



# SALT WATCH

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## Massachusetts Tax Update

On July 24, 2013, the Massachusetts House and Senate voted to override Governor Deval Patrick's veto of H. 3535,<sup>1</sup> an \$800 million transportation finance bill. The newly-enacted legislation contains a number of significant tax changes, which include market-based sourcing, a sales tax imposed on computer system design services, and the repeal of the utility corporation classification. The revenue raised by the bill is expected to prevent the need for immediate Massachusetts Bay Transportation Authority fare hikes to close the mass transit system's budget deficit, pay for the operation of regional bus services, fund Department of Transportation personnel costs, and finance some modest transportation projects. In addition, the Massachusetts Department of Revenue ("DOR") released TIR 13-10<sup>2</sup> on July 25, 2013, and a list of Frequently Asked Questions ("FAQs") on August 1, 2013,<sup>3</sup> that provide additional guidance regarding the newly-enacted sales and use tax on computer and software services.

### Income Tax

*Market-based Sourcing* – Effective January 1, 2014, sales, other than sales of tangible

<sup>1</sup> A copy of the bill may be viewed at [www.malegislature.gov/Bills/188/House/H3535](http://www.malegislature.gov/Bills/188/House/H3535).

<sup>2</sup> A copy of the technical information release may be viewed at [www.mass.gov/dor/businesses/help-and-resources/legal-library/tirs/tirs-by-years/2013-releases/tir-13-10.html](http://www.mass.gov/dor/businesses/help-and-resources/legal-library/tirs/tirs-by-years/2013-releases/tir-13-10.html).

<sup>3</sup> A copy of the FAQs may be viewed at [www.mass.gov/dor/docs/dor/law-changes/faqss-computer-software-2013.pdf](http://www.mass.gov/dor/docs/dor/law-changes/faqss-computer-software-2013.pdf).

personal property, shall be sourced to Massachusetts for income tax purposes if the corporation's market for the sale is in the state. Previously, Massachusetts required the sourcing of sales in the state based on cost-of-performance rules. Under the new legislation, the corporation's market for a sale is considered to be in a state in the following instances:

- A sale of a service to the extent that the service is "delivered" to a location in the state;
- A lease or license of intangible property if and to the extent the intangible property is used in the state; and
- The sale of intangible property, other than as provided above, where the property is a contract right, government license, or similar intangible property that authorizes the holder to conduct a business activity in a specific geographic area, if and to the extent that the intangible property is used in or otherwise associated with the state.

*Throw-out Rule* – in addition, sales, other than sales of tangible personal property, shall be excluded from the numerator and denominator of the sales factor if such sales are made to a state where the taxpayer is not taxable, or if the location of the sale cannot be determined or reasonably approximated.

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*Utility Corporations* – Effective January 1, 2014, the utility corporation classification is eliminated. Previously, corporations classified as utility corporations that were operating electric, gas, water, telephone, railroad, or similar businesses were taxed at the lower rate of 6.5% on their net income and were not subject to the net worth tax.

### Sales Tax

*Tax on Computer Services* – Effective July 31, 2013, computer design services are subject to sales and use tax. Computer design services are defined as the planning, consulting, or designing of computer systems that integrate computer hardware, software, or communication technologies and are provided by a vendor or a third party. In addition, sales tax will be imposed on the modification, integration, enhancement, installation, or configuration of standardized software. The DOR released TIR 13-10 on July 25, 2013, and a series of FAQs that provide the following additional guidance:

- Sales of computer services are sourced to Massachusetts if received at a Massachusetts vendor's location or if the service is performed or delivered to a customer's Massachusetts location. Sales of software services are generally sourced in the same manner as the sale of prewritten software.
- Taxable prewritten software and the associated installation charges are subject to tax.

- Technical support and training that do not involve the transfer of taxable prewritten software are not taxable. In addition, service technician charges for troubleshooting a customer's hardware or software or reinstallation of software are not taxable.
- Web site design services are taxable to the extent they involve the configuration or modification of open source code or prewritten software rather than custom software design.
- Web site hosting and data storage services (in the "cloud") are not taxable.

### Sales Tax

*Motor Fuel Tax* – The motor fuel tax rate for gasoline is increased from 21 cents per gallon to 24 cents per gallon as of July 31, 2013.

*Cigarette Tax* – The excise tax rate on cigarettes is increased from \$2.51 per package of 20 to \$3.51 per package of 20, effective July 31, 2013.

### Action Items

Although taxpayers will have a little more time to get ready for market-based sourcing (to become effective January 1, 2014), the same can't be said for the sales and use tax changes. The changes for sales and use tax on computer services became effective July 31, 2013. This change requires service



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providers to establish new remittance and collection procedures and to identify those items subject to tax that had not previously been subject to tax in Massachusetts. Informal discussions with the DOR indicate that additional FAQs will be issued. We anticipate that these new FAQs will provide additional detail on the nature of transactions that will be subject to tax.

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