

## **Exhibit J**

Preliminary List of Issues to Address in Taxation of Software and Related Services

## **Mississippi Taxation of Remote Internet-Based Computer Software Products and Services Study Committee**

### **Preliminary List of Issues to Address in Taxation of Software and Related Services**

The following is a preliminary list of the many policy and practical issues previously identified and discussed related to Mississippi's taxation of software and related services. Many of these were discussed at the Department of Revenue's hearing on its proposed regulation on November 3, 2021. The purpose of this preliminary list is to assist in identifying the scope of the issues that should be addressed by future legislation. Once finalized, the committee members can formulate and share their initial policy proposals for further discussion.

Members of the committee and the public are invited to suggest additional issues to be included in this list, which will be finalized prior to the next committee meeting in July.

- Core definitions
  - Software
    - Traditional definition
    - Should software be categorized as TPP, or a specified digital product, or both?
    - Does software include data?
    - Does software also include means of delivery or access?
  - Computer Software Sales and Services (current § 27-65-23)
    - What exactly does / should this mean?
    - Does this encompass the software itself, or just services related to selling software?
    - Traditionally encompassed on-site programming, etc. at a location in the state.
      - Much of this is now performed remotely.
  - Cloud computing
    - Is this a generic catch-all phrase for a combination of services, means of delivery, and products accessed or provided remotely?
  - SaaS – Software as a Service
    - Is there a difference between licensing software that will be used remotely and hiring someone to perform a service requiring them to utilize software?
      - i.e., the “true object” test
  - PaaS / IaaS – Platform / Infrastructure as a Service
    - Essentially the rental of space on a physical server or network located at a site other than that of the user.
    - Should this be taxable in Mississippi if the beneficiary of that is located here?
      - How to determine that physical location?

- If the underlying equipment is not in Mississippi, on what authority would Mississippi tax the rental of that property located outside the state?
  - Are there any other instances in which the state taxes the use of property that never physically enters the state?
- Sales versus use tax
  - Must distinguish which tax scheme applies to a given transaction.
  - If any item would not be subject to use tax (e.g., a service), should it be subject to sales tax solely because a remote provider has a certain level of sales in the state?
  - The use tax has a credit for sales taxes paid, but going forward should that also work in the reverse?
    - Ex. 1 – If a vendor paid or was assessed a sales tax, that same transaction would be exempt from use tax at the purchaser level.
    - Ex. 2 – If an end user self-remitted or was assessed use tax, should the vendor be exempt from sales tax assessment on the other side?
- Product v. Service Distinction
  - Should we formally adopt the “true object” test used by other states?
    - If so, should that extend beyond just software?
  - How do we distinguish between the actual licensing or sale of software, and the provision of non-taxable services that happen to utilize software?
- Location of traditional services for purpose of assessment
  - How to determine where a service is performed when the individuals providing the service are not located in same place as the recipient.
  - Are there any other instances in which Mississippi levies the sales tax on a service based exclusively on where the benefit is received rather than the physical location of the person performing the service?
- Taxation of mixed transactions
  - How to determine what portion of a single license fee or charge represents taxable v nontaxable items or items attributable to exempt / reduced rate / ordinary rate areas of a single purchaser.
  - How to determine what portion of a single license fee or charge is attributable to in-state versus out of state use.
    - Ex. 1 – A single license agreement that encompasses multiple distinguishable products or software platforms
    - Ex. 2 – A single license agreement authorizing access to or use of a product by users located in multiple jurisdictions
- Wholesale and resale transactions
  - How to define and document sales of software or services that are wholesale or resale transactions
    - Ex. 1 - Licensure of software that is in turn sub-licensed to another party
    - Ex. 2 – Licensure and use of software in providing a service that is taxable in its own right

- Internal / intercompany transactions
  - Should we distinguish how we tax the use of internal software that is self-developed versus that acquired from a third party?
  - If a company employee accesses software maintained on a server outside Mississippi, is that the same as the importation of TPP into the state?
    - If so, how is value determined for use tax purposes?
  - If an affiliate provides typical intercompany services to other affiliates that requires the use of software, should that be taxable?
    - Ex. – accounting, legal, purchasing, IT support, etc.
    - If so, how is that value to be determined?
      - If embedded within a general management of administrative services charge, how do we determine that portion attributable to the software?
      - If no charge is made, may one be imputed?
      - Are those intercompany charges subject to arms-length adjustments?
  - How do we treat the internal charge out of general administrative / overhead charges to Mississippi affiliates/locations for expenses actually incurred in cost centers outside the state?
    - Ex. 1 – Cost center at corporate headquarters outside Mississippi utilizes software that would have been taxable if located or actually used in the state. If that centralized cost is “pushed out” to the business locations, does that convert those extraterritorial uses into taxable transactions here?
    - Ex. 2 – The reverse of the above. If that cost center is located in Mississippi, does the “push out” to non-Mississippi locations mean that the original use escapes Mississippi taxation?
  
- Export exemption
  - Under what scenarios would the exemption for software or software services transmitted by the Internet to a destination outside the state apply?
  - How is “first use” determined?
  
- Industry-specific applications and questions
  - Internet service providers
  - ACH services
  - Bank core software
  - Medical billing software
  - Advertising / marketing
  
- Constitutional issues
  - How to avoid unconstitutional double taxation
    - Mississippi currently taxes 100% of any software loaded/maintained on server located in the state.
    - DOR proposes to tax the use of remotely maintained software if accessed by user in state.

- Classic internal consistency problem under Commerce Clause.
  - Credit for taxes paid to other states or taxes paid by other party to transaction.
    - Equality of credits/exemptions from sales tax for use taxes paid on same transaction (see above), to be on par with use tax exemption for sales taxes paid/assessed.
    - When is it appropriate to grant a credit for taxes paid to other jurisdictions?
    - What conditions would apply?
    - How to handle different policies adopted by different states?
      - Ex. 1 - Software was not actually taxed by the other state but would have been under Mississippi law.
      - Ex. 2 – Situation where Mississippi may have treated first acquisition as sale-for-resale but other state had different policy and tax was actually paid to that other state. Does Mississippi get to deny the credit for the taxes actually paid based on its different policy?
  - Are sales taxes apportionable generally?
    - If so, how to compute that ratio?
      - Number of authorized users?
      - Actual utilization?
      - Bundled transaction / multiple product issues?
  - Potential conflict with Internet Tax Freedom Act
- Procedural issues
  - Collection / self-reporting issues
    - Should all of these software related taxes be administered via a direct pay permit to remove the vendor from difficult determinations on taxability, rates, etc. that turn on end user facts and operations?
    - Is this necessary to avoid multiple / overlapping collection points?
  - Direct refunds claimed by end-users
    - If a vendor collects tax on a nontaxable item or collects at an incorrect rate, should the end user be able to seek a refund directly from the DOR or must they go through the vendor?
      - What are the end user's rights if the vendor refuses to cooperate?
  - End-user defenses to collection action brought by vendor following audit
    - Should we allow the end user to raise substantive defenses against a vendor who attempts to collect a tax retroactively, or should their liability be at the mercy of the vendor's defense or capitulation to an audit?
  - Transition and implementation of any new rules or policies
    - Will the new rules be retroactive or prospective?
  - Clarification of policies applicable to pre-adoption periods