Ohio Tax Talk: Adjusting To The Latest Telework Tax Rules

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As the world transitions out of COVID-19 lockdown, one of the most visible pandemic trends in the professional world we can expect to stick around is the shift toward either 100% remote work or a hybrid model combining on-site with work-from-home options.

With many employees pressuring their employers to adopt more lenient work-from-home policies and many employers obliging, municipalities that rely heavily on revenue derived from income taxes are now fighting to keep the revenue stream alive.

This article walks through Ohio's progression of taxing work-from-home arrangements in the pre-COVID-19 and COVID-19 era as well as the implications of the newly enacted H.B. 110.

The Pre-COVID-19 Era: Ohio's Municipal Income Tax and the 20-Day Rule

In our earlier article, we discussed how Ohio's municipal income tax is ordinarily withheld from employee paychecks to be paid to the municipality where the employee's principal place of work is located.[1]

To account for those who occasionally worked from home, Ohio traditionally utilizes a 20-day rule. Under the 20-day rule, employers must withhold municipal income tax for the employee's principal place of work for the first 20 days an employee works in another Ohio municipality, i.e., the nonprincipal place of work municipality,[2][2] and for the nonprincipal place of work municipality for all subsequent days.

Part One of the COVID-19 Era: H.B. 197

Early in the pandemic, municipalities that draw a lot of their revenue from income tax withholdings quickly realized that the work-from-home trend would drastically reduce their income tax revenues thanks to the 20-day rule.

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As a quick fix to the concerns of many major Ohio municipalities that are home to many large businesses, on March 27, 2020, Gov. Mike DeWine signed emergency legislation H.B. 197, which included Section 29 covering municipal income tax. Section 29 froze an employee's principal place of work to where it was on March 9, 2020 and directed employers to disregard the 20-day rule when determining the municipality for which municipal income tax must be withheld.

Section 29 left many questions unanswered and frustrated certain taxpayers. At the root of many frustrations with Section 29 was that employees saw their new work from home arrangements as an opportunity to lower their municipal income tax burdens if they resided in a municipality that had a lower income tax rate than their principal place of business. Section 29 directed employers to disregard the 20-day rule, which somewhat eliminated a tax savings for these employees. As a result, employees were left to file their own municipal income tax refund claims that were overcollected and overpaid by their employer to a location in which they did not work.

Many Ohio taxpayers have filed municipal income tax refund claims on that basis, but it is still uncertain whether cities will honor those refund claims filed for tax year 2020. The application of Section 29 also left employers with lingering questions. For example, Section 29 only applied when employees were "required to report for employment duties
because of the declaration."[3]

In Ohio, the only requirement to work from home was established by the director of Ohio's Department of Health's stay-at-home order issued in March 2020, which expired at the end of May 2020. Employers were left asking: what happens if the company policy requires remote work even after the stay-at-home order lapsed? Is the 20-day rule still applicable in that case? Should the word "required" be read more loosely to mean required by company policy as a
response to COVID-19? Will I be penalized if I don't withhold taxes based on my employee's work-from-home location?

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Part Two of the COVID-19 Era: H.B. 110

On July 1, 2021, the General Assembly enacted, and DeWine signed H.B. 110, Ohio's Biennial Budget Bill. A portion of H.B. 110 clarifies how employers should withhold municipal income taxes. Importantly, H.B. 110 alters the "required" language of Section 29 to read "in response to the COVID-19 pandemic." When a work-from-home policy is enacted by an employer in response to COVID-19, H.B. 110 gives employers options for how to withhold municipal income taxes through Dec. 31, 2021.

First, through the end of 2021, employers can assign any employee to a new or different work location, such as their residence, that may result in a change to the employee's principal place of work. For those newly assigned employees, the employer would be required to withhold and remit tax to the new principal place of work municipality.

Alternatively, through the end of 2021, employers with COVID-19-related remote work policies can withhold based on the employer's office location rather than where the employee resides or works remotely. In other words, employers have the option to utilize the traditional, pre-COVID-19 20-day rule when determining how to withhold for municipal income tax purposes.

Beginning in 2022, the traditional principal place of work set forth in Ohio Revised Code 718.011(A)(7) and the traditional 20-day rule would be reinstated. The provisions in H.B. 110 apply for purposes of municipal income tax withholding and the computation of the employer's municipal net profit tax, but not for purposes of the employee's actual underlying municipal income tax obligation.

H.B. 110 clarifies that an employee may be entitled to a refund for municipal income tax that is overpaid or overcollected by their employer in 2021. Whether employees are entitled to a refund for municipal income tax that was overpaid or overcollected by their employer in 2020 remains an outstanding question and will likely be determined by Ohio courts.

If an employee seeks to obtain a refund from the employee's workplace city because of the COVID-19 withholding rules, that

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workplace city may not require, as a condition for processing the employee's request, any statement or other documentation from the employee's employer, other than: (1) a statement verifying the number of days the employee worked at the employer's workplace city during the year; and (2) a statement that the employer did not refund any withheld taxes to the employee.

H.B. 110 also included special language that provides employers with extra comfort when sorting through the changes in Ohio's COVID-19-era municipal income tax laws. Section 757.40(B) of H.B. 110 provides as follows:

> If any employer withheld and remitted municipal income tax from an employee's
> qualifying wages earned between March 9, 2020, and December 31, 2021, to the
> municipal corporation in which the employee's principal place of work is located, the
> employer shall not be assessed any tax, penalty, or interest by any other municipal
> corporation for failure to situs or apportion those wages to the other municipal
> corporation or for failure to withhold municipal income tax from such wages to the
> other municipal corporation.

While it is still unknown how the state and municipalities will react to the changes generated by H.B. 110, it appears that, by enacting Section 757.40(B) of H.B. 110, the Ohio General Assembly is seeking to protect employers from hidden tax liabilities due to potential noncompliance.

Conclusion

The complexities of Ohio's municipal income tax and its withholding requirements will remain at the forefront of the minds of both individuals and businesses if widespread work from home policies continue. Ohio businesses should carefully analyze their withholding practices and contact their tax advisors to ensure compliance with H.B. 110 and all Ohio law requirements.

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Similarly, individuals who have worked remotely because of COVID-19 should consider whether they have overpaid their municipal income tax liability and may be entitled to a municipal income tax refund.

Local governments should consider the potential impact of H.B. 110 on municipal income tax revenues, issue guidance to taxpayers, establish processes for evaluating refund requests, and possibly reserve funds in anticipation of potential refund claims.

For more information, contact Edward I. Rivin, or any attorney with Frost Brown Todd's Tax practice team.

***Note:** This article was originally published by Law360 (July 29, 2021)*

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[1] ORC 718.011(A)(7).
[2] ORC 718.011(D).
[3] H.B. 197, Section 29.

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