

BRIGHTADVISOR®

Multi-State Payroll Guide

Navigating Nexus Rules, Withholding, Reciprocity, and Local Tax Compliance

The Complexity of Multi-State Payroll

When employees work across state lines, whether through remote work, travel, or multi-site operations, payroll compliance becomes significantly more complex. Each state has its own income tax rules, unemployment insurance requirements, and local tax obligations. Getting multi-state payroll wrong leads to penalties, back taxes, and employee dissatisfaction.

The rise of remote work has dramatically increased multi-state payroll complexity. Over 35% of U.S. workers now work remotely at least part time, often creating tax obligations in states where the employer has no physical office.

Understanding Nexus and Withholding Obligations

Nexus is the connection between your business and a state that creates a tax obligation. Having even one employee working in a state can create payroll tax nexus.

Nexus Trigger	Withholding Required?	SUI Registration?	Notes
Employee works in the state	Yes	Yes	Most common trigger for payroll nexus
Employee resides in the state	Typically yes	Depends on work state	Even if working remotely for out-of-state employer
Temporary travel to the state	Varies	Usually no	Some states have de minimis thresholds (days or dollars)
No income tax in the state	N/A	Yes (SUI still applies)	AK, FL, NV, NH, SD, TN, TX, WA, WY
Convenience of employer rule	May apply	Depends	CT, DE, MA, NE, NY, PA apply this rule

New York's "convenience of the employer" rule taxes non-resident remote workers as if they worked in New York unless the employee's out-of-state work is required by the employer for a bona fide business purpose. Several other states follow similar rules.

State Income Tax Withholding

Determine the correct state for income tax withholding based on where the employee performs work and where they reside. When an employee works in multiple states, you may need to withhold in more than one.

General Withholding Rules

1. Withhold in the state where work is physically performed (work state)
2. If the work state has no income tax, withhold only for the resident state (if applicable)
3. If a reciprocity agreement exists, withhold only for the resident state
4. Without reciprocity, withhold for both work state and resident state (employee claims credit)
5. Track days worked in each state for employees who split time across states

Common Reciprocity Agreements

Reciprocity agreements allow employees to pay income tax only in their state of residence, simplifying withholding. The employee must file a reciprocity exemption form with the work state.

State	Has Reciprocity With
Arizona	CA, IN, OR, VA
Illinois	IA, KY, MI, WI
Indiana	KY, MI, OH, PA, WI
Kentucky	IL, IN, MI, OH, VA, WV, WI
Maryland	DC, PA, VA, WV
Michigan	IL, IN, KY, MN, OH, WI
Ohio	IN, KY, MI, PA, WV
Pennsylvania	IN, MD, NJ, OH, VA, WV
Virginia	DC, KY, MD, PA, WV
Wisconsin	IL, IN, KY, MI, MN

Always obtain a completed reciprocity exemption certificate from the employee before applying a reciprocity agreement. Without the certificate, you must withhold for the work state.

State Unemployment Insurance (SUI)

SUI registration is required in every state where you have employees performing work, regardless of income tax obligations. Each state sets its own tax rate, wage base, and reporting requirements.

SUI Registration Checklist

Action	Timeline	Status
Register with state workforce agency	Before first payroll in the state	
Obtain state employer account number	Upon registration approval	
Determine assigned SUI tax rate	New employer rate until experience rating established	
Identify state wage base	Ranges from \$7,000 to \$62,500+ depending on state	
Set up quarterly SUI reporting	File Form 940 equivalent for each state	
Track employee wages against state wage base	Stop withholding after employee hits wage base	
Apply for voluntary contribution (if beneficial)	May lower your SUI rate in some states	

Local and City Tax Compliance

Many cities and counties impose their own income taxes or payroll taxes in addition to state taxes. These are commonly found in Ohio, Pennsylvania, Kentucky, Indiana, Maryland, and select cities in other states.

- Ohio: Over 600 municipalities levy local income tax (rates typically 1-3%)
- Pennsylvania: Local earned income tax (EIT) and local services tax (LST)

- Kentucky: Occupational license taxes in many cities and counties
 - Indiana: County income taxes with varying rates
 - New York City: Separate income tax for residents
 - San Francisco, Portland, others: Local payroll taxes and transit taxes
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Multi-State Compliance Best Practices

1. Maintain a state-by-state registration tracker with account numbers and filing frequencies
2. Use payroll software or a PEO that handles multi-state tax calculations automatically
3. Require remote employees to report any changes in work location immediately
4. Review nexus exposure annually as workforce distribution changes
5. Keep reciprocity certificates on file and renew as required
6. Consult with a tax professional for complex scenarios involving multiple high-tax states

BrightWealth® PEO partners handle multi-state payroll registration, withholding, filing, and compliance across all 50 states. As your workforce grows and disperses, our systems scale automatically to keep you compliant in every jurisdiction. Contact us for a complimentary multi-state payroll review.