



State and Local Tax Alert

Tennessee Edition



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Tennessee Announces Compromise Opportunity for Intangible Holding Company Expenses

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Over the past year, the Tennessee Department of Revenue has been actively engaged in the process of compromising a series of Tennessee excise tax assessments issued against companies that deducted intangible expenses paid to affiliated holding companies. The negotiations culminated in a settlement offered in November when the Department agreed to drop the assessments if the assessed taxpayers agreed to pay 25% of the amounts assessed. On November 29, 2011, the Department issued Notice 11-17 expressing its willingness to extend similar settlement terms to taxpayers that have yet to be audited or assessed by the Department.

Assessments on this issue typically have been made in situations in which the Department has identified "significant concerns" regarding the economic substance of the underlying intangible holding company transaction. Factors that the Department has considered relevant are: (1) the nature of the intangible property and how it is used, (2) the method by which the intangible asset was transferred to the holding company, (3) whether actual cash was exchanged in the relevant transactions, (4) whether the holding company has separate employees and office space, and (5) whether there are practical economic effects resulting from the transaction aside from tax planning. See Tenn. Ltr. Rul. 06-28; Tenn. Ltr. Rul. 06-35. When the Department has determined that intangible expenses are not related to bona fide, arms-length transactions, the Department has issued assessments disallowing the deduction of the intangible expense.

Potential Compromise

The Department believes there may be other taxpayers with comparable fact patterns that, upon future examination by the Department, may result in assessments. Accordingly, the Department is inviting taxpayers that have had intangible expenses disallowed or are concerned about potential disallowance to voluntarily approach the Department about the potential to compromise and settle their liability or potential liability. The Department has indicated that taxpayers who voluntarily approach the Department before December 31, 2011, will be considered a candidate for a compromise using the same 25% settlement currently being offered. Compromise requests may still be made after December 31, and will be evaluated to determine what terms should apply. The Notice indicates that the compromise requests can still be made for open tax years ending on or before June 30, 2012.

Taxpayers should be aware that the information in the notice may change. Thus, interested taxpayers should closely monitor the 2012 legislative session for the potential for new add-back legislation.

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