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Virginia Letter Ruling Finds Nexus Based on Employee Working From Home

The Virginia Department of Taxation recently issued a letter ruling which determined that an employee working from home within the state creates corporate income tax nexus.

Letter Ruling

The Virginia Department of Taxation (the Department) recently responded to a request for a letter ruling regarding the issue of whether a single employee working from a home office in Virginia creates corporate income tax nexus for an out of state corporation. Va. Dep’t Tax, Pub. Doc. No. 16-15 (Mar. 3, 2016). The taxpayer is an S corporation headquartered outside of Virginia that provides Internet-based templates for customers to produce their own websites.

The taxpayer has a single employee residing in Virginia and working from a home office. The employee is primarily responsible for bookkeeping and accounting matters, human resources and payroll, customer support conducted entirely by email, and legal consultative matters. The employee does not develop software, program computers, work on website templates, or solicit new customers.

The Department determined that the employee’s administrative and accounting activities from a home office within Virginia are sufficient to create nexus for Virginia corporate income tax purposes. The Department supported its position based on the positive Virginia payroll factor from the compensation paid to the Virginia employee. While the Department noted that *de minimis* activities within Virginia do not create nexus, it lacked sufficient factual information for a full examination of whether the employee’s activities within Virginia are *de minimis* compared to the taxpayer’s overall operations.

Considerations for Employers with Telecommuters

On a multistate basis, there is a split among states regarding whether an employee working from home providing nonsolicitation activities creates nexus, and potential challenges to states' assertion of tax filing obligations may be available depending on the facts. In addition, states may have different requirements depending on the tax type at issue (e.g., corporate tax, sales and use tax, payroll tax). While solicitation activities typically provide a greater connection to the state than nonsolicitation activities (e.g., administrative activities), and thus are more likely to create nexus, Public Law 86-272, a federal statute, prohibits states from imposing corporate income tax on out of state corporations if the corporation's activities within the state are limited to the solicitation of orders for the sale of tangible personal property and the orders are filled from outside the state. Public Law 86-272 does not provide immunity from state taxation for other tax types (e.g., sales and use tax) or from corporate income tax if the corporation is engaged in the solicitation of sales of services or conducts other nonsolicitation activities within the state exceeding a *de minimis* threshold (e.g., delivery, repair, training).

Overall, state taxing authorities have become increasingly aggressive in seeking to assert tax filing requirements on out of state corporations, and the Virginia letter ruling is consistent with the trend. For example, New Jersey and California have both determined that a single employee performing nonsolicitation services from a home office within the state creates nexus for corporate income tax purposes. See *Telebright Corp. v. Dir., N.J. Div. Tax.*, 424 N.J. Super. 384 (N.J. Super. Ct., App. Div. 2012); *Appeal of Warwick McKinley, Inc.*, Cal. State Bd. Equal. No. 489090 (Jan. 11, 2012) (note, the California State Board of Equalization was unable to rule on the constitutionality of the imposition of corporate income tax nexus based on the facts, and anecdotally, we have seen California take the contrary position that an employee working from home providing nonsolicitation services does not create nexus for sales and use tax purposes under certain facts). Similarly, the New York State and New York City regulations each provide that an out of state corporation is subject to corporate tax if it maintains an office, including a salesperson's home, hotel room, or trailer used on a construction site, in the jurisdiction. See 20 N.Y.C.R.R. § 1-3.2(a)(iv), (e); 19 R.C.N.Y. § 11-03(a)(iv), (e).

Telecommuting is becoming increasingly common, and telecommuting employees potentially may risk creating tax filing obligations, including corporate taxes and sales and use taxes, in the telecommuter's state. As such, it is important for companies to consider the potential state and local tax filing requirements as part of developing a telecommuting policy and before approving any employee's request to work from home. In addition, when creating any new presence or activity in a state, it is prudent to consider the specific state and local tax requirements on a state-specific basis.

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