

HOUSE BILL 644

By McCormick

AN ACT to amend Tennessee Code Annotated, Title 67, Chapter 4, Part 20; Title 67, Chapter 4, Part 21; Title 67, Chapter 4, Part 7 and Title 67, Chapter 6, relative to taxation.

WHEREAS, Tennessee's sales and use taxes, franchise and excise taxes, and business tax are intended to be broad-based taxes levied on all persons engaging in business in this State; and

WHEREAS, advances in technology and business practices now enable out-of-state companies to engage in business in this State in ways previously unaddressed by this General Assembly; and

WHEREAS, a physical presence in this State is now unnecessary to conduct profitable business in this State to the same extent as locally-based businesses; and

WHEREAS, advances in technology now enable out-of-state businesses to comply with this State's tax laws at costs similar to the compliance costs of locally-based businesses; and

WHEREAS, in light of these changes, many states have already reformed their rules for applying taxes to out-of-state businesses; and

WHEREAS, as applied to modern businesses, older provisions of this State's tax laws result increasingly in outcomes unintended by this General Assembly, and discourage businesses from investing in this State's property and people; and

WHEREAS, by changing these laws, this General Assembly intends to keep this State's tax laws in line with modern business practices; now, therefore,

BE IT ENACTED BY THE GENERAL ASSEMBLY OF THE STATE OF TENNESSEE:

SECTION 1. This act shall be known and may be cited as the "Revenue Modernization Act".

SECTION 2. Tennessee Code Annotated, Section 67-4-702(a), is amended by inserting the following as a new subdivision:

() “Substantial nexus in this state” means any direct or indirect connection of the taxpayer to this state such that the taxpayer can be required under the Constitution of the United States to remit the tax imposed under this part. Such connection includes, but is not limited to, any of the following:

(A) The taxpayer is organized or commercially domiciled in this state;

(B) The taxpayer owns or uses its capital in this state;

(C) The taxpayer has systematic and continuous business activity in this state that has produced gross receipts attributable to customers in this state; or

(D) 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:

(i) The taxpayer’s total receipts in this state during the tax period, as determined consistent with § 67-4-2012, exceed the lesser of five hundred thousand dollars (\$500,000) or twenty-five percent (25%) of the taxpayer’s total receipts everywhere during the tax period;

(ii) 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 consistent with § 67-4-2012, exceeds the lesser of fifty thousand dollars (\$50,000) or twenty-five percent (25%) of the average value of all the taxpayer’s total real and tangible personal property; or

(iii) The total amount paid in this state during the tax period by the taxpayer for compensation, as determined consistent with § 67-4-2012, exceeds the lesser of fifty thousand dollars (\$50,000) or twenty-five percent (25%) of the total compensation paid by the taxpayer;

SECTION 3. Tennessee Code Annotated, Section 67-4-711(a)(6), is amended by deleting the subdivision and substituting instead the following:

(6) The sale of any service that is delivered to a location outside this state;

SECTION 4. Tennessee Code Annotated, Section 67-4-717, is amended by deleting subsection (a) and substituting instead the following:

(a)

(1) All persons with substantial nexus in this state during the tax period and engaged in this state in any vocation, occupation, business, or business activity enumerated, described, or referred to in § 67-4-708(1)–(5), with or without establishing a physical location, outlet, or other place of business in the state, shall be subject to the tax levied by § 67-4-704. For purposes of this section, the phrase “engaged in this state” shall include, but not be limited to, any of the following:

(A) The sale of tangible personal property that is shipped or delivered to a location in this state;

(B) The sale of a service that is delivered to a location in this state;

(C) The leasing of tangible personal property that is located in this state; or

(D) Making sales as a natural gas marketer to customers located within this state through the presence in this state of the seller’s property, the holding of pipeline capacity by the seller on pipelines located in this state, or through the presence in this state of the seller’s employees, agents, independent contractors, or other representatives acting on behalf of the seller to solicit orders, provide customer service, or conduct other activities in furtherance of such sales. For purposes of this subdivision (a)(1)(D), the phrase “presence in this state of the seller’s

property” shall include property owned by the seller in this state during delivery to the customer, whether in a pipeline or otherwise.

(2) All persons that are subject to the tax levied by § 67-4-704 and have a physical location, outlet, or other place of business within a municipality in this state shall be subject to the tax levied by § 67-4-705. Persons that do not have a physical location, outlet, or other place of business within a municipality in this state shall not be subject to the tax levied by § 67-4-705.

SECTION 5. Tennessee Code Annotated, Section 67-4-2004, is amended by inserting the following as a new subdivision:

() “Substantial nexus in this state” means any direct or indirect connection of the taxpayer to this state such that the taxpayer can be required under the Constitution of the United States to remit the tax imposed under this part and part 21 of this chapter.

Such connection includes, but is not limited to, the following:

- (A) The taxpayer is organized or commercially domiciled in this state;
- (B) The taxpayer owns or uses its capital in this state;
- (C) The taxpayer has systematic and continuous business activity in this state that has produced gross receipts attributable to customers in this state;
- (D) 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
- (E) 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:
 - (i) The taxpayer’s total receipts in this state during the tax period, as determined under § 67-4-2012, exceed the lesser of five hundred thousand dollars (\$500,000) or twenty-five percent (25%) of the taxpayer’s total receipts everywhere during the tax period;

(ii) 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 § 67-4-2012, exceeds the lesser of fifty thousand dollars (\$50,000) or twenty-five percent (25%) of the average value of all the taxpayer's total real and tangible personal property; or

(iii) The total amount paid in this state during the tax period by the taxpayer for compensation, determined under § 67-4-2012, exceeds the lesser of fifty thousand dollars (\$50,000) or twenty-five percent (25%) of the total compensation paid by the taxpayer;

SECTION 6. Tennessee Code Annotated, Section 67-4-2006(b)(2)(N)(i), is amended by deleting the first sentence and substituting instead the following language:

Any intangible expense, or portion thereof, that is paid, accrued, or incurred in connection with a transaction with one (1) or more affiliates if the commissioner determines, upon application by the taxpayer, that the transaction or transactions giving rise to such intangible expense, or portion thereof, has a substantial business purpose and did not have as its principal purpose the avoidance of the tax levied by this part. If the taxpayer disputes the commissioner's determination, the burden shall be on the taxpayer to show by clear and convincing evidence that the commissioner's determination is incorrect.

SECTION 7. Tennessee Code Annotated, Section 67-4-2007(a), is amended by deleting from the first sentence the language "doing business in Tennessee" and substituting instead the language "doing business in this state and having substantial nexus in this state".

SECTION 8. Tennessee Code Annotated, Section 67-4-2012, is amended by deleting subsections (i) and (j) in their entirety and substituting instead the following language as a new subsection (i) and redesignating the remaining subsection accordingly:

(i)

(1) Receipts from sales, other than sales of tangible personal property, are in this state if the taxpayer's market for the sale is in this state. The taxpayer's market for a sale is in this state:

(A) In the case of sale, rental, lease, or license of real property, if and to the extent the property is located in this state;

(B) In the case of rental, lease, or license of tangible personal property, if and to the extent the property is located in this state;

(C) In the case of sale of a service, if and to the extent the service is delivered to a location in this state;

(D) In the case of intangible property:

(i) That is rented, leased, or licensed, if and to the extent the intangible property is used in this state; provided, that intangible property utilized in marketing a good or service to a consumer is considered used in this state if that good or service is purchased by a consumer who is in this state; and

(ii) That is sold, if and to the extent the property is used in this state; provided, that:

(a) A contract right, government license, or similar intangible property that authorizes the holder to conduct a business activity in a specific geographic area is considered used in this state if the geographic area includes all or part of this state;

(b) Receipts from intangible property sales that are contingent on the productivity, use, or disposition of the

intangible property shall be treated as receipts from the rental, lease, or licensing of such intangible property under subdivision (i)(1)(D)(i); and

(c) All other receipts from a sale of intangible property shall be excluded from the numerator and denominator of the receipts factor.

(2) If the state or states of assignment under subdivision (i)(1) cannot be determined, the state or states of assignment shall be reasonably approximated.

(3) If the state of assignment cannot be determined under subdivision (i)(1) or reasonably approximated under subdivision (i)(2), such sale shall be excluded from the numerator and denominator of the sales factor.

SECTION 9. Tennessee Code Annotated, Title 67, Chapter 4, Part 20, is amended by adding the following as a new section:

(a) Notwithstanding any law to the contrary, a taxpayer that meets the gross sales threshold and the receipts factor threshold during the tax period qualifies for the application of this section and may elect the application of this section by filing an election form with the department and providing such information as may be required by the commissioner on or before the due date of the tax return for the period for which such election is to take effect. Such election shall remain in effect until revoked by the taxpayer or until the taxpayer no longer qualifies for the election.

(b) For purposes of this section, the following shall apply:

(1) A taxpayer meets the gross sales threshold if the taxpayer's sales of tangible personal property in this state exceed one billion dollars (\$1,000,000,000), as determined under § 67-4-2012 without regard to this section;

(2) A taxpayer meets the receipts factor threshold, if the taxpayer's receipts factor, as determined under § 67-4-2012 without regard to this section, exceeds ten percent (10%); and

(3) "Certified distribution sales" means sales of tangible personal property made in this state by the taxpayer to a distributor that are resold for ultimate use or consumption outside the state; provided, that the distributor has certified that such property has been resold for ultimate use or consumption outside this state. Such certification shall be made in the manner prescribed by the commissioner.

(c)

(1) A taxpayer that has made the election described in subsection (a) shall, so long as such election is in effect, apportion net earnings and net worth in the manner prescribed elsewhere in this part and part 21 of this chapter; provided, however, that the total amount derived from certified distribution sales shall be excluded from the numerator of the receipts factor, as that term is defined elsewhere in this part and part 21 of this chapter.

(2) A taxpayer that has made the election described in subsection (a) shall, so long as such election is in effect, pay to the commissioner, annually, an excise tax on the total amount of certified distribution sales excluded from the numerator of the taxpayer's receipts factor. The amount of such tax shall be computed in the following manner:

(A) In the case of taxpayers excluding no more than two billion dollars (\$2,000,000,000) of certified distribution sales for the tax period, the amount of such tax shall be one half of one percent (0.5%) of the total amount of certified distribution sales;

(B) In the case of taxpayers excluding more than two billion dollars (\$2,000,000,000) but no more than three billion dollars (\$3,000,000,000) of certified distribution sales for the tax period, the amount of such tax shall be:

(i) Three-eighths of one percent (.375%) of certified distribution sales in excess of two billion dollars (\$2,000,000,000); plus

(ii) Ten million dollars (\$10,000,000);

(C) In the case of taxpayers excluding more than three billion dollars (\$3,000,000,000) but no more than four billion dollars (\$4,000,000,000) of certified distribution sales for the tax period, the amount of such tax shall be:

(i) One fourth of one percent (.25%) of certified distribution sales in excess three billion dollars (\$3,000,000,000); plus

(ii) Thirteen million, seven hundred and fifty thousand dollars (\$13,750,000); and

(D) In the case of taxpayers excluding more than four billion dollars (\$4,000,000,000) of certified distribution sales for the tax period, the amount of such tax shall be:

(i) One-eighth of one percent (.125%) of certified distribution sales in excess of four billion dollars (\$4,000,000,000); plus

(ii) Sixteen million, two hundred and fifty thousand dollars (\$16,250,000).

(3) The tax due under subdivision (c)(2) shall be in addition to all other taxes, including the tax imposed by § 67-4-2007(a).

SECTION 10. Tennessee Code Annotated, Section 67-4-2105(a), is amended by deleting from the first sentence the language “doing business in Tennessee” and substituting instead the language “doing business in this state and having substantial nexus in this state”.

SECTION 11. Tennessee Code Annotated, Section 67-4-2111, is amended by deleting subsections (i) and (j) in their entireties and substituting instead the following language as a new subsection (i) and redesignating the remaining subsection accordingly:

(i)

(1) Receipts from sales, other than sales of tangible personal property, are in this state if the taxpayer’s market for the sales is in this state. The taxpayer’s market for a sale is in this state:

(A) In the case of sale, rental, lease, or license of real property, if and to the extent the property is located in this state;

(B) In the case of rental, lease, or license of tangible personal property, if and to the extent the property is located in this state;

(C) In the case of sale of a service, if and to the extent the service is delivered to a location in this state; and

(D) In the case of intangible property:

(i) That is rented, leased, or licensed, if and to the extent the intangible property is used in this state; provided, that intangible property utilized in marketing a good or service to a consumer is considered used in this state if that good or service is purchased by a consumer who is in this state; and

(ii) That is sold, if and to the extent the property is used in this state; provided, that:

(a) A contract right, government license, or similar intangible property that authorizes the holder to conduct a business activity in a specific geographic area is considered used in this state if the geographic area includes all or part of this state;

(b) Receipts from intangible property sales that are contingent on the productivity, use, or disposition of the intangible property shall be treated as receipts from the rental, lease, or licensing of such intangible property under subdivision (i)(1)(D)(i); and

(c) All other receipts from a sale of intangible property shall be excluded from the numerator and denominator of the receipts factor.

(2) If the state or states of assignment under subdivision (i)(1) cannot be determined, the state or states of assignment shall be reasonably approximated.

(3) If the state of assignment cannot be determined under subdivision (i)(1) or reasonably approximated under subdivision (i)(2), such sale shall be excluded from the numerator and denominator of the sales factor.

SECTION 12. Tennessee Code Annotated, Section 67-6-102, is amended by inserting the following as a new subdivision:

() “Video game digital product” means the right to access and use computer software that facilitates human interaction with a user interface to generate visual feedback for amusement purposes, when possession of the computer software is

maintained by the seller or a third party, regardless of whether the charge for the service is on a per use, per user, per license, subscription, or some other basis;

SECTION 13. Tennessee Code Annotated, Section 67-6-231(a), is amended by designating the current language as subdivision (1) and by adding the following language as subdivision (2):

(2) For purposes of subdivision (a)(1), use of computer software includes the right to access and use software that remains in the possession of the dealer who provides the software or in the possession of a third party on behalf of such dealer. If the customer accesses the software from a location in this state as indicated by the residential street address or the primary business address of the customer, such access shall be deemed equivalent to the sale or licensing of the software and electronic delivery of the software for use in this state. If the sales price or purchase price of the software relates to users located both in this state and outside this state, the dealer or customer may allocate to this state a percentage of the sales price or purchase price that equals the percentage of users in this state. Nothing in this subdivision (a)(2) shall be construed to impose a tax on any services that are not subject to tax under this chapter, such as information services, payment processing services, internet access, or the mere storage of digital products, digital codes, or computer software.

SECTION 14. Tennessee Code Annotated, Section 67-6-233, is amended by deleting the language “specified digital products” wherever it appears and substituting instead the language “specified digital products or video game digital products”, and is further amended by deleting the language “specified digital product” wherever it appears and substituting instead the language “specified digital product or video game digital product”.

SECTION 15. Tennessee Code Annotated, Title 67, Chapter 6, Part 5, is amended by adding the following as a new section:

It is the legislative intent to impose the taxes levied by this chapter to the fullest extent allowed under the constitutions of the United States and the state of Tennessee.

SECTION 16. Tennessee Code Annotated, Title 67, Chapter 6, Part 5, is amended by adding the following as a new section:

(a) A dealer is presumed to have a representative, agent, salesperson, canvasser, or solicitor operating in this state for the purpose of making sales and is presumed to have a substantial nexus in this state if:

(1) The dealer enters into an agreement or contract with one (1) or more persons located in this state under which the person, for a commission or other consideration, directly or indirectly refers potential customers to the dealer, whether by a link on an Internet website or any other means; and

(2) The dealer's cumulative gross receipts from retail sales made by the dealer to customers in this state who are referred to the dealer by all residents with this type of an agreement with the dealer exceed ten thousand dollars (\$10,000) during the preceding twelve (12) months.

(b) The presumption in subsection (a) may be rebutted only by clear and convincing evidence that the person with whom the dealer has an agreement or contract did not conduct any activities in this state that would substantially contribute to the dealer's ability to establish and maintain a market in this state during the preceding twelve (12) months.

SECTION 17. If any provision of this act or the application of any provision of this act to any person or circumstance is held invalid, the invalidity shall not affect other provisions or applications of the act that can be given effect without the invalid provision or application, and to that end, the provisions of this act are declared to be severable.

SECTION 18. Sections 2–5, and 7–11 of this act shall take effect January 1, 2016, the public welfare requiring it, and shall apply to all tax years beginning on or after January 1, 2016. Sections 12–14 and 16 of this act shall take effect July 1, 2015, the public welfare requiring it. All other sections of this act shall take effect upon becoming a law, the public welfare requiring it.