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employee benefits lawflash

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New York State Updates Guidance on 14-Day Withholding Threshold

Department of Taxation and Finance provides clarification on when 14-day rule applies as well as exceptions to the rule, but several key issues remain unresolved.

On July 5, the New York Department of Taxation and Finance (the Department) issued a Technical Memorandum, TSB-M-12(5)I, outlining the Department's policy regarding the employer withholding threshold for employees that are expected to work 14 days or fewer in New York during the calendar year. Previously, the Department's policy regarding the 14-day withholding threshold was provided in its Withholding Tax Field Audit Guidelines. Despite the more formal guidance provided in TSB-M-12(5)I, the Department's policy regarding the withholding threshold leaves several open questions regarding the application of the withholding standard for nonresident employees.

Overview of the 14-Day Withholding Threshold

Section 671(a)(1) of the New York Tax Law provides that every employer maintaining an office or transacting business within New York and making payment of any wages subject to New York State personal income tax is required to deduct and withhold tax from those wages. The amount withheld should be substantially equivalent to the tax reasonably estimated to be due.

Generally, a nonresident individual is required to file a New York State personal income tax return to the extent that the individual has any New York source income.[1] For purposes of an employer's withholding requirements, however, TSB-M-12(5)I provides that an employer will not be assessed tax, penalties, or interest for failing to withhold New York State tax on wages paid to nonresident employees performing services both in and out of New York if **all** of the following conditions are met:

- The employee is assigned to a primary work location outside of New York State.
- The employer reasonably expects that the employee will work in New York State for 14 days or fewer in the calendar year.
- The employee **does not** work in New York State for more than 14 days (subject to certain special rules, as discussed below).
- The employee's compensation is not within the exceptions to the 14-day rule (discussed below).

If the employer reasonably expects that an employee will be required to work in New York State for more than 14 days in the calendar year, then the 14-day rule does not apply, and the employer is required to withhold on all New York State wages paid to the employee. TSB-M-12(5)I also provides that "when applying the 14-day rule, any part of a day spent working in New York counts as a full day. However, do not count any day spent in New

1. Please note that any deferred compensation that qualifies under the special federal blocking rules (i.e., benefits that are paid under a so-called "excess benefit plan" or benefits that are paid out as annuity over at least 10 years) should be subject to tax only in the employee's state of residence and not in the nonresidence state where the services are performed.

York for the **sole** purpose of job-related training, such as in-house training courses, trade association conferences or symposia, or professional development workshops, seminars, or conventions."

Special Rules

TSB-M-12(5)I provides several special rules. If a nonresident employee was not initially expected to work more than 14 days in New York State during the calendar year, but does in fact work more than 14 days in New York State, then the employer is required to withhold on all New York State wages paid after the 14th day. If a nonresident employee is assigned to a primary work location in New York or to a different position that will result in the employee working more than 14 days in New York, then the employer is required to withhold New York State wages paid on or after the date of the change.

Exceptions to the Rule

Under TSB-M-12(5)I, the 14-day rule does **not** apply to the following:

- Compensation paid to nonresident traveling salespersons when the compensation depends entirely on the volume of business transacted
- Compensation paid in one year that is related to services performed in a prior year (e.g., deferred compensation, compensation from statutory stock options)[2]
- Compensation paid to nonresident public speakers, athletes, or entertainers performing services in New York

Level of Authority

The Department's technical memoranda, such as TSB-M-12(5)I, explain its current existing policies. Generally, such technical memoranda serve only an advisory purpose and are not binding on the Department or entitled to administrative deference. As such, TSB-M-12(5)I should be viewed as an explanation of the Department's current policy regarding the 14-day withholding threshold.

Remaining Issues

The Department's guidance leaves several key issues unresolved. For example, how should the employer determine what constitutes a New York workday for purposes of calculating the 14-day exception? The memorandum describes what should be counted as a full New York workday, but this description raises numerous questions regarding the scope of activities that potentially may satisfy the standard for a New York workday.

The Department has not provided a *de minimis* standard or minimum threshold for the amount of work-related activities that should be required to constitute a New York workday. For example, should an employee who responds to a few work-related emails or makes a brief work-related phone call while on vacation in New York be treated as working in New York for the day?

Morgan Lewis contacted the Department on an informal basis to request further clarification regarding its application of the "workday" standard. Based on our discussion, the Department's explanation of what constitutes a New York workday is open-ended and can be open to interpretation. Therefore, although it is impractical to expect employers to track every day in which an employee performs any work-related function in New York, the Department potentially may consider any work activities performed in New York to be a New York workday for purposes of computing the 14-day threshold.

While TSB-M-12(5)I does not clarify the meaning of a workday for purposes of the 14-day rule, the Department's prior technical memoranda and return instructions for other areas of the New York tax law, namely nonresident

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2. *See* footnote 1 above regarding federal blocker rules that prevent state taxation on certain deferred compensations.

personal income tax, shed some light on the interpretation. TSB-M-06(5)I defines a normal workday as "any day that the taxpayer performed the usual duties of his or her job." Importantly, the memorandum further explains that "responding to occasional phone calls or emails, reading professional journals, or being available if needed does not constitute performing the usual duties of his or her job." Similarly, the instructions for Schedule A of Form IT-203-B, *Nonresident and Part-Year Resident Income Tax Return*, which computes the New York nonresident allocation of wage and salary income to New York, provides that workdays are "days on which [the employees] were required to perform the usual duties of [their] job."

Therefore, a case can be made that the Department's general interpretation of what activities constitute a "workday" involves the performance of services that are more substantial than making occasional phone calls or responding to a few emails when located in New York. As previously mentioned, however, the Department has yet to clearly define what constitutes a New York workday for purposes of the 14-day rule and potentially may take a different position on audit.

It is important to note, however, that the 14-day withholding threshold does not apply to compensation paid in one year that is related to services performed in a prior year, such as deferred compensation and compensation from statutory stock options. Many employers do not track withholdings for employees who worked in New York for 14 days or fewer in a given taxable year. Since the 14-day exception does not apply to compensation paid in one year that is related to services performed in a prior year, however, such information may be necessary in order to comply with New York withholding requirements. Similarly, employers seeking to come into compliance with withholding requirements through New York's Voluntary Disclosure and Compliance Program may be required to provide such information.

Implications

Overall, employers should continue to exercise diligence in maintaining information regarding the work locations of employees in order to comply with New York withholding requirements. For employees receiving the types of compensation that are within the exceptions to the 14-day rule, employers should also maintain employee work location records, even if the employees are working fewer than 14 days in New York. Employers should also continue to monitor any updates to the Department's guidance regarding the application of New York withholding requirements.

Contacts

If you have any questions or would like more information on the issues discussed in this LawFlash, please contact any of the following Morgan Lewis attorneys:

Washington, D.C.

Mary B. Hevener	202.739.5982	mhevener@morganlewis.com
Patrick Rehfield	202.739.5640	prehfield@morganlewis.com
Douglas Tan	202.739.5243	dtan@morganlewis.com

Palo Alto

William H. Gorrod	650.843.7221	wgorrod@morganlewis.com

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