

TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 17-13

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This ruling is based on the particular facts and circumstances presented, and is an interpretation of the law at a specific point in time. The law may have changed since this ruling was issued, possibly rendering it obsolete. The presentation of this ruling in a redacted form is provided solely for informational purposes, and is not intended as a statement of Departmental policy. Taxpayers should consult with a tax professional before relying on any aspect of this ruling.

SUBJECT

The application of the Tennessee franchise tax to a group of affiliated entities making a consolidated net worth election.

SCOPE

Revenue Rulings are statements regarding the substantive application of law and statements of procedure that affect the rights and duties of taxpayers and other members of the public. Revenue Rulings are advisory in nature and are not binding on the Department.

FACTS

[TAXPAYER] (the "Taxpayer") is a corporation that owns 100% of the stock of a [REDACTED COMPANY] that provides [REDACTED - PRODUCTS] to businesses in the [REDACTED] industries; this [REDACTED COMPANY] in turn owns 100% of the stock of several lower-tier [REDACTED] companies (collectively "[REDACTED COMPANY] Affiliates"). Taxpayer also owns 100% of an affiliate that provides consulting services to independent [REDACTED ENTITIES] in Tennessee. The consulting business is conducted through a single member limited liability company ("SMLLC") that owns [REDACTED NUMBER] other entities. Taxpayer plans to make an election to report its franchise tax on a consolidated basis with its affiliates pursuant to TENN. CODE ANN. § 67-4-2103(d). Included in this election will be the [REDACTED COMPANY] Affiliates, which, for the purposes of this ruling, are assumed to be exempt under TENN. CODE ANN. §§ 67-4-2008(a)(14), -2105(a); TENN. CODE ANN. § 56-4-217(b).

RULINGS

Should Taxpayer include its [REDACTED COMPANY] Affiliates in its affiliated group for purposes of the consolidated net worth election, even though the [REDACTED COMPANY] Affiliates are exempt from the Tennessee franchise tax? If so, how should the Taxpayer report the [REDACTED COMPANY] Affiliates' net worth when calculating consolidated net worth pursuant to TENN. CODE ANN. § 67-4-2103(d)?

Ruling: Although the [REDACTED COMPANY] Affiliates are exempt from Tennessee franchise tax, they are included in the Taxpayer's affiliated group for purposes of the consolidated net worth election. However, the [REDACTED COMPANY] Affiliates' assets and liabilities should be excluded

from the consolidated net worth calculation, and the [REDACTED COMPANY] Affiliates' factors should be excluded from both the numerator and denominator of affiliated group's apportionment formula because the [REDACTED COMPANY] Affiliates are exempt from the Tennessee franchise tax under TENN. CODE ANN. § 67-4-2105(a).

ANALYSIS

Tennessee imposes an excise tax at the rate of 6.5% on the net earnings of all persons, as defined under TENN. CODE ANN. § 67-4-2004(38) (Supp. 2016), doing business within Tennessee.¹ Tennessee also imposes a franchise tax at the rate of \$0.25 per \$100, or major fraction thereof, on the net worth of a person doing business in Tennessee, pursuant to TENN. CODE ANN. §§ 67-4-2105(a), -2106(a) (2013).² Persons subject to the Tennessee franchise and excise taxes include, but are not limited to, corporations, limited liability companies, and limited partnerships.³ With certain limited exceptions, each taxpayer is considered a "separate and single business entity" for Tennessee franchise and excise tax purposes and must file its Tennessee franchise and excise tax return on a separate entity basis.⁴

For tax years beginning on or after January 1, 2004, TENN. CODE ANN. § 67-4-2103(d) (2013) allows a taxpayer that is a member of an affiliated group to elect to compute its net worth for Tennessee franchise tax purposes on a consolidated basis. Each affiliated group member computing its net worth on a consolidated basis must file a separate Tennessee franchise and excise tax return.⁵

To compute net worth on a consolidated basis, all members of an affiliated group must file a group consolidated net worth registration form on or before the due date of the tax return for the period for which the election is to take effect.⁶ If a member enters or leaves the affiliated group at any time during the tax year, the affiliated group must file an amended group registration form on or before the due date of the return for the period in which the event takes place.⁷

Once made, the consolidated net worth election remains in effect for a minimum of five years.⁸ After the initial five years, the consolidated net worth election will continue unless the affiliated group

¹ TENN. CODE ANN. § 67-4-2007(a) (Supp. 2016).

² Note that, under TENN. CODE ANN. § 67-4-2108(a)(1) (2013), the franchise tax base "shall in no case be less than the actual value of the real or tangible property owned or used in Tennessee, excluding exempt inventory and exempt required capital investments." According to TENN. CODE ANN. § 67-4-2108(a)(3), for purposes of this section, "property" is to be "valued at cost less accumulated depreciation in accordance with generally accepted accounting principles."

³ TENN. CODE ANN. § 67-4-2004(38).

⁴ TENN. CODE ANN. §§ 67-4-2007(e)(1), -2106(c) (2013).

⁵ Consolidated net worth is reported on Schedule F2 of FAE 170.

⁶ TENN. CODE ANN. § 67-4-2103(g) (2013). The consolidated net worth registration form is available on the Department's website at <http://tn.gov/assets/entities/revenue/attachments/f1308301.pdf>.

⁷ *Id.*

⁸ TENN. CODE ANN. § 67-4-2103(h).

revokes its election by filing a group revocation election form.⁹ Following the consolidated net worth election, each member of the affiliated group that is subject to franchise and excise tax must file its own franchise and excise tax return. Each member must close its taxable year on the same date as all other members of the group.¹⁰

An “affiliated group” is defined as (1) “[a] taxpayer that, standing alone, is subject to the Tennessee franchise tax”; (2) “[a]ll other domestic persons in which the taxpayer, directly or indirectly, has more than 50% ownership interest”; (3) “[a]ll other domestic persons that, directly or indirectly, have more than 50% ownership interest in the taxpayer”; and (4) “[a]ll other domestic persons in which a person described in [(3), above,] directly or indirectly, have more than 50% ownership interest, regardless of whether such persons do business in Tennessee.”¹¹ For this purpose, a non-corporate taxable entity is more than 50% owned if upon liquidation more than 50% of the assets of the non-corporate taxable entity, directly or indirectly, accrue to a member or members of the affiliated group.¹²

The Taxpayer represents that Taxpayer, {REDACTED COMPANY} Affiliates, and SMLLC comprise an affiliated group under TENN. CODE ANN. § 67-4-2004(2), and therefore, the group plans to make a consolidated net worth election.

The Taxpayer states that the [REDACTED COMPANY] Affiliates are exempt from the franchise tax under TENN. CODE ANN. § 67-4-2105(a). Tennessee franchise tax law does not require such entities to either be included in the affiliated group or utilize the exemption. The two are not mutually exclusive. Accordingly, the [REDACTED COMPANY] Affiliates’ assets and liabilities should not be included when reporting the consolidated net worth on FAE 170 Schedule F2 because the [REDACTED COMPANY] Affiliates are exempt from the franchise tax under TENN. CODE ANN. § 67-4-2105(a). Moreover, the [REDACTED COMPANY] Affiliates’ factors should be excluded from both the numerator and the denominator of the combined group’s apportionment formula on FAE 170 Schedule NC pursuant to TENN. CODE ANN. § 67-4-2111.¹³

⁹ *Id.* TENN. CODE ANN. § 67-4-2103(i) authorizes the Commissioner of Revenue to accept a late election or a late revocation of an election, or to permit any early revocation of an election to compute net worth on a consolidated basis if the Commissioner determines there is reasonable and good cause for such action.

¹⁰ TENN. CODE ANN. § 67-4-2103(d).

¹¹ TENN. CODE ANN. § 67-4-2004(2)(A).

¹² TENN. CODE ANN. § 67-4-2004(2)(B).

¹³ Although the [REDACTED COMPANY] Affiliates should be listed on Schedule F2, it is not necessary to include their financial information. Listing the [REDACTED COMPANY] Affiliates on Schedule F2 allows the Taxpayer to provide the Department with a complete picture of the Taxpayer’s corporate structure. Listing the [REDACTED COMPANY] Affiliates does not affect the tax consequences of any entities subject to Tennessee franchise and excise tax.

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APPROVED: David Gerregano
Commissioner of Revenue

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