June 10, 2010 Montana Proposal for Model Withholding

Individual Income Tax Simplification for Multistate Wage Earners

Easy, Electronic Determination of Filing Responsibilities for Multistate Wage Earners: The MTC (and ideally partner with the FTA in doing so) would establish a multistate wage-earner web site with a calculator for individuals who worked in more than one state to quickly and easily make the once a year decision to file tax returns in another state. The calculator would enable a citizen to type in number of days in the state and rate of pay. The calculator would then tell the citizen "yes" or "no" if they needed to file a return in that state (based on each state's filing threshold). The web site for the calculator would then link to the income tax pages of each state so that the citizen can get more detailed forms and filing information.

The calculator would also be made available on or linked to on each state's web site and could be licensed to tax preparation software vendors. The MTC (and FTA if a partner) would be responsible for verifying and certifying the accuracy of the threshold information and the calculator on an annual basis.

Because the calculator would provide a simple "yes" or "no" answer to the citizen based on simply days in a state and rate of pay information, the citizen would not need to have any knowledge of the actual thresholds in each state (although that information could be made readily available for those wishing to know). Thus, there would no longer be a need for uniform threshold legislation among the states. This electronic service is actually simpler and more effective in providing citizens with direct and specific income filing guidance than uniform thresholds. So it provides better simplification with less interference with the tax policy prerogatives of each state.

Finally, taxpayers will benefit more quickly under this proposal because implementation of this simplification can proceed in a very short time period. It is not dependent on states taking legislative action to enact uniform thresholds. The proposal would be implemented administratively beginning with states that have either income or day thresholds for the imposition of their income taxes. Other states would be added as they certify their income or day thresholds to the MTC.

Tax Threshold: States would maintain their own individual thresholds based on either income or days in the state. The MTC would recommend that states without an income or days in the state threshold establish by law or rule such thresholds to participate in the national web site.

Record Keeping Guidance: The MTC will recommend a model guideline, taxpayer instruction or rule on common record keeping standards and advice for taxpayers who work in more than one state. The focus would be on advising time and rate of pay records and helpful documentation. Information on the record-keeping guidance from each state would be maintained on the multistate worker web site.

Preserve Source State Tax Priority: There will be no implicit or explicit reversal or erosion of tax priority as between source states and residency states. Source states will have first priority on the reporting and payment of taxes on income.

Withholding Tax Simplification for Employers

Decision on Income or Days in State Test: Provided that other key features of this proposal are adopted by the MTC, the MTC would recommend to the states the adoption by law or rule of an de minimis threshold for withholding taxes for an individual employee of 20 working days in a state. The use of the 20 working days test is specifically contingent on the absence of any changes from current law in income tax priority among the states or the right of each state to determine their own income tax imposition thresholds, the aggregation of employment service data among related parties, and an adequate employer reporting system for all employees working in multiple states.

Aggregation among Related Parties: The determination of whether "20 working days in a state" threshold is met by an employee will be made on a basis that aggregates the data for each employee among related party business entities.

This provision is essential to ensuring the proper accountability in the administration of the threshold, to preventing evasion, and supporting the integrity of the process.

Withholding Tax Exemption Process with Reporting Requirements: The employer exemption from withholding a host state's tax from paychecks and paying those amounts to a host state will be an exemption for which the employer will apply annually. This exemption will be intended for use by those employers that have plans to send employees into a state during the year, but the employer does not believe the presence of at least some of their employees will exceed the designated withholding thresholds. The benefit of the exemption will be to relieve the enterprise of withholding a host state's taxes from their employees and paying those amounts to the host state. To ensure accountability and prevent evasion, the exemption would not relieve the employer of certain periodic reporting responsibilities.

The annual application would include all related parties of the business entity making the application. It will include a declaration that the entity and their related parties may send employees into the state, but they do not anticipate that one or more employees will exceed the withholding threshold. The application will include a listing of all related parties, FEIN #s and all corporate officers of the entity and their related parties (the latter is to enforce the common withholding enforcement provision of officer liability for unpaid taxes) .

The exemption requirements will include an agreement by the entity to file periodic reports with the names and SSNs of employees that worked in the state and the data on either the number of days or the earnings of the employees attributed to them. As long as the thresholds are not met, however, there will be no taxes withheld or paid to the host state. This exemption ceases during the year with regard to any employee who exceeds the threshold during the year.

The business will commence withholding for those employees exceeding the threshold—but only those employees. The tax to be withheld will be only with respect to wages earned after the threshold was met by an employee and not with respect to prior wages.

If an entity fails to report as agreed to, the entity will be required to withhold taxes on all employees working in the state regardless of their work status with respect to the threshold. The model statute will also impose penalties for failing to report.

The other provisions previously developed in the Uniformity Committee's proposal with respect to employees not eligible for the withholding exemption would continue to apply and would be retained.

Other provisions in the original Uniformity Committee proposal that are determined to not be in conflict with the income tax and withholding exemption framework described in this proposal would also be retained.