

TENNESSEE DEPARTMENT OF REVENUE  
REVENUE RULING # 17-14

**Revenue rulings are not binding on the Department. 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**

Application of the Tennessee franchise and excise tax exemption under TENN. CODE ANN. § 67-4-2008(a)(10) to single member limited liability companies.

**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**

A limited liability company taxed as a partnership for federal income tax purposes (the "Partnership") wholly owns multiple single member limited liability companies (the "SMLLCs") that are disregarded for federal income tax purposes. The Partnership also owns interests in various statutory trusts (the "Trusts") that are similarly disregarded and taxed as divisions of the Partnership for federal income tax purposes. The Partnership is subject to the Tennessee franchise and excise taxes and conducts its business activities both within and without the state of Tennessee.

The SMLLCs and the Trusts have represented that they do not conduct any of their business activities in Tennessee and do not believe that they have a substantial nexus with Tennessee such that they would be subject to Tennessee franchise and excise tax on a separate entity basis. The SMLLCs' and the Trusts' sole business activities are the asset-backed securitization of [REDACTED] loans.<sup>1</sup>

**RULING**

Do the SMLLCs qualify for the exemption under TENN. CODE ANN. § 67-4-2008(a)(10)(A) (Supp. 2016) because their activities are treated as a division of the Partnership for federal tax purposes?

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<sup>1</sup> The Department has not reviewed or otherwise evaluated whether the SMLLCs and the Trust have nexus with Tennessee. Similarly, it is assumed for purposes of this ruling that the SMLLCs and Trusts meet the requirements of TENN. CODE ANN. § 67-4-2008(a)(10)(B) for exemption from Tennessee's franchise and excise taxes. The taxpayer cannot rely upon this ruling to support any assertions relating to a lack of nexus with Tennessee or entitlement to any exemption. It is beyond the scope of this ruling to address the application of the exemption to the Trusts.

**Ruling:** Yes, the SMLLCs qualify for the exemption under TENN. CODE ANN. § 67-4-2008(a)(10)(A) because they are treated as a division of the Partnership for federal tax purposes.

### 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.<sup>2</sup> 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).<sup>3</sup> Persons subject to the Tennessee franchise and excise taxes include, but are not limited to, corporations, limited liability companies, and limited partnerships.<sup>4</sup> 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.<sup>5</sup>

TENN. CODE ANN. § 67-4-2008(a)(10) provides an exemption from the Tennessee franchise and excise taxes for the types of entities listed in TENN. CODE ANN. § 67-4-2008(a)(10)(A).<sup>6</sup> Qualifying entity types include those “classified as a partnership or trust in accordance with 26 U.S.C. § 7701, and the federal regulations and rulings promulgated under 26 U.S.C. § 7701.”<sup>7</sup>

Interpretations of federal tax law are generally not controlling for purposes of applying Tennessee tax law.<sup>8</sup> However, whether an entity qualifies under TENN. CODE ANN. § 67-4-2008(a)(10)(A) presents an exception to this rule because TENN. CODE ANN. § 67-4-2008(a)(10)(A) depends on the entity classification rules under 26 U.S.C. § 7701.

26 U.S.C. § 7701(a)(2) (West 2014) defines partnership as a “syndicate, group, pool, joint venture, or other unincorporated organization, through or by means which any business, financial operation, or venture is carried on, and which is not, within the meaning of this title, a trust or estate or a corporation.”

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<sup>2</sup> TENN. CODE ANN. § 67-4-2007(a) (Supp. 2016).

<sup>3</sup> 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.”

<sup>4</sup> TENN. CODE ANN. § 67-4-2004(38).

<sup>5</sup> TENN. CODE ANN. §§ 67-4-2007(e)(1), -2106(c) (2013).

<sup>6</sup> Entities that meet the entity type requirement in subsection (A) must also meet the “sole purpose” requirement in subsection (B). Analyzing subsection (B) is beyond the scope of this ruling because the SMLLCs are assumed to meet the sole purpose requirement.

<sup>7</sup> TENN. CODE ANN. § 67-4-2008(a)(10)(A)(i).

<sup>8</sup> The Tennessee Court of Appeals has stated that “rulings of the federal courts in regard to federal tax laws are not binding on Tennessee courts when they are called upon to interpret Tennessee tax laws.” *Little Six Corp. v. Johnson*, 1999 WL 336308 at 3 (Tenn. Ct. App. May 28, 1999); *See also Tidwell v. Berke*, 532 S.W.2d 254, 261 (Tenn. 1975) (finding that the revision of a federal tax law does not precipitate a revised interpretation of a corresponding but unaltered state tax law).

Treas. Reg. § 301.7701-2(a) (West 2016) defines “business entity” as “any entity recognized for federal tax purposes (including an entity with a single owner that may be disregarded as an entity separate from its owner under § 301.7701-3).” That section goes on to state that “a business entity with two or more members is classified for federal tax purposes as either a corporation or partnership. A business entity with only one owner is classified as a corporation or is disregarded; if the entity is disregarded, its activities are treated in the same manner as ... a division of the owner.” Business entities not classified as corporations under Treas. Reg. § 301.7701-2(b) are considered “eligible entities” and can make a classification election.<sup>9</sup> Eligible entities with a single member can choose to be classified as an association taxable as a corporation or disregarded as an entity separate from its owner.<sup>10</sup>

The SMLLCs qualify for the exemption from the Tennessee franchise and excise taxes in TENN. CODE ANN. § 67-4-2008(a)(10)(A) because they are disregarded as entities separate from their parent, which is a partnership, for federal tax purposes.

The SMLLCs have only one owner, the Partnership. Under Treas. Reg. § 301.7701-2(a), the SMLLCs are classified as entities disregarded as separate from their owner and their income, deductions, gains, losses, and credits are reported on the owner’s income tax return.<sup>11</sup> Being an entity that is disregarded as separate from its owner for federal tax purposes is not in and of itself a classification, but instead, a default whereby the entity’s federal tax treatment is the same as its owner’s classification. Because federal tax law disregards the separate entity status of the SMLLCs, and instead treats them as a division of their owner, a partnership, the SMLLCs qualify as partnerships for the purposes of TENN. CODE ANN. § 67-4-2008(a)(10)(A).

Accordingly, the SMLLCs meet the entity type requirement in TENN. CODE ANN. § 67-4-2008(a)(10)(A) and, therefore, qualify for the exemption from the Tennessee franchise and excise taxes under TENN. CODE ANN. § 67-4-2008(a)(10).

Brent C. Mayo  
Assistant General Counsel

APPROVED: David Gerregano  
Commissioner of Revenue

DATE: 9/20/17

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<sup>9</sup> Treas. Reg. § 301.7701-3(a)

<sup>10</sup> *Id.*

<sup>11</sup> See Internal Revenue Service Publication 3402, Taxation of Limited Liability Companies. <https://www.irs.gov/pub/irs-pdf/p3402.pdf> (Last visited August 30, 2017).