

## **Adil Khoso's 2026 FBA Tax Conference Panel Report**

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### **Moderators:**

Andrew Reiter, Senior Manager at Blue J Legal

### **Speakers:**

Richard Jones, Partner at Sullivan & Worcester, LLP's Boston, MA office

Mathew Landwehr, Partner at Thompson Coburn, LLP's St. Louis, MO office

### **Summary:**

This session provided a high-level overview of state and local tax ("SALT") for federal practitioners. The discussion addressed constitutional and federal limitations on states' power to tax, the basic structure of state corporate income and sales-and-use-tax systems, and several current controversies, including post-*Wayfair* economic nexus, Public Law 86-272, fair-apportionment disputes, and software taxation.

### **Why SALT Matters:**

The discussion began with the point that SALT was not merely a state-level extension of federal tax practice. Andrew explained that SALT involved different tax structures and governing authorities. He noted that practitioners often must navigate local rules and administrative practices that may be less formal or less settled than their federal counterparts. Matt and Richard likewise emphasized that SALT practice was highly local and relationship-driven, requiring familiarity not only with the law, but also with the relevant state administrators and decisionmakers.

Andrew also stressed the practical importance of identifying SALT issues early. His point was that a federal practitioner did not need to become a SALT expert in a single session, but did need to recognize when a matter presented a SALT issue and seek guidance from in state-and-local counsel. He explained that it was far easier to structure a deal correctly on the front end than to clean up a state tax problem after the fact.

### **Constitutional Limitations on States' Taxing Power:**

Richard explained that, in the state-tax context, the principal federal constitutional limitations were the Due Process Clause and the Commerce Clause. Due process required a "definite link" or "minimum connection," while the Commerce Clause addressed the risk that a state tax would impose an undue burden on interstate commerce.

Richard then described *Complete Auto Transit, Incorporated v. Brady*, 430 U.S. 274 (1977), as the modern four-prong Commerce Clause test. Under that framework, a state tax must satisfy four requirements. First, the taxpayer or activity must have a substantial nexus with the taxing state. Second, the tax must be fairly apportioned. Third, the tax must not discriminate against interstate commerce. Fourth, the tax must be fairly related to services provided by the state.

### **Nexus, from *Quill* to *Wayfair*:**

Richard explained that, for many years, the Commerce Clause nexus standard was governed by *Quill*'s physical-presence rule. *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992). Under *Quill*, remote sales into a state were not enough by themselves. Some level of physical presence was ordinarily required. He also explained, however, that even before *Wayfair*, states had already begun pressing against that line through agency and attributional-nexus theories. As examples, he discussed in-state sales agents, the *Scripto* line of cases, and the recurring disputes involving Scholastic Books and teachers who distributed book-order forms to students and returned the orders. See *Scripto, Inc. v. Carson*, 362 U.S. 207 (1960); *Scholastic Book Clubs, Inc. v. CRS*, 38 A.3d 1183 (Conn. 2012).

Matt then explained that *Wayfair* changed the field. In *Wayfair*, South Dakota enacted a statute requiring a remote seller to collect and remit sales tax if, even without any physical presence, the seller had more than \$100,000 in sales into the state or 200 transactions in a year. The Supreme Court upheld that regime, overruled *Quill*, and held that South Dakota's economic-nexus statute satisfied constitutional requirements. Matt emphasized that this was a sales-and-use-tax case and that, after *Wayfair*, nearly every state with a sales tax enacted some form of economic-nexus threshold, though the precise thresholds now vary from state to state. He also noted that states continued to test the limits of *Wayfair*, including by removing transaction thresholds and pushing toward lower or broader standards. Andrew added that many practitioners have treated the South Dakota thresholds as a kind of safe harbor, even though the Court did not hold that those precise numbers were the only permissible standard.

### **Post-Wayfair Compliance and Exposure:**

Matt and Andrew explained that the consequences of *Wayfair* were practical as much as doctrinal. Matt used South Dakota and Colorado to illustrate the point. South Dakota's system was presented as comparatively easy to administer because its rates were uniform. Colorado, by contrast, was described as far more difficult because local rates and exemption rules could vary from one municipality to another. Matt used Amazon as the example of a remote seller that may have had to collect and remit tax in a state despite having no physical presence there, and he stressed that the real issue often became the burden of compliance. Andrew added that, in some jurisdictions, those differences can turn on extremely fine geographic distinctions, even down to the location of a mall, a block, or a street. Richard tied that compliance burden back to the Commerce Clause,

observing that questions about administrative burden were, at bottom, questions about whether a state had imposed an undue burden on interstate commerce.

Richard then gave a transactional example that underscored why these issues matter in practice. A buyer may acquire a fast-growing company years after it began making remote sales and discover that the target should have been filing in numerous states all along. Andrew added that, if the company never filed returns, the statute of limitations may never begin to run, which meant that the buyer may inherit exposure reaching back many years. Their point was that *Wayfair* had made early diligence far more important because economic nexus could create filing obligations in far more states than before.

### **Recent Nexus Controversies:**

Richard identified two recent nexus controversies. First, he discussed efforts to establish nexus through internet cookies stored on an in-state user's device. He explained that Massachusetts advanced that theory in a regulation, but that the theory was ultimately rejected. Second, he discussed disputes involving Amazon marketplace sellers whose inventory is placed by Amazon in fulfillment centers across different states. He explained that some courts have rejected nexus where the seller did not know the inventory was there and had no control over where Amazon stored it, while other jurisdictions have upheld nexus on the same basic facts. Matt added that, in practice, sellers often learned only after the fact where Amazon had placed their inventory.

### **Federal Statutory Limitations:**

In discussing federal statutory limitations, Richard focused on Public Law 86-272. He explained that the statute prevented a state from imposing a net income tax on a company whose only in-state activity consisted of soliciting orders for tangible personal property, so long as the orders were approved and shipped from outside the state. He also stressed that the statute remained important, even though states continue to test its limits.

Richard further explained that one current controversy was whether internet-based activities fell outside that protection. He noted that a phone call into the state ordinarily would not destroy the protection, but that states have begun asserting that online ordering functions, cookies, and internet chat features may do so.

### **Corporate Income Tax Basics:**

Matt explained that state corporate income tax matters because, unlike the federal government, which taxes the whole pie, each state claims only a slice. The difficulty was that different states use different methods to determine the size of their slice, and those competing claims could add up to more than the taxpayer actually earned.

Matt then explained that most states begin with federal taxable income and apply state-specific modifications. He described rolling conformity, static conformity, and selective conformity, or decoupling. He also explained that recent federal tax changes have pushed conformity issues to the front because some states automatically followed federal amendments while others adopted them only as of a fixed date or chose to depart from particular provisions. Andrew added that states often decoupled for budget reasons, not simply because they disagreed with federal policy. Richard then noted that, in this limited sense, state corporate income tax often did piggyback off federal law because federal taxable income was the starting point, even though state modifications could still create substantial controversy. He added that intercompany transactions remained a frequent source of dispute because states viewed them as especially vulnerable to manipulation.

**Apportionment:**

Matt explained that apportionment was the mechanism by which a multistate taxpayer's tax base was divided among the states in which it did business. He noted that states historically used payroll, property, and sales, but that many now place greater weight on sales, and many have moved to a single-sales-factor formula.

Richard then expanded on the concept. He explained that apportionment was an effort to measure what economic activity or benefit was fairly attributable to a particular state. Under the traditional three-factor method, property captured the capital employed in the state, payroll captured the human capital located there, and sales captured the market in the state. He then explained why the shift to a single-sales-factor formula matters. Because that method disregarded payroll and property, it tended to favor the taxpayer's headquarters state, where payroll and property were concentrated, and shifted the tax burden toward out-of-state companies selling into the jurisdiction. He emphasized that sales-factor sourcing was therefore where much of the action existed. For tangible personal property, he explained, sourcing generally followed the destination. For services, by contrast, states had moved from cost-of-performance approaches toward market-based sourcing tied to the customer's location.

In response to a question, Andrew explained that, when two or more states claim overlapping portions of the same income, the states did not ordinarily sort that out among themselves. He also emphasized a practical lesson for practitioners: apportionment disputes rarely sorted themselves out cleanly, and apparent simplicity could obscure materially different state approaches. Matt elaborated that each state issued its own assessment based on what it believed was its share of the taxpayer's income. Thus, if the combined claims exceeded the whole pie, the taxpayer must challenge those positions state by state. Richard added that different states may each be applying their own rules correctly, even if the total exceeded one hundred percent.

Richard also emphasized the fairness problems that could arise under single-sales-factor apportionment, particularly when a state excluded an extraordinary sale from the sales factor while

still taxing the income from that sale. He explained that this could keep the denominator artificially small and produce disproportionate results, especially for an out-of-state company. He framed the issue as one of constitutional fair apportionment, asking whether the taxing state was claiming more than its fair share of the taxpayer's activity.

### **Unitary Business Principle and Filing Methods:**

Matt described the unitary-business principle as both a sword and a shield. On one hand, it could permit a state to reach income from related entities that might not otherwise appear closely tied to the state. On the other hand, it allowed a taxpayer to argue that certain income should have been excluded from the apportionable base because it was not unitary income. He illustrated the point with the example of a multistate business that operated profitably in some states and at a loss in others, and a state that nonetheless sought to tax a share of the group's overall profit because the business was unitary. Richard added that the unitary-business principle determined what went into the apportionable base in the first place.

Matt also addressed filing methods, including separate-entity returns, consolidated returns, and combined returns, as well as "water's edge," which generally is the default method, and "worldwide," which is available by election in a handful of states, reporting. He noted that these choices could matter because one entity may have losses while another has profits, and combining them can materially affect the taxpayer's overall state tax position.

### **Sales and Use Tax Basics:**

Richard explained that sales tax was generally a transactional tax imposed on the retail sale of tangible personal property and, in some states, specified services. He also explained that use tax complemented sales tax by reaching in-state use or consumption where sales tax was not collected at the time of purchase. To illustrate the point, he explained that if a taxpayer bought skis in New Hampshire, which has no sales tax, and then brought them into Massachusetts for use, Massachusetts could impose a use tax because the taxable use occurred there even though the sale itself occurred elsewhere.

Richard further emphasized that the general aim of sales tax was to reach end-user consumption. That is why sales for resale are excluded and why many states exempt materials and equipment used in manufacturing goods that would later be sold at retail.

### **Software and Exemptions:**

Richard described software as a recurring source of controversy. He explained that, when software was sold on a physical medium, its treatment as tangible personal property was comparatively straightforward. As software moved to downloads and vendor-hosted systems, however, states changed their laws to preserve taxability, which in turn produced disputes over bundled

transactions and over the true-object test. He noted that software disputes also raised sourcing questions because the same software may be used in more than one state at the same time.

Matt then explained that exemptions were one of the most heavily litigated areas of SALT practice, particularly in Missouri. He identified entity-based, product-based, and use-based exemptions, including resale and manufacturing exemptions. He also explained that these disputes often arose when a taxpayer later realized that it should not have paid or collected tax in the first place and sought a refund. Matt used manufacturing exemptions to show why statutory interpretation remained central in SALT practice. A statute enacted decades ago may have to be applied to modern products and modern business models, including intangible products, and that creates significant room for controversy.

**Current Sales-and-Use-Tax Controversies:**

The session closed with a brief discussion of digital-service and digital-advertising taxes. Andrew framed the issue through the Internet Tax Freedom Act, noting that a state cannot tax a service differently merely because the service was delivered digitally rather than non-digitally. Richard responded that digital-advertising taxes remained highly controversial, that the issue was unsettled, and that Maryland had been a leading state in pushing those taxes forward. He added that disputes involving digital products and services remained highly fact intensive.