Statement of

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Before the

U.S. House of Representatives

Committee on the Judiciary

Subcommittee on Courts, Commercial and Administrative Law

Hearing on H.R. 1864

The Mobile Workforce State Income Tax Simplification Act of 2011

The Honorable Howard Coble, Chair

May 25, 2011

Chairman Coble, Ranking Member Cohen, and Members of the Subcommittee, I am Joe Crosby, COO & Senior Director, Policy for the Council On State Taxation, which is more commonly known as COST.

COST is a non-profit trade association consisting of nearly 600 multistate corporations engaged in interstate and international business. COST's objective is to preserve and promote equitable and non-discriminatory state and local taxation of multi-jurisdictional business enterprises.

I would first like to thank Chairman Coble and Congressman Johnson for introducing H.R. 1864, The Mobile Workforce and State Income Tax Simplification Act of 2011. I appreciate the opportunity to share with you COST's views on the important issues this legislation addresses: personal income taxes imposed on employees who travel away from their resident states for temporary work periods and the associated tax withholding obligations of their employers.

Widespread Problem

The problem addressed by H.R. 1864 can be simply stated: every business day hundreds of thousands of employees across the country are sent by their employers to work in nonresident states. The vast majority of these trips are temporary in nature, whereby the employee conducts business in the nonresident state for a short period of time and then returns to his/her resident state.

States currently have varying and inconsistent standards regarding the requirements:

- for *employees* to file personal income tax returns when traveling to a nonresident state for temporary work periods; and,
- for *employers* to withhold income tax on employees who travel outside of their state of residence for temporary work periods.

Employees who travel outside of their state of residence for business purposes are subject to onerous administrative burdens because, in addition to filing federal and resident state income tax returns, they may also be legally required to file an income tax return in every other state into which they travel, *even if they are there for only one day*.

The patchwork of inconsistent state laws and rules is shown by the map and chart attached as Exhibit A to my testimony. The challenges imposed upon employees to understand these widely divergent rules, track down the appropriate nonresident state forms and actually comply with this multiplicity of state tax rules is nearly insurmountable.

So too, employers are extremely hard pressed to comply with these varying and disparate rules and provide the appropriate nonresident state withholding. It is important to note that this tax compliance issue affects all employers whose employees travel for work: large and small businesses, charities and other non-profits, and even government agencies.

There is no practical technological solution to this problem. Very few employers, large or small, have the capability to integrate payroll with business operating systems to allow tracking of employees' whereabouts on a daily basis. Employers who have such capability face further challenges in attempting to use such systems to comply with the states' non-resident personal income tax withholding requirements. Employers' compliance with disparate state rules is almost exclusively via manual processes. Because of the current lack of uniformity, the costs of automating such systems would be exorbitant in relation to any compliance gains to the various states.

Simple Solution

The simple answer to this widespread problem is to legislate a federal threshold period of thirty days for temporary employee work assignments to nonresident states. Employees working in nonresident states for thirty or fewer days would remain fully taxable in their resident state for all earnings (to the extent the resident state chooses to have a state personal income tax system). The vast majority of employees who travel outside their resident state for employment purposes would fit within this threshold period. To the extent the employee has duties in the nonresident state for an extended period exceeding the thirty day annual threshold, then the employer would have adequate information to provide accurate withholding of wages to the nonresident state, and the employee would be on notice that the state filing rules must be complied with. This uniform rule would greatly ease compliance for all employers subject to state withholding rules and would provide much greater certainty for employees in fulfilling their personal nonresident state filing obligations.

Uniform Rules are Needed Now

While states' laws addressing nonresident withholding and personal income tax liability have been on the books for many years, resolution of this issue has reached a critical stage for corporations for a number of reasons, most notably the enactment of the Sarbanes Oxley Act of 2002. Under Section 404 of the Act, company management is required to certify that processes and procedures are in place to comply with applicable laws and regulations, including state tax rules. This rule, along with a commensurate desire by corporations to be fully compliant with all rules and requirements as part of corporate governance responsibilities, has increased the interest of business in desiring uniformity and simplicity in matters of nonresident state income and withholding laws.

Furthermore, employers have a significant interest in ensuring that employees comply with all state law taxation requirements. COST members are acutely aware of the burdens placed on their employees who travel outside their resident states for business. They have expressed a strong desire to meet their responsibilities as employers by assuring that their employees comply with these burdens. Unfortunately, the current patchwork of state rules makes it extremely difficult to comply fully.

A Federal Standard is the Only Solution

In a limited manner, some states have resolved the issue of nonresident personal income on a regional basis, typically with adjoining states through bilateral reciprocal agreements. These bilateral reciprocal agreements are helpful in discrete regional situations, but fall well short of solving a problem that is nationwide in scope.

Conceptually, there is no barrier to the states agreeing, in concert, to adopt a single, national standard governing personal income taxes imposed on nonresidents working in a state for temporary work periods. In fact, the Multistate Tax Commission (MTC) may soon approve a model statute that theoretically could provide the basis for such a national standard. Unfortunately, in the area of taxation, there are several historically insurmountable hurdles to achieving a simple system through voluntary state action.

Model state legislation such as that under consideration by the MTC faces a fundamental political challenge in every state in which it might be considered: by definition, the legislation, when considered in any one state, does not benefit those employees living in the state or their employers unless and until another state enacts the same law. Even then, the model statute benefits only those employees who reside in a state that has enacted the law and who are traveling to a state that has also enacted the same law (the MTC model statute is based on reciprocity). Thus, for employees who travel and their employers, there could be no simplification unless and until all states imposing a personal income tax have adopted the model statute. Furthermore, those states would have to adopt the model statute uniformly; in other words, state-to-state deviations from the model statute would significantly diminish, or completely eliminate, the benefits of the model statute. Finally, even if it were possible to achieve voluntary state action, it would require many years, and perhaps decades, to accomplish. Despite initiating discussions with representatives for state tax administrators more than five years ago, and despite a "fast track" process to develop model legislation, the model legislation has still not been approved.

There is not a single example in the history of state taxation in this country to suggest that voluntary adoption by all the states of a model tax statute to promote simplification is achievable.[1] As a result, we believe the only way to secure a nationwide resolution of the issues is to provide a uniform and simple set of rules established under federal guidelines, such as that set forth in H.R. 1864.

[1] There are examples of tax simplification resulting from federal intervention in areas where discussion among the states was already underway. The taxation of motor fuel used by interstate motor carriers is one such example. The International Fuel Tax Agreement (IFTA) began as a voluntary state effort in 1983, and in 1984 federal legislation authorized the formation of a working group that ultimately drafted a model statute to cover fuel taxes on interstate motor carriers. By the end of 1990, eight years after the effort began, sixteen states had joined the IFTA. Uniformity, however, was only achieved after the adoption of the Intermodal Surface Transportation Efficiency Act in 1991, where Congress mandated that states join the IFTA by September 30, 1996 or risk loss of certain transportation revenues.

H.R. 1864 – Explanation of Provisions

First and foremost, H.R. 1864 provides that all wages and other remuneration paid to an employee would be subject to the income tax laws in the state of the employee's residence. In addition, under the legislation wages and other remuneration are also subject to tax in the state in which the employee is present performing duties for more than thirty days in a calendar year, and employers would be subject to commensurate withholding requirements of that nonresident state. The thirty day threshold does not apply to professional athletes, professional entertainers, or certain public figures who, because of their national prominence, are paid on a per-event basis to give speeches or similar presentations. For example, a professional football player would be subject to nonresident state personal income taxes for performance in an athletic event. As another example, a well-known author who is an employee of a speakers' organization would be subject to nonresident state income taxes for making a presentation in a state and receiving compensation based on that event. In both of these cases, their respective employers would be subject to the nonresident state withholding requirements.

An employer may rely on an employee's determination of the time spent in a nonresident state absent knowledge of employee fraud or collusion between the employer and employee. If an employer, however, at its discretion, maintains a time and attendance system tracking where employees perform their services, such system must be used instead of the employee's determination.

An employee will be considered present performing duties in a state if the employee performs the preponderance of his or her duties in such state for such day. If an employee performs material employment duties in only the employee's resident state and one nonresident state during a single day, such employee will be considered to have performed the preponderance of his or her duties in the nonresident state for such day.

The terms "employee" and "wages or other remuneration" are defined by the state in which the employment duties are performed. These references to state law protect the prerogatives of the state, as the overall intention of the legislation is to make the least incursion practicable in current state withholding and personal income tax rules and regulations.

Impact on State Taxes

All states that levy a personal income tax provide residents with a credit for nonresident personal income taxes paid to other states. Thus, at a macro level, the difference between the loss of tax revenue that is currently received by a state from nonresidents is generally balanced by an increase in tax revenue resulting from fewer credits provided to residents for taxes paid to other states. I have included a detailed explanation of the impact on state tax receipts and a state-by-state analysis as prepared by Ernst & Young, LLP for identical legislation considered in the 111th Congress as Exhibit B to my testimony. As noted in the fiscal impact analysis, forty-four states either gain a small amount of revenue or have net reductions in revenue of one hundredth of one percent or less (0.01%). The impact of the legislation results in a redistribution of income taxes between resident and nonresident states with only a very slight reduction in total income taxes collected by the states. For all fifty states and the District of Columbia combined, the net change is a reduction in revenue of a mere one hundredth of one percent (.01%), which accrues as a net nationwide reduction of $42 million in overall personal income taxes.

Why such a small net reduction in overall personal income taxes? Under H.R. 1864, employees whose work responsibilities in nonresident states are under the thirty day threshold period would experience a reduction in personal income taxes only under the following two circumstances: (1) to the extent the employee's resident state imposes tax at a lower rate than the nonresident state or (2) when a nonresident state tax is imposed on an employee whose resident state does not also impose a personal income tax.

Conclusion

H.R. 1864 addresses a problem that is universally recognized by the state tax community. According to the Federation of Tax Administrators, "Complying with the current system is…indeed difficult and probably impractical."[2] Indeed, one prominent state tax official candidly acknowledged that even he does not comply with current law on his regular

[2] Statement of Harley Duncan before the House of Representatives Committee on the Judiciary, Subcommittee on Commercial and Administrative Law, November 1, 2007.

travels away from his home state, concluding that "there is widespread noncompliance" currently.[3]

The proposed solution articulated in H.R. 1864—a thirty day threshold period and associated operating rules that address both employee liability and employer withholding—is widely accepted as the appropriate framework to address the problem. In fact, the MTC's draft model statute is based on the predecessor to H.R. 1864.[4]

The only question we confront here is whether the problem is best addressed separately by each individual state or the Congress. I greatly respect my colleagues in state government and the work that they do, and I would like to think that they, working in concert, could solve this problem. Unfortunately, the practical political obstacles to achieving such a solution, and the historical lack of any evidence that such a solution is possible, leads me to conclude that state model legislation will not solve the problem.

Employees who travel outside of their home states for temporary work periods, and their employers, will remain subject to today's onerous burdens without Congressional action. Thus, I respectfully request your support for the speedy adoption of H.R. 1864.

I would be pleased to answer any questions you may have. Thank you.

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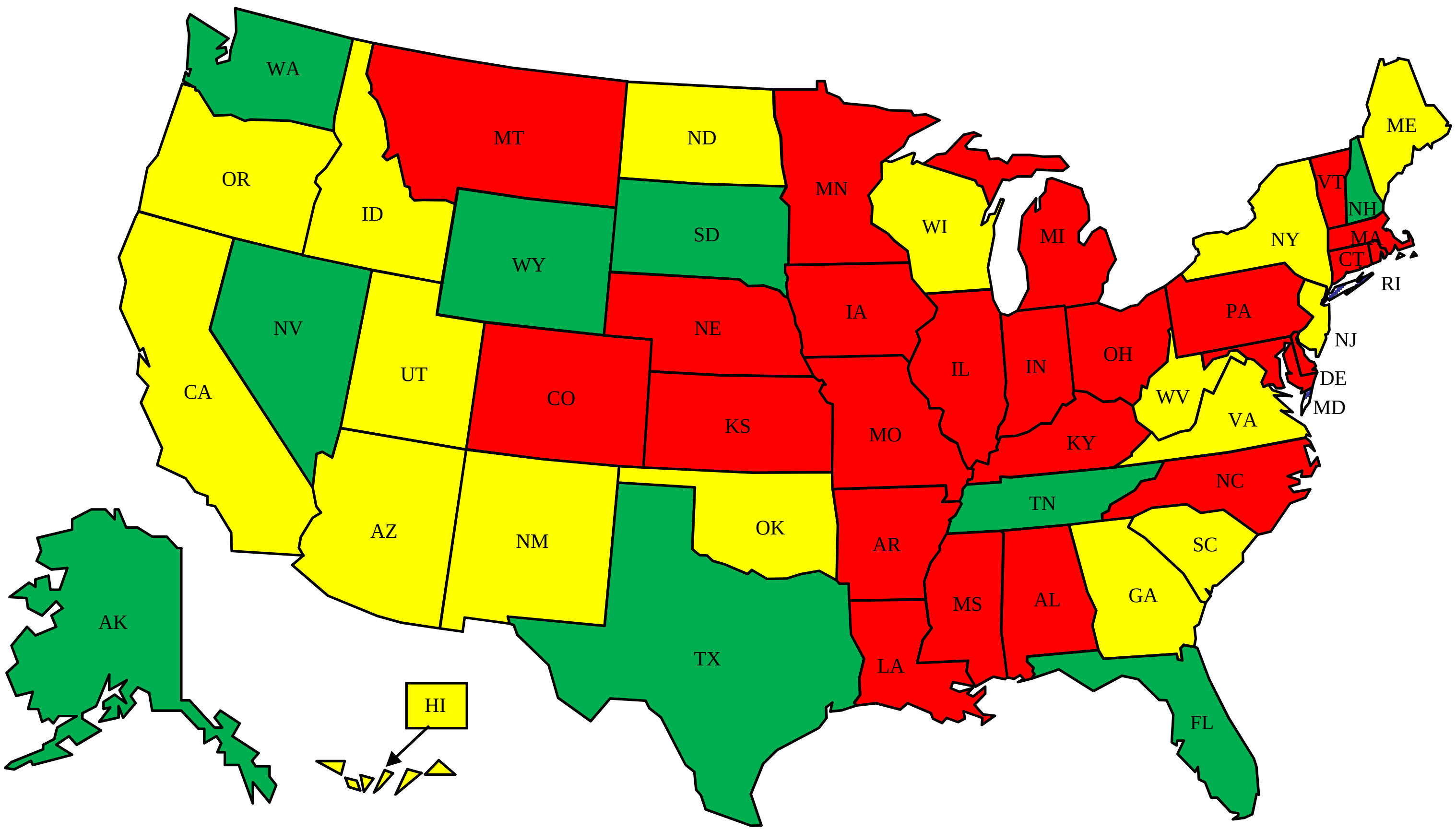
[3] White, Nicola M., "Many Agreed on Need for Mobile Workforce Tax Uniformity, but Will it Happen?" *State Tax Notes*, August 2, 2010, p. 271.
[4] Multistate Tax Commission: http://www.mtc.gov/Uniformity.aspx?id=4622.

Appendix A

Nonresident Personal Income Tax Withholding



Key

Nonresident employees subject to tax withholding on *first day* of travel

Nonresident employees subject to tax withholding after reaching threshold (see Appendix A for details)

No general personal income tax (or, in the case of Washington, DC, no tax on nonresidents)

— Appendix A —

Withholding Thresholds—More than half of the states that have a personal income tax require employers to withhold tax from a nonresident employee's wages beginning with the *first day* the nonresident employee travels to the state for business purposes. Some personal income tax states (identified on the map with a yellow background) provide for a threshold before requiring tax withholding for nonresident employees. The following chart details these withholding thresholds. Please note that this chart covers *withholding* only; many of these states have a different (and usually lower) standard for imposing tax on nonresidents (*i.e.*, the employee may owe tax even where the employer is not required to withhold tax).

State	No Withholding Required If Nonresident…
Arizona	is in the state for 60 or fewer days in a calendar year
California	earns in-state wages equal to or below "Low Income Exemption Table"
Georgia	is in the state for 23 or fewer days in a calendar year or if less than $5,000 or 5% of total income is attributable to Georgia
Hawaii	is in the state for 60 or fewer days in a calendar year
Idaho	earns in-state wages less than $1,000 in a calendar year
Maine	is in the state for 10 or fewer days in a calendar year
New Jersey	earns in-state wages less than the employee's personal exemption in a calendar year
New Mexico	is in the state for 15 or fewer days in a calendar year
New York	is in the state for 14 or fewer days in a calendar year
North Dakota	is in the state for 20 or fewer days in a calendar year and is a resident of a state that provides similar protections for nonresidents (reciprocal exemption); certain occupations (e.g., professional athletes) not protected
Oklahoma	earns in-state wages less than $300 in a calendar quarter
Oregon	earns in-state wages less than the employee's standard deduction
South Carolina	earns in-state wages less than $800 in a calendar year
Utah	*employer* does business in the state for 60 of fewer days in a calendar year
Virginia	earns in-state wages less than the employee's personal exemptions and standard deduction or, if elected by the employee, the employee's filing threshold
West Virginia	earns in-state wages less than the employee's personal exemptions
Wisconsin	earns in-state wages less than $1,500 in a calendar year

Reciprocal Agreements—In addition to the thresholds shown above, many states have reciprocal agreements with neighboring states that provide that taxes are paid in (and withheld for) the resident state only. For example, a resident of Virginia who works in Maryland is subject to tax only in Virginia. The converse also applies. In most states with reciprocal agreements, a "certificate of nonresidence" must be filed either with the employer or the nonresident state. A full list of state reciprocal agreements is beyond the scope of this document.

March 16, 2009

Estimates of State-by-State Impacts of the Mobile Workforce State Income Tax Fairness and Simplification Act

This analysis presents state-by-state estimates of the net change in state personal income taxes projected from the impact of the Mobile Workforce State Income Tax Fairness and Simplification Act at fiscal year 2008 levels. The net impact figures for each state include two components: 1) the reduction in income tax collections due to the increase in the number of in-state days (30 days less a state's current-law day threshold) required before a nonresident employee is subject to income taxation, and 2) the increase in tax collections in resident states due to reduced credits on resident income tax returns for taxes paid by the residents to other states where they work and are taxed as nonresidents.

The bill has the following features that are important determinants of the estimated state income tax impacts:

- A nonresident employee, with limited exceptions, performing employment duties in a state for 30 days or less would not be subject to the nonresident state's personal income tax.

- An employee is considered to be performing employment duties within a state for a day if the preponderance of their employment duties for the day are within a state. If employment duties are performed in a nonresident state and a resident state in the same day, the employee is considered to be performing employment duties in the nonresident state for the day.

- The legislation would not be effective until January 1, 2011.

Table 1 provides state-by-state estimates of the change in net personal income taxes (in millions of dollars) due to the proposal. The net change for all states and the District of Columbia (-$42 million) is the sum of the revenue reduction due to reduced taxes paid by nonresident employees and increased taxes paid to resident states due to lower credits. Table 1 also reports the net change as a percent of fiscal year 2008 total state taxes.[1]

Twenty-five states have either an income tax revenue gain or no loss under H.R. 3359; another 22 states have revenue reductions less than 0.02% (two-hundreds of a percent or two-tenths of a mill) of state tax collections. As the table illustrates, the bill redistributes income taxes between resident and nonresident states with only a very slight reduction in total income taxes collected

[1] The estimates were prepared by Ernst & Young LLP based on survey data provided by seventeen states through the Federation of Tax Administrators, as well as state tax collection data for other states from the U.S. Census *Governmental Finances* and state tax collection reports and journey-to-work data from the U.S. Census. More detailed estimates, as well as a description of the estimating methodology, are available upon request. The legislation will not affect local personal income taxes.

Table 1: Estimates of Impact of H.R. 3359, FY 2008		
State	**Net Change as a Percent of Total State Taxes**	**Net Change in Millions of Dollars**
Alabama	0.01%	$0.5
Alaska	0.00%	0.0
Arizona	0.01%	1.3
Arkansas	0.00%	-0.3
California	-0.01%	-6.2
Colorado	-0.02%	-1.5
Connecticut	0.02%	3.1
Delaware	0.08%	2.4
District of Columbia	0.00%	0.2
Florida	0.00%	0.0
Georgia	-0.01%	-1.8
Hawaii	0.00%	0.2
Idaho	0.00%	0.1
Illinois	-0.02%	-7.4
Indiana	0.03%	3.8
Iowa	0.01%	0.9
Kansas	0.00%	0.3
Kentucky	-0.01%	-1.3
Louisiana	-0.02%	-1.7
Maine	0.00%	0.1
Maryland	-0.01%	-1.0
Massachusetts	-0.03%	-6.9
Michigan	-0.01%	-1.8
Minnesota	-0.01%	-2.2
Mississippi	0.01%	0.6
Missouri	0.01%	1.6
Montana	0.00%	-0.1
Nebraska	0.00%	-0.1
Nevada	0.00%	0.0
New Hampshire	0.00%	-0.1
New Jersey	0.09%	26.2
New Mexico	0.00%	0.0
New York	-0.07%	-45.2
North Carolina	-0.01%	-1.6
North Dakota	0.00%	-0.1
Ohio	-0.01%	-1.7
Oklahoma	-0.01%	-0.5
Oregon	-0.04%	-2.7
Pennsylvania	-0.01%	-2.2
Rhode Island	0.12%	3.3
South Carolina	0.03%	2.3
South Dakota	0.00%	0.0
Tennessee	0.00%	-0.1
Texas	0.00%	0.0
Utah	-0.01%	-0.7
Vermont	0.01%	0.3
Virginia	-0.01%	-1.3
Washington	0.00%	0.0
West Virginia	-0.01%	-0.4
Wisconsin	0.00%	-0.4
Wyoming	0.00%	0.0
Total for All States	**-0.01%**	**-$42.0**

by the states. For all states combined, the net change in total taxes is only a reduction of -.01% or $42 million which accrues as a reduction in overall personal income taxes.

It is important to note that the proposed law change would not apply until January 1, 2011. As shown in Table 2, there would be no fiscal impact on states for fiscal years 2009 and 2010, and only a partial-year impact (less than 50% of the annual impact) for fiscal year 2011 that, for most states, ends July 31, 2011. The full fiscal year impact will first occur in fiscal year 2012.

Table 2
Fiscal Year Impact of H.R. 3359
FY 2008 Levels of Taxes

Fiscal Year	Impact on State Income Taxes
2009	no impact
2010	no impact
2011	less than $21 million
2012	$42 million

Table 3 compares the net impact estimates for the Mobile Workforce State Income Tax Fairness and Simplification Act considered by the 110th Congress and for the bill as prepared for introduction in the 111th Congress. As originally introduced, the bill included a 60-day threshold for nonresident taxation. As shown in the table, this would have reduced state net personal income tax collections by $102 million at fiscal year 2008 collection levels. The second line of the table shows that the reduction of the threshold to 30 days lowers the revenue impact by $55.6 million to a net reduction of $46.5 million. Adding the more expansive definition of a "day" worked in a nonresident state reduces the net loss further to $42 million. The combined impact of these two changes is a reduction in the states' net revenue loss by almost 60 percent compared to H.R. 3359 as originally introduced.

Table 3
Revenue Impacts of Alternative Versions of
the Mobile Workforce State Income Tax Act

Mobile Workforce Bill Proposals	Net Impact FY 2008 Levels	Change in Net Impact
1. Initial proposal with a 60-day threshold	-$102.1	
2. Proposal with a 30-day threshold	-$46.5	-$55.6
3. Proposal with a 30-day threshold and a revised definition of "day" in a state	-$42.0	-$4.5
Total Change in Proposal Impacts		**-$60.1**