



Mississippi Court Finds State Income Tax Dividend Exclusion Statute Unconstitutional

The Hinds County Chancery Court on March 20th invalidated the nexus-based restrictions contained within Mississippi's dividend exclusion statute, finding the provisions violated the Commerce Clause.

A copy of the Court's Order can be found [here](#).

The Mississippi Department of Revenue and the taxpayer, AT&T, had stipulated that the statute, Miss. Code Section 27-7-15(4)(i), exempts from a parent corporation's Mississippi gross income all dividends received from subsidiaries having a taxable presence in the state in the year of the distribution, but denies that exemption for dividends from subsidiaries having no Mississippi nexus or filing obligations.

AT&T challenged the constitutionality of the statute on the basis that it discriminated against interstate commerce by employing such geographic-based criteria, effectively using the tax code to reward corporations whose subsidiaries chose to establish business locations in the state and to effectively punish those that had not. The statute also was shown to subject the earnings of non-nexus subsidiaries to double taxation - once by the states in which they did business, and again by Mississippi at the parent level - not experienced by nexus subsidiaries.

The Court agreed that the statute was facially discriminatory and further noted that the State made no attempt to justify the restriction as a permissible compensatory tax scheme.

In its Order, the Court summarized the effect of the statute on multistate taxpayers as follows:

*Therefore, the statute **denies taxpayers a tax benefit**, the ability to deduct intercompany dividends from gross income in computing Mississippi income tax, based solely upon the choice of the taxpayer and its subsidiaries not to locate any operations in Mississippi or to file a Mississippi income tax return. ...*

*[T]his statutory scheme **disallows a valuable tax exemption based solely upon an interstate element**, that is whether the distributing corporation maintains property and/or employees in Mississippi or files*

*a Mississippi income tax return. As such, this **statute clearly favors domestic corporations over foreign competitors** and discourages corporations from choosing to locate their operations outside Mississippi. ...*

[T]his Court must find that the dividend exclusion statute is discriminatory in nature and on its face.

The Court also concluded the statute led to double taxation for certain companies, and held that the appropriate remedy under AT&T's circumstances was to strike the offensive limitation and thereby extend the benefits of the statute to dividends received from AT&T's non-nexus subsidiaries.

This decision is expected to affect a large number of corporate taxpayers in Mississippi, and questions remain as to how the decision might affect other taxpayers and future tax periods. The Department of Revenue will have thirty days from the date of the order to file a notice of appeal.

For further information, contact [John F. Fletcher](#) and [Matthew A. Mantle](#).

Remember that these legal principles may change and vary widely in their application to specific factual circumstances. You should consult with counsel about your individual circumstances. For further information regarding these issues,

John F. Fletcher

Partner, Jones Walker LLP

190 E Capitol St.

Jackson, MS 39201

601.949.4620 *tel*

601.949.4804 *fax*

jfletcher@joneswalker.com

Matthew A. Mantle

Partner, Jones Walker LLP

201 St. Charles Avenue

New Orleans, LA 70170-5100

504.582.8418 *tel*

504.589.8416 *fax*

mmantle@joneswalker.com

[Jones Walker State and Local Tax Practice Group](#)

www.joneswalker.com

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