



Legal Alert: MTC to Explore Apportionment Regulations for Cloud Services, Software and Electricity

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While meeting in Denver this week, the Multistate Tax Commission's Income Tax Uniformity Subcommittee advanced two separate projects to develop industry-specific apportionment regulations. One project will look at the electricity sales factor and the other will look at methods to source cloud services and software. Industry-specific apportionment projects like these help demonstrate why the MTC separately struggles with drafting a one-size-fits-all, uniform apportionment rule as they try to amend UDITPA.

The first apportionment project will examine the sourcing of electricity. MTC staff presented research on how states source electricity for income tax purposes. The staff concluded that while 31 states treat electricity as tangible personal property for sales factor purposes, there is little uniformity in how sales of electricity are reflected in the factor. The staff also noted that litigation and an increasing number of taxpayers requesting a specific apportionment methodology indicate uncertainty. After hearing the staff presentation, the Subcommittee voted to continue the project in an educational phase. The Subcommittee specifically instructed the staff to examine a prior model regulation drafted by the NorthEastern States Tax Officials Association (NESTOA), involve industry, and to consider lateral issues like P.L. 86-272 and nexus. The NESTOA model, which is the basis for Massachusetts' regulations, provides an elaborate series of rules for different types of sales, such as retail and wholesale. The NESTOA model also includes a throwout rule that excludes receipts from both the numerator and denominator if they are made to a jurisdiction in which the taxpayer is not subject to tax. The Subcommittee contrasted the NESTOA model with a simpler approach taken by Oregon that sources based upon a transmission point rather than the ultimate destination.

The second apportionment project is a newly launched effort to examine whether a model regulation to source cloud services and software is desirable. Several states noted that they have seen a dramatic increase in requests for letter rulings and

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informal advice on how to source cloud services. Idaho and Washington commented that they struggled with cloud service sourcing issues as they drafted legislation and regulations. The Subcommittee instructed MTC staff to research the issues and report back when they next meet. Washington, Idaho and North Dakota, offered to provide the research they have already done on the issue. The Subcommittee is scheduled to meet in person again at the MTC's annual meeting in July.

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