IN THE COURT OF APPEALS OF TENNESSEE
AT NASHVILLE
November 21, 2013 Session

VODAFONE AMERICAS HOLDING INC. & SUBSIDIARIES v. RICHARD H. ROBERTS, COMMISSIONER OF REVENUE, STATE OF TENNESSEE

Appeal from the Chancery Court for Davidson County
No. 071860IV Russell T. Perkins, Judge

No. M2013-00947-COA-R3-CV - Filed June 23, 2014

FRANK G. CLEMENT, JR., J., dissenting.

I respectfully dissent from the majority's conclusion that the facts of this case empowered the Commissioner of Revenue to issue a variance from the statutorily mandated apportionment methodology by which Plaintiffs must compute their Tennessee franchise and excise tax liability. The Commissioner's authority under Tenn. Code Ann. § 67-4-2014(a) to issue a variance is limited by Rule 1320-6-1-.35(1)(a)(4) to "unusual fact situations, which ordinarily will be unique and nonrecurring," and no such facts are specifically articulated in the Commissioner's variance letter and no such facts can be found in this record.

As Plaintiffs correctly contend, Tennessee's statutory scheme expressly required Plaintiffs to source their receipts for telecommunications services based upon the "cost of performance methodology" stated in our franchise and excise tax statutes, specifically, Tenn. Code Ann. §§ 67-4-2012(i) and 67-4-2111(i). Pursuant to the statutory mandate, Plaintiffs' service receipts are sourced - on an all-or-nothing basis - to a single state, that being the state where the preponderance of the taxpayer's costs of performing the service occurs under Tennessee's statutorily-mandated cost of performance methodology; here, the parties stipulated that the majority of Plaintiffs' "earnings producing activities" occurred in a state other than Tennessee. Accordingly, as the standard apportionment methodology mandates, none of Plaintiffs' receipts from their telecommunications services, not even those attributable to customers with Tennessee billing addresses, can be sourced to Tennessee.

The Commissioner acknowledges that Plaintiffs' contention is both statistically correct and derived from Tenn. Code Ann. § 67-4-2012(i)(2); nevertheless, the Commissioner contends this "fails to meet the higher goal of fairly representing the business

Plaintiffs derive from Tennessee." Accordingly, the Commissioner insists he exercised authority expressly accorded by the General Assembly, pursuant to Tenn. Code Ann. § 67-4-2014(a), to vary the standard formula.

I submit the reasons given by the Commissioner in his variance letter are insufficient to authorize the extraordinary use of his variance authority. Although his variance letter is very thorough and well-reasoned in many respects, the "reasons" identified do not provide a proper legal basis upon which a variance may be imposed, "fairness" notwithstanding. For example, the Commissioner does not identify "unusual fact situations, which ordinarily will be unique and nonrecurring," as required in Rule 1320-6-1-.35(1)(a)(4). That same rule requires that the nonrecurring unusual fact situation produce "incongruous results," yet the only unusual result identified by the Commissioner is that the states where the earning producing activities occurred, California, Georgia, and New Jersey, chose not to adopt the cost of performance methodology; thus, he was concerned the income may escape taxation. I find this circumstance irrelevant because the adoption of the cost of performance methodology was a policy decision by the Tennessee General Assembly; whether other states adopt the same or different methodologies is a policy decision of those states. Moreover, if another state's decision to not impose a corresponding tax were a concern of the Tennessee General Assembly, it could have adopted a catch-all tax provision to apply in such circumstances, but it did not. *See*, *e.g.*, Tenn. Code Ann. § 56-4-218 (the retaliatory insurance premium tax).[1]

The Commissioner's concern that "application of the [cost of performance] methodology would mean that the overwhelming majority of these Taxpayers' earnings would not be captured in any other state" is also problematic for *the variance statute does not authorize the Commissioner to impose a tax merely because another state chooses not to impose a tax*. Again, that is a policy decision that only the General Assembly may make. Moreover, there is no correlation between the Commissioner's finding that the apportionment formula "would not fairly represent the extent of Plaintiffs' business activities in Tennessee," and the fact the receipts at issue, revenue from customers with Tennessee billing addresses, are not subject to "other taxing jurisdictions." The Commissioner expressly found, as he stated in one paragraph, that the application of the cost of performance methodology would not fairly represent the extent of Plaintiffs' business activities in Tennessee and that "[u]se

[1]With the enactment of Tenn. Code Ann. § 56-4-218, the General Assembly imposed a retaliatory insurance premium tax in an amount equal to the difference between (a) the taxes imposed by Tennessee upon a foreign insurance company doing business in Tennessee, and (b) the taxes that would be imposed upon a hypothetical Tennessee insurance company doing the same amount and type of business in the foreign insurer's home state.

of the [cost of performance] methodology allows the Taxpayers . . . to derive substantial receipts from Tennessee markets without such receipts being accounted for in Tennessee . . . and without such receipts being recognized in other taxing jurisdictions." The fact that other jurisdictions do not tax receipts is simply no justification to support a finding that Tennessee may tax the otherwise untaxed receipts to "fairly" represent a company's business activity in Tennessee. I find no justification for this rationale and also find it contrary to the cost of performance methodology expressly enacted by the Tennessee General Assembly in Tenn. Code Ann. §§ 67-4-2012(i) and 67-4-2111(i).

The Commissioner also compared the benefits and deficiencies of the two apportionment methodologies, which I believe is a statement of the Commissioner's preference for the primary place of use method in spite of the fact the Tennessee General Assembly made the policy decision to adopt the cost of performance methodology for calculating franchise and excise tax liability for multi-state taxpayers. This criticism is evident from the following statement in the letter.

> The [primary place of use] method is straightforward and conceptually satisfying in that it treats as Tennessee receipts the payments that Tennessee customers/residents make for cellphone services provided by the Taxpayers. . . . .
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> The [cost of performance] method is not so straightforward because it sources receipts to the state where the greater proportion of the earnings-producing activity is performed, based on costs of performance. In the Taxpayers' particular situation, activities that produce earnings from providing cellphone service take place in multiple states. It may be a matter of judgment or opinion as to the particular state in which the greater portion of the earnings-producing activities associated with a particular receipt are performed based on costs of performance. At best, in the Taxpayers' particular situation, calculation of receipts to be included in the numerators of their gross receipts apportionment factors would be extremely complex using the [cost of performance] method that the Taxpayers propose.

Considering the statutes and rules applicable to the Commissioner's authority to impose a variance, I am convinced the Commissioner's preference for a "straightforward" method over a "not-so-straightforward" method is not a valid reason for imposing a variance.

Another reason the Commissioner provides for imposing the variance appears to be a reduction of gross receipts applicable to Tennessee. For example, the Commissioner stated that use of the cost of performance methodology would result in a substantial reduction in

the gross receipts that each Taxpayer would include in the receipts factor of its apportionment formula for each tax period, and, as a result, there would be substantial reduction in each Taxpayer's franchise/excise tax liability.

The Commissioner justified the variance, in part, on what he perceived to be a flawed cost of performance methodology mandated by the General Assembly, but again, that is a policy decision and such decisions are the prerogative of the General Assembly, not the Commissioner of Revenue or the courts. The Commissioner's criticism is apparent from the statement that "[c]osts associated with the performance of a particular earnings-producing activity that takes place across several states may, arguably, have been arbitrarily assigned by the Taxpayers to the various states in which the activity takes place" and when the Department attempts to verify whether a receipt has been correctly attributed to a particular state, "the Department may find itself largely dependent on the opinions and judgments of the Taxpayers, which may, arguably, be considered biased." Although the Commissioner's concern may be valid, the taxpayer's role in reporting the source of receipts is a direct result of the General Assembly's decision to employ the apportionment methodology; therefore, the Commissioner's concern of bias is no justification for deviating from a statutorily mandated apportionment methodology.

The parties cited numerous decisions to identify what they respectively believe is the intent of the General Assembly as it pertains to the use of the statutorily mandated "cost of performance methodology" for apportionment and the scope of the Commissioner's authority to change the methodology by which a taxpayer apportions its receipts. As noted earlier, the standard apportionment methodology - the "cost of performance methodology" - is expressly mandated in Tenn. Code Ann. §§ 67-4-2012(i) and 67-4-2111(i); the Commissioner's authority to impose a variance is specified in Tenn. Code Ann. §§ 67-4-2014 and 67-4-2112 and regulations including, specifically, Franchise & Excise Tax Rule 1320-6-1-.35(1)(a) & (c).

Having examined the numerous cases cited by the parties, I find three instructive: *Kellogg Co. v. Olsen*, 675 S.W.2d 707 (Tenn. 1984) ("*Kellogg*"); *American Tel. & Tel. Co. v. Huddleston*, 880 S.W.2d 682 (Tenn. Ct. App. 1994) ("*AT&T*"); and *Bellsouth Advertising & Publishing Corporation, v. Chumley*, 308 S.W.3d 350 (Tenn. Ct. App. 2009) ("*BAPCO*"). In two of the cases, *Kellogg* and *BAPCO*, the Commissioner imposed the variance against the wishes of the taxpayers, while in *AT&T* the taxpayers sought a variance which the Commissioner denied. I discuss the relevant aspects of each case below.

The issue in *Kellogg* was whether the taxpayer's claim of deductions for dividends received from foreign subsidiary corporations of which it owned more than 80% of each subsidiary created a "distortion" of its income which would justify the imposition of a

variance by the Commissioner. *Kellogg*, 675 S.W.2d at 708. The Kellogg Company deducted the full amount of those dividends in arriving at its "net earnings" for federal income tax purposes and for Tennessee excise tax purposes. *Id*. Under Tenn. Code Ann. § 67-2704 [now 67-4-2006(a)(1)] "net earnings" was defined as federal taxable income before the operating loss deduction and special deductions provided for in certain sections of the Internal Revenue Code, and subject to adjustments specified in the tax code and adjusted by subsections (b) and (c). Tenn. Code Ann. § 67-2704(b) [now § 67-4-2006(b)(2)] provided in pertinent part:

> There shall be subtracted from the federal taxable income:
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> (1) Dividends earned by a parent corporation from a subsidiary corporation where such parent owns eighty per cent (80%) or more of the stock of the subsidiary.

Kellogg, 675 S.W.2d at 708.

Tennessee's Commissioner of Revenue disagreed and imposed a variance for excise tax purposes that limited the deduction for "dividends received," which limitation increased Kellogg's franchise and excise taxes. *Id*. Taking exception with the variance, the Kellogg Company paid the additional excise taxes under protest and filed a claim for a refund.[2]

On appeal, this court noted that the *distortion* must be more than that which necessarily results from the application of a particular provision of the Internal Revenue Code before it can be corrected by the use of 26 U.S.C. § 482. The court observed that in the context of "nonrecognition" provisions, it has been stated that § 482

> "*cannot be allowed, in the absence of a taint, to change or modify (on the ground of income distortion) a transaction which Congress has seen fit to authorize specifically in spite of the fact that the transaction may well embody some sort of income distortion.* Having contemplated and authorized that possible distortion, Congress is not to be frustrated by use within the [Internal

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[2]The relevant facts were that the plaintiff, the Kellogg Company, a Delaware corporation, was subject to the Tennessee corporate excise tax because it was doing business in Tennessee. *Kellogg*, 675 S.W.2d at 708. During the fiscal years 1978-80, it received dividends from foreign subsidiary corporations and, in computing its tax for those years, it deducted the full amount of those dividends in arriving at its "net earnings." *Id.* The Commissioner assessed additional excise taxes because the plaintiff failed to reduce its dividends received deduction by the amount of expenses incurred in earning the dividends. Because no documentation of such expenses was provided, the Commissioner estimated the expenses allocable to earning the dividend income as 5% of the dividends received.

> Revenue] Service of the general provisions of Section 482." *See Ruddick Corp. v. United States*, 643 F.2d 747, 752 (1981). *See also General Electric Co. v. United States*, 3 Cl.Ct. 289 (1983).

Kellogg, 675 S.W.2d at 709 (emphasis added).

We also reasoned:

> Section 67-2723(c)(1) is properly invoked in the same circumstances as [26 U.S.C.] § 482, as described above. Those circumstances are not present in this case. The Commissioner points to the distortion which results when expenses incurred in earning non-taxable income are deductible as justification for her reduction of the dividends received deduction. *That distortion, if any, is not peculiar to the facts of this case. It will exist in every situation in which the deduction is available to a corporation, and therefore we believe the distortion was contemplated and authorized by the legislature. The Commissioner's authority under § 67-2723(c)(1) is not properly invoked to rewrite what she perceives to be an unwise provision in the statutory scheme.*

Id. (emphasis added).

Although shifting *income and/or deductions* among controlled corporations is not at issue here, the reasoning in *Kellogg* is instructive because it recognizes boundaries on the Commissioner's authority to impose a variance. More specifically, in spite of an "income distortion," the Commissioner cannot utilize the variance statute to change a transaction which the General Assembly has seen fit to authorize in the absence of specific grounds that justify the variance.

In *American Tel. & Tel. Co. v. Huddleston* ("*AT&T*"), the taxpayers sought a variance from the standard apportionment formula in Tenn. Code Ann. § 67-4-811 [now § 67-4-2012]. *AT&T*, 880 S.W.2d at 684-85. Although the issue in *AT&T* specifically pertained to whether the taxpayers must file as "a single, unitary, business enterprise," which is not at issue here, the discussion concerning the Commissioner's discretion to issue a variance was front and center.

The taxpayers claimed a refund of excise taxes based on the premise they were components of "a single, unitary, business enterprise," and sought permission to file on a combined basis under the provisions of Tenn. Code Ann. § 67-4-812(c) [now § 67-4-2014(c) with changes]. *Id*. at 685-86. The Commissioner denied the requested variance "because there was no evidence of evasion of taxes or shifting of income among the affiliated group

of corporations as required for combined reporting, pursuant to Tennessee Code Annotated § 67-4-812(c)."[3] *Id*. at 686. The trial court ruled in favor of the Commissioner holding that the taxpayers were not entitled to the requested variance and that each taxpayer had to file a separate excise tax return. *Id*. The taxpayers appealed.

On appeal, this court noted that when the Tennessee General Assembly adopted UDITPA in 1976, it delegated authority to the Commissioner of Revenue "to permit or require a variance from the standard apportionment formula when the formula does not 'fairly represent the extent of the taxpayer's business activity in this state.'" *Id*. at 691 (citing Tenn. Code Ann. § 67-4-812 [now § 67-4-2014]). This section, which has been referred to as a "relief provision," was adopted from Section 18 of the UDITPA, *id*., and it reads as follows:

> If the allocation and apportionment provisions of this part do not fairly represent the extent of the taxpayer's business activity in this state, the taxpayer may petition for or the commissioner may require, in respect to all or any part of the taxpayer's activity, if reasonable:
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> (1) Separate accounting;
> (2) The exclusion of any one (1) or more of the factors;
> (3) The inclusion of one (1) or more additional factors which will fairly represent the taxpayer's business activity in this state; or
> (4) The employment of any other method to effectuate an equitable allocation and apportionment of the taxpayer's earnings.

Id. (quoting Tenn. Code Ann. § 67-4-812(a) [now § 67-4-2014]).

Based on the above statute, the *AT&T* court reasoned that the Commissioner may exercise "reasonable discretion in determining whether facts or circumstances justify a departure from the statutory formula." *Id*. The court specifically stated that the burden, in that case, was upon the taxpayer who was seeking the variance "to establish that *its own unique facts and circumstances justify a departure from the standard apportionment formula*." *Id*. (citing *Peterson Mfg. Co. v. State*, 779 S.W.2d 784, 787 (Tenn.1989) (emphasis added)). The

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[3] When *AT&T* was decided, Tenn. Code Ann. § 67-4-812(c) stated:

> In order to prevent the evasion of taxes or to clearly reflect income under circumstances similar to those contemplated by [26 U.S.C.] § 482 of the Internal Revenue Code, the commissioner is given authority to: . . . (B) Require combined reports utilizing a common apportionment formula covering members of an affiliated group of corporations but only where [circumstances specified in the statute are established[.]

AT&T court also noted that the taxpayer seeking a variance must "provide clear and cogent evidence that the formula does not fairly represent its business activities in Tennessee." *Id*.

Significantly, the *AT&T* court also recognized that it was "*the intent of UDITPA that the standard formula be applied uniformly in all instances, except for those situations provided for in the relief provisions of section 18 of the Uniform Act* [codified at Tenn. Code Ann. § 67-4-812]." *Id.* (citing *Donald M. Drake Co. v. Department of Revenue*, 500 P.2d 1041, 1043-44 (Or. 1972)) (emphasis added).

The court also surveyed numerous decisions from other jurisdictions that had adopted UDITPA and made the following observations:

> *The standard statutory apportionment formula is presumed to be correct*, and the party seeking to employ an alternate method has the burden of showing that the statutory method is inappropriate. *Donald M. Drake Co.*, 500 P.2d at 1043-44; *Donovan*, 337 N.W.2d at 300. *The variance provision applies only in unusual and limited circumstances and is to be interpreted narrowly in order to carry out the purpose of uniform apportionment under the act*. *Donald M. Drake Co.*, 500 P.2d at 1044. *The burden is on the party seeking a variance to establish that the formula does not fairly represent its business activities in the taxing state*. *Donald M. Drake Co.*, 500 P.2d at 1041; *Deseret Pharm. Co. v. State Tax Comm'n*., 579 P.2d 1322, 1326-27 (Utah 1978). . . .
> . . . .
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> Other states which have adopted the UDITPA have concluded that the relief provision is intended to provide relief in exceptional circumstances which produced unconstitutional apportionment. With respect to the circumstances justifying use of the relief provision, the Florida Supreme Court held in *Roger Dean Enter.*, 387 So.2d 358: "The relief provision should be used when the statute reaches arbitrary or unreasonable results so that its application could be attacked successfully on constitutional grounds." *Id.* at 363.
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> *Decisions regarding relief provisions have indicated that the purpose of such provisions was to assure that the apportionment of interstate source income provides a division which satisfies the requirements of fair apportionment under the Federal Constitution*. *See American Bemberg Corp. v. Carson*, 188 Tenn. 263, 219 S.W.2d 169, (1949); *Dickey Clay Mfg. Co. v. Dickinson*, 200 Tenn. 25, 289 S.W.2d 533 (1956), which construed the relief provision in the apportionment provisions of the Tennessee excise tax law in effect prior to 1976. *The weight of authority indicates that this is the intended purpose of*

section 18 of UDITPA, and the standards regarding fair apportionment are applicable in determining whether the apportionment formula "fairly represents the taxpayer's activity" in Tennessee under Tennessee Code Annotated § 67-4-812(a).

AT&T, 880 S.W.2d at 691-92 (emphasis added).

The above survey reveals that in most cases it is the taxpayer that is seeking a variance that "fairly represents the taxpayer's activity" in a given state. It also reveals a circumstance I believe is significant, that in many circumstances the basis of the claim for relief, a variance, is on constitutional grounds, meaning the taxpayer claims it is entitled to relief because the standard tax methodology or a statute violates constitutional constraints. Here, the Commissioner seeks to impose the variance, not on constitutional grounds, but merely because the standard apportionment methodology does not fairly represent Plaintiffs' activities in Tennessee due, in part, to the fact other taxing authorities, states, are not capturing the taxpayer's income for services rendered to customers with Tennessee billing addresses. The survey also reveals that "the standard statutory apportionment formula is presumed to be correct," there is a "strong presumption in favor of the normal apportionment formula and against the applicability of the relief provision," "the party seeking to employ an alternate method has the burden of showing that the statutory method is inappropriate," the "variance provision applies only in unusual and limited circumstances and is to be interpreted narrowly in order to carry out the purpose of uniform apportionment under the act," and the burden of proof "is on the party seeking a variance." *Id*.[4]

As for the issue of fairness in the case at bar, it may be "more fair" to the people of Tennessee to require the inclusion of all of Plaintiffs' business activity (receipts) from customers with Tennessee billing addresses because doing so would increase Tennessee's tax revenue. The Commissioner, however, may not ignore the statutorily-mandated cost of performance apportionment methodology without proof that "peculiar or unusual circumstances" particular to Plaintiffs were not contemplated by Tennessee's franchise and excise statutory scheme. As noted earlier, Rule 1320-6-1-.35(1)(a)(4) authorizes the Commissioner to employ another method to effectuate an equitable allocation and apportionment; however, Tenn. Code Ann. §§ 67-1-911 and 67-4-812 permit a departure from the apportionment provisions only in limited and specific cases. *See* Tenn. Comp. R. & Reg. 1320-6-1-.35(1)(a)(4) (stating Tenn. Code Ann. "§§ 67-1-911 and 67-4-812 *may be invoked only in specific cases where unusual fact situations (which ordinarily will be unique*

[4] After a review of the statutory factors, the *AT&T* court concluded that the plaintiffs failed to meet the burden required to justify a variance, a departure from the normal statutory apportionment formula. Thus, the trial court's ruling in favor of the Commissioner was affirmed. *Id*. at 693.

and nonrecurring) produce incongruous results under the apportionment and allocation provisions contained in the Franchise and Excise Tax Laws." (emphasis added)).

In *Bellsouth Advertising & Publishing Corporation v. Chumley* ("*BAPCO*"), a case that both parties assert supports their respective but contradictory positions, the taxpayer was a multi-state taxpayer that challenged a variance the Commissioner issued that altered the taxing formula which increased the revenue assessed. The genesis of the dispute arose following an audit by the Tennessee Department of Revenue, when the taxpayer received a Notice of Assessment for franchise and excise taxes for the years 1997 through 2001. *BAPCO*, 308 S.W.3d at 355. The assessment, which was based upon a variance issued by the Commissioner, caused a tax liability of $13 million. The variance imposed by the Commissioner required the taxpayer to report its receipts as if they were derived from "advertising" pursuant to Tenn. Code Ann. § 67-4-2012(h), which is applicable to the sale of tangible property. *Id.* at 361.

The taxpayer challenged the Notice of Assessment contending it correctly calculated its tax liability by utilizing the cost of performance methodology prescribed by Tenn. Code Ann. § 67-4-2012(i) and the applicable rules and regulations. *Id*. at 355. In its complaint, the taxpayer stated it was engaged in "the business of compiling and publishing telephone directories pursuant to contracts with regulated and other telecommunications providers including BellSouth Telecommunications, Inc., which is an affiliated corporation that provides telecommunications services in Tennessee and eight other Southern States."[5] *Id.* The taxpayer stated that "its revenues were predominately derived from providing advertising services for the directories it published and that these advertising services were associated with various functions that were all performed outside the state of Tennessee." *Id*.

The Commissioner asserted that the statutory formula did not fairly represent the extent of the taxpayer's activities in Tennessee and that she acted within her statutorily granted discretion to apply a variance. *Id*. Significantly, the Commissioner specifically contended the taxpayer's *costs of performance* associated with its advertising was not outside of Tennessee, as the taxpayer contended. *Id*. at 356. Further, the Commissioner asserted that the taxpayer earned its Tennessee advertising revenues through its distribution of directories

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[5]The taxpayer further asserted that L.M. Berry, an affiliated corporation that functioned as an independent contractor, solicited advertising sales for the directories published by the taxpayer for distribution in Tennessee and other states. Based upon this and other facts, the taxpayer insisted that L.M. Berry was subject to Tennessee excise and franchise taxes "on its own net earnings derived from its activities performed on behalf of the taxpayer in Tennessee." *BAPCO*, 308 S.W.3d at 361. The taxpayer further stated that it engaged another affiliated corporation, Stevens Graphics, Inc., as an independent contractor, which prints all of the directories outside of Tennessee. It also stated the directories were then distributed within Tennessee by yet another independent contractor.

in Tennessee; thus, the receipts from its advertising should be placed in the numerator of the sales factor. *Id*. Alternatively she contended the taxpayer's computation of its apportionment formula under Tenn. Code Ann. § 67-4-2012(i)(2) did not fairly reflect its business activity in Tennessee; therefore, it was appropriate to impose a variance of the standard apportionment formula. *Id*.

After acknowledging the material facts were not disputed and that there were no Tennessee cases that had considered "the issuance of a variance from the cost of performance formula in connection with the sale of advertising," the *BAPCO* court focused on the specific concerns of the authors of UDITPA regarding the application of the cost of performance formula in the arena of income from *advertising in publications*." *Id*. at 365 (emphasis added).

> While the Commissioner acknowledges that the UDITPA as originally developed by the Multistate Tax Commission and as adopted in Tennessee, uses formulas designed to apply to all businesses, it points out that the authors of the uniform act recognized that those formulas did not function very well for certain types of businesses, and provided for variances in Section 18 of the uniform act, which is codified as Tenn. Code Ann. §§ 67-4-2014(a) and 67-4-2112(a). Specifically, the authors of the uniform act recognized that Section 17, which is the counterpart of Tenn. Code Ann. § 67-4-2012(i)(2) and at issue here, did not always adequately deal with all of the types of receipts of sales from other than tangible property. The Commissioner cites to Professor William J. Pierce, the "father" of UDITPA, who noted the deficiency in this area and the need for a variance under Section 18 to deal with certain situations not covered by Section 17 (Tenn. Code Ann. § 67-4-2012(i)(2)) as follows:
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>> Another problem arises in conjunction with sales other than sales of tangible personal property. Section 17 of the uniform act attributes these sales to the state in which the income-producing activity is performed. If the activity is performed in more than one state, the sales are attributed to the state in which the greater proportion of the activity was performed, based upon costs of performance. In many types of service functions, this approach appears adequate. However, there are many unusual fact situations connected with this type of income and probably the general provisions of Section 18 should be utilized for these cases. If we assume that the activity involved is the servicing of industrial equipment, the formula provided in the uniform act

> could be easily applied and the result appears equitable. In contrast, assume that the sales item involved is advertising revenue received by a national magazine publisher. The state of activity would be difficult, if not impossible, to ascertain, so it would appear that this type of income may well be apportioned on the same basis as subscription income. The national conference considered this problem at length and concluded that for certain types of sales income, exceptions would have to be established by the tax collection agencies, since no formula seemed to be satisfactory for every conceivable factual situation. Generally, it was felt that the provisions of Section 17 were the best that could be designed to cover the greater proportion of cases.
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> William J. Pierce, *The Uniform Division of Income for State Tax Purposes*, 35 Taxes 474, 780-781 (1957) (emphasis in original).

BAPCO, 308 S.W.3d at 365-66.

In *BAPCO*, the Commissioner insisted that Professor Pierce's analysis was on point and that the sales from advertising in the directories distributed in Tennessee "should be apportioned according to a circulation or distribution method." *Id*. at 366. In reaching the conclusion that the Commissioner did not abuse her discretion, the court reasoned:

> The unusual fact situation in this case is that all of the costs of production occurred outside of Tennessee, *but the revenue derived from the end product only occurred when the product was distributed in Tennessee which only then obligated the purchasers to pay the revenue proceeds to the producer for the sale of the advertising*. Certainly, *the circumstances of this case have a unique quality*, and while the process can be recurring, the "ordinarily" qualifier under the rule does not proscribe the issuance of a variance in all such cases.
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> In *American Tel. & Tel. Co. v. Huddleston*, 880 S.W.2d 682, 691-692 (Tenn. Ct. App. 1994), the Court said at page 691: "The Commissioner may therefore exercise reasonable discretion in determining whether facts or circumstances justify departure from the statutory formula." We hold that the Commissioner carried the burden of proof that the facts and circumstances of this case enabled her to exercise her reasonable discretion in declaring a variance for the

purpose of revising this formula to establish the basis for the revenue assessed.
We reverse the ruling of the Chancellor on this issue.

Id. at 367 (emphasis added).

I find the fact of the case at bar distinguishable from *BAPCO* because in *BAPCO* "the revenue derived from the end product only occurred *when the product was distributed in Tennessee which only then obligated the purchasers to pay the revenue proceeds to the producer for the sale of the advertising*." *Id*. Here, the revenue derived from providing wireless communication and data services had little if any bearing to the borders of Tennessee; this is because wireless communication and data services have no borders. Although the wireless customer may have a Tennessee billing address, the wireless communication and data service may be utilized from anywhere in the United States. Unlike *BAPCO*, Plaintiffs' receipts were earned without regard to where the wireless phones and/or data devices were used by the customers.

"It is axiomatic that a purpose in enacting uniform laws is to achieve conformity, not uniqueness." *Holiday Inns, Inc. v. Olsen*, 692 S.W.2d 850, 853 (Tenn. 1985). UDITPA is a uniform law and it is readily apparent from the Commissioner's variance letter that he did not favor the result that flowed from applying the statutorily-mandated cost of performance methodology; admittedly, neither do I. Nevertheless, neither the Commissioner nor the courts may refuse to apply the statutorily-mandated methodology when there are no unusual or unique facts or circumstances, which will be unique and nonrecurring, that would authorize the imposition of a variance. *See* Tenn. Comp. R. & Reg. 1320-6-1-.35(1)(a)(4). To allow the imposition of a variance to capture taxes that are "fair" to Tennessee in the absence of unusual and unique facts or circumstances peculiar to these taxpayers would result in an administrative or judicial amendment to the Franchise and Excise Tax Acts of Tennessee, which is not permitted. *See American Bemberg Corp. v. Carson*, 219 S.W.2d 169, 175 (Tenn. 1949); *see also Kellogg*, 675, S.W.2d at 709 (stating the Commissioner's authority does not allow him to "rewrite what she perceives to be an unwise provision in the statutory scheme.").

As Plaintiffs assert, "the 'fair representation' of business activities identified as a touchstone in the variance statutes cannot be judged in a vacuum based on the Commissioner's subjective idea of what is 'fair.'" Indeed, the Commissioner may not issue a variance simply because he believes the cost of performance methodology does not fairly represent the extent of business activities conducted in Tennessee. *See Kellogg*, 675 S.W.2d at 709. Further, as *Kellogg* additionally instructs, the Commissioner may not impose a variance unless the alleged distortion of tax is peculiar to a specific taxpayer and, if the alleged distortion in taxable income will exist in every situation in which the allocation of

income is available to an industry, the courts must assume the alleged distortion "was contemplated and authorized by the legislature." *Kellogg*, 675 S.W.2d at 709.

In the absence of facts sufficient to justify a deviation from UDITPA, a uniform law adopted by the Tennessee General Assembly, the Commissioner would be acting in excess of his statutory authority to impose a variance, and I am of the opinion the Commissioner failed to identify facts, and this record does not reveal facts, sufficient to invoke his authority under the variance statute. The invocation of the statutory authority to impose a variance is a condition precedent to the Commissioner having any discretion to issue a variance, a method to effectuate an equitable apportionment of Plaintiffs' net worth and net earnings for purposes of computing franchise and excise taxes as stated in Tenn. Comp. R. & Reg. 1320-6-1-.35(1)(a)(4).

For the foregoing reasons, the facts of this case are insufficient to invoke the Commissioner's limited authority under Tenn. Code Ann. § 67-4-2014(a); accordingly, I submit the Commissioner's issuance of a variance in this matter exceeded his statutory authority.

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FRANK G. CLEMENT, JR., JUDGE