

PUBLICATION

Navigating COVID-19: Tax Nexus, Withholding Taxes, and State Unemployment Taxes

September 9, 2020

COVID-19 has caused many companies to introduce or expand a remote work policy for employees, either in a temporary capacity or in a more permanent one. With a large number of companies' employees working remotely, several important tax issues need to be considered and addressed. Baker Donelson's Tax attorneys have fielded numerous calls from companies, as well as accountants and other professionals, to address these concerns. Three of the most significant issues include income tax nexus, withholding taxes, and state unemployment taxes.

Income and Other Tax Nexus

It is not uncommon for an employee to live in one state (State A) but work in another state (State B) where a business has its office(s). If that employee now works remotely from home (in State A where the company does not have a physical office), does the company now have an "office" in State A or "employees working" in State A? The answer to that question may determine whether State A's taxing agency will assert nexus over that company, thus possibly creating an income and/or other tax filing requirement. Several states have put forth guidance that provides that temporary remote work situations will not be considered for a potential tax nexus, however, as many companies move forward with plans for permanent remote work options, this tax nexus implication must be further analyzed.

Withholding Taxes

Withholding taxes refers to the taxes (income tax, Social Security, Medicare, etc.) that are withheld from employee wages and remitted to the IRS and/or applicable state taxing agencies. For remote work situations, the analysis focuses on the state income taxes that an employee may owe. An employee who resides in State A but works in State B may have filing requirements and be liable for income taxes in State A, State B, or a combination thereof. Each state has its own tax statutes and regulations, and potentially reciprocity agreements with other states, so each employee and company situation must be analyzed individually. Employers generally withhold and remit taxes based on the information provided by the employee on IRS Forms W-4 and the relevant state forms, however, employees are seeking advice from company HR departments regarding their specific circumstances.

State Unemployment Taxes

Employers are responsible for filing and paying unemployment taxes to states. Each state has its own set of statutes and regulations, but there is typically a hierarchy of "tests" that an employer must use to determine in which state to file and pay unemployment taxes on behalf of each employee. Onerously, this must be done on an employee-by-employee basis and may change if an employee's work scenario changes (i.e., works from home, travels regularly for work, etc.). This is an especially hot button issue as employers have laid off or furloughed employees and/or switched to on-going work-from-home options. Employers need to carefully analyze these situations as they can be liable for significant unemployment taxes if returns and taxes are not paid to the correct state.

It is important for employers to carefully review these issues during times of change within the company. The tax team at Baker Donelson monitors on-going State and Local Tax developments to provide up-to-date

guidance to employers during these difficult times. For more information on this please contact any member of the [Baker Donelson Tax group](#).