



California and Massachusetts Issue Employment Tax Guidance on Remote Work during Covid-19

In a prior SALT@Work column, we discussed the localization of work rules that determine where an employer will be subject to state unemployment insurance (UI) registration, reporting, and taxes when an employee works in multiple states.¹ When that prior column was submitted for publication, no state had issued guidance specifically discussing the UI localization of work rules as applied to a teleworking employee located outside the state of their normal work location. Shortly thereafter, however, two states – California and Massachusetts – issued or updated guidance pertinent to the localization rules that apply to UI and other employment taxes. This column summarizes that guidance and discusses its relevance among the other state employment tax regimes during the Covid-19 pandemic.

Background.

As previously discussed, states adopt uniform “localization of work” rules for sourcing wages subject to their respective UI taxes.² The localization of work rules provide for the following sequential tests:

- **Localization.** If an employee works entirely in a state, or the majority of work is performed in that state with only “incidental” work performed out-of-state, then the employee’s wages are sourced entirely to that state.
- **Base of Operations.** If an employee’s work is not localized in a single state, then wages are sourced to the employee’s “base of operations” state, so long as the employee performs some work in that state.
- **Direction and Control.** If neither the above tests apply, an employee’s wages are sourced to the state from which the employer exercises direction and control over the employee.
- **Residence.** If none of the above tests apply, the wages are sourced to the employee’s state of residence.³

During “normal” (non-pandemic) times, the localization of work rules are relatively straightforward for most employers, as most employees work in a single state with only incidental service out-of-state. However, during the Covid-19 pandemic and the resulting mandatory remote work policies, many employees are temporarily working in a state that differs from their normal work state. This work-from-anywhere situation created

some concern among employers as to when an employee’s temporary out-of-state service becomes more than “incidental” under the initial localization test, such that the employer would be required to report wages to another state.⁴

Unemployment insurance guidance – California. Providing much-needed clarity to many employers, the California Employment Development Department (EDD) was the first state UI administrator to issue guidance on multistate employment during Covid-19 and the application of the state’s localization of work rules.⁵

In seven new FAQs, the EDD explained how employers should apply the localization of work rules during COVID-19 and the resulting circumstances, including teleworking employees, layoffs, and business shutdowns, to name a few.⁶ Of particular note, the EDD explains when employers with employees teleworking in the state during Covid-19 would become subject to UI, as well as other California employment taxes such as the employment training tax (ETT) and state disability insurance (SDI) withholding:

The wages of employees who typically perform services in another state for an employer located outside of California will not be subject to [UI tax], [ETT], and [SDI] withholdings if those employees are temporarily performing services within California due to the COVID-19 pandemic. If a worker remains in California performing services after state or federal public health officials have ended stay-at-home orders and the worker could have resumed working at their normal work location outside California, the worker and the employer will be considered subject to California employment tax laws.⁷

Importantly, the EDD further explains, “[i]f the employee continues to perform services in California after the COVID-19 pandemic has ended, those services will become subject to UI Tax, ETT, and DI contributions.”⁸

The EDD’s response in the FAQ is consistent with its prior multistate employment guidance, as well as the U.S. Department of Labor’s guidance on the localization of work rules.⁹ As most relevant to Covid-19 remote work and the localization test, the EDD’s prior guidance explains:

An employee’s services are “localized” in California, and, therefore, considered subject to California employment taxes if

CHARLIE KEARNS is a Partner in the Washington, D.C. office, and ALEXANDRA LOUDERBACK is an Associate in the Sacramento, California office, of Everheds Sutherland (US) LLP.

all or most of the employee's services are performed in California with only incidental services performed elsewhere (for example, where the out-of-state service is *temporary or transient in nature* or consists of isolated transactions). Where the service performed outside of California is *either permanent, substantial, or unrelated*, it cannot be treated as localized in California.¹⁰

In the FAQ, the EDD distinguishes between temporary Covid-19 remote work and a permanent teleworking arrangement.

Paid family and medical leave – Massachusetts guidance. In addition to UI, a number of states have adopted paid family and medical leave (PFML) acts that are funded by employer contributions and/or employee withholding. Frequently, a state's PFML act will cross-reference or adopt

wage sourcing rules that follow the UI localization of work rules for purposes of determining the state where contributions or withholding is owed.¹¹ Accordingly, PFML wage sourcing issues have arisen during Covid-19 with respect to remote work similar to those described above in the context of UI taxes.

Among the states that have a PFML act, Massachusetts was the first state to issue guidance on teleworking during the Covid-19 pandemic. For background, Massachusetts adopted its PFML law in 2018, which permits most employees to take paid family leave of up to twelve weeks and medical leave of up to twenty weeks, with benefit payments beginning January 1, 2021.¹² PFML contribution requirements began on October 1, 2019, after a delayed start to allow employers more time to come into compliance with

the contribution.¹³ Generally, funding for Massachusetts PFML benefits will come from a split between employer contributions and employee contributions (via employer withholding), subject to exceptions.¹⁴ A "covered business entity," "covered contract worker," or "electing self-employed person" also will be required to make contributions to the PFML trust fund.¹⁵

On December 8, 2020, the Massachusetts Department of Revenue released Technical Information Release No. 20-15 (TIR), which extends a variety of previously-announced emergency rules first released in April on remote work during Covid-19, including the PFML-related rule.¹⁶ Under the extended TIR, an individual who previously performed services outside of Massachusetts and was not subject to PFML will not become subject



¹ See Kearns and Louderback, "Home is Where the Localization Is - Telework and Unemployment Insurance," 30 JMT 8 (Dec. 2020).

² *Id.*

³ See generally, U.S. Dep't of Labor Employment and Training Admin., Unemployment Insurance Program Letter No. 20-04 (May 10, 2004). If the localization of work rules creates a problem for an employer, the employer may submit a request for UI coverage under the Interstate Reciprocal Coverage Agreement (IRCA) – a multistate agreement to which most states ascribe. Under the IRCA, an employer may request to source wages of an employee working in multiple states to one of the following: a state where the employee performs service, a state where the employer has a place of business, or the employee's residence state. The request must be in writing and submitted to the affected states.

⁴ See Kearns and Louderback, "Home is Where the Localization Is - Telework and Unemployment Insurance," 30 JMT 8 (Dec. 2020).

⁵ CUI § § 602, 603; California Employment Dev. Dep't, Information Sheet: Multistate Employment (DE 231D), rev'n 12 (Dec. 2017).

⁶ The EDD's COVID-19 FAQ's can be found at https://www.edd.ca.gov/about_edd/coronavirus-2019/faqs/employer.htm.

⁷ *Id.*

⁸ *Id.*

⁹ See U.S. Dep't of Labor Employment and Training Admin., Unemployment Insurance Program Letter No. 20-04 (May 10, 2004), and California Employment Dev. Dep't, Information Sheet: Multistate Employment (DE 231D), rev'n 12 (Dec. 2017).

¹⁰ California Employment Dev. Dep't, Information Sheet: Multistate Employment (DE 231D), rev'n 12 (Dec. 2017) (emphasis added).

¹¹ *Id.* California's SDI withholding includes Paid Family Leave funding, both of which tie-back to the UI localization of work rules. In contrast, some PFML regimes do not directly incorporate the UI localization of work rules. For example, the District of Columbia's

PFML act requires a covered employer make contributions and withhold from the wages paid to a covered employee, where the "[employee's] employment for the covered employer is based in District of Columbia and who regularly spends a substantial amount of his or her work time for that covered employer in the District of Columbia and not more than 50% of his or her work time for that covered employer in another jurisdiction." D.C. Code § § 32-541.01(4)(A), 32-541.03(a).

¹² See M.G.L. c. 175M, § 1, *et seq.*

¹³ M.G.L. c. 175M, § 6.

¹⁴ *Id.*

¹⁵ *Id.* A covered business entity is one that contracts with self-employed individuals for services and is required to report the payment for those services on IRS Form 1099-MISC [1099-NEC] for more than 50 percent of its workforce. M.G.L. c. 175M, § 1. A covered contract worker is a self-employed individual for whom an employer or covered business entity is required to report payment for services on IRS Form 1099-MISC and to remit contributions to the PFML trust fund. *Id.*



to PFML solely because the individual is temporarily working from a location in Massachusetts due to a “Pandemic-Related Circumstance.”¹⁷ Conversely, an individual who previously performed services in Massachusetts but is temporarily working from a location outside of Massachusetts solely due to a Pandemic-Related Circumstance continues to be subject to the PFML rules.¹⁸ For these purposes, the Department defines “Pandemic-Related Circumstance” in the TIR as:

(a) a government order issued in response to the COVID-19 pandemic, (b) a remote work policy adopted by an employer in good faith compliance with federal or state government guidance or public health recommendations relating to COVID-19, or (c) the worker’s compliance with quarantine, isolation directions relating to a COVID-19 diagnosis or suspected diagnosis, or advice of a physician relating to COVID-19 exposure 2 (collectively, “Pandemic-Related Circumstances”).¹⁹

The TIR is effective until 90 days after the state of emergency in Massachusetts is lifted.²⁰ The Department makes clear that as of that date, “the rules set forth in this TIR will cease to be in effect and the presence of an employee in Massachusetts, even if due solely to a Pandemic-Related Circumstance ... will trigger the same tax consequences as under Massachusetts law more generally.”²¹

The Department’s temporary PFML rule is facially similar to its personal income tax (PIT) and wage withholding regulation (830 C.M.R. 62.5A.3) that has garnered so much attention and controversy, especially in regards to New Hampshire residents.²² Though there are similarities between the TIR and the PIT/withholding regulation, there are some differences:

- Most notably, the regulation includes an additional, catch-all prong in the definition of “Pandemic-Related Cir-

cumstance” that is not in the TIR (and hence not in the PFML rule): “any other work arrangement in which an employee who performed services at a location in Massachusetts prior to the Massachusetts COVID-19 state of emergency performs such services for the employer from a location outside Massachusetts during a period in which [the regulation] is in effect.”²³

- At the risk of stating the obvious, another difference between the PFML rule and the PIT/withholding rule are the statutes that underlie the rules. The PIT/withholding regulation’s Pandemic-Related Circumstance rule has faced harsh criticism because it arguably deviates from the ordinary withholding rules based on residency and source.²⁴ However, the TIR’s PFML rule largely comports with the regime’s ordinary sourcing rules, which are based on the Massachusetts localization of work rules.²⁵ In any case, the differing reactions to the TIR’s PFML guidance and the PIT/withholding regulation highlight the significant distinctions between income tax sourcing rules and UI localization rules.
- On a more practical side, Massachusetts PIT is entirely born by the individual employees and can involve material dollars. In contrast, PFML contributions are split between the employer and employee, and do not create as much liability. This is yet another reason why the regulation has generated more opposition and general interest than the TIR’s PFML rule.

Takeaways

Given the uniform adoption of the UI localization of work rules among the states, it would be appropriate for other states to adopt policies similar to California’s FAQs. Also, like the California UI guidance, the Massachusetts PFML guidance appropriately treats Covid-19 remote work as “incidental” to the employee’s pre-pandemic work location. Therefore, absent contrary guidance, employers may consider adopting these reasonable approaches in other states, including bifurcating Covid-19-related telework and permanent teleworking arrangements. ■

¹⁶ Massachusetts Dep’t of Revenue Technical Information Release No. 20-15, Dec. 8, 2020; see also Massachusetts Dep’t of Revenue Technical Information Release No. 20-10, July 21, 2020 (superseded by TIR 20-15) and Massachusetts Dep’t of Revenue Technical Information Release No. 20-5, Apr. 21, 2020 (superseded by TIR 20-5).

¹⁷ *Id.*

¹⁸ *Id.*

¹⁹ *Id.*

²⁰ *Id.*

²¹ *Id.*

²² See *New Hampshire v. Massachusetts*, No. 220154 (U.S. docketed Oct. 23, 2020) (petition pending review), available at <https://www.supremecourt.gov/docket/docketfiles/html/public/220154.html>, and several amici supporting New Hampshire’s challenge of the Massachusetts Pandemic-Related Circumstance wage withholding rule, which is essentially a temporary convenience of the employer test.

²³ 830 CMR 62.5A.3(2).

²⁴ See Kearns, “Give Me Convenience or Give Me Federal Preemption,” 30 JMT 7 (Oct. 2020).

²⁵ M.G.L. c. 175, § 1, -6(c)(1); M.G.L. c. 151A, § 1(k), 1(s)(A), -3. It is worth noting that, while the Department of Revenue administers the Massachusetts PFML act, the Department of Unemployment Assistance administers the state’s UI act. To-date, the Department of Unemployment Assistance has not issued UI guidance that reflects the position in the TIR.



SEEKING ASPIRING AUTHORS

The Journal of Multistate Taxation and Incentives welcomes articles offering practical information and ideas on tax planning for companies involved in multistate operations and transactions, and for individuals with assets or investments in more than one state. In addition, we seek articles on tax and nontax incentives that various governmental authorities offer to attract and maintain business. Articles should focus on matters of importance to practitioners and provide practical information on tax, legal, accounting, and business aspects affecting such taxpayers and transactions, with emphasis on planning possibilities. Articles may be state specific if the topic discussed has far-reaching implications that are of national concern.

Articles submitted for consideration must be sent to us exclusively. They must be at least 6,000 words in length and may be as long as 9,000 words. Articles should be submitted in electronic form and may be accompanied by exhibits. If accepted for publication, the article will be edited to conform with Journal style.

To submit articles, or for more information, please contact:

Journal of Multistate Taxation and Incentives
Jessica Silbering-Meyer, Managing Editor
Thomson Reuters
jessica.silbering-meyer@tr.com