nonresident employee only if such employee is "physically present performing duties" in the taxing state "for more than 60 days."[2]

However, H.R. 3359 in its current form is not enough and may unintentionally prove counterproductive. To be fully effective, H.R. 3359 must be conjoined with H.R. 1360, the Telecommuter Tax Fairness Act of 2007. H.R. 3359 lacks any definition of physical presence and fails to forbid states from adopting doctrines like New York's "convenience of the employer" rule, doctrines which pretend that taxpayers are present in-state when in fact they are not.

Consequently, H.R. 3359, if enacted into law without H.R. 1360 and its definition of physical presence, will likely be flouted by New York, deploying its employer convenience doctrine to push nonresident taxpayers over H.R. 3359's sixty (60) day minimum by treating out-of-state work days as days spent in New York. Moreover, H.R. 3359, if adopted without the safeguards of H.R. 1360, may encourage other states to emulate New York's employer convenience doctrine and thereby eviscerate the requirement that nonresident employees be physically present in the taxing state.

[1] For purposes of identification only. This statement expresses my personal views, not the views of any institution or group with which I am affiliated, professionally or otherwise.

[2] H.R. 3359, Section 2(a)(2).

BACKGROUND

In 2005, I was privileged to testify before this subcommittee on the subject of nonresident income taxation and New York's employer convenience doctrine.[3] I am something of a poster boy on this subject, having been the unsuccessful litigant in *Zelinsky v. Tax Appeals Tribunal.*[4] In that case, New York took its standard position that the days I worked at my home in New Haven, Connecticut were, for tax purposes, to be deemed days I was present in New York, even though I was not. At its most basic, New York's notion of employer convenience decimates the concept of physical presence by treating nonresident employees, particularly those who work at home, as being in New York even when they are not.

New York's practices in this respect have been widely and correctly condemned as unsound as a matter of policy and unconstitutional as a matter of law.[5] Most recently, three dissenting judges of New York's highest court condemned in the strongest terms New York's use of the employer convenience doctrine to impose New York's nonresident income taxes on Mr. Thomas Huckaby for working at his home in Nashville, Tennessee by pretending that, on those Tennessee days, Mr. Huckaby was in New York.[6]

Nevertheless, the New York Department of Taxation and Finance, supported by a majority of New York's highest court, persists in pretending that, for income tax purposes, nonresidents are present in New York on days when they are not. New York will not let logic stand in the way of revenue—particularly when the payors of that revenue are nonvoting nonresidents.

DEFINING PHYSICAL PRESENCE

Consider against this background the definition of "day" embodied in H.R. 3359. Under that definition, a nonresident employee is deemed to have performed a day of services in the taxing state only "if the employee performs more than 50 percent of the employee's employment duties in such State or locality for such day."[7] This is a reasonable definition,[8] perfectly appropriate for a sensible world.

But, in this context, we do not live in a sensible world. If the past is any indication (and I think it is), New York will respond to H.R. 3359 and its current definition of "day" by flouting that definition, declaring that a nonresident employee, under the employer convenience doctrine, is deemed to perform services in New York on days when such employee works at his out-of-state home or at any other out-of-state location which New York characterizes as having been chosen for the employee's convenience. New York will thereby propel nonresidents over the sixty day in-state minimum of H.R. 3359 by declaring (as New York does now) that out-of-state days should be treated for tax purposes as days spent in New York.

When a nonresident employee seeks to enforce H.R. 3359 against this illogical approach, he will be required by federal law to challenge New York's taxes in New York's courts.[9] And, as we saw in my case and in Mr. Huckaby's case, New York's courts, despite all of the U.S. Supreme Court case law to the contrary, uphold the New York tax commissioner when he declares, under the rubric of employer convenience, that employees who aren't in New York should be treated for tax purposes as though they are. Nothing in the current language of H.R. 3359 will compel New York's courts or its tax commissioner to reach a different conclusion. It is thus likely that New York, continuing current practice, will annually declare nonresidents to be in New York more than sixty (60) days based on work these nonresidents perform at their out-of-state homes and other out-of-state locations.

[3] A joint hearing of this subcommittee and the Subcomittee on the Constitution was held on May 24, 2005. My testimony is on page 32 of the printed transcript of this May 24, 2005 hearing (Serial No. 109–27) and at 36 STATE TAX NOTES 713 (2005), 2005 STT 101–2.

[4] 1 N.Y.3d 85 (2003), cert. denied 541 U.S. 1009 (2004).

[5] *See, e.g.,* Nicole Belson Goluboff, *New York Makes It Official: Double Taxing of Telecommuters Will Continue,* 40 STATE TAX NOTES 877 (2006); Walter Hellerstein, 1 STATE TAXATION (3rd ed. 2007)at para. 20.05[4][e][i] (the *Zelinsky* decision "does not withstand analysis"); William V. Vetter, *New York's Convenience of the Employer Rule Conveniently Collects Cash From Nonresidents, Part 1,* 42 STATE TAX NOTES 173 (2006); William V. Vetter, *New York's Convenience of the Employer Rule Conveniently Collects Cash From Nonresidents, Part 2,* 42 STATE TAX NOTES 229 (2006).

[6] 4 N.Y.3d 427, 440 (2005), cert. denied 126 S.Ct. 546 (2005).

[7] H.R. 3359, Section 2(d)(1).

[8] Though not an ideal definition, as it leaves unclear the metric for measuring whether the "more than 50 percent" test is satisfied. Is this a test of time spent on the job during the day in question? Or of the value of the employee's services? Or the relative importance of the tasks the employee performs during the day? H.R. 3359 does not say.

[9] Tax Injunction Act, 28 U.S.C. Section 1341.

Perhaps some hardy soul will emulate Mr. Huckaby and me and will fight New York's irrationality through the New York courts. Perhaps that intrepid taxpayer will also achieve what Mr. Huckaby and I could not, namely, U.S. Supreme Court review of New York's employer convenience fiction.

It would, however, be better to deal with this problem now as does H.R. 1360. H.R. 1360 addresses this problem with such clarity that even New York's courts and tax department will be compelled to acknowledge the inconvenient truth that a physical day outside New York is a physical day outside New York.

Specifically, H.R. 1360 does three important things. First, it forbids a state for any income tax purpose from deeming a taxpayer to be physically present in the state when he is not.[10] Second, H.R. 1360 specifically forbids "any convenience of the employer test or any similar test" which could otherwise eviscerate the physical presence requirement.[11] Third, H.R. 1360 precludes a variety of interpretive techniques which New York and its courts have used to avoid the obvious reality that, when nonresident taxpayers work at their out-of-state homes, they are not working in New York.[12]

Thus, together, H.R. 3359 and H.R. 1360 can help achieve the goal of rational income taxation of nonresidents.

POTENTIAL COUNTERPRODUCTIVE EFFECTS

My concern is not just that H.R. 3359 could prove ineffective because it lacks a strong definition of physical presence. I also fear that H.R. 3359, adopted without H.R. 1360, will inadvertently prove counterproductive and will cause other states to emulate New York and its employer convenience doctrine. If New York is able to avoid the more than sixty (60) day rule of H.R. 3359 by pretending that nonresidents work in state on days when they do not, other states will be tempted to take the same course to continue taxing nonresidents.

The U.S. Supreme Court's refusal to hear either my case or Mr. Huckaby's case, in practical terms, gives a green light to other states desiring to raise income tax revenue by pretending that nonvoting, nonresidents work in-state on days when they do not. If New York's courts are prepared to countenance this behavior, why should not other states' courts similarly condone such behavior as well?

Among the reasons why no other state has so far followed New York's aggressive lead in taxing nonresidents on days when they work out-of-state is that the states are watching Congress to see if it will legislate in this area. If H.R. 3359 is enacted unaccompanied by H.R. 1360, at least some tax commissioners will inform their respective governors and legislators that there is a way around H.R. 3359 and its more than sixty (60) day rule: adopt New York's employer convenience doctrine to declare that out-of-state days shall be deemed in-state days to get nonresidents above the sixty day minimum. Some revenue-starved officials will undoubtedly approve of this approach. If so, H.R. 3359 will have accidentally spread the irrationality of New York's employer convenience doctrine throughout the nation.

This scenario is avoidable by coupling H.R. 3359 with H.R. 1360 which forbids the adoption of the employer convenience doctrine and similar tests for taxing nonresidents on days they are outside the taxing state.

CONCLUSION

H.R. 3359 and its more than sixty (60) day rule represent a commendable effort to begin to rationalize the states' income taxation of nonresidents. However, H.R. 3359 in its current form is not enough and may unintentionally prove counterproductive. To be fully effective, H.R. 3359 must be conjoined with H.R. 1360 which would forbid states from adopting doctrines like New York's "convenience of the employer" rule, doctrines which pretend that taxpayers are present in-state when in fact they are not. Together, these two pieces of legislation would make more sensible our system of nonresident income taxation.

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[10] H.R. 1360, Section 2(a), adding to title 4 of the United States Code section 127(a).
[11] H.R. 1360, Section 2(a), adding to title 4 of the United States Code section 127(b).
[12] H.R. 1360, Section 2(a), adding to title 4 of the United States Code section 127(c).

PREPARED STATEMENT OF NICOLE BELSON GOLUBOFF, ESQUIRE

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Statement of Nicole Belson Goluboff, Esq.

Submitted to the House Committee on the Judiciary

Subcommittee on Commercial and Administrative Law

Hearing on

H.R. 3359, the "Mobile Workforce State Income Tax Fairness and Simplification Act of 2007"

November 1, 2007

I am Nicole Belson Goluboff, a lawyer and advocate for telecommuting, or "telework." My work involves extensive writing on the legal consequences of telework. I am the author of *The Law of Telecommuting* (ALI-ABA 2001 with 2004 Supplement) and *Telecommuting for Lawyers* (ABA 1998). I serve on the Advisory Board of the Telework Coalition (TelCoa), an organization that promotes telework though research, education, technology and legislation.

I thank the House Judiciary Committee Subcommittee on Commercial and Administrative Law for the opportunity to offer this written statement concerning H.R. 3359, the "Mobile Workforce State Income Tax Fairness and Simplification Act of 2007." This statement includes only my own views and not the views of any group with which I work.

I make this statement to urge the Subcommittee to advance H.R. 3359 together with H.R. 1360, the "Telecommuter Tax Fairness Act of 2007." I also urge that, in the event the Subcommittee determines that it will not approve H.R. 3359, it should nonetheless approve H.R. 1360.

I. H.R. 3359 and H.R. 1360 Address Related Problems

H.R. 3359 would prohibit a state from taxing the income earned by a nonresident employee unless the nonresident was "physically present performing duties" in that state for more than 60 days during the tax year.[1] The bill is designed to protect employees who work in multiple states from inconsistent state tax obligations and to protect their employers from unduly burdensome withholding obligations. The employee population the bill covers includes, among others, interstate telecommuters - people who are employed by organizations outside their states of residence and who perform some of their job responsibilities from home.

H.R. 1360 would prohibit a state from taxing the income earned by a nonresident employee for any period when he is "physically present in another State."[2] Like H.R. 3359, H.R. 1360 protects multi-state employees from inconsistent state tax requirements and protects their employers from onerous payroll obligations.

H.R. 1360 was introduced specifically to remedy the ill effects of a New York State tax doctrine known as the "convenience of the employer" rule[3] - a rule that unfairly penalizes interstate telecommuters.

1 H.R. 3359, Section (2)(a)(2).

2 H.R. 1360, Section 2(a), adding section 127(a) to chapter 4 of title 4 of the United States Code.

3 20 NYCRR §132.18(a)("If a nonresident employee … performs services for his employer both within and without New York State, his income derived from

Under the convenience of the employer rule, if a nonresident has a New York employer and works partly within New York and partly from his out-of-state home, New York may force him to treat the days he works at home as if they are days he works in New York and to pay New York tax on the income he earns on those days. However, the telecommuter's state of residence may (much more logically) treat the days the telecommuter works at home as home state days, rather than New York days, and it may also tax the income earned on those days.[4] Because the employee's telework days may be treated inconsistently by the two states, the employee is threatened with double taxation.

H.R. 1360 would eliminate the double tax risk by prohibiting New York - and any other state - from applying a convenience of the employer rule.[5] It would clarify that days worked at home are allocable to, and taxable by, the home state - not the employer's state. Thus, it would ease the confusion multi-state telecommuters currently face concerning where they

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New York State sources includes that proportion of his total compensation for services rendered as an employee which the total number of working days employed within New York State bears to the total number of working days employed both within and without New York State.... However, any allowance claimed for days worked outside New York State must be based upon the performance of services which of necessity, as distinguished from convenience, obligate the employee to out-of-state duties in the service of his employer").

[4] *See, e.g.,* Edward A. Zelinsky, "Employer Convenience, Telecommuting, and the Constitution: The Empire State Really Strikes Back," *State Tax Notes,* May 8, 2006, p. 451.

[5] H.R. 1360, Section 2(a), adding Sec. 127(b) to chapter 4 of title 4 of the United States Code.

owe taxes on the income they earn on their telework days, as well as the confusion employers face about where they have to withhold.

II. H.R. 1360 Is Necessary for H.R. 3359 To Achieve Its Goals

A. Without H.R. 1360, the "More Than 60 Days" Rule in H.R. 3359 Could Be Effectively Ignored

Both H.R. 3359 and H.R. 1360 make a nonresident's physical presence in a state a prerequisite to taxation there. However, H.R. 1360 includes a critical feature that H.R. 3359 lacks: It stresses the rigor of the physical presence requirement. Under H.R. 1360, New York would no longer be able to force a nonresident to pretend that a day when he was physically present in his home state was a day he was present in New York.

H.R. 3359 has no similar provision to assure that New York will truly honor the requirement that a nonresident be physically present for more than 60 days. If H.R. 3359 were enacted without H.R. 1360, New York could well insist that, when a nonresident calculates whether he was physically present in New York for more than 60 days during the year, he must count the days he chose to work in his home state as New York days. Other states looking to avoid the "more than 60 days" rule - and to exact as much revenue as possible from nonresidents with no vote - could do the same.[6]

As the Subcommittee considers H.R. 3359, it should not leave the "more than 60 days" requirement in that bill so vulnerable to disregard. Rather, it should make sure that multi-state workers have the protection against abuse H.R. 1360 provides - a clear message that physical presence truly means physical presence.

B. Without H.R. 1360, H.R. 3359 Could Worsen the Current Confusion

Even if H.R. 3359 were amended to make entirely clear that states like New York could not circumvent the "more than 60 days" rule by treating out-of-state days as if they were in-state days (or even if the current version of H.R. 3359 were construed to make this point clear already), enacting H.R. 1360 would still be necessary. Without H.R. 1360, H.R. 3359 could aggravate the very confusion it is intended to redress.

[6] The refusal of the U.S. Supreme Court in two recent cases to hear constitutional challenges to New York's convenience of the employer rule has left the door open for other states to adopt a similar rule and to begin treating nonresidents' out-of-state days as in-state days for tax purposes. *Huckaby v. New York State Division of Tax Apeals*, 4 N.Y.3d 427 (2005), *cert. denied*, 546 U.S. 976 (2005); *Zelinsky v. Tax Appeals Tribunal of New York*, 1 N.Y.3d 85 (2003), *cert. denied*, 541 U.S. 1009 (2004). While both H.R. 3359 and H.R. 1360 are before it, this Subcommittee has an important opportunity to stem the growth of this illogical and unfair policy.

Consider the case of a Connecticut resident who is employed by a company in Manhattan and who sometimes works from home. Under H.R. 3359, this telecommuter would, when figuring whether he had worked in New York for more than 60 days, count the days he worked at home as Connecticut days and count the days he worked in New York as New York days.

If the telecommuter did in fact spend more than 60 days working in New York - and, if H.R. 1360 were not also enacted - the telecommuter would then have to apply the convenience of the employer rule to determine his actual tax liability. Under the convenience rule, he would have to treat the very same at-home days he just counted as Connecticut days, as New York days. This fluctuating characterization of his telework days would breed tremendous confusion and compliance problems.

However, if H.R. 1360 and H.R. 3359 were enacted together, H.R. 3359 could much more effectively meet its goal to make the tax requirements for multi-state workers simpler and fairer. The telecommuter in my example would be able to treat his telework days as Connecticut days both for purposes of determining whether he was taxable in New York and, if he were taxable, for purposes of determining his specific tax liability.[7]

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[7] *See also* Nicole Belson Goluboff, "Congestion Pricing and the Convenience of the Employer Rule," *State Tax Notes*, Oct. 15, 2007, p. 181;

In sum, the two bills should be approved together because enacting H.R. 3359 without also enacting H.R. 1360 could (1) cause New York and other states to ignore the "more than 60 days" rule in H.R. 3359; and (2) exacerbate the current confusion by forcing telecommuters to determine their tax liability based on a slippery characterization of at-home days.

III. H.R. 1360 Should Be Approved Even If H.R. 3359 Is Not

Even if the Subcommittee decides not to advance H.R. 3359, it should still move H.R. 1360 forward. As I noted earlier,[8] H.R. 1360 is necessary to eliminate the confusion interstate telecommuters currently face concerning where they owe taxes and the confusion their employers face concerning where they must withhold. In addition, H.R. 1360 is necessary to assure the continued growth of interstate telecommuting, an important form of e-commerce.[9]

Dolores W. Gregory, "Proposal Barring New York's 'Convenience of Employer' Rule May Be Ripe for Attachment to Federal Energy Legislation," *BNA Multistate Tax Report*, Vol. 14, No. 9, Sept. 28, 2007, p. 471 (interview of Nicole Belson Goluboff); Nicole Belson Goluboff, "The U.S. House Judiciary Committee Should Consider the Telecommuter Tax Fairness Act" (Letter to the Editor), *State Tax Notes*, Aug. 20, 2007, p. 533.

[8] Section I.

[9] *See* Statement of Professor Edward A. Zelinsky, "Economic Development and the Dormant Commerce Clause: the Lessons of Cuno v. Daimler Chrysler and Its Effect on State Taxation Affecting Interstate Commerce," Joint Oversight Hearing of the Subcommittee on Commercial and Administrative Law and the Subcommittee on the Constitution, Civil Rights, and Civil Liberties, May 24, 2005, available at http://judiciary.house.gov/media/pdfs/zelinsky052405.pdf (discussing criteria for when Congress should intervene in state tax

Between 2004 and 2006, the number of Americans who worked from home for their employers at least once a month jumped by 63%, from 7.6 million to 12.4 million.[10] A key reason for this surge in growth is that telework offers important benefits for employees, businesses, governments and communities. Indeed, telework can help the nation address some of its most pressing challenges.

For example, by reducing the number of drivers on the road and the number of people who rely on mass transit, telework can reduce traffic congestion, air pollution and greenhouse gas emissions. It can lower the cost of maintaining and expanding our transportation infrastructure. It can also reduce our fuel consumption, helping us on the way to energy independence and reducing the cost of gasoline for America's workforce.

Telework can bring new jobs to rural communities. It can also enable businesses and government offices to continue running in the event of an emergency - like a terrorist attack, a catastrophic storm or a flu pandemic.

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policies, Professor Zelinsky explains: "Congress should exercise its Commerce Clause authority when conflicting tax policies impede the interstate mobility of persons, goods and services, thereby hindering the continental common market which is the U.S. economy. [The Telecommuter Tax Fairness Act] satisfies this criterion").

10 "Telework Trending Upward, Survey Says," WorldatWork Press Release, Feb. 8, 2007; The Dieringer Research Group, "2006 Telework Trendlines," 2006 American Interactive Consumer Survey.

Telework can help older Americans earn wages longer, and it can help disabled Americans, including disabled war veterans returning from Iraq and Afghanistan, enter or reenter the civilian workforce. It can help employees improve their work/family balance, and it can help employers become more profitable, reducing overhead, recruitment and turnover costs and increasing productivity.

By subjecting interstate telecommuters to the risk of double taxation, the convenience of the employer rule discourages telework and sabotages the nation's ability to maximize these benefits. To make it easier for more Americans to telework - to make it easier for the country to exploit the many advantages of Internet-based commuting - Congress should abolish the convenience rule.

IV. Conclusion

H.R. 3359 and H.R. 1360 should be approved together. The bills are related in that both are designed to protect multi-state employees from confusing state income tax obligations and to protect their employers from hard-to-manage payroll requirements.

H.R. 1360 must be enacted for H.R. 3359 to achieve its goals. If H.R. 3359 were approved without H.R. 1360, New York and other states could easily circumvent the "more than 60 days" requirement of H.R. 3359, applying a rule like the convenience of the employer rule to conclude that days a nonresident actually spent outside the state were in-state days.

Further, if H.R. 3359 were approved without H.R. 1360, the current confusion employees and employers face could worsen: Even if a multi-state telecommuter characterized his telework days as home state days for purposes of determining whether he had nexus in his employer's state, if he did have nexus, he would then have to characterize those same telework days as days spent in the employer's state for purposes of determining his specific tax liability in the employer's state.

Finally, even if the Subcommittee concludes that H.R. 3359 does not merit advancement, it should still approve and promote H.R. 1360. H.R. 1360 would bring greater clarity and fairness to the taxation of multi-state telecommuters, and it would remove a powerful deterrent to the continued growth of an important form of interstate e-commerce.

LETTER FROM VARIOUS EMPLOYERS IN SUPPORT OF H.R. 3359

H.R. 3359: "The Mobile Workforce State Income Tax Fairness and Simplification Act of 2007"
November 1, 2007

The employers listed below strongly support the enactment of H.R. 3359, The Mobile Workforce State Income Tax Fairness and Simplification Act of 2007, introduced by Congressman Hank Johnson and Congressman Chris Cannon.

This bill would enhance compliance with state personal income tax laws and simplify greatly the onerous burdens placed on employees who travel outside of their resident states for temporary periods and on employers who have corresponding withholding requirements.

Issue

Every work day in our country, thousands of Americans travel outside their home state on business trips for temporary periods. Most states have their own set of requirements for filing non-resident individual income tax returns and commensurate rules for employer withholding on those employees. Most individuals are not aware of this patchwork of non-resident state income tax filing rules, and many employers are required to incur extraordinary expenses to comply with withholding requirements.

Solution

H.R. 3359 would establish fair, administrable and uniform rules (including appropriate de minimis rules) to ensure that the appropriate amount of tax is paid to state and local jurisdictions without placing undue burdens on employees and their employers.

On behalf of American employers and their employees who travel for business, we request your support for this important legislation.

Sincerely,

Abercrombie & Fitch Co.
Aerospace Industries Association
Aker Kvaerner
Alaska Newspaper Inc.
Alliance Coal, LLC
Aluminium Company of America
Alutiiq LLC
American Eagle Outfitters, Inc.
American Payroll Association
Ann Taylor
Applied Materials
ARISE Incorporated
Association of Washington Business
Bank of America, N.A.
Bayer Corporation
BloodCenter of Wisconsin Inc.
Bob Evans Farms, Inc.
Business and Institutional Furniture Manufacturers Association (BIFMA)
Calista Corporation
Chiulista Services Inc.
Cisco Systems
City of West Des Moines, IA
CoAdvantage
The Coca Cola Company
Cokala Tax Reporting Solutions LLC

Community Health Systems
Community Memorial Hospital of Menomonee Falls Inc.
Consolidated Restaurant Operations, Inc.
Con-way Inc.
Costco Wholesale Corporation
CTR Systems
Council On State Taxation (COST)
Countrywide Home Loans
Delta Air Lines, Inc.
Discovery Communications LLC
Diocese of Buffalo, NY
Dow Chemical Company
EDS
Electronics for Imaging, Inc.
Elliott Davis, LLC
Fairbanks Scales, Inc.
Financial Executives International, Committee on Taxation
Four Seasons, Inc.
Friedman's, Inc.
General Motors Corporation
Georgia-Pacific LLC
Hall Financial Group
Hanover Direct, Inc.
Harbor America
HCR Manor Care
The Home Depot
Johnson & Johnson
Koch Industries, Inc.
La Quinta Inns & Suites
Limbach Facility Services LLC
Limited Brands, Inc.
Lockheed Martin Corporation
Louisiana Association of Business & Industry (LABI)
Lowes Companies, Inc.
Lutheran SeniorLife
Maryland Chamber of Commerce
MedicalEdge Healthcare Group
Microsoft Corp.
Modine Manufacturing Company
Money Management International
Montana Taxpayers Association
National Association of Manufacturers
National Association of Tax Reporting and Payroll Management
National Retail Federation
Neiman Marcus, Inc.
North Carolina Chamber
Oldcastle Glass, Inc.
Organization for International Investment
PepsiCo, Inc.
Perot Systems
Pitt Ohio Express, LLC
Pro-Factors, Inc.
Roche Diagnostics Corporation
Sempra Energy
Sephora
Sikich LLP
SynQ Solutions, Inc.
SYSCO Corporation
Teledyne Continental Motors
Telerx Marketing
The Container Store
The Financial Services Roundtable
The TJX Companies Inc.
Time Warner
Time Warner Cable
Town of Hopkinton, NH
Townsend and Townsend and Crew LLP
Transervice Logistics Inc.
Tunista Inc.
Turner Broadcasting System, Inc.
US Chamber of Commerce
Vilter Manufacturing LLC
Vermeer Mfg. Co.
Visa Inc.
Wachovia Corporation
Westinghouse Electric Company
Yulista Management Services Inc

LETTER FROM KRISTINA RASMUSSEN, DIRECTOR OF GOVERNMENT AFFAIRS, NATION TAXPAYERS UNION IN SUPPORT OF H.R. 3359

National Taxpayers Union

November 7, 2007

Subcommittee on Commercial and Administrative Law
United States House of Representatives
Washington, D.C. 20515

Dear Chairman Sanchez and Ranking Member Cannon:

On behalf of the 362,000 members of the National Taxpayers Union (NTU), I write to endorse H.R. 3359 (the Mobile Workforce State Income Tax Fairness and Simplification Act) and H.R. 1360 (the Telecommuter Tax Fairness Act). NTU encourages the joint advancement of both bills.

NTU and its members work to promote tax policies that are fair, equitable, and simple. We believe that the current patchwork of laws, which govern when a traveling or telecommuting non-resident employee must pay another state's income taxes, is in need of simplification. As America's workforce becomes more mobile and as our working environments become more flexible, we need forward-looking, pro-growth tax policies that reflect these realities.

H.R. 3359 would stipulate that non-resident employees would only be liable for taxes when they work in any given state or locality for more than 60 days in any calendar year. By setting a simple and uniform policy, this bill would help cut down on the billions of hours and dollars that are spent on tax compliance by employees and employers every year. Furthermore, according to testimony from the Council On State Taxation, adoption of this bill would result in a small net reduction (0.01 percent or $93 million) in revenue collections nationwide.

However, H.R. 3359 does not address the destructive policy of requiring employees of companies based "in-state" to pay income tax to that state regardless of where the work was performed – so long as the work *could* be performed "in-state." Although no other state besides New York currently applies its laws this way, as telecommuting becomes more common states will have strong fiscal and political temptations to harshly penalize out-of-state workers under their own laws. H.R. 1360, the Telecommuter Tax Fairness Act, would stop this anti-taxpayer practice.

Taken together, H.R. 3359 and H.R. 1360 would ease tax compliance for the nation's millions of traveling employees and telecommuters. We hope to work closely with you toward passage of these important bills. House roll call votes on H.R. 3359 and H.R. 1360 will be included in our annual Rating of Congress.

Sincerely,

Kristina Rasmussen

Kristina Rasmussen
Director of Government Affairs

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