# State and Local Tax Update

**Presented By:**

Matt Piatt | SALT Practice Leader

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# Welcome and Meet Your Presenter

## Matt Piatt, CPA, JD

*Senior Manager, State and Local Tax Leader*

Matt is a Senior Manager in RKL's Tax Services Group where he leads the State and Local Tax Practice. His expertise encompasses a comprehensive suite of state and local tax consulting. Matt's proficiency extends to various tax categories such as income, franchise, gross receipts, and sales and use tax. His services are wide-ranging and include nexus studies, voluntary disclosure agreements, taxability determinations, sourcing/apportionment issues, SALT M&A due diligence, and return review. Although Matt's expertise benefits various industry sectors, he has substantial experience working with construction contractors, private equity, strategic buyers, and closely held businesses.

Matt has over ten years of experience in accounting and finance, with a primary focus on state and local tax. He has worked at Big Four accounting firms, a prominent law firm, assisted in running a family business, as well as held a recent leadership role in the SALT M&A practice at a top 20 CPA firm.

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# What We Will Introduce

01. Erosion of Public Law 86-272 Protection

02. Digital Goods and Services Taxation

03. Remote Work and Nexus

04. Pass Through Entity Tax (PTET) After 2025

05. Questions & Answers

# What is Public Law 86-272?

- Enacted in 1959 to limit states' authority to impose income tax on out-of-state businesses
- Only applies to sales of tangible personal property
- Does not protect services, intangible goods, or non-sales activities

Protects businesses from state income tax if activities are limited to:

- Soliciting orders for sales of tangible goods
- Orders are sent outside the state for approval and fulfillment

# Public Law 86-272 Erosion by States

States are now commonly asserting that certain internet activities exceed mere solicitation of sales and are unprotected.

### New York

Issued revised regulations that were upheld on appeal in 2025; digital customer engagement (e.g., cookies, chatbots, etc.) is treated as an unprotected activity.

### Ohio

A finding of nexus was upheld based on a retailer's use of cookies and online customer support, despite the retailer having no physical presence in the state.

### California

Audits have concluded out-of-state manufacturers' activities are unprotected when post-sale support and remote diagnostics were offered to California customers via their websites.

### New Jersey and Massachusetts

Both states have issued regulations that mirror the MTC guidance, which provides various internet activities are unprotected.

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# What Activities are Likely Unprotected versus Still Protected?

## Unprotected

- Interactive website features (e.g., live chat, customer portals)
- Use of cookies or tracking technology for behavioral targeting
- Providing installation, repair, or maintenance services
- Maintaining inventory or consignment stock in-state
- Providing downloadable content (e.g., manuals, software, updates)
- Online training, tutorials, or webinars
- Employing in-state personnel for non-solicitation functions (e.g., tech support)

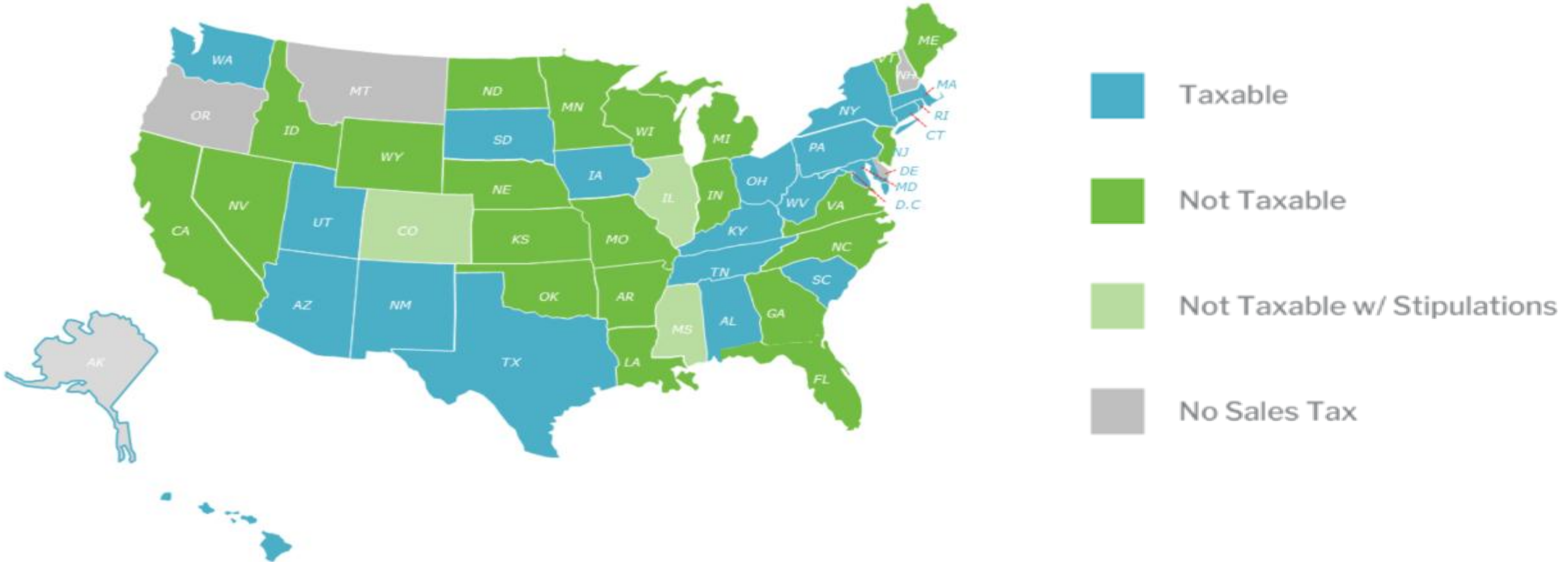
## Protected

- Static websites that only display product information and pricing
- In-state visits solely for the purpose of soliciting orders
- Attending trade shows (no on-site sales, limited to solicitation)
- Advertising in local media or online without customer interaction
- Hiring independent contractors for solicitation only
- Using third-party logistics providers (without owning/operating the facility)

# Digital Goods and Services Taxation

Sales Tax Base Expansion in Digital Goods and Services

Historically, states only taxed tangible personal property, leaving many digital products untaxed. To increase revenue, states are increasingly expanding the sales tax base to include digital products. Software-as-a-Service ("SaaS") is one common example.



# Recent Developments and Policy Changes

**Pennsylvania**

- Since 2016, canned software products, including SaaS or cloud-based software, and any maintenance, upgrades, and support related to that software have been taxable.
- Custom software and computer services were historically exempt.
- In 2017, PA provided guidance to assist vendors in distinguishing between taxable "support" services and nontaxable software "consulting" services. Many taxpayers still had questions regarding these distinctions.
- In 2024, new guidance was issued that didn't overturn the previous rulings but provided more comprehensive explanations and examples.
- This new guidance clarified that software-related services such as modifying, configuring, or altering canned software are taxable, regardless of whether these services are performed in conjunction with the sale or separately.
- The guidance also stated that consulting is also taxable if sold in conjunction with the software, even if invoiced separately.
- The recurring issue on audit is what is taxable "support" and what is nontaxable "consulting".
  - The contracts, invoices, and other supporting documentation that a taxpayer can produce are often determinative.

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# Recent Developments and Policy Changes continued…

| | |
|---|---|
| **Maryland** | • Effective July 1, 2025, Maryland expanded its sales and use tax to include a broad range of digital products and services. |
| **Ohio** | • Effective January 1, 2026, Ohio will eliminate several sales tax exemptions, including for digital audio and telecommunication services. |
| **Illinois** | • Effective January 1, 2025, Illinois now taxes online courses and cloud infrastructure services. |
| **Maine** | • Effective January 1, 2026, Maine will tax digital audiovisual and audio services. |
| **Texas** | • Revised definition of data processing services<br>  • Taxable data processing services now include internet hosting, streaming video subscriptions and website creation, repair and maintenance when they involve the storage, manipulation, compilation and entry of data. |
| **Louisiana** | • Effective January 1, 2025, digital products are now taxable, including streaming media, E-books, apps and games. |
| **Washington** | • Effective October 1, 2025, vendors must collect sales tax on new categories, including advertising services, IT support, digital automated services, among others. |

# Remote Work and Nexus

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# Remote Workers and SALT Issues

*The Pew Research Center reported that in 2023, 35 percent of workers with jobs that permit working from home, work from home all the time. The same report indicated 41 percent of workers whose jobs can be done remotely are on a hybrid schedule.*

## What does this mean for businesses?

- Many are regularly hiring employees who work outside of states where the company regularly does business.
- This creates income tax withholding challenges for employers, as work is being done in various states and localities outside of the employer's home state, and tracking employee work locations can be costly and burdensome.
  - Reciprocity agreements between states can reduce this burden, but those aren't always applicable.
- In general, having an employee in a state is nexus creating for both income tax and sales tax purposes. The risk of audit in this scenario is relatively high, as the company is likely on the state's radar since payroll withholding is likely required in the state.
- Having a remote worker in a state also creates potential compliance obligations for personal property tax if the employee(s) has company issued equipment (e.g., a laptop) as well potential unemployment tax compliance responsibilities.
- It is prudent for employers with remote workers to have a nexus study completed to understand their respective state filing footprints and how potential state filings might be minimized.

# Pass Through Entity Tax (PTET) – After 2025

# History of PTET and Current Status

- Tax Cuts and Jobs Act of 2017 capped SALT itemized deductions to $10,000 for the 2018 through 2025 taxable year. Increased to $40,000 for 2026 through 2030.
- To circumvent the cap, states enacted pass-through entity taxes (PTET).
- IRS Notice 2020-75 allowed state and local income taxes imposed on and paid by a partnership or S corporation to be deemed a federal deduction.
- Thus, PTET is a state tax election that creates a federal tax benefit.
- Under the final version of the One Big Beautiful Bill (OBBBA), PTET SALT payments are fully deductible, and there is no limit or qualifying entity language included, which had been introduced in various earlier versions of the bill.
- Pennsylvania does not have a PTET system; however, the state does allow an out-of-state credit for S corporation owners.
  - This means the PTET election in states outside of Pennsylvania could benefit Pennsylvania residents who own S corporations.

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# Dollar Benefit of Maryland PTET Election for PA S Corp. Owner

- **Assumptions**
  - $2,000,000 Maryland-source S corp income
  - Maryland income tax rate: 8%
  - SALT deduction cap for owner: $10,000
  - Federal marginal tax rate: 37%

| | Without PTET Election | With PTET Election |
|---|---|---|
| Maryland Tax Paid | $160,000 | $160,000 |
| Federal SALT Deduction | $10,000 (SALT cap) | Full $160,000 |
| Net Federal Taxable Income | $1,990,000 | $1,840,000 |
| Additional Federal Deduction | - | $150,000 |
| Federal Tax Savings (at 37%) | - | $55,500 |

**Key Takeaway: Maryland PTET Election increases the federal tax deduction by $150,000, reducing federal tax owed by $55,500. Owner isn't allowed increased SALT deduction of $40,000 due to income exceeding $500,000.**

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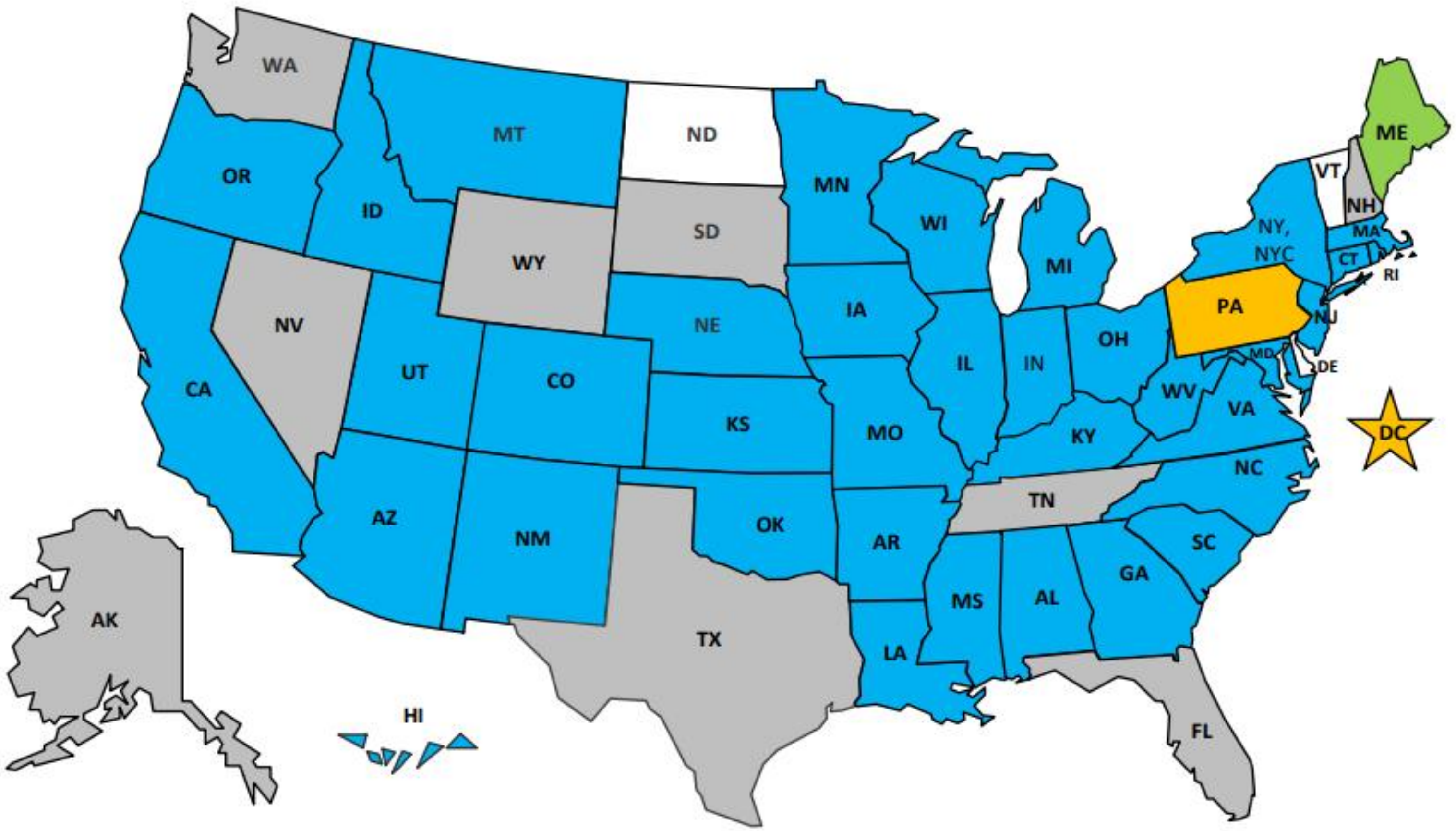
# States with Enacted or Proposed Pass-Through Entity (PTE) Level Tax

As of July 29, 2025




- 36 states (& 1 locality) that enacted a PTE tax since TCJA SALT deduction limitation, effective for 2024 (or earlier) unless noted: AL, AR, AZ, CA[5], CO[3], CT[1], HI, GA, IA[3], ID, IL[2], IN, KS, KY (& KY) ,LA, MA[3], MI[3], MD, MN[3], MO, MS, MT, NC, NE, NJ, NM, NY, OH, OK, OR[2], RI, SC, UT[2], VA[4], WI, WV, and NYC
- 2 states with active proposed PTE tax bills (PA - SB 396, HB 1610, DC - B26-0324)
- 1 state with pending proposed PTE tax bill for 2026 (ME – LD 191, HP 124)
- 9 states with no owner-level personal income tax on PTE income: AK, FL, NH, NV, SD, TN, TX, WA, WY
- 3 states with an owner-level personal income tax on PTE income that have not yet enacted or & do not have an active proposed bill on PTE taxes: DE, ND, and VT

[1] Mandatory 2018-2023, elective starting 2024
[2] State PTET expires on Dec. 31, 2025 and no longer in session, and likely will reintroduce PTET extension bills in 2026 (IL, OR, UT)
[3] State PTET expires when the federal cap expires or is otherwise not in effect (CO, IA, MA, MI, MN)
[4] State PTET expires Dec. 31, 2026
[5] State PTET expires Dec. 31, 2030

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