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5 KEY TAKEAWAYS

# State and Local Tax Risk and Opportunities

Kilpatrick's Lauren Ferrante recently presented **"State and Local Tax Risk and Opportunities"** as part of the **Center for Professional Education Multistate Corporate Taxation Webinar.**

**Key takeaways from Lauren's presentation include:**

1

**Public Law 86-272 Protections Are Narrowing, Especially for Internet and Non-Solicitation Activities**
Several recent state and court actions have significantly limited the scope of federal protection under Public Law 86-272 for out-of-state businesses. Courts in Minnesota and Wisconsin in *Uline, Inc. v. Commissioner of Revenue*, 10 N.W.3d 170 (Minn. 2024) and *ASAP Cruises, Inc. v. Wis. Dep't of Revenue*, 2025 WI App 44 (Wis. Ct. App. June 3, 2025), *petition for review denied* (Wis. Feb. 12, 2026) have upheld state actions denying protection when in-state activities went beyond mere solicitation—even if performed by independent contractors or involved collecting market data. Pending litigation, such as the *American Catalog Mailers Association* lawsuits in New York in New Jersey, are continuing to challenge states' narrowing of Public Law 86-272.

2

**Pre- and Post-*Wayfair* Litigation Continues to Shape Sales Tax Nexus**
Litigation continues to interpret the boundaries of state authority to require sales tax collection by remote sellers. Notably, the South Carolina Supreme Court held in *Amazon Servs., LLC v. S.C. Dep't of Revenue*, Appellate Case no. 2024-000625, Opinion no. 28319 (Mar. 18, 2026) that Amazon Services liable for pre-*Wayfair* sales tax as a marketplace facilitator, finding it was "engaged in the business of selling" even before state marketplace facilitator laws were enacted. In the post-*Wayfair* environment, states and localities are facing legal challenges for alleged unconstitutional overreach against remote sellers, with current and prior lawsuits in Illinois and Colorado challenging sourcing regimes and burdens under the U.S. Constitution.

3

**Remote Workforce Taxation Remains Contentious and State-Favorable**
The "convenience of the employer" rule—particularly in New York—continues to subject nonresident remote workers to state income tax on wages earned while working outside the state. In *Matter of Zelinsky*, New York courts upheld this rule, and the courts have thus far rejected constitutional challenges under U.S. Constitution. The case is now pending appeal, but the current trend favors state assertions of taxing authority over remote work arrangements.

4

**Apportionment Trends, with a spotlight on California**
Recently, California sourcing litigation is chalked full of significant issues, including the "matching principle" between the tax base and apportionment formula, fair apportionment and alternative apportionment. California's response to the Office of Tax Appeals' decision in *In re Microsoft Corp.*—which allowed the inclusion of foreign dividends in the sales factor that were excluded from the tax base—was to enact a new statute to exclude the income from apportionment. Litigation challenging this statute on multiple grounds, including as vague and retroactive, is ongoing. Other states, such as Florida, have presented a challenge to California's apportionment scheme to the U.S. Supreme Court, signaling continued disputes over fair apportionment and sourcing methods. And, a California court recently concluded that the taxpayer in *Smithfield Packaged Meats Corp. v. Cal. Franchise Tax Board*, case number 21STCV39637 (Superior Court of Cal., Los Angeles County (Feb. 26, 2026)) is entitled to use an alternative apportionment formula to fairly reflect its business activities in the state.

5

**State Taxation of the Digital Economy and AI Services Is Evolving, With ITFA Providing Key Limitations**
The Internet Tax Freedom Act (ITFA) continues to preempt state and local taxation of internet access and discriminatory taxes on electronic commerce. Recent cases have reinforced ITFA's protections for services like cloud storage and streaming, while states have tested the boundaries with new taxes on digital advertising and streaming services—sometimes successfully, sometimes not. With respect to artificial intelligence, recent state rulings (e.g., Indiana and Illinois) have determined that AI chatbot services delivered electronically without a software transfer are generally not taxable, but the legal landscape remains in flux as technology and business models evolve.

For more information, please contact:
**Lauren Ferrante, lferrante@ktslaw.com**

www.ktslaw.com