TENNESSEE DEPARTMENT OF REVENUE
LETTER RULING # 22-01

Letter rulings are binding on the Department only with respect to the individual taxpayer being addressed in the ruling. This ruling is based on the particular facts and circumstances presented and is an interpretation of the law at a specific point in time. The law may have changed since this ruling was issued, possibly rendering it obsolete. The presentation of this ruling in a redacted form is provided solely for informational purposes and is not intended as a statement of Departmental policy. Taxpayers should consult with a tax professional before relying on any aspect of this ruling.

SUBJECT

The availability of the Tennessee franchise and excise tax industrial machinery credit to an entity whose revenue is primarily from the sale of renewable information numbers and low carbon fuel standard credits.

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

[TAXPAYER] (the "Taxpayer") is a [STATE] limited liability company that is wholly owned by [PARENT]. The Taxpayer is [REDACTED].

The Taxpayer operates [AN INDUSTRIAL GAS] production facility at [TENNESSEE LOCATION], where it produces and sells [INDUSTRIAL GAS] ("industrial gas") to its customer, [REDACTED]. The industrial gas is produced by [REDACTED]. The Taxpayer uses [EQUIPMENT TO PRODUCE] the industrial gas it sells to its customer.

When the industrial gas produced by the Taxpayer is sold into the transportation fuel market, it qualifies for renewable identification numbers ("RINs") and if sold into California, it also qualifies for Low Carbon Fuel Standard ("LCFS") credits. RINs are credits purchased by refiners and importers of gasoline or diesel fuel to comply with the Renewable Fuel Standard ("RFS") program, which Congress created to reduce greenhouse gas emissions and expand the nation's renewable fuels sector while reducing reliance on imported oil.[1] Similarly, importers or refiners of fuel in California purchase LCFS credits to comply with a program created by the California Air Resource Board to reduce petroleum dependency and achieve air quality benefits.[2]

RINs and LCFS credits are generated when renewable fuel is produced.[3] Approximately 1,000 cubic feet of industrial gas generates 1 MMBTU[4] and 1 MMBTU generates 11.727 RINs.[5] RINs and LCFS credits may stay with the associated renewable fuel when it is sold or be separated from the renewable fuel and sold separately. RINs and LCFS credits can be used to demonstrate compliance, stored for later use, traded between regulated parties, or sold to fellow regulated parties. In the Taxpayer's case, the Taxpayer sells all RINs and LCFS credits to [CUSTOMER] under the same agreement as the industrial gas. The Taxpayer does not separate the RINs and LCFS credits from the industrial gas and does not sell the credits separately to other parties.

For accounting purposes, the Taxpayer accrues RINs and LCFS credits directly into revenue and accounts receivable based on when the credits are produced. The Taxpayer does not have an inventory or other balance sheet related item for RINs and LCFS credits since they are all sold to [CUSTOMER] with the gas when produced.

During the [YEARS] tax periods, the Taxpayer's revenue sources were as follows:

Year	Sales of Industrial Gas	Sales of RINs and LCFS credits
[REDACTED]	[PERCENTAGE]	[PERCENTAGE]
[REDACTED]	[PERCENTAGE]	[PERCENTAGE]
[REDACTED]	[PERCENTAGE]	[PERCENTAGE]

[1] *See* Renewable Fuel Standard Program, ENVIRONMENTAL PROTECTION AGENCY, https://www.epa.gov/renewable-fuel-standard-program (last visited Sept. 30, 2021).

[2] *See* Low Carbon Fuel Standard, AIR RESOURCES BOARD, https://ww2.arb.ca.gov/our-work/programs/low-carbon-fuel-standard (last visited Sept. 30, 2021).

[3] There are other ways to generate LCFS credits, but they are not applicable to this ruling.

[4] MMBTU stands for One million British Thermal Unit, which is a standard unit for measurement for natural gas financial contracts.

RULING

For the [YEARS] tax periods, is the Taxpayer eligible to claim the Tennessee franchise and excise tax industrial machinery credit under TENN. CODE ANN. § 67-4-2009(3) (Supp. 2021) with respect to purchases of equipment the Taxpayer made during those tax periods?

> Ruling: Yes. The Taxpayer's purchases of equipment during the [YEARS] tax periods qualify for the industrial machinery tax credit in TENN. CODE ANN. § 67-4-2009(3) (Supp. 2021) because the Taxpayer's principal business during the [YEARS] tax periods was manufacturing.

ANALYSIS

Tennessee imposes an excise tax at the rate of 6.5% on the net earnings of all persons doing business within Tennessee.[6] Tennessee also imposes a franchise tax rate at the rate of $0.25 per $100, or major fraction thereof, on the net worth of a person doing business in Tennessee.[7] Persons subject to Tennessee franchise and excise taxes include, but are not limited to, limited liability companies.[8]

Taxpayers who purchase qualifying industrial machinery that will be located in Tennessee are entitled to take an industrial machinery credit against their combined Tennessee franchise and excise tax liability for the period in which the purchase occurs.[9] The industrial machinery credit is generally equal to 1% of the purchase price of the qualifying machinery.[10] For Tennessee franchise and excise tax purposes, qualifying industrial machinery includes "industrial machinery" as defined in TENN. CODE ANN. § 67-6-102,[11] as well as certain additional computer-related assets.

TENN. CODE ANN. § 67-6-102 (46)(A)(i) (Supp. 2021) defines "industrial machinery" as "machinery . . . that is necessary to, and primarily for, the fabrication or processing of tangible personal property for resale and consumption off the premises . . . where the use of such machinery, equipment or facilities is by one who engages in such fabrication or processing as one's principal business."[12] Manufacturing is a taxpayer's principal business if more than fifty percent of its revenue at a given location is derived from fabricating or processing tangible personal property[13] for resale.[14]

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[6] TENN. CODE ANN. § 67-4-2007(a) (Supp. 2021).

[7] TENN. CODE ANN. § 67-4-2105(a) (Supp. 2021) and -2106(a) (2013).

[8] TENN. CODE ANN. § 67-4-2004(38) (Supp. 2021).

[9] TENN. CODE ANN. § 67-4-2009(3)(A) (Supp. 2021).

[10] *Id*. With certain exceptions, the credit shall not exceed fifty percent of the combined franchise and excise tax liability shown by the return before the credit is taken. TENN. CODE ANN. § 67-4-2009(3)(B). Any unused credit may be carried forward for a maximum of fifteen years. TENN. CODE ANN. § 67-4-2009(3)(C)(i). Note that industrial machinery credits of up to ten percent of the purchase price are available to qualifying taxpayers making certain levels of capital investments. *See, e.g.,* TENN. CODE ANN. § 67-4-2009(3)(I).

[11] *See* TENN. CODE ANN. § 67-6-102(46) (Supp. 2021).

[12] TENN. CODE ANN. § 67-6-102(46)(A)(i).

[13] "Tangible personal property" means "personal property that can be seen, weighed, measured, felt or touched, or that is in any manner perceptible to the senses." TENN. CODE ANN. § 67-6-102(95)(A).

[14] *Tenn. Farmers' Coop v. State ex rel. Jackson*, 736 S.W. 2d 87, 91-92 (Tenn. 1987) (holding that the Commissioner's 51 percent test based on gross sales is not erroneous for determining a taxpayer's principal business).

For the [YEARS] tax periods, the Taxpayer's revenue was derived from the sale of industrial gas and the credits that were created when the industrial gas was produced. These particular RINs and LCFS credits were generated by the same activity that produced the industrial gas and were not the product of any other effort or activity undertaken by the Taxpayer. Furthermore, the Taxpayer's only activity at its location in Tennessee was the production of industrial gas. Therefore, all of the revenue described above is derived directly from the process of producing industrial gas at the Tennessee location.

Consistent with these facts, the Taxpayer's principal business at its Tennessee location during the [YEARS] tax periods was manufacturing. Accordingly, the Taxpayer's purchases of equipment used primarily for the production of industrial gas during the [YEARS] tax periods qualify for the industrial machinery tax credit in TENN. CODE ANN. § 67-4-2009(3).

APPROVED:	David Gerregano Commissioner of Revenue
DATE:	2/2/2022