An Ounce of Prevention

Posted on May 7, 2026

By Andrea Muse

In this spring installment of Briefly Noted, members of the *Tax Notes State* Council speculate on the next areas for state compliance activity.

This article is intended for general information purposes only and does not and is not intended to constitute legal advice. The reader should consult with legal counsel to determine how laws or decisions discussed herein apply to the reader's specific circumstances.

Fair Apportionment in the Era of Single Sales Factor Apportionment

Karl A. Frieden is vice president and general counsel and Marilyn A. Wethekam is of counsel to the Council On State Taxation.

The principle of fair apportionment is a cornerstone of state corporate income taxation, ensuring that a state taxes no more than its fair share of a multistate enterprise's income. The Supreme Court has stated that "a state may not, when imposing an income-based tax, 'tax value earned outside its borders.'"[1] Although income attribution is primarily a statutory function, the Court has also made clear that "any formula used must bear a rational relationship, both on its face and in its application, to . . . values connected with the taxing State."[2] The move to single-sales-factor apportionment formulas and the adoption of market-based sourcing apportionment have intensified the scrutiny of apportionment formulas. As states employ sales as the sole measure to the exclusion of other in-state activities (property and payroll), apportionment continues to be a fertile ground for controversy at both the audit level and in litigation. Two recent decisions — *NuStar Energy L.P. v. Hancock*[3] and *Smithfield Packaged Meats Corp. v. California Franchise Tax Board*[4] — illustrate the complexities and philosophical differences generated in the quest for fair apportionment.

Lessons From *NuStar* and *Smithfield*

NuStar sold bunker fuel at Texas ports to foreign vessels. Although delivery occurred in Texas, the fuel was immediately transported and consumed outside Texas waters. For purposes of its franchise tax, Texas uses a single-sales-factor formula, sourcing receipts based on "business done in this

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

state."[5] NuStar argued that Texas should adopt an ultimate-destination or market-use test, excluding receipts from the numerator of the formula if the bunker fuel was not used or consumed in Texas. The dispute centered on the statutory language attributing receipts to Texas when goods are "delivered or shipped to a buyer in this state."[6] The Texas Supreme Court declined to read a market-based approach into the statute and held that the statute unambiguously adopts a place-of-delivery (or place-of-transfer) rule. Once possession and control pass to the buyer in Texas, the receipts are sourced to Texas, regardless of subsequent transport or use.

The *NuStar* decision underscores how a bright-line sourcing rule in a single-sales-factor apportionment scheme can produce results that appear divorced from the economic reality of the transaction. This raises the question whether the Texas-source receipts meaningfully reflect the value contributed by the state.

Smithfield arose under California's corporate income tax regime, which generally employs a single-sales-factor apportionment formula but allows the use of a three-factor formula for agricultural businesses.[7] In addition, like other states, California provides a statutory safety valve allowing the use of an alternative apportionment method when the standard formula does not accurately reflect the business done in the state.[8]

Smithfield, a vertically integrated pork producer, challenged the Franchise Tax Board's refusal to classify it as an agricultural business. The FTB, in reaching its conclusion, applied a product-based test, classifying Smithfield's receipts as nonagricultural because the final product had undergone processing (for example, bacon or sausage).

The superior court rejected the FTB's approach, instead focusing on the statute's emphasis on "activities" rather than products. The court found that a substantial portion of Smithfield's income-producing operations were agricultural in nature, notwithstanding the downstream processing activities. The court's analysis reaffirmed that an apportionment method must consider the actual business activities and not merely the products sold.

Addressing the safety valve alternative apportionment issues, the court held that even if Smithfield was not classified as an agricultural business, California's single-sales-factor formula did not fairly represent its in-state business activity, justifying the taxpayer's use of alternative apportionment. With over 98 percent of Smithfield's income-producing activities occurring outside California, reliance on the single-sales-factor formula overstated California's connection to Smithfield's income.

Comparative Analysis

The *NuStar* and *Smithfield* decisions illustrate differing philosophical approaches to the interpretation of apportionment statutes and resolving controversies. The Texas Supreme Court adopted a formalistic, text-driven approach. The court's analysis strictly adhered to the statutory delivery language, declining to incorporate a market-based concept without clear legislative direction. By contrast, the Los Angeles County Superior Court adopted a functional activity-based analysis looking through the underlying regulation to determine whether the formula reasonably

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

represented Smithfield's overall business activity. The *Smithfield* decision also demonstrates that even market-oriented apportionment systems — for example, single-sales-factor systems — may raise fairness concerns when the out-of-state business activity and in-state sales diverge sharply. Both decisions highlight the inherent risks with a single-sales-factor apportionment formula, either by over-attributing income to the state (*Smithfield*) or by sourcing income based on transient transactional contacts (*NuStar*).

Conclusion

The *NuStar* and *Smithfield* decisions illustrate both the rigidity and flexibility of apportionment statutes as well as the risks inherent in a single-sales-factor apportionment scheme. Multistate and multinational businesses must navigate between these poles. As states continue to refine sales-based apportionment, these cases signal that statutory text remains paramount — but equity and activity-based analyses retain an important, if uneven, role in guarding against distortion.

More Compliance and Incomplete Guidance

Lynn A. Gandhi is a partner with Foley & Lardner LLP in Detroit.

Let's hope the implementation of Michigan's new "Wholesale Marihuana Tax"[9] does not foretell the possibility of increasing compliance because of the enactment of new taxes with little preplanning by the Legislature and increasing calls for the Department of Treasury to do more with less.[10]

Even if you are not in the cannabis space, reviewing what is happening in Michigan should be of interest to all. Late in 2025, the Michigan Legislature and governor reached a consensus to find a steady, incremental revenue source that could be committed to road funding. After little public debate, the House proposed a new tax on wholesale "marihuana" (yes, with an "h," because Michigan is special, although the department has indicated they will use the more common "j" for purposes of guidance[11]) on the first wholesale transfer of product from a grower or processor to a retail establishment. The rate of tax is 24 percent, and the wholesaler is permitted to pass the tax on as a line-item charge to the retailer. The legislation quickly moved through both houses and was signed by the governor before year-end as the Comprehensive Road Funding Tax Act, MCL 205.901 et seq., with an effective date of January 1, 2027.

Initially, the Department of Treasury indicated that it would delay collection until early 2027 because it would need to develop and provide guidance, develop forms, and set up and test systems. Frequently asked questions were posted on the department's website to provide guidance to the already struggling marihuana industry. Without fanfare, the delayed collection date of early 2027 was removed from the department's website, with a note that collection was now "under review" and further information would be forthcoming. In mid-April, the department issued updated guidance indicating that the first quarterly payment would be due April 20, 2026.[12]

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

To accommodate the lack of forms, lack of lead time for the affected industry, and perhaps the pending litigation challenging the enactment of the tax, the department indicated in its updated guidance that it would waive penalties and interest for the first three quarters if a business submits at least 75 percent of its tax liability each quarter and files all 2026 quarterly returns with full payment by January 20, 2027.

Thus, just months into 2026, we have a struggling industry with structural banking challenges given a month's notice that it will need to comply with a recently enacted tax and come up with cash to make tax payments. Keep in mind there are no forms yet developed to assist in determining the tax due and there are two different methods to compute the tax depending on whether the transfer of product is between affiliated or unrelated parties. And then apply a rate of 24 percent! In an attempt to provide guidance, the department issued a revenue administration bulletin with more than 29 examples, which contained some apparent inconsistent statements, raising more questions among industry members. It should be noted that the department did not ask to be given a new tax to implement, during the high point of the filing season, with little to no additional budget or staff.

So where are we now? The Michigan Cannabis Industry Association recently filed a complaint[13] challenging the constitutionality of the tax on multiple grounds. First, notwithstanding the label of a "wholesale" tax, the association argues that the tax operates as a sales tax and, because of pyramiding, the resulting total tax on the final consumer exceeds the constitutional 6 percent limit. Second, the association argues that the tax violates the equal protection clause by imposing the entire burden of road funding on a small class of taxpayers without establishing the required rational basis. According to the association, there is little apparent reason why this limited class of Michigan businesses should bear the burden of fixing Michigan's roads. Third, the association claims the tax violates the uniformity clause of the Michigan Constitution by defining the tax base differently depending on the identity of the wholesalers and whether the transferor is affiliated with the retailer. This violates the requirement in the Michigan Constitution that non-property taxes must be levied uniformly upon taxpayers in the same class. An earlier challenge to the tax based on the failure to follow legislative procedural requirements is also pending at the Michigan Court of Appeals.[14]

So what's new in Michigan? Plenty. And despite competing tax proposals from the House and the governor for the new budget, we will see if the existing budget shortfall can be addressed without further new taxes. And if there are new taxes, let us hope that the Legislature is reasonable regarding the burdens of implementation for the department and taxpayers alike.

Where Compliance Comes From

Helen Hecht is uniformity counsel for the Multistate Tax Commission.

In these "Briefly Noted" contributions, we were asked to opine on "areas in which taxpayers may see more *compliance activity* and what that may look like." As always, I can speak only for myself here, and I have no "inside scoop." But for what it's worth, here are my thoughts.

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

I've told this story before. My first tax job was as an intern with the New Mexico Taxation and Revenue Department. I was assigned to help with audit and collection activities. But I'll always remember what the local office manager told me: "The most important thing you have to understand about our tax system is that it's voluntary."

By that, he meant that auditors and collectors can do only so much. But he was also explaining why a big part of my job would be to work the counter and the phones, answering taxpayers' questions, giving them information, and helping them comply. All this to say, I tend to think of "compliance activity" broadly.

This is why complexity is such a problem (at least for those who don't make a living off of it). Take our international tax system and its long reliance on complex transfer pricing theories to combat income shifting. As demonstrated by a number of recent cases, transfer pricing disputes can take years to litigate; will often involve dozens of experts, advisers, attorneys, etc.; and don't always lead to consistent results.[15] For the large multinational corporate groups involved, presumably it's worth it. But what about for the tax system itself?

Apparently, most countries have decided that the answer to that question is no, definitely not worth it. So the international tax system is now shifting to a minimum worldwide tax. And since the Tax Cuts and Jobs Act of 2017, the federal tax system has evolved along the same lines — to a system that's beginning to look a lot more like worldwide aggregation, but with some vestiges of the older, traditional approach. Will there be new compliance issues to deal with? Undoubtedly. Still, it looks like it's moving in the right direction. Finally. And this matters for the states, which have to rely on the federal government's compliance efforts.

But as bad as the transfer pricing problem was, there are other ways in which the effect of complexity on compliance can be "self-reinforcing." And yes, I'm talking about the partnership passthrough system. Partnerships get the advantage of paying tax only once. And to make sure the same substantive tax rules apply, it's taxed to the partners rather than the entity. But this only works because the income is taxed in the same year it's earned, rather than when distributed (which can be delayed indefinitely).[16]

Partnerships, unlike subchapter S corporations, are subject to few limitations on their size or the complexity of their structures. The challenge this presents is how to make sure partnerships are capturing essential tax information and properly conveying it to the ultimate taxpaying partners that need that information to comply with the law. And, of course, that same information is what facilitates any compliance activity, including state or federal audits.

Speaking of which, the federal government has made some faltering attempts to facilitate the audits of large partnerships — most recently enacting the Bipartisan Budget Act of 2015 and creating a federal centralized partnership audit regime. It's still unclear whether this will be any match for the

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

growing complexity of large partnerships. And again, this matters for the states, which rely heavily on the federal government's own compliance efforts.

Still, there are things states can do in the partnership area that, at least in my book, would count as "compliance activity." The first and most important is clarifying how state sourcing rules apply to partnership income. The second may be harder — figuring out how to ensure that partnerships are capturing necessary information, reporting it to their partners, and keeping it for purposes of any state tax audits.

For years, going back to the states' efforts to require partnerships to withhold on their nonresident partners, we've heard arguments that it's simply not possible for partnerships to know enough about their ultimate partners, or vice versa, to comply with certain state tax rules. I personally don't buy that. But I also hope that states don't ignore the important role that clear rules and information reporting play in tax compliance — especially given that our tax system is, at least in some sense, voluntary.

The Convenience of the Employee Might Not Be Convenient for the Employer

Glenn C. McCoy Jr. is a principal in national tax at Ryan LLC in New York.

The COVID-19 global pandemic, which literally plagued the world from March 2020 through May 2023, can be viewed as the primary catalyst that has permanently changed the "office landscape" for corporate workforces. During those years, government-mandated office closures forced employees to work from home rather than from their offices, which created a jurisdictional mismatch for the employees who lived in one state but commuted to work in a different state. As a result, complex tax compliance and reporting issues began to emerge for businesses, and it appears that both remote work and these resulting tax issues are here to stay. According to the Bureau of Labor Statistics, during the past two years, the rates of hybrid and remote work have stabilized as follows: Although 62 percent of the workforce have returned to offices full-time, 26 percent of employees are enjoying a hybrid arrangement, and 12 percent are still fully remote.[17] Of this 12 percent, the records are unclear regarding the percentage of those workers who work and live in a state that differs from their employer.

Although many employers want to offer the flexibility that today's remote work opportunities provide, it is critical for businesses to understand and properly comply with the tax consequences of permitting their out-of-state employees to continue to work remotely.

Employment Tax Issues

The most immediate tax issues involve employee withholding taxes and unemployment insurance taxes. Assuming that the state of residence and the state of employment both have a personal income tax, which state gets the employee's income taxes and where must the employer register for

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

unemployment insurance tax purposes? A classic example of these particular complications is the convenience of the employer rule in effect in New York[18] and a few other states.[19]

Although New York's convenience of the employer rule has existed for decades, its application became more widespread with the advent of the COVID-19 pandemic.[20] The rule dictates that nonresidents working remotely for New York-based employers are taxed by New York unless the work is *necessitated* by the employer's business, not the employee's preference. Recent New York cases, in particular *Matter of Zelinsky I*,[21] strongly uphold the convenience of the employer rule, concluding that remote work performed out of state is taxable by New York if done for the employee's convenience, even if the New York office is closed or the work was conducted during COVID-19 lockdowns. The New York Tax Appeals Tribunal affirmed that only strict business necessity, not personal preference or general remote work, overrides this rule. Connecticut,[22] Delaware,[23] Nebraska,[24] New Jersey,[25] New York,[26] and Pennsylvania[27] all maintain similar convenience of employer rules.

Other Tax Issues Caused by Remote Work

Dealing with employee withholding taxes, however, is just the tip of the iceberg. If an employee resides in a state in which their employer is *not* registered and/or has no business activity, the remote arrangement could trigger entirely new registration requirements and tax liabilities for corporate taxpayers. In these situations, it may become necessary for an employer to register with the secretary of state and other relevant tax authorities, provide a registered agent address, and pay corporate and business activity taxes, sales taxes, and so forth, in addition to the previously discussed employment taxes. If the employer does not recognize these potential obligations at the time the remote employee is hired, someday the business may well face multiple years of taxes, interest, and penalties for failure to register, file, and pay the inadvertently missed obligations.

Considering the variety of work arrangements for remote workers, and the numerous approaches by states to tax them, complicated tax compliance issues relating to out-of-state remote workers will remain for the near future.

High Taxes Drive Out Residents, Drive Up Enforcement

Timothy P. Noonan is a partner in the Buffalo and New York City offices of Hodgson Russ LLP.

Compliance and enforcement activity in the personal income tax area follows a similar and somewhat logical pattern, especially in the state tax residency area: States raise their tax rates, high-net-worth taxpayers move out of the state, and then the state audits those taxpayers. We've seen this play out in the past decade, especially in New York. The cap on the state and local tax deduction in 2017 led many taxpayers in high-tax states to seek greener pastures in states where getting a SALT deduction didn't matter (because there was no SALT).[28] Heavy enforcement followed.[29] A few years later, the

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

combination of the COVID-19 pandemic and the rise in tax rates in New York caused another major exodus and led to an unprecedented audit initiative in New York with thousands of new audits, especially so-called desk audits of former New Yorkers.[30]

We now seem to be at another inflection point, with various states either raising tax rates or proposing new taxes on high-income taxpayers. For example, as we reported in a recent installment of a *Tax Notes State* column, a California labor union has proposed the first-of-its-kind wealth tax — via a ballot initiative — on the net worth of California billionaires.[31] And this initiative will appear on the November 2026 ballot because it was just announced that the backers have collected over 1.5 million signatures, which is more than enough to clear the 875,000 threshold.[32] Although we don't know what the outcome will be — many are opposed to it, including the California governor — that hasn't stopped a not-insignificant portion of the 200-plus billionaires cited by the act's proponents from taking matters into their own hands and leaving the state for good.[33]

Not to be outdone, the state of Washington, just a few years after losing its status as a tax-free state with the imposition of a tax on capital gains (which caused many taxpayers to leave or consider leaving the state),[34] now is all in with the recent enactment of a full-scale personal income tax on income over $1 million at the rate of 9.9 percent.[35] Maine also recently enacted a 2 percent income tax surcharge on income over $1 million.[36] And of course, never a stranger to new taxes or higher tax rates, New York is in the midst of heated budget negotiations in which consideration is being given not only to higher tax rates on the wealthy but also to the imposition of a new pied-à-terre tax in New York City that would apply to nonprimary residences valued at or over $5 million.[37] For these (and certainly other) reasons, taxpayers are leaving these high-tax states. For example, between July 2024 and July 2025, Los Angeles County lost 54,000 residents.[38] And New York City experienced a net loss of about 114,000 people in 2025.[39]

So if past is prologue, as tax rates go up and residents flee these states, we can expect to see an increase in the amount of tax enforcement on this same class of taxpayers. And why not? In any audit, the taxpayer has the burden of proof. So in a residency case, that means the taxpayer has the burden to prove, usually by clear and convincing evidence, that they left the state and established themselves as a resident of the new state. This is no easy task. Unlike in baseball, a tie does not go to the runner. If a court finds that a taxpayer has equal ties to two different places, the court will likely conclude that the taxpayer has failed to meet their burden of proof.[40] Given the high standard of proof and faced with the economic reality that the loss of so many high-paying taxpayers is unsustainable, it's no wonder that historically we have seen the most aggressive audit activity in states with the highest taxes. And it will be no surprise if we see that trend continue in states that continue to push the envelope with new and higher taxes.

The Audits Are Coming! The Audits Are Coming!

Jamie E.T. Szal is a partner at Brann & Isaacson in Lewiston, Maine.

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

I could not very well be a SALTy New Englander, writing this over Patriots' Day weekend without working in a Paul Revere reference. We have been sounding this warning cry to our clients for quite some time. If my firm were limited to "one, if by state, and two, if by city," our signal lamps would have to alternate between one and two in a cribbed Morse code. The audits — and auditors — are here.

Our clients face a veritable onslaught of audits spanning the United States from coast to coast. Washington and California are auditing. Texas is auditing. Arizona is auditing. Minnesota is auditing. Wisconsin. Nebraska. Illinois. Ohio. Georgia. Florida. New Jersey. Pennsylvania. New York. Massachusetts. Vermont. My own home state of Maine. And then there are the cities sending out their foot soldiers. Philadelphia. All the Colorado home rule cities. Several of California's cities. Chicago.

When our firm litigated the *Wayfair* case,[41] we raised our deep concern that e-commerce companies, many with very small internal tax teams, would face multiple simultaneous audits. We were right. Companies struggle to manage the volume of audit demands within the timelines that auditors demand.

To fully understand when a compliance burden becomes an undue burden for companies, we have to consider not just the complexity of what is taxed and at what rate but also the administrative demands on companies trying to comply. Most auditors have blinders on, unwilling to consider the burden on the companies of grappling with that level of inquiry all at once. (As an aside, this is a full-circle moment for me. I recall, in the early days of my career at the Massachusetts Department of Revenue, thinking I was generous to give a company 30 days to respond. Now that I represent companies, I laugh at my naivety.) Auditors operate on their own internal timetable, some giving as little as two weeks to respond, many refusing reasonable extensions to allow a company to better project-manage multiple competing deadlines set by the other auditing states. The lack of uniformity among states extends to the data that auditors demand to satisfy their audit inquiries.

There are three trends coming through these audits:

1) Multiple states are proactively using the data they have about companies' filing records once they start compliance to go after those companies for preregistration, post-*Wayfair* periods. Arizona, Illinois, and Michigan are at the forefront of this trend. Michigan, most frustratingly, sends companies a letter suggesting they needed to register at an earlier date and directing recipients to the state's voluntary disclosure agreement program, only for those companies to be told by the voluntary disclosure agreement team that they are not eligible for the program because they are already registered. Talk about confusing the layperson. The bait-and-switch does nothing to assuage a company's concerns about the challenges it faces.

2) Multiple other states are using that same data to launch other business tax inquiries, such as California, Kentucky, Michigan, Minnesota, New Jersey, Pennsylvania, and Wisconsin. For example,

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

California's Franchise Tax Board has ordered the state's Department of Tax and Fee Administration to send it an annual report of vendors registered for sales and use tax purposes whose reported sales tax receipts exceed the franchise tax economic nexus threshold. California then sends the companies on that list that are not yet registered for franchise tax purposes a demand for *corporation* income tax returns. This demand fails to account for that company's actual business entity type. It also flies in the face of the successful litigation brought by my firm on behalf of the American Catalog Mailers Association to challenge California's effort to target companies protected by P.L. 86-272.[42]

3) Lastly, states are leapfrogging their way from retailers to their vendors and back on the hunt for anything that the state can argue is taxable software, with a particular focus on e-commerce software-as-a-service vendors. States want a piece of the whole e-commerce ecosystem, not just the retailers selling us the latest "it" phone, sweater, or bag.

The Supreme Court in *Wayfair* left open the question of what exactly "undue burden" means these days. With the rate of audits coming, I expect we'll soon see the e-commerce tax fight boil over into a full-scale revolution litigating that very question.

Focus on State Tax Compliance: 2026

Kathleen K. Wright teaches in the state and local tax program in the Braden School of Taxation at Golden Gate University.

Where will state tax authorities focus their attention in 2026 and 2027? As state tax authorities look ahead, one area stands out as a likely focal point for enhanced compliance efforts: residency. Residency audits stepped into the limelight with the acceptance by employers of remote work as the norm (rather than the exception). Residency audits may again draw enhanced resources if the California billionaire's tax proposal is slated for the November ballot and is enacted. Clients are already requesting tax advisers to provide a relocation strategy as California's tax burden continues to evolve. This tax (if enacted) targets the superrich, who would probably be subject to a California residency audit regardless of why they moved. But this additional tax may just be the extra incentive for them to take the plunge and move to a state with no individual income tax. That means residency audits may be on the upswing as California tries to keep its tax base from slipping away.

Status of Billionaire's Tax Proposal

The billionaire's tax proposal is expected to appear on the November 2026 ballot if it satisfies the signature requirements (874,641 certified signatures must be submitted for verification by June 25). Because the measure is a citizen-initiated ballot proposition, it would pass with a simple majority vote. The tax would be calculated as of December 31, 2026, and would be due with the 2026 California income tax returns.

Who Would Be Subject to the Billionaire's Tax?

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

The initiative would impose a tax on individuals determined to be California residents as of January 1, 2026 (the "tax obligation date"), with net worth subject to the tax measured as of December 31, 2026 (the "valuation date"). It assigns 100 percent of the taxpayer's wealth to California, regardless of the location of the taxpayer's assets or the residency of the taxpayer after January 1, 2026. In other words, billionaires leaving the state after January 1, 2026, would still have to pay the one-time tax because it is assessed retroactively on California residents as of that date. Constitutional issues abound using this approach.

How the Billionaire's Tax Will Operate

If enacted, the initiative would impose a one-time 5 percent excise tax on the net worth of resident taxpayers of $1 billion or more. The proposal looks to the California-resident taxpayer's worldwide assets, which include:

- publicly and privately held securities;
- business interests;
- contractual rights; and
- trust interests and transferred assets.

Exclusions from this computation include interests in real property not held in an entity (such as a principal residence), tangible personal property located outside California for at least 270 days in 2026, and certain retirement accounts.

The proposal also includes detailed valuation rules.

Will Billionaires Move?

What does the data say? The IRS publishes data on interstate moves by taxpayers with the latest report covering 2022 and 2023.[43] This report shows that Texas, Florida, North Carolina, South Carolina, and Tennessee[44] have experienced net inbound migration, while California, New York, Illinois, New Jersey, and Massachusetts have seen net outflows.[45] The IRS migration data are based on year-to-year address changes reported on individual tax returns filed with the IRS. All the states that lowered taxes on high-income taxpayers in the past few years gained more wealthy taxpayers than the states that raised their tax rates during that time.

Although relocation decisions are influenced by a variety of factors, tax policy remains an important consideration — particularly for the ultra-high-net-worth individuals. Even a one-time tax like the billionaire's tax may lead some taxpayers to reevaluate their connections to a particular state.

Compliance Implications

In this environment, residency determinations are likely to receive increased attention as part of California's broader compliance efforts. The Franchise Tax Board has long devoted significant resources to this area, reflecting the importance of residency in the state's tax system. The statutory provisions governing residency have not changed and there is an abundance of case law and

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

checklists that provide taxpayer guidance. The issue in these audits is typically whether the taxpayer possesses documentation that they moved and established residency in another state. Practitioner guidance is essential because it can help a taxpayer prepare for an anticipated audit.

Conclusion

California's tax authorities are well positioned to address residency issues through their audit programs and expertise. Therefore, taxpayers who were or are California residents on or after January 1, 2026, and meet the $1 billion threshold, should begin thinking about what impact the billionaire's tax will have on them and whether this incremental tax burden is enough to warrant a move.

FOOTNOTES

[1] *Container Corp. of America v. Franchise Tax Board*, 463 U.S. 159, 164 (1983).

[2] *Norfolk and Western Railway Co. v. Missouri State Tax Commission*, 390 U.S. 317, 328 (1968).

[3] *NuStar Energy L.P. v. Hancock*, No. 24-0037 (Tex. Mar. 13, 2026).

[4] *Smithfield Packaged Meats Corp. v. California Franchise Tax Board*, No. 21STCV39637 (Cal. Super. Ct. Los Angeles County Feb. 26, 2026). The court finalized the proposed ruling on April 28. Caitlin Mullaney, "Smithfield Foods Victorious in California Single-Sales-Factor Case," *Tax Notes State*, May 4, 2026, p. 366.

[5] Tex. Tax Code Ann. section 171.103(a).

[6] *Id.*

[7] Cal. Rev. & Tax. Code section 25128.

[8] Cal. Rev. & Tax. Code section 25137.

[9] Mich. H.B. 4951, Public Act 23 (Oct. 7, 2026).

[10] The author acknowledges that she is representing the Michigan Cannabis Association in a lawsuit challenging the constitutionality of the excise tax at the Michigan Court of Claims. The case is *Mitten Distro X LLC v. Michigan Department of Treasury*, Docket No. 26-000061-MT (Mich. Ct. Cl. Mar. 28, 2026).

[11] Michigan Department of Treasury, Revenue Administrative Bulletin 2026-3 (Mar. 17, 2026).

[12] Michigan Department of Treasury, "Reporting and Remitting Tax to Treasury" (last visited Apr. 30, 2026).

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

[13] *Mitten Distro X LLC*, Docket No. 26-000061-MT.

[14] The Michigan Supreme Court ordered the Michigan Court of Appeals to "expedite its consideration of this case." Order, *Michigan Cannabis Industry Association v. Michigan*, SC 169811 (Mich. Apr. 22, 2026).

[15] *See, e.g.*, *3M v. Commissioner*, 154 F.4th 574 (8th Cir. 2025); *Medtronic v. Commissioner*, 153 F.4th 682 (8th Cir. 2025). See also the pending appeals from decisions of the U.S. Tax Court in *Coca-Cola Co. v. Commissioner*, 155 T.C. 145 (2020), and *Facebook Inc. v. Commissioner*, 164 T.C. No. 9 (2025), and from a U.S. district court in *Perrigo Co. PLC v. United States*, No. 1:17-cv-00737 (W.D. Mich. Jan. 27, 2026). See also the pending Tax Court cases *Eaton Corp. v. Commissioner*, Nos. 2607-23 and 2608-23, and *Abbott Laboratories v. Commissioner*, No. 20227-23.

[16] Basically, partners can simply defer taking any distributions or can use a well-known scheme involving the borrowing of funds effectively guaranteed by future partnership distributions to avoid recognizing income. *See* Rachel Louise Ensign and Richard Rubin, "Buy, Borrow, Die: How Rich Americans Live Off Their Paper Wealth," *The Wall Street Journal*, July 13, 2021.

[17] *See* Connor Borkowski and Rifat Kaynas, "Telework Trends," 14(2) *Beyond the Numbers* (Mar. 2025).

[18] *See* N.Y. Comp. Codes R. & Regs tit. 20, section 132.18.

[19] At least six states (and certain municipalities) maintain a convenience of the employer rule, which deems employees working from out of state for an in-state employer to owe state income tax primarily to the state in which the employer is located, unless working outside the state is required by the employer.

[20] *See* N.Y. Comp. Codes R. & Regs tit. 20, section 132.18(a).

[21] *Matter of Zelinsky*, DTA Nos. 830517 and 830681 (N.Y. Tax App. Trib. May 15, 2025).

[22] Conn. Gen. Stat. section 12-711(C).

[23] 30 Del. Code section 1124(b).

[24] 316 Neb. Admin. Code section 22-003.01C.

[25] N.J. Stat. section 54A:5-8(e).

[26] N.Y. Comp. Codes R. & Regs tit. 20, section 132.18.

[27] 61 Pa. Code section 109.8.

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

[28] *See* Timothy P. Noonan, "Changing State Tax Residency: The Most Powerful (and Common) Response to the TCJA?" Noonan's Notes Blog, June 11, 2018.

[29] Based on audit data our firm obtained via a New York Freedom of Information Law request in 2025, the New York State Department of Taxation and Finance opened over 5,000 personal income tax audits in 2020 alone.

[30] Based on the same data obtained via our request, the state opened 11,071 audits in 2022 and 7,911 in 2023.

[31] *See* Noonan, Noah S. Chase, and Daniel P. Kelly, "California's New Wealth Tax Proposal: Are They Serious?" *Tax Notes State*, Feb. 23, 2026, p. 607.

[32] *See* Juliet Chung and Paul Kiernan, "California's Billionaire Tax Has the Signatures to Make the Ballot, Backers Say," *The Wall Street Journal*, Apr. 26, 2026.

[33] *See* Elijah Nicholson-Messmer, "As Ultrarich Sweat, Advisors Tackle 'Ripple Effects' of Proposed Billionaire Tax," *Financial Planning*, Feb. 6, 2026.

[34] *See* Noonan and Joseph F. Tantillo, "Peace Out, Pacific Northwest: An Exit Strategy for Washington Residents," *Tax Notes State*, Oct. 6, 2025, p. 7.

[35] *See* Washington Gov. Bob Ferguson press release, "Governor Ferguson Signs Millionaires' Tax Into Law" (Mar. 30, 2026).

[36] *See* Chung and Kiernan, *supra* note 32.

[37] *See* New York City mayor's office press release, "Mayor Mamdani, Governor Hochul Announce State's First Pied-à-Terre Tax, Requiring Ultrawealthy and Global Elites to Pay Their Fair Share" (Apr. 15, 2026).

[38] *See* Jenny Jarvie, "People Are Leaving Los Angeles, and It Could Haunt Us for Decades," *Los Angeles Times*, Apr. 9, 2026.

[39] *See* Chris Wade, "Report: NYC Exodus Amid High Taxes; Diminishing Services," *The Center Square*, Apr. 22, 2026.

[40] *See, e.g.*, *Kartiganer v. Koenig*, 194 A.D.2d 879 (N.Y. 1993).

[41] *South Dakota v. Wayfair Inc.*, 585 U.S. 162 (2018).

[42] *American Catalog Mailers Association v. California Franchise Tax Board*, Case No. CGC-22-601363 (Cal. Super. Ct. San Francisco County Dec. 13, 2023).

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.

[43] Internal Revenue Service, "Statistics of Income Tax Stats — Migration Data 2022-2023" (Mar. 20, 2026).

[44] According to a report published by the National Taxpayers Union Foundation (NTUF), the states gaining the most residents include Texas, which gained a new resident every 4 minutes and 40 seconds, Florida (every 4 minutes and 42 seconds), North Carolina (every 7 minutes and 36 seconds), South Carolina (every 8 minutes and 54 seconds), and Tennessee (every 12 minutes and 15 seconds). Andrew Wilford, "Migration in Minutes: Latest IRS Data on Interstate Migration Shows Taxpayers Continuing to Flee California and New York," NTUF (Apr. 6, 2026).

[45] According to the NTUF report, the states losing the most residents include California, which lost a resident every 2 minutes and 37 seconds, New York (every 3 minutes and 20 seconds), Illinois (every 9 minutes and 42 seconds), New Jersey (every 17 minutes and 36 seconds), and Massachusetts (every 18 minutes and 32 seconds). *Id.*

END FOOTNOTES

(C) Tax Analysts 2026. All rights reserved. Tax Analysts does not claim copyright in any public domain or third party content.