

PUBLICATION

Mississippi Court Rules Discriminatory Exclusion is Unconstitutional

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The Hinds County Chancery Court recently issued an opinion in *AT&T Corp. v. Miss. Dep't of Revenue* finding that Mississippi's dividend exclusion statute unlawfully discriminates against interstate commerce and is therefore unconstitutional under the Commerce Clause of the United States Constitution.

At issue in this case was the taxability of intercompany dividends received by AT&T from certain affiliates that had no business activities or income tax filing obligations in Mississippi. By its terms, Mississippi's statute providing for the exclusion of intercompany dividends from taxable income only applies when the distributing corporation is itself a Mississippi taxpayer. In its opinion, the court stated that the subject exclusion "clearly favors domestic corporations over foreign competitors and discourages corporations from choosing to locate their operations outside Mississippi," and ruled that the statute is discriminatory on its face.

The court determined that the Department of Revenue failed to meet its burden in establishing that the limited application of the subject exclusion is intended to serve as a "compensatory tax" designed to make interstate commerce bear a burden already borne by intrastate commerce, which would have allowed the statute to survive a constitutional challenge notwithstanding its discriminatory nature. The exclusion statute was therefore held unconstitutional.

In response to the court's finding that the exclusion is unconstitutionally discriminatory, the Department suggested that the court rescind the exclusion altogether, thereby eliminating the benefit for all Mississippi taxpayers. Fortunately, however, the court was not persuaded by the Department's proposed solution and instead struck the statute's discriminatory limitation and granted the tax benefit to AT&T for all of the tax years at issue.

Although this ruling is subject to appeal and further because Chancery Court decisions are not binding precedent, it potentially represents a significant victory for those Mississippi taxpayers who receive or have received intercompany dividends from affiliate-entities that do not have an income tax reporting obligation in Mississippi. Such taxpayers may wish to file protective refund claims now rather than wait for the outcome of a possible appeal and should be aware of the applicable time limitations for pursuing refunds.

If you have any questions concerning how the court's decision in *AT&T Corp.* could impact your ability to exclude intercompany dividends on future returns or possibly seek a refund for taxes paid in prior periods, please contact the author or any of the attorneys in the Firm's Tax Group.