

**TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 11-42**

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 each individual series of a series limited liability company must file as a separate entity for Tennessee franchise and excise tax purposes.

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;
- (C) 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

[SLLC] was organized on [DATE], as a Tennessee series limited liability company. The SLLC is wholly owned by the [LP]; each of the SLLC's [SERIES] is also wholly owned by the LP.

The LP currently owns a number of rental properties but plans to transfer ownership of such properties to the [SERIES]. It is anticipated that each [SERIES] will hold title to a separate piece of rental property in order to separate and mitigate certain liabilities associated with the

ownership of such property. Once the LP has completed the transfers of title, it is expected that [SLLC] will contain upwards of thirty separate series.

For federal tax purposes, the SLLC and each [SERIES] are disregarded to the LP and are included on the LP's federal income tax return.

QUESTION

May the SLLC file a single Tennessee franchise and excise tax return that reports the activities of all of the [SERIES]?

RULING

No. The SLLC and each individual [SERIES] must file its own separate return for Tennessee franchise and excise tax purposes.

ANALYSIS

Tennessee imposes an excise tax on all persons, as defined under TENN. CODE ANN. § 67-4-2004(37) (Supp. 2010), doing business within Tennessee. TENN. CODE ANN. § 67-4-2007(a) (Supp. 2010). 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) (Supp. 2010) and 67-4-2106(a) (Supp. 2010).¹ Persons subject to the Tennessee franchise and excise taxes include, but are not limited to, limited liability companies. TENN. CODE ANN. § 67-4-2004(37). With certain limited exceptions, each taxpayer is considered a “separate and single business entity” for Tennessee franchise and excise tax purposes and must file a franchise and excise tax return on a separate entity basis. TENN. CODE ANN. §§ 67-4-2007(e)(1) and 67-4-2106(c).

The threshold question in the determination of whether the SLLC may file a single Tennessee franchise and excise tax return that includes the [SERIES] is whether each individual series is considered a separate entity for Tennessee state tax purposes. As explained below, each individual series must be treated as a separate entity.

The Tennessee Revised Limited Liability Company Act, TENN. CODE ANN. § 48-249-101 *et seq.* (the “TRLLCA”) permits the establishment of a limited liability company by filing articles of organization with the Tennessee Secretary of State, as set forth in TENN. CODE ANN. § 48-249-201(a) (Supp. 2010).

The TRLLCA was amended in 2006 to permit the establishment of one or more designated series within a limited liability company. The limited liability company's articles of organization or operating agreement may “establish, or provide for the establishment of, one (1) or more designated series of members, holders, managers, directors, membership interests or financial

¹ Note that, under TENN. CODE ANN. § 67-4-2108(a)(1) (Supp. 2010), 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.” For purposes of this section, “property” is to be “valued at cost less accumulated depreciation in accordance with generally accepted accounting principles.” TENN. CODE ANN. § 67-4-2108(a)(3).

rights having separate rights, powers or duties, with respect to specified property or obligations of the LLC, or profits and losses associated with specified property or obligations, and any such series may have a separate business purpose or investment objective.” TENN. CODE ANN. § 48-249-309(a) (Supp. 2010).

If certain statutory requirements are met,² each series of a series limited liability company must be treated as a separate entity with respect to the “debts, liabilities, obligations and expenses” of the series. Specifically, TENN. CODE ANN. § 48-249-309(b) (“Separateness of series”) provides that “the **debts, liabilities, obligations and expenses** incurred, contracted for or otherwise existing, with respect to a particular series ... **shall** be enforceable against the assets **of such series only**, and not against the assets of the limited liability company generally, or any other series of the LLC.” (Emphasis added.) Additionally, none of the debts, liabilities, obligations, or expenses of the limited liability company generally, or of another series, are enforceable against the assets of the series when the statutory requirements are met. *Id.*

Because a tax constitutes a liability or obligation, the tax liability of a particular series is enforceable only against the assets of that series. The clear intent of TENN. CODE ANN. § 48-249-309(b), which is titled “Separateness of series,” is therefore for each series to be treated as a separate entity for Tennessee state tax purposes. This conclusion is strongly supported by additional provisions of the TRLLCA that expressly state that each series “shall” be treated as a “separate LLC” for various purposes, including the classification of interests and voting rights; rights to shares of profits and distributions; management duties, admission of members, and transfers of memberships; and termination. TENN. CODE ANN. § 48-249-309(d)-(h).

Additionally, the fact that each series is treated as a separate entity for federal tax purposes strongly suggests that each series must also be treated as a separate entity for Tennessee state tax purposes. The federal tax classification of a limited liability company generally governs its classification for Tennessee state tax purposes. TENN. CODE ANN. § 48-249-1003 (Supp. 2010) provides that, “[f]or purposes of all state and local Tennessee taxes, a domestic or foreign LLC shall be treated as a partnership or an association taxable as a corporation, as such classification is determined for federal income tax purposes.”³ Thus, for state tax purposes, a limited liability company will be treated as a corporation, partnership, or disregarded entity in the same manner as it is for federal purposes.

Importantly, applicable federal regulations treat each series as a separate entity for the purpose of determining federal tax classification. On September 13, 2010, the Internal Revenue Service filed Prop. Treas. Reg. §§ 301.6011-6, 301.6071-2, and 301.7701-1(a)(5), and amended Treas.

² TENN. CODE ANN. § 48-249-309(b)(1)(A) requires that the “LLC documents establish or provide for the establishment of one (1) or more series.” While an operating agreement qualifies as an “LLC document,” TENN. CODE ANN. § 48-249-309(b)(1)(C) requires that notice of the limitation on liabilities of a series be set forth in the articles of organization, which are filed with the Secretary of State. TENN. CODE ANN. § 48-249-309(b)(1)(B) requires that separate and distinct records be maintained for each series. Additionally, the assets associated with each series must be “reflected and held in separate and distinct records, directly or indirectly, including through a nominee or otherwise, and accounted for in such separate and distinct records separately from the other assets of the LLC and the assets of any other series of the LLC.”

³ This provision (originally codified at TENN. CODE ANN. § 48-211-101) was enacted in 1994, before the publication of the federal “check-the-box” regulations in late 1996. As a result, the provision does not specifically reference the “disregarded” entity option now available under the federal regulations.

Reg. §§ 301.7701-1(e) and (f).⁴ Under these proposed and amended federal regulations, each series is treated as a separate entity. As a result, each series' federal tax classification will be determined separately under Treas. Reg. §§ 301.7701-2, 301.7701-3, and/or 301.7701-4. Thus, a series with one owner is treated either as a corporation or as disregarded to its owner, and a series with two or more owners is treated either as a corporation or as a partnership.

Accordingly, each individual series must be treated as a separate limited liability company for Tennessee franchise and excise tax purposes.

The second question in the determination of whether the SLLC may file a single Tennessee franchise and excise tax return that includes the [SERIES] is whether the [SERIES] are treated as entities that are disregarded to the SLLC for franchise and excise tax purposes.

As noted above, each taxpayer is generally considered a "separate and single business entity" for franchise and excise tax purposes and must file a franchise and excise tax return on a separate entity basis. TENN. CODE ANN. §§ 67-4-2007(e)(1) and 67-4-2106(c). However, a limited liability company will nevertheless be disregarded to its owner for franchise and excise tax purposes under certain circumstances. In such instances, the limited liability company will not file a separate return; rather, it will be included on the return of its owner.

TENN. CODE ANN. §§ 67-4-2007(d) and 67-4-2106(c) provide that, for purposes of Tennessee franchise and excise taxation, a business entity will be classified as a corporation, partnership, or other type of business entity, consistent with the way the entity is classified for federal income tax purposes. However, TENN. CODE ANN. §§ 67-4-2007(d) and 67-4-2106(c) further provide that "entities that are disregarded for federal income tax purposes, except for limited liability companies whose single member is a corporation, shall not be disregarded" for Tennessee franchise and excise tax purposes. In other words, a limited liability company that is wholly owned by a corporation and that is disregarded for federal income tax purposes will be disregarded for Tennessee franchise and excise tax purposes as well. All other federally disregarded limited liability companies are treated as separate entities for franchise and excise tax purposes. TENN. CODE ANN. §§ 67-4-2007(e)(1) and 67-4-2106(c).

As explained below, each [SERIES] is properly considered a separate entity for franchise and excise tax purposes.

To be disregarded under TENN. CODE ANN. §§ 67-4-2007(d) and 67-4-2106(c), a particular [SERIES] must 1) constitute a single member limited liability company; 2) be classified as a disregarded entity for federal income tax purposes; and 3) be wholly owned by a corporation. If any of these requirements are not met, the [SERIES] will be treated as a separate entity for franchise and excise tax purposes.

The facts indicate that [LP] is the single member of each of the [SERIES] and that each [SERIES] is classified as a disregarded entity for federal income tax purposes. Thus, while a particular [SERIES] does in fact constitute a single member limited liability company and is classified as a disregarded entity for federal income tax purposes, the series is not wholly owned by a corporation. Rather, each [SERIES] is wholly owned by a limited partnership. Accordingly, each [SERIES] is properly considered a separate entity for franchise and excise tax purposes.

⁴ F.R. Doc. 2010-22793; 75 Fed. Reg. 55699 *et seq.*

Because the [SERIES] do not meet the requirements under TENN. CODE ANN. §§ 67-4-2007(d) and 67-4-2106(c) to be treated as disregarded entities, each such series must file its own separate Tennessee franchise and excise tax return.⁵

Note that the SLLC must also file a separate Tennessee franchise and excise tax return, for the same reasons discussed above with respect to the [SERIES] (*i.e.*, it is a single member limited liability company that is disregarded for federal tax purposes, but is wholly owned by a limited partnership instead of a corporation). However, unless the SLLC holds assets and/or has business activities in its own right separate and apart from the series, it will likely have only a minimal tax liability.⁶

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APPROVED: Richard H. Roberts
Commissioner of Revenue

DATE: 09/06/2011

⁵ The franchise and excise tax statutes do not permit affiliated groups to elect to file a single combined or consolidated return. TENN. CODE ANN. § 67-4-2103(d) (2006) does allow an affiliated group to elect to compute its net worth on a consolidated basis for franchise tax purposes. However, each member of the group must nevertheless still file its own separate franchise and excise tax return.

⁶ An entity with no positive net worth and no real or tangible property owned or used in Tennessee must pay a minimum franchise tax of \$100. TENN. CODE ANN. § 67-4-2119 (2006).