State and Local Taxes Update

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Remote Working Agreements

Working Remotely

- More people in the United States are working remotely

- What's the big deal?
  - Nexus
  - Additional Filing Requirements

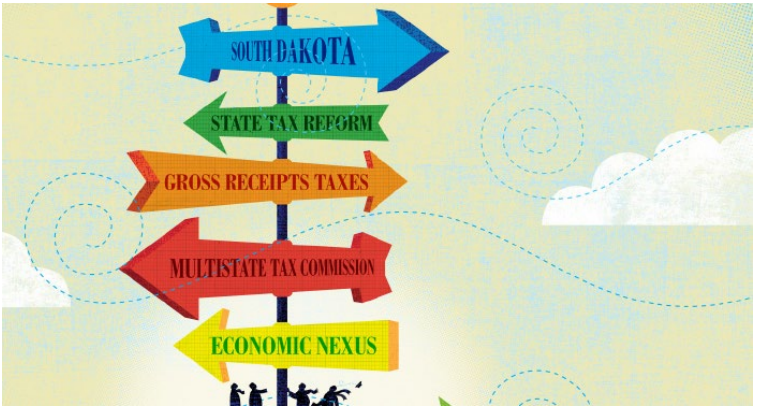
Nexus – What is it?

- A situation in which a business has tax presence in a particular state
- A connection between the taxing authority and an entity that must collect or pay the tax.
- How nexus can be created:
  - Income from sources within state
  - Owning or leasing property
  - Employees working within state
  - … and so much more!

Working Remotely and Nexus

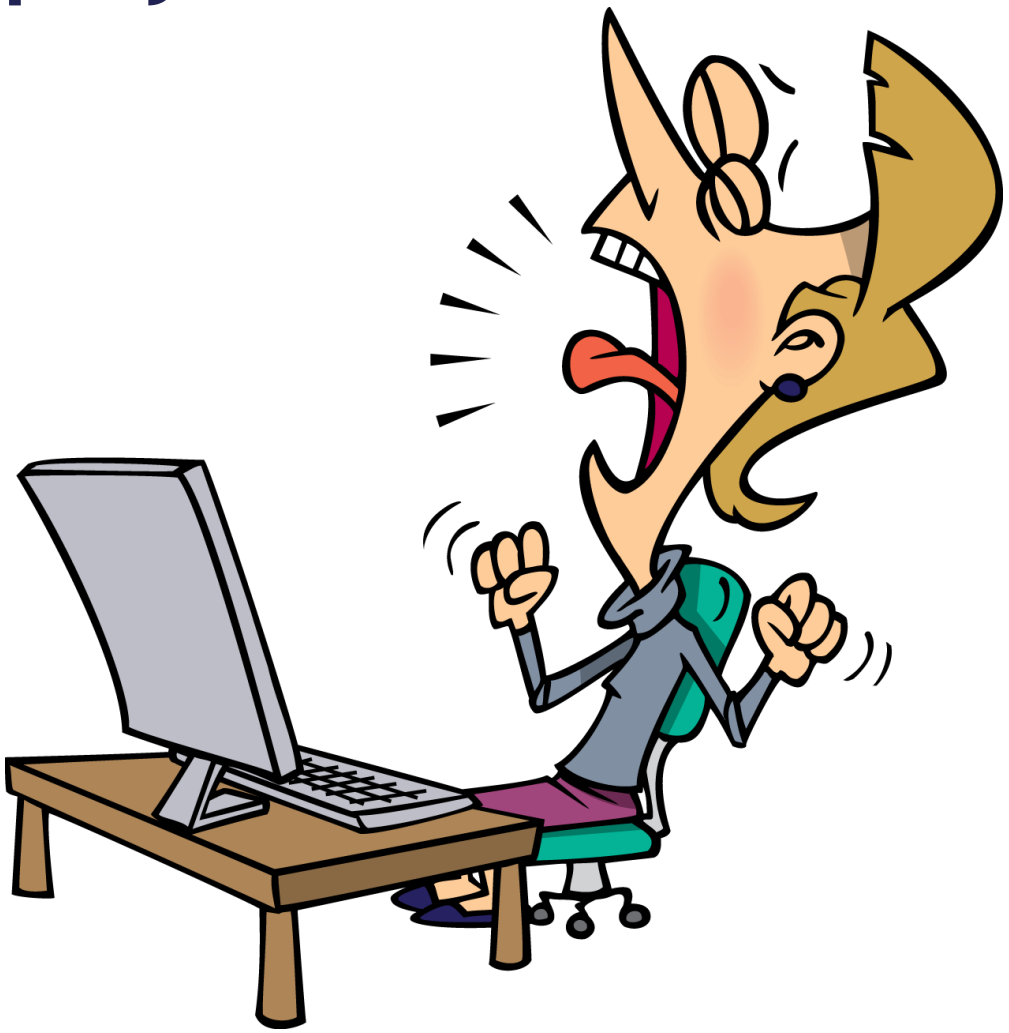
- Employees working in different states could potentially cause nexus

- Does the employee have a company owned laptop used for work?
  - Now you have property located in a new state



How will this affect employers?

- Potential filings in new states:
  - Register to do business
  - Income Taxes
  - Wage Withholdings



State Guidance

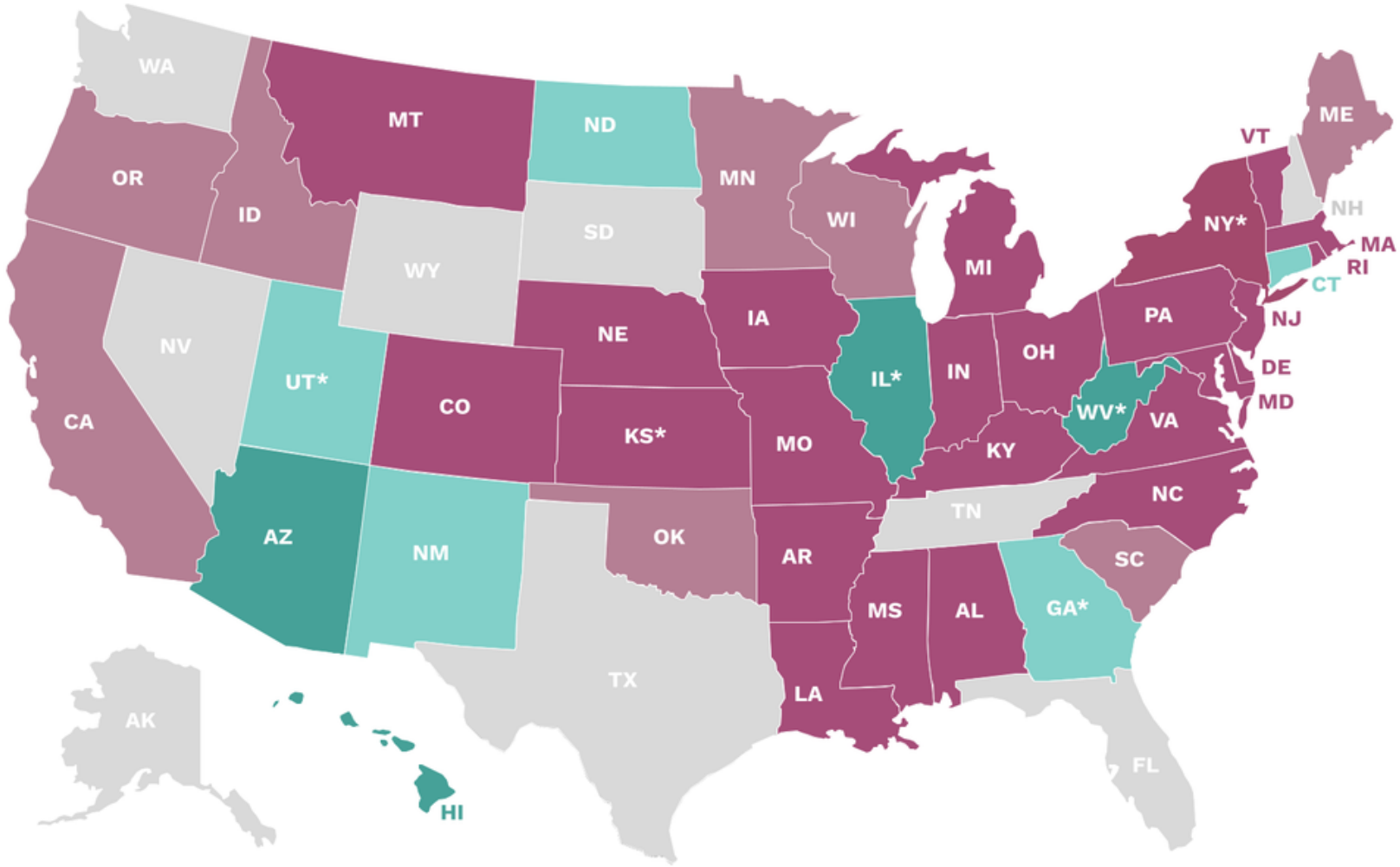
- Some states have provided guidance
  - AL, CA, CT, DC, GA, IN, IA, MA, MD, ME, MN, MS, ND, NJ, OR, PA, RI, SC, WI have waived nexus for businesses with remote employees during the pandemic or active official stay at home orders.
- However, if teleworking is the new norm, any temporary nexus waivers will not provide protection.

State Guidance

- Does your state have reciprocal agreements with other states?
  - If an employee had principally worked in a state other than their home state but is working from their home state due to the pandemic, there is no change to withholding from employment income if the states have a reciprocal agreement allowing the home state to have tax authority regarding withholding.
- In the absence of guidance providing an exception to a state's nexus position due to teleworking, businesses should assume an unchanged nexus standard

Which states are the most friendly to mobile workers and their employers?

- **Very Friendly.** State allows employees to work within the state for 30 or more days before employer is subject to withholding (AZ, HI, IL, WV).
- **Moderately Friendly.** State allows employees to work in the state between 15 and 29 days before employer subject to withholding (CT, GA*, NM, ND), or has other accommodating provisions (UT*).
- **Unfriendly.** State only allows employees to work in the state between 2 and 14 days before employer is subject to withholding (ME), or has a wage-based threshold (CA, ID, MN, OK, OR, WI).
- **Very Unfriendly.** State requires employer withholding on first day an employee works within the state (24 states), or requires an individual to file on first day even if employer isn't required to withhold on first day (NY).
- Not applicable. No state income tax.



Notes: Data as of May 2021. In **Georgia**, employer must withhold if the employee is in the state for more than 23 days in a calendar year, or if $5,000 or more or 5% or more of total income is attributable to Georgia. In **Illinois**, the 30-day threshold applies for tax years beginning after December 31, 2020 (this is the result of legislation enacted in 2019). **West Virginia** lawmakers enacted HB 2026 in 2021, imposing a 30-day threshold. This takes effect on June 28, 2021. In **Utah**, employer must withhold if the employer (not the employee) does business in the state for more than 60 days in a calendar year. ***Kansas** considered 30-day legislation in 2020.

Failure to Comply

- Penalties vary from state to state:
  - Failure to report employee to new state
  - Failure to withhold
  - Failure to file
    - In addition to back taxes and fees + interest

Employer Responsibility

- Do you know where your employees are working?
  - Ask them
  - Send surveys
  - Use IP address used to connect to company system
- Do you know how long they plan on working remotely?
  - Safe harbor rules exist

SALT Deduction Cap Workaround

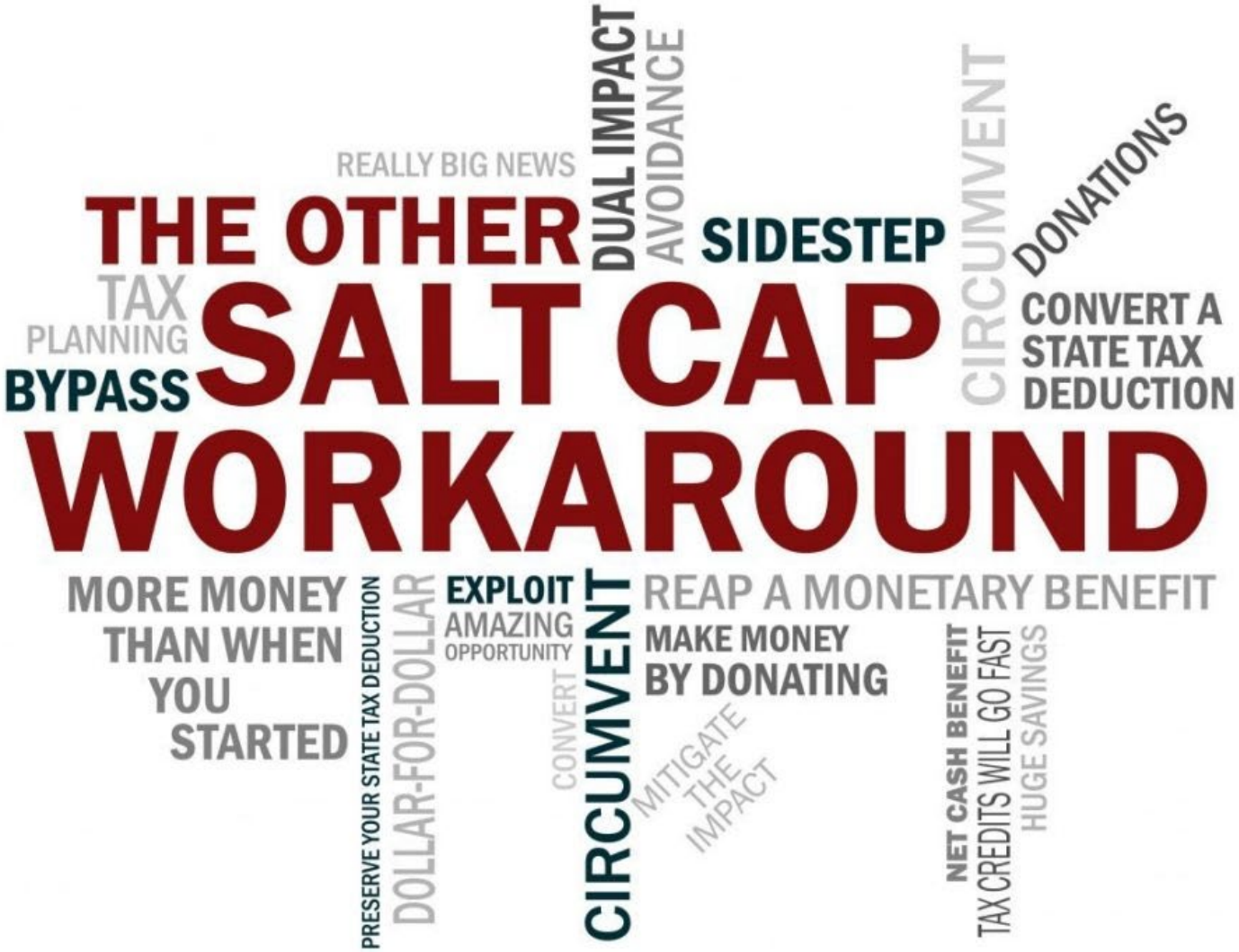
SALT (State and Local Tax) Deduction

The state and local tax deduction authorizes taxpayers who itemize when filing federal taxes to deduct specific taxes paid to state and local governments.

These taxes include:

- Property and real estate taxes
- Personal property taxes
- Income taxes
- General sales taxes

Under the Tax Cuts and Jobs Act, individual taxpayers can deduct a maximum of $10,000 in state and local income taxes on their federal income tax return for taxable years 2018 through 2025.


REALLY BIG NEWS
THE OTHER
DUAL IMPACT
AVOIDANCE
SIDESTEP
CIRCUMVENT
DONATIONS
TAX
PLANNING
BYPASS
SALT CAP
CONVERT A
STATE TAX
DEDUCTION
WORKAROUND
MORE MONEY
THAN WHEN
YOU
STARTED
PRESERVE YOUR STATE TAX DEDUCTION
DOLLAR-FOR-DOLLAR
EXPLOIT
AMAZING
OPPORTUNITY
CONVERT
CIRCUMVENT
REAP A MONETARY BENEFIT
MAKE MONEY
BY DONATING
MITIGATE
THE
IMPACT
NET CASH BENEFIT
TAX CREDITS WILL GO FAST
HUGE SAVINGS

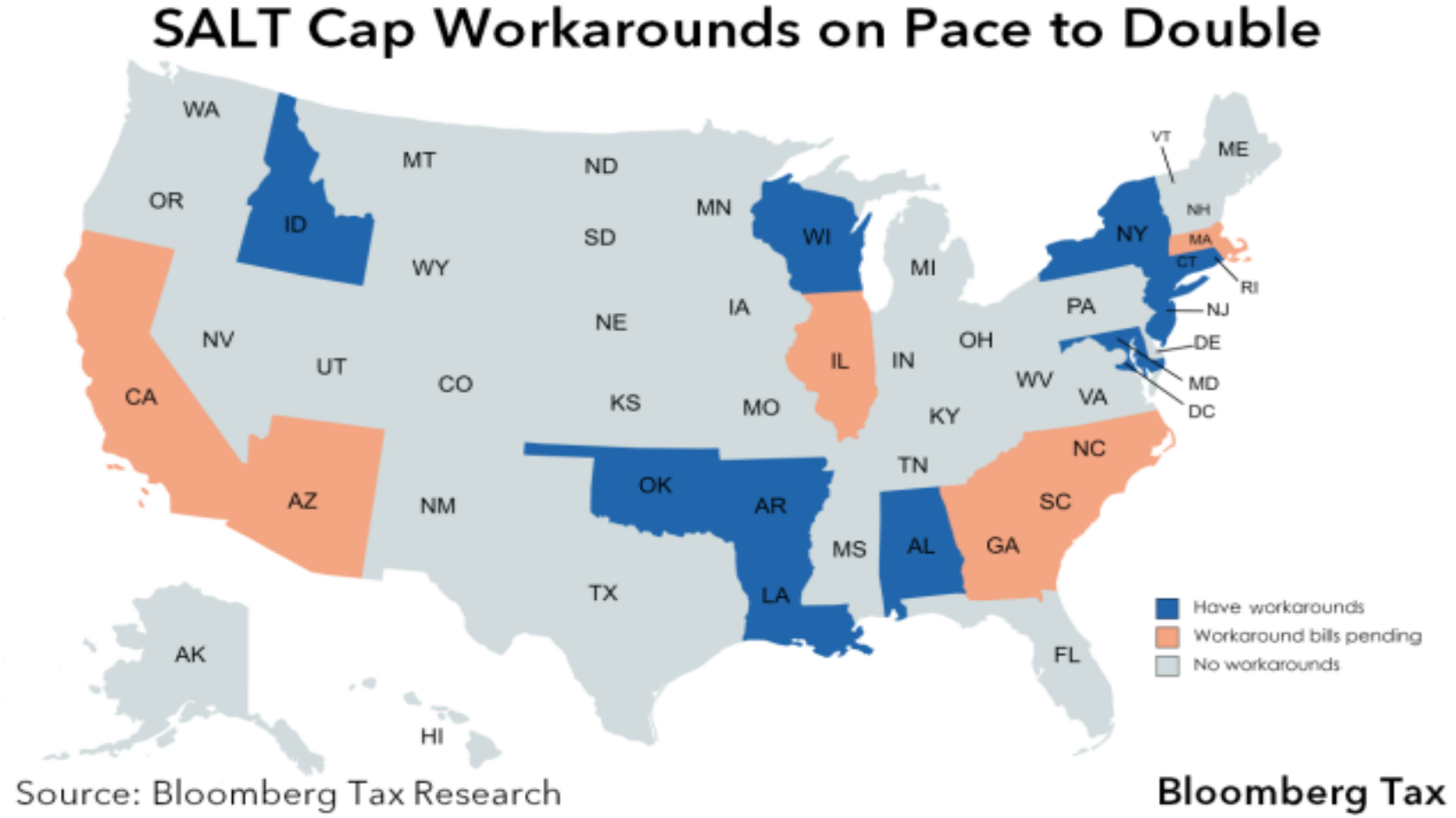
What is a SALT Deduction Cap Workaround?

- Legislation created to bypass, or work around the SALT deduction limitations.
- The workaround essentially applies to taxpayers that receive passthrough income.
- Enables pass-through entities (PTE) to deduct entity-level SALT payments as a business expense in place of non-deductible itemized deduction over the limited SALT cap.

How does the SALT Deduction Cap Workaround work?

- As there is no SALT deduction limit at the entity level, the workarounds allow businesses where income is taxed at the individual owner level to pay a partner's tax at the entity level in exchange for an equal tax credit. Partners can then use those credits to avoid the $10,000 cap on state and local deductions.

States that have enacted the SALT Cap Workaround



States that have enacted the SALT Cap Workaround

So far 20 states have enacted this legislation, other states are in consideration:

- Alabama, Arizona, Arkansas, California, Colorado, Connecticut, Georgia, Idaho, Illinois, Louisiana, Maryland, Massachusetts, Minnesota, New Jersey, New York, Oklahoma, Oregon, Rhode Island, South Carolina, and Wisconsin.
- Connecticut is the only state that requires a PTE tax; the rest are elective.
- Other States under consideration: Michigan and Ohio.

Who Qualifies?

Qualified entities include:

- Partnerships
- S Corporations
- Limited liability companies with multiple members treated as a partnership

Disqualified entities include:

- Pass-through entities that have a partnership or a disregarded entity as an owner publicly traded partnership
- Entities that are permitted or required to be in a combined reporting group

Who benefits most from the SALT Cap Workaround?

- States with high earners like NY and CA

- High income taxpayers with high property and state income tax

Current SALT negotiations

- Currently, a plan is being negotiated to lift the 2017 SALT cap tax laws for many taxpayers, while keeping it in place for high income earners.
- The proposition is to exclude the highest earning households from the proposed SALT benefit.
- Proposed income threshold to write off all state and local taxes for singles earning up to $550,000 (joint fillers $1,100,000)

Nexus Studies

What is a Nexus Study, and when should it be considered?

- A nexus study documents your business activities in a state or states, and whether (and why) they do or do not create nexus.
- If you are considering to register in a new state – a nexus study should be performed
- The study should address all tax types:
  - Sales Tax, Income Tax, Franchise Tax, and Gross Receipts Tax
- Physical presence will usually override economic nexus rules

Nexus Study Approach

- Nexus studies can be overwhelming for clients
- Use a phased Approach
  - Start with largest states first

What to do once additional states are identified?

- Calculate risk of not filing in prior periods for Sales Tax and Income Tax
- Voluntary Disclosure vs Prospective Filing

Pros and Cons - VDAs

- PROs
  - Limited exposure, tax liabilities, and penalties
  - VDA negotiation is often anonymous
  - Opportunity to “come clean” and get right with the state when you realize a mistake
- CONs
  - Any missing details can void the VDA or result in ineligibility
  - States have varying requirements for VDAs
  - Additional tax liabilities may be uncovered

Nexus Studies are not a one and done deal

- Clients should have a nexus study every year at a minimum
  - Identifies any new states that you need to register and start filing in
  - Also identifies states where you may decide to withdraw from

Questions?

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