

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING 07-27**

WARNING

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This presentation of the ruling in a redacted form is informational only. Rulings are made in response to particular facts presented and are not intended necessarily as statements of Department policy.

SUBJECT

Whether gross receipts from certain temporary labor services are subject to the business tax.

SCOPE

This letter ruling is an interpretation and application of the tax law as it relates to a specific set of existing facts furnished to the department by the taxpayer. The rulings herein are binding upon the Department and are applicable only to the individual taxpayer being addressed.

This letter ruling may be revoked or modified by the Commissioner at any time.

Such revocation or modification shall be effective retroactively unless the following conditions are met, in which case the revocation shall be prospective only:

- (A) The taxpayer must not have misstated or omitted material facts involved in the transaction;
- (B) Facts that develop later must not be materially different from the facts upon which the ruling was based;
- (G) The applicable law must not have been changed or amended;
- (D) The ruling must have been issued originally with respect to a prospective or proposed transaction; and
- (E) The taxpayer directly involved must have acted in good faith in relying upon the ruling; and a retroactive revocation of the ruling must inure to the taxpayer's detriment.

FACTS

[TAXPAYER] provides medical professional staffing for hospitals, clinics, and home care agencies. Each employee is a board certified, licensed individual who falls into one of the following categories:

- Registered Nurse
- Licensed Practical Nurse
- Certified Nursing Assistant
- Respiratory Therapist
- Physical Therapist
- Occupational Therapist
- Speech Language Pathologist

One hundred percent (100%) of company revenue is derived from billing for healthcare services provided by the Taxpayer's employees to individual patients, and each employee's medical services are tracked. All revenue is derived from specific healthcare services rendered within client facilities (hospitals, clinics and home care agencies). Each client is a healthcare provider and is not subject to the business tax pursuant to Tenn. Code Ann. § 67-4-708(3)(C)(i). All of the taxpayer's employees provide services identical to those provided by the employees of the client and must meet the same credentialing and screening requirements mandated by State and Federal regulations.

QUESTIONS

Is the Taxpayer exempt from payment of Tennessee business tax on gross receipts derived from providing services that qualify as an exempt activity pursuant to Tenn. Code Ann. §§ 67-4-708(3)(C)(i)-(xv)?

RULING

Yes, if the fee received by the Taxpayer for temporary labor services can be segregated and identified as having been generated solely by the performance of a service that is exempt from the Tennessee business tax, then the fee will be exempt from the tax.

ANALYSIS

The Business Tax Act, found in Tenn. Code Ann. §§ 67-4-701 et seq., is a component of Tennessee's scheme of privilege and excise taxes. Tenn. Code Ann. § 67-4-704(a) allows counties and incorporated municipalities to tax the privilege of making of sales by engaging in any business activity enumerated in § 67-4-708.

Under Tenn. Code Ann. § 67-4-708, there are five classes of business activities. A taxpayer's dominant business activity is used to determine under which of the five classifications a taxpayer belongs for the purposes of determining the appropriate tax rate to be applied to the taxpayer's gross receipts and the due date of the return. *See Hermitage Memorial Gardens Mausoleum and Memorial Chapel, Inc. v. Dunn et al.*, 541 S.W.2d 147 at 149 (Tenn. 1976). *See also* Tenn. Comp. R. & Regs. 1320-4-5-.15. "Dominant business activity" is defined as "the business activity which is the major and

principal source of gross sales at retail and the major and principal source of gross sales at wholesale of the business.” Tenn. Code Ann. § 67-4-702(4).

Under classification 3, Tenn. Code Ann. § 67-4-708(3)(C) applies the business tax to the “making of sales of services or engaging in the business of furnishing or rendering services.” “Services” are defined in pertinent part to mean and include “every activity, function or work engaged in by a person for profit or monetary gain except as otherwise provided in this part.” Tenn. Code Ann. § 67-4-702(19). Regulations add to this definition by stating that “services” include all activity, functions or work engaged in by one person for another person for a consideration but do not include sales of tangible personal property. Tenn. Comp. R. & Regs. 1320-4-5-.48(1)

The Taxpayer provides temporary labor services to hospitals, clinics and home care agencies that provide allied healthcare services to individual patients. Clearly, Tenn. Code Ann. § 67-4-708(3)(C) places the taxpayer under classification 3 since its dominant business activity is the rendering of services. However, Tenn. Code Ann. § 67-4-708(3)(C)(i)(xvi) exempts from the business tax the sales of several different types of services which are described in the Standard Industrial Classification (“SIC”) Index of 1972 as amended. Tenn. Code Ann. § 67-4-708(3)(C)(i) specifically exempts “medical, dental, and allied health services to human beings, including sanatorium, convalescent and rest home care, but excluding services by persons engaged in the business of making dentures and artificial teeth.”

Generally, the taxpayer’s dominant business activity does not matter when applying an exemption. In order for an exemption to apply, gross receipts must be derived from providing one of the exempt services enumerated in Tenn. Code Ann. § 67-4-708(3)(C)(i)-(xv). Furthermore, the taxpayer is only exempt as to its gross receipts from that particular exempt service. Gross receipts from other non-exempt activities are subject to the business tax.

In *Aabakus, Incorporated v. Huddleston*, WL 548148 (Tenn. Ct. App. 1996) the Tennessee Court of Appeals considered the applicability of the business tax exemptions set forth in Tenn. Code Ann. § 67-4-708(3)(C)(i)-(xv). Aabakus provided human resource management services to its clients and received a lump sum fee for agreeing to perform such services. In order to do this, Aabakus became the “employer” of its clients’ employees. The employees continued to perform the same work and remained under the client’s direct supervision.

Each payday, clients of Aabakus provided hours worked and rates of pay for each employee along with a wire transfer to cover the gross payroll, all applicable taxes, insurance premiums and Aabakus’s service fee. Aabakus would then prepare payroll checks, pay taxes and insurance premiums, and file all necessary reports for each client. Funds remaining in the hands of Aabakus represented Aabakus’s service fees. Aabakus claimed to be exempt from the business tax because it claimed to be providing exempt accounting, auditing, and bookkeeping services.

The court found that Aabakus provided many more services than the exempt accounting, auditing, and bookkeeping services that Aabakus claimed to be providing. *Id.* at *1. The service fee paid by each client was based on all the services performed by Aabakus. Thus, the accounting, auditing and bookkeeping services provided could not be separated from the other human resource functions performed. The accounting, auditing and bookkeeping services performed were not separate activities generating a separate share of the “value added” by Abakus’s business, but rather were part-and-parcel of the entire service package performed by Aabakus. No single function or service could be viewed as incidental to others. *Id.* at 5. In other words, the services Aabakus provided were not accounting or any of the other exempt activities described in the SIC Index of 1972 as amended.

The court went on to say that Aabakus’s services were a combination of the various SIC industry classifications that would be classified, if at all, under one of the miscellaneous industry categories. Its functions were much broader than the “payroll accounting services” then classified under SIC industry number 8721. Its services might have been more properly classified as management consulting included in industry code number 8742. *Id.* at 5. Thus, the services provided by Aabakus did not qualify for the exemption.

Aabakus did not provide its clients with simple bookkeeping services nor did it provide its clients with permanent or temporary employees. Thus, its business tax liability was based on the fees that it charged for its personnel management services. *Id.* at 6.

The determination of whether a service is exempt is made based on the specific service that the Taxpayer provides rather than the aggregate of all services provided. The Taxpayer must be able to segregate its gross receipts so that it is clear which fees are generated by providing a particular employee that exclusively performs one of the activities exempted by Tenn. Code Ann. § 67-4-708(3)(C)(i)-(xv).

Unlike Aabakus, the Taxpayer is providing its clients with temporary employees, who exclusively perform services exempt from the business tax under Tenn. Code Ann. § 67-4-708(3)(C)(i). The fees that the Taxpayer receives for the services that it provides are based on the classification of each of its employees and the services provided by each employee. Also, unlike Aabakus, the Taxpayer can separately account for fees based on the identity of the customer and the nature of the services provided that customer.

The services actually performed by the Taxpayer’s employees are classified under industry code number 8099 as health and allied services. Tenn. Code Ann. § 67-4-708(3)(C)(i) exempts from the business tax all gross receipts from providing allied health services. Under the facts presented, one hundred percent (100%) of the Taxpayer’s revenue is derived from billing for allied healthcare services provided to individual patients and each employee’s medical services can be specifically tracked. As such, the Taxpayer’s gross receipts, derived from providing allied health services, are not subject to the business tax.

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APPROVED: Reagan Farr
Commissioner

DATE: 9-14-07