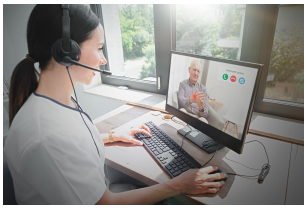

Kentucky Tax Talk: Pandemic Raises Telecommuting Issues

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All employers, whether private corporations, nonprofits or state government agencies such as the Kentucky Department of Revenue, have had to grapple with the effects of executive orders enforcing remote working in response to the COVID-19 pandemic.

As states continue to enforce these orders, and as Kentucky employers — including the DOR — continue to have the majority of their workforce telecommuting, many are wondering what effect this will have on their tax liability and the process for protesting or resolving same.

Tax Effect of Remote Working in Kentucky

While several states have provided express guidance on the tax implications of telecommuting, many have remained silent on the subject. But this is not the only thing to know — an important caveat is that many states maintain tax reciprocity agreements with surrounding states. If an employer is based in a state with a reciprocity agreement with another state in which it now has employees working from home, it most likely will not be required to change its tax withholding practices.

Like many other governors, Kentucky Gov. Andy Beshear issued several executive orders in mid-March, closing nonessential businesses and requiring those with the capability to allow their employees to work from home to do so. Following these executive orders and the growing impact of the COVID-19 pandemic, the Kentucky General Assembly passed S.B. 150 to provide additional relief to struggling Kentucky individuals and businesses.

Included in S.B. 150 was a variety of tax relief provisions, including the power to waive various fees, applications and forms; instructions to the DOR to adhere to federal tax filing and payment extensions; waiving all interest through the extended filing date; and power to extend filing deadlines for local occupational license tax

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returns.

While the DOR, Beshear and the General Assembly have provided significant tax relief and guidance during the COVID-19 pandemic, there has been no expressly stated position as to whether out-ofstate employers will be required to withhold Kentucky income tax on those employees now working from home in the state.

Kentucky borders seven states. Of those bordering states, Kentucky has reciprocity agreements with Indiana, Illinois, Ohio, Virginia and West Virginia. It does not have agreements with Tennessee and Missouri. The state additionally has reciprocity agreements with Michigan and Wisconsin. This means that for any business resident in a state with a reciprocal agreement that now has Kentucky resident employees working remotely, the business will not be required to start withholding Kentucky income tax.

In addition to not issuing any general guidance on the tax implications of telecommuting, Kentucky has also not issued guidance regarding telecommuting nexus for state income or local occupational license taxes. Likewise, local governments in Kentucky have also largely failed to address this issue to date.

Other states, such as Illinois, Indiana and Ohio, have issued express guidance as to tax implications of remote working. Some, such as Illinois, have provided that out-of-state employers will be responsible for withholding income earned at home by Illinois residents, while others have explicitly provided that they will not change existing withholding or nexus requirements. Many other states also have reciprocity agreements that may affect this liability.

With most states following a "doing business" standard, clearly an issue is raised when an employee is working full-time in one state in lieu of working full-time in their normal workplace in another state. Cases are aplenty holding that this circumstance can create not just withholding tax issues, but can also create income or transfer tax liability on the employer.

Unintended Consequences of Remote Working for Kentucky Taxpayers

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In addition to considering withholding and nexus implications of remote working, the DOR's remote working mandates and policies for its own employees over the past few months may cause issues for some taxpayers. While not publicly announced, it is our understanding that while most of the directors and supervisors at the department have returned to the office, the DOR is still only operating at 25% maximum capacity.

Beshear's guidance for government offices and agencies returning to work is that no more than 50% of employees should be physically present at any given moment, and that no more than 33% of the occupational capacity of the facility should be utilized as of May 18. So the DOR's 25% capacity may be an internal policy, or it may be that many of its employees are struggling to return, with the kinds of health and child care concerns that have been felt by many other employers.

The DOR has not resumed in person protest conferences or other appointments with taxpayers, but has been conducting telephonic conferences. It is anticipated that face-toface meetings could start back in August, but some are skeptical about this date. Indiana's DOR, meanwhile, started in-person appointments in late May for many of its district offices, and at its primary downtown Indianapolis office on June 15.

The Kentucky DOR's decision to continue to defer external, in-person meetings could negatively affect taxpayers, in that in-person conferences are typically more effective in helping resolve tax controversies — as opposed to a virtual protest conference via phone or video platforms. This is an important issue, as taxpayers are only statutorily guaranteed one protest conference as a matter of right.

Thus, a taxpayer must decide whether the issue and liability being protested are so timesensitive that they must push forward with a virtual conference, or whether they can wait for an in-person conference, even if it may still be months away. A local tax practitioner's experience with the DOR may be critical for successfully navigating these new challenges.

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The DOR has not issued official guidance on any issues related to COVID-19 since April 17. Thus, local practitioners are continuing to rely on unofficial guidance from DOR contacts to help advise clients. It is important for businesses to understand these new challenges and delays for tax disputes in Kentucky — and the pandemic's effects not only on their own remote employees, but on the DOR's own telecommuting workforce.

For more information, please contact Mark F. Sommer, Daniel G. Mudd, Elizabeth D. Mosley or any member of Frost Brown Todd's Tax practice group. You can also visit our Tax Law Defined Blog to read about the latest developments in federal, state and local taxation.

To provide guidance and support to clients as this global public-health crisis unfolds, Frost Brown Todd has created a Coronavirus Response Team. Our attorneys are on hand to answer your questions and provide guidance on how to proactively prepare for and manage any coronavirus-related threats to your business operations and workforce.

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