

The Telecommuter Tax Fairness Act Is Gaining Traction

by Nicole Belson Goluboff

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Support is growing, both within and outside Congress, for the Telecommuter Tax Fairness Act¹ — the federal bill that would prohibit New York and other states from applying the “convenience of the employer” rule.² The convenience rule is the state income tax rule that subjects nonresident telecommuters to the risk that they will be double taxed on the income they earn while working from home.

The Telecommuter Tax Fairness Act was introduced in May 2005 by U.S. Sen. Christopher J. Dodd, D-Conn., and U.S. House Rep. Christopher Shays, R-Conn. On its introduction, it was cosponsored by Sen. Joseph I. Lieberman, D-Conn., Reps. Rosa L. DeLauro, D-Conn., and Tom Davis, R-Va. In January 2006, Rep. Frank R. Wolf, R-Va., joined the group.

The adverse impact of the convenience of the employer rule on telecommuters throughout the United States is now widely recognized. Teleworkers from coast to coast are objecting to the rule, and a

¹S. 1097; H.R. 2558.

²See 20 NYCRR section 132.18(a) (“If a nonresident employee . . . performs services for his employer both within and without New York State, his income derived from New York State sources includes that proportion of his total compensation for services rendered as an employee which the total number of working days employed within New York State bears to the total number of working days employed both within and without New York State. . . . However, any allowance claimed for days worked outside New York State must be based upon the performance of services which of necessity, as distinguished from convenience, obligate the employee to out-of-state duties in the service of his employer”). See also 61 Pa. Code section 109.8; Neb. Admin. Code section 316-22-003.01C(1).

growing number of tax and pro-telework organizations are urging Congress to get involved. As support for the Telecommuter Tax Fairness Act intensifies, Washington must accelerate its passage.

I. Review of the New York Rule

A. In General

Under New York’s convenience rule, nonresidents who work for New York employers and telecommute some or most of the time may be required to treat the income they earn at home as if it is earned in New York and pay New York tax on it. Because the telecommuter’s state of residence may also tax the income he or she earns at home, the telecommuter may be taxed twice on that income.

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Even if the telecommuter’s state of residence has no income tax — or offers a credit for taxes paid to New York — the telecommuter may be harmed. If New York taxes income at a higher rate than the home state, the telecommuter will have to pay the New York rate on income earned elsewhere. Also, the telecommuter’s tax dollars will be used to support the libraries, schools, and other public services of New York (where the telecommuter neither lives nor votes), while the same services in the telecommuter’s home state may suffer from the diversion of that tax money to New York.

B. Necessity Test

Although, under the rule, employees who telecommute because of employer necessity do not have to allocate their out-of-state income to New York, few telework arrangements qualify as “necessary.” As long as the nature of the employee’s work is such

that it could be done in New York, New York may insist that telework is merely a convenience to the employee.³

New York has refused to regard telework as necessary even when the employer required the employee to work off-site. For example, in the recent case *Matter of Kakar*,⁴ the taxpayer was responsible for preparing and reviewing highly confidential financial information, which his company's president and CEO did not want "disseminated to other employees." Because of "adverse business conditions," the company decided to reduce its New York City work space. It reconfigured the office to provide multipurpose rooms for some employees to share. Because the shared work space did not provide the privacy Kakar needed to preserve the confidentiality of the reports he prepared, the employer "directed [him to] set up a satellite office" of the company in his New Jersey home. The company paid all expenses associated with that office.

Subsequently, Kakar moved to Arizona. He continued to telecommute for the company, working in the New York office "periodically." As with Kakar's New Jersey home office, the company paid all the expenses of the Arizona office.

Although Kakar's employer considered off-site work necessary, New York's Division of Tax Appeals did not. According to the division, New York was entitled to tax Kakar on the income he earned in New Jersey and Arizona.⁵

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New York's strained construction of employer "necessity" punishes telecommuters like Kakar for the management strategies of their employers. Under the New York scheme, nonresidents whose employers instruct them to keep the business running from their homes during a hurricane, transit strike, bird flu outbreak, or terror threat could well be treated as if they are working at a remote location merely to suit themselves.

However, New York's necessity test is not just too hard to satisfy: It is an entirely misplaced standard for determining the source of income. New York's focus on *why* employees telecommute — its insistence

on requiring remote workers to prove that telework is necessary for the employer — reflects the state's underlying mistrust of the practice. New York apparently assumes that, on their at-home days, telecommuters are either not really working or are not doing work for which their employers pay them. These assumptions take no account of the contemporary workplace.

In this era of cell phones, laptops, Blackberries, and Trio's, employers routinely expect their information-based workers to be productive anytime, anywhere — and employees routinely oblige. Both parties profit from the flexibility such mobile tools offer. Telecommuters should not be penalized for the mutually beneficial deal they strike with their employers to provide their services from a different state.⁶

C. New York's Far Reach

Formal rulings demonstrate that New York has applied the convenience rule to exact revenue from telecommuters near and far, including telecommuters residing in Connecticut, New Jersey, Pennsylvania, Maine, New Hampshire, North Carolina, Florida, Tennessee and Arizona.⁷ There is also increasing anecdotal evidence that telecommuters

⁶These two fundamental defects of the necessity test — that it is unreasonably difficult to meet and that it offers an irrelevant standard for determining income source — would not be corrected by the draft revisions to the application of the convenience rule that New York's Department of Taxation and Finance has recently prepared. Under these draft revisions, a "normal work day spent at the [telecommuter's] home office [would] be treated as a day worked outside [New York] if the taxpayer's home office is a bona fide employer office." (See New York State Department of Taxation and Finance, Office of Tax Policy Analysis, Technical Services Division, TSB-M-05 (XI DRAFT.) The test for determining whether the home office is a "bona fide employer office" involves an elaborate menu of factors, which, for many telecommuters, would be just as hard to satisfy as the current necessity test. The "bona fide employer office" test would also be just as irrelevant: New York's out-to-lunch presumption remains that interstate telecommuting is, in most cases, simply an employee device for evading New York taxes.

⁷See, e.g., *Huckaby v. New York State Division of Tax Appeals*, 4 N.Y.3d 427 (2005), cert. denied, 74 U.S.L.W. 3272 (Oct. 31, 2005) (Tennessee); *Zelinsky v. Tax Appeals Tribunal of New York*, 1 N.Y.3d 85 (2003), cert. denied, 541 U.S. 1009 (2004) (Connecticut); *Matter of Speno*, 35 N.Y.2d 256 (1974) (New Jersey); *Matter of Phillips*, 267 A.D.2d 927 (App. Div. 3d Dept. 1999) (Pennsylvania); *Matter of Kakar*, DTA No. 820440 (Feb. 16, 2006) (New Jersey and Arizona); *Matter of Gray*, DTA No. 819457 (Feb. 24, 2005) (New Hampshire); *Matter of Wallace*, DTA No. 817182 (Dec. 21, 2000) (Maine); *Matter of Roemer*, DTA No. 815734 (Sept. 3, 1998) (Florida); *Matter of King* (State Tax Commission, Apr. 6, 1987) (North Carolina). (For the court of appeals' decision in *Huckaby*, see *Doc 2005-6487* or *2005 STT 62-21*. For the court of appeals' decision in *Zelinsky*, see *Doc 2003-25309* or *2003 STT 228-10*.)

³See, e.g., *Matter of Kakar*, DTA No. 820440 (Feb. 16, 2006). (For the *Matter of Kakar*, see *Doc 2006-3721* or *2006 STT 41-23*.)

⁴*Id.*

⁵*Id.*

across the country have either been affected by New York's rule or believe they are at risk.⁸

II. The Remedy

Dodd and Shays introduced the Telecommuter Tax Fairness Act to redress the unfair results the convenience rule produces. The act provides that, when applying its income tax laws to a nonresident, a state may treat the nonresident as working in the state only if the nonresident is physically present there; that the state may not tax the nonresident on income the nonresident earns while physically outside the state; and that the state may not treat a nonresident as physically present in the state on the grounds that the nonresident is working at home for his or her own convenience.⁹

Because Dodd, Shays, and two of the bill's original cosponsors were from Connecticut, and because New York had distinguished itself among the states as an especially aggressive enforcer of the convenience rule, some may have initially viewed the problem as a local one — a dispute between Connecticut and New York not requiring federal intervention. However, there is now broad appreciation for the national consequences of the convenience rule and the need for congressional action.

III. The *Huckaby* Case

*Huckaby v. New York State Division of Tax Appeals*¹⁰ brought the national impact of the convenience rule into sharp focus. As has been previously reported,¹¹ Thomas Huckaby was a Tennessee resident who telecommuted to an employer in New York. Although he spent approximately 75 percent of his work time in Tennessee and only 25 percent of his work time in New York, under the convenience rule, New York required him to pay New York taxes on his entire income.

Huckaby challenged that excessive taxation in the New York courts, arguing that New York's application of the convenience rule to him violated his

rights under the Due Process and Equal Protection clauses of the U.S. Constitution. The New York courts upheld the tax. Huckaby sought the review of the U.S. Supreme Court, but, on October 31, 2005, the Court refused his appeal.

The case sounded an alarm for the country that New York was claiming authority to tax telecommuters located anywhere — not just in neighboring states, like Connecticut, but in every state in the nation. Further, the case warned Americans that states other than New York are free to assert the same authority.

IV. After *Huckaby*

A. Public Outcry

Immediately following the Supreme Court's decision, commentary blasting New York's telecommuter tax appeared in newspapers across the United States, including papers in Texas, New Hampshire, Ohio, Tennessee, Colorado, California, and even New York.¹² One reason for the indictment was that a telework tax threatens the continued growth of the work-at-home population.¹³ That population represents a significant segment of the American workforce: In 2005 approximately 10 million Americans telecommuted to their employers at least on a part-time basis.¹⁴ Over 45 million workers, including self-employed people, did at least some of their work from home.¹⁵

B. Traction in Congress

Also, after *Huckaby*, as mentioned above, Wolf signed on as a cosponsor of the Telecommuter Tax Fairness Act. Wolf has long been a proponent of

⁸Position Statement in Support of The Telecommuter Tax Fairness Act, January 2006, available at <http://www.TelCoo.org> (click on link for "The Telecommuter Tax Fairness Act").

⁹S. 1097; H.R. 2558.

¹⁰*Huckaby v. New York State Division of Tax Appeals*, 4 N.Y.3d 427 (2005), cert. denied, 74 U.S.L.W. 3272 (Oct. 31, 2005).

¹¹See, e.g., Goluboff, Nicole Belson, "State Taxation of Interstate Telecommuters: The U.S. Supreme Court's Silence Puts Congress in the Driver's Seat," *State Tax Notes*, Nov. 21, 2005, p. 719, 2005 STT 223-5, or Doc 2005-23145; Setze, Karen, "U.S. Supreme Court Declines to Hear Challenge to New York 'Convenience' Test," *State Tax Notes*, Nov. 7, 2005, p. 502, 2005 STT 210-1, or Doc 2005-22090; Goluboff, Nicole Belson, "Congress Must Slam the Brakes on New York's Convenience-of-the-Employer Rule," *State Tax Notes*, May 2, 2005, p. 363, 2005 STT 83-13, or Doc 2005-7616.

¹²See "Another Tax Grab: Telecommuting Becomes Endangered," *New Hampshire Union Leader*, Nov. 14, 2005 (New Hampshire); "Standard Needed on Taxing," *The Leaf Chronicle*, Nov. 14, 2005 (Tennessee); "A Tax Congress Should Remedy," *The Lima News*, Nov. 13, 2005 (Ohio); "Telecommuters Become Target for Tax Man," *The Gazette*, Nov. 9, 2005 (Colorado); "Mr. Huckaby's Lament," *The Journal News*, Nov. 9, 2005 (New York); "The Telecommuter Tax: Tax Policy Example of States' Ignorance of Information Age," *The Monitor*, Nov. 8, 2005 (Texas); "The Telecommuter Tax," *The Orange County Register*, Nov. 7, 2005 (California).

¹³See "The Telecommuter Tax: Tax Policy Example of States' Ignorance of Information Age," *The Monitor*, Nov. 8, 2005.

¹⁴Herman, Tom, and Rachel Emma Silverman, "Telecommuters May Face New Taxes," *The Wall Street Journal*, Nov. 1, 2005 (citing the Telework Advisory Group for WorldatWork as the source for this statistic).

¹⁵See ITAC (the Telework Advisory Group for WorldatWork) press release, "Annual Survey Shows Americans Are Working From Many Different Locations Outside Their Employer's Office," available at <http://www.workingfromanywhere.org> (providing data from the 2005 American Interactive Consumer Survey conducted by the Dieringer Research Group).

telework. In 2000 he secured legislation that required federal agencies to make telework available to every eligible staff member.¹⁶ Subsequently, he secured two pieces of enforcement legislation. Those imposed significant financial penalties on some agencies if they failed to meet requirements designed to ensure the wide-scale use of telework in the federal workforce.¹⁷

Shortly after Hurricane Katrina, in a letter to President Bush, Wolf urged the president “to embrace telework as a workplace priority,” emphasizing that, as “the nation’s largest employer, the federal government should be the model for telework for every level of government as well as the private sector.”¹⁸ He reiterated those sentiments in November 2005, when he participated in a hearing conducted by a subcommittee of the House Committee on Government Reform concerning how to mitigate the effect of high gasoline prices on American workers.¹⁹

The Telecommuter Tax Fairness Act would help ensure that the federal government can meet its goal to increase telework among federal employees. It would also liberate the private sector to expand its reliance on that essential form of interstate commerce.

C. New Support Within Telework Industry

The Telework Coalition,²⁰ a telework advocacy group headquartered in Washington, had been endorsing the federal bill from its infancy, before the measure had congressional sponsors. *Huckaby* compelled more organizations that promote telework to declare their support for the legislation.²¹ Those organizations include ITAC (the Telework Advisory Group for WorldatWork),²² which is based in Arizona; the Telework Exchange,²³ in Virginia; and the Association for Commuter Transportation, in Georgia.²⁴

D. Tax Community’s Call for Reform

Before the Supreme Court’s decision in *Huckaby*, the Telecommuter Tax Fairness Act received the

endorsement of the National Taxpayers Union (NTU), a taxpayer advocacy organization based in Virginia with a membership of 350,000. The group described the bill as “common-sense legislation” addressing an “unfair and inequitable” tax rule. The convenience rule, NTU said, is “already [creating] a major problem” for telecommuters with New York employers and “could be a potential nightmare” for millions of telecommuters nationwide.²⁵

After *Huckaby*, the Tax Foundation, a nonpartisan tax research organization based in Washington, prepared a paper urging Congress to provide a remedy for the problems the convenience rule creates.²⁶

The Tax Foundation offered three principal reasons for Congress to get involved. The “most important” of those is “to prevent state taxpayers from facing double taxation.” The double taxation, the paper explained, “introduces economic distortion into the decision whether to telecommute or normally commute.”²⁷

The “next most important reason,” the paper said, “is the benefit principle of taxation.” According to that principle, “a state should get the right to tax a person’s income when that person is benefiting from services provided by the state. A physical-presence rule [such as the Telecommuter Tax Fairness Act sets forth] better matches taxes paid and benefits received, since only employees who are physically present are significantly benefiting from public services.”²⁸

The third reason Congress should pass remedial legislation, according to the Tax Foundation, is “to reduce tax complexity.” Businesses “with telecommuters in other states would have to withhold income tax for their employees in those states,” the paper said. “Since different states have different rules on telecommuting, this would quickly become a compliance burden” for employers. “A rule like that embodied in the Telecommuter Tax Fairness Act would create one clear, simple rule to guide businesses.”²⁹

V. Opportunity for Mutual Support

The Telecommuter Tax Fairness Act is currently pending before the House Judiciary Committee. However, it is not the only bill before that committee

¹⁶Public Law 106-346.

¹⁷P.L. 108-447; P.L. 109-108.

¹⁸Letter from Frank R. Wolf to President Bush, Sept. 15, 2005, available at <http://www.house.gov/wolf/news/2005/09-16-telework.html>.

¹⁹House Government Reform Subcommittee on the Federal Workforce and Agency Organization, “Mitigating the Impact of High Gas Prices on the American Workforce,” remarks by Rep. Frank R. Wolf, available at <http://www.reform.house.gov>.

²⁰<http://www.TelCoa.org>.

²¹“Support for ‘The Telecommuter Tax Fairness Act’ Is Growing,” PRWeb press release, available at <http://www.prweb.com/prweb.php?prid=335338>.

²²<http://www.workingfromanywhere.org>.

²³<http://www.teleworkexchange.com>.

²⁴<http://www.actweb.org>.

²⁵Letter from Paul J. Gessing, director of government affairs, National Taxpayers Union, to Rep. Chris Shays, June 10, 2005, available at <http://www.ntu.org>.

²⁶Atkins, Chris, “Telecommuter Tax Fairness Act of 2005: Restoring Balance to State Taxation of Telecommuters,” Jan. 31, 2006, available at <http://www.taxfoundation.org/news/show/1316.html>.

²⁷*Id.*

²⁸*Id.* (citations omitted).

²⁹*Id.*

that seeks to eliminate the double taxation of some state nonresidents. Another bill, H.R. 4019, has a similar goal.

H.R. 4019 would assure that states cannot tax the income of nonresident retired partners. Both the telecommuter tax bill and the pension tax bill may make better time on their journey through Congress if they carpool.

The American Institute of Certified Public Accountants, a group representing over 350,000 members, has endorsed H.R. 4019. In a written statement that the AICPA submitted to the Judiciary Subcommittee on Commercial and Administrative Law,³⁰ the group described the bill's history: In 1996 the federal government enacted P.L. 104-95, which prohibited states from taxing nonresident retirement income. Now, according to the AICPA, there is a concern that states may construe the 1996 law too narrowly. Specifically, they may construe it to protect from taxation some retirement income of only those nonresident retirees who were employees, not those who were partners. H.R. 4019 is intended to clarify that the 1996 law prohibits taxation of the retirement income earned both by nonresident employees and by nonresident partners. The AICPA offered its support for H.R. 4019, in part, because the group objected to the double taxation risk nonresident retirees face.³¹

H.R. 4019 was sponsored by Rep. Chris Cannon, R-Utah, and, as of March 22, 2006, has 22 cosponsors. Because H.R. 4019 and H.R. 2558 (the Telecommuter Tax Fairness Act) are both intended to prohibit unfair, double taxation of nonresidents, the sponsors of both bills could benefit from collaborating to accomplish their similar missions.

Further, Cannon and a host of cosponsors of H.R. 4019 are also members of the House Judiciary Committee.³² As such, they could encourage the committee to act on the two nonresident income tax bills together and to recommend swift passage of both. Addressing the two bills at once would promote both legislative efficiency and badly needed tax simplification.

³⁰AICPA, "Statement for the Hearing Record, Subcommittee on Commercial and Administrative Law, Committee on the Judiciary, U.S. House of Representatives, Holding Hearings on H.R. 4019 December 13, 2005 Relating to the State Taxation of Non-Resident Retirement Income," Dec. 16, 2005, available at <http://tax.aicpa.org>.

³¹*Id.*

³²As of March 22, 2006, the cosponsors of H.R. 4019 who also serve on the House Judiciary Committee are Reps. Howard Coble, R-N.C., Bob Goodlatte, R-Va., Steve Chabot, R-Ohio, Ric Keller, R-Fla., Mike Pence, R-Ind., J. Randy Forbes, R-Va., Tom Feeney, R-Fla., and Rick Boucher, D-Va.

VI. Telecommuter Bill's Good Mileage Potential

As I have previously argued,³³ by facilitating telework, the Telecommuter Tax Fairness Act would help the nation achieve many critical objectives. It would enable both government and businesses to continue functioning during emergencies. It would help Americans cope with high gasoline prices, reduce our foreign oil dependence, and reduce traffic and air pollution. The act would ease the challenges many employees face when trying to meet both job and family demands. It would help older and disabled people continue working,³⁴ and it would bring more jobs to the nation's rural areas.

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Further, the Telecommuter Tax Fairness Act would help the country meet those goals without requiring the government to create new, costly programs. It would help by removing a rule that unduly burdens interstate business arrangements. Those and other advantages explain why the legislation has gained momentum. It's time for Congress as a whole to rally behind this bipartisan bill and see to its enactment during the current session. ☆

³³Goluboff, Nicole Belson, "State Taxation of Interstate Telecommuters: The U.S. Supreme Court's Silence Puts Congress in the Driver's Seat," *supra* note 10; Goluboff, Nicole Belson, "Congress Must Slam the Brakes on New York's Convenience-of-the-Employer Rule," *supra* note 10; Goluboff, Nicole Belson, "Put the Telecommuter Tax Fairness Act in the Passing Lane," *State Tax Notes*, Nov. 1, 2004, p. 319, 2004 STT 211-2, or Doc 2004-19727.

³⁴See, e.g., Joachim, David S., "Computer Technology Opens a World of Work to Disabled People," *The New York Times*, Mar. 1, 2006.