Contents

Chapter 3: Nexus

Overview

Nexus describes a connection that must be present before a taxing jurisdiction has the right to impose a tax on an entity's activity. An entity must have some contact or connection with a state before it may be taxed. At what point is that connection sufficient to trigger taxation in that state? Traditional nexus principles published in court cases, Revenue Rulings, and the Tennessee code help answer this question.

The Tennessee code states that "persons" or "taxpayers"[1] that are "doing business" *and* having a "substantial nexus in this state" are subject to the franchise tax[2] and excise tax.[3]

> ⚠ **Businesses formed and operating in Tennessee will always have nexus in this state. The question of nexus applies to out-of-state businesses with a limited connection to the state.**

1. Doing Business in Tennessee

Only entities "doing business in Tennessee"[4] may be taxed. Doing business in Tennessee is defined, in part, as "any activity purposefully engaged in within Tennessee, by a person with the object of gain, benefit, or advantage, consistent with the intent of the general assembly to subject such persons to the Tennessee franchise/excise tax to the extent permitted by the United States Constitution and the Constitution of Tennessee."

The law provides four exceptions for certain activities that otherwise would be considered doing business in Tennessee.[5] The exceptions involve:

- Product samples at a trade show;
- Activities of magazine publishers;
- Out-of-state person's equipment is in state on a temporary basis; or
- The temporary presence of employees in Tennessee.

More specifically, the following activities do not create nexus:

- The presence of employees and/or product samples and/or other promotional materials at one or more trade shows, exhibits, conventions, or similar events in Tennessee for a total of not more than twenty days per calendar year; provided, that the activities of the entity's employees while in the state are limited to:

  - Maintaining or facilitating the trade show or convention;

  - Purchasing of goods on behalf of their employer;

  - Soliciting sales; and

  - Gathering samples, promotional material or other information offered at the event.

- Activities by publishers of magazines and books who contract with Tennessee printers for the printing of their magazines or books, when such activities in the state are limited solely to activities having to do with:

  - The printing, storage, labeling, and/or delivery to the United States mail or common carrier of such magazines or books;

  - The maintenance of raw materials with respect to such activities;

  - The maintenance of employees solely in connection with the production and quality control of such printing, storage, labeling and/or delivery; provided, that the publisher and printer are not affiliated with one another.

    - Persons are affiliated with one another, if, either directly or indirectly, one controls the other, or if the persons are directly or indirectly controlled by a common parent.

- Physical presence in this state of an out-of-state person's equipment, tooling, inventory, and employees on a temporary basis, when:

  - The activity in which such items and employees are engaged is not the pursuit, creation or maintenance, by the out-of-state person or any person that is affiliated with it, of a market in this state;

- The equipment and tooling are not used, worked on, or held in this state by a person that is affiliated with the out-of-state person;
- The out-of-state person's employees have no control over the use or work done in this state by the in-state person; and
- The extent and value of such items, the number of such employees, and the number of days the employees work in this state, in light of all the facts and circumstances, are qualitatively and quantitatively de minimis. Persons are affiliated with one another, if, either directly or indirectly, one controls the other, or if the persons are directly or indirectly controlled by a common parent.

- The temporary presence of employees solely for the purpose of purchasing goods from vendors in this state for use in the employer's business out-of-state, provided that:
  - The total number of days the employer has one or more employees present in this state does not exceed thirty per calendar year; and
  - The employer does not furnish, directly or indirectly, any office in this state for their use.

2. Substantial Nexus

In addition to "doing business," an entity must have substantial nexus in the state to be subject to tax. The term "substantial nexus in this state" was enacted in 2015 by the Revenue Modernization Act of 2015 ("RMA") and applies to all tax years beginning on or after January 1, 2016. It means any direct or indirect connection of the taxpayer to this state such that the taxpayer can be required under the U.S. Constitution to remit franchise and excise tax. [6] Such connection includes, but is not limited to:

- The taxpayer is organized or commercially domiciled in this state;
- The taxpayer owns or uses its capital in this state;
- The taxpayer has systematic and continuous business activity in this state that has produced gross receipts attributable to customers in this state;

- The taxpayer licenses intangible property for use by another party in this state and derives income from that use of intangible property in this state; or

- The taxpayer has "bright-line presence" in this state. A person has bright-line presence in this state for a tax period if any of the following applies:

  - The taxpayer's total receipts in this state during the tax period, as determined under the apportionment formula,[7] exceed the lesser of $500,000 or 25% of the taxpayer's total receipts everywhere during the tax period;

  - The average value of the taxpayer's real and tangible personal property owned or rented and used in this state during the tax period, as determined under the apportionment formula,[8] exceeds the lesser of $50,000 or 25% of the average value of all the taxpayer's total real and tangible personal property; or

  - The total amount paid in this state during the tax period by the taxpayer for compensation, as determined under the apportionment formula,[9] exceeds the lesser of $50,000 or 25% of the total compensation paid by the taxpayer.

Revenue Modernization Act Expands Nexus

The RMA's addition of "substantial nexus in this state" expands the number of businesses that might have nexus under the Due Process Clause and/or Commerce Clause. Persons that would have been subject to the franchise and excise tax before the enactment of the RMA and the substantial nexus definition will continue to be subject to the tax even if they do not meet any of the bright-line tests. However, under the substantial nexus definition, out-of-state businesses that previously were not subject to the franchise and excise tax may now be subject to the tax. For example:

- Prior to the law change, an out-of-state company whose only connection with Tennessee was sales made into the state from outside the state would not be subject to the franchise and excise tax. However, for tax years beginning on or after January 1, 2016, this taxpayer would be subject to the tax if its sales into the state exceed the lesser of $500,000 or 25% of the taxpayer's total receipts, or if any other contact with the state is sufficient to create substantial nexus. Note that physical presence is not required.

If a taxpayer does not meet the bright-line presence test in Tennessee, it may have substantial nexus if its contact with the state is sufficient. For instance:

- A company incorporated in Tennessee (a domestic entity) is always subject to the tax. If there is no property, payroll, or sales within the state, a franchise and excise tax return and minimum franchise tax payment of $100 is required.

- An out-of-state entity doing business in the state may have nexus if it is engaged in systematic and continuous business activity that has produced receipts attributable to Tennessee customers that are short of the bright-line threshold. The frequency and nature of the activity in the state should be evaluated to determine if the connection with the state is sufficient to create nexus. However, a taxpayer with only economic presence (customers) in Tennessee does not automatically have substantial nexus solely on the basis that it has systematic and continuous activity in the state that produces some amount of income that is less than the bright-line threshold.

- An out-of-state business that contracts with full-time agents to conduct business in the state for less than $50,000 a year would create nexus under traditional nexus principles, as published in court cases, even though the bright-line test was not met.

Physical presence in the state will often create nexus, but a small physical presence will not always create nexus.

Furthermore, inventory located at a warehouse in the state will not always create nexus unless the bright-line threshold is met. However, it might in some cases. If the "doing business" requirement is met and the inventory is substantial in amount, but is short of the bright-line threshold, this might create nexus.

Entity Specific Nexus

1. Trucking Companies

A trucking company is subject to franchise and excise tax if it provides intrastate transportation services within Tennessee, makes deliveries of goods into Tennessee that originate in another state, or transports goods from Tennessee for delivery into another state. However, a motor carrier traveling through Tennessee that originates and terminates outside Tennessee, where the vehicle makes no pickups or deliveries and conducts no other business activity in Tennessee,

does not constitute doing business in Tennessee and therefore does not establish nexus.[10] For example:

- A motor carrier is not doing business in Tennessee and is not subject to franchise and excise tax if its only connection with the state is that it operates trucks traveling from Indiana through Kentucky and Tennessee to a destination in Alabama. The trucks do not have any pickups or deliveries in Tennessee. Truck drivers stopping in Tennessee to refuel or purchase a meal does not otherwise constitute doing business in Tennessee.

2. Foreign Corporations

A company that is treated as a foreign corporation under the Internal Revenue Code ("IRC") and has no effectively connected income ("ECI") with a United States trade or business will not be considered to have a substantial nexus in Tennessee. If a company is treated as a foreign corporation under the IRC but has income effectively connected with a United States trade or business, then its net earnings and net worth connected with its United States trade or business will be its net earnings and net worth for franchise and excise tax purposes. Furthermore, only property used in, payroll attributable to, and receipts effectively connected with its company's United States trade or business will be considered when calculating its apportionment factors.

Whether a company has income effectively connected with a United States trade or business and the amount of its net earnings and net worth connected with its United States trade or business will be determined in accordance with the provisions of the IRC. Guidance from the IRS[11] states generally, when a foreign person engages in a trade or business in the United States, all income from sources within the United States connected with the conduct of that trade or business is ECI. This applies whether there is any connection between the income and the trade or business being carried on in the United States during the tax year. Generally, an entity must be engaged in a trade or business during the tax year to be able to treat income received in that year as ECI. Entities are usually considered to be engaged in a U.S. trade or business when they perform personal services in the United States. Whether they are engaged in a trade or business in the United States depends on the nature of their activities. Deductions are allowed against ECI, and it is taxed at the graduated rates or lesser rate under a tax treaty. Consider the following when deciding whether an entity is engaged in a trade or business in the United States. Certain kinds of fixed, determinable, annual, or periodical income are treated as ECI because:

- Certain IRC sections require the income to be treated as ECI;
- Certain IRC sections allow elections to treat the income as ECI;

- Certain kinds of investment income are treated as ECI if they pass either of the two following tests:
  - The Asset-Use Test – The income must be associated with U.S. assets used in, or held for use in, the conduct of a U.S. trade or business.
  - Business Activities Test – The activities of that trade or business conducted in the United States are a material factor in the realization of the income.
- If the entity's only U.S. business activity is trading in stocks, securities, or commodities (including hedging transactions) through a U.S. resident broker or other agent, it is not engaged in a trade or business in the United States.

Party to a Treaty

A taxpayer treated as a foreign corporation under the IRC, who would have income effectively connected with a United States trade or business under the IRC, does not have substantial nexus with Tennessee for purposes of the franchise and excise tax if the United States is a party to a treaty under which the taxpayer has no effectively connected income. If a company is treated as a foreign corporation under the IRC and has no income effectively connected to a United States trade or business, it does not have substantial nexus with Tennessee.[12] IRC §894 provides that the provisions of the IRC shall be applied to any taxpayer with "due regard" for the treaty obligations of the United States that apply to the taxpayer.

3. Financial Institutions

Financial institutions doing business and having substantial nexus in Tennessee file a combined franchise and excise return with unitary businesses[13] on Form FAE174.

Financial Institution Defined

A financial institution[14] is a:

- Holding company;[15]
- Regulated financial corporation;[16]
- Subsidiary of a bank holding company or a regulated financial corporation;

- Investment entity[17] that is indirectly owned (more than 50%) by a bank holding company or a regulated financial corporation; or

- Any other person that is carrying on the "business of a financial institution."[18]

    - If more than 50% of an entity's gross receipts are from carrying on the "business of a financial institution," franchise and excise tax Form FAE174 should be completed instead of Form FAE170. For example, Car Wash, Inc. has $151,000 in gross receipts. The washing service generated gross receipts of $75,000 and the remainder of the receipts is interest income from a note receivable. Car Wash, Inc. is a financial institution because the $76,000 in interest income constitutes over 50% of the entity's gross receipts.

⚠ **Credit unions, insurance companies, and certain trusts are exempt from franchise and excise tax. Tenn. Code Ann. § 67-4-2008(4), (10), (14).**

Doing Business

As stated previously, an entity must be doing business in the state in order to be subject to franchise and excise tax.

In addition to the standard definition of "doing business," a financial institution is presumed to be doing business in this state if the total of its assets and the absolute value of its deposits attributable to sources within this state, regardless of whether the deposits are accepted or maintained at locations in this state, is $5,000,000 or more.[19] Tangible assets are attributable to Tennessee if they are located in the state. Intangible assets are attributable to Tennessee if the income earned on those assets is attributable to this state. Deposits are attributed to Tennessee if they are made by this state or any of its agencies, instrumentalities, or subdivisions; or by any resident of this state, regardless of whether the deposits are accepted or maintained at locations in this state.

A financial institution may also be deemed to be doing business in this state if it:

- Maintains an office in this state;

- Has an employee, representative or independent contractor conducting business in this state;
- Regularly sells products or services to customers that receive the product or service in this state;
- Regularly solicits business from potential customers in this state;
- Regularly performs services outside this state that are consumed in this state;
- Regularly engages in transactions with customers in this state that involve intangible property, including loans, and result in receipts flowing to the taxpayer from within this state;
- Owns or leases property located in this state; or
- Regularly solicits and receives deposits from customers in this state.

Due Process and Commerce Clause

The state applies the franchise and excise tax to the extent permitted by the United States Constitution and the Constitution of Tennessee. According to the Commerce Clause and Due Process Clause of the United States Constitution, the flow of interstate commerce cannot be impeded and there must be a minimal connection between the company's interstate activities and the taxing state. These constitutional restrictions are considered before Tennessee can assert nexus to tax an out-of-state entity.

According to the U.S. Supreme Court, there must be a "minimal connection" between a company's interstate activities and the taxing state for the Due Process Clause to be satisfied. A company must have "substantial nexus" in that state for the Commerce Clause to be satisfied. Specifically, the Supreme Court in *Complete Auto Transit, Inc. v. Brady*[20] listed four requirements that must be met to satisfy the Commerce Clause:

- The tax is applied to an activity with a substantial nexus with the taxing state;
- The tax is fairly apportioned;
- The tax does not discriminate against interstate commerce; and

- The tax is fairly related to the services provided by the state.

To determine if an entity is taxable under the U.S. Constitution, one must know the meaning of the terms "minimal" (minimal contacts) and "substantial" (substantial nexus). Some courts have interpreted these terms to mean physical presence in the state is required. However, the Supreme Court in *South Dakota v. Wayfair, Inc.*[21] has ruled that physical presence is not necessary to create substantial nexus. Substantial nexus requires substantial activities in the taxing state (e.g., the entity has customers in the taxing state). This interpretation is commonly referred to as "economic nexus."

Nexus-Related Issues

1. Ownership Interests Do Not Create Nexus

For federal income tax purposes (and in most other states), some entities are taxed directly, such as corporations, and others are taxed indirectly to their owners, such as S corporations, limited liability companies, and partnerships. Tennessee franchise and excise tax applies directly to all taxpayers. In other words, pass-through entities are taxed at the entity level and not at the owner level.

Each taxable entity stands on its own attributes as to whether it is doing business and has substantial nexus in the state. An ownership interest in a pass-through entity (e.g., an LP, LLC, or S corp.) that operates in Tennessee does not create a franchise and excise tax filing requirement for the owner. The taxpayer subject to the franchise and excise tax is always the entity that conducts business in the state. However, there are two exceptions to this rule, as described below.

SMLLC Owned by a Corporation

An SMLLC owned by an entity taxed as a corporation is disregarded for franchise and excise purposes. If either entity has nexus with the state, the activities of *both* the corporation *and* the SMLLC are included in one franchise and excise tax return filed under the corporation. Although the corporate owner may not otherwise have a connection with the state, the activities of the SMLLC operating in the state will subject the corporate owner to franchise and excise tax.

- For example, a New York corporation that has no connection with Tennessee becomes the sole owner of an LLC in Nashville, TN. The SMLLC is disregarded to the corporation

for federal income tax purposes. The New York corporation will file one franchise and excise tax return that includes the activities of both the corporation and the SMLLC.

General Partnership with a Limited Liability Owner

The second exception is when an entity that offers its owner(s) limited liability protection, and that otherwise has no connection with the state, owns an interest in a general partnership ("GP") that is doing business and has substantial nexus in the state. The GP is not a type of entity that is subject to franchise and excise tax, but its Tennessee activity is taxed at the first ownership level that offers limited liability protection. For example:

- A limited liability company that otherwise has no connection with the state has an ownership interest in a GP that is doing business in the state. The limited liability company will be subject to franchise and excise tax and must file a return and compute its tax liability based on its percentage ownership share of the GP's net worth/property and income attributes.

2. Standard for Nexus and Right to Apportion

Another nexus-related issue is whether a taxpayer's activities in another state are sufficient to permit the taxpayer to apportion its net worth and net earnings subject to Tennessee franchise and excise tax. For example, if a taxpayer's only connection with another state is an insignificant sale made into that state, the taxpayer does not have the right to apportion.

Tennessee statutes provide the test for determining when a taxpayer has the right to apportion.[22]

- A taxpayer with business activities that are taxable both inside and outside the state must apportion its net worth and net earnings.

- A taxpayer is considered taxable in another state only if the taxpayer is conducting activities in that state that, if conducted in Tennessee, would constitute doing business in Tennessee and subject the taxpayer to either Tennessee's franchise tax **or** excise tax.

Therefore, the same "doing business" standard for nexus also applies to the right to apportion.

Taxpayers that are subject only to a franchise tax or similar tax in another state would still have the right to apportion their net earnings for the excise tax base, even when the taxpayer is protected from paying an excise tax or similar tax in that other state.

Taxpayers entitled to apportion must compute apportionment ratios and apply such ratios in the manner set forth by statute so that franchise and excise tax is levied only on the portion of the taxpayer's net worth and net earnings generated by Tennessee operations.[23] Please see Chapter 14 for more information on apportionment.

Example of Nexus and Right to Apportion

Corporation X is based in Tennessee but has five salespeople making $30,000 each based in another state along with tangible personal property, such as a car, computer, inventory samples, and advertising materials. The salespeople work out of their homes. All their activity in the other state comes within the exemption limits for sales solicitation under Public Law 86-272 (discussed in the next section). Corporation X will be allowed to apportion since the connections in the other state would have required that a Tennessee franchise tax return be filed if they had occurred in Tennessee.

⚠ **Being subject to taxation in another state under that state's law is not the criteria for determining if an entity may apportion.**

Public Law 86-272

1. Overview

Public Law 86-272 ("P.L. 86-272")[24] is federal statutory law that preempts state law. The application of P.L. 86-272 should be considered after nexus has been determined. This law prohibits any state from imposing an *income tax* on out-of-state taxpayers whose only connection with the state is the *solicitation*[25] of orders for sales of *tangible personal property* when such orders are approved and shipped from outside the state. P.L. 86-272 states:

- No State, or political subdivision thereof, will have power to impose a *net income tax* on the income derived within such State by any person from interstate commerce if the only business activities within such State by or on behalf of such person during such taxable year are either, or both, of the following:

  - The solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and

- The solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person enable such customer to fill orders resulting from such solicitation are orders described in paragraph above.

- The above provisions do not apply with respect to any corporation which is incorporated under the laws of that State; a domestic corporation.

    - P.L. 86-272 prohibits a state from taxing the income of a corporation formed under the laws of another jurisdiction whose only business activities within the state consist of "solicitation of orders" for tangible goods, provided that the orders are sent outside the state for approval and the goods are delivered from out of state.

Limited liability entities that are subject to excise tax in this state but meet the requirements of P.L. 86-272 are exempt from the excise tax. They should check the box "Public Law 86-272 applied to excise tax" on page one of the franchise and excise tax return and complete only the franchise tax portion of the return. This law does not apply to the franchise tax because the franchise tax is not based on income. [26]

The limitation on taxation afforded by P.L. 86-272 may be lost if a taxpayer performs activities outside those protected by the law. If in-state activities go beyond the mere solicitation of orders for sales of tangible personal property, the protection of P.L. 86-272 is lost and the excise tax return must be completed for all activities for the entire tax year. Actions that will preempt a taxpayer from claiming exemption under P.L. 86-272 are called unprotected activities.

Solicitation is specifically defined and means:

- Speech or conduct that explicitly or implicitly invites an order; and

- Activities that neither explicitly nor implicitly invite an order but are entirely *ancillary* to requests for an order.

    - *Ancillary activities* are those activities that serve no independent business function for the seller apart from their connection to the solicitation of orders. Activities that a seller would engage in apart from soliciting orders are not considered ancillary to the solicitation of orders. The mere assignment of activities to sales personnel does not, merely by such assignment, make such activities ancillary to solicitation of orders. Additionally, activities that seek to promote sales are not ancillary because P.L. 86-272 does not protect activity that

facilitates sales; it only protects ancillary activities that facilitate the request for an order.

- Conducting activities that do not fall within this definition of solicitation will cause the company to lose its protection from a net income tax afforded by P.L. 86-272, unless the disqualifying activities, taken together, are *de minimis*.

2. Unprotected vs. Protected Activities

The Multistate Tax Commission ("MTC") has published the *Statement of Information Concerning Practices of Multistate Tax Commission and Signatory States Under Public Law 86-272*,[27] which provides a national standard for what constitutes solicitation. This document lists activities that do and do not go beyond mere solicitation. Protected activities are often referred to as immune activities because they may be performed without losing P.L. 86-272 protection. The performance of any unprotected (or non-immune) activities will cause the taxpayer to lose its P.L. 86-272 protection. The lists of unprotected and protected activities are as follows:

Unprotected/Non-Immune Activities

The following in-state activities will cause otherwise protected sales to lose their protection:

- Making repairs or providing maintenance or service to the property sold;
- Collecting current or delinquent accounts, whether directly or by third parties;
- Investigating credit worthiness;
- Installation or supervision of installation at or after shipment or delivery;
- Conducting training courses, seminars or lectures, other than for sales personnel;
- Providing any kind of technical assistance or service (including engineering assistance or design service), other than for solicitation;
- Handling customer complaints;
- Approving or accepting orders;

- Repossessing property;
- Securing deposits on sales;
- Picking up or replacing damaged or returned property;
- Hiring, training, or supervising personnel, other than sales personnel;
- Using agency stock checks or other methods to facilitate sales;
- Maintaining a sample or display room in excess of 14 days at any one location within the state during the tax year;
- Carrying samples for sale, exchange or distribution in any manner for consideration or other value;
- Owning, leasing, using or maintaining any of the following facilities or property in-state:
    - Repair shop
    - Parts department
    - Office (other than an in-home office)
    - Warehouse
    - Meeting place for directors, officers, or employees
    - Stock of goods (other than samples for sales personnel)
    - Telephone answering service
    - Mobile stores (e.g., trucks with driver salesmen)
    - Real property or fixtures to real property of any kind
- Consigning stock of goods or other tangible personal property to any person, including an independent contractor, for sale;
- Maintaining, by either an in-state or an out-of-state resident employee, an office or place of business (other than an in-home office), unless the office is not publicly attributed to the company and used solely for sales solicitation;
- Entering into, selling or otherwise disposing of franchising or licensing agreements; and

- Conducting any activity which is not entirely ancillary to requests for orders.

Protected/Immune Activities

The following in-state activities will not cause the loss of protection for otherwise protected sales:

- Soliciting orders for sales by any type of advertising (e.g., notice in a newspaper that a salesman will be in town at a certain time);
- Soliciting orders from an in-home office;
- Carrying samples and promotional materials only for display or distribution without charge or other consideration;
- Furnishing and setting up display racks and advising customers on the display of the company's products without charge or other consideration;
- Providing automobiles to sales personnel for their use in conducting protected activities;
- Passing orders, inquiries and complaints on to the home office;
- Missionary sales activities (e.g., solicitation of indirect customers for the company's goods through other entities, such as wholesalers);
- Coordinating shipment or delivery without payment or other consideration;
- Checking of customers' inventories for reorder (this does not include checking inventory for other purposes, such as quality control and on-site restocking);
- Maintaining a sample or display room for 14 days or less at any one location within the state during the tax year;
- Recruiting, training or evaluating sales personnel;
- Mediating direct customer complaints to foster customer relations and facilitate

requests for orders; and

- Owning, leasing, using or maintaining personal property in an in-home office or automobile that is solely limited to conducting protected activities (e.g., a salesman's use of a cell phone, fax machine, copier, laptop computer, etc. for solicitation)

De Minimis Exception

Tax immunity is not lost if an unprotected activity establishes only a trivial (or *de minimis*) connection with the state. *De minimis* is a legal term that means "trifling" or "minimal."[28] If a non-immune activity is *de minimis* in volume and/or amount (i.e., it does not have some degree of regularity), the protection afforded by P.L. 86-272 will not be lost. The taxpayer will not be subject to the excise tax.

Independent Contractors

P.L. 86-272 provides protection to certain in-state activities if conducted by an independent contractor that would not be afforded if performed by a taxpayer or its employees or other representatives. Independent contractors may engage in the following limited activities in the state without affecting the taxpayer's immunity:

- Soliciting sales
- Making sales
- Maintaining an office

However, sales representatives who represent a single principal are not considered to be independent contractors and are subject to the same limitations as those provided under P.L. 86-272 and the MTC's *Statement of Information*.

Also, maintenance of a stock of goods in the state by an independent contractor under consignment or any other type of arrangement with the company, except for purposes of display and solicitation, will remove the protection afforded by P.L. 86-272.

P.L. 86-272 Examples

- A regional manager's activities in state include recruitment, training, and evaluation of sales employees. The company uses in-state hotels and homes for sales-related meetings. Salesmen are provided a car and a stock of free samples for the purpose

of soliciting orders. The company was careful to not have the salesmen engage in activities that the company would normally engage in, such as repairing or servicing the products sold. In this case, the company is protected under P.L. 86-272 and is not subject to excise tax, but it would report the car and other equipment used in Tennessee on its franchise tax return.

- A corporation has 25 employees in the state who primarily solicit orders for sales of tangible personal property, which are approved and fulfilled from a location outside of the state. The company is *doing business* in the state; it is purposefully engaged in the state with the object of gain, benefit or advantage. In addition, the salaries of the employees in the state exceed the *substantial nexus* bright-line threshold of $50,000. The corporation must file a franchise and excise tax return. The corporation has determined that it is eligible to claim exemption from excise tax under P.L. 86-272, so the corporation checked the applicable box on the first page of the return. Upon examination, however, it was determined that the corporation's in-state activities went beyond those protected under P.L. 86-272; the corporation's employees did research and development activities that were not *de minimis* in nature. The corporation is subject to both the franchise and excise taxes.

[1] Tenn. Code Ann. § 67-4-2004(38).
[2] Tenn. Code Ann. § 67-4-2105(a).
[3] Tenn. Code Ann. § 67-4-2007(a).
[4] Tenn. Code Ann. § 67-4-2004(14).
[5] Tenn. Code Ann. § 67-4-2004(14)(E)(i)-(iv).
[6] Tenn. Code Ann. § 67-4-2004(49).
[7] Tenn. Code Ann. § 67-4-2012.
[8] Tenn. Code Ann. § 67-4-2012.
[9] Tenn. Code Ann. § 67-4-2012.
[10] Revenue Ruling 17-08.
[11] https://www.irs.gov/individuals/international-taxpayers/effectively-connected-income-eci.
[12] Tenn. Code Ann. § 67-4-2004(49)(B).
[13] Tenn. Code Ann. § 67-4-2004(52).
[14] Tenn. Code Ann. § 67-4-2004(17).
[15] Tenn. Code Ann. § 67-4-2004(21).
[16] Tenn. Code Ann. § 67-4-2004(45).
[17] Tenn. Code Ann. § 67-4-2004(30).
[18] Tenn. Code Ann. § 67-4-2004(5).
[19] Tenn. Code Ann. § 67-4-2004(14)(B).
[20] *Complete Auto Transit, Inc. v Brady*, 430 U.S. 274 (1977).
[21] *South Dakota v. Wayfair, Inc.*, 585 U.S. ___ (2018).
[22] Tenn. Code Ann. §§ 67-4-2010, 67-4-2110.
[23] Tenn. Code Ann. §§ 67-4-2012, 67-4-2110.
[24] 15 USC § 381, enacted in 1959.
[25] *Wisconsin v. William Wrigley, Jr. Co*, 505 U.S. 214 (1992) provides an interpretation of the phrase "solicitation of orders." Also, solicitation is defined as "[t]he act or an instance of requesting or seeking to obtain something; a request or petition." Black's Law Dictionary (7th ed. 2000).
[26] Attorney General Opinion # 04-159.
[27] http://www.mtc.gov/uploadedFiles/Multistate_Tax_Commission/Uniformity/Uniformity_Projects/A_-_Z/StatementofInfoPublicLaw86-272.pdf.
[28] Black's Law Dictionary (8th ed. 2004).