Indiana Department of Revenue

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Income Tax Information Bulletin	#28
Subject:	Application of State and County Income Taxes to Residents with Out-of-State Income and Nonresidents with Indiana Source Income
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Replaces Bulletin #28, dated November 2023

Summary of Changes

Other than nonsubstantive, technical changes, this bulletin has been updated to clarify treatment of compensation when a nonresident performs services outside Indiana and to provide guidance regarding the income tax exemption for compensation for employees who work in Indiana 30 days or less per year.

Introduction

Full-year Indiana residents must report all income that is reported for federal income tax purposes on their Indiana individual income tax return (Form IT-40). This includes all income, even if it is derived from sources outside Indiana.

Full-year nonresidents who received income from Indiana sources must file an Indiana individual income tax return (Form IT-40PNR). They are subject to tax on that part of their total federal income that is derived from or connected with Indiana sources. If the nonresident's only Indiana source income was from an Indiana partnership or S corporation, the nonresident shall be included in the entity's composite return and is not required to file Form IT-40PNR, though the individual may file a Form IT-40PNR if the individual chooses to do so.

Part-year Indiana residents must file an Indiana individual income tax return (Form IT-40PNR). They are subject to tax on that part of their total federal income that was received while they were residents of Indiana. In addition, they are also taxable on income from Indiana sources received while they were nonresidents of Indiana.

If a joint federal income tax return is filed, a joint Indiana return is also required. If separate federal income tax returns are filed, separate Indiana returns are also required. If one spouse is a full-year Indiana resident, the other spouse is a nonresident for all or part of the year, and the spouses file a joint federal income tax return, the couple must file a joint Form IT-40PNR, reporting their respective incomes as stated above.

Income Received from Indiana Sources

Income received from Indiana sources is considered Indiana income to nonresidents, except certain types of Indiana source income subject to tax only by the taxpayer's state of legal residence. Interest, dividends, royalties, and gains from the sale of capital assets are subject to tax only by the taxpayer's state of legal residence unless such income results from conducting a trade or business in Indiana or from the sale of real or tangible personal property located in Indiana. If a trade or business is conducted in Indiana, or real or tangible personal property is located in Indiana, the income should be reported as Indiana income.

Income from a qualified pension, annuity, or profit-sharing plan is subject to tax by the taxpayer's state of legal residence. Lump sum distributions from qualified plans are subject to tax by the state that, at the time of distribution, is the taxpayer's state of legal residence.

Deferred compensation other than from a qualified retirement plan, accumulated vacation, bonus, severance, sick pay, or income from a stock option plan are directly attributable to services performed and are taxable by the state where the services were performed.

For nonresidents, compensation is earned in the state in which services are actually performed, regardless of whether the compensation is being performed for an Indiana-based employer. This includes remote work performed outside Indiana and other work performed outside Indiana for the convenience of the employer.

State Tax Agreements

Taxpayers may be subject to individual income tax by both their state of residence and the state from which the income is derived. The state of Indiana has entered into agreements with several states to eliminate the requirement of paying tax to two states on the same income. Tax treatment of out-of-state income depends upon the type of income and the state from which the income is derived.

In the case of tax credits, Indiana only allows credits for individual income tax paid to other states or localities. Other taxes such as property taxes, corporate income taxes, and unincorporated

business taxes are not allowed as a basis for claiming such credits. To claim this credit, a worksheet indicating how the credit was computed must be provided. The following information must also be provided:

- A copy of the other state's tax return, if one is filed.
- If a return from another state is not filed and the credit is for nonresident composite tax or pass through entity tax paid by a pass-through entity,
    - A K-1 or similar information statement by the entity from the other state showing the credit, or
    - In the case where a pass-through entity has filed for several states, a statement from the entity with a breakdown of the income and tax paid by jurisdiction.

Information from a statement other than a K-1 or K-1 equivalent will be considered on a case-by-case basis.

- For credits of taxes paid to a foreign country:
    - A copy of Federal Form 1116 (Computation of Foreign Tax Credit)
    - If the credit is such that Federal Form 1116 is not required to be filed or all necessary underlying information is available on another federally-required form, a copy of Form 1099-DIV or an equivalent statement showing the foreign tax paid.

Do not include a withholding statement such as a Form W-2. Include a Form W-2G only if you did not file a return in the other state.

In computing the credit allowed by Indiana, adjusted gross income that is subject to tax in both states should be used as a basis for calculating the allowable credit. Adjustments that increase or decrease the taxable amount in other states should not be considered in calculating the allowable credit. For example, State A allows a deduction for medical expenses, but Indiana does not; therefore, the credit would be based on the income before the medical expense deduction.

Reciprocal Agreement States

Five states have a reciprocal agreement with the state of Indiana. They are Kentucky, Michigan, Ohio, Pennsylvania, and Wisconsin. All salaries, wages, tips, and commissions earned in these states by an Indiana resident must be reported as if they were earned in Indiana. A credit cannot be taken for any state taxes withheld by or paid to any of these states in connection with income from salaries, wages, tips, and commissions. If taxes have been withheld or paid to any of these states, a claim for refund should be filed with that state by filing that particular state's income tax form for nonresidents.

Residents of Kentucky, Michigan, Ohio, Pennsylvania, and Wisconsin who have Indiana income will report and pay state income tax on that income to their state of residence. The reciprocity agreements do not cover local income taxes.

With regard to income from sources other than salaries, wages, tips, and commissions, that income is **not** covered by a reciprocity agreement. For Indiana purposes, income from other

sources and taxes on that income are treated in the manner as it would be for a state discussed below.

If a resident of one of the above states has wages, salaries, tips, or commissions from Indiana sources, and the individual's only income from Indiana sources is wages, salaries, tips, or commissions, Form IT-40RNR must be filed. A credit for Indiana state and county tax withholding amounts will be allowed, and any Indiana county tax liability will be figured. If a resident of one of the above states has income from Indiana other than wages, salaries, tips, or commissions, Form IT-40PNR must be filed.

Reverse Credit Agreement States

The reverse credit agreement applies to Indiana residents who have income from the following jurisdictions and to residents of those jurisdictions who have income from Indiana. Included are Arizona, Oregon, and Washington, D.C. However, for Washington, D.C., the reverse credit treatment does not apply to the unincorporated business franchise tax (Form D-30) actually imposed on an individual. Instead, the Washington D.C. unincorporated business franchise tax will be treated in a manner similar to taxes from states with no agreement with Indiana (see below).

For example, a resident of Indiana with rental income from property owned in a reverse credit state will file a resident Indiana return and include the rental income on the Indiana return. The taxpayer will file a nonresident return for the state where the income was earned and claim a credit for the taxes paid to Indiana on the rental income.

A resident of a reverse credit state with income from Indiana will file a resident return with their state of residence and include the Indiana income. The taxpayer will then file an Indiana Form IT-40PNR and claim a credit for taxes paid to the state of residence for the Indiana source income.

States with No Agreement with Indiana

When a person receives income from any state, possession, or foreign country other than those covered in sections on Reciprocal Agreement States and Reverse Credit Agreement States, the taxpayer might be required to pay income taxes to both jurisdictions. The taxpayer may take a credit for taxes paid to other states against the taxpayer's Indiana adjusted gross income tax liability.

The credit is equal to the least of the following:

- The amount of income tax actually paid to the other state, possession, or foreign country on income from that jurisdiction
- An amount equal to the Indiana income tax rate multiplied by the adjusted gross income taxed by both Indiana and the jurisdiction
- The amount of Indiana adjusted gross income tax due to Indiana for the tax year

List of states with no agreement:

Alabama	Kansas	New Jersey	Washington

Arkansas	Louisiana	New Mexico	West Virginia
California	Maine	New York	
Colorado	Maryland	North Carolina	
Connecticut	Massachusetts	North Dakota	
Delaware	Minnesota	Oklahoma	
Georgia	Mississippi	Rhode Island	
Hawaii	Missouri	South Carolina	
Idaho	Montana	Utah	
Illinois	Nebraska	Vermont	
Iowa	New Hampshire	Virginia	

This credit is only available for taxes for which the taxpayer is personally liable. Taxes imposed directly at the entity level generally are not eligible for this credit. However, for tax years 2019 and later, a pass through entity tax imposed after 2017 by another state similar to the Indiana pass through entity tax imposed under IC 6-3-2.1 is eligible for this credit as a result of P.L. 1-2023 (SEA 2-2023). This also includes an individual's share of other states' elective pass through entity taxes where the effect is to exclude pass through entity income otherwise required to be included in the individual's income from the other state. Information similar to that required for composite taxes will be required to substantiate this credit. Any refund claims for out-of-state pass through entity taxes are subject to provisions of IC 6-8.1-9-1 for timeliness. A composite tax similar to those imposed under IC 6-3-4-12, IC 6-3-4-13, and IC 6-3-4-15, is eligible for the credit.

Local Income Tax Credit

All Indiana residents who are subject to a county income tax and also required to pay income taxes to a locality outside Indiana are allowed a credit against their Indiana county tax liability. This credit is allowable for local income taxes paid to a locality of another state even if the income is exempt from state-level taxation as a result of a reciprocity agreement.

The credit for taxes paid to a locality outside Indiana must be supported by a separate calculation of the credit. If the taxpayer is required to file a return with the locality in another state, a copy of the return must be submitted with the claim for credit. Withholding statements or other evidence of tax payment will be acceptable if no return is required to be filed with the locality outside Indiana.

The allowable credit is equal to the least of:

- The amount of income tax actually paid to a locality in another state
- The amount of adjusted gross income taxed by the locality outside of the state of Indiana multiplied by the county rate to which the taxpayer is subject
- The amount of county tax due on the Indiana return

The credit should be computed separately for each portion of income taxed by a locality in another state. In addition, on a joint return, the credit should be calculated separately for the husband and wife. Any unused credit attributable to one spouse cannot be used to reduce the other spouse's county tax liability.

This credit is only available for taxes for which the taxpayer is personally liable. Taxes imposed directly at the entity level, including but not limited to pass through entity taxes imposed as a federal, state and local tax limitation workaround, are not eligible for this credit. This disallowance applies even if the taxpayer would be subject to out-of-state local income taxes except for a credit against the taxpayer's tax for entity-level taxes. However, a composite local income tax similar to those imposed under IC 6-3-4-12, IC 6-3-4-13, and IC 6-3-4-15, is eligible for the credit.

Information similar to what is provided for the state income tax credit is required for the local income tax credit. However, in the case of localities that do not require local income tax returns under normal practice for nonresident employees, taxes reported on Form W-2 will be accepted if the individual does not file a return for that locality.

Special Rules for Employees Who Work in Indiana for 30 Days or Less in a Calendar Year

For 2024 and later, IC 6-3-2-27.5 permits an income tax exemption for employee compensation if the employee is a nonresident of Indiana and works less than 30 days during a calendar year (the "30-day safe harbor"). This exemption does not apply to individuals who are any of the following:

- Indiana residents for any portion of the taxable year
- Professional sports team members, including players, coaches, and other personnel included in the definition of team member provided in IC 6-3-2-2.7(a)(4)
- Race team members, regardless of whether the individual is an employee or an independent contractor
- Other professional athletes who are not professional sports team members or race team members
- Professional entertainers who receive compensation as a professional on a per-event basis
- Public figures, defined as a person of prominence who performs services at discrete events, including speeches, public appearances, and similar events, and are paid on a per-appearance basis

For the last five categories, if an individual is in one or more of those categories for any part of the year, the individual will be treated as not qualifying for the 30-day safe harbor.

The 30-day safe harbor applies only to compensation received as an employee. The 30-day safe harbor does not apply to income other than compensation, including but not limited to:

- Self-employment income
- Income received as an independent contractor

Income other than compensation received from a pass-through entity, such as net income reported on Schedule IN K-1 or IT-41 Schedule IN K-1

- Income from the sale or exchange of property attributable to Indiana

The 30-day safe harbor also does not apply to deferred compensation from Indiana sources unless all of the following conditions are met:

- The individual qualified for the 30-day safe harbor for the year in which the compensation was earned
- The individual performed the services generating the deferred compensation in 2024 or later
- The individual is not an Indiana resident at the time the deferred compensation is paid.

For purposes of determining whether a particular workday counts toward the 30-day safe harbor, the following apply:

- An employee must be physically present in Indiana for a workday to count.

Remote work is considered to be performed at the location where the actual work occurs regardless of the employer's location. For instance, a Kentucky resident working remotely from their Kentucky residence will be treated as working from Kentucky. If that same employee worked remotely from a home in Indiana, the employee will be treated as working in Indiana.

If an employee works in two or more states on the same day, the following apply:

  - If an employee works only in Indiana and the employee's state of residence, the employee will count the workday as an Indiana workday.
  - If an employee works in Indiana and also works in one or more states other than the employee's state of residence, the employee will treat the workday as being attributed to the state in which the employee performed work the longest.
  - Any portion of the day in which the employee is in transit shall not be counted as time for purposes of attributing time to a state.

If an individual works for an employer in a non-employee capacity (e.g., an independent contractor) and as an employee with substantially similar job duties, the days worked in a non-employee capacity count toward the 30-day safe harbor. In addition, the days worked in a non-employee capacity count regardless of the amount of work performed in Indiana. Further, the employee is not relieved of tax on non-employee compensation regardless of the number of days worked in Indiana.

If an employee exceeds the 30-day limit, the employee is taxable on all compensation from the first day. However, if the employee is a resident of a reciprocal state, that exemption from state income tax continues to apply.

Withholding Requirements for Indiana Residents with Out-of-State Income

When an Indiana resident earns wages in another state that also levies a withholding tax on wages and the nonresident employer does not have a business connection with Indiana, the employer is not required to withhold Indiana state and local income tax. **NOTE**: It might be prudent for the employer to voluntarily withhold state and local income taxes on behalf of the employee or for the employee to make estimated income tax payments in accordance with the provisions in Income Tax Information Bulletin #3, available at in.gov/dor/resources/tax-library/information-bulletins/.

When an Indiana resident earns wages in another state that also levies a withholding tax on wages and the nonresident employer has a business connection with Indiana, the employer is required to withhold both Indiana state and local income taxes, pursuant to IC 6-3-4-8(a). However, in this situation, Indiana state tax should be withheld only to the extent that the employee's Indiana liability exceeds the taxes withheld in the employee's state of employment. Likewise, Indiana local income taxes should be withheld only to the extent that the employee's Indiana local income tax liability exceeds the local taxes withheld for the employee's locality of employment. While IC 6-3-2-1(a) could be read to require an employer who is required to withhold the full Indiana rate over and above whatever rate the employer might be withholding with regard to another state's income tax, the department does not require withholding in this situation.

Example: An Indiana resident works exclusively in Illinois for an employer with a business connection with Indiana. The Illinois employer withholds Illinois state income taxes on behalf of the employee at 4.95% (the income tax rate in Illinois). Typically, no additional withholding is required for Indiana income tax (rate of 3.05% for 2024) because the Indiana resident will be able to claim a credit on her Indiana income tax return up to the amount paid in Illinois. However, Indiana local income tax will be required to be withheld.

NOTE: The previous sentence is qualified with *typically* because the credit available to the Indiana resident would apply only if the employee does actually end up paying tax in the other state.

More information related to Indiana state and local income tax, including withholding information, is available online in various department documents at the link above.

If you have any questions concerning this bulletin, contact the Tax Policy Division at taxpolicy@dor.in.gov.

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