

NEW JERSEY TELEWORKING TAX: “NO MORE MR. NICE GUY” EFFECTIVE OCTOBER 1, 2021

Hodgson Russ State & Local Tax Alert
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We now return to our regularly scheduled programming in New Jersey. Earlier this month, the Division of Taxation announced the end of its temporary taxpayer-friendly policies relating to COVID-19 and teleworking. As of October 1, 2021, the old, not-so-friendly tax policies go back into place.

For each tax issue impacted by COVID-19, attorneys in our State & Local Tax practice provide a summary of the temporary COVID-19 policy and the Division’s pre-pandemic policy, as well as our thoughts on the implications of the return to business as usual in the Garden State.

Corporation Business Tax (CBT)

Temporary COVID-19 Policy (ending Sept. 30, 2021)

- The Division temporarily waived the CBT nexus standard that is generally met if an out-of-state corporation has an employee working from home in New Jersey. As long as the out-of-state employer did not otherwise have physical presence in or economic nexus with New Jersey, the Division did not consider the employer to have nexus for CBT purposes during the waiver period.

Business as Usual (resuming Oct. 1, 2021)

- Under *Telebright Corp., Inc. v. Director, Div. of Taxation*, 25 N.J. Tax 333 (Tax 2010), *aff’d*, 424 N.J. Super. 384 (App. Div. 2012), New Jersey courts have held that one employee working from home in New Jersey on a full-time basis is sufficient to subject an out-of-state corporation to CBT.

Implications

- While the world was thrown into chaos in the immediate aftermath of the pandemic, many employees found a silver lining in the freedom of being able to work from any location they chose during the pandemic. From a tax perspective, this normally would have created immediate consequences to corporate employers. However, to provide relief, New Jersey agreed not to apply *Telebright* to employers who were allowing employees to work from New Jersey as a result of the pandemic.

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- *Telebright* did not address the situation of occasional work from home, which certainly happened before COVID-19 and will continue in the future. In *Telebright*, the employer “regularly and consistently” permitted one of its employees to telecommute full-time from New Jersey. To date, there has been no New Jersey court decision that has addressed the CBT nexus implications of an employee working from home one or two days a week.
- Employers relying on P.L. 86-272 for protection from income taxation in New Jersey should be especially vigilant about reviewing their employees’ work from home locations. Unless employees located in New Jersey are sales employees engaged solely in permitted solicitation activities, those employees could cause a business to lose the protection of P.L. 86-272.
- Even employers with no receipts apportionable to New Jersey will be responsible for the CBT minimum tax if they have nexus as the result of a teleworking employee.
- New Jersey rules on short period returns should permit an out-of-state employer that becomes subject to CBT in the last quarter of 2021 as the result of a teleworking employee to file a short period return that prorates entire net income and the allocation factor.
- Partnerships are not subject to the CBT and so the latest guidance from the Division does not impact employers that are organized as partnerships. However, that raises the question of whether New Jersey failed to provide notice of nexus relief to businesses organized as partnerships during the pandemic.

Sales Tax

Temporary COVID-19 Policy (ending Sept. 30, 2021)

- The Division temporarily waived the Sales Tax nexus standard that is generally met if an out-of-state seller has an employee working in New Jersey. As long as the out-of-state seller did not maintain any physical presence other than employees working from home in New Jersey solely due to the pandemic, and was below certain economic activity thresholds enacted after *South Dakota v. Wayfair*, 504 U. S. 298 (2018), the Division did not consider the seller to have nexus for Sales Tax purposes during the waiver time period.

Business as Usual (resuming Oct. 1, 2021)

- An employee working from home in New Jersey will create physical presence and Sales Tax nexus for an out-of-state employer because working at a location in New Jersey is considered physical presence in the state.

Implications

- As discussed above with respect to CBT nexus, the *Telebright* decision supports New Jersey’s position that an employee working from home in New Jersey on a full-time basis creates constitutional nexus. There does not seem to be a logical reason to reach a different conclusion for purposes of Sales Tax nexus. However, the same questions remain under the Sales Tax – what about an employee working from home on an occasional basis? There may be circumstances where such an arrangement does not satisfy constitutional nexus.

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- From a practical perspective, the return to pre-COVID-19 policy is most likely to impact small sellers because New Jersey employs economic nexus, affiliate nexus, and click-thru nexus in order to subject out-of-state sellers to Sales Tax obligations. With respect to economic nexus, a remote seller that makes a retail sale of tangible personal property, specified digital products, or taxable services delivered into New Jersey must register, collect, and remit Sales Tax if the remote seller meets either of the following criteria:
 - The remote seller’s gross revenue from sales of tangible personal property, specified digital products, or taxable services delivered into New Jersey during the current or prior calendar year, exceeds \$100,000; or
 - The remote seller sold tangible personal property, specified digital products, or taxable services delivered into New Jersey in 200 or more separate transactions during the current or prior calendar year.

New Jersey Employer Withholding

Temporary COVID-19 Policy (ending Sept. 30, 2021)

- For purposes of employer withholding obligations, during the temporary period of the COVID-19 pandemic, the Division advised that wage income must be sourced “as determined by the employer in accordance with the employer’s jurisdiction.”

Business as Usual (resuming Oct. 1, 2021)

- According to the Division, employers must cease sourcing income in accordance with the employer’s jurisdiction and should resume sourcing income based on where the service or employment is performed.

Implications

- The Division’s temporary policy left something to be desired in terms of clarity. If it is assumed that the policy was aimed at the most likely scenario – New York employers with employees working from home in New Jersey – then the temporary policy is an acknowledgment that the Division would respect New York’s convenience of the employer rule and not require withholding for employees working from home in New Jersey temporarily. Under New York’s “convenience” rule any normal work day spent at a New Jersey home office will be treated as a day worked outside New York only if the employee’s home office qualifies as a bona fide employer office.
- Under the pre-pandemic rules that are going back into effect, if an out-of-state business employs New Jersey residents working in New Jersey, it must register, file, and pay New Jersey employer withholdings.
- The Division’s withholding guidance provides that employers are not obligated to withhold New Jersey income tax from residents if the resident meets all three of the following requirements:
 - Employed totally outside New Jersey;
 - Subject to the withholding tax of another state; and
 - The withholdings required by that state equal or exceed the withholdings required for New Jersey.

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- In the more likely situation where an employee works outside New Jersey only part of the time, the employer must withhold New Jersey taxes to offset the employee’s resident income tax liability.
- The Division’s policy statements on employer withholding reflect the Division’s longstanding tolerance of New York’s convenience rule, which is most clearly evidenced in the credits that New Jersey grants residents for personal income taxes paid to New York in order to avoid double taxation. However, change may be on the horizon. In a brief filed with the U.S. Supreme Court, New Jersey has described New York’s convenience rule as unconstitutional and has alleged that the New York rule has resulted in a loss of revenue of approximately \$1 billion during the 12-month period beginning March, 2020, as a result of credits New Jersey will provide residents relating to income residents earned while working from home in New Jersey.

If you would like more information about the above New Jersey tax issues, contact Open Weaver Banks (646.218.7524), Debra Silverman Herman (646.218.7532) or Elizabeth Pascal (716-848-1622).