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New York State Taxation of Telecommuters

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A familiar story, heard over and over again during this past year, involves people who used to live and work in New York but moved out of state once the pandemic hit. The decision to move out of state was made easier as many employers allowed or required employees to telecommute.

Similarly, nonresidents of New York State who physically commuted to New York pre-COVID could now avoid entering the state to work due to the increased availability of telecommuting. At tax time, the questions to ask are (1) whether any tax is owed and payable to the state of New York; and (2) if so, how much?

Due to the increased financial pressures that have accompanied this pandemic, New York State taxpayer residency and telecommuting-related audits will most likely increase significantly. Residency rules are complicated, and auditors will look at multiple factors in making their assessment, making it important for taxpayers to consult with an experienced tax professional.

New York's Telecommuting Rules

Taxpayers who live and work in different states may be subject to taxation in more than one state. For taxpayers who physically commute from one state to another, it is clear in which state they are "working." How taxpayers will be taxed on wages earned depends on the rules of the state(s) where the taxpayer resides and works.

While this is not a new issue, the rise in telecommuting due to COVID-19 has raised new questions and novel complications for many taxpayers. Various factors affect the determination of whether taxpayers are considered to have worked "in-state" and thus are subject to taxation for wages earned.

In New York, if a taxpayer is a nonresident but their primary business office is located in New York, telecommuting days are still considered "days worked in the state." Accordingly, the taxpayer will continue to owe New York State income tax on that income even though the taxpayer was physically working outside of New York.

However, if the employer specifically acted to establish a bona fide employer office at the taxpayer's telecommuting location, the taxpayer will not have a tax obligation to New York State from wages earned while working from the bona fide office.[1] Under the law, the question becomes what constitutes a bona fide employer office?

New York State outlines several factors to provide some clarity. A taxpayer must prove the existence of either (i) the primary factor or, in the alternative, (ii) four of the six secondary factors and three of the ten tertiary or other, factors. Most taxpayers will not fall under the primary factor and instead must resort to a combination of secondary and other tertiary factors to avoid taxation.

Primary, Secondary, and Tertiary Factors Explained

The primary factor in determining whether a location is a bona fide employer office is whether the home office contains or is near specialized facilities. If the employee has duties that require special equipment or facilities that cannot be performed at the employer's place of business, but such facilities are available near the taxpayer's home, the home will qualify as a bona fide employer office.

The primary factor is usually clear-cut. For example, an employee who must visit a racetrack to test automobiles or work in a laboratory located near certain samples would certainly qualify. The secondary factors, by contrast, may appear straightforward, but they can be complex.

Secondary factors that are considered include the following:

1. The home office is a requirement or condition of employment.
2. The employer has a bona fide business purpose for the employee's home office location.
3. The employee performs some of the core duties of his or her employment at the home office.
4. The employee meets or deals with clients, patients, or customers on a regular and continuous basis at the home office.
5. The employer does not provide the employee with a designated office space or other regular work accommodations at one of its regular places of business.
6. The employer reimburses expenses for the home office.

Please note that four of these six factors must be satisfied in order to avoid New York State tax liability.

The home office requirement above may seem employee-friendly, especially during COVID-19 since employers were mandating that employees work from home. However, it is not enough that employees are required to work from home because they could also technically work from anywhere. The real issue is whether the employee must work from a certain geographic location.

When conducting an audit, New York State will look to find any reason to consider the taxpayer to be assigned to a New York work location. Therefore, it is essential for taxpayers to maintain documentation showing that their work location must be in their home state and that they have consistently worked from that location.

The secondary factor of meeting or dealing with others regularly and continuously from a home office also appears very taxpayer friendly on its face. Most employees are all too familiar with Zoom meetings with both co-workers and clients from their home office over the past year. Unfortunately, virtual meetings do not satisfy this factor.[2]

Taxpayers must also show three out of ten tertiary or other factors. These include showing that the employee uses a separate phone line and office space solely for business purposes; inventory or business records are stored in the home office; or the home office location is listed on the business letterhead or in advertising materials, among others.

The difficulty in establishing the secondary and tertiary factors means that it is likely that many employees who were merely telecommuting from another state during the pandemic will be considered as working from New York for tax purposes. As a result, they will be required to pay New York State income tax for tax year 2020.

New York Residency Issues

Another twist for taxpayers who relocated out of New York due to the pandemic involves whether they changed their residency for tax purposes. For instance, let's take a common fact pattern: a couple lived in an apartment in New York City and worked in the city as well. In March 2020, they decided to leave the city and telecommute to work from a residence in New Jersey due to COVID.

In November 2020, the apartment lease in the city expired and they decided not to renew. They continued to telecommute from their New Jersey residence. Several questions are raised as a result: Where should they be taxed? Did they change their domicile to New Jersey? If so, when did the change of domicile occur?

Generally, if the couple's intent was to leave New York permanently and change domicile to another state, then they are no longer considered New York State residents for tax purposes. However, as a non-resident (or part-year resident) telecommuter, it is important to note that the taxpayer may still owe taxes to New York on wages earned in New York. Some states may offer credits for taxes paid to New York State.

Importantly, auditors for New York State will be looking closely at those who changed their residency during COVID to check whether or not the move was permanent.[3] Taxpayers who subsequently move back to New York or engage in other activities in New York may be adjudged to have only made a temporary move out of state. If this is so, they will be deemed New York residents throughout the entire period and all income, wherever earned, would be subject to taxation by New York.

Conclusion

Due to the increased financial pressures that have accompanied this pandemic, New York State taxpayer residency and telecommuting-related audits will most likely increase significantly. Residency rules are complicated, and auditors will look at multiple factors in making their assessment, making it important for taxpayers to consult with an experienced tax professional.

Attorneys should be prepared to advise clients about how tax laws apply to their situation, not only to reduce audit risk, but also minimize the extent and scope of any audit that does occur.

1. Frequently Asked Questions about Filing Requirements, Residency, and Telecommuting for New York State Personal Income Tax, October 19, 2020. https://www.tax.ny.gov/pit/file/nonresident-faqs.htm#telecommuting.
2. *Id.*
3. Will COVID-19 Affect Your Clients' New York State Tax Residency?," by Karen Tenenbaum, Esq. and Marisa Friedrich, Esq., *Nassau Lawyer*, December 2020.

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