HB 280

Proposed Language Change

Suggested by Telecommunications Industry

Distributed by the office of Co-Chair Foster

The Basic Point:

The purpose of both Cost of Performance (COP) and Market Sourcing is to decide where income should be assigned by identifying where the benefit of the service or product is earned or received.

For businesses that operate large communications networks, the value is the network itself—the system that allows people and systems in different places to connect instantly and continuously.

When someone accesses the internet, the service does not stop at that person's location. It necessarily involves multiple users and a wide range of infrastructure working together across many states. Because of that, the benefit of the service cannot realistically be tied to just one location.

Why Market Sourcing Misses the Reality

Market sourcing treats telecommunications like a product delivered to a single point. That does not reflect how these services actually work.

- A customer in Alaska is not buying a single data transmission; they are buying access to a nationwide network.
- That access depends entirely on the existence and operation of massive infrastructure—fiber lines, switches, data centers, and backup systems spread across the country.

Without that infrastructure, there is no service.

Example:

Imagine an Alaskan resident using ChatGPT to edit a document. The user uploads the file and receives an edited version. The servers doing that work are not located in Alaska; they are typically located in states like Virginia, Texas, or Arizona.

If the product was the edited document alone, the benefit might reasonably be viewed as received by the Alaskan user. In this situation, Market Sourcing would make economic sense.

Telecommunications, however, are fundamentally different.

Both the Alaskan user and ChatGPT's servers rely on AT&T's network to communicate. And much of the work that makes that communication possible—routing, security, and keeping the network running—happens in places unrelated to the user and the servers. In fact, there may be a lot of working being done in states where neither the Alaskan resident or the

ChatGPT server are located. Just as important, the work being done in unrelated locations is necessitated by the Alaskan resident's desire to have ChatGPT edit their document.

Why Sourcing Only to One End User Doesn't Work

Because so much of the work happens outside the users' state, sourcing all of the income to the Alaskan resident's location is incomplete. At a minimum, market sourcing ignores the other side of the interaction—the servers.

Treating this as a simple, one-location transaction does not match economic reality.

Why Cost of Performance Makes More Sense

The benefit of a communications network is shared. It supports users, servers, public services, and businesses across the country at the same time. The most reasonable way to reflect where value is created is to look at where the network is built, operated, and maintained.

For that reason, COP is a more accurate and fair way to source income from network-based services than tying everything to where a single user happens to be located when accessing the network.

Amendment to HB280 34-LS1349\A

On Page 9 – new language highlighted

17.**(a)** Sales, other than sales **described in Section 16** [OF TANGIBLE PERSONAL PROPERTY], are in this state if **the taxpayer's market for the sales is in this state. The taxpayer's market for sales is in this state:**

(1) in the case of sale, rental, lease, or license of real property, if and to the extent the property is located in this state;

(2) in the case of rental, lease, or license of tangible personal property, if and to the extent the property is located in this state;

(3) in the case of sale of a service, if and to the extent the service is delivered to a location in this state; and

(4) in the case of intangible property,

(i) that is rented, leased, or licensed, if and to the extent the property is used in this state, provided that intangible property utilized in marketing a good or service to a consumer is "used in this state" if that good or service is purchased by a consumer who is in this state; and

(ii) that is sold, if and to the extent the property is used in this state, provided that:

(A) a contract right, government license, or similar intangible property that authorizes the holder to conduct a business activity in a specific geographic area is "used in this state" if the geographic area includes all or part of this state;

(B) sales from intangible property sales that are contingent on the productivity, use, or disposition of the intangible property shall be treated as a sale of the rental, lease, or licensing of such intangible property under subsection (a)(4)(i); and

(C) all other sales of intangible property shall be

excluded from the numerator and denominator of the sales factor.

[: (a) THE INCOME-PRODUCING ACTIVITY IS PERFORMED IN

THIS STATE; OR]

(b) **If the state or states of assignment under subsection (a) cannot be determined, the state or states of assignment shall be reasonably approximated.**

(c) If the taxpayer is not taxable in a state to which a sale is assigned under subsection (a) or (b), or if the state of assignment cannot be determined under subsection (a) or reasonably approximated under subsection (b), such a sale shall be excluded from the denominator of the sales factor.

(d) The tax administrator may adopt regulations as necessary or appropriate to carry out the purposes of this section [THE INCOME-PRODUCING ACTIVITY IS PERFORMED BOTH IN AND OUTSIDE THIS STATE AND A GREATER PROPORTION OF THE INCOME-PRODUCING ACTIVITY IS PERFORMED IN THIS STATE THAN IN ANY OTHER STATE, BASED ON COSTS OF PERFORMANCE].

(e)notwithstanding (a) the sales of a telecommunications service provider or a mobile telecommunications service provider, other than sales described in Section 16, are in this state if:

(1) the income-producing activity is performed in this state; or,

(2) the income-producing activity is performed both in and outside this state and a greater proportion of the income-producing activity is performed in this state than in any other state, based on costs of performance.