

Speaker 1 ([00:01](#)):

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Alysse McLoughlin ([00:16](#)):

We know that they don't like handling tax cases at all.

Nikki Dobay ([00:20](#)):

What?

Alysse McLoughlin ([00:20](#)):

But they definitely seem to understand what was at stake here.

Nikki Dobay ([00:30](#)):

Hello and welcome to GeTtin' SALTy, a state and local tax policy podcast hosted by Greenberg Traurig. My name is Nikki Dobay, shareholder in the Sacramento, California, and Portland, Oregon offices. I am super pleased to be joined today by a dear friend, Alysse McLoughlin. She's a partner at Jones Walker in New York. Alysse, thank you so much for joining me.

Alysse McLoughlin ([00:52](#)):

Thank you so much for having me. I'm really excited to be here and to be talking about SALT tax issues.

Nikki Dobay ([00:57](#)):

And today we are going to have part two of a discussion of more. We did a podcast earlier this year with Joe Bishop-Henchman from NTU where we talked about really focused on the federal issues and more. So we're going to follow up with a deeper dive into the state issues. But before we get there, Alysse, you are new to the podcast. There is a question I ask the newbies, how did you get into state and local tax?

Alysse McLoughlin ([01:27](#)):

Oh, I wanted to do this from the time I was three. No, not true. So I had graduated law school. I went to be a federal tax lawyer at a large law firm in New York and I did that for two and a half years. And to show my age, maybe I shouldn't, but at the time, it was before the check the box rules were in place. And to figure out whether something was a partnership, you actually had to investigate four different characteristics, whether I had continuity of ownership and interest in all these different things. I felt like that's what I was doing over and over and over again. So I really did not like it. I was actually going to quit tax law and I said, "Let me see what else is out there." And I interviewed with Art Rosen and Peter Faber at McDermott Will & Emery and got a job there working with them and Diane Smith, three great minds of the tax area. And that started me on my career and I loved it. So that's how I got into it.

Nikki Dobay ([02:23](#)):

So the rest is history?

Alysse McLoughlin ([02:25](#)):

Yes, they're history.

Nikki Dobay ([02:26](#)):

As they say. So, well most of us didn't think this is what we'd be doing at age three, so I think you're in very good company there.

([02:37](#)):

All right, so let's talk about more, and I think this conversation is timely. The oral arguments before the Supreme Court were just about 10 days ago, I think December 5th was the day. So I'm sure you've listened. I've done some listening. But maybe let's set the stage a little bit because there was an earlier podcast, but the more cases, not a state tax case. This is a case that involves whether or not IRC 965, the mandatory repatriation tax, is constitutional under the 16th Amendment or whether or not it's subject to the apportionment clause of the US Constitution. And these are all questions that will impact whether or not for federal purposes that is a constitutional tax. Why the heck do we care about this for state tax purposes? I mean, they've got their stuff, we've got our stuff, right?

Alysse McLoughlin ([03:38](#)):

Well yeah, and that is I think what everyone thinks. But then as we all know, if you're in the state tax world, if you're looking at corporate income tax or personal income tax, what is the tax base of that? It comes from federal income tax. So this does impact very directly is what might be in the tax base for federal people.

Nikki Dobay ([03:57](#)):

And so what are the two big issues I think that we'll be talking about today on the state tax side?

Alysse McLoughlin ([04:03](#)):

So one issue really has to do with federal conformity. Some states automatically adopt the federal income tax code as their starting point. Some as of certain date, some kind of automatically update it. But if you're starting at that point and if it comes back that this tax was not something that the federal government could impose, then all of a sudden you're going to look at it here and, oh, all of a sudden that's not in the federal tax base. So the question is what happens there and whether people can file for refunds at the state level.

([04:34](#)):

So now if we have a tax base that might not include this at the federal level, so then what happens at the state level? You would think, "Okay, yes, people can file for a refund." But the issue there is the transition tax was something that was like a portioned out over eight years, you paid that tax over eight years. So at the state level, almost no states did that. I think one state might have. But otherwise it was... Do you remember which state it was?

Nikki Dobay ([05:01](#)):

I don't remember which state.

Alysse McLoughlin ([05:05](#)):

Okay, I don't either. One state, one lucky state. But otherwise, people paid that tax over eight years ago, or they paid it in 2017, '18, right around there. So now the statute is run. So a lot of times you may not have something that is taxable at the federal level, but you still pay tax on the state level and you may

not be able to get a refund. So people might be able to get a refund if they're under audit at a state or sometimes if they're under audit at federal level and that statute of limitations will extend to the state, but otherwise something that may not be taxable there all of a sudden becomes taxable just because of the statute of limitations.

Nikki Dobay ([05:41](#)):

And so that's with respect to 965. So I think let's say how this plays out is the Supreme Court rules in favor of the mores. And we'll get to later in the podcast when we talk a little bit about the oral arguments, whether or not we think that will happen, but let's say that happens. So 965 will be deemed to be unconstitutional. So for state purposes, those states that conform to the federal code, that seems to go away in the tax base. And then the question becomes is there statute open at the state level to get that refund. States, we know that there's no state that's alike in this realm, so you're going to have to dig into all those statute of limitations provisions.

Alysse McLoughlin ([06:28](#)):

Right. Well, you're right because the interesting thing is that a lot of times if you have a federal change, that will trigger opening the state statute. But here the federal change is in a year after they actually reported it. And I think you're right, it will be interesting to kind of dig through the state statutes and see if you can say, "Okay, we changed what we reported in 2020. For federal purposes, we get a refund." And so therefore, can that somehow carry back? Because that income was really reported earlier, but it was a federal change. So I think you're right. It is also just digging through the statutes in every state, which will be different in every state.

Nikki Dobay ([07:05](#)):

Right. I mean, the question is, is this a federal change for purposes of reporting that as we're required to do at the state level, that would obviously be great for taxpayers, but you could see the states pushing back on those positions. So that could be one really, we'll say, interesting for lack of a better word, thing that may come out of this. But what about the broader impact of the Supreme Court ruling that 965 is unconstitutional because there was no realization?

Alysse McLoughlin ([07:40](#)):

So there is so much there and it depends on how the Supreme Court does rule on this. And like you said, we will talk later about where we think they're going, but they can either somehow rule very narrowly and just say 965 is unconstitutional. But depending on what they say, there could be so much more of an impact from this. So there are so many other provisions in federal income tax area where you do have something that is a pass-through tax, so where a shareholder or an owner of an entity is subject to tax based on what's happening at the entity that they own. So for instance, partnerships are passed through taxation, S-corps are passed through taxation. So if this is overruled because certain things aren't an income realization because something happens at a lower level, at an entity level, then that could invalidate all of those areas. It could invalidate some of the taxation on how REITs are taxed.

([08:32](#)):

And then the other thing is if it's not a realization event because a deemed realization of this money that came back that the corporations had earned over many, many years, so if it's the deemed realization event is deemed to not be create income, then you have market to market might be deemed not appropriate OID where you have the original issue discount where you say there's certain interest over

the years. That might not be there. There's so many areas that can be invalidated from this. So it really will be interesting to see what happens with what the court does rule on this.

Nikki Dobay ([09:09](#)):

And I think the other really interesting piece about this for purposes of the potential state impact is I've heard some argue that just because it would be unconstitutional for purposes of the federal code, the states aren't impacted by the 16th Amendment and we already have apportionment rules. So potentially, the states could keep all of these rules in place, but okay, perhaps maybe they can, but the whole reason to conform to the federal code is to help with administration. Yeah, let's take a state that just says, "Nope, we're going to keep all these provisions in our law." That state agency no longer has the ability to piggyback off of a federal audit or things that are happening on that federal return. So it really does create two completely different tax structures potentially that taxpayers would have to comply with.

Alysse McLoughlin ([10:13](#)):

Right. And I think you're right on that. And when you look at it, not only would the states have to though change their laws to say, "We are going to now affirmatively not follow the federal tax base. We're going to do it as the federal tax base could have been in effect if this was deemed constitutional." So you're right, so then what happens? Because that's the whole almost beauty of the corporate income tax or the state corporate income tax or the state personal income tax, is that the starting point was always what the federal one is. And not every state has that, but most states have that. I believe Mississippi might be one that doesn't. It's a nightmare when you look through it because you don't have that federal base, you don't have that starting point. So, you're right.

([10:59](#)):

So if a state does say, "Okay, yes, we don't have to follow follow this 16th Amendment. We don't care about this apportionment clause, so we are going to say we still have these items that are taxable," what do taxpayers do? They have to now do two different layers of tax. They have to do the federal as if these principles were constitutional and then as if they're not and report one to federal and report one to the states. But then the states also have relied on the federal government to some extent. We know that they didn't have to and they can look into the federal issues, but it's always been much easier for them to rely on what the federal government is doing, and now they wouldn't have that ability to do it. So I think it does create a big issue for the states on they might want to say, "We're not going to conform," but it's not as easy as saying we won't conform. There's a lot that they're going to have to do administratively to make that work.

Nikki Dobay ([11:50](#)):

I think one other question that would raise, or one other issue that would raise is potentially due process issues for taxpayers is that they would have to keep completely separate books and records for purposes of calculating the state income taxes versus the federal income tax. I mean, obviously taxpayers have to do that in the context of other state taxes, but if we're in this post Wayfair world where we talk about burdens, would that be enough to tip any scale? So I think just a lot of really significant potential issues at the state level if the Supreme Court is to determine that 965 is unconstitutional.

([12:38](#)):

Now, let's take the flip of that, which I know is your favorite part. Let's say that the Supreme Court goes the direction of affirming 965 and saying that it is constitutional. And we won't say they'll affirm the

Ninth Circuit's decision because that decision was very broad, but they go down that path. How does that impact? So we're not going to have all these text base issues now, but I know you have a lot of thoughts on how that is potentially very significant for taxpayers at the state level.

Alysse McLoughlin ([13:14](#)):

Yeah. So I think it's interesting, because if we go back, what this impacts the most is probably 965 and GILTI, GILTI income. Those are both categories of income that are earned by a corporation, but the shareholders deemed to be taxable on it. So we know when a lot of states look at that, they will say, "Okay, we're taxing that" if they tax it. A lot of states don't. But to the extent they do tax that and include that in the income base, it comes in as a deemed dividend or something like that. So it's a net income that comes in. And if they allow you to include it in the apportionment factor, you include it on that net basis. But that is really a mismatch. Everything else you are including in a gross basis, which means that if you're including your expenses from foreign operations and denominator, you are really undercounting the contribution that those operations contributed to the multinational income of that business.

([14:17](#)):

So if they are undercounting that, I mean we know that apportionment, a lot of states have a lot of leeway on how they're going to do this, but if the Supreme Court decision essentially says that, "We think that this is taxable by the entity, by the shareholder, by whoever gets it and it's taxable because it's income that they actually earned its income, they received its income, their income from operations," and I think that makes it much stronger that you can't treat it differently for apportionment purposes, so if you're saying it's income, I think the arguments are much stronger that you have to be fully including that in the factors. So I think that helps the arguments that taxpayers have that you can't treat this differently. The GILTI is from active operations and now it's active operations that where the income is attributable to the taxpayer, not as a deemed dividend but kind of attributable to the taxpayer, then I think that really strengthens those arguments for fair apportionment.

Nikki Dobay ([15:19](#)):

And that's an area where I think we've just really begun to see the cases being filed in litigation, being pursued in this area. And I have to say, it seems to be a broader issue with apportionment that the states want everything to come in as apportionable income. Yet when it comes to the factor, they're very focused on limiting. I mean it's kind of like they have their cake and they want to eat it too because they're like, "Well, it's apportionable income but it's not part of your normal trader business or your normal operations. So we're not going to give you factor representation at all or it's going to be very narrow." And we've seen some states in 965 and GILTI provide no factor representation and just say, "We aren't even going to give you the net." So to your point, I think this will be a very interesting case to watch on that side if the government ultimately wins that case.

Alysse McLoughlin ([16:21](#)):

Agree. I do think that's important. One other thing, I'm jumping ahead for a minute, but this is something that I noticed in the oral arguments because I have always had my theory on this income part of it and the realization. But if you look through the briefs and if you look at the oral argument, there was also a lot of discussion on how the taxpayer was saying, "Well, you know what? Partnerships and corporations are different." Essentially the taxpayer is trying to allow the Supreme Court to narrow the ruling and just say, "This will apply only to 965 and maybe some other taxes, but not to everything."

You're not invalidating the tax on partnerships, or that partners are taxed on partnerships, that S-corp owners are taxed on S-corporations, that type of thing.

[\(17:09\)](#):

So if you look at it, they are talking about how there's a difference between partnerships traditionally, S-corporations, corporations, and the Supreme Court seem to be saying... And again, you can never tell how a decision is really going to come out from what questions you get an oral argument, but the Supreme Court really seemed to be saying a few times, "Corporation is not really different from a partnership. That shouldn't be a distinction that is there." Now, I think that's really important in a nexus context because there's a lot of cases, recent cases where people are talking about how do you tax the gain when someone sells a partnership interest or sells something on a 338(h)(10) or an S-corp. The states all say, "Well, the owner has nexus with the state because it was a pass through entity and that's different than what's going on with the corporation."

[\(18:00\)](#):

I personally don't think that's right because if you look at, for instance, a lot of LLCs and a lot of partnership, state partnership rules now, corporations, S-Corps, LLCs are not really different. They do provide limited liability. The partners don't really own the items that the entity owns. And also if you have, for instance, a limited partnership, only one person is really managing that partnership where only the general partners, you have people who are very passive. Well, so I've always thought that's something where that's why the limited partner doesn't have nexus is because it's really no different from a corporation. And we know that in the corporation that should really be what the rule is.

[\(18:41\)](#):

So I think that it's going to be interesting to see what the decision ultimately comes up with and if there's going to be something addressing that issue because I think that's something that could be helpful for taxpayers in saying, "Therefore you're not taxable on maybe a passive interest in a pass-through entity when you sell that." Again on the other side, is that something where the states come and say, "Wait, you know what? We think we can now tax when you sell a corporation"? So it's really I think very possible opportunity. Very scary also. But I think that's also something that we really have to look at when the Supreme Court's decision comes out.

Nikki Dobay [\(19:17\)](#):

Yeah. So let's get into a few nuances of the oral argument, because this is a case where I feel like the stakes are high, either whether the Supreme Court upholds what the Ninth Circuit did or overrules the Ninth Circuit. It seems like based on the oral arguments, again, we have no idea, and I'll also say probably based on some of the politics of the court, we probably aren't going to get one of those drastic decisions in either direction. So a lot of commentary is that the taxpayer brought this case to preclude Congress from being able to enact a wealth tax, but the Ninth Circuit's decision ruling against the taxpayer completely opens the door to Congress enacting a wealth tax. So those are kind of the bookends on this.

[\(20:10\)](#):

I mean, at this point I think there was something like over 40 amicus briefs filed in this case with most folks really trying to significantly narrow the scope of the Supreme Court's decision. So from the oral arguments, Alysse, where is your crystal ball taking you about how this decision might come down? And you've provided some thoughts on what are they going to say about our partnerships really different than corporations, but how do you think the Supreme Court cracks this nut?

Alysse McLoughlin ([20:44](#)):

So again, with the caveat that you can never tell what is happening from oral argument, but looking at the oral argument and listening to what the judges were doing, I think it did indicate that they really do want to decide this on a narrow basis, that maybe we don't agree with 965. Maybe. That essentially I think they kept going to the taxpayer, "Let us know why this is different from all of the other provisions. Let us know. Let us know." And I'm not sure that they got something there that they felt they could rely upon. So then I would think that it is going to probably, they're going to not decide in favor of the taxpayer. I think it's more likely that that's going to happen. But I think you're right. I think there was also a very big concern on wealth taxes and I think that they're going to make sure that no matter what happens, those won't be permissible from their decision because we know that they don't like handling tax cases at all.

Nikki Dobay ([21:41](#)):

What?

Alysse McLoughlin ([21:41](#)):

But they definitely seem to understand what was at stake here.

Nikki Dobay ([21:47](#)):

Yeah, I definitely heard the justices kind of across the board concern that this would have a ruling in favor of the taxpayer would have very broad implications. And they seem to be going down the adverse path, very broad adverse implications with respect to the internal revenue code. And yes, those questions about, "How is this different, why won't this impact subpart F or some of these other provisions?" And then they also seem to express those concern if the government were to get a complete win.

([22:22](#)):

The other thing I really did hear them talk about at several points was the due process clause. I thought that was interesting because they talked about it in the context of, is it just that 965 goes back so many years and that it was going back to 1986? I think that could have significant impacts for state tax purposes too, especially if we get some language that talks about retroactivity and how maybe that's how 965 is going to be deemed unconstitutional, is not because there was no actual realization or it was only deemed, but that it just went back 30 some years.

Alysse McLoughlin ([23:08](#)):

Right. So the realization almost might've been 30 years ago, 29 years ago, 28 years ago, maybe different owners of the corporation and it's now... So yeah, it was interesting I thought because the justices did keep trying to lead I think the taxpayer over to due process and he kept saying, "No, that's not what I'm arguing." So I agree with you. I think that due process, definitely there might be something coming out with respect to that that might be a way to differentiate this from everything else. And again, I think that would be interesting because as you were even mentioning at the beginning, due process for if the tax base gets too complex, is that a due process issue from the state tax field? We're always interested in what is going on with the due process clause. Again, whatever I think the Supreme Court decides I think is going to be really interesting here.

Nikki Dobay ([24:05](#)):

Yeah. So I think we'll be back in 2024 for a follow-up conversation after that decision comes out. I thought that one possible path would be they just would say, "Oh, we didn't mean to take this case, nevermind." But after hearing how engaged they were, despite they're not liking to deal with tax issues, we're going to get a decision and we'll see how it comes out. So maybe they'll kick it back to the Ninth Circuit for a little bit more factual analysis or analysis of the due process clause, but I think it's going to be a pretty interesting decision that we'll see.

Alysse McLoughlin ([24:43](#)):

I agree. I would love to be back here in 2024 talking about it because I think there's going to be a lot of ramifications almost whichever way they go.

Nikki Dobay ([24:51](#)):

All right. Well, you definitely will be. So thank you for your thoughts, Alysse. Before I let you go, we have to do a surprise non-tax question. And so I'm going to keep it holiday themed. The holiday season is upon us, it's December 15th when we're doing this recording. So lots of holiday parties happening for many folks. And how this works as I ask the question and then I'll answer it to allow you time to collect your thoughts, but is there some holiday tradition in your family or for you that you're really excited about this time of year?

([25:29](#)):

For me, I don't really have. Too many traditions that I like, have to do every year. I do like to drink eggnog and have some holiday hattes or some festive fun drinks. But the one fun thing that I'm very much looking forward to is I'm going to be picking up a new puppy next week. And so we will be having all the puppy fun, which I'm just focusing on the fun part. I'm not going to focus on any of the difficulties with puppies, but I'm very much looking forward to having a puppy to play with over the holiday season. So that's my big fun. So what is your holiday fun that you're looking forward to?

Alysse McLoughlin ([26:09](#)):

So my holiday fun is as soon as it turns December and I have now moved to New Orleans where I lived part of the time, and so I go to Lafitte's Blacksmith Shop, and they have a frozen eggnog daiquiri, which is my favorite thing. Okay, I wish it was something that was more family-friendly and wholesome, but oh my god, do I love these frozen daiquiris. They're so good.

Nikki Dobay ([26:36](#)):

All right. All right. It looks like I'm coming to New Orleans next year. So they have all of December?

Alysse McLoughlin ([26:41](#)):

All of December.

Nikki Dobay ([26:43](#)):

Okay.

Alysse McLoughlin ([26:43](#)):

Really good.

Nikki Dobay ([26:44](#)):



It's like the McDonald's eggnog shake, but better.

Alysse McLoughlin ([26:48](#)):

So much better.

Nikki Dobay ([26:49](#)):

Okay. Well, thank you so much, Alysse, for joining me. Again, we will be back in 2024 talking about the decision. Thank you to the listeners for joining us. This is the last episode of 2023, but we will be back in 2024. We'll be taking off a few weeks. There will be information about Alysse and my contact info in the show notes and we will see you in 2024 on GeTtin' SALTY.