

MISSISSIPPI TAX BULLETIN

STATE AND LOCAL TAX REPORTS AND PLANNING

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MISSISSIPPI INCOME TAX DEVELOPMENTS SPRING 2006

by J. Paul Varner

I. LEGISLATIVE DEVELOPMENTS.

A. Importing/Exporting Tax Credit. Legislation was enacted in 2004 that entitles taxpayers to an income tax credit for certain charges paid in connection with importing or exporting products at public seaports and airports located in Mississippi. Bills were passed in the 2006 legislative session to reduce from \$5 million to \$2 million the minimum capital investment that must be made in Mississippi to be eligible for the credit, and to extend the date of repeal of such credit to July 1, 2010. (House Bill 744 and Senate Bill 2652, effective July 1, 2006).

B. Credit for Jobs Skills Training Costs. Mississippi law allows an income tax credit equal to 50% of the costs incurred by certain employers for providing skills training programs to its employees. A Bill was passed in the 2006 legislative session to extend the date of repeal of such credit to July 1, 2008. (House Bill 745, effective July 1, 2006).

C. Credit for Broadband Technologies. Mississippi law allows an income and franchise tax credit to telecommunications enterprises for the cost of equipment used in the deployment of broadband technologies. A bill was passed in the 2006 legislative session to extend the period during which such credit may be claimed until July 1, 2020. (House Bill 1507, effective July 1, 2006).

D. Growth and Prosperity Act Amendments. Under the Growth and Prosperity Act, approved businesses locating in certain designated counties are granted exemptions from all state income, franchise, and sales/use taxes and most county property taxes. A bill was

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passed in the 2006 legislative session to extend from December 31, 2015 to December 31, 2020 the period within which state and local tax exemptions may be granted under the Growth and Prosperity Act. The bill also extends from December 31, 2005 to December 31, 2010 the period within which a county may apply to become a designated growth and prosperity county. (House Bill 1510, effective January 1, 2006).

E. **Credit for Rehabilitation of Historic Structures.** A bill was passed in the 2006 legislative session to allow an income tax credit for a portion of the cost incurred to rehabilitate a certified historic structure or a structure located in a historic location that has been certified by the State Department of Archives and History. The credit is equal to 25% of the costs incurred for an owner-occupied dwelling and 50% of the costs incurred for all other property. (Senate Bill 3067, January 1, 2006).

II. ADMINISTRATIVE DEVELOPMENTS.

A. **Income Tax on Gaming Winnings.** The Mississippi State Tax Commission amended the income tax regulations relating to gambling winnings and losses effective July 30, 2005. The regulations update procedures for reporting, withholding requirements, and reduce the tax rate on gaming winnings. Income Tax Regulation 309 was amended to reduce the tax rate from 5% to 3% on all gross gaming winnings in Mississippi. Gaming losses are not deductible against gaming winnings for income tax purposes. Income Tax Regulation 1122 requires Mississippi gaming establishments to withhold 3% of gaming winnings. Forms W 2G or 1099 that reflect such income and the 3% withheld by gaming establishments serve as the filing for the gambling patrons. The gaming establishments must file a monthly return and pay the amount withheld on or before the 15th of the following month. The amended regulation also changes the length of time that gaming establishments are required to keep records and information from four years to three years.

B. **Wage and Tax Statements.** The Mississippi State Tax Commission amended Income Tax Regulation 1114, which addresses the filing of wage and tax statements and reports, effective July 17, 2005. The amended regulation states that all wage and tax statements and reports must be filed on or before the date prescribed by the Commissioner. Previously, the regulation required all such statements and reports to be filed by January 31.

C. **Terminated Employees.** The Mississippi State Tax Commission amended Income Tax Regulation 1115, which pertains to terminated employees. Effective July 17, 2005, statements furnished to terminated employees must be reported on Form W 2 and provide all information required by the Commissioner and the Internal Revenue Service. Each statement should identify withholdings regardless of source, on a state by state basis, with the withholdings for each state identified.

D. **Withholding Records.** The Mississippi State Tax Commission amended Income Tax Regulation 1120, which pertains to withholding records to be kept by employers. Effective July 17, 2005, employers are required to keep for a period of three years the following: all wage, tax, and income information statements and reports required by the Commissioner along with copies of Form W 2s that cannot be delivered to the employee after a reasonable effort by the employer.

E. **GO Zone Act Guidance.** On December 21, 2005, the Mississippi Tax Commission provided guidance regarding the Mississippi income tax treatment of the tax relief portions of the Gulf Opportunity Zone Act of 2005 ("The GO Zone Act").

1. *Bonus Depreciation.* Income Tax Regulation 504 provides that bonus depreciation is not an allowable deduction. Accordingly, Mississippi law does not follow the federal provisions allowing a 50% first year bonus depreciation related to rebuilding.

2. *Timber Expensing and Carryback.* Mississippi does not follow the federal law allowing small timber producers to double the expensing amounts for qualified timber property under 500 acres. Nor does Mississippi allow a five year “farming” carryback of certain net operation losses. Mississippi does provide a reforestation credit equal to 50% of the cost of an approved reforestation plan subject to a lifetime credit of \$10,000.
3. *Net Operating Loss Carryback.* Mississippi income tax law provides for a net operating loss carryback of two years and a net operating loss carry forward period of twenty ears. Mississippi does not follow federal law, which allows certain net operating losses to be carried back for five years under the GO Zone Act.
4. *Environmental Remediation Cost Expensing.* The GO Zone Act allows taxpayers to currently expense environmental remediation costs incurred to qualified contaminated sites as a result of Hurricane Katrina for two years, through December 31, 2007. Mississippi does not allow this deduction. However, a tax credit of 25% is specifically allowed for remediation activities performed at Brownfield sites throughout Mississippi. The annual credit will be equal to the lesser amount of the amount of income tax imposed on the Brownfield site, or \$40,000, and the maximum lifetime credit for each site is \$150,000. In order to qualify for this credit, taxpayers be approved by the Department of Environmental Quality before submitting an application to the Mississippi State Tax Commission.
5. *Expansion of Expensing for Capital Investments.* The Go Zone Act increased the expensing limitation by the lesser of \$100,000 or the cost of qualified Internal Revenue Service- GO Zone Property. This increases the limitation from \$100,000 to \$200,000 for qualified property. In addition, the Act increases the \$400,000 investment limitation by the lesser of the cost of qualified GO Zone property or \$600,000 placed in service during the tax year. These provisions apply to all property purchased after August 28, 2005, which is placed in service before December 31, 2007. Pursuant to Income Tax Regulation 54, Mississippi income tax law follows federal law regarding the amount allowable as a deduction for Section 179 property.
6. *Cleanup and Demolition Expensing.* Mississippi follows federal law regarding the income tax treatment for costs incurred for cleanup and demolition expenses. Mississippi taxpayers may expense 50% of their cleanup costs, which would otherwise be capitalized, if incurred or paid following August 27, 2005, until January 1, 2008. The cleanup expenses apply to demolition of property and cleanup of debris in the Katrina GO Zone, if held by the taxpayer for use for business, trade, or the production of income or property, as defined in Internal Revenue Code § 221(a)(1).
7. *Public Utility Casualty Losses.* Under federal law, public utilities located in the Katrina GO Zone may qualify to receive a ten year carryback on casualty losses. However, Mississippi net operating loss provisions do not follow federal law and provide a carryback of two years and a forward of twenty years.

III. JUDICIAL DEVELOPMENTS.

A. *Murphy Oil v. Commissioner.* On May 26, 2005, in a very troublesome opinion the Mississippi Supreme Court reversed the trial court's decision and reinstated a franchise tax assessment imposed by the Mississippi State Tax Commission against Murphy Oil Co. USA, Inc.¹ The court made its ruling based on a

¹*Mississippi State Tax Commission v. Murphy Oil USA, Inc.* (No. 2003-CA-00325-SCT).

procedural issue rather than the merits of the case. The Supreme Court reversed the decision of the trial court holding that it had improperly "reweighed the evidence" and did not "adhere to the correct standard of review." The Supreme Court stated that in reviewing the order of a state agency it and the trial court are limited by the arbitrary and capricious standard of review, which is a difficult burden of proof for any litigant to satisfy. It further noted that the Mississippi Constitution does not permit Mississippi courts to retry de novo matters on appeal from administrative agencies, though it did not cite any specific provision of the Mississippi Constitution as authority for this conclusion. As stated in the well-reasoned dissenting opinion in this case, the standard of review was not an issue that was briefed and argued by either party before the Supreme Court.

The ruling in *Murphy Oil* effectively nullified the new Mississippi statute governing judicial appeals of Mississippi State Tax Commission decisions, and severely threatened the due process rights of those subject to the rulings of the Commission.

B. Murphy Oil-On Rehearing. Murphy Oil filed a petition for rehearing with the Mississippi Supreme Court. The brief asserted, among other things, that if the court upheld its original opinion, then Murphy Oil and all similarly situated taxpayers were entitled to have their assessments remanded to the State Tax Commission for a full evidentiary hearing on the record. The Taxation Section of the Mississippi Bar, Council on State Taxation and Mississippi Manufacturing Association each filed separate "friend of the court" briefs in support of the petition for rehearing. The Tax Commission's brief, while maintaining that the Court's substantive holding is correct, also urged the Court to reconsider its holding on the nature of the judicial review in chancery court. The court granted the motion.

In its second opinion in this case, which was handed down on October 13, 2005, the Mississippi Supreme Court obviously realized that its first opinion was based on erroneous assumptions of fact. It withdrew the first opinion and substituted the second opinion in its place. The Mississippi Supreme Court based its ruling on the merits of the franchise tax issue and rejected the destination sales theory as a way to account for Mississippi receipts for purposes of the franchise tax apportionment formula. The second opinion devotes only one paragraph to the procedural issue that was the subject of the entire first opinion. Quoting from its 1969 decision in *Tenneco, Inc. v. Barr*², the court stated that "the Legislature has made it the public policy of this state to provide a full evidentiary judicial hearing in cases of the character now under consideration." The court concluded that the trial court properly "reviewed evidence and determined the cause" under *Tenneco* and applicable statutory authority.

While the court clarified the role of the trial court in tax cases, it did not address the standard of review issue. Since *Tenneco* did not require the trial court to use the arbitrary and capricious standard of review to overturn the decision of the Tax Commission, and since the applicable statutes require the trial court to "hear and determine the cause...as in other cases," it seems clear that the appropriate standard of review for the trial court in tax cases is a preponderance of the evidence.

In light of the revised opinion in *Murphy Oil* it is clear that the tax dispute resolution process allows taxpayers to continue to have a full evidentiary judicial hearing in tax cases. The two administrative hearings will continue for the foreseeable future to be informal hearings without a record.

² 224 So. 2d 208, 211 (Miss. 1969).

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