

Department of Revenue

Revenue Notice # 08-10: Individual Income Tax and Withholding – Wages of Nonresident Individuals Assigned to Minnesota for Work Performed in Minnesota – Revocation of Revenue Notice # 01-10

Introduction

For nonresident individuals, *Minnesota Statutes*, section 290.17, subdivision 2, provides that income from wages as defined in section 3401(a) and (f) of the *Internal Revenue Code* is assigned to Minnesota to the extent that the work of the employee is performed in Minnesota. Income assigned to Minnesota is subject to Minnesota individual income tax and withholding tax.

Legislation in 2008 eliminated an exclusion from taxable income for work performed in Minnesota by a Minnesota resident and received when the taxpayer was a full-year nonresident. The 2008 legislation applies to taxable years beginning after December 31, 2007. Payers are required to withhold Minnesota tax beginning with payments made after April 1, 2008.

Nonetheless, federal law (title four of the *United States Code*, section 114; codified in *Minnesota Statutes*, section 290.17, subdivision 2) prohibits state taxation of “retirement income” paid to nonresidents. This generally includes, but is not limited to, income from:

- qualified pension plans, qualified annuity plans, or qualified individual retirement plans;
- nonqualified plans that would have been qualified plans had applicable income thresholds not been exceeded; and
- nonqualified plans where payments are made in at least ten substantially equal annual installments or over the life of the ex-employee.

Additionally, to the extent income recognized by a nonresident on the sale of stock purchased through statutory stock options (*Internal Revenue Code*, sections 422 and 423) is not wages under section 3401(a) and (f) of the *Internal Revenue Code*, it is not assignable to Minnesota.

Three main sources of deferred income from wages remain: (1) severance pay, (2) equity based awards, and (3) other non-statutory deferred compensation. The extent to which these sources when recognized by a nonresident are assigned to Minnesota constitutes the subject of this notice.

Department Position – Severance Pay

If an employer pays a nonresident with severance pay, the resulting income from wages is assigned to Minnesota to the extent that work connected with the employment from which the payment is received was performed in Minnesota.

Department Position – Equity Based Awards

If an employer pays a nonresident with an equity based award, including non-statutory stock options, stock appreciation rights, or restricted stock, the resulting income from wages is assigned to Minnesota in the ratio of days worked in Minnesota during the “allocation period” to the total number of days worked during the “allocation period.”

The allocation period begins on the date the equity based award is granted and ends at the earlier of (1) the date the award or corresponding stock is substantially vested or (2) the date the award or corresponding stock is sold.

Department Position – Other Non-Statutory Deferred Compensation

If an employer pays a nonresident with other non-statutory deferred compensation, the resulting income from wages is assigned to Minnesota in the ratio of days worked in Minnesota during the “allocation period” to the total number of days worked during the “allocation period.” The allocation period is the period of time during which the employee accrued the right to the deferred compensation.

Department Position – Administrative Guidance

The department recognizes that the change in law may initially place administrative burdens on employers as they improve their administrative systems to comply with the 2008 law change. When allocation issues arise that could result in penalties for failure to withhold the correct amount of tax due to limited historical data available to the employer, the taxpayer may request abatement under *Minnesota Statutes*, section 270C.34 and as further illustrated in Revenue Notice # 97-01. Whether to grant an abatement request remains a case-by-case determination based on reasonable cause.

This Revenue Notice revokes Revenue Notice # 01-10.

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for Tax Policy and External Relations

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