

GIL 21-18-1 Nonresident Income Tax Withholding for Personal Services

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October 5, 2018

Dear XXXX,

Guidance has been requested from several taxpayers about what level of presence in Nebraska is necessary to determine if personal services are being provided “substantially in Nebraska,” thus requiring a payor maintaining an office or conducting business in Nebraska¹ to withhold income tax from payments to nonresident individuals that are in excess of \$600.² This issue arises frequently when the nonresident individual³ in question visits Nebraska one or more times to conduct onsite testing, research, consultation, or other activities; and also spends much of his or her time outside Nebraska at the home office, for example, performing important activities such as analyzing data, consulting with other professional colleagues, or writing a report. Under these circumstances, how is the payor to determine if the professional services were “substantially performed in Nebraska” and therefore subject to the income tax withholding required by [Neb. Rev. Stat. § 77-2753\(2\)](#). To provide guidance to taxpayers throughout the state, the Nebraska Department of Revenue (Department) has decided to answer this question by issuing a General Information Letter (GIL).

GILs address general questions; provide analysis of issues; and direct taxpayers to the Nebraska statutes, Department regulations, revenue rulings, or other sources of information to help answer a question. A GIL is a statement of current Department policy, and taxpayers may rely on the Department to follow the principles or procedures described in a GIL until it is rescinded or superseded. You may also find current regulations, revenue rulings, information guides, taxpayer rulings, and other GILs at revenue.nebraska.gov that may be helpful to you.

[Section 77-2753](#) contains no definition or other instruction as to what “substantially performed in Nebraska” means. Consequently, the Department must discern the common and ordinary meaning of the word “substantially.” The Oxford English Dictionary defines “substantially” as “to a great or significant extent” and “for the most part; essentially.” [Dictionary.com](#) defines the term as “of ample or considerable amount” and “basic, or essential; fundamental.” These definitions imply that “substantially” has both a qualitative and a quantitative aspect. That is, the importance of the activity that must be performed in Nebraska and the amount of the activity that is performed in Nebraska both contribute to the determination of what is “substantial.”

Recognizing that this definition remains mixed and indefinite, the Department believes that it is in the best interests of both the state and the taxpaying public that the income tax withholding on personal services performed by a nonresident should be administered in a way that simplifies the analysis to the greatest extent possible and allows the payor to make an objective assessment. The payor is in position to know which activities it requires to be performed in Nebraska and which may be performed anywhere.

¹ Or making payments in excess of \$5,000.

² This income tax withholding requirement is in Neb. Rev. Stat. § 77-2753(2).

³ Or a corporation, partnership, or limited liability company that receives compensation for personal services in this state and of which all or substantially all of the shareholders, partners, or members are the individuals performing the personal services per Neb. Rev. Stat. § 77-2753(2)(c).

Consistent with this viewpoint, the Department has determined that the withholding requirement applies, unless it is clear based on the terms of service and the circumstances that: (a) no essential activities must be performed in Nebraska; or (b) if no essential activities must be performed in any particular state, more activities will be performed in another state than will be performed in Nebraska. When either of these circumstances are true, the parties may execute Form W-4NB, Nonresident Individuals Performing Personal Services in Nebraska, to document why the income tax withholding does not apply.

To be essential activities taking place in Nebraska, the activities must be performed in Nebraska to satisfactorily complete the services. This can be determined by the contract or the terms of the engagement. If the services cannot be performed satisfactorily without performing certain activities in Nebraska (that are more than de minimis) the services are considered to be performed substantially in Nebraska. If the activities that must be performed at a particular location must occur in more than one state, the payor may limit the withholding to the portion of the contract that reflects the relative number of activities essential to Nebraska compared to all essential activities. If no essential activities are required to be performed in any particular state, Nebraska withholding applies only if the greater portion of the service will be performed in Nebraska, as compared to any other state.

Example 1. A Nebraska business pays an out-of-state consultant to update its human resource department procedures. The contract requires the consultant to make one on-site visit to view the operation in person and another on site visit to present the final report to the board of directors of the company in person. The first on-site visit is anticipated to be a half day with an overnight stay and the presentation should be an hour with no overnight stay. The contracted price assumes the consulting firm spends 200 hours on the contract, all of the rest of which will takes place at the home office. Because the on-site visit and report presentation are essential activities that are required by the payor to be performed in Nebraska, the services are substantially performed in Nebraska and income tax withholding is required on the full contract price.

Example 2. An advertising agency that is a nonresident sole proprietorship makes a presentation in person to a Nebraska business to develop a new advertising campaign for the business. The sole proprietorship is successful and agrees to develop several print and video advertisements consistent with the presentation. The photographs, graphics, and clip art are obtained from common sources available anywhere and the agency hires a local video production company to shoot some film of the business that he may use. The agency owner has other clients in Nebraska and maintains a small office in Nebraska where he works once a week. He is also on site for the video shoot, but the shoot could have been completed without him. However, most of the work for this client will be performed while he is in the Nebraska office in case something comes up that may require personal observation. In this situation, none of these essential tasks must be performed in Nebraska. The up-front presentation is not essential because it was not part of the services the payor was seeking, and generated no obligation on the payor. However, since more of the work will be performed while in Nebraska than any other state, the payment is subject to withholding on the full contract amount.

Example 3. A nonresident engineering consultant is performing a contract for services in Nebraska. The nonresident individual voluntarily attends one 2-hour meeting in Nebraska at the beginning of the project to simply meet the individuals he will be working with and be given an overview of the project. The engineering services are all completed at the engineer's office outside of Nebraska. All future meetings are held by video conference. In this situation, the tasks performed in Nebraska are not essential to the successful completion of the engagement. In addition, the duties are predominantly performed in another state.

Example 4. An engineering firm consisting entirely of nonresident partners is hired to examine and test the efficiency of all of a Nebraska manufacturing company's facilities. These inspections and tests typically take three full days per manufacturing facility to complete. The company has three manufacturing plants in Nebraska, one in Kansas and one in Iowa. After the inspections and testing, the engineering firm believes it will commit 2,000 hours to study the inspection and testing results, develop recommendations, and package its recommendations into a 500-page detailed report and two-hour PowerPoint presentation to the manufacturing company's Board which could be presented in person or via Skype. The essential duties that must be performed on-site are the inspections and testing at the factories, 60% of which are in Nebraska and 40% of which are in other states. In this situation, withholding is required on 60% of the contract price.

To summarize, the requirement to withhold income tax from payments in excess of \$600 does not apply when the agreement between the payor and the nonresident individual makes it clear that: (a) no activities must be performed in Nebraska and (b) if no activities are required to be performed in any particular state, the most hours performed in any single state are performed in a state other than Nebraska. The payor and payee should execute a [Form W-4NB, Nonresident Individuals Performing Personal Services in Nebraska](#), when applicable. If the requirements of the service or the circumstances change substantially, the payor and payee should reconsider whether a Form W-4NB continues to reflect the understanding of the parties and whether the withholding requirement should apply. Failure to reconsider will not relieve the payor from liability when the facts and circumstances change.

If the payor accepts or reconsiders an acceptance of a Form W-4NB in good faith, the payor will not be liable for withholding with respect to the personal services that are provided by the nonresident individual.

Please note that, whether or not income tax withholding is required by [Neb. Rev. Stat. § 77-2753\(2\)](#), nonresident individuals with Nebraska source income are required to file a [Nebraska Individual Income Tax Return, Form 1040N](#), and the accompanying [Nebraska Schedule III](#).

For the Tax Commissioner

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