

## ***Zelinsky* — Round 2 of the Convenience of the Employer Test**

by Lynn A. Gandhi

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In this installment of *Smitten With the Mitten*, Gandhi reviews *In the Matter of Edward A. Zelinsky v. Tax Appeals Tribunal of the State of New York* and analyzes how the increase in remote work because of the COVID-19

pandemic could affect the case's outcome.

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There was no doubt it was going to happen because of the pandemic. With the mandated shutdown of workplaces and the requirement for nonessential employees to work from home, a challenge to New York's convenience of the employer rule was anticipated.<sup>1</sup> Particularly as Massachusetts adopted a similar rule in March 2020, with the foresight that the pandemic was going to continue far beyond the time frame initially considered.<sup>2</sup> Ohio adopted a similar rule

<sup>1</sup>N.Y. Comp. Codes R. & Regs. tit. 20, section 132.18(a), which provides: "Any allowance claimed for days worked outside New York State must be based upon the performance of services which of necessity, as distinguished from convenience, obligate the employee to out-of-state duties in the service of his employer." The name of the test is a misnomer and can more aptly be thought of as the "convenience of the employee" test, or, as the New York Court of Appeals has suggested, the more appropriate name would be the "necessity of the employer" test. See *Zelinsky*, n.3. As a reminder for those not familiar with the New York court system, the New York Court of Appeals is the highest-level state court. The New York Supreme Court is the name of the trial-level court.

<sup>2</sup>830 Mass. Code Regs. 62.5A.3, adopted Mar. 5, 2021, effective for services performed from Mar. 10, 2020, through 90 days after the date when the Massachusetts governor gives notice that the Massachusetts COVID-19 state of emergency is no longer in effect.

for purposes of its municipal income taxes, both of which were subject to litigation.<sup>3</sup> While the matter of *New Hampshire v. Massachusetts* is gone, the city of Columbus case continues.<sup>4</sup> What was not necessarily anticipated is that the plaintiff would be none other than the famous professor Edward A. Zelinsky.<sup>5</sup>

As an adjunct law professor, I have assigned the *Zelinsky* case to my students to expose them to the application of the commerce clause and the concept of fair apportionment in the context of income

<sup>3</sup>In Mar. 2020 section 29 of H.B. 197 was enacted to require work performed at home to be treated as if it had been performed at one's workplace for Ohio municipal income tax purposes. The biennial budget bill, signed into law by Gov. Mike DeWine (R) on July 1, extends through Dec. 31, the temporary municipal income tax withholding rule for employers under section 29 of H.B. 197. However, the budget bill amends section 29 to provide that an individual employee's tax liability for wages earned from Jan. 1 to Dec. 31 will no longer be deemed automatically to be the employee's principal place of work, as had been provided under the temporary rule when section 29 was enacted. While employers will still be required to withhold taxes based on an employee's principal place of work, an individual employee's income tax liabilities will generally be determined and allocated between jurisdictions based, in part, on where the employee actually works each day, in accordance with provisions and limitations outlined in chapter 718 of the Ohio Revised Code and other state laws and local ordinances.

<sup>4</sup>*New Hampshire v. Massachusetts*, \_\_\_ U.S. \_\_\_ (2020), motion to file complaint denied. Order List, 594 U.S. 2 (June 28, 2021) (Order: 154, Orig.). The U.S. Supreme Court was no doubt influenced by the amicus brief of the solicitor general. See Brief for the United States as Amicus Curiae, at 4, *New Hampshire v. Massachusetts* (May 25, 2021). This does not mean that the challenge is gone. As noted, a stronger case may be made by residents of New Hampshire who would be subject to the tax and may either receive an assessment if they have failed to pay the tax or for whom a claim for refund is denied. The matter of *The Buckeye Institute v. City of Columbus* continues. *The Buckeye Institute v. Columbus City Auditor and Ohio Attorney General*, Franklin County of Common Pleas, July 2, 2020, 20-CV-004301. *Denison v. Kilgore*, filed by the Buckeye Institute for one of its clients, was filed in Franklin County Court of Common Pleas in Feb. 2021 and settled in favor of Buckeye's client in Apr. 2021. Note that the language adopted by the 2021 biennial budget bill, *supra* note 3, tempers the impact of the case.

<sup>5</sup>The Morris and Annie Trachman Professor of Law at Benjamin N. Cardozo School of Law of Yeshiva University, B.A., 1972, M.A., J.D., 1975, M.Phil., 1978; Yale University. Professor Zelinsky was an editor of the *Yale Law Journal*, a teaching fellow in the Yale University Department of Economics, and law clerk to Judge J. Joseph Smith of the U.S. Court of Appeals for the Second Circuit. Professor Zelinsky represented himself and his spouse, Doris, pro se in *In the Matter of Edward A. Zelinsky v. Tax Appeals Tribunal of the State of New York*, 1 N.Y.3d 85, 801 N.E. 2d 840, 769 N.Y.S.2d 464, cert. denied, 541 U.S. 1009 (2004) (hereinafter *Zelinsky I*), and he was also an author of an *amicus curie* brief filed in support of the state of New Hampshire.

taxation of individuals. The case is always well received, as students easily relate to the working schedule of law professors and comprehend the work-from-home concept. It is also a good case to introduce the regime of state credits afforded to residents for taxes paid to other states, as well as the lack of consistency in the rate at which such credits are calculated and the practical impact that tax rates can have.

### *Zelinsky I*

In *Zelinsky I*, Zelinsky sought a refund for income taxes paid in 1994 and 1995 at the New York Tax Appeals Tribunal.<sup>6</sup> Professor Zelinsky, a Connecticut resident, commuted into New York City three days a week to teach class and meet with students. The rest of the week he worked from home, performing research and scholarly writing, preparing and grading exams, and conducting necessary administrative matters. During the fall of 1995, he was on sabbatical and worked exclusively from home.<sup>7</sup> In preparing his returns for both years, Zelinsky apportioned his salary from Cardozo to New York according to the number of days he commuted to the school, with the remainder of his salary reported to Connecticut. New York issued notices of deficiency, maintaining that the entire amount of his Cardozo salary was subject to tax by New York under the convenience of the employer test, as Zelinsky worked from home for his own convenience and had not been obligated to work outside New York by his employer. The portion of his salary reported to Connecticut was taxed by Connecticut, which did not provide a full credit for taxes paid to New York.<sup>8</sup>

Zelinsky contested the deficiencies and also sought a refund of taxes paid on the salary he earned during his sabbatical, which he had forgotten to allocate in full to Connecticut, claiming that the application of the convenience of the employer test violated the commerce and due process clauses of the U.S. Constitution. Zelinsky

challenged the application of the test under the second prong of *Complete Auto Transit Inc. v. Brady*<sup>9</sup> (that the tax was not “fairly apportioned”) and that it failed the external consistency test.<sup>10</sup>

In rejecting his argument and affirming the decision of the appellate division, which had affirmed the Tax Appeals Tribunal (and the administrative law judge’s rejection of the constitutional challenges), the Court of Appeals reviewed the application of the test to the general regime that limits the state’s taxation of nonresidents to income derived from sources within the state.<sup>11</sup> New York-source income includes income attributable to “a business, trade, profession or occupation carried on in this State.” When a nonresident works both in New York and in another state, New York-source income must be apportioned and allocated according to regulations of the commissioner of taxation and finance.<sup>12</sup>

The New York regulation provides that the apportionment ratio is the days worked in New York to total days worked.<sup>13</sup> This ratio is limited to the extent of the convenience of the employer test, which limits days worked outside the state to only those days for which the employer, by necessity, obligated the employee to perform out-of-state duties, “as distinguished from convenience.” Thus, nonresidents employed in New York who work from home when not required to do so by their employers must treat those days as if they had been present at their work location in New York, with

<sup>9</sup> 430 U.S. 274 (1977).

<sup>10</sup> As noted by the Court of Appeals, “External consistency looks ‘to the economic justification for the State’s claim upon the value taxed, to discover whether a State’s tax reaches beyond that portion of value that is fairly attributable to economic activity within the taxing State. . . . The threat of real multiple taxation . . . may indicate a State’s impermissible overreaching’ (*Oklahoma Tax Commission v. Jefferson Lines Inc.*, 514 U.S. 175, 185 (1995)). External consistency is ‘essentially a practical inquiry’ (*Goldberg v. Sweet*, 488 U.S. 252, 264 (1989)) for determining ‘whether the State has taxed only that portion of the revenues from the interstate activity which reasonably reflects the in-state component of the activity being taxed’ (*Id.* at 262). No particular apportionment formula or method need be used to satisfy constitutional requirements, ‘and when a State has chosen one, an objecting taxpayer has the burden to demonstrate “by clear and cogent evidence” that “the income attributed to the State is in fact out of all appropriate proportion to the business transacted . . . in the State, or has led to a grossly distorted result.”’ (*Jefferson Lines*, 514 U.S. at 195, quoting *Moorman Manufacturing Co. v. Bair*, 437 U.S. 267, 274 (1978)).”

<sup>11</sup> N.Y. Comp. Codes R. & Regs. tit. 20, section 132.18(a).

<sup>12</sup> *Zelinsky I* at 90.

<sup>13</sup> N.Y. Comp Codes R. & Regs. tit. 20, section 132.18(a).

<sup>6</sup> The procedural process consisted of multiple appeals: first to an appeal to an administrative law judge, then to the New York Tax Appeals Tribunal, then to the New York Appellate Division, and then to the New York Court of Appeals.

<sup>7</sup> *Zelinsky I* at 89.

<sup>8</sup> *Id.* Seven states in total now have a convenience of the employer test: Arkansas, Connecticut, Delaware, Massachusetts, Nebraska, New York, and Pennsylvania.

the wages associated with those days treated as New York-source income.<sup>14</sup>

### The Court's Analysis

The Court of Appeals found the application of the test to be constitutional and noted that the test had been adopted to prevent abuses from commuters who could conceivably spend an hour working each weekend day and then claim “2/7 of their work days were non-New York days,” resulting in a lower effective New York income tax rate.<sup>15</sup> The court voiced its concern that further abuse could continue if a nonresident took work home for the evening and weekend, transforming “employment that takes place wholly within New York into an interstate business activity subject to the Commerce Clause.”<sup>16</sup> The court found that as “all of petitioner’s teaching is accomplished in New York,” all salary associated with that employment position was properly allocable to New York.<sup>17</sup> The court noted it was concerned that if such argument was adopted, Zelinsky would be able to avoid taxes that his colleagues who work from home in New York, or at the law school, would pay.<sup>18</sup> The court held that the test neither “unfairly burdens interstate commerce nor discriminates against the free flow of goods in the marketplace. Nor does it result in differential treatment benefiting in-state interests at the expense of out-of-state interests. Rather, the convenience test serves merely to equalize tax obligations among residents and nonresidents, preventing nonresidents from manipulating their New York tax liability by choice of auxiliary work . . . unavailable to similarly situated New York resident employees.”<sup>19</sup>

The Court of Appeals further contemplated the extent to which Zelinsky’s work at home could affect interstate business activity and implicate the commerce clause, finding that New York taxation of his nonresident income would still be fairly

apportioned because of the linkage between his income and the business of teaching. The Court found that as he was hired to teach, it did not matter whether he fulfilled those duties two days a week or five days a week — his salary was for teaching and thus New York sourced. The other functions Professor Zelinsky performed were deemed “ancillary” by the court.<sup>20</sup> The court found that as Zelinsky benefited directly from his employment opportunity in New York and his office located in New York, multiple taxation by New York and Connecticut was due to his own choice of residence and “is not a structural evil that flows from either tax individually, but it is rather the accidental incident of interstate commerce being subject to two different taxing jurisdictions.”<sup>21</sup> As the “New York tax imposed did not ‘reach beyond that portion of value that is fairly attributable to economic activity within the taxing State,’ the taxpayer has failed to demonstrate by clear and cogent evidence that the income attributed to New York was in fact out of all appropriate proportion to the business transacted here or has led to a grossly distorted result.”<sup>22</sup>

### Zelinsky II

On to *Zelinsky II*.<sup>23</sup> The petition filed by Professor Zelinsky contests the application of the convenience of the employer test based on an amended return filed for 2019, which apportioned his Cardozo income based on the days spent in New York.<sup>24</sup> As more than six months passed without a response by the Department of Taxation and Finance, the statute permits a claim may be filed with the Tax Commission.<sup>25</sup> In his petition, Professor Zelinsky requests that the Tax Appeals

<sup>14</sup> *Id.*

<sup>15</sup> *Zelinsky I* at 92.

<sup>16</sup> *Id.* It is not clear why the Court of Appeals believed this to be so horrific. Indeed, it is the rare professional service activity today that is not engaged in interstate commerce.

<sup>17</sup> *Zelinsky I* at 95.

<sup>18</sup> *Zelinsky I* at 94. The court did not address the fact that such colleagues chose to live in New York and had the same opportunities as Zelinsky to live in Connecticut or even New Jersey!

<sup>19</sup> *Zelinsky I* at 94.

<sup>20</sup> This appears to be at odds with the reality of academic positions, many of which place significant emphasis on scholarly research and publishing, as well as administrative duties. The court merely stated that his scholarly writings, even if written at home, solely attached prominence to his position as a professor at Cardozo. The court made no mention of the development of exams nor the grading of same, all of which are also required to complete the task of “teaching” and would appear to be more than “ancillary.”

<sup>21</sup> *Matter of Tamagni v. Tax Appeals Tribunal*, 91 N.Y.2d 530,543 (1998), citing *Jefferson Lines*, 514 U.S. at 192.

<sup>22</sup> *Zelinsky I* at 96, citing *Jefferson Lines*, 514 U.S. at 195.

<sup>23</sup> *In the Matter of Edward Zelinsky*, Case No. 830517, New York State Division of Tax Appeals (hereinafter *Zelinsky II*).

<sup>24</sup> The original return had reported his entire Cardozo salary to New York.

<sup>25</sup> N.Y. Tax Law section 689(c).



Division revisit the impact of the convenience of the employer test, overturn its previous ruling, and grant the requested refund. While recognizing the legal principle of *stare decisis*, Professor Zelinsky provides five additional legal arguments to support a reversal of his prior case.

First, Zelinsky notes the expansion of remote work since his last challenge, especially because of the coronavirus crisis. Intervening New York cases have noted that “precedents should be overturned ‘when the lessons of time may lead to a different result,’” and thus, the convenience of the employer test warrants new consideration.<sup>26</sup> Citing *South Dakota v. Wayfair Inc.*, he urges reconsideration and reversal particularly in light of remote work prompted by COVID-19.

Second, Zelinsky urges that the dissent in a 2005 decision at the New York Appellate Division, which found that the dormant commerce clause requirement of apportionment and the due process clause prohibition on extraterritorial taxation preclude New York taxation on days worked outside the state,<sup>27</sup> be adopted as law.

Third, Zelinsky argues that the decision in *Zelinsky I* failed to properly apply the dormant commerce clause and the due process clause of the U.S. Constitution, and he cites numerous law review articles and other publications by legal commentators that criticized the original holding.

Fourth, Zelinsky argues that as applied to the facts of his employment by Cardozo in 2019, the test produces results that are arbitrary and grossly distorted and thus unconstitutional. By applying the test to apportion zero income to Connecticut, even though most of his workdays in 2019 were spent doing legal scholarship in Connecticut, no income was apportioned to Connecticut. Fair apportionment must be something other than zero.

And fifth, Zelinsky argues that the application of the convenience of the employer test is “economically self-destructive” in the post-pandemic world. The test leads to “irrational tax overreach which encourages individuals to sever their ties with New York.”

A decision in *Zelinsky II* is not expected until 2022. And as noted, there are several levels of appeal, so it may be several years thereafter before a final determination is achieved in the case.

### *Zelinsky III?*

Note that while *Zelinsky II* makes multiple references to the increase in remote work because of COVID-19, the petition itself does not challenge the convenience of the employer test because of the pandemic, as the year at issue is 2019. Could this be *Zelinsky III*? A challenge for 2020 may carry more weight, as the mandated work location closures due to the pandemic required employees to work from home, and to the extent they lived out of state, such work was performed out of state. Indeed, the mandate to work from home would meet the requirement under the test to count as a non-New York day, as such remote work was of necessity and required by employers. There would be little opportunity for the abuse that concerned the Court of Appeals.

However, further pandemic guidance issued by New York in October 2020 noted that if you are a nonresident whose primary office is in New York state, your days working remotely during the pandemic will be considered days worked in the state unless your employer has established a bona fide employer office at your telecommuting location. According to the Department of Taxation and Finance, a government mandate to work from home is not sufficient to treat such day as an out-of-state day. This appears inapposite to the plain language of the test, which would count a day as out of state if required by your employer. The guidance linked to TSB-M-06(5)I, a technical services memorandum that provides the “bona fide employer office” safe harbor rules. These rules permit an out-of-state remote employee credit for days worked out of state if she can establish a bona fide employer office in her home.<sup>28</sup> This guidance is circular in its logic, as it finds an exception to the exception of the convenience of the employer test. The state cannot have it both ways. If the

<sup>26</sup> *Zelinsky II*, citing *People v. Taylor*, 9 N.Y.3d 129, 149 (2007). See also *Matter of Brooke S.B. v. Elizabeth A.C.C.*, 28 N.Y.3d 1, 23 (2016).

<sup>27</sup> Citing Judge Robert Smith’s dissent in *Huckaby v. N.Y. State Division of Tax Appeals*, 4 N.Y.3d 427, 440 (2005).

<sup>28</sup> According to TSB-M-06(5)I, there are a number of factors that determine whether your employer has established a bona fide employer office at your telecommuting location. Importantly, the employer must have taken specific action to establish an office at your telecommuting location. With this factor, the remote worker will owe New York state income tax on income earned while working remotely.

precedence of *Zelinsky* still controls, the test dictates that pandemic-mandated remote work days be treated as non-New York days. The remote work was mandated and required; employees had no option. How and why should the factors of TSB-M-06(5)I apply?

The concept that office work will be “transformed into interstate commerce” has already occurred, particularly given the “work from anywhere” recruitment tool that has been readily adopted since the pandemic, and for which there is a great demand. An employer knowing that it will be hiring an employee who is resident in another state should be deemed a tacit acknowledgement that work for the business enterprise will be performed in another jurisdiction. Treating such services as if performed “at the workplace” would violate the external consistency test and ignore the “protection and benefits” provided by the employee’s state of residence, which inure to the employer’s benefit. If Professor Zelinsky was teaching via Zoom during 2020, which Zelinsky has acknowledged he was, then clearly all his teaching was not accomplished in New York. And further, how does this affect his employer? While his employer is an academic nonprofit organization without concern for state income taxes, what about the failure to withhold Connecticut income tax from Zelinsky’s salary? What will the Tax Appeals Tribunal decide if faced with a 2020 challenge to the convenience of the employer test? That the employer failed to establish a bona fide work location? There was no voluntary nature to the performance of Zelinsky’s work in Connecticut for 2020, and his employer was certainly aware that he fulfilled his teaching obligations while working remotely from his home in Connecticut.

### Conclusion

As is often the case in state tax, further challenges lurk around the corner. U.S. companies are now faced with tracking where their employees are actually located when working remotely. Only a few businesses require daily geographic recordkeeping. The concept of work from anywhere (or everywhere) is not sustainable as an efficient practice under current administrative payroll and benefit regimes. The desire to pivot quickly to a new work model should not be

executed in haste and must be supported by the withholding and unemployment insurance reporting requirements of the states, to say nothing of medical benefit networks and other labor and employment guidelines. There are challenging times ahead as this new model expands.

Further, imagine the incentives the Empire State could provide to entice schools of higher learning to establish locations in New York if the *Zelinsky I* decision is upheld. If a school had a brick-and-mortar shell somewhere in the state and offered most of its classes online to students around the globe, taught by instructors located in multiple states and countries, think of the taxes New York could collect from the instructors, as well as tuition charges. With this revenue, perhaps it could offer incentives for all great schools to establish a location in the state. Would the justification that the Court of Appeals relied on, that the “economic justification in taxing petitioner’s income begins with the fact that his entire source of his disputed income is a law school located in New York,” still apply? The Court of Appeals further stated that “the taxpayer is able to earn his salary — all of it — because of the benefits he receives every day from New York.”<sup>29</sup> What about the benefits and protections the law school receives from the states and other countries where its remote students are located? Aren’t the students themselves the market for the law school’s (and hence, Zelinsky’s) services? If the student roster is known at the start of class, would it be more appropriate for the law school to apportion Zelinsky’s salary among those jurisdictions in which the students are located, particularly if the students participate remotely? Stayed tuned — interesting times indeed lie ahead. ■

<sup>29</sup> *Zelinsky I* at 95.