



**Insight Paper # 08:**

**Tennessee Family-Owned Non-Corporate Entity Exemption Changes**

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Tennessee recently enacted some changes to its legislation that may impact your business. There are multiple changes in this legislation, but the change with the largest potential impact relates to franchise and excise tax exemptions. For the last several years, Tennessee has had an exemption to its Franchise and Excise tax called the Family-Owned Non-Corporate Entity (“FONCE”) exemption. Under this exemption if your entity was not a corporation, was at least 95% owned by family members, and had at least 66.67% of its gross receipts originating from “passive investment income,” then your entity could claim an exemption to Tennessee’s Franchise and Excise taxes. In the past, passive investment income has included all rental income for purposes of this gross receipts test.

The recently passed legislation revised the qualifying criteria for this FONCE exemption, and the following are some of the key points.

- Any rental income received from commercial property after June 30, 2009 will no longer qualify as passive investment income for purposes of the gross receipts test.
- Properties leased for residential purposes that include not more than 4 residential units will be considered residential (in other words, duplexes and quadplexes still qualify as residential property). Therefore, rental income from these units will still qualify as passive investment income for purposes of the FONCE exemption gross receipts test.
- Rental income from residential property or farm property is considered passive investment income for purposes of the FONCE exemption gross receipts test.
- For purposes of the family ownership test, ownership units held in trust will not be treated as family ownership unless the units are property of an estate or trust of a deceased individual who was a family member while living.

We wanted to inform you of these changes and also remind you that we are here to work with you on strategies related to managing the effects of these tax changes on your business. If you have any questions about this new legislation and its impact to you, please contact Caren Creason, CPA, CVA in our office at (901) 761-3003, and she will be happy to assist you in any way regarding questions or concerns you may have and the options available to you.

**The Marston Group, PLC**