MULTISTATE TAX COMMISSION

Working Together Since 1967 to Preserve Federalism and Tax Fairness

To: **Wood Miller, Chair**
Members of MTC Income & Franchise Tax Uniformity Subcommittee

From: **Shirley Sicilian, General Counsel**

Date: **June 11, 2010**

Subject: **Model Mobile Workforce Statute**

On March 22, 2010, the Uniformity Committee recommended its model Mobile Workforce statute to the Executive Committee, and on April 7, 2010, the Executive Committee approved the model for public hearing. A public hearing was held after 30 days notice on May 10, 2010. Public Comment was received from Boerio & Company, CPAs; Council on State Taxation; the Massachusetts Department of Revenue; the Missouri Department of Revenue; and the Montana Department of Revenue. On May 18, 2010, the hearing officer submitted a report to the Executive Committee (Attachment 1). On May 21, the Montana Department of Revenue provided additional comments to the Executive Committee, recommending that the model be sent back to the Uniformity Committee (Attachment 2). On May 24, 2010 the Executive Committee met by teleconference to discuss the matter and voted to send the proposal back to Uniformity Committee for further consideration. On June 10, the Montana Department of Revenue provided an alternative proposal (Attachment 3).

The model is now before the Uniformity Committee for reconsideration.

MULTISTATE TAX COMMISSION

Working Together Since 1967 to Preserve Federalism and Tax Fairness

Report of the Hearing Officer
Model Mobile Workforce Withholding and Individual Income Tax Statute
May 18, 2010

I. Introduction and Summary

On April 7, 2010, the Commission Executive Committee approved proposed model Mobile Workforce statutes for public hearing. Under the proposal, an employer would not be required to withhold non-resident employee wage income for a state if the employee spent less than a de-minimus number of work days there and did not fall into one of the exception categories. Likewise, the employee would not be required to file and pay tax on that wage income to the non-resident state, as long as the employee has no other income attributable to the state. The employee would, of course, be subject to tax on that income in his or her home state.

On May 10, 2010, the hearing officer held the public hearing and received written comments from the Council on State Taxation, the Massachusetts Department of Revenue, the Missouri Department of Revenue, the Montana Department of Revenue, and the managing director of CPA firm Boerio and Company. (*See* Attachments B through F, Public Comments.) This Report summarizes the proposal's procedure and substance, reviews the public comment received, and explains the hearing officer's recommendation that the proposal be approved with modifications. (*See* Attachment A, Proposal with recommended modifications.)

The proposal is now before the Executive Committee to consider approval for a bylaw 7 survey. The Committee may approve the proposal, with or without modifications; remand the proposal to an earlier stage of the process for further development; or reject the proposal and end the project. If the proposal is approved, it will be submitted to a bylaw 7 survey of Compact member states. The bylaw 7 survey asks whether the state would consider adopting the proposal in its jurisdiction. If a majority of Compact member states respond in the affirmative, the proposal will be submitted to a vote of the Commission in July, 2010.

II. Procedural Background

A. Development of the Proposal

At its May 2009 meeting, the Executive Committee discussed the extent to which standard withholding requirements pose challenges for employers when employees earn

wage income during short business visits to non-resident states. These challenges have prompted some in the business community to support federal legislation H.R. 3359 and H.R. 2110, which would pre-empt states from taxing this non-resident wage income. (*See* Attachment H, H.R. 2110.) The Executive Committee referred the issue to the Uniformity Committee and asked that it expedite development of a model state law to address these challenges for states that wish to do so.

The Uniformity Committee, at its July 2009 meeting, formed a small work group of five states (Idaho, Colorado, Montana, New York, and California) to create a list of relevant policy questions. The work group held two teleconferences in August of 2009 and produced a policy checklist. The Uniformity Income & Franchise Tax Subcommittee then met by teleconference in September, October, and November of 2009 to answer those questions. (*See* Attachment G, Policy checklist.) Each of the Subcommittee teleconferences was well attended by state and taxpayer representatives, including the Council on State Taxation, the American Payroll Association, and the Federation of Tax Administrators.

Based on the Subcommittee's policy choices, staff produced a draft model statute which was discussed and further amended by the Subcommittee at in-person and teleconference meetings held December 2, 2009; January 22, 2010; March 3, 2010 and March 22, 2010. During each discussion, the Subcommittee received valuable input from the Council on State Taxation, the American Payroll Association, and other individual business representatives. On March 22, 2010 the Subcommittee voted to approve the model and the Uniformity Committee then voted to recommend it favorably to the Executive Committee for approval for public hearing. On April 7, 2010, the Executive Committee approved the model for public hearing.

B. Public Hearing

A public hearing was held after 30 days notice on May 10, 2010 in Washington, D.C. Oral public comments were received. In addition, five sets of written comments were received prior to the closure of the public comment period on May 10, 2010. A one day extension of time was granted in one case. The written comments are attached as Exhibits:

Exhibit B	Council On State Taxation (COST) – Joseph R. Crosby, COO & Senior Director, Policy
Exhibit C	Massachusetts Department of Revenue (MA DOR)– Michael T. Fatale, Chief, Rulings and Regulations Bureau
Exhibit D	Missouri Department of Revenue (MO DOR) – Wood Miller, Managing Counsel, General Counsel's Office
Exhibit E	Montana Department of Revenue (MT DOR) – Dan Bucks, Director of Revenue
Exhibit F	Boerio and Company CPAs – (Boerio) Dave Clark, Managing Director

III. Summary of Proposal

Basic Structure

- ***Covers Both Employer Withholding and Non-resident Employee Individual Income Tax.*** Under the model recommended by the Uniformity Committee, an employer would not be required to withhold a non-resident employee's wage income for a state if the employee spent less than a de-minimus number of work days there and did not fall into one of the exception categories. Likewise, the employee would not be required to file and pay tax on that income to the non-resident state, as long as the employee has no other income attributable to the state. The employee would, of course, be subject to tax on that income in his or her home state.
- ***Addresses Only State Tax.*** The model does not address local withholding or individual income taxes. The Subcommittee felt that should be an option for the states, but need not be included in our basic model.
- ***Reciprocity.*** The withholding and individual income exemptions are contingent on enactment of substantially similar exemptions in the non-resident employee's home state.
- ***Specific Statement on Jurisdiction to Tax.*** Both the individual income and the withholding provisions include a specific statement that the exceptions have no application to the imposition of, or jurisdiction to impose, this or any other tax on any taxpayer.

Important Details

- ***20 work-day threshold.*** The model sets 20 work days as the de-minimus threshold under which the state would not exercise its jurisdiction to require withholding or individual income tax filing. Any part of a day spent in a state counts as one day toward the threshold, even if multiple states are visited in a single 24 hours. Presence in a state purely for travel through it does not count toward the threshold.
- ***No Income Threshold.*** The model does not set an income threshold, although income level is a factor in one of the exceptions to the rule.
- ***Exceptions.*** The model provides exceptions from the exclusions for: (1) professional athletes and members of a professional athletic team, (2) professional entertainers, (3) "persons of prominence," (4) construction workers, (5) persons who are "key employees" under IRC 416(i) provisions related to deferred compensation, by virtue of the income test but not the ownership test, and whether working for a privately or publicly traded company. An employee would be considered a "key employee" for our purposes if that person is one of the 50 highest paid officers in a publicly or privately held company, and had a salary of at least $160,000 in 2010. (The income threshold under IRC 416(i) is indexed to inflation in $5,000 increments.)
- ***Employer Safe-Harbor from Withholding Penalties.*** A safe-harbor from penalties is provided for situations where the employer has miscalculated the number of days. The safe harbor is available where the employer has relied on (1) a time and attendance system, (2) or if no time and attendance system is available, then employees

travel records, or (3) if neither a time and attendance system nor employee travel records are available, then employee travel expense reimbursement requests.

IV. Public Comment and Hearing Officer Recommendations

Threshold Number of Days

COST provided written and oral comment in strong support of an amendment to lengthen the day threshold from 20 to 30. COST's comments point out that the original federal bill would have established a 60 day threshold, which COST estimates would have a net fiscal impact on all states together of less than $100 million annually. After negotiations at the federal level, the bill's sponsor introduced new legislation cutting the day threshold in half, to 30 days. COST estimates that moving from 60 to 30 days would double the number of employees that would be subject to nonresident taxation and reduces the net fiscal impact to $40 million annually. Information available to COST shows that moving from 30 to 20 days will again nearly double the number of employees subject to tax. No further estimate is provided for the net fiscal impact. But COST notes that there may be no fiscal impact at stake even at substantially higher threshold levels because of reciprocity agreements and because several states already provide thresholds for nonresidents in excess of 20 days.

Some states do already provide thresholds for nonresidents in excess of 20 days. But according to data provided by COST and the American Payroll Association, there are not very many. More than half the states that have an individual income tax allow no exemption – based on either day or dollars – and presumably would currently require employers to withhold for nonresidents beginning with the first day of employment duties in the state. Of the remaining states that allow an exemption, only four have a day threshold set higher than 20 days (AZ, HI, GA, and UT).[1]

This means that for the large majority of states, a day threshold of 20 days is a significant increase compared to current provisions. COST estimates the net fiscal impact for all states together would be something less than $40 million. On average, that impact would be less than $1 million per state. Even this figure would present a difficulty for states in the current fiscal situation. But the proposal does not tend to impact states uniformly. Instead, there are extreme variances. At least one state is estimated to have a negative $45 million impact itself, while others would actually experience a positive impact.[2] These are significant impacts for states. A threshold of 20 days is also likely to have a significant impact for some states, but 20 days is 33% less than a 30 day threshold, and the volatility of the result should decrease accordingly.

Although fewer employees will come under a 20 day exception, the reduction in fiscal variance will enable more states to adopt the proposal, and allow greater

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[1] *See* Mobile Workforce Briefing Book, p. 8; Prepared by COST and submitted as testimony to the Uniformity Committee on September 9, 2009.

[2] *Id.,* p. 63.

administrative cost savings for both states and employers through increased uniformity. In addition, many states provide reciprocal agreements – with no day or dollar threshold - and the proposed statutory language explicitly preserves those agreements with their resulting administrative benefits to individuals and employers.

The MO DOR's comments further remind us that moving the threshold in either direction creates offsetting administrative and revenue impacts. For example, moving the threshold downward reduces the proposal's administrative benefits for states, employers, and employees; but also reduces state revenue loss. On the other hand, moving the threshold upward increases administrative benefits, but also increases revenue loss.

The Commission states, after receiving significant helpful input from COST and the American Payroll Association, have chosen to set the balance at 20 days and the hearing officer does not recommend a change to that delicate balance.

Income Threshold vs. Day Threshold

The MT DOR commented that the proposal's provisions on individual income tax should be revised to reference the income threshold filing level in any state that has an income threshold for individual income tax. Alternatively, the MT DOR suggests the proposal be returned to the Uniformity Committee for further consideration. The MT DOR is concerned that the 20 day threshold creates a "dual test" that adds unnecessary complexity, creates inequities between non-resident and resident individual income taxpayers, creates inequities among non-resident individual income taxpayers, and is inconsistent with the established position of the MTC concerning filing thresholds for business activity taxes.

- ***Consistency with other Commission recommendations on physical presence***

The MT DOR's last concern raises an especially important point and bears careful consideration. The proposal is in no way intended to signal an endorsement of a physical presence nexus standard for individual income or any other tax. Rather, the proposal is intended as an exercise of state authority to allow a de minimus exception within the clear scope of state taxing jurisdiction. The existence of the de minimus exception itself indicates a presumption of state taxing authority, which would be exercised absent the explicit exemption. The proposal is intended to be consistent with Commission's position on business activity tax nexus. That position acknowledges the desirability of state-authorized de minimus exceptions for non-domiciliary corporations, and proposes a standard based on de minimus amounts of physical property, employees, or sales in a state. Likewise, this proposal would establish a state de minimus exception for non-resident individuals, applicable to only wage income; and sets a standard based on, among other things, de minimus employee presence (IIT 1(a)) or income (IIT 2(e)) in the state. This de minimus exception does not apply if there is *any other* income sourced to the state, whether or not the employee is physically present. (*See* IIT section 1(a) and (b).) If other types of income are sourced to the state, or if the employee falls within one of the enumerated exceptions, the provision retains full authority for the state to exercise its jurisdiction to tax, regardless of physical presence.

Indeed, the withholding provision includes explicit language on this point:

> (3) This section establishes an exception to withholding and deduction requirements and has no application to the imposition of, or jurisdiction to impose, this or any other tax on any taxpayer.

Likewise, the individual income tax "returns and payment" portion of the proposal includes explicit language on the same point:

> (2) This section is applicable to the determination of an individual income taxpayer's filing requirement and has no application to the imposition of, or jurisdiction to impose, this or any other tax on any taxpayer.

However, there is no such language currently included in the individual income tax "non-resident compensation exclusion" portion of the proposal. In light of the MT DOR's concerns on this important point, the hearing officer recommends similar language be added to that section, as follows:

> (4) This section creates an exclusion from non-resident compensation under certain de minimus circumstances and has no application to jurisdiction to impose this or any other tax on any taxpayer.

- ***Potential for inequities***

MT DOR also suggests the proposal creates inequities among and between residents and non-residents in the application of income taxes. Individual income taxpayers are generally excused from filing if income falls below a certain threshold. Under the proposal, it will be possible for non-residents to earn income in the state above that threshold, yet not be subject to tax there. The MT DOR recommends that the individual income tax day and income thresholds be eliminated and states rely instead on their standard filing thresholds (this could be specific in the model, but need not be). The hearing officer does not believe the non-resident "safe harbor" based on number of days creates an inconsistency among residents and non-residents that supports elimination of the threshold. Many states currently provide reciprocity agreements that create the same sorts of inconsistency for their respective residents. That is, non-residents may be completely excused from filing, regardless of the amount of income earned in the state. The existence of these agreements seems to indicate that states view the administrative gains for themselves, their residents, and employers, to be worth the level of inconsistency created. The non-residents are not excused from state income tax, rather they simply pay to their state of residence rather than the source state. The proposal explicitly preserves these existing reciprocity agreements. The proposal also retains consistent treatment of residents among the states by establishing a reciprocity requirement for application of the statute – that is, the "safe harbor" applies only to employees from states that reciprocate for the home state's residents. (*See* Individual income tax section 1(c)). For these reasons, the hearing officer does not recommend a change.

- ***Added complexity***

The MT DOR also expresses concern that the proposal creates added complexity by establishing a 20 day threshold in addition to states' standard "income based" filing requirement threshold. Complexity is an important consideration and the concern is well

taken. However, the hearing officer believes that, without the 20 day threshold for individual income tax, the administrative burden that we are trying to rectify for employers would simply fall to employees. Employees who spend only small amounts of time in the state would become responsible for determining the state's filing requirements and, if necessary, filing in the state, all without the benefit of having his or her income withheld for the state by the employer. Under the proposal, both the non-resident employee and the employer can rely on the 20 day threshold. If the employee spends less than 20 days in the state, the employee knows he or she need not file there, and the employer will withhold for the employee's home. This should reduce administrative burden for employees who might otherwise face non-uniform filing thresholds and exceptions in multiple states. For this reason, the hearing officer does not recommend a change.

"Key Employee" Clarifications

Two commenters recommend clarifications to the "key employee" exception in the Individual Income Tax provision 2(e). First, the MA DOR suggests deleting "identified as," because there is technically no "identification" of such persons pursuant to the Code. The MA DOR also recommends language be added, based on its understanding that the Uniformity Subcommittee members "were seeking a dollar limitation like that set forth in [IRC Section] 416(i) that has general applicability, and that therefore would not be limited to circumstances in which a company happened to have in place a specific type of benefit plan." The hearing officer believes this understanding is correct and recommends the proposed changes be adopted as follows:

> (e) a person who is ~~identified as~~ a key employee, without regard to ownership or the existence of a benefit plan, for the year immediately preceding the current tax year pursuant to Section 416(i) of the Internal Revenue Code.

Second, Mr. Clark of Boerio and Company expressed concern in his written comments that the "key employee" exception (to the filing exemption) may sweep in certain self-employed persons – officers of LLCs, LLPs, partnerships, etc. But during the hearing, Mr. Clark suggested an amendment was not necessary, since the exemption is for wage income only and would not apply to self-employed persons at all. The hearing officer agrees with Mr. Clark's understanding and no amendment is necessary.

Respectfully Submitted,

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Shirley K. Sicilian
Hearing Officer

Attachment A

MULTISTATE TAX COMMISSION

Working Together Since 1967 to Preserve Federalism and Tax Fairness

MTC Model Mobile Workforce Act

As Approved for Public Hearing - Showing Recommendations of the Hearing Officer
May 18, 2010

INDIVIDUAL INCOME TAX

- **Computation of Taxable Income**
  - **Adjusted Gross Income from Sources Within This State.**
    - **Nonresident Compensation, Exclusion**

(1) Compensation subject to withholding pursuant to [cite to state withholding tax], without regard to [cite to withholding tax exception (below)], that is received by a nonresident for employment duties performed in this state, shall be excluded from state source income if:

(a) the nonresident has no other income from sources within this state for the tax year in which the compensation was received;

(b) the nonresident is present in this state to perform employment duties for not more than 20 days during the tax year in which the compensation is received, where presence in this state for any part of a day constitutes presence for that day unless such presence is purely for purposes of transit through the state; and

(c) the nonresident's state of residence provides a substantially similar exclusion or does not impose an individual income tax.

(2) This section shall not apply to compensation received by:

(a) a person who is a professional athlete or member of a professional athletic team;

(b) a professional entertainer who performs services in the professional performing arts;

(c) a person of prominence who performs services for compensation on a per-event basis;

(d) a person who performs construction services to improve real property, predominantly on construction sites, as a laborer; or

(e) a person who is ~~identified as~~ a key employee, without regard to ownership or the existence of a benefit plan, for the year immediately preceding the current tax year pursuant to Section 416(i) of the Internal Revenue Code.

(3) This section shall not prevent the operation, renewal or initiation of any agreement with another state authorized pursuant to [cite to Code section that allows reciprocity agreements].

(4) This section creates an exclusion from non-resident compensation under certain de minimus circumstances and has no application to jurisdiction to impose this or any other tax on any taxpayer.

INDIVIDUAL INCOME TAX

- **Returns and Payment**
  - **Persons required to file returns, exception**

(1) A nonresident whose only state source income is compensation that is excluded pursuant to [Cite to Nonresident Compensation, Exclusion] has no tax liability under this Act and need not file a return. Provided that when, in the judgment of the Department, such nonresident should be required to file an informational return, nothing in this section shall preclude the Department from requiring such nonresident to do so.

(2) This section is applicable to the determination of an individual income taxpayer's filing requirement and has no application to the imposition of, or jurisdiction to impose, this or any other tax on any taxpayer.

WITHHOLDING TAX

- **Withholding from Compensation, Exception**

(1) No amount is required to be deducted or retained from compensation paid to a nonresident for employment duties performed in this state if such compensation is excluded from state source income pursuant to [cite to Nonresident Compensation, Exclusion], without regard to [cite to Nonresident Compensation, Exclusion, § (1)(a)].

(2) An employer that has erroneously applied the exception provided by this section solely as a result of miscalculating the number of days a nonresident employee is present in this state to perform employment duties shall not be subject to penalty imposed under [cite to withholding penalty provisions] if:

(a) the employer relied on a regularly maintained time and attendance system that (i) requires the employee to record, on a contemporaneous basis, his or her work location each day the employee is present in a state other than (A) the state of residence, or (B) where services are considered performed for purposes of [cite to state unemployment insurance statute], and (ii) is used by the employer to allocate the employee's wages between all taxing jurisdictions in which the employee performs duties;

(b) the employer does not maintain a time and attendance system described in subsection (a) and relied on employee travel records that the employer requires the employee to maintain and record on a regular and contemporaneous basis; or

(c) the employer does not maintain a time and attendance system described in subsection (a), or require the maintenance of employee records described in subsection (b), and relied on travel expense reimbursement records that the employer requires the employee to submit on a regular and contemporaneous basis.

(3) This section establishes an exception to withholding and deduction requirements and has no application to the imposition of, or jurisdiction to impose, this or any other tax on any taxpayer.

Attachment B

Officers, 2009-2010

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U.S. Bancorp

Richard Prem
Amazon.Com

Bruce J. Reid
Microsoft Corporation

Frances B. Sewell
Tyco International

John H. Stagmeier
Georgia-Pacific LLC

Amy Thomas Laub
Tempur-Pedic International Inc.

Warren D. Townsend
Wal-Mart Stores, Inc.

R. Paul Weatherford
Sears Holdings Management Corporation

James R. Williams
Massachusetts Mutual Life Insurance Co.

Testimony to the Multistate Tax Commission

Proposed Model Mobile Workforce Withholding and Individual Income Tax Statute

Joseph R. Crosby
COO & Senior Director, Policy
Council On State Taxation

May 10, 2010

Thank you once again for the opportunity to provide testimony to the Multistate Tax Commission (MTC) on behalf of the Council On State Taxation (COST) regarding the MTC's proposed Model Mobile Workforce Withholding and Individual Income Tax Statute ("Model Statute"). COST appreciates the significant efforts made by the MTC on this important project and strongly urges the MTC to set the "day threshold" in the Model Statute at 30 days.

About COST

COST is a nonprofit trade association based in Washington, DC. COST was formed in 1969 as an advisory committee to the Council of State Chambers of Commerce and today has an independent membership of nearly 600 major corporations engaged in interstate and international business. COST's objective is to preserve and promote the equitable and nondiscriminatory state and local taxation of multijurisdictional business entities.

The Day Threshold Must be Lengthened to 30 Days

Legislation introduced during both the 109th and 110th Congress addressing the taxation of nonresident employees set a threshold of 60 days below which nonresidents would not be subject to personal income tax in a state. After careful consideration and deliberation, the threshold was set at 60 days because it struck an appropriate balance between two goals: 1) to provide administrative simplification for employees and employers; and 2) to minimize disruptions to state revenue flows. The 60-day threshold is far shorter than any other law Congress has enacted in this area, most of which provide for full preemption. Importantly, a 60-day threshold would have a net fiscal impact on the states as a whole of less than $100 million annually.

Despite this careful balancing, the MTC opposed the 60-day threshold as too long. As part of extensive negotiations between the employer community and representatives of the states, Rep. Hank Johnson (D-GA) determined that a 30-day threshold was an appropriate compromise, and he introduced legislation to that effect in the 111th Congress (H.R. 2110). As an aside, H.R. 2110 includes numerous other changes from prior federal legislation that were included at the request of representatives of state and local governments.

Based on a survey of employers conducted by COST, the 30-day threshold more than doubled the number of employees that would be subject to nonresident taxation (when compared against the number that would be subject to tax under a 60-day threshold). On the positive side, the lower threshold also reduces the net fiscal impact on the states as a whole to approximately $40 million annually.

The MTC's Model Statute sets the day threshold at 20 days. Based on information available to COST, a 20-day threshold would again nearly double the number of employees subject to tax (when compared to a 30-day threshold). In the context of a model statute to be adopted at the state level, the MTC should feel no need to set such a low threshold. There is likely no fiscal impact at stake even if a substantially higher threshold is selected because of the reciprocity provision in the Model Statute. Of equal importance, if the Model Statute creates a fiscal impact, state legislatures will debate whether the fiscal impact is acceptable when compared to the benefits provided to their state residents. Several states already provide thresholds for nonresidents in excess of 20 days without any apparent deleterious impact, fiscal or otherwise. Furthermore, dozens of reciprocal agreements exist between states that provide for total exemptions from tax—no thresholds, day, dollar or otherwise. A 30-day threshold is the minimum that should be included in the Model Statute.

Conclusion

As noted in our previous testimony, there are several areas in the Model Statute where COST would support further modifications (e.g., the definition of a "day" and the employer reliance standard). These areas, although important, do not critically impair the Model Statute. The insufficient day threshold must be remedied if the Model Statute is to achieve its goals. We urge the MTC to raise the threshold to 30 days.

Attachment C

From: Fatale, Michael
Sent: Wednesday, April 21, 2010 12:20 PM
To: 'lking@mtc.gov'
Cc: 'Shirley K. Sicilian'
Subject: Mobile Workforce comments

The following comments are submitted in connection with the MTC's draft Model Mobile Workforce Withholding and Individual Income Tax Statutes ("draft model statute"), which is set forth on the MTC's web site and is stated to be subject to a public hearing to be held on April 7, 2010.

My comments are with respect to section 2 of the draft model statute, which currently states:

> **(2) This section shall not apply to compensation received by:**
>
> > **(a) a person who is a professional athlete or member of a professional athletic team;**
> > **(b) a professional entertainer who performs services in the professional performing arts;**
> > **(c) a person of prominence who performs services for compensation on a per-event basis;**
> > **(d) a person who performs construction services to improve real property, predominantly on construction sites, as a laborer; or**
> >
> > **(e) a person who is identified as a key employee, without regard to ownership, for the year immediately preceding the current tax year pursuant to Section 416(i) of the Internal Revenue Code.**

In particular, my comments are with respect to section 2(e) of the draft model statute. My comments are as follows.

First, section 2(e) of the draft model statute currently references a person "who is ***identified as*** a key employee" under Internal Revenue Code ("Code") section 416(i). But it seems to me that there is no "identification" as such that takes place under this Code provision. Therefore, I think that section 2(e) of the draft model statute should merely reference a person that "***is*** a key employee" within the meaning of this Code section.

Second, also with respect to section 2(e) of the proposed model statute, I question whether this section should state not merely "without regard to ownership" but instead "without regard to ownership ***or the existence of a benefit plan***." I make this comment because the definition of a "key employee" set forth in the referenced Code section 416(i) seems to apply only in the instance of certain benefit plans. In particular, Code section 416(i)(1)(A) defines a "key employee" as follows:

> **In general -- The term "key employee" means an employee who, at any time *during the plan year*, is--**
>
> **(i) an officer of the employer having an annual compensation greater than $130,000,**
> **(ii) a 5-percent owner of the employer,**
> **(iii) a 1-percent owner of the employer having an employer compensation from the employer of more than $150,000...**

I do not purport to be an expert on the Code's benefit plan rules in general, or Code section 416 in particular, and so among other things I have no knowledge as to the breadth of what constitutes a "plan" within the meaning of Code s. 416(i). I do note that the definition set forth in Code section 416(i)(1)(A) appears to apply throughout Code section 416(i), where the tests set forth in Code section 416(i)(1)(A) are further qualified. However, nothing set forth in Code section 416(i) seems to dispense with the notion clearly indicated in Code section 416(i)(1)(A) that this Code section's definition of a "key employee" only applies in the context of certain benefit plans. In contrast, it is my general understanding that the states participating in the MTC's Model Workforce drafting effort were seeking a dollar limitation like that set forth in Code s. 461(i) that has general applicability, and that therefore would not be limited to circumstances in which a company happened to have in place a specific type of benefit plan. Therefore, I would suggest adding the reference to section 2(a) as stated above that states that this section applies irrespective as to the existence of a benefit plan.

Thank you for considering my comments.

Michael T. Fatale
Chief, Rulings & Regulations Bureau
Massachusetts Department of Revenue
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Boston, MA 02114-9566
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Fatale@dor.state.ma.us

Attachment D

From: Miller, Wood [mailto:Wood.Miller@dor.mo.gov]
Sent: Monday, May 10, 2010 1:17 PM
To: Loretta King
Subject: MTC: Comments from Missouri for Public Hearing for Proposed Mobile Workforce Withholding and Individual Income Tax Statute

To: Shirley Sicilian, Hearing Officer
From: Wood Miller, Managing Counsel, General Counsel's Office, Missouri Department of Revenue
Date: May 10, 2010
RE: Proposed Model Mobile Workforce Withholding and Individual Income Tax Statute

These commits are submitted in regard to the threshold number of days contained in the proposed model statute. While it is desirable to balance the benefits and costs of tax administration for both individual income tax and for withholding tax and for both employers and for the state tax administrator, the current proposal includes a threshold of twenty days for both the jurisdiction for a non-resident individual to be subject to a states income tax and for his employer to be subject to that non-resident state's withholding tax requirement. In setting the threshold, there is a concern that the costs may begin to outweigh the benefits not only in terms of tax amounts but also in terms of administrative costs. Corporate income tax payers are already familiar with a 14 day threshold connected with P.L. 86-272 and the Statement of Information Concerning Practices of Multistate Tax Commission and Signatory States under Public Law 86-272. Therefore, consideration could be given to the benefits derived from a uniformity of standards across taxation of income.

Thank you for considering my comments.

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Wood.Miller@dor.mo.gov

Attachment E

From: Bucks, Dan [mailto:DBucks@mt.gov]
Sent: Tuesday, May 11, 2010 5:28 PM
To: Loretta King; Shirley K. Sicilian
Cc: Joe Huddleston; Gilmer, Brenda; Daw, C A; Walborn, Eugene; McHugh, Shona; Lee Baerlocher; Miller, Wood
Subject: Additional Comment from Montana for Public Hearing on Model Mobile Workforce Withholding and Individual Income Tax Statute

To: Shirley Sicilian, Hearing Officer, Multistate Tax Commission
From: Dan Bucks, Director of Revenue, State of Montana
Subject: Further Comments on Model Mobile Workforce Withholding and Individual Income Tax Statute

Please accept this further comment and clarification with regard to the Model Mobile Workforce Withholding and Individual Income Tax Statute.

Item 2 of the comments I submitted yesterday focused on the inequity that the 20 working days test can create between residents and non-residents in the application of a state's income tax. That inequity also occurs among non-residents. A non-resident person with an annual rate of pay of $60,000 would earn $4,385 in 19 days. Thus, $4,385 is the value of the income tax exemption created by the 20 working days test for this person. However, a non-resident person with an annual rate of pay of $120,000 would earn $8,770 in 19 days. So the value of the second person's tax exemption created by the 20 working days test is twice as much—$8,770. The higher the rate of pay, the higher the value of the tax exemption created by the 20 working days test. Thus, the 20 working days test is contrary to principles of income tax equity because it treats non-residents persons with higher incomes more favorably than those with lower incomes, both residents and non-residents. The proposed statute would create this inequity both between non-residents with higher incomes and residents with lower incomes and also among non-residents of different income levels. Please note that the proposal does not create any inequity between residents with different incomes. In all cases under the proposal, the persons who are given favorable treatment as compared to other taxpayers are higher income non-residents—and the greater the income of the non-resident person, the greater the unjustified advantage they will enjoy over other taxpayers in the state where they had a temporary presence. A uniform income threshold for the imposition of a state's income tax avoids this inequity entirely. The inequity described here is a major reason to abandon using the number of working days, in any form, as the basis for imposing an individual income tax.

From: Bucks, Dan
Sent: Monday, May 10, 2010 8:47 AM
To: 'lking@mtc.gov'
Cc: Joe Huddleston (jhuddleston@mtc.gov); 'Shirley K. Sicilian'; Gilmer, Brenda; Daw, C A; Walborn, Gene; McHugh, Shona; Baerlocher, Lee; 'Wood.Miller@dor.mo.gov'
Subject: Comments from Montana for Public Hearing on Model Mobile Workforce Witholding and Individual Income Tax Statutes
Importance: High

To: Shirley Sicilian, Hearing Officer
From: Dan Bucks, Director of Revenue, State of Montana
Re: Model Mobile Workforce Withholding and Individual Income Tax Statutes

These comments are submitted in regards to the proposed model statute section 1 with regard to individual income taxation. This section should be revised to reference the income threshold filing level in any state that has an income threshold for their individual income tax. Alternatively, should the hearing officer wish to defer this matter for additional study, this section of the model statute could be returned to Multistate Tax Commission's Uniformity Committee for further consideration. Montana considers this section of the proposed model statute as now drafted to be unwise for these reasons:

1. The 20 day working presence test creates more complexity for the income tax administration of individual states that employ an income threshold for determining when a non-resident must file an income tax return. Instead of a simple income threshold test, the non-resident person and the taxing authority would need to apply a two-part test—the income test and the 20 working days in the state test to determine if the non-resident needs to file an income tax return. This double test would unnecessarily burden the tax administrative process. Further, there is no significant gain to the individual taxpayer in their initial decision to file a return for states that employ an income threshold. Most individuals know quite well their rate of pay and can determine whether or not they have exceeded the income filing thresholds of individual states in which they have worked. Further, states make the key features of their income tax systems, including filing thresholds, readily available to individuals on their web sites.
2. The dual test creates an inequity between residents and non-residents in the application of income taxes. Montana requires single individuals, residents and non-residents, to file individual income tax returns if they earn more than $3,860 in income in Montana. A non-resident individual whose annual rate of pay is more than $50,360 can exceed this threshold in 19 days or less. Thus, it will be possible for a material number of non-residents to earn more than $3,860 in income in Montana, yet under that model statute be excused from filing a Montana return. This result is inequitable with regard to Montana residents who will earn less income, but still be required to file Montana individual income tax returns. We see no reason why non-residents should be granted special, favorable treatment as compared to residents in the application of any state individual income tax. If the model statute were to rely on the income filing thresholds of each state, this inequity favoring non-residents would not be created by the model statute.
3. The potential inequities created by the 20 day test may be even greater in cases where the non-resident person works for more than one employer, including related parties, in a given state. Manipulation can occur unless related employers are aggregated.
4. The 20 day presence test is inconsistent with the established position of the Multistate Tax Commission concerning filing thresholds for business activity taxes. The Commission has clearly recommended economic threshold measures as opposed to physical presences thresholds for business taxes. Given the rapid growth of pass-through entity businesses that link between individual income taxes and business income taxes, the inconsistency between these two very different approaches to filing becomes increasingly problematic. Further, if the Commission were to endorse a

physical presence test for individual income taxes, it has the potential for undermining the credibility of the Commission with regard to its historic opposition to federal legislation imposing a physical presence test on states for the imposition of their business activity taxes. The Commission should be consistently supporting economic measures, instead of physical presence measures, with regard to the imposition of different forms of income taxation.

Attachment F

From: Dave Clark [mailto:Dave.Clark@boerio.com]
Sent: Sunday, May 09, 2010 2:56 PM
To: Loretta King
Cc: Shirley K. Sicilian
Subject: Comments to Proposed Model Mobile Workforce Withholding and Individual Income Tax Statute

Ms. Shirley Sicilian, Hearing Officer
Multistate Tax Commission

Dear Ms. Sicilian:

I am concerned that the reference to Section 416(i) of the Internal Revenue Code at Section (2)(e) of the Nonresident Compensation, Exclusion section of the Model Statute is overly broad.

I participated in the conference call at which this reference was discussed. My understanding was that the reference to the Internal Revenue Code (IRC) for this purpose was intended to provide an administratively convenient cross-reference to capture "key employees." After some discussion, the final reference was to Section 416(i) "without regard to ownership," which effectively omitted Sections 416(i)(1)(A)((ii) and (iii) from the definition of key employee for this purpose. Therefore, the key employee definition included officers having annual compensation greater than $130,000, adjusted for inflation.

However, Section 416(i)(3) treats certain self-employed persons as employees for this purpose. As Section 416(i)(3) was not specifically excluded from the final definition in the Model Statute, I belive the final definition would include numerous individuals who are officers in LLCs, LLPs, partnerships, etc. and receiving earned income greater than $130,000 (adjusted for inflation). I do not believe that was the intent expressed on the conference call in which I participated. I thought the exception at Section (2)(e) was intended to include certain highly paid officers of major corporations. As written, I believe it would apply to a much broader and larger group than that.

My suggested "fix" would be to add language along the lines of: ", without regard to Section 416(i)(3) regarding self-employed individuals" at the end of Section 2(e).

Respectfully submitted,

David Clark

Attachment G

MULTISTATE TAX COMMISSION

Working Together Since 1967 to Preserve Federalism and Tax Fairness

Model Mobile Workforce Withholding Statute
Income & Franchise Tax Uniformity Subcommittee
Policy Checklist showing Subcommittee Direction
As of March 22, 2010

I. Application of the Rule:

A. Should the rule address (1) the employee's responsibility to file (i.e., the state's exercise of jurisdiction), and thus obviate the employer's responsibility to withhold, or (2) only the employer's responsibility to withhold, and leave open the employee's responsibility to file?

- **A filing exemption should be provided for non-resident employees whose only connection to the state is employment related activity that falls below a certain de minimus threshold.**

- **Under the draft model, an employer should be relieved of responsibility to withhold wage income for an employee whose employment related activity falls below the de minimus threshold**.

B. Should the rule address local, as well as state, income tax withholding?

- **The draft model should address state income tax withholding. Inclusion of local income tax withholding under the same rule should be optional.**

C. Should the rule include a reciprocity provision to encourage enactment?

- **A reciprocity provision should be included**

- **The draft model should explicitly preserve existing reciprocity agreements**.

II. Specifics of the Rule – the threshold:

A. Should the threshold be stated in terms of:
   1. Time?

- **The threshold should be based on time.**

a. The number of days the employee is present in the state – 10, 30, 60?

- **The threshold time should be 20 work days.**

b. How should a "day" be calculated?

i. Preponderance of a day or any part of a day?

- **Any part of a day should count as a day. If the employee works during a single day in more than one non-resident state, each non-resident states recognizes one day.**

ii. Include travel time to, away from, and/or through, the state?

- **An employee is not present in a state if his or her presence is purely for purposes of transit through the state.**

2. Income?
   a. Only income subject to withholding or including income from other sources, such as intangibles and real property?
   b. Only such income as is attributable to the state or all such income?

- **The draft model should not include a specific income threshold.**

3. Some combination of both? (e.g., no requirement to withhold if employee is in the state for less than 10 days AND has/had wage income below $100,000/year)

- **The de minimus threshold should be stated in terms of time only, with an exception that would generally include high-income employees. See Policy Question II.B.**

B. Exceptions?
   1. Professional entertainers?

- **The draft model should include an exception to the de minimus time threshold for professional entertainers, including actors/actresses**

2. Professional athletes?

- **Yes, the draft model should include an exception to the de minimus time threshold for professional athletes and members of a professional athletic team.**

3. Certain public figures?

- **Yes, the draft model should include an exception to the de minimus time threshold for certain public figures.**

4. Others?

   - **An exception should be added to generally include persons who meet the definition of "key employee" under IRC § 416 (i), without reference to the ownership criteria, whether the employer is public or privately held.**

   - **An exception should be added for construction workers.**

III. Scope of the Rule – beyond the threshold?

A. Should the rule address wage income sourcing? If so,
   1. should the wage income sourcing rule apply only for determining whether the threshold is met, OR
   2. for determining both whether the threshold is met and where the income is attributable for withholding and personal income tax purposes? If the latter,
      a. If an employee is present in a state, but the threshold is not met, should the income that would otherwise be attributed to the state of presence be attributed instead to the state of residence or to the state that is the base of employment?
      b. Other issues?

   - **No.**

B. Should the rule address issues of evidence?
   1. Should the rule specify which records will (or may) be relied upon (employee, employer, or both)?
   2. Other?

   - **Yes. A safeharbor from penalties should be provided. The safe harbor should allow the employer to rely on (1) a time and attendance system, (2) employees travel records, or (3) employee travel expense reimbursement requests – in that order.**

C. Should the rule address (or explicitly state that it does not address) issues of employer nexus for either withholding or any other business tax?

   - **Yes.**

111TH CONGRESS
1ST SESSION

H. R. 2110

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

IN THE HOUSE OF REPRESENTATIVES

APRIL 27, 2009

Mr. JOHNSON of Georgia (for himself, Mr. JORDAN of Ohio, Mr. GOODLATTE, Mr. BUTTERFIELD, and Ms. FOXX) 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 to tax certain income of employees for employment duties performed in other States.

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".

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

(a) IN GENERAL.—No part of the wages or other remuneration earned by an employee who performs employ-

ment duties in more than one State shall be subject to income tax in any State other than—

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

(2) the State within which the employee is present and performing employment duties for more than 30 days during the calendar year in which the income is earned.

(b) WAGES OR OTHER REMUNERATION.—Wages or other remuneration earned in any calendar year are not subject to State 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 earned as of the commencement date of duties in the State 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 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.—

(A) An employee will be considered present and performing employment duties within a State for a day if the employee performs the preponderance of the employee's employment duties within such State for such day.

(B) Notwithstanding subsection (d)(1)(A), if an employee performs material employment duties in a resident state and one nonresident

state during one day, such employee will be considered to have performed the preponderance of the employee's employment duties in the nonresident state for such day.

(C) For purposes of subsection (d)(1), the portion of the day the employee is in transit shall not apply in determining the location of an employee's performance of employment duties.

(2) EMPLOYEE.—The term "employee" shall be defined by the State 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 for wages or other remuneration on a per-event basis, 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 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 in which the duties are performed.

(7) STATE.—The term "State" means each of the several States of the United States.

(8) TIME AND ATTENDANCE SYSTEM.—The term "time and attendance system" means a system where the employee is required on a contemporaneous basis to record his work location for every day worked outside of the state in which the employee's duties are primarily preformed and the employer uses this data to allocate the employee's wages be-

tween all taxing jurisdictions in which the employee performs duties.

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

SEC. 3. EFFECTIVE DATE.

This Act shall be effective on January 1, 2011.

○

From: Bucks, Dan
To: Compact Members & Alternates;
cc: Shirley K. Sicilian; Joe Huddleston; Gregory S. Matson;
Subject: Comments for MTC Exec. Committee Meeting RE: Model Mobile Workforce Withholding and Individual Income Tax Statute
Date: Friday, May 21, 2010 7:36:28 PM

Dear Colleagues,

I have prepared the following observations for the MTC Executive Committee meeting on Monday, May 24, 2010. I would hope you or your designee would have an opportunity to review these comments. Thank you.

The current MTC mobile workforce proposal would begin an unfortunate process of undermining the source principle of taxation—the principle that persons and businesses earning income in a state should help pay for the public services from which they benefit by reporting that income and paying taxes to that state. For decades, the source principle has trumped the residency principle when the two conflict. The reason that the source principle takes precedence over the residency principle is at least two-fold:

1. It achieves fundamental equity and order in the division of income among the states by matching the reporting of income to the state that supplied the services that supported the earning of that income, and
2. In practice, it helps reduce the gaming and manipulation of the income tax system by those who would seek to artificially shift income to states other than where the income was earned.

The MTC draft proposal initiates a risky process of undermining the source principle of income taxation by

1. Establishing a physical presence threshold for income taxes that is subject to manipulation,
2. Reversing taxing priority among states by requiring a priority for residency taxation over source taxation in certain circumstances including assigning a priority for non-income states over income tax states, and
3. Allowing an employee to avoid income taxes in a state even though they work there for more than 20 days by allowing the person's employment to be shifted among related party employers (i.e. the proposal does not require aggregation of employment by several employers, including by jointly owned or managed businesses).

Income tax states already face problems with false or manipulated claims of residency in non-income tax states by persons seeking to avoid income taxes. Recent cases pursued by the Montana Department of Revenue with respect to persons making false residency claims in Nevada have involved hundreds of thousands of tax dollars in each case. The draft proposal will only provide greater incentives for persons and their employers to improperly avoid taxes otherwise due the states in which they are earning income—through false claims of residency in non-income tax states, dividing days of working in a state among multiple, related employers and resisting the production of documentation of employee presence in a state. The result will be increased non-compliance by non-residents with state income tax laws and an improper reduction in the tax base of income states.

States seeking to counter these negative effects on their legitimate tax base will, under the draft proposal, face greater costs and burdens and diminished effectiveness of their compliance activities designed to ensure that non-resident persons pay the correct amount of tax to each state. This proposal creates this increased burden for state taxing authorities because instead of administering a simple income threshold, states will now need to administer a dual test—both an income threshold and a "20 working days in the state" test. The latter will function as a higher hurdle over which states will need to jump. The current income threshold test is more easily administered by states because it is supported by considerable third party income reporting and exchange of information systems among states and the IRS. However, there is no established third party reporting and exchange of information system among tax agencies for employee travel data. Further, the draft proposal does not establish a sufficiently robust system of reporting to support effective and compliance with

its terms. States cannot rely for this information upon the consistent cooperation of the non-resident or their out-of-state employer who also may be out of compliance with the state's withholding tax system and may be enabling the non-resident employee's tax avoidance. Consequently, states engaging in non-resident compliance efforts will find these activities to be more costly and less effective.

Montana does not have data from other states on their non-resident compliance efforts. However, our experience over the last five years indicates that non-residents have very high non-compliance rates—extending up to 70% or more. They may well outnumber the compliant non-residents. Further, about half of those who are initially identified as non-compliant refuse to respond to any communications short of formal legal action. While we have had productive results in non-resident compliance, this area is already complex and challenging. The MTC draft proposal will, in our judgment, seriously damage these important compliance efforts and harm our resident taxpayers.

The MTC draft proposal also has the unfortunate effect of creating an exemption from source state taxation that is of greater value in dollar terms the higher the income of the non-resident. Higher income non-residents would be favored as compared to lower income employees regardless of residency. There is no clear justification for this inequity—which can be further amplified by the means of tax avoidance previously described.

Finally, the MTC draft proposal provides a road map for federal imposition of physical presence requirements on the states. It makes no difference if the physical presence requirements are expressed as filing thresholds or nexus standards. Either way, federal imposition of physical presence requirements will seriously unbalance the tax systems of many states by undermining source taxation of out-of-state businesses and non-residents earning income within their borders. The result will be to unfairly shift the cost and burden of providing services required by those who enter a state from outside to in-state residents and businesses.

The MTC has throughout its history been the primary institution supporting the effective application of the source principle of taxation. As a key component of source taxation, the MTC has advocated economic measurements, as opposed to physical measurements that can be more readily manipulated, as the thresholds for the imposition of state taxes. Economic standards best ensure equity in the division of income among the states and between the taxes borne by out-of-state and in-state participants in a state's economy. These economic measures will only be implemented by the state's themselves, because large multistate and multinational enterprises have no interest in their federal imposition. Unless the MTC remains true to its principled history of supporting economic measures over physical ones, the future prospects of equitable taxation based on the proper implementation of source taxation will diminish greatly. Now is not the time for the MTC to lose either its way or its voice. This proposal should be returned to the Uniformity Committee so that it can be reformulated to strengthen and not weaken the application of the source principle of taxation.

Dan Bucks
Director of Revenue
State of Montana