Goodbye, 2020! Goodbye, Goodbye, Goodbye!

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The coronavirus has presented one of the greatest challenges in our lifetimes. The loss of life is heartbreaking and tragic. In response to the economic impact of the pandemic, our federal government administered financial triage through the CARES Act stimulus bill, at an enormous cost that was nevertheless woefully inadequate in the eyes of many. Even with the anticipated distribution of promising vaccines, the pandemic will continue well into 2021 as we usher in a new administration with President-elect Joe Biden and await the results of a runoff in Georgia to determine control of the United States Senate. The uncertainties are many, but it seems clear that the actions — and inactions — of our federal government will greatly affect the financial pressures on the states, and in turn affect state tax policies, legislative actions, and state tax administrations.

Regardless of federal help, states will need to take action to deal with this financial crisis. States will be facing a budgeting conundrum on a very large scale: the need to recover significant lost revenues in 2020 and into 2021 (and likely beyond that), with the conflicting need to spend money to help those individuals and businesses most severely affected by the pandemic. Some industries — most notably brick-and-mortar retail, hospitality, and sports and entertainment, as well as other large event venues — have been in the eye of this economic storm. These businesses employ millions and contribute enormously to state and local government revenues, both directly and indirectly through those they employ. States, for their own financial benefit, need to help these businesses survive. 2020 also brought renewed attention to social injustices, and the cost of critical social programs will need to be taken into account. An urgent need to address and balance these needs will likely manifest in new legislation and new tax agency priorities and initiatives.

Many state legislatures, particularly in states that entered the pandemic with a budget deficit, may need to put greater emphasis on raising revenues. In contrast, states that started 2020 with a rainy day fund may have more flexibility, a greater ability to balance these needs, and be positioned to attract businesses from higher-taxing states.

States will also need to address changes in business operations, initially forced by the pandemic — most notably the increase in remote workers. The trend toward more remote workers, and greater flexibility in working location, is expected to continue after the pandemic. This trend will raise issues of employer nexus, sourcing employee income for withholding and reporting, unemployment tax, labor laws and risk management, and exacerbate worker classification issues, just to name a few. States will need to anticipate the impact of these business operational changes and develop state tax policy and changes to state and local tax laws. Efforts have been made in the past, including during this pandemic, to spur congressional action to create a unified approach on remote workers. Expect those efforts to continue in 2021, but unless and until Congress takes action, this will be an extremely challenging issue for businesses and state and local governments in the coming year.

One other issue that will likely get renewed attention in 2021 is the state and local tax deduction cap workaround for flow-through entities, given the recent notice by the IRS.[39] That notice may inspire action by some states, but there is also speculation that the Biden administration may support raising or eliminating the cap.

But state budgets will likely be the focus of state legislatures and state agencies given the size of the revenue shortfalls and taxpayer needs. With such high stakes, look for states to consider:

- significant "tinkering" with current tax systems, such as increases in tax rates and/or graduated tax rates; decoupling from select (revenue losing) sections of the IRC; eliminating, reducing, or deferring

[39] Notice 2020-75, 2020-49 IRB 1.

deductions and credits; and changes to tax incentive programs;

- transfer pricing initiatives, such as the new programs in Indiana and North Carolina;
- tougher sales tax enforcement and refinements to post-*Wayfair* sales tax nexus laws, and to the rushed and inconsistent marketplace facilitator laws, now that the dust has settled post-*Wayfair*, at least to some extent;
- testing the waters in applying *Wayfair* nexus concepts to income and other taxes, and efforts to erode the protections of P.L. 86-272; and
- continued exploration of ways to tax e-commerce, such as digital advertising taxes and various efforts to tax online services.

A consistent theme may be a less hospitable approach by some states to out-of-state businesses. While this is not a new concern, the financial needs caused by the pandemic may escalate it.

Finally, timing will be an interesting factor to watch. State legislative sessions will likely commence before we have definitive answers on the pandemic (and with challenging social distancing procedures needed), solid and complete economic data upon which states can make decisions, and further federal action (if any). States will be watching their counterparts to copy good ideas and to avoid more extreme actions that could jeopardize economic development.

Recent years have seen a scattershot approach to significant SALT law changes by states, first in adopting *Wayfair* nexus laws, and then marketplace facilitator laws. The 2021 state-by-state recovery efforts from the worst pandemic in over a century will undoubtedly be very diverse.